Key Wealth

Key Wealth Institute

Dollar-Cost Averaging: A Steady Path to Investing Success

For many, the stock market can be a daunting place. The fear of making a wrong move, buying at the peak or losing because of market swings often keeps investors on the sidelines. But there is a simple, effective strategy that could help ease these fears while building wealth over time. Dollar-cost averaging (DCA) values consistency over perfect timing and can help you reduce the overall cost per share.

In the DCA approach, an individual invests a fixed amount of money at regular intervals — regardless of market conditions. Instead of attempting to time the market, which even professional investors struggle to do successfully, DCA spreads purchases over time: You buy more shares when prices are low, and fewer when prices are high, a strategy that is likely to reduce the overall cost per share of the equities you select.

If you contribute regularly to a 401(k) or another employer-sponsored retirement plan, you're already using DCA. A portion of your earnings is invested automatically with each paycheck, taking the guesswork out of when to buy. But you can also use DCA as a personal investing strategy that can provide an average cost per share that's lower than the average market price (though it can't guarantee a profit or protect against a loss in a declining market).

A personal approach: Meet Lila Byars

Lila Byars is a 35-year-old single marketing manager who wanted to build her financial future but wasn't comfortable navigating the stock market's complexities. She recently got a promotion and a sizeable bump in pay. She already had a modest 401(k) through her employer, but she wanted to use her extra cash for something more daring, but not too risky, because she feared market downturns.

After reading about dollar-cost averaging, Lila developed a strategy, following these helpful tips:

Determine your investment intervals and amount

Lila calculated she could comfortably invest $500 each month.

Choose an investment vehicle

Because of her age, she decided she could invest in a popular but sometimes volatile stock, instead of a safer investment such as a mutual fund.

Set up automatic contributions

Automating her investment ensured consistency and removed the temptation to time the market.

Stick to your plan

Market ups and downs are inevitable, but Lila stayed committed to the strategy.

To get started, Lila opened a brokerage account with automatic monthly transfers from her linked bank account to purchase the stock. After Lila began investing, the price per share was high for some months; for other months, it was lower. But instead of stressing about timing the market, she remained focused on her long-term goal.

By the end of the year, her disciplined approach helped her buy shares at an average cost lower than the stock's average price. She fared far better than if she had saved $6,000 and bought all at once in December.

The math behind dollar-cost averaging

Lila is a fictional investor, but we used an actual S&P 500 stock performance in 2024 to break down her investment over the past year. We won't name the stock but you can sample this method with any equity you prefer.

Month	Investment	Price/Share	Shares Purchased
January 2024	$500	$108.10	4.62533
February 2024	$500	$172.31	2.89995
March 2024	$500	$150.83	3.31475
April 2024	$500	$165.04	3.02951
May 2024	$500	$169.12	2.95612
June 2024	$500	$216.13	2.31336
July 2024	$500	$240.62	2.07747
August 2024	$500	$209.01	2.39225
September 2024	$500	$235.16	2.12617
October 2024	$500	$238.78	2.09385
November 2024	$500	$318.22	1.57114
December 2024	$500	$415.96	1.20207
Total	**$6,000**		**30.60197**

Average cost per share with DCA (rounded):

$196

($6,000 ÷ 30.60197)

Average market price per share:

$220

As you can see, Lila's average cost per share is 11% lower than the average market price per share of her stock in 2024, demonstrating how DCA can be beneficial in a volatile market, helping to average out the purchase price over time.

Advantages of dollar-cost averaging

DCA offers several key advantages to investors. Among them:

Reduced risk

By investing consistently, you avoid the risk of investing a large sum of money at a market peak. When the market is down, your fixed dollar amount buys more shares. When the market is up, your money buys fewer shares. This strategy can help lower your average cost per share over time.

Emotionless investing

DCA takes the emotion out of investing. You don't have to worry about timing the market or making impulsive decisions based on fear or greed.

Discipline and automation

DCA instills discipline in your investing approach. You can set up automatic investments, making it easier to stick to your plan.

Accessibility

DCA is a viable option for investors of all levels, especially those without a lump sum.

Why not invest in one lump sum?

Lump-sum investing involves investing a large sum of money all at once instead of spreading it out over time with dollar-cost averaging.

Proponents of lump-sum investing argue that markets have historically tended to rise over the long-term, so investing a lump sum as soon as possible gives the investment more time to grow. This approach can particularly appeal to those who have received a sudden influx of cash, such as an inheritance or a work bonus. However, lump-sum investing carries a higher degree of risk, exposing the entire investment to market volatility at a single point in time.

Now, if Lila had invested $6,000 in January 2024, she would have made larger gains by the end of the year. However, she didn't have that much cash on hand at the time. If she had waited until she had the entire $6,000 in her bank account in December, she would not have fared nearly as well. On December 24, 2024, Lila's stock was one of the hottest in the country and closed at $462.28. If she had invested the lump sum then, she would have been able to purchase only 12.98 shares. When the stock price slipped to $355.70 on February 14, 2025, her portfolio would have been worth only $4,616.59.

In comparison, her DCA strategy allowed her to purchase 30.61 shares in 2024, which had a value of $10,893.98 that same day.

Is dollar-cost averaging right for you?

DCA can be a suitable strategy for many investors, but it's essential to consider your circumstances and goals. DCA can be a wise choice if you're investing for the long term and want to avoid timing the market.

Key factors you should consider include:

Investment goals

DCA aligns well with long-term investment goals such as retirement savings.

Market volatility

DCA can help mitigate the impact of market volatility on your investments.

Discipline

DCA requires discipline to invest consistently, regardless of market conditions.

Tax implications

When Lila eventually sells her shares, she'll likely have to pay capital gains taxes on any profit she makes. The amount of tax she owes will depend on how long she holds the shares and her income tax bracket. Short-term capital gains (for assets held less than a year) are taxed at her ordinary income tax rate. Long-term capital gains (for assets held longer than a year) are taxed at lower rates.

Dollar-cost averaging also has limitations, such as:

Missed opportunities

DCA may result in lower returns in a consistently rising market compared to investing a lump sum initially.

Time commitment

DCA is a long-term strategy that requires patience and discipline. It may take time to see significant results.

Fees

Depending on the investment and brokerage platform you use, fees may be associated with each investment transaction. You should compare various institutions' fees before you begin investing. These fees can eat into your returns over time.

Final thoughts

For Lila and many other investors, dollar-cost averaging offers a straightforward way to participate in the market without worrying about perfect timing. Investing regularly and consistently allows you to take advantage of market fluctuations while steadily building your portfolio.

By understanding DCA's mechanics, potential benefits, and limitations, you can decide whether this strategy is right for you. Remember, dollar-cost averaging is not a guarantee of success, but it can be a valuable tool for building wealth long-term.

For more information, please contact your advisor.

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