the increasing degree of openness of the sector to international trade. This relatively high degree of openness may also be the reason that exchange rate uncertainty imposes positive impacts to the volume of trade of this trade sector.

Furthermore, it is estimated that an increase of exchange rate uncertainty by one percentage point can cause an increase of the sector's volume of trade by 0.79 to 0.58 percentage point.

CHAPTER 6

CONCLUSIONS AND REMARKS

6.1. Conclusions

There are several conclusions that can be drawn from this research. They are:

a) The level of real exchange rate uncertainty under the period of fixed-exchange rate regime in Indonesia (1986-1997) is not strictly below the level of real exchange rate uncertainty under the period of free-floating exchange rate regime (1997-2006). High level of real exchange rate regime during the adoption of fixed-exchange rate regime may occur due to rapid devaluation. Similar evidence also found by Langley et al. (2000) in Thailand. They found that exchange rate volatility eras may happen during fixed-exchange rate regime. These eras coincide with rapid devaluation and opening of the financial sector. Moreover, calculated exchange rate uncertainty for the sample of this research is presented in Appendix.

b) Product of Indonesia and trading partner's GDP per capita is positively related to trade. This result implies an increase of product of GDP per capita can be seen as an increase of income and purchasing power. Increase of purchasing power leads to higher ability to consume goods and services which can be reflected to increase in international trade as well. Similar evidence also found by Cho et al. (2002) and Rose (2004).

c) Product of Indonesia and trading partner's population is positively related to trade. This results implies that the more population live in trading partners, the more demand of goods and services and the more capability to produce goods and services. Therefore, more population may lead to more international trade. Similar result is also found by Cho et al. (2002) and Rose (2004).

d) Distance as a proxy of transport cost is negatively related to trade. This result implies that increase of distance means higher transport cost. Moreover, higher transport costs make international trade to be more expensive. Thus, higher transport costs discourage international trade. Similar evidence is also found by Cho et al (2002) and Rose (2004).

e) Real exchange rate uncertainty imposes different impacts on different trade sectors. Negative impacts are usually found in trade sectors which have protected commodities or which can be easily substituted with domestic production. Positive impacts are usually found in trade sectors which have high level of openness, high level of industry concentration and high level of multinational activities or high level of foreign direct investments. Similar evidence also found by Maskus (1986). However, this research differs with the findings of Maskus (1986) and Cho et al. (2002) in terms of the impact of exchange rate uncertainty of agricultural products. Maskus (1986) and Cho et al (2002) find that agricultural products are usually imposed the most severe negative impacts by exchange rate uncertainty. This research finds that agricultural products may also have positive relation with exchange rate uncertainty.

6.2. Research Limitations

The research has several limitations in its study. They are:

a) Main trading partners chosen may be not the best sample of the whole population of Indonesia's bilateral trade. Especially since economic crisis, there are changes in the rank of importance of trading partners. For example, there is increasing importance of China as Indonesia's trading partner since 1998.

b) The measure of exchange rate uncertainty is arbitrarily chosen. The measure used may not be the best measurement of exchange rate uncertainty. However, there is no conclusive opinion available in literatures about the best measure of exchange rate uncertainty.

c) The research does not incorporate third-country risk effects as proposed by Cushman (1986). Cushman elaborates that bilateral trade may increase due to increase of exchange rate risk of third country. It implies that relative exchange rate uncertainty may affect bilateral trade. Thus, there may be bias in the results due to expulsion of this third-country risk effect in the model.

6.3. Suggestions

The findings of this research affirm that exchange rate uncertainty as not always a disadvantage to international trade, rather it can act as a virtue as well. Therefore, actions or policies to redeem exchange rate uncertainty are not obligated to be implemented. Similar suggestion also proposed by Maskus (1986). He argues that although exchange rate uncertainty may discourage international trade, the costs of policies to reduce exchange rate uncertainty may be outweighed by the gain from lower exchange rate risk.