

## Trade - Absolute vs. Comparative Advantage

Someone (or country, organization, etc.) who is the best at doing something is said to have an **absolute advantage**.

A person (or country, organization, etc.) has a **comparative advantage** at producing something if they can produce it at the lowest opportunity cost (giving up the least).

So what's the difference and why is it important? Well, a country might be the best at making all kinds of things (absolute advantage), but by trying to do everything, they take away more time and resources from the most valuable thing they could be doing. On the flip side, a country might be bad at making almost everything, but still have a comparative advantage in doing what they're least bad at!

Comparative advantage is the whole basis for **trade and specialization**. Everyone is better off and you get more efficiency when people (or countries, etc.) focus on their comparative advantage and trade for the other things they want/need. The key to this efficiency is to not compare their absolute advantages, but to compare their opportunity costs.

For example, Steph Curry has an absolute advantage in basketball. But did you know [he's also great at organizing garages](#)? His neighbor, Josh, a 16 year old kid, is not as good at doing either. Now Steph could spend 2 hours organizing his own garage, but he'd give up the chance to make \$10 million making an Under Armour commercial. Josh takes 4 hours to organize the garage, but he'd only be giving up \$10 an hour working at McDonald's. So who should do what? Who's got the **absolute** advantage for basketball? How about garage organizing? Who's got the **comparative** advantage in basketball? Garage organizing?

So how would this relate to international trade? Should we even be manufacturing T-shirts in the U.S.? Is that the most valuable/efficient use of our resources? What else could those workers be doing instead? Considering that on average, it costs taxpayers \$145,000 to educate a child in the U.S. (from 1<sup>st</sup> to 12<sup>th</sup> grades), is standing over a sewing machine all day really the best use of our human capital?

That's the theory, but in reality, how many people who lost low-skilled factory jobs really ended up with a higher-skilled, better paying job?

Let's see how it works...

The U.S. can make 4 cars or 12,000 T-shirts per day. China can make 2 cars or 8,000 T-shirts per day.

	number of cars	number of t-shirts
US	4	12,000
China	2	8,000

Who has the **absolute** advantage for cars? \_\_\_\_\_ T-shirts? \_\_\_\_\_

What's the U.S.'s opportunity cost for making 4 cars? \_\_\_\_\_

What's China's opportunity cost for making 4 cars? \_\_\_\_\_

Who has the comparative advantage for cars? \_\_\_\_\_

What's the U.S.'s opportunity cost for making 24,000 t-shirts? \_\_\_\_\_

What's China's opportunity cost for making 24,000 t-shirts? \_\_\_\_\_

Who has the comparative advantage for t-shirts? \_\_\_\_\_

According to the law of comparative advantage, which country should produce which product?

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Assume cars are worth \$20,000 each and t-shirts are worth \$2 each. Fill in the dollar values based on the original chart

	Dollar value of cars	Dollar value of t-shirts
US		
China		

If both countries spend 1 day making each of the products for themselves (one day for cars and one day for t-shirts), what would be the total dollar value of cars and t-shirts produced by both countries after 2 days?

If both countries spend 2 days making the product for which they have a comparative advantage, what would be the total dollar value of cars and t-shirts produced by both countries after 2 days?

