

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

COMMENTARY NUMBER 636
May CPI, Real Retail Sales and Earnings, Housing Starts
June 17, 2014

**When Understated Headline Inflation Generates Contracting Activity,
the Economy Is in Serious Trouble,**
Inflation More Than Wiped Out the Headline Gain in May Retail Sales
Inflation-Adjusted Earnings Fell for Second Month
May Annual Inflation: 2.1% (CPI-U), 2.1% (CPI-W), 9.9% (ShadowStats)
Housing Starts in a State of Volatile Stagnation
**Second-Quarter GDP Contraction Should Follow in Wake of
Continuing Downgrades of First-Quarter GDP Growth**

PLEASE NOTE: The next regular Commentary is scheduled for Wednesday, June 25th, covering the third estimate, second revision of first-quarter 2014 GDP, along with May new orders for durable goods and new- and existing-home sales.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Headline Annual Inflation Has Risen 100-Basis Points in Three Months. The headline 0.4% monthly increase in May 2014 CPI-U topped market expectations, and reflected the gain of a full-percentage point in headline annual inflation during the last three months. The increase in official inflation reporting has hit the point—against a severely weakening economy—that even the heavily understated headline inflation is accounting for more than all of the nominal growth in key measures of business activity. Such was seen in contracting inflation-adjusted real May retail sales and real earnings. The actual economy is so weak that the underlying contraction is surfacing in official reporting.

That circumstance has become a signal for severe underlying economic weakness. As discussed in the [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#) and detailed in the [Public Comment on Inflation](#), the use of understated inflation in estimating activity in series such as the GDP, real retail sales and industrial production, overstates actual economic activity, camouflaging the severity of an economic downturn and occasionally even masking an entire recession. When an economic downturn shows up in official reporting, such is a sign that a severe, actual economic contraction already is in place. In the current circumstance, as most headline real economic activity turns negative, headline GDP growth also should continue to do so.

Further Downside to First-Quarter GDP Reporting? As discussed in the *Week Ahead* section, market expectations are for another sharp-downside revision to first-quarter 2014 GDP, on June 25th. Where the initial reporting was for real annualized quarterly growth of 0.1%, the first revision took the headline change to a contraction of 1.0% (-1.0%). Second revision expectations are for a deeper contraction of 1.8% (-1.8%). The issue is that significant first-quarter growth—initially reported from the impact of the Affordable Care Act (ACA)—was instead a net contraction.

Second-Quarter GDP Growth Also a Likely Contraction. Based on April and May reporting, real retail sales, industrial production and housing starts activity are favoring flat-to-positive quarter-to-quarter changes for their respective series, not contractions. Although, that pattern should shift to the downside in the next round of reporting—with an early indicator on production out with the June 25th release on durable goods orders—what has been seen to date in these reasonably-volatile and unstable series is not at all inconsistent with an ongoing economic contraction.

Indeed, the odds are high of a second-quarter contraction, given early indications from the April trade data, and likely outright inventory liquidation in the quarter, as opposed to the first-quarter's slowing of inventory growth. Additionally, the consumer utility surge that still props up the current negative growth rate in the first-quarter, should reverse in the second quarter, and the ACA problem also should be an added drag on the second-quarter. In combination, these factors are enough to subtract roughly four-percentage points from the annualized second-quarter growth rate, more than offsetting any upside surprises in other reporting, and leaving the initial headline second-quarter growth in contraction.

This Commentary. Today's (June 17th) missive covers the headline reporting of the May consumer price index (CPI) and related series such as real retail sales and real earnings, as well as housing starts,

and it reviews the broad economic outlook in the context of May data and other factors. The usual gold versus silver, oil and the Swiss franc graphs are included at the end of the *Hyperinflation Watch* section.

Consumer Price Index—May 2014—Seasonals Start to Reverse, With Some Pending Catch Up in Headline Inflation Reporting. May was the first month in calendar-year 2014, where seasonal adjustments did not have the effect of meaningfully reducing headline-inflation reporting. The seasonal biases should switch to favoring higher headline-inflation reporting in the next several months.

CPI-U. The headline, seasonally-adjusted CPI-U for May 2014 rose month-to-month by 0.35% (rounds to 0.4%), versus a 0.26% headline increase in April. On a not seasonally-adjusted basis, the May CPI-U rose by 0.35% (rounds to 0.3%), while April rose by an unadjusted 0.33%. For the first time this calendar year, seasonal adjustments provided a boost (albeit absolutely minimal) to the headline inflation number.

Encompassed by the headline May 2014 CPI-U gain of 0.35% (up by 0.35% unadjusted), aggregate energy inflation in May was up by an adjusted 0.92% (up by an unadjusted 1.29%) for the month. In the other major CPI sectors, adjusted food inflation was up by 0.45% for the month (up by 0.40% unadjusted), while “core” inflation rose by an adjusted 0.33% (up by 0.25% unadjusted).

Not seasonally adjusted, May 2014 year-to-year inflation for the CPI-U was a gain of 2.13%, versus 1.95% in April, 1.51% in March and 1.13% in February, an increase in the annual rate of inflation by 100-basis points in three months.

CPI-W. The May 2014 headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.34% (up by 0.33% unadjusted), versus an adjusted gain of 0.29% (up by 0.38% unadjusted) in April. Unadjusted, May 2014 year-to-year CPI-W inflation rose to 2.10%, up from 1.96% in April, 1.41% in March and 0.98% in February.

Chained-CPI-U. Initial reporting of unadjusted year-to-year inflation for the May 2014 C-CPI-U was 1.98%, up from 1.80% in April, 1.36% in March and 0.97% in February.

Alternate Consumer Inflation Measures. The ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual inflation was roughly 5.7% in May 2014, up from 5.5% in April 2014. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, rose to about 9.9% in May, versus 9.7% in April.

Real (Inflation-Adjusted) Retail Sales—May 2014—Sales Gain Was All in Rising Headline Inflation. In nominal terms, before adjustment for inflation, headline monthly retail sales rose by 0.34% in May, versus a revised 0.50% (previously 0.09%) gain in April ([Commentary No. 634](#)). Based on today’s reporting of a 0.35% headline monthly gain in the May 2014 CPI-U, and in the context of the prior reporting of April CPI-U, seasonally-adjusted real (inflation-adjusted) monthly retail sales notched lower by 0.1% in May (-0.1%), following a revised 0.24% gain [previously a 0.17% decline (-0.17%)] in April.

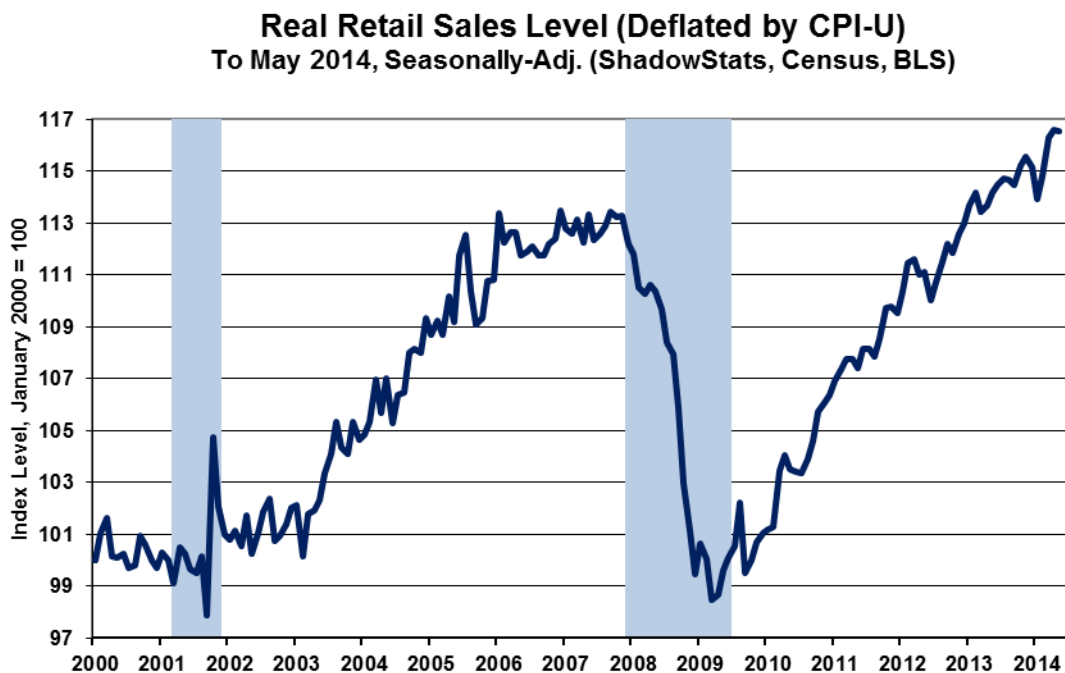
Year-to-year change in May 2014 real retail sales was a 2.07% gain, versus a revised 2.55% annual gain in April (see related graphs in the *Reporting Detail* section). In normal economic times, annual real growth falling below 2.0% would signal a pending recession. That signal had been given recently and

