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

COMMENTARY NUMBER 516
March Retail Sales and PPI, Gold

April 12, 2013

Despite Concerted Central Bank and Wall Street Efforts to Tarnish Gold,
Gold Does Not Tarnish; It Remains the Primary Hedge Against
Looming Fiscal Fiasco and Dollar Debasement

March Retail Sales Delivered a Traditional Recession Signal

March PPI Hammered by Energy-Price-Suppressing Seasonal Factors

---

PLEASE NOTE: The next regular Commentary *is scheduled for Tuesday, April 16th, covering March industrial production, housing starts, CPI and related inflation-adjusted retail sales and earnings.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY.

Beware the U.S. Dollar. The Federal Reserve and the federal government already have opted to prevent systemic (as in banking-system and Wall Street) collapse at all costs. That decision was made during the 2008 panic, and little has changed. The economy is turning down, anew, having never really recovered; the domestic and global banking systems remain deeply troubled; and the U.S. government's fiscal crisis and related longer-term, sovereign-solvency issues appear to remain well outside the realm of any potential political solution.

The price of gold has been hit heavily recently, and was slammed today, but the extraordinarily bullish fundamentals supporting gold have not changed. There are a number of entities ranging from central banks—particularly the Federal Reserve—to some on Wall Street, who are terrified by gold. Central bankers view strong gold prices as a condemnation of their horrendously flawed policies, while there are those on Wall Street who see gold as an unhealthy distraction from potential commissioned sales on stocks and bonds.

The games being played here are vicious, but the underlying fundamental value of gold as a store of wealth, and as an asset that preserves the purchasing power of the dollars invested in it, cannot be altered by the machinations of the people who created the crises threatening the collapse of the U.S. dollar. These same people commonly have not been noted for being forthright with the general public.

As to "anti-gold fundamentals" that have been circulating recently, they lack substance. Heavily publicized "concerns" as to current Federal Reserve policy—expressed by some at the Fed—raise legitimate issues. Yet, those issues and risks were understood fully and accepted by the U.S. central bank and its management, when Fed Chairman Bernanke's concepts of quantitative easing were launched and then successively expanded.

Now, a delicate public-relations game is underway, with appropriate cautions being expressed within the Fed. Yet, continued deterioration in the U.S. economy, in U.S. banking-system solvency and in long-term U.S. fiscal stability offers no likely circumstance in the near future that would enable the Federal Reserve to reverse its easing actions of recent years. Quite to the contrary, continuing efforts to prevent the collapse of the financial system most likely will lead to expanded, not reduced, Federal Reserve accommodation. As discussed in *Hyperinflation 2012*, there is no easy or painless way out of this circumstance, for the Federal Reserve or for the U.S. government.

Not so coincidentally with the Fed's orchestrated self-criticism, there have been rumors of large gold sales; likely market interventions aimed at depressing the price of gold; and mounting Wall Street jawboning against gold as a commodity, as a safe-haven preservation-of-wealth investment, and in favor the soon to be heavily debased U.S. dollar. Contentions that the world (or the stock market) is back to normal, that everything is understood and under control are nonsense. Those happy thoughts should fall apart quickly under the pressures of real world developments.

Jawboning, rumors and intervention are old tricks of the trade, but usually they are short-lived in terms of impact. The Federal Reserve will keep playing its games as long as possible, but economic stresses on the financial system and market stresses from the still simmering fiscal crisis should further force the Fed's save-the-system actions sooner, rather than later. Of particular concern, the U.S. fiscal fiasco—a known toxin for the U.S. dollar—should force its way to the top tier of global financial market concerns within the next month or two. As a result, current efforts at boosting the dollar and hitting precious metals pricing may be aimed simply at resetting the gold- and dollar-market bases at more-favorable systemic levels, before the turmoil begins.

