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

COMMENTARY NUMBER 533
May Industrial Production and PPI

June 14, 2013

Weakening Economy and Rising Inflation Should Become the Trend

Contraction in Second-Quarter Production
Suggested by Faltering Numbers

Headline PPI Jumped 0.5% with Shifting Seasonal-Factor Distortions

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PLEASE NOTE: The next regular Commentary *is scheduled for Tuesday, June 18th, covering the May consumer price index (CPI), related real retail sales and earnings series, and housing starts.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Softening Economic Activity in Conjunction with Rising Inflation. Weaker-than-expected headline industrial production, and stronger-than-expected PPI finished-goods (wholesale) inflation, were contrary to what the Fed or the financial market would like to have seen. Nonetheless, that trend of rising inflation, amid contracting business activity, increasingly will become the norm in the months and year ahead. Inflation can be tied to a strong economy or to monetary/currency distortions that can reflect a weak economy.

The happier inflation scenario is based on a demand-driven circumstance, such as seen generally in the context of booming economic activity. Due to excess demand, prices are rising, but so too are employment levels.

The current inflation circumstance, however, is driven by weakness in the U.S. dollar, broadly as desired by the Federal Reserve in this post-2008-panic environment. Sporadic weakness in the dollar has been a primary driving factor behind the sporadic high oil prices and rising gasoline prices. Currency volatility usually is reflected in parallel energy-price volatility. As weakness in the U.S. dollar begins to intensify more regularly, so too should the upside pressures on energy inflation. Not only is such inflation intensified by economic weakness, but also it can become somewhat self-feeding in driving economic activity lower.

Consider, for example, rising gasoline costs for consumers who lack growth in limited income and/or credit. With the rising cost of meeting necessary gasoline demand, those without adequate disposable income have to cut back in other areas of consumption, in less-necessary expenditures (see consumer liquidity discussion in *Commentary No. 532*), in order to compensate for significantly higher gasoline prices.

A more-comprehensive assessment of the May economic and inflation data will follow in the June 18th *Commentary* covering the May CPI release, real retail sales, real earnings, and housing, in addition to and the context of the other major economic releases for the month.

May 2013 PPI. The seasonally-adjusted, finished-goods producer price index (PPI) for May 2013 rose by 0.46% for the month (a rounded 0.5% headline gain), up by 0.51% unadjusted. That followed a seasonally-adjusted April decline of 0.66% (a rounded headline 0.7%), which was down by 0.31% unadjusted.

The monthly May gain was dominated by higher energy and food prices and was in the context of a turn to a relatively-neutral (still-negative) side of the heavily-distorted, energy-related seasonal-factor adjustments. Those same distorting seasonals will flip to the plus-side in June.

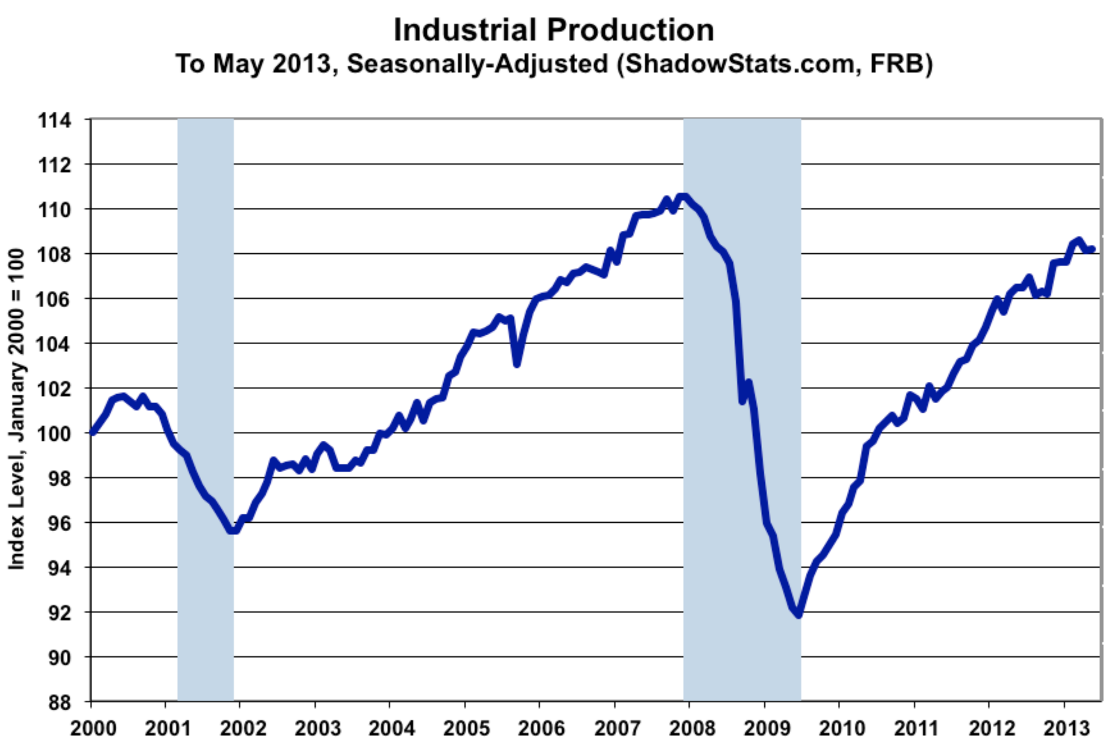
Unadjusted and year-to-year, May's total finished-goods PPI jumped to 1.70%, from a 0.56% gain in April. May's annual change basically regained the 1.71% level of February 2013; otherwise, it was the strongest wholesale inflation reading since 2.35% in October 2012.

