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

COMMENTARY NUMBER 555
August Retail Sales and Producer Price Index

September 13, 2013

Below-Consensus Retail Sales Activity Continues,
With Growth Due to Rising Inflation Not to Rising Demand

Producer Price Index Gain Still Shy of Full Oil-Price Impact

PLEASE NOTE: The next regular Commentary *is scheduled for Monday, September 16th, covering August industrial production, followed by subsequent* Commentaries *on Tuesday, September 17th (July CPI, real retail sales and earnings), and on Wednesday, September 18th (July housing starts). The September 17th release of* Income, Poverty and Health Insurance Coverage: 2012 (The Poverty Report) *will be covered in the* Commentaries *of the 17th and/or 18th, depending on the timing of the release of the data and complexity of the needed analysis.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Early August Economic Releases Were Troubled. Following the report of deteriorating August labor conditions (see *Commentary No. 554*), today's retail sales report provided further indication of a weakening economy. The level of headline retail sales growth in August disappointed market expectations and did not top market expectations for related consumer inflation. Market expectations for the major measures of U.S. economic activity increasingly are taking on the appearance of being perpetually overly optimistic.

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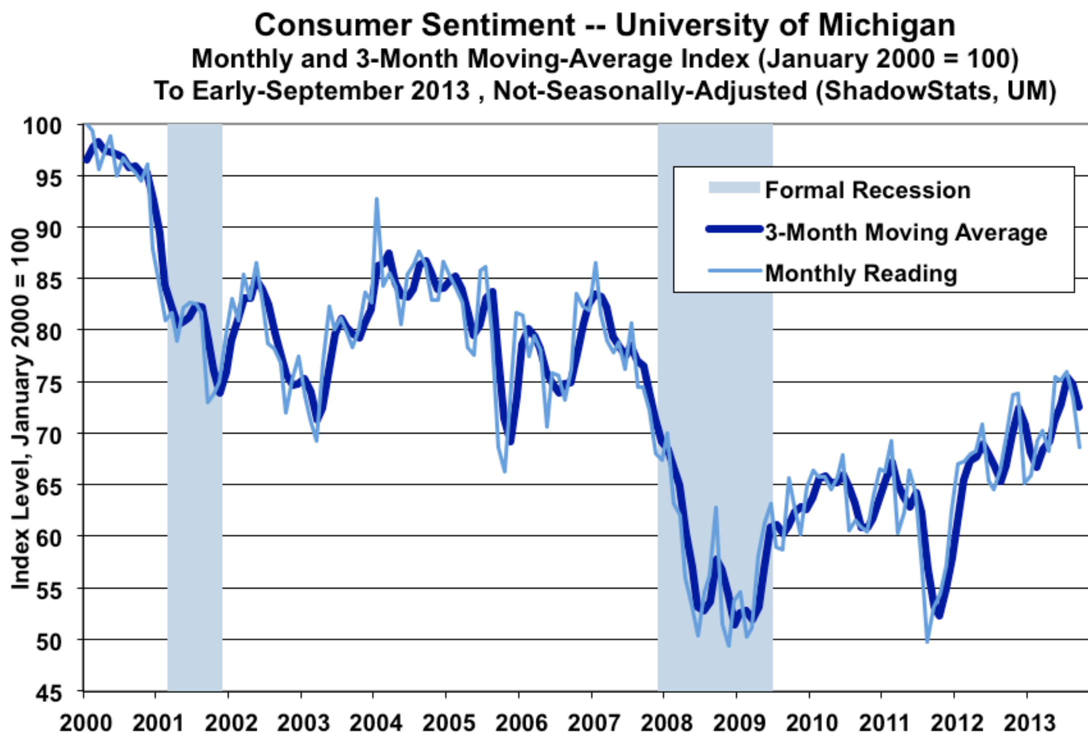
At the same time, the August producer price index exceeded expectations for finished goods inflation, even though seasonal factors depressed oil and food prices meaningfully.

