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

COMMENTARY NUMBER 619
March Retail Sales, Consumer Liquidity

April 14, 2014

First-Quarter Retail Sales Contracted Net of Likely Inflation

Shifting and Unreported Seasonal Factor Changes Boosted Headline Numbers in Advance of the Annual Benchmark Revision

Consumer Liquidity Remains Structurally Impaired

PLEASE NOTE: The next regular Commentary *is scheduled for tomorrow, Tuesday, April 15th, covering the March CPI and real retail sales and earnings, followed by one on April 16th, covering housing starts and industrial production and a summary of major March 2014 economic reporting.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE COMMENTARY

March Nominal Retail Sales Jumped; First-Quarter Real Retail Sales Contracted. In volatile month-to-month reporting that is not to be trusted, March retail sales rose by a better-than-expected 1.1%. The retail series likely faces net, historical downside revisions in its pending, April 30th, annual benchmark revision. Nonetheless, net of the effects of inflation, first-quarter 2014 real retail sales should show an annualized quarter-to-quarter contraction of 1.4%, or so, consistent with a decline in first-quarter 2014 GDP. The advance estimate of first-quarter GDP also is due for release on April 30th.

Where the releases of *2014 Hyperinflation Report—The End Game Begins* *First Installment Revised* (April 2nd) and *2014 Hyperinflation Report—Great Economic Tumble* *Second Installment* (April 8th) present a broad picture of likely economic, systemic and financial conditions in the coming year, this week's reporting will do much to set consensus expectations for the headline first-quarter GDP estimate. The remaining major March reports (see *Week Ahead* section) generally should disappoint market expectations and move the consensus outlook increasingly towards a looming GDP contraction.

Accordingly, Wednesday's (April 16th) *Commentary No. 621*, covering March 2014 residential construction (housing starts) and industrial production detail, and subsequent to the reporting of March real retail sales and earnings on Tuesday, will provide an updated summary of the latest economic detail.

Today's brief *Commentary* covers the detail of nominal (not-adjusted-for-inflation) March 2014 retail sales.

March Retail Sales in Rebound. Dominated by gains in auto sales, boosts from spurious and historically-inconsistent concurrent-seasonal-factor adjustments, and presumed relief otherwise from the negative impact of bad weather in January and February, headline March retail sales rose by 1.1%, following a revised 0.7% (was 0.3%) headline gain in February. That said, net of likely March consumer inflation (see *Week Ahead* section)—the way GDP is reported—inflation-adjusted, or real, retail sales still showed a meaningful quarter-to-quarter contraction in first-quarter 2014.

Separately, the reporting of auto sales is heavily gimmicked. New, near-term seasonal adjustments (inconsistent with the published historical series) boosted headline reporting, and negative weather effects—estimated for retail sales—generally have been overstated. Where retail sales reporting often is revised heavily on a monthly basis, and downside revisions could be expected for the just-released headline data, next month, the annual benchmark revision for the series also scheduled for April 30th. Net downside revisions to previously-reported retail sales activity of recent years are likely.

