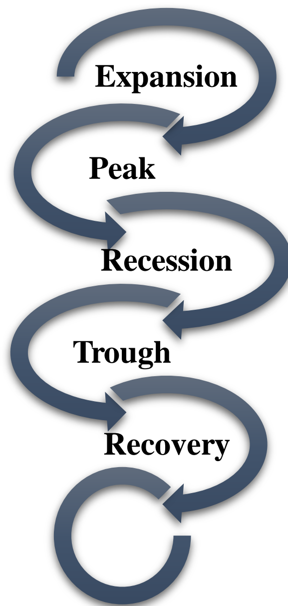
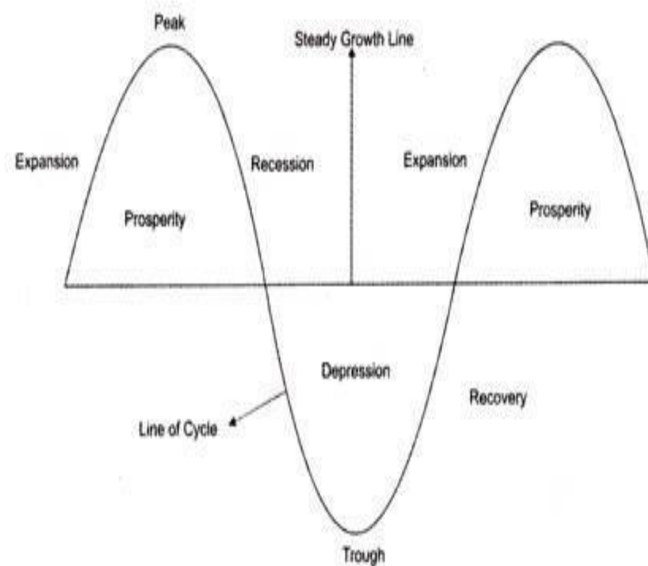
Business Cycle

A business cycle, sometimes called a "trade cycle" or "economic cycle," refers to a series of stages in the economy as it expands and contracts. Constantly repeating, it is primarily measured by the rise and fall of gross domestic product (GDP) in a country.
Business cycles are universal to all nations that have capitalistic economies. All such economies will experience these natural periods of growth and declines, though not all at the same time. However, given the increased globalization, business cycles tend to happen at similar times across countries more often than they did before.

Phase of Business Cycle





1. **Expansion-**

During this stage production increase in all sectors of economy. As a result of increased production employment opportunities increase. This on turn the purchasing power of the people. the velocity of the money supply is high, and investment is high.

2. **Peak-**

The economy then reaches a saturation point, or peak, which is the second stage of the business cycle. The maximum limit of growth is attained. The economic indicators do not grow further and are at their highest. Prices are at their peak.

3. **Recession-**

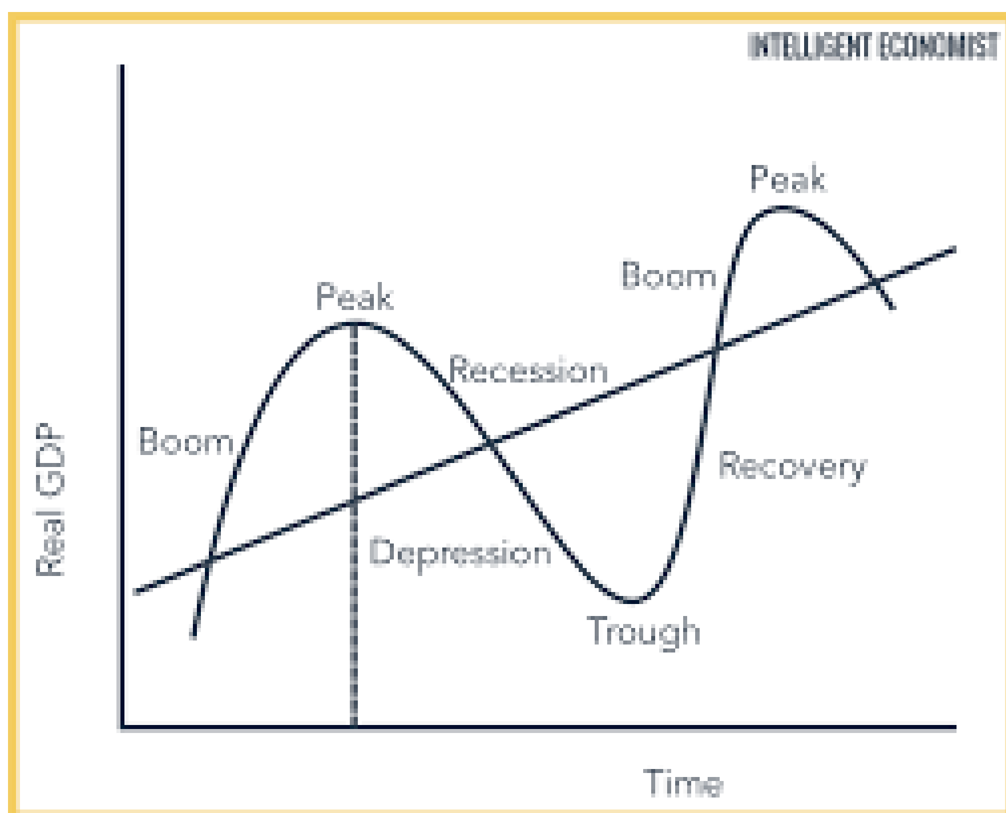
The recession is the stage that follows the peak phase. The demand for goods and services starts declining rapidly and steadily in this phase. Producers do not notice the decrease in demand instantly and go on producing, which creates a situation of excess supply in the market. Prices tend to fall.

