Benefiting from volatility

In volatile markets it is quite understandable to be concerned about the value of your investments. However, it is possible to make market volatility work for you. Regular investing, usually monthly, and phasing, drip feeding a lump sum into an investment over a number of months, can work to your advantage in volatile markets.

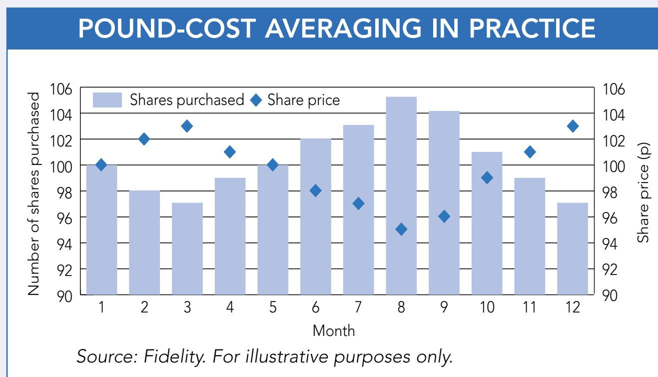
The main benefit of investing regularly is known as 'pound-cost averaging'. Don't let this complicated term confuse you as the principle is quite simple really. If the market does fall, then you know that your next monthly investment will benefit from the higher number of shares you will be purchasing at the lower price. Of course, in a rising market, this will result in less shares being purchased but then your existing shares should be showing a profit.

Over a period of a few years, pound cost averaging means that the average price paid can be lower than the average share price for that period since more shares are bought when prices are low and fewer when prices are high.

How does it work?

The diagram below shows how the share price of a theoretical investment (represented by the dots) can fluctuate over time. As can be seen from the bars, an investment of £100 per month buys a lower number of shares when the share price rises but a higher number of shares when the share price falls.

POUND-COST AVERAGING IN PRACTICE



Source: Fidelity. For illustrative purposes only.

Please note that past performance is not a guide to what might happen in the future.

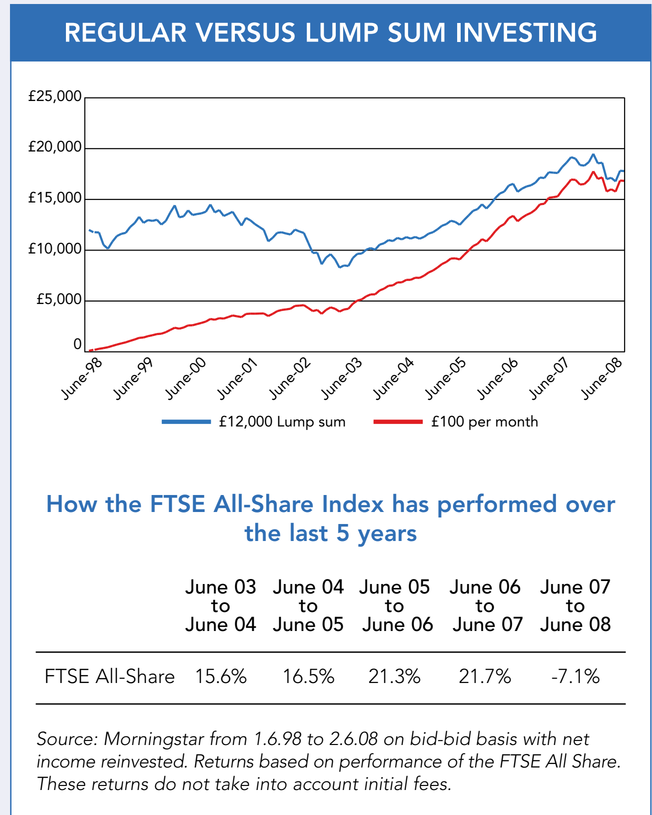
You should be aware that unlike a deposit account, the value of investments can go down as well as up and you may not get back the amount invested.

No need to time the market

We all know that markets can go up and down but often these movements can be quite extreme. In volatile markets, investing regularly or phasing means that you don't have to worry so much about putting all your money into shares just prior to when prices may fall.

The illustration below shows how a regular investment of £100 per month invested in UK shares over the last 10 years would have performed against a lump sum investment of £12,000 (i.e. £100 x 12 months x 10 years). Whilst investing a lump sum upfront ultimately resulted in a better overall return, investing monthly produced a much smoother return, helped by pound cost averaging reducing the effects of market volatility. The falls in the market between 2001 and 2003, meant that the regular investment of £100 purchased more shares which helped to boost the investment value when the market recovered.

REGULAR VERSUS LUMP SUM INVESTING



How the FTSE All-Share Index has performed over the last 5 years

	June 03 to June 04	June 04 to June 05	June 05 to June 06	June 06 to June 07	June 07 to June 08
FTSE All-Share	15.6%	16.5%	21.3%	21.7%	-7.1%

Source: Morningstar from 1.6.98 to 2.6.08 on bid-bid basis with net income reinvested. Returns based on performance of the FTSE All Share. These returns do not take into account initial fees.

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