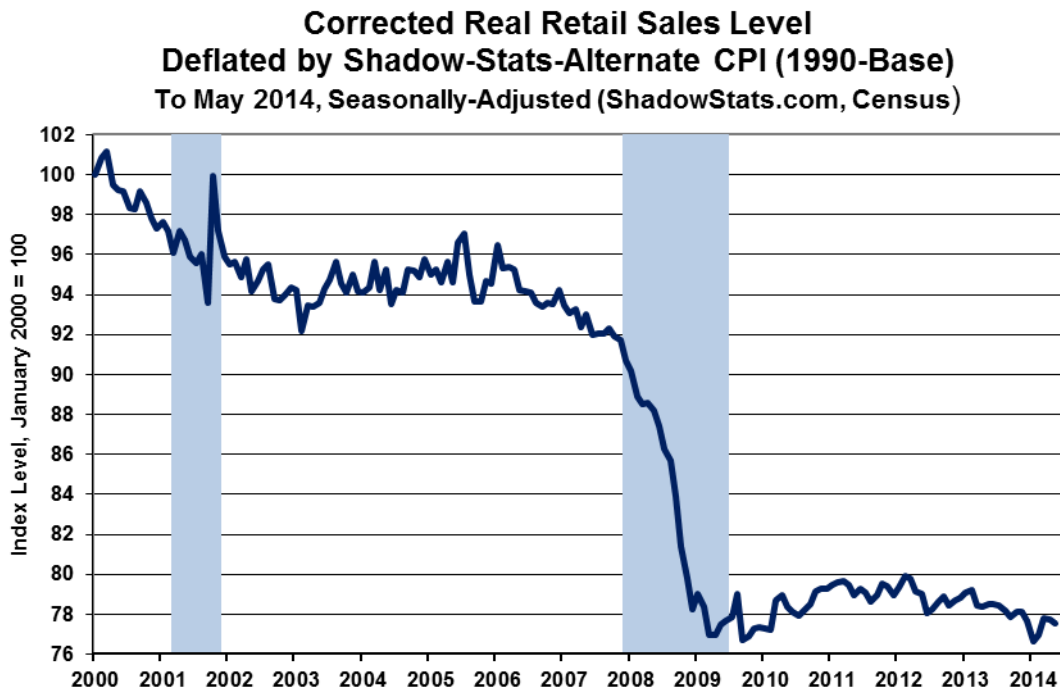
was approached anew in initial April reporting and now in initial reporting for May 2014. In the current circumstance, the signal likely will serve as an indicator of renewed downturn in broad economic activity.

No Fundamental Basis for Growth in Personal Consumption, Housing or Real Retail Sales. As discussed in [Commentary No. 632](#) and [Commentary No. 634](#), there has been no change in the underlying consumer-liquidity fundamentals. With low levels of stagnant, real household income and lack of the ability and/or willingness of the consumer to offset limited income with debt expansion, 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 real sales data should continue to trend meaningfully lower, in what rapidly should gain recognition as a formal new or double-dip recession.

Corrected Real Retail Sales. The apparent “recovery” in the headline real retail sales series, is due to the understatement of the rate of inflation used in deflating the retail sales and the other series. As discussed more fully in *Chapter 9* of [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

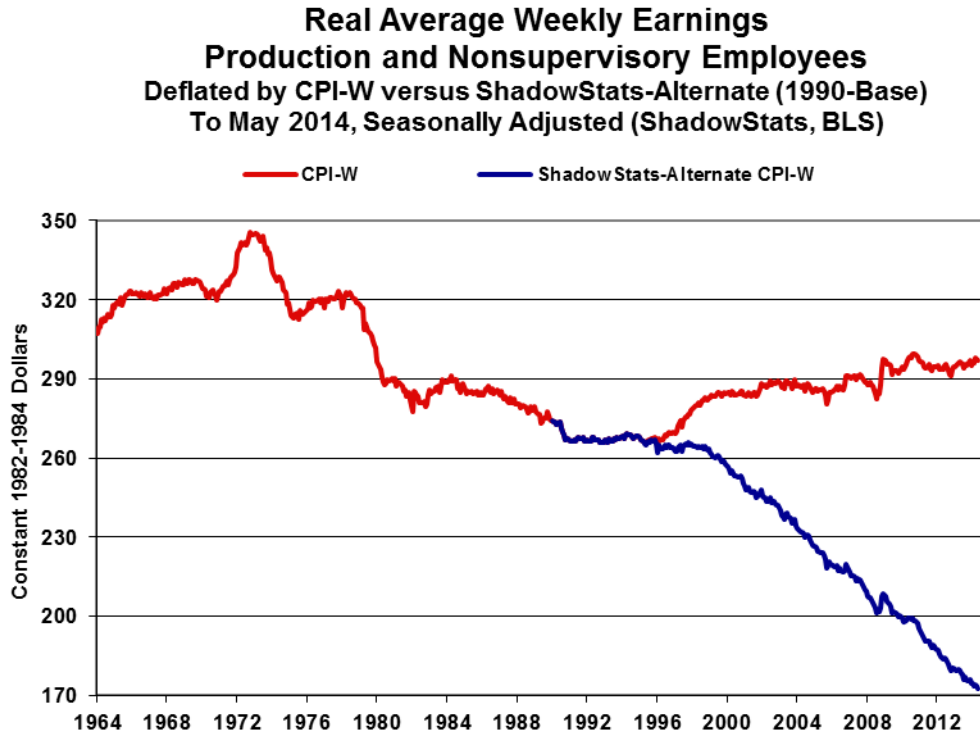




The first graph preceding reflects real retail sales as usually reported by the St. Louis Fed, deflated by the CPI-U, but it is indexed to January 2000 = 100. ShadowStats did the deflation using the May 2014 CPI-U and nominal retail sales releases. As seen in the first graph, official real retail sales recently recovered its pre-recession high, declined into 2014, hit a new post-recession high in April, as revised, and the flattened out in May. The headline recovery, though, is a statistical illusion. Even so, the first-quarter 2014 headline real retail sales activity contracted versus fourth-quarter 2013. That said, where the CPI-U understates inflation (see the [Public Comment on Inflation](#)), its use in calculating real retail sales has the effect of overstating actual inflation-adjusted activity.

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 and renewed downturn, 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 deepened, so far, in 2014.

Real (Inflation-Adjusted) Average Weekly Earnings—May 2014—Second Monthly Drop. Coincident with today’s CPI-W release, the BLS also published real average weekly earnings for May. 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) fell for the second month in a row, down by 0.19% (-0.19%) for May 2014, versus an unrevised 0.14% (-0.14%) decline in April, versus a revised 0.66% (previously 0.61%) gain in March.



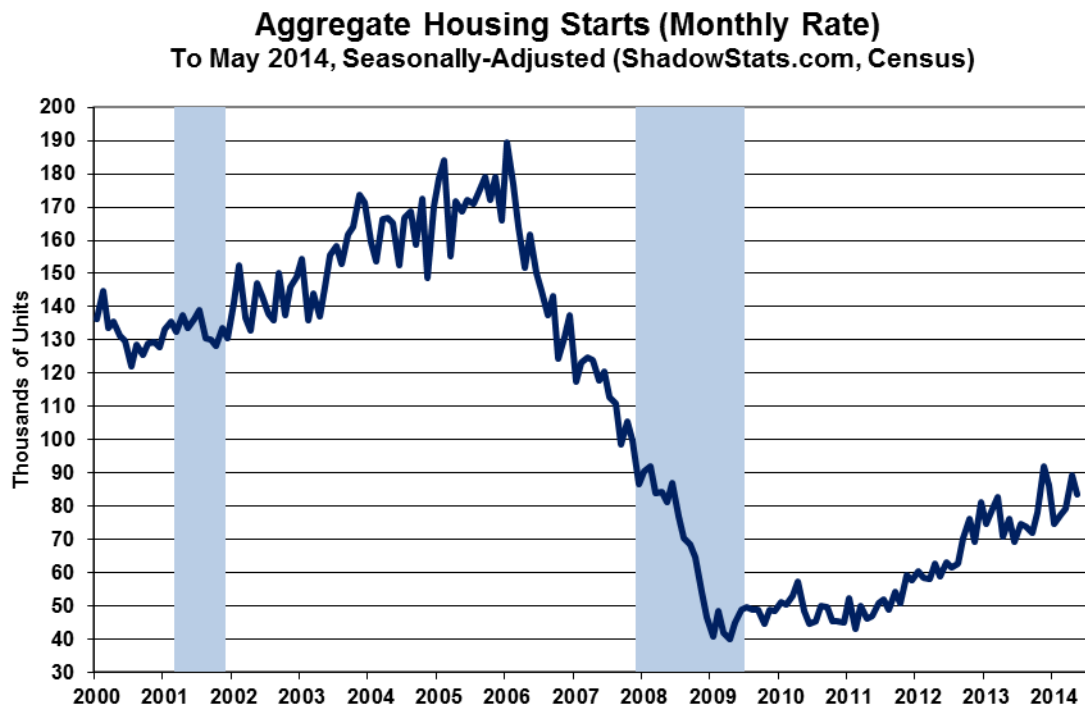
Year-to-year, May 2014 real average weekly earnings rose by 0.28%, versus a revised 0.37% gain in April, and versus a revised 0.54% gain in March. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility. Prior-period revisions usually are due to the instabilities in the BLS monthly surveys.

The accompanying regular graph of this series (above) 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.

Housing Starts—May 2014—Volatile Stagnation. The headline monthly contraction of 6.5% (-6.5%) in housing starts for May 2014 was not statistically significant, but it was mirrored in even less-significant monthly declines of 5.9% (-5.9%) and 7.6% (-7.6%), respectively, in single-unit and multiple-unit structures.

Aggregate housing starts in May 2014 still were 56.0% (-56.0%) below the pre-recession high seen in January 2006, and first-quarter 2014 activity contracted both quarter-to-quarter and year-to-year. Given the usual statistical insignificance of the broad monthly change (again the case in May), and the frequent, large prior-period revisions, the May 2014 number is indistinguishable, in terms of statistical significance, from the pace of first-quarter activity and should be viewed, accordingly, as relatively-stagnant activity versus first-quarter 2014. Aggregate detail is reflected in the accompanying graph and—in historical perspective—in the *Reporting Detail* section.

