Chapter 3.1

1. True or False? The Parable of the Magic Island was about the effect of an island that converts one nation's currency into another nation's currency.

◉ True

◉ False

2. True or False? The Parable of the Magic Island is intended to demonstrate that trading with others is akin to magic, in that it allows a nation to acquire a permanent increase in wealth by only paying a temporary economic adjustment cost.

◉ True

◉ False

3. True or False? The Parable of the Magic Island is intended to demonstrate that a country trading with other countries has the same consequences for an economy as a technological innovation.

◉ True

◉ False

4. True or False? The Parable of the Magic Island is intended to demonstrate that international trade and technological innovation have vastly different consequences for an economy.

◉ True

◉ False

5. True or False? The Parable of the Magic Island is intended to demonstrate that, like magic, benefits from international trade are simply not real.

◉ True

◉ False

6. True or False? The Parable of the Magic Island is intended to demonstrate that international trade and immigration have vastly different consequences for an economy.

7. Which of the following is the best statement regarding the consequences of trade with China?

    a. Overall the benefits are positive, helping virtually every segment of the U.S. economy

    b. Overall the benefits are positive, but it has adversely impacted many manually intensive / low-skill workers in the U.S.

    c. Overall the benefits are positive, but it has adversely impacted high-skill and highly educated workers.

    d. Overall the benefits are negative, though a few high-skill and highly educated workers have benefitted.

Chapter 3.2

In this worksheet we will learn the concept of *comparative advantage* and how people, groups, and nations gain from trading with one another. You have heard the saying: *there is no such thing as a free lunch.* That saying is wrong. You can get something from nothing, and I'll show you how, using an economic model.

Suppose we have two countries, the U.S. and Cuba, whose production possibilities frontiers (PPFs) for producing beer and cigars are as follows.

U.S.: Number Cigars Produced = 20 − 1(Number Beers Produced)
Cuba: Number Cigars Produced = 20 − 2(Number Beers Produced)

(1) Plot the PPF's for each country below. Clearly label which country corresponds to each PPF

(2) For the U.S., the opportunity cost of producing one beer is _____ cigar(s).
(3) For the U.S., the opportunity cost of producing one cigar is _____ beer(s).
(4) For Cuba, the opportunity cost of producing one beer is _____ cigar(s).
(5) For Cuba, the opportunity cost of producing one cigar is _____ beer(s)

(6) The two countries reside in *autarky*, meaning the two countries do not trade with one another. Fill in the table below.

		Production	Exports	Imports	Consumption
U.S.	Cigars				
	Beers				
Cuba	Cigars				
	Beers				

(7) Now suppose that the two countries engage in trade. We will learn that when countries trade, they willproduce the good for which they possess a comparative advantage, the good with the lowest opportunity cost, and only that good. If this is the case, then the U.S. will be producing _____cigars and _____ beers, while Cuba will be producing _____ cigars and _____beers.

(8) After trade, suppose that Cuba trades 10 cigars for 7 beers, meaning Cuba exports 10 cigars to the U.S. and imports 7 beers from the U.S. Fill in the table below.

		Production	Exports	Imports	Consumption
U.S.	Cigars				
	Beers				
Cuba	Cigars				
	Beers				

(9) After trade, Cuba gains _____ beers and _____ cigars, relative to autarky.

(10) After trade, the U.S. gains _____ beers and _____ cigars, relative to autarky.

(11) For the U.S., indicate the point of consumption on the PPF curve before trade. Then, indicate the point of consumption for the U.S. after trade. Do the same for Cuba.

(12) Can you get something for nothing? How?

Practice Questions
Chapter 3.2—Comparative advantage

(13) A Production Possibilities Frontier is a curve depicting the ...

○ a. The maximum amount of good A one region can produce, given it is producing a certain amount of good B.

○ b. All the various "feasible" points of production for goods A and B for a region.

