



Success is the sum of small efforts, repeated day in and day out.

Robert Collier

Test Yourself - Business Cycles and Unemployment



What is a business cycle?



A business cycle is alternating periods of economic growth and contraction, which can be measured by changes in real GDP.





What are the four phases of a business cycle?

The four phases of a business cycle are:



- ✘ **Peak** - the phase of the business cycle during which real GDP reaches its maximum after rising during a recovery
- ✘ **Recession** - a downturn in the business cycle during which real GDP declines
- ✘ **Trough** - the phase of the business cycle in which real GDP reaches its minimum after falling during a recession
- ✘ **Recovery** - an upturn in the business cycle during which real GDP rises



What is economic growth?



Economic growth is an expansion in national output measured by the annual percentage increase in a nation's real GDP.



Why is growth an economic goal?



Growth is an economic goal because it increases our standard of living ... it creates a bigger “economic pie.”



**How long before a downturn is a
recession?**



A recession is defined as at least two consecutive quarters in which GDP declines.



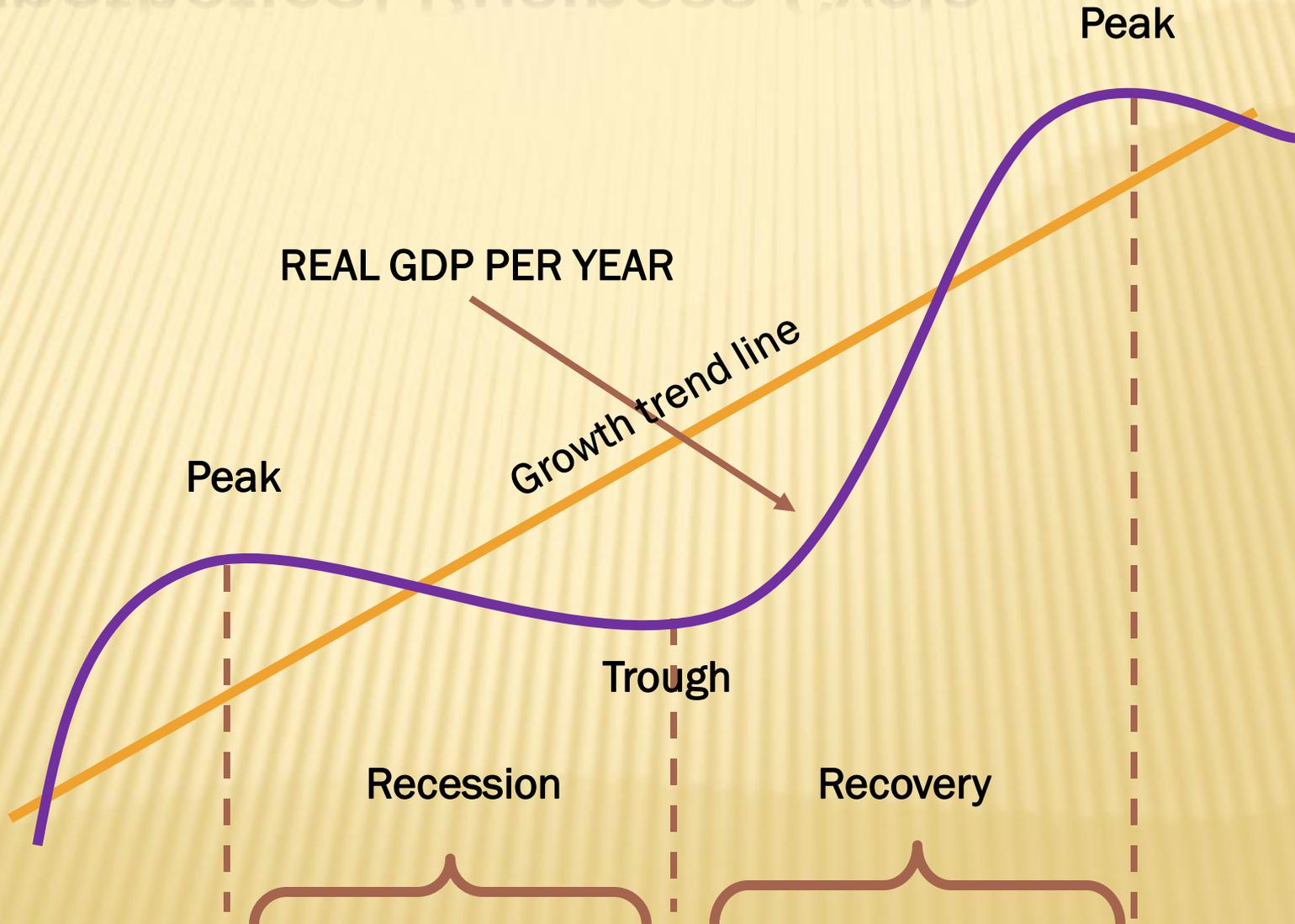
When is a downturn considered a depression?