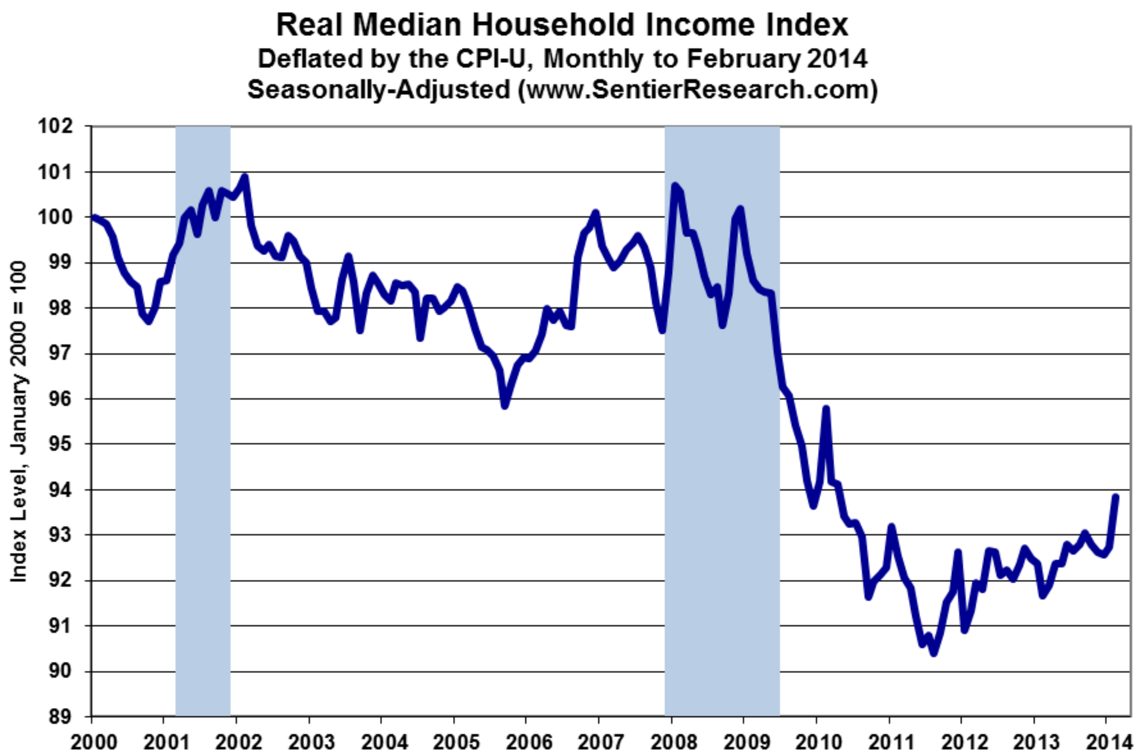
Underlying Fundamentals Remain Bleak. The stronger March 2014 detail still left intact the basic outlook of renewed broad economic downturn, as well as the traditional recession signals that have been seen in recent months. During the six-plus years of economic collapse, activity in consumer buying of goods and services has been constrained by the intense, structural-liquidity woes besetting the consumer, as discussed in the consumer-liquidity section. Without real, or inflation-adjusted, 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 or in personal-consumption activity that dominates the headline change in GDP.

Nominal (Not-Adjusted-for-Inflation) Retail Sales—March 2014. In the context of an upside revision to February and a downside revision to January headline sales activity, and not adjusted for consumer inflation, headline March 2014 retail sales showed a statistically-significant, seasonally-adjusted monthly gain of 1.1%. That was 1.14% at the second decimal point, and a monthly gain of 1.57% before prior-period revisions. The March gain followed a revised, statistically-significant month-to-month gain of 0.73% (previously up by 0.27%), and a revised decline of 0.68% (previously down by 0.64%, initially a decline of 0.41%) in January.

Year-to-year, March 2014 retail sales growth rebounded from softer numbers in January and February, up by a statistically-significant 3.78%, versus a revised 1.78% (previously 1.48%) in February, and a revised 1.90% (previously 1.94%, initially 2.57%) in January.

As of the headline March reporting, nominal first-quarter 2014 sales rose at an annualized quarter-to-quarter pace of just 0.29%, versus a 2.93% pace in fourth-quarter 2013. As discussed in the "real retail sales" section, such should reflect a quarter-to-quarter contraction in real first-quarter 2014 activity.

Real (Inflation-Adjusted) Retail Sales—March 2014. The headline 1.14% nominal gain in the monthly March retail sales was before accounting for inflation. Real retail sales for March (adjusted for inflation), will be reported along with the headline estimate of consumer inflation, the March CPI-U, in tomorrow's April 15th *Commentary No. 620*. As discussed in the *Week Ahead* section, March headline inflation should be close to nil, likely on the plus-side, leaving headline March real retail sales at close to its nominal month-to-month gain. Real annualized quarter-to-quarter retail sales in first-quarter 2014 likely contracted by about 1.4%, versus a 1.8% annualized gain in fourth-quarter 2013.

