

COMMENTARY NUMBER 953-A

May 2018 Monetary Conditions, Labor Numbers, April Construction Spending

June 1, 2018

Federal Reserve Has Pushed Real Annual Money Supply Growth Down to Levels That Threaten an Intensifying, “New” Economic Contraction

Annual Growth Weakened Sharply for All Money Supply Measures in May 2018, Along with Continued Monthly and Annual Contractions in the Monetary Base

May Labor-Market Stress Remained Consistent with Headline Unemployment Much Closer to a Record High Than a Record Low

Headline May U.3 Unemployment Declined to 3.8%, Lowest Level Since October 2000, at the First Decimal Point

May U.3 (Second Decimal Point) Hit a Post-1994 (Modern-Series) Record Low of 3.75%, Down from 3.93% in April, Otherwise at the Lowest Level Since December 1969

May U.6 Unemployment Declined to 7.59%, from 7.79%, the Lowest Since October 2000

The May ShadowStats-Alternate Eased to 21.4%, from 21.5%, Lowest Since September 2009, Declining on Top of U.6 but Still Tempered by Long-Term Discouraged and Displaced Workers

May Payroll Jobs Gained 223,000 (up by 238,000 Net of Revisions), but with Annual Growth of 1.61% Still in Recession-Signal Territory

Real Construction Spending Held Shy of Its Pre-Recession Peak by 19.5% (-19.5%), Despite Surging Headline Activity in April 2018, and in the Context of Unstable Reporting and Pending Benchmark Revisions

PLEASE NOTE: The next missive (Commentary No. 953-B), scheduled for Monday, June 4th, will provide an extended review of the May 2018 Employment and Unemployment detail and April 2018 Construction Spending numbers, expanding upon today's headline and summary "Flash" coverage. The ShadowStats Money Supply and Alternate Unemployment details for May have been posted on the Alternate Data Tab.

Best wishes to all — John Williams (707) 763-5786

FLASH Coverage (June 1st): *Opening Comments and Executive Summary* provides preliminary highlights and summary detail of this morning's releases of May 2018 Employment and Unemployment and April Construction Spending. Such allows for early-day release of this *Commentary*, with a full update following in regular *Commentary No. 953-B* on Monday, June 4th. The usual ***Consumer Liquidity Watch*** and ***Week, Month and Year Ahead*** sections also will follow in *No. 953-B* (most recent are versions available in prior [Commentary No. 952](#)).

Employment and Unemployment coverage begins on page 2.

Construction Spending coverage begins on page 7.

Hyperinflation Watch reviews current monetary conditions along with the May 2018 estimate of annual growth in the ShadowStats Ongoing Estimate of Money Supply, beginning on page 9.

FLASH COVERAGE—OPENING COMMENTS AND EXECUTIVE SUMMARY

Headline Economic Reporting Generally Does Not Get Much Better Than This; Underlying Reality and Prospects Tell a Different Story. Today's (June 1st) headline economic news could not have been much better. The U.3 unemployment rate dropped to an 18-year (or a 49-year) low in May 2018, depending on the historical base used for comparison. That was accompanied by a solid gain in payroll employment, on top of an upside revision to April's payrolls. Separately, April construction spending jumped in the month, showing its strongest annual real growth since January 2017. One could argue that an intensifying economic boom is in play.

Underlying reality, though, is not so rosy. Discussed briefly here, to be covered in more-extensive detail in the supplemental, Monday (June 4th) *Commentary No. 953-B*, employment conditions remain highly stressed, more common for an economy in non-recovered recession, than with one that purportedly is booming in ongoing expansion. Much of that has to do with how the government counts its unemployed and defines its various unemployment and economic measures.

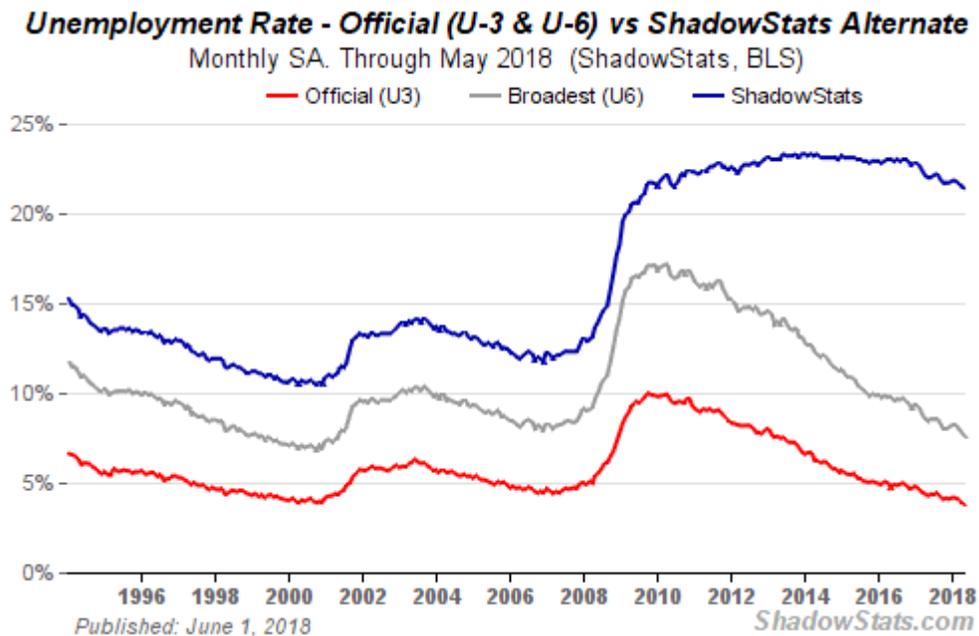
As to the regularly-volatile Construction Spending series, indeed it is noted for its usually-massive, frequent monthly revisions. The unstable monthly details will undergo their annual benchmarking next

month, coincident the release of the headline May 2018 detail on July 2nd. Although showing mixed-monthly changes, but generally-uptrending, smoothed activity (see [Commentary No. 950](#) and [Commentary No. 951](#)), most construction-related series remain deep in non-economic-expansion territory, never having recovered pre-recession peaks. Real Construction Spending, for example remains shy by 19.5% (-19.5%) of regaining its March 2006 pre-recession high.

Discussed in prior [Commentary No. 952](#), the U.S. consumer remains in a tightening liquidity bind, amidst faltering optimism as to future conditions. Along with the faltering private surveys on the consumer outlook, the Conference Board Help-Wanted Online Advertising® (HWOL) for May 2018 showed a sharp pullback in monthly and annual activity, none of which is consistent with underlying, booming employment conditions.

