

DO INFLATION AND EXCHANGE RATES MATTER FOR ISLAMIC AND CONVENTIONAL STOCK INDICES? EVIDENCE FROM INDONESIA

Luqmanul Hakiem Ajuna

Institut Agama Islam Negeri Sultan Amai, Gorontalo, Indonesia

ARTICLE INFO

Article history:

Received: September 23, 2025

Revised: December 22, 2025

Accepted: December 23, 2025

Available: December 24, 2025

Keywords:

Arbitrage Pricing Theory; Composite Stock Price Index; Exchange Rate; Indonesian Sharia Stock Index; Inflation

DOI: [10.15575/fjsfm.v6i2.50349](https://doi.org/10.15575/fjsfm.v6i2.50349)

ABSTRACT

This study examines the effects of inflation and the rupiah exchange rate on stock market performance in Indonesia, with a comparative focus on the Indonesian Sharia Stock Index (ISSI) and the Indonesia Composite Stock Price Index (IHSG). Employing a quantitative approach, the study utilizes monthly secondary data from 2014 to 2023 obtained from the Indonesia Stock Exchange, Bank Indonesia, and the Central Bureau of Statistics. Multiple linear regression analysis is applied to assess both partial and simultaneous effects of macroeconomic variables on Islamic and conventional stock market indices. The empirical results reveal that inflation does not have a significant effect on either ISSI or IHSG. In contrast, the rupiah exchange rate exerts a significant influence on both indices, indicating that exchange rate movements play a more dominant role in shaping stock market performance than inflation. These findings suggest that, within the Indonesian context, exchange rate dynamics constitute a key source of systematic risk affecting both Islamic and conventional equity markets. The results provide empirical support for the Arbitrage Pricing Theory by highlighting the unequal influence of macroeconomic factors on asset prices. This study contributes to the literature by offering comparative evidence on the sensitivity of Islamic and conventional stock markets to macroeconomic conditions in an emerging economy.

*Corresponding author

e-mail: luq.h.ajuna@iaingorontalo.ac.id

1 Introduction

The relationship between macroeconomic variables and stock market performance remains a central concern for investors and policymakers, particularly in emerging markets characterized by high economic volatility and exposure to external shocks. Stock market indices function not only as indicators of current economic conditions but also as reflections of investor expectations regarding macroeconomic stability, policy credibility, and future growth prospects. Consequently, understanding how key macroeconomic variables—especially inflation and exchange rates—affect stock market performance is essential for informed investment decisions and effective policy formulation.

In Indonesia, this issue is further complicated by the coexistence of two major stock market indices within a dual market structure: the Composite Stock Price Index (IHSG), representing the conventional equity market, and the Indonesia Sharia Stock Index (ISSI), which consists exclusively of sharia-compliant stocks. While IHSG covers firms across a wide range of sectors, including finance, commodities, and services, ISSI is more concentrated in real-sector firms due to Islamic screening criteria such as leverage restrictions and prohibitions on speculative and non-halal activities. These structural differences suggest that Islamic and conventional stock indices may respond differently to macroeconomic shocks.

Macroeconomic theory posits that inflation and exchange rates influence stock prices through multiple transmission channels. Inflation affects corporate profitability by increasing production costs and eroding real investment returns, potentially depressing stock valuations (Mankiw, 2018; Boediono, 2019). Exchange rate movements influence firms' cost structures, export competitiveness, foreign **debt** burdens, and cross-border capital flows, making exchange rate stability a critical determinant of stock market performance in open economies (Krugman & Obstfeld, 2018; Salvatore, 2015). However, despite these theoretical linkages, empirical findings remain inconsistent, particularly in emerging markets such as Indonesia (Harsono, 2018).

Recent empirical evidence published between 2019 and 2025 highlights persistent inconsistencies in the inflation–stock market relationship. Cointegration and vector error correction model (VECM) studies document long-run relationships between inflation and Indonesian stock indices, though with varying directions and magnitudes (Dewi & Fauzan, 2023; Laksono., 2024). Some regression-based studies report significant negative effects of inflation on both IHSG and ISSI (Nugroho, et al., 2023; Katmas & Indarningsih, 2022; Handriani, et al., 2021; Ratnaningrum, et al., 2023), while others find no statistically significant effects in either the short or long run (Rapach, 2022; Otieno, et al., 2019). These divergent results suggest that inflation effects may be highly sensitive to sample periods, econometric specifications, and structural breaks, particularly during crisis episodes (Canarella & Miller, 2016; Abbate, Eckmeier & Prieto, 2023).

