

# Basic economic ideas and resource allocation (A Level)

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Multiple choice questions by topic [with answers](#)

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## Efficient resource allocation

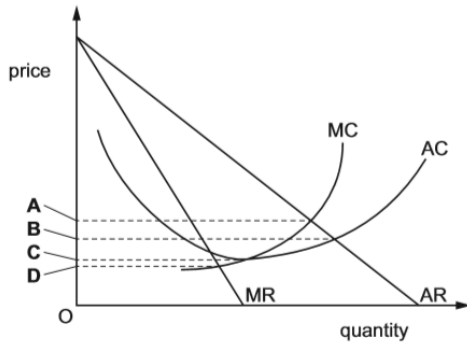
Which statement is correct?

- A** In a command economy firms compete and profit maximise allocating resources efficiently.
- B** In a command economy resources are privately owned.
- C** In a market economy prices are used to signal the value of individual resources.
- D** In a market economy resources are allocated by central planners.

Answer C

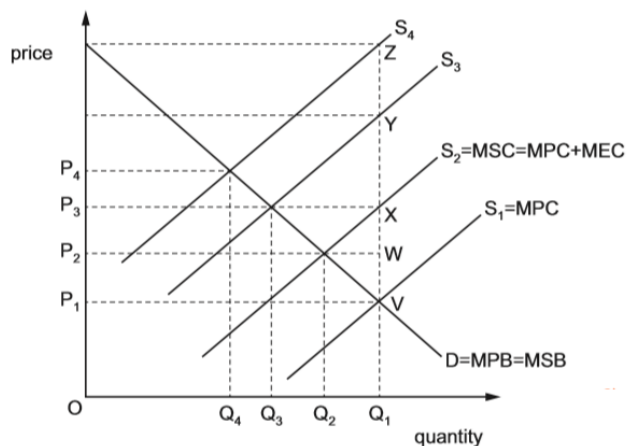
The diagram shows the cost and revenue curves for a firm.

At which price does allocative efficiency occur?



Answer A

The diagram shows the market for a good that creates a negative externality in production and no positive externalities. The current level of consumption is  $OQ_1$ .



The government decides to tax producers of the good.

Which size of tax on producers would result in a socially efficient allocation of resources?

- A** VW
- B** VX
- C** VY
- D** VZ

Answer B

In an economy, no one can be made better off without making someone else worse off.

What does **not** necessarily follow from this?

- A** The conditions for allocative efficiency have been met.
- B** The conditions for productive efficiency have been met.
- C** The distribution of income is socially acceptable.
- D** The economy is operating at a point on its production possibility curve.

Answer C

The current distribution of goods between two individuals in a two-person economy with given technology and resources is at point X.

According to the Pareto criterion, which point would definitely indicate increased allocative efficiency?



Answer B

The concept of allocative efficiency assumes that each individual in society is the best judge of their own economic welfare.

Which example of government intervention is based on an argument which rejects this assumption?

- A pollution controls
- B subsidies for merit goods
- C the provision of public goods
- D the regulation of monopolies

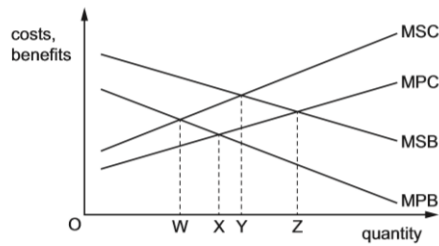
Answer B

What is the purpose of trying to achieve economic efficiency?

- A to achieve full employment
- B to achieve the cheapest possible price for products
- C to ensure resources are not wasted
- D to use as many resources as possible

Answer C

The diagram shows the market for a product, the production of which has both external costs and external benefits.



Answer C

What is the difference between the level of output that would be produced by the market and the socially optimum level?

- A WX      B WY      C XY      D XZ

Assuming there are no externalities, where would a nationalised firm set output to maximise social welfare?

- A where average revenue equals average cost  
B where average revenue equals marginal cost  
C where marginal revenue equals marginal cost  
D where marginal revenue is zero

Answer B

A project has a social cost of \$100 million, a private cost of \$40 million and an external benefit of \$20 million. Its net social value is zero.

What can be concluded about the project?

- A External cost is greater than external benefit.  
B Private cost is greater than external cost.  
C Private cost is greater than private benefit.  
D Social cost is greater than social benefit.

