John Williams'

Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 837
August Trade Deficit, Construction Spending, Fed Policy

October 6, 2016

With Contracting Monthly, Quarterly and Annual Activity,
Real Construction Spending Remained Down by 25% (-25%) from
Recovering Its Pre-Recession Peak

Weakest Real Construction Spending Growth since Series Trough in 2011

Widening of August Trade Deficit Was Due to Shrinking Services Surplus,
Reflecting Payments for Importing Rio Olympics Intellectual Property

With Second-Quarter Real Merchandise Trade Deficit Worst Since 2007,
Temporary Soybean Export Explosion Has Narrowed Third-Quarter Deficit

Central Bank Intervention Appeared to Drive October 4th Gold Selling.
Is a Policy Shift Pending?

PLEASE NOTE: The next regular Commentary, *scheduled for Friday, October 7th will cover the September employment and unemployment numbers and the ShadowStats Ongoing Money Supply M3.*

Best wishes to all — John Williams

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OPENING COMMENTS AND EXECUTIVE SUMMARY

Why Are the Central Banks Hitting Gold Prices? Massive one-shot selling of non-physical gold on Tuesday, October 4th, appeared to be typical of gold-price-depressing market interventions seen repeatedly in recent years. Those interventions have been orchestrated regularly by central banks. Such market manipulations normally would be of concern to regulators, unless the regulators were complicit in the nefarious activity.

Most recently, the U.S. Federal Reserve has been using threats of raising rates—continual jawboning of pending rate hikes—to support the U.S. dollar and to keep gold prices down. Traditionally, the Fed and other central banks view rising gold prices as a signal from the markets that the central bankers are not doing their jobs. Orchestrated jawboning continues, but it may have run its course as a primary policy tool, with central-bank credibility near an all-time low. Post-election, the Fed likely will face economic and liquidity circumstance more conducive to expanded quantitative easing, than to meaningful rate hikes. Reverting now to obvious market manipulation of the price of gold could be a leading indicator of pending central-bank policy otherwise shifting towards intensified U.S. dollar debasement.

Holding physical gold and silver remains the primary hedge in preserving the purchasing power and liquidity of one's wealth and assets in the difficult times ahead. The hedge needs to be held into and through the crisis, in order to provide its full benefit.

A Continuing Recession Signal from the Private Sector. Ongoing monthly economic-reporting details for key series, public and private, increasingly confirm the patterns of declining or collapsing economic activity. For example, consider The Conference Board Help Wanted OnLine® Advertising, which has been generating an ongoing signal for economic downturn. Published yesterday, on October 6th, details of the September 2016 help-wanted online advertising are available here: The Conference Board Help Wanted OnLine®. A review of those numbers shows that the year-to-year declines in the monthly data continue unabated, versus the observations detailed in the *Commentary No. 820* discussion. Historically, such activity has been among the best leading indicators of an unfolding recession. Other indicators will be reviewed in tomorrow's *Commentary No. 838* of October 7th.

Today's *Commentary* (October 6th). These *Opening Comments* cover the summary of the August 2016 releases for the monthly trade deficit and construction spending.

The *Week and Month Ahead* updates the previews of Friday's employment and unemployment reporting.

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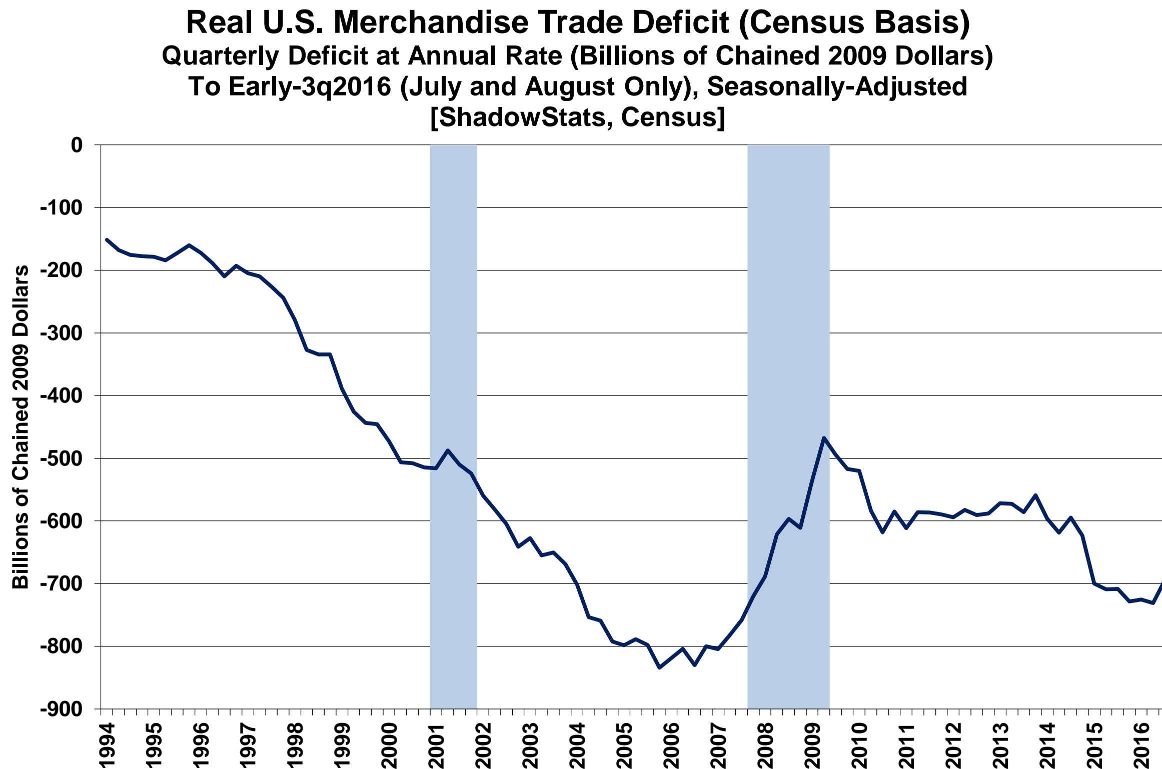
U.S. Trade Deficit—August 2016—Mixed Pressures from Soybeans and the Rio Olympics. In the last three years, the nominal trade surplus has not varied by more than $1 billion month-to-month, except in August 2016. That regular stability is due to the services series being largely assumed and modeled with a guessed-at surplus of about $20 billion (plus-or-minus) being used as plug number in narrowing the headline deficit in the goods number. Given the lack of variability in the services surplus, the real merchandise trade deficit generally has been good surrogate for estimating the quarterly change in real net exports, which can dominate headline GDP growth, most-usually on the downside. Those roles were reversed in August 2016.

The services surplus balance took a one-time hit of $1.2 billion in August 2016, reflecting the payment of U.S. interests for the use of intellectual property (broadcast rights) of the Rio Olympics.

On the goods-side, the incredible, but temporary surge in U.S. soybean exports from the more-common monthly level of $1.6 billion in June, to $5.2 billion in July, continued at $5.2 billion in August. Without the temporary spike, or otherwise miserably-inadequate seasonal adjustments, the third-quarter trade balance would be wider up by 5.2%, rather than narrower by 3.8% (-3.8%). The difference there otherwise would have consensus estimates looking at a possible contraction in real third-quarter 2016 GDP growth (to be published on October 28th, less than two weeks before the election on November 8th), instead of quarterly GDP growth somewhere in excess of two-percent.

Graph 1: Inflation-Adjusted, Quarterly U.S. Merchandise Trade Deficit through Early 3q2016 (July and August)



Shown in *Graph 1*, the second-quarter 2016 real merchandise trade deficit held at its worst reading since third-quarter 2007 (although such never surfaced in the headline second-quarter 2016 GDP reporting,

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discussed in *Commentary No. 836*). Yet, the unusual and continuing surge in July and August 2016 exports of soybeans continue to give the initial trend in the real third-quarter 2016 merchandise trade deficit, a positive but still likely short-lived boost. Any negative revision to the GDP's third-quarter estimate from the August trade data was due to Rio, and was not reflected in the real merchandise trade deficit shown in *Graph 1*.

Nominal (Not-Adjusted-for-Inflation) August 2016 Trade Deficit. The headline August 2016 deficit of $40.725 billion widened by $1.178 billion versus a revised $39.547 billion deficit in July 2016. That $1.178 billion deterioration in the headline monthly trade balance reflected a minimal gain of $1.470 billion in monthly exports, more than offset by a $2.647 billion surge in imports (rounding difference). The headline August 2016 deficit also narrowed versus an unrevised $44.639 billion in August 2015. The dominant factors in these unusual numbers were discussed in the prior section. Shifting activity in energy-related products did not have heavy impact in the monthly trade balance changes.

Energy-Related Petroleum Products. From an import standpoint, declining oil prices had bottomed out in February 2016, inching higher by 0.7% in March, gaining 6.5% in April, 16.0% in May, 15.2% in June and 4.2% in July, but they fell by 4.0% (-4.0%) in August 2016. The impact of that August price decline was muted by surging physical oil-import volume in the month.

The not-seasonally-adjusted average price of imported oil declined to $39.38 in August 2016, versus $41.02 in July 2016, and it was down from $49.33 per barrel in August 2015. Separately, not-seasonally-adjusted physical oil-import volume in August 2016 averaged 8.279 million barrels per day, up from 7.277 million in July 2016 and up from 7.080 million in August 2015.

Real (Inflation-Adjusted) August 2016 Trade Deficit. Seasonally-adjusted, and net of oil-price swings and other inflation (2009 chain-weighted dollars, as used in GDP deflation), the August 2016 merchandise trade deficit (no services) narrowed to $57.478 billion, versus a revised July $58.225 billion, and from a $61.443 billion in August 2015.

The August and July numbers followed unrevised real deficits of $64.548 billion in June 2016, $60.892 billion in May 2016, $57.316 billion in April 2016, $56.033 billion in March 2016, $63.607 billion in February 2016 and $61.668 billion in January 2016.

