

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

**COMMENTARY NUMBER 459**  
**Second-Quarter GDP, Annual GDP Revisions**

**July 28, 2012**

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**GDP Revisions Showed a Later “Full Recovery” with Shifted Growth Patterns**

**Double-Dip Downturn Looms**

**Velocity of Money (M3) Is Rising**

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*PLEASE NOTE: The next regular Commentary is scheduled for Wednesday, August 1st, covering the June PCE deflator and construction spending. A subsequent Commentary on Friday, August 3rd, will cover the July report on employment and unemployment reporting.*

*Best wishes to all — John Williams*

**Opening Comments and Executive Summary.** Economic activity slowed in second-quarter 2012. Reflected in real (inflation-adjusted) gross domestic product (GDP) reporting, headline growth slowed from a revised 2.0% in the first-quarter to 1.5% in the second-quarter. As usual, both first- and second-quarter gains were statistically insignificant. The government’s margin of reporting error allows for those quarter-to-quarter changes easily to be contractions, instead of the official gains that reverberate through the popular media and the financial markets.

Accompanying the initial estimate of second-quarter GDP were GDP revisions for the limited period of first-quarter 2009 to first-quarter 2012. With the onset of the revision period being in the midst of the

greatest domestic economic crash since the Great Depression, the results likely were heavily distorted. Still, a clearer official picture of the economic collapse will not be available until the next full benchmark revision, which is not imminent. The revisions shifted real growth from 2010 back into 2009, muting patterns of previously-reported peak and trough year-to-year growth. On a relative basis, 2011 annual growth was little changed, with a net negative impact on revamped historical GDP activity through 2011.

That said, some unusual patterns and related underlying assumptions—in the fourth-quarter 2011 to second-quarter 2012 period—appear to have been aimed at protecting the illusion of recovery. The so-called full-recovery—where real GDP activity first topped pre-recession levels—was revised into fourth-quarter 2011, from third-quarter 2011.

In the *Hyperinflation Watch* section, the velocity of money is updated for M2 and M3. The M2 velocity continues to fall, while M3 velocity continues to rise. The difference is that growth in M2, a component of the broader M3, has been growing faster than M3.

Also, the general outlook is updated. While the broad outlook is unchanged, fundamentals keep pummeling economic activity into what increasingly is being recognized as a double-dip recession, while events keep pushing the U.S. financial system ever closer to the ultimate dollar disaster: an outright collapse in the dollar's purchasing power.

***Second-Quarter 2012 GDP.*** *Note: As usual, the finer detail from the quarterly GDP release is covered in the Reporting Detail section. Summary results and the “inflation-corrected” GDP detail are included in this section. The primary analysis of the annual GDP revisions is covered in the section following.*

Headline real GDP growth was 1.5% in the second-quarter, down from a revised 2.0% (previously 1.9%) in the first-quarter. Year-to-year real growth slowed to 2.2% in the second-quarter, from a revised 2.4% (previously 2.0%) in the first-quarter.

GDP inflation—the implicit price deflator (IPD)—was reported at an annualized quarter-to-quarter rate of 1.5% in the second-quarter, down from a revised 2.2% (previously 2.0%) in the first-quarter. Year-to-year, IPD inflation was 1.7% in the second-quarter, versus an unrevised 2.0% in the first-quarter. As discussed below, IPD inflation is understated, which has the effect of overstating real growth.

Updated Inflation-Corrected GDP Graphs. The following graphs incorporate the annual GDP revisions and the initial estimate of second-quarter 2012 GDP. *Graph 1* reflects official reporting with the real GDP level—as deflated by the IPD—indexed to 1q2000 = 100. The dark, narrow line reflects the revised data, the lighter, background line is the old series.

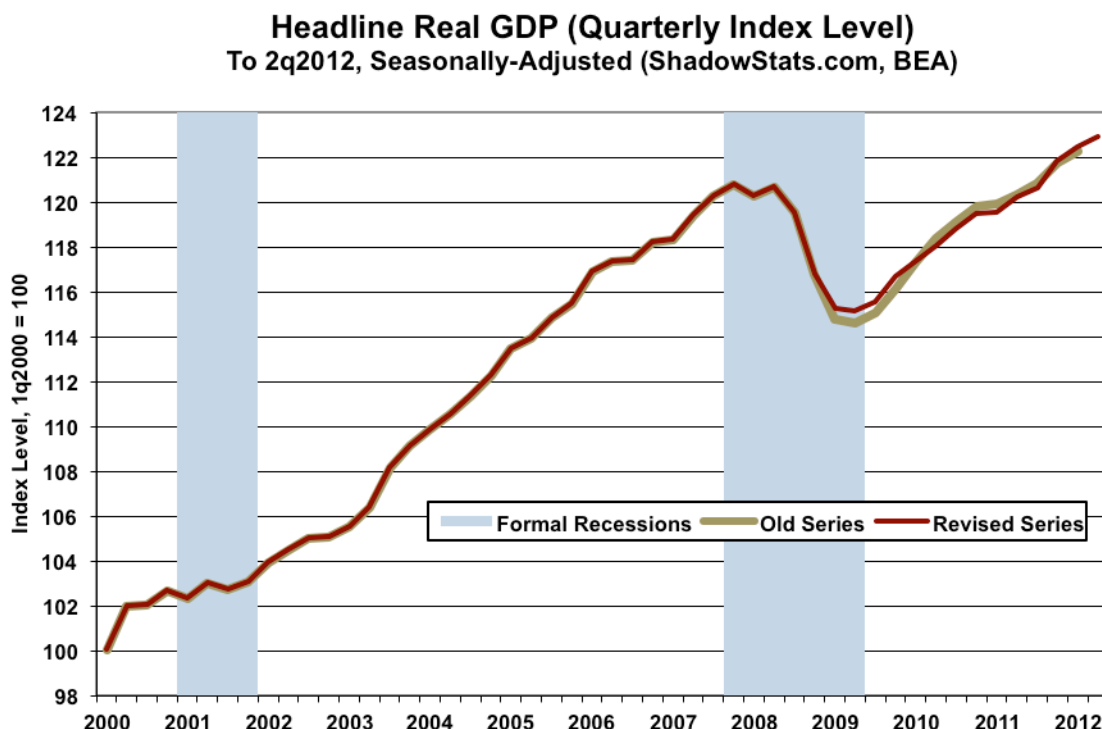
Note that the recent full-recovery of real GDP activity—versus pre-recession levels—survived the revisions. It is shown now, however, as having happened a quarter later than before, in fourth-quarter 2011, instead of the third-quarter. No other major economic series supports the GDP's pattern of full recovery, and that raises serious issues as to GDP reporting quality.

