Exercise walk-through

External influences on business activity ▪ 6.1

eXercise

You must be able to

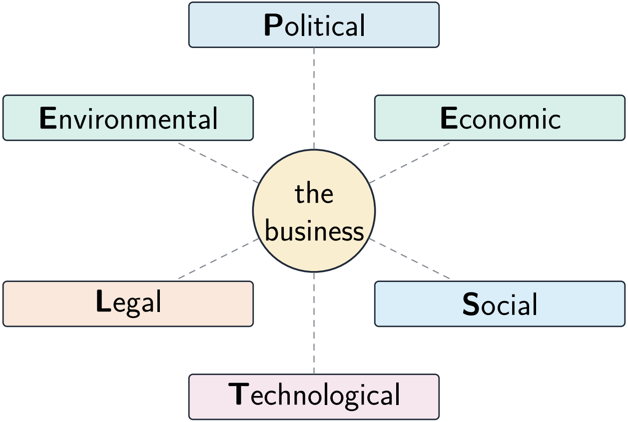
- describe the stages of the business cycle and the effect of interest rates
- explain how a change in the exchange rate affects exporters and importers
- analyse and evaluate how a business should respond to external change

Method — The economic environment

- **Business cycle:** boom $\rightarrow$ recession $\rightarrow$ slump $\rightarrow$ recovery.
- **Interest rate up:** borrowing costs more $\rightarrow$ customers spend less, firms invest less.
- **Exchange rate:** *appreciation* (currency rises) $\rightarrow$ exports dearer, imports cheaper; *depreciation* $\rightarrow$ exports cheaper (good for an **exporter**), imports dearer.

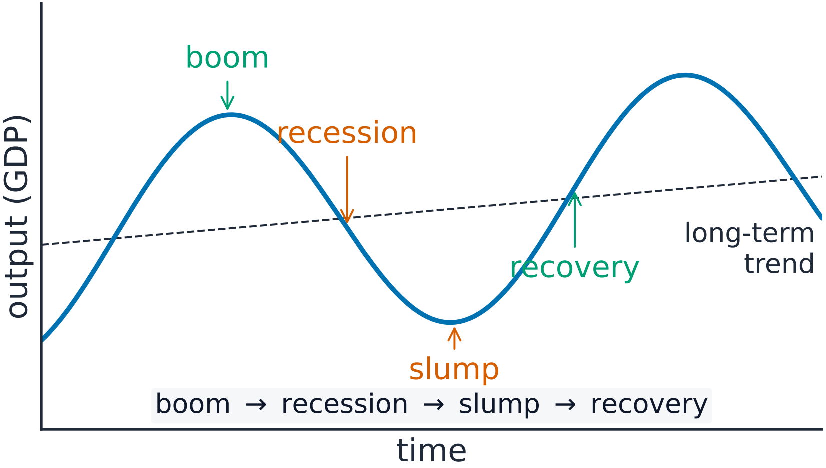
Answer shapes: AO1 + AO2 + AO3 (reasoning chain) + AO4 (a supported judgement *in context*).

Method — The economic environment



PESTLE groups the six wider external forces that act on a business

Method — The economic environment



Method — The economic environment

a weak currency helps exporters; a strong one helps importers

appreciation	**depreciation**
(currency rises)	(currency falls)
exports dearer,	exports cheaper,
imports cheaper	imports dearer

Practice 2.1 ▪ 2 marks

Define the term *inflation*.

Solution 2.1

Worked steps

a general rise in the level of prices over time (2 for a clear definition; 1 for a partial idea).

Practice 2.2 ▪ 2 marks

State the four stages of the business cycle.

Solution 2.2

Method: The economic environment

Worked steps

boom, recession, slump, recovery (2 for all four; 1 for a partial list).

Practice 2.3 ▪ 2 marks

State one effect on a business of a rise in interest rates.

Solution 2.3

Method: The economic environment

Worked steps

any one of: loans cost more, lowering profit; customers spend less, lowering demand; less new investment (2 for a developed point; 1 for a basic one).

Exam-style 3.1 ▪ 3 marks

Explain one effect on a business of a **recession**.

Solution 3.1

Method: The economic environment

Worked steps

[3] **AO1** 1 — state an effect (falling demand; lower sales; cost-cutting; risk of closure). **AO2** up to 2 — develop it, e.g. in a recession customers have less income $\rightarrow$ sales fall $\rightarrow$ the firm may cut costs or staff to survive (2 developed / 1 limited).

Exam-style 3.2 ▪ 8 marks

A firm exports most of its goods. Analyse the impact on it of a **fall** (depreciation) in the local currency.

Solution 3.2

Method: The economic environment

Worked steps

[8] **AO1** + **AO2** + **AO3** up to a developed chain on **two** effects. Example chains — *exports cheaper abroad*: the local currency falls → the firm's prices abroad fall → it sells more → higher revenue. *Imported inputs dearer*: any imported materials cost more → variable costs rise → some of the export gain is offset. Maximum 8; reward a two-sided analysis.

Exam-style 3.3 ▪ 12 marks

Interest rates have risen sharply. Evaluate how a business with large loans should respond.

Solution 3.3

Method: The economic environment

Worked steps

[12] **AO1** 2 / **AO2** 2 / **AO3** 2 / **AO4** up to 6. Options: **repay debt** to cut interest (but uses cash), **raise prices** (but may lose sales), **cut costs** (but may harm quality), **delay investment** (but may fall behind rivals). Judgement: the best response depends on how large the loans are, how price-sensitive demand is, and whether the rate rise is temporary — a firm with heavy debt may prioritise repaying or refinancing, while a strong firm may simply absorb the higher cost.