

Unit 5: Chapter 21

BUSINESS, THE ECONOMY AND GOVERNMENT

Learning Outcomes from this chapter

***On
completion,
you should
be able to:***

Outline the impact of different economic variables on Irish businesses

Outline the impact of inflation on Irish businesses

Explain how interest rates can impact businesses in Ireland

Outline the benefits and challenges of falling unemployment rates

Illustrate the impact of fluctuations in exchange rates with our main trading partners

Explain the ways in which the government affects the labour force

Discuss why the government encourages enterprise in Ireland

Describe how the government encourages and regulates business activity

Discuss how the government can use the tax system to create a positive climate for business in Ireland

Evaluate the role of Enterprise Ireland and IDA Ireland

Explain how business affects the development of the economy

Economic variables

Different economic variables affect the economy, businesses, consumers and the government:

1. Inflation
2. Interest rates
3. Employment
4. Exchange rates
5. Taxation



Inflation	Sustained increase in the general level of prices over a period of time
Deflation	Decrease in the general level of prices in two consecutive quarters

Potential impact of high inflation rates on the Irish economy

Purchasing power of money falls over time – saving is discouraged
More wage demands from workers are likely – there may be strikes and poor morale
Lower standard of living – less purchasing power, as the cost of living rises
Exports become less competitive, as Irish selling prices rise in relation to goods from other countries
Increased government expenditure on wages (e.g. teachers, nurses), as the cost of living rises

1. Inflation

The cost of borrowing money expressed as a percentage of amount borrowed

Potential impact of high interest rates on the Irish economy

Debt capital more costly: higher repayments for individuals and government when borrowing or repaying debt at a variable rate; if a business has borrowed, the higher repayments make it harder to expand

Harder to attract investors: return for savings in deposit accounts are higher, so savings accounts offer a more attractive, risk-free return for investors

Less consumer spending: more expensive to access loans, mortgage repayments are higher, so consumers spend less

2. Interest rates

Unemployment

Percentage of labour force not currently employed

Benefits and challenges of low unemployment levels**Benefits:**

- Government tax revenue increases, government spending on social welfare decreases
- Less emigration and 'brain drain' of highly skilled workers
- Increased spending: incomes are higher

Challenges:

- Labour shortages in certain areas may cause high wage inflation
- Pressure on rent/property prices in areas of high employment
- Social costs (e.g. commuting workers have less time for community involvement)

3. Employment levels

The price of one currency expressed in terms of another currency

What happens if sterling (£) weakens against the euro (€)?

Sterling would not buy as much euro as it did before, so sterling has weaker purchasing power in the exchange rate

This can:

- Lower demand for Irish goods by UK consumers
- Lower demand for Irish holidays by UK holidaymakers
- Increase demand for UK imports (vs buying domestically)
- Increase demand for UK holidays for Irish people (vs holidaying in Ireland)

4. Exchange rates

Direct tax	Tax on earnings/income (e.g. PAYE, USC, corporation tax)
Indirect tax	Tax on spending and consumption (e.g. VAT, SSdT, excise duties)

What are the impacts on Irish business if the government changes tax rates?

If corporation tax was increased from 12.5%, businesses would keep less of the profit, so they might need to increase prices or reduce staff.

If there was a reduction in PAYE rates, consumers would have more disposable income, which could lead to an increase in demand for goods.

If import duties were increased/introduced, the businesses importing raw materials or finished goods for resale would face increased costs, which could lead to lower profits or higher prices.

If VAT was decreased, a business could keep more of the profit for each item sold, or reduce their selling price. More competitive prices could stimulate the economy.

5. Taxation

Government expenditure	Increase or decrease capital: one-off expenditure (e.g. build a school) and current/day-to-day expenditure (e.g. wages)
Government agencies	Enterprise Ireland, Industrial Development Agency, LEOs
Government taxation	Can change tax rates to encourage or discourage certain behaviours; can introduce new taxes (e.g. SSdT).
Government grants	Issue financial grants to aid expansion in certain industries or lines of work through LEOs, Enterprise Ireland and IDA
Government regulations	Adjust or introduce new laws (e.g. environmental, data protection)

How the government creates a climate for business
