Sample Problem: Chapter 4

Suppose two countries, France and Germany, use only capital and labor for production.

* France has 2,050 units of capital and 916 units of labor.
* Germany has 816 units of capital and 270 units of labor.
* Both countries produce two goods, cars and wine.
* In Germany, there are 366 units of capital and 135 units of labor employed in the wine industry.
* In France, there are 926 units of capital and 618 units of labor employed in the wine industry.

1. Which country is labor-abundant? Which country is capital-abundant?
2. Which industry is labor-intensive in Germany? Which industry is capital-intensive in Germany?
3. Suppose that France and Germany do not engage in international trade. Assuming the countries have identical preferences, which country would have the cheaper relative price of wine?
4. Now, suppose the two countries trade with one another. What will happen to the relative price of wine in France? In Germany?
5. What is the effect of free trade on labor in France? On capital owners in France?
6. What are the effects of free trade on wage and rental on capital in Germany?
7. With the opening of trade, what is most likely to occur in terms of the production of cars in France? In Germany?