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

COMMENTARY NUMBER 602
January CPI, Real Retail Sales and Earnings

February 20, 2014

Strongest Signal for a Recession Since September 2007

January Real Retail Sales Activity Plunged by 0.6% for the Month

Unadjusted Monthly January 0.4% CPI Inflation
Squashed to 0.1% by Seasonal Adjustments

January Annual Inflation: 1.6% (CPI-U), 1.7% (CPI-W), 9.2% (ShadowStats)

PLEASE NOTE: The next regular Commentary *is scheduled for Thursday, February 27th, covering GAAP-accounting for the U.S. government, January 2014 existing- and new-home sales, and new orders for durable goods. The GAAP analysis might be published separately on the 26th. A further* Commentary *on the 28th will cover the second estimate, first revision of fourth-quarter 2013 GDP.*

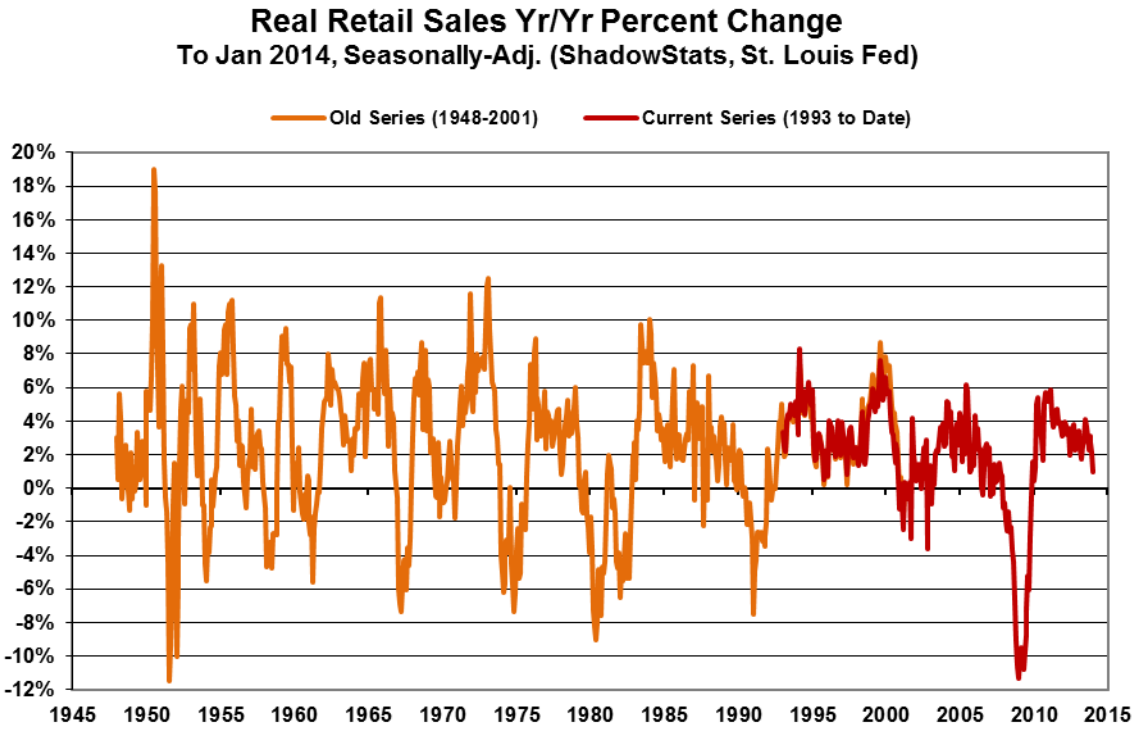
Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Underlying CPI Inflation Picks Up; Economic Activity Is in Decline. Early indications abound of a probable downturn in the current quarter (January through March of 2014). The increasingly likely contraction in headline first-quarter 2014 gross domestic product (GDP) has been signaled by the January 2014 reporting detail on employment (*Commentary No. 598*), industrial production (*Commentary No.*

600), housing starts (*Commentary No. 601*) and retail sales (*Commentary No. 599* and today's *Commentary*). A particular issue has arisen with real retail sales, discussed in today's (February 20th) *Commentary*, along with the consumer price index (CPI).

In addition to the various downside revisions to the economy in prior months and the reporting of weak-to-minus monthly activity in January, real retail sales (inflation-adjusted based on the CPI-U) clearly are signaling a recession. Year-to-year change in the post-World War II series is plotted in the accompanying graph, and generally it has signaled a pending recession whenever growth dropped below 2.0%. It hit 1.0% in January 2014, the strongest recession signal seen since September 2007. The formal recession began in December 2007.



Exceptions to the signal seen in the graph, such as in the mid-1990s, will be discussed in the upcoming *Second Installment* of the hyperinflation report. Where not all economic downturns have been official recessions, the pending downturn appears likely to gain formal recognition as one.

In the inflation arena, unusual seasonal factors helped to contain the reported January headline CPI.

Seasonal Factors Suprressed Headline January 2014 CPI Inflation. In the context of the seasonal-factor revisions that changed previously-reported, monthly headline CPI-U inflation in 2013 by plus or

minus 0.2% in various months, the 0.14% headline, seasonally-adjusted inflation rate for January 2014 seemed a little light, where the unadjusted monthly inflation was 0.37%.

The inflation-suppressing seasonal adjustments were across the board. The headline gain in January 2014 CPI-U of 0.1% was 0.4% unadjusted. The total included aggregate energy inflation up at an adjusted 0.6% pace, but that was an unadjusted 2.1% gain. In the other major CPI sectors, adjusted food inflation increased by 0.1%, but that was up by 0.4%, unadjusted, while "core" inflation rose by an adjusted 0.1%, which otherwise was a 0.2% unadjusted gain.

There was a time when the Bureau of Labor Statistics (BLS) used very heavy seasonal adjustments to temper headline January inflation, where many firms set regular annual price hikes for January 1st. That behavior, however, appears to have changed markedly in recent years, with much less of a need for related seasonal adjustments. The seasonal-adjustment modeling system has gone awry, and that also will be discussed in the upcoming *Second Installment* to the hyperinflation report.

Beyond the regular revisions to the seasonal adjustments, there also was the annual two-year reweighting of the not-seasonally-adjusted chain-weighted CPI-U.

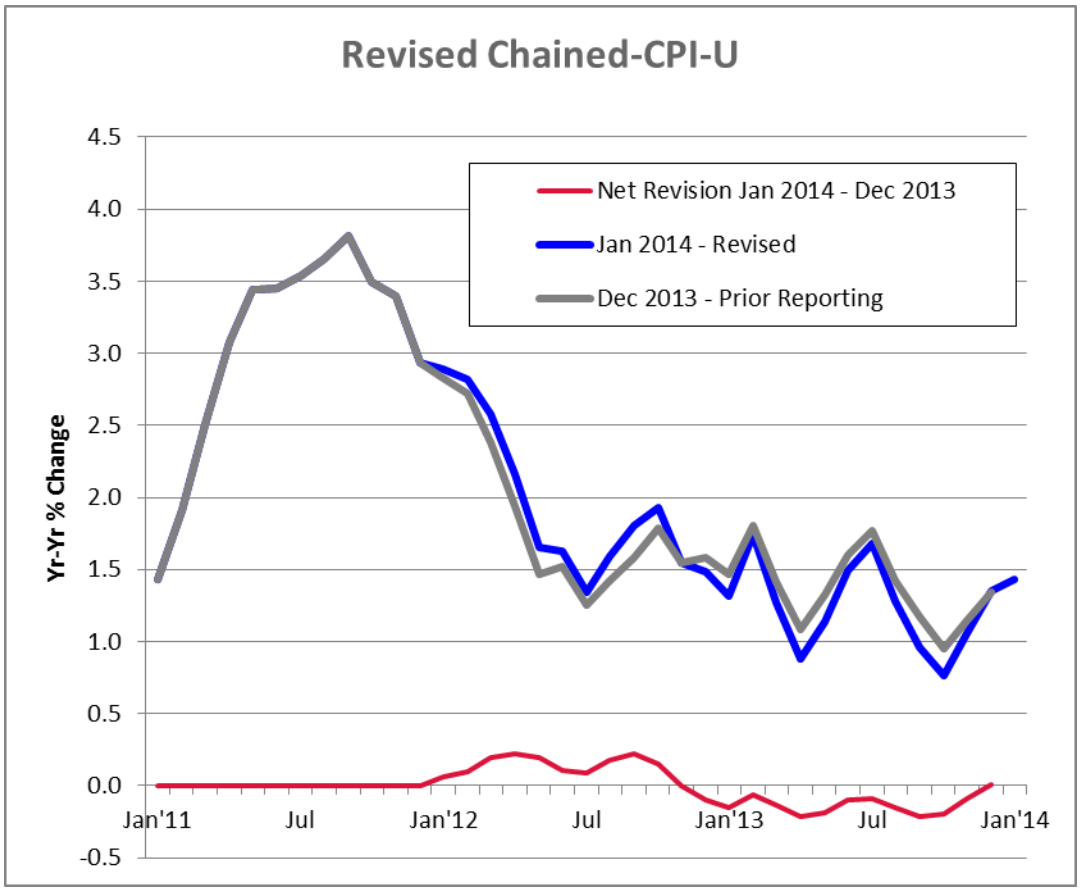
As Currently Constructed, the Chain-Weighted CPI Would Not Work Well as a COLA. As discussed frequently here, the politicians who sometimes look to talk about actually reducing the federal budget deficit have suggested changing the inflation measure used in calculating cost-of-living-adjustments (COLA), so as to reduce COLAs. A once popular idea was to use some form of a Chain-Weighted CPI-U (C-CPI) to replace the CPI-W in calculating COLAs for programs such as Social Security. A chain-weighted index understates inflation for COLA purposes, because it measures inflation where the substitution of goods is allowed in the measured basket of goods and services, instead of using the traditional fixed-weight basket of goods and services.

