

**WAINGANGA COLLEGE OF
ENGINEERING AND MANAGEMENT**

RESEARCH PAPER

ON

**IMPACT OF GST ON THE FINANCIAL
PERFORMANCE OF SMALL
BUSINESSES IN INDIA**

Submitted By

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DECLARATION

I, **Poorva Vasant Ghormare**, hereby declare that the research paper entitled “**Impact of GST on the Financial Performance of Small Businesses in India**” is prepared by me as part of my academic work for the MBA programme at **Wainganga College of Engineering and Management**.

The information presented in this research paper has been collected from relevant secondary sources and academic literature. I have made sincere efforts to present the information accurately and objectively.

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1. ABSTRACT

The Goods and Services Tax (GST) was introduced in India on **1 July 2017** as a major reform of the indirect taxation system. It replaced several central and state-level indirect taxes and aimed to create a more integrated, transparent and technology-driven tax structure.

Small businesses play an important role in the Indian economy by generating employment, supporting local supply chains and contributing to economic development. However, small businesses generally operate with limited financial and administrative resources. Therefore, the implementation of GST has had significant implications for their financial performance.

This research paper examines the impact of GST on the financial performance of small businesses in India. The study focuses on profitability, revenue, working capital, cash flow, compliance costs, input tax credit, accounting practices, digitalisation and business growth.

The study is primarily based on secondary data and published research literature. The review indicates that GST has generated several benefits, including improved transparency, digital accounting, better documentation, reduction in cascading taxation and greater integration of markets. At the same time, small businesses have faced challenges related to compliance costs, digital systems, professional accounting expenses and working-capital management.

The overall conclusion of the study is that GST has had a **mixed impact in the short term but increasingly positive effects in the long term** for businesses that have successfully adapted to the digital compliance environment.

Keywords: GST, Small Businesses, MSMEs, Financial Performance, Profitability, Working Capital, Cash Flow, Input Tax Credit, Compliance Cost.

2. INTRODUCTION

Small businesses are an important part of the Indian business environment. They operate across various sectors such as manufacturing, retail, wholesale, services, food processing, transportation and trading.

These businesses provide employment opportunities and contribute significantly to local and national economic activity. However, small businesses often face financial constraints and have limited administrative resources.

The introduction of GST created a significant change in the manner in which businesses manage indirect taxation. The GST system introduced a common framework for taxation of goods and services and significantly increased the importance of digital accounting and documentation.

For small businesses, GST has both opportunities and challenges. The input tax credit mechanism can reduce cascading taxation and improve cost efficiency. At the same time, registration, invoicing, return filing, reconciliation and record maintenance can increase administrative costs.

Financial performance includes profitability, revenue growth, liquidity, cash flow, working-capital efficiency and overall financial sustainability. Therefore, the impact of GST should be examined from multiple financial dimensions rather than simply looking at the tax paid by businesses.

This research paper attempts to understand the overall impact of GST on small businesses and identify the major factors that influence their financial performance.

3. BACKGROUND OF GST IN INDIA

Before GST, India had multiple indirect taxes imposed by central and state governments. These included VAT, Central Excise Duty and Service Tax, among others.

The existence of multiple indirect taxes created complexities in taxation and interstate business transactions.

GST was introduced to create a more unified indirect-tax system.

One of the important features of GST is the **Input Tax Credit (ITC)** mechanism. Eligible businesses can claim credit for GST paid on inputs against their output tax liability, subject to the applicable conditions.

GST has also increased the importance of electronic records, digital invoices and online tax compliance.

This transition has been beneficial for businesses that are technologically capable, but it has created adjustment difficulties for some small businesses.

4. SMALL BUSINESSES IN INDIA

Small businesses form an important part of India's entrepreneurial ecosystem.

Under the revised MSME classification applicable from **1 April 2025**, a small enterprise is classified based on investment in plant and machinery/equipment and annual turnover. The current threshold for a small enterprise is investment of up to **₹25 crore** and annual turnover of up to **₹100 crore**.

Small businesses can be found in almost every major sector of the Indian economy.

Some important characteristics of small businesses are:

- Limited working capital.
- Small administrative teams.
- Greater dependence on external accountants.
- Limited technological resources in some cases.
- High sensitivity to compliance costs.

- Dependence on timely customer payments.
- Limited ability to absorb sudden cost increases.

These characteristics make GST particularly important from a financial-management perspective.

5. STATEMENT OF THE PROBLEM

GST was introduced with the objective of simplifying indirect taxation and improving economic efficiency.

