

-A fixed or pegged exchange rate is when a country's monetary authority sets official buying and selling rates for its currency in relation to a foreign currency and commits to trading at those rates without limits. These rates can be the same, but often they differ slightly, leading to narrow bands within which the exchange rate can fluctuate, despite being considered "fixed."

-The Bretton Woods system established bands within which exchange rates could fluctuate. This allowed some flexibility while still maintaining a fixed exchange rate regime. The bands acted as limits, preventing exchange rates from deviating too far from the established rate.

- A "crawling peg" is a type of fixed exchange rate where the government periodically adjusts the exchange rate in small increments. This can be considered a form of fixed exchange rate because the adjustments are predetermined and controlled by the government in order to prevent inflation differentials and single large devaluation.

- There is a problem with a fixed exchange rate. It restricts a government's ability to use monetary policy for stabilization. If a country faces a sudden and permanent decline in export demand, it suffers more under fixed exchange rates. Without the flexibility to adjust export and import prices quickly, domestic employment and output decrease.

- The idea of fiscal policy is lowering interest rates but the problem is exchanging rate remain unchanged and capital markets open leading nominal domestic interest rate and nominal foreign interest rate to be the same which implies domestic interest rate being determined by foreign interest rate not by money supply by monetary policy. And this causes the government to buy back their money if they try to supply more money and lose their foreign reserves due to selling excess money for foreign currency by agents. If not, the currency will depreciate

-Because capital is mobile leading nominal interest rate and nominal foreign interest rate to be the same. And if the government attempts to expand money supply, they will face the situation that they have to buy back and lose their foreign reserves.

- Sterilized monetary policy refers to interventions by central banks to influence exchange rates without affecting the domestic money supply. The authors consider sterilized interventions as largely ineffective because they do not neither significantly impact interest and exchange rates nor relative

money supplies, making them akin to smoke and mirrors in terms of their effectiveness.

- Three main advantages of fixed exchange rate

+ Reduced Uncertainty: Fixed exchange rates provide stability and reduce uncertainty for businesses engaged in international trade, investment, and financial transactions. Also good for workers and enhanced competitiveness

+ Restrain Domestic Inflation Pressures: can be caused by excessive government budget deficits or in the wage- and price-setting decisions of the private sector in order to follow expansionary macroeconomic policies.

+ Fixed rates have the attraction of anchoring price inflation for internationally traded goods and providing a guide for private-sector inflation expectations.

- Reduced International Trade: Exchange rate uncertainty can discourage international trade by making it difficult for businesses to predict the costs of importing and exporting goods and services.

- Discouraged Investment: Investors may be hesitant to commit capital to countries with volatile exchange rates due to the increased risk and uncertainty associated with currency fluctuations.

- Workers and firms hurt by protracted exchange-rate swings often demand import protection from their governments.

- The European Union believed that exchange rate variability would be detrimental to the establishment of a common market because:

+ Variations in exchange rates can lead to shifts in competitiveness within the EU, potentially undermining the political consensus for free intra-EU trade.

+ Fixed exchange rates were seen as a means to maximize the gains from a unified market and to prevent exchange rate-induced disruptions in competitiveness among member states.

- By pegging to a low inflation currency will help to restrain domestic inflation pressures.

- As government pegging to a low inflation currency will help them resist and prevent any temptations to follow macroeconomic policies

-When a country experiences periods of unstable prices, pegging its currency to another stable currency or a fixed exchange rate can help stabilize inflation. This stabilization is important for goods traded internationally. Pegging provides a clear reference point for both businesses and individuals, which helps them anticipate inflation accurately. - The bigger the size of capital markets the harder the ability to defend a peg as daily volume of foreign exchange transactions now exceeds \$1 trillion per day, a number far greater than the reserves of any central bank.

-Defending a currency peg involves ensuring the value of a country's currency remains fixed to another currency or asset. To achieve this, central banks must have enough resources to repurchase the high-powered monetary base, which includes deposits at the central bank plus currency in circulation. Typically, they wouldn't need to buy the entire base to fend off a speculative attack. Instead, they can shrink the monetary base, which raises interest rates. High interest rates make it costly for speculators to bet against the domestic currency, discouraging speculative attacks and helping maintain the peg.

-Major central banks have the ability to access swap-line arrangements with other central banks, enabling them to swiftly borrow the foreign currency required for intervention. As long as a government is not insolvent, it can obtain additional resources from private markets to absorb high-powered money.

- Enough reserves to buy back monetary base like in table 1, It shows countries like Belgium, Ireland, Netherlands, UK, and so on have their total reserves more than their monetary base and it said the ratio of total reserves to the base was over 100 percent even the weakest country like Italy have nearly 50 percent meaning that they over 100 percent success to defend their peg.

- Speculative attack on the central bank's foreign reserves can trigger a domestic bank run. By having the central bank acting as a lender and providing currency loans to the bank system, the monetary base will become large, and this could bloat the stock of potential private sector claims on the central bank's foreign reserves.

- Because there are other objectives like controlling high interest rates will have negative effects to domestic economy. But if the government ignore it leading to uncredible and making exchange rate more vulnerable to speculative attack.