

# The Allianz Economic Indicator: A leading indicator of global growth momentum

The Allianz Indicator condenses a host of different trends into one overall index (hard indicators: crude oil price, retail sales, production figures; monetary indicators: stock index, real exchange rate, yields; soft indicators: consumer confidence, purchasing managers' index). This provides pointers to global economic momentum. Regional indices for the USA, the euro area and Japan as well as hard, monetary and soft sub-indices increase the informative value of the Allianz World Indicator.

## AUTHOR:

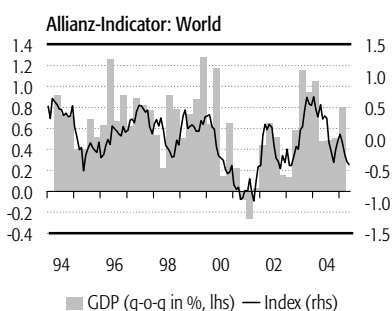
DR. HARALD JÖRG  
Tel.: +49.69.2 63-199 13  
harald.joerg@dresdner-bank.com

## SLOWING GLOBAL MOMENTUM – THE CURRENT

### DEVELOPMENT IN THE ALLIANZ ECONOMIC INDICATOR

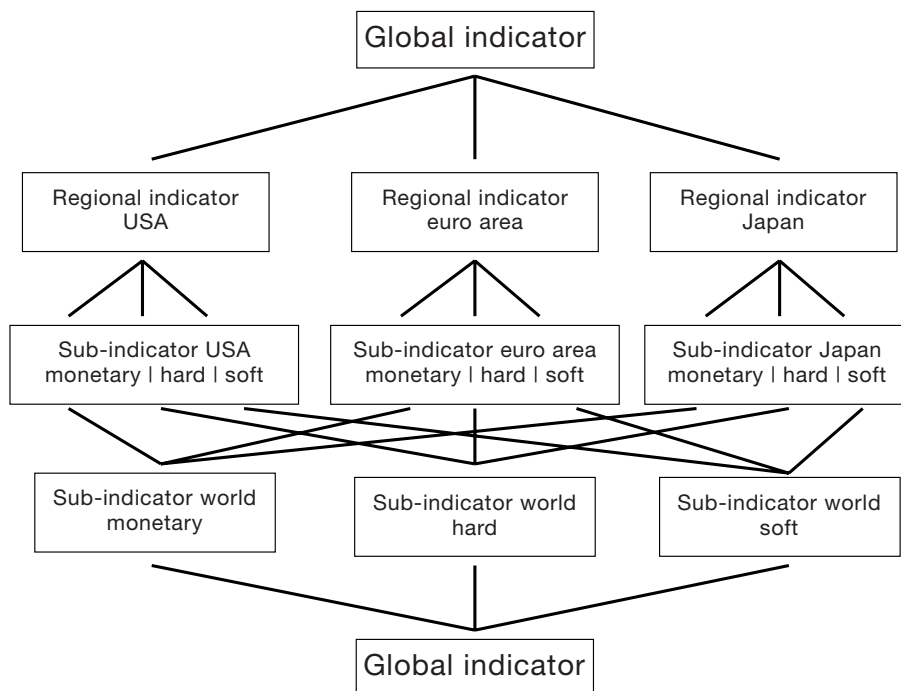
The Allianz Indicator started to rise in 2002 and reached a peak in January 2004, since when it has trended weaker. This has been accompanied by a slowing in the pace of global economic expansion. Having gained around 1 % quarter-on-quarter in the second half of 2003 and the first quarter of 2004, the pace of growth in the three economic regions roughly halved in the remaining three quarters of last year. The Allianz Indicator correctly forecast this slowdown in the course of 2004.

The indicator then stabilized at the end of 2004/beginning of 2005, only to return to its downward path as from February 2005. This development strongly suggests that, following higher growth in the first quarter of 2005, the second quarter will see a substantial slowdown.



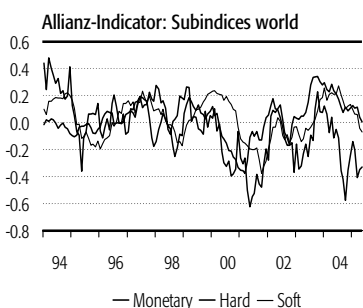
### COMPOSITION OF THE ALLIANZ ECONOMIC INDICATOR

The global Allianz Economic Indicator comprises regional indices for the USA, the euro area and Japan. The regional indices are in turn broken down into hard, monetary and soft sub-indices. From the sub-indices hard (accordingly: monetary, soft) for the USA, the euro area and Japan we arrive at the global sub-index hard (accordingly: monetary, soft). The global sub-indices hard, monetary and soft in turn provide the global economic indicator (on composition and calculation see chart below and pages 24 and 25).



