John Williams'

Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 939

February Employment/Unemployment, Private Surveying, M3, January Trade Deficit

March 9, 2018

**Worst-Ever Real Merchandise Trade Deficit Looms,
Pushing Trade Policy and Dollar Concerns to the Fore**

**Unstable, Nonsense Numbers Were Inconsistent with Related Economic Data
In an Otherwise Not Credible Employment and Unemployment Report**

Non-Comparable Shifting Seasonal Adjustments Bloated Payroll Growth

**Payroll Jobs Jumped by 313,000,
While the Count of the Household Survey Employed Jumped by 785,000,
Yet the Number of Unemployed Rose, Too?**

**February 2018 Unemployment Rates Changed Minimally Month-to-Month:
U.3 Eased to 4.14% versus 4.15%, U.6 Rose to 8.24% from 8.19%, and the
ShadowStats-Alternate Held at 21.8%**

**Private Surveying of February Labor Conditions Showed Monthly Contractions,
Annual Growth but No Economic Expansion**

Fed Policy to be Pressured by a Faltering Economy and Dollar Issues

February Money Supply M1, M2 and M3 and the Monetary Base Slowed Sharply

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PLEASE NOTE: The next regular Commentary, planned for Wednesday, March 14th, will review February Consumer and Producer Prices Indices and Retail Sales. A missive on Friday, March 16th, will cover February Industrial Production and New Residential Construction (Housing Starts).

Best wishes — John Williams (707) 763-5786

Today's (March 9th) ***Opening Comments and Executive Summary.*** The ***Opening Comments*** reviews the U.S. trade deficit circumstance in the context of issues tied to tariffs, trade agreements and the U.S. dollar. Separately, the Conference Board Help-Wanted Online Advertising® (HWOL) is updated for February 2018. The ***Executive Summary*** (page 6) highlights details from February Employment and Unemployment and from the January Trade Deficit reporting.

The ***Reporting Detail*** (beginning on page 10) reviews in greater depth the February labor numbers, with background issues covered in the ***Supplemental Labor-Detail Background*** (page 27), and full reporting of the January Trade Deficit (page 35).

The ***Hyperinflation Watch*** reviews looming FOMC activity and Monetary Conditions, including the initial estimate of year-to-year change in the February 2018 ShadowStats Ongoing Money Supply M3 and the latest detail on the Saint Louis Federal Reserve's Monetary Base (page 38).

The ***Consumer Liquidity Watch*** (page 42) has been updated for the full-February 2018 estimate of the University of Michigan's Consumer Sentiment measure, along with the January 2018 monthly detail on Consumer Credit Outstanding (both real and nominal), and for Fourth-Quarter 2017 Real Household Debt Outstanding.

The ***Week, Month and Year Ahead*** (page 55) provides background on recent *Commentaries* and prospects for the reporting of next week's February CPI, PPI, Retail Sales, Industrial Production and Housing Starts.

OPENING COMMENTS AND EXECUTIVE SUMMARY

Deteriorating U.S. Trade Deficit Intensifies Domestic Economic Distress and Needs to Be Addressed, But What About the Dollar. The ShadowStats contention remains that a primary factor behind Donald Trump's upset victory in the 2016 Presidential Election was the economic distress felt on Main Street, U.S.A., at that time. People tend to vote their pocketbooks. Much of the economic displacement of recent years had been due to a variety of domestic policies and trade agreements, under a number of administrations, which helped to offshore U.S. productive capacity, related employment and wealth creation. That is an area that has needed some positive redirection for some time.

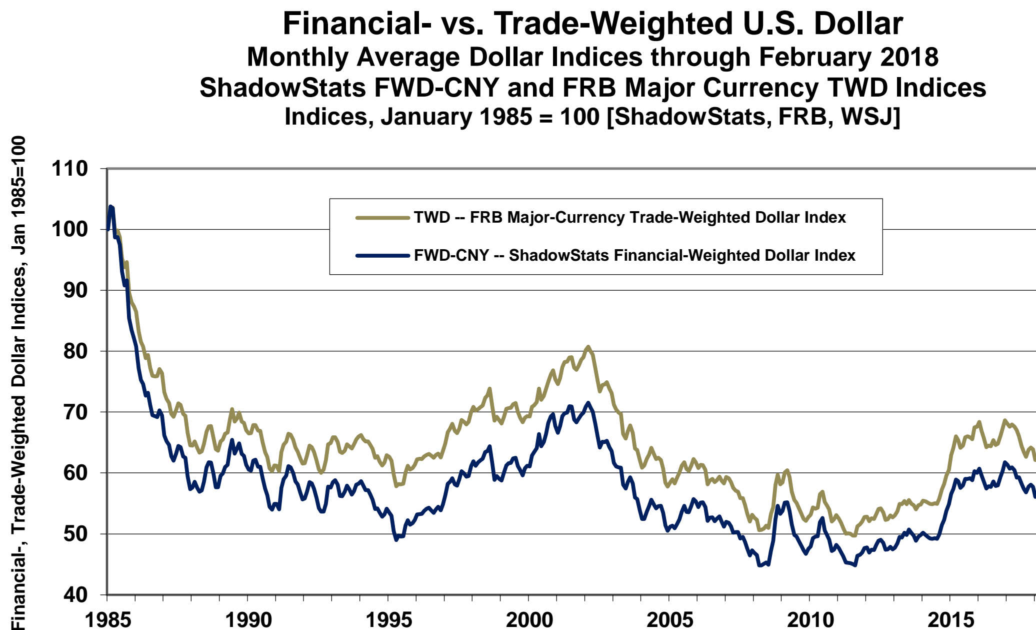
In the context of the just-reported January trade numbers (see the *Reporting Detail*), which suggested the first-quarter 2018 real U.S. Merchandise Trade Deficit was on track for its worst showing in history, yesterday (March 8th) President Trump announced and discussed a variety of actions ranging from tariffs to renegotiations of existing trade deals to consideration of new trade arrangements. What was not

mentioned or discussed, however, was the U.S. dollar. While various negotiations and tariffs have been under way or under consideration for some time, one factor that obviously had been discussed but is not being mentioned at the moment is the U.S. dollar. From *Commentary No. 933* of January 26, 2018:

> **Talking Down the U.S. Dollar Intensifies Downside Risks to the U.S. Equity and Credit Markets.** At the Davos World Economic Forum, on Wednesday, January 24th, U.S. Treasury Secretary Steven T. Mnuchin signaled that the Trump Administration would like to see a weaker dollar in order to help boost the U.S. trade balance. That triggered some intensified dollar selling, which continued into Thursday, despite subsequent hemming and hawing by the Treasury Secretary and others in the Administration, until President Trump said that he had been misunderstood and really wanted a strong dollar.

The weaker a domestic currency is in the global currency markets, the more price-competitive that country's products are in global trade. Generally the stronger a country's economy, technology, fiscal conditions and political stability are, the stronger will be the domestic currency. In combination, those factors often can be a net-positive in global trade. Nonetheless, in a weakened circumstance, currency games often are played and, as noted above, that issue has been raised.

Graph OC-1: Financial- versus Trade-Weighted U.S. Dollar to February 2018



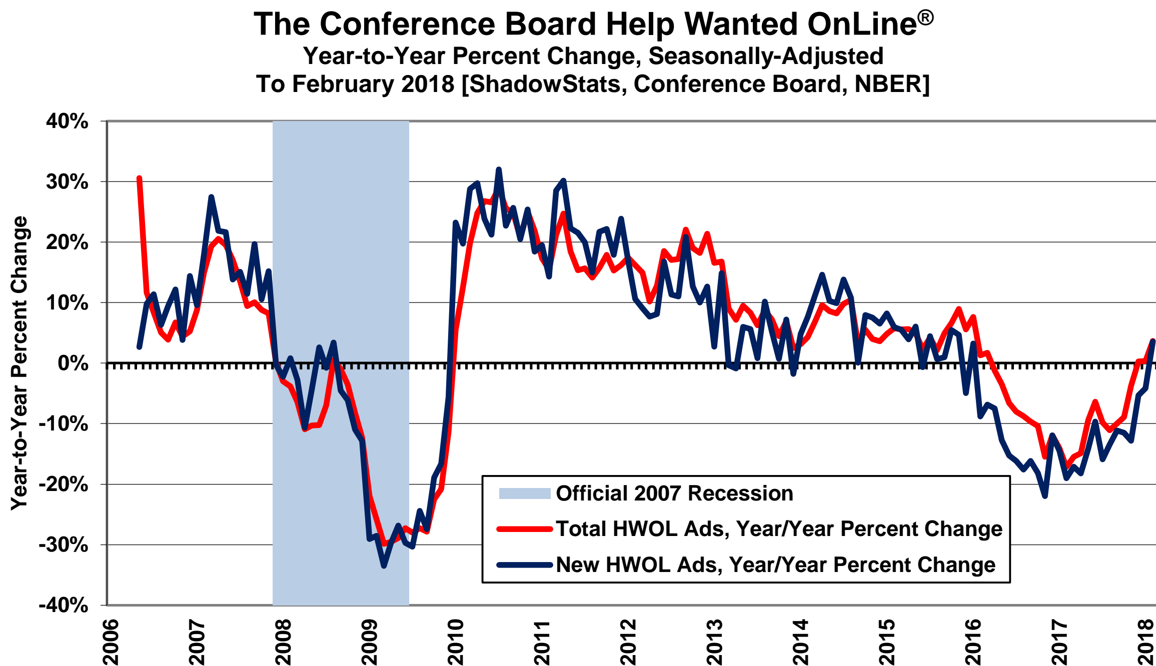
Irrespective of any officially desired or designed direction for the U.S. dollar, it generally has been weakening in the last year. With a new Federal Reserve Chairman in office, policy actions may vary from experience. It remains the ShadowStats contention that a renewed weakening, not a strengthening, in the U.S. economy is at hand. A shift in market expectations in that direction would tend to back away from intensified Fed tightening and rate hikes, back towards some easing (perhaps renewed quantitative easing), all with implications for a weaker dollar, and potentially for some limited trade benefit (see today's *Hyperinflation Watch* page 38).

February 2018 Help-Wanted Advertising Declined for the Month, Gained Year-to-Year but Continued in Deepening Economic Non-Expansion. The Conference Board Help-Wanted Online Advertising® (HWOL) for February 2018 declined month-to-month by 3.8% (-3.8%), having been unchanged in January, while the "New Ads" subcomponent fell in the month by 6.1% (-6.1%) having jumped by 7.2% in January. The monthly patterns continue to be irregular, with monthly gains and losses split evenly for both series in the last twelve months.

Where "Total Ads" reflected a year-to-year gain of 3.7% in February 2018, following 0.4% in January 2018 and 0.3% in December 2017, such followed 20-consecutive months of year-to-year decline. "New Ads" annual growth turned positive in February, up by 3.6% year-to-year, have declined by 4.1% (-4.1%) year-to-year in January 2018, its 24th consecutive month of annual decline. Although sharply improved in the month, the protracted year-to-year deterioration in labor-market demand reflected in "New Ads" remains a meaningfully-negative, leading indicator to broad economic activity. Against the November 2015 series peaks, February 2018 "Total Ads" were down by 17.6% (-17.6%), with "New Ads" down by 25.9% (-25.9%).

Annual growth began to slow in 2010 and turned negative year-to-year in late-2015 and early-2016. The shaded area in the graph reflects the formal bounds of the 2007 to 2009 recession. While the HWOL held in negative annual growth territory into early-2010, beyond the formal economic trough in June 2009, keep in mind that payroll employment—traditionally a coincident economic indicator to the general economy—did not hit its cycle trough until February 2010.

Graph OC-2: The Conference Board Help Wanted OnLine® to February 2018



Many thanks to The Conference Board for permission to publish the accompanying graph of year-to-year change in its *Help Wanted OnLine®* data. The annual percentage change is plotted for two series: Total Ads (red line) and New Ads (blue line). Where, "Total ads are all unduplicated [online] ads appearing

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during the reference period. This figure includes ads from the previous months that have been reposted as well as new ads." While, "New ads are all unduplicated ads which did not appear during the previous reference period. An online help wanted ad is counted as 'New' only in the month it first appears." Related background details and reporting are found here: The Conference Board Help Wanted OnLine®.

While much of this text is repetitive of prior discussions in *Commentary No. 934-A*, *No. 852* and *No. 820*, the detail here has been updated for the latest information. These comments and analysis remain those of ShadowStats alone, not those of The Conference Board.

ShadowStats follows a number of business indicators—both conventional and not—looking for reliable reporting of real-world economic activity and for indications of shifting patterns in same. The HWOL is one of the best, private leading-indicator measures. Pre-natural disaster economic disruptions and recovery boosts in the last five months of 2017, a number of major government economic indicators, including production, employment and housing and construction measures, had been showing "unexpected" weakness, or continued non-recovery and renewed downturn in the post-2007 economic collapse period.

The disaster-recovery boost appeared peak in November 2017, with many elements of broad economic activity beginning to turn down anew. Those trends should continue in play, with odds increasing for an outright contraction in first-quarter 2018 GDP net of short-lived, natural-disaster reporting disruptions, and the current, beginning unwinding of same (see *Commentary No. 936*, *Commentary No. 937* and *Commentary No. 938*).

The Conference Board Help Wanted OnLine® Advertising, Historical Background. *[Please note: this section generally has been repeated, unrevised from prior reporting, other than for updated links. It provides general background and historical perspective for the series.]* The HWOL basic concept has proven itself over the last century, in the context of the closely-paralleled tallying of help-wanted advertising in newspapers. The current on-line series tracked the economic collapse into 2009, parallel with the last of the series based on newspaper help-wanted advertising. The beauty and benefit of a good leading indicator is that it provides a meaningful "advance" signal of a shift in economic activity, before that shift may become obvious in other series. Such is a particularly valuable commodity, when headline data out of the federal government increasingly are politicized and unreliable (see *Special Commentary No. 885*, *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*).

With the preceding ShadowStats comments in mind, the following caution, posted on the Conference Board's web site, speaks for itself:

> NOTE: Recently, the HWOL Data Series has experienced a declining trend in the number of online job ads that may not reflect broader trends in the U.S. labor market. Based on changes in how job postings appear online, The Conference Board is reviewing its HWOL methodology to ensure accuracy and alignment with market trends.

First fully covered by ShadowStats in *Commentary No. 820* of July 16, 2016, the HWOL is updated here through February 2018 (released March 7th). As a leading economic indicator, help-wanted advertising had its roots as far back in time as the initial reporting of Industrial Production, post-World War I. The Conference Board has adapted the concept to reflect the fundamental shift of help-wanted advertising from printed newspapers to online advertising. The prior newspaper-based series simply was the best leading indicator of its day.

Back in the days when help-wanted advertising was the primary source of classified-advertising revenue for the physically-printed, folding newspapers, the Conference Board's Help-Wanted Advertising Index (newspapers) simply was the most reliable leading indicator available of broad economic activity. It was a component of the Commerce Department's Index of Leading Economic Indicators. It led activity in employment as well as the Gross National Product (GNP) and the now-headline Gross Domestic Product (GDP), which is a subcomponent of the GNP (ex-trade flows in factor income such as interest and dividend payments).

The National Bureau of Economic Research (NBER) has published detail with the St. Louis Federal Reserve on help-wanted advertising indices constructed back to 1919. From the post-World War I era into the 2000s, year-to-year change in the various historical help-wanted series always signaled what would become recognized eventually as a formal recession, when the annual change in the index contracted by 15% (-15%) or more, which has happened here.

Since formal tracking switched to help-wanted advertising on the Internet, around 2005, as seen with The Conference Board Help Wanted OnLine®, that series has been through only one, formally-confirmed down-cycle in the economy. The year-to-year growth plots in the accompanying graph begin with the first annual-growth rate availability in May 2006. Even with a limited initial history, the new series tracked that headline downturn into 2009 (in tandem with the final surveys of newspaper help-wanted online advertising, which continued for a while), and it has tracked to the downside in the current environment of what appears to be a "new," still-unfolding recession (see *Special Commentary No. 935*).

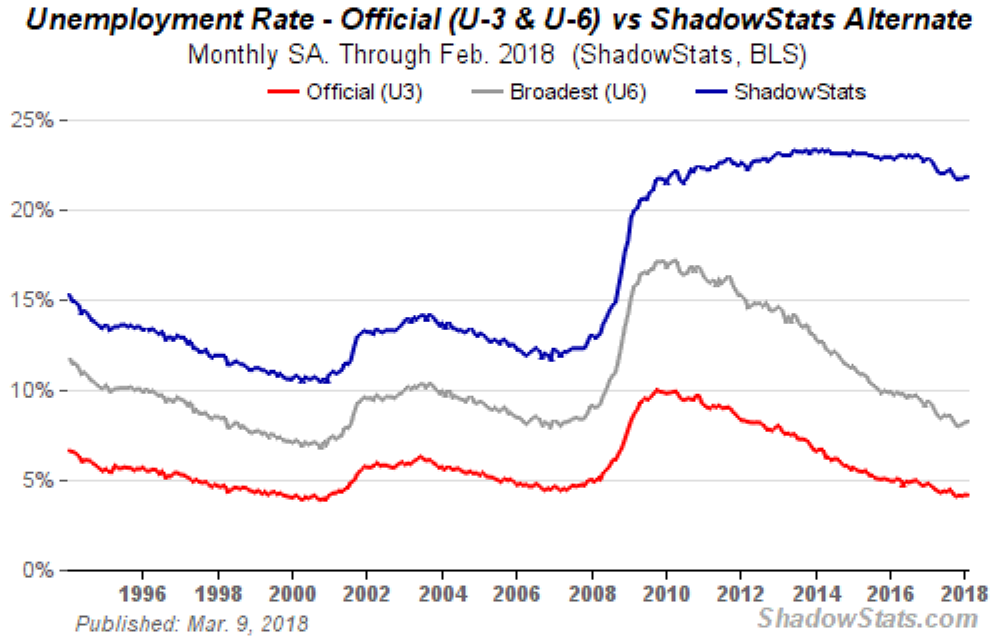
Time will establish new annual growth parameters that would signal a formal recession. My betting remains that they will look much like the earlier series, and much like the pattern seen in the present series in terms of year-to-year contraction. Those looking for independent confirmation of underlying economic conditions should find this series to be highly valuable. As for the BLS employment and unemployment series, they should still begin to catch up with the Conference Board's high-quality, independent leading indicator, despite the ongoing , heavy upside reporting biases deliberately structured into the BLS series and expanded anew into the initial 2017 payroll-survey benchmarking. See the discussions in *Special Commentary No. 885*, *Commentary No. 864* and in the *Birth-Death/Bias-Factor Adjustment (BDM)* section of today's *Supplemental Labor-Detail Background* on page 27.

EXECUTIVE SUMMARY: Employment and Unemployment—February 2018—Nonsense Reporting of the First Order. In the seasonally-adjusted Household Survey data, although the U.3 headline unemployment rate held at a 17-year low of 4.1% in February 2018, for the fifth straight month, at the second decimal point it was 4.14%, just shy of the 4.15% reading in January. Broader U.6 unemployment rate rose for the third month, to 8.24% in February 2018, from 8.19% in January and 8.08% in December, while the still-broader ShadowStats-Alternate held at 21.8% for the second month, up from 21.7% in December, all as reflected in accompanying *Graph 1*.

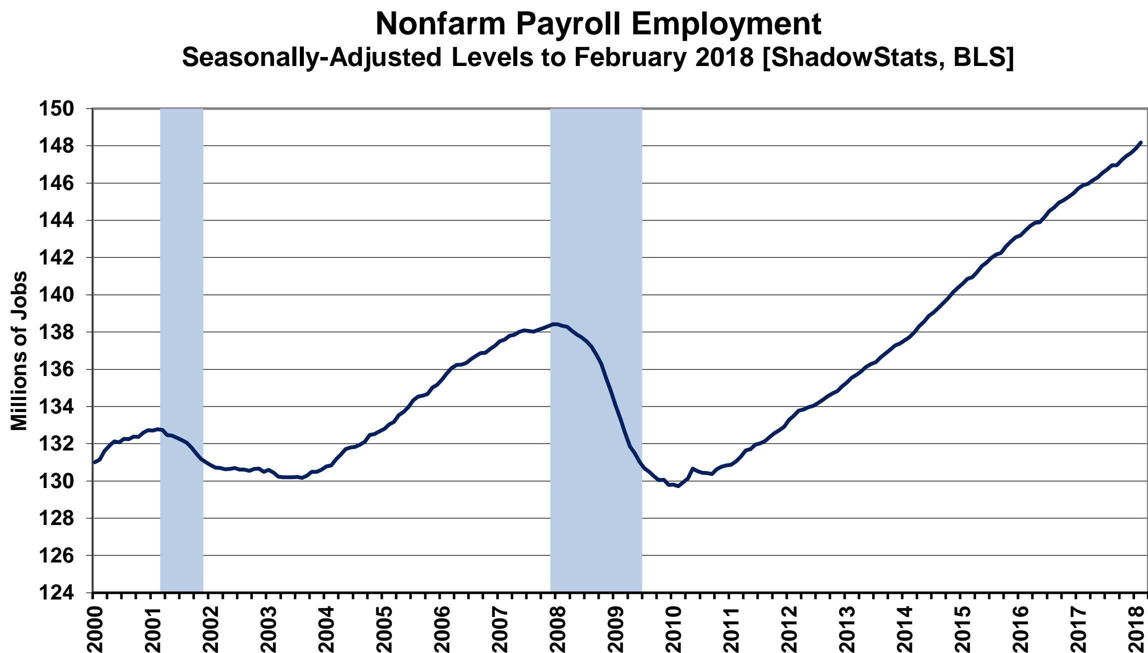
February 2018 payrolls rose month-to-month by 313,000, versus 239,000 [previously 200,000] in January 2018 and 175,000 [previously 160,000] in December. The unexpectedly-strong monthly gain in February and upside revisions to January and December all were due to inconsistent seasonal-factor games played by the Bureau of Labor Statistics (BLS), as discussed in the *Reporting Detail* and the *Supplemental Labor-Detail Background* on page 27. Also discussed in the *Reporting Detail*, much of the underlying

monthly payroll gains by industry simply were incompatible with other, usually better-quality industry indicators.

Graph 1: Comparative Unemployment Rates U.3, U.6 and ShadowStats



Graph 2: Nonfarm Payroll Employment 2000 to Date



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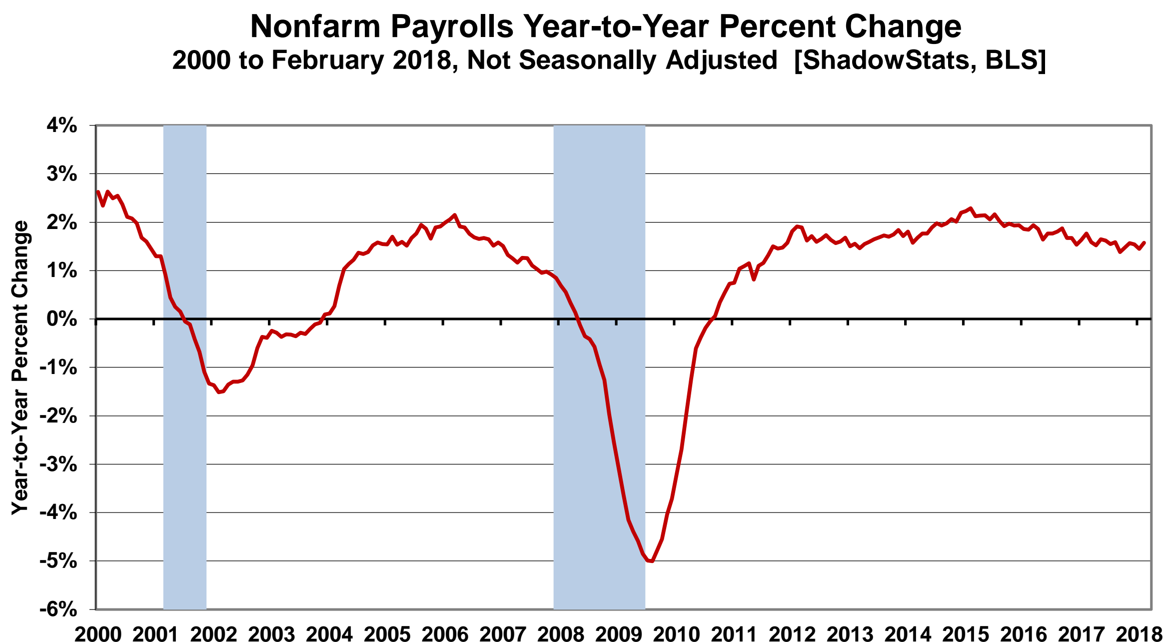
Graph 3: Payroll Employment, Year-to-Year Percent Change, 2000 to Date



Reflected in *Graph 3*, annual payroll growth of 1.57% in February 2018, versus the recent, regular (as opposed to hurricane-distorted) near-term low of 1.45% in January 2018, still broadly remained in a downtrend that has reached a level and pattern of growth that usually precedes and signals the onset of a recession (again, see the *Reporting Detail*).

Separately, discussed in the *Opening Comments*, the February 2018 Conference Board Help-Wanted Online Advertising® survey showed monthly contractions, annual growth and a continued state of economic non-expansion.

Despite ongoing political- and stock-market-hyped speculation of the U.S. economy being at full employment, the U.6 and ShadowStats measures show that not to be the case. Such is confirmed in expanded *Reporting Detail* discussions tied to the employment-population ratio and the participation rate (*Graphs 6* to *8*), as well as to the low level of headline annual growth in payroll employment (see *Graphs 3*, *17* and *18*). Extended coverage on the February 2018 details of both the Household and Payroll follow in the *Reporting Detail* (see page 10).

Trade Deficit—January 2018—Real Merchandise Trade Headed for Its Worst Quarterly Deficit in History, Amidst Continuing Monthly Deterioration. The headline January 2018 inflation-adjusted real trade-deficit deepened, again, by more than consensus expectations. It widened in a manner that showed the First-Quarter 2018 Real Merchandise Trade Deficit to be on track for its worst shortfall in modern economic reporting. That circumstance also was suggestive of downside reporting pressures on the First-Quarter 2018 GDP (due for release on April 27th).

