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2006 - What Are the Most Market Moving Economic Indicators for the U.S. Dollar?

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Non-farm payrolls use to be the most market moving economic indicator for the US dollar, but this is no longer true. Back in April of 2005, we published a report using 2004 data that ranked non-farm payrolls as the single piece of economic data that caused the biggest average daily movement for the US dollar during that year. We have now updated the analysis by looking at the impact of economic data on currency prices between June 2005 and June 2006. The latest report indicates that the ISM or Institute of Supply Management's index of manufacturing sentiment actually surpassed the non-farm payrolls as the market moving indicator for the US dollar over the past 12 months. The changes that we have seen in the rankings are primarily due to the shifts in the economic cycle, changes to major market themes and the Federal Reserve's greater emphasis on inflation. Regardless of whether you are a fundamental or a technical trader, knowing which economic data can cause the biggest shifts in the markets is extremely important. Depending upon your specific trading strategy, it will help you to decide when to be in the markets and when to stay out.

Shifting Importance of Fundamental Data over Time

With the US dollar representing the other side of 90 percent of all currency transactions, US economic data is hands down the most important releases to watch. In our study, we attempt to further narrow this down to the select few that can cause the biggest movements by looking at various time frames to gage both the knee-jerk and slightly more settled reaction. Starting with the knee-jerk reaction in the first 20 minutes of trading, unemployment and the Federal Reserve's interest rate decision still win out. However, going down the rankings, we see that the trade balance, inflation and retail sales have become much more important while the report on foreign purchases of US Treasuries has slipped from the third most market moving to the sixth. The Federal Reserve's persistent interest rate hikes along with the rapid increases in oil and gold prices has pushed concerns about funding for the US' current account and trade balances to the back burner. Between June 2005 and June 2006 alone, oil prices have increased to a high of 50 percent while the price of gold was up 73 percent at its highest point during the 12 months. Therefore it is no wonder that inflation has shot up in significance. As overnight lending rates reach higher and higher, market participants are more prone to use price growth (the Fed's primary issue when determining monetary policy) to analyze how long the steady diet of 25 basis points can last.

	Top Indicators As Of 2006 (20-Minutes)		Top Indicators As Of 2004 (20-Minutes)
1	Non-Farm Payrolls	1	Non-Farm Payrolls
2	Interest Rates (FOMC)	2	Interest Rates (FOMC)
3	Trade Balance	3	Foreign Purchases Of US Treasuries (TIC)
4	Inflation (CPI)	4	Trade Balance
5	Retail Sales	5	Current Account
6	Foreign Purchases of US Treasuries (TIC)	6	Durable Goods
7	ISM Manufacturing	7	Retail Sales
8	Producer Price Index	8	Inflation (CPI)
9	Personal Consumption	9	GDP

For this updated version of the Most Market Moving Indicators, we decided to include the 60-minute range. This time frame enjoys the split advantage of still reflecting the market's initial response, but also covers more of the developing trend. Unsurprisingly, many of the indicators from the 20-minute list make this list as well, proving that their knee-jerk reaction is often a catalyst for a longer move rather than just a simple readjustment. The only major change that we see is the flipped position of the trade balance and FOMC rate decision.

	Top Indicators As Of 2005 (60-Minutes)
1	Non-Farm Payrolls
2	Trade Balance
3	Interest Rates (FOMC)
4	Inflation (CPI)
5	ISM Manufacturing
6	Empire Index
7	Durable Goods
8	Retail Sales
9	Producer Price Index

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Where ISM Wins Out

Now we move onto the full, daily range which measures an indicator's ability to truly spark shifts in market sentiment or otherwise key off the beginning of new trends. Not surprisingly, many of the same indicators that have held the upper echelons of the Top Market Movers' list in 2004, remain there today. Non-farm payrolls and the trade balance are two indicators that have survived the upset. However, there are a few surprises for the most current data, the most remarkable of which was the rise of ISM manufacturing to the top spot. This development can be explained in a few ways. The ISM tends be released on the first business day of each month, which allows it to be interpreted as a leading indicator for non-farm payrolls. The ISM report contains two key subcomponents that shed more light on how the data for the rest of the month will be released. The headline ISM manufacturing number is accompanied by the components - prices paid and employment. With independent employment and inflation reads continuously ranking in the top nine, the advanced release is basically a spring board for setting up expectations for the official releases due later in the month. The prices paid indicator in particular has garnered a healthy amount of attention. The employment component is used to forecast payrolls which are released a few days later while the prices paid component is used to forecast the consumer and producer price indexes along with the Federal Reserve's rate decision.

	Top Indicators As Of 2006 (Daily)		Top Indicators As Of 2004 (Daily)
1	ISM Manufacturing	1	Unemployment (NFPs)
2	Non-Farm Payrolls	2	Interest Rates (FOMC)
3	Trade Balance	3	Foreign Purchases of US Treasuries (TIC)
4	Personal Consumption	4	Trade Balance
5	Inflation (CPI)	5	Current Account
6	Empire Index	6	Durable Goods
7	GDP	7	Retail Sales
8	Philadelphia Fed Index	8	Inflation (CPI)
9	Foreign Purchases of US Treasuries (TIC)	9	GDP

Why Some Releases Do Not Make the List

There are many indicators that do not make the list even though traders think that they should. Industrial Production and the University of Michigan Consumer Confidence surveys are good examples. These indicators are usually released on days with many competing economic releases. Over the past 12 months, at least one indicator was released at the same time as industrial production every single month. As a result, the actual release holds less significance.

Decreasing Market Volatility

One final reason for the changes in rankings is the comparatively smaller daily trading range for the EUR/USD between June 2005 and 2006. In 2004, the average daily range for the EUR/USD was 111 pips. This has dropped to 104 pips over the past 12 months. Though the decline may seem small, it is more prominently reflected on those days when releases are due. When non-farm payrolls were at the head of the list in 2004, the average daily move of the EUR/USD on the back of the release was 193 pips. This compares to the 130 pip daily range for the ISM index, which tops this year's list. Contracting interest rate differentials around the world has also contracted market volatility.

	Top Indicators As Of 2006 (Daily)	Avg. Range (pips)	Top Indicators As Of 2004 (Daily)	Avg. Range (pips)
1	ISM Manufacturing	130	Non-Farm Payrolls	193
2	Non-Farm Payrolls	115	FOMC Decision	140
3	Trade Balance	114	TICS	132
4	Personal Consumption	112	Trade Balance	129
5	Inflation (CPI)	109	Current Account	127
6	Empire Index	109	Durable Goods	126
7	GDP	108	Retail Sales	125
8	Philadelphia Fed Index	107	Inflation - CPI	123
9	TICS	106	GDP	110

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Conclusion

As the world changes, so has the importance of different economic data on the US dollar. While technical trading generally dominates the market scene, fundamentals are just as important and as we have seen can also yield a significant influence over the behavior of currencies. Some traders will choose to trade news flow while others who adopt range trading strategies are smart enough to know when to avoid them. Our study suggests that not only should those traders watch the non-farm payrolls report closely, but also the ISM report going forward.

Resources:

Macroeconomic Implications of the Beliefs and Behavior of Foreign Exchange Traders:
http://www.georgetown.edu/faculty/evansm1/New%20Micro/chinn.pdf