

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

COMMENTARY NUMBER 487

November Employment and Unemployment, October Construction, PCE Deflator

December 7, 2012

Nonsense November Jobs and Unemployment Numbers

Serious Revision Issues with Bloated Pre-Election Payroll Numbers

Discouraged Workers Jumped by 20.4% in November

November Unemployment: 7.7% (U.3), 14.4% (U.6), 22.9% (ShadowStats.com)

M3 Annual Growth Slows Anew

PLEASE NOTE: The next regular Commentary is scheduled for Thursday, December 13th, covering November retail sales and PPI, followed by a Commentary on Friday, December 14th, covering November industrial production, CPI and related deflated series.

Best wishes to all — John Williams

Opening Comments and Executive Summary. Economic activity continues to sink anew, while monthly reporting quality continues to be pummeled by unstable concurrent-seasonal-factor adjustments, by downside revisions to prior-period reporting and with temporary distortions and disruptions from Hurricane Sandy. Hit hard by all three factors, the November payroll and unemployment numbers were of particularly questionable quality.

With the lives of roughly 7% to 8% of the U.S. labor force disrupted by Hurricane Sandy, and with significant difficulties continuing well beyond the survey week of November 5th, into subsequent weeks, there is no possibility of the Bureau of Labor Statistics (BLS) having conducted a normal surveying of households in determining the purported November 2012 unemployment rate of 7.7%. I know of many individuals and businesses in the region that were without power, telephone service or their usual physical locations, for up to three weeks or more.

Offering something of a contrary view, the BLS noted in today's (December 7th) news release on employment and unemployment conditions that, "Hurricane Sandy made landfall on the Northeast coast on October 29th, causing severe damage in some states. Nevertheless, our survey response rates in the affected states were within normal ranges. Our analysis suggests that Hurricane Sandy did not substantively impact the national employment and unemployment estimates for November."

The conclusion there is open to question. Beyond the difficulties of the BLS carrying out anything akin to the normal door-to-door or telephone household surveying, or the lack of ability or willingness of heavily damaged businesses to submit payroll data on a timely basis, whatever responses the BLS received and put through its happy assumptions and modeling likely did not include much of a sampling of those who had been through the greatest disruptions.

Standardly, if a reporting company does not submit its payroll data on a timely basis, the BLS assumes that the company remains in business and imputes the data for the non-reporting firm, based on prior reports from the company and on the general trend of employment in the related industry.

In the extreme, the BLS conceivably could report monthly payrolls, without any input from businesses, using its ongoing trend model that had suggested a 126,000 jobs gain for November, which was reasonably close to the headline 146,000 gain. Suggestive of possibly some trend massaging, most of the industry data were pretty close to trend, except for a drop off in construction jobs and an unusual surge in retail clothing store employment. My betting is that reporting in subsequent months will see some realignment of the November payroll data, as harder numbers are booked from the affected areas.

In terms of the unemployment data, however, there will be no revised surveys, so a meaningful number for November simply may not be knowable.

Ongoing Hurricane Issues and Concurrent Seasonal Factors. The reporting complications tied to the hurricane will be reasonably short-lived. November payrolls eventually will revise to a more accurate number. Where renewed economic downturn was underway before Sandy hit, Sandy likely will take the blame for any economic weakness reported in the month ahead. Sandy also will provide some boost to the economy in the rebuilding of damaged structures, and the replacement of lost or damaged goods, in the next quarter or two, but such gains will be fleeting, unless there is a fundamental turnaround in the prospects for consumer liquidity, as discussed in [*Special Commentary \(No. 485\)*](#).

These temporary, storm-related reporting problems are separate from the ongoing inconsistencies and instabilities created by the use of concurrent seasonal factors in seasonally-adjusting both the payroll- and household-survey data. As discussed in the regular *Commentaries* on employment and unemployment (see the *Concurrent Seasonal Factors* section, below), the BLS has moved in recent years to abandon regular seasonal adjustments that once were set only once or twice per year, to "concurrent" adjustments that are revised each month, including a full revision to the underlying historical series.

The big problem is that in the wake of the worst economic downturn since the Great Depression, seasonal factors that are recalculated each month are highly volatile and not stable. Unless the revamped historical data are published along with the most-recent estimate, meaningful period-to-period comparisons cannot be made, since the month-to-month numbers are not consistent.

Where no revisions are published to prior months by the BLS, the unemployment data are not comparable month-to-month. The BLS publishes two months of revisions for the payroll data, but beyond that, the payroll data are not comparable either. These systems enable a variety of undetected boosting or depression of current monthly numbers based on unpublished changes to prior data.

Basically, none of the seasonally-adjusted unemployment data are meaningful when compared month-to-month. Also, seasonally-adjusted, monthly payroll employment gains currently are being boosted in the most-recent months through the unpublished shifting in the seasonal adjustments of earlier data.

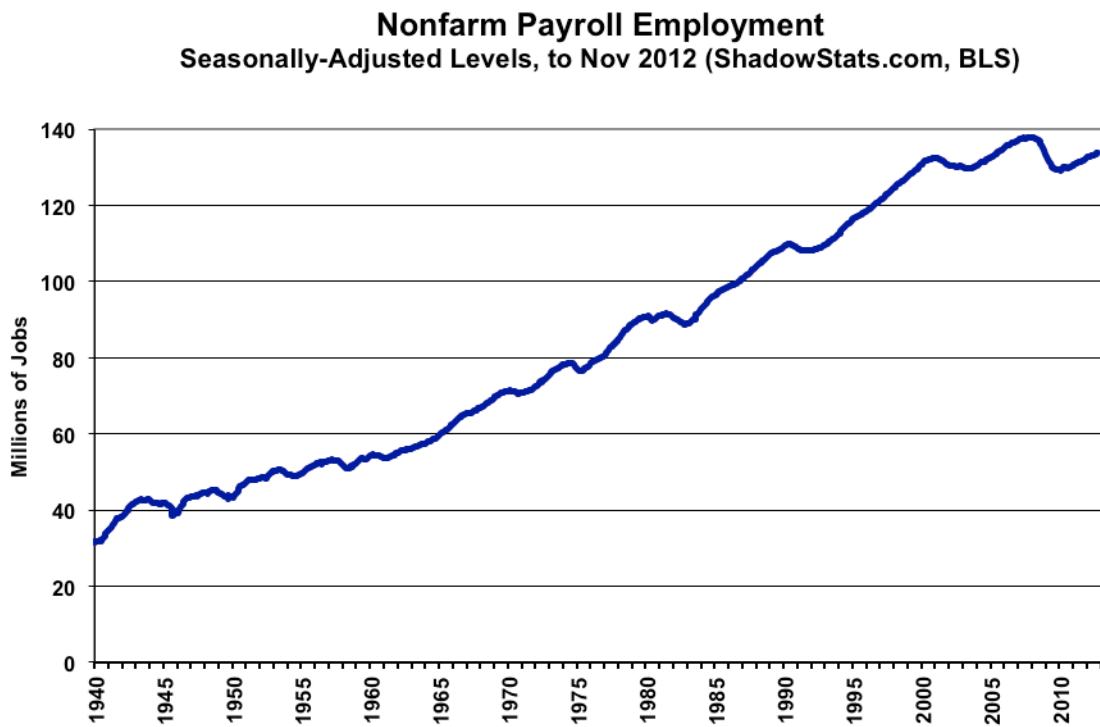
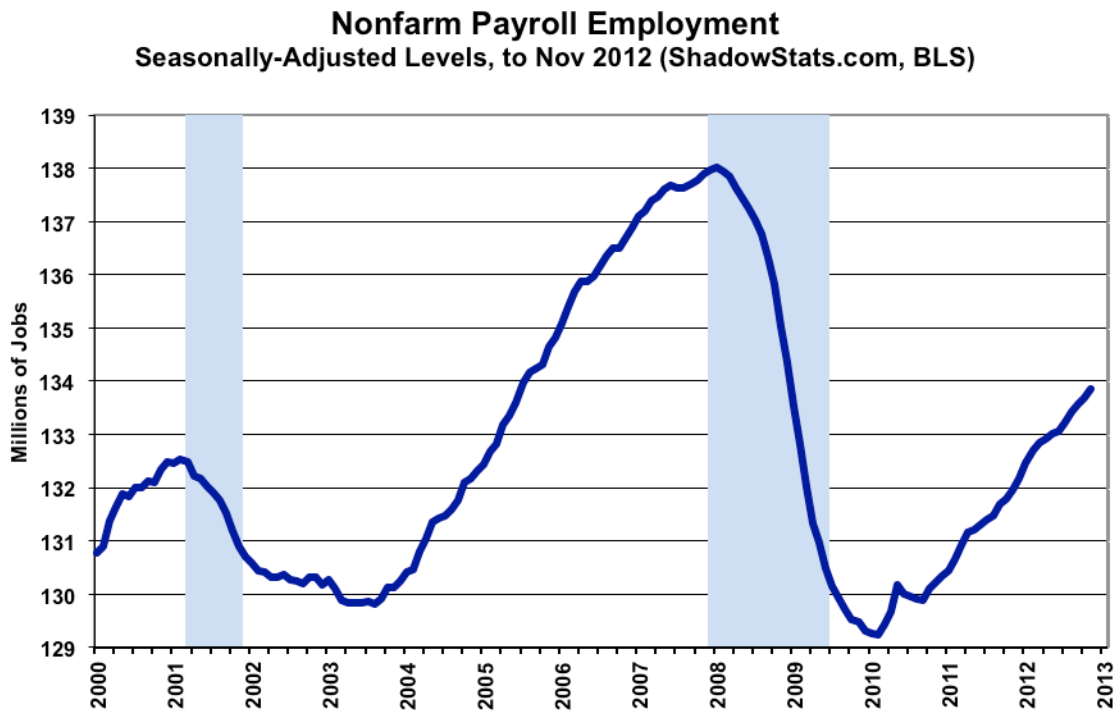
Payrolls and Unemployment. Beyond the surveying and reporting complications discussed here, November payroll employment showed a monthly headline gain of 146,000, but that was after a significant downside revision to October's reporting. Net of prior-period revisions, November's seasonally-adjusted monthly gain was 97,000. October's adjusted gain was revised lower to 138,000, from initial reporting of 171,000, but there was more to that revision.

Along with November's reporting, the not-seasonally-adjusted October payroll level was revised lower by 90,000 jobs (normally, the seasonally-adjusted number would revise in tandem, that was only partially true here). Such a revision is unusually large and would not reflect revised reporting from a company. Instead it most likely reflected a downside adjustment to otherwise overly-optimistic assumptions made by the BLS for its October reporting. The significance here is that the October headline jobs gain of 171,000—the result of those happy assumptions—was the last number put out by the BLS before the presidential election.

The issues with the headline U.3 unemployment rate dropping by 0.2%, from 7.9% to 7.7% (actually down by 0.12% from 7.87% to 7.75%), are (1) the month-to-month numbers simply are not comparable due to concurrent seasonal factor adjustments (see *Household Survey* section), and (2) the November number likely resulted from an unusually poor-quality survey (see *Opening Comments*).

Of some meaning, though, the count of unadjusted “short-term” discouraged workers jumped by 20% in November, with increasingly distressed, unemployed individuals being dropped from the government's headline-unemployment and labor-force numbers. The BLS's broadest U.6 unemployment rate eased to an unadjusted 14.6% in November, from 14.8% in October, with the November ShadowStats (SGS) Alternate Unemployment measure holding at 22.9%.

Following are the usual graphs of nonfarm payrolls with the first graph showing seasonally-adjusted payroll levels (indexed to January 2000 = 100), reflecting detail of the current employment level well below its pre-2007 recession peak. There has been no full recovery as reported in the GDP. 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.



Other Reporting—Construction, PCE Deflator. October 2012 construction spending rose month-to-month by a statistically insignificant 1.4%. Despite continuing upside revisions to prior-period reporting, the series continued to show an ongoing low level of stagnation. Some weakness in November construction employment suggests somewhat weaker construction spending in November. Although some pick-up in activity from reconstruction tied to Hurricane Sandy is likely in the next quarter or two.

Year-to-year inflation in the October PCE deflator rose to 1.7% from a revised 1.6% (previously 1.7%) in September, generally moving in tandem with the consumer inflation measures published by the BLS. PCE inflation held below the 2.0% target of the Federal Reserve for the seventh-straight month.

[More complete details on November employment and unemployment, and the details on October construction spending and the PCE deflator are found in the Reporting Detail section.]

HYPERINFLATION WATCH

November Broad Money Growth Slowed. Based on roughly three weeks of reported data, the preliminary estimate of annual growth in the SGS or ShadowStats Ongoing-M3 Estimate for November 2012—to be published tomorrow (December 8th) in the [Alternate Data](#) section—is on track to slow to 3.5% from an upwardly revised 3.6% (previously 3.5%) in October. As usual, revisions to prior months in this or the following numbers are due primarily to Federal Reserve revisions to underlying data. Recent annual M3 growth peaked at 4.1% in February 2012, faltered, dropping back to 2.5% in May, then rose to 3.6% in October, and now is notching lower, once again. Such a pattern of slowing growth—in an environment of massive Federal Reserve accommodation—still remains suggestive of an uncontained systemic-solvency crisis.

The seasonally-adjusted, month-to-month gain estimated for November 2012 money supply M3 likely will be around 0.1%, versus a revised 0.3% (previously a 0.5% gain) in October. The estimated month-to-month M3 changes, however, remain less reliable than the estimates of annual growth.

For November 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 November is on track to show year-to-year growth of about 7.2%, versus a revised 7.3% (previously 6.8%) annual gain in October, with month-to-month growth estimated at roughly 0.4% in November, versus a revised 0.9% (previously 0.8%) in October. The early estimate of M1 for November shows year-to-year growth of roughly 10.8%, versus a revised 13.1% (previously 12.2%) in October, with month-to-month change a likely contraction of 1.3% in November, versus a 1.5% (previously 1.3%) gain in October. The variability in year-to-year growth rates still reflects sharp monthly gains a year ago in M1 and M2 that resulted from a shifting of funds out of the aggregate M3 number into M1 and M2 component accounts.

Hyperinflation Update. The [Special Commentary \(No. 485\)](#), published on November 27th, updated [Hyperinflation 2012](#) and the broad outlooks on the economy and inflation, as well as systemic stability and the U.S. dollar. None of the economic releases of the past two weeks, and certainly no advertised negotiating activity by Washington politicians, have altered those outlooks. If anything, except for the standard nonsense in GDP reporting, the latest data and revisions show an increasingly negative, not positive, outlook for business activity. For new subscribers, as well as for those who otherwise are not

familiar with hyperinflation report or recent the special commentary, linked above, those documents are suggested as background reading on the financial turmoil and currency upheaval facing the United States in the next year or two.

REPORTING DETAIL

EMPLOYMENT AND UNEMPLOYMENT (October 2012)

Severe and Deliberate Disruptions to Unemployment and Employment Reporting Accuracy Continued in November, on Top of Hurricane Distortions. As discussed in the *Opening Comments and Executive Summary*, changes in the November headline unemployment data versus October, and monthly changes in reported nonfarm payrolls, have been warped by the concurrent-seasonal-factor adjustment policies of the Bureau of Labor Statistics (BLS). Combined with simplifying assumptions by the BLS that appear to have bypassed, at least temporarily, systemic distortions from the worst storm ever to hit the East Coast, November's concurrently-adjusted headline employment and unemployment numbers are not meaningful.

To the extent that there is any significance in the monthly reporting, it is that the economy is not in recovery, and that unemployment—as viewed by common experience (the SGS Alternate Measure)—remains at a level that rivals any other downturn of the post-Great Depression era.

PAYROLL SURVEY DETAIL. The BLS reported today (December 7th) a seasonally-adjusted November 2012 month-to-month headline payroll employment gain of 146,000 (a gain of just 97,000 before downside revisions to pre-election reporting). Where the standard 95% confidence interval on monthly headline payroll employment reporting is +/- 129,000, the current numbers appear to be so far out of balance as to be absolutely meaningless here. Beyond concurrent-seasonal-factor distortions (discussed below), the latest survey results likely are a function of modeling fantasies built into the BLS estimates of activity by non-reporting companies. Further, the magnitude of prior-period revisions was great enough to raise the question of phony data (euphemistically: overly optimistic assumptions) being plugged into pre-election reporting, as discussed in the *Opening Comments and Executive Summary*.

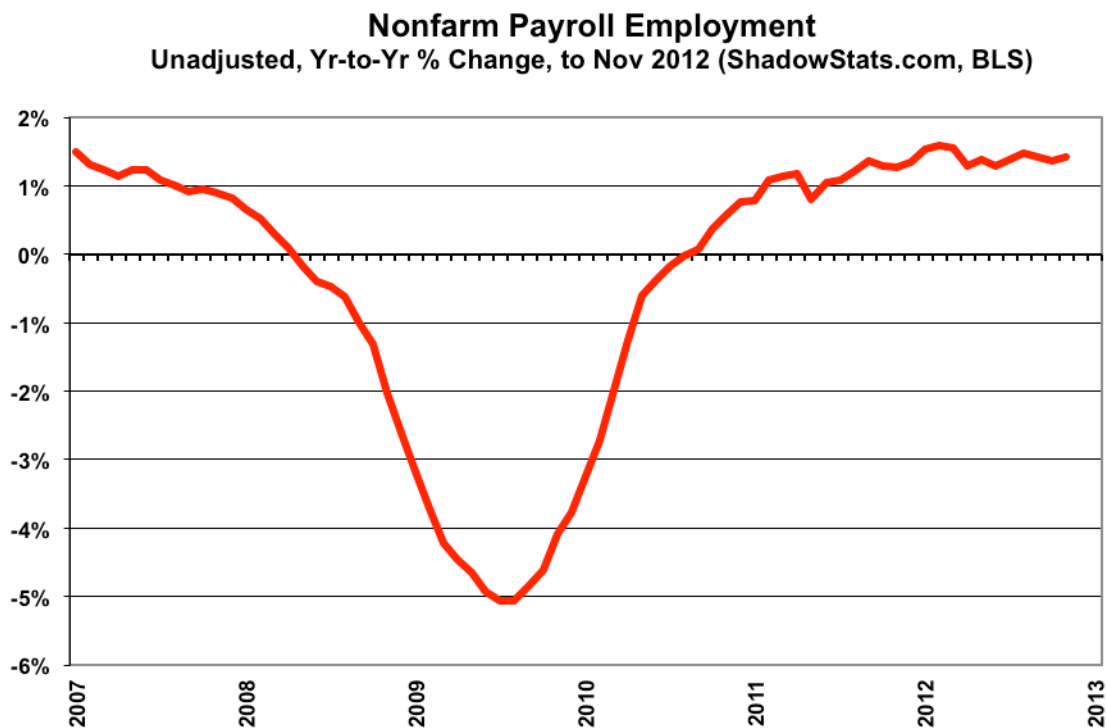
The adjusted October month-to-month increase was revised to 138,000 (previously 171,000), while the September month-to-month change was revised to a 132,000 (previously a 148,000, initially a 114,000) gain. If, however, the September change were counted on a consistent basis, with the latest concurrent-seasonal-factor calculations, the revised September gain actually was 143,000.

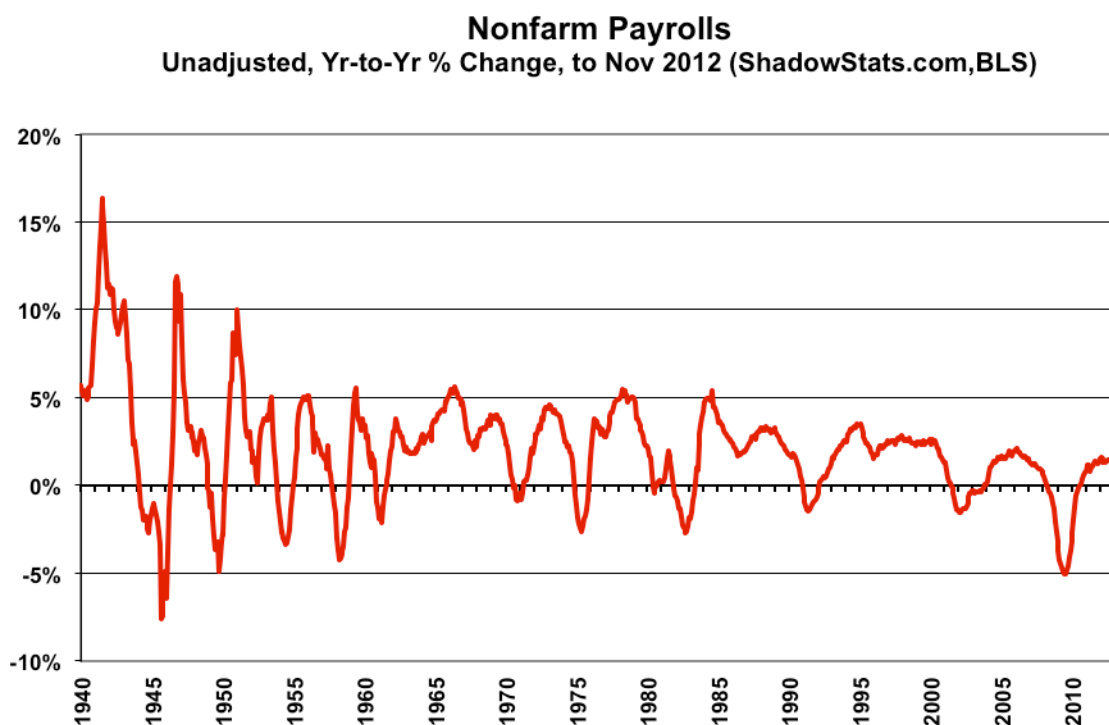
As discussed in the *Opening Comments and Executive Summary* the inconsistent use of concurrent-seasonal-adjustment factors had had the effect of pushing relative payroll gains into the pre-election reporting period, and now it is shifting monthly growth into the most-recent reporting. The BLS publishes two prior months of consistent data with concurrent-seasonally-adjusted payrolls, but no prior months of consistent data with the unemployment rate.

Trend Model. As described generally in [Payroll Trends](#), the trend indication from the BLS seasonal-adjustment model is for a 140,000 monthly payroll gain in December 2012, based on today's reporting. While the trend indication often misses actual reporting (the indication for November was a 126,000 monthly gain versus the official 146,000 headline gain), it usually becomes the basis for the consensus outlook.

In terms of year-to-year change, the not-seasonally-adjusted growth in November 2012 payrolls was 1.42%, while October annual growth revised sharply lower to 1.38% (initially a 1.45% estimate, with September growth revising to 1.43% (previously 1.44%, initially 1.38%).

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.





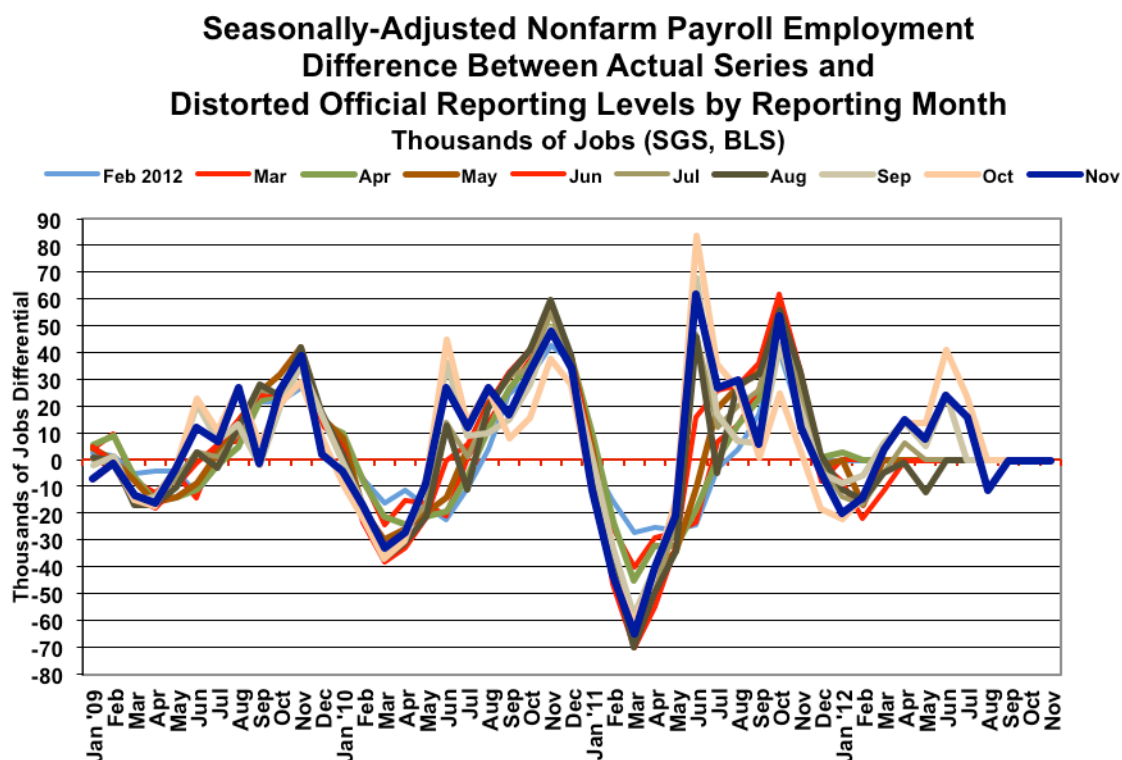
As shown in the longer-term graph (historical detail back to 1940), with the bottom-bouncing of recent years, current annual growth has recovered from the post-World War II record 5.06% decline in August 2009, which remains the most severe annual contraction seen since the production shutdown at the 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 seen in October and shifting into November reporting.

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 (September and October 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 a similar seasonal-adjustment approach, as discussed in the *Opening Comments and Executive Summary*, and in [Commentary No. 473](#), [Commentary No. 461](#), [Commentary No. 451](#) and [Commentary No.](#)

[453](#).) As a result, the reported September-through-November 2012 seasonally-adjusted payroll data are not consistent with earlier published reporting. Conceivably, the shifting and unstable seasonal adjustments could move 90,000 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 again in November's 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. Ten 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 90,000 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. This is separate from the surveying issues evident in the November 2012 reporting. 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 recently-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.

November 2012 Bias. The not-seasonally-adjusted November 2012 bias was a negative 29,000, versus a positive 90,000 in October 2012, and versus a current estimation of a negative 30,000 bias in November 2011. The aggregate upside bias for the twelve months ended November 2012 was 538,000, versus 537,000 in October. At present, that is a monthly average of roughly 45,000 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 (or has been devastated by a hurricane), 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 45,000 jobs per month in the current year, but the actual overstatement of monthly jobs likely exceeds that number by a significant amount. Nonetheless, the BLS published its preliminary estimate for the 2012 benchmark revision September 27th, indicating an upside revision to not-seasonally-adjusted March 2012 payrolls of 386,000, or roughly 32,000 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 the political establishment. As a separate issue, there is no chance that the November household accurately reflected conditions in the New York City metropolitan area, during the week following Hurricane Sandy (see *Opening Comments*).

The 0.2-percentage-point decline reported in the November headline unemployment rate could have been that, by extreme coincidence, but the official headline number just as easily could have increased, or have been unchanged, month-to-month. Due to the survey-quality issues in November, however, a meaningful number now likely is unknowable.

The official actual (not necessarily accurate) numbers could be revealed by the BLS, if it chose to do so. There is no way to tell what the actual numbers are, given current BLS reporting policies; the BLS calculates but does not report consistent data, as part of its standard monthly-estimation process. Nonetheless, the annual publication of revisions to the seasonally-adjusted data are due with the next month's labor reporting. At that time, the historical data will be consistent for the only time during the year. What the actual, comparable unemployment rates were when the controversially-large month-to-month decline in the unemployment rate was reported in September 2012, however, never will be known. That is because the August and September revised detail available next month will follow three prior unstable and unpublished monthly revisions, since the initial inconsistent reporting of early October 2012.

With that as background, following are the inconsistent 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 to post-election pontifications in the nation's capital. Separately, though, the not-seasonally-adjusted numbers generally are consistent in their preparation.

Headline Household Employment. Based on the November 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), November 2012 employment dropped month-to-month by 122,000, after October and September employment soared by incredible (as in unbelievable) respective monthly gains of

of 410,000 and 873,000. As just discussed above, though, the seasonally-adjusted monthly change here is without significance, due to the underlying data not being comparable on a month-to-month basis.

Unemployment Rates. The reported November 2012 seasonally-adjusted headline (U.3) unemployment rate of 7.75% (rounds to 7.7%, just 6,000 jobs out of 12,029,000 shy of rounding up to 7.8%) was down by 0.12 percentage point (rounds to 0.2%) month-to-month, from the 7.87% (7.9%) October unemployment rate. The November and October unemployment rates were estimated separately and inconsistently. The official +/- 0.23 percentage-point 95% confidence interval for the monthly headline number is meaningless in the context of comparative month-to-month reporting. On an unadjusted basis, November's U-3 unemployment rate was 7.4 %, versus October's 7.5%, and September's 7.6%.

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). Reflecting a seasonally-adjusted reduction in individuals working part-time for economic reasons (the number increased month-to-month on an unadjusted basis), as well as a surge in short-term discouraged workers, the November U.6 unemployment rate declined to a seasonally-adjusted 14.4%, versus 14.6% in October and 14.7% in September. The unadjusted November U.6 rate held at 13.9%, same as in October, and versus 14.2% in September.

Discouraged Workers. The count of short-term discouraged workers (never seasonally-adjusted) rose by 20.4% in the month to 979,000 for November, versus 813,000 in October and 802,000 in September. Keep in mind, though, that the published monthly November number also is net of those who rolled out of "short-term" into the not-officially-counted "long-term" discouraged-worker category.

The current official number reflects the flow of the unemployed, or the balance of the headline unemployed—increasingly giving up looking for work—leaving the headline 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 ShadowStats or SGS-Alternate Unemployment Measure.

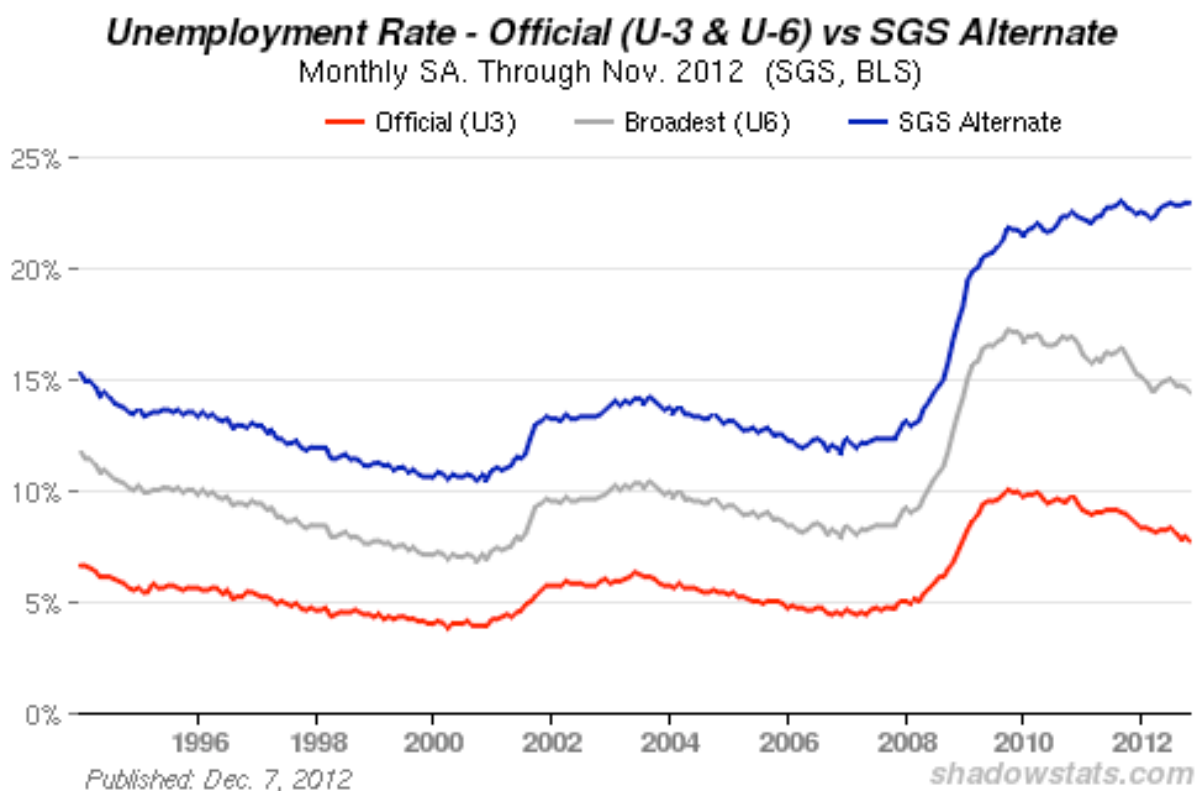
In 1994, during the Clinton Administration, "discouraged workers"—those who had given up looking for a job because there were no jobs to be had—were redefined so as to be counted only if they had been "discouraged" for less than a year. This time qualification defined away the long-term discouraged workers. The remaining short-term discouraged workers (discouraged 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 22.9% in November, the same as in October, and was up from 22.8% in September, reflecting the toll of an increasing number of unemployed leaving the headline labor force. 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 often 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, even as 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 (a ShadowStats.com measure), at what has been an accelerating pace. The aggregate November data show an increasing rate of individuals dropping out of the headline (U.3) labor force. See the [Alternate Data](#) tab for more detail.

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



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 (October 2012)

October Construction Spending Continued in Stagnation, Despite Another Incremental Upside Prior-Month Revision. In four of the last five months, the headline growth rate in construction spending has been against a prior-month's level that was revised higher by 1.0% +/- 0.1%, suggestive of a recent downside reporting bias in the monthly series.

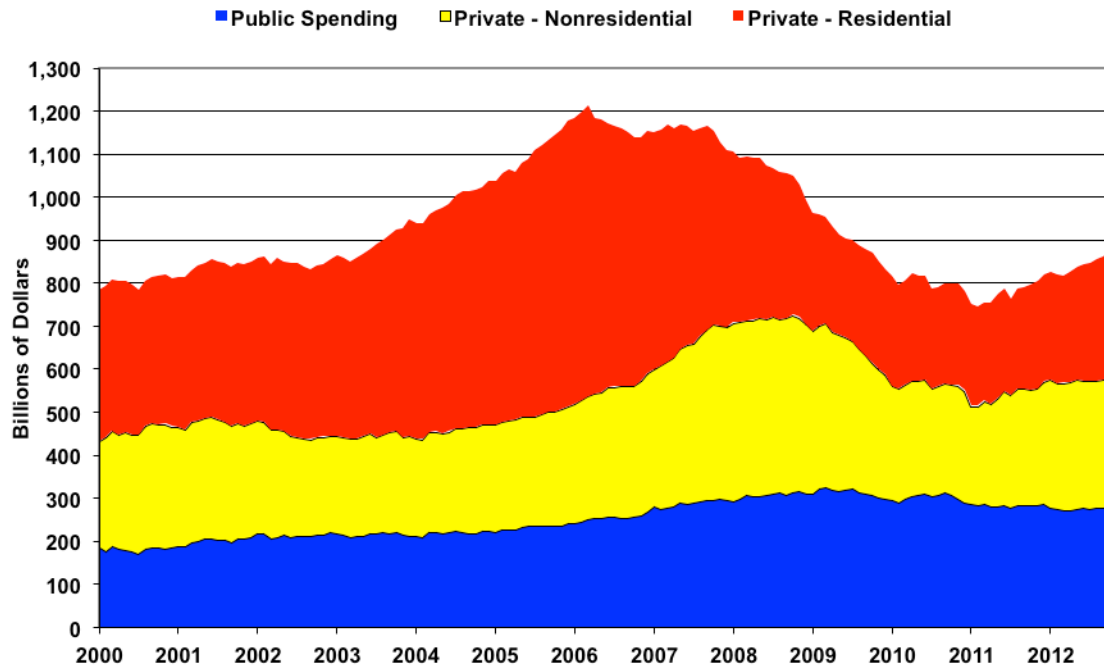
That said, the trend of stagnation in construction spending, at low levels of activity, continued in the latest survey, particularly after likely inflation adjustment. The October numbers reflected little if any impact from the disruptions and destruction of Hurricane Sandy, with the headline month-to-month gain in activity statistically insignificant. Mixed “superstorm” impact, however, is likely for the upcoming November data, with some temporary upside effects likely for the next quarter or so following.

The Census Bureau reported December 3rd that the total value of construction put in place in the United States during October 2012 was \$872.1 billion, on a seasonally-adjusted—but not inflation-adjusted—annual-rate basis. That estimate was up for the month by a statistically-insignificant 1.4% +/- 2.3% (all confidence intervals are at a 95% level), from an upwardly revised \$860.4 (previously \$851.6) billion in September. Before prior-period revisions, the October level actually was up by 2.4% from initial September reporting. The monthly gain in September versus August activity revised to 0.5%, from an initial estimate of a 0.6% monthly gain.

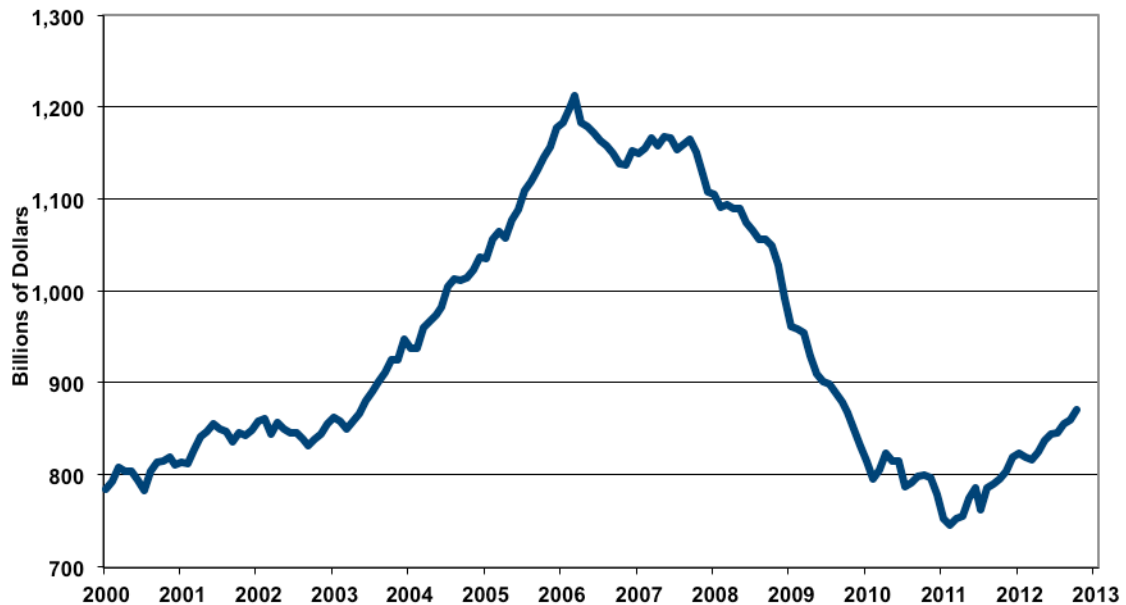
Although aggregate October construction spending was up year-to-year by a statistically-significant 9.6% +/- 2.7%, the gain likely was more than covered by increases in actual construction costs. The Bureau of Economic Analysis (BEA) continued to underestimate year-to-year inflation in “structures” at 2.9% in its first revision to third-quarter GDP 2012. Year-to-year, September 2012 construction growth was revised higher to 8.9% (previously 7.8%).

The statistically-insignificant 1.4% gain in monthly October construction spending included a 0.8% gain public construction spending, which had revised to a 0.1% (previously 0.8%) monthly contraction in September. October private construction rose by 1.6% in the month, versus a revised 0.8% (previously 1.3%) monthly gain in September. The accompanying graphs show the 1.6% monthly gain in October total construction, with private residential construction up by 3.0%, private nonresidential construction up by 0.3% and public construction up by 0.8% for the month.

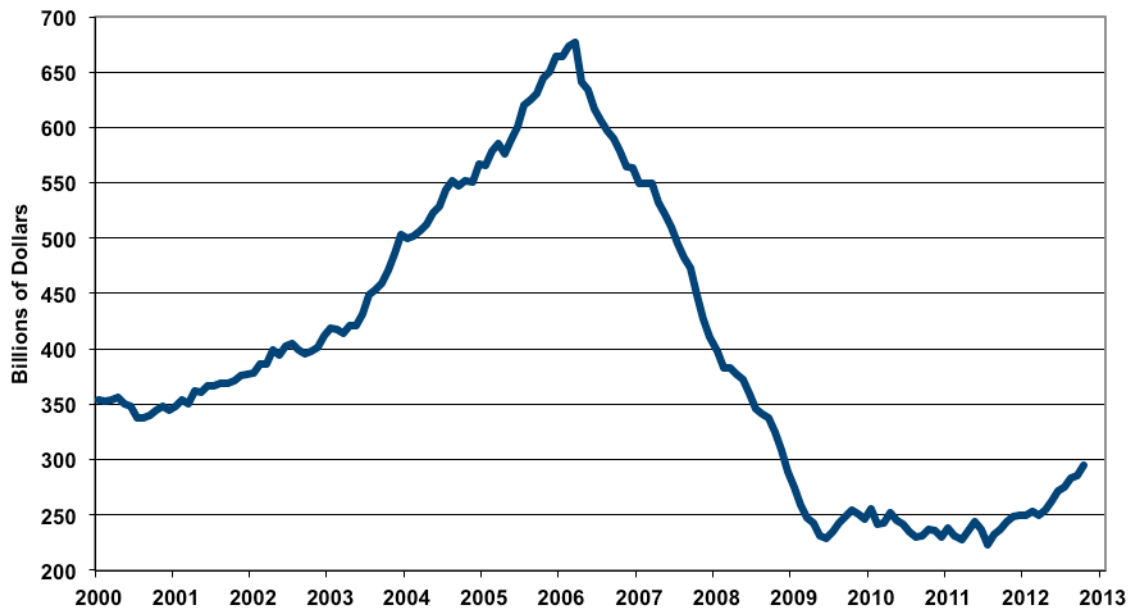
Construction Spending, Monthly to Oct 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



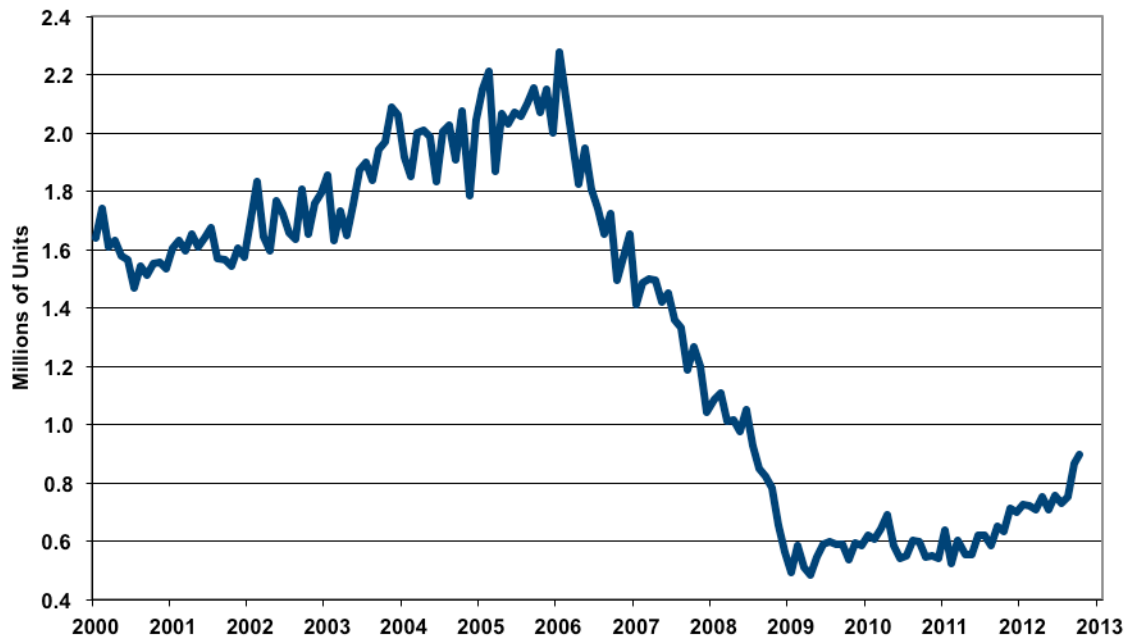
Total Construction Spending, Monthly to Oct 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



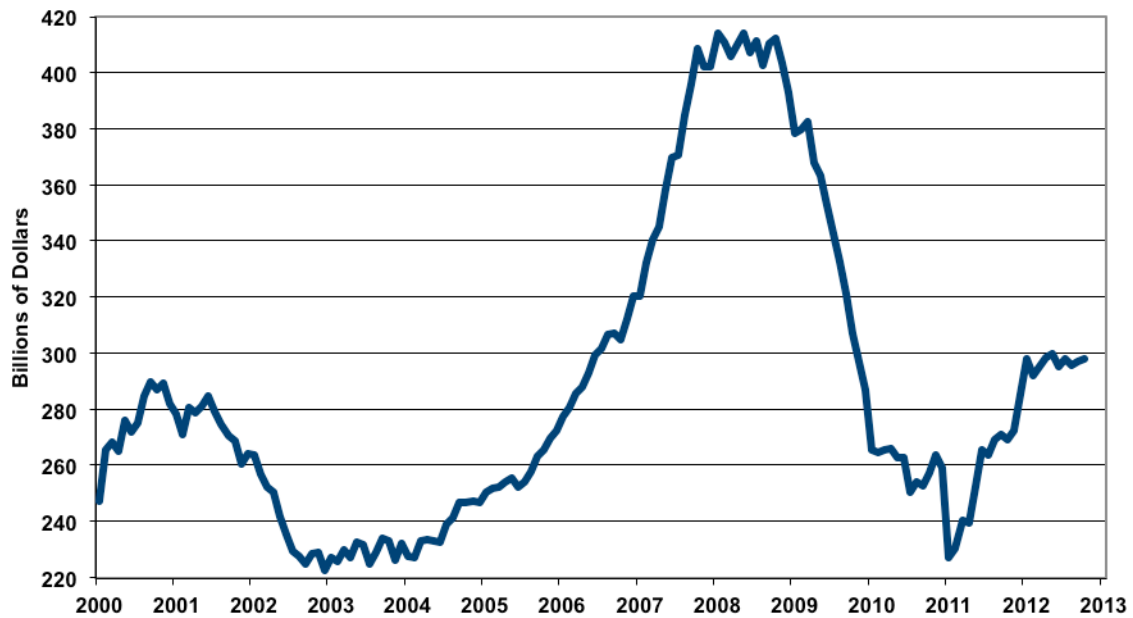
Private Residential Construction to Oct 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



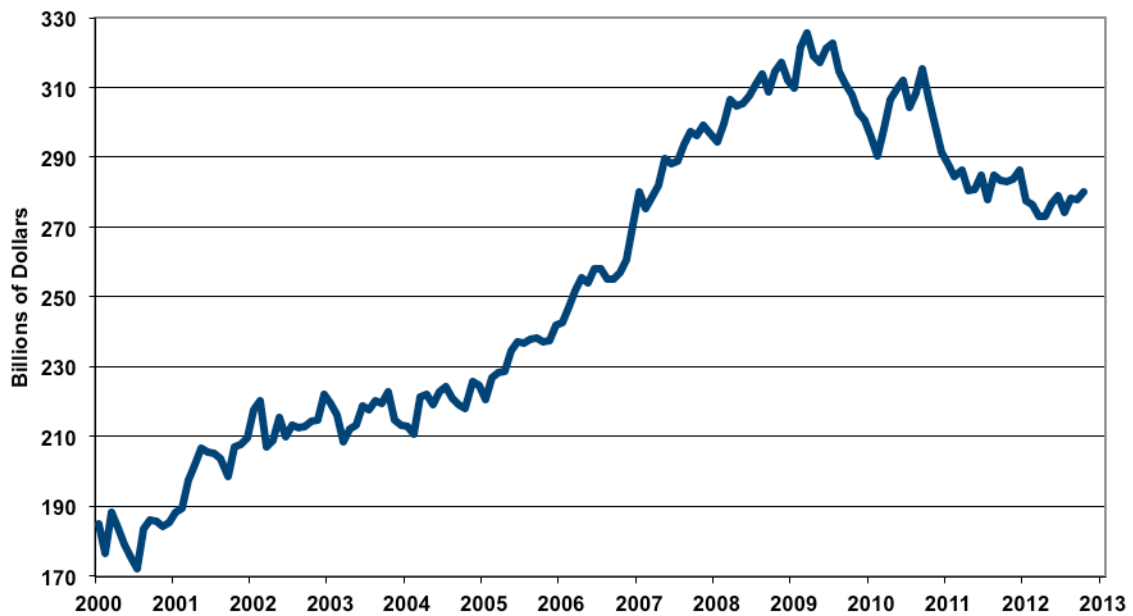
Housing Starts (Annual Rate by Month)
2000 to Oct 2012, Seasonally-Adjusted (ShadowStats.com, Census)



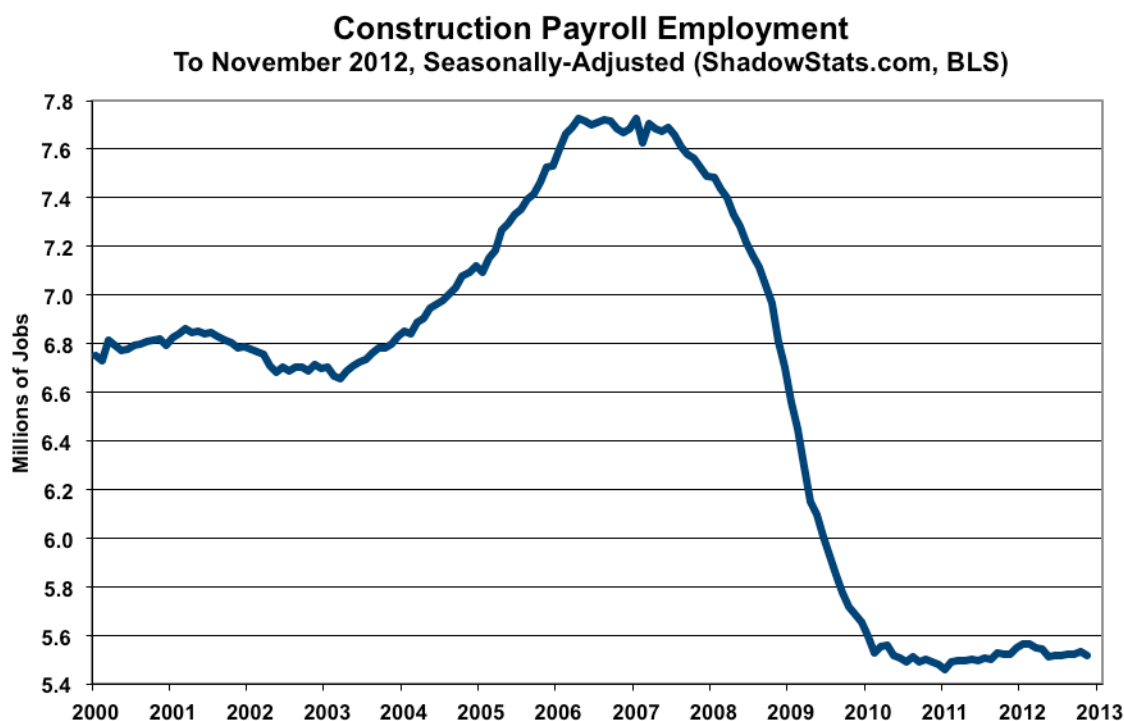
Private Nonresidential Construction to Oct 2012
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



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



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



As shown in the graph above, consistent with deteriorating stagnation in construction activity, and suggestive of some downside construction spending numbers in November 2012, the seasonally-adjusted November construction-employment level was reported at 5.514 million, down by 0.4% or 20,000 jobs from the downwardly revised 5.534 (previously 5.539) million reading in October, per the November payroll survey, as published by the Bureau of Labor Statistics. Not seasonally adjusted, November 2012 construction payrolls turned negative year-to-year (down 0.1%) for the first time this year (first time since August 2011).

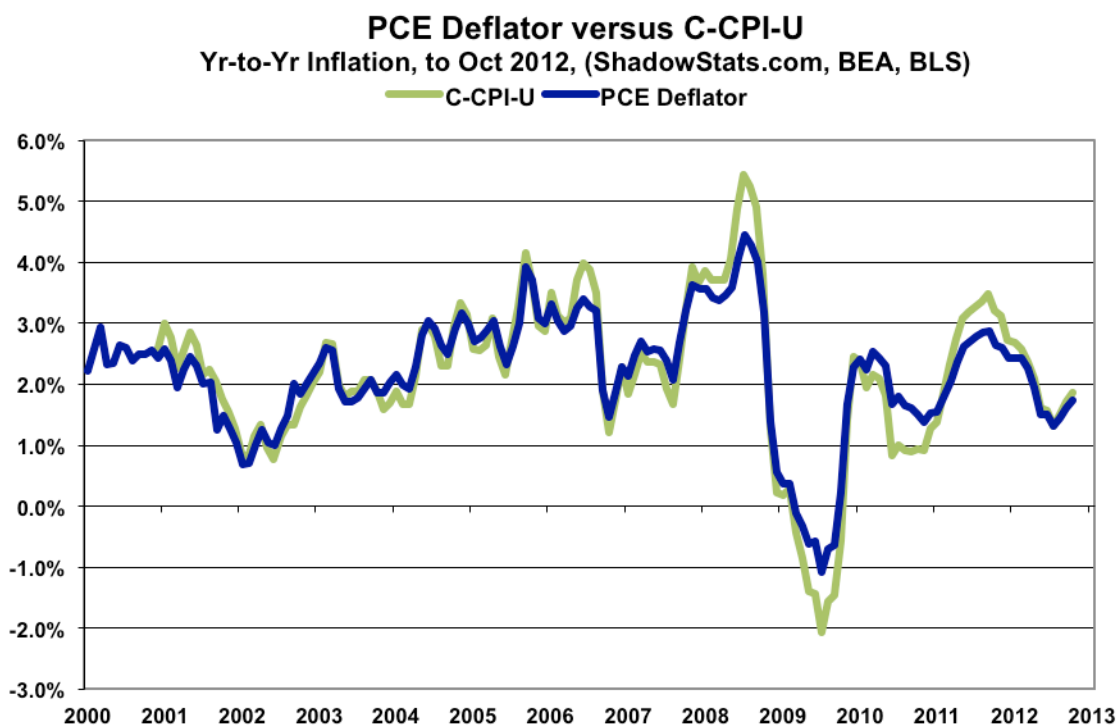
PERSONAL CONSUMPTION EXPENDITURE (PCE) DEFLATOR (October 2012)

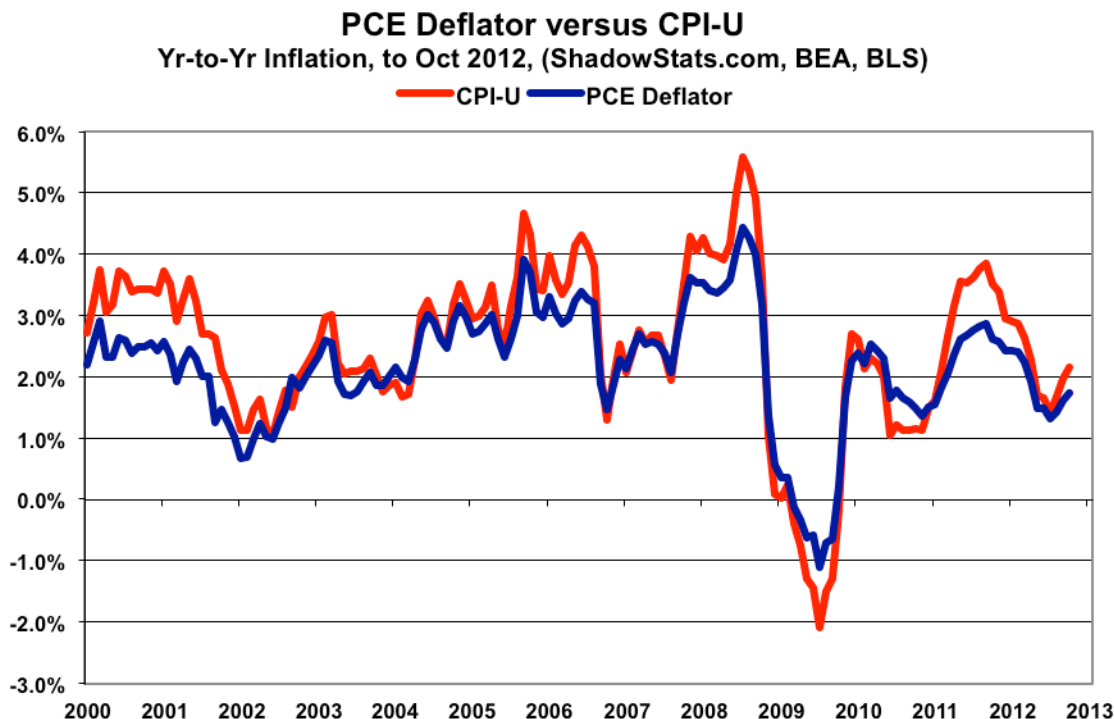
October PCE Deflator Rose 0.1% Month-to-Month, 1.7% Year-to-Year. Published on November 30th by the Bureau of Economic Analysis (BEA), the regularly-unstable implicit pricing residual,

published as the seasonally-adjusted October PCE deflator, was up for the month by 0.13% (up by 0.02% before prior-period revisions), versus a revised 0.33% (previously 0.38%) monthly gain in September.

