



GST 2.0 REFORMS AND THE INDIAN MARKET: A STUDY

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ABSTRACT:

GST (Goods and Services Tax) 2.0 is India's next-generation overhaul of its indirect tax regime, unveiled in 2025 via decisions of the 56th GST Council. The reforms aim to simplify tax slabs, reduce the rates on essential goods, rationalize input and output tax relationships, provide relief to consumers, and facilitate compliance for businesses—especially Micro, Small, and Medium Enterprises (MSMEs). This paper examines the nature of the GST 2.0 reforms, their likely economic effects on consumption, inflation, business margins, sectoral competitiveness, and government revenues. It also studies challenges of implementation, potential winners and losers in the market, and policy recommendations for maximizing gains. Drawing on recent data, government notifications, expert commentary, and industry reports, this study concludes that while GST 2.0 holds strong promise for boosting consumer demand, easing costs, and formalising the economy, its success will depend on effective compliance infrastructure, clear communication, managing revenue trade-offs, and ensuring that the benefits are passed through to consumers rather than being absorbed in margins.

KEYWORDS:

GST 2.0, TAX REFORM, INDIA, CONSUMPTION, INFLATION, MSMEs, COMPLIANCE, REVENUE IMPACT, MARKET EFFICIENCY

PAPER ACCEPTED DATE:

18th October 2025

PAPER PUBLISHED DATE:

6th November 2025

PAPER DOI NO:

10.5281/zenodo.17544653

PAPER DOI LINK:

<https://zenodo.org/records/17544653>

INTRODUCTION

India's Goods and Services Tax (GST) regime, introduced in 2017, unified many indirect taxes into a single structure but adopted a multi-slab rate system (0%, 5%, 12%, 18%, 28%, plus cesses). Over time, businesses, consumers, and policy analysts have pointed to complexities: classification disputes, inverted duty structures, delays in input tax credits (ITC), and compliance burdens.

Against this backdrop, in 2025 the government, under the 56th GST Council meeting, announced "GST 2.0" reforms aimed at simplifying this structure, rationalising rates, easing burdens on consumers, and stimulating economic growth. These reforms came into effect from September 22, 2025. The purpose of this paper is to study the reforms' content, their impacts on different economic actors (consumers, businesses, government, sectors), the potential trade-offs, and how they may shape India's market landscape.

RESEARCH METHODOLOGY

This research is a descriptive and analytical study primarily based on secondary sources. The data gathered includes government notifications from the GST Council

and the Central Board of Indirect Taxes and Customs (CBIC), reports from tax advisory firms, media coverage, expert opinions, and observed early market reactions. The core timeframe for this analysis extends from the period of the announcement up to several months post-implementation (late 2025).

LITERATURE REVIEW

The original Goods and Services Tax (GST), introduced in 2017, unified numerous indirect taxes under a structure that featured multiple rate slabs: 0%, 5%, 12%, 18%, 28%, along with cesses.

Prior to the 2.0 reforms, key complexities identified by various stakeholders included classification disputes, inverted duty structures (where input taxes were higher than output taxes), delays in the disbursement of Input Tax Credits (ITC), and significant compliance burdens.

The necessity for the GST 2.0 reforms arose against this backdrop of complexity, with the explicit aims of simplifying the existing structure, rationalizing tax rates, alleviating consumer burdens, and boosting overall economic growth.

Experience from other countries that have adopted Value Added Tax (VAT) or GST systems suggests that simplification of rates, reduction of the number of slabs, and removal of numerous exemptions typically lead to more efficient tax administration, lower compliance costs, and reduced market distortions.

International lessons, particularly from efficient tax administrations (e.g., in some Asian countries and the EU), underscore the critical importance of a digital tax administration, including automated refunds and well-integrated portal systems, for achieving better compliance and reducing tax leakage.

SUBJECT MATTER: KEY FEATURES OF GST 2.0 REFORMS

The GST 2.0 reforms, effective from September 22, 2025, focus on structural simplification and targeted relief.

