

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

**COMMENTARY NUMBER 476**

**September CPI, Industrial Production, Real Retail Sales and Earnings**

**October 16, 2012**

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**Quarterly Industrial Production Contracted for First Time Since Official Recession**

**Quarterly Pace of Inflation Picked Up, With CPI and PPI Topping Market Expectations**

**September Year-to-Year Inflation: 2.0% (CPI-U), 2.0% (CPI-W), 9.6% (SGS)**

**Real Average Weekly Earnings Continued to Tumble**

**Inflation Provided Half of September Retail Sales Growth**

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*PLEASE NOTE: The next regular Commentary is scheduled for tomorrow, Wednesday, October 17th, covering September housing starts.*

*A Special Commentary reviewing economic, inflation and systemic conditions is planned for Monday, October 29th. It will include significant September-economic and third-quarter-GDP reporting, as well as detail on fiscal-2012 operations of the federal government. Any updates to timing of this missive will be advised in the schedule box on [www.shadowstats.com](http://www.shadowstats.com).*

*Best wishes to all — John Williams*

**Opening Comments and Executive Summary.** The economy continues to show signs of faltering, while the pace of inflation continues to increase. On the economic front, half the 1.15% monthly gain

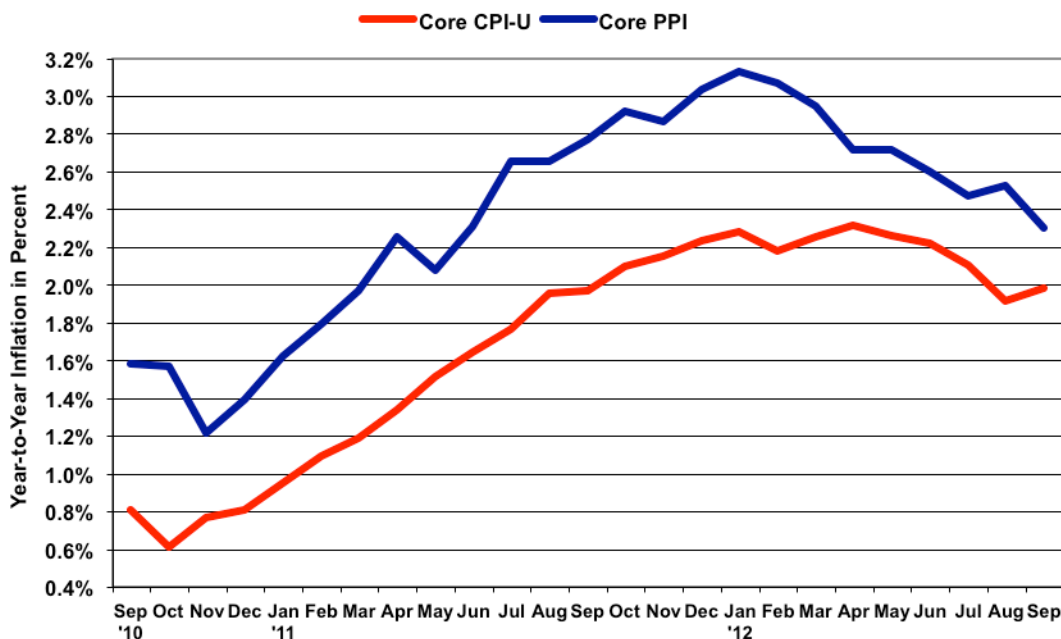
reported in September retail sales (see [Commentary No. 475](#)) was due to inflation, and that non-inflation component likely will evaporate away in the monthly revisions ahead. The 0.41% monthly gain in September industrial production was due largely to prior-period downside revisions. Nonetheless, as reported, third-quarter 2012 industrial production showed the first quarterly contraction for the series since the end of the “recession” in second-quarter 2009.

Reflecting both weak labor conditions and rising consumer inflation, real (inflation-adjusted) average weekly earnings continued to tank, down 0.4% for the month of September 2012, and down by 0.3% year-to-year, all based on official Bureau of Labor Statistics (BLS) inflation reporting. Accordingly, consumer liquidity remains impaired and chances of an actual near-term economic recovery remain nil.

In conjunction with the preceding, negative trade impact on third-quarter GDP (see [Commentary No. 474](#)), and flat-to-positive quarterly housing starts likely in tomorrow’s reporting, the “advance” estimate of third-quarter 2012 GDP, due for release on Friday, October 26th, has a fair shot of coming in weaker than the current 1.3% headline growth rate for second-quarter GDP. That also would provide a downside reporting surprise to market expectations of stronger growth. A weaker number is a virtual certainty, after ensuing monthly revisions.

***A Continuing Surge in Inflation.*** The headline September CPI-U monthly inflation number was 0.6% for the second month, reflecting some minor catch up in gasoline price inflation. Year-to-year inflation rose from 1.7% in August to 2.0% in September. Parallel moves were seen in the other series with CPI-W up by 0.7% for the second month, with annual inflation increasing from 1.7% in August to 2.0% in September. Adjusted to pre-Clinton (1990) methodology, annual SGS-Alternate CPI inflation rose from roughly 5.2% in August to 5.5% in September, while the 1980-based measure rose from about 9.3% in August to 9.6% in September, versus 9.0%.

**"Core" CPI-U and PPI Year-to-Year Inflation**  
Since QE2 Announcement Nov. 3, 2010 (SGS, BLS)



**Core Inflation.** The inflationary pressures from high oil prices have continued to spread in the broad economy, as shown in the accompanying graph, which has tracked the impact of QE2 on “core” inflation, inflation net of direct food and energy inflation. High oil prices, however, still have significant, longer-range inflationary impact on the general economy. Based on early market reaction to QE3, new inflationary impact should surface in the core numbers of the months ahead, but it has not done so, yet.

The September 2012 year-to-year CPI-U core inflation was 1.98% versus 1.91% in August. In contrast, the PPI annual core inflation turned somewhat lower in September to 2.30%, versus 2.53% in August.