These not-so-happy consumer liquidity conditions largely remain an artefact of Federal Reserve policies that evolved rapidly during in the Panic of 2008, aimed at saving the banking system at all costs. Acceptable costs included a lack of meaningful economic expansion. Discussed in today's full *Hyperinflation Watch*, those policies remain in play, and U.S. consumer liquidity and prosperity remain of only secondary consideration in ongoing Fed policy, against the survival of the still-troubled domestic and global banking systems.

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



Employment and Unemployment—May 2018—Record-Low Unemployment Accompanied by a Solid Gain in Payrolls. Per the Bureau of Labor Statistics (BLS), the seasonally-adjusted Household Survey numbers showed the May 2018 headline unemployment rate (U.3) dropping to a new cycle low and a new 19-year low of 3.8% (3.75% at the second decimal point) [down from 3.93% in April], a rate last seen in October 2000 at the first decimal point. At the second decimal point, that was the lowest level ever seen in the modern series (redefined in 1994). Against earlier reporting, that was at the lowest level since December 1969, when Richard Nixon was President.

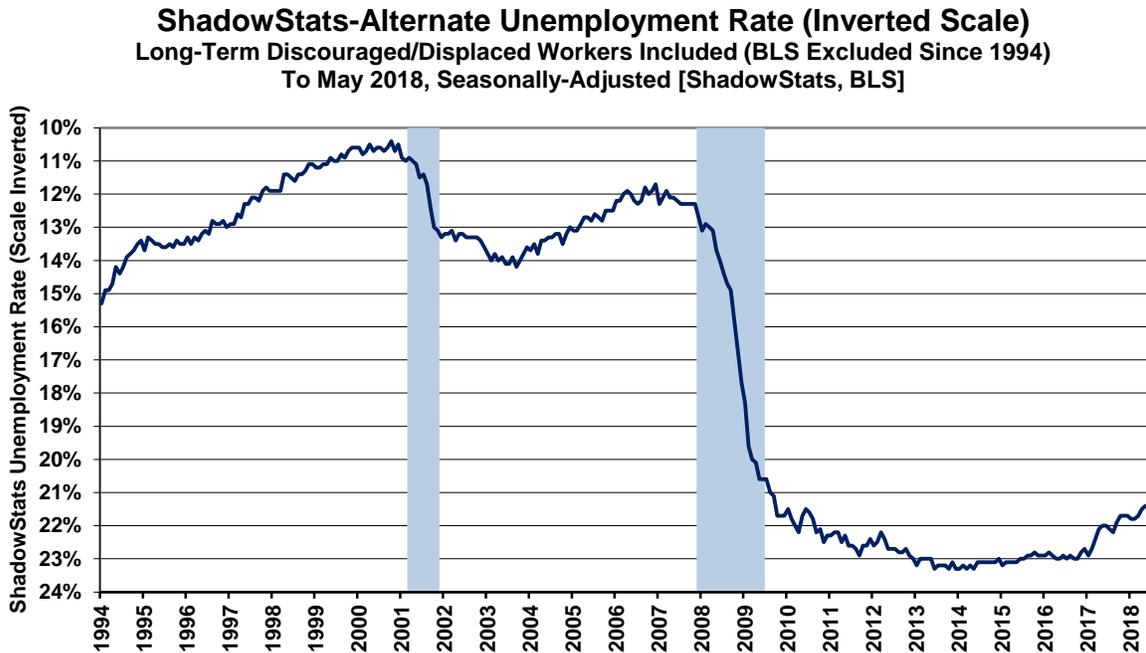
Built upon the U.3 rate, including those marginally attached to the labor force, and those working part-time for economic reasons (unable to find full-time employment), the seasonally-adjusted, broader U.6 unemployment rate declined to 7.59% in May 2018, from 7.79% in April, its lowest reading since October 2000.

Built upon the U.6 rate (and U.3), and accounting for estimates of long-term “discouraged” and displaced workers no longer tallied in government surveying, the still-broader ShadowStats-Alternate unemployment rate declined to 21.4% in May 2018, from 21.5% in April, lowest since September 2009, at the purported depths of the Great Recession. These rates are reflected in accompanying *Graph 1*.

While the current headline unemployment likely qualifies as “full employment,” such remains unconfirmed by historically-low Employment-to-Population and Labor-Force-to-Employment (Participation) Ratios, which were little changed in May, at levels more consistent with a headline unemployment rate of about 10% instead of 3.8%. The difference is the unusually large number of discouraged and displaced workers in this cycle, not counted in the headline U.3, as well as a goodly number not included in U.6 (see definitions and detail in [Commentary No. 948](#) (the *Supplemental Labor-Detail Background*), which also will be repeated in *No. 953-B*).

The inverted scale of the ShadowStats Alternate Unemployment Rate (*Graph 2*) is a surrogate for the magnitude of discouraged and displaced workers, who also are reflected in the accompanying *Graphs 3* and *4* of the *Civilian Employment-to-Population Ratio* and the *Labor-Force Participation Rate*.

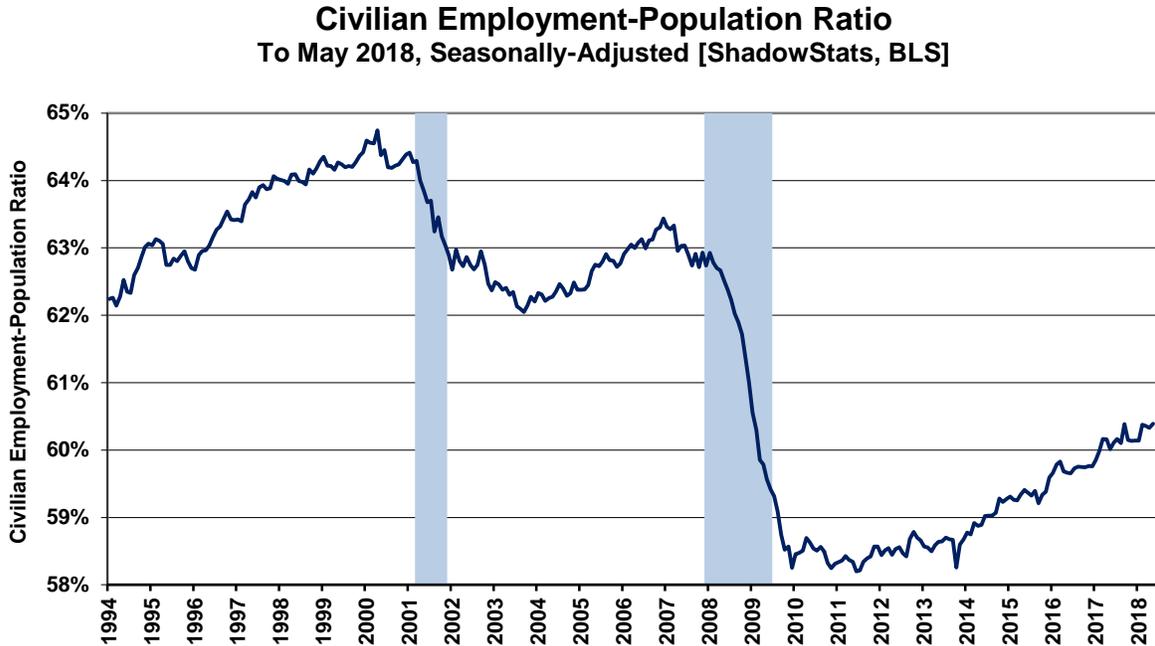
Graph 2: Inverted-Scale — ShadowStats Alternate Unemployment Measure