1. **Simplified Slab Structure:** The previous multi-slab system has been simplified. The 12% and 28% tax slabs have been largely eliminated, resulting in two primary slabs: a 5% rate for essential or merit goods, and an 18% rate as the standard levy.
2. **Demerit/Luxury Rate:** A new, significantly higher 40% rate has been introduced for ultra-luxury goods, tobacco, and other similar items deemed 'sin goods'.
3. **Rate Rationalization:** Many items previously taxed at the higher 12% or 28% slabs have been reclassified into the 5% or 18% slabs. This has benefited sectors such as consumer electronics, automobiles (small cars), cement, and construction raw materials.
4. **Exemptions/Zero GST:** Preferential rates or complete exemptions (0% GST) have been applied to essentials like daily goods, certain Fast-Moving Consumer Goods (FMCG), foodstuffs, and in some cases, life-saving drugs, medicines, education, and health insurance policies.
5. **Relief and Complies the economy.**
6. **Consumer Demand and Inflation:** Consumers are expected to benefit from lower prices on essential and daily-use goods (moving to 5% or exemption), which should boost disposable income, particularly for lower and middle-income groups. This should stimulate purchasing power and consumption demand, potentially moderating structural inflation in non-fuel/non-oil categories.
7. **Business and Working Capital:** Businesses, especially manufacturers and MSMEs, are expected to see improved margins and reduced working capital constraints. This is due to the planned speed-up of ITC refunds and the better alignment of input and output tax rates. Sectors like FMCG, consumer durables, small cars, and textiles are key winners.
8. **Formalization and Inclusion:** The simplification

and lower rate structure are expected to encourage unorganized businesses to transition into the formal GST system, granting them better access to credit and improved regulatory clarity.

9. **Government Revenue:** While the widespread rate cuts on essentials will lead to a loss of tax revenue, the introduction of the 40% demerit slab is intended to partially offset these losses. The government is hopeful that a significant increase in consumption and the broadening of the tax base will eventually lead to a net economic gain.
10. **Redistributive Effects:** The cuts on basic goods disproportionately benefit lower-income households, while the higher tax on luxury/sin goods primarily affects higher-income groups, suggesting a potential redistributive effect of the tax burden.

KEY FEATURES OF GST 2.0 REFORMS

Simplified slab structure: The multi-slab system has been simplified. The 12% and 28% slabs are largely removed. The new regime has essentially two main slabs: 5% (for essential or merit goods) and 18% (standard rate). In addition, a 40% demerit/luxury/sin rate has been introduced for ultra-luxury goods, tobacco, and similar items.

Rate reductions and reclassification: Many items formerly in higher slabs (12% or 28%) have been shifted to 5% or 18%. Essentials like daily goods, FMCG, food stuffs, insurance, etc., have been given preferential rates or exemptions. Some sectors like consumer electronics, automobiles (small cars, etc.), cement, construction raw materials have also benefitted from rate cuts.

Exemptions / Zero GST: Certain life-saving drugs, medicines, items like UHT milk, paneer, Indian breads, education and health-insurance policies are exempted or set at 0% GST in certain cases.

Relief to MSMEs and compliance simplification: The reforms include measures to reduce compliance burden, rationalise input-output taxation to reduce inverted duty anomalies, speed up input-tax credit refunds, and simplify registration / return procedures for smaller businesses.

Revenue and government trade-offs: While rate cuts reduce tax burden on many goods, there is a trade-off in revenue. Certain luxury/sin categories are taxed more heavily (40%) to compensate. Also, some estimates indicate revenue losses from reductions in slabs, though with hopes that increased consumption may partially offset this.

EFFECTS ON CONSUMERS

Lower prices for essential goods: With many daily-use goods, toiletries, food items, basic appliances moving to lower slabs (5%) or exemption, consumers are likely to see price reductions. This boosts disposable income, especially for lower and middle-income households. Inflation pressures may moderate in certain categories.

Increase in purchasing power and consumption demand: Reduced tax burden means more real income. This tends to stimulate demand for both essentials and other goods. With the Navratri/festive season aligned with the reforms, demand can see uplift

Heterogeneous impact: Consumers of luxury/sin goods may face higher taxes; consumers of mid-range goods may benefit; those in remote/rural areas might benefit less if supply chain costs or retail markups prevent full pass-through. Also, exemption items benefit those who use them; non-exempt or luxury items may see price hikes or remain expensive.

Inflation and price stability: Some food and essential item inflation may ease. However, inflationary pressures from other sources (fuel, energy, supply constraints) remain. The reform may help reduce structural inflation in non-fuel, non-oil items.

EFFECTS ON BUSINESSES AND INDUSTRY

Working capital and margins: Businesses, especially manufacturers and MSMEs, often suffered from inverted duty structures (input taxes higher than output taxes), delayed refunds, and complex tax compliance. GST 2.0 aims at aligning input and output rates better, speeding refunds, and simplifying compliance, which can reduce working capital constraints and improve margins.

