

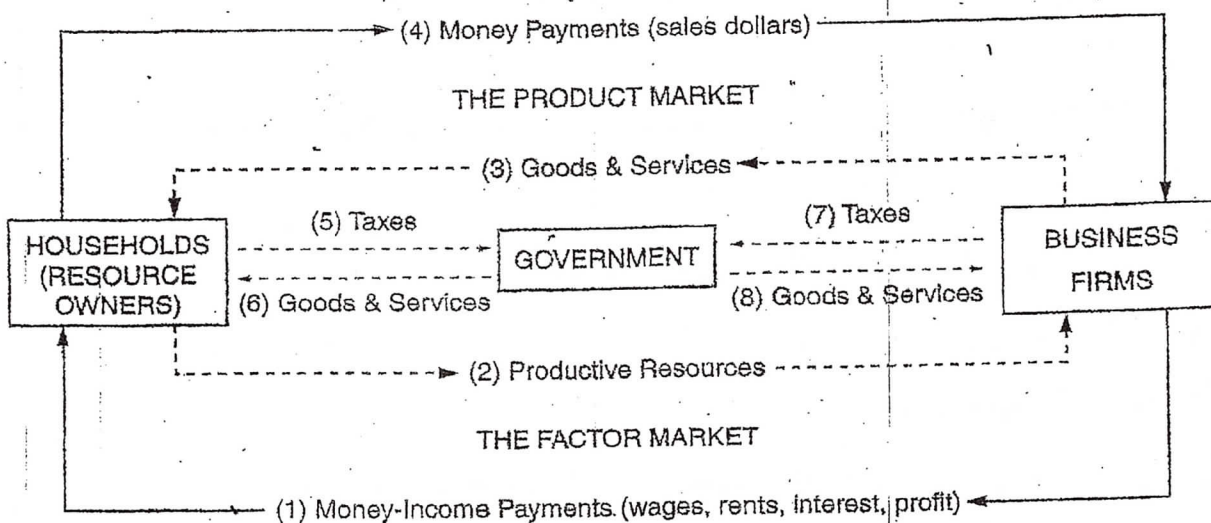
Understanding the Circular Flow of the Macroeconomy

Firms provide goods and services to households through the product markets. Households pay for these goods and services with money. Households supply firms with productive resources: labor, land, capital and entrepreneurial skills. Firms pay money income to households. The value of income firms pay to households, including the profits that business owners receive, equals the dollar value of output. Firms and households decide how much to buy or sell in the markets for goods and resources. For example, Tran spends \$10.00 on school supplies at the market, buying goods and paying with money. The market owner uses the \$10.00 to pay part of the salary of Mariko, the cashier. The firm is buying resources and paying for them with money. The \$10.00 is now ready to be spent in another round. Firms and households pay taxes and user fees to the government, which provides them with some goods and services, such as police protection and national defense.



Figure 10.1

The Circular Flow of Resources, Goods, Services and Money Payments



Activity written by Helen Roberts, University of Illinois, Chicago, Ill.

Part A

Each of the flows in the circular flow diagram in Figure 10.1 is numbered. Identify which number matches the transaction described in the statements below. Consider only the first transaction — not the return flow.

- 1. David buys a CD at the local store for \$9.99. _____
- 2. Emily earns \$6.50 per hour entering data at the music conservatory. _____
- 3. Maria pays her federal income tax. _____
- 4. Jagdish receives \$15,000 in profits from his half-ownership of a coffee shop. _____
- 5. Keisha makes decorative pillows that she sells for \$30.00. _____
- 6. Mammoth Toys Inc. hires 100 new employees. _____
- 7. The National Park Service opens two new campgrounds in Yellowstone National Park. _____

Part B

Write T if the statement is true and F if the statement is false.

- 8. Money flows are clockwise. _____
- 9. Goods and services flows are clockwise. _____
- 10. The resource market determines the price per acre of farmland. _____
- 11. The product market determines the price of a computer. _____
- 12. Firms sell resources in the resource markets. _____
- 13. Government buys resources and households sell resources. _____
- 14. Government buys products, and firms sell products. _____
- 15. The product market determines the salary of the C.E.O. of a firm. _____
- 16. The resource market determines the price of soda. _____
- 17. The resource market determines the price of soda-bottling equipment. _____