With a fixed-weight basket, the COLA reflects maintaining a constant standard of living. With the chain-weighted approach, a substitution-based basket lowers the reported level of inflation, where it reflects the lower costs of people having to buy hamburger, because steak has become too expensive. Most people living with the effects of inflation prefer the fixed-basket or constant-standard-of living measure (see the *Public Comment on Inflation*), where they are able to continue eating the desired amount of steak, as opposed to having to shift to consuming more hamburger.

Beyond the question as to how to define a COLA, there is a significant functional difference between the C-CPI and the regular CPI (CPI-U, CPI-W) measures. The not-seasonally-adjusted CPI numbers never are revised. Accordingly, contracts, agreements, legislation, etc., based on an unadjusted CPI measure for a particular month, quarter or year, are dealing with a fixed number. The C-CPI, however, only realizes the bulk of its "savings" for the government, versus other measures, after two years of revisions to the substitution weightings, which currently take place with January reporting.

In the accompanying graph, courtesy of ShadowStats affiliate www.ExpliStats.com, today's release of the 2012 and 2013 revisions showed changes to the C-CPI-U moving in opposite directions, with the second revision to 2012 raising the average annual inflation rate by 0.12% (it had been revised lower in the initial revision), versus the first revision to the 2013 average annual inflation rate revising lower by 0.13%. The lack of a timely, fixed benchmark inflation rate makes the use of any such measure for financial purposes unnecessarily uncertain, complex and difficult.

The simplest approach for those in Washington, who wish to reduce or increase COLA adjustments, simply is to take an established CPI benchmark and subtract or add to that annual inflation reporting in order to get the desired number and spending effect. At least everyone knows what is being done there, rather than the government playing political games with bad-quality headline inflation reporting, as otherwise has been the case for decades. Again, see the *Public Comment on Inflation* and the ShadowStats-Alternate CPI measures.



Headline Reporting – CPI-U. The headline, seasonally-adjusted CPI-U for January 2014 rose by 0.14%. Net of prior-period revisions, that headline monthly gain would have been 0.15% (0.1496%), just shy of rounding up to a 0.2% headline gain. On a not-seasonally-adjusted basis, the January 2014 CPI-U was up by 0.37% for the month.

Due to the annual revision of five years of seasonally-adjusted CPI data—unadjusted data never are changed—headline December 2013 CPI-U rose by a downwardly-revised seasonally-adjusted 0.24% (unchanged on an unadjusted basis), versus an upwardly-revised 0.11% gain (down by 0.20% unadjusted) in November. The two biggest, seasonally-adjusted headline CPI-U inflation revisions in the last year were 0.21% to the upside, from -0.37% to -0.16%, in April 2013, and 0.16% to the downside, from 0.48%

to 0.32%, in June 2013. Where the monthly headline revisions were seasonal-factor related, they tended to balance out over the period of a year.

The impact of those revisions is seen in the current reporting of real retail sales and real earnings, discussed later. Most contract or wage indexing is tied to the unrevised unadjusted levels, as is the usual calculation of year-to-year inflation.

Not seasonally adjusted, January 2014 year-to-year inflation for the CPI-U was a gain of 1.58%, versus 1.50% in December.

CPI-W. The January 2014 headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.14% in January (up by 0.38% unadjusted), versus a downwardly-revised 0.28% gain in December (up by 0.02% unadjusted). Unadjusted, January 2014 year-to-year CPI-W inflation was 1.55%, versus 1.45% in December 2013.

Chained-CPI-U. The initial reporting of unadjusted year-to-year inflation for the January 2014 C-CPI-U was 1.43%, up from a revised 1.38% (previously 1.34%). The revisions here were in annual adjustments to the weighting of the surveyed basket of goods and services, as discussed and graphed earlier in this section.

Alternate Consumer Inflation Measures. Adjusted to pre-Clinton methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual CPI inflation was roughly 5.0% in January 2014, the same as in December 2013. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, rose to about 9.2% (9.17% for those using the second decimal point) in January 2014, versus 9.1% in December.

Real (Inflation-Adjusted) Retail Sales—January 2014. As covered in *Commentary No. 599*, the nominal monthly decline of 0.41% in headline January 2014 retail sales, a revised December 2013 decline of 0.12%, and a revised 0.26% gain for November, all were before accounting for inflation.

Based on today's reporting of a 0.14% headline gain in the January 2014 CPI-U, and incorporating seasonal-adjustment revisions to prior CPI-U adjusted headline data, seasonally-adjusted real retail sales fell month-to-month by 0.55% in January 2014, following a revised 0.36% (previously 0.07%) decline in December, and a revised 0.15% (previously 0.40%) gain in November.

Year-to-year growth in January 2014 real retail sales skidded to a 0.99% gain, down from revised 2.08% (previously 2.57%) annual growth in December, and from 2.77% (previously 2.96%, initially 3.43%) in November, as reflected in the graphs of the *Reporting Detail* section and in the first graph at the beginning of these *Opening Comments*. In normal economic times, the current level of annual real growth in retail sales would signal imminent recession. This meaningfully increases chances for an outright contraction in the current quarter's economic activity.

No Recovery in GDP or Real Retail Sales. Also as noted in *Commentary No. 599*, 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 in continued real earnings difficulties, discussed shortly—these data should continue to trend meaningfully lower, in what will gain recognition as a formal new recession or a double-dip recession.

That said, GDP expanded beyond pre-recession levels twelve quarters ago, starting in second-quarter 2011, and it has kept rising, well beyond the reported activity of any other series, including real retail sales and industrial production. There is no other major economic series showing the GDP's pattern of both official, full recovery and extensive new growth. While real retail sales tend to lead the GDP, the "recovery" in retail reporting lagged the purported GDP recovery by two years. In like manner, the industrial production measure—a coincident GDP indicator—broke above its pre-recession high in November 2013 reporting, but has been falling back as of January 2014 reporting.

