1 Unique, Stable Target and Steady State Points

This appendix proves Theorems 2-3 and:

Lemma 1. *If* $\check{m}$ *and* $\hat{m}$ *both exist, then* $\check{m} \leq \hat{m}$.

1.1 Proof of Theorem 2

The elements of the proof of Theorem 2 are:

- Existence and continuity of $\mathbb{E}_t[m_{t+1}/m_t]$
- Existence of a point where $\mathbb{E}_t[m_{t+1}/m_t] = 1$
- $\mathbb{E}_t[m_{t+1}] - m_t$ is monotonically decreasing

1.2 Existence and Continuity of $\mathbb{E}_t[m_{t+1}/m_t]$

The consumption function exists because we have imposed sufficient conditions (the WRIC and FVAC; Theorem 1).

Section 2.8 shows that for all t, $a_{t-1} = m_{t-1} - c_{t-1} > 0$. Since $m_t = a_{t-1}\mathcal{R}_t + \xi_t$, even if ξ_t takes on its minimum value of 0, $a_{t-1}\mathcal{R}_t > 0$, since both a_{t-1} and $\mathcal{R}_t$ are strictly positive. With m_t and m_{t+1} both strictly positive, the ratio $\mathbb{E}_t[m_{t+1}/m_t]$ inherits continuity (and, for that matter, continuous differentiability) from the consumption function.

1.3 Existence of a point where $\mathbb{E}_t[m_{t+1}/m_t] = 1$.

This follows from:

1. Existence and continuity of $\mathbb{E}_t[m_{t+1}/m_t]$ (just proven)
2. Existence a point where $\mathbb{E}_t[m_{t+1}/m_t] < 1$
3. Existence a point where $\mathbb{E}_t[m_{t+1}/m_t] > 1$
4. The Intermediate Value Theorem

1.3.1 Existence of m where $\mathbb{E}_t[m_{t+1}/m_t] < 1$

If RIC holds. Logic exactly parallel to that of Section 3.1 leading to equation (39), but dropping the Γ_{t+1} from the RHS, establishes that

$$\begin{aligned}\lim_{m_t \uparrow \infty} \mathbb{E}_t[m_{t+1}/m_t] &= \lim_{m_t \uparrow \infty} \mathbb{E}_t\left[\frac{\mathcal{R}_{t+1}(m_t - \mathrm{c}(m_t)) + \xi_{t+1}}{m_t}\right] \\ &= \mathbb{E}_t[(\mathsf{R}/\Gamma_{t+1})\text{\TH}_{\mathsf{R}}] \\ &= \mathbb{E}_t[\text{\TH}/\Gamma_{t+1}] \end{aligned} \tag{1}$$

$$< 1$$

where the inequality reflects imposition of the GIC-Nrm (27).

If RIC fails. When the RIC fails, the fact that $\lim_{m\uparrow\infty} \mathrm{c}'(m) = 0$ (see equation (31)) means that the limit of the RHS of (1) as $m \uparrow \infty$ is $\bar{\mathcal{R}} = \mathbb{E}_t[\mathcal{R}_{t+1}]$. In the next step of this proof, we will prove that the combination GIC-Nrm and ~~RIC~~ implies $\bar{\mathcal{R}} < 1$.

So we have $\lim_{m\uparrow\infty} \mathbb{E}_t[m_{t+1}/m_t] < 1$ whether the RIC holds or fails.

1.3.2 Existence of $m > 1$ where $\mathbb{E}_t[m_{t+1}/m_t] > 1$

Paralleling the logic for c in Section 3.2: the ratio of $\mathbb{E}_t[m_{t+1}]$ to m_t is unbounded above as $m_t \downarrow 0$ because $\lim_{m_t\downarrow 0} \mathbb{E}_t[m_{t+1}] > 0$.

Intermediate Value Theorem. If $\mathbb{E}_t[m_{t+1}/m_t]$ is continuous, and takes on values above and below 1, there must be at least one point at which it is equal to one.

1.3.3 $\mathbb{E}_t[m_{t+1}] - m_t$ is monotonically decreasing.

