

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

COMMENTARY NUMBER 639

Review of the Deepening Economic and Pending U.S. Dollar and Hyperinflation Crises

July 11, 2014

Outlook Continues for Massive U.S. Dollar Sell-Off, Pending Hyperinflation

**U.S. Economy on Track for Downside Shocks that Could Roil Markets and
Provide Political Cover for Reinvigorated Quantitative Easing**

**Fed Has Monetized 76% of Net Issuance of Publicly Held Treasury Debt,
Since January 2013 Expansion of QE3;
Pace of Fed Monetization at 88% Year-to-Date 2014**

PLEASE NOTE: The next regular Commentary is scheduled for Tuesday, July 15th, covering June retail sales. That will be followed by a Commentary on July 16th, covering the June producer price index (PPI) and industrial production, and another on July 17th, covering June housing starts.

TODAY'S COMMENTARY: Although there were no major economic releases this week, the Reporting Detail section covers the concurrent-seasonally-adjusted payroll-employment data that were not covered in the July 3rd [Commentary No. 638](#) on June labor conditions. Regular, major economic reporting for June resumes next week, as covered in the Week Ahead section, with the exception of the June CPI being published one week later than usual (June 2nd).

Material that usually would be found in the Hyperinflation Watch section, including the June M3 estimate and a review of monetary-system activity, instead is in the main text of today's missive, covered in the general review of economic conditions and the pending U.S. dollar and hyperinflation crises.

Best wishes to all! — John Williams

DEEPENING ECONOMIC WOES AND PENDING U.S. DOLLAR AND HYPERINFLATION CRISES

OPENING COMMENTS

Looming Second-Quarter GDP Contraction Could Trigger U.S. Dollar Sell-Off. Now into the second-half of 2014, the broad outlook for a hyperinflationary great depression—beginning this year—has not changed, but it has evolved, with various details continuing to fall into place, such as the renewed downturn in domestic economic activity.

The long-standing 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* of that *First Installment Revised*.

This *Commentary* reviews some elements of the general outlook, along with various updated details in separate *Economic*, *Monetary*, and *Market Conditions* sections.

Declining GDP. U.S. economic activity has turned down anew, with headline first-quarter 2014 GDP contracting at an annualized real pace of 2.9% [-2.9%], following 2.6% fourth-quarter growth. Coming into the July 30th GDP benchmark revisions, and the coincident “advance” estimate of second-quarter GDP, market expectations for second-quarter growth appear to be holding around a positive 3.2%.

Nonetheless, second-quarter growth also likely will be in contraction (see *Commentaries* [No. 637](#) and [No. 638](#)). Negative GDP reporting should be seen in the initial, or subsequent first revision to, headline second-quarter estimate, at the end of July, or August. If the initial estimate in July is positive (as was the initial estimate of first-quarter GDP), it most likely will be enough below consensus expectations to shock the popular outlook towards a “new recession,” with attendant adjustments hitting the markets.

In turn, 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 pressures on the U.S. dollar, as well as potentially resurrect elements of the 2008-Panic. Unexpected economic weakness intensifies stress on an already weakened banking system, hence a perceived need for expanded, not reduced, quantitative easing. Unexpected economic weakness also savages projections of headline, cash-based, federal-budget deficits (particularly the 10-year versions) as well as projected funding needs for the U.S. Treasury. All these crises will combine against the U.S. dollar.

The fundamental issues threatening the dollar could not be worse. They include, but are not limited to:

- A severely damaged U.S. economy, which never recovered post-2008 and is turning down anew, including a sharply widening trade deficit (see *Economic Conditions*).
- The U.S. government not addressing its long-term solvency issues.

- Monetary malfeasance by the Federal Reserve, in its process of seeking to provide liquidity to a troubled banking system, and also to the U.S. Treasury, with a current pace of monetization at 88% of effective net issuance of the federal debt to be held by the public, so far, in calendar-year 2014 (see *Monetary Conditions*).
- Mounting domestic and global crises of confidence in a dysfunctional U.S. government, where the relative positive rating by the public of the U.S. President tends to have a meaningful correlation with the foreign-exchange-rate strength of the U.S. dollar.
- Mounting global political pressures contrary to U.S. interests.

Intensifying weakness in the U.S. dollar will place upside pressure on oil prices and other commodities, boosting domestic 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 (see *Market Conditions*).

ECONOMIC CONDITIONS

When Headline GDP Activity Contracts, Actual Economic Conditions Are Horrendous. Upside biases—built into GDP reporting—usually are enough to eliminate negative headline GDP reporting. When the biases no longer cover contractions—when headline GDP sinks by 2.9% (-2.9%), for example—the actual economy is in severe trouble, as suggested in the chapter on historical downturns in [*2014 Hyperinflation Report—Great Economic Tumble*](#).

