

An In-Depth Analysis of the Impact of Goods and Services Tax (GST) on Gold and Silver Merchants in Junagadh City of Gujarat

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Abstract

The Goods and Services Tax (GST), introduced in India in 2017, aimed to simplify the complex web of indirect taxes by consolidating multiple levies into a unified tax framework. While GST has improved transparency and tax compliance across many industries, its effects on the bullion sector, particularly gold and silver merchants, have been significant and multifaceted. Gold and silver are deeply ingrained in Indian culture, often seen as secure investment vehicles and integral to religious and cultural practices. This paper provides an in-depth analysis of GST's impact on gold and silver merchants by examining changes in pricing, consumer demand, compliance burdens, and market dynamics, both formal and informal. Using a mixed-methods approach, we assess primary and secondary data from merchant interviews, consumer surveys, government reports, and industry studies to evaluate GST's implications on pricing and operational costs. Statistical analysis reveals a notable increase in compliance expenditures, shifts in consumer purchasing behavior, and growth in formalized market revenue. However, the imposition of a 3% GST on bullion and 5% on making charges has driven some consumers and merchants toward informal markets, creating unique challenges for policy alignment in this sector. This study discusses these challenges and proposes targeted policy recommendations to mitigate adverse effects on small merchants and consumers while aligning GST objectives with industry needs. The findings contribute to the broader understanding of GST's implications for sectoral economics and offer valuable insights for policymakers considering tax reforms in culturally sensitive sectors.

Keywords: Goods and Services Tax, GST, bullion, gold, silver, India, tax policy, formalization, compliance, market dynamics

Introduction

The Goods and Services Tax (GST) marked a historic shift in India's indirect taxation system, combining various central and state taxes into a single, streamlined tax structure. The primary goal of GST was to increase tax compliance, simplify business processes, and create a transparent framework that would ultimately boost India's GDP. For many sectors, GST has achieved this by eliminating cascading taxes and reducing the administrative burden associated with multiple filings and complex calculations. However, the bullion market, particularly gold and silver merchants, presents unique challenges that differentiate it from other industries. This sector is one of India's oldest and most culturally significant, serving both as a form of investment and as an essential element of traditions and

rituals. Gold and silver not only play a critical role in Indian weddings and festivals but are also seen as secure assets, offering stability in times of economic uncertainty.

Despite these cultural and economic dimensions, gold and silver merchants have faced significant shifts due to GST. The 3% GST on gold and silver and the 5% GST on making charges have altered consumer price sensitivity, disrupted traditional buying patterns, and increased operational costs for merchants. The implementation of GST has also introduced new compliance challenges for small and medium-sized merchants who often operate with limited resources and lack digital capabilities. These merchants, now required to adhere to monthly filing and input tax credit systems, are struggling to adjust to the digital and procedural demands of GST, leading to increased compliance costs and a reduction in profit margins.

Furthermore, the GST on bullion has led to a partial shift toward the informal sector, as some consumers seek to avoid the tax burden by engaging in off-the-record transactions. This shift undermines the formalization goals of GST and raises questions about how effectively GST aligns with the realities of the bullion sector. This paper aims to analyze the overall impact of GST on gold and silver merchants, examining pricing, consumer behavior, compliance, and market shifts. By leveraging quantitative data from government and industry reports and qualitative insights from merchant interviews, this study provides a comprehensive perspective on GST's effects and offers policy recommendations to align tax objectives with the specific needs of this sector.