Encompassed in this general pattern of ongoing weakness in consumer-related real estate, and as discussed in [Commentary No. 632](#) and [Commentary No. 634](#), there have been no changes in the underlying consumer-liquidity structural problems that are constraining consumer spending and investment. There is nothing that would support a sustainable turnaround in the housing industry or general economic activity. There never was an economic recovery, and there is no recovery underway, just general bottom-bouncing that broadly is turning down anew.



May 2014 Housing-Starts Reporting. Headline May 2014 housing starts showed a statistically-insignificant, monthly headline contraction in seasonally-adjusted activity of 6.5% (-6.5%) +/- 11.9% (all confidence intervals are at the 95% level). The month-to-month gain was in the context of a negligible downside revision to headline April activity. Net of prior-period revisions, May housing starts fell by 6.6% (-6.6%). April starts were up by a revised 12.7% (previously a 13.6% gain). Reporting in the

housing starts series remained highly unstable, and it generally has been unstable enough in recent years that headline month-to-month changes in activity rarely have been statistically significant.

Year-to-year change in the seasonally-adjusted, aggregate May 2014 housing-starts measure was a statistically-insignificant gain of 9.4% +/- 1.9%, versus a revised 26.3% (previously 26.4%) annual gain in April.

By-Unit Category. Where the irregular housing starts series can show varying patterns, that partially is due to a reporting mix of residential construction products, with the largest physical-count category of one-unit housing starts—generally for individual consumption—resulting in new home sales, versus multi-unit starts that generally reflect the building of rental and apartment units.

Housing starts for single-unit structures in May fell month-to-month by a statistically-insignificant 5.9% (-5.9%) +/- 13.9%, following a revised 4.6% (previously 0.8%) gain in April. May's year-to-year gain of 4.7% +/- 12.4% also was statistically-insignificant, following a revised 12.4% (previously a 9.8% annual gain in April).

Reporting of housing starts for apartment buildings (generally 5-units-or-more) in May 2014 fell by 8.3% (-8.3%) +/- 25.4%, versus a revised 32.6% (previously 42.9%) gain in April. On a year-to-year basis, May's gain of 19.2% +/- 29.7% was statistically-insignificant. April's year-to-year gain revised to 64.2% (previously 70.0%).

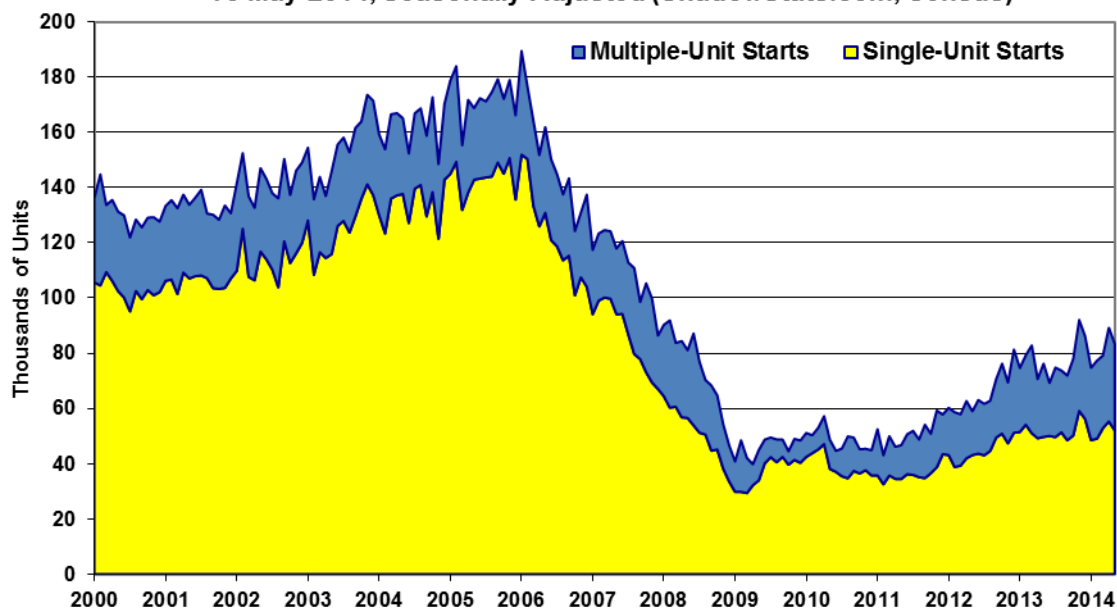
Expanding the multi-unit housing starts category to include 2-to-4-units plus 5-units-or-more usually reflects the bulk of rental- and apartment-unit activity. The Census Bureau does not publish estimates of the 2-to-4-units category, due to statistical significance problems. Nonetheless, the total multi-unit category can be calculated by subtracting the single-unit category from the total category.

Accordingly, statistically-insignificant aggregate May monthly contraction of 6.5% (-6.5%) was composed of a 5.9% (-5.9%) decline in one-unit housing starts, combined with a 7.6% (-7.6%) monthly contraction of multiple-unit structures (2-units-or-more, including the 5-units-or-more category), as reflected in the accompanying graphs.

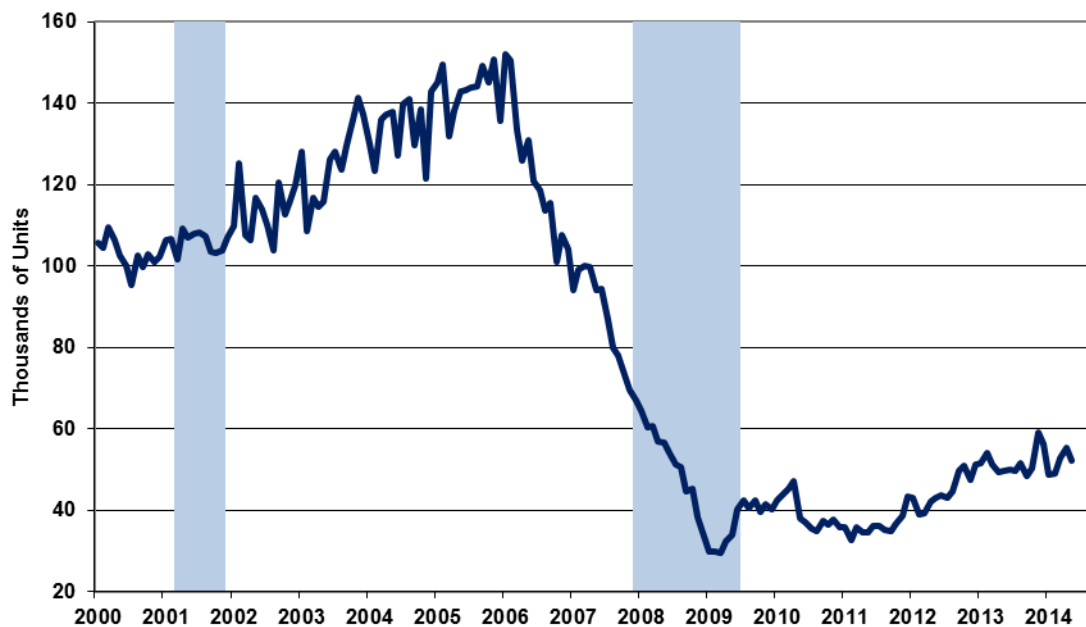
Graphs of Housing Starts Activity. Headline reporting of housing starts is expressed at an annualized monthly pace, which was 1,001,000 in May 2014, versus a revised 1,071,000 in April. Those details are shown in aggregate graphs in the *Reporting Detail* section. Where the magnitude of monthly activity more realistically is reflected at the actual monthly rate of 83,417 in May, versus the annualized headline 1,001,000, the monthly rate scale is used in the accompanying graphs in this section. With either scale, the appearance of the graph and the monthly and annual percent changes are the same.

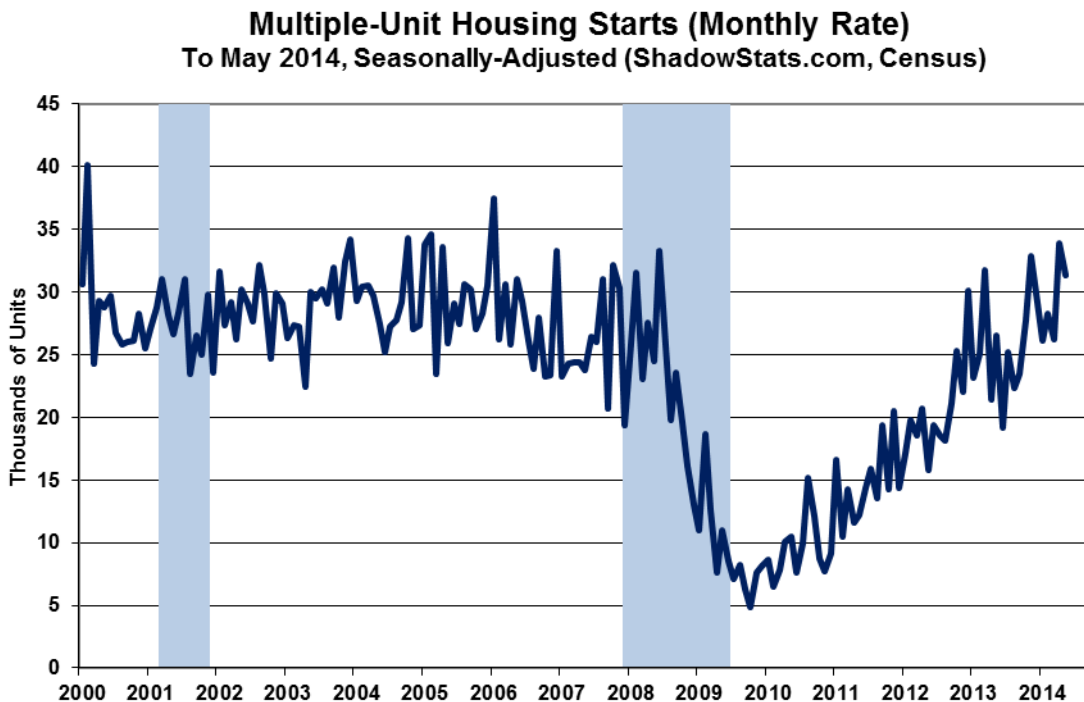
The record monthly low seen for the present aggregate series was in April 2009, where the annualized monthly pace of sales was down 79% (-79%) from the January 2006 pre-recession peak. Against the downside-spiked low in April 2009, the May 2014 headline number was up by 109%, but it still was down by 56% (-56%) from the January 2006 series high.