Generally reflecting negative revisions in the benchmarking of underlying economic data, such as the trade deficit, industrial production, durable goods orders, retail sales and construction spending, downside revisions to recent GDP reporting are likely in the upcoming annual benchmark revisions to that series. Further detail will be published in a *Commentary* prior to July 30th revisions.

Underlying, current economic and trade activity actually is deteriorating and weak enough relative to first-quarter 2014 that the benchmark GDP revision should be accompanied by an initial (or ensuing first-revision) headline contraction in second-quarter 2014 GDP, on top of a possibly still-deepening first-quarter 2014 GDP contraction (as revised in the benchmarking).

Consumer Liquidity Cannot Support an Economic Rebound. The primary structural issue impeding economic growth remains impaired consumer liquidity. Although the issue has been discussed frequently in these *Commentaries*, the detail is repeated here, where the graphs have been updated for the latest consumer credit outstanding detail.

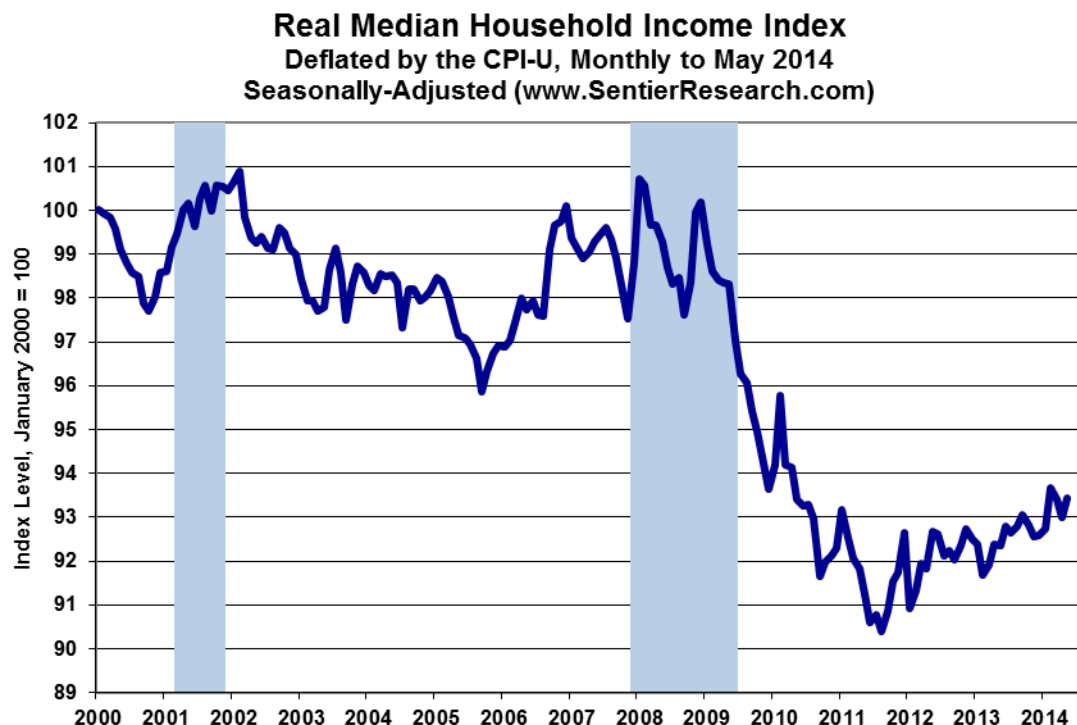
Ongoing structural and fundamental liquidity problems for the consumer are restraining real, or inflation-adjusted, expansion of retail sales, personal consumption and housing activity. Without real growth in income, and without the ability and/or willingness to offset declining purchasing power with debt expansion, the consumer lacks the ability to fuel a traditional, consumption-based recovery in U.S. economic activity. Despite redefinition of the GDP series in July 2013, personal consumption expenditures still account for 68% of GDP activity.

The first two graphs following show real median household income through May 2014, based on numbers provided by www.SentierResearch.com, and consumer credit outstanding, as updated by the Federal Reserve for May 2014.

Real median household income showed continued income stagnation in May 2014, notching higher, but still near the cycle-low for the series. As GDP purportedly started its solid recovery in mid-2009, household income plunged to new lows. Deflated by headline CPI-U, the annual series published by the Census Bureau showed further that annual real median household income in 2012 was at levels seen in the late-1960s and early-1970s (see the *Hyperinflation Report – Second Installment*).

