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GST 2.0 & “Viksit Bharat”: The Role of Next-Generation GST Reforms in Supporting MSMEs and Achieving Inclusive Growth by 2047

*¹ Rahul Kumar

*¹ Assistant Professor, Department of Commerce, CPD Jain Girl's PG College, Tijara (Alwar), RRB Matsya University, Alwar, Rajasthan, India.

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Abstract

The introduction of “next-generation” Goods and Services Tax (GST) reforms in September 2025, popularly branded GST 2.0, represents the most significant recalibration of India’s indirect-tax architecture since the tax’s launch in July 2017. Announced by Prime Minister Narendra Modi in his Independence Day address of 15 August 2025 and operationalised through the recommendations of the 56th GST Council meeting, the reforms collapse the earlier four-tier rate structure into a simplified two-slab system of 5 per cent and 18 per cent, supplemented by a 40 per cent demerit rate on luxury and sin goods. This review paper examines the architecture of GST 2.0 and critically assesses its implications for India’s Micro, Small and Medium Enterprises (MSMEs)-a sector contributing roughly 30 per cent of national Gross Domestic Product, over 45 per cent of exports and employment for close to 28 crore persons. Drawing on official government data, industry surveys and contemporary policy analysis, the paper situates these reforms within the overarching national mission of Viksit Bharat @2047. It argues that rate rationalisation, inverted-duty correction, faster refunds and simplified registration collectively strengthen MSME liquidity, competitiveness and formalisation, thereby advancing inclusive growth. The paper also identifies persistent challenges and offers policy recommendations for the reform’s next phase.

*Corresponding Author

Rahul Kumar

Assistant Professor, Department of
Commerce, CPD Jain Girl's PG College,
Tijara (Alwar), RRB Matsya University,
Alwar, Rajasthan, India.

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1. Introduction

India’s Goods and Services Tax, launched on 1 July 2017, was hailed as the country’s most ambitious fiscal reform since independence-subsuming a fragmented web of central and state levies into a single national market. Yet, over its first eight years, the tax also attracted persistent criticism for its complexity. A multi-tier structure of nil, 5, 12, 18 and 28 per cent rates, layered with cesses on sin and luxury goods, generated frequent classification disputes, an inverted duty structure in several manufacturing segments, blocked input tax credits and heavy compliance costs that fell disproportionately on smaller enterprises^[1].

Against this backdrop, Prime Minister Narendra Modi used his Independence Day address of 15 August 2025 to announce a package of “next-generation” GST reforms, describing them as a “Diwali gift” that would lower the tax burden on the common citizen, farmers, MSMEs, women, youth and the middle class^[2]. The reforms were formally approved at the 56th meeting of the GST Council, chaired by Union Finance Minister Nirmala Sitharaman, and rolled out from 22

September 2025-the first day of Navratri^[3]. Widely referred to as GST 2.0, the package rests on three declared pillars: structural reforms, rate rationalisation and ease of living/ease of doing business^[1].

This paper reviews GST 2.0 through the specific lens of the MSME sector and the national vision of Viksit Bharat @2047-the goal of transforming India into a developed nation by the centenary of its independence. Because MSMEs form the backbone of India’s employment and export ecosystem, the manner in which tax reform reshapes their cost structures, cash flows and compliance experience has direct consequences for inclusive growth. The paper is organised as follows: Section 2 traces the rationale for reform; Section 3 details the architecture of GST 2.0; Section 4 profiles the MSME sector; Section 5 analyses the transmission channels through which the reforms affect MSMEs; Section 6 links these to Viksit Bharat 2047; Section 7 reviews early empirical evidence; and Section 8 discusses challenges and recommendations.

