Convergence to the Model Solution

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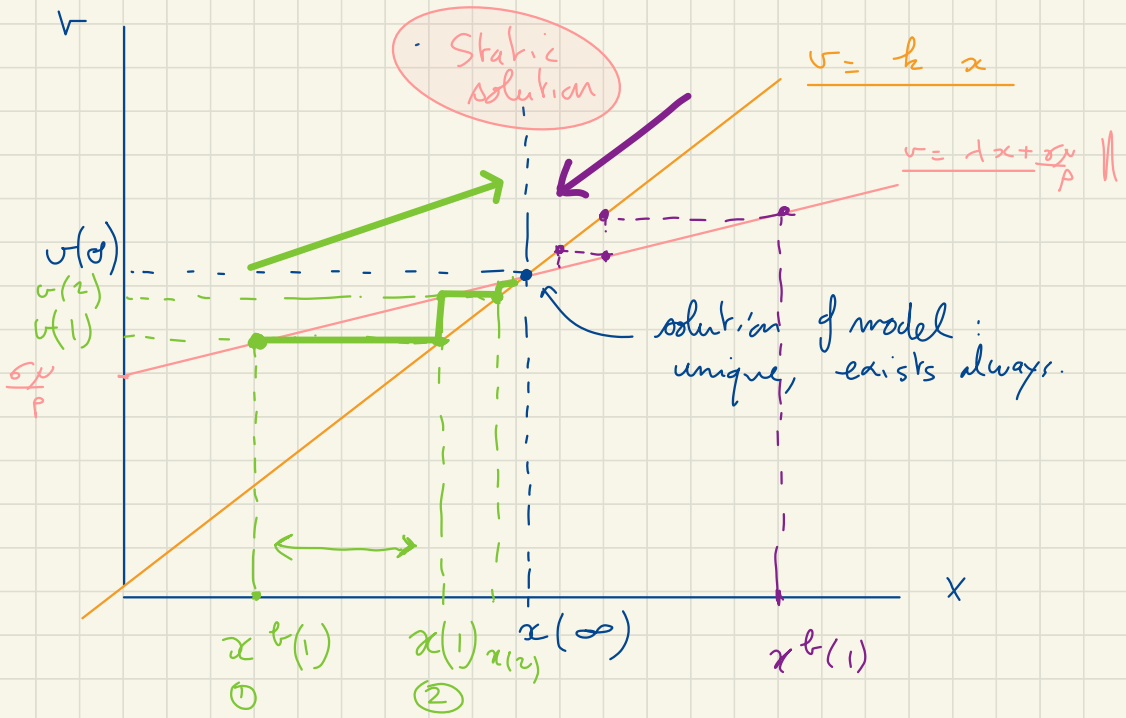
Solution of model with $\rho = 0$ & $\gamma = 1$



Discrete time

- At time $t = 1$, households expect $x^{k_2}(1)$
- Households max. utility given $x^{k_2}(1)$
  - ↳ $v(1) = \lambda x^{k_2}(1) + \frac{\sigma\nu}{\rho}$
  - ↳ $x(1) = \frac{v(1)}{k_2} = \left[\lambda x^{k_2}(1) + \frac{\sigma\nu}{\rho}\right] \frac{1}{k_2}$
- At time 2, households expect $x^{k_2}(2) = x(1)$

- Households max utility given $x^h(t) = x(t)$