

# THE USEFULNESS OF PURCHASING POWER PARITY IN MEASURING BALANCE OF TRADE AND PREDICTING EXCHANGE RATE IN MALAYSIA AND INDONESIA DURING PERIOD 1994-1998

Prepared by: Erna Yuliana Tjong

## ABSTRACT

---

The topic of this research is focus on how PPP works in Indonesia and Malaysia. The PPP is used as one of the tool for forecasting of the exchange rate but this has failed in Indonesia and Malaysia during year 1994 to 1998. According to PPP, the economy forces acting through arbitrage activities on the international commodity market will ensure that general price level of domestic goods moves in lie with the general price of foreign goods. In fact, the real movements are not solely based on the price level. There are other factors such as speculation, issues, government control and etc.

In addition, PPP also can be used to measure how sensitivity of PPP in the Balance of trade of a country. As a result, the PPP of Malaysia and Indonesia was not explained in their Balance of Trade due to comparative advantage they had.

In order o get the primary data for the research, interviewing the economic analysis and statistic research must be conducted. In addition, information obtained on the economic report in Malaysia and Indonesia.

In the literature review, there is a theoretical foundation from some previous researches; findings and result will also be mentioned.