

***The Business of Banking***

by

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**Lesson Description:** In this lesson students will perform a play to learn how a bank is a business. Students will understand that banks make loans, charging fees (interest) to customers to gain revenue, and offer savings accounts on which they will pay interest.

**Grade Level:** 4/5

**Standard:** Economics Standard 2: Students will examine the interaction of individuals, families, communities, businesses, and governments in a market economy.

**End of Cluster Expectations (Benchmarks):** Students will understand the role of banks and other financial institutions in the economy.

**Essential Question:** How do banks make a profit?

**Assessment**

**Benchmark Statement:** This assessment gives evidence of the student’s ability to understand the role of banks in the economy.

***Constructed Response***

<p><b>Data</b></p> <p><b>HEADLINE: ABC Bank Offering 5% Interest on Savings Accounts</b></p>
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What interest rate should ABC Bank charge for loans? Explain your answer.

**Sample Response:** ABC Bank should charge an interest rate of 8% because they need to make enough money to pay interest on savings accounts, salaries and other expenses and still make a profit. (Valid rate: any rate above 5%)

**Rubric:**

- 2 – This response gives a valid rate with an accurate and relevant explanation.
- 1 – This response gives a valid rate with an inaccurate, irrelevant, or no explanation.
- 0 – Inaccurate response.

**Multiple Choice**

<p><b>Data</b></p> <p><b>HEADLINE: 1<sup>st</sup> National Bank Offering 8% Interest on Loans</b></p>
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What interest rate should 1<sup>st</sup> National Bank pay to the customers for savings accounts? Circle the correct answer.

- a. 12%
- b. 10%
- c. 8%
- d. 6%

The answer is **d**.

**Objective(s):** Students will be able to:

- explain how banks make a profit;
- explain why banks require borrowers to pay higher interest on loans than the bank pays out on savings accounts.

**Prior Knowledge and Skills:** Students should be familiar with the concepts of goods, services, resources, taxes, incentives.

**Time to Complete:** One to two 45 minute class periods

**Materials/resources needed:**

- Visual 1: A Bank is a Business (1 transparency)
- Handout 1: “A Visit to the First Bank of Ourtown” (1 copy per pair of students)
- (Optional) Name tags for 15 actors – see “Cast of Characters” for each scene
- (Optional) Tape or yarn for attaching name tags to students
- Handout 2: Assessment (1 copy per student)

**Procedure:**

1. Tell the students that a bank is a business, not just a place to keep money safe.
2. Explain to students that they will be performing a play about the different services banks provide.
3. Divide students into pairs. Distribute one copy of the play Handout 1, “A Visit to the First Bank of Ourtown,” to each pair. Allow students a few minutes to read the play silently.

4. Assign roles for reading/performing the play. To allow all students to participate, assign different students for each scene (Scene 1 has 8 characters, Scene 2 – 9, Scene 3 – 9) .
5. Tell students to listen as the play is read for services a bank performs and how a bank is a business.
6. Read/perform the play, stopping after each scene to discuss the following.

**Scene #1:**

- a. How is a bank a business? *(It sells services related to money and credit.)*
- b. What are some services a bank provides? Record students' responses on the board. *(checking accounts, savings accounts, check cashing, money transfers, loans)*
- c. What is the goal of most businesses? *(to make a profit)*
- d. What is **interest**? *Tthe price people pay to borrow money; the price banks pay as an incentive for people to save their money in a bank.)*
- e. What is **profit**? *Tthe money left after a business pays its expenses.)*

**Scene #2:**

- f. What **expenses** does a bank have? List students' responses on the board. *(wages, computers, office supplies, interest on savings accounts, taxes; students might also suggest electricity, phone service, advertising, building mortgage)*
- g. What is **revenue**? *(Money paid to the bank for services they provid.e)*
- h. What are a bank's sources of revenue? *( charging their customers fees for services such as checking accounts, charging interest on loans)*
- i. What is a **loan**? *(a specific amount of money a consumer borrows from a bank with the promise to repay in the future)*
- j. Define **incentive**. *(rewards or penalties people receive from engaging in a particular activity)* Ask students: "What are some incentives you receive for finishing your homework? for positive classroom behavior?" *(Answers will vary.)*
- k. Ask students to recall that in the play Maddy's mom has a savings account at the bank. What incentive do banks give customers for saving their money in the bank? *(The bank pays interest.)* Remind students that the bank charges interest to borrowers for using the bank's money.
- l. How much interest should a bank charge and how much should it pay? Why? *Tthe bank must charge a greater percentage on a loan than it will pay for saving accounts, so that the bank can make a profit.)*

