

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

COMMENTARY NUMBER 543
June CPI, Industrial Production, Real Retail Sales and Earnings

July 16, 2013

Slowing Growth with Rising Inflation

Real Retail Sales and Real Earnings Contracted in June

Annualized Quarterly Production Growth Slowed to 0.59% from 4.23%

June Year-to-Year Inflation: 1.8% (CPI-U), 1.8% (CPI-W), 9.4% (ShadowStats)

PLEASE NOTE: The next regular Commentary is scheduled for tomorrow, Wednesday July 17th, covering June housing starts.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Unhappy Developments. The opening headlines—suggestive of movement towards the unhappy combination of a weakening economy with rising inflation—all are based on today's (July 16th) official reporting. The details do not get better when viewed in the context of the ShadowStats alternate measures. As discussed in the *Opening Comments* and *Reporting Detail* sections, headline consumer inflation spiked above market expectations, with both real (inflation-adjusted) retail sales and earnings

contracting as a result. Quarterly industrial production slowed to a stall, based on June reporting, and, as discussed in the *Week Ahead* section, tomorrow's housing starts detail likely will show an outright quarterly contraction for second-quarter 2013. Where tomorrow's (July 17th) *Commentary* will include a month-to-date summary of major June economic reporting, along with an updated summary of the *Hyperinflation Outlook*, today's comments are limited to a summary of the data published this morning.

Consumer Price Index—June 2013. Reflecting the continuing seasonal-adjustment shift from suppressing to boosting adjusted energy-related inflation, headline CPI-U increased by 0.5% in June, topping market consensus. As a result, annual inflation jumped to 1.8% in June, from 1.4% in May.

The volatility here reflects a broken, seasonal-adjustment system, where traditional trends—in areas such as energy prices—have been upended by recent extreme turmoil in the energy markets. As discussed in [Commentary No. 541](#), covering the June PPI, both monthly and annual inflation data are best viewed on a not-seasonally-adjusted basis. That said, however, there are other issues in terms of methodological changes, in recent decades, that were designed to understate the government's reporting of consumer inflation, as discussed in the [Public Comment on Inflation Measurement](#).

CPI-U. Per the Bureau of Labor Statistics (BLS), the headline, seasonally-adjusted CPI-U for June 2013 rose by 0.5% (0.48% at the second decimal point) month-to-month, and was up by 0.24%, unadjusted. In May, the adjusted CPI-U rose by 0.1% (0.15% at the second decimal point), and was up by 0.18%, unadjusted. Unadjusted, June 2013 year-to-year CPI-U inflation was 1.75%, up from 1.36% in May.

Core CPI-U. Seasonally-adjusted June 2013 “core” CPI-U inflation (net of food and energy inflation) rose by 0.16% (0.08% unadjusted) month-to-month, versus an adjusted 0.17% (0.10% unadjusted) gain in May. Year-to-year the core CPI-U inflation rate eased to 1.64% in June, from 1.68% in May.

CPI-W. The headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose month-to-month in June by 0.57% (up by 0.26% unadjusted), following an adjusted 0.16% (up by 0.20% unadjusted) gain in May. Unadjusted, June 2013 year-to-year CPI-W inflation was 1.75%, up from 1.24% in May.

Chained-CPI-U. The initial reporting of year-to-year inflation for the June 2013 C-CPI-U was 1.60%, up from 1.31% in May.

ShadowStats Alternate Consumer Inflation Measures. The ShadowStats-Alternate Consumer Inflation Measures, 1990-Base, showed year-to-year inflation at roughly 5.2% in June 2013, up from 4.8% in May; with the 1980-Base, inflation was about 9.4%, up from 9.0% in May 2013.

Real (Inflation-Adjusted) Retail Sales—June 2013. Adjusted for the June CPI-U, real retail sales contracted by 0.11% month-to-month, versus a revised 0.39% gain in May. Nominal (before inflation adjustment) sales had risen by 0.37% in June, but that was more than offset by the 0.48% month-to-month increase in the June CPI-U. Nominal May retail sales gained a revised 0.54% month-to-month, partially offset by 0.15% headline CPI-U inflation in May.

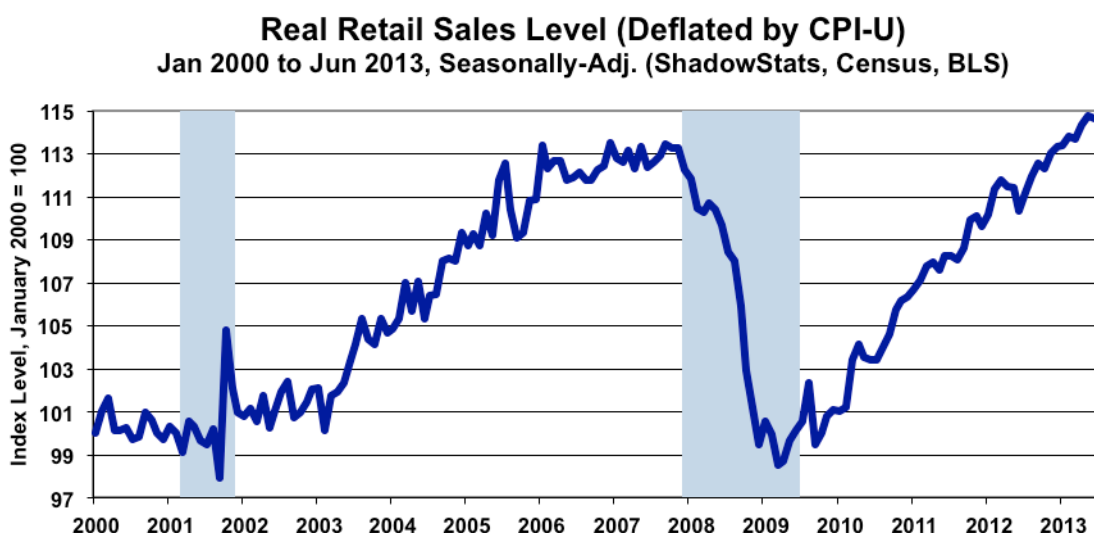
Year-to-year, June 2013 real retail sales rose at an annual pace of 3.90%, versus a revised 2.98% in May. In normal economic times, the recent levels in annual real growth would be signaling a pending recession, but the current circumstance likely is signaling a renewed downturn in broad economic activity.

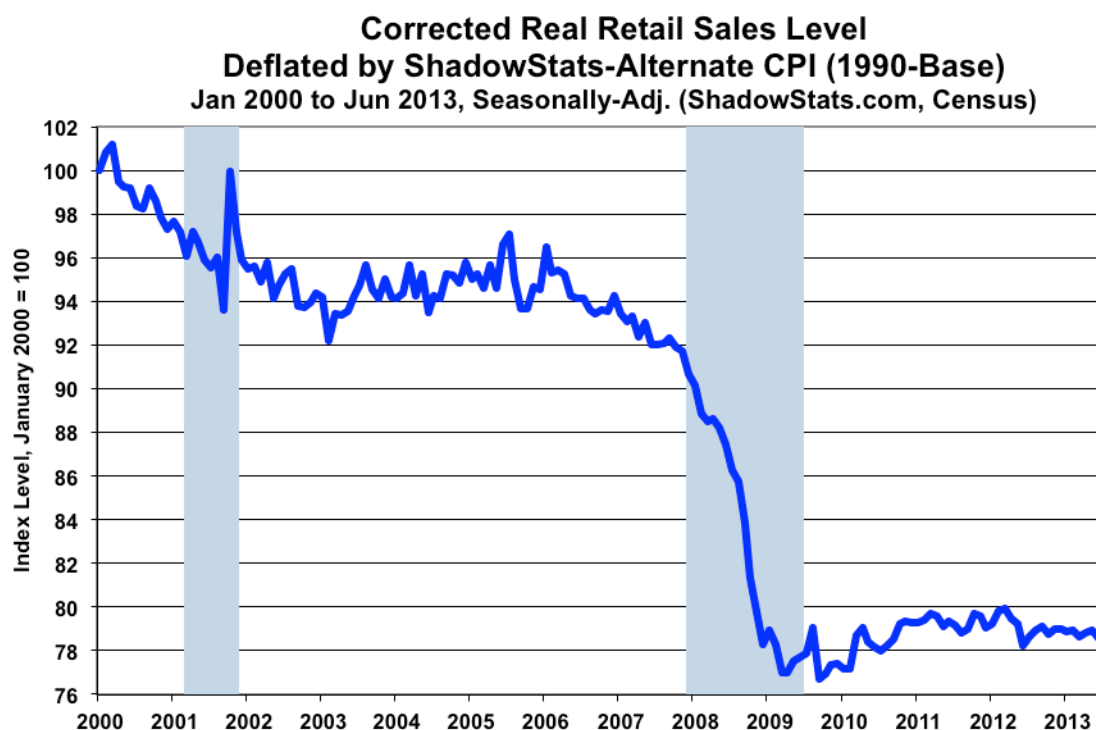
Above Pre-Recession Levels. Real retail sales is the only series, other than GDP, to have broken above its pre-recession high. With June 2013 reporting, though, the real retail sales series has pulled back slightly from that nascent expansion. The GDP, however, began its new expansion more than a six quarters ago and has kept rising, well beyond the reported activity of any other series, including real retail sales. There is no other series showing the GDP's pattern of official, full recovery and extensive new growth.