The term **depression** is primarily an historical reference to the extreme deep and long recession of the early 1930s and currently has no definition.

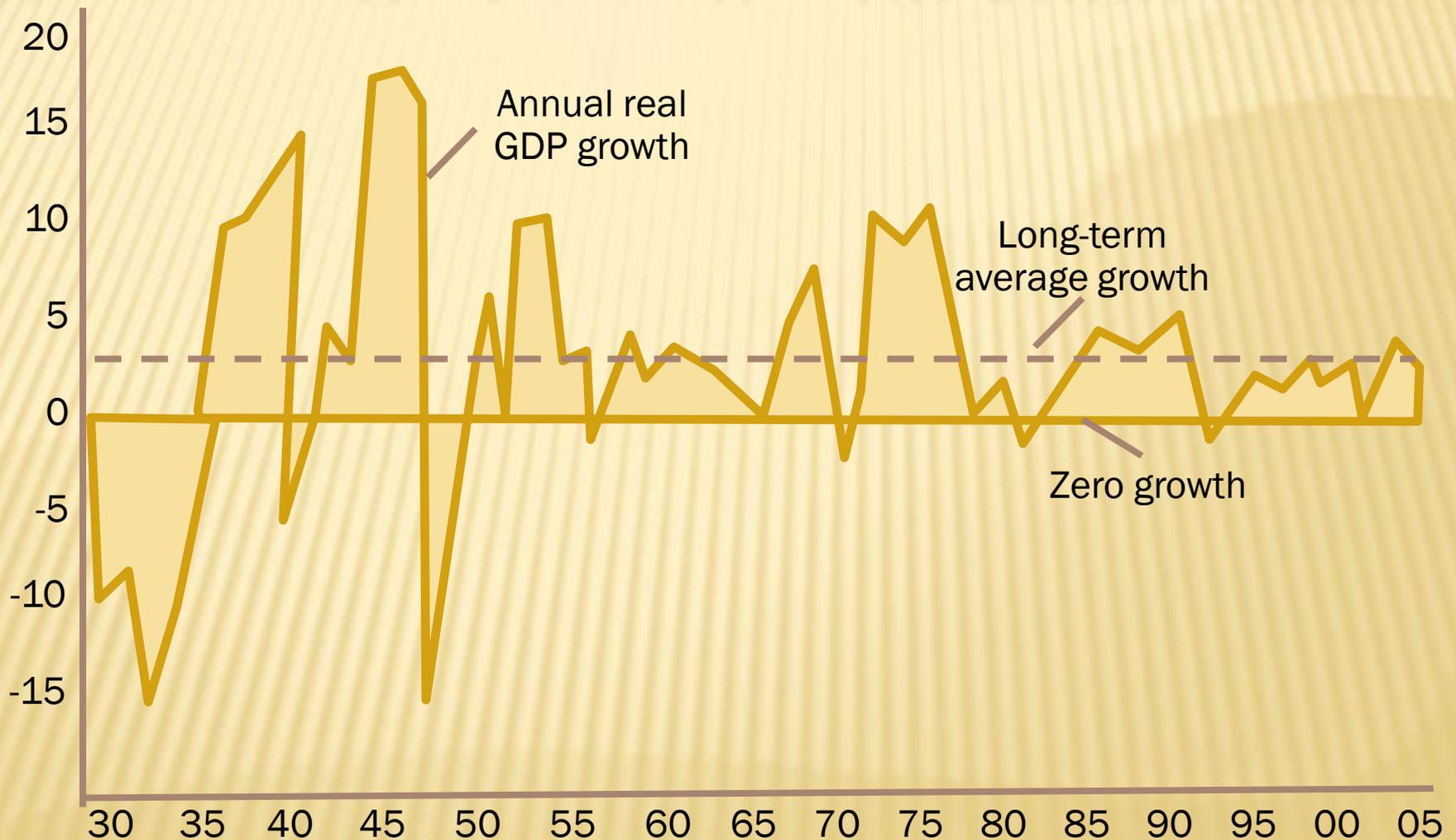


Hypothetical Business Cycle





Business Cycles in the US 1929-2005





What are the three types of economic indicators?



The three types of economic indicators are:

- ✘ **Leading** - variables that change before the real GDP changes
- ✘ **Coincident** - variables that change at the same time that the real GDP changes
- ✘ **Lagging** - variables that change after the real GDP changes



