

#### **Introduction to Financial Markets**

# Bloomberg L.P.

#### 1. Economics I

GDP and its link to markets Inflation and other releases Markets and sentiment

Alex Reid

# About the presenter - Alex Reid

Over 20 years practical experience in financial markets Africa, Asia, Australia, Europe, Middle East, UK, USA

Trader: NatWest, Greenwich Capital, RBS

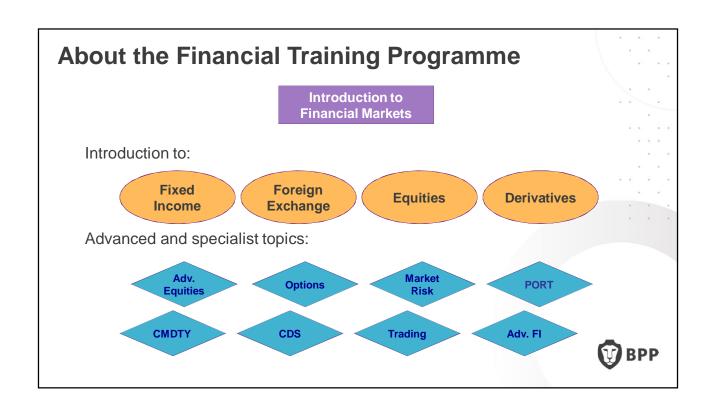
Corporate bonds, derivatives

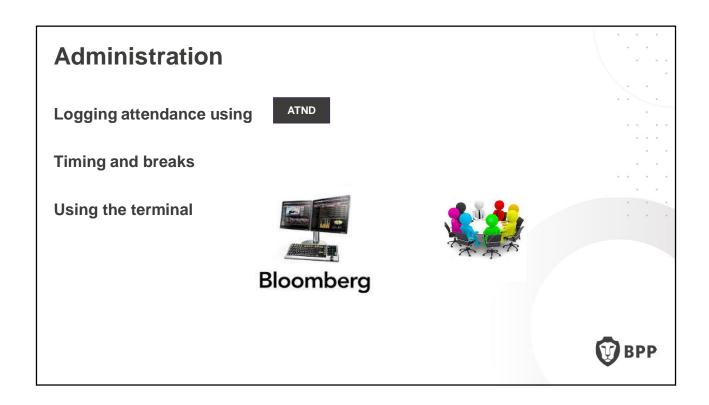
Trainer: ANZ Global Markets and exhibit3 Ltd Graduate programmes, bank's staff and clients

CFA, ACMA, BSc (hons) St.Andrews University









# **Overall course programme**

	Topics
Session 1	Economics I
Session 2	The finance industry
Session 3	Government
Session 4	Economics II
Session 5	Fund managers
Session 6	Essential math concepts

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#### **Gross Domestic Product**

GDP is the best known barometer of economic health Typically released quarterly & compared with prior period





https://www.ons.gov.uk/peoplepopulationandcommunity/wellbeing/bulletins/personalandeconomicwellbeingintheuk/september2020

How closely do financial markets correlate to GDP?



# **Economy versus stock market**

Access US GDP in dollar terms using ticker below Chart it using a quarterly frequency (GP Q) Then use the "compare" tab and add the S&P500 index



What do you see?

Do the US stock market and economy move in sync?

GDP CUR\$ <>



# **Absolute GDP and change**

The absolute level of GDP is hard to put in context Only crops up when one country overtakes another e.g. France / UK and China / Japan



**ECO** 

Two GDP figures are widely followed:

- 1. Change in GDP (QoQ and YoY)
- 2. GDP per capita
  Relative economic wellbeing of population



### **Nominal and Real GDP**

GDP is measured and reported in money terms



Imagine an economy's total production is 1 bicycle

Sold at a dollar value of \$1,000 in 2019

In 2020 total production is also 1 bicycle, but sold at \$1,020

Growth in nominal GDP is 2%

But real GDP growth is 0%

Published GDP figures typically highlight real GDP



# Impact on financial markets

In the short term,

How do you think a strong GDP release impacts:

**US GDP** 



Chinese GDP

Equity prices?

Currencies?

