

FINANCIAL CONDITIONS INDEXES: AN OVERVIEW

From Raw Data to Regime Signals:

- Filters through hundreds of economic indicators and market ratios using Granger causality to identify true leading relationships
- Combines them into composite indexes via linear regression and nonlinear Machine Learning (ML) models to capture evolving dynamics

Unified Market Gauge:

- Condenses credit, liquidity, funding, and volatility metrics into one forward-looking signal

Key Advantages:

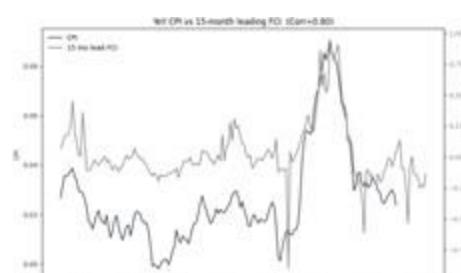
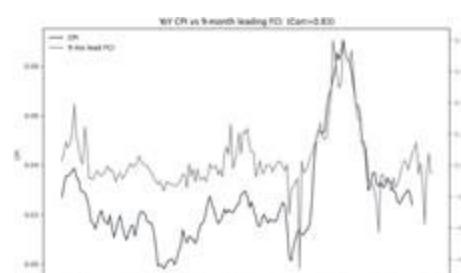
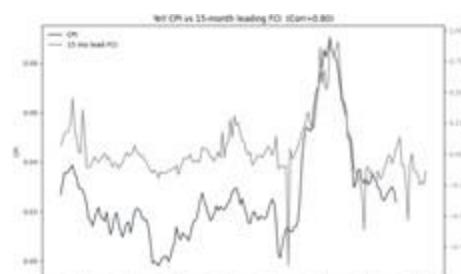
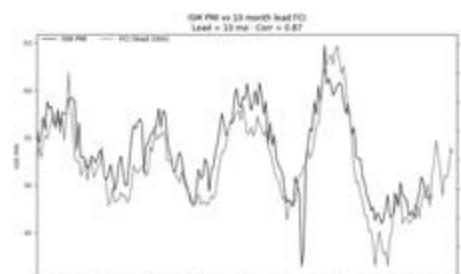
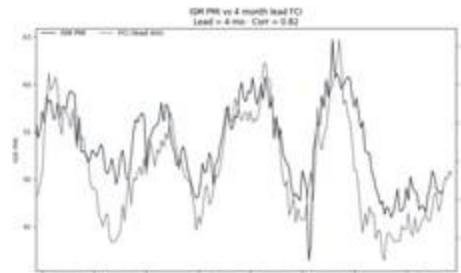
- **Noise Reduction:** Focuses on sustained regime shifts, not transient spikes
- **Actionable Alerts:** Flags predefined thresholds for tactical pivots

Tactical Use Cases:

- **Sector Tilts:** Rotate between cyclicals and防守性 as conditions evolve
- **Risk Management:** Signal hedges during widening spreads/volatility surges
- **Portfolio Timing:** Align duration, beta, and carry exposure with macro trends

Adaptive, ML-Enhanced:

- Rolling recalibration ensures indexes evolve as relationships change, maintaining a forward-looking view on financial conditions



2 - MONTH ISM AND CPI FINANCIAL CONDITIONS INDEXES

Correlations:

