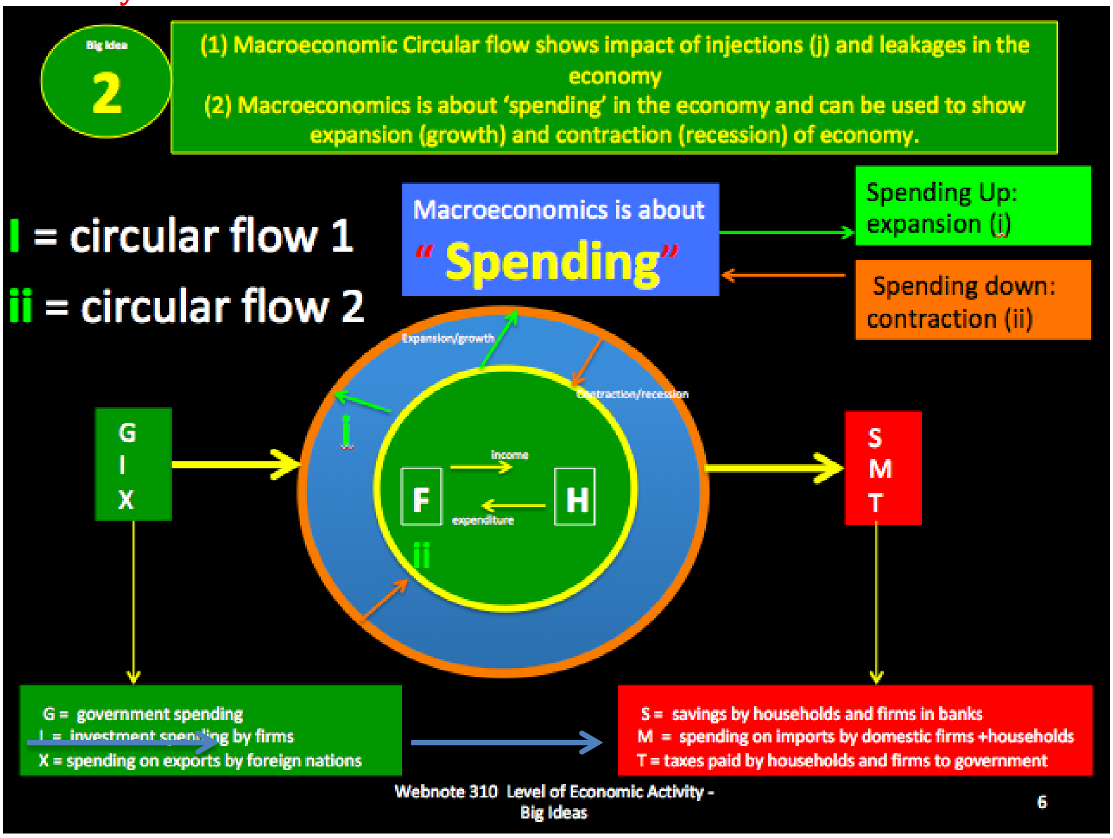
Macroeconomic Circular flow of income: How does microcredit and FDI affect the economy?

Macroeconomy circular flow of income: what grows and shrinks an economy?



Macreconomic circular flow of income showing injetions and leakages is a very useful diagram to show key events in an economy. Essentially the diagram can be used to show expansionary policy (Circular Flow i to ii) or contractionary policy (Circular Flow ii to i). The government has a key role here and if you study the injections and leakages in the diagram you will see that government spending (G) and taxes (T) have a huge influence in the size of the economy. However the market is also important. Investment (I) and Exports (X) along with Imports (M) and Savings (S) are all carried out in economic markets. It is then a useful diagram to show and understand how the government and the market plays a part in achieving economic growth (expansionary policy) and also what the government can do if the economy is in economic recession (falling GDP). In this case the government could increase G or reduce T. Or maybe the economy has a problem with rising inflation. In this case the government can also take action to help the economy to recover. It can reduce G or increase T to bring about a reduction in spending and therefore there will be less upward pressure on prices due to less scarcity.

Remember: Injections: Grow/expand economy Leakages: Shrink/contract the economy.

Example: large investment by multi national corporations make the economy bigger. These could be recorded as I (investment) spending in the marcreconomic circular flow of income.