

GST and Investor Behavior How Tax Reforms Influence Risk Preferences

**Could Also Be Included As A Sub-Topic For
“Behavioral Responses to GST Changes: A Study on Investor Sentiment”**

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1. INTRODUCTION

The GST changed consumer choices, company practices, and investment decisions, changing the economy. Tax laws affect investor psychology, risk appetite, and investment allocation. Investors consider tax policies based on market stability, after-tax profitability, and economic stability (Paul & Basu, 2024). Capital assets available in India's capital markets include debt instruments, equities securities, mutual fund units, derivatives, and alternative investments. The Reserve Bank of India and the Securities and Exchange Board of India manage financial markets to finance firms and create wealth for people, boosting economic development. Capital market taxes affect investor behaviour, portfolio selection, and market efficiency. This study analyses how alternative tax regimes affect Indian stock market investment by studying market reactions (Kiruba & Chandra, 2023). This research examines how asset class tax rules affect regulatory movements, investment choices, economic development, capital creation, and market efficiency. GST impacts investor risk aversion, portfolio diversification, and discretionary income, according to this research. Policymakers must understand these processes to design tax regimes that encourage market participation, reduce risk-taking distortions, and boost financial system efficiency.

1.1. BACKGROUND OF THE STUDY

1.1.1 Overview of GST: Global and Indian Perspectives

India's indirect tax structure has changed since GST was implemented. The GST is a nationwide indirect tax system that unifies taxes. The GST, which went into effect on July 1, 2017, unified various indirect taxes (Patnaik & Ramanjaneyulu, 2023). The charges included VAT, sales, and service taxes. It merged federal and state indirect taxes to establish a consistent national tax framework. GST was intended to improve revenue collection, eliminate tax evasion, and simplify business. GST is a destination-based tax levied at the point of consumption, not origin. GST divides goods and services into four tax brackets: 5%, 12%, 18%, and 28%. The Goods and Services Tax (GST) has been modified multiple times to meet corporate and economic demands. The GST Council, the tax's governing body, has helped it evolve to work efficiently. However, GST concerns exist (Bhalla, Sharma, & Kaur, 2023). This paper examines India's GST's impact, development, problems, and possible effects.

1.1.2 Investor Behavior and Economic Reforms

Economic reforms refocus investors when market behaviours change, such as tax policy changes affecting market dynamics and financial market incentives. GST significantly impacted investor techniques due to its implications on discretionary income, market circumstances, and business financial performance (Garg, Narwal, & Kumar, 2023). Investors' risk preferences are affected by rebalancing their portfolios to accommodate for changing tax legislation. The Goods and Services Tax simplifies taxes, improving operational efficiency, but investors still modify their market view depending on price and industry availability. The GST

implementation is making investors hesitant due to higher administrative expenses and uncertainties. Well-structured tax reform enhances investor trust by boosting market transparency and reducing tax inefficiencies. The study examines how GST adoption affects investor attitude by examining risk perception, market evaluation, and investing habits. Policymakers must create tax regimes that ensure financial income, promote economic growth, and stabilise investment markets (Bhalla, Kaur, & Sharma, 2022).

1.1.3 Behavioral Finance: Key Concepts and Theories

Rather than depending on traditional economic reasoning for sensible investment decisions, behavioural finance examines how human cognitive limits and psychological biases influence these processes. Prospect theory, a fundamental concept in behavioural finance, illustrates how investors perceive gains and losses asymmetrically, with loss aversion indicating that people are more concerned about potential losses than about recovering lost funds (Kancharla, Das, Kumar, Sawarn, & Rai, n.d.). Market trends, as well as bubbles and collapses, are both driven by individuals' inherent tendency to conform to collective behaviour. Investors often exhibit high-risk conduct stemming from their excessive trust in their market knowledge. The behaviours of market participants and the anomalies in financial markets during and subsequent to the GST reform may be more effectively analysed using the framework of behavioural finance, which is grounded in psychological principles.

