

SSEIN1.a: Comparative Advantage Notes

Two men live alone on an isolated island. To survive they must undertake a few basic economic activities like water carrying, fishing, cooking and shelter construction and maintenance. The first man is young, strong, and educated. He is also, faster, better, more productive at everything. The second man is old, weak, and uneducated. He produces less than the younger man. In some activities the difference between the two is great; in others it is small. For instance, the younger man can gather 50 coconuts every hour, or catch 150 fish. While the older man can only gather 5 coconuts or catch 25 fish every hour.

1. Who is better at all activities in the scenario above? _____
2. What is the opportunity cost for the younger man if he dedicates his hour to gathering coconuts? _____
3. What is the opportunity cost for the older man if he dedicates his hour gathering coconuts _____
4. Should they work separately or together on the island? Explain.

- Absolute Advantage – person or nation can produce _____
- _____
- Comparative Advantage – the ability to produce _____
- _____
- Law of comparative advantage – a nation or person is better off when it produces goods and services for which it has a _____

▪ Coconuts or Fish?

Absolute Advantage		
	Coconuts	Fish
Young		
Old		

- Young Man has _____ advantage because he can _____

Comparative Advantage		
	Coconuts	Fish
Young		
Old		

- OGO – “Other goes over” method shows the _____
- Young Man has _____ advantage because he _____
- _____ than the old man.

- His opportunity cost for collecting coconuts is _____ relative to the old man.
- The old man has the _____ advantage in catching fish because he gives _____
- _____
- His opportunity cost for catching fish is _____ relative to the young man.
- Important Note: the only time two people/nations/firms will not trade is if there is no _____ when opportunity cost is the _____

- Steps for Determining Comparative Advantage
 - Scenario: Canada and Mexico are considering the trade of two goods. Canada can produce 100 Furs or 100 trees. Mexico can produce 50 furs or 200 trees.

Step 1: Input the Data

Productive Output		
	Fur	Trees
Canada		
Mexico		

Step 2: Find the Opportunity Cost of Production

Opportunity Cost		
	Fur	Trees
Canada	_____ / _____ = _____	_____ / _____ = _____
Mexico	_____ / _____ = _____	_____ / _____ = _____

Step 3: Analyze the Data to Determine Comparative Advantage

- It costs Canada _____ fur for every tree it produces.
- It costs Mexico _____ fur for every tree it produces.
- It costs Canada _____ tree for every fur it produces.
- It costs Mexico _____ tree for every fur it produces.
- Therefore, _____ should specialize in the production of fur, while _____ should specialize in the production of trees.

Kate and Carl

Productivity Per Hour		
	T-Shirts per hour	Birdhouses per hour
Kate	6 (_____ / _____ = _____)	2 (_____ / _____ = _____)
Carl	1 (_____ / _____ = _____)	1 (_____ / _____ = _____)

1. Who has absolute advantage in this situation? _____
2. It costs Kate _____ birdhouses to produce 1 t-shirt.
3. It costs Kate _____ shirts to produce 1 birdhouse.
4. It costs Carl _____ to produce 1

- t-shirt.
5. It costs Carl _____ to produce 1 birdhouse.
6. _____ has a comparative advantage when producing t-shirts.
7. _____ has a comparative advantage when producing birdhouses.
8. Therefore, _____ should produce t-shirts and _____ should produce birdhouses.