

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

COMMENTARY NUMBER 605
Global Political Risks, January Construction Spending
March 5, 2014

Global Political Tensions Offer Increased Risk of U.S. Dollar Sell-Off
Minimal January Gain in Construction Spending Was Not Significant;
Inflation-Adjusted Series Remained Stagnant

PLEASE NOTE: A Special Commentary is scheduled for tomorrow, Thursday, March 6th, covering budget-deficit reality, based on analysis of the 2013 GAAP-based financial statements of the U.S. government. That will be followed by the Regular Commentary on Friday, March 7th, covering February employment and unemployment, and the January trade balance.

Today's Opening Comments and Executive Summary focus on currency risks tied to the crisis in Ukraine; a new approach to previewing biases built into BLS payroll reporting; and the detail on January construction spending, previously scheduled for the upcoming March 7th Commentary. See the Hyperinflation Watch for scheduling of the Second Installment of the hyperinflation report.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Crisis in Ukraine Highlights Global-Political Risk to the U.S. Dollar. The fundamentals could not be much weaker for the value of the U.S. dollar, or stronger for the price of gold. That circumstance had been in place for some time prior to, and as discussed in the *First Installment* of [Hyperinflation 2014—](#)

[*The End Game Begins*](#). The U.S. currency and U.S. financial system have faced an intensifying, broad range of vulnerabilities in recent months. Negative shocks in the areas of economic activity, domestic- and global-political circumstances have continued, while U.S. government and Federal Reserve authorities increasingly have found themselves unable to address a non-recovering economy as well as the mounting risks of financial-system instabilities.

Under these circumstances, Russia's military action against Ukraine, and related bellicose comments from Russia concerning the U.S. dollar and banking system, have raised the risks markedly of instabilities in the dollar and the domestic financial system. Talk of action to abandon the dollar as the global reserve currency; to move to dump the dollar; and to damage U.S. banks financially, cannot be taken lightly. China has been supportive of the Russian military action and also previously has called for the removal of the dollar as the global reserve currency. There have been stories of discontent within OPEC as to the dollar's reserve status.

The risks here are manifold. Keep in mind that in 2008, the U.S. financial system was on the brink of actual collapse. All the actions taken then by the Fed and the U.S. Treasury, including creating or spending whatever money was needed, all the bailouts, guarantees, interventions, etc., were only stopgap measures. The actions forestalled a financial-system collapse, temporarily, but they did little, if anything, to restore normal economic activity or financial-system solvency.

The problems of 2008 remain. A renewed crisis largely is just a matter of timing. As the system moves again to the brink, however, the Fed and the Treasury likely will find themselves with their ammunition much reduced, as a result of the post-2007 battle, which still is being waged in certain quarters.

Then there is the unexpected. Something goes wrong, and various financial triggers are pulled, as threatened or otherwise. To the extent the rest of the world sees a pending demise the U.S. dollar, there likely will be a number of large investors, sovereign and private, who would look to front run the Russians, or other hostile states, looking to get of the U.S. currency while they could.

A panicked sell-off in the U.S. dollar and dumping of dollar-denominated paper assets remains in the offing. Where a bad economic statistic, or fiscal or monetary blunder by the government or Federal Reserve had been viewed as the most likely proximal triggers for the dollar's demise, global political instabilities also have become a leading contender. There likely will be a confluence of negative factors that will accelerate the decline in the dollar's value. How that translates into inflation and other detail, again, is covered in [*Hyperinflation 2014—The End Game Begins*](#). Physical gold and silver remain the primary hedges for those looking to preserve the purchasing power of their wealth and assets.

Pending February Employment Numbers—Seasonal Adjustment Trend. In discussing the January 2014 headline payroll numbers last month, as usual, ShadowStats published the underlying trend projection for seasonally-adjusted payroll-employment growth for the month head. That trend number for February was for headline growth of 183,000. That trend number was based on the seasonal-adjustment modeling of the Bureau of Labor Statistics (BLS) of the monthly payroll data, and the reporting biases created by the process. The trend model is of particular interest to those trying to anticipate the upcoming headline numbers.

The specific, current BLS modeling biases, and analyses of same, are discussed in a brief article, which can be found on our affiliate site, ExpliStats.com. Those biases should impact the aggregate headline February reporting, directly. Public access to the detail is restricted until tomorrow, Thursday, March 6th, but ShadowStats subscribers can read the article [ExpliStats Payroll Trend](#), today, by using the password "a1401" that has been set aside for ShadowStats readers.

The ShadowStats outlook for the headline February jobs and unemployment reporting is discussed in the *Week Ahead* section.

