

Compounding in Mutual Funds

CHEEKU, I SHALL TELL YOU ABOUT COMPOUNDING IN MUTUAL FUNDS TODAY.

ALL RIGHT, SIR! BUT WHAT DOES 'COMPOUNDING' MEAN?

CHEEKU, COMPOUNDING MEANS ADDING UP. IT ALSO MEANS TO THE ADDING UP OF PROFITS.

YOU MEAN EARNING MORE PROFITS?

THAT'S RIGHT, CHEEKU! MUTUAL FUND INVESTMENTS ARE A BETTER AVENUE OF EARNING COMPOUNDED RETURNS.

COMPOUNDING DEPENDS UPON TWO FACTORS: RE-INVESTMENT AND A LONG TIME PERIOD. THE MORE TIME YOU ALLOW FOR COMPOUNDING, THE MORE RETURNS YOU EARN.

SIR, I DID NOT QUITE UNDERSTAND.

IMAGINE YOU INVESTED RS. 10,000 FOR TEN YEARS. EVERY YEAR, YOU EARN A 10% INTEREST ON IT. SO IN TEN YEARS, HOW MUCH WILL THE NET AMOUNT OF INTEREST BE?

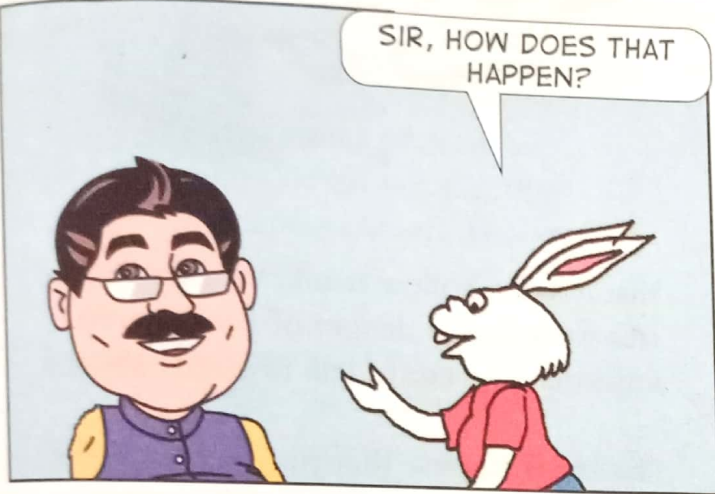
AT THE RATE OF 10%, I WILL EARN RS. 1,000 INTEREST EVERY YEAR. SO IN TEN YEARS, I WILL HAVE EARNED NET INTEREST WORTH RS. 10,000.



YOU ARE RIGHT! BUT COMPOUNDING WORKS DIFFERENTLY. IN THE FIRST YEAR YOU EARN RS. 1,000, BUT IN THE SECOND YEAR YOU EARN RS. 1,100 AND THIS WAY THE AMOUNT OF INTEREST KEEPS ON INCREASING EVERY YEAR.



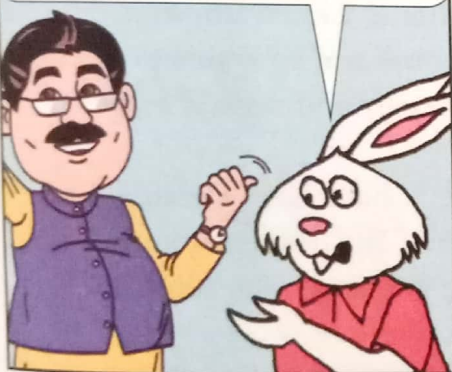
SIR, HOW DOES THAT HAPPEN?



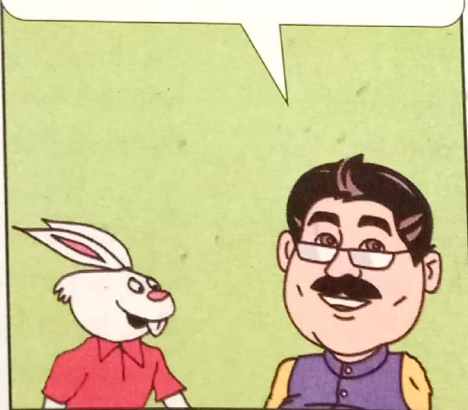
THAT'S THE BENEFIT OF COMPOUNDING IN MUTUAL FUNDS. ALONG WITH THE AMOUNT YOU HAVE ORIGINALLY INVESTED, YOUR APPRECIATION ALSO GETS INVESTED AND HENCE EARNS MORE RETURN FOR YOU EVERY YEAR.



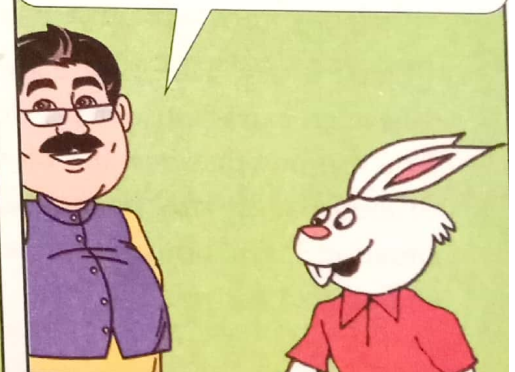
HOW DO WE RECEIVE THE COMPOUND, SIR? DO WE GET IT IN LUMP SUM OR IN SIP?



IT CAN BE BOTH WAYS, CHEEKU.



THERE ARE MANY DIVERSIFICATIONS AS WELL.



DIVERSIFICATION? WHAT'S THAT, SIR?



NOT TODAY, CHEEKU! I SHALL TELL YOU ABOUT IT IN THE NEXT ISSUE.

