John Williams'
Shadow Government Statistics
Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 872
February PPI, CPI, Retail Sales and Earnings and the FOMC

March 15, 2017

FOMC Fiddles with Boosting Interest Rates,
While Annual Real M3 Growth Just Plunged to a
New Signal for a Major Economic Downturn

Annual Contraction in First-Quarter Real Earnings Is a Virtual Certainty;
Back-to-Back Quarterly Contractions Also Are in Play;
Circumstances Not Seen Since the Stalled GDP of Second-Half 2012

February Nominal Retail Sales Gain of 0.08% Was Less than Inflation;
Inflation-Adjusted Real Sales Declined by 0.04% (-0.04%) for the Month

Headline Annual Inflation Surge Has Been Due to Energy-Price Distortions,
Not to an Overheating Economy

February 2017 Monthly CPI Inflation Rose by 0.12%,
Pushing Annual CPI-U Inflation to a 60-Month High of 2.74%, with
CPI-W at 2.82% and ShadowStats at 10.5%

February Final-Demand PPI Annual Inflation Hit a 59-Month High of 2.19%

PLEASE NOTE: The next regular Commentary*, scheduled for tomorrow, Thursday, March 16th, will review the FOMC action, related U.S. dollar circumstances and February Housing Starts, followed by a* Commentary *on Friday, March 17th, covering February Industrial Production and an updated economic review. Please call me at (707) 763-5786, if you have questions or would like to talk.*

Best wishes to all — John Williams

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OPENING COMMENTS AND EXECUTIVE SUMMARY

FOMC Boosted the Fed Funds Rate, Irrespective of Faltering Economic Activity. As broadly expected, the Federal Reserve's Federal Open Market Committee (FOMC) announced a quarter-point boost in the targeted federal funds rate this afternoon (March 15th). The FOMC statement continued to note, "However, the actual path of the federal funds will depend on the economic outlook as informed by incoming data." Therein lies the underlying qualifier in these carefully-worded FOMC missives, which shortly still should blow apart headline Fed policy and related financial-market hype around the U.S. dollar and U.S. equities (see also *Commentary No. 871* and *Commentary No. 870*).

Where this circumstance and related underlying economic reality and systemic-solvency issues will be reviewed in tomorrow's (March 16th) *Commentary No. 873*, with a follow-up economic update in Friday's (March 17th) *Commentary No. 874*, some troubling economic signals from today's headline inflation reporting are reviewed briefly here. Separately, given tomorrow's FOMC review, the graphs of the U.S. dollar and gold, which usually accompany the monthly CPI *Commentary*, will be published in that review instead of today's.

Fresh Signals of Broad Economic Contraction. With headline February 2017 CPI-U and CPI-W inflation in hand, two series are generating new signals of pending or intensifying economic downturn: Quarterly Real Earnings Growth, and Annual Real Growth in Money Supply M3 (ShadowStats Ongoing Measure).

Referenced in both the *Executive Summary* and in the *Reporting Detail* covering the *Consumer Price Index*, Real Earnings are on track for a second, consecutive quarter-to-quarter contraction in first-quarter 2017, while year-to-year change in first-quarter 2017 Real Earning is a virtual certainty for an annual contraction. The last time those two patterns of change were seen either separately or together was in the second-half of 2012. Annualized GDP growth for those two quarters in combination was 0.04%, virtually no growth; there has been no weaker two-quarter period of headline GDP growth since.

Discussed in *Real (Inflation-Adjusted) Money Supply M3—February 2017—Annual Growth Has Signaled New Economic Downturn* in the *Consumer Price Index* section of the *Reporting Detail* (see pages 19 and 20), real year-to-year change in M3 has dropped to a level that always has signaled an economic downturn. The current signal, though, is in the context of the economy never having recovered from its collapse into 2009 (see *Graph 9*, and *Commentary No. 869*).

As will be reviewed in Friday's *Commentary No. 874*, these signals are in the context of a variety of other indicators that portray broad economic activity in collapse into 2009, from which there has been no full recovery, and which has turned to low-level stagnation and renewed downturn. That circumstance still impairs banking-system liquidity and solvency, and ultimately will prevent the Federal Reserve from escaping is quantitative-easing quagmire.

Today's *Commentary* (March 15th). The balance of these *Opening Comments and Executive Summary* covers summary detail of the February 2017 CPI, PPI and Retail Sales (nominal and real), with the headline numbers expanded upon in the *Reporting Detail*.

The *Week, Month and Year Ahead* updates previews of reporting still ahead this week, specifically Housing Starts on Thursday and Industrial Production on Friday.

Executive Summary: Retail Sales—February 2017—Headline Monthly Gain of 0.08% Turned to an Inflation-Adjusted Real Contraction of 0.04% (-0.04%). In the context of upside revisions to previously reported activity in January 2017 and December 2016, nominal Retail Sales in February gained a statistically insignificant 0.08% for the month, versus an upwardly-revised 0.64% gain in January 2017 and a 0.98% gain in December 2016. Net of prior-period revisions, headline February growth would have been 0.39%.

The February 2017 nominal year-to-year change in Retail Sales showed a statistically-significant increase of 5.86%, versus an upwardly revised 6.01% annual gain in January 2017 and a revised 4.39% annual gain in December 2016.

Despite reflecting softer automobile sales in February 2017, and downside revisions to same in January 2017 and December 2016, current headline retail sales reporting remains heavily distorted, with more-reliable month-to-month detail not likely to be published before the benchmark revisions of 2019 (see 2017 Notice in the *Reporting Detail*).

Real Retail Sales (Adjusted for Inflation). The headline detail from the coincident release of the February 2017 CPI-U, showed month-to-month, seasonally-adjusted CPI-U inflation of 0.12% in February 2017, 0.55% in January 2017 and 0.26% in December 2016, with year-to-year seasonally-adjusted CPI-U inflation of 2.80% in February 2017, 2.54% in January 2017 and 2.09% in December 2016. Accordingly, real monthly sales declined by 0.04% (-0.04%) in February 2017, versus a real gain of 0.09% in January 2017, and a revised gain of 0.73% in December 2016. Real annual Retail Sales growth was 2.79% in February 2017, versus a revised 3.38% in January 2017 and a revised 2.25% in December 2016.

Real Retail Sales Graphs, Corrected and Otherwise. In the *Reporting Detail*, *Graphs 4* and *6* show the level of real retail sales activity (deflated by the CPI-U), while *Graphs 5* and *7* show year-to-year percent change. The apparent "recovery" of headline real retail sales shown in the following *Graph 1* (see also *Graph 4* in the *Reporting Detail*) generally continued into late-2014. Although headline reporting turned down in December 2014, into first-quarter 2015, it turned higher into the third-quarter 2015, slowed to a near-standstill in fourth-quarter 2015 and contracted in first-quarter 2016, with an uptick in second-quarter 2016, renewed slippage into third-quarter 2016, and with a further uptick in fourth-quarter 2016 and early 2017.

Nonetheless, headline real growth in retail sales continued to be overstated heavily, due to the understatement of CPI-U inflation used in deflating the retail sales series. Discussed more fully in *Chapter 9* of [2014 Hyperinflation Report—Great Economic Tumble](#) – *Second Installment* and [Public](#)

Commentary on Inflation Measurement, deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

Both of the accompanying graphs are indexed to January 2000 = 100.0 to maintain consistency in the series of graphs related to corrected inflation-adjustment, including the regular plots of the "corrected" industrial production index (see the prior section), and "corrected" new orders for durable goods and "corrected" GDP (both covered in Commentary No. 863 and No. 859 Special Commentary).

The first graph here reflects the official real retail sales series, except that it is indexed, instead of being expressed in dollars. The plotted patterns of activity and rates of growth are exactly same for the official series, whether the series is indexed or expressed in dollars, again, as is evident in a comparison again of *Graph 1* with *Graph 4* in the *Retail Sales—Nominal and Real* in the *Reporting Detail* section.

Instead of being deflated by the CPI-U, the "corrected" real retail sales numbers—in *Graph 2*—use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation. With the higher inflation of the ShadowStats measure, the revamped numbers show a pattern of plunge and stagnation and renewed downturn. That pattern generally is consistent with consumer indicators such as real average weekly earnings (see the next section), faltering consumer liquidity conditions (see *Consumer Liquidity Conditions* updated in prior Commentary No. 871, and the *ECONOMY* section of No. 859 Special Commentary).

[Graphs 1 and 2 follow on the next page.]

