Chief economist's comment

Was 2019 better than we think?

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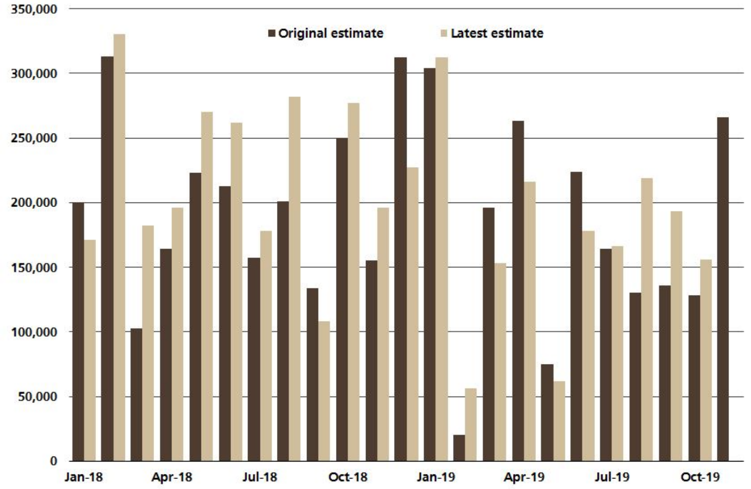
- Economic data is revised more and more often. Revisions to data are larger and larger. Structural changes make data less and less reliable.
- Markets tend to ignore data revisions, and focus on the next new (unreliable) number. But data revisions can be biased in one direction.
- In the US, data revisions have been neutral for most of this year. Data has tended to be revised higher recently. Data that markets tend to focus on is more likely to be revised up.
- In 2019 Germany saw positive revisions to a lot of its important data. The German economy was not as bad as markets might think.

Economic structural change create problems with economic data. Investors want precise numbers, but economic numbers are never precise. And when the world is changing significantly, precision is less and less likely.

Economic data is revised all the time. However, investors are always keen to find out what happens next. Revisions to past data are often forgotten in the rush to uncover the future. The risk is that markets end up with a false idea of what has actually happened.

The key US employment data is nearly always revised up
Change in US non-farm payrolls - original estimate/latest estimate

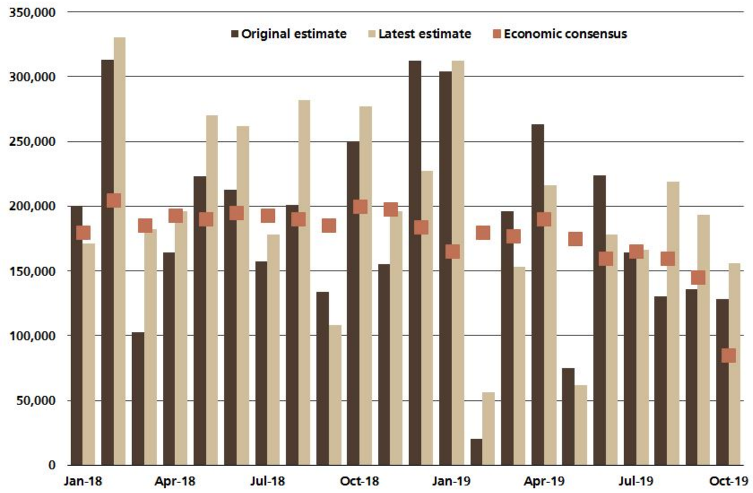


Source: Bloomberg, Haver, UBS - the most recent months will, of course, continue to be revised

The US employment report is one of the most closely watched statistics in financial markets. As the previous chart shows, you should watch for quite a while before deciding what has happened. Revisions to payrolls have averaged over forty-one thousand since the start of 2018. Nearly three-quarters of the revisions have been positive.

The creates an interesting problem for economists in financial markets. Should economists forecast what they believe to be correct? Or should economists try to forecast the incorrect initial number that the financial markets will react to? The following chart shows that economists are (just about) closer to the "true" payrolls number than the initial estimate on average. For example what seemed like a big underestimation in June this year turned out to be almost exactly right.