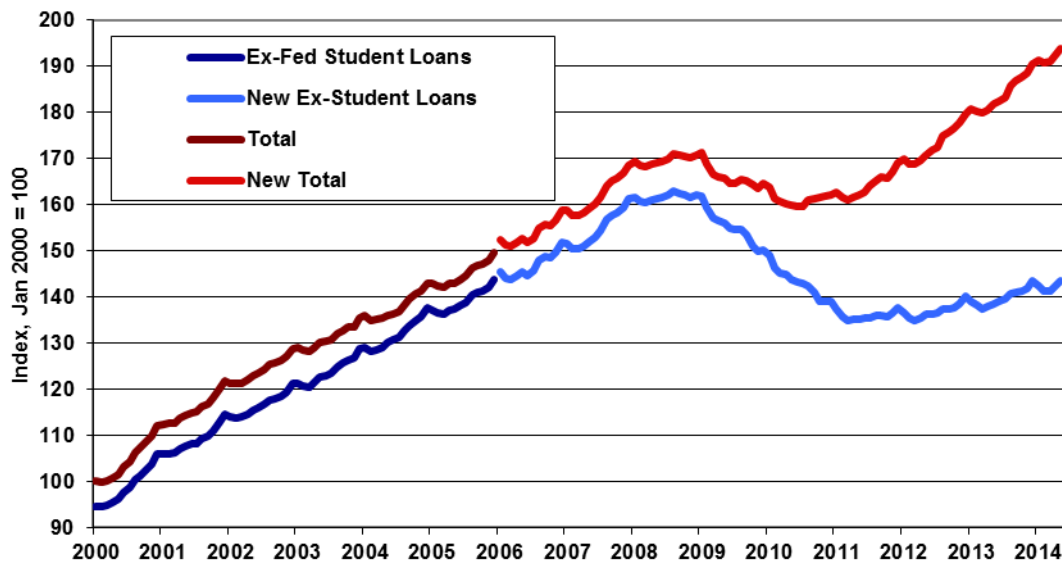
Growth in consumer credit, post-2008 Panic, has continued to be dominated by growth in federally-held student loans, not in bank lending to consumers that otherwise might help to fuel broad consumption growth.

The third and fourth graphs following reflect the final June 2014 reporting of the ever-volatile consumer confidence (Conference Board) and consumer sentiment (University of Michigan) indices. Current levels for both series remain deep in traditional-recession territory. The patterns with these series, as with household income, have been of collapse and stagnation, since 2007, as opposed to the pattern of economic collapse and recovery indicated in the faulty GDP series, at least through its fourth-quarter 2013 reporting.



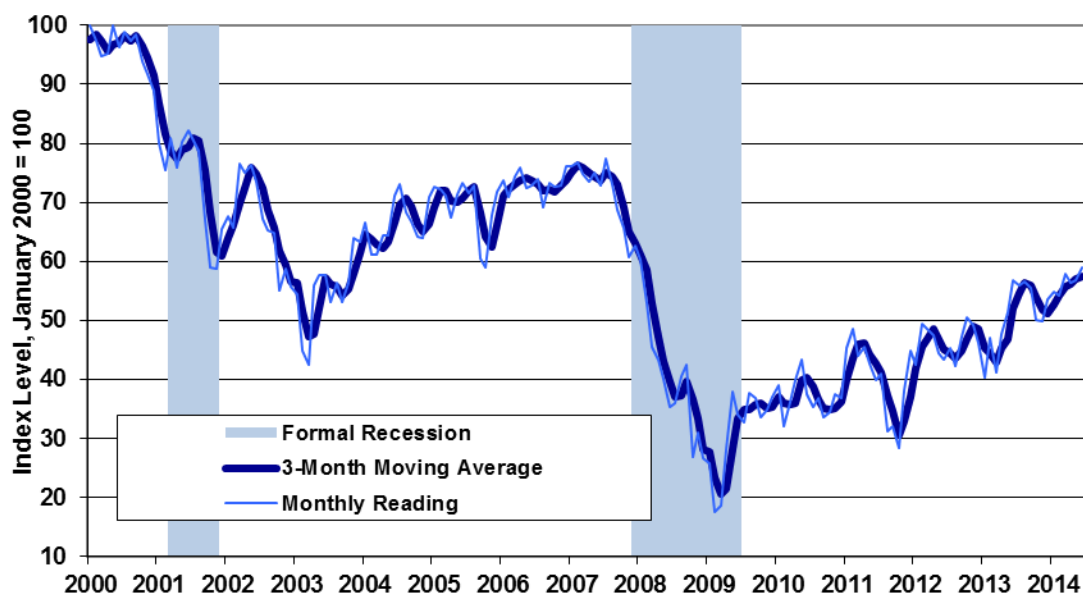
ShadowStats Consumer Credit Outstanding Index Total and Total Ex-Student Loans

