Stock market development and performance in the Middle East, 1870-1913

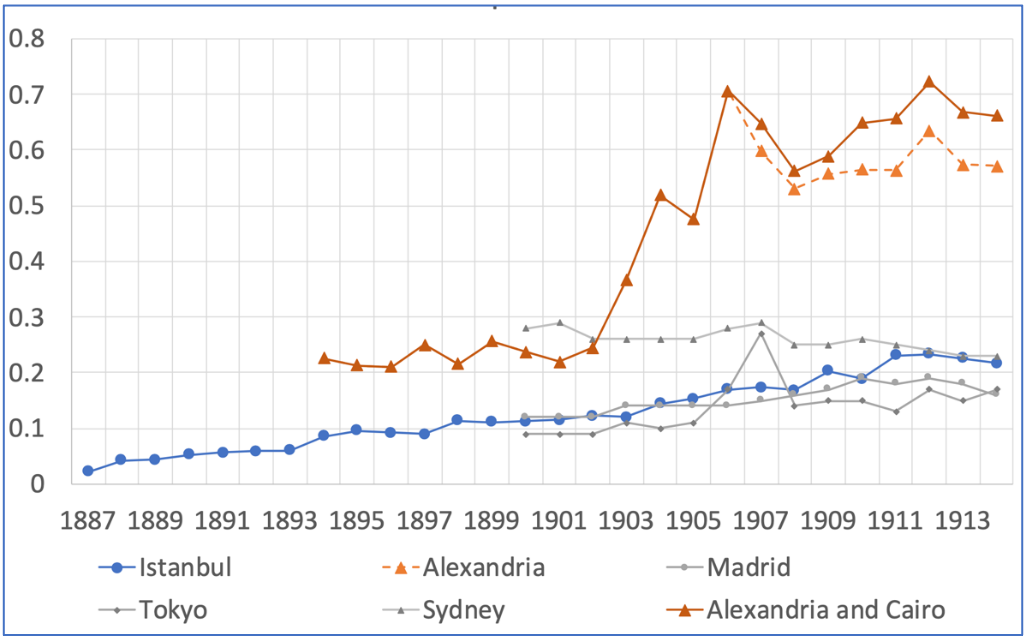
Ali Coşkun Tunçer (UCL)
a.tuncer@ucl.ac.uk

The literature on stock market development and performance before World War I have expanded significantly in the last decades. In addition to well-known cases of Britain, France, Germany and the United States, new estimates of stock market performance for emerging markets like Australia (Moore 2010), Ireland (Hickson and Turner 2005), Belgium (Annert et al 2006) started challenging some of the long-prevailing ideas on the drivers of stock market capitalisation (Rajan and Zingales 2003, La Porta et al. 2008). New comparative studies on stock market performance address some of the methodological shortcomings of the previous research, yet they remain largely focused on the core stock exchanges of the global economy before 1914 (Moore 2010, Mussachio 2010, Kuvshinov and Zimmermann 2021). In this paper, I provide the first estimates of stock market performance for three major stock exchanges of the Middle East before 1914: Istanbul, Alexandria, and Cairo. Officially all three were founded within the Ottoman Empire, however, given that Egypt was a de facto British protectorate after 1882, Alexandria and Cairo stock exchanges operated under a different legal framework. This legal variation makes the case for a comparative study of the Middle Eastern stock exchanges.

The origin of stock market formation in the Ottoman Empire can be taken back to the first foreign loan contracted in 1854; when the government and local bankers of Istanbul showed an interest in establishing a stock exchange to facilitate transactions on the Ottoman bonds. A new commercial code in 1861, permitting the foundation of joint-stock companies, encouraged the local bankers to take the first steps towards this purpose. *Galata* Bourse started operating in the Galata district of Istanbul in 1866, and it gained official status in 1873. Similarly in Egypt, well before the British control in 1882, the Khedives also had an interest in establishing a stock exchange in Alexandria to attract foreign capital and create a local market for Egyptian bonds. Initially, the exchange was specialised in cotton futures, and its activities were only expanded under British rule. In 1883 Alexandria Stock Exchange was founded, and this was followed by the Cairo Stock Exchange in 1903.