As discussed in [Commentary No. 542](#), covering nominal retail sales, there has been no change in the underlying consumer-liquidity fundamentals. There is nothing that would support a sustainable expansion in retail sales, personal consumption, housing or general economic activity. There never was a broad economic recovery, and there is no recovery underway, just general bottom-bouncing that is turning down anew. As official consumer inflation continues its upturn, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze, these data should trend meaningfully lower, in what eventually will gain recognition as a formal, double-dip recession.

The apparent “recovery” in the real retail sales series (as well as in the GDP) is due to the understatement of the rate of inflation used in deflating the respective series. As discussed more fully in [Hyperinflation 2012](#) and [Special Commentary \(No. 485\)](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth. The recovery patterns does not hold, however, if the series is corrected for understated inflation.

Corrected Retail Sales. The first graph here reflects real retail sales as usually reported by the St. Louis Fed, deflated by the CPI-U, but it is indexed to January 2000 = 100. ShadowStats did the deflation using the June 2013 CPI-U release. The CPI-U, however, understates inflation (see the [Public Comment on Inflation](#)), with the effect of overstating inflation-adjusted growth. Instead of being deflated by the CPI-U, the “corrected” real retail numbers in the second graph use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation.



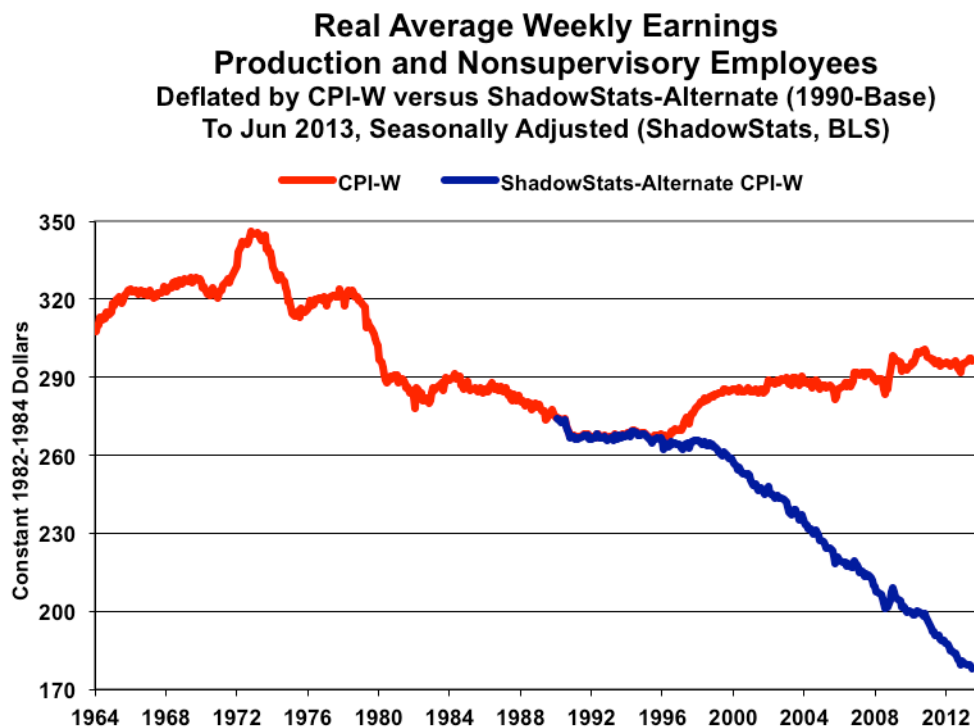


With the higher inflation of the ShadowStats measure, the revamped numbers show a pattern of plunge and stagnation, consistent with patterns seen in real median household income, consumer confidence measures and housing statistics. The recent topping-out reverted to renewed decline in second-quarter 2012, in this series that had been bottom-bouncing along a low-level plateau of economic activity since the economic collapse from 2006 into 2009.

Real Average Weekly Earnings—June 2013. The production and nonsupervisory employees real average weekly earnings is the only such series published by the BLS for which there is a meaningful history. Headline real average weekly earnings (deflated by the CPI-W) fell by 0.3% for the month, in the context of a downside revision to May's reporting. Before prior-period revisions, June real earnings declined by 0.6% for the month. In revision, May 2013 now shows a 0.1% monthly decline (previously a 0.2% gain). For both May and June, the monthly contractions reflected rising inflation. Unadjusted and year-to-year, June real earnings gained 1.5%, versus an unrevised 0.6% annual gain in May.

The following graph of real average weekly earnings shows the earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially weakened CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings.

Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been flat for the last decade. Deflated by the ShadowStats measure, real earnings have been in fairly regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See [Public Commentary on Inflation Measurement](#) for further detail.

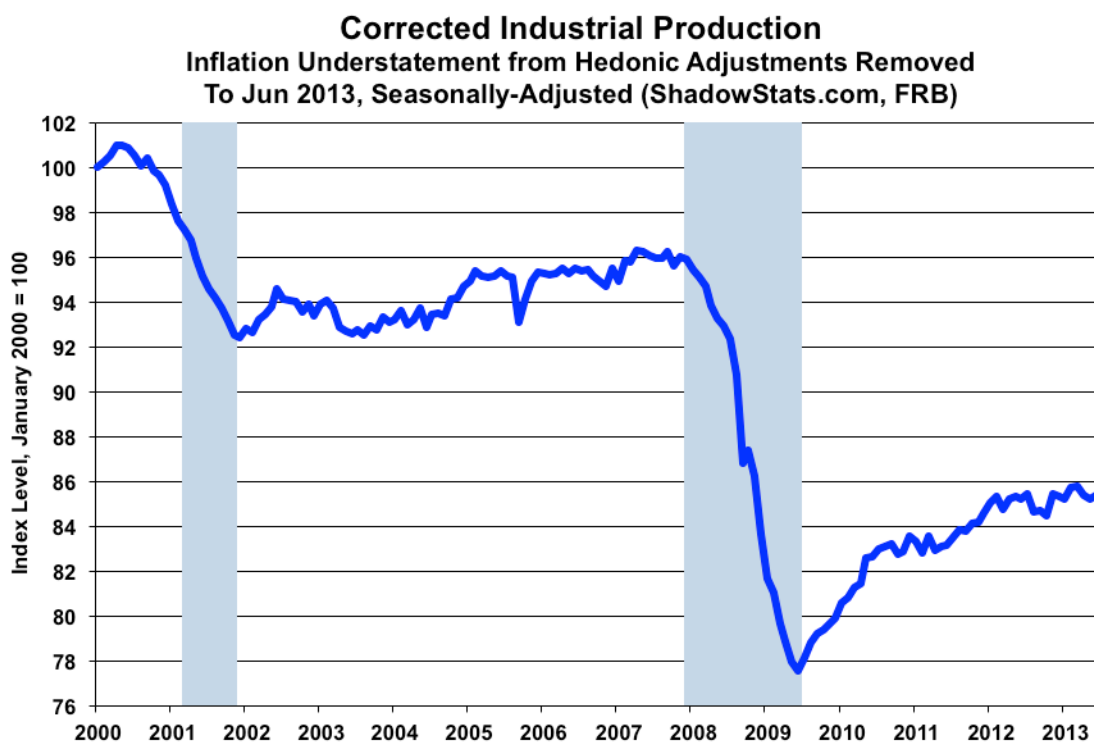
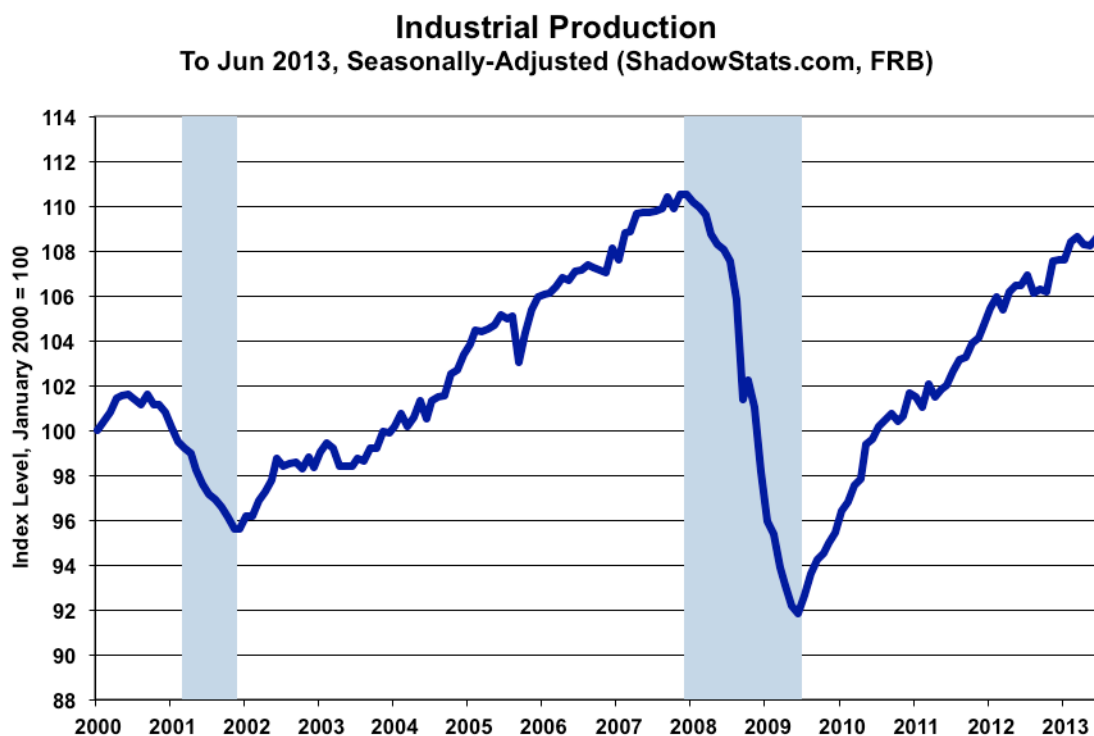


Industrial Production—June 2013. While the headline 0.3% (0.31% at the second decimal point) monthly gain in June industrial production was in line with market expectations, annual growth of 1.98% remained at a level that was consistent with the onset with an intensifying downturn. Further, with initial second-quarter 2013 reporting in place, annualized quarterly growth for the second-quarter slowed to stalling speed, at 0.59%, down from 4.23% in the first-quarter.