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



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





*[For further details on May CPI, real retail sales and earnings, and housing starts, see the **Reporting Detail** section.]*

[Various drill-down detail and graphics options for the headline May CPI and housing starts are available to our readers at ShadowStats-affiliate www.ExpliStats.com.]

HYPERINFLATION WATCH

Hyperinflation Summary Outlook. *[PLEASE NOTE: Other than for the italicized text in the next paragraph, and minor language clean up, the text in this summary is unchanged from the prior Commentary.]* The hyperinflation and economic outlooks were updated 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. A basic summary of the broad outlook is found in the *Opening Comments* and *Overview and Executive Summary* in the *First Installment Revised*. The broad outlook for a hyperinflationary great depression beginning

this year has not changed—only evolved—with various details continuing to fall into place. A formal and more-condensed summary of the extraordinarily-difficult times ahead will take over this section, soon. What follows here is still-evolving detail on the economic disaster, all to be incorporated into that summary.

Economy Turns Down Anew. Consistent with the above *Special Commentaries*, a renewed U.S. business slowdown/downturn was evident in the revised headline contraction of 1.0% in first-quarter 2014 GDP, versus 2.6% growth in fourth-quarter 2013, *and what likely will be reemphasized with a possible further downside revision to the first-quarter numbers in the week ahead. At the same time, the popular outlook for second-quarter GDP should shift increasingly into the recession camp (see the Opening Comments), with the annual GDP revisions and initial second-quarter GDP reporting looming on July 30th. As financial-market expectations increasingly shift towards renewed or deepening recession, that circumstance, in confluence with other fundamental issues, should place mounting and massive selling pressure on the U.S. dollar, as well as potentially resurrect elements of the 2008-Panic.*

Intensifying weakness in the U.S. dollar will place upside pressure on oil prices and other commodities, boosting inflation and inflation fears. Both the dollar weakness and resulting higher inflation should boost the prices of gold and silver, where physical holding of those key precious metals remains the primary hedge against the pending inflation and financial crises.

The fundamental issues threatening the dollar, again, include, but are not limited to: the U.S. government not addressing its long-term solvency issues; monetary malfeasance by the Federal Reserve seeking to provide liquidity to a troubled banking system, and to the U.S. Treasury, with a current pace of 69% monetization of effective net issuance of public federal debt; a mounting domestic and global crisis of confidence in a dysfunctional U.S. government; mounting global political pressures contrary to U.S. interests; and a severely damaged U.S. economy, which never recovered post-2008 and is turning down anew (including a sharply widening trade deficit).

GDP Contractions. Generally reflecting weaker numbers in revisions to underlying data, downside revisions to recent GDP reporting are increasingly likely in the July 30th annual benchmark revisions. Underlying, current economic activity actually is deteriorating and weak enough that the benchmark GDP revision should be accompanied by an initial headline contraction in second-quarter 2014 GDP, on top of a deepening first-quarter 2014 GDP contraction, which faces two further near-term revisions (including the benchmark).

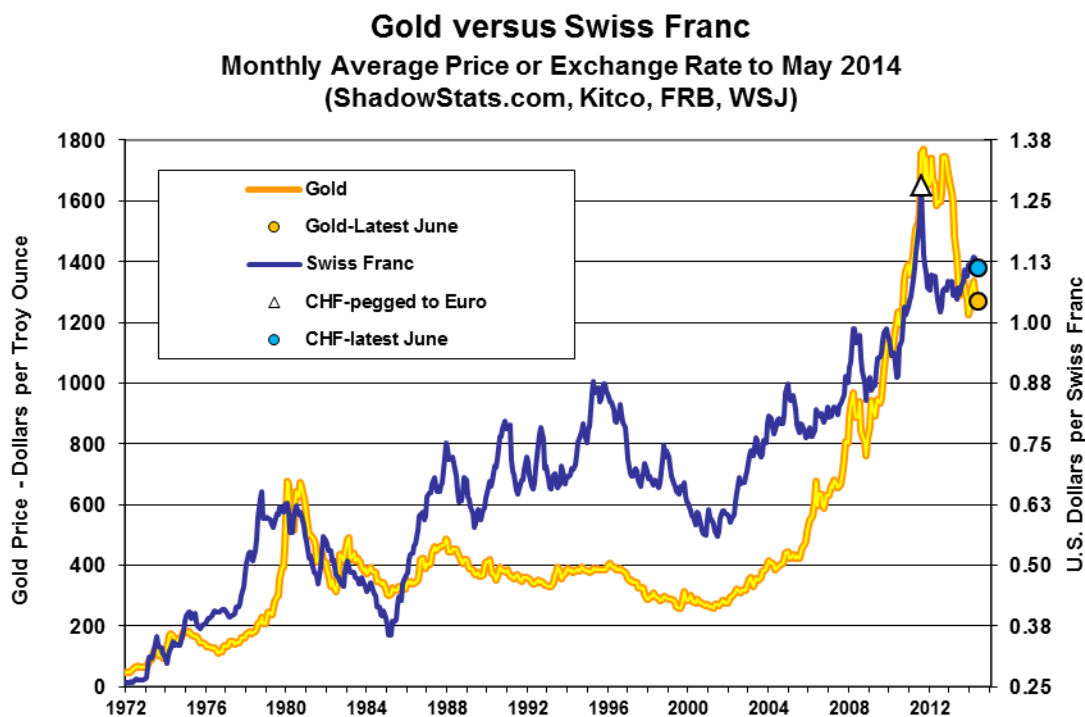
With continued deterioration in the trade deficit (see [Commentary No. 632](#)) and underlying weakness in labor conditions (see [Commentary No. 633](#)), broad deterioration remains likely in general economic activity and inflation conditions, despite the *relatively positive May production report*. As those patterns continue to unfold, market expectations—and related financial-market reactions—again should move into the “renewed recession” camp before or coincident with the July 30th annual revisions to GDP.

