

COMMENTARY NUMBER 469
2011 Income and Poverty Report, July Trade Balance

September 12, 2012

**Real Median Household Income Collapses to 16-Year Low;
2011 Income Below Levels of Late-1960s, Early-1970s**

**Income Variance Hits Record High,
Suggestive of Greater Financial and Economic Crises Ahead**

Trade Deficit Contained by Short-Lived Decline in Oil Prices

PLEASE NOTE: The next regular Commentary is scheduled for Friday, September 14th, covering August CPI, PPI, retail sales, industrial production and related series.

Best wishes to all — John Williams

Opening Comments and Executive Summary. Today's (September 12th) release of the Census Bureau's 2011 income and poverty survey showed no indications of an economic recovery in place or pending, and it was suggestive of even more-difficult times to come.

Consumers simply cannot make ends meet. Inflation-adjusted, or real, median household income declined for the fourth-straight year, plunging to its lowest level since 1995. Deflated by the CPI-U, the 2011 reading actual stood below levels seen in the late-1960s and early-1970s. The Census numbers confirmed the annual patterns suggested by the monthly reporting of real median household income

published by Sentier Research, whose numbers are updated later in this general section. Real median individual income also declined for the year, for both men and women.

At the same time, despite the ongoing nature of the economic and systemic-solvency crises, and the effects of the 2008 financial panic, income dispersion—the movement of income away from the middle towards both high- and low-level extremes—has hit a record high, instead of moderating, as might be expected during periods of financial distress. Extremes in income dispersion usually foreshadow financial-market and economic calamities. With the current circumstance at a record extreme, and well above levels estimated to have prevailed before the 1929 stock-market crash and the Great Depression, increasingly difficult times are likely for the next several years.

In other reporting, the July trade deficit was contained by a short-lived decline in oil prices, with little impact likely, so far, on third-quarter GDP reporting.

July consumer credit continued its stagnation, net of U.S. government-held student loans. The Federal Reserve, however, introduced a discontinuity into the series.

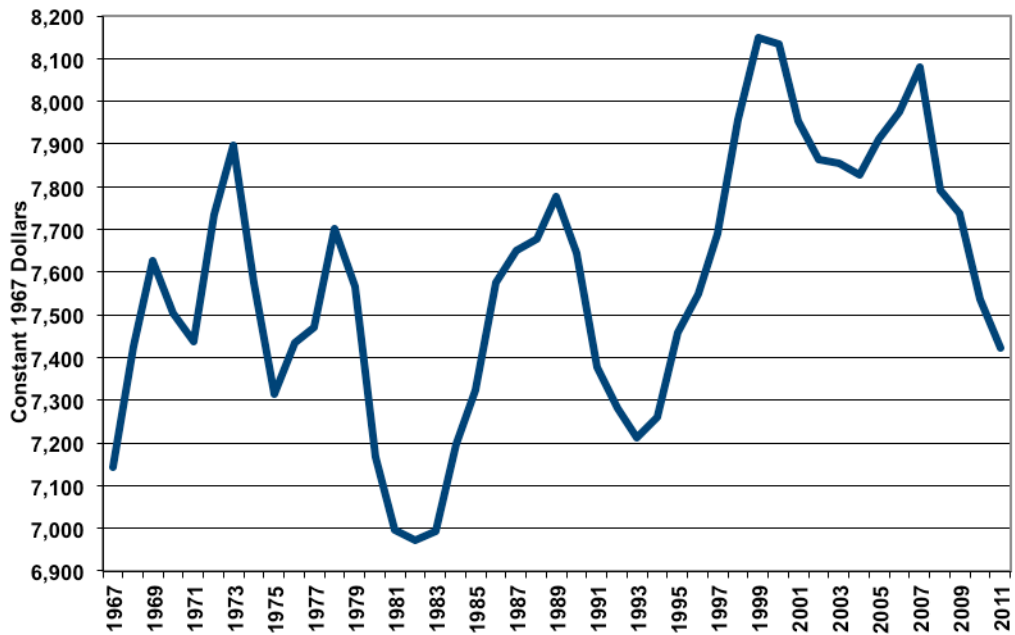
Household Income and Income Variance Deteriorated Sharply in 2011, Suggestive of Still-Greater Crises Ahead. Some of the text that follows is repetitive from prior years; the story varies little. The U.S. Census Bureau published [*Income, Poverty, and Health Insurance Coverage in the United States: 2011*](#), today, September 12th. The value of this report is in its estimates of household income and income variance, not in the titled poverty or health insurance estimates. Annual poverty reporting *per se* is not too meaningful, where the structure of the reporting is highly subjective. Surprisingly, fewer people were reported in poverty as of 2011 than as of 2010, but the decline in the poverty rate from 15.1% in 2010 to 15.0% in 2011 was not statistically significant.