As suggested in the *Graph 2*, which is inflation-corrected, the recovery is nothing but an illusion created by the use of too-low inflation estimates in deflating series such as the GDP (see [Public Comment on Inflation](#)). It is the same as *Graph 1*, but the IPD has been adjusted to add back roughly two-percentage points of annual inflation estimated to have been lost due to methodological changes of recent decades,

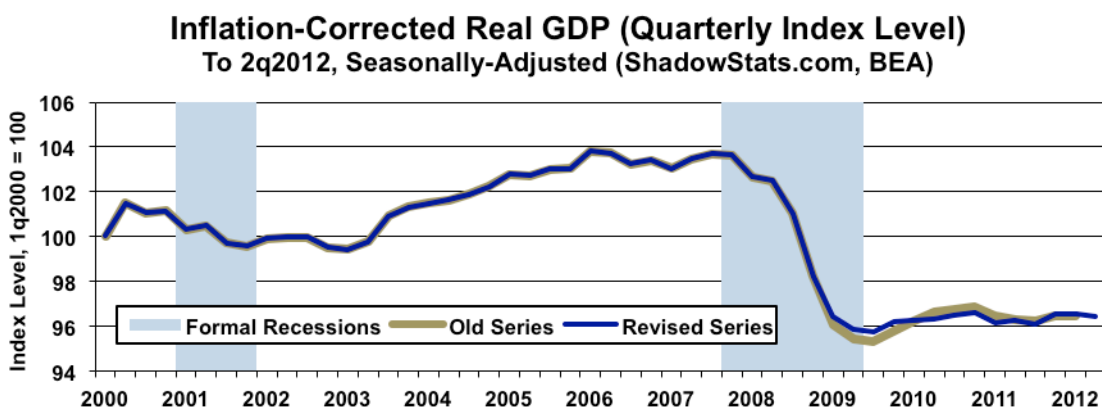
specifically, the use of hedonic quality adjustments (see discussion in [Hyperinflation 2012](#) and [Special Report No. 445](#)). Both *Graphs 1* and *2* are plotted to the same scale for purposes of comparison.

Of note, the shifting of activity from 2010 to 2009 in the revisions leaves the revised, inflation-corrected series showing more of a flat-line bottom-bouncing—subsequent to the economic collapse—than before.

*Graph 1*



*Graph 2*



**Annual GDP Revisions.** The annual GDP revisions—back to first-quarter 2009—did not alter the previous official reporting meaningfully, or the government’s official GDP story, fundamentally. Plotted

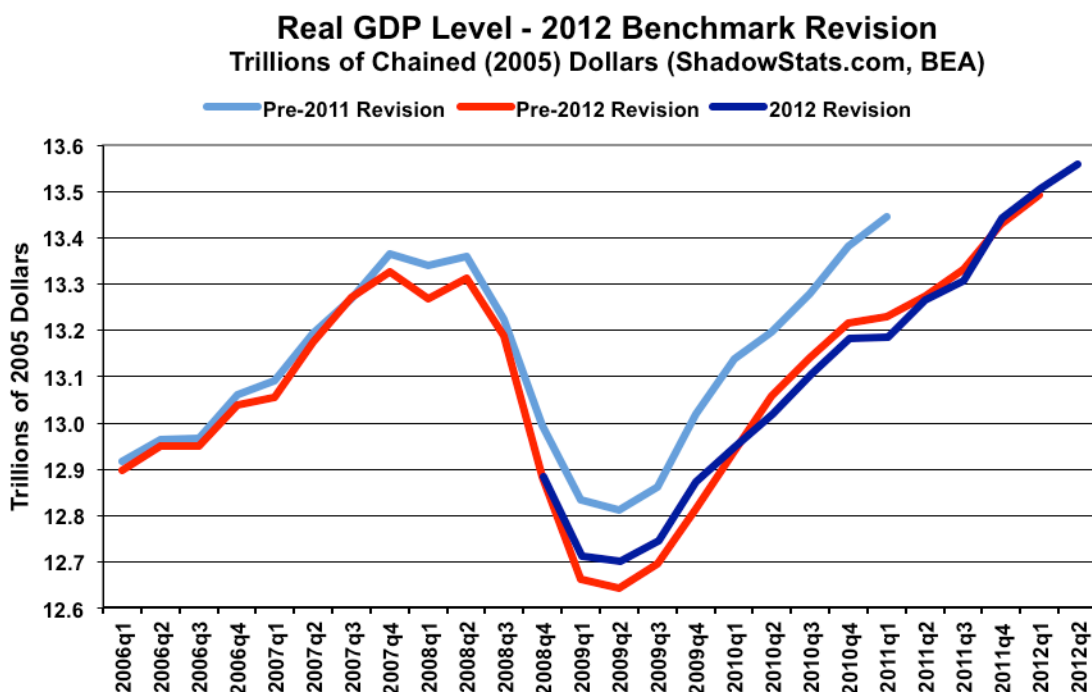
in *Graph 3* are the levels of real (inflation-adjusted) GDP activity both before and after the 2012 revisions, and also before the 2011 annual revisions. The 2012 revisions were smaller than the 2011 (pre-2012) revisions and basically shifted activity from 2010 back into 2009.

Shifting Growth Patterns. The real annual change in full-year 2009 GDP, versus 2008, revised to a 3.07% contraction (previously a 3.49% decline), 2010 annual growth revised to a 2.39% gain (previously 3.03%), and 2011 annual growth revised to 1.81% (previously 1.74%), with a net-negative revision of 0.12% to the real GDP level for 2011, versus prior reporting. The new 2009 annual contraction of 3.07% still was the worst on record since the post-war wind-down of industrial production in 1946, as shown in *Graph 13* in the *Reporting Detail* section.

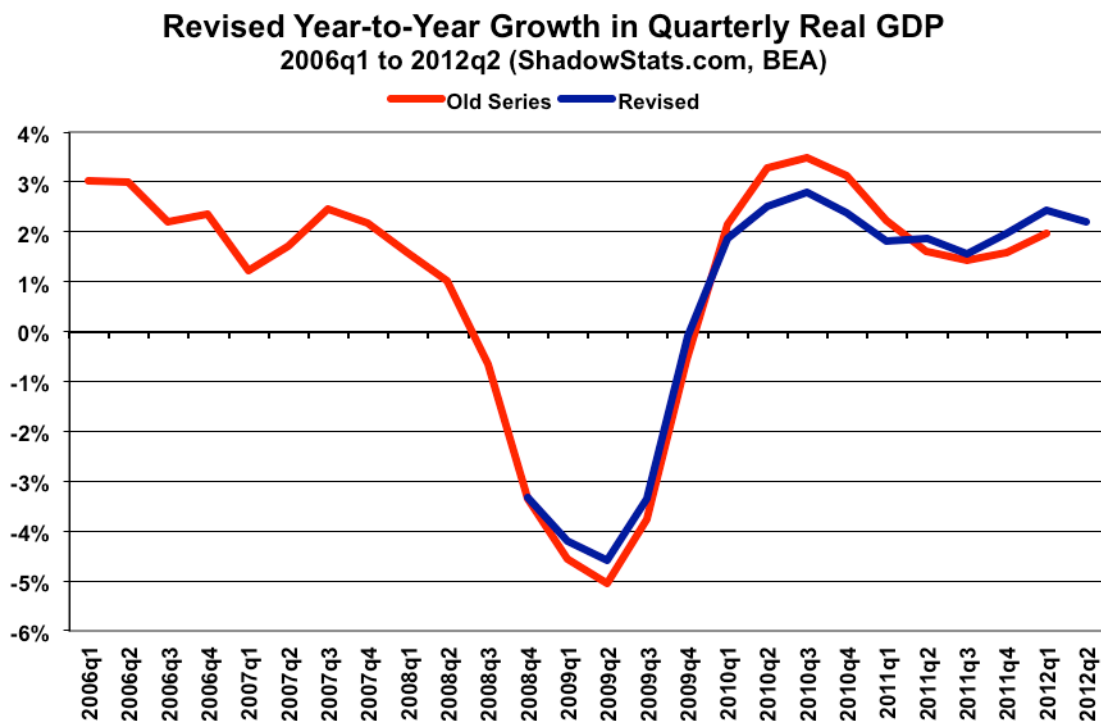
The shifting growth patterns had the effect of dampening both the recent trough and peak in year-to-year real GDP growth, as shown in *Graph 4* of the revisions to year-to-year GDP growth. The latest year-to-year growth of 2.21% was off the revised near-term peak growth of 2.80% (previously 3.51%) reported during third-quarter 2010. The cycle trough in second-quarter 2009 also was revised, to a 4.58% year-to-year decline (previously a 5.03% drop). Nonetheless, the cycle trough remained the deepest annual contraction seen for any quarterly GDP in the history of the series, which began with first-quarter 1947 (see *Graph 12* in the *Reporting Detail* section).

