

Impact of GST 2.0 on Consumer & Economy

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Abstract

The GST 2.0 reforms, effective from September 22, 2025, represent the most significant recalibration of India's indirect tax framework since its 2017 inception. This report provides an exhaustive analysis of the structural, macroeconomic, and sectoral impacts of this new tax regime. The core of the reform is the rationalization of the four-tiered tax structure into a simplified two-slab system (5% and 18%), complemented by a special 40% de-merit rate for luxury and sin goods. The strategic timing of these rate cuts, coinciding with the festive season, is designed to serve as a powerful catalyst for a consumption-led economic revival. The analysis projects a significant moderation in consumer price inflation, alongside a notable boost to India's Gross Domestic Product (GDP). On a sectoral level, key industries like Fast-Moving Consumer Goods (FMCG), consumer durables, and automobiles are poised for a demand surge. “Lower prices on essentials are expected to boost consumption, with companies like Britannia, HUL, and Nestlé benefiting” (Times of India, 2025b). Concurrently, the reforms address long-standing challenges by correcting inverted duty structures, lowering input costs for manufacturers and Micro, Small, and Medium Enterprises (MSMEs), and streamlining compliance procedures. While potential challenges such as logistical complexities and the paradoxical financial burden on the insurance sector are noted, the overall assessment indicates

that the new GST framework is a strategic, structural reform aimed at bolstering domestic resilience and setting the stage for sustained, inclusive economic growth.

Keywords: GST Reforms, Indian Economy, Taxation, Macroeconomic Impact, GST 2.0, Consumer Spending, Fiscal Policy, MSMEs

The Goods and Services Tax (GST) 2.0 reforms, introduced by Prime Minister Narendra Modi and approved during the 56th GST Council meeting on September 3, 2025, represent the most significant overhaul of India's indirect tax system since its original implementation in 2017. Positioned as a "next-generation" reform, this initiative aims to create a more citizen-friendly tax structure by simplifying processes, easing compliance burdens, and improving the overall business environment. The GST Council's unified endorsement—reflecting agreement from all states and union territories—highlights a shared commitment to making the tax system more transparent, equitable, and growth-oriented.

This reform package focuses on a wide range of economic drivers, including labor-intensive sectors, agriculture and farmers, healthcare, and the aspirational middle class. Rather than just adjusting tax rates, GST 2.0 seeks to fix long-standing structural issues such as ambiguous slab rates, cumbersome compliance, and unresolved disputes. In doing so, the government intends to build a more robust, reliable, and transparent tax framework that can support sustained economic growth.

The reforms took effect on September 22, 2025—deliberately chosen to coincide with the beginning of Navratri, a major festive season marked by heightened consumer spending in India. The timing of reforms during Navratri was a deliberate move to spur consumption" (Economic Times, 2025a). By lowering prices on many goods during this period, the government aims to boost domestic demand and generate a surge in household consumption. This strategic timing reflects a broader policy goal: to use tax reforms as a tool to stimulate

demand and create a strong multiplier effect on the economy, especially during times of global economic uncertainty.

2.0 The 2025 GST Framework: Key Structural and Rate Changes

2.1 Streamlined Rate Structure: Transition to a Two-Tier System

A central feature of the 2025 GST reform is the overhaul of the previous four-tier tax structure (5%, 12%, 18%, and 28%) into a simplified two-rate system. Under the new framework, a 5% "Merit Rate" applies to essential goods, while a uniform 18% "Standard Rate" covers the majority of other goods and services (Vision IAS, 2025). This shift eliminates the former 12% and 28% slabs, aiming to enhance transparency and reduce complexity for both businesses and consumers. By simplifying the rate structure, the reform seeks to minimize classification-related disputes, which were a frequent source of confusion and legal challenges in the earlier system.

