Lesson 4

Save and Invest: Put It in the Bank

Lesson Description

Students read a passage on “Banking Basics” and assess the role of banks as financial intermediaries that bring together savers and borrowers. After learning about different account types, students research information about various products from a bank and design a poster that shows the benefits and drawbacks of various accounts.

National Standards in K–12 Personal Finance Education (www.jumpstart.org)

Saving and Investing
Standard 1: Discuss how saving contributes to financial well-being.

Instructional Objectives

Students will:

- Describe the benefits of using a bank.
- Evaluate the role of banks as financial intermediaries between savers and borrowers.
- Compare various accounts offered by commercial banks.

Time Required

One 50-minute class period

Materials Required

- Copies of the classroom visuals
  - *Visual 1: Banking Basics – Reading Anticipation Guide*
  - *Visual 2: Fast Facts about the FDIC*
- Copies of the following handouts for each student
  - *Handout 1: Banking Basics*
    Note to the teacher: The Dallas Fed wishes to thank the Boston Fed for the use of its publication “Banking Basics” to develop the lesson. To download the publication, go to http://www.bos.frb.org/education/pubs/banking2.pdf. To order copies, e-mail bostonfed.publications@bos.frb.org.
  - *Handout 2: Thinking about Banks*
  - *Handout 3: Comparing Accounts*

Procedure

1. Introduce the lesson using the following questions:
   - Why should savers not keep their money in a piggy bank or a mattress?
     Answers will vary, but might include a lack of safety and missed opportunities to earn interest.
   - Besides keeping money at home, where can savers keep money?
     Savers can deposit their money in a bank.
   - What are the benefits of using a bank?
     Student answers might include:
     Keeping money safe from loss or theft
     Making payments easily and inexpensively
     Maintaining records of financial transactions
     Depositing paychecks directly
     Building savings and earning interest
     Establishing credit

2. *Display Visual 1: Banking Basics – Reading Anticipation Guide.* Read each statement individually to the class and ask them if they know any facts to support each statement. Briefly discuss each statement with the class in light of the students' prior knowledge.

3. *Distribute Handout 1: Banking Basics* to each student. Have each student read the selection independently. Have students engage in a think-pair-share activity in which they:
   - *Think* about the reading and the statements on the anticipatory guide. What new information has the reader learned about each of the statements? As they read, have students write the number of the anticipatory statement in the margin next to the text that supports or describes the statement.
   - *Pair* with another reader. Discuss each of the seven anticipatory statements with the partner. Each of the students should note information from the reading that supports each statement.
   - *Share* the supporting statements and information from the reading with the entire class. Ask students to describe the supporting evidence for each statement found in the reading.

4. Display *Visual 2: Fast Facts about the FDIC*. Review the facts about federal deposit insurance with students. Emphasize that deposits are automatically covered, up to the legal limit, at any insured bank.

Closure

5. Review the major concepts of the lesson using the following questions:
   - How did early lending lead to the creation of banks?
     Institutions developed that efficiently brought together savers and borrowers.
   - How do banks serve as intermediaries between savers and borrowers?
     By pooling savers' money and loaning it to borrowers who are judged to be good credit risks, banks create income for savers in the form of interest and provide a source for borrowers to access funds.
   - What are the major benefits of placing savings in a bank?
     Bank accounts are good for short-term financial needs and goals. They provide safety and liquidity while at times offering interest payments.
   - What are some potential drawbacks of placing savings in a bank?
     Some accounts limit access (at least for a period of time), and the interest rate may be lower than the return possible on other investments.

Assessment

6. Distribute the student activity entitled *Handout 2: Thinking about Banks*. Allow students to answer the questions in class or assign the activity as homework.

7. Remind students of the last statement from *Visual 1: Banking Basics – Reading Anticipation Guide*:

   Different types of bank accounts have advantages and disadvantages for depositors.

Tell students that in order to compare types of bank accounts, a saver must conduct research. Distribute *Handout 3: Comparing Accounts*. Have students complete the research and create the poster that is described in the handout.

Evaluate student work by considering the completeness and accuracy of information in the table and the poster, as well as the design and clarity of the presentation of information in the visual.

Visual 1: Banking Basics – Reading Anticipation Guide

1. Banks are businesses that sell products and try to make a profit.

2. Banks bring together savers and borrowers.

3. The financing of merchant voyages in the ancient world provided the basis for the modern banking industry.

4. All borrowers pay interest for loans, but risky borrowers pay more.

5. Depositing money in a bank is one of several options for savers.

6. Banks provide safety and potential earnings to depositors.

7. Different types of bank accounts have advantages and disadvantages for depositors.

Visual 2: Fast Facts about the FDIC

- The Federal Deposit Insurance Corporation (FDIC) is an independent agency of the U.S. government and is backed by the full faith and credit of the federal government.
- FDIC protects against the loss of insured deposits if an FDIC-insured bank or savings association fails. No depositor has ever lost a single penny of FDIC-insured funds.
- FDIC insurance covers funds in deposit accounts, including checking and savings accounts, money market deposit accounts and certificates of deposit (CDs).
- FDIC insurance does not cover other financial products and services that insured banks may offer, such as stocks, bonds, mutual fund shares, life insurance policies, annuities or municipal securities.