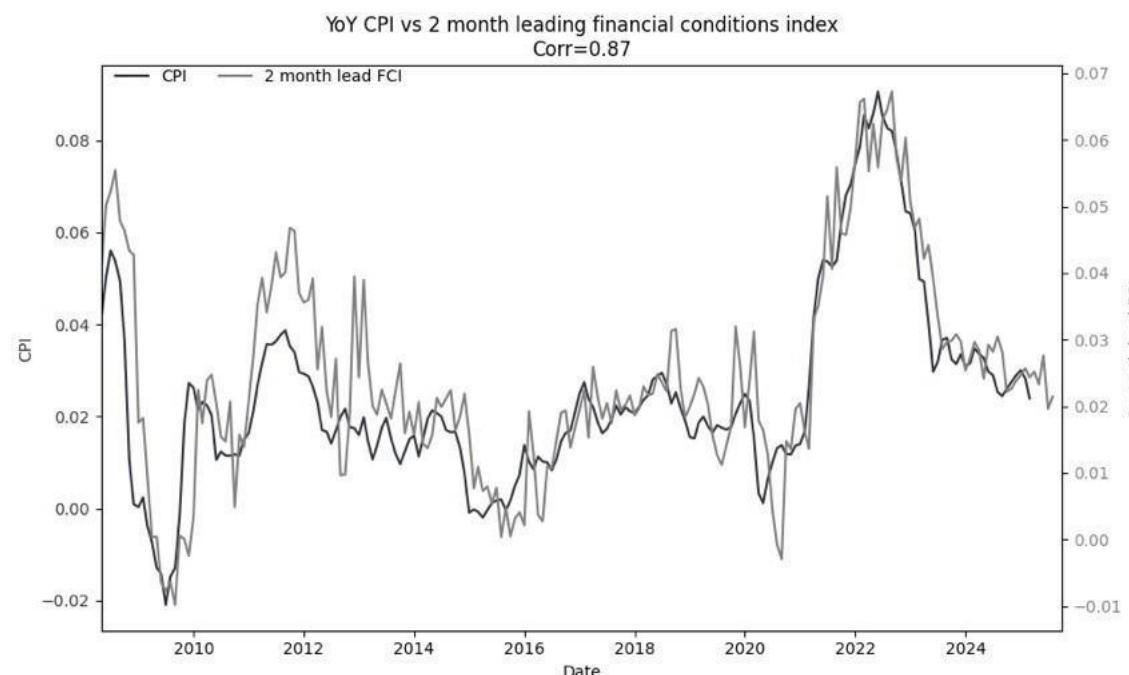
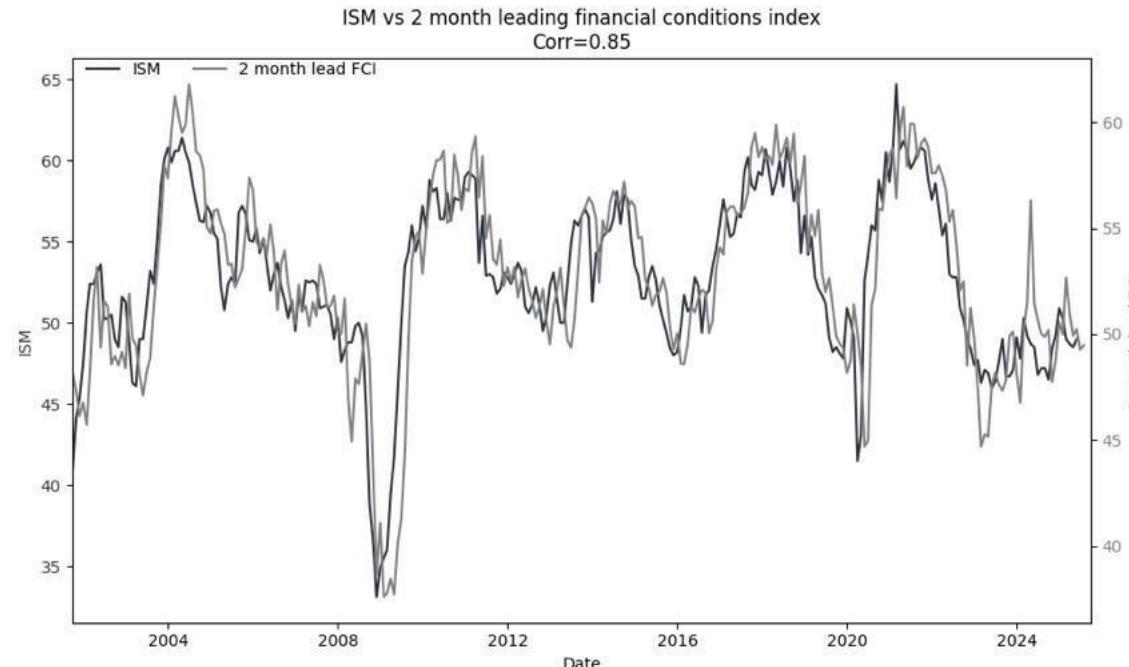
- ISM vs. 2-month FCI: Correlation = 0.85
- YoY CPI vs. 2-month FCI: Correlation = 0.87

