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A study on impact of GST implementation on functioning of Indian Economy

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ABSTRACT

GST can be termed as the game changer as it is the biggest tax reform in India founded on the notion of "one nation, one market, one tax" has finally come to the implementation. The moment that the Indian government was waiting for a decade has finally come to its existence. The single biggest indirect tax regime has kicked into force, dismantling all the inter-state barriers with respect to trade. The GST rollout, with a single stroke, has converted India into a unified market of 1.3 billion citizens. The expectations from the implementation of GST tax reform will boost the Indian economy and huge shift will be seen from unorganized to organized sector. This paper makes an attempt in understanding the impact of GST implementation on functioning of Indian Economy and its implications on select sectors of India.

Key Words: GST, VAT, CENVAT, Services Tax, Impact of GST on Indian Economy

1.INTRODUCTION

Goods and Services Tax (GST) is an indirect tax which was introduced in India on 1 July 2017 and was applicable throughout India which replaced multiple cascading taxes levied by the central and state governments. Goods and Service Tax is applied on services and goods at a national level with a purpose of achieving overall economic growth. Currently, Indian consumers have to pay indirect tax on goods and services such as Value Added Tax, Service Tax, Excise Duty, Customs Duty, etc. Under the current system, each State has a right to levy their own tax on the goods coming into their dominion for sale and consumption, while the Centre levies taxes on manufacture of the goods. All these direct taxes levied on the traders are passed down to the consumer.

The Constitution (One Hundred and Twenty-second Amendment) Bill, 2014 was introduced in the Lok Sabha by Finance Minister Arun Jaitley on 19 December 2014 and bill was passed by the House on 6 May 2015,[1] receiving 352 votes for and 37 against. The GST is governed by a GST Council and its Chairman is the Finance Minister of India. Under GST, goods and services are taxed at the following rates, 0%, 5%, 12%, 18% and 28%.[2] There is a special rate of 0.25% on rough precious and semi-precious stones and 3% on gold. In addition a cess of 15% or other rates on top of 28% GST applies on few items like aerated drinks, luxury cars and tobacco products.[3] GST has been commonly accepted around the world and more than 140 countries have acknowledged the same which ranges between 15%- 20% in most of the countries.

The idea behind implementing GST across the country in 29 states and 7 Union Territories is that it would offer a win-win situation for everyone. Manufacturers and traders would benefit from fewer tax filings, transparent rules, and easy bookkeeping; consumers would be paying less for the goods and services, and the government would generate more revenues as revenue leaks would be plugged.

Objectives of the study

- To study the impact of GST on functioning of Indian Economy
- To study the implications of GST on select sectors of Indian Economy

2.Research methodology

The research paper is an attempt of exploratory research, based on the secondary data sourced from journals, Internet, articles, previous research paper. Looking into requirements of the objectives of the study the research design employed for the study is of descriptive type. Keeping in view of the set objectives, this research design was adopted to have greater accuracy and in depth analysis of the research study. Available secondary data was extensively used for the study.

3.Literature review

Dr. R. Vasanthagopal, (2011) Studied "GST in India: A Big Leap in the Indirect Taxation System", and found that the positive impacts are dependent on a neutral and rational design of the GST, balancing the conflicting interests of various stakeholders.

Anushuya and Narwal (2014) studied, "Application of CGE Modals In GST" and concluded that both GST & CGE are very popular all over the world but GST is a powerful concept in the field of indirect taxes.

Merin Jose (2015) Assistant professor, P G Dept. of Commerce, Pavanatma College highlighted in study "Goods and Services Tax (GST) features" Implementation of a comprehensive GST across goods and services is expected to increase India's GDP somewhere within a range of 0.9 percent to 1.7 percent. It will also boost export potential and will create more employment opportunities. It will be profitable for both Central and State governments.

Siddharth Shah, MBA (Mumbai University) and CFA Level II (CFA Institute) in the study "The Impact of Goods & Service Tax on Indian Economy" highlighted that The GST Bill is undoubtedly the biggest tax reform tabled by the Government in the post-liberalization age. The positive impact of GST on GDP growth due higher productivity, efficiency and ease of doing business will be seen over a period of time. But in the short and medium term, a disproportionate GST rate implemented to keep the States happy rate may hurt consumption, earnings, GDP growth rate, investor sentiment and the ruling party itself.

Alisha Gupta & Minaxi Rani (2016), Assistant Professor (Extn.), Department of Commerce, Government Girls College, Hisar (Haryana), in the study "Basic concepts and features of good and service tax in India" highlighted that GST is a single national uniform tax levied across India on all goods and services. Study also highlights that introduction of the Goods and Services Tax will be a significant step towards a comprehensive indirect tax reform in the country. It is also expected to bring about efficiency and transparency in the indirect tax mechanism in India. Further it will also encourage an unbiased tax structure that is neutral to business processes and geographical locations.