Now define $\boldsymbol{\zeta}(m_t) \equiv \mathbb{E}_t[m_{t+1}] - m_t$ and note that

$$\begin{aligned}
\boldsymbol{\zeta}(m_t) < 0 &\leftrightarrow \mathbb{E}_t[m_{t+1}/m_t] < 1 \\
\boldsymbol{\zeta}(m_t) = 0 &\leftrightarrow \mathbb{E}_t[m_{t+1}/m_t] = 1 \\
\boldsymbol{\zeta}(m_t) > 0 &\leftrightarrow \mathbb{E}_t[m_{t+1}/m_t] > 1,
\end{aligned} \tag{2}$$

so that $\boldsymbol{\zeta}(\hat{m}) = 0$. Our goal is to prove that $\boldsymbol{\zeta}(\bullet)$ is strictly decreasing on $(0, \infty)$ using the fact that

$$\begin{aligned}
\boldsymbol{\zeta}'(m_t) \equiv \left(\frac{d}{dm_t}\right)\boldsymbol{\zeta}(m_t) &= \mathbb{E}_t\left[\left(\frac{d}{dm_t}\right)(\mathcal{R}_{t+1}(m_t - \mathrm{c}(m_t)) + \xi_{t+1} - m_t)\right] \\
&= \bar{\mathcal{R}}\,(1 - \mathrm{c}'(m_t)) - 1.
\end{aligned} \tag{3}$$

Now, we show that (given our other assumptions) $\boldsymbol{\zeta}'(m)$ is decreasing (but for different reasons) whether the RIC holds or fails.

If RIC holds. Equation (18) indicates that if the RIC holds, then $\underline{\kappa} > 0$. We show at the bottom of Section 2.9.1 that if the RIC holds then $0 < \underline{\kappa} < \mathrm{c}'(m_t) < 1$ so that

$$\begin{aligned}
\bar{\mathcal{R}}\,(1 - \mathrm{c}'(m_t)) - 1 < \bar{\mathcal{R}}(1 - &\underbrace{(1 - \text{Þ}_{\mathsf{R}})}_{\underline{\kappa}}) - 1 \\
&= \bar{\mathcal{R}}\text{Þ}_{\mathsf{R}} - 1 \\
&= \mathbb{E}_t\left[\frac{\mathsf{R}}{\Gamma\psi}\frac{\text{Þ}}{\mathsf{R}}\right] - 1 \\
&= \underbrace{\mathbb{E}_t\left[\frac{\text{Þ}}{\Gamma\psi}\right]}_{=\text{Þ}_{\underline{\Gamma}}} - 1
\end{aligned}$$

which is negative because the GIC-Nrm says $\text{Þ}_{\underline{\Gamma}} < 1$.

If RIC fails. Under ~~RIC~~, recall that $\lim_{m\uparrow\infty} \mathrm{c}'(m) = 0$. Concavity of the consumption function means that c' is a decreasing function, so everywhere

$$\bar{\mathcal{R}}\,(1 - \mathrm{c}'(m_t)) < \bar{\mathcal{R}}$$

which means that $\boldsymbol{\zeta}'(m_t)$ from (3) is guaranteed to be negative if

$$\bar{\mathcal{R}} \equiv \mathbb{E}_t\left[\frac{\mathsf{R}}{\Gamma\psi}\right] < 1. \tag{4}$$

But the combination of the GIC-Nrm holding and the RIC failing can be written:

$$\overbrace{\mathbb{E}_t\left[\frac{\boldsymbol{\text{Þ}}}{\Gamma\psi}\right]}^{\text{Þ}_{\underline{\Gamma}}} < 1 < \overbrace{\frac{\boldsymbol{\text{Þ}}}{\mathsf{R}}}^{\text{Þ}_{\mathsf{R}}},$$

and multiplying all three elements by $\mathsf{R}/\boldsymbol{\text{Þ}}$ gives

$$\mathbb{E}_t\left[\frac{\mathsf{R}}{\Gamma\psi}\right] < \mathsf{R}/\boldsymbol{\text{Þ}} < 1$$

which satisfies our requirement in (4).

1.4 Proof of Theorem 3

The elements of the proof are:

- Existence and continuity of $\mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t]$
- Existence of a point where $\mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t] = 1$
- $\mathbb{E}_t[\psi_{t+1}m_{t+1} - m_t]$ is monotonically decreasing

1.4.1 Existence and Continuity of the Ratio

Since by assumption $0 < \underline{\psi} \leq \psi_{t+1} \leq \bar{\psi} < \infty$, our proof in 1.2 that demonstrated existence and continuity of $\mathbb{E}_t[m_{t+1}/m_t]$ implies existence and continuity of $\mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t]$.

