Notes on William Berhard and David Leblang, 'Democratic Institutions and Exchange Rate Commitments,' *International Organization*, 53, no. 1, (Winter 1999), pp.71-97

Since the collapse of the Bretton Woods system in 1971, states have been relatively free to choose to which exchange rate mechanism they ascribed. The choice boiled down to pegging the rate to another currency, floating or a multilateral regime. The authors argue that this choice is determined by the preferences of politicians, which may be separate from economic and social interests, and nature of the domestic legislative institutions.

They begin by outlining some of the competing theories which link exchange rate decisions to domestic institutions.

1. choosing a fixed exchange rate imposes external discipline which would benefit states with less internal discipline, that is, those governed by coalitions rather than majoritarian governments.
2. Weak states lack the ability to implement policies required for the fixed rate system, so it will only be found in majoritarian systems
3. Governments which are likely to see policy reversed after losing power, i.e. majoritarian governments, are more likely to try to 'tie the hands' of their successors, which can best be done with a fixed exchange rate system.

These three contradictory theories all fail to take into account the preferences of politicians.

The authors' theory, taking politicians preference for re-election as a starting point, suggests that in a decisive electoral system, where the electoral system tends to produce single party governments, the party in power will want to maximize its chances for re-election by maintaining monetary control over the economy. It can do this more easily with a floating currency. In a proportional representation system where coalitions are frequent, the costs of a fixed rate may not preclude a party from participating in government, and a fixed rate may provide a focal point for parties in a coalition with highly variable policies an opinions. Hence in a proportional representation system, fixed rate policies will be preferred.

The authors then test the theory, coding states on their electoral systems and including tests for the influence of other factors on the choice of fixed versus float, including international systemic factors such as dependence on trade, vulnerability to shocks and mobility of capital and domestic economic and political factors.

The results of the analysis, using both multinomial and binomial logit, support the authors' theory. In the multinomial test, holding other variables at their means, that politicians in a majoritarian government are 82% more likely to join a floating system than those in a proportional system. The value in the binomial test was 65%. The results did not change markedly over time or when the sample was restricted to those states which changed their policies. Partisanship also had little effect, suggesting ideology has little impact on the regime chosen.

The authors conclude by noting the literature which argues that states have little choice over the regime they adopt and that the demands on politicians have changed. The authors counter that politicians are the ones who respond, and that institutions, some of which will expose politicians to the effects of internationalization, others of which will offer shelter, will determine how politicians will pursue their interests.