Leading Indicators

- × changes in business and consumer credit
- × new orders (or lack of) for plant and equipment
- × new consumer goods orders (or lack of)
- × unemployment claims (or lack of)
- × delayed deliveries
- × new business formed (or lack of)
- × average workweek
- × new building permits (or lack of)
- × changes in inventories
- × material prices
- × stock prices
- × changes in money supply



Coincident Indicators

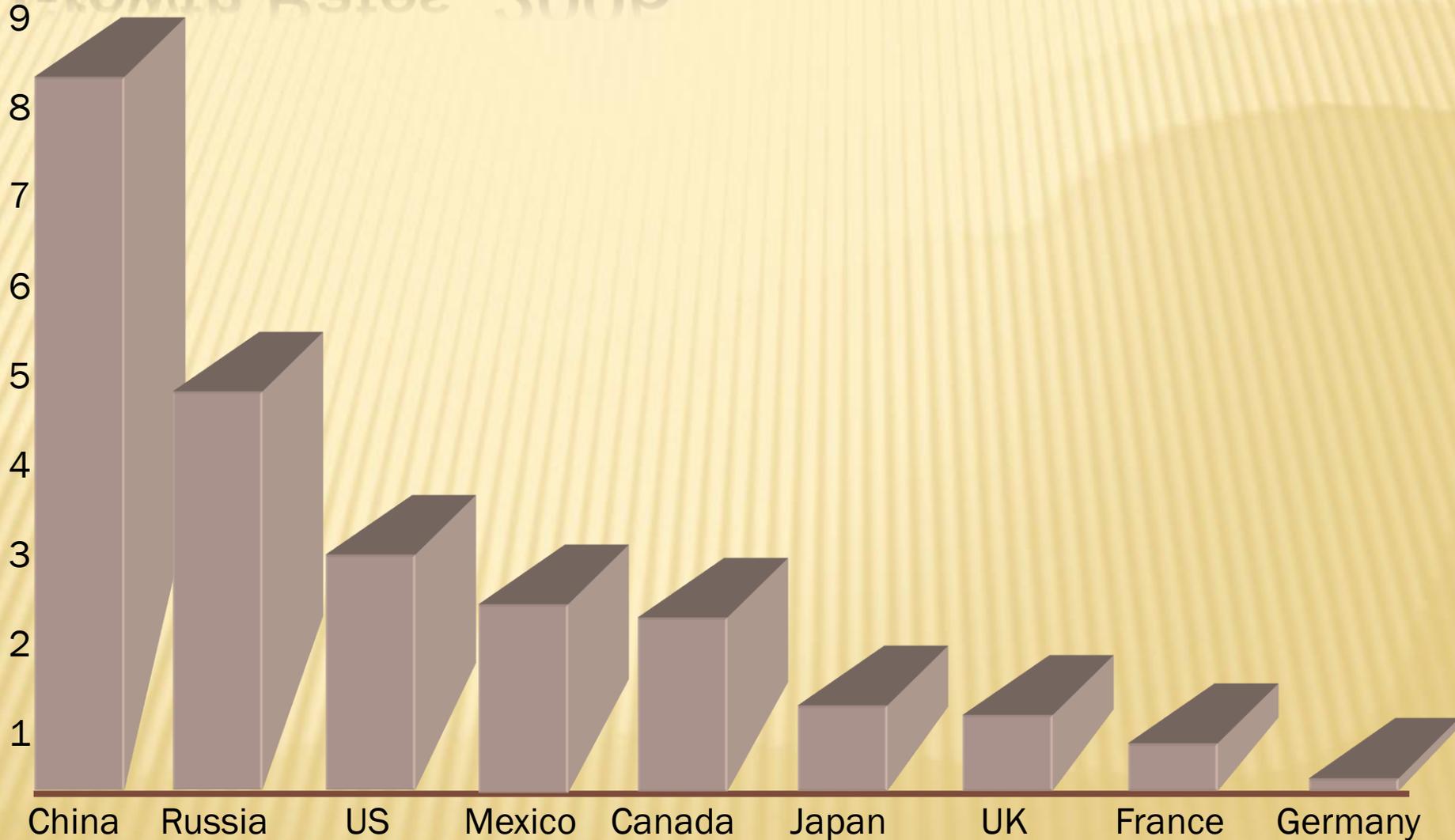
- ✘ nonagricultural payrolls
- ✘ personal income
- ✘ industrial production
- ✘ manufacturing and trade sales



