Circular Flow Model

Essential Question: How do goods, services, and the factors of production circulate through a market economy?

Warm Up

1. Review: What are the factors of production? Describe each one.

2. Why do people work?

3. What do you hope to purchase with your future earnings once you start your first career?

Circular Flow Model Background

Economists use the circular flow model to show how resources flow through a market or market-based economy. The assumption is that households provide the factors of production (land, labor, capital) to the firms. Firms use those factors to create goods and services which households purchase.

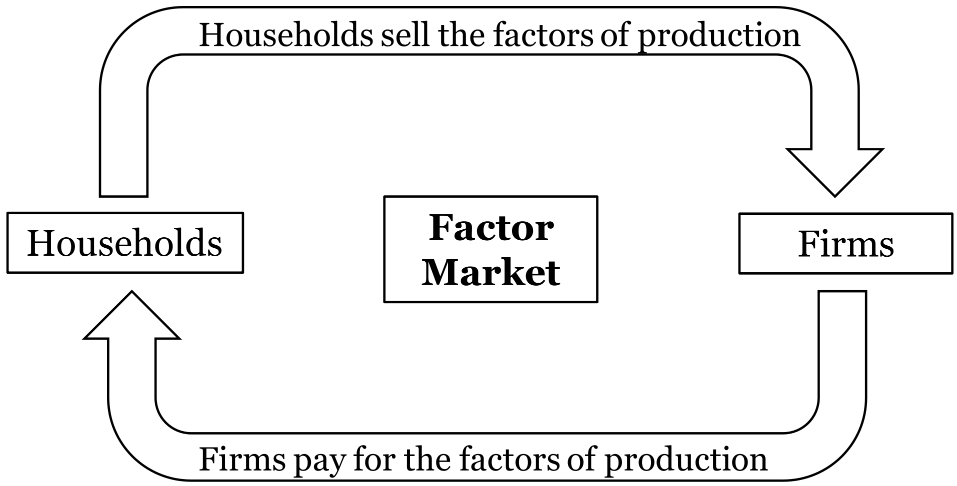
Circular Flow Model Vocab

- Households: individuals or groups living together
- Factors of Production: land, labor, capital
- Firms: businesses that use the factors of production to make goods and services
- Product Market: Firms sell goods and services to households
- Factor Market: Households sell their factors of production to firms (example: allowing a firm to rent your land)
- Factor Payments: money paid to households
- Circular Flow Model: shows the flow of goods, services, and factors of production between households and firms in an economy

Circular Flow Model

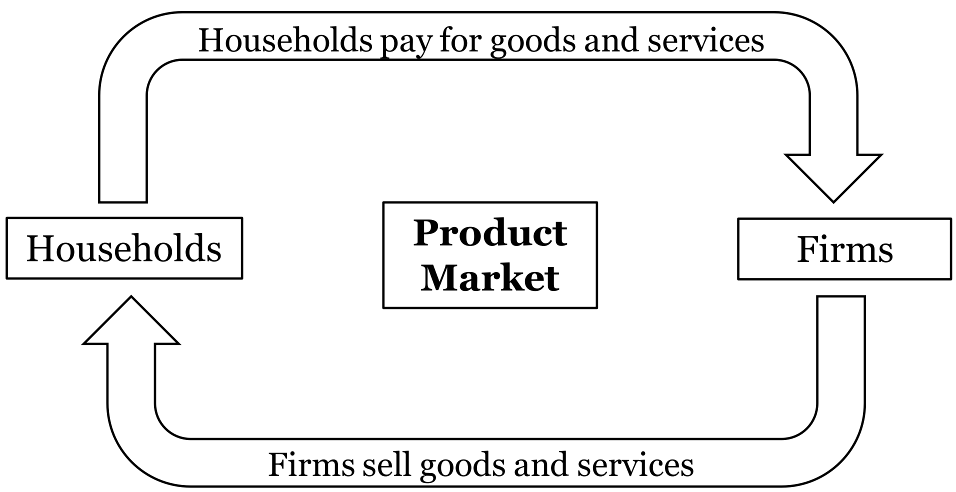
Directions: Observe each circular flow diagram below and then describe your own real world, specific example using real factors, goods and services.

The Factor Market



Your Own Example of the Factor Market:

The Product Market



Your Own Example of the Product Market: