

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

COMMENTARY NUMBER 637
GDP Revision, Durable Goods Orders, New- and Existing-Home Sales
June 25, 2014

**Collapsing First-Quarter 2014 Economic Activity (GDP, GNP and GDI)
Fell Below Third-Quarter 2013 Levels**

GDP Activity Fell, Even Before Adjusting for Slowing Inventory Growth

Quarterly GDP Activity Contracted, Even Before Adjusting for Inflation

**Looming Second-Quarter Economic Contraction Likely to
Formalize “Renewed” Recession and to Hit Markets Hard**

Durable Goods Orders Turned Down in Otherwise Stagnant Activity

Despite Monthly Gain, Existing-Homes Sales Continued in Annual Contraction

**Neither Monthly nor Annual New-Home Sales Gain
Was Statistically-Significant**

PLEASE NOTE: The next regular Commentary is scheduled for Thursday, July 3rd, covering June employment and unemployment, the May trade deficit and construction spending.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Severe First-Quarter GDP Contraction Sets Background for Looming Second-Quarter Downturn.

Today's (June 25th) missive covers the headline reporting of the second revision to first-quarter GDP, May reporting of new orders for durable goods and the May estimates on existing- and new-home sales. The impact of upcoming economic releases on the outlook for second-quarter GDP will be assessed in the appropriate *Commentaries* as the new data are published.

The downside "second" revision to first-quarter GDP was particularly severe and should help to move consensus expectations away from a second-quarter economic boom, and towards a second-quarter economic contraction. Two back-to-back quarterly contractions in GDP would meet most definitions of a formal recession. The economic factors that pulled the first-quarter GDP into a deep contraction continue to promise trouble for the second-quarter. Keep in mind that the consensus outlook had been for ongoing positive GDP growth in the first-quarter, until the initial headline reporting hit.

The small downturn in headline May new orders for durable goods was in the context of stagnant activity. Similarly, the headline "gains" in May new- and existing home sales either were statistically insignificant, and/or were in the context of contracting annual activity. Nothing in these releases suggested surging economic growth for second-quarter 2014.

As noted in the prior [Commentary No. 636](#), 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. That should shift to the downside in the upcoming round of reporting, although the non-GDP data discussed in this *Commentary* are more-flat to minus in perspective

Odds remain high of a second-quarter contraction, given early indications from the widening April trade deficit (see *Week Ahead* section for next week's May reporting), and likely outright inventory liquidation in the quarter, as opposed to the first-quarter's "slowing" of inventory growth. Additionally, the consumer surge in utility consumption that still props up the current negative growth rate in the first-quarter GDP, should reverse in the second quarter, and ongoing Affordable Care Act problems also should be a continued drag on second-quarter growth. In combination, these factors are enough to subtract roughly four-percentage points from the annualized second-quarter GDP growth rate, more than offsetting any upside reporting, and leaving the initial headline second-quarter growth in contraction.

Benchmark GDP Revision on July 30th. The Bureau of Economic Analysis (BEA) will release its annual revisions of GDP for the last three years, with partial revisions going back to first-quarter 1999, along with still another revision to first-quarter 2014 GDP and the initial estimate of second-quarter 2014 GDP. Generally, downside revisions are likely to GDP reporting of recent years, but that detail will be covered in a separate *Commentary* in advance of the revisions.

Incorporating benchmark revisions from other series, the July 30th GDP benchmark should show a weaker pattern of growth in recent years, with downside revision patterns and trends leading into second-quarter 2014 GDP reporting. The revisions could show the "renewed" recession to have been in place

before first-quarter 2014. Accordingly, odds remain high that the market outlook and consensus will have shifted meaningfully towards the renewed-recession camp by the July GDP benchmark, if not before then.

As sentiment shifts in that direction, global markets should respond with increased selling pressure against the U.S. dollar, with resulting upside inflationary pressures on oil and other commodities. In turn gold and silver prices should rally in response to the global weakness in the dollar and to the nascent, rising inflationary pressures. Physical gold and silver remain the primary hedges against the financial and inflation turmoil ahead. Please see [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), and [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#) for details.

Gross Domestic Product—First-Quarter 2014, Second Revision—Deepening Contraction Sets Stage for “Renewed” Recession. Even with all the upside gimmicks built into gross domestic product (GDP) reporting, actual underlying economic activity is so weak as to generate a meaningful contraction in the formal and official headline first-quarter GDP.

The severity of the current economic downturn was emphasized by large downside revisions to key economic growth patterns, including features not otherwise seen since the onset of the official 2007 recession. The latest downside revisions reflected primarily a large reversal in the guesstimated economic impact of the Affordable Care Act (ACA), from a positive contribution to GDP growth of 1.01%, to a negative contribution of 0.16% (-0.16%), along with a revised widening of the trade deficit. As a result, the headline contraction for first-quarter GDP deepened to 2.93% (-2.93%) from 0.98% (-0.98%) in the prior reporting, and a reversal of direction from the 0.11% gain in initial reporting.

Annualized real (inflation-adjusted) quarterly contractions deepened sharply for the GDP, the broader gross national product (GNP) and the GDP’s theoretical equivalent of gross domestic income (GDI), along with meaningful slowing in annual growth. First-quarter 2014 GDP, GNP and GDI measures of activity officially fell below the same measures for third-quarter 2013 (two quarters ago), let alone the sharp fall-off versus the prior fourth-quarter 2013 reporting. Second-quarter 2014 GDP activity would have to rebound by 3.0% in order to regain the level of real fourth-quarter 2013 GDP activity. Nonetheless, an outright GDP contraction in second-quarter 2014 remains likely.

Final sales—GDP net of changes in inventories—revised into outright contraction, down at an annualized pace of 1.23% (-1.23%) in the first-quarter, having shown positive growth of 0.66% at the prior revision. Inventory growth slowed during the quarter (minimal inventory revisions in the latest detail), which was an economic negative. Nonetheless, with final sales or GDP activity—net of inventory swings—still in contraction, that takes the aggregate first-quarter GDP contraction outside the scope of being a simple inventory adjustment.

Of equal significance, before adjustment for inflation, the nominal GDP, GNP and GDI all contracted quarter-to-quarter, showing unfolding patterns not seen since the early days of the official 2007 economic crash.

The issue for the economy is not the heavily-touted bad weather in first-quarter 2014 and a potential second-quarter recovery from same, but rather ongoing, severe structural liquidity constraints on the

consumer, as last discussed in [Commentary No. 632](#), [Commentary No. 634](#) and in the *Consumer Liquidity* discussion later in this section.

As to the weather, a surge in consumer utility usage still largely offsets any negative impact from the unseasonable weather on other areas of activity during the first-quarter. That pattern will tend to reverse in the second-quarter, with utility surge reversing, with offsets to weather-related gains. The major negative factors in the first-quarter GDP generally were not weather related. Little affected by the weather, a slowdown in inventory growth and a marked deterioration in the trade deficit accounted for the bulk of the contraction in first-quarter GDP. Those inventory and trade factors both should be ongoing issues in second-quarter GDP reporting.

Headline Gross Domestic Product (GDP). The third estimate of, and second revision to first-quarter 2014 GDP showed a revised, statistically-insignificant, real (inflation-adjusted), annualized, quarterly contraction of 2.93% (-2.93%). Previously, the headline first-quarter change in activity had been a contraction of 0.98% (-0.98%), versus an initial estimate of a 0.11% gain. That was against a 2.63% headline gain in fourth-quarter 2013.

In nominal terms, before inflation adjustment, first-quarter GDP contracted at an annualized pace of 1.71% (-1.71%), versus nominal annualized growth of 4.25% in fourth-quarter 2013. Year-to-year nominal GDP growth slowed to 2.91% in first-quarter 2014, from 4.08% in fourth-quarter 2013.

The latest year-to-year or annual rates of change for the real-GDP series are graphed in the *Reporting Detail* section. First-quarter 2014 GDP year-to-year growth was a revised 1.54%, versus 2.59% in fourth-quarter 2013.

Implicit Price Deflator (IPD). The third estimate of first-quarter 2014 GDP inflation, or the implicit price deflator (IPD), was at a revised annualized quarterly pace of 1.26%, versus 1.58% in fourth-quarter 2013. Year-to-year, first-quarter 2014 IPD inflation was a revised 1.34%, versus 1.45% in fourth-quarter 2013. For comparison purposes, on a seasonally-adjusted, annualized quarter-to-quarter basis, headline CPI-U inflation was up by 1.91% in first-quarter 2014, versus 1.14% in fourth-quarter 2013. On a year-to-year basis, first-quarter 2014 CPI-U (unadjusted) inflation was 0.86%, versus 1.23% in fourth-quarter 2013. Generally, the weaker the inflation rate used in deflating an economic series, the stronger will be the resulting inflation-adjusted growth.

Gross National Product (GNP). The second estimate of first-quarter 2014 real GNP showed a revised, annualized quarter-to-quarter contraction of 3.61% (-3.61%) [initially down by 2.11% (-2.11%)], following a 3.06% gain in fourth-quarter 2013. In terms of year-to-year change, annual growth slowed to a revised 1.59% in first-quarter 2014, from 2.69% in fourth-quarter 2013. Again, annualized first-quarter GDP was a 2.91% contraction, versus a 2.63% gain in the fourth-quarter.

In nominal terms, before inflation adjustment, first-quarter GNP contracted at an annualized pace of 2.39% (-2.39%), versus nominal annualized growth of 4.68% in fourth-quarter 2013.

GNP is the broadest measure of U.S. economic activity, where GDP is GNP net of trade flows in factor income (interest and dividend payments). As a reporting gimmick aimed at boosting the headline reporting of economic growth for net-debtor nations such as Greece and the United States, international reporting standards were shifted some decades back to reporting headline GDP instead of GNP.

The relatively greater quarterly contraction in U.S. first-quarter 2014 GNP, versus the GDP, fully reflected a sharp deterioration in the net flow of factor income between the United States and the rest of the world. The net deterioration was due to a large falloff in U.S. receipts from the rest of the world in first-quarter 2014, plus a second quarterly increase in U.S. payments to the rest of the world.

Gross Domestic Income (GDI). GDI is the theoretical income-side equivalent of the consumption-side GDP estimate. The GDP and GDI are made to equal each other with the addition of a “statistical discrepancy” to the GDI-side of the equation, but the discrepancy just as easily could be added to the GDP number. Net of the statistical discrepancy, the estimate of headline real GDI annualized quarterly change for first-quarter 2014 was a contraction of 2.61% (-2.61%) [initially down by 2.26% (-2.26%)], versus growth of 2.60% in the fourth-quarter. Year-to-year annual growth slowed to a revised 1.22% in first-quarter 2014, versus 2.51% in the fourth-quarter.

