UNIVERSITI TEKNOLOGI MARA

IMPACT OF ECONOMIC FACTORS TOWARDS EXCHANGE RATE IN MALAYSIA

NUR SYAHIRAH BT JAMALUDIN
2020968955

Final Year Project submitted in fulfillment of
the requirements for degree of
Bachelor of Business Administration (Hons)
Investment Management

Faculty of Business and Management

FEBRUARY 2022

ABSTRACT

This paper aims to study the relationship between exchange rate and Gross Domestic Product (GDP), inflation and interest rate in Malaysia. Time series data over the period of 1991 to 2020, a total of 30 observations have been collected from World Bank Data. It also discusses the effect of economic factors towards the exchange rate using regression analysis to determine whether these factors will affect the exchange rate or not. The findings have concluded that all of the independent variables GDP, inflation and interest rate have a positive relationship with the exchange rate and are statistically significant, influencing the exchange rate during the study period. The model does not suffer from the multicollinearity, serial correlation and heteroskedasticity while being tested. Currency fluctuations are a natural result of most major countries' use of variable exchange rates. As a result, the value of a currency might change from one moment to the next. The Asian Financial Crisis, which began with the depreciation of the Thai baht in the summer of 1997, is a good illustration of the chaos created by unfavourable currency movements. This currency contagion expanded to neighbouring nations including Indonesia, Malaysia, and South Korea, causing severe economic contractions as bankruptcies and stock markets fell. So this study will concentrate on Malaysia as one of the countries that was affected by the Asian Financial crisis to help us be more prepared in the future.

Keywords: Exchange Rate, Gross Domestic Product (GDP), Inflation, Interest Rate, Malaysia

Table of Contents

CHAPTER 1: INTRODUCTION

1.1 Introduction

One of the most significant predictors of a country's relative economic health is its currency exchange rate. Exchange rates are important in determining a country's amount of commerce, which is crucial in almost every free market nation on earth. As a result, exchange rates are one of the most closely monitored, examined, and manipulated economic indicators. Malaysia's national currency is the ringgit, which is a Southeast Asian currency.In international currency exchange markets, the currency is abbreviated as MYR. The Malaysian Ringgit is issued and controlled by Bank Negara Malaysia,the country's central bank (Pilania, 2021). At the moment, Covid-19 is another factor influencing the ringgit. The ringgit has fallen to its lowest level versus the US dollar, as the US dollar rose on demand for haven currencies amid global economic uncertainty caused by the Covid-19 epidemic and lower crude oil prices (Adam, 2020). Malaysia's currency rate for one US dollar in March 2019 was RM4.08,and it has since fallen to RM4.26 in July 2020. The ringgit appreciated by 0.1% against the US dollar in the second quarter of 2021.This was largely due to the weakening of the US dollar in the earlier part of the quarter as a result of declining real US Treasury bond yields which led investors towards higher-yielding assets (Central Bank of Malaysia).

The foreign exchange rate can be used to determine the relative state of the economy.Apart from the Asian crisis of 1997 to 1998, economic fundamentals are also important for the ringgit (Shahrier,2020). For many firms, 2015 was a trying year as they dealt with not just a sluggish economy but also unprecedented currency volatility since the Asian financial crisis of 1997-1998.The ringgit,like other regional currencies, has been beaten and wounded. The effects of the ringgit's depreciation have been felt by everyone from large organisations to small and medium-sized businesses (SMEs). The impact is not limited to the corporate community; the average person has also been affected by rising import prices.The dangers that firms face during periods of currency volatility go beyond these factors,and frequently into areas that aren't immediately apparent. Even if a company does not trade internationally,it may be harmed. Even if companies are not involved in international trade,businesses must be aware that foreign