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THE INFLUENCE OF EXCHANGE RATE FLUCTUATIONS ON TRADE AND INVESTMENTS

Abstract: this article examines how exchange rate fluctuations affect trade and investment flow in Malaysia. Exchange rate volatility has significant implications for Malaysia economy, influencing the cost of imports and exports and affecting investor confidence. The study also aims to assess the relationship between exchange rate changes and trade dynamics, while considering potential policy implications to mitigate adverse impacts.

Keywords: exchange rate, trade, investment, Malaysia, economic impact

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ВЛИЯНИЕ КОЛЕБАНИЙ ВАЛЮТНОГО КУРСА НА ТОРГОВЛЮ И ИНВЕСТИЦИИ

Аннотация: в статье рассматривается, как колебания обменного курса влияют на торговлю и инвестиционный поток в Малайзии. Нестабильность обменного курса имеет значительные последствия для экономики Малайзии, влияя на стоимость импорта и экспорта и подрывая доверие инвесторов. Исследование также направлено на оценку взаимосвязи между изменениями обменного курса и динамикой торговли, а также на рассмотрение потенциальных политических последствий для смягчения негативных последствий.

Ключевые слова: обменный курс, торговля, инвестиции, Малайзия, экономическое воздействие

Exchange rates are crucial for open economies like Malaysia, where international trade and foreign investment are vital components of economic activity. Fluctuations in exchange rates can alter the relative prices of goods and services, directly impacting trade balances, business profitability, and foreign investment flows. This article explores the effects of exchange rate volatility on Malaysia's trade and investment sectors, emphasizing the importance of a stable exchange rate for sustainable economic growth [1].

Past research has shown that exchange rate fluctuations can impact trade and investment in various ways. Studies indicate that a depreciating currency generally boosts exports by making goods cheaper abroad, while a strengthening currency has the opposite effect. For Malaysia, whose exports are highly reliant on international markets, exchange rate stability is particularly important. In addition, foreign direct investment (FDI) tends to decline when exchange rates are unstable, as uncertainty discourages long-term investment commitments [2].

This study uses an econometric approach to analyze the relationship between exchange rate fluctuations and trade and investment in Malaysia from 2000 to 2023. Data on exchange rates, trade volumes, and FDI flows were gathered from the World

Bank and Bank Negara Malaysia. A time-series analysis was conducted to evaluate the correlation between exchange rate volatility and changes in trade and investment indicators [3].

The impact of exchange rate fluctuations on trade and investment in Malaysia

1. Impact on Trade and Economic Growth: Studies indicate that fluctuations in the Malaysian Ringgit (MYR) significantly affect the country's trade. For example, currency depreciation generally harms exports by raising input costs for manufacturing, although it sometimes boosts competitive advantage for exporters in global markets. However, excessive volatility tends to dampen investor confidence, increasing transaction risks and reducing overall trade volume. According to Tam Mei Si (2021) from TAR UMT, a stable exchange rate is crucial for maintaining economic growth, as volatility has adverse impacts on Malaysia's GDP, especially during crises like the COVID-19 pandemic when the MYR experienced notable depreciation [4].

2. Sectoral Sensitivity to Exchange Rate Changes: The influence of exchange rate fluctuations varies across sectors. The financial, property, and construction sectors in Malaysia, for example, are more sensitive to currency volatility, with these industries facing increased risks during periods of depreciation. Conversely, consumer goods and industrial sectors demonstrate relatively lower sensitivity, indicating more stability amid exchange rate fluctuations. Studies suggest that the financial sector often benefits from higher revenue through hedging products during volatile periods, as highlighted by JEM (2017) [2].

3. Investment Effects: Exchange rate stability plays a crucial role in attracting Foreign Direct Investment (FDI). Research demonstrates that currency instability discourages foreign investors due to the increased risk and potential loss in value, particularly affecting sectors like manufacturing, which relies on imported raw materials. Studies indicate that maintaining a stable currency can boost FDI inflows, supporting long-term economic growth in Malaysia.

Asian Financial Crisis (1997-1998): Malaysia's MYR depreciated sharply,

prompting the government to peg the currency to the USD to stabilize it. This pegging helped control inflation and stabilize trade flows but also restricted policy flexibility.

In the year of 2008 Global Financial Crisis happened, although Malaysia had moved to a managed float system, the global economic downturn led to MYR depreciation, impacting both imports and exports. Inflation rose as import costs increased, but exports became more competitive internationally. After that, COVID-19 Pandemic in the year of (2020, The pandemic led to MYR volatility due to disruptions in global trade and economic uncertainty. Depreciation made exports cheaper, which benefited some sectors but led to increased import costs, impacting industries reliant on imported goods and raw material [4].

When the MYR depreciates, Malaysian exports like electronics, rubber, and palm oil become cheaper for foreign buyers, which can boost demand. However, industries that rely heavily on imported raw materials (such as the automotive industry) may face higher input costs, which could offset some export gains.

A weaker MYR increases the cost of imported goods, impacting consumer purchasing power. This can lead to inflation as higher import prices are passed to consumers, affecting everything from food to electronics. This inflationary pressure can decrease domestic demand and create challenges for businesses reliant on imported supplies [1].

Exchange rate stability is a priority for foreign investors, as fluctuations impact their expected returns. Investors are typically attracted to countries where they can anticipate consistent profitability. Volatility in the MYR may deter FDI, especially in capital-intensive sectors like manufacturing and technology, where capital depreciation could lead to financial losses and also. To mitigate risks, investors may diversify their portfolios across countries or assets less susceptible to exchange rate volatility. Malaysia's FDI may shift towards less volatile sectors like finance or services, where returns are less impacted by currency fluctuations.

Intervention Mechanism Bank Negara Malaysia could consider targeted

interventions to stabilize the currency during periods of significant volatility and also diversifying the export market for example by expanding trade partnerships could reduce reliance on a limited number of export destinations, spreading exchange rate risk.

Exchange rate fluctuations play a pivotal role in shaping Malaysia's economic environment, particularly in its trade and investment sectors. By managing currency stability, Malaysia can safeguard its economic growth and maintain its position in the global market.

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