Dollar-Cost Averaging

Dollar-cost averaging is a big term for a fairly simple concept. If you buy a set dollar amount of stocks or stock mutual funds at regular intervals (e.g., every month or every quarter), you’re using the dollar-cost averaging technique.

For example, you invest $60 each month in stocks or stock mutual funds. During the year the prices of the stocks and mutual funds will go up and down.

- When the price is down, your regular $60 investment in stocks buys you more shares.
- When the price is up, $60 buys you fewer shares.

This is dollar-cost averaging.

Other examples of dollar-cost averaging:

- When you leave your money in a mutual fund and reinvest all of the dividends, you are also dollar-cost averaging.
- If you participate in a 401(k) or other payroll deduction investment plan, you are dollar-cost averaging with each payroll deduction.

If you have a large sum to invest:

- You have a choice of whether to invest it all at once or to dollar-cost average by investing it in smaller amounts spread out over a 12-month period.

Dollar-cost averaging can be a way to limit the risk that can come from investing in a fund or funds just before the price drops.

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