Heavy reporting in the week ahead should show further signs of faltering business activity, rising inflation and deteriorating consumer income and liquidity circumstances. Where structural liquidity problems continue to constrain consumer activity and broad economic growth, some updated detail will be available from the latest *Poverty Report* (2012 data), discussed below and the *Week Ahead*.

Accordingly, consumer liquidity issues are updated in these *Opening Comments*, followed by summaries of the reporting on August retail sales and the producer price index. The *Hyperinflation Outlook* will be updated with the September 18th *Commentary.*

Broad Economy Still Is Dependent on Consumer Liquidity. As discussed in *Commentary No. 552* and updated here and in *Commentary No. 553*, sustainable growth in retail sales and personal consumption is not possible without parallel growth in consumer income and liquidity. Inflation-adjusted median household income is not growing, and without the availability of normal debt expansion and with an ongoing lack of willingness for the consumer to spend or to take on new debt, there is no economic recovery in place or pending.

Reflecting the latest detail are two graphs. The first is of the University of Michigan's consumer sentiment series, as of its preliminary estimate for September. The second is of consumer credit outstanding, as updated through July by the Federal Reserve Board.



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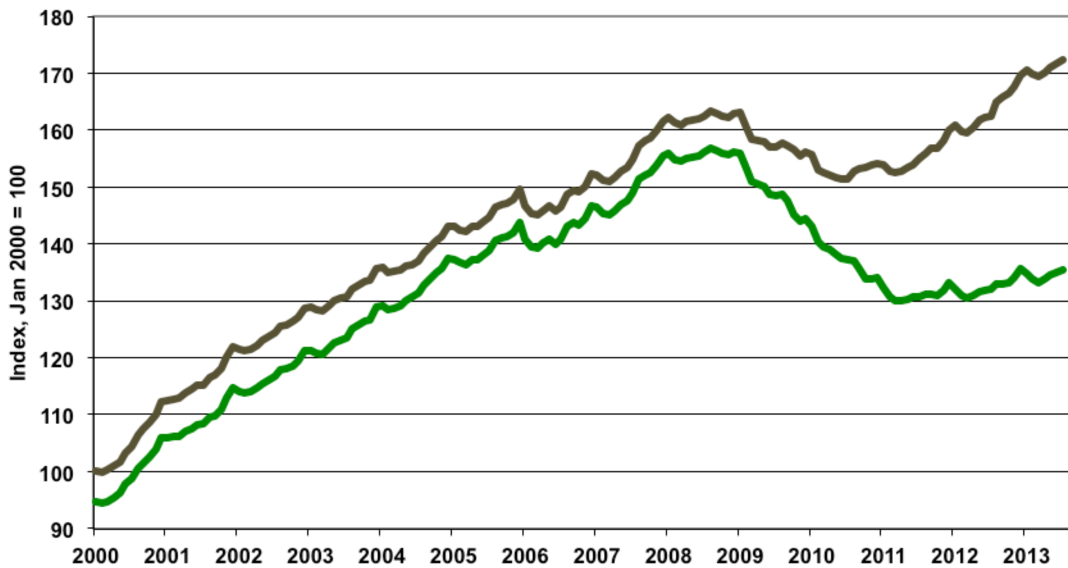
The graph reflecting the University of Michigan's early-September consumer-sentiment measure shows renewed downturn. Despite the repeated upticks in the series and subsequent declines or flattening, the mood of consumers remains at levels commonly seen in post-World War II recessions, not in expanding recoveries, as touted with the regular GDP reporting.