As noted earlier, these revisions—purporting to show a slightly shallower downturn—are highly suspect, given that the revision period started with first-quarter 2009, right in the middle of the economic collapse. More-accurate reporting awaits more extensive and thorough prior-period revisions.

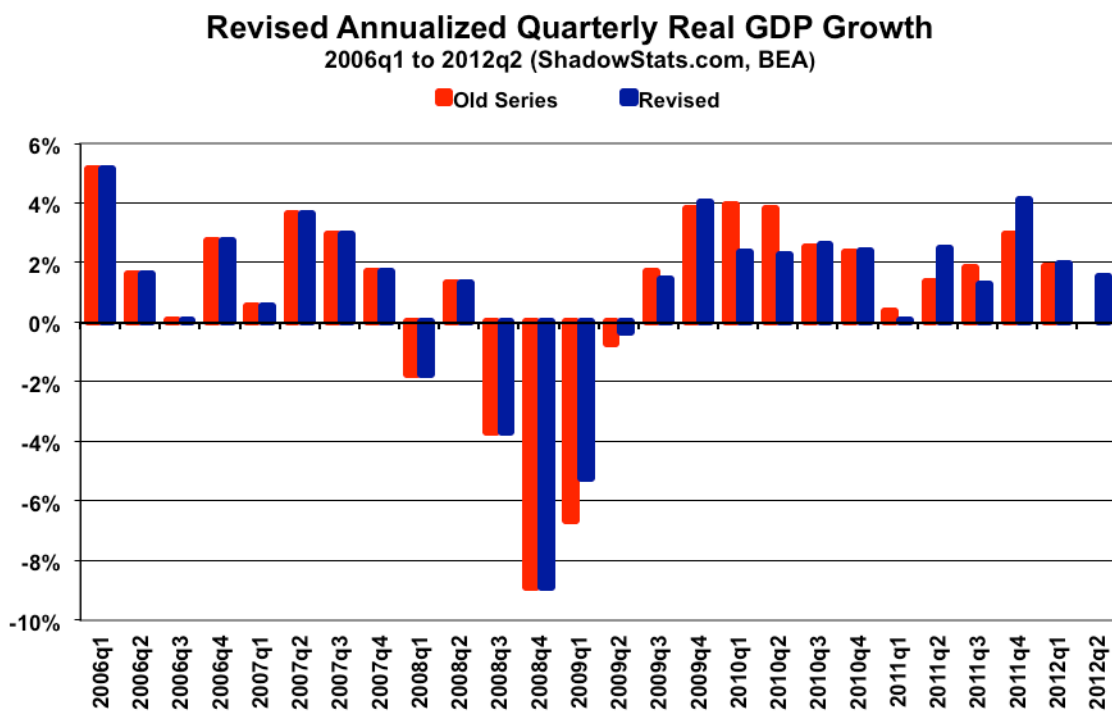
**Graph 3**



*Graph 4*



*Graph 5*



*Graph 5* shows the revised headline or annualized quarterly real GDP growth. The only credible revisions here are the ones that show downside changes in 2010 growth, as suggested by recent benchmark revisions to fundamental series that underlie GDP reporting. The big upside revision to fourth-quarter 2011 appears to be a gimmick aimed at propping up the illusion of full-recovery.

Revised GDP Graphs of 2007 Recession. The following series of graphs show the revisions and prior reporting in detail, with the plots beginning with fourth-quarter 2007, the official onset of the recession. *Graphs 6* and *7* first show the nominal (not-adjusted-for-inflation) and the real (inflation-adjusted) series. Note that the nominal revisions were negligible, which means that the bulk of the revisions to the real series were based on changes in the IPD—the GDP’s rate of inflation.

Revised GNP. The revisions to real gross national product (GNP), as shown in *Graph 8*, tended to run with the GDP, except for the pre-benchmark, first-quarter 2012 faltering of the GNP series, which has been revised away. The BEA will not publish its initial estimate of second-quarter 2012 GNP for at least another month. GNP is the broadest measure of U.S. economic activity, where GDP is GNP net of trade in factor-income, or interest and dividend payments.

Revised GDI. Gross domestic income (GDI) is the income-side reporting equivalent of the consumption-side GDP. As shown in *Graph 9*, the revisions to real GDI activity all were to the downside and generally were much more pronounced than the GDP and GNP changes. Where the GDP and GDI are supposed to be equal, they rarely are, given their separate surveys and compilations. The difference between them is added as a “statistical discrepancy” to the GDI side, in order to have both sides equal. Usually, and in theory, the statistical discrepancy between the GDP and GDI narrows in a benchmark revision, where more complete data are available. Here, however, the discrepancy widened.

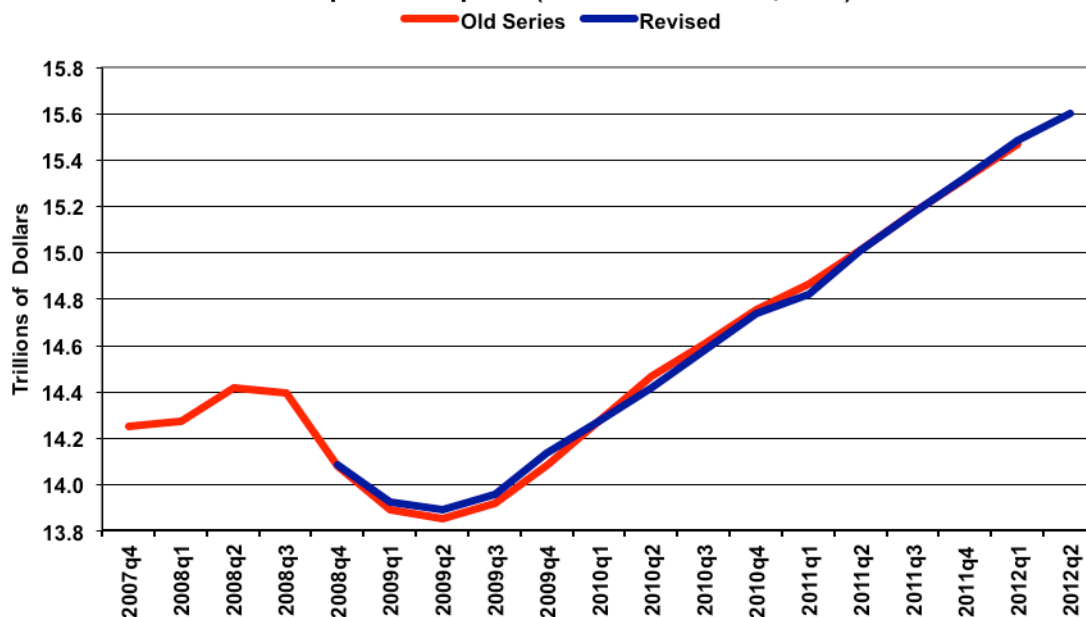
This GDI series receives little press coverage. Accordingly, it is not massaged as heavily as is the GDP series, and it likely is a better reflection of underlying reality.

