



Prudential Investment Managers

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What is rand cost averaging and how does it benefit your investments?

When the future looks uncertain and markets seem volatile, rand cost averaging is an effective technique that has been shown to serve investors well over the long term.

How does it work?

Simply put, rand cost averaging is the process of “phasing in” an investment amount over regular intervals instead of as a single lump sum. This allows investors to capture different prices over time, thereby smoothing out the risk of price volatility. One of the more practical approaches to rand cost averaging is to purchase units (in a unit trust fund) via debit order each month. To demonstrate how this works, the below example assumes that you have just started a monthly debit order investment of R500.

In month 1, the cost of a unit is R1. This means that your R500 debit order

investment buys you 500 units in the fund ($R500 \div R1 = 500$ units).

In month 2, markets crash. The value (price) of the units in your fund drops to 50c per unit. You still own 500 units, but at 50c each, the value of your investment is now worth R250 instead of R500 ($500 \text{ units} \times 50\text{c} = R250$). You continue to make your monthly debit order investment of R500, however, this month your investment amount buys you 1 000 units since the unit price is 50c ($R500 \div 50\text{c} = 1\,000$ units). You now have a total of 1 500 units in your fund, and the value of the investment is worth R750 ($1\,500 \text{ units} \times 50\text{c} = R750$).

In month 3, markets bounce back and the price per unit rebounds to R1.25. Your monthly debit order investment of R500 therefore buys you another 400 units ($R500 \div R1.25 = 400$ units), bringing your total number of units to 1 900, valued at R2 375 ($1\,900 \text{ units} \times R1.25 = R2\,375$). However, the total amount that you invested over the 3-month period was only R1 500. So where did that extra R875 come from?

Well, you could think of it as a “reward” for sticking to your plan, rather than panicking when the market crashed in month 2. If you had panicked and decided not to invest for that month, you would have missed out on the opportunity to buy more units at a lower price. You might have thought you’d keep your R500 safely in your bank account, in case the market tumbled further, which seems a perfectly “cautious” move to make. The problem with this approach, however, is that investors often feel that the “right” time to add to their investment is only once markets have recovered, and consequently, the opportunity to purchase units cheaply has passed.

This brings us to the second benefit of rand cost averaging, in that following a set strategy reinforces positive investor behaviour. Looking back to the market sell-off in March/April 2020, the future looked particularly bleak and scary. As markets tumbled, the unit prices of most funds across the world dropped significantly. Not only were investors fearful of what this meant for their investments, they were also fearful for their jobs, their businesses, their health, their loved ones, and ultimately their future. Pausing a debit order investment until the world seemed a little more stable would have seemed like a perfectly rational, sensible thing to do. But as our example demonstrates, veering away from your investment plan when markets were down would have significantly eroded the value of your investment. Nobody would have guessed how quickly

markets would have tumbled, and subsequently recovered thereafter. Those who kept their debit order investments running throughout the sell-off would have benefitted from buying more units at far reduced prices when things looked most bleak.

This is perhaps the biggest benefit of rand cost averaging in that it removes emotions from the investment process. When markets are down, you don't have to panic and wonder what to do. You don't have to change course or make big decisions. By simply sticking to your plan, and continuing your monthly debit order, regardless of the "noise" and the "narratives" around you, you are likely to reap the rewards in the long term.

At Prudential, we have a range of unit trusts for you to choose from to start a debit order investment, beginning from as little as R500 per month. To view our full fund range please visit the [Our Funds](#) section of our website or try our [Fund Selector tool](#) to see which Prudential fund is best suited to you. Our [Past Performance tool](#) is also a great way to see what the value of your investment would have been if you started your debit order investment sooner. And if you're ready to start [investing now](#), you can do so online in under 10 minutes.

For more information please feel free to contact our Client Services Team on 0860 105 775 or email us at query@prudential.co.za.