

Flow of income between households and firms



**ASSIGN
BUSTER**

In everyday life we experience the circular flow of income between households and firms. If we buy an item in the shop we are doing the circular flow between households and firms. It is important to us to know how the circular flow works. We can control our spending and can save as much as we can if we fully understand the circular flow. In macroeconomics it stated there that the terms circular flow refers to a straightforward economic form which portrays the mutual circulation of income between manufacturer and patrons. In the circular flow model, the mutually supporting entities of manufacturer and buyer are referred to as “ firms” and “ households” correspondingly and supply each other with aspects in order to ease the flow of income. The households are the one who owns the factors of production (FOP) while the firms are the one who uses the factors of production such as land, labour, entrepreneurship and capital. By the factors of production the firms will pay the factors of income to the households. Such as in land the firm will pay rent, in labour the firm will pay wages, in entrepreneurship the firm will pay profits and in capital the firm will pay interest.

1. 1 BODY:

1. 1. 1 CIRCULAR FLOW BETWEEN HOUSEHOLDS AND FIRMS:

The diagram above represents the circular flow between households and firms. There are four flows in the above diagram. First, flows of factors of production (land, labour, capital, entrepreneurship) from households to firms. Second, flow of incomes (rent, wages, interest, profit) from firms to households. Third, flow of output (goods and services) from firms to

households. Fourth, flow of spending/expenditure from households to firms (the household will buy the goods and services from the firm).

There are two movements of funds in the circular flow income. These are “withdrawals and injections”. Withdrawals will happen if there are changes of funds going out of the circular flow of income. Injections will happen if there are changes of funds going into the circular flows of income. The government is the reason of having withdrawals and injections in the circular flow of income.

in order to have a stable economy the government will have to do the injections (I-Investments, G-Government Expenditures, X-Export) and withdrawals (S-Savings, T-Taxation, M-Import). The government will influence the circular flow in the economy. In withdrawals, for e. g. if the economy is having a maximum growth, the government will encourage the households by savings. The central bank will put a high interest so that they will cut down their spending and save their money in the bank. In injections, for e. g. if the economy is having a depression many are unemployed, the government will inject into the economy by their expenditures. The government will build some projects such as bridges, roads, schools and other building projects to make sure that they can contribute to the economy by giving jobs to the people.

Withdrawals: Savings (S), Taxation (T), Imports (M)

Savings –It encourages save and not spending. The household may not go shopping for unnecessary goods but spend only on necessary goods like foods and clothing. Saving also comprises lessening expenditures, such as

<https://assignbuster.com/flow-of-income-between-households-and-firms/>

persisting costs. For e. g. if the person just receive her salary, she may only spend on her daily expenses and the rest will goes into her bank account.

Taxation –The government implemented tax. The households will pay the tax to the government through their incomes. The government must collect taxes so that they can build hospitals, roads and give us a secure place to live in.

Imports –If the economy is having a maximum growth, households is having an abundant of resources (money) and they prefer to buy goods and services internationally than buying goods and services domestically.

Injections: Investments (I), Government Expenditures (G), Exports (X)

Investments –The household income can invest in investments so that it will circulate into the economy. The government will encourage foreign companies to invest in the economy. For e. g. the government will go for foreign direct investments (FDI) and foreign trade zone (FTZ). They can offer them a lower tax and reduce the barriers of entry for foreign companies to invest in the economy.

Government Expenditures –The government collects taxes from the households and they use the taxes in government spending in order to create in-flows of funds back into the economy. For e. g. the government injects money in the economy by giving jobs through building, subsidies to company that is undergoing bankruptcy.

Exports –The government will encourage the local firms to sell their goods and services in foreign countries. The foreign expenditures will go back to the circular flow.

1. 2 CONCLUSION:

I therefore conclude that the circular flow between households and firms is helpful. If we fully understand how the circular flow circulates we are having an advantage to know when we are going to invest our money. It is very helpful for us to know why the government must implement taxes. They implement taxes to help our economy to be stable and to give us a safety place to live. In the circular flows I fully understand how important the factors of production (land, labour, capital, entrepreneurship) to the firms and how crucial the factors of income (rent, wages, interest, profit) to the households.

