



Cambridge Assessment
International Education

BUSINESS 9609

Cambridge international A Level



NEW ERA
international school

KEY TERMS:



Corporate social responsibility (CSR):

- the concept that accepts that business should consider society's interests in its activities and decisions.

Pressure group:

- organisations created by people with a common interest or aim which put pressure on businesses and governments to change policies to reach a pressure group objectives.

Environmental & Social audit:

- report assessing the impact of a business's activities on the environment and society.

KEY TERMS:



Information technology (IT):

- the use of electronic technology to gather, store, process and communicate information.

Computer aided design (CAD):

- using computers and IT to assist in the designing of products.

Computer aided manufacturing (CAM):

- using computers and computer controlled machinery to speed up production processes and make them more flexible.

Innovation:

- Creating more effective processes, products or way of doing things in a business.

UNIT 1. BUSINESS AND ITS ENVIRONMENT

CHAPTER 6. EXTERNAL INFLUENCES ON BUSINESS ACTIVITY



6.1 External influences on business activity continued

6.1.2 Economic

- how government might intervene to help businesses and encourage enterprise
- how government might intervene to constrain business activity
- how government might deal with market failure
- the key macroeconomic objectives of governments: low unemployment, low inflation, economic growth
- how macroeconomic objectives and performance of an economy can have an impact on business activity
- government policies used to achieve macroeconomic objectives: monetary, fiscal, supply-side and exchange rate policies
- the impact of changes in these government policies on business and business decisions

EXTERNAL ECONOMIC INFLUENCES ON BUSINESS BEHAVIOUR

Government economic objectives:

In practice, achieving all objectives at the same time is difficult. There are conflict:

- Rapid **economic growth** can help to reduce unemployment – but inflation might rise.
- Economic growth, by increasing peoples' living standards and their ability to buy imports, often leads to a Balance of Payments (Current Account) deficit.

9.1 Government economic objectives



Figure 9.1 Economic objectives of governments

EXTERNAL ECONOMIC INFLUENCES ON BUSINESS BEHAVIOUR

Also, the main economic objective might change over time:

- Rising prices caused by external factors could mean that the government prioritises the reduction of inflation not the reduction of unemployment.
- Negative economic growth (**recession**) could mean the government prioritises achievement of economic growth over greater equality of income and wealth.

9.1 Government economic objectives



Figure 9.1 Economic objectives of governments

ECONOMIC GROWTH – WHY IT IS CONSIDERED DESIRABLE

- It means that a country is becoming richer.
- It is measured by increase in gross domestic product (GDP).
- It is important to a country for several reasons:
 - Higher GDP => average living standards
 - Higher levels of output => employment => consumer incomes
 - More resources can be devoted to public sector (health, education...)
 - Poverty reduced, demand increase, tax income increase...



KEY TERMS:

Economic growth:

- ... an increase in a country's productive potential measured by an increase in real GDP.

Recession:

- ... a period of six months or more of declining real GDP.

Gross domestic Product (GDP):

- ... the total value of goods and services produced in a country in one year – real GDP has been adjusted for the effects of inflation.