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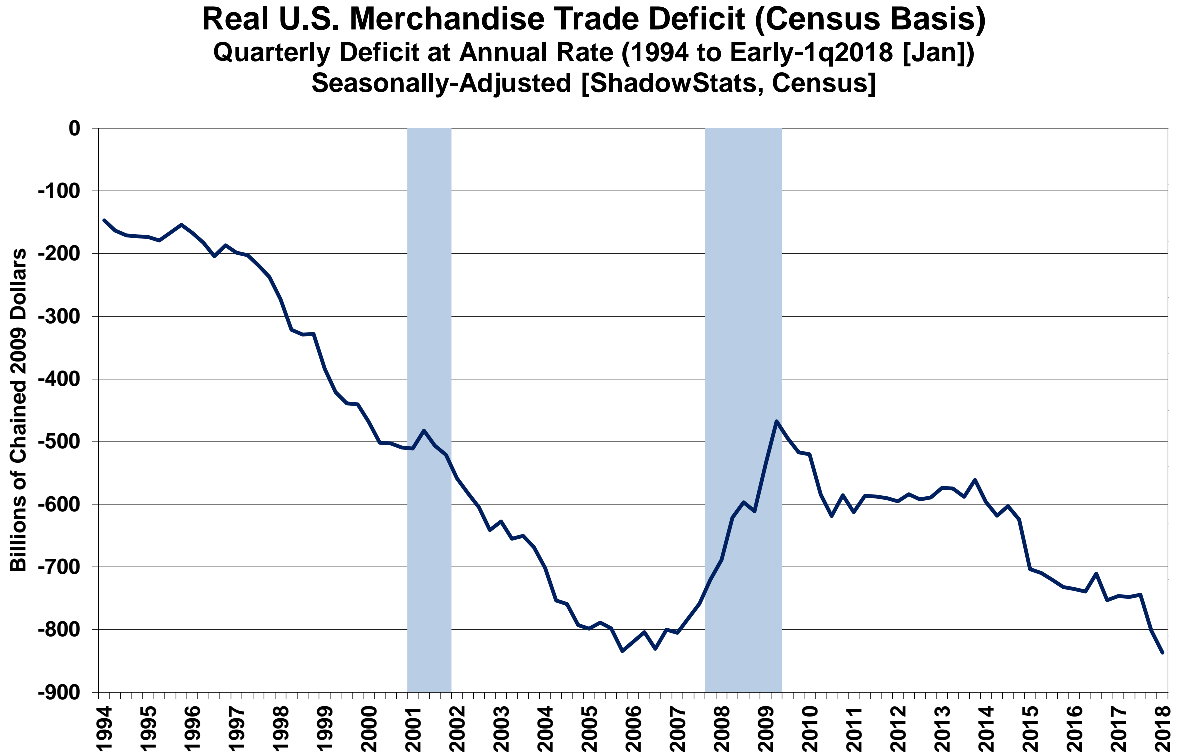
January's Nominal Goods and Services Trade Deficit Topped $56 Billion for First Time Since 2008. The seasonally-adjusted monthly trade balance for goods and services widened on a balance-of-payments basis by $2.693 billion, or by 5.0%, to $56.601 billion, versus a revised, widened deficit of $53.908 billion in December 2017. The widening in the monthly January deficit reflected a sharp decline of $2.696 billion in exports, with imports virtually unchanged, a decline of $0.004 (-$0.004) billion. The headline January 2018 deficit also widened by $7.909 billion, or by 16.2%, versus the year-ago $48.692 billion trade shortfall for January 2017.

Graph 4: Real Quarterly Merchandise Trade Deficit (1994-2018)



Quarterly Real Deficits Moving Towards Economic-Crisis Levels. Detailed in the *Real Trade Deficit* section in the *Reporting Detail*, adjusted for inflation, the annual real merchandise trade deficit in 2016 widened for the year to $734.5 billion, versus $716.4 billion in 2015. The 2016 annual trade shortfall then was the worst since 2008.

On an annual basis, the 2017 real merchandise trade deficit widened to $760.2 billion, versus $734.5 billion in 2016. The 2017 deficit was the worst since 2007.

Based solely on the initial headline detail for January 2018, first-quarter 2018 is on track for an annualized quarterly deficit of $836.7 billion. Such would be the worst quarterly deficit in the history of the series, in the modern economic history of the United States.

[Extended graphs and analysis of the Labor Data and Trade Deficit (page 35) follow in the **Reporting Detail.***]*

REPORTING DETAIL

EMPLOYMENT AND UNEMPLOYMENT (February 2018)

February U.S. Labor Conditions Showed Unusual Instabilities, Inconsistencies and Seasonal-Adjustment Distortions. In the context of the regular reporting distortions discussed in *Special Commentary No. 885* as well as in the *Supplemental Labor-Detail Background* on page 27, incorporated here by reference, broad labor circumstances generally have weakened sharply, irrespective of what may appear still to be happy headline details, on the surface.

The Bureau of Labor Statistics (BLS) released the details of its February 2018 Household Survey (Unemployment Rate) and Payroll Survey (Payroll Employment) this morning, Friday, March 9, 2018.

Household Survey details show that despite headline U.3 unemployment holding at 4.1% for the fifth straight month, general circumstances are not improving. The inverted-scale plot of the ShadowStats Alternate Unemployment Rate measure is shown in *Graph 6*, for comparison with the *Graphs 7* and *8* of the Civilian Employment-to-Population Ratio and the Labor-Force Participation rate. Where the latter two series gyrated around recent hurricane disruptions, and had weakened anew in January 2018, they bounced back minimally with an unusual surge in "other industries." Nonetheless, the lower the reading of those ratios, the more-distressed are employment conditions, as correlated with the heavy impact of discouraged and displaced workers on the level of the ShadowStats Alternate Unemployment Measure.

Seen in *Graph 17*, annual growth in unadjusted payroll employment held at low levels seen historically with economies either coming out of recession, or in the current circumstance of falling into recession, although the February 2018 annual growth moved minimally above the near-term January 2018 low.

The headline monthly payroll February 2018 gain of 313,000 jobs (367,000 net of prior-period revisions) was bloated heavily by the inconsistent and non-comparable use of monthly seasonal-adjustment factors. Separately, strong, headline payroll gains in areas such as the construction industry, ran counter to headline estimates of industry activity, as discussed and reviewed in the *Payroll Survey* section.

In terms of underlying reality, the seasonally-adjusted 313,000 monthly payroll jobs gain in February, likely was on the plus-side of flat (see *Supplemental Labor-Detail...*). In the context of the *ShadowStats-Alternate Unemployment Rate Measure* discussion (also in the *Supplemental Labor-Detail...*), headline February 2018 unemployment at 4.1% for the U.3 rate was much closer to 21.8%, when viewed from the context of common experience. Extended assessment of headline labor-reporting distortions, again, is found in *No. 885*.

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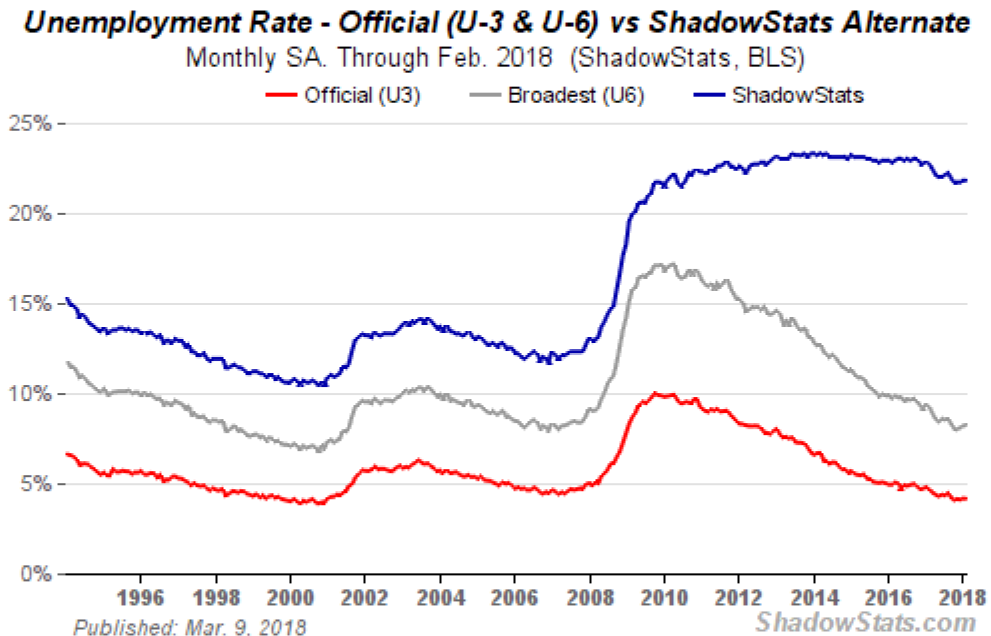
Household Survey: Counting All Discouraged and Displaced Workers, February 2018 Unemployment Held at 21.8%. The headline detail from the Household Survey continued nonsensically positive in February 2018, never recovered from heavily-distorted hurricane impacts in September and October 2017, negligibly revised in December's annual benchmarking (revisions there were only to seasonal adjustments, not in correcting unadjusted levels of activity), boosted in terms of population in January 2018, and now with an unusually large surge of 608,000 in "other" private industry employed.

Adding back into the total unemployed and labor force the ShadowStats estimate of effectively displaced long-term discouraged workers—a broad measure of unemployment more in line with common experience—the ShadowStats-Alternate Unemployment Estimate for February 2018 held at 21.8% for a second month. The broadest government unemployment measure U.6 held at 8.2% (although moving higher at the second decimal point), while the headline U.3 rate held at 4.1% for the fifth month. The ShadowStats estimate generally shows the toll of long-term unemployed leaving the headline labor force, effectively becoming long-term discouraged or displaced workers. That broad unemployment level is heavily dependent on the underlying level of U.6 unemployment, on top of which the ShadowStats measure is constructed (see a full description of the series in the *Supplemental Labor-Detail Background*, page 27).

Unemployment Circumstances Remained Heavily Distorted. *Graphs 5* to *9* reflect various aspects of the Household Survey detail, which generates the unemployment rate. Moving beyond wild internal data gyrations of recent months (see *Commentary No. 915*, *Commentary No. 919-B* and *Commentary No. 924*) the headline unemployment rate U.3 at 4.14% in February 2018, followed 4.15% in January, 4.09% in December 2017, 4.12% in November and 4.07% in October—the lowest level since December 2001. The broader U.6 rate rose to 8.24% in February 2019, versus 8.19% in January, 8.08% in December 2017, 7.99% in November and 7.99% in October. The ShadowStats-Alternate measure, built upon U.6, held at 21.8% in February 2018, versus 21.8% in January and 21.7% in each of December, November and October 2017. Those headline rates are plotted here in *Graph 5* (*Graph 1* in the *Executive Summary*).

Graph 5: Comparative Unemployment Rates U.3, U.6 and ShadowStats
(Same as Graph 1 in the Executive Summary)



Graph 6 shows the inverted-scale plot of the ShadowStats Alternate Unemployment Rate measure, as usual, for comparison with the plots in *Graphs 7* and *8* of the Civilian Employment-to-Population Ratio and the Labor-Force Participation rate, where both those measures jumped sharply with September hurricane disruptions to the data, falling back sharply in recent months, with some pick-up in February. The higher those ratios, the healthier are the employment conditions in the economy. Nonetheless, both measures currently are running counter to what should be very positive news. They are at low levels, consistent with severe recessions, despite the headline December 2017 U.3 unemployment rate having hit a 17-year low, in theory a strong economic positive. Headline U.3 unemployment largely remains a nonsense number.

Reflected in *Graph 5*, the headline U.3 was 4.14% in February 2018, versus 4.15% (rounding to 4.1%) in January, 4.09% in December and versus 4.12% in November. U.6 (U.3 plus those employed part-time for economic reasons, and those marginally attached to the labor force, including discouraged workers) rose to 8.24% in February 2018, versus 8.19% in January, 8.08% in December and 7.99% in November, while the ShadowStats-Alternate measure (U.6 plus all estimated long-term discouraged and displaced workers) held at 21.8% in February 2018, versus 21.8% in January and 21.7% in December.

Dysfunctional, Seasonally-Adjusted Headline Detail from the Household Survey. Despite the headline U.3 unemployment holding at its lowest level since January 2001, employment circumstances remained heavily stressed and unstable, suggestive of an economy still deep in non-recovery and non-expansion, instead of one purportedly expanding rapidly at full employment. Systemic imbalances and instabilities are indicated by the labor-force participation rate (labor force/population) and the employment-to-population ratio (headline employment/population) near historic lows. Still, with the headline unemployment rate so low, those ratios should be approaching historic highs, not holding near historic lows, as seen in *Graphs 7* and *8*.

Graphs 6 to *8* reflect longer-term unemployment and discouraged-worker conditions. *Graph 6* is of the ShadowStats unemployment measure, with an inverted scale. The higher the unemployment rate, the weaker will be the economy, so the inverted plot tends to move visually in tandem with plots of most economic statistics, where a lower number means a weaker economy. The upturn on the headline ShadowStats measure is in tandem with renewed weakening in the broad employment indicators.

The inverted-scale of the ShadowStats unemployment measure tends to move with the employment-to-population ratio over time, which rose to 60.4% in February 2018, versus 60.1% in January and 60.1% December, then down from higher, post-hurricane disruptions, with the ShadowStats unemployment measure holding even in February. Nonetheless, that ratio remained somewhat off its post-1994 record low, the historic low and bottom subsequent to the 2007 economic collapse (only the period following the series redefinition in 1994 reflects consistent reporting), as shown in *Graph 7*.

The labor force containing all unemployed (including total discouraged/displaced workers) plus the employed, however, tends to be correlated with the population, so the employment-to-population ratio remains something of a surrogate indicator of broad unemployment and, again, with a strong correlation with the ShadowStats unemployment measure.

Graph 8 shows the February 2018 participation rate (ratio of the headline labor force to the population) rising to 63.0%, having held at a rounded 62.7% for the prior three months, having jumped to a 63.0% in hurricane-distorted September, from 62.9% in August.

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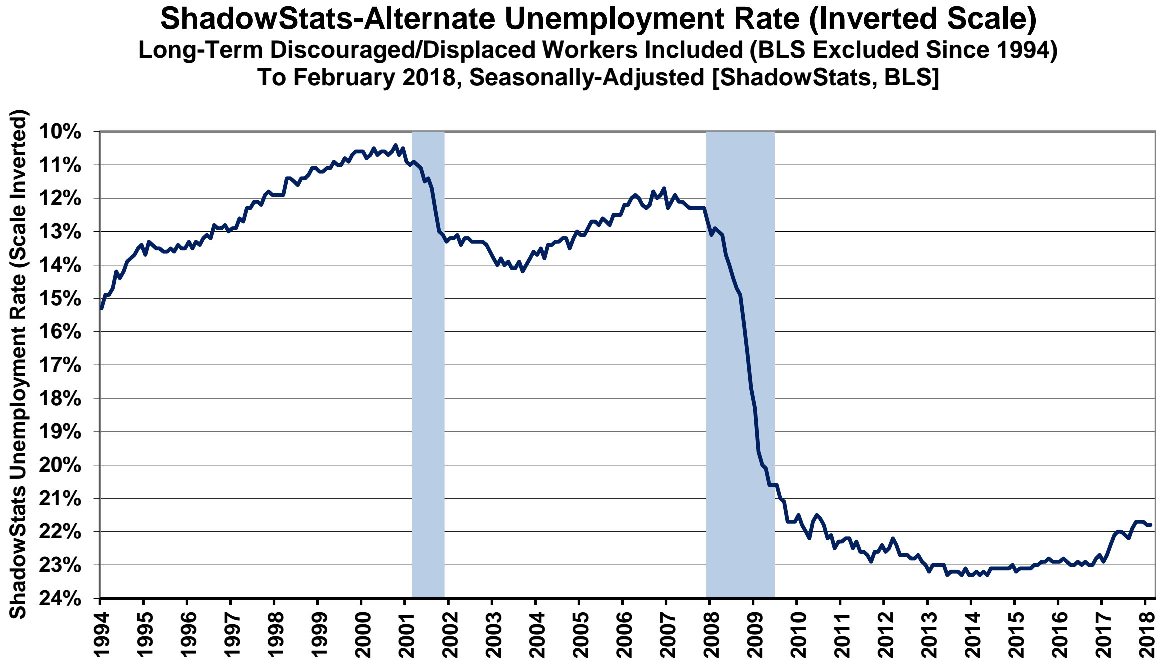
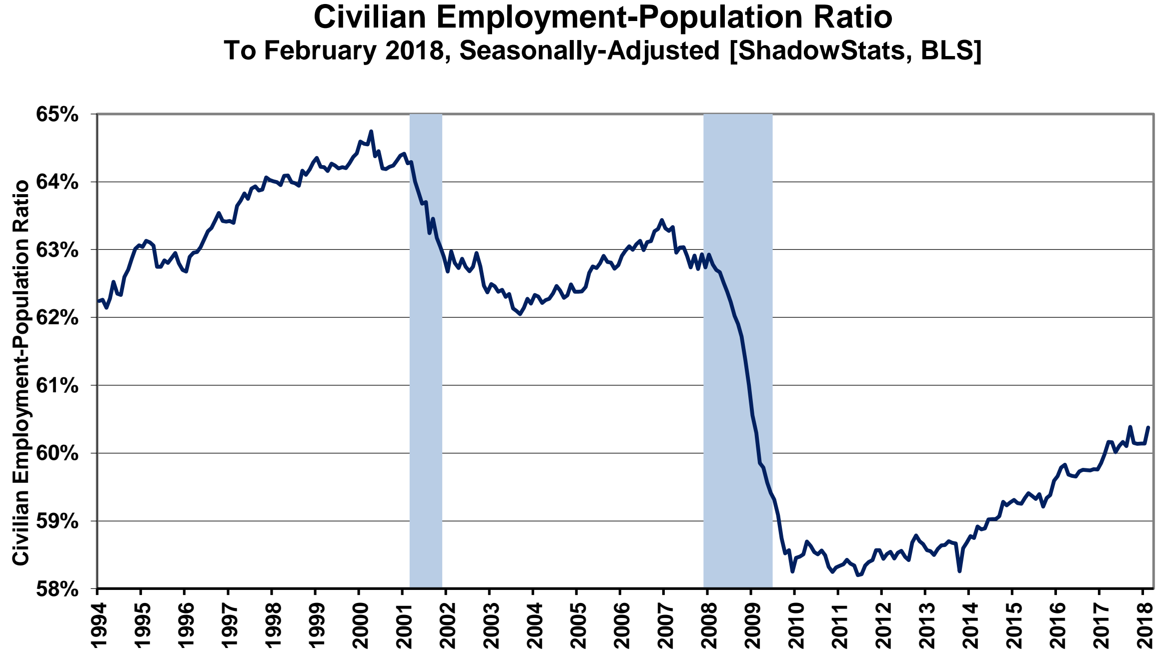
Graph 6: Inverted-Scale ShadowStats Alternate Unemployment Measure



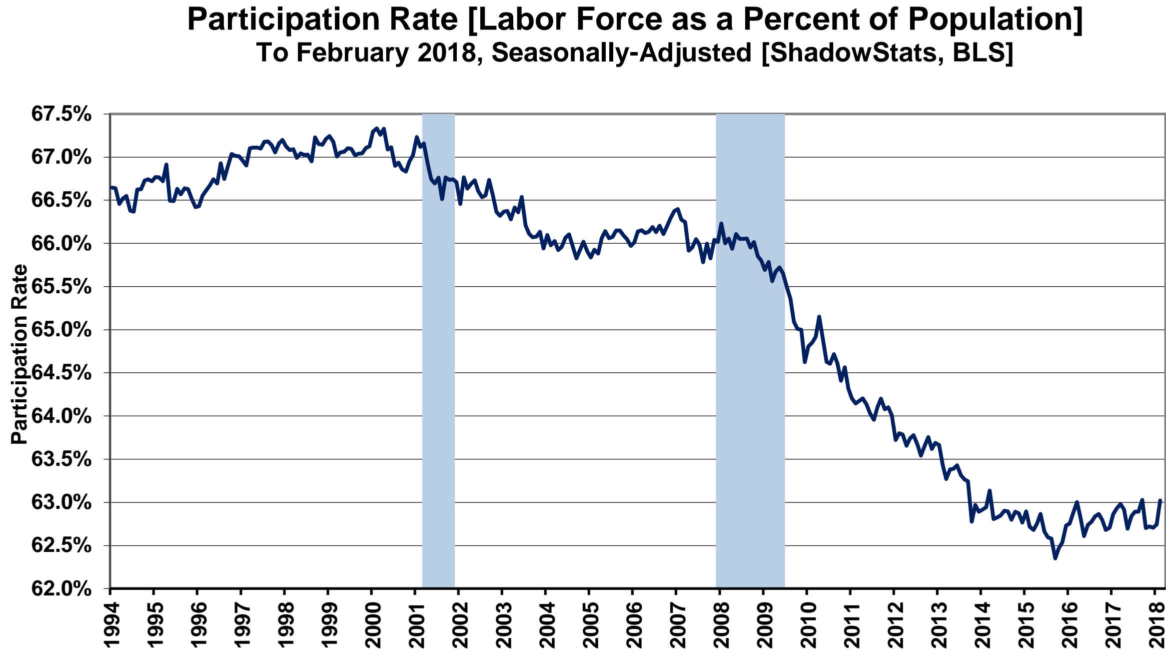
Graph 7: Civilian Employment-to-Population Ratio



Graphs 6 through *8* reflect labor data available in consistent detail only back to the 1994 redefinitions of the Household Survey and the related employment and unemployment measures. Before 1994,

employment and unemployment data consistent with the February 2018 Household-Survey reporting simply are not available, irrespective of any protestations to the contrary by the BLS.

Graph 8: Labor-Force Participation Rate



The Economy Remains Far From Full-Employment. Discussed in the *Fedspeak* portion of the *Fed* section of *No. 859 Special Commentary* (see also the *Opening Comments* of *Commentary No. 870*), certain members of the Federal Reserve Board (see *Commentary No. 827*) have suggested that an unemployment rate near 5.0% (headline U.3 is at 4.1% at the moment) reflected full-employment conditions in the United States. As noted in, and updated from the earlier employment/unemployment *Commentary No. 845*, one would expect that "full employment" not only would be consistent with a certain headline unemployment rate, traditionally about 5.0%, but also with a coincident labor-force participation rate, traditionally of about 66%.

For example, at the formal onset of the recession in December 2007, the headline unemployment rate was 5.0%, with the participation rate at a 66.0% near-term peak (higher peaks in participation, in the early 2000's, were coincident with U.3 unemployment of about 4.0%). Full employment with unemployment at 5.0%, also minimally should be reflected at a near-term peak in the participation rate, not at a trough. The February 2018 headline unemployment rate of 4.1%, for example was in the context of a 63.0% participation rate. Yet, that participation rate was more consistent with a headline unemployment rate (U.3) of 8.5% instead of the headline 4.1%. Where the count of Household Survey employed generally is not gimmicked, that 66% full-employment participation rate—consistent with the latest hyped "full-employment" economy—generally was consistent with a U.3 unemployment 70% above the hyped 5.0% full-employment unemployment rate, and well more than double the current headline U.3 number.[1]

[1] Consider with the February 2018 population of 256.934 million, that the implied labor force at a full-employment participation rate of 66.0% would be 0.66 x 256.934 = 169.576. That labor force less current headline employed, 169.576 – 155.215 = 14.361 million implied unemployed / labor force of 169.576 = 8.5% unemployment. The problem with the assumptions underlying these numbers and concept, again, remains that the economy is not at full employment, as claimed.

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The reason for the heavily-distorted current unemployment detail remains that the numbers reflect the unusual nature of the post-recession drop in headline unemployment. The declining unemployment rate heavily has reflected discouraged and displaced, unemployed persons being defined out of the labor force, instead of the more-traditional and positive circumstance of the unemployed being reemployed.

Other Major Indicators Do Not Show a Growing, Expanding—Let Alone Recovered—Economy. Regularly plotted here are various graphs that mirror the patterns of *Graphs 6* to *8* (1994-to-date where available), which do not confirm the purported headline recoveries in the GDP or relative employment. That detail was expanded upon and covered in *Special Commentary No. 935*; see also recent *Commentary No. 938* covering the GDP. Some of those series are updated in this section.

Consider *Graph 9*, which shows the ShadowStats version of that GDP, also plotted from 1994, but now through the February 28th second-estimate of fourth-quarter 2017 GDP, where the plot has been corrected for the understatement of inflation used in deflating the headline GDP.

Other graphs range from the January 2018 Cass Freight Index (*Graph 10*) to December 2017 U.S. Petroleum Consumption (*Graph 11*), January 2018 U.S. Industrial Capacity Utilization (*Graph 12*), related January Consumer Goods Production (*Graph 13*) and January Housing Starts (*Graph 14*), with all but the Petroleum Consumption graph from *Commentary No. 936*, *Commentary No. 937* and *Commentary No. 938*.

[Graphs 9 to 14 begin on the next page.]

