John Williams'

Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 984

Financial-Market Alert and Economic Review—June 24, 2019

UPDATED ALERT: New Recession Breaks into the Open, with an Annual Decline in Freight Activity Not Seen Since the Great Recession, May 2019 Zero Net Payroll Growth and Quarterly Contractions in Key Series

As the Downturn Intensifies, So Too Should U.S. Dollar Selling and Flight to Gold, With the Stock Market Vulnerable to Massive Selling

Fed Chair Powell Hinted at Possible Later Easing, but Current Conditions Justify Greater Accommodation Now; New Quantitative Easing Is Possible by September

With FOMC Easing Hinted, U.S. Stocks Rose to New Highs; but a Greater Dollar Plunge and a Greater Gold Price Surge Each More Than Offset the Stock Gains

Excessive FOMC Tightening and Rate Hikes Triggered the New Downturn

When the Fed Shifted to Its Restrictive Monetary Stance, Much of the U.S. Economy Still Had Not Recovered from Its Collapse into 2009; That Exacerbated Already Heavily Negative Consumer Financial Conditions

Tightening Has Continued, With the May 2019 Monetary Base at a Six-Year Low, Down 3.2% (-3.2%) From December 2018

Full Economic Recovery Requires More than Interest Rate Cuts and FOMC Easing

Also Needed Are Meaningful Tax Cuts for Main Street U.S.A., and Stimulative Government Spending, Despite the Ongoing Budget-Deficit Disaster

In Response to Such Deficit-Busting Stimulus, Global Markets Likely Would Savage the Dollar, Unless the U.S. Government First Could Put in Place a Credible Plan for Balancing Its Finances Once Economic Conditions Had Stabilized

Government Action Is Unlikely, Though, Shy of Response to a Financial Crisis or Panic

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Note to Subscribers: The *ShadowStats* general outlook has not changed, specifically including a rapidly deepening U.S. economic downturn, reflected in mounting downside pressures on the U.S. dollar, flight to safety and upside pressures on gold and silver prices, and increasingly high risk of heavy stock-market selling in the weeks and months ahead.

An expanded ***ShadowStats ALERT*** begins on page 5, updating the April 22nd version published in ***Special Commentary No. 983-B***. Incorporated here by reference, ***No. 983-B*** reviewed broad economic conditions and sovereign solvency issues that ultimately affect the political and financial stability of the United States, and it expanded upon earlier *ALERT* versions published in ***Commentary No. 983-A*** of February 20th, ***Hyperinflation Watch No. 4*** of December 11, 2018 and the original ***Special Commentary No. 973 – ALERT*** of October 14, 2018. Also incorporated here by reference is ***Commentary No. 970*** of September 26, 2018, on a potential, pending Tipping Point in the U.S. financial markets, and ***Consumer Liquidity Watch No. 5*** of November 21, 2018 as to underlying consumer-liquidity issues. Long-range prospects for economic-turmoil and eventual U.S. hyperinflation have continued to close in rapidly, along with a flight to safety out of a weakening U.S. dollar and flight into precious metals, amidst volatile stock-market activity since late-December 2018. The more negative the pressure on the dollar, and the stronger the flight-to-safety in precious metals and the more dangerous the situation for domestic equity prices. A rapidly weakening U.S. Dollar and rallying gold and silver prices are solid signs of impaired systemic and market conditions that easily can mutate investor fears into other market distortions.

Your comments and suggestions always are invited.

Best Wishes — John Williams (707) 763-5786, johnwilliams@shadowstats.com

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ShadowStats Commentaries, Bullet Editions, Watches and Daily Updates:

- The ***Daily Update*** posts regularly on the *ShadowStats* home page (**www.ShadowStats.com**), covering major economic releases, usually within two-to-three hours of headline publication. Unusual market circumstances, and pending *ShadowStats* publications also are covered.
- The ***Bullet Edition*** usually publishes multiple times per month, as dictated by economic and financial-market developments. Simply put, the ***Bullet Edition*** conveys brief communications and analyses on topics of particular near-term significance.
  - ***Bullet Edition No. 12,*** late in the week ahead, will review the June 25th Retail Sales benchmark revisions and the June 27th second estimate of First-Quarter 2019 GDP, among other reporting.
- ***Regular Commentaries*** should publish every six weeks, or so, providing a more comprehensive overview of general conditions, occasionally as a *Special Commentary*.
  - ***Special Commentary No. 983-B*** posted April 22nd.
  - ***Commentary No. 985*** likely will be published in late July.
- ***Hyperinflation*** and ***Consumer Liquidity Watches*** will update monthly, with alternating updates roughly every other week, beginning in the next couple of weeks.
- ***Telephone Consulting*** is part of the regular service for subscribers. Whenever you have a question on the *ShadowStats* outlook or otherwise would like to talk, please call John Williams at (707) 763-5786.

All ***Current*** and ***Earlier ShadowStats Commentaries*** and other writings (back to 2004) are available here in the ***Archives Section*** (linked to the full archives), otherwise located in the left-hand column of the **ShadowStats Home Page** (www.ShadowStats.com).

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ShadowStats ALERT

OVERVIEW

FUMBLING FED, FALTERING ECONOMY AND LOOMING FINANCIAL CRISES

New Recession Deep Enough to Have FOMC Easing / Quantitative Easing by September

Irrespective of Other Global Issues, U.S. Dollar Should Be Pummeled

Dollar Weakness Tends to Spike Domestic Inflation and Flight from Equities

Watch for Heavy Stock Selling, Flight from the Dollar and Intensified Flight to Gold!

U.S. Government Needs to Address Its Long-Range Sovereign-Solvency Issues Now

Economic Reporting of the Last Six Months Has Shown an Intensifying, Broad Economic Downturn. U.S. economic circumstances are deteriorating sharply and quickly. With the partial exception of blips in May 2019 Real Retail Sales, and likely, heavily disrupted and distorted First-Quarter 2019 GDP data. Better-quality reporting of headline major economic series of the last couple of months has signaled a sharply deteriorating recession. Payroll Jobs, Household Survey Employment and Unemployment, Real Earnings, Industrial Production, Construction Spending, New Residential Construction and the CASS Freight Index™ all have continued markedly weaker in the latest reporting. Current growth patterns here generally have not been seen since the onset of the Great Recession in First-Quarter 2008. The GDP and Retail Sales series likely suffer from government-shutdown disrupted and distorted data, and they could see some pending reporting-quality improvement from annual benchmark revisions of June 25th for Retail Sales, and the June 27th third-estimate of First-Quarter 2019 GDP revisions and the July 26th annual benchmark revisions for the GDP.

Unfolding Business-Cycle Timing, Consecutive Quarter-to-Quarter Contractions in Real GDP. Noted in ***Special Commentary No. 983-B*** of April 22nd, and updated here, ShadowStats contends that headline reporting of inflation-adjusted, real quarterly GDP "growth" likely peaked in second-quarter 2018 and slowed into third- and fourth-quarter 2018, with the "level" of activity falling into outright quarter-to-

quarter contraction in first-quarter 2019, with second-quarter 2019 continuing in downturn and with third-quarter 2019 also likely in decline. Eventually, the present circumstance should be recognized, measured and timed as a "new" recession, off an economic peak level of activity in Fourth-Quarter 2018 GDP (likely timed to November 2018). Again, late fourth-quarter 2018 and early first-quarter 2019 numbers appear heavily distorted by government-shutdown data disruptions.

Formal GDP Contractions Still Are to Be Seen. Reviewed in ***Special Commentary No. 983-B***, ***Bullet Edition No. 4***, ***Bullet Edition No. 5***, ***Bullet Edition No. 7*** and ***Bullet Edition No. 11***, current headline detail shows annualized real quarterly GDP growth of 2.2% in fourth-quarter 2018, down from 3.4% in third-quarter 2018 and a near-term peak of 4.2% in second-quarter 2018. First-Quarter 2019 GDP came in at 3.2% in its "advance" estimate, and revised to 3.1% in its second estimate. With pending revisions in the week and month ahead, whether or not the first-quarter growth estimate turns negative in revision, there most certainly will be consecutive headline quarterly contractions pending in the reporting of Second-Quarter and Third-Quarter 2019 GDP. Nonetheless, underlying economic series still indicate a First-Quarter 2019 GDP contraction, as discussed in ***SECTION 1***. The ultimate, official "Recession" call and timing eventually will be set by the National Bureau of Economic Research (NBER).

FOMC Efforts to Reverse Quantitate Easing Have Triggered the Intensifying "New Economic Downturn." In broad perspective, the current economic disruption effectively is the long-range, second down-leg of still-unresolved and unfolding circumstances of the 2007/2008 financial collapse. Indeed, the roots of this current "new" recession are found directly in that effective systemic failure or collapse of 2007/2008, and the ensuing, extraordinary Federal Reserve and the U.S. Federal Government systemic "bailout," which left broad swaths of the domestic economy never fully recovered from the Great Recession, when the FOMC began to tighten systemic liquidity in 2017, after an aborted attempt in 2015. FOMC rate hikes of the last couple of years have had the effect of constraining consumer liquidity and depressing the economy, all part of the Fed's efforts to reverse the Quantitative Easing (QE) used earlier in the systemic crisis to bailout and to salvage the failing banking system (see respective discussions in ***Sections 1*** and ***3***). Extended analysis of underlying detail follows in ***SECTION 1: HEADLINE NUMBERS INCREASINGLY SHOW RECESSION***, beginning on page 8.

U.S. Recessions Traditionally Are Not Good News for the Stock Market or the U.S. Dollar, and Usually Trigger Stimulative Policy Actions from the Federal Reserve and the Federal Government. The price of Gold remains the Canary in the Coal Mine for the U.S. financial markets. Likely impact of an intensifying economic downturn on the U.S. financial markets is reviewed in ***SECTION 2: FINANCIAL MARKET IMPLICATIONS***, beginning on page 30. Despite the heavily hyped U.S. stock-market rally in response to Federal Reserve Chairman Jerome Powell's June 19th FOMC News Conference, where he hinted there could be some FOMC easing in future, market reactions in U.S. dollar trading and in the trading of precious metals had heavily negative implications for the U.S. equity markets.

Federal Reserve Policies Have Given Maximum Attention to Banking System Needs, With Only Minimal, Secondary Consideration to the Needs of Main Street U.S.A. Owned by the major banks, the U.S. Federal Reserve provided an unconditional bailout to the U.S. banking and financial systems at the onset of the banking-system-collapse-triggered Great Recession, along with cooperative systemic bailout operations from the U.S. government. Broadly ignored were the needs of Main Street U.S.A.,

which largely never recovered fully from the Great Recession, along with major sectors of the U.S. economy, including the Manufacturing and Construction industries.

The Fed's tightening of recent years, which accelerated in 2017, was designed to help return the banking system to more normal functioning. Yet, the efforts to reverse the systemic distortions created by the financial-system bailout, by raising interest rates and constraining systemic liquidity, triggered a "new" recession, although major portions of the economy had never fully recovered from the economic crash from 2007 into 2009.

With the U.S. government pursuing "unsustainable" fiscal policies, as acknowledged by Federal Reserve Chairman Jerome Powell in public comments on CNBC and by U.S. Treasury Secretary Steven Mnuchin in his introduction to the 2018 Financial Statement of the U.S. Government (see ***SECTION IV*****),** and as the FOMC begins to suggest that it may have to backpedal on its tightening, the Fed has succeeded in setting up the U.S. economy for a major downturn, the U.S. dollar for a major crash, along with flight capital seeking the traditional safety of precious metals, particularly gold, and the U.S. stock market for a major sell-off. The unfolding impact of the recent, evolving Federal Reserve policies on the escalating economic and financial-market crises are reviewed in ***SECTION 3: FEDERAL RESERVE AND MONETARY POLICY***, page 36.

Massive Systemic Distortions from Federal Reserve Policies of Recent Decades Threaten Domestic Financial and Economic Tranquility. Economic stability, U.S. Government fiscal conditions and policies, and long-range U.S. Sovereign Solvency issues are reviewed in ***SECTION 4: STIMULATIVE FISCAL POLICY NEEDED ALONG WITH FED EASING,*** beginning on page 41.

[SECTION 1 begins on the next page.]

SECTION 1 – HEADLINE NUMBERS INCREASINGLY SHOW RECESSION

Major Sectors of the Economy Still Never Have Recovered from the Great Recession

Aborted FOMC Tightening Drove the 2015 Production Downturn, Masked by Bad Data

Lost Economic Recovery Begins to Gain Some Notice. The popular media and the financial markets have begun to notice, discuss and confirm the long-time ShadowStats contention that major sectors of the U.S. economy never recovered from the economic collapse from fourth-quarter 2007 into 2009, more popularly known as the Great Recession. The continuing economic malaise, doldrums and non-recovery, range from the Manufacturing and Construction Sectors of the economy, to the level of real Consumer Income, Consumer Credit and business activity on Main Street U.S.A. Such was discussed extensively in ***Special Commentary No. 983-B*** of April 22nd, which provided extended coverage of the ShadowStats broad outlook for the U.S. economy and financial markets. Subsequent economic reporting was updated in ***Bullet Edition No. 7***, ***No. 8***, ***No. 9***, ***No. 10*** and ***No. 11***. The ShadowStats forecast of a formal new Recession has not changed materially, and the major points in ***No. 983-B*** remain intact. As will be discussed, recent headline reporting from Payroll Employment and Construction Activity, to Industrial Production and Freight Activity consistently have shown an unfolding economic recession.

A Lack of Recovery and Economic Expansion. In traditional Business Cycle definition, inflation-adjusted "Real" economic activity hits an economic "Peak." Activity declining off its "Peak" enters a "Recession," which bottoms in a "Trough." Activity moving off the "Trough" enters "Recovery," until activity "Recovers" its "Pre-Recession Peak." Growth beyond that "Pre-Recession Peak" is "Economic Expansion," until activity hits a new "Peak" and the cycle begins again. Some of apologists for normal downside cycles in the economy use "Expansion" as euphemism for anything that is off bottom. Yet, the historical norm is measuring "Expansion" of from prior peak activity.

Current headline economic reporting has shown the uncomfortable reality of a record 137 consecutive months of economic non-expansion in the Manufacturing Sector of Industrial Production (unprecedented in the 100-year history of Industrial Production) as reported by the Federal Reserve Board (see *Graph 5*). The same can be said for record-long periods of economic non-expansion in the post-World War II history of the Construction Industry—particularly tied to Residential Real Estate—as reported by the Commerce Department. Consider *Graph 27* of Housing Starts, which shows in the current cycle that not only has the series failed to recover its pre-recession high, but also that it has failed to recover the pre-recession high of any recession back to World War II. The same can be said for private sector Real Estate surveys, such as the high-quality Existing-Home Sales series from the National Association of Realtors.

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Extended Period of Economic Non-Expansion for Main Street U.S.A. As to underlying, common economic experience, Census Bureau surveying of Real Median Annual Household Income, Bureau of Labor Statistics Surveying of Real Average Weekly Earnings, Federal Reserve surveying of Real Consumer Credit and private surveying of Consumer Liquidity and Financial conditions, show an unprecedented period of non-expansion in U.S. Consumer Real Income and Real Credit Outstanding for Main Street U.S.A.

The recent excessive liquidity tightening (asset sales) and rate hikes by the Federal Reserve have hit the aggregate U.S. economy heavily on the downside, triggering what is gaining recognition as a new recession, a deepening, painfully exacerbating and significant downturn in non-recovered economic segments of the Great Recession.

Consider Annie Nova's June 14th **CNBC story** citing a study commissioned and published by Bankrate.com: ***47 Million Are Worse Off Now Than Before the Great Recession***, with the sub-title: ***Nearly half of Americans born before 1990 have seen no financial improvement***.

ShadowStats will publish its ***Informal Survey of Economic Condition*** in the next couple of days. While not scientifically designed, responses suggest a mixed economic environment by region, across the United States, with some areas booming or slowing off recent peaks, against a broad swath of regional activity that never recovered pre-recession highs. Reporting of actual local circumstances, as seen with the bank rate study and the informal ShadowStats survey, reflects the first-hand, local-economy experiences of the survey participants, as opposed to survey participants being asked to forecast the broad national economy, usually as seen with national consumer opinion surveys.

The traditional confidence and sentiment surveys generally ask respondents to forecast the economy six months into the future. Where the average survey respondent is not an economist, responses most frequently tend to reflect the tone of the popular press. Professor David Fan, PhD, of the University of Minnesota, established such several decades ago. By indexing the relative positive or negative nature of the tone of press coverage towards the economy and the markets, he was able to predict the movements in the Confidence and Sentiment surveys with high a degree of accuracy. Albert Sindlinger, who began the formal consumer surveying concept in the 1930s, reached that same conclusion.

Broad Indicators of Economic Activity Continue to Show a Clear and Meaningful Downturn in the General Economy. The FOMC's tentative, negative shift away from contending that U.S. economic growth is healthy and normal is a late-game canard. The May 2019 employment numbers were far from normal and healthy, as were most other headline economic series. The Fed wants to tighten, and simply is hoping to put off an inevitable easing for as long as possible.

Consider the recent trends in the CASS Freight Index™, which *ShadowStats* classifies as a highest-quality, reliable indicator of broad U.S. activity. It has a significantly better history of signaling U.S. economic health than does the FOMC (see *Graphs 1* and *2*).

[Coverage of the CASS Freight Index™ begins on the next page.]

CASS Freight Index™ Just Took Its Biggest Annual Hit Since the Great Recession Onset

May 2019 CASS Freight Index™ Year-to-Year Decline of 6.0% (-6.0%) Was the Deepest Annual Drop Since Going Into and Coming Out of the Great Recession. May 2019 CASS Freight Index™ (www.CassInfo.com, June 18th) fell year-to-year by 6.0% (-6.0%), the worst annual decline with the series in deepening contraction, since a drop of 5.2% (-5.2%) in February 2008, the second month of the formal Great Recession. It also was the weakest annual performance since November 2009, coming out of the Great Recession. The May 2019 12-month moving average declined month-to-month for the seventh straight month – all signaling a new recession and deepening second-quarter 2019 economic contraction. Those year-to-year and moving average metrics neutralize seasonality in this unadjusted series.

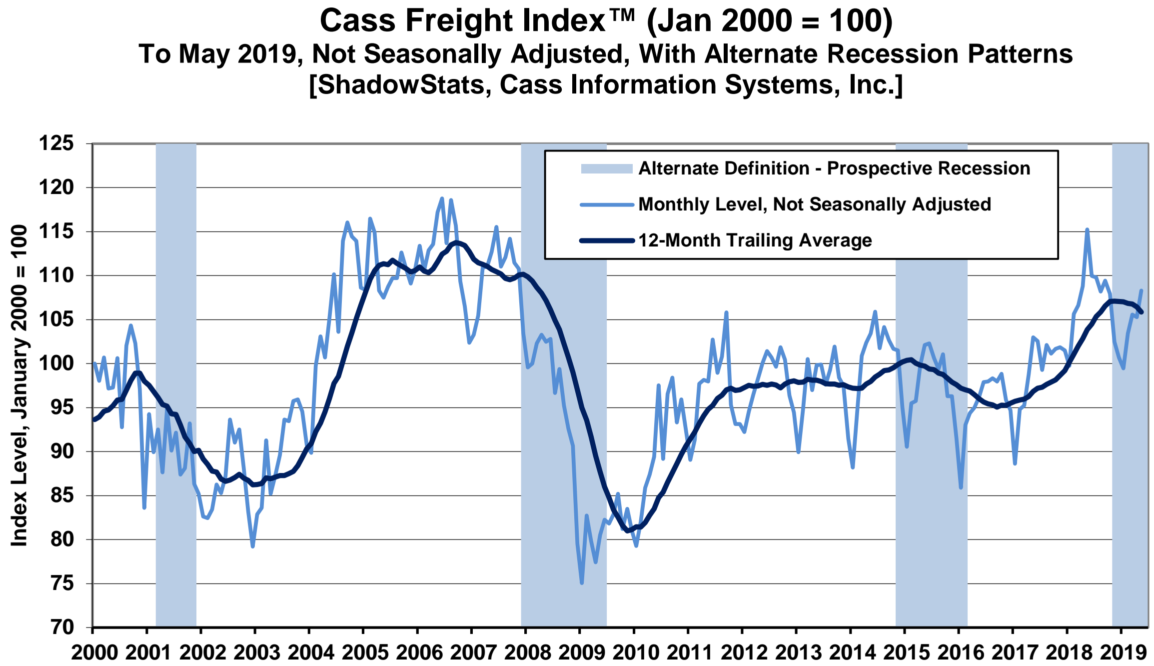
The current decline in annual growth was the deepest since the 2009 headline recovery from the Great Recession. Yet the pattern of a new downturn in annual growth and annual moving average last were seen in early 2015, at the onset of meaningful downturns in series such as Manufacturing, which recently also turned negative year-to-year in April 2019 reporting, for the first time since early 2015. Discussed in ***SECTION 3*, page 37**, a brief but aborted FOMC tightening in 2015 resulted in a drop in the level of the QE-boosted Monetary Base (see *Graphs 38* and *39*), with Industrial Production and Manufacturing declining as though they were in recession, as a result. Except, headline Production and Manufacturing reporting (controlled by the Federal Reserve) masked the downturn until several years later, when it surfaced in annual Manufacturing and Production benchmark revisions (see *Graph 36*). The CASS Freight Index™, however, showed the downturn in real time.

