Does Reality Support Theory?

Predictions of Simple Model

(Heckscher-Ohlin hypothesis)

1. Countries will export goods in which they have a comparative advantage and import those in which they do not.
2. Free trade leads to specialization of production according to comparative advantage
3. Maximized Consumer Welfare (lower product prices)
Does Trade Lower Consumer Prices?

• Next 2 slides show consumer prices
• Look at Balance of Trade Spreadsheet for trade information.

CPI, by Category
1990-2004
Simple Model Predictions for Job Growth and Nature of Trade under NAFTA

- Increased demand in Mexico for US goods => increase in US employment.
- Specialization would occur:
  - High value-added jobs would be retained in US because of human capital advantage relative to Mexico
  - Lower-skilled jobs would go to Mexico with its comparative advantage of abundant cheap labor
- Is that what has happened?
US Trade Deficits with Mexico and Canada

US Trade Deficits with Canada & Mexico, 1989-2003

Mexico
Canada

Job Loss by State

NAFTA costs jobs in every state

Compensation: May Explain Job Loss to Canada but not Mexico

![Relative Compensation, 1975-2002: U.S. = 100](chart)


Industries where US has greatest trade advantage with Mexico

- 39--PLASTICS AND ARTICLES THEREOF
- 29--ORGANIC CHEMICALS
- 10--CEREALS
- 48--PAPER & PAPERBOARD & ARTICLES (INC PAPR PULP ARTL)
- 02--MEAT AND EDIBLE MEAT OFFAL
- 12--OIL SEEDS ETC.; MISC GRAIN, SEED, FRUIT, PLANT ETC
- 52--COTTON, INCLUDING YARN AND WOVEN FABRIC THEREOF
- 76--ALUMINUM AND ARTICLES THEREOF
- 38--MISCELLANEOUS CHEMICAL PRODUCTS
- 88--AIRCRAFT, SPACECRAFT, AND PARTS THEREOF
- 59--IMPREGNATED ETC TEXT FABRICS; TEX ART FOR INDUSTRY
- 47--WOOD PULP ETC; RECOVD (WASTE & SCRAP) PPR & PPRBD
- 40--RUBBER AND ARTICLES THEREOF
- 32--TANNING & DYE EXT ETC; DYE, PAINT, PUTTY ETC; INKS
- 23--FOOD INDUSTRY RESIDUES & WASTE; PREP ANIMAL FEED
- 37--PHOTOGRAPHIC OR CINEMATOGRAPHIC GOODS
- 11--MILLING PRODUCTS; MALT; STARCH; INULIN; WHT GLUTEN
- 15--ANIMAL OR VEGETABLE FATS, OILS ETC. & WAXES
- 21--MISCELLANEOUS EDIBLE PREPARATIONS
- 60--KNITTED OR CROCHETED FABRICS
- 41--RAW HIDES AND SKINS (NO FURSKINS) AND LEATHER
Industries where Mexico has the greatest trade advantage with the US

83—MISCELLANEOUS ARTICLES OF BASE METAL
71—NAT ETC PEARLS, PREC ETC STONES, PR MET ETC; COIN
70—GLASS AND GLASSWARE
03—FISH, CRUSTACEANS & AQUATIC INVERTEBRATES
69—CERAMIC PRODUCTS
95—TOYS, GAMES & SPORT EQUIPMENT; PARTS & ACCESSORIES
01—LIVE ANIMALS
63—TEXTILE ART NESOI; NEEDLECRAFT SETS; WORN TEXT ART
08—EDIBLE FRUIT & NUTS; CITRUS FRUIT OR MELON PEEL
96—SPECIAL CLASSIFICATION PROVISIONS, NESOI
84—NUCLEAR REACTORS, BOILERS, MACHINERY ETC.; PARTS
22—BEVERAGES, SPIRITS AND VINEGAR
99—SPECIAL IMPORT PROVISIONS, NESOI
61—APPAREL ARTICLES AND ACCESSORIES, KNIT OR CROCHET
07—EDIBLE VEGETABLES & CERTAIN ROOTS & TUBERS
90—OPTIC, PHOTO ETC, MEDIC OR SURGICAL INSTRMNTE ETC
62—APPAREL ARTICLES AND ACCESSORIES, NOT KNIT ETC.
94—FURNITURE; BEDDING ETC; LAMPS NESOI ETC; PREFAB BD
85—ELECTRIC MACHINERY ETC; SOUND EQUIP; TV EQUIP; PTS
27—MINERAL FUEL, OIL ETC.; BITUMIN SUBST; MINERAL WAX
87—VEHICLES, EXCEPT RAILWAY OR TRAMWAY, AND PARTS ETC
Engineers & Computer Scientists: Share of Industry Workforce

Percent of Technical Professionals by Industry

0 2 4 6 8 10 12 14
Electronic Machinery Textiles Apparel Instruments and Related Products Plastics Machinery Chemicals Grains & Cereals Aircraft & Parts Aircraft & Related Products

Industries where Mexico has a trade advantage

Occupational Distribution - Electronics
- Management, business, & financial
- Professional & related
- Production workers

Occupational Distribution - Furniture
- Management, business, & financial
- Professional & related
- Production workers

Occupational Distribution - Apparel
- Management, business, & financial
- Professional & related
- Production workers

Occupational Distribution - Instruments & Related Products
- Management, business, & financial
- Professional & related
- Production workers