



Introduction to Financial Markets

Bloomberg L.P.

1. Economics I

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

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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

LinkedIn



About the Financial Training Programme

Introduction to
Financial Markets

Introduction to:

Fixed
Income

Foreign
Exchange

Equities

Derivatives

Advanced and specialist topics:

Adv.
Equities

Options

Market
Risk

PORT

CMDTY

CDS

Trading

Adv. FI



Administration

Logging attendance using

ATND

Timing and breaks

Using the terminal



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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

GDP and its link to markets.
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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\$ <>



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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

Two GDP figures are widely followed:

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



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ECO



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



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



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

CONSENT

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

CONSENT



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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?

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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



Summary

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



Review question

Question	(a)	(b)	(c)	(d)
Which of the following is false ?	Higher inflation tends to weaken a currency	CPI measures include goods AND services	PPI is a lagging indicator and less relevant than CPI	The US GDP deflator adjusts for technology



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