

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

COMMENTARY NUMBER 473

September Employment and Unemployment, August Construction Spending, PCE Deflator

October 5, 2012

**Phony Unemployment Rate Drop? Here Is How It May Have Happened
With Deliberately-Inconsistent Numbers, Only the BLS Can Clear-Up the Reporting**

September Unemployment: 7.8% (U.3), 14.7% (U.6), 22.8% (ShadowStats.com)

September Payroll Gain Was Statistically Insignificant

M3 Annual Growth Notches Higher Again

PLEASE NOTE: The next regular Commentary is scheduled for Friday, October 12th, covering September PPI and the August trade balance.

The Special Commentary reviewing economic, inflation and systemic conditions is planned for next week, the week of October 8th. As publication nears, more-specific timing will be posted in the schedule box on www.shadowstats.com.

Best wishes to all — John Williams

Opening Comments and Executive Summary. The August-to-September change in the headline unemployment rate almost certainly was not a 0.3% decline. The Bureau of Labor Statistics (BLS) knows the reported change in unemployment was wrong—other than by extreme coincidence—and it knows

what consistent reporting actually showed. Only politics prevents the BLS from releasing the correct number, whether the unemployment rate actually declined, held even, or rose as predicted by consensus forecasters. The lack of transparency here in the data preparation allows for direct political manipulation.

The problem is that the BLS knowingly has been preparing the seasonally-adjusted headline unemployment numbers on an inconsistent and non-comparable basis for some time. The September number was prepared using a different set of seasonal factors than was used in coming up with the August number. The reporting difference can be large, when proper consistent month-to-month changes are used.

For example, consider the 0.4-percentage-point decline in the headline unemployment rate for November 2011. That drop in unemployment of that magnitude never was real. Once per year—with the release of December data—the seasonally-adjusted monthly unemployment rates are revised and restated, so as to be consistent. In December 2011, that 0.4-percentage-point drop in November was revised to a 0.2-percentage-point decline. As noted in the text excerpt following, this circumstance allows for outright manipulation of the data, with no cross-checking possible of the unpublished numbers being revised and re-revised every month. The December 2012 restatement of today's headline unemployment decline will not be published until January 2013, well after the presidential election.

Indeed, with the Fed's QE3 formally tied to bringing down the unemployment rate, and with presidential election one month from tomorrow, an unexpected and unusually-large 0.3-percentage-point plunge in the headline unemployment rate might raise more than a couple of eyebrows. The BLS has the correct number and could publish it. It had to calculate a consistent August 2012 number in order to estimate September 2012. Now would be a particularly good time for the BLS to come clean on its unemployment estimates, even if the numbers "confuse" data users. Avoiding such confusion is the stated reason as to why the BLS does not publish comparable monthly headline unemployment rates.

Prior Comments on the Headline Unemployment Rate Seasonal Adjustments. The issues have been discussed in early writings, such [Commentary No. 461](#). The relevant text from *No. 461* is repeated here:

The July employment and unemployment numbers published today, August 3rd [2012], were worthless and likely misleading. What has been done in the last couple of decades to the reporting methodologies for monthly labor data, compounded by distortions introduced into the system from the economic collapse of the last five years, has left the heavily-followed employment and unemployment series seriously impaired as to significance, and potentially subject to direct political manipulation.

Suspecting at one time that the jobs numbers were being rigged against him by his own Bureau of Labor Statistics (BLS), President Richard M. Nixon proposed a new approach to reporting the numbers. Although the proposed changes never were implemented, several decades later the BLS adopted reporting methods that were somewhat parallel to the late-President's thinking.

A member of an advisory panel to the Bureau of Labor Statistics during the Nixon Administration once described to me how Nixon wanted to change the unemployment reporting. The President simply suggested the release each month of only one number, the seasonally-adjusted or the not-seasonally-adjusted unemployment rate—whichever one was lower at the time—without telling the public which one had been released.

Few would believe that such a reporting methodology ever would have been enacted. Still, the nature of this morning's headline unemployment rate report was very much in keeping with

Nixon's purported sense of reporting propriety for politically-sensitive economic data. His creative approach to handling the unemployment numbers has been vindicated to a certain extent, to wit the BLS just published the July 2012 headline unemployment rate, but it will not tell the public what the appropriate comparative number was for June.

Due to the deliberate, inconsistent reporting of monthly unemployment rates, the official 0.1 percentage point increase in the July headline rate was not necessarily so. Against the June unemployment rate that had been revised internally by the BLS, so as to be consistent with the July reporting, headline July unemployment could have shown an actual 0.2 percentage point, or more, increase; it could have been unchanged; or it could have declined. Annual revisions to last year's data showed a difference of 0.2 percentage point versus initial estimates of month-to-month change in at least one month.

Only the BLS knows what the actual June-to-July change was, and it will not publish a hard number, on a consistent basis, until after the election, along with the December 2012 data to be released in January 2013. By then, today's number will have been revised (but not re-reported) five times, where any revision that would happen to match today's reporting would be purely coincidental. Of key importance, whatever today's actual month-to-month change was, it never will be published in the normal course of business. The lack of "transparency" here opens the potential for direct political manipulation of the data.

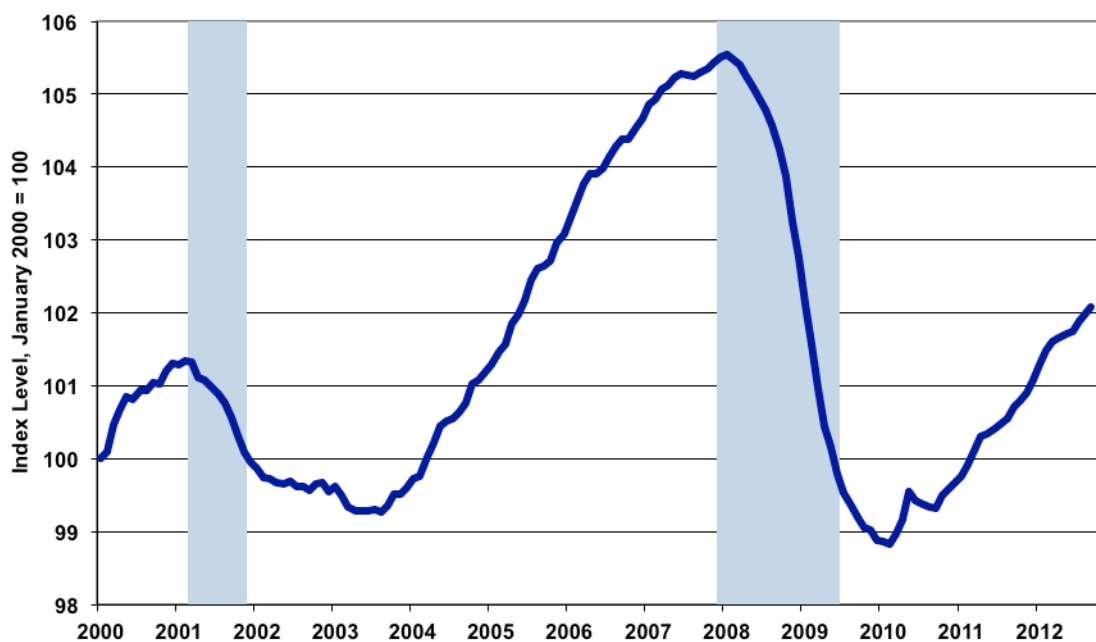
Concurrent Seasonal Adjustments. Simply put, the headline July unemployment rate was calculated in the context of a set of seasonal factors unique to July's reporting (see [Commentary No. 451](#) and [Commentary No. 453](#)). That same calculation also generated revised unemployment rates for June, and earlier, which were consistent with the July estimate. Still, the BLS will not publish the revised, consistent June number—leaving in place instead the now-obsolete unique June calculation of the month before—so as "to avoid confusing data users." As would have been the case with President Nixon's proposal, the published numbers here have no meaning in terms of month-to-month comparisons, and extremely few people have any idea that there even is a problem in the reporting.

This all is despite the BLS knowing what actually is the consistent July versus June comparison. 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 is touting, and around which the financial markets are gyrating nonsensically, today.

