

## Abstract

This study is concerned with two interconnected issues. First, the suitability of interest rate chosen by ECB is assessed in individual Eurozone countries using seven versions of Taylor rule. The methodology primarily emphasizes robustness by employment of various measures of inflation and output gap. The policy rates were found to be too low in all Eurozone's peripheral countries for prolonged period of time. Second, the sensitivity of real estate prices to a change in interest rate in Greece, Ireland, Italy, Portugal, Spain and UK is estimated using VAR, VECM, BVAR and Panel VAR. The prime concern is whether the low policy rates can be the cause of housing bubbles. The housing prices respond most vividly to interest rate in Ireland, Spain and UK (approximately 3.5% increase in the price as a response to 1% decrease in interest rate) which are also the countries where flexible interest rate mortgages are dominant. Monetary policy is shown to be an important determinant of housing prices but it is not the sole reason for the bubbles.