Measuring “poverty” is difficult, at best, when few can agree on a definition. There are many who do not consider themselves to be poor, even though they meet the government’s standards, while others think they are poor but are not defined as such. Separately the whole process has been heavily influenced by politics, with even some short-term efforts at impacting the numbers. For example, the survey’s inner-city sampling size was reduced (with Congressional oversight) during the Clinton Administration, and then re-expanded at the end of the Clinton era.

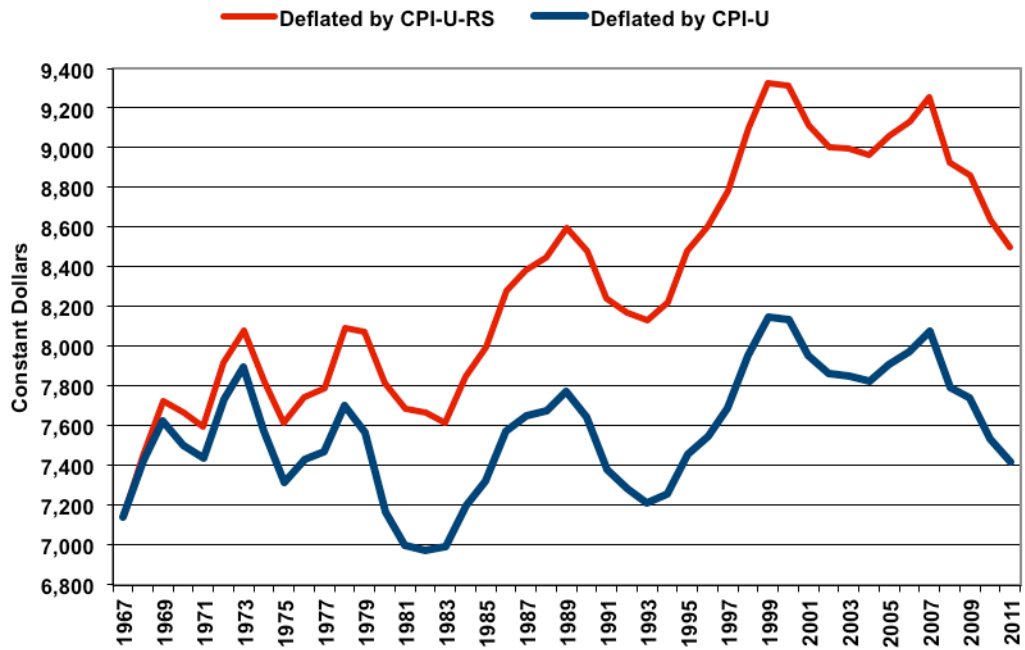
The actual survey usually is piggy-backed on the March household unemployment survey of the year following the reported data. So, the March 2012 survey of 2011 data is what was published today, by the Census Bureau, which conducted the household survey on behalf the Bureau of Labor Statistics. Following is a brief update of significant numbers.

Real Median Household Income Is at Its Lowest Level Since 1995. Consumer income remained in contraction during 2011, with both real (inflation-adjusted) median household income and real median individual income sinking on an annual basis. Given consumers lack of ability to expand their borrowing in order to make up for shortfalls in income, the chances of there having been a full economic recovery since 2009 (as reflected in the GDP), or of a recovery pending in the immediate future, are nil.

Median Household Income (1967 Dollars)
 Deflated by CPI-U, (ShadowStats.com, BLS, Census Bureau)



Median Household Income (1967 Dollars)
 CPI-U vs CPI-U-RS, (ShadowStats.com, BLS, Census)



The preceding two graphs show inflation-adjusted median levels of household income from 1967 through 2011. The median household income measure is the middle measure of the survey and likely is a better reflection than the mean household income measure of how most households are doing. When the income dispersion measure is high—it is at a record high as of 2011, as discussed below—the mean, or average, measure tends to be skewed (in the current case to the upside), which is why the reported real mean household income turned slightly higher in the 2011 survey.

