Economics 314 | Spring 2014
Daily Question #9 | February 14 ♥

In our analysis of the Solow model, we characterized the Golden Rule level of $k^* = k_{GR}$ as "optimal" in the sense of maximizing steady-state consumption per person. In the Ramsey model, our "persons" like consumption, so it seems like the Golden Rule level of k^* would be optimal here as well, but it is not. If a Ramsey economy were initially at the Golden Rule level of k_{GR}, why would households not choose to save enough to sustain $k^* = k_{GR}$? Show the initial level of consumption per effective labor unit and the convergence path on a phase plane for an economy that starts with $k = k_{GR}$.