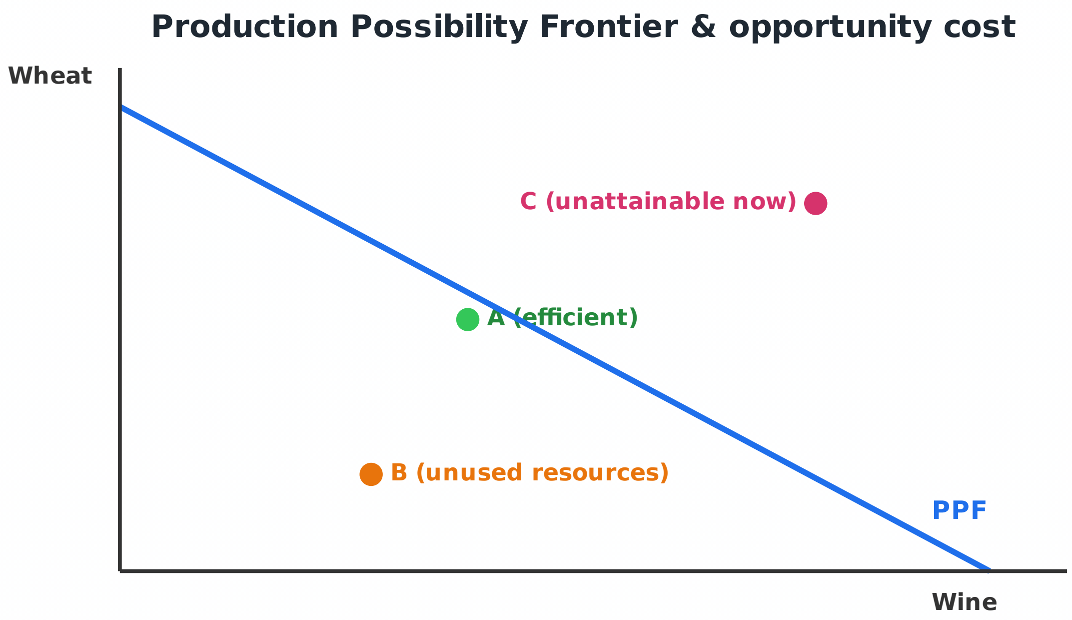
Unit 3 Diagram Bank — Must-Know Diagrams for the Exam

Every diagram you need for the Unit 3 examination, in one place. For each one: what it shows, how to draw it, and the single point examiners most want to see. Use this as your final-revision checklist — cover the caption and try to reproduce each diagram from memory.

1. Gains from trade (PPF)

The production possibility frontier shows the maximum combinations of two goods an economy can produce. Comparing two countries' PPFs reveals comparative advantage and the gains from specialising and trading.



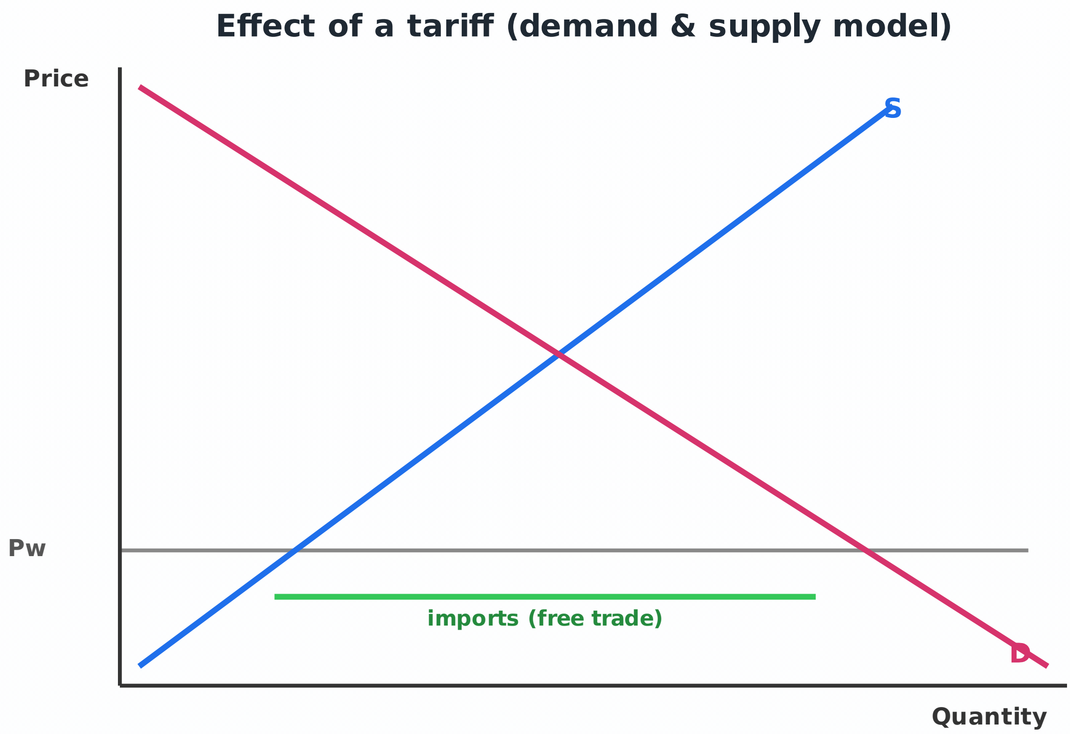
Moving along the PPF, more wine means less wheat — that trade-off is the opportunity cost.