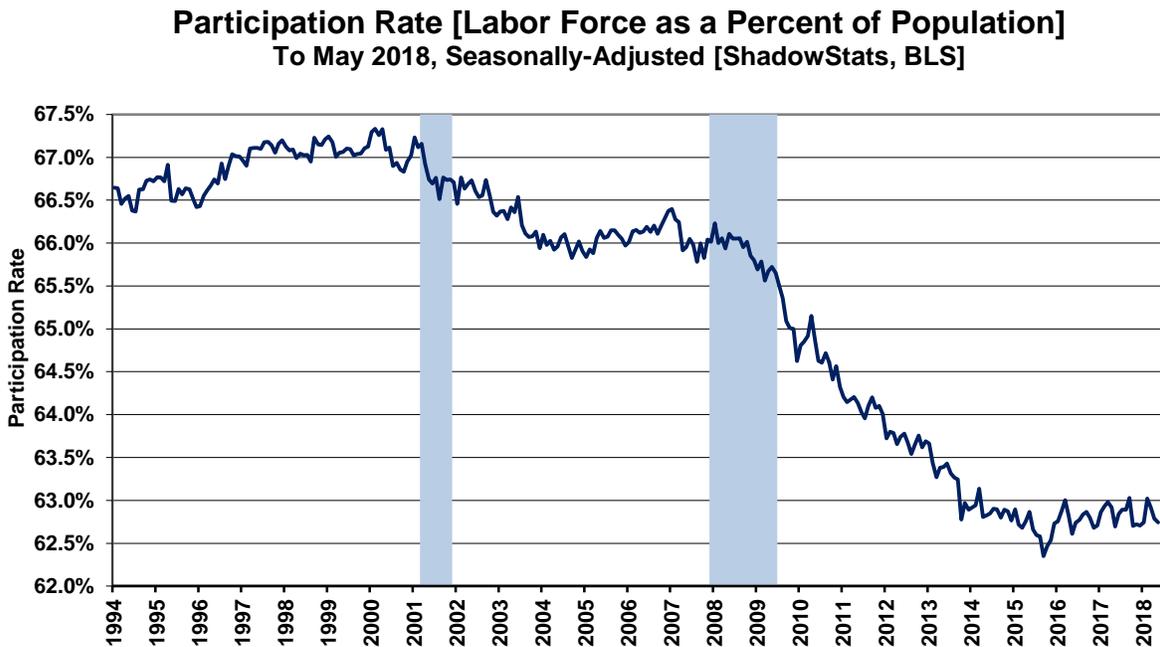
The Household Survey counts an employed person only once, irrespective of how many jobs or part-time jobs he or she may hold. In contrast, the Payroll Survey counts only the number of jobs, irrespective of the number of people holding those jobs. In that circumstance, a person holding two or more part-time

jobs is counted as employed with each job. The Household Survey estimated an adjusted 7.442 million individuals held multiple jobs in May, down from 7.667 million in April.

