



## Circuits

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Circuits can be used as a tool to show the economic relationships, that is, the flows between economic actors.

These flows involve transactions that are regulated by contracts.



Each actor in the circuit performs a number of activities as per the relationship one is part, and has obligations/expectations as per the contract involved. These actors include

- the individual,
- the business organization
- the state.

... and the fortune teller?

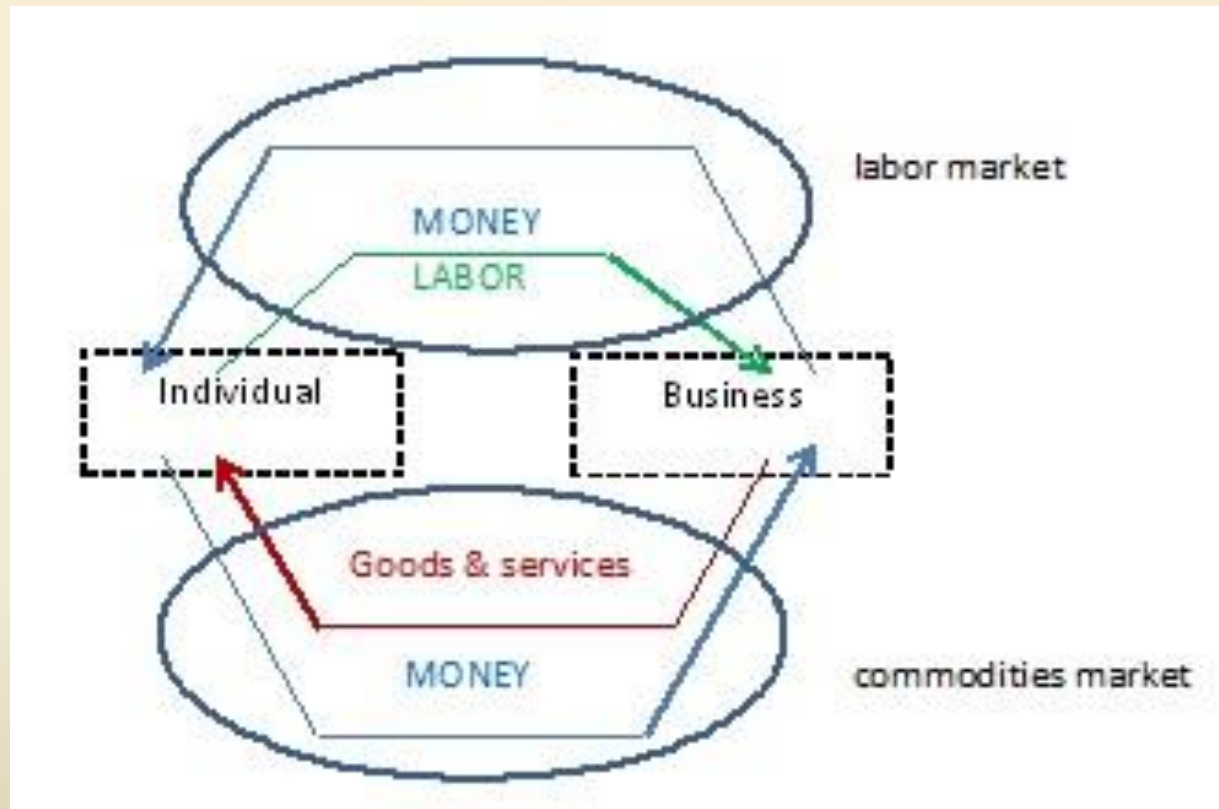


A circuit is underpinned by a principle and an assumption.

1. In principle *what is earned in the economy is equivalent to what is spent in the economy.*
2. The assumption that the circuit makes is the equivalence between the *goods flow*, and the *earnings flow*.



