

One hundred twenty years after the birth of the Dow Jones Industrial Average, there's hardly a news story about the American stock market that doesn't mention "the Dow"—for its iconic presence in American financial markets is undeniable. Yet, over the course of its 120 years of existence, to what extent has the Dow reflected the nature of the U.S. economy at large?

We hear about the Dow Jones Industrial Average every day, but have you ever thought about its history? Did you know it comprises only 30 stocks? Is it still relevant? Is it still a good indicator to track major American industry? Is it a good benchmark for your portfolio? After all, notable companies like Amazon, Google, Facebook and many others have no presence in the Dow, and companies that have been so much a part of American culture like Woolworth's, Bethlehem Steel, Sears, and even AT&T are distant memories to Dow watchers. Take a look at the Dow in August 1982:

Exxon Corporation	Minnesota Mining & Manufacturing Company	F. W. Woolworth Company
Eastman Kodak Company	Merck & Co., Inc.	Westinghouse Electric Corporation
E.I. du Pont de Nemours & Company	International Paper Company	United Technologies Corporation
Bethlehem Steel Corporation	International Harvester Company	United States Steel Corporation
American Tobacco Company (B shares)	International Business Machines Corporation	Union Carbide Corporation
American Telephone and Telegraph Company	Inco Limited	Texaco Incorporated
American Express Company 1	Goodyear Tire and Rubber Company	Standard Oil Co. of California
American Can Company	General Motors Corporation	Sears Roebuck & Company
Aluminum Company of America	General Foods Corporation	The Procter & Gamble Company
Allied Chemical Corporation	General Electric Company	Owens-Illinois, Inc.

Johns-Manville was replaced by American Express.



JULY 2016 WHITE PAPERS

BACKGROUND

It was not until the spring of 1896 that Charles Dow had developed his ideas to the point where he completely removed the railroad issues from his general market average and created two separate Averages: the Industrials and the Railroads. Shortly thereafter, The Wall Street Journal reported an independent Railroad Average, as well as an Average composed entirely of industrial and natural resource concerns, which became known as the Dow Jones Industrial Average (DJIA). Although both Averages first appeared on May 26, 1896, the Industrials were not regularly reported in the WSJ until October 7 of that year. Their starting point that day was a mere 40.94—a long way from where the DJIA sits today.

Early on, the Industrials were a dynamic Average, changing composition on an almost monthly basis. Because the DJIA was supposed to represent the current business environment in the U.S., Charles Dow actively sought to include the key industries of his time: sugar, spirits, leather, cordage, tobacco, gas, lead, rubber, coal, iron, and electrical products. Therefore, the original Industrial Average boasted names like American Cotton Oil, American Sugar, Distilling & Cattle Feeding, Laclede Gas, National Lead, and U.S. Rubber.

This is a far cry from today's Index, which is dominated by retailing, oil, technology, pharmaceuticals, and entertainment companies, and includes such names as American Express, Walt Disney, Merck, Microsoft, and United Technologies. The grid below has the Dow's most up-to-date holdings.

3M Company	General Electric Company	Nike, Inc.		
American Express Company	The Goldman Sachs Group, Inc.	Pfizer Inc.		
Apple Inc. 1	The Home Depot, Inc.	The Procter & Gamble Company		
The Boeing Company	Intel Corporation	The Travelers Companies, Inc.		
Caterpillar Inc.	International Business Machines Corporation	UnitedHealth Group Incorporated		
Chevron Corporation	Johnson & Johnson	United Technologies Corporation		
Cisco Systems, Inc.	JPMorgan Chase & Co.	Verizon Communications Inc.		
The Coca-Cola Company	McDonald's Corporation	Visa Inc.		
E.I. du Pont de Nemours & Company	Merck & Co., Inc.	Wal-Mart Stores, Inc.		
Exxon Mobil Corporation	Microsoft Corporation	The Walt Disney Company		
Dropped from Average				
AT&T ↓				

The only company on the original list of Industrials that has endured to the present day is General Electric, although it has been removed from the Index twice (only to be reinstated later, obviously). The original Railroad Average was replaced by the more generalized Transportation Average after a number of trucking, airline and air-shipping concerns were added to it in 1970. These changes also included the first Dow stocks to come from the tech-heavy Nasdaq, not just from the New York Stock Exchange (NYSE).

The last major development in DJIA history was the 15-stock Dow Jones Utilities Average, which first appeared in 1929.

Despite public perception to the contrary, the Dow Averages have continued to change in recent years—and these alterations are far from accidental. A new component has been added, on average, every three years since the inception of the Average.



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WHO AND WHY

TThe editors of the Dow Jones Indices oversee any shifts in the composition of the Averages and see that periodic adjustments are made, both to ensure the Dow's continued reflection of the current business climate and to compensate for mergers and bankruptcies involving Dow stocks. This function has maintained Charles Dow's original commitment to ensure that the mix of companies on the Averages remains analogous to the broader market.

When choosing a company to represent a specific industry in the Dow, the following criteria are considered: Is the company a leader? How long has it been around? Does it treat its shareholders well? What is its reputation in the industry? Dow companies must be leaders in a particular industry or sector. The Dow has traditionally comprised corporate giants and massive companies whose shares have been publicly traded for decades.

Although companies like Coca-Cola (NYSE: KO) and McDonald's (NYSE: MCD) might appear outdated compared to the Amazons and Facebooks of the world, that Coke and McDonald's have been multi-billion-dollar companies for decades suggests an incredible staying power that their juvenile competition has yet to demonstrate. Though the presence of decades-old companies like Caterpillar (NYSE: CAT) on the Index may also make it appear antiquated, many investors forget that Caterpillar is a global company that helps to develop and modernize the world.

