

THE IMPACT OF INFLATION AND FOREIGN
EXCHANGE FLUCTUATION ON
MANUFACTURING SECTOR:
COMPARISON BETWEEN MALAYSIA AND
SINGAPORE

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APRIL 2007




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"DECLARATION OF ORIGINAL WORK"

I, Nadia binti Kamarul Ariffin, (I/C: 820703105890)

Hereby, declare that,

- This work has not previously been accepted in substance for any degree, locally or overseas and is not being concurrently submitted for this degree or any other degrees
- This project paper is the result of my independent work and investigation, except where otherwise stated
- All verbatim extracts have been distinguished by quotation marks and sources of my information have been specifically acknowledged.

Signature: 

Date: 12 MAY 2007

LETTER OF SUBMISSION

30 APRIL 2007

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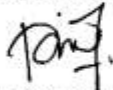
Dear Sir,

SUBMISSION OF PROJECT PAPER

Attached is the project paper titled "THE IMPACT OF INFLATION AND FOREIGN EXCHANGE FLUCTUATION ON MANUFACTURING SECTOR: COMPARISON BETWEEN MALAYSIA AND SINGAPORE" to fulfill the requirement as needed by the Faculty of Business Management, Universiti Teknologi MARA.

Thank you

Yours sincerely



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ABSTRACT

Several studies show that certain companies were uniquely affected by the changes of Consumer Price Index (CPI) and foreign exchange (FOREX) fluctuation. This project paper tries to find the effect of inflation and FOREX fluctuations on manufacturing sector by comparing the impact in Malaysia and Singapore. This study tries to achieve two objectives; (1) to identify the correlation of inflation fluctuations on the manufacturing sector, and (2) to identify the correlation of exchange rate fluctuations on the manufacturing sector. The independent variables were the quarter CPI rates and the quarter exchange rates from 1996 to 2005, while the dependent variables were 40 companies' return on equity from Malaysia and Singapore.

The panel data regression was employed to measure the impact of inflation and exchange rates to the return on equities of the manufacturing companies. The panel data regression model had regress the data for each forty companies, but the result is represented in the overall manufacturing sector performance for both countries. The result found that the manufacturing sector for the Singaporean companies was negatively affected by the inflation fluctuations, but the manufacturing sector for the Malaysian companies seems to be not affected. While the manufacturing sector for both countries seems to be affected by the exchange rate fluctuations with Malaysian companies were negatively affected and the Singaporean companies were positively affected.

CHAPTER 1

INTRODUCTION

1.0 Background of the Study

It is a widely held view that exchange-rate movements and inflation fluctuation should affect corporate expected cash flows, and hence stock returns, by causing changes in the home currency value of foreign currency denominated revenues (costs) and the terms of competition for multinationals and firms with international activities (importers and exporters). To study the implications of exchange rate and inflation towards company performance, this paper examines the responses of those both economic exposures to the manufacturing sector by comparing the impact between Malaysia and Singapore.

This paper answers two questions. First, what is the correlation between exchange rate exposure and the manufacturing sector? Second, what is the correlation between inflation rate exposure and the manufacturing sector? Answering both questions help to find the effect of exchange rate and inflation rate toward the return on equity of manufacturing sectors in Malaysia and Singapore.

Two empirical findings are reported to be at the origin of this interest, which is a negative association between inflation and economic growth (Barro, 1995) and a positive relationship between the development of the financial system and economic growth. These two strands of the empirical literature (the finance-growth and inflation-growth relationship) have lived separate lives but one obvious link is that inflation might be affecting economic growth through the financial sector.