The Power of Compounding

Regardless of where you choose to invest your money—cash, stocks, bonds, real estate or a combination of places—the key to saving for retirement is to make your money work for you. It does this through the power of compounding. Compounding investment earnings is what can make even small investments become larger given enough time.

You are probably already familiar with the principle of compounding. Money you put into a savings account earns interest. Then you earn interest on the money you originally put in, plus on the interest you've accumulated. As the size of your savings account grows, you earn interest on a bigger and bigger pool of money.

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This chart shows the value of $1,000 compounded at various rates of return over time:

Years	4%	6%	8%	10%
10	$1,481	$1,791	$2,159	$2,594
20	$2,191	$3,207	$4,661	$6,728
30	$3,243	$5,743	$10,063	$17,449

The chart provides an example of how an investment grows at different annual rates of return over different time periods. Notice how the amount of gain increases each 10-year period. That's because money is being earned on an increasingly larger pool of money.

The real power of compounding comes with time. The earlier you start saving, the more your money can work for you. For every 10 years you delay before starting to save for retirement, you will need to save three times as much each month to catch up. No matter how young you are, the sooner you begin saving for retirement, the better.

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