Question No. 2

2. 0 INTRODUCTION:

A business trade cycle is very crucial in every economy. By knowing and fully understanding the business trade cycle it will help us recover if we are experiencing depression and it can help us maintain if we are in a full employment level in economy. Business trade cycle is the fluctuations in the level of economic activities of a country over a period of time. It is also a persisting fluctuation in economic movement consisting of downturn and upturn and development and regression. The cycle engage the shifts over the period of time between comparatively fast development of output (upturn and wealth), and stages of comparative stagnation or decline

(retrenchment or depression). Using the gross domestic product fluctuations is often measured.

2. 1 BODY:

2. 1. 1 CONCEPTS/ SITUATIONS OF THE BUSINESS TRADE CYCLES:

Full Employment –is a situation of the country’s economy, where everyone or almost all individuals eager and capable to work at the existing salary and operational situations and are able to perform. In this level of economic activity all factors of production are completely utilized.

Unemployment –happens when individuals are jobless and they have keenly looked for job within the previous weeks. Rate of the frequency of unemployment and it is calculated as a percentage by dividing the number of unemployed persons by all persons presently in the force of labour is an unemployment rate.

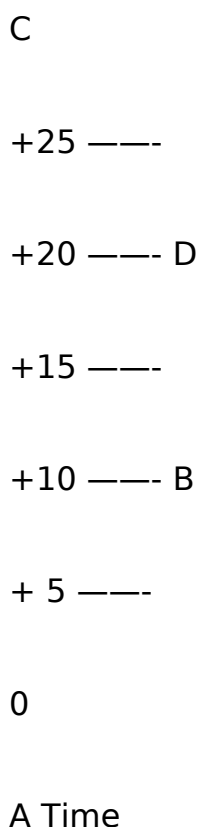
Recession –happens when economic growth becomes negative. The economy is having unemployment. Business cycle tightening, a major slowdown in economic movement is a recession. Recessions usually happen when there is an extensive fall in expenditure frequently following a difficult supply shock or the eruption of an economic bubble.

Inflation –happens when there is a general rise in the level of prices. In inflation the economy is having a full employment. When the general cost level rises, every entity of money purchases lesser goods and services. Subsequently, inflation also replicates erosion in the buying strength of

currency a loss of true worth in the internal channel of exchange and unit of account in the country.

2. 1. 2 BUSINESS TRADE CYCLE:

Annual Growth Rate (%)



The business trade cycle diagram has four phases and each phase have its own characteristics.

Phase A – In phase A, it represents the depression in the economy. The economic activity in this level is the lowest. They are having motionless output. The firms are unenthusiastic. The firms are scared to produce more. The employment level in this phase is very low. The aggregate demand is lesser than the aggregate supply due to a high unemployment. People would not buy goods and services that are unnecessary. The inflation rate is

negative in this level. Firms would not invest in this level or the firms will wait to invest new investments.

Phase B – In phase B, it represents the recovery in the economy. The economic level activity in this economy is low but it is rising. Fast economic development as output levels increase. Firms become confident and will begin to invest. The employment level in this economy is rising. The resources are increasingly utilized. Space between authentic and possible general production level tightens. Aggregate demand is lesser than the aggregate supply due to the economic recovery but if it is booming it is possible to have an equal aggregate demand and aggregate supply. The economy is having a low but rising inflation rate. Recovery begins when firms would not postponed new funds to restore outdated assets.

Phase C – In phase C, it represents the prosperity in the economy. The economy is experiencing a highest economic level activity. Companies are very confident and they are persistent to invest. In this phase the economy reached the peak level. The economy is experiencing a very high employment level. All resources are fully utilized and have reached maximum growth. The aggregate supply is equal to aggregate demand. The economy is experiencing a very high inflation rate. If the demand of household is high the firm's pricing will go up in order to achieve the fully utilized factors.