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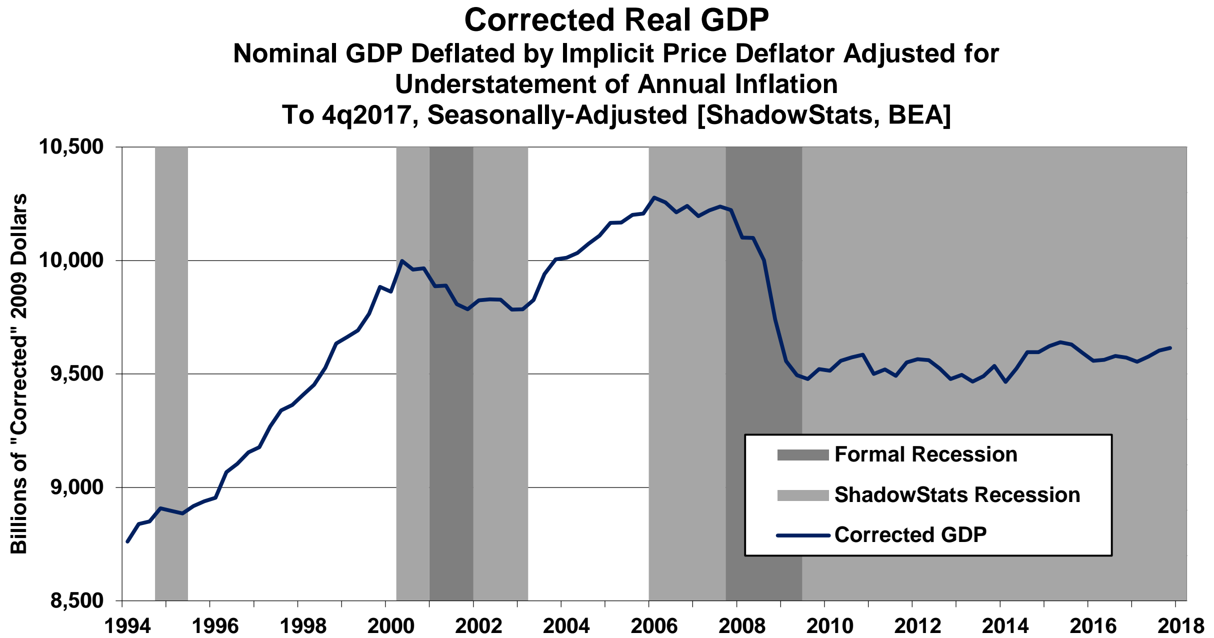
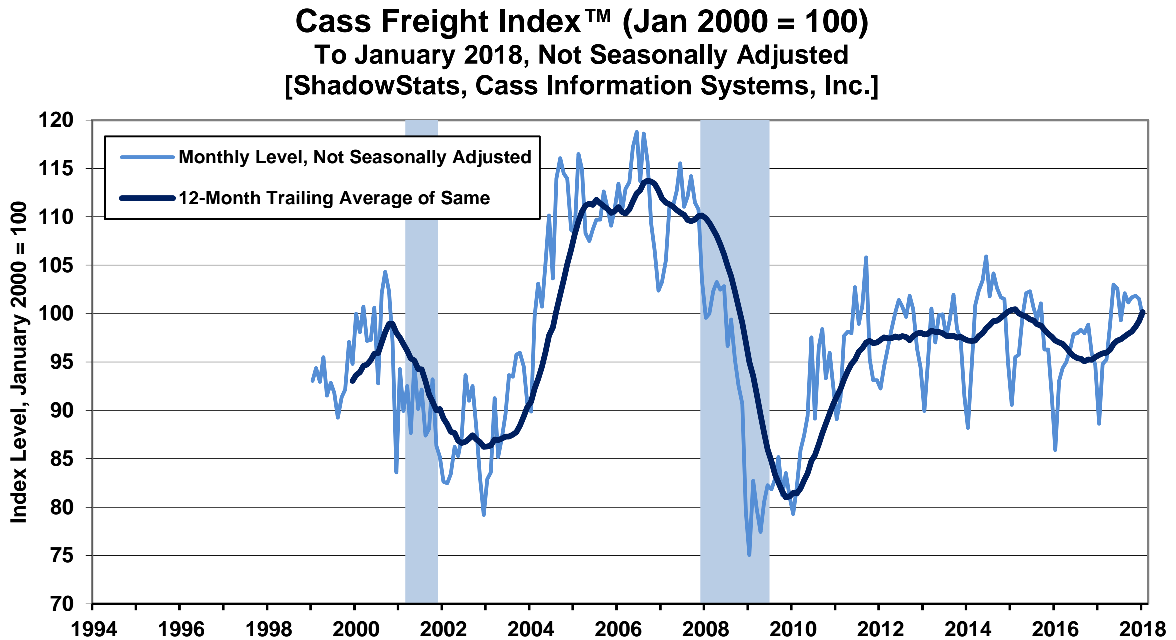
Graph 9: Corrected Real GDP through 4q2017, Second-Estimate



Graph 10: Cass Freight Index for North America (2000 – January 2018), Indexed to January 2000 = 100



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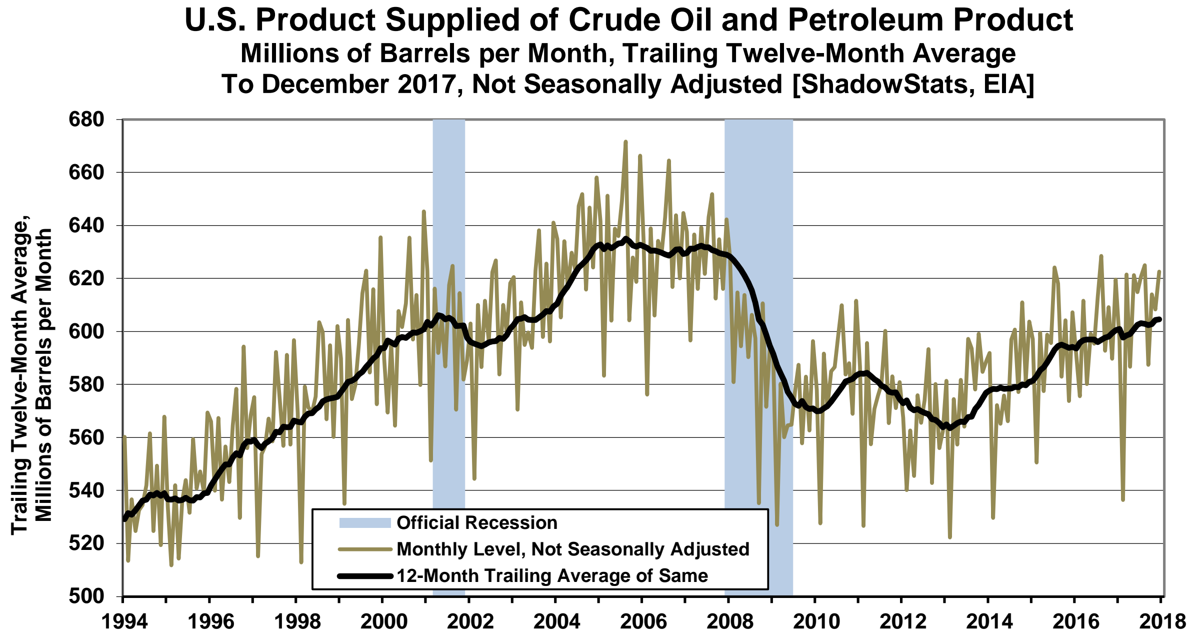
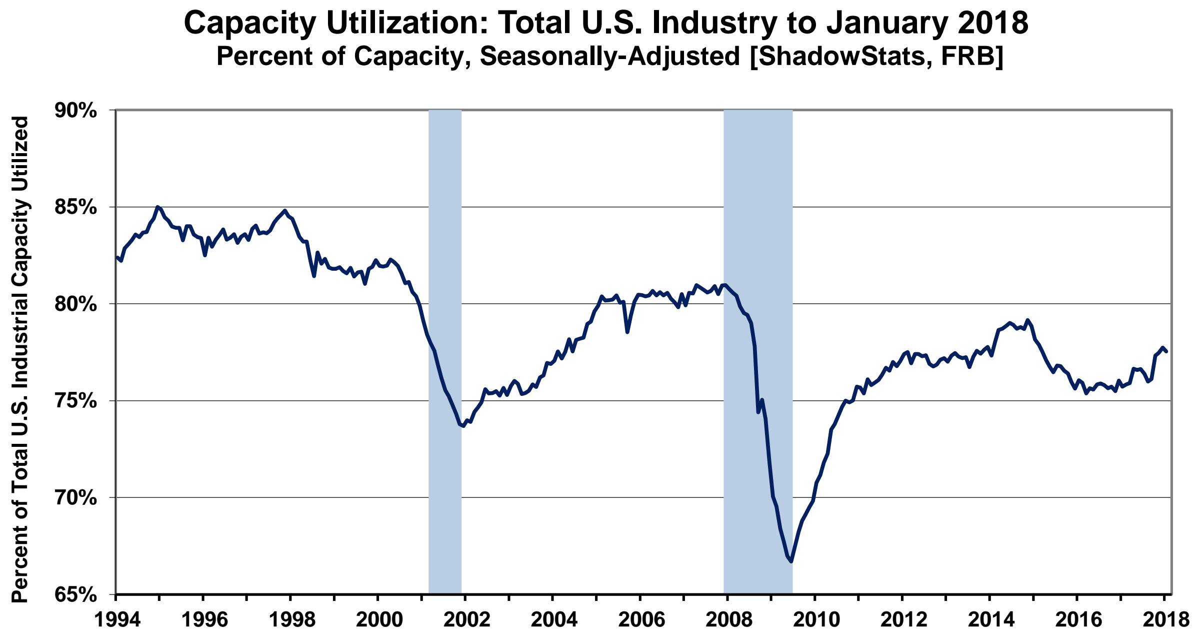
Graph 11: U.S. Petroleum Consumption to December 2017



Graph 12: Utilization of Total U.S. Industrial Production Capacity (1994 to January 2018)



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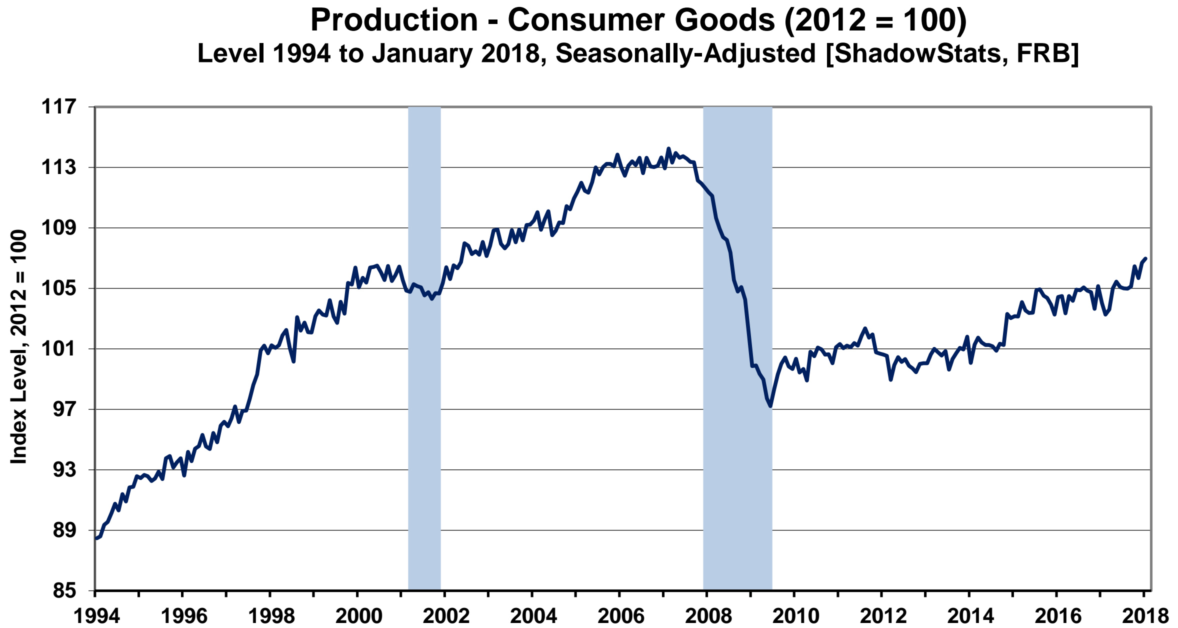
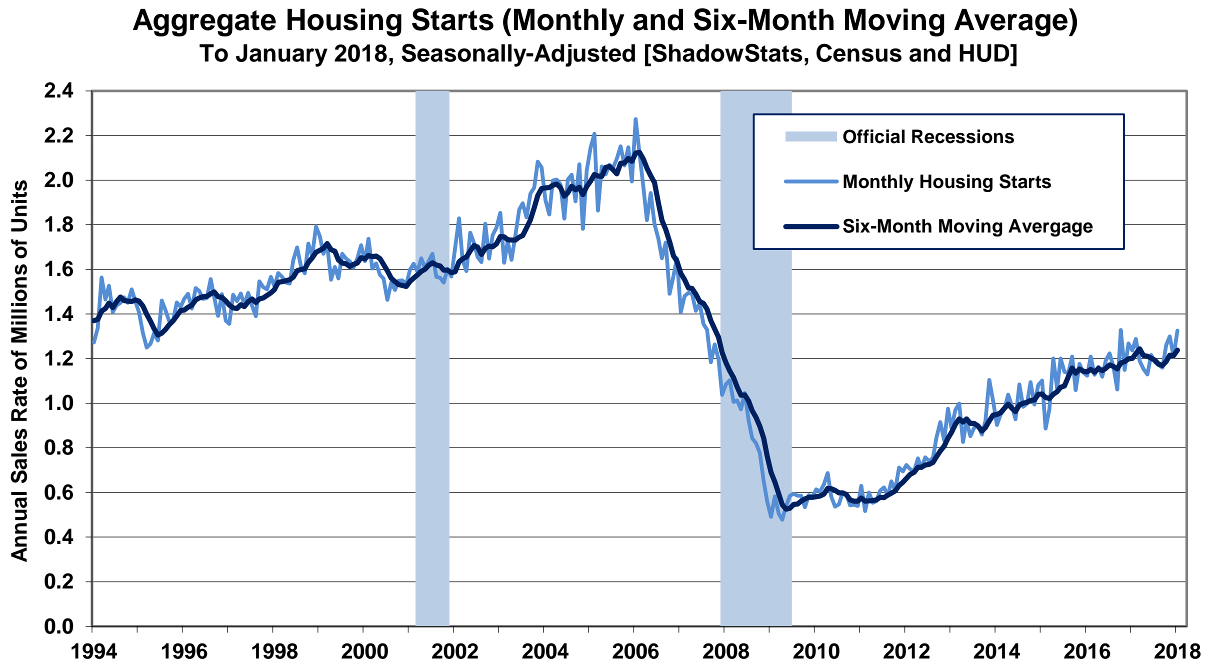
Graph 13: Industrial Production – Consumer Goods Sector (1994 – January 2018)



Graph 14: Housing Starts, Annual Rate by Month (1994 – January 2018)



Headline Unemployment Rates. The headline February 2018 U.3 unemployment rate of 4.1% [4.14 % at the second decimal point] followed 4.1% [4.15%] in January 2018, 4.1% [4.09%] in December 2017, 4.1% [4.12%] in November, and 4.1% [4.07%] in October, which followed 4.2% [4.20%] in September,

4.4% [4.44%] in August, 4.3% [4.33%] in July, 4.3% [4.35%] in June, 4.3% [4.28%] in May, 4.4% [4.38%] in April, 4.5% [4.48%] in March, 4.7% [4.68%] in February and 4.8% [4.78%] in January 2017.

Formally, the month-to-month decline of 0.01% (-0.01%) in the February 2018 U.3 was well shy of being statistically-significant (+/- 0.23% at the at the 95% confidence interval). Other than for the once-per-year December benchmarking, however, such consideration broadly is nonsense, given that the comparison of monthly numbers otherwise is on an inconsistent basis, a circumstance that resumed for the next eleven months with the January 2018 headline detail (again, see the following *Supplemental Labor-Detail Background*).

On an unadjusted basis, unemployment rates are not revised and, in theory, are consistent in post-1994 methodology. The unadjusted unemployment rate U.3 eased to 4.39% in February 2018, from 4.49% in January, from 3.93% in December 2017, 3.92% in November, 3.89% in October, 4.07% in September, 4.53% in August, versus 4.60% in July, 4.49% in June, 4.11% in May 2017, 4.11% in April, 4.56% in March, 4.95% (rounds to 4.9%) in February and 5.14% in January.

Unemployment rate U.6 is the broadest unemployment rate published by the BLS. It includes accounting for those marginally attached to the labor force (including short-term discouraged workers) and those who are employed part-time for economic reasons (*i.e.*, they cannot find a full-time job).

On top of the seasonally-adjusted February 2018 U.3 unemployment rate, some downside pressure on the unadjusted monthly count of marginally-attached workers (including discouraged workers) and more than offsetting upside pressure on the adjusted number of people working part-time for economic reasons, the adjusted February 2018 U.6 unemployment rate rose to 8.24%, from 8.19% in January, versus 8.08% in December 2017, 7.99% in November, 7.99% in October, 8.29% in September, 8.56% in August, 8.53% in July, 8.54% in June, 8.42% in May, 8.57% in April, 8.82% in March, 9.20% in February and 9.39% in January. The unadjusted U.6 unemployment rate was 8.60% in February 2018, versus 8.85% in January 8.00% in December 2017, 7.66% in November, 7.61% in October, 8.29% in September, 8.64% in August, 8.86% in July, 8.59% in June, 8.10% in May, 8.15% (rounds to 8.1%) in April, 8.94% in March, 9.54% in February and 10.08% in January 2017.

Marginally-Attached and Displaced Workers. New discouraged and otherwise marginally-attached workers always are moving into U.6 unemployment accounting from U.3, while those who have been discouraged or otherwise marginally-attached for one year, continuously, are dropped from the U.6 measure. As a result, the U.6 measure has been easing along with U.3, for a while, but those being pushed out of U.6 still are counted in the ShadowStats-Alternate Unemployment Estimate, which has remained relatively stable, despite recent monthly declines. Monthly counts in February 2018 showed a reduced level of 1.602 million marginally attached, of which 373,000 were discouraged workers.

That latest, official "discouraged" number, again, reflected the flow of the headline unemployed—giving up looking for work—leaving the headline U.3 unemployment category and being rolled into the U.6 measure as short-term "marginally-attached discouraged workers," net of the further increase in the number of those moving from short-term discouraged-worker status into the netherworld of long-term discouraged-worker status.

It is the displaced worker—the long-term discouraged-worker category—that defines the ShadowStats-Alternate Unemployment Measure. There is a continuing rollover from the short-term to the long-term

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category, with the ShadowStats measure encompassing U.6 and the short-term discouraged workers, plus the long-term discouraged workers. In 1994, "discouraged workers"—those who had given up looking for a job because there were no jobs to be had—were redefined so as to be counted only if they had been "discouraged" for less than a year. This time-qualification defined away a large number of long-term discouraged and displaced workers. The remaining redefined short-term discouraged and redefined marginally-attached workers were included in U.6.

ShadowStats Alternate Unemployment Estimate. Adding back into the total unemployed and labor force the ShadowStats estimate of effectively displaced long-term discouraged workers—a broad measure of unemployment more in line with common experience—the ShadowStats-Alternate Unemployment Estimate for February 2018 was 21.8%, versus 21.8% in January, 21.7% in December 2017, 21.7% in November, 21.7% in October 2017, 21.9% in September, 22.2% in August, 22.1% in July, 22.0% in June, 22.0% in May, 22.1% in April, 22.4% in March, 22.7% in February and 22.9% in January 2017. The ShadowStats estimate generally shows the toll of long-term unemployed leaving the headline labor force—effectively becoming long-term discouraged or displaced workers—as discussed in the *Supplemental Labor-Detail Background*, page 27.

Payroll Survey: February's 313,000 Jobs Gain Was Dominated by Industries Otherwise Reported in Stagnation or Downturn; Recession Signal from Annual Growth Continued, Albeit Less Intense. In the context of heavily distorted headline reporting and inconsistent and non-comparable seasonal-adjustments, the headline month-to-month payroll employment gain in February 2018 was 313,000, versus 239,000 in January 2018 and 174,000 in December 2017, as reflected in *Graphs 15* and *16*,

There Was No Relationship Between Payroll-Change and Other Indicators of Key Industry-Sector Activity. Consider that of 313,000 monthly gain in February 2018 payrolls, 143,000 came from a combination of Construction (the largest sector gain of 61,000), Manufacturing (up by 31,000) and Retail Sales (up by 50,000). Those areas also showed strong growth in January, and, with the exception of Retail Sales, showed strong jobs growth in December. Where headline reporting February detail for activity in those individual series will follow in the next week or so, the headline payroll details simply do not correspond with the relatively independent reporting of activity those series.

For example, while real construction spending was up month-to-month in December, it was down in January and certainly has not been growing in tandem with the headline purported employment growth, as reflected in *Graphs 22* and *23* in the *Construction Payrolls* section.

Manufacturing was unchanged in December and January, while Real Retail Sales declined in December and collapsed in January, as discussed for both series in Commentary No. 936.

Non-Comparable and Inconsistent Seasonally-Adjusted Monthly Changes. As discussed separately for the dominant gain in construction payrolls (*Construction Payrolls* section), the adjusted headline February total payroll gain detail was stated on a consistent basis with the December and January headline details, but not with prior periods, from which current headline growth was borrowed (see the *Supplemental Labor-Detail Background*, page 27, for discussion on the various reporting distortions and gimmicks).

Consider the latest aggregate headline detail, where the level of the December 2017 seasonally-adjusted payrolls revised higher by 15,000 jobs, but that was in the context of a downside-revision to the unadjusted level of December payroll levels by 28,000 (-28,000) jobs. The adjusted January 2018 payroll level revised higher by 24,000 jobs, on top of a downside revision of 1,000 (-1,000) jobs to the unadjusted level. In the context of (1) the unadjusted data are the core numbers, and (2) the headline monthly revisions affect only the most three recent months, based on the latest month's imputed seasonal factors, positive shifts in seasonal factors were borrowed from before November. The effect was to boost headline December, January and February activity, without having to restate the earlier seasonally-adjusted periods, from which the growth was borrowed (again, see the *Supplemental Labor-Detail Background* discussion on concurrent seasonal factor distortions).

Headline Payroll Detail. The headline February 2018 payroll gain of 313,000 formally was statistically-significant +/- 135,000 (a confidence interval more appropriately in the range +/- 300,000) at the 95% confidence interval (all confidence intervals used are at the 95% level). That followed a revised headline payroll gain of 239,000 [previously 200,000] in January and 175,000 [previously 160,000] in December 2017, again see *Graphs 15* and *16.*

Annual percentage growth in payroll employment, also gained, but remained in recession-signal territory with a 1.57% year-to-year increase in February 2018, following an unrevised 1.45% year-to-year gain in unadjusted payrolls January 2018 payrolls, which was the weakest level since coming out of the 2007 recession in August 2011, other than for a benchmark-revised, hurricane-induced trough of 1.38% in September 2017. Unadjusted year-to-year change in December 2017 payrolls was 1.55% [previously 1.56%], see *Graphs 17* and *18.*

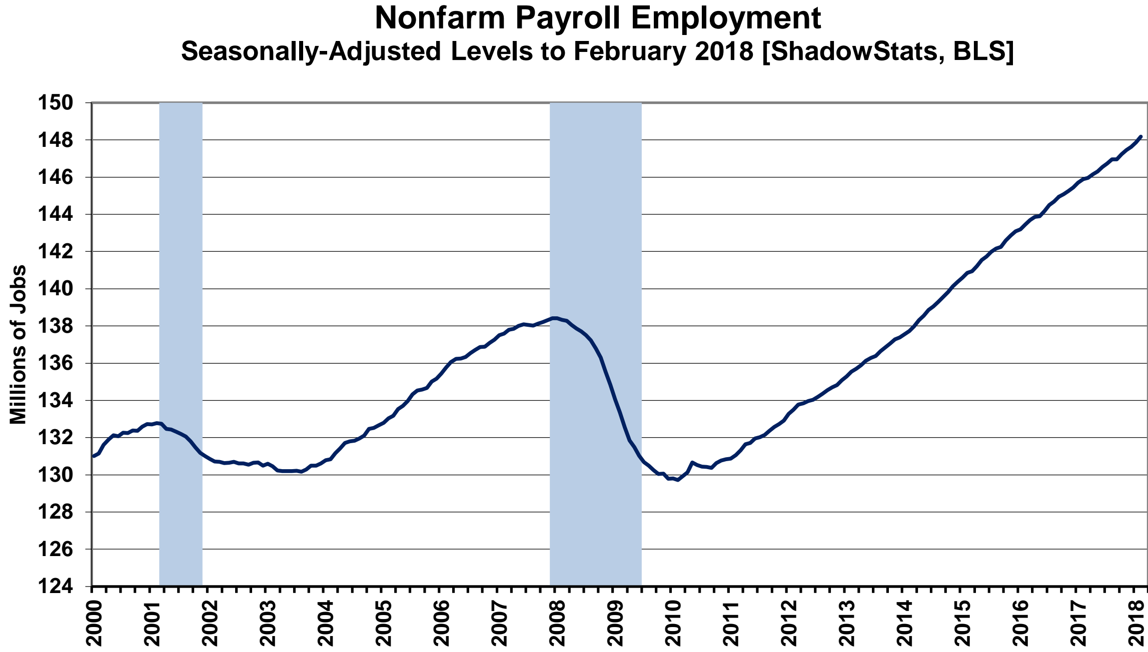
Contrary to claims by economists at the San Francisco Fed, far from being healthy or normal, such low-level annual growth rates are seen either coming out of recession, or going into recession, but never seen consistently in the regular variability of ongoing, normal economic activity, as discussed in *Commentary No. 843*. Current levels of annual growth in unadjusted payrolls likely are at the threshold, on the downside, of heading into recession.

Graphs 15 to *18* show the headline payroll series, level and annual change, both on a shorter-term basis, since 2000, and on a longer-term historical basis, from 1945. In perspective, the longer-term graph of the headline payroll-employment levels shows the extreme duration of what had been the official non-recovery in payrolls, the worst such circumstance of the post-Great Depression era.

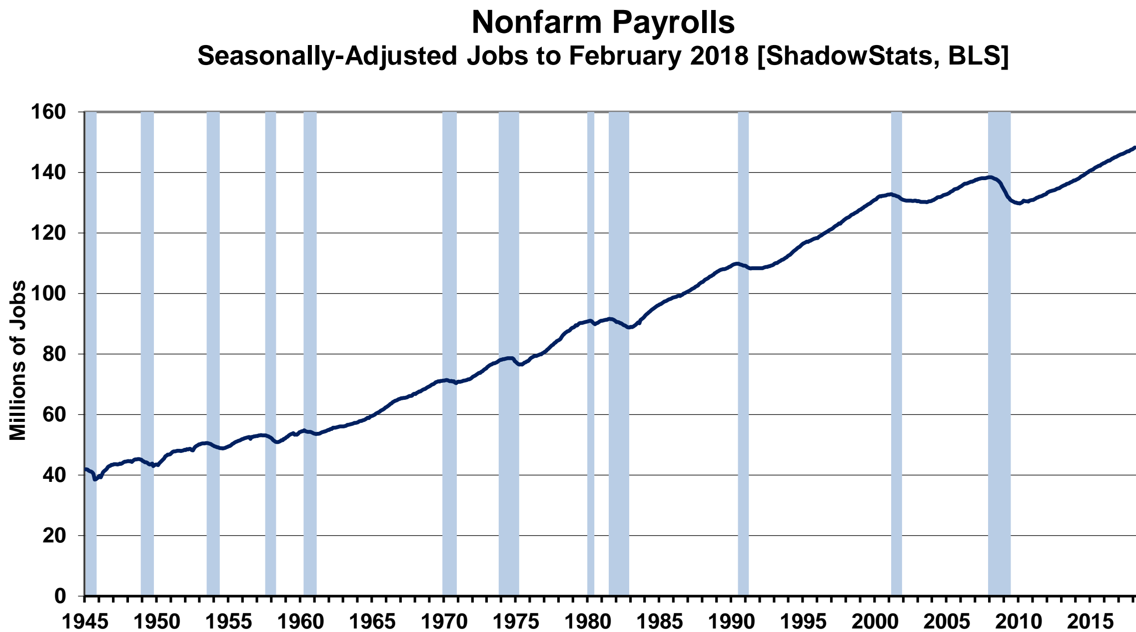
[Graphs 15 to 20 begin on the next page.]