Graph 3: Civilian Employment-to-Population Ratio

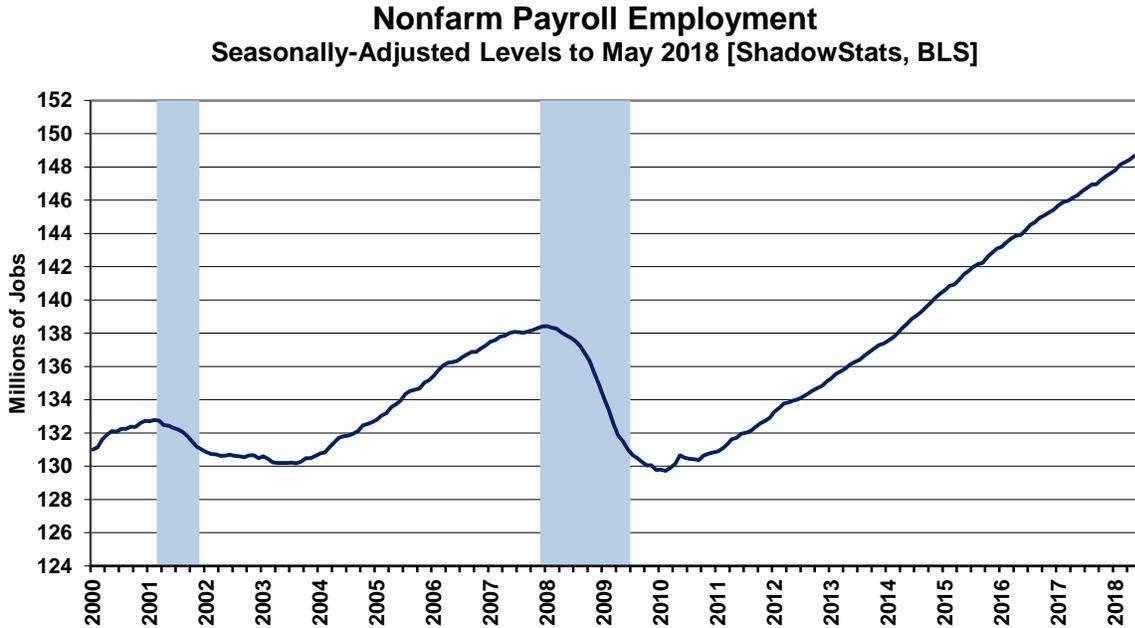


Graph 4: Labor-Force Participation Rate

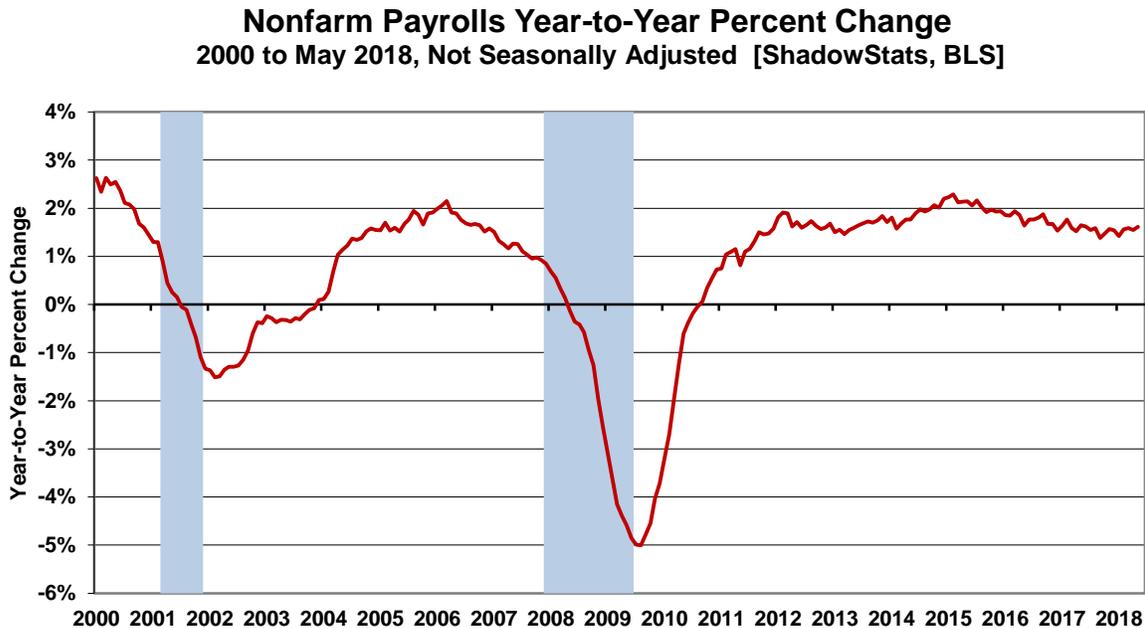


May 2018 payrolls rose month-to-month 223,000, versus a revised 159,000 [previously 164,000] gain in April, shown in *Graph 5*. Reflected in *Graph 6*, unadjusted annual payroll growth of 1.61%, versus an unrevised 1.55% in April 2018, broadly remained in a downtrend that has reached a level and pattern of growth usually preceding and signaling the onset of a recession.

Graph 5: Nonfarm Payroll Employment 2000 to Date

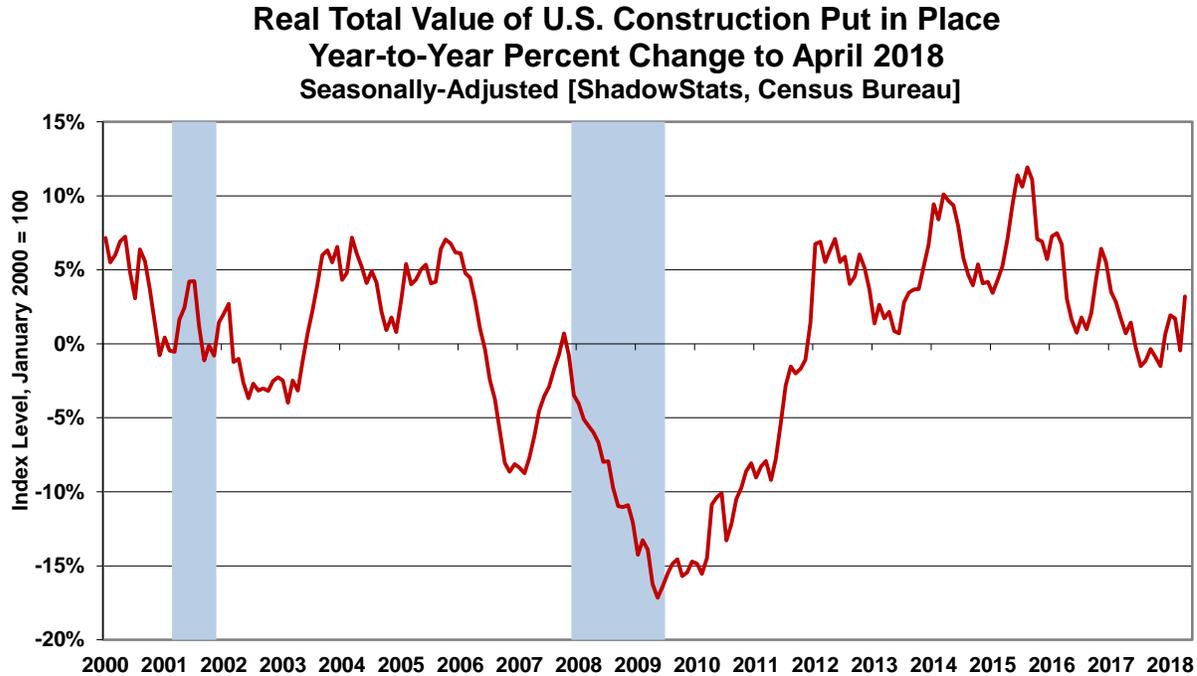


Graph 6: Payroll Employment, Year-to-Year Percent Change, 2000 to Date



Construction Spending—April 2018—Activity Surged in April 2018, Pushing Annual Real Growth to Its Highest Level Since January 2017. The regularly-volatile Construction Spending series, saw an unusually-large monthly gain of 1.8% in April, up by 7.6% year-to-year. The gain primarily was in private, single-unit residential construction, contrary to indications in recently reported Housing Starts activity (see [Commentary No. 950](#)). The movement was enough to boost inflation-adjusted real annual growth to its highest level since January 2017 (see *Graph 7*). While that is a positive economic signal, it likely will not survive next month’s July 2nd benchmarking of the series.