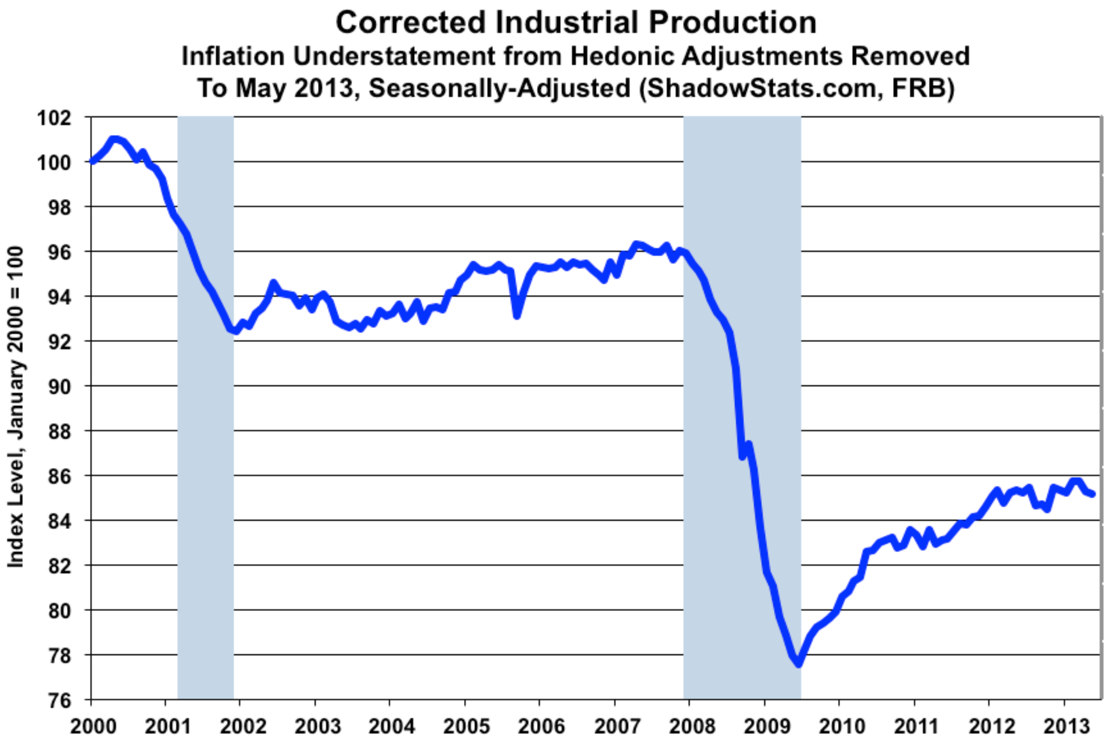
May 2013 Industrial Production. In the context of downside prior-period revisions, headline industrial production was "unchanged" (up by 0.04%) month-to-month in May, versus a revised 0.43% monthly decline in April. With two months of second-quarter 2013 industrial production in hand, production is on track to be flat or in contraction on a quarterly basis. That is not good news for second-quarter GDP growth prospects. Further, May's year-to-year growth slowed to an annual 1.6% gain, from a downwardly-revised 1.8% pace of growth in April. The last time year-to-year production growth slowed to that level was at the onset of the recent economic collapse. Taken together, the latest reporting in this unstable series suggests that a re-intensification of the economic downturn is under way.