2. From GST 1.0 to GST 2.0: The Rationale for Reform

The original GST subsumed seventeen central and state taxes and thirteen cesses into one framework, creating “one nation, one tax.” Its success is visible in a widening tax base and buoyant revenues, with monthly gross collections routinely crossing ₹2 lakh crore by 2024–25. However, the reform remained incomplete in three respects that GST 2.0 seeks to address. First, rate complexity. The coexistence of four principal slabs invited disputes over whether a product belonged, for instance, in the 12 or the 18 per cent bracket. Second, the inverted duty structure—where inputs were taxed at higher rates than finished goods—trapped working capital in accumulated, hard-to-recover input tax credit (ITC), a distortion acutely felt in labour-intensive sectors such as textiles, footwear and fertilisers [4]. Third, the compliance burden of registration, multiple returns and slow refunds weighed heavily on micro and small firms with limited accounting resources. Reserve Bank of India expert assessments have long placed the MSME credit gap in the range of ₹20–30 lakh crore, a shortfall aggravated whenever liquidity is locked in delayed refunds [5].

GST 2.0 responds to each of these deficiencies through a deliberate simplification of rates, a correction of duty inversions and a suite of process reforms aimed squarely at reducing friction for the smallest taxpayers.

3. The Architecture of GST 2.0

The central structural change is the collapse of the four-tier system into a two-slab model—a 5 per cent merit rate for essential and mass-consumption items and an 18 per cent standard rate for most other goods and services—supplemented by a 40 per cent demerit rate reserved for a small set of luxury and sin categories such as tobacco, pan masala, aerated drinks, high-end automobiles, yachts and private aircraft [3][6]. The intermediate 12 and 28 per cent slabs, along with the compensation cess in most categories, have effectively been removed.

In practical terms, roughly 90 per cent of items formerly in the 28 per cent slab moved down to 18 per cent, while close to 99 per cent of items in the 12 per cent slab moved to 5 per cent [4]. Rate cuts applied to around 375 categories of goods—from kitchen essentials and daily-use products to electronics and automobiles—took effect on 22 September 2025 [7]. Several everyday staples such as Ultra-High Temperature (UHT) milk, paneer and Indian breads now attract nil GST, and individual life and health insurance policies were fully exempted [1]. The Centre estimated a net fiscal implication of approximately ₹48,000 crore from the rate changes [8]. Table 1 Summarises the transition from the legacy structure to GST 2.0.

Table 1: Comparison of the legacy GST structure and GST 2.0. Source: compiled from GST Council and PIB releases [1–3].

Feature	GST 1.0 (2017–2025)	GST 2.0 (from 22 Sep 2025)
Principal slabs	Nil, 5%, 12%, 18%, 28% + cess	5% and 18% (+ 40% demerit)
Sin/luxury goods	28% + variable cess	Flat 40% demerit rate
Registration	Manual, often delayed	Risk-based; ~3 days for low-risk firms
Refunds	Slow, working capital locked	90% provisional refund upfront
Dispute resolution	Backlogged litigation	GSTAT operational (Dec 2025)

The rate rationalisation extends beyond goods to key services. Individual life and health insurance premiums, previously taxed, were fully exempted—a measure expected to lower the cost of financial protection for households and to expand insurance penetration, an explicit Viksit Bharat objective. Reductions were also concentrated in employment-intensive and consumption-linked categories: household essentials such as soaps, toothpaste and shampoos moved to lower brackets, while a range of packaged foods, medicines, auto components and construction materials saw meaningful cuts [1–6]. For the vast population of micro and small traders whose turnover is dominated by such everyday categories, the practical effect is a simpler invoice, fewer rate-classification errors and a lighter effective tax on the goods they sell most.

Beyond rates, GST 2.0 introduces a set of process reforms of particular relevance to smaller taxpayers. A risk-based registration system grants approval within roughly three days for low-risk applicants, while high-risk cases undergo Aadhaar-based verification [9]. Provisional refunds of 90 per cent are released upfront for exporters and units affected by inverted duty structures, a provision that took effect from 1 November 2025 and directly frees working capital [4]. The reforms also envisage pre-filled returns, automated refund processing for low-risk claims, and quarterly filing options to reduce operational strain [9]. Institutionally, the Goods and Services Tax Appellate Tribunal (GSTAT) became operational by December 2025, promising faster dispute resolution and greater predictability for businesses [10].