With June production activity up by 0.31%, May’s “unchanged” level revised to a 0.04% monthly contraction, from an initial 0.04%. The rounded headline 0.3% gain in aggregate production reflected a 0.3% gain in manufacturing, a 0.8% gain in mining activity, and a 0.1% decline in utility usage.

Suggestive of a renewed downturn in broad economic activity, year-to-year growth in June 2013 was 1.98%, versus a revised 1.69% in May. The last time that year-to-year production growth slowed to current levels was at the formal onset of the 2007 recession, as can be seen in the second production graph in the *Reporting Detail* section.

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 indications of renewed downturn.

[For further detail on the June CPU, inflation-adjusted series and industrial production, see the Reporting Detail section.]

HYPERINFLATION WATCH

Hyperinflation Outlook—Unchanged Summary. *[The Outlook summary will be revised with tomorrow’s housing starts Commentary of July 17th. Otherwise, this summary has not been revised since Commentary No. 536 of June 26th].* The comments here are 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 planned for the near future.

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. The FOMC and Federal Reserve Chairman Ben Bernanke have put forth a plan for reducing and eventually ending quantitative easing in the form of QE3. The tapering or cessation of QE3 is contingent upon the U.S. economy performing in line with overly-optimistic economic projections provided by the Fed. Initially, market reaction pummeled stocks, bonds and gold.

Underlying economic reality remains much weaker than Fed projections. As actual economic conditions gain broader recognition, market sentiment should shift quickly towards no imminent end to QE3, and then to expansion of QE3. The markets and the Fed are stuck with underlying economic reality, and, eventually, they will have to recognize same. Business activity 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. Specifically, banking-system solvency and liquidity remain the primary concerns for the Fed, driving the quantitative easing. Economic issues are secondary concerns for the Fed; they are used as political cover for QE3. That cover will continue for as long as the Fed needs it.

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 appeared 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, and Mr. Bernanke’s press conference following the June 19th FOMC meeting, 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](#)).

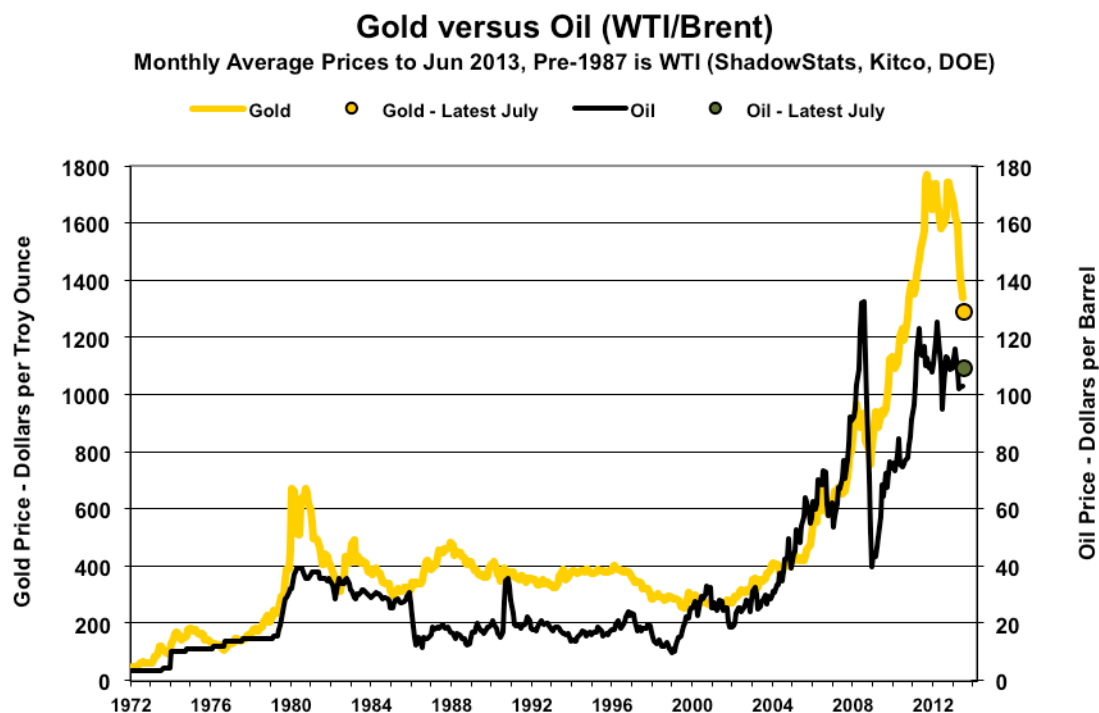
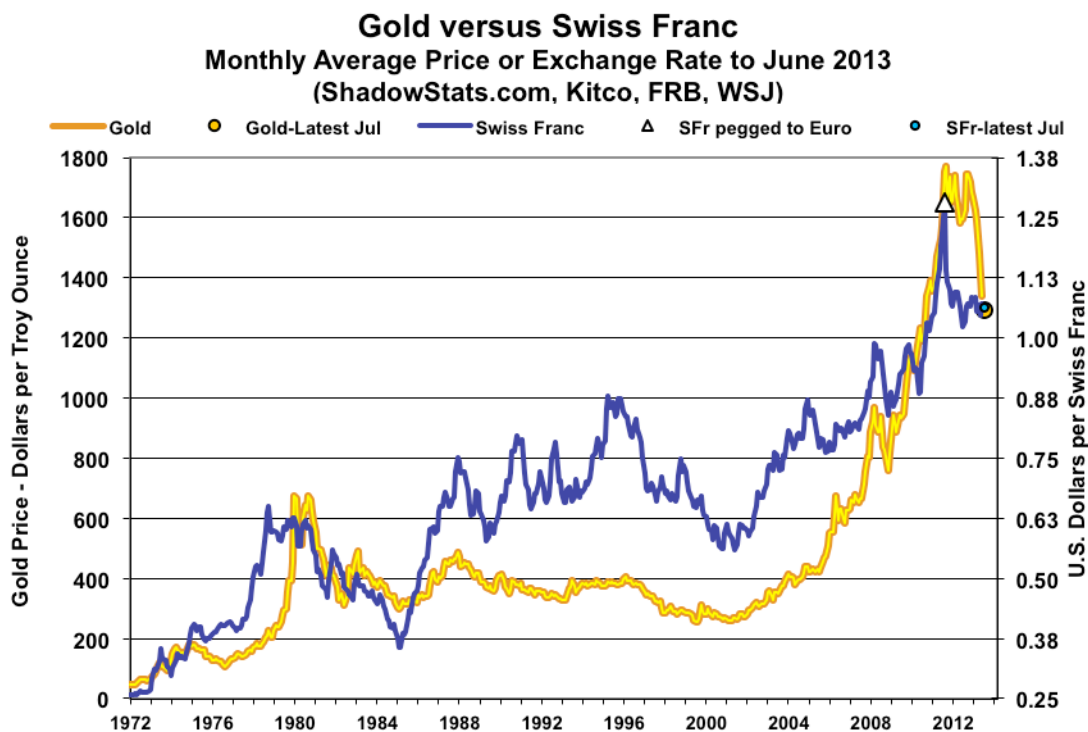
Efforts at delaying meaningful fiscal action, including briefly postponing conflict over the Treasury's debt ceiling, bought the politicians in Washington minimal time in the global financial markets, but the time has run out and patience in the global markets is near exhaustion. The continuing unwillingness 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](#).