Plot two goods on the axes; the straight or bowed frontier shows the trade-off. The country with the flatter trade-off (lower opportunity cost) in a good has the comparative advantage in it.

> **Watch for:** Label the opportunity cost (the slope) — comparative advantage is about opportunity cost, not who can produce more in total.

2. Tariff on the demand & supply model

A tariff raises the price of imports from the world price to the world price plus the tariff, lifting domestic production, cutting domestic consumption and shrinking imports.

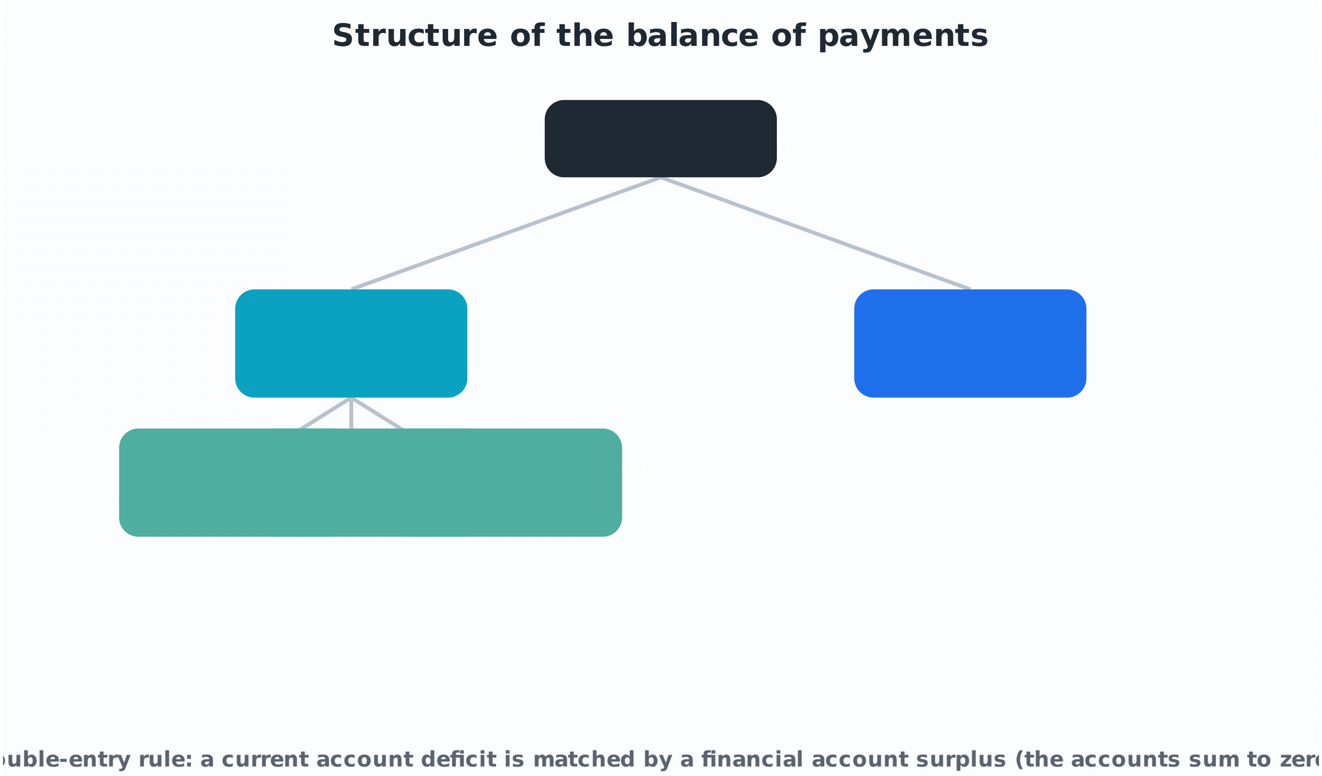


Draw domestic D and S, a horizontal world-price line, then a higher world-price-plus-tariff line. The import quantity is the gap between domestic demand and supply at each price.

