



# Multidimensional endogenous gridpoint method: Solving triangular dynamic stochastic optimization problems without root-finding operations



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## HIGHLIGHTS

- Certain dynamic stochastic models can be solved without root finding operations.
- The paper describes a class of such models using five conditions.
- The solution method is multidimensional endogenous gridpoint method (EGM).
- Typical member of this class is a model of multiple stock dynamics.

## ARTICLE INFO

### Article history:

Received 13 May 2015

Received in revised form

20 July 2015

Accepted 31 July 2015

Available online 8 August 2015

### JEL classification:

C63

D90

### Keywords:

Endogenous grid method

Multidimensional continuous choice

Dynamic structural models

## ABSTRACT

This paper defines the class of triangular dynamic stochastic optimization problems with multiple continuous choices which can be solved by the multidimensional generalization of the method of endogenous gridpoints without costly root-finding operations. The typical member of this class is a model of multiple asset dynamics, with potential applications in wealth, health and human capital accumulation, portfolio problems, multisector growth models, etc.

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## 1. Introduction

The endogenous gridpoint method (EGM) introduced by Carroll (2006) to solve stochastic dynamic models with one continuous state variable and a single continuous control, proved to be very fast and accurate<sup>1</sup>—mainly due to its ability to solve the first order conditions directly without root-finding operations. The method

had been generalized to a number of settings,<sup>2</sup> where it proved to retain its numerical advantage over the traditional dynamic programming approach. Yet, the applicability of EGM method had been shown only for a collection of particular economic models, whereas the class of models which can be solved without root-finding operations has not been rigorously characterized.<sup>3</sup>

This paper proposes five conditions which are jointly sufficient for a given problem to belong to the class of *triangular* dynamic optimization problems that can be solved by the multidimensional version of EGM in such a way that all root-finding operations are

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<sup>1</sup> As a result, the computation of the solution for a classic consumption–savings model that could “easily done on a 386-series PC, taking 5–20 min per calculation” by Deaton (1991, p. 1229), takes only a fraction of a second on a modern laptop (Jørgensen, 2013, p. 289), with the speedup of approximately two orders of magnitude from the use of EGM when compared to traditional value functions iterations. Barillas and Fernandez-Villaverde (2007) and Iskhakov et al. (2015) find similar magnitude of the speedup with no effect on the solution accuracy.

<http://dx.doi.org/10.1016/j.econlet.2015.07.033>  
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<sup>2</sup> See Barillas and Fernandez-Villaverde (2007), Hintermaier and Koeniger (2010), Ludwig and Schön (2014), Fella (2014) and Iskhakov et al. (2015) for various applications of EGM framework.

<sup>3</sup> White (2015) develops a general theory of EGM, which does not however aim at defining the class of problems solvable without root-finding operations.

avoided. The key insight is to ensure that the system of Euler equations that characterizes the solution has a triangular structure, and thus can be solved directly using forward substitution under standard EGM assumptions of analytical invertibility of marginal utilities.

To simplify the exposition, in this paper I only consider unconstrained choice problems. The standard approach of treating corner solutions which relies on the monotonicity of the policy function<sup>4</sup> or Inada (1963) derivative conditions can be generalized with additional assumptions, but general treatment based on Kuhn–Tucker conditions used by Hintermaier and Koeniger (2010) is also available for particular applications. It should also be noted that the proposed multidimensional EGM does not break the curse of dimensionality—multidimensional integration and interpolation on irregular grids are inevitable in these models.<sup>5</sup>

## 2. Two-dimensional illustrative example

Consider a discrete time<sup>6</sup> dynamic optimization problem with two state variables  $X_t$  and  $Y_t$ , and two continuous decision variables  $x_t$  and  $y_t$ , which represent, for example, the choice of consumption and the exercise intensity in the model of health and wealth dynamics. Denoting the instantaneous utility function  $u(x_t, y_t)$  and the discount factor  $\beta$ , the Bellman equation of the problem is

$$V_t(X_t, Y_t) = \max_{x_t, y_t} \{u(x_t, y_t) + \beta E[V_{t+1}(X_{t+1}, Y_{t+1}) | X_t, Y_t, x_t, y_t]\}, \quad t \in \{1, \dots, T-1\}. \quad (1)$$

