

Excessive Imbalance Procedure in the EU: a welfare evaluation

Andrzej Torój*

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We develop a framework for assessing the welfare implications of the new EU's Excessive Imbalance Procedure (EIP) to be implemented in 2012, with a special focus on the current account constraint. For this purpose, we apply a New Keynesian 2-region, 2-sector DSGE model, using the second order Taylor approximation of the households' utility around the steady state as a standard measure of welfare. The compliance with the CA criterion is ensured by modifying the policymakers' loss function in line with Woodford's (2003) treatment of the zero lower bound of nominal interest rates. We also compare the impact of the EIP between countries along the dimensions of catching-up process and euro area membership.

*Ministry of Finance in Poland and Warsaw School of Economics