Again, reflected in *Graph 1*, the annualized quarterly real merchandise trade deficit was $623.1 billion for fourth-quarter 2014, $700.0 billion for first-quarter 2015, $709.1 billion for second-quarter 2015, $708.4 billion for third-quarter 2015, $728.6 billion for fourth-quarter 2015, $725.2 billion for first-quarter 2016, and $731.0 billion for second-quarter 2016. That still was the worst quarterly showing since third-quarter 2007, but somehow it never got into headline second-quarter 2016 GDP growth.

That said, the massively distorted July and August 2016 readings have set an early trend for a real third-2016 merchandise trade deficit of $694.2 billion. With the monthly data still in flux, that quarterly trend should shift sharply towards a widening deficit in next month's reporting, and beyond.

Headline deficits likely will get much deeper in the months and quarters ahead, intensifying the ongoing and more-common negative impact on headline GDP.

Construction Spending—August—Real Monthly, Quarterly and Annual Contractions Intensified, with Ongoing Low-Level Stagnation. Where this series remains highly volatile and subject to large monthly revisions, nominal August 2016 spending declined, in the context of a downside revision to headline July and an upside revision to June 2016 activity, with inflation-adjusted real activity in the construction spending series remaining negative, on a monthly, quarterly and annual basis. Real monthly spending declined in August 2016, the third monthly contraction in four months. Second- and third-quarter 2016 real spending indicated quarterly contractions, while year-to-year change in real spending tumbled at ever-deepening annual rates in June, July and August 2016, the first monthly year-to-year contractions since late-2011. The series increasingly has followed a pattern seen when construction spending patterns previously have fallen into deep, recessionary contractions.

Real construction spending generally continued in down-trending, low-level, stagnating non-recovery, with the level of August 2016 still shy of its June 2006 pre-recession peak by 24.6% (-24.6%).

Construction Inflation—ShadowStats Composite Construction Deflator (CCD). Deflation of the Construction Spending series was restructured recently to reflect the ShadowStats Composite Construction Deflator (CCD), as detailed in *Commentary No. 829* and in the *Construction Inflation* section of the *Reporting Detail*.

Accompanying *Graphs 2* to *5* show comparative nominal and real construction activity for the aggregate series, as well as for private residential- and nonresidential-construction and public-construction. Seen after adjustment for inflation, the real aggregate series generally has remained in low-level stagnation, now down-trending into third quarter 2016. Areas of recent relative strength in the major subcomponents generally have flattened out, or turned down, after inflation adjustment, except for private nonresidential spending, which just turned minimally from up-trending to down-trending.

Headline Reporting for August 2016. In the context of a downside revision to July and an upside revision to June activity, the headline, total value of construction put in place in the United States for August 2016 was $1,114.2 billion, on a seasonally-adjusted, but not-inflation-adjusted, annual-rate basis. That estimate was down month-to-month by a statistically-insignificant 0.7% (-0.7%), versus a downwardly-revised $1,150.6 billion in July 2016. Net of prior-period revisions, the headline monthly decline in August 2016 was a still-statistically-insignificant 1.0% (-1.0%).

In turn, July was down by a revised 0.2% (-0.2%), versus an upwardly-revised $1,154.1 billion in June 2016, with June up by a revised 1.1% versus an unrevised $1,143.8 in May.

Adjusted for CCD inflation, total real month-to-month spending in August fell by 1.0% (-1.0%), versus a revised decline of 0.7% (-0.7%) in July 2016 and an unrevised gain of 0.6% in June 2016.

On a year-to-year annual-growth basis, August 2016 nominal construction spending declined by a statistically-insignificant 0.3% (-0.3%), following a downwardly revised annual gain of 1.3% in July 2016, and an upwardly revised gain of 2.1% in June 2016. Net of construction costs indicated by the CCD, the year-to-year change in total real construction spending dropped to a 63-month low of minus 3.3% (-3.3%) in August 2016, versus a deeper, revised decline of 1.6% (-1.6%) in July 2016 and a revised annual decline of 0.5% (-0.5%) in June 2016. The headline annual real decline in August activity was the weakest since the historical series troughed in its collapse into 2011.

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The statistically-insignificant, monthly decline of 0.7% (-0.7%) in aggregate August 2016 construction spending, versus a decline of 0.2% (-0.2%) in July 2016, included a headline monthly drop in August of 2.0% (-2.0%), versus a monthly plunge of 3.5% (-3.5%) in July public spending. Private spending declined by 0.3% (-0.3%) in August having gained 0.8% month-to-month in July. Within total private construction spending, residential-sector activity also fell by 0.3% (-0.3%) in August, having gained 0.5% in July, while the nonresidential sector fell by 0.4% (-0.4%) in August, in the context of revising sharply lower to a 1.0% monthly gain in July.

Quarterly Trends. Reflecting headline August 2016 reporting in the context of the revisions to June and July 2016 headline detail, second-quarter 2016 real construction still plunged quarter-to-quarter, with an early trend towards contraction intensifying into third-quarter activity.

With all spending revisions and the latest inflation estimates in hand, first-quarter 2016 real construction spending rose at an unrevised annualized pace of 7.3%. Second-quarter 2016 showed an unrevised real contraction of 8.5% (-8.5%). Based on reporting just for July and August 2016, the early trend for third-quarter 2016 activity was a quarterly contraction of 2.7% (-2.7%). Previously, based solely on the initial July 2016 estimate, the early third-quarter trend had been for a real, annualized quarterly contraction of 2.0% (-2.0%).

Going back into last year, fourth-quarter 2015 real construction spending contracted at an annualized pace 5.4% (-5.4%), following annualized quarterly real gains of 10.1% in third-quarter 2015, 26.0% in second-quarter 2015 and 5.3% in first-quarter 2015.

Construction Spending Graphs. Despite protracted and variable stagnation in broad activity, the pattern of inflation-adjusted activity here—net of inflation estimates—does not confirm the economic recovery suggested by the headline GDP or employment series, as discussed in the *Reporting Detail*.

To the contrary, the latest broad construction reporting in real terms generally shows a pattern of low-level stagnation, where activity never recovered pre-recession highs, and where the pattern of stagnation has begun to turn down anew. Only the private, nonresidential sector had shown a recovery to pre-recession highs in nominal terms, only in the headline July 2016 detail, while the stagnating, related real series there—the only one up-trending in July—turned down in August 2016 (see *Graph 4*).

A variety of construction spending and related, comparative graphs (*Graphs 6* to *14*) are found in the *Reporting Detail* section. *Graphs 2* to *5*, which follow here, show plots of the comparative construction series both before and after adjustment for inflation.

[Graphs 2 to 5 begin on the next page.]

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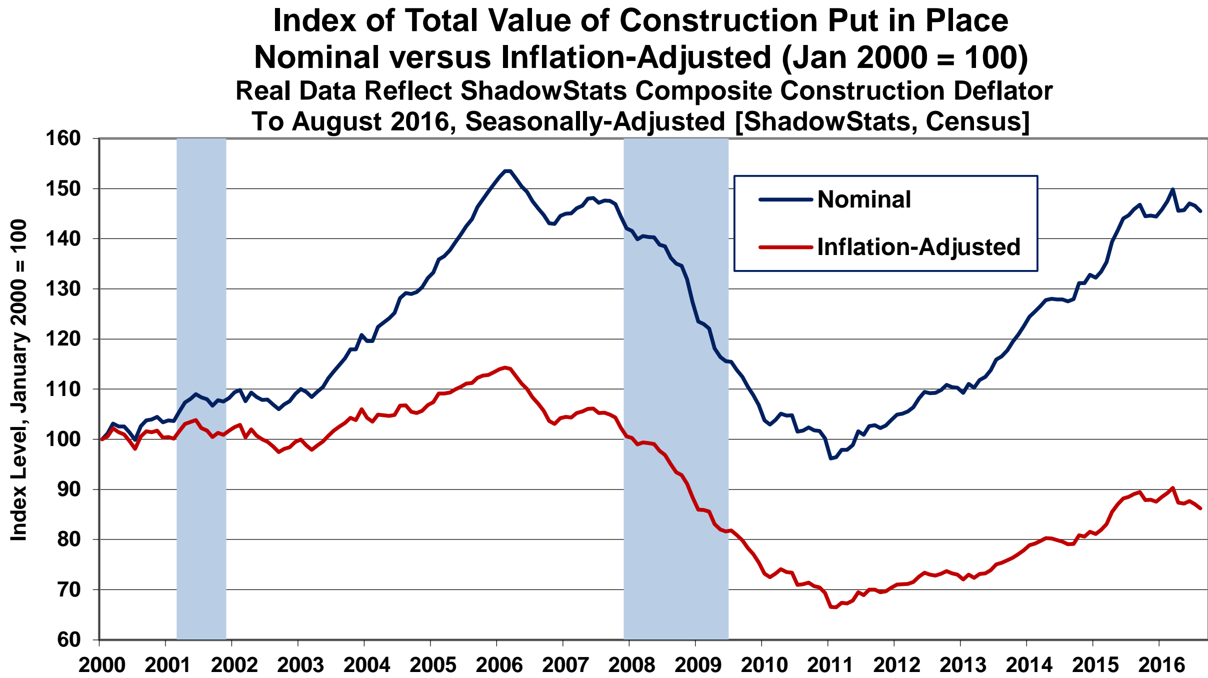
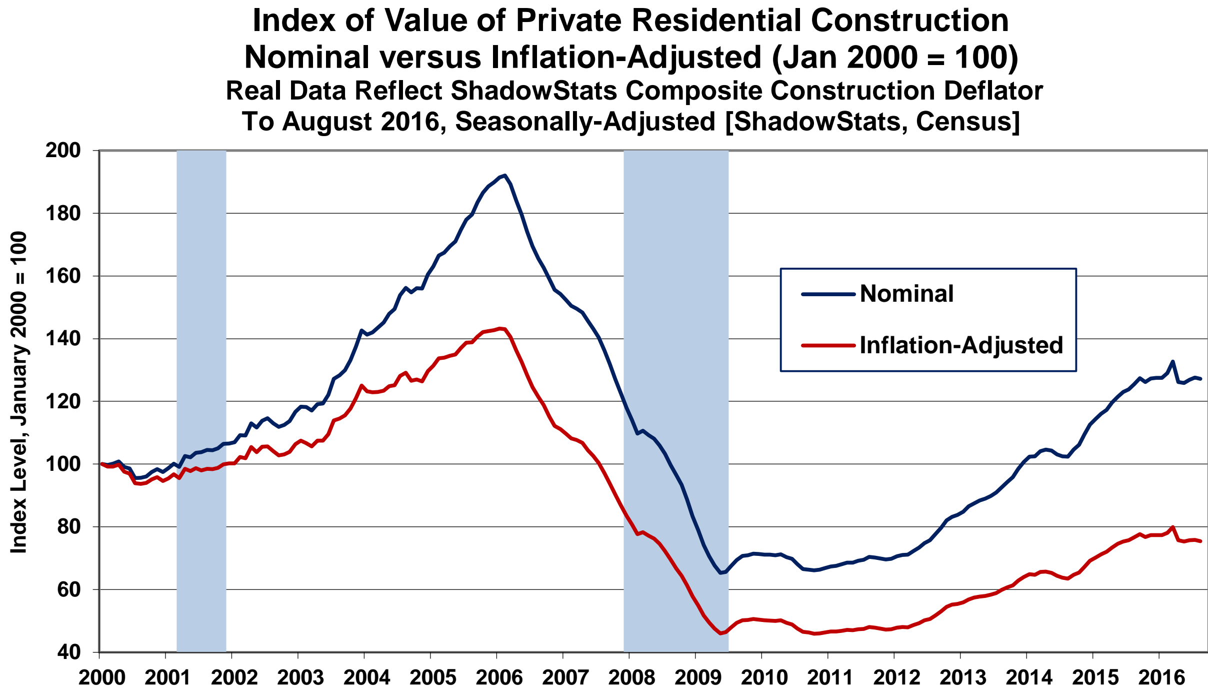
Graph 2: Index, Nominal versus Real Value of Total Construction