Assume that the transition rules for the states  $X_t$  and  $Y_t$  can be written as

$$\begin{aligned} X_{t+1} &= \chi(f(X_t, x_t), g(Y_t, y_t), \xi_{t+1}), \\ Y_{t+1} &= \psi(f(X_t, x_t), g(Y_t, y_t), \xi_{t+1}), \end{aligned} \quad (2)$$

in other words *sufficient statistics*  $f(t) = f(X_t, x_t)$  and  $g(t) = g(Y_t, y_t)$  contain all the information about period  $t$  that determines the distribution of values of the states in period  $t+1$ . Following the tradition in operations research (Powell, 2007, pp. 129–144), I refer to  $(f(t), g(t))$  as *post-decision states*. For simplicity, assume that functions  $\chi$ ,  $\psi$ ,  $f$  and  $g$  are time invariant.<sup>7</sup> The expectation in (1) is taken over the joint distribution of idiosyncratic shocks  $\xi_{t+1} \in \mathbb{R}^K$ , and because of (2) can be written conditional on  $(f(t), g(t))$ .

The solution of the problem given by the family of policy functions  $\delta_t : (X_t, Y_t) \rightarrow (x_t, y_t)$ ,  $t \in \{1, \dots, T-1\}$  satisfies the system of first order conditions for (1)

$$\begin{cases} u'_x(x_t, y_t) + \beta f'_x(t) \\ \times E \left[ \frac{\partial V_{t+1}}{\partial X_{t+1}} \chi'_f + \frac{\partial V_{t+1}}{\partial Y_{t+1}} \psi'_f \middle| f(t), g(t) \right] = 0, \\ u'_y(x_t, y_t) + \beta g'_y(t) \\ \times E \left[ \frac{\partial V_{t+1}}{\partial X_{t+1}} \chi'_g + \frac{\partial V_{t+1}}{\partial Y_{t+1}} \psi'_g \middle| f(t), g(t) \right] = 0. \end{cases} \quad (3)$$

By envelope theorem we have

$$\begin{aligned} \frac{\partial V_t}{\partial X_t} &= \beta f'_x(t) E \left[ \frac{\partial V_{t+1}}{\partial X_{t+1}} \chi'_f + \frac{\partial V_{t+1}}{\partial Y_{t+1}} \psi'_f \middle| f(t), g(t) \right] \\ &= - \frac{f'_x(t)}{f'_x(t)} u'_x(x_t, y_t), \\ \frac{\partial V_t}{\partial Y_t} &= \beta g'_y(t) E \left[ \frac{\partial V_{t+1}}{\partial X_{t+1}} \chi'_g + \frac{\partial V_{t+1}}{\partial Y_{t+1}} \psi'_g \middle| f(t), g(t) \right] \\ &= - \frac{g'_y(t)}{g'_y(t)} u'_y(x_t, y_t). \end{aligned} \quad (4)$$

Combining (4) with (3), we derive the system of Euler equations

$$\begin{cases} u'_x(x_t, y_t) = \beta f'_x(t) E \left[ \chi'_f \frac{f'_x(t+1)}{f'_x(t+1)} u'_x(x_{t+1}, y_{t+1}) \right. \\ \left. + \psi'_f \frac{g'_y(t+1)}{g'_y(t+1)} u'_y(x_{t+1}, y_{t+1}) \middle| f(t), g(t) \right], \\ u'_y(x_t, y_t) = \beta g'_y(t) E \left[ \chi'_g \frac{f'_x(t+1)}{f'_x(t+1)} u'_x(x_{t+1}, y_{t+1}) \right. \\ \left. + \psi'_g \frac{g'_y(t+1)}{g'_y(t+1)} u'_y(x_{t+1}, y_{t+1}) \middle| f(t), g(t) \right], \end{cases} \quad (5)$$

which constitutes the set of necessary conditions linking the optimal choices  $(x_t, y_t)$  in period  $t$  to the optimal choices  $(x_{t+1}, y_{t+1})$  in  $t+1$ , given  $(f(t), g(t))$ . Note that  $(x_t, y_t)$  does not appear in the right hand side (RHS) in (5).

Given an appropriate terminal condition, for example  $\delta_T(X_T, Y_T) = (X_T, 0)$  in the hypothetical model of health and wealth dynamics, the EGM method is implemented by fixing the grid over  $(f(t), g(t))$ ; computing RHS in (5) for each point of this grid, using the next period policy function  $\delta_{t+1}$  to find  $(x_{t+1}, y_{t+1})$ ; backing out the optimal decision by solving (5) for  $(x_t, y_t)$ ; and finally recovering the endogenous state point  $(X_t, Y_t)$  from post-decision states and optimal decision. Repeating the latter steps for all points in the grid over  $(f(t), g(t))$  yields an approximation of the policy function  $\delta_t$ , and the backward induction continues to the period  $t-1$ .