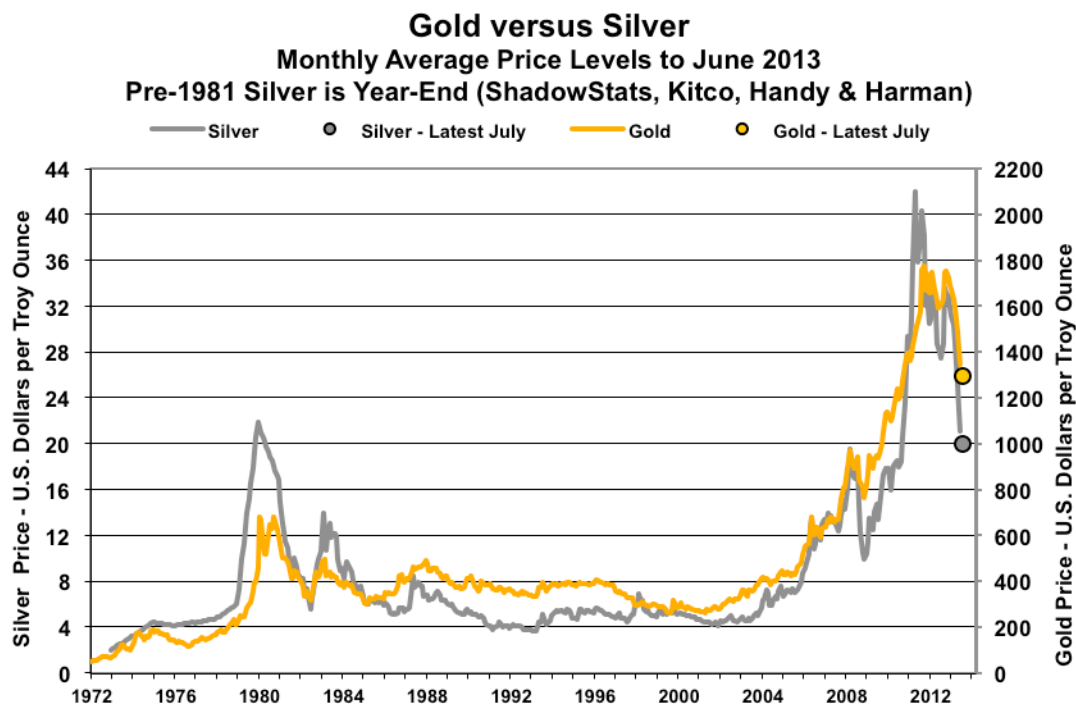
U.S. Dollar Remains Proximal Hyperinflation Trigger. The unfolding fiscal catastrophe, in combination with the Fed's direct monetization of Treasury debt, eventually (more likely sooner rather than later) will savage the U.S. dollar's exchange rate, boosting oil and gasoline prices, and boosting money 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 intermittent panicked selling of gold has not been. 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.

Monthly Gold Graphs. Following are the regular graphs of gold prices versus the Swiss franc, oil prices and silver prices that usually accompany the *Commentary* on the monthly CPI release. The recent turmoil in the markets has abated some, at the moment. Yet, the underlying fundamentals could not be much weaker for the U.S. dollar, and they could not be stronger for gold and silver. Higher oil prices reflect political instabilities in the Middle East and face significant, further upside pressure when the U.S. dollar comes under heavy selling. The “latest July” points in the following graphs are mid-day (New York) market prices, or London afternoon or daily fixes for gold and silver, as of July 16th.





REPORTING DETAIL

CONSUMER PRICE INDEX—CPI (June 2013)

June Consumer Inflation Spiked by Positive Seasonal Factors for Energy Prices. Reflecting the continuing shifts in monthly seasonal adjustments from suppressing to boosting adjusted energy-related inflation, headline consumer inflation increased by 0.5% in June, topping market consensus. As a result, annual inflation jumped to 1.8% in June, from 1.4% in May.

The volatility here is reflective of a broken, seasonal-adjustment system, where long-term trends in areas such as energy prices have been upended by the recent extreme turmoil in the energy markets. As discussed in [Commentary No. 541](#), both monthly and annual inflation data are most meaningfully viewed on a not-seasonally-adjusted basis. That said, there are other issues in terms of methodological changes—

made to the series in recent decades—that were designed to understate the government’s reporting of consumer inflation, as discussed in the [Public Comment on Inflation Measurement](#).

Notes on Different Measures of the Consumer Price Index

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

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

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

*The **C-CPI-U (Chain-Weighted CPI-U)** is an experimental measure, where the weighting of components is fully substitution based. It generally shows lower annual inflation rate than the CPI-U and CPI-W. The latter two measures once had fixed weightings—so as to measure the cost of living of maintaining a constant standard of living—but now are quasi-substitution-based. Since it is fully substitution based, the series tends to reflect lower inflation than the other CPI measures. Accordingly, the C-CPI-U is the “new inflation” measure being considered by Congress and the White House as a tool for reducing Social Security cost-of-living adjustments by stealth.*

*The **ShadowStats Alternative CPI-U Measures** are attempts at adjusting reported CPI-U inflation for the impact of methodological change of recent decades designed to move the concept of the CPI away from being a measure of the cost of living needed to maintain a constant standard of living. There are two measures, where the first is based on reporting methodologies in place as of 1980, and the second is based on reporting methodologies in place as of 1990.*

CPI-U. The Bureau of Labor Statistics (BLS) reported this morning, July 16th that the headline, seasonally-adjusted CPI-U for June 2013 rose by 0.5% (0.48% at the second decimal point) month-to-month, and was up by 0.24%, unadjusted. In May, the adjusted monthly CPI-U rose by 0.1% (0.15% at the second decimal point), and was up by 0.18%, unadjusted.

As happens at this time of year, seasonal adjustments for energy-related inflation shifted to the plus-side. Per the BLS, a 0.6% monthly increase (0.4% increase per the more-comprehensive Department of Energy surveying) in not-seasonally-adjusted gasoline prices for June 2013 was turned to a 6.3% monthly gain by these irregular and distorting seasonal-adjustment factors. The seasonally-adjusted June inflation numbers reflected some catch-up from energy-inflation understatement earlier in the year.

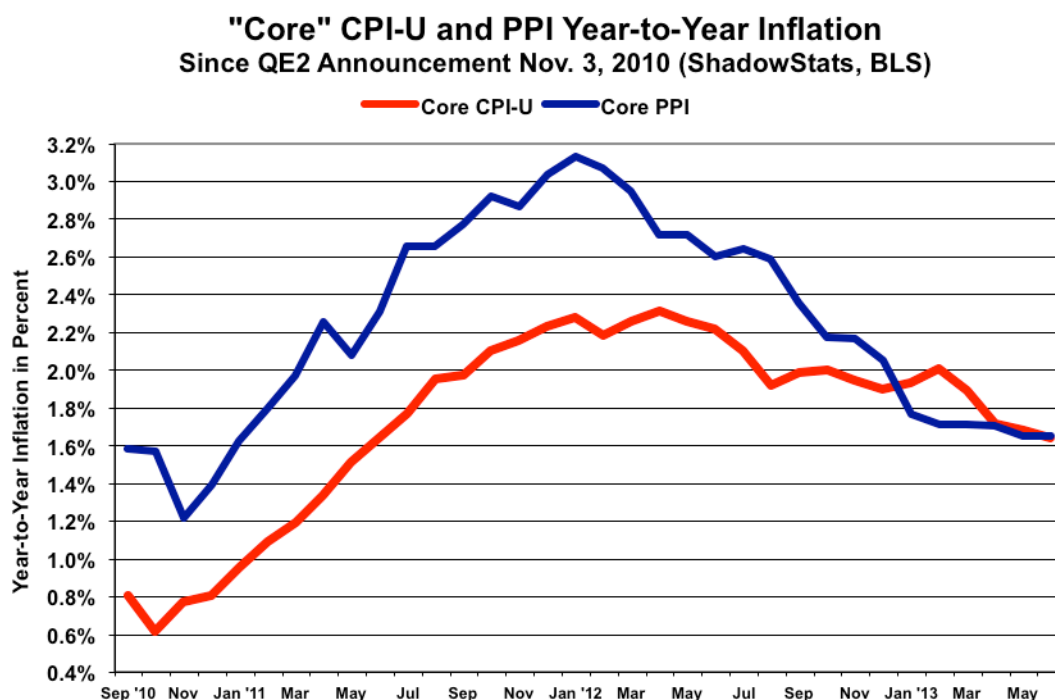
Encompassed by the headline CPI-U monthly gain of 0.5% (0.2% unadjusted), aggregate energy inflation in June 2013 was a 3.4% (unadjusted 1.7%) monthly gain. In the other major CPI sectors, adjusted food inflation was up by 0.2% for the month (up by 0.1% unadjusted), and “core” inflation was up by an adjusted 0.2% (unadjusted 0.1%).

Annualized, seasonally-adjusted CPI-U inflation showed a contraction of 0.03% in second-quarter 2013, versus first-quarter 2013. The annualized quarterly inflation rate for the first-quarter was 1.44%. The large swing was due primarily to the unstable seasonal adjustments applied to gasoline prices. Not-seasonally-adjusted, year-to-year CPI-U inflation was 1.39% in second-quarter 2013, versus 1.68% in the first-quarter.

Not seasonally adjusted, June 2013 year-to-year inflation for the CPI-U was 1.75%, up from 1.36% in May.

Year-to-year, CPI-U inflation would increase or decrease in next month’s July 2013 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.04% decline in monthly inflation reported for July 2012. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for July 2013, the difference in July’s headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the June 2013 annual inflation rate of 1.75%.

Core CPI-U. Seasonally-adjusted June 2013 “core” CPI-U inflation (net of food and energy inflation) rose by 0.16% (0.08% unadjusted) month-to-month, versus an adjusted 0.17% (0.10% unadjusted) gain in May.