Answer A

Some multinational oil companies extracting oil in developing countries are now required to repair the damage they do to the environment.

Which best describes the total costs incurred by the oil companies in such circumstances?

- A external costs  
B private costs plus external costs  
C social costs plus external costs  
D social costs plus private costs

Answer B

A government decided to approve a road building scheme because it was socially beneficial. In making its decision it calculated private costs at \$800m, private benefits at \$800m and external costs at \$150m.

What **must** have been true about the external benefits of the scheme?

- A External benefits equalled private benefits.  
B External benefits exceeded external costs.  
C External benefits exceeded \$200m.  
D There were no external benefits.

Answer B

A proposal for a new power station was rejected by the government because it was not socially beneficial.

The government calculated that the private costs would be \$800m, private benefits \$900m and external benefits \$300m.

What must have been true about the external costs of the power station?

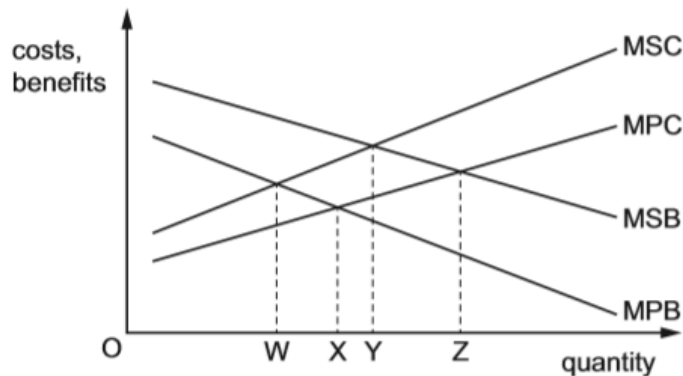
- A External costs were equal to external benefits.  
B External costs were greater than \$400m.  
C External costs were less than external benefits.  
D There were no external costs.

Answer B

## Externalities

The diagram shows the market for a product, the production of which has both external costs and external benefits.

## Market failure



Answer C

What is the difference between the level of output that would be produced by the market and the socially optimum level?

- A** WX      **B** WY      **C** XY      **D** XZ

Assuming there are no externalities, where would a nationalised firm set output to maximise social welfare?

- A** where average revenue equals average cost  
**B** where average revenue equals marginal cost  
**C** where marginal revenue equals marginal cost  
**D** where marginal revenue is zero

Answer B

A project has a social cost of \$100 million, a private cost of \$40 million and an external benefit of \$20 million. Its net social value is zero.

What can be concluded about the project?

- A** External cost is greater than external benefit.  
**B** Private cost is greater than external cost.  
**C** Private cost is greater than private benefit.  
**D** Social cost is greater than social benefit.

Answer A

Some multinational oil companies extracting oil in developing countries are now required to repair the damage they do to the environment.

Which best describes the total costs incurred by the oil companies in such circumstances?

- A** external costs  
**B** private costs plus external costs  
**C** social costs plus external costs  
**D** social costs plus private costs

Answer B

A government decided to approve a road building scheme because it was socially beneficial. In making its decision it calculated private costs at \$800m, private benefits at \$800m and external costs at \$150m.

What **must** have been true about the external benefits of the scheme?

A proposal for a new power station was rejected by the government because it was not socially beneficial.

The government calculated that the private costs would be \$800m, private benefits \$900m and external benefits \$300m.

What must have been true about the external costs of the power station?

- A External costs were equal to external benefits.
- B External costs were greater than \$400m.
- C External costs were less than external benefits.
- D There were no external costs.

Answer B

Cost benefit analysis

A government is considering improving the rail links in its country. It also has to choose one of four high-speed routes.

The benefits and costs of each route are shown below.

Which route should be chosen?

	private benefits \$bn	external benefits \$bn	private costs \$bn	external costs \$bn
A	14	20	0.4	0.1
B	16	22	1.6	0.4
C	18	12	0.2	1
D	20	18	2	4

Answer B

The government is considering building flood defences along a river. It has calculated the costs and benefits as follows.

	costs \$m	benefits \$m
private	450	260
external	60	190

According to cost-benefit analysis, which decision and reasoning about flood defences is correct?

	decision	reasoning
A	build	external benefits are greater than external costs
B	build	social benefits are greater than private benefits
C	do not build	private costs are greater than the external benefits
D	do not build	social costs are greater than the social benefits

Answer D