In nominal terms, before inflation adjustment, first-quarter GDI contracted at an annualized pace of 1.39% (-1.39%), versus nominal annualized growth of 4.22% in fourth-quarter 2013.

Distribution of Headline GDP Growth. Despite the severely-limited significance of the following detail, it is included for those interested in the reported internal patterns of GDP growth, as guessed at by the BEA. The third estimate, second revision, of headline change in first-quarter 2014 GDP was for a contraction of 2.93% (-2.93%). That annualized contraction rate is detailed in the following aggregation of contributed growth. Please note that the annualized growth number in each sub-category is the additive contribution to the aggregate, headline change in GDP, where $0.71\% - 1.97\% - 1.53\% - 0.14\% = -2.93\%$. The prior aggregate headline GDP change was estimated at a contraction of 0.98% (-0.98%) in the first revision, and at positive growth of 0.11% for the initial first-quarter estimate. Headline GDP growth was 2.63% in fourth-quarter 2013:

- **Consumer Spending Contributed 0.71% (Previously 2.09%, Initially 2.04%) to First-Quarter Growth; 2.22% in Fourth-Quarter.** Consumer-dependent personal consumption accounts for 68% of the GDP, but the outright contraction in first-quarter retail sales was not evident in the first-quarter personal-consumption headline reporting or detail. The largest downside revision to consumption was reversal in healthcare consumption from contributing 1.01% to the aggregate growth rate in the prior estimate, to subtracting 0.16% (-0.16%) in the current estimate. Somehow the government previously had misread the “positive” contribution from the Affordable Care Act to first-quarter 2014 activity. The remaining big “plus” in personal consumption was utility consumption (contributing 0.79% to the aggregate growth rate), which resulted from bad-weather effects, which should reverse in second-quarter reporting.
- **Business/Residential Investment Subtracted 1.97% (-1.97%) [Previously 1.98% (-1.98%), Initially 1.01% (-1.01%)] from First-Quarter Growth; Contributed 0.41% to Fourth-Quarter.** The contraction in private investment was changed from the prior estimate. The contraction here largely reflected a continued slowdown in inventory build-up, which knocked 1.70% (previously 1.62%, initially 0.57%) off the headline GDP growth rate. Accordingly “final sales”—GDP net of inventory change—was at a revised, annualized contraction of 1.23% (-1.23%), previously a gain of 0.64%, initially a gain of 0.66%, versus 2.61% growth in fourth-quarter 2013. Importantly, the first-quarter contraction no longer is just an inventory correction.
- **Net Exports Subtracted 1.53% (-1.53%) [Previously 0.95% (-0.95%), Initially 0.83% (-0.83%)] from First-Quarter Growth; Contributed 0.99% to Fourth-Quarter.** Consistent with some of the

recent revisions to the trade series, the trade data provided the second large component in the downside revision to headline first-quarter GDP growth. Next week's release of the May trade data largely will set the pace of a likely negative trade contribution to the initial estimate of second-quarter 2014 GDP (see *Week Ahead* section).

- **Government Spending Subtracted 0.14% (-0.14%) [Previously 0.15% (-0.15%), Initially 0.09% (-0.09%)] from First-Quarter Growth; Subtracted 0.99% (-0.99%) in Fourth-Quarter.** Federal government spending made an unrevised 0.05% positive contribution to first-quarter GDP growth (0.16% positive from nondefense, 0.11% negative from defense), otherwise dominated by a revised contributing contraction of 0.18% (-0.18%), previously down by 0.20% (-0.20%), initially down by 0.14% (-0.14%), from spending by state and local governments.

Economic Reality. With first-quarter 2014 GDP growth formally in severe contraction, the general outlook has not been altered. The broad economy has turned down anew, and the second-quarter GDP is likely to follow the first-quarter in contraction. Accordingly, the gist of much of the following text is along the lines of other recent GDP commentaries, but the details and numbers have been updated for today's third reporting of aggregate first-quarter 2014 economic activity.

The GDP remains the most-worthless and the most-heavily modeled, massaged and politically-manipulated of government economic series. It does not reflect properly or accurately the changes to the underlying fundamentals that drive the economy. Underlying real-world economic activity suggests that the broad economy began to turn down in 2006 and 2007, plunged into 2009, entered a protracted period of stagnation thereafter—never recovering—and then began to turn down anew in second- and third-quarter 2012 (see [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), and [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#)). Irrespective of the reporting gimmicks introduced in the July 2013 GDP benchmark revision (beware upcoming July 30, 2014 revisions), the consistent, fundamental pattern of historical activity is shown in the accompanying two sets of “corrected” GDP graphs.

Please note that the pattern of activity shown for the “corrected” GDP series is much closer to the patterns shown in the graphs of monthly real median household income and other liquidity measures (see [Commentary No. 632](#) and [Commentary No. 634](#) and the *Consumer Liquidity* comments in this *Opening Comments* section) and of economic series not otherwise reliant on understated inflation for their reported growth (see the second installment of the *Hyperinflation Report*). A sustainable business recovery could not have taken place since 2009, and a recovery will not be forthcoming until the consumer's structural income and liquidity problems are resolved.

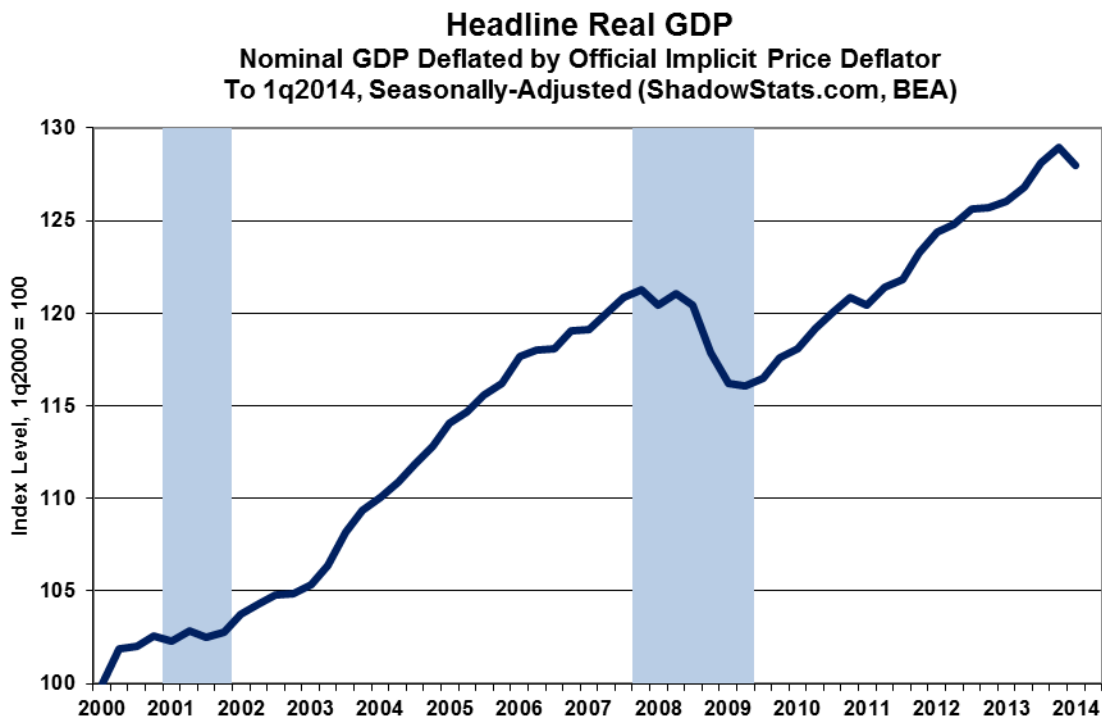
Official and Corrected GDP. As usually discussed in the *Commentaries* covering the quarterly GDP reporting and monthly revisions, the full economic recovery indicated by the official, real GDP numbers remains an illusion. It is a statistical illusion created by using too-low a rate of inflation in deflating (removing inflation effects) from the GDP series. The accompanying two sets of graphs tell that story, updated for the third estimate of first-quarter 2014 GDP.