Commodities?



### Inflation

Inflation is a measure of change in prices



We touched on inflation with GDP (nominal v real)

Inflation is typically measured via an index Such as Consumer Price Index (CPI) How do you think inflation measures are calculated?



#### Different measures of inflation

CPI is probably the best-known term associated with inflation Central banks often "target" a level for CPI But you will see other releases on the terminal

Measure	Target ?
CPI	ECB 0-2%, UK 1-3%, China assumed to be about 3%
GDP deflator	US "stable prices" (1-2%?)
PPI, RPI, Core	Of interest to investors, even if not often used as target

US Fed pays closer attention to GDP deflator
But does not have an explicit target for it
How does the deflator differ from CPI-style measure?





# Inflation targeting

Inflation erodes the value of money. Even at 3% per annum, Half the value of a dollar/euro/yuan/etc. is lost in 24 years

But the benefits of having some inflation are:

- 1. Encourages investment
- 1
- 2. "Liquidity trap". We repay nominal debt with real income







#### Other measures of inflation

Core inflation excludes food and oil prices

Producer prices (PPI) are a "factory gate" measure Other "wholesale" price indices are similar in nature Why might investors pay close attention to PPI releases?



PPI ----



CPI —



🕡 врр

### Other economic releases

Use the function

ECO

Find recent releases for: Retail Sales, Housing, Employment

The most data tends to come from the USA Consider the market impact of these figures







# **Sentiment surveys**

How do consumers (or businesses) feel about the economy

Methodology is typically asking questions about: Feelings about current position, future position Sometimes also previous position e.g. 6 months ago

These have some validity as forward-looking indicators



# **University of Michigan**

University of Michigan Consumer Sentiment Index A US indicator, probably the best-known release

**CONSSENT** 

- 1.Own position today versus 12 months ago
- 2.Own position in 12 months' time
- 3. Wider economy in 12 months' time
- 4. Wider economy in next 5 years
- 5. Current appetite for major purchases

Base year 1966 set at 100. Rising level seen as positive



#### **Consumer sentiment and markets**

Produce a long-term chart of this index using GP Q

CONSSENT



See how it compares with the S&P500 index As well as its correlation with 10-year US Treasury yields

SPX <index>

GT10 <gov>



#### Other sentiment measures

Purchasing Managers Indices
Why do investors pay heed to these?





Bloomberg

Tankan

Quarterly survey of Japanese firms

**IFO** 

German businesses

Optional ... set an alert for the next release date

Which markets do you think will respond to this event?



# **Alternative reading**

An alternative, micro-based view of economy For Ray Dalio, it is all like a game of monopoly!

http://www.bwater.com/Uploads/FileManager/research/how-the-economic-machine-works/a-template-for-understanding--ray-dalio-bridgewater.pdf

The Economist magazine

**Bloomberg QUIC** 

Roubini, Krugman, Mankiw, Shiller, Rogoff, Samuelson, Minsky, Stiglitz





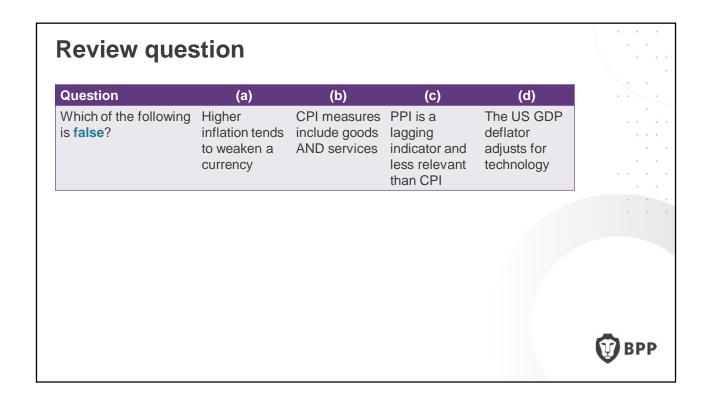
Many Bloomberg users follow economic releases

GDP and inflation are probably the most significant Along with interest rate announcements (previously!)

Employment & housing are among other significant data

Markets do not always respond as predicted Short-term and longer term responses can differ





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