ShadowStats regularly follows and analyzes the CASS Index as a highest-quality coincident/leading indicator of underlying economic reality. We thank CASS for their permission to graph and to use their numbers. Reviewed and detailed in ***Bullet Edition No. 4***, ShadowStats is using tentative alternative, unofficial "Recession" bars in certain graphs for the 2015 mini-recession and the still unfolding December 2018 onset of the current "new" recession, as seen *Graphs 1* and *2* of the headline CASS Index, and *Graph 4* of headline Capacity Utilization of the Manufacturing Sector.

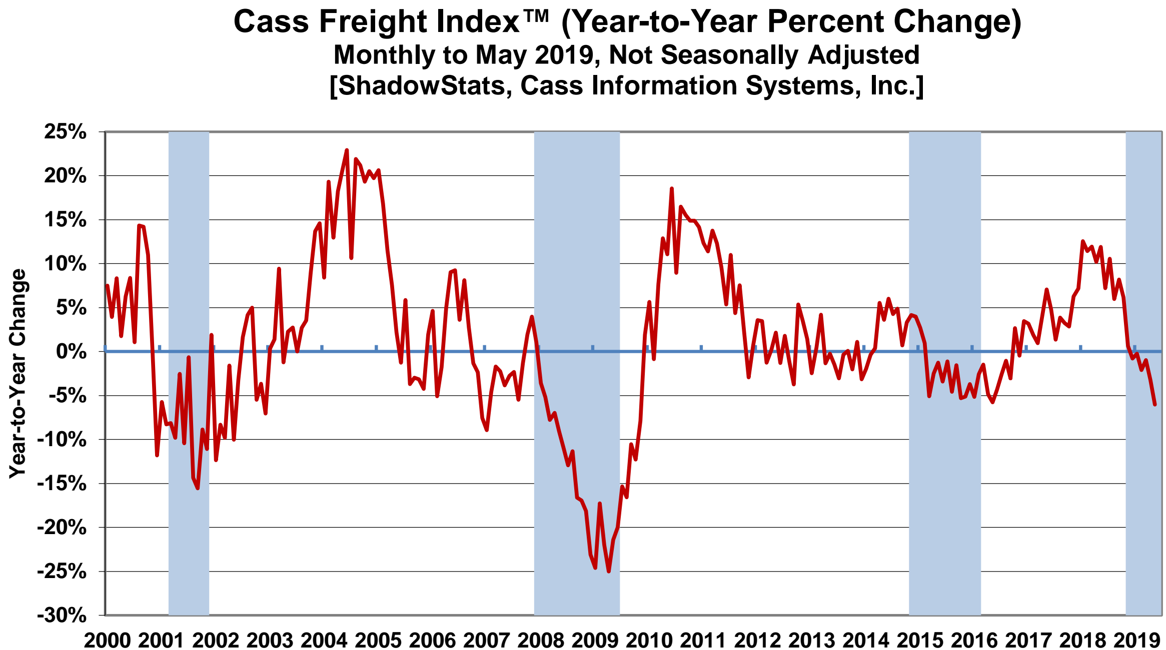
Discussed in ***SECTION 3*** the 2015 downturn seen in the CASS Freight Index™, and the Industrial Production and Manufacturing sectors was triggered by the aborted FOMC tightening in 2015 (see *Graph 38*), but again the production downturn was not obvious in the headline economic numbers of the time (other than for CASS), masked by the Fed's inaccurate headline Production data. The Fed's headline Production and Manufacturing series did not catch up with that underlying reality until the 2017/2018 benchmark revisions to the Manufacturing series (again, see later *Graph 36*).

[Graphs 1 and 2 follow on the next page]

Graph 1: CASS Freight Index™ Moving-Average Level, January 2000 to May 2019



Graph 2: CASS Freight Index™ Year-to-Year Change, January 2000 to May 2019



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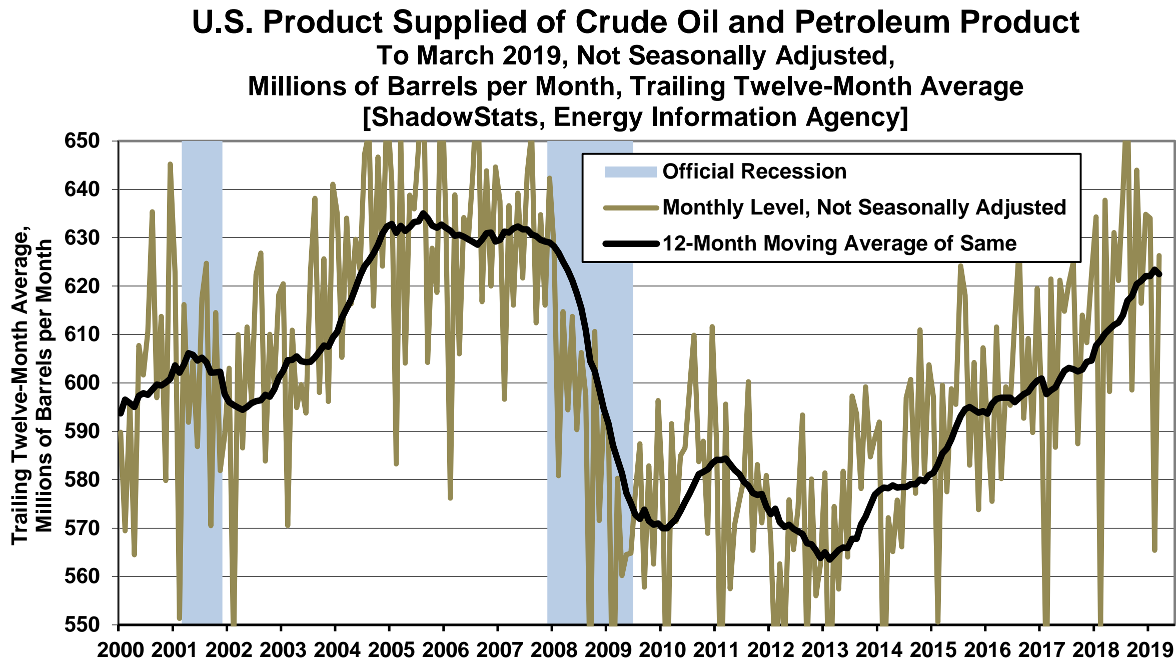
U.S. Crude Oil and Product Supplied Just Turned Down in Its 12-Month Moving Average

Another Sign of Topped U.S. Economic Activity. ShadowStats regularly seeks out measures of U.S. economic activity that are of good quality and not heavily manipulated, politically or otherwise. The twelve-month moving average of the physical volume of U.S. Product Supplied of Crude Oil and Petroleum Product just took its first monthly downturn in two years, also suggestive of downturn in broad economic activity.

Graph 3: U.S. Crude Oil and Petroleum Product Supplied, January 2000 to March 2019



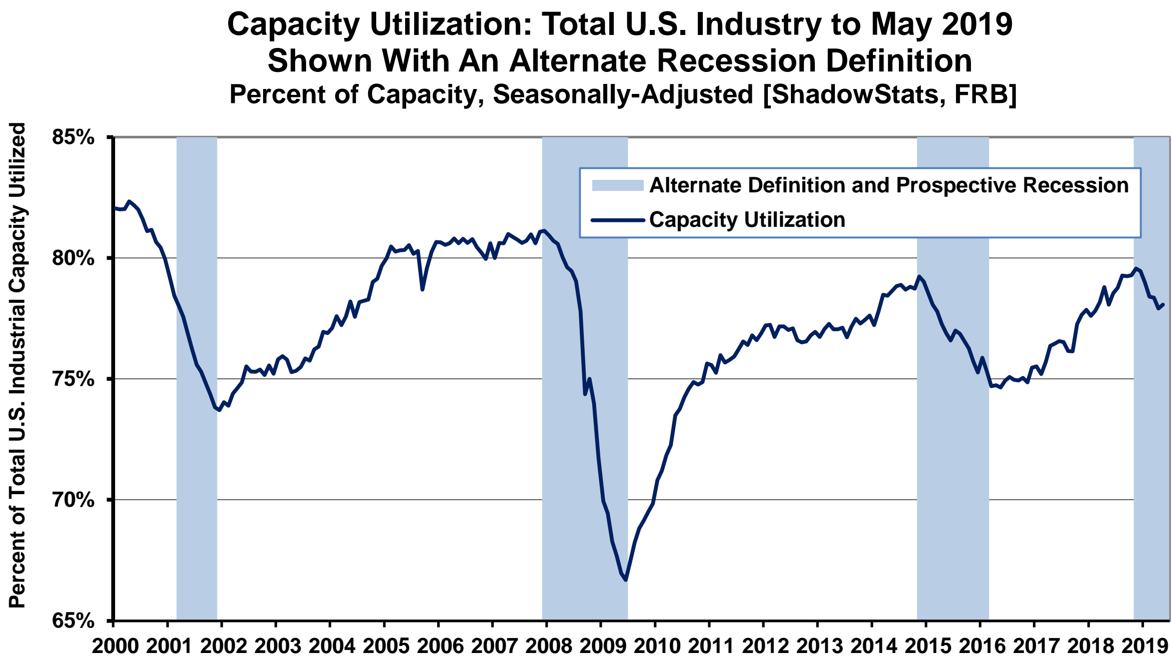
Production and Manufacturing on Solid Tracks for Consecutive Quarterly Contractions

May 2019 Industrial Production and Its Dominant Manufacturing Sector Both Gained in the Month, on Top of Downside Revisions, With Second-Quarter Activity on Solid Track for Second Consecutive Quarterly Declines (Federal Reserve Board, June 14th). Manufacturing gained 0.19% in May, with Mining up by 0.05% and Utilities up 2.11%, all contributing to the May 2019 aggregate monthly gain of 0.37% in Industrial Production. The Utilities change is random and usually dominated by unseasonable weather. The Mining Sector has had strong growth in the last year, dominated by oil production, but new exploration has been declining in the last six months. The dominant Manufacturing sector of Industrial Production is in a clear recession, although it showed its first monthly gain in four months from a temporary jump in auto production (*Graphs 5 to 8*).

Consistent with the ShadowStats forecast for an unfolding new recession, beginning with a quarterly contraction in first-quarter 2019 GDP (currently at 3.1%, subject to some likely downside revisions in the next two months), first-quarter 2019 Industrial Production declined at a revised annualized pace of 2.2% (-2.2%) [previously 1.9% (-1.9%)], on top of an unrevised fourth-quarter 2018 gain of 3.9%. Based on two months of reporting, the early trend for second-quarter 2019 is an annualized drop of 1.3% (-1.3%). Year-to-year, growth in Production slowed from 4.0% in 4q2018, to a revised 2.8% [previously 2.9%] in 1q2019, to an early-trend 1.3% in 2q2019. The dominant (75% of Production) Manufacturing Sector showed revised 4q2018 annualized growth of 1.5% [previously 1.6%], but plunged to a revised decline of 2.2% (-2.2%) [previously 2.1% (-2.1%)] in 1q2019, with an early-trend 2q2019 quarterly decline of 2.4% (-2.4%), along with successive quarterly year-to-year gains slowing from 2.2% in 4q2018, to 1.2% in 1q2019, to just 0.1% in 2q2019.

The unfolding 2019 recession was triggered by excessive Federal Reserve tightenings, which have constrained consumer liquidity and consumption. Weakness in the dominant personal consumption sector of the economy usually spreads quickly throughout the system. Consumer Goods Production (*Graphs 9* and *10*) contracted at a revised annualized 5.1% (-5.1%) [previously 4.7% (-4.7%)] in 1q2019, versus a 4q2018 revised gain of 2.4% (previously 2.5%), with an early-trend 2q2019 contracting an annualized 3.0% (-3.0%), and with year-to-year change on track for a 2q2019 annual decline of 1.2% (-1.2%), following a drop in 1q2019 of 0.3% (-0.3%), and an annual gain of 1.5% in 4q2018.

Graph 4: Utilization of Total U.S. Industrial Production Capacity (Showing Alternate Recession Bars)



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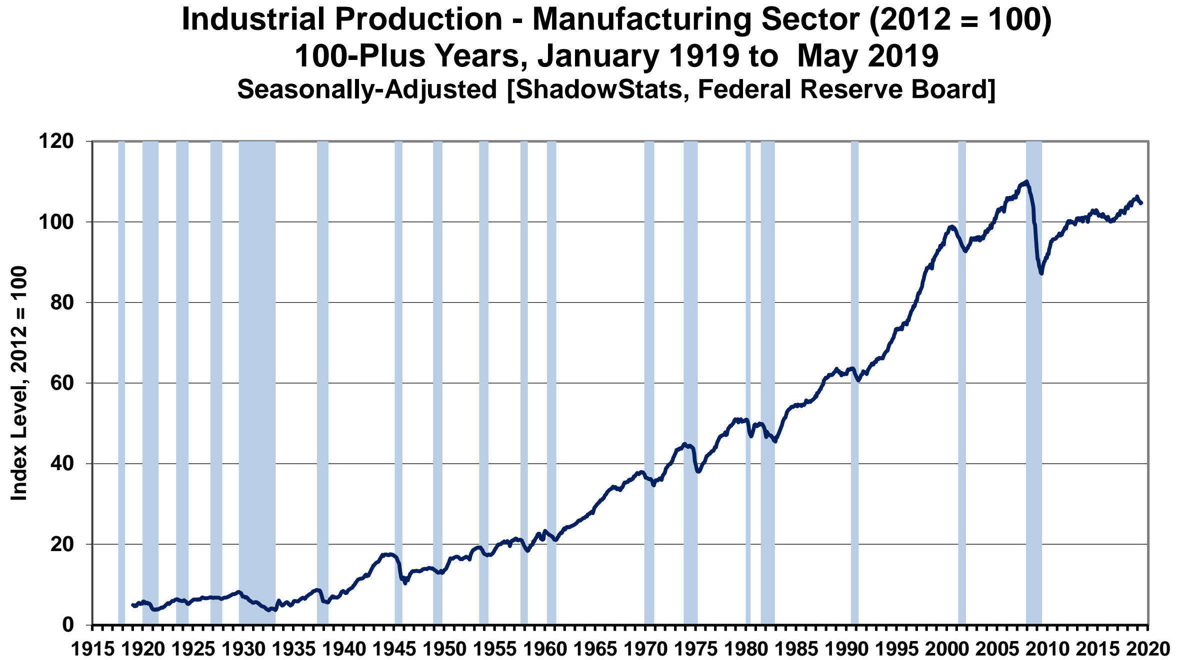
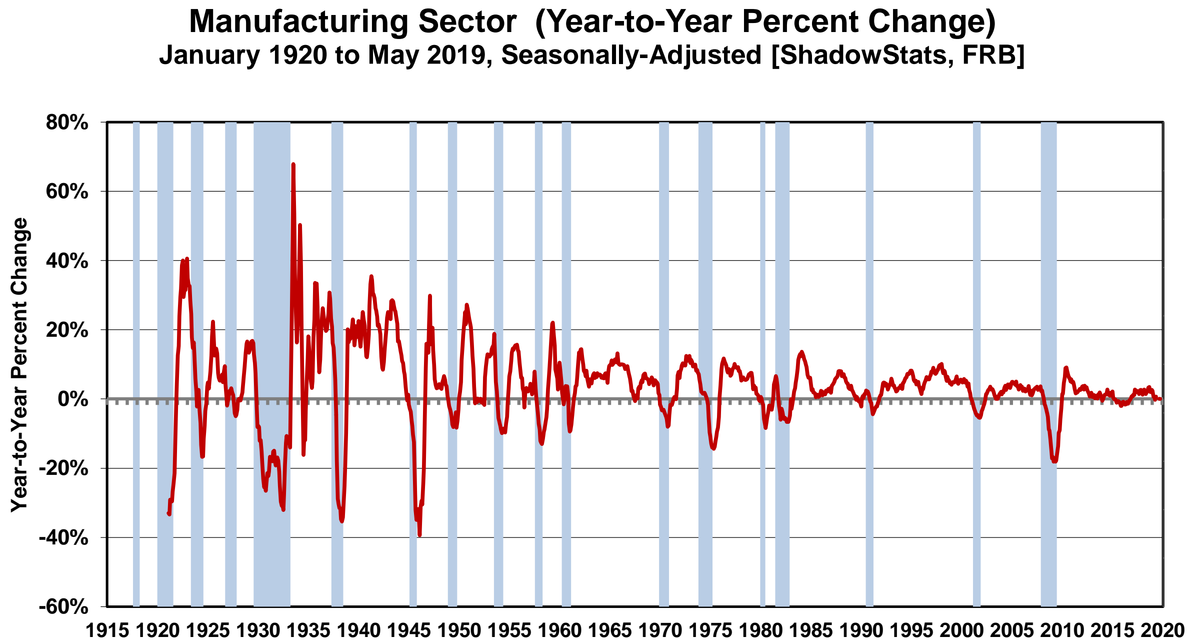
Graph 5: Manufacturing Sector, Full Historical Series, January 1919 to May 2019



Graph 6: Manufacturing Sector, Full Historical Series, Year-to-Year Percent Change, January 1920 to May 2019



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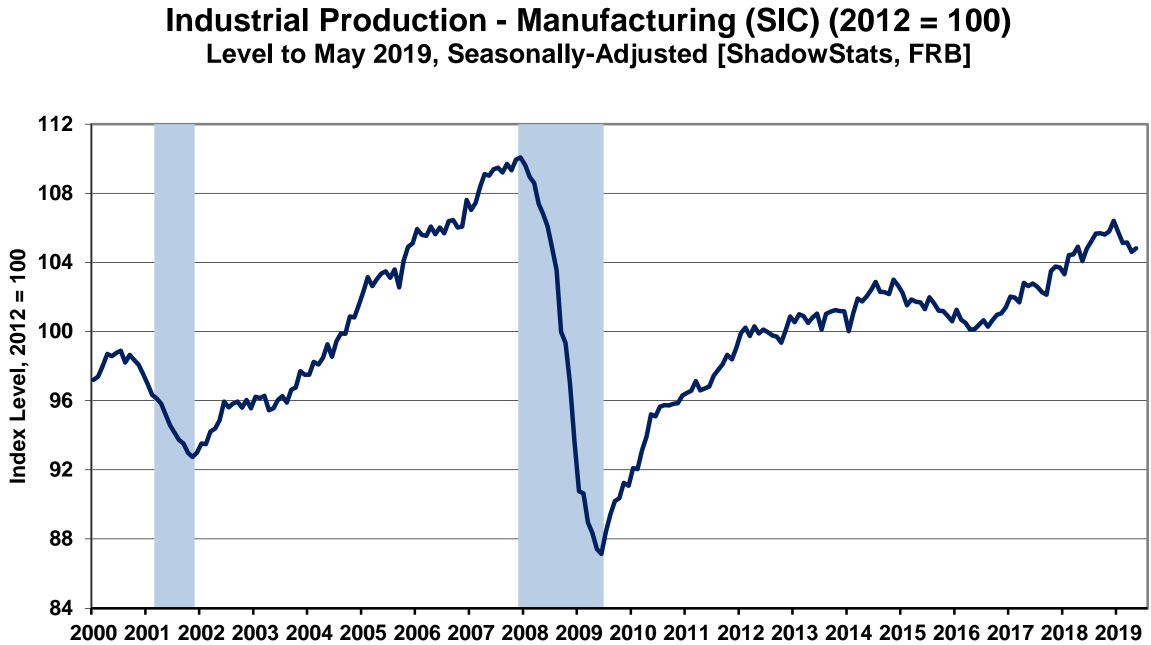
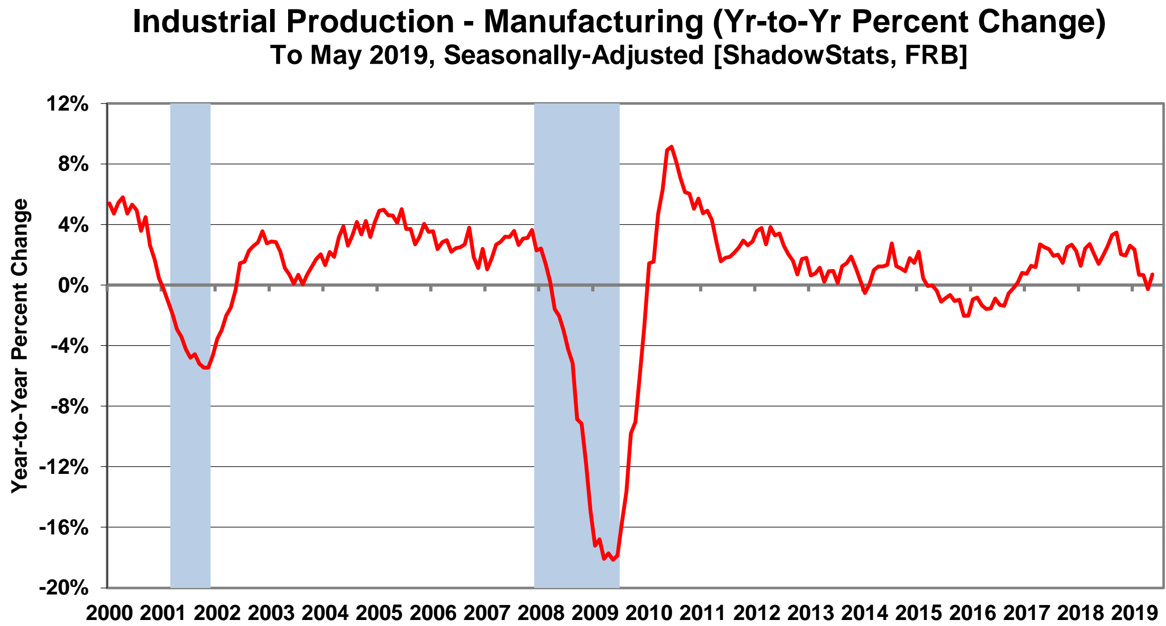
Graph 7: Industrial Production – Manufacturing , January 2000 to May 2019



