

Goods and Services Tax

“Everyone’s a Winner”

Until very recently it could take ten days for a truck to transport tea from the gardens of Darjeeling to the ten million plus tipplers of New Delhi, 1500 kms by road to the west. By contrast, lettuces grown on farms around the horticultural hub of Almeria in Southern Spain routinely transit the 2200 kms to the forks of London’s lettuce lovers in 2-3 days.

The World Bank estimates that 60% of the journey time of an Indian truck is spent stationary and logistics costs in India are put at 14% of GDP as against 8% for advanced economies.

There are a number of reasons for these discrepancies, but the biggest culprit has historically been India’s byzantine maze of domestic taxes and excise. Differing sales and value added taxes in each State, including some City levies too, compelled trucks to stop at multiple border check posts in their cross-country journeys. Officials and tax inspectors routinely checked loads, way-bills and other documents. Real or imaginary non-compliance exposed drivers – and therefore truck owners – to corruption and delay. As trucks queued up for hours, and sometimes even days, the border posts often became townships in their own right. All manner of refreshments were available ‘till drivers paid up and awaited the nod of often venal officialdom to allow them on their way.

These differing tax regimes also meant companies, such as Emami, an Ocean Dial investee company with a market leading position in niche consumer goods, had to set up multiple warehouses and distribution hubs in different States. This meant raw materials might traverse the country to a factory with the best tax breaks in one state, only for finished products to come all the way back to be sold in bigger markets near where the raw materials were first sourced. The road blocks of course were suffered each way.

It also prevented companies from choosing logistically advantageous locations which could service consumers across many geographies. In turn this had a knock-on effect on warehousing, transport and distribution costs to say nothing of the administrative and bureaucratic hassles involved in accounting for all these differences. This again contrasts with the US and European models where even the largest consumer companies have concentrated their distribution hubs strategically – for example Procter and Gamble have only six mega- distribution centres to service all 50 US states.

In 2016 Prime Minister Modi’s Government took a significant step forward to resolving this situation by passing the historic Goods and Services Tax Act which modifies and harmonises State and Central taxes, and introduces a whole new regime of registration and compliance. Its introduction will see the physical barriers to transit for most products replaced by an electronic collection of input and output taxes which are then shared between State and Central Governments.

GST was launched at a special midnight session of Parliament on 1 July 2017 so it is now over a year old. It has not been the smoothest of transitions and has involved an IT exercise of mammoth proportions with an estimated 10 million businesses registering for the new electronically administered tax. The barriers have been coming down however and the system is beginning to bed down.

Most significantly it has brought a huge number of businesses into the tax net, as failure to register makes it impossible to charge GST when you sell, or reclaim it, when you buy. The

level of cash 'leakage' has been reduced and the tax take should rise, to say nothing of the huge cache of data this will create on economic activity throughout India. The more recently introduced Electronic Way-bill Act further reduces unaccounted for transits and cash leakage as goods travel between States. Like GST, the initial implementation has been imperfect, but is improving.

Economists have estimated that in time the GST could raise India's GDP growth rate by 1.5% while logistics experts suggest truck journey times will reduce by up to 20%. By-passing bottle necks and consolidating warehouses should improve transport efficiencies and reduce costs.

Emami and other consumer companies seem to have focused on rejigging their distribution relationships first and are now focusing on their supply chain reorganisation, so the benefits will play out over some time. Consumers should benefit too as the GST laws restrict excessive profiteering from the new tax regime.

So now a truck driver from Darjeeling should have a much swifter journey to Delhi. Improved physical infrastructure will also help. As both GST and the expressway build out show, there are few smooth passages to Indian investment but, like a nice cup of Darjeeling tea, it is certainly worth the wait.

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