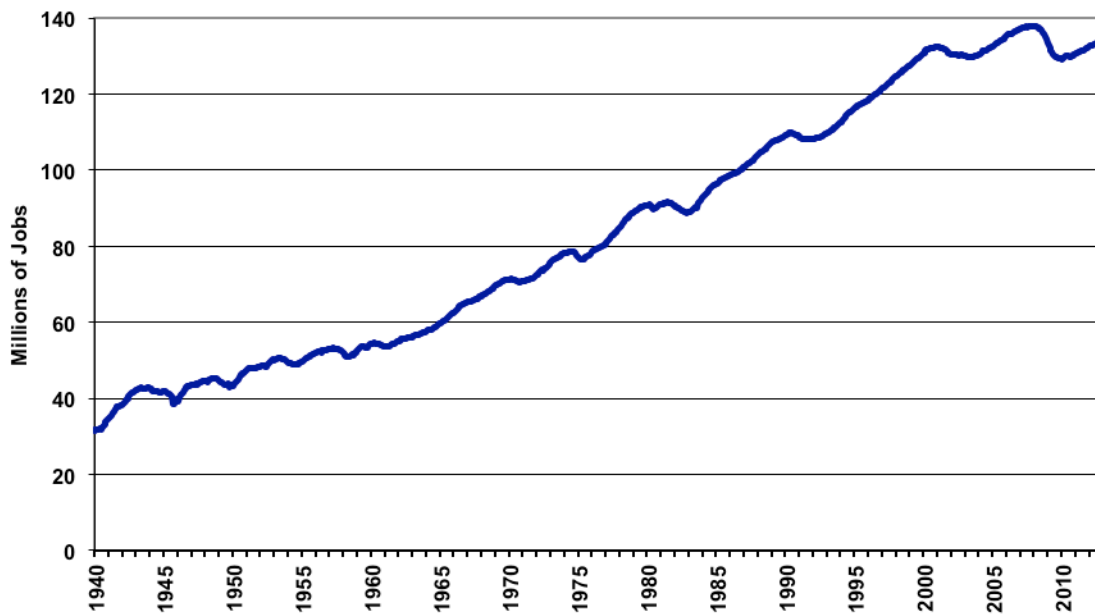
Although I would argue in the post-economic-crash environment that concurrent seasonal adjustments are unstable and less accurate than the old fixed-seasonal-adjustment system, the BLS contended when introducing the new system that the concurrent-seasonal-adjustment system was more accurate. Assuming for the moment that the BLS is correct, *the concurrent-seasonally-adjusted series can provide more-accurate information to the public, only if the actual and consistent numbers actually are published.*

September 2012 Employment and Unemployment Reporting. The first graph following shows seasonally-adjusted payroll levels (indexed to January 2000 = 100), reflecting detail of the current employment level well below its pre-2007 recession peak. The second, longer-term graph of the payroll employment level, shows historical detail back to 1940 and, in perspective, that payroll levels still are minimally above levels in 2000.

**Nonfarm Payroll Employment (Monthly Index Level)
To Sep 2012, Seasonally-Adjusted (ShadowStats.com, BLS)**



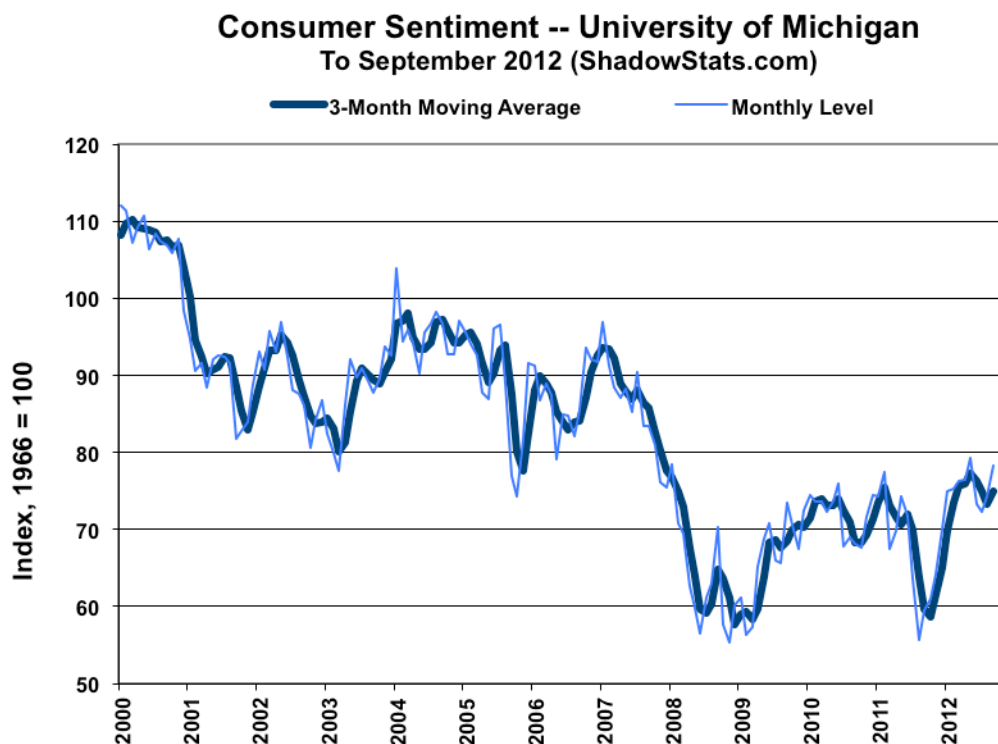
**Nonfarm Payroll Employment
Seasonally-Adjusted Levels, to Sep 2012 (ShadowStats.com, BLS)**

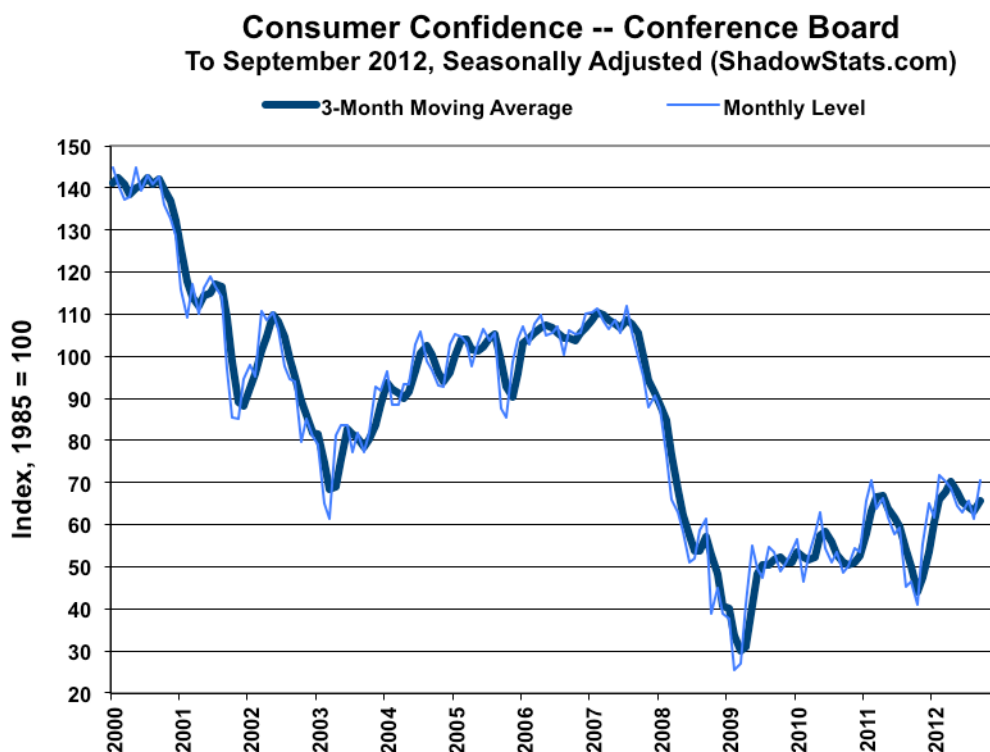


The 114,000 gain in nonfarm payrolls reported for September was not statistically significant, and reflected an influx of previously-reported seasonally-adjusted jobs growth was revised into the current reporting, without the revisions to prior history being published.

September's 7.80% headline U.3 unemployment rate—down by a meaningless 0.3%, as reported—contrasted with an unchanged, broader September U.6 rate of 14.7% and an unchanged SGS-Alternate Unemployment Measure of 22.8%

New Consumer Data. The University of Michigan's September consumer sentiment measure showed a monthly jump, but that was far shy of the seasonally-adjusted gain reported with the Conference Board's September consumer confidence measure. The Conference Board number, which is seasonally-adjusted, likely with some issues, as discussed in [Commentary No. 472](#), is shown below, once again. Both series continue to fluctuate within recent bounds, with trends that remain at levels seen only in the depths of the worst post-World War II recessions.





Hyperinflation Watch—September M3 Money Supply. Based on more than three weeks of reported data, the preliminary estimate of annual growth for the September 2012 SGS Ongoing-M3 Estimate—to be published tomorrow (October 6th) in the [Alternate Data](#) section—is on track to hit 3.3%, up from a revised 3.2% (previously 3.1%) in August. As usual, revisions to prior months were due primarily to Federal Reserve revisions to underlying data. Nonetheless, with recent annual growth having peaked at 4.2% in February 2012, the upturn in annual broad money growth that began in February 2011, had faltered, leveled out and now is notching higher again. Such a pattern—in an environment of massive Federal Reserve accommodation—still remains suggestive of an intensifying systemic-solvency crisis.

The seasonally-adjusted, month-to-month change estimated for September 2012 M3 likely will be around 0.4%, versus 0.3% in August. The estimated month-to-month M3 changes, however, remain less reliable than the estimates of annual growth.

For September 2012, early estimates of year-to-year and month-to-month changes follow for the narrower M1 and M2 measures (M2 includes M1, M3 includes M2). Full definitions are found in the [Money Supply Special Report](#). M2 for September is on track to show year-to-year growth of about 6.9%, versus 6.3% in August, with month-to-month growth estimated at roughly 0.7% in September, versus 0.4% in August. The early estimate of M1 for September shows year-to-year growth of roughly 12.4%, versus a revised 10.8% (previously 10.3%) in August, with month-to-month change a likely gain of 2.1% in September, versus a 0.6% gain in August. The variability in year-to-year growth rates reflects sharp

monthly gains a year ago in M1 and M2 that reflected a shifting of funds out of M3 accounts into the M1 and M2 accounts.