The numerical efficiency of EGM in two-dimensional problems satisfying (2) hinges on whether the system (5) can be solved for  $(x_t, y_t)$  by direct computation. The original one-dimensional EGM relies on the analytical invertibility of the marginal utility function, which is enough to yield the optimal period  $t$  choice by direct computation when (5) only has one equation. Clearly, the invertibility of all the partial derivatives is insufficient in the multidimensional case. Because (5) is a system of non-linear equations, even the existence of the solution is not guaranteed without additional conditions on the utility function.

## 3. M-dimensional triangular dynamic optimization problems

Consider now an optimization problem with  $M$  continuous choice variables  $x_t = (x_t^1, \dots, x_t^M) \in \mathbb{R}^M$  which govern the transitions of  $M$  continuous state variables  $X_t = (X_t^1, \dots, X_t^M) \in \mathbb{R}^M$ . Let  $s_t \in \mathbb{R}^N$  denote additional state variables which follow *uncontrolled*  $N$ -dimensional Markov processes, and therefore will be referred to as exogenous states.<sup>8</sup> The following assumptions are needed to derive the main result below.

<sup>8</sup> To simplify the exposition, they will be treated as discrete. In applications these states are either discrete or discretized as in Tauchen (1986).

<sup>4</sup> Used by Carroll (2006), Fella (2014) and Iskhakov et al. (2015).

<sup>5</sup> Ludwig and Schön (2014) show that already in two-dimensional case the computational cost of Delaunay triangulation may offset the speed advantage of the EGM approach. However, White (2015) proposes an interpolation method which takes into account the ordinal information about the endogenous gridpoints produced by EGM. Orthogonal polynomial approximation (Judd, 1998, pp. 202–223) may be suggested as another useful interpolation method.

<sup>6</sup> Both infinite and finite horizon cases are included assuming that the infinite horizon model is solved by time iterations indexed with  $t$ , and  $T = +\infty$ .

<sup>7</sup> It is straightforward to extend the analysis to time varying specifications.

**Assumption A1.** Transition rules for the continuous state variables  $X_t^1, \dots, X_t^M, j \in \{1, \dots, M\}$  can be expressed in the form

$$X_{t+1}^j = \chi^j \left( f^1(X_t^1, x_t^1, s_t), f^2(X_t^1, x_t^1, X_t^2, x_t^2, s_t), \dots, f^M(X_t, x_t, s_t), s_t, s_{t+1}, \xi_{t+1} \right), \quad (6)$$

such that the post-decision states  $f(t) = (f^1(t), \dots, f^M(t)) \in \mathbb{R}^M$  admit the following structure:

$$\begin{aligned} f^1(t) &= f^1(X_t^1, x_t^1, s_t), \\ f^2(t) &= f^2(X_t^1, x_t^1, X_t^2, x_t^2, s_t), \\ &\dots \\ f^M(t) &= f^M(X_t^1, x_t^1, \dots, X_t^M, x_t^M, s_t) = f^M(X_t, x_t, s_t), \end{aligned} \quad (7)$$

where  $\chi^j(\cdot)$  and  $f^j(\cdot)$  are deterministic differentiable functions, and  $\frac{\partial f^j}{\partial x} \neq 0$  and  $\frac{\partial f^j}{\partial x} \neq 0, \xi_{t+1} \in \mathbb{R}^K$  are idiosyncratic shocks.

**Assumption A2.** Transition probabilities  $P(s_{t+1}|X_t, s_t) = P(s_{t+1}|s_t)$  are independent of  $X_t$ .

**Assumptions A1** and **A2** ensure that the post-decision states  $f(t)$  form a set of sufficient statistics for the states and decisions in period  $t$ .

**Assumption A3.** Equations  $f^j(X_t^1, x_t^1, \dots, X_t^j, x_t^j, s_t) = \hat{f}$  can be analytically solved for  $X_t^j$ , while holding other arguments fixed, for all  $j \in \{1, \dots, M\}$  and arbitrary constant  $\hat{f}$ .