The charts show median household income deflated using two Bureau of Labor Statistics (BLS) inflation measures, the CPI-U and the CPI-U-RS. In both instances, 2011 median household income has dropped to the lowest levels since 1995. I emphasize here that these graphs use government numbers, not any alternate ShadowStats.com inflation measure.

In the case of the median household income series deflated by the CPI-U (shown in both graphs), which is the measure used by the BLS when it deflates its broad income measures, and also is the inflation measure used in deflating the monthly median household income measures published by Sentier Research (see the next section), the 2011 level of median household income is below the levels seen in the late-1960s and early-1970s.

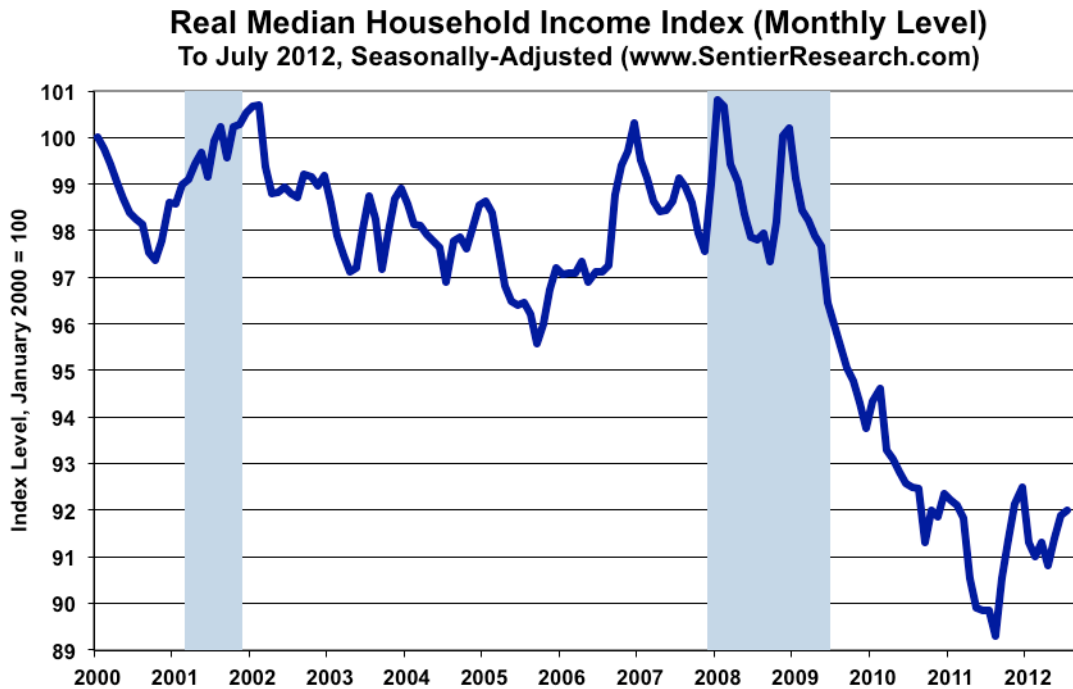
The CPI-U-RS is an “experimental” BLS series used by the Census Bureau, and it enables Census to report the survey details with artificially-reduced historical inflation levels. The result is a stronger inflation-adjusted pattern of income levels (the red, narrower line in the second graph), than what usually would be the official weaker picture (blue line) based on deflation using the traditional CPI-U reporting.

The CPI-U (All Urban Consumers) is the headline consumer inflation number published by the BLS and the one most commonly used in deflating consumer-related dollars. The Census Bureau appears to have used the CPI-U in its annual poverty reports as recently as 2003.

The CPI-U-RS (Current Methods) is a special version of the CPI-U with its history restated so as to reduce earlier-year inflation by imputing what it would have been, using today’s “advanced” CPI reporting methodologies. The CPI-U-RS is the index used by the Census Bureau in deflating income numbers in the *Poverty Report* since 2003. It also is the series reverse-engineered by ShadowStats.com for constructing the SGS Alternate CPI estimates, as discussed in [Public Comment on Inflation](#).