Phase D – In phase D, it represents the recession in the economy. The economy is experiencing high but falling economic level activity. The production in this level will decline. Company's confident to invest begun to

decrease. Unemployment is rising. Resources are not fully utilized in this level. Difference between authentic and possible general production expands. The aggregate supply is more than the aggregate demand. The economy is experiencing a high but falling inflation rate. Recession will begin if the firms will become pessimist and will stop investing. Hardship is extensive in this level but if the loss is not too critical it is still a recession level.

2. 2 CONCLUSION:

In conclusion, the business trade cycle is very crucial in every businessman and even to normal individuals. We must be vigilant in our economy. We must know what is happening around us to avoid so much loss. During recession and depression, people should be very careful in spending money and save as much so that we would not end up in nothing. During recovery, it is a good time to invest but invest only if you are sure and analyze properly if the economy will going to boost or not. During prosperity, people will spend more as the employment level reaches its maximum growth.

Investors and individuals can invest and spend as long as you know what is going on in the economy. Be sure that you are knowledgeable and well inform about your investments and in your future investments. There is no harm in predicting the future's economy as long as you can coup up with it.

Question No. 4

3. 0 INTRODUCTION:

In every country there are people are unemployed. What are the main reason of being unemployed? Is it because of low qualification, above of the

age limit or people are basically lazy? There are so many reason why people are being unemployed. These are due to economic level activity, firm's regulations on qualifications, age limit and own self perception. Some individuals are just lazy especially if the government are giving them allowances. Some countries like in USA their government is giving some allowances to the unemployed people. Some are experiencing shame to be unemployed some are undergoing depression of being unemployed.

According to <http://www.bls.gov/news.release/mmls.nr0.htm> the U. S. Bureau of Labour Statistics reported that in December 2010 employers took 1, 483 mass layoff actions involving 137, 992 workers. In a single employer at least 50 persons involved in a mass layoff. 19, 564 are the total number of mass layoff events in 2010 and preliminary declares at 1, 854, 596 were lesser than in 2009 when both results and claims reached their maximum annual point on record.

3. 1 BODY:

3. 1. 1 COST OF UNEMPLOYMENT:

Financial Cost -Individuals experience financial cost due to unemployment in the country. It affects financially to the unemployed person. Individuals can lose their nature of living. For e. g. unemployed person can lose his car, mortgage, things that he used to live and even people who used to be his friends. It also cost in his own family necessities. For e. g. if the unemployed is a family man it cost his wife and children's necessities.

Personal Cost -In this cost of unemployment it can affects the person's lifestyle, confidence, well of being and even psychological stability. The

unemployed person will feel conscious of every person in his surroundings. He will feel insecure, he will think of what others talk behind his back and he even think nonsense towards others. By all of these the unemployed will do stupid things to cover their feelings like drinking alcoholic drinks, smoking and some taking drugs to ease their pain.

Societal Cost –In this cost of unemployment the person will become hysterical. As mention above about the personal cost that it can affects their emotional and psychological stability if these become unstable, the person might do some stupid things. For e. g. beating up his wife and children due to the wife's nagging. Neighbours and friend will keep distance not only to the unemployed person but to his family too. This will happen due to the uncertain deeds by the unemployed person.

Economic Cost –As in the circular flow of income labour is one of the factors of production. If the economy is having an increased of unemployment it affects the income in the country. For e. g. as of the increasing of unemployment the firms will lower the wages of their employees and the employees cannot do anything, the employer can easily find another employees to replace them. This will cause a lower gross domestic product (GDP) or output in the country.

Costs to the government –Government gave us a safety place to live in, gives education, free medical and gives us some benefits. If unemployment increases, government can collects taxes lesser as unemployed cannot pay taxes to the government. Firms will be having lesser profit due to unemployment and there will be a reduction of corporate tax. Households

cannot spend more and only spend in the necessary goods, low consumption and low consumer spending. This will lead a decrease in tax revenues from service tax and value added tax (VAT). The government must to increase their benefits cost. For e. g. government will put on more spending in health care and education as the unemployed person cannot send their family in hospitals and in schools.

