

INTERNATIONAL CONFERENCE PROCEEDING

**BUSINESS MANAGEMENT:
DIRECTIONS AND STRATEGIES
IN RESPONSE TO
ASEAN ECONOMIC COMMUNITY 2015**



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FACULTY OF ECONOMICS
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Jember, 2 November 2013

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**UNIVERSITY OF JEMBER
FACULTY OF ECONOMICS
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MOVEMENT EFFECTS OF PORTFOLIO INVESTMENT AGAINST REAL EFFECTIVE EXCHANGE RATE STABILITY IN ASEAN

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Abstract

Effort to attract foreign investment in form of portfolio is very important for developing countries. However, the portfolio investment establishment policies of financial liberalization in ASEAN can lead to real exchange rate appreciation and may have the effect of exchange rate competitiveness, harm exports and economic growth fluctuation. This research was intended to identify the performance and comparison of the movement of portfolio investment and foreign direct investment and to analyze portfolio investment linkage and real effective exchange rate in ASEAN. The analysis results by Generalized Method of Moment (GMM) provided an illustration that Indonesia, Malaysia and The Philippines had a positive significant impact on the real effective exchange rate stability. Meanwhile, Singapore and Thailand had a negative insignificant relationship. Portfolio investment flowing on the free floating exchange rate system causes an appreciation of real effective exchange rate which affects the rising price of domestic assets in the foreign exchange market. Government intervention in the determination of exchange rates on the floating exchange rate system causes less productive mechanism of inter-country trade. However, portfolio investment flows can be easily controlled, so the real effective exchange rate becomes uncompetitive against the currencies of other countries which are the main trading partners.

Keywords: portfolio investment, real effective exchange rate, GMM approach, ASEAN

INTRODUCTION

The flow of capital in the ASEAN region is increasingly higher by the increasingly more integrated finance in the region. This is reflected in the high capital flows to emerging markets, as well as indicators of region restrictions and transparency of capital flows

ASEAN ECONOMIC AND MONETARY INTEGRATION: THE FEASIBILITY OF THE OPTIMUM CURRENCY AREA

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Abstract

Economic integration in recent years has become a trend in many parts of the world, including ASEAN. The process of economic integration in ASEAN has begun with economic cooperations that lead to the establishment of the ASEAN Economic Community (AEC). Follow-up of the ASEAN economic community is area with the establishment of a regional currency. The purposes of this study are to analyze the opportunity of establishment of the currency area in ASEAN and to analyze the relationship between the exchange rate variability and the forming OCA-index variables in the short and long term. This study focused on two analyses; the descriptive analysis and quantitative analysis using the Error Correction Model (ECM). The results of descriptive and quantitative analysis showed that the ASEAN countries have diverging economies. It is an obstacle to the establishment for the currency area because the divergence of economies in those countries will make the regional policy ineffective. However, the opportunity of the establishment of the currency area in ASEAN is still open, especially in the long run. This is supported by the increasingly smaller economic divergence between the ASEAN countries and the OCA index that is not too high.

Keywords: Optimum currency area, OCA index, ECM, ASEAN

INTRODUCTION

Opportunities formation of a currency area in the region was first disclosed by Mundel in 1961. Ramayandi and Tjahjawardita (2010) define the currency area as a region where there is only one currency in circulation in the region. Meanwhile, Saichu (2007)



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