

Online Appendix

Monetary Policy, Redistribution, and Risk Premia

A Proofs of analytical results

A.1 Proposition 1

Proof. Multiplying both sides of (14) by a_0^i , integrating over all i , and then using asset market clearing $\int_0^1 a_0^i \omega_0^i di = \int_0^1 a_0^i di$, we obtain the claimed expression for the risk premium on capital. Differentiating with respect to ϵ_0^m , we have that

$$\frac{d [\mathbb{E}_0 \log(1 + r_1^k) - \log(1 + r_1)]}{d\epsilon_0^m} = \sigma^2 \frac{d\gamma}{d\epsilon_0^m} = \gamma \sigma^2 \int_0^1 \frac{d [a_0^i / \int_0^1 a_0^i di']}{d\epsilon_0^m} (1 - \omega_0^i) di,$$

as claimed, where the second equality uses (14) and asset market clearing. \square

A.2 Proposition 2

Proof. The result for $\frac{dk_0}{d\epsilon_0^m}$ follows from differentiating (16). Now differentiating household i 's consumption policy function and (17) and integrating over all i yields

$$\frac{dc_0}{d\epsilon_0^m} = (1 - \beta) \left[\frac{dy_0}{d\epsilon_0^m} + \frac{(1 - \delta_0)q_0 k_{-1}}{k_0} \chi^x \frac{dk_0}{d\epsilon_0^m} \right],$$

where we have used firms' flow of funds, asset market clearing, and equilibrium investment. Differentiating goods market clearing and using equilibrium investment yields

$$\frac{dy_0}{d\epsilon_0^m} = \frac{dc_0}{d\epsilon_0^m} + q_0 \left(1 + \frac{x_0}{k_0} \chi^x \right) \frac{dk_0}{d\epsilon_0^m}.$$

Combining these and using capital accumulation yields the result for $\frac{dc_0}{d\epsilon_0^m}$. \square

A.3 Proposition 3

Proof. The Taylor rule and Fisher equation imply

$$\frac{d\pi_0^P}{d\epsilon_0^m} = \frac{1}{\phi} \frac{d \log(1 + r_1)}{d\epsilon_0^m} - \frac{1}{\phi}. \quad (\text{A.1})$$

Combining with equilibrium labor demand, the production function, and a rigid nominal wage in period 0 yields

$$\frac{1}{y_0} \frac{dy_0}{d\epsilon_0^m} = \frac{1-\alpha}{\alpha} \frac{1}{\phi} \frac{d \log(1+r_1)}{d\epsilon_0^m} - \frac{1-\alpha}{\alpha} \frac{1}{\phi}. \quad (\text{A.2})$$

By (15), (18), and (20), it follows that

$$\frac{dk_0}{d\epsilon_0^m} = -\frac{k_0}{1-\alpha+\chi^x} \left[-\gamma\sigma^2 \frac{1}{n_0} \text{Cov}^i \left(\frac{dn_0^i}{d\epsilon_0^m}, \omega_0^i \right) + \frac{d \log(1+r_1)}{d\epsilon_0^m} \right], \quad (\text{A.3})$$

where Cov^i denotes a cross-sectional covariance. Combining this with (21), (A.1),

$$\frac{1}{\pi_0} \frac{d\pi_0}{d\epsilon_0^m} = \frac{1}{y_0} \frac{dy_0}{d\epsilon_0^m} \quad (\text{A.4})$$

implied by equilibrium profits, and

$$\frac{1}{q_0} \frac{dq_0}{d\epsilon_0^m} = \chi^x \frac{1}{k_0} \frac{dk_0}{d\epsilon_0^m} \quad (\text{A.5})$$

implied by equilibrium investment, we have that

$$\begin{aligned} \text{Cov}^i \left(\frac{dn_0^i}{d\epsilon_0^m}, \omega_0^i \right) &= \frac{1}{1-\gamma\sigma^2(1-\delta_0) \frac{q_0}{n_0} \frac{\chi^x}{1-\alpha+\chi^x} \text{Cov}^i(k_{-1}^i, \omega_0^i)} \times \\ &\quad \left[-\text{Cov}^i \left(\frac{1+i_{-1}}{P_0} B_{-1}^i, \omega_0^i \right) \left(\frac{1}{\phi} \frac{d \log(1+r_1)}{d\epsilon_0^m} - \frac{1}{\phi} \right) + \right. \\ &\quad \left. \left(\frac{\pi_0}{y_0} \frac{dy_0}{d\epsilon_0^m} - (1-\delta_0)q_0 \frac{\chi^x}{1+\alpha+\chi^x} \frac{d \log(1+r_1)}{d\epsilon_0^m} \right) \text{Cov}^i(k_{-1}^i, \omega_0^i) \right]. \quad (\text{A.6}) \end{aligned}$$

Finally, combining (A.3) and (19) yields

$$\frac{dy_0}{d\epsilon_0^m} = \left[\gamma\sigma^2 \text{Cov}^i \left(\frac{dn_0^i}{d\epsilon_0^m}, \omega_0^i \right) - n_0 \frac{d \log(1+r_1)}{d\epsilon_0^m} \right] \times \left(\frac{1+\chi^x(1-\beta(1-\delta_0)k_{-1}/k_0)}{1-\alpha+\chi^x} \right). \quad (\text{A.7})$$

With heterogeneity in γ^i and the assumption that households' initial endowments are consistent with the portfolios (14), we have $\text{Cov}^i(B_{-1}^i, \omega_0^i) < 0$ and $\text{Cov}^i(k_{-1}^i, \omega_0^i) > 0$. At least around the RANK benchmark with the same aggregate allocation, the sys-

tem of equations (A.2), (A.6), and (A.7) thus implies

$$\begin{aligned} \frac{dy_0}{d\epsilon_0^m} &< \frac{dy_0}{d\epsilon_0^m}|_{RANK} < 0, \\ Cov^i \left(\frac{dn_0^i}{d\epsilon_0^m}, \omega_0^i \right) &< 0 = Cov^i \left(\frac{dn_0^i}{d\epsilon_0^m}, \omega_0^i \right) |_{RANK}, \\ 0 &< \frac{d \log(1+r_1)}{d\epsilon_0^m} < \frac{d \log(1+r_1)}{d\epsilon_0^m} |_{RANK} < 1. \end{aligned}$$

We can thus conclude from (A.1), (A.4), and (A.5) that a monetary tightening generates deflation, a fall in profits, and a fall in the price of capital; from (A.6) that it generates a rise in the risk premium only in the model with heterogeneity; and that the real effects of a monetary shock are amplified in the model with heterogeneity. \square

A.4 Proposition 4

Proof. For a household up against a portfolio constraint or following a rule-of-thumb, their equilibrium portfolio ω_0^i is simply implied by the constraint or rule-of-thumb. For all other households, a Taylor approximation of (13) yields the optimal portfolio share in capital

$$\omega_0^i \approx \frac{1}{\gamma^i(\varsigma^i + \eta^i)} \frac{\mathbb{E}_0^i \log(1 + r_1^{k,i}) - \log(1 + r_1) + \frac{1}{2}(\varsigma^i + \eta^i)\sigma^2}{\sigma^2}, \quad (\text{A.8})$$

where \mathbb{E}_0^i is the household's subjective expectation and $r_1^{k,i}$ is the return on capital accounting for the idiosyncratic component of its return. Given the distributional assumptions on η^i and ς^i , we have that

$$\mathbb{E}_0^i \log(1 + r_1^{k,i}) - \log(1 + r_1) + \frac{1}{2}(\varsigma^i + \eta^i)\sigma^2 = \mathbb{E}_0 \log(1 + r_1^k) - \log(1 + r_1) + \frac{1}{2}\sigma^2, \quad (\text{A.9})$$

where \mathbb{E}_0 denotes the objective expectation and r_1^k the return on capital without idiosyncratic risk (equivalently, aggregating over idiosyncratic risk). Then multiplying both sides of (A.8) by a_0^i , integrating over all unconstrained households which we denote as the set $i \notin C$, and then using asset market clearing, it is straightforward to show

$$\mathbb{E}_0 \log(1 + r_1^k) - \log(1 + r_1) + \frac{1}{2}\sigma^2 = \gamma\sigma^2$$

where now

$$\gamma \equiv \left(1 - \frac{\int_{i \notin C} a_0^i (1 - \omega_0^i) di}{\int_{i \notin C} a_0^i di} \right) \left(\int_{i \notin C} \frac{a_0^i}{\int_{i' \notin C} a_0^{i'} di'} \frac{1}{\gamma^i (\varsigma^i + \eta^i)} di \right)^{-1}.$$

Differentiating and again using market clearing, (A.8) for unconstrained households, and (A.9) yields

$$\frac{d [\mathbb{E}_0 \log(1 + r_1^k) - \log(1 + r_1)]}{d\epsilon_0^m} = \gamma \left(\frac{\int_0^1 a_0^i di}{\int_{i \notin C} a_0^i \omega_0^i di} \right) \sigma^2 \int_0^1 \frac{d \left[a_0^i / \int_0^1 a_0^{i'} di' \right]}{d\epsilon_0^m} (1 - \omega_0^i) di.$$

The remaining arguments in Propositions 2 and 3 are unchanged. \square

A.5 Proposition 5

Proof. We first characterize households' portfolio share in capital in the limit of zero aggregate risk. Up to second-order, (13) implies

$$\mathbb{E}_0 \hat{r}_1^k - \hat{r}_1 + \frac{1}{2} \sigma^2 = \gamma^i \delta_{z_1}^{c_1^i} \sigma^2 + o(\|\cdot\|^3) \quad (\text{A.10})$$

given the first-order approximation of \hat{c}_1^i in terms of the states

$$\hat{c}_1^i = \delta_{z_1}^{c_1^i} \hat{\epsilon}_1^z + \delta_{m_0}^{c_1^i} \hat{\epsilon}_0^m + o(\|\cdot\|^2)$$

with coefficients δ . Anticipating the result in Proposition 1, it follows that

$$\delta_{z_1}^{c_1^i} = \frac{\bar{\gamma}}{\gamma^i}. \quad (\text{A.11})$$

Approximating up to first order the period 1 resource constraint and equilibrium wages and profits, the method of undetermined coefficients implies

$$\delta_{z_1}^{c_1^i} = \frac{\bar{w}_1 + \bar{\pi}_1 \bar{k}_0^i}{\bar{c}_1^i}. \quad (\text{A.12})$$

Substituting in (A.11) and re-arranging, we can conclude that

$$\frac{\bar{q}_0 \bar{k}_0^i}{\bar{a}_0^i} = \frac{\bar{\pi}_1 \bar{k}_0^i}{(1 + \bar{r}_1) \bar{a}_0^i} = \frac{\bar{c}_1^i}{(1 + \bar{r}_1) \bar{a}_0^i} \frac{\bar{\gamma}}{\gamma^i} - \frac{\bar{w}_1}{(1 + \bar{r}_1) \bar{a}_0^i},$$

where the first equality uses $\bar{q}_0 = \frac{\bar{\pi}_1}{1+\bar{r}_1}$ absent aggregate risk.

We now characterize households' marginal responses to a unit of income in the limit of zero aggregate risk. Differentiating and combining households' optimal portfolio choice condition and period 1 resource constraint yields

$$0 = \mathbb{E}_0 (c_1^i)^{-\gamma^i} \frac{\gamma^i}{c_1^i} (r_1^k - r_1) \left((1+r_1) \frac{\partial b_0^i}{\partial n_0^i} + \pi_1 \frac{\partial k_0^i}{\partial n_0^i} \right). \quad (\text{A.13})$$

A second-order approximation then implies

$$\begin{aligned} 0 = & \left((1+\bar{r}_1) \frac{\overline{\partial b_0^i}}{\partial n_0^i} + \bar{\pi}_1 \frac{\overline{\partial k_0^i}}{\partial n_0^i} \right) \left(\mathbb{E}_0 \hat{r}_1^k - \hat{r}_1 + \frac{1}{2} \sigma^2 \right) \\ & - \left((1+\bar{r}_1) \frac{\overline{\partial b_0^i}}{\partial n_0^i} + \bar{\pi}_1 \frac{\overline{\partial k_0^i}}{\partial n_0^i} \right) \frac{\gamma^i + 1}{\bar{c}_1^i} (\bar{w}_1 + \bar{\pi}_1 \bar{k}_0^i) \sigma^2 + \bar{\pi}_1 \frac{\overline{\partial k_0^i}}{\partial n_0^i} \sigma^2 + o(\|\cdot\|^3). \end{aligned} \quad (\text{A.14})$$

Again anticipating the result in Proposition 1 and using (A.11) and (A.12), it follows from (A.14) that

$$\bar{q}_0 \frac{\overline{\partial k_0^i}}{\partial n_0^i} = \frac{\bar{\gamma}}{\gamma^i} \frac{\overline{\partial a_0^i}}{\partial n_0^i}$$

using $\bar{q}_0 = \frac{\bar{\pi}_1}{1+\bar{r}_0}$ and $\frac{\overline{\partial b_0^i}}{\partial n_0^i} + \bar{q}_0 \frac{\overline{\partial k_0^i}}{\partial n_0^i} = \frac{\overline{\partial a_0^i}}{\partial n_0^i}$. The expression for $\overline{mpr}_0^i \equiv \frac{\overline{\partial k_0^i}}{\frac{\overline{\partial a_0^i}}{\partial n_0^i}}$ follows. \square

A.6 Proposition 6

Proof. We first derive the result up to second order. Multiplying both sides of (A.10) by $\frac{\bar{c}_1^i}{\gamma^i}$, integrating over all households i , and making use of the market clearing conditions which imply that

$$\int_0^1 \bar{c}_1^i di = \int_0^1 (\bar{w}_1 + \bar{\pi}_1 \bar{k}_0^i) di,$$

we obtain

$$\mathbb{E}_0 \hat{r}_1^k - \hat{r}_0 + \frac{1}{2} \sigma^2 = \left(\frac{\bar{c}_1^i}{\int_0^1 \bar{c}_1^{i'} di'} \frac{1}{\gamma^i} \right)^{-1} \sigma^2 + o(\|\cdot\|^3), \quad (\text{A.15})$$

defining $\bar{\gamma}$ as in the claim.

We now derive the result up to third order. The third-order approximation of optimal portfolio choice for household i is

$$\mathbb{E}_0 \hat{r}_1^k - \hat{r}_1 + \frac{1}{2} \sigma^2 = \gamma^i \delta_{z_1}^{c_1^i} \sigma^2 + \left[\gamma^i \left(\delta_{m_0}^{c_1^i} \gamma + \delta_{m_0 z_1}^{c_1^i} \right) - (\gamma^i)^2 \delta_{m_0}^{c_1^i} \delta_{z_1}^{c_1^i} + \gamma^i \delta_{z_1}^{c_1^i} \delta_{m_0}^{r_1} - \gamma \delta_{m_0}^{r_1} \right] \hat{\epsilon}_0^m \sigma^2 + o(\|\cdot\|^4).$$

given the second-order expansion of \hat{c}_1^i in terms of the underlying states

$$\hat{c}_1^i = \delta_{m_0}^{c_1^i} \hat{\epsilon}_0^m + \delta_{z_1}^{c_1^i} \hat{\epsilon}_1^z + \frac{1}{2} \delta_{m_0}^{c_1^i} (\hat{\epsilon}_0^m)^2 + \delta_{m_0 z_1}^{c_1^i} \hat{\epsilon}_0^m \hat{\epsilon}_1^z + \frac{1}{2} \delta_{z_1}^{c_1^i} (\hat{\epsilon}_1^z)^2 + \frac{1}{2} \delta_{\sigma^2}^{c_1^i} \sigma^2 + o(\|\cdot\|^3).$$

Making use of (A.11) substantially simplifies this to

$$\mathbb{E}_0 \hat{r}_1^k - \hat{r}_1 + \frac{1}{2} \sigma^2 = \gamma^i \delta_{z_1}^{c_1^i} \sigma^2 + \gamma^i \delta_{m_0 z_1}^{c_1^i} \hat{\epsilon}_0^m \sigma^2 + o(\|\cdot\|^4). \quad (\text{A.16})$$

Again multiplying both sides by $\frac{\bar{c}_1^i}{\gamma^i}$, integrating over all households i , and making use of the market clearing conditions, we obtain

$$\mathbb{E}_0 \hat{r}_1^k - \hat{r}_1 + \frac{1}{2} \sigma^2 = \bar{\gamma} \sigma^2 + \frac{\bar{\gamma}}{\int_0^1 \bar{c}_1^i di} \left(\int_0^1 \bar{c}_1^i \delta_{m_0 z_1}^{c_1^i} di \right) \hat{\epsilon}_0^m \sigma^2 + o(\|\cdot\|^4).$$

