# **Trading**

Why do people trade?

As long as the trade is voluntary, for both parties the value of,

Item received > Item given away

Usually made easier through the use of money.

Basically, trading settling problems in allocation strategies.

## **Output problems**

Output problems state that you get a certain amount of product out of a given input.

## Input problems

Input problems state that it takes a certain amount of input to get a given product.

## **Absolute Advantage**

#### For output problems:

You look at if one nation (individual/company) can produce more output with the same resources as the other.

#### For Input Problem:

You look at who uses the least amount of input to get the output.

## **Comparative Advantage**

An individual, business, or country can produce a good or service at a lower <u>Opportunity</u> <u>Cost</u> than another producer.

Opportunity Cost will always be expressed in the good not the input.

One actor cant have the comparative advantage in both situations.

### **Terms of Trade**

The rate by which one unit of a good or service is traded for another unit of a good or service.

The Terms of Trade will only be beneficial to both producers if the exchange rate falls between both of their opportunity cost.

## **Finding Mutually Beneficial Terms of Trade**

- Calculate the opportunity costs and identify which nations have the comparative advantage.
  - 1. A nation which has comparative advantage in something should specialize in that something.
- 2. Pick a good in which the opportunity costs of both are whole numbers
- 3. Mutually Beneficial Terms of Trade will be between the 2 opportunity costs.

# **Consumption Possibilities**

- Combinations of goods and services that could be consumed.
- People in the nations have greater access to the two goods than they did before.