Graph 15: Nonfarm Payroll Employment, 2000 to Date

(Same as Graph 2 in the Executive Summary)



Graph 16: Nonfarm Payroll Employment, 1945 to Date



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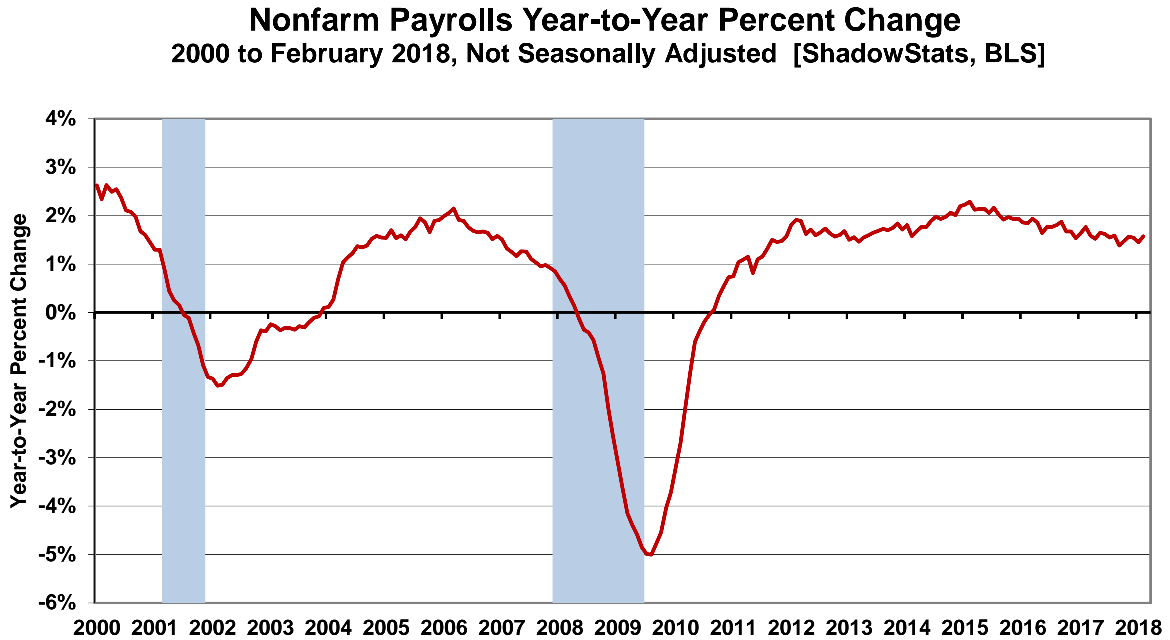
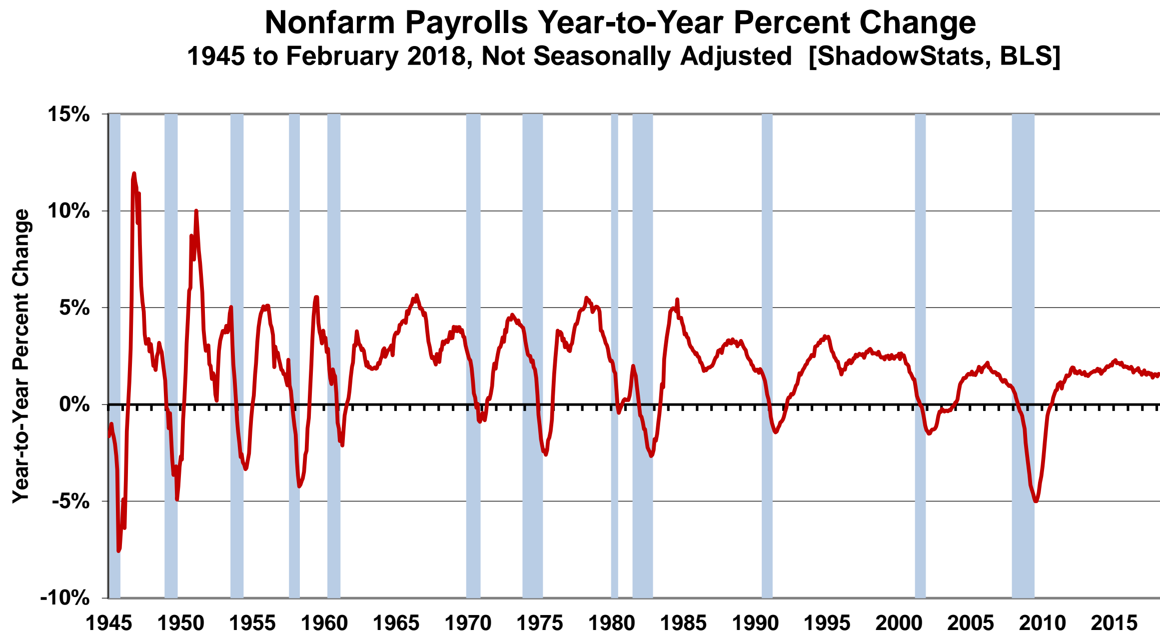
Graph 17: Payroll Employment, Year-to-Year Percent Change, 2000 to Date

(Same as Graph 3 in the Executive Summary)



Graph 18: Payroll Employment, Year-to-Year Percent Change, 1945 to Date



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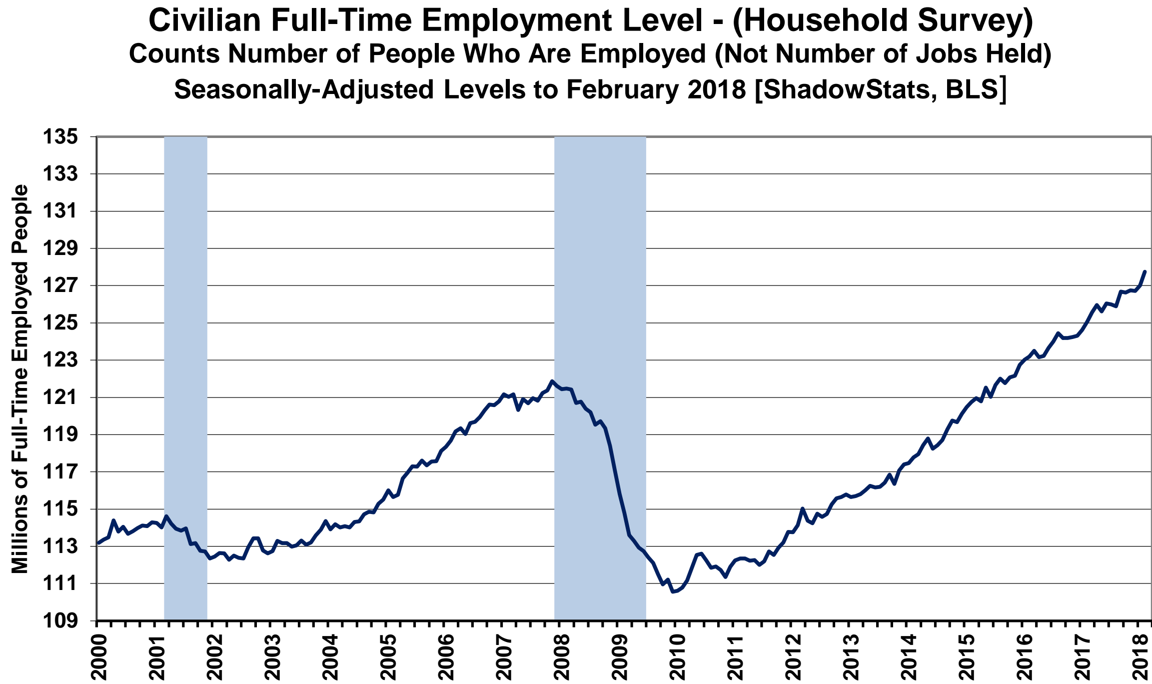
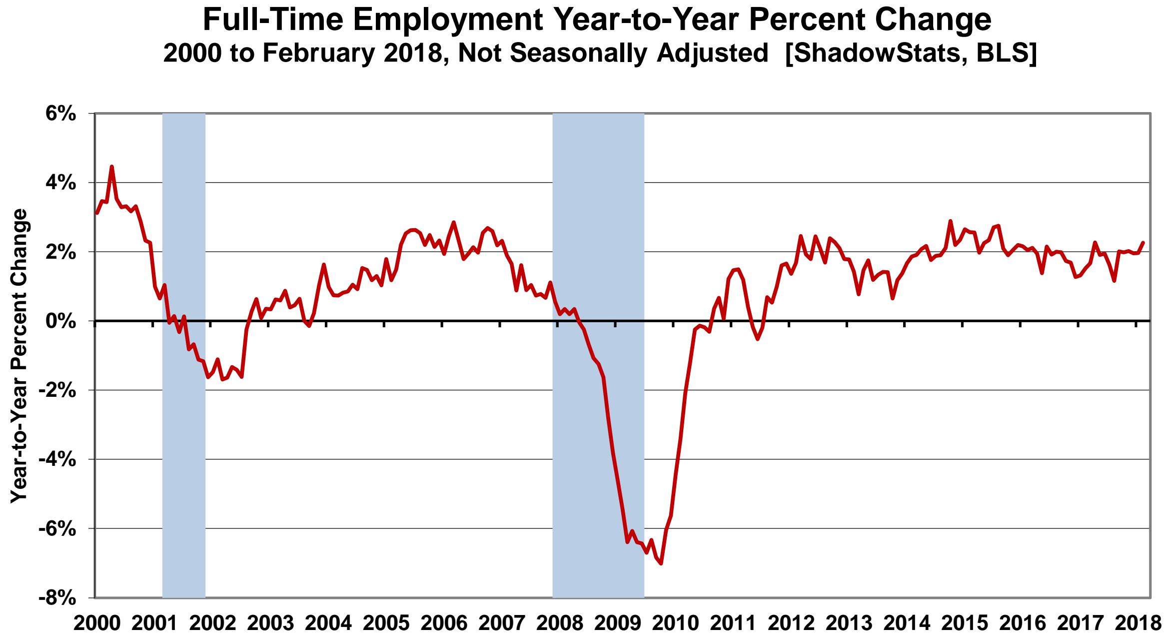
Graph 19: Full-Time Employment (Household Survey), 2000 to Date



Graph 20: Full-Time Employment (Household Survey), Year-to-Year Percent Change, 2000 to Date



Unlike the Payroll Survey, which counts "employed" people with more than one job (such as part-time jobs) for each job counted, the Household Survey counts employed individuals only once, irrespective of the number of jobs held.

Where, out of the payroll survey, headline payroll employment (again, counting each par-time job as an employed person) rose month-to-month by 313,000 in February 2018, out of the household survey, full-time employment rose by 729,000, with another 277,000 gained in part-time employment, with multiple job holders (already counted as employed individuals) increasing by 19,000. Among other differences, the payroll survey is nonfarm, where the Household Survey covers agricultural employment.

Year-to-year change in unadjusted full-time employment jumped to 2.26% in February 2018, reflecting a sudden surge of workers in "other industries," versus 1.97% in January 2018 and 1.95% in December 2017.

February 2018 Construction Payrolls Rose by 0.9% Month-to-Month and by 4.2% Year-to-Year, but Remained Down by 7.1% (-7.1%) from the Pre-Recession Peak. In the context of headline February 2018 payroll reporting, construction payrolls gained sharply month-to-month, on top of upsides revision to seasonally-adjusted January 2018 and December 2017 activity, as reflected in accompanying *Graph 21*.

Yet, despite the upside revision to those adjusted number, the unadjusted January 2018 number was not revised and the unadjusted December number was revised lower. Seen in this construction series, which accounted for the largest single month-to-month gain for a major industry sector in the full payroll series, the BLS is playing unconscionable games with the seasonally-adjusted data, discussed in *Section I, Headline Distortions from Shifting Concurrent Seasonal-Adjustment Factors* in the *SUPPLEMENTAL LABOR-DETAIL BACKGROUND* that follows. The current seasonally-adjusted numbers are not comparable with prior periods.

Separately, consider *Graph 21* of total U.S. Construction Payroll Employment through February 2018 versus *Graph 22* of real Total Construction Spending Put in Place in the United States through January 2018. In theory, employment levels, which have been soaring since 2016, should be consistent with real construction activity, which basically has been flat in the same period, actually contracting year-to-year in recent months. Even so, the surging February 2018 construction payroll employment numbers still were 7.15% (-7.15%) shy of recovering the pre-recession high for the series.

Headline Construction Detail. All that said, the headline February 2018 construction payrolls rose month-to-month by 0.86% in February, versus 0.57% [previously 0.51%] in January and a revised 0.60% [previously 0.47%] in December 2017, versus unadjusted annual gains of 4.18% in February 2018, versus an unrevised 3.61% in January 2018 and a downwardly revised 4.03% [previously 4.04%] in December 2017.

[Graphs 21 and 22 follow on the next page.]

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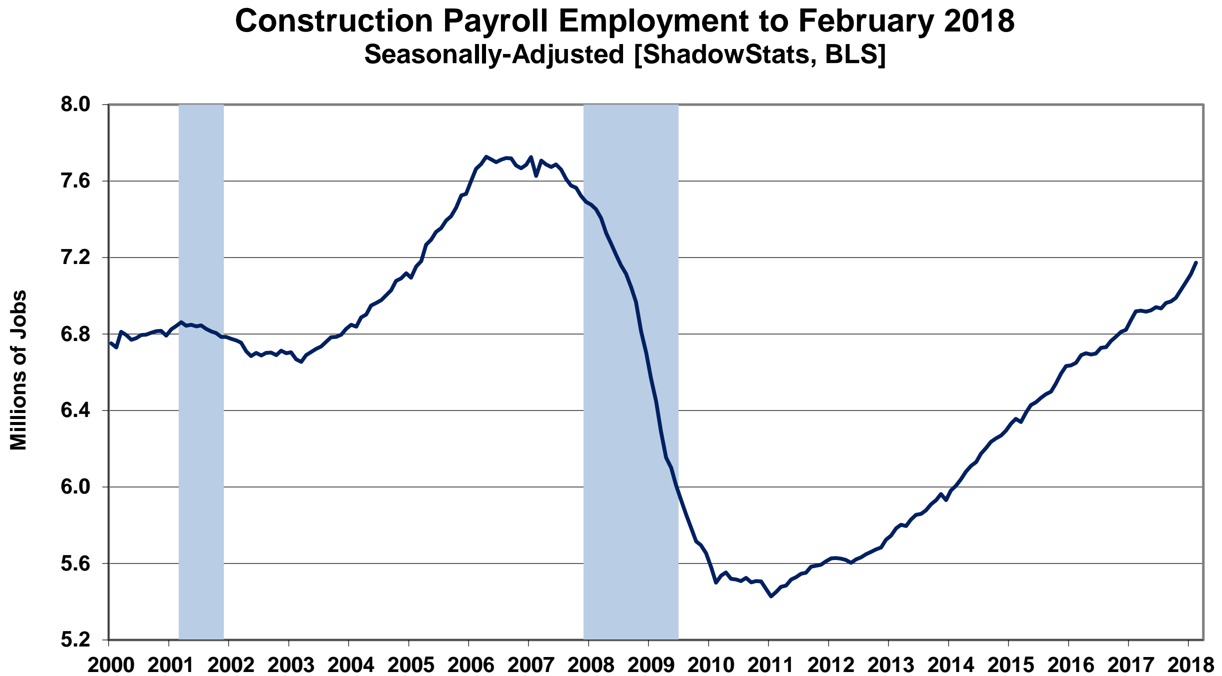
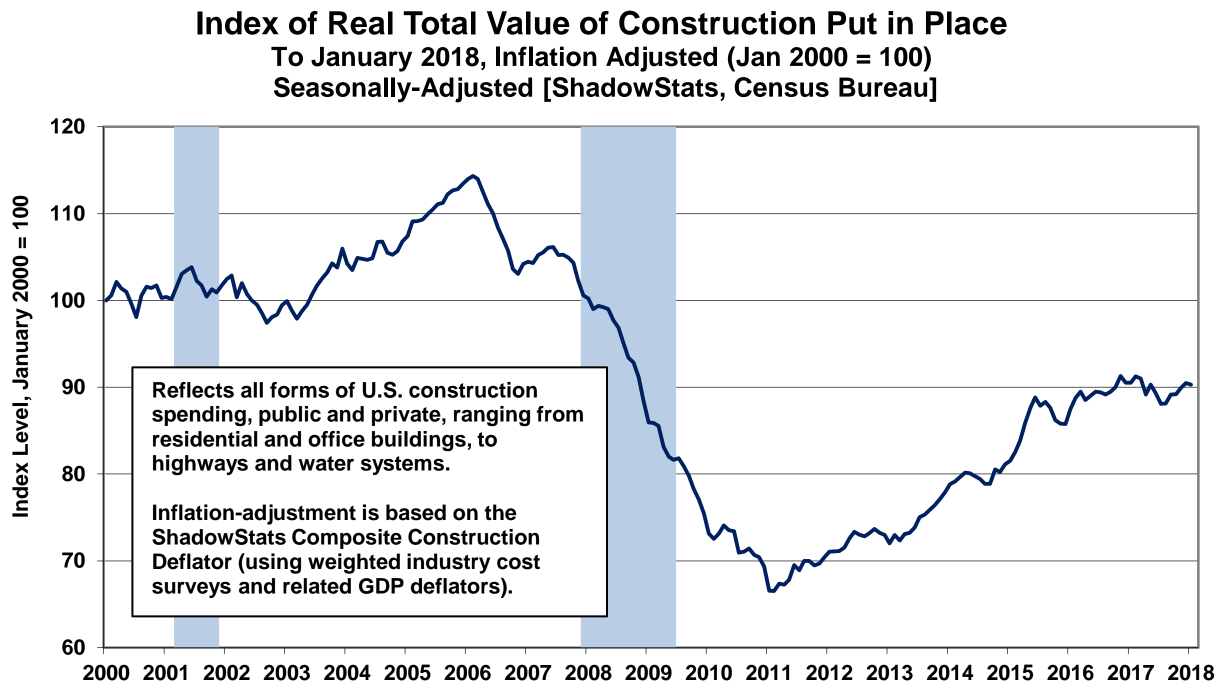
Graph 21: Construction Employment (Payroll Survey), 2000 to Date

(Updates Graph 27 in Commentary No. 938)



Graph 22: Real Total Value of Construction Put in Place, 2000 to Date

(Same as Graph 24 in Commentary No. 938)



[The Supplemental Labor-Detail Background Begins on the Next Page.]

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SUPPLEMENTAL LABOR-DETAIL BACKGROUND

The following material provides background on issues with headline monthly reporting of labor data from the Bureau of Labor Statistics (BLS) surveys: the Establishment Survey (nonfarm payrolls) and the Household Survey (unemployment and employment detail). The text here is not revised each month from its prior version, except for updated monthly numbers through the latest headline detail (currently February 2018), which also are referenced separately in the related standard employment and unemployment text in the *Executive Summary* and *Reporting Detail.* Note: Accompanying Household (December 2017) and Payroll-Survey (January 2018) comments have updated to reflect recently-published 2017 annual benchmarkings.

(I.) Headline Distortions from Shifting Concurrent Seasonal-Adjustment Factors
(II.) Payroll-Employment Monthly Bias Factors (Birth-Death Modeling)
(III.) ShadowStats Alternate-Unemployment Rate (Accounting for Displaced Workers)

(I.) Headline Distortions from Shifting Concurrent Seasonal-Adjustment Factors. There remain serious and deliberate flaws with the government's seasonally-adjusted, monthly reporting of both employment and unemployment (there are parallel issues with the Retail Sales, New Orders for Durable Goods and Trade Deficit series). Each month, the BLS uses a concurrent-seasonal-adjustment process to adjust both the payroll and unemployment data for the latest seasonal patterns. As new headline data are seasonally-adjusted for each series, the re-adjustment process also revises the monthly history of each series. A new seasonally-adjusted history is recalculated for every month, going back five years, so as to be consistent with the new seasonal patterns generated for the current headline number. The problem remains that the historically-comparable revised data are not published along with the new headline detail.

Detailed in the regular monthly BLS press release covering employment/unemployment BLS (second page of the *Technical Note*, subheading *Seasonal Adjustment*):

> For both the household [unemployment] and establishment [payroll] surveys, a concurrent seasonal adjustment methodology is used in which new seasonal factors are calculated each month using all relevant data, up to and including the data for the current month. In the household survey, new seasonal factors are used to adjust only the current month's data. In the establishment [payroll] survey, however, new seasonal factors are used each month to adjust the three most recent monthly estimates. The prior 2 months are routinely revised to incorporate additional sample reports and recalculated seasonal adjustment factors. In both surveys, 5-year revisions to historical data are made once a year.

Discussed in the following paragraphs, the historical data never are published on a consistent basis for the Payroll Survey, even when accompanying headline benchmark revisions. The Household Survey is published only once per year on a consistent basis, in December (see the opening note above), but the numbers become inconsistent, once again, with the ensuing January reporting. Headline month-to-month inconsistencies in the seasonally-adjusted Household Survey are highly variable every month, but that detail never is published and is not knowable by the public.

<u>Effective Reporting Fraud.</u> The problem remains that the BLS does not publish the monthly historical revisions along with the new headline data. As a result, current headline reporting is neither consistent nor comparable with published historical data, including the most-recent months, and the unreported

actual monthly variations versus headline detail can be meaningful. The deliberately-misleading reporting effectively is a fraud. The problem is not with the BLS using concurrent-seasonal-adjustment factors; it is with the BLS not publishing the consistent data, where those data are calculated each month and are available internally to the Bureau. The BLS expressed reasons for not publishing the revised monthly numbers on a consistent basis: "Numerous revisions during the year, however, should be avoided, because they tend to confuse data users and to increase publication costs substantially."

Household Survey. In the case of the published Household Survey (unemployment rate and related data), the seasonally-adjusted headline numbers usually are not comparable with the prior monthly data or any month before. Accordingly, the published headline detail as to whether the unemployment rate was up, down or unchanged in a given month is not meaningful in terms of statistical significance, and what actually happened is not knowable by the public. Month-to-month comparisons of these popular numbers are of no substance, other than for market hyping or political propaganda. In theory, the headline month-to-month reporting in the Household Survey is made consistent only in the once-per-year reporting of December data, with annual revisions back for five years. Again, though, all historical comparability disappears, with the ensuing headline January reporting, and with each monthly estimate thereafter.

Consider *Graphs SLD-1* and *SLD-2*, where data are available from the BLS to calculate the month-to-month seasonal-adjustment variability in the Payroll Survey. Similar detail is not available for the Household Survey, yet the monthly instability likely is of similar magnitude. Shown here as an example with the Payroll Survey, the headline January 2017 payroll level was prepared on a consistent basis with the levels of December 2016 and November 2016, but not with October 2016, with the result the headline monthly gains were consistent only for January and December. With the Household Survey, except for December, seasonally-adjusted monthly detail is not comparable with any other month, so seasonally-adjusted, month-to-month Household Survey comparisons have no meaning, even for the headline month.

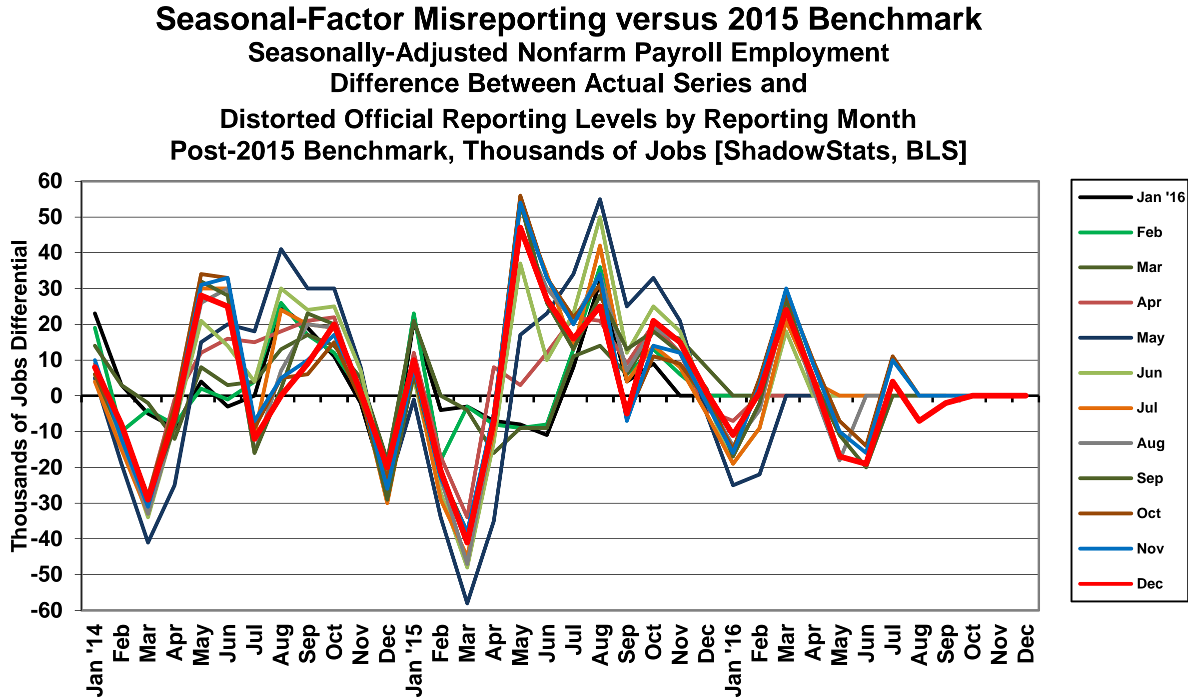
Payroll or Establishment Survey. In the case of the published Payroll Survey data (payroll-employment change and related detail), again, the current monthly changes in the seasonally-adjusted headline data are comparable only with the prior month's month-to-month reporting, not before. Due to the BLS modeling process, the historical data never are published on a consistent basis, even with publication of the annual benchmark revision (see the comments with *Graphs SLD-1* and *SLD-2*).

Where the BLS does provide modeling detail for the Payroll Survey, allowing for third-party calculations, no such accommodation has been made for the Household Survey. ShadowStats affiliate ExpliStats has done such third-party calculations for the payroll series, and the resulting detail of the differences between the current headline reporting and the constantly-shifting, consistent and comparable history are reflected here in *Graph SLD-1*, showing the full monthly variability in the 2016 historical seasonal adjustments in the period since the 2015 payroll benchmark revision. As seen here, consistent data never are published. The benchmark-revised system is run in the background for three months before the headline January publication, which allows the initial headline publishing to stray from the actual initial benchmarking. *Graph SLD-1* shows how far the system strayed from the initial 2016 benchmarking, in its formal benchmark reporting of January 2017.

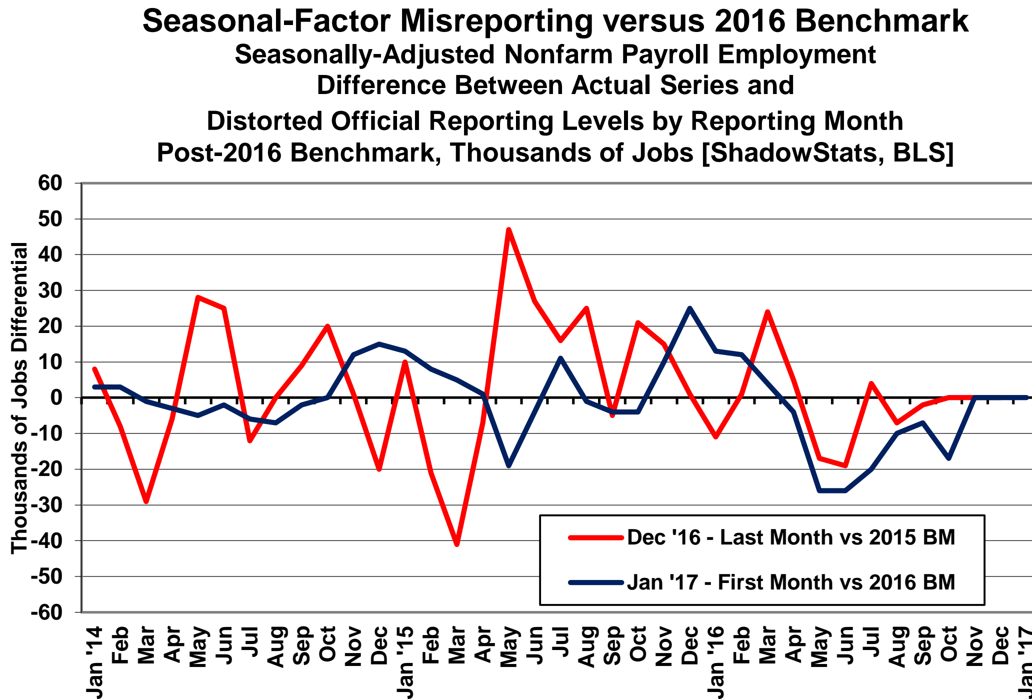
Where the red line reflected seasonal-factor straying through December 2016 from the 2015 benchmarking, the blue line indicates the straying in January 2017 versus the initial 2016 benchmarking. The January 2017 detail suggested a reversal of seasonal factors, consistent with the benchmarking detail

and the new “selective” seasonal adjustment processes. Such variability in seasonal factors, though, rarely is seen in a stable economic series. These data again suggest heavily-gamed headline reporting.

Graph SLD-1: Concurrent-Seasonal-Factor Irregularities – December 2016 Detail versus 2015 Benchmarking



Graph SLD-2: Concurrent-Seasonal-Factor Irregularities – January '17 Detail versus 2016 Benchmarking



As seen in the detail, the differences go both ways and often are much larger. Such was the case for November 2014, coming out of the 2014 benchmark revision, as detailed and discussed in the *Opening Comments* of *Commentary No. 784*. Subscribers interested in the modeling of specific industry payroll components on a consistent month-to-month basis—not otherwise available— should contact johnwilliams@shadowstats.com or at (707) 763-5786.

(II.) Payroll-Employment Monthly Bias Factors (Birth-Death Modeling: BDM). Despite the ongoing, general overstatement of monthly payroll employment (see *Special Commentary No. 885*, entitled *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*), the BLS adds in upside monthly biases to the payroll employment numbers. The continual overstatement is evidenced usually by regular and massive, annual downward benchmark revisions (2011, 2012 and 2017 excepted), with the 2017 benchmark revision of February 2, 2018 on the upside by 138,000 (initially estimated at 95,000).

As a separate matter, though, formalized, downside revisions increasingly have been more than offset by upside revisions to the monthly bias factors, going forward, as was the case in 2016 (see *Commentary No. 864*). The initial estimate (summary number) for the 2016 benchmarking was for a downside revision in total payrolls for March of 2016 by 150,000 (-150,000), down for March 2016 by 224,000 (-224,000) in just private-sector employment (see *Commentary No. 830*). Those changes, however, were massaged and recast to an aggregate downside revision of 81,000 (-81,000) jobs. That change then was used to impute adjustments back to April 2015, and it should have been carried forward to December 2016, but that did not happen, again, as discussed in the *Opening Comments* of *No. 864*.