○ c. All the various combinations of consumption of goods A and B a region can realize, if it trades with other regions
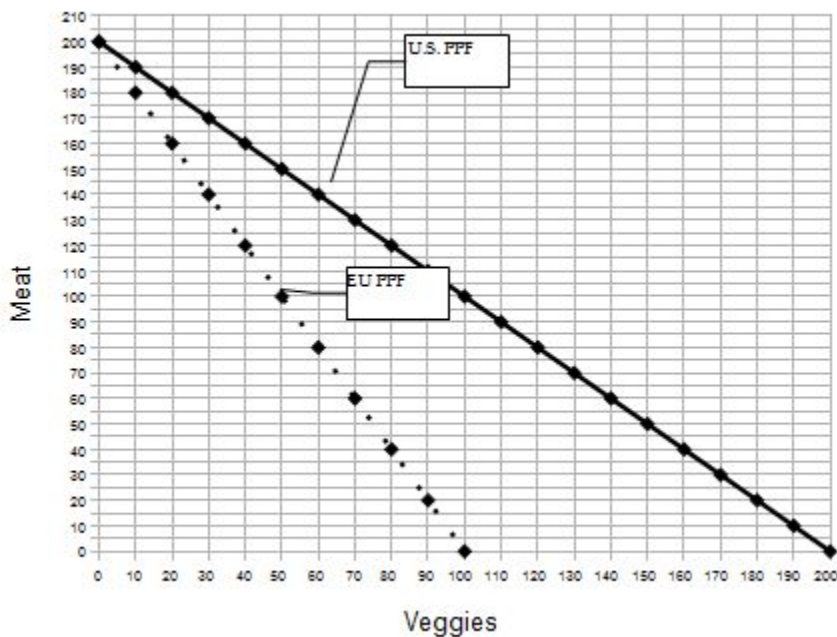
○ d. both a and b

(14) In the graph below, the formula for the U.S. PPF is...?

○ a) US: Meat = 200 - 1(Veggies)

○ b) US: Meat = 100 - 1(Veggies)

○ c) US: Meat = 200 - 2(Veggies)

○ d) US: Meat = 200 - (1/2)(Veggies)

(15) In the graph below, the formula for the E.U. PPF is...?

○ a) EU: Meat = 200 - (1/2)(Veggies)

○ b) EU: Meat = 200 - 2(Veggies)

○ c) EU: Meat = 200 - 1(Veggies)

○ d) EU: Meat = 100 - 2(Veggies)

(16) U.S. and E.U. PPF (use this graph to answer questions 2 and 3)

Practice Questions
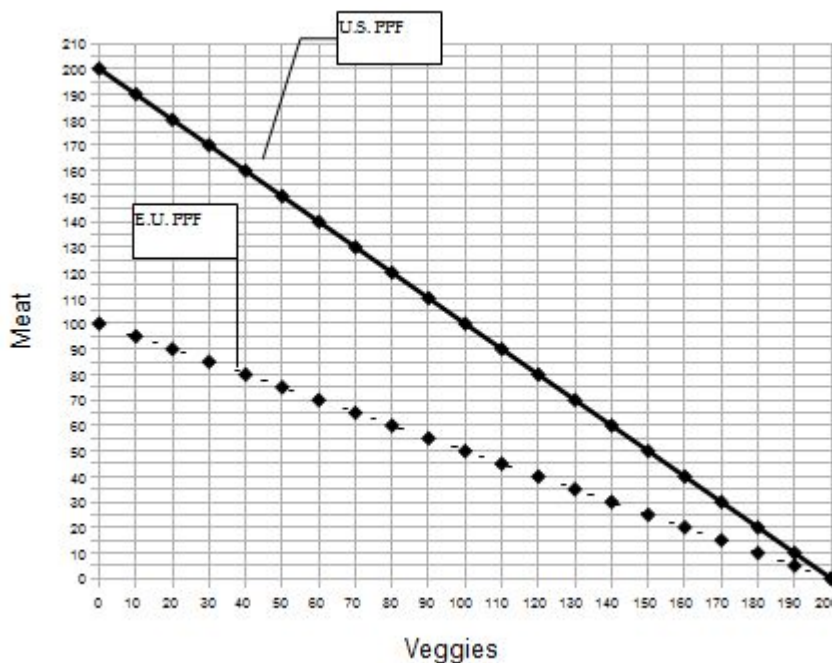**Chapter 3.2—Comparative advantage**

(17) In the graph below, the formula for the U.S. PPF is...?

