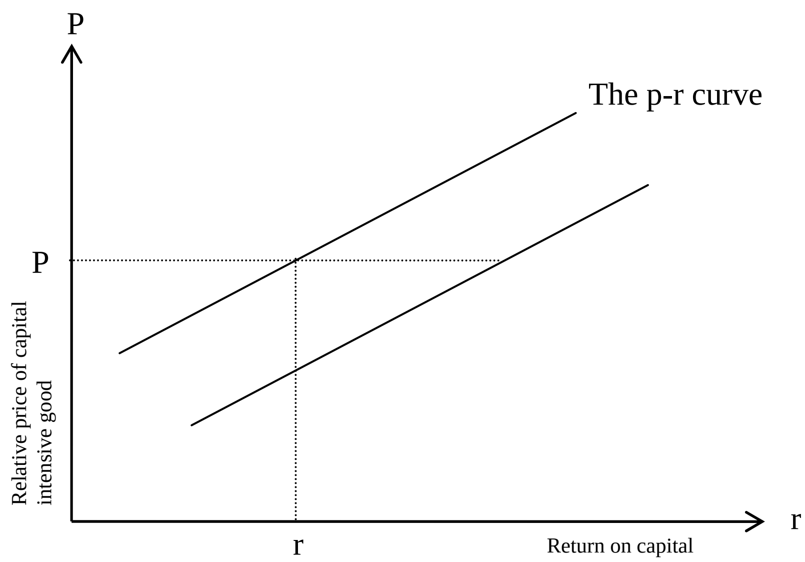
APPENDIX B

THE KEMP-JONES MODEL

Figure 1.B

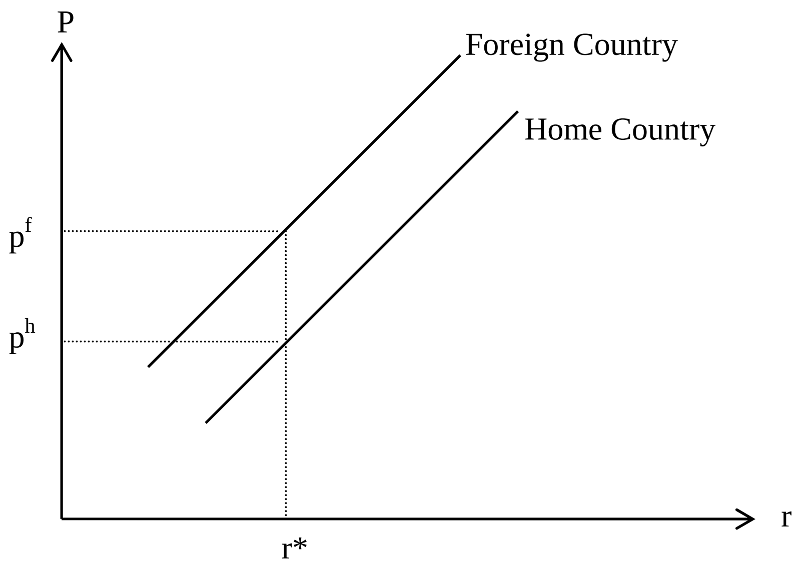
The p-r Curve and Technical Progress



The p-r curve represents the relationship between commodity prices and factor prices reflecting the technology of a country when both goods are produced and endowment is irrelevant (Ruffin, 1984). In Figure1, the upward sloping p-r curve will shift to the right, for instance if there is technical progress in the capital intensive good sector.

Figure 2.B

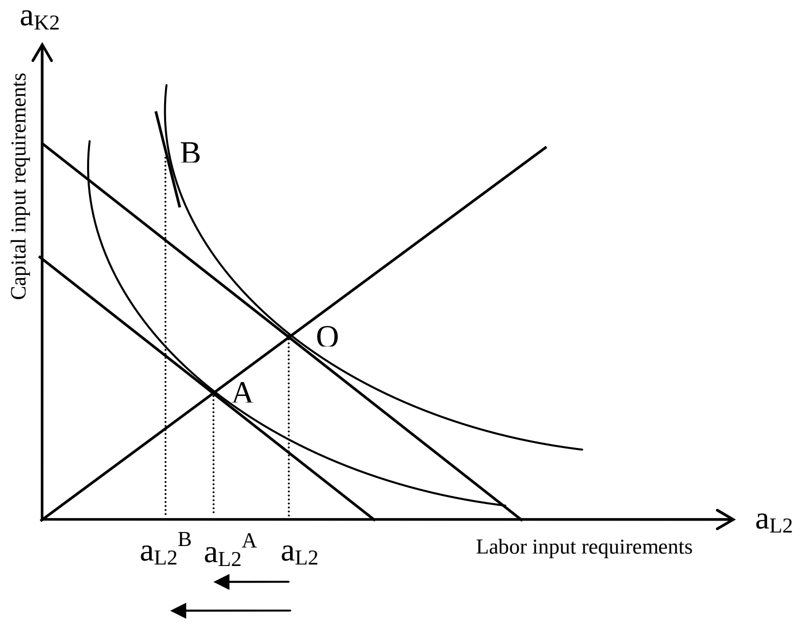
Two-Country Case with Perfect Capital Mobility



If two countries, home and foreign, fact the same rental rate (r^*), then the comparative advantage in the production of the capital-intensive good is in home country whose the p-r curve lies below that of foreign country.

Figure 3.B

The Unit Labor Cost of the Capital-Intensive Goods Sector



- The unit labor cost at initial point 0 is $a_{L2}w$.
- The unit labor cost at A (with technical progress) is $a_{L2}^{A}w$.
- The unit labor cost at B (with possible labor market distortions) is $a_{L2}^{B}w$.

The reduction in unit labor cost could be identical in case A and B. In such a case, we cannot distinguish if an improvement in comparative advantage is a result of A or B, by simply looking at the unit labor costs. The comparative Advantage Index (CAI) decomposition of this paper allows us to distinguish the two.