### DEVELOPMENT IN THE GLOBAL SUB-INDICES

The decline in the global economic indicator since early 2004 stems from all global sub-indices. The monetary environment, for example, has relentlessly continued to cloud over, due mainly to the reversal in the US Federal Reserve’s interest rate stance mid-2004. A similar picture to the monetary global sub-index is also painted by the indicators of sentiment (soft global sub-index). Particularly pronounced was the deterioration in the hard global sub-index from July to October 2004, driven primarily by the sharp jump in crude oil prices during that period. The economic steadying depicted in the global index end-2004/early 2005 is due exclusively to a temporary recovery in the hard sub-index.



Development in the regional sub-indices since the beginning of 2005 is rather varied. Subdued growth expectations in the euro area can be attributed to a collapse in the soft regional sub-index, with a continued negative trend in the hard indicator. The monetary euro area sub-index, on the other hand, signals conditions still slightly more conducive to growth than in America and Japan. Stateside, the hard and soft regional sub-index have deteriorated significantly in recent months. In Japan, however, the mood is still one of optimism, in comparison to the two other regions – something of a surprise given the negative readings in the hard regional sub-index.

**LEADING INDICATOR: WORLD**

	monetary	hard	soft	total
Jan 04	0.3	0.4	0.5	0.4
Feb 04	0.3	0.3	0.0	0.2
Mar 04	0.5	-0.5	0.2	0.0
Apr 04	0.6	0.2	0.4	0.4
May 04	0.6	-0.2	0.6	0.2
Jun 04	0.6	-0.1	0.5	0.3
Jul 04	0.5	0.0	0.9	0.4
Aug 04	0.3	-0.7	0.5	0.0
Sep 04	0.2	-0.8	0.3	-0.2
Oct 04	0.2	-0.7	0.1	-0.2
Nov 04	0.1	-0.8	0.2	-0.3
Dec 04	0.1	-0.9	0.1	-0.3
Jan 05	0.3	-0.1	0.2	0.1
Feb 05	0.3	-0.7	0.1	-0.2
Mar 05	0.4	-1.1	-0.1	-0.3
Apr 05	0.3	-0.9	-0.6	-0.4
May 05	0.1	-0.8	-0.5	-0.4

**LEADING INDICATOR: USA**

	monetary	hard	soft	total
Jan 04	1.5	0.1	1.8	0.9
Feb 04	1.4	0.2	1.1	0.8
Mar 04	1.2	0.3	1.2	0.8
Apr 04	1.3	0.2	1.1	0.7
May 04	1.2	0.1	0.9	0.6
Jun 04	1.0	0.0	1.0	0.5
Jul 04	0.8	-0.2	1.2	0.4
Aug 04	0.6	-0.8	0.8	-0.1
Sep 04	0.6	-1.0	0.8	-0.2
Oct 04	0.6	-1.3	0.4	-0.4
Nov 04	0.5	-0.6	0.5	0.0
Dec 04	0.6	-0.2	0.7	0.2
Jan 05	0.6	-0.2	0.4	0.1
Feb 05	0.4	0.0	0.2	0.2
Mar 05	0.4	-0.8	0.1	-0.2
Apr 05	0.1	-0.5	-0.4	-0.3
May 05	0.0	-0.6	-0.7	-0.4

**LEADING INDICATOR: EMU**

	monetary	hard	soft	total
Jan 04	0.8	0.3	1.2	0.6
Feb 04	0.2	-0.2	1.2	0.2
Mar 04	0.1	-0.8	1.6	-0.1
Apr 04	0.6	-0.2	1.6	0.4
May 04	0.0	-0.8	1.5	-0.1
Jun 04	0.1	-0.4	1.5	0.2
Jul 04	0.2	-0.5	1.7	0.2
Aug 04	-0.1	-0.7	1.6	-0.1
Sep 04	-0.5	-0.8	1.3	-0.2
Oct 04	0.0	-1.5	1.1	-0.6
Nov 04	-0.1	-1.0	1.2	-0.3
Dec 04	-0.1	-0.8	1.1	-0.2
Jan 05	0.3	-0.6	0.8	-0.1
Feb 05	0.2	-1.1	0.8	-0.4
Mar 05	0.3	-0.9	1.1	-0.2
Apr 05	-0.1	-1.2	0.8	-0.5
May 05	-0.2	-0.8	0.8	-0.3

**LEADING INDICATOR: JAPAN**

	monetary	hard	soft	total
Jan 04	0.3	0.1	0.3	0.7
Feb 04	0.2	0.1	0.2	0.5
Mar 04	0.2	-0.1	0.2	0.3
Apr 04	0.3	0.0	0.2	0.5
May 04	0.2	-0.1	0.2	0.3
Jun 04	0.2	-0.1	0.2	0.4
Jul 04	0.2	-0.1	0.3	0.3
Aug 04	0.1	-0.4	0.2	-0.1
Sep 04	0.1	-0.4	0.2	-0.2
Oct 04	0.1	-0.6	0.1	-0.4
Nov 04	0.1	-0.4	0.1	-0.2
Dec 04	0.1	-0.2	0.1	0.0
Jan 05	0.1	-0.1	0.1	0.1
Feb 05	0.1	-0.2	0.1	0.0
Mar 05	0.1	-0.4	0.1	-0.3
Apr 05	0.0	-0.3	0.0	-0.4
May 05	0.0	-0.3	-0.1	-0.4

To sum up, world economic activity will probably slow in the second quarter of 2005 – in all three economic areas. That said, we still expect global economic growth to continue edging upward in the second three months of this year. In the euro area the monetary conditions are stable and in Japan the mood remains upbeat. However, should the economic indicators remain mired at this reduced level in the months ahead, the prospect of an acceleration in the economy in the second half of 2005 will become increasingly unlikely.

