Dollar Cost Averaging in a Bear Market

Description

Dollar cost averaging is the act of investing a specific amount in a certain investment over time. When the price of the investment is high, you'll buy a lower number of shares. When the price of the investment is low, you'll buy a higher number of shares. For example, a passive investor might buy $100 every month in a market-wide exchange-traded fund (ETF) like **SPDR S&P 500 ETF Trust**.

The stock market is correcting. So, a dollar cost averaging investing strategy is not a bad idea. But investors need to be extra careful in a bear market, in which prices are sliding more quickly than normal. Here are a few things to keep in mind.

Be diversified

Dollar cost averaging into SPDR S&P 500 ETF Trust is a good way to invest for investors who prefer to invest passively. You might also balance your investment with a bond fund. Otherwise, no matter how attractive a stock appears to be, don't put all your eggs in one basket. Diversifying across a group of the best ideas in different sectors is a safer way to invest.

Buy quality businesses

If you choose to be a do-it-yourself investor by investing in individual stocks, you should consider dollar-cost averaging into quality businesses during a bear market. In a bear market, something is broken in the economy, and most, if not all, stocks fall. You will have peace of mind holding quality names.

What are quality businesses? They should report stable and growing profits in the long run. Ideally, these stocks will also pay sufficient yields with safe dividends. In today's rising interest rate environment, a sufficient yield may be +4%.

You can start investing by researching big Canadian bank stocks, big telecom stocks, and stable utility stocks during a bear market. Right now, among the big bank stocks, **Bank of Nova Scotia** and **CIBC** offer the largest dividend yields of over 5%. Their stocks are also discounted by about 11% and 17%, respectively. A pundit believes the bank stocks could drop at least another 8% in this market downturn, which would imply yields of +5.5% in these high-yield bank stocks.

Since the big Canadian bank stocks tend to increase their dividends over time, it's a good idea to consider buying them in bear markets and lock in a juicy yield. You would expect them to rebound in time and continue churning out greater earnings and dividends over time.

Keep costs low

It's certainly smart to dollar cost averaging in a bear market. However, it may not be too smart to dollar cost average too frequently if you're paying trading fees. Thankfully, some online brokerages now offer free trading, which allows investors to dollar cost average at no cost.

Even if you're trading for free, it would be better to set buy points ahead of time so that you won't be swayed by wild market movements in real time on market open days. Your online brokerage may allow you to set up alerts that can notify you when certain stocks hit a certain price point.

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