

Problem Set 02

Instructions: Answers must be submitted online through the designated Canvas assignment. This Problem Set is due on **October 21 at 01:59pm**. Please write as legible and clearly as possible. You will not be given full credit if your answers cannot be easily understood.

Questions

1. [8 points] Answer the following short questions
 - (a) [2 points] In your own words, how would you define **Labor Abundance** in the Heckscher-Ohlin model setting?
 - (b) [2 points] How does the capital-labor ratio help us determine patterns of trade?
 - (c) [2 points] Describe the key difference(s) that separate the HO model from the Ricardian model
 - (d) [2 points] Describe the **Gravity Model**. What does this model ignore?

2. [6 points] Suppose we are considering an **HO Model setting**, where countries have not yet opened up to trade. Two goods are produced: **Suits and Ozempic**. Suppose that tailoring **Suits** is **labor-intensive** in production as it is primarily done by hand and making **Ozempic** is **capital-intensive** in production as it requires exact and automated machinery. The countries, Country A and Country B, have the following **Labor (L) and Capital (K)** endowments.

Factor	L	K
Country A	1120	575
Country B	1680	950

- (a) [2 points] What are the **Capital-Labor Ratios** for each country?
- (b) [2 points] Which country has comparative advantage in producing Ozempic?
- (c) [2 points] How will trade flows look once each country specializes?

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3. [6 points] How do trade outcomes play out for owners of factor inputs when trade opens? Address both capital and labor outcome when a country is abundant in either capital or labor.
4. [4 points] Consider the **Specific-Factor Model**. What are the implications for domestic labor income of switching from autarky to open trade, when a given country is **land-abundant**? Is this impact different if the country is **capital-abundant** instead?