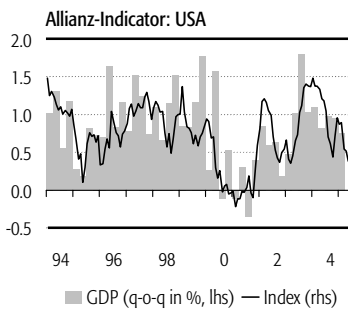
**WHY AN INDICATOR OF GLOBAL GROWTH MOMENTUM?**

It is vital that all economic decisions be underpinned by authoritative economic analysis examining both the current situation of the economy and its likely development. For this a broader picture is necessary, looking beyond one's own country to international developments. Crucial are economic indicators delivering valuable pointers on macroeconomic trends, mostly *ex ante*. Things become confusing, however, when individual indicators send out different messages, as is generally the case at economic turning points. In this situation it is helpful to condense the information into one single indicator modeling the fundamental direction of economic development.

But in the process of condensing economic indicators into one single indicator important information for the economic interpretation of further cyclical development (shown by the indicator) is lost. If, for instance, indicators of sentiment and/or monetary time series cause the condensed overall index to rise, while suggesting that the preconditions for an economic upswing are brightening, this does not necessarily mean that the rebound will actually take place. The more hard time series on the real side of the economy that deliver evidence of an upswing, the more justified we are in speaking of it. An additional breakdown of the overall indicator into suitable sub-indices therefore increases the informative content.

## THE ALLIANZ INDICATOR MEASURES ECONOMIC MOMENTUM

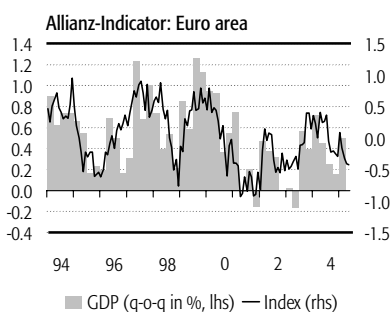
The Allianz Group and Dresdner Bank global economic indicator seeks to satisfy the above requirements, serving to capture early on changes in economic development in the major economic areas USA, euro area and Japan. Aggregated across these three economic areas, it also provides an indication of global economic momentum. With the aggregation method it is also possible to divide the overall indicator into sub-indices.



For measuring economic activity at the macro level, macroeconomic output is the suitable variable. The Allianz Economic Indicator therefore takes as its reference time series the seasonally adjusted rate of change in real gross domestic product quarter-on-quarter. The indicator is calculated monthly, thus already providing pointers to the economic dynamic within a quarter.

Diagnosing quarterly changes is far more difficult than estimating year-on-year changes. The former are extremely volatile, whereas the latter contain information already known, namely the data from several quarters previously published. However, the customary practice of basing economic indicators on reference variables compared year-on-year suggests an accuracy in analysis that does not exist. Of course the adjustment quality suffers in an approach showing quarterly change. But it is the more appropriate method in early economic diagnosis.

The indicator is comprised of three regional indices. By taking the euro area, the US and Japan it depicts 67 % of the entire world economy. In turn, the regional indices are construed from the sub-indices “hard” (real economic time series), “monetary” (financial time series) and “soft” (corporate and household surveys). Values in the overall indicator higher than zero are consistent with a rate of expansion above the respective past ten-year trend.



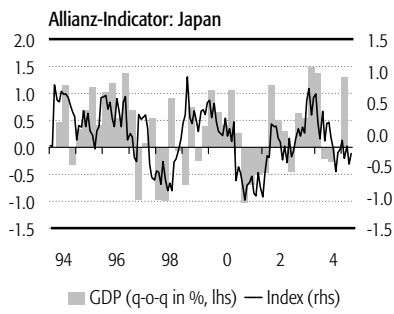
As a rule the sub-indices are formed from the following indicators:

Sub-index hard: production indices  
new orders  
retail sales  
crude oil price

Sub-index monetary: three month money  
10-year bond yields  
share index  
real exchange rate

Sub-index soft: corporate survey indices (e.g. Purchasing Managers' Index)  
consumer confidence

To form the sub- and regional indices the trending time series are trend-adjusted and all time series subsequently subjected to a suitable standardization method. Aggregation to the relevant sub- and regional indices is made as the arithmetic mean.



The global indicator is composed of the weighted average of the three regional indices (euro area, USA and Japan). The shares of real gross domestic product in the three regions in 2003 prices and US dollars serve as the weights. This regional subdivision of the global indicator is complemented by a weighted concentration of the relevant sub-indices from the regions into monetary, hard and soft global sub-indices.