

Research Paper

Comparing the share market crash in the 1930's with current crisis

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There has been much discussion about whether the current financial crisis is going to result in another Great Depression. Prolonged global recession is certainly a very likely scenario. We think it's unlikely that it will be as bad this time given the extent of global, co-ordinated, fiscal stimulus. However, it is informative to look at what happened to share market returns in the US and Australia at that time.

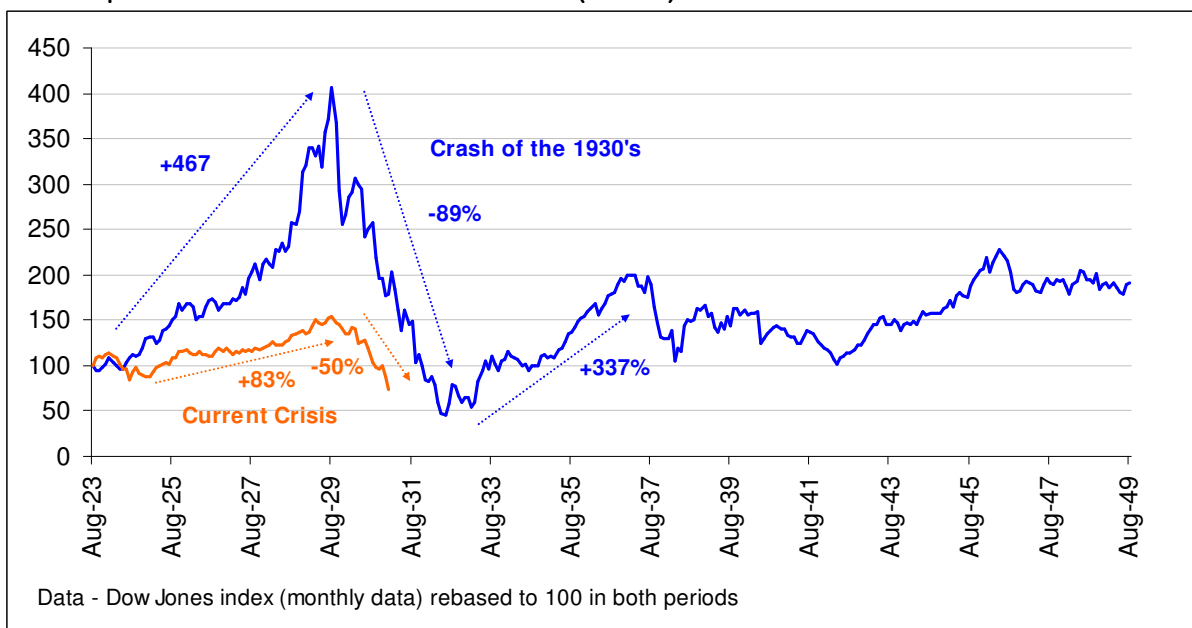
The US comparison

In the US, there was a long bull run in the sharemarket prior to the crash that began in 1929. In the chart below, we show what happened if you invested \$100 into the Dow Jones Industrial Index at the beginning of that boom (the blue line). It shows that \$100 grew to \$407, delivering a 467% return. The sharemarket then crashed and investors lost 89% of their investment value over the next 3 years. Interestingly, once the market bottomed in 1931, it rose by 337% over the next 5 years.

As a comparison, we have also shown on the same chart the value of \$100 invested in the Dow Jones over the same period before the current share market crash (orange line). As shown in the chart, the Dow Jones rose by 83% in the recent bull market (2003 – 2007) and has fallen 50% over the past 16 months.

As you can see, the two markets were very different. The more recent bull run in the share market was far more subdued than the one prior to the 1929 crash. Perhaps the crash will also be less?

US Comparison – The Dow Jones Index then (1930's) and now



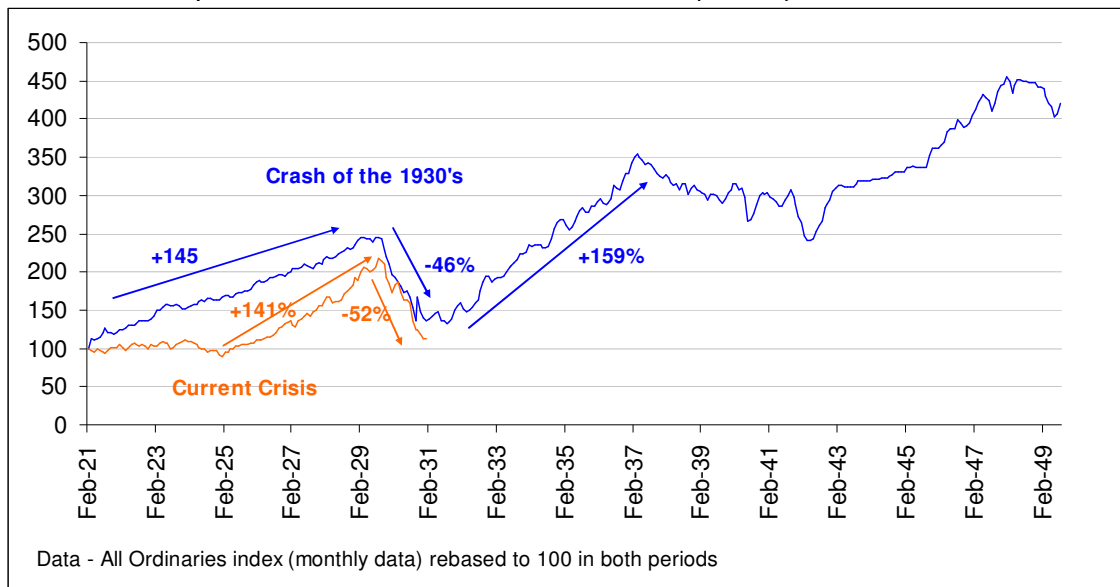
The Australian comparison

In Australia, there was also a long bull run in the sharemarket prior to the crash that began in 1929. In the chart below, we show what happened if you invested \$100 into the Australian All Ordinaries Index at the beginning of that boom (the blue line). It shows that \$100 grew to \$245, delivering a 145% return. The sharemarket then crashed and investors lost 46% of their investment value over the next 2 years. Again, once the market bottomed, it rose again strongly - by 159% over the next 6 years.

Again as a comparison, we have shown on the same chart the value of \$100 invested in the Australian All Ordinaries Index over the same period of time before the current share market crash (orange line). As shown in the chart, the Australian All Ordinaries Index rose by 141% in the recent bull market (2003 – 2007) and has fallen 52% over the past 16 months.

In this case, the return patterns are more similar. Are we soon to see a big rise in the sharemarket?

Australian Comparison – The All Ordinaries Index then (1930's) and now



Both charts clearly show a potential opportunity emerging, but no crash is ever the same, so caution is wise.

Also note that both charts show the price returns on the stock markets. They do not include the effect of dividends. These can substantially increase long term returns.