General Outlook to Be Revised in Upcoming Special Commentary. The nature and implications of QE3—announced recently by the FOMC of the Federal Reserve Board—were discussed in the *Opening Comments* of [Commentary No. 470](#). Specifically, while general circumstances have continued to advance towards the ultimate demise of the dollar, the general outlook is unchanged. While QE3 is an enabling action for the onset of massive inflation, the outside timing of 2014 for the ShadowStats.com hyperinflation forecast remains in place. The hyperinflation outlook will be reviewed and updated fully in the pending *Special Commentary*. The following summary of the broad outlook is has not been changed since the September 14th *Commentary*.

The detail in [Special Commentary No. 445](#) (June 12th) updated the hyperinflation outlook and the outlook for U.S. economic, U.S. dollar, and systemic-solvency conditions. That Special Commentary supplemented [Hyperinflation 2012](#) (January 25th), which remains the primary missive 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 has led to a full recovery as of fourth-quarter 2011, and that “recovery” has continued through second-quarter 2012 GDP reporting.

In contrast to the 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 full recovery shown in the GDP series.

Federal Reserve Chairman Ben Bernanke has 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. Indeed, common experience suggests that the economy has not recovered. 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, as discussed in [Commentary No. 467](#), [Special Commentary No. 445](#), and [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, suggesting 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, and the most recent readings on income variance suggest that the worst is yet to be seen, as discussed in [Commentary No. 469](#).

With the economy weak enough to provide political cover for further Federal Reserve accommodation to the still-struggling banking system, QE3 was introduced on September 13th. That action effectively provided for open-ended monetization of U.S. Treasury debt at the Fed's discretion. The mechanism for eventual full debasement of the dollar now is in place, and it likely will come into full play, as needed to support the banking system and as needed to assure "successful" auctions of Treasury debt.

QE3 likely will lead to a massive dollar-selling crisis, and that will begin the process of a rapid upturn in domestic consumer inflation. A near-term dollar-selling crisis is now of a much greater risk, post-QE3. Separately, though, a dollar-selling crisis could begin at any time, triggered by various economic, sovereign-solvency or political issues. With the guidelines set for QE3, even negative employment reports could trigger massive dollar selling.

REPORTING DETAIL

EMPLOYMENT AND UNEMPLOYMENT (September 2012)

Severe and Deliberate Disruptions to Unemployment and Employment Reporting Accuracy by the BLS. Both September's headline unemployment rate change versus August, and recent payroll reporting changes have been warped by the concurrent seasonal-factor adjustment policies of the Bureau of Labor Statistics (BLS).

As has been discussed frequently, reporting of month-to-month changes in both payroll employment and the unemployment rate is of such poor quality that the headline labor data have become worthless as indicators of current economic activity. Problems with seasonal-factor distortions—created by the economic collapse and exacerbated by the use of concurrent seasonal factors—have widened the likely margins of reporting error in the payroll survey to something beyond the usual +/- 129,000 jobs at the 95% confidence level (see [Hyperinflation 2012](#)), and the monthly headline unemployment numbers simply no longer are comparable on a month-to-month basis (see *Opening Comments and Executive Summary*).

Nonetheless, these numbers will be pulled apart by the financial markets and politicians well beyond any extremely limited significance in the numbers. To the extent that there is significance in the monthly reporting, it is that the economy is not in recovery and that unemployment—as viewed by common experience—remains at a level that rivals any other downturn of the post-Great Depression era.

Benchmark Revision Estimate. On September 27th, the BLS published its initial estimate of the benchmark revision to the not-seasonally-adjusted March 2012 payroll level. The BLS estimated an

upside revision of 386,000 to the March numbers, or roughly 32.2 thousand jobs per month. The benchmark will be published with the January 2013 payroll data on February 1, 2013, with changes imputed back into 2011 and up to the present.

PAYROLL SURVEY DETAIL. The BLS reported today (October 5th) a statistically-insignificant, seasonally-adjusted September 2012 month-to-month payroll employment gain of 114,000 (a gain of 200,000 before prior-period revisions) +/- 129,000 (95% confidence interval). [Concurrent-seasonal-factor distortions likely have widened the margin of reporting error—the 95% confidence interval—to meaningfully beyond the official +/-129,000.]

The adjusted August month-to-month change was revised to a 142,000 (previously 96,000) gain, while the July month-to-month gain was a revised 181,000 (previously 141,000, initially 163,000). If, however, the July change were counted on a consistent basis, with the latest concurrent seasonal factor calculations, the revised July gain actually was 157,000. The inconsistent seasonal-adjustment factors are pushing relative payroll gains into the current timeframe.

The BLS publishes two prior months of consistent data with concurrent-seasonally-adjusted payrolls, but no prior months of consistent data with the unemployment rate. This issue is discussed in the *Concurrent Seasonal Factor Distortions* section.

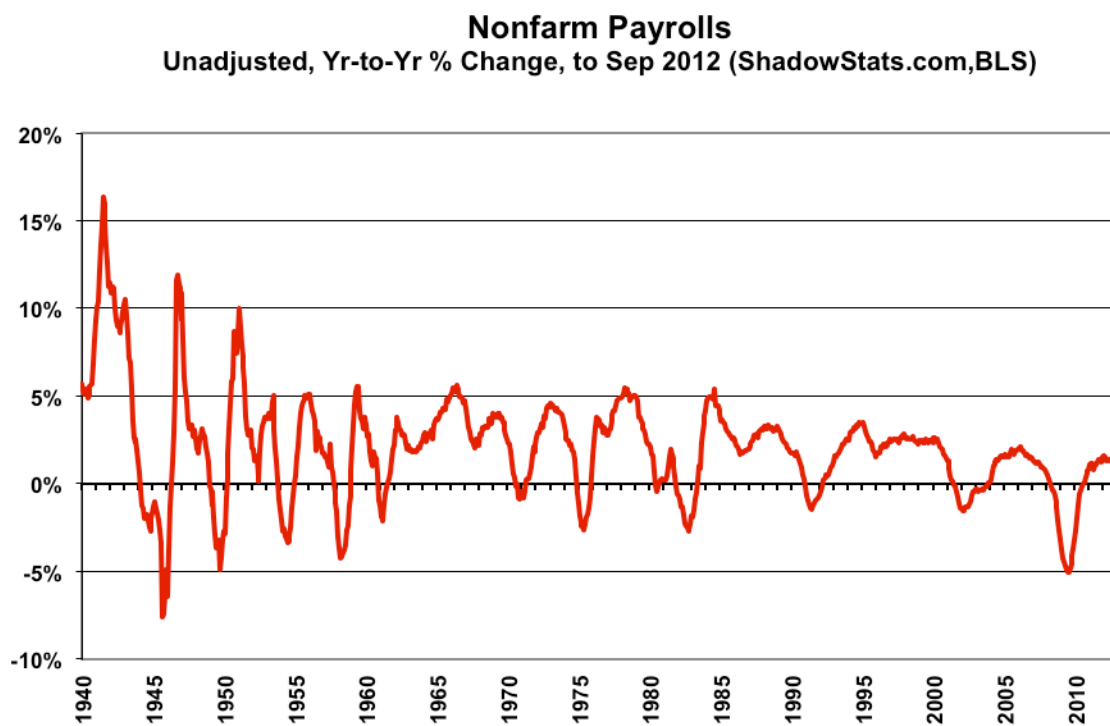
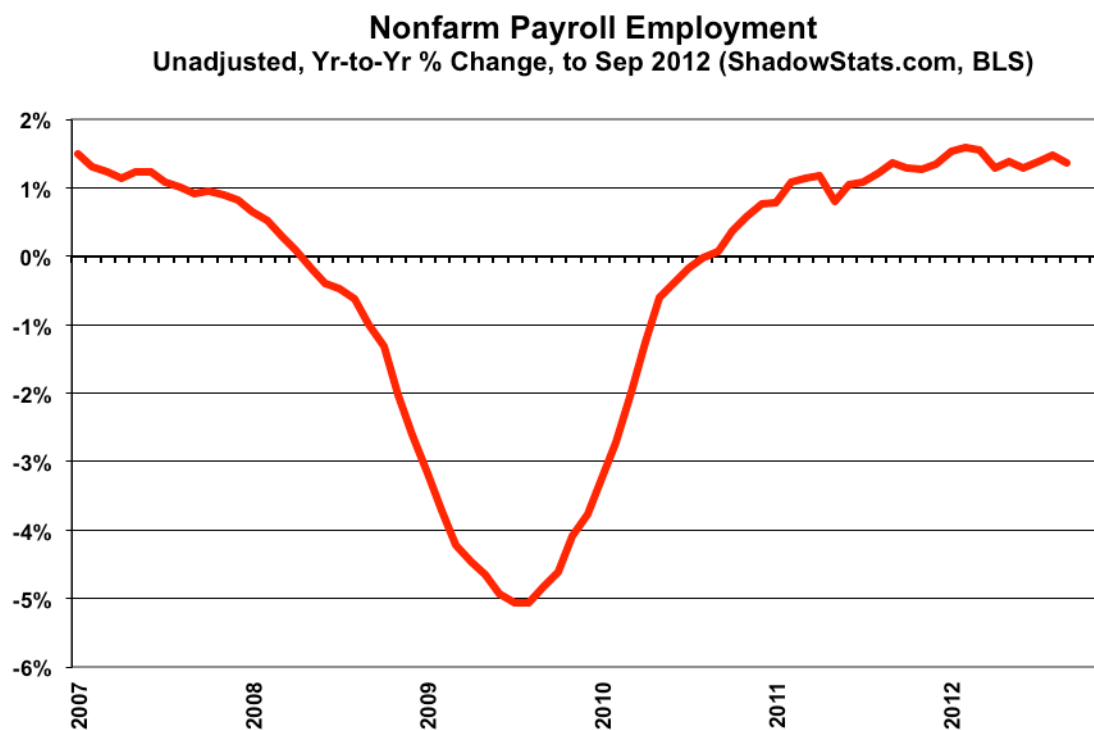
As described generally in [Payroll Trends](#), the trend indication from the BLS seasonal-adjustment model is for an 83,000 payroll gain in October, based on today's reporting. While the trend indication often misses actual reporting (the indication for September was a 104,000 gain, versus an actual 114,000 headline gain), it usually becomes the basis for the consensus outlook.