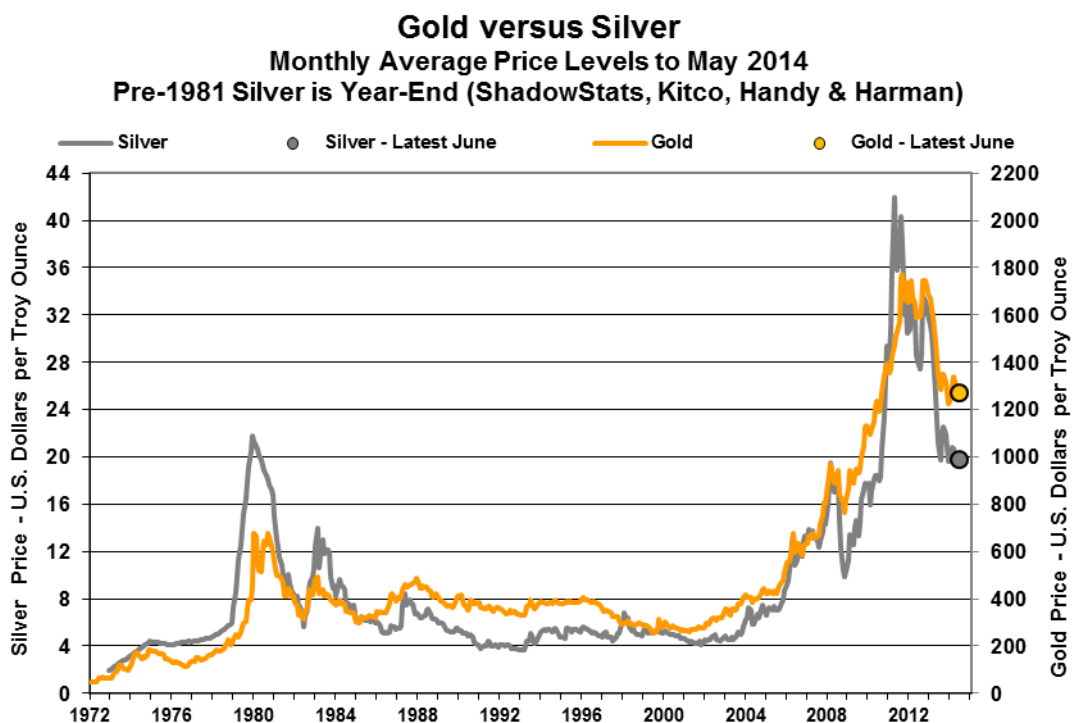
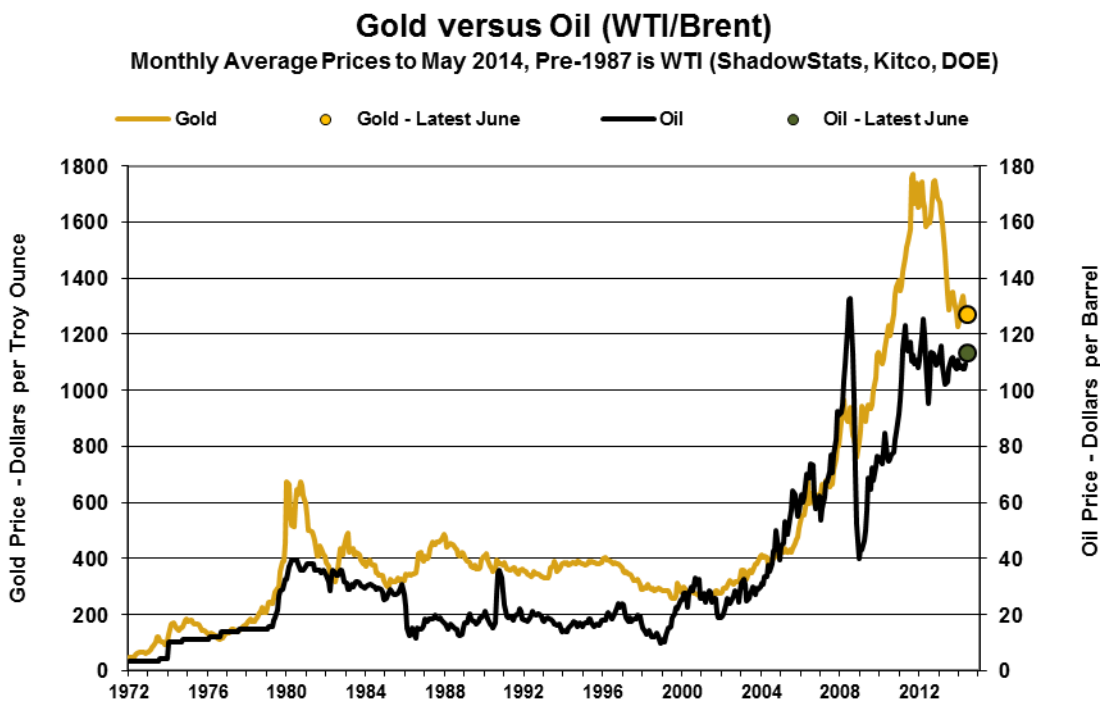
Monthly Gold Graphs. Following are the regular graphs of gold prices versus the Swiss franc, oil prices and silver prices that usually accompany the *Commentary* on the monthly CPI release. Volatile markets continue, amidst mounting global political tensions, a rapidly weakening U.S. economy and nascent recognition of rising inflation. Related market fears also center on worsening fiscal and monetary

instabilities, and deteriorating domestic political circumstances. All these issues have sharply negative implications for the U.S. dollar, which remains a good bet to be an early casualty. Precious metals and oil prices would benefit from a weakened U.S. dollar.

As discussed in the two installments of the *2014 Hyperinflation Report*, linked above, 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 unusual price volatility in the last year or two. More-recent oil price volatility has reflected intensifying global political instabilities, but oil prices also will face significant, further upside pressure as the U.S. dollar comes under heavy selling pressure.

The “latest June” points in the following graphs reflect approximate conditions as of late-afternoon New York time, June 17th.





REPORTING DETAIL

CONSUMER PRICE INDEX—CPI (May 2014)

Headline Annual Inflation Has Risen 100-Basis Points in Three Months. The headline 0.4% monthly gain in the May 2014 CPI-U topped market expectations, and reflected the gain of a full-percentage point in headline annual inflation in the last three months. The increase in official inflation reporting has hit the point with a weakening economy that it increasingly is accounting for more than all of the nominal growth, as seen in the reporting of contracting May real, inflation-adjusted retail sales and real earnings. As headline real economic activity turns negative, the GDP growth also should continue to do so.

At the same time, May reporting was the first in calendar-year 2014 in which seasonal adjustments did not have the effect of meaningfully reducing headline inflation reporting. The biases should swing in a direction of higher headline inflation in the next several months.

Going forward, and as discussed in [2014 Hyperinflation Report—The End Game Begins](#) – *First Installment Revised*, risks of a massive flight from the U.S. dollar threaten upside energy and global-commodity inflation, which would drive headline consumer inflation much higher. The nascent dollar problems could accelerate at any time, with little warning. Renewed financial-market turmoil surrounding deteriorating global and domestic political, fiscal and monetary instabilities, and rapidly worsening economic activity, 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—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, June 17th, that the headline, seasonally-adjusted CPI-U for May 2014 rose month-to-month by 0.4% (0.35% at the second decimal point). The April CPI-U had increased by 0.3% (0.26% at the second decimal point). On a not seasonally-adjusted basis, the May CPI-U rose by 0.35% (rounds to 0.3%), where April CPI-U rose by an unadjusted 0.33%. For the first time this calendar year, seasonal adjustments provided a boost (albeit absolutely minimal) to the headline inflation number.

Monthly Gasoline Prices. The BLS used a gain of 0.7% in not-seasonally-adjusted gasoline prices, above the 0.4% increase indicated by the more-comprehensive, industry-based surveying of the Department of Energy. Although last year’s numbers showed some seasonal spike to gasoline, the adjusted gain in May 2014 gasoline prices also was unchanged, at 0.7%. Seasonal adjustments actually were negative for aggregate energy inflation, but were positive for monthly food inflation as well as for the headline “core” inflation, net of food and energy price increases.

Major CPI Groups. Encompassed by the headline May 2014 CPI-U gain of 0.35% (up by 0.35% unadjusted), aggregate energy inflation in May was up by an adjusted 0.92% (up by an unadjusted 1.29%) for the month. In the other major CPI sectors, adjusted food inflation was up by 0.45% for the month (up by 0.40% unadjusted), while “core” inflation rose by an adjusted 0.33% (up by 0.25% unadjusted).

Year-to-Year CPI-U. Not seasonally adjusted, May 2014 year-to-year inflation for the CPI-U was a gain of 2.13%, versus 1.95% in April, 1.51% in March and 1.13% in February, an increase in the annual rate of inflation by 100-basis points in three months.

Year-to-year, CPI-U inflation would increase or decrease in next month’s June 2014 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.32% gain in the monthly inflation reported for June 2013. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for June 2014, the difference in June’s

headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the May 2014 annual inflation rate of 2.13%.

Core CPI-U. Seasonally-adjusted May 2014 “core” CPI-U inflation (net of food and energy inflation) rose 0.33% (0.25% unadjusted), versus an adjusted increase of 0.24% (0.25% unadjusted) in April. Year-to-year “core” inflation was 2.03% in May, versus 1.83% in April 2014, 1.66% in March and 1.57% in February.

CPI-W. The May 2014 headline, seasonally-adjusted CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.34% (up by 0.33% unadjusted), versus an adjusted gain of 0.29% (up by 0.38% unadjusted) in April, versus an adjusted 0.19% gain (up by 0.73% unadjusted) in March, and an adjusted 0.05% gain in February (up by 0.36% unadjusted). Unadjusted, May 2014 year-to-year CPI-W inflation rose to 2.10%, up from 1.96% in April, 1.41% in March and 0.98% in February.

Chained-CPI-U. Initial reporting of unadjusted year-to-year inflation for the May 2014 C-CPI-U was 1.98%, up from 1.80% in April, 1.36% in March and 0.97% in February.

[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](#).

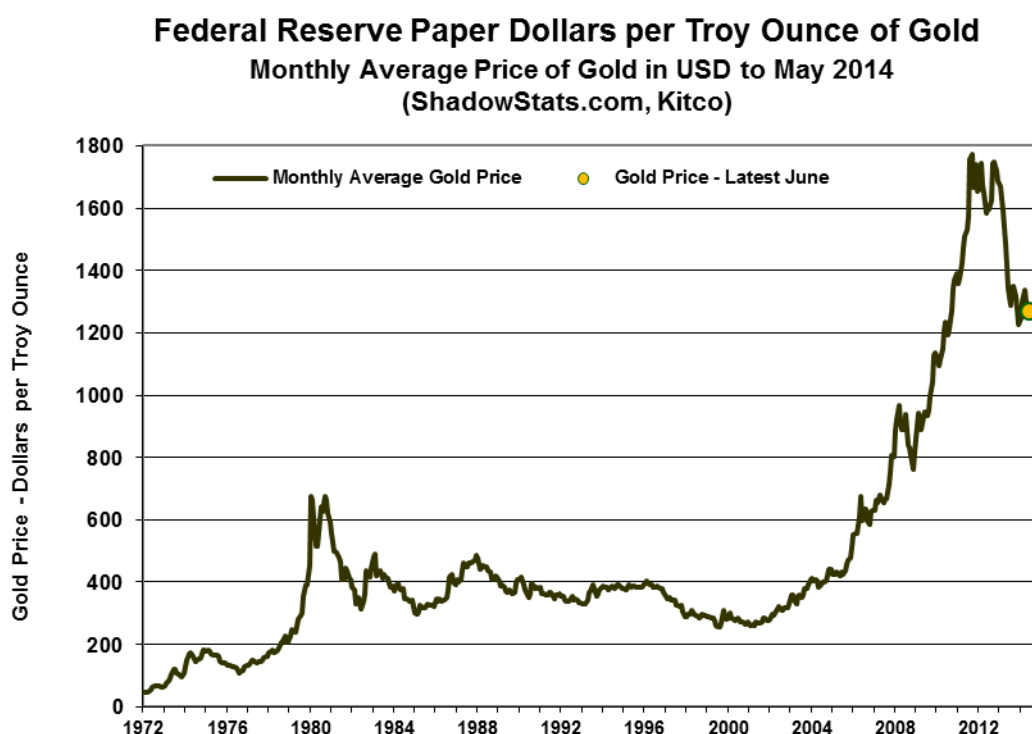
Alternate Consumer Inflation Measures. Adjusted to pre-Clinton methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual inflation was roughly 5.7% in May 2014, up from 5.5% in April 2014. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, rose to about 9.9% (9.86% for those using the second decimal point) in May, versus 9.7% in April.