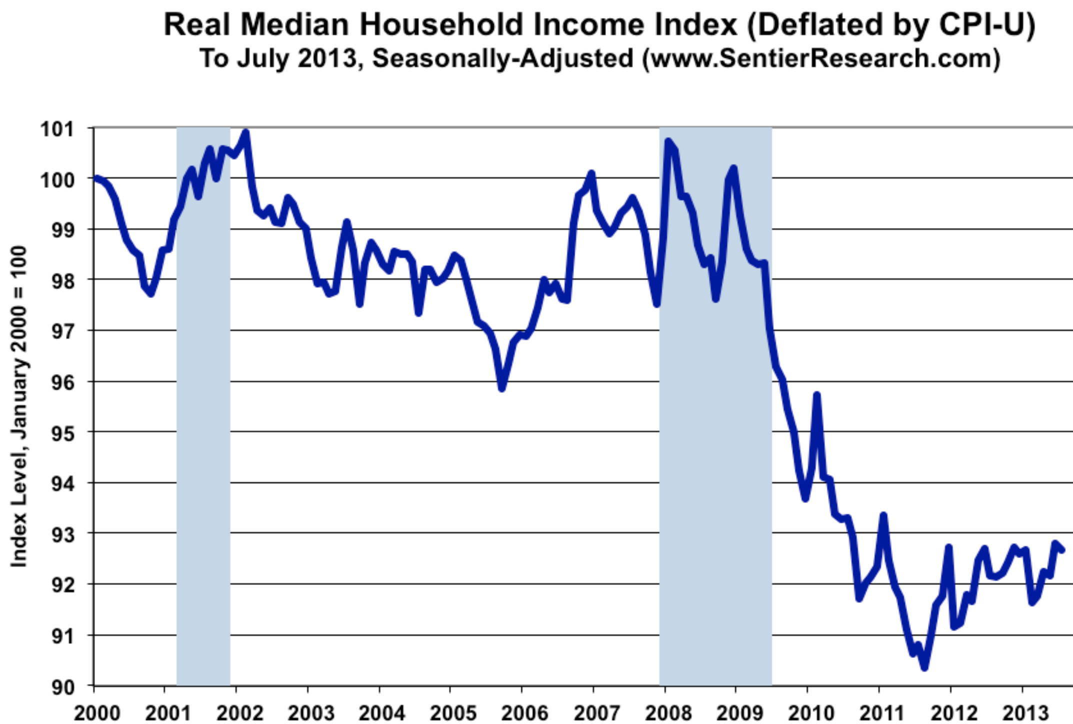
The second graph shows the estimate of July 2013 consumer credit outstanding from the Federal Reserve. As has been the case for the full post-2008 financial-panic period, nearly all the growth seen in this series has been due to the expansion of federally-owned student loans, not in bank lending to consumers that otherwise could help to fuel broad consumer activity. The lack of regular bank lending into the regular flow of commerce continues as an indicator of ongoing solvency and liquidity issues within the U.S. banking system.

Income Problems Should Remain Evident in the Upcoming Poverty Report. The accompanying graph here is the previously-published (*Commentary No. 553*) estimate of real (inflation-adjusted) median household income (data courtesy of www.SentierResearch.com). It is included as an indicator of what may be seen in the September 17th release of the Commerce Department's *Income, Poverty and Health Insurance Coverage: 2012*.

Discussed in the *Week Ahead* section, the "Poverty Report" is a very heavily politicized document, as to its estimates of people in poverty, its estimates of poverty thresholds, and its unconscionable use of the CPI-U-RS to minimize negative trends in the poverty and income data.

Of significance in the report, however, are the nominal income numbers and estimates of income distribution. Where the Census Bureau will estimate real median household income for the year of 2012, the accompanying graph is of estimates from www.SentierResearch.com of monthly numbers, based on the same series concept, through July 2013. The Census data are deflated annually by the CPI-U-RS. The data in the accompanying graph are deflated by the CPI-U, on a monthly basis. For reasons covered below, for only the post-2000 period of the monthly data, the two deflation series effectively are consistent.

