Why Regular Investing Could Enhance Your Returns

Description

For many investors, the idea of regularly buying shares in small amounts is rather unattractive. After all, it can mean more effort in terms of submitting more than one trade, while commission costs can mount up even in a world of low-cost online sharedealing.

However, buying shares regularly in small amounts can be a prudent move. It can lead to less volatility and even improved returns in the long run. Plus, aggregated orders can mean the time and cost of trading more than once is only marginally higher.

Risk/reward

For any investor buying shares in any company, there is a risk of loss. Profit warnings can come from nowhere, while wider market falls can start without any prior warning. As such, putting a significant amount of capital into one or more stocks in one transaction could be a risky move. The company (or companies) in question may make a surprise announcement about unsatisfactory recent trading, while investor sentiment may react negatively to more general economic data which is worse than expected.

Buying in small amounts on a regular basis helps to neutralise this short term risk. It means that if after the first purchase a share price falls, an investor may be able to obtain a lower average entry point than they would have done if they had made only one large transaction. Clearly, the opposite is true if the share price rises following the first purchase, but even in that situation the investor in question would still be in a profitable position.

Psychology

An investor buying regularly may also be less worried about the short term price movements of a particular stock. They know that even if the share price falls in the near term, they will still be able to take advantage of it. In fact, it may be a better situation for them than a stock price which is rising, as their capital returns in the long could end up being higher.

The effect of this on their attitude may also be positive. They may worry less in the short term, which could help them to keep a clear mind when considering their next investment decisions. In contrast, an investor who makes fewer, larger transactions may end up obsessing over the short term performance of their portfolio. This could lead to less mental capital for considering the long-term opportunities on offer.

Costs

In the past, the effort and cost of buying shares in small parts was viewed as outweighing any potential advantages. Today, though, aggregated orders mean commission costs can be ultra-low, since they are aggregated with the orders of many other investors seeking to buy the same stocks at the same time. Furthermore, orders can be inputted well in advance or even on a regular basis, thereby reducing the amount of effort required on the part of the investor.

As such, buying shares in small amounts and investing regularly could be a means of improving returns and also reducing risk. Therefore, it seems to be a worthwhile pursuit for Foolish investors.

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peterstephens