[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 \$2,599 per troy ounce, based on May 2014 CPI-U-adjusted dollars, and \$11,048 per troy ounce, based on May 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 May 2014 CPI-U inflation, the 1980

silver-price peak would be \$151 per troy ounce and would be \$643 per troy ounce in terms of May 2014 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

As shown in Table 1, on page 31 of [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), 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—May 2014. In nominal terms, before adjustment for inflation, headline monthly retail sales rose by 0.34% in May, versus a revised 0.50% (previously 0.09%) gain in April ([Commentary No. 634](#)). Based on today's reporting of a 0.35% headline monthly gain in the May 2014 CPI-U, and in the context of prior April CPI-U reporting, seasonally-adjusted real (inflation-adjusted) monthly retail sales notched lower by 0.1% in May (-0.1%), following a revised 0.24% gain (previously a 0.17% decline) in April.

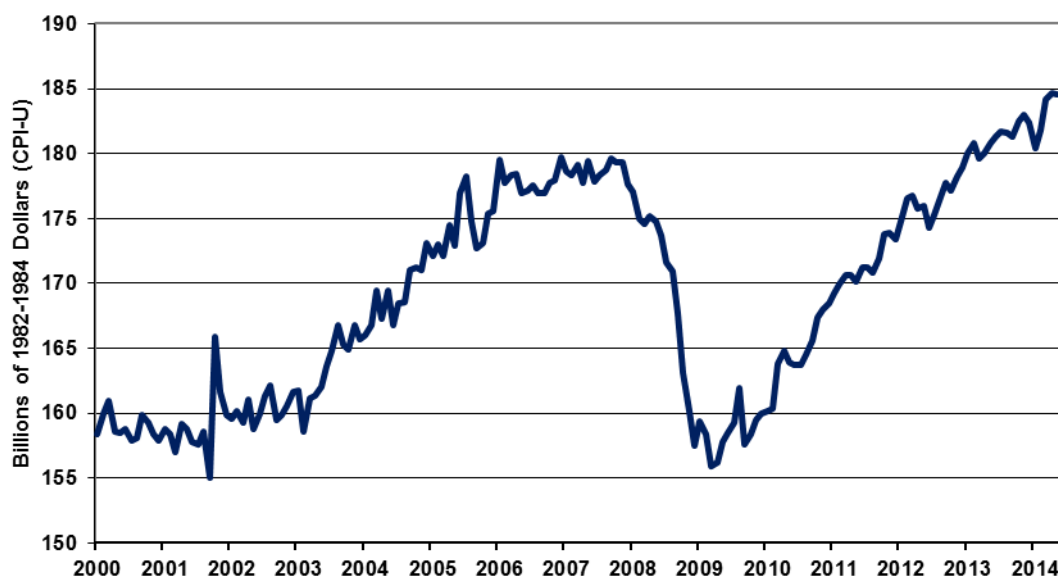
Year-to-year change in May 2014 real retail sales was a 2.07% gain, versus a revised 2.55% (previously 2.05%) annual gain in April, as shown in the second and fourth graphs following. In normal economic times, annual real growth falling below 2.0% would signal a pending recession. That signal had been given recently and was approached anew in initial April reporting and now initial reporting for May 2014. In the current circumstance, the signal likely will serve as an indicator of renewed downturn in broad economic activity.

Real Retail Sales Graphs. The first of the four graphs preceding 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 a bounce-back in February and March (and now April, in revision), with May to the downside of flat. Year-to-year activity, which had plunged to a near-standstill in January and February, also bounced back some in March, leveled off in April, and pulled back sharply in May. The third and fourth graphs show the level of and annual growth in real retail sales (and its predecessor series) in full post-World War II detail.

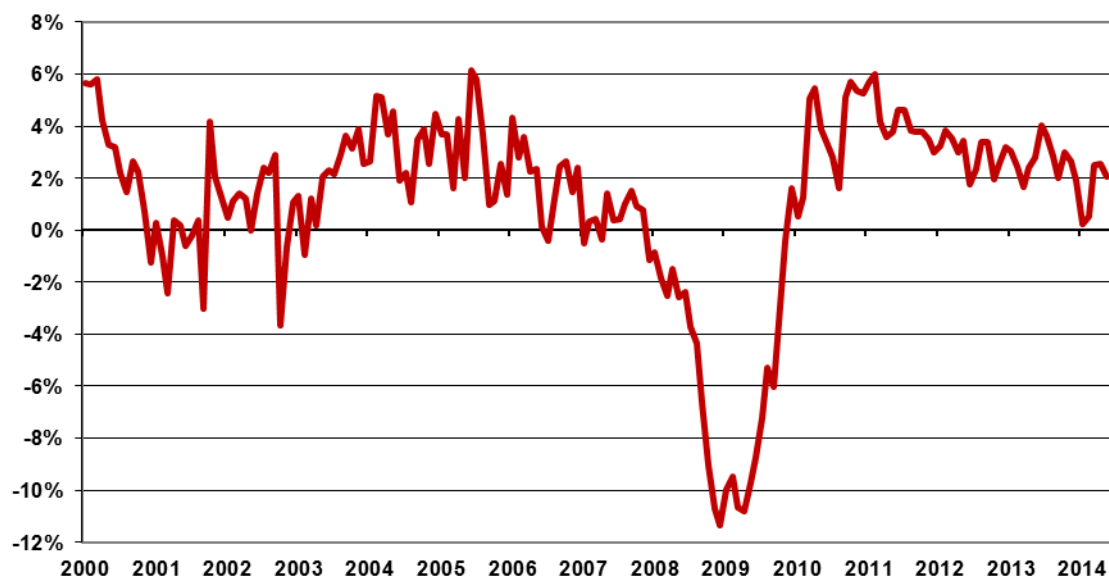
The gross domestic product (GDP) expanded beyond pre-recession levels twelve quarters ago, starting in second-quarter 2011, and it has kept rising, well beyond the reported activity of any other series, including real retail sales and industrial production. There is no other major economic series showing 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 has fluttered since, still holding above pre-recession levels (see [Commentary No. 635](#)).

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 *Chapter 9* of [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

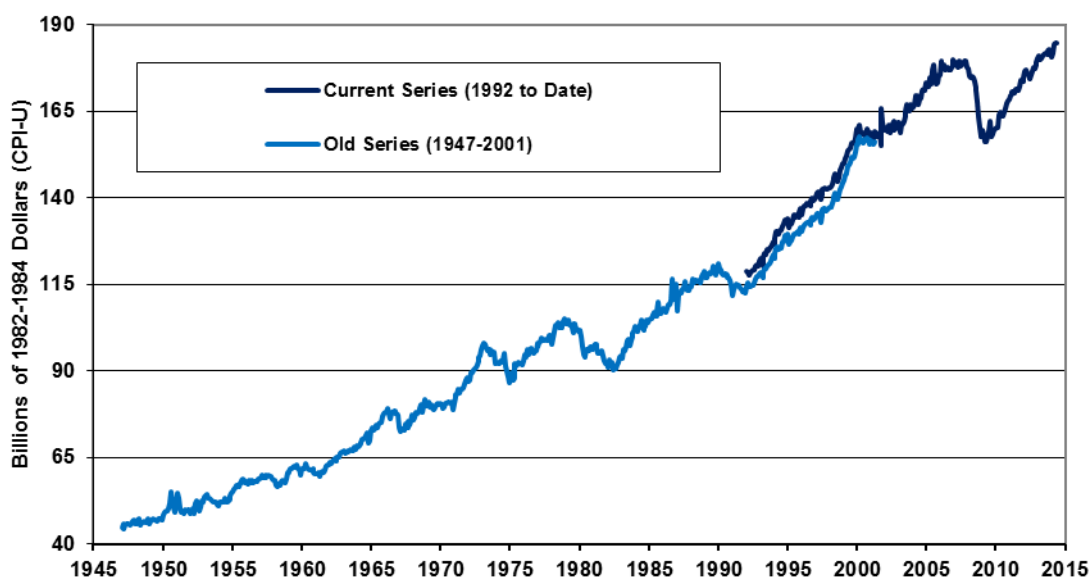
**Real Retail Sales (Deflated by CPI-U), Revised
To May 2014, Seasonally-Adj. (ShadowStats, Census, BLS)**



