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## Article

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## Flexible Exchange Rate Regimes in Emerging Markets: Current Insights and Avenues for Future Research

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### ABSTRACT

**Purpose:** Providing a structured literature review on the flexibilization of exchange rate regime in emerging countries with a focus on recent studies conducted in the field, in order to identify promising opportunities of future research.

**Design/methodology/approach:** Starting with a review of the International Monetary System (IMS) evolution before addressing the theoretical corpus related to exchange rate regimes, before shedding the light on the main types of exchange regimes. Then, reviewing the main studies published between 2000 and 2023.

**Findings:** The more we deepen the research in the field, the more we realize that the literature has not given enough interest to study the impact of exchange rate regime flexibilization on the microeconomic level, especially on companies. Indeed, it would be interesting to study the impact of exchange rate regimes flexibilization on companies mainly through financial performance indicators, e.g., solvency, turnover and financial profitability.

**Research limitations/implications:** The limitations of this study are the few even missing work studies done on the micro economic level to deeply analyze the aspects of this shutter.

**Originality/value:** The originality of this work is to have a critical analysis of the existing knowledge body and current contributions in the field in order to identify potential further unexplored aspects such as studying the impact of exchange rate regime on firms, on the micro economic level, which is an area not exploited in literature. A better understanding of the impact on companies' profitability could benefit more practitioners as well as policy-makers to more likely frame and control the process of floating their local currency.

*Keywords: Exchange rate regime, Flexibilization, Emerging countries, MENA region, Literature review, International monetary fund*

## I. Introduction

The global economy is constantly evolving and governments must adapt their monetary and fiscal policies and exchange rate regimes so as to develop their competitiveness, their ability to attract foreign investment and manage capital flows. However,

finding the optimal exchange rate regime can be a complex task, especially for emerging economies in regions such as the Middle East and North Africa (MENA) and Sub-Saharan Africa.

Therefore, the countries concerned must determine the best suitable exchange rate regime to their economic needs and adequate to the requirements of each type of exchange rate regime willing to be adapted: fixed, intermediate or floating. Fränkel (1999) argued that "no single currency regime is right for all countries or at all times". Thus, each country has to adapt its exchange rate regime to

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its economic situation whenever it is deemed necessary. This choice is much more difficult for developing countries because they are in a continuous mission of adaptability of their monetary and fiscal policy but also their exchange rate regime. Hence the empirical studies on the impact of exchange rate variations on the macroeconomic variables of these countries, through fundamental and behavioral approaches. As a result, many authors such as Bouoiyour.J & Rey.S (2005), Brixiova.Z, Egert.B and Hadj Amor Essid.T (2014) disagreed on whether the exchange rate regime has a direct impact on the long term economic growth or not, creating a big debate. Furthermore, other studies were held by Peters (2014), Hadj Amor.T, El Araj.R (2009), Akiba.H, Iida.Y & Kitamura.Y (2009), in order to figure out if there is an optimal combination of exchange rate regimes to maximize the welfare.

Since the collapse of the Bretton Woods system in 1973, due to US. Trade deficit and rising inflation as well as the Nixon shock, a large proportion of developing countries members of the International Monetary Fund (IMF) had the right to choose the exchange rate regime that best suited their economy, and the majority of them had chosen a fixed parity, linked to their main foreign partner. Some countries, after the economic crises experienced during the 80s and 90s, decided to adapt a floating exchange rate regime, while others decided to remain on a fixed exchange rate regime. Nevertheless, it should be noted that the number of countries adopting an intermediate exchange rate regime, which is considered fragile, or even floating, has been increasing since the 1980s.

From this perspective, it seems hard to sustain a fixed exchange rate regime on the long-term in a context of more liberalized capital flows. Consequently, some emerging countries have been obliged to look forward more flexibility; the difference between these countries was the ease of transition, some have had a smoother one, while others went through more complicated phases, due to their different levels of financial openness.

Despite the significant literature in this field, the knowledge upon emerging markets should be

enriched given the precarious situation of these countries, whether at the macro or micro economic level. In this study, we would provide a comprehensive up-to-date and critical review of the literature. Additionally, by highlighting areas where further research is needed, we aim to find gaps of research and identify a promising agenda for future unexploited aspects of research in this field.

To meet these objectives, this paper aims to answer the following questions:

1. What is the state of research on flexible exchange rate regimes in emerging markets?
2. What are the potential future areas of research on flexible exchange rate regimes in emerging markets?

