This study used Vector Auto regression (VAR) model to analyze effectiveness of monetary policy transmission mechanism in Indonesia through Interest Rate Channel period of 1990:2-2007:1. The effectiveness was measured by two indicators. They are: (1). how fast or how many time lag needed since the shock of monetary instruments (rSBI) until the realisation of final target of monetary policy (inflation). (2). How strong the variables of Interest Rate Channel response the shock of SBI interest rate and other variable. This study used secondary data issued by Bank Indonesia and BPS as well as from International Finance Statistic (IFS). The result of the study shows that response velocity of variable in Interest Rate Channel towards shock instrument of monetary policy (rSBI) until reach the final target about 10 quarterly or twenty six months. While impulse response function of variables in this channel to the shock instrument of monetary policy (rSBI) is quiet strong and the main variable in interest rate money market among bank (rPUAB) able to explain diversity final target of monetary policy (inflation) about 63,11%. This result once shows a strong Granger causality and predictive power between rPUAB as the operational target with inflation as the final target of monetary policy. Thus we can conclude that mechanism of monetary policy transmission through Interest Rate Channel is effective to reach the final target of monetary policy of Indonesia period of 1990:2-2007:1

Keyword :

Monetary Policy, Impulse Response Function and Variance Decomposition