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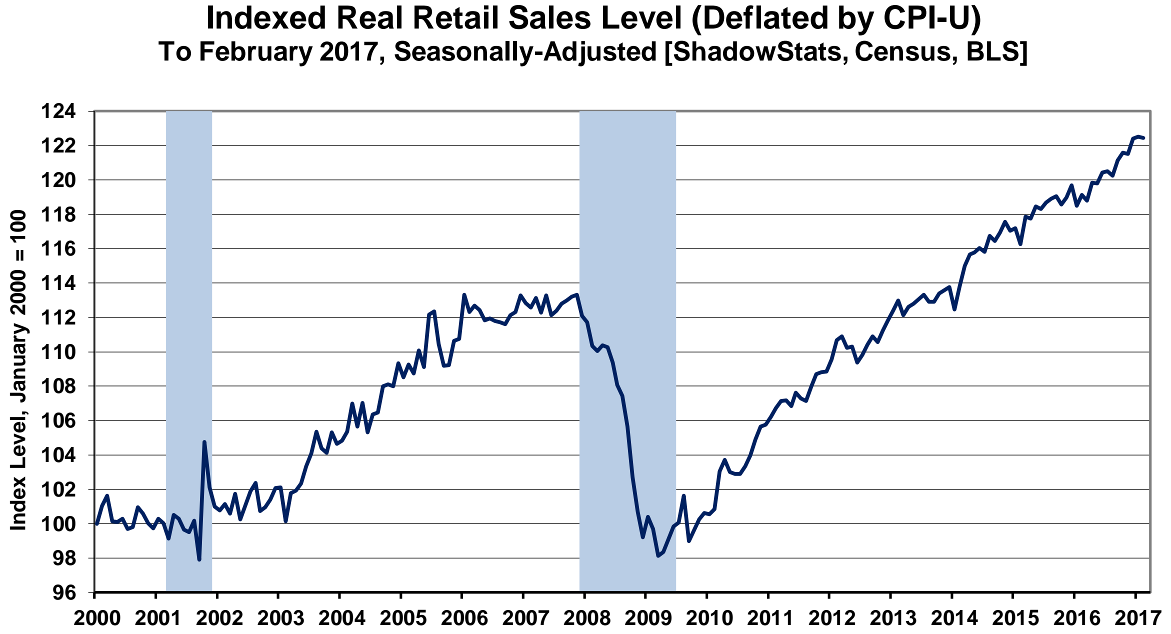
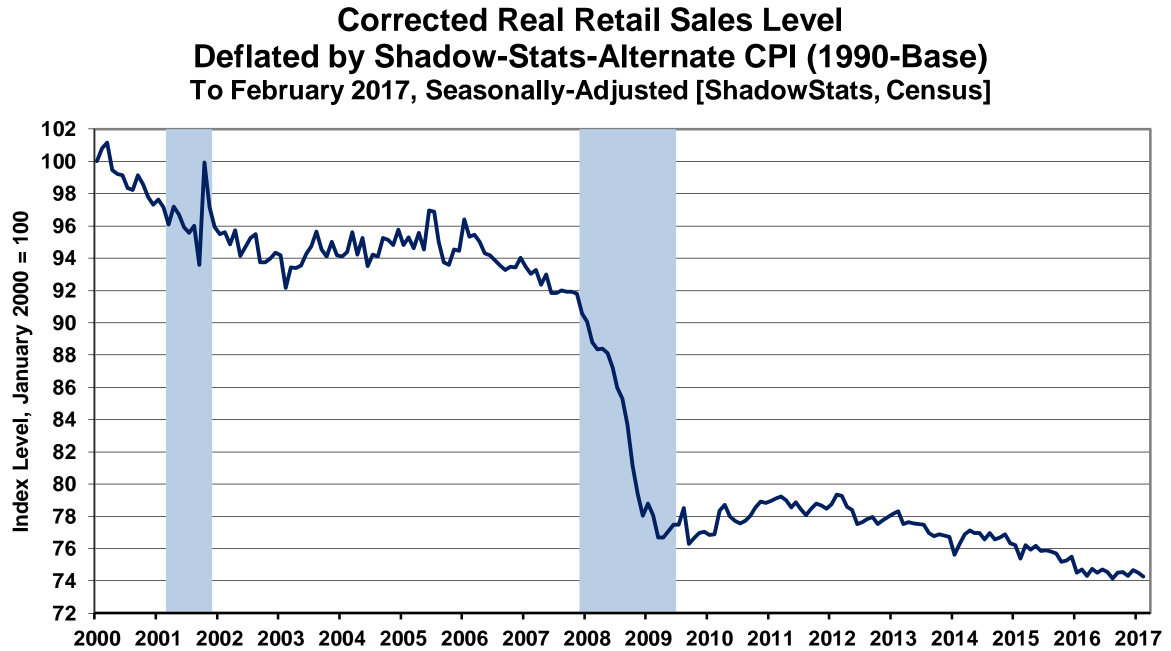
Graph 1: Headline Real Retail Sales Level, Indexed to January 2000 = 100



Graph 2: "Corrected" Real Retail Sales Level, Indexed to January 2000 = 100



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Consumer Price Index (CPI)—February 2017—Annual CPI-U Inflation Rose to a Five-Year High of 2.74%, Up by 0.12% Month-to-Month. The headline February 2017 CPI-U monthly inflation gain was 0.12%, versus 0.55% in January, with both readings depressed by seasonal adjustments. Those adjustments usually lower headline inflation the in first half of the year, versus the second half. Not adjusted for seasonal factors, as most people experience life, headline CPI-U February inflation was 0.31% month-to-month, versus 0.58% in January.

Unadjusted year-to-year inflation jumped to a 60-month high of 2.74% in February 2017, versus 2.50% in January 2017. The current inflation surge continued to be driven by gasoline prices, not by an overheating economy. Unadjusted, year-to-year gasoline costs in December 2016 broke above zero for the first time since the oil-price collapse of July 2014, and strongly so, to 9.15%. The annual gain in January 2017 gasoline prices surged to 20.27% and jumped again in February 2017 to 30.66%.

Although headline annual February CPI-U inflation hit a five-year high of 2.7%, year-to-year inflation is not and has not been quite as low as indicated, when considered in the context of traditional CPI reporting and common experience. The ShadowStats-Alternate Inflation Measures showed year-to-year inflation in February 2017 of 6.3%, based on 1990 methodologies, and 10.5%, based on 1980 methodologies.

Where the Consumer Price Index for All Urban Consumers (CPI-U) is the broadest headline consumer-inflation number, used to adjust numerous economic measures such as retail sales for inflation effects (see the *Retail Sales*, *Nominal and Real* section in the *Reporting Detail*), the narrower Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) is used for deflating measures such as earnings for production and nonsupervisory employees on private nonfarm payrolls. February 2017 seasonally-adjusted CPI-W rose month-to-month by 0.06%, versus 0.81% in January 2017. Unadjusted, year-to-year change in the February 2017 CPI-W was a gain of 2.82%, up from 2.51% in January 2017.

However measured, the small upturn in February 2017 consumer inflation was enough to turn minimally-positive nominal month-to-month growth in nominal retail sales to a minimally-negative month-to-month decline, and to set up real average weekly earnings for quarterly real contractions in a manner not seen since the almost flat activity in second-half 2012 real GDP, circumstances commonly seen only during formal recessions.

Real Average Weekly Earnings—February 2017—On Track for Consecutive Quarterly Contractions and a Quarterly Year-to-Year Downturn. In the production and nonsupervisory employees category—the only series for which there is a meaningful history, the regularly-volatile real average weekly earnings, deflated by the CPI-W, were up by 0.12% month-to-month in February 2017, having declined in January by a deeper, revised 0.52% (-0.52%), the sixth consecutive monthly decline for the series.

Year-to-year, the adjusted February 2017 annual detail declined for the third straight month, down by 0.39% (-0.39%), versus a deeper revised January 2017 annual decline of 0.51% (-0.51%) and an unrevised annual decline of 0.07% (-0.07%) in December 2016.

Such left fourth-quarter 2016 in an unrevised 1.36% (-1.36%) annualized real quarter-to-quarter contraction, with first-quarter 2017 on track for an annualized quarterly contraction of 2.00% (-2.00%), based on two months of reporting.

Year-to-year change in first-quarter 2017 Real Earnings also is on track for the first annual contraction since fourth-quarter 2012, down at a year-to-year pace of 0.51% (-0.51%). Where month-to-month

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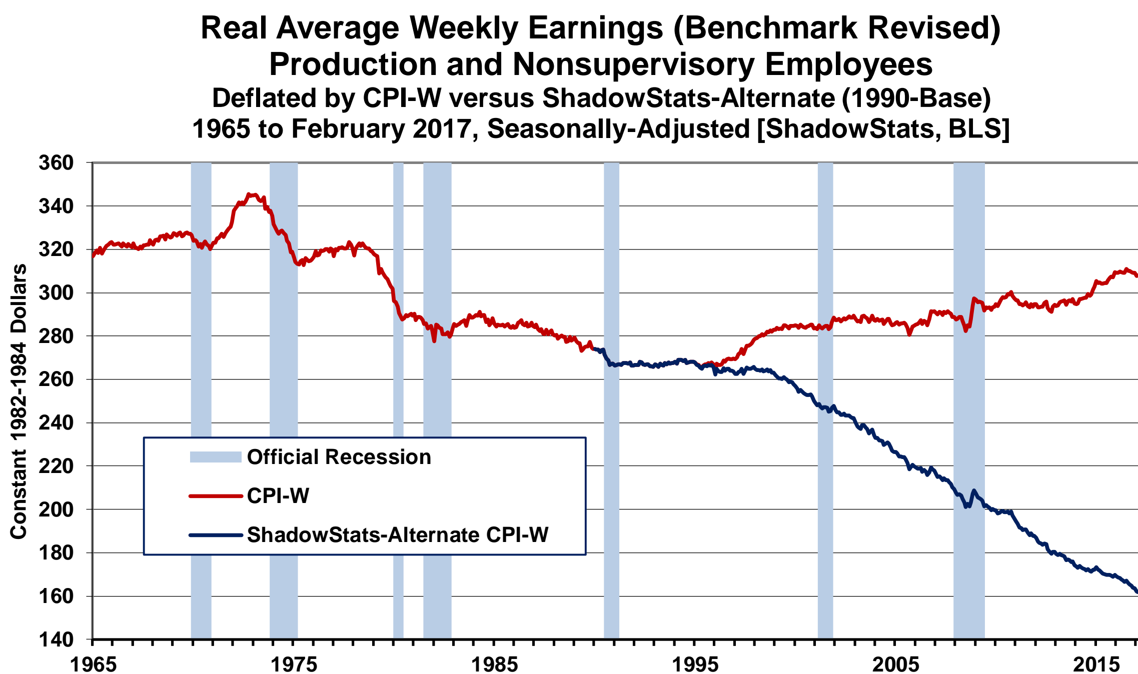
growth in real earnings for March 2017 would have to hit 1.5% to avoid such an annual contraction, monthly growth has not broken above 1.0% in the entire period of purported economic recovery, post-2009. Neither consecutive quarterly contractions nor a quarterly year-to-year contraction has been seen since second-half 2012, when headline GDP growth slowed to a stall.

Graph 3 plots the seasonally-adjusted earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially-weakened CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been in a minimal uptrend for the last two decades (albeit spiked recently by negative headline inflation). Deflated by the ShadowStats (1990-Based) measure, real earnings have been in fairly-regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See the *Public Commentary on Inflation Measurement* for further detail.

Graph 3: Real Average Weekly Earnings, Production and Nonsupervisory Employees, 1965-to-Date



Producer Price Index (PPI)—February 2017—Headline PPI Goods Inflation Rose by 0.27%; Construction Inflation Declined by 0.09% (-0.09%); Dominant Margins in the Services Sector Rose by 0.45%; with Aggregate PPI Inflation Up by 0.27%. Still reflecting surging energy inflation, the year-to-year gain in the aggregate Final-Demand PPI rose from 1.73% in January 2017, to 2.19% in February 2017, a 59-month high, catching up with the annual inflation pattern seen in January's CPI-U.

The headline month-to-month February 2017 PPI inflation of 0.27%, which softened from 0.63% in January, generally reflected neither real-world activity, nor common experience, except by coincidence,

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as discussed in the *Reporting Detail*. As structured, the monthly wholesale inflation rate remains dominated by usually softer inflation in the services sector, which frequently mutes the monthly inflation gains on the product side, seen particularly in the energy sector, although such was not the case in February.