**Assumption A4.** There exist permutations  $k^1 = (k_{(1)}^1, \dots, k_{(M)}^1)$  and  $k^2 = (k_{(1)}^2, \dots, k_{(M)}^2)$  of the natural numbers 1 to  $M$  such that if  $J_{k^1}$  and  $J_{k^2}$  are the corresponding permutation matrices<sup>9</sup> and  $H$  is the Hessian of the utility function  $u(x_t, s_t)$  for a fixed  $s_t$ , it holds that the permuted Hessian  $H^P = J_{k^1} H J_{k^2}$  is lower triangular, the diagonal elements of  $H^P$  are non-zero, i.e. letting  $i = k_{(l)}^1$  and  $j = k_{(l)}^2, l \in \{1, \dots, M\}$ ,  $\frac{\partial^2 u(x_t, s_t)}{\partial x_t^i \partial x_t^j} \neq 0$ , the partial derivatives  $\frac{\partial u(x_t, s_t)}{\partial x_t^i}$  are strictly monotone in  $x_t^j$ , and their inverses in  $x_t^j$  have analytical forms.

**Assumption A4** essentially describes the situation when the Hessian of the utility function can be converted to a lower triangular form by re-labeling the variables (according to permutation  $k^2$ ) and permuting the rows of the matrix (according to  $k^1$ ). For additively separable utility  $u(x_t, s_t) = \sum_{j=1}^M u_j(x_t^j, s_t)$  with strictly monotone and analytically invertible partial derivatives, **A4** is satisfied with any permutation  $k^1 = k^2$ . A non-trivial example of utility function satisfying **A4** is  $u(x_t^1, x_t^2) = (x_t^1)^{\alpha_1} (x_t^2)^{\alpha_2}$  when  $\alpha_1 = 1$  and  $\alpha_2 \neq 1$ .

**Assumption A5.** The utility function  $u(x_t, s_t)$  is concave in  $x_t$ , and standard regularity conditions (9.4–9.7) in [Stokey et al. \(1989, pp. 260–263\)](#) hold.

**Proposition 1.** Under **Assumptions A1–A5** the dynamic optimization problem given by the Bellman equation

$$V_t(X_t, s_t) = \max_{x_t} \left\{ u(x_t, s_t) + \beta E \left[ V_{t+1}(X_{t+1}, s_{t+1}) | X_t, s_t, x_t \right] \right\}, \quad (8)$$

<sup>9</sup> Permutation matrix  $J$  is obtained from the identity matrix by permuting its rows; the product  $JA$  is given by same permutation of rows, and product  $AJ$  by same permutation of columns of matrix  $A$ .

where  $X_t \in \mathbb{R}^M, x_t \in \mathbb{R}^M$  and  $s_t \in \mathbb{R}^N, t \in \{1, \dots, T-1\}$ , and the terminal policy function  $\delta_T : (X_T, s_T) \rightarrow x_T$ , admits a solution method which avoids all root-finding operations.

**Proof.** The proof is by construction. The system of Euler equations for the problem complying with **Assumptions A1** and **A2** is composed of  $M$  equations<sup>10</sup>

$$u'_{x^j}(x_t, s_t) = \beta \sum_{k=j}^M \frac{\partial f^k(t)}{\partial x_t^j} E \left[ \sum_{i=1}^M \frac{\partial \chi^i}{\partial f^k} \mathcal{L}_{t+1}^i \middle| s_t, f(t) \right], \quad (9)$$

where  $j \in \{1, \dots, M\}$  and  $\mathcal{L}_{t+1}^i$  is a linear function of marginal utilities evaluated at the optimal decisions in period  $t+1$ ,<sup>11</sup>

$$\begin{aligned} \mathcal{L}_{t+1}^i &= \frac{\frac{\partial f^i(t+1)}{\partial x_{t+1}^i} u'_{x^i}(x_{t+1}, s_{t+1})}{\frac{\partial f^i(t+1)}{\partial x_{t+1}^i}} \\ &+ \sum_{k=i+1}^M \left( \frac{\frac{\partial f^k(t+1)}{\partial x_{t+1}^k}}{\frac{\partial f^k(t+1)}{\partial x_{t+1}^k}} - \frac{\frac{\partial f^{k-1}(t+1)}{\partial x_{t+1}^{k-1}}}{\frac{\partial f^{k-1}(t+1)}{\partial x_{t+1}^{k-1}}} \right) u'_{x^k}(x_{t+1}, s_{t+1}). \end{aligned} \quad (10)$$