Cost of production and supply chain effects: Lower GST on raw materials, packaging, transport helps reduce input costs. Especially for sectors like FMCG, textiles, construction, electronics. Reduced logistics costs (for example, on commercial transport) help lower final costs.

SECTORAL WINNERS AND LOSERS:

- a) Winners: FMCG, consumer durables, small cars, textiles, construction materials, appliances, insurance, daily goods.
- b) Moderately impacted: Mid-range and premium goods—though some tax benefit; but some items may stay under higher slab or increase due to sin / luxury tax.
- c) Losers (or neutral): Luxury goods, sin goods which face higher rates; businesses unable to pass through full benefits due to competition or price stickiness.

Compliance, regulatory load and adaptation: For many businesses, the reforms reduce complexity, but there is still adjustment cost—re-classifying items, updating invoicing systems, training staff, handling revised return/ITC procedures. Smaller and unorganised firms may find this more burdensome.

Effect on formalisation and MSME inclusion: Simplification and lower rate structure can encourage unorganised businesses to enter formal GST system. Formality leads to better access to credit, better regulatory clarity, longer-term stability.

IMPACTS ON GOVERNMENT REVENUE AND FISCAL CONSIDERATIONS

Revenue loss and gain trade-offs: Rate cuts mean loss of tax revenue from many items; introduction of 40% demerit slab is meant to offset some losses. Early estimates suggest that while some revenue is foregone in essentials, luxury/sin tax increases and growth in consumption may help.

State governments' concerns: States depend heavily on GST revenues; any net loss may require compensations. The removal of compensation cess for most items (except some like tobacco) may affect state revenues. Coordination with states is essential.

Inflation's effect on tax base: Lowering rates may reduce inflation in certain goods, but may shift demand, increasing turnover in reduced-rate items; tax base may broaden. If consumption grows significantly, revenue from the standard rate slab (18%) may increase.

Cost of implementation: Government needs to invest in communication, GST portal upgrades, training, grievance redressal, clarifying classifications to avoid litigations and disputes. These transition costs are non-trivial.

Long-term fiscal sustainability: The reforms' net impact on growth (via higher consumption, formalisation) will affect tax collections over time. If reforms succeed, broader economic growth may lead to higher overall revenue even with lower rates in many categories.

MACROECONOMIC IMPACTS

Consumer demand and GDP growth: Lower taxes on many consumer goods, combined with enhanced purchasing power, is likely to lift consumption, a major component of GDP. With reforms timed ahead of festive season, there may be a boost in overall economic activity.

Inflation trends: By reducing GST on essentials and mainstream goods, inflation in consumer prices may moderate. This helps in managing CPI inflation, lowering cost-of-living pressures, which in turn helps real incomes.

Investment and business sentiment: Simplification and reduced tax uncertainty may improve business sentiment. Lower tax burdens may incentivize investment in production, manufacturing, supply chain infrastructure.

Distributional effects: Lower-income households benefit disproportionately from GST cuts on basic goods, while luxury tax increases affect higher income groups more. Thus, there may be some redistributive effect.

Trade, exports, and competitiveness: Export-oriented sectors benefit if input costs reduce and compliance burdens ease. Also, international perception of India as a smoother tax regime may attract investment. On the other hand, higher GST on luxury/sin goods may affect imports of those.

CHALLENGES AND RISKS IN IMPLEMENTATION

Pass-through of benefits: Even if rates are cut, manufacturers, retailers, and intermediaries may not fully pass on savings to final consumers. Price stickiness, cost structures, input inflation may blunt the benefit.

Classification disputes and legal ambiguity: With many items moving slabs, some subjectivity in classification may lead to disputes, litigations, or varying state-level interpretations.

Administrative capacity: Ensuring small businesses, rural traders, informal sector can understand and comply with new rules, updating of accounting systems, digital tools, etc.

Monitoring and enforcement: Ensuring firms do not exploit transition periods, mischaracterize goods, or avoid tax liabilities. Effective grievance redressal and audit mechanisms are needed.

Balancing revenue and fiscal health: Revenue shortfall in short term could stress government budgets, especially for states; if consumption growth does not offset losses, deficits may widen. Also risk of inflation from other sources (fuel, energy) undermining gains.

COMPARISONS WITH GST REFORM EXPERIENCES ELSEWHERE & LESSONS

Many countries that adopted VAT or GST systems have found that simplifying rates, reducing slabs, and removing exemptions often lead to more efficient tax administration, lower compliance costs, and fewer distortions. India's move echoes experiences in some Asian countries.