The "unchanged" monthly activity in aggregate May production reflected a 0.1% gain in manufacturing, a 0.7% gain in mining activity, and a 1.8% decline in utility usage.

Corrected Industrial Production. Hedonic quality adjustments understate the inflation used in calculating some components of industrial production, with the effect of overstating the inflation-adjusted growth reported in the headline industrial production series (see [Special Commentary (No. 485)] and [Public Comment on Inflation]). The two graphs following address that issue. The first reflects official industrial production reporting, indexed to January 2000 = 100, instead of the Fed's index that is set at 2007 = 100. The 2000 indexing is used simply to provide for some consistency in this series of revamped graphics. The second graph is a corrected version of the first, with estimated hedonic-inflation adjustments backed-out of the official deflator.

The "corrected" graph does show some growth in the period following the official June 2009 near-term trough in production activity. Yet, that upturn has been far shy of the full recovery and the renewed expansion reported in official GDP estimates. Production levels have not regained pre-recession highs (even uncorrected) but, instead, entered a period of protracted low-level stagnation in 2012, with a quarterly contraction in third-quarter 2012, followed by continued stagnation and new indications of a renewed economic downturn. Second-quarter 2013 likely also will reflect a quarter-to-quarter contraction.





[For further detail on the May PPI and industrial production, see the **Reporting Detail** *section.]*

HYPERINFLATION WATCH

Hyperinflation Outlook—Expanded Summary. The hyperinflation outlook was revised and updated with new detail on May 29th, in *No. 527: Special Commentary*, and this summary was revised and expanded to reflect the content of that *Special Commentary* in *Commentary No. 531* of June 8th. The following text has not been changed since *No. 531*. It is intended as background material for new subscribers and for those looking for a brief summary of the broad outlook of the economic, systemic and inflation crises that face the United States in the year or so ahead.

Background Material. *No. 527: Special Commentary* (May 2013) supplemented *No. 485: Special Commentary* (November 2012), reviewing shifting market sentiment on a variety of issues affecting the U.S. dollar and prices of precious metals. *No. 485*, in turn, updated *Hyperinflation 2012* (January 2012)—the base document for the hyperinflation story—and the broad outlook for the economy and inflation, as well as for systemic-stability and the U.S. dollar. Of some use, here, also is the *Public Comment on Inflation*.

These are the primary articles outlining current conditions and the background to the hyperinflation forecast, and they are suggested reading for subscribers who have not seen them and/or for those who otherwise are trying to understand the basics of the hyperinflation outlook. The fundamentals have not changed in recent years, other than events keep moving towards the circumstance of a domestic U.S. hyperinflation by the end of 2014. Nonetheless, the next, fully-updated hyperinflation report is targeted for publication late this month (June 2013).

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

Typical of an approaching, major turning point in the domestic- and global-market perceptions, bouts of extreme volatility and instability have been seen with increasing frequency in the financial markets, including equities, currencies and the monetary precious metals (gold and silver). Consensus market expectations on the economy and Federal Reserve policy also have been in increasing flux, but the markets are stuck with underlying reality and, eventually, they will have to recognize same. The economy remains in continued and deepening trouble, and the Federal Reserve—despite currency-market platitudes to the contrary—is locked into quantitative easing by persistent problems now well beyond its control.

At the same time, rapidly deteriorating expectations for domestic political stability reflect widening government scandals, in addition to the dominant global-financial-market concern of there being no viable prospect of those controlling the U.S. government addressing the long-range sovereign-solvency issues of the United States government. All these factors, in combination, show the end game to be nearing.

The most visible and vulnerable financial element to suffer early in this crisis likely will be the U.S. dollar in the currency markets (all dollar references here are to the U.S. dollar, unless otherwise stated). Heavy dollar selling should evolve into massive dumping of the dollar and dollar-denominated paper assets. Dollar-based commodity prices, such as oil, should soar, accelerating the pace of domestic inflation. In turn, that circumstance likely will trigger some removal of the U.S. dollar from its present global-reserve-currency status, which would further exacerbate the currency and inflation problems tied to the dollar.

This still-forming great financial tempest has cleared the horizon; its impact on the United States and those living in a dollar-based world will dominate and overtake the continuing economic and systemic-solvency crises of the last eight years. The issues that never were resolved in the 2008 panic and its aftermath are about to be exacerbated. Based on the precedents established in 2008, likely reactions from the government and the Fed would be to throw increasingly worthless money at the intensifying crises. Attempts to save the system all have inflationary implications. A domestic hyperinflationary environment should evolve from something akin to these crises before the end of next year (2014). The shifting underlying fundamentals are discussed in No. 527: Special Commentary; some of potential breaking crises will be expanded upon in the next revision to the hyperinflation report.