To answer these questions, we provide a comprehensive review of the literature, published between 2000 and 2023 in peer-reviewed journals, on the flexibilization of exchange rate regimes in emerging countries. Starting with a first section where we would examine the evolution of the International Monetary System (IMS), and define the exchange rate regimes based on the IMF classification while highlighting their advantages and drawbacks. Then, we would point various theories surrounding exchange rate regimes and iterate the different studies in the field. In the second section will provide an overview of the different research studies conducted in the last two decades concerning the flexibility of exchange rate regimes in the MENA region and Sub-Saharan countries. We will examine the main findings and conclusions of these studies in order to provide a comprehensive understanding of the existing literature on exchange rate regimes in these regions and to identify unexploited areas for further research.

Our analysis would take into account the economic and political context in which these studies were conducted, and we would consider the broader implications of our findings for policymakers and researchers in the field.

## II. Literature Review

### A. Evolution of the International Monetary System (IMS)

The IMS allows an appraisal of value and money exchange between countries, and as any system, it has regulations that serve calculating the exchange rate and terms of international transactions. Meaning that by promoting trade, it helps mobilizing capital from a nation to another. Moreover, the IMS has many economic agents notably multinational corporations, investors, financial institutions, etc. Over the past 75 years, it started by the Gold Standard phase (1875 -1914) which, thanks to its fixed exchange rate system with few fluctuations, the international trade witnessed a boost and less trade disparities.

The evolution of the international monetary system has been a complicated and dynamic process, marked by substantial alterations in economic and geopolitical environments. The Bretton Woods system, which was formed in 1944 as part of the Bretton Woods Agreement, was distinguished by fixed exchange rates related to the US dollar, which was itself pegged to gold. However, this system encountered difficulties as a result of the United States' trade deficit and rising inflation in the 1960s and early 1970s. President Nixon's decision to forsake the dollar's gold convertibility effectively ended the Bretton Woods system, ushering in an era of floating exchange rates. This time saw greater exchange rate volatility, currency crises, and a fight to build a new global monetary order.

The following establishment of managed floating and other exchange rate regimes, as well as the dominance of the US dollar in international trade and finance, formed the modern international monetary system. Globalization, financial innovation, and the expansion of emerging economies are all influencing the system's evolution, which presents both opportunities and challenges for global economic stability and collaboration.

### B. Exchange Rate Regimes: Classification of the IFM

Exchange rates are described as the value of one country's currency in relation to another. They can be defined as the average rate for a given timeframe or as the rate at the end of the time frame. According to The International Monetary Fund (IMF), there are three main big categories of exchange rate regime:

- **Hard pegs:** Give legal tender status to another country's currency (full dollarization) or require the central bank to hold foreign assets in an amount at least equivalent to the local currency in circulation and bank reserves. A tight peg goes hand in hand with sound fiscal and structural policies and low inflation.
- **Soft pegs:** Currencies that maintain a stable value relative to an anchor currency or composite currency unit. The exchange rate may be pegged to the anchor currency over a tight or wide band; in certain instances, the peg varies over time, often in response to variations in inflation rates across countries. Although soft pegging keeps a tight "nominal peg" (nominal price or quantity targeted by monetary policy) to buffer inflationary expectations, it gives monetary policy limited flexibility to deal with shocks. But soft pegs can be susceptible to financial crises - which can lead to large devaluations and even the abandonment of the peg - and tend not to be long lasting
  - Crawl-like arrangements
  - Stabilized arrangements
  - Conventional pegs
  - Pegged exchange rates within horizontal bands.
- **Floating:** as the name infers, the floating rate is essentially a market-driven system. In countries with this regime, the central bank acts (buying or selling currency against the local currency) mainly to restrict short-term fluctuations in the exchange rate. The floating rate regime has the benefit of maintaining an autonomous

**Table 1.** Synthesized Table of Advantages and Drawbacks on Each Regime

Regime Classification	Advantages	Disadvantages
Hard Pegs	<ul style="list-style-type: none"> <li>- Reduced administrative expenses;</li> <li>- Sounder financial sector;</li> <li>- Reduced inflation;</li> <li>- Reduced interest rates;</li> <li>- Mitigated exchange rate risks;</li> <li>- Low volatility</li> </ul>	<ul style="list-style-type: none"> <li>- Lost national symbol by adopting the dollarization;</li> <li>- No more independent monetary policy;</li> <li>- More exposure of central banks to liquidity risks during depression or recession periods;</li> <li>- High Volatility of foreign currency reserves</li> </ul>
Soft Pegs	<ul style="list-style-type: none"> <li>- Maintained stability;</li> <li>- Maintained competitiveness;</li> <li>- Reduces interest rates;</li> <li>- Easily managed anchor;</li> <li>- Reduced inflation;</li> <li>- Medium volatility</li> <li>- Medium volatility of foreign currency reserves</li> </ul>	<ul style="list-style-type: none"> <li>- Openness to currency crises;</li> <li>- Possible financial crises;</li> </ul>
Floating	<ul style="list-style-type: none"> <li>- Free adjustment to external shocks;</li> <li>- Autonomous monetary policy;</li> <li>- Low volatility of foreign currency reserves</li> </ul>	<ul style="list-style-type: none"> <li>- Risk of continuous increase of general level of prices: rise of inflation;</li> <li>- High volatility</li> </ul>

Source: Authors

monetary policy. In the countries that apply it, the foreign exchange market and other financial markets must be well developed to absorb shocks with minimal fluctuations in the exchange rate.