In terms of year-to-year change, the not-seasonally-adjusted growth in September 2012 payrolls was 1.38%, versus an upwardly revised 1.48% (previously 1.38%) in August.

The following graphs of year-to-year unadjusted payroll change had shown a slowly rising trend in annual growth into 2011, which primarily reflected the still-protracted bottom-bouncing in the payroll series. That pattern of growth flattened out in late-2011, as shown in the first graph of the near-term detail in year-to-year change, and it has fluttered around a slightly lower level since April 2012.

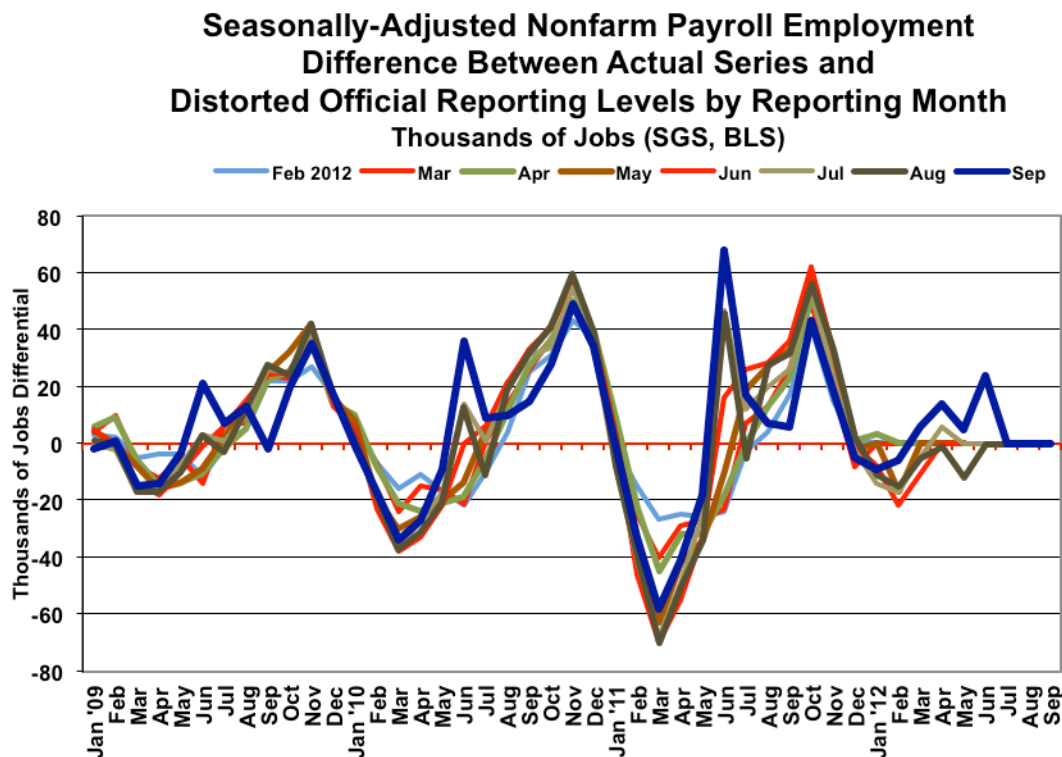
As shown in the longer-term graph (historical detail back to 1940), with the bottom-bouncing of recent years, current annual growth has recovered from the post-World War II record 5.06% decline in August 2009, which remains the most severe annual contraction seen since the production shutdown at the end of World War II (a trough of a 7.59% annual contraction in September 1945). Disallowing the post-war shutdown as a normal business cycle, the August 2009 annual decline was the worst since the Great Depression. Still, even with small annual growth in the series since mid-2010, the current level of employment is far from reflecting any economic recovery.

The regular graph of seasonally-adjusted payroll levels since 2000, showing detail of the current employment level well below its pre-2007 recession peak, as well as a longer-term graph of the payroll employment level, showing historical detail back to 1940 and, in perspective, that payroll levels still are minimally above levels in 2000, are located in the *Opening Comments and Executive Summary* section.



Concurrent Seasonal Factor Distortions. Unreported, seasonally-adjusted monthly payroll numbers still are showing a shift of first-half of the year jobs to the second-half of the year, with the peak upside reporting effect due for October 2012, the last employment report before the November election.

Despite revisions in the monthly data each month that go back years, the BLS only publishes two months of revisions with each nonfarm payrolls release (July and August in the current instance), so as not to confuse data users. (The BLS publishes no revised data on a monthly basis for the household survey, despite similar seasonal-adjustment approach, as discussed in the *Opening Comments and Executive Summary*, and in [Commentary No. 461](#), [Commentary No. 451](#) and [Commentary No. 453](#)). As a result, the reported July-through-September 2012 seasonally-adjusted payroll data are not consistent with earlier reporting. Conceivably, the shifting and unstable seasonal adjustments could move 80,000 jobs or more from earlier periods and insert them into the current period as new jobs, without there being any published evidence of that happening. The following graph suggests that something along those lines happened in September, with even greater effects due for October reporting.



The issues with the BLS's concurrent-seasonal-factor adjustments and related inconsistencies in the monthly reporting of the historical time series are further discussed and detailed in the ShadowStats.com posting on May 2nd of [Unpublished Payroll Data](#).

Note: Incomplete and inconsistent BLS payroll reporting continues. Eight months have passed since the annual benchmark revisions to payroll employment, and the latest concurrent seasonal factors show renewed misreporting of the BLS's own historical payroll levels, as well as ongoing instabilities in the BLS's seasonal factors.

As discussed in prior writings (see [Hyperinflation 2012](#), for example), seasonal-factor estimation for most economic series has been distorted severely by the extreme depth and duration of the economic contraction. These distortions are exacerbated for payroll employment data based on the BLS's monthly seasonal-factor re-estimations and lack of full reporting.

Where the BLS recalculates the monthly seasonal factors each month for payroll employment, going back a number of years, outside of benchmarks, it only publishes the revised data for the last two months of reporting. The benchmark revision that accompanied the release of January 2012 payrolls, in theory, included a full update of the revised concurrent seasonally-adjusted data (actually it is off by a month or two). In the preceding graph, though, the latest revised (but not published by the BLS) adjusted payroll data show increasingly volatile, monthly seasonal-adjustment distortions of up to 80,000 jobs per month, with previously-reported payroll employment being shifted from the first-half to the second-half of the year. If seasonal-adjustment factors were stable in month-to-month reporting, which they should be under normal circumstances, then the graph of differences would be flat and at zero.

Note: A further big issue remains that the month-to-month seasonally-adjusted payroll data have become increasingly worthless, with reporting errors likely now well beyond the official 95% confidence interval of +/- 129,000 jobs in the reported monthly payroll change. Yet the media and the markets tout the data as meaningful, usually without question or qualification.

Birth-Death/Bias Factor Adjustment. Despite the ongoing and regular overstatement of monthly payroll employment—as evidenced usually by regular and massive, annual downward benchmark revisions (2011 and the just-announced 2012, excepted)—the BLS generally adds in upside monthly biases to the payroll employment numbers. The process was created simply by adding in a monthly “bias factor,” so as to prevent the otherwise potential political embarrassment of the BLS understating monthly jobs growth. The “bias factor” process resulted from an actual such embarrassment, with the underestimation of jobs growth coming out of the 1983 recession. That process eventually was recast as the now infamous Birth-Death Model (BDM), which purportedly models the effects of new business creation versus existing business bankruptcies.

September 2012 Bias. The not-seasonally-adjusted September 2012 bias was a negative 9,000, versus a positive 87,000 in August 2012, and versus a current estimation of a negative 26,000 bias in September 2011. The aggregate upside bias for the 12 months ended September 2012 was 563,000, versus 546,000 in August. At present that is a monthly average of roughly 47,000 jobs created out of thin air, on top of some indeterminable amount of other jobs that are lost in the economy from business closings. Those losses simply are assumed away by the BLS as part of the BDM, as discussed below.