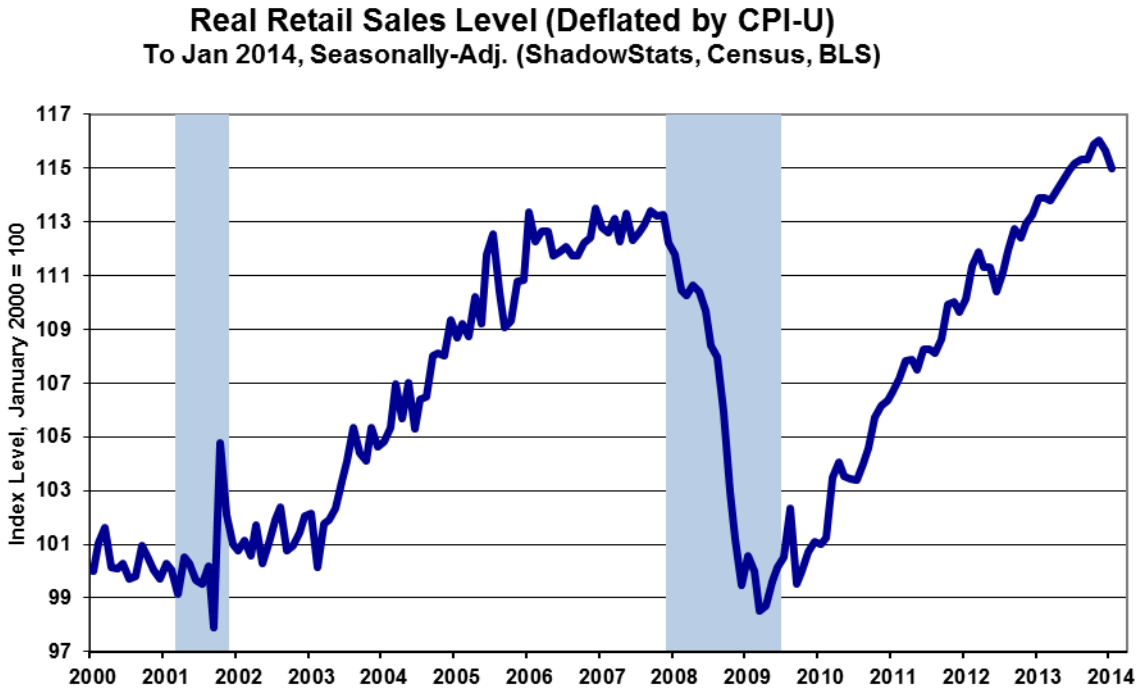
The apparent recoveries in the real retail sales series and industrial production (as well as in the GDP) are due to the understatement of the rate of inflation used in deflating retail sales and other series. As discussed more fully in *Hyperinflation 2012* and *Special Commentary (No. 485)*, and as will be updated in the *Second Installment* of the hyperinflation report, deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

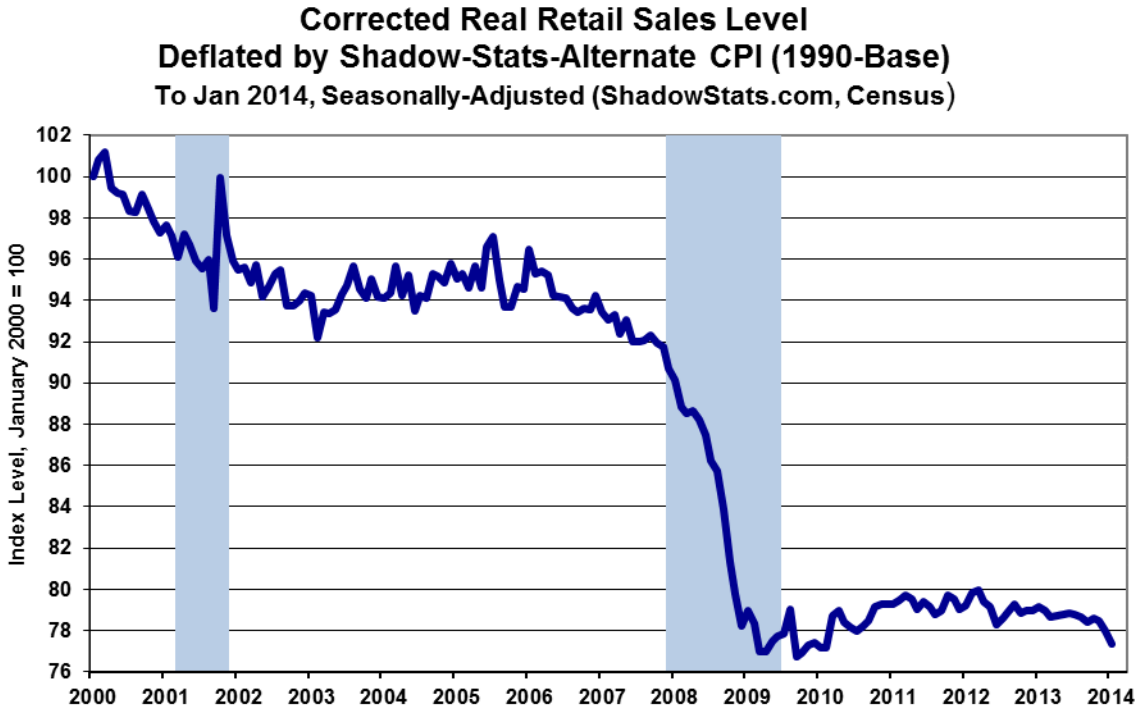
As shown in the latest "corrected" real retail sales graph, with the deflation rates corrected for understated inflation, the recent pattern of real sales activity has turned increasingly negative. The corrected graph shows that the post-2009 period of protracted stagnation ended, and a period of renewed contraction began in second-quarter 2012.

Corrected Retail Sales. The first graph following 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 January 2014 CPI-U and nominal retail sales releases. 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 sales 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, unemployment and housing statistics. A topping out in late-2011 and early-2012 reverted to renewed decline in second-quarter 2012 in this series, which had been bottom-bouncing along a low-level plateau of economic activity since the economic collapse from 2006 into 2009. The renewed contraction has been deepening in the most recent reporting.



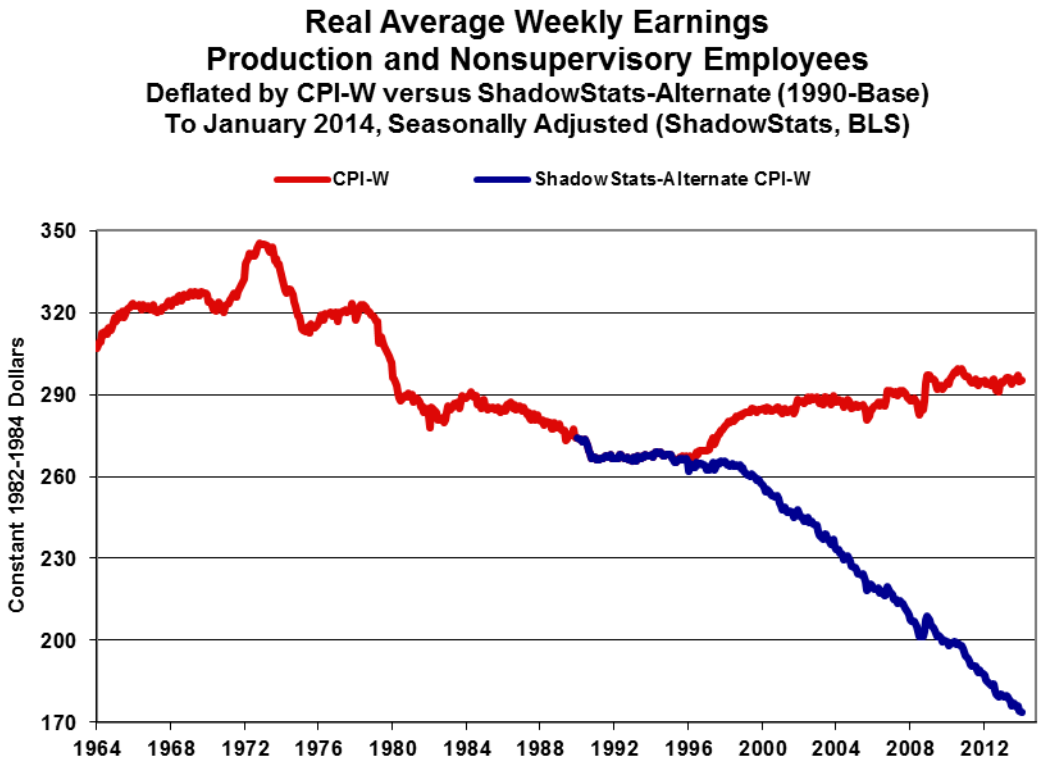


Real Average Weekly Earnings Rose Minimally in January, Following Downwardly-Revised December. Today's release of real (inflation-adjusted) average weekly earnings for January reflected changes from the annual revision to the seasonally-adjusted CPI-W inflation used in deflating the earnings data, as well as from annual seasonal-adjustment revisions to the earnings numbers themselves. In the production and nonsupervisory employees series—the only series for which there is a meaningful history—headline real average weekly earnings (again, deflated by the CPI-W) rose by 0.16% for the month of January 2014, following a revised 0.73% (previously 0.49%) plunge in December 2013.