Timely cycle signal:

- FCI leads shifts in manufacturing activity and inflation by ~2 months
- Early warning for tightening or easing conditions

Short-term:

- Shift sector & factor exposures ahead of official data releases
- Complements our longer-horizon (4, 9, 15 month) FCIs for more complete cycle coverage



4 - MONTH ISM AND CPI FORECASTS

Correlations:

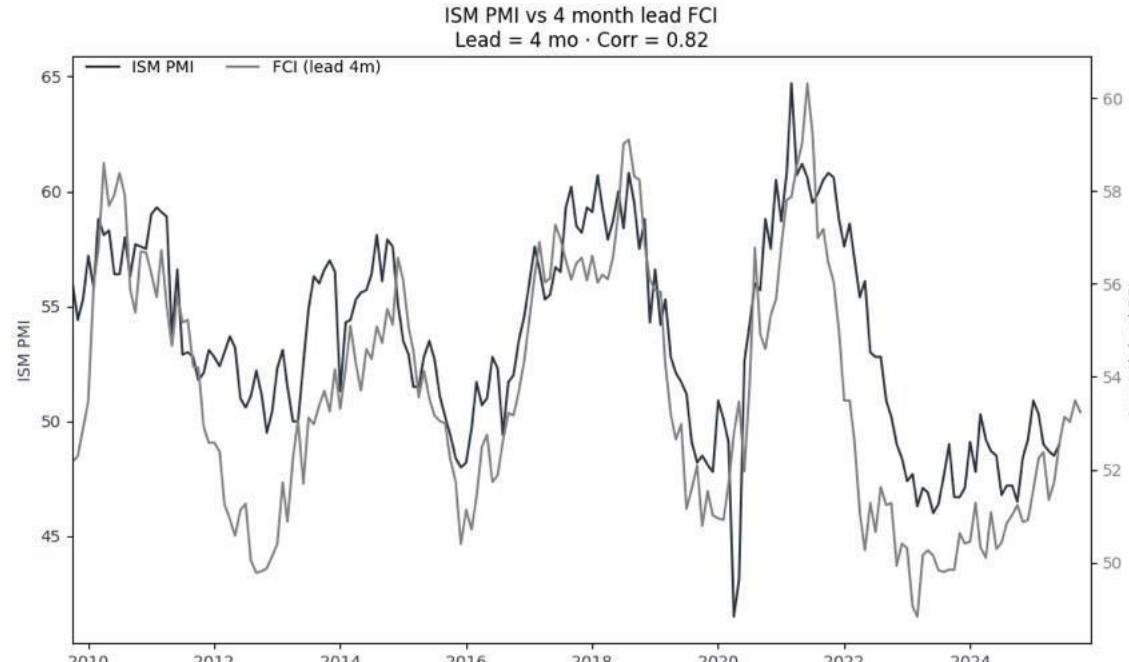
- ISM PMI vs. 4-month FCI: Correlation = 0.82
- YoY CPI vs. 4-month FCI: Correlation = 0.88

Consistent Turning-Point Signals:

- FCI reliably leads major inflection points in both activity (ISM) and inflation (CPI) by roughly four months
- Captures downturns (2011, 2015) and recoveries (2013, 2021) ahead of official prints

Tactical:

- Asset Allocation: Position risk exposures proactively around growth/inflation cycles
- Risk Management: Anticipate tightening or easing conditions before consensus



