**Business Cycle**

A **business cycle** is a cycle of fluctuations in the [Gross Domestic Product](https://corporatefinanceinstitute.com/resources/economics/gdp-formula/) (GDP) around its long-term natural growth rate. It explains the expansion and contraction in [economic activity](https://corporatefinanceinstitute.com/resources/economics/definition-market-economy/) that an economy experiences over time.

A business cycle is completed when it goes through a single boom and a single contraction in sequence. The time period to complete this sequence is called the length of the business cycle.

A boom is characterized by a period of rapid economic growth, whereas a period of relatively stagnated economic growth is a recession. These are measured in terms of the growth of the real GDP, which is inflation-adjusted.

The business cycle, also known as the economic cycle, refers to the fluctuations in the economy between periods of expansion and contraction. It consists of four distinct stages:

**Stages of a business cycle**

Business cycles can last for virtually any length of time. The duration of a business cycle is the amount of time it takes to complete all six stages:

1. **Expansion** :A business cycle always starts with the expansion stage. During this stage, there are clear positive economic indicators, including growth in income, employment, demand, supply and profit. Throughout an expansion, the frequency of investments from private and public entities increases, and both businesses and individuals generally repay their debts on time.

2. **Peak** :When the economy becomes saturated and upward growth can no longer continue, the business cycle enters the peak stage. Wages, employment rates and prices for goods and services are as high as they can go, given the current economic conditions. At this point, these economic indicators can not rise further.

3. **Recession** or contraction The recession stage starts as soon as expansion ends and economic activity begins to decline. It lasts until the GDP returns to the point that marked the beginning of the expansion stage. During a recession, demand begins to decline almost immediately, but producers fail to adjust their output until the market has excess supply. Positive economic indicators like prices and wages start to fall at this point.

4. **Depression** :The depression stage begins once the GDP falls below the pre-expansion level or the steady growth line. During a depression, unemployment rates rise dramatically, while economic growth declines steadily. A depression lasts until economic activity can't decrease in value any further or outside investment occurs that stimulates the economy.

5. **Trough** :When the depression stage reaches its lowest point, a business cycle enters the trough stage. At this point, the economy experiences negative economic growth, as the production of goods and services decreases and wages reach their lowest point. Regardless of the severity of a business cycle, the trough is always the lowest point in relation to economic growth.

6. **Recovery** :After the GDP reaches its lowest point in the cycle, the recovery stage commences. During this stage, the economy begins to recover and reverse the negative trends. Demand increases and supply soon follows. Eventually, investments resume, and employment and production begin to rise. The recovery stage lasts until the GDP returns to a steady growth line. Once it reaches this point, the current business cycle ends and a new one begins as it enters the expansion stage again.



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