

International Trade

Suppose that the Brewing Industry and the Wine Industry use the Same type of Skills and Equipment

In the US we have 100 beverage workers, and in France they have 100 beverage workers.
In the US, 1 worker can make either 4 barrels of beer or 2 barrels of wine per day.
In France, 1 worker can make either 1 barrel of beer or 4 barrels of wine per day.

1. Draw the PPF For France. Draw the PPF for the U.S.

Put Beer on the X axis and Wine on the Y axis

2. What is the slope of the PPF for France? What is the Slope of the PPF for the US?
What is the equation of the PPF for France? For the US?

3. In the US, what is the opportunity cost to produce one barrel of beer?
To produce 1 barrel of wine?

4. In France, what is the opportunity cost to produce one barrel of beer?
To produce 1 barrel of wine?

Definition: You have an **absolute advantage** in producing something if you can do it with fewer resources.
(In other words, you are more productive, it takes you less time or workers)

Definition: You have a **comparative advantage** if you can do it with a smaller opportunity cost.
(You give up less than someone else when you produce this good)

5. Question: Who has an absolute advantage in beer? In wine? Why?

6. Question: Who has a comparative advantage in beer? In wine? Why?

Countries should specialize in what they have a comparative advantage in, and then trade!

7. Suppose we don't trade, and each use 1/2 our workers to produce each product. How much Beer and Wine will we have???

8. Suppose we specialize? How much of each do we end up with?

9. What would be a fair trading price that we could use, where both countries would benefit?

****Neither country will be willing to give up more for something than they could do on their own!*

Note: Comparative advantage makes people in both countries better off! Even if one country has an absolute advantage in everything!

The benefit only depends on the opportunity costs being different, so that a comparative advantage exists!

