



**ECO 1311, University of Dallas**  
**Comparative and Absolute Advantage-- Practice Problems**

1. In Australia one unit of labor can produce 25 computers or 25 bushels of wheat. In Taiwan one unit of labor can make 30 computers or 50 bushels of wheat. Assume that computers and wheat are the only two goods in the world. (What is the purpose of this assumption?)
  - a. What is Australia's opportunity cost of making a computer? What is Taiwan's opportunity cost of making a computer?
  - b. What is Australia's opportunity cost of producing a bushel of wheat? What is Taiwan's opportunity cost of producing a bushel of wheat?
  - c. Does Australia have *absolute advantage* in producing anything? Explain.
  - d. Does Australia have *comparative advantage* in producing anything? Explain.
  - e. Does Taiwan have *comparative advantage* in producing anything? Explain.
  - f. Is it possible for Australia to gain by trading with Taiwan? Explain.
  - g. Is it possible for Taiwan to gain by trading with Australia? Explain.
  - h. What are the *limiting terms of trade*, outside of which exchange between Australia and Taiwan will not occur? (These will be barter ratios, e.g. 2 computers/bushel of wheat.)
  
2. Omega Inc. is on the front page of *Fortune*, *Forbes*, and *Bloomberg BusinessWeek* for its rapid growth and high profits gained by producing a wide range of high quality, reasonably priced goods. Congressmen praise Omega as an example of successful entrepreneurship.

---

Some problems have been extracted and/or adapted from:

- Cowen, Tyler, and Alex Tabarrok. *Modern principles of microeconomics*. Macmillan International Higher Education, 2015.
- Acemoglu, Daron, David Laibson, and John List. *Economics, global edition*. Pearson, 2015.
- Miller, Roger LeRoy. *Economics Today: The Micro View*. Pearson, 2018.

As it happens Omega is located on an island off the coast of New Jersey. They are noted for their secrecy as much as for their success. All anyone outside of Omega Inc. knows is that raw materials and workers go onto the island and finished goods come out.

One day an investigative reporter manages to sneak on the island. He discovers that Omega is not manufacturing at all – they are an import/export business. When this is revealed the praise turns to bitter criticism. Where Omega had previously been lauded for their efficiency, Congressmen now demand an investigation of this corporation that is stealing American jobs.

- a. Is the US any worse off if Omega turns out to be exporting and importing rather than manufacturing? Why?
- b. Would it be reasonable to argue that trade is simply an alternate means of production? Explain.
- c. The business economist Peter Drucker (*Innovation and Entrepreneurship*, 1985) once described the activities of entrepreneurs as (1) introducing new products; (2) introducing new processes (i.e. new ways to produce old products); (3) opening up new markets; and (4) discovering new resources and new sources of old resources. Doesn't international trade do these same things? Is there any reason why we should fear international trade any more or less than entrepreneurship? Is it more damaging to lose your job to a low-wage foreigner than it is to lose your job because of a domestic innovation in production that requires less labor?
- d. International trade theory suggests that, as two nations move from no trade to free trade, there will be a tendency for the prices of goods to move toward world prices, and also a tendency for the prices of the inputs (wages, rents, etc.) used to produce the goods to converge to a world input price level. This could be part of the explanation for falling or stagnant incomes of many US workers, especially those who are less educated.
- e. Is there some reason why US workers should be paid more than Indian or Chinese workers with the same qualifications doing the same work? Are people entitled to be supported in the manner to which they have become accustomed?

---

Some problems have been extracted and/or adapted from:

- Cowen, Tyler, and Alex Tabarrok. *Modern principles of microeconomics*. Macmillan International Higher Education, 2015.
- Acemoglu, Daron, David Laibson, and John List. *Economics, global edition*. Pearson, 2015.
- Miller, Roger LeRoy. *Economics Today: The Micro View*. Pearson, 2018.