Low Interest Rates

Dear Dr. Per Cap:

My savings account barely pays interest. Looking at my monthly bank statements I haven't earned more than 0.01% in years. What's the point of saving money when I only earn a few pennies of interest each month?

Signed, Losing Interest

Dear Losing

I understand your frustration with today's low interest savings accounts. As of May 2020 Bankrate.com lists the national average interest rate for savings accounts at 0.1%. This rate is known as the Annual Percentage Yield or APY - a percentage that reflects the total amount of interest paid on the account, based on the interest rate compounded daily for a 365-day period. That's a mouthful so let me put it in simpler terms.

If a saver puts $100 into an account with an APY of 0.15% (half a percentage point more than the national average) it will take almost 500 years to double her money. A tortoise could make a dozen trips around the world in that time.

For a saver like yourself earning a 0.01% APY, a $1,600 balance will earn about one penny in monthly interest. That's absolutely shocking considering the interest rates banks charge consumers on mortgages, auto loans, and credit cards. More frustrating is the fact that large national banks are some of the biggest offenders when it comes to low APY's.

How banks determine the interest they pay on their savings and sometimes checking accounts depends on a variety of factors. Monetary policy set by the central bank or Federal Reserve, credit market conditions, the economy, and competition from other banks all weigh in. So it definitely pays to shop around for the best rates on savings accounts, certificates of deposit, and money market accounts. Often smaller local banks and credit unions will offer higher interest rates than big corporate banks to attract customers.

You also don't have to limit yourself to bricks and mortar financial institutions where you live. A quick search online will reveal banks located anywhere in the country offering APY's much higher than the national average. Just make sure you're dealing with an established bank that provides Federal Deposit

Insurance Corporation (FDIC) coverage - insurance that protects your account for up to $250,000 per account owner in the event of a bank failure. Hey, it happens.

Now let me go back to your main question. It's always important to save money regardless of how much interest, if any, you earn on those savings. Furthermore saving isn't really about capital appreciation, that's what investing is for. Saving is about safeguarding your deposits or principal and providing liquidity - the ability to quickly and easily withdraw your money.

If you're not satisfied with that answer, ask yourself three questions. Do I have enough money saved to cover three months of emergency expenses? Have I paid off all of my consumer debt; i.e. credit cards and personal loans? Have I reached the point where I can pay all of my bills every month and still have money left over?

If you answer yes to all of the above, you're ready to graduate to the more lucrative, albeit riskier, world of investing.

Ask Dr. Per Cap *is a program funded by First Nations Development Institute with assistance from the FINRA Investor Education Foundation. For more information, visit www.firstnations.org. To send a question to Dr. Per Cap, email askdrpercap@firstnations.org.*