CHAPTER V

CONCLUSIONS AND RECOMMENDATIONS

This chapter clarifies the discussion of findings in Chapter 4. According to the research findings of the analysis, several conclusions regarding international diversification and hedging policy from Indonesian perspective can be described. Several limitations of this study and recommendations for further study and finance practitioner are discussed in the last part of this chapter.

5.1 Conclusion

This study analyzed that performances of international diversification both with and without hedging policy from Indonesian perspective shows statistically significant risk reduction and superior return/risk ratio (only by TG strategy) compared to domestic performance. While by the comparison between international diversification with hedging policy and international diversification without hedging policy does not significantly differ. The comprehensive conclusion of this study is stated below:

1. Unhedged international diversification against domestic performance describes that during the research period taken, the return of international portfolio without hedging policy in Southeast Asia does not significantly differ on EQW and MVP portfolio strategies, and significantly higher return on TG portfolio strategy compared to domestic performance. While internationally unhedged diversified portfolio risk on EQW and MVP portfolio strategies shows statistically significant risk reduction, except

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for unhedged TG that is not significantly differ compared to domestic performance. Return/risk ratio of internationally unhedged EQW and MVP diversified portfolios is also not significantly different compared to domestic performance, but unhedged TG shows a significant higher value than domestic performance. Furthermore, annual overview of international portfolios also shows better performance than domestic performance. It can be concluded that international diversification in Southeast Asia provides mostly indifferent return and mostly lower risk than domestic performance. This result supports Indonesian investors to diversify their portfolio to international equity markets in Southeast Asia sub region.

2. Hedged international diversification against domestic performance describes that during the research period taken, international portfolio with hedging policy in Southeast Asia is not significantly different on EQW and MVP portfolio strategies compared to domestic performance, but it shows significantly higher return on TG portfolio strategy compared to domestic performance. While internationally hedged diversified portfolio risk on EQW, MVP and TG portfolio strategies show statistically significant risk reduction. Return/risk ratio of internationally EQW and MVP hedged diversified portfolios is not significantly different compared to domestic performance, while hedged TG show significant higher value than domestic performance. Furthermore, annual overview of international portfolios also shows better performance than domestic performance. It can be concluded that international diversification in Southeast Asia provides better return and lower risk than domestic performance. This
result supports Indonesian investor to diversify their portfolio to international equity markets in Southeast Asia sub region.

3. Hedged international diversification against unhedged international diversification shows that hedging policy provides not significant difference from Indonesian perspective. Since results are not significantly different on risk, return and return/risk ratio on hedged EQW and MVP, and TG portfolio strategies. It can be concluded that hedging policy for international diversification is not giving significant benefits for Indonesian investors if it is viewed from hypothesis testing that this study conducted but it can be helpful from descriptive approach inasmuch as the findings of hedging policy also reduced the international portfolio risk. Eventually, based on the overall findings, it is supported hedging policy for Indonesian investors that intended to diversify their portfolio internationally.

5.2 Research Limitation

This research has some limitations which may affect the research results such as:

1. Because of the limitation of researcher to obtain real forward rates data, this study uses hypothetical forward rates as an alternative.

2. Some adjustments for such extreme outcomes with return/risk ratio are needed in this research. Thus some outcomes may not be real values.

3. Monthly portfolio performance evaluation can be sensitive enough to observing hypothetical testing of means, but it is also necessary to make some observation by
using annual and 5 years portfolio performance evaluation. Monthly data is needed in order to make annual and 5 year portfolio performance evaluation.

4. International beta of equity markets is very hard to measure because of differences in currency each country. Although, beta can be favorable to measure risk to market.

5.3 Recommendation

For the next international diversification research study, the researcher hopes that:

1. The better measurement for international diversification performance such as International Capital Asset Pricing Model and the risk free rate that has been discounted. The discounted risk free rate approach is popularized by Prof. Aswath Damodaran from New York University.

2. Researcher highly recommends the next research study to measure decomposition of variance of the unhedged equally weighted portfolio, so the effect of currency risk can be observed comprehensively from the portfolio. Besides, currency rate can also be treated like an asset that can be optimized the return and risk. In the next research study, researcher hopes that currency rate can be utilized as an optimal asset and decomposed to observe the effects.

3. International equity markets index based on region and sub region can be very helpful as a benchmark in international diversification field.