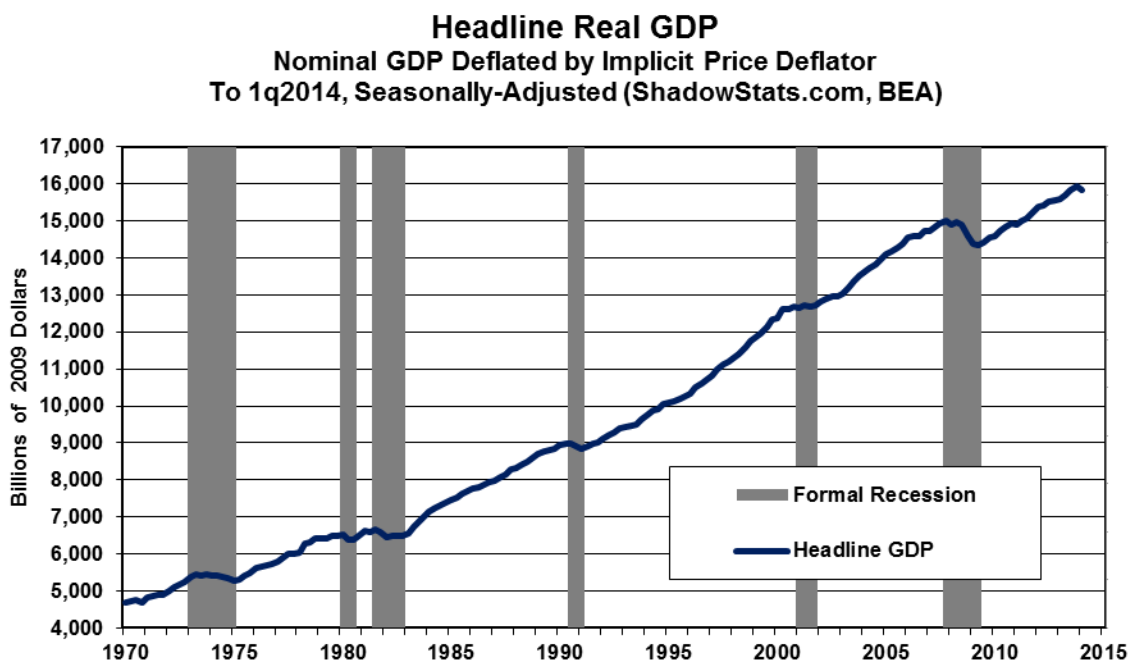
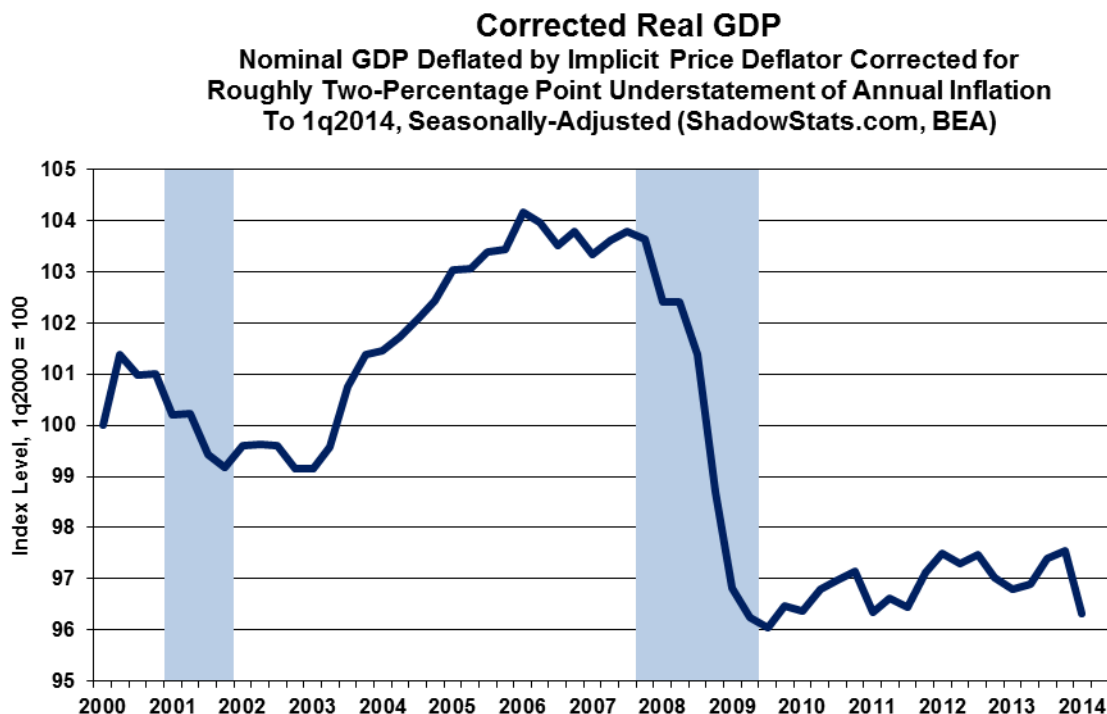
The first set of graphs (2000-to-date) is the one traditionally incorporated in the *GDP Commentaries*. The second set updates the longer-term graphs (1970-to-date), published in [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#).

Shown in the first graph of official *Headline Real GDP*, GDP activity has been reported above pre-2007 recession levels—in full recovery—since second-quarter 2011 (it had been fourth-quarter 2011 before the July 2013 benchmarking), and headline GDP had shown sustained growth since, now in a deepening downturn with the second first-quarter 2014 revision. Adjusted for official GDP inflation (the implicit price deflator), the level of first-quarter 2014 GDP currently stands at 5.5% (previously 6.3% in fourth-quarter 2013) above the pre-recession peak-GDP estimate of fourth-quarter 2007. In contrast, the “corrected” GDP version, in the second graph, shows first-quarter 2014 GDP activity at 7.5% below the pre-recession peak of first-quarter 2006.

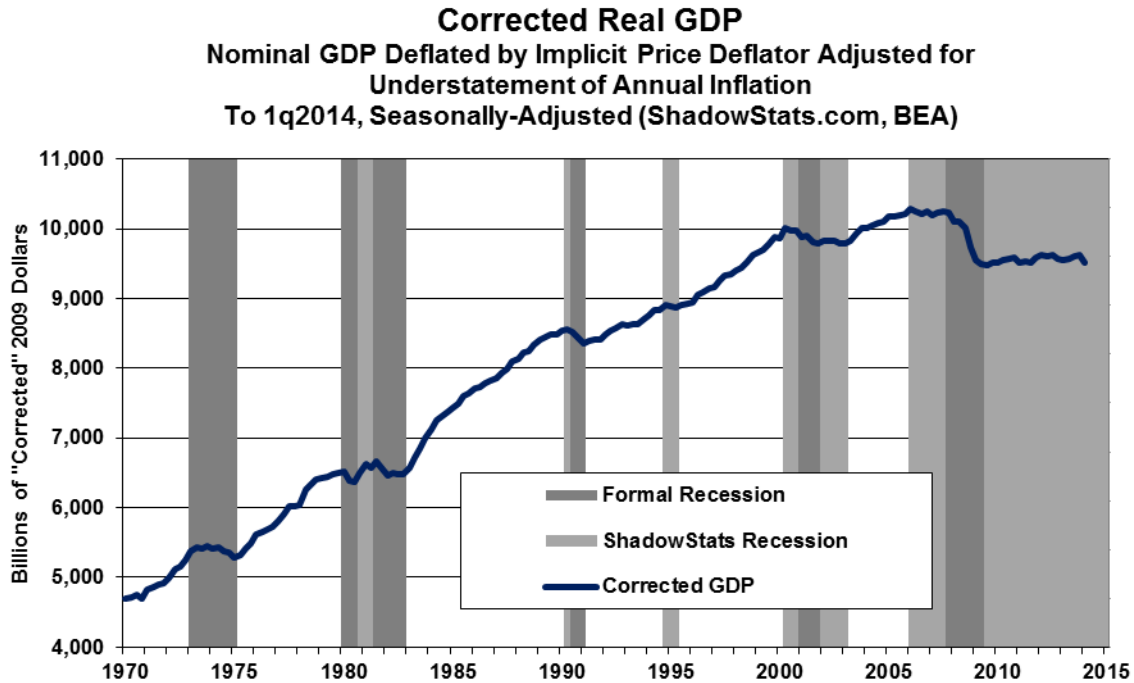
Also, as discussed in the second installment of the *Hyperinflation Report*, no other major economic series has shown a parallel pattern of official full economic recovery and meaningful expansion beyond, consistent with the GDP reporting. Either the GDP reporting is wrong, or all other major economic series are wrong. While the GDP is heavily modeled, imputed, theorized and gimmicked, it also encompasses reporting from those various major economic series and private surveys, which still attempt to survey real-world activity. Flaws in the GDP inflation methodologies and simplifying reporting assumptions have created the “recovery.”

The second graph in each series plots the *Corrected Real GDP*, corrected for the understatement inherent in official inflation estimates (see [Public Commentary on Inflation Measurement](#)), with the deflation by the implicit price deflator (IPD) adjusted for understatement of roughly two-percentage points of annual inflation. The inflation understatement has resulted from hedonic-quality adjustments, as discussed in the hyperinflation reports. Both graphs in the first set are indexed to first-quarter 2000 = 100, and show official periods of recession as shaded areas.





The shaded areas in the “corrected” graph in this second set reflect official as well as ShadowStats-defined recessions, as discussed in detail in the second installment of the *Hyperinflation Report*.



New Orders for Durable Goods—May 2014—Monthly Contraction Was in the Context of Ongoing Stagnation. The headline 1.0% contraction (-1.0%) in May new orders for durable goods was well within the normal reporting variability of this highly unstable series, and reported activity remained consistent with ongoing stagnation.

Nominal (Not-Adjusted-for-Inflation) May 2014 Reporting. The regularly-volatile, seasonally-adjusted nominal level of May 2014 new orders for durable goods fell by 1.01% (-1.01%) for the month, following a revised gain of 0.85% in April. On a year-to-year basis (seasonally-adjusted), May 2014 orders rose by 2.72%, following a revised gain of 7.30% in April 2014.

Nondefense or commercial aircraft orders usually provide extreme headline volatility to the new orders series. For the second month, however, high volatility was seen in new orders for defense capital goods. For May 2014, defense capital goods orders fell by 31.4% (-31.4%) for the month, after surging by a revised 38.2% on a month-to-month basis in April. Net of defense new orders, May new orders rose by 0.69%, while April new orders fell by a revised 0.64% (-0.64%) for the month. New orders for nondefense capital goods fell by 0.49% (-0.49%), versus a revised monthly decline of 0.59% (-0.59%).

Although some on Wall Street purportedly may be cherry-picking these defense details today, in an effort to help rally stocks on the “good” economic news (ignoring the implications of the horrendous GDP), the durable goods orders details are not meaningful, and the new-orders series remains stagnant at best.

In this traditionally-unstable durable goods series, the headline May monthly and annual gains were within the scope of normal month-to-month volatility. An ongoing longer-term pattern of stagnation has remained in place for the durable goods series, particularly when viewed net of inflation, as seen in the

accompanying graphs. The patterns of activity in this series remain of a nature that commonly precedes or coincides with a recession or deepening business downturn.

Net of Volatility in Commercial Aircraft Orders. The reporting of contractions and surges in commercial aircraft orders is seen more commonly than large defense swings, in an irregularly-repeating process throughout the year, and it often dominates headline monthly durable goods orders. These extremely volatile aircraft orders are booked well into the future and are indicative more of longer-term, rather than shorter-term prospects for manufacturing activity.

In May, nondefense (or commercial) aircraft orders fell by 3.98% (-3.98%) for the month, following a revised monthly contraction of 7.40% (-7.40%) in April. Net of the aircraft numbers, month-to-month new orders fell by 0.81% (-0.81%) in May, versus a revised 1.47% gain in April. Year-to-year orders, ex-commercial aircraft, were up by 3.94% in May, versus a revised gain of 3.66% in April.

Real (Inflation-Adjusted) Durable Goods Orders—May 2014. ShadowStats uses the PPI aggregated inflation measure “durable manufactured goods” for deflating the new orders for durable goods series. Published only on a not-seasonally-adjusted basis, the related PPI series reflected a headline unchanged monthly inflation in May, following a 0.2% rise in monthly inflation in April, with headline annual inflation of 1.1% in May 2014, versus 1.0% in April 2014.

