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FACTSHEET

Time is of the essence

Start thinking about preparing for any big events as soon as you can

None of us know exactly what life's got in store for us, but we know that there are a handful of major events that we're quite likely to encounter at some stage. These include some of the great milestones of life, such as buying a property, getting married, starting a family, buying a holiday home or planning for retirement.

It's essential to start thinking about preparing for any big events as soon as you can. Often this means saving for major expenses that may not yet be in sight but which we know are awaiting us just over the horizon.

READILY ACCESSIBLE SAVINGS

Before you start investing for the medium to long term, initially it's important to keep three to six months' worth of living expenses in a readily accessible cash savings account – don't invest that money! Don't invest any money that you may need to access in a hurry in the event of a short-term emergency.

By investing in stocks and shares, you'll gain access to potential returns that saving in cash alone cannot offer. Of course, there is an inherent risk that some or all investments may not keep pace with cash or may even go down in value, but real risk should be seen as the permanent – not temporary – loss of capital. Saving in cash carries its own risks when low interest rates fail to keep pace with price inflation.

TEMPORARY MARKET SENTIMENT

While investors must accept the short-term fluctuations of markets, those investing for the long-term are usually in a position to ignore day-to-day gyrations in asset values. Over the long run, asset prices follow their fundamental values – either up or down – rather than being affected by temporary market sentiment.

Timing the right moment to enter the market is notoriously difficult. While you may have a lump sum that you'd like to invest, implementing a regime of regular investment might be a lower-risk approach, even though you might forgo the opportunity to invest your money at the bottom of the market when an asset is at its cheapest.

TIMING THE MARKET

Investing regularly reduces the danger of making a one-off investment at the top of a market cycle before asset values fall. At some points, you may have to pay more than if you had made a lump sum investment, but at others you could pay less – unless of course the price of the asset rises (or falls) each and every month onward. By keeping to a regime of regular investment, the emphasis shifts away from timing the market to time *in* the market.

POUND-COST AVERAGING

You also benefit from 'pound-cost averaging' by investing the same amount each month, perhaps through Direct Debit. When the price of an asset is high, you will buy less of it, and when the price is low you will buy more.

The effect of 'pound-cost averaging' means that, on average, the price paid is lower than the average asset price over the period. There is no guarantee that pound-cost averaging will result in better returns than lump sum investing, but it can help smooth the ups and downs of market volatility.

GENERATING EXTRA RETURNS

The earlier you commit to investing an affordable monthly amount, the longer your money can work in the market. Reinvested gains can themselves generate extra returns, creating the effect of compounding, which, in a growing market, is larger the longer money is invested.

It follows that the nearer to the time when you plan to realise your investments, the less time your money will have remaining to achieve compounded returns. It is worth bearing this in mind when regularly reviewing your investments, which themselves should be updated to take account of any changes in your circumstances or priorities.

PERCENTAGE OF YOUR SALARY

Much as your pension contributions (when a percentage of your salary) will automatically rise in line with any salary increases, it could be worth applying the same principle to the amount you regularly invest. Increasing your Direct Debits will help to ensure your investments can continue to keep pace with your long-term goals.

Failing to increase your regular investment contributions means that, over time, their real value – and the quantity of assets they will buy – will normally fall. To improve the chance of your investments growing over time to meet your future financial goals, make sure you review your monthly contributions regularly so they don't fall behind both inflation and your means. ■