

Subject: Economics

Topic: Law of Comparative Advantage and Gains from Trade

Sub-topic: Gains from Trade and Terms of Trade

Level: S.5

Learning objectives:

Content

Students should be able to

1. compute the gains from trade for two countries with given Terms of Trade
2. explain the gains from trade for two countries with different Terms of Trade
3. explain the relationship between Terms of Trade and the distribution of gains from Trade
4. draw conclusion on the possible range of Terms of Trade that is beneficial to a country

Language

Students should be able to write a paragraph to explain the gains from trade for a country based on the Terms of Trade using the following pattern:

As Country A has the comparative advantage in the production of good X, Country A should specialize in good X production and exports good X. The opportunity cost of producing 1 unit of good X is _____ units of good Y. Given that the terms of trade are 1 unit of good X for _____ units of good Y, Country A can gain _____ units of good Y for each unit of good X exported.

S.5 Economics
Law of Comparative Advantage and Gains from Trade
Gains from Trade and Terms of Trade
Worksheet 2

Name: _____ Class: _____ No.: _____ Date: _____



Writing

Case I

The following table shows the output conditions of two countries, A and B, under autarky. The two goods produced are rice and computers. Suppose the Terms of Trade (TOT) are 1 unit of rice for 1 unit of computers. What are the gains from trade for both countries? Explain your answer.

Autarky table	Each unit of resources can produce		
	Rice (in units)		Computers (in units)
Country A	20	OR	12
Country B	5	OR	10

First, work out the opportunity cost of producing rice and computers for both countries using the following table:

Opportunity cost table		
Country A		
Country B		

Explain the direction of specialization and trade of the two countries below:

Country A's opportunity cost of producing rice is _____ units of computers. Country B's _____

As _____

_____, _____

Therefore, _____

Hint: The direction of specialization and trade obtained above forms the basis of your calculations. Make use of the organizer below to sort out the useful information for your explanation.

Country ____ specializes in rice production and exports rice.	
The opportunity cost of producing 1 unit of rice	_____ units of computers
Terms of Trade: 1 unit of rice	_____ units of computers
Gains from Trade	TOT – opportunity cost = _____ units of computers for each unit of rice exported

Country _____ opportunity cost of producing 1 unit of rice is _____. Given that the terms of trade are _____, Country _____ can gain _____ for each unit of rice exported.

Hint: Now, repeat the steps above to find the gains for the country exporting computers.

Country _____ specializes in rice production and exports rice.	
The opportunity cost of producing 1 unit of rice	
Terms of Trade: 1 unit of rice	
Gains from Trade	

Country **A's** opportunity cost of producing 1 unit of rice is _____ . Country **B's**

_____ . As Country B can produce rice

_____ , Country B has the comparative advantage

_____ . Therefore, Country B should specialize in _____

_____ ..

Country B's opportunity cost of _____ . Given that the terms of trade are _____ , Country B can gain _____ for each unit of computers exported.

Hint: In Cases II and III, as production conditions under autarky remain unchanged, just explain the gains from trade for each country with different Terms of Trade and try to come up with a conclusion at the end.

Case II

The following table shows the output conditions of two countries, A and B, under autarky. The two goods produced are rice and computers. Suppose the Terms of Trade (TOT) are **1 unit of rice for 2 units of computers**. What are the gains from trade for both countries? Explain your answer.

Autarky table	Each unit of resources can produce		
	Rice (in units)		Computers (in units)
Country A	20	OR	12
Country B	5	OR	10

The following vocabulary items may help you in your explanation:

gains from trade is zero, therefore, trade is not beneficial to

Gains from trade for Country A:

Country A' opportunity cost of _____

Given that _____

Country A can gain _____

Gains from trade for Country B:

Case III

The following table shows the output conditions of two countries, A and B, under autarky. The two goods produced are rice and computers. Suppose the Terms of Trade (TOT) are **1 unit of rice for 0.6 unit of computers**. What are the gains from trade for both countries? Explain your answer.

Autarky table	Each unit of resources can produce		
	Rice (in units)		Computers (in units)
Country A	20	OR	12
Country B	5	OR	10

Now write to explain the gains from trade for Country A.

The following vocabulary items may help you in your explanation:

as, is lower than, therefore, given that, gains from trade is zero, trade is not beneficial to

Country A's opportunity cost of producing 1 unit of rice is _____

1. From results obtained in Cases I to III, determine the factor affecting the distribution of gains from trade for both countries.

1. What is the range of Terms of Trade that is beneficial to both countries?

The Terms of Trade should lie between the _____ . In this case, TOT are