Graph 8: Manufacturing, Year-to-Year Percent Change, January 2000 to May 2019



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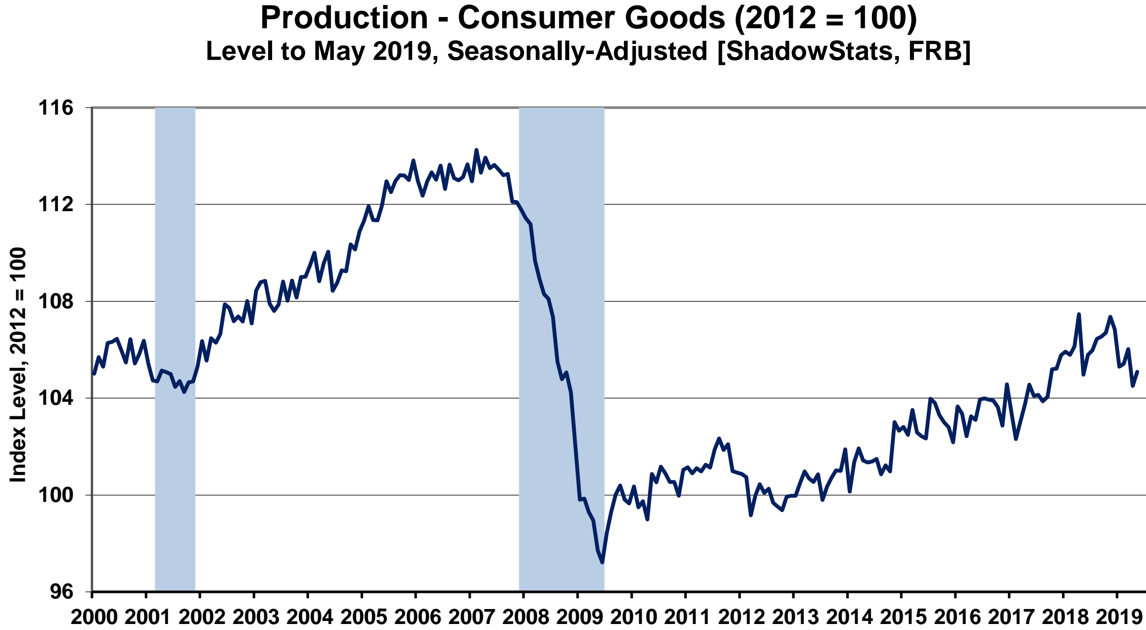
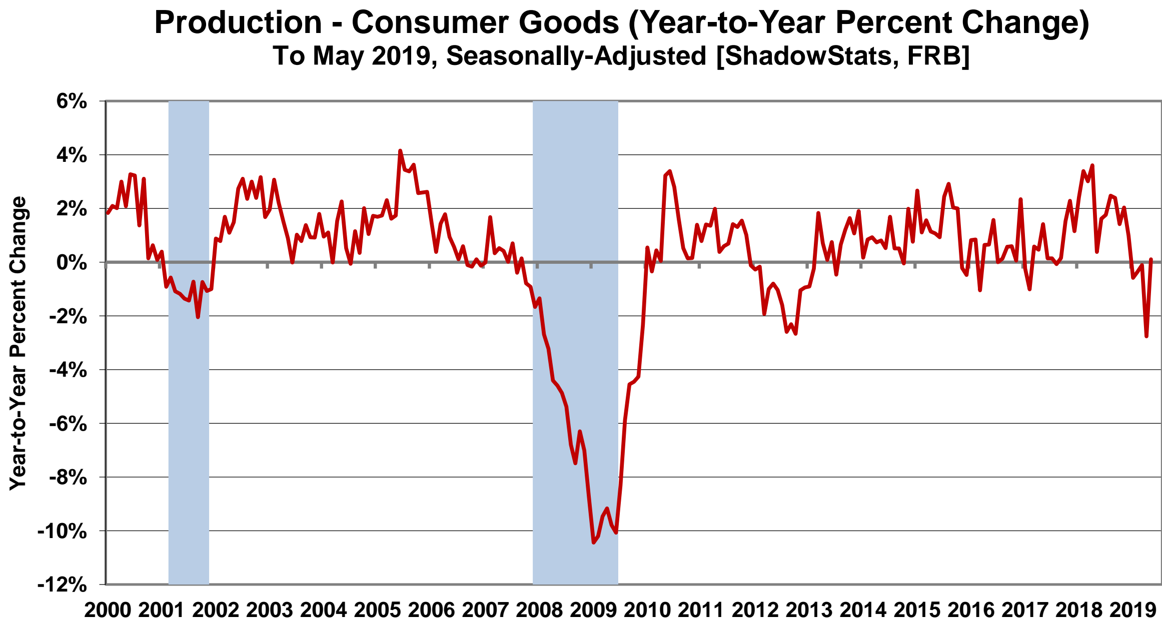
Graph 9: Manufacturing, Consumer Goods Production, January 2000 to May 2019



Graph 10: Consumer Goods Production, Year-to-Year Percent Change, January 2000 to May 2019



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Retail Sales Series Likely Still Encompasses Bad Data, June 25th Benchmarking at Hand

Nominal May 2019 Retail Sales Gained 0.55% on Top of Upside Revisions. Real Retail Sales Was on Track for a Second-Quarter 2019 Quarterly Gain, Following Two Consecutive Quarterly Contractions, Subject to Likely Downside Revisions Pending in the June 25th Benchmarking. The nominal May 2019 monthly gain of 0.55% (0.5% rounded), followed a sharply revised gain of 0.29% [previously a decline of 0.19% (-0.19%)] in April, and a revised monthly gain of 1.76% [previously 1.68%] in March 2019, as reported by the Census Bureau on June 14th. Despite the broad upside monthly revisions to April and March 2019 reporting, the back-to-back quarterly contractions in fourth-quarter 2018 and first-quarter 2019 Real Retail Sales remained intact, the first consecutive quarterly downturns seen since the Great Recession. That said, although the varied reporting encompasses different elements of the series, Retail Sales payrolls, which excludes restaurants, plunged month-to-month and year-to-year in May 2019, as discussed shortly.

Net of CPI-U inflation, as tallied regularly by the St. Louis Fed, real monthly sales in May gained 0.47%, versus a revised decline of 0.03% (-0.03%) [previously 0.51% (-0.51%)] in April, having gained a revised 1.34% [previously 1.27%] in March. Despite year-ago downside revisions, year-to-year real growth slowed to 1.33% in May 2019, down from a revised 1.69% [previously 1.10%] in April 2019 and a revised 1.94% [previously 1.87%] in March 2019. Real annual growth below 2.0% rarely is seen outside of recessions.

Discussed previously, the government shutdown disrupted the regular surveying and reporting in late 2018 and early 2019 (for example, see ***Bullet Edition No. 11***). A full *Bullet Edition* analysis of the Retail Sales series will follow tomorrow's June 25th benchmaking.

May 2019 Payrolls Showed a Zero Net Gain

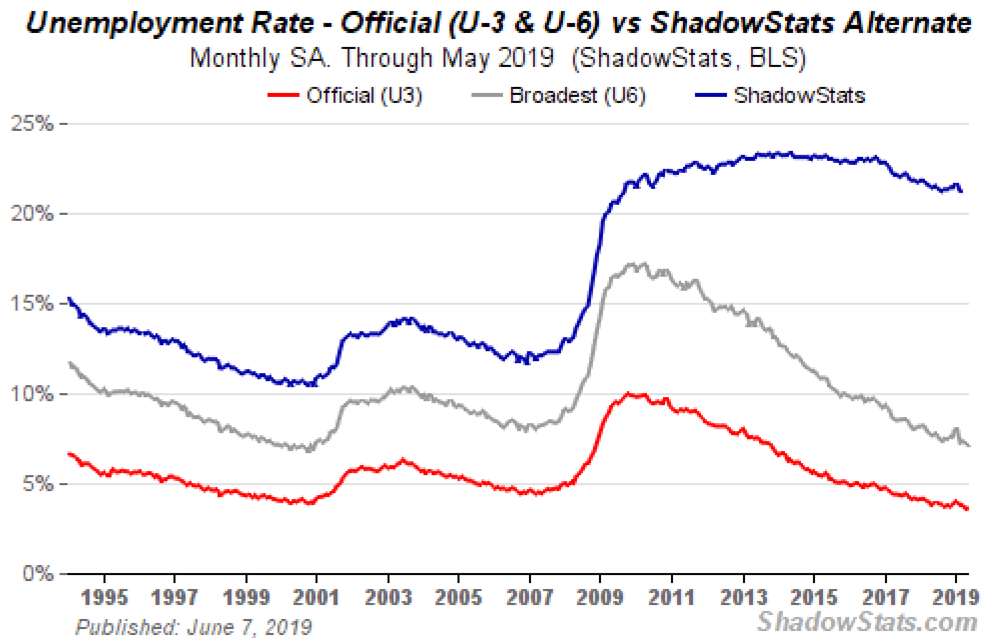
Real Earnings Are on Track for a Second-Quarter 2019 Quarterly Contraction

New Recession Continues to Roll Out, With May 2019 Monthly Payrolls Unchanged at a Zero Net Gain; Full-Time Employment Dropped for a Third Straight Month, With Annual Growth of 0.9% the Weakest Since October 2013. Disastrous May 2019 Payrolls and Employment numbers were consistent with an unfolding recession, as reported by the Bureau of Labor Statistics on June 7th. Headline May 2019 U.3 Unemployment notched negligibly higher at the second-decimal point, to 3.62%, from its 49-year low of 3.58% in April.

Yet, still running counter to the historically low headline unemployment rate, Labor–Market Stress levels (Employment-Population Ratio and the Participation Rate) held at seven-month highs (see *Graphs 17* and *18*). Under normal economic circumstances, high levels of employment stress usually are consistent with high levels of unemployment, not near-record low unemployment. As seen in the comparative inverted-scale *Graphs 19* and *20* of the headline U.3 unemployment rate and the ShadowStats Alternate measure.

Broader U.6 Unemployment eased to 7.09% in May 2019, from 7.26% in April (it includes those marginally attached to the labor force and those working part-time for economic reasons). On top of U.6, the ShadowStats Alternate Unemployment Estimate, including long-term displaced/discouraged workers not counted by the BLS, notched lower to 21.1%, having held at 21.2% for the three prior months (see *Graph 11*).

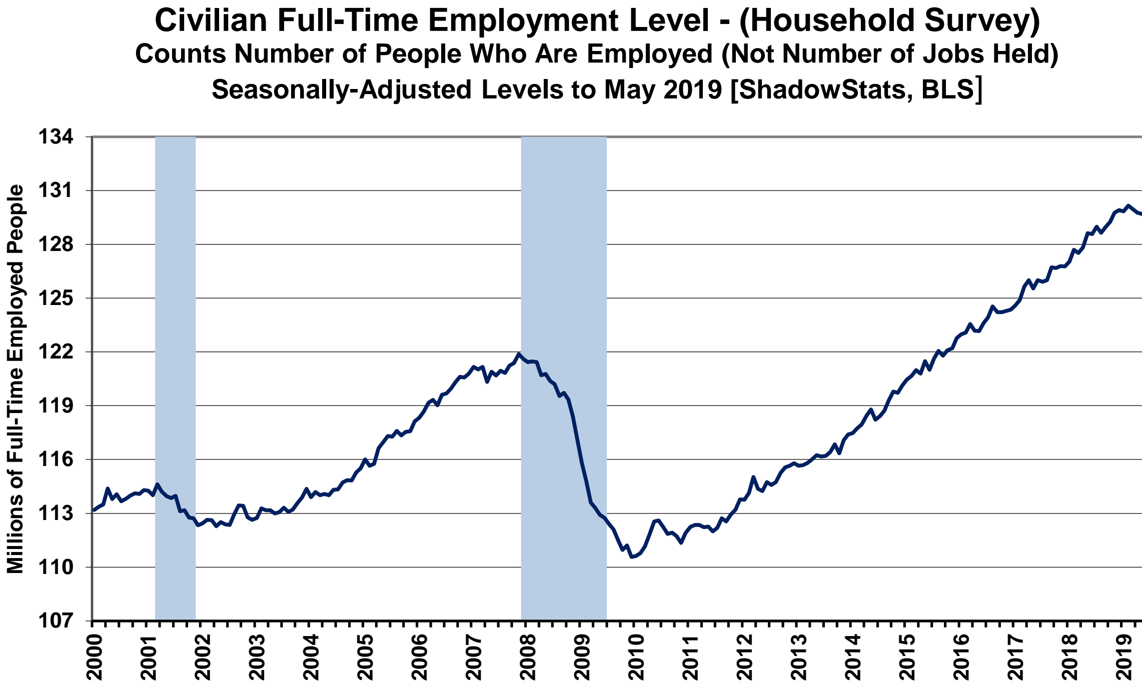
Graph 11: Unemployment Rates U.3 and U.6 vs. ShadowStats Alternate Unemployment, Jan 1994 to May 2019



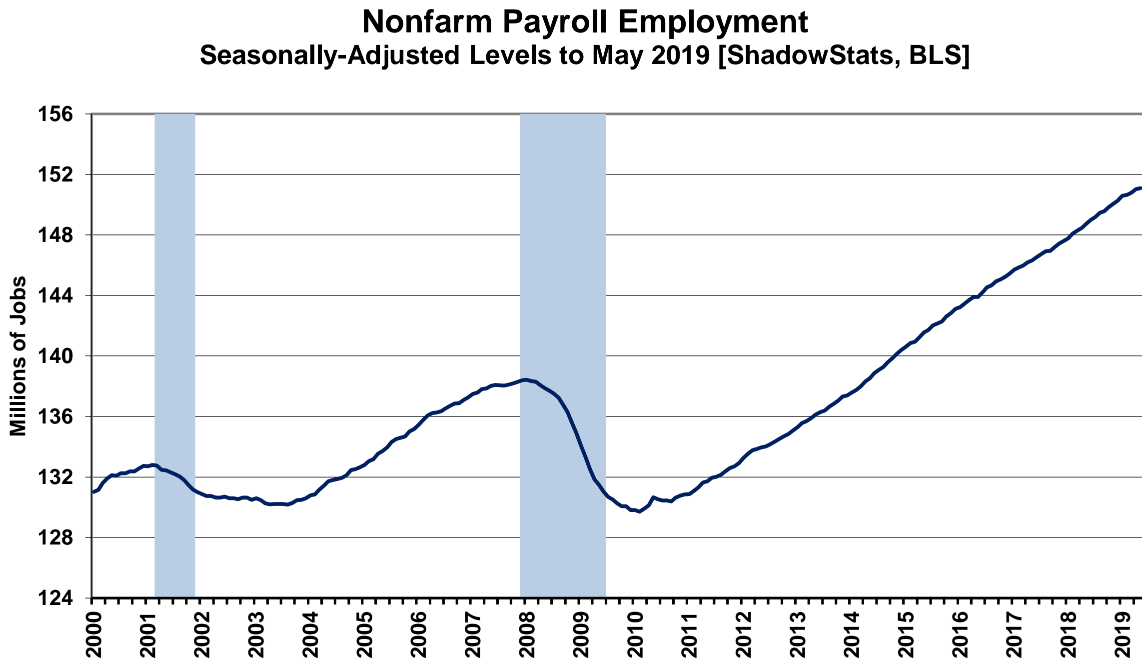
Further, full-time employment declined month-to-month for the third straight month, with annual growth there falling to 0.86%, its lowest level since October 2013 (see *Graphs 12* and *14*). Such behavior of that series is more consistent with deteriorating economic conditions and a recession, instead of the booming, healthy employment picture still touted by the Fed.

[Graphs 12 to 15 begin on the next page.]

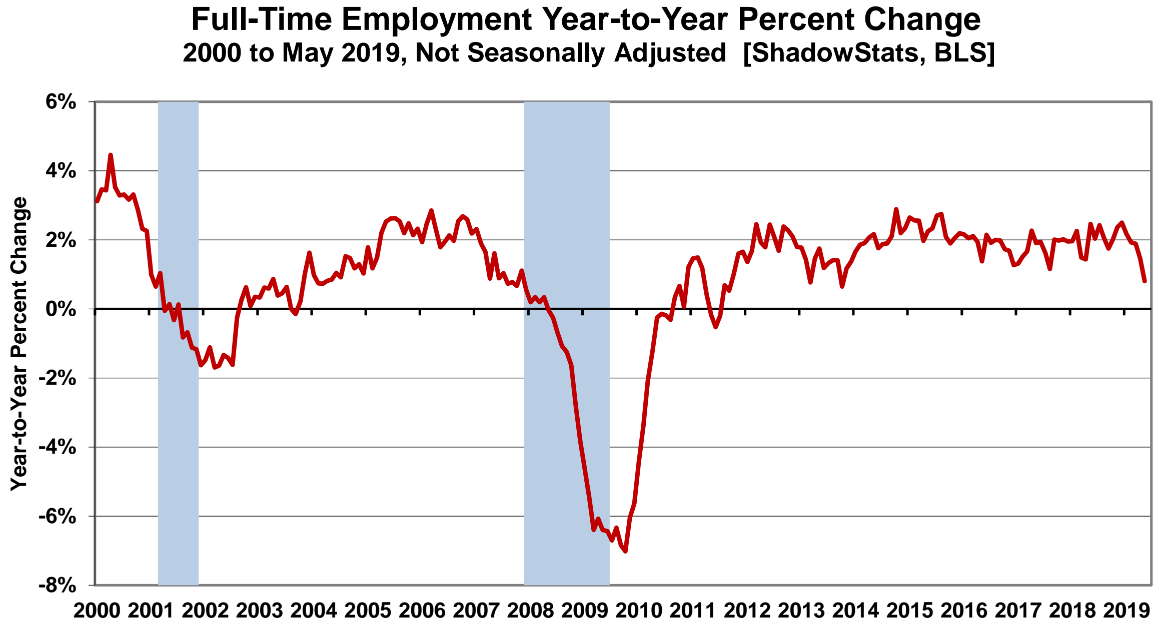
Graph 12: Full-Time Employment, January 2000 to May 2019



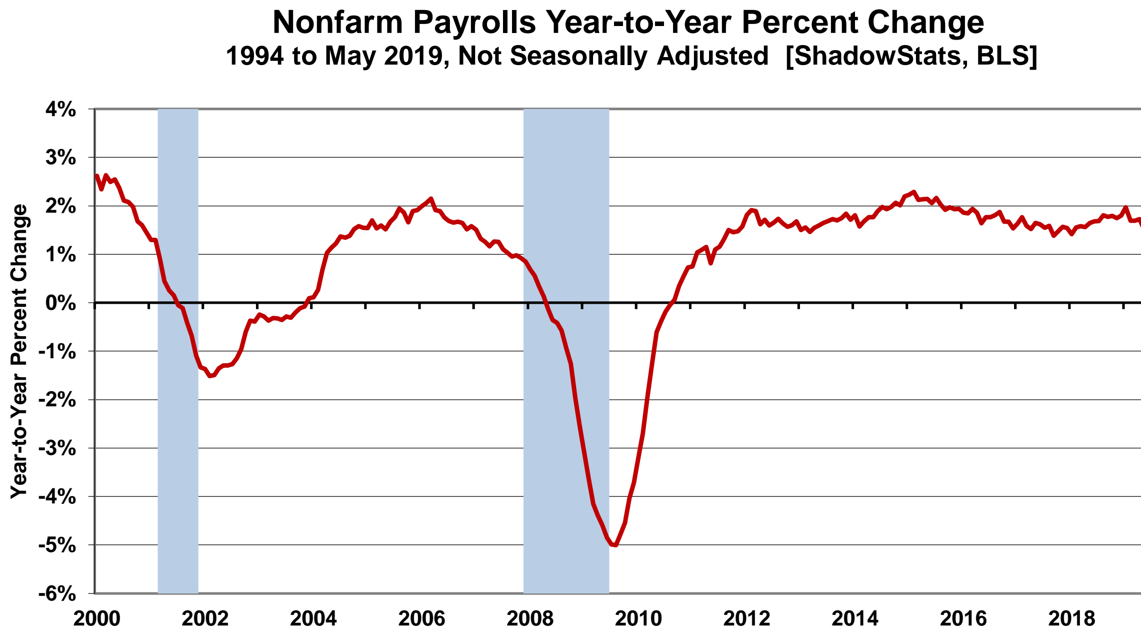
Graph 13: Nonfarm Payroll Employment, January 2000 to May 2019



Graph 14: Full-Time Employment, Year-to-Year Percent Change, January 2000 to May 2019