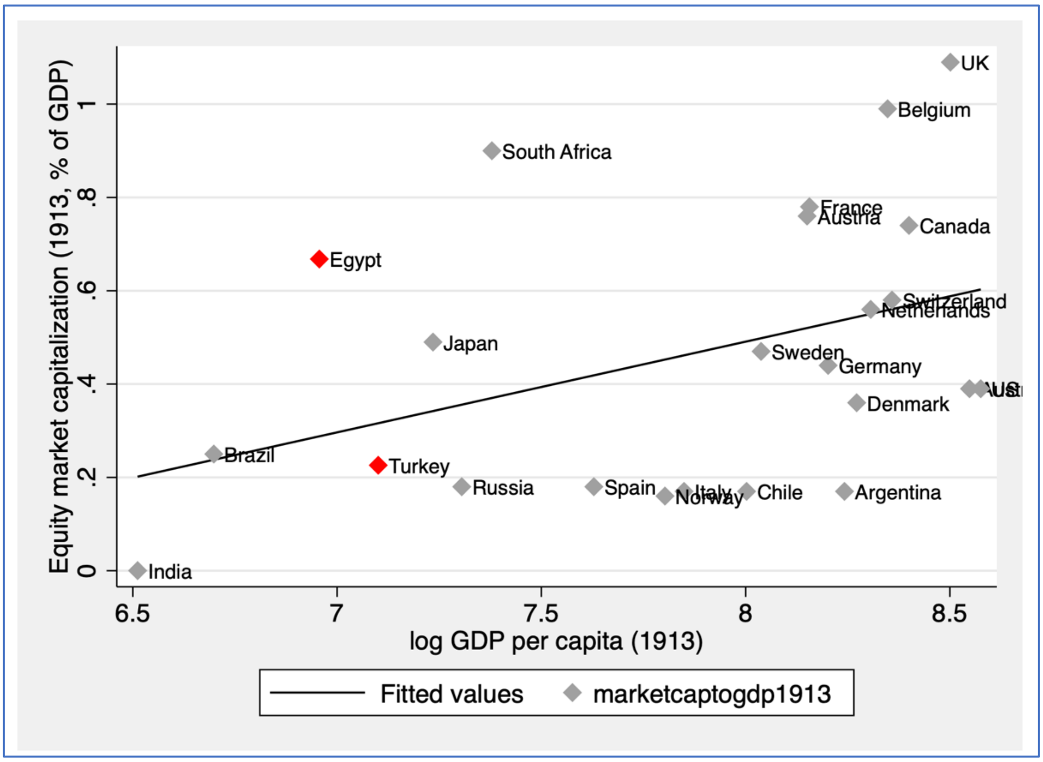
Despite being the earliest stock exchanges in the region, and comparable in size to many other peripheral exchanges, the research on these three markets have so far been scarce. I combine multiple historical collections from the archives of Credit Lyonnais, Ottoman State Archives, Egyptian official statistics to estimate the first time series of market capitalisation, stock returns and the sectoral composition of three markets: Istanbul, Alexandria, and Cairo. Preliminary findings indicate that the equity market capitalization as a percentage of GDP by 1913 for Turkey and Egypt was 21% and 66% respectively. This level was comparable to the other peripheral stock exchanges at the time such as Madrid and Tokyo, and in the case of Egypt, it was higher than many other peripheral stock exchanges (Figure 1).

Figure 1 Equity market capitalization as a percentage of GDP



Note: Egypt and Turkey are the author's calculations, the rest is elaborated from Moore (2010)

Figure 2 Stock market development c.1913



Note: Egypt and Turkey are the author's calculations, the rest is elaborated from Rajan and Zingales (2003)

In comparison to their level of economic development in 1913, Egypt had a higher level of equity market capitalization, whereas Turkey followed a standard pattern (Figure 2). This picture looks even more typical for the number of listed companies per population, as both countries ranked at a similar level to Japan, Russia, and Brazil. A closer look at disaggregated figures may suggest some potential mechanisms to explain these correlations.

First, the percentage of foreign companies operating in the region and listed on the Istanbul, Alexandria and Cairo stock exchanges were significantly high: 72% in Egypt and 36% in Turkey. This was partly thanks to the liberal system of capitulations that made possible the listing of joint-stock companies under different legal codes. Yet, these foreign companies had lower and more volatile returns compared to local ones.

Second, unlike many other emerging stock markets, the overall share of manufacturing was significantly low: 2.4% of total market capitalization in Egypt and 1.3% in Turkey. Instead, there was a significant concentration in finance, followed by transport and public utilities. There was also a discrepancy between foreign and local companies in terms of their sectoral distribution, whereby the latter group concentrated more on the manufacturing sector.

Finally, some of the differences within the region can be explained by the microstructure of the stock exchanges and the broader legal institutional framework governing capital flows within the region. During the period in question, Egypt was a veiled British protectorate, whereas Ottoman Turkey maintained its political sovereignty influenced by the French legal code in financial and commercial matters. These differences had an impact on the rules organising the stock exchanges. Yet both countries converged in terms of their legal systems as they were subject to the stipulations of the capitulations. The legal extraterritoriality created an attractive institutional environment for foreign companies, but they remained concentrated in the finance sector.