Discussed in the *Public Comment on Inflation*, the CPI-U-RS restates inflation history as though all the revisions to inflation methodologies of recent decades always had been in place. These are the revisions that destroyed the CPI–U as a measure of the cost of maintaining a constant standard of living, and that destroyed the CPI-U as a measure of actual out-of-pocket expenditures. The difference in using the two different approaches to deflating the nominal numbers is that using just the official headline CPI-U for deflation, as the BLS and most economists do, shows that real median household income in 2011 had fallen back to levels seen in the late-1960s and early-1970s. Using the RS-series gimmicks (only Census uses the RS-series), Census shows that real income has grown since the early-1970s, but, even so, reported real income still has fallen since before the 2007 recession.



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Post-2000, the differences between the annual inflation rates in the CPI-U and the CPI-U-RS are nil, since the defining methodological changes largely were pre-2000. Accordingly, the accompanying post-2000 graph of monthly real median household income should look basically the same, deflated by either inflation series, if only the RS-data were available for such purposes on a monthly basis.

To the extent the monthly estimates are reflected in annual activity, the annual real median household income number for 2012 likely will be little changed (either up or down) from 2011, and it should continue to hold below pre-recession levels. The various estimates of income variance or dispersion likely will have deteriorated further in 2012 versus 2011.

Retail Sales—August 2013. The headline 0.2% gain in August retail sales was close to what appears to be the market-consensus outlook for the headline August CPI-U. In what appears to have become a recurring pattern, headline retail sales disappoint market expectations, and then any headline monthly sales growth is offset by an equivalent or greater, headline monthly gain in consumer inflation. With prices driving retail sales, not demand, the economy is not growing in real, or inflation-adjusted, terms.

Despite an upside revision to July reporting, which had the effect of dampening the relative August gain, activity in consumer buying of goods and services remains constrained by the intense, structural-liquidity woes besetting the consumer, as discussed in the preceding section. 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. In like manner, the consumer has lacked the ability to fuel the purported post-June 2009 recovery in economic activity.

Nominal, or not adjusted for inflation, August 2013 retail sales showed a statistically-insignificant, seasonally-adjusted monthly gain of 0.21% (a gain of 0.49% before prior-period revisions). The August increase followed a revised, statistically-significant month-to-month gain of 0.43%. August 2013 real retail sales will be detailed in the September 17th *Commentary* covering the release of the August CPI-U consumer inflation measure. With market expectations developing around 0.2% headline CPI-U inflation, such a result would push the headline nominal retail sales growth of 0.21% to something close to nil.

Year-to-year, nominal August 2013 retail sales rose by a statistically-significant 4.67%, versus a revised 5.73% (previously 5.40%) in July. In normal economic times, the recent levels in annual real growth would have been signaling a pending recession, and August 2013 real year-to-year growth will have moved lower, still, even allowing for the upside revision to the July 2013 data. In the current circumstance, that signal likely will serve as an indicator of a renewed downturn in broad economic activity.

Producer Price Index (PPI)—August 2013: Major Changes Will Create a New PPI Series. The regularly-volatile, headline, seasonally-adjusted finished-goods producer price index (PPI) rebounded in August 2013 by 0.30% (up by 0.41% unadjusted), versus a headline unchanged (down by 0.15% unadjusted) monthly number in July.

August's gain in finished goods reflected a seasonally-adjusted 0.83% (0.92% unadjusted) monthly increase in finished energy costs, and a seasonally-adjusted gain of 0.59% (0.88% unadjusted) in food costs, with no change in month-to-month "core" inflation (net of food and energy) on both a seasonally-adjusted and unadjusted basis. The adjusted monthly gains in both the energy and food categories were muted by constraining seasonal adjustments.

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Unadjusted and year-to-year, August 2013 total finished-goods PPI inflation eased to 1.38%, versus 2.12% in July.

Experimental New Series. With the February 2014 reporting of the January 2014 PPI, the series will go through a major overhaul, redefinition and expansion, as discussed by the BLS at this link *New PPI*. The BLS has just started publishing what the new series and reporting will look like, on an "experimental" basis. For example, the recently published experimental PPI for last month's reporting of July 2013 "final demand goods," appears to be reasonably close to the current "finished goods" estimate published for July, with both the official reporting and experimental reporting showing "unchanged" seasonally-adjusted monthly inflation in July, but with respective 0.8% and 0.6% monthly gains in June.