1.4.2 Existence of a stable point

Since by assumption $0 < \underline{\psi} \leq \psi_{t+1} \leq \bar{\psi} < \infty$, our proof in Subsection 1.2 that the ratio of $\mathbb{E}_t[m_{t+1}]$ to m_t is unbounded as $m_t \downarrow 0$ implies that the ratio $\mathbb{E}_t[\psi_{t+1}m_{t+1}]$ to m_t is unbounded as $m_t \downarrow 0$.

The limit of the expected ratio as m_t goes to infinity is most easily calculated by modifying the steps for the prior theorem explicitly:

$$\begin{aligned}
\lim_{m_t\uparrow\infty} \mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t] &= \lim_{m_t\uparrow\infty} \mathbb{E}_t\left[\frac{\Gamma_{t+1}\left((\mathsf{R}/\Gamma_{t+1})\mathrm{a}(m_t) + \xi_{t+1}\right)/\Gamma}{m_t}\right] \\
&= \lim_{m_t\uparrow\infty} \mathbb{E}_t\left[\frac{(\mathsf{R}/\Gamma)\mathrm{a}(m_t) + \psi_{t+1}\xi_{t+1}}{m_t}\right]
\end{aligned}$$

$$
\begin{aligned}
&= \lim_{m_t \uparrow \infty} \left[\frac{(\mathsf{R}/\Gamma)\mathrm{a}(m_t)+1}{m_t} \right] \\
&= (\mathsf{R}/\Gamma)\text{Þ}_{\mathsf{R}} \qquad (5)\\
&= \text{Þ}_{\Gamma} \\
&< 1
\end{aligned}
$$

where the last two lines are merely a restatement of the GIC (21).

The Intermediate Value Theorem says that if $\mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t]$ is continuous, and takes on values above and below 1, there must be at least one point at which it is equal to one.

1.4.3 $\mathbb{E}_t[\psi_{t+1}m_{t+1}] - m_t$ *is monotonically decreasing.*

Define $\boldsymbol{\zeta}(m_t) \equiv \mathbb{E}_t[\psi_{t+1}m_{t+1}] - m_t$ and note that

$$
\begin{aligned}
\boldsymbol{\zeta}(m_t) < 0 &\leftrightarrow \mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t] < 1 \\
\boldsymbol{\zeta}(m_t) = 0 &\leftrightarrow \mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t] = 1 \qquad (6)\\
\boldsymbol{\zeta}(m_t) > 0 &\leftrightarrow \mathbb{E}_t[\psi_{t+1}m_{t+1}/m_t] > 1,
\end{aligned}
$$

so that $\boldsymbol{\zeta}(\hat{m}) = 0$. Our goal is to prove that $\boldsymbol{\zeta}(\bullet)$ is strictly decreasing on $(0, \infty)$ using the fact that

$$
\begin{aligned}
\boldsymbol{\zeta}'(m_t) \equiv \left(\frac{d}{dm_t}\right)\boldsymbol{\zeta}(m_t) &= \mathbb{E}_t\left[\left(\frac{d}{dm_t}\right)(\mathcal{R}(m_t - \mathrm{c}(m_t)) + \psi_{t+1}\xi_{t+1} - m_t)\right] \qquad (7)\\
&= (\mathsf{R}/\Gamma)\left(1 - \mathrm{c}'(m_t)\right) - 1.
\end{aligned}
$$

Now, we show that (given our other assumptions) $\boldsymbol{\zeta}'(m)$ is decreasing (but for different reasons) whether the RIC holds or fails (~~RIC~~).

If RIC holds. Equation (18) indicates that if the RIC holds, then $\underline{\kappa} > 0$. We show at the bottom of Section 2.9.1 that if the RIC holds then $0 < \underline{\kappa} < \mathrm{c}'(m_t) < 1$ so that

$$
\begin{aligned}
\mathcal{R}\left(1 - \mathrm{c}'(m_t)\right) - 1 &< \mathcal{R}(1 - \underbrace{(1 - \text{Þ}_{\mathsf{R}})}_{\underline{\kappa}}) - 1 \\
&= (\mathsf{R}/\Gamma)\text{Þ}_{\mathsf{R}} - 1
\end{aligned}
$$

which is negative because the GIC says $\text{Þ}_{\Gamma} < 1$.

