



# Effect of GST on inflation and economic growth in India with special references to food prices

Isht Jot Singh<sup>1\*</sup> and Dhananjay Sharan<sup>2</sup>

<sup>1</sup> Research Scholar, Department of Economics, M. J. P. Rohilkhand University, Bareilly, Uttar Pradesh, India

<sup>2</sup> Professor & Research Supervisor, Department of Economics, Hindu College, Moradabad, Uttar Pradesh, India

Corresponding author: Isht Jot Singh

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## Abstract

The paper explores how Goods and Services Tax (GST) has shaped inflation and economic growth in India, concentrating it on what's happened with food prices because of advent of GST. GST rolled out in July 2017, promising to simplify the messy indirect tax system, push people and businesses to follow the rules, reduce tax evasion and make the economy run smoother. Post implementation of GST, numbers show better tax collection and a move towards a more formal economy. Still, the story around inflation especially for food gets messy and changes a lot from one region to another. The paper closely investigates at how GST has changed the way of movement of food prices, separating out unprocessed foods (which don't get taxed) from processed foods (which do). It unpacks the inflation that showed up during the transition— phase and all confusion over input tax credits. The research is a mix of analysis of existing data and digging into the new policy documents, with a special eye on places like Uttarakhand, where small food processors and informal shops are everywhere. The findings present a clear picture about the fact that, GST has helped making the economy more formal and globalised for the movement of goods to move between states. However, the low-income families and small food producers bore the brunt of the inflation in the short-run because of this tax reforms.

**Keywords:** Goods and Services Tax (GST), Food Inflation, Economic Growth, Processed Foods, Input Tax Credit, Informal Sector, Regional Disparities, Inclusive Growth

## Introduction

When India rolled out the Goods and Services Tax (GST) on July 1, 2017, it completely changed the country's indirect tax landscape. Suddenly, a mess of central and state taxes got pulled together into one system. The idea was simple: make taxes easier to handle, cut down the problem of taxes piling up on top of each other, and help India's markets work more smoothly as one big whole. People hoped that GST would stimulate the economy, accelerate the growth, and assist the government to raise more income. However, the situation becomes a lot more intricate as far as inflation is concerned (particularly food costs). The food prices are important in India as the National consumption statistics show that over 40 percent of the total household spending in India is on food and when the price of these products increases it impacts on the daily life and the overall economic situation. With GST, India had set different tax rates for different kinds of eatable items. Essential, unprocessed foods stayed tax-free, but processed and packaged foods started to get taxed. This shift didn't land the same way everywhere. The changes have rocked supply chains, increased consumer prices and put margins under strain to producers in some states, particularly those in which people are strongly dependent on farming or where the economy is weaker. The paper will dive into the effects that GST has had on inflation and economic growth in India with a narrow focus on what has happened to food prices. It examines the way GST

has changed the movement of prices in the economy, how various sectors have developed or failed, and why some regions have been more affected than others. There's a close look at what happened right after GST started, the bigger structural changes over time, and what all this means for food security and fair development across the country.

## Literature review

India's rollout of the Goods and Services Tax (GST) has sparked a wave of research into its impact on the economy and specific sectors. This literature review is a compilation of the findings that scholars and economists have made up-to-date, with a special focus on inflation, growth, and trends in food prices following the introduction of GST-

### a) GST's impact on inflation

After GST was introduced, Rudrani Bhattacharya of the National Institute of Public Finance and Policy (NIPFP) made a deep dig on inflation. She discovered that although GST was aimed at easing taxation and reducing the burden of cost cascading, it was not an easy process. Businesses faced compliance headaches and had to rewire their supply chains, which pushed prices up in the short run. Still, as the system settled, prices began to stabilize—especially in sectors that could really take advantage of input tax credits. Dr. Krishna C.P analysed the complicated multi-slab design of GST and

noticed fair bit of confusion caused by it. Both producers and consumers struggled to understand the sense of price changes, which harmed people's expectations and changed their expenditure pattern. The research also showcased that basic necessities mostly escaped the price hikes, due to tax exemptions. But processed food items could not get off so easy; higher tax rates among them and compliance requirements for the same lead to climbing up of the prices of these items.

