The Economic Indicators Guide

Introduction

Does the CPI, PMI or ECM mean anything to you? This guide book will explain some 20 of these terms to enhance your knowledge of economic indicators that affect your investment.

Economic indicators are used by the Federal Reserve to monitor inflation. When they reflect inflationary pressure, the Fed will increase interest rates. Conversely, when they show signs of deflation, a decrease of interest rates become imminent.

Interest rates are important for the economy because they influence the willingness of individuals and business to borrow money and make investments. An increase of interest rates will eventually slow down the economy, while a decrease will fuel an expansion.

** The Federal Reserve Bank
The Fed was created in 1913, and serves the function of being the national bank of the USA - but it's really not just one bank - there are 13 separate district banks, plus an additional 25 regional branches spread all around the country. Each district bank has a president and its own board of directors.

The Fed is run by a seven member board of governors - with each governor being appointed by the President (the U.S. president) to a term of 14 years each. Currently, Mr. Alan Greenspan is the chairman of the Fed.

1. Beige Book

Each Federal Reserve Bank gathers anecdotal information on the current economic conditions in it District through reports from Bank and Branch directors and interviews with key businessmen, economists, market experts, and other sources. The Beige Book summarizes this information by District and sector.

Importance:
The Fed uses this report, along with other indicators, to determine interest rate policy at FOMC meetings. These meetings are held two weeks after the Beige Book's release.

If the Beige Book portrays inflationary pressure, the Fed may raise interest rates. Conversely, if the Beige Book portrays recessionary conditions, the Fed may lower interest rates.

Available: It is released at 2.00pm ET on the Wednesday less than two weeks prior to an FOMC meeting.

2. Chicago Purchasing Managers' Index (PMI)

It's based on surveys of more than 200 purchasing managers regarding the manufacturing industry in the Chicago area whose distribution of manufacturing firms mirrors the national distribution. The 50% marks the breakeven line between an expanding and contracting manufacturing sector. Reading above 50% indicate and expanding factory sector while values below 50 are indicative of contraction.

Importance: Along with the Philadelphia Fed Index, helps to forecast the results of the much more closely watched ISM index, which is released on the following business day. The ISM index is a leading indicator of overall economic activity.

Available: Last business day of the month at 10.00 am ET. Data for current month.

3. Consumer Confidence Index

A survey of 5,000 consumers about their attitudes concerning the present situation and expectations regarding economic conditions conducted.

Importance: This report can occasionally be helpful in predicting sudden shifts in consumption patterns. And since consumer spending accounts for two-thirds of the economy, it gives is insight about the direction of the economy. However, only index changes of at least five points should be considered significant.

Available: Last Tuesday of the month at 10.00 ET. Data for month prior.

4. Consumer Price Index (CPI)

An index that measures the change in price of a representative basket of goods and services such as food, energy, housing, clothing, transportation, medical care, entertainment and education. It's also known as the cost-of-living index.

The final sales figure, which excludes inventories, can sometimes be helpful in identifying underlying growth trends as inventories represent unsold goods, and a large inventory increase will boost GDP but might be indicative of weakness rather than strength.

Importance: It's important to monitor the CPI excluding food and energy prices for monthly stability. This is referred to as the "core CPI" and gives a clearer picture of the underlying inflation trend. The rate of change of the core CPI is one of the key measures of inflation for the US economy. Inflationary pressure is generated when the core CPI posts larger-then-expected gains.

Available: Around the 13th of the month at 8.30am ET. Date for month prior.

5. Durable Goods Orders

Its official name is Advance Report on Durable Goods Manufacturer's Shipments and Orders. This is a government index that measures the dollar volume of orders, shipments, and unfilled orders of durable goods . Durable goods are new or used items generally with a normal life expectancy of three years or more. Analysts usually exclude defence and transportation orders because of their volatility.

Importance: This report gives us information on the strength for US manufactured durable goods, from both domestic and foreign sources, When the index is increasing, it suggests demand is strengthening, which will probably result in rising production and employment. A falling index suggests the opposite. This is also one of the earliest indicators of both consumer and business demand for equipment. Increased expenditures on investment goods reduces the prospect of inflation.

Available: Around the 26th of the month at 8.30am ET. Data for the month prior.

6. Employment Cost Index (ECI)

The ECI is designed to measure the change in the cost of labor, including wages and salaries as well as benefits.

Importance: It's useful in evaluating wage trends and the risk of wage inflation. If wage inflation threatens, it's likely that interest rates will rise, then bond and stock prices will fall.