Twenty-one of the last thirty-one months have shown rising year-to-year, or annual, core CPI-U inflation, with the year-to-year core rate easing to 1.64% in June from 1.68% in May. The CPI core annual inflation number generally was in line, once again, with the core-PPI growth, which held at 1.65% in June, the same level as in May.

The June 2013 CPI-U year-to-year core rate still was well above the core inflation of 0.61%, in November 2010, when Federal Reserve Chairman Bernanke introduced QE2 in a successful bid to debase the U.S. dollar, with the effect of spiking oil prices. The expansion in QE3 into monetization of Treasury debt has created sporadic upside pressures here in recent months. Nonetheless, the core annual inflation numbers in June 2013—for both the CPI-U and PPI—continue to reflect the ongoing impact of higher energy prices in the broad economy, as suggested by the accompanying graph.

CPI-W. The June 2013 headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose month-to-month by 0.57% (up by 0.26% unadjusted), following an adjusted 0.16% (up by 0.20% unadjusted) gain in May.

Annualized, seasonally-adjusted CPI-W inflation showed a contraction of 0.37% in second-quarter 2013, versus first-quarter 2013. The annualized quarterly inflation rate for the first-quarter was 1.22%. Again, the large swing was due primarily to the unstable seasonal adjustments applied to gasoline prices. Not-seasonally-adjusted, year-to-year CPI-W inflation was 1.26% in second-quarter 2013, versus 1.43% in the first-quarter.

Unadjusted, June 2013 year-to-year CPI-W inflation was 1.75%, up from 1.24% in May.

Chained-CPI-U. The initial reporting of year-to-year inflation for the June 2013 C-CPI-U was 1.60%, up from 1.31% in May. On a quarterly basis, not-seasonally-adjusted (the data are not reported on a seasonally-adjusted basis), year-to-year C-CPI-U inflation was 1.34% in second-quarter 2013, versus 1.45% in the first-quarter.

[The balance of the text in this Chained-CPI-U sub-section is unchanged from the prior CPI Commentary.] The Chained-CPI-U is the fully substitution-based series that is included in the President's fiscal-2014 budget as a new cost-of-living adjustment factor. Congress also has been pushing for the C-CPI as a way to reduce cost-of-living payments for Social Security, etc., by stealth. This would be an outright fraud on the public, continuing a pattern of similar, earlier successful efforts at deceptive inflation reporting, seen in the past several decades (see the discussion in [Public Commentary on Inflation Measurement and Chained-CPI](#)).

The BLS indicates that the C-CPI-U, “is designed to be a closer approximation to a cost-of-living index than other CPI measures. [That is, a fully-substitution as opposed to a fixed-weight basis cost of living measure, where the fixed-weight measures reflect (and substitution-based measures do not reflect) the cost of maintaining a constant standard of living. Again, see the above-linked *Public Commentary*.]

“That said, BLS publishes thousands of indexes each month; these indexes can vary by which items, geographic areas, and populations are covered. As different users have different needs, BLS cannot say which index is necessarily better than another. As such, BLS takes no position on what the Congress or the Administration should use to make adjustments to Social Security or any other federal program.

“The C-CPI-U to our knowledge currently is not used in any federal legislation as an adjustment mechanism.”

The BLS has posted new C-CPI material on its site, apparently beginning to anticipate the pending new political uses for the measure: [Chained CPI](#).

Alternate Consumer Inflation Measures. Adjusted to pre-Clinton methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual CPI inflation was roughly 5.2% in June 2013, up from 4.8% in May.

The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, rose to about 9.4% (9.38% for those using the second decimal point) in June 2013, versus an annual inflation rate of 9.0% in May 2013.

[The balance of the text in this Alternate Consumer Inflation Measures sub-section is unchanged from the prior CPI Commentary.]

Note: The ShadowStats-Alternate Consumer Inflation Measure largely has been reverse-engineered from the BLS’s CPI-U-RS series, which provides an official estimate of historical inflation, assuming that all current methodologies were in place going back in time. The ShadowStats estimates effectively are adjusted on an additive basis for the cumulative impact on the annual inflation rate of various methodological changes made by the BLS (the series is not recalculated).

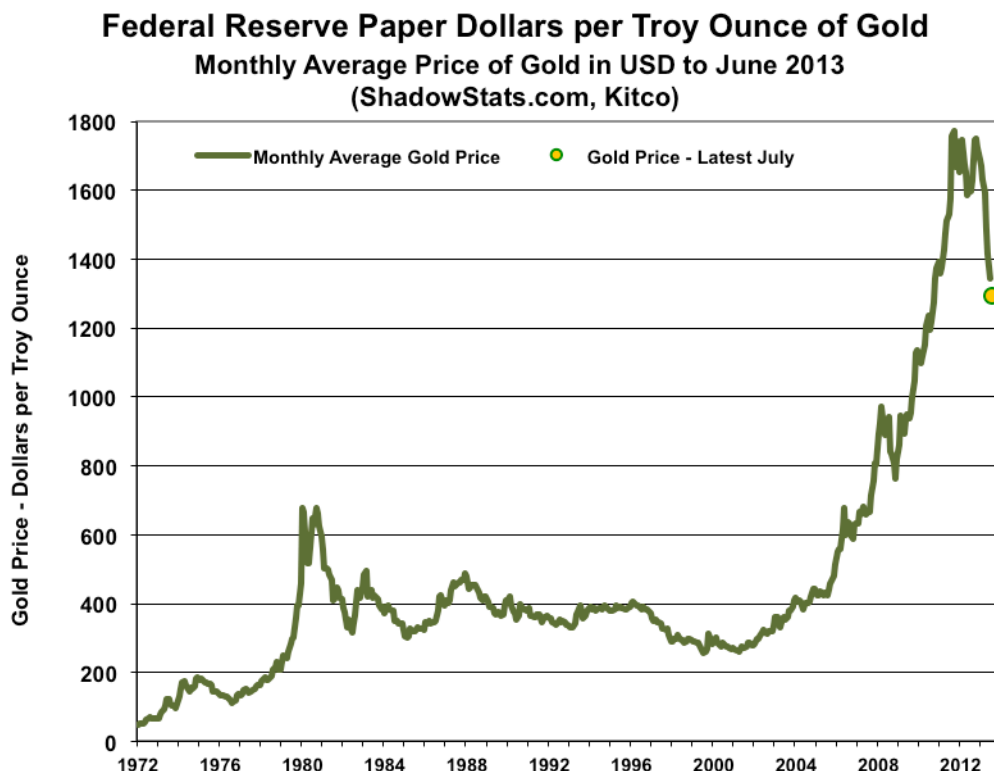
Over the decades, the BLS has altered the meaning of the CPI from being a measure of the cost of living needed to maintain a constant standard of living, to something that neither reflects the constant-standard-of-living concept nor measures adequately what most consumers view as out-of-pocket expenditures. Roughly five percentage points of the additive ShadowStats adjustment reflect the BLS’s formal estimate of the annual impact of methodological changes; roughly two percentage points reflect changes by the BLS, where ShadowStats has estimated the impact not otherwise published by the BLS. (See [Public Commentary on Inflation Measurement and Chained-CPI](#) for further details.)

Gold and Silver Highs Adjusted for CPI-U/ShadowStats Inflation. Despite the September 5, 2011 historic-high gold price of \$1,895.00 per troy ounce (London afternoon fix), and despite the multi-decade-high silver price of \$48.70 per troy ounce (London fix of April 28, 2011), gold and silver prices have yet to re-hit their 1980 historic levels, adjusted for inflation. The earlier all-time high of \$850.00 (London afternoon fix, per Kitco.com) for gold on January 21, 1980 would be \$2,551 per troy ounce, based on June 2013 CPI-U-adjusted dollars, and \$10,212 per troy ounce, based on June 2013 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (all series not seasonally adjusted).

In like manner, the all-time high nominal price for silver in January 1980 of \$49.45 per troy ounce (London afternoon fix, per silverinstitute.org), although approached in 2011, still has not been hit since 1980, including in terms of inflation-adjusted dollars. Based on June 2013 CPI-U inflation, the 1980 silver-price peak would be \$149 per troy ounce and would be \$595 per troy ounce in terms of June 2013 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

As shown in Table 1 on page 50 of [Hyperinflation 2012](#), and as updated in Table III on page 40 of [Special Commentary \(No. 485\)](#), over the decades, the increases in gold and silver prices have compensated for