Basic FDIC Deposit Insurance Coverage Limits*	
Single Accounts (owned by one person)	$250,000 per owner
Joint Accounts (two or more persons)	$250,000 per co-owner
Certain retirement accounts (includes IRAs)	$250,000 per owner
Revocable Trust Accounts	$250,000 per owner per beneficiary subject to specific limitations and requirements
Corporation, Partnership and Unincorporated Association Accounts	$250,000 per corporation, partnership or unincorporated association
Employee Benefit Plan Accounts	$250,000 for the non-contingent, ascertainable interest of each participant
Government Accounts	$250,000 per official custodian

* On January 1, 2014, the standard coverage limit will return to $100,000 for all deposit categories except IRAs and certain retirement accounts, which will continue to be insured up to $250,000 per owner.

Source: http://www.fdic.gov/deposit/index.html

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Handout 1: Banking Basics

Some young savers stash their cash in shoe boxes or jelly jars. Others use "piggy banks," which today look more like spaceships or cartoon characters. In any case, the same problem arises. Sooner or later, the piggy bank or jelly jar fills up, and you have to make a decision: Should I spend the money or continue to save? And if I continue to save, should I open a bank account or just find a bigger jar?

Maybe you've had to face such a decision yourself. If you decide to keep your money at home, it will just sit there and won't earn any extra money for you. You also run the risk that a burglar, a fire, or some other disaster will wipe out your savings in the wink of an eye. Then again, if you open a bank account, you can't "visit" your money as easily as you can when it sits in your dresser drawer. You can't just walk into a bank in the middle of the night to count your cash. You can't run the coins through your fingers or toss the bills in the air and let them rain down on your head. Opening a bank account is a big step because you are putting your money in someone else's hands. You're counting on someone else to handle your money responsibly. Before you do that, it might be a good idea to understand how banks operate.

What is a bank?

A bank is a business. But unlike some businesses, banks don't manufacture products or extract natural resources from the earth. Banks sell financial services such as car loans, home mortgage loans, business loans, checking accounts, credit card services, certificates of deposit, and individual retirement accounts.

Some people go to banks in search of a safe place to keep their money. Others are seeking to borrow money to buy a house or a car, start a business, expand a farm, pay for college, or do other things that require borrowing money.

Where do banks get the money to lend? They get it from people who open accounts. Banks act as go-betweens for people who save and people who want to borrow. If savers didn't put their money in banks, the banks would have little or no money to lend. Your savings are combined with the savings of others to form a big pool of money, and the bank uses that money to make loans. The money doesn't belong to the bank's president, board of directors, or stockholders. It belongs to you and the other depositors. That's why bankers have a special obligation not to take big risks when they make loans.

How did banking begin?

Imagine for a moment that you are a merchant in ancient Greece or Phoenicia. You make your living by sailing to distant ports with boatloads of olive oil and spices. If all goes well, you will be paid for your cargo when you reach your destination, but before you set sail you need money to outfit your ship. And you find it by seeking out people who have extra money sitting idle. They agree to put up the money for your voyage in exchange for a share of your profits when you return . . . if you return.

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Handout 1: Banking Basics

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The people with the extra money are among the world's first lenders, and you are among the world's first borrowers. You complain that they're demanding too large a share of the profits. They reply that your voyage is perilous, and they run a risk of losing their entire investment. Lenders and borrowers have carried on this debate ever since. Today, people usually borrow from banks rather than wealthy individuals. But one thing hasn't changed: Lenders don't let you have their money for nothing. Lenders have no guarantee that they will get their money back. So why do they take the risk? Because lending presents an opportunity to make even more money.

For example, if a bank lends $50,000 to a borrower, it is not satisfied just to get its $50,000 back. To make a profit, the bank charges interest on the loan. Interest is the price borrowers pay for using someone else's money. If a loan seems risky, the lender will charge more interest to offset the risk. (If you take a bigger chance, you want a bigger payoff.)

But the opportunity to earn lots of interest won't count for much if a borrower fails to repay a loan. That's why banks often refuse to make loans that seem too risky. Before lending you money, they look at:

- How much and what types of credit you use, such as credit cards, auto loans, or other consumer loans;
- Whether or not you have a history of repaying your loans, and
- How promptly you pay your bills.

Banks also use interest to attract savers. After all, if you have extra money, you don't have to put it in the bank. You have lots of other choices:

- You can bury it in the backyard or stuff it in a mattress. But if you do that, the money will just sit there. It won't increase in value, and it won't earn interest.
- You can buy land or invest in real estate. But if the real estate market weakens, buildings and land can take a long time to sell. And there's always the risk that real estate will drop in value.
- You can invest in the stock market. But like real estate, stocks can also drop in value, and the share price might be low when you need to sell.
- You can buy gold or invest in collectibles such as baseball cards, but gold and collectibles fluctuate in value. Who knows what the value will be when it's time to sell? (In 1980, gold sold for $800 an ounce. By 1983, the price had sunk below $400.)

