The Economic Cycle

THE ECONOMIC PROBLEM

- The flow of goods and services
  - The basic problem is limited resources and unlimited needs and wants
  - Goods and services
    - They must be produced
    - To produce them the factors of production are needed (Capital, Labour, Natural resources and Entrepreneurship)
    - The participants then partake in these goods and services

CONT.

- Participants are:
  - Households: they own all the factors of production and businesses require it from them
  - Businesses: they buy the factors of production that they require
  - Government: collect tax from the above which they use to satisfy our other needs and wants
  - Foreign Sector: imports and exports

Households

Government

Businesses

CONT.

- The market is therefore where all these interact within the economic cycle
- The economic cycle has a two-way flow of money and goods/services
- Businesses buy the factors of production that we own and we buy back the end results of the factors of production used by business

FACTORS OF PRODUCTION

Natural Resources	- Rent
Labour	- Salaries/Wages
Capital	- Interest
Entrepreneurship	- Profit

NATURAL RESOURCES

- Include all raw materials
- That are converted into finished products
- Natural Resources are limited and usually cant be replaced
- Resources differ from place to place
- Natural resources cant always be used in their natural state

EXAMPLES IN SA

- Minerals
- Forestry
- Agriculture
- Fishing
- Water

EXAMPLE PICTURES

Forestry

Mining

Agriculture

EXAMPLE PICTURES

Fishing

Water

LABOUR

- Definition: Labour includes all efforts mental and physical to create goods and services
- Characteristics:
  - Unskilled: usually have no formal education and illiterate
  - Semi-skilled: usually have limited education but perhaps have received on the job training
  - Skilled: usually have a formal education and are professionals of some sort

CAPITAL

- Definition: all resources used in the manufacture of goods or in the provision of services.

- Characteristics:
  - Used over a period of time
  - Goods (machinery/equipment) used to produce other goods
  - Capital is formed through savings and profits
  - Capital is initially supplied by the owner/(s)

ENTREPRENEURSHIP

- Definition: the combination of the other three factors by the owner (entrepreneur) in order to generate profit.

CHARACTERISTICS:

<u>following critical entrepreneurial qualities:</u>

- **Visionaries**
- **creative thinkers**
- **risk takers**
- **good leaders**
- **Independent**
- **perseverance and commitment.**
- **opportunists**
- They are individuals who either had the necessary **expertise, knowledge and skills to make the business a success, or** the **ability to recognise their shortcomings and then hire the right people to fill the gaps.**

ENTREPRENEURS

Richard Branson

Donald Trump

Mark Shuttleworth

THE FOREIGN SECTOR

- International trade refers to trade between countries
- Very few countries (if any) are self sufficient
- Many sectors rely heavily on foreign trade
- If this sector were to collapse the SA economy could also be crushed

REASONS FOR INTERNATIONAL TRADE

- Natural resources are unevenly distributed
  - Natural resources vary from country to country
  - And it is important to obtain these resources
- Climate differs in different regions
  - Climate impacts on agriculture
  - As certain products require different conditions
- Labour specialisation
  - Over time certain countries have become specialists in certain products

CONT.

- Preferences, wants and needs
- Income
  - The higher ones income the more they want
  - If the local market can not satisfy these needs imports are required
- Improved transport and communications
  - People can now come into contact with foreign products more easily
  - With the ability to communicate with anyone in the world, markets must be able satisfy our needs

POTENTIAL PROBLEMS

- Different countries have different currencies
- Laws and customs differ between countries
- Restrictions on foreign trade
- Capital flow
  - Easier when it happens in one country
  - Than between two different countries
- Granting credit between different countries
- Cultural differences between countries
- Distance between countries

EXCHANGE RATES AND CURRENCIES

- It is the price of one currency expressed in the terms of another
- Exchange rates become very important when dealing with foreign trade
- When goods are imported Rands must be exchanged to pay for those products/services
- Currencies of the world (Page 33)

IMPORTS AND EXPORTS

- Imports refer to SA business buying goods from another country to sell in SA
- Exports refer to SA business selling goods to other countries so they can sell and use those items in their economy
  - Demand and supply determines the price
  - The price of currencies is known as exchange rates
  - Currencies are bought and sold on Forex Market
  - SA has a floating economy (i.e. determined by supply and demand)

CONT.