### C. Exchange Rate Main Theories

Understanding the factors that influence exchange rates is essential for policymakers, investors, and market participants. Over the years, several economic theories have been proposed to explain the dynamics of exchange rate movements. This section of the article provides an overview of prominent theories:

#### 1. Purchasing Power Parity (PPP)

Purchasing Power Parity, introduced by Cassel.G (1925), posits that the exchange rate between two currencies is determined by the ratio of their general price levels. It assumes that a country's currency will appreciate or depreciate to equalize the purchasing power of different currencies. PPP is considered a generalization of the "one price applies to all goods in an economy" rule. However, it often oversimplifies real-world complexities, such as transportation costs and market imperfections, limiting its predictive power.

#### 2. Interest Rate Parity (IRP)

Interest Rate Parity, developed by Keynes.J M in the 1923, emphasizes the relationship between interest rates and exchange rates. It states that the difference between the short-term interest rate and the forward exchange rate must be considered when adjusting the evolution of the exchange rate between two currencies. The work on establishing hedged and unhedged interest rate parity has been completed. While theoretically sound, it assumes away factors like transaction costs and risk, making it less effective in volatile markets.

#### 3. International Fisher Effect (IFE)

The International Fisher Effect, proposed by Fisher.I in 1930, is used to forecast spot currency fluctuations and future changes in nominal interest rates. It suggests that an economy with lower interest rates will also experience reduced rates of inflation. The IFE assumes a link between interest rates, inflation expectations, and exchange rate movements. Yet, it may oversimplify economic conditions, as real-world inflation and interest rate relationships can be more intricate.

#### 4. *Balance of Payments Approach to the Exchange Rate*

The Balance of Payments Approach, developed by Mundell, R. (1965) and Fleming, M. (1961), highlights the impact of a nation's balance of payments on its exchange rate. It states that the supply and demand for foreign currencies, influenced by the balance of payments, determine the exchange rate. While it considers external trade dynamics, it might not fully capture speculative pressures or asset market influences.

#### 5. *Monetary Policy Theory*

The Monetary Policy Theory, proposed by Wicksell, K. (1898-1907), Fisher, I. (1907-1937), and Keynes, J. M. (1936), emphasizes the role of a nation's central bank in influencing its economy through changes in the money supply and interest rates. However, it assumes a simplified relationship between money supply, interest rates, and exchange rates, which may not always hold true.

#### 6. *Fear of Floating Concept:*

The Fear of Floating concept, introduced by Obstfeld, M., Rogoff, K. (1995) and Eichengreen, B. (2000), addresses concerns related to exchange rate volatility and loss of control over monetary policy under a floating exchange rate system. It suggests that some nations may prefer to tie their currency to a reliable external anchor, such as the US dollar or a basket of currencies, to mitigate perceived risks associated with exchange rate fluctuations. Yet, it focuses on countries' reluctance to embrace fully floating rates, rather than explaining the mechanics of exchange rate movements.

#### 7. *Adaptive Expectations Theory:*

The Adaptive Expectations Theory, proposed by Muth, J. in the 1961, suggests that individuals and businesses base their future inflation expectations on past experiences, gradually updating them as new information becomes available. This theory emphasizes

that changes in expectations of future inflation play a significant role in short-term changes in exchange rates, as predictions based on historical patterns tend to become self-fulfilling. However, it assumes that individuals base their predictions solely on past experiences, overlooking more complex factors that can influence expectations.

#### 8. *Asset Market Approach:*

The Asset Market Approach, introduced by Meese, R. and Rogoff, K. in 1983, asserts that exchange rates are determined by the supply and demand for assets denominated in different currencies. It suggests that exchange rates represent the cost of one currency relative to another, influenced by supply and demand dynamics in the market for assets. Factors such as projected returns, anticipated future exchange rates, and the risk associated with holding assets denominated in a particular currency impact the demand for such assets. Nevertheless, it simplifies the complex relationship between exchange rates and asset markets, neglecting factors like market sentiment and geopolitical events.

### III. Current State of Research

Exchange rate regimes and their flexibility have been the subject to several studies in the last two decades, particularly in the MENA and Sub-Saharan countries. Over the years, countries have shifted towards more flexible exchange rate regimes, moving away from fixed exchange rate systems. This trend has been driven by a variety of factors, including globalization, integration and openness into the global financial system, and the need for greater macroeconomic stability.