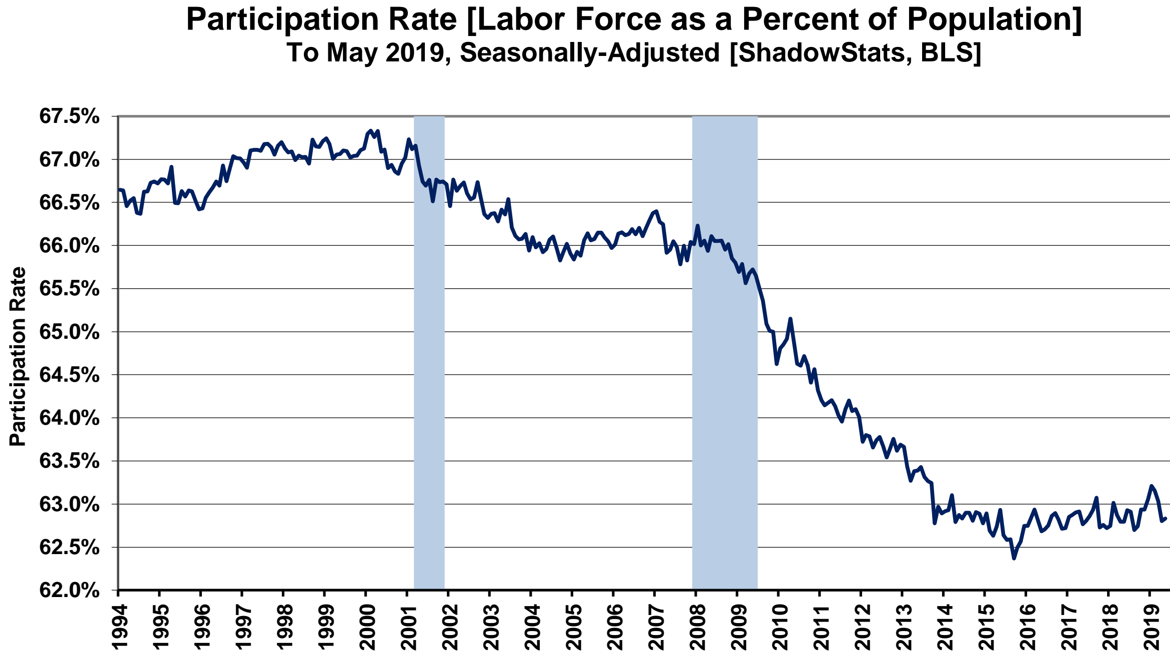


Graph 15: Nonfarm Payroll Employment, Year-to-Year Percent Change, January 2000 to May 2019

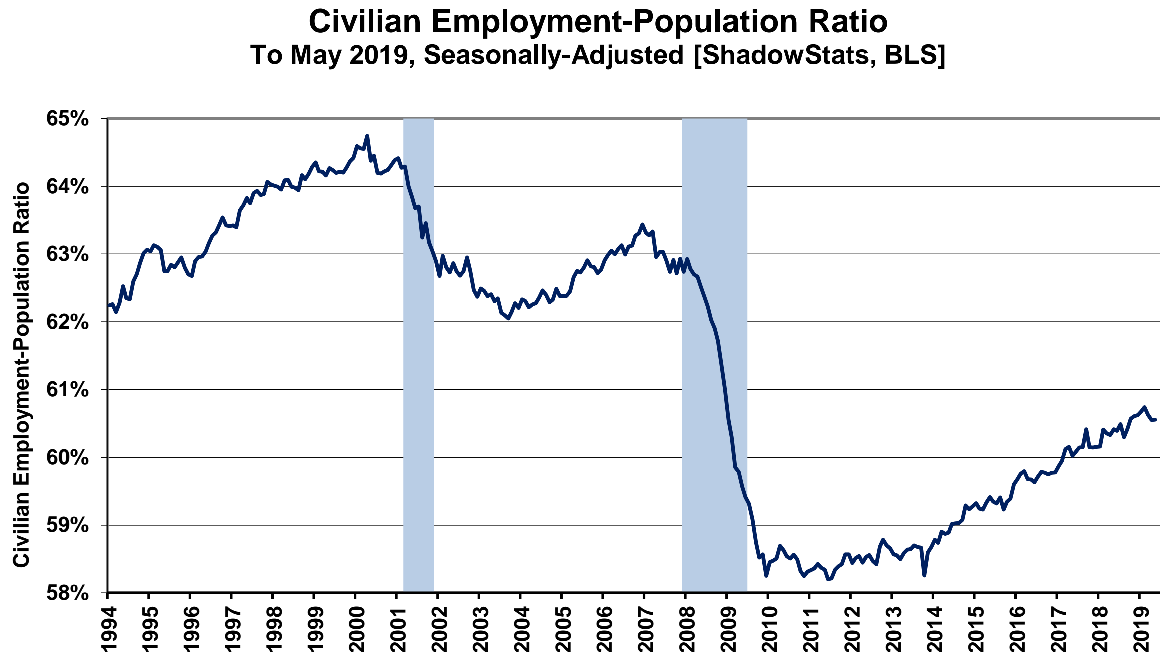


Labor Market Stress Continued at Levels Consistent With the Depths of a Recession, Not at Near-Record Low Headline Unemployment Levels

Graph 16: Participation Rate - Labor Force as a Percent of Population, January 1994 to May 2019



Graph 17: Civilian Employment-Population Ratio, January 1994 to May 2019



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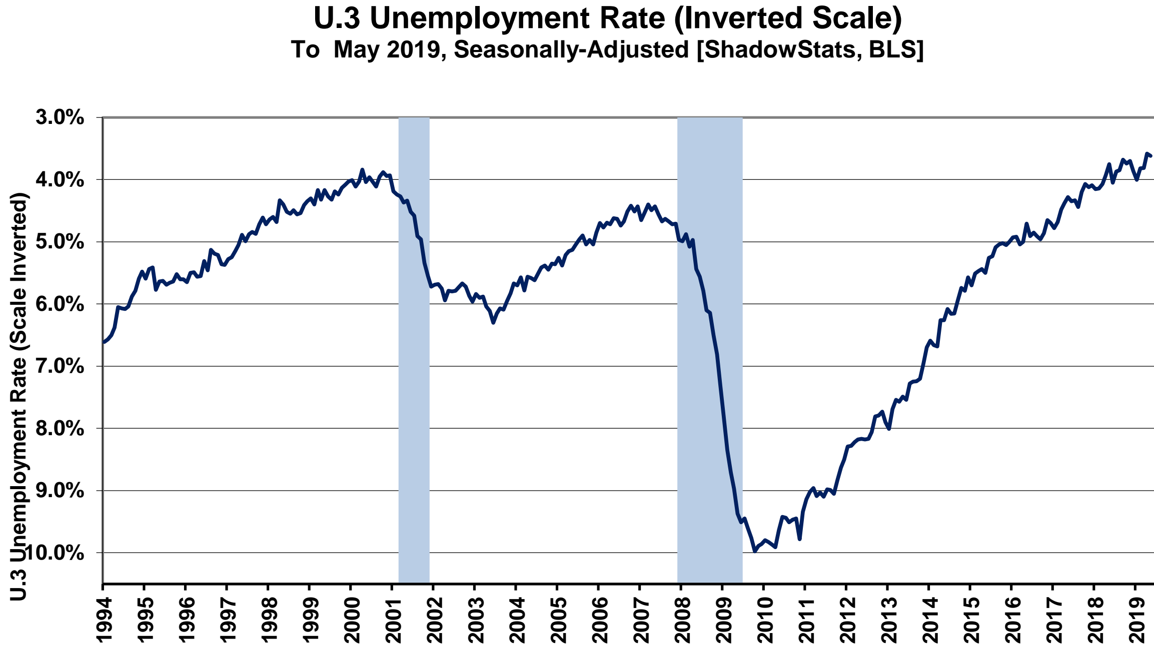
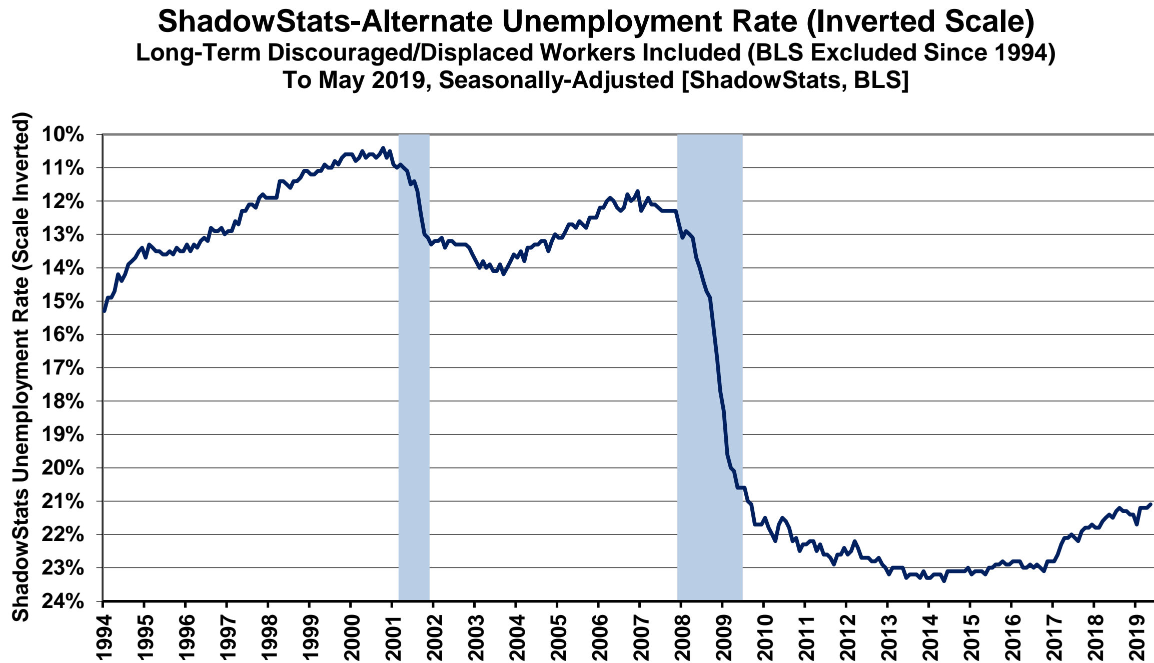
Graph 18: Headline U.3 Unemployment Rate, Inverted Scale, January 1994 to May 2019



Graph 19: ShadowStats-Alternate Unemployment Rate, Inverted Scale, January 1994 to May 2019



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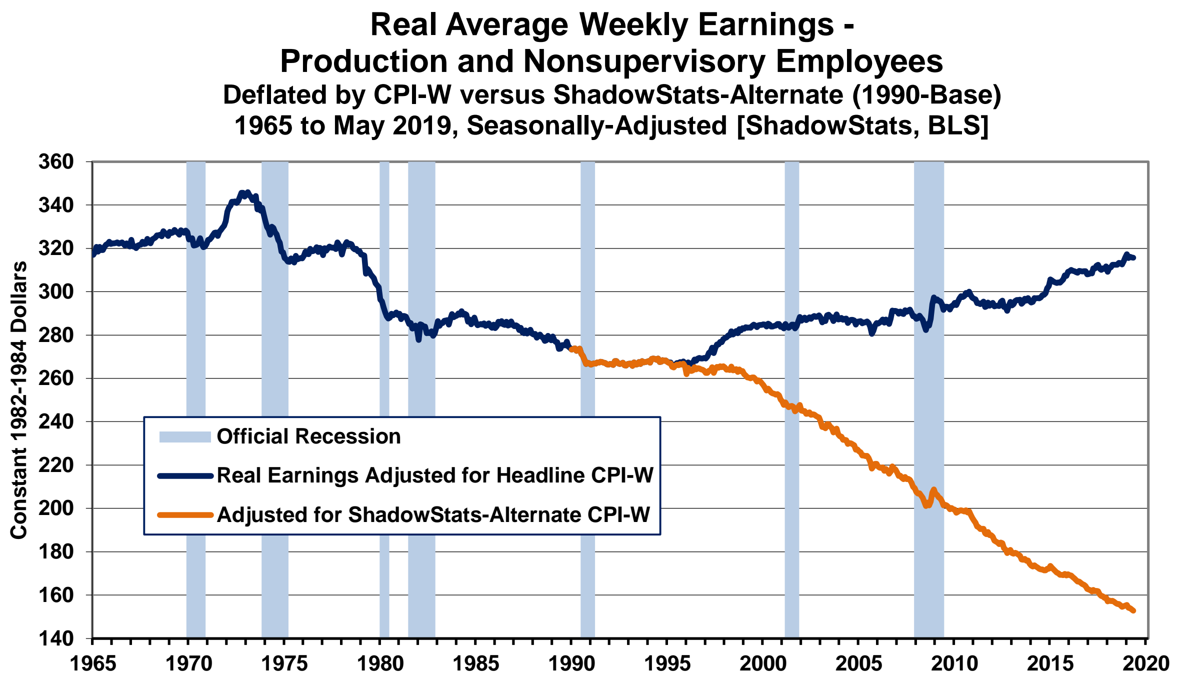
Real Average Weekly Earnings Are on Track for a Second-Quarter 2019 Quarterly Decline. Based on Payroll Employment reporting and the CPI-U/CPI-W, headline Real Average Weekly Earnings for all employees on private nonfarm payrolls rose by 0.14% month-to-month in May 2019, having declined 0.39% (-0.39%) in April, while weekly earnings for production and nonsupervisory employees declined by 0.03% (-0.03%) in May and by 0.09% (-0.09%) in April. Both series were on track for second-quarter 2019 annualized contractions, respectively of 1.25% (-1.25%) and 0.70% (-0.70%), suggestive of a downturn in broad economic activity. *Graph 20* reflects the headline numbers, as well as the ShadowStats Alternate estimate, based on inflation adjusted for government reporting gimmicks since 1990 (see *Consumer Liquidity Watch No. 5 – Special Edition*). Complicating the aggregate earnings outlook, May 2019 Payrolls showed zero month-to-month gain, net of revisions.

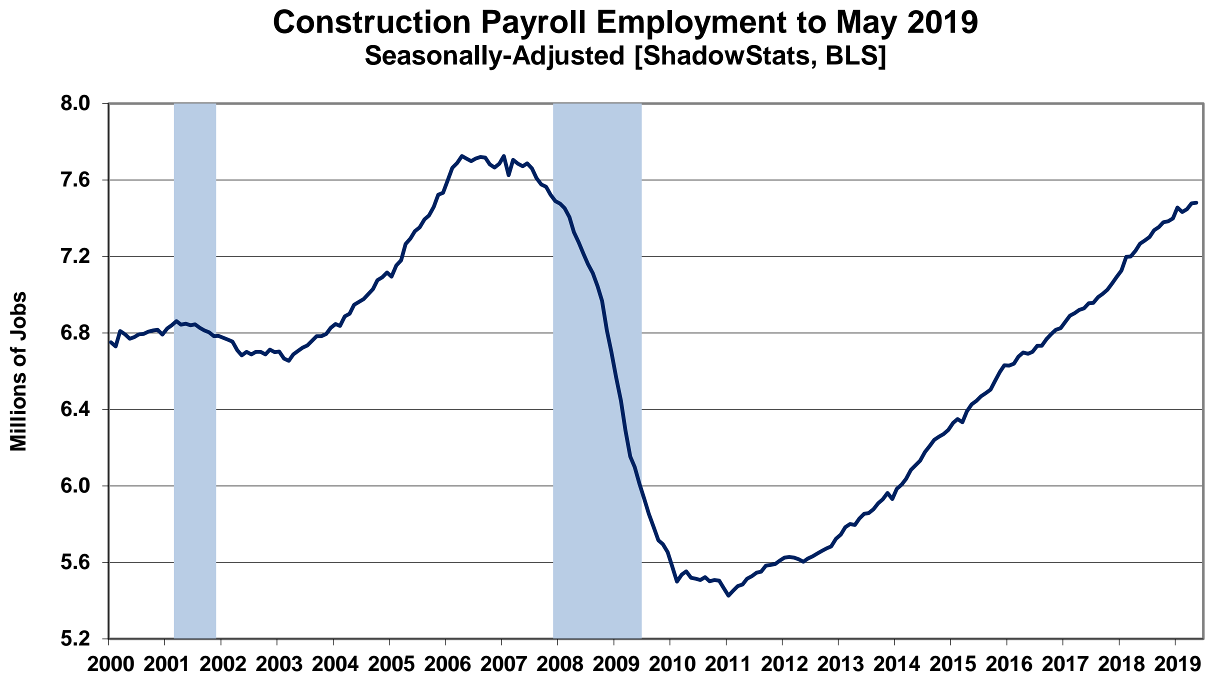
Graph 20: Real Average Weekly Earnings, 1965 to May 2019



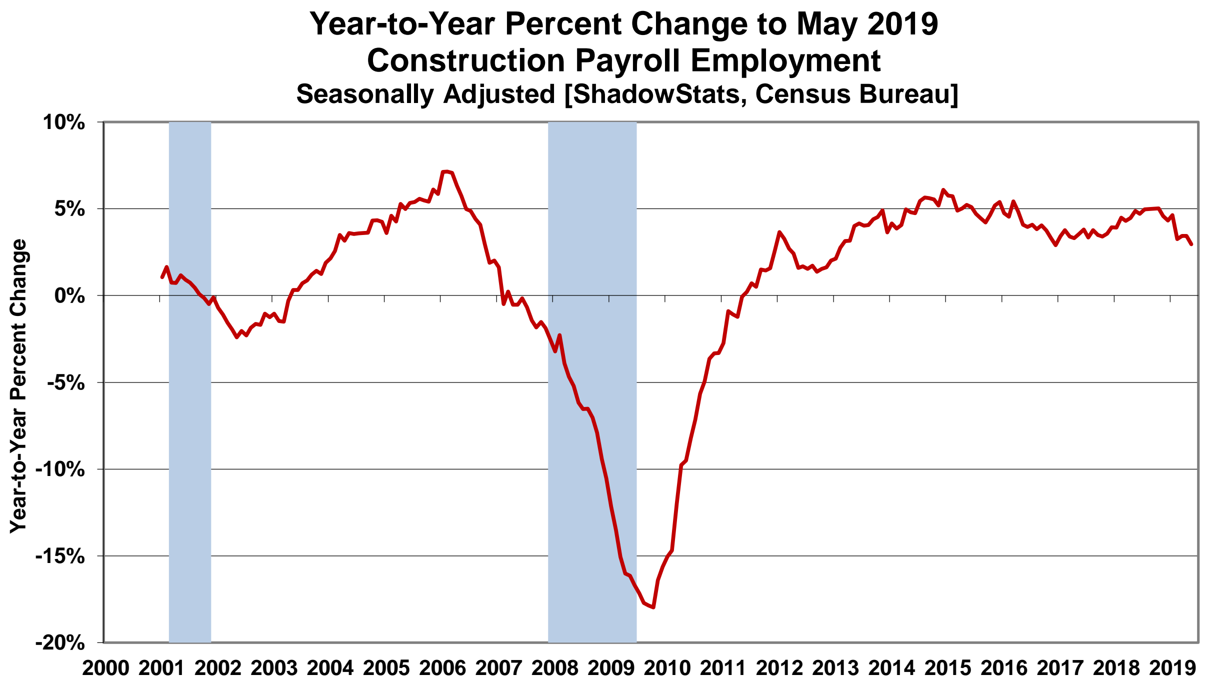
May 2019 Payroll Employment Growth Ground to a Halt. May payrolls rose by a much weaker than expected headline 75,000 jobs in May, but that entire gain came about only because April payrolls were revised lower by 75,000 (-75,000), on top of downside revisions to March payrolls. Month-to-month payroll growth was zero, net of revisions. The annual percentage gain in unadjusted May 2019 payrolls dropped to 1.52%, its lowest reading since 1.42% in January of 2018 (see *Graphs 13* and *15*). Unlike the Household Survey of employment and unemployment, which counts an individual as "employed" only once, irrespective of how many jobs or part-time jobs held, the Payroll Survey counts only the number of jobs (part-time and full-time), irrespective of how many individuals actually are employed.

Retail Sales payrolls fell in the month by 7,600 (-7,600) [down 8,300 (-8,300) net of revisions], declining by an adjusted 75,700 (-75,700) jobs year-to-year [down by deepening 0.7% (-0.7%) year-to-year, unadjusted].

Graph 21: Construction Payroll Employment, January 2000 to May 2019



Graph 22: Construction Payroll Employment Year-to-Year Change, January 2000 to May 2019



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May Construction payrolls rose by 4,000 [dropped by 4,000 (-4,000) net of revisions], with annual growth falling to 2.77% from a revised 3.51% [previously 3.59%], its weakest showing since December 2016, otherwise 2012 (see *Graph 21*). In other key series, Manufacturing payrolls effectively were unchanged in the month, up by 3,000 [up by 1,000 net of revisions], up by a slowing, unadjusted 1.5% year-to-year. The Construction Employment level in May 2019 remained 3.2% (-3.2%) [previously 3.1% (-3.1%) shy of ever recovering its pre-recession peak activity.