2.2 Introduction of the Special De-merit Rate (40%) and Expanded Zero-Rated Category (0%)

To uphold a progressive taxation model and maintain fiscal balance, the reform introduces a new "De-merit Rate" of 40%, applied to a limited range of luxury and socially harmful goods—such as aerated sugary beverages and premium luxury vehicles—that are considered non-essential. At the same time, the zero-rated (0%) category has been broadened to cover more essential goods and services. This now includes educational items like notebooks, maps, and pencils, as well as 33 critical life-saving medicines and diagnostic tools for serious chronic illnesses. In a notable shift, individual premiums for health and life insurance have been fully exempted from GST—down from the earlier 18% rate—marking a significant step toward making these services more accessible.

2.3 Detailed Sector-wise Impact of Rate Revisions

The 2025 GST reforms have introduced widespread changes that affect multiple sectors of the economy:

Essential Commodities: The GST rate on many everyday items has been reduced from the previous 12% or 18% to a lower 5%. This includes common household products like soaps, shampoos, hair oil, and toothpaste, along with packaged food items such as biscuits, pasta, namkeens, and cornflakes—making these essentials more affordable for consumers.

Consumer Discretionary Goods: Products that were earlier taxed at 28% have now been shifted to the new 18% standard rate, offering considerable financial relief to middle-income households. This rate reduction applies to appliances like air conditioners, refrigerators, televisions, and washing machines. In addition, the GST on small passenger vehicles—cars with engines under 1200cc and two-wheelers under 350cc—has also been lowered from 28% to 18%, making them more accessible to the average buyer.

Core Industries: Major Gains for Manufacturing and Construction are major beneficiaries. The manufacturing and construction sectors stand out as key beneficiaries of the 2025 GST reforms. One of the most notable changes is the reduction of GST on cement from 28% to 18%, a move anticipated to boost infrastructure growth and stimulate activity in the real estate market. Additionally, the GST on commercial transport vehicles, including trucks and buses, has also been cut from 28% to 18%. This reduction is expected to bring down logistics and transportation costs, enhancing overall efficiency.

Services Sector: Enhancing Affordability Through Tax Reductions

To make services more accessible to the average consumer, the GST on several service categories has been lowered. Hotel accommodations priced up to Rs.7,500 per night now attract only 5% GST, reduced from the earlier 12%. Similarly, services like gyms, salons, barbershops,

and yoga centers have seen their GST rates cut from 18% to 5%, making them more affordable for the general public.

Agriculture and Rural Economy: Focused Relief for Farmers and Rural Communities

The reform also delivers targeted benefits to the rural economy. GST on agricultural equipment—including farm machinery, irrigation tools, and fertilizers—has been reduced from 12% or 18% to a uniform 5%. This change is expected to lower input costs for farmers and promote the use of modern, eco-friendly agricultural technologies.

A comprehensive summary of the rate changes is provided in the table below.

Table: GST Rate Changes Across Key Sectors

Sector/Product/Service	Previous GST Rate	New GST Rate	New Slab
Household & Essentials			
Soaps, Shampoos, Toothpaste	18%	5%	Merit
Packaged Foods (biscuits, namkeens)	12% or 18%	5%	Merit
UHT Milk, Paneer, Indian Breads	5%	0%	Exempt
Consumer Discretionary			
TVs, ACs, Refrigerators	28%	18%	Standard
Small Cars (<1200cc)	28%	18%	Standard
Bikes (≤ 350 cc)	28%	18%	Standard
Core Industries			
Cement	28%	18%	Standard
Commercial Goods Vehicles (trucks)	28%	18%	Standard

Services			
Hotel Stays (<₹7,500/day)	12%	5%	Merit
Salons, Gyms, Yoga Services	18%	5%	Merit
Individual Health & Life Insurance	18%	0%	Exempt
Agriculture & Healthcare			
Farm Machinery, Tractors	12%	5%	Merit
33 Life-Saving Drugs	12%	0%	Exempt
Other Medicines	12%	5%	Merit
Sin & Luxury Goods			
Luxury Cars, Premium Bikes	28% + Cess	40%	De-merit
Aerated Sugary Drinks	28% 40%	40%De-merit	De-merit

This table provides a representative overview of key changes and is not exhaustive.

