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Impact of GS Ton Inflation

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Key Words:- Introduction, Impact of GST on industry, Inflation rate in India, Impact of GST on Indian Economy, Positive Aspects of GST, Negative Aspects of GST, High selective tax incidence suppress demand for certain industry, Leads to fragmented markets and promoted inefficient production distribution, Demonetization, Impact on the Economy, Effects on government finances, Conclusion, References.

Introduction

As the world economy slows, and increasing financial volatility and turbulence become the "newest normal," only a few economies have the resilience to be a refuge of stability and the Potential to be an outpost of opportunity. India is one of those few. As oil and commodity prices Continue to be soft, and in the wake of actions taken by the government and the Reserve Bank of India, macro-economic stability seems reasonably assured for India. This bedrock of stability coupled with reforms to unleash the entrepreneurial energies of India can create the policy credibility and business environment that India is indeed seizing the historic opportunity afforded by domestic and international developments to propel the economy to a high growth trajectory.

Key amongst these reforms is the goods and services tax (GST), which has, in some ways, been "Priced" into expectations of the government's reform program.

The Union Budget 2007-08 announced that India should move towards a national level GST by April 1, 2010, and an Empowered Committee of State Ministries with Central Government would prepare a roadmap for the introduction of GST in India. Accordingly, the Government of India. The proposed GST Structure keeps liquor and petroleum products out of the purview of GST.

Regarding applicability of GST on natural gas, decision will be taken in course of time. Excise duty, presently levied by the states shall not be affected. Tobacco products shall be subject to GST with input tax credit. Centre shall be allowed to levy state excise duty over GST on tobacco products. GST shall be levied on imported goods and services by centre. Input tax credit shall be available and tax revenue shall go to the state based on following destination principle. Existing central excise/sales tax concession scheme in the special area is likely to continue. Various schemes if needed shall be converted into cash refund scheme so that chain on input tax credit is not disturbed. Rate of GST shall be prescribed in due course of time. It is expected to be revenue neutral.

The Indian GST is expected to represent a leap forward in creating a much cleaner dual VAT which would minimize the disadvantages of completely independent and completely centralized systems. A common base and common rates (across goods and services) and very similar rates (across States and between Centre and States) will facilitate administration and improve compliance while also rendering manageable the collection of taxes on inter-state sales.

Impact of GST on industry

Manufacturing sector in India is one of the highly taxed sectors in the world. A complex and high taxation structure has the tendency to render products uncompetitive in the international market or eats up large portions of the cost arbitrage available in manufacturing set-ups in low cost economies such as India. For instance, the manufacturing cost of most products in India is nearly half than in the west. But, the incidence of multistage taxation i.e. customs duty on imports, central excise duty on manufacture, central sales tax (CST) / value added tax (VAT) on sale of goods, service tax on provision of services and levies such as entry tax, octroi and cess by the State or local municipal corporations and related costs such as loss of tax credit, compliance and litigation cost chip away this advantage to the extent of almost 50 per cent.

Inflation rate in India

The annualized inflation rate in India was 3.78% as of August 2015, as per the Indian Ministry of Statistics and Programme Implementation. This represents a modest reduction from the previous annual figure of 9.6% for June 2011. Inflation rates in India are usually quoted as changes in the Wholesale Price Index (WPI), for all commodities.1) Many developing countries use changes in the consumer price index (CPI) as their central measure of inflation. India used WPI as the measure for inflation but new CPI(combined) is declared as the new standard for measuring inflation (April 2014) CPI numbers are typically measured monthly, and with a significant lag, making them unsuitable for policy use. India uses changes in the Consumer Price Index (CPI) to measure its rate of inflation.

Provisional annual inflation rate based on all India general CPI (Combined) for November 2013 on point to point basis (November 2013 over November 2012) is 11.24% as compared to 10.17% (final) for the previous month of October 2013. The corresponding provisional inflation rates for rural and urban areas for November 2013 are 11.74% and 10.53% respectively. Inflation rates (final) for rural and urban areas for October 2013 are 10.19% and 10.20% respectively.