Lagging Indicators

- ✘ unemployment rate
- ✘ duration of unemployment rate
- ✘ labor cost per unit of output
- ✘ inventories to sales ratio
- ✘ outstanding commercial loans
- ✘ commercial credit to personal income ratio
- ✘ prime interest rate

An International Comparison of Real GDP Growth Rates, 2005





What is the civilian labor force?



The civilian labor force is defined as all people 16 years or older who are either employed or unemployed, excluding members of the armed forces and people in institutions.



Who is considered employed?



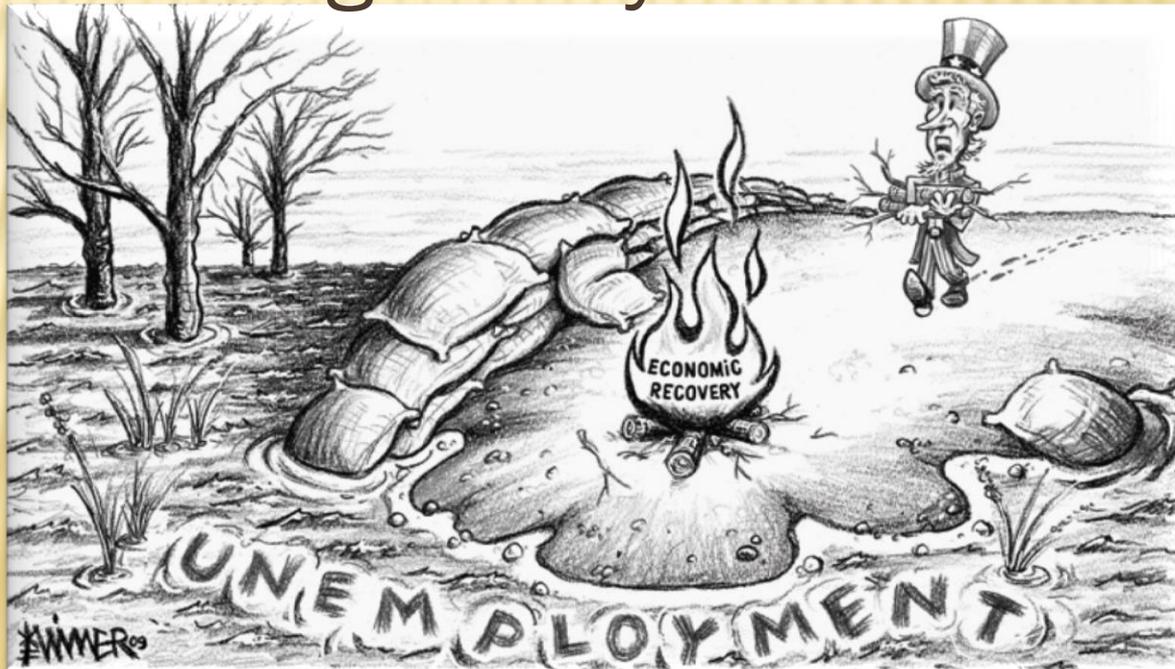
Anyone who works at least one hour a week for pay or at least 15 hours per week as an unpaid worker in a family business is considered employed.



