



# Economics and business

**SOURCE 1.1** Economic indicators include the rate of economic growth, trends in unemployment, inflation and sustainability.

# Chapter 1

# Indicators of economic performance and how Australia's economy is performing

## Main focus

Measuring economic performance allows us to determine the success and market strength of a country's economic system. This enables countries to be compared, and can help to keep a country's economy and markets strong. Economic performance is monitored and evaluated using a variety of measures known as economic indicators. These indicators include the rate of economic growth, trends in unemployment, inflation and sustainability. We also need to examine the fluctuations and changes in the business cycle to understand how they affect the economy.

## Why it's relevant to us

To assess economic performance, we need to be aware of the key economic indicators used to measure and evaluate the economy. Measuring economic performance gives us a deeper understanding of how Australia performs in the global market.

## Inquiry

- How is Australia's economy performing according to the indicators of economic performance?
- How is the performance of the Australian economy measured?
- How are the different economic sectors interconnected?
- How is the economy affected by fluctuations in the business cycle?

## Key terms

- business cycle
- classical economics
- consumer price index (CPI)
- consumption
- economic performance indicators
- free market
- gross domestic product (GDP)
- inflation
- interest rates
- monetarism
- New Deal
- sustainability index
- Sustainable Development Goals (SDGs)
- unemployment
- workforce

## Let's begin

Ideas about how to run and how to measure an economy have an effect on many aspects of our daily lives – from the level of taxes we pay and the funding levels of our schools, to the level of government support offered to businesses.



**SOURCE 1.9** Generally, an increase in consumer spending per head of population is regarded as a sign of economic progress.

GDP as a statistical measure does have some limitations. It does not take account of illegal economic output such as work undertaken for 'cash in hand' that is not declared to the tax authorities. It also does not include work that is unpaid such as volunteer work. Additionally, it fails to take into account reductions in quality of life and losses that occur through natural disasters. For instance, if an earthquake occurs, GDP will measure the economic value of rebuilding but will not take into account the value of the economic assets such as the buildings lost. For this reason, GDP can be inaccurate as a measure of real economic activity.

## Consumption

Statistics are collected on the level of consumer spending, known as **consumption**. This is another indicator of economic growth. Generally, an increase in consumer spending per head of population is regarded as a sign of economic progress.

### GLOSSARY

**consumption** the use of goods and services by consumer spending

## ECONOMICS AND BUSINESS FACT

- Consumption in the following states and territories fell in October 2017: Western Australia (−0.3%), Queensland (−0.1%), Victoria (−0.1%), the Northern Territory (−0.4%), the Australian Capital Territory (−0.2%), and Tasmania (−0.1%)
  - New South Wales (0.0%) was unchanged
  - South Australia (0.1%) rose in October 2017
- (Source: Australian Bureau of Statistics, 8501.0 – Retail trade, Australia, January 2018.)

**Inflation**

- 1 Explain the meaning of 'inflation'.
- 2 Describe two effects of inflation.
- 3 Explain how Australia's CPI is measured.
- 4 Look up the most recent CPI figures released by the ABS.
  - a What is the overall percentage change over the last quarter?
  - b What is the overall percentage change over the past year?
  - c What group had the most significant price rise over the past quarter and by how much?
  - d What group had the most significant price fall over the past quarter and by how much?

**DEVELOPING YOUR UNDERSTANDING 1.3****1.4 Unemployment levels**

The level of unemployment is an important indicator of economic performance. It indicates how well the important economic resource of labour is being utilised. Unemployment also affects the level of wages paid and, therefore, the level of consumer spending, economic growth and, hence, standard of living.

In Australia, the level of official unemployment is measured as the number of people of working age without a job who are available for work. The ABS defines a person as being unemployed if they are aged 15 years or over and are:

- not employed
- taking active steps to find work
- available to start work.

The **unemployment rate** is the percentage of available workers, known as the **workforce**, who are unemployed.

**GLOSSARY**

**unemployment rate** number of unemployed persons divided by the number of people in the labour force

**workforce** the individuals capable of working in a given economy



**SOURCE 1.13** In bad economic times, unemployment rises when workers are made redundant.

## Jobs growth

## DEVELOPING YOUR UNDERSTANDING 1.5

**\$A climbs as economy adds 61 600 jobs in November**

Employment surged past all expectations in November 2017, rising the most in more than two years, while the jobless rate remained near five-year lows.

Australia's annual jobs growth rate at 3.2% is more than twice the US pace of 1.4% and the second fastest on record.

The unemployment rate stayed at 5.4% as more people went looking for work, matching the lowest reading since February 2013.

While firms are hiring workers, they are not so keen on paying them more, leaving wage growth near record lows and putting an unwelcome cap on consumer spending and inflation.