Supply factors [edit]

The supply side inflation is a key ingredient for the rising inflation in India. The agricultural scarcity or the damage in transit creates a scarcity causing high inflationary pressures. Similarly, the high cost of labor eventually increases the production cost and leads to a high price for the commodity. The energies issues regarding the cost of production often increases the value of the final output produced. These supply driven factors have basically had a fiscal tool for regulation and moderation. Further, the global level impacts of price rise often impacts inflation from the supply side of the economy.

Consensus on the prime reason for the sticky and stubbornly high Consumer Price Index, that is retail inflation of India, is due to supply side constraints; and still where interest rate remains the only tool with The Reserve Bank of India.[8] Higher inflation rate also constraints India's manufacturing environment. (2

Domestic factors [edit]

Developing economies like India have generally a lesser developed financial market which creates a weak bonding between the interest rates and the aggregate demand. This accounts for the real money gap that could be determined as the potential determinant for the price rise and inflation in India. There is a gap in India for both the output and the real money gap. The supply of money grows rapidly while the supply of goods takes due time which causes increased inflation. Similarly Hoarding has been a problem of major concern in India where onions prices have shot high in the sky. There are several other stances for the gold and silver commodities and their price hike. (3)

Impact of GST on Indian Economy

Like every coin has two sides; even GST will probably have its own Positives and negative impacts:

Positive Aspects of GST

1) The main reason to implement GST is to abolish the cascading effect on tax. A product on which excise duty is paid can also be liable to VAT. Suppose a product A is manufactured in a factory. As soon as it releases from factory, excise duty has to be paid to central government. When the product A is sold in same state then VAT has to be paid to the State Government. Also no credit on excise duty paid can be taken against output VAT. This is termed as cascading effect since double taxes is levied on same product.
2) GST will lead to more transparent and neutral manner to raise revenue.
3) Implementation of GST will help resolve various issues concerning taxation and logistics with regard to e-commerce business, which has been recording rapid growth in the country, says a study.
4) Simplified and cost saving system as procedural cost reduces due to uniform accounting for all types of taxes. Only three type of account; CGST, SGST & IGST have to be maintained. (4

Negative Aspects of GST

There are following negative aspects of Goods and Services Tax (GST):

1) Majority of dealers are not covered with the central excise but are only paying VAT in the state. Now all the VAT dealers will be required to pay Central Goods and Services Tax (CGST).
2) GST is referred as single taxation system in India but in reality it is a dual tax in which both state and centre collects separate tax on single transaction of sale & service. However GST has some negative aspect but at the end it will boost economy.

3) GST would impact negatively on the real estate market. It would add up to 8 percent to the cost of new homes and reduce demand by about 12 percent.

4) Service tax litigations have risen substantially in recent years and that may be because of the absence of a pan-India Goods and Services Tax (GST) regime that can potentially remove several ambiguities around indirect taxation, experts maintain.(5)

• Adverse effect on the competitiveness of indigenous goods and services because of the cascading effect

Because of the cascading effect due to multiple taxes the cost for production of service and goods shoots up and that will end up with decrease in profit on such products and services.

• High selective tax incidence suppresses demand for certain industry

There is over-lapping of tax base in the case of several taxes. This leads to significantly higher tax incidence on selected products and services, where VAT as well as excise/service tax is also levied on the same base value. Items like consumer products, white goods and Automobiles are taxed under VAT as well as Excise on the same sale price at a high tax rate (12.5% and 16% respectively + cascading tax on tax). The high tax incidence suppresses the demand for such goods/ services due to demand elasticity with resultant adverse impact on the growth of such sectors.