To recover the policy functions  $\delta_t, t \in 1, \dots, T-1$  the multi-dimensional EGM algorithm performs the following steps:

1. Initialize the backward induction with policy function  $\delta_T : (X_T, s_T) \rightarrow x_T$ . Proceed backwards through time periods  $t \in T-1, \dots, 1$ :
2. Loop over all points  $s_t$ , for each point  $s_t$ :
3. Proceed through the points of the fixed  $M$ -dimensional grid over post-decision states  $f(t) = (f^1(t), \dots, f^M(t))$ :
4. Conditional on the particular values of post-decision states  $\hat{f} = (\hat{f}^1, \dots, \hat{f}^M)$ , compute the right hand sides ( $\text{RHS}^1(\hat{f}), \dots, \text{RHS}^M(\hat{f})$ ) of the Euler equations (9) using (6) to find the values of the next period continuous states  $X_{t+1}$  and calculating the expectations over the idiosyncratic shocks  $\xi_{t+1}$ <sup>12</sup> and the transition probabilities of exogenous states  $s_{t+1}$ . The value  $\mathcal{L}_{t+1}^i$  in (9) can be both computed directly using the analytical formula (10) or interpolated over the endogenous grid in  $t+1$ , depending on whether the computational cost or the accuracy of the solution is prioritized. **Assumption A2** enables integrating over the transition probabilities of the exogenous state process. The optimal values of decision variables  $x_{t+1}$  are found using  $M$ -dimensional interpolation of the period  $t+1$  policy function  $\delta_{t+1}$ .
5. Solve the Euler equations in the system (9) for  $x_t$  in the order of permutation  $k^1$ . Namely start by computing  $x_t^j = \left( \frac{\partial u(x_t, s_t)}{\partial x_t^j} \right)^{-1} (\text{RHS}^j(\hat{f}), s_t)$ , where  $i = k_1^1$  and  $j = k_1^2$ , and then compute the rest of the elements of vector  $x_t$  in the order of permutation  $k^2$ , substituting previously computed solutions into every equation. The necessary analytical inverses of the partial derivatives exist due to **Assumption A4**, allowing for direct computations of the solutions of all Euler equations in the system. Due to strong monotonicity of partial derivatives of the utility function, each equation has exactly one solution, thus ensuring that the system as whole has exactly one solution.<sup>13</sup>

<sup>10</sup> See [Appendix](#) for the derivation.

<sup>11</sup> It follows that  $\mathcal{L}_{t+1}^i$  is a negative of the partial derivative of the period  $t+1$  value function with respect to  $X_{t+1}^i$ , see (18) in the [Appendix](#).

<sup>12</sup> Both quadrature, Monte Carlo or other methods can be used, see also [Judd \(1998, pp. 251–331\)](#).

<sup>13</sup> I assume existence of a solution for every equation (9), otherwise the solution set of problem (8) is empty.

6. Compute the values of continuous states  $X_t^j$ ,  $j \in \{1, \dots, M\}$ , from Eqs. (7) by forward substitution. The required implicit functions are analytic under [Assumption A3](#).
7. Continue through all the points of the grid on post-decision states in step 3, and by collecting the associated pairs  $(X_t, x_t)$  obtain (an approximation of) the current period policy function  $\delta_t : (X_t, s_t) \rightarrow x_t$  for given  $s_t$ .
8. Continue with the rest of the discrete state points  $s_t$  in step 2, and the rest of time periods in step 1 to recover the policy functions  $\delta_t : (X_t, s_t) \rightarrow x_t$  for all  $s_t$  and  $t$ . The algorithm concludes after period  $t = 1$  policy function is found (in the finite horizon case) or when two successive approximations of the policy functions are sufficiently close (in the infinite horizon case).

None of the steps 1–8 require root-finding operations. Yet, the algorithm consequently solves the first order conditions of the maximization problem in (8), and because by [Assumption A5](#) the problem is concave, finds the solution to the dynamic optimization problem.  $\square$

#### 4. Discussion and conclusions

The model of *multiple stock dynamics* is a typical member of the class of triangular dynamic optimization problems developed in this paper. Total wealth, various disaggregated financial assets, investments in housing and durables, overall and specific health, human capital and job specific human capital—are examples of stocks which dynamics can be modeled in various combinations with a triangular dynamic optimization problem.