The slow pace of wage rises is a major reason the Reserve Bank of Australia (RBA) last month forecast core inflation would not reach the floor of its 2 to 3% target band until early 2019.

**SOURCE 1.14** Adapted from '\$A climbs as economy adds 61 600 jobs in November', *The Sydney Morning Herald*, 14 December 2017

- 1 Define the term 'unemployment rate'.
- 2 What was Australia's annual growth in jobs at the end of 2017?
- 3 While jobs growth is positive, explain what has happened to wages growth. How can this impact on economic growth and consumer spending?

## 1.5 The level of interest rates

**Interest rates** reflect the cost of borrowing money. Interest on money borrowed is like 'rent' on the money you have borrowed until you have repaid it. Investors and consumers often need to borrow money in order to purchase items or invest in economic development. If interest rates are high, investors are less likely to borrow in order to invest in new business ideas or expansion of existing businesses. This will result in less economic growth.

However, low interest rates can be a disincentive for people to save, so governments must strike a balance with interest rates. The Australian Government often encourages banks to increase

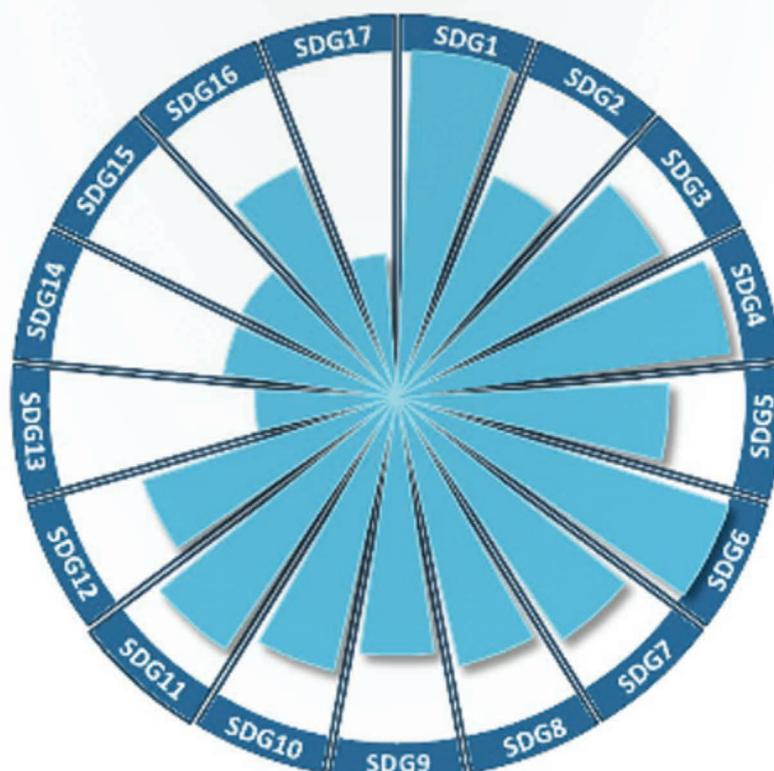
### GLOSSARY

**interest rate** the amount paid by a lender to a borrower for the use of assets

interest rates when the economy is booming to prevent it from overheating. In an overheated economy, the demand for goods and services increases faster than supply, driving up inflation. At the moment, interest rates are at a record low as the Reserve Bank of Australia tries to ensure that the economy is growing at the desired rate.

OVERALL SDG PERFORMANCE	Global rank	Score or value	Regional average
SDG Index	20 (of 149)	74.5/100	75.3/100
<b>Comparison with other development metrics</b>			
Human Development Index, 2014	2 (of 188)	0.93/1	0.88/1
Subjective Wellbeing, 2015	10 (of 149)	7.3/10	6.6/10
GDP per capita, PPP, 2015	13 (of 149)	US\$47 318	US\$40 671
Global Competitiveness Index, 2016	21 (of 140)	5.5/10	4.9/10
Environmental Performance Index, 2016	13 (of 180)	87.2/100	84.4/100