January 2014 Construction Spending—Stagnation Continued. The headline 0.1% monthly gain in January 2014 construction spending was not statistically significant, but net of upside revisions to December's reporting, the monthly gain for January would have been 1.4%. This pattern of weak reporting and subsequent upside revision is seen in this particular series, more often than not. That said, the regular monthly reporting rarely is statistically significant. As shown in the accompanying graph, and in the graphs in the *Reporting Detail* section, the collapse in construction spending since early-2006, although it has seen some upside activity since 2011, has not come close to recovery, particularly when viewed after adjustment for inflation.

Adjusting Construction Spending for Inflation. There is no perfect inflation measure for deflating construction, but the pre-revision PPI's "new construction index" (NCI) was the closest found in publicly-available series. ShadowStats continues to look for a more-appropriate index for construction that also is available to the public. The revamped PPI includes a new series called "final demand construction" (FDC). In contrast to the 1.3% year-to-year January 2014 inflation of the NCI, which the BLS has left intact and continues to publish, the FDC showed year-to-year January 2014 construction inflation of 3.1%, which was more in line with private surveys of current construction costs. The big issue with the FDC, however, is that the BLS only publishes it with a history back to November 2009, which makes the reported inflation detail of very limited value in deflating series that have histories going back decades. Accordingly, ShadowStats continues to use the NCI for deflation of construction spending, for the time being.

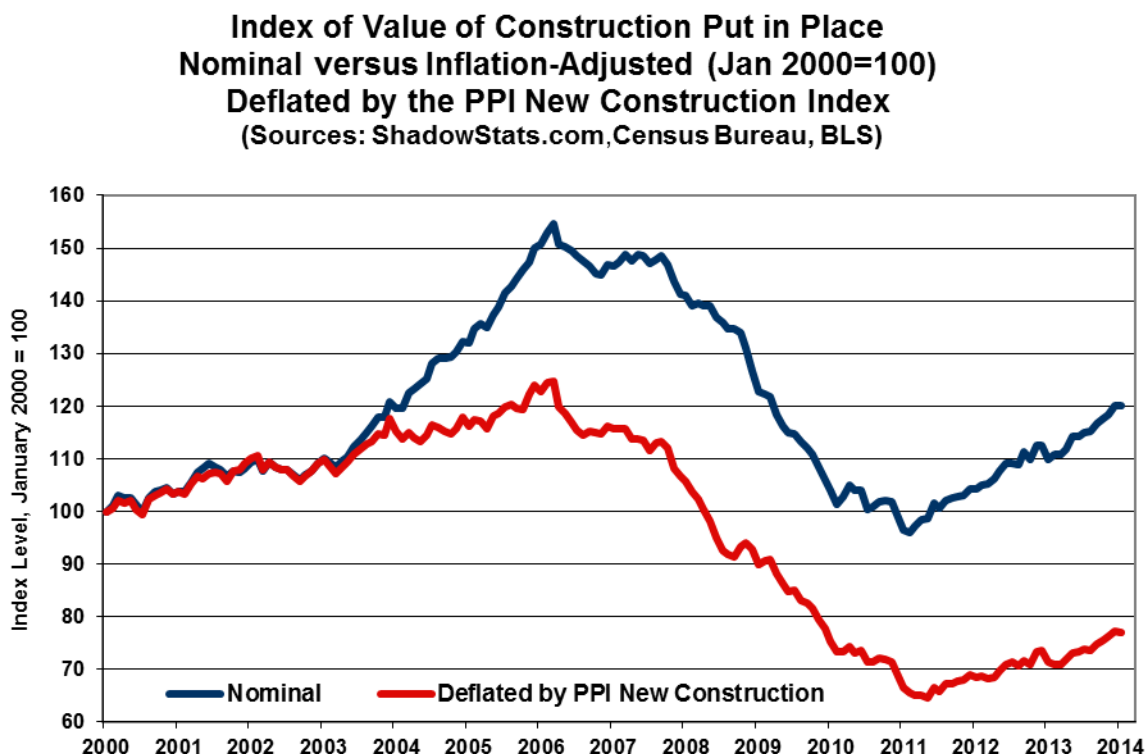
Official Reporting. The headline, total value of construction put in place in the United States for January 2014 was \$943.1 billion, on a seasonally-adjusted—but not-inflation-adjusted—annual-rate basis. That estimate was up month-to-month by a statistically-insignificant 0.1%. The January level of activity was against a revised \$941.9 billion in December, which was up by a revised 1.5% versus a revised \$928.3 billion in November. Before prior-period revisions, headline construction spending in January 2014 was up by 1.4% from the initial reporting for December 2013.