Unadjusted and year-to-year, January 2014 real earnings growth rose to 0.38%, from a downwardly revised 0.15% (previously 0.44%) annual gain in December 2013. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility. Prior-period revisions usually are due to the instabilities in the BLS monthly surveys.

The accompanying graph of this series 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.



[For greater detail on the January 2014 CPI, real retail sales and earnings, see the* Reporting Detail *section.]

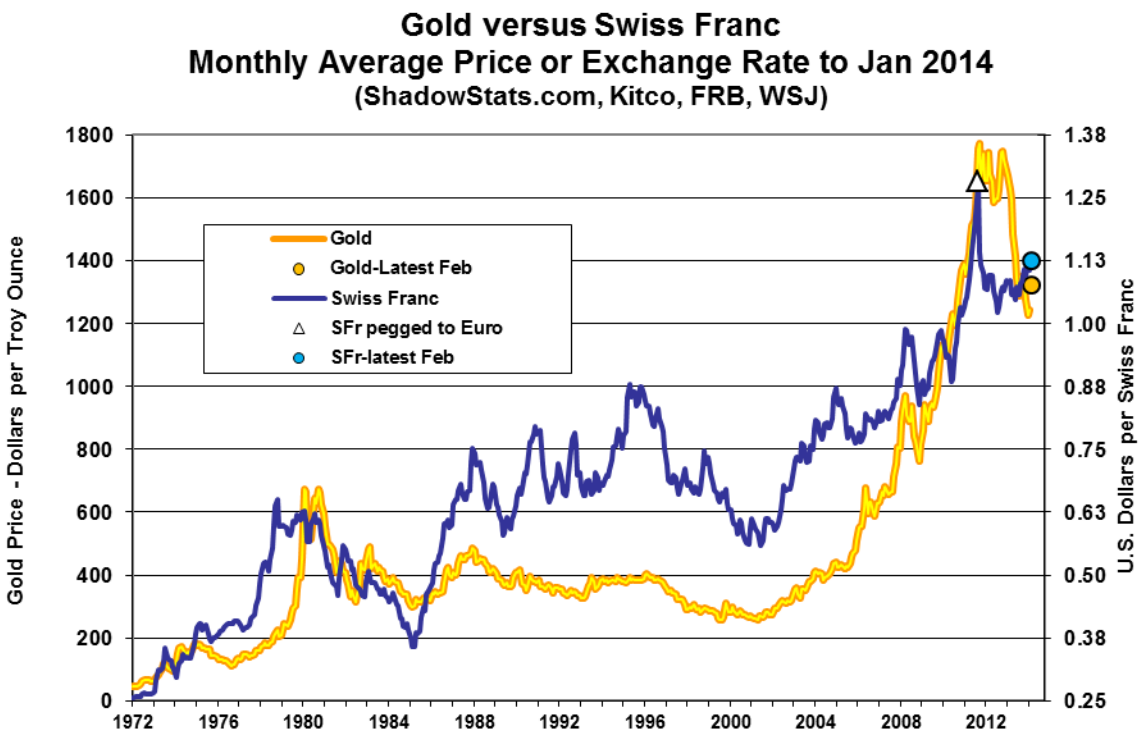
HYPERINFLATION WATCH

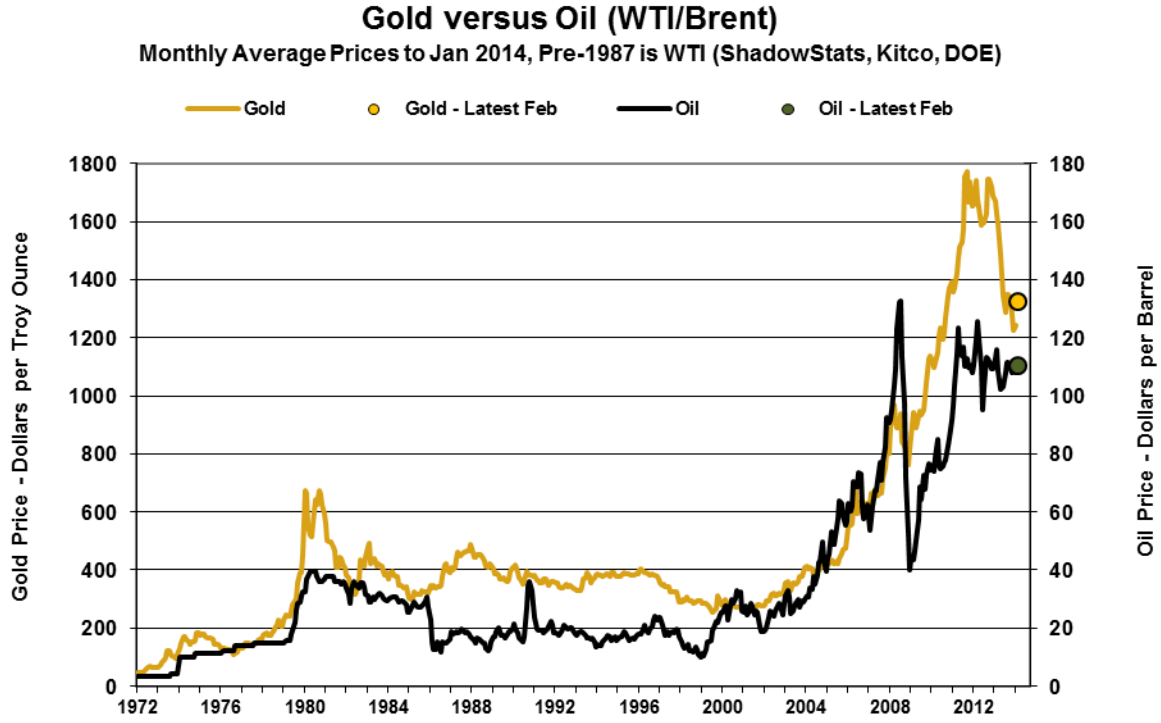
Hyperinflation Outlook. With the *First Installment* of *Hyperinflation 2014—The End Game Begins* published on January 7th, a new *Hyperinflation Summary* for this section will be added in conjunction with the publication of the *Second Installment*. The second and final installment will cover historical and prospective economic activity, as well as possible protective and preventative actions and reactions at both a personal and federal level, versus the unfolding circumstance. It will be published following the analysis of the much-delayed publication of the 2013 GAAP-based financial statements of the United States government, which currently are due for release next week, on February 26th. The new material in the *Second Installment* will supplement and update the basic material already available to ShadowStats readers in Chapters 4, 5 and 9 of *Hyperinflation 2012*.