The difference in reporting is that traditional CPI-U deflation shows that the level of 2011 median household income is below where it was in 1969. These issues also are discussed more fully in the [Hyperinflation Special Report \(2011\)](#).

Monthly Real Median Household Income Continued Its Bottom-Bouncing in July 2012. The annual decline in real median household income in 2011 was consistent with the monthly real median household income numbers as published by www.SentierResearch.com. The Sentier numbers, which also are based on the Census Bureau’s monthly surveying, indicated the 2010 to 2011 annual decline. Shown in the following graph is the Sentier monthly household income index, updated through July 2012. The index has shown some slight bottom-bouncing to the upside so far in 2012.

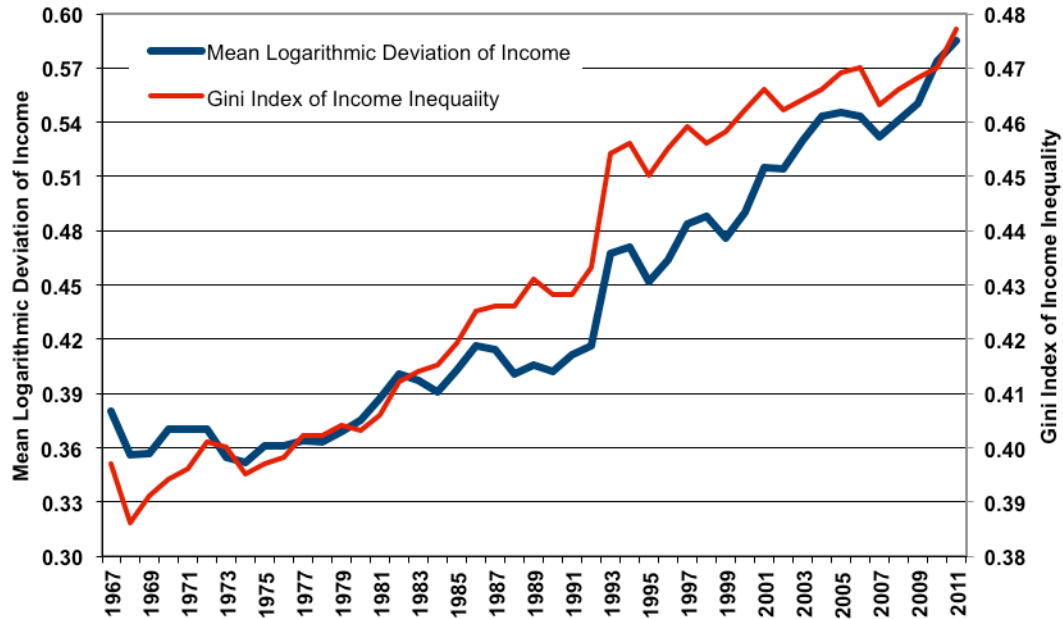


Rising Income Dispersion (Let Alone a Record Level) Tends to Foreshadow Economic and Financial-Market Turmoil. Back to the Census Bureau’s reporting, measures of income dispersion, or variance, indicate how income is distributed within a population. A low level of income dispersion indicates that income tends to be concentrated in the middle, while a high level of dispersion indicates heavier income concentrations in the extremes of low and high income, with less in the middle. The higher the variance of income is, as shown in the next graph, the greater is the income dispersion.

Generally, the more moderate the income variance is, the stronger the middle class is, and the healthier the broad economy will be in the longer term. Conversely, the greater the variance in income is, the more negative are the longer-term economic implications. For example, a person earning \$100,000,000 per year is not going to buy proportionately more automobiles than someone earning \$100,000 per year, so a strong middle class generally is a better circumstance for the auto industry than is extreme income dispersion.

Shown in the following graph are the Gini Index of Income Inequality and the Mean Logarithmic Deviation of Income (MLD), two of the more popular income dispersion series. Some of the finer points and mathematics behind several of the income variance measures are covered in the Census Bureau’s article: *The Changing Shape of the Nation’s Income Distribution*.

