

Dow Jones Industrial AverageSM

The Dow Jones Industrial AverageSM, also referred to as The Dow[®] or the industrial average, is one of the best-known icons of American culture and among stock-market observers around the world. It is as much a staple of news reports as traffic and weather, and its actions are reported whenever a major world event occurs. Whether The Dow[®] rises or falls, the eyes of the world are always upon it.

History of The Dow[®]

Created in 1896 by Charles Dow, one of the founders of *The Wall Street Journal*, the industrial average was not the first market index. That distinction belongs to an 1884 predecessor of what is today known as the Dow Jones Transportation AverageSM, also the creation of Mr. Dow. This stock index was originally named the Dow Jones Railroad Average. In the late 19th century railroading was the most important industry in the United States and the Transportation Average was a gauge of not only the market, but the broader economy as well.

As industrial stocks comprised a small but growing part of the market, Mr. Dow felt compelled to create an index for this segment as well. He used the two indexes to confirm broad market trends, reasoning that because industrial companies produced goods and the railroads delivered them, a bull market was sustainable only if both sectors were participating.

The new Dow Jones Industrial Average originally had 12 stocks, including a leather maker, a steel provider and a sugar producer. First published May 26, 1896, and regularly featured in the *Journal* as of October of that year, The Dow[®] waited more than 25 years to achieve prominence outside the narrow canyon of Wall Street.

In 1896, investing in the stock market was considered a highly speculative activity, particularly with regards to industrial stocks. Railroad stocks were tolerable as they were the “blue-chips” of their day, but bonds were the truly prudent investment.

By the 1920s, popular attitudes had changed. Average citizens began investing in stocks, driving the industrial average from the 100 range in 1924 up to nearly 400 before the Crash of 1929. Ironically, it was the the market’s fall that brought The Dow’s reputation to the attention of Main Street USA as the index lost nearly 30% of its value over the course of two days. Before that, investors had been more focused on their individual stocks. But after the crash, there was greater interest in general market conditions.

Though it had come close in 1929, The Dow[®] did not actually rise above 400 points until the end of 1954. The economic upheaval of the 1930s and the international disruption of World War II kept it fluctuating below that mark for 25 years.



"A person watching the tide coming in, and who wishes to know the spot which marks the high tide, sets a stick in the sand at the points reached by the incoming waves until the stick reaches a position to where the waves do not come up to it, and finally recede enough to show that the tide has turned. This method holds good in watching and determining the

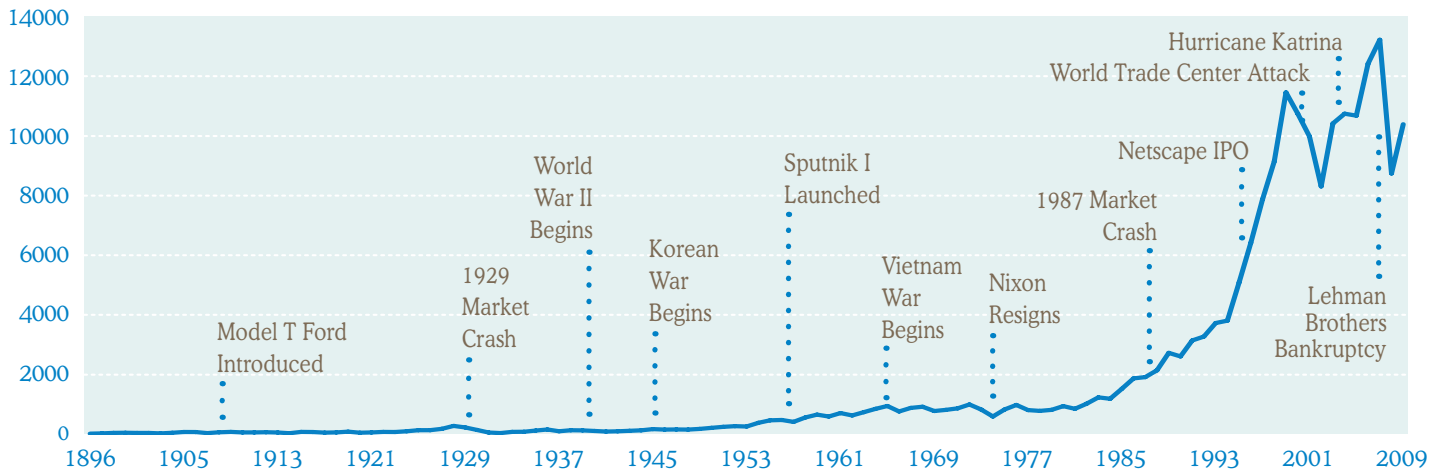
flood tide of the stock market. The average of [stock prices] is the peg which marks the height of the waves. The price-waves, like those of the sea, do not recede all at once from the top. The force which moves them checks the inflow gradually, and time elapses before it can be told with certainty whether high tide has been seen or not."