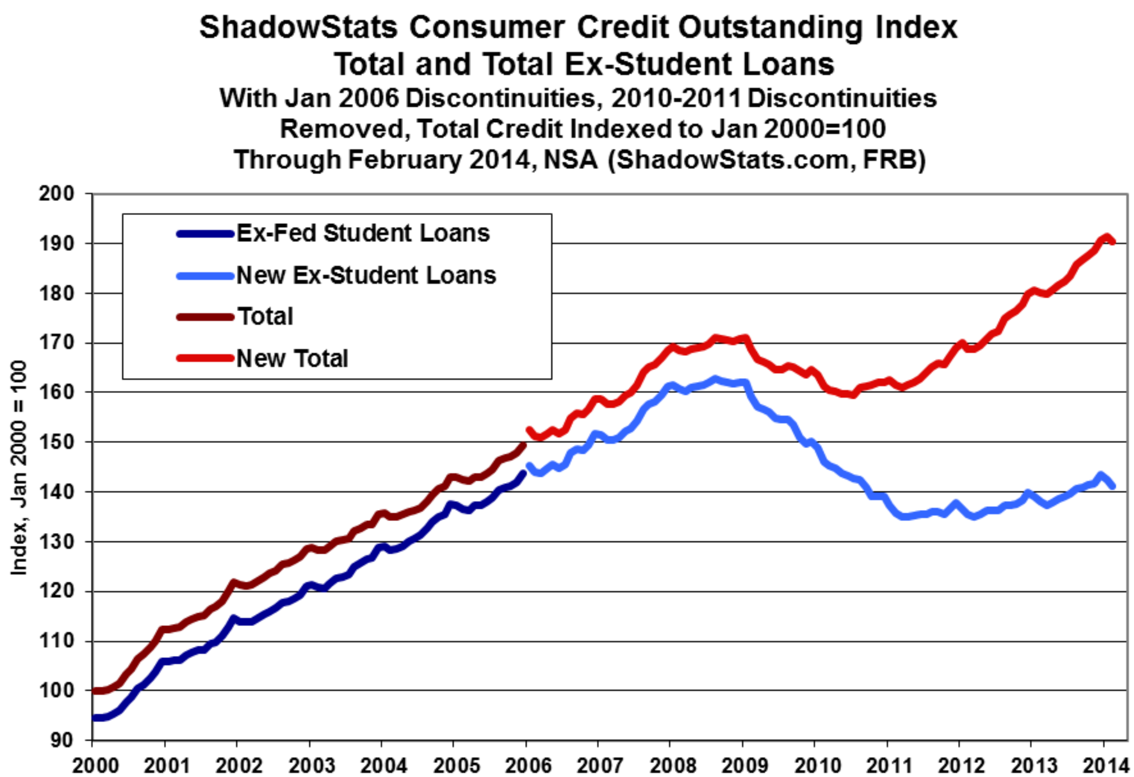


Consumption Constrained by Continuing Structural Consumer Liquidity Woes. Serious, structural liquidity problems continue to impair consumer activity, meaningfully, as discussed frequently in these *Commentaries* and as indicated in the accompanying graphs. Without real, inflation-adjusted, growth in income, and without the ability or willingness to take on meaningful new debt, the consumer simply cannot sustain real growth in retail sales or in the personal-consumption activity that dominates the headline growth in GDP (see *2014 Hyperinflation Report—Great Economic Tumble – Second Installment*).