Still Living with the 2008 Crisis. 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 (see new detail in Commentary No. 530). The official recovery seen in GDP has been a statistical illusion generated by the use of understated inflation in calculating key economic series (see No. 527: Special Commentary, Commentary No. 528 and 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.

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 ongoing panicked actions by the Federal Reserve, where it still proactively is monetizing U.S. Treasury debt at a pace suggestive of a Treasury that is unable to borrow otherwise.

Before and since the mid-April rout in gold prices, there had and has been mounting hype about the Fed potentially pulling back on its "easing" and a coincident Wall Street push to talk-down gold prices. As discussed in No. 527: Special Commentary, those factors appear to be little more than platitudes to the Fed's critics and intensified jawboning to support the U.S. dollar and to soften gold, in advance of the still-festering 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.

Further complicating the circumstance for the U.S. currency is the increasing tendency of major U.S. trading partners to move away from using the dollar in international trade, such as seen most recently in the developing relationship between France and China (see No. 527: Special Commentary).

The Fed's recent and ongoing liquidity actions themselves suggest a signal of deepening problems in the financial 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 softening annual growth in the broad money supply, despite a soaring pace of annual growth in the monetary base, and in global banking-system stress that followed the crisis in Cyprus and continuing, related aftershocks.

Still Living with the U.S. Government's Fiscal Crisis. Again, as covered in No. 527: Special Commentary, the U.S. Treasury is in the process of going through extraordinary accounting gimmicks, at present, in order to avoid exceeding the federal-debt ceiling. Early-September appears to be the deadline for resolving the issues tied to the debt ceiling, including—in theory—significant budget-deficit cuts.

Both Houses of Congress recently put forth outlines of ten-year budget proposals that still 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. There still appears to be no chance of a forthcoming, substantive agreement on balancing the federal deficit.

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, including briefly postponing conflict over the Treasury's debt ceiling, bought the politicians in Washington minimal time in the global financial markets, but the time 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*.

U.S. Dollar Remains Proximal Hyperinflation Trigger. 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 has given way to mounting instabilities, and severe market turmoil likely looms, despite the tactics of delay by the politicians and ongoing obfuscation by the Federal Reserve.

This should become increasingly evident as the disgruntled global markets begin to move sustainably against the U.S. dollar. As discussed earlier, a dollar-selling panic is likely this year—still of reasonably high risk in the next month or so—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.

The rise in the price of gold in recent years was fundamental. The recent panicked sell-off in gold was not. With the underlying fundamentals of ongoing dollar-debasement in place, the upside potential for gold, in dollar terms, is limited only by its inverse relationship to the purchasing power of the U.S. dollar (eventually headed effectively to zero). Again, physical gold—held for the longer term—remains as a store of wealth, the primary hedge against the loss of U.S. dollar purchasing power.

REPORTING DETAIL

INDEX OF INDUSTRIAL PRODUCTION (May 2013)

May Industrial Production Was Suggestive of Continuing Downturn. In the context of downside prior-period revisions, headline industrial production was unchanged May, versus April. With two months in hand, second-quarter production is on track to be flat or in contraction on a quarter-to-quarter basis. Further, May's year-to-year growth slowed to an annual 1.6% gain, from a downwardly-revised 1.8% pace of growth in April. The last time year-to-year production growth slowed to that level was at the formal onset of the 2007 recession. Taken together, the latest reporting in this unstable series suggests that a re-intensification of the economic downturn is under way.

