

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

COMMENTARY NUMBER 419
January CPI, PPI, Real Retail Sales and Housing Starts

February 17, 2012

Annual “Core” Inflation Rose for 15th Straight Month

Year-to-Year January Consumer Inflation: 2.9% (CPI-U), 3.1% (CPI-W), 10.5% (SGS)

Headline CPI and PPI Inflation Rates Understated Due to Unstable Seasonal Factors

PLEASE NOTE: The next regular Commentary is scheduled for Friday, February 24th, covering January new and existing home sales.

Best wishes to all — John Williams

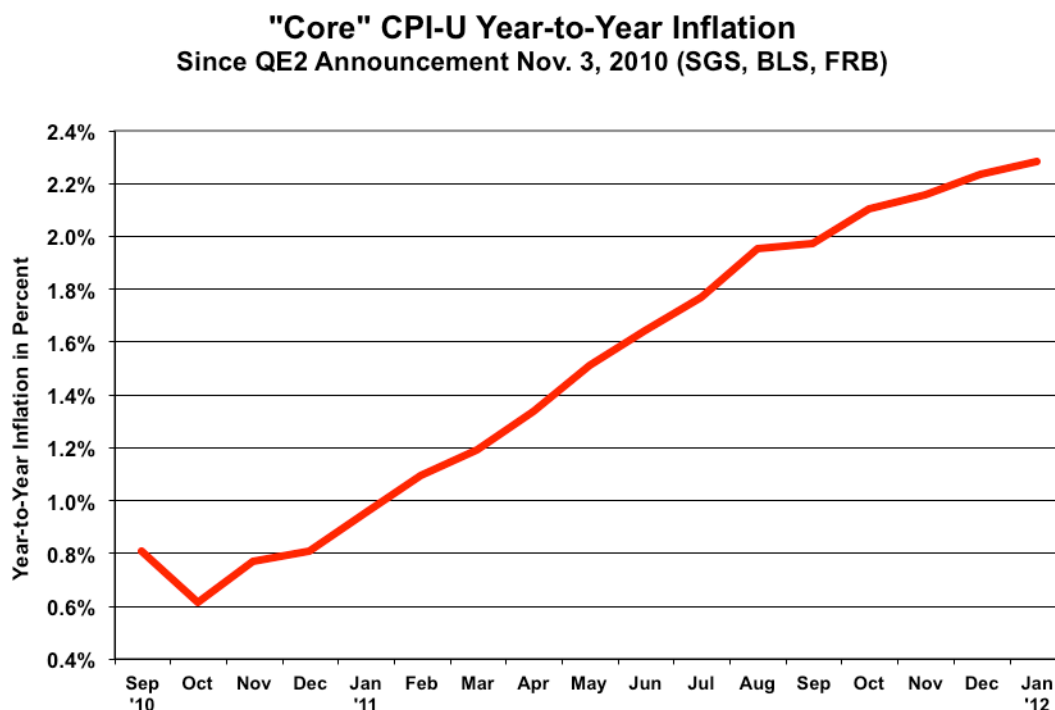
Opening Comments and Executive Summary. Key business data for January were of mixed results but, on balance, were on the soft-side of consensus expectations. In terms of the headline labor data, retail sales, industrial production and housing starts, only the jobs and unemployment numbers beat expectations; the other headline releases generally were much weaker than expected. In the context of prior-period revisions and special circumstances, the labor numbers were not as hot as they appeared, the retail sales were even worse than reported, but the production and housing data were somewhat stronger. Nonetheless, there was nothing released that altered the basic outlook on bottom-bouncing economic activity.

On the inflation front, the headline numbers were softer than expected, but that was due fully to unstable seasonal-adjustment factors for gasoline and energy-related prices. In the case of the energy prices that were overly depressed in January's CPI and PPI reporting by poor-quality seasonal adjustments, there will come a period in the months ahead when the distortions will swing the other way, overstating the seasonally-adjusted monthly inflation. Nonetheless, year-to-year (unadjusted) aggregate inflation remained high, while "core" inflation continued to show the still-spreading inflationary impact of the Fed's QE2 on the broad economy.

CPI and PPI. Headline monthly CPI-U inflation for January was 0.21%, 2.93% year-to-year, versus respective flat monthly inflation and 2.96% annual inflation in December. The SGS-Alternate consumer inflation estimate for annual inflation was 10.5% in January, versus 10.6% in December.

The seasonally-adjusted headline CPI-U was understated by unstable monthly seasonal adjustment factors, but "core" inflation continued to increase both monthly and year-to-year, as high oil prices that resulted from dollar-debasement efforts in QE2 continued to permeate the non-energy segments of the broad economy.

As shown in the accompanying graph, annual "core" inflation has increased for 15 straight months, since Mr. Bernanke began jawboning QE2 in October 2010.

