FACTFILE:
GCE BUSINESS STUDIES

UNIT A2 2: THE COMPETITIVE BUSINESS ENVIRONMENT
BUSINESS CYCLES

Learning Outcomes

Students should be able to:
- analyse and evaluate the impact of tbusiness cycles.

The Business Cycle

Definition:

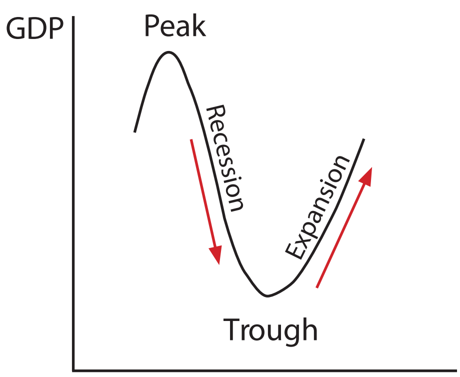
The Business Cycle (also known as the economic cycle) is a term describing the changes that occur in the level of real Gross Domestic Product (GDP) over time.

A business cycle is characterised by periods of expansion or recession.

A period of expansion is typically characterised by increases in levels of disposable income, industrial activity (output), and employment levels.

A period of recession is typically characterised by decreases in the above indicators. Throughout the cycle, a recession is measured from a peak to the trough (downturn), whereas growth in the economy occurs in the period between a trough and a peak (boom).

Figure 1: Business Cycle



Four Stages of the Business Cycle

The business cycle can be characterised in four aspects:

1. **Contraction** – a period when output decreases over time and levels of economic activity measured in terms of real GDP, declines (also called a downturn).
2. **Trough** – a period when the economy hits bottom, in terms of levels of economic activity

measured in terms of real GDP (also called depression or slump).

3. **Expansion** – a period when the economy starts growing again, and levels of economic activity, measured in terms of real GDP, increase (also known as recovery or upswing).

4. **Peak** – When the economy is over-heated, and levels of real GDP increases (also called a boom).

Effects of the business cycle on business:

These include:-

- Business Confidence – during periods of economic growth, management are more likely to be more confident about future business prospects. This may lead to increases in levels of investment, improved sales revenues and market share, increased levels of industrial output for many business organisations and increased levels of consumer spending. However, during periods of recession, business confidence tends to decrease, as does the amount spent on capital investment, consumer spending and employment levels are also likely to fall.

- Profitability – during periods of economic growth, business profitability levels are likely to increase (assuming costs are controlled). In this instance profits can be reinvested to fund future expansion of the business. However, in recessionary times, profits are likely to decline and cost reduction measures implemented in a business in order to maintain profits or reduce losses.

- Employment levels – during periods of economic growth, employment levels are likely to increase as business organisations employ additional staff. This in turn reduces levels of unemployment in the economy and the number of people claiming unemployment benefits. However, during a period of recession, business organisations are likely to implement redundancies, as a way of reducing staff numbers and associated costs. This has a knock-on effect of increasing unemployment levels in the economy.

- **Output levels** – during a period of economic growth, a business organisation may expand capacity in order to meet increased levels of demand. However, during a recessionary period, where levels of demand are likely to fall, a business will reduce levels of output in order to reduce costs and preserve profitability.

- **Other** – during a period of economic growth, greater levels of competition might arise through an increase in the number of business organisations that commence trading operations. This may be a reflection of increased consumer demand and/or opportunities for growth. However, during a period of recession, where output tends to stagnate, the number of businesses that fail or wind up, is likely to increase, as will the corresponding level of unemployment due to the lack of job opportunities.

Important functions of the management team in a business organisation is to understand, manage and anticipate the potential impact of the different phases of the business cycle and respond accordingly in order to ensure survival of the business.

SUMMARY

The Business Cycle (also known as the economic cycle) is a term describing the changes that occur in the level of real Gross Domestic Product (GDP) over time.

A business cycle is characterised by periods of expansion or recession.

There are typically four elements in a business cycle.

Issues such as business confidence, investment, employment levels and output levels will all be affected by periods of growth and/or decline in a business cycle.

REVISION QUESTIONS

1. Using a business with which you are familiar, explain what is meant by the term 'business cycle'.

2. With reference to the local (or UK) economy, explain each of the following terms:
   a. Peak.
   b. Growth.
   c. Decline.
   d. Trough.

3. Evaluate the impact of the business cycle on each of the following types of business:
   a. high-value motor car manufacturer, such as Rolls Royce or Jaguar;
   b. discount supermarket, selling essential products at basic price levels.

4. With reference to a business such as Mash Direct Limited (See Specimen Assessment Materials, A2 2, Examination Paper), evaluate the ways in which the business might respond to the various stages of the business cycle, as it participates in global trading activities.