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RBI Working Paper Series No. 4: Rules of the Monetary Game

The Reserve Bank of India placed on its website a Working Paper titled "[Rules of the Monetary Game](#)" under the Reserve Bank of India Working Paper Series*. The paper is authored by Dr. Prachi Mishra and Dr. Raghuram Rajan.

Aggressive monetary policy actions by one country can lead to significant adverse cross-border spillovers on others, especially as countries contend with the zero lower bound. If countries do not internalize these spillovers, they may undertake policies that are collectively suboptimal. Instead, countries could agree to guidelines for responsible behaviour that would improve collective outcomes. This paper puts forward some of the practical issues that need to be considered in framing possible rules of the monetary game. Policies could be broadly characterized and rated based on analytical inputs and discussion. Policies that generally have positive or domestic effects could be rated Green, policies that should be used temporarily and with care could be rated Orange, and policies that should be avoided at all times could be rated Red.

The paper provides a brief review of the some of the frameworks that have been used in the literature to assess spillovers, and makes the case that models may reflect the policy biases of those devising them, and may be at too early a stage to be able to draw strong conclusions from them. Therefore, while more empirical analysis should be undertaken, it should be seen as an input to a dialogue rather than definitive, with the analysis being refined as outcomes are better understood.

With economic analysis on the international spillovers from domestic policies still at an early stage, it is unlikely we will get strong policy prescriptions soon, let alone international agreement on them, especially given that a number of country authorities like central banks have explicit domestic mandates. The paper, therefore, suggests a period of focused discussion, first outside international meetings, then within international meetings. Such a discussion need not take place in an environment of finger pointing and defensiveness, but as an attempt to understand what can be reasonable, and not overly intrusive, rules of conduct. As consensus builds on the rules of conduct, we can contemplate the next step of whether to codify them through international agreement, see how the Articles of multilateral institutions like the IMF will have to be altered, and how country authorities will interpret or alter domestic mandates to incorporate international responsibilities.

** 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.*