Graph 3: Index, Nominal versus Real Value of Private Residential Construction



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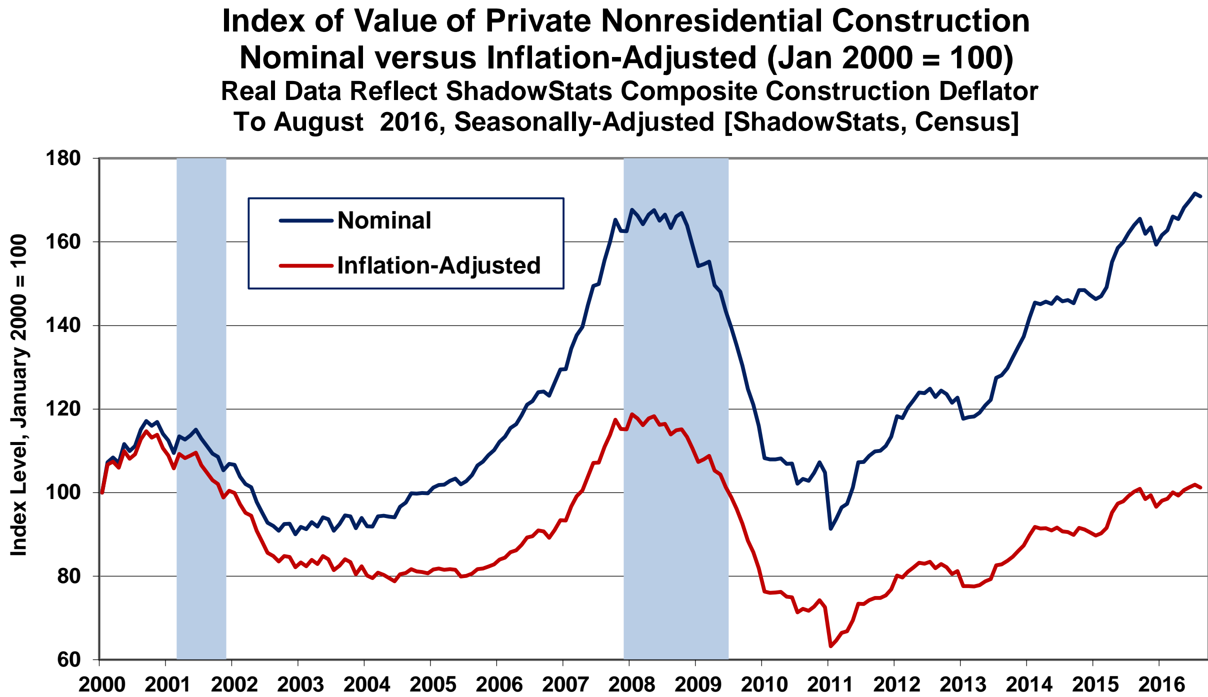
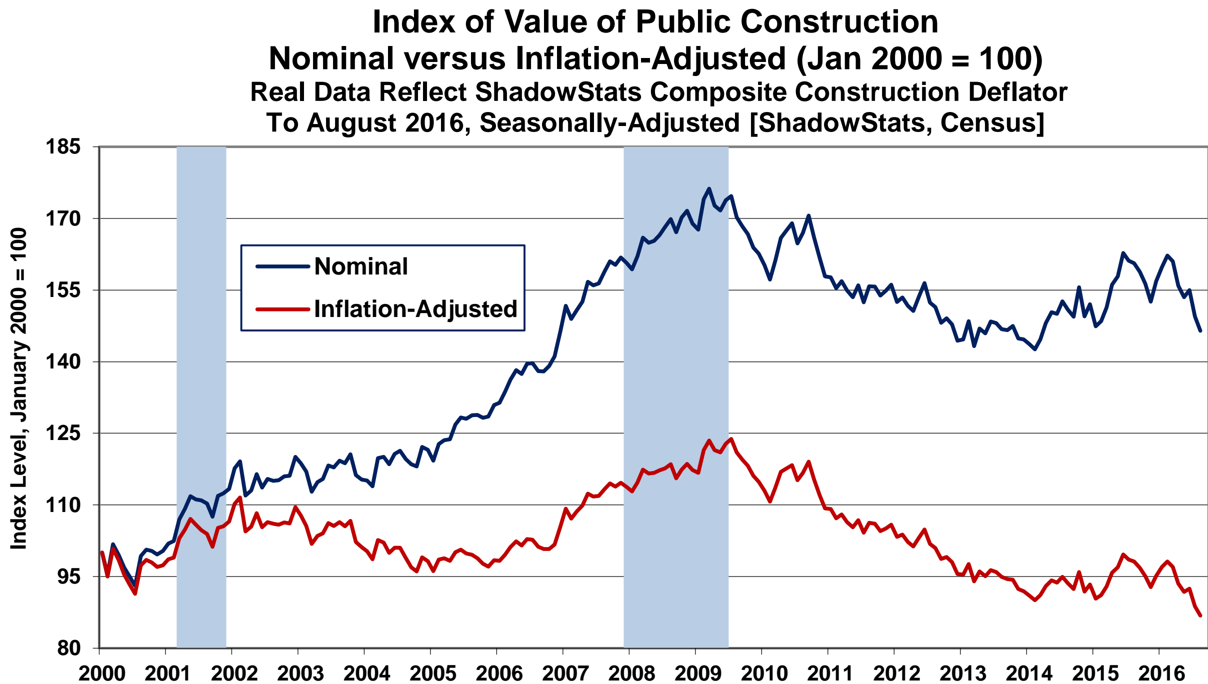
Graph 4: Index, Nominal versus Real Value of Private Nonresidential Construction



Graph 5: Index, Nominal versus Real Value of Public Construction



[The **Reporting Detail** *section contains additional analysis and graphs.]*

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REPORTING DETAIL

U.S. TRADE BALANCE (August 2016)

Mixed Pressures from Soybeans and the Rio Olympics. In the last three years, the nominal trade surplus has not varied by more than $1 billion month-to-month, except in August 2016. That regular stability is due to the services series being largely assumed and modeled with a guessed-at surplus of about $20 billion (plus-or-minus) being used as plug number in narrowing the headline deficit in the goods number. Given the lack of variability in the services surplus, the real merchandise trade deficit generally has been good surrogate for estimating the quarterly change in real net exports, which can dominate headline GDP growth, most-usually on the downside. Those roles reversed in August 2016.

The services surplus balance took a one-time hit of $1.2 billion in August 2016, reflecting the payment of U.S. interests for the use of intellectual property (broadcast rights) of the Rio Olympics.

On the goods-side, the incredible, but temporary surge in U.S. soybean exports from the more-common monthly level of $1.6 billion in June, to $5.2 billion in July, continued at $5.2 billion in August. Without the temporary spike, or otherwise miserably-inadequate seasonal adjustments, the third-quarter trade balance would be wider up by 5.2%, rather than narrower by 3.8% (-3.8%). The difference there otherwise would have consensus estimates looking at a possible contraction in real third-quarter 2016 GDP growth (to be published on October 28th, less than two weeks before the election on November 8th), instead of quarterly GDP growth somewhere in excess of two-percent.

Shown in *Graph 1* in the *Opening Comments*, the second-quarter 2016 real merchandise trade deficit held at its worst reading since third-quarter 2007 (although such never surfaced in the headline second-quarter 2016 GDP reporting, discussed in *Commentary No. 836*). Yet, the unusual and continuing surge in July and August 2016 exports of soybeans continue to give the initial trend in the real third-quarter 2016 merchandise trade deficit, a positive but still likely short-lived boost. Any negative revision to the GDP's third-quarter estimate from the August trade data was due to Rio, and was not reflected in the real merchandise trade deficit shown in *Graph 1*.

