Remember, economics is the study of how societies produce and distribute goods in an attempt to satisfy the wants and needs of its members.

How do we satisfy our wants and needs in a global economy?

- We can be economically self-sufficient.
- We can specialize and trade with others, leading to economic interdependence (i.e. Globalization)
Imagine... only two goods: potatoes and meat... only two people: a potato farmer and a cattle rancher

What should each produce? Why should they trade?

The Production Opportunities of the Farmer and the Rancher

<table>
<thead>
<tr>
<th>Hours Needed to Make 1 lb. of:</th>
<th>Amount Produced in 40 Hours</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Meat</td>
</tr>
<tr>
<td>Farmer</td>
<td>20 hours/lb</td>
</tr>
<tr>
<td>Rancher</td>
<td>1 hour/lb</td>
</tr>
</tbody>
</table>

Production Possibilities Frontiers

(a) The Farmer’s Production Possibilities Frontier
**Production Possibilities Frontiers**

(b) The Rancher's Production Possibilities Frontier

**The Gains from Trade: A Summary**

<table>
<thead>
<tr>
<th></th>
<th>The Outcome Without Trade:</th>
<th>The Outcome With Trade:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>What They Produce and Consume</td>
<td>What They Produce and Consume</td>
</tr>
<tr>
<td><strong>Farmer</strong></td>
<td>1 lb meat (A) 2 lbs potatoes</td>
<td>0 lbs meat 4 lbs potatoes</td>
</tr>
<tr>
<td><strong>Rancher</strong></td>
<td>20 lbs meat (B) 2.5 lbs potatoes</td>
<td>24 lbs meat 2 lbs potatoes</td>
</tr>
</tbody>
</table>

**The Outcome With Trade:**

- Farmer: Gets 3 lbs meat for 1 lb potatoes, 3 lbs meat (A*)
- Rancher: Gives 3 lbs meat for 1 lb potatoes, 21 lbs meat (B*)

---

**The Outcome Without Trade:**

- Farmer: 1 lb meat (A), 2 lbs potatoes
- Rancher: 20 lbs meat (B), 2.5 lbs potatoes

**With Trade:**

- Farmer: 3 lbs meat for 1 lb potatoes, 3 lbs meat (A*)
- Rancher: 21 lbs meat for 1 lb potatoes, 3 lbs potatoes
Trade Expands the Set of Consumption Possibilities

(a) How Trade Increases the Farmer’s Consumption

(b) How Trade Increases The Rancher’s Consumption

The Gains from Trade: A Summary

<table>
<thead>
<tr>
<th></th>
<th>The Gains From Trade:</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Increase in Consumption</strong></td>
<td></td>
</tr>
<tr>
<td>Farmer</td>
<td>2 lbs meat (A*- A)</td>
</tr>
<tr>
<td></td>
<td>1 lb potatoes</td>
</tr>
<tr>
<td>Rancher</td>
<td>1 lb meat (B*- B)</td>
</tr>
<tr>
<td></td>
<td>1/2 lb potatoes</td>
</tr>
</tbody>
</table>
The Farmer and the Rancher
Specialize and Trade
Each would be better off if they specialized in producing the product they are more suited to produce, and then trade with each other.
- The farmer should produce potatoes.
- The rancher should produce meat.

The Principle of Comparative Advantage
Differences in the costs of production determine the following:
- Who should produce what?
- How much should be traded for each product?

Who can produce potatoes at a lower cost—the farmer or the rancher?

Absolute Advantage
- Describes the productivity of one person, firm, or nation compared to that of another.
- Absolute advantage can be measured in two ways:
  - Least number of hours to produce a good.
  - Most number of goods produced in a given amount of time.
Comparative Advantage

- Compares producers of a good according to their opportunity cost.
- The producer who has the smaller opportunity cost of producing a good is said to have a comparative advantage in producing that good.

The Opportunity Cost of Meat and Potatoes

<table>
<thead>
<tr>
<th></th>
<th>1 pound of meat</th>
<th>1 pound of potatoes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farmer</td>
<td>2 pounds of potatoes</td>
<td>1/2 pound of meat</td>
</tr>
<tr>
<td>Rancher</td>
<td>1/8 pounds of potatoes</td>
<td>8 pounds of meat</td>
</tr>
</tbody>
</table>

Should Tiger Woods Mow His Own Lawn?

?!?
What are the pros and cons of Globalization?

- Globalization means that free trade is spread to all corners of the world with no hindrances.

- [Globalization Video](#)