Evidence regarding exchange rate effects is similarly mixed, though somewhat more consistent in finding significant relationships. Error correction and VECM studies indicate that the rupiah exchange rate significantly influences IHSG and ISSI, both in the short and long run (Ratnaningrum, et al., 2023; Dinata, et al., 2025; Vikaliana, 2017; Handriani, et al., 2021; Nugroho, et al., 2023; Amal & Musthofa, 2023). Event-based analyses during the COVID-19 crisis show that rupiah depreciation exerted negative effects on Indonesian

stock indices (Priyono & Kartiko, 2021; Marpaung & Pangestuti, 2024). However, multivariate regression studies report mixed coefficient signs, suggesting that exchange rate transmission mechanisms may differ across economic regimes and between export-oriented and import-dependent firms (Yildirim & Ivrendi, 2016; Demir & Razmi, 2022).

Most critically, direct comparative empirical analyses examining whether Islamic and conventional stock indices respond differently to macroeconomic shocks remain limited. Existing studies predominantly analyze ISSI and IHSG separately or focus on performance and volatility comparisons rather than on macroeconomic transmission mechanisms. As a result, definitive conclusions regarding differential macroeconomic sensitivities between sharia-compliant and conventional indices remain elusive.

These limitations reveal several important research gaps. Empirically, the absence of rigorous head-to-head comparisons constrains understanding of differential macroeconomic transmission across market segments. Methodologically, substantial heterogeneity across econometric approaches complicates reconciliation of conflicting findings. Temporally, the 2014–2023 period encompasses multiple economic regimes—including the 2018 U.S. Federal Reserve tightening, the 2020 COVID-19 shock, and the 2023 global inflation surge—yet remains underexplored. Theoretically, limited attention has been given to explaining why sharia-compliant indices, characterized by real-sector orientation and financial screening, may exhibit distinct macroeconomic responses.

Against this backdrop, this study conducts a comparative analysis of the effects of inflation and the rupiah exchange rate on ISSI and IHSG over the 2014–2023 period within a unified analytical framework. By examining both indices simultaneously using consistent data and methodology, this study enables direct statistical comparison of macroeconomic sensitivities across market segments. The findings are expected to contribute to the literature on macroeconomic transmission in segmented capital markets and to provide practical insights for investors, policymakers, and Islamic finance practitioners in Indonesia's dual-index system.

2 Literature Review

2.1. Theoretical Framework: Arbitrage Pricing Theory (APT)

Arbitrage Pricing Theory (APT) developed by Ross (1976) explains that asset returns are influenced by multiple systematic risk factors rather than a single market factor as proposed by the Capital Asset Pricing Model (CAPM). APT allows macroeconomic variables—such as inflation and exchange rates—to function as common risk factors that systematically affect expected returns across financial assets (Reinganum, 1981). Within this framework, changes in macroeconomic conditions influence stock prices through their impact on expected cash flows and required risk premiums. Inflation and exchange rate movements alter firms' cost structures, real profitability, and valuation fundamentals, which are subsequently reflected in stock prices and market indices (Shapiro, 1975).

In the Indonesian capital market, both the Indonesia Composite Stock Price Index (IHSG) and the Indonesian Sharia Stock Index (ISSI) represent aggregated equity valuations that respond to macroeconomic shocks. Although ISSI consists of sharia-compliant stocks subject to screening criteria such as leverage limits and restrictions on interest-based activities, these criteria do not eliminate exposure to systematic

macroeconomic risks. Consequently, under the APT framework, inflation and exchange rate fluctuations are expected to affect both conventional and Islamic stock indices, although the magnitude of the impact may differ due to differences in sectoral composition and financial structure.

2.2. Inflation and Stock Market Performance

Inflation is defined as a sustained increase in the general price level that reduces purchasing power and increases economic uncertainty (Abaioo & Agyapong, 2024). From a capital market perspective, inflation influences stock prices through several interrelated channels. Rising inflation increases firms' production and operating costs, elevates discount rates applied to future cash flows, and raises required risk premiums, which collectively reduce the present value of expected corporate earnings (Fama & Schwert, 1977). In emerging markets, inflation instability is often exacerbated by weaker institutional frameworks and higher macroeconomic volatility, resulting in stronger negative reactions from equity investors.