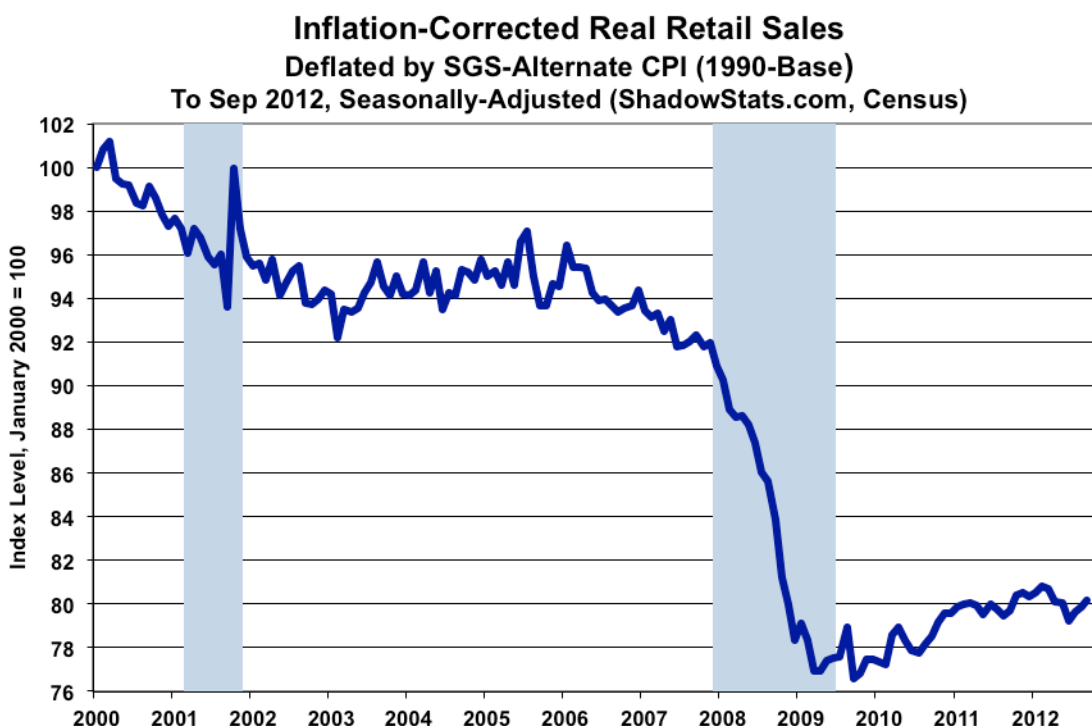
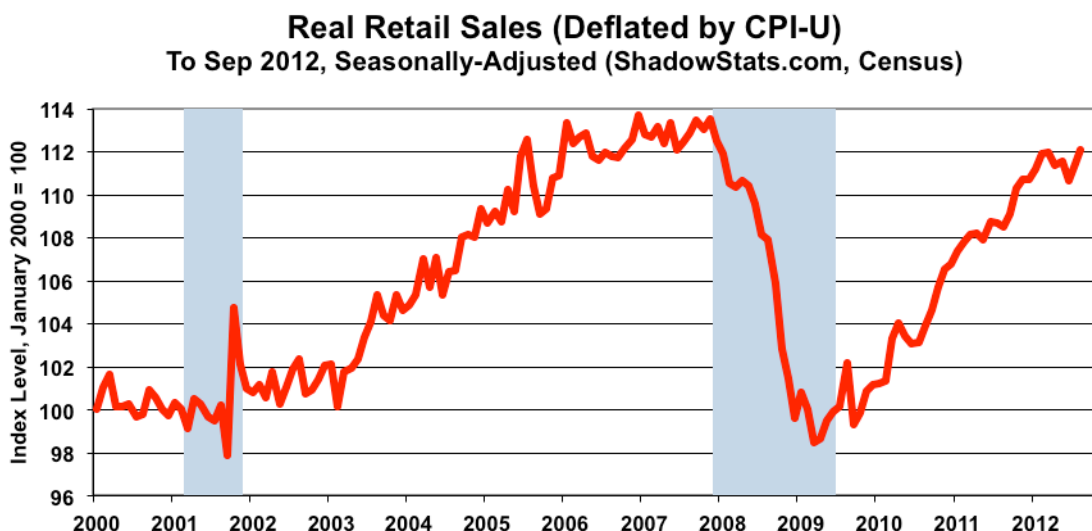
**See Reporting Detail.** Other than for the series referenced above to other *Commentaries*, the numbers discussed in the *Opening Comments* are covered more fully in the *Reporting Detail* section. What follows next are the “inflation-corrected” series for retail sales and industrial production, which provide estimates of actual retail sales and industrial production series net of the impact of the understated inflation used in reporting those headline series.

**Real (Inflation-Adjusted) Retail Sales.** The chances for sustainable, real (inflation-adjusted) gains in retail sales remain nil, where the consumer lacks adequate income growth and credit availability to fund ongoing increases in real consumption. Various consumer liquidity issues were discussed recently in [Commentary No. 469](#) and were reviewed partially in [Commentary No. 475](#).

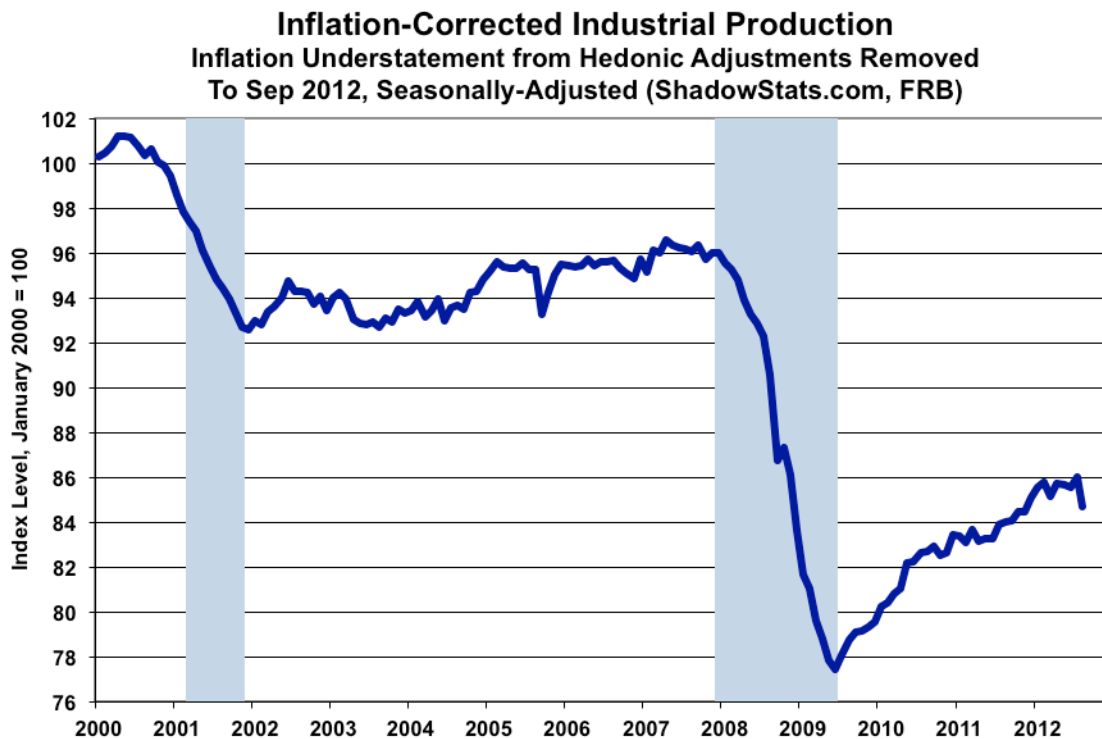
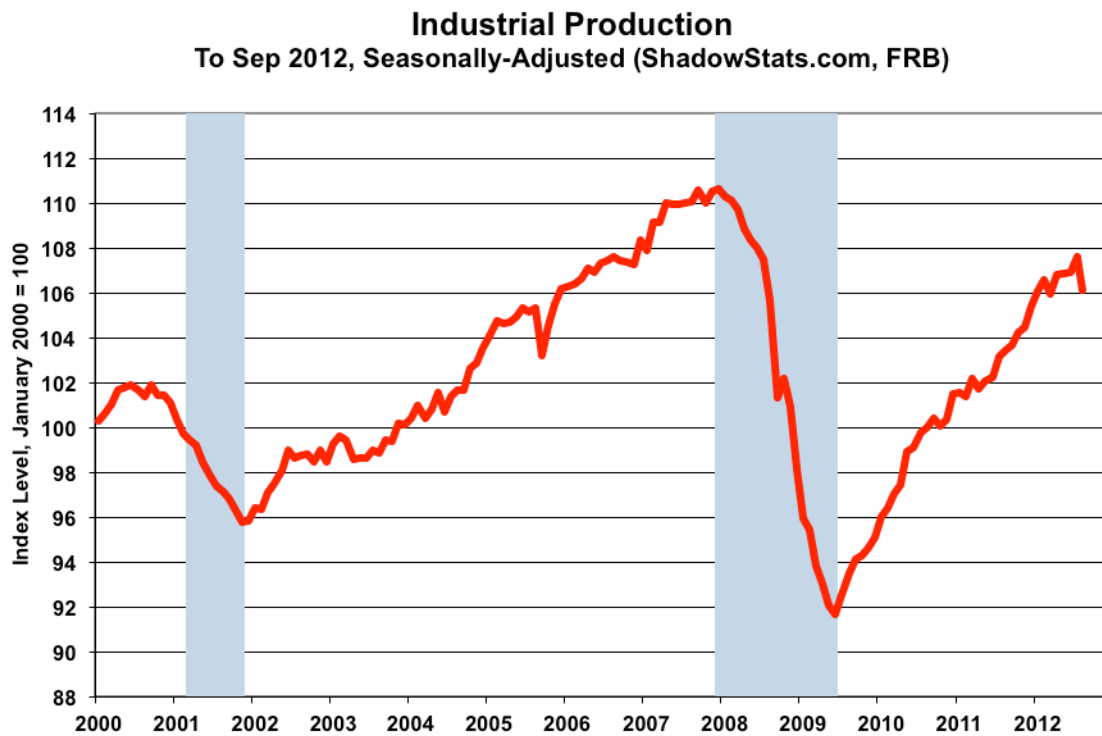
**Inflation-Corrected Retail Sales.** The first graph following reflects real retail sales as reported by the St. Louis Fed and as deflated by the CPI-U. The CPI-U, however, understates inflation (see the [Public Comment on Inflation](#)), with the effect of overstating the inflation-adjusted growth.