9.2 Economic growth and the business cycle – impact on business strategy

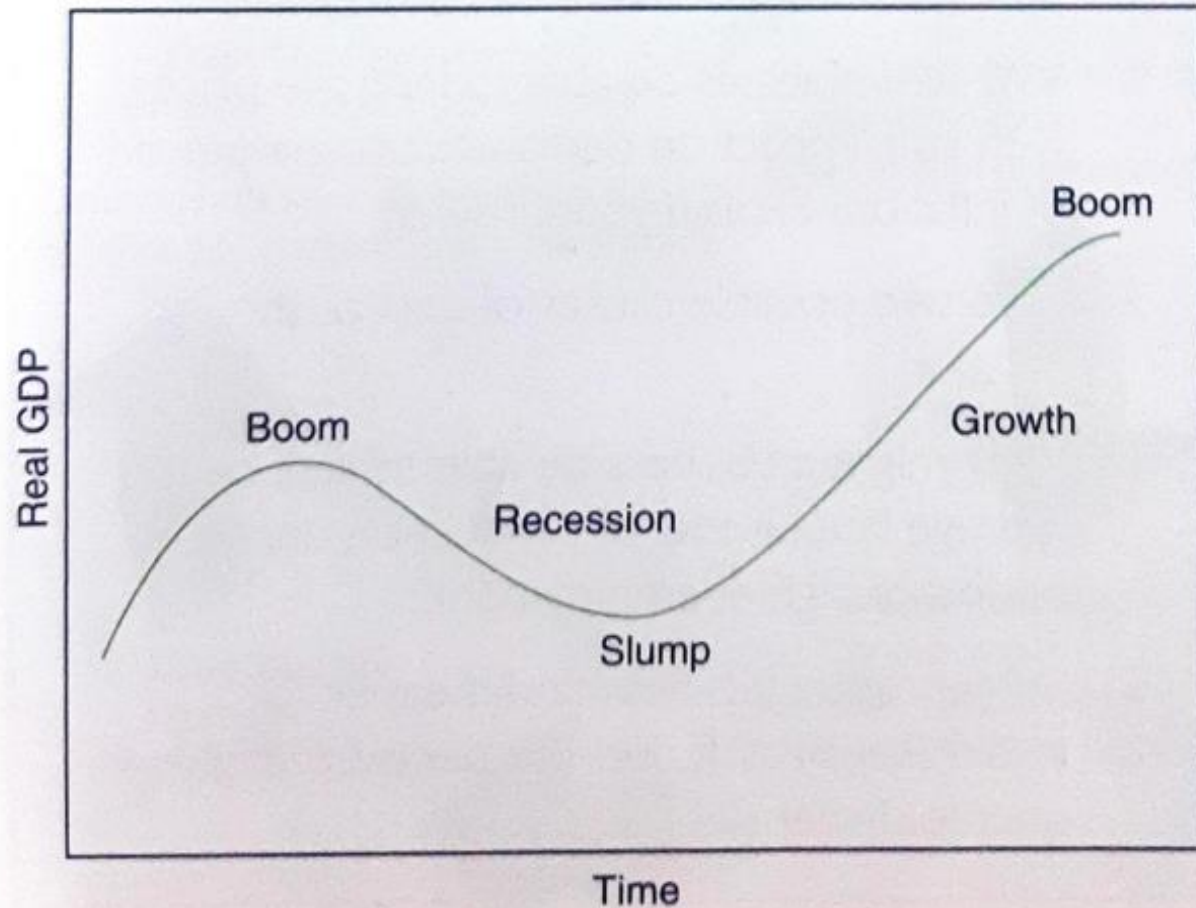


Figure 9.2 The stages of a typical business cycle

THE FACTORS THAT LEAD TO ECONOMIC GROWTH



Business (or economic) cycle:

... a regular swings in economic activity, measured by real GDP, that occur in economies varying from boom conditions to recession.

- Boom
- Downturn or recession
- Slump
- Recovery and growth

Stage of business cycle	Possible business strategies
Economic growth Average consumer incomes should be increasing	<ul style="list-style-type: none"> • Increase prices to take advantage of higher consumer demand – but will demand fall? • Develop new products that appeal to consumers with higher incomes – income elastic products but this could be an expensive strategy.
Recession Average consumer incomes likely to fall	<ul style="list-style-type: none"> • Lower prices as consumers have less to spend – but will perceived quality be lower? • Develop new products (perhaps 'inferior' goods) that appeal to consumers with lower incomes – but will this damage the brand image and existing consumer loyalty?

Table 9.1 How can businesses respond to swings in the business cycle?

PROGRESS CHECK



1. What does 'an increase in real GDP' mean?
2. What likely to happen to average incomes – or living standards – during a period of economic growth?
3. What would you expect to happen to the level of unemployment during a recession and why?