Empirical studies generally document a negative relationship between inflation and stock market performance, particularly in emerging economies. In Indonesia, several studies find that inflation exerts a significant negative effect on the Indonesia Composite Stock Price Index (IHSG), indicating that higher inflation tends to weaken overall market performance ((Nugroho, et al., 2023; Katmas & Indarningsih, 2022; Handriani, et al., 2021; Ratnaningrum, et al., 2023). Although empirical evidence focusing specifically on the Indonesian Sharia Stock Index (ISSI) remains relatively limited, existing research suggests that Islamic stock indices exhibit sensitivities to inflationary pressures comparable to those of conventional indices, despite the application of sharia screening mechanisms (Robiyanto, 2017).

Since inflation directly affects fundamental valuation components—such as expected cash flows, discount rates, and risk perceptions—across all equity assets, both conventional and Islamic stock indices are expected to respond negatively to inflationary shocks (Umar, et al., 2020; Bahloul et al., 2017; Naifar, 2016). Accordingly, the following hypotheses are proposed:

H₁: Inflation has a significant negative effect on the Indonesian Sharia Stock Index (ISSI).

H₂: Inflation has a significant negative effect on the Indonesia Composite Stock Price Index (IHSG).

2.3. Exchange Rate and Stock Market Performance

Exchange rate movements represent a key transmission channel through which macroeconomic shocks affect financial markets, particularly in open and emerging economies such as Indonesia (Krugman & Obstfeld, 2018). Currency depreciation increases import costs, raises the domestic burden of foreign-denominated debt, and heightens macroeconomic uncertainty, thereby weakening corporate profitability and investor confidence (Salvatore, 2015). These effects are especially pronounced in economies that rely heavily on imported inputs and foreign capital inflows.

Although Islamic stock indices are constructed using sharia screening criteria—such as leverage limits and restrictions on interest-based activities—firms included in ISSI remain exposed to exchange rate risk through trade activities, foreign investment flows, and broader macroeconomic transmission mechanisms (Dewandaru et al., 2014). Empirical studies indicate that both Islamic and conventional stock indices respond to exchange rate movements, with differences in magnitude largely attributable to variations in sectoral

composition and financial structure, particularly leverage constraints (Ratnaningrum, et al., 2023; Dinata, et al., 2025; Vikaliana, 2017; Handriani, et al., 2021; Nugroho, et al., 2023; Amal & Musthofa, 2023).

Given Indonesia's economic structure as a net importing and foreign capital-dependent economy, exchange rate depreciation is expected to exert negative pressure on stock market performance by increasing production costs, worsening corporate balance sheets, and triggering capital outflows. Therefore, the following hypotheses are formulated: **H₃**: Exchange rate depreciation has a significant negative effect on the Indonesian Sharia Stock Index (ISSI).

H₄: Exchange rate depreciation has a significant negative effect on the Indonesia Composite Stock Price Index (IHSG).

3 Research Methods

This study employs a quantitative descriptive approach using secondary data obtained from official sources, including the Indonesia Stock Exchange (IDX), the Central Bureau of Statistics, and Bank Indonesia. Data collection is conducted through a documentation method, utilizing published statistical reports and financial data relevant to the research variables. Prior to empirical analysis, the data are subjected to classical assumption tests to ensure the validity and reliability of the regression model.

Multiple linear regression analysis is applied to examine the effect of inflation and exchange rate variables on stock market performance. Specifically, the analysis evaluates both partial and simultaneous effects of inflation and exchange rates on the Indonesian Sharia Stock Index (ISSI) and the Indonesia Composite Stock Price Index (IHSG). This approach enables the assessment of the magnitude and direction of the relationships between macroeconomic variables and stock market indices.

4 Results and Discussion

4.1. Result

4.1.1. Descriptive Statistics

This study employs multiple linear regression analysis to examine the effect of inflation and exchange rates on the Indonesian Sharia Stock Index (ISSI) and the Indonesia Composite Stock Price Index (IHSG). The analysis is based on **120 observations**, consisting of monthly data covering the period **2014–2023**.

Descriptive statistical analysis is conducted to provide an overview of the data characteristics for each variable. The statistics reported include the mean, standard deviation, minimum value, and maximum value for the dependent variables (ISSI and IHSG) and the independent variables (inflation and exchange rate). The results of the descriptive statistics are presented in Table 1.