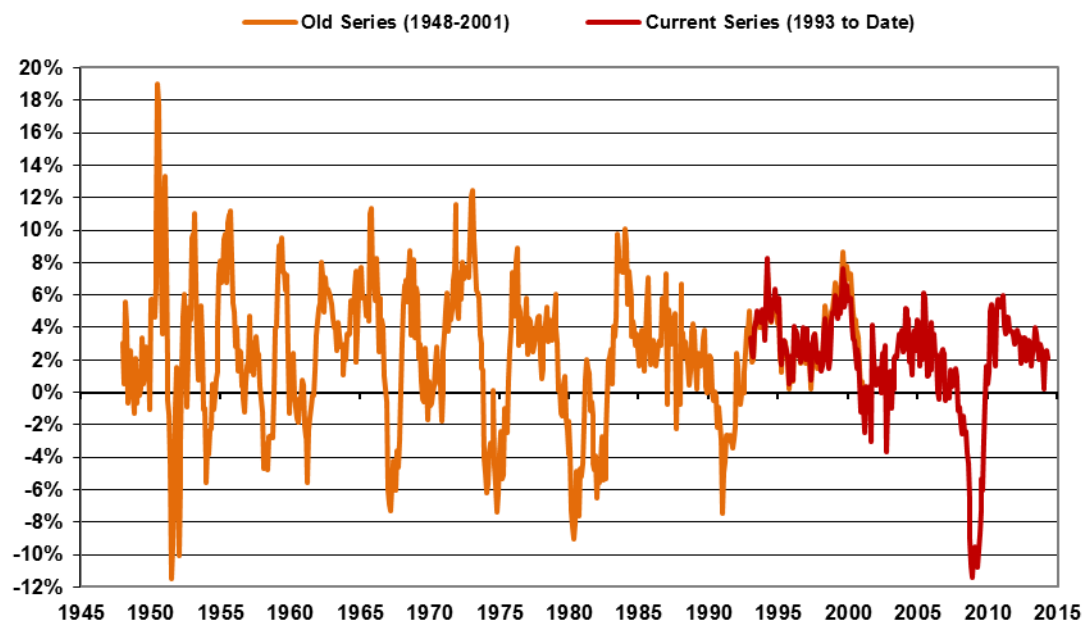
**Real Retail Sales Year-to-Year % Change
To May 2014, Seasonally-Adj. (ShadowStats, Census, BLS)**



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



Real Retail Sales Yr/Yr Percent Change
To May 2014, Seasonally-Adj. (ShadowStats, St. Louis Fed)



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.

Also, as discussed in [Commentary No. 632](#) and [Commentary No. 634](#), there has been no change in the underlying consumer-liquidity fundamentals. With low levels of stagnant, real household income and lack of the ability and/or willingness of the consumer to offset limited income with debt expansion, 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.

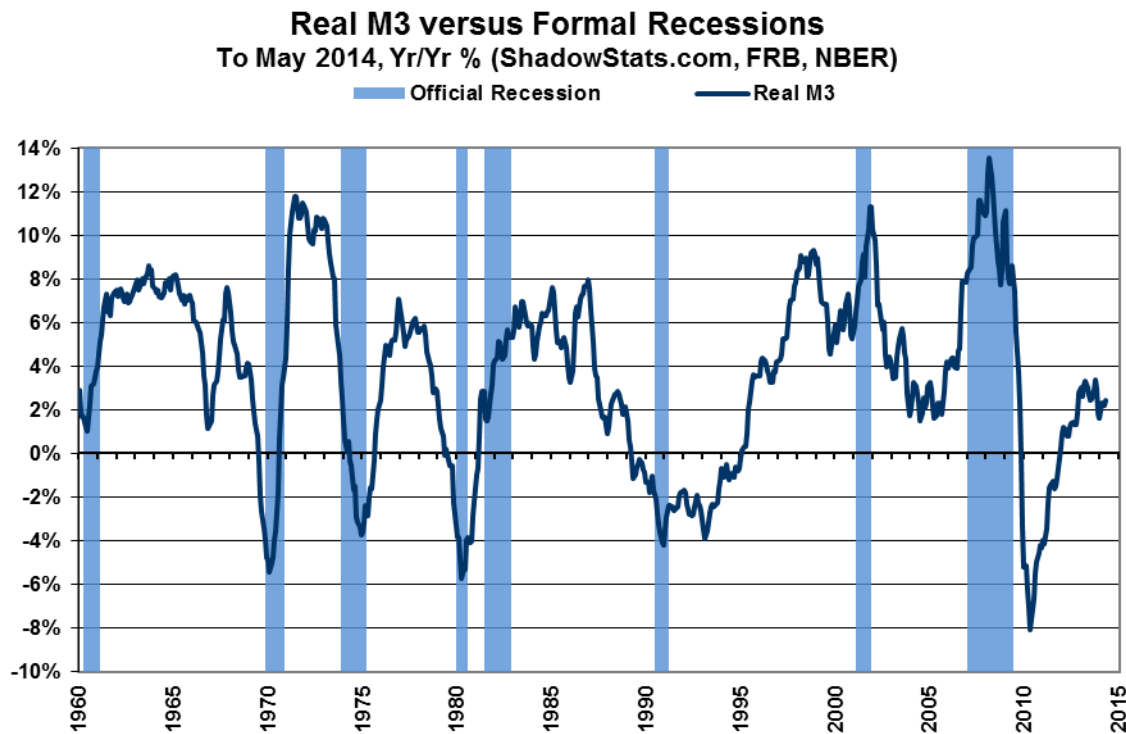
As official consumer inflation continues its upturn in the months ahead, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze—reflected partially by continued real earnings difficulties, discussed in the next section—these data should continue to trend meaningfully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

Real (Inflation-Adjusted) Average Weekly Earnings—May 2014. Coincident with today's May 2014 CPI-W release, the BLS also published real average weekly earnings for May. 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) fell by 0.19% in May (-0.19%), versus an unrevised 0.14% decline in April (-0.14%), versus a revised 0.66% (previously 0.61%) gain in March.

Year-to-year, May 2014 real average weekly earnings rose by 0.28%, versus a revised 0.37% (previously 0.32%) gain in April, and versus a revised 0.54% (previously 0.50%) gain in March. 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—May 2014. The signal for a double-dip or ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), remains in place and continues, despite real annual M3 growth holding in positive territory. As shown in the accompanying graph—based on May 2014 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in M3 for May 2014 notched higher to 2.4% from an unrevised 2.2% in April. The slight pickup in the May annual growth rate reflected a somewhat stronger gain in annual headline M3 growth than in the annual CPI-U inflation.



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.

A renewed downturn in official data appears to be underway, and that eventually could 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. Further discussion of this issue is found in *Chapter 8* of the [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#).

RESIDENTIAL CONSTRUCTION (May 2014)

Housing-Starts Activity Remained in Volatile Stagnation. The May headline monthly contraction of 6.5% (-6.5%) in housing starts was not statistically significant, but it was mirrored in even less-significant monthly declines of 5.9% (-5.9%) and 7.6% (-7.6%), respectively in single-unit and multiple-unit structures.

Aggregate housing starts in May 2014 still were 56.0% (-56.0%) below the pre-recession high seen in January 2006, and first-quarter 2014 activity contracted both quarter-to-quarter and year-to-year. Given the usual statistical insignificance of the broad monthly change (again the case in May), and the frequent, large prior-period revisions, the May 2014 number is indistinguishable, in terms of statistical significance, from the pace of first-quarter activity and should be viewed, accordingly, as relatively-stagnant activity versus first-quarter 2014.

Encompassed in this general pattern of ongoing weakness, and as discussed in [Commentary No. 632](#) and [Commentary No. 634](#), there have been no changes in the underlying consumer-liquidity structural problems that are constraining consumer spending and investment. There is nothing that would support a sustainable turnaround in the housing industry or general economic activity. There never was an economic recovery, and there is no recovery underway, just general bottom-bouncing that broadly is turning down anew.

May 2014 Housing-Starts Reporting. The Census Bureau reported today, June 17th, a statistically-insignificant, monthly headline contraction in the seasonally-adjusted level of May 2014 housing starts of 6.5% (-6.5%) +/- 11.9% (all confidence intervals are at the 95% level). The month-to-month gain was in the context of a negligible downside revision to headline April activity. Net of prior-period revisions, May housing starts fell by a still-statistically-insignificant 6.6% (-6.6%). April starts were up by a revised 12.7% (previously a 13.6% gain).

Year-to-year change in the seasonally-adjusted, aggregate May 2014 housing-starts measure was a statistically-insignificant gain of 9.4% +/- 1.9%, versus a revised 26.3% (previously 26.4%) annual gain in April.

Reporting in the housing starts series remains highly unstable, and it generally has been unstable enough in recent years that headline month-to-month changes in activity rarely have been statistically significant.

By-Unit Category (See Graphs in the Opening Comments). Where the irregular housing starts series can show varying patterns, that partially is due to a reporting mix of residential construction products, with the largest physical-count category of one-unit housing starts—generally for individual consumption—resulting in new home sales, versus multi-unit starts that generally reflect the building of rental and apartment units.

Housing starts for single-unit structures in May fell month-to-month by a statistically-insignificant 5.9% (-5.9%) +/- 13.9%, following a revised 4.6% (previously 0.8%) gain in April. May's year-to-year gain of 4.7% +/- 12.4% also was statistically-insignificant, following a revised 12.4% (previously a 9.8% annual gain in April).

Reporting of housing starts for apartment buildings (generally 5-units-or-more) in May 2014 fell by 8.3% (-8.3%) +/- 25.4%, versus a revised 32.6% (previously 42.9%) gain in April. On a year-to-year basis, May's year-to-year gain of 19.2% +/- 29.7% was statistically-insignificant. April's year-to-year gain revised to 64.2% (previously 70.0%).