INFLATION AND UNEMPLOYMENT – IMPACT ON BUSINESS ACTIVITY



Inflation and unemployment – impact on business activity

- Causes of inflation
 - Demand pull inflation
 - Cost push inflation
- Causes of unemployment /cyclical, structural and frictional/

TERMS

Unemployment: exists when members of the working population are willing and able to work but are unable to find a job.

Cyclical unemployment: caused by low demand for products during recession stage of the business cycle.

Structural unemployment: caused by decline in important industries.

Frictional unemployment: caused by workers losing/leaving jobs and taking a long time to find others – perhaps because they have the 'wrong' skills.

IMPACT OF UNEMPLOYMENT ON BUSINESS



Negative impact:

- Reduces incomes of those unemployed – less to spend on products.
- May lead to increased taxes to pay welfare benefits – reducing retained profits (if corporation tax increased) or reducing consumer demand (if income tax increased).
- Unemployed workers lose skills and work incentives – reduces the quality of the labour force.

Positive impact:

- May encourage work incentive of those in employment to reduce chances of losing jobs.
- Increased supply of available labour may allow firms to offer reduced wages – or not to increase wages.
- Unemployed workers may be prepared to move to regions of country where there is labour shortage.

PROGRESS CHECK



1. Explain one reason why some unemployed workers might find it difficult to find a job during a period of economic growth.
2. Will all businesses be able to increase prices, with little impact on demand, during a period of inflation? Explain your answer.
3. Give two possible causes of cost push inflation.
4. Why might a business be able to reduce the average labour cost of production during a period of high unemployment?
5. Why might a business find it easier to retain (keep) staff during a period of high unemployment?

GOVERNMENT ECONOMIC POLICIES



Fiscal policy

... decisions about government spending, taxes and government borrowing.

Monetary policy

... decisions about the rate of interest and supply of money in the economy.

9.4 Government economic policies – how business strategy can adapt

Fiscal policy can be used to:

- raise revenue for government spending
- vary government spending levels, for example, on health and education
- boost spending on goods and services in the economy by using expansionary fiscal policy, for example, during a recession
- reduce demand for goods and services if inflation is a major problem
- cut the government's budget deficit if this is becoming too large.

Expansionary fiscal policy operates in the following way:

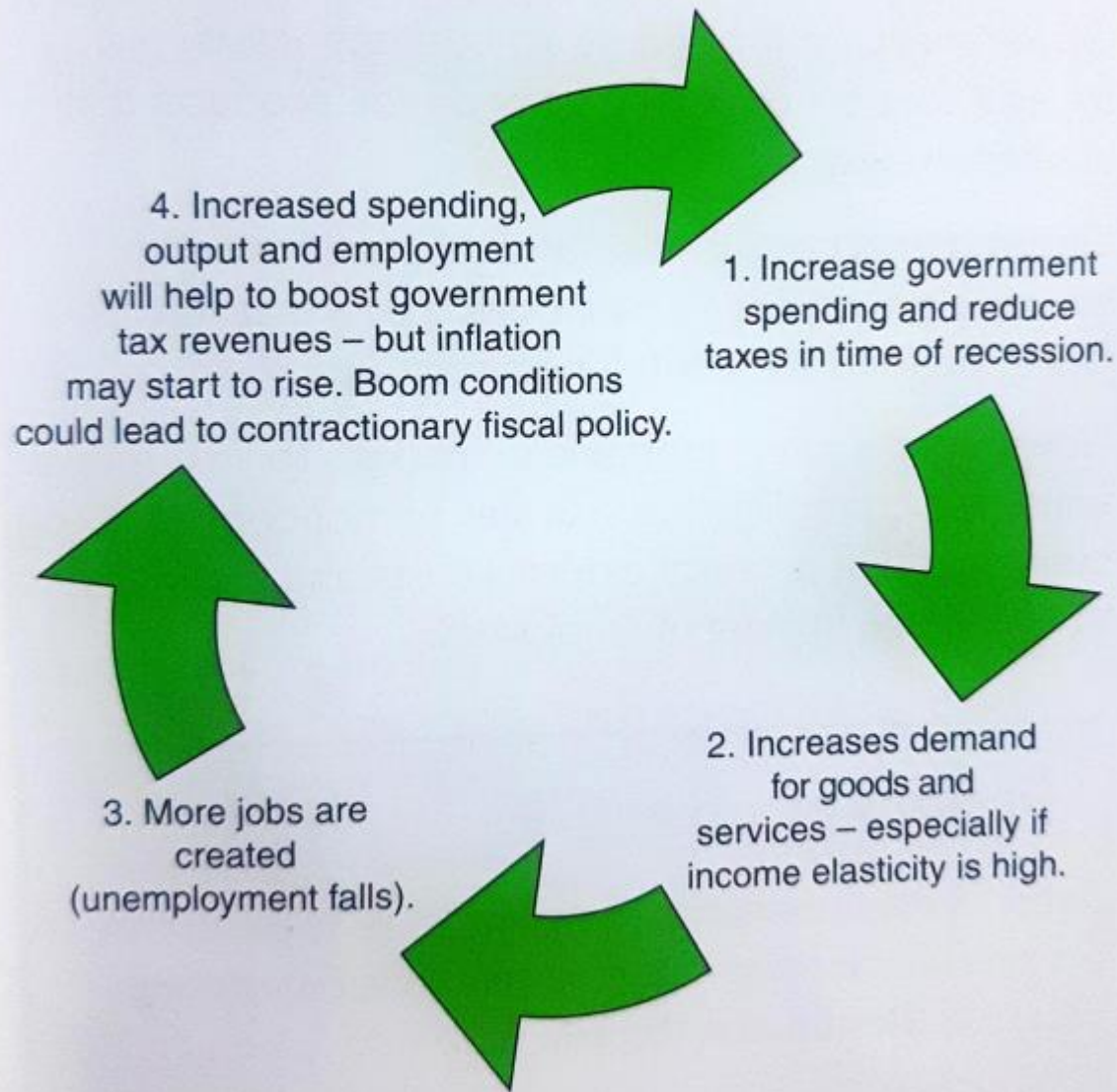


Figure 9.3 The impact of expansionary fiscal policy

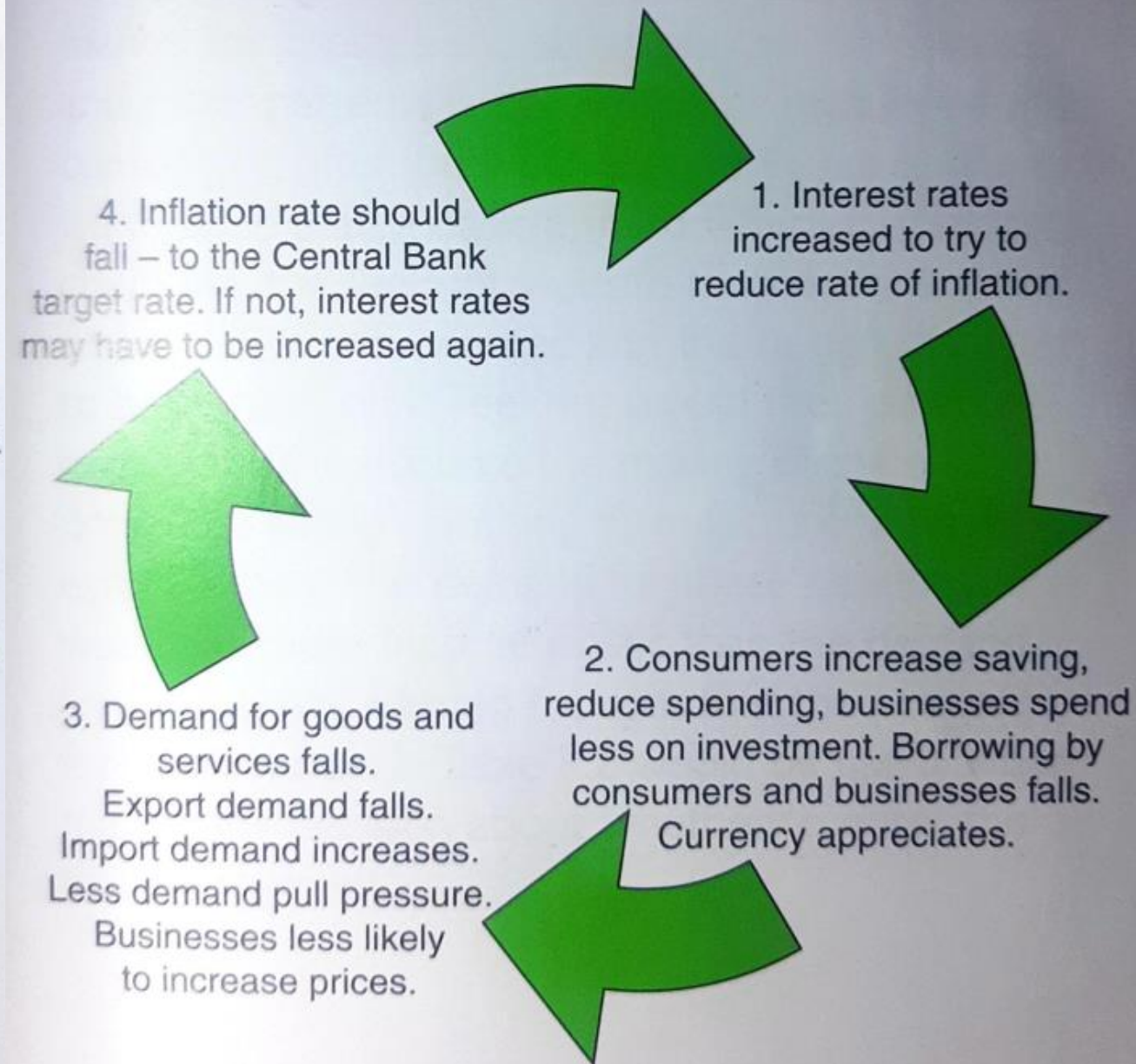


Figure 9.4 The impact of higher interest rates

Fiscal and Monetary Policy

Fiscal Policy Tools

Changes in government spending



Tax policy: Changes in tax rates and rules

Monetary Policy Tools

Open market operations Reserve requirement



Buy or sell



3% or 10% of demand deposits



Interest on required and excess reserves

Discount rate

PROGRESS CHECK



- What decisions might a government take if it planned to introduce an 'expansionary fiscal policy'?
- Why might the demand for some businesses' products be little affected by a reduction in income tax?
- How might an increase in a country's rate of corporation tax (on profits) affect a multinational company's plans to invest in the country?
- Which business is likely to be more affected by an increase in interest rates: a petrol retailing business or house construction business? Explain your answer.
- Under what economic circumstances is a central bank likely to increase interest rates?