The grid below is a snapshot of the August 1976 Dow, for a bit of nostalgia, yet really not that long ago:

Allied Chemical Corporation	Exxon Corporation † (formerly Standard Oil Co. of New Jersey)	Owens-Illinois, Inc.
Aluminum Company of America	General Electric Company	The Procter & Gamble Company
American Can Company	General Foods Corporation	Sears Roebuck & Company
American Telephone and Telegraph Company	General Motors Corporation	Standard Oil Co. of California
American Tobacco Company (B shares)	Goodyear Tire and Rubber Company	Texaco Incorporated
Bethlehem Steel Corporation	Inco Limited † (formerly International Nickel Company, Ltd.)	Union Carbide Corporation
Chrysler Corporation	International Harvester Company	United States Steel Corporation
E.I. du Pont de Nemours & Company	International Paper Company	United Technologies Corporation (formerly United Aircraft Corporation)
Eastman Kodak Company	Johns-Manville Corporation	Westinghouse Electric Corporation
Esmark Corporation † (formerly Swift & Company)	Minnesota Mining & Manufacturing Company ↑	F. W. Woolworth Company
	Dropped from Average	
Anaconda Copper Mining Company ↓		

Anaconda Copper was replaced by Minnesota Mining & Manufacturing. International Nickel changed its name to Inco, Swift & Company changed its name to Esmark, Standard Oil (NJ) changed its name to Exxon Corporation, United Aircraft changed its name to United Technologies Corporation.

An example of the logic used to maintain the Dow's weighting is illustrated by the changes made in 1985 after Dow component General Foods was bought out by tobacco giant Philip Morris. The sudden addition of Philip Morris to the Average upset the industry weighting by doubling the number of tobacco companies (American Brands, formerly American Tobacco, was already there). As a result, the editors of the Index decided to drop American Brands entirely and add McDonald's to the Industrial Average to better represent the restaurant industry.





WHO AND WHY CONTINUED

Regarding bankruptcies, the only company that has ever fallen off of the DJIA due to financial difficulties is the John Manville Company, which was caught in a wave of litigation relating to its innovative fire-retardant product, asbestos. Chrysler's run-in with red ink—eventually resolved by a bailout from the U.S. government—was probably responsible for its deletion in the early 1980s, although the company never did, in fact, go bankrupt. The only other high-profile bankruptcy was Texaco in 1987, after its attempted acquisition of Getty Oil resulted in a major fine due to a breach of contract, but Texaco was not removed from the Dow until 1997. Even Exxon's Valdez disaster and Union Carbide's Bopahl tragedy were not enough to get them kicked off the Index.

Currently, 30 stocks are listed in the Dow Jones Industrial Average, 20 in the Dow Jones Transportation Average, and 15 in the Dow Jones Utilities Average.

CONCLUSION

Sometimes our white papers are heavy and cumbersome with information on U.S. and world geopolitical and economic driver theories. Others we write with more levity, like our Presidential Election Cycle paper a few months ago. Our white papers on the Dow fall somewhere in-between. It's surprising, however, that many people talk about the DJIA (and no wonder: it gets all the headlines) but don't know it lists only 30 stocks, are unfamiliar with the Dow's history, or are even aware of its Transportation and Utilities Indexes.

To those ends, this white paper was meant to be just as nostalgic as informative. Children today will never flip through the Sears Catalog, sit at a Woolworth's counter, or wait a week for pictures to be developed from Kodak film onto Kodak paper—that's a lost generation. Thankfully, I remember those days; they show me, as an advisor, that nothing lasts forever and innovation will always change and shape our country. So its crucial to look far down the line for companies that will appear on our radar screens as well as those that will fade away.

Is the Dow Jones Industrial Average still a great indicator for measuring your investment success? Probably not. It doesn't include many of today's major technology players that drive the economy and change the landscape in which we live. Plus, it's only 30 stocks—hardly a broad representation of the American landscape.

At WT Wealth Management we use the Standard & Poor 500 as our basic measurement benchmark. With its representation of America's largest 500 companies, it covers nine different sectors, from Industrials to Utilities to HealthCare to Consumer Discretionary. Which means the S&P 500 represents the entire universe of the American economy much more fairly and broadly than the DJIA does, in part because the S&P 500 includes the major drivers of today's economy: Wells Fargo, Amazon, Facebook, Google, FedEx, UPS, MasterCard, etc., etc.

We'll leave you with a look at 1956 (oh, has the world changed):





CONCLUSION CONTINUED

July 3, 1956

Allied Chemical and Dye Corporation	General Electric Company	The Procter & Gamble Company
American Can Company	General Foods Corporation	Sears Roebuck & Company
American Smelting & Refining Company	General Motors Corporation	Standard Oil Co. of California
American Telephone and Telegraph Company	Goodyear Tire and Rubber Company	Standard Oil Co. of New Jersey
American Tobacco Company (B shares)	International Harvester Company	The Texas Company
Bethlehem Steel Corporation	International Nickel Company, Ltd.	Union Carbide Corporation
Chrysler Corporation	International Paper Company ↑	United Aircraft Corporation
Corn Products Refining Company	Johns-Manville Corporation	United States Steel Corporation
E.I. du Pont de Nemours & Company	National Distillers Products Corporation	Westinghouse Electric Corporation
Eastman Kodak Company	National Steel Corporation	F. W. Woolworth Company
	Dropped from Average	
Loew's Theatres Incorporated ↓		

Loew's was replaced by International Paper.

DISCLOSURE

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DISCLOSURE CONTINUED

Diversification and asset allocation may not protect against market risk or a loss in your investment.

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