The studies on exchange rate regimes in the MENA region and Sub-Saharan countries have tried to understand the impact of exchange rate flexibility on various aspects of the economy, including inflation,

trade, capital flows, and economic growth. Researchers have also analyzed the role of different institutional, political, and economic factors in shaping the choice of exchange rate regimes in these regions.

### A. Publishing Activity by Region

The descriptive statistics of the sample reviewed indicate that the majority of the studies focused on the Middle East North African region (MENA) or on emerging markets globally, while little attention South America and Europe. As a matter of fact, 55% of the studies are conducted in MENA region, 25% in global emerging markets, 10% in South America and 10% in Europe. This demonstrates the big interest given to MENA region due to the importance of its emerging economies.

### B. Publishing Activity by Year

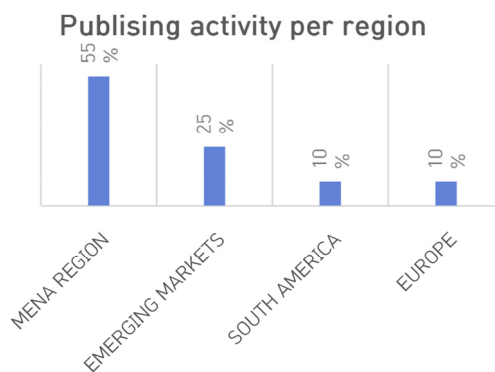
**Early 2000s:** Research on emerging market exchange rate regimes continues to evolve during this time period. Scholars examined many countries' experiences, including those that adopted more flexible exchange rate arrangements in reaction to financial crises or as part of broader economic changes: Frankel 1995, Zhou, Su. 1995, Dibooglu 2000, **Post-Global Financial Crisis (late 2000s to early 2010s):** The 2008 global financial crisis rekindled interest in exchange rate regimes, particularly their role in alleviating or exacerbating economic shocks. During this period, research concentrated on the efficiency of flexible exchange rates in emerging nations during times of financial turbulence.

### C. Publishing Activity by Econometric Models

In terms of methodology, the authors of the reviewed work use a variety of theoretical, conceptual, qualitative analysis and econometric estimators,

ranging from simple regressions to complex regressions.

Panel unit root, panel co-integration, panel causality test and panel Granger causality tests are examples of dynamic panel models used in the majority of the studied samples. Furthermore, the two-step general methods of moments (GMM estimations) were used in the evaluated work because it helps avoiding biased estimates and control for other potential confounding factors that may affect the relationship between the different variables, by generating correct standards errors and p values (Cottrell & Lucchetti, 2016). Another econometric method utilized in the conducted studies is the Dynamic Stochastic General Equilibrium (DSGE), in order to define the optimal exchange rate regime for an emerging economy for a stable monetary policy.



Source: Authors

**Figure 1.** Distribution of the Sampled Studies Per Region



**Figure 2.** Annual Distribution of the Sampled Studies

**Table 2.** Publishing Journals and Their Related Articles, with Their Respective SJR Ranking and Citation Count (End of September 2023)

