

1.4 — The Ricardian View of Trade: Formal One-Factor Model — Practice Problems (Solutions)

ECON 324 — International Trade

Suppose the following facts to set up:

- Home has 100 Laborers
 - Requires 5 workers to make 1 wheat
 - Requires 10 workers to make 1 car
- Foreign has 200 Laborers
 - Requires 2 workers to make 1 wheat
 - Requires 8 workers to make 1 car

Plot wheat (w) on the horizontal axis and cars (c) on the vertical axis.

1. Write the equation of each country's production possibilities frontier (PPF).
2. Graph each country's PPF.
3. Which country has an *absolute* advantage in producing each good? Why?
4. Find each country's opportunity cost of producing each good.
5. Which country has a *comparative* advantage in producing each good? Why?
6. Which country should specialize in producing which good?
7. What will the range of possible terms of trade be?