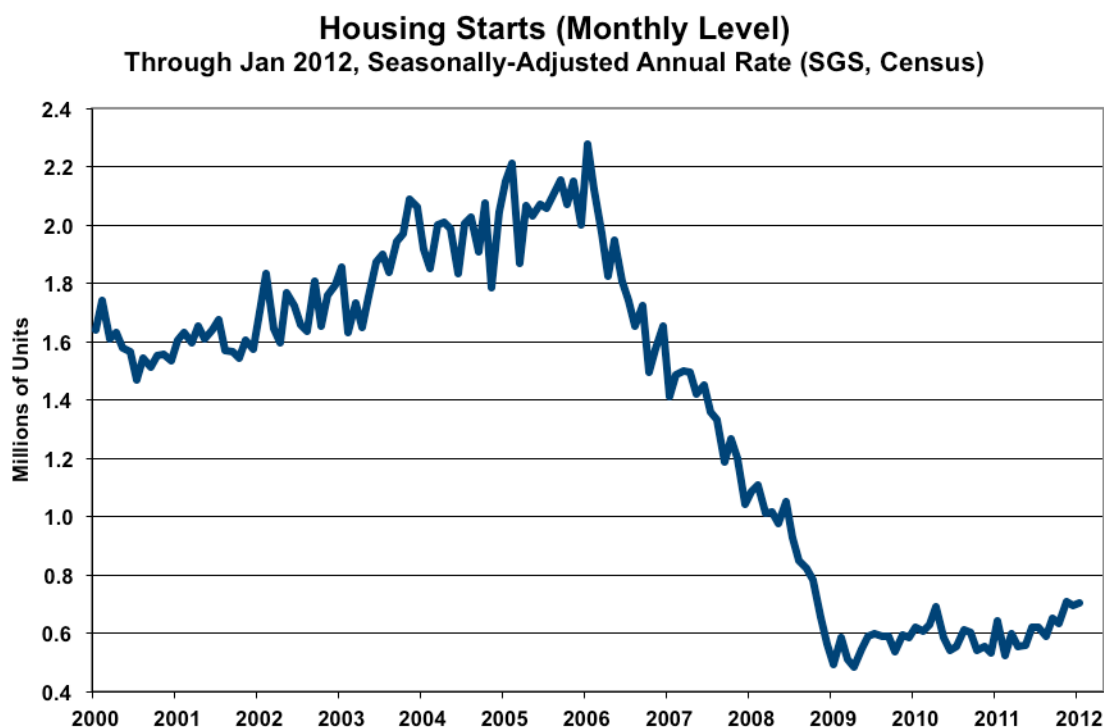


January's headline wholesale inflation at the finished goods level was 0.1% for the month, 4.1% year-to-year, versus a 0.1% monthly decline in December, with year-to-year inflation then at 4.8%. As with the

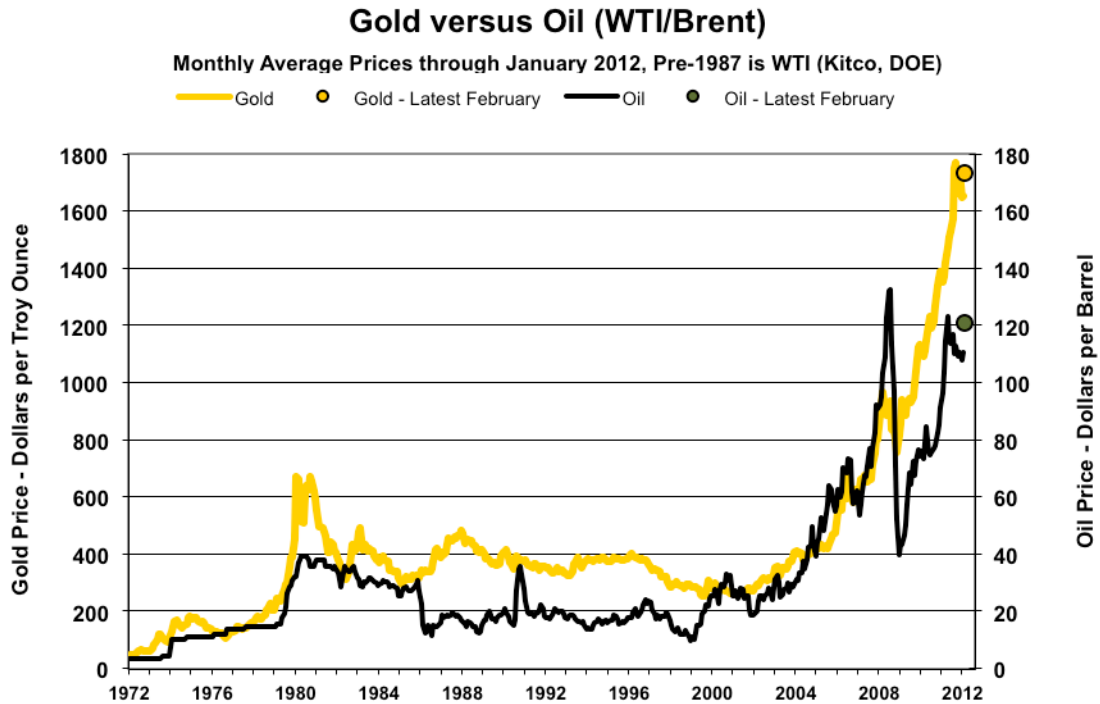
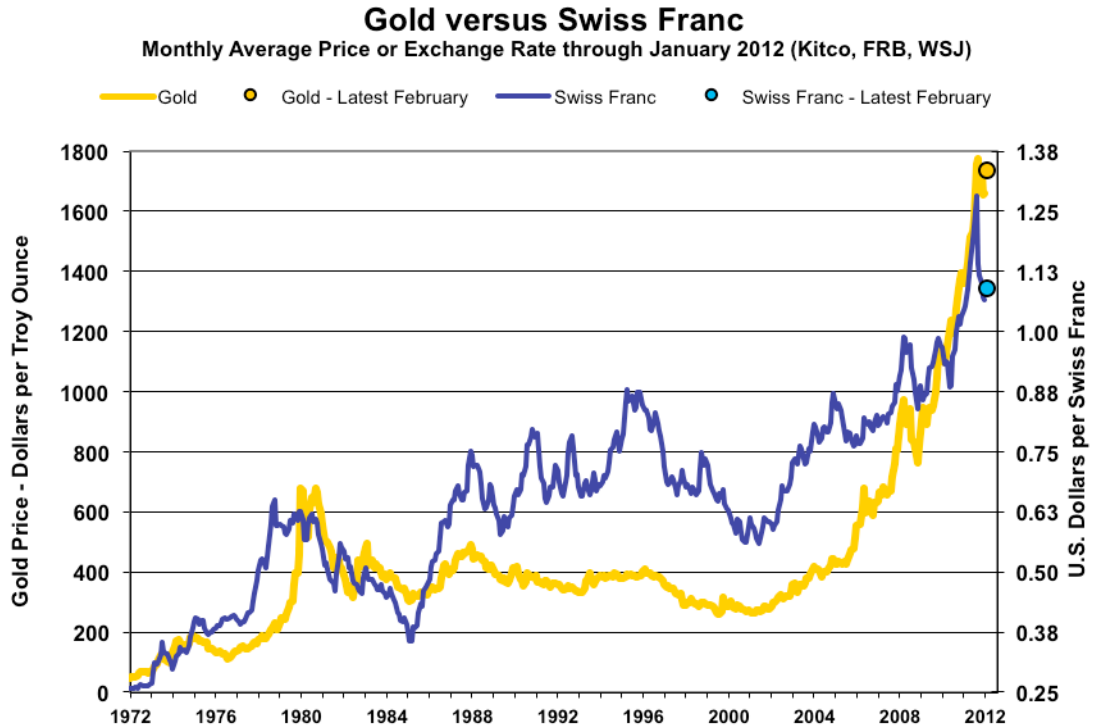
CPI, unstable seasonal factors muted the headline monthly PPI inflation rate, while “core” inflation rose again, month-to-month.

