THE GREAT TULIP BOOM

INTRODUCTION

History The tulip was introduced into western Europe from the Middle East in the middle of the 1600s. It flourished in the Dutch climate and became a local favorite. As the popularity of tulips increased, the price of tulip bulbs soared. A single tulip bulb sold for hundreds of times the price of a pig or a sheep and a thousand times higher than the price of a bushel of wheat.

Mystery Why would people choose to spend a fortune on a single tulip bulb?

Economic History In the Netherlands in the 1600s, there were many wealthy people with money to invest. When the value of rare tulip bulbs began to rise rapidly, people began to buy them, not to use in their own gardens, but rather because they believed they could sell them at higher prices than they paid; in other words, they were “speculating” in tulip bulbs. Eventually tulip prices rose so high that insufficient numbers of buyers were willing to buy. Those who owned tulip bulbs tried to sell them before prices fell, but when many bulbs were offered for sale at the same time, prices fell. Each succeeding reduction in price caused more people to attempt to sell the bulbs they owned, and tulip bulbs soon became all but worthless. Many who had speculated in tulip bulbs were ruined financially.

CONCEPTS

Financial Investment
Rate of Return
Risk
Speculation

OBJECTIVES

◆ Recognize that people invest in order to earn a return on their investment, and that higher rates of return are usually associated with higher risks

◆ Understand that expected demand can drive the price of a product extremely high, as people buy with the hope of reselling at a higher price, but that speculative prices can collapse either because people stop believing that the price of the product will continue to increase, causing demand to fall, or sellers liquidate their stocks, causing supply to fall

LESSON DESCRIPTION

The teacher displays the prices of many goods in the 1600s in the Netherlands to prices paid for rare tulip bulbs during the Great Tulip Boom of the 1630s. Students perform a simulation of the boom and write a short essay expressing their personal feelings about the relationship between risk and rates of return.

TIME REQUIRED

One class period

MATERIALS

Display version of Visual 1.

★ One envelope for each student. Five of the envelopes should contain one “tulip bulb” each, made from the pattern in Activity 1; the rest of the envelopes should contain seven ten-florin pieces made from the same activity sheet

★ Enough copies of Activity 2 to give one copy to each student

PROCEDURE

1. Ask students how much they would be willing to pay for a single tulip bulb. (Most tulip bulbs today sell for no more than 50 to 75 cents.) After receiving various answers, tell them that at one time, some people in the Netherlands were willing to spend their entire fortunes to purchase one or two tulip bulbs.

2. Display Visual 1. Explain that the florin was the Dutch unit of currency in the 1600s, that a “last” was approximately 80 bushels, that a “tun” was equivalent to about 2,240 pounds, and that a “hogshead” was about 63 gallons. Ask students to guess what the price of a rare tulip bulb was in Holland in the 1630s. When they have made several guesses, project“2,500 florins” on Visual 1 after “one rare tulip bulb.” Tell students

★ all students–basic course material
■ average and above average students

that in the 17th century some Dutch people spent their entire fortunes to purchase one or two bulbs. Ask students why people might be willing to spend so much money in a way that seems foolish. (As the price of tulips rose, people bought bulbs because they believed they could sell them for more than they paid. In other words, they *speculated.*) Explain to students that a *speculator* is one who buys some commodity, not to use it, but rather because he or she believes that the commodity can be sold for a higher price. Speculators often make a great deal of money, but they also risk losing a lot of money. Explain that risk is often associated with a high *rate of return.* (A rate of return is the percentage earned on investment.) For example, today most savings deposits in banks and thrift institutions are insured against loss, but they usually pay lower rates of return than do stocks and bonds.

3. Ask students what they think eventually happened to the price of tulip bulbs in the 1630s. Students will probably answer that the price fell at some point. If this answer is given, ask students to explain why the price fell. (Speculators stopped buying and tried to sell when they felt the price would go no higher.) Tell students that they are going to act as speculators themselves, to see what happened to the price of tulips.

4. Designate one student to record prices on the board. Distribute envelopes containing either a tulip bulb or seven ten-florin pieces to the other students. Explain to students that they are speculators who want to buy tulip bulbs in order to resell them at higher prices. When the simulation ends, students who currently hold the tulip bulbs will receive 2 extra credit points for each bulb, while the three students with the greatest number of florins will receive 5 points each. Explain that you will allow at least 15 min-utes for buying and selling bulbs. After that, the simulation may end at any time. The best way to earn a lot of florins in this simulation probably is to buy tulip bulbs and then sell them for higher prices, but there is a risk that at some point people will stop wanting to buy bulbs or will be will-ing to buy them only at lower prices. Also explain to students that, whenever someone *sells* a bulb, he or she must report to the recorder the price that was paid. (Buyers should **not** also report prices, as this would result in double-counting each transaction.)

