

Variety Trade and Skill Premium in a Calibrated General Equilibrium Model: The Case of Mexico*

Manoj Atolia
Florida State University[†]

Yoshinori Kurokawa
State University of New York at Buffalo[‡]

October 29, 2008

Abstract

It can be theoretically shown that variety trade can be a possible source of increased skill premium in wages. No past studies, however, have empirically quantified how much of the increase in skill premium can be accounted for by the increase in variety trade. This paper now formulates a static general equilibrium model and then calibrates it to the Mexican input-output matrix for 1987. In the calibrated model, our numerical experiments show that the increase in U.S.-Mexican variety trade can explain approximately 12 percent of the actual increase in skill premium in Mexico from 1987 to 2000.

Keywords: Variety Trade, Skill Premium, Variety-Skill Complementarity, Calibrated General Equilibrium Model, Mexico

JEL Classifications: F12, F16

*We are very grateful to Timothy Kehoe for his invaluable guidance and to Cristina Arellano, Michele Boldrin, and Terry Roe for their helpful advice. We are also grateful to Winston Chang, Koichi Hamada, Katsuhito Iwai, Michihiro Ohyama, and Yoshimasa Shirai for their suggestions and encouragement. We wish to thank Pedro Amaral, Paul Klein, and Esteban Rossi-Hansberg for their useful comments. We also thank Kim Strain for her careful correction of our English. However, the remaining errors are exclusively ours.

[†]Department of Economics, Florida State University, Tallahassee, FL 32306, USA. Tel.: 1-850-644-7088. Email: matolia@fsu.edu.

[‡]Department of Economics, SUNY at Buffalo, NY 14260, USA. Tel.: 1-716-645-2121x447. Email: ykurok@buffalo.edu.