Household Income Dispersion
Gini Index versus Mean Logarithmic Deviation
 1967 to 2011 (Census Bureau, Poverty Report)



Conditions surrounding extremes in income variance usually help to fuel financial-market bubbles, followed by financial panics and economic depressions. The sequence of those factors tends to redistribute income in a manner that usually lowers income variance, helping economic recovery. Other than for a brief dip following the 1987 stock-market crash, however, U.S. income variance since 1987 has been higher than has been estimated for the economy going into the 1929 stock-market crash and the Great Depression, and its current reading remains nearly double that of any other “advanced” economy. Instead of being tempered by the 2008 financial panic and the ongoing economic and systemic-solvency crises, variance increased to record levels in 2011. This suggests that the greatest negative impact of the systemic turmoil, so far, has been on those in the middle-income area. It also is suggestive of even greater financial and economic crises still ahead.

Discontinuity Introduced in Reporting of July Consumer Credit Outstanding. Rounding out an unhappy picture for consumer spending and for any near-term economic recovery, July consumer credit continued to be stagnant other than for activity in federal holdings of student loans.

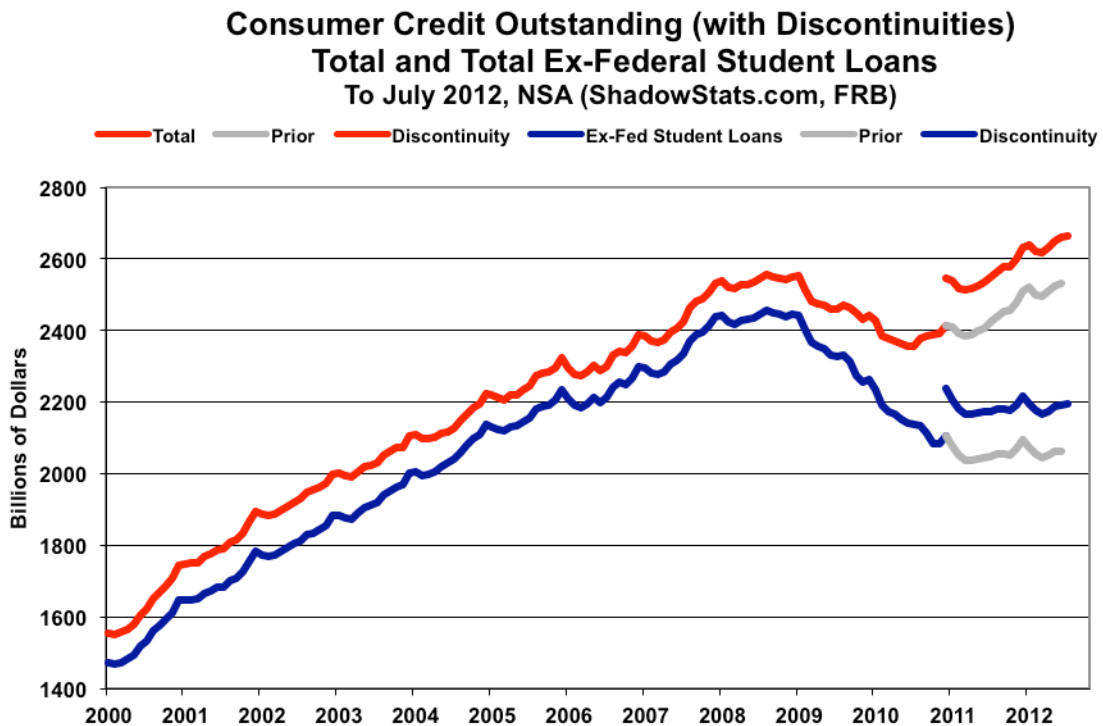
In recent decades, consumers have tended to make up for the shortfall in real income growth through debt expansion. The debt expansion option basically was taken out of play as a result of the financial panic of 2008 and the related debt crisis. Without real income growth or debt expansion potential, households do not have the ability to fuel positive, inflation-adjusted growth in the 73% of GDP that depends on consumer buying (personal consumption and residential investment). Accordingly, there has been no broad economic recovery and none is imminent, as discussed in [Special Report No. 445](#) and

[Hyperinflation 2012](#). Updated, related consumer confidence and sentiment graphs are found in [Commentary No. 468](#).