5. As students begin to buy and sell among themselves, the recorder should write each price that is paid on the board. Announce the time when 5 minutes have passed, when 10 minutes have passed, and when 15 minutes have passed. Have the recorder make a special mark on the board beside the last price recorded before each time announcement. Allow the simulation to continue for a time, and then end it.

6. Give 5 extra credit points to the three students with the most florins and 2 points for each tulip bulb that a student has. Point out that the students with the greatest number of florins took a speculative risk by buying the bulbs, but that it paid off for them when they were able to sell them at higher prices. Ask students who have bulbs whether they were satisfied with a small gain (two extra credit points), or whether they would rather have sold their bulbs in hope of making more money.

7. Examine the prices recorded on the board. Have students analyze the prices paid to see if they can determine a pattern. (Ideally, prices will rise early in the game and fall as the game nears its end.)

CLOSURE

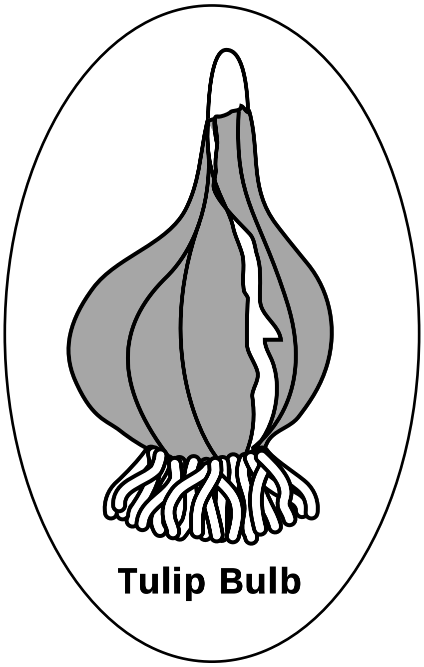
Explain that some people like to invest their money only in very safe ways, while others are willing to put at least some money in investments that are riskier but pay a high rate of return. Distribute Activity 2 and ask each student to write a paragraph or two explaining his or her answer.

VISUAL 1
PRICES OF VARIOUS ITEMS IN THE NETHERLANDS IN THE 1630S

	Florins
Four Lasts of Rye	558
Four Fat Oxen	480
Two Lasts of Wheat	448
Eight Fat Swine	240
Two Tuns of Butter	192
Twelve Fat Sheep	120
One Thousand Pounds of Cheese	120
One Complete Bed	100
One Suit of Clothes	80
Two Hogsheads of Wine	70
One Silver Drinking Cup	60
One Rare Tulip Bulb	?

Prices taken from Charles Mackay, *Memoirs of Extraordinary Popular Delusions and the Madness of Crowds,* 2nd ed., London: Office of the National Illustrated Library, 1852. Reprint, New York: Farrar, Straus and Giroux, 1932, pp. 89-97.

ACTIVITY 1



10 Florins	10 Florins	10 Florins	10 Florins	10 Florins
10 Florins	10 Florins	10 Florins	10 Florins	10 Florins

ACTIVITY 2
HOW DO YOU FEEL ABOUT RISK?

Name ________________________

Imagine that you are a wealthy citizen of the Netherlands in the early 1600s. You have 1,000 florins to invest. You can choose among four investments:

- Put your florins in a bank. The banker will pay you five percent interest. Bank deposits were not insured as they are in the United States today, but your banker has a good reputation, and you feel that your money is safe with him.

- Buy shares in a joint-stock company that exports goods to England and brings back English goods to be sold in the Netherlands. This venture is relatively safe, but there is a chance that the ship might sink, or that the profits of trading will be lower than expected. The joint-stock company expects to make a profit of at least 20 percent.

- Buy shares in a joint-stock company that is sending a ship to the East Indies. The journey over open seas is dangerous and the ship might very well be lost. If the venture succeeds, the joint-stock company may make a profit of three or four hundred percent.

- Buy tulip bulbs. Yesterday an acquaintance of yours sold a rare tulip bulb for 20 times what he had paid for it only a month before.

You may invest your entire 1,000 florins in one alternative, or you may divide your money among two or more investments. Write a paragraph explaining which investment(s) you chose and the reason for your choice(s).