**THE MARKET MECHANISM**

**Teacher's Guide**

This is a simple simulation designed to explore the market mechanism and in particular the processes that underpin each transaction between buyer and seller. It is quick and fun but introduces some very powerful ideas.

**Subject content**

The essential proposition is that any and every transaction in a market depends on a win-win expectation for both sides. The terminology here is a matter of preference. The buyer is gaining 'value-for-money' (or consumer surplus) while the seller makes a profit (or 'producer surplus'). Both sides are driven by this search for gain or profit.

The inner logic of buying and selling is an important idea but can be taken at two levels:

***Basic level***

The buyer judges the value of the product to be higher than its price. The seller judges the price of the product to be higher than its cost. Both sides expect a surplus or profit to arise from exchanging the price for the product or the product for the price. This is a basic condition for any transaction to take place. If either side does not expect a gain, then no deal is possible.

***Advanced level***

Making a gain from a transaction is a necessary but not sufficient condition for longer term trading to take place. Enter opportunity cost. The consumer requires their estimated value of a product not only to exceed its price but also the opportunity cost of its price. Given a limited budget, even a product that is 'worth the price' will not be purchased if there is another product offering better value-for-money.

We can see that when a consumer purchases a bag of Walker's Salt and Vinegar Crisps, they are announcing a 'winner': the best value available in a given marketplace. Similarly, the product is also Walker's 'winner' in the contest for resources, defeating other potential products such as the Lamb and Mint Sauce flavour that was tried and discontinued.

The surplus or profit taken away from a transaction by buyer and seller has vital business consequences. The buyer's perception of having enjoyed value-for-money makes for repeat purchases and builds reputation and long-term brand value. The seller's achievement of profit triggers further production and ongoing commitment to the product.

**Classroom practice**

To run the simulation, the students should divide into groups of three. The groups each need a table and three chairs. One student sis the buyer, one is the seller and the other acts as an observer with responsibility for recording what takes place.

Note that the seller should be regarded as 'Mr/Ms Walker'. It should be explained to the students that for these purposes, the distribution chain and its costs will be ignored.

*It is much more effective to use the real product and some real money.*

**Walker's Crisps**

Founded by Henry Walker in Leicester during the 1880s, the company began making potato crisps in 1948. Flavoured crisps were introduced in 1954. Later, Walkers was bought by US company Nabisco and sold on to Pepsico in 1989. It then became a top national brand selling over 10 million bags per day and is now worth over £450m

Buyer and seller sit at opposite sides of the table with the

observer at one end. The seller is given a bag of Walker's

Crisps and offers it to the buyer at 50p. There is unlikely

to be a sale. It is offered again at 45p and then

at a price decreasing in 5 pence stages until a sale is

agreed. 'Mr/Ms Walker' should be aware that the total unit

crisps is 20p. So the finally agreed price must be 25p or

more.

The students should take time over each offer price and

give the observer a chance to record reactions. S/he

should ask 'Why are you not buying?' and record the

answer.

When agreement for a transaction is reached, there will be a moment of exchange – crisps for money. At this point the observer should call 'Stop!' and freeze the action. Both buyer and seller should be asked exactly why they are making the exchange of money for crisps or vice versa. Answers should be as honest and thoughtful as possible. The observer makes appropriate notes...

Involving the whole class, a list on whiteboard or flip chart can then be compiled that highlights the motives of buyer and seller in the simulated transaction. These should illuminate the ways in which a product adds value and the role of profit among other business objectives.

**THE MARKET MECHANISM**

**Student's guide**

**Subject idea**

Everyone is used to buying things that they want – and not buying things that they don't think are good enough value for money.

This is a simple activity designed to explore how the market works and in particular the processes that drive each transaction between buyer and seller.

The essential idea is that every deal in every market depends on a win-win expectation for both buyer and seller.

This can now be put to the test...with a bag of Walkers Crisps.

**Instructions**

When asked, divide into groups of three and put chairs either side of one table with one further chair at the end. Decide who will be 'Mr/Ms Walker', the buyer and the observer.

The buyer and seller should sit at opposite sides of the table and the observer at the end. 'Mr/Ms Walker' has the bag of crisps and offers it to the buyer at 50p. Assuming that this price is rejected, the observer should ask why and keep a record. Keep offering the crisps at 5p less than the previous price until a deal is struck. 'Mr/Ms Walker' should be aware that the overall unit cost of the crisps (including variable and fixed costs) is 20p. The observer must keep a record of the reason why each offer is rejected or accepted.

When a price does finally lead to a 'buy' decision, the observer should call 'Stop!' and ask each side in the transaction exactly why they are buying or selling. Try to get to the real reason and dig down as deep as possible! Again, keep notes.

A class discussion will follow and the logic of buying and selling will become clear. Think carefully about how the sale of a product affects the *future* behaviour of both buyer and seller.