The July 2012 level of consumer credit outstanding was published by the Federal Reserve in the context of a discontinuity in the series introduced for December 2010, where the levels of aggregate consumer credit from December 2010 forward were shifted higher by 5.5%, which narrowed slightly to roughly 5.0% in the most recent reporting. Once again, this highlights the inability of the Fed to gather consistent and reasonably accurate information on a timely basis. The one-time upside shift in activity was due to a census of finance companies.

As explained by the Fed, “The Federal Reserve Board announced on Friday (September 7th) the completion of the 2010 Census of Finance Companies and Survey of Finance Companies. These data have been collected every five years to provide a comprehensive and accurate statistical snapshot of the balance sheet of the finance company industry. The statistical results of the 2010 surveys will be incorporated in the July Consumer Credit (G. 19) statistical release.”

As seen in the following graph, the underlying pattern of federally-owned student loans has accounted for all growth in consumer credit outstanding since the economic collapse of 2006 to 2009, to date, despite the discontinuity. Net of the student loans, consumer credit outstanding has been stagnant, holding near the low of the current cycle.



July Trade Deficit Kept in Check by Short-Lived Drop in Oil Prices. The headline July trade deficit deteriorated minimally—almost unchanged—to \$42.0 billion, versus a revised \$41.9 (previously \$42.9) deficit in June. Net of a short-lived plunge in oil prices, the inflation-adjusted deficit for July widened sharply. With inflation adjustment, the early implications as to impact on third-quarter GDP are largely neutral, perhaps slightly positive.

Hyperinflation Watch—General Outlook Unchanged. *General circumstances have not changed, and the text that follows is the same as in the prior Commentary. This summary will be updated with the September 14th Commentary. The detail in [Special Report No. 445](#) (June 12th) 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. Those reports are suggested as background reading for new subscribers.*

Official GDP reporting shows plunging economic activity from fourth-quarter 2007 to second-quarter 2009, with an ensuing upturn in activity that led to a full recovery as of fourth-quarter 2011, and that “recovery” has continued through second-quarter 2012 GDP reporting.

In contrast to GDP reporting—and in line with patterns seen in better-quality economic series—I contend that 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.

Federal Reserve Chairman Ben Bernanke recently observed that broad aggregate measures of the U.S. economy, such as GDP, do not appear to be reflecting the common experience of the general public. General experience suggests that the economy has not recovered. 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 overstates deflated economic growth (see also [Special Report No. 445](#), [Public Comment on Inflation](#)).

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, and public awareness of this should grow rapidly in the months ahead.

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—and it should follow as needed to support the banking system—likely will lead to a massive dollar-selling crisis, and that will begin the process of a

rapid upturn in domestic consumer inflation. A dollar-selling crisis, however, could begin at any time, triggered by any number of economic, sovereign-solvency or political issues.

REPORTING DETAIL

U.S. TRADE BALANCE (July 2012)

Minor Deterioration in Headline July Trade Deficit Held in Check by Plunging Imported Oil Prices. The headline July trade deficit widened minimally—almost unchanged—versus a revised June deficit, although it was slightly narrowed versus the initial June headline deficit. Net of a plunge in oil prices, the inflation-adjusted deficit for July deteriorated sharply. With inflation adjustment, however, the impact on third-quarter GDP, at this point, appears to be neutral (perhaps slightly positive).

Nominal (Not-Adjusted-for-Inflation) Trade Deficit. The Bureau of Economic Analysis (BEA) and the Census Bureau reported yesterday (September 11th) that the nominal, seasonally-adjusted monthly trade deficit in goods and services for July 2012, on a balance of payments basis, widened to \$42.0 billion from a revised \$41.9 (previously \$42.9) billion in June. The July 2012 deficit also narrowed from a \$45.6 billion deficit in July 2011.

Against the revised June detail, the seasonally-adjusted July 2012 trade balance reflected lower levels of both exports and imports, with declining prices for imported oil heavily impacting the import numbers.

Crude Oil and Energy-Related Petroleum Products. For the month of July 2012, the not-seasonally-adjusted average price of imported oil dropped to \$93.83, from \$100.13 per barrel in June, and from \$107.91 in May 2012, and it was down from \$104.27 in July 2011. Oil prices since have turned higher.

