

Name (print): _____ Due: _____

Second Exercise on Comparative Advantage

Each student will complete their own paper.

	Home	Foreign*	Possible production		Relative
Labor (hours / year)	L=600	L*=1500	Home	Foreign	Productivity
			$L O_{LS}$	$L^* O^*_{LS}$	O_{LS}/O^*_{LS}
Shoes (pair S / hour)	$O_{LS}=10$	$O^*_{LS}=2$			
			$L O_{LT}$	$L^* O^*_{LT}$	O_{LT}/O^*_{LT}
Tea (bushel T / hour)	$O_{LT}=5$	$O^*_{LT}=4$			
Opportunity costs					
Tea					
	O_{LS}/O_{LT} (pair S / bushel T)				
Shoes					
	O_{LT}/O_{LS} (bushel T / pair S)				

1. Use the Ricardian model of international trade to answer the following questions. The table above shows the labor productivity of each country in each industry as its output per hour of labor.
 - a. If Home produces both goods in autarkic equilibrium (no trade), then what relative price of S must prevail? Hint: workers will not want to produce a good unless its price is greater than or equal to its opportunity cost.

 - b. Which country has comparative advantage in which good and why?

 - c. Turn your paper over and graph one possible international trade equilibrium. Assume that the countries agree to trade at a relative price of S in the middle of the range of their opportunity costs. (Hint: use the possible production values you may have calculated while completing the table above.)

 - d. How will Home's wage rate compare to the wage rate in Foreign? (Hint: use the relative productivity values that you may have calculated while completing the table.)