Irrespective of the irregular, short-term volatility that hits the markets for gold and silver and the exchange rate for the U.S. dollar; held for the long term, gold remains the primary hedge against the U.S. dollar debasement ahead. Again, the fundamentals are unchanged. Whether gold is purchased at $250, $2,500 or $25,000 per ounce, it preserves the purchasing power of the dollars invested. Someone looking to take profits at $100,000 an ounce is missing what has happened. Those "profits" again are just the preserved purchasing power of the invested dollars. Another way of viewing that is the implied proportionate amount of dollar purchasing power that was lost with the dollars not invested in hard assets.

Economy. If individuals could receive their paychecks on a seasonally-adjusted basis, then perhaps the headline inflation numbers might have somewhat greater meaning for the average consumer. The seasonally-adjusted headline 0.6% percent decline in headline PPI was a monthly gain of 0.2% on an unadjusted basis. A similar pattern of weaker, adjusted inflation and stronger, unadjusted (or common experience) inflation is likely for the headline March CPI due out on April 16th (see *Week Ahead*),

Even allowing for a possible headline contraction in the March CPI-U, the nominal (not-adjusted-for-inflation) 0.4% monthly contraction for March retail sales should remain in contraction in real (inflation-adjusted) terms. Further, real year-to-year growth likely will hit a cycle low, signaling an intensifying or pending intensification of the renewed downturn in economic activity.

The brief economic comments on today's (April 12th) PPI and nominal retail sales, will be expanded significantly with the April 16th *Commentary*, which will detail not only the March CPI and related real retail sales and earnings, but also March industrial production and housing starts. Reporting for March 2013 generally has disappointed market expectations, so far, on employment and retail sales. That pattern likely will continue.

March 2013 Retail Sales. Disappointing the market outlook, headline retail sales declined by a statistically-insignificant 0.43% (down 0.74% before prior-period revisions) in March, following a revised February gain of 1.03%. Year-to-year, March sales slowed to 2.82%, from a downwardly revised 4.36% in February. The March annual growth was the slowest since the early days of the official, post-June 2009 economic recovery. With month-to-month March headline CPI-U likely to be flat or a minus, inflation-adjusted retail sales should be in decline for the month, and weak enough year-to-year to be generating a reliable indication of renewed economic downturn.

The increasing weakness in sales likely reflects the constraints on consumption from the intense, structural-liquidity woes besetting the consumer. Without real growth in income, and without the ability or willingness to take on meaningful new debt, the consumer simply cannot sustain real growth in retail sales.

March 2013 Producer Price Index (PPI). Regularly-volatile wholesale inflation, as reported in the seasonally-adjusted, finished-goods producer price index (PPI), fell by 0.56% (up by 0.20% unadjusted) in March. The contraction was dominated by negative seasonal-adjustment pressures on energy costs. The March decline followed a February headline gain of 0.66% (0.77% unadjusted). The rounded, seasonally-adjusted headline decline of 0.6% in March reflected a 0.8% monthly increase in food prices and a 0.2% gain in "core" inflation, which were more than offset by a 3.4% decline in finished energy prices.

Unadjusted and year-to-year, March's finished-goods PPI rose by 1.13%, versus a preliminary 1.71% gain in February.

[Further details on March retail sales and the PPI are found in the* Reporting Detail *section.]

HYPERINFLATION WATCH

Hyperinflation Outlook—Updated. *Updated text is underlined in the first, and beginning in the fifth paragraphs following, along with the addition of a link to the new version of the Public Commentary on Inflation in the third paragraph. Otherwise, this synopsis is unchanged from that published in Commentary No. 512 of March 25th. The summary outlook here is intended for new subscribers and for readers looking for a condensed version of the broad overview of economic, inflation and financial circumstances, or who otherwise are not familiar with the hyperinflation report or special commentaries, linked below. Those latter documents are suggested as background reading on the financial turmoil and currency upheaval facing the United States in the next year or two.*

The November 27, 2012 *Special Commentary (No. 485)* updated *Hyperinflation 2012* and the broad outlook for the economy and inflation, as well as for systemic stability and the U.S. dollar. These remain the two primary articles outlining current conditions and the background to the hyperinflation forecast. The basics have not changed here, other than events keep moving towards the circumstance of a domestic hyperinflation by the end of 2014. Nonetheless, the next fully-updated hyperinflation report is targeted for publication around mid-May.