The separate and new "final demand services" category, which includes trade (change in margins for wholesalers and retailers), transportation and warehousing, among other areas, however, showed a headline gain of 0.5% for July 2013. As a result, the total "final demand" (goods, services and construction which are sold for personal consumption, capital investment, U.S. Government, and export [BLS definition]) were up by 0.4% for the month of July, instead of the currently published, official "unchanged," and with year-to-year July 2013 inflation at 1.9% instead of 2.1%. A comprehensive analysis of the new versus old PPI, including its leading relationship—if any—with the CPI, will be published in a later *Commentary.*

[For further detail on the August retail sales and PPI, see the* Reporting Detail *section.]

HYPERINFLATION WATCH

Hyperinflation Outlook—Unchanged. The next update of the *Hyperinflation Outlook* is planned for the September 18th *Commentary.* This summary has been not been revised since *Commentary No. 550* of August 16th. 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

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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, a fully-updated hyperinflation report is planned in 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. Yet, the talk of ending (or extending/expanding) QE3 still appears to be little more than jawboning, aimed either at placating a growing chorus of Fed critics or at manipulating variously the gold, currency and domestic-stock markets. Indeed, as part of the ongoing mind-games with the public, various Fed officials regularly offer contradictory stories, when the stock market needs a boost or distraction from other concerns, such as pending discord over U.S. fiscal policy.

Underlying economic reality remains much weaker than Fed projections. As actual economic conditions gain broader recognition, market sentiment should shift increasingly 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, 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. These factors, in combination, show the end game to be nearing, and while they may have been in recent summer-holiday hibernation, post-Labor Day political turmoil is imminent.

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, at

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any time, with little or no warning. 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 precedents established in 2008, likely reactions from the government and the Fed would be to throw increasingly worthless money at the intensifying crises, hoping to push the problems even further into the future. Such attempts to save the system, however, all have exceptional inflationary implications.

The global financial markets appear ready to move beyond the forced patience with U.S. policies that had been induced by the financial terror of the 2008 panic. Accordingly, the U.S. dollar faces likely extreme and negative turmoil in the months ahead. A domestic hyperinflationary environment still 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. Despite the happy news from the redefined GDP series that the recession was shallower, and the recovery more rapid, than previously estimated, there still never has been an actual recovery following the economic downturn that began in 2006, and collapsed into 2008 and 2009. No other major economic series has confirmed the pattern of activity now being reported in the GDP.

Instead, what followed was a protracted period of business stagnation that began to turn down anew in second- and third-quarter 2012 (see the corrected GDP graph in the *Opening Comments* section of *Commentary No. 546*). 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 still should gain eventual recognition as the second-dip in a double- or multiple-dip recession, with current reporting in basic economic series coming into synchronization with a renewed downturn in broad economic activity starting in second- and third-quarter 2013.

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. As of August 15, 2013, the Fed had monetized 110% of the net issuance of U.S. Treasury debt, since the beginning of the calendar year.

The Fed's unconscionable market manipulations and games playing in fueling speculation over the future of quantitative easing clearly have been used to move the U.S. dollar (the purpose of initial quantitative easing was U.S. dollar debasement). QE3 and continuing efforts at dollar-debasement are not about to go away. 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. The loss of some reserve

status for the U.S. dollar is likely, as the crises break, and that would intensify both the dollar-selling and domestic U.S. inflationary pressures.

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 soft 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 still 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 have put forth outlines of ten-year budget proposals that remain 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*). Recent reductions reported in the year-to-date cash-based 2013 deficit reflect gimmicks such as the U.S. government declaring itself dividends out of government-backed and controlled Fannie Mae and Freddie Mac. Those dividends also have helped the Treasury operate around the limits of the current debt ceiling. If the government consolidated those entities into its financial statements, as would happen in the corporate world, the deficit position would be much bleaker, as it is otherwise with generally accepted accounting principles or GAAP-based accounting.