Table 1 Statistic Descriptive

Variable	N	Minimum	Maximum	Mean	Std. Deviation
Inflation	120	132	836	378.56	174.331
Exchange Rate	120	11,404	16,367	13,957.37	1,006.192
ISSI	120	244,910,428	614,595,792	356,653,573.10	77,249,332.658
IHSG	120	422,192	727,279	583,172.67	81,477.719
Valid N (listwise)	120				

Source: Data processed using IBM SPSS version 22, 2024.

Based on Table 1, all variables consist of 120 valid observations, indicating that the dataset is complete and suitable for further analysis. The table provides an overview of the distribution and variability of inflation, exchange rates, ISSI, and IHSG during the observation period.

Inflation over the period 2014–2023 recorded an average value of 378.56, with a minimum value of 132 observed in August 2020 and a maximum value of 836 recorded in December 2014. The standard deviation of 174.331 indicates moderate variability in inflation levels during the study period, reflecting fluctuations in price stability across different economic conditions.

The exchange rate variable shows a mean value of IDR 13,957.37 per USD, with the lowest value of IDR 11,404 recorded in March 2014 and the highest value of IDR 16,367 observed during periods of currency depreciation. The standard deviation of 1,006.192 suggests notable volatility in the rupiah exchange rate throughout the observation period.

The Indonesian Sharia Stock Index (ISSI) exhibits a mean value of 356,653,573.10, with the lowest level recorded in September 2015 and the highest level observed in December 2023. The relatively large standard deviation of 77,249,332.658 indicates substantial fluctuations in the performance of sharia-compliant stocks, reflecting sensitivity to macroeconomic conditions and market dynamics.

Similarly, the Indonesia Composite Stock Price Index (IHSG) recorded an average value of 583,172.67, with a minimum value observed in November 2015 and a maximum value achieved in December 2023. The standard deviation of 81,477.719 suggests that IHSG experienced considerable variability over the study period, consistent with changes in domestic and global economic conditions.

Overall, the descriptive statistics indicate that both ISSI and IHSG experienced significant fluctuations during the period 2014–2023, highlighting the relevance of examining the role of macroeconomic variables—particularly inflation and exchange rates—in explaining stock market performance in Indonesia.

4.1.2. Model Fit

To evaluate the adequacy of the proposed regression models, an assessment of model fit is conducted using the coefficient of determination (R^2) and the simultaneous F-test. These statistics are employed to examine the extent to which inflation and exchange rates jointly explain variations in stock market performance, as represented by the Indonesian Sharia Stock Index (ISSI) and the Indonesia Composite Stock Price Index (IHSG). The model fit results provide an overall indication of the explanatory power and statistical validity of the regression models before further interpretation of individual parameter estimates.

Tabel 2 Model Summary and Simultaneous Test Results

Index	R	R ²	Adjusted R ²	F-Statistic	Sig.
ISSI (Y1)	0.626	0.392	0.381	37.647	0.000
IHSG (Y2)	0.574	0.329	0.318	28.687	0.000

Source: Processed data using IBM SPSS version 22, 2024.

The model fit statistics indicate that the regression models for both ISSI and IHSG demonstrate satisfactory explanatory power. The coefficient of determination (R^2) shows that inflation and exchange rates jointly account for **39.2% of the variation in ISSI** and **32.9% of the variation in IHSG**, while the remaining variation is explained by other macroeconomic and firm-specific factors not included in the models.

The relatively higher R^2 value for ISSI suggests that Islamic stock market performance is slightly more sensitive to the selected macroeconomic variables compared to the conventional stock market. This finding may reflect differences in sectoral composition and financial structure between sharia-compliant and conventional stocks, particularly with respect to leverage constraints and exposure to interest-based financing.

Furthermore, the F-statistic values for both models are statistically significant at the 5% level ($p < 0.01$), indicating that inflation and exchange rates simultaneously exert a significant effect on stock market performance. This result confirms the overall validity of the regression models and supports the relevance of macroeconomic factors in explaining movements in both Islamic and conventional stock indices in Indonesia.

Overall, the model fit results are consistent with the Arbitrage Pricing Theory (APT), which posits that asset prices and returns are influenced by multiple systematic risk factors. The findings imply that inflation and exchange rate fluctuations function as important sources of systematic risk in the Indonesian capital market, affecting both sharia-compliant and conventional equity segments.

4.1.3. Regression Analysis and Hypothesis Testing

4.1.3.1 Regression Results and Hypothesis Testing for ISSI

This subsection presents the results of the multiple linear regression analysis examining the partial effects of inflation and exchange rates on the Indonesian Sharia Stock Index (ISSI). The estimation results are reported in Table 3.