3.0 Macroeconomic Impact and Economic Projections

3.1 Inflation Dynamics: Analyzing the Effect on Price Trends

The recent GST rate reductions are expected to help ease inflationary pressures in the economy. Various economists and research institutions forecast a decline in Consumer Price Index (CPI) inflation by approximately 50 to 90 basis points (0.5–0.9%) over the next year, assuming the full benefit of tax cuts is passed on to consumers. Some forecasts, such as Citi's, are even more optimistic, predicting a drop of up to 1.1 percentage points.

These projections are particularly noteworthy in light of India's current inflation environment. As of July 2025, headline CPI inflation stood at just 1.55%—the lowest level recorded since June 2017. Even more striking is the food inflation rate, which entered negative territory at -1.76%, indicating a rare deflation in food prices not seen in over six years. Thus, the

GST 2.0 reforms are not being deployed in response to high inflation, but rather as a forward-looking strategy to reinforce and extend an already favorable inflationary trend.

The strategic timing of the reforms enhances their overall impact. With inflation already at low levels, households are likely to feel the effects of price reductions more strongly, both psychologically and financially. By cutting taxes across a broad range of goods and services, the reforms effectively increase disposable income for consumers. This additional spending power is expected to drive higher consumption, creating a positive cycle of demand-led economic growth. It reflects a calculated use of fiscal policy to amplify purchasing power and strengthen consumer confidence in the economy. However, the true magnitude of this impact will hinge on how much of the tax savings businesses actually pass on to consumers—something that, in the absence of a formal anti-profiteering framework, will largely be influenced by the level of competition in the market.

3.2 Boosting GDP Growth: A Consumption-Driven Strategy

The GST rationalization is being recognized as a key driver of India's economic expansion. Experts estimate that these reforms could contribute an additional 20 to 30 basis points (0.2–0.3%) to GDP growth in FY26, largely fueled by a projected rise in domestic consumption—the largest component of the nation's GDP.

The reforms have been strategically timed to counter external economic challenges, such as the recent 50% tariff imposed by the United States on Indian exports. By reducing the cost of domestically produced goods, the government is intentionally shifting focus from external trade to internal consumption, positioning the Indian consumer as a stabilizing force in the face of global trade disruptions.

Lower prices on both essential and aspirational items are expected to drive household spending, which will in turn boost manufacturing activity and job creation. This reflects a forward-thinking strategy that taps into the strength of India's vast domestic market to create a

more resilient and self-reliant economic growth path. When coupled with other positive developments—such as declining inflation, favorable monsoon conditions, and recent personal income tax cuts—the GST reforms are expected to lay the foundation for a strong and sustained recovery in consumer demand.

3.3 Fiscal Impact: Revenue Outlook and Long-Term Viability

The recent GST rate reductions have sparked concerns about a possible dip in government revenues. While the government estimates the gross revenue loss at around ₹48,000 crore, some economists suggest it could be closer to Rs.1 lakh crore. However, a detailed assessment by the State Bank of India (SBI) indicates that the actual fiscal impact may be quite limited, with the Centre expected to bear only about Rs.3,700 crore in revenue loss for FY26.

This modest impact is based on the assumption that increased consumption and better tax compliance will help offset the initial shortfall. Historically, GST collections have demonstrated strong growth, with average monthly revenues steadily rising. The new, simplified rate structure is expected to ease compliance requirements, promote voluntary registration, and expand the tax base. This reform could trigger a virtuous cycle—lower tax rates leading to higher sales and greater formalization of the economy, ultimately resulting in increased tax revenues. As a result, the projected fiscal risks are seen as well-calculated and sustainable in the long run.