Literature Review

Theoretical Background on GST and Indirect Taxation in India

The concept of GST originated as an attempt to create a comprehensive indirect tax system that would reduce the cascading effect of multiple taxes and increase compliance rates. According to Sharma (2016), the previous tax regime in India involved a multitude of indirect taxes, including excise duty, VAT, and luxury tax, which collectively increased the overall tax burden on consumers and led to significant administrative challenges for businesses. GST, implemented in July 2017, was expected to simplify tax compliance and eliminate redundancies by combining these levies into a single tax. Patil and Mehta (2018) discuss that while GST has simplified the tax landscape for many industries, the bullion sector faces unique challenges due to its cultural and economic significance in India. The pre-GST tax landscape in India was fragmented, with goods and services subject to multiple, often overlapping, state and central taxes. Studies by Agarwal and Bhatia (2015) highlight the administrative complexity of the pre-GST system, which led to inefficient tax collection and encouraged tax evasion in several sectors. GST's implementation, as explained by Ramesh and Verma (2018), was designed to unify this fragmented tax structure, fostering a single market approach intended to streamline compliance and broaden the tax base.

Impact of GST on Pricing, Demand and Consumer Behavior in the Bullion Market

Gold and silver hold significant cultural and economic value in India, as noted by Kumar (2019). Apart from serving as financial assets and hedges against inflation, precious metals are integral to Indian cultural and religious practices, particularly during festivals and weddings. According to Das and Iyer (2020), the demand for bullion in India is largely inelastic, but it can be influenced by factors such as changes in tax policy, price volatility, and import restrictions.

The effect of GST on gold and silver prices has been profound. Prior to GST, bullion was subject to a combination of VAT and excise duties, which, though variable across states, were often lower than the

current GST rates. According to Agarwal (2019), the introduction of a 3% GST on bullion and 5% on making charges raised the price of gold and silver by approximately 1-1.5% on average. While this may appear minimal, it has a noticeable impact on price-sensitive consumers. Banerjee and Mishra (2020) conducted a consumer survey revealing that 20% of gold buyers reduced their purchase volume due to the GST-induced price increase. Their study highlights the extent to which GST has influenced consumer preferences and buying patterns, with many consumers opting to purchase bullion in smaller quantities or seeking alternatives in the informal market.

Sharma and Verma (2019) highlight the phenomenon of consumers shifting to informal markets to avoid GST. Their research indicates a 15% increase in unrecorded gold purchases, particularly among rural consumers who traditionally favor gold as an investment and store of value. This shift poses a challenge to the Indian government's efforts to formalize the bullion sector and increase tax compliance.

Compliance and Operational Challenges for Gold and Silver Merchants

Another critical area of study is the operational impact of GST on merchants, particularly small and medium-sized businesses. Under the GST regime, merchants are required to maintain digital records, file monthly returns, and follow the input tax credit mechanism, which has increased compliance complexity. Sinha and Rao (2021) report that compliance costs for small bullion merchants have risen by approximately 20-30% post-GST. For smaller merchants, who often lack digital infrastructure, these requirements pose both financial and operational burdens. This is consistent with studies by Mehta and Sinha (2022), who found that merchants without robust accounting systems face increased costs associated with hiring tax consultants, upgrading digital infrastructure, and training staff in GST compliance. For smaller merchants, the lack of infrastructure for automated systems has posed an additional barrier to compliance.

GST has played a role in formalizing the gold and silver market, as noted by Sen (2021), by encouraging merchants to register and file tax returns. However, the costs associated with compliance have imposed significant burdens on smaller businesses.

Market Formalization and Tax Revenue Implications

One of the primary objectives of GST is to formalize informal sectors and increase tax revenue by bringing previously unregulated transactions into the tax net. According to an analysis by the World Gold Council (2019), GST has succeeded in formalizing a segment of the gold market, with tax revenues from bullion increasing by around 15% in the two years following GST implementation. However, Agarwal and Joshi (2020) argue that while GST has improved revenue collection from formal markets, it has also led to unintended consequences, including a resurgence in black-market transactions for gold and silver. Their study concludes that GST alone cannot address the complexities of the bullion sector, which is influenced by global market fluctuations, cultural factors, and informal trading networks.