The importance of digital tax administration: countries with efficient e-invoicing, automated refunds, well-integrated portal systems often see better compliance and lower leakage. India's strengthening of GSTN / e-invoicing / refund process is aligned with this.

Transition costs are always high. Australia, New Zealand, and many EU countries had multiple disputes initially when classifying goods or handling refund claims. Adequate training, clear policy communication, well-defined appeals mechanisms are crucial.

Revenue volatility is a risk: when tax cuts are made, short term revenue dips occur; but over time with formalization, growth of base, the net revenue can recover. Policy makers need buffer mechanisms (reserves, compensations) for times of shortfall.

Social equity and consumption patterns matter: the poorest benefit most from cuts in essentials; but luxury goods tax need careful calibration so as not to unduly penalize local producers in luxury sectors or craftsmen.

EARLY MARKET REACTIONS & EVIDENCE

Consumer responsiveness: Reports suggest strong positive reactions in sectors with rate cuts—FMCG, consumer durables, daily essentials—leading to expectations of sales increases during festivals.

Price adjustments: Some companies (e.g., in consumer goods, electronics) have announced or begun reducing prices to pass on GST reductions. However, there are also cases where prices have not adjusted fully, due to input costs or other margins.

Sectoral anticipation: Automobile manufacturers,

appliance makers are expected to benefit from demand increase. The real estate/construction sector, with reduced rates on cement etc., expects cost savings. Insurance industry may see higher uptake if life/health insurance becomes zero or low taxed.

State level roll-out challenges: States like Jammu & Kashmir have adopted protocols (consumer benefit protocols, helpdesks) to ensure compliance and awareness. Some states may lag in implementation or enforcement.

Fiscal estimates: Early projections indicate a revenue loss in some categories, but government expects net economic gain via higher consumption and formalization. There is also expectation of inflation relief for consumers.

POLICY RECOMMENDATIONS

Ensure full pass-through to consumers: Regulatory oversight and consumer protection to monitor that reductions in GST rates lead to lower retail prices. Provide clarity and penalties if producers/retailers fail to adjust.

Strengthen compliance infrastructure: Upgrade GSTN, e-invoicing tools, simplified returns, helpdesks, training, especially for MSMEs and small traders.

Clear classification and dispute resolution: Define goods/categories sharply; reduce subjective ambiguities; activate the Goods and Services Tax Appellate Tribunal (GSTAT) and state-level adjudication to reduce litigation and delays.

Align rates and input tax credit flows: Ensure that input rates, raw material taxation, packaging, transport are aligned so that businesses do not suffer cash flow stress due to mismatches.

Fiscal buffers and state compensation: Because states' revenues may be affected, central governments should arrange compensations, maintain fiscal discipline, and avoid sudden revenue gaps.

Continuous monitoring and adjustment: Use data to track impacts on consumption, inflation, revenues; be prepared to adjust slabs, rates, or regulations in cases where unintended distortions occur.

Consumer awareness and transparency: Public communication campaigns to educate citizens about GST 2.0 changes: what items are cheaper, what is exempt, what documentation or compliance may be needed.

OUTCOMES: LIKELY ECONOMIC EFFECTS

The GST 2.0 reforms are anticipated to have heterogeneous impacts across the economy.

1. Consumer Demand and Inflation: Consumers are expected to benefit from lower prices on essential and daily-use goods (moving to 5% or exemption), which should boost disposable income, particularly for lower and middle-income groups. This should stimulate purchasing power and consumption demand, potentially moderating structural inflation in non-fuel/non-oil categories.

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CONCLUSION

GST 2.0 represents a significant tax reform in India, arguably the most sweeping since the original GST rollout in 2017. By rationalising multiple tax slabs, reducing rates on essentials, introducing a higher rate for luxury/sin goods, simplifying compliance, and easing burdens on MSMEs and consumers, the reforms aim to make the indirect tax regime more citizen-centric, growth-oriented, and fair.

For the Indian market, the reforms have potential to stimulate demand, reduce inflation in everyday items, support business competitiveness, foster formalisation, and improve fiscal efficiency. However, these gains are not guaranteed. Their realisation depends on effective

implementation: ensuring benefits are passed through along supply chains, avoiding classification ambiguities, building institutional capacity, and managing revenue trade-offs especially for state finances.

In sum, GST 2.0 is more than just a tax rate cut—it is a structural reform intended to reshape consumption patterns, support wider economic inclusion, simplify regulatory burdens, and reinforce India's aspiration of a more formal, equitable, and growth-driven market economy. If executed well, it could mark a new chapter in India's market development and pave way for stronger, more sustainable economic growth.

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