What is interest?

Interest is the cost of borrowing money (or the amount earned on savings).

What are interest rates?

An interest rate tells you how high the cost of borrowing is, or how high the rewards are for saving. Interest rates are expressed as percentages.

How might interest rates affect me?

So, if you're a borrower, the interest rate is the amount you are charged for borrowing money, shown as a percentage of the total amount of the loan. The higher the percentage, the more you have to pay back for a loan of a given size. In simple terms, if the interest rate is 10% on a £1,000 loan, it means £100 is paid in interest so the total amount that needs to be paid to the bank is £1100.

If you're a saver, the interest rate tells you how much money will be paid into your account, as a percentage of your savings. The higher the interest rate, the more will be paid into your account for a given sized deposit.

Even a small change in interest rates can have a big impact. It's important to keep an eye on whether they rise, fall or stay the same.

What's the difference between a fixed interest rate and a variable interest rate?

Banks usually offer both fixed interest rates and variable interest rates. Fixed interest rates do not change over the term (or life) of the loan. Whereas variable interest rates can change. They fluctuate, often because of changes in base rates (benchmark) set by the Bank of England.

Some people prefer the stability of fixed interest rates as the borrower knows exactly how much needs to be repaid every month, so it's easier to predict than variable rates. Some people choose variable interest rates as they offer low interest rates to begin with and some people may be optimistic about a future decrease in the cost of borrowing.