WHAT ARE PREDICTION MARKETS?

Ever hear of prediction markets and wondered how they work? These markets let participants trade contracts tied to future events. Let's dive into the basics of what prediction markets and event contracts are and how they work.

Prediction markets are marketplaces where participants buy and sell contracts tied to the outcome of future events. These contracts, often called event contracts, gain or lose value based on whether a specific outcome occurs. A contract's price reflects how likely market participants believe that outcome is.
(material omitted)
Even though prediction markets involve trading contracts like financial markets do their goal is different and they aren't the same as more traditional investments like stocks, ETFs or bonds.

HOW DO THEY WORK?

Prediction markets are rather unique in how the event contracts are created, traded and paid out. Here are the steps involved in how prediction markets normally work. An event is defined: (text omitted)

1. Contracts are listed (text omitted)
2. Participants trade contracts (text omitted)
3. The event resolves (text omitted)
4. The event contract settles (text omitted)

(text omitted) Prediction market prices are commonly displayed in terms of probabilities. If a contract trades for $0.40, that price can be viewed as implying a 40% chance of success. If the price later moves to $0.70, the implied probability rises to 70%, This dynamic pricing reflects:

- New information (such as data releases or announcements)
- Shifts in sentiment
- Changes in perceived risk

As a result, prediction markets are constantly updating their outlook, sometimes in real time. These probabilities show what the market thinks at a given moment. They aren't guaranteed and can shift as trading activity changes.

Event contract example:
Say there is a prediction market asking: **Will Team A win the game?** There are two contracts:

*__YES__ (Team A wins)

*__NO__ (Team A does not win

Suppose the **Yes** contract is trading at $0.60. This price implies that the market believes Team A has about a 60% chance of winning. The $0.60 paid upfront for the contract is the most the buyer can lose on one contract while w=the most the contract can pay at settlement is $1.

When the game ends, the trading stops:

If Team A wins, Yes contracts settle at $1 and No contracts settle for **$0.**

If Team A loses, No contracts settle at $1 and Yes contracts settle at $0.

Assuming Team A wins, the Yes contracts purchased for $0.60 would settle for $1, resulting in a profit (payout above the purchase price).

WHAT KINDS OF EVENTS ARE USED IN PREDICTION MARKETS?

Prediction markets have been applied to a broad set of topics, including:

- Sports and entertainment (text omitted)
- Economics (text omitted)
- Politics
- Business and technology (text omitted)

The common thread is that each event must have a clearly defined outcome that can be verified by an agreed upon source. This source is typically specified in advance by the exchange. Sources may include league records, certified election results, or statements from recognized authorities responsible for reporting on the event. (Text omitted)

PREDICTION MARKETS VS TRADITIONAL FINANCIAL MARKETS

Prediction markets and traditional financial markets may look similar on the surface, since both involve tradeable products and changing prices, but they are designed for very different purposes.

Traditional Financial Markets

Traditional financial markets are places where people invest in assets such as stock, bonds, ETFs, and often with the goal of long-term growth in income. Key features include:

- **Ownership and investment exposure.** (text omitted)
- **Established markets and regulations.** (text omitted)
- **Value tied to future performance.** (text omitted)

Prediction Markets

Prediction markets are designed to reflect how likely a specific event is to occur. They do not provide ownership or long-term investment exposure. Some key differences include:

- **Contracts tied to defined outcomes. (**text omitted)
- **No ownership or ongoing value.** (text omitted)
- **Value based on event resolutions.** (test omitted)

This information was taken from an article by Fidelity Investments. entitled “What are Prediction Markets” published on Google. Some text was omitted because it was too lengthy to repeat here. Please read the full article to get a complete picture of what prediction markets are, how they operate, and what damage they have the ability to cause, not only to those who have predilections toward gambling, but could very easily become corrupted by insider trading. With bets being placed virtually anonymously, by millions of people who have access to information that is available to only a few people, the temptation to use this information to one’s own advantage could be too tempting to overcome, giving corruption a strong foothold. Be aware of the monster this could become.