Resurgent Annual Energy Inflation Continued. Headline PPI goods inflation rose month-to-month by 0.27% in February 2017, versus 1.01% in January, and 0.55% in December 2016. Unadjusted annual inflation there rose by 3.87% in February 2017, versus 3.10% in January 2017 and 1.87% in December 2016, still dominated by surging energy costs. Such is the closest the Bureau of Labor (BLS) comes these days to reporting wholesale inflation as it did for the decades leading into a scrapping of the traditional system in January 2014.

Year-to-year change in annual energy inflation continued to explode in February 2017, up by 19.17%, following annual gains of 13.98% in January 2017 and 5.89% in December 2016. Those three months reflected the first meaningful annual pickup in energy inflation since the 2014 collapse in oil prices.

On balance, with profit-margin gains in the dominant services area up month-to-month by 0.45% in February 2017, 0.27% in January 2017 and 0.09% in December 2016 (softened by rising gasoline prices), and the margin-distorted construction industry inflation down by 0.09% (-0.09%) in February 2017, following a monthly gain of 0.26 % in January and a December decline of 0.09% (-0.09%), the headline monthly goods inflation gain of 0.27% in February ended up as the average for the aggregate index.

Aside from the irregular distortions to the headline detail from estimating wholesale inflation versus profit margins in the services sector, regular monthly revisions for October 2016, based on the February 2017 detail, indicated highly unstable surveying/reporting in trade services (see the *Reporting Detail*).

[The* Reporting Detail *contains significant further analysis and graphs on Retail Sales, the CPI and related series and detail on the PPI.]

REPORTING DETAIL

RETAIL SALES – Nominal and Real (February 2017)

Muted by Upside Revisions, February's Headline Nominal Retail Sales Growth Fell Below Headline Inflation Detail. In the context of upside revisions to previously reported activity in January 2017 and December 2016, nominal retail sales in February gained 0.08% for the month, which fell shy of the headline 0.12% monthly gain in CPI-U, leaving the headline real contraction for the monthly activity at

0.04% (-0.4%). Net of prior-period revisions, headline February growth would have been 0.39%. Reflecting softer automobile sales in February 2017, and downside revisions to same in January 2017 and December 2016, current headline retail sales reporting remains heavily distorted, with more-reliable month-to-month detail not likely to be published before the benchmark revisions of 2019 (see 2017 Notice that follows).

Nominal (Not-Adjusted-for-Inflation) Retail Sales—February 2017. In the context of an upside revision to the level of December 2016 activity, the Census Bureau reported this morning, March 15th, that headline nominal February 2017 Retail Sales rose by 0.08% month-to-month, versus an upwardly-revised 0.64% [previously 0.36%] monthly gain in January 2017 and a 0.98% [previously 0.95%, initially 0.63%] monthly gain in December 2016.

That seasonally-adjusted, headline February 2017 gain of 0.08% +/- 0.59% was not statistically-significant (all confidence intervals are expressed at the 95% level). Net of prior-period revisions, February 2017 sales gained by 0.39%, which still would have been insignificant. The revised headline January 2017 monthly retail sales gain of 0.98% +/- 0.23%, however, was statistically-insignificant. There were no unusually-large revisions suggested, in the context of the seasonal-factor distortions detectable in today's limited availability of just five months of consistently-reported detail.

Year-to-Year Annual Change. The January 2017 nominal year-to-year change in Retail Sales showed a statistically-significant increase of 5.86% +/- 0.82%, versus an upwardly revised 6.01% [previously 5.56%] annual gain in January 2017 and a revised 4.39% [previously 4.35%, initially 4.13%] annual gain in December 2016.

February Core Retail Sales, Net of Food and Gasoline. Reflecting an environment that should be seeing rising, seasonally-adjusted food prices and but weaker gasoline prices [an unadjusted February decline of 1.7% (-1.7%) per the Department of Energy], seasonally-adjusted grocery-store sales were unchanged at 0.00% month-to-month, with gasoline-station sales declined by 0.64% in February 2017.

Under normal conditions, the bulk of non-seasonal variability in food and gasoline sales is in pricing, instead of demand. "Core" retail sales—consistent with the Federal Reserve's historical preference for ignoring food and energy prices when "core" inflation is lower than full inflation (when the Fed is looking to downplay inflation)—are estimated using two approaches:

Version I: February 2017 versus January 2017 seasonally-adjusted retail sales series—net of total grocery store and gasoline-station sales—rose by 0.16%, versus the official headline aggregate sales gain of 0.08%.

Version II: February 2017 versus January 2017 seasonally-adjusted retail sales series—net of the monthly change in the level of revenues for grocery stores and gas stations—by 0.13%, versus the official headline aggregate sales gain of 0.08%.

Annual Retail Sales Benchmark Revision Set for April 26th. The Census Bureau intends to publish its annual benchmark revision of the series on April 26, 2017, encompassing the 2015 Annual Retail Trade Survey. Where these benchmarkings can be squirrelly, they most often downgrade prior economic activity, although last year's revisions were relatively minor (see *Commentary No. 804*). ShadowStats will publish an analysis of the detail within a couple of days of the publication.

Real Retail Sales (Adjusted for Inflation)—February 2017. The headline detail from today's coincident (March 15th) release of the February 2017 CPI-U, showed month-to-month, seasonally-adjusted CPI-U inflation of 0.12% in February 2017, 0.55% in January 2017 and 0.26% in December 2016, with year-to-year seasonally-adjusted CPI-U inflation of 2.80% in February 2017, 2.54% in January 2017 and 2.09% in December 2016. Accordingly, real monthly sales declined by 0.04% (-0.04%) in February 2017, versus a real gain of 0.09% [previously down by 0.19% (-0.19%)] in January 2017, and a revised gain of 0.73% [previously 0.69%] in December 2016. Real annual Retail Sales growth was 2.79% in February 2017, versus a revised 3.38% [previously 2.95%] in January 2017 and a revised 2.25% [previously 2.22%, initially 1.99%] in December 2016.

Intense Signal of Recession in Annual Real Growth Remained in Temporary Abeyance. During normal economic times, annual real growth in Retail Sales at or below 2.0% signals an imminent recession. That signal broadly has been in play since February 2015 (the "new" recession likely will be timed from December 2014, based on industrial production, retail sales and other indicators), suggesting a deepening, broad economic downturn. Where December 2016 previously was at 1.99% and 2.22%, and where January 2017 came in at 2.95% now 3.38%, going against a very weak January 2016, and where February 2016 has come in at 2.79%, in the context of revised CPI-U adjusted growth patterns and late headline detail, that signal is in temporary abeyance.

First-Quarter 2017 Annualized Real Growth on Track to Soften versus Fourth-Quarter 2016. First-Quarter 2017 is set on an early trend for annualized quarter-to-quarter real growth of 2.03% [previously 1.00% based just on initial January reporting] in Retail sales, versus a revised annualized pace of 4.02% [previously 3.98%, initially 3.21%] in fourth-quarter 2016, versus an unrevised third-quarter 2016 pace of 2.02%, versus a revised 1.58% [previously 3.81%] annualized growth in second-quarter 2016, versus a revised estimate of annualized quarterly real contraction of 0.94% (-0.94%) [previously 0.58% (-0.58%)] in first-quarter 2016.

Structural Liquidity Issues Continue to Impair Retail Sales. An extreme consumer-liquidity bind continues to constrain retail sales activity, as updated in the *Consumer Liquidity Conditions* section of prior *Commentary No. 871* and as fully reviewed in the *CONSUMER LIQUIDITY* section of *No. 859 Special Commentary*. 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 domestic personal consumption, including retail sales, real or nominal. That circumstance—in the last nine-plus years of economic collapse and stagnation—has continued to prevent a normal recovery in broad U.S. economic activity, 70% of which is dependent on personal spending.

As headline consumer inflation continues its upside climb in the year ahead, and as overall Retail Sales continue to suffer from the ongoing consumer liquidity squeeze, the real Retail Sales data generally should continue to trend meaningfully lower, in what eventually still should gain recognition as a formal "new" recession.

Real Retail Sales Graphs. *Graph 4*, the first of the four graphs following, shows the level of real retail sales activity (deflated by the CPI-U) since 2000; *Graph 5* shows the year-to-year percent change for the same period. Annual real growth had slowed markedly into fourth-quarter 2015 and 2016, generating an intense recession signal, with some recent upturn in annual real growth. *Graphs 6* and *7* show the level of, and annual growth in, real retail sales (and its predecessor series) in full post-World War II detail.

