

CHAPTER V

CONCLUSION AND RECOMMENDATION

5.1 Conclusion

This study will investigate the dynamic effects of the Global Economic Policy Uncertainty (GEPU), global oil prices, and the BI Rate on Indonesia's stock market performance proxied by the Jakarta Composite Index (IHSG) within the VAR framework. The preliminary test results indicate that oil prices and IHSG are stationary at first difference after being non-stationary at level, whereas the GEPU and the BI Rate are stationary at level. Two lags are selected for the model, and the stability test confirms that all roots of the characteristic equation lie inside the unit circle, indicating stability in the estimated model. This empirical evidence provides a strong foundation to examine the effects of global uncertainty, commodity price shocks, and monetary policy on Indonesia's stock market behavior.

Based on the results obtained, it can be stated that GEPU will not become the main lagged predictor of IHSG movements in an absolute and autonomous way. However, the Granger causality results reject any statistically significant causal relationship from GEPU to IHSG. Hence, global uncertainty does not always spillover into delayed market adjustments. Nevertheless, the finding of significant contemporaneous relationships indicates that global uncertainty is transmitted swiftly into the Indonesian market via investor sentiment, changing expectations, and the immediate repricing of risk. This implies that the ways in which GEPU impacts stock market performance are not so much as a source of fluctuations in your stock market, but as a channel through which wider global shocks are transferred and consequently absorbed by your domestic market.

The different short-run and long-run effects are significant in explaining the role of global uncertainty in Indonesia's stock market. Impulse response analysis results show that, the shocks within the system lead to responses which are transient and taper off as time passes, implying that the uncertainty related shocks to the system do not lead to permanent changes in the way the markets behave at least in the short run. This trend indicates that although higher uncertainty in global events will result in volatility, the effects will tend to become less pronounced over time as the system adjusts itself back to equilibrium following incorporation of the new

information. On the other hand, a cointegration test conducted using Johansen cointegration method shows that there exists a long-term equilibrium relationship between GEPU, oil price, IHSG, and BI rate, indicating that higher uncertainty in global events is still incorporated into a wider structural framework.

Domestic macro factors that have relations with GEPU can be seen in the relationship between oil price and BI rate. Based on the outcome of the Granger causality test, both oil price and BI rate are categorized as two important sources of shocks in the system. This means that commodity price changes and domestic monetary policy have a higher importance compared to GEPU in affecting the market. As for the oil price, this represents a kind of exogenous shock that can be affected by the situation in the global commodity market, geopolitics, and global commodity demand. On the other hand, the BI rate functions as an adjustment mechanism in the domestic area, and thus the importance of monetary policy cannot be overlooked.

This view is supported further by FEVD analysis, according to which all of the variables are first explained through the shocks from themselves, while the contribution of Oil Prices and BI Rate in explaining the IHSG becomes increasingly important as time progresses. Such results imply that Indonesian stock market is not only affected by its internal impulses but also by external commodity conditions and domestic responses to such impulses as well. Within this framework, the transmission of uncertainty also received support from the GEPU, with oil prices and monetary policy acting as the more dominant drivers of adjustment in the system. It thus seems that the stock market reacts more to situations where rising uncertainty is coupled with changing real exogenous conditions and policy variables than when uncertainty rises alone.

5.2 Recommendations

1. Policy Recommendations

- Bank Indonesia should continue to strengthen its monetary policy framework by monitoring oil price fluctuations in the world due to the role they play as a major source of external shock to the domestic economy.

- Finally, the government should coordinate implement policies that are able to reduce the economic policy uncertainty. This is particularly important to ensure that the financial markets remain stable.
- Uncertainty shocks could be reduced if the government can improve the transparency and consistency of their economic policy making. In turn, this will help to engender investor confidence in the Indonesian economy.

2. Recommendations for Future Research

- Moreover, future research can extend the model by incorporating other macro variables like inflation, exchange rate, or economic growth.
- Structural breaks might occur in the form of nonlinear VAR or time-varying parameter models. The structural change models reveal how the connections between variables shift over time.
- Another suggestion for future work is sub-period analysis, which could be conducted by comparing pre-and post-crisis periods to understand the transmission mechanisms among variables.

