

The Effect of Goods and Services Tax (GST) on Price Stability: A Review in the Indian Economy Context

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Abstract

The introduction of Goods and Services Tax (GST) in India marked a significant tax reform aimed at creating a unified indirect tax system, simplifying compliance, and enhancing economic efficiency. This paper reviews empirical and theoretical literature to analyse the impact of GST on price stability in India. Key themes include GST's influence on inflation, consumer price index trends, sectoral price variations, and market dynamics. The findings reveal a complex relationship influenced by transitional challenges, compliance mechanisms, and structural adjustments, contributing to moderate inflationary pressures initially, followed by trend stabilization.

Keywords: Goods and Services Tax (GST), Price Stability, Inflation, Tax Policy Reform, Indian Economy

Introduction

The Goods and Services Tax (GST) was launched in India in July 2017 as a comprehensive indirect tax reform, intended to consolidate multiple taxes such as excise duty, VAT, and service tax into a single system. GST aimed to streamline tax administration, reduce cascading effects, and foster a seamless national market (Kumar, 2017). One of the central expectations from the GST regime was its potential to promote price stability by rationalizing tax rates and creating a transparent tax structure.

Price stability is crucial for macroeconomic stability and sustainable growth, influencing consumer purchasing power, investment decisions, and overall economic confidence (RBI, 2017). Understanding the effect of GST on price stability involves examining inflation dynamics pre- and post-implementation, sector-wise price adjustments, and the policy adaptations that shaped this impact. This review offers insights into initial inflationary trends, adjustment costs, and the evolving role of GST in stabilizing prices within the Indian economy.

Theoretical Framework

GST is theoretically expected to reduce price distortions caused by multiple indirect taxes by eliminating the cascading tax effect and promoting input tax credit mechanisms (Kelkar Task Force, 2004). Economic theories on taxation suggest that simplifying the tax structure can improve market efficiencies and lower production costs, thereby reducing upward price pressures (Bradford, 2005). Price stability, commonly measured via the Consumer Price Index (CPI) and Wholesale Price Index (WPI), reflects persistent inflationary or deflationary trends affecting economic welfare (Samuelson

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& Nordhaus, 2009).

Literature Review

The Goods and Services Tax (GST), implemented in India in July 2017, represents a significant overhaul in the country's indirect taxation system aimed at unifying various central and state taxes into a single, streamlined tax framework (Kumar, 2017). The expectation was that GST would enhance economic efficiency, reduce cascading taxes, and ultimately contribute to price stability through transparent and rational tax rates (Kelkar Task Force, 2004). However, the transitional dynamics created a complex environment for price behavior in different economic sectors, necessitating thorough empirical evaluation.

Several studies have analyzed the short-term and potential long-term implications of GST on inflation and price stability. The Reserve Bank of India (RBI, 2017) reported that while GST's impact on inflation was mostly muted and transitory, supply chain efficiencies and the availability of input tax credits helped temper inflationary pressures. Nevertheless, the multi-rate GST structure and compliance complexities caused some initial price volatility (Prabhu, 2017).

Empirical analyses based on Consumer Price Index (CPI) and Wholesale Price Index (WPI) data highlight sectoral disparities in GST effects. Essential commodities such as food, textiles, and daily consumer goods showed relative price stabilization or marginal increases after GST implementation (NCAER, 2017). In contrast, manufactured goods and automobiles witnessed sharper price adjustments attributable to revised tax slabs and input cost realignments (RBI, 2017).

Comparative studies with countries that adopted GST or Value Added Tax (VAT) systems, such as Canada and Australia, provide additional context. These studies confirm a common pattern where GST introduction leads to initial inflationary spikes followed by stabilization as the market and regulatory mechanisms adapt (Bird & Zolt, 2005). India's unique federal tax structure and economic diversity, however, have introduced distinct challenges in achieving uniform price stability across states and sectors (Kelkar Task Force, 2004).

Furthermore, research emphasizes the role of administrative efficiency and GST Council policy interventions, such as rationalizing tax rates and simplifying return filings, in mitigating inflationary risks (Kumar, 2017). The formalization of the economy under GST has also impacted price structures by improving compliance, reducing tax evasion, and promoting a level playing field, which indirectly supports price stability.