However, the transition required businesses to adopt digital systems and new compliance procedures.

For small businesses, additional expenses related to accounting software, professional services and employee training can affect profitability.

Similarly, the timing of tax payments and input-tax-credit utilisation can influence working capital and cash flow.

Therefore, the problem addressed by this research is:

“What has been the impact of GST on the financial performance of small businesses in India, particularly with respect to profitability, working capital, cash flow, compliance costs and business growth?”

6. OBJECTIVES OF THE STUDY

The objectives of the study are:

1. To examine the impact of GST on the financial performance of small businesses in India.
2. To analyse the effect of GST on profitability.
3. To study the impact of GST on revenue and business growth.
4. To examine the effect of GST on working capital.
5. To analyse the impact of GST on cash flow.
6. To identify GST-related compliance costs.

7. To study the role of input tax credit in business efficiency.
8. To examine the impact of GST on accounting and digitalisation.
9. To identify the major challenges faced by small businesses.
10. To provide suitable recommendations for improving GST compliance and financial management.

7. RESEARCH QUESTIONS

The study attempts to answer the following questions:

1. Does GST have a significant impact on the financial performance of small businesses?
2. Has GST affected the profitability of small businesses?
3. Has GST increased compliance costs?
4. How does GST affect working capital?
5. What is the impact of GST on cash flow?
6. Has GST encouraged digital accounting?
7. Has GST helped small businesses expand into interstate markets?
8. What are the major challenges faced by small businesses under GST?

8. HYPOTHESES

Hypothesis 1

H₀: GST has no significant impact on the financial performance of small businesses.

H₁: GST has a significant impact on the financial performance of small businesses.

Hypothesis 2

H₀: GST has no significant impact on the profitability of small businesses.

H₁: GST has a significant impact on the profitability of small businesses.

Hypothesis 3

H₀: GST has no significant impact on working-capital requirements.

H₁: GST has a significant impact on working-capital requirements.

Hypothesis 4

H₀: GST compliance costs have no significant relationship with financial performance.

H₁: GST compliance costs have a significant relationship with financial performance.

9. REVIEW OF LITERATURE

9.1 Bhalla, Sharma and Kaur (2023)

Bhalla, Sharma and Kaur studied the effect of GST on business performance among Indian MSMEs. Their research used data from **404 registered MSMEs**.

The study reported an overall positive relationship between GST-related factors and business performance. Technology transition, tax awareness and operational efficiency were important factors influencing the ease of doing business.

The research suggests that GST can contribute positively to business performance when enterprises are able to adapt to digital systems and understand tax requirements.

9.2 Kolte and Jagtap (2026)

Kolte and Jagtap examined the impact of GST on the financial management of MSMEs. Their study considered factors such as working capital, cash flow, compliance costs, profitability and accounting practices.

The study highlighted improvements in transparency and digital record keeping but also identified increased compliance burdens and operational costs.

9.3 Monisha and Ravichandran (2026)

A recent study examined GST compliance perception and SME profitability in India. The study found that compliance-cost burden can negatively affect profitability, whereas digital readiness can contribute positively to business performance.

This finding indicates that technological capability is an important factor in determining the financial impact of GST.

9.4 Mallidi (2025)

Mallidi examined GST implementation and its impact on small and medium enterprises. The research considered compliance burden, input tax credit, working capital, profitability and interstate business performance.

The findings indicate that GST can initially increase compliance costs while also creating benefits through improved input-tax-credit utilisation and reduced cascading taxation.

10. RESEARCH GAP

The existing literature shows that GST has both positive and negative effects on small businesses.

However, different businesses experience GST differently depending on:

- Size of business.
- Industry.
- Level of digitalisation.
- Tax awareness.
- Availability of professional support.
- Working-capital position.
- Geographic market.

There is therefore a need for a comprehensive study that examines GST from multiple financial perspectives.

This research addresses this gap by considering profitability, revenue, working capital, cash flow, compliance costs and digitalisation together.

11. RESEARCH METHODOLOGY

11.1 Research Design

The study follows a **descriptive and analytical research design**.

11.2 Data Collection

The research primarily uses secondary data obtained from:

- Government publications.
- Ministry of MSME resources.
- GST-related government information.
- Academic research papers.
- Journals.
- Published empirical studies.
- Institutional reports.

11.3 Variables

Independent Variable

GST implementation and compliance.

Dependent Variables

- Profitability.
- Revenue.
- Working capital.
- Cash flow.
- Compliance cost.
- Accounting efficiency.
- Business growth.