How GST Works:

GST proposes to abolish the varying levels of taxation between States, and consider the country as a single whole organism when it comes to taxes on goods and services instead of as a segmented creature. All the sundry taxes will be clubbed into just 2 levels – Central GST and State GST. What a trader will essentially be able to do is claim a refund on the taxes already paid at different stages of value addition. The consumer who buys the product will have to pay only the GST charged by the last dealer in the supply chain, as everyone else would have the opportunity to set-off the taxes paid at the previous stages. GST will also prevent the multiple taxation occurring on certain goods and thereby ensures transparency with regards to the rate of taxation and the total amount that goes to the government as taxes on a product. When introduced, GST will not only make the tax system simpler, but will also help in increased compliance, boost tax revenues, reduce the tax outflow in the hands of the consumers and make exports competitive.

Impact of GST on Indian Economy:

Removal of tax barriers on introduction of uniform GST across the country with seamless credit will make India a common market leading to economy of scale in production and efficiency in supply chain. It will expand trade and commerce. GST will have favourable impact on organized logistic industry and modernized warehousing.

GST will remove cascading effect of taxes imbedded in cost of production of goods and services and will provide seamless credit throughout value chain. This will significantly reduce cost of indigenous goods and will promote 'Make in India'. The sectors which have long value chain from basic goods to final consumption stage with operation spread in multiple states such as FMCG, pharma, consumer durables, automobiles and engineering goods will be the major beneficiaries of GST.

Tax policies play an important role on the economy through their impact on both efficiency & equity and its high time India braced itself for a relook at the current status. Historically, India has relied too much on indirect taxation because of political compulsions, an agrarian economy, low income levels and lack of infrastructure to track personal income. In order to simplify and rationalize indirect tax structures, government of India attempted various tax policy reforms at different points of time. While VAT was a welcome change during 2005, over the years, people have identified shortcomings in the structure while levying VAT both at Central level and State level. Also, CENVAT has the limitation of non-inclusion of several taxes such as VAT, ACD, surcharge etc. In the present state-level VAT scheme, there is a cascading effect on account of CENVAT element. Lastly, there is lack of integration of VAT on goods with tax on services at the state level and hence the cascading effect of service tax. To address such issues, a comprehensive tax reform (GST is a part) having an extensive base to kick-start the applicability of an efficient and harmonized consumption tax system has been proposed.

Uniform tax regime: With only one or two tax rates across the supply chain as against multiple tax structure at present, state specific advantages/disadvantages are gone. This provides a fair play ground for all stakeholders and focus can be brought in to efficiency rather than vantage points.

Greater tax revenues: A simpler tax structure can bring about greater compliance, thus increasing the number of tax payers and in turn tax revenues for the government. By removing cascading effect, layers of taxes and simplifying structures, the GST would encourage compliance, which is also expected to widen the tax base.

Competitive pricing: A cursory look at the retail price of any product manufactured in India reveals that the total tax component is roughly 25-30% of the cost of the product. GST will effectively mean that the tax paid by the final consumer will come down in most cases and will help in boosting consumption, which is again beneficial to companies.

Push to exports: With a fall in production cost in domestic market, the competitiveness of Indian goods in international market will increase. This bodes well for exporters, who compete with global manufacturers which operate on very different cost structures.

Shaking up corporate operations: The new tax regime will force many companies to restructure their operations. Companies will now insist vendors and suppliers to furnish invoices as GST will make it impossible for firms to evade taxes. Big companies stand to benefit as they have a supply chain in order and can offset taxes paid on inputs whereas smaller firms may end up spending more as compliance cost will rise.

Lowering Inflation: Inflation would be reduced as the cascading (tax on tax) effect of taxes would be eliminated. Inflation will remain low as GST rates on essential goods such as food grain, household consumer items and essential services have been either exempt or kept lower. Most of the services are not accounted in the consumer price CPI inflation basket and hence the higher GST rates may not get reflected on the retail price movement as measured by the government data. There are services like health, education, miscellaneous segment, transportation are outside the ambit of GST hence, GST implementation on CPI impact will be minimal.

Impact of GST on Different sectors of the Economy:
GST will have varied implications on different sectors of the Economy. To highlight a few are

Real estate & infrastructure: The implementation of GST is theoretically expected to help the consumers and builders. However, there are some concerns too like Eligibility of credits and concessions still remain a cause of worry for the real estate sector. The Model GST Law restricts credit on goods and services acquired for construction of immoveable property (other than plant and machinery). This clause is interpretative which may lead to litigation and result in denial of credits in certain situations. It will benefit real estate sector by ensuring a uniform tax structure and improve tax compliance by developers and looks at bringing in greater transparency for the sector and may minimize unscrupulous transactions.

Media & entertainment: Since the levy of entertainment tax will remain the right of local bodies, chances are that under the GST regime, cinema tickets prices may come down. DTH and cable television services are expected to become cost effective under the GST regime but the quantum of DTH and cable bill will depend on the levy of entertainment tax.

