

**The University of Illinois at Chicago**  
**Economics 514: International Trade and Policy**

Midterm Examination

Name: \_\_\_\_\_

February 25, 1999

There are 70 total points. GOOD LUCK!

Answer true, false, or uncertain and explain your answer. These questions are worth 5 points each.

1. Capital flows from the United States to Mexico will lower the wage rate in the United States and increase it in Mexico.
2. Israel experienced a huge increase in its supply of labor in the 1990s, especially from the former Soviet Union territories. The result for production in Israel is an increase (or no change) in the output of every sector of the economy.
3. Last September, Malaysia imposed capital and currency controls which fixed capital within the country. In Wong's terminology, Malaysia was counting on capital and goods trade being substitutes. What are the necessary conditions for this to be true? Is this reasonable?
4. A lawyer is a better typist than his (or her) secretary. Who should do the typing? Why?
5. What is Leontief's paradox? Which explanation do you find most plausible?
6. State and demonstrate graphically the factor price equalization theorem in the 2-goods and 2-factors and 2-countries case.

These questions are each worth 20 points.

7. In the 2-goods, 2-factors model, suppose there are 2 technologies available for producing each good. The advanced technology uses 20% less capital and labor than the backward technology. Suppose that the former West Germany (WG) uses the advanced technology and the former East Germany (EG) uses the backward technology.
  - a. How do wages and rental rates compare in WG and EG after reunification, if labor and capital must remain in their original region?
  - b. If capital, but not labor or technology, becomes mobile between WG and EG, what happens to the product mix and factor returns? Use a graph in your answer.
  - c. If WG's minimum wage laws are extended to EG, what happens to the product mix and to factor returns? Use a graph in your answer.

8. The impact of international trade on advanced-country wages can be estimated by checking what prices, and therefore wages, would have been if there were no imports. Assume that trade in manufactures is produced with 2 factors, skilled and unskilled labor.
  - a. Construct a model (use a graph) showing advanced countries' trade and production. Advanced countries (OECD) have a comparative advantage in skill-intensive good X. Identify the autarky price, world price, exports, imports, and trade triangle.
  - b. Analyze the effect of trade on advanced-countries wages for unskilled workers.
9. What information do you need to compute this model?