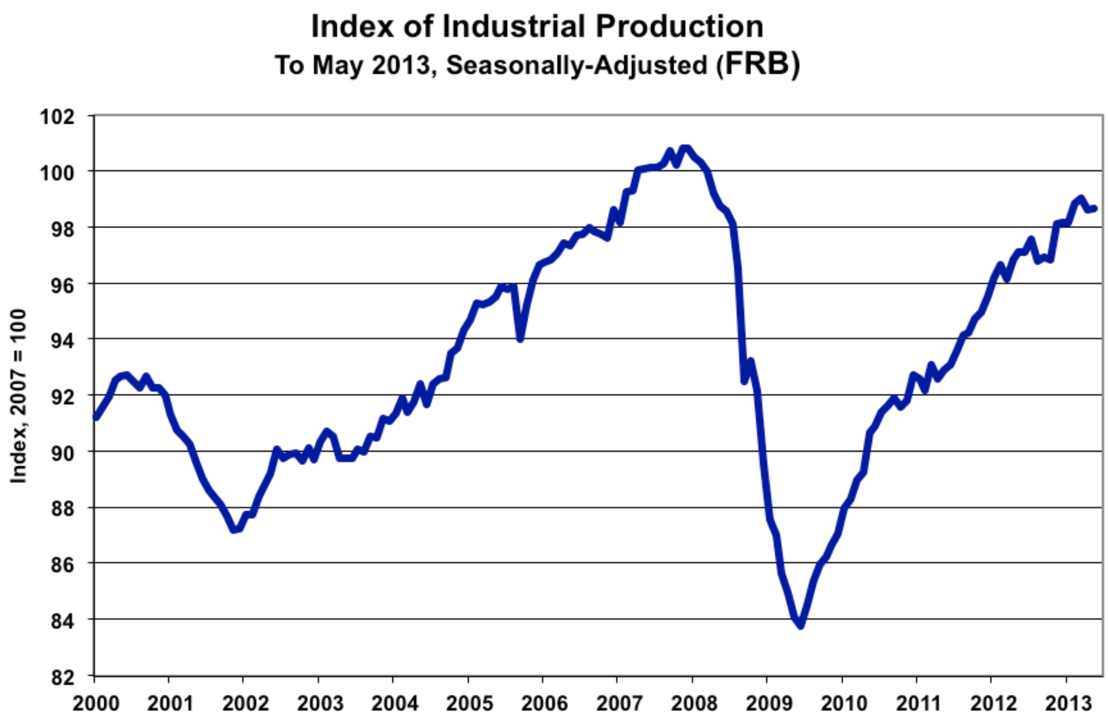
May 2013 Industrial Production. The Federal Reserve Board released its estimate of seasonally-adjusted, May 2013 industrial production this morning, June 14th. In the context of downside prior-period revisions, the headline monthly production activity was "unchanged" in May, at the first decimal point, up by 0.04% at the second decimal point, but down by 0.07% before prior-period revisions. The headline unchanged monthly activity in aggregate production reflected a 0.1% gain in manufacturing, a 0.7% gain in mining activity, and a 1.8% decline in utility usage.

For prior months, the revised April contraction was 0.43% (previously 0.53%), the March gain revised to 0.19% (previously 0.32%, initially 0.41%), and the February gain revised lower, to 0.72% (previously 0.91% and 1.06%, initially 0.75%).

On track to show flat or contracting second-quarter 2013 growth, the May and April index levels averaged 98.65, versus 98.70 in first-quarter 2013. The May contraction in the ISM purchasing managers production survey would favor June and quarterly outright production contractions.

Also suggestive of a renewed downturn in broad economic activity, year-to-year growth in May slowed to 1.61%, from a downwardly revised 1.84% (previously 1.95%) in April, from a downwardly-revised 3.03% (previously 3.26%, initially 3.47%) annual gain in March, and from a downwardly revised 2.28% (previously, 2.37% and 2.49%, initially 2.46%) in February. The last time that year-to-year production growth slowed to current levels was at the formal onset of the 2007 recession.

The "recovery" in industrial production is reflected in the following two sets of graphs. The first graph in the first set shows the monthly level of the production index, while second graph shows the year-to-year or annual percent change in the same series for recent historical detail, in the period beginning January 2000. The second set of graphs shows the same data in historical context since World War II.


Index of Industrial Production
To May 2013, Seasonally-Adjusted (FRB)
Index, 2007 = 100
102
100
98
96
94
92
90
88
86
84
82
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013


