MHAO

WORKSHOP 10

SAVINGS ACCOUNTS & SAVINGS GOALS

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Savings Accounts

The most common type of bank account, and probably the first account you'll ever have, is a savings account. Savings accounts allow you to keep your money in a safe place while it earns a small amount of interest each month. These accounts usually require a low minimum balance ($25), although some may require no minimum balance at all. This depends on the bank and the type of account.

Besides the fact that you will be less likely to spend it, putting your money in a savings account is a safer option because it is *insured.* In addition to insurance, banks and credit unions keep your money in a locked and fireproof safe.

Banks insure your money (up to $100,000) through the **Federal Deposit Insurance Corporation (FDIC).** This means that even if the bank goes out of business (which is very rare), your money will still be there. The FDIC is an independent agency of the federal government that was created in 1933 after the bank failures of the 1920s and early 1930s. Not a single person has lost money in a bank that was insured by the FDIC since then. Similarly, the National Credit Union Administration (NCUA) insures credit union accounts up to $250,000.

When you put your money into a savings account, it earns interest. **Interest** is money the bank pays you so that they can use your money to provide loans for other people. This does not mean you cannot have your money whenever you want it, it is simply how banks make money and how they are able to fund their loans.

It works like this:

1. You open a savings account at the bank.
2. The bank pays you interest on the money that you deposit and leave in that account.
3. The bank then loans that money out to other people, charging a slightly higher interest rate on the loan than what they pay you for your savings account.
4. The difference in interest the bank pays you vs. the interest they charge others is part of how they stay in business.

Interest on savings accounts is usually compounded daily and paid monthly. **Compounded interest** is the interest on a deposit that is calculated based on the original amount of money in your account (the initial principal) as well as the accumulated interest from previous periods.[136] This accumulated interest is essentially a form of "interest on interest" that can help make an account grow faster.

The great thing about compounded interest is that your bank is paying you interest on the money they've already paid you in interest! That means that if your account earns 1% interest, then each day, 1/365th of that 1% of the amount of money you have in your savings account is then added to your total.

Daily compounding = Principal (1 + interest rate/365)365 = (daily compounded amount)[137]

It should be noted that the interest an individual earns on their savings account is generally very little compared to interest earned on investments or very large deposits. The average interest rate is usually around 0.06%, which means you'll likely earn just a few cents each month depending on the size of your deposit. Many online banks and credit unions offer higher interest rates on savings accounts, which means more interest earned.[138]

Note: Savings accounts are a great way to keep your money safe, earn interest on that money, save up for bigger purchases in the future, and have a safety net or "emergency fund" in case of unexpected circumstances.

[136] Jason Fernando. "Compound Interest." *Investopedia* Feb, 16, 2021. https://www.investopedia.com/terms/c/compoundinterest.asp

[137] Original material from Peerlink National Technical Assistance Center.

[138] Matthew Goldberg. "What is the average interest rate for savings accounts?" *Bankrate*, April 28, 2022. https://www.bankrate.com/banking/savings/average-savings-interest-rates/#:~:text=The%20national%20average%20interest%20rate,ll%20earn%20on%20your%20savings.

Different Types of Savings Accounts

Opening a savings account is the easiest way for people to save and earn money at the same time. It is the simplest form of investment. The following section goes through the different types of savings accounts available so you can decide which one is most suitable for you.[139]

Regular Savings Accounts:

Regular savings accounts are great for people who plan to make monthly deposits and earn a small amount of interest at the same time. These accounts offer the greatest freedom to control your account and make as many withdrawals as you need.

Benefits:	Shortfalls:
• Easy to access • Has low or no minimum balance • No limits in making withdrawals • No withdrawal charges	• Low interest rates • Interest rates change with the market

Certificate of Deposit (CD):

Also known as “time deposits,” CDs offer the highest interest rates among saving accounts. By putting your savings in a CD for a predetermined time (anywhere from 6 months to 5 years), your money accumulates interest. Charges are applied when withdrawals are made before maturity of the account. This option is great for long-term saving but not if you need to access your savings account often to withdraw or transfer money.

Benefits:	Shortfalls:
• Offers the highest interest rates • Fixed interest rates	• Charges apply when withdrawals are made preterm • Withdrawals made preterm are made with notices ahead of time

[139] Original material from Peerlink National Technical Assistance Center.