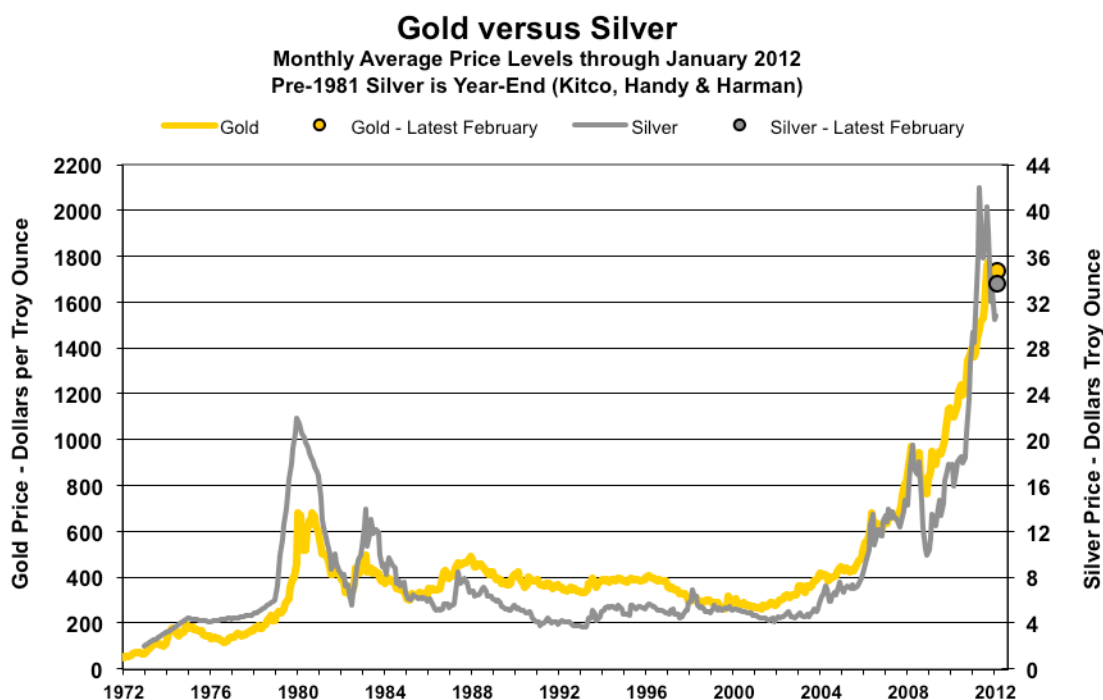
Real (Inflation-Adjusted) Retail Sales. January’s headline 0.38% monthly gain in retail sales was a 0.17% gain after adjustment for monthly CPI-U inflation. Revised December retail sales were flat both before and after inflation adjustment. Annual real growth slowed to 2.83% in January, from 3.16% in December. The downside revision to annualized fourth-quarter real retail sales activity was enough to put some downside pressure on the upcoming first revision to fourth-quarter GDP, due for release on February 29th. Structural issues impairing consumer liquidity continue, with no turnaround in play.