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 global markets previously had expressed their extreme discomfort with the unresolved longer-range sovereign solvency issues of the United States, by dumping dollars at the time of the failed July/August 2011 fiscal negotiations. The continuing unwillingness and political inability of the current government to address those issues, only pushes along the regular unfolding of events that eventually will trigger a massive flight from the U.S. dollar and a domestic hyperinflation, as discussed in *Commentary No. 491*.

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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 extreme 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 near-term—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.

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REPORTING DETAIL

RETAIL SALES (July 2013)

August Retail Sales Gain—Muted by an Upside Revision to July—Was Little More than Inflation. In what has become something of a recurring pattern, headline retail sales disappoint market expectations, with any headline monthly sales gains being offset by an equivalent, headline monthly gain in consumer inflation. The headline 0.2% gain in August retail sales was close to what appears to be developing as a market-consensus inflation outlook for the September 17th report on the August CPI-U.

Despite an upside revision to July reporting, which had the effect of dampening the relative August gain, activity in consumer buying of goods and services remained constrained by the intense, structural-liquidity woes besetting the consumer, as discussed in the *Opening Comments.* 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.

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In like manner, the consumer has lacked the ability to fuel the purported post-June 2009 recovery in economic activity.

Otherwise, highly variable and unstable seasonal factors have just continued to cloud activity in the June 2013-to-August 2013 period, and in July 2012-to-August 2012, five months that are published on a non-comparable basis with all the other historical monthly numbers. Although the historical numbers were consistent at the time of the May 31st benchmark revision, four intervening rounds of post-revision concurrent-seasonal adjustments have thrown all the historical data into disorder. The resulting inconsistencies allow for unreported shifts in the historical data that most likely 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. 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, as discussed in the Opening Comments *and in* Hyperinflation 2012 *and* Special Commentary (No. 485).

Nominal (Not-Adjusted-for-Inflation) Retail Sales—August 2013. Not adjusted for what likely will be an offset from August consumer inflation (September 17th), today's (September 13th) report on August 2013 retail sales—issued by the Census Bureau—indicated a statistically-insignificant, seasonally-adjusted monthly gain of 0.21% (a gain of 0.49% before prior-period revisions) +/- 0.59% (all confidence intervals are at the 95% level). The August increase followed a revised, statistically-significant month-to-month gain of 0.43% (previously 0.20%) +/- 0.2%.

Year-to-year, August 2013 retail sales rose by a statistically-significant 4.67% +/- 0.78%, versus a revised 5.73% (previously 5.40%) in July. Prior-period revisions, one year ago, reflected little more than the unstable monthly revisions in the concurrent-seasonal-adjustment process, where revised estimates are reported and shown only selectively. Indeed, the pattern of growth here remains distorted by the resulting lack of fully-consistent, seasonally-adjusted numbers being published by the Census Bureau.

Core Retail Sales. Seasonally-adjusted monthly grocery-store sales rose by 0.16% in August, with gasoline-station sales declining by 0.03% for the month. 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:

Version I: August 2013 versus July 2013 seasonally-adjusted retail sales series—net of total grocery store and gasoline station revenues—rose by 0.26%, versus the official gain of 0.21%.

Version II: August 2013 versus July 2013 seasonally-adjusted retail sales series—net of the monthly change in revenues for grocery stores and gas stations—increased by 0.20%, versus the official gain of 0.21%.

Real (Inflation-Adjusted) Retail Sales—August 2013. August 2013 real retail sales will be detailed in the September 17th *Commentary* covering the release of the August CPI-U consumer inflation measure.

With market expectations developing around 0.2% headline CPI-U inflation, such a result would push the headline nominal retail sales growth of 0.21% to something close to nil.