Adjusted for PPI inflation, per the new construction index (see the preceding section), aggregate real spending in January 2014 was down month-to-month by 0.5%, versus a 1.4% gain in December 2013 and a 1.1% gain in November.

On a year-to-year or annual-growth basis, January 2014 construction spending was up by a statistically-significant 9.3%, versus a revised 6.6% annual gain in December, and a revised 5.2% gain in November. Net of construction costs indicated by the NCI, year-to-year growth in spending increased to 7.9% in January, versus 5.2% in December and 4.0% in November. More-realistic private surveying suggests

annual costs to be up by enough to come close to turning some of those annual construction-spending growth rates flat or into annual contractions (again, see preceding section).

The usual full spectrum of eight graphs in the *Reporting Detail* section reflects the 0.1% monthly gain in January total construction, and component changes of private residential construction up by 1.1%, private nonresidential construction down by 0.2%, and public construction down by 0.8%.



[For greater detail on January 2014 construction spending, 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 shortly (likely in the week beginning March 10th), including analysis of the 2013 GAAP-based financial statements of the United States government and detail from the Federal Reserve's 2013 annual flow-of-funds analysis (due for release on March 6th). 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](#).

REPORTING DETAIL

CONSTRUCTION SPENDING (January 2014)

Minimal Growth in Headline Construction Spending Was in the Context of Upside Revisions. The headline 0.1% monthly gain in January 2014 construction spending was not statistically-significant, but net of upside revisions to December's reporting, the monthly gain for January would have been 1.4%. This pattern of weak reporting and upside revision is seen in this particular series, more often than not. That said, the regular monthly reporting rarely is statistically significant. As shown in the graphs that follow, the collapse in construction spending since early-2006 has not been close to recovery, particularly after adjustment for inflation.

Adjusting Construction Spending for Inflation. There is no perfect inflation measure for deflating construction, but the pre-revision PPI's "new construction index" (NCI) was the closest found in publicly-available series. ShadowStats continues to look for a more-appropriate index for construction that also is available to the public. The revamped PPI includes a new series called "final demand construction" (FDC). In contrast to the 1.3% year-to-year January 2014 inflation of the NCI, which the BLS has left intact and continues to publish, the FDC showed annual January 2014 construction inflation of 3.1%, more in line with private surveys of current construction costs. The big issue with the FDC, however, is that the BLS only publishes it with a history back to November 2009, which makes the reported detail of very limited value in deflating series that have histories going back decades. Accordingly, ShadowStats continues to use the NCI for deflation of construction spending, for the time being.

Official Reporting. The Census Bureau reported (March 3rd) the headline, total value of construction put in place in the United States for January 2014 at \$943.1 billion, on a seasonally-adjusted—but not-inflation-adjusted—annual-rate basis. That estimate was up month-to-month by a statistically-insignificant 0.1% +/- 1.8% (all confidence intervals are at the 95% level), and it was against a revised \$941.9 (previously \$930.5) billion in December, which was up by a revised 1.5% (previously a 0.1%) monthly gain, versus a revised \$928.3 (previously \$929.9, initially \$934.4) billion in November.

The headline construction spending amount in January 2014 was up by 1.4% from the initial reporting for December 2013, before prior-period revisions.

Adjusted for PPI inflation per the new construction index (see the preceding section), aggregate real spending in January 2014 was down month-to-month by 0.5%, versus a 1.4% gain in December 2013 and a 1.1% gain in November.

On a year-to-year or annual-growth basis, January 2014 construction spending was up by a statistically-significant 9.3% +/- 2.1%, versus a revised 6.6% (previously 5.3%) annual gain in December, and a revised 5.2% (previously 5.5%, initially 5.9%) gain in November. Net of construction costs indicated by the NCI, year-to-year growth in spending increased to 7.9% in January, from 5.2% in December and 4.0% in November. More-realistic private surveying suggests annual costs to be up by enough to come close to turning some of those annual construction-spending growth rates flat or into annual contractions.

The statistically-insignificant 0.1% monthly gain in January 2014 construction spending, versus the 1.5% gain in December, included a 0.8% contraction in January public construction spending, versus a 0.4% revised gain in November. January private construction was up by 0.5% for the month, versus a revised 1.9% monthly increase in December. The following graphs reflect the 0.1% monthly gain in January total construction, with private residential construction up by 1.1%, private nonresidential construction down by 0.2%, and public construction down by 0.8%. Also reflected is the 1.5% monthly gain in December total construction, with private residential construction up by 2.6%, private nonresidential construction up by 1.2% and public construction up by 0.4%.

