

# ***THE ECONOMIC ENVIRONMENT***



# What is the Economic Environment?

- *...refers to all those economic factors which have a bearing on the functioning of a business unit*
- ...also consists of factors that affect consumer purchasing power and spending patterns
- also depends on the economic environment to sell the finished goods

# The Economic Environment cont/d..

- We will focus on the following economic factors
- Economic system
- Economic conditions (such as interest rates, inflation, unemployment, etc.)
- Economic policies
- Market structures

# The Economic Systems

- Each country faces the problem of sharing resources equitably
- The problem arises because of scarcity of resources
- Three fundamental questions come up:
  - *What is to be produced?*
  - *How are these goods to be produced? and*
  - *For whom are the goods to be produced?*

# The Goals of an Economic System

- *Stability* - a condition in which the balance between money available and goods produced remains about the same
- *Full employment* – ensures all those who want to work have jobs.
- *Growth* – is an increase in the quantity of goods and services produced by our resources.

# Types of Economic Systems

- The common ones are:
- *Market / Capitalist*
- *Command / Planned and*
- *Mixed*

# Market / Capitalist Economic Sys.

- ...individuals control all or most factors of production and make all or most production decisions
- ...there is little Government intervention
- ...markets decide what, when, and for whom to produce

# Market / Capitalist Economic Sys.

- ...individuals control all or most factors of production and make all or most production decisions
- ...there is little Government intervention
- ...markets decide what, when, and for whom to produce



# Market / Capitalist Economic Sys.

## ❑ Advantages

- Freedom of choice
- Encourages competition
- encourages professionalism
- Speedy decision making

## ❑ Disadvantages

- Market forces if not controlled can cause hardships
- Profit motive can lead to harm
- Disregards public goods
- Gap between rich and poor widens

# Command / Planned Economic Sys.

- The government controls all or most factors of production and makes all or most production decisions
- Two types are common: Communist and Socialist systems
- *Communist* - all industries owned and run by central government
- *Socialist* - main industries run by government while less crucial ones by individuals

# Command/Planned Economic Sys.

## ❑ Advantages

- provision of social services
- equitable distribution of resources
- resource utilization is planned and achieved for society
- avoids emergency of monopolies

## ❑ Disadvantages

- High inefficiencies in operation
- positions are filled by political appointments
- bureaucratic procedures common and hence delay in making decisions
- high taxes because of emphasis on public goods

# Mixed Economic Systems

- In most cases it is rare to have on type of system
- Mixed economic systems combine elements of command and market economies
- Most economies have mixed economic systems
- What about Zambia?

# *Economic Conditions*

- Economic conditions or factors that can affect businesses include:
- *Inflation* - a persistent increase in prices of goods and services. Leads to an increase in costs and prices
- *Income* - money available for spending after the major deductions (e.g. taxes and other deductions). Affects purchase behavior (and hence firm's sales)
- *Exchange Rate* - rate at which the national currency can be exchanged for other currencies (e.g. \$ 1 = ZMW 9.8418). Dictates the prices of imported raw materials

## *Economic Conditions cont/d...*

- *Interest Rates* - the cost of borrowing money, hence affects the costs of a business
- *Unemployment Levels* - occurs when someone actively searching for work is unable to find it. Affects the spending power of individuals (hence firm sales)

# Market Structures

- ...or the degree of competition is also an important consideration as it affects prices, resource use, profit levels and efficiency
- Common types are:
- *Perfect Competition* - characterized by a very large number of small firms producing an identical product. Firms are price takers.
- *Monopolistic Competition* – characterized by many sellers of slightly differentiated products
- *Oligopoly* - characterized by a small number of very large firms that have the power to influence the price
- *Monopoly* - exists when an industry or market has only one producer. Firm is price maker.

