

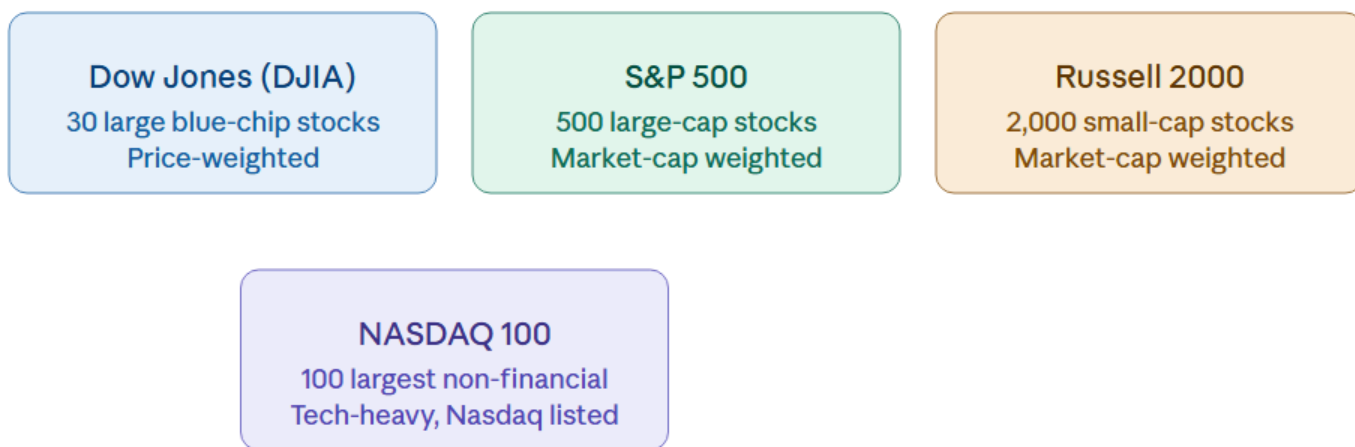
# Personal Finance #5

## What do Stock Indices Mean and Do?

When you invest, the natural question is: "Am I doing well?" But "doing well" doesn't mean much in isolation. If your portfolio grew 5% last year, is that good? It depends entirely on what the broader market did. If everything went up 20%, you actually underperformed significantly. If everything fell 10%, you were a star.

That's why investors use **benchmarks** — standardized indices that track groups of securities and serve as a yardstick for performance. Rather than asking "did I make money?", you ask "did I beat the index?" Here's a visual overview, and then we'll break each one down.

### U.S. INDICES



Comparison	Dow	S&P 500	Russell 2000	NASDAQ 100
# of stocks	30	500	2,000	100
Company size	Large (mega)	Large-cap	Small-cap	Large (tech)
Weighting	Price	Market cap	Market cap	Modified mkt cap
Best measure	Industrial economy	Broad U.S. market	Small business health	Tech sector

### GLOBAL EQUIVALENTS



Now let's walk through each one:

**Dow Jones Industrial Average (DJIA)** — The oldest and most famous, dating back to 1896. It tracks just 30 large, well-established American companies — think Apple, Boeing, Goldman Sachs. What makes it unusual is that it's *price-weighted*, meaning a higher share price gives a stock more influence over the index, regardless of how big the company is. That's a quirk that makes it less representative of the actual market, but it's still widely

quoted as a quick gut-check on how "the market" is doing. Think of it as a reading on the health of America's biggest, most iconic businesses. This is not a great benchmark for the overall market.

**S&P 500** — Most professional **investors consider this the true benchmark** for the U.S. market. It tracks 500 large companies across all sectors and is *market-cap weighted*, meaning bigger companies have more influence. If the S&P 500 is up 10% and your portfolio is up 7%, you underperformed. It's broad enough to be a genuine snapshot of the large-cap U.S. economy.

**Russell 2000** — While the Dow and S&P focus on big companies, the Russell 2000 tracks 2,000 smaller companies. This matters because small-cap stocks behave very differently — they tend to be more volatile, more sensitive to the domestic economy, and often lead market recoveries (or declines) before the big players do. If you own small-cap funds, this is your benchmark.

**NASDAQ 100** — This tracks the 100 largest non-financial companies listed on the Nasdaq exchange. Because the Nasdaq has historically attracted tech companies, the NASDAQ 100 is heavily weighted toward names like Apple, Microsoft, Nvidia, Amazon, and Meta. When "tech is up," this index usually moves more than the others.

Each year, stocks can be added to, or subtracted from, these indices based upon decisions by the people that oversee these indices. So if you compare this year's DJIA index to one from 10 years ago, **there will be a number of companies that are new, and a number that are no longer in the index - because the index can only have 30 companies at any one time.**

**The rest of the world has the same idea.** Every major economy has developed its own version of these benchmarks:

- The **FTSE 100** (the "Footsie") tracks the 100 largest companies on the London Stock Exchange — it's the UK's equivalent of the S&P 500.
- The **Nikkei 225** does the same for Japan, tracking 225 blue-chip companies on the Tokyo Stock Exchange.
- Germany's **DAX** covers the 40 largest companies on the Frankfurt exchange.
- The **Hang Seng** covers Hong Kong, while the **Shanghai Composite (SSE)** is the main gauge for mainland China's market.

The practical takeaway: before you can judge whether your investments are doing well, you need to decide *which benchmark is the right comparison*. A tech-focused portfolio should be measured against the NASDAQ 100, not the Dow. A small-cap fund against the Russell 2000. Using the wrong benchmark is like judging a marathon runner by how fast they swim.