11.4 Research Approach

The study uses comparative analysis and qualitative synthesis of existing research.

No original primary survey results are claimed in this paper. The numerical findings mentioned from published studies belong to those respective studies.

12. IMPACT OF GST ON FINANCIAL PERFORMANCE

GST affects the financial performance of small businesses through multiple channels.

The major areas are:

- Profitability.
- Revenue.
- Working capital.
- Cash flow.
- Compliance cost.
- Accounting.
- Digitalisation.
- Market expansion.

The effect can be positive or negative depending on the business's ability to adapt.

13. IMPACT ON PROFITABILITY

Profitability is one of the most important measures of financial performance.

GST can improve profitability through the input-tax-credit mechanism and reduction in cascading taxation.

When eligible input tax credits are properly utilised, the effective tax burden on the value added by the business can be reduced.

However, GST compliance can also increase costs.

Businesses may have to spend money on:

- Accountants.
- GST consultants.
- Accounting software.
- Employee training.
- Internet and digital infrastructure.
- Record maintenance.

Therefore, the overall impact on profitability depends on the balance between tax efficiency and compliance expenditure.

14. IMPACT ON REVENUE AND BUSINESS GROWTH

GST has contributed to greater integration of India's domestic market.

Small businesses that maintain proper GST documentation may find it easier to deal with larger organisations and participate in formal supply chains.

GST can also facilitate interstate business transactions.

The ability to sell products and services to customers across different states can create opportunities for business expansion.

Therefore, GST may have an indirect positive impact on revenue growth.

15. IMPACT ON WORKING CAPITAL

Working capital refers to the funds required for the day-to-day operation of a business.

GST can influence working capital because businesses need to manage:

- Tax payments.
- Customer receivables.
- Supplier payments.
- Input tax credit.

- Inventory.
- Operating expenses.

For example, if a business has to pay its GST liability before collecting money from customers, it may experience temporary liquidity pressure.

On the other hand, effective input-tax-credit utilisation can reduce the net tax outflow.

Thus, GST's impact on working capital varies according to the business model and cash-flow cycle.

16. IMPACT ON CASH FLOW

Small businesses are generally more sensitive to cash-flow fluctuations because they have limited financial reserves.

GST can affect cash flow through the timing of:

- Sales.
- Customer payments.
- Purchases.
- Input tax credit.
- Tax payments.

Proper GST planning is therefore essential for small businesses.

Businesses should include expected GST liabilities in their monthly cash-flow forecasts.

17. IMPACT OF GST COMPLIANCE COST

Compliance cost is a major concern for small businesses.

GST compliance may require expenditure on:

- Tax professionals.
- Accounting software.
- Digital infrastructure.
- Employee training.
- Record keeping.
- Reconciliation.
- Return filing.

For large businesses, these costs may represent a relatively small proportion of total expenditure.

For very small businesses, however, compliance costs can have a noticeable effect on profitability.

Recent research has also identified compliance-cost burden as an important factor associated with SME profitability.

18. IMPACT ON ACCOUNTING AND DIGITALISATION

GST has encouraged businesses to adopt digital accounting practices.

Small businesses increasingly need to maintain proper records of:

- Purchases.
- Sales.
- Tax invoices.
- Input tax credit.
- Output tax.
- Tax payments.

Digital accounting can improve:

- Accuracy.
- Transparency.
- Financial reporting.
- Inventory management.
- Tax planning.

- Business decision-making.

Although digitalisation creates initial costs, it can improve efficiency in the long term.

19. IMPACT ON FORMALISATION

GST has contributed to the formalisation of business transactions.

Formalisation can provide benefits such as:

- Better financial records.
- Greater business credibility.
- Improved access to formal finance.
- Better relationships with organised buyers.
- Improved financial planning.

However, formalisation also increases the need for proper documentation and compliance.

20. IMPACT ON INTERSTATE BUSINESS

One important advantage of GST is the creation of a more integrated indirect-tax environment.

Small businesses can potentially reach customers beyond their home state.

This is particularly important for businesses involved in:

- E-commerce.
- Wholesale.
- Manufacturing.
- Distribution.
- Online services.

GST can therefore support expansion into wider markets.

21. MAJOR POSITIVE IMPACTS OF GST

The major positive impacts identified are:

- Reduction in cascading taxation.
- Better tax transparency.
- Improved documentation.
- Digitalisation of accounting.
- Better utilisation of input tax credit.
- Greater market integration.
- Easier interstate transactions.
- Formalisation of businesses.
- Improved financial records.
- Potential improvement in operational efficiency.