Instead of being deflated by the CPI-U, the “inflation-corrected” numbers in the second graph use the SGS-Alternate Inflation Measure (1990-Base) for deflation. As discussed in [Hyperinflation 2012](#) and [Special Commentary No. 445](#), with the higher inflation of the SGS measure, the revamped numbers suggest a topping out process in a series that has been bottom-bouncing along a low-level plateau of economic activity in the period following the economic collapse.

The two charts are indexed to a consistent scale, and they update *Graphs 28* and *29* in [Special Commentary No. 445](#).



**Industrial Production.** Headline September 2012 industrial production reflected a third-quarter 2012 quarterly decline, even in official reporting. The following graphs update *Graphs 30* and *31* in [Special Commentary No. 445](#). The first reflects official industrial production, indexed to January 2000 = 100, instead of the 2007 = 100 used by the Fed. The 2000 indexing is used to provide for some consistency in these revamped graphics. The second graph is an inflation-corrected version of the first, with estimated hedonic-inflation adjustments backed-out of the official deflator used in reporting a number of industrial-production components.



**Hyperinflation Watch—Outlook Unchanged, Broad 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 *Special Commentary* scheduled for October 29th. The following summary of the broad outlook 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](#).

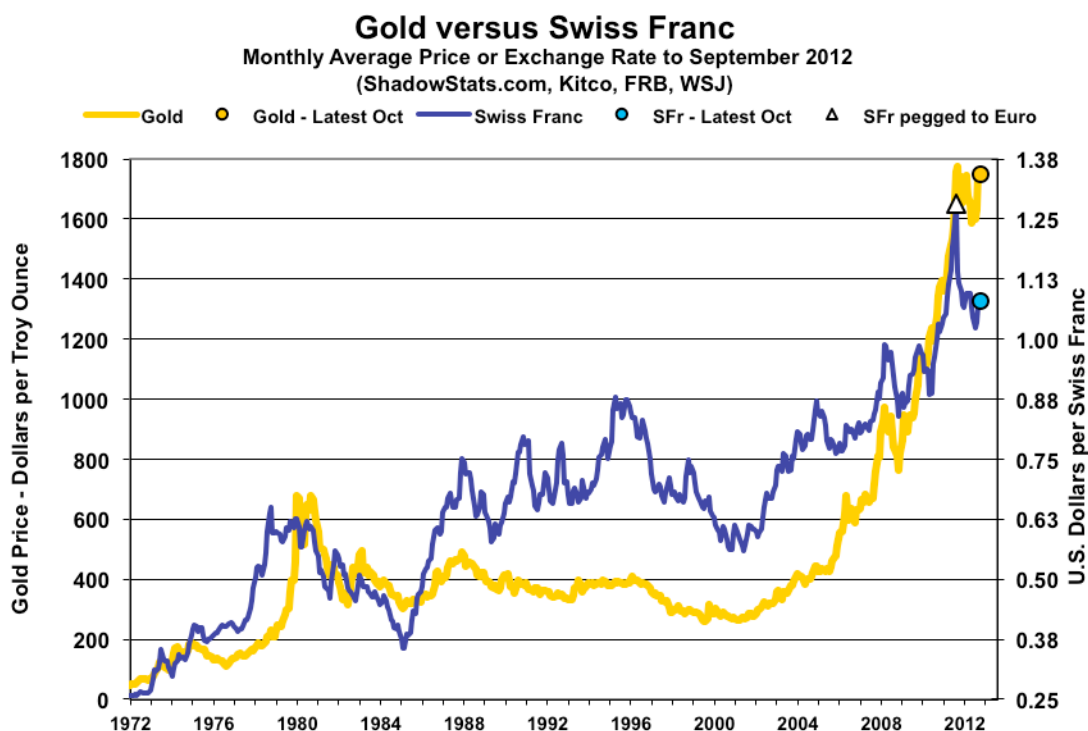
With the economy weak enough to provide political cover for further Federal Reserve accommodation to the still-struggling banking system, QE3 was introduced on September 13th. That action effectively provided for open-ended monetization of U.S. Treasury debt at the Fed’s discretion. The mechanism for

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.

**Traditional Gold Graphs.** Following are graphs of the price of gold versus the Swiss franc, oil and silver that usually are published with the monthly *Commentary* covering the CPI release. Added to the “Gold versus Swiss franc” graph is a marker for when the Swiss National Bank (SNB) moved to tie the Swiss franc to the falling euro, while the U.S. dollar otherwise was collapsing against the stronger Western currencies and gold.