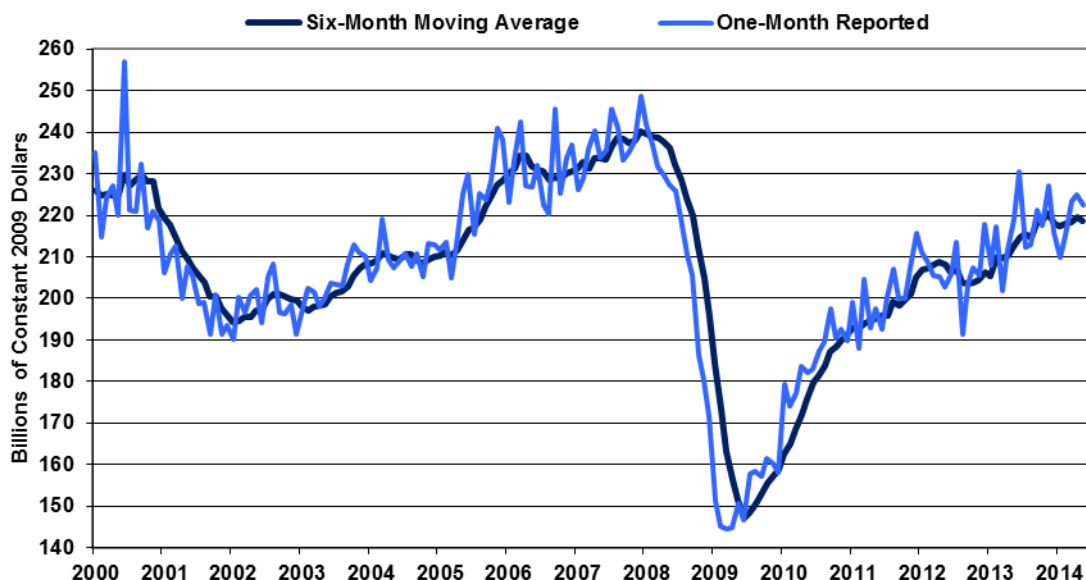
Adjusted for that inflation, and again as reflected in the accompanying graphs, real month-to-month aggregate orders fell by 1.01% (-1.01%), versus a revised gain of 0.60% in April. Ex-commercial aircraft, orders fell for the month by 0.81% (-0.81%), versus a revised gain of 1.23% in April.

Real year-to-year aggregate orders rose by 1.61% in May, versus a revised 6.27% gain in April, and, ex-commercial aircraft, they rose by 2.82% in May and by a revised 2.66% in April.

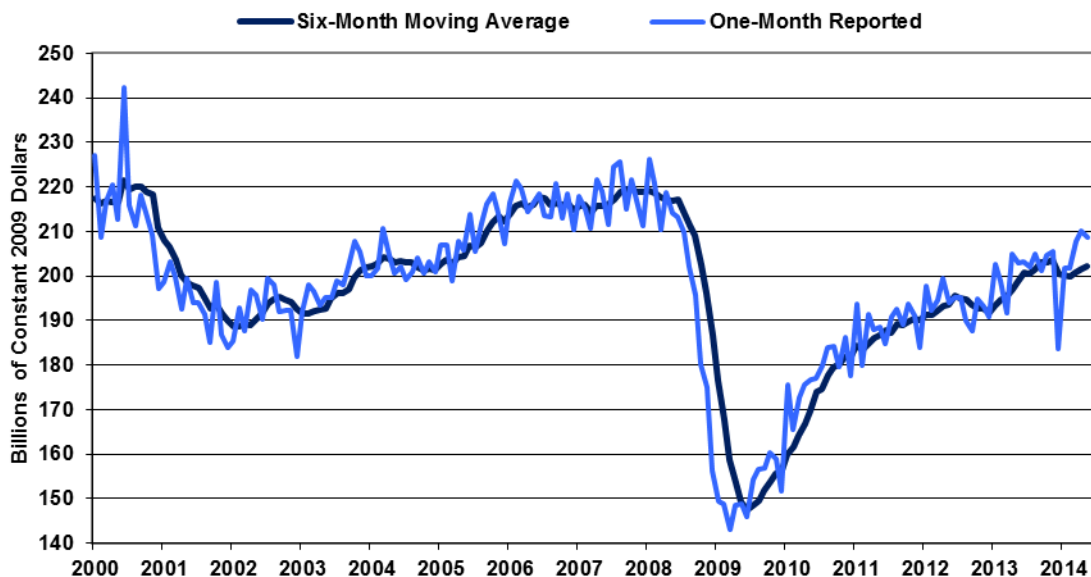
Graphs of Inflation-Adjusted and Smoothed Durable Goods Orders and the Corrected Series. The first two graphs following plot new orders for durable goods, adjusted for inflation. Consistent with the recently revamped Producer Price Index (PPI) series, the inflation measure used here is an aggregation published from the PPI for “Durable Manufactured Goods.” These graphs show monthly as well as a six-month moving average of the activity level. The first graph shows the aggregate new orders series. The second graph is the headline series, net of the unstable commercial-aircraft order sector. Accordingly, that plot is somewhat smoother than the first graph.

In terms of inflation-adjusted activity, both of these series have shown a slowing uptrend and flattening-out in the last two-to-three years—with a dip and upside bouncing into 2013, and renewed stagnation in recent reporting. Broadly, there has been a recent general pattern of stagnation or bottom-bouncing evident in the orders—clearly not the booming recovery that is seen in official GDP reporting. The real (inflation-adjusted) level of orders in May 2014 remained at or below both the pre-2001 and pre-2007 recession highs. The pattern of recent stagnation and downturn in the inflation-adjusted series also is one that commonly precedes or is coincident with a recession.

Real New Orders for Durable Goods
Monthly, Deflated by PPI--Durable Manufactured Goods (\$2009)
To May 2014, Seasonally-Adjusted (ShadowStats.com, Census, BLS)

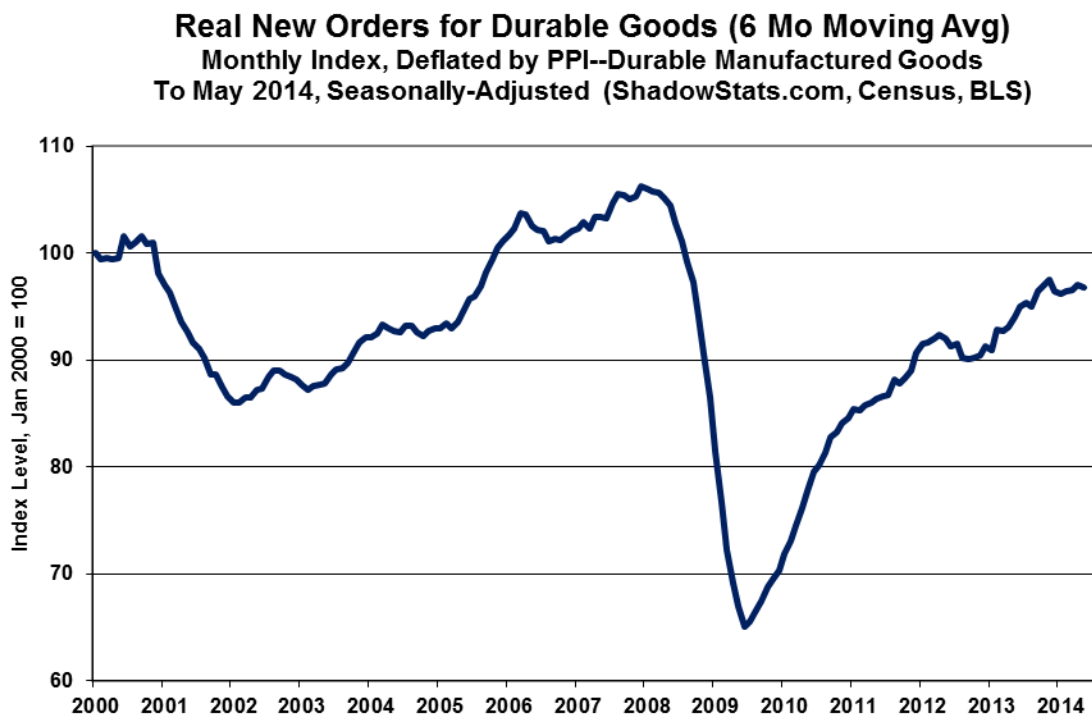


Real Durable Goods Orders (Ex-Nondefense Aircraft)
Monthly, Deflated by PPI--Durable Manufactured Goods (\$2009)
To May 2014, Seasonally-Adjusted (ShadowStats.com, Census, BLS)



As with other economic series that are deflated by official government inflation measures, estimates of inflation-adjusted growth in new orders for durable goods are overstated, due to the understatement of the official inflation. That understatement here is through the use of hedonic-quality adjustments—usually not perceived by the consumer—used to reduce the pace of headline inflation (see [Public Comment on Inflation](#)). As has been done with other series such as the GDP, retail sales and industrial production, ShadowStats publishes an experimental corrected version of the inflation-adjusted graph of real new orders for durable goods, corrected for the understatement of the related headline PPI inflation.

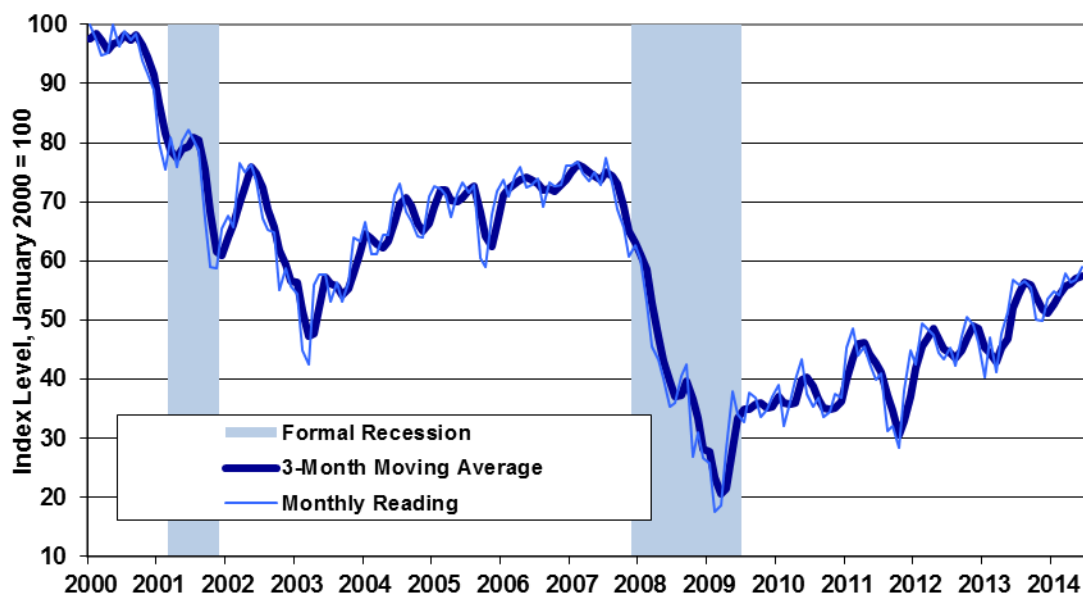
The two graphs following reflect a smoothed version of the real total durable goods orders series (using a six-month moving average). The first graph reflects the real series, as graphed previously, only indexed to January 2000 = 100. The second graph is a “corrected” version of the first, where the estimated, understated inflation effects (overstated inflation-adjusted growth effects) from hedonic adjustments have been reversed by ShadowStats. As shown in [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), the “corrected” real new orders for durable goods series shows a fair correlation to the “corrected” industrial production series.