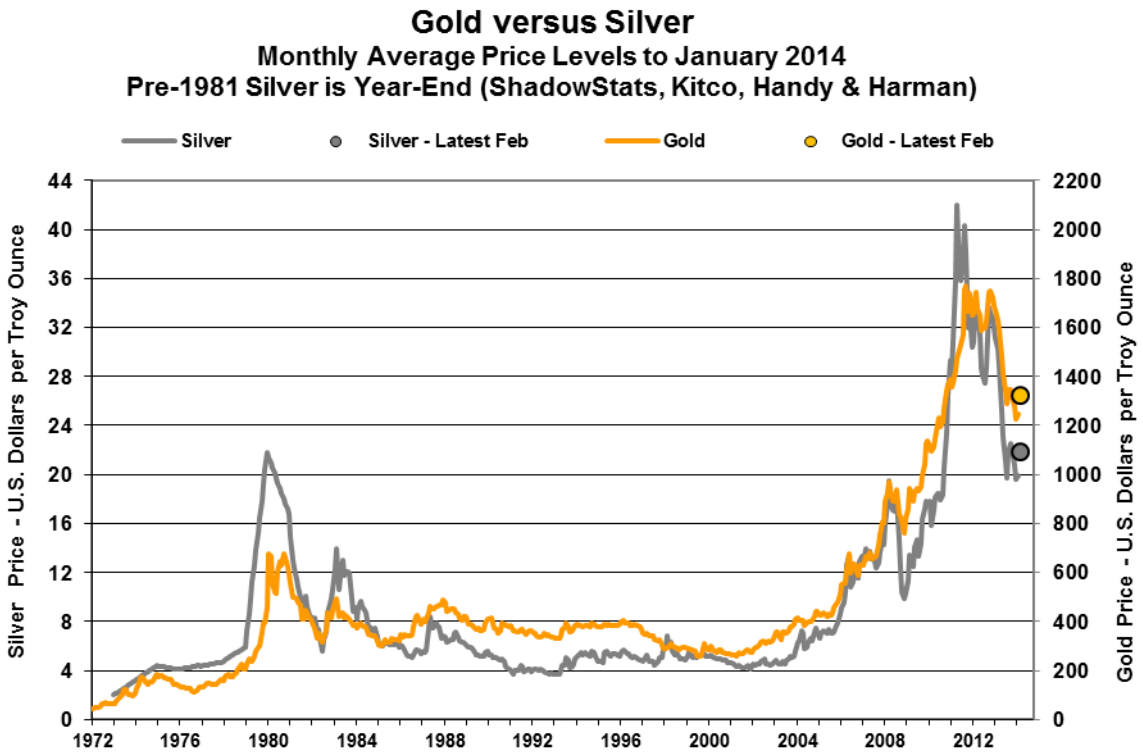
Monthly Gold Graphs. Following are the regular graphs of gold prices versus the Swiss franc, oil prices and silver prices that usually accompany the *Commentary* on the monthly CPI release. Turmoil in the markets has continued, with the dollar showing new softness, along with some rebound in the prices of precious metals. As discussed in *Hyperinflation 2014—The End Game Begins*, the underlying fundamentals could not be much weaker for the U.S. dollar, and they could not be stronger for gold and silver, irrespective of recent price movements. Oil price volatility partially has reflected shifting political circumstances in the Middle East, but oil prices face significant, further upside pressure as the U.S. dollar comes under heavier selling pressure.

Renewed market turmoil surrounding worsening economic activity, fiscal and monetary instabilities, and deteriorating political conditions in the Nation's capital, all should be poison to the markets. The U.S. dollar remains a good bet to be an early casualty; precious metals and oil prices should benefit.

The "latest February" points in the following graphs reflect conditions as of roughly late-afternoon New York time, February 20th.


Gold versus Swiss Franc
Monthly Average Price or Exchange Rate to Jan 2014
(ShadowStats.com, Kitco, FRB, WSJ)
Gold
Gold-Latest Feb
Swiss Franc
SFr pegged to Euro
SFr-latest Feb
Gold Price - Dollars per Troy Ounce
U.S. Dollars per Swiss Franc
1800
1600
1400
1200
1000
800
600
400
200
0
1.38
1.25
1.13
1.00
0.88
0.75
0.63
0.50
0.38
0.25
1972
1976
1980
1984
1988
1992
1996
2000
2004
2008
2012


Gold versus Oil (WTI/Brent)
Monthly Average Prices to Jan 2014, Pre-1987 is WTI (ShadowStats, Kitco, DOE)
Gold
Gold - Latest Feb
Oil
Oil - Latest Feb
Gold Price - Dollars per Troy Ounce
Oil Price - Dollars per Barrel
1800
1600
1400
1200
1000
800
600
400
200
0
180
160
140
120
100
80
60
40
20
0
1972
1976
1980
1984
1988
1992
1996
2000
2004
2008
2012



REPORTING DETAIL

CONSUMER PRICE INDEX—CPI (January 2014)

Seasonal Factors Reduced Headline January CPI-U to 0.1% from 0.4%. In the context of seasonal-factor revisions that changed prior reporting of monthly headline CPI-U inflation in 2013 by plus or minus 0.2%, in various months, the 0.14% headline, seasonally-adjusted inflation rate for January 2014 seemed a little light, where the monthly inflation was 0.37%, unadjusted.

The seasonal-factor inflation suppressant was across the board. The headline gain in January 2014 CPI-U of 0.1% (up by 0.4% unadjusted) included aggregate energy inflation up by an adjusted 0.6% (an unadjusted 2.1% gain). In the other major CPI sectors, adjusted food inflation was up by 0.1% (up by 0.4% unadjusted), while "core" inflation rose by an adjusted 0.1% (up by 0.2% unadjusted).

Going forward, as discussed in *Hyperinflation 2014—The End Game Begins*, risks of a massive flight from the U.S. dollar, favor resulting upside energy inflation driving headline consumer inflation much

higher. The dollar problems could break at any time, with little warning. Renewed financial-market turmoil surrounding fiscal and monetary instabilities, worsening economic activity, and deteriorating political conditions in the Nation's capital, all should pummel the U.S. dollar. Ongoing economic and financial-system-liquidity crises still threaten systemic instabilities that, as with their 2008 Panic precursors, cannot be contained without further, official actions that have serious inflation consequences.

As a separate issue, inflation—as generally perceived by the public, from the standpoint of personal income or investment use—continues to run well above any of the government's rigged price measures. Related methodological changes to the CPI series in recent decades 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, February 20th, that the headline, seasonally-adjusted CPI-U for January 2014 rose by 0.1% (0.14% at the second decimal point). Net of prior-period revisions, the headline monthly gain would have been 0.15% (0.1496%), just shy of rounding

up to a 0.2% headline gain. On a not-seasonally-adjusted basis, the January 2014 CPI-U was up by 0.37% for the month.

Due to the annual revision of five years of seasonally-adjusted CPI data—unadjusted data never are changed—headline December 2013 CPI-U rose by a revised seasonally-adjusted 0.24% (previously 0.30%, and unchanged on an unadjusted basis), versus a revised 0.11% (previously 0.03%) gain (down by 0.20% unadjusted) in November. The two biggest, seasonally-adjusted headline CPI-U inflation revisions in the last year were 0.21% to the upside, from -0.37% to -0.16%, in April 2013, and 0.16% to the downside, from 0.48% to 0.32%, in June 2013. Where the monthly headline revisions were seasonal-factor related, they tended to balance out over the period of a year.

The impact here of those revisions is seen in the current reporting of real retail sales and real earnings, discussed later. Most contract or wage indexing is tied to the unrevised unadjusted levels, as is the usual calculation of year-to-year inflation.

Monthly Gasoline Prices. The BLS used a gain of 1.4% in not-seasonally-adjusted gasoline prices, instead of the lower 1.0% increase indicated by the more-comprehensive, industry-based surveying of the Department of Energy. With heavily-negative seasonal adjustments, the unadjusted gain in gasoline prices was turned into a seasonally-adjusted 1.0% monthly contraction. Seasonal adjustments also were negative for monthly food and the headline "core" inflation.

Major CPI Groups. Encompassed by the headline gain in January 2014 CPI-U of 0.1% (up by 0.4% unadjusted), aggregate energy inflation in January was up by an adjusted 0.6% (an unadjusted 2.1% gain) for the month. In the other major CPI sectors, adjusted food inflation was up by 0.1% for the month (up by 0.4% unadjusted), while "core" inflation rose by an adjusted 0.1% (up by 0.2% unadjusted).

Year-to-Year CPI-U. Not seasonally adjusted, January 2014 year-to-year inflation for the CPI-U was a gain of 1.58%, versus 1.50% in December.