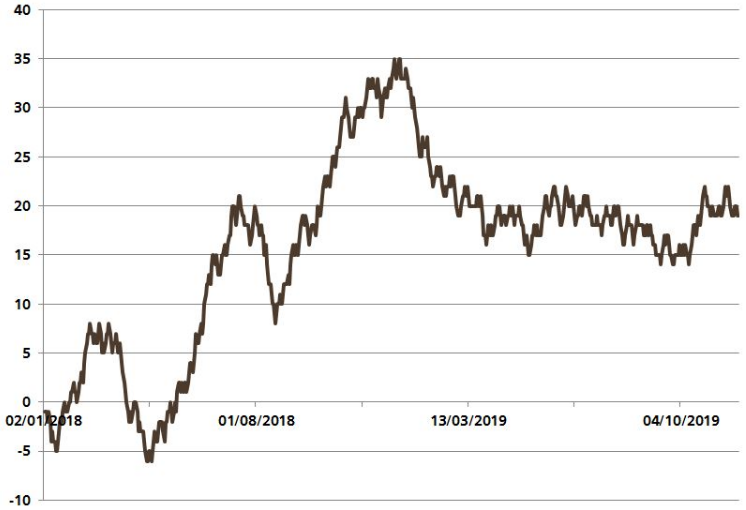
Economists tended to be closer to reality than the initial data release
Change in US non-farm payrolls: initial release; initial consensus; latest number



Source: Bloomberg, Haver, UBS

We can see the trend of revisions across a wider range of data releases by looking at a "revise index". This works the same way an economic "surprise" index does. If a key data release from the past is revised in an economically positive way, the index goes up one. If a key data release from the past is revised in an economically negative way, the index goes down one. The level of the index is not important – in fact it is an irrelevant number. It is the direction the index is trending that matters. A rising index means that data is repeatedly being revised higher after publication. A falling index means data is repeatedly being revised lower.

US growth revisions: limited, with recent positive bias
US growth revise index: positive economic revisions increase the index 1 point, negative reduce the index 1 point

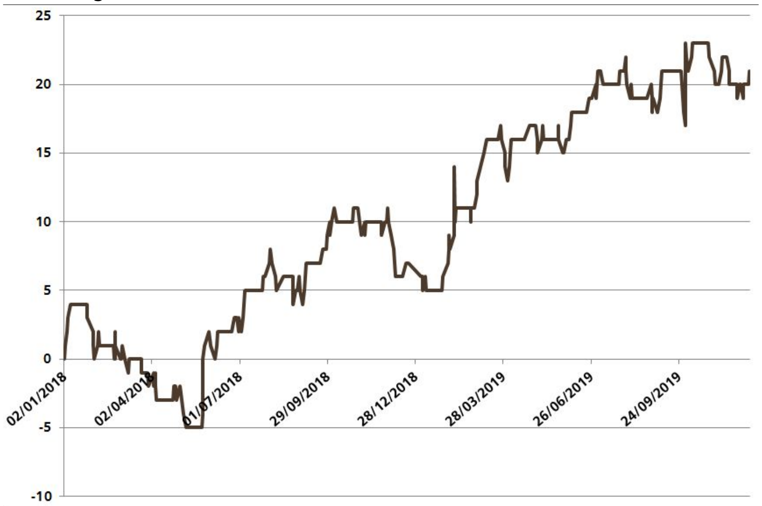


Source: Bloomberg, UBS calculations. The index looks at the same growth indicators used in the UBS growth surprise index – with the exception of initial jobless claims, which are excluded here. Initial jobless claims are *always* revised higher as late claims are incorporated into the data. The revise index only looks at the *first* revision to the data – some economic data is of course revised well beyond the life span of any economist.

US growth data has tended to be revised higher since October, after a long period when upward and downward revisions were fairly evenly balanced. This is not the dramatic bias of 2018, when data was continually being revised higher, but there has been a slightly better history than first assumed.

If data revisions mean that Americans have reason to be slightly more cheerful, the Germans have reason to be dancing in the streets. (They probably won't – as Germans, like everyone, else tend to ignore data revisions.)

Things are better than first thought in the German economy
German growth revise index



Source: Bloomberg, UBS calculations

There are fewer German growth details published than in the United States. This does mean that sentiment data has more of an influence over the German revise index. In Germany, there are proportionately more sentiment numbers relative to proper economic data than is the case in the United States. Nonetheless there as been a strong trend to revising past data higher. Remember, the level of the index is irrelevant – it is the direction that matters. Germans seem to be biased towards being pessimistic when first reporting their numbers. The public relations problem for Germany is that first impressions do seem to last in the minds of investors.

France and the Netherlands has been more stable in their revisions than Germany in recent months. Spain looks more like Germany, with a trend of positive revisions. In Spain's case these seem quite focused in the consumer sector. Twenty out of twenty two retail sales numbers have been revised higher since the start of 2018.

Investors in financial markets are inevitably forward looking. The interest is on what can be earned in the future, not what has happened in the past. However, the tendency to revise economic data significantly may mean that investors who only look ahead have a misunderstanding of the health of a specific economy. Every once in a while it is worth pausing to consider what really happened, not what you think happened.

Appendix

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