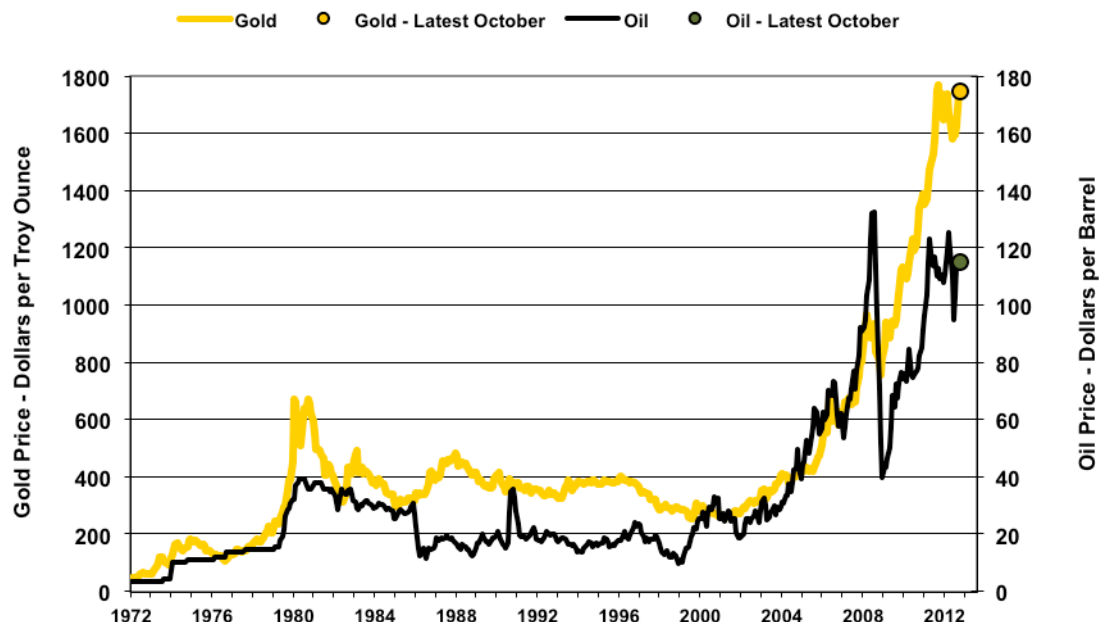
That dollar sell-off was a result of global rejection of the U.S. currency in the wake of the just-demonstrated inability and unwillingness of the U.S. government to address its mortal sovereign-solvency problems. What happened in July and August 2011 was just a taste of what lies ahead in a full collapse of the U.S. dollar. Intervention needed to maintain the artificial peg of the Swiss franc to the euro has become expensive for the SNB and likely will not hold through the next dollar crisis.





## Gold versus Oil (WTI/Brent)

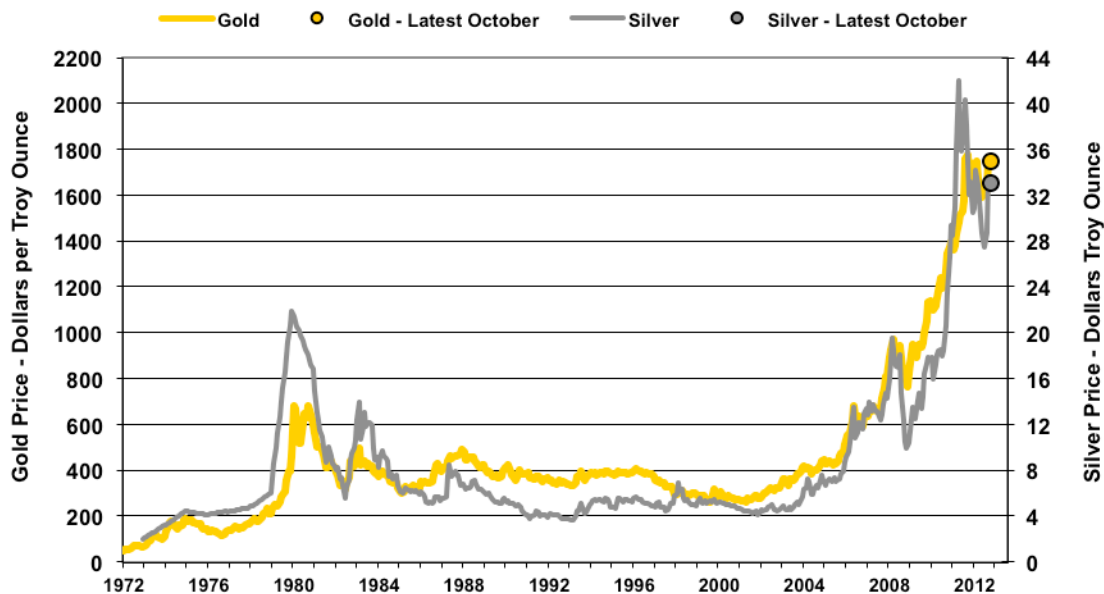
Monthly Average Prices to Sep 2012, Pre-1987 is WTI (ShadowStats.com, Kitco, DOE)



## Gold versus Silver

Monthly Average Price Levels to September 2012

Pre-1981 Silver is Year-End (ShadowStats.com, Kitco, Handy & Harman)





## REPORTING DETAIL

### CONSUMER PRICE INDEX—CPI (September 2012)

**September Headline CPI-U Inflation Hit 0.6% for Second Consecutive Month.** Reflecting minimal catch up from the underreporting of gasoline inflation in August, the September headline 0.6% month-to-month inflation topped a consensus expectation of around 0.5%. Other than for August's similar reporting, the headline inflation number was the strongest since June 2009. Accordingly, the annual inflation rate also rose, with the year-to-year September 2012 CPI-U inflation increasing to 2.0%, from 1.7% in August.

A pattern of surging inflation was evident in the September 2012 finished-goods PPI, as well, which topped headline expectations, gaining 1.1% for September 2012 and 2.1% year-to-year (see [Commentary No. 474](#) for details).

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### ***Notes on Different Measures of the Consumer Price Index***

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

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

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

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

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

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**CPI-U.** The BLS reported today (October 16th) that the headline, seasonally-adjusted CPI-U for September 2012 rose by 0.57% (0.45% unadjusted) for the month. That followed an adjusted August monthly increase of 0.60% (up by 0.56% unadjusted).

Reported monthly-average gasoline prices and related seasonal factors caught up partially in September, from some understatement in August. Per the Department of Energy, unadjusted monthly average gasoline prices rose by 3.4% in September 2012. In 2011, September seasonal adjustments boosted energy price inflation, where an unadjusted 0.7% monthly decline in September 2011 gasoline prices was turned into a 2.9% increase for the seasonally-adjusted number.

As published in today's reporting, unadjusted monthly average gasoline prices for September rose by 4.1% per the BLS. Seasonally-adjusted, September's gasoline prices gained 7.0% for the month, versus the unadjusted 4.1% gain.

On a seasonally-adjusted quarterly basis, annualized quarterly inflation for the CPI-U was 2.30% in third-quarter 2012, versus 0.75% inflation in the second-quarter.

September 2012 unadjusted year-to-year CPI-U inflation increased to 1.99%, from 1.69% in August.

Year-to-year total CPI-U inflation would increase or decrease in next month's October 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the virtually unchanged (a 0.03% contraction) reading in the adjusted monthly level reported for October 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for October 2012, the difference in October's headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from the September 2012 annual inflation rate of 1.99%.

Eighteen of the last twenty-two months have shown rising year-to-year, or annual, "core" CPI-U inflation (net of food and energy inflation), including the September 2012 year-to-year core rate of 1.98%, versus a 1.91% annual rate in August. Still, the September annual core rate remains off April's cycle-high of 2.31%. In contrast, the PPI annual core inflation turned somewhat lower in September, to 2.30%, from 2.53% in August.

The September CPI core rate still was well above the core inflation of 0.61%, in November 2010, when Mr. Bernanke introduced QE2 in a successful bid to debase the U.S. dollar, with the effect of spiking oil prices. The introduction of QE3 should create some renewed upside pressures here, but those pressures still are pending. The core annual inflation numbers for both the CPI-U and PPI reflect the ongoing impact of higher energy prices in the broad economy (see the graph and comments in the *Opening Comments and Executive Summary*).

