

Basic Economic Concepts
Comparative Advantage and Trade

Terms

Absolute advantage
comparative advantage
specialization
gains from trade

Read Chapter 2 Why Do We Trade? from the Everything Economics Book

1. Explain why Adam Smith believed free trade led to greater wealth.
2. What is absolute advantage?
3. Define comparative advantage.

Use the information about Art and Paul to complete the chart below showing how many songs can be written and how many surgeries can be performed. Assume that each has one hour to complete their work.

	Songs written	Brain surgeries performed
Art	opportunity cost 1 song =	opportunity cost 1 surgery =
Paul	opportunity cost 1 song =	opportunity cost 1 surgery =

4. Who has the comparative advantage in songwriting?
5. Who has the comparative advantage in brain surgery?
6. Explain why Bangladesh has a comparative advantage in producing T-shirts.

Reading pages 23- 29 – you do not have to answer any questions but read these pages anyway!

Watch Comparative Advantage Practice at <https://www.youtube.com/watch?v=HneRNVtahYw>

Follow Mr. Clifford examples and answer his first set of questions. Which country has an ABSOLUTE ADVANTAGE in producing each product?

- 1.
- 2.
- 3.
- 4.

The US can produce 20 planes or 2 cruise ships AND France can produce 12 planes or 2 cruise ships

	Planes	Cruise Ships
US		
France		

Use the chart above to help you answer the following questions:

- What is the opportunity cost of producing one of each product?
- Who has the comparative advantage in planes?
- Who has the comparative advantage in cruise ships?
- What is a terms of trade that benefits both countries?

Korea can produce 3 cars or 9 motorcycle AND Germany can produce 4 cars or 8 motorcycles

	Cars	Motorcycles
Korea		
Germany		

Use the chart above to help you answer the following questions:

- What is the opportunity cost of producing one of each product?
- Who has the comparative advantage in planes?
- Who has the comparative advantage in cruise ships?
- What is a terms of trade that benefits both countries?

Japan can produce 4 laptops or 12 phones AND Brazil can produce 1 laptops or 5 phones.

	Laptops	Phones
Japan		
Brazil		

Use the chart above to help you answer the following questions:

- What is the opportunity cost of producing one of each product?
- Who has the comparative advantage in planes?
- Who has the comparative advantage in cruise ships?
- What is a terms of trade that benefits both countries?

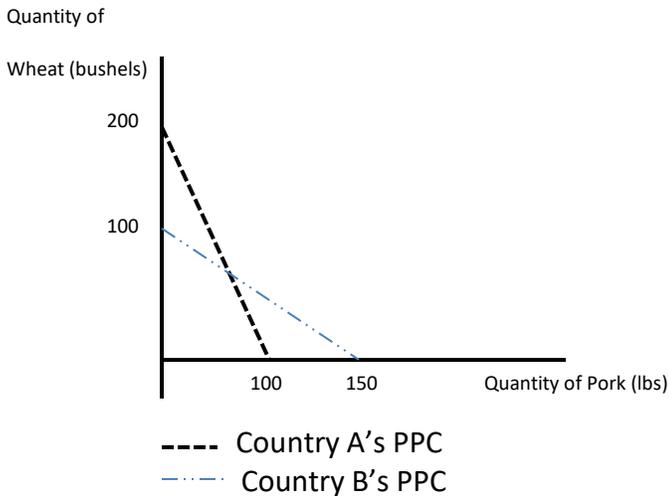
Cuba takes 4 hrs to make a TV and 12 hrs to make salsa AND Mexico takes 1 hr to make a TV and 5 hours to make salsa

	TVs	Salsa
Cuba		
Mexico		

Use the chart above to help you answer the following questions:

- What is the opportunity cost of producing one of each product?
- Who has the comparative advantage in planes?
- Who has the comparative advantage in cruise ships?
- What is a terms of trade that benefits both countries?

Work through the following example without Mr. Clifford's help.



Which country has the absolute advantage in wheat production?

Which country has the absolute advantage in pork production?

Which country has a comparative advantage in wheat?

Which country has a comparative advantage in pork?

	Wheat	Pork
Country A		
Country B		

Watch Comparative Advantage and Terms of Trade <https://www.youtube.com/watch?v=ol4NexZOill>

Use Mr. Clifford's example and complete the grid that shows how many toys and planes China and the USA can produce

	Planes	Toys
USA		
China		

Complete the grid below showing the per unit opportunity cost for each good.

	Planes	Toys
USA	1 plane =	1 toy =
China	1 plane =	1 toy =

Which country should specialize in producing planes?

Which country should specialize in producing toys?

Mr. Clifford explains the importance of the terms of trade. In order to benefit from trade both countries must do better than if they produced the items themselves. In other words when the USA gives China 1 plane they must get at least _____ toys in trade in order to benefit. China is not willing to pay more than _____ toys for a plane.

Suppose that Fred and Barney both produce pizza and hot dogs. The table below gives the number of items they can produce with the same amount of resources.

	Pizza	Hot Dogs
Fred	2	4
Barney	8	2

Complete the chart below showing the per unit opportunity cost of each good.

	Pizza	Hot Dogs
Fred	1 pizza =	1 hot dog =
Barney	1 pizza =	1 hot dog =

If Barney specializes in pizza and then trades with Fred, in order for that trade to benefit her she must get at least _____ hot dogs for 1 pizza. If Fred specializes in hot dogs and trades, in order for the trade to be beneficial for him he must get at least _____ pizza for 1 hot dog.

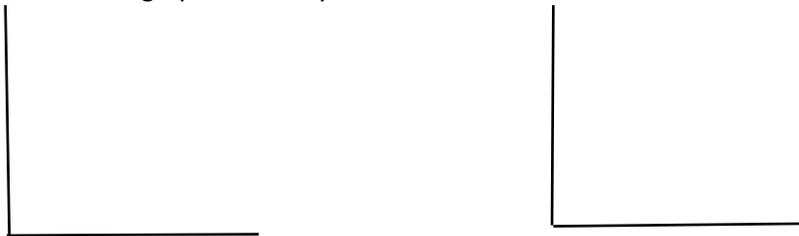
Suppose that Jane and Bob both produce widgets and gadgets from their available resources, but they currently do not trade with one another. The table below gives the number of hours of labor needed to produce one widget or one gadget for Bob and Jane.

	Hours of labor needed to produce a widget	Hours of labor needed to produce a gadget
Bob	2	4
Jane	3	1.5

To solve this problem you need to determine how much product can be produced. Assume that Jane and Bob each have 120 hours of labor time. Complete the chart below to show their production.

	Widgets produced	Gadgets produced
Bob		
Jane		

Sketch two graphs that show Bob's and Jane's production possibility frontier. Place Widgets on the y-axis and gadgets on the x-axis. Label both graphs carefully.



What is Bob's opportunity cost of producing an additional gadget ?

What is Jane's opportunity cost of producing an additional gadget?

What is Bob's opportunity cost of producing an additional widget?

What is Jane's opportunity cost of producing an additional widget?

Which product should Bob specialize in?

Which product should Jane specialize in?