Available: Last business day of January, April, July and October at 8.30 ET. Data for quarter prior.

7. Employment Report

The employment report is actually two separate reports which are the results of two separate surveys. The household survey is a survey of roughly 60,000 households. This survey produces the unemployment rate. The establishment survey is a survey of 375,000 businesses. This survey produces the nonfarm payrolls, average workweek, and average hourly earnings figures, to name a few. Both surveys cover the payroll period which includes the 12th of each month.

This release is the single most closely watched economic statistic because of its timeliness, accuracy and its importance as an indicator of economic activity. Therefore, it plays a big role in influencing financial market psychology during the month.

Importance: Non-farm payroll is a coincident indicator of the economic growth. The greater the increase in employment, the faster the total in economic growth.

An increasing unemployment rate is associated with a contracting economy and declining interest rates. Conversely, a decreasing unemployment rate is associated with an expanding economy and potentially increasing interest rates. The fear is that wages will rise if the unemployment rate becomes too low and workers are hard to find. The economy is considered to be full employment when unemployment between 5.5% and 6.0%.

If the average earnings is rising sharply, it may be an indication of potential inflation. When the average workweek is trending higher, it forecasts additional employment increases.

Available: First Friday of the month at 8.30am ET. Data for month prior.

8. Existing Home Sales

This report measures the selling rate of pre-owned houses. It's considered a decent indicator of activity in the housing sector.

Importance: This provides gauge of not only the demand for housing, but the economic momentum. People have to be financially confident in order to buy a house.

Available: On the 25th of the month (or on the first business day thereafter) at 10.00am ET. Data for month prior.

9. Gross Domestic Product (GDP)

GDT measures the dollar value of all goods and services produced within the borders of the United States, regardless who owns the assets or the nationality of the labor used in producing that output. Data are available in nominal and real dollars. Investors always monitor the real growth rates because they are adjusted for inflation.

Importance: This is the most comprehensive measure of the performance of the US economy.

Healthy GDP growth is between 2.0% and 2.5% (when unemployment rate is between 5.5% and 6.0%). This translates into strong corporate earnings, which bodes well for the stock market.

A higher GDP growth leads to accelerating inflation, while lower growth indicates a weak economy.

Revision: Revised estimates are released during the second and third months of the quarter based in more complete information. Benchmark data and new seasonal adjustment factors are introduced in July with the release of second quarter date. This revision affects at least three year worth of data, Its significant is moderate.

Available: Third or Fourth week of the month at 8.30am ET for the prior quarter, with subsequent revisions released in the second and the third months of the quarter.

10. Housing Starts and Building Permits

A measure of the number of residential units on which construction is begun each month.

Importance: It's used to predict the changes of gross domestic product. While residential investment represents just four percent of the level of GDP, due to its volatility it frequently represents a much higher portion of changes in GDP over relatively short period of time.

Revisions: The data are revised monthly for the prior two months to incorporate more complete information. New seasonal adjustment factors are introduced in February with the release of the January data. This revision affects at least three years of data, but its significance is generally small.

Available: Around the 16th of the month at 8.30am ET. Data for month prior.

11. Industrial Production and Capacity Utilization

The Index of Industrial Production is a chain-weight measures of the physical output of the nations factories, mines and utilities. The capacity utilization rate measures the proportion of plant and equipment used in production by these industries.

Importance: While the industrial sector of the economy represents only about 25% of the GDP, changes in GDP are heavily concentrated in the industrial sector. Therefore, changes in The Index of Industrial Production provide useful information on the current growth of GDP.

Investors use the capacity utilization rate as an inflation indicator. If it gets above 85%, inflationary pressures are generated.

Available: Around the 15th of the month at 9.15am ET. Data for month prior.

12. Initial Claims

A government index that tracks the number of people filing first-time claim of state unemployment insurance.

Importance: Investors use this indicator's four week moving average to predict trends in the labour market. A move of 30,000 or more in claims shows a substantial change in job growth. Remember that the lower the number of claims, the stronger the job market, and vice versa.

Revisions: Revised figures for the previous week are released each Thursday. The significance of these revision is moderate.

Available: Thursday at 8.30am ET, Data for week ended prior Saturday

13. ISM Manufacturing Index

The ISM Manufacturing Index based on surveys of 300 purchasing managers nationwide representing 20 industries regarding manufacturing activity. It covers indicators as new orders, production, employment, inventories, delivery times, prices, export orders, and imports orders.