— Charles Dow, creator of the Dow Jones Industrial AverageSM, in the January 31, 1901, edition of *The Wall Street Journal*

The 1950s were one of The Dow’s best decades in history, climbing almost 240% to close 1959 at 679.36. However, not until the high-flying 1980s and 1990s would there again be such substantial gains in the stock market. Those two decades represent an era of unparalleled prosperity, despite the crash in 1987 and a brief bear market kicked off by the Gulf War in the early 1990s. The Dow[®] rose 228.25% during the 1980s to close at 2753.20 at the end of 1989 and 317.59% during the 1990s, ending 1999 and the century at 11497.12.

In the last 10 years of the 20th century, the Dow Jones Industrial AverageSM burst through several 1000-point milestones, crossing the 10000 barrier for the first time on March 29, 1999. The excitement generated by this event was felt around the world. Though the number itself had no special significance, it served to highlight the spectacular performance of the index and—by extension—the U.S. economy.

The Dow Jones Industrial AverageSM Throughout History (December 1896 – December 2009)



The Dow[®] peaked at 11722.98 on January 14, 2000, before sliding into a bear market brought on by the same “dot coms” that had helped its dizzying climb. After weathering the September 11, 2001, terrorist attacks and hitting bottom in October 2002, the industrial average once again crossed 10000 in December 2003.

The Dow Jones Industrial AverageSM proved its resilience by making a comeback amid the Iraq War and a volatile energy market. In the final stretch of 2006, The Dow Jones Industrial AverageSM gained momentum and repeatedly pummeled record after record. The succession of events began on October 19, 2006, when The Dow[®] closed at 12011.73; simultaneously reaching a new unprecedented high and breaking the 12000 mark on the 19th anniversary of “Black Monday” (the 1987 crash). On November 17, the industrial average soared to 12342.

The Dow[®] is not called “the Market’s Measure” for nothing. Just as equity markets worldwide climbed and peaked in 2007, so did The Dow[®], hitting its peak on October 9, when it closed at 14164.53. That marked the end of the current (and longest ever) U.S. bull market.

With news of a rapid and harrowing meltdown in the credit markets, the DJIA[®] started to fall throughout the rest of 2007 and into 2008. As the loss of faith in bond markets spread to equities—and then to Wall Street institutions themselves—the markets continued to tumble, and The Dow[®] spiraled downward—to 11893.69 on March 7, 2008.

On September 15, 2008, the Dow Jones Industrial AverageSM fell 504.48 to 10917.51 on news that Lehman Brothers had failed and that Merrill Lynch would be purchased by Bank of America. September 29 marked the largest drop in the DJIA’s history: 777.68, closing at 10365.45. The index would have several three-digit falls in October, including a 733.08 drop (the second-largest in history) on the October 15 to close at 8577.91.

The Dow[®] rallied several times in the ending months of 2008. Its second largest gain ever was on October 28, up 889.35, to close at 9069.12. However, bear sessions after Election Day brought it below 9000 in November for the first time since June 3, 2003; and below 8000 (on November 19) for the first time since October 14, 2002.

December 2008 saw The Dow[®] steady on news of a massive government infrastructure program in the United States proposed by the incoming Obama administration, the shake-out of the markets (including free-falling oil prices), and the idea that the bear market might have reached a bottom. It rose to 8924.14 on December 16, as wary investors sought stability and a few brave souls went bargain hunting. It finished the year at 8776.39, down almost 34% for the year.

