# 04. Compounding returns

Recognising the value of compounding returns, and how to it works for my**super**.

Welcome to an insider's guide to investing with my**super**. As a member, it's worth knowing the ins and outs of how your money is working for you. Not that you have to do anything, but to achieve your goals it helps to understand how your investment lives and breathes.

**Guide 04.**
is an insight to compounding returns.

Here we recognise the power of reinvesting your my**super** earnings to earn even more, and why time is the most important factor.

### What are compounding returns?

Compounding returns are when you make money not only on the money you put in (capital) but the money you've been making (interest or dividends). It's when you reinvest what you earn, to effectively earn income from your income.

This happens by doing nothing. The more you leave your investment, the more income it makes, and in turn the more income it makes of that.

### How does compounding returns impact my**super**?

Compounding returns are how your my**super** investment will help you reach your long-term goal. Putting money in is great, but it's the interest or dividends you make off the earnings on top of the capital, that makes it significantly more significant.

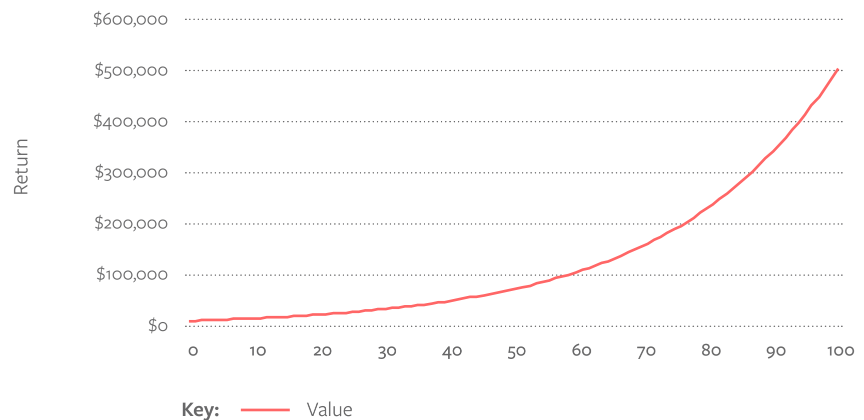
## How do you make the most of compounding returns?

The most important aspect of compounding is time. The longer you have been reinvesting your income the more powerful the compounding effect.

Example 1:

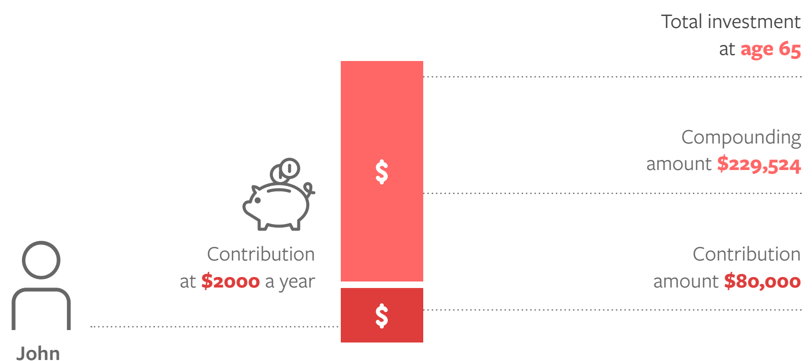
This graph shows how John's $10,000 saving invested today with a return of 4.0% a year (after tax) will grow over time due to compounding returns. The capital quickly accelerates in value as time passes.

### Compounding interest




Example 2:

This diagram demonstrates the impact of compounding returns. John starts contributing $2,000 a year at age 25, with a 6% annual rate of return. At 65 his investment would come to $309,524. Only $80,000 of that would have come from his $2,000-per-year contribution. The rest, $229,524, would come from return on his investment. That is the power of compounding.




To maximise the impact of compounding returns, time is the most important ingredient. In example 2, John's total investment would have been much lower ($222,870) if he delayed by just five years. This highlights that you do not need to invest large sums to become financially independent; you just need to start early.

## What do you have to do for compounding returns?

As powerful as compounding is, when it comes to successful long-term investing there are certain things you can do to maximise your return and the impact of compounding returns.

The key aspects to consider is starting early and consistency. The sooner you start saving the quicker the effects of compounding. Compounding also works best when returns are consistent, and losses are minimised. It's a good idea to invest in a diverse portfolio, to protect yourself against market volatility (markets gains and losses).

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