EXCHANGE RATES – HOW BUSINESS ACTIVITY CAN BE AFFECTED



Impact of exchange rate appreciation

- Costs of imports fall – business may decide to import more materials/components from foreign suppliers; consumers may buy cheaper imported goods rather than those made domestically.
- Prices increase – this makes exports less competitive and foreign demand may fall.
- It would now be cheaper – than before the appreciation – for a domestically based business to locate in a foreign country.

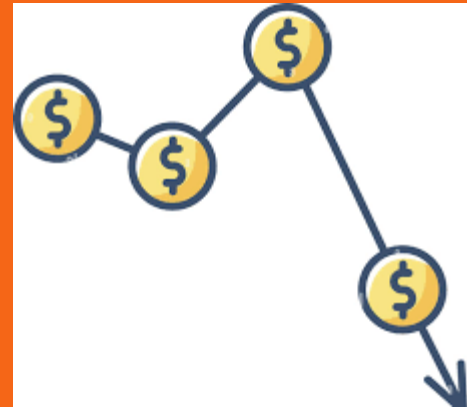


EXCHANGE RATES – HOW BUSINESS ACTIVITY CAN BE AFFECTED



Impact of exchange rate depreciation

- Costs of imports rise – domestically produced goods appear better value and demand for them might increase.
- Export prices fall – demand for exports might increase. Businesses may now be more likely to expand into foreign markets.
- It would now be cheaper – than before the depreciation – for foreign businesses to locate in the domestic country, creating more competition for local businesses.