Real Disposable Personal Income (DPI). Finally, as seen in *Graph 10*, there were significant and unstable—generally downside—revisions to real disposable income. Details on the games being played here by the BEA will be explored in the August 1st *Commentary*, which will cover the July 31st annual revisions to the monthly data. Detail on the current quarterly reporting is covered in the *Reporting Detail* section.

As noted in earlier writings, in the twenty presidential elections since the first publication of annual disposable income data in 1929, no incumbent party has retained the White House when annual real disposable income growth has been below 3.0% in the presidential election year. The 2012 circumstance is developing, so far, strongly against the incumbent party for the November election. Again, further detail will follow in the August 1st *Commentary*.

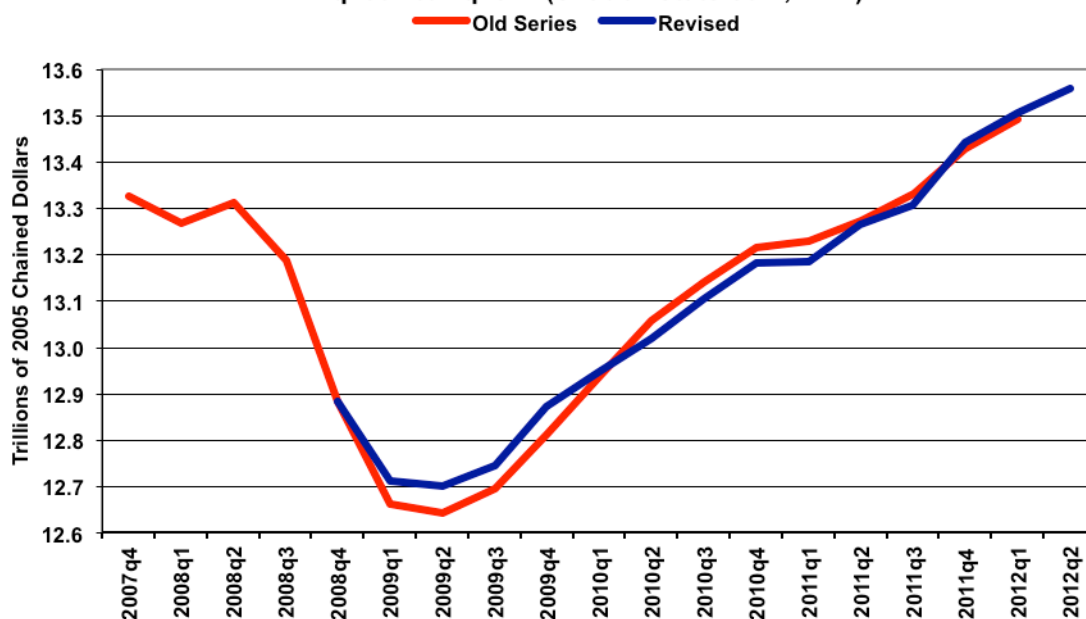
*Graph 6*

**Nominal GDP Level - 2012 Benchmark Revision**  
4q2007 to 2q2012 (ShadowStats.com, BEA)



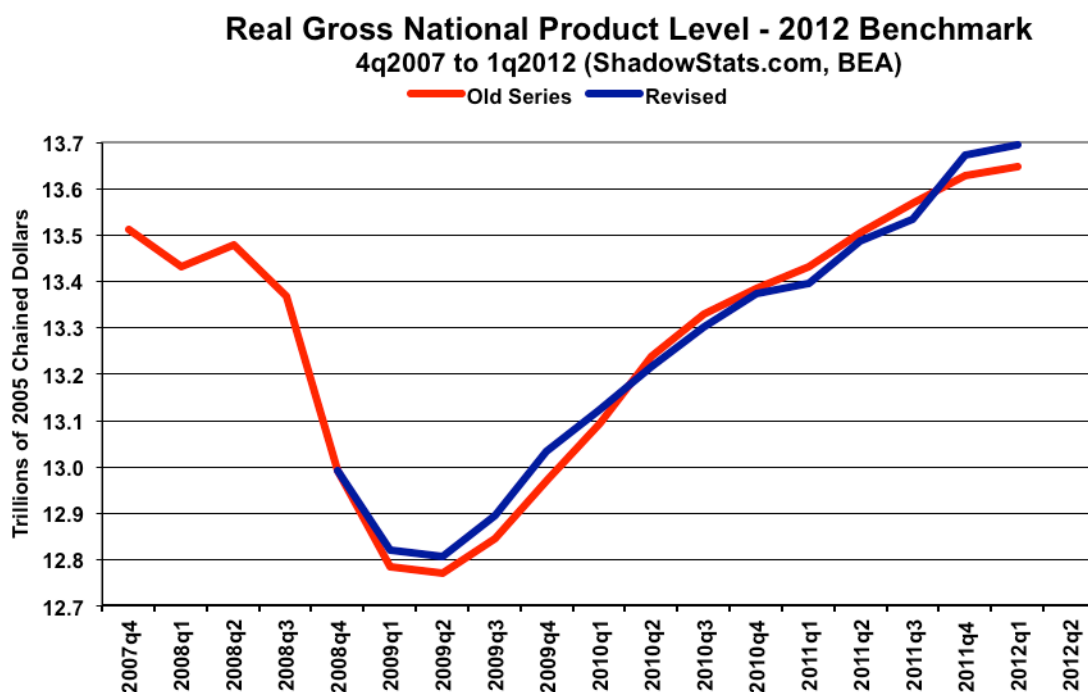
*Graph 7*

**Real GDP Level - 2012 Benchmark Revision**  
4q2007 to 2q2012 (ShadowStats.com, BEA)

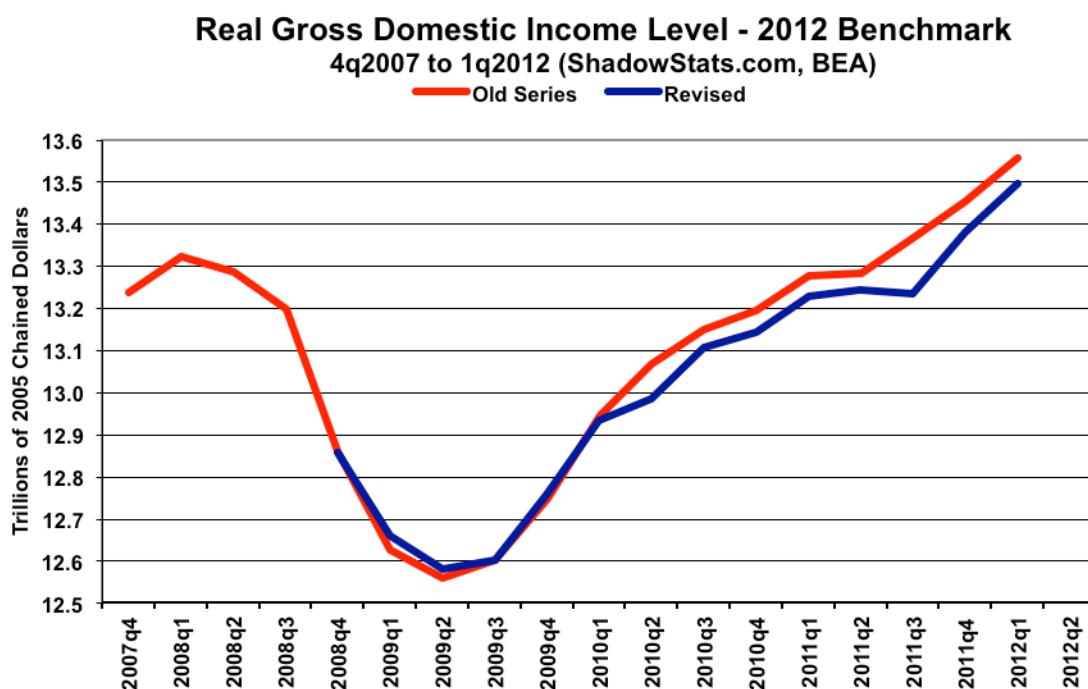




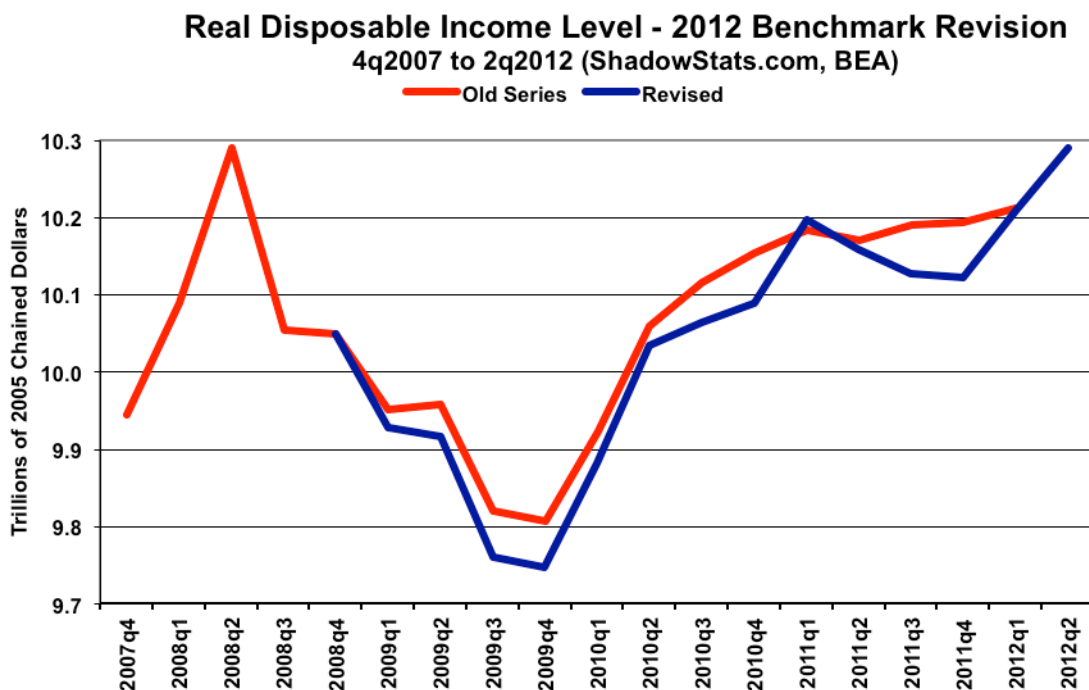
*Graph 8*



*Graph 9*





**Graph 10**

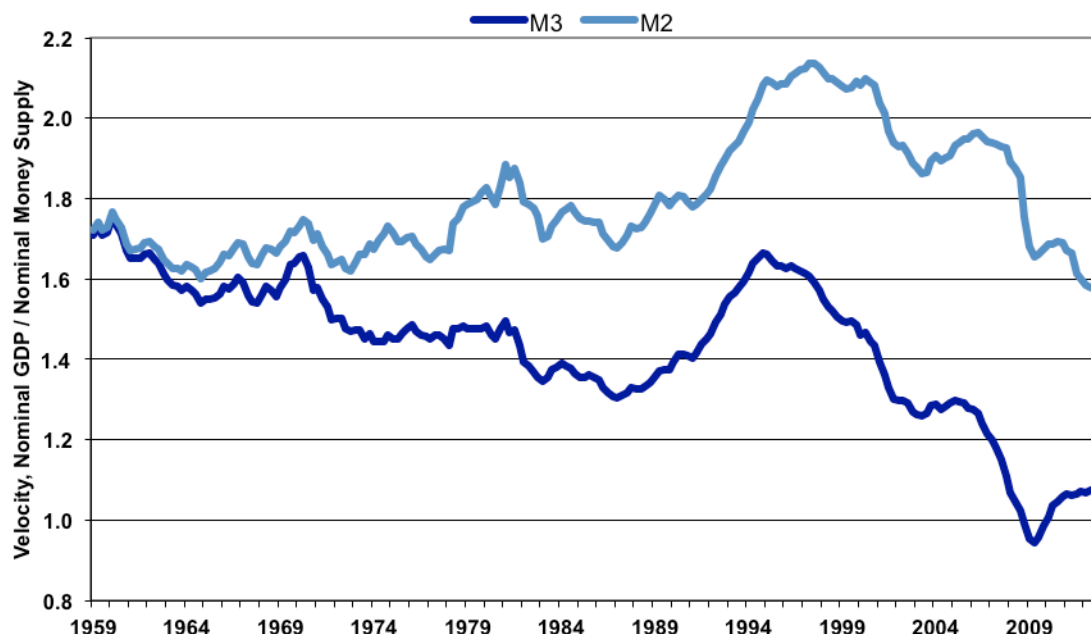
