Real convergence vs. macroeconomic imbalances in the European Union.

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Abstract

The nominal convergence criteria established in the Maastricht Treaty were assumed to increase also the real convergence degree in the euro area. The first decade of the euro area (EA) functioning showed that real and nominal divergence between members of the common currency area persist. This paper provides an extended analysis of the convergence degree of euro candidates and the EA member states with the common currency area. It also aims at indicating the potential interdependencies between the high rate of real (as well as nominal) convergence and macroeconomic imbalances. The analysis indicates that the hypothesis of the common currency area endogeneity, assuming that countries which faced challenges with fulfilling the nominal convergence criteria even before euro adoption would be able to fulfill them much faster after the currency union accession, did not come true. On one hand, most EA member states had problems with meeting the Maastricht criteria after euro adoption and are still not highly converged in terms of economic structure. On the other hand, the business cycles synchronization has been observed and the correlation of cyclical components is still increasing which is undoubtedly advantageous from the perspective of common monetary policy and its adequacy for the EA member states. However, in the time of crisis we could observe that even the highly converged countries reported alarming macroeconomic imbalances. Euro candidates should draw conclusions from the EA members' experience and take into account, while their preparations for the common currency adoption, that a high degree of the nominal and real convergence is not sufficient to fully benefit from the EA membership.