

Write in the box the number of the question you are answering on this page as it is designated in the examination.

Question 2

- a) With equal amounts of resources, Luna can produce more machines, than Ashna (40 compared to 10), so it has an absolute advantage in producing machines.
- b) With equal amounts of resources, Luna can produce more food, than Ashna (40 <sup>tons</sup> compared to 30 <sup>tons</sup>), so it has an absolute advantage in producing <sup>food</sup> machines.
- c) In order to produce one extra machine, Luna has to sacrifice one ton of food, while Ashna would have to sacrifice 3 tons of food for the same goal. Therefore, Luna has lower opportunity costs in <sup>the</sup> production of machines than Ashna, so it has a comparative advantage in the production of machines.
- d) In order to produce one extra ton of food, Ashna has to sacrifice  $\frac{1}{3}$  of a machine, while Luna would have to sacrifice 1 machine for the same goal. Therefore, Luna has higher opportunity cost in the production of food than Ashna, so Ashna has a comparative advantage in the production of food. So Luna will import food when the two countries trade.
- e) The <sup>acceptable</sup> terms of trade lie between the two opportunity costs of the countries. In this case, these terms are: one machine should cost something between 1 ton and 3 tons of food (including the price of 1 ton per machine and 3 tons per machine). One example of terms of trade is: 1 machine costs 2 tons of food.