What causes unemployment?



Unemployment happens when total spending falls so that businesses find it profitable to produce a lower volume of goods and avoid unsold inventory. Since businesses want less output, they discharge or lay off workers.





Who is considered unemployed?



Anyone who is 16 years of age and above and who is actively seeking employment is considered unemployed.



NOT IN LABOR FORCE

- × armed forces
- × household workers
- × students
- × retirees
- × persons with disabilities
- × institutionalized
- × discourage workers

CIVILIAN LABOR FORCE

- × Employed
 - + employees
 - + self-employed
- × Unemployed
 - + new entrants
 - + re-entrants
 - + lost last job
 - + quit last job
 - + laid off

Total Population Age 16 and Over



What is the unemployment rate?



The unemployment rate is the percentage of people in the labor force who are without jobs and are actively seeking jobs.

$$\text{unemployment rate} = \frac{\# \text{ unemployed}}{\# \text{ civilian labor force}} \times 100$$



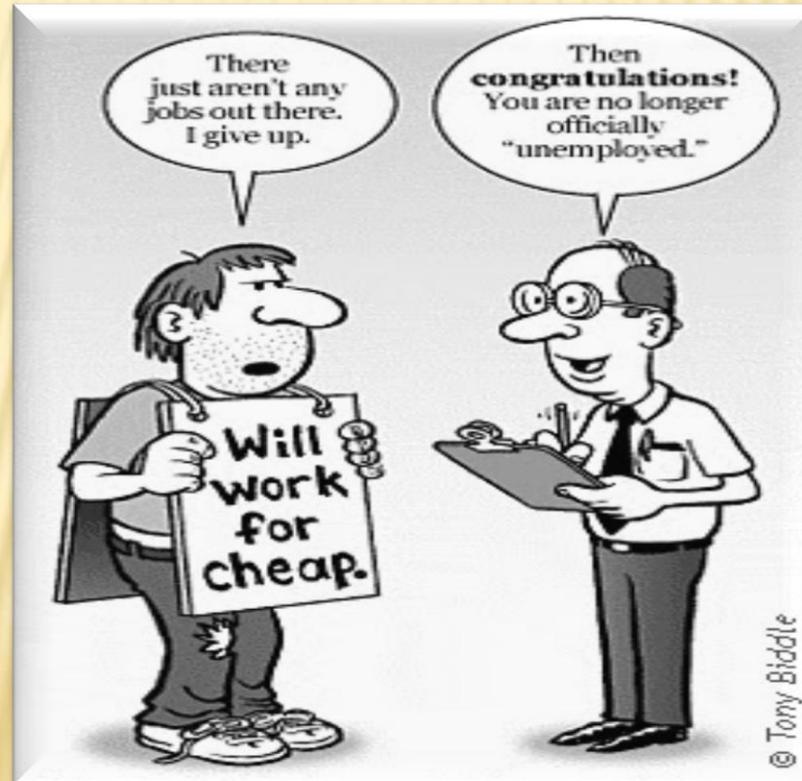
How is the unemployment rate calculated?



60,000 households are surveyed each month in order to determine the unemployment rate.



Who is a discouraged worker?





A discouraged worker is a person who wants to work, but who has given up searching for work.



What is underemployment?

What is underemployment?



Full-time workers who are working part-time or at jobs below their level of skills are considered underemployed.



What are criticisms of the unemployment rate?