Table 3 Regression Results for ISSI

Variable	Coefficient (B)	t-Statistic	Sig.
Constant	-358,983,714.832	-3.767	0.000
Inflation	31,752.281	0.874	0.384
Exchange Rate	50,411.887	8.011	0.000

Source: Processed data using IBM SPSS version 22, 2024.

The regression results indicate that inflation does not have a statistically significant effect on ISSI. Although the inflation coefficient is positive ($\beta = 31,752.281$), the associated probability value exceeds the 5% significance level ($p = 0.384$), suggesting that inflationary fluctuations during the observation period did not directly influence the performance of sharia-compliant stocks. This finding implies that the Islamic stock market may exhibit relative resilience to inflationary pressures, potentially due to its emphasis on real-sector activities and restrictions on speculative financial practices.

In contrast, the exchange rate shows a positive and statistically significant effect on ISSI ($\beta = 50,411.887$; $t = 8.011$; $p < 0.01$). This result indicates that movements in the rupiah exchange rate play a dominant role in shaping the performance of the Islamic stock market in Indonesia. Exchange rate dynamics likely affect ISSI through trade exposure,

import cost adjustments, and foreign investment flows, which remain relevant even under sharia screening mechanisms.

Overall, these findings suggest that among the macroeconomic variables examined, the exchange rate constitutes a more influential systematic risk factor for the Islamic stock market than inflation. Accordingly, H_1 is not supported, while H_3 is supported.

4.1.3.2 Regression Results and Hypothesis Testing for IHSG

This subsection reports the regression results for the Indonesia Composite Stock Price Index (IHSG), representing the overall performance of the conventional stock market. The estimation results are presented in Table 4.

Table 4 Regression Results for IHSG

Variable	Coefficient (B)	t-Statistic	Sig.
Constant	-849.696	-0.008	0.994
Inflation	-38.642	-0.961	0.339
Exchange Rate	42.891	6.154	0.000

The regression results reveal that inflation does not have a statistically significant effect on IHSG. The inflation coefficient is negative ($\beta = -38.642$), indicating an inverse relationship, but the effect is statistically insignificant at the 5% level ($p = 0.339$). This finding suggests that inflation alone did not exert a direct influence on overall stock market performance during the study period, possibly due to market anticipation, adaptive investor expectations, or the presence of other dominant macroeconomic factors.

Conversely, the exchange rate has a positive and statistically significant effect on IHSG ($\beta = 42.891$; $t = 6.154$; $p < 0.01$). This result confirms that currency movements significantly affect the Indonesian stock market as a whole. Exchange rate depreciation may influence IHSG through increased production costs for import-dependent firms, balance sheet effects on foreign-denominated liabilities, and shifts in foreign portfolio investment, all of which contribute to market-wide valuation changes.

These findings indicate that exchange rate fluctuations are a key determinant of conventional stock market performance in Indonesia, while inflation plays a less prominent role. Therefore, H_2 is not supported, whereas H_4 is supported.

4.2. The Discussion

This section discusses the empirical findings by explicitly linking them to the theoretical framework and prior empirical studies outlined in the literature review. In line with the Arbitrage Pricing Theory (APT), this discussion examines how inflation and exchange rate movements function as systematic macroeconomic risk factors influencing stock market performance in both Islamic and conventional capital markets in Indonesia.

4.2.1. Inflation and the Indonesian Sharia Stock Index (ISSI)

The empirical results show that inflation does not have a statistically significant effect on the Indonesian Sharia Stock Index (ISSI). This finding is consistent with the theoretical arguments presented in the literature review, which suggest that although inflation is generally considered a systematic risk factor under the APT framework, its impact on asset prices may depend on market structure, investor behavior, and the prevailing macroeconomic environment.

From the perspective of Islamic finance, sharia-compliant stocks are typically characterized by lower leverage, stronger balance sheets, and closer linkages to real economic activities. As discussed in the literature review, these characteristics may reduce the sensitivity of Islamic equities to inflation-induced increases in financing costs and discount rates. Moreover, Islamic investors tend to adopt a long-term investment horizon and emphasize prudence and compliance, which may dampen reactions to short-term inflation fluctuations.