**Scene #3:**

- m. Ask students to imagine a world without banks. Discuss the following questions:
  - If your parents needed \$10,000 to buy a new car, how would they get the money? *(borrow from family or friends)*
  - How would they be able to get \$200,000 to buy a house? *( Most likely they would have to save money for a very long tim.e)*
  - Would they always be able to find someone willing or able to lend the money? *(not necessarily)*

- n. Explain that because of the challenge of finding a friend or relative willing and able to lend money, banks are very important. Banks can pool money from all their deposits to make loans to individuals or businesses.

7. Write this example on the board: A bank receives the following deposits:

\$ 1,000  
\$ 5,000  
\$ 3,000  
\$ 5,000  
\$14,000

Although the bank cannot lend out all of this money, by putting these deposits together they are able to lend more than a friend or family member could.

8. Display Visual #1. Explain to students that the borrower pays the bank more interest than the bank pays on savings accounts, so the bank makes a profit.

**Closure:**

1. Ask students the following questions:
  - a. How do banks make a profit? (*by charging customers for services and charging interest on loans*)
  - b. Why does a bank charge a higher interest rate on loans than it pays on savings accounts? (*The bank needs to bring in enough revenue to pay for salaries, equipment, telephone service, deposit slips, pens, pay interest on savings accounts, etc., and still make a profit.*)
  - c. What services do banks provide? (*savings accounts that earn interest and keep money safe, checking accounts, transfer of money, check cashing*)
  - d. What expenses do banks have? (*wages, equipment such as computers, telephone service, deposit slips, pens, interest on savings accounts, etc.*)

**Assessment:**

Distribute Handout 2 to each student. Encourage students to answer the constructed response question with complete sentences and a detailed explanation.

**Citation:**

The play, "The First Bank of Ourtown," from Unit II: Money and Banks in *The Money Tree*. Federal Reserve Bank of St. Louis, 1989.

Visual 1

# A Bank is a Business

Revenue – Expenses = Profit  
**(10% - 5% = 5%)**

You Pay:  
Interest on Loan  
10%



Bank Pays:  
Interest on Savings

**Handout 1****A VISIT TO THE FIRST BANK OF OURTOWN****Cast of Characters**

<b>SCENE 1</b>	<b>SCENE 2</b>	<b>SCENE 3</b>
Bobby	Tammy	Mr. Knowsit
Beth	Susie	Cody
Mr. Knowsit	Maddy	Devin
Ms. Savalot	Ms. Savalot	Tammy
Cody	Mr. Saver	Susie
Devin	Teller #2	Maddy
Customer #1	Teller #1	Beth
Teller #1	Ms. Borrower	Ms. Savalot
	Mr. Knowsit	Bobby

(The setting is the lobby of a bank. Mr. Knowsit's class is visiting the **First Bank of Ourtown**.)

**SCENE #1:**

Bobby: (Looking around) Hey, this place is cool! Do you think the banker will give us any money?

Beth: Don't be silly. The money doesn't belong to the banker. It belongs to the depositors who have their accounts here.

Mr. Knowsit: Gather around class. Be sure to give your best attention now. Boys and girls, this is Ms. Savalot. She is a banker here at the First Bank of Ourtown.

Ms. Savalot: Good morning, and welcome! I hope you will find your visit here interesting and worthwhile. Please feel free to ask questions anytime during our tour. I would like to start your visit with a question. Does anyone know who owns this bank?

Cody: I think the government owns all banks. You can tell by the way everything looks expensive in here.

Devin: Yeah, and everybody who works here looks serious. They must work for the government.

Ms. Savalot: Actually, although banks are watched over by governments, they are owned by individuals, just like any other business.

Beth: Business? This isn't a business, it's a bank! Businesses sell things.

Ms. Savalot: That's correct, businesses sell goods and services. Banks sell services related to money and credit. I, along with some other individuals, own this bank.

Bobby: Wow, you must be rich to have all this money!

