COUNCIL FOR Economic Education
You're never too young to learn about money

Compound Interest Assessment Answer Key

Directions: Write a brief answer to each of the following questions.

1. What is savings?
   Savings is disposable income (income after taxes) minus consumption spending (money spent on goods and services).
2. Why do people save?
   To buy goods and services in the future.
3. What is principal?
   The original amount of money deposited minus interest or the original amount of a loan without any interest.
4. What is interest rate?
   The percentage of the amount of a loan that is charged for a loan. Also, the percentage paid on a savings account.
5. What is interest?
   The amount of money that people pay to borrow money or the amount of money that people earn when they save money.
6. Why do banks pay interest?
   They use customer deposits, which may represent savers, to make loans to other customers, who are borrowers.
7. What is simple interest?
   Interest paid only on the principal.
8. What is compound interest?
   Interest paid on the principal and on any interest earned.
9. What factors affect how much interest someone earns on their deposits?
   For example, how long they save, how regularly they save, how much interest is paid, how often the interest is compounded.
10. How does compound interest affect the use of credit cards?
    If balances aren't paid in full each month, the account holder is charged interest on the original balance as well as any interest charged.
11. How does time affect the amount of compound interest earned or paid?
    The more often the interest is compounded on interest earned, the more money you are paid to save. The more often the interest is compounded on interest paid on a loan, the more money that is being paid to creditors.
12. Why do banks pay interest on savings and creditors charge interest?
    Banks pay interest for using the customers' deposits to make loans; creditors charge interest for loaning you the money.