



# Investing A Large Sum: Phase It In, Or All At Once?

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**F**lashback to October 2014. Stocks were on a roll. The Canadian market and several global indices had just turned in 1-year returns of 20%+, and the Canadian bond market was up 6%. The past five years in general had been a profitable period in the markets and investors had little to complain about. But geopolitical tensions were heating up, China was starting to slow down, the price of oil had just dropped 15% over the summer, and stock valuations were reaching expensive territory relative to historic levels. Some investors were starting to get skittish, and more managers were calling for caution.

Enter Tim, an engineer in his mid-50s who was due to receive \$500,000 before year-end from an inheritance. Tim invests with Steadyhand Investment Funds and holds the Founders Fund (a fund with a benchmark of 60% stocks/40% fixed income). His intention was to invest the money in line with his long-term plan, but he was wary of the markets. Tim's not a fan of volatility, but also realized that he needed to put the money to work if he wanted to see it grow over time. Keeping it in a bank account or GICs wouldn't do him any favours given the prevailing interest rates. He considered three options:

- 1. Invest it all at once;**
- 2. Phase it in, in pre-determined tranches (dollar cost averaging) over the course of the next year;**
- 3. Keep it in cash and wait until a better entry point presents itself.**

It was a decision Tim lost a lot of sleep over. Receiving a large sum of money can be a nice problem to have, but it can also come with a lot of stress. If you were in Tim's shoes, what would you have done?

## The Decision: Dollar Cost Averaging

Tim decided to commit to dollar cost, averaging the money into the Founders Fund. He set up a plan whereby he would invest the \$500,000 in four tranches of \$125,000 each. The transactions would take place on December 31, 2014; March 31, 2015; June 30, 2015; and September 30, 2015. His decision provided him with some peace of mind, knowing that he wouldn't invest all the money at once at a potentially inopportune time. But he would only know in hindsight whether his returns would be better or worse as a result of his strategy of phasing the money in.

Tim's decision was probably the best choice for him given his anxiety over what to do. He was wise to go with either the first or second option. Sitting in cash and waiting for a better entry point would've likely caused him a lot more stress, not to mention plenty of second-guessing, market watching and gray hair. Nobody knows what will happen in the markets in the short term, and picking an entry point can be an extremely difficult decision. Indeed, we've come across investors who moved to cash after the market meltdown of 2008/'09 with the intention of getting back in at a better time, but are still waiting on the sidelines. The gains they've lost out on have been substantial.

## The Result

The last tranche of Tim's dollar-cost averaging plan occurred on September 30th. His money is fully invested and we now have the benefit of hindsight when evaluating his return. His investment was worth \$492,860 as of September 30th (down 1.4%). If he invested the money in a lump sum on December 31st, it would have grown to \$506,600 (up 1.3%).

Tim's decision cost him in the form of a lower return (in fact, a negative return), but it provided him with peace of mind, which is a tradeoff that some investors are fine with. When evaluating the results, one could conclude that Tim would have been better off sitting in cash rather than going the dollar cost averaging route. While this may be true, Tim would still be left with the question of when to invest the money. Further, knowing that he would've avoided a small loss by sitting in cash could lead him to believe that he has some skill in timing the market, and he may be inclined to wait it out longer. As mentioned, this can be a dangerous game. To this point, consider that although Tim's investment dropped modestly in value at September 30th, it had grown to \$507,200 just one month later (at the time of writing).

Dollar cost averaging won't always produce an inferior return to a lump sum investment. In a steadily declining market, it will produce a better result. And if implemented over a longer time period, it can serve as

a valuable strategy in dampening a portfolio's volatility. That said, markets rise more frequently than they fall, and studies have shown that returns are more often better with a lump sum investment approach (Vanguard has produced a good research report on the topic, available at [https://pressroom.vanguard.com/content/nonindexed/7.23.2012\\_Dollar-cost\\_Averaging.pdf](https://pressroom.vanguard.com/content/nonindexed/7.23.2012_Dollar-cost_Averaging.pdf)).

Tim's dilemma is not uncommon. Because of the emotional benefit that dollar cost averaging can provide, it can be a valuable strategy for investors like him. If one thing's for certain, it's that either approach to investing a large sum of money beats sitting on the sidelines indefinitely.

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