Key Questions

What can be Learned from the 1929 Market Crash?

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There are important lessons to be learned from the 1929 Crash for today's investors.

The market had a milestone event last week, but it wasn't one to celebrate: It marked the 90th anniversary of the 1929 Stock Market Crash and the opening round of a years-long financial slump and the Great Depression. On October 28, 1929, now known as Black Monday, the Dow Jones Industrial Average plunged nearly 13%, only to fall another 12% the following day, Black Tuesday. From its peak in September 1929 to its trough in June 1932, the Dow sank by a breathtaking 87%.

With the S&P 500 Index recently hitting all-time highs, it's easy to understand why most of us overlooked the anniversary. And we don't see conditions unfolding in ways that would lead to the global trauma that began nine decades ago. Still, there are important lessons to be learned from that difficult time, ones from which investors can benefit today.

After reaching its high of 362 in September 1929, the Dow plummeted, bottoming out at 47 in June 1932. (We use the Dow rather than the S&P 500 since the Dow was the only broad market indicator in use before, during, and for decades after the 1929 Crash.)To put this decline into even sharper perspective, the market in 1932 was less than half of what it had been in October 1916, just prior to America's entry into World War I. It w ould not be until November 1954 – a quarter of a century after the Crash began — before the Dow breached its September 1929 high.

Market history during the Crash makes for grim reading, the kind that sends chills down an investor's spine. However, a close inspection of the data during that time also reveals some important facts that have significant — and positive — implications for long-term investors.

Make no mistake, an investor literally could not have picked a worse entry point for buying US stocks than September 1929. Twenty-five years is an awfully long time for someone to just recover their losses. But what about a long-term investor who had been steadily purchasing equities prior to the Crash?

For example, if an investor had bought one unit of the Dow (or a constant fraction of the index) at the start of every month from January 1920 to September 1929, they would have had a cost basis of 146 — 60% below the index's high of 362. If that same investor had stopped buying at the time of the Crash, they would have recouped all their capital by January 1936, a span of a little over six years. And it would have taken less time if you include any dividends received. Even an investor who began buying stocks when the Dow began its breakout in 1925 and bought every month until the Crash would have had a cost basis of 196. If they had stopped buying at the time of the Crash, they would have been whole by January 1946.

The message is clear: Dollar-cost averaging shortened the time needed to recover losses from the Crash and its aftermath from 25 years to between 6 to 17 years.

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But what if the investor had continued dollar-cost averaging during the Great Depression? Would that have hurt their investment performance?

In fact, the case for maintaining a disciplined investing strategy is even more compelling: Purchasing one unit of the Dow at the start of every month from 1925 through 1934 would have resulted in a cost basis of 162 at the end of that 10-year period. As a result, the investor would have been in the black by mid-1936, a mere 18 months later.

We are firm believers in having a long-term investing strategy and sticking to it. And as the evidence from the ’29 Crash shows, it’s a powerful approach that pays off for patient investors.

For more information, please contact your Key Private Bank Advisor.

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