Dollar-Cost Averaging

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If you are investing monthly into a 401(k) or other type of brokerage account, you might be tempted to abandon your long-range plans and take your money out during a volatile market. However, investors may benefit from the strategy of dollar-cost averaging as a way to potentially take advantage of a declining market.

What is Dollar-Cost Averaging?

Dollar-cost averaging is a term for investing a predetermined dollar amount at regular intervals over a period of time, regardless of the purchase price of the investment. When markets are in decline, this strategy allows an investor to buy shares when the cost is lower, reducing the average cost per share over time.[1] Contrast this strategy with lump sum investing of a large amount at one time. Many investors naturally fall into dollar-cost averaging as they invest monthly into retirement or other investment accounts. If you invest the same amount each month into a fund, some months the price of the investment will be higher, but some months the price will be lower. See the hypothetical example below of an investment of $30,000 which shows a comparison of both lump sum investing and dollar-cost averaging strategies over a period of three months.

Dollar-Cost Averaging

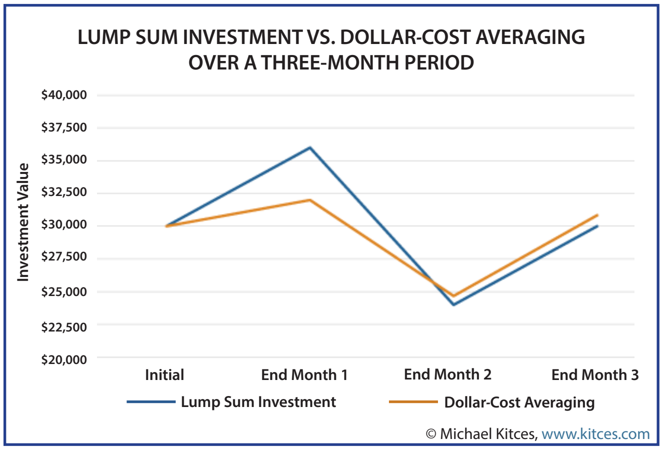
Month	Money Invested	Price/Share	Number of Shares
Month 1	$10,000	$100 per share	100 Shares
Month 2	$10,000	$120 per share	83.33 Shares
Month 3	$10,000	$80 per share	125 Shares
Total	**$30,000**	**Ave. price per Share=$97.30**	**308.33 Shares**
If prices go back to original price/share:		**$100/share at 308.33 shares**	**Value: $30,833**

Source: Michael Kitces, www.kitces.com

Lump Sum Investing

Month	Money Invested	Price/Share	Number of Shares
Month 1	$30,000	100 share	300 shares
Month 2	0	$120 per share	0
Month 3	0	$80 per share	0
Total	**$30,000**	**$100 share**	**300 Shares**
If prices go back to original price/share:		**$100/share at 300 shares**	**Value: $30,000**

Source: Michael Kitces, www.kitces.com



Conclusion

From the hypothetical example, you can see that in a volatile market, the dollar-cost averaging strategy resulted in more shares at a lower cost per share and yielded higher returns than the lump sum investing strategy. Although dollar-cost averaging does not always guarantee a higher value at the end of the time period, especially when the market is steady or going up, it can potentially help reduce the cost of shares in a declining market.[2] Speak to your financial advisor to learn more about dollar-cost averaging and whether it is right for you.

1. McWhinney, J. (2019). Use dollar-cost averaging to build wealth over time. Https://www.investopedia.com/investing/dollar-cost-averaging-pays/
2. Kitces, M. (2016). Dollar cost averaging may help to manage risk but on average it just reduces returns. Retrieved from https://www.kitces.com/blog/dollar-cost-averaging-versus-lump-sum-how-dca-investing-can-manage-risk-but-on-average-reduces-returns/