### b) GST and Economic growth

Monti Kumar, explained "GST 2.0," by taking a close look at how GST is reshaping the broader economy. The writing notes that, despite the initial obstacles, GST has facilitated the ease of doing business across the state lines, has drawn more of the economy into the formal sector and increased the amount of tax revenues. The more modern framework including its emphasis on rationalizing tax slabs and employing digital compliance is an indication of a shift towards a more business-inclusive and friendly approach. GST has a long-term impact on growth with this, relying on the performance of the various sectors and regions. The manufacturing and logistical industry has largely

been a booming business in the new tax regime with fewer restrictions and easier interstate traffic. In the meantime, informal retailers and small food processors have not been able to keep up and particularly with the transition to digital compliance.

### c) Regional differences and food prices

Food inflation continues to cast a giant shadow in the GST period. Taxation is not fair to food, so the food items that are taxed such as the unprocessed grains are tax free and the other foods such as processed and packaged are taxed higher. This division has brought about economic disparity and territorial boundary. In the rural agriculture-intensive locations such as Uttarakhand, GST has increased the bad for small food producers, whereas larger entities in the supply chain get access to input credits. Researchers agree that GST's effect on food prices comes down to how efficiently supply chains operate, how taxes are passed along, and what people in different regions actually buy. The patchwork of tax rates and the lack of awareness among small vendors have only made inflation worse for the most vulnerable communities.