In terms of not-seasonally-adjusted physical oil imports, July 2012 volume averaged 8.875 million barrels per day, versus 8.781 in June and 8.784 million in May 2012, but it was down from 9.108 million barrels per day in July 2011.

Caution on Data Quality. *The standard caution here for the monthly detail is that heavy distortions likely continue in the seasonal adjustments, much as has been seen in other economic releases, such as retail sales and payrolls, where the headline number reflects month-to-month change. As has been discussed frequently (see [Hyperinflation 2012](#) for example), the extraordinary length and depth of the current*

business downturn have disrupted regular seasonality patterns. Accordingly, the markets should not rely heavily on the accuracy of the monthly headline data.

Real (Inflation-Adjusted) Trade Deficit. Adjusted for seasonal factors and net of oil-price swings and other inflation (2005 chain-weighted dollars as used in reporting real GDP), the July 2012 merchandise trade deficit (no services) came in at \$46.5 billion, versus a revised \$44.0 (previously \$44.2) billion in June.

The July estimate—the first hard number that will have impact on third-quarter GDP reporting—annualized to \$558.6 billion, versus a revised annualized pace of the second-quarter 2012 trade deficit of \$562.4 billion (previously \$563.2 billion). The first-quarter estimate was unrevised at \$574.7 billion. The slight quarterly narrowing suggested by the initial July estimate was not meaningful enough to indicate anything other than a net-neutral or slightly-positive impact on the net-export account in the “advance” third-quarter GDP estimate due for release at the end of October.

Week Ahead. *Market recognition of an intensifying double-dip recession has taken 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 continue to show up in prior-period revisions.

Producer Price Index—PPI (August 2012). The August 2012 PPI is scheduled for release by the Bureau of Labor Statistics (BLS) tomorrow, Thursday, September 13th, and should show a strong gain. Depending on the oil contract followed, oil prices rose by seven-to-elven percent on average in August. The gain in related energy prices should be supplemented somewhat by seasonal adjustments that tend to boost energy prices at this time of year. Food prices also are on the rise, which in combination with still relatively strong “core” inflation should generate something of a jump (likely above consensus) in wholesale prices for August.

Consumer Price Index—CPI (August 2012). The release by the Bureau of Labor Statistics (BLS) of the August 2012 CPI numbers is scheduled for Friday, September 14th. The headline CPI inflation rate is due for a sharp jump on both a monthly and annual basis, reflecting rising energy, food and “core” inflation, with headline inflation reporting likely stronger than market expectations.

Of particular import, unadjusted monthly average gasoline prices rose by 8.1% in August 2012 (Department of Energy). Consider that August seasonal-adjustment factors tend to boost energy price inflation, where an unadjusted 6.8% monthly decline in August 2011 gasoline prices was turned into a 1.9% increase by the seasonal adjustments of that month. The BLS can use its “intervention analysis” to mute some of the seasonal adjustment impact, but the contribution of gasoline prices to the August headline CPI inflation still should be significant.

Year-to-year total CPI-U inflation would increase or decrease in August 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the 0.33% gain in the seasonally-adjusted monthly level reported for August 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for August 2012, the difference in August's headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from the July 2012 annual inflation rate of 1.41%. For example, if the headline monthly inflation number for August 2012 were around the 0.6%, then the year-to-year or annual inflation rate for August would increase to roughly 1.7%.

Retail Sales (August 2012). Scheduled for release on Friday, September 14th, by the Census Bureau, headline August 2012 retail sales likely will surprise market expectations on the downside, with any gains more than accounted for by higher inflation. Structural liquidity problems besetting the consumer should continue to cap consumption growth at a level below the pace of inflation. With the August CPI-U likely to show a solid increase, real (adjusted-for-inflation) retail sales should contract for the month.

Industrial Production (August 2012). Due for release Friday, September 14th, by the Federal Reserve, the headline August 2012 industrial production number also should come in below market expectations. The latest GDP revision suggested that second-quarter inventory building had not been as strong as initially estimated, and the ISM's purchasing managers survey has shown the manufacturing sector in decline for the three months through August, with an outright contraction in August production. Even with seasonal-factor distortions the industrial production number has a good chance of generating a negative reporting surprise, along with some downside revisions to earlier reporting.
