



Informed Investor Series

Understanding Dollar Cost Averaging

White Paper

The **Informed Investor Series** explores how better understanding markets may help you to make the most informed investment decisions possible.

The **Understanding Dollar Cost Averaging** white paper discusses how it is not always easy to invest when markets are in a downturn and, historically, what we have seen in the markets might suggest that *dollar cost averaging* may be a worthy strategy to consider, particularly if the market is declining.

Understanding Dollar Cost Averaging

It is not always easy to invest in stocks when the market is declining.

Headlines may create fear, and historically fear has not gone well with investing. Concerns may develop like, "What if the market continues to decline after I invest?" "How much further will the market decline?" "How much of my money will I lose?"

The fact is no one can predict the future, and while no two markets are the same and past performance is never an indication of future results, historically, what we have seen might suggest that Dollar Cost Averaging may be a worthy strategy to consider particularly if the market is declining.

Dollar cost averaging is simply a disciplined, systematic, and unemotional method of investing a fixed dollar amount, at regular intervals, regardless of the direction of the market.

As an example, let's assume the market is declining or you fear it will decline and you have \$100,000 that is part of your growth allocation you typically would have placed in stocks. One of the historic challenges of investing in the stock market is that the market is cyclical, . it It goes up and it goes down, but we do not know how much it will go up or how much it will go down, and we do not know when it will do either.

With the \$100,000 investment in a declining market, some investors limit themselves to two options; invest all of it at one time or not to invest it at all out of fear of the declining market.

Dollar cost averaging offers a third option.

Instead of putting all of the \$100,000 in the market today, you can invest at regular intervals, regardless of the stock price. Maybe you decide to invest \$10,000 over the next 10 months or invest the money in equal amounts over the next 12 months.

The advantage of investing this way is that your money buys more shares at the lower stock prices when the market is declining and fewer shares at the higher prices when the market goes higher. What dollar cost averaging does is to take advantage of the fact that markets typically move in cycles.

Let's say that hypothetically you made what we will call a "onetime investment" of your \$100,000 - meaning you put it to work all at once in January of this year when the share price was at \$100. If we divide \$100,000 into \$100 share price, that would mean you bought 1,000 shares ($\$100,000 / \$100 \text{ share price} = 1,000 \text{ shares}$).

What if instead, we hypothetical dollar cost averaged into the market over a 12 month period. Please keep in mind that this is for illustrative purposes only, and does not represent an investment or how any particular investment might reaction in a down market.

Understanding Dollar Cost Averaging

Let's assume in our hypothetical example above, that the market is declining and by July the price is down \$80 a share. The 1,000 shares you bought in your "onetime investment" in January would now be worth \$80,000, a \$20,000 loss (1,000 shares X \$80 share price = \$80,000).

Month Invested	Amount Invested	Price Per Share	Number of Shares Purchased	Cumulative Number of shares	Value of Cumulative Shares	Amount Remaining in Dollar Cost Averaging Account	Total Value
January	\$8,333.33	\$100.00	83.33	83.33	8333.33	\$91,666.67	\$100,000.00
February	\$8,333.33	\$95.00	87.72	171.05	16249.99	\$83,333.34	\$99,583.33
March	\$8,333.33	\$90.00	92.59	263.65	23728.06	\$75,000.01	\$98,728.07
April	\$8,333.33	\$85.00	98.04	361.68	30743.17	\$66,666.68	\$97,409.85
May	\$8,333.33	\$90.00	92.59	454.28	40884.92	\$58,333.35	\$99,218.27
June	\$8,333.33	\$85.00	98.04	552.32	46946.86	\$50,000.02	\$96,946.88
July	\$8,333.33	\$80.00	104.17	656.48	52518.61	\$41,666.69	\$94,185.30
August	\$8,333.33	\$85.00	98.04	754.52	64134.36	\$33,333.36	\$97,467.72
September	\$8,333.33	\$80.00	104.17	858.69	68695.08	\$25,000.03	\$93,695.11
October	\$8,333.33	\$85.00	98.04	956.73	81321.85	\$16,666.70	\$97,988.55
November	\$8,333.33	\$90.00	92.59	1049.32	94438.82	\$8,333.37	\$102,772.19
December	\$8,333.37	\$95.00	87.72	1137.04	108018.79	\$(0.00)	\$108,018.79

In contrast, by July, our dollar cost averaging account would have been worth \$94,185.30. We arrive at this number by taking the 656.48 shares we would have purchased by July and multiplying it by the \$80 share price (656.48 X \$80 = \$52,518.61) plus we would have had \$41,666.69 of our original \$100,000 that we still would not have yet invested. When we add both we have a total of \$ 94,185.30 (\$52,518.61 + \$41,666.69 = \$94,185.30). This compares to the \$80,000 value of our "onetime investment" had we invested all of the \$100,000 in January of this year.

Historically, the stock market has moved in cycles and the likelihood could be that eventually, the market might begin to increase. If by January of next year the price per share was once again at \$100 a share, hypothetically our "onetime investment" would be worth \$100,000 (1,000 shares X \$100 share price) which would be the original amount invested.

However, the dollar cost average account, because you were buying more shares as the market declined, it would be worth \$113,703.99 (1,137.04 shares purchased over the year by dollar cost averaging x \$100 a share = \$113,703.99) compared to the \$100,000 we would have had if we invested all at once.

Understanding Dollar Cost Averaging

This hypothetical dollar cost averaging example would suggest that the benefit of dollar cost averaging in a declining market could be that you lose less when the market hits bottom and because ideally you are buying more shares at the lower prices, your account could be worth more than jumping in the market all at once.

It is important to understand that dollar cost averaging will not protect you from a loss and does not guarantee you a profit. You may lose money if you liquidate shares when the price is lower than the price you purchased them.

However, as you can see, dollar cost averaging has the potential to make what we feel is a significant difference when investing over a period of time and creates a disciplined, systematic, and unemotional method of investing for the long term investor.

Understanding Dollar Cost Averaging

Disclosures

¹Source: Bloomberg and Dunham & Associates

²Facts on File

Investments are subject to risks, including possible loss of principal. Investors should consider the investment objectives, risk factors and expenses of any investment carefully before investing. Diversification does not guarantee profit or ensure against loss.

The S&P 500, or the Standard & Poor's 500, is a stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices. It differs from other U.S. stock market indices, such as the Dow Jones Industrial Average or the Nasdaq Composite index, because of its diverse constituency and weighting methodology. It is one of the most commonly followed equity indices, and many consider it one of the best representations of the U.S. stock market, and a bellwether for the U.S. economy.

All examples are hypothetical and are for illustrative purposes only. We encourage you to seek personalized advice from qualified professionals regarding all personal finance issues. The solution for an investor depends on their and their family's unique circumstances and objectives.

Information contained in the materials included in the Bull & Bear in a CloudSM Marketing Campaign is believed to be from reliable sources, but no representations or guarantees are made as to the accuracy or completeness of information. This document is provided for informational purposes only and should not be construed as individual investment advice.