International Monetary System

Present International Monetary system (1972-present), Part B

Pegging of Currencies

- Pegging of Currencies means its fixed value in terms of

A. A single currency

B. A basket of currencies

C. SDRs

- Special Drawing Rights are international reserves asset created by the IMF

Pegging of Currencies

- A semi fixed system adjusts the exchange rate slowly by small amounts
- On a continuous basis to correct for any overvaluation and undervaluation
- Designed to discourage speculation by setting an upper limit Pegging of Currencies

Crawling Peg

- Crawling peg involves periodic adjustment of fixed exchange rate to catch up with market determined rates.
- In this system an attempt is made to combine the advantages of fixed exchange rate with flexibility of floating exchange rate
- It fixes the exchange rate at a given level which is responsive to changes in market conditions i.e. it is allowed to crawl.

Crawling Peg

- In a Crawling Peg arrangement the currency is adjusted periodically “in small amounts at a fixed rate or in response to changes in selective quantitative indicators (past inflation differentials vis-à-vis major trading partners…)
- A Crawling Band allows a periodic adjustment of the exchange rate band itself

Crawling Peg

- The upper and lower limits are decided for exchange rate depending demand and supply of foreign exchange
- As the exchange rate crosses these limits, fiscal and monetary policies come into play to push the exchange rate within the target zone
- But in this case, these limits are sustained for some time and if it is felt that economic indicators are being disturbed, the monetary authorities let the exchange rate depreciate or appreciate as the case may be

Target Zone Arrangements

- Target zone arrangement involves member countries having fixed exchange rate among their currencies
- Alternatively, they may use a common currency.

Thank You