Housing Starts. The housing starts series continued in its fourth year of bottom-bouncing, with a statistically meaningless 1.5% headline monthly gain in January, which followed a revised December decline of 1.9%. The series remains highly volatile and subject to heavy revisions, but there is no turnaround in play.



Updated U.S. Treasury Receipts of Payroll Tax Withholdings. The latest assessment of U.S. Treasury receipts of payroll tax deposits is available at [Payroll Tax Receipts](#). Year-to-year change in tax receipts is running below what would be expected, based on annual bonus payments and based on the growth in earnings and employment as reported by the Bureau of Labor Statistics. Either bonuses are less than expected, or the BLS earnings and employment estimates are overstated. Clarification of the details should be worked out in the post-bonus month of April.





Hyperinflation Watch. Beyond the monthly economic and inflation details covered in this *Commentary*, the economic, inflation and hyperinflation outlooks in [Hyperinflation 2012](#) are not changed.

The preceding charts are the gold-price graphs that are run regularly along with the monthly CPI release. The upside pressure on oil prices, at the moment, largely is from escalating political tensions in the Middle East, not from significant new weakness in the U.S. dollar. Risk remains high, though, of a sharp sell-off in the U.S. dollar and dumping of dollar-denominated paper assets, particularly as the euro area crises come to head and the damages are absorbed, in due course, by the global financial system.

REPORTING DETAIL

CONSUMER PRICE INDEX—CPI (January 2012)

Unusual Seasonal Adjustments to Gasoline Prices Muted Reported CPI Inflation. For the second month, irregular seasonal adjustment patterns have muted gasoline-price inflation as well as aggregate CPI-U reporting. A similar pattern was seen with January PPI reporting. The nature of CPI and PPI seasonal adjustments, however, is that they get revised only once per year, instead of every month as is done in the concurrent seasonal adjustments of payroll employment and retail sales. Accordingly, whatever is short-changed by the CPI seasonals in one month will be restored fully in a later month.

Notes on Different Measures of the Consumer Price Index

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

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

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

*The **C-CPI-U (Chain-Weighted CPI-U)** is an experimental measure, where the weighting of components is fully substitution based. It generally shows lower annual inflation rate than the CPI-U and CPI-W. The latter two measures once had fixed weightings—so as to measure the cost of living of maintaining a constant standard of living—but now are quasi-substitution-based.*

*The **SGS Alternative CPI-U Measures** are attempts at adjusting reported CPI-U inflation for the impact of methodological change of recent decades designed to move the concept of the CPI away from being a measure of the cost of living needed to maintain a constant standard of living.*

CPI-U. The BLS reported today (February 17th) that the headline, seasonally-adjusted January 2012 CPI-U gained 0.21% (up by 0.44% unadjusted) for the month. That followed an unrevised flat reading in December (to the second decimal point, adjusted December CPI-U was up by 0.01%, down by 0.25% unadjusted).

The January 2012 CPI reflected seasonal adjustment factors that were sharply at variance with the adjustments used in 2011 and suggest systemic instability that throws into question the significance of the adjusted month-to-month headline numbers. Using the 2011 seasonal adjustments to gasoline prices, January 2012's headline CPI-U would have been up by 0.33% instead of by 0.21%. January 2012 reporting reflected an unadjusted 3.6% increase in monthly average gasoline prices (the Department of Energy reported an unadjusted 3.4% gain), with the adjusted BLS estimate narrowing to a seasonally-adjusted monthly gain of 0.9%. In January 2011, however, a 3.8% unadjusted monthly gain in gasoline prices narrowed only slightly, to a 3.5% monthly gain, after seasonal adjustment.

Despite the unusual seasonal-adjustment muting of monthly gasoline-price inflation, the January CPI-U still showed the ongoing trend of mounting inflationary pressures from the spread of higher energy prices into the broad economy (see the graph and comments in the *Opening Comments and Executive Summary*). On an annual basis, “core” CPI-U inflation moved higher for the 15th straight month, up to 2.28% in January, from 2.23% in December. When Fed Chairman Bernanke used his jawboning in a successful effort to debase the U.S. dollar in the global markets, in advance of announcing QE2 in November 2010, annual “core” inflation was at 0.61%.

Annual revisions to the seasonally-adjusted monthly CPI-U numbers (the unadjusted numbers never are revised, shy of correcting an outright reporting error) resulted in adjustments to recent annualized quarterly inflation rates. Annualized fourth-quarter 2011 CPI-U was a revised 1.30% (previously 0.94%), down from a revised 3.09% (previously 3.07%) in the third-quarter.

January 2012's unadjusted year-to-year CPI-U inflation eased slightly to 2.93%, from 2.96% in December 2011.

Year-to-year total CPI-U inflation would increase or decrease in next month's February 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the 0.44% gain in the adjusted monthly level reported for February 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for February 2012, the difference in February's headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from January 2012's reported annual inflation rate of 2.93%.

CPI-W. The narrower, seasonally-adjusted CPI-W, which has greater weighting for gasoline than does the CPI-U, also rose by 0.21% (up by 0.47% unadjusted) in January 2012, versus a flat December reading (at the second decimal point, down 0.01%, down by 0.29% unadjusted).