If RIC fails. Under ~~RIC~~, recall that $\lim_{m\uparrow\infty} \mathrm{c}'(m) = 0$. Concavity of the consumption function means that c' is a decreasing function, so everywhere

$$
\mathcal{R}\left(1 - \mathrm{c}'(m_t)\right) < \mathcal{R}
$$

which means that $\boldsymbol{\zeta}'(m_t)$ from (7) is guaranteed to be negative if

$$
\mathcal{R} \equiv (\mathsf{R}/\Gamma) < 1. \qquad (8)
$$

But we showed in Section 2.6 that the only circumstances under which the problem has a nondegenerate solution while the RIC fails were ones where the FHWC also fails (that is, (8) holds).

1.5 A Third Measure

A footnote in Section 3 mentions the possibility of calculating growth in the expectation of the log of m rather than the expectation of the ratio. Here we show that one way of doing that is to calculate a nonlinear adjustment factor for the expectation of the ratio.

$$\begin{aligned}
\log\left(\mathbf{m}_{t+1}/\mathbf{m}_t\right) &= \log(\Gamma\psi_{t+1}m_{t+1}) - \log m_t \\
&= \log\Gamma(a_t\mathcal{R} + \psi_{t+1}\xi_{t+1}) - \log m_t \\
&= \log\Gamma(a_t\mathcal{R} + 1 + (\psi_{t+1}\xi_{t+1} - 1)) - \log m_t
\end{aligned}$$

Now define $\tilde{m}_{t+1} = a_t\mathcal{R} + 1$, and compute the expectation:

$$\begin{aligned}
\mathbb{E}_t[\log\left(\mathbf{m}_{t+1}/\mathbf{m}_t\right)] &= \mathbb{E}_t\left[\log\Gamma(\tilde{m}_{t+1} + (\psi_{t+1}\xi_{t+1} - 1))\right] - \log m_t \\
&= \log\Gamma + \mathbb{E}_t\left[\log(\tilde{m}_{t+1}(1 + \tilde{m}_{t+1}^{-1}(\psi_{t+1}\xi_{t+1} - 1))\right] - \log m_t \\
&= \underbrace{\log\Gamma + \log\tilde{m}_{t+1} - \log m_t}_{\equiv\log\mathbb{E}_t[\mathbf{m}_{t+1}/\mathbf{m}_t]} + \mathbb{E}_t\left[\log(1 + \tilde{m}_{t+1}^{-1}(\psi_{t+1}\xi_{t+1} - 1))\right]
\end{aligned}$$

and exponentiating tells us that

$$\exp(\mathbb{E}_t[\log\mathbf{m}_{t+1}/\mathbf{m}_t]) = \mathbb{E}_t[\mathbf{m}_{t+1}/\mathbf{m}_t]\exp(\mathbb{E}_t\left[\log(1 + \tilde{m}_{t+1}^{-1}(\psi_{t+1}\xi_{t+1} - 1))\right]) \tag{9}$$

and this latter factor is a number that approaches 1 from below as m_t rises. Thus the expected growth rate of the log is smaller than the log of the growth rate of the expected ratio.

1.6 Proof of Lemma

1.6.1 Pseudo-Steady-State m Is Smaller than Target m

Designate

$$\begin{aligned}
\check{\mathrm{m}}_{t+1}(a) &= 1 + a\mathcal{R} \\
\hat{\mathrm{m}}_{t+1}(a) &= 1 + a\underbrace{\mathcal{R}/\underline{\psi}}_{\bar{\mathcal{R}}>\mathcal{R}}
\end{aligned} \tag{10}$$

so that we can implicitly define the target and pseudo-steady-state points as

$$\begin{aligned}
\hat{m} &= \hat{\mathrm{m}}_{t+1}(\hat{m} - \mathrm{c}(\hat{m})) \\
\check{m} &= \check{\mathrm{m}}_{t+1}(\check{m} - \mathrm{c}(\check{m}))
\end{aligned} \tag{11}$$