Nominal (Not-Adjusted-for-Inflation) August 2016 Trade Deficit. The Bureau of Economic Analysis (BEA) and the Census Bureau reported October 5th, the nominal, seasonally-adjusted monthly trade deficit in goods and services for August 2016, on a balance-of-payments basis. Such was released in the context of a minimal widening revision to the monthly deficit for July.

The headline August 2016 deficit of $40.725 billion, widened by $1.178 billion versus the revised $39.547 [$39.474] billion in July 2016. The $1.178 billion deterioration in the headline monthly deficit reflected a minimal gain of $1.470 billion in monthly exports, more than offset by a $2.647 billion surge in imports (rounding difference). The headline August 2016 deficit also narrowed versus an unrevised

$44.639 billion in August 2015. The dominant factors in these unusual numbers were discussed in the prior section. Shifting activity in energy-related products did not have heavy impact in the monthly trade balance changes.

Energy-Related Petroleum Products. From an import standpoint, declining oil prices had bottomed out in February 2016, inching higher by 0.7% in March, gaining 6.5% in April, 16.0% in May, 15.2% in June and 4.2% in July, but they fell by 4.0% (-4.0%) in August 2016. The impact of that August price decline was muted by surging physical oil-import volume in the month.

The not-seasonally-adjusted average price of imported oil declined to $39.38 in August 2016, versus $41.02 in July 2016, and it was down from $49.33 per barrel in August 2015. Separately, not-seasonally-adjusted physical oil-import volume in August 2016 averaged 8.279 million barrels per day, up from 7.277 million in July 2016 and up from 7.080 million in August 2015.

New and Ongoing Cautions and Alerts on Data Quality. Potentially heavy distortions in headline data continue from seasonal adjustments. Similar issues affect other economic releases, such as labor conditions and retail sales, where the headline number reflects seasonally-adjusted month-to-month change. Discussed frequently (see *2014 Hyperinflation Report—Great Economic Tumble* for example), the extraordinary length and depth of the current business downturn and disruptions have distorted regular seasonality patterns. Accordingly, markets should not rely too heavily on the accuracy of the monthly headline data.

Be aware of another overhaul and historical revisions to the trade services sector, due for release on October 24th. These series overhauls and redefinitions usually do not result in long-overdue downside corrections to the historical economy, but instead tend to bloat recent, reported economic activity with theoretical constructs of seriously-troubled concepts.

This is true particularly where Administration Statistical Bureaus (Census and the BEA, and separately the BLS) appear to be putting prior principles of historical-reporting consistency in the trash bin of headline economic reporting. Among other factors, pending is the addition of U.S. Trade in Information and Communications Technology (a purportedly, meaningfully large and growing surplus, albeit nebulous). Due to historical inconsistencies, it will add to the touted post-2009 “recovery” in the GDP (with no revisions prior to 2013), with emphasis of mitigating a 2014 slowdown in the GDP (see *Commentary No. 823*).

Separately, as usual, the “advance” detail on goods trade, released on September 29th, bore little information useful in estimating the full trade detail released less than one week later, on October 5th.

Real (Inflation-Adjusted) August 2016 Trade Deficit. Seasonally-adjusted, and net of oil-price swings and other inflation (2009 chain-weighted dollars, as used in GDP deflation), the August 2016 merchandise trade deficit (no services) narrowed to $57.478 billion, versus a revised July $58.225 [previously $58.274] billion, and from a $61.443 billion in August 2015.

The August and July numbers followed unrevised real deficits of $64.548 billion in June 2016, $60.892 billion in May 2016, $57.316 billion in April 2016, $56.033 billion in March 2016, $63.607 billion in February 2016 and $61.668 billion in January 2016.

Again, reflected in *Graph 1* of the *Opening Comments*, the annualized quarterly real merchandise trade deficit was $623.1 billion for fourth-quarter 2014, $700.0 billion for first-quarter 2015, $709.1 billion for second-quarter 2015, $708.4 billion for third-quarter 2015, $728.6 billion for fourth-quarter 2015, $725.2 billion for first-quarter 2016, and $731.0 billion for second-quarter 2016. That still was the worst quarterly showing since third-quarter 2007, but somehow it never got into headline second-quarter 2016 GDP growth.

That said, the massively distorted July and August 2016 readings have set an early trend for a real third-2016 merchandise trade deficit of $694.2 billion [initially $699.3 billion, based solely on July reporting]. With the monthly data still in flux, that quarterly trend should shift sharply towards a widening deficit in next month's reporting, and beyond.

Headline deficits likely will get much deeper in the months and quarters ahead, intensifying the ongoing and more-common negative impact on headline GDP.

CONSTRUCTION SPENDING (August 2016)

Spending Held in Real Quarterly Contractions and Low-Level Stagnation. Where this series remains highly volatile and subject to large monthly revisions, nominal August 2016 spending fell, in the context of a downside revision to headline July and an upside revision to June 2016 activity, with inflation-adjusted real activity in the construction spending series remaining negative, on a monthly, quarterly and annual basis. Real monthly spending declined in August 2016, the third monthly contraction in four months. Second- and third-quarter 2016 real spending indicated quarterly contractions, while year-to-year change in real spending tumbled at ever-deepening annual rates in June, July and August 2016, the first monthly year-to-year contractions since late-2011. The series increasingly has followed a pattern seen when construction spending patterns previously have fallen rapidly in recessionary contractions.

Real construction spending generally continued in down-trending, low-level, stagnating non-recovery, with the level of August 2016 still shy of its June 2006 pre-recession peak by 24.6% (-24.6%).

Ongoing Liquidity Constraints on the Consumer Constrain Residential Construction Spending. Consumer liquidity conditions were updated fully in the *Opening Comments* section of Commentary No. 833, with a brief update in Commentary No. 836. The extreme liquidity bind besetting consumers continues to constrain personal-consumption expenditures and related residential-real-estate sales activity. Without sustainable growth in real income, and without the ability and/or willingness to take on meaningful new debt in order to make up for the income shortfall, the U.S. consumer remains unable to sustain positive growth in broad domestic economic activity.

Where the private housing sector never recovered from the business collapse of 2006 into 2009, there remains no chance of a near-term, sustainable turnaround in residential construction, without a fundamental upturn in consumer and banking-liquidity conditions. That has not happened and does not appear to be in the offing.

Construction Inflation—ShadowStats Composite Construction Deflator (CCD). ShadowStats introduced a Composite Construction Deflator (CCD) last month, for use in converting current or nominal (not-adjusted for inflation) headline construction spending into inflation-adjusted, real or constant-dollar

terms. Detailed in *Commentary No. 829*, previously used measures from the Producer Price Index (PPI), lacked historical consistency and did not measure inflation appropriately for the construction spending series.

Accordingly, ShadowStats constructed the CCD specifically for deflating the construction spending series. The CCD is a composite of pricing series, weighted by broad industry segment as compiled in the headline construction spending, with consistent historical tabulation back to before 2000. The combined indices reflect price deflators out of National Income (GDP) reporting, with quarterly numbers there interpolated into smoothed monthly series, in conjunction with privately surveyed monthly cost indicators.

There is no perfect inflation measure, public or private for deflating construction. For the historical series in the accompanying graphs, as shown in *Graphs 2* to *5* in the *Opening Comments*, and in the accompanying *Graphs 7* and *10* in this section, the inflation-adjusted numbers are deflated by the CCD.

Seasonally-adjusted August 2016 CCD month-to-month inflation rose by 0.25%, following gains of 0.40% in July and 0.28% in June. In terms of year-to-year inflation, the August 2016 CCD gained 3.09%, following annual gains of 2.95% in July 2016 and 2.65% in June 2016.

The Data and Graphics Here Reflect Monthly Levels, Not Smoothed, Moving Averages. Unlike the housing-starts and home-sales series—where ShadowStats smooths the irregular and continually-revised monthly data with accompanying plots of smoothed, six-month moving averages—the construction spending series is shown here only on a monthly basis, as published. While the spending series is extremely volatile in its monthly revisions, it tends to be reasonably smooth in the residual month-to-month change. Note the comparative monthly volatilities in the non-smoothed *Graphs 11* and *12*.

[Graphs 6 and 7 follow on the next page]

