The Magic of Markets:
How Trade Creates Wealth

INTRODUCTION

This lesson involves students in a trading simulation designed to illustrate a complex marketplace in which goods are traded. Students use this experience to investigate the conditions that encourage or discourage trade among individuals.

Trade is the voluntary exchange of goods and services. The decision to trade is made because two or more parties involved in the exchanges expect to gain. When one or both of the trading partners believe they can no longer gain from trading, the exchanges will stop.

CONCEPTS

- Trade
- Voluntary Exchange
- Incentives
- Costs
- Benefits

MATERIALS

- A variety of dollar store items (one for each student)
- Lunch bags (one for each student)
- A marker and flip chart.

LEARNING OBJECTIVES

Students will:

1. Understand that people voluntarily exchange goods and services because they expect to be better off after the exchange.
2. Realize the importance of free trade to increase a country's prosperity.

PROCEDURE

1. Preparation for the simulation:
   Buy a large number of small, easy to exchange items - such as miniature candy bars, small boxes of raisins, inexpensive small toys, package of paper clips, pencils, stickers, and enough small brown lunch bags for each student. Place the trading articles, unequally, in brown paper bags and staple them shut.

2. Before the simulation begins, set the demonstration up by introducing the concept of trade. Tell the students that you have some chewing gum to offer them in exchange for something that they might have. Ask who would like to offer something in exchange for a piece, or several pieces of chewing gum. After a transaction ask students who lost and who gained from the exchange. *(Both parties won. Both people gave up something that had lesser value to get something of greater value to them. Hence, they both gained.)*

Or: Describe the following situation to the class. Imagine that a teenage music lover walks into a music store, picks out the latest CD by his favourite artist and pays the owner $18. Who gained and who lost in this situation? *(Both people gained in the trade. The music lover gave up something of lesser value, $18, to get something of more value, the CD. The owner gave up something of lesser value, the CD, to get something of more value, $18. Both the music lover and owner ended up with something of more value to them. Hence, they both gain.)*

3. Ask, "Why do people trade?" Put some student responses on the board and indicate that these responses are hypotheses. Explain to the class that today's activity will give the students information and experience with which to test the hypotheses.

4. Randomly hand out a small bag to each person in the room. Explain that the items they receive are gifts to them. Tell them you wanted to please them, although you are aware they might not have received something they like. Ask students to open their bags and look at the object WITHOUT removing it from the bag or showing anyone else. Each student is to rate his/her initial satisfaction with the object the bag. Using a 1 to 5 rating system, with 5 being very high satisfaction, *ask for a show of hands for each rating 0, 1, 2, 3, etc., and record each tally on the board. Tell them to be very honest, otherwise the experiment won't work.*

5. Tabulate the scores of all players. This number represents how happy the players are as a group with their items. Write this number on the board and report it to the group.

Base Group Rating (with no trade)	

6. Now allow a round of trade. Ask each player to turn to the person on their left and right ONLY to engage in trade. The person may have to creatively market their item, or split their items up (eg. pack of erasers) especially if they have ended up with something less desirable. Allow approximately two minutes for trading.

7. After the trading round is complete, have students once again rate their satisfaction with the items they have. They may have a new one or they may be stuck with their initial one, in which case their rating may not improve. Again tabulate the group rating. This number should be higher than in the first tabulation, indicating that, in the second round with limited trade, the players as a group are slightly happier with their items.

Round 2 Group Rating (with unlimited trading)	

8. Now you allow a second round of trade. Players are free to trade items with whomever they like. Allow approximately five minutes for trading. Once trading has ceased, again ask players to rate their items and tabulate the group total. *(All students may change their ratings, even if they have never traded.)* The new total should be even higher than previous two ratings indicating that opening up the trade barrier has made players even happier.

9. Record the numeric results of the experiment on the board (the three ratings).

DEBRIEF

1. How many people made trades? Ask several traders what they traded and why. *(Generally most of the students will have made trades; however, there will be a few who were either satisfied with what they had and did not trade, or who had something that no one would trade to obtain.)*

2. Which items were most popular? Which were least popular? Why?

3. Did anyone trade more than once? Why? Did anyone not trade? Why? *(Several people should have made numerous trades.)*

4. Discuss the tally of satisfaction points on the board. How might we explain the changes in satisfaction from round to round? *(As the number of potential trading partners increased, more people were able to find and trade for something they liked better. Thus, the total level of satisfaction increased as the size of the trading group increased.)*

5. Why did you trade? (*People trade to get something of more value by giving up something of less value.)* Who gained and who lost? (Both parties expected it to be a win-win situation otherwise they wouldn't have made the transaction. Maybe some of them changed their minds later as they saw other more desirable items.)

6. Were all of you happy with your trades? *(Probably not. Students who had little to trade may not have been pleased. Students who couldn't find what they wanted may have been dissatisfied. Students who traded and then realized they missed a better trade may have*

been unhappy. Finally, students who either underestimated the costs of a trade or overestimated its benefits or both—may have been unhappy.) Trading doesn't guarantee happiness. Economists merely maintain that trade will continue if people anticipate that they will be better off after the trade if they had not traded at all.

7. Did the trading behaviour confirm or contradict the hypotheses we listed at the beginning of the activity? *(Often the initial responses that students may have put on the board as to why people trade are "to get something they don't have, or to take advantage or sucker someone." Students should see that trade only takes place when both parties expect to gain.)*

8. If we were to observe twenty people buying items at a grocery store, what could we conclude about their gains and losses? Their wealth? *(Each transaction takes place because both parties expect to gain. If one party does not expect to gain, there is no transaction and we would have nothing to observe! Therefore, we observe people trading money for groceries we can conclude their wealth and the wealth of the grocery store has increased.)*

CONCLUSION

Voluntary exchange occurs only when all participating parties expect to gain. This is true for trade among individuals or organizations within a nation, or in different nations

Without trade barriers people are able to take full advantage of the opportunities of the international marketplace. People can buy better and cheaper goods and services, sell to the most promising markets, choose from the best investment opportunities in the world. Openness to foreign competition boosts productivity and living standards, shifts resources from less productive into more productive uses, and makes more available for less.

The magic of markets combines procedures from lesson plans developed by the Foundation for Economic Education (www.fee.org), the Foundation for Teaching Economics (www. Fte.org), and the Fraser Institute.