It remains to further characterize the coefficient on $\hat{\epsilon}_0^m \sigma^2$ in closed form. Taking a second-order approximation of the period 1 resource constraint and equilibrium wages and profits, the method of undetermined coefficients implies

$$\bar{c}_1^i \delta_{m_0 z_1}^{c_1^i} + \bar{c}_1^i \delta_{m_0}^{c_1^i} \delta_{z_1}^{c_1^i} = \alpha \bar{w}_1 \delta_{m_0}^{k_0} + \bar{\pi}_1 \delta_{m_0}^{k_0^i} - (1 - \alpha) \bar{\pi}_1 \bar{k}_0^i \delta_{m_0}^{k_0}. \quad (\text{A.17})$$

It follows that

$$\int_0^1 \bar{c}_1^i \delta_{m_0 z_1}^{c_1^i} di = - \int_0^1 \bar{c}_1^i \delta_{m_0}^{c_1^i} \delta_{z_1}^{c_1^i} di + \bar{\pi}_1 \int_0^1 \delta_{m_0}^{k_0^i} di,$$

using market clearing and the definition of equilibrium wages and profits.¹ Further using a first-order approximation to capital claims market clearing and goods market clearing implies

$$\int_0^1 \bar{c}_1^i \delta_{m_0 z_1}^{c_1^i} di = \int_0^1 \bar{c}_1^i \delta_{m_0}^{c_1^i} \left(1 - \delta_{z_1}^{c_1^i} \right) di = \int_0^1 \bar{c}_1^i \delta_{m_0}^{c_1^i} \left(1 - \frac{\bar{\gamma}}{\gamma^i} \right) di,$$

where the second equality uses (A.11). Recall from Proposition 5 that $\overline{mpr}_0^i \equiv \frac{\bar{\gamma}}{\gamma^i}$.

¹We linearize rather than log-linearize with respect to $\{k_0^i, b_0^i, a_0^i\}$ since these may be negative.

Since the definition of $\bar{\gamma}$ implies

$$\int_0^1 \bar{c}_1^i \delta_{m_0}^{c_1^i} \left(1 - \frac{\bar{\gamma}}{\gamma^i}\right) di = \int_0^1 \left(\bar{c}_1^i \delta_{m_0}^{c_1^i} - \frac{\bar{c}_1^i}{\int_0^1 \bar{c}_1^{i'} di'} \int_0^1 \bar{c}_1^{i'} \delta_{m_0}^{c_1^{i'}} di' \right) \left(1 - \frac{\bar{\gamma}}{\gamma^i}\right) di$$

and

$$\frac{d \left[\frac{c_1^i}{\int_0^1 c_1^{i'}} \right]}{d\epsilon_0^m} = \frac{1}{\int_0^1 \bar{c}_1^{i'} di'} \left(\bar{c}_1^i \delta_{m_0}^{c_1^i} - \frac{\bar{c}_1^i}{\int_0^1 \bar{c}_1^{i'} di'} \int_0^1 \bar{c}_1^{i'} \delta_{m_0}^{c_1^{i'}} di' \right),$$

we obtain the coefficient on $\hat{\epsilon}_0^m \sigma^2$ given in the claim. \square

B Empirical appendix

B.1 The effect of monetary shocks

B.1.1 Robustness to details of estimation approach

We first demonstrate that the broad messages of our baseline estimates of the effects of a monetary policy shock in section 3.1 are robust to details of the estimation.

Given a monetary policy shock, Table A.1 summarizes the impact effect on the 1-year Treasury yield, the impact effect on the real S&P 500 return (implied by the real rate and excess return), and the share of the latter accounted for by news about future excess returns in the Campbell-Shiller decomposition (26). First, we find that the baseline results using 6 lags in the VAR are little affected if 4-8 lags are used instead. Second, we find that the results are broadly robust to using the same January 1991 - June 2012 period for both the VAR and IV regressions, or limiting the analysis of monetary policy shocks to the first half of the IV sample alone (January 1991 - September 2001). The expansionary monetary policy shock lowers the stock market when using the second half of the IV sample alone (October 2001 - June 2012), but we note that the instrument is weak over this sub-sample (having a first-stage F statistic of 4.7, not shown). Third, we find that news about future excess returns tends to be, if anything, even more important when adding other variables included in the analyses of Bernanke and Kuttner (2005) and Gertler and Karadi (2015) on which we build. Finally, we find similar results when using as the instrument the three-month ahead Fed Funds futures contract instead of the current contract.

	1-year Treasury yield (<i>pp</i>)	Real stock return (<i>pp</i>)	Share future excess return news (%)
Baseline	-0.22	2.02	58%
Number of lags in VAR			
4	-0.21	1.93	52%
5	-0.22	1.88	54%
7	-0.23	1.94	62%
8	-0.23	1.99	55%
Sample periods			
VAR: 1/91-6/12, IV: 1/91-6/12	-0.14	1.52	36%
VAR: 7/79-6/12, IV: 1/91-9/01	-0.21	3.15	50%
VAR: 7/79-6/12, IV: 10/01-6/12	-0.17	-2.01	38%
Variable added to VAR			
Excess bond premium	-0.21	2.30	79%
Mortgage spread	-0.24	1.62	53%
3-month commercial paper spread	-0.19	2.26	66%
5-year Treasury rate	-0.17	1.64	77%
10-year Treasury rate	-0.17	1.60	75%
Term spread	-0.21	2.04	64%
Relative bill rate	-0.18	2.63	70%
Change in 3-month Treasury rate	-0.19	2.35	65%
3-month ahead FF as IV	-0.20	2.28	65%

Table A.1: robustness of 1 SD monetary shock on returns and components

Notes: series for the Gilchrist and Zakrajsek (2012) excess bond premium, mortgage spread, 3-month commercial paper spread, 5-year Treasury rate, and 10-year Treasury rate are taken from the dataset provided by Gertler and Karadi (2015). The term spread (10-year Treasury rate less 1-month Treasury yield), relative bill rate (difference between the 3-month Treasury rate and its 12-month moving average), and change in the 3-month Treasury rate are constructed using CRSP.

B.1.2 Testing invertibility and comparing SVAR-IV and LP-IV

We now demonstrate that the assumption of invertibility implicit in our SVAR-IV is validated by statistical tests suggested in the literature.

Stock and Watson (2018) propose a Hausman-type test statistic of the null hypothesis that invertibility is satisfied by comparing the impulse response at horizon h for a given variable under the SVAR-IV and LP-IV. We implement the LP-IV by projecting each outcome variable h months ahead on the 1-year Treasury yield, instrumenting for

	1-yr Trea- sury	CPI	Industrial produc- tion	1-mo real rate	1-mo excess return	Dividend/ price
SW [2018] test	0.47	0.63	0.97	0.80	0.68	0.75
Granger test	0.07	0.15	0.88	0.12	0.44	0.93

Table A.2: tests of invertibility assumed in the VAR

Notes: the first row is the bootstrapped p-value for the null hypothesis that the SVAR-IV and LP-IV impulse responses are the same 1, 13, 25, and 37 months after shock, using the test statistic provided in Stock and Watson (2018). We construct the variance matrix needed for this statistic using the 10,000 iterations of the wild bootstrap used to construct confidence intervals for our SVAR-IV estimates in the main text. The second row is the p-value for the null hypothesis that the coefficients on 6 lags of the instrument are jointly equal to zero when added to the VAR.

the latter using the Fed Funds futures surprise also used in our baseline SVAR-IV.² The first row of Table A.2 summarizes the p-value for this test in our setting jointly applied at horizons $h \in \{1, 13, 25, 37\}$ for each variable, demonstrating that we cannot reject the null at standard significance levels.

Stock and Watson (2018) also recommend the use of the complementary Granger causality test in Forni and Gambetti (2014): if invertibility is satisfied, lagged values of the instrument should not have predictive power given the variables included in the VAR. We include 6 lags of our instrument in the VAR and construct an F statistic associated with the null hypothesis that these coefficients are jointly zero for each variable in the VAR. We again cannot reject the null at standard significance levels.