The DJIA[®] started the new year of 2009 on the upswing, perhaps cheered by the thought that markets might improve with the new administration. The Dow[®] closed at 9015.10 on January 6; but that was as high as it would go in the new quarter. Stocks were soon to be driven down by persistent bad news in retail, manufacturing and the hemorrhaging financial sector. With no apparent end in sight to the recession and government bailout efforts having little effect on the general economy, The Dow[®] would sink in February and go into a serious dive early the next month, closing under 7000 on March 2 for the first time since May 1, 1997.

After a hesitant rally later in March, The Dow[®] began a tentative but sustained rise in the second quarter 2009, cracking 8000 on April 3. By May 31, The Dow[®] was able to settle in over 8500.

The DJIA[®] advanced over 200 points on June 1 on news that the index was changing components (out with General Motors and Citigroup; in with Travelers and Cisco Systems). After a subsequent dip, the summer marked the beginnings of a months-long rally that would see The Dow[®] close above 10k once more (10015.86 on October 14). The DJIA[®] closed the year at 10428.05, making 2009, remarkably, one of its best years ever.

Calculating The Dow®

The Dow® is calculated using very nearly the same formula now as at its inception: Simply add the prices of the component stocks on their primary exchanges and divide this sum by the current divisor.

The divisor, however, is not the number of stocks, as it originally was. In 1916, the editors of *The Wall Street Journal* raised the number of components in The Dow® from 12 to 20. Then, in 1928, they increased the number of components again—this time to 30—and also introduced the adjusted divisor.

The adjusted divisor is designed to keep the index consistent through events such as component changes, stock splits, large dividend distributions, mergers and acquisitions, and spin-offs. It ensures that the index remains at the same level immediately after one of these events as it was before. For example, in a 2-for-1 stock split the number of existing shares is doubled and the price is halved. Since the index calculation is based on price, not adjusting the divisor would cause The Dow® to plunge in value as one of its components' stock prices fell by 50%, even though there was no change in the value of an investor's holding in the stock. Instead of one share worth \$10, for example, an investor would have two worth \$5 apiece.

Over the years, there have been so many changes to the divisor, most of them downward adjustments, that it is now a fraction.

The formula for calculating a divisor change is as follows:

$$D_{t+1} = D_t * \sum C_t^a / \sum C_t$$

Where:

- D_{t+1} Divisor to be effective on trading session t+1
- D_t Divisor on trading session t
- C_t^a Components' adjusted closing prices for stock dividends, splits, spin-offs and other applicable corporate actions on trading session t
- C_t Components' closing prices on trading session t

Component Selection

At any given time, The Dow's 30 components usually account for 25% to 30% of the total market value of all U.S. stocks. The Dow® doesn't literally "represent" the entire U.S. market. Rather, it is a blue-chip index representing the leading companies in the industries driving the U.S. stock market. As a result, its performance is highly correlated with that of indexes containing hundreds or thousands of stocks.

Component changes are rare and usually occur only when an existing company is going through a major change, such as a shift in its main line of business, acquisition by another company or bankruptcy. There is no review schedule.

Changes are made as needed at the discretion of the managing editor of *The Wall Street Journal*. While the responsibility rests with this individual, other senior editors may be consulted.

