

Trade and labor market interactions revisited

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Abstract. We examine how globalization affects wages, unemployment, and welfare under an imperfect labor market. Using a firm-heterogeneity model with a fair wage-effort mechanism, we reveal that the effect of trade liberalization on wages and welfare changes according to the level of price elasticity and the fairness parameter. This implies that the accepted wisdom of the existing literature on trade and labor markets (i.e., globalization raises wages) doesn't hold true universally. We also reveal that the effect of trade liberalization on unemployment depends on the degree of globalization, which is measured by the level of trade cost.

Keywords: fair wage; firm heterogeneity; price elasticity; trade; unemployment; welfare

JEL classifications: F12; F15; F16

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