## Circuit 1: microcircuit



## a/Features

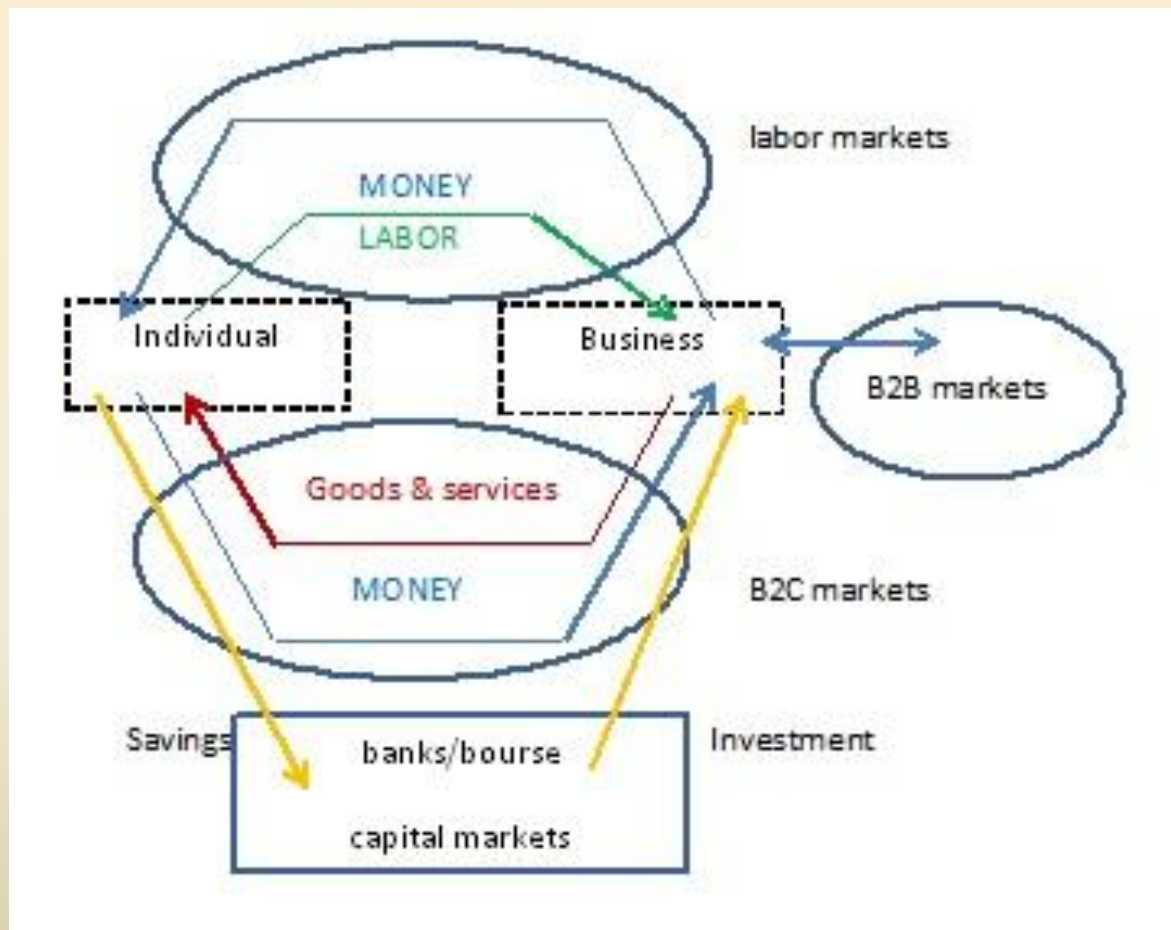
- Labor markets: agreement over wage and type of job through individual employment contracts
- Goods markets: agreement over price and type of commodity through contracts of sales (tangibles e.g. food), mandates (services e.g. medic) and work (services e.g. painting a house)

*The fact that employment contracts are individual clashes with the traditional economic concept of the household*

## b/Extensions

Considering that there is also a B2B market where firms obtain primary resources to use in their production systems (e.g. machines, furniture) involving sales contracts, the circuit can be expanded to include supplier markets.