9/ 10 - MONTH ISM AND CPI FORECASTS

Correlations:

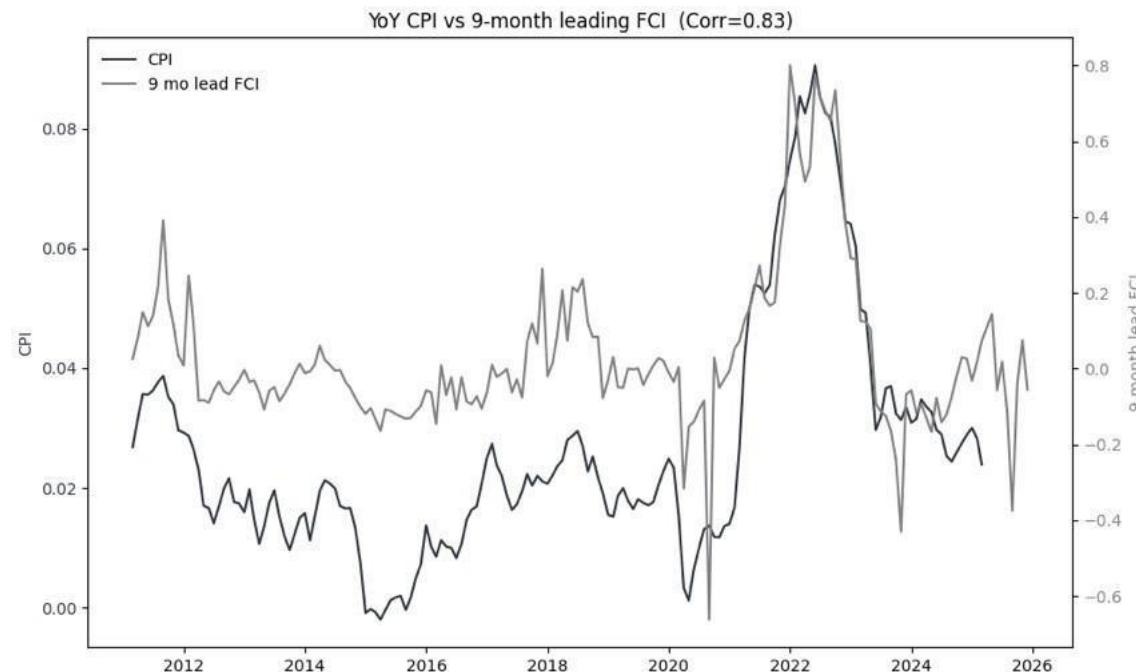
- 10-month FCI leads ISM PMI with Correlation = 0.87, accurately anticipating major cycle turns
- 9-month FCI leads YoY CPI with Correlation = 0.83, capturing inflation peaks and troughs nearly a year in advance

Consistent Across Regimes:

- Early warnings before financial downturns and shocks
- Timely signal on the 2021–2022 inflation surge

Intermediate:

- Strategic Allocation: Shift equity vs. fixed-income exposure based on 9–10-month forward momentum
- Inflation Hedging: Calibrate duration and commodities positions ahead of CPI inflection points
- Risk Management: Preempt cyclical slowdowns with defensive positioning nearly a year before traditional data confirms



15 - MONTH ISM AND CPI FORECASTS

Correlations:

- 15-month FCI leads ISM PMI with Correlation = 0.93, delivering the earliest warning of manufacturing cycle turns
- 15-month FCI leads YoY CPI with Correlation = 0.80, signaling inflation upswings and slowdowns more than a full year before realized CPI prints

Deep-Cycle Insights:

- Forewarns the 2021–2022 inflation spike back in late-2020

Strategic:

- Advanced Tactical Allocation: Position portfolios for the next cycle pivot well before consensus
- Policy Intelligence: Inform central-bank watch and rate-cut/tighten expectations with a 15-month head start
- Risk Overlay: Deploy defensive overlays or tail-risk hedges over a longer horizon to protect multi-quarter exposures