> **Watch for:** Show the import bracket shrinking after the tariff, and be ready to identify who gains (domestic producers, government revenue) and who loses (consumers, efficiency).

3. Structure of the balance of payments

The balance of payments splits into the current account (trade balance plus primary and secondary income) and the capital and financial account, which mirror each other under the double-entry rule.

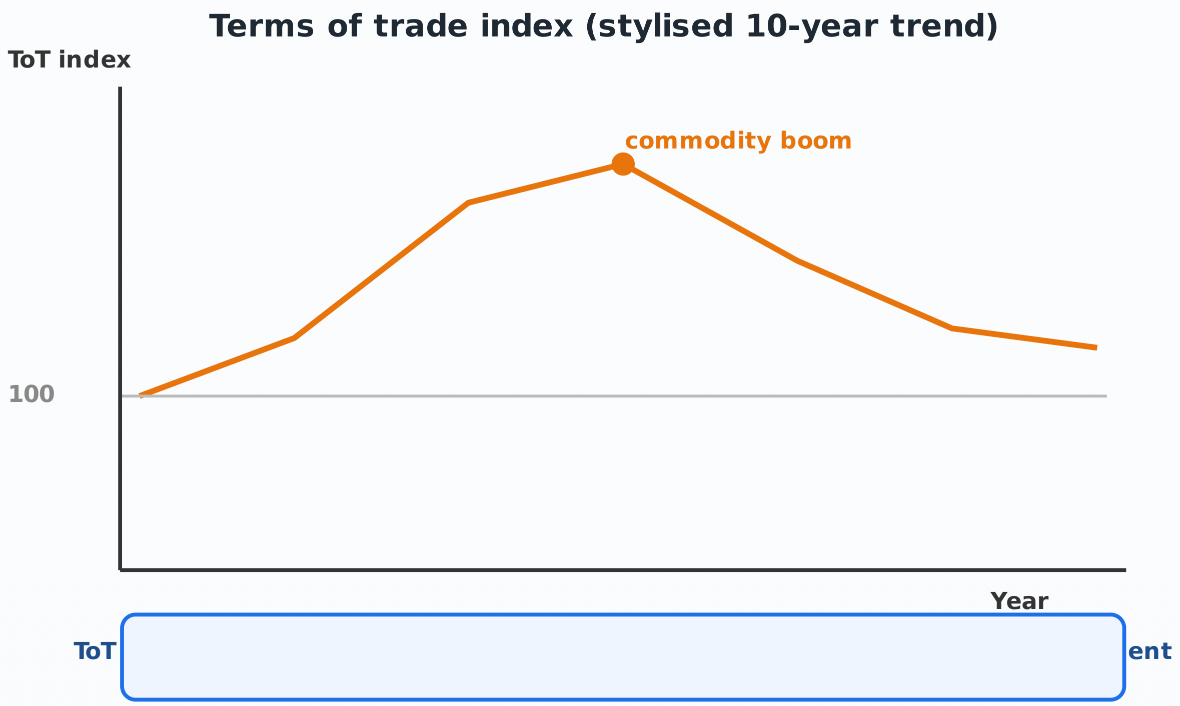


Draw the tree: BOP at the top branching into the current account and the capital & financial account, then break the current account into its components.