Industrial Production Year-to-Year % Change
Jan 2000 to May 2013, Seasonally-Adj. (ShadowStats, FRB)
Yr-to-Yr % Change
10%
8%
6%
4%
2%
0%
-2%
-4%
-6%
-8%
-10%
-12%
-14%
-16%
2000
2001
2002
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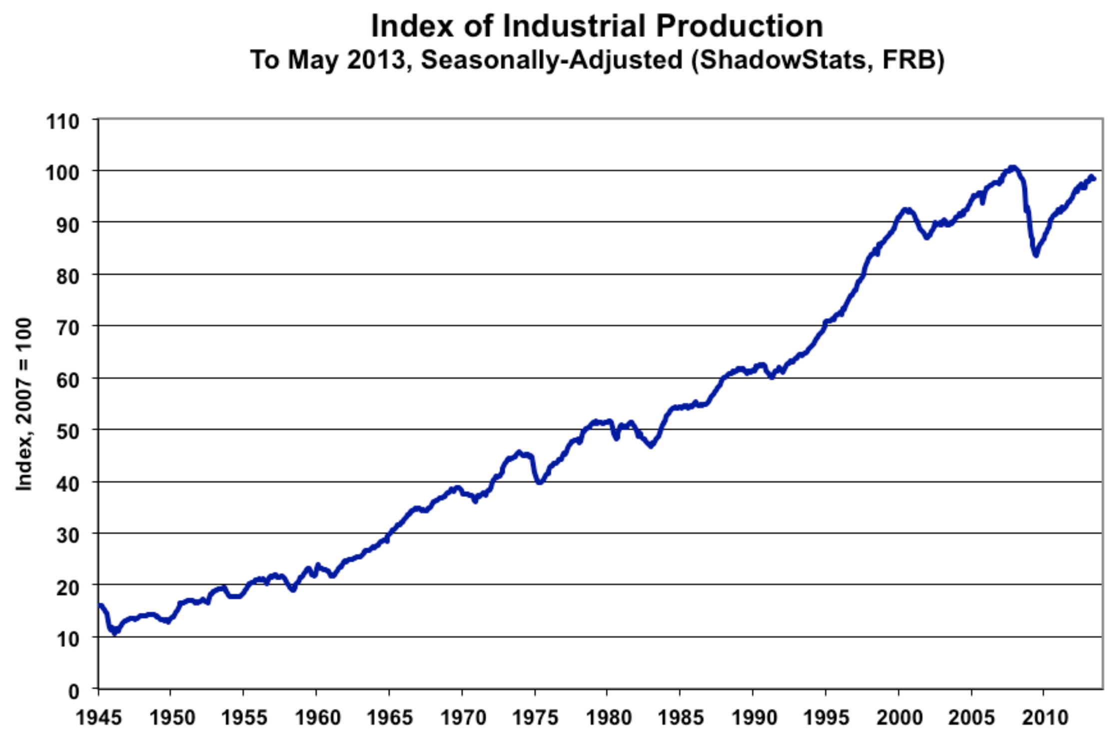
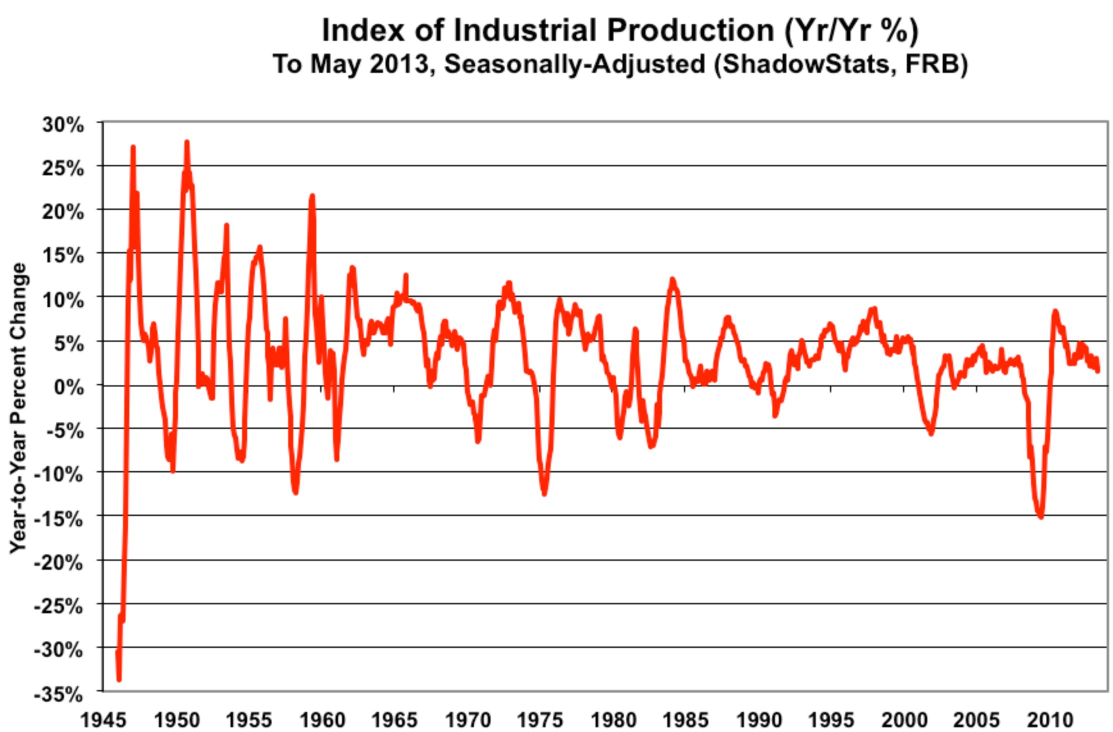
2011
2012
2013