Graph 7: Total Real Construction Spending, Year-to-Year Percent Change

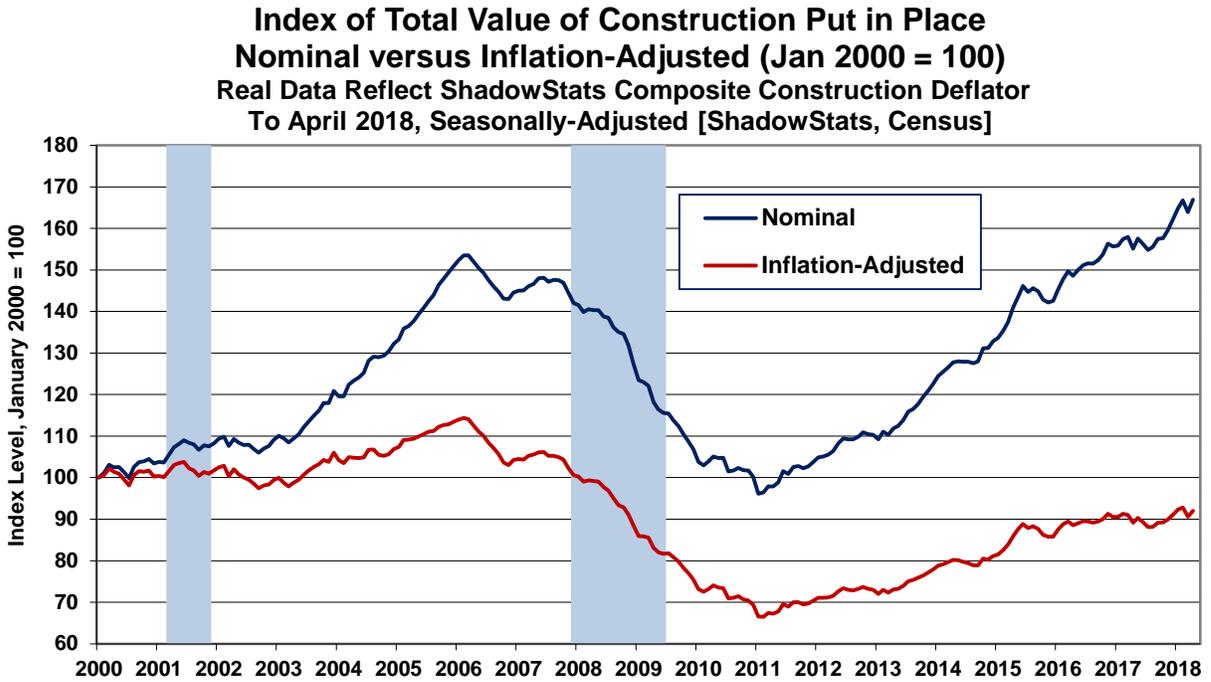


Despite the aggregate headline monthly and annual gains, April 2018 Real Construction Spending held shy by 19.5% (-19.5%) of regaining its March 2006 pre-recession high (see *Graph 8*). That general pattern also was reflected in its major subsidiary series seen in *Graphs 9 to 11*.

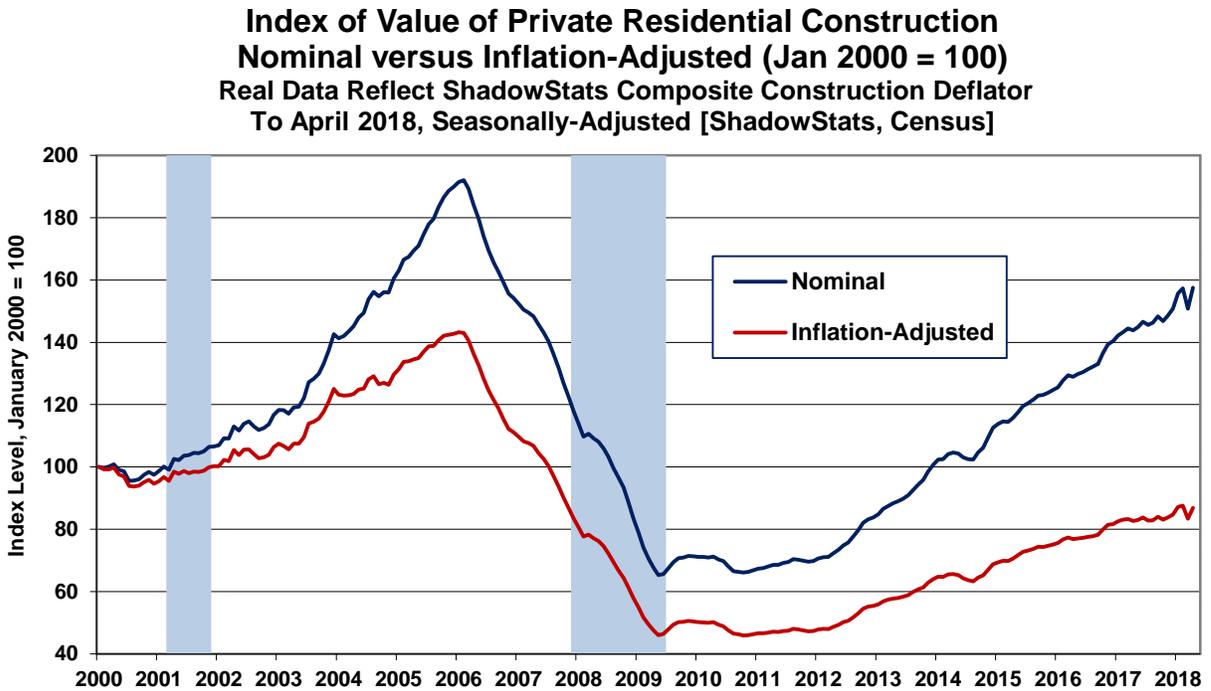
Extended coverage of April 2018 Construction Spending follows in *Commentary 953-B* of June 4th.

[Graphs 8 to 11 begin on the next page.]