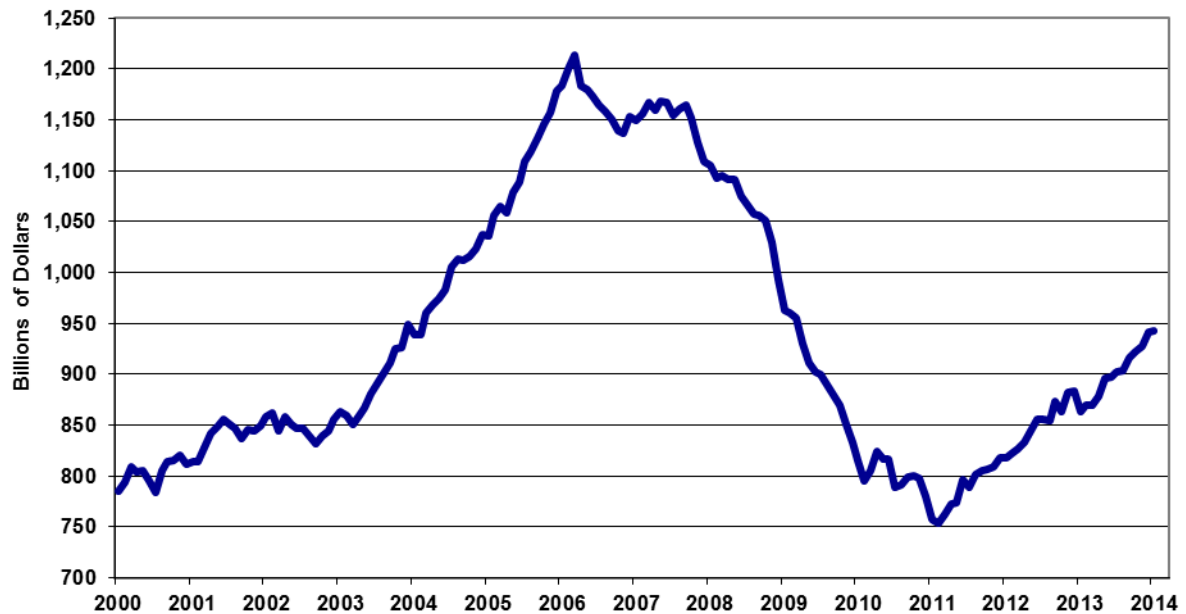
Construction and Related Graphs. The two graphs following reflect total construction spending through January 2014, before and after inflation adjustment. The inflation-adjusted graph is on an index basis, with January 2000 = 100.0.

Adjusted for the PPI's NCI measure, real construction spending shows the economy slowing in 2006, plunging into 2011 and then turning minimally higher in an environment of low-level stagnation, through the most-recent reporting. The pattern of inflation-adjusted activity here does not confirm the economic recovery shown in the headline GDP series (see [Commentary No. 604](#)). To the contrary, the latest construction reporting, both before (nominal) and after (real) inflation adjustment, shows a pattern of ongoing stagnation, as reflected in the first two graphs following.

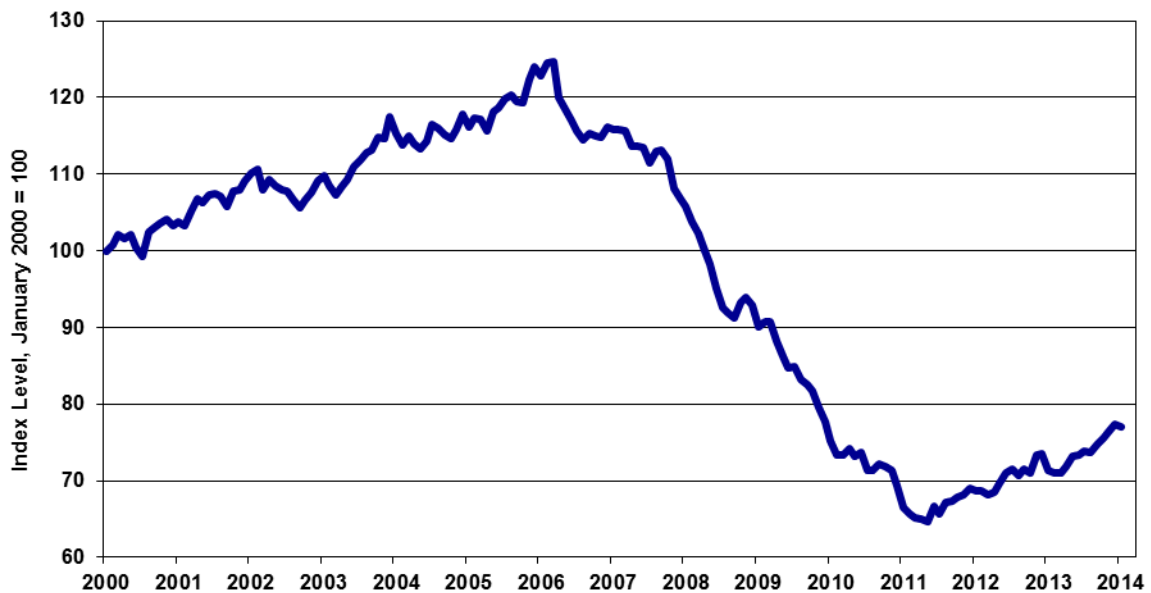
The third graph following reflects the reporting of January 2014 construction employment (see [Commentary No. 598](#) for related benchmark-revision detail), which will be updated with the pending March 7th *Commentary* and the release of February 2014 labor conditions. In theory, payroll levels should move more closely with the inflation-adjusted aggregate series, where the nominal series reflects the impact of costs and pricing, as well as a measure of the level of physical activity.