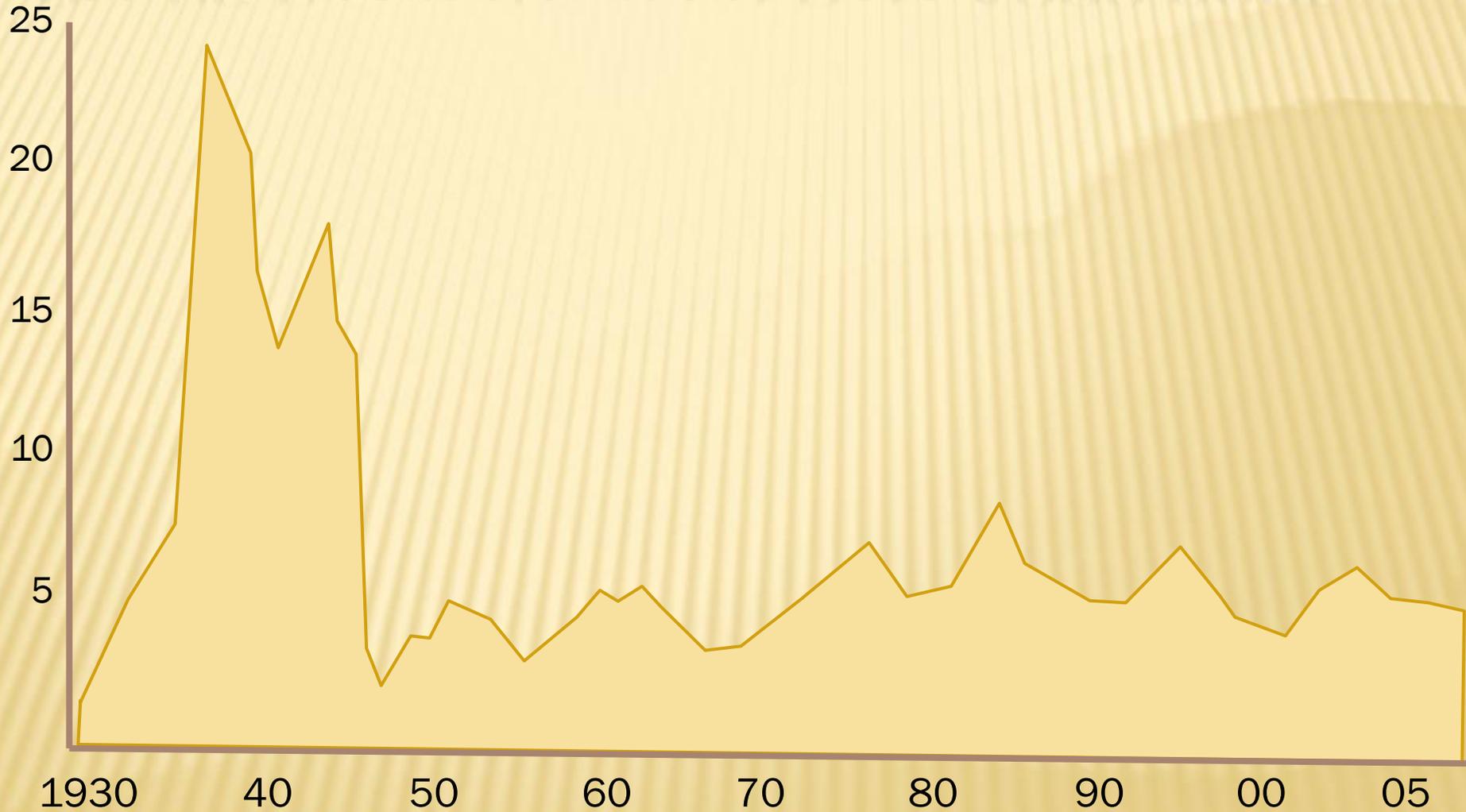


Criticisms of the unemployment rate are:

- ✘ It does not include discouraged workers.
- ✘ It includes part-time workers.
- ✘ It doesn't measure all underemployment.



The US Unemployment Rate 1929-2005





What are the types of unemployment?



The types of unemployment are:

- ✘ **Seasonal** - unemployment caused by recurring changes in hiring due to changes in season or weather conditions
- ✘ **Frictional** - normal search time required by workers with marketable skills who are changing jobs, or entering or re-entering the labor force
- ✘ **Structural** – a mismatch of the skills or location of workers out of work and the skills or location required for existing job opportunities
- ✘ **Cyclical** - unemployment caused by the lack of jobs during a recession or trough



What is full employment?

