Econ 165
Winter 2001/02

Stanford University
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Hand-out week 1

This week:

1. Classical Trade Theory

   1.1 the Ricardo model: unit labor requirements, comparative advantage, gains from trade.

   1.2 the Heckscher–Ohlin model: the 2x2x2 setup, four theorems: Stolper–Samuelson, Rybczynski, Heckscher–Ohlin, factor price equalization.

Readings: Krugman&Obstfeld, chpts 2, 4, and 5.

Practice problems:

1. How much does "Krugman&Obstfeld" cost abroad? Try to find the lowest foreign price by checking online booksellers.

2. Solve problems 1–5, K&O, chpt 2 (feel free to look at problems 6–10).

3. Explain the difference between absolute and comparative advantage. Come up with examples where someone (say you) has an absolute advantage (or disadvantage) in two activities. Who has the comparative advantage? Could one have a comparative advantage in both activities or none?

4. The 2x2x2 standard trade model — do it yourself: start with factor endowments and depict possible factor market equilibria in an Edgeworth box, translate these equilibria into a production possibility frontier, assume social indifference curves and depict the autarky equilibrium including the equilibrium relative price, finally take two countries (turning one upside down) and depict the free trade situation.