Federal Reserve - Lesson Plan

Overview:

The Federal Reserve System is the formal organization for studying and implementing monetary policy.

Objectives:

Students will be able to:

- ❏ Understand the purpose and functions of the Federal Reserve

Background and Information:

- ❏ The Federal Reserve is the central bank of the U.S.

Time:

45 Minutes

Materials:

- ❏ iPad
- ❏ **Gods of Money** app
- ❏ Federal Reserve Worksheets

Educational Goals:

- ❏ To develop an increased understanding of how the U.S. economy works.
- ❏ To understand how U.S. budget deficits contribute to the federal debt.

Activity: Revenue

I. **LECTURE** *10 minutes*

  A. Prior to the creation of the Federal Reserve:
    1. Markets were often unstable
    2. People had little faith in the banking system

  B. The Federal Reserve was created by the U.S. Congress in 1913.

  C. The Federal Reserve is often called “The Fed.”

  D. The Fed is an independent entity.

  E. But the Fed is subject to oversight by Congress.

  F. The Fed’s decisions do not have to be approved by the President or anyone else in government.

  G. Congress periodically reviews the Fed’s activities.

  H. The Fed is headed by the Board of Governors of the Federal Reserve.

  I. The Board of Governors consists of 7 people appointed by the President and must be confirmed by the Senate.

  J. The Board is led by the Chairman.

  K. There are 12 regional Federal Reserve Banks around the country.

L. The Fed's mandate is to promote:
    1. Sustainable growth
    2. High levels of employment
    3. Stability of prices
    4. Long-term interest rates
M. The Fed serves as:
    1. The banker's bank
    2. The government's bank
    3. The regulator of financial institutions
    4. The nation's money manager
N. The Fed also includes the Federal Open Market Committee, better known as the FOMC
O. The Fed has three main tools for influencing the economy:
    1. The Federal Funds Target Rate
    2. The Banks Reserve Requirement
    3. The Fed balance sheet
P. The Federal Funds Target Rate
    1. The Federal Funds Rate is the interest rate at which banks borrow reserves from each other.
    2. The FOMC sets the Federal Funds Rate target.
    3. The Federal Funds Rate influences the cost of borrowing and lending money throughout the U.S. economy:
        a) Home loans
        b) Auto loans
        c) Personal loans
        d) Credit card interest rates
    4. When the Fed changes the Federal Funds Rate:
        a) Lowering the rate means the Fed is putting more money into the economy to encourage growth.
            (1) A lower rate makes it cheaper to buy a house or a car, which encourages spending
        b) Raising the rate means the Fed is slowing the economy to counteract or prevent inflation.
            (1) A higher rate makes it more expensive to buy a house or a car, which discourages spending
Q. The Federal Reserve also sets Bank Reserve Requirements.
    1. The bank reserve requirement is the amount of cash a bank must have in reserve compared to its total assets.
    2. The reserve requirements influences how much money banks can create through loans.
    3. A lower reserve requirement encourages lending and economic growth.
    4. A higher reserve requirement discourages lending and slows economic growth.
R. The Fed also influences the economy by expanding or contracting its balance sheet.
    1. Increasing the balance sheet encourages economic growth.
    2. Decreasing the balance sheet slows economic growth.
S. The Fed tries to sustain steady economic growth.

1. If the economy grows too fast, high inflation may result.
2. If the economy slows too much, a recession may occur.

T. The Federal Reserve is the U.S.'s central bank.

U. Every country or economic union, such as the European Union, has a central bank. Some examples:
   1. European Central Bank (ECB)
   2. Bank of England
   3. Bank of Japan

II. DEMONSTRATION *15 minutes*

A. On the iPad, open the **Gods of Money** app.

B. Tap 'Start' Gods of Money.

C. Tap 'Watch' historical data.

D. Set the Start Date to **Jan 2015**.

E. Tap 'Start >'.

F. When the Budget window appears, close it by tapping the checkmark (in the upper right).

G. Pause the app by tapping the date (in the upper right).

H. In the dashboard, note the Federal Funds Effective Rate.
   1. This is the interest rate paid by banks when they borrow money from the Federal Reserve.

I. In the control panel, note the controls that deal with the Federal Reserve:
   1. Assets & Liabilities
      a) This is the Fed's "balance sheet."
      b) Increasing the Fed's balance sheet encourages economic growth.
      c) Decreasing the Fed's balance sheet slows economic growth.
      d) When the Great Recession started in 2008, the Fed grew its balance sheet rapidly to counteract the Great Recession.
   2. Federal Funds Target Rate
      a) The most important tool in the Fed's toolbox.
      b) The FOMC sets this interest rate.
      c) The Federal Funds Target Rate greatly influences the cost of borrowing money. This rate ultimately determines the cost of getting
         (1) A mortgage to buy a home
         (2) A loan to buy a car
         (3) A personal loan, such as a student loan
      d) When the Great Recession started in 2008, the Fed lowered the Federal Funds Target Rate to near 0% to encourage economic growth, and kept it at nearly 0% for years.
   3. Bank Reserve Requirement
      a) A higher bank reserve requirement discourages lending and slows economic growth.
      b) A lower bank reserve requirement encourages lending and economic growth.
      c) The bank reserve requirement is currently (about) 10%.

III. IN-CLASS ASSIGNMENT *20 minutes*

A. Pass out the **Federal Reserve Worksheets**, one per student.
B. Have students follow the instructions on the worksheet:
   1. Start and run **Gods of Money** to find and record the Assets & Liabilities, Federal Funds Target Rate, Federal Funds Effective Rate, and Bank Reserve Requirement values for 1970 through 2010 at 10-year intervals.
      a) For Assets & Liabilities, be sure to use consistent dollar units, e.g. billions of dollars.
         (1) If a value is in trillions, multiply by 1000 to get billions.
         (2) If a value is in millions, divide by 1000 to get billions.
   2. Create 2 line charts for 1970 - 2010 showing:
      a) Revenue & Expenditures
      b) Budget Deficit & Federal Debt
   3. Use the values to answer the worksheet questions.

IV. HOMEWORK ASSIGNMENT *15 minutes*

A. Assign students to complete the homework assignment on the worksheet.