Despite the published downside revision of 206,000 (-206,000) to March 2015 payrolls in the 2015 benchmarking (see *Commentary No. 784* and *Commentary No. 784-A*), the BLS upped its annual upside-bias factors since then by 65,000. Such discrepancies, however, are not unusual for the BLS.

Considering related actions of recent years, discussed in the benchmark detail of *Commentary No. 598*, the benchmark revision to March 2013 payroll employment was to the downside by 119,000 (-119,000), where the BLS had overestimated standard payroll employment growth.

With the March 2013 revision, though, the BLS separately redefined the Payroll Survey so as to include 466,000 workers who had been in a category not previously counted in payroll employment. The latter event was little more than a gimmicked, upside fudge-factor, used to mask the effects of the regular downside revisions to employment surveying, and likely was the excuse behind an increase then in the annual bias factor, where the new category could not be surveyed easily or regularly by the BLS. Elements here likely had impact on the unusual issues with the 2014 benchmark revision.

Abuses from the 2014 benchmarking were detailed in *Commentary No. 694* and *Commentary No. 695*. With the headline benchmark revision for March 2014 showing understated payrolls of 67,000 (-67,000), the BLS upped its annual add-factor bias by 161,000 for the year ahead.

Historically, the upside-bias process was created simply by adding in a monthly "bias factor," so as to prevent the otherwise potential political embarrassment to the BLS of understating monthly jobs growth. The creation of "bias factor" process resulted from such an actual embarrassment, with the underestimation of jobs growth coming out of the 1983 recession. That process eventually was recast as the now infamous Birth-Death Model (BDM), which purportedly models the relative effects on payroll

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employment of jobs creation due to new businesses starting up, versus jobs lost due to bankruptcies or closings of existing businesses.

February 2018 Add-Factor Bias. In context of the recently published 2017 benchmarking (see the *Opening Comments* of Commentary No. 934-B), the not-seasonally-adjusted monthly add-factor bias in February 2018 was a positively-revised 125,000, previously up by 124,000. The revamped, aggregate upside annual bias for the trailing twelve months through February 2018 is estimated from the current headline bias reporting at 1,071,000, up by 179,000 or 20% from the last prior count of 892,000 in December 2017. That is a monthly average now of 89,250, versus 74,333 in December 2017, jobs created out of thin air, on top of some indeterminable amount of other jobs that are lost in the economy from business closings. Those losses simply are assumed away by the BLS in the BDM, as discussed below.

Problems with the Model. The aggregated upside annual reporting bias in the BDM reflects an ongoing assumption of a net-positive jobs creation by new companies versus those going out of business. Such becomes a self-fulfilling system, as the upside biases boost reporting for financial-market and political needs, with relatively good headline data, while often also setting up downside benchmark revisions for the next year, which traditionally are ignored by the media and the politicians. The BLS cannot measure meaningfully the impact of jobs loss and jobs creation from employers starting up or going out of business, on a timely basis (within at least five years, if ever), or by changes in household employment that were incorporated into the 2017 redefined payroll series. Such information simply is guesstimated by the BLS, along with the addition of a bias-factor generated by the BDM. Private surveying runs counter to the BLS contentions.

Positive assumptions—commonly built into government statistical reporting and modeling—tend to result in overstated official estimates of general economic growth. Along with these happy guesstimates, there usually are underlying assumptions of perpetual economic growth in most models. Accordingly, the functioning and relevance of those models become impaired during periods of economic downturn, and the current, ongoing downturn has been the most severe—in depth as well as duration—since the Great Depression.

Indeed, historically, the BDM biases have tended to overstate payroll employment levels—to understate employment declines—during recessions. There is a faulty underlying premise here that jobs created by start-up companies in this downturn have more than offset jobs lost by companies going out of business. Recent studies continue to suggest that there has been a net jobs loss, not gain, in this circumstance. Nonetheless, if a company fails to report its payrolls because it has gone out of business (or has been devastated by a hurricane), the BLS assumes the firm still has its previously-reported employees and adjusts those numbers for the trend in the company's industry.

The presumed net additional "surplus" jobs created by start-up firms are added on to the payroll estimates each month as a special add-factor. On top of that, the monthly BDM add-factors have been increased now to an average of 89,250 jobs per month for the current year. As a result, in current reporting, the aggregate average overstatement of employment change easily exceeds 200,000 jobs per month (the underlying positive base-assumption upside bias, plus the monthly Birth-Death Model add-factor).

(III.) ShadowStats Alternate-Unemployment Rate (Accounting for Displaced Workers). In 1994, the Bureau of Labor Statistics (BLS) overhauled its system for estimating unemployment, including changing survey questions and unemployment definitions. In the new system, measurement of the previously-

defined discouraged or displaced workers disappeared. These were individuals who had given up looking for work, because there was no work to be had. These people, who considered themselves unemployed, had been counted in the old survey, irrespective of how long they had not been looking actively for work. These were individuals who were and would be considered displaced workers, due to circumstances of severely-negative economic conditions or other factors such as changing industrial activity resulting from shifting global trade patterns.

The new survey questions and definitions had the effect of minimizing the impact on unemployment reporting for those workers about to be displaced by the just-implemented North American Free Trade Agreement (NAFTA). At the time, I (John Williams) had close ties with an old-line consumer polling company, whose substantial economic monthly surveys were compared closely with census-survey details. The new surveying changed the numbers, and what had been the discouraged-worker category soon became undercounted or effectively eliminated. Change or reword a survey question, and change definitions, you can affect the survey results meaningfully.

The post-1994 survey techniques also fell far shy of adequately measuring the long-term displacement of workers tied to the economic collapse into 2008 and 2009, and from the lack of subsequent economic recovery. In current headline reporting, the BLS has a category for those not in the labor force who currently want a job. Including the currently-defined level of "marginally attached workers," which incorporates the currently-defined and undercounted "discouraged workers" category used in the U.6 calculation, those not in the labor force currently wanting a job was an unadjusted 5.364 million in January 2018, 5.171 million on a seasonally-adjusted basis. Due to the coincident annual revision of the BLS's population estimate, these number are not comparable with prior-period estimates (see today's *Opening Comments*). While some contend that that number includes all those otherwise-uncounted discouraged workers, such is extremely shy of underlying reality due to changes in survey methodology since 1994.

The ShadowStats number—a broad unemployment measure more in line with common experience—is my estimate. The approximation of the ShadowStats "long-term discouraged worker" category—those otherwise largely defined out of statistical existence in 1994—reflects proprietary modeling based on a variety of private and public surveying over the last two-plus decades. Other than using the BLS's U.6 estimate as an underlying monthly base with my modeled adjustments, I have not found a way of accounting adequately for the current unemployment circumstance and common experience using just the monthly headline data published by the BLS.

Some broad systemic labor measures from the BLS, though, are consistent in pattern with the ShadowStats measure, even allowing for the shifts tied to an aging population with retiring "baby boomers." Shown in the *Reporting Detail*, the graph of the inverted ShadowStats unemployment measure has a strong correlation with the employment-to-population ratio, in conjunction with the labor-force participation rate (see *Graphs 6* to *8*). Other measures, such as the ShadowStats-Alternate GDP Estimate, the Cass Freight Index, U.S. Petroleum Consumption, etc. are highlighted in subsequent *Graphs 9* to *14* there and in the *Economy* section of *Special Commentary No. 935*.

Headline February 2018 Detail. Adding back into the total unemployed and labor force the ShadowStats estimate of effectively displaced workers, of long-term discouraged workers—a broad unemployment measure more in line with common experience—the ShadowStats-Alternate Unemployment Estimate for February 2018 was 21.8 %, versus 21.8% in January 2018, 21.7% in December 2017, 21.7% in

November, 21.7% in October, 21.9% in September, 22.2% in August, 22.1% in July, 22.0% in June, 22.0% in May, 22.1% in April, 22.4% in March 2017, 22.7% in February, and 22.9% in January. Built upon the headline U.3 and U.6 estimates, the February December 2018 ShadowStats reading was down by 150 basis points or 1.5% (-1.5%) from the 23.3% series high seen in May 2014.

In contrast, the February 2018 headline U.3 unemployment rate of 4.1% was down by 590 basis points or by 5.9% (-5.9%) from its peak of 10.0% in October 2009. The broader U.6 unemployment measure of 8.2% in February 2018, was down by 900 basis points or 9.0% (-9.0%) from its peak of 17.2% April 2010.

A subscriber raised the question as to why the ShadowStats Alternate Unemployment Estimate had been holding around 23%, at the time. Recalculated each and every month, the ShadowStats estimate generally picks up the net flows of headline "discouraged" workers, who have been redefined out of existence after having been inventoried in the BLS accounting of the U.6 rate for about eleven months (where individuals have not looked actively for a job in one year). In turn, U.6 picks up as "discouraged workers" those in U.3 who have not actively looked for work in the last four weeks. It is the resulting reduction in the U.3 and U.6 "unemployed" and the related labor forces used in calculating those respective headline unemployment rates that has accounted for the bulk of the reduction in those headline rates, with much of the difference flowing into and holding reasonably steady in the ShadowStats alternate measure.

Seen in the usual graph of the various unemployment measures (*Graph 1* in the *Executive Summary*, *Graph 5* in the *Reporting Detail*), there indeed is a noticeable divergence in the ShadowStats series versus U.6 and U.3, with the BLS headline U.3 unemployment measure broadly flat recently, against a higher level, uptrending U.6 and a still-higher level, relatively stagnant, but also uptrending ShadowStats number, which had been flat in for several months.

The reason for the longer-term divergence versus the ShadowStats measure, again, is that U.6 only includes discouraged and marginally-attached workers who have been "discouraged" for less than a year. As the discouraged-worker status ages, those that go beyond one year fall off the government counting, even as new workers enter "discouraged" status. A similar pattern of U.3 unemployed becoming "discouraged" or otherwise marginally attached, and moving into the U.6 category, also accounted for the early divergence between the U.6 and U.3 categories.

With the continual rollover, the flow of headline workers continues into the short-term discouraged workers category (U.6), and from U.6 into long-term discouraged worker or displaced-worker status (the ShadowStats measure). There was a lag in this happening as those having difficulty during the early months of the economic collapse, first moved into short-term discouraged status, and then, a year later they began moving increasingly into longer-term discouraged or displaced status, hence the lack of earlier divergence between the series. The movement of the discouraged unemployed out of the headline labor force had been accelerating. While there is attrition in long-term discouraged numbers, there is no set cut off where the long-term discouraged workers cease to exist. See the *Alternate Data* tab at www.ShadowStats.com for historical detail.

Generally, where the U.6 largely encompasses U.3, the ShadowStats measure encompasses U.6. To the extent that a decline in U.3 reflects unemployed moving into U.6, or a decline in U.6 reflects short-term discouraged workers moving into the ShadowStats number, the ShadowStats number continues to

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encompass all the unemployed, irrespective of the series from which they may have been ejected and correspondingly has been reasonably stable over a longer timeframe.

Great Depression Comparisons. Discussed in these regular *Commentaries* covering the monthly unemployment circumstance, an unemployment rate in the 21% to 23% range might raise questions in terms of a comparison with the purported peak unemployment in the Great Depression (1933) of 25%. Hard estimates of the ShadowStats series are difficult to generate on a regular monthly basis before 1994, given meaningful reporting inconsistencies created by the BLS when it revamped unemployment reporting at that time. Nonetheless, as best estimated, the current ShadowStats level likely is about as bad as the peak actual unemployment seen in the 1973-to-1975 recession and the double-dip recession of the early-1980s.

The Great Depression peak unemployment rate of 25% in 1933 was estimated well after the fact, with 27% of those employed then working on farms. Today, less than 2% of the employed work on farms. Accordingly, a better measure for comparison with the ShadowStats number might be the Great Depression peak in the nonfarm unemployment rate in 1933 of roughly 34% to 35%.

[Extended Coverage of the U.S. Trade Deficit Begins on the Next Page.]

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U.S. TRADE DEFICIT (January 2018)

Real Merchandise Trade Deficit Held on Track for Worst Quarterly Showing in Recorded History. Consistent with the discussion in *Commentary No. 937* (based on the advance estimate of the January goods deficit), the headline full reporting of the monthly deficit indeed widened sharply in January 2018, remaining on track to be worst real quarterly U.S. merchandise trade deficit ever recorded. The prior headline real trade-deficit also had deepened in December 2017 by more than expected, widening to monthly, quarterly and annual levels not seen for more than a decade. A pattern continued of monthly deterioration and often prior-period negative revisions seen in recent months.

Noted in *Commentary No. 934-B* the December 2017 nominal balance of payments deficit, before inflation adjustment, including both goods and services, was at its most-negative reading since 2008. Despite a widened December deficit in revision, the headline January 2018 deficit was even worse. Where the deficit widened sharply in calendar year 2017, such reflected rapidly-deteriorating trade balances with China, OPEC and NAFTA (Mexico and Canada), among others. Where the deteriorating deficits are direct subtractions from headline growth in Gross Domestic Product (GDP), the worse-than-expected fourth-quarter 2017 shortfall knocked 1.1% (-1.1%) off real fourth-quarter GDP growth and the unfolding first-quarter 2018 numbers likely will help push first-quarter GDP into negative territory.

January's Nominal Goods and Services Trade Deficit Topped $56 Billion for First Time Since 2008. The nominal January 2018 balance-of-payments trade deficit at $56.6 billion was the worst reading since October 2008. Before inflation adjustment, with oil breaking above $130 per barrel in 2008, the monthly deficit in goods and services had spiked sharply in 2008 to a near-record peak of $66.8 billion in July.

For the inflation-adjusted real merchandise trade in January 2018 of $69.7 billion, however, the same monthly superlative gets pushed back to being the worst since August 2006 ($70.4 billion), only topped minimally by two other spiked months. If the first-quarter 2018 real merchandise trade deficit averages at the January 2018 level, such would be the worst real-quarterly merchandise trade deficit recorded in modern U.S. history. That circumstance is referenced in today's *Opening Comments*, discussed later and plotted in *Graph 4* in the *Opening Comments* and in *Graph 23* here.

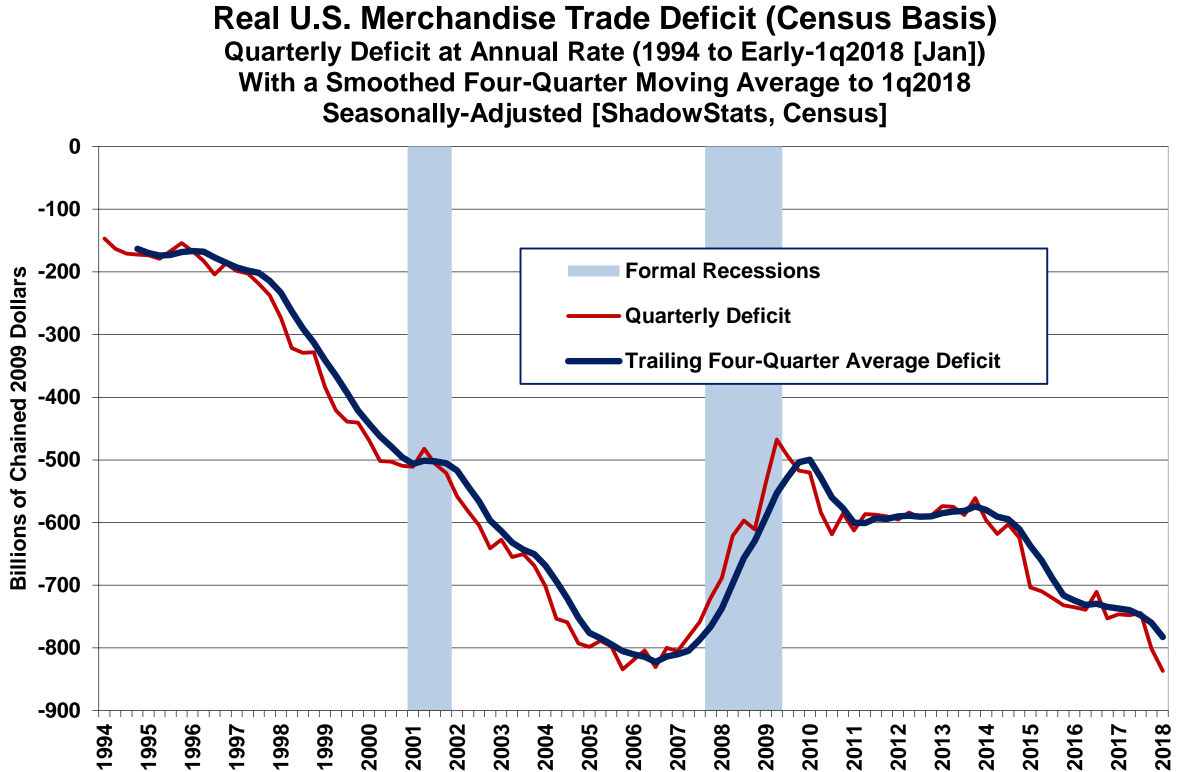
Declining Exports Widened the Nominal January 2018 Trade Deficit. The Bureau of Economic Analysis (BEA) and the Census Bureau (Census) reported Wednesday, March 7th, that the nominal (not adjusted for inflation), seasonally-adjusted monthly trade deficit in goods and services for January 2018 widened on a balance-of-payments basis by $2.693 billion, or by 5.0%, to $56.601 billion, versus a revised, widened deficit of $53.908 [previously $53.118] billion in December 2017. The widening in the monthly January deficit reflected a sharp decline of $2.696 billion in exports, with imports virtually unchanged, with a decline of $0.004 (-$0.004) billion.

The headline January 2018 deficit also widened by $7.909 billion, or by 16.2%, versus the year-ago $48.692 billion trade shortfall for January 2017. Factors affecting the net deterioration in the January 2018 trade balance included declining aircraft orders and industrial supplies, while the aggregate imports reflected surging oil imports offset by declining consumer and capital goods.

Energy-Related Petroleum Products. January 2018 imported oil prices rose by an unadjusted 5.1% to $54.76 per barrel, versus $52.10 per barrel in December 2017, and by 24.6% versus $43.94 per barrel in

January 2017. Separately, unadjusted physical oil-import volume in January 2018 averaged 7.772 million barrels per day, up from 6.903 million in December 2017 but down from 8.353 million in January 2017.

Graph 23: Quarterly and Four-Quarter Smoothed, Real Merchandise Trade Deficit (1994-2018)



Real January 2018 Merchandise Trade Deficit. Reporting detail for the real merchandise trade deficit is discussed here and plotted in *Graph 23* (see also *Graph 4* of the *Executive Summary*). The seasonally-adjusted details are in real terms, net of oil-price swings and other inflation (2009 chain-weighted dollars, as used in GDP deflation), and in context, for the second straight month, of revised 2017 monthly data.

The January 2018 merchandise trade deficit (no services) widened to $69.723 billion, from a revised $68.466 [previously $68.447] billion in December. The January 2018 real trade shortfall of $69.723 billion also widened versus the deficit of $65.549 billion in January 2017.

In 2016, the annual real merchandise trade deficit widened for the year to $734.5 billion, versus $716.4 billion in 2015. The 2016 annual trade shortfall then was the worst since 2008.

On an annual basis, the 2017 real merchandise trade deficit widened to $760.2 billion, versus $734.5 billion in 2016. The 2017 deficit was the worst since 2007.

The first-quarter 2017 deficit narrowed minimally to a $746.6 billion, with the second-quarter 2017 deficit widening to $748.0 billion, the third-quarter 2017 deficit revised to $744.3 [previously $744.2] billion, with the fourth-quarter 2017 real merchandise trade deficit exploding to a revised $801.7 [previously $801.6] billion, the worst showing since second-quarter 2007.

Based solely on the initial headline detail for January 2018, first-quarter 2018 is on track for an annualized quarterly deficit of $836.7 billion. Such would be the worst deficit in the history of the series, in the modern economic history of the United States.

Irrespective of occasional, quarterly aberrations and increasingly irregular, headline month-to-month activity, headline deficits broadly should continue to deteriorate sharply in the months and quarters ahead, revising and intensifying the ongoing and commonly-negative impact on headline GDP reporting.

Ongoing Cautions and Alerts on Data Quality. Monthly trade data can be influenced by irregular shipping patterns, affected by factors ranging from labor disruptions to unusual weather conditions. Separately, potentially heavy distortions in headline data continue from inconsistent and unstable 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/non-expansion and related, ongoing disruptions have distorted regular patterns of seasonality.

[The* Hyperinflation Watch *begins on the next page.]

HYPERINFLATION WATCH

MONETARY CONDITIONS

Beware Unexpected Economic Weakness and Mounting Trade Deficit Pressures! In the context of today's stronger-than-expected headline February labor details, consensus expectations have to be riding high for an interest rate hike out of the Federal Open Market Committee (FOMC) of the Board of Governors of the Federal Reserve System on March 21st.

Nonetheless, as regularly discussed here, unexpected, negative economic shocks loom in the next month or so, with retail sales and industrial production continuing to show negative catch up following recent hurricane distortions, as well as intensifying issues with the labor numbers. Systemic reporting distortions largely should have passed from the numbers by publication of headline February 2018 economic data. Several non-consensus factors loom:

- Discussed below, money supply growth has started to show a pattern of weakness common to the onset of economic downturns.
- The rate-hike "clinching," strong February jobs report, was of questionable quality (see the *Reporting Detail*) and should be followed by a series of much weaker, related underlying detail reports such as retail sales and industrial production (see *Pending Releases* in the *Week, Month and Year Ahead* section).
- The Fed well may come under political pressure from the Administration to back off its support of the U.S. dollar, as discussed in today's *Opening Comments*.
- In particular, though, as market sentiment increasingly shifts towards a weaker economy, pressure and expectations should mount on the FOMC to pull back from further tightening.

With the U.S. central bank's primary concern being the maintenance of solvency and liquidity in a still-troubled banking system, intensifying economic difficulties remain likely to cause the FOMC to back off its formal, current pattern of promised rate hikes and balance-sheet liquidation, to revert again towards expanded quantitative easing, as openly allowed for in current FOMC policy.

February 2018 Money Supply M3 Annual Growth Eased to 4.4% from an Upwardly-Revised 4.6% in January 2018, with the Monetary Base Annual Growth Dropping to 2.3% from 4.9%. Based on three-plus weeks of reporting, with continued, sharp softening growth in the narrower M2 and M1 measures, the estimate of nominal annual growth for the ShadowStats Ongoing M3 Money Supply in

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February 2018 declined to a five-month low of 4.4%, versus an upwardly revised 4.6% [previously 4.5%] in January 2018.

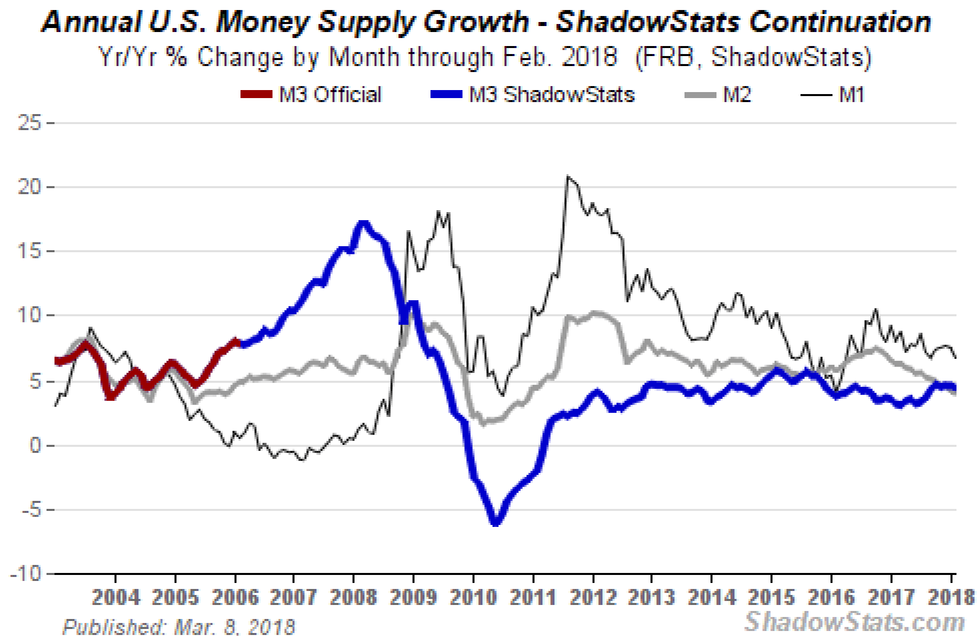
Those growth rates were against unrevised annual gains of 4.6% in December 2017, 4.5% in November 2017 and 4.7% in October 2017. That October annual growth rate was the highest level of year-to-year monthly growth since November 2015.

Those M3 growth rates were against unrevised annual gains of 4.2% in September 2017, 3.6% in August 2017 and irregular notching of annual growth lower back in time, until an unrevised 3.0% in March 2017. That had been the weakest year-to-year change since July 2012.

M2 Annual Growth Weakest Since December 2010. Separately, nominal year-to-year growth for M2 declined to 4.0% in February 2018, its lowest annual growth rate since December 2010, following unrevised annual growth of 4.2% in January 2018, 4.7% in December 2017, 4.6% in November 2017, 5.0% in October 2017, 5.1% in September 2017, 5.3% in August 2017, 5.6% in July 2017, 5.6% in June 2017 and 5.9% in May 2017.

M1 Annual Growth at a 21-Month Low. Annual nominal growth in February 2018 M1 slowed to 6.8%, its lowest annual growth rate since April 2016, down from 7.6% in January 2018, versus unrevised annual gains of 7.7% in December 2017, 7.6% in November 2017, 7.5% in October 2017, 6.8% in September 2017, 7.2% in August 2017, 8.7% in July 2017, 7.7% in June 2017 and 7.9% in May 2017.

Graph HW-1: Comparative Money Supply M1, M2 and M3 Yr-to-Yr Changes through February 2018



For those living in the headline money-supply world comprised of just the Fed's M1 and M2, annual money growth had been relatively stronger for both M1 and M2, than for M3, although that difference narrowed recently, with M3 growth now declining in tandem, with M1 and M2, where M3 narrowly had overtaken slowing annual M2 growth last month. With all three money measures virtually unchanged or

negative month-to-month, along with sharply declining annual growth rates, the patterns here are suggestive of weakening or declining economic activity.

Where there had been some accelerating pace of annual growth in M1 into December, that likely reflected some movement into cash/near-cash. The relative weakness in annual M3 growth, versus M2 and M1 (M2 includes M1; M3 includes M2) had reflected a shift over time in funds from accounts included just in M3, such as large time deposits and institutional money funds, into accounts in M2 and M1. The recent relative gains in annual M3 growth may have reflected a returning flow of cash from M2 back into M3 accounts, again, such as large-time deposits and institutional money funds. Yet, the latest, softening headline details likely reflect softening business activity at the moment, more than anything else does. The latest estimates of level and annual changes for February 2018 M3, M2 and M1, and for earlier periods, are detailed in the Alternate Data tab of www.ShadowStats.com. See the *Money Supply Special Report* for full definitions of those measures.

Amidst Series Revisions, Annual Growth the Monetary Base Also Has Pulled Back Sharply in the Last Month or Two. As annual growth in M3 jumped in recent months, so, too, did annual growth in the Monetary Base. In the wake of near-term volatility surrounding recent rate hikes by the FOMC, and the related market efforts by New York Fed to establish or maintain consistent trading-range activity for the targeted federal funds rate, the level of the monetary base had been reasonably stable, with annual percentage change fluctuating around zero.