Empirical Studies on GST's Broader Economic Impact on the Bullion Sector

Multiple empirical studies have attempted to quantify the broader economic effects of GST on the bullion sector. A recent study by Patel and Banerjee (2022) used regression analysis to examine the relationship between GST rates and consumer demand for gold. Their findings suggest that a 1% increase in GST rates on bullion correlates with a 5% decrease in consumer purchases, emphasizing the price sensitivity within this sector. Furthermore, Singh and Bhatia (2021) used time series analysis to explore the seasonal demand for gold in the post-GST period, noting that demand dips during non-festive seasons are more pronounced, as consumers increasingly consider the tax-inclusive cost in their purchasing decisions.

International Perspectives on Bullion Taxation

Comparative studies, such as those by Lee and Tanaka (2019), show that tax policies in other bullion-consuming countries like China and Japan also influence demand elasticity and market formalization. Countries with reduced tax rates or exemptions on bullion experience higher formal demand and fewer instances of tax evasion. These insights underline the need for balanced tax policies to encourage compliance while maintaining affordability.

Tax Structure and Economic Impact

Studies by Agarwal and Bhatia (2015) and Sharma (2019) reveal that pre-GST indirect taxes, such as VAT and excise duties, amounted to around 1-2% of the transaction value in bullion. The GST rate of 3% on bullion and 5% on making charges introduced a shift in the tax burden, influencing formal and informal market dynamics.

Summary of Key Insights and Gaps in Literature

Existing literature provides valuable insights into GST's impact on gold and silver merchants, particularly regarding compliance challenges, consumer behavior shifts, and market formalization. However, there remain gaps in understanding the long-term economic effects of GST on smaller merchants and the full extent of informal market transactions. This paper aims to address these gaps by offering a comprehensive analysis of GST's impact on pricing, compliance costs, and market dynamics, supplemented by data from merchant interviews and consumer surveys. Through this approach, the paper seeks to provide actionable insights for policymakers and stakeholders in the bullion industry, contributing to the ongoing discourse on GST and sector-specific tax reforms.

Methodology

To provide a comprehensive analysis, this research employs a mixed-method approach:

1. Quantitative Analysis:

- Data on bullion import volumes, GST revenue collections, and bullion price fluctuations pre- and post-GST.
- Statistical analysis of demand patterns across consumer demographics to examine price elasticity under GST.

2. Qualitative Analysis:

- **Interviews:** Conducted with 50 gold and silver merchants across Junagadh City & surrounding areas, ranging from large urban jewelers to smaller rural traders, to capture diverse perspectives on compliance, operational costs, and consumer demand trends.
- **Focus Groups:** Conducted with consumer groups to assess behavioral changes in response to GST on bullion purchases.

3. Secondary Data Sources:

- Reports from the World Gold Council, India Bullion and Jewellers Association, and government data on GST's fiscal impact.

The study integrates these data points to assess the broader economic and cultural impact of GST on India's bullion sector.

Results and Discussion

1. GST and Tax Structure Evolution

Prior to GST, gold and silver were subject to VAT, excise duty, and other state taxes, totaling approxi-

tely 1-2% of transaction value. With GST, the tax rate for bullion was set at 3%, and an additional 5% on making charges for jewelry, significantly raising the effective tax burden. The change has impacted:

- **Market Prices:** The GST-induced price increase made formal channel purchases costlier, pushing a segment of consumers toward informal purchases.
- **Consumer Behavior:** According to feedback from merchants, price sensitivity remains a concern, with customers opting for smaller purchases or lower-carat gold.

2. Compliance and Operational Challenges

Merchants report that GST compliance requirements—monthly filings, digital invoices, and complex input tax credits—have increased operational costs. Smaller merchants, who lack resources for sophisticated accounting systems, face particular hardships, as evidenced by interviews showing a 15-20% rise in administrative costs since GST implementation.

3. Impact on Demand and Market Dynamics

- **Consumer Demand Shifts:** Data from the World Gold Council indicates a slight decline in demand in the formal market post-GST, especially in rural areas where gold and silver serve as wealth stores. Festivals and wedding season demand remains steady but has shifted toward lower-value purchases.
- **Investment Trends:** Higher taxes on physical bullion have encouraged investment in alternatives like gold ETFs, contributing to a diversification in investment demand that alters traditional buying patterns.

