

CHAPTER V

CONCLUSION

5.1 Conclusion

Based on the results of this study on the Impact of the Federal Funds Rate, Exchange Rate, and Money Supply on Inflation in Indonesia using the ARDL method, The following conclusions can be constructed::

1. The Federal Funds Rate has a significant effect on Indonesia's inflation in the short run but not in the long run. In the short run, when the Fed raises its interest rate, it tends to push Indonesian inflation up slightly in the following month, but this effect is partially reversed the month after. This happens because a higher Fed rate causes investors to pull their money out of Indonesia, which weakens the rupiah and makes imported goods more expensive, temporarily pushing prices up. However, in the long run, this effect fades away, most likely because Bank Indonesia adjusts its own policies to counteract the pressure coming from US monetary decisions, preventing a permanent impact on domestic prices.
2. The exchange rate has a significant effect on Indonesia's inflation, but the effect takes time to show up. In the short run, changes in the rupiah exchange rate do not immediately affect inflation and only become significant after three months, with a negative direction. This means that when the rupiah weakens, it does not instantly raise prices. Instead, after a few months, the reduced purchasing power of households tends to slow down spending and demand, which can actually hold back price increases. In the long run, the exchange rate is significant at the

10% level, confirming that currency movements do have a meaningful connection to inflation in Indonesia over time, even if the relationship is not very strong.

3. The money supply does not have a significant effect on Indonesia's inflation in either the short run or the long run. Even though Indonesia's broad money supply grew consistently throughout the observation period, this growth did not directly push inflation higher in a statistically reliable way. This suggests that Bank Indonesia has managed liquidity in the financial system well enough that increases in money supply do not automatically translate into rising prices. It also reflects the fact that inflation in Indonesia during this period was more influenced by external shocks and structural factors rather than by how much money was circulating in the economy.

4. A long-term association between the variables is confirmed by the Error Correction Model result, which displays a negative and significant CointEq(-1) coefficient of -0.104939. This means that when inflation moves away from its long-run path due to a short-run shock, about 10.49% of that gap is corrected every month, so it takes around 9 to 10 months for inflation to fully return to its normal level. This slow adjustment reflects the fact that prices in Indonesia do not change instantly and tend to be sticky, meaning it takes time for the economy to fully absorb and respond to external disturbances.

5.2 Suggestions

Based on the results and conclusions above, the following suggestions are offered:

1. For Bank Indonesia and the Government

Since the exchange rate is the variable that shows the clearest connection to inflation in this study, Bank Indonesia should keep prioritizing exchange rate stability as part of its monetary strategy. Keeping the rupiah stable and predictable helps prevent sudden spikes in import costs that could push domestic prices up, especially during periods of aggressive Fed rate hikes like what happened in 2022 and 2023. Beyond that, Bank Indonesia should also work on communicating its monetary policy decisions more clearly to the public. When people understand what is happening with interest rates and liquidity, they tend to form more stable expectations about future prices, which itself helps keep inflation under control.

2. For the Government in Fiscal and Trade Policy

Since neither the money supply nor the Federal Funds Rate shows a strong and lasting impact on inflation, this study points to the importance of non-monetary factors in driving price changes in Indonesia. The government should therefore focus more on supply-side policies, such as improving how food is distributed across the country, managing fuel and electricity prices carefully, and reducing how much Indonesia depends on imported goods for daily needs. Keeping food prices and energy costs stable is likely to be more effective in maintaining low inflation than relying only on monetary tools.

3. For Future Researchers

Future researchers are encouraged to add more variables to the model to get a fuller picture of what drives inflation in Indonesia. Variables such as global oil prices, food commodity prices, the BI interest rate, or even measures of public inflation expectations could be worth exploring. Using a longer observation period or trying different methods such as the nonlinear ARDL (NARDL) model could also be helpful, especially to test whether a weaker rupiah and a stronger rupiah affect inflation differently, since the standard ARDL model used in this study assumes the effect is the same in both directions. A study at the regional or provincial level could also be interesting, given that inflation tends to vary significantly across different parts of Indonesia.