The model of human capital accumulation by [Imai and Keane \(2004\)](#) is an example of two-dimensional triangular problem where choices of consumption  $C_t$  and labor supply  $h_t$  govern the dynamics of wealth  $A_t$  and human capital  $K_t$ . The transition rules are given by

$$K_{t+1} = \xi_{t+1} \left( k_0 + \delta K_t + g_1(t)(B_1 + K_t) \right) \times \left[ (h_t + d_1)^\alpha - B_2(h_t + d_1) \right], \quad (11)$$

$$A_{t+1} = (1 + r)A_t + RK_t h_t - C_t,$$

where  $r$  is interest rate,  $R$  rental rate of a unit of human capital,  $\xi_{t+1} \in \mathbb{R}^1$  is idiosyncratic wage shock, and  $(k_0, \delta, g_1(t), d_1, \alpha, B_1, B_2)$  are parameters ([Imai and Keane, 2004](#), pp. 605–608). With  $X_t = (K_t, A_t)$ ,  $\chi^1 = \xi_{t+1}f^1(K_t, h_t)$  and  $\chi^2 = f^2(K_t, h_t, A_t, C_t)$  [Assumptions A1–A3](#) are clearly satisfied. The utility function in the model is concave and additively separable, thus satisfying [A4](#) and [A5](#). With the proposed approach, the models like this can be further enriched by including additional dimensions, for example health process or job-specific human capital, at relatively low computational cost.

#### Acknowledgments

I am thankful to Bertel Schjerning, John Rust, Xiaodong Fan and Thomas Jørgensen for invaluable discussions, as well as participants of seminars at University of New South Wales, University of Copenhagen, Higher School of Economics, and the participants of the Initiative for Computational Economics at Zurich (ZICE 2014 and 2015). I acknowledge the financial support from the Australian Research Council Centre of Excellence in Population Ageing Research (project number CE110001029) and Michael P. Keane's Australian Research Council Laureate Fellowship (project number FL110100247).

#### Appendix. Derivation of the Euler equations

Consider the problem given by (6) and (8). Due to [A1–A2](#) the expectations can be written as  $E(\cdot | s_t, f(t))$ . The first order and envelope conditions in (8) are,  $j \in \{1, \dots, M\}$

$$\begin{aligned} u'_{x^j}(x_t, s_t) + \beta \sum_{i=1}^M E \left[ \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \right. \\ \left. \times \sum_{k=j}^M \left( \frac{\partial \chi^i}{\partial f^k} \frac{\partial f^k(t)}{\partial x_t^j} \right) \middle| s_t, f(t) \right] = 0 \\ \Rightarrow u'_{x^j}(x_t, s_t) + \beta \sum_{k=j}^M \frac{\partial f^k(t)}{\partial x_t^j} \\ \times E \left[ \sum_{i=1}^M \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \frac{\partial \chi^i}{\partial f^k} \middle| s_t, f(t) \right] = 0. \end{aligned} \quad (12)$$

$$\begin{aligned} \frac{\partial V_t(X_t, s_t)}{\partial X_t^j} &= \beta \sum_{i=1}^M E \left[ \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \right. \\ &\quad \left. \times \sum_{k=j}^M \left( \frac{\partial \chi^i}{\partial f^k} \frac{\partial f^k(t)}{\partial x_t^j} \right) \middle| s_t, f(t) \right] \\ &= \beta \sum_{k=j}^M \frac{\partial f^k(t)}{\partial x_t^j} \\ &\quad \times E \left[ \sum_{i=1}^M \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \frac{\partial \chi^i}{\partial f^k} \middle| s_t, f(t) \right]. \end{aligned} \quad (13)$$

Combination of (12) and (13) for  $j = M$  gives

$$\frac{\partial V_t(X_t, s_t)}{\partial X_t^M} = -\phi_t^M u'_{x^M}(x_t, s_t), \quad (14)$$

where  $\phi_t^M = \frac{\partial f^M(t)}{\partial x_t^M} / \frac{\partial f^M(t)}{\partial x_t^M}$ . Taking the differences in (12) and (13) between  $j \in \{1, \dots, M-1\}$  and  $j+1$  gives

$$\begin{aligned} u'_{x^j}(x_t, s_t) - u'_{x^{j+1}}(x_t, s_t) + \beta \frac{\partial f^j(t)}{\partial x_t^j} \\ \times E \left[ \sum_{i=1}^M \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \frac{\partial \chi^i}{\partial f^j} \middle| s_t, f(t) \right] = 0, \end{aligned} \quad (15)$$

