Herald-Journal

Noel Swain: Why is the Dow Jones Industrial Average important?

Published: Wednesday April 17th, 2019

"What is the Dow Jones industrial average, and why is it important to me?"

Phil was sitting in my office recently and posed that question. My answer was somewhat shallow. "Well," I said, "it is an index of the stock of 30 U.S. corporations chosen by the Dow Jones company to represent the overall movement of the largest companies in America."

"Do the companies in the Dow change?" asked Phil. I told him yes, but I didn't know much past that. So I dug into it a little and came upon some interesting facts.

The Dow Jones industrial average was first calculated on May 26, 1896. It consisted of 12 companies, none of which remain in the index today. GE, the last of the original 12, was removed on June 26, 2018.

The list was expanded to 30 companies during the 1920s. The DJIA was created by Wall Street Journal Editor Charles Dow. It was named after Dow and one of his business associates, statistician Edward Jones. Originally started to measure the movement of the stocks of heavy industry, many of the current companies have no ties to that sector at all.

When it was first published it reached a high of 78.38 before falling to 28.48, its all-time low, during the Panic of 1896. If that were to happen today, it would be like the Dow falling from about 25,000 to just over 9,000. During the late 1920s, the Dow soared to 381.17, before falling all the way to 41.22 by July of 1932. It would be 1954 before the Dow reached its 1920s high again.

In looking at the companies that made up the Dow of 30 years ago, only 12 are still in it today. Some of the ones that have been replaced are ALCOA, Bethlehem Steel, General Motors, Sears, Westinghouse and Woolworth. Many of the companies in it today, like Apple, Microsoft, Nike and Verizon, were infant companies 30 years ago.

The DJIA is sensitive to economic and political events in this country, as well as around the world.

In 2007, the Dow reached a high of 14,165 before falling all the way to 6,547 in March 2009, or 53.8%. That was the worst stock market crash since the 1929-32 decline of almost 90%.

The Real Estate bubble, along with very loose lending practices by Fannie Mae and Freddie Mac, caused the market to overheat and run the stock market way past its intrinsic value. I can't help but notice that some of the events that caused the crash more than 10 years ago are happening again today. That does not mean I'm predicting a 2008-style crash anytime soon. It does mean that we should be ever-vigilant, because nobody rings a bell when a crash starts.

So yes, Phil, the Dow Jones industrial average is important to you because it can help you keep track of the movement of the stock market and thus the economy. And anyone who invests his or her money should keep up with how it's doing.