

MACROECONOMICS UNIT 1

PRACTICE SHEET



Part 1: Production Possibilities- Assume that the table below shows the economy of Cliffordland.

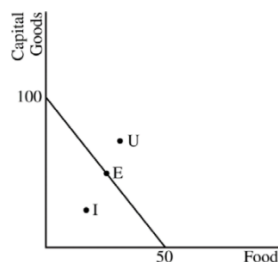
| | A | B | C | D | E |
|----------------|----|----|----|----|---|
| Capital Goods | 0 | 2 | 4 | 6 | 8 |
| Consumer Goods | 30 | 28 | 25 | 15 | 0 |

- Calculate the opportunity cost of switching from combination A to producing B. **2 Consumer goods**
- Calculate the opportunity cost of switching from combination B to producing D. **13 Consumer goods**
- Calculate the opportunity cost of switching from combination B to producing A. **2 Capital goods**
- Calculate the opportunity cost of switching from combination D to producing B. **4 Capital goods**
- Is this an example of increasing opportunity cost or constant opportunity cost? Explain. **This is an example of increasing opportunity cost. The first 2 capital goods cost 2 consumer goods while the last two capital goods cost 15 consumer goods. This production possibilities curve is bowed out.**
- Assume the economy of Cliffordland intentionally decides to produce combination D rather than combination B. What is the long-term trade-off of this decision? Explain. **Choosing to produce more capital goods and less consumer goods will provide more long run growth in the future.**

Part 2: FRQ Practice- Complete the following released question from the 2019 AP exam (Set 2, Question 3).

7. **(a) 1 point**

- One point is earned for drawing a correctly labeled production possibilities curve (PPC) for Sweden with food on the horizontal axis, capital goods on the vertical axis, and the relevant numerical values plotted.



(b) 1 point

- One point is earned for showing point I inside the PPC, point E on the PPC, and point U outside the PPC.

(c) 1 point

- One point is earned for stating that Sweden's economic growth rate will slow or be reduced.

(d) 1 point

- One point is earned for stating that Norway has a comparative advantage in the production of capital goods and for explaining that it has the lowest opportunity cost in producing capital goods (the opportunity cost of producing one unit of capital goods in Norway is $1/4$ a unit of food and in Sweden is $1/2$ a unit of food).

(e) 1 point

- One point is earned for stating a number between 20 and 40 units of capital.

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Part 3: Comparative Advantage- Answer the following questions to verify that you fully understand opportunity cost, absolute advantage, comparative advantage, and terms of trade.

Units produced per hour

| | Beef | Peppers |
|--------|-------------------------|----------------------|
| China | 20 1B cost 1/4 P | 5 1P cost 4 B |
| France | 8 1B cost 1/2 P | 4 1P cost 2 B |

Hours needed to produce one unit

| | Plane | Car |
|---------|-----------------------|------------------------|
| Mexico | 12 1P cost 2 C | 6 1C cost 1/2 P |
| Bolivia | 25 1P cost 5 C | 5 1C cost 1/5 P |

- Is this an output problem or an input problem? **Output, the question is giving the amount produced**
- What is China's opportunity cost of producing 1 pepper? **4 Beef**
- What is France's opportunity cost of producing 1 beef? **1/2 Pepper**
- What is China's opportunity cost of producing 1 beef? **1/4 Pepper**
- What is France's opportunity cost of producing 1 pepper? **2 Beef**
- Who has the absolute advantage in producing beef? Explain. **China because they can produce more beef. 20 > 8**
- Who has the absolute advantage in producing peppers? Explain. **China because they can produce more peppers. 5 > 4**
- Who has the comparative advantage in producing beef? Explain. **China because they have a lower opportunity cost. 1/4 < 1/2**
- Who has the comparative advantage in producing peppers? Explain. **France because they have a lower opportunity cost. 2 < 4**
- What would acceptable terms of trade be between China and France? **Possible terms of trade include 1 pepper for 3 beef**
- Is this an output problem or an input problem? **Input, the question is giving the amount hours required to produce a specific number of units**
- What is Mexico's opportunity cost of producing 1 plane? **2 Cars**
- What is Bolivia's opportunity cost of producing 1 car? **1/5 Plane**
- What is Mexico's opportunity cost of producing 1 car? **1/2 Plane**
- What is Bolivia's opportunity cost of producing 1 plane? **5 Cars**
- Who has the absolute advantage in producing cars? Explain. **Bolivia because they take fewer hours to produce a car. 5 hours < 6 hours**
- Who has the absolute advantage in producing planes? Explain. **Mexico because they take fewer hours to produce a plane. 12 hours < 25 hours**
- Who has the comparative advantage in producing cars? Explain. **Bolivia because they have a lower opportunity cost. 1/5 < 1/2**
- Who has the comparative advantage in producing planes? Explain. **Mexico because they have a lower opportunity cost. 2 < 5**
- What would acceptable terms of trade be between Mexico and Bolivia? **Possible terms of trade are 1 plane for 3 cars**