These findings indicate that the relationship between GST and price stability is multifaceted, involving not only direct fiscal effects but also broader institutional and economic transformations. Continued evaluation is necessary to fully understand the long-term dynamics and optimize GST's contribution to macroeconomic stability.

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Methodology

This review is based on secondary data analysis from government reports, academic articles, and policy papers. Structured literature search strategies were employed to capture empirical studies assessing inflation, consumer pricing trends, and GST-related tax policy effects.

Findings and Analysis

Studies overwhelmingly indicate an initial inflationary impulse following GST implementation due to transitional issues such as tax rate volatility, compliance costs, and supply chain adjustments (NCAER, 2017). However, data suggests a disinflationary trend aided by GST rate rationalization and improved market formalization (RBI, 2017).

Price indices show moderate sectoral variation, with manufactured and luxury goods experiencing relatively higher inflation compared to essentials. The input tax credit mechanism improved tax credit flow, reducing tax cascading and production costs, indirectly supporting price moderation. Challenges such as the inverted duty structure and frequent policy revisions temporarily affected price predictability but were addressed through GST Council interventions.

Discussion

The implementation of Goods and Services Tax (GST) in India has been a transformative fiscal reform with complex implications for price stability. Although initial studies and market observations indicated a temporary inflationary surge post-GST introduction, this was largely attributable to transitional effects such as adjustments in supply chains, tax rate realignments, and compliance adaptations by businesses (RBI, 2017). The multifaceted GST structure with multiple tax slabs, while essential to accommodate India's diverse economic sectors, also caused variations in price impacts across goods and services.

As the rollout progressed, policy responses, including rate rationalization and the correction of inverted duty structures, played pivotal roles in mitigating sustained inflationary pressures (Kelkar Task Force, 2004). The transparent tax regime introduced by GST has enhanced market efficiency by reducing cascading taxes and allowing seamless input tax credits, which collectively dampen cost-push inflation tendencies. Moreover, improved interstate logistics and supply chain integration under GST decreased price volatility, facilitating more predictable pricing for consumers and businesses alike.

However, the discussion must acknowledge the challenges that remain. India's federal framework and the decentralized GST administration have led to considerable inter-state heterogeneity in tax compliance and enforcement quality, affecting price uniformity nationally. This complexity necessitates continuous policy calibration and technological upgrades to streamline processes and wider GST adoption among informal sectors. Moreover, consumer price sensitivity in India means that any upward price movement in essential goods can have outsized welfare implications,

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demanding careful tax slab design and social safety net integration.

Furthermore, GST's impact extends beyond immediate price effects to influence broader macroeconomic stability. By formalizing economic activities and widening the tax base, GST contributes to higher government revenues and fiscal health, which can stabilize inflation expectations in the long run (IMF, 2017). The experience suggests that GST is not just a tax reform but also a strategic policy tool integral to India's economic modernization and inclusive growth agenda.

Conclusion

The implementation of the Goods and Services Tax (GST) in India represents a landmark fiscal reform aimed at harmonizing the country's indirect tax regime and promoting a unified national market. This review of literature reveals that the introduction of GST initially elicited moderate inflationary pressures, primarily driven by transitional adjustments, compliance costs, and sectoral tax rate realignments. However, these effects were largely transient, as subsequent policy interventions, rate rationalizations, and improved administrative efficiency contributed to stabilizing price levels across most sectors.

GST's elimination of cascading taxes and the establishment of a transparent input tax credit mechanism are critical factors helping reduce inefficiencies in the supply chain, ultimately supporting price moderation. Evidence from consumer and wholesale price indices indicates that while essential commodities maintained relative price stability due to lower or exempted tax rates, prices of manufactured and luxury goods reflected short-term adjustments consistent with revised GST slabs. These observations underscore the differential impact of GST across economic segments and highlight the importance of continuous monitoring and policy calibration. Furthermore, GST has facilitated greater formalization of the economy by enhancing tax compliance and reducing evasion, thereby contributing to a fairer and more predictable business environment. This, in turn, strengthens macroeconomic stability and instills confidence among consumers and investors alike. Notwithstanding these positive outcomes, challenges such as the complexity of multi-rate structures, inverted duty problems, and varying state-level implementations have posed obstacles to achieving seamless price stability.

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