Empirically, this result supports previous studies reviewed earlier, including (Al Amin & Sholahuddin, 2023; Wijayanti, et al., 2025), which find that inflation does not significantly influence ISSI. The insignificance of inflation may also reflect the relatively stable inflation environment during the observation period, which did not reach levels severe enough to alter corporate fundamentals or investor expectations in the Islamic capital market. Therefore, while inflation is theoretically relevant under APT, its role as a dominant pricing factor for ISSI appears limited in the Indonesian context.

4.2.2 Inflation and the Indonesia Composite Stock Price Index (IHSG)

The results further indicate that inflation does not have a statistically significant effect on the Indonesia Composite Stock Price Index (IHSG). This finding aligns with the literature review, which highlights that the relationship between inflation and stock market performance in emerging economies is often mixed and context-dependent.

According to APT, inflation affects asset prices through its influence on expected cash flows and discount rates. However, as discussed earlier, effective monetary policy, credible inflation targeting, and positive economic growth can mitigate these adverse effects. In Indonesia, coordinated policy responses by the government and Bank Indonesia appear to have successfully contained inflationary pressures, thereby preventing inflation from becoming a dominant risk factor in stock market pricing.

This result is consistent with prior empirical evidence reviewed in the literature, including (Ramadhani, et al, 2024; Dinata & Yusbardini, 2025) which also report an insignificant effect of inflation on IHSG. The growing depth and diversification of the Indonesian capital market, along with increasing participation by domestic investors, may further reduce the sensitivity of the overall market to inflation shocks. Consequently, similar to ISSI, inflation does not emerge as the primary macroeconomic driver of stock market movements during the study period.

4.2.3 Exchange Rate and the Indonesian Sharia Stock Index (ISSI)

In contrast to inflation, the rupiah exchange rate is found to have a statistically significant effect on ISSI. This result strongly supports the APT-based argument presented in the literature review that exchange rate movements constitute a key systematic risk factor in open and emerging economies.

As discussed earlier, exchange rate fluctuations affect Islamic equities through multiple transmission channels, including trade competitiveness, import costs, and foreign investment flows. Although sharia screening limits leverage and interest-based exposure, it does not eliminate firms' exposure to currency risk arising from international trade and macroeconomic conditions. Consequently, exchange rate movements remain a critical determinant of ISSI performance.

This finding is consistent with previous empirical studies reviewed earlier, particularly (Ratnaningrum, et al., 2023; Dinata, et al., 2025; Vikaliana, 2017; Handriani, et al., 2021),

which document a significant relationship between the rupiah exchange rate and Islamic stock indices in Indonesia. The result reinforces the notion that Islamic capital markets, while governed by ethical and contractual constraints, remain integrated with the broader macroeconomic environment and are sensitive to currency dynamics.

4.2.4 Exchange Rate and the Indonesia Composite Stock Price Index (IHSG)

The empirical results also reveal a statistically significant effect of the rupiah exchange rate on IHSG, confirming the importance of exchange rate stability for overall stock market performance. This finding is fully aligned with the theoretical discussion in the literature review, which emphasizes that exchange rate movements influence stock prices through capital flows, corporate balance sheets, and investor sentiment.

From the APT perspective, exchange rate risk directly affects expected returns by altering firms' cost structures and foreign currency exposure. In Indonesia, a net importing and foreign capital-dependent economy, currency depreciation tends to increase production costs and heighten macroeconomic uncertainty, thereby exerting downward pressure on stock prices. Conversely, exchange rate stability or appreciation enhances investor confidence and supports capital inflows, leading to improved market performance.

This result corroborates earlier empirical findings discussed in the literature review, including (Yunanto & Medyawati, 2021; Ilham & Nyoman, 2019), which demonstrate a significant relationship between exchange rate movements and IHSG. The consistency between theoretical expectations and empirical outcomes strengthens the validity of the regression results.

Overall, the findings of this study reinforce the relevance of Arbitrage Pricing Theory in explaining stock market performance in Indonesia. While inflation does not emerge as a significant pricing factor for either ISSI or IHSG during the study period, the exchange rate consistently functions as a dominant systematic risk factor affecting both Islamic and conventional stock indices.

These results confirm the arguments presented in the literature review that macroeconomic variables do not uniformly influence stock markets; instead, their effects depend on market structure, investor behavior, and institutional context. In the Indonesian case, exchange rate dynamics play a more critical role than inflation in shaping stock market performance, highlighting the importance of currency stability for both Islamic and conventional capital markets.