B.1.3 Adding relative wealth responses to the VAR

We finally augment our VAR with two measures of the relative wealth of agents with heterogeneous exposures to capital. The wealth of agents more exposed to the stock market rises on impact of a monetary easing, consistent with the model mechanisms.

We construct the relative wealth measures using monthly data on the returns of hedge funds and mutual funds through which households invest. In each case, we have an unbalanced panel of data on returns r_{ft} and assets A_{ft} for funds indexed by f and months in time indexed by t ; the data sources are described further below. For each fund, we project the time-series of its monthly return on the S&P 500 return relative

²Following Stock and Watson (2018), to make this specification comparable with the SVAR-IV and further improve the precision of estimates, we include 6 lags of each of the variables included in the VAR as controls. Moreover, given the serial correlation of the instrument discussed in Ramey (2016) and Stock and Watson (2018), we include a lag of the instrument as an additional control.

to the 1-month Treasury return. The estimated coefficient is the fund's estimated beta β_f . We sort funds by their beta, compute the median fund beta β_{p50} , and then define the average monthly return (weighted by the prior month's assets) for funds with a beta above or below the median, r_t^{high} and r_t^{low} , respectively. Finally, we define the relative total return index relative to an initial date 0 as

$$relwealth_t = \prod_{s=0}^t (1 + r_s^{high}) - \prod_{s=0}^t (1 + r_s^{low}).$$

This is a measure of the relative wealth of a household which continually reinvests in high beta funds versus a household which continually reinvests in low beta funds. We obtain one such measure for hedge funds and another for mutual funds.

Our source of hedge fund data is the Lipper TASS database from June 1990 through June 2012. Following Getmansky, Lee, and Lo (2015), we focus on funds that provide monthly data; we define the monthly fund return as the ratio of its NAV to its prior month NAV if these measures are available, and as the self-reported return if they are not; we only keep observations for which the monthly fund return is between -100 and 200; and we only keep observations for which the monthly fund return is not equal to the last two observations. In addition, since our construction of total return indices requires an accurate measure of assets at the fund level, we only keep observations with reported estimated assets which are not equal to the previous observation. Finally, to accurately estimate fund betas, we keep only funds with at least 120 observations meeting the criteria described above. We are left with 733 hedge funds in the sample.

Our source of mutual fund data is the CRSP Survivorship-Bias-Free Mutual Fund database from June 1990 through June 2012. We keep only observations with non-missing returns and prior period total net assets. Again, to accurately estimate fund betas, we keep only funds with at least 120 observations meeting the criteria described above. We are left with 13,011 mutual funds in the sample.

Having constructed the relative wealth measures in this way, we add both to our VAR. We estimate the VAR and the IV regressions using the January 1991 - June 2012 period. Figure A.1 displays the estimated responses of both relative wealth measures to a monetary easing which results in a roughly 0.2pp decline in the 1-year Treasury yield; the estimated responses of the other variables in the VAR are similar to the baseline results presented in the main text and are thus excluded for brevity. In both cases a household (continually re-)invested in high beta funds would experience an increase

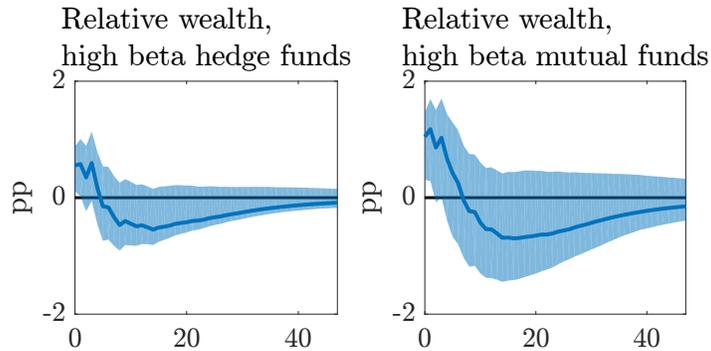


Figure A.1: effects of a 1 SD monetary shock on relative wealth measures

Notes: see notes accompanying Figure 1 in main text.

in relative wealth on impact of a monetary easing, after which its wealth share would decline.³ We emphasize that this result is not mechanical: while the hedge funds and mutual funds are sorted based on their unconditional betas over the sample period, these measures of relative reported returns do not otherwise use any information on market returns, and their conditional response to a monetary easing need not have exhibited the same qualitative pattern as the excess S&P 500 return — but they do.

B.2 Micro moments from the SCF

B.2.1 Construction of household portfolios

We now provide supplemental details on our measurement of household portfolios using the 2016 SCF described in section 3.3. We proceed in five steps.

First, to the SCF data we add an estimate of defined benefit pension wealth for each household, since this is not included in the SCF measure of net worth. We use the estimates of Sabelhaus and Volz (2019).

Second, we proceed by line item to allocate how much household wealth is in directly held claims on capital, indirect claims on capital through business equity, or nominal claims. Direct claims on capital are non-financial assets (vehicles, primary residence, residential real estate excluding the primary residence, non-residential real estate, and other miscellaneous non-financial assets). Indirect claims on capital through business equity come in two forms: publicly traded stocks or privately-owned businesses. We

³The larger response of the relative wealth measure using mutual funds is consistent with the fact that we estimate a larger dispersion in betas in the sample of mutual funds than hedge funds.

assume the following line items reported in the SCF summary extract include stocks:⁴ stock mutual funds, other mutual funds, and directly held stocks, all of which we assume are fully invested in stocks; combination mutual funds, 50% of which we assume are invested in stocks; and savings accounts that may be invested in stocks and are included in transaction accounts (such as 529 or state-sponsored education accounts), other managed assets, and quasi-liquid retirement assets, for which we use the self-reported fraction of these accounts invested in stocks. We assume the remaining portion of these line items not invested in stocks, as well as all other line items not mentioned above, are purely nominal assets or liabilities.

Third, we assume a functional form for households' leverage through these equity claims. We assume that the leverage of publicly traded stocks held by household i is

$$lev_{public}^i = lev_{public} \epsilon^i$$

and the leverage of private businesses owned by household i is

$$lev_{private}^i = lev_{private} \epsilon^i,$$

where the idiosyncratic component ϵ^i is drawn from a $\Gamma(\theta^{-1}, \theta)$ distribution having mean one. lev_{public} thus reflects the aggregate leverage of the household sector in publicly traded stocks; $lev_{private}$ reflects the aggregate leverage of the household sector in private businesses; and θ controls the dispersion of household leverage in these claims. The Γ distribution is right-skewed, which accords well with the heterogeneity in portfolios studied by Calvet, Campbell, and Sodini (2007) and the recent papers on household returns discussed below.

Fourth, we use the FA to discipline lev_{public} and $lev_{private}$. We set lev_{public} to the net leverage of the consolidated nonfinancial corporate sector (FA table S.5.a) and financial business sector (FA table S.6.a), net of the central bank (FA table S.61.a), government DB pension funds (FA tables L.119.b and L.120.b), all defined contribution (DC) pension funds (FA tables L.118.c, L.119.c, and L.120.c), and mutual funds (FA table L.122).⁵ We set $lev_{private}$ to the net leverage of the consolidated nonfinancial

⁴Our approach here follows the construction of the EQUITY variable in the summary extract.

⁵We exclude the central bank and government DB pension funds because we model these as part of the government sector (the latter consistent with our interpretation of DB pensions in footnote 24). We exclude DC pension funds and mutual funds because we view these as pure pass-through entities whose assets have already been folded into that of households using our approach described so far.

noncorporate sector (FA table S.4.a) and non-profit sector (FA table B.101.n). We compute net leverage by dividing the aggregate position in capital by net equity issued to other sectors. Capital is given by total assets net of nominal assets and equity assets. Net equity issued to other sectors is given by equity liabilities plus net worth net of equity assets. Using the Q2 2019 release of the FA, the resulting measures of 2016 leverage we obtain are $lev_{public} = 1.6$ and $lev_{private} = 1.1$.