**Hyperinflation Watch—Rising M3 Money Velocity, Updated Outlook.** Incorporating the revised nominal GDP data, as well recent revisions to underlying money data published by the Federal Reserve, current estimates of money velocity for money supply M2 and M3 are published and graphed in the next section. Velocity continues to fall for M2, but M3 velocity has been rising for the last three years.

Separately, with the GDP revisions in place, the general economic and systemic outlooks are reviewed. While the broad outlook is unchanged, fundamentals keep pummeling economic activity into what eventually be recognized as a double-dip recession, while events keep pushing the U.S. financial system ever closer to the ultimate dollar disaster: an outright collapse in the dollar's purchasing power.

**M3 Velocity Is on the Rise.** Subscribers regularly raise questions as to what is happening to the velocity of money, and the following is in response. The nature of velocity is discussed in some detail in the 2008 [Money Supply Special Report](#). Velocity simply is the number of times the money supply turns over in the economy in a given year, or the ratio in nominal terms (not adjusted for inflation) of GDP to the money supply. At present, the velocity of M2 is falling, but the velocity of M3 (using the SGS Ongoing-M3 Measure) is rising, as shown in *Graph 11*. Since the annual revisions to nominal GDP were minimal (see *Graph 6*), the plots of velocity shown in the following graph show only the revised data.