Ms. Savalot: I work hard to earn profits for this bank, but the money does not belong to me.

Cody: Bobby, the money in the bank belongs to the people who deposit their money here. My mom has a savings account here, so part of the money in this bank belongs to her.

Ms. Savalot: That's right! When people save part of their income they deposit it in a bank so they can earn interest. The interest is added to the account, and it begins to earn interest, too. Over time, the savings account keeps growing, unlike it would in a piggy bank at home.

Devin: What I want to know is, how can a bank stay in business paying out all this interest to people with savings accounts?

Ms. Savalot: That's a good question, Devin. You know that individuals who own businesses want to make profits. If all we did was hold deposits and pay interest, we couldn't stay in business. Let me tell you about some of the services we provide at our bank. Cody, I already mentioned that we put each depositor's money into a savings account, for which we pay interest. We also accept deposits into checking accounts, transfer money to someone else when a check is written, and we "cash" checks for our customers when they want currency and coins. There is a customer at the window now. Let's see what kind of transaction she is conducting.

Customer #1: (To Teller #1) I would like to take money from my account. May I cash this check, please?

(Teller takes check, turns it over, stamps it, and then pretends to type in some numbers on a computer terminal.)

Ms. Savalot: (To the students) Remember boys and girls, the customer can only draw out as much money as she or her has deposited. The teller always carefully counts out the cash as it is given to the customer.

Teller #1: (To Customer) Twenty, thirty, thirty-five, thirty-six, thirty-seven, dollars and twenty-five cents. Thank you, and have a nice day!

**SCENE #2:**

- Tammy: I still don't see how you're going to stay in business, taking deposits and paying interest on savings accounts, transferring money, and cashing checks. You're going to be too broke to buy your own lunch!
- Susie: And what about all the other expenses you have? We learned from Mr. Knowsit that all businesses have to pay for resources, such as the wages you pay the tellers, that computer, and telephones, even deposit slips and pens.
- Maddy: Yeah, and what about taxes?! All businesses have to make tax payments to governments.
- Ms. Savalot: Hold on! When we lend money, we charge the borrower interest on the loan. That's where most of our revenue comes from. Chances are your family has a loan from a bank right now. When people buy a house, a car, or start a business, they usually do not have enough money saved to pay cash. So they take out a loan. The bank places the money in a checking account for them, and they purchase their house or car. Then, each month, they make a payment which includes interest for the money they borrowed. On a loan for \$1,000, for example, the borrower may pay back \$1,100. The extra \$100 of interest is revenue for the bank. Let's watch a few more transactions at the teller's window to get a better idea of how we operate.
- Mr. Saver: (To Teller #2) I would like to make a deposit. This is my paycheck, and here is a deposit slip which shows how I want it distributed.
- Teller #2: Yes, sir, Mr. Saver. I see that you want to place \$125 in checking, \$35 in savings, and \$15 cash to take with you.
- Ms. Savalot: (To the students) The amount of the deposit and amount of cash returned has to be equal to the amount of the check.
- Teller #2: Here is your receipt which has your new checking and savings balances and here is your cash: ten, fifteen dollars. Thank you and have a nice day!
- Teller #1: (To Ms. Borrower) May I help you?
- Ms. Borrower: Yes, I would like to apply for a loan.
- Teller #1: I will call over one of our loan officers to discuss it with you.
- Ms. Savalot: I will help you, if you don't mind having some observers. These boys and girls are learning about how a bank operates.
- Ms. Borrower: Oh, that will be fine. You see, I want to apply for a loan.

Ms. Savalot: How much would you like to borrow and for what purpose do you want the loan?

Ms. Borrower: I want to borrow \$2,000 to buy a car. It costs \$5,000, but the dealer is giving me \$3,000 for my old car.

Ms. Savalot: Well, here is a loan application form. If you will fill it out, I will then go over your application, run a credit check, and let you know in two days whether or not your loan is approved. (Ms. Borrower gets out a pen and begins filling out the form.)

Maddy: Ms. Savalot, what did you mean by letting her know if the loan is approved? Don't you want to lend as much money as you can so you can increase revenues for the bank?