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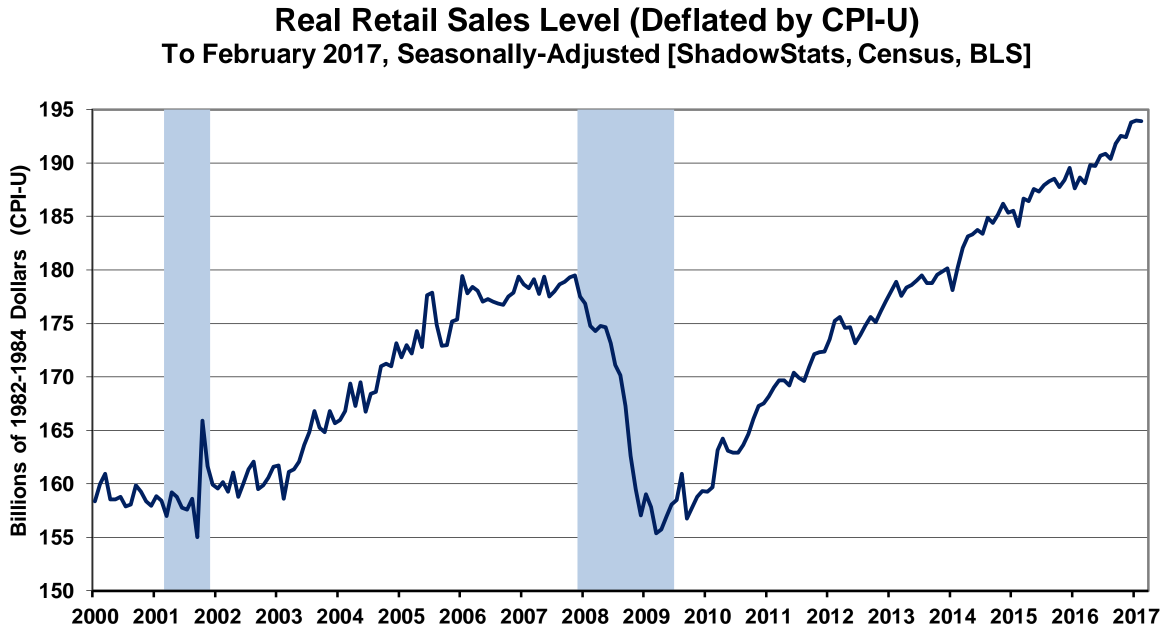
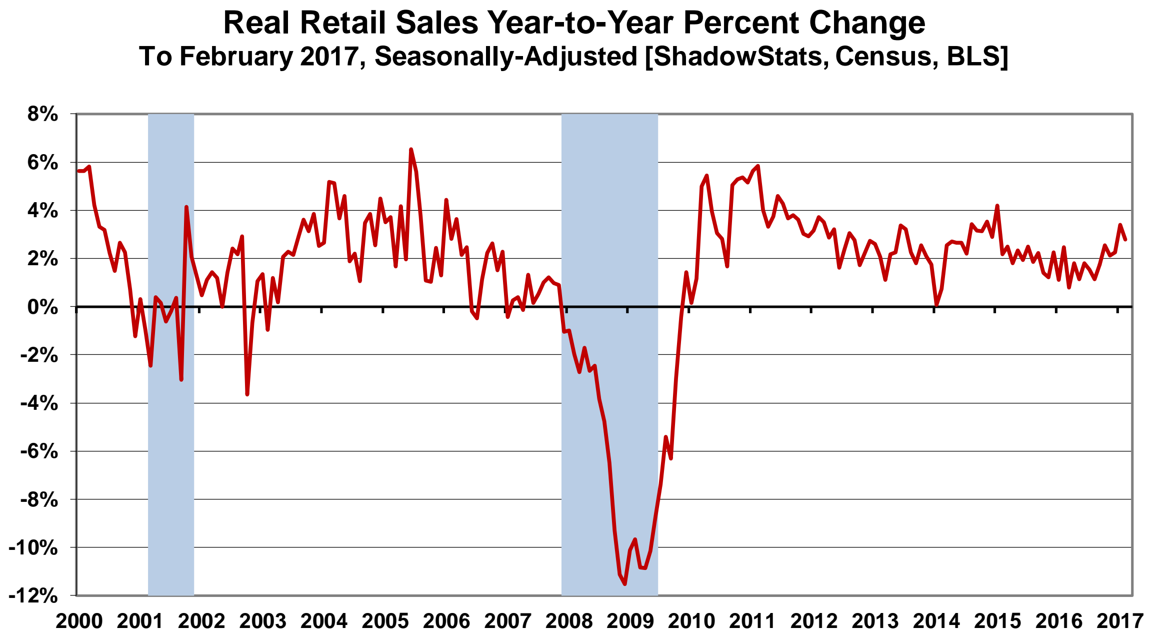
Graph 4: Level of Real Retail Sales (2000 to Date)



Graph 5: Real Retail Sales (2000 to Date), Year-to-Year Percent Change



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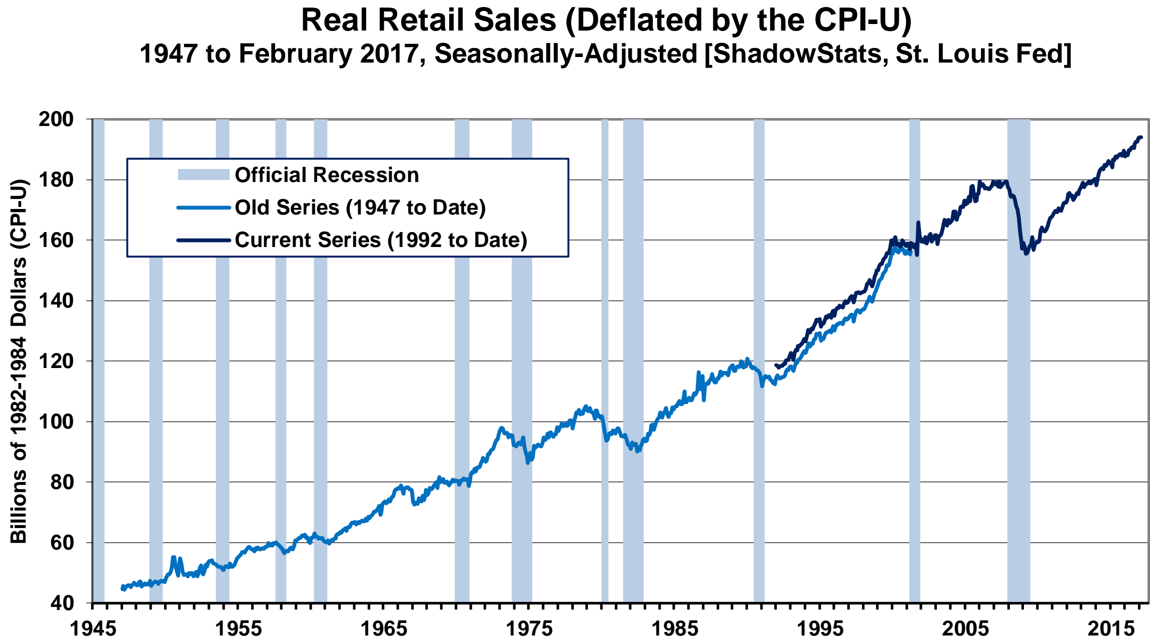
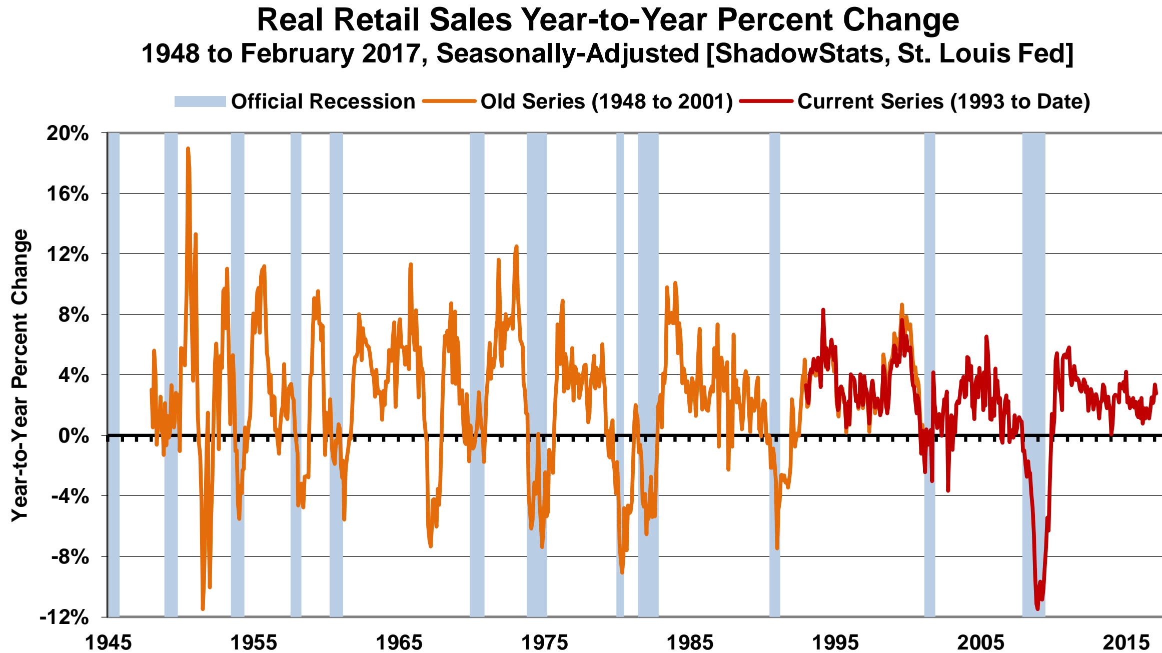
Graph 6: Level of Real Retail Sales (1947 to Date)



Graph 7: Real Retail Sales (1948 to Date), Year-to-Year Percent Change



The relative strength seen in the real retail series since the economic trough in 2009 largely has reflected the understatement of the rate of inflation used in deflating the series. Discussed more fully in *Chapter 9* of *2014 Hyperinflation Report—Great Economic Tumble – Second Installment*, deflation by too low an

inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted, real economic growth. Shown in the latest "corrected" real retail sales—*Graph 2* in the *Executive Summary* section—with the deflation rates corrected for the understated inflation reporting of the CPI-U, the recent pattern of real sales activity has turned increasingly negative. The corrected graph shows that the post-2009 period of protracted stagnation ended, and a period of renewed and ongoing contraction began in second-quarter 2012 and continues to date. The corrected real retail sales numbers use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation instead of the CPI-U.

CONSUMER PRICE INDEX—CPI (February 2017)

Headline CPI-U Inflation Rose by 0.1% for the Month, 2.7% Year-to-Year. In the context of entry into the first-half of a calendar year, with a regular pattern of downside seasonal-adjustments to month-to-month CPI reporting—from January through June—the headline February 2017 CPI-U monthly inflation gain of 0.1% [up by 0.12% at the second decimal point] was the consensus. Not adjusted for seasonal factors, however, as most people experience life, headline CPI-U February inflation was 0.31% month-to-month.

Unadjusted year-to-year inflation jumped to a 60-month high of 2.7% [up by 2.74% at the second decimal point]. The current inflation surge continued to be driven by gasoline prices, not by an overheating economy. Unadjusted, year-to-year gasoline costs in December 2016 broke above zero for the first time since the oil-price collapse of July 2014, and strongly so, to 9.15%. The annual gain in January 2017 gasoline prices surged to 20.27% and jumped again in February 2017 to 30.66%.

With adjusted and unadjusted monthly contractions in the energy sector, the monthly February inflation gains of 0.12% (adjusted) and 0.31% (unadjusted) were driven by a combination of rising prices in the food and "core" (ex-food and energy), again, on both adjusted and unadjusted bases.

Separately, although headline annual February 2017 CPI-U inflation hit a five-year high of 2.7%, year-to-year inflation is not and has not been quite as low as indicated, when considered in the context of traditional CPI reporting and common experience. The ShadowStats-Alternate Inflation Measures showed year-to-year inflation in February 2017 of 6.3%, based on 1990 methodologies, and 10.5%, based on 1980 methodologies.

