



The Impact of Exchange Rate Uncertainty on the Industrial Sector Growth Using ARDL Technique

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Abstract

The industrial sector is one of the most important sectors of the Iran economy that its value-added always forms one of the major items of gross domestic product (GDP). Considering the large size of the industry and its contribution to the economy of Iran, it can be said that the accurate identification of the effective variables in this sector and the appropriate planning is of abundant importance. Exchange rate, particularly the uncertainty arising from its fluctuations, is among the variables that highly affect the performance of economy and development of various economic sectors, particularly the growth of the industry. Therefore, this study examines the impact of exchange rate uncertainty on the growth of the manufacturing sector of Iran using the quarterly data over the period of 1988 to 2008. To this end, uncertainty index arising from exchange rate fluctuations was, first, calculated by exponential generalized autoregressive conditional heteroskedasticity (EGARCH) variance model and, then, the short-run dynamic relationships and long-term cointegration were estimated through autoregressive distributed lag (ARDL) model. The results show that there is a significant negative relationship between the uncertainty of exchange rates and the growth of the industrial sector in both short-term and long-term models. Error correction factor (-0.75) also indicates the high speed of adjustment process towards the long-run model. Considering the results of this study, it is recommended to adopt proper foreign exchange, monetary, and fiscal policies to reduce exchange rate uncertainty and to use insurance models to compensate for the loss and damages caused by such uncertainty that may be sustained by the active exporters and importers in the industrial sector.

Keywords: industrial sector, economic growth, uncertainty, exchange rate

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