Index of Industrial Production
To May 2013, Seasonally-Adjusted (ShadowStats, FRB)
Index, 2007 = 100
110
100
90
80
70
60
50
40
30
20
10
0
1945
1950
1955
1960
1965
1970
1975
1980
1985
1990
1995
2000
2005
2010


Index of Industrial Production (Yr/Yr %)
To May 2013, Seasonally-Adjusted (ShadowStats, FRB)
Year-to-Year Percent Change
30%
25%
20%
15%
10%
5%
0%
-5%
-10%
-15%
-20%
-25%
-30%
-35%
1945
1950
1955
1960
1965
1970
1975
1980
1985
1990
1995
2000
2005
2010

As shown more clearly in the first set of graphs, current activity has notched lower, and annual growth has slowed to levels last seen in a slowing-growth pattern at the onset of the formal 2007 recession. Annual growth remains well off the recent relative peak for the series, which was 8.50% in June 2010, going against the official June 2009 trough of the economic collapse. Indeed, as shown in the second set of graphs, the year-to-year contraction of 15.02% in June 2009, at the end of second-quarter 2009, was the steepest annual decline in production since the shutdown of war-time production following World War II.

Although official production levels have moved higher since the June 2009 trough, the series still remains shy of a full recovery and appears to be turning down anew, unlike the dubious data in the GDP, which show full recovery as of fourth-quarter 2011, with continuous, new expansion ever since.

Corrected for the understatement of inflation used in deflating portions of the industrial production index, the series has shown more of a bottom-bouncing and recent-downturn pattern, since 2009, where it appears to have topped out coming into 2012, with a renewed downturn likely in process. The corrected production series is discussed and graphed in the *Opening Comments* section. Please note also that index base for those graphs showing production levels, both the corrected graph and the accompanying graph based on official reporting, is January 2000 = 100, instead of the Federal Reserve's official 2007 = 100, used in the graphs here.

PRODUCER PRICE INDEX—PPI (May 2013)

Energy-Related Inflation Resurfaced as Distorting Seasonal Factors Turned Neutral. As reported this morning, June 14th, by the Bureau of Labor Statistics (BLS), the regularly-volatile, seasonally-adjusted finished-goods producer price index (PPI) for May 2013 rose by a month-to-month headline 0.5% (0.46% at the second decimal point, up by 0.51% unadjusted), following an unrevised April headline decline of 0.7% (0.66% at the second decimal point, down by 0.31% unadjusted).

The monthly gain was dominated by higher energy and food prices, in the context of a turn to the relatively-neutral (still-negative) side of the heavily-distorted, energy-related seasonal-factor adjustments. Those same distorting seasonals will flip to the plus-side in June.

The seasonally-adjusted, rounded 0.5% (0.5% unadjusted) gain in headline monthly inflation for the May 2013 PPI reflected an adjusted 1.4% (unadjusted 1.7%) month-to-month increase in finished energy prices, and an adjusted 0.6% (unadjusted 0.6%) month-to-month gain in food prices, along with a negligible contribution from an adjusted 0.1% gain (unadjusted 0.1% decline) in "core" inflation.

Unadjusted and year-to-year, May's total finished-goods PPI jumped to 1.70%, from a 0.56% gain in April. May's annual change basically regained the 1.71% level of February 2013; otherwise, it was the strongest wholesale inflation reading since 2.35% in October 2012. The May 2013 PPI still is well off its near-term peak of 7.08%, seen in July 2011.

<u>Core Finished Goods.</u> "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 May 2013, the seasonally-adjusted month-to-month core PPI was up by 0.05% (down by 0.05% unadjusted), versus a 0.11% gain (up by 0.05% unadjusted) in April. Year-to-year, unadjusted May 2013 core finished-goods inflation eased slightly to 1.65% from 1.71% in April. A comparison of core-PPI with core-CPI-U year-to-year growth in May will be graphed in the *Reporting Detail* section of the pending June 18th *Commentary*.

Intermediate and Crude Goods. Reflecting generally higher average oil prices and mixed seasonal-factor impact, on a month-to-month basis, seasonally-adjusted May 2013 intermediate-goods eased by 0.1%, following a 0.6% decline in April, while May crude-goods prices rose by 2.2%, following a 0.4% decline in April.

Year-to-year inflation in unadjusted May 2013 intermediate goods declined by 0.2%, having dropped by 1.0% in April. Year-to-year inflation in May 2013 crude goods jumped by 7.6%, having increased by 3.1% in April.