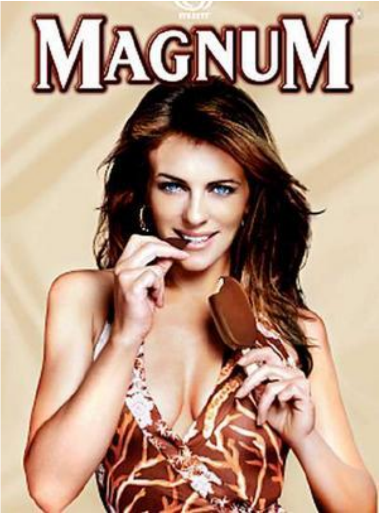
- Imports generate a sale of our currency (supply)
- Exports generate a purchase of our currency (demand)

DEMAND, SUPPLY AND PRICES

- Demand: it is not the same as a need or desire. We may need or want a product but that doesn't mean we can afford it.
- Thus demand is:
  - The need for a product
  - The ability to afford it
  - The willingness to pay
- Demand is always price related (a specific volume of demand at a specific price at a specific point in time)

RATIO BETWEEN DEMAND AND PRICE

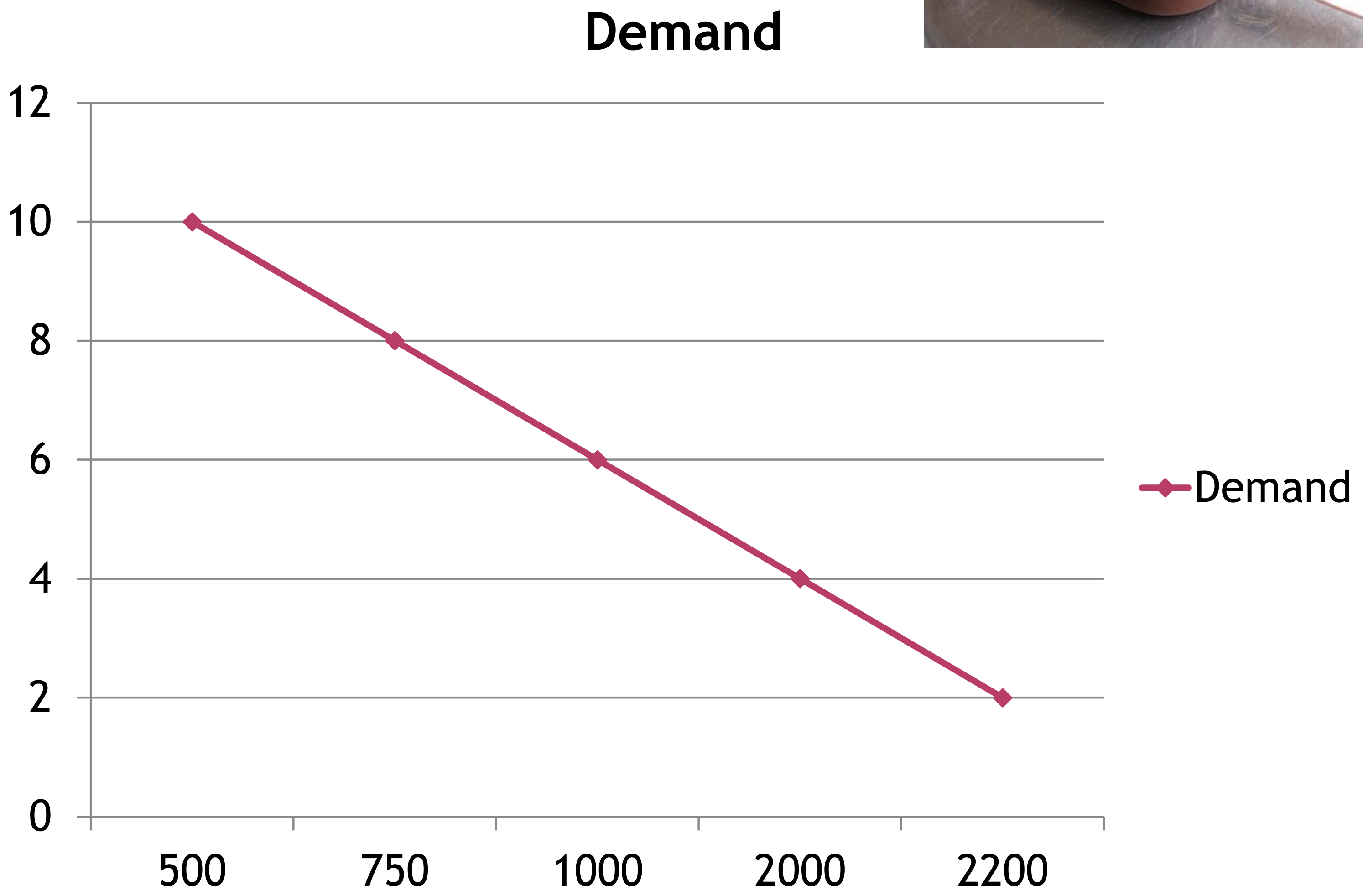
- Use the information below to the demand curve