**CPI-W.** The headline seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.67% (0.50% unadjusted) for the month, versus a seasonally-adjusted 0.74% (0.66% unadjusted) gain in August.

On a seasonally-adjusted quarterly basis, annualized quarterly inflation for the CPI-W was 2.50% in third-quarter 2012, versus 0.33% inflation in the second-quarter.

Unadjusted, September 2012 year-to-year CPI-W inflation was 2.01%, versus 1.67% in August.

**C-CPI-U.** Year-to-year inflation for the September 2012 C-CPI-U was 1.72%, versus 1.51% in August.

*Note: The chain-weighted CPI-U is the fully substitution-based series that gets touted as a CPI replacement by inflation apologists and by those who oppose use of the existing CPI-U and CPI-W, including a number of politicians looking to cut deficit spending by using the C-CPI-U to reduce Social Security annual cost of living (COLA) adjustments artificially. The series is reported only on an unadjusted basis and is revised annually for the prior two years, unlike the unadjusted CPI-U, which never is revised, except for outright calculation errors.*

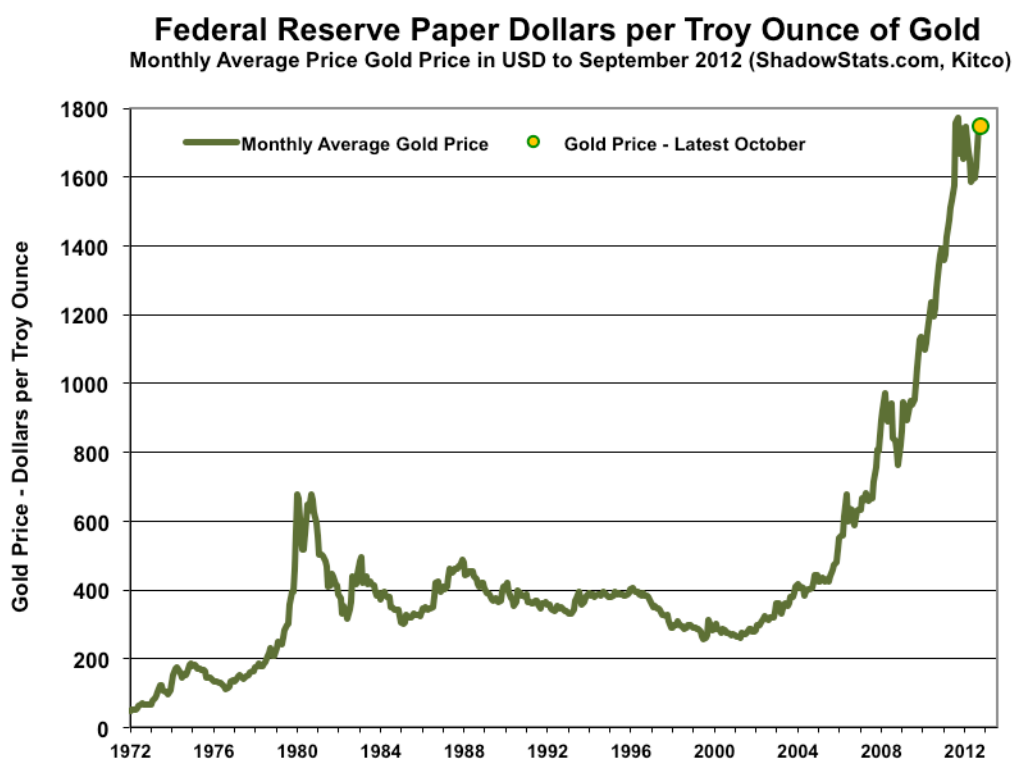
**Alternate Consumer Inflation Measures.** Adjusted to pre-Clinton (1990) methodology, annual CPI inflation was roughly 5.5% in September 2012, versus 5.2% in August. The SGS-Alternate Consumer Inflation Measure, which reverses gimmicked changes to official CPI reporting methodologies back to 1980, was about 9.6% (9.64% for those using the extra digit) in September 2012, versus 9.3% in August.

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

**Gold and Silver Highs Adjusted for CPI-U/SGS Inflation.** Despite the September 5, 2011 historic-high gold price of \$1,895.00 per troy ounce (London afternoon fix), and despite the multi-decade-high silver price of \$48.70 per troy ounce (London fix of April 28, 2011), gold and silver prices have yet to re-hit their 1980 historic levels, adjusted for inflation. The earlier all-time high of \$850.00 (London afternoon fix, per Kitco.com) for gold on January 21, 1980 would be \$2,528 per troy ounce, based on September 2012 CPI-U-adjusted dollars, and \$9,513 per troy ounce based on September 2012 SGS-Alternate-CPI-adjusted dollars (all series not seasonally adjusted).

In like manner, the all-time high price for silver in January 1980 of \$49.45 per troy ounce (London afternoon fix, per silverinstitute.org), although approached in 2011, still has not been hit since 1980, including in terms of inflation-adjusted dollars. Based on September 2012 CPI-U inflation, the 1980 silver-price peak would be \$147 per troy ounce and would be \$553 per troy ounce in terms of September 2012 SGS-Alternate-CPI-adjusted dollars (again, all series not seasonally adjusted).

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



***Real (Inflation-Adjusted) Retail Sales.*** Based on September CPI-U reporting, inflation- and seasonally-adjusted September 2012 retail sales rose by 0.58% for the month, where, before inflation-adjustment (nominal basis), the current number was up by 1.15%. August real retail sales were revised to a 0.55% (previously 0.28%) monthly gain, where the nominal monthly gain in August was revised to 1.16% (previously 0.89%). Detail of the September's nominal retail sales reporting can be found in [Commentary No. 475](#), where issues of reporting distortions—inflated current numbers—from the use of unstable concurrent-seasonal-adjustment factors are discussed.

On a seasonally-adjusted basis, annualized quarterly growth in real retail sales was 3.1% for third-quarter 2012, versus an annualized contraction of 1.7% in the second-quarter. To the extent the Bureau of Economic Analysis pays any attention to underlying economic series, the quarterly gain here would be a plus to pending third-quarter GDP reporting.

Corrected for understated inflation (CPI-U) used in deflating the series, however, the inflation-corrected series graphed in the *Opening Comments and Executive Summary* shows flat-to-minus activity in recent quarters, more in line with common experience.

Year-to-year, September 2012 real retail sales rose at an annual pace of 3.30%, versus a revised 3.27% (previously 2.93%) in August. Reporting of annual growth remains at a level that would be on the brink of generating a reliable signal of pending recession, during more-normal economic times.