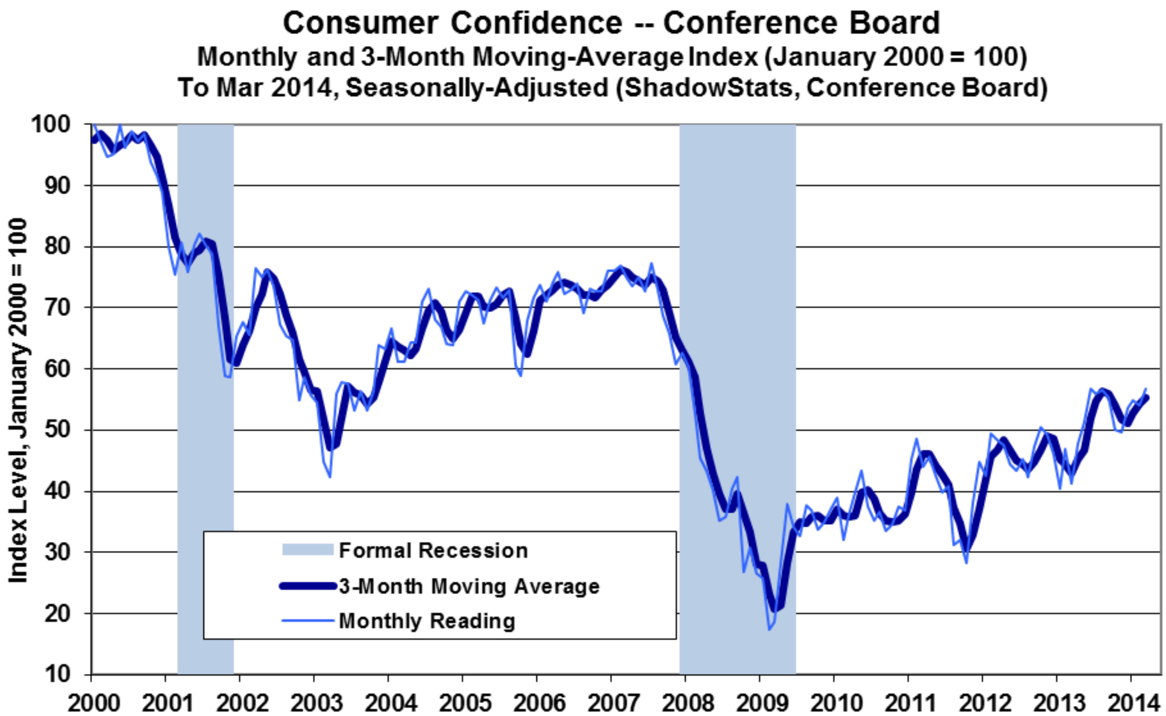
The preceding graph of real median household income by month, based on data published by www.SentierResearch.com, showed continued income stagnation in February 2014. Despite the uptick in the seasonally-adjusted February number, median household income remains near the cycle-low for the series.