Price per ice cream	Quantity demanded	Total
R10	500	R5 000
R8	750	R6 000
R6	1000	R6 000
R4	2000	R8 000
R2	2200	R4 400

CONT.


HOLANDA
MAGNUM
Classic
Cont. Net.
115 ml (91 g)


Demand
12
10
8
6
4
2
0
500
750
1000
2000
2200
Demand

CONT.

- The demand for a particular product is in direct correlation with the price
- Substitute products will change the outcome of the demand for the original product plotted
  - Example if we just plotted Magnum Ice Cream and the price for other Ola' ice cream drops the Magnum graph will change (i.e. demand for Magnum will drop and vice versa)
- Complementary products also change the outcome of the demand
  - Example if the price of ice lollys decrease the demand for ice creams decrease and vice versa

DEMAND CAN ALSO BE INFLUENCED BY

- Change in tastes and habits
- Changes in income
- Business Cycle (economic climate like recession)
- Volume of money in circulation
- Tax
- Changes in population

SUPPLY

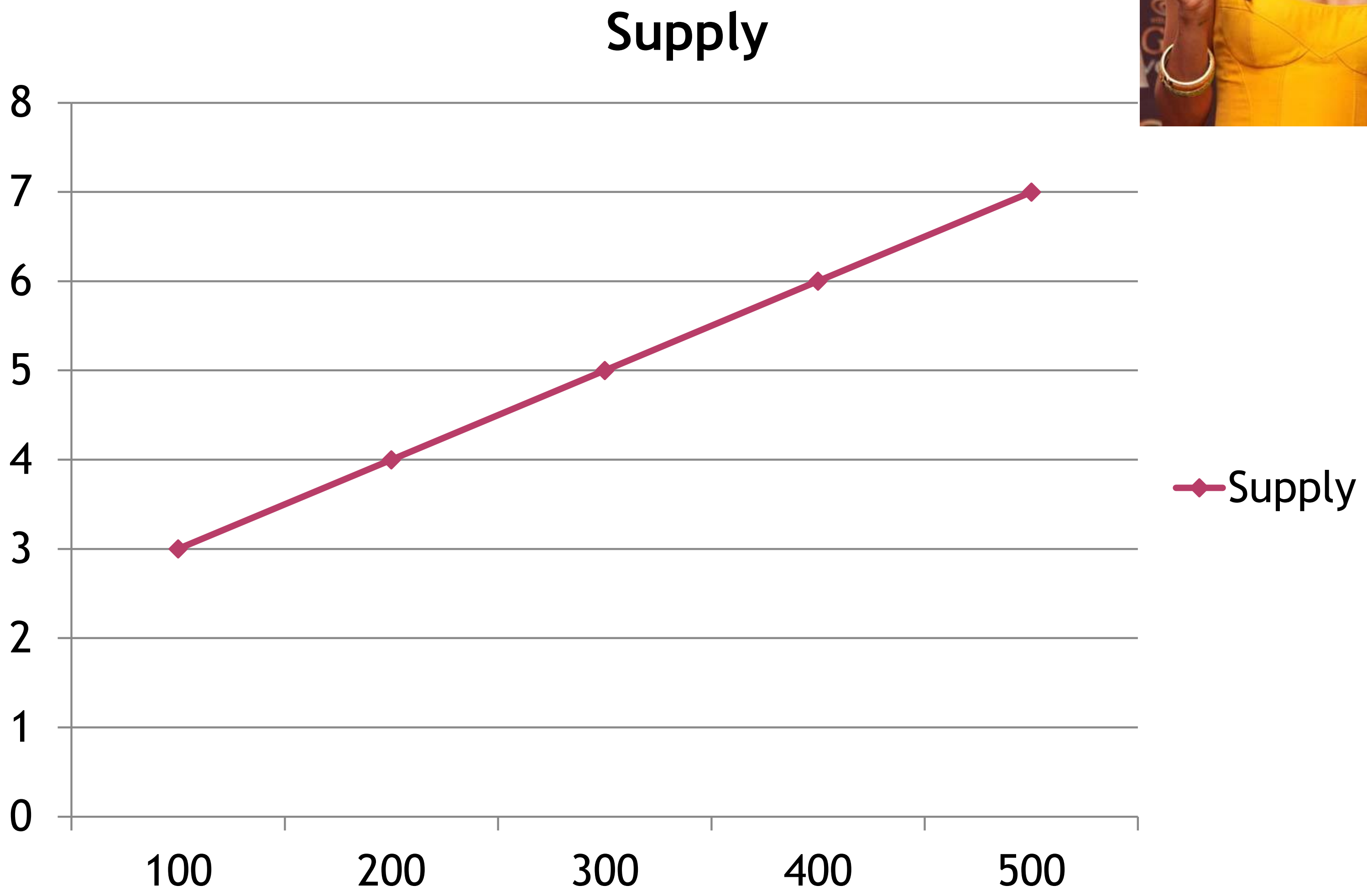
- Supply: refers to the quantity that the supplier is prepared to offer at a given point in time at a given price
- Supply only refers quantity of stock that is offered for sale