Longer-Range Inflation Outlook. Despite the U.S. dollar strength subsequent to the election and the today's (March 15th) quarter-point FOMC rate hike (see the *Opening Comments*), a tremendous threat to the dollar and systemic liquidity and stability continues, tied to the U.S. Federal Reserve's inability to resolve fundamentally the 2008 financial collapse, other than having bought limited additional time with its emergency stopgap measures (see *No. 859 Special Commentary*). Since the 2008 crisis, domestic- and global-banking systems have not been stabilized in a healthy or sustainable manner. Efforts to stimulate a non-recovering U.S. economy, amidst renewed faltering activity, have been nil, up through the advent of the Trump Administration. Given standard lead times, positive impact from an economic-stimulus package this year would not have significant effect until 2018, at the earliest, a time lapse fraught with potential disaster created by an still-incapacitated Fed, fighting to the death a battle it already lost in the 2008 panic.

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In the context of current economic reporting and signals, faltering economic activity should become increasingly obvious, with related stresses on domestic systemic-liquidity and solvency issues pushing the U.S. central bank back towards expanded quantitative easing by mid-year 2017. Such would generate high risk of extreme flight from the U.S. dollar—a massive dollar debasement—threatening an increasingly-rapid upturn in energy and dollar-based commodity inflation, driving headline U.S. inflation much higher.

Compounding the high-risk of a near-term run on the U.S. dollar remains mounting recognition in global markets that the U.S. Federal Reserve and other central banks still have no effective idea as to how to boost current economic activity, how to stabilize global banking-system solvency, or otherwise how to slog their way out of a self-generated quagmire.

Notes on Different Measures of the Consumer Price Index

The Consumer Price Index (CPI) is the broadest inflation measure published by the U.S. Government, through the Bureau of Labor Statistics (BLS), Department of Labor:

*The **CPI-U (Consumer Price Index for All Urban Consumers)** is the monthly headline inflation number (seasonally adjusted) and is the broadest in its coverage, representing the buying patterns of all urban consumers. Its standard measure is not seasonally-adjusted, and it never is revised on that basis except for outright errors.*

*The **CPI-W (CPI for Urban Wage Earners and Clerical Workers**) covers the more-narrow universe of urban wage earners and clerical workers and is used in determining cost of living adjustments in government programs such as Social Security. Otherwise, its background is the same as the CPI-U.*

*The **C-CPI-U (Chain-Weighted CPI-U)** is an experimental measure, where the weighting of components is fully substitution based. It generally shows lower annual inflation rate than the CPI-U and CPI-W. The latter two measures once had fixed weightings—so as to measure the cost of living of maintaining a constant standard of living—but now are quasi-substitution-based. Since it is fully substitution based, the series tends to reflect lower inflation than the other CPI measures. Accordingly, the C-CPI-U is the "new inflation" measure being proffered by Congress and the White House as a tool for reducing Social Security cost-of-living adjustments by stealth. Moving to accommodate the Congress, the BLS introduced changes to the C-CPI-U estimation process with the February 26, 2015 reporting of January 2015 inflation, aimed at finalizing the C-CPI-U estimates on a more-timely basis, and enhancing its ability to produce lower headline inflation than the traditional CPI-U.*

*The **ShadowStats Alternative CPI-U Measures** are attempts at adjusting reported CPI-U inflation for the impact of methodological change of recent decades designed to move the concept of the CPI away from being a measure of the cost of living needed to maintain a constant standard of living. There are two measures, where the first is based on reporting methodologies in place as of 1980, and the second is based on reporting methodologies in place as of 1990.*

CPI-U. The Bureau of Labor Statistics (BLS) reported this morning, March 15th that the headline, seasonally-adjusted February 2017 2016 CPI-U rose month-to-month by 0.1% (up by 0.12% at the second

decimal point). That followed monthly gains of 0.6% (0.55%) in January, 0.3% (0.26%) in December 2016, 0.2% (0.21%) in November and 0.3% (0.29%) in October.

The adjusted headline February 2017 monthly inflation increase was weakened by mixed seasonal adjustments, minimally boosted by positive seasonal adjustments to the food sector, but heavily hit by negative seasonals in the energy and "core" (ex-food and energy) sectors. On an unadjusted basis, monthly February 2017 CPI-U gained 0.31%, 0.58% in January and 0.03% in December 2016, having declined by 0.15% (-0.15%) in November, and having increased by 0.12% in October.

February 2017 seasonal adjustments for monthly gasoline inflation were negative, "depressing" an unadjusted headline monthly decline of 2.13% (-2.13%) in gasoline prices into a deeper, adjusted decline of 2.96% (-2.96%). The Department of Energy (DOE) had estimated an unadjusted monthly decline in February gasoline prices of 1.71% (-1.71%).

While early-March 2017 retail gasoline prices (DOE) are running higher month-to-month by about 0.9%, severely negative seasonal adjustments to March 2017 gasoline prices easily could push the headline, seasonally-adjusted CPI-U into a month-to-month contraction.

Major CPI-U Groups. Encompassed by the seasonally-adjusted monthly CPI-U gain of 0.12% in February 2017 [up by an unadjusted 0.31%], February food inflation rose by a seasonally-adjusted 0.24% [up by 0.22% unadjusted], February energy inflation declined by a seasonally-adjusted 0.97% (-0.97%) [down by an unadjusted 0.71% (-0.71%)], while the adjusted February "core" (ex-food and energy) inflation rate was up by 0.21% [up by 0.42% unadjusted]. Separately, core CPI-U inflation showed unadjusted year-to-year inflation of 2.22% in February 2017, versus 2.27% in January 2017, 2.20% in December 2016, 2.11% in November 2016 and 2.14% in October 2016.

Year-to-Year CPI-U. Not seasonally adjusted, February 2017 year-to-year inflation for the CPI-U rose to a 60-month high of 2.7% (2.74% at the second decimal point), versus 2.5% (2.50%) in January 2017, 2.1% (2.07%) in December 2016, 1.7% (1.69%) in November 2016 and 1.6% (1.64%) in October 2016.

Year-to-year, CPI-U inflation would increase or decrease in next month's March 2017 reporting, dependent on the seasonally-adjusted month-to-month change, versus the adjusted, headline gain of 0.11% in March 2016 CPI-U. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for March 2017, the difference in March's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the February 2017 annual inflation rate of 2.74%. Given an early guess of a seasonally-adjusted contraction of 0.1% (-0.1%), in the monthly March 2017 CPI-U, that would leave the annual CPI-U inflation rate for March 2017 at about 2.5%, plus-or-minus, depending on rounding.

CPI-W. The February 2017 seasonally-adjusted, headline CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose month-to-month by 0.06%, following gains of 0.61% in January, 0.29% in December 2016, 0.22% in November and 0.32% in October and 0.29%.

On an unadjusted basis, year-to-year CPI-W rose by 2.82% in February 2017, versus 2.51% in January 2017, 1.99% in December 2016, 1.51% in November 2016 and 1.45% in October 2016.

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Chained-CPI-U. The headline C-CPI-U is not seasonally adjusted, but it is revised regularly, as last happened with the January 2017 reporting. Headline February 2017 C-CPI-U annual inflation came in at 2.89%, versus 2.58% in January 2017, 2.07% in December 2016, 1.58% in November 2016 and 1.53% in October 2016.

See discussions in the earlier CPI *Commentary No. 721* and in the opening notes in the *CPI Section* of *Commentary No. 699* as to recent changes in the series. More-frequent revisions and earlier finalization of monthly detail have been designed to groom the C-CPI-U series as the new Cost of Living Adjustment (COLA) index of choice for the budget-deficit-strapped federal government, as discussed in the *Public Commentary on Inflation Measurement*.

Caution: Artificially-low inflation numbers estimated by the U.S. Government and used in fields ranging from Social Security COLAs (see the 2017 CPI-W estimate discussion in *Commentary No. 841*) to determining income-tax brackets, have been redesigned in recent decades specifically to help reduce the federal deficit. They are harmfully misleading to anyone using a government CPI estimate as a meaningful cost-of-living measure for guidance on income or investment purposes.

Alternate Consumer Inflation Measures. The ShadowStats-Alternate Consumer Inflation Measures are constructed on top of the unadjusted CPI-U series. Adjusted to 1990 methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—year-to-year annual inflation was roughly 6.3% in February 2017, versus 6.1% in January 2017, 5.7% in December 2016, 5.3% in November 2016, 5.2% in October 2016 and 5.0% in September 2016.

The February 2017 ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, was at about 10.5% (10.53% at the second decimal point, versus 10.3% (10.27%) in January 2017, 9.8% (9.81%) in December 2016, 9.4% (9.40%) in November 2016, 9.3% (9.34%) in October 2016 and 9.1% (9.15%) in September 2016. Detail, along with an inflation calculator will be found in the CPI section of the Alternate Data tab of the www.ShadowStats.com home page.

Note: The ShadowStats-Alternate Consumer Inflation Measures largely have been reverse-engineered from BLS estimates of the anticipated impact on annual CPI inflation from various changes made to CPI reporting methodology since the early 1980s, as also incorporated in the CPI-U-RS series. That series provides an official estimate of historical inflation, assuming that all current methodologies were in place going back in time. The changes reflected there are parallel with and of the same magnitude of change as estimated by the BLS, when a given methodology was changed.

The ShadowStats estimates are adjusted on an additive basis for the cumulative impact on the annual inflation rate from the various BLS changes in methodology (reversing the net aggregate inflation reductions by the BLS). The series are adjusted by ShadowStats for those aggregate changes, but the series otherwise are not recalculated.

