- When interest is compounded, the annual rate of interest (R) is called the **nominal rate**
- The **effective rate,R** is the simple interest rate that would yield the same amount of interest after 1 year.
- When a bank advertises a "7% annual interest rate compounded daily and yielding 7.25%", the nominal interest rate is 7% and the effective rate is 7.25%.

$$R_e = [(1 + \frac{R}{n})^{n-1}] * 100 \tag{1}$$

The effective rate is useful for comparing rates with different compounding periods.