The fourth graph following shows total nominal construction spending, broken out by the contributions from total-public (blue), private-nonresidential (yellow) and private-residential spending (red).

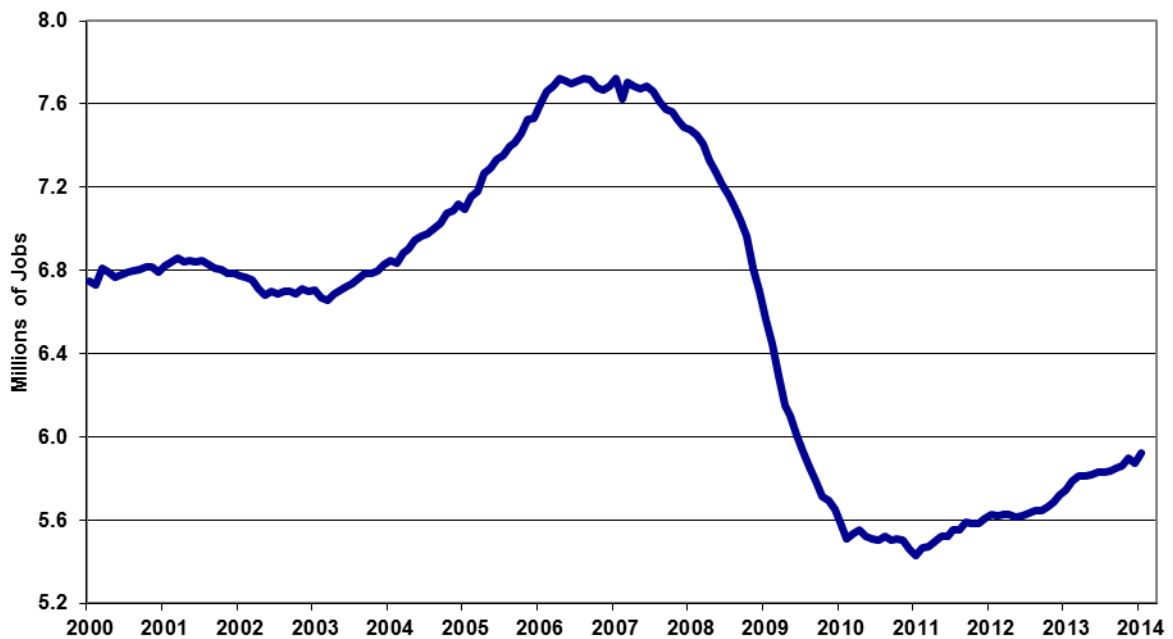
Total Construction Spending, Monthly to January 2014
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