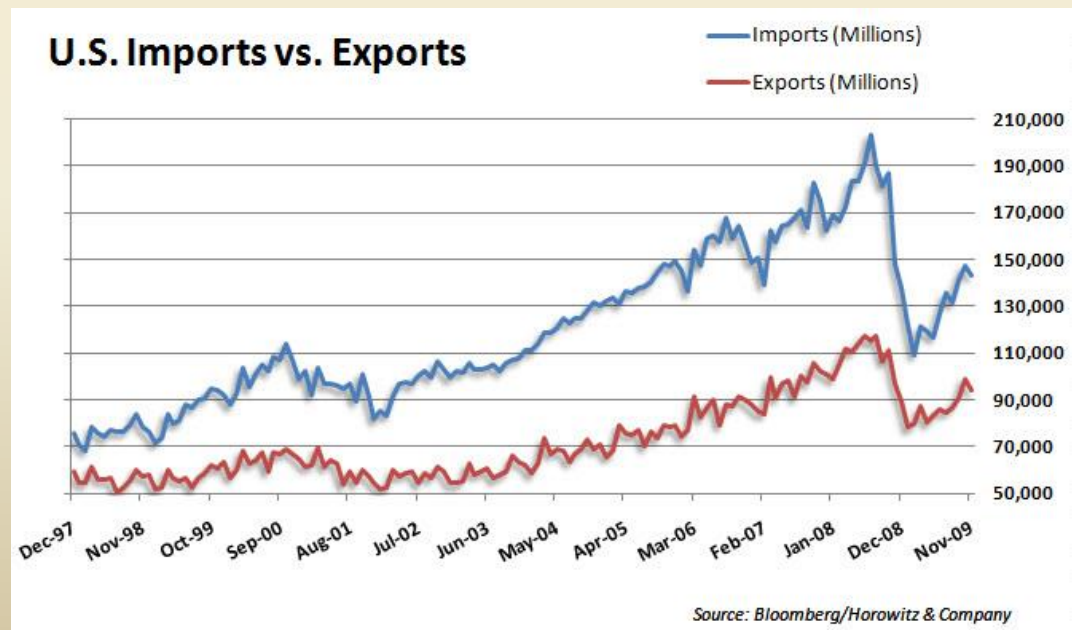
Money not spent immediately on consumer goods & services is saved by the individual in banks or invested through other financial institutions belonging to capital markets. This money helps establish credit for purchase and investment purposes by the business to allow either increase production or/and replace old machinery.





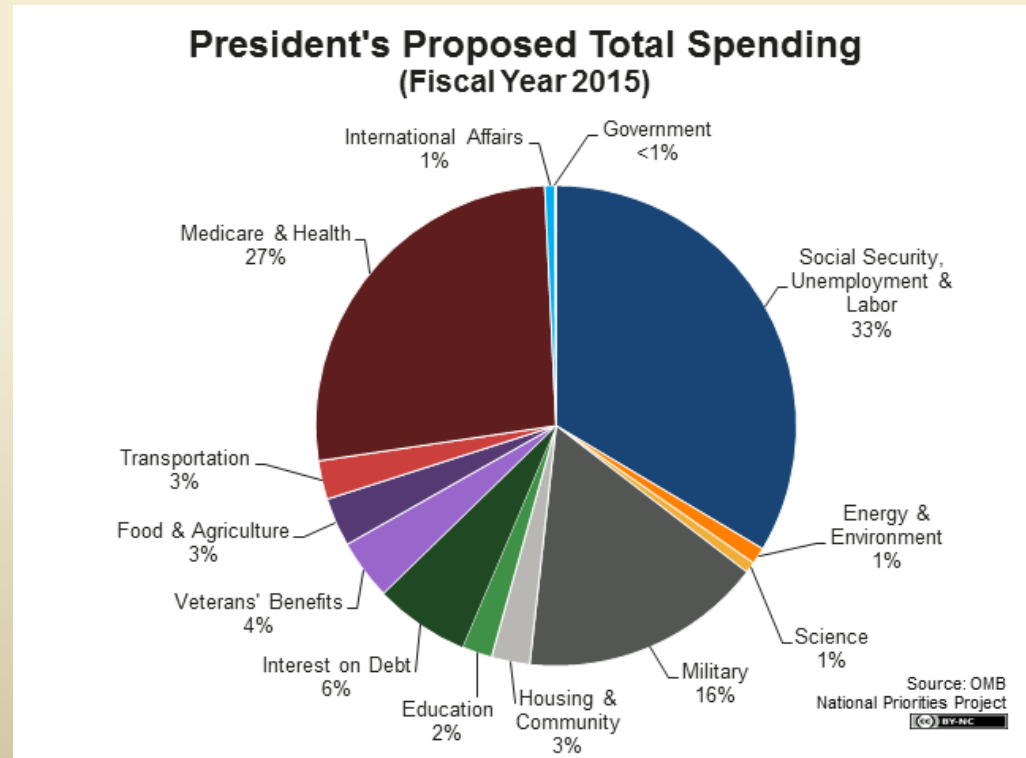
Considering that both the individual and business organisations are in relationship with foreign economies, a part of their earnings will be spent on imports.

The degree of import expenditure has an important impact on the domestic economy.