5 Conclusion

This study examines the effects of inflation and the rupiah exchange rate on the performance of Islamic and conventional stock markets in Indonesia, as represented by the Indonesian Sharia Stock Index (ISSI) and the Indonesia Composite Stock Price Index (IHSG) over the period 2014–2023. The empirical results indicate that inflation does not have a significant effect on either ISSI or IHSG, whereas the rupiah exchange rate exerts a significant influence on both indices. These findings suggest that, during the observation period, inflation did not function as a dominant macroeconomic risk factor in shaping stock market movements in Indonesia. In contrast, the exchange rate emerged as a key systematic risk factor affecting both Islamic and conventional stock market performance. Overall, the results provide empirical support for the Arbitrage Pricing Theory (APT),

which emphasizes the role of specific macroeconomic factors—particularly exchange rates—as primary determinants of asset prices.

The implications of this study are both theoretical and practical. From a theoretical perspective, the findings reinforce the relevance of Arbitrage Pricing Theory in the context of the Indonesian capital market by demonstrating that macroeconomic variables do not exert uniform effects on stock prices. The exchange rate is shown to be more influential than inflation in explaining movements in both ISSI and IHSG. From a practical perspective, the results offer important insights for investors, portfolio managers, and policymakers. Investors, especially those operating in the Islamic stock market, should place greater emphasis on exchange rate dynamics when formulating investment strategies. For monetary authorities and capital market regulators, these findings highlight the importance of maintaining exchange rate stability as part of broader efforts to safeguard market stability and enhance the attractiveness of both Islamic and conventional capital markets.

Despite its contributions, this study has several limitations. First, the analysis is restricted to two macroeconomic variables—inflation and the exchange rate—and therefore does not fully capture other systematic factors that may influence stock market performance, such as interest rates, economic growth, or global economic conditions. Second, the use of a linear regression approach assumes stable and linear relationships among variables over time, which may not fully reflect the dynamic nature of financial markets. Future research is encouraged to incorporate additional macroeconomic and global variables, apply dynamic or non-linear modeling approaches, and conduct cross-country or crisis-period analyses to obtain a more comprehensive understanding of the determinants of Islamic and conventional stock market performance.

References

- Abaidoo, R., & Agyapong, E. K. (2024). Commodity prices, inflation, and inflation uncertainty among emerging economies. *Journal of Economic and Administrative Sciences*, 40(3), 622–640.
- Abbate, A., Eickmeier, S., & Prieto, E. (2023). Financial shocks and inflation dynamics. *Macroeconomic Dynamics*, 27(2), 350–378.
- Al Amin, I., & Sholahuddin, M. (2023). The effect of inflation, interest rates, and USD exchange rate on the Indonesian Sharia Stock Index (ISSI) during 2019–2022. *International Journal of Applied Finance and Business Studies*, 11(1), 50–58.
- Amal, M. A., & Musthofa, M. W. (2023). The impact of the Dow Jones Islamic Market, interest rate, rupiah exchange rate, and inflation on the Indonesian Sharia Stock Index during 2018–2022. *Jurnal Ekonomi Syariah Teori dan Terapan*, 10(2).
- Bahloul, S., Mroua, M., & Naifar, N. (2017). The impact of macroeconomic and conventional stock market variables on Islamic index returns under regime switching. *Borsa Istanbul Review*, 17(1), 62–74.
- Boediono. (2019). *Ekonomi makro*. BPFE.
- Canarella, G., & Miller, S. M. (2016). Inflation persistence and structural breaks: The experience of inflation-targeting countries and the USA. *Journal of Economic Studies*, 43(6), 980–1005.