Over the decades, the BLS has altered the meaning of the CPI from being a measure of the cost of living needed to maintain a constant standard of living, to something that neither reflects the constant-standard-of-living concept nor measures adequately what most consumers view as out-of-pocket expenditures. Roughly five percentage points of the additive ShadowStats adjustment since 1980 reflect the BLS's formal estimate of the annual impact of methodological changes; roughly, two percentage points reflect

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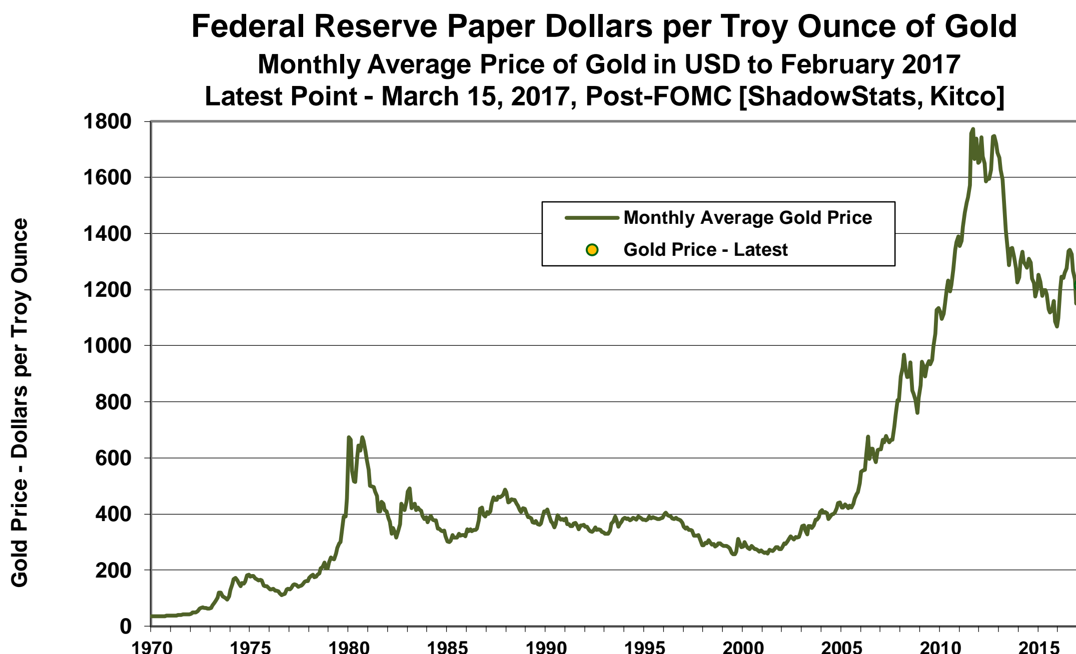
changes by the BLS, where ShadowStats has estimated the impact not otherwise published by the BLS. For example, the BLS does not consider more-frequent weightings of the CPI series or shifting the nature of retail outlets to be changes in methodology. Yet those changes have had the effect of reducing headline inflation from what it would have been otherwise (See Public Commentary on Inflation Measurement *for further details.)*

Graph 8: Monthly Average Gold Price in Dollars (Federal Reserve Notes)



Gold and Silver Historic High Prices Adjusted for February 2017 CPI-U/ShadowStats Inflation—

CPI-U: GOLD at $2,661 per Troy Ounce, SILVER at $155 per Troy Ounce
ShadowStats: GOLD at $13,982 per Troy Ounce, SILVER at $813 per Troy Ounce

Despite the September 5, 2011 historic-high gold price of $1,895.00 per troy ounce (London afternoon fix), and despite the multi-decade-high silver price of $48.70 per troy ounce (London fix of April 28, 2011), gold and silver prices have yet to re-hit their 1980 historic levels, adjusted for inflation. The earlier all-time high of $850.00 (London afternoon fix, per Kitco.com) for gold on January 21, 1980 would be $2,661 per troy ounce, based on February 2017 CPI-U-adjusted dollars, and $13,982 per troy ounce, based on February 2017 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (all series here are not seasonally adjusted).

In like manner, the all-time high nominal price for silver in January 1980 of $49.45 per troy ounce (London afternoon fix, per silverinstitute.org)—although approached in 2011—still has not been hit since 1980, including in terms of inflation-adjusted dollars. Based on February 2017 CPI-U inflation, the 1980 silver-price peak would be $155 per troy ounce and would be $813 per troy ounce in terms of the February 2017 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

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Shown in *Table 1*, on page 47 of [No. 859 Special Commentary](), over the decades, the increases in gold and silver prices have compensated for more than the loss of the purchasing power of the U.S. dollar as reflected by CPI inflation. They also effectively have come close to fully compensating for the loss of purchasing power of the dollar based on the ShadowStats-Alternate Consumer Price Measure (1980-Methodologies Base).

Real (Inflation-Adjusted) Retail Sales—February 2017—Down Month-to-Month by 0.04% (-0.04%), Up Year-to-Year by 2.79%. February 2017 real Retail Sales are covered in the prior *Retail Sales - Nominal and Real* section.

Real Average Weekly Earnings—February 2017—First-Quarter on Solid Track for Quarterly and Annual Contractions, Following Fourth-Quarter Quarterly Decline. The headline estimate for February 2017 real average weekly earnings was published coincident with today's (March 15th) release of the February CPI-W. In the production and nonsupervisory employees category—the only series for which there is a meaningful history, the regularly-volatile real average weekly earnings were up by 0.12% month-to-month in February 2017, having declined in January by a revised 0.52% (-0.52%) [previously down by 0.42% (-0.42%)], the sixth consecutive monthly decline for the series.

Year-to-year, the adjusted February 2017 annual detail declined for the third straight month, down by 0.39% (-0.39%), versus a revised January 2017 annual decline of 0.51% (-0.51%) [previously down by 0.41% (-0.41%)] and an unrevised annual decline of 0.07% (-0.07%) in December 2016.

Such left fourth-quarter 2016 in an unrevised 1.36% (-1.36%) annualized real quarter-to-quarter contraction, versus third-quarter 2016 growth of 1.48%, a second-quarter 2016 annualized contraction of 0.11% (-0.11%) and unrevised first-quarter 2016 annualized growth of 1.81%.

<u>Annual Contraction Now Is a Virtual Certainty for First-Quarter 2017 Real Earnings.</u> With the initial headline February 2017 in place, first-quarter 2017 is on track for an annualized quarter-to-quarter contraction of 2.00% (-2.00%). Based on just the initial January 2017 reporting, the early pace of annualized contraction had been 1.87% (-1.87%).

Year-to-year change in first-quarter 2017 real earnings is on track for the first annual contraction since fourth-quarter 2012, down at a year-to-year pace by 0.51% (-0.51%) [previously 0.47% (-0.47%)]. Where month-to-month growth in real earnings for March 2017 would have to hit 1.5% to avoid such an annual contraction, monthly growth has not broken above 1.0% in the entire purported period of economic recovery, post-2009.

The 2015 rally in real annual income and the subsequent slowdown in latter 2016 were tied directly to the impact of collapsing gasoline prices, and a subsequent rebound in inflation-adjusted income.

While these usually heavily-revised and seasonally-adjusted monthly changes are without much, if any, meaning in the near-term—effectively reporting garbage—over the longer term and quarterly, and particularly the benchmarked trends tend to be of some substance. As with the BLS reporting tied to the nonfarm payrolls, the headline seasonally-adjusted monthly data here are not comparable due to reporting issues with concurrent seasonal factor adjustments (see *Headline Distortions from Shifting Concurrent-Seasonal Factors* in prior [Commentary No. 871]()).

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Separately, the CPI-W deflated reporting here also is biased versus the CPI-U-deflated series, where the CPI-W—more heavily weighted with gasoline prices—tends to have much deeper, negative headline inflation, with resulting stronger headline, real growth than would be seen with the CPI-U, when gasoline prices are falling, and vice versa. Such was true again, in the February 2017 detail, where lower, seasonally-adjusted gasoline prices generated a headline monthly CPI-W gain of 0.06%, versus a CPI-U gain of 0.12%.

Found in the *Executive Summary* section, *Graph 3* plots this series, showing the seasonally-adjusted earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially-weakened headline CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been in a minimal uptrend for the last two decades (albeit spiked recently by negative headline inflation). Deflated by the ShadowStats (1990-Based) measure, real earnings have been in fairly-regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See the *Public Commentary on Inflation Measurement* for further detail.

Real (Inflation-Adjusted) Money Supply M3—February 2017—Annual Growth Has Signaled New Economic Downturn. The signal for a double-dip, multiple-dip or simply protracted, ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), has just been re-triggered, although the prior signal had remained in place, despite real annual M3 growth having rallied in positive territory post-2010. Shown in *Graph 9*—based on February 2017 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in February 2017 M3 plunged to 0.39%, from 1.09% in January 2017, from 1.53% in December 2016 and from a prior peak growth of 5.67% in February 2015. Such has reflected rapidly slowing nominal annual M3 growth (see *Commentary No. 871*) and rapidly rising annual CPI-U inflation.

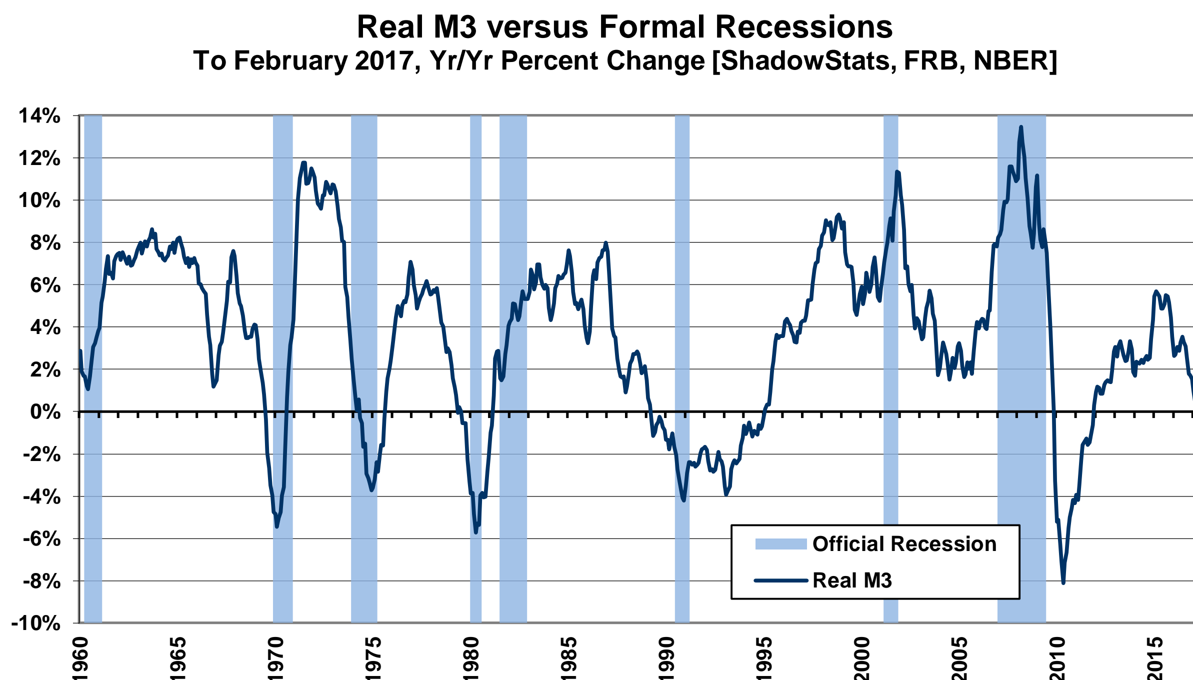
The current growth pattern has fallen to the level last seen in plunging growth into the 2009 economic collapse, and at a level always seen going into or already in a recession.