1.1.4 GST and Financial Markets: Empirical Studies

The effects of changes to the Goods and Services Tax on market liquidity, investor confidence, and sectoral performance are investigated using data from actual financial market research (James, 2021). Investors respond to changes in their tax payments and the higher expenditures of complying with the GST by altering their investment holdings, which generates initial price shocks, according to many studies. Analysts assessed the market's performance before and after the GST was implemented by monitoring stock movements and investment flows, providing evidence of changes in investor turnover and risk-adjusted behaviour (Singh & Singh, 2024). Empirical findings from research that do not significantly impact markets allow policymakers to create tax policies that foster financial growth and operational success while stabilising financial markets.

1.1.5 Risk Preferences and Market Volatility Post-Reforms

The implementation of the Goods and Services Tax (GST) alters investors' risk tolerance, leading to increased market volatility. The market increasingly becomes unpredictable over time owing to regulatory changes that affect various industries differently regarding compliance costs, compelling investors to reassess their risk tolerance (Anand & Kumari, 2023). In the follow-up periods, a notable reallocation of assets occurs as conservative investors choose stable assets, while risk-seeking traders capitalise on market opportunities to invest in volatile elements. The degree of market development, the precision of regulatory rule formulation, and the consistency of a stable economic environment are all variables that enhance market stability. By understanding these market dynamics, policymakers and financial

professionals are better positioned to anticipate market fluctuations, mitigate irrational speculation, and facilitate smooth economic transitions during policy changes (Bhattarai, Nguyen, & Nguyen, 2019).

1.2. RESEARCH PROBLEM

The Goods and Services Tax (GST) reform alters the dynamics of financial markets by affecting investor sentiment, risk appetite, and volatility. Although designed to simplify taxation systems, the implementation of GST often induces investor apprehension and results in alterations to their financial behaviours (Haron & Ayojimi, 2018). Analysts must assess the impact of these changes on investors' risk tolerance, diversification strategies, and investment choices. The existing research on investor conduct and financial reactions after the implementation of GST is inadequate. This study will use a behavioural finance perspective to investigate the impact of GST on risk management behaviours and market stability patterns, therefore addressing the existing knowledge gap.

1.3. SIGNIFICANCE OF THE STUDY

Policymakers, financial experts, and investors may benefit from the study's findings, which clarify the link between tax changes and market reaction patterns (Hoseini, 2020). Understanding the influence of GST on investors' risk preferences, market participation, and investment habits is critical for market design and tax policy development. This study uses behavioural finance ideas to improve investors' financial literacy, allowing them to make more informed decisions in the face of economic uncertainty. The report will help policymakers achieve a more efficient balance between tax efficiency and economic development by outlining measures for stabilising the financial system post-transition (Idrees, Alam, & Agarwal, 2019).

1.4 RESEARCH OBJECTIVES

- I. To evaluate how GST reforms affect investor sentiment throughout multiple financial sectors.
- II. To investigate the connection between economic transformations caused by GST and investor preferences for risk stakes.
- III. To analyse the fiscal policy connection that impacts investors to choose between high-risk and low-risk investment approaches.
- IV. To assess how market dynamics and investment choices change because of GST reforms.

1.5 RESEARCH QUESTIONS

- I. How do GST reforms impact investor sentiment across multiple financial sectors?
- II. What is the relationship between economic transformations caused by GST and investor preferences for risk-taking?

- III. How does fiscal policy influence investors' decisions to choose between high-risk and low-risk investment approaches?
- IV. How do market dynamics and investment choices change as a result of GST reforms?

1.6 SCOPE AND LIMITATIONS

The study examines the impact of GST on investment decisions, market volatility, and risk-taking behaviour among investors after the implementation of tax changes. An empirical study using financial data and behavioural finance theories assesses investor behaviour in stock markets, mutual funds, and other investment instruments. The reliance on secondary sources for data collecting constrains this study, since it fails to assess investors' real-time reactions to events (Islam, Ghani, Mahyudin, & Manickam, 2017). The methodology further examines exogenous variables such as global economic activity, legislative changes, and divisional market fluctuations that extend beyond the effects of GST. The research demonstrates substantial behavioural impacts on financial markets due to tax legislation, despite addressing particular limitations.