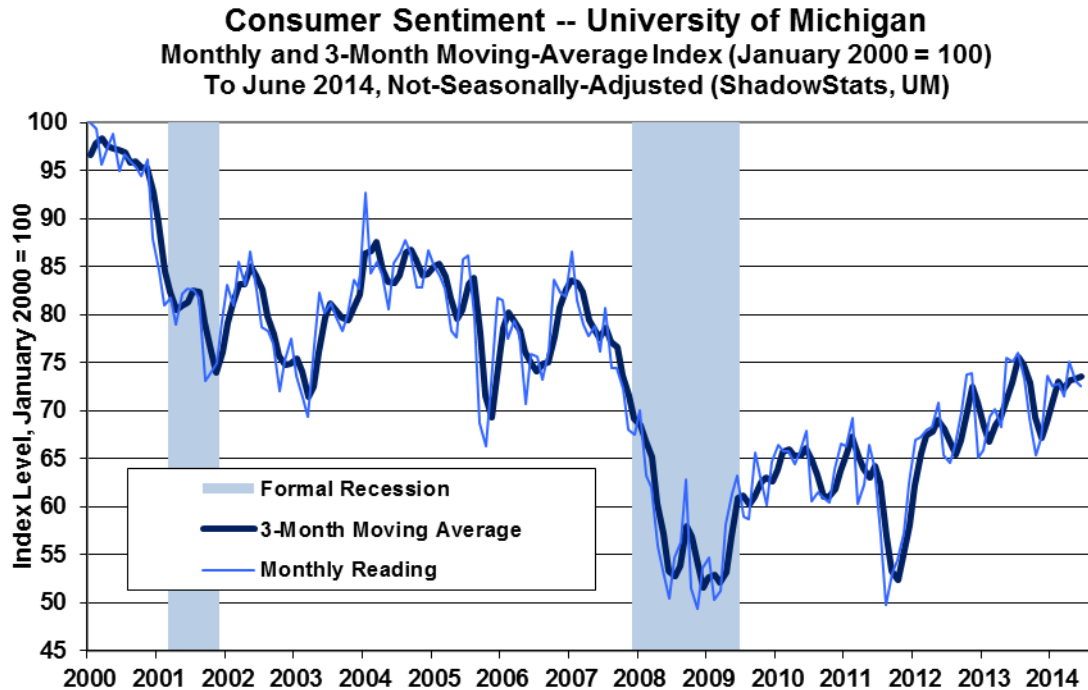
With Jan 2006 Discontinuities, 2010-2011 Discontinuities
Removed, Total Credit Indexed to Jan 2000=100
Through May 2014, NSA (ShadowStats.com, FRB)



Consumer Confidence -- Conference Board

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



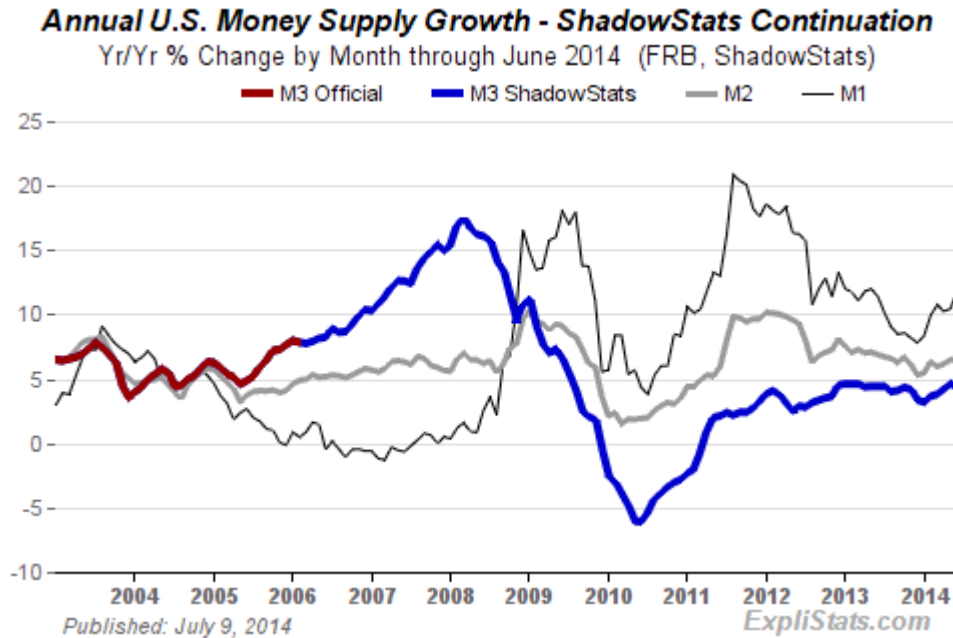


MONETARY CONDITIONS

Money Supply M3 Annual Growth Slowed to 4.4% in June 2014, from 4.6% in May. Annual growth in June 2014 M3 is estimated to have been about 4.4%, down from an unrevised 4.6% in May. Monthly year-to-year growth began to slow after hitting a near-term peak of 4.6% in each of the months of January, February and March 2013, the onset of expanded QE3. Growth then hit a near-term trough of 3.2% in January 2014, but that period of slowing growth had reversed fully as of May 2014, with a slight pullback in June. An initial estimate of annual growth in M3, and first readings of annual growth for M2 and M1 in June 2014 have been posted on the [Alternate Data](#) tab of www.shadowstats.com.