Corrected Real Durable Goods Orders (6 Mo Moving Avg)
 Monthly Index, Corrected for Hedonic Adjustment Distortions
 To May 2014, Seasonally-Adjusted (ShadowStats.com, Census, BLS)



Consumer Confidence -- Conference Board
 Monthly and 3-Month Moving-Average Index (January 2000 = 100)
 To June 2014, Seasonally-Adjusted (ShadowStats, Conference Board)



Consumer Liquidity—Updated. As discussed in [Commentary No. 632](#) and [Commentary No. 634](#), there has been no change in the underlying consumer-liquidity fundamentals. Lacking real growth in income

and available credit, combined with confidence levels that remain deep in recession territory, the consumer is unable to fuel actual, positive growth in inflation-adjusted personal consumption or in related housing data. 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.

The preceding graph shows the updated consumer confidence measure, through June, reported by the Conference Board. Consumer confidence remains deep in traditional recession territory, reflecting an economic pattern of plunge-and-stagnation, as suggested by the “corrected” GDP series, as opposed to the plunge-and-rebound indicated in official headline GDP reporting.

Despite Monthly Jump, Existing-Home Sales Fell Year-to-Year for Seventh Straight Month. In the context of the consumer liquidity issues discussed in the prior section, the headline 4.9% monthly gain in May 2014 was third and largest month-to-month positive move since the existing-home sales series began its renewed slide in July 2013. Nonetheless, the May reading was down by 5.0% year-to-year—the seventh straight annual decline—and down by 9.1% from the near-term peak in activity last July. May 2014 sales activity, at an annualized pace of 4,890,000 also was down by 32.7% from the June 2005 pre-recession peak in activity.

Headline May Existing-Home Sales Rose by 4.9% for the Month, Down 5.0% (-5.0%) Year-to-Year. Headline May 2014 existing-home sales (counted based on actual closings, National Association of Realtors [NAR]) showed a seasonally-adjusted 4.9% month-to-month gain, following a revised 1.5% gain in April. Net of prior-period revisions, May sales gained 5.2% for the month

On a year-to-year basis, May 2014 annual sales contracted by 5.0% (-5.0%), versus a revised 6.6% decline (-6.6%) in April. The May annual contraction was the seventh consecutive month where headline sales were reported below those of the year before.

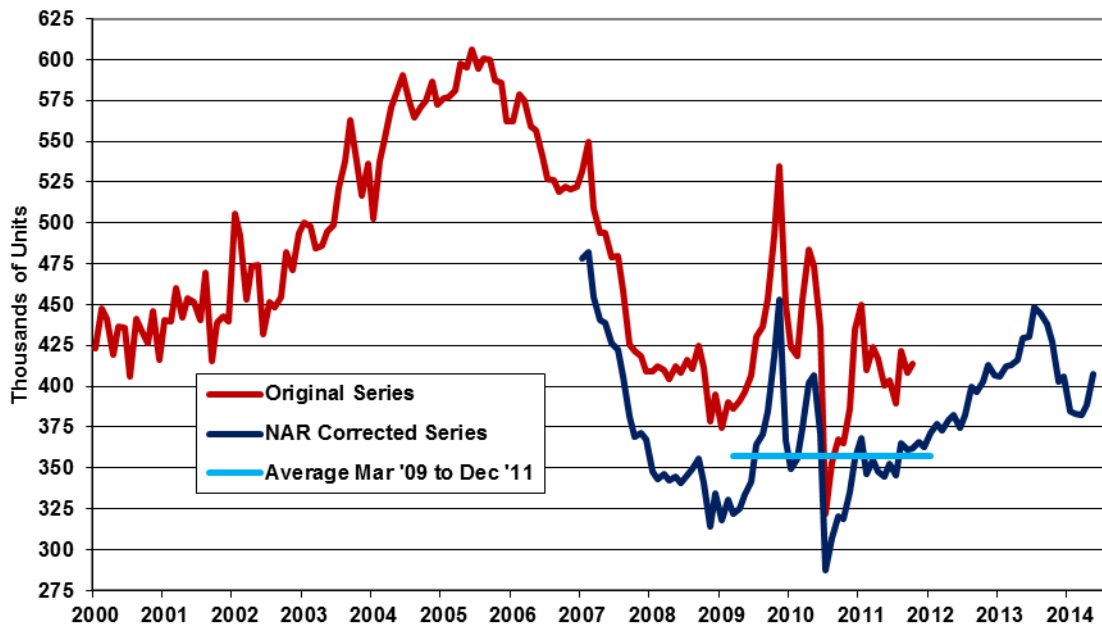
Smoothed for irregular distortions, the series remained statistically consistent with a period of broad stagnation that has turned into renewed downturn, as shown in the accompanying graph. The data quality, though, remains questionable.

The NAR estimated the portion of total sales in “distressed” properties for May 2014 declined to 11% (8% foreclosures, 3% short sales), versus 15% (10% foreclosures, 5% short sales) in April 2014.

Reflecting continuing lending problems, related banking-industry and consumer-solvency issues, and the ongoing influx of speculative investment money into the existing-housing market, the NAR also estimated that all-cash sales in May 2014 were 32%, the same as in April 2014 and down from 33% in May 2013.

Existing-Home Sales Graph. Smoothed for irregular distortions, the existing-home sales series remained statistically consistent with a period of broad stagnation that has turned into renewed downturn, with both fourth-quarter 2013 and first-quarter 2014 in quarter-to-quarter contractions, and first-quarter 2014 in year-to-year contraction. Second-quarter data have shown some uptick on a monthly basis, but remain lower in terms of year-to-year change. Those patterns are reflected in the accompanying graph.

**Existing Home Sales (Not-Annualized Monthly Level)
To May 2014, Seasonally Adjusted (ShadowStats.com, NAR, HUD)**

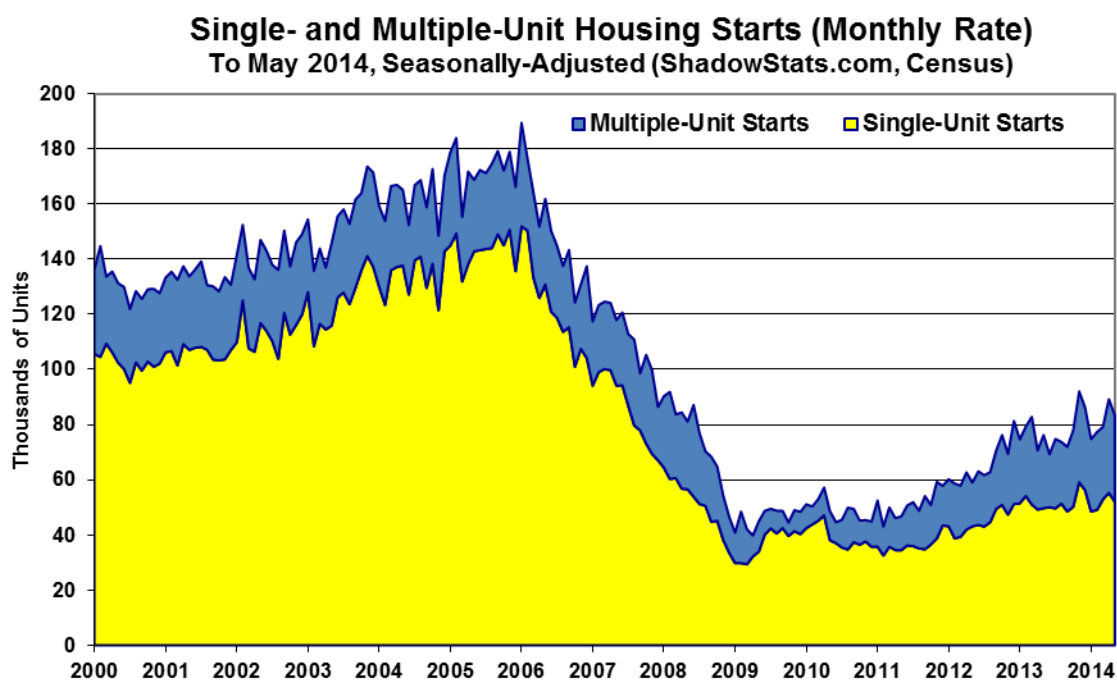
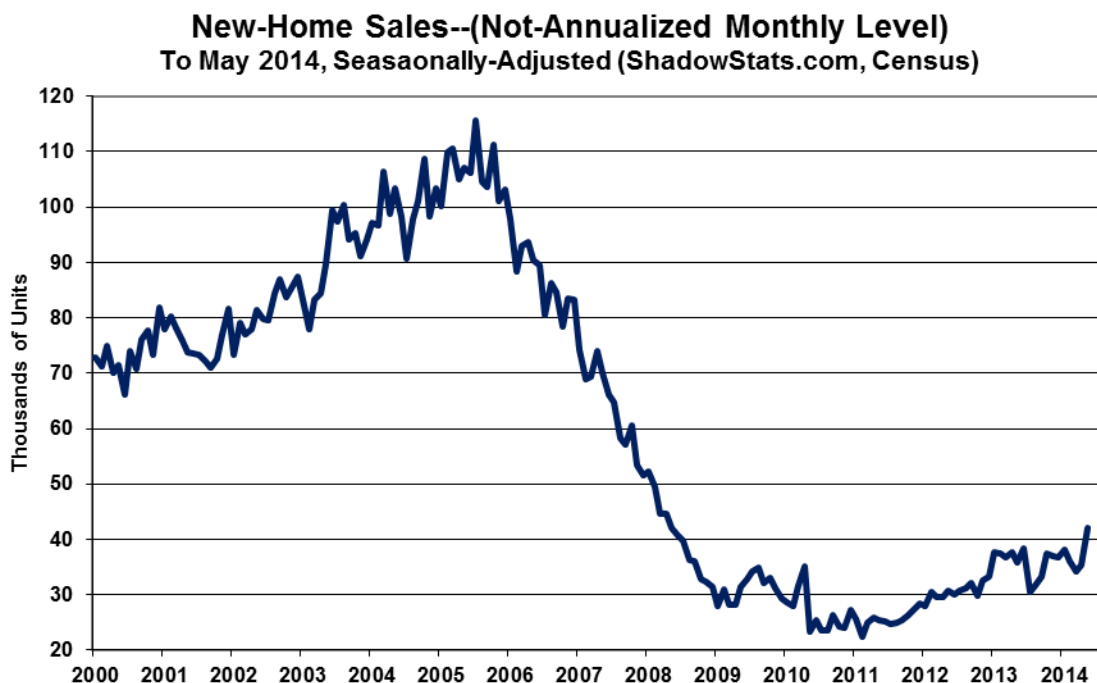


New-Home Sales—May 2014—Headline Monthly and Annual Gains Were Not Statistically Significant. In the context of the consumer liquidity issues discussed earlier, despite an unusually large sales gain of 18.6% month-to-month, and a 16.9% year-to-year increase in new-home sales, the changes in new-home sales activity, on both a monthly and annual basis, remained statistically-insignificant. Accordingly, ongoing stagnation remains the pattern for the series. Headline May 2014 sales activity still was down by 63.7% from the pre-recession peak, seen in July 2005.