Importance: It's considered as the king of all manufacturing indices. Readings of 50% or above are typically associated with an expanding manufacturing sector and a healthy economy, while readings below 50 are associated with contraction.

Additionally, its various sub-components contain useful information about manufacturing activity. The production component is related to industrial production, new orders to durable good orders, employment to factory payrolls, prices to producer prices, export orders to merchandise trade exports and import orders to merchandise imports.

The index is seasonally adjusted for the effects of variations within the year, differences due to holidays and institutional changes.

Available: ON the first business day of the month at 10.00am ET. Data for month prior.

14. ISM Services Index (aka Non-Manufacturing ISM)

This index is based on a survey of roughly 370 purchasing executives in industries including finance, insurance, real-estate, communications and utilities. It reports on business activity in the service sector.

Importance: Readings above 50% indicates expansion for non-manufacturing components of the economy. While readings below 50 indicate contraction.

The index is seasonally adjusted for the effects of variations within the year, differences due to holidays and institutional changes.

This is a new index, created in 1997, so it's not followed as closely by investors as ISM MAnufacturing Index, which dates to the 1940's.

Available: ON the third business day of the month at 10.00 am ET. Data for month prior.

15. New Home Sales (aka New Single-Family Houses Sold)

This report is based on interviews of about 10,000 builders or owners of about 15,000 selected building projects. It measures the number of newly constructed homes with a committed sale during the month.

Importance: It's considered a good gauge of near-term spending for housing-related items and of consumer spending in general. However, investors prefers the existing home sales report, which accounts for 84% of all houses sold and is released earlier in the month.

Available: Around the last business day of the month at 10.00am ET. Data for month prior.

16. Personal Income and Consumption

This report is also know as Personal Income and Outlays. Personal income represents the income that households receive from all sources, including employment, self-employment, investments and transfer payments.

Personal outlays are consumer spending which is devided into durable goods, non-durable goods, and services.

Importance: Income is the major determinant of spending and consumer spending accounts for two-thirds of the economy. Greater spending spurs corporate profits and benefits the stock market.

Available: First business day of the month at 8.30am ET. Data for two months prior.

17. Philidelphia Fed

Regional manufacturing index that covers Pensylvania, New Jersey and Delaware. This region represents a reasonable cross section of the national manufacturing activities.

Importance: Reading above 50% indicates an expanding factory sector while values below 50 are indicative of contraction. Alomg with the Chicago Purchasing Manager's Index, helps to forecast the results of the much more closely watched ISM index. The ISM index is a leading indicator of overall economic activity.

Availabiity: Third Thursday of the month at 10.00am ET. Data for the current month.

18. Producer Price Index (PPI)

The Producer Price Index (PPI) measures the average price of a fixed basket of capital and consumer goods at the wholesale level. There are three primary publication structures for the PPI: industry, commmodity and stage-of-processing.

Importance: Lt's important to monitor the PPIexcluding food and energy prices for its monthly stabilty. this is referred as the "core PPI" and gives a clearer picture of the underlying inflation trend. Changes in the PPI are considered a precursor of consumer price inflation. Inflationary pressure is generated when the core PPI posts larger-than-expected gains.

Availability: Around the 11th of each month at 8.30am ET. Data for month prior.

19. Retail Sales

This index measures the total sales of goods by all retail establishments in the U.S.(sales of services are not included). These fugures are in current dollars and are not adjusted for inflation. However, the data are adjusted for seasonal, holiday and trading-day differences between the months of the year.

Importance: This is considered the most timely indicator of broad consumer spending patterns. It gives you a sense of the trends among different types of retailers. These trends can help you spot specific investment opportunities. It is important to monitor retail sales excluding autos and trucks to aviod the move extreme volatility.

Availabilty: Around the 12th of the month at 8.30am ET. Data for the month prior.

20. International Trade

This report measures the difference between exports and imports of US goods and services.

Importance: Imports and exports are important components of aggregate economic activity, representing approximately 14 and 12% of GDP respectively. Typically, stronger exports are bullish for corporate earnings and the stock market.

Changes in trade balance with particular countries can have implications for foreign exchange and policy with that trading partner, so this report is also important for investors who are interested in diversifying globally.

Revision: Data for the prior three months are revised monthly to incorporate more complete information. New seasonal adjustment factors are introduced in July. This revision affects at least three years worth of data, Its significance is small.