YEAR	REVIEW	SJR RANK	ARTICLE	Citation count
2000	Southern Economic Journal	Q2	International Monetary Regimes and Incidence and Transmission of Macroeconomic Shocks: Evidence from the Bretton Woods and Modern Floating Periods, Dibooğlu.S	16
2001	Global Business and Finance Review	Q4	Does exchange rate volatility affect trade? Evidence from several European countries, Laopodis.NT	6
2002	Global Business and Finance Review	Q4	Exchange rate and stock market interactions: evidence from an emerging economy, Laopodis.NT	3
2003	Finance & Development	Q4	Should MENA Countries Float or Peg? As they open up their economies, MENA countries may need to rethink their exchange rate regimes, Jbili.A and Kramarenko.V	31
2005	Blackwell Publishing	Q1	Exchange Rate Regime, Real Exchange Rate, Trade Flows and Foreign Direct Investments: The Case of Morocco, Bouoiyour.J And Rey.S	60
2006	Journal of Financial Regulation and Compliance	Q3	Internal risk control benchmark setting for foreign exchange exposure: The case of the Moroccan Dirham, Al Janabi.A.M	25
2007	Global Business and Finance Review	Q4	Does exchange rate volatility affect international trade flows? McPherson. M O	-
2009	Int Econ Econ Policy	Q3	The optimal exchange rate regime for a small country, Akiba.H & Iida.Y & Kitamura.Y	9
2009	Journal of Economics and International Finance	NR	Sustainability of exchange rate policies and external public debt in the Mena region, Neaime.S	35
2009	Panoeconomicus	Q2	Long Term Dynamic of Real Exchange Rate, Trade Liberalization and Financial Integration: The Case of South-East Mediterranean Countries, Hadj Amor.T & El Araj.R	1
2011	International Economics	Q2	The transfer effect: A comparative perspective between the European monetary union regime and fixed and floating regimes, Bouhoucha.M	-
2011	International Economics	Q2	Exchange Rate Policy and Sovereign Spreads in Emerging Market Economies, Gumus.I	17
2012	International Review of Financial Analysis	Q1	Switching to floating exchange rates, devaluations, and stock returns in MENA countries, Chortareas.G, Andrea Cipollini.A & Eissa.MA	21
2012	North American journal of Economics & Finance	Q2	Fear of floating or monetary policy as usual? A structural analysis of Mexico's monetary policy, Best.G	22
2012	Journal of International and Global Economic Studies	NR	Monetary Policy and Choice of Exchange Rate Regime for the Developing Countries: Case of Morocco, Tounsi.S, Ragbi.A & Firano.Z	1
2014	Rev. Middle East Econ. Fin.	NR	The Real Exchange Rate and External Competitiveness in Egypt, Morocco and Tunisia, Brixiova.Z, Egert.B, and Hadj Amor Essid.T	38
2014	Social science research Network Electronic journal	NR	The Interaction between Exchange Rate Regime and Economic Growth: Empirical evidence for Tunisia, Bouzid.A	-
2014	International Economics and economics policy	Q3	Monetary policy, exchange rate targeting and fear of floating in emerging market economies, Peters.A C	23
2018	China Finance Review International	Q1	Monetary model of exchange rate determination under floating and non-floating regimes, Ibhagui.W C	7
2019	Global business Review	Q2	Can Exchange Rate Volatility Influence the Export Positively? Evidence from Turkey Under the Regime Shifts, Bilgili.F, Ulucak.R, Soykan.M & Erdogan.S	10
2019	Economic Modeling	Q1	Does monetary policy credibility mitigate the fear of floating?, Montes.GC, Ferreira.FC	16
2019	Journal of policy modeling	Q2	Effect of monetary policy credibility on the fear of floating: Evidence from Brazil, Montes.GC, Ferreira.CF	8
2021	International Journal of Finance & Economics	Q2	Co-movement of foreign exchange rate returns and stock market returns in an emerging market: Evidence from the wavelet coherence approach? He.X, Gokmenoglu.K , Kirikkaleli.K, Rizvi.S	8
2022	Revue Française d'Economie et de Gestion	NR	Transmission Channels, Financial Instability and Exchange Rates: The Case of the MENA Zone, FIRANO.Z & MOULOUEDE.B	-



**Table 2.** Continued

YEAR	REVIEW	SJR RANK	ARTICLE	Citation count
2022	Journal of Risk and Financial Management	Q3	Exchange Rate Volatility Effect on Economic Growth under Different Exchange Rate Regimes: New Evidence from Emerging Countries Using Panel CS-ARDL Model, Ameziane.K & Benyacoub.B	4
2022	Journal of International Financial Markets, Institutions and Money	Q1	Global financial conditions, capital flows and the exchange rate regime in emerging market economies, Lu.D, Liu.J, Zhou.H,	3
2022	Research in International Business and Finance	Q1	Macroeconomic and monetary policy responses in selected highly indebted MENA countries post Covid 19: A structural VAR approach, Neaime.S, Gayset.I	2
2023	Journal of Financial Economic Policy	Q3	Monetary policy and inflation targeting under global uncertainty: a SVAR approach for Tunisia, Trabelsi.E, Ben Khaled.A	-

Source: Authors

## D. Macroeconomic Factors: Research Review

### 1. Endogenous Factors

#### 1) Monetary policy

The literature on exchange rate policies and their effects on developing market economies is rich in information. According to Gumus (2011), a flexible exchange rate policy is associated with lower sovereign spreads than a fixed exchange rate policy. However, additional factors that determine sovereign spreads must be considered. Best (2012) highlights the fear of floating in Mexico's monetary policy decisions, indicating the necessity for additional research on the trade-offs involved in selecting an exchange rate regime.

Despite concerns about exchange rate volatility, Peters (2014) addresses the relationship between monetary policy, exchange rate targeting, and the fear of floating. Ibhagui (2018) confirms that under floating regimes, the exchange rate is more susceptible to monetary policy changes. Finally, Montes and Ferreira (2019) propose that greater monetary policy credibility can lower exchange rate volatility and alleviate the risk of floating. Overall, these research give light on the complicated dynamics of exchange rate controls, floating anxiety, and the ramifications for emerging market economies.

#### 2) Stock markets

Chortareas.G, Andrea Cipollini.A and Eissa.M A

(2012) investigate the impact of transitioning to floating exchange rates and devaluations on MENA stock returns. According to their findings, such policy changes are related with a drop in stock returns, with the amount and direction of the impact shifting among nations and across time. Furthermore, the authors discover that adopting a floating exchange rate regime and devaluations have a greater negative impact on stock returns in nations with lower levels of financial development and among enterprises with higher amounts of foreign currency debt.