Nothing is normal: not the economy, not the financial system, not the financial markets and not the political system. The system remains still in the throes and aftershocks of the 2008 panic and the near-systemic collapse, and from the ongoing responses to same by the Federal Reserve and federal government. Further panic is possible and hyperinflation is inevitable.

The economic and systemic solvency crises of the last eight years continue. There never was an actual recovery following the economic downturn that began in 2006 and collapsed into 2008 and 2009. What followed was a protracted period of business stagnation that began to turn down anew in second- and third-quarter 2012. The official recovery seen in GDP has been a statistical illusion generated by the use of understated inflation in calculating key economic series (see *Public Comment on Inflation*). Nonetheless, given the nature of official reporting, the renewed downturn likely will gain recognition as the second-dip in a double- or multiple-dip recession.

Indeed, what continues to unfold in the systemic and economic crises is just an ongoing part of the 2008 turmoil. All the extraordinary actions and interventions bought a little time, but they did not resolve the various crises. That the crises continue can be seen in deteriorating economic activity and in the panicked actions by the Federal Reserve, where it proactively is monetizing U.S. Treasury debt at a pace suggestive of a Treasury that is unable to borrow otherwise.

Continuing hype about the Fed potentially pulling back on its "easing" and a coincident Wall Street push to talk-down gold prices, appear to be little more than hype, designed to jawbone and to help support the U.S. dollar and soften gold in advance of the imminent crises in the federal-budget and debt-ceiling negotiations. Despite orchestrated public calls for "prudence" by the Fed, the underlying and deteriorating financial-system and economic instabilities have self-trapped the Fed into an expanding-liquidity or easing role that likely will not be escaped until the ultimate demise of the U.S. dollar.

Indeed, the Fed's recent and ongoing liquidity actions can be viewed as a signal of deepening problems in the system. Mr. Bernanke admits that the Fed can do little to stimulate the economy, but it can create systemic liquidity and inflation. Accordingly, the Fed's continuing easing moves appear to have been primarily an effort to prop-up the banking system and also to provide back-up liquidity to the U.S. Treasury, under the political cover of a "weakening economy." Mounting signs of intensifying domestic banking-system stress are seen in a renewed weakening of broad money growth, despite a soaring monetary base, and in global banking-system stress, as reflected in the recent Cyprus crisis and its ongoing aftershocks.

Both Houses of Congress recently put forth outlines of ten-year budget proposals that are shy on detail. The ten-year plan by the Republican-controlled House proposes to balance the cash-based deficit as well as to address issues related to unfunded liabilities. The plan put forth by the Democrat-controlled Senate does not look to balance the cash-based deficit. Given continued political contentiousness and the use of unrealistically positive economic assumptions to help the budget projections along, little but gimmicked numbers and further smoke-and-mirrors are likely to come out of upcoming negotiations. With the release of the Administration's budget for fiscal-year 2014, these issues should be coming to a head, now, in April and May; there still appears to be no chance of a substantive agreement.

Indeed, ongoing and deepening economic woes assure that the usual budget forecasts—based on overly-optimistic economic projections—will fall far short of fiscal balance and propriety. Chances also remain nil for the government fully addressing the GAAP-based deficit that hit $6.6 trillion in 2012, let alone balancing the popularly-followed, official cash-based accounting deficit that was $1.1 trillion in 2012 (see *No. 500: Special Commentary*).

Efforts at delaying meaningful fiscal action, and at briefly postponing conflict over the Treasury's debt ceiling, have bought the politicians in Washington minimal time in the global financial markets, but the time largely has run out and patience in the global markets is near exhaustion. The continuing unwillingness and political inability of the current government to address seriously the longer-range U.S. sovereign-solvency issues, only pushes along the regular unfolding of events that eventually will trigger a domestic hyperinflation, as discussed in *Commentary No. 491*.