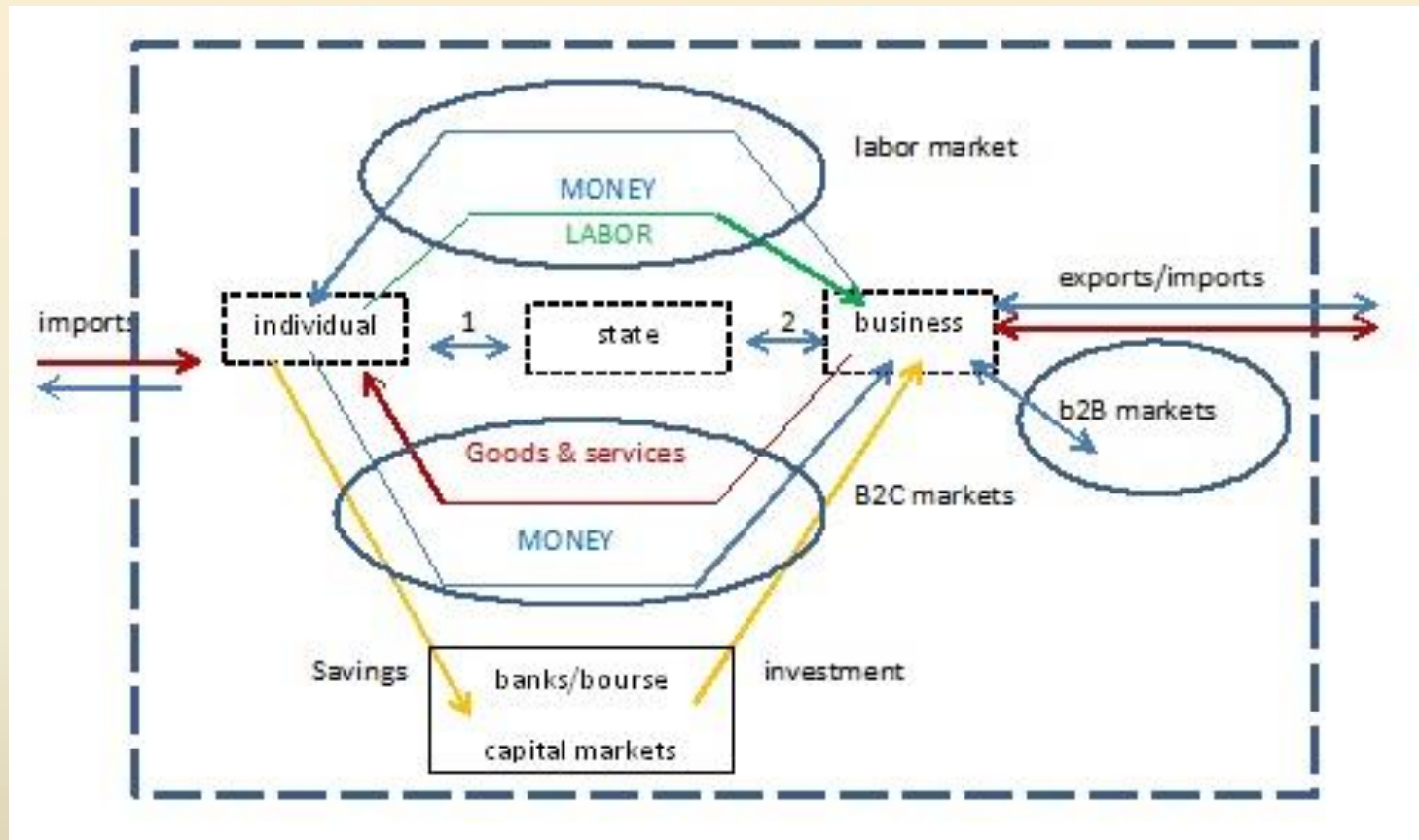


Another part of the earnings will be used in the form of taxes to finance government expenditure as per the role the state has been set to play, and in particular to provide the economy with

- the necessary infrastructure
- public goods
- benefits.



## Circuit 2: macrocircuit



Note that the diagram represents the relationship between the individual, the business and the state, which is different from considering the citizens as an aggregate and the business industries as an aggregate.

If the former perspective is closer to the experience of those concerned and who tend to see the state as an aggregate whose figure-head is the head of state, the latter perspective is taken by the state. Hence the antagonisms!

## Reading – *Real World Micro* (Dollars & Sense)

1.1 ideological bases of free markets

1.2 ideological bases of free markets especially the “invisible hand”  
thesis