Watch for: State the double-entry rule explicitly — a current account deficit is matched by a financial account surplus; the two sum to zero (ignoring errors).

4. The terms of trade index

The terms of trade is an index of export prices relative to import prices, set to a base of 100. Commodity booms push it well above 100 and lift national income.

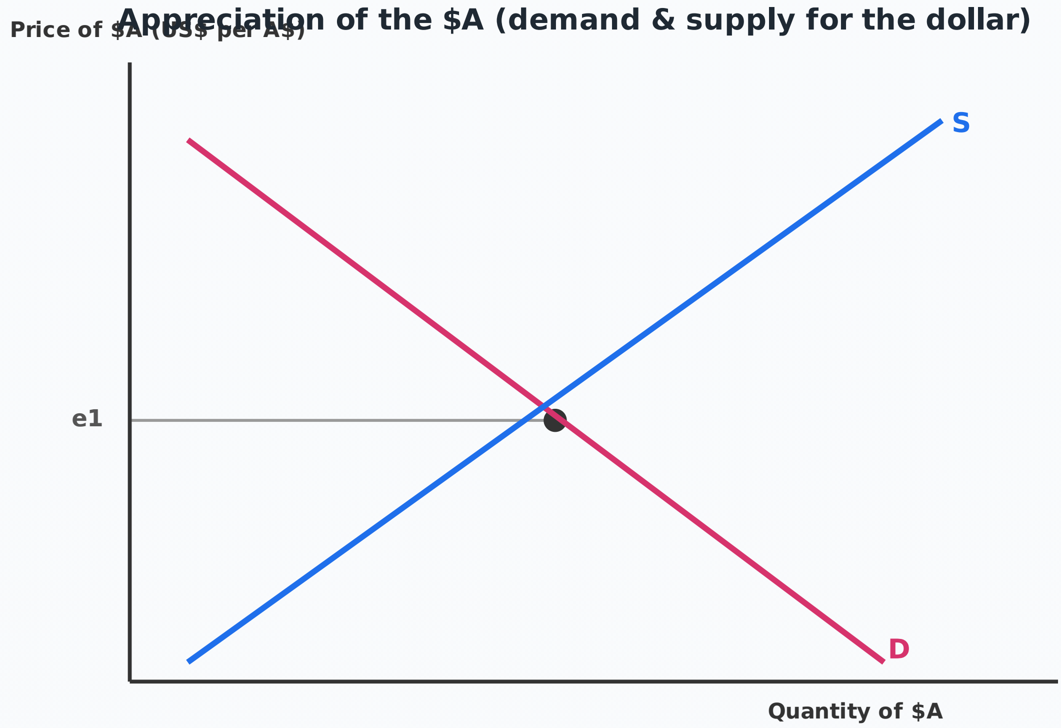


Plot the index over time against a base-100 line; mark the commodity-boom peak and recall the formula (export price index ÷ import price index × 100).

Watch for: Don't confuse the terms of trade (a price ratio) with the trade balance (a value). A rising terms of trade can occur even when the trade balance is in deficit.

5. Exchange-rate determination

The exchange rate is the price of the dollar, set where demand for $A meets supply of $A. A rise in demand (or fall in supply) appreciates the dollar; the reverse depreciates it.



Put the price of $A on the vertical axis and the quantity of $A on the horizontal. Shift the demand or supply curve and read off the new equilibrium exchange rate.

Watch for: Label the axes correctly (price of $A vertical, quantity of $A horizontal) — mislabelled axes are a frequent and avoidable loss of marks.

If you can reproduce these five diagrams from memory — correctly labelled, with the shift and new equilibrium marked — you are equipped for the diagram-dependent questions in the Unit 3 examination. Pair this bank with the data-interpretation and extended-answer technique guides for full exam coverage.