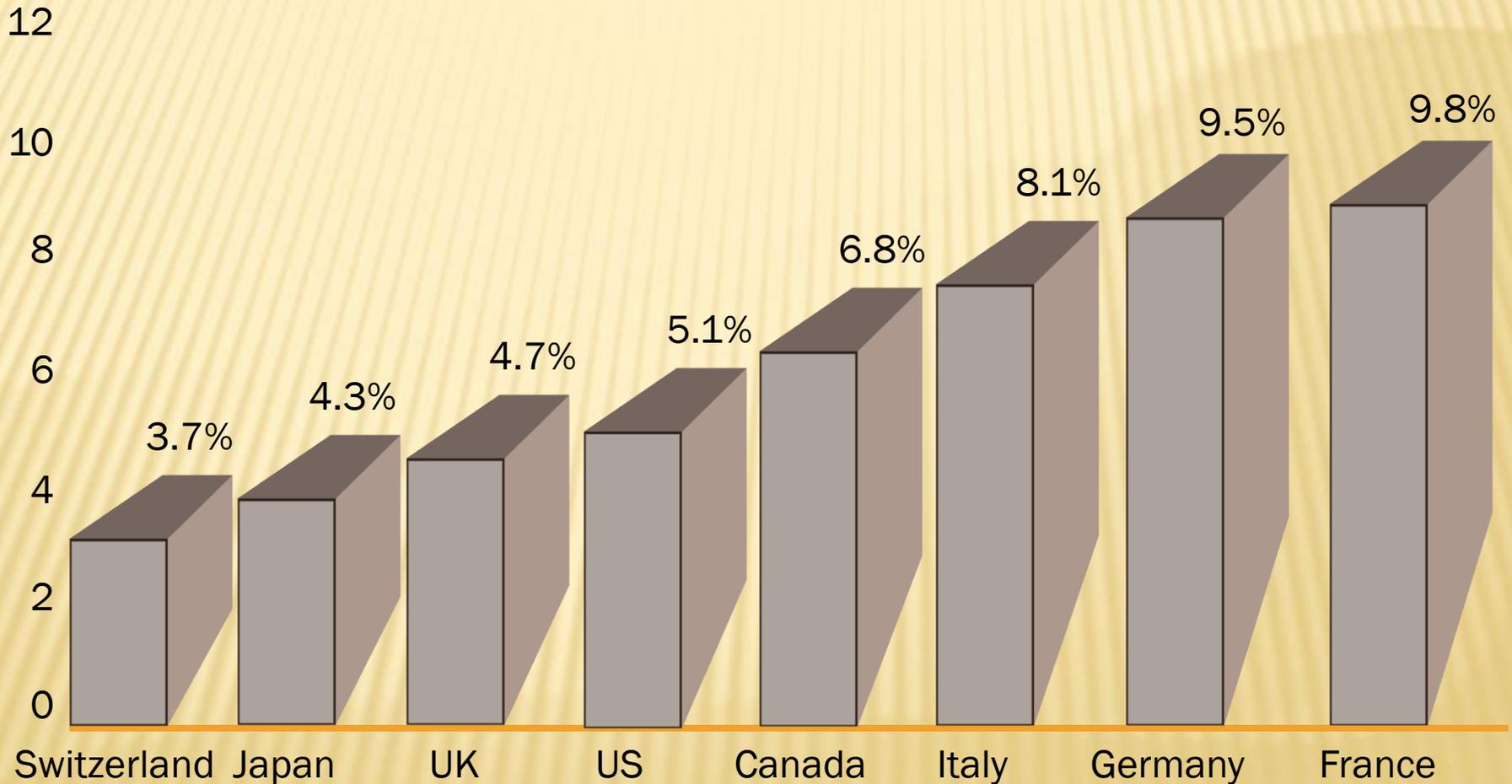


Full employment means avoiding cyclical and structural unemployment, while keeping frictional unemployment reasonably low.

The natural rate of unemployment changes over time, but today it is considered to be about 5%.



Unemployment Rates, 2005





What is the cost of unemployment?



The GDP gap is the cost of unemployment.

The **GDP gap** is the difference between full-employment real GDP and actual real GDP. It's the gap between actual and potential real GDP and so measures the monetary losses of real goods and services when at less than full employment.



The End