April 2019 Nominal Construction Spending Dropped 1.2% (-1.2%) Year-to-Year

Other Than for February, Last Time That Happened Was the Onset of the Great Recession

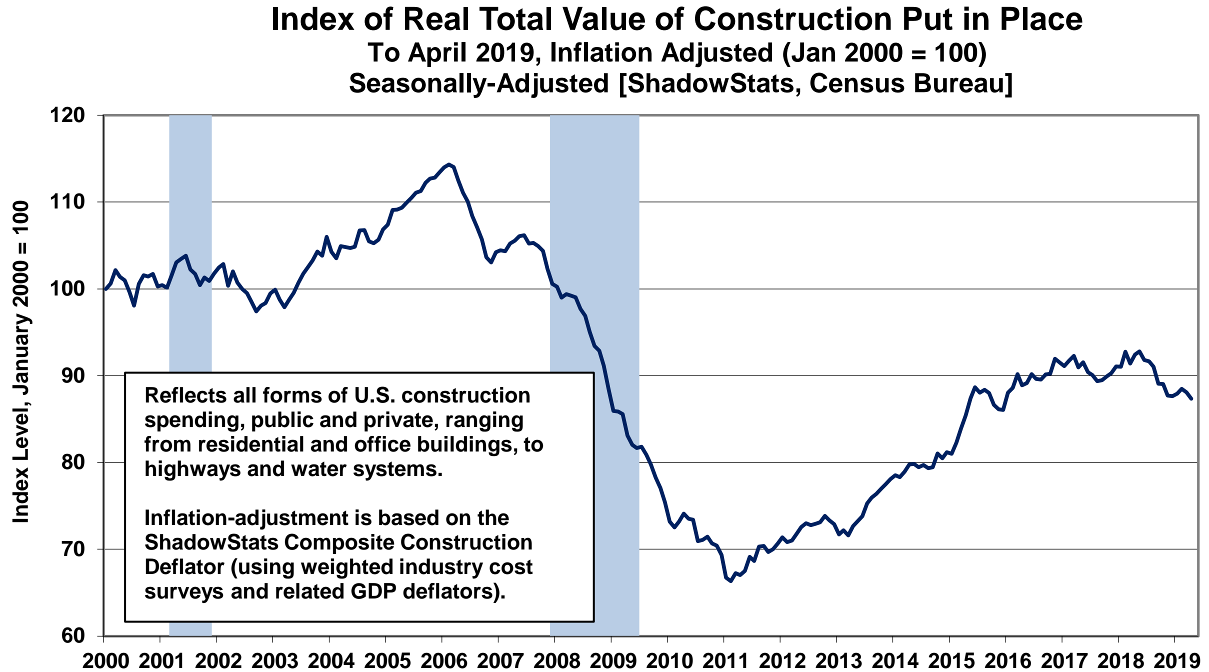
Real Spending Is on Track for Its Fourth Consecutive Quarter-to-Quarter Contraction

April Construction Spending Continued Signaling Recession. Nominal Growth Held "Unchanged" at 0.0% Month-to-Month, on Top of Upside Revisions to March and February, but Fell Year-to-Year by 1.2% (-1.2%). Annual change in nominal April Construction Spending showed a 1.2% (-1.2%) decline, holding below 1.0% for the fourth straight month, as reported by the Census Bureau on June 3rd. Monthly nominal annual growth has continued fluctuating around 0.0% despite upside revisions to February and March activity. Nominal year-to-year growth in monthly aggregate spending dropped below 1.0%, to 0.7% in January 2019. The last time nominal annual growth in Construction Spending dropped below 1.0% in a month was in December 2007, in advance of the January 2008 formal onset of the Great Recession. Annual nominal growth in February 2019 dropped by a revised 0.6% (-0.6%) [previously 0.9% (-0.9%)], March 2019 revised annual activity was a gain of 0.5% [previously a contraction of 0.8% (-0.8%)], again with April 2019 in annual decline of 1.2% (-1.2%).

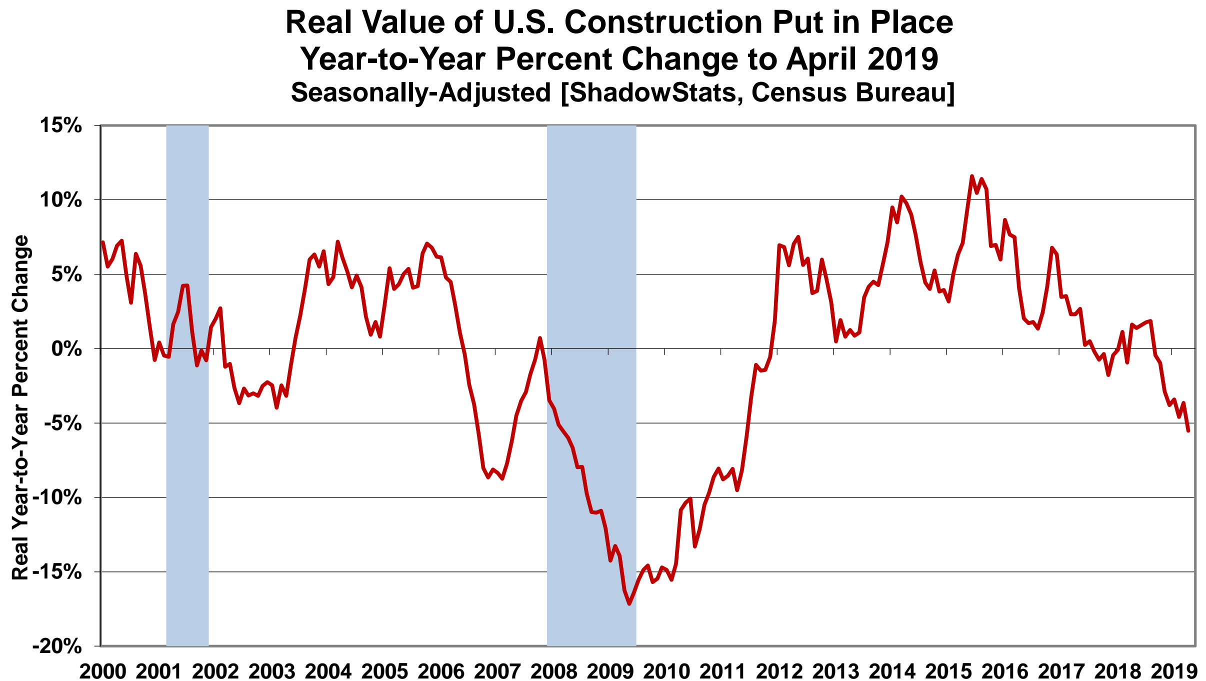
Nominal month-to-month aggregate Construction Spending, again was unchanged at a rounded 0.0% [down by 0.05% (-0.05%) at the second decimal point], versus a revised 0.1% (0.10%) gain [previously down by 0.86% (-0.86%)] in March and a revised gain of 1.0% (1.02%) [previously 0.68%] in February. Given minimal mixed revisions to February and March Residential Construction activity, and with an intensified downturn there in April, Private Construction dropped by 1.8% (-1.8%) in the month. In contrast, Public Construction jumped by 4.8% in April, dominated by a 21.3% surge in Highway and Street Construction.

In inflation-adjusted real terms, the new headline aggregate reporting showed a year-to-year annual decline for the eighth straight month, with first-quarter 2019 activity negative quarter-to-quarter for the third consecutive quarter, and with second-quarter 2019 activity on early track for a fourth consecutive quarterly decline. Implications here are for eventual downside revisions to both fourth-quarter 2018 and first-quarter 2019 GDP, and increasingly for a second-quarter 2019 GDP contraction.

Graph 23: Index of Real Total Value of Construction Put in Place, January 2000 to April 2019



Graph 24: Year-to-Year Change in Real Construction Spending, January 2000 to April 2019



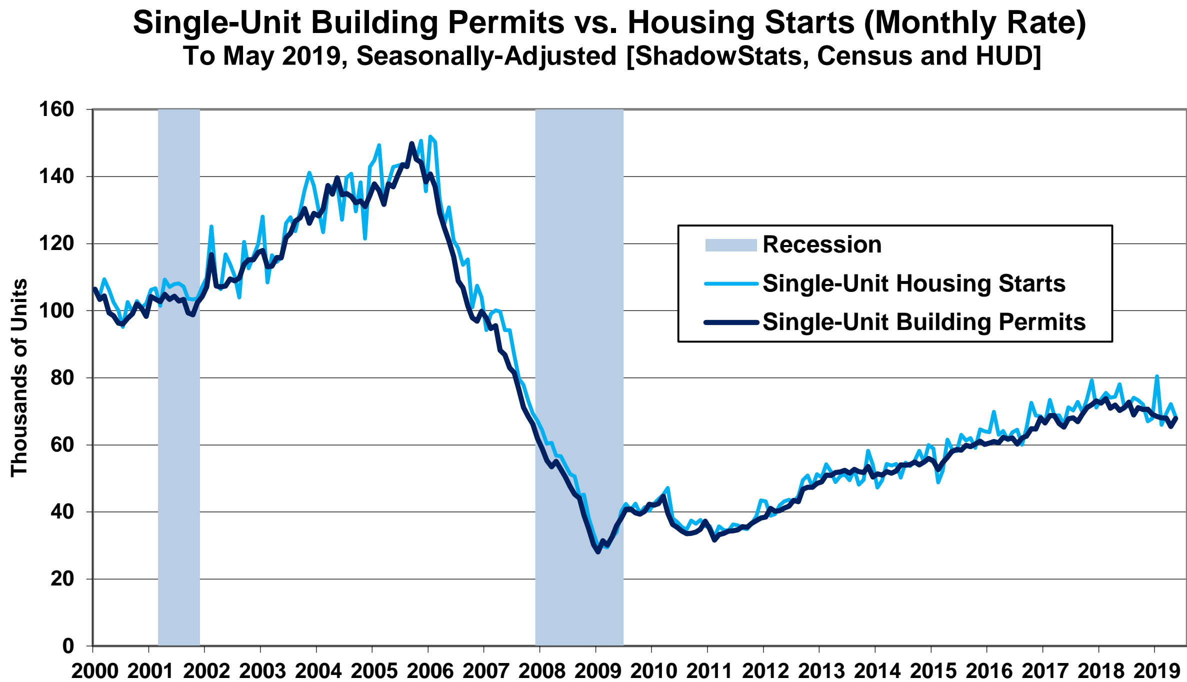
Reporting of May 2019 Single-Unit Building Permits Was Stable and Significant, as Usual, Showing Second-Quarter Activity on Track for Third Consecutive Quarterly and Annual Contractions (Census Bureau, June 18). May 2019 New Residential Construction headline Housing Starts and revisions were nonsensically volatile as usual, but the dominant and statistically meaningful Single-Unit Building Permits series held on track for its fifth-consecutive quarter-to-quarter and third-consecutive quarterly year-to-year contractions in second-quarter 2019. Broad residential construction remained strongly negative, with monthly and annual contractions in Housing Starts, on top of a 2.8% upside revision to April aggregate Starts. As usual, none of the monthly or annual changes in headline Housing Starts (as opposed to Building Permits) activity was close to being statistically significant at a 90% confidence interval, except for the significant annual decline of 12.5% (-12.5%) in the dominant Single-Unit Starts Housing Starts category.

More-stable Building Permits, which lead Housing Starts, showed a small, statistically–insignificant monthly gain of 0.3% and annual decline of 0.5% (-0.5%). Yet the highly stable, dominant Single-Unit category, showed a statistically-significant monthly gain of 3.7% and annual decline of 3.3% (-3.3%), indicating second-quarter 2019 activity on track for a fifth-consecutive annualized quarter-to-quarter decline, down by 8.3% (-8.3%), following a first-quarter drop of 10.6%% (-10.6%), with second-quarter 2019 also on track for a third consecutive quarterly year-to-year decline, down by 6.2% (-6.2%), following an unrevised annual decline of 5.9% (-5.9%) in first-quarter 2019 (see *Graphs 25* and *26*).

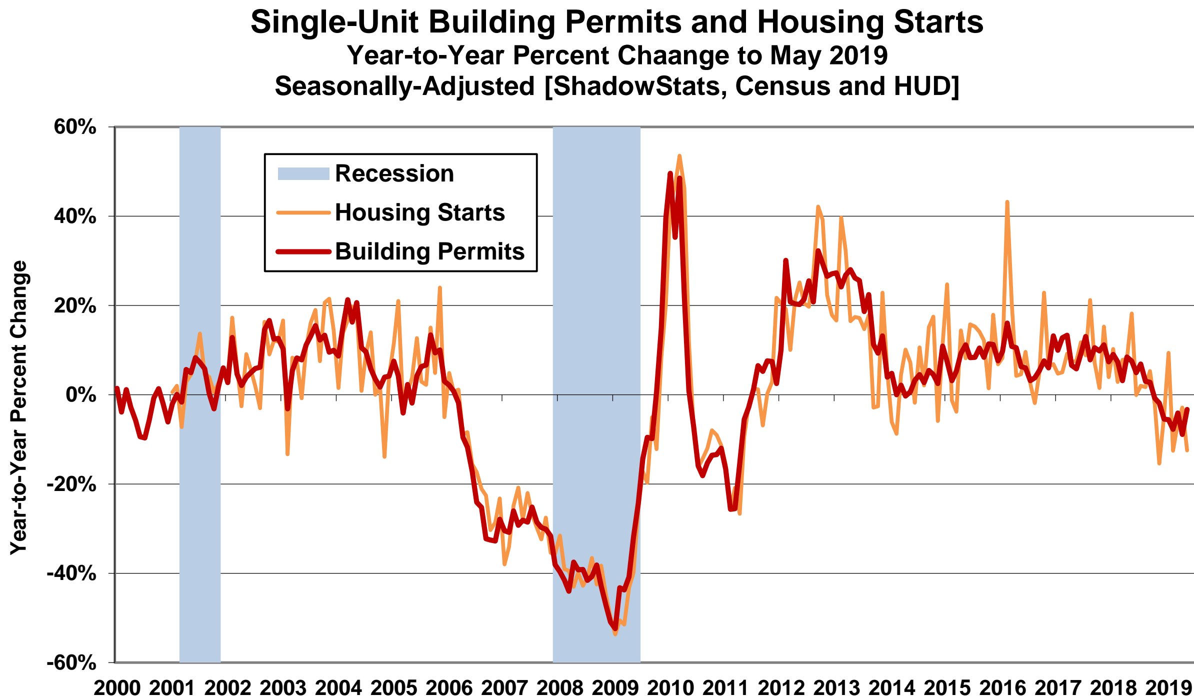
Reflected in *Graphs 27* and *28*, irrespective of month-to-month reporting volatility and instabilities, not only has the headline Housing Starts series not recovered its current pre-recession peak, it has not recovered any of its other post-World War II pre-recession peaks.

[Graphs 25 to 28 of Single-Unit Building Permits and Housing Starts begin on the next page.]

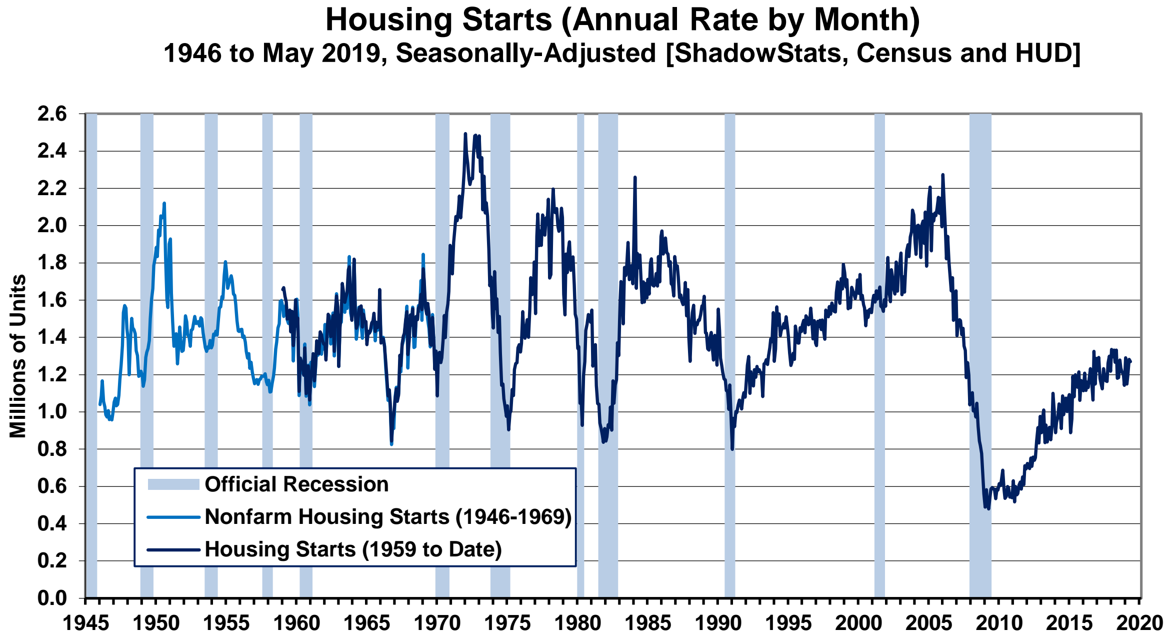
Graph 25: U.S. Single-Unit Building Permits/Housing Starts, January 2000 to May 2019



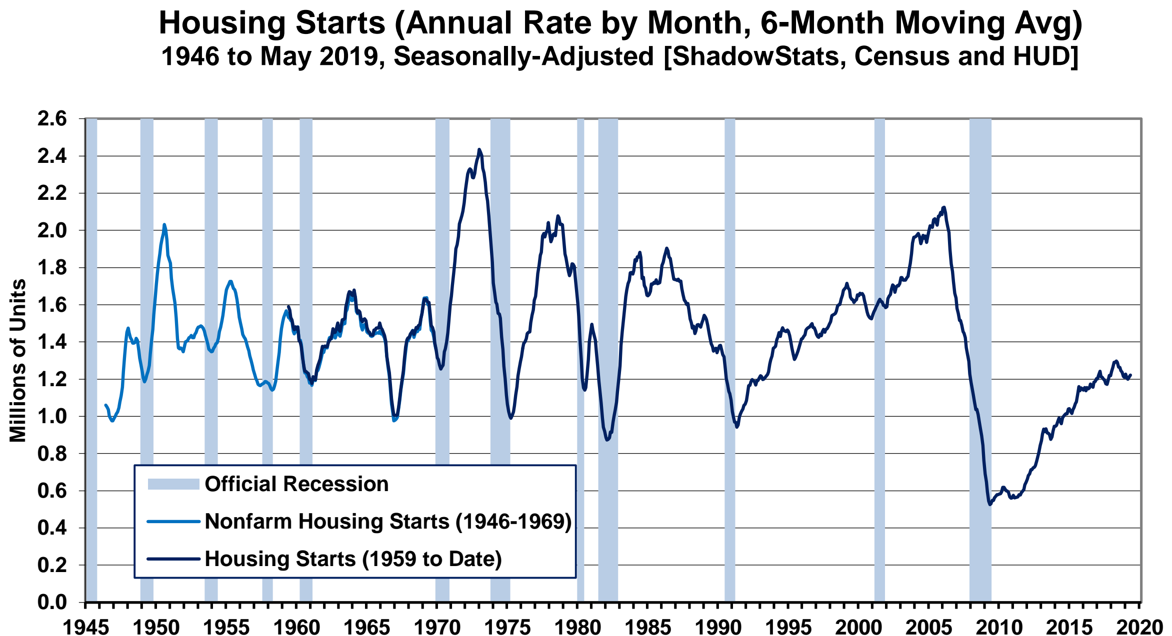
Graph 26: U.S. Single-Unit Building Permits/Housing Starts, Year-to-Year Change, January 2000 to May 2019



Graph 27: Housing Starts, Annual Rate by Month, 1946 to May 2019



Graph 28: Housing Starts, Six-Month Moving Average of Annual Rate by Month, 1946 to May 2019



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SECTION 2 - FINANCIAL MARKET IMPLICATIONS

Weakening Economy and Fed Easing Should Hit Stocks and the Dollar, but Boost Gold

Watch for Heavy Selling of the U.S. Dollar and a Sharp Rally in Gold Prices

The Dollar and Gold Serve as the Canary in the Coal Mine for Stocks and Bonds

With Stock Market Selling, Dollar Turmoil and Rising Inflation Ahead, Holding Physical Gold and Silver Provides a Hedge, Protecting the Long-Term Purchasing Power of One's Wealth and Assets. What had become a fundamental disconnection between happy hype in the media and FOMC as to a rapidly expanding, healthy U.S. economy, and the underlying reality of a "new" economic downturn on top of a meaningful portion of U.S. economic activity that never fully recovered its pre-Great Recession 2007 peak, has dissipated. The markets have begun to recognize both a new unfolding recession and an underlying systemic weakness that never was worked out of the Great Recession. Severe enough market disruptions and mounting U.S. dollar concerns actually could begin to accelerate the global financial markets focusing on long-term U.S. sovereign solvency issues, which would tend to accelerate dollar selling, domestic U.S. inflation and the flight of assets / cash into gold and silver. With mounting negative economic news of the couple of months, which increased speculation and expectations of a likely Federal Reserve easing—not renewed tightening—the markets increasingly have fled the U.S. dollar for the long-term, store-of-wealth stability of physical gold and silver.

FOMC "Hints" Rallied Stocks, but Gold Rallied Even More and the Dollar Sold Off Even More. Consider recent market activity in response to the June 19th FOMC meeting and the subsequent press conference of Fed Chairman Powell. He indicated that FOMC members were concerned about the economy and would ease if necessary. In response, with no overt action taken by the FOMC, the price of gold jumped by 1.02%, silver by 1.22% and the U.S. Dollar Index declined by 0.43% [all per the *Wall Street Journal* quotes]. At the same time, the Dow Jones Industrial Average was up by 0.15% on the day, post press conference. As the stock market rallied amidst the hoopla of a "hinted" later easing, stocks hit new highs into Friday, June 21st, with the closing Friday numbers showing the Dow Jones Industrial Average (DJIA) and the S&P 500 up respectively by 1.0% and 1.2% from their pre-FOMC closing prices on Tuesday, June 18th. In contrast, Gold was up by 3.8%, and the U.S. dollar was down against the Swiss Franc by 2.4% (-2.4%), or restated, the CHF was up against the dollar by 2.5%.

The point is that for investors living outside the U.S. dollar, their holdings of U.S. equities likely dropped in value last week, despite the dollar-based headline stock index gains. Traditionally, recessions generate bear stock markets, reflective of weakening economic conditions, activity and declining revenues and earnings.

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Physical gold and silver remain the primary hedges—stores of wealth—for preserving the purchasing power of one's U.S. dollar assets, in the context of liquidity and portability, during the difficult times and a likely period of a weakening U.S. dollar and highly inflationary times that lie ahead.