Problems with the Model. The aggregated upside annual reporting bias in the BDM reflects an ongoing assumption of a net positive jobs creation by new companies versus those going out business. Such becomes a self-fulfilling system, as the upside biases boost reporting for financial-market and political needs, with relatively good headline data, while often also setting up downside benchmark revisions for the next year, which traditionally are ignored by the media and the politicians. Where the BLS cannot

measure meaningfully the impact of jobs loss and jobs creation from employers starting up or going out of business, on a timely basis (within at least five years, if ever), such information is estimated by the BLS along with the addition of a bias-factor generated by the BDM.

Positive assumptions—commonly built into government statistical reporting and modeling—tend to result in overstated official estimates of general economic growth. Along with happy guesstimates, there usually are underlying assumptions of perpetual economic growth in most models. Accordingly, the functioning and relevance of those models become impaired during periods of economic downturn, and the current downturn has been the most severe—in depth as well as duration—since the Great Depression.

Indeed, historically, the BDM biases have tended to overstate payroll employment levels—to understate employment declines—during recessions. There is a faulty underlying premise here that jobs created by start-up companies in this downturn have more than offset jobs lost by companies going out of business. So, if a company fails to report its payrolls because it has gone out of business, the BLS assumes the firm still has its previously-reported employees and adjusts those numbers for the trend in the company's industry.

Further, the presumed net additional “surplus” jobs created by start-up firms, get added on to the payroll estimates each month as a special add-factor. These add-factors are set now to add an average of about 47,000 jobs per month in the current year, but the actual overstatement of monthly jobs likely exceeds that number by a significant amount. With the underlying economy continuing to falter, I expected a significant downside benchmark revision for 2012 (based on the upcoming March 2012 benchmark that will be published in 2013), and given current details of the BLS’s overly positive estimates. The BLS, however, published its preliminary estimate for the 2012 benchmark on September 27th, indicating an upside revision to not-seasonally-adjusted March 2012 payrolls of 386,000, or roughly 32.2 thousand per month. At that pace, there will be no relief in current reporting issues before the 2013 benchmark to be published in February of 2014.

HOUSEHOLD SURVEY DETAILS. As discussed in the *Opening Comments and Executive Summary* and earlier writings such as [Commentary No. 461](#), seasonally-adjusted month-to-month comparisons of components in the household survey have no meaning other than from the impact they have as hyped by the media, Wall Street and election-year politicians. The 0.3-percentage-point decline reported in the September headline unemployment rate could have been that, by extreme coincidence, but the headline number just easily could have reflected no change or even increased month-to-month.

The actual numbers could be revealed by the BLS, if it chooses to do so. There is no way to tell what they are, given current BLS reporting policies; the BLS calculates but does not report consistent data, as part of its standard monthly estimation process.

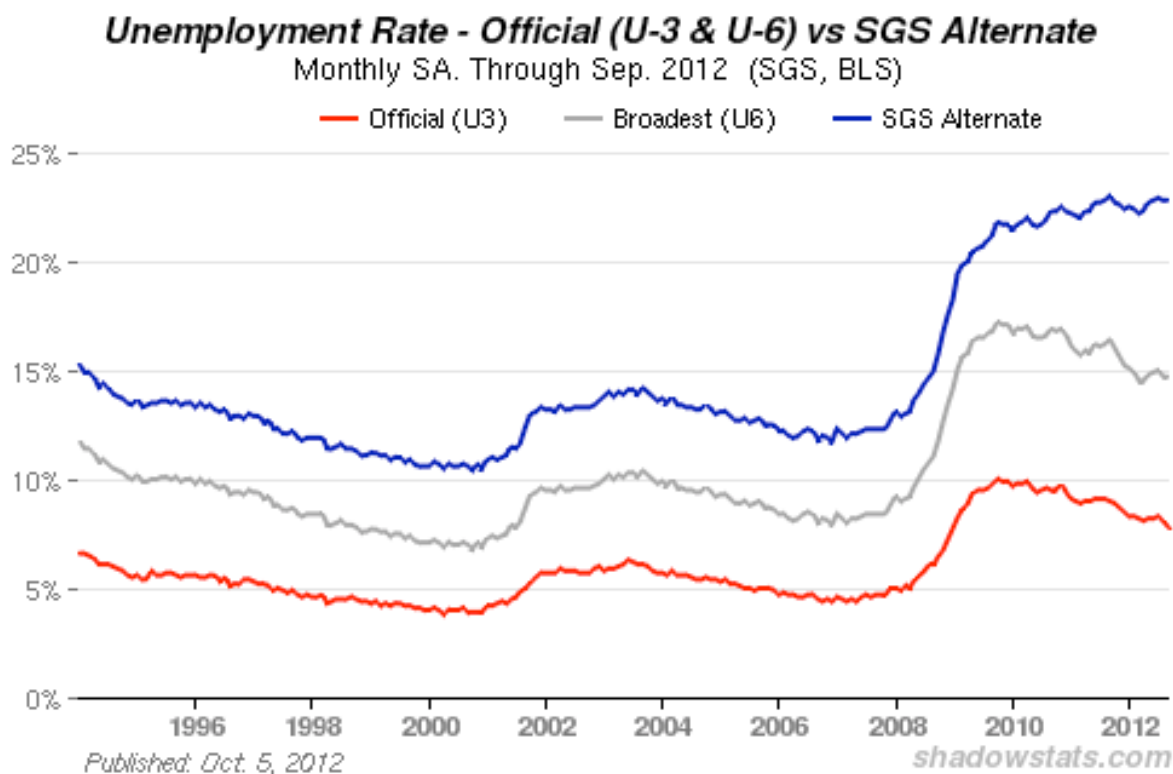
With that as background, following are the meaningless seasonally-adjusted numbers and absolutely worthless month-to-month comparisons, that will cause today’s markets to gyrate, will excite the popular press and will lead the political candidates to pontificate. Separately, at least the not-seasonally-adjusted numbers are consistent in their preparation.

Headline Household Employment. Based on the September household survey, which counts the number of people with jobs, as opposed to the payroll survey that counts the number of jobs (including multiple job holders more than once), September 2012 employment soared by an unbelievable 873,000, after

falling by 119,000 in August. As just discussed above, though, the seasonally-adjusted monthly change here is without significance, due to the underlying data not being comparable on a moth-to-month basis.

Unemployment Rates. The reported September 2012 seasonally-adjusted headline (U.3) unemployment rate of 7.80% was down by 0.31 percentage point, which rounds to the headline 0.3 percentage point, when compared the 8.11% unemployment rate that was separately and inconsistently estimated for August. In turn, similar numbers were separately and inconsistently estimated for July at 8.25%. The official +/- 0.23 percentage-point 95% confidence interval for the monthly headline number is meaningless in the context as discussed above, where the headline monthly change cannot be calculated due to underlying data inconsistencies, as discussed in the *Opening Comments*. On an unadjusted basis, September's U.3 unemployment rate was 7.6%, versus August's 8.2%.

CAUTION: Month-to-month comparisons of the various unemployment rates are meaningless due to deliberate inconsistencies in BLS reporting.



The broadest unemployment rate published by the BLS, U.6 includes accounting for those marginally attached to the labor force (including short-term discouraged workers) and those who are employed part-time for economic reasons (they cannot find a full-time job). The September U.6 unemployment rate held at a seasonally-adjusted 14.7%, the same as in August, and down from 15.0% in July. The unadjusted September U.6 rate declined to 14.2%, from 14.6% in August.

Discouraged Workers. The count of short-term discouraged workers (never seasonally-adjusted) eased to 802,000 in September, from 844,00 in August. The published number reflects the balance of the headline unemployed—increasingly giving up looking for work—leaving the U.3 unemployment category and being rolled into the U.6 measure as short-term “discouraged workers,” versus those moving from short-term status into the netherworld of long-term discouraged-worker status. It is the long-term discouraged worker category that defines the SGS-Alternate or ShadowStats.com Unemployment Measure.

In 1994, during the Clinton Administration, “discouraged workers”—those who had given up looking for a job because there were no jobs to be had—were redefined so as to be counted only if they had been “discouraged” for less than a year. This time qualification defined away the long-term discouraged workers. The remaining short-term discouraged workers (less than one year) are included in U.6.

Adding the SGS estimate of excluded long-term discouraged workers back into the total unemployed and labor force, unemployment—more in line with common experience as estimated by the SGS-Alternate Unemployment Measure—held at 22.8% in September, the same as in August, and down from 22.9% in July. The SGS estimate generally is built on top of the official U.6 reporting, and tends to follow its relative monthly movements. Accordingly, the SGS measure will suffer some of the current seasonal-adjustment woes afflicting the base series.