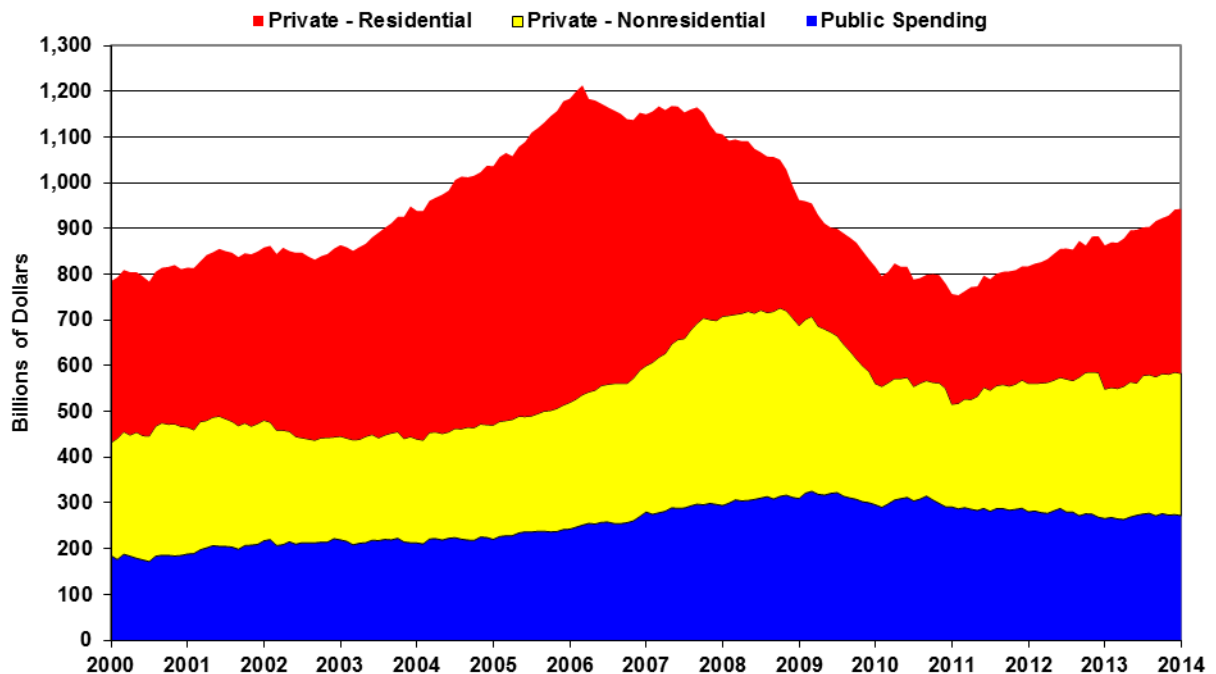
Index of Value of Construction Put in Place
To January 2014, Inflation-Adjusted (Jan 2000=100)
Deflated by the PPI New Construction Index
(Sources: ShadowStats.com, Census Bureau, BLS)



Construction Payroll Employment (Revised)
To Jan 2014, Seasonally-Adjusted (ShadowStats.com, BLS)