SUPPLY TABLE, CURVE AND LAW OF SUPPLY

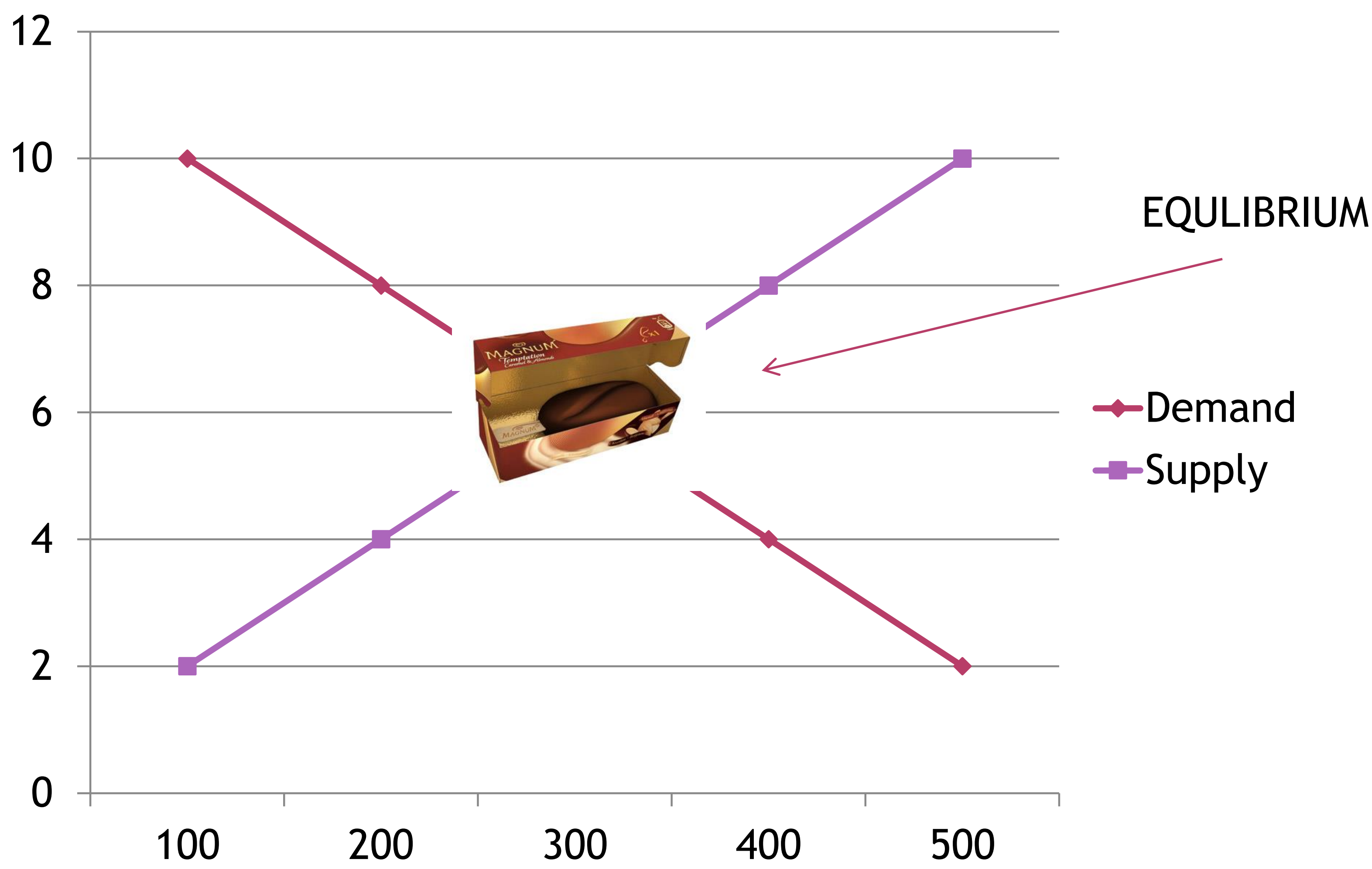
- Sellers always strive to sell at the highest price
- The higher the price the more goods supplier will be willing to supply

Price per unit of ice cream	Quantity offered
R3	100
R4	200
R5	300
R6	400
R7	500

CONT.



COMPLETION OF A DEMAND AND SUPPLY GRAPH



EXPLANATION

- Now that you have drawn the demand and supply curve you will notice that:
  - Demand is indirectly proportional to price
  - Supply is directly proportional to price
  - The point at which the two graphs meet is known as the EQUILIBRIUM
  - This is where suppliers and consumers are willing to meet each other
  - In this example the acceptable price would be R6 for an ice cream and 300 of them will be supplied

THE EXCHANGE OF GOODS AND SERVICES

- In an open economy, goods and services are imported from and exported to other countries
- Definition of a market;
  - Any place where buyers and sellers
    - Exchange information
    - Determine prices
    - Determine the quantity to be exchanged
- The economic thus involves a continuous two way flow of money and goods and services

DEFINITION OF PRICE

- It is the monetary value of a product
- The consumer wants to pay as little as possible
- The higher the demand for a product or service, the higher the price

INFLATION

- Definition: the continuous rise in prices in general terms
- Measuring inflation (CPI)
  - CPI: Consumer Price Index
  - Used to measure the average cost of an average shopping basket of goods
  - In South Africa
  - About 1500 regular shopping items and services
  - Grouped into 40 categories

CONT.

- Once the survey is complete on these goods
- The rate is calculated for CPI
- Done by working out the percentage change from one period to the next
- I.E. if the inflation rate is 12% that means the average increase of all goods would be 12 %
- Once every 5 years the data for the CPI is set as the “base year” for the next 5 years

- Discussion on how certain issues can lead to inflation
  - Unemployment
  - Lower interest rates
  - An increase in salaries and wages
  - Importing goods

CONSEQUENCES OF INFLATION

- Money is used to express the value of goods and services, if its value drops it creates negative feelings in the economy
- Peoples standard of living may decrease if salaries don’t keep up with inflation
- If the value of our money depreciates faster than those countries around us that we trade with imports decrease but exports increase