The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first slows sharply, approaches zero and turns negative in a given cycle; the signal is not dependent on the depth of the downturn or its duration. Breaking into positive territory does not generate a meaningful signal one way or the other for the broad economy. The previous "new" downturn signal was generated in December 2009, even though there had been no upturn since the economy purportedly hit bottom in mid-2009. The ongoing issue here confounding the regular signal is that the U.S. economy never has recovered fully from its collapse into 2009 (see *Commentary No. 869*). The initial economic downturn never evolved into a meaningful or sustainable recovery. The current level and pattern of real annual M3 growth always has been followed by annual contraction and recession signal.

Again, when real M3 growth breaks above zero, there is no signal; the signal is generated only when annual growth moves to zero and into negative territory, where it continues to head at present. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of economic series have continued to the present, with significant new softness in recent reporting. Actual post-2009 economic activity has remained at relatively low levels of

activity—in protracted stagnation, with no actual recovery (see *Graphs 2* and *3* in the *Opening Comments*, [Commentary No. 869](#) and the *ECONOMY* section of [No. 859 Special Commentary](#)).

Graph 9: Real M3 Annual Growth versus Formal Recessions



Despite the purported, ongoing recovery shown in headline GDP activity, a renewed downturn in official data is underway that likely still will gain official recognition as a "new" recession, in the first-half of 2017. Underlying reality remains that the collapse into 2009 was followed by a plateau of low-level economic activity—no meaningful upturn, no recovery from or end to the official 2007 recession—and the unfolding "new" downturn remains nothing more than a continuation and re-intensification of the downturn that began unofficially in 2006.

PRODUCER PRICE INDEX (February 2017)

Final Demand PPI Annual Inflation Hit a 59-Month High. In the context of monthly PPI goods inflation rising by 0.27%, construction inflation declining by 0.09% (-0.09%), the dominant "margins" in the services sector rising by 0.45% and the aggregate Final-Demand PPI monthly inflation up by 0.27%, year-to-year change in that aggregate February 2017 PPI inflation rose by 2.19%, to a five-year high. The increased inflation did not reflect an overheating economy, only energy-price distortions that have been rigged heavily through the Federal Reserve's dollar propping gimmicks and recent OPEC supply issue jawboning.

Year-to-Year Energy Inflation Continued Meaningfully to the Plus-Side, for the Third Month. The continued jump in the old-fashioned goods inflation was dominated, once again, by higher energy prices. Not-seasonally-adjusted annual change in energy inflation continued to soar, up by 19.17% in February 2017, versus 13.98% in January 2017 and having jumped meaningfully—for the first time since the 2014

collapse in oil prices—into positive territory in December 2016. The annual energy inflation surge in the January 2017 was preceded by a 5.89% year-to-year gain in December 2016, which followed minor flutterings of an annual decline of 0.11% (-0.11%) in November 2016, a gain of 0.53% in October 2016, annual declines of 2.89% (-2.89%) in September 2016, 9.98% (-9.98%) in August 2016, and so on, back to fourth-quarter 2014.

The headline monthly Final-Demand PPI inflation generally reflects neither real-world activity, nor common experience, except by possible coincidence. As structured, the monthly wholesale inflation rate remains dominated by the services sector, which remains of negligible real-world value.

Services-Side Nonsense Detail. Separately, while the services component of the PPI has negligible theoretical value, as discussed in the *Bulk of Reporting Is of Little Practical Use* section, it also has proven to be highly unstable in its surveying and related reporting. Consider that the monthly PPI detail is subject to revision five months after its initial reporting. Those changes usually are small.

For the October 2016 PPI revision this month, the headline monthly change revised from an initial month-to-month contraction of 0.1% (-0.1%) to a monthly increase of 0.3%. The primary culprit in that was an upside revision to the "profit margins" in the trade services sector (see *Inflation That Is More Theoretical than Real World*), taking that component from a headline October 2016 monthly decline of 1.2% (-1.2%), as initially reported, to a revised monthly gain of 0.4% in the just-revised detail.

Bulk of Reporting Is of Little Practical Use. *[The background text here and in the next subsection is as published previously.]* Beyond the broad issues with general inflation measurement (see *Public Commentary on Inflation Measurement*), indeed the bulk of the PPI is covered by the "services" sector, where inflation is determined largely by shifting profit margins. Discussed in the next subsection, profit-margin inflation estimates generally are handled in a manner counter-intuitive to the more-traditional measurement of inflation in goods and services, otherwise calculated as a measurement of change in prices. Accordingly, the headline detail here increasingly has a limited relationship to real-world activity.

The conceptual differences between goods inflation and services profit margins do not blend well and are not merged easily or meaningfully in the current version of the PPI. While, the dual measures are more meaningfully viewed independently than as the hybrid measure of the headline Producer Price Index Final Demand—ShadowStats separates the analyses of those sectors by sub-category—the aggregate headline series here also is reviewed and covered within the headline reporting conventions of the Bureau of Labor Statistics (BLS).

Inflation That Is More Theoretical than Real World. Effective with January 2014 reporting, a new Producer Price Index (PPI) replaced what had been the traditional headline monthly measure of wholesale inflation in Finished Goods (see *Commentary No. 591*). In the new headline monthly measure of wholesale Final Demand, Final Demand Goods basically is the old Finished Goods series, albeit expanded.

The new otherwise dominant Final Demand Services sector largely reflects problematic and questionable surveying of intermediate or quasi-wholesale profit margins in the services area. To the extent that profit margins shrink in the services sector, one could argue that the resulting lowered estimation of inflation actually is a precursor to higher inflation, as firms subsequently would move to raise prices, in an effort to regain more-normal margins. In like manner, in the circumstance of "increased" margins—due to the

lower cost of petroleum-related products not being passed along immediately to customers—competitive pressures to lower margins would tend to be reflected eventually in reduced retail prices (CPI). The oil-price versus margin gimmick works both way. In times of rapidly rising oil prices, it mutes the increase in Final Demand inflation, in times of rapidly declining oil prices; it tends to mute the decline in Final Demand inflation.

The current PPI series remains an interesting concept, but it appears limited as to its aggregate predictive ability versus general consumer inflation. Further, there is not enough history available on the new series (just seven years of post-2008-panic data) to establish any meaningful relationship to general inflation or other economic or financial series.

February 2017 Headline PPI Detail. The Bureau of Labor Statistics (BLS) reported March 14th, that the seasonally-adjusted, month-to-month, headline Producer Price Index (PPI) Final Demand inflation for February 2017 was 0.27%. That was against monthly gains of 0.63% in January, 0.18% in December 2016 and a revised 0.09% [previously 0.45%] monthly gain. The November index level was not revised, but the monthly change reflected the impact of a revised 0.27% gain in the level [previously down by 0.09% (-0.09%)] of the index for October. On a not-seasonally-adjusted basis—all annual growth rates are expressed unadjusted—year-to-year PPI Final Demand inflation in February 2017 was a 59-month high of 2.19%, versus 1.64% in January 2017, 1.65% in December 2016, 1.28% in November 2016 and a revised 1.09% [previously 0.82%] in October 2016.

For the three major subcategories of February 2017 Final Demand PPI, headline monthly Goods inflation rose by 0.27%, Services “inflation” (profit margins) gained 0.45% and Construction inflation declined by 0.09% (-0.09%), with respective unadjusted annual growth rates of 4.05%, 1.44% and 1.23%.

Final Demand Goods (Weighted at 33.84% of the Aggregate Index). Running somewhat in parallel with the old Finished Goods PPI series, headline month-to-month Final Demand Goods inflation in February 2017 rose by 0.27%, having gained by 1.01% in January and 0.55% in December 2016. There was neutral impact on the aggregate goods headline reading from underlying seasonal-factor adjustments. Not-seasonally-adjusted, February Final Demand Goods inflation also was 0.27%.

Unadjusted, year-to-year goods inflation in February 2017 showed an annual gain of 3.87%, following gains of 3.10% in January 2017 and 1.87% in December 2016.

Headline seasonally-adjusted monthly changes by major components of the February 2017 Final Demand Goods:

- “Foods” inflation (weighted at 5.43% of the total index) gained 0.35% month-to-month in February 2017, having been unchanged at 0.00% in January 2017 and having gained 0.53% in December 2016. Seasonal adjustments were negative for the February headline change, which was up by 0.44% unadjusted. Unadjusted and year-to-year, annual February 2017 foods inflation declined by 1.80%, having declined by 2.23% (-2.23%) in January 2017 and by 1.12% (-1.12%) in December 2016.
- “Energy” inflation (weighted at 5.49% of the total index) rose by 0.60% in February 2017, having gained 4.69% in January 2017 and 1.80% month-to-month in December 2016. Seasonal adjustments were minimally negative, with unadjusted monthly energy inflation up by 0.62% in

the month. Unadjusted and year-to-year, February 2017 energy prices continued to soar, up by 19.17% in February 2017, versus 13.98% in January 2017 and 5.89% in December 2016.

- "Less foods and energy" ("Core" goods) monthly inflation (weighted at 22.92% of the total index) rose by 0.09% in February 2017, having gained 0.36% in January 2017 and 0.27% in December 2016. Seasonal adjustments were positive for monthly core inflation, with an unadjusted monthly activity unchanged at 0.00%. Unadjusted and year-to-year, February 2017 was up by 2.00%, versus gain of 2.09% in January 2017 and 1.73% in December 2016.

Final Demand Services (Weighted at 64.09% of the Aggregate Index). Headline monthly Final Demand Services inflation rose by 0.45% in February 2017, having gained 0.27% in January 2017 and 0.09% in December 2016. The overall seasonal-adjustment impact on headline February services inflation was negative, with an unadjusted monthly gain of 0.71%. Year-to-year, unadjusted February 2017 services rose by 1.44%, versus annual gains of 0.81% in January 2017 and 1.55% in December 2016.