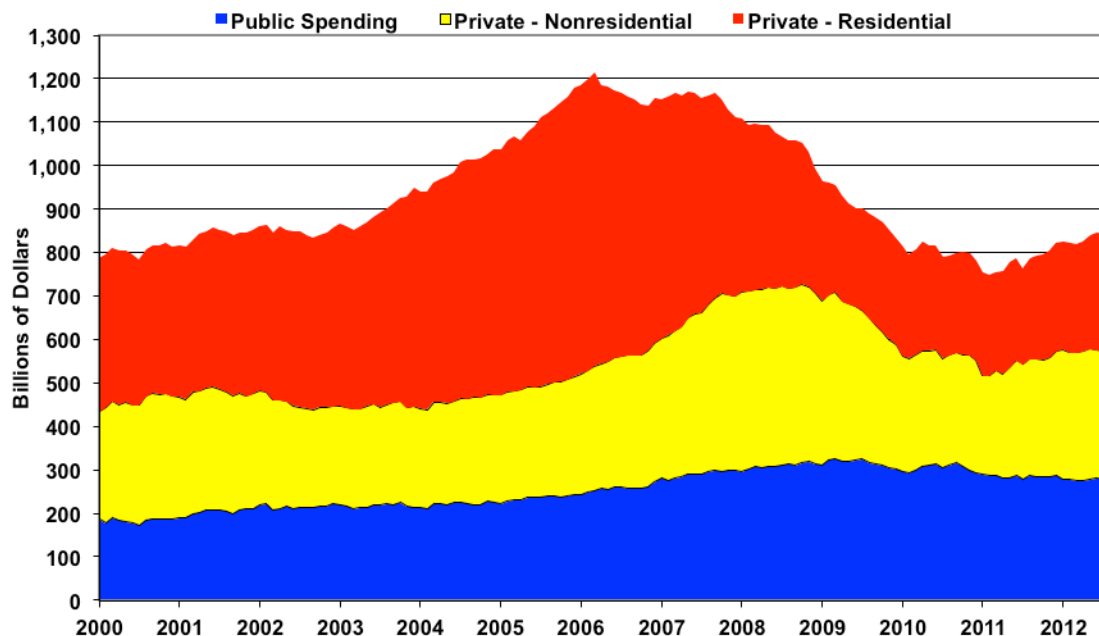
There continues to be a noticeable divergence, however, in the ShadowStats.com series versus U.6. The reason for this is that U.6, again, only includes discouraged workers who have been discouraged for less than a year. As the discouraged-worker status ages, those that go beyond one year fall off the government counting, and new workers enter “discouraged” status. Accordingly, with the continual rollover, the flow of headline workers continues into the short-term discouraged workers (U.6), and from U.6 into long-term discouraged worker status (ShadowStats.com Measure), at what has been an accelerating pace. The aggregate August data show an increasing rate of individuals dropping out of the headline (U.3) labor force. See the [Alternate Data](#) tab for more detail.

As discussed in previous writings, an unemployment rate nearing 23% might raise questions in terms of a comparison with the purported peak unemployment in the Great Depression (1933) of 25%. The SGS level likely is about as bad as the peak unemployment seen in the 1973 to 1975 recession. The Great Depression unemployment rate was estimated well after the fact, with 27% of those employed working on farms. Today, less than 2% work on farms. Accordingly, for purposes of Great Depression comparison, I would look at the estimated peak nonfarm unemployment rate in 1933 of 34% to 35%.

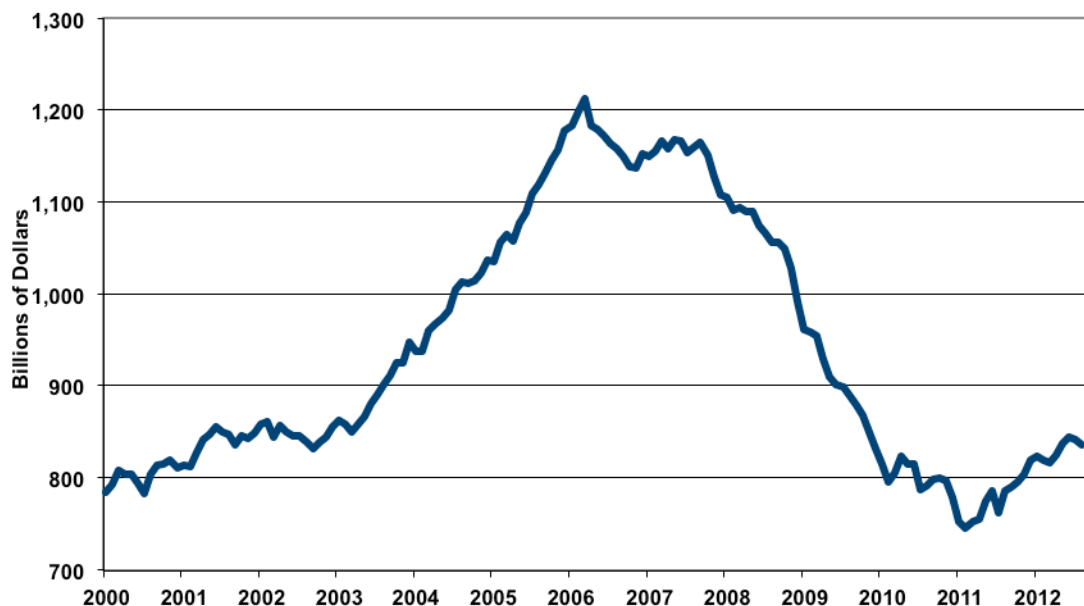
CONSTRUCTION SPENDING (August 2012)

Decline in August Construction Spending Continued to Reflect Bottom-Bouncing. The trend of stagnation in construction spending, at low levels of activity, remained in place, as of the latest survey. The Census Bureau reported October 1st that the total value of construction put in place in the United States during August 2012 was \$837.1 billion, on a seasonally-adjusted—but not inflation-adjusted—annual-rate basis. That estimate was down for the month by a statistically-insignificant 0.6% +/- 2.5% (all confidence intervals are at a 95% level), from an upwardly revised \$842.0 billion (previously \$834.4 billion) in July. Before prior-period revisions, the August spending level actually was up by 0.3% from initial July reporting. The monthly decline for July versus June was revised to 0.4% (previously 0.9%).

Construction Spending, Monthly to August 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)

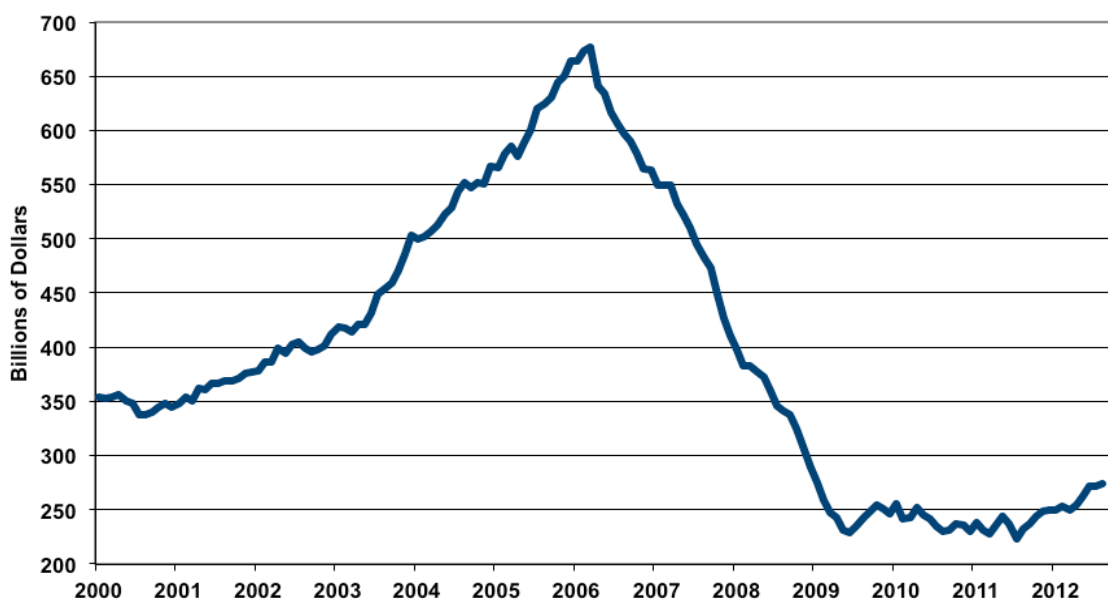


Total Construction Spending, Monthly to August 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)

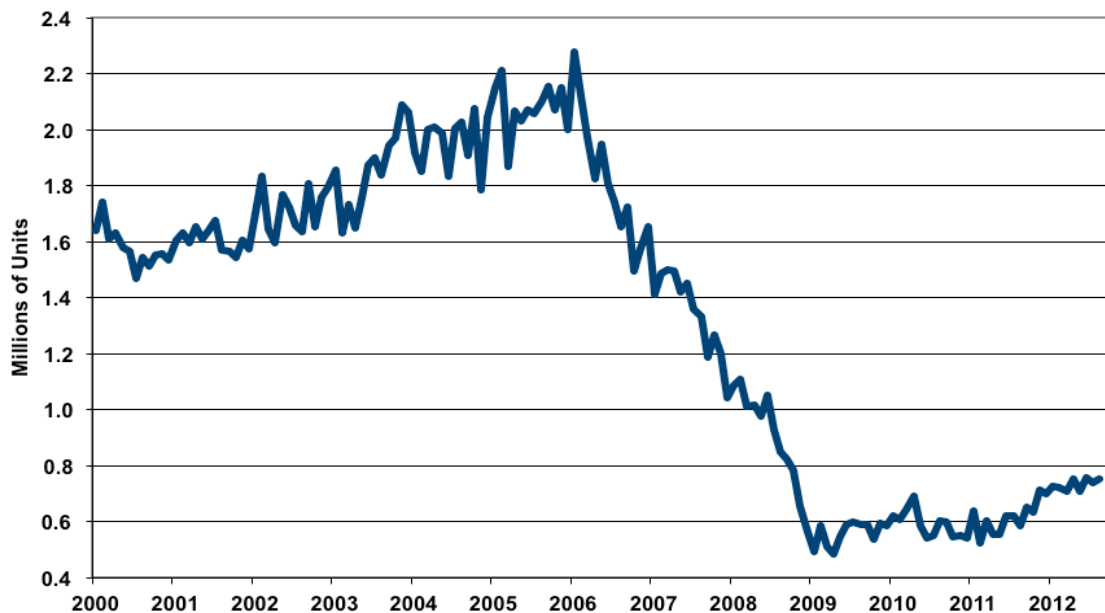


The following graph on private residential spending is shown along with an accompanying graph on the housing starts data as of August 2012. The difference is the smoother pace of actual spending (not-adjusted for inflation), instead of the less regular count of physical monthly starts.

