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Best Exchange Rate Regime

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Abstract

There are around two hundred countries in the world. However, number of currencies circulated in the world is lesser than number of countries. It infers that no single currency is acceptable by all economies of the world. The evolution of the currency regime shows that world economy has adopted different types of currencies regime in different times. It varied from fixed to intermediate to floating exchange rate regime. The present study will deal with finding the solution of best currency for all economies. It finds that there is no single currency best for all economies for all times. It depends on trade cycle and economic structure.

Keywords: Exchange Rate, Regime, Economy.

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1. INTRODUCTION

The economic transaction across the border is dome on the basis of exchange rate regime influencing the economic growth and employment. This exchange rate regime is broadly subdivided into three parts namely fixed exchange rate, floating exchange rate and hybrid exchange rate that is combination crawling peg and managed floating. Government or monetary authority is the regulator of the fixed exchange rate regime while market is regulator in floating exchange rate regime. Hybrid exchange rate regime is regulated by both government and market. It has been shown in the Tble-1. Sometime this Exchange Rate Regime (ERR) also includes soft and hard exchange rate pegs. In the Soft Exchange rate regime, the exchange rate is determined by market but Central bank intervenes. In the Hard exchange rate regime, the central bank fixes the exchange rate.

Over the period the world economies have adopted different currencies and having different exchange rate regimes depending upon growth phase and economic structure. Therefore, one should analyse the advantages and disadvantages of exchange rate regimes followed by world economies.

2. Objectives

Objective of this study is to know the advantages of different currency regimes for policy implications to enhance the economic growth.

3. History of Global Exchange rate regime

It was pertinent in the history of Exchange rate regime that most of the countries moved away from the Silver and bimetallic exchange rate regime to gold standard by 1900 (Bordo, 2003).The Gold standard continued till 1944, the year of Bretton Woods Stable peg according to which many countries pegged their currencies in terms of USA dollar that was pegged in terms of gold with 2.5 per cent variation. It has been shown in the table-1.

Table.1. History of Exchange Rate Regime

Period	Exchange Rate Regime
1880 -1900	Silver and bimetallic
1900-1914	Gold standard, currency union and currency board
1914-1945	Gold Exchange standard, floats and managed floats currencies,
1946-1971	Bretton Woods Adjustable peg
1972-2000	Free floats, Crawling peg
2000-2020	Floating and managed floating
Source: **Bordo M.D. (2003),** "Exchange Rate Regime Choice in Historical perspective", IMF, Working Paper 03/160	

4. Literature reviews

The evolution of exchange rate regime has been shown in the table-1. It shows that there are different types of Exchange rate regimes. However, categorically they evolved around three types of regimes-fixed, intermediate and floating. Currency union and currency boards come under fixed exchange rate. Adjustable pegs, crawling pegs, basket pegs and bands come under intermediate regime. Managed floats and free floats come under floating exchange rate regime. **Milton Friedman (1953)** supported floating exchange rate that supports monetary independence and insulates from shocks. No single currency is best for all economies or for all times **(Frankel, 1999).**

5. Analysis

One should talk about advantages and disadvantages to know which currency regime is best. It depends of economic situation. It has been shown in table-2. This table clearly shows the advantages of currency regimes adopted by different economies. No single currency regime has been adopted by all economies. Therefore, one can say that no single exchange rate regime is good for all economies in the world.

Table.2. Countries in Different Exchange Rate Regimes

S.No.	Types of Exchange Rate Regime	Country	Remarks	Advantage and Disadvantage
1	No Separate Legal Tender	Ecuador, Monaco ,	No own currency Ecuador accepts USA Dollar, Salvador , Monaco accepts Euro	No control of domestic monetary authority on monetary policy
2	Currency Board	Dominica, Bulgaria	Domestic currency is pegged to a Foreign currency (Anchor Currency) at a fixed exchange rate. The circulated domestic currency is backed by its foreign reserve. Hongkong and USA follow this regime.	**Advantage:** Price stability , Credibility in the eye of international investors, Disadvantage: No government autonomy, NO lender of last resort
3	Conventional Peg	Saudi Arabia	Domestic currency value is fixed with another currency in which periodic or incremental adjustment is not permitted	Advantage: Facilitate trade, boosts real income Disadvantage: Domestic currency is deprived of purchasing power to buy foreign goods
4	Stabilised Arrangements	Iran, Singapore	Central bank intervenes with narrow band	Advantage: Low transaction cost with low inflation Disadvantage: Restricts nation to adjust economic change
5	Crawling Peg	Nicargua, Botswania	Domestic currency value is fixed with another currency in which periodic or incremental adjustment is permitted	Advantage: Regular adjustment to Changes Disadvantage: Increase vulnerability to speculative attack
6	Crawling Like arrangement	China, Vietnam	Domestic currency value is maintained with 2.00 per cent variation of last six months average exchange rate	Advantage: minimises volatility of exchange rate Disadvantage: No effective to shock
7	Pegged	Morocco	Exchange rate is fixed with	Advantage: Low

	Exchange rate within Horizontal bands		± 1.00 per cent variation	exchange rate Disadvantage: Low purchasing power
8	Floating	Belarus, Yemen	Domestic currency value fluctuates around a fixed value of exchange rate	Advantage: Currency trade without restriction Disadvantage: Highly volatile
9	Free Floating	Russia, UK	Known by Clean float. Currency value is determined by market	Advantage: currency trade Disadvantage: volatile
Source: Prepared by author				

6. Findings and Policy implications

From ongoing analysis one finds that there is no single exchange rate regime followed by the world economy in all times. A country should adopt the exchange rate regime depending upon the trade cycle and its economic structure.

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