The unfolding fiscal catastrophe, in combination with the Fed's direct monetization of Treasury debt, eventually (more likely sooner rather than later) will savage the U.S. dollar's exchange rate, boosting oil and gasoline prices, and boosting money supply growth and domestic U.S. inflation. Relative market tranquility likely will not last much longer, despite the tactics of delay by the politicians and obfuscation by the Federal Reserve.

This should become increasingly evident as the disgruntled global markets begin to move sustainably against the U.S. dollar. A dollar-selling panic is likely this year—of reasonably high risk in the next month or two—with its effects and aftershocks setting hyperinflation into action in 2014. Gold remains the primary and long-range hedge against the upcoming debasement of the U.S. dollar, irrespective of any near-term price gyrations in the gold market.

REPORTING DETAIL

RETAIL SALES (March 2013)

A Clear, Traditional Recession Signal at Hand. As discussed in the *Opening Comments and Executive Summary*, the headline 0.43% contraction in March retail sales surprised market expectations on the downside. Even with the headline, month-to-month CPI-U for March 2013 likely to be flat or a small contraction (see *Week Ahead*), real (inflation-adjusted) retail sales should be in decline for the month, with a low level of real year-to-year growth. Such annual growth traditionally is seen only leading into a regular downturn in economic activity, or—in the current circumstance—signaling an intensifying, renewed contraction in the economy.

What is happening here likely is primarily a reflection of constraints on consumption from the intense, structural-liquidity woes besetting the consumer. Without real growth in income, and without the ability or willingness to take on meaningful new debt, the consumer simply cannot sustain real growth in retail sales, let alone in the broader personal consumption measure in GDP.

Otherwise, highly variable and unstable seasonal factors clouded activity in the January 2013-to-March 2013 period, and in February 2012-to-March 2012, five months that are published on a non-comparable basis with all the other historical monthly numbers, due to the use of concurrent seasonal adjustments. These inconsistencies allow for unreported shifts in the historical data that could distort the reporting of current headline numbers.

Note: The stability of the seasonal-adjustment process (particularly the concurrent seasonal-adjustment process used with retail sales) and of sampling methods has been disrupted severely by the unprecedented depth and length of the current economic downturn in the post-World War II era (the period of modern economic reporting), as well as temporarily from the impact of Hurricane Sandy. Under such circumstances, where the markets effectively are flying blind as to actual economic activity, consideration of broad underlying fundamentals is essential. Consumer income and credit remain structurally impaired, again, as discussed recently in Commentary No. 513 *and in* Hyperinflation 2012 *and* Special Commentary (No. 485).

Nominal (Not-Adjusted-for-Inflation) Retail Sales. Not adjusted for a likely monthly drop in consumer inflation, this morning's (April 12th) report on March 2013 retail sales—issued by the Census Bureau—indicated a statistically-insignificant, seasonally-adjusted monthly decline of 0.43% (that otherwise would have been a statistically-significant decline of 0.74%, before prior-period revisions) +/- 0.6% (all confidence intervals are at the 95% level). The March decline followed a revised monthly gain of 1.03% (previously 1.06%) in February.

Year-to-year, March 2013 retail sales rose by 2.82% +/- 0.8%, versus a downwardly revised 4.36% (previously 4.62%) in February. The March annual growth was the slowest since the early days of the post-June 2009 official recovery, and almost certainly will show a level of inflation-adjusted growth that would signal an unfolding recession in normal economic times.

Nonetheless, the pattern of growth here remains distorted by a continuing pattern of unstable concurrent seasonal-adjustment factors and the lack of fully-consistent, seasonally-adjusted numbers being published by the Census Bureau.

