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Money and Monetary Policy in Canada

LESSON PLAN MODULE 9:

MONETARY POLICY IN CANADA

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This module addresses a number of concepts, relationships and ideas presented previously, primarily in modules 6, 7 and 8. This includes such things as the objectives of the Bank of Canada, its methods of achieving those goals, exchange rates and the impact that inflation has on our economy. As such, many of the activities in this lesson reflect ones that have been used in these earlier modules.

Learning Outcomes

The students will be able to:

1. Explain the objectives of the Bank of Canada.
2. Identify how the Bank of Canada monitors the economy and intervenes as necessary.
3. Describe how inflation impacts our economy.
4. Explain why the Bank of Canada is so concerned about the output gap.
5. Identify how the Bank of Canada policies affect spending, borrowing, saving and investing.

New terminology

- Policy Interest Rate
- Inflation expectations
- Output gap
- Effective lower bound of interest rates
- Negative interest rates
- Deflation
- Consumer Price index (CPI)
- CPIX
- Natural Rate of Interest
- Flexible Exchange Rate

Implementation Strategies

This lesson will take three periods to complete. During the first period the students will engage in a group activity called “Pass the Mike.” In the second period the students will be engaged in a different group activity called “Heads Together.” The third period will involve watching a video on exchange rates and discussing how changes in the exchange rate affect different situations. This lesson will require internet access.

Direction to the teacher on how the game “Pass the Mike” is played.

Below, the teacher will find a list of questions and new terms which will not be presented to the students until the start of the game. To begin the game, the teacher will take a handheld instrument which we will call “the mike” and give it to one of the groups. When doing so, the teacher will indicate which term that group must explain. The group will then pick a member who must go to the front of the room and give as complete an answer as possible. The teacher will award a mark out of 5 for the answer and, if there is missing or incorrect information that can be added or corrected by another group, that group will be awarded a bonus point. Once that term (and subsequent question) has been completed the person holding the mike will determine the next term that is to be addressed and hand the mike to another group of his or her choosing. Once a student has held the mike they are not eligible to hold it again. The selected group must pick a member and follow the pattern. This will continue until all terms have been explained and all questions have been answered. **All terms must be answered before any question can be assigned**. Each group must have the same number of opportunities as each of the other groups. The group with the greatest number of points wins.

Period One:

- Begin the lesson by dividing the class into 4 groups.
- Explain that they are going to have to read and become knowledgeable on the content of the first two sections of Module 9 - 9.1 and 9.2
- Explain to them that how they prepare and learn the material is up to them but that all members must have the same working knowledge of the material once they have finished the task.
- Indicate to them that this work is in preparation for a group contest called “pass the Mike.”
- Allow them time to read the material and prepare for the game.

- Begin the game by revealing the terms and questions and assigning the first term to a group.
- Continue playing the game and awarding points until it is finished and a winner has been declared.

List of Terms:

1. Policy Interest Rate
2. Inflation expectations
3. Output gap
4. Effective lower bound of interest rates
5. Negative interest rates
6. Deflation
7. Consumer Price index (CPI)
8. CPIX
9. Natural Rate of Interest
10. Flexible Exchange Rate

List of Questions:

1. What is the Bank of Canada's primary objective and what is its target inflation rate?
2. What areas does the Bank of Canada hope to influence in adjusting interest rates?
3. What is the Bank of Canada concerned about as the economy approaches its short-term capacity?
4. Why is price stability so important?
5. Why is the Bank of Canada concerned about inflation?
6. What impact does higher than desired inflation have?
7. How does the Bank of Canada measure inflation?
8. What types of things can affect the CPI?
9. Why is the Bank of Canada so focused on the output gap?
10. Why is deflation also a cause for concern?

- Conclude this part of the lesson by holding a plenary session and addressing any outstanding questions or comments.

Period Two:

- Divide the class into groups of four and tell them that they will engage in the "Heads Together" activity based on their reading of Module 9, section 9.3 and 9.4 up to the end of the section, "The Importance of Clear Communications to the Public – and Forecasting Expertise."

  (If you have not engaged in this activity before it simply involves the group closing in together to discuss quietly an answer to a question once they are told "Heads Together." After a few moments, they will be told "Heads Apart" and it will be expected that a group will provide an answer. Other groups can then add to the explanation if appropriate.)

- Allow them a few minutes to read the section and then engage in the "Heads Together" activity for each of the following questions:
  1. What is affected by changing the policy interest rate?
  2. What is the formula for total demand in our economy?
  3. What aspects of our economy are of particular interest to the Bank of Canada?
  4. Why would the Bank of Canada raise interest rates?
  5. What is the target interest rate for the Bank of Canada?
  6. Explain how the Bank of Canada might go about establishing a nominal neutral interest rate?
  7. The Bank of Canada lowered the policy interest rate to .25% and then started to raise it. What does this indicate about how the Bank of Canada is viewing our economy?

- Conclude this section by having the students read the Canadian Bankers Association's article entitled "Understanding Interest Rates" found at: https://www.cba.ca/understanding-interest-rates

Period Three:

- Begin the lesson by asking the students to explain the term "exchange rate."
- Once they have a working definition, have them watch the following video – https://www.youtube.com/watch?v=uWIm4-iF7W4

- Once they have watched the video, inform them that they are going to look at various situations and discuss whether or not these individuals would be happy with a hypothetical change in the exchange rate.
    1. Richard is a business executive who is looking to borrow a few million dollars to expand his company into the United States.
    2. Fred has considerable money tucked away in a personal savings account and a large sum of readily available cash that he is looking to do something with and was considering buying foreign currency as an investment.
    3. Lucy and Ricky are planning the purchase of a vacation property in either Florida or Muskoka.
    4. Marie owns an exporting company whose business is just starting to take off as a result of her recent trip abroad.
    5. You own an import company that is growing because of a recent promotion with companies across the country.
    6. Jimmy and his wife are on a fixed income and have been managing their money well. They are in the middle of planning a lifelong trip to the Mediterranean.

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- Read the following announcement regarding a change in the exchange rate:

    "Over the last short while, as a result of both international commodities developments including the rise in the price of oil and the announcement from the Bank of Canada that it was raising interest rates by .25%, the exchange rate on the Canadian dollar has risen from 76.4 cents U.S. to 81.3 cents American."

- Ask the students now to consider each of the six scenarios above and discuss whether or not the individuals would like the announcement explaining why.
- Conclude the lesson by having the students read 9.5 in module 9 – "Different Choices for Monetary Policy."

Evaluations

1. The “Pass the Mike” activity could be evaluated for clarity of understanding.
2. The “Heads Together” activity could be evaluated.

Other Related Activities

1. The students could follow the exchange rate of the Canadian dollar over a period of time and record both the changes and the reasons.
2. Canada is a commodity nation that is closely tied to oil. The students could follow the price of oil and see what impact it had on the Canadian dollar.
3. The students could research what has happened to Canadian interest rates over the last 18 months.

On-line Links

Canadian Bankers Association: Understanding Interest Rates – https://www.cba.ca/understanding-interest-rates

YouTube: Exchange Rates – https://www.youtube.com/watch?v=uWIm4-iF7W4

Bank of Canada – Monetary Policy – How It Works – http://www.bankofcanada.ca/publications/books-and-monographs/why-monetary-policy-matters/4-monetary-policy/