Things to continue to think about:

Equation (1): Being elite is not something that enters into the representative consumer’s utility. This is nice in the sense that we can show the kinds of relationships we want, but on the other hand it drops the idea that the elite is very interested in maintaining their status per se. This has pluses and minuses since sticking a demand for being elite into the model could be said to be “baking in” the result.

Equation (2): There are also a couple of things happening here. So, being elite (as indicated by the theta parameter) is not something that can be gained or lost. One is simply endowed with it. Also, it is not an economically meaningless social feature: here it is assumed that high status people can squeeze more education out of their budget that equally wealthy alternative consumers. So, we are at least saying that high status makes the consumer more productive in terms of getting high E\_t.

Equation (3): The expectation on the part of the consumer is that returns in period t+1 will be dependent on the level of education and the return. Notice that, at this point, this is all consistent with a model in which education actually plays a productive role in the market.

Equation (4) seems to have a disconnect. The profit of colleges is assumed to be \tau\alpha Y\_t. But, if that is true, then the budget constrain in (2) is not correct. The revenue of the college is paid for by the consumer. That is, we are showing in (2) that the consumer pays (in our latest discussion$ (E\_t)/(\theta) for a level of education E\_t, right? But the college receives a payment of \tau\alpha Y\_t. If this is a general equilibrium model, then these need to be connected. Also, in (7) I am not sure where the \delta parameter came from. Should it be \rho or \beta?

Equation (9) adds a cost to firms of hiring educated people (let’s assume education does not enter into revenue as we discussed). This is where I feel the model is weakest. The people here (where I am going to give the talk) are firmly of the belief that markets would discipline all this kind of BS. So, firms paying for high E\_t where E\_t adds nothing to the productivity - they would say - simply go out of business. The only reason they don’t is because we bake into the model that they don’t have to. This is not going to fly, I suspect.

My original vision for the model is one in which these problems persist as an endogenous feature of the model, not because we bake it in. Now, of course, you have to bake it in somewhere. But, I am still of the opinion that it should probably be a feature of utility - you consume stuff and status.

Perhaps rather than being endowed with status, it could also be a choice variable. Or it could be a function of E\_t as we have been discussing (to create a role for schools that don’t do anything other than provide status). Still, questions remain about why competitive firms would ever blow money. However, if the representative agent receives or maintains status according to something happening in the last period, they may be willing to buy status through education and see some return to it in period 2.

In any event, I think that the firms should be competitive, but providing consumption in terms of both profit and status. Or something like that.