Your plan has an auto-defense against market volatility

One of the hardest parts about investing for the future is choosing when to invest. Is the market on the way up? Or on the way down? Most experts would say it's impossible to know. Fortunately, employer-sponsored retirement plans have a secret weapon: DOLLAR-COST AVERAGING.

Dollar-cost averaging is when a person invests the same amount of money at regular intervals over a period of time. For investors in retirement plans, this is what happens every time a percentage of their income is invested from their paychecks.

With a dollar-cost-averaging approach, investors buy more shares when the price is low and fewer when the price is high. In a volatile market, where security prices regularly go up and down, this helps reduce the impact of any major individual price change.

Retirement Services

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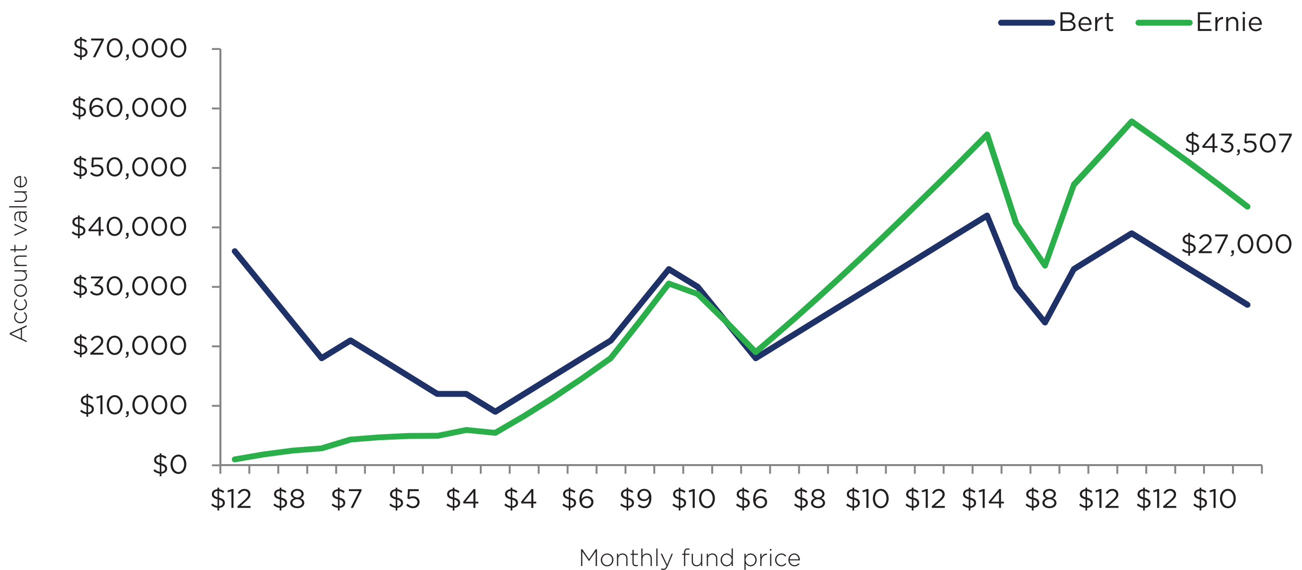
CONSIDER THIS EXAMPLE: Two friends, Bert and Ernie, each decide to invest $36,000 into a mutual fund. Bert invests all of his money upfront, when the value of the fund is at an all-time high. Ernie, on the other hand, puts in $1,000 each month for three years, regardless of the fund's price.



Note: This is a hypothetical example and not indicative of any particular investment product.

In this scenario, because Bert invested all at once, at one of the fund's highest price points, his account lost money when he redeemed it at the end of the 3-year period, and the fund price had dropped to $9 per share. Ernie also bought at the high point, but he bought shares at the low point too. Because he bought more shares when the price was low and fewer when the price was high, Ernie still ended up with a positive return on his $36,000 total investment at the end of the 3-year period.

Of course, not every scenario works out exactly in this way. Dollar-cost averaging does not guarantee a positive result. It does, however, help take the emotion out of investing. People have a natural tendency to want to buy a stock when it is doing well and to sell it when it performs poorly. Buying high and selling low is the exact opposite of what an investor wants to do, and that approach almost guarantees a loss. With dollar-cost averaging, however, the investment happens automatically. That can help prevent the "buy high, sell low" mistake.

People investing for retirement need to think carefully about their fund choices and make selections based on both their time horizon and their comfort with risk. But even with conservative choices, the value of a portfolio will go up and down as part of the market's normal price changes. When the market is particularly volatile and prices are changing dramatically, it is important to remember your retirement plan's secret weapon: dollar-cost averaging.

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