Any revisions in the following numbers are due to recent revisions in underlying data by the Federal Reserve. The seasonally-adjusted, preliminary estimate of month-to-month change for June 2014 money supply M3 showed roughly a 0.1% gain, down from a revised 0.6% (previously 0.5%) in May. Estimated month-to-month M3 changes, however, remain less reliable than are the estimates of annual growth.

Growth for June M1 and M2. For June 2014, year-to-year and month-to-month changes follow for the narrower M1 and M2 measures (M2 includes M1, M3 includes M2). Full definitions of the measures are found in the [Money Supply Special Report](#). M2 for June 2014 showed year-to-year growth of 6.5%, versus a revised 6.6% (previously 6.5%) in May, with month-to-month gain of 0.4% in June, versus a revised 0.7% (previously 0.6%) gain in May. For M1 in June 2014, year-to-year growth was 11.9%, versus a revised 10.5% (previously 10.1%) gain in May, with a month-to-month June gain of 1.5%, versus a revised 0.5% (previously 0.1%) gain in May.



Fed Has Monetized 88% of Net Treasury Debt Issuance for the Public, Year-to-Date. Despite the recent “tapering” in the Federal Reserve’s quantitative easing program, the Fed’s net acquisition of U.S. Treasury securities so far in calendar-year 2014 (through July 9th), versus net debt issuance of the U.S. Treasury for the public in the same period, has reflected effective monetization of 87.9% of the increase in debt. That is an increased portion from the effective monetization of 71.8% of the net issuance of publicly-held debt for the full calendar-year 2013, due partially to some slowing of debt issuance by the Treasury.

That means that from the onset of expanded quantitative easing QE3 in January 2013 to date, the Fed has monetized 75.5% of the increased Treasury debt held by the public. Against, the net increase in total gross federal debt, the Fed effectively has monetized 73.9% of the net debt increase so far in 2014, 61.3% of the total in 2013, and 64.2% of the net debt issuance since the onset of expanded QE3.

The ongoing monetization of the Treasury debt likely was a contributing factor to the recent minimal pickup seen in broad money supply (M3) growth. It also shows that the market in U.S. Treasury securities remains anything but free and open, and it artificially depresses yields and correspondingly boosts bond prices.

FOMC Reservations. Minutes of the last FOMC meeting, released on July 9th, suggested that the QE3 increased purchases of Treasury and mortgage-backed securities would end in October 2014, if the economy performed as “expected.”

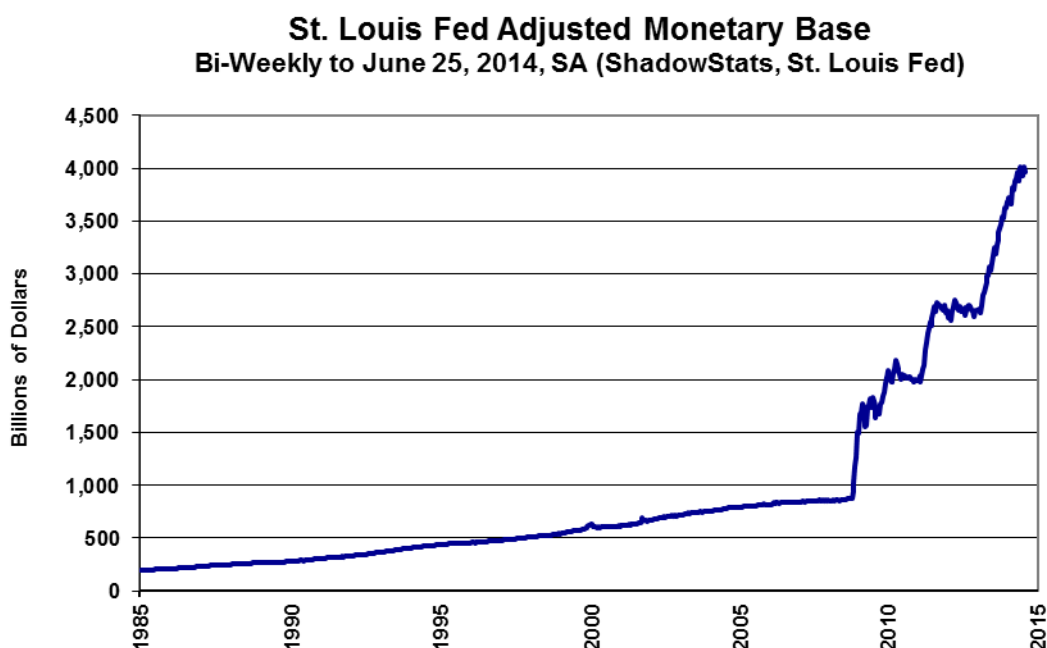
“... [FOMC] participants generally agreed that if incoming information continued to support its expectation of improvement in labor market conditions and a return of inflation toward its longer-run objective, it would be appropriate to complete asset purchases with a \$15 billion reduction in the pace of purchases in order to avoid having the small, remaining level of purchases receive undue focus among