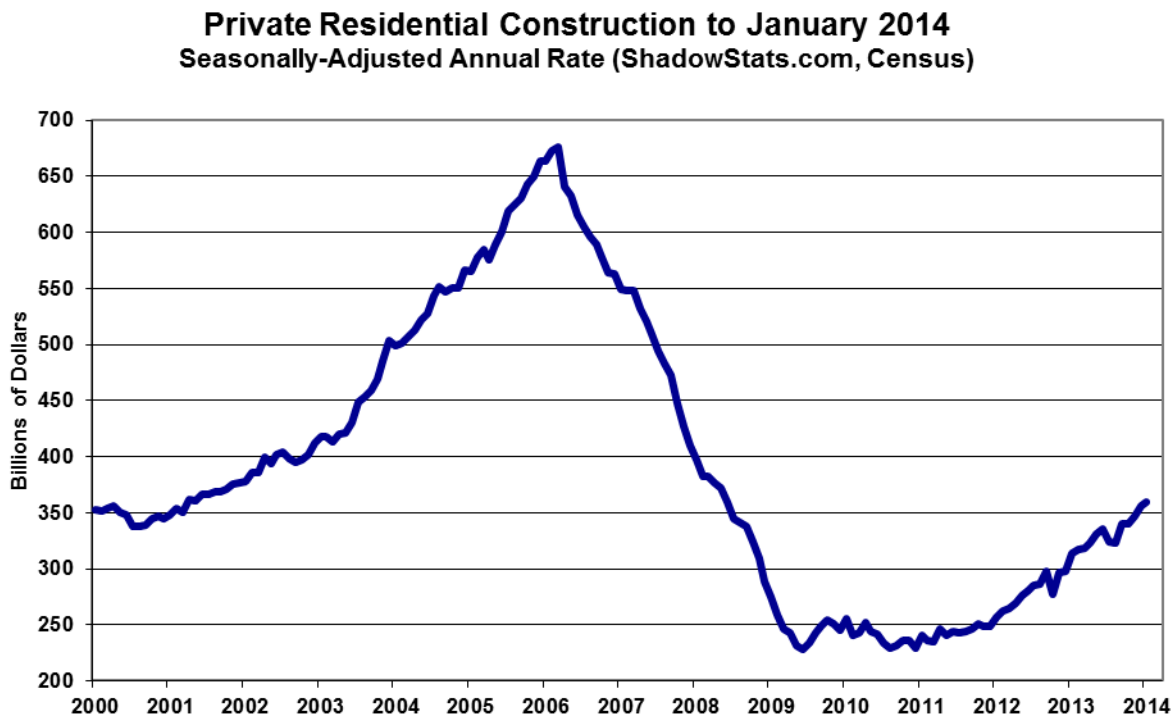


Construction Spending, Monthly to January 2014
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)

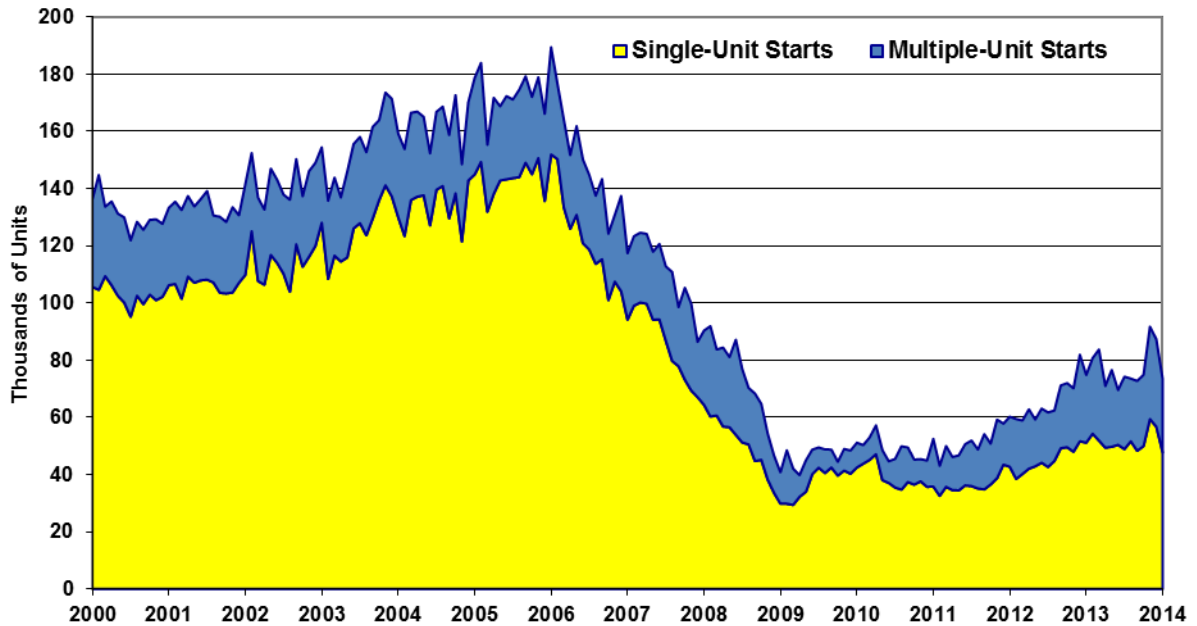


The next two graphs cover private residential construction, including housing starts data, for January. As detailed in [Commentary No. 601](#), the recent surge, and the subsequent, increasingly-corrective pullback in housing starts activity, likely was at least partially an artefact of surveying and reporting disruptions around the October government shutdown. Keep in mind that the construction spending series is in nominal (not-adjusted-for-inflation) dollars, while housing starts and building permits reflect unit volume.

The last two graphs (third and fourth graph following), show the patterns of the monthly level of activity in private nonresidential construction spending and in public construction spending. The spending in private nonresidential construction remains well off its historic peak, but has bounced higher recently off a secondary, near-term dip in late-2012. Public construction spending, which is 98% nonresidential, continues in a broad downtrend, with intermittent, short-lived bounces.