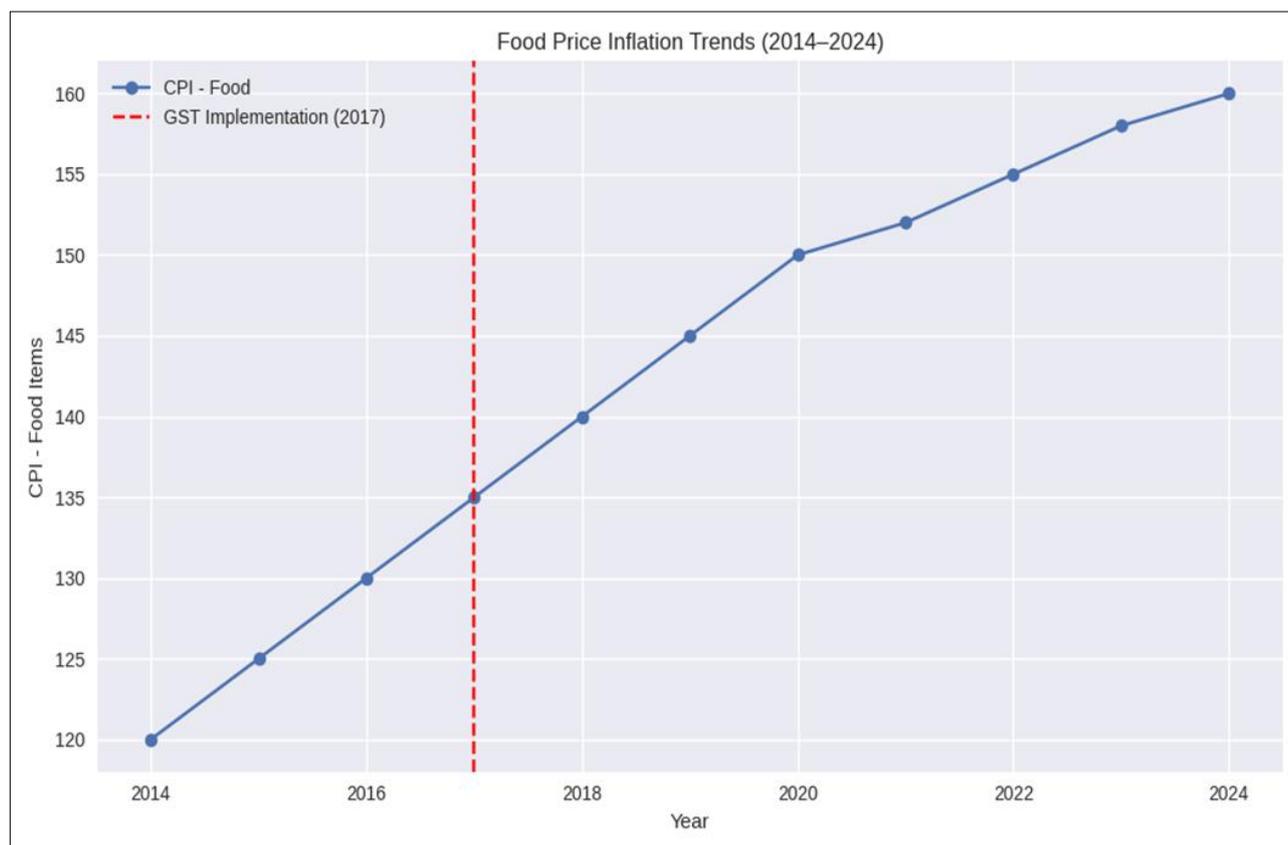


Fig 1: CPI before and after the introduction of GST

### Discussion

#### ▪ Food price inflation: sectoral shifts and transitional pressures

The rollout of the Goods and Services Tax (GST) in July 2017 marked a turning point in India's approach to taxing the food sector. Prior to GST, the tax on food was disjointed among states with combination of exemption and different rates. The new regime created a sharp contrast with the unprocessed fresh

produce including fruits, vegetables, and cereals being left out, and the processed and packaged foods being subject to the GST with tax rates between 5% and 18. This was not just a technical change but a complete transformation of the food pricing in India which resulted in inflationary pressure which was imbalanced in various food market segments.

This change is highlighted in the data of Figure 1. The Consumer Price Index (CPI) of the food rose slightly between

