

University of Wisconsin - Madison
Econ 101 – Spring 2007
Professor Meta Brown

Homework 2

Due February 7th-9th, 2007

Please be sure to include (1) your name, (2) your teaching assistant's name, and (3) your section time on your answers. Please staple pages together. Also note that late homework will not be accepted.

1. Besaid Island produces two goods, bicycles and wheat. In the following table, different feasible production combinations are given for Besaid Island. Assume that Besaid Island's production possibility frontier is linear between combinations A to B, B to C, C to D and D to E.

Combination	Bicycles	Wheat
A	1,000	0
B	800	800
C	600	1,200
D	300	1,600
E	0	1,800

- a) Draw Besaid Island's production possibility frontier with bicycles on the vertical axis and wheat on the horizontal axis.
- b) If Besaid Island is currently producing at combination C, what is the opportunity cost of producing 400 more units of wheat?
- c) If Besaid Island is currently producing at combination D, what is the opportunity cost of producing 1 more bicycle?
- d) Give one example of a production combination that is feasible but not efficient.
- e) What is the difference between a straight-line production possibility frontier and a bowed-out production possibility frontier in terms of the opportunity cost?

2. Suppose America can either produce 30 units of grapes or 25 units of apples in one day. Suppose Mexico can produce 35 units of grapes or x units of apples in one day. For what values of x does Mexico have absolute advantage in apples? For what values of x does America have comparative advantage in apples?

3 Suppose Illinois has 1000 people and that it needs 5 people to produce a ton of grain or 10 people to produce a TV. Suppose Wisconsin has 2000 people and it needs 10 people to produce a ton of grain or 100 people to produce a TV.

a) Draw the PPF of both states.

b) Suppose each state needs only 150 tons of grain and has no use for more than 150 tons. If they don't trade, what is the most number of TVs that each state can produce?

c) Suppose each state needs only 150 tons of grain and has no use for more than 150 tons. If they do trade, what is the most number of TVs that the two states together can produce?

d) Which state has the absolute advantage in grain? in TVs? Which state has the comparative advantage in grain? in TVs?

e) Draw the combined PPF of the two states with trade.

4. Identify whether the following statements are normative (N) or positive (P).

a) Today, the stock market witnessed a significant rise in the Dow, NASDAQ and S&P 500.

b) What we need is a government that spends tax money wisely.

c) Currently the unemployment rate is about 4.7%.

d) The government should lower farm subsidies to ensure fair play in the international agricultural market.