

Niramol Surapatana 2010: A Study of the Relationship between Financial Conditions Index and Output gap. Master of Economics, Major Field: Economics, Department of Economics. Thesis Advisor: Mr. Arun Kiarasarn, Dip.de IIIeme Cycle 225 pages.

The objective of this study is to apply the Financial Conditions Index (FCI) of Charles Goodhart and Boris Hofmann to predict the direction of output gap which is an indicator of price pressure and can be used as an element in predicting the trend of short term inflation in conducting the monetary policy.

The FCI was constructed from the Bank of Thailand's four main financial variables that impacted the monetary transmission mechanism, i.e. Real Minimum Lending Rate(MLR), Real Effective Exchange Rate (REER), Real Housing Price index (RHPI) and the ratio of Market capitalization to GDP (MCap/GDP), using the quarterly time-series from the first quarter 1994 to the fourth quarter 2005. The Vector Auto Regression (VAR) and Impulse Response Function are used to determine the relationship of these 4 variables and the output gap, as well as the weight of each variable, assuming a negative relationship between the FCI and the output gap.

This study analyzed the change in the FCI and the output gap by comparing the current quarter with the same quarter of previous year, and then, compared the directional result of both indicators. The study found that the relationship of these two indicators corresponded to the assumption. This showed that FCI can indicate the direction of the output gap faster than real economic data. The Granger causality test showed that FCI could indicate both the change in the short-term and long-term output gap. The Cointegration test also showed that there was a long-term relationship between FCI and the output gap. The result lead to the conclusion that FCI can be used as a leading indicator to predict the change in the direction of short-term output gap, and as a coincident economic index.

---

Student's signature

---

Thesis Advisor's signature