Faculty of Business and Economics
Department of Economics

THE UNIVERSITY OF MELBOURNE

ECON10003
Pre-Tutorial #9

Introductory Macroeconomics

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Week Starting 10th May 2021

The Tutorial. This week's tutorial looks at international trade.

Note that your tutor is under no obligation to go through the answers to the pre-tutorial work in detail. The focus in the tutorial will be on the tutorial work itself – the questions here are preparatory.

Reading Guide. You should look carefully over lectures 17 and 18. You may also find Chapter 16 of BOFAH useful.

Key Concepts. Production possibilities curve. Absolute/Comparative advantage. Specialisation.

Problems.

1. What is a production possibilities curve? What is meant by the term comparative advantage? How does it differ from the term absolute advantage? Is it possible for someone not to have a comparative advantage?

2. The following table shows the number of minutes it takes to produce one unit of each good. There are two workers in the economy.

	Shirt	Hat
Julia	60	120
Tim	30	90

   (a) Julia and Tim each work 8 hours per day. Draw this production possibilities curve for Julia, for Tim, and for the economy as a whole.

   (b) What is the pattern of comparative advantage? Who has the absolute advantage in producing shirts? Who has the absolute advantage in producing hats?

   (c) Suppose that Julia and Tim like to consume shirts and hats in equal proportions. That is, these goods are perfect complements. Illustrate using the individual production possibilities curve, where they would like to consume if there was no trade.

   (d) At what prices would Julia and Tim both be happy to trade with each other? What would happen if the price of hats in the market exceeded 3 shirts? What would Julia produce? And Tim?

3. Consider a commodity, which is exported from county B to country A.

(a) Draw the demand and supply curve for this good, in country A and in country B. What does the export of this good from B to A imply about the equilibrium price of this good in autarky in each country?

(b) In a trade equilibrium, the price in each country must be the same and the world demand for the good must equal the world supply for the good. Use the demand and supply analysis to show that it is necessary for the world price to lie between the two countries' autarky prices for a trade equilibrium to exist.