

ABSTRACT

This study aims to analyze the determinants of the Rupiah exchange rate against the US Dollar during the 2018-2022 period using the Monetary Approach framework. Employing monthly time-series data, this research applies the Vector Error Correction Model (VECM) to examine short-run dynamic relationships and long-run equilibrium. The variables analyzed include the differentials in money supply (M), national income (Y), interest rates (RL), and inflation (INF) between Indonesia and the United States on the exchange rate (E). The cointegration test confirms the existence of a stable long-run equilibrium relationship. In the long run, an increase in the national income (Y) and interest rate (RL) differentials leads to a Rupiah appreciation, while a higher inflation (INF) differential leads to depreciation, consistent with theory. However, an anomaly was found where an increase in the money supply (M) differential is correlated with appreciation. The error correction mechanism analysis shows that national income (Y) acts as the primary and significant adjustment variable in restoring the system to its equilibrium. Furthermore, the Impulse Response Function (IRF) and Variance Decomposition (VD) analyses reveal that the exchange rate (E) acts as the dominant source of shocks affecting other monetary and real variables. Conversely, the exchange rate's own movement is most significantly influenced in the long run by shocks from interest rates (RL) and money supply (M). Overall, these findings affirm the consistency of the Monetary Approach in explaining the Rupiah's dynamics and highlight the importance of inflation stability and the dual role of interest rates in maintaining exchange rate stability.

Keywords: *Rupiah Exchange Rate, Monetary Approach, VECM, Cointegration, Macroeconomic Variables.*