4. **Trough-**

There is further decline until the prices of factors, as well as the demand and supply of goods and services, contract to reach their lowest point. The economy eventually reaches the trough. It is the negative saturation point for an economy.

5. **Recovery-**

After the trough, the economy moves to the stage of recovery. In this phase, there is a turnaround in the economy, and it begins to recover from the negative growth rate. Demand starts to pick up due to low prices and, consequently, supply begins to increase. The population develops a positive attitude towards investment and employment and production starts increasing.



Causes of Business Cycle

1. **Expansion and contraction of loans by banks**
2. **Change in volume of investment or Change in the marginal efficiency of capital**
3. **Under consumption or Excessive savings**
4. **Lack of adjustment between demand and supply**
5. **Innovation-** Development of new technologies of production affects the production, employment, income. It led to the phase of prosperity. If there is lake of innovation it may lead to phase of depression.
6. **Feelings of Entrepreneur-** If entrepreneur are optimistic and hopeful it will lead to the phase of prosperity. But if he is pessimistic and frustrated it may lead to phase of depression.
7. **Other Factors-** External factors such as wars, revolution, crisis, rate of growth of population.

Measures for Controlling Business Cycle

1. **Monetary Policy**

Monetary policy as measure to control business cycle fluctuation refers to all those measures which are taken with a view to control money and credit supply in the country. When we are in the state of full employment and we are facing inflation, a deflationary policy may be adopted. The central bank can reduce the quantity of money in circulation. The bank can adopt different measures for this purpose, like increase in the bank rate, selling of securities in the market, increasing the reserve ratio of the member banks etc.

On the other hand, in case of deflation the central bank can adopt inflationary monetary policy by lowering the bank rates or purchase of securities. Monetary policy has achieved a very limited success in the past, because central bank has not full power over the supply of money and credit in the country. Moreover, the quantity of money has failed during the world depression of 1930s.

2. **Fiscal Policy**

Fiscal policy as measure to control business cycle fluctuation nowadays is considered to be a powerful anti-cycle weapon in the hands of the government. Fiscal policy involves the process of shaping the public finance (income and expenditure) with a view of reduce fluctuations in the business cycle and attainment of full employment without inflation.

In case of inflation the governments reduce the public work programs, imposing heavy taxes on business profits to discourage private investment, reduces purchasers' power, taking loans from the people, prepares surplus budget to reduce public debt. All these fiscal measures greatly help in reducing the inflationary trend in the economy.

If the economy facing depression, the government increases it expenditure on public works programs like construction of new canals, new roads, buildings etc. Increase in government expenditure, income, employment, profit and consumption of the people. In order to encourage private investment, the government reduces taxes on profit. The government also prepares deficit budget and the deficit is met by loans. All these fiscal measures to control business cycle sets in upswing in the economy.

3. **Non- Fiscal Policy and Non- Monetary Policy**

Non- fiscal policy and non-monetary policy includes direct control by the government. The government may restrict certain kinds of investment or economic activity. This control may be more discriminatory than other economic activity. Its implementation requires honest & efficient administration and should be used under extraordinary circumstances.