WEEK AHEAD

Generally, Weaker Economic Data Are Likely for the Balance of May and Beyond. In the context of a near-consensus May payroll report, an above-consensus retail sales number and below-consensus industrial production growth, most remaining economic reporting in the month ahead likely will disappoint an overly-optimistic consensus view of the broad economy. Separately, as was the case in the prior two months of consumer-inflation reporting, May 2013 consumer inflation should be muted by seasonal-adjustment constraints on oil and gasoline prices, but headline June consumer inflation still could break into positive territory.

[The text in remainder of this Week Ahead *section, including series detail is unchanged from the prior* Commentary.*]* Going forward, reflecting the still-likely negative impact on the U.S. dollar in the currency markets from continuing QE3 and the still-festering fiscal crisis/debt-ceiling debacle, reporting in the ensuing months and year ahead generally should reflect much higher-than-expected inflation (see *No. 527: Special Commentary*).

Where expectations for economic data in the months and year ahead should tend to soften, weaker-than-expected economic results still remain likely, given the intensifying structural liquidity constraints on the consumer. Increasingly, previous estimates of economic activity should revise lower, particularly in upcoming annual benchmark revisions, as has been seen already in industrial production, new orders for durable goods, retail sales, and the trade deficit, and as likely is pending for construction spending (July 1st). The big event, though, will be the July 31st comprehensive overhaul, benchmark revision and redefinition of the GDP back to 1929. A ShadowStats estimate of the likely net shift in GDP reporting patterns (generally slower growth in recent years) will be published before that revision.

Reporting Quality Issues and Systemic Reporting Biases. Significant reporting-quality problems remain with most major economic series. Headline reporting issues are tied largely to systemic distortions of seasonal adjustments. The data instabilities were induced by the still-ongoing economic turmoil of the last six-to-seven years, which has been without precedent in the post-World War II era of modern economic reporting. These impaired reporting methodologies provide particularly unstable headline economic results, where concurrent seasonal adjustments are used (as with retail sales, durable goods orders, employment and unemployment data), and they have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series.

With an increasing trend towards downside surprises in near-term economic reporting, recognition of an intensifying double-dip recession should continue to gain. Nascent concerns of a mounting inflation threat, though muted, increasingly have been rekindled by the Fed's monetary policies. Again, though, significant inflation shocks are looming in response to the fiscal crisis and a likely, severely-negative response in the global currency markets against the U.S. dollar.

The political system and Wall Street would like to see the issues disappear, and the popular media do their best to avoid publicizing unhappy economic news, putting out happy analyses on otherwise negative numbers. Pushing the politicians and media, the financial markets and their related spinmeisters do their best to hype anything that can be given a positive spin, to avoid recognition of serious problems for as long as possible. Those imbedded, structural problems, though, have horrendous implications for the markets and for systemic stability, as discussed in *Hyperinflation 2012*, *No. 485: Special Commentary* and *No. 527: Special Commentary*.

Consumer Price Index—CPI (May 2013). The release by the Bureau of Labor Statistics (BLS) of the May 2013 CPI numbers is scheduled for Tuesday, June 18th. The CPI could come in near a developing, slightly-positive market consensus.

Average gasoline prices rose month-to-month in May by 1.0 percentage point, on a not-seasonally-adjusted basis, per the Department of Energy. The BLS seasonal adjustments, however, should wipe out most of the increase in gasoline prices and other energy inflation. As recently revised, an unadjusted monthly 3.6% decline in May 2012 gasoline prices was turned into a 4.4% decline by downside seasonal adjustments. Similar effects in the May 2013 number generally would neutralize the effects of higher energy prices on the headline inflation number. Given some likely upside inflation pressures from food prices and core inflation, though, a small headline gain in the May 2013 CPI-U is a reasonable expectation.

Year-to-year, CPI-U inflation would increase or decrease in May 2013 reporting, dependent on the seasonally-adjusted monthly change, versus a reported 0.13% decline in monthly inflation for May 2012. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for May 2013, the difference in May's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the April 2013 annual inflation rate of 1.06%. For example, a month-to-month unchanged headline May 2013 CPI-U would increase May annual inflation to about 1.2%

Residential Construction (May 2013). Also on Tuesday, June 18th, the Census Bureau will publish the estimate of May 2013 housing starts activity. Despite developing market expectations for a strong headline gain, reported month-to-month change likely will continue to be statistically-insignificant, with ongoing stagnation in activity for single-unit housing starts.

In the wake of a 75% collapse in aggregate 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 discussed in the *Opening Comments* section.