1.7 STRUCTURE OF THE THESIS

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CHAPTER 2: LITERATURE REVIEW

A deliberate approach towards lowering fiscal imbalances and establishing a stable environment in which the economy may run free and flourish is tax reform. By harmonising and rationalising trade processes and motivating investments, which results in higher revenues, tax policies significantly affect innovation (Ahmad & Stern, 1991; Dyreng et al., 2020; Gale & Samwick, 2014; Ngwaba & Azizi, 2019). Public or private sector companies contribute to fulfil the objectives of a tax policy or system (De Paepe & Dickinson, 2014; Long & Miller, 2017). Changes in taxes that enhance the design of companies affect their development, expansion, and running operations. Tax laws affect company investment decisions and strategies (Hassett & Hubbard, 2002; Higgins et al., 2015; Miles & Snow, 2003). By means of new technology, they helped to moderate the modernisation of company processes, thus reducing business taxes; they also paved the path for worldwide corporate development (Guziejewska et al., 2014; Masso et al., 2013).

Through better performance, businesses may directly help the economy by providing significant goods and services, hence increasing economic development and efficiency (Hines, 2017; Doner & Schneider, 2000; Jones-Smith et al., 2020). Ninety percent of world businesses are micro-, small-, or medium-sized businesses (MSMEs; Asian Development Bank Report, 2020; World Bank Report, 2021). Regarding sales, profitability, and productivity, they have more growth potential than large units (McKenzie & Woodruff, 2017). Comprising seven out of every ten occupations, they are the most job generators worldwide (UN Report, 2021; Harvie, 2008, 2015).

Research on the MSME sector has grown as it has expanded globally. MSMEs are particularly vulnerable to changes, mainly national tax reforms (Ocheni, 2015) given their small scale.

Following tax reform, the MSME sector has had varying effects in many different countries. After tax reform, Freudenberg et al. (2017) empirically showed that business companies—especially Australian small businesses—benefitted from cash flow increases. Revenue losses resulting from US tax rate fluctuations raised the tax load of businesses, according to Plesko and Toder (2013). The entrepreneurial activities of even small companies have had a major influence on tax developments concerning the generation and use of tax benefits (Cullen & Gordon, 2006). Following changes to the tax system, businesses from Malaysia and New Zealand found compliance problems (Buchan et al., 2012; Ramli et al., 2015.). MSME trade (A. K. Sinha et al., 2021), compliance behaviour, and costs (Inasius, 2019; Matarirano et al., 2019) were evaluated in relation to other tax policies. Over the effect of tax reform on company performance, policymakers, academic economists, and the government find themselves at a stand-still. Policymakers' focus has lately shifted from income generation to better business performance, which finally propels economic development (Greene, 2021; Hines, 2017).

CHAPTER 3: RESEARCH METHODOLOGY

3.1 Approach and Research Design

This qualitative study examining how the Goods and Services Tax (GST) affects investor behaviour and risk preferences uses secondary data. The study seeks to assess how changes in taxes affect general risk appetite, investment decision-making, and market sentiment. It is experimental in character. Reviewing current research, financial data, government policies, and expert opinions helps the study to understand investor behaviour after the GST application.

3.2 approaches of data sampling

Since this research is based on secondary qualitative data, deliberate sampling is used to choose pertinent sources that provide a whole understanding of the link between GST changes and investment behaviour. Included in the choosing process were scholarly journal studies on taxes and financial conduct.

publications from government agencies (e.g., Ministry of Finance, RBI) on tax changes and investment patterns; financial market research and economic surveys linked with the impact of GST on investor confidence; expert comments, policy evaluations, and case studies from industry publications and business magazines.

3.3 gathering of data

Published literature, economic reports, and policy papers among other secondary data sources form the basis of the research. Data is gathered from: government websites and tax records.

Financial institution, investment company, tax advisory body reports; research papers from financial magazines and economic think tanks

Case studies investigating how GST affects stock markets, mutual funds, and alternative investing strategies.

With consideration for their risk-taking behaviour, asset allocation preferences, and investment strategies in reaction to tax policy changes, a thematic analysis is done to find trends in investor reactions to GST revisions.

3.4 Ethical Viewpoint

Since this study depends only on secondary data, ethical issues include making sure that all sources are appropriately cited and referenced to preserve academic integrity. None of personal or sensitive information is utilised; all of the material comes from validated financial databases, studies, and freely accessible publications.

