6 Key Economic Indicators for Investors

Insights and strategies

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What are Economic Indicators?

Economic indicators are key pieces of data that are released in order to give insight into the performance of a country's economy. They're often referred to as macroeconomic indicators, as they show data on a large scale.

Macroeconomic indicators are used to analyse current and future trends – whether for investment purposes or to judge the health of an economy. Most economic indicators are official data releases, produced by governments or non-profit organisations.

What is the Purpose of Economic Indicators?

The main purpose of economic indicators is to give an understanding of the state of an economy. For investors, traders and analysts, economic indicators provide information that can help them to discover new opportunities and adjust their portfolios.

Economic indicator announcements are widely followed, which means markets can move dramatically around each release as traders and investors adjust their positions. Therefore, most fundamental analysis will include economic indicators.

Traders and investors will keep an eye on analysts' predictions for upcoming data releases to shape their trading strategies. If the actual figures are massively different from the expectations, there can be more volatility as everyone scrambles to adjust.

As most economic indicators are produced by or for policy makers, these indicators can also influence decisions going forward and ultimately change the course of political strategies.

Economic indicators will have a larger influence in the countries that they are about – ie UK data releases will have a more direct impact on the FTSE 100, British pound and UK companies than on other markets.

Types of Economic Indicators

So Important to Economists and Investors?

01 Leading indicators

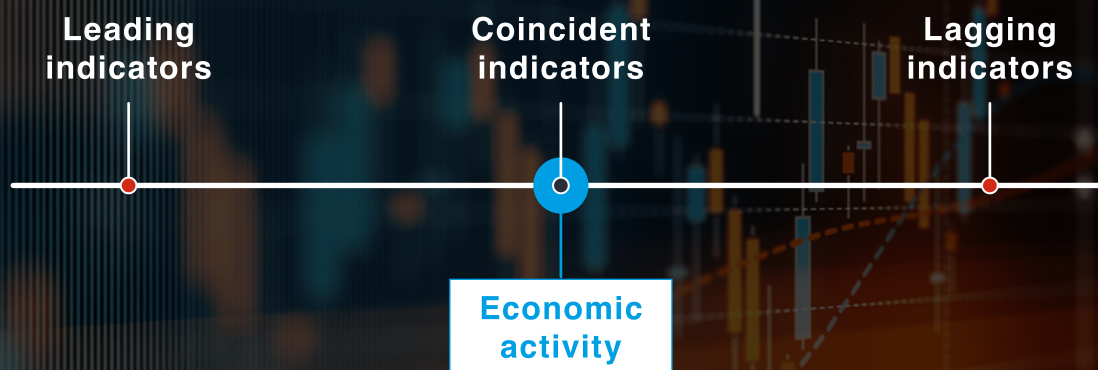
which are used to predict future the movements and trends of an economy. These figures change before the economy does, which can be helpful for identifying opportunities but risky, as they're not 100% accurate

02 Coincident indicators

which are used to predict future the movements and trends of an economy. These figures change before the economy does, which can be helpful for identifying opportunities but risky, as they're not 100% accurate

03 Lagging indicators

which trail the economy and are released after economic activity occurs. These aren't necessarily useful for identifying trading opportunities, but provide essential insights into the health of an economy



Key Macroeconomic Indicators to Watch

There are a number of data releases that can help traders and analysts understand changes to a country's economy, the main ones are:

1. **Gross Domestic Product (GDP)**
2. **Interest Rates**
3. **Currency Markets**
4. **Unemployment and Wages**
5. **Consumer Price Index (CPI)**
6. **Producer Price Index (PPI)**
7. **Balance of Trade**
8. **Housing Market**
9. **Manufacturing & Non - Manufacturing Activity**

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Why GDP Is
So Important to Economists and Investors?

Key Takeaways

- Gross domestic product tracks the health of a country's economy.
- It represents the value of all goods and services produced over a specific time period within a country's borders.
- Economists can use GDP to determine whether an economy is growing or experiencing a recession.
- Investors can use GDP to make investments decisions—a bad economy means lower earnings and lower stock prices.

What is GDP

Gross domestic product (GDP) is one of the most common indicators used to track the health of a nation's economy. The calculation of a country's GDP takes into consideration a number of different factors about that country's economy, including its consumption and investment.

GDP is perhaps the most closely-watched and important economic indicator for both economists and investors alike because it is a representation of the total dollar value of all goods and services produced by an economy over a specific time period. As a measurement, it is often described as being a calculation of the total size of an economy.

The figure is generally expressed as a dollar amount and its growth rate as percentage change from one period to the next (where the time period is typically quarterly or yearly). The figure is reported in the United States on a quarterly basis by the Bureau of Economic Analysis. While quarterly growth rates are a periodic measure of how the economy is faring, annual GDP figures are often considered the benchmark for the overall size of the economy.

GDP for Economists and Investors

GDP is an important measurement for economists and investors because it is a representation of economic production and growth. Both economic production and growth have a large impact on nearly everyone within a given economy. When the economy is healthy, there is usually a lower level of unemployment, and wages tend to increase as businesses hire more labor to meet the growing demand of the economy. Economists look at positive GDP growth between different time periods (usually year-to-year) to make an assessment of how much an economy is flourishing. Conversely, if there is negative GDP growth, it may be an indicator that an economy is in or approaching a recession or an economic downturn.