Still, in late 2017, the pace of annual growth had turned higher, rapidly moving to consecutive, multi-year highs, pulling back in roughly parallel timing with M3. Both series peaked near-term in December 2017 and multi-year highs (Monetary Base up by 9.7% year-to-year in the two weeks ended January 3, 2018, now has fallen back to levels last seen in September 2017, at 2.3% as of the end of February 2018). Accompanying *Graphs HW-2* and *HW-3*, reflect that detail.

Aside from short-term gyrations around the timing of change in the targeted federal funds rate (as could have affected the late-December 2017, early-January 2018 data), circumstances generally should remain relatively stable, until the Fed begins to sell its Treasuries and Mortgage-Backed Securities more heavily, as part of its planned "balance sheet normalization," or otherwise to embark upon expanded quantitative easing, amidst increasing liquidity stresses in the banking system from deteriorating economic conditions.

The FOMC accelerated its liquidation of Treasury notes and bonds coming into late-January, the first week of February 2018, likely triggering liquidity problems that exacerbated heavy stock market selling at the time.

Yet, the level of the Monetary Base remains well within the bounds of activity seen in the last several years. That said, prior to the institution of Quantitative Easing, changing the level of the Monetary Base had been the primary tool of the Federal Reserve Board's Federal Open Market Committee (FOMC) for targeting growth in the money supply. Whether the recent upside movements in annual growth for M3 and the Monetary Base resume or continue to soften, remains to be seen, and may depend on headline economic reporting in the near-term. Recent money growth was beginning to look like a potential covert shift in FOMC policy (most-recently towards easing/now perhaps more overtly towards a tightening).

These issues will be reviewed further in the *Hyperinflation Watch* of next week's *Commentary No. 940.*

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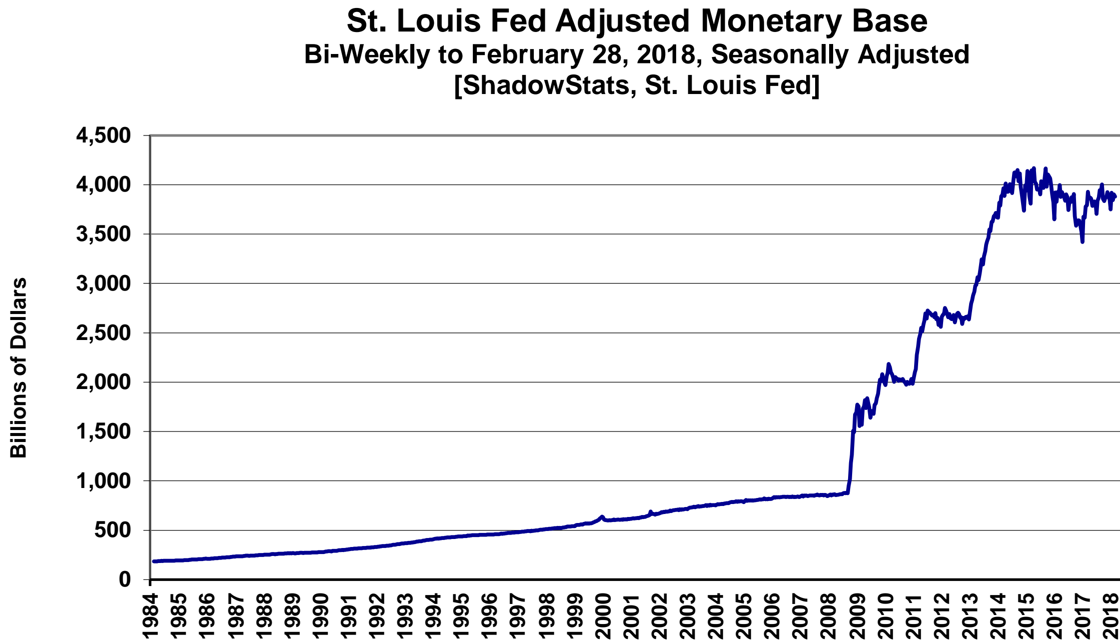
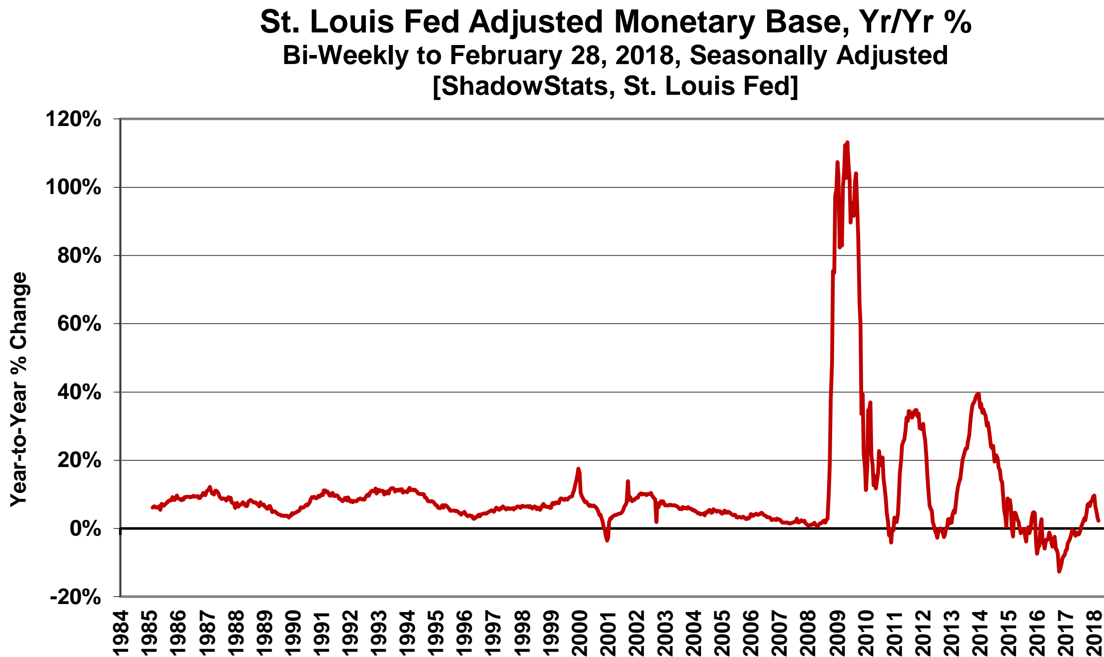
Graph HW-2: Saint Louis Fed Monetary Base, Billions of Dollars (1984 to February 28, 2018)



Graph HW-3: Year-to-Year Percent Change, Saint Louis Fed Monetary Base (1985 to February 28, 2018)



[The **Consumer Liquidity Watch** *begins on the next page.]*

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CONSUMER LIQUIDITY WATCH

CONSUMER LIQUIDITY, INCOME, CREDIT AND RELATIVE OPTIMISM. *[Updated for Fourth-Quarter 2017 Household Debt, January 2018 Consumer Credit Outstanding and the full-February 2018 Consumer Sentiment, opening paragraphs and links.]*

Continuing Consumer Liquidity Stresses Constrain Broad Economic Activity. The U.S. consumer faces increasing financial stress, which recently had been mirrored in renewed softening of fundamental headline economic activity, including Payroll-Employment, Real Retail Sales, Housing and Construction, and the Manufacturing/Production sector, all pre-hurricane activity. Net of what have been mixed, but significant, near-term hurricane distortions, initial hits to activity were followed by related and transient economic boosts from recovery, replacement and restoration activity. Funded by insurance payments and savings liquidation, those distortions broadly should pass from headline data by the February/March reporting of January/February 2018-headline detail. Discussed recently (see *Commentary No. 936* and *Commentary No. 937*) hurricane-boosted activity appears to be passing, as early first-quarter economic activity continues to turn down. Such effects have been, and will continue to be seen, as discussed in the separate analyses of relevant series in covered in the regular *ShadowStats Commentaries*. While there have been recent signals of faltering consumer liquidity (see the updated Consumer Credit Outstanding), headline consumer optimism has remained strong, despite rapidly softening activity.

Monthly series that have faced the most severe, disaster-triggered reporting disruptions, where headline details have yet to stabilize or correct, still include in particular Household Survey Employment and Unemployment (see today's *Reporting Detail*). Retail Sales and Industrial Production appear to have stabilized, and are beginning to turn down anew, but they still need to subside to levels stable with normal consumption activity and inventories. Despite the initial slowing in Fourth-Quarter 2017 GDP growth, the series remains heavily bloated from the disaster-distortions (see *Commentary No. 933*), a downside revisions still could loom for the fourth-quarter detail, along with increasing odds for an outright quarterly contraction in real First-Quarter 2018 GDP (see *Commentary No. 937*).

***Liquidity Issues Limit Economic Activity*.** Severe and persistent constraints on consumer liquidity of the last decade or so drove economic activity into collapse through 2009, and those conditions have prevented meaningful or sustainable economic rebound, recovery or ongoing growth since. The limited level of, and growth in, sustainable real income, and the inability and/or unwillingness of the consumer to take on new debt have remained at the root of the liquidity crisis and ongoing economic woes.

These underlying pocketbook issues contributed to the anti-incumbent electoral pressures in the 2016 presidential race. The post-election environment showed a near-term surge in both the consumer confidence and sentiment measures to levels generally not seen since before the formal onset of the recession in 2001, let alone 2007. Yet, underlying liquidity conditions, economic reality and lack of

positive actions out of the government to turn the economy meaningfully, so far, all have continued to remain shy of consumer hopes, and those numbers have begun to stumble in recent detail.

A temporary liquidity boost fueled by recent disaster effects, such as insurance payments or savings drawdowns to fund replacement of storm-damaged assets, are of a one-time nature and short-lived in terms of ongoing economic impact. The underlying, fundamental longer-term liquidity issues remain in place. Nonetheless, mirroring the disaster-fueled economic hype in the popular press, consumer optimism had rallied strongly, albeit, again, now faltering or mixed, as discussed shortly.

Including the various consumer-income stresses discussed in *Special Commentary No. 888*, broad, underlying consumer-liquidity fundamentals simply have not supported, and still do not support a fundamental turnaround in general economic activity—a post "Great Recession" expansion—and broadly are consistent with a "renewed" downturn in that non-recovered economic activity. Indeed, never truly recovering post-Panic of 2008, limited growth in household income and credit have eviscerated and continue to impair broad, domestic U.S. business activity, which is driven by the relative financial health and liquidity of consumers. These underlying liquidity conditions and reality—particularly income and credit—remain well shy of average consumer hopes and needs, irrespective of the new tax laws.

The combined issues here have driven the housing-market collapse and ongoing, long-term stagnation in consumer-related real estate sales and construction activity, and have constrained both nominal and real retail sales. Related, personal-consumption-expenditure and residential-construction categories accounted for 73.1% of the headline real, fourth-quarter 2017 U.S. GDP.

Net of short-lived disaster distortions (insurance payments, savings liquidations), with the better-quality economic indicators and underlying economic reality never having recovered fully from the collapse into 2009, consumers increasingly should pull back on consumption in the months ahead. Underlying reality is evident in more-meaningful economic indicators—not the GDP—irrespective of the transient boosts from disasters or political gimmicks, discussed recently in *General Commentary No. 929* and the *Executive Summary* of *Commentary No. 928*.

Anecdotal Evidence of Business and Consumer Uncertainty Continue to Indicate a Seriously-Troubled Economy and Very Dangerous Financial Markets. Against what appears to be a headline economic consensus that all is right again, with the U.S. economy and financial markets, underlying real-world common experience suggests a much different outlook. Regularly discussed here, ongoing non-recovery, low-level stagnation and signs of renewed downturn remain patterns common to key elements of headline U.S. economic activity. Consider factors ranging from housing sales and broad construction activity, to headline reporting of domestic manufacturing, as well as those series that are heavily gimmicked, such as the Gross Domestic Product (GDP), also regularly discussed and dissected here.

Similar signals of such economic stress are seen in patterns of activity that move along with the real-world broad economy. They range from indicators such as freight volume and domestic consumption of petroleum to factors such as levels of real consumer debt outstanding, real average weekly earnings and measures of employment stress in the broad economy. Those stresses are reflected in historically-low levels of the employment-population ratio and the labor-force participation rate. With the liquidity-starved U.S. consumer driving three-quarters of the GDP, there is no way for the broad economy to boom—happy Retail Sales headlines aside—without some meaningful shift in underlying consumer circumstances. Links to background discussions in these various areas are found in the *Recent*

Commentaries section of the *Week, Month and Year Ahead*, along with links to background discussions on the quality of the more-politicized GDP (*Commentary No. 928*) and employment/unemployment details discussed in the *Supplemental Labor-Detail Background* of *Commentary No. 930-B*.

Beyond assessing headline economic numbers, ShadowStats also looks at anecdotal evidence, including comments by subscribers and clients, who live in the real world. Two broad observations have come from a number of recent conversations. First, real estate activity appears to be slowing in recently strong areas. Second, a number of major companies are "sitting on their hands," holding back on issuing new contracts to third-party vendors in areas such as upgrading computer systems and other consulting. The companies cite the slowdown in contracts as "due to uncertainty," an issue, as well with the U.S. consumer, where that uncertainty encompasses:

- Unfolding circumstances in the Washington, D.C. political arena.
- Where the manic financial markets are headed.
- Ultimately, what is, or will be, happening to near-term business activity?

Economic reporting, and business and financial-market stories sometimes receive happy year-end spikes in the press. That circumstance was supplemented in late-2017 by near-term hurricane boosts to, and distortions of, some current economic activity, such as the November Retail Sales reporting. The latter circumstance should prove fleeting. The underlying, broadly-faltering U.S. economy should be dominating headline economic reporting, once again, and all too soon, most likely in the next couple of months. That said, albeit reflecting some of the headline economic hype in the popular press, headline consumer optimism remains strong.

Consumer Optimism: Consumer Sentiment and Confidence Boom. On top of the December 2017 readings pulling back sharply for both The Conference Board's Consumer-Confidence Index® (Confidence), and the University of Michigan's Consumer Sentiment Index (Sentiment), January 2018 Confidence and Sentiment (February 2nd) readings were minimally-positive and down, with the February numbers rising anew. Such is despite faltering home sales in January (see *Commentary No. 937 Reporting Detail*). The February 2018 consumer numbers were just updated for Confidence (February 27th) and Sentiment (March 2nd).

Reflected in *Graphs CLW-1* and *CLW-2*, Confidence and Sentiment monthly readings had jumped sharply, respectively to multi-year highs in November and October. Yet, the December Confidence reading plunged, more than offsetting the November gain and most of the October gain, in context of a downside revision to the November reading. Similarly, November and December Sentiment readings, and now January also pulled back sharply or only minimally recovered, largely offsetting the October surge there.

Nonetheless, both measures turned higher in February 2018, despite mounting economic and financial-market uncertainties. Following a downside revision to the January 2018 reading, Confidence jumped to its highest level since November 2000, when both series were then falling into the 2001 recession. The rising numbers here for both Confidence and Sentiment are at their highest levels since 2000, above their pre-2007 recession peaks. They remain down from their early-2000 peaks, however, by 9.6% (-9.6%) for Confidence and by 11.0% (-11.0%) for Sentiment.

For both the Conference Board's seasonally-adjusted [unadjusted data are not available] Consumer-Confidence Index® (*Graph CLW-1*), and the University of Michigan's not-seasonally-adjusted Consumer-Sentiment Index (*Graph CLW-2*), the three-month moving averages also were above pre-2007 recession highs, yet the still-high moving averages have flattened out, having begun to falter in September 2017, before the storm-distorted, unusual headline surges in October and November activity.

On a monthly as well as smoothed bases (see *Graphs CLW-1 to CLW-3*), both series continued above their pre-2007 recession peaks. On a monthly basis, the Confidence measure at its highest level since May 2000, as it had been plummeting into the onset of 2001 recession, with the current February 2018 reading down from its interim May 2000 peak level by 9.6% (-9.6%).

On a monthly basis, aside from its near-term peak of October 2017, the Sentiment measure is at its highest level since January 2004, currently down by 3.9% (-3.9%) from that interim January 2004 peak.

Pre-election, September 2016 Confidence and Sentiment jumped and then plunged in October 2016, likely reflecting concerns as to the direction of the presidential race. Post-election, both measures rallied sharply, reflecting surges in consumer optimism into early-2017. Both series then topped and pulled back, with mixed numbers into August and September 2017, but with the October 2017 Sentiment measure showing a large jump, purportedly because consumers were willing to accept diminished prospects for their living standards (see *Commentary No. 916*)? Nonetheless, the Sentiment measure retrenched in November and December. The Conference Board blamed hurricane impact in Texas and Florida for its downturn in September 2017 Confidence, but those numbers exploded into October and November 2017, again reversing largely with December's headline downturn.

Showing the Consumer Confidence and Consumer Sentiment measures on something of a comparable basis, *Graphs CLW-1* to *CLW-3* reflect both measures re-indexed to January 2000 = 100 for the monthly reading. Standardly reported, the Conference Board's Consumer Confidence Index® is set with 1985 = 100, while the University of Michigan's Consumer Sentiment Index is set with January 1966 = 100.

The Confidence and Sentiment series tend to mimic the tone of headline economic reporting in the press (see discussion in *Commentary No. 764*), and often are highly volatile month-to-month, as a result. Recent press has been highly positive on the headline economic and employment news, reflecting short-lived hurricane boosts to activity particularly on unemployment (not payroll employment), retail sales and industrial production. As headline financial and economic reporting in the next month or two turn increasingly-negative and unstable, so too should the surging "optimism." Increasingly, a downturn in consumer outlook should take hold, despite any euphoric headlines, reflecting some deep-seated consumer liquidity issues.

Broadly, though, the harder, financial consumer measures remain well below, or are inconsistent with, periods of historically-strong economic growth as suggested by headline GDP growth in 2014, for second-and third-quarter 2015 and for third-quarter 2016 and into third-quarter 2017. In current environment of surging optimism, beyond having happy feelings about the future, consumers still need actual income, cash-in-hand or credit in order to increase their spending.

Smoothed for irregular, short-term volatility, the two series still generally had held at levels seen typically in recessions, until the post-2016 election circumstance. Suggested in *Graph CLW-3*—plotted for the last 48 years—the latest readings of Confidence and Sentiment recently have recovered levels seen in periods

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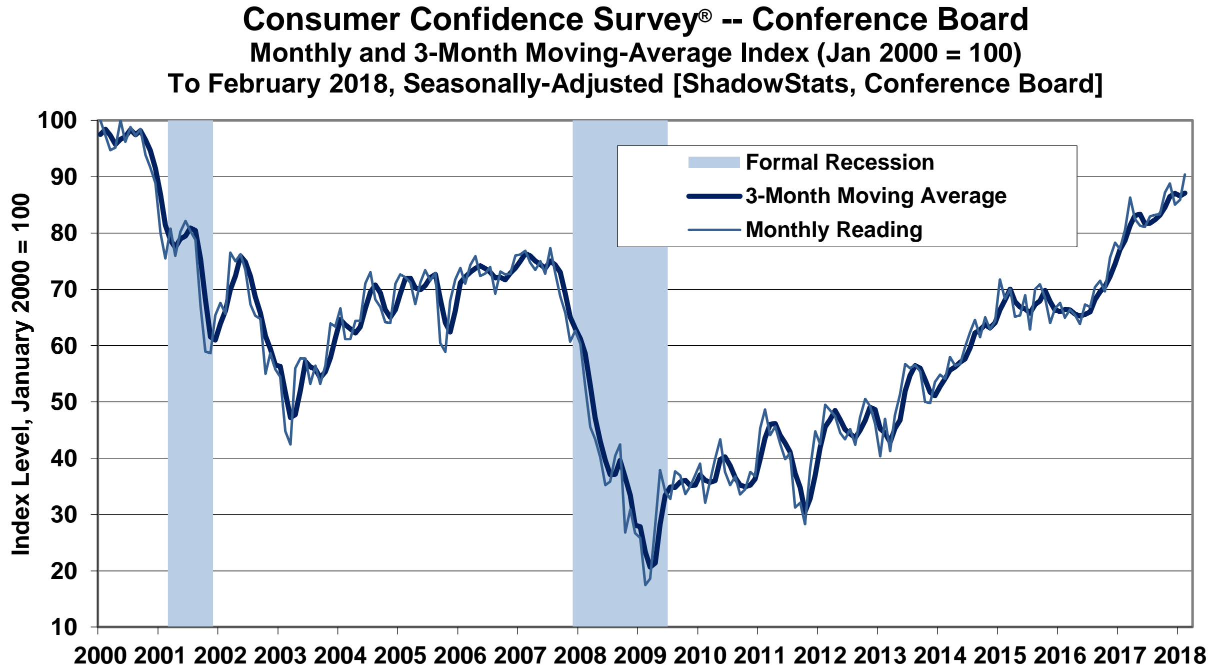
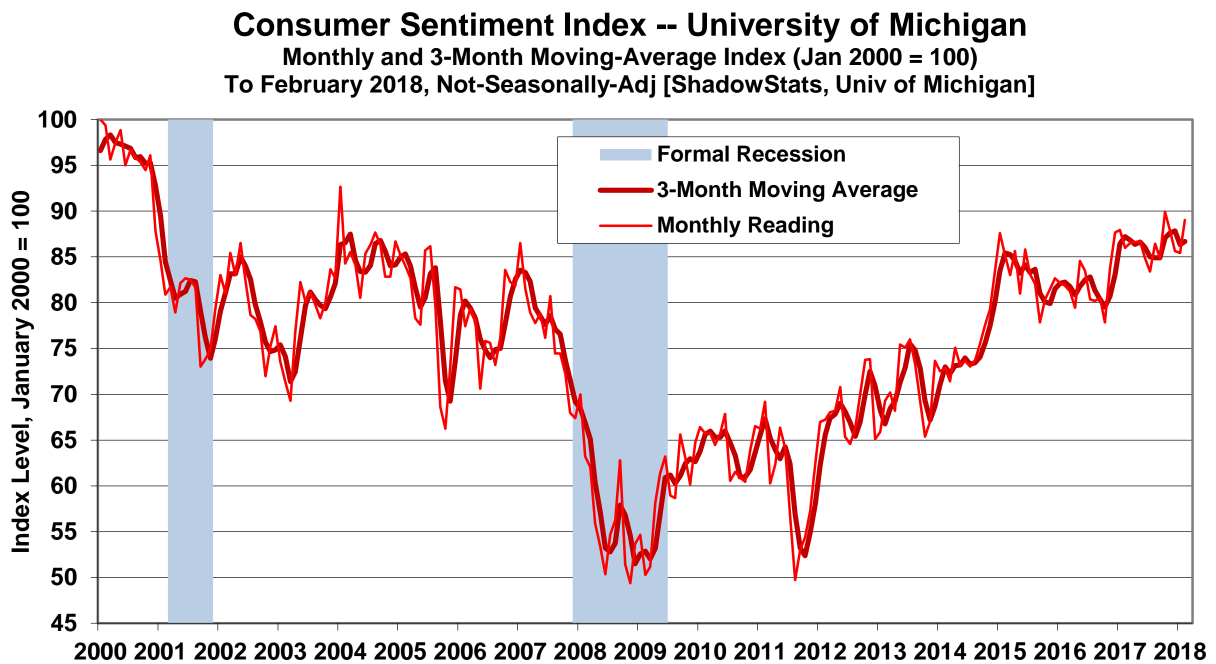
of normal, positive economic activity of the last four decades, with their six-month moving averages at levels last seen going into the 2001 recession, although increasingly, they appear to be topping out.

Graph CLW-1: Consumer Confidence (2000 to 2018)



Graph CLW-2: Consumer Sentiment (2000 to 2018)



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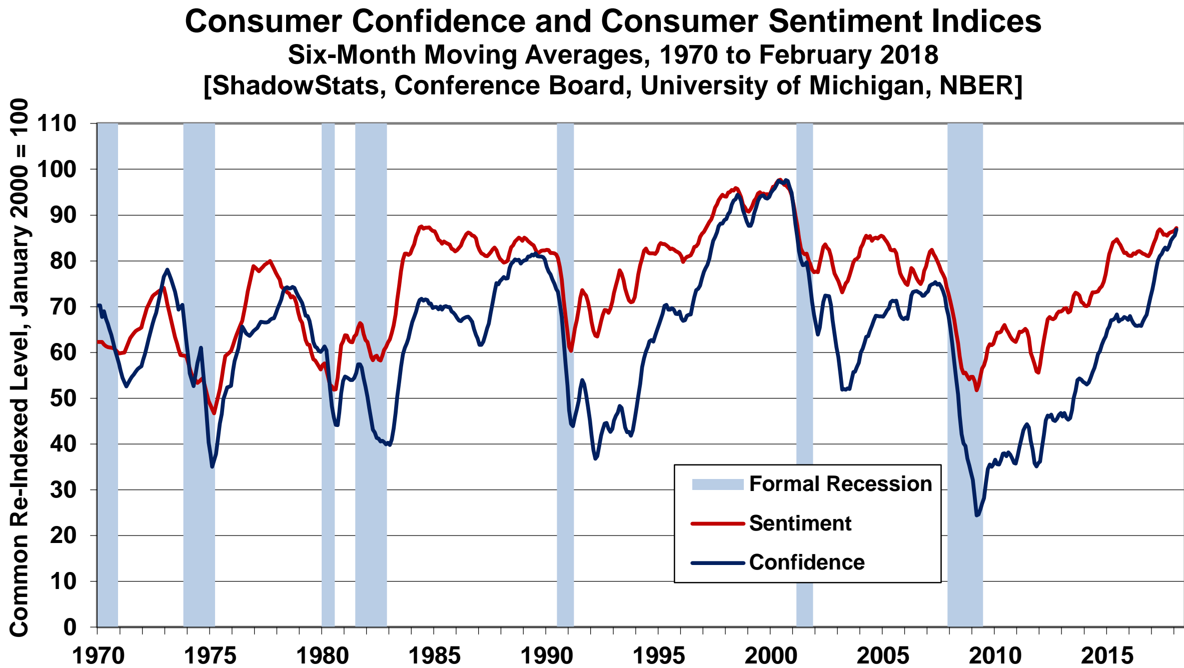
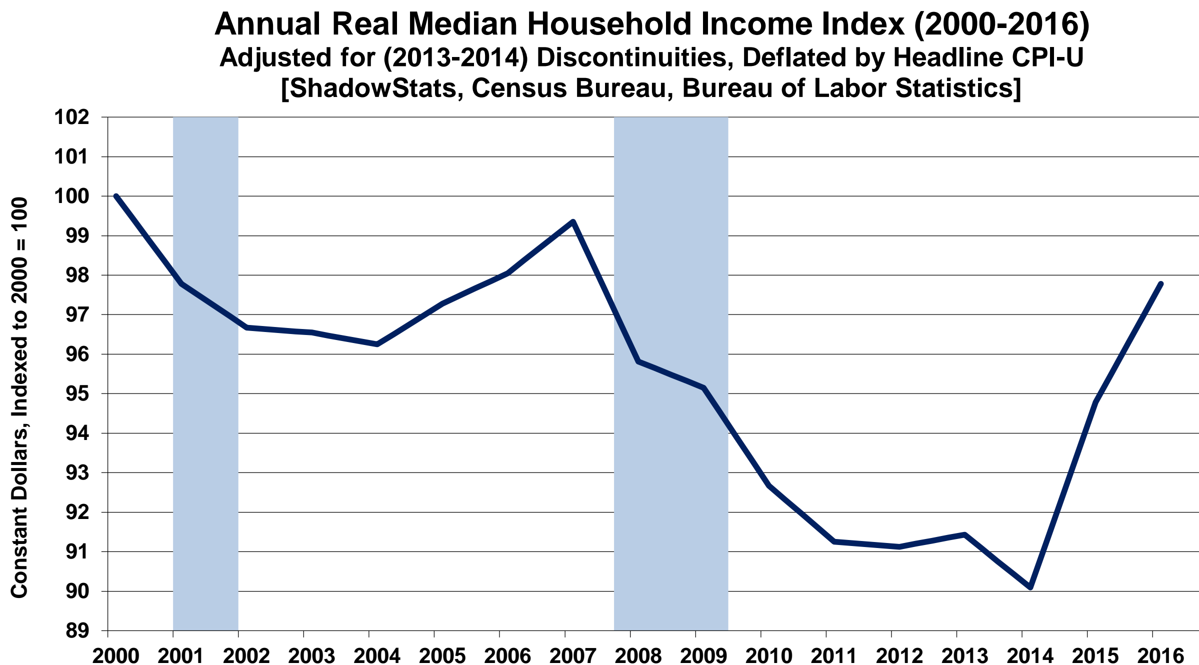
Graph CLW-3: Comparative Confidence and Sentiment (6-Month Moving Averages, 1970 to 2018)



2016 Annual Real Median Household Income Still Was Below Its 2007 Pre-Recession High, Below Activity in the Late-1990s, About Even with the Mid-1970s. The measure of real monthly median household income, which was provided by www.SentierResearch.com, generally can be considered as a monthly version of the annual detail shown in *Graph CLW-4*, based on the most-recent annual detail released by the Census Bureau and as discussed the *Opening Comments* of *Commentary No. 909*.

