

## **Monetary-Fiscal Policy Mix and Inflation in Korea**

Sora Chon

Wongi Kim

### **Abstract**

This paper investigates monetary-fiscal policy mix as a determinant of inflation in Korea using the fiscal theory of the price level framework. To this end, we first check fiscal-related regime changes assuming that fiscal policy plays a predominant role in determining the transitions between these regimes in the inflation dynamics of Korea. Our empirical investigation reveals that distinct fiscal regimes are not statistically identifiable when using the Threshold Vector Autoregression (TVAR) approach. We then estimate a medium-scale dynamic stochastic general equilibrium model (DSGE) under two different regimes: active fiscal policy - passive monetary policy (Regime F) and passive fiscal policy - active monetary policy (Regime M). DSGE estimation reveals Regime M prevailed. The results suggest that monetary policy plays a significant role in determining inflation in Korea.

JEL Classification Numbers: E13; E31; E32

Keywords: Fiscal Theory of the Price level; Monetary Policy; Fiscal Policy; Regime