Weaving it Right

What is the issue?

Recent GST rate rationalisation in textile sector is a concern for already stressed MSME sectors.

What was the GST regime for textiles?

- The **manmade fibres (MMF) sector** had an inverted duty structure with GST rates for
  - Fibre and yarn – 18%
  - Apparel below Rs 1000 – 5%
  - Apparel above Rs 1000 – 12%
- Inverted duty structure occurs when the tax rate on inputs is greater than the tax on the finished product.
- In the case of **cotton sector**, the inverted duty problem does not exist. The GST rates were
  - Fibre and yarn – 5%
  - Apparel below Rs 1000 – 5%
  - Apparel above Rs 1000 – 12%

What changes did government make?

- **MMF Sector -** The Centre had sought to correct the inverted duty structure of MMFs
  - All the finished product rates was raised to 12%
  - The raw materials (Fibre and yarn) rates were flattened to 12% from 18%.
- **Cotton Sector -** To rationalise rates across the sector, the 5% slab was sought to be removed in the case of cotton fabrics as well.

What is the government's rationale?

- Rationalising and lowering rates would address the inverted duty structure problem prevailing in MMF sector and make Indian textile sector competitive.
- Inverted duty structure build-up credits and cascade costs and block the crucial working capital for the industry.

How the changes are viewed by various stakeholders?

- For Manufacturers the government's decision appears to be a mixed bag.
- **For MMF manufacturers** the decision seems good.
- It will save a lot of working capital.
- It will reduce the costs related to accounting.
- It will help to resolve the input tax credit residues accumulate because of inverted tax

structure.

- However the representatives of other segments have expressed their concern.
- **For MSME sector** that dominates the textile sector the decision is a concern.
- It already faces decreased business due to pandemic induced closures.
- Also there is a huge rise in the price of the cotton yarn (30%-40%).
- This decision is expected to significantly increase their cost of production.
- Hence it will be difficult to market the products.
- Similarly manufacturers dependent on the cotton value chain also disapprove of the GST hike on cotton-based products.

What is the general opinion?

- In the guise of correcting rate anomalies, the Centre and States had sought to raise the revenues.
- However taking the short-term route to raise revenues through rate hikes will be an error.
- A higher rate of taxes on inputs and finished products will lead to tax evasion.

What will be an ideal solution?

- The ideal solution would be to keep all input and output rates at 5% while retaining the high-end fabrics at 12%.
- This would be inflation-friendly and boost output.
- However it would not be that acceptable to governments who are looking for a revenue boost.
- Hence a GST of 8% for both input and output will curb prices without hurting production too much.
- However this should be a temporary measure and the rate should eventually move to 5 per cent.
- Lower and fewer GST rates across and within sectors should be considered the ideal.

Reference

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