4. The MSME Sector: India’s Engine of Inclusive Growth

Any assessment of GST 2.0’s developmental impact must begin with an appreciation of the scale of the MSME sector. According to the Union Ministry of MSME, the sector contributes approximately 30 per cent of India’s GDP, around 35.4 per cent of manufacturing output and roughly 45.7 per cent of the country’s exports [11]. As the second-largest employer after agriculture, MSMEs support close to 28 crore jobs and represent the principal vehicle for entrepreneurship among women, rural populations and marginalised communities [12].

Formalisation has accelerated sharply since the launch of the Udyam Registration Portal on 1 July 2020 and the Udyam Assist Platform in January 2023 for informal micro-enterprises. Together, these platforms had recorded over 6.5 crore registered units by mid-2025, a roughly fifteen-fold increase in five years [11]. Notably, the number of GST-registered MSMEs is reported to have grown from around 5 lakh in 2017 to well over one crore, underlining GST’s role as an instrument of formalisation [13].

This formalisation drive is reinforced by a widening credit-support architecture. The Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) has facilitated guarantees worth approximately ₹9.80 lakh crore since inception, including a record ₹3 lakh crore in the financial year 2024–25 alone, while the Prime Minister’s Employment

Generation Programme (PMEGP) has generated over 80 lakh jobs, roughly 80 per cent of them in rural areas [11]. GST 2.0 dovetails with these schemes: by improving cash flow and formal credibility, the tax reforms enhance an enterprise's ability to access collateral-free and priority-sector credit, magnifying the impact of the existing financial-inclusion machinery.

The policy environment for MSMEs was further liberalised in the Union Budget 2025–26, which revised the classification criteria by raising investment limits 2.5 times and turnover limits twofold—for example, the micro-enterprise turnover ceiling rose from ₹5 crore to ₹10 crore and the medium-enterprise ceiling from ₹250 crore to ₹500 crore, effective 1 April 2025. This change removes the so-called “graduation penalty,” allowing firms to grow without abruptly losing access to MSME benefits [12]. GST 2.0 complements this liberalisation on the taxation side.

5. GST 2.0 and MSMEs: Channels of Impact

The reforms transmit to the MSME sector through five reinforcing channels: input-cost compression, correction of inverted duties, working-capital release, compliance simplification, and deeper formalisation.

5.1 Input-Cost Compression

Rationalised rates on raw materials, intermediates, packaging and commercial transport reduce input costs for MSMEs. Rate reductions were concentrated in MSME-heavy segments—textiles, leather and footwear, toys, cement, auto components and logistics—where lower expenses improve operating margins and support competitive pricing in both domestic and export markets [4–14]. For consumer-facing micro-enterprises, lower rates on finished essentials also stimulate demand, widening the market they serve.

5.2 Correction of the Inverted Duty Structure

Perhaps the most technically important gain for manufacturers is the alignment of input and output tax rates. Where raw materials had historically been taxed more heavily than finished goods—as in textiles and fertilisers—credit accumulated and remained blocked. By smoothing the flow of ITC, GST 2.0 reduces this distortion, strengthens domestic manufacturing and improves the viability of value-added production within India [4]. This directly supports the Make in India and Aatmanirbhar Bharat objectives that underpin the Viksit Bharat mission.

5.3 Working-Capital Release Through Faster Refunds

For enterprises constrained by delayed refunds, the provision of 90 per cent provisional refunds upfront—operational from 1 November 2025—is transformative. Releasing capital previously tied up in extended refund cycles reduces dependence on expensive external finance, a critical benefit given the sector's persistent credit gap [4–5]. A Deloitte India survey of 1,096 senior executives (the GST@9 Survey) found strong demand for exactly such liquidity measures, with 89 per cent favouring automatic interest on delayed refunds, 88 per cent supporting invoice-based ITC eligibility and 87 per cent backing quarterly tax payment mechanisms—indicating that GST 2.0 is closely aligned with the sector's own priorities [15].

