IGCSE ECONOMICS CIE SECTION 2 – THE ALLOCATION OF RESOURCES PRACTICE TEST (SAMPLE)

STUDY GUIDE

SAMPLE STUDY GUIDE WITH LIMITED QUESTIONS

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Introduction

Preparing for a certification exam can feel overwhelming, but with the right tools, it becomes an opportunity to build confidence, sharpen your skills, and move one step closer to your goals. At Examzify, we believe that effective exam preparation isn't just about memorization, it's about understanding the material, identifying knowledge gaps, and building the test-taking strategies that lead to success.

This guide was designed to help you do exactly that.

Whether you're preparing for a licensing exam, professional certification, or entry-level qualification, this book offers structured practice to reinforce key concepts. You'll find a wide range of multiple-choice questions, each followed by clear explanations to help you understand not just the right answer, but why it's correct.

The content in this guide is based on real-world exam objectives and aligned with the types of questions and topics commonly found on official tests. It's ideal for learners who want to:

- Practice answering questions under realistic conditions,
- Improve accuracy and speed,
- Review explanations to strengthen weak areas, and
- Approach the exam with greater confidence.

We recommend using this book not as a stand-alone study tool, but alongside other resources like flashcards, textbooks, or hands-on training. For best results, we recommend working through each question, reflecting on the explanation provided, and revisiting the topics that challenge you most.

Remember: successful test preparation isn't about getting every question right the first time, it's about learning from your mistakes and improving over time. Stay focused, trust the process, and know that every page you turn brings you closer to success.

Let's begin.

How to Use This Guide

This guide is designed to help you study more effectively and approach your exam with confidence. Whether you're reviewing for the first time or doing a final refresh, here's how to get the most out of your Examzify study guide:

1. Start with a Diagnostic Review

Skim through the questions to get a sense of what you know and what you need to focus on. Your goal is to identify knowledge gaps early.

2. Study in Short, Focused Sessions

Break your study time into manageable blocks (e.g. 30 – 45 minutes). Review a handful of questions, reflect on the explanations.

3. Learn from the Explanations

After answering a question, always read the explanation, even if you got it right. It reinforces key points, corrects misunderstandings, and teaches subtle distinctions between similar answers.

4. Track Your Progress

Use bookmarks or notes (if reading digitally) to mark difficult questions. Revisit these regularly and track improvements over time.

5. Simulate the Real Exam

Once you're comfortable, try taking a full set of questions without pausing. Set a timer and simulate test-day conditions to build confidence and time management skills.

6. Repeat and Review

Don't just study once, repetition builds retention. Re-attempt questions after a few days and revisit explanations to reinforce learning. Pair this guide with other Examzify tools like flashcards, and digital practice tests to strengthen your preparation across formats.

There's no single right way to study, but consistent, thoughtful effort always wins. Use this guide flexibly, adapt the tips above to fit your pace and learning style. You've got this!

Questions

1. **Which system relies on consumers to determine what is produced, with resources allocated by the price mechanism?**
   - A. Market Economic System
   - B. Mixed Economic System
   - C. Command Economy
   - D. Traditional Economy

2. **What term describes an agreement between two or more firms to sell a product at the same price?**
   - A. Price Discrimination
   - B. Price Fixing
   - C. Collusion
   - D. Market Sharing

3. **Which term describes an economy where private sector and public sector both play important roles?**
   - A. Market Economic System
   - B. Mixed Economic System
   - C. Command Economy
   - D. Traditional Economy

4. **Why might a market economy require government intervention to achieve allocative efficiency?**
   - A. Markets always allocate efficiently; no intervention needed
   - B. Markets can fail due to externalities, public goods, information gaps, and equity considerations; government can correct these
   - C. Government intervention worsens efficiency in all cases
   - D. Only monetary policy matters for efficiency

5. **Which policy instruments can correct a negative externality by raising private costs toward social costs?**
   - A. Taxes (Pigouvian tax) or regulation
   - B. Subsidies and deregulation
   - C. Price ceilings and non-price rationing
   - D. Tariffs and quotas

6. Which term describes goods that are detrimental to consumers and are often over-consumed?

A. Merit Goods

B. De-merit Goods

C. Public Goods

D. Normal Goods

7. A situation in which a good or service is produced at the lowest possible cost and full use of resources is called?

A. Productive Efficiency

B. Allocative Efficiency

C. Dynamic Efficiency

D. Free Rider

8. A price floor set above the equilibrium price leads to what outcome?

A. Surplus

B. Shortage

C. No effect

D. Equilibrium price

9. Which term best describes a good that is non-excludable but rivalrous, such as rival natural resources?

A. Pure public good

B. Private good

C. Common resource

D. Club good

10. Which term describes shifts in the demand curve caused by non-price factors such as tastes, income, and expectations?

