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RESERVE BANK OF INDIA

वेबसाइट : www.rbi.org.in/hindi

Website : www.rbi.org.in

इ-मेल email: helpdoc@rbi.org.in

संचार विभाग, केंद्रीय कार्यालय, एस.बी.एस.मार्ग, मुंबई-400001

DEPARTMENT OF COMMUNICATION, Central Office, S.B.S.Marg, Mumbai-400001

फोन/Phone: 91 22 2266 0502 फैक्स/Fax: 91 22 22660358

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**RBI Working Paper Series 5:
Stability of Real Effective Exchange Rate Important for
Sustaining Growth of Industrial Production**

The Reserve Bank of India today placed on its website a Working Paper titled "[Impact of Real Exchange Rate Volatility on Use-Based Industrial Production in India](#)" under the Reserve Bank of India Working Paper Series*. This paper is authored by Alice Sebastian, Upasana Sharma, Thangzason Sonna and Dr. Himanshu Joshi.

The paper focuses on the impact of exchange rate volatility on industrial growth in the context of the increasing integration of India's industrial sector with global economy through higher export and import intensity. The paper also explores the implications of exchange rate volatility on the use based components of the index of industrial production (IIP) using EGARCH methodology for calculating volatility of real effective exchange rate (REER).

The empirical evidence for 36 country REER suggests that the adverse impact of REER volatility is uniformly evident in the use based sub-components of IIP, viz., basic, capital and intermediate goods, except for consumer goods. In case of 6 country REER, barring basic goods, the adverse impact of exchange rate volatility was visible in all other use based components of IIP. Magnitude-wise, with the exception of the large negative impact of REER volatility on capital goods, the impact on other use based industries is generally limited. These differences may be ascribed to the varying extent of the direction, quantum and composition of trade, competitiveness and the sufficiency of domestic demand. The implication of this finding is that the stability of REER is important for sustaining the growth of industrial production, underlining the need for appropriate management of volatility of both the nominal exchange rate and domestic inflation.

**The Reserve Bank of India introduced the RBI Working Papers series in March 2011. These papers present research in progress of the staff members of the Reserve Bank and are disseminated to elicit comments and further debate. The views expressed in these papers are those of authors and not of the Reserve Bank of India. Comments and observations may kindly be forwarded to authors. Citation and use of such papers should take into account its provisional character.*