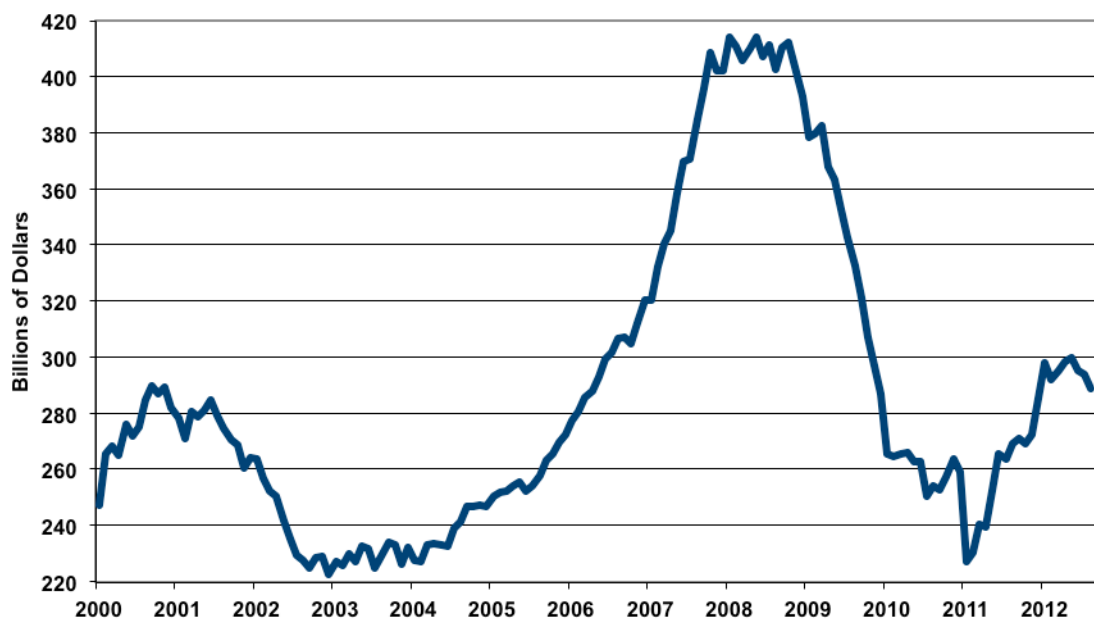
Private Residential Construction to August 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



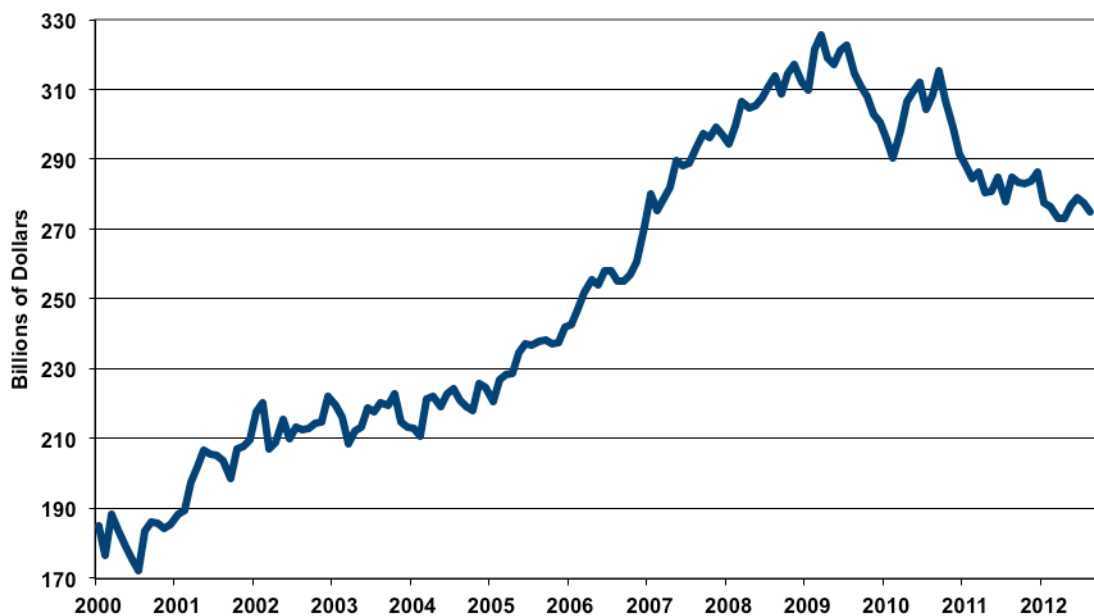
Housing Starts (Annual Rate by Month)
To August 2012, Seasonally-Adjusted (ShadowStats.com, Census)



Private Nonresidential Construction to August 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



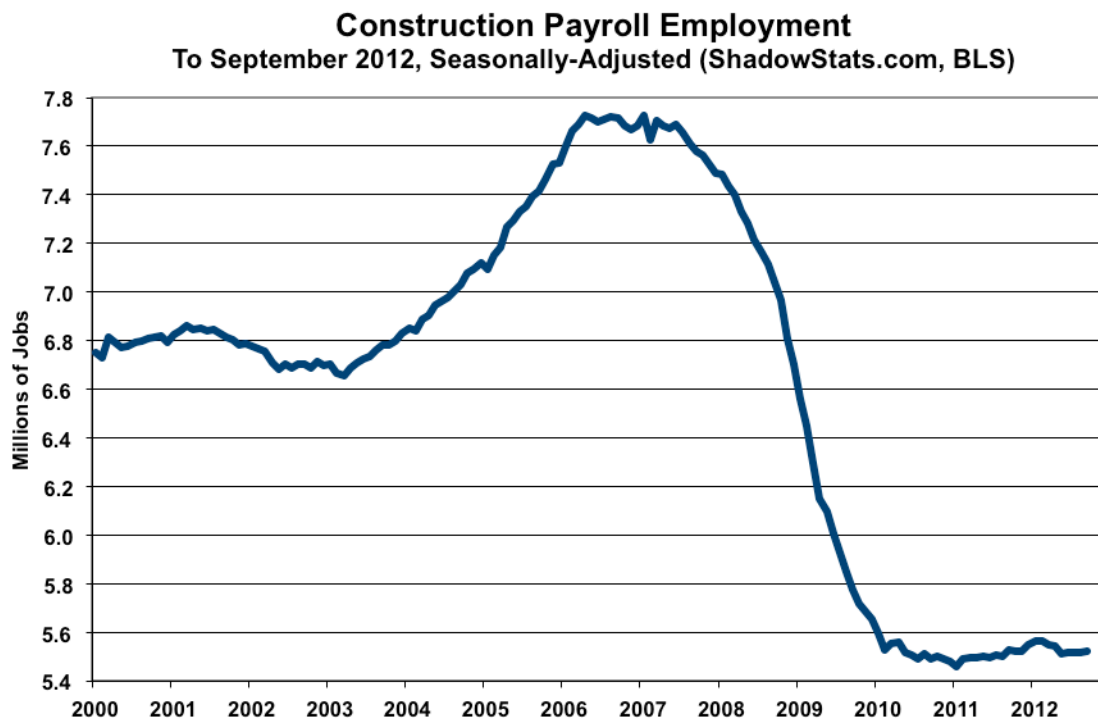
Public Construction, Monthly to August 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



Although aggregate August construction spending was up year-to-year by a statistically-significant 6.5% +/- 2.5%, the gain likely was more than covered by increases in construction costs. The Bureau of Economic Analysis (BEA) underestimated the year-to-year inflation in “structures” at 4.0% for second-quarter 2012. Year-to-year, July 2012 construction growth was revised higher to 10.3% (previously 9.3%).

The insignificant 0.6% decline in monthly August construction spending included a 0.8% drop in August public construction spending, which revised to a 0.5% (previously 0.4%) contraction in July. August private construction fell by 0.5% in the month, versus a revised 0.3% (previously 1.2%) monthly decline in July.

As reflected in the preceding graphs, August total construction fell by 0.6% for the month, with private residential construction up by 0.9%, private nonresidential construction down by 1.7% and public construction down by 0.8% for the month.