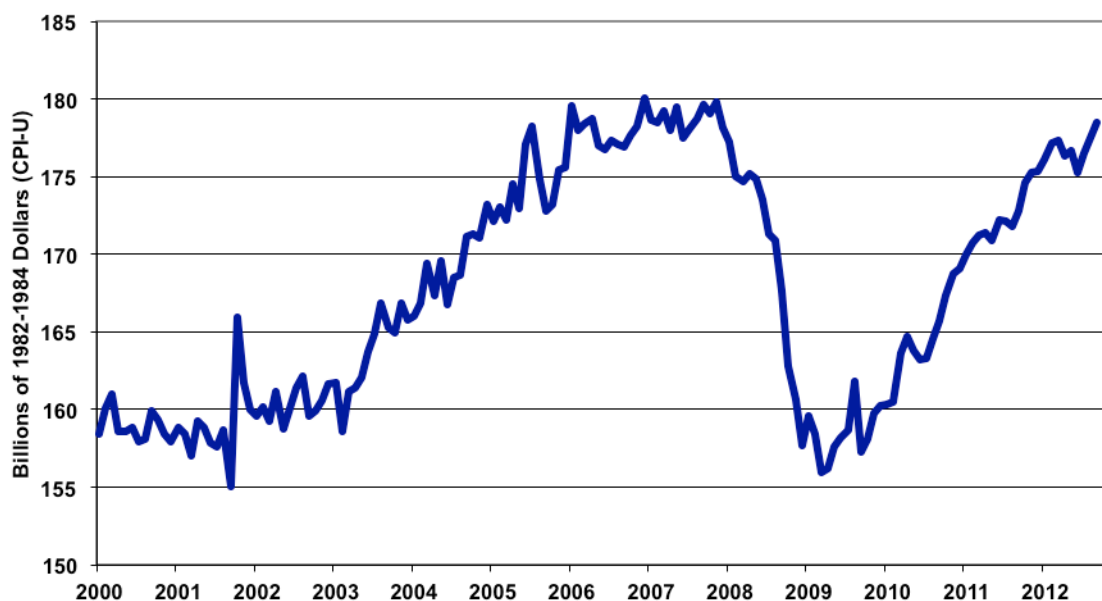
The first graph following shows real retail sales activity (deflated by the CPI-U) since 2000. The second graph shows the same series in full post-World War II detail.

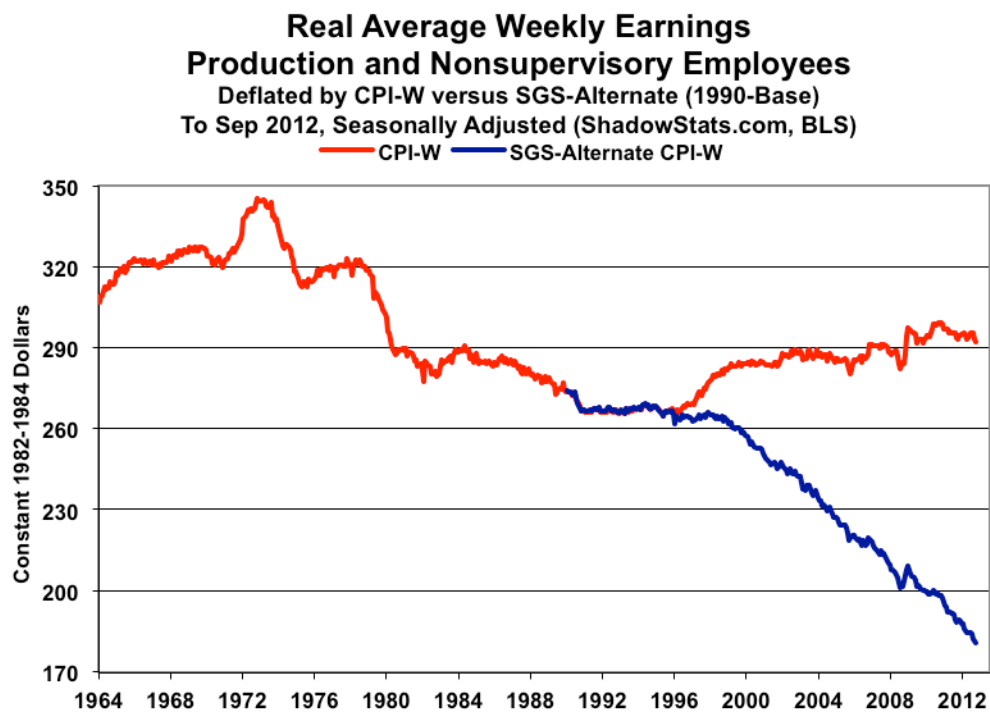
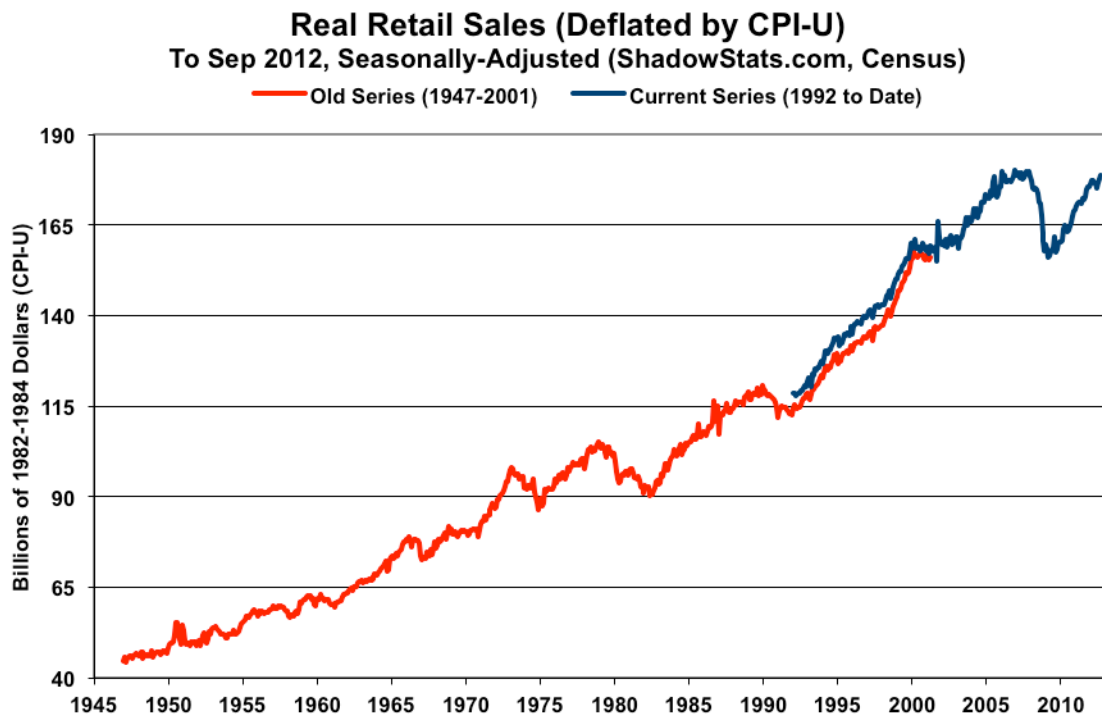
The recent pattern turns increasingly negative in the updated “inflation-corrected” real retail sales graph shown in the *Opening Comments and Executive Summary section*. The inflation-corrected numbers use the SGS-Alternate Inflation Measure (1990-Base) for deflation instead of the CPI-U. As discussed in [Hyperinflation 2012](#) and [Special Commentary No. 445](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating economic growth.

There has been no change in the underlying fundamentals. There is nothing that would support a sustainable turnaround in retail sales, personal consumption or in general economic activity. There is no recovery, just general bottom-bouncing.

