

Guide to Effective Rates of Return for Investors

Looking out for *you*[®]

“Effective” Versus “Nominal” Rates of Return.

Lately you may have noticed that, more and more, banks, fund managers and other financial institutions advertise and quote an “effective” rate of return (also known as “yield”) and a “nominal” rate on their investment accounts.

Why & What’s the Difference?

It is a simple matter but it can be most important when choosing between different investment accounts. The “nominal” rate is the rate of return quoted on an annual basis. It does not take into consideration how many times in a year the income return is credited/paid into your account. The “effective” rate, instead, takes the payments into consideration and assumes that these payments will be reinvested back into your account with the principal for a full year, resulting in a bigger return.

An Example may Help.

Let’s put it another way. The “nominal” rate of return is what you will be paid for one period. So, if you invest \$10,000 at 12.00% p.a. for one year, you will earn total return of \$1,200 at the end of your one year investment.

If however, you invest your \$10,000 at 12.00% p.a. for one year with income paid to you monthly and you reinvest your monthly income each time it is paid with your principal, you will harness the benefits of compounding income. The accumulation of income with your principal each month will give you an “effective” return of 12.68% p.a. which will result in you earning an investment return of \$1,268 p.a. or \$68 more.

It is important to remember that to reap the benefits of compounding returns, that is, income on your income, you need to reinvest your income with your principal each time it is paid.

If income is only paid once a year at the end of your investment term there will be no difference between the “nominal” rate of return and the “effective” rate of return.

Making the Right Investment Decision.

To help you make a clear and fair comparison when choosing the right account for you to invest in, we have provided a special ‘Rate of Return Conversion Chart’.

It is important that when you are considering different investments you always look at both the rate of return and the timing of these payments. Remember, the higher the frequency of payments means the more income you can accumulate over the term of your investment which will ultimately result in a greater return being paid to you.

How to use the Rate of Return Conversion Chart.

What type of rate is being offered? Is it a “nominal” or “effective” rate? If the rate quoted is nominal you can use the chart to convert it to an effective rate for ease of comparison. Apply the following simple steps:

1. Refer to the first column of the chart: ‘Nominal Rate % p.a.’
2. Determine how often income is paid on the investment: e.g. monthly, quarterly, half-yearly or yearly.
3. By referring to the appropriate column (that is when income is paid), you can determine the effective rate on the investment. Take for instance a nominal rate of 8%, if the income is paid monthly, the effective rate is 8.30%; if paid quarterly, the effective rate is 8.24% etc.

It is important to remember that the effective rate is calculated by assuming that the investor maintains the investment for a full 12 months and re-invests the income as it accrues.

Simply, the effective rate is made up of the nominal rate of return adjusted for the effect of compounding.

Why Income Paid More Often Can Be Better.

Quite simply, the greater the frequency income is paid and then reinvested, the higher the return to you.

If You Need More Information.

Having read this far, you should have a good understanding of the meaning of “effective” rate in relation to “nominal” rate and the principle of compounding income returns. However, if you have any further questions, please contact our Wealth Team experts who will be happy to assist on **1800 818 818**.

Where to Find Accounts With Competitive Returns.

Check out our investment choices at www.latrobefinancial.com. We have Investment Accounts which pay income returns as often as monthly.

Open an Investment Account Today.

To start enjoying the benefits of “effective” rates of return, open your Investment Account today by completing the Application Form in the Product Disclosure Statement (PDS) or go online at www.latrobedirect.com.

Rate of Return Conversion Chart

Nominal Rate %	Effective Equivalent Effective Rate % p.a. where income is paid:			
	p.a.	Monthly	Quarterly	Half-Yearly
4.00	4.07	4.06	4.04	4.00
4.25	4.33	4.32	4.30	4.25
4.50	4.59	4.58	4.55	4.50
4.75	4.85	4.84	4.81	4.75
5.00	5.12	5.09	5.06	5.00
5.25	5.38	5.35	5.32	5.25
5.50	5.64	5.61	5.58	5.50
5.75	5.90	5.88	5.83	5.75
6.00	6.17	6.14	6.09	6.00
6.25	6.43	6.40	6.35	6.25
6.50	6.70	6.66	6.61	6.50
6.75	6.96	6.92	6.86	6.75
7.00	7.23	7.19	7.12	7.00
7.25	7.50	7.45	7.38	7.25
7.50	7.76	7.71	7.64	7.50
7.75	8.03	7.98	7.90	7.75
8.00	8.30	8.24	8.16	8.00
8.25	8.57	8.51	8.42	8.25
8.50	8.84	8.77	8.68	8.50
8.75	9.11	9.04	8.94	8.75
9.00	9.38	9.31	9.20	9.00
9.25	9.65	9.58	9.46	9.25
9.50	9.92	9.84	9.73	9.50
9.75	10.20	10.11	9.99	9.75
10.00	10.47	10.38	10.25	10.00
10.25	10.75	10.65	10.51	10.25
10.50	11.02	10.92	10.78	10.50
10.75	11.30	11.19	11.04	10.75
11.00	11.57	11.46	11.30	11.00
11.25	11.85	11.73	11.57	11.25
11.50	12.13	12.01	11.83	11.50
11.75	12.40	12.28	12.10	11.75
12.00	12.68	12.55	12.36	12.00
12.25	12.96	12.82	12.63	12.25
12.50	13.24	13.10	12.89	12.50
12.75	13.52	13.37	13.16	12.75
13.00	13.80	13.65	13.42	13.00

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