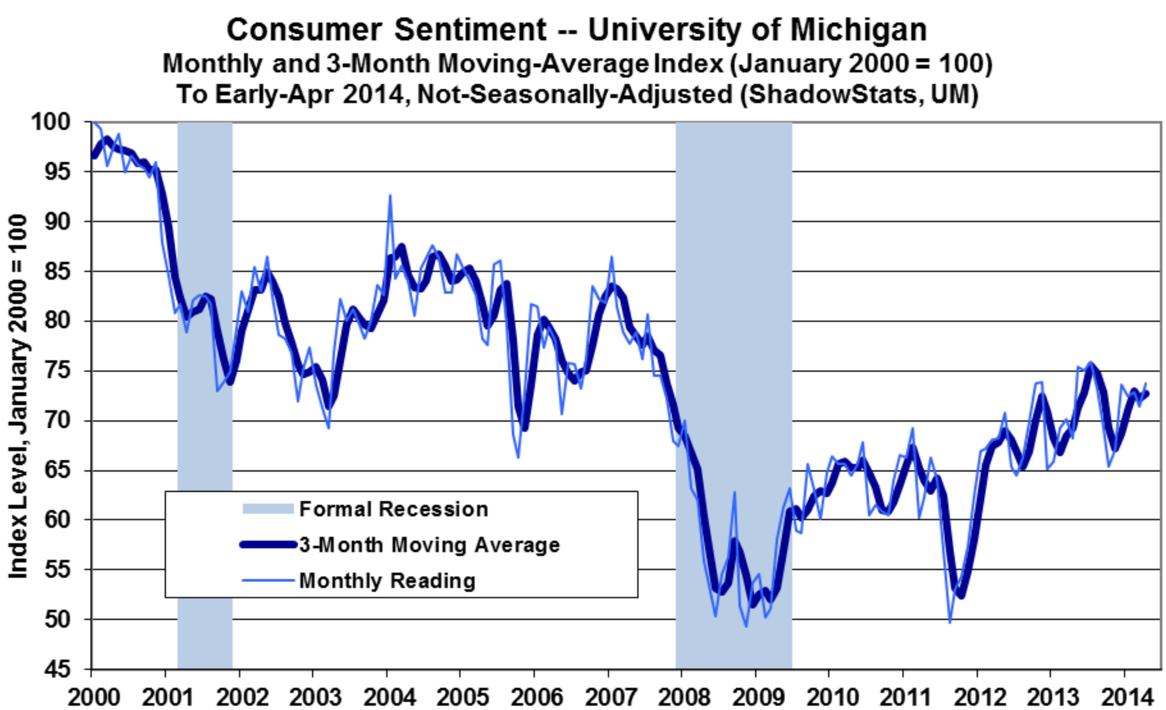
As the GDP purportedly was starting a solid recovery in mid-2009, household income plunged to new lows. Deflated by headline CPI-U, the annual series published by the Census Bureau showed further that annual real median household income in 2012 was at levels seen in the late-1960s and early-1970s (again, see the *Hyperinflation Report – Second Installment*).

The next graph shows consumer credit outstanding (Federal Reserve Board), updated through February 2014. Practically all the post-2008-Panic growth in consumer credit has been in federally-backed student loans, instead of in bank lending to the consumer that would tend to fuel consumption of washing machines, etc., potentially helping to offset lack of income growth.



The last two graphs reflect the ever-volatile consumer confidence (March 2014 reporting, Conference Board) and consumer sentiment (early-April 2014 reporting, University of Michigan). Current levels in both series remain deep in traditional recession territory. The pattern here, as with household income, has been one of collapse and stagnation, as opposed to the pattern of economic collapse and recovery indicated in the faulty GDP series.


Consumer Confidence -- Conference Board
Monthly and 3-Month Moving-Average Index (January 2000 = 100)
To Mar 2014, Seasonally-Adjusted (ShadowStats, Conference Board)
Index Level, January 2000 = 100
100
90
80
70
60
50
40
30
20
10
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
Formal Recession
3-Month Moving Average
Monthly Reading


Consumer Sentiment -- University of Michigan
Monthly and 3-Month Moving-Average Index (January 2000 = 100)
To Early-Apr 2014, Not-Seasonally-Adjusted (ShadowStats, UM)
Index Level, January 2000 = 100
100
95
90
85
80
75
70
65
60
55
50
45
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
Formal Recession
3-Month Moving Average
Monthly Reading

Again, without growth in real income; without the ability or the will to expand debt meaningfully; and without the confidence to take on new debt, where possible; the consumer simply cannot sustain real growth in retail sales, housing or in the dominant, personal-consumption measure of the GDP. There is no broad economic recovery that is pending or underway.

[For further detail on March retail sales, see the* Reporting Detail *section, and ShadowStats-affiliate www.ExpliStats.com]

HYPERINFLATION WATCH

Hyperinflation Summary Outlook. The hyperinflation and economic outlook were updated fully in the last two weeks, with the publication of *2014 Hyperinflation Report—The End Game Begins First Installment Revised*, on April 2nd, and publication of *2014 Hyperinflation Report—Great Economic Tumble Second Installment*, on April 8th. Consistent with those *Special Commentaries* and any interim economic reporting, a revised summary outlook is planned shortly for this section.