Using these steps, we decompose the \$104,721bn in total U.S. household net worth ($\sum_i A^i$) into \$11,228bn in nominal claims ($\sum_i B^i$) and \$93,492bn in capital ($\sum_i Qk^i$).⁶

Fifth and finally, we use recent evidence on the heterogeneity in households' expected returns on wealth to discipline θ . Using granular data on the portfolios of the universe of Swedish households, Bach, Calvet, and Sodini (2018) construct household-specific measures of expected excess returns. Over the 2000-2007 period, the cross-sectional standard deviation in expected excess returns on gross assets was 32% of the expected excess returns of the global market.⁷ We choose $\theta = 1.18$ so that the implied cross-sectional standard deviation in leverage on assets in our SCF sample equals 32% of the aggregate leverage in public equities estimated above ($lev_{public} = 1.6$). The fact that a positive value of θ is needed to match the evidence on return heterogeneity is consistent with broader results from the literature that households in fact do not hold identical, diversified equity portfolios.⁸ Nonetheless, even when $\theta \rightarrow 0$, in which case households hold the same, diversified portfolio of equity claims, there is heterogeneity in capital portfolio shares (and thus expected returns) because of households' heterogeneous portfolios across nominal claims, capital, and equity.

B.2.2 Application to the 2007-2009 SCF panel

Using the 2007-2009 SCF panel, we can apply the exact same methodology as described in the prior subsection to characterize households' portfolios and sort them into three groups as of 2007. In this subsection, we follow these households over the next two

⁶We have validated that this aggregate balance sheet is consistent with market clearing in nominal claims after accounting for the balance sheets of the government and rest of the world. We refer the reader to the January 2020 working paper version of this paper for further details on this analysis.

⁷In their Table VI, these authors report a cross-sectional standard deviation in expected excess returns of 1.9%. In their section I.D., they report a long-run (1983-2016) average of the global market excess return of 5.8%. The ratio between these is 32%. We use this evidence from Scandinavia because of the absence of comparable data in the United States with exhaustive coverage of households' wealth.

⁸It is also consistent with the fact that some households invest in equity through levered investment intermediaries such as hedge funds and private equity, which cannot be explicitly identified in the SCF.

		Group (g)		
		a	b	c
1	Share households	4%	35%	61%
2	$\sum_{i \in g} W_{2007} \ell_{2007}^i / \sum_i W_{2007} \ell_{2007}^i$	4%	21%	75%
3	$\sum_{i \in g} A_{2007}^i / \sum_i A_{2007}^i$	16%	64%	21%
4	$\sum_{i \in g} Q_{2007} k_{2007}^i / \sum_{i \in g} A_{2007}^i$	2.0	0.5	1.2
5	$\sum_{i \in g} A_{2009}^i / \sum_i A_{2009}^i - \sum_{i \in g} A_{2007}^i / \sum_i A_{2007}^i$	-1.9%	-0.4%	+2.2%
6	$\sum_{i \in g} Q_{2009} k_{2009}^i / \sum_{i \in g} A_{2009}^i$	1.8	0.5	1.2

Table A.3: heterogeneity and persistence in the 2007-2009 SCF panel

Notes: observations are weighted by SCF sample weights. Construction of capital and bond positions implicit in business equity use $lev_{public,2007} = 1.4$, $lev_{public,2009} = 1.3$, $lev_{private,2007} = 1.1$, and $lev_{private,2009} = 1.2$ obtained using the Financial Accounts for 2007 and 2009. θ is calibrated so that expected return heterogeneity in 2007 is as in Bach et al. (2018), and ϵ^i is assumed the same in 2007 and 2009 for each household.

years using this survey's unique panel structure, demonstrating that the evolution of portfolios is broadly consistent with the mechanisms in our model.

Rows 1-4 of Table A.3 summarize households by group as of 2007. The moments are quite consistent with the 2016 counterparts in Table 2 in the main text.

Row 5 reports the change in the aggregate wealth share of households in each group between 2007 and 2009. The key message is that a households experienced a decline in their wealth share over these two years — consistent with the decline in house prices, the S&P 500, and many other claims on capital over the 2007-2009 period, and the fact that these households were levered in such claims. The redistribution away from a households on impact of a decline in the price of capital is indeed a key mechanism at play in the quantitative model.

Row 6 reports the aggregate capital portfolio share in 2009 by group. The key message is that it is very close to its counterpart in 2007; portfolio heterogeneity across groups is quite persistent. This holds even within each group: at the individual household level, projecting the capital portfolio share in 2009 on a constant and its 2007 value implies a coefficient of 0.95 on the latter.⁹ This is consistent with the permanent differences in risk tolerance across households in the quantitative model.

We note that the redistribution away from a households and the persistence in capital portfolio shares holds even if we exclude all assets and liabilities involving vehicles and housing, thereby focusing on capital held in business equity alone.

⁹As portfolio shares can become very large when net worth is close to zero, we run this regression only on (the more than 97% of) households with a 2007 capital portfolio share between -10 and 10.

C Infinite horizon environment

C.1 Environment

We now outline in more detail the environment studied in section 3.

Households The unit measure of households is now organized into three groups $i \in \{a, b, c\}$ with measures $\{\lambda^i\}$ such that $\sum_i \lambda^i = 1$. Household ι in group $i(\iota)$ is comprised of a continuum of members $j \in [0, 1]$ supplying a differentiated variety of labor, with full consumption insurance within the household. The household has Epstein-Zin preferences

$$v_t^\iota = \left((1 - \beta) \left(c_t^\iota \Phi \left(\int_0^1 \ell_t^\iota(j) dj / \bar{\ell}_t^\iota \right) \right)^{1-1/\psi} + \beta \mathbb{E}_t \left[(v_{t+1}^\iota)^{1-\gamma^{i(\iota)}} \right]^{\frac{1-1/\psi}{1-\gamma^{i(\iota)}}} \right)^{\frac{1}{1-1/\psi}}$$

where $\bar{\ell}_t^\iota$ denotes the household's labor endowment. As we prove in the next subsection, in equilibrium the representative household of each group holds a unitary labor endowment, so that these preferences simplify to (27) as given in the main text. Assuming that the household was alive the previous period, it faces the resource constraint

$$P_t c_t^\iota + B_t^\iota + Q_t k_t^\iota + Q_t^{\bar{\ell}, i(\iota)} \bar{\ell}_t^\iota \leq (1 - \tau) \int_0^1 W_t(j) \ell_t^\iota(j) dj - \int_0^1 AC_t^W(j) dj + (1 + i_{t-1}) B_{t-1}^\iota + (\Pi_t + (1 - \delta) Q_t) k_{t-1}^\iota \exp(\varphi_t) + Q_t^{\bar{\ell}, i(\iota)} \bar{\ell}_{t-1}^\iota + T_t^\iota,$$

where the cost of setting the wage for member j is (29), and $Q_t^{\bar{\ell}, i}$ is the price of the labor endowment for households in group i . It will be convenient to define the household's share of its group's aggregate financial wealth inclusive of labor endowment,

$$\mu_t^\iota = \frac{(1 + i_{t-1}) B_{t-1}^\iota + (\Pi_t + (1 - \delta) Q_t) k_{t-1}^\iota \exp(\varphi_t) + Q_t^{\bar{\ell}, i(\iota)} \bar{\ell}_{t-1}^\iota}{\int_{\iota': i(\iota')=i(\iota)} \left[(1 + i_{t-1}) B_{t-1}^{\iota'} + (\Pi_t + (1 - \delta) Q_t) k_{t-1}^{\iota'} \exp(\varphi_t) + Q_t^{\bar{\ell}, i(\iota')} \bar{\ell}_{t-1}^{\iota'} \right] d\iota'}.$$

Finally, households further face the capital constraint (30). In our calibration, this constraint will (almost always) only bind for c households.

Supply-side A union represents each labor variety j across households. Each period, it chooses $W_t(j), \ell_t(j)$ to maximize the utilitarian social welfare of union members

subject to the allocation rule

$$\ell_t^i(j) = \mu_t^i \phi^{i(i)} \ell_t(j).$$

That is, within group i , labor is allocated across households in proportion to their wealth. The labor packer combines varieties supplied by the union, earning profits each period (33) given (32). The representative producer hires ℓ_t units of the labor aggregator in period t and combines it with $k_{t-1} \exp(\varphi_t)$ units of capital rented from households. It further uses $\left(\frac{k_t}{k_{t-1} \exp(\varphi_t)}\right)^{\chi^x} x_t$ units of the consumption good to produce x_t new capital goods, where it again takes k_t as given. Taken together, it earns profits

$$\begin{aligned} \Pi_t k_{t-1} \exp(\varphi_t) = \\ P_t (z_t \ell_t)^{1-\alpha} (k_{t-1} \exp(\varphi_t))^\alpha - W_t \ell_t + Q_t x_t - P_t \left(\frac{k_t}{k_{t-1} \exp(\varphi_t)}\right)^{\chi^x} x_t. \end{aligned}$$

Productivity follows (34).

