Investing strategies: compound growth

Compounding is a key element in building wealth. Through the magic of compound growth, an investment can grow to many times its original size. All it takes is time.

est that you earn when interest payments are reinvested.

Suppose you invest $10,000 in a compound-interest Guaranteed Investment Certificate (GIC) that earns 8 per cent annually, and is held in a plan where tax is deferred (such as an RRSP).

In the first year, your $10,000 will generate $800 in interest. That $800 will then be added to your original investment principal. In the second year, you'll have $10,800 earning 8 per cent, which will generate $864.

That is then added to your existing investment, and so on.

By the end of the tenth year, assuming that no tax has been paid, your $10,000 will have grown to $21,589. And after 25 years, your original $10,000 will be worth $68,485—almost seven times what you originally invested, without your having to add a single cent.

The principle of compound growth also applies to other forms of investment income.

When dividend income is reinvested in more shares of the same stock, it's called a Dividend Reinvestment Plan (DRIP). Mutual funds and segregated funds also let you benefit from compound growth. Your earnings are usually reinvested in more units of the underlying fund.