

A strategy for investing in changing market conditions

Rupee Cost Averaging

An investment strategy
for volatile markets



Shahid Afridi is always advised to go easy with the bat and boost the score by including singles in his game rather than only going for boundaries. The advice might be conservative but the aim is to ensure that he doesn't risk his wicket in the frenzy of hitting trajectories over the ropes.

Investors are often cautioned the same advice when it comes to investing. Don't risk your money in the hope that sixes and fours are always going to result in big scores. Rather than just going for the big hits, devise a strategy which involves a consistent mix of singles and boundaries. Invest regularly rather than waiting to make all your money in a single go. This would ensure that even in relatively worse economic conditions, if prices were to plunge drastically, your investment could subsequently rebound and shield you from the fury of capital markets.

The idea to buy units when prices are low and sell when prices

are high; seems so simple. But the reality is that no one investor can time the market to perfection. How do you when prices are low? How do you when prices are high? How do you find out the change in the cycle? Is there a genie that would knock on your door and tell you that the timing of the market is great? The answer to all these questions is that "There is no way of knowing". Timing the market is like gambling with uncertainties.

Although practically impossible to time the market, it is still possible to reap the rewards of the peaks in the market and hedge yourself against the market diving downwards. This wise concept in investment terminology is known as 'Rupee Cost Averaging' (RCA). Investors are not psychics but every investor likes a healthy profit! The way to ensure strong and healthy returns is to make sure that a fixed pre-determined amount of money is invested regularly for a longer period of time.

Rupee Cost Averaging Basics

Rupee Cost Averaging is an effective investment strategy that takes out market timing from the investment equation. All one has to do is to invest a fixed, pre-decided amount of money on a regular basis over a longer period of time.

The amount invested per month is constant but one buys more units when the price is low and fewer units when the price is high which implies that the average cost per unit is also on the lower end.

One of the biggest advantages of this strategy is that it takes emotions out of investing and disciplines investors to adhere to their strategy when markets turn volatile. In fact, often one of the worst things investors can do when the market dips is to take their money out of the market, because it often means selling low and missing the chance to add to a portfolio when prices are down.

Regular investing following Rupee Cost Averaging can help you cope with the human tendency of hesitating to invest in a declining market, when the price of an asset may actually be more reasonable.

Does it work when prices are rising and falling?

The purpose of rupee-cost averaging is to take the guesswork out of investing by providing you with an average cost per share that's lower over the long term. Let's look at 2 examples to see what your average price per share would be when prices are rising and when prices are falling.

When unit price is rising. When unit price is rising, Rs.5000 is invested in a mutual fund on the first of each month. The investor in this example would methodically acquire 1098.9 units at an average cost of Rs.27.83 each. And there's no guesswork or worry about what the price is about to do.

When unit price is falling. Rupee-cost averaging in this scenario can reduce loss compared to making a lump-sum investment. Rs.5000 is invested in a mutual fund on the first of each month. The investor in this scenario would have bought 986.3 units at an average cost per unit of Rs.30.83. The investment's value at the end of the period would be Rs.25643.8.

By comparison, someone who invested the entire Rs.30,000 in January at Rs.38 per unit would have owned only 789.4 units, and the investment would have been worth only Rs.20524.4 at the end of the period.

RUPEE-COST AVERAGING WHEN UNIT PRICES RISE			
Month	Amount Invested	Unit Price	No. of Units Purchased
01-Jan	Rs.5000	Rs.22	227.3
01-Feb	Rs.5000	Rs.26	192.3
01-Mar	Rs.5000	Rs.26	192.3
01-Apr	Rs.5000	Rs.28	178.6
01-May	Rs.5000	Rs.31	161.3
01-Jun	Rs.5000	Rs.34	147.1
Total:	Rs.30000	Avg Cost: Rs.27.83	Total: 1098.9

RUPEE-COST AVERAGING WHEN UNIT PRICES FALL			
Month	Amount Invested	Unit Price	No. of Units Purchased
01-Jan	Rs.5000	Rs.38	131.6
01-Feb	Rs.5000	Rs.31	161.3
01-Mar	Rs.5000	Rs.29	172.4
01-Apr	Rs.5000	Rs.32	156.3
01-May	Rs.5000	Rs.29	172.4
01-Jun	Rs.5000	Rs.26	192.3
Total:	Rs.30000	Avg Cost: Rs.30.83	Total: 986.3

Is rupee-cost averaging right for you?

Rupee-cost averaging is a very effective and globally accepted concept. If a fund's unit price fluctuates a lot, rupee-cost averaging can prove to be very effective way to offer smart investment exposure with a hedge against market volatility. The most important element of rupee-cost averaging is commitment and sticking to your investment schedule.

Rupee Cost Averaging is designed for investors who believe in the power of the capital markets yet don't have the stomach to deal with its volatility. RCA's systematic approach to investing and withdrawing is an effective way to accumulate wealth over the long term. Rupee-cost averaging doesn't guarantee a profit or eliminate risk, and it won't protect you from a loss if you sell shares at a market low. Before adopting this strategy, you should consider your ability to continue investing through periods of low price levels.

Call us at 0800-24611



HEAD OFFICE
Mezzanine Floor,
Bahria Complex III,
M.T.Khan Road, Karachi.
PABX: +92-21-35635312-4
FAX: +92-21-35635315

REGIONAL OFFICE (NORTH)
Office No. 502, 5th Floor,
Green Trust Tower,
Blue Area, Islamabad.
Tele: +92 51 111-246-111
Fax: +92 51 2813017

REGIONAL OFFICE (CENTRAL)
Office No. 101, 1st Floor,
Siddiq Trade Centre,
72 Main Gulberg, Lahore.
Tele: +92 42 35876277-8
Fax: +92 42 35792111