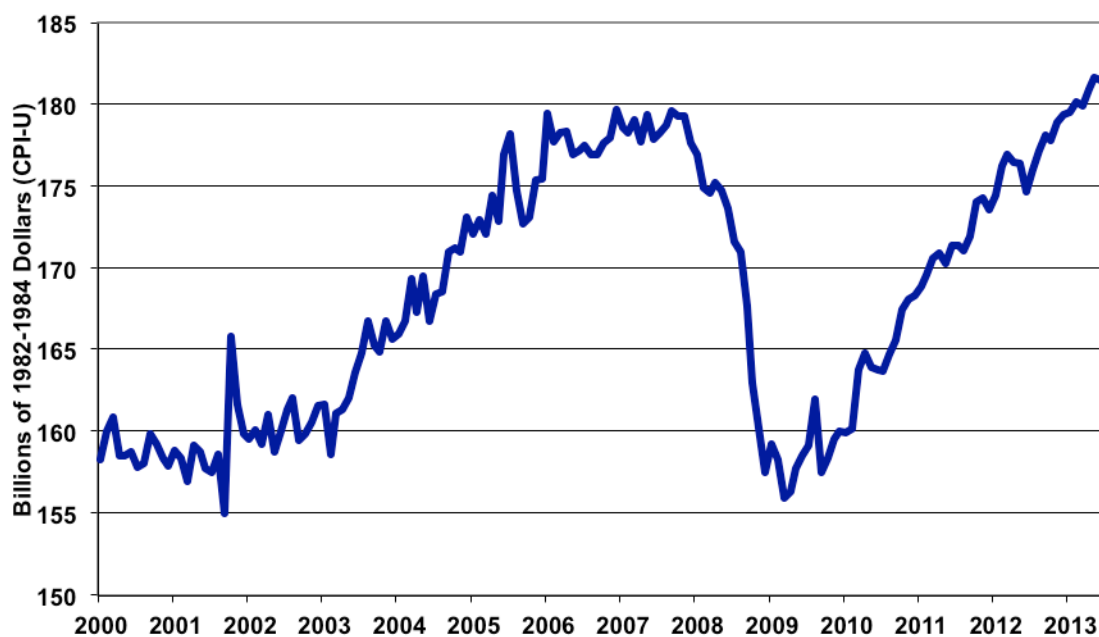
more than the loss of the purchasing power of the U.S. dollar as reflected by CPI inflation, while they effectively have compensated fully for the loss of purchasing power of the dollar based on the ShadowStats-Alternate Consumer Price Measure (1980-Methodologies Base).



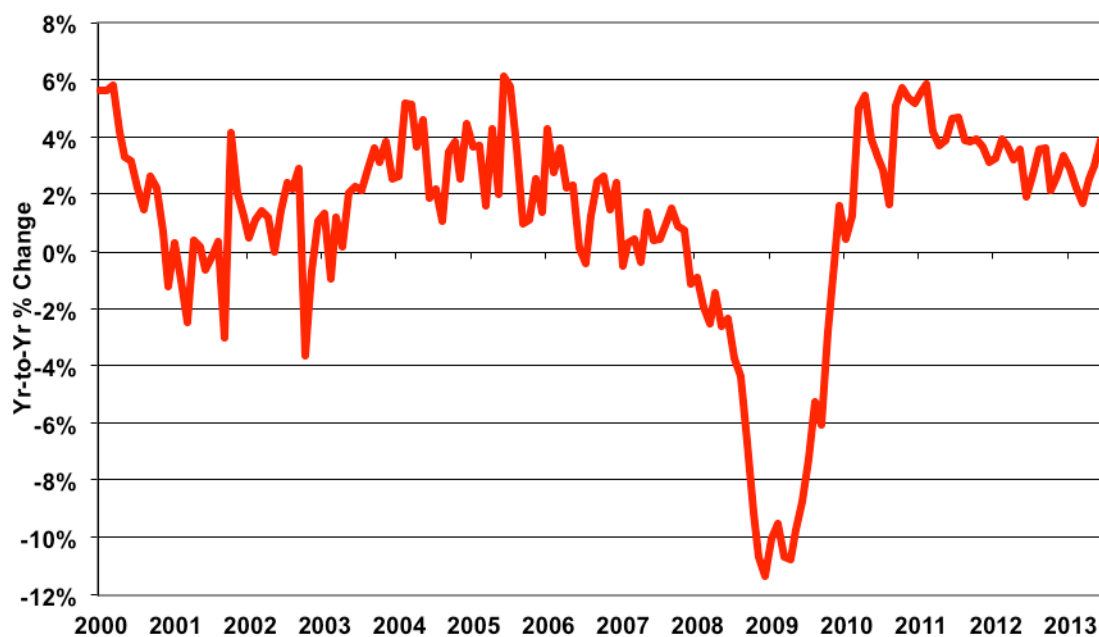
Real (Inflation-Adjusted) Retail Sales—June 2013. June 2013 real retail sales contracted by 0.11% month-to-month, versus a revised 0.39% (previously 0.40%) real gain in May. Nominal (before inflation adjustment) sales had risen by 0.37% in June, but that was more than offset by the 0.48% month-to-month increase in the June CPI-U. Nominal May retail sales gained a revised 0.54% month-to-month, partially offset by 0.15% headline CPI-U inflation in May. See [Commentary No. 542](#) for nominal retail sales reporting detail as published for June 2013.

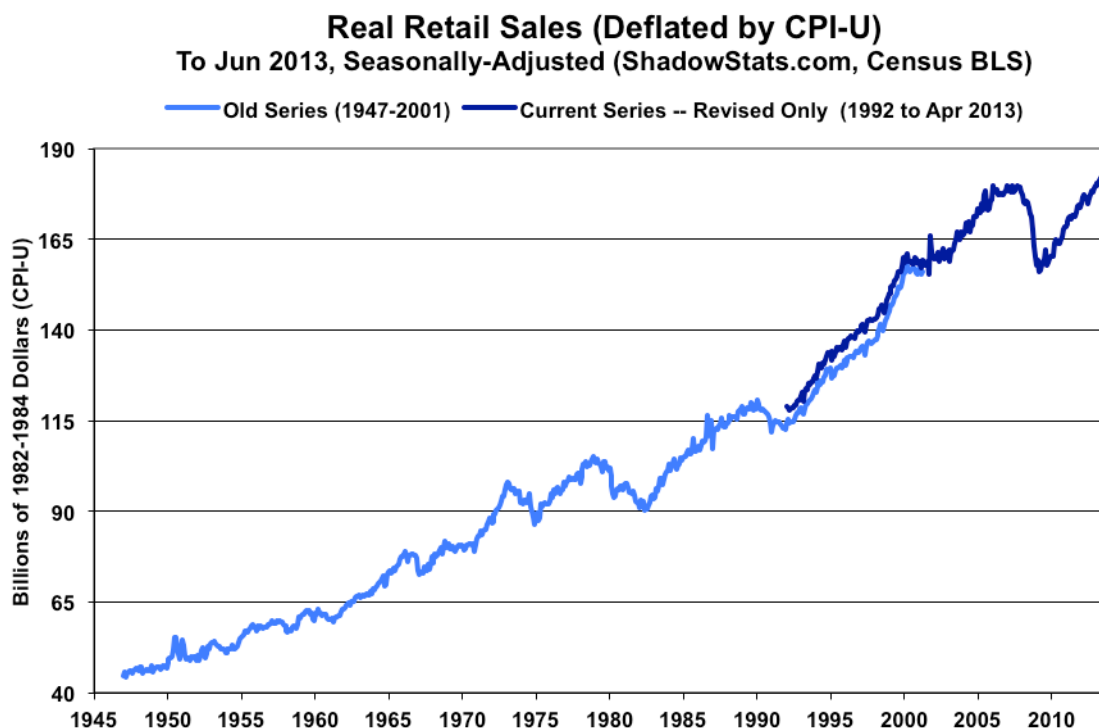
Year-to-year, June 2013 real retail sales rose at an annual pace of 3.90%, versus a revised 2.98% (previously 2.88%) in May, as seen in the second graph following. In normal economic times, the recent levels in annual real growth would be signaling a pending recession. In the current circumstance, this signal likely will serve as an indicator of a renewed downturn in broad economic activity.

Real Retail Sales (Deflated by CPI-U)
Jan 2000 to Jun 2013, Seasonally-Adj. (ShadowStats, Census, BLS)



Real Retail Sales Year-to-Year % Change
Jan 2000 to Jun 2013, Seasonally-Adj. (ShadowStats, Census, BLS)





Above Pre-Recession Levels. The first of the three preceding graphs shows the level of real retail sales activity (deflated by the CPI-U) since 2000, and the second graph shows year-to-year percent change for the same period. The third graph shows the level of the real retail sales series in full post-World War II detail. With June 2013 reporting, the headline real retail sales series has pulled back slightly from its nascent expansion above pre-recession levels. The GDP expanded beyond pre-recession levels, more than a six quarters ago, and it has kept rising, well beyond the reported activity of any other series, including real retail sales. There is no other major economic series showing the GDP's pattern of official, full recovery and extensive new growth.

The apparent “recovery” in the real retail sales series (as well as in the GDP) is due to the understatement of the rate of inflation used in deflating retail sales and other series. As discussed more fully in [Hyperinflation 2012](#) and [Special Commentary \(No. 485\)](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

With the deflation rates corrected for understated inflation, the recent pattern of real sales activity turns increasingly flat-to-negative, as shown in the latest “corrected” real retail sales graph in the *Opening Comments* section. The corrected graph shows that the post-2009 period of protracted stagnation ended, and a period of renewed contraction began in second-quarter 2012. The corrected real retail sales numbers use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation instead of the CPI-U.

As discussed in [Commentary No. 542](#), there has been no change in the underlying consumer-liquidity fundamentals. There is nothing that would support a sustainable turnaround in retail sales, personal

consumption, housing or general economic activity. There never was a broad economic recovery, and there is no recovery underway, just general bottom-bouncing that is turning down anew.