5.4 Compliance Simplification

Faster three-day registration, pre-filled returns and automated refunds reduce the time and resources that small firms must

divert to tax administration. Combined with faceless adjudication and a functioning GSTAT, these measures lower both compliance costs and litigation risk, allowing entrepreneurs to focus on core business activities [16]. Correct HSN-code classification nonetheless remains essential even under fewer slabs, and firms must align their ERP, billing and accounting systems with the new structure to file accurately [9].

5.5 Deeper Formalisation

Lower rates and simpler procedures widen the incentive for informal enterprises to register, bringing more firms into the formal fold. Formalisation, in turn, improves credibility and access to formal credit-enabling MSMEs to integrate into higher-value supply chains and to benefit from priority-sector lending and credit-guarantee schemes such as CGTMSE [16–17]. The cumulative effect is a virtuous cycle of formalisation, credit access, investment and job creation.

5.6 Export Competitiveness

Because MSMEs account for close to 46 per cent of India's exports, the reform's treatment of exporters carries strategic weight [11]. The combination of upfront provisional refunds, smoother ITC flows and lower input costs improves the price competitiveness of Indian goods in global markets and reduces the working-capital penalty that exporters previously bore during long refund cycles. Analysts have framed these measures as a partial buffer against external headwinds—such as shifting global tariff regimes and softening demand—by strengthening domestic manufacturing and export margins simultaneously [14]. For medium enterprises in particular, which generate a disproportionate share of MSME exports, the reforms lower the cost of scaling into export-ready production.

6. Linking GST 2.0 to Viksit Bharat @2047

Viksit Bharat @2047 is the Government of India's long-term vision to become a fully developed, high-income nation by 2047, the centenary of independence. Articulated through NITI Aayog's approach paper and pursued as a “Team India” effort with the states, the mission rests on the empowerment of four constituencies—the poor (Gareeb), youth (Yuva), farmers (Annadata) and women (Nari)—and aspires to build a multi-trillion-dollar economy with equitable, sustainable growth [18–19].

GST 2.0 contributes to this vision on several fronts. By lowering the tax on essentials, it raises household disposable income, particularly for lower- and middle-income families, thereby advancing the equity dimension of inclusive growth. By strengthening MSMEs—the largest source of non-agricultural employment—it supports mass job creation and rural entrepreneurship, directly serving the Gareeb and Yuva pillars. Cheaper machinery and equipment benefit farmers (Annadata), while reduced levies on healthcare essentials and sanitary products advance the Nari pillar [14].

The macroeconomic logic of the reform rests on a consumption multiplier. Lower rates on mass-consumption goods raise real purchasing power; higher demand feeds into greater output by the very MSMEs that dominate consumer-facing production; and rising output supports employment and, ultimately, revenue buoyancy. Independent analysts have estimated that sustained consumption momentum from the reforms could add on the order of 0.6 per cent to GDP, a non-trivial contribution to the growth trajectory required for India's aspiration of becoming a multi-trillion-dollar

developed economy by 2047 ^[8]. For a mission whose economic ambition is frequently framed in terms of a roughly US\$30 trillion economy, broad-based demand generated through indirect-tax relief is a structurally sound engine, because it is distributed across millions of households and enterprises rather than concentrated in a few sectors.

Officials have further framed the two-slab system as a stepping stone toward the eventual convergence to a single GST rate by 2047, a simplification that would mark the maturation of India's indirect-tax regime in line with international best practice ^[8]. In this sense, GST 2.0 is not merely a rate revision but a structural down-payment on the institutional architecture of a developed economy.

7. Early Evidence: Revenue, Consumption and Sentiment

Preliminary data suggest that the reforms have supported

consumption without collapsing revenue. Gross GST collections rose 4.6 per cent year-on-year to about ₹1.96 lakh crore in October 2025—the first full month reflecting the rate cuts-driven by strong festive and pent-up demand, even as rates fell across hundreds of categories ^[7]. Collections moderated to ₹1.70 lakh crore in November 2025 (a 0.7 per cent year-on-year rise), a figure analysts read as evidence that expanding consumption volumes were offsetting the revenue impact of lower rates ^[20].