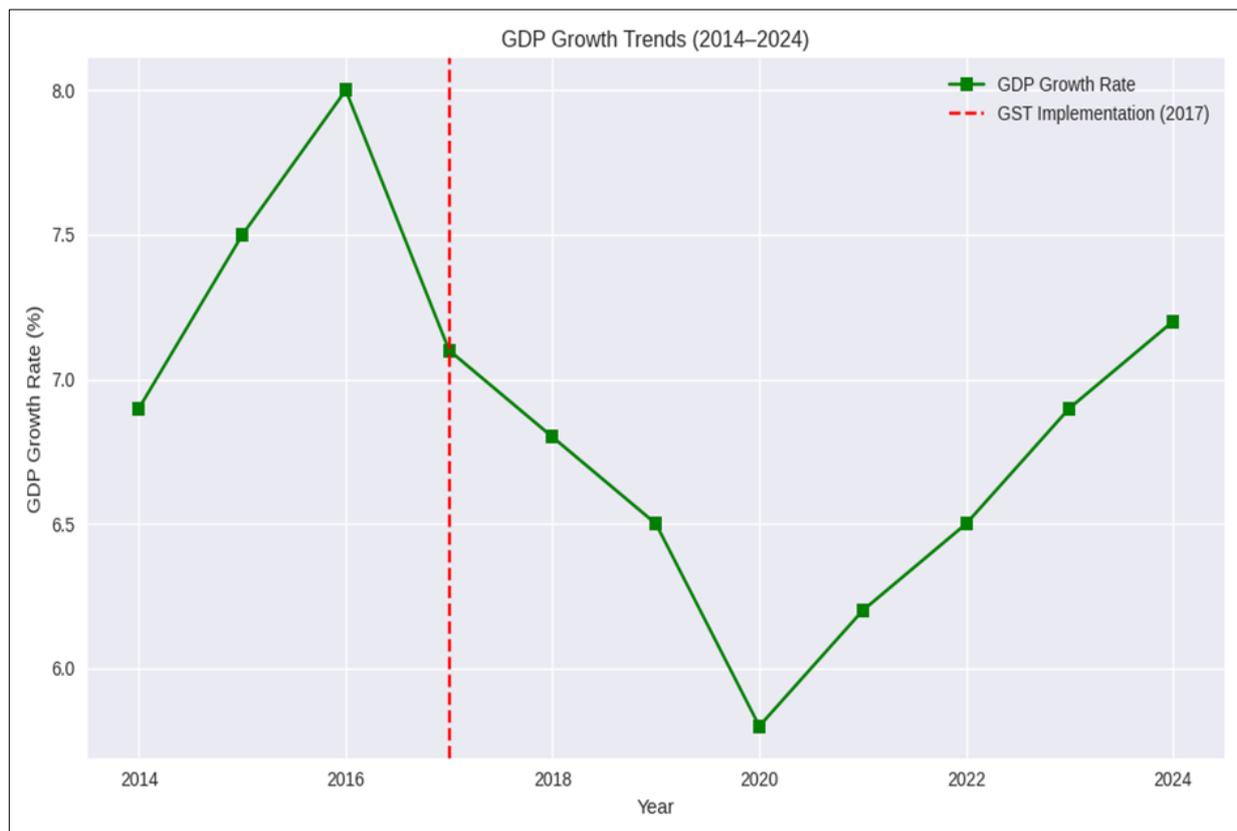
2014 and 2016, the increase is around 120 to 135, and it is principally determined by supply-side conditions, including changes in monsoon patterns, the cost of inputs, and transportation bottlenecks. Nevertheless, the rates of CPI started to grow faster after the introduction of GST in 2017 (with a significant inflection point in the graph), as the index increased to 140 in a comparatively brief time frame. This was not a statistical anomaly. Several structural forces were at play: businesses, facing higher compliance and logistics costs due to the new tax regime, passed these expenses on to consumers. Price increase had been particularly dramatic in the processed items such as foods, which are becoming more popular with city residents and aspiring middle-income families, and which also consume convenience foods as a staple.

Compounding the inflationary effect, many small and semi-formal food processors lacking the administrative capacity or knowledge to fully utilize input tax credits found themselves squeezed. Unlike the big players who may have the advantage of streamlining and claiming credit on tax compliance, these small players end up bearing the burden of cascading taxes, which further increases the end-consumer prices. Although,

following the initial turbulence of GST, supply chains became more flexible to new system and the world settled after 2018, food CPI was still heading in the same way to the top, to 160 by end of 2024. Such rising pressure in prices particularly in the value added and packaged food areas is resonant with the results of Bhattacharya and Gupta (2020) <sup>[1]</sup> who emphasize that the inflationary effect of GST was not uniform across all sectors but was rather greater in locations where value addition was facilitated by processing and packaging.

▪ **GDP growth: formalization gains in the face of transitional frictions**

The introduction of GST was projected to create a driver in economic growth by acting as a unifier of the national market, improving tax collection and eradicating within the Indian economy, internal trade barriers that had previously disproportionately divide the economy. Such reforms theoretically should enhance investment, efficiency and productivity. In practice, however, the post implementation period was aftermath was marked by turbulence and adjustment costs.



**Fig 2:** GDP Growth prior and post implementation of GST

As depicted in Figure 2, India's GDP growth rate held steady at a robust 7.5–8% from 2014 to 2016. However, the growth experienced in the short run after the implementation of GST recorded at 6.5%. This short-term slowdown was not unexpected: as businesses, anticipating the change, depleted inventories; supply chains particularly those dominated by informal networks in food retail and small-scale processing were temporarily disrupted; and small enterprises struggled to

adapt to the digitalized, documentation of GST compliance system.