As shown in the graph above, in line with the ongoing bottom-bouncing reported through August 2012 in construction spending, and suggestive of continued industry stagnation in September, the seasonally-adjusted September construction-employment level was reported at 5.523 million in September, little changed from a revised 5.518 (previously 5.515) million in August, per the September payroll survey as published today by the Bureau of Labor Statistics.

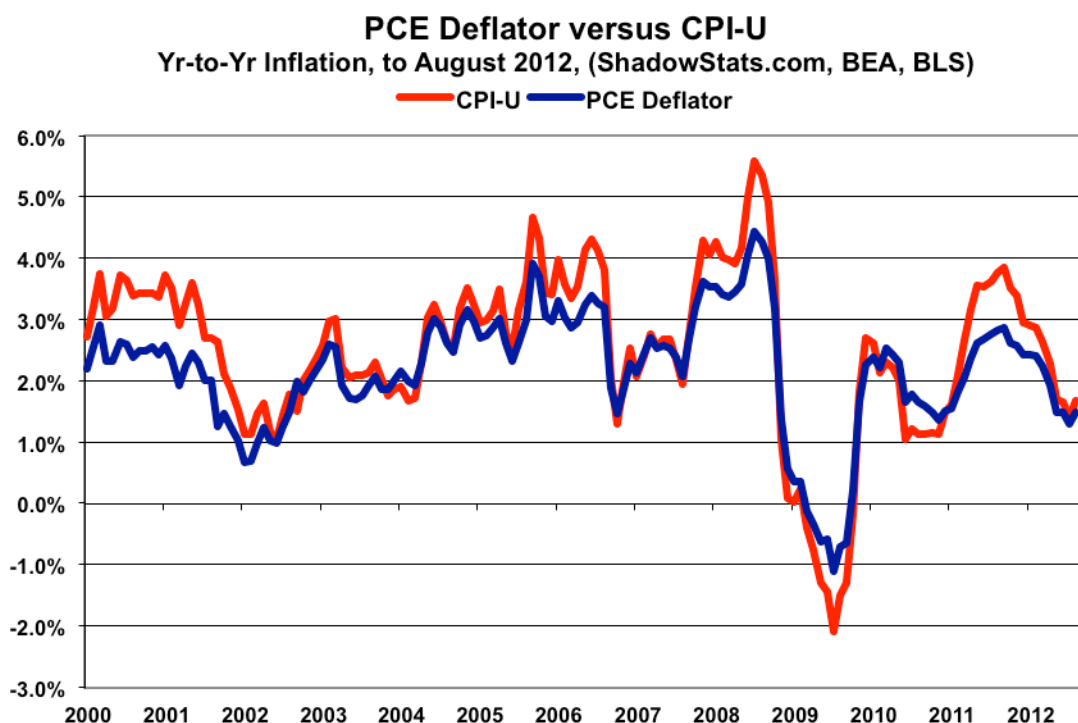
PERSONAL CONSUMPTION EXPENDITURE (PCE) DEFLATOR (August 2012)

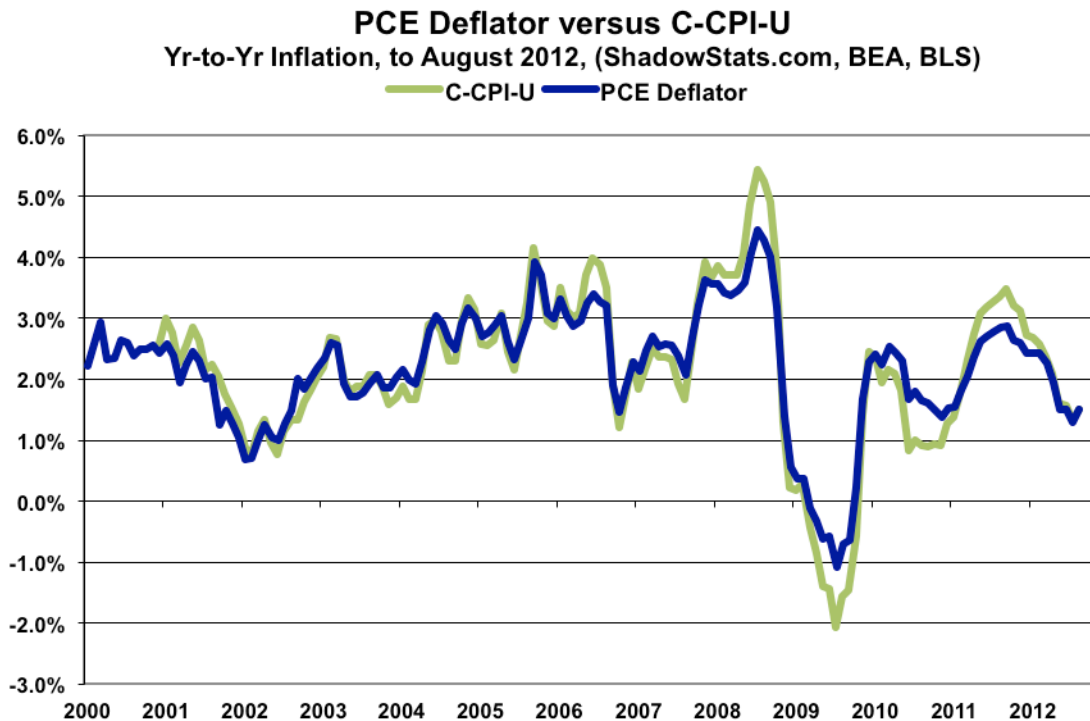
August PCE Deflator Jumped 0.43% for the Month, with Year-to-Year Inflation at 1.49%.

Published on September 28th by the Bureau of Economic Analysis (BEA), the seasonally-adjusted August PCE deflator was up by 0.43% for the month, versus revised 0.12% monthly gain (previously unchanged [up by 0.01%]) in July.

Year-to-year PCE-deflator growth picked up to 1.49% in August, versus a revised 1.29% (previously 1.30%) increase in July. Annual PCE inflation held below the Fed's 2.0% target for the fifth straight month. Nonetheless, below-target PCE inflation reporting should not become a protracted pattern here. The PCE deflator tends to follow the general direction of the CPI measures, which are due for a jump, again, in September.

PCE Deflator versus Other Inflation Measures. Where, in theory the PCE deflator measure should be virtually identical to the chain-weighted-CPI (C-CPI-U) (see [Commentary No. 470](#) for details of the latest C-CPI-U and other inflation measures), it did catch-up with the C-CPI-U in the two most recent months of reporting, as shown in the accompanying graphs. The August 2012 PCE deflator showed 1.5% year-to-year inflation, versus 1.3% in July. That compared with annual inflation in the August C-CPI-U at 1.5%, versus 1.3% in July; August CPI-U at 1.7%, versus 1.4% in July; August CPI-W at 1.7%, versus 1.3% in July; and the August SGS-Alternate (1980-Base) at 9.3%, versus 9.0% in July.





This “inflation targeting” effort by the Federal Reserve primarily is window-dressing for those in the markets who think the Fed really would move to contain inflation at the cost of impairing still-fragile banking-system solvency. The Fed’s primary function remains keeping the banking system afloat, at any cost, as suggested by the introduction of QE3, and as likely will be demonstrated again as the U.S. central bank overtly reacts to a re-intensifying systemic solvency crisis.

NOTE: The PCE deflator is the heavily massaged and modeled inflation rate for personal consumption expenditure, published on a monthly basis by the Bureau of Economic Analysis (BEA), and quarterly as part of the GDP release. The monthly series, which is a surrogate measure of consumer inflation—fully substitution and hedonic-based—generally tends to yield, and currently is yielding the lowest annual consumer inflation rate of the major series (see the preceding graphs of the PCE deflator versus the CPI-U and the C-CPI-U. Unlike the more widely followed CPI-U measure, which never is revised and is published on a seasonally unadjusted-basis, the PCE deflator is heavily revised for many years following initial reporting, and it is available only on a heavily-massaged, seasonally-adjusted basis.

Week Ahead. Market recognition of an intensifying double-dip recession has taken stronger hold, at the moment, while recognition of a mounting inflation threat has been rekindled a bit by recent Fed monetary policy announcements and rising headline inflation numbers. 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, otherwise, it puts a happy spin on the numbers; and the financial markets 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, as discussed in the Hyperinflation Watch section.

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.

U.S. Trade Balance (August 2012). The August 2012 trade deficit detail will be released on Thursday, October 11th. The U.S. trade deficit continues in fundamental deterioration, with the effect that the August number has a fair shot of deteriorating by more than market expectations. A deteriorating deficit has negative impact on GDP growth. A significantly wider deficit in August (or July in revision) would tend to put downside pressure on third-quarter GDP estimates, while a significant continued narrowing in the deficit (as indicated in initial July reporting) would tend to boost the GDP. The general trend here going forward, again, though, likely will be for trade deterioration and net negative impact on the GDP estimates.

Producer Price Index—PPI (September 2012). The September 2012 PPI is scheduled for release on Friday, October 12th, by the Bureau of Labor Statistics (BLS), and it should show a strong gain monthly gain for a second month. Depending on the oil contract followed, oil prices were flat to plus fifteen percent on average in September. The gain in related energy prices should be supplemented, again, by seasonal adjustments that tend to boost energy prices at this time of year. Higher food price in combination with still relatively strong “core” inflation and energy should generate something of a jump (likely above consensus) in September wholesale prices.