As official consumer inflation continues its upturn in the months ahead, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze—reflected partially by recent real earnings difficulties, discussed in the next section—these data should trend meaningfully lower, in what eventually will gain recognition as a formal, double-dip recession.

Real (Inflation-Adjusted) Average Weekly Earnings—June 2013. Coincident with the CPI release for June 2013, the BLS published real average weekly earnings for June 2013. For the production and nonsupervisory employees series—the only series for which there is a meaningful history—headline real average weekly earnings (deflated by the CPI-W) fell by 0.3% for the month in the context of downside prior-period revisions. Before prior-period revisions, June real earnings decline by 0.6% for the month. In revision, May 2013 now shows a 0.1% monthly decline (previously a 0.2% gain). For both May and June, the contractions reflected rising inflation.

Unadjusted and year-to-year, June real earnings gained 1.5%, versus an unrevised 0.6% annual gain in May. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility.

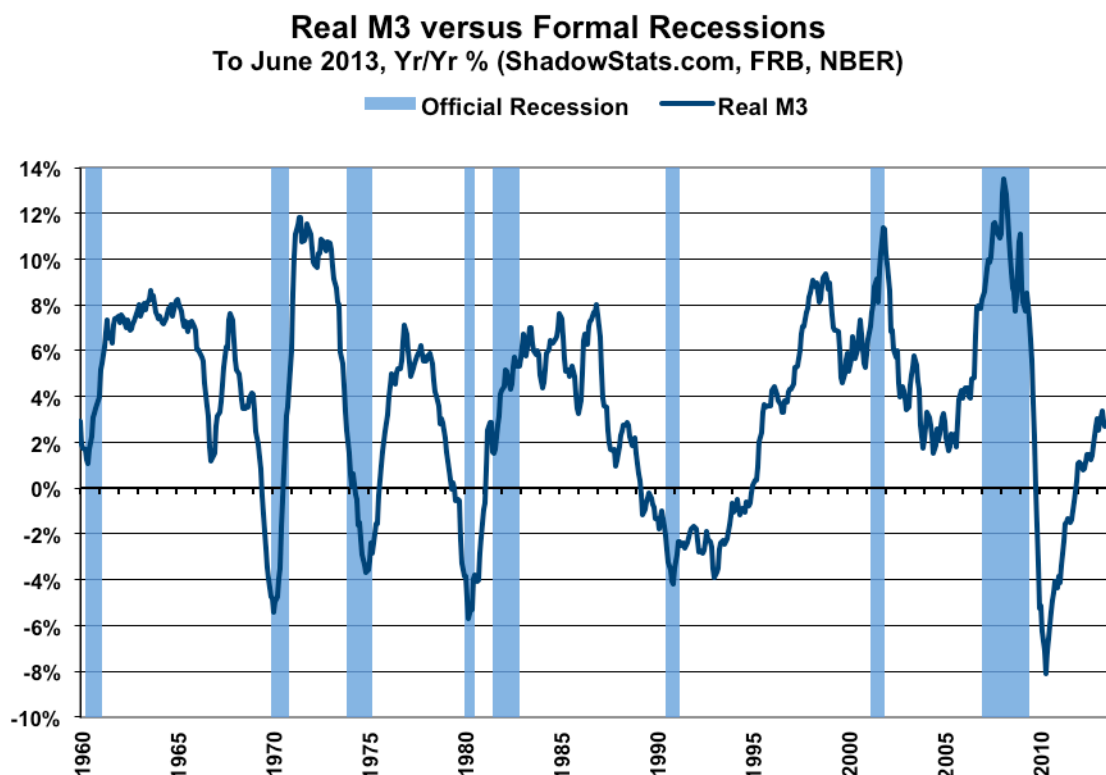
The regular graph of this series is in the *Opening Comments* section. As shown there, the graph plots the earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially weakened CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been flat for the last decade. Deflated by the ShadowStats measure, real earnings have been in fairly regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See [Public Commentary on Inflation Measurement](#) for further detail.

Real Money Supply M3 (June 2013). The signal for a double-dip or ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), discussed in [Hyperinflation 2012](#), remains in place and continues, despite real annual M3 growth having turned to the upside. As shown in the accompanying graph—based on June 2013 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in M3 for June 2013 slowed to 2.7% from an unrevised 2.9% in May. The slower growth reflected a notch higher in nominal M3 annual growth, more than offset by the increase in year-to-year CPI-U inflation.

[The balance of the text in this Real Money Supply M3 sub-section is unchanged from the prior CPI Commentary.] The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first turns negative in a given cycle; the signal is not dependent on the depth of the downturn or its duration. Breaking into positive territory does not generate a meaningful signal one way or the other for the broad economy. The current downturn signal was generated in December 2009, even though there had been no upturn since the economy hit bottom in mid-2009. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of series continued into 2011 and 2012, with significant new softness in recent reporting. Actual post-

2009 economic activity has remained at low levels—in protracted stagnation—as discussed in [Special Commentary \(No. 485\)](#).

A renewed downturn in official data is becoming more obvious, and that eventually should lead to official recognition of a double-dip recession. Reality remains that the economic collapse into 2009 was followed by a plateau of low-level economic activity—no upturn or recovery, no end to the official 2007 recession—and the unfolding renewed downturn remains nothing more than a continuation and re-intensification of the downturn that began unofficially in 2006.



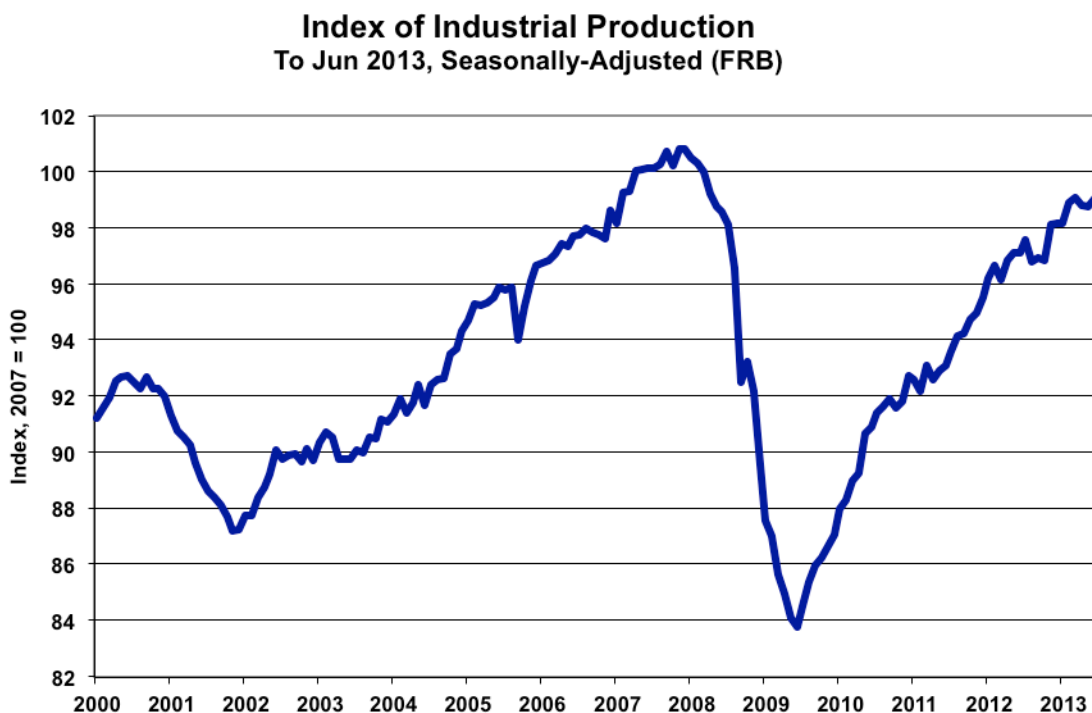
INDEX OF INDUSTRIAL PRODUCTION (June 2013)

June Industrial Production Continued Signaling an Intensifying Downturn. Although the 0.31% monthly gain in June industrial production was in line with market expectations, annual growth of 1.98% remained at a level that was consistent with the onset of a recession in normal economic times—an intensified downturn in the current circumstance. Further, with initial second-quarter 2013 reporting in place, annualized quarterly growth for the second-quarter slowed to a stalling speed of 0.59%, from the 4.23% in the first-quarter.