Year-to-year, CPI-U inflation would increase or decrease in next month's February 2014 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.35% increase in the monthly inflation reported for February 2013. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for February 2014, the difference in February's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the January 2014 annual inflation rate of 1.58%.

Core CPI-U. Seasonally-adjusted January 2014 "core" CPI-U inflation (net of food and energy inflation) rose by 0.13% (0.16% unadjusted), versus a revised 0.10% (previously up by 0.11%, fell by 0.10% unadjusted) in December. Year-to-year "core" inflation was 1.62% in January 2014, versus 1.72% in December 2013. The usual PPI "core" inflation comparison graph will resume next month, with revamped PPI numbers.

CPI-W. The January 2014 headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.14% in January (up by 0.38% unadjusted), versus a revised 0.28% gain in December (previously up by 0.34% for the month, and up by 0.02% unadjusted). Unadjusted, January 2014 year-to-year CPI-W inflation was 1.55%, versus 1.45% in December 2013.

Chained-CPI-U. The initial reporting of unadjusted year-to-year inflation for the January 2014 C-CPI-U was 1.43%, up from a revised 1.38% (previously 1.34%). The revisions here were in annual adjustments to the weighting of the surveyed basket of goods and services. See revision detail and comments in the *Opening Comments*.

[The balance of the C-CPI-U discussion is unchanged from the prior Commentary *covering the CPI.]* The recent, two-year budget deficit agreement (see *Commentary No. 581*) cut cost-of-living adjustments (COLA) for certain military retirees by one-percent. The Congressional negotiators did not use the Chained-CPI as had been threatened otherwise for Social Security, etc., where the idea had been that the chained series would cut COLAs by about one-percent on an annual basis, versus existing calculations. The approach taken is more open about what is being done, as opposed to the prior subterfuge of trying to pass off a fully-substitution-based CPI as a legitimate COLA measure.

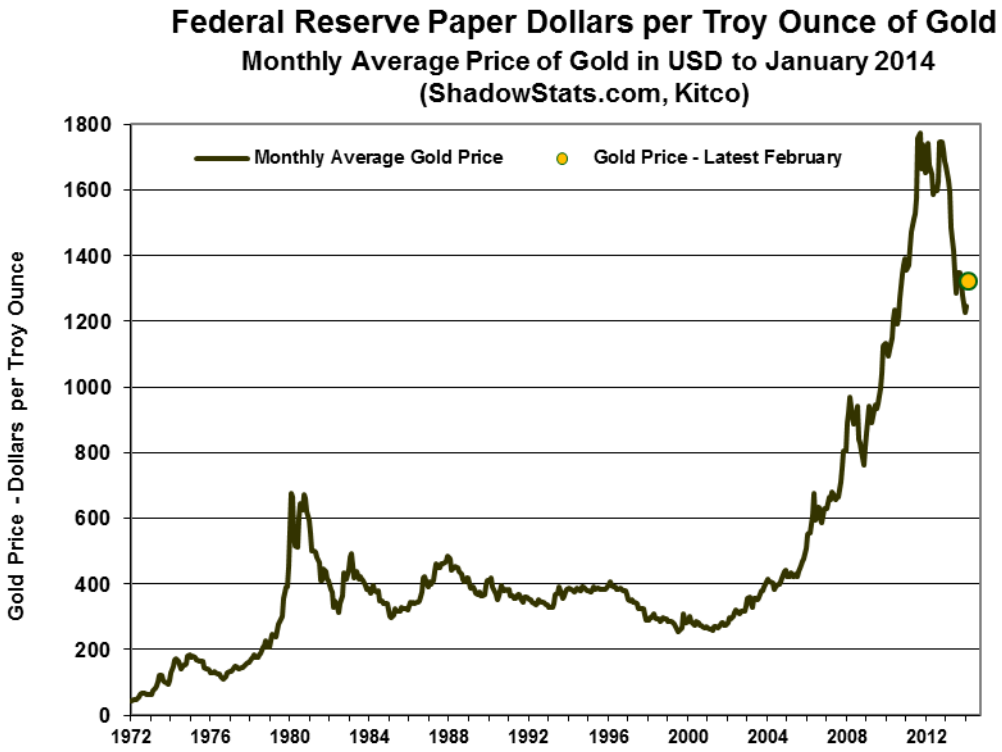
The Chained-CPI-U currently is not designed as a benchmark cost-of-living indicator, with the series subject to revisions for two years, before the inflation-rate reduction is realized fully. Despite White House and Congressional considerations of making the chained index the new cost-of-living-adjustment (COLA) measure for programs such as Social Security, the system cannot be made workable as a concept for using a substitution-based CPI measure as a COLA, without the new index becoming even more of a sham than it already is. For further detail, see the *Public Commentary on Inflation Measurement and Chained-CPI*), and the C-CPI material posted on the BLS site, apparently in anticipation possible 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 5.0% in January 2014, about the same as in December 2013. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, rose to about 9.2% (9.17% for those using the second decimal point) in January 2014, versus 9.1% in December.

[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 $2,555 per troy ounce, based on January 2014 CPI-U-adjusted dollars, and $10,601 per troy ounce, based on January 2014 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 January 2014 CPI-U inflation, the 1980 silver-price peak would be $149 per troy ounce and would be $617 per troy ounce in terms of January 2014 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

As shown in Table 1, on page 31 of *Hyperinflation 2014—The End Game Begins*, 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 come close to fully compensating for the loss of purchasing power of the dollar based on the ShadowStats-Alternate Consumer Price Measure (1980-Methodologies Base).

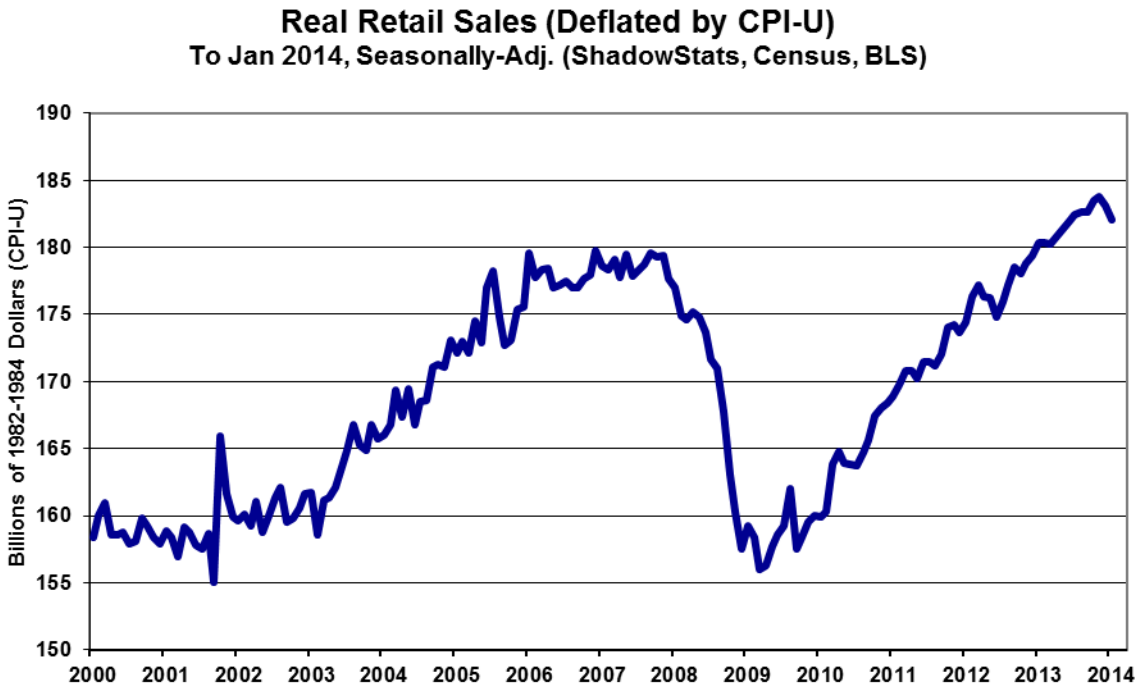
Real (Inflation-Adjusted) Retail Sales—January 2014. Real retail sales clearly are signaling a recession. Inflation-adjusted (based on the CPI-U) year-to-year change retail sales since World War II, as graphed in the *Opening Comments*, generally has signaled a pending recession whenever growth has dropped below

2.0%. It hit 1.0% in January 2014, generating the strongest recession signal seen since September 2007, just three months before the formal onset of the recession. Exceptions seen in the graph, such as in the mid-1990s, will be discussed in the upcoming *Second Installment* of the hyperinflation report (not all recessions have been official).

