

PART TWO

The shortcomings of new orders as cyclical indicators are also substantial, however. Their leads are far from uniform in length and often rather short. The "extra" cycles in ordering are interesting and on the whole explicable phenomena, but as a general rule the closer the specific cycles of an indicator series come to having a one-to-one correspondence with business cycles, the more useful is the series. More than anything else, the presence in the new order data of relatively large and frequent "irregular" movements constitutes a major limitation on the use of these series for forecasting or identifying business cycle turns.

It is not difficult to conceive of various ways of reducing these deficiencies. A forecasting index of new orders might be planned to include series selected for good records of conformity, timing, and smoothness. It is preferable, however, to base selection not merely on the empirical records but also on the considerations that explain them. In this study much attention has been given to such considerations. Once series have been rated, on the strength of their actual or expected records, those that are judged better may be given larger weights. Improved performance of the composite index should then result from the strengthening of the part played by the more consistent and early leaders among the new order data.

Beyond other more conventional techniques of index construction, diffusion measurements are promising. The established empirical rule that diffusion indexes lead the corresponding aggregates was shown to apply to new orders. Being based on series that themselves have a strong tendency to move ahead of the ebb and flow of general business, diffusion indexes of new orders are therefore especially early indicators of cyclical revivals and recessions. Various devices, such as cumulation, weighted graduation, and averaging the duration of movements in the series used for diffusion measurements, are available to reduce irregularities with a minimum loss in timeliness.

But any such improvements should be supplemented by efforts to make the workable data available more promptly. What is needed primarily is reliable aggregative estimates of new orders divided into a larger number of industry series than that provided in the present breakdown of government statistics.