May 2014 New-Home Sales Headline Gain Was Insignificant. Boosted by a relative downside revision to April reporting, May 2014 headline new-home sales (Census Bureau, counted based on contract signings) rose by a statistically-insignificant 18.6%, following a revised 3.7% monthly gain in April.

Year-to-year, May 2014 sales rose by a statistically-insignificant 16.9%. That followed a revised decline of 6.0% (-6.0%) in April.

New-Home Sales Graphs. The regular monthly graph of new-home sales activity follows, along with graphs of the latest existing-home sales (see preceding graph) a graph on related housing starts activity, as published in [Commentary No. 636](#). The second graph following reflects the latest housing starts, broken out in aggregate and by single and multiple unit sales.



*[For further details on GDP, durable goods and new- and existing home sales,
see the Reporting Detail section.]*

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

HYPERINFLATION WATCH

Hyperinflation Summary Outlook. *[PLEASE NOTE: Other than for the non-bold, italicized text starting with the next paragraph, 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 intensified, revised headline contraction of 2.9% (-2.9%) in first-quarter 2014 GDP, versus 2.6% growth in fourth-quarter 2013. Coming into the July 30th GDP benchmark revisions, the popular outlook for second-quarter GDP should shift increasingly into the recession camp (see the Opening Comments). 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 possibly still-deepening first-quarter 2014 GDP contraction, which faces one further near-term revision (the July 30th 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.

REPORTING DETAIL

GROSS DOMESTIC PRODUCT—GDP (First-Quarter 2014, Third Estimate, Second Revision)

Deepening Contraction in First-Quarter 2014 Helps Set Stage for Second-Quarter Contraction and “Renewed” Recession. Even with all the upside gimmicks built into gross domestic product (GDP) reporting, underlying actual economic activity is so weak at present as to generate a severe contraction in first-quarter headline GDP reporting.

The severity of the current economic downturn was emphasized by large downside revisions to key economic growth patterns, including features not otherwise seen since the onset of the official 2007 recession. The latest downside revisions reflected primarily a large reversal in the guesstimated economic impact of the Affordable Care Act, from a positive contribution to GDP growth of 1.01%, to a contraction of 0.16% (-0.16%), along with a revised widening of the trade deficit. As a result, the headline contraction for first-quarter GDP deepened to 2.93% (-2.93%) from 0.98% (-0.98%) in the prior reporting, and a reversal of direction from the 0.11% gain in initial reporting.

Annualized real (inflation-adjusted) quarterly contractions deepened sharply for the GDP, the broader gross national product (GNP) and the GDP’s theoretical equivalent of gross domestic income (GDI), along with meaningful slowing in annual growth. First-quarter 2014 GDP-related broad measures of activity officially fell below the same measures for third-quarter 2013 (two quarters ago), let alone the sharp fall-off versus the prior fourth-quarter 2013 activity. Second-quarter GDP activity would have to

rebound by 3.0% to regain the level of real fourth-quarter 2013 GDP activity. Even so, an outright GDP contraction in the second-quarter remains likely.

Final sales—GDP net of changes in inventories—revised into outright contraction, down at an annualized pace of 1.23% (-1.23%) in the first-quarter, having shown positive growth of 0.66% at the prior revision. Inventory growth had slowed (minimal revision in the latest detail), which is an economic negative. Nonetheless, with GDP activity net of inventory swings still in contraction, that takes the aggregate first-quarter GDP contraction outside the scope of being a simple inventory adjustment.

Of equal significance, before adjustment for inflation, the nominal GDP, GNP and GDI all contracted quarter-to-quarter, unfolding patterns not seen since the early days of the official 2007 economic crash.

The issue for the economy is not the first-quarter's bad weather and a potential second-quarter recovery from same, but rather ongoing, severe structural liquidity constraints on the consumer, as last discussed in [Commentary No. 632](#) and [Commentary No. 634](#) and in the *Opening Comments*. Nothing positive is happening in the consumer liquidity area. Lacking real growth in income and available credit, combined with confidence levels that remain deep in recession territory, the consumer is unable to fuel actual, positive growth in inflation-adjusted personal consumption.

As to the weather, a surge in consumer utility usage still largely offsets any negative impact from the unseasonable weather on other areas, during the first-quarter. That pattern will tend to reverse in the second-quarter. The major negative factors in the first-quarter GDP generally were not weather related. Little affected by the weather, a slowdown in inventory growth and a marked deterioration in the trade deficit accounted for the bulk of the contraction in first-quarter GDP, and the inventory and trade factors both should be ongoing issues in second-quarter GDP reporting. See the distribution of the headline quarterly GDP growth rate by major components, in the *Opening Comments*.

Otherwise, the GDP remains the most-worthless and the most-heavily modeled, massaged and politically-manipulated of government economic series. It does not reflect properly or accurately the changes to the underlying fundamentals that drive the economy. Underlying real-world economic activity suggests that the broad economy began to turn down in 2006 and 2007, plunged into 2009, entered a protracted period of stagnation thereafter—never recovering—and then began to turn down anew in second- and third-quarter 2012 (see [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), and [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#)).

Notes on GDP-Related Nomenclature and Definitions

For purposes of clarity and the use of simplified language in the text of the GDP analysis, here are definitions of several key terms used related to GDP reporting:

Gross Domestic Product (GDP) is the headline number and the most widely followed broad measure of U.S. economic activity. It is published quarterly by the Bureau of Economic Analysis (BEA), with two successive monthly revisions, and with an annual revision in the following July.

Gross Domestic Income (GDI) is the theoretical equivalent to the GDP, but it generally is not followed by the popular press. Where GDP reflects the consumption side of the economy and GDI reflects the offsetting income side. When the series estimates do not equal each other, which almost always is the case, since the series are surveyed separately, the difference is added to or subtracted from the GDI as a “statistical discrepancy.”

Although the BEA touts the GDP as the more accurate measure, the GDI is relatively free of the monthly political targeting the GDP goes through.

Gross National Product (GNP) is the broadest measure of the U.S. economy published by the BEA. Once the headline number, now it rarely is followed by the popular media. GDP is the GNP net of trade in factor income (interest and dividend payments). GNP growth usually is weaker than GDP growth for net-debtor nations. Games played with money flows between the United States and the rest of the world tend to mute that impact on the reporting of U.S. GDP growth.

Real (or Constant Dollars) means the data have been adjusted, or deflated, to reflect the effects of inflation.

Nominal (or Current Dollars) means growth or level has not been adjusted for inflation. This is the way a business normally records revenues or an individual views day-to-day income and expenses.

GDP Implicit Price Deflator (IPD) is the inflation measure used to convert GDP data from nominal to real. The adjusted numbers are based on “Chained 2009 Dollars,” as introduced with the 2013 comprehensive revisions, where 2009 is the base year for inflation. “Chained” refers to the substitution methodology which gimmicks the reported numbers so much that the aggregate of the deflated GDP sub-series missed adding to the theoretically-equivalent deflated total GDP series by \$41.8 billion in “residual,” as of the initial estimate of second-quarter 2013.

Quarterly growth, unless otherwise stated, is in terms of seasonally-adjusted, annualized quarter-to-quarter growth, i.e., the growth rate of one quarter over the prior quarter, raised to the fourth power, a compounded annual rate of growth. While some might annualize a quarterly growth rate by multiplying it by four, the BEA uses the compounding method, raising the quarterly growth rate to the fourth power. So a one percent quarterly growth rate annualizes to $1.01 \times 1.01 \times 1.01 \times 1.01 = 1.0406$ or 4.1%, instead of $4 \times 1\% = 4\%$.

Annual growth refers to the year-to-year change of the referenced period versus the same period the year before.

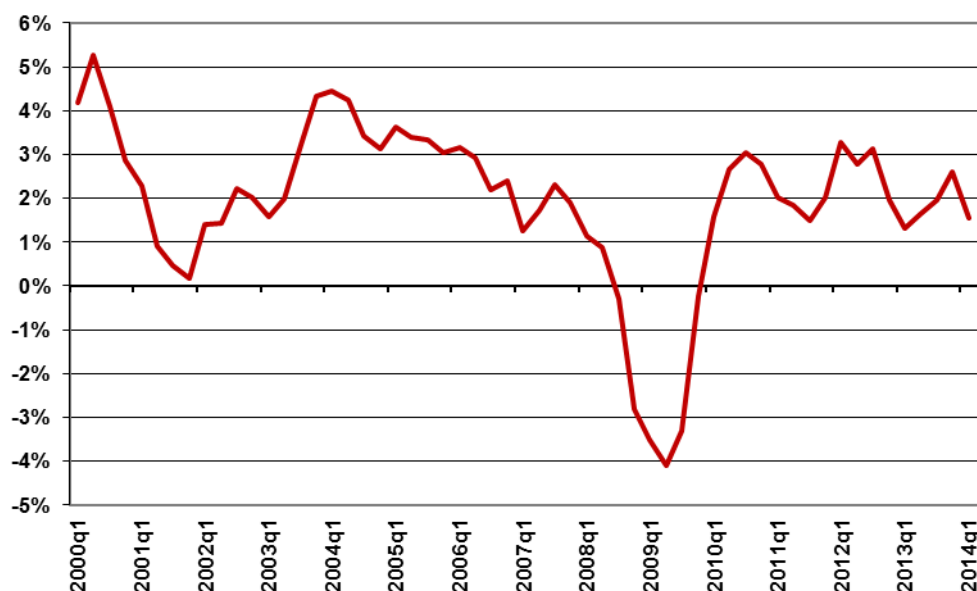
Gross Domestic Product (GDP). Published this morning, June 25th, by the Bureau of Economic Analysis (BEA), the third estimate of, and second revision to first-quarter 2014 GDP showed a revised, statistically-insignificant, real (inflation-adjusted), annualized, quarterly contraction of 2.93% (-2.93%) +/- 3.5% (95% confidence interval). Previously, the headline first-quarter change in activity had been a contraction of 0.98% (-0.98%), versus an initial estimate of a 0.11% gain. That was against a 2.63% headline gain in fourth-quarter 2013, a 4.13% gain in third-quarter 2013, a 2.48% increase in second-quarter 2013 and a 1.15% gain in the first-quarter 2013. Again, distribution of the headline quarterly GDP growth rate, by major components, is detailed in the *Opening Comments*. \

In nominal terms, before inflation adjustment, first-quarter GDP contracted at an annualized pace of 1.71% (-1.71%), versus nominal annualized growth of 4.25% in fourth-quarter 2013. Year-to-year nominal GDP growth slowed to 2.91% in first-quarter 2014, from 4.08% in fourth-quarter 2013.