In normal economic times, the recent levels in annual real growth would have been signaling a pending recession, and August 2013 real year-to-year growth will have moved lower, still, even allowing for the upside revision to the July 2013 data. In the current circumstance, this signal likely will serve as an indicator of a renewed downturn in broad economic activity.

PRODUCER PRICE INDEX—PPI (August 2013)

August PPI Rebounded, but the Existing PPI Series Is About to Disappear in a Complete Overhaul and Redefinition. As reported September 13th by the Bureau of Labor Statistics (BLS), the regularly-volatile, headline, seasonally-adjusted finished-goods producer price index (PPI) for August 2013 rose by 0.30% (up by 0.41% unadjusted), versus a headline unchanged (down by 0.15% unadjusted) monthly number in July.

August's gain in finished goods reflected a seasonally-adjusted 0.83% (0.92% unadjusted) monthly increase in finished energy costs, and a seasonally-adjusted gain of 0.59% (0.88% unadjusted) in food costs, with no change in month-to-month "core" inflation (net of food and energy) on both a seasonally-adjusted and unadjusted basis. The seasonally-adjusted monthly gains in both the energy and food categories were muted by seasonal adjustments.

Unadjusted and year-to-year, August 2013 total finished-goods PPI inflation eased to 1.38%, versus 2.12% in July, still remaining well off its 7.08% near-term peak of July 2011.

Experimental New Series. Come the February 2014 reporting of the January 2014 PPI, the series will go through a major overhaul, redefinition and expansion (see the descriptive BLS link: *New PPI*). The BLS has just started publishing what the new series and reporting will look like, on an "experimental" basis.

For example, the recently published experimental PPI for last month's reporting of July 2013 "final demand goods," appears to be reasonably close to the current "finished goods" estimate published for July, with both the official reporting and experimental reporting showing "unchanged" seasonally-adjusted monthly inflation in July, but with respective 0.8% and 0.6% monthly gains in June.

One of the new features is "final demand services," which includes trade (change in margins for wholesalers and retailers), transportation and warehousing, among other categories. The new "services" category showed a headline gain of 0.5% for July 2013. As a result, the total final demand (goods, services and construction which are sold for personal consumption, capital investment, U.S. Government, and export [BLS definition]) were up by 0.4% for the month of July, instead of the currently published, official "unchanged," and with year-to-year July 2013 inflation at 1.9% instead of 2.1%. A comprehensive analysis of the new versus old PPI, including its leading relationship—if any—with the CPI, will be published in a later *Commentary.*

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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 weighting of 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 August 2013, again, the seasonally-adjusted, month-to-month core PPI was unchanged (also unchanged unadjusted), versus an adjusted gain of 0.05% (unchanged unadjusted) in July. Year-to-year, unadjusted August 2013 core finished-goods inflation slowed to 1.15%, from 1.20% in July. A comparison of core-PPI with core-CPI-U year-to-year growth in August 2013 will be graphed in the September 17th *Commentary* covering the August release of the CPI-U.

Intermediate and Crude Goods. Reflecting generally higher average oil prices, although rising at a slower pace than the year before, and reflecting negative seasonal-factor impact, seasonally-adjusted August 2013 intermediate-goods inflation was flat, month-to-month, for a second month, while August crude-goods prices fell by 2.7% for the month, following a 1.2% gain in July.

Year-to-year inflation in unadjusted August 2013 intermediate goods was at a slower 0.5% annual pace than the 1.3% gain reported for July. Year-to-year inflation in August 2013 crude goods slowed to 1.6%, versus an annual gain of 9.3% in July.

WEEK AHEAD

Weaker-Economic and Stronger-Inflation Reporting Remain Likely in the Month and Months Ahead. *[Other than for the section on the pending releases, the balance of this* Week Ahead *section is unchanged from the prior* Commentary.*]* Although there appears to have been some downside adjustment to consensus expectations on the economy, the markets still are overly optimistic. That circumstance and underlying fundamentals that are suggestive of deteriorating business activity, mean that weaker-than-consensus economic reporting should remain the ongoing trend.