On a seasonally-adjusted basis, the annualized quarterly inflation rate for fourth-quarter 2011 CPI-W was a revised 1.19% (previously 0.79%), down from a revised 3.35% (previously 3.31%) in the third-quarter.

Unadjusted, January 2012's year-to-year CPI-W inflation was 3.15%, versus the 3.20% reported for December 2011.

C-CPI-U. Year-to-year inflation in the January 2012 C-CPI-U eased to 2.60%, from 2.77% in December 2011. The chain-weighted CPI-U is the fully substitution-based series that gets touted as a CPI replacement by inflation apologists and by those who oppose use of the existing CPI-U and CPI-W, including a number of politicians looking to cut deficit spending by using the C-CPI-U to reduce Social Security annual cost of living (COLA) adjustments. The series is reported only on an unadjusted basis.

Alternate Consumer Inflation Measures. Adjusted to pre-Clinton (1990) methodology, annual CPI inflation was roughly 6.3% in January 2012, the same as in in December 2011. The SGS-Alternate Consumer Inflation Measure, which reverses gimmicked changes to official CPI reporting methodologies back to 1980, eased to about 10.5% (10.48% for those using the extra digit) in January 2012, from about 10.6% in December 2011.

The SGS-Alternate Consumer Inflation Measure adjusts on an additive basis for the cumulative impact on the annual inflation rate of various methodological changes made by the BLS (the series is not recalculated). Over the decades, the BLS has altered the meaning of the CPI from being a measure of the cost of living needed to maintain a constant standard of living, to something that neither reflects the constant-standard-of-living concept nor measures adequately most what consumers view as out-of-pocket expenditures. Roughly five percentage points of the additive SGS adjustment reflect the BLS's formal estimate of the annual impact of methodological changes; roughly two percentage points reflect changes by the BLS, where SGS has estimated the impact not otherwise published by the BLS.

Gold and Silver Highs Adjusted for CPI-U/SGS Inflation. Despite the September 5, 2011 historic-high gold price of \$1,895.00 per troy ounce (London afternoon fix), and despite the multi-decade-high silver price of \$48.70 per troy ounce (London fix of April 28, 2011), gold and silver prices have yet to re-hit their 1980 historic levels, adjusted for inflation. The earlier all-time high of \$850.00 (London afternoon fix, per Kitco.com) of January 21, 1980 would be \$2,476 per troy ounce, based on January 2012 CPI-U-adjusted dollars, \$8,890 per troy ounce based on SGS-Alternate-CPI-adjusted dollars (all series not seasonally adjusted).

In like manner, the all-time high price for silver in January 1980 of \$49.45 per troy ounce (London afternoon fix, per silverinstitute.org), although approached in 2011, still has not been hit since 1980, including in terms of inflation-adjusted dollars. Based on January 2012 CPI-U inflation, the 1980 silver price peak would be \$144 per troy ounce and would be \$517 per troy ounce in terms of SGS-Alternate-CPI-adjusted dollars (again, all series not seasonally adjusted).

As shown in Table 1 on page 50 of [Hyperinflation 2012](#), over the decades, the increases in gold and silver prices have compensated for more than the loss of the purchasing power of the U.S. dollar as reflected by CPI inflation, while it has effectively fully compensated for the loss of purchasing power of the dollar based on the SGS-Alternate Consumer Price Measure (1980 Methodologies Base).

Real (Inflation-Adjusted) Retail Sales. Based on the January 2012 CPI-U reporting, inflation- and seasonally-adjusted January 2012 retail sales rose by 0.17% for the month, where, before inflation-adjustment, the current number was up by 0.38% (see [Commentary No. 418](#) for details of the nominal reporting). December real retail sales revised to a virtually unchanged reading, a 0.01% (initially a 0.07%) gain, where the nominal (not-adjusted-for-inflation) number revised to a flat reading (up by 0.02%, previously up by 0.09%).

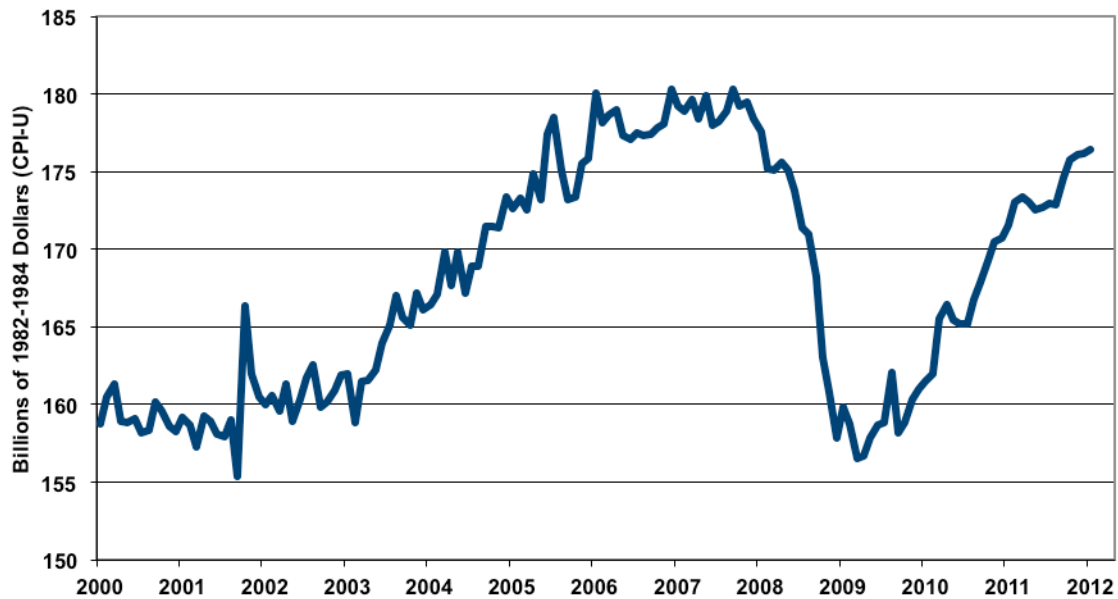
January's real retail sales rose at a slower year-to-year pace of 2.83%, down from a revised 3.16% (previously 3.37%) in December.