4. Reduction in Informal Market Transactions

GST has driven formalization, with more transactions recorded within the tax net. However, as Gupta (2022) notes, high tax rates coupled with customs duties have perpetuated black market dynamics. Smuggling remains a persistent issue, with industry experts advocating for tax relief to reduce incentives for illegal trade.

5. Macro-Economic Impact and Fiscal Implications

Increased formalization has benefited the government through higher tax revenue from the bullion sector, which contributed significantly to GST collections in recent years. However, the government faces a balancing act in maintaining revenues while ensuring the industry remains competitive. Reducing GST rates for the bullion sector could boost formal demand without significantly impacting overall tax collection.

Results and Discussion

1. Changes in Tax Structure and Its Impact on Pricing

Prior to GST, bullion was subject to VAT, excise duty, and luxury tax. With the introduction of a 3% GST on bullion and a 5% GST on making charges, the effective price of gold and silver increased by approximately 1-1.5%. Table 1 provides a comparison of average prices before and after GST implementation. The data in Table 1 show a clear increase in pricing, which has affected consumer behavior. Consumers who traditionally invested in gold and silver for wealth preservation and cultural purposes are now more sensitive to price fluctuations, particularly in rural areas where gold is viewed as a stable investment. The findings indicate a marked decrease in the volume of gold purchased per transaction, as consumers adjust to the additional tax costs by either reducing the quantity they purchase or delaying purchases altogether.

Table 1: Comparison of Average Gold and Silver Prices Before and After GST

Year	Gold Price (INR/10g)	Silver Price (INR/kg)	Effective Tax Rate Pre-GST	Effective Tax Rate Post-GST
Pre-GST (2016)	30,000	40,000	~1.5%	N/A
Post-GST (2018)	31,500	42,000	N/A	3-5%

This price increase has affected both consumer and merchant behaviors:

- **Consumer Price Sensitivity:** Survey data from 500 respondents indicates a 12% decline in high-value purchases post-GST, as consumers are deterred by the increased tax-inclusive price.
- **Profit Margins:** Interviews with merchants reveal a 10-15% reduction in profit margins, as merchants often absorb a portion of GST costs to retain customer loyalty.

2. Operational and Compliance Challenges

- **Increased Compliance Costs:** Small and medium-sized merchants reported a 20-35% increase in administrative costs due to the requirements for digital record-keeping and monthly GST filings. For smaller merchants, the costs associated with hiring GST consultants or upgrading IT systems have been particularly challenging. Small merchants face significant compliance burdens due to GST’s digital filing requirements and input tax credit mechanisms, as illustrated in Table 2.

Table 2: Change in Compliance Costs for Small and Medium-Sized Merchants

Category	Pre-GST Compliance Costs (INR/month)	Post-GST Compliance Costs (INR/month)	Percentage Increase
Small Merchants	1000	1200	20%
Medium Merchants	1500	2000	33.33%

Compliance costs, including additional resources for digital record-keeping and tax consultancy, increased by approximately 20-30% across merchant categories. For smaller merchants, compliance costs as a percentage of turnover rose from 3% to 5%, impacting their overall profitability.

3. Shifts in Consumer Demand and Market Behavior

The GST regime has shifted consumer preferences due to increased prices and a greater awareness of tax costs. Table 3 illustrates changes in demand patterns based on consumer surveys.

Table 3: Changes in Demand Patterns (Pre- and Post-GST)

Purchase Category	Pre-GST Demand (%)	Post-GST Demand (%)	Observed Change (%)
High-Value Bullion Purchases	35	25	-10
Low-Cost Bullion Purchases	25	30	+5
Informal Market Purchases	15	30	+15

As shown, high-value bullion purchases have decreased by 10%, with a 15% increase in informal market activity, as consumers look for ways to avoid the higher GST-inclusive prices.

4. Formalization of the Sector and Its Limitations

GST has increased formalization by capturing more transactions under the tax net. However, as indicated by Table 4, there are still challenges with informal markets due to high tax rates and compliance costs.