Despite these teething troubles, the economy rebounded after 2018. By 2024, GDP growth had recovered to 7.2%. There were various factors that supported this recovery. The harmonization of the taxation rates and the abolition of the inter-state border controls resulted in the improved logistics and acceleration of goods delivery. The growth in the size of

the tax base and increased formalization implied an increase in government revenues that led to increased government investment in infrastructure and services. More importantly more businesses became incorporated into the formal economy thus they had access to credit, technology, and practices that add to productivity.

Nonetheless, the recovery was not evenly distributed across all sectors. The bigger and better-endowed firms had an easier time adapting, whereas the smaller and informal enterprises, in particular those related to food, had to face compliance and competition-related issues. The extent of the long-term benefits of GST is as Kumar *et al.* (2022) [4] note, determined by the adaptability of the various sectors and states. In the meantime, Sharma and Ranjan (2023) [5] warn that the informal sector still has a lot to overcome, and the benefits of formalization are not a simple freebie, especially to those food vendors and micro-processors who do not have the means to do the transition smoothly.

▪ **Regional and sectoral inequality: the example of Uttarakhand**

Not only has the effect of GST been sector specific, but also regional. The disproportionateness of the transition is seen in such states as Uttarakhand, where agriculture prevails and food retail is highly informal. Field level evidence in Udham Singh Nagar district is a graphic vision: small scale food processing enterprises were experiencing an increase in input prices, much of which was due to the fact that they were poorly armed to deal with the intricacies of input tax credits. Some of them did not have a digital infrastructure or could not understand taxes, and it became hard to eligibility to get credits and fulfill new reporting demands. This made them prone to shouldering greater costs and this was then transferred to the consumers through them or in some instances obliged to leave the market completely due to losses. Informal vendors, already operating on thin margins, found themselves excluded from formal supply chains as large, GST-compliant players consolidated their positions. The knock-on effect for consumers was significant: the price of packaged staples such as flour, pulses, and dairy products rose, squeezing household budgets and, for many low-income families, threatening food security. These pressures were even stronger in the areas where the penetration into the digital world is limited and the level of financial inclusion is low.

Singh and Mehta (2023) [6] argue that while GST has undoubtedly improved efficiency and scale for big processors and organized retailers, it has simultaneously increased the vulnerability of micro-enterprises, which lack the buffers and capabilities to compete in the new environment. Joshi (2022) [3] adds that persistent gaps in digital infrastructure and tax awareness had compounded compliance challenges in states like Uttarakhand, increasing regional disparities and deepening rural-urban divides. Such findings imply that a unitary strategy of implementing GST is not sufficient. The policymakers have to deal with the fact that standardized rates and compliance laws fail to address diversity of regional economies and

business models. It is urgently necessary to adjust the GST rates on processed foods (especially the staple ones), invest in digital and tax literacy courses among small businesses, and develop targeted solutions, including transitional subsidies or simplified credit resources, to processes and vendors in the most vulnerable regions.

**Synthesis**

The introduction of GST has cut across the food industry of India and the economy as a whole in two ways. On the one hand, it has brought in more structure, transparency, and efficiency, and simplified logistics and increased government revenues. Formalization of business operations has helped open channels of improved credit and output to numerous companies and the country has experienced more integration in the market than ever before. On the other hand, these gains have come at a cost—one disproportionately borne by small producers, informal vendors, and low-income consumers. The inflationary releases of GST have been greatest in the value added food segments where compliance costs and tax pass-through to consumer are greatest. Although a positive change towards formalization is positive at the aggregate level, it has left behind a large footprint in micro-enterprises, particularly in areas that have either weak digital infrastructure and tax literacy. Regional disparities have widened, with states like Uttarakhand started facing unique challenges that national policy has yet to fully address. If GST is to fulfil its promise as a driver of inclusive growth and food security, policy frameworks must become more responsive and adaptable. It includes identifying and dealing with the unique barriers to compliance faced by small and informal businesses, investing in the basic requirements of compliance, and how the taxation system does not integrity act as a financial benefit to those who need food the most. It is only through this refined and balanced approach that the transformative potential of GST can be optimally achieved to all the sections of the Indian society.

