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Inflation Targeting and Real Exchange Rate in ASEAN-3 using: Vector Error Correction Model (VECM)

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ABSTRACT

This study investigates inflation targeting (IT) in ASEAN-3, focusing on the role of real exchange rate and the macroeconomics variables. This research applies VECM (Vector Error Correction Model) as the method analysis. The Granger test shows us there is the relationship between GDP and Exchange rate. It means the expansion of economy that governments do in the previous time, have been influencing our economy now. This statement strengthens by the estimation result that shows the GDP has significant influence the amount of exchange rate in the short term and in the long term. The impulse response forecast that GDP gives a negative impact to the exchange rate. But the exchange rate has a positive response in economic growth. The results of forecast error variance decomposition showed that the logarithm of real exchange rate explains a few percent of the forecast error variance of production and the logarithm of the inflation rate. In ASEAN-3 the output is the smallest influence to exchange rate and inflation. This research demonstrates IT ASEAN-3 appear to follow a "mixed strategy" whereby both inflation and real exchange rates are important determinants of policy interest rates.

Keywords: Inflation Targeting (IT), real exchange rate, macroeconomics variable

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The abstract has been approved by the advisor and the examiners :

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