CHAPTER VI

CONCLUSIONS AND RECOMMENDATIONS

Based on the empirical results of study and discussion from the previous chapter, the main objective of this research is to examine the impact of trade open, government expenditure, net capital inflow and foreign aid on Real Exchange Rate in Indonesia over annual period 1981 - 2013. In this study, the writer used Error Correction Model (ECM) model empirically test the impact of trade open, government expenditure, net capital inflow and foreign aid on Real Exchange Rate in Indonesia. From the analysis of data that has been conducted, it is obtained the following conclusions and recommendations.

6.1 Conclusions

The exchange rate is very important, if a country must conduct economic transactions with other countries. In economics, the exchange rate of a country's currency can be divided into two, namely the real exchange rate and nominal exchange rate (Mankiw, 2006). The nominal exchange rate is the value that is used when exchanging the currency of a country with the currency of another country. While the real exchange rate states the rate at which someone can trade goods or services from a country with goods or services from other countries.

Government expenditure has positive and significant impact to real exchange rate in short run. It shows that increase in government expenditure has appreciate real exchange rate in indonesia. Meanwhile, government expenditure has negative and significant impact to real exchange rate in long run. According Prabawa (

2013), Based on government expenditure data, government consumption used for personnel expenditure, depreciation and expenditure of goods, both central and local government, so that this component is not a productive and significant expenditure in affecting the real exchange rate in the long term.

6.2 Recommendations

The exchange rate becomes important because the exchange rate can be used as an instrument to measure the economic condition of a country. A country that has a stable currency value indicates that the country has stable economic conditions (Salvatore, 1997). Extremely high exchange rate fluctuations will disrupt economic activity from both the real sector and the monetary sector. So good exchange rate management is required in order for the movement of the exchange rate to be stable so that fluctuations can be predicted and the economy can continue to run well. Government should control government expenditure in indonesia, because in long run government expenditure has negative on real exchange rate and also government should keep stably real exchange rate in short run and long run.