

## 1.3 — The Ricardian View of Trade: Comparative Advantage — Practice Problems

ECON 324 — International Trade

Tuesday August 25, 2020

*Gondor* and *Rohan* can each produce *oil* ( $o$ ) and *linen* ( $l$ ).

If *Gondor* devotes all of its resources to producing either good, it can produce 500 barrels of oil or 200 yards of linen. If *Rohan* devotes all of its resources to producing either good, it can produce 300 barrels of oil or 100 yards of linen.

Currently, *Gondor* is producing 250 barrels of oil and 100 yards of linen, and *Rohan* is producing 150 barrels of oil and 50 units of linen.

Put oil ( $o$ ) on the horizontal axis and linen ( $l$ ) 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?