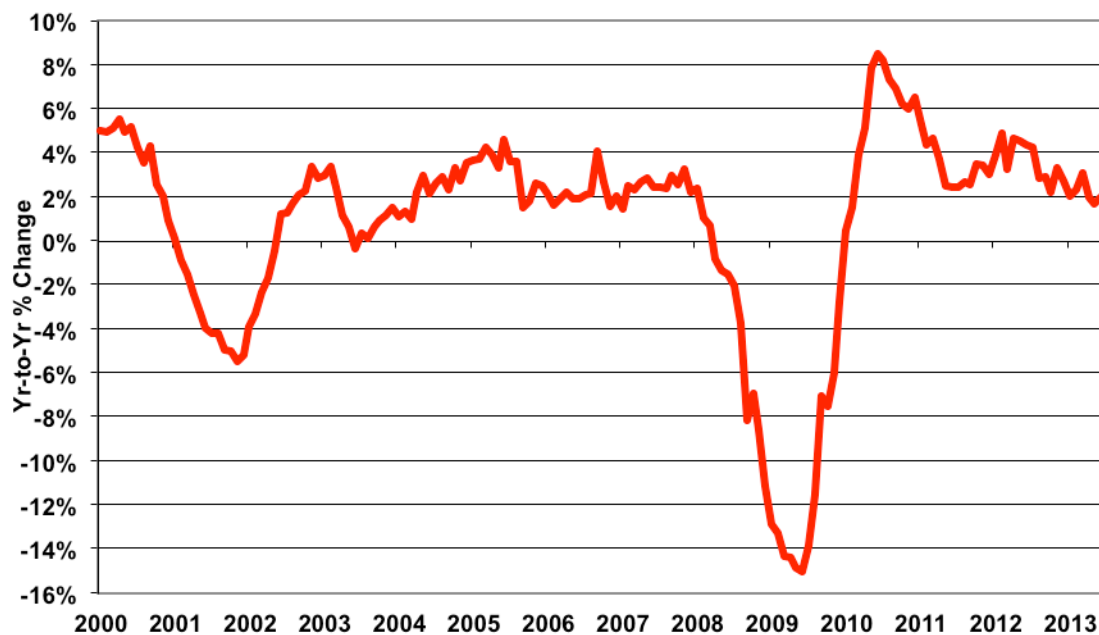
Industrial Production—June 2013. The Federal Reserve Board released its estimate of seasonally-adjusted, June 2013 industrial production this morning, July 16th. In the context of unusually-minimal, prior-period revisions, headline monthly production activity increased by 0.31%, versus an unrevised “unchanged” in May, at the first decimal point, but before the rounding, May was revised to a 0.04% decline at the second decimal point, versus an initial estimate of a 0.04% gain. The headline 0.3% gain in aggregate production reflected a 0.3% gain in manufacturing, a 0.8% gain in mining activity, and a 0.1% decline in utility usage.

Suggestive of a renewed downturn in broad economic activity, year-to-year growth in June was 1.98%, versus a revised 1.69% (previously 1.61%) increase in May. The last time that year-to-year production growth slowed to current levels was at the formal onset of the 2007 recession, as shown in the second graph following.

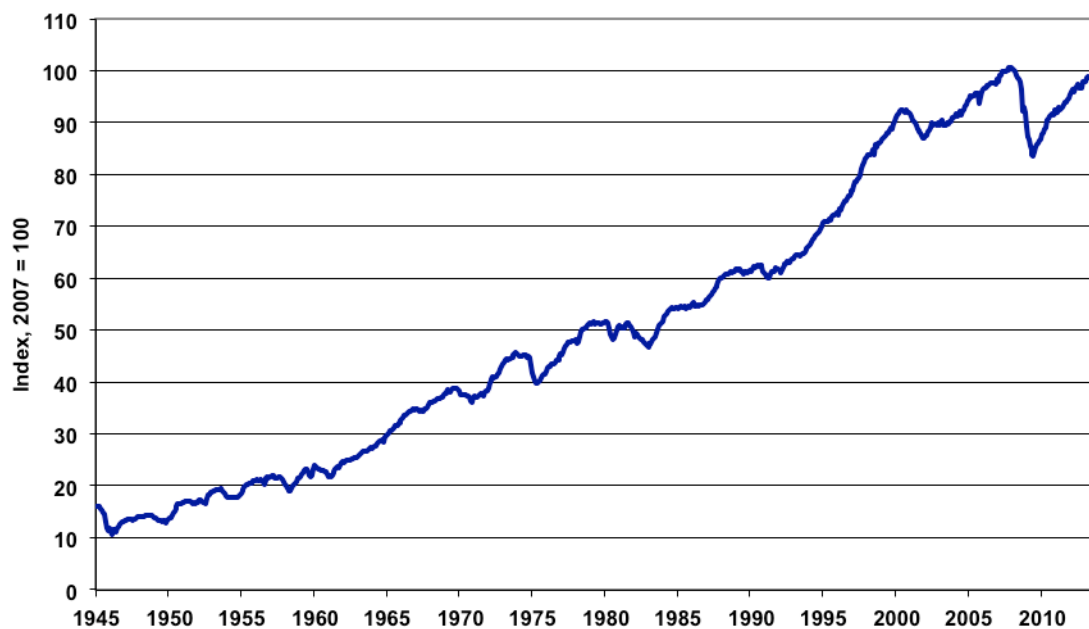
The “recovery” in industrial production is reflected in the following two sets of graphs. The first graph in the first set shows the monthly level of the production index, while the just-referenced second graph shows the year-to-year or annual percentage change in the same series for recent historical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



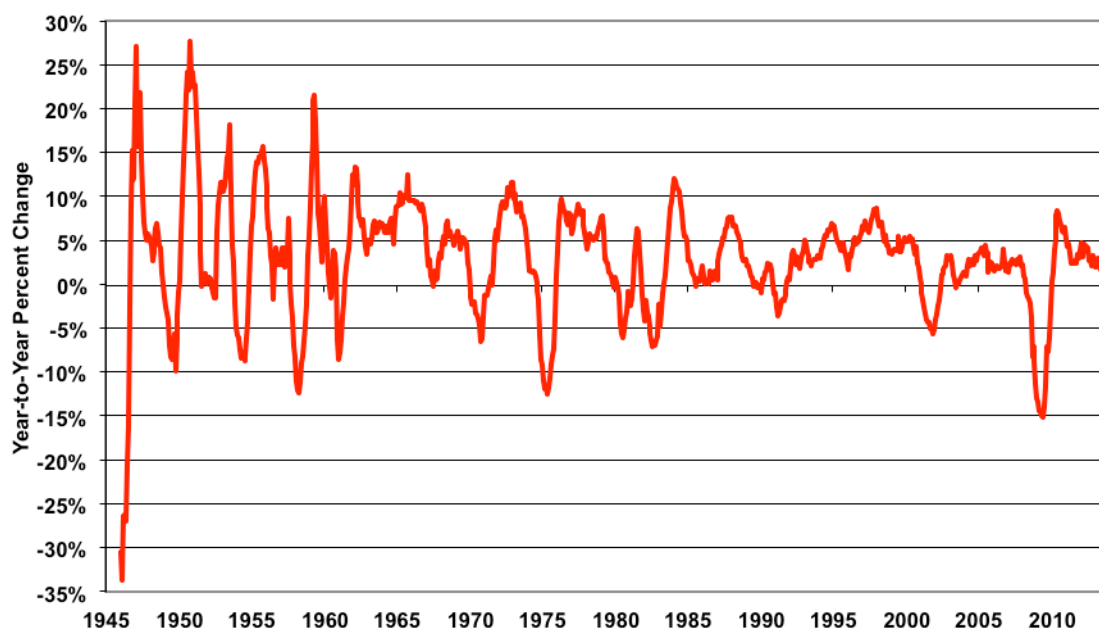
Industrial Production Year-to-Year % Change
Jan 2000 to Jun 2013, Seasonally-Adj. (ShadowStats, FRB)



Index of Industrial Production
To Jun 2013, Seasonally-Adjusted (ShadowStats, FRB)



Index of Industrial Production (Yr/Yr %)
To Jun 2013, Seasonally-Adjusted (ShadowStats, FRB)



As shown more clearly in the first set of graphs, current activity has dipped 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 the 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.

WEEK AHEAD

Weaker Economic and Stronger Inflation Data Are Likely for June and Beyond. *[Except for the underlined text in the Residential Construction detail, this Week Ahead section is unchanged from the prior Commentary.]* Despite the stronger than expected headline payroll numbers for June, the balance of upcoming June economic releases, and beyond likely will disappoint a still overly-optimistic consensus view of the broad economy. Separately, with energy-inflation related seasonal-adjustment factors swinging to the plus-side in June, combined with stable oil and higher gasoline prices for the month, higher inflation headline CPI reporting is likely in June, with higher CPI and PPI in the months ahead.

Reflecting the still-likely negative impact on the U.S. dollar in the currency markets from continuing QE3 and the still-festered fiscal crisis/debt-ceiling debacle (see *Hyperinflation Outlook* section), reporting in the ensuing months and year ahead generally should reflect much higher-than-expected inflation (see [No. 527: Special Commentary](#)).

While expectations for economic data in the months and year ahead should begin to soften, weaker-than-expected economic results still remain likely, given the intensifying structural liquidity constraints on the consumer. Recent downside benchmark revisions to industrial production, new orders for durable goods, retail sales, the trade deficit and construction spending suggest downside revisions to GDP growth of recent years.

Indeed, the pending, big revision event remains 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 shortly.

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*](#).

Residential Construction (June 2013). On Wednesday, July 17th, the Census Bureau will publish its estimate of June 2013 housing starts activity. Despite developing market expectations for a relatively-strong headline gain of about 5%, such a month-to-month increase would be statistically-insignificant, signaling ongoing stagnation or renewed downturn in activity, particularly for single-unit housing starts.

Separately, housing starts likely will show an outright quarterly contraction, as was discussed in [*Commentary No. 534*](#). Assuming no meaningful upside revisions to prior periods, June starts would have to jump by more than 20%, month-to-month, in order to push second-quarter 2013 activity into positive territory relative to first-quarter 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 and does not appear to be in the offing.
