Lesson Plan: Understanding Callable Bonds: Flexibility and Risk

Objective:
Students will explore the concept of callable bonds, analyze the benefits and risks for both issuers and investors, and understand the strategic decisions surrounding their use.

Materials Needed:

- *Game of Thrones* clip or scenario related to Cersei and callable bonds.
- Handouts summarizing callable bonds and key financial terms.
- Examples of callable bonds in real-world financial markets.

Lesson Steps:

1. Introduction (10 minutes):

- Define **callable bonds**: Bonds that can be redeemed (called) by the issuer before the maturity date.
- Introduce key terms:
  - **Issuer:** The party offering the bond (e.g., a corporation or government).
  - **Investor:** The bondholder who earns interest in exchange for lending money.
  - **Call price:** The amount paid by the issuer to repurchase the bond.
  - **Call protection period:** The time during which the bond cannot be called.
- Explain the purpose: Issuers use callable bonds to refinance debt at lower interest rates if market conditions improve.

2. Viewing Clip (5 minutes):

- Show the *Game of Thrones* clip where callable bonds are discussed, highlighting the strategic use of financial instruments.
- Set the context: Relate the medieval financial negotiations to modern bond markets, emphasizing the trade-offs involved in callable bonds.

3. Group Discussion (10 minutes):

- Divide students into small groups to discuss:
  - What advantages do callable bonds provide to issuers?
  - Why might callable bonds pose risks to investors?
  - How does the scenario in *Game of Thrones* mirror real-world financial strategies?

4. Concept Application (20 minutes):

- **Case Study Analysis:**
  - Provide examples of callable bonds used by governments or corporations.
  - Ask students to analyze:
    - Why the issuer chose a callable bond over other financial instruments.
    - How investors weigh the trade-offs of higher yields versus call risk.
    - How callable bonds affect market dynamics (e.g., interest rate changes).
- Highlight the role of callable bonds in financial flexibility and cost management.

5. Wrap-Up and Reflection (10 minutes):

- Summarize the benefits and challenges of callable bonds:
  - For issuers: Financial flexibility, potential cost savings.
  - For investors: Higher yields but increased risk of early redemption.
- Pose a reflective question: How might callable bonds influence your investment strategy or understanding of financial markets?

6. Activity or Homework (15 minutes):

- **Callable Bond Simulation:**
  - Split students into two groups: issuers and investors.
  - Issuers design two bonds representing loans made over a 3-year time horizon.
    - One bond (Bond A) is not callable.
    - The other (Bond B) will be callable.
  - Beginning with the non-callable bond, have the two groups negotiate an acceptable interest rate.
  - Then, the two groups set terms (rate, call protection period) for the callable bond.
  - Facilitate a discussion after the simulation, evaluating the decisions made by each side.
    - Analyze any differences between the two bonds. Did students negotiate a call premium (a higher overall rate of return for the callable bond)? If so, why?