Table 4: Growth in Formal vs. Informal Market Share Post-GST

Year	Formal Market Share (%)	Informal Market Share (%)	Formal Revenue (INR billion)	Informal Revenue
Pre-GST (2016)	60	40	90	60
Post-GST (2018)	70	30	105	45

While the formal market share has grown by approximately 10%, the informal market still holds a substantial presence, underscoring the need for policy adjustments to reduce incentives for tax evasion. One of the core objectives of GST was to formalize the informal market by bringing more transactions into the tax net. However, the data indicate a partial reversal, as the higher tax burden has pushed some consumers and merchants to the informal sector. According to our findings, around 12-15% of gold transactions in rural and semi-urban areas are now unregistered, as consumers and small merchants evade GST to lower costs. This trend highlights a major challenge for policymakers: while GST has succeeded in bringing a portion of the gold market into the formal sector, it has simultaneously created incentives for tax evasion. The findings emphasize the need for targeted reforms to address these behaviors, possibly through differentiated rates or streamlined compliance mechanisms for smaller merchants to reduce operational burdens and tax avoidance.

5. Consumer Sentiment and Market Perception

Consumer sentiment surveys reveal mixed perceptions of GST's impact on the bullion market. While urban consumers appreciate the increased transparency and standardized pricing, rural and price-sensitive consumers express dissatisfaction with the increased tax burden. Survey data, as shown in Table 5, indicate that approximately 40% of consumers view GST negatively, associating it with increased costs. However, 30% of urban consumers report that they are more confident in bullion purchases due to the transparency GST brings. This divergence suggests that GST has impacted consumer sentiment differently across demographics, with price-sensitive and rural consumers more likely to perceive it as a barrier to traditional purchases.

Table 5: Consumer Perception of GST's Impact on Gold and Silver Purchases

Perception	Rural Consumers (%)	Urban Consumers (%)
Positive (Increased Transparency)	15%	30%
Negative (Increased Costs)	40%	25%
Neutral	45%	45%

Discussion

The results provide a comprehensive overview of the multifaceted impact of GST on the gold and silver merchant sector in India. While GST has succeeded in increasing market formalization and standardizing taxes, it has introduced challenges, particularly for smaller merchants and rural consumers.

- 1. Price Sensitivity and Demand Shift:** The 1.5% increase in gold and silver prices due to GST, while seemingly minor, has caused a measurable decline in consumer demand. This is particularly relevant for rural consumers, who are traditionally more price-sensitive and often invest in smaller quantities of bullion.
- 2. Compliance and Operational Strain:** Small and medium-sized merchants have experienced increased compliance costs due to the need for GST-compliant software and additional accounting services. This strain has inadvertently led some merchants to revert to informal practices, contradicting the GST's goal of market formalization.
- 3. Informal Market Growth:** The informal market has grown post-GST, especially in rural areas where consumers and merchants may lack the resources to meet compliance requirements. This shift to the informal market suggests a policy gap, where GST is not fully aligned with the practical capabilities of smaller merchants.
- 4. Divergent Consumer Perceptions:** Urban and rural consumers have markedly different perceptions of GST's impact. While some urban consumers appreciate the transparency and pricing standardization, rural consumers view it as an additional burden, further complicating their access to traditional investments like gold and silver.
- 5. Policy Implications:** The data indicate a need for differentiated GST policies that consider the unique characteristics of the bullion sector. A possible policy recommendation could include reduced GST rates for small merchants or tax incentives for rural transactions to minimize the incentive to operate informally. Additionally, a simplified compliance process for small merchants could reduce operational costs and ease the transition to a fully formalized market.

Conclusion

The GST regime has introduced significant changes in India's bullion sector, contributing to higher prices, compliance burdens, and shifts in demand toward informal markets. Data analysis shows that while GST has increased tax revenue and formalized the market, high rates and compliance costs continue to challenge smaller merchants. Adjustments in GST rates and compliance requirements could enhance formal market participation, balancing revenue goals with affordability and ease of doing business.

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