Graph CLW-4: Annual Real Median U.S. Household Income (1967 to 2016)



Last Monthly Estimate Showed Stagnating Monthly Real Growth. Last reported by Sentier Research, in what appears to have been the final estimate for the series, May 2017 Real Median Household Income was statistically unchanged, despite a boost from falling gasoline prices. Discussed in *General Commentary No. 894*, and in the contexts of then-faltering gains in post-election consumer optimism, and inflation-adjusted activity boosted by declining headline Consumer Price Index (CPI-U) inflation (weakened by seasonally-adjusted gasoline price declines), May 2017 Real Median Monthly Household Income was "statistically unchanged" (a statistically-insignificant monthly gain of 0.10%). That followed a statistically-significant monthly gain of 1.00% in April 2017. Shown in *Graph CLW-4*, such enabled May 2017 real monthly median household income to hold a level regained in April and otherwise last seen in February 2002. Year-to-year real median household income rose to 2.44% in May 2017, the highest level since June 2016, following an annual gain of 1.57% in April 2017 (see *Graph CLW-5*).

Where real monthly median income plunged into the headline trough of the economic collapse in 2009, it did not then rebound in tandem with the headline GDP activity. When the GDP purportedly started its solid economic recovery in mid-2009, the monthly household income numbers nonetheless plunged to new lows, hitting bottom in 2011. The income series then held in low-level stagnation, until collapsing gasoline prices and the resulting negative CPI-U inflation drove a post-2014 uptrend in the inflation-adjusted monthly income index. The index approached pre-recession levels in the December 2015 reporting, but it remained minimally below the pre-recession highs for both the formal 2007 and 2001 recessions until recent months. Real median household income had the potential to resume turning down anew, as the headline pace of monthly consumer inflation picked up anew, with the August 2017 CPI.

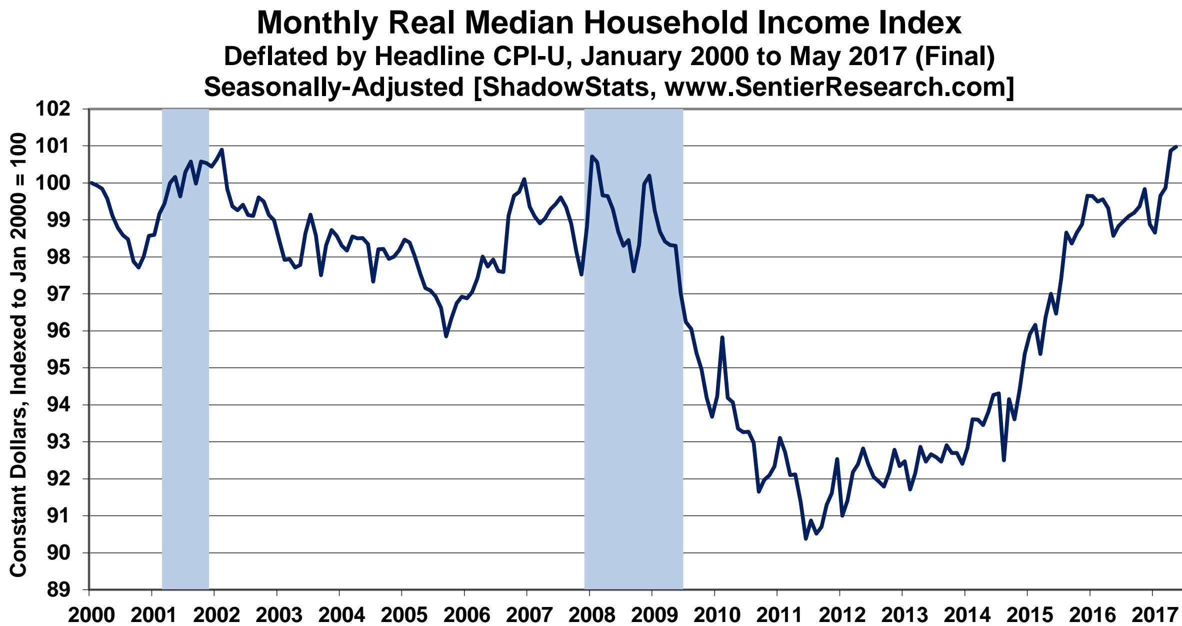
Nonetheless, the most-recent recent "rebound" reported in the series still left consumers financially strapped. Where lower gasoline prices had provided some minimal liquidity relief to the consumer, indications are that any effective extra cash largely was used to help pay down unsustainable debt or other obligations, not to fuel new consumption. Except for mixed gyrations in first-half 2017, the effects of changing gasoline prices in the headline CPI-U generally had reversed, pushing headline consumer inflation higher and beginning to push real income lower.

Differences in the Monthly versus Annual Median Household Income. The general pattern of relative monthly historical weakness has been seen in the headline reporting of the annual Census Bureau numbers, again, shown in *Graph CLW-4*, with 2014 real annual median household income having hit a ten-year low, and, again, with the historically-consistent 2015 and 2016 annual number still holding below the 2007 pre-recession high.

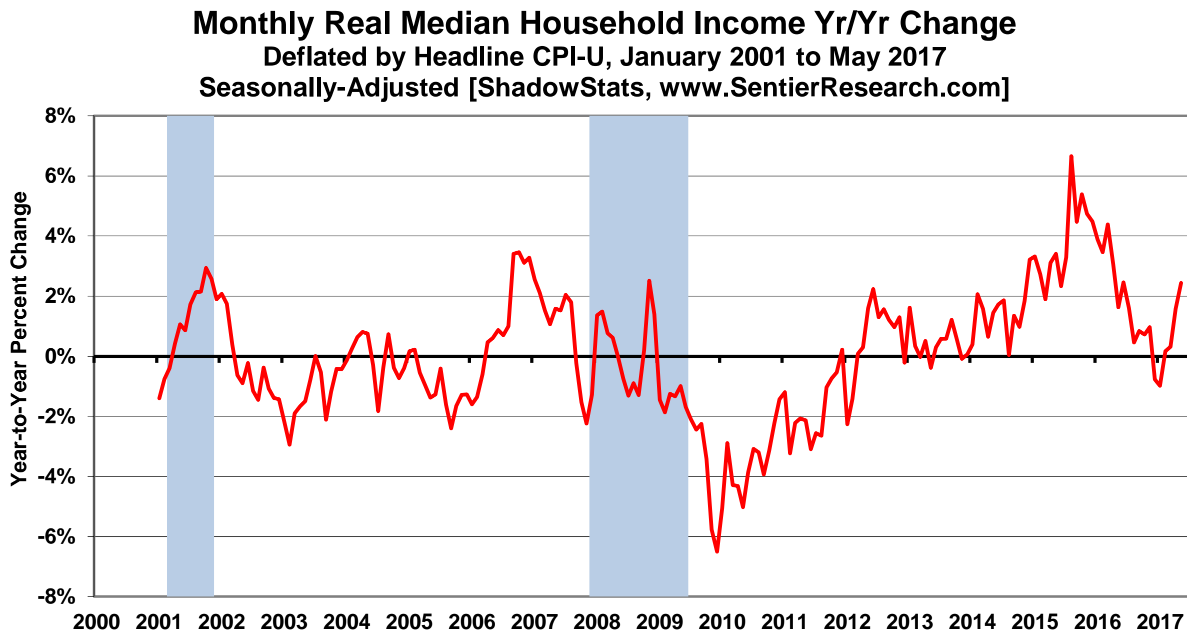
The Sentier numbers had suggested a small increase in 2014 versus 2013 levels, low-inflation induced real increases in 2015 and 2016. Allowing for the direction difference in 2014, and continual redefinitions and gimmicks in the annual series (again, see the *Opening Comments* of *Commentary No. 909*) the monthly and annual series had remained broadly consistent, although based on separate questions within the Consumer Population Series (CPS), as conducted by the Census Bureau.

Where Sentier used monthly questions surveying current annual household income, the headline annual Census Bureau detail is generated by a once-per-year question in the March CPS survey, as to the prior year's annual household income. The Median Household Income surveying results are broadly consistent with Real Average Weekly Earnings.

Graph CLW-5: Monthly Real Median Household Income (2000 to May 2017) Index, January 2000 = 100



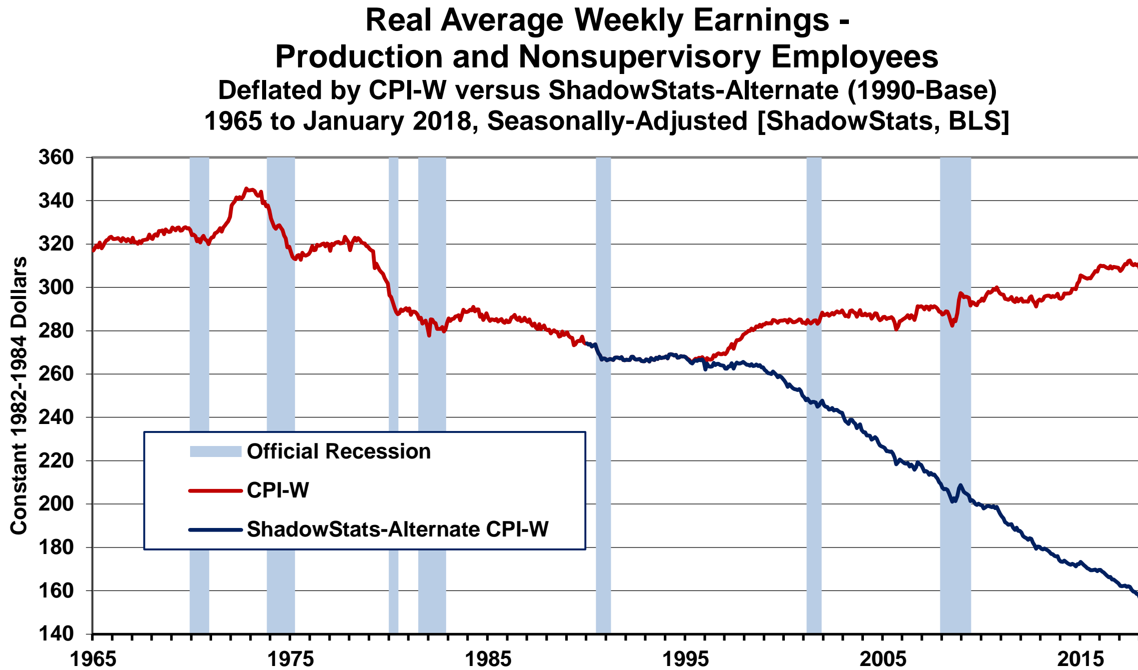
Graph CLW-6: Monthly Real Median Household Income (2000 to May 2017) Year-to-Year Change



Real Average Weekly Earnings—January 2018—Heading into a Third-Consecutive, Quarterly Contraction. For the production and nonsupervisory employees category—the only series for which there is a meaningful history (see the *Executive Comments* and *Graph 13 Commentary No. 934-B*), real average weekly earnings contracted monthly by 0.78% (-0.78%) in January 2018, setting up first-quarter 2018 as a likely, third-consecutive quarter of contraction in real earnings. Based on the January detail, the early trend for first-quarter 2018 is for an annualized contraction pace of 2.92% (-2.92%). That also

would be the fifth real quarterly contraction of the last six quarters. See the *Reporting Detail* for further information.

Graph CLW-7: Real Average Weekly Earnings, Production and Nonsupervisory Employees, 1965-to-Date

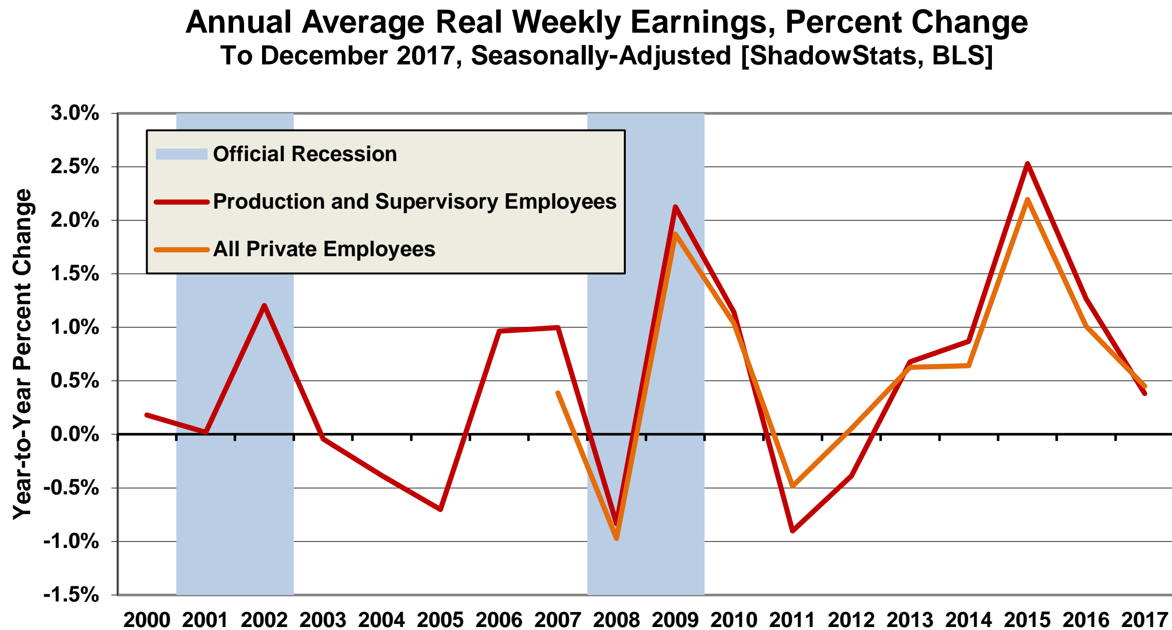


Graph CLW-7 plots the seasonally-adjusted earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially-weakened CPI-W (also used in calculating 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.

Shown in *Graph CLW-8*, and as discussed in *Commentary No. 931*, both the "all-employees" and "production and nonsupervisory employees" categories showed a sharply slowing pace in annual growth in 2017. Presumably coming off more-positive economic circumstances, the patterns there are consistent with a renewed economic downturn, not with a new economic boom, and the current pace of decline is greater than the average tax reduction to be seen by consumers in the year ahead.

Not all economic downturns are reflected in the headline economic data. For example, industrial production indicated the U.S. economic downturn intensified in fourth-quarter 2014, enough to qualify as a new recession, which is consistent with the plot in *Graph CLW-8*. See the related discussions in *Commentary No. 928* and *Commentary No. 936*.

Graph CLW-8: Annual Average of Weekly Earnings, Annual Percent Change (2000 to 2017)



When income growth is inadequate to support consumption growth, consumers often make up the difference in debt expansion. Yet, real Consumer Credit Outstanding has shown a patterns of declining annual real growth for the last several quarters, irrespective of the specific series, as reflected in the plots of real monthly year-to-year change in *Graph CLW-13*.

Consumer Credit: Lack of Expansion in Real Consumer Credit Constrains Economic Growth. The final five graphs on consumer conditions address consumer borrowing. Where debt expansion can help make up for a shortfall in income growth, expansion of consumer debt, which would help fuel expansion in personal consumption, has been nonexistent.

Quarterly Series. Consider *Graph CLW-9* of *Household Sector, Real Credit Market Debt Outstanding*. The level of real household debt declined in the period following the Panic of 2008, reflecting loan defaults and reduced banking lending, and it has not recovered fully, based on the Federal Reserve's flow-of-funds accounting through fourth-quarter 2017, released on March 8th. Household Sector, Real Credit Market Debt Outstanding in fourth-quarter 2017 still was down by 10.8% (-10.8%) from its pre-recession peak of third-quarter 2007. That was against a revised third-quarter 2017 decline of 11.0% (-11.0%) [previously 10.9% (-10.9%)]. The flattened visual uptick at the latest point in *Graph CLW-9* reflected a slowing in real year-to-year change from 1.72% [previously 1.70%] in second-quarter 2017, to 1.48% [previously 1.55%] in third-quarter 2017 and to 1.47% in fourth-quarter 2017. Such completes 41 straight quarters—a full decade-plus—of credit non-expansion, versus its pre-recession peak.

The series includes mortgages, automobile and student loans, credit cards, secured and unsecured loans, etc., all deflated by the headline quarterly CPI-U. The level of real debt outstanding has remained stagnant for several years, reflecting, among other issues, lack of normal lending by the banking system

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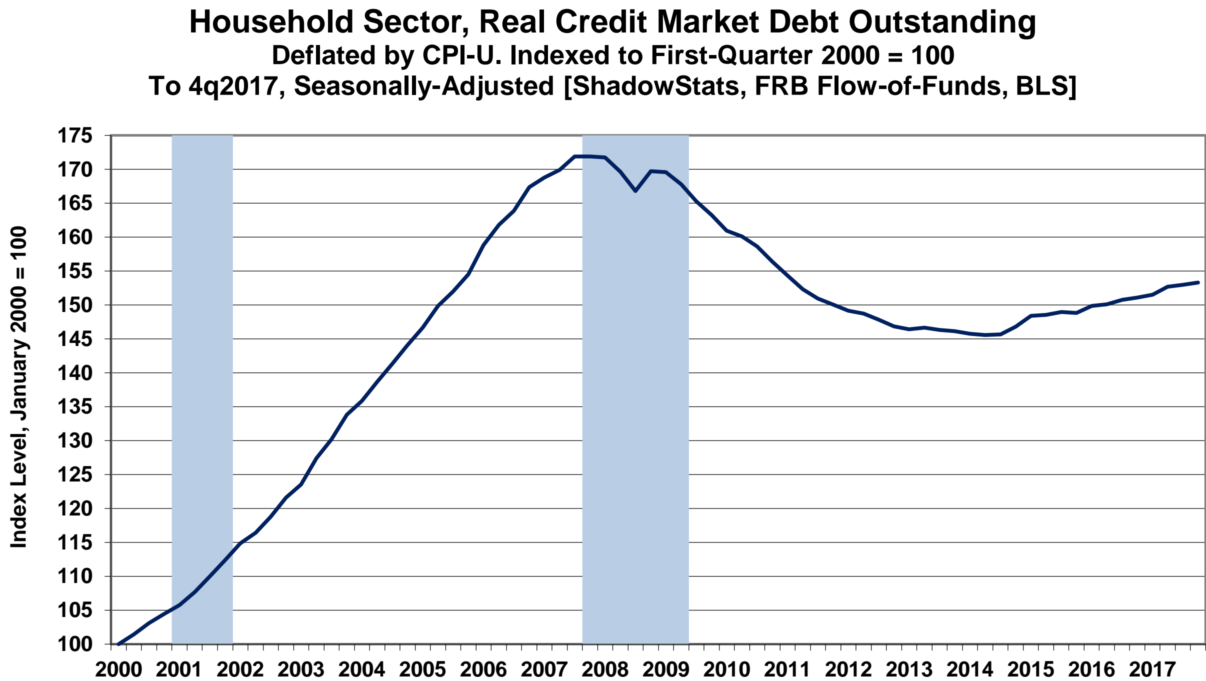
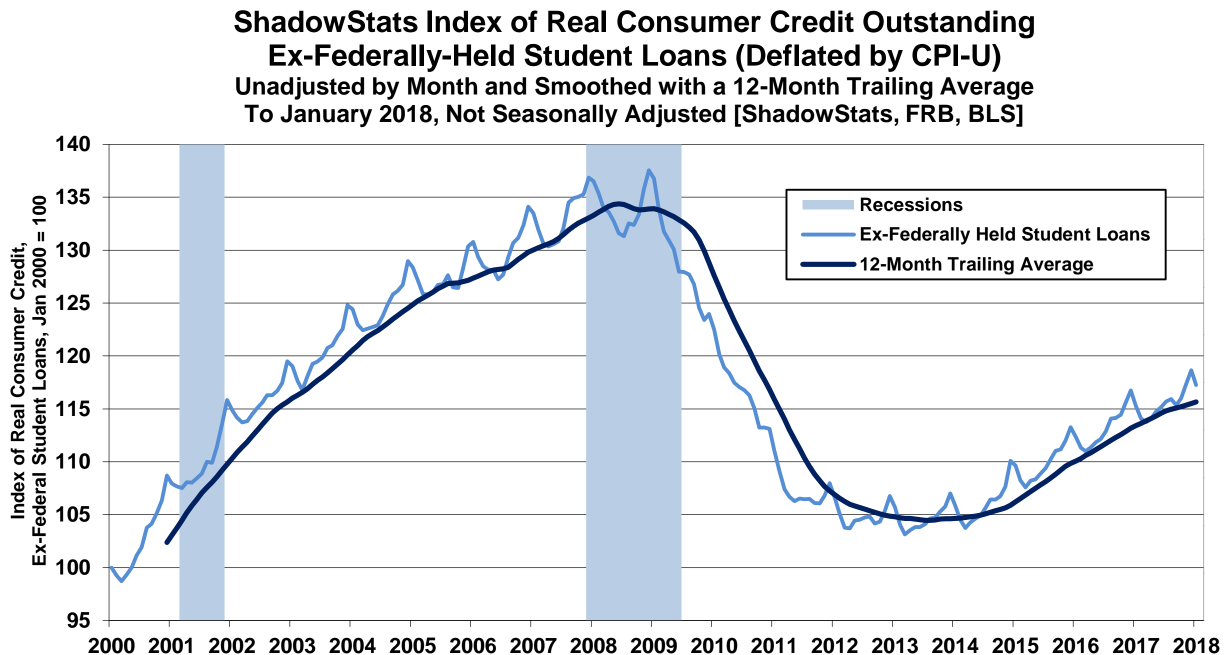
into the regular flow of commerce. The slight upturn seen in the series through 2015 and into 2016 was due primarily to gasoline-price-driven, negative CPI inflation, which continued to impact the system through second-quarter 2016 and intermittently into fourth-quarter 2017. Current activity also has reflected continuing relative strength from student loans, as shown in the *Graphs CLW-10* to *CLW-13*.

Graph CLW-9: Household Sector, Real Credit Market Debt Outstanding (2000 through Fourth-Quarter 2017)



Graph CLW-10: Real Consumer Credit Outstanding, Ex-Federal Student Loans (2000 to 2018)



Shown for comparative purposes is *Graph CLW-10*, real, not-seasonally-adjusted Consumer Credit Outstanding, Ex-Federally-Held Student Loans, has not recovered on a monthly, let alone the 12-month trailing-average basis used as a surrogate for seasonal adjustment. Discussed in the next section, this measure of consumer credit now has been through 121 months 40-plus quarters of non-expansion. That is reflected on a parallel basis through fourth-quarter 2017 reporting shown in *CLW-9*. Please note that the scale in *Graph 10* is indexed to Consumer Credit Outstanding Ex-Federal Student Loans equal to 100 in January 2000. In *Graphs 11* to *13*, that indexing is applied to the total Consumer Credit Outstanding number, which is greater in amount than its dominant Ex-Federal Student Loans subcomponent.

Monthly Series. Indeed, the ShadowStats analysis usually focuses on the particular current and continuing weakness in monthly levels of consumer credit, net of what has been rapidly expanding government-sponsored student loans. Where detail on that series only is available not-seasonally-adjusted, the following three related graphs and the preceding *Graph CLW-10* are so plotted.

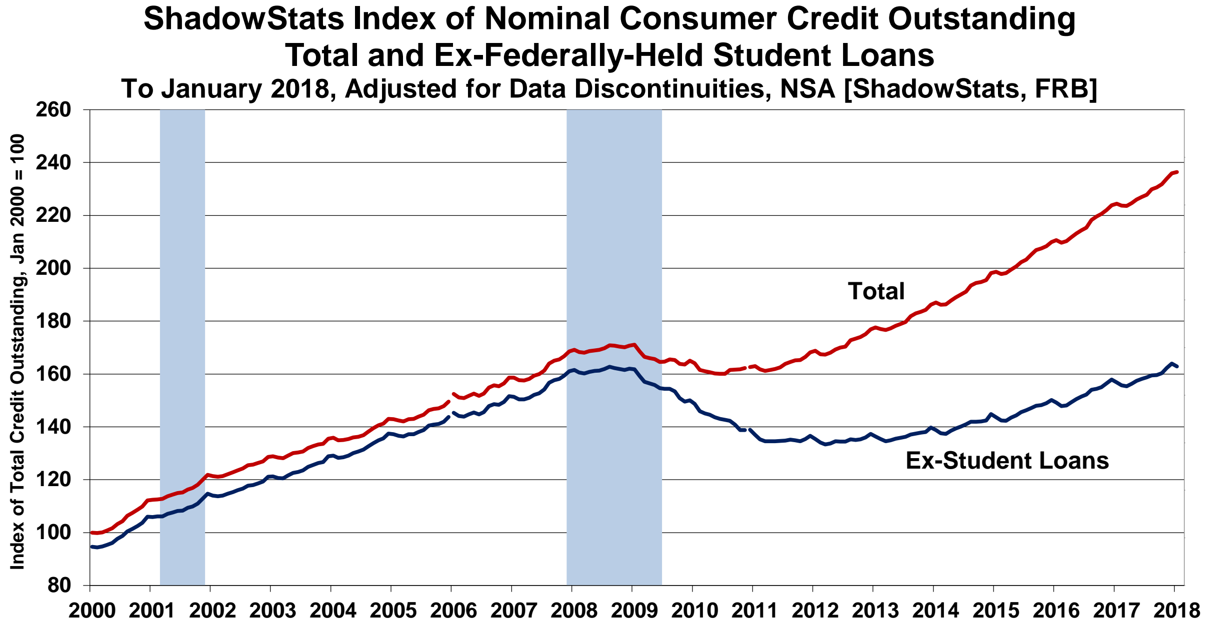
Shown through the January 2018 reading (released March 7th), the headline nominal monthly Consumer Credit Outstanding (*CLW-11*) is a subcomponent of the nominal Household Sector debt. Where *Graph CLW-12* reflects the real or inflation-adjusted activity for monthly Consumer Credit Outstanding terms of both level (*Graph CLW-12*) and year-to-year change (*Graph CLW-13*). *Graphs CLW-12* and *CLW-10* are comparable to the inflation-adjusted Household Sector plot in *Graph CLW-9*.

