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FRIDAY, JANUARY 29, 2010 Why wait for GDP numbers when another index will do?

What drives people crazy about the economy are the mixed messages sent by the different statistics in the news every day.

Today, we get the "advance estimate" on how U.S. gross domestic product changed in the fourth quarter. The good news, according to a Bloomberg survey of economists, is that economic output likely rose at a 4.7 percent annualized rate, compared with 2.2 percent in the third quarter.

UPDATE: The Bureau of Economic Analysis reported the economy grew at a 5.7 percent annual rate in the fourth quarter.

Will you feel any better knowing that? GDP is a statistic from 30,000 feet, hard to distinguish for those walking along Main Street, where conditions don't look so good.

One economist who isn't eagerly awaiting the initial read on GDP is S. Boragan Aruoba of the University of Maryland. I first talked with him a year ago after the Federal Reserve Bank of Philadelphia launched the Aruoba-Diebold-Scotti Business Conditions Index, named after its three creators.

The index is built from six indicators: weekly initial jobless claims, quarterly real GDP, and monthly data on payroll employment, industrial production, personal income, and manufacturing and trade sales.

Given his index's use of GDP, I'd wondered if new data would cause a significant shift in the direction of the ADS Index.

Aruoba said it shouldn't, because the index is updated regularly using more frequently issued data. An eye-popping GDP number should not swing the ADS Index one way or another because critical employment and industrial production data are already baked into it.

"I'm personally not dying to hear what the number is going to be," he said. "If I trust the index, it won't give me much more information than I already have."

In January 2009, the ADS Index was showing a plunge in business conditions that had not been seen since 1980. After that, the index began a rapid ascent, reaching positive territory during July. Its trend line supports the widespread belief by economists that the recession ended at some point between June and August.

And that's what makes the ADS Index so useful. At a glance, you can see if conditions are decelerating, accelerating or stuck in neutral.

Unfortunately, the ADS Index lately has meandered around its zero line, meaning we're stuck in neutral.

Posted by Mike Armstrong @ 12:20 PM Permalink | Post a comment

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