Policy The government follows a standard Taylor rule (37) where monetary policy shocks m_t follow (38). The government sets $\tau = -\frac{1}{\epsilon-1}$ and sets the transfers T_t^i to households alive the previous period

$$T_t^i = \int_0^1 AC_t^W(j) dj + \tau \int_0^1 W_t(j) \ell_t^i(j) dj + \mu_t^i \nu^{i(i)} ((1 + i_{t-1}) B_{t-1}^g - B_t^g).$$

Within group i , the government rebates the proceeds from its trade in the bond market to households in proportion to their wealth.¹⁰ As described in the main text, the government further collects the wealth of dying households and endows it to newborns.

Market clearing Market clearing in goods each period is now

$$\int_l c_t^i + \left(\frac{k_t}{k_{t-1} \exp(\varphi_t)}\right)^{\chi^x} x_t = (z_t \ell_t)^{1-\alpha} (k_{t-1} \exp(\varphi_t))^\alpha,$$

in labor is

$$\left[\int_0^1 \ell_t(j)^{(\epsilon-1)/\epsilon} dj \right]^{\epsilon/(\epsilon-1)} = \ell_t,$$

¹⁰We assume, however, that households do not internalize the dependence of their rebate on their wealth in their decisions, preserving the neutrality of government participation in the bond market.

in the capital rental market is

$$\int_{\iota} k_{t-1}^{\iota} = k_{t-1},$$

in the capital claims market is

$$(1 - \delta) \int_{\iota} k_{t-1}^{\iota} \exp(\varphi_t) + x_t = \int_{\iota} k_t^{\iota},$$

in bonds is

$$\int_{\iota} B_t^{\iota} + B_t^g = 0,$$

and in the labor endowment is

$$\int_{\iota: i(\iota)=a} \bar{\ell}_t^{\iota} = 1, \quad \int_{\iota: i(\iota)=b} \bar{\ell}_t^{\iota} = 1, \quad \int_{\iota: i(\iota)=c} \bar{\ell}_t^{\iota} = 1.$$

Equilibrium Given initial state variables $\{W_{-1}, \{B_{-1}^{\iota}, k_{-1}^{\iota}\}, i_{-1}, z_0, p_0, m_0\}$ and the stochastic processes (34)-(38), the equilibrium naturally generalizes Definition 1. Since labor varieties and unions j are symmetric, $\ell_t(j) = \ell_t$ and going forward we drop j .

C.2 Aggregation into representative households

Within each group of households $i \in \{a, b, c\}$, we can then prove the homogeneity of households' policies in wealth, implying a representative household of each group.

Proposition C.1. *Households' optimal policies satisfy*

$$v_t^{\iota} = \mu_t^{\iota} v_t^{i(\iota)}, \quad c_t^{\iota} = \mu_t^{\iota} c_t^{i(\iota)}, \quad B_t^{\iota} = \mu_t^{\iota} B_t^{i(\iota)}, \quad k_t^{\iota} = \mu_t^{\iota} k_t^{i(\iota)}, \quad \bar{\ell}_t^{\iota} = \mu_t^{\iota},$$

where the variables with an $i \in \{a, b, c\}$ superscript correspond to those of a representative household endowed with aggregate group-specific wealth. Furthermore, the evolution of wealth shares is identical across households in a given group, conditional on surviving through the next period:

$$\frac{\mu_{t+1}^{\iota}}{\mu_t^{\iota}} = \mu_{t,t+1}^{i(\iota)}. \tag{A.18}$$

This result follows from households' ability to trade labor endowments with other households in the same group, the assumed labor allocation rule, the assumed lump-sum transfers, and the assumed endowments. We exclude the proof for brevity.

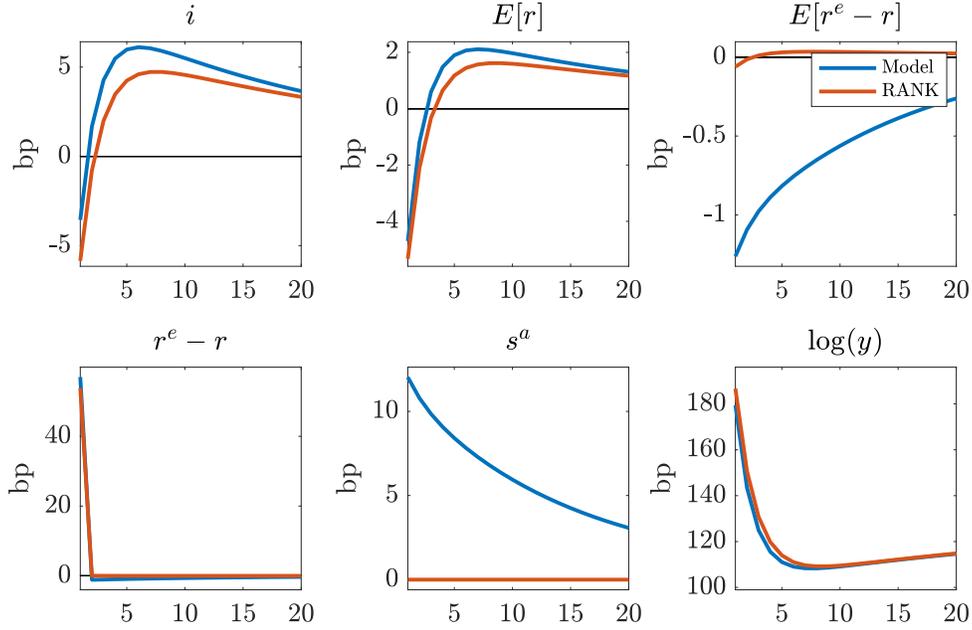


Figure A.2: responses to positive productivity shock

Notes: see notes accompanying Figure 2 in main text.

C.3 Re-scaled economy

The results of the prior subsection allow us to summarize the equilibrium in terms of the first-order conditions of the three representative households $i \in \{a, b, c\}$, their resource constraints, and the market clearing conditions. Scaling by the price level P_t and permanent level of productivity z_t , we obtain a stationary transformation of the economy which we can numerically solve over the state variables

$$\left\{ \frac{k_{t-1}}{z_{t-1} \exp(\epsilon_t^z)}, \frac{W_{t-1}}{P_t z_{t-1} \exp(\epsilon_t^z)}, s_t^a, s_t^b, p_t, m_t \right\},$$

where s_t^i denotes the financial wealth share of group i .

D Additional quantitative results

D.1 Impulse responses to other shocks

We now characterize the impulse responses to other shocks in section 3.

In Figure A.2, we summarize the effects of a two standard deviation increase in

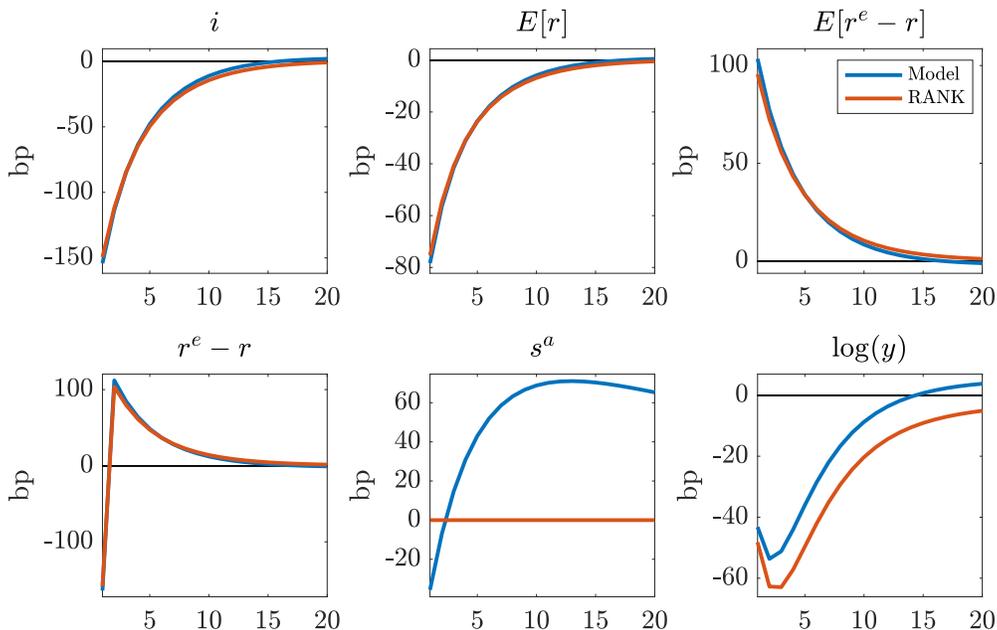


Figure A.3: responses to positive disaster probability shock

Notes: see notes accompanying Figure 2 in main text.