These findings, joining the study conducted by Laopodis.N T (2002) on the Greek stock market returns, imply that the effects of changing exchange rate regimes and devaluations on stock market performance are influenced by contextual factors such as financial development and firm-specific features. The study underscores the importance of considering these nuances when evaluating the effects of exchange rate policies on stock returns in MENA countries. In the same sense, He.X, Gokmenoglu.K, Kirikkaleli.K, Rizvi.S K (2021) studied the impact of exchange rate volatility on the Turkish stock market during several periods, to point out the negative correlation between the two components. The more volatile an exchange rate regime is, which is the case of more flexible exchange rate regimes, the less are stock returns.

#### 3) Internal risk control

Al Janabi. A M (2006) focuses his research on

the importance of internal risk control benchmark setting in controlling foreign exchange exposure and limiting currency risk. In order to manage foreign exchange exposure and lower the risk of currency swings, the author contends that internal risk control benchmark setting is essential. He specifically investigates the Moroccan Dirham and its associated internal risk control practices. The author does not use any empirical data or statistical analysis to test the hypothesis. Instead, the author provides a discussion of the importance of internal risk control benchmark setting for managing foreign exchange exposure and reducing currency risk, based on a review of the literature and practical considerations. The study underlines the significance of defining realistic and attainable benchmark levels for foreign exchange exposure, while taking the company's individual foreign exchange exposure profile and risk

tolerance into account. As crucial considerations in selecting optimal benchmark levels, market conditions, economic conditions, and company-specific characteristics are explored. This study emphasizes the need of internal risk control benchmark setting in efficiently managing currency fluctuations and avoiding foreign exchange risks.

#### 4) Economic growth

Bouoiyour.J and Rey.S (2005) undertake research on the impact of Morocco's exchange rate regime and real exchange rate on trade flows and foreign direct investments. Their findings indicate that policymakers in Morocco and other similar economies should evaluate the choice of exchange rate regime and its consequences for trade and investment, because unlikely for European countries as shown

**Table 3.** Representative Table of the Macroeconomic Factors Related to the Literature Review

Factors	PROXIES/VARIABLES	SAMPLE OF THE LITERATURE
ECONOMIC GROWTH	Trade flows Foreign direct investments Inflation Gross domestic product	Laopodis.N T (2001) McPherson.M O (2007) Bouoiyour.J and Rey.S (2005) Akiba.H & Iida.Y & Kitamura.Y (2009) Ameziane.K & Benyacoub.B (2022) Lu.D, Liu.J, Zhou.H (2022)
COMPETITIVENESS	Trade balance (exports)	McPherson.M O (2007) Hadj Amor.T, El Araj.R (2009) Brixiova.Z, Balazs Egert.B and Hadj Amor Essid.T (2014) Bilgili.F, Ulucak.R, Soykan.M E, Erdogan.S (2019)
MONETARY POLICY	Sovereign spreads Fear of floating	Gumus.I (2011) Best.G (2012) Peters.A C (2014) Ibhagui.O W (2018) Montes.G C, Ferreira.C F (2019) Neaime.S, Gaysset.I (2022) Trabelsi.E, Ben Khaled.A (2023)
MACROECONOMIC SHOCKS	Transmission of external shocks Contagion effect	Dibooğlu.S (2000) Neaime.S, Gaysset.I (2022) Trabelsi.E, Ben Khaled.A (2023)
STOCK MARKETS	Stock returns	Laopodis.N T (2002) Chortareas.G, Andrea Cipollini.A, Eissa.M A (2012) He.X, Gokmenoglu.K , Kirikkaleli.K, Rizvi.S K (2021)
PUBLIC DEBTS	External debt	Neaime.S (2009) Neaime.S, Gaysset.I (2022)
TRANSFER EFFECT	Transfer effect	Bouchoucha.M (2011)
INTERNAL RISK CONTROL	Internal risk control benchmark	Al Janabi.A M (2006)

Source: Authors

by Laopodis.N T (2001), exchange rate volatility has no impact on bilateral trade flows. Bouoiyour.J and Rey.S (2005) study provides useful information for policymakers in developing effective strategies in various areas; noticeably a rising volatility and overvaluation can lead to a deterioration of the trade balance. However, such volatility doesn't affect foreign direct investments. Moreover, reducing the public deficit is essential to reach effective monetary policy and exchange rate stability. These results should be taken into consideration while looking for an equilibrium of exchange rate in Emerging markets.

