



# MONEYWISE

VALUING PEOPLE. VALUING MONEY.

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## THIS MONTH'S TOPIC:

### PUT COMPOUND INTEREST TO WORK FOR YOU

The current rising interest rates may mean higher costs for mortgages and other variable rate credit, such as credit cards. However, it also means higher interest paid on savings. Take advantage of compound interest and put those rates to work for you to earn more on your money.

#### UNDERSTANDING COMPOUND INTEREST

When interest is compounded, you earn profit on the money you save, as well as on the interest you have already earned. The money you save is known as the principal. Compound interest offers an advantage over simple interest where you only earn profit on the principal and not any interest paid.

Compound interest helps your money to grow faster over time. The more frequently it is compounded, the greater the compound interest will be. For example, an account that compounds daily will build faster than an account that compounds monthly or annually.

#### PROS AND CONS OF INTEREST

Compounding interest can work for or against you, depending on the products you use. Compound interest on a savings account, especially a high-yield account, provides benefits. The larger the account or the higher the interest rate earned, the faster your money will grow. If you are able to withstand the risk, an investment account or retirement account may be able to offer this opportunity.

Investing



However, when used on a loan product or a credit card, compounding may cause your debt to build faster. Be aware of the terms of all accounts you have. If you have high-interest debt, work to pay that off as quickly as possible.

#### RISING INTEREST RATES

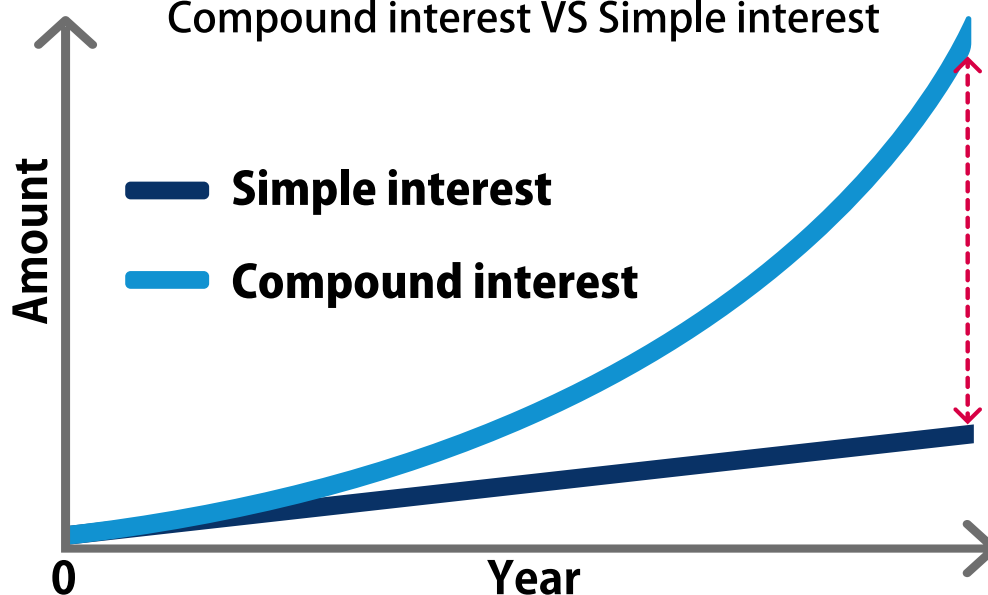
The Federal Reserve's Federal Open Market Committee has raised the federal funds rate seven times in 2022 to combat inflation. Currently it is between 4.25% and 4.5%, up from near zero in 2020 to combat the pandemic's effect on the economy. Average bank interest rates on savings accounts are still low in the U.S., at a national average annual percentage yield, or APY, of 0.30%. However, high-yield accounts may earn between 3% and 4% for those who qualify. Talk with a representative from your financial institution to see what products they offer with compounding interest.



## THE MORE OFTEN THE INTEREST COMPOUNDS, THE FASTER IT WOULD GROW

### THE POWER OF COMPOUNDING

Compound interest VS Simple interest



#### COMPOUND INTEREST AT WORK

This chart shows how much money you would earn if you deposited \$500 in an account that earns 3% compounded annually. If no other deposits are made, the account owner would earn \$79.64 on the initial deposit after five years.

Years	Future Value (Compounded at 3% annually)
Initial Deposit (Year 0)	\$500.00*
Year 1	\$515.00
Year 2	\$530.45
Year 3	\$546.36
Year 4	\$562.75
Year 5	\$579.64

\*Chart assumes no further deposits are made.

The more often the interest compounds, the faster it would grow. And if you add additional funds to the account, the interest would be compounded on the new principal as well.

Commit to saving today by taking the Kentucky Saves Pledge at [www.kentuckysaves.org](http://www.kentuckysaves.org). The pledge is a personal commitment to save money, reduce debt, and build wealth over time. You simply type your name, choose a savings goal, and pledge how much you plan to save each month to reach your goal. There is no commitment, and you will receive free information on ways to save via email or text message.

#### REFERENCES:

Federal Open Market Committee meeting calendars, statements, and minutes (2022). Washington, DC. Board of Governors of the Federal Reserve System. <https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm>

Personal savings rate (2022). Washington, DC: U.S. Bureau of Economic Analysis: <https://fred.stlouisfed.org/series/PSAVERT>

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