investors. If the economy progresses about as the Committee expects, warranting reductions in the pace of purchases at each upcoming meeting, this final reduction would occur following the October meeting.”

Ongoing economic “improvement,” however, is a highly unstable pre-condition to the Fed ending its asset purchases. As discussed separately in the *Opening Comments*; the economy should prove to be anything but healthy, in the headline reporting of the months ahead. With an intensified economic downturn, the banking system—the Fed’s primary concern—would come under mounting financial stress. Banking system liquidity is likely to flow as needed, with the Fed continuing to use the weakening economy as political cover for any reinvigorated quantitative easing. More, not less, QE3 is the likely outlook for Federal Reserve policy in the year ahead

Monetary Base. As reflected in the following graphs, despite the “tapering” in debt purchases, the monetary base remains topped-out, temporarily, at \$3.963 trillion (June 25th), still near its record high level of \$4.012 trillion (April 16th). Year-to-year growth, however, has started to slow, with the current flat-to-minus level of activity is measured against a year-ago period of rapid growth.

As the dollar began to push recent lows, policy efforts were undertaken in the euro area, again, to drive funds into the U.S. dollar. Similar activity was seen in an effort to counter a nascent U.S. dollar selling panic in August 2011. The underlying fundamentals supporting the U.S. dollar simply could not be worse, as discussed in the *Opening Comments*. A massive dollar sell-off against most other major Western currencies remains likely in the near future.



St. Louis Fed Adjusted Monetary Base, Yr/Yr %
Bi-Weekly to June 25, 2014, SA (ShadowStats, St. Louis Fed)



MARKET CONDITIONS

Economic, Currency and Inflation Shocks Can Roil Various Financial Markets. A renewed economic downturn, massive flight from the U.S. dollar and runaway domestic inflation are not anticipated by consensus forecasters or by the financial markets, at present. As sentiment moves in the direction of those troubles, significant selling likely will hit the stock and bond markets, coincident with a global pummeling of the U.S. dollar. As discussed in the *Hyperinflation Report*, physical gold remains the primary hedge against the financial turmoil ahead. Physical gold and silver will tend to preserve the purchasing power of individual wealth and assets throughout a hyperinflation crisis.

As suggested in the following section, equities may hold fairly steady against official headline CPI inflation, as would inflation-adjusted bonds (except in a hyperinflation, as discussed in the *Second Installment*), but they do not hold even with more-traditional consumer inflation, which measures the cost-of-living on the basis of maintaining a constant standard of living, and on the basis of reflecting actual out-of-pocket expenses. Holding physical gold and silver as stores of wealth resolves the issues in those areas, and provides needed primary hedging against the loss of purchasing power in affected assets.

Some Comparative Market Numbers—Equities versus Gold and Silver. With the extremely volatile financial markets of recent years, it is easy to cherry-pick dates to show desired comparative relative gains and losses in indicators of various financial assets. The price or index changes discussed here simply are measured from December 31, 1999 to date, a period consistently used by ShadowStats for long-term comparative purposes, reflecting activity in the new century; and from December 31, 2013 to date (July 10, 2014), reflecting changes since the beginning of the year.

Putting the gold and silver markets in perspective versus the U.S. stock market—specifically the Dow Jones Industrial Average (DJIA) and the Standard & Poor’s 500 (S&P 500)—as of July 10, 2014, the closing levels for the DJIA and the S&P 500 were down 0.9% and 1.0% from their respective all-time closing highs of July 3, 2014. In contrast, the July 10th London afternoon gold fix was down by 29.3% from its all-time high of September 5, 2011, while the London silver fix was down by 55.8% from its recent historic high of April 29, 2011.

That said, in the period from December 31, 1999 to July 10, 2014, the price of gold rose by 361.8%, with silver up by 303.4%. In contrast, the DJIA gained 47.1%, with the S&P 500 up by 33.7% in the same period of the last 14-plus years.