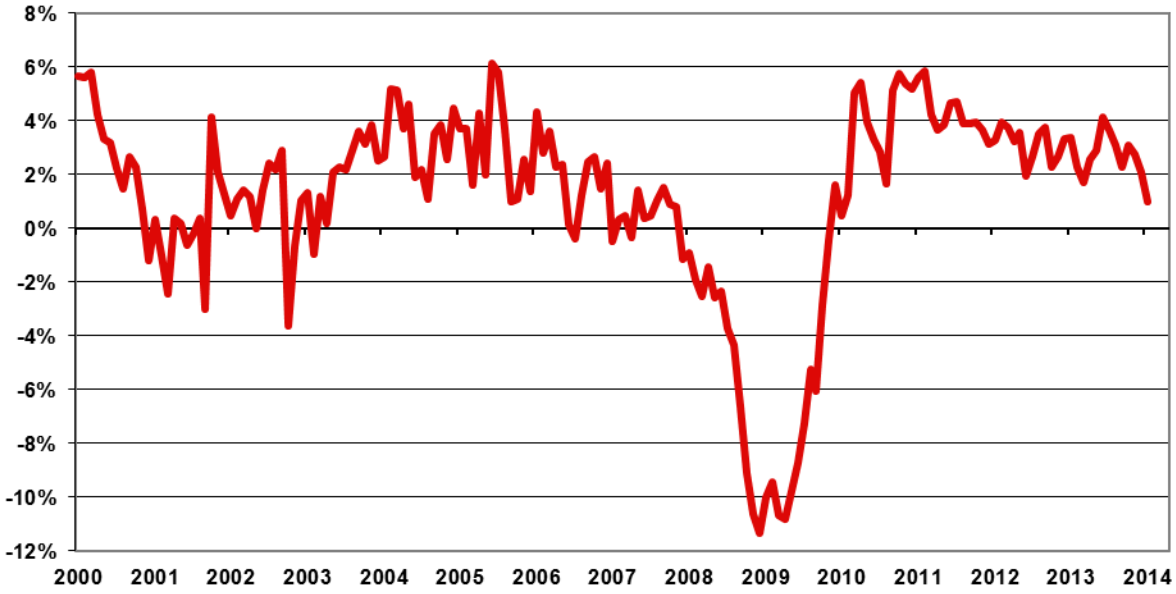
As covered in *Commentary No. 599*, the nominal monthly decline of 0.41% in headline January 2014 retail sales, a revised December 2013 decline of 0.12% (previously a gain of 0.23%), and a revised 0.26% (previously a 0.44%, initially a 0.68%) gain for November, all were before accounting for inflation.

Based on today's reporting of a 0.14% headline gain in the January 2014 CPI-U, and incorporating seasonal-adjustment revisions to prior CPI-U adjusted headline data, seasonally-adjusted real (inflation-adjusted) monthly retail sales fell by 0.55% in January 2014, following a revised 0.36% (previously 0.07%) decline in December, and a revised 0.15% (previously 0.40%) gain in November.

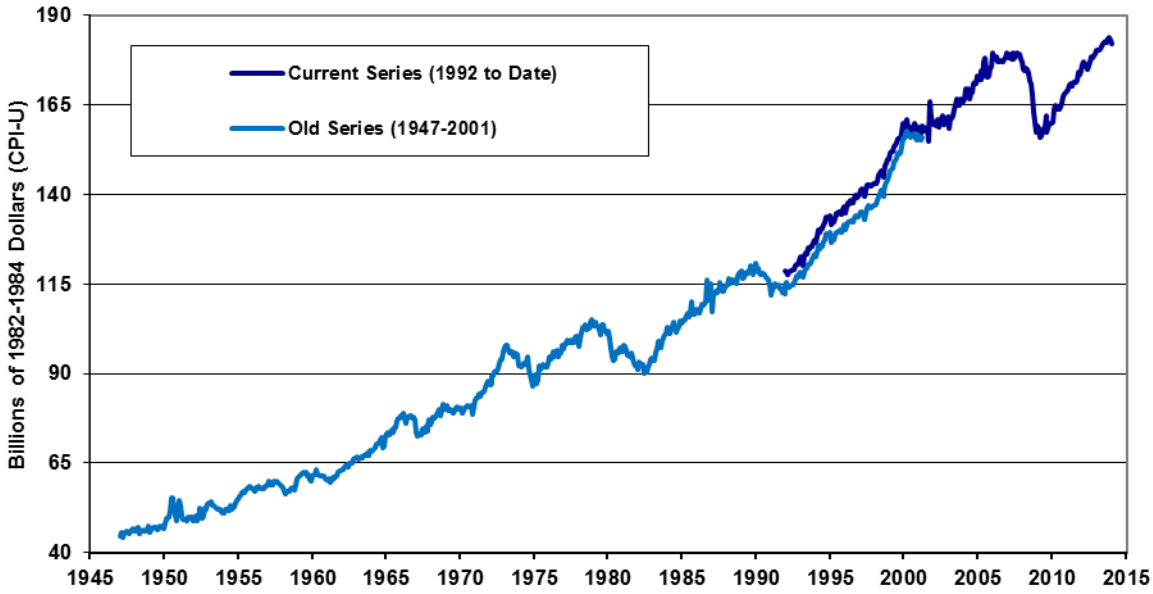
Year-to-year growth in January 2014 real retail sales skidded to a 0.99% gain, down from revised 2.08% (previously 2.57%) annual growth in December, and from 2.77% (previously 2.96%, initially 3.43%) in November, as reflected seen in the second graph following (and the longer-term graph in the *Opening Comments*). In normal economic times, the low level in annual real growth would signal a pending recession. In the current circumstance, this signal likely will serve as an indicator of a renewed downturn in broad economic activity, if not an outright contraction in economic activity in the current quarter.



Real Retail Sales Year-to-Year % Change
To Jan 2014, Seasonally-Adj. (ShadowStats, Census, BLS)



Real Retail Sales (Deflated by CPI-U)
To Jan 2014, Seasonally-Adj. (ShadowStats, St. Louis Fed)



Real Retail Sales—Downside Revisions and Plunging Activity. The first of the three preceding graphs shows the level of real retail sales activity (deflated by the CPI-U) since 2000; the second graph shows year-to-year percent change for the same period. The level of monthly activity turned down sharply in December 2013 and January 2014, with year-to-year change in activity plunging to near a standstill.

The third graph (immediately-preceding) shows the level of real retail sales (and its predecessor series) in full post-World War II detail. Again, a graph of year-to-year change in real retail sales since World War II is shown in the *Opening Comments.*

As to the level of real retail sales, given December 2013 and January 2014 reporting, the nascent expansion of the headline series above pre-recession levels, which began in February 2013, faltered in September, gained minimally in October and November, and then turned sharply negative in the last two months.

The gross domestic product (GDP) expanded beyond pre-recession levels twelve quarters ago, starting in second-quarter 2011, and it has kept rising, well beyond the reported activity of any other series, including real retail sales and industrial production. There is no other major economic series showing the GDP's pattern of both official, full recovery and extensive new growth. While real retail sales tend to lead the GDP, the "recovery" in retail reporting lagged the purported GDP recovery by two years. In like manner, the industrial production measure—a coincident GDP indicator—broke above its pre-recession high in November 2013 reporting, but that also has started to pull back with downside revisions and outright contractions as of January 2014 reporting.

The apparent "recovery" in the real retail sales series and industrial production (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)*, and was will be updated in the *Second Installment* of the hyperinflation report, deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

As shown in the latest "corrected" real retail sales graph, in the *Opening Comments*, with the deflation rates corrected for understated inflation, the recent pattern of real sales activity has turned increasingly negative. 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 also discussed in *Commentary No. 599*, 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.