CHAPTER 4: IMPACT OF GST REFORMS ON INVESTOR SENTIMENT

4.1 Investor Attitude: Definition and Main Influences

Investor sentiment is the general attitude, feeling, and opinion of individuals on financial markets. Government policies, the state of the economy, and more general market movements all help to define it. The main forces influencing market mood include macroeconomic indicators (GDP growth, inflation, interest rates), regulatory changes (such as GST), company profitability, and worldwide economic events (John & Dhannur, 2019). Behavioural finance argues that, even if investors do not always behave logically, policy changes, risk perception, and market psychology shape them. One important overhaul in India that has rebuilt the indirect tax structure is the Goods and Services Tax (GST). This affected both sector-specific investment choices and market performance as well as investor confidence directly and indirectly.

4.2 Study of Market Trends Both Before and Following GST

Indian markets were erratic and opaque before GST was adopted in 2017, and investors worried about how it may affect various companies. Concerns about the tax load on companies, supply network interruptions, and compliance expenses drove short-term stock price swings Joy, Thomas, & Puthussery, 2020). Markets calmed slowly after GST as companies adapted to the new tax code. Several companies, notably FMCG, e-commerce, and logistics, gained from the streamlined tax structure, hence enhancing investor mood in these sectors. Conversely, industries including real estate and manufacturing saw early slowdowns because of rising tax demands and challenging compliance, therefore undermining investor confidence.

4.3 Reactions in Behaviour to Changing GST Rates.

Changes in taxes have a major effect on market liquidity and firm profitability, so investor behaviour is very sensitive to them. Depending on the asset type, the many tax slabs under GST affected investment choices differently (Khoja & Khan, 2020). Lowering GST rates on basic products and services raised customer demand, therefore improving stock performance in related companies. Conversely, more taxes led to a wary investor approach towards luxury goods, cars, and real estate. Stock market movements, portfolio adjustments, and changing investment selections have matched market responses to GST rate changes—cuts or increases.

4.4 Affect of Tax Policies on Sector-Specific Sentiment

- Depending on their tax structure and compliance load, various industries reacted differently to GST changes.
- Why GST enhanced logistics and lowered cascading taxes for the fast-moving consumer goods (FMCG) industry, therefore generating more investment?
- Reduced sales and higher GST rates initially compromised investor trust in the automotive industry. Still, later rate cut helped to rebuild confidence.
- GST raised under-construction property taxes, therefore slowing down the industry and discouraging investment (Mohanty, Mohapatra, Tripathy, & Matta, 2023).
- While GST had little direct influence on banking and financial services, financial organisations had to modify their pricing strategies, therefore influencing short-term mood.
- Retail and E-commerce: Reduced state-level taxes raised sector investor confidence.

4.5 Case Studies Reflecting Significant Market Events Driven by GST

First case study: response of the market towards the 2017 GST implementation.

When GST became active in July 2017, the stock market was erratic. First reluctant, investors caused brief declines in industries like real estate and manufacturing. Still, when companies adjusted over time the markets recovered (Nayak, Palai, Khatei, & Mallick, 2022).

Second example analysis: 2019 market reaction and GST rate cuts

In 2019 the government lowered GST rates on a range of consumer products, including cars, in order to increase demand. This represented changing investor mood, which raised stock values for FMCG and automotive firms.

Third case study: GST on virtual reality and cryptocurrency in 2022.

Different investors responded to the GST taxing of digital assets. Although some saw it as an effort for control, others believed it discouraged bitcoin purchases.

CHAPTER 5: GST AND INVESTOR RISK PREFERENCES

5.1 An outline of investment choice risk preferences.

In investing, risk preference is an investor's readiness to bear financial risks in order to maximise returns. Three usually separate investors: risk-averse, risk-neutral, and risk-seeking. While risk-seeking investors are willing to take on greater risks in exchange for maybe larger earnings, risk-averse investors prioritise capital protection and desire consistent returns. An investor's risk tolerance is largely influenced by laws on taxes, regulations, and market conditions (Nayaka & Panduranga, 2021). The introduction of GST (Goods and Services Tax) in India has had a major impact on investor mood, changing risk preferences as a consequence of rises in firm expenditures, compliance criteria, and overall market volatility.