As official consumer inflation continues to pick up, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze—as reflected partially by real earnings, discussed in the next section, and again in [Commentary No. 469](#)—these data should continue trending meaningfully lower, in what eventually will become a formal double-dip recession.

**Real Retail Sales (Deflated by CPI-U)**  
To Sep 2012, Seasonally-Adjusted (ShadowStats.com, Census)

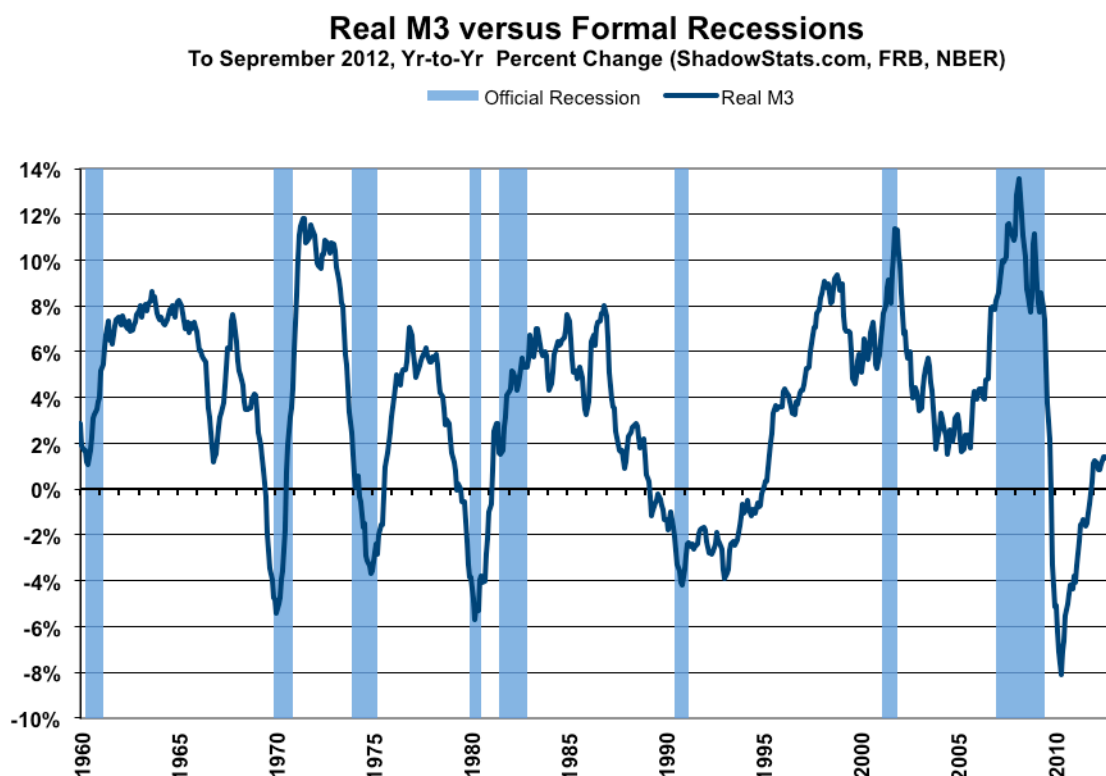




**Real Earnings.** Coincident with today's (October 16th) CPI releases for September 2012, the BLS published real (inflation-adjusted) average weekly earnings for September 2012. The production and nonsupervisory employees series showed that real average weekly earnings (deflated by the CPI-W) were down by 0.4% (up by 0.3% before inflation) for the month, versus an unrevised 0.8% contraction (0.1% contraction before inflation adjustment), for the month of August.

The production and nonsupervisory employees series is the only one published by the BLS that has meaningful historical data. The preceding graph of the series shows earnings deflated by both the CPI-W and the SGS-Alternate Inflation Measure (1990-Base).

**Real Money Supply M3.** The signal for a double-dip or ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), discussed in the in [Hyperinflation 2012](#), remains in place and continues, despite real annual M3 growth having turned to the upside. As shown in the following graph—based on the September 2012 CPI-U report and the latest SGS-Ongoing M3 Estimate—annual inflation-adjusted growth in M3 for September 2012 was 1.3%, versus 1.4% in August, with higher inflation more than offsetting an uptick in nominal (not-adjusted-for-inflation) annual M3 growth.





The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first turns negative in a given cycle; the signal is not dependent on the depth of the downturn or its duration. Breaking into positive territory does not generate a meaningful signal one way or the other for the broad economy. The current downturn signal was generated in December 2009. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of series continued in 2011, with significant new softness in recent reporting. A renewed downturn in official data is becoming more obvious, and that eventually should lead to recognition of a double-dip recession.

## INDEX OF INDUSTRIAL PRODUCTION (September 2012)

**Quarterly Production Fell for First Time Since the Official Recession.** Despite continued large revisions that accounted for half the headline growth reported for September 2012, third-quarter 2012 production was in outright contraction. Historically, that would be a negative signal for next week's initial estimate of third-quarter 2012 GDP, but the GDP of recent years increasingly has shown little relationship to underlying economic series, such as industrial production. Decades ago, industrial production actually was used as the broadest indicator of U.S. economic activity.

September's monthly production gain of 0.4% encompassed a 0.2% increase in manufacturing, a 0.9% increase in mining and a 1.5% increase in output from utilities.

The manufacturing sector was dominated by no growth in production of consumer goods (automotive products were down significantly, again, where an effort at reduction in excess inventories still appears to be underway). Mining activity growth partially reflected the re-opening of oil platforms that had been shut down in the Gulf of Mexico during August, related to Hurricane Isaac.

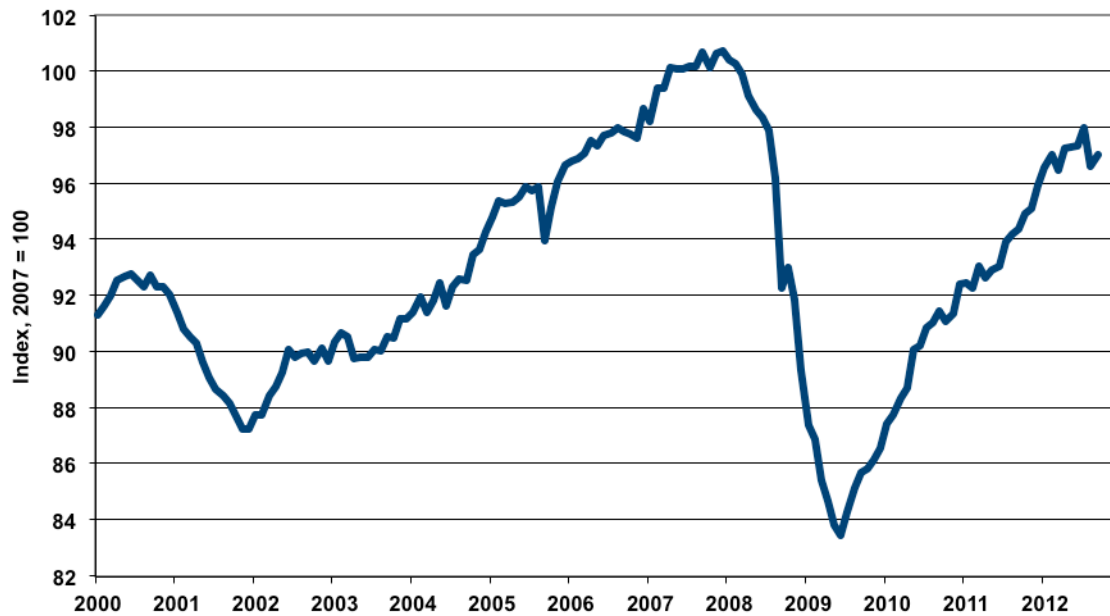
**September 2012 Reporting.** This morning's (October 16th) release by the Federal Reserve Board of seasonally-adjusted September 2012 industrial production showed a headline monthly 0.41% gain (up by 0.22% before prior-period revisions), versus a revised 1.38% (previously 1.16%) monthly decline in August.

On a seasonally-adjusted basis, third-quarter industrial production contracted at an annualized pace of 0.40%, the first quarterly contraction in the series since second-quarter 2009, the official end of the recession. Second-quarter 2012 production had expanded at an annualized pace of 2.56%, versus the first-quarter.

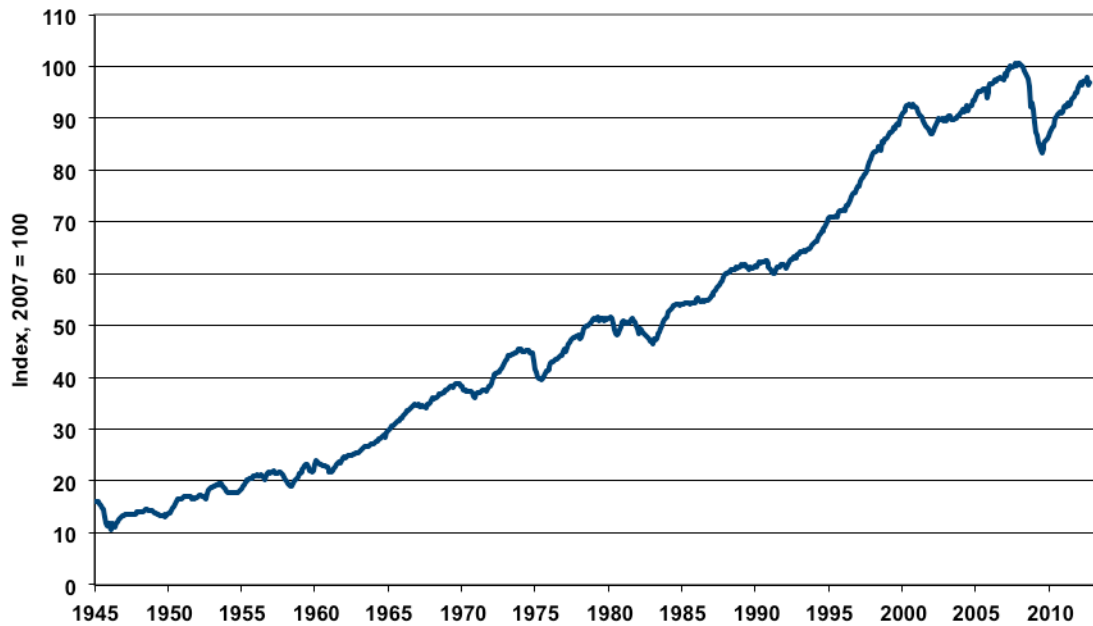
Year-to-year growth for September 2012 production was 2.81%, versus a revised 2.60% (previously 2.80%) in August. That was well off the recent relative peak annual growth of the series at 8.13%, in June 2010. The year-to-year contraction of 15.15% seen in June 2009, at the end of second-quarter 2009, was the steepest annual decline in production growth since the shutdown of war-time production following World War II.

The "recovery" in industrial production is reflected in the following graphs. Both graphs show the monthly level of the production index. The first of these shows recent historical detail for the period beginning in 2000, the second shows the same data in historical context since World War II.

**Index of Industrial Production**  
To Sep 2012, Seasonally-Adjusted (FRB)



**Index of Industrial Production**  
To Sep 2012, Seasonally-Adjusted (FRB)



Corrected for the understatement of inflation used in deflating portions of the industrial production index, the series has shown more of a bottom-bouncing pattern since 2009, and it appears perhaps to have topped out in recent reporting. The inflation-corrected production series is graphed in the *Opening Comments and Executive Summary* section. Please note that index base for the inflation-corrected graphs is January 2000 = 100, instead of the official 2007 = 100 used in the graphs here.

**Week Ahead.** As noted in [Commentary No. 474](#), public speculation as to political manipulation of labor-related data, produced by the Department of Labor, has hit a level of activity that is unprecedented. Whether or not manipulations have taken place with current reporting, supporting evidence either way likely will be forthcoming in the year ahead. Upcoming, initial reporting of third-quarter GDP on October 26th and the October labor report on November 2nd—in the two weeks before the election—would be likely manipulation targets, if the data indeed were being massaged. In any event, numbers that are far removed from common experience will tend to be viewed by the public with extreme skepticism.

Nonetheless, market recognition of an intensifying double-dip recession has taken stronger hold, 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—shy of manipulated data—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.

**Residential Construction (September 2012).** Detail on September housing starts is due for release tomorrow, Wednesday, October 17th, by the Census Bureau. In the wake of a 75% collapse in activity from 2006 through 2008, the ensuing four-year pattern of housing starts stagnation at an historically low level of activity continues, with no fundamental shift likely in the near future, including the just-passed September. As has become the standard circumstance here, any reported monthly gain likely would not be statistically significant.

**New and Existing Home Sales (September 2012).** The September existing home sales release is scheduled for Friday, October 19th, from the National Association of Realtors, while the new home sales report from the Census Bureau is scheduled for Wednesday, October 24th. Entrenched patterns of stagnation likely have continued in both series, and the pending monthly results are not likely to be statistically-significant.

**New Orders for Durable Goods (September 2012).** The initial estimate for September 2012 new orders for durable goods is scheduled for release on Thursday, October 25th, by the Commerce Department. As has been the case for months—except for August's sharp decline in areas other than commercial aircraft

orders—whatever month-to-month change is reported for this regularly volatile series, it likely will not be outside the bounds of normal activity.

In terms of the potential inflation contribution to new orders growth, the seasonally-adjusted, month-to-month change in the September PPI finished goods capital equipment index was a decrease of 0.1%, with year-to-year adjusted inflation at 1.7%. Due to hedonic-quality adjustments to this portion of the PPI series, however, as with the GDP numbers, those inflation data understate inflation reality and correspondingly overstate inflation-adjusted growth.

***Gross Domestic Product—GDP (Third-Quarter 2012, First or “Advance” Estimate).*** The first-estimate of third-quarter 2012 GDP is due for release by the Bureau of Economic Analysis (BEA) on Friday, October 26th. A consensus appears to be developing for stronger growth than the 1.3% annualized, real (inflation-adjusted) headline growth last reported for second-quarter 2012.

Reality is in the direction of much weaker growth, with mixed signals from industrial production (negative), retail sales (positive) and the trade deficit (negative) pressuring quarterly change to below consensus. With the BEA usually trying to target its “advance” growth estimate at the consensus, however, and with some potential of other massaging of numbers the week before the election, any stronger growth that is reported likely will revise to the downside in later months.

In any event, the new numbers likely will not be statistically significant, with the GDP series remaining the most worthless, the most heavily politicized and the most misleading of any major government economic statistical release.

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