• Leads to fragmented markets and promoted inefficient production / Distribution

The taxes on Inter State movement of goods (CST& entry tax etc.) create tax barriers within India. It holds back India from becoming a single national market. The combined effect of CST and state VAT is reflected in fragmenting India into different state markets. Separate and independent taxation of goods and services under different legislations increases tax disputes. There is a strong interdependence of goods and services in the supply chain until any goods or service reaches ultimate consumer. The line between goods and services is getting blurred by the day such as in the case of intangibles, telecom and IT products it's difficult to decide whether charged under service tax rate or product tax rate.(6

Issues & Challenges in the Implementation of GST

Successful implementation of GST regime is a great challenge for Centre and States. Everybody in the political class agrees India must switch to the goods and services tax (GST) regime. Centre-state talks have been on for some time to fix GST's contours and modalities of implementation. Improving tax compliance, in turn, will boost state coffers, thereby reducing fiscal deficits and providing resources for social spending. Removal of tax multiplication will mean consumer friendly product pricing, benefiting individual of the country. Replacing the existing Indirect Tax Structure by entirely a new model would pose a series of challenges like – Classification of taxable and exempt goods and services and deciding GST rate in line with the International Standards, Preparing the administrative machinery for levy and collection of GST, Simplified tax structures with clarity of Points of Tax and Tax Credits, Creating consumer and

Supplier awareness before introduction of the new system, Attaining high technical standards for implementation of GST model with the help of information technology and thereby reducing transaction cost. The Recent Reports says that there are disagreements among states and Unions over formation of Council to monitor GST in all states and the role of Union Finance Minister to veto the proposals passed by Council by majority decision.(7

Demonetization: Impact on the Economy

There are potentially two ways in which the pre-demonetization money supply will stand altered in the new regime: one, there would be agents in the economy who are holding cash which they cannot explain and hence they cannot deposit in the banking system. This part of the currency will be extinguished since it would not be replaced in any manner. Second, the government might choose to replace only a part of the currency which was in circulation as cash. In the other words, the rest would be available only as electronic money. This could be a mechanism used to force a transition to cashless medium of exchange. The empirical extent of these two components will be unraveled only over the next six months. These two would have different effects on the economy in the short term and in the medium term, as will be explored below.

Turning to the effects of demonetization, the first major and sustained effect of demonetization would follow from the extent to which the currency is extinguished and what this currency was being used for. It is being assumed that all currency which will potentially be extinguished would be currency being used as a store of value in the first and second category of transactions in the table above. If this assumption is correct, then the impact of extinguishing this currency would be limited. On the other hand, if the currency is used for any of the other transactions in the economy, either as a store of value or more importantly, as a medium of exchange, then the impact on the economy and the agents in the economy could be substantial. If, for instance, the extinguished cash was used as a medium of exchange in financing unaccounted income generation or income in the informal sector, demonetization would result in these activities closing down and a corresponding reduction in the incomes and employment associated with these activities. (8)

Effects on government finances

The effects of demonetization on government finances can be divided into three categories: the impact through RBI's finances, the impact through taxes and the impact through credit available to finance deficits.

The RBI earns seigniorage through the printing of currency. In the demonetization, a part of the currency will be extinguished. For this part of the currency, the RBI can print the notes given the assets on its books, but there would be no takers. In other words, this part of the currency would be like new money that can be introduced into the economy and hence yields seigniorage to the RBI once again when released into circulation. RBI, however, cannot lend this to the government since that would involve additional liability buildup on its balance sheet. So, this currency can only be released when foreign exchange is being converted to rupees for instance and not sterilized thereafter. At this point there would accrue some dividends to the government as well. However, to the extent the government and the RBI seek to move the economy towards digital instruments, this option might not be exercised and the dividend might not accrue.(9

Conclusion

The government is likely to release a draft paper for a final discussion between the stakeholders by late October. The combined GST rate is being discussed by government. The rate is expected to be around 14-16 per cent. After the total GST rate is arrived at, the states and the Centre will decide on the CGST and SGST rates. Currently, services are taxed at 10 per cent and the combined indirect taxes on most goods are around 20 per cent. It is preferred every economy must adopt GST or VAT at national level to make their economy attractive for foreign investors. By implementing GST, the developing economy like India can achieve sustainable and balanced development.

The demonetization undertaken by the government is a large shock to the economy. The impact of the shock in the medium term is a function of how much of the currency will be replaced at the end of the replacement process and the extent to which currency in circulation is extinguished. While it has been argued that the cash that would be extinguished would be "black money" and hence, should be rightfully extinguished to set right the perverse incentive structure in the economy, this argument is based on impressions rather than on facts. While the facts are not available to anybody, it would be foolhardy to argue that this is the only possibility.

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