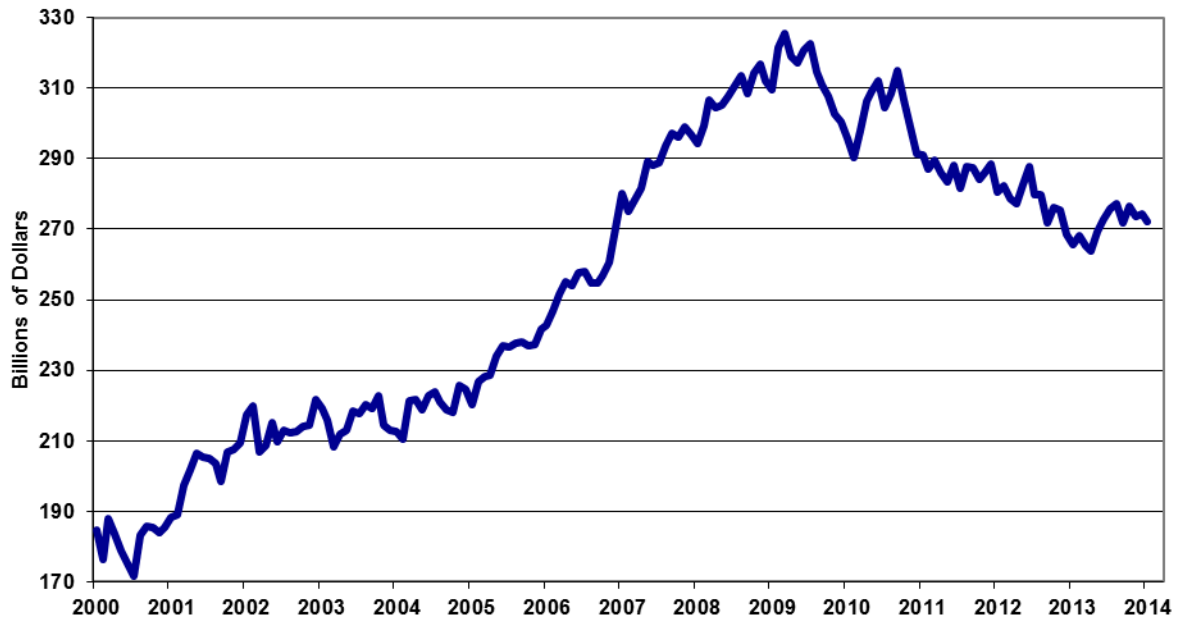
Single- and Multiple-Unit Housing Starts (Monthly Rate)
To Jan 2014, Seasonally-Adjusted (ShadowStats.com, Census)



Private Nonresidential Construction to January 2014
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



Public Construction, Monthly to January 2014
Seasonally-Adjusted Annual Rate (ShadowStats.com, Census)



WEEK AHEAD

Much 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. Expectations should continue to be hammered, though, by continuing, downside corrective revisions and continued, 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 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 the 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 global political instabilities. The dollar faces pummeling from continuing QE3, the ongoing U.S. fiscal-crisis debacle, a weakening U.S. economy and deteriorating U.S. and global political conditions (see *Opening Comments* and [*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:

U.S. Trade Deficit (January 2014). The Commerce Department and Bureau of Economic Analysis (BEA) will release the January 2014 trade-balance data on Friday, March 7th. Continued deterioration in the monthly trade deficit remains likely. Any widening (or narrowing) of the December deficit, in revision, would have negative (or positive) impact on the second revision to fourth-quarter GDP. The initial reporting for January will help set the tone for expectations of the initial first-quarter 2014 reporting of the net-export-account contribution to GDP activity. Market expectations for the January headline deficit reporting appear to be for little change from the initial December 2013 estimate of \$38.7 billion. Again, reporting risk favors continued widening of the monthly trade shortfall.

Employment/Unemployment (February 2014). The Bureau of Labor Statistics (BLS) will release its February 2014 labor data on Friday, March 7th. Following January's 113,000 consensus-shocking low gain in payroll employment (the second straight month of negative surprises), a further downside surprise to expectations is a fair bet.

The BLS trend model suggests a 183,000 jobs gain for February (see detail available in the *Opening Comments* section). Where the consensus tends to close in around the trend, expectations seem to be running about 30,000 to 40,000 jobs below trend. Again, underlying economic reality would suggest a downside surprise versus both the trend and market expectations.

Expectations appear to be for the headline February U.3 unemployment rate to hold near January's 6.6% reading. Underlying fundamentals would suggest an upturn in U.3, but the BLS's continuing purge of discouraged workers from the unemployment rolls and labor force would argue in favor of a lower rate. As discussed regularly in the employment/unemployment-related *Commentaries*, month-to-month comparisons of U.3 are of no meaning, here, because of the standard, inconsistent reporting calculations that leave the monthly unemployment data not comparable.

If U.3 drops, there likely would be some further labor-force loss associated with that. The broader U.6 and ShadowStats unemployment measures would tend to hold, or increase anew, at their broader and higher respective levels.

Again, all these numbers are unsettled and could come in well outside general expectations.
