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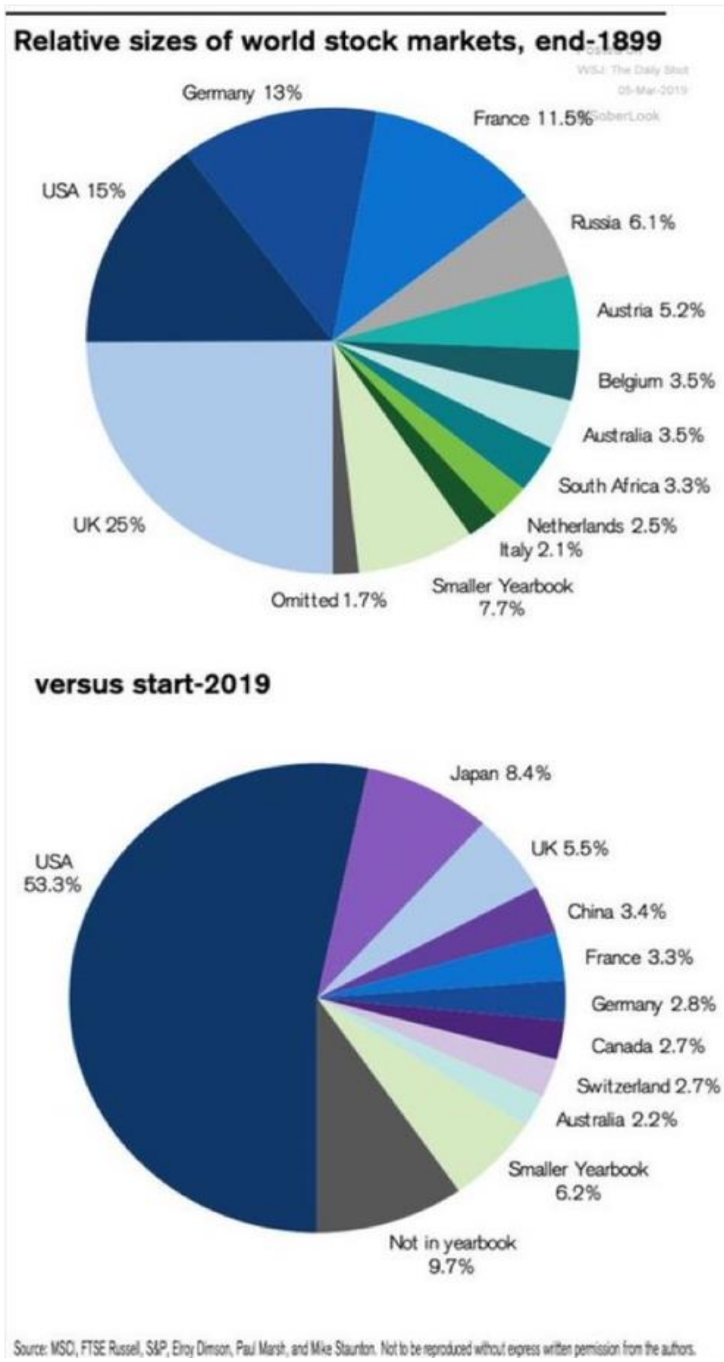
THE MARKETS OF 1899 AND 2019



With April comes spring, though that's yet to be reflected in the temperatures here in Toronto. Still, baseball is back, and temperatures will soon rise, so I'm feeling optimistic after a long winter. I came across a chart contrasting the size of equity markets in 2019 versus 1899 that I think is worthy of discussing, I must admit to having a weakness for these types of comparisons because they simultaneously satisfy my curiosity and often offer valuable insights for investing.

The economic world of 1899 was still very Eurocentric, with UK equities representing fully 25% of world market capitalization. According to the chart above, European nations accounted for 62.8% of total capitalization in 1899. China and Japan are notable for their complete absence from the 1899 calculation. Canada was also absent, while Australia accounted for 3.5%. The great emerging market of the 19thcentury, the United States, stood at a respectable 15%. Countries that are now considered to represent the "West" comprised 81.3% of the 1899 total.

It will be no surprise to readers that things have changed considerably in the intervening 120 years. The United States now dominates global equity capitalization, making up 53.3% of the total. The influence of European nations has withered, representing a mere 14.3% in 2019. Japan (8.4%) and China (3.4%) appear on the 2019 chart, as does Canada by surpassing the market size of its Commonwealth cousin Australia.

The dominance of Europe in 1899 is, in part, attributable to the fact that its colonial empires were still largely intact and making significant economic contributions. However, other factors also played important roles, and these would later produce the economic landscape of today.

The first factor was the power of ideas. The industrial revolution began in early 19thcentury Britain and quickly spread to the Continent. The United States also embraced the industrial revolution, but its role was much like that of China today. The United States was then a source of cheap labour for Europeans, with late 19thNew York being a centre for inexpensive garment making. It's interesting to reflect on those days given the current trade tensions between the United States and China. Technology developed rapidly in the 19thcentury to spur the industrial revolution. Also important was the concept of capitalism and an environment that allowed individuals to profit from their efforts, which accounts for the growth of capital markets and economies in the 19thcentury. The emergence of the rule of law allowed business dealings to be done with greater confidence. These concepts were first embraced by the countries that dominated the world economy of 1899.

A second powerful influence on the charts above can be found in the competitive landscape. Europe and the United States profited from the adoption of the industrial revolution and the embracing of capitalism, as discussed above, but they also benefited from the slowness of other nations to follow suit. Japan essentially isolated itself from the rest of the world until the mid 19thcentury. The fragmented politics of China and India hindered the economic development of those nations until recently.

The global competitive landscape is now much more balanced. Technology has certainly produced a more level playing field. As important has been the embracing of the pursuit of profit, even from nations such as China, which has produced a quasi-capitalist one party state. India also, in its own way, is consciously pursuing economic growth.

A forecast of global market capitalization in another 120 years would seem an obvious exercise. The United States would still be the largest, though relatively smaller, market. China would be much larger and in second place, and India would become a substantial presence. Europe would continue to shrink in influence.

However, things are seldom so straightforward. It is almost guaranteed that there will be surprises when this chart is drawn in 2139. Those surprises will probably come from political developments. Factors such as the political environment and the rule of law will undoubtedly play a large role in determining the economic future of nations. Adverse political developments, for instance, are the biggest risk to the continued growth of nations such as China and India.

The chart above demonstrates the power of macro factors on nations, their economies and markets. The past 120 years has produced a lot of change and, as we are all aware, the pace of change is increasing. The Global Investment Letter attempts to place today's markets in geopolitical and historical context. It is an investment style that continues to produce gratifying results.

I hope you found the chart as thought provoking as I did.

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