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Children's understanding of market forces

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Abstract

This study investigated children's understanding of the effect of changes in supply and demand on the exchange value of everyday goods and services. Sixty-four children (aged 6, 8, 10 and 12) were told short stories and asked to predict whether certain circumstances would affect price or exchange rate. Explanations for their answers were also elicited and scored. Two dimensions were manipulated in the stories: Money vs. barter, and supply vs. demand. A second study ($N = 64$) sought to dissociate effects of supply and demand from direct and indirect causation. It was found that children can understand supply and demand to a larger extent than was thought, and that demand effects are easier to understand than supply effects. The findings are interpreted in terms of the relative complexity of the mechanism in each case.

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1. Introduction

This study investigates children's understanding of two main economic forces, supply and demand. As economics textbooks explain, at prices above the equilibrium

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there is *excess supply* while at prices below the equilibrium there is *excess demand*. The effect of excess supply is to force the price down, while excess demand creates shortages and forces the price up. The price where the amount consumers want to buy equals the amount producers are prepared to sell is the *equilibrium market price*. The present study investigates the development of these notions in children.

The progress of economic understanding in children in general has been traced by several investigators over the years and the reader is referred to these sources (Berti & Bombi, 1988; Berti & Grivet, 1990; Danziger, 1958; Furth, 1980; Furnham & Cleare, 1988; Jahoda, 1979; Leiser, 1983; Leiser, Sevón, & Levy, 1990; Stacey, 1982; see especially Webley, 2005, for a recent review of the literature, which covers well the issues of interest in this study).

We will stress here several prominent features of this development. Progress in understanding is characterized by a transition from isolated partial systems, to an increasing integration of understanding; by a transition from understanding of economics as motivated by ethical considerations to a realization that economics has its own logic, distinct from moral considerations (Leiser et al., 1990; Sevón & Weckström, 1989), and from one that relies on the motivation of individuals, to one based on an appreciation of the aggregate effects of the actions and desires of groups of people (Leiser, 1983; Leiser et al., 1990).

Berti and Grivet (1990) were the first to address the question that will concern us, namely the understanding of the effect of supply and demand on prices. These authors studied children's understanding of the relations between changes in supply, demand, and prices, by telling stories about a small and isolated village, where ''each inhabitant produces and sells just one commodity''. The stories involved the changes (increase or decrease) in one out of the three variables and the children (aged 8–13) were asked to tell ''what she/he thought would happen afterwards, what customers and sellers would do''. When required, the experimenter offered a cue by explicitly asking about the variable affected (e.g., ''will the price remain the same or will it change?''). Children understood the effect of price changes on purchases long before they understood the converse effects of changes in supply and demand on prices. There was not a clear pattern in the relative difficulty of answering questions involving a change in demand and a change in supply. When children aged 8–9 were asked to explain their prediction, it became clear that they failed to separate moral from economic considerations and typically countenanced changes in prices only as a way to ease life for poor people. People were thought to want to earn enough money to live on, not to maximize profit. These last results by Berti and Grivet (1990) were obtained in a working class area of Torino, Italy, and form an intriguing contrast with the findings by Thompson and Siegler (2000), to which we return below on another topic. Working with middle-class children in a Catholic school in Pittsburgh, USA, they report that, out of several possible goals relevant to economics, preschoolers really only understood the concept of desire to acquire valued goods (i.e., greed), whereas the 7 years old had some understanding of the additional economic principles involved (seeking profits, acquiring goods inexpensively, or competing successfully with other sellers).