Gold Standard - Lesson Plan

Overview:

A nation’s money can be backed by a commodity, such as gold or silver, or it can be issued only via the authority of the government.

Objectives:

Students will be able to:

- ❏ Define fiat money and commodity money
- ❏ Understand the advantages and disadvantages of fiat money and commodity money

Background and Information:

- ❏ Gold is a valuable precious metal.
- ❏ In the past, gold coins were used as currency.

Time:

45 Minutes

Materials:

- ❏ iPad
- ❏ **Gods of Money** app
- ❏ Gold Standard Worksheets

Educational Goals:

- ❏ To develop an increased understanding of how the U.S. economy works.
- ❏ To understand the difference between fiat money and commodity money.
- ❏ To understand the advantages and disadvantages of fiat money and commodity money.

Activity

I. **LECTURE** *10 minutes*

A. There are two types of money systems a country can have.

1. Commodity money is backed by a commodity, such as gold.
2. Fiat money is issued by the authority of the government.

B. In earlier times, governments issued gold coins as money. This is called a “gold specie standard.”

C. Later, governments adopted a “gold bullion standard:”

1. Gold coins do not circulate
2. The government agrees to sell gold bullion at a fixed price.
3. Paper money and coins made of common metals are circulated instead of gold coins.

D. Commodity money in the U.S.

1. The U.S. was on a gold standard for many years.

2. From 1944 to 1971 the value of one troy ounce of gold was fixed at $35.
3. The U.S. gold standard was completely abandoned in August 1971.

E. Why use gold? Gold is:
   1. Rare - its scarcity means it holds its value over time
   2. Durable - gold does not physically degrade over time
   3. Divisible - gold can be melted and cast into smaller pieces
   4. Fungible - “gold is gold is gold;” one ounce of pure gold is the same as any other ounce of pure gold, regardless of where it is or when it was mined
   5. Easily identified - solid gold is easily identified by its characteristics:
      a) Color
      b) Density
      c) Malleability (or bendability - pure gold is quite soft)

F. Commodity money
   1. Advantages
      a) Commodity money protects its users from high inflation and hyperinflation.
      b) Commodity money provides fixed international exchange rates
      c) Commodity money prevents a government using deficit spending
   2. Disadvantages
      a) Commodity money prevents a government’s central bank from expanding the money supply to stimulate the economy.
      b) May limit economic growth.
      c) The money supply would essentially be determined by the rate of gold production.

G. Fiat money
   1. In modern times all countries use fiat money.
   2. Advantages
      a) Allows expansion of the money supply which can be used to
         (1) Stimulate the economy
         (2) Rapidly raise money in times of crisis:
            (a) War
            (b) Recession
            (c) Depression
   3. Disadvantages
      a) Can lead to high inflation and hyperinflation
      b) Is not backed by a physical commodity

H. Some people advocate the U.S. going back to commodity money.

II. DEMONSTRATION *15 minutes*

A. Start Gods of Money at Jan 1971:
   1. On the iPad, open the **Gods of Money** app.
   2. Tap ‘Start’ Gods of Money.
   3. Tap ‘Watch’ historical data.
   4. Set the Start Date to **Jan 1971**.
   5. Tap ‘Start >’.

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

C. Pause the app by tapping the date (in the upper right).
D. In the dashboard, note the price of Gold: $35, where it has been fixed since 1944.
E. In the control panel, note the Gold Standard switch in the ‘On’ position.
F. Resume the app by tapping the date.
G. When the Gods of Money Guide appears:
   1. Tap the blue arrow to expand it
   2. Tap the ‘X’
   3. Tap ‘Turn off Guide.’
H. Watch the Gold Standard switch.
   1. At what date is the Gold Standard switch set to ‘Off?’ (September 1971)
      a) (The actual date the U.S. completely abandoned the gold standard was August 15, 1971.)
   2. When the gold standard was abandoned, the U.S. changed from commodity money to fiat money.
   3. With fiat money, the price of gold is allowed to float; that is, the market sets the price of gold.
I. Note the price of gold, which immediately starts to climb.
J. When the date is Sep 1972, pause the app by tapping the date.
   1. What is the price of gold? ($66).
   2. What is the rate of inflation? (3.2%)
K. Why did inflation not increase rapidly once the gold standard was abandoned?
   1. When President Nixon ended the gold standard, he also implemented a 90-day freeze on prices and wages.

III. IN-CLASS ASSIGNMENT: *20 minutes*

A. Pass out the **Gold Standard 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 indicated values.
   2. Use the values to answer the worksheet questions.

IV. HOMEWORK ASSIGNMENT *15 minutes*

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