The annualized real growth rate for fourth-quarter retail sales slowed to 1.48%, in revision, from initial reporting of 1.67%. That could translate into a slight downward revision in personal consumption growth in the first revision to fourth-quarter GDP, due for release on February 29th.

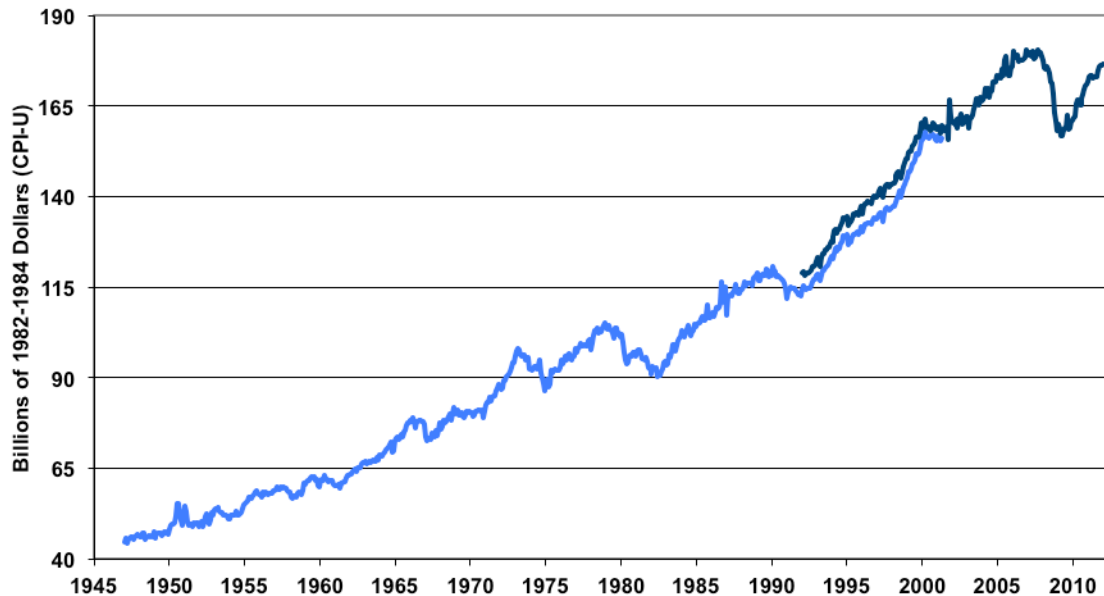
The ongoing “recovery” in real retail sales is reflected in the following graphs, which show the latest monthly levels of CPI- and seasonally-adjusted activity. The first graph shows close historical detail for the period beginning in 2000; the second shows the same data in historical context since World War II.

Using the SGS Alternate-CPI Inflation estimates for deflation of the retail series would not reflect an ongoing rise in activity for the last year or so, but rather an ongoing pattern of bottom-bouncing, as shown and discussed in [Hyperinflation 2012](#) (see Graph 27, page 44). It has been my preference here and wherever otherwise possible, to use the official estimates (the series here is as calculated by the St. Louis Fed), since that eliminates a level of argument over what is being reported. As official consumer inflation picks up further, and as overall retail sales suffer from the ongoing consumer liquidity squeeze, these data should turn down meaningfully in what eventually will become a formal double-dip recession.

Real Retail Sales (Monthly Level)
Through January 2012, Seasonally-Adjusted (SGS, Census)