A. Changes in Demand

B. Movements Along Demand Curve

C. Law of Demand

D. Elastic Demand

Answers

1. A
2. B
3. B
4. B
5. A
6. B
7. A
8. A
9. C
10. A

Explanations

1. Which system relies on consumers to determine what is produced, with resources allocated by the price mechanism?

A. Market Economic System

B. Mixed Economic System

C. Command Economy

D. Traditional Economy

The main concept here is how a market uses price signals and consumer demand to allocate resources. In a market economy, what gets produced is driven by what consumers are willing and able to buy. Prices reflect scarcity and value, so when demand for a product rises, prices go up and resources shift into its production; when demand falls, prices drop and production can move toward other goods. This price mechanism coordinates producers' decisions and keeps resources flowing toward where they're valued most, without central planning. The other systems don't rely on this voluntary, price-driven guidance: a command economy uses central planners to decide what to produce, a traditional economy follows long-standing customs, and a mixed economy blends market forces with some government intervention. So the described system is the market economy.

2. What term describes an agreement between two or more firms to sell a product at the same price?

A. Price Discrimination

B. Price Fixing

C. Collusion

D. Market Sharing

When competitors agree to set the same price for a product, they're engaging in price fixing. This is a direct attempt to remove price competition and keep prices at a level they choose together, rather than letting the market determine them. It can be done through explicit agreements or through informal understandings, and it's considered anti-competitive and illegal in many places because it harms consumers by keeping prices higher than they would be in a competitive market. Price discrimination, in contrast, involves charging different prices to different buyers based on willingness to pay, not agreeing on one shared price. Market sharing is about dividing up markets—such as by geography or customer type—so each firm sells in its own segment, which may involve different pricing strategies but is about allocation of markets, not fixing a single price across firms. Collusion is the broader idea of firms cooperating to influence outcomes, with price fixing being a specific form of collusion.

3. Which term describes an economy where private sector and public sector both play important roles?

A. Market Economic System

B. Mixed Economic System

C. Command Economy

D. Traditional Economy

Mixing private and public sectors describes an economy where both play important roles. In a mixed economy, most production and prices are driven by markets and private firms, but the government steps in to provide public goods and services (like defense, education, healthcare), regulate markets to prevent abuse, and redistribute income to improve fairness. This combination aims to keep efficiency from market forces while addressing what markets alone might miss, such as social welfare or environmental protection. The other systems rely almost entirely on one sector. A market economy centers on private decisions with little government intervention. A command economy is dominated by government planning and state ownership. A traditional economy follows longstanding customs and practices. Therefore, the system that fits the description of both private and public roles is the mixed economy.

4. Why might a market economy require government intervention to achieve allocative efficiency?

A. Markets always allocate efficiently; no intervention needed

B. Markets can fail due to externalities, public goods, information gaps, and equity considerations; government can correct these

C. Government intervention worsens efficiency in all cases

D. Only monetary policy matters for efficiency

Allocative efficiency means resources are used to produce the mix of goods and services that society values most, with prices guiding production to match consumer preferences. However markets don't always do this because of certain failures. Externalities occur when the actions of buyers or sellers affect others who aren't involved in the transaction. Negative externalities (like pollution) impose costs not reflected in market prices, leading to overproduction; positive externalities (like vaccination) create benefits not captured by prices, leading to underproduction. Government can correct these by taxes or regulation on negative externalities, or subsidies for activities with positive externalities, helping private costs and benefits align with social costs and benefits. Public goods, such as national defense or street lighting, are often underprovided in a free market because people can free-ride on others' contributions. Government provision ensures these goods are available. Information gaps can cause buyers or sellers to make choices that don't reflect true costs or quality, leading to misallocation. Regulations, standards, and information disclosures help everyone make better-informed decisions. Equity considerations address the fairness of outcomes. Some resource allocations that are efficient in a narrow sense may be viewed as unfair, so government redistribution can improve overall welfare and move the economy closer to a socially desirable allocation. Other choices ignore these market failures or assume government action always reduces efficiency, which isn't generally true and doesn't reflect how intervention can correct misallocations.

5. Which policy instruments can correct a negative externality by raising private costs toward social costs?

A. Taxes (Pigouvian tax) or regulation

B. Subsidies and deregulation

C. Price ceilings and non-price rationing

D. Tariffs and quotas

When a negative externality exists, social costs exceed private costs, so too much is produced from the viewpoint of society. The way to fix this is to raise the private cost per unit to match the social cost, nudging the market toward the socially efficient level. A Pigouvian tax does exactly that by charging a per-unit tax equal to the external cost. This makes producers face higher costs, reducing output until the private and social costs align. Regulation works similarly by imposing standards or limits that raise production costs, forcing behavior changes that lower output to the socially optimal point. Subsidies would decrease costs and encourage more production, making the externality worse. Price ceilings and non-price rationing affect pricing or allocation but don't specifically internalize the external cost. Tariffs and quotas influence trade and quantities but aren't targeted tools for aligning private costs with social costs in domestic markets.

