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Dollar Cost Averaging

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Abstract

Dollar Cost Averaging is a strategy for purchasing equity securities that is widely recommended by professional investment advisors and commentators, but which has been virtually ignored by academic theorists and textbook writers. In this paper we explore whether the strategy is but another instance of irrational behavior by individual investors, or whether it is an investment heuristic that has survival value in an environment in which security prices exhibit mean reversion behavior that has only belatedly been recognized by academic theorists. Our evidence supports the view that the uninformed individual investors who follow this strategy in purchasing individual stocks to add to an existing portfolio are better off than if they followed the 'rational' strategies traditionally recommended by academics.

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