*Graph 11*

**Velocity of M3 and M2 (1q1959 to 1q2012)**  
ShadowStats.com, FRB, BEA



Velocity has theoretical significance, where, in combination with money supply growth, it should be a driving force behind inflation. Yet, since velocity is ratio of two numbers that are not particularly well or realistically measured, I do not put much weight in its actual estimate, and as an inflation predictor, it has to be viewed in the context of accompanying money supply growth.

M3 velocity hit its near-term peak in first-quarter 2005, bottomed in second-quarter 2009 and generally has been flat or rising since. M2 velocity hit its near-term peak in second-quarter 2006, and other than for a brief bump, it has been declining since.

M3 and M2 currently are showing opposite patterns, because the growth in M3 has been much weaker than growth in M2. The reason behind the difference largely is that much of the relatively stronger M2 growth has reflected cash moving out of M3 categories—such as large time deposits and institutional money funds—into M2 or M1 accounts. M3 contains M2, and M2 contains M1. The effect of the funds shift has no impact on M3, but it spikes M2 growth. The clarity of what is happening here is why I like to follow the broadest money measure available. Again, full definitions can be found in the [Money Supply Special Report](#), which I expect to update in the next several months as to data used; the principles remain same

**General Outlook.** *General circumstances have not changed, with the broad outlook discussed in detail in [Special Report No. 445](#) (June 12th), which updated the hyperinflation outlook and the outlook for U.S. economic, U.S. dollar, and systemic-solvency conditions. That Special Report supplemented*

[Hyperinflation 2012](#) (January 25th), which remains the primary Commentary detailing the hyperinflation story.

Revised official GDP reporting still shows plunging economic activity from fourth-quarter 2007 to second-quarter 2009 (the 2012 annual revisions did not pre-date first-quarter 2009), with an ensuing upturn in activity that led to a full recovery as of fourth-quarter 2011 (revised from the previously estimated third-quarter 2011 full recovery), and that recovery has continued through initial second-quarter 2012 reporting.

In contrast to GDP reporting—and in line with patterns seen in better-quality economic series—I still contend the economy began turning down in 2006, plunging in 2008 into 2009 and subsequently stagnating—bottom-bouncing—at a low level of activity ever since. There has been no recovery since mid-2009, and the economic downturn now is intensifying once again. The renewed slowdown is evident in the current reporting of nearly all major economic series. Not one of those series shows a pattern of activity that confirms the recovery evident in the GDP series.

As shown in the *Opening Comments and Executive Summary*, the official recovery simply is a statistical illusion created by the government's use of understated inflation in deflating the GDP, which has the result of overstating economic growth (see [Special Report No. 445](#)).

The long-term fiscal solvency issues of the United States—where GAAP-based accounting shows annual deficits running in the \$5 trillion range—are not being addressed, and the politicians currently running the government lack the political will to address those issues. That circumstance initially suggested a hyperinflation crisis by the end of this decade, but federal government and Federal Reserve actions—in response to the systemic-solvency crisis of 2008—accelerated the process, indicating a hyperinflation problem by no later than the end of 2014. The continuing economic downturn is intensifying the fiscal- and systemic-solvency problems.

Neither economic nor systemic-solvency issues have been resolved by U.S. government or Federal Reserve actions. With the economy weak enough to provide cover for further Fed accommodation to the still-struggling banking system, the next easing by the Fed—possibly as early as the week ahead—likely will lead to a massive dollar selling crisis and that will begin the process of a rapid upturn in domestic consumer inflation.

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## REPORTING DETAIL

### GROSS DOMESTIC PRODUCT—GDP (Second-Quarter 2012 - First Estimate, Annual Revisions)

**Second-Quarter GDP Growth Was Little More than Statistical Noise; Benchmark Revisions Shifted Growth Around But Did Not Alter Outlook.** The initial estimate of headline GDP growth for second-quarter 2012 was 1.5%, down from a benchmark revised 2.0% (previously 1.9%) in the first-quarter and from a nonsensical 4.1% (previously 3.0%) in the fourth-quarter. When all the dust settles on recent

reporting of economic and business activity, inventory policies of the U.S. automotive industry likely will be under question, along with quality issues surrounding the GDP's implicit price deflator, which is used in estimating real, or inflation-adjusted, economic growth.

Net of estimated changes in inventory building, second-quarter headline growth was 1.2%, versus 2.4% in the first-quarter and 1.6% in the fourth-quarter. As discussed and graphed in the *Opening Comments and Executive Summary* section and in [Hyperinflation 2012](#) and [Special Report No. 445](#), the “recovery” is an illusion created by the use of understated inflation in deflating key dollar-denominated series, such as the GDP. The lower the rate of inflation that is used for the deflator, the stronger is the reported inflation-adjusted growth. Net of that inflation understatement, the revised “inflation-corrected” version of real GDP shows that economy activity has been virtually flat, at a low-level plateau activity since the economy crashed from 2006/2007 into 2009.

The benchmark revisions also are discussed and graphed in the *Opening Comments and Executive Summary*. The revisions largely were reflected in changes to inflation estimates, muting the peak and trough in annual growth contained in the 2009-to-date restricted period of revisions, with growth being shifted from 2010 back into 2009. Further, the new numbers likely are distorted heavily by the beginning of the revision period falling right the middle of the economic collapse. At such time as there is the next full benchmark revision, perhaps a more meaningful picture of economic activity will be brought forth, one where the “recovery” in GDP is reflected in other major series as well

Consistent with this regular overstatement of broad economic activity by the Bureau of Economic Analysis (BEA), the GDP series remains the most worthless and the most heavily politicized of the government's popularly followed economic reports.

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### **Notes on GDP-Related Nomenclature and Definitions**

*For purposes of clarity and the use of simplified language in the text of the GDP analysis, here are definitions of several key terms used related to GDP reporting:*

**Gross Domestic Product (GDP)** is the headline number and the most widely followed broad measure of U.S. economic activity. It is published quarterly by the Bureau of Economic Analysis (BEA), with two successive monthly revisions, and with an annual revision in the following July.

**Gross Domestic Income (GDI)** is the theoretical equivalent to the GDP, but it generally is not followed by the popular press. Where GDP reflects the consumption side of the economy and GDI reflects the offsetting income side. When the series estimates do not equal each other, which almost always is the case, since the series are surveyed separately, the difference is added to or subtracted from the GDI as a “statistical discrepancy.” Although the BEA touts the GDP as the more accurate measure, the GDI is relatively free of the monthly political targeting the GDP goes through.

**Gross National Product (GNP)** is the broadest measure of the U.S. economy published by the BEA. Once the headline number, now it rarely is followed by the popular media. GDP is the GNP net of trade in factor income (interest and dividend payments). GNP growth usually is weaker than GDP growth for net-debtor nations. Games played with money flows between the United States and the rest of the world tend to mute that impact on the reporting of U.S. GDP growth.

**Real (or Constant Dollars)** means the data have been adjusted, or deflated, to reflect the effects of inflation.

**Nominal** (or **Current Dollars**) means growth or level has not been adjusted for inflation. This is the way a business normally records revenues or an individual views day-to-day income and expenses.

