

Top-Down Analysis

Top-down analysis is a form of analysis that starts at and focuses on broad economic factors such as gross domestic product (GDP) or interest rates. It is driven by the belief that nothing affects security prices (especially in the short run) more profoundly than the economy and other top-down-type characteristics.

In a pure top-down analysis approach, the investor starts by analyzing and forecasting macroeconomic variables such as GDP and inflation. The investor then systematically moves to more specific variables. The output from the earlier stages is used as input in the later stages.

If the investor has done his or her job properly, when it comes time to decide which individual securities to buy, the decision should be simple and obvious. The investor should buy those securities that will give them the greatest exposure to the factors they believe will be favorable.