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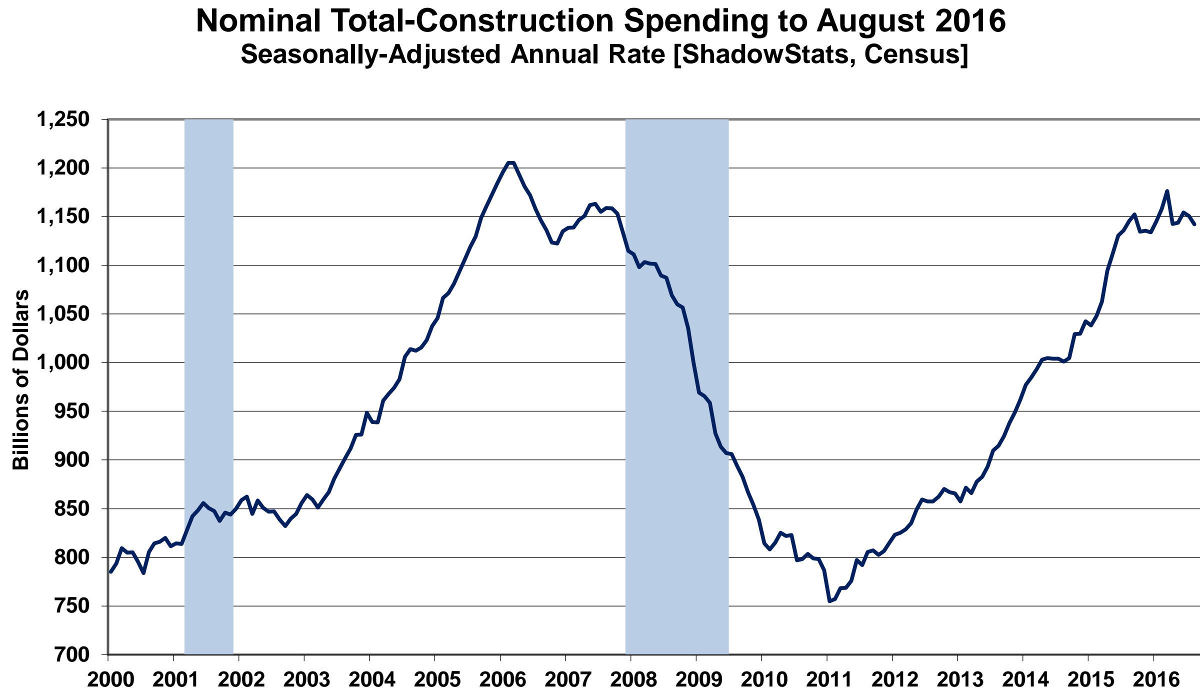
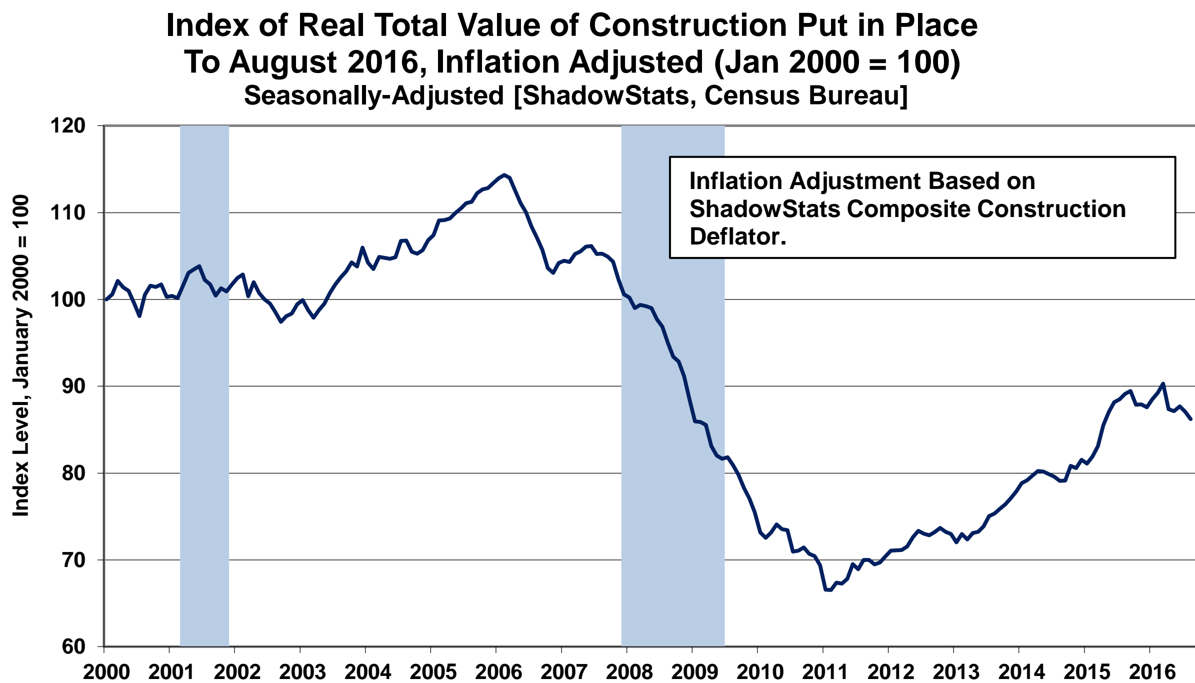
Graph 6: Total Nominal Construction Spending



Graph 7: Index of Total Real Construction Spending



Headline Reporting for August 2016. In the context of a downside revision to July and an upside revision to June activity, the Census Bureau reported October 3rd that the headline, total value of construction put in place in the United States for August 2016 was $1,114.2 billion, on a seasonally-

adjusted, but not-inflation-adjusted, annual-rate basis. That estimate was down month-to-month by a statistically-insignificant 0.7% (-0.7%) +/- 1.8% (all confidence intervals are at the 95% level), versus a downwardly-revised $1,150.6 [previously $1,153.2] billion in July 2016. Net of prior-period revisions, the headline monthly decline in August 2016 was a still-statistically-insignificant 1.0% (-1.0%).

In turn, July was down by a revised 0.2% (-0.2%) [previously unchanged], versus an upwardly-revised $1,154.1 [previously $1,153.5, initially $1,133.5] billion in June 2016. In turn, June was up by a revised 1.1% [previously up by 0.9%, initially down by 0.6% (-0.6%)] versus an unrevised $1,143.8 in May.

Adjusted for CCD inflation, total real month-to-month spending in August fell by 1.0% (-1.0%), versus a revised decline of 0.7% (-0.7%) in July 2016 and an unrevised gain of 0.6% in June 2016.

On a year-to-year annual-growth basis, August 2016 nominal construction spending declined by a statistically-insignificant 0.3% (-0.3%) +/- 2.1%, following a downwardly revised annual gain of 1.3% [previously up by 1.5%] in July 2016, and an upwardly revised gain of 2.1% [previously up by 2.0%, initially up by 0.3%] in June 2016. Net of construction costs indicated by the CCD, the year-to-year change in total real construction spending dropped to a 63-month low of minus 3.3% (-3.3%) in August 2016, versus a deeper, revised decline of 1.6% (-1.6%) in July 2016 and a revised annual decline of 0.5% (-0.5%) in June 2016. The headline annual real decline in August activity was the weakest since the historical series troughed in its collapse into 2011.

The statistically-insignificant, monthly decline of 0.7% (-0.7%) in aggregate August 2016 construction spending, versus a decline of 0.2% (-0.2%) in July 2016, included a headline monthly drop in August of 2.0% (-2.0%), versus a monthly plunge of 3.5% (-3.5%) in July public spending. Private spending declined by 0.3% (-0.3%) in August having gained 0.8% month-to-month in July. Within total private construction spending, residential-sector activity also fell by 0.3% (-0.3%) in August, having gained 0.5% in July, while the nonresidential sector fell by 0.4% (-0.4%) in August, in the context of revising sharply lower to a 1.0% monthly gain in July.

Quarterly Trends. Reflecting headline August 2016 reporting in the context of the revisions to June and July 2016 headline detail, second-quarter 2016 real construction still plunged quarter-to-quarter, with an early trend towards contraction continuing in third-quarter activity.

With all spending revisions and the latest inflation estimates in hand, first-quarter 2016 real construction spending rose at an unrevised annualized pace of 7.3%. Second-quarter 2016 showed an unrevised real contraction of 8.5% (-8.5%). Based on reporting just for July and August 2016, the early trend for third-quarter 2016 activity was a quarterly contraction of 2.7% (-2.7%). Previously, based solely on the initial July 2016 estimate, the early third-quarter trend had been for a real, annualized quarterly contraction of 2.0% (-2.0%).

Going back into last year, fourth-quarter 2015 real construction spending contracted at an annualized pace 5.4% (-5.4%), following annualized quarterly real gains of 10.1% in third-quarter 2015, 26.0% in second-quarter 2015 and 5.3% in first-quarter 2015.

Graphs 2 to *5* in the *Opening Comments* show comparative nominal and real construction activity for the aggregate series as well as for private residential- and nonresidential-construction and public-construction. Seen after adjustment for inflation, the real aggregate series generally has remained in low-level stagnation, now down-trending throughout 2016, into the third quarter. Areas of recent relative strength

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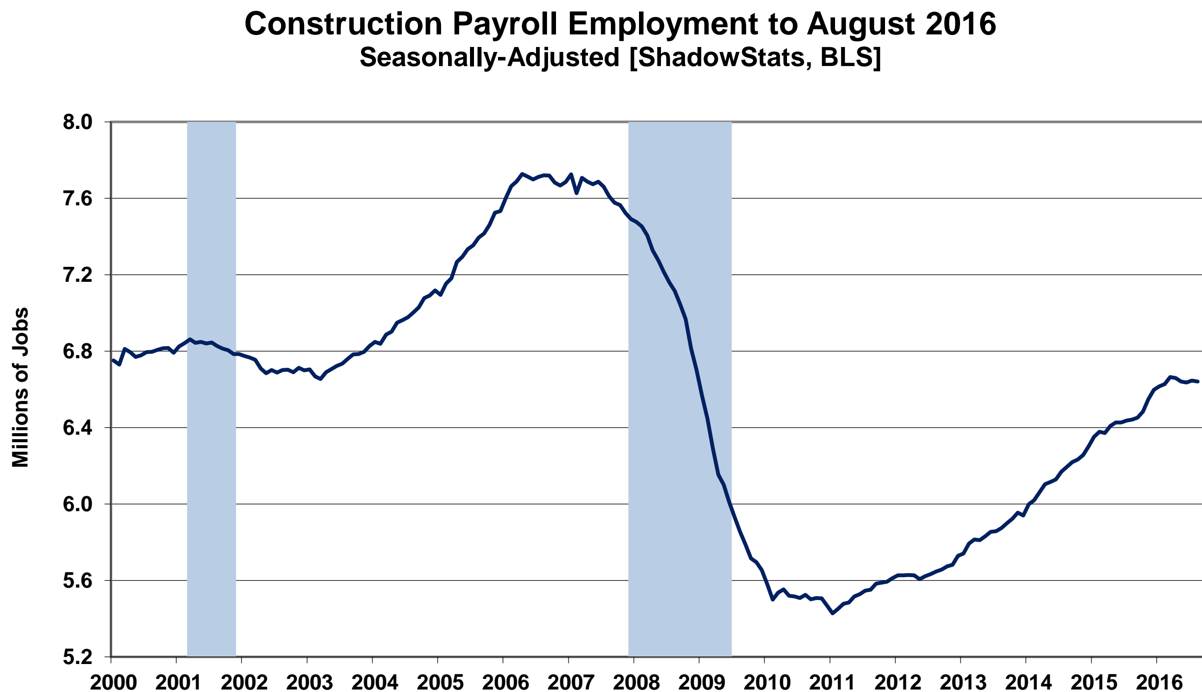
in the major subcomponents generally have flattened out, or turned down, after inflation adjustment, except for private nonresidential spending, which just turned minimally from up-trending to down-trending.