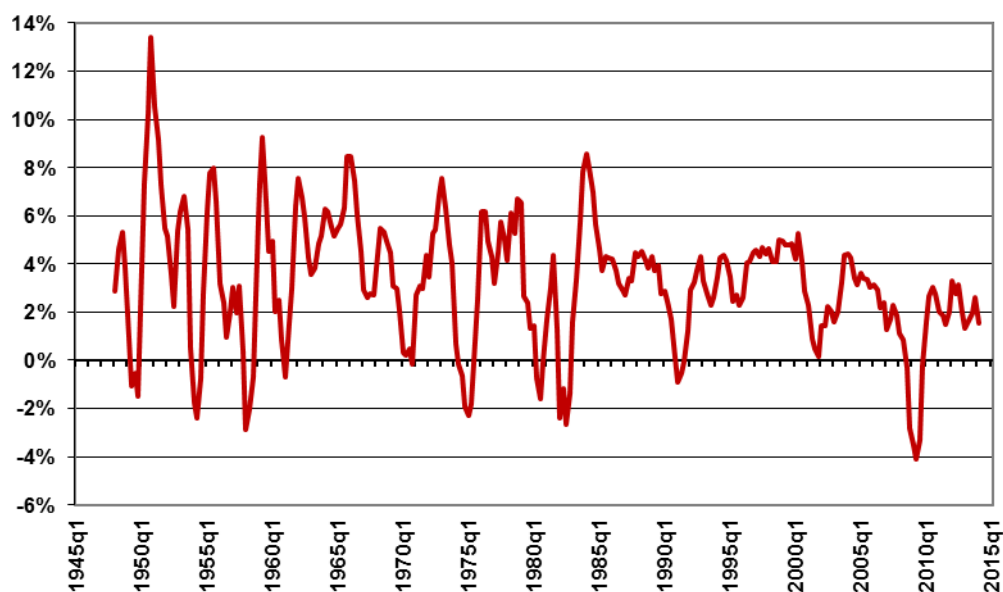
Shown in the following two graphs are the latest year-to-year or annual rates of change for the real GDP series. First-quarter 2014 GDP year-to-year growth was a revised 1.54% (previously 2.05%, initially 2.33%), versus 2.59% in fourth-quarter 2013, 1.97% in the third-quarter, 1.63% in the second-quarter 2013 and 1.32% in the first-quarter of 2013.

The first graph shows near-term historical detail since 2000. The second graph shows the full history of the series. The latest quarterly year-to-year growth remained below the near-term peak of 3.13% growth reported for third-quarter 2012. The current-cycle trough was in second-quarter 2009 at a 4.09% year-to-year decline. That was the deepest annual contraction seen for any quarterly GDP in the history of the series, which began with first-quarter 1947.

Quarterly Real Gross Domestic Product
Year-to-Year Change 2000-to-Date (ShadowStats, BEA)



Quarterly Real Gross Domestic Product
Year-to-Year Change 1947-to-Date (ShadowStats, BEA)



Implicit Price Deflator (IPD). The third estimate of first-quarter 2014 GDP inflation, or the implicit price deflator (IPD), was at a revised annualized quarterly pace of 1.26% (previously 1.27%, initially 1.30%), versus 1.58% in fourth-quarter 2013, 1.97% in the third-quarter 2013, 0.58% in the second-

quarter 2013 and 1.67% in the first-quarter 2013. Year-to-year, first-quarter 2014 IPD inflation was a revised 1.34% (previously 1.35%, initially 1.36%), versus 1.45% in fourth-quarter 2013, 1.41% in third-quarter 2013, 1.44% in second-quarter 2013 and 1.74% in first-quarter 2013.

For comparison purposes, on a seasonally-adjusted, annualized quarter-to-quarter basis, CPI-U inflation published by the Bureau of Labor Statistics (BLS), headline CPI-U inflation was up by 1.91% in first-quarter 2014, versus 1.14% in fourth-quarter 2013, 2.16% in the third-quarter, 0.40% in the second-quarter, and 1.19% in the first-quarter. On a year-to-year basis, first-quarter 2014 CPI-U (unadjusted) inflation was 0.86%, versus 1.23% in fourth-quarter 2013, versus 1.55% in the third-quarter, 1.39% in the second-quarter, and 1.68% in the first-quarter 2013.

The weaker the inflation rate used in deflating an economic series, the stronger will be the resulting inflation-adjusted growth.

Gross National Product (GNP). The second estimate of first-quarter 2014 real GNP showed an annualized quarter-to-quarter contraction of 3.61% (-3.61%) [initially down by 2.11% (-2.11%)], following a 3.06% gain in fourth-quarter 2013. In terms of year-to-year change, annual growth slowed to 1.59% (initially 1.98%) in first-quarter 2014, from 2.69% in fourth-quarter 2013. Again, annualized first-quarter GDP was a 2.91% contraction, versus a 2.63% gain in the fourth-quarter.

In nominal terms, before inflation adjustment, first-quarter GNP contracted at an annualized pace of 2.39% (-2.39%), versus nominal annualized growth of 4.68% in fourth-quarter 2013.

GNP is the broadest measure of U.S. economic activity, where GDP is GNP net of trade flows in factor income (interest and dividend payments). As a reporting gimmick aimed at boosting the headline reporting of economic growth for net-debtor nations such as Greece and the United States, international reporting standards were shifted some decades back to reporting headline GDP instead of GNP.

The relatively greater quarterly contraction in U.S. first-quarter 2014 GNP, versus the GDP, fully reflected a sharp deterioration in the net flow of factor income between the United States and the rest of the world. The net deterioration was due to a large falloff in U.S. receipts from the rest of the world in first-quarter 2014, plus a second quarterly increase in U.S. payments to the rest of the world.

Gross Domestic Income (GDI). GDI is the theoretical income-side equivalent of the consumption-side GDP estimate. The GDP and GDI are made to equal each other, every quarter, with the addition of a “statistical discrepancy” to the GDI-side of the equation, but the discrepancy just as easily could be added to the GDP number. Net of the statistical discrepancy, the revised estimate of headline real GDI annualized quarterly change for first-quarter 2014 was a contraction of 2.61% (-2.61%) [initially down by 2.26% (-2.26%)], versus growth of 2.60% in the fourth-quarter. Year-to-year annual growth slowed to 1.22% (initially 1.31%) in first-quarter 2014, versus 2.51% in the fourth-quarter.

In nominal terms, before inflation adjustment, first-quarter GDI contracted at an annualized pace of 1.39% (-1.39%), versus nominal annualized growth of 4.22% in fourth-quarter 2013.

Benchmark GDP Revision on July 30th. The BEA will release its annual revisions of GDP for three years, with partial revisions going back to first-quarter 1999, along with the initial estimate of second-quarter 2014 GDP. Generally, downside revisions are likely to GDP reporting of recent years, but that detail will be covered in a separate *Commentary* in advance of the revisions.

ShadowStats-Alternate GDP. The ShadowStats-Alternate GDP estimate for first-quarter 2014 GDP remains a 1.9% year-to-year contraction, versus a revised headline year-to-year gain of 1.5% (previously 2.0%, initially 2.3%). The alternate fourth-quarter 2013 estimate was a 1.4% year-to-year contraction, versus a headline year-to-year gain of 2.6% (see the [Alternate Data](#) tab). The July 30th benchmark revisions to GDP reporting of recent years generally should be to the downside and bring the historical series more in line with the ShadowStats estimates.

While annualized real quarterly growth is not estimated formally on an alternate basis, the headline quarter-to-quarter contraction for the first-quarter likely was even deeper, net of all the regular reporting gimmicks. An actual quarterly contraction appears to have been a realistic possibility for the real GDP in most quarters since the official second-quarter 2009 end to the recession.

Adjusted for understated inflation and other methodological changes (such as the inclusion of intellectual property, including software), the business downturn that began in 2006/2007 is ongoing; there has been no meaningful economic rebound. The “corrected” real GDP graph, and the longer-term “corrected” graph updated from [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#) (see the *Opening Comments* section) is based on the removal of the impact of hedonic quality adjustments that have reduced the reporting of official annual GDP inflation by roughly two-percentage points. It is not the same measure as the ShadowStats-Alternate GDP, which reflects reversing additional methodological distortions (“Pollyanna Creep”) of recent decades.

NEW ORDERS FOR DURABLE GOODS (May 2014)

May 2014 New Orders for Durable Goods Fell in Context of Ongoing Stagnation. The headline 1.0% contraction (-1.0%) in May new orders for durable goods was well within the normal reporting variations of this highly unstable series and remained consistent with ongoing stagnation.

Nominal (Not-Adjusted-for-Inflation) May 2014 Reporting. The Census Bureau reported today, June 25th, that the regularly-volatile, seasonally-adjusted nominal level of May 2014 new orders for durable goods fell by 1.01% (-1.01%) for the month, following a revised gain of 0.85% (previously 0.80%) in April. On a year-to-year basis (seasonally-adjusted), May 2014 orders rose by 2.72%, following a revised gain of 7.30% (previously 7.08%) in April 2014.

Where nondefense or commercial aircraft orders usually provide extreme volatility to the orders series, for the second month, high volatility was seen instead in new orders for defense capital goods. For May 2014, defense capital goods orders fell by 31.4% for the month, after surging by 38.2% (previously 39.27%) on a month-to-month basis in April. Net of defense new orders, May new orders rose by 0.69%, while April new orders fell by a revised 0.64% (-0.64%) [previously down by 0.82% (-0.82%)] for the month, while new orders for nondefense capital goods fell by 0.49% (-0.49%), versus a revised monthly decline of 0.59% (-0.59%) [previously down by 1.00% (-1.00%)].