6. Which term describes goods that are detrimental to consumers and are often over-consumed?

A. Merit Goods

B. De-merit Goods

C. Public Goods

D. Normal Goods

Some goods are considered harmful to health or welfare and are often consumed more than is socially desirable. These are de-merit goods. The idea is that individuals may not fully take into account the negative effects of consuming them, or they may be addicted, so consumption overshoots the socially optimal level. Governments frequently intervene with taxes or restrictions to curb use and reduce social costs, which is tied to the notion that these goods impose costs on society beyond the price paid by the buyer. Examples include tobacco, alcohol, and other unhealthy choices. By contrast, merit goods are benefits that people tend to underconsume because they don't fully recognize their value; public goods are things like national defense or clean air that markets typically fail to provide efficiently due to non-excludability and non-rivalry; normal goods are simply goods whose demand rises as income increases, not inherently harmful.

7. A situation in which a good or service is produced at the lowest possible cost and full use of resources is called?

A. Productive Efficiency

B. Allocative Efficiency

C. Dynamic Efficiency

D. Free Rider

Productive efficiency is about using resources in the most cost-effective way, with none of them wasted. When an economy or firm is producing at the lowest possible average cost for the given mix of outputs and all resources are fully employed, it's operating efficiently. This is why it sits on the production possibility frontier: you can't produce more of one good without giving up some of another, and you can't lower costs further without changing technology or inputs. Allocative efficiency, by contrast, would mean producing the right mix of goods that society values most. Dynamic efficiency looks at improvements over time and new technology. A free rider is someone who benefits from a public good without paying for it.

8. A price floor set above the equilibrium price leads to what outcome?

A. Surplus

B. Shortage

C. No effect

D. Equilibrium price

When a price floor is set above the market-clearing price, the higher price keeps the market above the level where buyers and sellers agree on quantity. At this higher price, producers want to supply more while buyers want to buy less, so the quantity supplied exceeds the quantity demanded. This creates a surplus of the good. For example, if the equilibrium price is 10 and the floor is 12, suppliers may offer more than buyers are willing to purchase at 12, producing extra units that sit unsold. This surplus would persist unless the government buys the excess or implements other measures to reduce supply or raise demand.

9. Which term best describes a good that is non-excludable but rivalrous, such as rival natural resources?

A. Pure public good

B. Private good

C. Common resource

D. Club good

The key idea is a good that cannot be easily kept out from others but whose use by one person reduces the amount available for everyone else. This describes a common resource: you can't easily exclude people from using a shared natural resource, but each use diminishes what others can use. Think of fish in a shared lake or grazing land—open access leads to overuse unless managed, a concept often called the tragedy of the commons. Pure public goods are non-excludable and non-rivalrous, so they don't fit because this resource is rivalrous. Private goods are excludable and rivalrous, so they're not non-excludable. Club goods are excludable and non-rivalrous up to a point, so they're also not non-excludable in the sense required here. Therefore, the term that best describes a good that is non-excludable but rivalrous is a common resource.

10. Which term describes shifts in the demand curve caused by non-price factors such as tastes, income, and expectations?

A. Changes in Demand

B. Movements Along Demand Curve

C. Law of Demand

D. Elastic Demand

Changes in demand describe the situation where the entire demand curve shifts to the left or right because of non-price factors like tastes, income, and expectations. When people's preferences rise for a product, or incomes increase, or they expect prices to rise in the future, they're willing to buy more at every price, so the curve moves to the right. If these factors reduce desired purchases, the curve shifts left. This is different from a movement along the demand curve, which occurs only when the price of the good itself changes—other things held constant. The law of demand explains the inverse price–quantity relationship but doesn't describe a shift of the curve. Elastic demand refers to how responsive quantity demanded is to price changes, not to shifting due to non-price factors. So the term for shifts caused by tastes, income, and expectations is changes in demand.

Next Steps

Congratulations on reaching the final section of this guide. You've taken a meaningful step toward passing your certification exam and advancing your career.

As you continue preparing, remember that consistent practice, review, and self-reflection are key to success. Make time to revisit difficult topics, simulate exam conditions, and track your progress along the way.

If you need help, have suggestions, or want to share feedback, we'd love to hear from you. Reach out to our team at hello@examzify.com.

Or visit your dedicated course page for more study tools and resources:

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We wish you the very best on your exam journey. You've got this!