**AVERAGE PERFORMANCE BY SDG**



**SDG DASHBOARD**



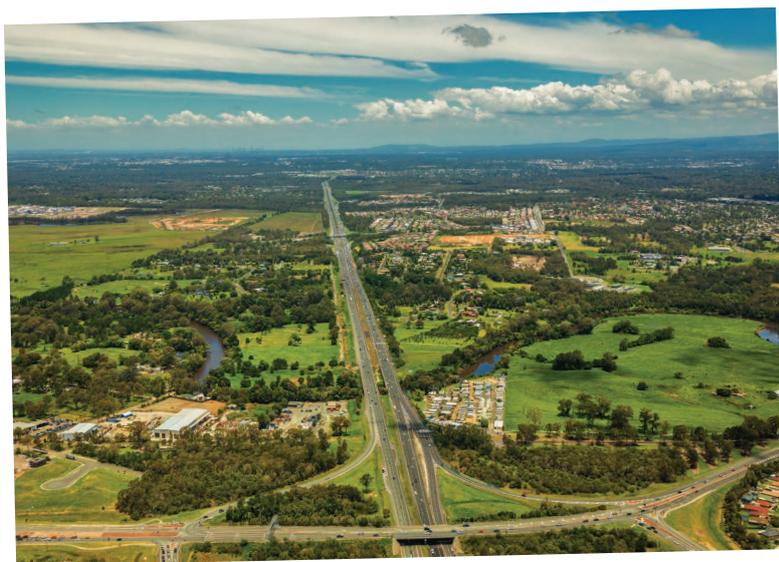
**SOURCE 1.15** Australia's performance on each of the Sustainable Development Goals, 2016 (Source: [https://issuu.com/unsdsn/docs/sdg\\_index\\_and\\_dashboards\\_country\\_pr](https://issuu.com/unsdsn/docs/sdg_index_and_dashboards_country_pr))



**The business cycle****DEVELOPING YOUR UNDERSTANDING 1.8**

- 1 Define the concept of the 'business cycle'.
- 2 What occurs in a recession and in an expansion to the economy?
- 3 Explain the role of the government in a recession or decline in the economy. Why do governments intervene?
- 4 Read the article below and answer the questions that follow.

In the 2017/18 federal budget, the government focused on a number of areas to support the economy. These included guaranteeing essential services, providing opportunities for people and supporting businesses to create more employment. The government also announced a number of infrastructure projects to support production, employment and economic growth. Projects included the National Rail Line upgrade, the Geelong Rail Line upgrade, planning for a rail link to Tullamarine airport, upgrading the Bruce Highway in Queensland and developing the western Sydney Airport. Other projects and measures included investing in schools, and cutting taxation rates for businesses to make it more enticing to invest and expand.

**SOURCE 1.21** Budget 2017/18

- a Explain the benefits of governments carrying out infrastructure projects.
- b Why would the government cut taxes to businesses in Australia?
- c Explain the benefits to Australia if there are high levels of economic activity.

## REFLECTING AND CONSOLIDATING

### Chapter summary

- The economic performance of a nation determines the living standards of its citizens.
- Classical economic theories state that the market works best when left alone by the government and that the 'invisible hand' allocates economic resources where they will be best used.
- Keynesian theories state that the government should use monetary and fiscal policy to control a nation's economy.
- Monetarists believe that the government should not intervene in a free market except via monetary policy.
- Government intervention in the economy depends on economic and social conditions.
- Economic performance indicators are a way of measuring a nation's economic performance.
- GDP is the total value of goods and services produced in a nation in one year, minus the cost of production.
- Inflation refers to an increase in the price of goods and services.
- Unemployment levels have an impact on wage levels and total demand in an economy.
- Interest rates reflect the cost of borrowing money.
- The business cycle moves through periods of recession and expansion.

### Multiple-choice questions

- Classical economic theorists believe that the market would be controlled by
  - the dynamic lever.
  - the spirit level.
  - the invisible hand.
  - the central bank.
- Which of the following is a financial measure of an economy?
  - Quality of life
  - Environmental conservation
  - Health and education outcomes
  - Inflation levels
- An expansion in the economy during the business cycle benefits the economy by
  - providing employment for people.
  - reducing taxation revenue to the government.
  - increasing unemployment levels.
  - reducing the amount of goods and services available.
- Which of the following does not happen when high employment levels are present in an economy?
  - Income tax revenue falls as a result of fewer people earning income
  - Government expenses decrease
  - Decreased rates of crime, family breakdown and regional decay
  - Individuals have the opportunity to change jobs whenever they choose
- The rates of consumer spending have been increasing slowly in Australia. This has been caused by
  - an increase in spending at department stores.
  - weak or little wages growth.
  - consumers only buying goods online.
  - a decrease in spending at cafés.

### Short-answer questions

- 1 Explain how the Australian Government measures:
  - a economic growth
  - b inflation
  - c unemployment.
- 2 Discuss why it is important to measure each of the factors in Question 1 when assessing economic performance.
- 3 Summarise the theories of one economist mentioned in this chapter.
- 4 Discuss the economic and social costs of:
  - a high unemployment
  - b environmental issues.
- 5 Explain why GDP is not the only way to measure economic wellbeing.
- 6 Why is it important for the federal government to manage the economy to ensure economic recessions are overcome?

### Extended-response questions

- 1 Using the ABS website, locate the following statistics:
  - unemployment figures for the past 12 months
  - inflation figures for the past four quarters.
- 2 Describe any changes you noticed in the graphs.
- 3 Suggest some reasons for and consequences of these changes.

Use a spreadsheet application, such as Microsoft Excel, to construct a graph for each showing the changes.