Although some on Wall Street purportedly may be cherry-picking these defense details to aid in rallying stocks on the “good” economic news (ignoring the implications of the horrendous GDP), the durable goods orders details are not meaningful and new orders remain stagnant at best.

In this traditionally-unstable durable goods series, the headline May monthly and annual gains were within the scope of normal month-to-month volatility. A longer-term pattern of stagnation has remained in place for the durable goods series, particularly when viewed net of inflation. The patterns of activity in this series remain of a nature that commonly precedes or coincides with a recession or deepening business downturn. The inflation-adjusted real series, and the same series corrected for understatement of the official inflation series, are discussed and graphed in the *Opening Comments* section.

Net of Volatility in Commercial Aircraft Orders. The reporting of contractions and surges in commercial aircraft orders is seen more commonly in an irregularly-repeating process throughout the year and often dominates headline monthly durable goods orders. These extremely volatile aircraft orders are booked well into the future and are indicative more of longer-term, rather than shorter-term prospects for manufacturing activity.

In May, nondefense (or commercial) aircraft orders fell by 3.98% (-3.98) for the month, following a revised contraction of 7.40% (-7.40%) [previously down by 4.12% (-4.12%)] month-to-month in April. Net of the aircraft numbers, month-to-month new orders fell by 0.81% (-0.81%) in May, versus a revised 1.47% (previously 1.17%) gain in April. Year-to-year orders, ex-commercial aircraft, were up by 3.94% in May, versus a revised gain of 3.66% (previously 3.24%) in April.

Caution: Current durable goods reporting remains subject to many of the same sampling and concurrent-seasonal-adjustment problems that are seen with retail sales, payroll and unemployment reporting. Unusual seasonal-factor volatility raises issues as to the significance of reported seasonally-adjusted monthly and annual changes. While those issues are brought into balance, temporarily, with an annual benchmark revision to durable goods orders—as was seen on May 15th this year—subsequent reporting already has made all historical reporting prior to February 2014 inconsistent with the current headline numbers.

Real (Inflation-Adjusted) Durable Goods Orders—May 2014. ShadowStats uses the PPI aggregated inflation measure “durable manufactured goods” for deflating the new orders for durable goods series. Published only on a not-seasonally-adjusted basis, the related PPI series reflected a headline unchanged monthly inflation in May, following a 0.2% rise in monthly inflation in April, with headline annual inflation of 1.1% in May 2014, versus 1.0% in April.

Adjusted for that inflation, and again as reflected in the graphs of the *Opening Comments* section, real month-to-month aggregate orders fell by 1.01% (-1.01%), versus a revised gain of 0.60% (previously 0.56%) in April. Ex-commercial aircraft, orders fell for the month by 0.81% (-0.81%), versus a revised gain of 1.23% (previously 0.93%) in April.

Real year-to-year aggregate orders rose by 1.61% in May, versus a revised 6.27% (previously 6.05%) gain in April, and, ex-commercial aircraft, they rose by 2.82% in May and by a revised 2.66% (previously 2.25%) in April.

Graphs of Inflation-Adjusted and “Corrected” Smoothed Durable Goods Orders. Two sets of inflation-adjusted graphs are found in the *Opening Comments* section. The first set shows the monthly as well as a six-month moving-average activity for both the aggregate new orders series and the series net of the unstable commercial-aircraft order sector. The moving-average levels in both series have been holding in a pattern of near-stagnation, with some a recent turn to the downside, and a current upside blip.

Real levels of the May 2014 orders remained at or below both the pre-2001 and pre-2007 recession highs. The pattern of recent stagnation and downturn in the inflation-adjusted series also is one that commonly precedes or is coincident with a recession.

The second set of graphs in the *Opening Comments* section also shows the pattern of historical real new durable goods orders net of official inflation and “corrected” for the understatement of that inflation (overstatement of official, inflation-adjusted growth).

EXISTING-HOME SALES (April 2014)

Despite Monthly Jump, Existing Home Sales Fell Year-to-Year for Seventh Straight Month. The headline 4.9% monthly gain in May 2014 was third and largest month-to-month positive move since the existing-home sales series began its renewed slide in July 2013. Nonetheless, the May reading was down by 5.0% year-to-year—the seventh straight annual decline—and down by 9.1% from the near-term peak in activity last July. May 2014 sales activity, at an annualized pace of 4,890,000 also was down by 32.7% from the June 2005 pre-recession peak in activity.

Headline May Existing-Home Sales Rose by 4.9% for the Month, Down 5.0% (-5.0%) Year-to-Year. The Monday (June 23rd) release of May 2014 existing-home sales (counted based on actual closings, National Association of Realtors [NAR]) showed a seasonally-adjusted 4.9% month-to-month gain, following a revised 1.5% (previously 1.3%) gain in April. Net of prior-period revisions, May sales gained 5.2% for the month

On a year-to-year basis, May 2014 annual sales contracted by 5.0% (-5.0%), versus a revised 6.6% decline (-6.6%) [previously a 6.8% contraction (-6.8%)] in April. The May annual contraction was the seventh consecutive month where headline sales were reported below those of the year before.

Smoothed for irregular distortions, the series remained statistically consistent with a period of broad stagnation that has turned into renewed downturn, as seen in the graph in the *Opening Comments*. The data quality, though, remains questionable.

The NAR estimated the portion of total sales in “distressed” properties in May 2014 declined to 11% (8% foreclosures, 3% short sales), versus 15% (10% foreclosures, 5% short sales) in April 2014.

Reflecting continuing lending problems, related banking-industry and consumer-solvency issues, and the ongoing influx of speculative investment money into the existing-housing market, the NAR also estimated that all-cash sales in May 2014 were 32%, the same as in April 2014 and down from 33% in May 2013.

As discussed in the *Opening Comments*, there has been no underlying improvement in fundamental consumer liquidity conditions, and most underlying economic numbers are showing a renewed economic downturn. There is no basis here for an imminent recovery in the housing market.

Existing-Home Sales Graph. The regular monthly graph of existing-home sales activity is included in the *Opening Comments* section, along with graphs of the latest new-home sales and housing starts. Existing-home sales activity recently has turned down anew, with both fourth-quarter 2013 and first-

quarter 2014 in quarter-to-quarter contractions, and first-quarter 2014 in year-to-year contraction. Second-quarter data have shown some uptick on a monthly basis, but remain lower in terms of year-to-year change.

NEW-HOME SALES (May 2014)

Headline Monthly and Annual Gains Were Not Statistically Significant. Despite unusually large sales 18.6% month-to-month and 16.9% year-to-year increases for new home sales, the changes in activity on both a monthly and annual basis remained statistically insignificant. Accordingly, ongoing stagnation remains the pattern for the series. Headline May 2014 sales activity still was down by 63.7% from the pre-recession peak, seen in July 2005.

May 2014 New-Home Sales Headline Gain Was Insignificant. As reported Tuesday (June 24th) by the Census Bureau, May 2014 headline new-home sales (counted based on contract signings), and in the context of a downside revision to April reporting, rose by a statistically-insignificant 18.6% +/- 20.2% (95% confidence interval), following a revised 3.7% (previously 6.4%) monthly gain in April.

Year-to-year, May 2014 sales rose by a statistically-insignificant 16.9% +/- 22.9%. That followed a revised decline of 6.0% (-6.0%) [previously a decline of 4.2% (-4.2%)] in April.

As discussed in the *Opening Comments*, there has been no underlying improvement in fundamental consumer liquidity conditions, and most underlying economic numbers are showing a renewed economic downturn. There is no basis here for an imminent recovery in the housing market.

New-Home Sales Graphs. The regular monthly graph of new-home sales activity is included in the *Opening Comments* section, along with graphs of the latest existing-home sales and housing starts.

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 accelerating pace of economic decline seen in the third estimate of real first-quarter 2014 GDP, which still is the first contemporary reporting of a quarterly GDP 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:

Construction Spending (May 2014). The Commerce Department has scheduled release of May 2014 construction spending for Tuesday, July 1st, along with annual revisions to the series. The headline monthly changes, as usual, should not be statistically significant, while previous data will be subject to unusually large and unstable revisions. The annual revisions generally should show weaker historical numbers than had been reported previously.

U.S. Trade Deficit (May 2014). The Commerce Department and Bureau of Economic Analysis (BEA) will release their estimate of the May 2014 trade-balance data on Thursday, July 3rd. The May reporting will determine the impact of partial second-quarter trade data on the initial reporting of second-quarter GDP (July 30th). While the market consensus appears to be for some narrowing of the May versus April deficit, underlying fundamentals continue to favor net trade deterioration, a negative for GDP growth. If the May deficit held at or deteriorated from the April reporting, then the negative contribution to the annualized headline second-quarter GDP growth likely would exceed a 1.0% contraction (-1.0%). A

significant change in the monthly deficit detail would have meaningful impact on the pending GDP growth.

Employment/Unemployment (June 2014). The Bureau of Labor Statistics (BLS) also will release its June 2014 labor data on Thursday, July 3rd. Following May's near-consensus and artificially-bloated 217,000 gain in payroll employment, a weaker-than-expected May number is favored by the underlying economic fundamentals.

Based on the headline payroll employment reporting in May, the BLS trend model indicates a 243,000 headline jobs gain for June 2014, as indicated by ShadowStats affiliate www.ExpliStats.com. The consensus outlook tends to settle in around the trend number, but the markets appear to be expecting something closer to 220,000. Accordingly, the headline BLS reporting machine is structured to deliver an upside surprise to the markets, but underlying economic reality, again, would indicate a pending downside surprise to those expectations.

Separately, expectations appear to be for the June U.3 unemployment rate to hold at a highly-troubled 6.3% reading, as seen in April and May. Underlying economic reality and the fundamental drivers of economic activity would suggest a general upturn in U.3, but the BLS's continuing purge of discouraged workers from the unemployment rolls and headline labor force would argue in favor of a lower rate. Separately, as discussed regularly in the employment/unemployment-related *Commentaries*, month-to-month comparisons of U.3 are of no meaning, because of the standard, inconsistent reporting calculations that leave the monthly data not comparable.

If U.3 drops anew, there likely would be additional labor-force loss associated with those relative, but still-not-comparable numbers. The broader U.6 and ShadowStats unemployment measures would tend to hold, or increase anew, at their broader and higher respective levels. All the Labor Department numbers remain unsettled and could come in well outside general expectations.