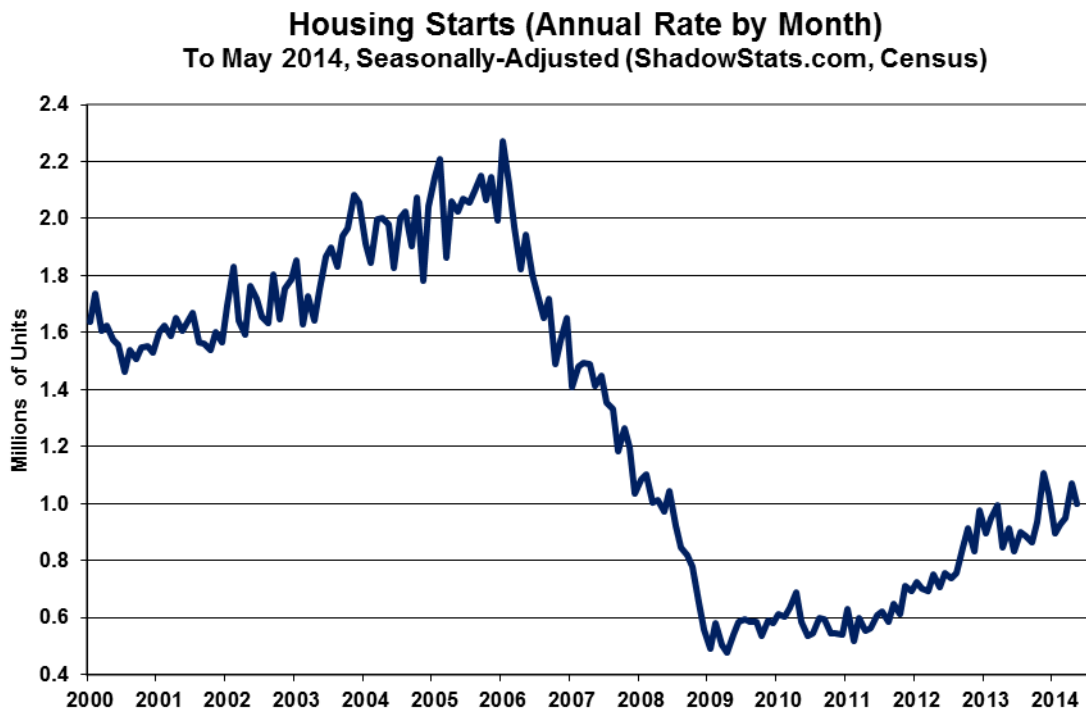
Expanding the multi-unit housing starts category to include 2-to-4-units plus 5-units-or-more usually reflects the bulk of rental- and apartment-unit activity. The Census Bureau does not publish estimates of the 2-to-4-units category, due to statistical significance problems (a general issue for the aggregate series).

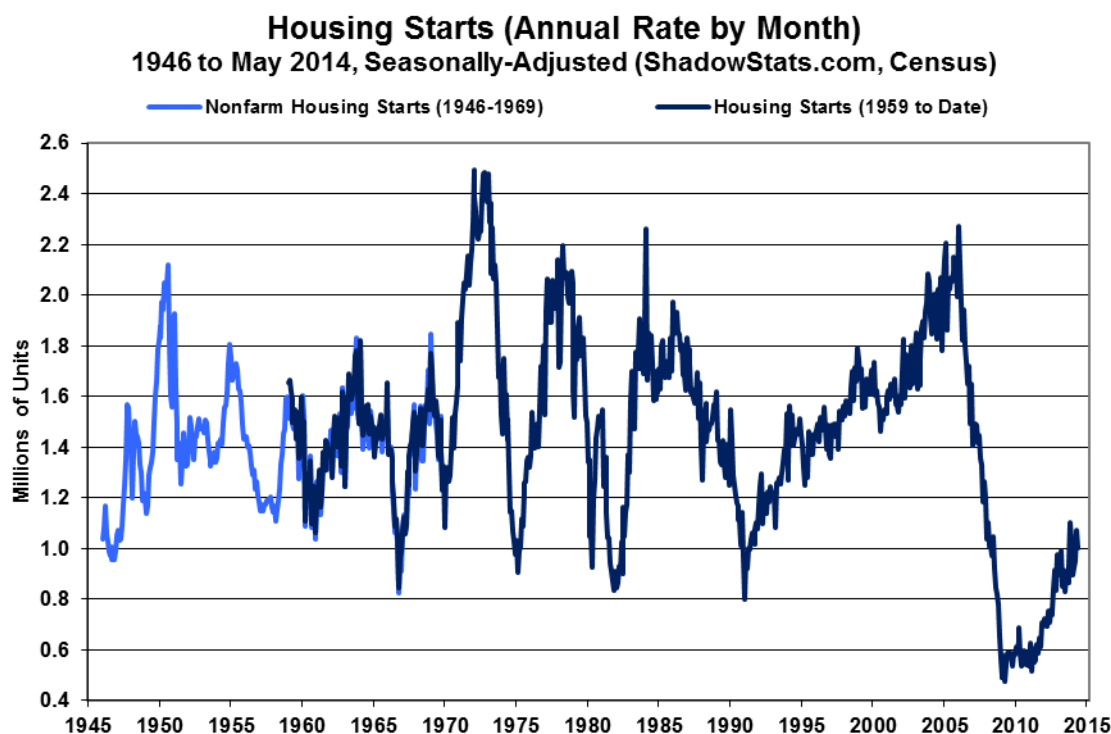
Nonetheless, the total multi-unit category can be calculated by subtracting the single-unit category from the total category.

Accordingly, statistically-insignificant aggregate May monthly contraction of 6.5% (-6.5%) was composed of a 5.9% (-5.9%) decline in one-unit housing starts, combined with a 7.6% (-7.6%) monthly contraction of multiple-unit structures (2-units-or-more, including the 5-units-or-more category). The breakout of these series is graphed in the *Opening Comments* section.

Graphs of Aggregate Housing Starts Activity. Headline reporting of housing starts is expressed at an annualized monthly pace of starts, which was 1,001,000 in May 2014, versus a revised 1,071,000 in April. Those details are shown in the following, aggregate graphs. Where the magnitude of monthly activity more realistically is reflected at the actual monthly rate of 83,417 in May, versus the annualized headline 1,001,000, the monthly rate is used in the scales of the graphs in the *Opening Comments* section. With either scale, the appearance of the graph and the monthly and annual percent changes are the same.

The record monthly low seen for the present aggregate series was in April 2009, where the annualized monthly pace of sales was down 79% (-79%) from the January 2006 pre-recession peak. Against the downside-spiked low in April 2009, the May 2014 headline number was up by 109%, but it still was down by 56% (-56%) from the January 2006 series high.





WEEK AHEAD

Much-Weaker-Economic and Stronger-Inflation Reporting Likely in the Months and Year Ahead.

Although shifting to the downside, amidst fluctuations, market expectations generally still appear to be overly optimistic as to the economic outlook. Expectations should continue to be hammered, though, by ongoing downside corrective revisions and an accelerating pace of downturn in headline economic activity. The initial stages of that process have been seen in the recent headline reporting of many major economic series (see [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#)), including the second estimate of real first-quarter 2014 GDP, which was the first contemporary reporting of a quarterly contraction since the formal end of the 2007 recession in mid-2009.

Weakening, underlying economic fundamentals indicate still further deterioration in 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 also remains likely, as has been seen in recent reporting. Upside pressure on oil-related prices should reflect intensifying impact from global political instabilities and a weakening U.S. dollar in the currency markets. Food inflation has been picking up as well. The dollar faces pummeling from the weakening economy, continuing QE3, the ongoing U.S. fiscal-crisis debacle, and deteriorating U.S. and global political conditions (see [*Hyperinflation 2014—The End Game Begins \(Updated\)*](#) – *First Installment*). 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:

Existing- and New-Home Sales (May 2014). May 2014 existing-home sales are due for release on Monday, June 23rd, from the National Association of Realtors, with the May 2014 new-home sales report from the Census Bureau due on Tuesday, June 24th.

A pattern of stagnation or intensifying downturn appears to be in play for both the existing- and new-home sales. In particular, a renewed downtrend has been unfolding in existing-home sales. While monthly changes in home-sales activity usually are not statistically-significant, still-unstable reporting and revisions (both likely to the downside) also remain a fair bet for the new-home sales series. Both series remain highly volatile.

New Orders for Durable Goods (May 2014). The reporting of May 2014 new orders for durable goods is scheduled for Wednesday, June 25th, by the Census Bureau. Other than for the continuing sharp and irregular volatility in commercial aircraft orders, new orders generally have been stagnant, plus or minus, particularly net of inflation. Commercial aircraft orders usually are booked years in advance with relatively minimal impact on near-term production activity. Net of the unstable aircraft reporting, some intensification in downside activity is likely, coincident with slowing activity seen recently in the broad economy. Market expectations appear to be for flat-to-minus orders, with headline reporting a fair bet to disappoint expectations on the downside.

Gross Domestic Product—GDP (First-Quarter 2014, Third Estimate, Second Revision). The Bureau of Economic Analysis (BEA) has scheduled its release of the third estimate of, second revision to, first-quarter 2014 GDP for Wednesday, June 25th. Expectations appear to be for a further sharp downside revision to the headline real annualized growth in first-quarter 2014 GDP. The initial headline reporting

was plus 0.1% for the quarter. The first revision took that to a contraction, minus 1.0% (-1.0%). Bloomberg currently is showing expectations for a revised quarterly contraction of 1.8% (-1.8%).

The issue is that initial estimates of personal consumption healthcare expenditures—purportedly boosted strongly by the Affordable Healthcare Act during the quarter—did not increase as advertised, but rather contracted. The market expectations for a downside revision are reasonable. Similar healthcare-boosting patterns were assumed as part of still relatively strong market expectations for second-quarter GDP growth, and downside revisions to those expectations also are likely (see the *Opening Comments* section). The first-quarter GDP number will be revised again on July 30th, as part of the annual benchmark revision, along with the release of the initial estimate of second-quarter 2014 GDP growth.