Year-to-date 2014, from December 31, 2013 to July 10, 2014, the price of gold rose by 11.3%, with silver up by 10.3%. In contrast, the DJIA gained 2.0%, with the S&P 500 up by 6.3% in the same period. Most of the stock-price gains of the last year, and in the last fourteen years, however, have had trouble keeping up with official headline inflation. In contrast, the precious metals have remained well ahead of official inflation. Looking at more realistic inflation numbers, equities have been big losers in terms of maintaining the purchasing power of the U.S. dollar, while the precious metals have offset the damages of actual inflation and most likely will continue to do so (see [Public Commentary on Inflation Measurement, 2014 Hyperinflation Report—The End Game Begins](#) – First Installment Revised page 31, and [2014 Hyperinflation Report—Great Economic Tumble](#) – Second Installment pages 103 and 104).

For example, in real terms, net of headline CPI-U inflation, the price of gold still rose by 225.3%, with silver up by 184.2%, in the period from December 31, 1999 to July 10, 2014. In contrast, the DJIA gained just 3.5%, while the S&P 500 actually declined by 5.8% in the same 14-plus years of activity.

Also in real terms, year-to-date 2014, from December 31, 2013 to July 10, 2014, the price of gold rose by 9.0%, with silver up by 8.0%. In contrast, the near-all-time high DJIA was down by 0.1%, after inflation adjustment, with the S&P 500 up by 4.1% in the same year-to-date period.

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, but the CPI release will about a week later than usual this month (June 22nd).

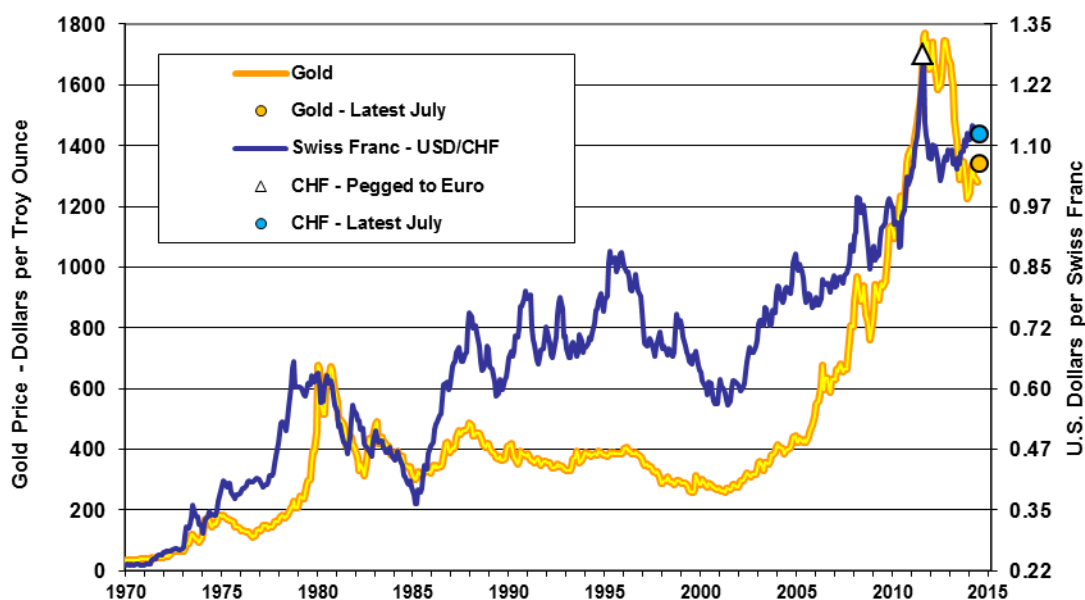
Volatile markets continue, amidst mounting global political tensions, a rapidly weakening U.S. economy and nascent recognition of rising inflation. Related market fears also center on worsening fiscal and monetary instabilities, and deteriorating domestic political circumstances. All these issues have 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 particularly from a weakened U.S. dollar.

As discussed earlier, 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 several years. More-recent oil price volatility increasingly has reflected 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 July” points in the following graphs reflect fixes or closing prices in London or New York, where appropriate, as of July 10th.