Or you can put the money in a bank, where it will be safe and earn interest. Many types of bank accounts also offer quick access to your money.

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Handout 1: Banking Basics

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What types of accounts do banks offer?

People use banks for different purposes. Some have extra money to save; others need to borrow. Some need to manage their household finances; others need to manage a business. Banks help their customers meet those needs by offering a variety of accounts.

Savings accounts are for people who want to keep their money in a safe place and earn interest at the same time. You don't need a lot of money to open a savings account, and you can withdraw your money easily.

Certificates of deposit (CDs) are savings deposits that require you to keep a certain amount of money in the bank for a fixed period of time (example: $1,000 for two years). As a rule, you earn a higher rate of interest if you agree to keep your money on deposit longer, and there is usually a penalty if you withdraw your money early.

Checking accounts offer safety and convenience. You keep your money in the account and write a check, use a debit card or access your account online when you want to pay a bill or transfer some of your money to someone else. If your checkbook or debit card is lost or stolen, you can cancel the debit card or close your account and open a new one so that nobody can use your old account information. (When cash is lost or stolen, you rarely see it again.) Another attractive feature of a checking account is that your bank sends you a monthly record of the checks you have written, and you can use that record if you ever need to prove that you've made a payment. Banks sometimes charge a fee for checking accounts, because processing transactions can be costly.

Many banks also offer no-fee checking and checking accounts that earn interest if you agree to keep a certain amount of money—a minimum balance—in the account. But these accounts are limited to non-business customers. Banking laws almost always require businesses to use regular checking accounts that do not pay interest.

Money market deposit accounts are similar to checking accounts that earn interest, except that they usually pay a higher rate of interest and require a higher minimum balance (often $2,500 or more). They also limit the number of checks you can write per month.

Name:____ Date:____________

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Handout 2: Thinking about Banks

1. Use information from Handout 1: Banking Basics to complete the table below.

How do banks and other financial institutions serve savers?	How do banks and other financial institutions serve borrowers?

2. Use the terms below to complete this flowchart, labeling all boxes and arrows.

Banks and other financial institutions
Deposits
Interest payments (use twice)
Loans

3. How does the riskiness of a loan affect the interest charges that a borrower must pay? Explain your answer.

4. What factors should a saver consider when choosing an account at a bank?

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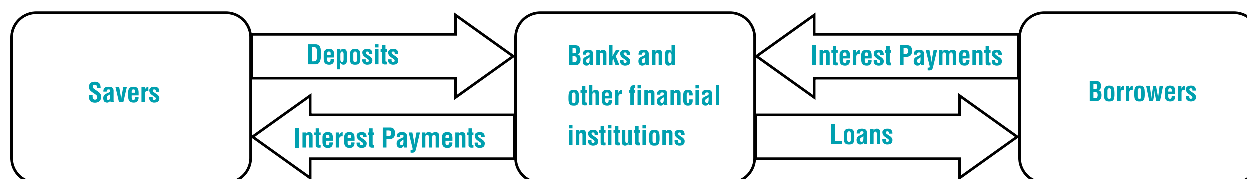
Handout 2: Thinking about Banks

Suggested Answers

1. Complete the table below.

How do banks and other financial institutions serve savers?	How do banks and other financial institutions serve borrowers?
Answers will vary but should include: • Provide safety for deposits • Allow access to funds • Pay interest on deposits	Answers will vary but should include: • Allow borrowers access to loan funds without having to borrow from individuals • Pool savings from many individual savers to allow larger loans

2. Use the terms below to complete this flowchart, labeling all boxes and arrows.



Banks and other financial institutions

Deposits

Interest payments (use twice)

Loans

3. How does the riskiness of a loan affect the interest charges that a borrower must pay? Explain your answer.

As the riskiness of a loan increases, the saver demands a higher rate of return to compensate for the possibility of a loss due to default.

4. What factors should a saver consider when choosing an account at a bank?

Savers should consider the deposit insurance, the interest rate promised and the limitations on withdrawal. Usually, accounts that offer higher interest rates have more restrictions on withdrawals, while accounts that have fewer restrictions on access to the deposits offer a lower rate of return.

Name:____ Date:____________

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Handout 3: Comparing Accounts

Choose a bank or other financial institution that has an office close to your home or school. Visit the office or the website to find information about the five accounts listed on the table below. Complete the table and record the name of the institution and the source of your information.

	Checking	Saving	CD (3-month)	CD (36-month or longer)	Money Market Deposit Account
Interest rate					
Minimum deposit					
Account fees					
Transaction limits					
Deposit insurance limits					
Penalties for withdrawal					

Name of institution:____

Source of information:____

Using the information from your research, make a poster that shows the benefits and the drawbacks of each account.