Pharma Sector: GST is expected to benefit the pharma and healthcare industries. It will create a level playing field for generic drug makers, boost medical tourism and simplify the tax structure. The pharma sector is hoping for a tax respite as it will make affordable healthcare easier to access by all.

Telecommunications: In the telecom sector, prices are expected to come down after GST. Manufacturers will save on costs through efficient management of inventory and by consolidating their warehouses. Handset manufacturers will find it easier to sell their equipment as GST will negate the need to set up state-specific entities, and transfer stocks thereby will also save up on logistics costs.

Textile Industry: The Indian textile industry provides employment to a large number of skilled and unskilled workers in the country. It contributes about 10% of the total annual export, and this value is likely to increase under GST. GST would affect the cotton value chain of the textile industry which is chosen by most small medium enterprises as it currently attracts zero central excise duty.

Agriculture Sector: Agricultural sector is the largest contributing sector the overall Indian GDP. It covers around 16% of Indian GDP. One of the major issues faced by the agricultural sector is transportation of agri products across state lines all over India. It is highly probable that GST will resolve the issue of transportation and may provide India with its first National Market for the agricultural goods.

FMCG: The FMCG sector could see significant savings in logistics and distribution costs as the GST will eliminate the need for multiple sales depots. The GST rate for this sector is expected to be around 17% which is way lesser than the 24-25% tax rate paid currently by FMCG companies. This includes excise duty, VAT and entry tax – all of which will be subsumed by GST.

Automobile Sector: Under the current tax system, there are several taxes applicable on this sector like excise, VAT, sales tax, road tax, motor vehicle tax, registration duty which will be subsumed by GST. Though there is still some ambiguity due to tax rates and incentives/exemptions provided by different states to the manufacturers/dealers for manufacturing car/bus/bike, the future of the industry looks rosy. Under GST Luxury cars may be cheaper by Rs 1 lakhs and SUV rates may also fall by 6-10%.

E-Commerce: The e-com sector in India has been growing by leaps and bounds. In many ways, GST will help the e-com sector’s continued growth but the long-term effects will be particularly interesting because the model GST law specifically proposes a tax collection at source (TCS) mechanism, which e-com companies are not too happy with. The current rate of TCS is at 1% and it’ll remain to be seen if it dilutes the rapid boom in this sector in any way in the future. The GST law will address the issues related to inter-state movement of goods by e-commerce players thereby helping the e-commerce players who are today subjected to entry taxes by destination states along with the requirement of statutory forms, way-bills, road-permits, local registration and other such requirements.

Oil & Gas: The Oil & Gas Industry would largely be negatively impacted by the introduction of GST; the reason being that 5 petroleum products (i.e. crude, natural gas, ATF, diesel and petrol) are excluded from the coverage of GST for the initial years while the remaining petroleum products (for e.g. kerosene, naphtha, LPG, etc) are covered within the coverage of GST. Also it would result in non-creditable tax costs for e.g. a refinery producing diesel & petrol will pay GST on the procurement of plant, machinery and services; which GST would not be creditable against the out excise duty & VAT which would be levied on petrol & diesel. The said tax costs would have an inflationary impact on the overall economy.

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These are the implications of GST on few select sectors impacting the functioning of the economy. A list of the products on which tax burden has gone up and reduced is also added with the changes.

Products on which tax burden comes down		
Product	**Current effective tax rate***	**GST rate (%)**
Mobile Phone	20.02	12
Footwear (below Rs. 500)	14.41	5
Ready-made garments	18.16	12
Cars for the handicapped	20-22	18
Medicines	11	5
Renewable energy devices	17-18	5
Iron ore	17-18	5
Music instruments (handmade)	0-12.5	0
Contact lenses	18	12
Processed food	14	12
Products on which tax burden goes up		
Product	**Curren t effective tax rate***	**GST rate (%)**
Butter	5.66	12
Television	24.39	28
Footwear (Above Rs. 500	14.41	18
Biscuits (Above Rs. 100/kg)	16-09	18
Cornflakes	9.86	18
Wristwatch	20.64	28
Jam	5.66	18
Baby food (sold in unit containers)	7.06	18
Small Cars (<4m<1200cc petrol)	25-27	28+ 1**
Small Cars (<4m<1500cc diesel)	25-27	28+ 3**

* Current effective tax rate includes central excise duty, VAT and various local levies
** GST compensation cess

Source: EY, GST Council

4.Conclusion

The introduction of the Goods and Services Tax will be a very noteworthy step in the field of indirect tax reforms in India. By merging a large number of Central and State taxes into a single tax, GST is expected to significantly ease double taxation and make taxation overall easy for the industries. For the end customer, the most beneficial will be in terms of reduction in the overall tax burden on goods and services. Introduction of GST will also make Indian products competitive in the domestic and international markets. A larger impact is expected on the administrative compliance cost of GST which is likely to increase tax revenue from the "parallel" or "black" economy. Last but not least, the GST, because of its transparent character, will be easier to administer and once implemented, the proposed taxation system holds great promise in terms of sustaining growth for the Indian economy.

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