**GDP Implicit Price Deflator (IPD)** is the inflation measure used to convert GDP data from nominal to real. The adjusted numbers are based on “Chained 2005 Dollars,” at present, where the 2005 is the base year for inflation, and “chained” refers to the methodology which gimmicks the reported numbers so much that the total of the deflated GDP sub-series misses the total of the deflated total GDP series by nearly \$107 billion in “residual” as of fourth-quarter 2011.

**Quarterly** growth, unless otherwise stated, is in terms of seasonally-adjusted, annualized quarter-to-quarter growth, i.e., the growth rate of one quarter over the prior quarter, raised to the fourth power, a compounded annual rate of growth. While some might annualize a quarterly growth rate by multiplying it by four, the BEA uses the compounding method, raising the quarterly growth rate to the fourth power. So a one percent quarterly growth rate annualizes to  $1.01 \times 1.01 \times 1.01 \times 1.01 = 1.0406$  or 4.1%, instead of  $4 \times 1\% = 4\%$ .

**Annual** growth refers to the year-to-year change of the referenced period versus the same period the year before.

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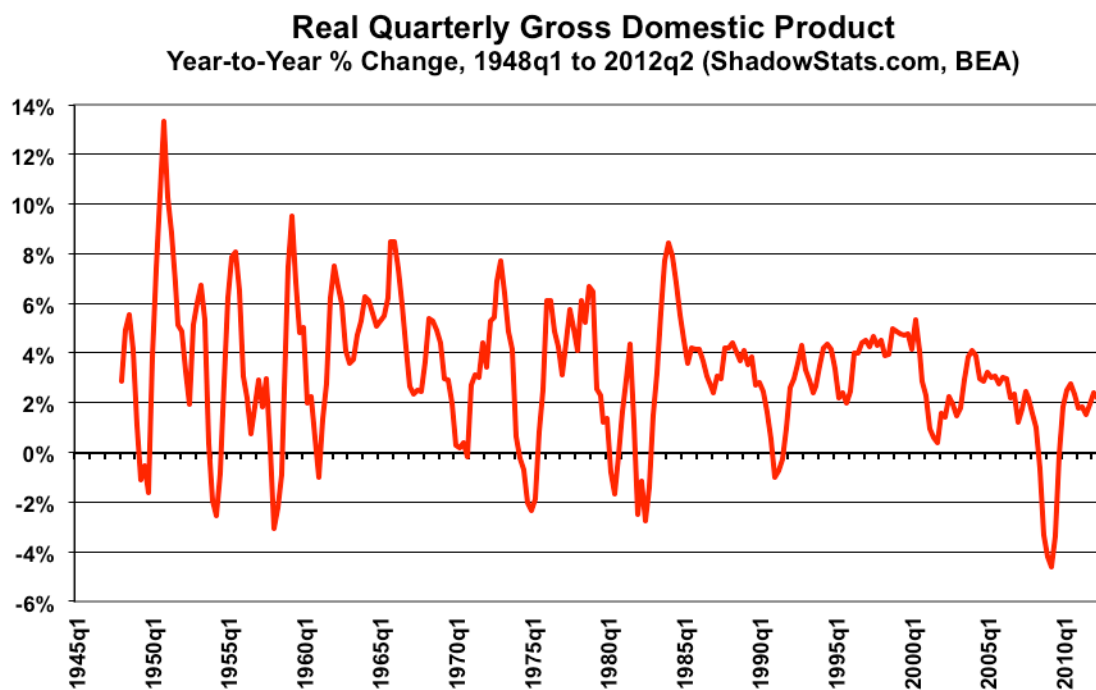
**GDP.** Published yesterday, July 27th, by the Bureau of Economic Analysis (BEA), the first or “advance” estimate of second-quarter 2012 gross domestic product (GDP) showed real (inflation-adjusted) quarterly growth at a statistically-insignificant 1.54% +/- 3% (95% confidence interval). That was weaker than the benchmark-revised 1.96% (previously 1.87%) growth in the first-quarter, and down from 4.10% (previously 2.95% in the fourth-quarter).

For five of the six quarters since first-quarter 2011 (fourth-quarter 2011 now excepted), estimated growth rates have been little more than statistical noise around the unchanged level, and these heavily guessed-at numbers possibly have been massaged to keep the quarterly growth rates in minimally-positive, as opposed to minimally-negative territory. For example, of note among the just-published revisions in that period, first-quarter 2011 headline growth (that’s annualized quarter-to-quarter growth) revised to 0.08% from previous reporting of 0.36%

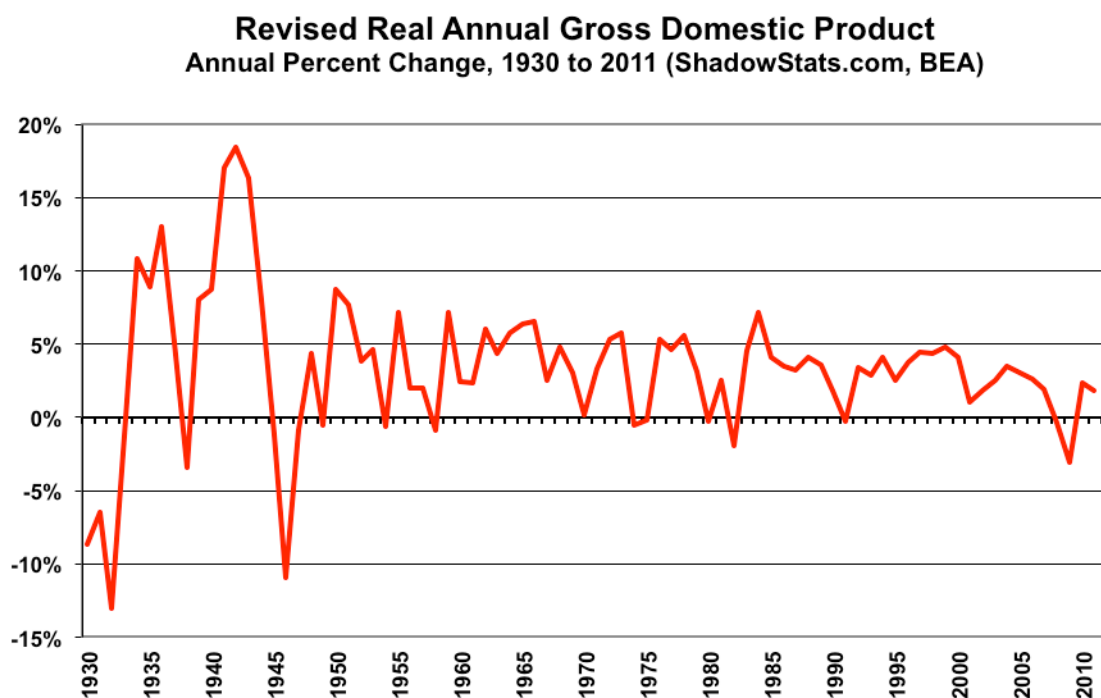
As shown in *Graph 12*, the year-to-year real change in second-quarter 2012 GDP was 2.21%, down from a benchmark-revised 2.45% (previously 1.99%). The jump in annual growth in first-quarter 2012 was against a revised first-quarter 2011 number that, again, was virtually unchanged on a quarter-to-quarter basis. The latest annual growth still was off the revised near-term peak growth of 2.80% (previously 3.51%) reported during third-quarter 2010. The cycle trough in second-quarter 2009 also was revised, to a 4.58% year-to-year decline (previously a 5.03% drop). Nonetheless, the cycle trough remained the deepest annual contraction seen for any quarterly GDP in the history of the series, which began with first-quarter 1947.