Table: Projected Macroeconomic Impact from Various Research Sources

Economic Indicator	Projection Range	Source/Analyst
CPI Inflation Moderation	50–90 bps over 12 months	Economic Times, 2025b
CPI Inflation Moderation	up to 1.1 percentage points	Citi
GDP Growth Boost	20–30 bps in FY26	QuantEco Research, HDFC Bank, Standard Chartered

Net Revenue Loss (Centre)	Rs 3,700 crore in FY26	Times of India, 2025
Gross Revenue Loss	Rs 48,000 crore (Govt. Estimate)	GST Council, Government

4.0 Sectoral Analysis and Stakeholder-Specific Effects

4.1 Effects on Consumers and Households

One of the most immediate and visible outcomes of the GST 2.0 reforms is the increase in consumer purchasing power. The across-the-board reduction in tax rates on both everyday essentials and higher-end consumer goods offers substantial relief to the public. By lowering the GST on essential products—from the earlier 12% and 18% rates to the new 5% merit rate—the reforms directly reduce the cost of living for millions of households.

This is especially significant for India’s growing middle class, as price reductions on goods like small cars, two-wheelers, and electronic appliances make previously aspirational purchases more affordable.

The reforms are carefully designed to benefit both urban and rural consumers. Urban demand is expected to rise with reduced prices on consumer durables and vehicles, while rural households stand to gain from lower GST on farm equipment, fertilizers, and agricultural inputs. This targeted strategy supports increased purchasing capacity in rural areas, helping to drive demand in key sectors. Overall, the reforms aim to promote inclusive growth by stimulating consumption across all demographic and economic segments.

4.2 Effects on the Manufacturing and MSME Sectors

The manufacturing industry—an essential pillar of India’s economic development—is set to gain significantly from the GST 2.0 reforms. Lower tax rates on a broad range of raw materials, intermediate goods, and finished products are expected to reduce production costs, boost competitiveness, and stimulate market demand. A key highlight is the resolution of

inverted duty structures, particularly in sectors like man-made textiles. In this segment, GST rates on fibers and yarns have been brought down from 18% or 12% to 5%, correcting a major imbalance that previously strained manufacturers' working capital. This change is likely to improve profit margins and enhance global and domestic competitiveness.

For Micro, Small, and Medium Enterprises (MSMEs), the reforms are especially transformative. The shift to a simpler two-rate GST structure is expected to minimize classification-related disputes and ease compliance, enabling small businesses to concentrate on growth rather than navigating complex tax processes. In addition, the introduction of a new “Simplified GST Registration Scheme” promises swift registration—within just three days—for qualifying low-risk businesses. This reform is a significant step toward streamlining regulatory processes, enhancing ease of doing business, and fostering entrepreneurship across the country.

4.3 In-Depth Look at Key Industries Automobile Sector:

The automotive sector stands to gain considerably from the GST 2.0 reforms. The reduction in GST from 28% to 18% on small cars, motorcycles with engine capacities up to 350cc, as well as commercial vehicles like buses and trucks, offers substantial relief to both consumers and the logistics industry. This move is expected to stimulate demand in the mass-market segment.

However, the transition also brings challenges—particularly for automobile dealers. Many have existing inventories purchased at the previous higher tax rate, and the compensation cess paid on these vehicles is non-refundable. This creates a potential financial strain for dealers stuck with unsold stock. While companies such as Tata Motors have committed to fully passing on the tax benefits to consumers, addressing the inventory issue will require a coordinated effort across manufacturers, dealers, and policymakers to avoid disruptions in the supply chain.

Insurance & Healthcare Sector:

The GST exemption on individual life and health insurance premiums is designed to make insurance more accessible and affordable, supporting the goal of broader financial inclusion. However, this move has created a complex challenge for insurance providers. With their services now exempt from GST, insurers lose the ability to claim Input Tax Credit (ITC) on the goods and services used in their operations. What was once a tool to reduce their overall tax liability now turns into an added cost. (Economic Times, 2025c).