REPORTING DETAIL

RETAIL SALES (March 2014)

March Retail Sales Showed a Rebound. Dominated by a gain in auto sales, boosts from spurious and historically-inconsistent concurrent-seasonal-factor adjustments, and presumed relief otherwise from the negative impact of bad weather in January and February, headline March retail sales rose by 1.1%, following a revised 0.7% (was 0.3%) headline gain in February. That said, net of likely March consumer inflation (see *Week Ahead* section)—the way GDP is reported—inflation-adjusted, or real, retail sales still showed a meaningful quarter-to-quarter contraction for first-quarter 2014.

Separately, the reporting of auto sales is heavily gimmicked. New, near-term seasonal adjustments (inconsistent with the published historical series) boosted headline reporting, and negative weather effects—estimated for retail sales—generally have been overstated. Where retail sales reporting often is revised heavily on a monthly basis, and downside revisions could be expected for the just-released headline data, next month, the annual benchmark revision to the series also is scheduled for April 30th. Net downside revisions to previously-reported retail sales activity of recent years are likely.

Reporting Instabilities and Distortions. Prior-period revisions of one year ago reflected little more than the unstable monthly revisions in the concurrent-seasonal-adjustment process. Where only the February and March 2013 numbers are shown on a consistent basis with headline numbers, activity in February 2013 was upped by 0.7%. That was due solely to revisions in the historical seasonal adjustments for the period ended March 2014, which also spiked the current headline seasonal factors and headline numbers in parallel.

Concurrent seasonal adjustments are recalculated every month, but not reported on a consistent, historical basis. This allows for invisible shifts in seasonally-adjusted current activity that are not consistent with published historical reporting. Further, the stability of the seasonal-adjustment process (particularly the concurrent-seasonal-adjustment process used with retail sales) and 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).

Retail sales reporting suffers the same inconsistency issues that are seen with other series, such as payroll employment, the unemployment rate, and durable goods orders. The highly variable and unstable seasonal factors here have continued to cloud relative activity in the January 2014-to-March 2014, and in the February 2013-to-March 2013 periods, five months that are published on a non-comparable basis with all the other historical numbers.

Although the published historical numbers were consistent at the time of the May 31, 2013 benchmark revision (again, the next benchmark revision is set for April 30, 2014), ten intervening rounds of post-revision, concurrent-seasonal adjustments now have thrown all the historical numbers into disorder. The resulting inconsistencies allow for unreported shifts in the historical data that are distorting the estimates of the current headline numbers.

Underlying Fundamentals Remain Bleak. The stronger March 2014 detail still left intact the basic outlook of renewed broad economic downturn, and the traditional recession signals that have been in place continue. As has been the circumstance during the six-plus years of economic collapse, activity in consumer buying of goods and services has been constrained by the intense, structural-liquidity woes besetting the consumer, as discussed, in the *Opening Comments* section. Without real, or inflation-adjusted, 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 or in personal-consumption activity that dominates the headline change in GDP.

Nominal (Not-Adjusted-for-Inflation) Retail Sales—March 2014. In the context of an upside revision to February and a downside revision to January sales activity, and not adjusted for consumer inflation, today's (April 14th) report on March 2014 retail sales—issued by the Census Bureau—indicated a statistically-significant, seasonally-adjusted, headline monthly gain of 1.1%. That was an increase of 1.14% at the second decimal point, +/- 0.58% (all confidence intervals are at the 95% level), and a monthly gain of 1.57% before prior-period revisions. The March gain followed a revised, statistically-significant month-to-month gain of 0.73% +/- 0.23% (previously up by 0.27%), and a revised decline of 0.68% (previously down by 0.64%, initially a decline of 0.41%) in January.

Year-to-year, March 2014 retail sales growth rebounded from softer numbers in January and February, up by a statistically-significant 3.78% +/- 0.82%, versus a revised 1.78% (previously 1.48%) in February, and a revised 1.90% (previously 1.94%, initially 2.57%) in January.

