

Stock Market Returns from 1815 to 1925

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It could be said that our insight into the stock market is as long as the tips of our noses. Perhaps that is right. Walk into any broker's office, look at the stock market chart on his wall, and undoubtedly you will see a chart of the wealth indices of investment in the U.S. capital markets beginning in the year 1926. Why 1926? That only represents the last 80 years of the history of mankind. Were there no stock markets before 1926? What is so unique about this date, and what can we learn from the stock market if it did exist before 1926?

To answer the last part of the question, the stock market did exist before 1926. And to be more to the point, 1926 is a date that is believed to be when quality financial data became available. To answer the larger question regarding the stock market's appearance prior to 1926, we have the most helpful insight from Ibbotson Associates, Inc.'s recent chapter in the *Stocks, Bonds, Bills and Inflation Yearbook 2006*, entitled "Stock Market Returns from 1815 to 1925." This study focuses on the history of the New York Stock Exchange. What follows is a condensed version of the article with a few supplements.

Equity prices for companies listed on the New York Stock Exchange (NYSE) were not published from a single source over the period of January 1815 to December 1870. For many years those bulletins were inscribed by hand with a stylus on a sheaf of tissue and carbon paper that produced up to 24 copies at a time. Until the introduction of the small,

hand-cranked printing presses in the mid 1880s—and with the Dow, Jones news ticker in 1897—these hand written bulletins were the main source of information for Wall Street traders and investors. Dow, Jones & Co. continued to deliver bulletins by messenger until the end of World War II.¹

From 1871 through 1925, major New York newspapers were publishing stock prices. The *New York Shipping List* served as the official source for NYSE share price collection until the early 1850s. In the mid 1850s, the *New York Shipping List* reported prices for fewer and fewer stocks. Therefore Ibbotson had to go to other papers such as the *New York Herald* and *The New York Times* to fill in the gaps.²

It is important to note that companies were rather concentrated into specific industries. In 1815, the index was almost evenly split between banks and insurance companies. Banks, transportation firms (primarily canals and railroads), and insurance companies made up the index by the 1850s.³ By the end of the sample period (1925), the index was dominated by transport companies and other industrials. The first Dow Jones Average appeared in the *Afternoon News Letter* on July 3, 1884. It consisted of the closing prices of eleven companies: nine railroads and two industrials.⁴ Industrial companies tended to rely on a combination

of debt and their founders' wealth to finance their growth. This was partly a matter of choice as incorporation did not offer major benefits to owners at that time. But it was partly because the securities of industrial corporations were regarded as peculiar, unstable, and speculative. Even the largest and most visible firms were not public corporations. For example, two industrial giants of the period, the Singer Manufacturing Company and McCormick Harvesting Machine, were still closely held corporations.⁵

To provide the reader with a frame of reference, the War of 1812 ushered in new economic development. People no longer felt economically dependent on Britain and renewed their efforts to establish links between the agricultural West and the industrial East. Canal companies took advantage of this new-found mode and built canal systems to link the East to the West, canals we know as the Erie and the lesser Chesapeake and Ohio Canals. Railroads were unproven then, but locomotive power to pull heavy freight loads was soon developed.⁶ The industrial revolution was under way. It would provide the impetus to move the capital structure of the markets from private hands to public in the course of 100 years.

Ibbotson's study shows that from 1815 to 1925 the distribution of raw stock prices for much of the period remained around \$100 per share. They also analyzed the income re-

1 Capital Ideas, *The Improbable Origins of Modern Wall Street*, Peter L. Bernstein, Wiley Press, 1992, p. 24

2 *Stocks, Bonds, Bills and Inflation 2006 Yearbook*, Ibbotson and Associates, Inc., p. 193

3 *Stocks, Bonds, Bills and Inflation 2006*, p. 195

4 Capital Ideas, p. 27

5 *Ibid*, p. 28

6 *Official National Handbook*, Chesapeake and Ohio Canal, 1991, p. 15



Stock Market Returns *continued*

	Income Return	Capital Appreciation	Total Return	Standard Deviation
1825 to 1925	5.9%	1.3%	7.3%	16.3%
1926 to 2005	4.2%	5.9%	10.4%	20.2%

turn (dividends) to shareholders and found that the geometric mean of returns to be 5.9%. Capital appreciation of stocks, on the other hand, had a geometric mean of 1.3%. The table above compares the returns for this period to the 1926 to 2005 period.

Ibbotson's conclusion is that dividend policies have evolved over the past two centuries, and that management of old most likely paid out earnings and kept their stock prices lower.⁷ Given the fact that in the 1800s shares of stock were concentrated in the hands of the wealthy few and that in the absence of an

individual income tax, which did not come about until the Civil War, and in the absence of a corporate tax, which did not come about until 1909, the distribution of income through dividend payouts to the shareholders made sense. All excess distributions of profit would keep the price of a company's stock stable. Conversely, in today's financial world, capital appreciation is accepted as a substitute for dividend payments.

From 1815 to 1925, the stock markets of the United States could be likened to an emerging market with different owner types, industry concentrations, and capital and dividend policy structures than today's markets. Reviewing historical

financial data and its lack of quality prior to 1926 now makes it easier to understand why most market charts of today begin in 1926. Ibbotson has performed a great service by accumulating and refining stock market data from 1815 to 1925, and hopefully the investment community can continue to use this data to further our understanding of today's and tomorrow's stock markets.

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⁷ Stocks, Bonds, Bills and Inflation 2006 Yearbook, p. 196

