The Toronto Stock Market: A 30-Year Flashback

While day-to-day market gyrations have recently captured everyone's attention, lost in the noise of price movements is how markets change over time. In this edition of Market Perspectives, we look at the constitution of the Toronto Stock Market Index in September 1981, comparing it to its constitution today, at the end of September 2011. The changes are interesting. Even the name of the Index itself has changed. Where today we have the S&P/TSX Composite, reflecting the TSX's adoption of US index standards, in 1981 it was known as the TSE 300.

Consider the following table of comparative economic indicators. Over the 30-year period from September 1981–September 2011, the TSX increased six-fold as inflation and interest rates fell dramatically. While the rate of inflation fell, commodity prices generally rose, reflecting a variety of supply/demand and general pricing constraints.

	TSX Level	CPI	Cda Bond Yield	Oil	Gold
September 1981	1,883	12.6%	17.7%	$36	$430
September 2011	11,624	3.2%	2.7%	$86	$1,620

Source: Bloomberg, Bank of Canada, CIBC World Markets, US FRED, USAGold.com.

Sector Weights	Sep 1981	Sep 2011
Oil & Gas	22%	20%
Metals/Minerals	14%	6%
Gold	3%	16%
Financials	13%	27%
Industrial/Forest	12%	4%
Consumer/Merchds/Media	12%	7%
Pipeline/Utility	12%	12%
Transportation	6%	3%
Real Estate/Other	5%	5%

Source: Bloomberg and TSX

Clearly, the Canadian stock market itself has changed dramatically as well.

The biggest changes? First, and consistent with the experience all around the globe, is the ascendency of the Financial Services sector. Financial stocks were 13% of the TSE in 1981; today, they are 30%. Why such growth? We believe lower interest rates and baby boomer borrowing had much to do with it. Whether such strength can continue in light of the global financial upheaval witnessed since 2007 presents a huge question mark today.

The next biggest increase is Golds. While bullion prices have ratcheted up smartly over the past 4 years, Canada has also become a global mining centre. Barrick Gold, through acquisitions, is the leading global player in the Gold sector.

Where the Gold sector gained, the Base Metals sector lost, primarily as a result of the takeovers of such heavyweight names as Alcan, Inco, Falconbridge and Noranda. Only time will tell how the loss of such Canadian leaders will influence the domestic economy going forward.

What is also interesting is the gutting of the traditional Industrial and Forest Products sectors. The Forest Products sector now represents 0.1% of the S&P/TSX, compared to a 2% weight in the TSE in 1981. The Steel industry has fallen from 3% to 0.3%. The Forest sector has seen a steady erosion of its status as a leading Canadian industry; the Steel sector has been restructured, with the remnants now owned by larger international companies. On the positive side, the rise of global fertilizer stocks, Potash and Agrium has been a plus.

In the Consumer sector, Canada lost its flagship brands, Seagrams, Molson, Labatts; companies with centuries-old heritage. Again, foreign ownership has replaced domestic.

Canada has always been an Oil and Gas mainstay and that hasn't changed over the years. Our Pipeline and Utility sector weights have remained stable over the decades.

What is interesting is how foreign ownership (Canadian companies owning foreign financial and gold companies, foreign companies owning Canadian metal mining, industrial and consumer companies) has skewed the Canadian benchmark index. At Leon Frazer, we have never been index-driven. When we consider diversification, it is in the context of exposure to a single industry, not relative to a benchmark that changes over time. Though weights may adjust in an index, we see no reason to change our clients' ownership of dividend-growing companies on the basis of an arbitrary index adjustment. ●