U.S. Dollar - Intensifying Weakness Should Lie Ahead. *Graph 29* is the traditional ShadowStats Gold Price graph versus the Swiss Franc (USD/CHF). *Graphs 30* to *33* plot Gold versus Silver, Gold versus Oil, and the Financial- versus Trade-Weighted U.S. Dollar.

Gold versus Stocks. *Graphs 34* and *35* show plots of the price level of the S&P 500 Total Return Index (all dividends reinvested) versus the price of physical Gold, with both series indexed to January 2000 = 100. The first plot shows both series in nominal terms, before inflation adjustment, and a second plot in real, inflation-adjusted terms, deflated by the headline CPI-U. While Gold has outperformed the S&P 500 since the beginning of millennium, it is interesting to note that the S&P 500, net of headline CPI inflation, did not break above parity until 2013. Where the S&P had been closing the gap with Gold, Gold recently has picked up the edge anew, in the wake of the deteriorating outlook for the U.S. dollar and economy. The final price points in the graphs reflect the closing or late-day New York quotes of June 21, 2019.

Prices of Gold and Silver—Remain the Canary in the Coal Mine for the U.S. Financial Markets. Any panicked market conditions raise the risk of triggering actions and turmoil in other areas, including risks of a major run against the U.S. dollar and of triggering of intensified-inflation and eventual-hyperinflation concerns in the United States. Again, this *ALERT* updates the prior versions in ***Special Commentary No. 983-B*** and earlier. A still-waffling Federal Reserve (still formally on hold, neither tightening nor easing) faces a self-created market conundrum.

Domestic and global financial, economic and political risks continue to evolve, still deteriorating rapidly in aggregate, as somewhat hinted at in the Fed Chairman's Press Conference. The FOMC's self-conflicting position through the December 2018 meeting had developed to the point that ongoing, intensified tightening heavily threatened headline economic activity, the U.S. dollar and domestic equity markets. Where the rate hikes formally were put on hold at the March 2019 FOMC meeting, meaningful damage to the economy already had been done. Those damages will continue to play out into 2020, with a deepening downturn. At the same time, a move towards renewed easing (lowering interest rates) or quantitative easing to help the economy would pummel the U.S. dollar in the global markets, reflecting foreign and domestic flight capital out of the U.S. markets.

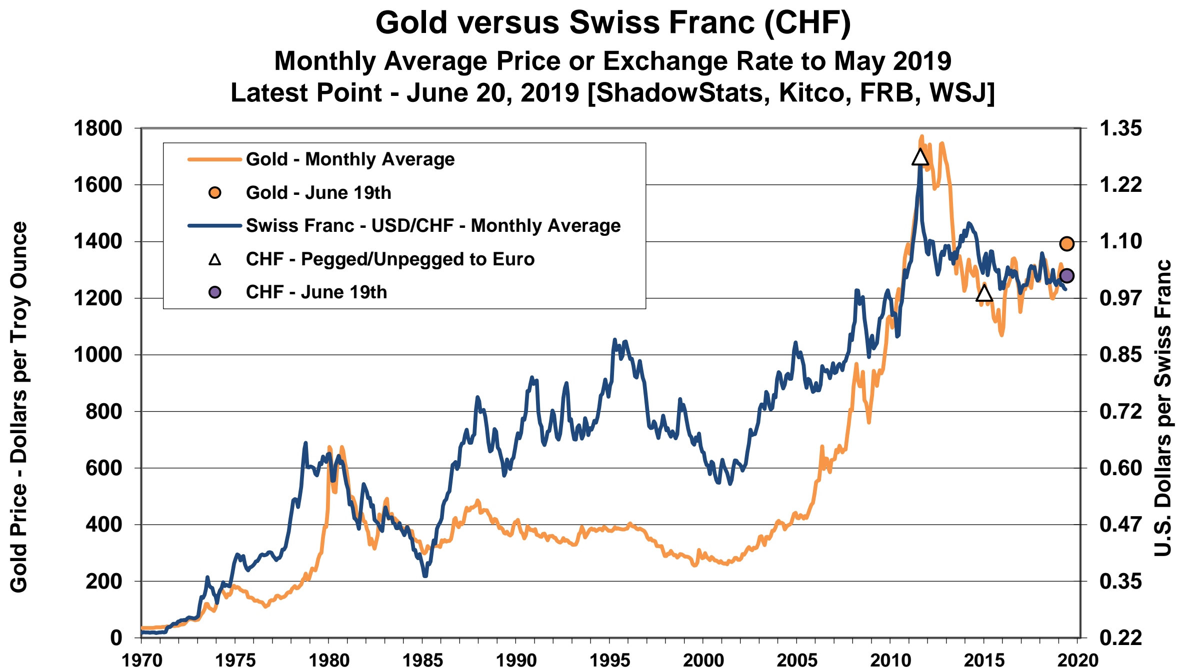
Again, the more negative the pressure on the U.S. dollar, and the stronger the flight to safety in gold, the more dangerous the situation is for domestic equity prices. A rapidly weakening U.S. Dollar and rallying gold and silver prices are solid signs of impaired equity market conditions that easily can mutate into other market distortions and investor fears. Risks are high for a major stock-market sell-off in the months ahead. Indeed, circumstances are at hand that could trigger one of the worst U.S. financial panics / systemic disruptions of the last century. Some of the involved issues have been festering for decades; others have surfaced only recently and include:

- Rapidly deteriorating, uncontained and unsustainable U.S. deficit spending and burgeoning debt levels, leading to ultimate long-range solvency issues for the U.S. Treasury and full debasement of the U.S. dollar (hyperinflation), discussed in ***SECTION 4***.

- Unresolved instabilities from actions taken by Federal Reserve and other central banks to save the U.S. and global banking system in 2008.
- Recent Federal Reserve tightening and now not tightening (not easing yet, either).
- An unfolding, formal new U.S. recession, triggered by the FOMC's tightening, but not recognized openly by the Fed, yet. The downturn, however, increasingly is gaining recognition in the financial markets.
- Exploding risks of internal political instabilities in the United States and its major U.S. trading partners and allies, including the United Kingdom. In the United States, consider the unprecedented internal hostility between Democrats and Republicans in Congress. Some of the dangerously disruptive potential of that circumstance was discussed in Commentary No. 888 of May 22, 2017.
- Mounting military tensions between the United States and Iran.
- Increasingly, overly inflated equity prices, an overvalued U.S. Dollar and undervalued precious metals.

These rapidly evolving elements have fallen into place, raising risks of extraordinary financial-market and systemic disruptions. Financial market circumstances here are reviewed from the standpoint of the U.S. Dollar and the precious metals Gold and Silver. Again, those latter areas act something like the proverbial Canary in a Coal Mine, as an early warning of serious trouble in the U.S. financial-system and/or in inflationary developments. They also remain the ultimate stores of wealth for preserving the purchasing power of one's wealth and assets.

Graph 29: Gold versus the Swiss Franc



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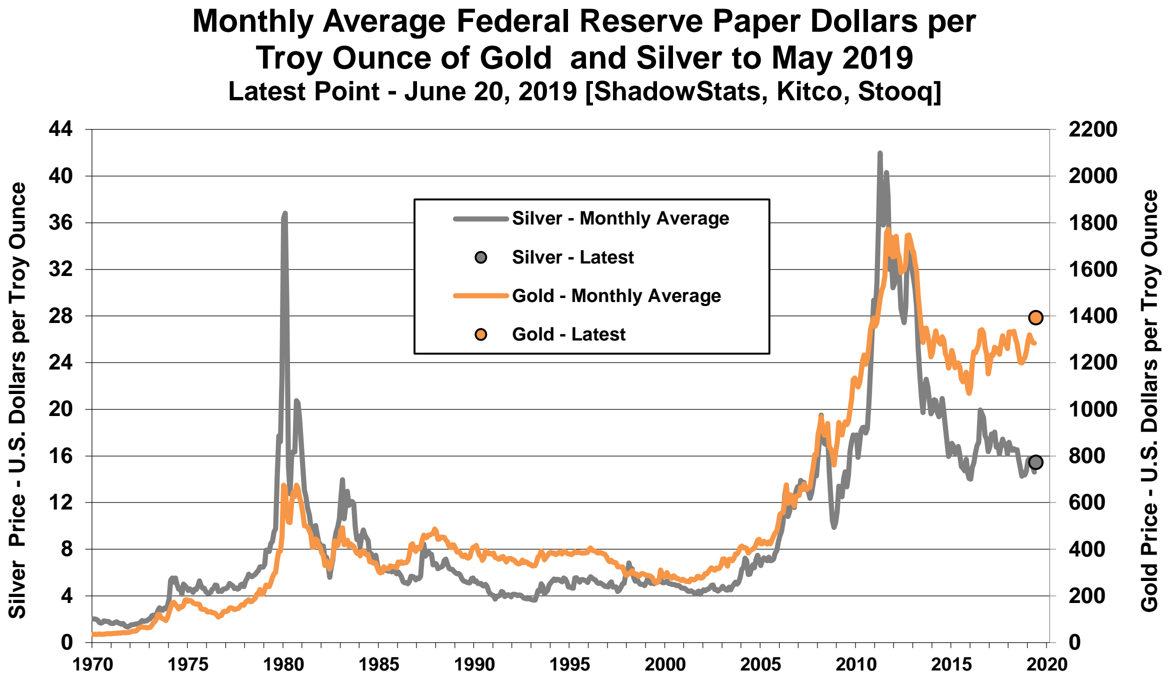
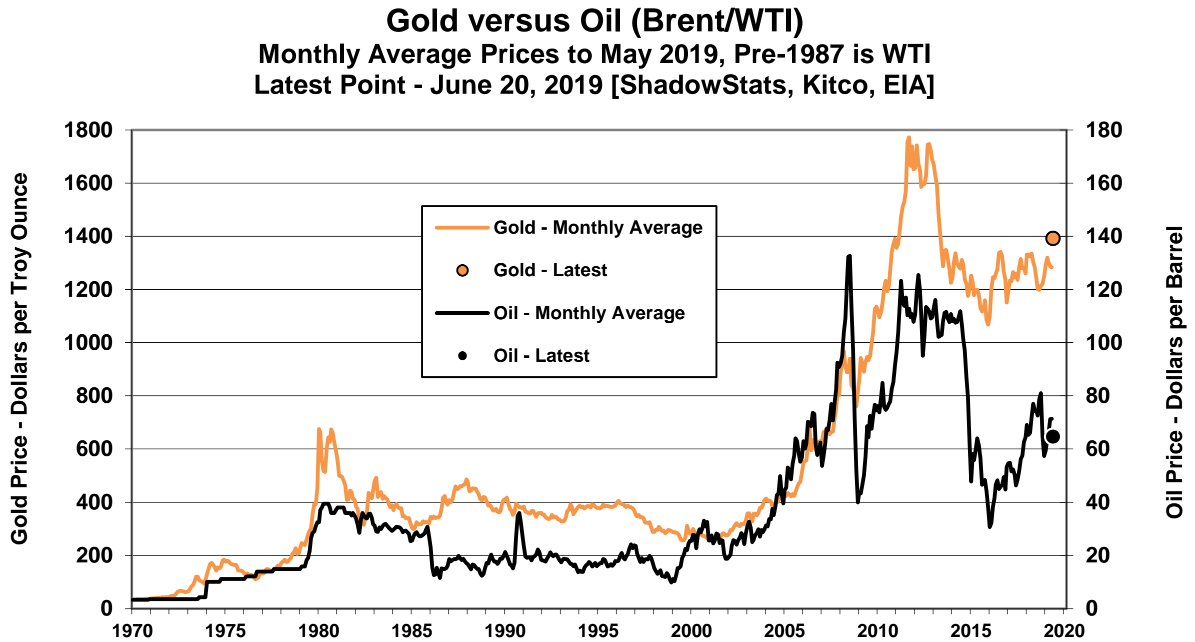
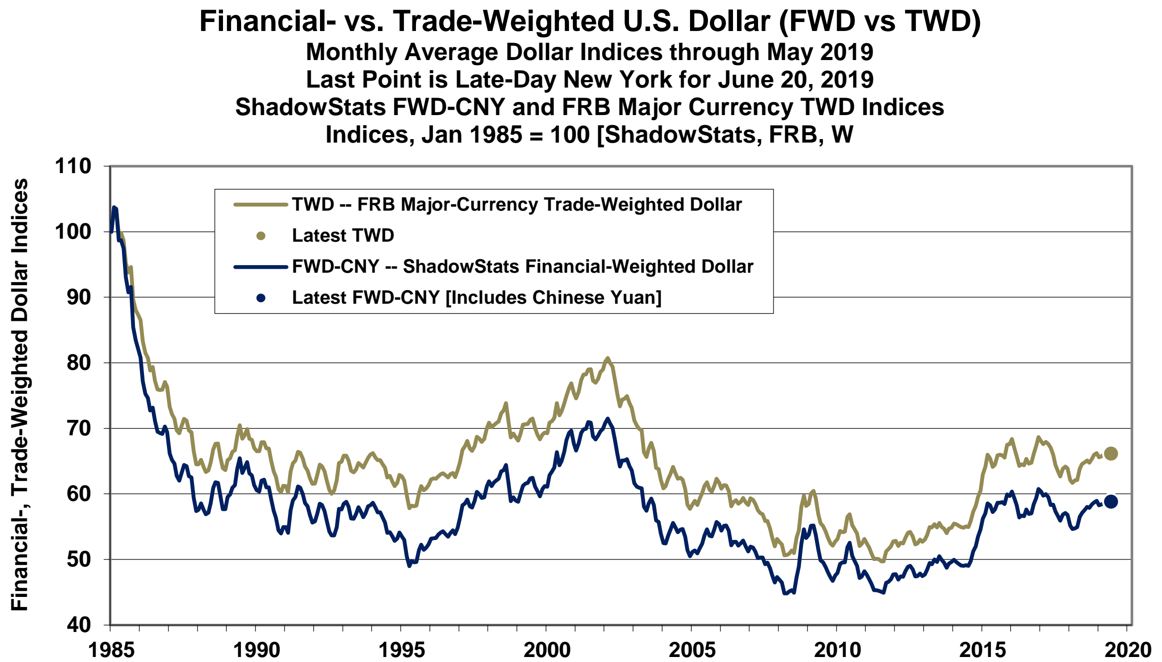
Graph 30: Gold versus Silver



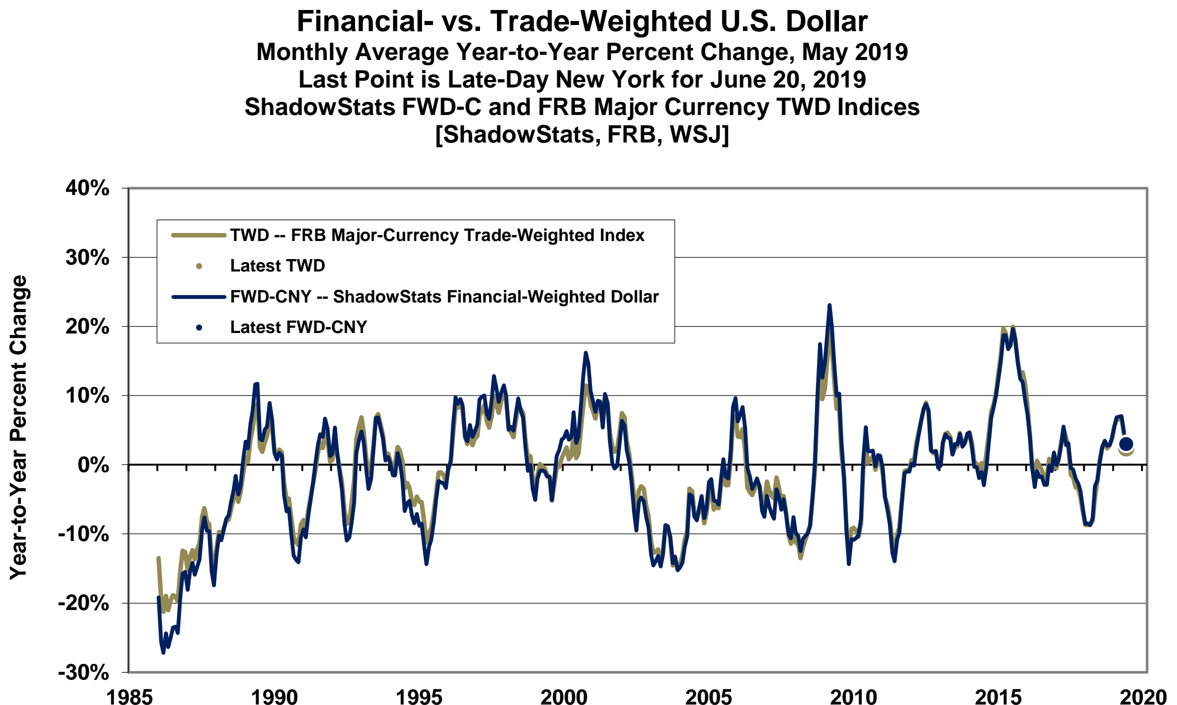
Graph 31: Gold versus Oil



Graph 32: Financial- vs. Trade-Weighted U.S. Dollar, January 1985 = 100



Graph 33: Financial- vs. Trade-Weighted U.S. Dollar, Year-to-Year Percent Change



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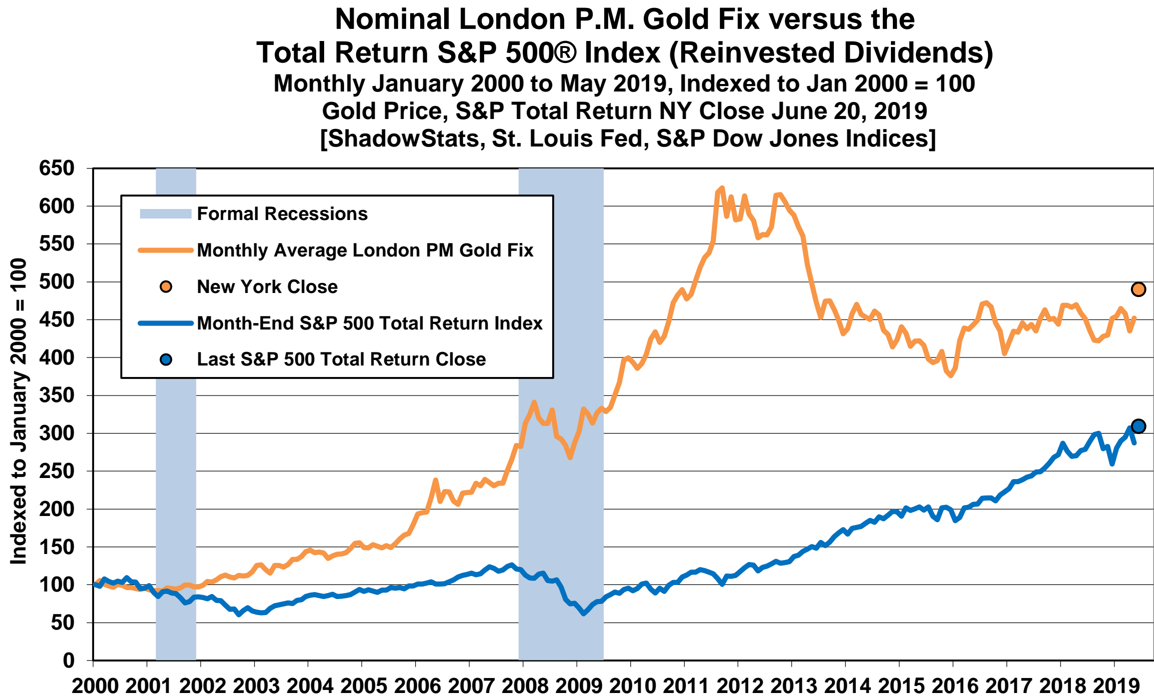
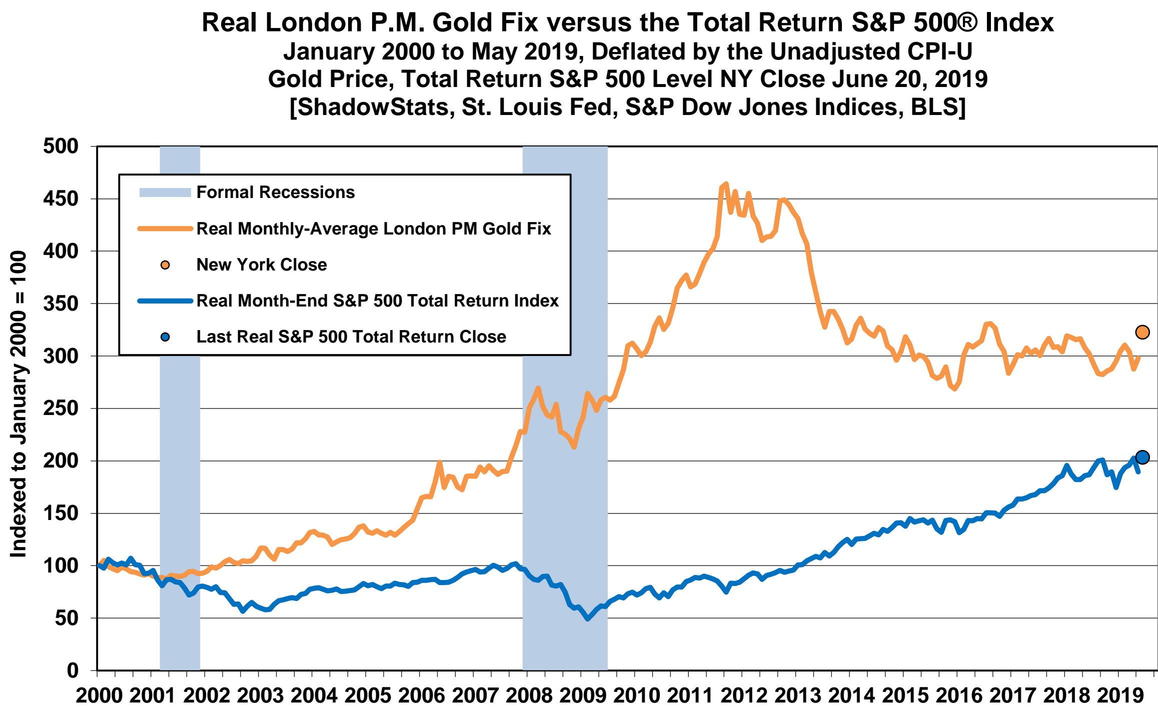
Graph 34: Nominal Gold versus the Nominal Total Return S&P 500



Graph 35: Real Gold versus the Real Total Return S&P 500



SECTION 3 - FEDERAL RESERVE AND MONETARY POLICY

FOMC Continues to Tighten, Despite "Easing Talk"

Rapidly Intensifying "New" Economic Downturn Exacerbates Negative Conditions in Areas of the Economy and Consumer Finances That Never Recovered from the Great Recession. The June 19th Federal Open Market Committee (FOMC) Meeting did not alter headline basic policy or outlook by much, holding the targeted Federal Funds Rate in its 2.25% to 2.50% range. Yet, hints of possible future FOMC easing action came from Fed Chairman Powell's Press Conference, where he indicated some concern on the economy, along with promises that the FOMC would take stimulative action as needed. The consensus outlook for the meeting had been for no action, other than an indication of some possible easing, soon, and that was what happened.