$$\begin{aligned} \frac{\partial V_t(X_t, s_t)}{\partial X_t^j} - \frac{\partial V_t(X_t, s_t)}{\partial X_t^{j+1}} \\ = \beta \frac{\partial f^j(t)}{\partial x_t^j} E \left[ \sum_{i=1}^M \frac{\partial V_{t+1}(X_{t+1}, s_{t+1})}{\partial X_{t+1}^i} \frac{\partial \chi^i}{\partial f^j} \middle| s_t, f(t) \right], \end{aligned} \quad (16)$$

which leads to  $j \in \{1, \dots, M-1\}$

$$\frac{\partial V_t(X_t, s_t)}{\partial X_t^j} = \frac{\partial V_t(X_t, s_t)}{\partial X_t^{j+1}} + \phi_t^j [u'_{x^{j+1}}(x_t, s_t) - u'_{x^j}(x_t, s_t)]. \quad (17)$$

Linearizing the recursive expression (17) using (14) as the base, we have

$$\frac{\partial V_t(X_t, s_t)}{\partial X_t^j} = -\phi_t^j u'_{x^j}(x_t, s_t) - \sum_{i=j+1}^M (\phi_t^i - \phi_t^{i-1}) u'_{x^i}(x_t, s_t). \quad (18)$$

The system of Euler equations (9) follows from (12) and (18).

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## Erratum

# Corrigendum to “Multidimensional endogenous gridpoint method: Solving triangular dynamic stochastic optimization problems without root-finding operations” [Econ. Lett. 135 (2015) 72–76]



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## ARTICLE INFO

## Article history:

Assumption A1 in Iskhakov (2015) is incomplete. The correct version should read:

**Assumption A1.** Transition rules for the continuous state variables  $X_t^1, \dots, X_t^M, j \in \{1, \dots, M\}$  can be expressed in the form

$$X_{t+1}^j = \chi^j \left( f^1(X_t^1, x_t^1, s_t), f^2(X_t^1, x_t^1, X_t^2, x_t^2, s_t), \dots, f^M(X_t, x_t, s_t), s_t, s_{t+1}, \xi_{t+1} \right), \quad (1)$$

such that the post-decision states  $f(t) = (f^1(t), \dots, f^M(t)) \in \mathbb{R}^M$  admit the following structure

$$\begin{aligned} f^1(t) &= f^1(X_t^1, x_t^1, s_t), \\ f^2(t) &= f^2(X_t^1, x_t^1, X_t^2, x_t^2, s_t), \\ &\vdots \\ f^M(t) &= f^M(X_t^1, x_t^1, \dots, X_t^M, x_t^M, s_t) = f^M(X_t, x_t, s_t), \end{aligned} \quad (2)$$

where  $\chi^j(\cdot)$  and  $f^j(\cdot)$  are deterministic differentiable functions, the partial derivatives of  $f^j(t)$  take the form

$$\begin{aligned} \frac{\partial f^j(t)}{\partial x_t^i} &= \frac{\partial f^j(X_t^1, x_t^1, \dots, X_t^j, x_t^j, s_t)}{\partial x_t^i} \\ &= g_i^j \left( f^1(t), \dots, f^j(t), s_t \right), \quad i \leq j \end{aligned} \quad (3)$$

for each  $j = 1 \dots M$  and arbitrary functions  $g_i^j$ , and it holds  $\frac{\partial f^j(t)}{\partial x_t^j} \neq 0$  and  $\frac{\partial f^j(t)}{\partial x_t^j} \neq 0$ ;  $\xi_{t+1} \in \mathbb{R}^K$  are idiosyncratic shocks.

The additional condition (3) ensures that  $\frac{\partial f^k(t)}{\partial x_t^j}$  does not depend on the continuous state and decision variables in period  $t$  other than through the post decision states. These partial derivatives had been implicitly treated as constants in Section 3. I apologize for the error and express my gratitude to Jeppe Druedahl and Thomas Jørgensen at the University of Copenhagen for pointing it out.

With the above correction, the example in Section 4 is invalid. Yet, the main message of the paper is unchanged: triangular dynamic stochastic optimization problems with certain structure can be solved with the multidimensional version of the endogenous grid point method without any root-finding operations.

## References

- Iskhakov, F., 2015. Multidimensional endogenous gridpoint method: Solving triangular dynamic stochastic optimization problems without root-finding operations. *Econ. Lett.* 135, 72–76.