

How pound cost averaging can help you navigate market volatility

Pound cost averaging is the concept of making regular payments into your investments to help smooth out the impact of ups and downs caused by market volatility.

How does pound cost averaging work?

Very simply, it involves making regular payments into your investments rather than investing a lump sum all at once. By making regular payments, you're buying fewer units when prices are high and more when prices are low, essentially averaging out prices. This is why it's often seen as a good approach when markets are volatile. Plus, it removes the worry about making a lump sum investment right before a market fall.

If you invest a lump sum just before a market fall, you'll be buying when prices are high, and you'll miss out on the opportunity to buy more units at a cheaper price. This means that your investment returns are likely to be lower too.

Even experienced investors know that it's almost impossible to time the market – sell investments just before prices go down and buy them just before they go up. And this is particularly true during periods of market volatility, when you could see big rises one day and equally big falls the following day.

So, although with any investment approach the value of your investments can go down as well as up, and you might not get back all the money you paid in, pound cost averaging can feel like a less daunting way to invest.

Key points about pound cost averaging

It can:

- Help create a disciplined, systematic approach to investing
- Remove the worry of making lump sum investments at the wrong time
- Provide a smoother, more consistent way into the market
- Help mitigate the impact of falling asset prices

Pound cost averaging isn't guaranteed to be the best investment strategy, even during periods of market volatility. But it can be a lower maintenance and potentially less stressful approach to investing as you don't have to constantly worry about how markets are performing.



A pound cost averaging example

This example shows how pound cost averaging works for two different people investing in the same asset over a volatile period in markets.

Investor A pays in £1,000 a month over a year, while investor B puts in a lump sum of £12,000 in January. Across the year, the market rises and falls, and the unit price of the asset follows the same trend.

By December, investor A has bought over 1,000 more units and paid a lower average price than investor B. In addition, the value of their plan is almost £2,000 more than investor B's plan.

Month	Unit price	Investor A payments	Investor B payments
January	£2.00	£1,000	£12,000
February	£1.91	£1,000	-
March	£1.74	£1,000	-
April	£1.70	£1,000	-
May	£1.65	£1,000	-
June	£1.57	£1,000	-
July	£1.52	£1,000	-
August	£1.57	£1,000	-
September	£1.61	£1,000	-
October	£1.65	£1,000	-
November	£1.74	£1,000	-
December	£1.83	£1,000	-
Total units bought		7,077	6,000
Average Price Paid		£1.71	£2.00
Final Value		£12,923	£10,956

Pound cost averaging in rising markets

Of course, there's no guarantee that pound cost averaging will result in better outcomes than investing a lump sum. And it's important to understand that in a rising market, investing a lump sum from the start would mean you'd be buying investments at a lower price, which in turn could potentially mean higher long-term returns.

However, ups and downs are part of investing, and no one can say with any certainty when markets will stop rising. So pound cost averaging can be a useful approach to make sure you don't buy at the wrong time and are able to take advantage of market volatility.



Remember, investments can go down as well as up and you might not get back all the money you paid in.



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