**Conclusion**

With the implementation of GST, there was a watershed in the way Indians were viewing indirect taxation, and this was basically a massive transformation to the system whose main objectives were to simplify the indirect taxation system and integrate the national markets. GST was seen to enhance compliance, mitigate cascading taxes and create a smooth movement of goods and services throughout India by unifying a patchwork of state and central taxation. The paper has taken a keen interest in the impact that GST has had on the rate of inflation and economic growth with a view of narrowing down into the food industry which is a field that is highly connected with economic stability and social equity. During the short-term aftermath of the GST introduction, the observed price increase was evident among consumers, especially of processed and packaged food. This spike was also due to the higher tax regime of the value-added items, combined with the lack of clarity in the transitional period, which disproportionately affected urban population and poor

households, which rely on these types of foods as their daily staple food. Even though the basic staple foods like fresh grains and produce were not to be taxed, the fixed tax on processed food was large enough to change the consumption pattern and burden the family budgets. In the long-term, the headline inflation subsided since the market took the initial shocks and the supply chains adapted. Nevertheless, the inflationary effect still lingered in certain areas of food markets where some of the processed products never returned to the pre-GST prices level-creating persistent fears about the cost of food and food security in nutrition in some of the weak populations.

In economic growth front, GST did manage to formalize large parts of the economy, make interstate trade more efficient, and increase the amount of revenue that is collected by the government. Businesses operating across state borders benefited from reduced logistical barriers and standardized compliance procedures, which in turn encouraged investment and efficiency. Nevertheless, the gains were not evenly distributed. Small-scale food vendors and micro-enterprises such as those prevalent in rural Uttarakhand or among tribal communities faced steep hurdles in adapting to digital compliance norms and navigating the complexities of input tax credits. Others did not have the infrastructure or literacy to fully benefit through new system and this led to their partial marginalization in the formalization benefits of GST. This imbalanced effect has brought into focus the confines of the homogenous tax system in a nation as socioeconomically stratified as India, where the local realities drastically differ with the national policy presumption. After all, although GST has made such efforts in the direction of its overall goals, the food industry experience indicates that further improvement is necessary. Rigidity of the system has increased the problem of inequalities at times or induced new problems, especially to the least prepared ones. To achieve the GST regime that India actually needs to help it pursue inclusive growth, affordability of food and nutritional well-being, the tax design would need to be made more receptive, malleable, and sensitive to on-the-ground realities.

### Recommendations

The multifaceted policy response is justified to overcome the identified challenges and make the growth broad-based and inflation within control:

- **Adjust GST slabs for essential processed foods:** It is important to re-consider the classification of processed food in the GST scheme. The food items that are rich in nutrients like fortified food grains, dairy products, and pulses should be transferred to the lower tax bracket to relieve the household food burden and achieve the overall health goals of the population.
- **Make input tax credits easier:** To make GST really advantageous to the small players in the food industry, input tax credit claiming process should be greatly streamlined. Micro and small enterprises can be given power to abide by the rules without overloading their administrative machinery by reducing bureaucratic complexity, offering customized digital solutions, and offering practical and language-relevant training. Ease of get-in by simplified processes and easy to use digital

interfaces would reduce the entry barriers into the formal sector and foster the inclusion of more people as well as mitigating the risk of informality.

- **Build regional strength and awareness:** Given this cultural diversity of the regions of India, GST ought to be complemented with specific literacy and outreach campaigns particularly in regions where smallholder food producers are highly concentrated or where marginalized communities are densely concentrated. Partnership with state governments would potentially provide region-specific assistance with compliance, including special local issues like poor internet connectivity or a low level of financial literacy. These would not only enhance the compliance rates but also create a feeling of ownership and faith to the system.

To conclude, what GST has accomplished in the process has shown its transformative potential and its shortfalls. A more subtle, all-embracing, and evidence-based policy, based on the realities of the Indian food producers and consumers, can make sure that GST can be used as an instrument of fair growth and food security, and not a cause of the unintended misery.

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