By evaluating the ideal exchange rate regime for a small open economy, Akiba.H & Iida.Y & Kitamura.Y (2009) contribute to the literature. They contend that such an economy should use a flexible exchange rate regime in conjunction with an inflation-targeting monetary policy. When compared to a fixed exchange rate system, this combination achieves a more favorable trade-off between exchange rate stability and monetary independence. This study emphasizes the need of carefully analyzing the best exchange rate regime and monetary policy framework for small open economies in order to maximize economic outcomes. Came the study of Ameziane.K & Benyacoub.B in 2022, stating that intermediate exchange rate regimes could be considered more effective in terms of growth in emerging markets and controlling more exchange rate volatility. Focusing on capital flows, Lu.D, Liu.J, Zhou.H (2022) concluded through their study that When global risk aversion is low, particularly for gross liability flows, the flexible exchange rate regime stabilizes capital flows, but when it is high, it does not play this role. We also show that larger deviations in hedged interest parity would amplify the impact of global risk aversion, explaining the failure of flexible exchange rate regimes during periods of high global risk aversion.

## 2. Exogenous Factors

### 1) Competitiveness

Hadj Amor.T and El Araj.R (2009) conducted study

on the impact of trade liberalization in South-East Mediterranean countries. According to their findings, trade liberalization has resulted in a devaluation of these countries' real currency rates, which has been accompanied by growing financial integration. Furthermore, trade liberalization has resulted in a more flexible exchange rate system, increasing export competitiveness. The findings highlight the significance of trade liberalization and its consequences for currency rates and financial integration in the South-East Mediterranean region.

Brixiova.Z, Balazs Eger.B and Hadj Amor Essid.T (2014) investigate the impact of the real exchange rate on external competitiveness in Egypt, Morocco, and Tunisia in a similar study. Their research shows that changes in the real exchange rate have a considerable impact on these nations' trade balances and external competitiveness, a result also confirmed by McPherson.M O (2007) when studying the effects of currency market dynamics on global commerce; when it's positive for exporters, it is negative for importers. While a short-term decrease in the real exchange rate increases trade balance and competitiveness, it may lead to a decline in competitiveness in the long run due to negative impacts on production and efficiency. The study also emphasizes the non-linear relationship between the exchange rate and competitiveness, with worker productivity and the business environment playing important roles.

Regarding Bilgili.F, Ulucak.R, Soykan.M E, Erdogan.S (2019) examination, their research focuses on currency rate volatility and its impact on Turkish exports, with a special emphasis on the manufacturing sector. According to the findings, currency rate volatility has a favorable impact on exports, particularly in the industrial sector. Furthermore, the study finds that the positive impact of exchange rate volatility on exports is stronger during periods when the floating exchange rate regime switches. Furthermore, enterprises with higher export market diversification benefit more strongly.

Overall, these research papers help us comprehend the complicated links that exist between trade liberalization, exchange rate movements, and external

competitiveness. The findings emphasize the necessity of taking a variety of factors into account when studying the effects of exchange rates on trade and competitiveness in different nations, such as financial integration, productivity, sector-specific effects, and regime transformations.

### 2) Macroeconomic shocks

Diboolu's study from 2000 examines the occurrence and transmission of macroeconomic shocks under various international monetary regimes. The data show that macroeconomic shocks were more promptly and widely propagated among countries during the Bretton Woods era. Shocks, on the other hand, tend to be absorbed more locally under the modern floating system, resulting in a lower impact. This suggests that the international monetary system chosen can have a major impact on the occurrence and transmission of macroeconomic shocks. The study emphasizes the need of taking into account the impact of various monetary regimes on global economic stability and the interdependence of national economies. Yet, Neaime.S and Gaysset.I (2022), through their econometric models, find that MENA region remain vulnerable to external shocks even with flexible exchange rate policies if they are not appropriately effective. A result confirmed by Trabelsi.E, Ben Khaled.A (2023), with a study on Tunisia. In the long term, the rising world uncertainty related to different shocks has a positive correlation with the inflation that central bank cannot control.

### 3) Transfer effect

In 2011, Bouchoucha.M conducted research on the transfer impact under various currency rate regimes, identifying the European monetary union regime as having a stronger transfer effect than fixed and floating exchange rate regimes. The study's findings provide useful insights into the effects of exchange rate regimes on the transfer effect, with the European monetary union system having a heightened impact. This study advances our understanding of the processes and dynamics of transfer effects in various exchange rate systems,

giving insight on the consequences for economic integration and policy coordination within the European monetary union.

### 4) Public debts

In 2009, Neaime.S conducted research on the relationship between exchange rate regimes and external debt sustainability in the MENA area. According to the analysis, the region's overall foreign debt sustainability is rather poor. It does, however, discover that a flexible exchange rate regime is linked to greater levels of external debt sustainability. This implies that MENA countries with a flexible exchange rate policy may have stronger mechanisms for addressing foreign debt obligations.