- Demir, F., & Razmi, A. (2022). The real exchange rate and development theory, evidence, issues, and challenges. *Journal of Economic Surveys*, 36(2), 386–428.
- Dewi, N. F., & Fauzan, A. (2023). The relationship between exchange rate, inflation, foreign exchange reserves, export, and import in Indonesia: A vector error correction model approach. In *Proceedings of the 3rd International Seminar on Science and Technology (ISSTEC 2021)* (Vol. 2720, Article 020025). AIP Publishing.
- Dinata, G. A., & Yusbardini, Y. (2025). The influence of rupiah exchange rate, world oil prices, and inflation on the Composite Stock Price Index (IHSG). In *Proceedings of the Tarumanagara International Conference on the Applications of Social Sciences and Humanities (TICASH 2024)* (pp. 72–81). Atlantis Press.
- Fama, E. F., & Schwert, G. W. (1977). Asset returns and inflation. *Journal of Financial Economics*, 5(2), 115–146.
- Handriani, M. S., Isnurhadi, I., Yuliani, Y., & Sulastri, S. (2021). The effect of inflation rate, rupiah exchange rate, world oil prices, and world gold prices on the Indonesian Sharia Stock Index (ISSI). *International Journal of Business, Economics and Management*, 4(2), 363–371.
- Harsono, A. R. (2018). *Pengaruh inflasi, suku bunga, dan nilai tukar rupiah terhadap Indeks Harga Saham Gabungan* [Undergraduate thesis, Universitas Brawijaya]. <https://repository.ub.ac.id/162675/>
- Ilham, K. R., & Nyoman, S. I. A. (2019). The influence of world stock index, BI rate, and Fed rate through IHSG on exchange rates in Indonesia (2006–2015). *Russian Journal of Agricultural and Socio-Economic Sciences*, 93(9), 216–226.
- Katmas, E., & Indarningsih, N. A. (2022). The effect of BI interest rate, exchange rate, and inflation on the Indonesian Sharia Stock Index (ISSI). *Indonesian Interdisciplinary Journal of Sharia Economics*, 5(2), 768–782.
- Krugman, P. R., & Obstfeld, M. (2018). *International economics: Theory and policy* (11th ed.). Pearson.
- Laksono, R. (2024). Analysis of the influence of macroeconomic factors on long-term and short-term fluctuations of the Indonesian stock exchange using the ECM approach. *Technium Social Sciences Journal*, 63, 162–173.
- Mankiw, N. G. (2018). *Prinsip-prinsip ekonomi* (7th ed., Indonesian trans.). Salemba Empat.
- Marpaung, N. N., & Pangestuti, I. R. D. (2024). Macroeconomic factors and the Jakarta Stock Exchange: A comparative analysis pre- and during the COVID-19 pandemic. *SAGE Open*, 14(2), 21582440241247894.
- Naifar, N. (2016). Do global risk factors and macroeconomic conditions affect global Islamic index dynamics? A quantile regression approach. *The Quarterly Review of Economics and Finance*, 61, 29–39.
- Nugroho, I., Hidayatullah, M. S., & Jayanti, A. A. (2023). The effect of inflation, exchange rate, and BI rate on the Indonesian Sharia Stock Index. *Journal of Islamic Economics and Finance Studies*, 4(1), 114–132.
- Otieno, D. A., Ngugi, R. W., & Muriu, P. W. (2019). The impact of inflation rate on stock market returns: Evidence from Kenya. *Journal of Economics and Finance*, 43(1), 73–90.
- Priyono, A. A., & Kartiko, A. (2021). The effect of COVID-19, rupiah exchange rate, and inflation on the Indonesian Sharia Stock Index. *Indonesian Interdisciplinary Journal of Sharia Economics*, 4(1), 313–336.

- Rapach, D. E. (2002). The long-run relationship between inflation and real stock prices. *Journal of Macroeconomics*, 24(3), 331–351.
- Reinganum, M. R. (1981). The arbitrage pricing theory: Some empirical results. *The Journal of Finance*, 36(2), 313–321.
- Salvatore, D. (2015). *International economics* (11th ed.). Wiley.
- Shapiro, A. C. (1975). Exchange rate changes, inflation, and the value of the multinational corporation. *The Journal of Finance*, 30(2), 485–502.
- Umar, Z., Kenourgios, D., Naeem, M., Abdulrahman, K., & Al Hazaa, S. (2020). The inflation hedging capacity of Islamic and conventional equities. *Journal of Economic Studies*, 47(6), 1377–1399.
- Vikaliana, R. (2017). Effect of inflation, interest rate (BI rate), and rupiah exchange rate on the Indonesian Composite Index. *The Management Journal of Binaniaga*, 2(1), 41–52.
- Wijayanti, N., Trisnafi, K., & Adlan, M. A. (2025). The impact of macroeconomic variables on the Jakarta Islamic Index and LQ45 Index. *El-Kahfi: Journal of Islamic Economics*, 6(1), 197–208.
- Yildirim, Z., & Ivrendi, M. (2016). Exchange rate fluctuations and macroeconomic performance: Evidence from four fast-growing emerging economies. *Journal of Economic Studies*, 43(5), 678–698.
- Yunanto, M., & Medyawati, H. (2021). The impact of exchange rate, Bank Indonesia certificates, and global indexes on the Composite Stock Price Index (IHSG). *The Journal of Asian Finance, Economics and Business*, 8(6), 651–660.