productivity in both the model and counterfactual RANK economies. In the first row, the first panel demonstrates that the central bank following a standard Taylor rule will cut the nominal interest rate (in response to the price deflation induced by this shock). The second and third panels demonstrate that the expected real interest rate and the expected excess returns on capital decline following the shock, the former being a standard real business cycle response. The first two panels of the second row demonstrate that redistribution drives the decline in the risk premium in our model: as in the case of a negative monetary policy shock, realized excess returns on capital are substantially positive on impact, and this raises the wealth share of high MPR a households who hold levered claims on capital. The third panel in this row demonstrates that output rises, as expected. The difference between the output responses in the model and RANK is minimal, arising from the endogenous tightening of monetary policy in the model in response to the stimulus from lower risk premia.

In Figure A.3, we summarize the effects of a two standard deviation increase in disaster risk in both the model and RANK economies. In the first row, the first panel demonstrates that the central bank following a standard Taylor rule will cut the nominal interest rate (again in response to the price deflation induced by this shock,

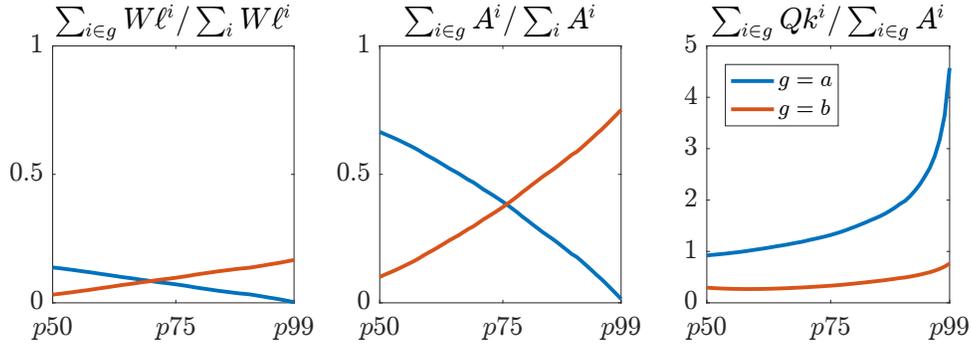


Figure A.4: alternative cutoff in the capital portfolio share

Notes: observations are weighted by SCF sample weights. Targets in the baseline calibration use a 90th percentile cutoff in the capital portfolio share.

reflecting the increase in precautionary saving associated with the increase in disaster probability). The second panel demonstrates that the expected real interest rate declines following the shock. The third panel demonstrates that expected excess returns rise following the shock, reflecting both the persistent increase in the quantity of risk and transitory redistribution of wealth away from the relatively risk tolerant. The latter is absent in the RANK economy. The first two panels in the second row rationalize the dynamics of the wealth distribution in the model with heterogeneity: realized excess returns on capital are negative on impact and positive in the quarters which follow, so a households lose in relative wealth on impact but then recoup these losses. The final panel demonstrates that output falls on impact of the increase in uncertainty — despite the fact that the households’ intertemporal elasticity of substitution is less than one. This is consistent with the effects of uncertainty shocks in New Keynesian environments studied in the literature. It is for this reason that the model-implied equity premium is countercyclical.

D.2 Alternative calibration of wealth and leverage

We now present the results in an alternative calibration in which a households hold a smaller fraction of the economy’s wealth but are more levered. Because these forces have offsetting effects in determining the effects of redistribution on risk premia, the effects of a monetary policy shock are comparable to our baseline results.

Formally, we change the cutoff in the capital portfolio share between group a and b agents. Figure A.4 summarizes the fraction of labor income, fraction of wealth, and

	Description	Value	Moment	Target	Model
σ^z	std. dev. prod.	0.7%	$\sigma(\Delta \log c)$	0.5%	0.6%
χ^x	capital adj cost	3.5	$\sigma(\Delta \log x)$	2.1%	2.2%
β	discount factor	0.988	$4\mathbb{E}r_{+1}$	1.4%	1.2%
γ^b	RRA b	21	$4\mathbb{E}[r_{+1}^e - r_{+1}]$	7.1%	7.4%
σ^p	variation log dis. prob.	0.47	$\sigma(4\mathbb{E}r_{+1})$	2.3%	2.1%
ρ^p	persist. log dis. prob.	0.80	$\rho(4\mathbb{E}r_{+1})$	0.80	0.75
γ^a	RRA a	2.5	k^a/a^a	4.6	4.7
\underline{k}	lower bound k^i	0.4 k	k^c/a^c	1.1	1.0
\bar{s}^a	newborn endowment a	0%	$\lambda^a a^a / \sum_i \lambda^i a^i$	2%	2%
\bar{s}^c	newborn endowment c	40%	$\lambda^c a^c / \sum_i \lambda^i c^i$	23%	25%
b^g	real value govt bonds	-3.1	$-\sum_i \lambda^i b^i / \sum_i \lambda^i a^i$	-11%	-11%

Table A.4: targeted moments and calibrated parameters, alternative calibration

Notes: see notes accompanying Table 5 in main text. The disutilities of labor $\{\bar{\theta}^a, \bar{\theta}^b, \bar{\theta}^c\}$ are jointly set to $\{0.00, 2.61, 0.44\}$ so that the average labor wedge is zero for each group and $\ell = 1$.

ratio of aggregate capital to wealth for groups a and b as we vary the cutoff (the moments for c households are unaffected). As is evident, a higher cutoff means that group a households are more levered, but conversely have a lower share of total wealth. Our baseline calibration employed a cutoff at the 90th percentile.

In this subsection we instead employ a cutoff at the 99th percentile. The targeted moments are the right-most points in Figure A.4: a agents are now less than 1% of agents, earn even less labor income than that, own 2% of wealth, and have a capital portfolio share of 4.6; b agents are over 39% of agents, earn 17% of labor income, own 75% of wealth, and have a capital portfolio share of 0.8. These targets mean that we can interpret our a agents as capturing highly levered sectors such as security broker-dealers and hedge funds, which issue nominal claims to households (the asset-rich b and asset-poor c) to hold capital. Indeed, the estimates in He and Krishnamurthy (2013) imply that these sectors own 3% of U.S. wealth and have leverage of 4.5, comparable to the 2% wealth share and capital portfolio share of 4.6 obtained here.

Given these new targets, we adjust our calibration as follows. We maintain the same externally set parameters as in Table 4 except that we set $\lambda^a = 1\%$; $\phi^a = 0$ (so a agents do not supply any labor, consistent with their interpretation as levered institutions); $\lambda^b = 39\%$; $\phi^b = 17\%/\lambda^b$; $\nu^a = 2\%/\lambda^a$; $\nu^b = 75\%/\lambda^b$. We further set the

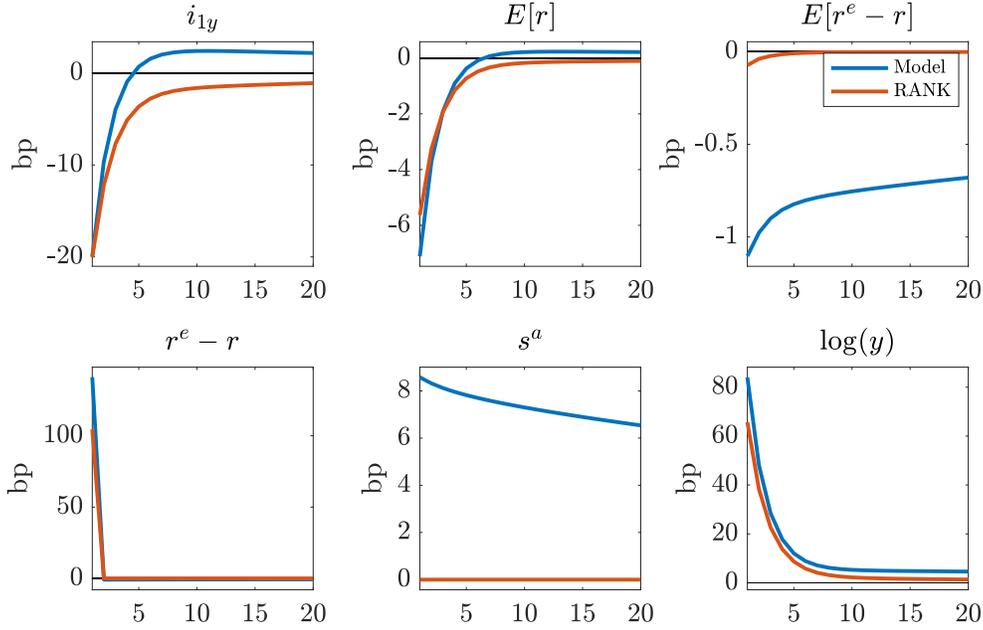


Figure A.5: responses to negative monetary policy shock, alternative calibration

Notes: see notes accompanying Figure 2 in main text.