The FOMC most certainly would like to raise rates and to tighten liquidity further, to help the banking industry. Unfolding, underlying reality, though, remains that the economy is tumbling anew, thanks to the excessive FOMC tightening and rate hikes of the last year. In the national interest, the FOMC should act as soon as possible to ease.

Where the Federal Reserve's Federal Open Market Committee (FOMC) formally was neutral as to a change in policy, the FOMC nonetheless shortly will find itself in a position where it will have little choice but to ease, very possibly returning to some form of Quantitate Easing, given the severity of the "new" downturn that appears to be underway. The U.S. economy visibly is sinking quickly and meaningfully, reflecting mounting consumer liquidity stresses, which also will mean mounting financial stresses in the business and banking communities, the latter being the FOMC's client community.

Again, overly aggressive FOMC rate hikes and policy tightening of recent years triggered the unfolding "new" downturn, yet when the Fed first moved to tighten those policies in 2017, after years of Quantitative Easing (QE), many areas of the U.S. economy still had not then, and have not since recovered fully from the Great Recession and Banking System Collapse that engendered QE. Accordingly, it likely will take further fiscal stimulus from the Federal Government in the form of some tax relief aimed at Main Street U.S.A. and some form of increased government spending aimed at areas such as infrastructure, if the economy is to be returned to some normal functioning. Considerable Great Recession non-recovery means that even more action is needed to stabilize the system at present and for the longer haul than what the FOMC appears to be considering. That latter, fiscal stimulus process, however, likely will be difficult, given the rapidly deteriorating federal budget deficit conditions.

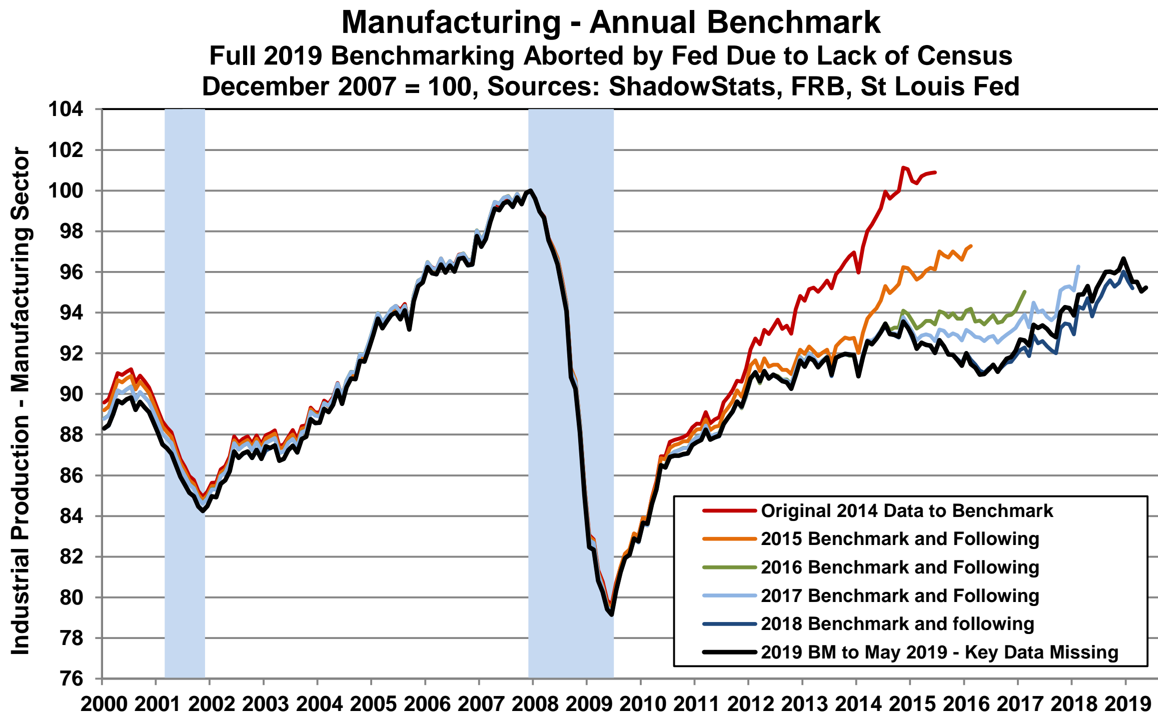
Graphs 38 to *41* of the monthly and quarterly Saint Louis Federal Reserve's Adjusted Monetary Base reflect periods of Federal Reserve easing when expanding, and tightening when in decline. The issues involved with these monetary measures have those involved the markets considering the nature of the broad and uncertain scope of the financial risks that lie ahead.

Federal Reserve Has Tightened Since December 2018. Reflected in *Graphs 38* and *39* of the monthly Saint Louis Fed Adjusted Monetary Base, the May 2018 Monetary Base has contracted to a six-year, low, down by 3.2% (-3.2%) from December 2018, the Fed's last formal tightening.

Federal Reserve Tightening. Going back a little further, the interest rate hikes since late-December 2017 have strangled consumer liquidity, pushing the U.S. economy into a new downtrend (see *Graphs 40* and *41*). *Graph 41* shows the year-to-year decline of 12.2% (-12.2%) in the first-quarter 2019 St. Louis Fed Adjusted Monetary Base, following a fourth-quarter 2018 annual decline of 10.3% (-10.3%). The first-quarter 2019 annual decline was the deepest seen since the Depression of 1920-1921 [an annual decline of 15.1% (-15.1%) in fourth-quarter 1921], following World War I. First-quarter 2019 showed a deeper annual drop than the third-quarter 1937 annual decline of 10.9% (-10.9%), credited with helping to trigger the second down-leg of the Great Depression.

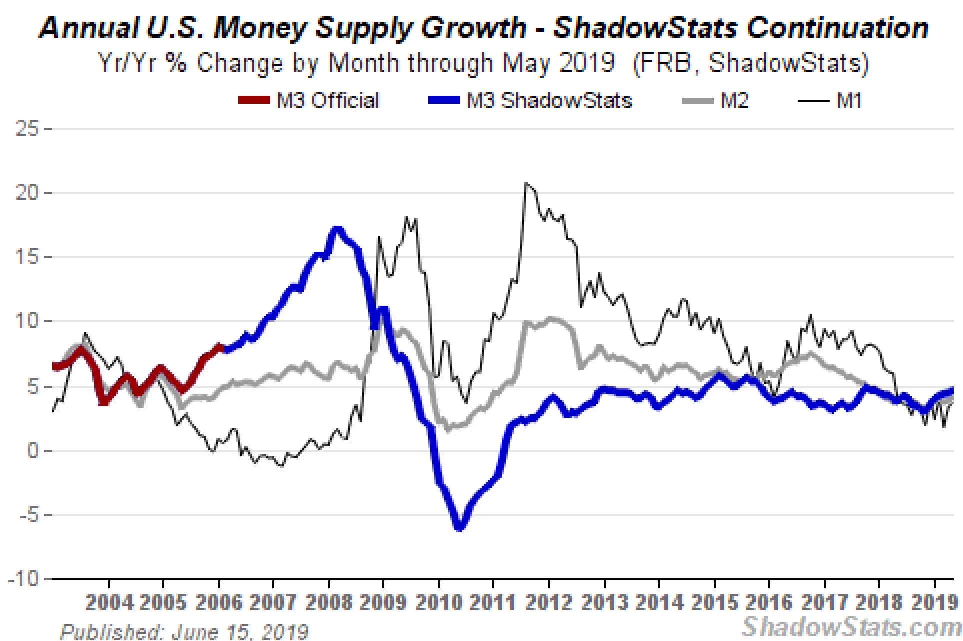
Aborted 2015 Tightening Pummeled Production and Manufacturing in 2015. Largely repeated here from ***SECTION 1***, as seen in *Graphs 38* and *40*, there was an aborted monetary tightening in 2015, which pushed domestic Production and Manufacturing activity into recession, although that downturn was revealed only later, after several years of Production benchmark revisions (see *Graph 36*). The FOMC retreated anew in 2017, beginning its current tightening. Production and Manufacturing responded similarly, anew, along with much of the balance of headline U.S. economic activity. What happened to the economy in 2015 was see in the CASS Freight Index™ in *Graphs 1* and *2* and is discussed there. *Graph 36* shows disrupted manufacturing revisions that eventually mirrored the 2015 dip in the Monetary Base, as seen in *Graphs 38* and *40*.

Graph 36: Minimalized Fed Benchmark Manufacturing Revisions Masked an FOMC-Induced Recession



Annual Growth Has Picked Up Minimally in M1, M2 and M3. Mirroring a combination of what have been Fed tightening policies, a collapsing Monetary Base and an annual benchmarking, annual growth in Money Supply M1 slowed to a near-term trough of 1.9% in March 2019, picking up to 3.4% in April and 3.8% in May. Money Supply M2 in March 2019 slowed to a 3.8% near-term trough, picking up to 3.9% in April and 4.1% in May. Annual growth in Money Supply M3 (ShadowStats Ongoing Measure) continued to rise off its November 2018 trough, to 4.3% in March 2019, to 4.4% in April and 4.50% in May, broadly shown in *Graph 37*, reflecting perhaps shifting expectations that it might be good time to lock-in higher interest rates. These data are published and plotted on the Alternate Data tab of http://www.shadowstats.com.

Graph 37: Annual Growth in Monthly Nominal Money Supply M1, M2 and M3

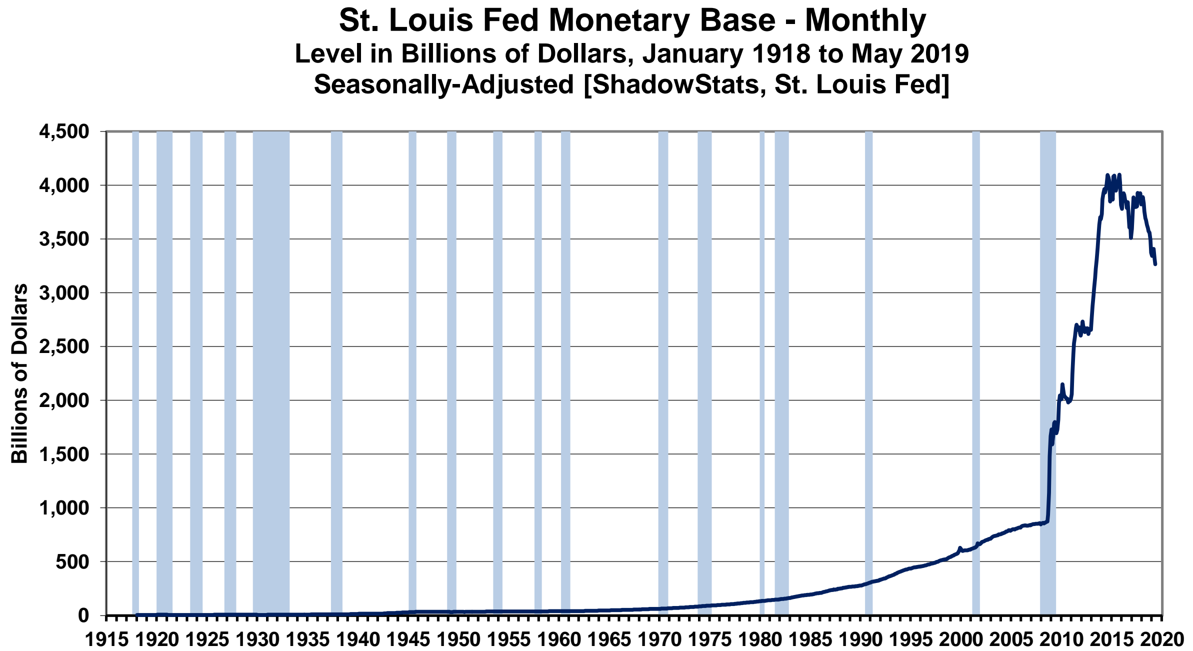


Level of the Seasonally Adjusted Monthly Monetary Base in May 2019 Was Down by 3.2% (-3.2%) from December 2018, Down by 4.6% (-4.6%) Unadjusted at a Six-Year Low. Despite FOMC talk of holding policy steady subsequent to the December 2018 FOMC tightening, liquidation of the Fed's balance sheet continued at least into May 2019, with the level of the Saint Louis Fed's Adjusted Monetary Base dropping, both seasonally adjusted and unadjusted, down respectively against the December 2018 level by 3.2% (-3.2%) adjusted, and by 4.6% (-4.6%) unadjusted. Annual change in May 2018 was a decline of 11.6% (-11.6%), both adjusted and unadjusted, off its near-term trough of 13.0% (-13.0%) in February 2019, as reflected in *Graphs 38* and *39*.

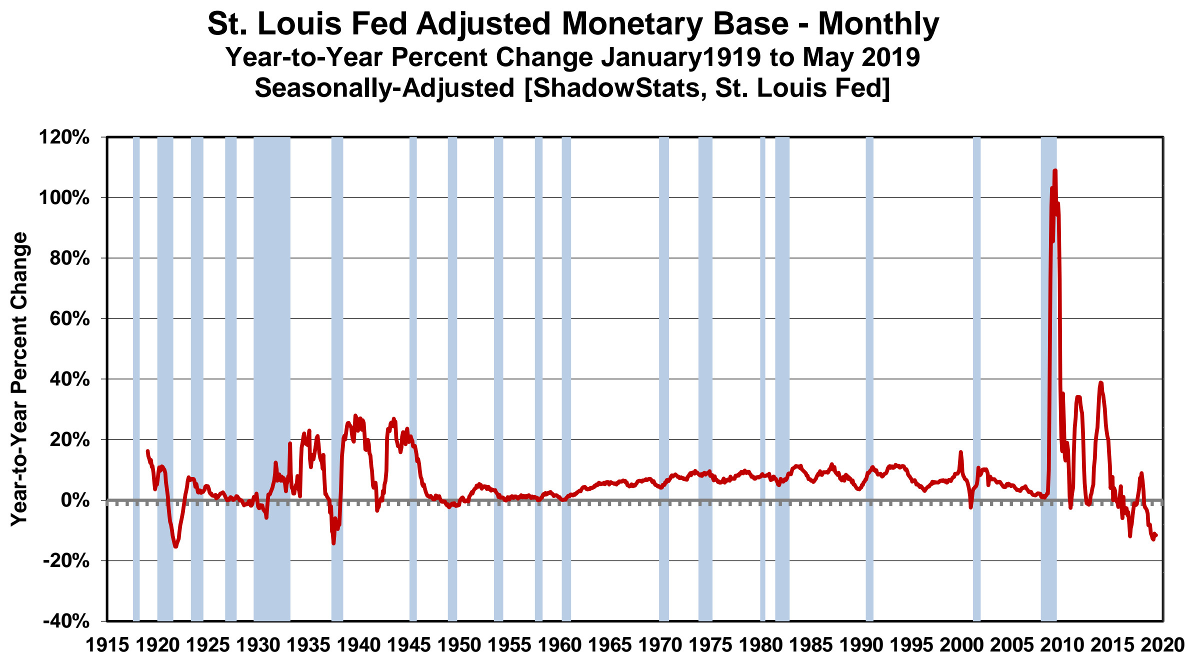
Annual Growth in First-Quarter 2019 Monetary-Base Plunged Year-to-Year as Though It Were 1921. Discussed in ***Special Commentary No. 983-B*** first-quarter 2019 of the St. Louis Fed's Adjusted Monetary Base declined year-to-year by 12.0% (-12.0%), the deepest annual plunge since 1921, since the post-World War I depression, leading into the roaring '20s, the 1929 Stock Crash and the Great Depression. It was a deeper year-to-year quarterly decline than the 10.9% (-10.9%) in third-quarter 1937, credited with triggering the second down-leg of the Great Depression. The Federal Reserve attempts to

minimize the effects of annual growth in the Monetary Base on the annual growth of the Money Supply, although there is carry-through impact. *Graphs 40* and *41* plot he quarterly Monetary Base series.

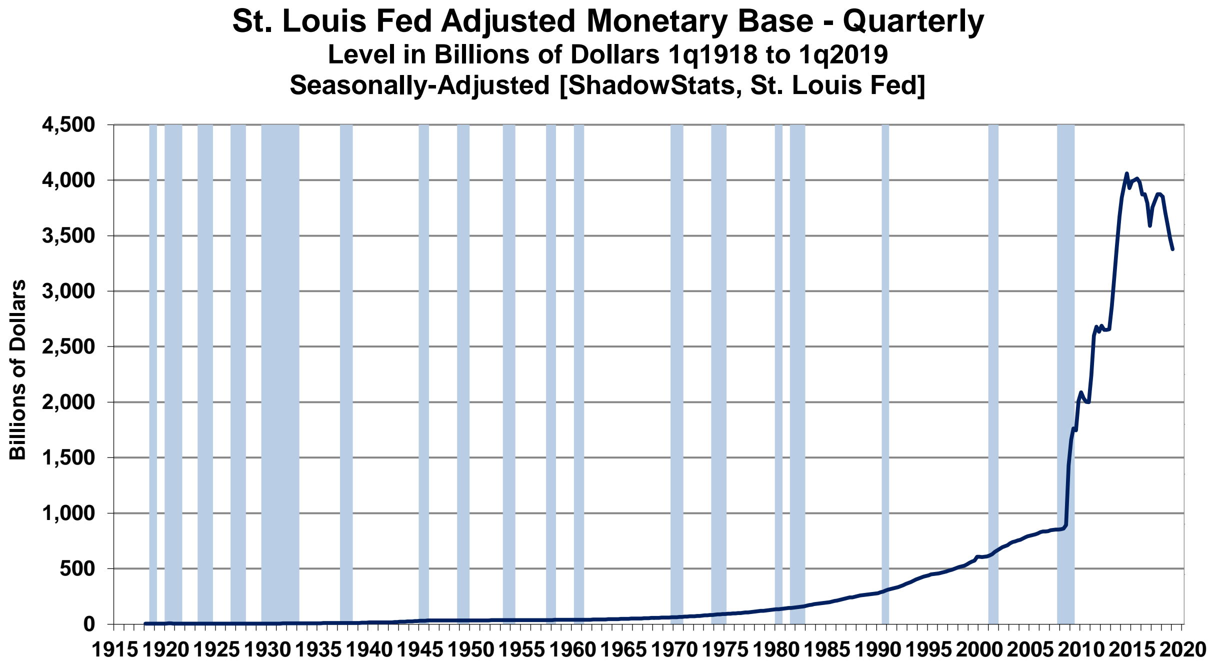
Graph 38: Saint Louis Fed Monthly Monetary Base, Billions of Dollars, January 1918 to May 2019



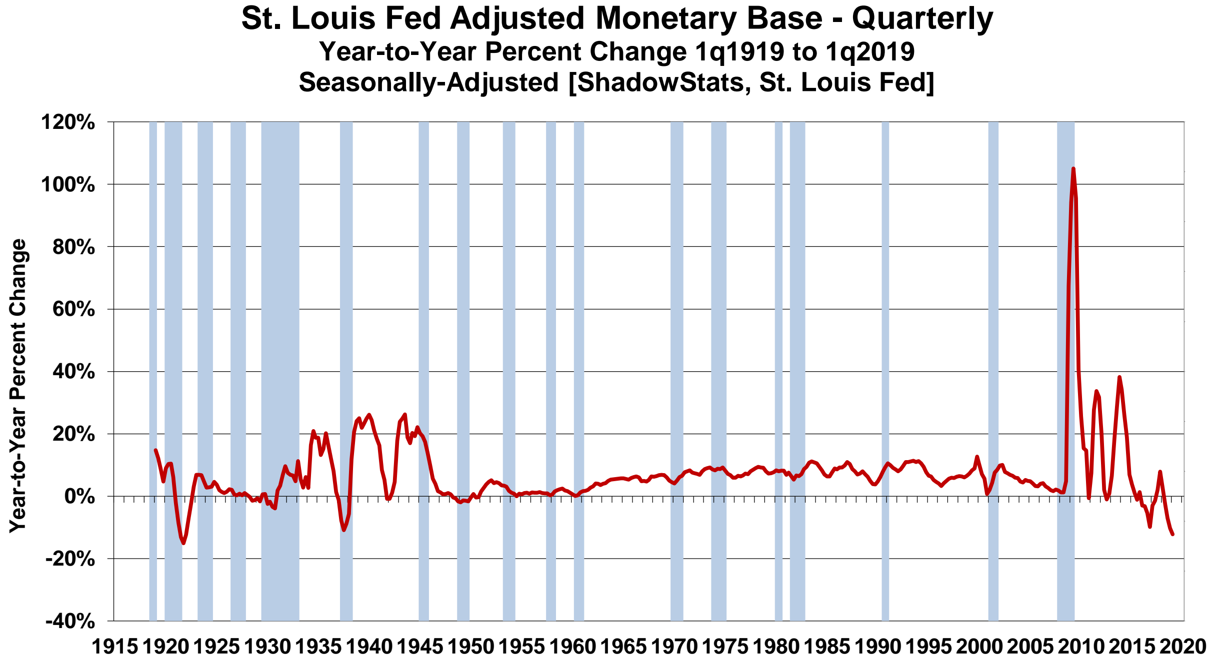
Graph 39: Yr-to-Yr Percent Change, Monthly Saint Louis Fed Monetary Base, January 1919 to May 2019



Graph 40: Saint Louis Fed Quarterly Monetary Base, Billions of Dollars, 1q1918 to 1q2019



Graph 41: Yr-to-Yr Percent Change, Quarterly, Saint Louis Fed Monetary Base, 1q1920 to 1q2019



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SECTION 4 - STIMULATIVE FISCAL POLICY NEEDED ALONG WITH FED EASING

Yet, "Current Fiscal Policy Is Not Sustainable"

ShadowStats Contends That Major Areas of the U.S. Economy Remain Impaired from the Effects of the Great Recession and That Expansive Fiscal Stimulus and Continued Trade Overhaul Are Needed on Top of Renewed Federal Reserve Easing, in Order to Restore Domestic Economic Health. The problem here is that fiscal stimulus expands the budget deficit, and the global markets—particularly the currency markets versus the U.S. dollar—would react strongly against such action, given the broadly uncontained U.S. deficit and debt expansion crisis.

