CHAPTER 5

CONCLUSION AND RECOMMENDATION

5.1. Conclusion

This study explored the potential spillovers of monetary policy from the US to Indonesia, the transmission mechanisms, and the economic implications of those spillovers. Using quantitative approaches the study revealed that changes in U.S. monetary policy especially interest rate changes greatly have affected Indonesia's exchange rates, inflation, and stability of financial market. The result confirmed the previous studies which showed the financial turbulence in the case of the United States monetary tightening period resulted in capital outflows, depreciation of the Rupiah and raising inflationary pressure, for example, during 2013 Taper Tantrum.

The outcomes underscore the exchange rate channel as an important vehicle of transmission, with variations in the U.S. dollar significantly affecting the Indonesian Rupiah. This depreciation of the currency usually amplifies inflation via rising import prices, particularly in periods of global financial instability. The research also indicated that Bank Indonesia's actions, particularly its interest rate policy and its interventions in the foreign exchange market, played a crucial role in mitigating the detrimental impact of external factors on the nation's economy, highlighting the mediating role of domestic monetary policy.

The study also noted Indonesia's growing vulnerability to global monetary spillovers, due to its reliance on commodity exports and financial liberalization. These findings emphasize Indonesia's challenge to design a monetary policy that must determine a time-consistent monetary independence concerning its exchange rate, following the international policy trilemma propounded by Mundell (1963) and Fleming (1962). That balance is necessary because it increases resiliency to external shocks, and supports longer-term economic stability.

5.2. Recommendation

With a view to strengthening economic resilience and minimising negative side-effects arising from cross-country spillovers of monetary policy, the following recommendations are made:

1. Strengthening Foreign Exchange Reserves:
   Part of efforts to keep Indonesia's economy resilient to sudden capital flow reversals should be to build up sizeable foreign exchange reserves. Adequate reserve levels will support Bank Indonesia’s ability to intervene in foreign exchange markets to prevent excessive volatility of the Rupiah from triggering unnecessary economic instability, particularly in challenging times.
2. Diversifying the Economy:
   Policies must drive the development of high-value sectors (such as manufacturing and digital services) to reduce reliance on commodity exports. Investing in infra, technology and education will hold the key to economic diversification and resilience to changes in global commodity prices.
3. Enhancing Regional Cooperation:
   Regional collaboration via initiatives like ASEAN+3 can likewise enhance financial safety nets for Indonesia during a crisis. Together, all these will contribute to ensuring critical liquidity support and reinforcing regional financial stability by broadening mechanisms such as the Chiang Mai Initiative Multilateralization (CMIM).
4. Improving Monetary Policy Communication:
   Bank Indonesia needs to communicate clearly and transparently in a future-oriented way to manage the expectations of the market and break momentum trading behaviour. This can build confidence among local investors by aligning domestic policy signals with conditions of the international financial system and so help smoother capital flows and less volatility.
5. Promoting Sustainable Investment:
   By offering good incentives and guarantee on an acceptable stable regulation, encourage long-term foreign direct investment (FDI) to strengthen the resilience of Indonesia’s economy. Pro-green and pro-sustainable development policies can also

attract global investors who follow environmental social governance (ESG) principles of investment, thus ensuring a more sustainable and stable capital base.

6. Global Policy Coordination:

   Indonesia must push for global monetary policies to be coordinated and creates solutions to systemic risk arising from the unilateral movements of the major economies. Participation in the G20 and other such platforms is vital to ensuring the integration of developing country needs and concerns into international processes.