

## Handout Glossary of Terms

1. **Comparative advantage:** The ability to produce [a good or service] at a lower cost compared to other producers, whether they are countries, firms, or individuals.<sup>1</sup>

To clarify the difference between **comparative advantage** and **absolute advantage**, an example can be helpful. If France and England both want wool and wine, which country should produce what? If France is more efficient at making both wine and wool than England, that does not mean that England should produce neither wine nor wool. If England can produce more wool than it can wine, it has a **comparative advantage** in wool production. France would have to give up more cases of wine to make wool than England since England is better at making wool than wine. Note that England has no **absolute advantage** but rather a **comparative advantage** in making wool. Thus, if France specializes in making wine and England in wool, the total output of wine and wool would be higher, so both countries would be better off trading these goods with each other.

2. **Absolute advantage:** The ability to produce a good or service at an “absolutely” lower cost, usually measured in units of labor or resource input required to produce one unit of the good.<sup>1</sup>
3. **Opportunity cost:** The highest-value, next-best alternative that must be sacrificed to attain something or to satisfy a want.<sup>1</sup>
4. **Specialization:** The division of productive activities among persons and regions so that no one individual or one area is totally self-sufficient.<sup>1</sup>
5. **Trade-offs:** Alternatives that must be given up when one is chosen rather than the other.<sup>2</sup>

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1. R. L. Miller, *Economics Today*, 8th ed. (HarperCollins College Publishers, 1994).

2. G.E. Clayton, *Economics: Principles and Practices* (Glencoe McGraw-Hill, 1999).