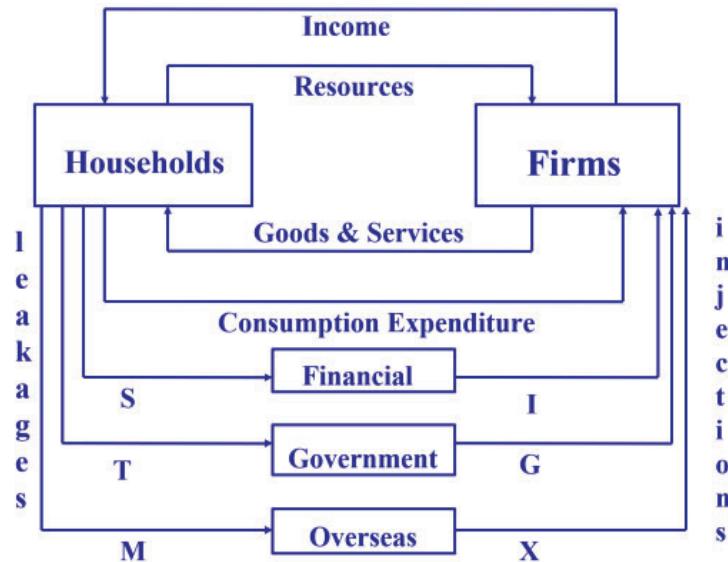

MACROECONOMICS

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CIRCULAR FLOW

Circular flow – a simple model of all participants in the economy; make more sense of the complex real and money flows between various economic units



2 sector flow

- Firms generate income (Y) for hh as they contribute their resources
- Y = value of g/s produced
- Y is used by hh to spend on g/s (E)
- Firms use the sales to pay income for resources
- Equilibrium: $Y = E$

| | Leakages | Injections |
|------------------|--|--|
| Financial sector | Savings (S) | Investment (I) |
| | Deposits taken from households as not yet spent income | Firms borrow money from banks to invest in the production |
| Government | Taxation (T) | Government expenditure (G) |
| | Households' income not spent but contribute to government budget | Creates employment and income e.g. welfare payment, subsidies |
| Overseas | Imports (M) | Exports (X) |
| | Payments to foreign businesses for their g/s | Foreign expenditure to local businesses for g/s |

EQUILIBRIUM