KEY TERMS

- **Exchange rate:**
...price of a currency in terms of another.
- **Exchange rate appreciation:**
...rise in the value of a currency relative to other currencies.
- **Exchange rate depreciation:**
...fall in the value of a currency relative to other currencies.



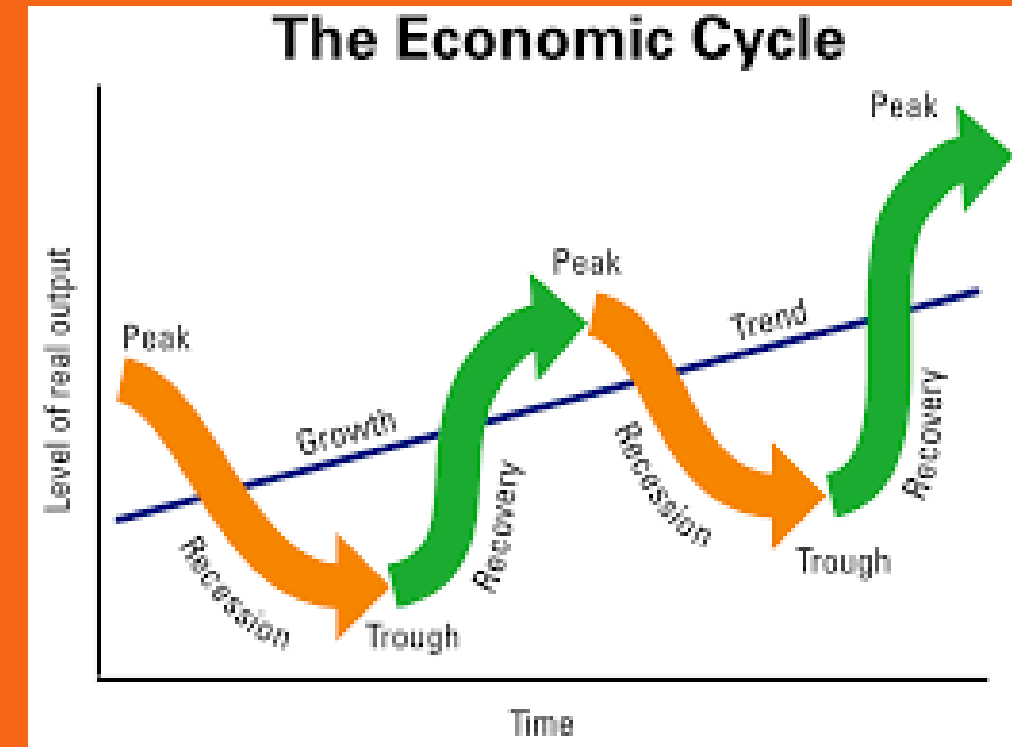
PROGRESS CHECK



- Give a numerical example of an exchange rate appreciation of your own country's currency.
- Give a numerical example of an exchange rate depreciation of your own country's currency.
- Explain why a business importing components and exporting completed products would **lose** and **gain** from a currency appreciation.
- Why might a business be encouraged to begin exporting following a depreciation of the currency?

FURTHER ECONOMIC ISSUES

- Governments limit or constrain business activity, e.g. by legal controls or placing a tax on the products that business makes.
- Governments can subsidize and support business activity, e.g. subsidies to businesses that are at risk of failing or grants to new business start-ups.
- Governments often intervene in markets to limit market failure, e.g. controlling the activities of monopolies; taxing businesses that produce external costs; and giving grants to encourage training of employees.



PROGRESS CHECK



- Give an example of a product in your country that the government either bans completely or tries to limit the sale of.
- Give one possible disadvantage of the government subsidizing a business that is at risk of falling.
- Give one reason why a government might provide financial support to businesses that train employees.