The general pattern of real activity had been one of low-level, up-trending stagnation that now has turned lower in recent quarters. The aggregate nominal detail, before inflation adjustment, is shown in *Graph 6* of this *Reporting Detail*, with the real, inflation-adjusted activity plotted in *Graph 7*. *Graphs 9* and *10* show the relative patterns of nominal and real activity aggregated by sector.

Construction and Related Graphs. Earlier *Graphs 6* and *7*, and later *Graphs 9* and *10* reflect total construction spending through August 2016, both in the headline nominal dollar terms, and in real terms, after inflation adjustment. *Graph 7* is on an index basis, with January 2000 = 100.0. Adjusted for the CCD, real aggregate construction spending showed the economy slowing in 2006, plunging into 2011, then turning minimally higher in an environment of low-level stagnation, trending lower from late-2013 into mid-2014 and then some boost into early-2015. Activity declined in fourth-quarter 2015, with an early-2016 fluttering trend that has turned lower, once again, into third -quarter 2016.

The pattern of non-recovered, inflation-adjusted activity here—net of ShadowStats inflation estimates—does not confirm the economic recovery indicated by the headline GDP series (see *Commentary No. 836* and *No. 777 Year-End Special Commentary*). To the contrary, the broad construction reporting, both before (nominal) and after (real) inflation adjustment, generally still shows a pattern of low-level activity, where aggregate activity never recovered pre-recession highs and has flattened-out anew, turning lower in second- and third-quarter 2016.

Graph 8: Construction Payroll Employment to August 2016



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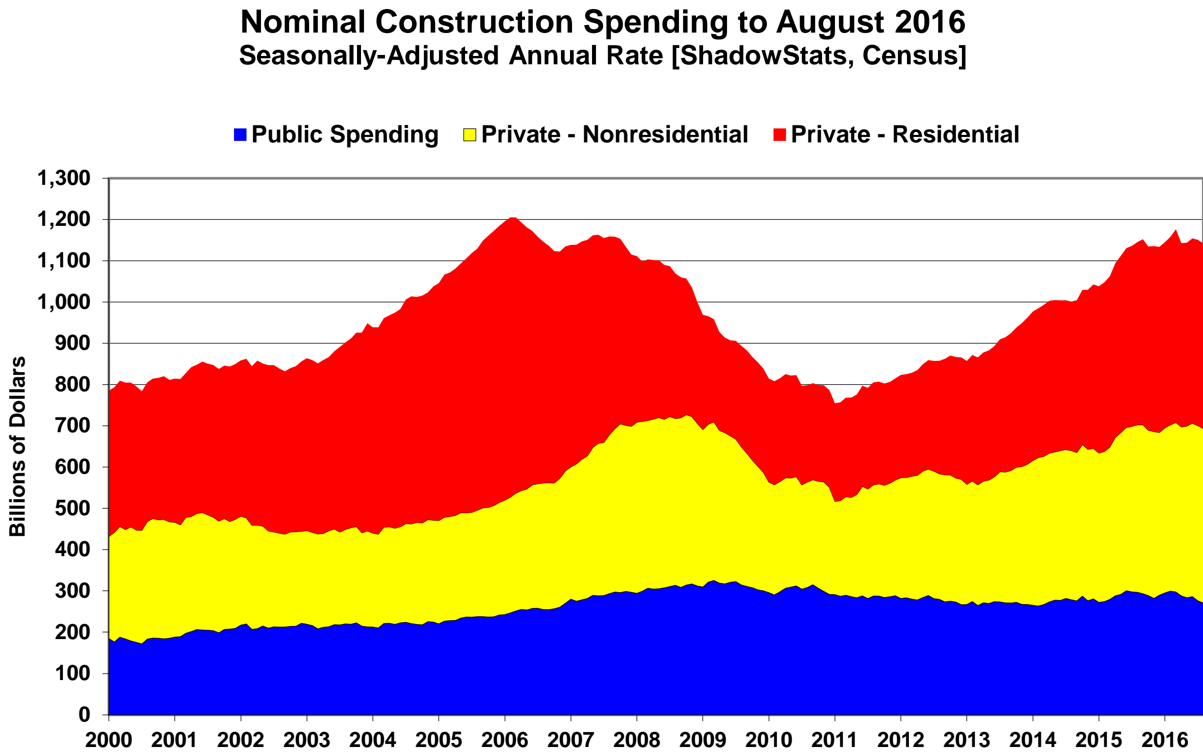
Construction Employment Not Recovering. *Graph 8* shows August 2016 construction employment, as discussed and detailed in the *Payroll Employment* section of *Commentary No. 829*. In theory, payroll levels should move more closely with the inflation-adjusted aggregate series, where the nominal series reflects the impact of costs and pricing, as well as a measure of the level of physical activity. Where construction payrolls have gone flat or turned down, such is consistent now with the contracting quarterly and collapsing annual growth here in headline real construction spending. The construction employment graph will be updated for September labor details in tomorrow's *Commentary No. 838* of October 7th.

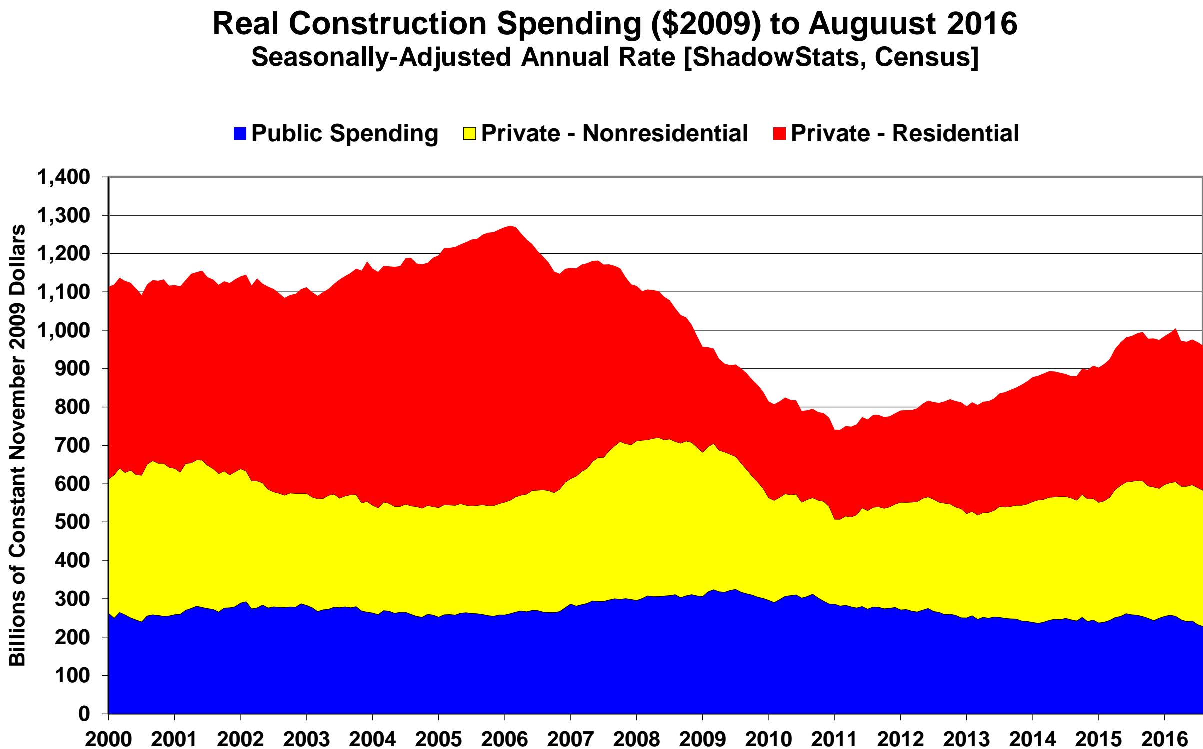
Graphs of Construction Activity. *Graph 9* shows total nominal construction spending, broken out by the contributions from total-public (blue), private-nonresidential (yellow) and private-residential (red) spending. *Graph 10* shows the same breakout by sector as in *Graph 9,* but the detail is in real, inflation-adjusted terms, reflected in constant November 2009 dollars, deflated by the *ShadowStats Composite Construction Deflator (CCD)*, as discussed in the earlier *Construction Inflation* section.

[Graphs 9 to 15 begin on the next page.]

