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ABOUT MIKE ARMSTRONG



Mike Armstrong, a business editor and writer for nearly two decades, is the Inquirer's business columnist and PhillyInc blog editor.

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THURSDAY, JANUARY 15, 2009

## Philadelphia Fed launches new index to measure change in business conditions

All any of us really want to know is: When will the recession end?

Take your pick of the predictions. Some economists say the economy will improve in the second half of 2009. Others see it happening in 2010.

I don't really know the answer - no one really does.

But that doesn't keep forecasters, analysts and journalists from looking for signs of a turnaround. The clues, we believe, are in the rivers of statistics that gush from the federal government and the private-sector every day.

But what to focus on? Does a 2.7 percent drop in December retail sales mean as much as the loss of 524,000 jobs in the same month?

Some who want to keep it simple look only at the changes in the monthly employment report issued by the **Labor Department** or the quarterly reports on gross domestic product released by the **Commerce Department**.

But business cycles are so complex that no one variable can truly define them.

That's why economists pick several different factors and see how they interact. One such measurement is the **Conference Board's Index of Leading Economic Indicators**, which consists of 10 different sets of data, including building permits, interest rate spread and real money supply.

But that report comes out once a month, and a lot can change in intervening weeks.

Now the **Federal Reserve Bank of Philadelphia** is publishing a new index that's designed to tell whether the economy is getting better or worse, and it will be updated at least once a week. Called the **ADS business conditions index**, the measurement draws from U.S. government data on six indicators:

- \* Initial jobless claims, which are issued every Thursday.
- \* Payroll employment, industrial production, personal income, and manufacturing and trade sales - all released monthly.
- \* Real gross domestic product, issued quarterly.

The "ADS" in the name of index comes from the economists behind it: S. Boragan Aruoba, of the **University of Maryland**; Francis X. Diebold, of the **University of Pennsylvania**; and Chiara Scotti, of the **Federal Reserve Board**.

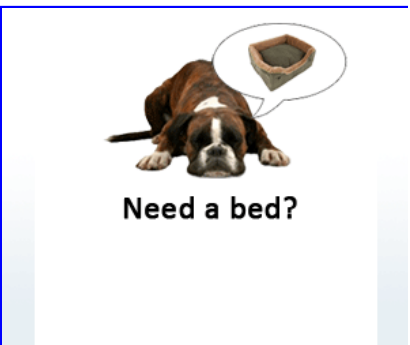
Aruoba walked me through the index, which is hosted on the Philly Fed's Web site. Over the six months the economists have been running the data, they found the index does correlate with the official periods of recession and expansion identified by the **National Bureau of Economic Research**.

The ADS index increases during expansions and decreases during recessions. So the more negative the index gets, the weaker the economy is. Starting in mid-2007, the index began a sustained decline. The NBER identified the start of the current recession as December 2007.

The trouble with waiting for NBER to declare a recession is that the announcement typically occurs months after one has begun. The ADS index will tell us at least once a week if business conditions are getting better or worse.

On Friday, when the Labor Department issued the gloomy jobs report, Aruoba and his colleagues revised the ADS with not only the December numbers but also the revised data for October and November. The overall downward trend for the ADS steepened as the index responded to the negative employment statistics.

The ADS will be revised today up to 90 minutes following the release of initial weekly jobless claims and again



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may, at some point, signal the start of better days sooner than our other tracking indicators.

Posted by Mike Armstrong @ 2:30 AM Permalink | Post a comment

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