

Yogoda Satsanga Mahavidyalaya
B.COM Sem III
Subject: Macroeconomics
Topic: Circular flow of Income-Four Sector Economy

Circular Flow of Income in a Four-Sector Economy

- A four-sector economy consists of:
 - (a) Households,
 - (b) Firms
 - (c) Government and
 - (d) Foreign sector.

(A) Household Sector:

- (a) Households provide factor services to firms, government and foreign sector. In return, it receives factor payments.
- (b) Households also receive transfer payments from the government and the foreign sector.
- (c) **Households spend their income on:**
 - (i) **Payment for goods and services purchased from firms.**

(ii) **Tax payments to government;**

(iii) **Payments for imports.**

(B) Firms:

(a) Firms receive revenue from households, government and the foreign sector for sale of their goods and services.

(b) Firms also receive subsidies from the government.

(c) **Firm makes payments for:**

(i) **Factor services to households;**

(ii) **Taxes to the government;**

(iii) **Imports to the foreign sector.**

(C) Government:

- Government receives revenue from firms, households and the foreign sector for sale of goods and services, taxes, fees, etc.
- Government makes factor payments to households and also spends money on transfer payments and subsidies.

(D) Foreign Sector:

- Foreign sector **receives revenue** from firms, households and government for **export of goods and services**.
- It **makes payments for import of goods and services** from firms and the government.
- It also makes **payment for the factor services to the households**.

FINANCIAL SYSTEM

- **The savings of households, firms and the government sector get accumulated in the financial system.**
- Financial system invests money by lending out money to households, firms and the government.
- The inflows of money in the financial market are equal to outflows of money.
- It makes the circular flow of income complete and continuous.

The circular flow of income in a four-sector economy is shown below:

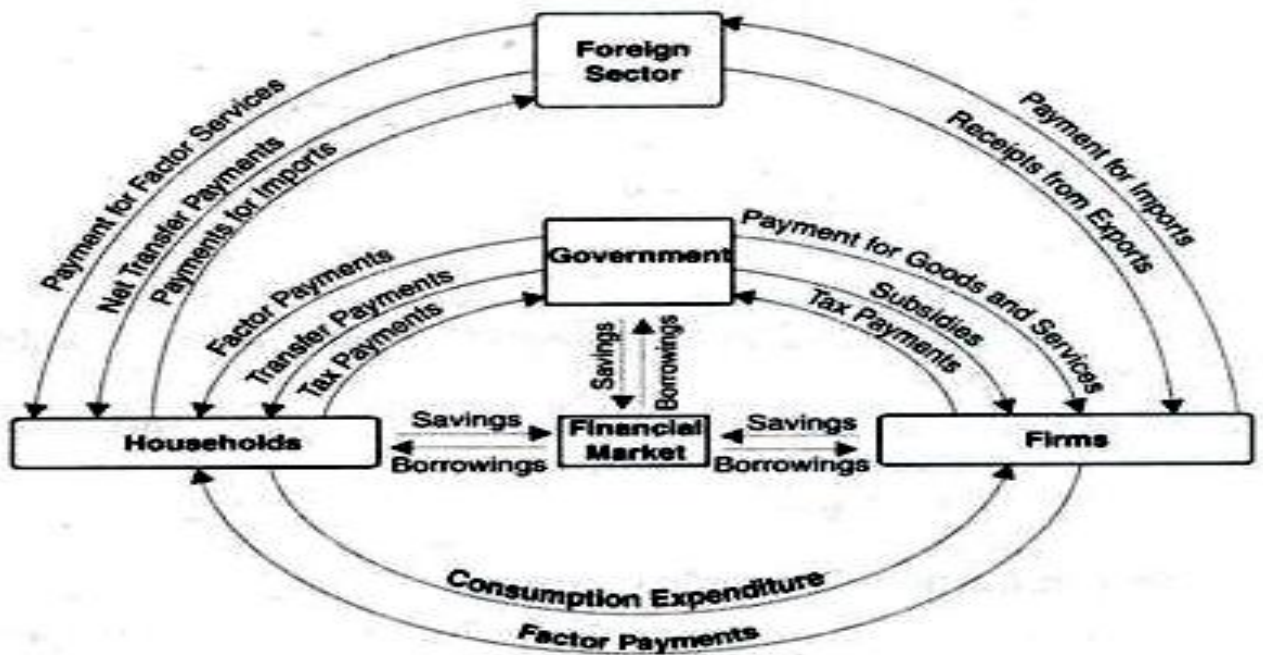


Fig. 1.7

Circular flow of income in a four-sector economy.

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