Year-to-year, the PCE-deflator strengthened to 1.74% in October, versus a revised 1.61% (previously 1.71%) in September 2012. Annual PCE inflation held below the Fed's 2.0% target for the seventh straight month. Nonetheless, the differential is narrowing, and below-target PCE inflation reporting should not survive as a protracted pattern here. The PCE deflator tends to follow the general direction of the CPI annual inflation rates, which are likely to show renewed increases in December, following a flat-to-minus showing in November.

PCE Deflator versus Other Inflation Measures. Where, in theory, the PCE deflator measure should be virtually identical to the fully substitution-based chain-weighted-CPI (C-CPI-U) (see [Commentary No. 482](#) for details of the latest C-CPI-U and other inflation measures), it actually moved in tandem with, and had held at the same level as the C-CPI-U in the three months of reporting through September. In October, however, the C-CPI-U pulled ahead, once again, in terms of annual inflation. In contrast, despite all the methodological manipulation aimed at making the CPI-U a fully-substitution based index, that process is not complete, and headline CPI-U annual inflation generally remains stronger than the PCE deflator and C-CPI-U measures, as it did in October. Those series are shown in the accompanying graphs; see the [Public Comment on Inflation](#) for further detail on the methodological machinations.





The October 2012 PCE deflator showed 1.7% year-to-year inflation, versus a revised 1.6% in September. That compared with annual inflation in the October C-CPI-U at 1.9%, versus 1.7% in September; October CPI-U at 2.2%, versus 2.0% in September; October CPI-W at 2.2%, versus 2.0% in September; and the October SGS-Alternate (1980-Base) at 9.8%, versus 9.6% in September.

This “inflation targeting” effort by the Federal Reserve remains 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.

Revised Third-Quarter PCE Deflator. As noted in [Commentary No. 486](#), year-to-year change in the third-quarter personal consumption expenditures (PCE) deflator was revised to 1.45% (previously 1.50%), versus 1.64% in the second-quarter, and 2.36% in the first-quarter. For comparison purposes, year-to-year CPI-U inflation was 1.70% in third-quarter 2012, versus 1.89% in the second-quarter, and 2.82% in the first-quarter.

This PCE-deflator number, which is being used by the Fed as an “inflation target,” otherwise is gamed by the BEA to reduce GDP inflation, artificially, with the result of overstating inflation-adjusted GDP growth. Overstated economic activity and understated inflation numbers are happy news for both the federal government and for the Federal Reserve.

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, in addition to the political massaging—generally tends to yield the lowest annual consumer inflation rate of any major series. Unlike the more widely followed CPI-U and CPI-W measures, which never are revised, as published on a seasonally unadjusted-basis, the PCE deflator is heavily revised, forever, following initial reporting, and it is available only on a massaged, seasonally-adjusted basis.

Week Ahead. Business activity reflected in November reporting should tend to reflect more-negative distortions than did October, in the wake of the damage and business disruptions from Hurricane Sandy. Some of that impact should turn temporarily positive by December, with rebuilding of facilities and replacement of goods damaged or destroyed in the unusually severe late-October tempest.

Otherwise, in terms of general economic activity, until such time as financial-market expectations catch up fully with underlying reality, or underlying reality catches up with the markets, reporting generally should continue to show higher-than-expected inflation and indicate 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, as seen recently, for example, in the reporting of October retail sales, industrial production, housing starts, new- and existing-home sales, new orders for durable goods, and November payroll employment.

Significant reporting-quality problems continue with most widely followed series. Headline reporting issues are tied largely to systemic distortions of seasonal adjustments, distortions that have been induced by the still-ongoing economic turmoil of the last five years. The recent economic collapse has been without precedent in the post-World War II era of modern economic reporting. These distortions have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series. In any event, where numbers are too far removed from common experience, they tend to be viewed by the public with extreme skepticism.

Still, recognition of an intensifying double-dip recession continues to gain, while recognition of a mounting inflation threat has been rekindled a bit by recent Fed monetary policies and rising headline inflation numbers. The political system would like to see the issues disappear; 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.

U.S. Trade Balance (October 2012). The October 2012 trade deficit detail will be released on Tuesday, December 11th. While the U.S. trade deficit continues in fundamental deterioration, the October and next month's November numbers may be impacted by disruptions from Hurricane Sandy. Not only the flow of goods may have been affected, but also the flow of paperwork, particular through the Port of New York. Where imports usually exceed exports, any reported reductions in activity would tend to hit imports harder, resulting in a temporary narrowing of the monthly trade deficit. Goods and reporting flows should be back to normal by December's reporting. Accordingly, there could be a misleadingly "positive" report

in October (meaning a narrowing of the monthly deficit), with close to full catch-up and a more-negative (widening deficit) by December.

Retail Sales (November 2012). Scheduled for release on Thursday, December 13th, by the Census Bureau, the headline November 2012 retail sales number should be an outright contraction. Weakening consumption already was in play before Hurricane Sandy, and the storm likely had some residual negative impact in November.

The reporting here, as with industrial production, may be particularly skewed or volatile depending on how the Census Bureau has worked the numbers. Despite what appear to be positive market expectations for the headline number, a contraction—both before and after adjustment for inflation—is likely. Also a fair bet is that any weakness will be attributed to Sandy, not to the renewed decline in consumer activity that was underway before the storm. Depending, however, on how quickly recovering consumers begin to replace lost items, retail sales impact in November actually could be something of a positive for sales.

As with the production numbers, the revisions to earlier, pre-storm reporting will be of particular interest.

Producer Price Index—PPI (November 2012). The November 2012 PPI is scheduled for release on Thursday, December 13th, by the Bureau of Labor Statistics (BLS). The headline November PPI likely will be in contraction for a second month.

Depending on the oil contract followed, oil prices were down month-to-month in November by two-to-three percent, on average. That drop in energy prices should be offset partially, if not largely, by supportive seasonal adjustments in the month. Higher food prices in combination with still relatively strong “core” inflation should help to generate a less-negative-than-expected headline inflation number. A surprise positive headline number for wholesale inflation even is an outside shot.

Consumer Price Index—CPI (November 2012). The release by the Bureau of Labor Statistics (BLS) of the November 2012 CPI numbers is scheduled for Friday, December 14th. Headline CPI inflation rate is due for a contraction on a monthly basis, and for some slowdown on an annual basis. Seasonally-unadjusted monthly-average gasoline prices declined by 7.6% in November, per the Department of Energy, and that monthly decline will be exacerbated in BLS calculations by negative seasonal adjustments. In November 2011, an unadjusted 1.1% monthly decline in November gasoline prices became a 2.4% decline after seasonal adjustment. Without offsets, the adjusted decline in gasoline prices would be worth about a 0.4% monthly drop in the CPI-U.

Given upside pressures from both food and core inflation, however, there is some chance of the headline number being less-negative than developing market expectations.

Year-to-year, CPI-U inflation would increase or decrease in the November 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the 0.09% gain in the adjusted monthly level reported for November 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for November 2012, the difference in November’s headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the October 2012 annual inflation rate of 2.16%. For example, a 0.2% monthly decline in the headline November 2012 CPI-U, would tend to lower the annual inflation rate to around 1.9%

Industrial Production (October 2012). Due for release on Friday, December 14th, by the Federal Reserve, the headline November 2012 industrial production number is likely to show an outright decline, reflecting increasing efforts at reducing undesired business inventories, as well as some impact from the storm. While likely to disappoint minimally-positive market expectations, this series also is subject to frequent and significant downside revisions.

Weakening production already was in play before Hurricane Sandy, and the storm certainly had some residual negative impact in November. The reporting here, as with the guesstimated activity in retail sales, may be particularly skewed or volatile depending on how the Fed has adjusted the numbers for the storm. Despite what appear to be positive market expectations, for the headline number, a contraction is likely. Also a fair bet is that any “unexpected” weakness will be attributed to Sandy, not to the renewed decline in broad economic activity that was underway before the storm. Of particular interest will be the revisions to earlier, pre-storm reporting.