Industry experts caution that insurers may respond by increasing base premiums to offset this financial burden, which could undermine the very benefit the exemption was meant to offer. This reveals an unintended consequence of the policy that needs careful management to ensure the original goal—greater affordability—is not compromised.

On the other hand, the healthcare sector as a whole stands to gain significantly. Reductions in GST on essential medical items—including life-saving drugs, diagnostic tools, surgical equipment, and other healthcare products—are expected to enhance accessibility and lower costs, ultimately making healthcare more affordable for the general population.

Real Estate and Construction:

The reduction of GST on cement from 28% to 18% marks a significant advantage for the real estate and infrastructure sectors. Since cement and steel account for a large share of construction expenses, this tax cut is expected to lower overall material costs by around 10%. These savings can translate into more affordable housing and reduced project costs. As a result, the real estate market is likely to see increased demand, while large-scale infrastructure projects could progress more rapidly. This, in turn, is anticipated to generate employment opportunities and give a substantial boost to the construction industry as a whole.

Table: Sectoral Gainers and Challenges

Sector	Positive Impacts	Negative Impacts/Challenges
FMCG	Lower prices on essentials to boost consumption; improved margins for companies; greater demand from rural markets.	Logistical challenges with re-tagging prices on existing inventory.
Automobiles	Lower prices on small cars and bikes to spur mass-market demand; lower costs for logistics and commercial vehicles.	Dealers face financial losses on unsold inventory due to non-refundable cess.
Manufacturing	Lower input costs; correction of inverted duty structures; improved competitiveness and export potential.	Requires recalibration of ERP systems and billing software; coordination across supply chain.
Insurance	Premiums on life and health policies now exempt from tax, improving affordability for consumers.	Insurers lose Input Tax Credit (ITC), which could be passed on to consumers as a new cost burden.
Real Estate & Construction	Lower GST on cement and other materials reduces construction costs; makes housing more affordable and spurs infrastructure development.	Requires seamless pass-through of benefits to the end consumer.

5.0 Conclusion: Summary of Findings and Future Prospects

The GST 2.0 reforms mark a decisive and strategic effort to simplify, make fairer, and promote growth within India's indirect tax system. By streamlining tax slabs and implementing widespread rate cuts, these reforms aim to increase affordability for consumers and stimulate domestic consumption—an essential pillar of India's economic strength. The timing of these changes, aligned with the festive season, is a deliberate move to maximize economic impact and foster a positive cycle of consumer spending driven by optimism.

Projections suggest a substantial pass-through of tax reductions to consumers, which should help ease inflation and contribute significantly to GDP growth in the upcoming fiscal year. Although there are concerns about revenue loss from these rate cuts, the government is optimistic that increased consumption and improved tax compliance will balance out the initial shortfall. On the sectoral front, industries such as FMCG, consumer electronics, and automobiles are expected to experience heightened demand, while key sectors like manufacturing and construction will benefit from lower input costs and correction of past structural issues.

The transition, however, is not without its challenges. Retailers will need to manage price adjustments, and automobile dealers face financial strain due to unsold inventory purchased under the old tax rates. Additionally, the GST exemption on insurance premiums presents a paradox: insurers lose the ability to claim Input Tax Credit, potentially leading to higher base premiums for customers, which could counteract the intended relief. (Economic Times, 2025c).

In summary, these “Next-Generation GST” reforms lay a strong foundation for a more resilient and prosperous India by focusing on simplification, rationalized rates, and streamlined administration. While implementation hurdles remain, the reforms comprehensively position

India to withstand global uncertainties by relying on its robust domestic market. The overall success will hinge on the full transmission of benefits to consumers and the effective roll-out of updated compliance and dispute resolution processes. This marks a significant new phase in India's economic development, where fiscal policy is actively used not just for revenue generation but as a key driver of growth and public welfare.

Conflict of Interest: The corresponding author, on behalf of second author, confirms that there are no conflicts of interest to disclose.

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