22. MAJOR NEGATIVE IMPACTS OF GST

The major challenges are:

- Increased compliance requirements.
- Additional accounting expenses.
- Digital infrastructure costs.
- Training requirements.
- Working-capital pressure.
- Increased administrative workload.
- Dependence on tax consultants.
- Difficulty understanding tax procedures.
- Cash-flow pressure due to timing differences.

23. COMPARATIVE ANALYSIS

Area	Positive Effect	Negative Effect
Profitability	Input tax credit and reduced cascading	Compliance expenses
Revenue	Wider market access	Pricing adjustments
Working Capital	ITC may reduce tax outflow	Liquidity pressure
Cash Flow	Better records	Timing of tax payment
Accounting	Digitalisation	Software cost
Compliance	Standardised system	Increased administrative work
Interstate Business	Better market integration	Additional compliance
Formalisation	Better credibility	More documentation

24. MAJOR FINDINGS

The major findings of the study are:

1. GST has a multidimensional impact on small-business financial performance.
2. GST can improve profitability through better input-tax-credit utilisation and reduction of cascading taxes.
3. Compliance costs can negatively affect the profitability of very small businesses.
4. GST has encouraged digital accounting and record keeping.
5. Working-capital effects depend on the timing of purchases, sales, customer payments and tax payments.
6. GST can create opportunities for interstate market expansion.
7. Businesses with stronger digital capabilities are generally better positioned to manage GST compliance.
8. GST has contributed to formalisation and improved transparency.
9. The initial transition to GST created significant adjustment challenges.
10. In the long term, businesses that adapt effectively can obtain greater benefits from the GST framework.

25. SUGGESTIONS AND RECOMMENDATIONS

25.1 Simplify GST Compliance

GST procedures for small businesses should remain simple, predictable and easy to understand.

25.2 Increase GST Awareness

Training programmes should be conducted to educate small-business owners about:

- Registration.
- Invoicing.
- Input tax credit.
- Returns.
- Payments.
- Record keeping.

25.3 Promote Affordable Accounting Software

Small businesses should be encouraged to use affordable digital accounting systems.

25.4 Improve Professional Support

Small businesses with limited accounting knowledge should have access to reliable professional guidance.

25.5 Improve Working-Capital Planning

Business owners should include GST payments in their regular cash-flow forecasts.

25.6 Improve Resolution of ITC Issues

Efficient resolution of input-tax-credit issues can help businesses manage liquidity more effectively.

26. CONCLUSION

GST has brought a significant transformation to India's indirect taxation system and has had a considerable effect on small businesses.

The impact of GST cannot be described as completely positive or negative. It depends on the size, sector, technology adoption, financial strength and tax awareness of the business.

In the short term, GST created challenges through increased compliance requirements, accounting costs and digital adaptation. These challenges were particularly significant for small enterprises with limited administrative resources.

In the long term, GST has created several opportunities. These include improved transparency, digitalisation, input-tax-credit utilisation, formalisation and better integration of the domestic market.

The evidence reviewed suggests that GST can contribute positively to business performance when businesses have sufficient digital capability and tax awareness. However, compliance costs remain an important concern.

Therefore, the overall conclusion is that **GST has had a mixed short-term impact and a generally more favourable long-term impact on small businesses**, provided that enterprises are able to adapt effectively to the digital tax environment.

Simplifying compliance, improving taxpayer education, reducing avoidable administrative costs and supporting digital adoption can further enhance the benefits of GST for small businesses.

27. LIMITATIONS OF THE STUDY

The study has the following limitations:

1. It is primarily based on secondary data.
2. No original primary survey has been conducted.
3. GST's impact differs across industries.
4. Different studies use different methodologies and samples.
5. Financial performance is also influenced by factors such as inflation, competition, interest rates and consumer demand.

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28. SCOPE FOR FUTURE RESEARCH

Future research can focus on:

- GST and profitability of retail businesses.
- GST and working capital of manufacturing SMEs.
- GST and e-commerce businesses.
- GST compliance among rural enterprises.
- GST and women-owned businesses.
- GST and access to bank finance.
- GST and formalisation.
- State-wise comparison of GST impact.
- Comparison between micro and small enterprises.
- Long-term impact of GST on business growth.

A primary survey of 100–500 small-business owners can also be conducted in future research to statistically test the hypotheses proposed in this paper.

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