3. 2 CONCLUSION:

I therefore conclude that the cost of unemployment has a big negative impact in our economy and the individuals surround it. The households, firms and the government should help each other in order to decrease the unemployment. Households should give the maximum factors of production. Firms will use all the factors of production efficiently. Government will monitor the economy vigilantly and must create a faster solutions if there is an increased of unemployment in the country. Government have to know what is the right time to increase and decrease taxes in order to balance the economy in the country. Furthermore, all individuals have their own responsibilities in order to have a full employment economy.

Question No. 5:

4. 0 INTRODUCTION:

Unemployment causes if the economy is having a depression and recession. It affects all the individuals in searching a job. If you resign from a job, the gap between the moment you resign and the time that you started to work again is also unemployment. There are some causes of unemployment. These are frictional unemployment, structural unemployment, technological unemployment, regional unemployment and seasonal unemployment.

<https://assignbuster.com/flow-of-income-between-households-and-firms/>

4. 1 BODY:

4. 1. 1 Causes of Unemployment

Frictional Unemployment –This type of unemployment happens when people is searching for a job. When the firm takes time to choose which candidates qualified the most for a certain job, those candidates are unemployed and the period of time of waiting is called frictional unemployment. For e. g. fresh graduate students they must take some time finding a job before they can find one.

Frictional unemployment happens due to factor immobility. These are geographical immobility and occupational immobility. Geographical immobility happens when an employee do not want to be relocated to another place. For e. g. a manager in a company may refused to be relocated to another state if he is going to be apart from his family.

Occupational immobility happens when the employee cannot perform well to his job due to poor knowledge and lack of experience. For e. g. a fresh graduate engineer cannot fully comprehend the work due to his lack of experience.

Structural Unemployment –Happens when the economy in the country changes and it is experiencing a rapid growth while other industries are tightening and need to have a closure. For e. g. last time Malaysia in 1960's they focus in agriculture, 1980's focus in manufacturing companies and in 2000 they already focus in tourism. Structural unemployment happens if there is a change in demand trend, taste and preferences. For e. g. in 1980's there is a demand of leather jackets but as the changes in fashion occurs nowadays people prefer wear cotton than leather.

<https://assignbuster.com/flow-of-income-between-households-and-firms/>

Technological Unemployment –Happens when there is a rapid growth of technological changes in the country. By this the firms will prefer to use machines than labourers. Automation will be use by the firms in order to increase productivity. For e. g. the machine can produce 500 outputs a day while in the other hand 10 labourers can produce 500 outputs. The firm will prefer to have a machine than more labourers. Redundancy will occur to the excess employees.

Regional Unemployment –Happens when a particular region is having unemployment. For e. g. a state is having a sea port in almost 15 years of operation suddenly they have a closure due to the changes of economic growth. They want to open an airport. The employees in the sea port will be unemployed and will switch to a job. However by switching a job they must undergo some training courses to coup with the new technologies.

Seasonal Unemployment –Happens when there is changes in weather and season in the country. Some countries are having four seasons like Europe. They have winter, spring, autumn and summer. Some jobs cannot carry if it is winter season and so on with the other seasons. For e. g. during winter in Europe the oceans freezes the fishermen cannot do fishing so they will wait until the block of ice in the oceans melt. Another example if it is raining for a month, the farmers cannot plant crops in the fields they will wait until the rain stops to enable to plant crops.

CONCLUSION:

I therefore conclude that having a full knowledge about the causes of unemployment will helps us create solutions on how to prevent to be

unemployed for a long period of time. Individuals should prepare by upgrading themselves and do some training courses. By doing these it can helps us preparing ourselves specially the rapid changing of our technology. It is very helpful if individuals have their own part time job during seasonal unemployment. Fishermen can do some mechanics during winter season. The main point is that people do not want to be unemployed, one good solution is that people can reach out to the government programs so that they can coup up with the uprising economy in the country.