The headline monthly changes by major component for February 2017 Final Demand Services inflation:

- "Services less trade, transportation and warehousing" inflation, or the "Other" category (weighted at 38.87% of the total index), rose by 0.54% month-to-month, having declined by 0.09% (-0.09%) in January 2017 and having gained 0.09% in December 2016. Seasonal-adjustment impact on the adjusted February detail was neutral, where the unadjusted monthly reading also was a gain of 0.54%. Unadjusted and year-to-year, February 2017 "other" services inflation was up by 1.64%, having gained 1.28% in January 2017 and 2.02% in December 2016.
- "Transportation and warehousing" inflation (weighted at 4.94% of the total index) rose month-to-month in February 2017 by 0.26%, having gained 1.14% in January 2017, and having declined by 0.26% (-0.26%) in December 2016. Seasonal adjustments were positive for the headline February reading, where the unadjusted monthly number was unchanged at 0.00%. Unadjusted and year-to-year, February 2017 transportation inflation was up by 1.59%, having gained 1.05% in January 2017 and having been "unchanged" at 0.00% in December 2016.
- "Trade" inflation (weighted at 20.28% of the total index) increased month-to-month in February 2017 by 0.35%, having gained 0.88% in January 2017 and having been "unchanged" at 0.00% in December 2016. Seasonal adjustments had a negative impact here, where the unadjusted monthly change was a gain of 1.06%. Unadjusted and year-to-year, February 2017 trade inflation rose to 0.88%, from 0.09% in January 2017 and versus a gain of 0.98% in December 2016.

Final Demand Construction (Weighted at 2.08% of the Aggregate Index). Although a fully self-contained subsection of the Final Demand PPI, Final Demand Construction inflation receives no formal headline coverage. Month-to-month construction inflation contracted by 0.09% (-0.09%) in February 2017, having gained 0.26% in January 2017 and having declined 0.09% (-0.09%) in December 2016. The impact of seasonal factors on the February reading was neutral, where the unadjusted monthly change also was a contraction of 0.09% (-0.09%). The issues here are a combination of monthly headline cost changes along with a quarterly estimate of contractor profit-margin changes that have little connection to real-world activity. The latter circumstance was addressed in *Commentary No. 829* of September 2, 2016.

On an unadjusted basis, year-to-year construction inflation rose by 1.23% in February 2017, versus 1.32% in January 2017 and 0.61% in December 2016. Private surveys are showing much higher construction-related inflation than is reported in the PPI, by an order of magnitude of a couple of hundred basis points,

such as reflected in the privately-published Building Cost and Construction Cost Indices [Dodge Data and Analytics (McGraw Hill) *Engineering News-Record*] and in construction-related price deflators in the National Income Accounts, such as the Gross Domestic Product (GDP). Discussed in *Commentary No. 829*, ShadowStats has constructed a Composite Construction Deflator (CCD) now used by ShadowStats in deflating the Census Bureau's monthly estimates of Construction Spending Put in Place in the United States.

PPI-Inflation Impact on Pending Reporting of New Orders for Durable Goods. As to the upcoming reporting of February 2017 new orders for durable goods, monthly inflation (reported only on a not-seasonally-adjusted basis) for new orders for manufactured durable goods in February 2017 was 0.18%, versus 0.30% in January and 0.18% in December 2016. Year-to-year annual inflation continued to rise, hitting 1.45% in February 2017, versus 1.33% in January 2017 and 0.97% in December 2016. February 2017 durable goods orders (both nominal and real) will be reported on March 24th and covered in the ShadowStats *Commentary* of that date.

WEEK, MONTH AND YEAR AHEAD

Despite Today's (March 15th) Rate Hike, Continued Economic Woes Promise a Compromised, Frustrated Fed and Deteriorating U.S. Dollar Support. The outlook for future FOMC actions and the assessment of current economic activity will be reviewed in the next two *Commentaries* (*Nos. 873* and *874*), as discussed in today's *Opening Comments.*

Accordingly, this opening section of the *Week, Month and Year Ahead* will not be separately updated until *Commentary No. 875*, planned for March 24th.

Prior General Background. Separately, *No. 859 Special Commentary* updated near-term economic and inflation conditions, and the outlook for same, including the general economic, inflation and systemic distortions evolving out of the Panic of 2008 that have continued in play, and which need to be addressed by the new Administration in the immediate future (see also the *Hyperinflation Watch* of *Commentary No. 862* and *Commentary No. 869*).

Contrary to the official reporting of an economy that collapsed from 2007 into 2009 and then recovered strongly into ongoing expansion, underlying domestic reality remains that the U.S. economy started to turn down somewhat before 2007, collapsed into 2009 but never fully recovered. While the economy bounced off its 2009 trough, it entered a period of low-level stagnation and then began to turn down anew in December 2014, a month that should mark the beginning of a "new" formal recession (see *General Commentary No. 867*).

Coincident with and tied to the economic crash and the Panic of 2008, the U.S. banking system moved to the brink of collapse, a circumstance from which U.S. and global central bank policies never have recovered. Unwilling to admit its loss of systemic control, the Federal Reserve has been making loud noises of raising interest rates, in order to contain an overheating economy. As this ongoing crisis evolves towards its unhappy end, the U.S. dollar ultimately should face unprecedented debasement with a resulting runaway domestic inflation.

Broad economic and systemic conditions are reviewed regularly, with the following *Commentaries* of particular note: *No. 777 Year-End Special Commentary* (December 2015), *No. 742 Special Commentary: A World Increasingly Out of Balance* (August 2015) and *No. 692 Special Commentary: 2015 - A World Out of Balance* (February 2015). Those publications updated the long-standing hyperinflation and economic outlooks published in *2014 Hyperinflation Report—The End Game Begins – First Installment Revised* (April 2014) and *2014 Hyperinflation Report—Great Economic Tumble – Second Installment* (April 2014). The two *Hyperinflation* installments remain the primary background material for the hyperinflation circumstance. Other references on underlying economic reality are the *Public Commentary on Inflation Measurement* and the *Public Commentary on Unemployment Measurement*.

Recent Commentaries:

Commentary No. 871 covered February Labor Conditions, updated Consumer Liquidity and the ShadowStats Ongoing M3 Measure for February 2017, and a revised FOMC outlook.

Commentary No. 870 assessed the headline details for the January 2017 Trade Deficit and January Construction Spending, and reviewed prospects for an FOMC rate hike on March 15th.

Commentary No. 869 reviewed and assessed underlying economic reality and a broad variety of indicators in the context of the second-estimate of fourth-quarter 2016 GDP.

Commentary No. 868 covered the January 2017 reporting of New Orders for Durable Goods.

General Commentary No. 867 assessed mixed signals for a second bottoming of the economic collapse into 2009, which otherwise never recovered its level of pre-recession activity. Such is in the context of contracting and faltering industrial production that now rivals the economic collapse in the Great Depression as to duration. Also covered were January 2017 New- and Existing Home Sales.

Commentary No. 866 reviewed the prior headline January 2017 detail of the CPI (and related series), PPI, Industrial Production, Residential Construction and Retail Sales, both nominal and real.

Commentary No. 864 analyzed the prior January 2017 Employment and Unemployment detail, including benchmark and population revisions, and estimates of December Construction Spending, Household Income, along with the prior update to Consumer Liquidity.

Commentary No. 861 covered the December 2016 nominal Retail Sales, the PPI, with a brief look at some summary GAAP reporting on the U.S. government's fiscal 2016 operations. The GAAP-detail will be reviewed this month in a *Special Commentary*.

No. 859 Special Commentary reviewed and previewed economic, financial and systemic developments of the year passed and the year or so ahead.

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

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reporting methodologies of the last several decades, which have tended to understate inflation and to overstate economic activity—as generally viewed in the common experience of Main Street, U.S.A.—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 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 2016 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 July 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*, *Crudele on Census Bureau Fraud* and *John Crudele on Retail Sales.*

PENDING RELEASES:

***Updated* - Residential Construction—Housing Starts (February 2017).** The Census Bureau will release February 2017 residential construction detail, including Housing Starts, tomorrow, Thursday, March 16th, covered in *Commentary No. 873* of that date. In line with common-reporting experience of recent years, monthly results are likely to be unstable and not statistically meaningful, holding in a general pattern of down-trending stagnation. That said, in the wake of the nonsensical extreme swings in recent months, almost anything is possible in this unstable series, despite positive consensus expectations for the headline detail.

Irrespective of the generally meaningless headline detail, the broad pattern of housing starts still should remain consistent with the low-level, stagnant activity, seen at present, where January 2017 activity was down by 45% (-45%) from recovering the pre-recession high of the series. That stagnation is particularly evident with the headline detail viewed in the context of a six-month moving average. Again, this series remains subject to regular and extremely-large, prior-period revisions.

Discussed in *Commentary No. 660* on the August 2014 version of this most-unstable of major monthly economic series, the headline detail here simply is worthless. The series best is viewed in terms of a six-

month moving average. Again, not only is month-to-month reporting volatility frequently extreme, but also the headline monthly growth rates rarely come close to being statistically significant.

Updated in the *Consumer Liquidity Conditions* in prior *Commentary No. 871*, 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 an income shortfall, the liquidity-strapped U.S. consumer is unable to sustain growth in broad economic activity, including sustainable growth in demand for residential construction.

***Updated* - Index of Industrial Production (February 2017).** The Federal Reserve Board will publish its estimate of February 2017 Industrial Production activity on Friday, March 17th, with coverage in *Commentary No. 874* of that date. As had most frequently been the case, recently, the headline monthly reporting should resume coming in on the downside of flat, and below consensus. While consensus expectations have settled in around a monthly gain of 0.2% to 0.3%, a headline monthly production drop remains likely, reflecting weaker manufacturing (disappointing robust automobile manufacturing expectations), offsetting any mining gains, combined with the recently gyrating utilities sector showing some relative stability. The headline detail also should be in the context of downside revisions within the last six months of data, with all current and recent production reporting also subject to an annual benchmark revision on March 31st.

PENDING SPECIAL COMMENTARIES: ***GAAP-Based Accounting of the U.S. Government (Fiscal-Year 2016).*** With some preview in *Commentary No. 861* and *No. 859 Special Commentary*, full analysis is planned as a *Special Commentary* before the March 30th GDP revision and the March 31st annual benchmark revisions to Industrial Production.

The long-delayed consolidation of the major *ShadowStats* reporting into one volume, including the recommended reading list is targeted now for the third full week in April.

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