Sectoral signals were encouraging. The supply value of prepared foodstuffs grew around 17 per cent in September–October 2025 versus 11 per cent a year earlier, while buses and passenger cars grew about 20 per cent against 12 per cent, and construction-related items such as cement and ceramics grew roughly 19 per cent against 2 per cent ^[20]. Table 2 summarises the post-reform collection trend.

Table 2: Gross GST collections in the first two months after GST 2.0. Source: official GST data as reported ^[7-20].

Month (2025)	Gross GST (₹ lakh cr)	YoY Growth	Context
October	~1.96	+4.6%	First full month post-reform; festive demand
November	~1.70	+0.7%	Post-festive; volume growth offsets rate cuts

Business sentiment has moved in a similar direction. Industry bodies pledged to pass on the benefit of rate cuts to consumers, and MSME-focused surveys record a shift in how small firms perceive GST—from a compliance mandate toward a facilitator of formalisation and operational efficiency ^[15-16]. While two months of data cannot settle questions of long-run revenue neutrality, the early evidence is consistent with the reform's central hypothesis: that simplification and rate reduction can be self-financing through higher consumption and improved compliance, rather than requiring a trade-off between growth and fiscal prudence.

8. Challenges and Policy Recommendations

Notwithstanding its promise, GST 2.0 faces genuine implementation challenges. First, state revenue concerns persist: several states flagged potential losses during the Council deliberations, and the discontinuation of the compensation cess raises questions about fiscal balance in the transition period ^[3]. Second, the reforms may deepen residual inverted-duty anomalies in specific segments such as packaging, pharmaceuticals and certain farm inputs, requiring continued rate calibration ^[7]. Third, transition costs for MSMEs-reconfiguring ERP and billing systems, re-mapping HSN codes and re-pricing inventory-fall hardest on the smallest firms with limited technical capacity ^[9].

To consolidate the gains, the following measures merit consideration:

- Institutionalise automatic interest on delayed refunds and pre-deposits, as strongly endorsed by industry, to entrench liquidity discipline.
- Move progressively toward invoice-based ITC eligibility and seamless credit utilisation to reduce mismatches and blocked credit.
- Provide targeted digital-transition support and helpdesks for micro-enterprises adapting billing and accounting systems.
- Complete the correction of remaining inverted-duty structures in packaging, pharmaceuticals and agricultural inputs.
- Protect state finances through a transparent, rules-based revenue-sharing mechanism during the cess phase-out.

- Sustain the roadmap toward eventual rate convergence, communicating the trajectory clearly to build business confidence.

Conclusion

GST 2.0 marks a decisive maturation of India's indirect-tax system. By collapsing a complex five-rate structure into a lean two-slab model, correcting long-standing duty inversions, accelerating refunds and simplifying registration and returns, the next-generation reforms address precisely the frictions that had most constrained the country's Micro, Small and Medium Enterprises. For a sector that generates close to a third of national output, nearly half of exports and employment for tens of crores of citizens, these changes translate into lower input costs, healthier cash flows, deeper formalisation and enhanced competitiveness.

Situated within the Viksit Bharat @2047 mission, GST 2.0 functions as both an immediate stimulus-raising disposable incomes and consumption-and a long-term structural investment in the institutions of a developed economy. Early revenue and consumption data indicate that simplification and rate rationalisation need not come at the cost of fiscal health. The reform's ultimate success, however, will depend on disciplined follow-through: completing inverted-duty correction, safeguarding state finances, supporting the digital transition of the smallest firms, and steadily advancing toward a simpler, more predictable and growth-oriented tax ecosystem. If these conditions are met, GST 2.0 can serve as a meaningful pillar of India's journey from an emerging economy to an inclusive, developed Viksit Bharat by 2047.

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