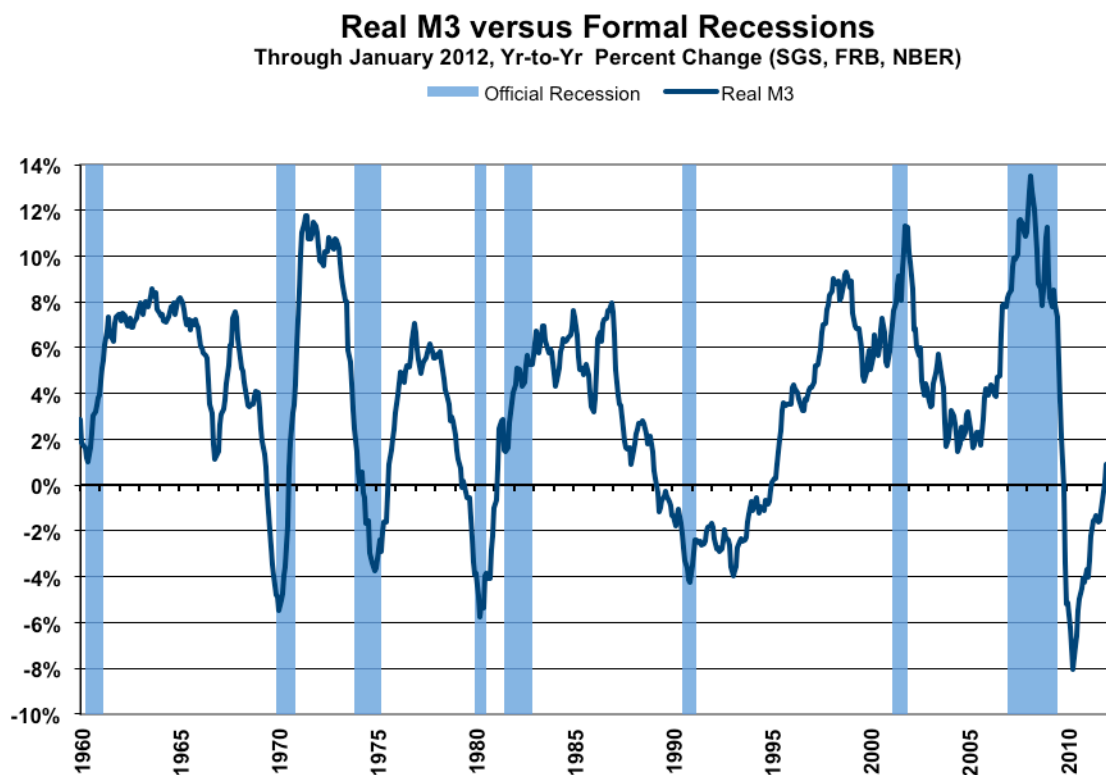
Real Retail Sales (Monthly Level)
Through January 2012, Seasonally-Adjusted (SGS, Census)
— Old Series (1947-2001) — Current Series (1992 to Date)



There has been no change in the underlying fundamentals. There is nothing that would support a sustainable turnaround in retail sales, personal consumption or in general economic activity. There is no recovery, just general bottom-bouncing. Accordingly, real retail sales levels in the months ahead should become increasingly negative (see the household and disposable income comments and the liquidity issues also discussed in *Hyperinflation 2012*).

Real Money Supply M3. The signal for a double-dip or ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), discussed in the in [Hyperinflation 2012](#), remains in place and continues, despite real annual M3 growth having turned to the upside. Based on the January 2012 CPI-U report and the latest January SGS-Ongoing M3 Estimate, the annual growth in real M3 for January 2012 was 1.0%, versus a revised 0.1% (previously 0.3%) gain estimated for December. The rising growth primarily reflects an accelerating pick-up in annual M3 growth.

The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first turns negative in a given cycle; the signal is not dependent on the depth of the downturn or its duration. Breaking into positive territory does not generate a meaningful signal one way or the other for the broad economy. The current downturn signal was generated in December 2009. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of series continued in 2011, and in January 2012 reporting, with a renewed downturn likely to be obvious to most observers in the year ahead, eventually leading to recognition of a double-dip recession.



PRODUCER PRICE INDEX—PPI (January 2012)

January's PPI Muted by Unusual Oil-Price Seasonal Adjustments. As reported yesterday, February 16th, by the Bureau of Labor Statistics (BLS), the regularly-volatile, seasonally-adjusted finished-goods producer price index (PPI) for January 2012 notched higher by 0.1% (up by 0.3% unadjusted), following a 0.1% month-to-month decline (down by 0.4% unadjusted) in December 2011. The January result was in the context of revised seasonal factors and a revamped weighting of PPI components.

While the effects of the revisions on the aggregate finished goods numbers appeared to be minimal, energy inflation seasonal adjustments were unusually unstable in the January data. January 2012 finished energy goods rose by 0.3%, unadjusted, for the month, which became a 0.5% contraction after seasonal adjustment. In contrast, finished energy goods in January 2011 rose by 1.6% unadjusted, which became a 1.8% increase after seasonal adjustment. January's low inflation number was dominated by that unusual adjustment pattern.

The monthly "core" PPI—net of food and energy—jumped by 0.4% in January, however, up from 0.3% in December, reflecting the still spreading impact of higher oil costs throughout the broad economy. Year-to-year "core" held at 3.0% year-to-year (unadjusted) in January, against initial reporting of 3.0% in December.

Unadjusted and year-to-year, January 2012's total finished goods PPI inflation eased to 4.1% from 4.8% in December. The relatively high level of annual PPI inflation generally still reflects ongoing impact of the Fed's dollar-debasement policies, not surging economic demand. Annual changes now are going against the year-ago period when Mr. Bernanke was running QE2 and meeting with early success in debasing the U.S. Dollar.

The revisions, however, had greater pact at the intermediate and crude-good-levels. On a monthly basis, seasonally-adjusted January intermediate goods prices fell by 0.4%, versus a revised 0.2% (previously 0.5%) decline in December, with January crude goods prices up by 1.5%, following a revised 1.5% (previously 1.1%) decline in December. Year-to-year inflation in unadjusted January intermediate goods was 4.2%, versus an unrevised 6.1% in December, with January's annual inflation in crude goods at 4.5%, versus an unrevised 6.4% in December.

