

Compounding Effect - A Lesson on How Money Makes Money

Contributed by
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If only I had learnt about the compounding effect of money when I was a teenager. I had heard of the seven wonders of the world, but no one ever told me about the eighth wonder, the effect of compounding. Not matter if you are young or slightly older, read on to discover how money can make money.

The compounding of interest earned is one of the most critical lessons that should be learnt by everyone. To explain the effect of compounding I will use a brief example. If you take \$10,000 and receive 6% interest over one year you will receive \$600. If you reinvest the \$10,600 in year two, you will receive \$636 interest. In year 3 you will receive \$674 interest and this amount increases each year, so long as you re-invest the capital and interest each year.

The next step and even more effective way to use the compounding of interest is to contribute additional money, for example \$100, each month to the capital and interest amounts. This will assist in fast tracking your wealth more quickly and has the effect of growing your capital amount at a rapid rate.

Instead of the investor earning interest on principal, they earn interest on principal and interest, year after year after year.

If you start early in life, this can have a dramatic effect on the capital growth over time. If an 18 year old invests \$100 per month and earns 6% interest until the age of 65, they will have accumulated \$313,187. They would have invested \$56,400 in this time, a profit of \$256,787. However if the same person started investing at 25 years of age, they will have accumulated only \$199,149. They will have invested \$48,000 in this time. So by starting 7 years earlier and investing \$8,400 more (7 years x \$100/month) they will have accumulated \$114,038 more at 65 years.

It is crucial that we teach the compounding effect to everyone in our lives as it is THE KEY to future financial success for most of us. For the sake of some short term pain by putting away some money, we can experience terrific long-term gain. Do not be tempted to withdraw from the interest earned each year as this will negate the effect of compounding and will limit success with this strategy.

One of the best things about the effect of compounding interest is that it does not discriminate - EVERYBODY can do it, no matter whether you are rich or poor or where you live in the world. The big decision is when to start and I urge you all to start today.

You can read more information about the affect of compounding and see some great tables that clearly illustrate the effect of compounding at http://www.achievesuccess.com.au/money/compounding_effect.htm

If it is wealth creation opportunities you are after then check out the life-changing information at <http://www.achievesuccess.com.au/money>

Start compounding your interest today and make the most of this 8th wonder in the world.

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