Core Retail Sales. In March 2013, seasonally-adjusted monthly grocery-store sales were down minimally by 0.02%, while gasoline-station sales fell by 2.2%, reflecting negative seasonal-factor impact on gasoline prices. Under normal conditions, the bulk of non-seasonal variability in food and gasoline sales is in pricing, instead of demand. "Core" retail sales—consistent with the Federal Reserve's preference for ignoring food and energy prices when "core" inflation is lower than full inflation—are estimated using two approaches:

<u>Version I:</u> March 2013 versus February 2013 seasonally-adjusted retail sales series—net of total grocery store and gasoline station revenues—fell by 0.24%, versus the official decline of 0.43%.

<u>Version II:</u> March 2013 versus February 2013 seasonally-adjusted retail sales series—net of the monthly change in revenues for grocery stores and gas stations—declined by 0.18%, versus the official drop of 0.43%.

Real (Inflation-Adjusted) Retail Sales. With headline March 2013 CPI inflation likely to be flat to a small contraction, the headline inflation-adjusted, or real, estimate of the March 2013 monthly retail sales decline could narrow from 0.43%, but it likely will remain in month-to-month contraction. The inflation-adjusted retail sales details will be provided in the April 16th *Commentary*, which will cover the release of March 2013 CPI-U. Real year-to-year change likely will hit a new cycle low in the range of historical growth that traditionally signals pending recession, during normal economic times.

PRODUCER PRICE INDEX—PPI (March 2013)

Energy-Related Seasonals Pushed Headline PPI into Contraction. As reported this morning, April 12th, by the Bureau of Labor Statistics (BLS), the regularly-volatile, seasonally-adjusted finished-goods producer price index (PPI) for March 2013 fell by 0.56% (up by 0.20% unadjusted), dominated by negative seasonal-adjustment pressures on energy costs. That followed a February 2013 headline gain of 0.66% (up by 0.77% unadjusted).

The rounded 0.6% seasonally-adjusted decline (0.2% unadjusted gain) reported in headline monthly inflation for the March 2013 PPI reflected an adjusted 0.8% month-to-month (an unadjusted 0.8%) increase in food prices, plus an adjusted 0.2% gain (unadjusted 0.1% gain) in "core" inflation, which were more than offset by an adjusted 3.4% decline (unadjusted unchanged) in finished energy prices.

Unadjusted and year-to-year, March's total finished-goods PPI rose by 1.13%, versus a preliminary 1.71% gain in February. Annual change in the PPI has weakened on a monthly basis from a 7.08% near-term peak seen in July 2011, after which the annual numbers began going against a year-ago period, when Mr. Bernanke was running QE2, meeting with early success in debasing the U.S. Dollar and generating an increase in oil prices. QE3's impact, so far, has just started to come into play, with the Fed's expanded easing program having put some upside pressure on oil prices.

Core Finished Goods. "Core" inflation is net of food and energy inflation. The concept of core inflation as a realistic measure of full inflation remains nonsensical, where food and energy account for 41.4% of the finished goods PPI (24.6% of the CPI-U, 27.6% of the CPI-W).

That said, the core measure, still is useful as an indication of how energy prices, in particular, are impacting the broad economy. For March 2013, the seasonally-adjusted month-to-month core PPI was up by 0.16% (up by 0.05% unadjusted), repeating the February headline gain of 0.16% (up by 0.05% unadjusted). Year-to-year, unadjusted March core finished-goods inflation also held at 1.71% for the second month. A comparison of core-PPI with core-CPI-U year-to-year growth in March will be graphed in the *Opening Comments and Executive Summary* section of the April 16th *Commentary*.

Intermediate and Crude Goods. Reflecting generally lower average oil prices and negative seasonal-factor impact, on a month-to-month basis, seasonally-adjusted March 2013 intermediate-goods prices fell by 0.9%, following an increase of 1.3% in February, where March crude-goods prices were down by 2.5%, following a 0.3% decline in February.