Graph 9: Aggregate Nominal Construction Spending by Major Category to Date



Graph 10: Aggregate Real Construction Spending by Major Category (Billions of November 2009 Dollars)



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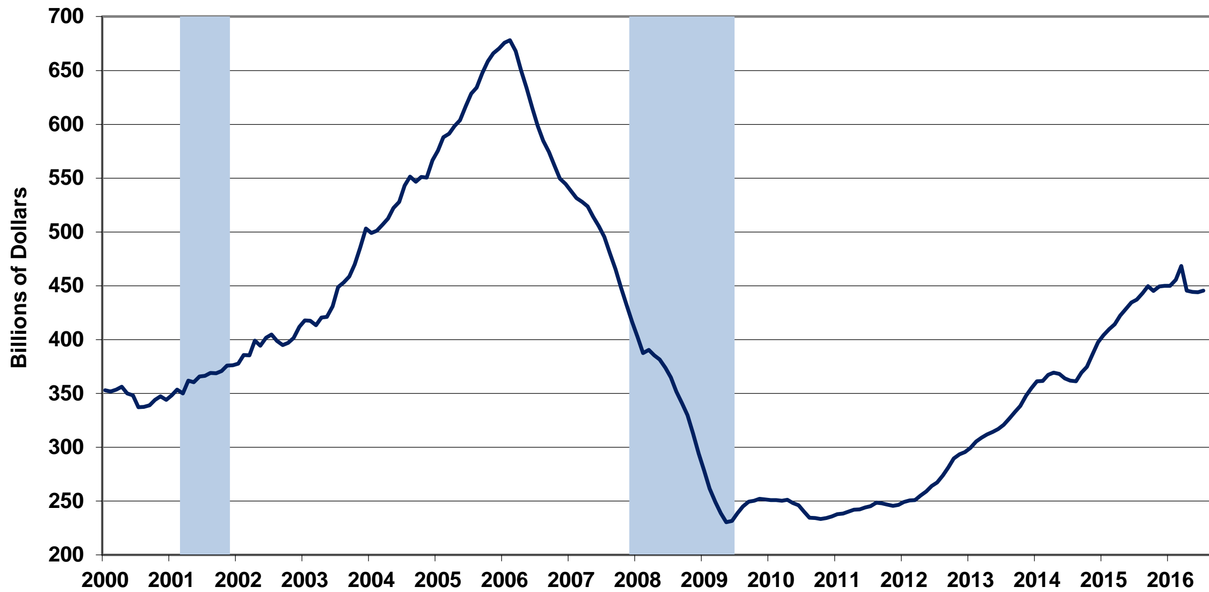
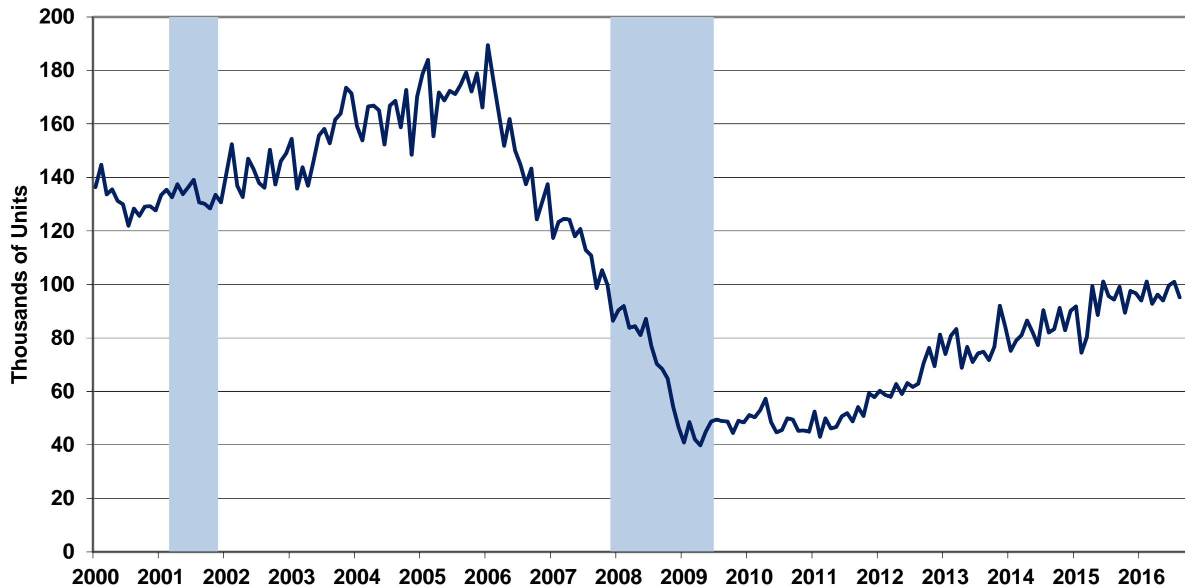
The next two graphs (*Graphs 11* and *12*) cover private residential construction spending, along with housing starts (combined single- and multiple-unit starts) for August 2016 (see [Commentary No. 834](#)).

Graph 11: Nominal Private Residential Construction Spending to Date

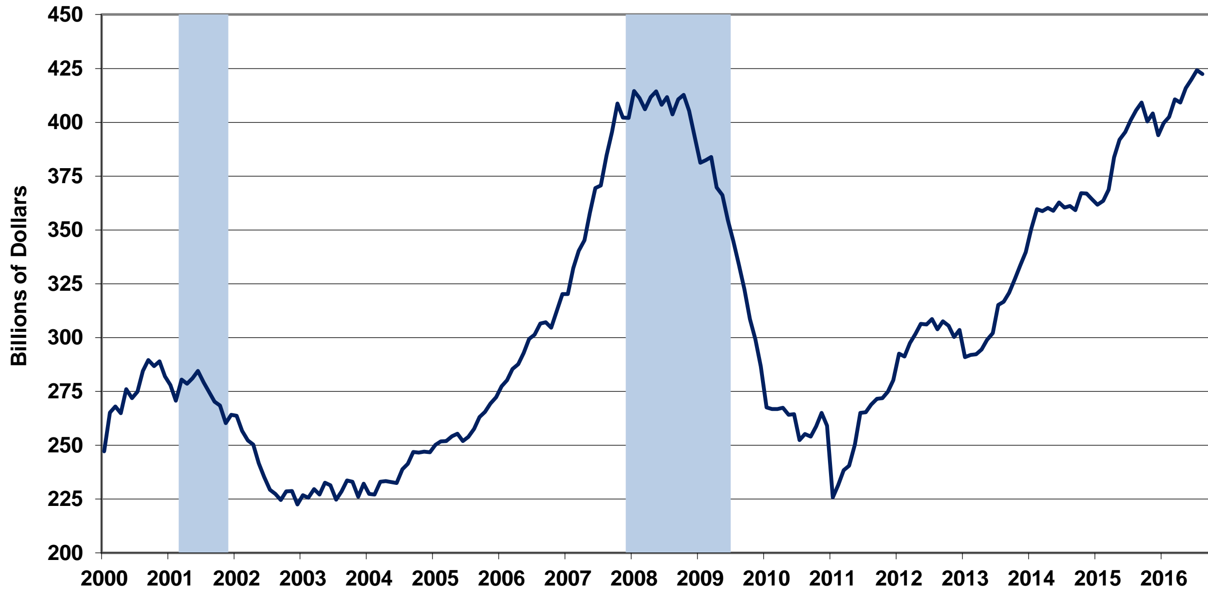


Graph 12: Single- and Multiple-Unit Housing Starts to Date

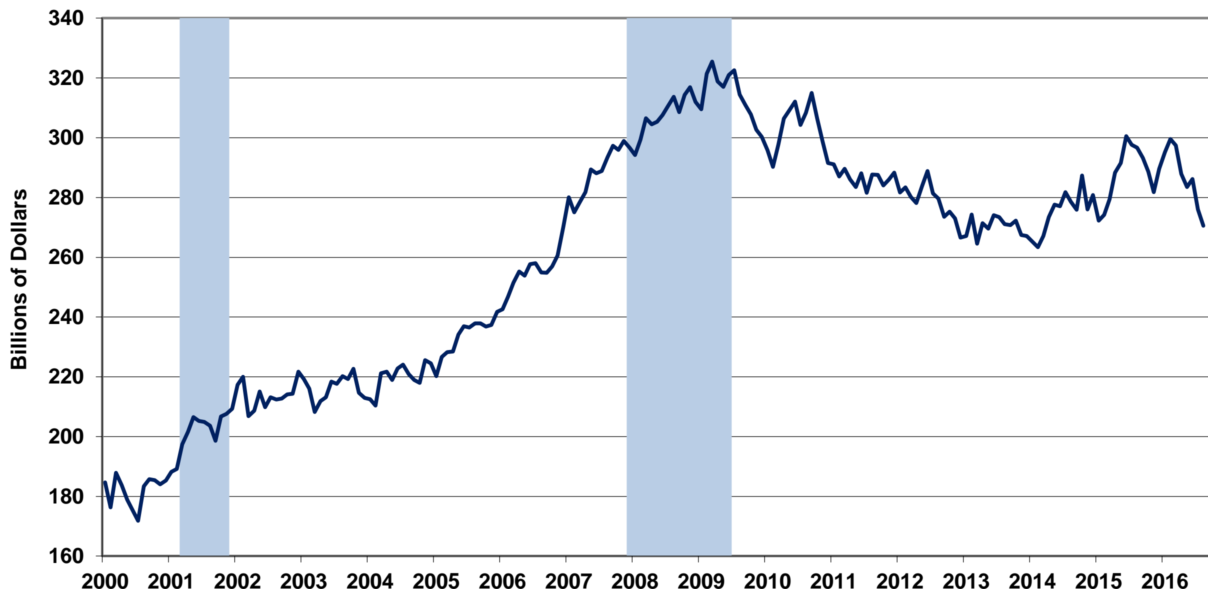


Keep in mind that the construction spending series is in nominal terms, while housing starts reflect unit volume, which should be parallel with the inflation-adjusted series shown in *Graph 3* of the *Opening Comments* section, *Graph 10* and presumably with the headline construction-payroll data in *Graph 8*.

Graph 13: Nominal Private Nonresidential Construction Spending to Date



Graph 14: Nominal Public Construction Spending to Date



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The final two graphs (*Graphs 13* and *14*) show the patterns of the monthly level of activity in private nonresidential-construction spending and in public-construction spending.

Private Non-Residential Construction spending had surged in last revisions (pulled back in this month's revisions), and in headline reporting, to a pre-recession peak in July 2016; the series backed off that prior reporting with the headline August detail.