In terms of full-year annual growth, shown in *Graph 13*, annual change in 2009 versus 2008 revised to a 3.07% contraction (previously a 3.49% decline), 2010 annual growth revised to a 2.39% gain (previously 3.03%), and 2011 annual growth revised to 1.81% (previously 1.74%). The 2009 annual contraction remained the worst on record since the post-war wind-down of industrial production in 1946.

*Graph 12*



*Graph 13*





***Implicit Price Deflator (IPD) and PCE Deflator.*** The second-quarter 2012 GDP implicit price deflator (IPD) was reported at an annualized quarterly inflation rate of 1.51%, against 2.17% (previously 2.02%) reported for the first-quarter, and 0.13% (previously 0.85%) reported for the fourth-quarter. Second-quarter year-to-year inflation was estimated at 1.70%, versus 1.98% (previously 2.00%) in the first-quarter, and 1.96% (previous 2.18%) in the fourth-quarter.

For comparison purposes, annualized seasonally-adjusted quarterly inflation for the CPI-U in the second quarter was 0.75%, versus 2.48% in the first-quarter, and versus 1.30% in the fourth-quarter, with year-to-year CPI-U at 1.89%, versus 2.82% in the first-quarter, and versus 3.29% in the fourth-quarter.

The lower the inflation rate that is used in deflating the GDP, the stronger is the resulting inflation-adjusted number and vice versa.

Year-to-year change in the second-quarter personal consumption expenditures (PCE) deflator was 1.65%, versus a revised 2.36% (previously 2.00%) in the first quarter. The PCE deflator will be explored in more detail in the August 1st *Commentary*, which will cover the July 31st annual revisions to monthly data.

***SGS-Alternate GDP.*** The SGS-Alternate GDP estimate for second-quarter 2012 is a 2.2% contraction versus the official estimate of a 2.2% gain. The SGS second-quarter estimate is the same as the 2.2% contraction level estimated for first-quarter 2012, versus the revised official estimate of 2.4% (previously 2.0%) year-to-year growth (see the [Alternate Data](#) tab). The SGS measure does not undergo benchmark revisions.

While annualized real quarterly growth is not estimated formally on an alternate basis, a quarter-to-quarter contraction once again appears to have been a realistic possibility for the second-quarter, as it has been for five of the last six quarters, a period of protracted business bottom-bouncing in the real world.

Adjusted for gimmicked inflation and other methodological changes, the business downturn that began in 2006/2007 is ongoing; there has been no meaningful economic rebound. The inflation-corrected GDP graph (see the *Opening Comments and Executive Summary* section and [Hyperinflation 2012](#) and [Special Report No. 445](#)) is based on the removal of the impact of hedonic quality adjustments that have reduced the reporting of annual GDP inflation by roughly two-percentage points. It is not the same measure as the SGS-Alternate GDP, which reflects the impact of reversing additional methodological distortions of recent decades.

***GNP and GDI.*** Initial estimates of second-quarter 2012 gross national product (GNP) and gross domestic income (GDI) will not be published for another month or so. Where GNP is the broadest measure of U.S. economic activity (GDP is GNP net of trade in factor-income, or interest and dividend payments), and where GDI is the income-side reporting equivalent of the consumption-side GDP, the BEA deems its information quality as inadequate, at this time, for publication. The same easily could be said for the GDP.

Nonetheless, the GNP and GDI data were included in the annual revisions, where graphs and comments are offered in the *Opening Comments and Executive Summary*.



**Real Disposable Income.** Detail on the games being played by the government in reporting real disposable income also will be explored in the August 1st *Commentary*, which will cover the July 31st annual revisions to monthly data.

For second-quarter 2012, the annualized quarterly growth rate for real disposable income was estimated at 3.25%, up from a benchmark-revised 3.41% (previously 0.68%) in the second quarter, and up from a revised 0.16% contraction (previously a 0.16% gain) in the fourth-quarter. In terms of year-to-year growth, second-quarter disposable income gained 1.29%. That was against a revised 0.11% (previously 0.26%) annual gain in the first-quarter, and a 0.34% (previously 0.40%) gain in the fourth-quarter.

Since the first publication of annual disposable income data in 1929, no incumbent party has retained the White House, when annual real disposable income growth has been below 3.0% in a presidential election year. Even with the revisions, the current circumstance is developing, so far, against the incumbent party for the 2012 election.

**Week Ahead.** *Market recognition of an intensifying double-dip recession is taking a somewhat stronger hold, at the moment, while recognition of a mounting inflation threat remains sparse. 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 or to put a happy spin on the numbers; 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 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.*

**Personal Consumption Expenditure (PCE) Deflator (June 2012, Annual Revisions).** The Bureau of Economic Analysis is scheduled to release the June 2012 PCE deflator and the annual revisions to it and related monthly series on Tuesday, July 31st. The Federal Reserve's targeted inflation measure (target of 2.0% year-to-year inflation) likely will hold around May's annual inflation estimate of 1.5%, paralleling the reporting patterns of the various CPI measures. Nonetheless, as discussed previously, the current concept of an inflation target serves only as pabulum for the financial markets, not as a defining priority that drives Fed policy.

**Construction Spending (June 2012).** Due for release on Wednesday, August 1st, by the Census Bureau, June construction spending likely will show ongoing stagnation at low levels of activity, particularly after inflation-adjustment. Once again, monthly changes should not be statistically significant.

**Employment and Unemployment (July 2012).** July labor data are due for release by the Bureau of Labor Statistics (BLS) on Friday, August 3rd. As often is the case, the consensus jobs estimate appears to be settling around the trend estimate that comes out of the BLS seasonal-adjustment models. The payroll trend number for July is 108,000 as discussed in [Commentary No. 453](#).

Nonetheless, the July numbers, once again, should disappoint market expectations, given intensifying underlying weakness in related fundamentals. Payroll growth could be well below 100,000. While an

upside tick in the actual U.3 unemployment rate—to 8.3%—is likely, the headline number could come in anywhere. Inconsistent concurrent-seasonal-factor reporting makes reported month-to-month changes in the headline unemployment rate absolutely meaningless (see the unemployment concurrent-seasonal-factor discussion in [Commentary No. 453](#)).

Simply put, the headline July unemployment rate will be calculated in the context of a set of seasonal factors unique to July's reporting. That same calculation also will generate revised unemployment rates for June, and earlier, which would be consistent with the new July estimate. Still, the BLS will not publish the revised, consistent June number, so as "to avoid confusing data users."

As a result, that uniquely calculated July unemployment rate will be published and compared with the unrevised and June unemployment rate that was uniquely calculated and published one month ago. The headline July and June numbers put before the public will be inconsistent and, accordingly, not comparable.

This all is despite the BLS knowing what actually is the consistent June number. If used, the consistent number could affect the headline monthly change in the unemployment rate by several tenths of a percentage point, in either direction, versus what the mainstream media will be touting, and around which the financial markets will be gyrating nonsensically.

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