

Specific Factors Model

For questions 1-4 regarding the Specific Factors models assume there are two countries (Home and Foreign), two goods (Manufacturing and Agriculture) and three factors of production (capital, land and labor) with capital and land being specific to Manufacturing and Agriculture respectively.

1. In the specific factors model if both countries have identical endowments of all three factors as well as identical preferences can trade be mutually beneficial?
2. In the specific factors model if the price of Agriculture increases as a result of trade, it is possible for labor to gain more than the owners of land?
3. In the specific factors model with **fixed world prices** if the endowment of labor increases what will happen to the real return to labor? What about the real returns to capital and land?
4. In the specific factors model with **fixed world prices** if the endowment of either specific factor decreases what will happen to the real returns to both specific factors?

Heckscher-Ohlin Model

For this question regarding the Heckscher-Ohlin model assume the following: there are two countries, Home and Foreign, abundant in capital and labor respectively. There are two goods (airplanes and bicycles) that are produced by two factors of production. Further, assume airplane production is capital intensive and bicycle production is labor intensive. Assume both countries have identical preferences and in autarky both countries produce both goods.

- a. If these two countries were to trade which country would export which good?
- b. State the theorem that pertains to the result in (a).
- c. What will happen to the capital intensity of production in Home?
- d. What will happen to the capital intensity of production in Foreign?
- e. What will happen to the real wage in Home and in Foreign?
- f. What will happen to the real rental rate in Home and Foreign?

g. State the theorem that pertains to the results in (e) and (f).

True, False or Uncertain:

h. With **fixed world prices**, if immigration increases the labor force in the Home country, the Home country will *decrease* its production of airplanes.