Separately, given that energy-inflation-related seasonal-adjustment factors are on the plus-side for a couple of months, combined with stable or higher oil and gasoline prices—exacerbated at the moment by political tensions in the Middle East—stronger-than-expected headline CPI and PPI also are likely for at least the next month or two.

Reflecting the still-likely negative impact on the U.S. dollar in the currency markets, pending from continuing QE3, and the still-festering fiscal crisis/debt-ceiling debacle (see *Hyperinflation Outlook*

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section), reporting in the ensuing months and year ahead generally should reflect much higher-than-expected inflation (see *No. 527: Special Commentary*).

Where market expectations for economic data in the months and year ahead should continue to soften, still-weaker-than-expected economic results remain likely, given the intensifying structural liquidity constraints on the consumer, as discussed in the *Opening Comments*.

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*.

Index of Industrial Production (August 2013). The August 2013 index of industrial production is scheduled for release on Monday, September 13th, by the Federal Reserve Board (FRB). Inventories still are too high for existing demand, and an outright monthly contraction in production remains possible. Minimally, a continuing downside surprise to artificially high expectations is a good bet for August, as are continuing downside revisions to prior-period reporting.

Consumer Price Index—CPI (August 2013). The release by the Bureau of Labor Statistics (BLS) of the August 2013 CPI numbers is scheduled for Tuesday, September 14th. The headline CPI is a fair bet to come in around the developing, positive, market consensus of about 0.2% for headline CPI-U.

Average gasoline prices eased month-to-month in August 2013 by 0.4 percentage point, for a second month, on a not-seasonally-adjusted basis, per the Department of Energy. The BLS seasonal adjustments, however, largely should offset the nominal monthly decline in gasoline prices. As last revised, an unadjusted monthly 7.2% gain in August 2012 gasoline prices was widened to a 7.6% gain, with upside

seasonal adjustments. Similar effects in the August 2013 number would push the unadjusted monthly gasoline price contraction to neutral. Given likely upside inflation pressures from food prices and core inflation, a modest headline gain in August 2013 CPI-U is a reasonable expectation.

Year-to-year, CPI-U inflation would increase or decrease in the August 2013 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.52% increase in monthly inflation reported for August 2012. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for August 2013, the difference in August's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the July 2013 annual inflation rate of 1.96%. For example, if the headline August CPI-U inflation were 0.2%, annual inflation would slow to approximately 1.6% or 1.7%.

2013 Poverty Report (2012 Data). Also due for release on Tuesday, September 17th, sometime after 10 a.m. Washington time, is the Commerce Department's *Income, Poverty and Health Insurance Coverage: 2012*, popularly known as the *Poverty Report*. As discussed more fully in the *Opening Comments* section, the *Poverty Report* is a heavily politicized document, as to its estimates of people in poverty, its estimates of poverty thresholds, and its unconscionable use of the CPI-U-RS to minimize negative historical trends in the poverty and income data.

Of significance in the report, though, are the nominal income numbers and estimates of income distribution, and the Census Bureau will estimate real median household income for the year of 2012. Where annual activity should have some relationsip to estimates of the monthly data discussed in the *Opening Comments,* the annual real median household income number for 2012 likely will be little changed (either up or down), and it should continue to hold below pre-recession levels. The various estimates of income variance or dispersion likely will have deteriorated further in 2012, versus 2011. All these are factors that should confirm the ongoing structural liquidity issues impairing consumer spending.

Residential Construction (August 2013). On Wednesday, September 18th, the Census Bureau will publish its estimate of August 2013 housing starts activity. Despite near-perpetual market expectations for strengthening activity in housing starts, reported month-to-month change likely will continue to be statistically-insignificant, with ongoing stagnation seen in the aggregate series, as well as particularly 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 and still does not appear to be in the offing, again, as discussed in the *Opening Comments*.

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