   ○ a) US: Meat = 200 - 1(Veggies)

   ○ b) US: Meat = 200 - 2(Veggies)

   ○ c) US: Meat = 100 - (1/2)(Veggies)

   ○ d) US: Meat = 100 - 1(Veggies)

(18) In the graph below, the formula for the E.U. PPF is...?

   ○ a) EU: Meat = 100 - (1/2)(Veggies)

   ○ b) EU: Meat = 100 - 2(Veggies)

   ○ c) EU: Meat = 200 - 1(Veggies)

   ○ d) EU: Meat = 200 - (1/2)(Veggies)

(19) Use this graph to answer questions 20 and 21.

(20) If the PPF for a clan is: grain = 10 - (3/4)(salmon), the opportunity cost of grain is _____ salmon.

(21) If the PPF for a clan is: grain = 10 - (3/4)(salmon), the opportunity cost of salmon is _____ grain.

(22) If the PPF for a clan is: grain = 10 - (1/2)(salmon), the opportunity cost of salmon is _____ grain.

(23) If the PPF for a clan is: grain = 10 - (1/2)(salmon), the opportunity cost of grain is _____ salmon.

(24) If the opportunity cost of one grain is 1/5 salmon, the opportunity of one salmon must be _____ grain.

5

Practice Questions
Chapter 3.2—Comparative advantage

(25) If a country can produce salt at a lower opportunity cost than the U.S., that country has a(n) _____ in salt.

○   absolute advantage

○   relative advantage

○   comparative advantage

○   production advantage

(26) Countries can only consume at a point outside (above, and to the right) of their PPF curve if they...

○   a. exploit their laborers

○   b. engage in slavery

○   c. trade with other regions

○   d. export goods but do not import anything

○   e. both c and d

(27) When two countries engage in and benefit from trade (and have linear PPFs), each country will produce ...

○   a. only those goods for which they have a comparative advantage

○   b. only those goods in which they produce at a lower opportunity cost

○   c. all the goods which they can produce the most number of units, relative to other countries

○   d. any good, it doesn't matter, as both countries will still benefit from trade

○   e. both a and b

(28) Trade is such a blessing to the world because it allows every region to "get something for nothing",

○   True

○   False

(29) When countries trade, the type of food a country produces doesn't tell us everything about the type of foods that country consumes.

○   True

○   False

Practice Questions
Chapter 3.2—Comparative advantage

(30) Two countries can always engage in trade so long as their PPFs are different. If the PPFs are the same, they are neither harmed nor benefited by trade.

○ True

○ False

Use the following information for questions 31 & 32.

Suppose that, initially, the US and EU do not engage in trade. In autarky, the U.S. produces and consumes 1,000 Meat and 2,000 Veggies, while the EU produces and consumes 1,500 Meat and 2,000 Veggies. Once they engage in trade, the US produces 4,500 Veggies and no Meat, while the EU produces no Veggies and 3,000 Meat.

(31) True or False: If the U.S. and EU traded 2,000 Veggies for 1,000 Meat, both countries are made unambiguously better off.

○ True

○ False

(32) True or False: If the U.S. and EU traded 1,000 Veggies for 2,000 Meat, both countries are made unambiguously better off.

○ True

○ False

(33) The anti-globalization crowd is largely against international trade because...

○ They believe trade allows multinational corporations to "bully and oppress" smaller countries.

○ They believe most countries have near identical PPFs

○ They believe most countries have non-linear PPFs

○ They don't believe in the concept of comparative advantage