

Boston College
Problem Set 1, Fall 2012
EC 131 - Principles of Microeconomics (Continued)

2. Explain the difference between absolute advantage and comparative advantage. Which is more important in determining trade patterns, absolute advantage or comparative advantage? Why?

3. The only two countries in the world, Alpha and Omega, face the following production possibilities frontiers.

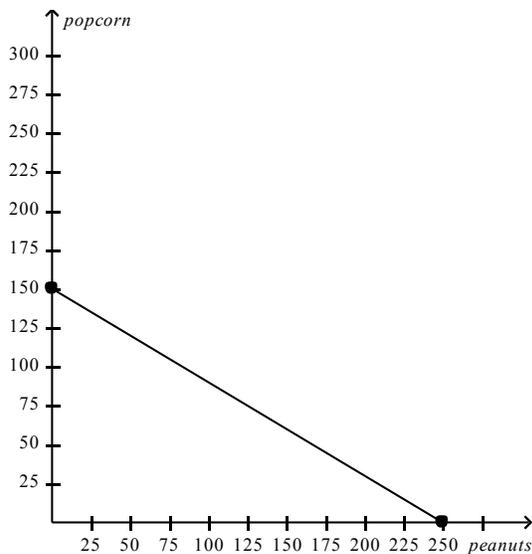


Figure 1: Alpha's Production Possibilities Frontier

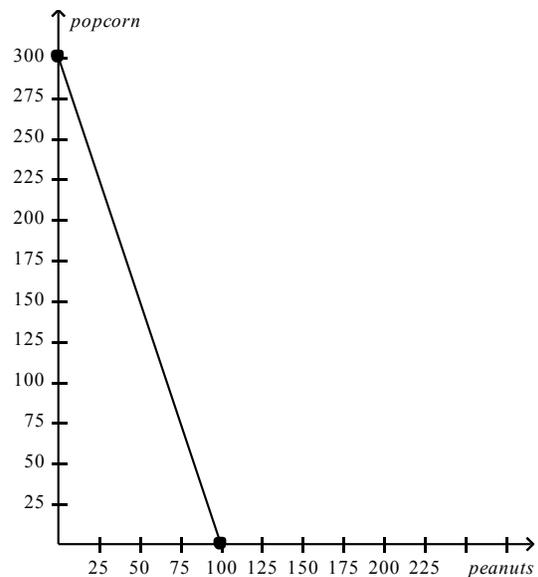


Figure 2: Omega's Production Possibilities Frontier

(a) Assume that each country decides to use half of its resources in the production of each good. Show these points on the graphs for each country as point A.

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(b) If these countries choose not to trade, what would be the total world production of popcorn and peanuts?

(c) Now suppose that each country decides to specialize in the good in which each has a comparative advantage. By specializing, what is the total world production of each product now?

(d) If each country decides to trade 100 units of popcorn for 100 units of peanuts, show on the graphs the gain each country would receive from trade. Label these points B.

4. Assume that Japan and Korea can switch between producing cars and producing airplanes at a constant rate.

	Hours Needed to Make 1		Quantity Produced in 2400 Hours	
	Car	Airplane	Cars	Airplanes
Japan	30	150	80	16
Korea	50	150	48	16

Table 1: Production technology for Japan and Korea

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- (c) Suppose that without trade, Japan produced and consumed 50 cars and 6 airplanes, and Korea produced and consumed 27 cars and 7 airplanes. Both countries decide then to specialize in the production of the good in which it has a comparative advantage and trade 28 cars for 8 airplanes. What is the consumption in both countries of cars and airplanes after trade?