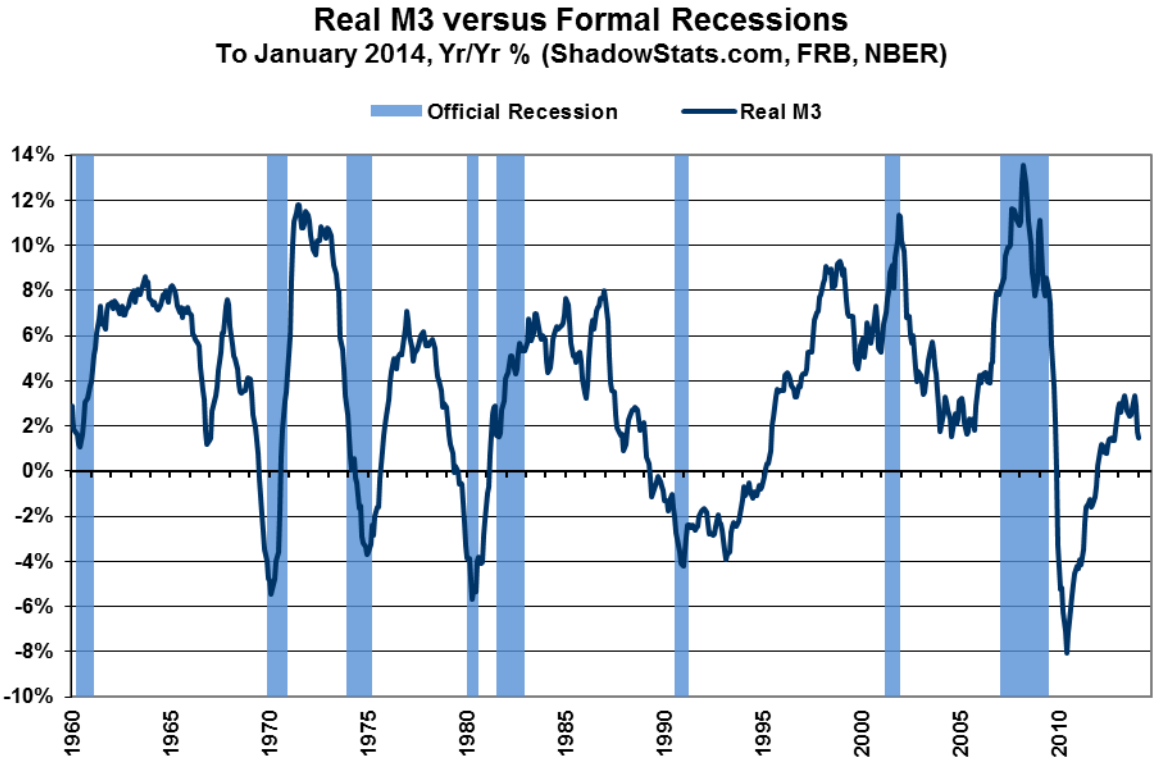
As official consumer inflation continues its upturn in the months ahead, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze—reflected partially by continued real earnings difficulties, discussed in the next section—these data should continue to trend meaningfully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

Real (Inflation-Adjusted) Average Weekly Earnings—January 2014. Coincident with today's January 2014 CPI-W release, the BLS also published real average weekly earnings for January, along with the

annual seasonal-adjustment revisions to the earnings series and to the monthly CPI-W inflation rates used in adjusting real earnings. In 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) rose by 0.16% for the month of January, following a revised 0.73% (previously 0.49%) decline in December.

Unadjusted and year-to-year, January 2014 real earnings growth rose to 0.38%, from a downwardly revised 0.15% (previously 0.44%) annual gain in December 2013. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility. Prior-period revisions usually are due to the instabilities in the BLS monthly surveys.

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—January 2014. 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 and, now, having downed, again. As shown in the accompanying graph—based on January 2014 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in M3 for January 2014 slowed to 1.5% from a revised 1.7% (previously 1.8%) in December. The slowing in the January annual growth rate for real M3 again reflected a combination of a lower nominal annual growth rate in M3 and a higher annual CPI-U inflation rate.

[The balance of the text in this Real Money Supply M3 *sub-section is unchanged from the prior CPI* Commentary*, with a planned full update of the analysis (including still-another signal) in the pending* Second Installment *of* Hyperinflation 2014.*]* 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 "new" or 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. This will be discussed more extensively in the upcoming *Second Installment* to *Hyperinflation 2014—The End Game Begins*.

WEEK AHEAD

Weaker-Economic and Stronger-Inflation Reporting Likely in the Months and Year Ahead. Although shifting to the downside, market expectations generally still appear to be overly optimistic as to the economic outlook, based on data that likely were puffed-up in the process of going through the data-gathering and reporting distortions of the October shutdown to the federal government. Expectations should continue to soften, though, with an increasing number of corrective revisions and disappointing

headline economic activity. The initial stages of that process have been seen in the recent reporting of December and January payroll, retail sales, housing starts and industrial production data, and in the December trade-balance detail.

That corrective circumstance and underlying weak economic fundamentals remain highly suggestive of deteriorating business activity. Accordingly, weaker-than-consensus economic reporting should become the general trend until such time as an unfolding "new" recession receives general recognition.

Stronger inflation reporting remains likely. Upside pressure on oil-related prices should reflect intensifying impact from a weakening U.S. dollar in the currency markets, and from ongoing political instabilities in the Middle East. The dollar faces pummeling from continuing QE3, the ongoing U.S. fiscal-crisis debacle, a weakening U.S. economy and deteriorating U.S. political conditions (see *Hyperinflation 2014—The End Game Begins*). Particularly in tandem with a weakened dollar, reporting in the year ahead generally should reflect much higher-than-expected inflation.

A Note on Reporting-Quality Issues and Systemic Reporting Biases. Significant reporting-quality problems remain with most major economic series. Ongoing headline reporting issues are tied largely to systemic distortions of seasonal adjustments. The data instabilities were induced by the still-evolving economic turmoil of the last seven-to-eight 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.

PENDING RELEASES:

GAAP-Based Financial Statements of the United State Government (2013). Initially scheduled for mid-December 2013, these financial statements were rescheduled by the U.S. Treasury for Wednesday, February 26th. The 2013 detail should show a much bleaker U.S. fiscal circumstance than has been commonly hyped. See *Hyperinflation 2014—The End Game Begins* for further detail.

Existing- and New-Home Sales (January 2014). January 2014 existing-home sales are due for release tomorrow, Friday, February 21st, from the National Association of Realtors, with the January new-home sales report from the Census Bureau due on Wednesday, February 26th. With these highly volatile and unstable series, whether existing or new sales, a pattern of stagnation or intensifying downturn appears to be in play for both. While monthly changes in home-sales activity usually are not statistically-significant, still-unstable reporting and revisions (both likely to the downside) remain a fair bet for the new-home sales series, which was so heavily disrupted as a result of the October shutdown of the federal government.

New Orders for Durable Goods (January 2014). The reporting of January 2014 new orders for durable goods is scheduled for Thursday, February 27th, by the Census Bureau. Other than for the continuing sharp and irregular volatility in commercial aircraft orders, new orders generally have been stagnant-to-

down, recently. Some intensification of recent, sporadic downside movement in orders still is likely in the month or two ahead, coincident with slowing activity currently seen in other economic indicators.

Gross Domestic Product—GDP (Fourth-Quarter 2014, Second Estimate, First Revision). The Bureau of Economic Analysis (BEA) has scheduled release of the second estimate of fourth-quarter 2013 GDP for Friday, February 28th. Market expectations appear to be for a downside revision to the initial 3.2% headline estimate, perhaps by an order of magnitude of a full-percentage point.

Underlying reality would tend to favor an even greater downside revision, disappointing the already negative market expectations. The most recent reporting of the trade deficit, retail sales, industrial production and housing starts all suggest a significant downside adjustment to this heavily-overstated, annualized quarterly growth rate.