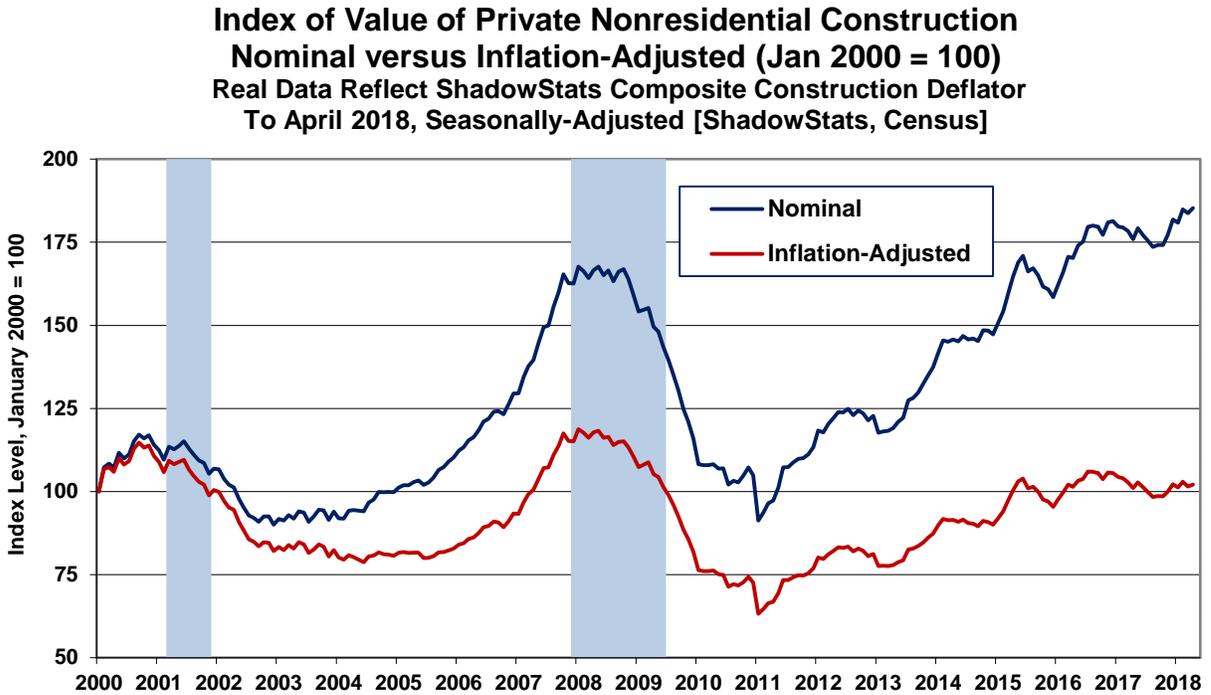
Graph 8: Index, Nominal versus Real Value of Total Construction



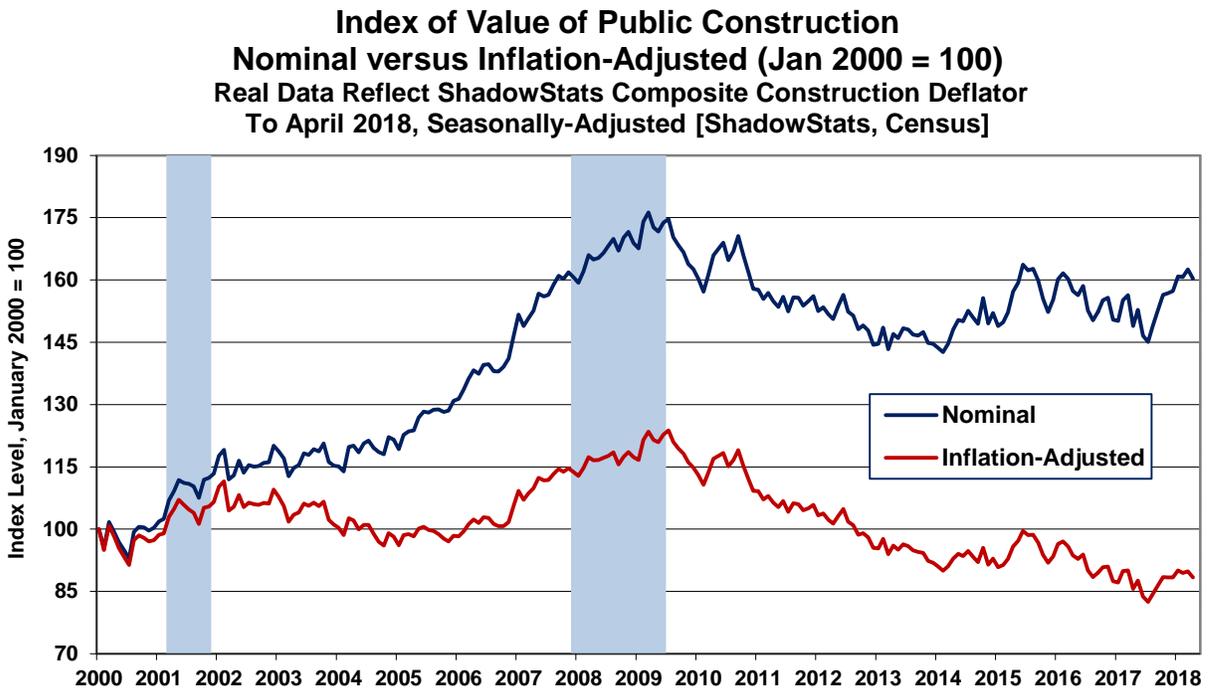
Graph 9: Index, Nominal versus Real Value of Private Residential Construction



Graph 10: Index, Nominal versus Real Value of Private Nonresidential Construction



Graph 11: Index, Nominal versus Real Value of Public Construction



[Extended analysis and graphs of Employment and Unemployment, and Construction Spending will follow in regular Commentary No. 953-B, planned for June 4th.

The Hyperinflation Watch begins on the next page.]

HYPERINFLATION WATCH

MONETARY CONDITIONS

Intended Consequences: Beware “Unexpected” Economic Weakness/FOMC Policy Change!

Despite the record-low unemployment rate in May 2018, underlying labor-market stresses and continued weak annual growth in payroll employment signal economic trouble ahead. Private surveying of jobs-market conditions and real-median-household income also suggest that recent headline, economic strength is not as advertised (see the *Opening Comments* and *Consumer-Liquidity Watch* of [Commentary No. 952](#)).

Separately, seriously-conflicting policy issues for the Federal Open Market Committee (FOMC) of the Board of Governors of the Federal Reserve System include the tightening systemic liquidity, at the same time as trying to maintain banking system solvency/liquidity. The current tightening in monetary policy threatens to tank (or to exacerbate current, underlying weakness in) major sectors of U.S. economic activity. In conflict, such an intensifying economic downturn would stress banking-system liquidity.

The U.S. central bank’s primary concern remains the maintenance of solvency and liquidity in a still-troubled banking system. Intensifying economic and financial stresses on that system remain likely to cause the FOMC to back off its 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.

As the mounting economic/systemic stresses continue to unfold, market pressures and expectations should mount on the FOMC to pull back from further tightening. Accordingly, consensus expectations as to the timing and frequency of future rate hikes by the Fed increasingly should begin to waver, with negative impact on the U.S. dollar and an upside push to a commodity-driven (oil) U.S. inflation, despite what is or will be recognized as a weakening economy. Again, banking-system liquidity and solvency are the dominant policy consideration for the FOMC, not the relative strength of the domestic economy, as has been demonstrated frequently from the 2008 banking crisis to present.