5.2 GST Reform and Risk Appetite Changes

The introduction of GST in 2017 affected investor risk-taking behaviour by resulting both long-term structural benefits and short-term market turbulence. Market uncertainty first led to risk-averse behaviour as investors knew nothing about how tax cuts would affect individual companies (Panga, Malpani, & Malpani, 2018). But investor confidence rose as companies adapted to the new tax structure, thereby increasing risk-taking in sectors such logistics, FMCG, and e-commerce that would profit from GST.

Furthermore affecting risk appetite were changes in tax rates. Higher GST rates on luxury goods and real estate, for example, led to less investment in these sectors because investors thought the prices were higher and the demand was lower (Rani, Sonia, & Narwal, 2022). On the other hand, industries that saw tax cuts attracted more people as their profitability grew and investment grew as well (Renjith, 2021). Consequently, GST reforms produced a dynamic change in risk preferences as investors reallocated their portfolios based on tax advantages and sectors growth expectations.

5.3 Sectoral Examining of Risk Behaviour Following GST

Investor risk behaviour changed significantly across different sectors after GST came into effect.

Reduced tax rates and simplified supply chains helped the FMCG and consumer goods sectors to take more risks. Expecting higher consumer spending, investors put cash into FMCG companies (Sankar, 2017).

Why, then? Taxation on under-construction homes caused real estate market risk aversion to rise and investment to fall. Investors favoured less risk assets such known equities or bonds.

- Cars: First, higher tax rates discouraged investment; then, later tax cuts rebuilt confidence and changed risk preference.
- In banking and financial services, GST had minimal effect on risk preferences, therefore enabling investors to keep their present course.
- Eliminating indirect taxes produced more investment in technology and e-commerce companies.

This sector-specific variation in risk preferences shows how tax changes influence investment activity, thereby causing investors to rethink their risk tolerance in front of legal consequences.

5.4 Behavioural Preceptions and Investor Choice-Making

Behavioural finance studies how psychological prejudices affect decisions on investments. During the GST changes, many factors shaped investor risk preferences:

Originally negative about GST because of worries about growing expenditures and compliance, investors adopted cautious investment practices (Saran, 2018).

- Herd Mentality: Investors followed industry trends instead of making independent, data-driven assessments when markets reacted to GST, hence creating sector-specific bubbles.
- Overconfidence bias: Investors made speculative investments later on that were subsequently reversed after overestimating GST benefits in certain industries.

Knowing these prejudices helps one to understand why some investors were reluctant while others grabbed new prospects in the post-GST market (Sehrawat & Dhanda, 2015).

5.5 Diverse Portfolio Implications

As investors seek to balance risk and return, GST reforms have changed portfolio diversification strategies. Reallocating investment to tax-advantaged businesses, improving supply chain efficiency, and capitalising on growing consumer demand have been responses by investors to tax changes (Singh, Mohapatra, & Kalra, 2020). Due to GST's simplified tax structures, investors were more exposed to growth sectors including FMCG, logistics, and e-commerce; hence, they moved away from usually high-return industries like real estate and luxury goods.

To balance risk and lower sector-specific volatility, investors often combine equities, fixed-income instruments, and mutual funds under multi-asset strategies.

The introduction of GST had a significant impact on investor risk preferences; originally it caused caution but later it encouraged confidence in sectors orientated on growth. Tax reforms changed risk behaviour in many different fields, which made investors rethink their approach and shift to fit a new legal environment (Paul & Basu, 2024). Financial planners, legislators, and investors hoping to optimise portfolio variety and risk management in a post-GST economy must first understand these developments.

CHAPTER 6: MARKET VOLATILITY AND BEHAVIORAL PATTERNS

The Goods and Services Tax (GST) in India, one of the country's largest tax reforms, caused significant market volatility due to concerns about compliance costs, tax burdens, and sectoral effects. Short-term volatility was evident as indices like the Nifty 50 and Sensex moved in the weeks after the GST rollout (Kiruba & Chandra, 2023). Real estate, automobiles, and manufacturing witnessed early reductions due to greater tax rates and compliance concerns, while tax simplification helped industries like FMCG, logistics, and e-commerce. High trading volumes, speculative investments, and short-term sell-offs defining the transition period revealed investor worries about the impact of GST on company operations (Patnaik & Ramanjaneyulu, 2023).

