Relationship Between Policy Rate and Stock Market in Thailand Using Markov-Switching EGARCH

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ABSTRACT

This study finds the relationship between policy rate and stock return in Thailand by using Markov-switching EGARCH model. This paper composed of two part, the first part provided the estimated parameters of six models such as, AR, MS-AR, GARCH, MS-GARCH, EGARCH, and MS-EGARCH model, and then tested. The result showed that MS-EGARCH is the most suitable model to explain stock return in Thailand. In the second part, the Markov-switching EGARCH model is used to test the relationship between inter-bank rate and stock return of Thailand. The inter-bank rate data are divided into six groups by maturity as 1 day, 1 week, 1 month, 3 month, 6 month and 12 month inter-bank rate. The result showed that the inter-bank rate has no direct effect to stock return of Thailand, but for short term maturity, 1 week, and 1month rate, they had influence on the conditional variance of stock return. Finally the estimated parameter value showed that when the market is in the state of high mean and low variance, increasing in short term maturity inter-bank rate will lower the risk in the stock market.