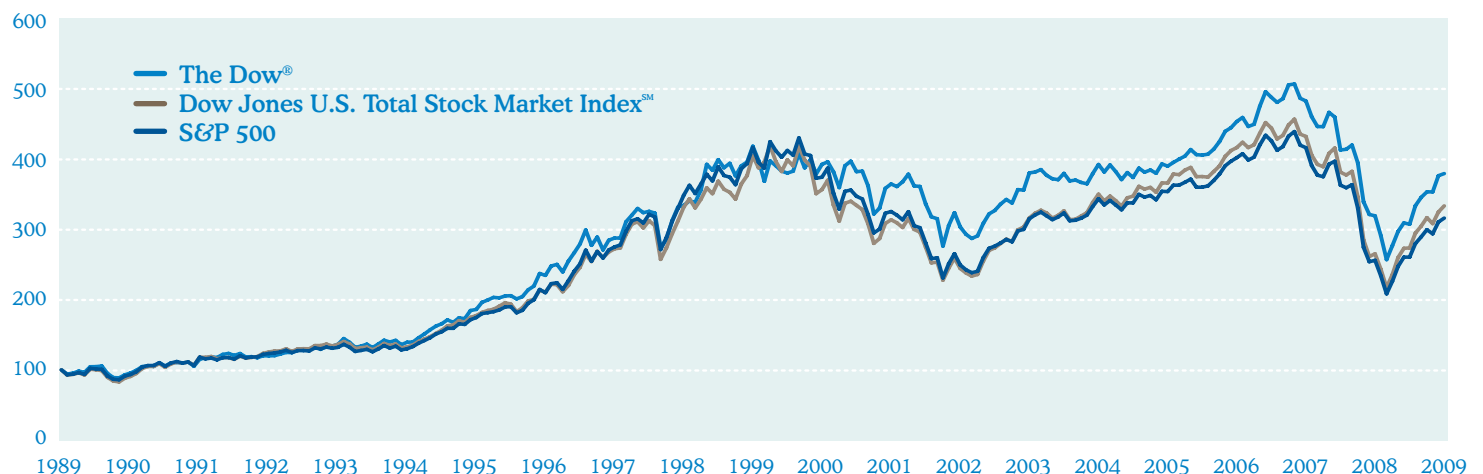
Selected components are always U.S. companies, are leaders in their industries, are widely held by investors and have long records of sustained growth.

Relevance

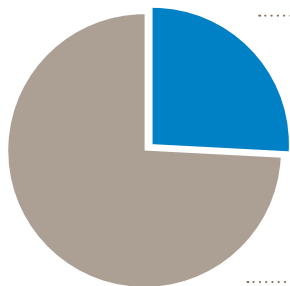
The Dow® is an example of the elegance of simplicity. It tracks closely with other major market indexes with more complex methodologies and yet easily can be calculated with paper and pencil. Moreover, it is the only major market index with more than 100 years of history.

Today The Dow® is quoted worldwide on a daily basis in news broadcasts, on Web sites, in newspapers and journals, and in conversation. It also has been licensed to financial institutions around the world as the basis of investment products.

How The Dow® Compares (December 1989 – December 2009)



The Dow® and the Total Market



As of December 31, 2009, The Dow® represented 28% of the float-adjusted market capitalization of the Dow Jones U.S. Total Stock Market IndexSM, which provides near-complete coverage of the U.S. stock market.

Did You Know?

- General Electric is the only stock in The Dow® today that was also included in the original 12. It was removed twice in the early years of the 20th century but both times was returned to the industrial average in subsequent component changes.
- For more than four months in the second half of 1914, The Dow® was not published. The New York Stock Exchange was closed because of World War I. It was feared that the instability caused by the war would cause the market to plummet.
- Throughout most of its history, the industrial average's components have been chosen from among the stocks listed on the New York Stock Exchange, though there was never any rule in the index's methodology that said an NYSE listing was a requirement for eligibility. It was not until November 1, 1999, that stocks from the Nasdaq Stock Market (Intel Corp. and Microsoft Corp.) were added to The Dow®.
- No component changes were made to the Dow Jones Industrial AverageSM during the 1940s and the 1960s.
- The Dow's greatest one-day percentage gain took place March 15, 1933, well into the Depression. The index rose 15.34%, or 8.26 points, on that day. Its greatest percentage loss was on October 19, 1987 — otherwise known as "Black Monday" — when the industrial average fell 22.61%, or 508.00 points.



The Dow® on May 26, 1896

American Cotton Oil	Laclede Gas
American Sugar	National Lead
American Tobacco	North American Utility
Chicago Gas	Tennessee Coal & Iron
Distilling & Cattle Feeding	U.S. Leather (preferred)
General Electric	U.S. Rubber



The Dow® Today

3M	IBM
Alcoa	Intel
American Express	Johnson & Johnson
AT&T	JPMorgan Chase
Bank of America	Kraft Foods
Boeing	McDonald's
Caterpillar	Merck
Chevron	Microsoft
Cisco Systems	Pfizer
Coca-Cola	Procter & Gamble
DuPont	The Travelers Companies
Exxon Mobil	United Technologies
General Electric	Verizon
Hewlett-Packard	Wal-Mart Stores
Home Depot	Walt Disney

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