Furthermore, the analysis reveals that using foreign currency denominated loans increases the probability of debt hardship. Countries that rely substantially on foreign currency debt are more likely to experience debt trouble. Moreover, the study discovers that countries with a higher level of external debt relative to GDP are more vulnerable to debt distress. Fostering the research more with a study done with Gaysset.I in 2022, the authors concluded once again that under fixed exchange rate, high external debts and their increase during crisis periods cannot be sustained effectively. These findings provide light on the factors impacting external debt sustainability in the MENA area and highlight the significance of exchange rate regimes and debt composition in managing and mitigating external debt risks.

## IV. Results and Future Research Propositions

In the past two decades, the literature review has revealed that the impact of exchange rate flexibility has primarily been examined from a macroeconomic standpoint. This includes its influence on trade flows, monetary policies (Gumus.I 2011, Peters.A C 2014, Montes.G C, Ferreira.C F 2019, Neaime.S & Gaysset.I 2022, Trabelsi.E & Ben Khaled.A 2023), macro-

economic stability (Peters.A C 2014), capital flows, foreign direct investments, fiscal policy, external competitiveness (Hadj Amor.T & El Araj.R 2009, Brixiova.Z, Balazs Egert.B and Hadj Amor Essid.T 2014), exports (Bilgili.F, Ulucak.R, Soykan.M E, Erdogan.S 2019), and foreign currency debt (Neaime.S 2009, Neaime.S & Gaysset.I 2022).

However, the effects on the microeconomic level, particularly on firms, have been largely overlooked or given little attention. Given that firms play a pivotal role in the economy, it is crucial to explore the impact of flexible exchange rate regimes on their competitiveness and financial performance. This is especially important considering the dynamic and constantly evolving nature of the global economy, where the impact of exchange rate movements can have far-reaching consequences on individual firms and the wider economy.

Therefore, it is imperative that policymakers, researchers, and business leaders alike pay closer attention to the micro-level impacts of exchange rate flexibility to better understand its effects on individual firms and the economy as a whole. The limited attention given to the microeconomic level and the impact of exchange rate flexibility on individual firms is a critical gap in the existing research, given the significant role firms play in driving economic growth and development. In today's dynamic global economy, where exchange rate movements can have far-reaching effects, it is essential to explore the impact of flexible exchange rate regimes on individual firms' competitiveness and financial performance. Policymakers, business leaders, and researchers should pay closer attention to the micro-level impacts of exchange rate flexibility to better understand its effects on individual firms and consequently the economic growth.

## V. Conclusion

This paper undertakes an in-depth exploration of

the existing body of literature regarding the trend toward the flexibilization of exchange rate regimes in emerging economies. The objective is to provide valuable insights that can serve as a guide for policymakers and regulators when making crucial decisions about selecting the most suitable exchange rate regime for their respective countries.

The literature under scrutiny delves into various aspects of the impact of flexible exchange rate regimes on a spectrum of macroeconomic variables. These variables include but are not limited to export competitiveness, foreign direct investments (FDIs), capital flows, monetary policy formulation, susceptibility to exchange rate volatility, indebtedness levels, and overall economic performance.

The findings derived from this comprehensive review of the literature suggest that opting for a flexible exchange rate regime can yield substantial benefits for a nation's economic growth, enhance the credibility of its monetary policy, and bolster its competitiveness in the global market. However, it's crucial to note that the success of this approach hinges on the effective management of exchange rate volatility by monetary policymakers. This finding underscores the delicate balance that must be struck to reap the rewards of flexibility while minimizing potential downsides.

One noteworthy concept that emerges from the literature is the notion of the "Fear of floating," particularly relevant to emerging economies. It posits that these economies tend to benefit from a lower degree of exchange rate volatility, as it enhances the credibility of their monetary policies. Consequently, it encourages these nations to adopt a gradual or complete floatation of their currencies. This insight underscores the complexity of exchange rate regime choices in emerging economies, where policy considerations intertwine with credibility concerns.

Despite the substantial body of work in this area, a notable gap in the literature is the limited attention given to the microeconomic level, especially the impact on individual companies that isn't exploited enough. To address this gap, it would be valuable to explore how the flexibilization of exchange rate

regimes influences companies, primarily through key financial performance indicators such as financial profitability, economic profitability. Studies to conduct on these indicators may encompass other aspects noticeably solvency and turnover. Moreover, the study should consider various determining factors that can shape the impact on companies, including their size, the sector in which they actively operate, and their degree and direction of openness to foreign trade.

A more nuanced understanding of how exchange rate regime flexibilization affects companies could have significant practical implications. It could equip practitioners and policymakers with valuable insights, enabling them to better navigate and control the process of transitioning to a floating exchange rate regime for their local currency. By bridging this gap in the literature, we can further enhance our comprehension of the multifaceted dynamics at play when making critical decisions about exchange rate policies in emerging economies.

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