Then subtract:

$$\begin{aligned}
\hat{m} - \check{m} &= \left(\hat{a}\underline{\psi}^{-1} - \check{a}\right)\mathcal{R} \\
&= \left(a(\hat{m})\underline{\psi}^{-1} - a(\check{m})\right)\mathcal{R} \\
&= \left(a(\hat{m})\underline{\psi}^{-1} - (a(\hat{m} + \check{m} - \hat{m}))\right)\mathcal{R} \\
&\approx \left(a(\hat{m})\underline{\psi}^{-1} - (a(\hat{m}) + (\check{m} - \hat{m})\mathrm{a}'(\hat{m}))\right)\mathcal{R} \\
(\hat{m} - \check{m})(1 - \underbrace{a'(\hat{m})\mathcal{R}}_{<\text{Þ}_\Gamma<1}) &= (\underline{\psi}^{-1} - 1)\hat{a}\mathcal{R}
\end{aligned} \tag{12}$$

The RHS of this equation is strictly positive because $\underline{\psi}^{-1} > 1$ and both $\hat{a}$ and $\mathcal{R}$ are positive; while on the LHS, $(1 - \mathcal{R}a') > 0$. So the equation can only hold if $\hat{m} - \check{m} > 0$. That is, the target ratio exceeds the pseudo-steady-state ratio.[1]

1.6.2 The m Achieving Individual Expected-Log-Balanced-Growth Is Smaller than the Individual Pseudo-Steady-State m

Expected log balanced growth occurs when

$$
\begin{aligned}
\mathbb{E}_t[\log \mathbf{m}_{t+1}] &= \log \Gamma \mathbf{m}_t \\
\mathbb{E}_t[\log \mathbf{p}_{t+1} m_{t+1}] &= \log \Gamma \mathbf{p}_t m_t \\
\mathbb{E}_t[\log \psi_{t+1} m_{t+1}] &= \log \Gamma m_t \\
\mathbb{E}_t[\log (a(m_t)\mathsf{R} + \psi_{t+1}\xi_{t+1}\Gamma)] &= \log \Gamma m_t \\
\mathbb{E}_t[\log (a(m_t)\mathcal{R} + \psi_{t+1}\xi_{t+1})] &= \log m_t
\end{aligned} \tag{13}
$$

and we call the m that satisfies this equation $\tilde{m}$.

Subtract the definition of $\check{m}$ from that of $\tilde{m}$:

$$
\exp(\mathbb{E}_t[\log (a(\tilde{m})\mathcal{R} + \psi_{t+1}\xi_{t+1})]) - (a(\check{m})\mathcal{R} + 1) = \tilde{m} - \check{m} \tag{14}
$$

Now we use the fact that the expectation of the log is less than the log of the expectation,

$$
\exp(\mathbb{E}_t[\log (a(\tilde{m})\mathcal{R} + \psi_{t+1}\xi_{t+1})]) < (a(\tilde{m})\mathcal{R} + 1) \tag{15}
$$

so

$$
\begin{aligned}
\exp(\mathbb{E}_t[\log (a(\tilde{m})\mathcal{R} + 1)]) - (a(\check{m})\mathcal{R} + 1) &< \tilde{m} - \check{m} \\
(a(\tilde{m})\mathcal{R} + 1) - (a(\check{m})\mathcal{R} + 1) &< \tilde{m} - \check{m} \\
(a(\tilde{m}) - a(\tilde{m} + \check{m} - \tilde{m}))\mathcal{R} &< \tilde{m} - \check{m} \\
(a(\tilde{m}) - (a(\tilde{m}) + (\check{m} - \tilde{m})\bar{\mathrm{a}}')\mathcal{R} &< \tilde{m} - \check{m} \\
(\tilde{m} - \check{m})\bar{\mathrm{a}}'\mathcal{R} &< \tilde{m} - \check{m} \\
\underbrace{\bar{\mathrm{a}}'\mathcal{R}}_{<\text{Þ}_\Gamma} &< 1
\end{aligned} \tag{16}
$$

where we are interpreting $\bar{\mathrm{a}}'$ as the mean of the value of a' over the interval between $\tilde{m}$ and $\check{m}$.

[1]The use of the first order Taylor approximation could be substituted, cumbersomely, with the average of a' over the interval to remove the approximation in the derivations above.