Long-term and short-term patterns help examine market volatility after GST. Short-term volatility occurred during the first six months of GST implementation, with traders seeing notable intraday volatility. Market corrections took place in high-tax sectors like real estate and automobiles, leading to uncertainty and erratic market swings. Long-term volatility trends

decreased as companies raised their tax compliance and operations, and long-term investors favoured sectors with great compliance efficiency like FMCG, IT, and e-commerce (Bhalla, Sharma, & Kaur, 2023).

Market volatility is highly influenced by psychological aspects of investors and behavioral prejudices. The adoption of GST set off a range of psychological responses among investors that influenced their decision-making process. Herd mentality affected investors' early reactions to GST, leading to sector-wide overreactions marked by both despair and hope. Investors overstated GST's impact on growth sectors, leading to speculative FMCG and logistics equity investments and market falls in the next months (Garg, Narwal, & Kumar, 2023). Anchoring bias misinterpreted short-term volatility as a permanent decrease, leading to hesitant investment behavior and postponement of portfolio changes meant to provide long-term benefits.

CHAPTER 7: POLICY RECOMMENDATIONS AND PRACTICAL IMPLICATIONS

The implementation of GST has been a challenge due to the mismatch between tax policy goals and market expectations. To address this, governments must provide improved transparency, predictability, and consistency in tax policies. Structured feedback mechanisms, industry debates, and regular stakeholder involvement can help match tax rates to investor perspectives. Limiting the frequency of fluctuations in GST rates and compliance criteria will help lower financial market anxiety (Bhalla, Kaur, & Sharma, 2022). A long-term tax road map should be provided to businesses and investors to assist in financial management and risk analysis.

To boost investor confidence, policy consistency and open communication are essential. Clear and consistent tax policies can minimize regular GST changes, enhance investor risk assessment systems, and increase investor awareness of the long-term benefits of GST. Temporary tax cuts or incentives for high-impact industries can boost investor confidence and draw money to growth-oriented businesses. Reducing bureaucratic obstacles and improving GST compliance technology can also improve investor confidence and market participation.

GST should support economic stability and policies favorable for investors by balancing incentives for economic growth with tax income collecting (Kancharla, Das, Kumar, Sawarn, & Rai, n.d.). Recommendations include changing GST rates based on industry cycles, lightening small investor and company compliance load, and juggling monetary policies and GST.

Policymakers, investors, and authorities need to cooperate to ensure the effective application of GST reforms. Policymakers should keep constant GST rules, offer relief options tailored to each industry, strengthen mechanisms of tax dispute settlement, spread investments to lower market risk connected to GST, stay current with tax developments, prioritize long-term investment plans over reacting to GST-generated short-term volatility, increase transparency in taxation data sharing, monitor GST's impact on financial markets, and motivate tax compliance (James, 2021). By matching tax policies with economic stability goals and market expectations, GST improvements can help India's economic efficiency and investment confidence.

CHAPTER 8: CONCLUSION

A revolutionary tax reform, India's Goods and Services Tax (GST) significantly affected risk preferences, market volatility, and investor behaviour. Although simplifying the tax system was GST's primary goal, its impact on investment decisions and financial markets is very noteworthy. Initially, as investors reacted to changes in taxation rates across several sectors, GST generated short-term uncertainty and volatility. Market mood did, however, eventually settle, and companies which benefited from tax breaks—including FMCG, e-commerce, and logistics—saw rising investor confidence.

After GST, investor risk preferences altered; they shifted their portfolios to tax-efficient industries while reducing exposure to highly taxed companies such luxury goods and real estate. Market fluctuations are much influenced by behavioural biases like overconfidence, herd mentality, and loss aversion.

Policy stability, transparent taxation systems, and better investor awareness are needed if we are to properly benefit from GST. Improved regulatory collaboration, strategic tax changes, and incentives for high-impact businesses might all assist to raise investor confidence. GST has to be linked with economic stability and investment-friendly policies if India's evolving economy is to have long-term market growth and financial resilience.

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