Public Construction spending, which is 98% nonresidential, had continued in a broad downtrend into 2014, with intermittent bouts of fluttering stagnation and then some upturn in 2015. In 2016, the nominal series still appears to be fluttering in something of a volatile topping-out process, turning lower still in its latest reporting, still shy of its pre-recession peak. Viewed net of inflation, in *Graphs 4*, *5* and *10,* indeed, both series appear stalled shy of their pre-recession peaks.

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WEEK AND MONTH AHEAD

Near-Term Headline Economic Deterioration Should Intensify, Increasingly Frustrating Fed Provocateurs, Pummeling the U.S. Dollar and Boosting Gold, Silver and Eventually Oil Prices. Market expectations for business activity should continue to deteriorate, amidst intensifying, negative headline economic reporting. Irrespective of continuing talk by some FOMC members of a near-term rate hike, an ongoing and deepening domestic economic downturn promises intensified stress on systemic liquidity. That circumstance ultimately dooms the U.S. central bank to an intensified quantitative easing.

Fed-policy retrenchment should remain very much alive, shifting towards that renewed quantitative easing, in the post-election environment, as discussed in the *Opening Comments* of *Commentary No. 835*, which reviewed August durable goods orders, home-sales activity and the most-recent FOMC inaction.

Commentary No. 836 updated the latest GDP reporting (third-estimate of second-quarter 2016), as well as provided an economic reality check on some harder, less-theoretical and more-independent (non-government) economic numbers.

Commentary No. 834 detailed August activity in residential construction units (*i.e.*, housing starts), while underlying consumer liquidity and household income conditions were updated fully in *Commentary No. 833*, along with continuing discussion of FOMC options and the latest consumer inflation detail.

The general trend in weakening expectations for business activity and movement towards looming recession recognition, reflect an ongoing broad spectrum of market-disappointing headline data, such as

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seen in *Commentary No. 832*. Earlier FOMC considerations also were covered in *Commentary No. 831*, while the initial payroll benchmark revision for 2016 was discussed in *Commentary No. 830*, following the latest headline detail on payrolls, trade and construction spending in *Commentary No. 829*.

Broad economic and systemic details detail otherwise have been reviewed most recently in *Commentary No. 827*, *Commentary No. 826*, *Commentary No. 825*, *Commentary No. 824*, *Commentary No. 823*, *Commentary No. 822*, *Commentary No. 821*, *Commentary No. 820*, *Commentary No. 818*, *Commentary No. 817*, *General Commentary No. 811*, *Supplemental Commentary No. 807-A*, *Commentary No. 800*, *Commentary No. 799*, *Commentary No. 796-A*, *Commentary No. 796* and *No. 777 Year-End Special Commentary*.

Negative market reactions had surfaced in trading of the U.S. dollar and in related financial markets, with some upside pressure on gold, silver and oil prices, subsequent to recent, weaker-than-expected headline economic data or suggestions of a less-aggressive tightening stance by the Fed. Fed rate-hike jawboning, however, had put a temporary flutter into those market movements, placing some Fed-desired support under the U.S. currency.

Again, though, the fundamental liquidity issues facing the Fed remain dominated by the impact of perpetual U.S. economic non-recovery and a renewed, intensifying downturn. If the Fed should raise rates in the near future, ongoing negative economic pressures still will mount, forcing the U.S. central bank back into a position of having to support domestic financial- and banking-system liquidity needs. Effectively, the Fed will have no way out other than to return to some form of expanded quantitative easing.

Temporary jawboning aside, market reactions increasingly should reflect a renewed sense of Federal Reserve impotence in the wake of the latest no rate hike, with bleak longer-term implications for the U.S. dollar. While anything is possible, Fed tightening prior to the election appears now to be out of consideration, with renewed quantitative easing becoming the likely target of post-election speculation, as the deepening recession unfolds.

Rapidly weakening, regular monthly economic reporting should continue and result in much worse-than-expected—increasingly negative—reporting for at least the next several quarters of GDP (and GDI and GNP).

CPI-U consumer inflation—intermittently driven lower in 2015 and early-2016 by collapsing prices for gasoline and other oil-price related commodities—likely has seen its near-term, year-to-year low. Headline monthly March to June 2016 detail moved into positive headline territory, in tandem with rising gasoline prices. CPI inflation was "unchanged"—minimally negative—with a switch to positive seasonal adjustments for gasoline prices only partially offsetting the unadjusted monthly drop in gasoline prices in July. August CPI was boosted by "core" inflation. Going forward, a weakening U.S. dollar increasingly should boost inflation, with a related upturn in oil prices, gasoline and other commodities. The *Public Commentary on Inflation Measurement* reviews fundamental reporting issues with the headline CPI.

Note on Reporting-Quality Issues and Systemic-Reporting Biases. Significant reporting-quality problems remain with most major economic series. Beyond the pre-announced gimmicked changes to reporting methodologies of the last several decades, which have tended to understate actual inflation and

to overstate actual economic activity, ongoing headline reporting issues are tied largely to systemic distortions of monthly seasonal adjustments.

Data instabilities—induced partially by the still-evolving economic turmoil of the last nine-to-eleven years—have been without precedent in the post-World War II era of modern-economic reporting. The severity and ongoing nature of the downturn provide particularly unstable headline economic results, with the use of concurrent seasonal adjustments (as seen with retail sales, durable goods orders, employment and unemployment data). That issue is discussed and explored in the labor-numbers related *Supplemental Commentary No. 784-A* and *Commentary No. 695*.

Further, discussed in *Commentary No. 778*, a heretofore unheard of spate of "processing errors" surfaced in recent surveys of earnings (Bureau of Labor Statistics) and construction spending (Census Bureau). This is suggestive of deteriorating internal oversight and control of the U.S. government's headline economic reporting. That construction-spending issue now appears to have been structured as a gimmick to help boost the recently-published 2016 GDP benchmark revisions, aimed at smoothing the headline reporting of the GDP business cycle, instead of detailing the business cycle and reflecting broad economic trends accurately, as discussed in *Commentary No. 823*.

Combined with ongoing allegations in the last year or two of Census Bureau falsification of data in its monthly Current Population Survey (the source for the BLS Household Survey), these issues have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series (see *Commentary No. 669*). John Crudele of the *New York Post* continues his investigations in reporting irregularities: *Crudele Investigation*. In the 1990s, the Census Bureau and BLS played political-reporting games with the nature of statistical sampling size in "inner cities" in the Census Bureau surveying tied to the monthly Household Surveys and the annual piggy-backed Poverty Survey. Such had major distorting impact on the headline data, and it may be in the works, again.

PENDING RELEASE:

Employment and Unemployment (September 2016). The Bureau of Labor Statistics (BLS) will publish its September 2016 labor data tomorrow, Friday, October 7th. Headline detail will be covered in *Commentary No. 838* of that date. Both the more-inclusive unemployment-rate numbers, as well as the headline payroll-employment details, are open for continuing negative headline surprises, given the ongoing, general weakening tone in a number of business indicators.

In the context of the recent extreme volatility and inconsistencies in the last several months of payroll and unemployment detail, almost anything is possible with the BLS, particularly with the presidential race in nearing its climax. To the extent that pre-election political influences come into play, the reporting of September's data and next month's October data are the months mostly likely to be affected, but September is the most likely to be affected.

Nonetheless, underlying reality remains a much weaker-than-expected economy, which increases the odds of a hefty downside surprise to the headline payroll gain in September. Market expectations are for a headline monthly payroll gain of 169,000, plus-or-minus, although the consensus likely will soften a bit, given a weaker-than-0 expected ADP estimate released this morning (October 5th).

Although the consensus outlook is for the headline U.3 unemployment rate to hold at 4.9% in September, the headline unemployment detail remains completely unstable and not comparable month-to-month, due to the inconsistent use of published seasonally-adjusted numbers. Such has been demonstrated in recent reporting, as discussed fully in *Commentary No. 819*. An element to watch as to meaningless month-to-month comparisons, is where trends in the number of employed properly should move opposite from the trends in the unemployed count. Recent headline experience frequently has been where both the employed and unemployed counts nonsensically move in the same direction, where, for example, surging headline employment was matched by surging unemployment. That said, again, anything is possible in the next month, but the Household-Survey data increasingly should trend weaker than expected.

Underlying economic fundamentals continue to weaken, suggesting continued slowing or negative month-to-month growth in headline payrolls, as well as stagnation or deterioration in the broader unemployment rates such as U.6 and particularly the ShadowStats Alternate Unemployment Measure.

PLANNED UPDATES: Comprehensive *Special Report* and ShadowStats Website. ShadowStats is updating fully, into one, massive background piece—a *Special Report (Commentary)*—the latest broad outlook for the U.S. and global economies, financial markets and systems, and inflation (U.S. hyperinflation). All of that will be in the context of incorporating and fully revising, wherever necessary, the materials in the *2014 Hyperinflation Report—The End Game Begins*, *2014 Hyperinflation Report—Great Economic Tumble*, *No. 777 Year-End Special Commentary* and other intervening missives, including the most-recent *Hyperinflation Outlook Summary* as found in *Commentary No. 783*.

The various background articles available at the www.ShadowStats.com site also will be updated in the process, including those first published in 2004 as introductory articles to the site. As usual, all original material will remain available to subscribers (all original public material also will remain available to anyone visiting the site).

As to timing, the *Special Report* is progressing and should be published this month. It will include updated, consistent GAAP-based financial detail on the U.S. government's financial condition through September 30, 2015 and initial prospects for the fiscal year ended September 30, 2016.

Updates to the various public materials on the Web site will be staggered through year-end. The introduction of the *2004 Primer Series* will be first (the link is to the initial background article that addressed among other issues political manipulation of data).

We also will introduce, in conjunction with the *Special Report*, a section with links to books and articles that we have found of particular interest and substance. Anyone with materials they would like to have considered for inclusion should send details in an e-mail to johnwilliams@shadowstats.com or call John Williams directly at (707) 763-5786.

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