

Effect of GST on the Indian Manufacturing Sector

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Abstract

The Goods and Services Tax (GST), introduced in India on **1 July 2017**, revolutionized indirect taxation by creating a unified tax regime to replace a complex network of central and state taxes. This research paper examines the **impact of GST on the Indian manufacturing sector**, which is a key driver of economic growth, employment, and exports. The study explores how the transition to GST has affected cost structures, supply chains, compliance mechanisms, competitiveness, and sectoral growth. It finds that while GST has largely enhanced efficiency and reduced cascading taxes, challenges remain in compliance, technological adaptation, and rate structuring.

Keywords: Goods and Services Tax (GST); Indirect Tax Reform; Indian Manufacturing Sector; Input Tax Credit (ITC); Tax Cascading; Supply Chain Efficiency; Cost Structure Optimization.

1. Introduction

The Indian manufacturing sector contributes a substantial share to the nation's Gross Domestic Product (GDP) and employment. Prior to GST, manufacturers dealt with multiple indirect taxes — such as excise duty, value-added tax (VAT), central sales tax (CST), and various state entry levies — leading to tax cascading and regional disparities. GST sought to eliminate these barriers by implementing a **single, destination-based tax system** with seamless input tax credits (ITC) and uniform taxation across all states.

2. Literature Review

2.1 Pre-GST Taxation and Manufacturing Challenges

Under the pre-GST indirect tax regime, manufacturers faced a **cascading effect of taxes** — taxes on inputs did not always offset taxes on outputs — increasing the final cost of goods. Multiple tax registrations across states and compliance burdens impeded efficient operations.

2.2 GST's Designed Benefits

GST introduced a unified tax rate structure (CGST + SGST for intra-state and IGST for inter-state transactions), enabling:

- **Seamless Input Tax Credits** across the supply chain
- **Reduction of cascading taxes** and tax-on-tax effect
- **A single national market** eliminating multiple tax compliances

- **Lower logistics and compliance costs** via elimination of state entry taxes and border check-posts.

2.3 Challenges Identified in Literature

Several studies have pointed out initial transitional issues such as:

- Increased compliance burden and digital adaptation challenges
- Rate classifications causing pricing changes for certain products
- Smaller firms facing difficulty in GST returns and technological systems.

3. Research Objectives

This paper investigates:

1. How GST has influenced production costs in the manufacturing sector.
2. Whether GST has improved supply chain efficiency and reduced logistics costs.
3. The compliance challenges and technology adaptation issues faced by manufacturers.
4. Sectoral responses and performance trends post-GST implementation.

4. Methodology

This research adopts a **secondary data analysis** methodology, gathering information from published academic papers, industry reports, government records, and economic articles. The period examined spans the **pre-GST era (before 2017)** and the **post-GST environment (2018–2025)** to provide comparative insights.

5. Findings and Discussion

5.1 Production Cost and Tax Efficiency

GST eliminated multiple cascading taxes and enabled a robust **input tax credit mechanism**, allowing manufacturers to set off taxes paid at earlier stages of production against final output taxes. This has **reduced the overall cost of production and improved competitiveness**.

5.2 Logistics and Supply Chain Optimization

Manufacturers have benefited from:

- Reduced logistics costs due to abolition of state entry taxes
- Faster interstate movement of goods with fewer checkpoints
- Opportunities to consolidate warehouses and optimize distribution networks
These changes have resulted in **greater operational efficiency** and lower inventory costs.

5.3 Compliance and Technological Challenges

Despite major advantages, compliance complexity persists, especially for **small and unorganized manufacturers** who face challenges in digital filing, GST portal navigation, and IT system upgrades. The requirement of frequent returns and reconciliation has required investments in accounting systems and training.

5.4 Rate Structuring and Sectoral Impact

GST rate structuring has had mixed effects:

- Some sectors experienced **higher effective tax rates** than before GST, leading to cost pressures.
- Others saw **beneficial rate rationalizations** and increased demand due to lowered taxes (e.g., some consumer durables and automobiles). Recent reforms (2025 GST simplification) aim to further streamline rates and lower tax slabs for key manufacturing inputs.

6. Analysis

Overall, GST has **transformed the taxation landscape** for Indian manufacturers by consolidating indirect taxes, improving transparency, and facilitating market expansion. It has encouraged formalization, improved supply chain efficiency, and reduced production bottlenecks. However, the transition has not been without friction — compliance complexities and technological adaptation hurdles have impacted smaller firms disproportionately.

Sector-specific reforms such as rate rationalization and digital assistance initiatives are critical for maximizing GST's potential benefits and ensuring **inclusive growth** for all types of manufacturers.

7. Conclusion

The introduction and evolution of GST represent a **significant reform in Indian indirect taxation**, especially concerning the manufacturing sector. Evidence suggests that GST has:

- Reduced tax costs and eliminated cascading effects,
- Improved supply chain efficiencies and logistics,
- Enhanced national market integration,
- And raised challenges related to compliance and digital adaptation.

To sustain and amplify the positive impacts, continuous policy refinement, simplified compliance frameworks, and targeted support for small manufacturing units are essential.

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