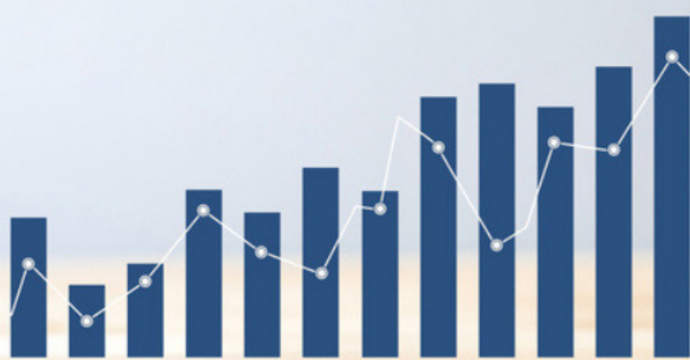
Investors pay attention to the GDP because a significant percentage change in the GDP–either up or down–can have a significant impact on the stock market. In general, a bad economy usually means lower earnings for companies. And this can translate into lower stock prices.

Investors may pay attention to positive and negative GDP growth when they are devising an investment strategy. However, it's important to note that because GDP is a measurement of the economy in the previous quarter or year, it is better used to help explain how economic growth and production have impacted your stocks and your investments in the past. It is not considered a helpful predictor of how the market will move in the future.

Nominal vs. Real GDP

GDP can be expressed in two different ways—nominal GDP and real GDP. Nominal GDP takes current market prices into account without factoring in inflation or deflation. Nominal GDP looks at the natural movement of prices and tracks the gradual increase of an economy's value over time.

On the contrary, real GDP factors in inflation. meaning it accounts for the overall rise in price levels. Economists generally prefer using real GDP as a way to compare a country's economic growth rate. Real GDP is how economists can tell whether there is any real growth between one year and the next. It is calculated using goods and services prices from a base year, rather than current prices, in order to adjust for price changes. By comparing the resulting real GDP to nominal GDP, economics can calculate a GDP price deflator, which can serve as a measure of inflation in the economy.



What is
Non-Farm Report?

Key Takeaways

- Non-farm payrolls (NFP) are an important economic indicator related to employment in the U.S.
- Understanding this data release can help set up forex trades to take advantage of unexpected changes in employment.
- Technical analysis can be employed to the NFP report using 5- or 15-minute chart intervals.

What is Non-Farm Report

The non-farm payroll (NFP) report is a key economic indicator for the United States. It is intended to represent the total number of paid workers in the U.S. minus farm employees, government employees, private household employees and employees of nonprofit organizations. The non-farm payroll report causes one of the consistently largest rate movements of any news announcement in the forex market. As a result, many analysts, traders, funds, investors, and speculators anticipate the NFP number and the directional movement it will cause. With so many different parties watching this report and interpreting it, even when the number comes in line with estimates, it can cause large rate swings.

The release of the NFP generally occurs on the first Friday of every month at 8:30 a.m. EST.4 This news release creates a favorable environment for active traders because it provides a near guarantee of a tradable move following the announcement. As with all aspects of trading, whether we make money on it is not assured. Approaching the trade from a logical standpoint, based on how the market is reacting, can provide us with more consistent results than simply anticipating the directional movement the event will cause.

Analyzing the Non-Farm Report Numbers

Like any other piece of economic data, there are three ways to analyze the U.S. non-farm payroll number:

A higher payroll figure is good for the U.S. economy. This is because more job additions help to contribute to healthier and more robust economic growth. Consumers who have both money and a job tend to spend more, leading to growth. As a result, foreign exchange traders and investors look for a positive addition of at least 100,000 jobs per month. Any release above—let's say 200,000—will help to fuel U.S. dollar gains. An above-consensus estimate release will have the same effect.

An expected change in payroll figure causes a mixed reaction in the currency markets. Forex investors witnessing an expected change in the NFP report will turn to other sub-components and items to gain some sort of direction or insight. This includes the unemployment rate and manufacturing payroll sub-component. So, if the unemployment rate drops or manufacturing payrolls rise, currency traders will side with a stronger dollar, a positive for the U.S. economy. But, should the unemployment rate increase, manufacturing jobs decline, investors will drop the U.S. dollar for other currencies.

A lower payroll figure is detrimental for the U.S. economy. Like any other economic report, a lower employment picture is negative for the world's largest economy and the greenback. Should the NFP report show a decline below 100,000 jobs (or a less-than-estimated print), it's a good sign the U.S. economy isn't growing. As a result, Forex traders will favor higher-yielding currencies against the U.S. dollar.

The NFP Trading Strategy

The NFP report generally affects all major currency pairs, but one of the favorites among traders is the GBP/USD. Because the forex market is open 24 hours a day, all traders have the ability to trade the news event.

The logic behind the strategy is to wait for the market to digest the information's significance. After the initial swings have occurred, and after market participants have had a bit of time to reflect on what the number means, they will enter a trade in the direction of the dominating momentum. They wait for a signal indicating the market may have chosen a direction to take rates. This avoids getting in too early and decreases the probability of being whipsawed out of the market before it has chosen a direction.

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Understanding
Consumer Price Index (CPI)

Key Takeaways

- The Consumer Price Index measures the average change in prices over time that consumers pay for a basket of goods and services.
- CPI is the most widely used measure of inflation and, by proxy, of the effectiveness of the government's economic policy.
- The CPI statistics cover professionals, self-employed, unemployed, people whose incomes are below the federal poverty threshold, and retired people in the country but excludes non-metro or rural populations, farm families, armed forces, people who are currently incarcerated, and those in mental hospitals.
- CPI-W measures the Consumer Price Index for Urban Wage Earners and Clerical Workers while the CPI-U is the Consumer Price Index for Urban Consumers.

What is Consumer Price Index (CPI)?

The Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care. It is calculated by taking price changes for each item in the predetermined basket of goods and averaging them. Changes in the CPI are used to assess price changes associated with the cost of living. The CPI is one of the most frequently used statistics for identifying periods of inflation or deflation. While it does measure the variation in price for retail goods and other items paid by consumers, the Consumer Price Index does not include things like savings and investments, and can often exclude spending by foreign visitors.