Current Fed Policy Is Setting Up Future Economic and Systemic Turmoil. Take out rising headline inflation rates and from declining annual growth in the “tightened” nominal money supply measures, and a new recession-signal already is unfolding and intensifying rapidly (see the discussion and graph on pages 17 to 19 of [Commentary No. 949](#)). Annual real or inflation-adjusted growth in all three money supply measures has continued to drop, from a combination of falling nominal growth against rising annual CPI-U inflation, a pattern set to intensify, once again, with a likely continued further jump in May annual inflation (due for release on June 12th). Money supply (under FOMC control) drives liquidity, and weakening consumer liquidity, including faltering growth in real income and credit threatens broad economic activity already has started to intensify.

Regularly discussed here, unexpected, negative economic shocks lie ahead, not only in regular, near-term monthly reporting of popularly-followed series, but also as seen with recent and looming annual benchmark revisions to key series (again, see [Commentary No. 949](#)).

May 2018 M3 Annual Growth Eased to a Nine-Month Low of 4.0%, with Annual Growth in M1 and M2 Sinking to Levels Last Seen in 2010, Along with a Contracting Monetary Base. Based on three-plus weeks of reporting, with continued, sharply softening annual growth the narrower, monthly M2 and M1 measures sank to levels last seen in 2010, the estimate of nominal annual growth for the ShadowStats Ongoing M3 Money Supply in May 2018 hit a nine-month low of 4.0%. That was down from revised annual gains of 4.2% [previously 4.3%] in April 2018, 4.5% [previously 4.4%] in March 2018 and unrevised annual growth of 4.5% in February 2018, 4.5% in January 2018, 4.6% in December 2018, 4.5% in November and 4.7% in October 2017. That October year-to-year change was highest level seen since November 2015.

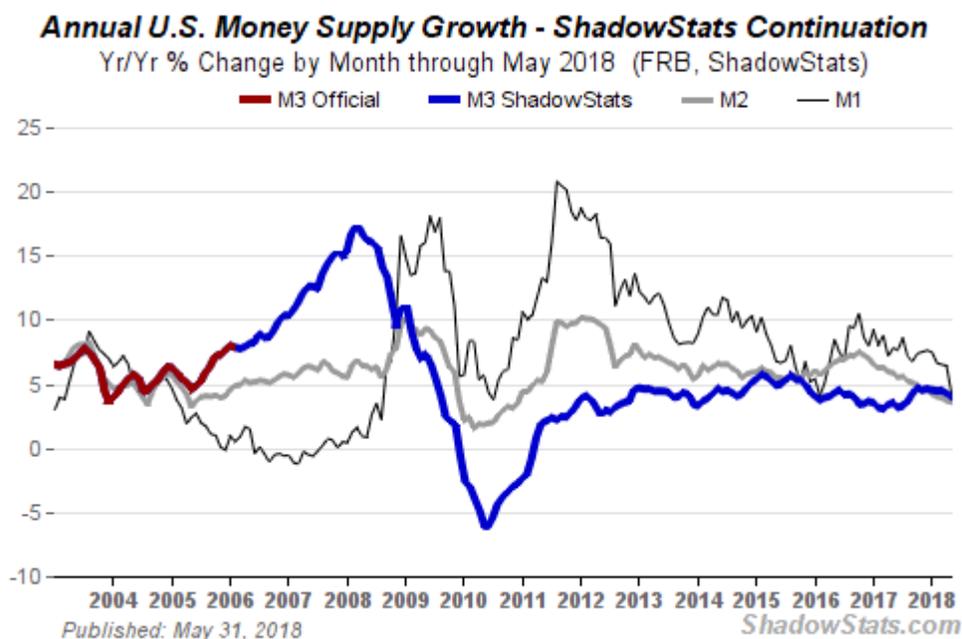
Those M3 growth rates were against unrevised annual gains of 4.2% in September 2017, 3.6% in August 2017 and irregular notching of annual growth lower back in time, to an unrevised 3.0% in March 2017, which was weakest year-to-year change since July 2012.

M2 Annual Growth Still Weakest Since December 2010. Separately, nominal year-to-year growth for M2 declined to 3.6% [3.64%] in May 2018, the lowest level seen since 3.6% [3.60%] December 2010. That was against annual growth of 3.7% in April 2018, 4.0% in March 2018, 4.1% in February 2018, 4.2% in January 2018, 4.7% in December 2017, 4.6% in November 2017, 5.0% in October 2017, 5.2% 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 Multi-Year Low. Annual nominal growth in May 2018 slowed to 4.3%, its lowest level since the one-month of February 2016, otherwise at its lowest level since July 2010. The May 2018 growth of 4.3% was down from a revised 6.5% [previously 6.4%] in April 2018, 6.6% in March 2018, 6.7% in February 2018, 7.5% in January 2018, 7.7% in December 2017, 7.6% in November 2017, 7.4% 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. Going backwards in time, the monthly annual change in M1 tends to notch higher, hitting a near-term peak annual of 10.6% in October 2016, which was the strongest growth since 10.7% in September 2014.

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 in recent years for both M1 and M2, versus M3, until January 2018, when annual M3 growth overtook M2, in conjunction with interest rates being pushed higher by the FOMC. Nonetheless, the monthly annual growth in each of M1, M2 and M3 has slowed consistently since December 2017, near-term, along with the year-to-year contractions in the Monetary Base, all reflecting Federal Reserve policy.

Fed Policy Actions Have Moved Towards Restraining Headline Economic Activity. Annual M3 growth is declining in tandem with M1 and M2, at the same time as annual year-to-year CPI-U inflation was the rise in February through April 2018, again with a likely continued rise in May. These patterns are suggestive of weakening or declining economic activity, of the FOMC actively pushing to slow domestic economic growth, which still largely never recovered from the banking-crisis-induced economic collapse of 2008.

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

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 strength in annual M3 growth, however, reflected a returning flow of cash from M2 back into M3 accounts, again, such as large-time deposits, institutional money funds and Fed funds repurchase agreements. Still, the latest, softening headline details likely reflects and/or will tend to induce softening business activity. The latest estimates of level and annual changes for April 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. *Commentary No. 949* will update the April 2018 inflation-adjusted annual M3 growth.