Year-to-year inflation in unadjusted March 2013 intermediate goods declined by 0.8%, having increased by 1.2% in February. Year-to-year inflation in March crude goods declined by 0.3%, having increased by 0.9% in February.

WEEK AHEAD

Weaker Economic and Softer Inflation Data Should Surface in the Near-Term. Reflecting the intensifying structural liquidity constraints on the consumer, and in anticipation of the likely negative impact, of the continuing and expanded QE3 and the still-pending fiscal crisis/debt-ceiling negotiations, on the U.S. dollar in the currency markets, reporting in the months and year ahead generally should reflect higher-than-expected inflation and weaker-than-expected economic results. As with the PPI, the March CPI, should prove to be an exception. Increasingly, previous estimates of economic activity should revise lower, particularly in upcoming annual benchmark revisions, as was seen for industrial production, and as pending for new orders for durable goods (May 17th), retail sales (May 31st), trade deficit (June 4th) and GDP (July 31st—comprehensive overhaul and redefinition back to 1929).

Significant reporting-quality problems continue with most major economic series. Headline reporting issues remain 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 reported 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 by the Fed's monetary policies. The political system would like to see the issues disappear, and it still appears to be trying to work numerical slight-of-hand with series such as the GDP and related projections of the federal budget deficit. The media do their best to avoid publicizing unhappy economic news or, otherwise, they put a happy spin on the numbers. Pushing *the politicians and media, the financial markets and related spinmeisters 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* Hyperinflation 2012 *and* No. 485: Special Commentary.

Consumer Price Index—CPI (March 2013). The release by the Bureau of Labor Statistics (BLS) of the March 2013 CPI numbers is scheduled for Tuesday, April 16th. Although gasoline prices stopped surging in late-March, average gasoline prices still were up by 1.2% month-to-month, on a not-seasonally-adjusted basis, per the Department of Energy. The BLS seasonal adjustments, however, should push gasoline prices into an adjusted monthly contraction, perhaps to an order-of-magnitude contraction of 4.5%. As recently revised, an unadjusted monthly gain of 8.1% in March 2012 gasoline prices was reduced to just a 2.0% gain by downside seasonal adjustments.

A 4.5% contraction in adjusted gasoline prices, by itself, would reduce headline CPI-U by roughly two-tenths of a percentage point. Combined with rising food and core inflation, the decline in energy goods could be offset to a large extent. Market expectations appear to be developing around "unchanged" for the headline March 2013 CPI-U. That is not unreasonable, although the reporting risk likely is slightly to the downside of expectations.

Year-to-year, CPI-U inflation would increase or decrease in March 2013 reporting, dependent on the seasonally-adjusted monthly change, versus a reported 0.31% monthly inflation rate in March 2012. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for March 2013, the difference in March's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the February 2013 annual inflation rate of 1.98%. For example, an "unchanged" headline March 2013 CPI-U would result in year-to-year inflation of roughly 1.7%.

Index of Industrial Production (March 2013). The release of detail on the March 2013 index of industrial production also is scheduled for Tuesday, April 16th, by the Federal Reserve. With the downside benchmark revision in place, and with inventories still too high for existing demand levels, weaker production—below developing upside expectations—is a fair bet for March reporting.

Reporting in the series remains extremely volatile and subject to significant monthly revisions. Recent reporting generally has been stronger than would be suggested by underlying fundamentals.

Residential Construction (March 2013). In the third major release scheduled for Tuesday, April 16th, the estimate of March housing starts activity will be published by the Census Bureau. Despite developing market expectations of a small headline gain, reported month-to-month changes likely will continue to be statistically-insignificant.

In the wake of a 75% collapse in activity from 2006 through 2008, and an ensuing four-year pattern of housing starts stagnation at historically low levels, little has changed. There remains no chance of a near-term, sustainable turnaround in the housing construction market, unless there is a fundamental upturn in consumer and banking liquidity conditions. That has not happened, as detailed most recently in *Commentary No. 513*.