One approach would be to address the American people and Global Markets on the circumstance, outlining credible, enforceable actions to move U.S. government finances to long-term sustainability, once economic domestic economic activity has stabilized. While such may seem impossible or impractical, something needs to be done immediately.

If the issues are not addressed, which is the highly likely near-term outcome, the balance of this section, largely repeated from ***Special Commentary No. 983-B***, provides some idea as to where the U.S. circumstance is headed.

Federal Deficit Is Out of Control and "Not Sustainable." Discussed in the ***Special Commentary No. 983-B***, Treasury Secretary Mnuchin summarized the ***2018 Financial Statement of the U.S. Government*** as follows: "The projections in this *Financial Report* show that current policy is not sustainable."

At present, with current operations, the budget deficit has been ballooning, despite U.S. Federal Debt being at its prescribed ceiling, which the Congress has not been willing to address, and which the U.S. Treasury has been able to skirt breaking, using "extraordinary measures." Much of the text that follows comes from ***No. 983-B*****.**

Based on generally accepted accounting principles (GAAP), the headline net obligations of the Federal Government, including the unfunded liabilities valued in today's dollars, have reached an order of magnitude of well over $100 trillion, including $22.0 trillion in existing **U.S. Treasury debt** (the largest amount of sovereign debt in the world. That $100-plus trillion needed in hand to cover existing U.S. obligations not only is five-times greater than the headline nominal U.S. GDP, but also tops current estimates of the aggregate global GDP of about $85 trillion. Indeed that circumstance is unsustainable and uncontainable, yet those controlling the U.S. government consistently refuse to address the nation's long-term solvency issues, although they talk about it.

Fourteen years ago, the regular annual reporting of government financial conditions in the *Financial Report of the United States Government*, showed that U.S. Government fiscal conditions and long-term financial operations had deteriorated to the point of unsustainability by the end of the government's fiscal

year 2004. Conditions have continued to deteriorate markedly ever since. The government's financial statements reflect GAAP-based (generally accepted accounting principles) accrual accounting, as used in accounting for most businesses, going well beyond the regular cash-in versus cash-out accounting of the headline monthly and annual federal budget numbers.

The GAAP statements include not only concepts such as Accounts Receivable and Payable, Assets and Depreciation, but also projections of the net present value (NPV) of unfunded liabilities tied to programs such as Social Security and Medicare. The NPV discounts the future value of obligations net of related income, so as to reflect the amount of money effectively needed in hand today to cover those future obligations, allowing for interest rates, etc.

Based on what was then a particularly large $11 trillion surge in 2004 unfunded liabilities, tied to Medicare expansion in 2006, I raised the issue then of an inevitable U.S. hyperinflation, with a key advisor to both the Bush Administration and then Federal Reserve Chairman Alan Greenspan. I was told simply that the problem was too far into the future to worry about. Indeed, continuing to push the big problems further into the future still appears to be the only working strategy for the Congress, the Fed and recent and current Administrations.

The financial conditions of the United States Government have continued to deteriorate each year by an amount that is beyond the political willingness and ability of the federal government to address. Purportedly, it was Arthur Burns, Federal Reserve Chairman under Richard Nixon, who first offered the advice that helped guide a number of Administrations. The gist of the imparted wisdom was that if the Fed or federal government ran into economic or financial-system difficulties, the federal budget deficit and the U.S. dollar simply could be ignored—or sacrificed. Ignoring them would not matter, it was argued, because doing so would not cost the incumbent powers any votes. Yet, the U.S. dollar and the budget deficit do matter.

Complicating the current circumstance, the Fed still is trying to unwind its banking-system rescue package from the 2008 panic, but it has not been able to stabilize fully either the banking system or the economy. As an inevitable, renewed downturn in the economy continues to unfold, and as foreign investors increasingly back away from holding U.S. dollars and Treasury securities, the U.S. central bank will have little choice but to flood the system anew with liquidity and to monetize significant new amounts of Treasury debt.

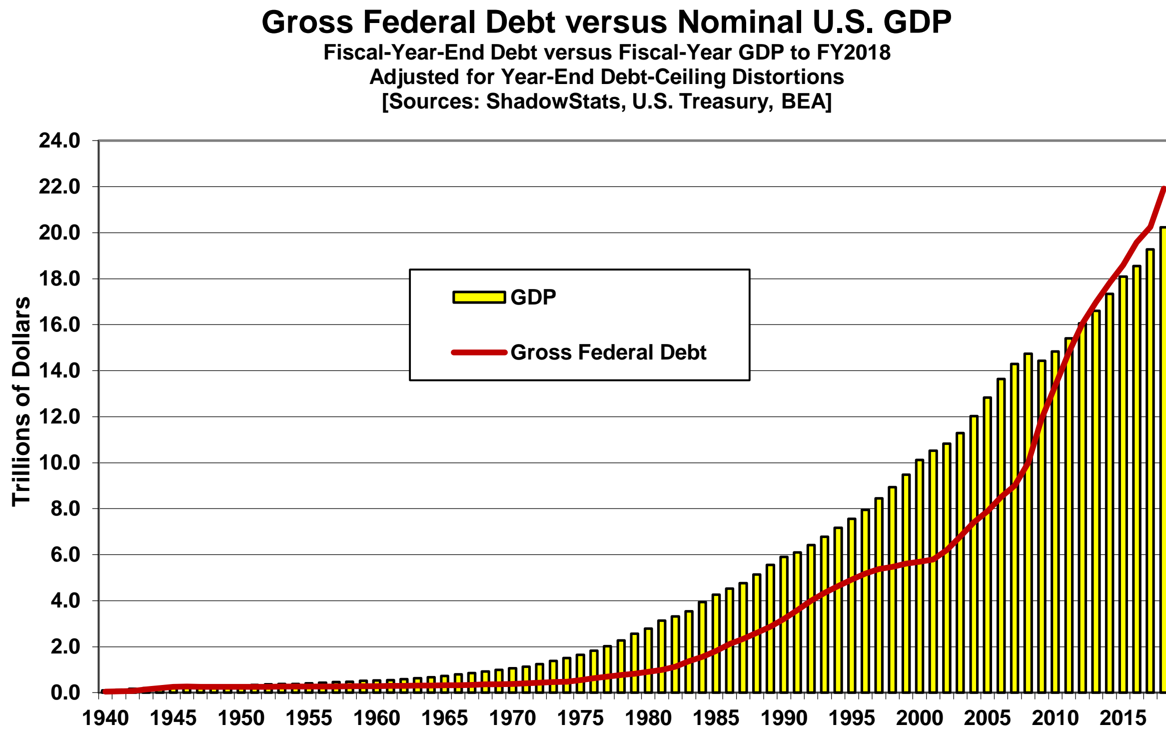
As global markets look to escape their looming losses in U.S. dollar holdings, that day of ultimate reckoning for the U.S. currency likely remains near. A flight from the dollar and hyperinflation fears could break over a very short period, as quickly as the banking panic of 2008, for example, or it could evolve over longer periods and intermittent crises.

ShadowStats Hyperinflation Forecasts. I have published the *Shadow Government Statistics* newsletter since 2004. Early on, I began discussing the long-term insolvency of the United States Government leading to a domestic hyperinflation likely around 2018 or 2019. The ShadowStats' *Hyperinflation Watch* coverage has evolved over the years, in the context of what I view as inevitable hyperinflation. In the wake of the financial crisis of 2008, the timing of the hyperinflation forecast was advanced to 2014, which obviously did not happen. Yet, underlying fundamentals only have deteriorated since. Again, unless the United States addresses the long-range solvency issues currently in play for the U.S. Treasury,

a hyperinflation will hit the United States, and it likely will be set off much earlier than most anticipate, by any number of factors that could trigger a panicked sell-off in the U.S. dollar.

Incorporated here by reference, I wrote in *Hyperinflation 2014—The End Game Begins (Revised), No. 614*, of April 2, 2014: "The [ShadowStats] forecast of a U.S. hyperinflation has been in place since at least 2006. Those who have read the various ShadowStats reports on hyperinflation—as opposed to just catching occasional sensationalized headlines in the press—usually recognize that the forecast has been of a future circumstance, in what used to be the distant future. In the early writings, the outside time limit for the crisis was 2018 or 2019, the end of the current decade. That outside timing was moved in closer in time, to 2014, following the near-collapse of the financial system in 2008. [For those interested, the full series of hyperinflation reports to the point in time is described and linked at the end of the *Definitions and Background* section in *No. 614*]."

Graph 42: Nominal Gross Federal Debt versus Gross Domestic Product



Given a GAAP-based shortfall in current total U.S. government operations and obligations at an order of magnitude minimally of $100 trillion (including the NPV of unfunded liabilities), that is the amount of cash needed in hand today, in today's dollars, to cover U.S. net obligations going forward. Reflected in *Graph 42*, in nominal terms—today's dollars—the total value of economic activity in the United States, as measured by the GDP for the fiscal year-ended September 30, 2018 stood at $20.3 trillion. That was against total public debt of the U.S. Treasury at that time of $21.5 trillion, with the excess of debt level over GDP expanding rapidly. **There is no chance of the U.S. government covering its total net-present-value obligations in excess of $100 trillion, under stable monetary conditions.**

In the current circumstance, unless the U.S. government meaningfully overhauls its planned expenses (a significant reduction in spending) and/or increases its revenues (a significant increase in tax revenues) going into the future, including overhauling Social Security, Medicare and Medicaid, it has no chance of covering its net obligations going forward, other than by just printing the dollars needed, generating dollar-debasement and eventual hyperinflation. The potential hyperinflation here is every bit the same as seen in the German Weimar Republic post-World War I, Zimbabwe in the 1990s and 2000s and Venezuela, with inflation hitting 80,000% in 2018.

When a Currency Is Debased, Precious Metals Function as Stores of Wealth. Since establishing the Federal Reserve System 1913 ago, and since abandoning the gold standard for the U.S. dollar in two steps, in 1933 and 1971, the United States has experienced a subsequent, cumulative, significant domestic price inflation not seen before in its history.

Reflecting the function of gold and silver as stores of wealth, their U.S.-dollar-based prices tend to rally in a manner commensurate with the ongoing debasement of the U.S. currency. Such was seen particularly in the period following the final, formal break between the dollar and gold in 1971. The average price of gold was $41 per troy ounce in 1971 and $1,269 in 2018, forty-six years later.

Traditionally—literally over millennia—gold has been the dominant precious metal as a store-of-wealth, with silver a close second. Although silver prices increasingly have reflected an element of industrial demand in the last century, the gold-silver price relationship in the open markets, post-1974 (when private U.S. gold ownership was re-allowed) has been highly correlated, at 91% in terms of movement in monthly-average prices, and 92% in terms of movement in the annual-average prices. The store-of-wealth function has remained the primary driving factor behind the price movements in both these precious metals over time.

Some Historical Perspective on Gold, Silver and the Preservation of Wealth. Over the millennia, gold and silver have served investors—those holding the physical precious metals—with a stable, liquid and portable store of wealth against inflation or monetary turmoil, as well as often providing a vehicle for financial and personal survival in times of political and social upheaval.

In countries where currency was denominated in gold and/or silver, the hard currency was its own store of wealth. Most commonly, however, political states have ended up debasing their currencies or moving to a fiat currency backed by no hard assets, as seen with the present-day U.S. Dollar.

Roughly the same amount of silver that would buy a loaf of bread in ancient Rome, would buy a loaf of bread today in New York City.

A Broadway enthusiast who could get a third-row center seat for a prime New York City play in 1925 for the cost of a five-dollar gold piece, could get that same seat in 2017 for the value of the gold content of that same five-dollar coin.

While both metals have seen increased industrial usage in the last century, particularly for silver (exclusive of jewelry and related products), the store-of-wealth aspects of gold and silver, again, have been the primary and dominant drivers of price movements of both precious metals throughout history, and particularly in the nearly half century since President Richard Nixon closed the Gold Window.

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Abandoning Gold. The gold standard was a system that automatically imposed and maintained monetary discipline. Excesses in one period would be followed by a flight of gold from the system and a resulting contraction in the money supply, economic activity and prices.

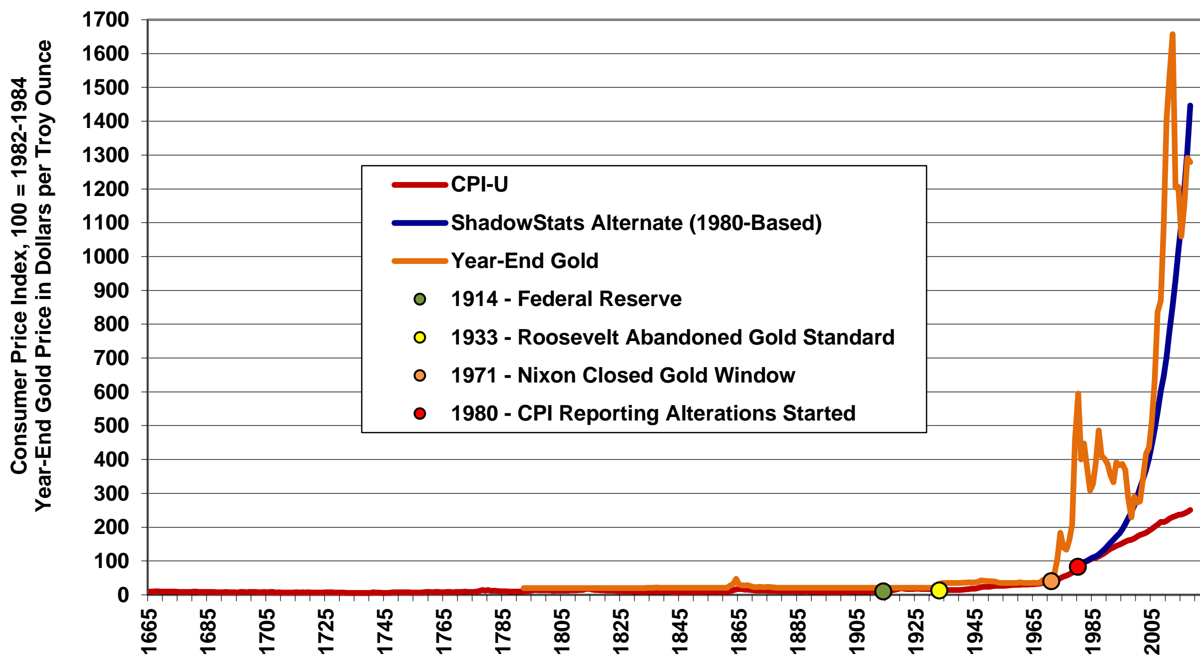
Faced with the Great Depression, and unable to stimulate the economy due partially to that discipline, President Franklin Roosevelt used the depression as an excuse to abandon the domestic gold standard. He adopted close to a fully-fiat currency (not backed by hard assets), under the auspices of what could be called the "debt standard," where the government effectively could print and spend whatever money it wanted to create.

Roosevelt's actions were against the backdrop of the banking system being in a state of collapse. There was no deposit insurance at the time, and available Federal Reserve policies were ineffective, as banks failed and the money supply imploded. A depression collapsed into the Great Depression, with intensified consumer price deflation. Importantly, a sharp decline in broad money supply was and is a prerequisite to significant goods-and-services price deflation.

Where Roosevelt abandoned the domestic gold standard on April 5, 1933, eliminating domestic convertibility of U.S. dollars for gold and making illegal the domestic private ownership of monetary gold, Nixon eliminated the international convertibility of U.S. dollars for gold on August 15, 1971.

When chances of reopening the Gold Window were viewed as nil, Congress and President Ford enacted legislation allowing U.S. citizens to own physical gold, once again, as of December 31, 1974.

Graph 43: Consumer Inflation 1665 to 2018 versus the Price of Gold



Graph 43 presents some historical perspective on year-end gold price versus inflation from the 17th century-to-date, as experienced in the American Colonies and later the United States. Gold prices have not been fitted mathematically to the inflation curve, but do tend to show a leading relationship to it. Despite ups and downs around wars, the California Gold Rush, through World War I, the graph shows what appears to be a fairly stable level of prices up to the founding of the Federal Reserve in 1913 (began activity in 1914) and to Roosevelt's abandoning of the domestic gold standard in 1933. Then, inflation takes off in a manner not seen in the prior 250 years, and at an exponential rate when viewed using the ShadowStats-Alternate Measure of Consumer Prices in the last several decades.

The ShadowStats measure approximates headline Bureau of Labor Statistics' Consumer Price Index (CPI-U) inflation as it currently would be, net of changes made to reporting methodologies since 1980, when the federal government pushed inflation-reducing changes to reporting methodologies, so as to help cut federal spending in such areas as Social Security cost of living adjustments (see *Public Comment on Inflation*). Of significance, gold generally has continued to cover fully the "common experience" inflation, not just the artificially suppressed headline CPI-U, as seen in the graph.

Robert Sahr of Oregon State University constructed the price levels shown prior to 1913. Price levels since 1913 either are the CPI-U or ShadowStats-based, as indicated. All references to inflation, unless otherwise stated, reflect the headline CPI-U. The ShadowStats-Alternate Measure is shown for background informational purposes.

Persistent year-to-year inflation (and the related compounding effect) did not take hold until post-Franklin Roosevelt. Additionally, the CPI level reflects purchasing power lost over time for those holding dollars, which is cumulative, and which has reached extremes due to the later-era compounding effect. Consider that consumer prices at the time of the founding of the Federal Reserve in 1913 were about the same as they had been in New Amsterdam (today's New York City) in 1665.

Against prices in 1913, based on the current, understated headline CPI-U inflation, prices in 2017 were 25.5 times what they were in 1913, or in reverse, $1.00 in 1913 was worth about $0.04 in 2018. The annual average price of gold rose from $20.67 per troy ounce in 1913, to $1,269 in 2018, significantly more than protecting against the headline inflation gain over the same time span.

Allowing for minor, average-annual price-level declines in 1949, 1955 and 2009, the United States has not seen a major deflationary period in consumer prices since before World War II. The reason for this is the abandonment of the gold standard and recognition by the Federal Reserve of the impact of monetary policy—free of gold-standard system restraints—on the economy and inflation.

Federal Reserve Chairmen Alan Greenspan and Ben Bernanke both were students of the Great Depression period. As did Mr. Greenspan before him, Mr. Bernanke vowed not to allow a repeat of the 1930s money-supply collapse and a resulting severe deflation. Fed Chair Janet Yellen confirmed she was in Mr. Bernanke's camp. To my knowledge, current Fed Chairman Jerome Powell yet to weigh in on the matter.

Where Roosevelt abandoned the gold standard and its financial discipline for the debt standard, thirteen successive administrations have pushed the debt standard to the limits of its viability. Such has been seen now in recent economic and systemic turmoil, and in the ongoing threat of systemic upheaval, with the U.S. government facing the risk of a default created by potential conflicts between Congress and the

White House, along with long-range sovereign-solvency issues tied to roughly $100 trillion-plus net present value of long-term federal obligations.

Otherwise faced with intractable financial-system instabilities, the Federal Reserve of today is looking for higher inflation to help support higher interest rate to help pull the banking system away from collapse. Any inflation created here would feed directly into spiking the near-term prices of precious metals.

# # #

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