Post-2008 Panic, growth in outstanding consumer credit has continued to be dominated by growth in federally-held student loans, not in bank loans to consumers that otherwise would have fueled broad consumption or housing growth. Although in slow uptrend, the nominal level of Consumer Credit Outstanding (ex-student loans) has not recovered since the onset of the recession. These disaggregated data are available and plotted only on a not-seasonally-adjusted basis, with the pattern of monthly levels during one year reflecting some regular, unadjusted seasonal dips or jumps.

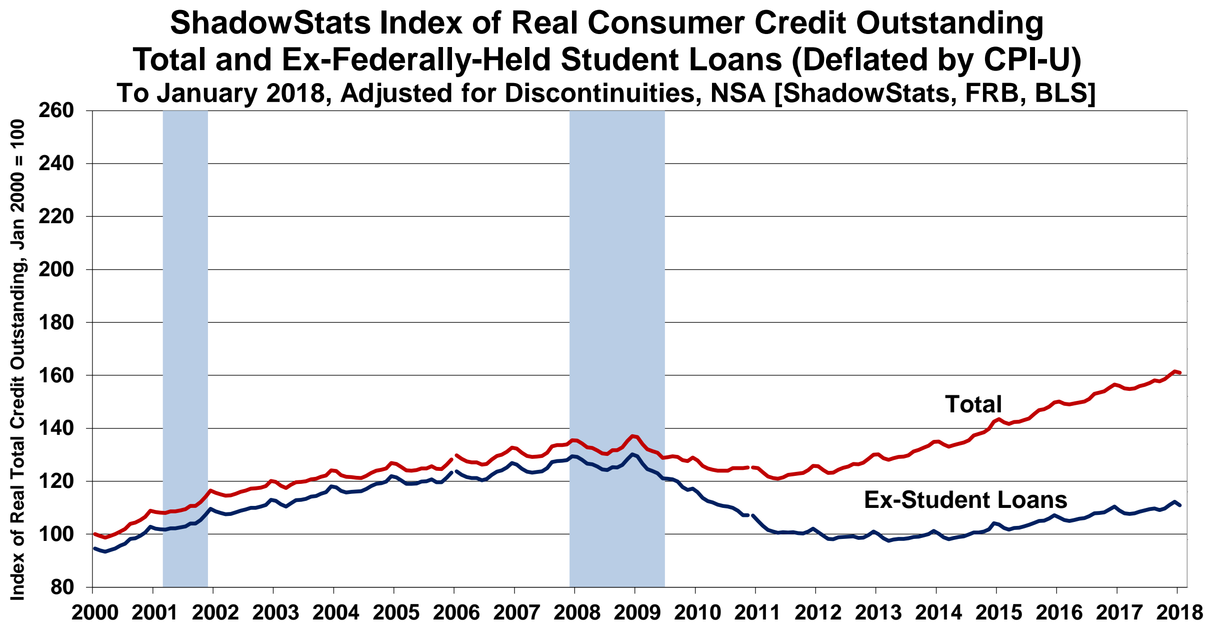
Adjusted for inflation, the lack of recovery in the ex-student loan area is more obvious. Where the recent monthly downside move in the not-seasonally-adjusted real consumer credit reflected a seasonal pattern, the pattern of year-to-year growth has been in downtrend, suggesting some tightening of credit conditions. Adjusted for discontinuities and inflation, ex-student loans, consumer credit outstanding in January 2018 was down from recovering its December 2007 pre-recession peak by 14.3% (-14.3%). That is 121 months or a full, ten-plus years of non-expansion of credit. Year-to-year real growth shown in *Graph CLW-13* tends to resolve most of the monthly distortions in the not-seasonally-adjusted data.

[Graphs CLW-11 to CLW-13 begin on the next page.]

Graph CLW-11: Nominal Consumer Credit Outstanding (2000 to 2018)



Graph CLW-12: Real Consumer Credit Outstanding (2000 to 2018)



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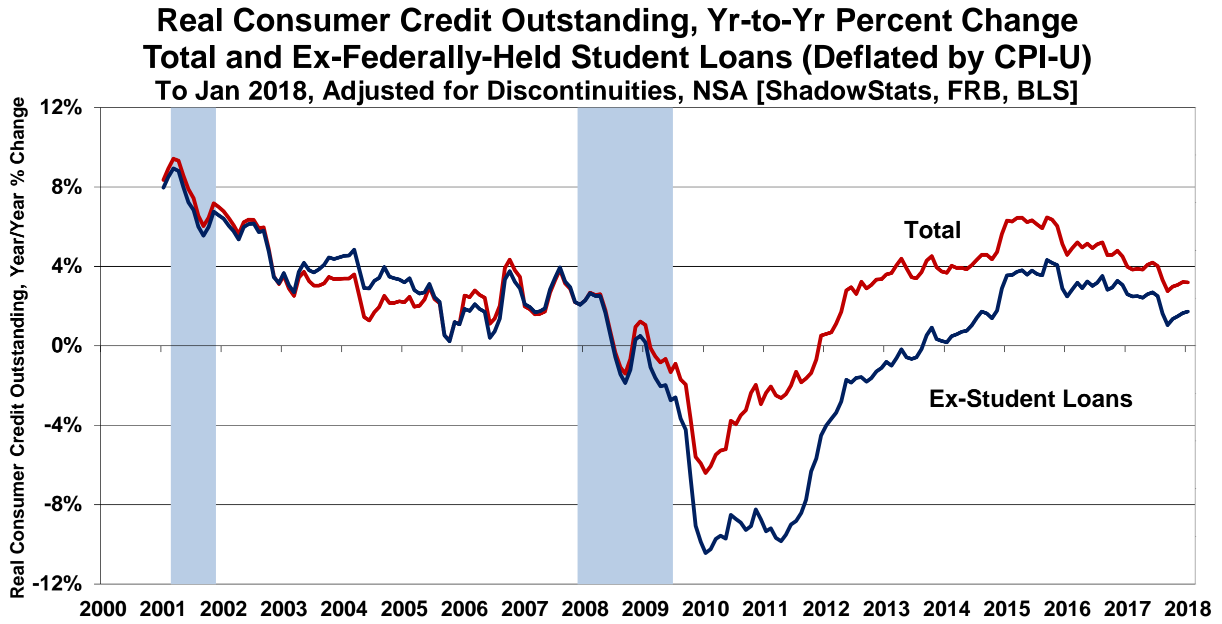
Graph CLW-13: Year-to-Year Percent Change, Real Consumer Credit Outstanding (2000 to 2018)



[The **Week, Month and Year Ahead** *begins on the next page.]*

WEEK, MONTH AND YEAR AHEAD

Instabilities and Turmoil in the U.S. Dollar and Financial-Markets Continue at High Risk, in the Context of a Faltering and Non-Expanding Real-World Broad Economy. Updated outlooks for the U.S. economy, the U.S. dollar, gold, silver and the financial markets were reviewed in *Special Commentary No. 935*, covered there in the opening *Executive Summary* beginning on page 2 of that report, with *Contents* and links to *Major Sections* and *Graphs* beginning on page 6. Renewed economic faltering was discussed in *Commentary No. 936*, *Commentary No. 937*, *Commentary No. 938* and in today's *Opening Comments* and *Reporting Detail*, in the context of an unusually-unstable employment and unemployment data from a headline-positive February labor report.

Conditions Take a Turn for the Worse. Natural-disaster-impact from late 2017 continued to unwind in most headline monthly economic reporting in January, a pattern that should intensify in the next couple of months. These elements suggested not only some downside revision for the second estimate of Fourth-Quarter 2017 GDP (seen some components), but also meaningful risk for an outright quarterly contraction in the initial estimate of First-Quarter 2018 GDP on April 27th, particularly with the deteriorating trade deficit discussed in *Commentary No. 937*. Increasingly, headline economic details are likely to disappoint consensus expectations (again, see today's *Opening Comments* and *Hyperinflation Watch*).

The real-world economy is not recovering or booming as advertised, despite heavy hype in the press of a booming, full-employment economy, and in the context recent FOMC tightening actions.

If not already there, reporting in most series should be back to normal (allowing for hurricane disruptions and recovery) by the headline reporting of February 2018 economic activity, as discussed in *General Commentary No. 929*. That reporting starts next week. Most series increasingly should reflect "unexpected" downtrending economic activity. Where misleading, recent headline details have contributed to a manic stock market, the mania like it could be starting to unwind. The process should accelerate as market perceptions increasing shift towards renewed economic downturn.

An unhappy period of market readjustment to underlying real-world circumstances looms, where Wall Street's proponents of a never-ending stock-market rally have parlayed temporary, nonrecurring economic boosts from natural disasters into a year-end 2017 economic boom. Negative economic "surprises" increasingly should shock the markets and the U.S. dollar on the downside, as was seen in last week's activity. As the reported economic downturn intensifies in the months ahead, the FOMC—under its new Chairman Jerome H. Powell—eventually should face an "unexpected" policy retrenchment, moving back towards quantitative easing.

In these circumstances, the U.S. dollar and financial markets remain at extraordinarily-high risk of intensified panicked declines, likely in the very near term (see the *Opening Comments* and *Hyperinflation*

Watch, with more to follow in *Commentary No. 940* of March 14th. Holding physical gold and silver remain the ultimate hedges—stores of wealth—for preserving the purchasing power of one's U.S. dollar assets, during times of high inflation and currency debasement, and/or political- and financial-system upheaval, Please call (707) 763-5786, if you would like to discuss current circumstances, or otherwise.

Best wishes – John Williams

PENDING ECONOMIC RELEASES: Consumer Price Index—CPI (February 2018). The Bureau of Labor Statistics (BLS) will release its February 2018 CPI on Tuesday, March 13th, which will be covered in *Commentary No. 940* of March 14th. The headline February CPI-U likely will be on the plus side, perhaps up by 0.2% in the month, plus-or-minus, in the context of a monthly gain in unadjusted gasoline prices, more than offset by negative seasonal adjustments. Unadjusted year-to-year annual inflation for February 2018 should firm to 2.2% or 2.3%, from the 2.1% level seen in January 2018.

Negative Monthly Inflation Impact from Higher Gasoline Prices and Negative Seasonal Adjustments. Unadjusted gasoline prices jumped month-to-month by a hurricane-induced 10.6% in September 2017, retreating by 5.4% (-5.4%) in October, rebounding by 2.6% in November, dropping by 3.3% (-3.3%) in December 2017, rising by 3.2% in January 2018 and by a further 1.3% (1.27% is the Department of Energy estimate) for February 2018. Nonetheless, February marks the onset of a four-month shift to negative seasonal adjustments to gasoline prices, with the likely impact of transmuting the unadjusted monthly gasoline gain of 1.3% into a monthly contraction of about 1.1% (-1.1%). That translates into a negative gas-price contribution of about 0.04% (-0.04%) to the headline, seasonally-adjusted monthly CPI-U inflation. Likely boosted, though, by higher food and "core" (net of food and energy) inflation, the headline monthly CPI-U reading could come in around 0.2% for February 2018.

Annual Inflation Rate. Noted in *Commentary No. 936*, year-to-year CPI-U inflation can be estimated for February 2018 reporting, dependent on the seasonally-adjusted month-to-month change, versus the adjusted, headline gain of 0.03% (unchanged at the first decimal point) in the February 2017 CPI-U. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for February 2018, the difference in February's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the unadjusted January 2018 annual inflation rate of 2.07%. Given an early guess of a 0.2% seasonally-adjusted monthly gain in February 2018 CPI-U, that would leave the annual CPI-U inflation rate for February 2018 at about 2.2% to 2.3%.

Retail Sales—Nominal and Real (February 2018). The Census Bureau will release its "advance" estimate of February 2018 nominal (not-adjusted-for-inflation) Retail Sales on Wednesday, March 14th. Given the release of the February CPI-U on March 13th, both nominal and real (adjusted for inflation) Retail Sales will be discussed in *Commentary No. 940* of that date. In the context of much weaker-than expected (contracting) January 2018 Retail Sales and downside revisions to activity in November and December 2017, the unwinding of the natural-disaster-recovery boosts should continue along with consumers pulling back fin response to tightening liquidity conditions.

While consensus expectations likely will favor a small monthly gain, expectations likely will not be met, in the context of aggregate activity, net of revisions. Net of inflation, real retail sales likely will have contracted for the third straight month.

Again, beyond lingering distortions from insurance payments and savings liquidation covering hurricane losses, consumer "liquidity" remains impaired. Per the *Consumer Liquidity Watch* section, without sustainable growth in real income, and without the ability and/or willingness to take on meaningful new debt to make up for an income shortfall, the liquidity-strapped U.S. consumer remains unable to sustain regular, broad growth in economic activity, including Retail Sales, real or otherwise.

Producer Price Index—PPI (February 2018) The Bureau of Labor Statistics (BLS) will release the February 2018 PPI on Wednesday, February 14th, with detail covered in *Commentary No. 940* of that date. Odds favor negative, wholesale inflation on the goods side of the reporting, reflecting a combination of falling wholesale gasoline and crude oil prices in February, exacerbated by negative seasonal adjustments in energy-sector inflation.

The dominant services-sector "inflation," however, often provides some counter-move to the hard-inflation estimate on the goods side, where services likely would be a positive contributor in the current circumstance. Such comes particularly from counterintuitive "inflation" or "deflation," reflecting rising or falling "margins," in turn reflecting falling or rising costs. Guesstimation in that services sector remains highly problematic, as discussed in *Inflation that Is More Theoretical than Real World?* in *Commentary No. 936*, where, again, the services component could offset some of the negative pressures in the headline goods inflation.

Per the Department of Energy (DOE), unadjusted crude oil prices and wholesale gasoline prices declined in February 2018. Based on the two most-widely-followed oil contracts, monthly-average oil prices fell by 5.4% (-5.4%) [Brent] and by 2.3% (-2.3%) [WTI]. That was accompanied by declines in unadjusted, monthly-average wholesale gasoline prices of 2.1% (-2.1%) [NY Harbor] and by 4.9% (-4.9%) [Gulf Coast]. Where PPI seasonal adjustments for energy costs turn negative in February, petroleum-related unadjusted monthly price changes should have strongly-negative impact on the month-to-month adjusted Final Demand Goods component of the PPI.

Industrial Production (February 2018). The Federal Reserve Board will publish its estimate of February 2018 Industrial Production on Friday, March 16th, with coverage in *Commentary No. 941* of that date. Discussed in *Commentary No. 936*, net of surging utility usage, induced by extreme winter-weather conditions, production appeared to have peaked in November 2017, following heavy, recovery distortions from hurricane disruptions to petroleum production and by factors such as production of replacement automobiles for storm-destroyed vehicles. Those distortions have begun to unwind in a process that likely accelerated in February 2018, with production having a good shot of a monthly pullback, net of revisions. That is despite recent oil-production-boosted mining strength, along with continuing non-recovery and non-expansion in the dominant manufacturing sector and net of extreme, continued irregular volatility in winter-related utility consumption.

New Residential Construction—Building Permits and Housing Starts (February 2018). The Census Bureau and the Department of Housing and Urban Development will release the February 2018 estimate of New Residential Construction, including Housing Starts and Building Permits on Friday, March 16th, with detail covered in *Commentary No. 941* of that date. While this series remains wildly unstable and statistically-insignificant in its monthly reporting, given the extreme monthly gains and revisions in January 2018 reporting, consensus expectations likely will be for headline decline in February.

Accordingly, in line with the common-reporting experience of extreme volatility and unstable revisions, February's monthly results also likely will be unstable, heavily revised and not statistically meaningful, holding in a general pattern of stagnation. That said, given those frequent extreme monthly gyrations, almost anything is possible in this unstable series, in a given month. Such is despite the likely negative consensus outlook for headline February reporting.

Irrespective of the usual lack of headline-reporting significance, the broad pattern of Housing Starts should remain consistent with the low-level, stagnant-to-downtrending activity seen in the last year. Both Housing Starts and Building Permits showed patterns of continuing non-recovery in the context of respective January 2018 activity being down by 41.7% (-41.7%) and by 38.3% (-38.3%) from recovering pre-recession highs (see *Commentary No. 936*). Such low-level stagnation is evident particularly with headline detail viewed in the context of a six-month moving average. Again, these series remains subject to regular and extremely large, prior-period revisions.

The liquidity bind besetting consumers continues to constrain residential real estate activity, as updated in today's *Consumer Liquidity Watch* section. 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 income shortfall, the U.S. consumer remains unable to sustain positive growth in domestic personal consumption, including residential real estate activity and related demand for residential construction. That circumstance—in the last eleven-plus years of economic collapse and stagnation—has continued to prevent a normal recovery in broad U.S. economic activity.

Note on Reporting-Quality Issues and Systemic-Reporting Biases. In the context of historical background provided in *Special Commentary No. 885*: *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*, significant reporting-quality problems remain with most major economic series. Beyond pre-announced gimmicked changes to reporting methodologies of the last several decades, which have tended both to understate inflation and to overstate economic activity meaningfully—as generally viewed in the common experience of Main Street, U.S.A.—ongoing, near-term headline reporting issues often reflect 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 have provided particularly unstable headline economic results, with the use of concurrent seasonal adjustments (as seen with retail sales, durable goods orders, employment and unemployment data). While historical seasonal-factor adjustments are revised every month, based on the latest, headline monthly data, the consistent, revamped historical data are not released or reported at the same time. That issue is discussed and explored in the labor-numbers related *Supplemental Commentary No. 784-A* and *Commentary No. 695*.

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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 several years 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*). Investigative-financial/business reporter John Crudele of the *New York Post* has written extensively on such reporting irregularities: *Crudele Investigation*, *Crudele on Census Bureau Fraud* and *John Crudele on Retail Sales*.

LINKS TO PRIOR COMMENTARIES AND SPECIAL REPORTS

Prior Writings Underlying the Current *Special Commentaries* and a Sampling of Recent *Regular Commentaries*. Underlying the recent *Special Commentary No. 935* *(Part One)* and the pending *Special Commentaries(Part Two)* on Inflation, and *(Part III)* on the Federal Reserve and U.S. banking system, are *Commentary No. 899* and *General Commentary No. 894*, along with general background from regular *Commentaries* throughout 2017.

These missive also are built upon writings of prior years, including *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). In turn, they 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. *[Listed here are* Commentaries *of the last several months or so, plus recent* Special Commentaries *and others covering a variety of non-monthly issues, including annual benchmark revisions, dating back through the beginning of 2017. Please Note: Complete ShadowStats archives back to 2004 are found at* www.ShadowStats.com *(left-hand column of home page).]* These regular weekly *Commentaries* are published at least weekly and update the general outlook, as circumstances develop.

Commentary No. 938 (March 1st) reviewed January 2018 Construction Spending and the second estimate of Fourth-Quarter 2017 GDP.

Commentary No. 937 (February 27th) covered January 2018, New Orders for Durable, New- and Existing-Home Sales, the "advance" estimate of the January 2018 Merchandise Trade Deficit and the Cass Freight Index™.

Commentary No. 936 (February 19th) covered the January 2018 CPI and PPI, Retail Sales, Industrial Production and New Residential Construction (Housing Starts and Building Permits).

Special Commentary No. 935 (February 12th) was the first part of a three part-series reviewing economic and financial conditions of 2017 and the year-ahead, inflation and the U.S. government's balance sheet and conditions in the U.S. banking system and Federal Reserve options.

Commentary No. 934-B (February 6, 2018) provided extended coverage on the January 2018 Employment and Unemployment details, the 2017 benchmark revisions to Payroll Employment and the January annual recasting of population, along with coverage of the December 2017 Trade Deficit.

Commentary No. 934-A (February 2, 2018) provided initial detail on the January 2018 Employment and Unemployment details and the 2017 benchmark revisions to Payroll Employment, along with coverage of January Conference Board Help Wanted OnLine® Advertising, January Monetary Conditions and December 2017 Construction Spending.

Commentary No. 933 (January 26, 2018) covered December New Orders for Durable Goods, the Cass Freight Index™ and the first estimate of Fourth-Quarter 2017 GDP.

Commentary No. 932 (January 18, 2018) covered December Industrial Production and New Residential Construction (Housing Starts and Building Permits).

Commentary No. 931 (January 15, 2018) reviewed December 2017 Retail Sales and the CPI and PPI, along with an update on the U.S. dollar, the financial markets and gold graphs.

Commentary No. 930-B (January 8th) expanded upon the December 2017 Employment and Unemployment numbers and Household Survey benchmarking, Conference Board Help Wanted OnLine® Advertising, December Monetary Conditions and the November 2017 Trade Deficit and Construction Spending, otherwise headlined in *No. 930-A*.

Advance Commentary No. 930-A (January 5, 2018) provided a brief summary and/or comments (all expanded in *Commentary No. 930-B*) on December 2017 Employment and Unemployment numbers, Household Survey benchmarking, Conference Board Help Wanted OnLine® Advertising, December Monetary Conditions and the November 2017 Trade Deficit and Construction Spending.

General Commentary No. 929 (December 28, 2017) reviewed current economic and market conditions at year-end 2017.

Commentary No. 928 (December 22, 2017) covered November 2017 New Orders for Durable Goods, New- and Existing-Home Sales and the third estimate of Third-Quarter 2017 GDP.

Commentary No. 927 (December 19, 2017) reviewed November 2017 New Residential Construction (Housing Starts and Building Permits) and Cass Freight Index™, along with an expanded discussion on underlying economic reality and the financial markets.

Commentary No. 926 (December 15, 2017) reviewed the headline November 2017 numbers for Retail Sales (both real and nominal), and Industrial Production, along a discussion on the dampening economic impact of business and consumer "uncertainty."

Commentary No. 925 (December 13th) reviewed November 2017 headline detail on the CPI and PPI, along with an update on the FOMC actions and the regular U.S. dollar, gold graphs.

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Commentary No. 924 (December 8, 2017) discussed the November 2017 Employment and Unemployment details and Conference Board Help Wanted OnLine® Advertising, the October Trade Deficit and Construction Spending and updated Monetary Conditions in November.

Commentary No. 923 (November 29, 2017) covered the second estimate of Third-Quarter 2017 GDP, including initial estimates for Third-Quarter GNP, GDI and Per Capita Real Disposable Income, the October Trade Deficit, Cass Freight Index and New-Home Sales.

Commentary No. 919-B (November 6, 2017) provided more in-depth detail on the October 2017 labor detail.

Commentary No. 919-A (November 3, 2017) provided initial detail and background on October labor data, and reviewed the October 2017 Conference Board Help Wanted OnLine® Advertising, the September Cass Freight Index™, Trade Deficit and Construction Spending, and updated Monetary Conditions.

Special Commentary No. 918-B (October 30, 2017) provided a more comprehensive review of the initial third-quarter 2017 GDP detail, along with update versions of the *Hyperinflation Watch* and *Consumer Liquidity Watch*.

Commentary No. 917 (October 26/27, 2017) reviewed September Industrial Production, New Orders for Durable Goods, New Residential Construction (Housing Starts and Building Permits) and New- and Existing-Home Sales.

Commentary No. 916 (October 20th) reviewed the September 2017 Retail Sales details along with the headline Consumer and Producer Price Indices for September.

Commentary No. 915 (October 6, 3017) reviewed the September 2017 Employment and Unemployment details, along with September 2017 monetary conditions.

Commentary No. 913 (September 28, 2017) reviewed the third-estimate of second-quarter 2017 GDP, with a further consideration of some unusual economic reporting in the near future.

Commentary No. 910 (September 15, 2017) reviewed the August 2017 releases of Industrial Production and nominal and real Retail Sales.

Commentary No. 909 (September 14, 2017) assessed the annual release of 2016 Real Median Household Income, along with a review of August Consumer Price Index (CPI) and the Producer Price Index (PPI) and an updated *Alert* on the financial markets

Commentary No. 908-B (September 6, 2017) provided extended detail of the August 2017 Labor and Monetary conditions and July 2017 Construction Spending, along with coverage of the July 2017 Trade Deficit and the initial estimate of the 2017 Payroll Employment benchmarking.

Special Commentary No. 904 (August 14, 2017) issued an "Alert" on the financial markets (including U.S. equities, the U.S. dollar gold and silver, as well as FOMC policy), in the context of historical activity and unfolding circumstances of deteriorating economic and political conditions. Separately, headline details were reviewed for the July Consumer Price Index (CPI) and the Producer Price Index (PPI).

Commentary No. 903 (August 7, 2017) discussed new signals of economic deterioration in terms of political and FOMC considerations, along with headline coverage of the July labor data, M3 and The Conference Board Help Wanted OnLine®, and June trade deficit and construction spending.

Commentary No. 902-B (July 31, 2017) reviewed the 2017 annual benchmark revisions of GDP and related series, along with the "advance" estimate of second-quarter 2017 GDP.

Commentary No. 900 (July 19, 2017) reviewed June 2017 New Residential Investment (Housing Starts and Building Permits), and previewed the upcoming annual GDP benchmark revisions and the coincident "advance" estimate of second-quarter 2017 GDP.

Commentary No. 897 (July 6, 2017) reviewed the headline May 2017 Construction Spending and the annual revisions to same, along the May Trade Deficit, and June The Conference Board Help Wanted OnLine® Advertising and the May Cass Freight Index™.

General Commentary No. 894 (June 23, 2017) reviewed unfolding economic, financial and political circumstances in the context of market expectations shifting towards an "unexpected" headline downturn in broad economic activity, along with headline details on May 2017 Real Median Household Income (Sentier Research) and New- and Existing-Home Sales.

Commentary No. 890 (June 5, 2017) covered the negative-downside annual benchmark revisions to the trade deficit, the May 2017 estimates of labor conditions, ShadowStats Ongoing Money Supply M3, The Conference Board Help Wanted OnLine® Advertising and April 2017 estimates of the Cass Freight Index™, and the monthly trade deficit and construction spending.

Special Commentary No. 888 (May 22, 2017) discussed evolving political circumstances that could impact the markets and the economy, reviewed the annual benchmark revisions to Manufacturers' Shipments and New Orders for Durable Goods and updated Consumer Liquidity Conditions.

Commentary No. 887 (May 18, 2017) reported on the April 2017 detail for Industrial Production and Residential Construction (Housing Starts), with some particular attention to historic, protracted periods of economic non-expansion, of which the current non-recovery is the most severe.

Special Commentary No. 885, entitled *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*, (May 8, 2017) reviewed the unusual nature of the headline reporting of the April 2017 employment and unemployment details.

Commentary No. 882 (April 27, 2017) summarized the annual benchmark revisions to Retail Sales and reviewed the March 2017 releases of New Orders for Durable Goods and New- and Existing-Home Sales.

Commentary No. 877 (April 2, 2017) outlined the nature of the downside annual benchmark revisions to industrial production, along with implications for pending annual revisions to Retail Sales, Durable Goods Orders and the GDP.

Commentary No. 876 (March 30, 2017) current headline economic activity in the context of formal definitions of the business cycle (no other major series come close to the booming GDP, which is covered in its third revision to fourth-quarter activity). Also the February 2017 SentierResearch reading on real median household income was highlighted.

Commentary No. 875 (March 24, 2017) assessed and clarified formal definitions of the U.S. business cycle, which were expanded upon significantly, subsequently, in *No. 876*. It also provided the standard review of the headline February 2017 New Orders for Durable Goods, New- and Existing-Home Sales and the Cass Freight Index™.

General Commentary No. 867 (February 24, 2017) assessed mixed signals for a second bottoming of the economic collapse into 2009, which otherwise never recovered its level of pre-recession activity. Such was 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 the prior January 2017 New- and Existing Home Sales.

Commentary No. 864 (February 8, 2017) analyzed 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 (January 13, 2017) 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.

No. 859 Special Commentary (January 8, 2017) reviewed and previewed economic, financial and systemic developments of the year passed and the post-election year ahead.

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