RESIDENTIAL CONSTRUCTION (January 2012)

Housing Starts Continued Bottom-Bouncing. Housing starts showed a statistically-meaningless monthly upside bounce in January, reflecting another monthly reversal (to the upside in this case) in the highly volatile activity in apartment starts. Indeed, the regularly volatile aggregate housing starts series continued its protracted bottom-bouncing in January's reporting. With the series into its fourth year of activity at 75% below 2006's record construction level, there remains no relief in sight.

The Census Bureau reported yesterday (February 16th) a statistically-insignificant month-to-month increase in seasonally-adjusted January 2012 housing starts of 1.5% (up 6.4% before prior-period

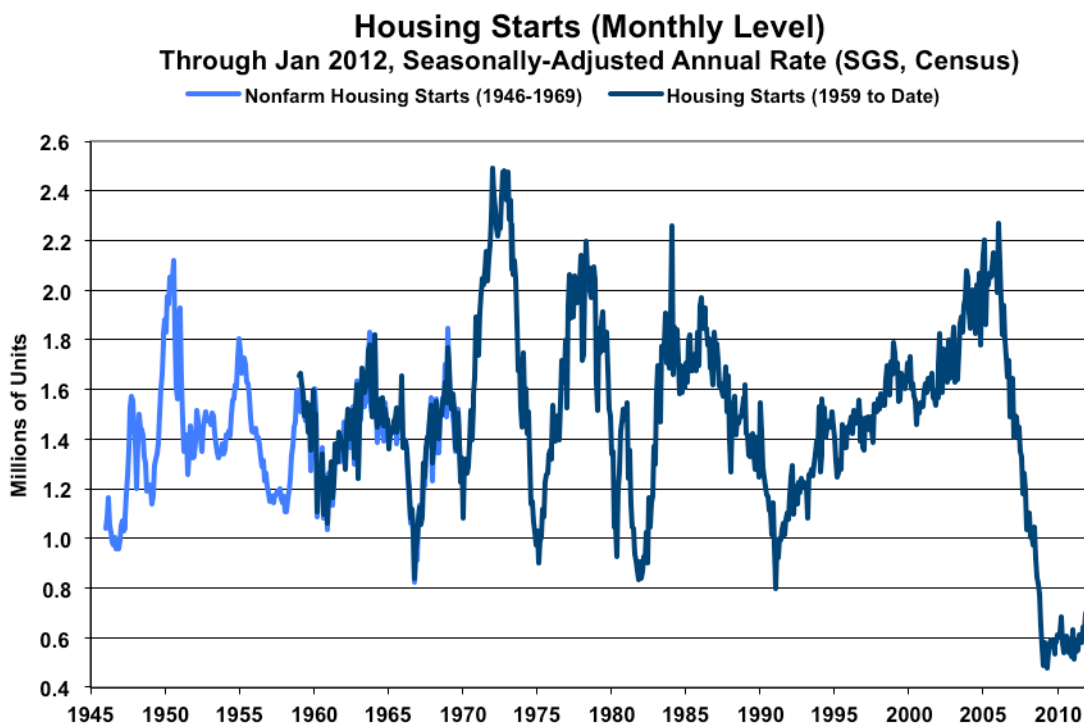
revisions) +/- 19.9% (all confidence intervals are at the 95% level). December starts were revised to a monthly decline of 1.9% (previously a drop of 4.1%).

Starts for apartment buildings remained extremely volatile, month-to-month, jumping by a statistically meaningless 14.4%, after falling by 34.9% (previously 27.8%) in December.

The year-to-year change in aggregate January housing starts was a statistically-insignificant increase of 9.9% +/- 16.6%, following a revised 32.9% (previously 24.9%) annual gain in December.

Indeed, the pattern of housing starts has remained one of stagnation at an historically low-level plateau of activity, over the last 38 months. Since December 2008, housing starts have averaged a seasonally-adjusted annual rate of 586,000. In that period, all monthly readings have been within the normal range of monthly variability for the aggregate series around that average, with the 699,000 January 2012 monthly reading at 19.3% above average.

As shown in the following graph, current monthly housing starts activity remains off the record monthly low seen for the present series in April 2009. The current number also is well below any level reported in the predecessor nonfarm housing starts series, which was introduced in 1946. The usual graph showing detail from 2000 to date is included in the *Opening Comments and Executive Summary*.



Week Ahead. Recognition of an intensifying double-dip recession as well as an escalating inflation problem remains sporadic. The political system would like to see the issues disappear until after the election; the media does its best to avoid publicizing unhappy economic news; and the financial markets will do their best to avoid recognition of the problems for as long as possible, problems that have horrendous implications for the markets and for systemic stability.

Until such time as financial-market expectations move to catch up fully with underlying reality, or underlying reality catches up with the markets, reporting generally will continue to show higher-than-expected inflation and weaker-than-expected economic results in the months and year ahead. Increasingly, previously unreported economic weakness should show up in prior-period revisions.

Home Sales (January 2012). January 2012 existing home sales data are due for release on Wednesday, February 22nd, from the National Association of Realtors. New home sales are due for release from the Census Bureau on Friday, February 24th. Following the pattern of activity in housing starts, both series likely will continue their patterns of bottom-bouncing, and the monthly results are not likely to be statistically meaningful.