# *Government Monetary and Fiscal Policies*

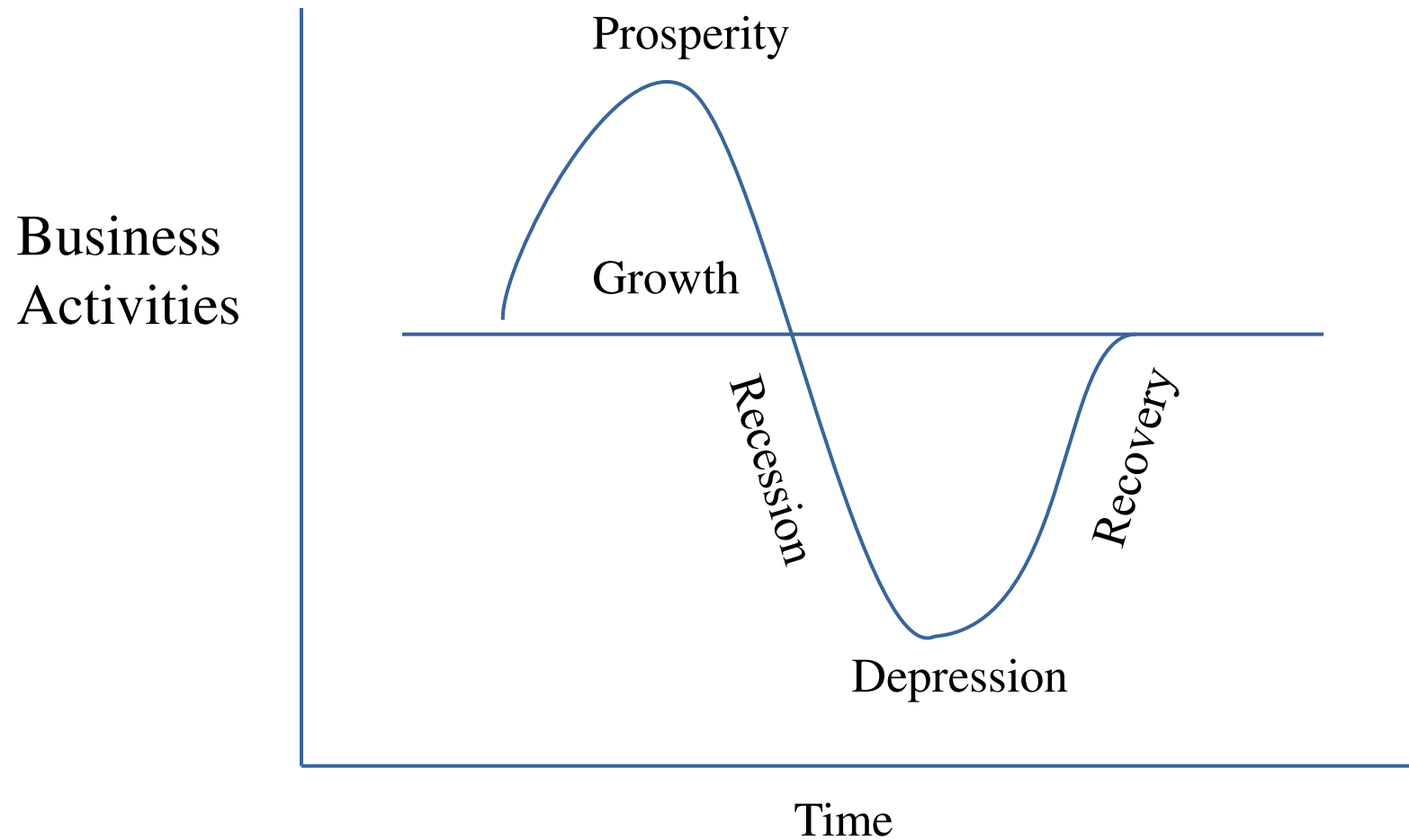
- The government also affects the economy by the deliberate policies that it comes up with
- *Monetary Policy* - government attempts to influence economic activity by influencing money supply using interest rates
- *Fiscal Policy* - entails the use of government expenditure and taxation to control the economy



# *Economic Cycles*

- ...refer to the general trends that occur in the economy leading to certain patterns that have an effect on business
- Phases involved are as follows:
- *Prosperity*
- *Recession*
- *Depression* and
- *Recovery*

# *Economic Cycles cont/d...*



# Questions ???