As of the headline March reporting, nominal first-quarter 2014 sales rose at an annualized quarter-to-quarter pace of just 0.29%, versus a 2.93% pace in fourth-quarter 2013. As discussed in the "real retail sales" section, such should be a quarter-to-quarter contraction in real first-quarter 2014 activity.

March Core Retail Sales. Despite soaring food prices and a 5.0% jump in monthly gasoline prices, seasonally-adjusted monthly grocery-store sales rose by just 0.21% in March, with gasoline-station sales falling by 1.33%. Such are the artefacts of a corrupted concurrent-seasonal-adjustment process. 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: March 2014 versus February 2014 seasonally-adjusted retail sales series—net of total grocery store and gasoline station revenues—rose by 1.61%, versus the official gain of 1.14%.

Version II: March 2014 versus February 2014 seasonally-adjusted retail sales series—net of the monthly change in revenues for grocery stores and gas stations—rose by 1.26%, versus the official gain of 1.14%.

Real (Inflation-Adjusted) Retail Sales—March 2014. The headline 1.14% nominal gain in the monthly March retail sales was before accounting for inflation. Real retail sales for March (adjusted for inflation), will be reported along with the headline estimate of consumer inflation, the March CPI-U, in tomorrow's April 15th *Commentary No. 620*. As discussed in the *Week Ahead* section, March headline inflation should be close to nil, likely on the plus-side, leaving headline March real retail sales at close to its nominal month-to-month gain. Real annualized quarter-to-quarter retail sales in first-quarter 2014 likely contracted by about 1.4%, versus a 1.8% annualized gain in fourth-quarter 2013.

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 headline reporting of most major economic series.

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 *Hyperinflation 2014—The End Game Begins (Updated)*). 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 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:

Consumer Price Index—CPI (March 2014). The Bureau of Labor Statistics (BLS) has scheduled release of the March 2014 CPI for tomorrow, Tuesday, April 15th. The headline CPI-U is a fair bet to be close to unchanged for the month, perhaps on the plus-side.

Average gasoline prices rose month-to-month in March 2014 by 5.0%, on a not-seasonally-adjusted basis, per the Department of Energy, but BLS seasonal adjustments will depress gasoline prices in the headline March CPI by enough to knock 0.1% off what otherwise would have been reported. Upside pressure on the seasonally-adjusted, headline CPI likely will come from higher food prices and "core" inflation.

Year-to-year, CPI-U inflation would increase or decrease in March 2014 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.23% decline in the monthly inflation reported for March 2013. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for March 2014, the difference in March's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the February 2014 annual inflation rate of 1.13%. For example, a headline seasonally-adjusted, month-to-month increase of 0.1% in March 2014 would mean that annual inflation for March 2014 would come in at about 1.4% to 1.5%.

Residential Construction—Housing Starts (March 2014). On Wednesday, April 16th, the Census Bureau will publish its estimate of March 2014 housing starts. This series was distorted heavily to the upside by data-gathering and reporting issues that resulted from the government shutdown in October, and it is still suffering reporting instabilities. Despite near-perpetual market expectations for strengthening activity in housing starts, month-to-month change likely will remain in a pattern of statistical-insignificance, with ongoing stagnation and renewed downturn or downside revisions seen in the aggregate series, as well as particularly in single-unit housing starts. As usual, this series is subject to large prior-period revisions.

In the wake of a 75% collapse in aggregate activity from 2006 through 2008, and an ensuing five-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.

Index of Industrial Production (March 2014). Also on Wednesday, April 16th, the March 2014 index of industrial production will be released by the Federal Reserve Board. Net of the ongoing irregular volatility in utility output tied to seasonable or unseasonable weather, market expectations for moderate March production growth are a fair bet to be disappointed on the downside, as consumption slows and companies increasingly move to reduce excessive inventory levels. As usual, this series is subject to large prior-period revisions.