% Real stock return	Data [90% CI]	Model	RANK
Dividend growth news	34% [-11%,71%]	47%	66%
–Future real rate news	7% [-6%,21%]	11%	35%
–Future excess return news	58% [21%,106%]	42%	-0%

Table A.5: decomposition after monetary shock, alternative calibration

Notes: see notes accompanying Table A.5 in main text.

death probability to $\xi = 0.045$, which is higher than the baseline death probability so that we are able to target the low wealth share of a agents in this calibration. We maintain the same calibration targets as in Table 5 except that we target the lower wealth share and higher capital portfolio share of a agents. The results are reported in Table A.4. We calibrate a agents to be more risk tolerant than in the baseline.

Figure A.5 compares the effects of a monetary policy shock in this environment to a counterfactual RANK economy in which $\gamma^i = 18$ for all groups. Table A.5 presents the Campbell-Shiller decomposition of the stock market return following the shock. As is evident, it remains the case that a substantial share of the stock market return is due to news about future excess returns. And again, the impact effect on output is

	Description	Value	Moment	Target	Model
σ^z	std. dev. prod.	0.6%	$\sigma(\Delta \log c)$	0.5%	0.6%
χ^x	capital adj cost	3.5	$\sigma(\Delta \log x)$	2.1%	2.2%
β	discount factor	0.993	$4\mathbb{E}r_{+1}$	1.4%	1.5%
$\gamma^a = \gamma^b = \gamma^c$	RRA	12	$4\mathbb{E}[r_{+1}^e - r_{+1}]$	7.1%	6.6%
σ^p	variation log dis. prob.	0.83	$\sigma(4\mathbb{E}r_{+1})$	2.3%	2.1%
ρ^p	persist. log dis. prob.	0.80	$\rho(4\mathbb{E}r_{+1})$	0.80	0.75
η^b	idio. risk b	0.005	k^a/a^a	2.0	2.0
\underline{k}	lower bound k^i	0.4 k	k^c/a^c	1.1	1.1
\bar{s}^a	newborn endowment a	0%	$\lambda^a a^a / \sum_i \lambda^i a^i$	18%	21%
\bar{s}^c	newborn endowment c	40%	$\lambda^c a^c / \sum_i \lambda^i c^i$	23%	24%
b^g	real value govt bonds	-3.1	$-\sum_i \lambda^i b^i / \sum_i \lambda^i a^i$	-11%	-11%

Table A.6: targeted moments and calibrated parameters, idiosyncratic risk

Notes: see notes accompanying Table 5 in main text. The disutilities of labor $\{\bar{\theta}^a, \bar{\theta}^b, \bar{\theta}^c\}$ are jointly set to $\{0.90, 3.83, 0.45\}$ so that the average labor wedge is zero for each group and $\ell = 1$.

roughly 1.3 times larger than in the RANK economy.

D.3 Alternative microfoundation of portfolio heterogeneity

We now present the results in an alternative environment which microfounds differences in portfolios and MPRs without appealing to differences in risk aversion. Instead, we assume households experience idiosyncratic returns on capital, and the volatility of these returns differs across groups, consistent with one of the alternative forms of heterogeneity considered in section 2.5. We demonstrate that our quantitative results are again robust to this setting.

Formally, we assume that households' choice of capital k_t^i in period t is subject to an idiosyncratic quality shock at $t+1$, turning into $\epsilon_{t+1}^i k_t^i$ units of capital which can be rented in the spot market to firms. The quality shock is an *iid* shock from a lognormal distribution, the variance of which is the group-specific parameter η^i :

$$\log \epsilon_{t+1}^i \sim N\left(-\frac{1}{2}\eta^i, \eta^i\right).$$

In equilibrium, this only affects households' portfolio choice; since the quality shock

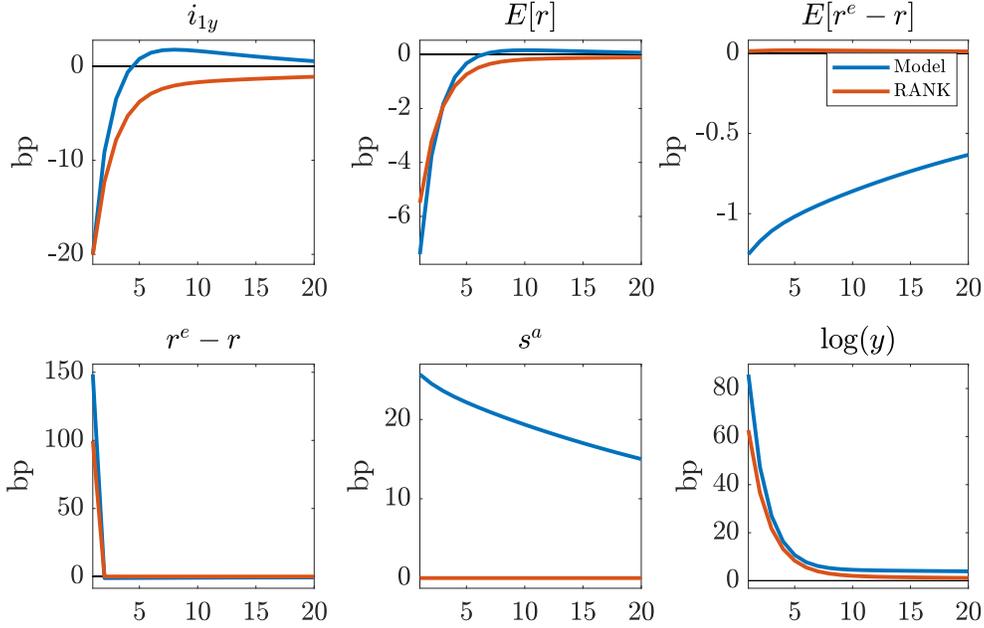


Figure A.6: responses to negative monetary policy shock, idiosyncratic risk

Notes: see notes accompanying Figure 2 in main text.

% Real stock return	Data [90% CI]	Model	RANK
Dividend growth news	34% [-11%,71%]	46%	66%
–Future real rate news	7% [-6%,21%]	20%	35%
–Future excess return news	58% [21%,106%]	34%	-1%

Table A.7: decomposition after monetary shock, idiosyncratic risk

Notes: see notes accompanying Table A.5 in main text.

has a mean value of one, the representative household still rents k_t^i units of capital and none of the supply-side conditions or aggregate resource constraints are affected.

To rationalize their high leverage, a households are now calibrated to be those with the smallest volatility of idiosyncratic returns; equivalently, they have the highest risk-adjusted returns. Formally, we maintain the same externally set parameters as in Table 4 and set $\eta^a = 0$. We then re-calibrate the parameters in Table A.6 assuming that households share the same level of risk aversion γ calibrated to match the level of the equity premium, and calibrating η^b and \underline{k} to match households' capital portfolio shares. Taken together, this environment builds on a large literature on entrepreneurship in macroeconomic models emphasizing idiosyncratic risk and entrepreneurs as those with

relatively good investment ideas.

Figure A.6 compares the effects of a monetary policy shock in this environment to a counterfactual RANK economy in which η^i is identical across groups. Table A.7 presents the Campbell-Shiller decomposition of the stock market return following the shock. It remains the case that a substantial share of the stock market return is due to news about future excess returns. And again, the impact effect on output is roughly 1.4 times larger than in the RANK economy.

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