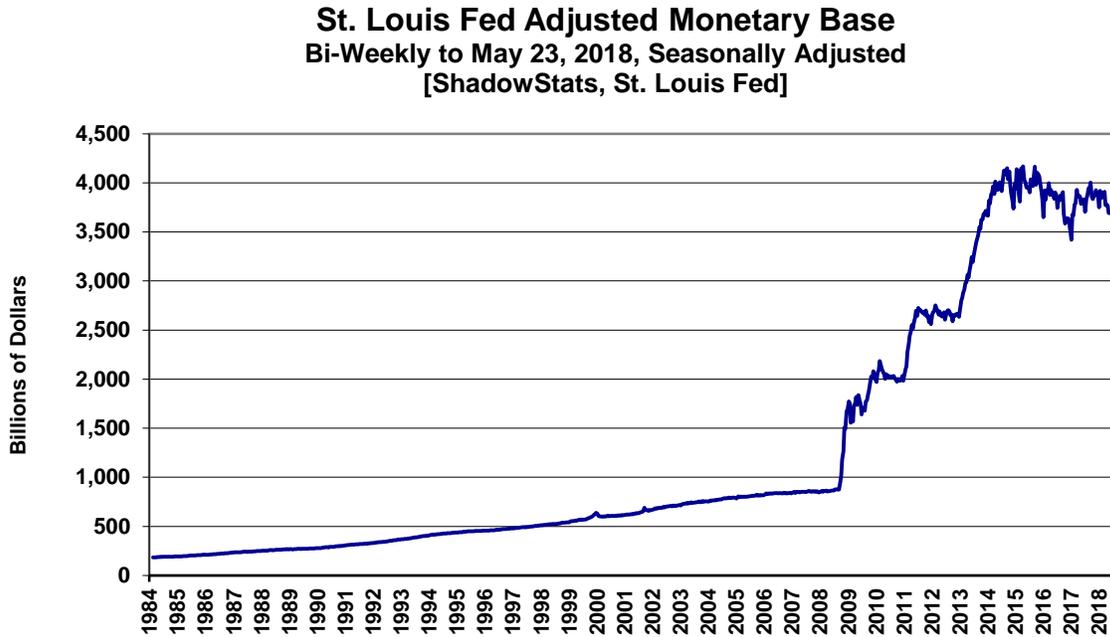
May 2018 Monetary Base Has Declined Both Month-to-Month and Year-to-Year for the Third Straight Month. As annual growth in M3 jumped in late 2017 so, too, did annual growth in the Monetary Base. In the wake of near-term volatility surrounding recent rate hikes by the FOMC, and the related market efforts by New York Fed to establish or stabilize a 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. Annual growth in both series peaked near-term in December 2017, at multi-year highs. The Monetary Base was up by 9.7% year-to-year in the two weeks ended January 3, 2018, fell back to 2.3% in the two weeks ended February 28th, turned down year-to-year 2.3% (-2.3%) for the two weeks ended March 28th, by 2.4% for the two weeks ended April 25th and the Saint Louis Fed's estimate of the Monetary Base was down by 2.6% (-2.6%) year-to-year in the two weeks ended May 23rd. Accompanying *Graphs HW-2* and *HW-3*, reflect that detail.

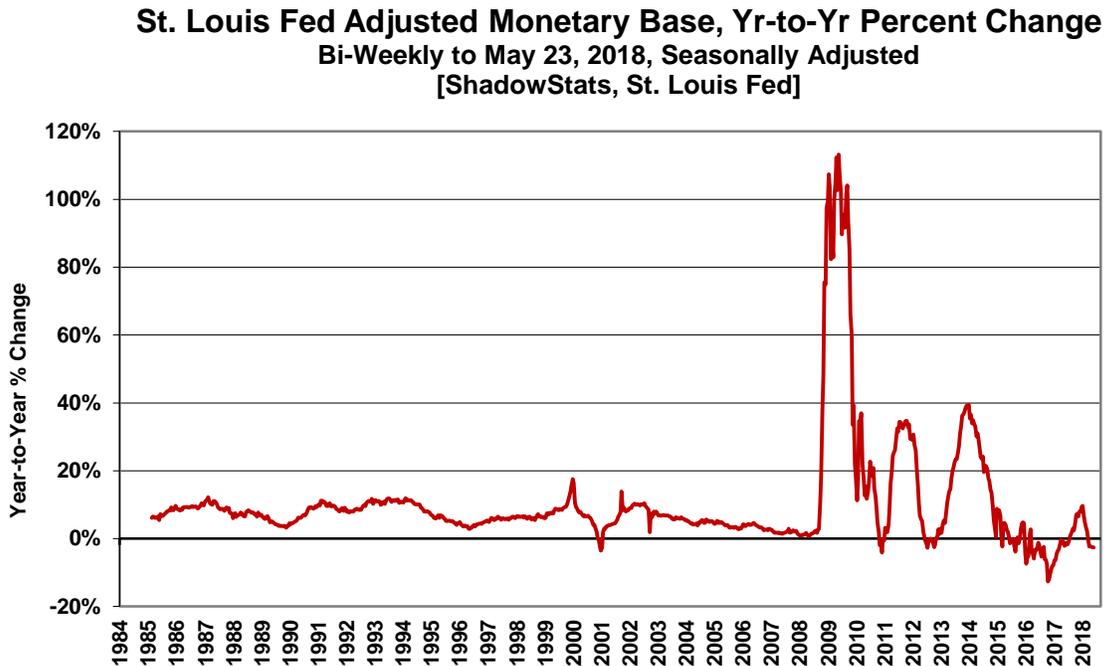
Aside from short-term gyrations around the timing of change in the targeted federal funds rate (as could have affected the late-March 2018 data), circumstances generally should remain relatively stable, until the

Fed sells its Treasuries and Mortgage-Backed Securities more heavily, as part of its planned “balance sheet normalization.” More speculatively, the Fed could fall back on expanded quantitative easing, amidst mounting liquidity stresses in the banking system, generated by deteriorating economic conditions.

Graph HW-2: Saint Louis Fed Monetary Base, Billions of Dollars (1984 to May 23, 2018)



Graph HW-3: Year-to-Year Percent Change, Saint Louis Fed Monetary Base (1985 to May 23, 2018)



While the level of the Monetary Base remains within the bounds of activity seen of the last several years, it is trending lower. Prior to Quantitative Easing, changing the level of the Monetary Base had been the primary tool of the FOMC for targeting growth in the money supply. Late-2017 upside movements in annual growth for M3 and the Monetary Base have reversed, dropping off sharply, together. With the current activity confirming a sharp tightening in FOMC policy, intended negative economic consequences already have started to flow, as discussed in the opening paragraphs of this *Hyperinflation Watch*.