Ms. Savalot: Certainly we want to increase our revenues by making loans and receiving interest payments, but banks have to be careful. We want to be sure that the individuals and businesses we lend money to will pay us back. So we go over the loan application of each borrower and verify that the person is employed and makes enough money to repay the loan. We also examine the credit record of the applicant to see if he or she has a good history of paying on time.

Tammy: Gee, it's really important then for people to pay back their loans if they want to get other loans in the future.

Susie: Ms. Savalot, I remember you saying that interest on loans was one of the ways banks receive revenues. Where else do you get revenue from?

Ms. Savalot: Revenue for banks also comes from fees for checking services. Many banks have a monthly service charge to cover the expense of transferring money in and out of checking accounts. Some banks that do not charge a fee require that the depositor always keep a minimum balance in the account, say \$100.

Maddy: I get it. The bank can use that \$100 for loans and earn interest without having to pay any out. That covers the bank's expense of servicing the account.

Mr. Knowsit: I couldn't have said it better myself, Maddy. Now class, can someone review for us the bank's sources of revenue and expenses? (Lots of hands) Yes, Susie.

Susie: Well, banks receive revenues from the interest paid by borrowers and from fees it collects for checking services.

Mr. Knowsit: Good! Now, who wants to describe the expenses? (Lots of hands) Tammy.

Tammy: Banks have to pay for the resources they use, they pay interest to savers, and of course, they pay taxes.

Susie: Does it always come out even?

Ms. Savalot: I mentioned before that I want to help my bank make a profit. Profit is the money left from our revenues after all of the expenses are paid. Profit belongs to the owners of the bank, and part of the profit becomes income to the owners. Another part of the profit is called “bank capital” and is a kind of business saving.

**Scene #3:**

Mr. Knowsit: Thanks Ms. Savalot. Now class, let’s continue reviewing what we’ve learned today. Who owns the bank? (Hands raised) Cody.

Cody: Banks are regulated and insured by the government, but they are owned by individuals, just like all businesses.

Mr. Knowsit: Good, Cody. You were paying attention. Next, if banking is a business, what goods and services does it sell? (Hands) Devin.

Devin: Banks are in the business of money and credit.

Mr. Knowsit: Would you explain a little further what that means, Devin.

Devin: Well, banks provide services, like checking accounts. They take deposits into checking accounts and then transfer the money when you write a check. They also cash checks. They accept deposits into savings accounts and pay interest to savers.

Mr. Knowsit: What other services do banks provide? (Hands) Tammy.

Tammy: They make loans to individuals and businesses. If you want to buy a car or something and don’t have enough cash, you can get a loan from a bank.

Susie: If the bank approves you for the loan.

Mr. Knowsit: That’s right, Susie. Now what do you have to do to be approved by the bank for a loan? Bobby.

Bobby: Well, you fill out an application and the bank investigates your credit history to see if you have paid off any other loans you have had. They also verify your job and income to decide whether you can afford to pay back the loan.

Mr. Knowsit: How does the bank make a profit? (Hands) Maddy.

Maddy: The bank receives revenue from two sources: fees for checking account services and interest from loans.

Beth: Then, from its revenues, the bank pays interest on savings, taxes, and payments for the resources it consumes. What's left over is profit. The profit can be paid to the owners or be saved. The part that is saved is called bank capital.

Ms. Savalot: Wow! Boys and girls, I'm really impressed with all you have remembered!

Mr. Knowsit: Thank you for the tour, and the lesson on banks.

Maddy: On behalf of the whole class, thank you, Ms. Savalot!

Ms. Savalot: You are welcome, boys and girls. I hope you will come back to the First Bank of Ourtown and someday you will have your accounts and loans with us.

Source: The First Bank of Ourtown from Unit II: Money and Banks in *The Money Tree*.  
Federal Reserve Bank of St. Louis, 1989.

**Handout 2 – Economics Standard 2  
Assessment**

Name \_\_\_\_\_

**Data**

**HEADLINE: ABC Bank Offering 8% Interest on Loans**

What interest rate should ABC Bank pay to the customers for savings accounts?  
Explain your answer.

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**Data**

**HEADLINE: 1<sup>st</sup> National Bank Offering 8% Interest on Loans**

What interest rate should 1<sup>st</sup> National Bank pay to the customers for savings accounts? Circle the letter of the correct answer.

- a. 12%

- a. 10%
- b. 8%
- c. 6%