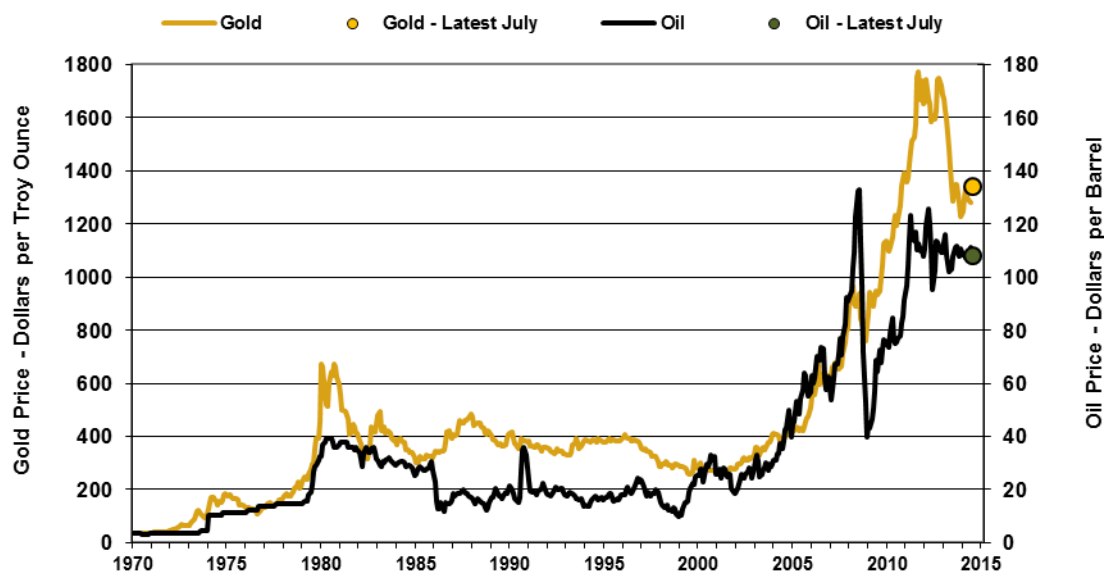
Gold versus Swiss Franc (CHF)

Monthly Average Price or Exchange Rate to June 2014
(ShadowStats.com, Kitco, FRB, WSJ)

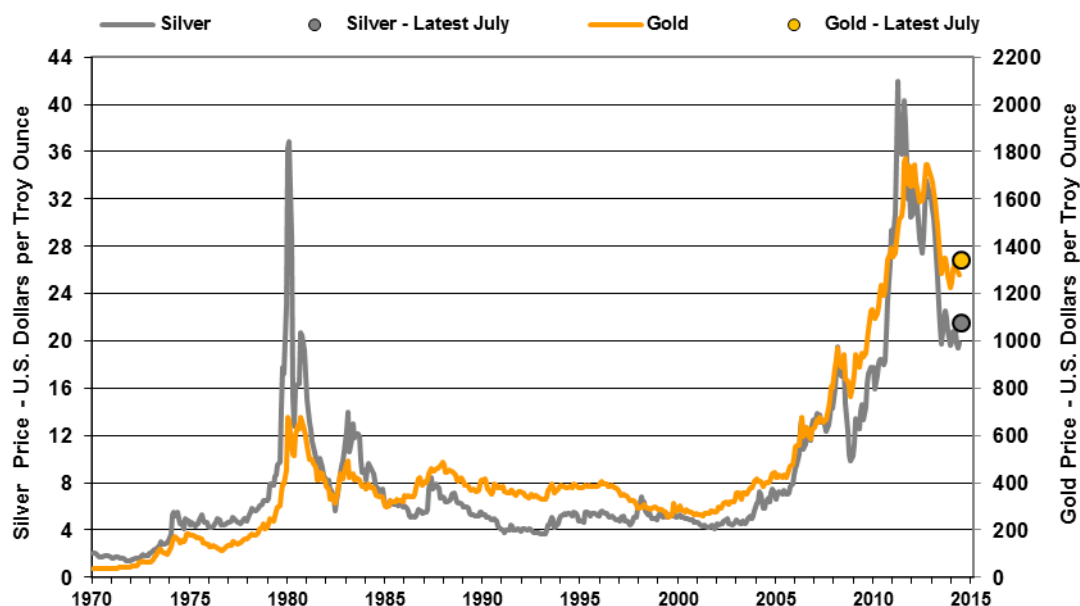


Gold versus Oil (Brent/WTI)

Monthly Average Prices to June 2014, Pre-1987 is WTI
(ShadowStats, Kitco, DOE)



Gold versus Silver Monthly Average Price Levels to June 2014 (ShadowStats, Kitco, Stooq)



REPORTING DETAIL

PAYROLL EMPLOYMENT (JUNE 2014)—SUPPLEMENTAL

Concurrent Seasonal Factor Distortions Bloated the March Headline Jobs Gain to 304,000, Instead of the Consistent 288,000 Number. The following material is supplemental to the June 2014 payroll-employment detail discussed in the prior July 3rd [Commentary No. 638](#). It covers the June concurrent-seasonally-adjusted payroll data as deduced from material made available by the Bureau of Labor Statistics (BLS).

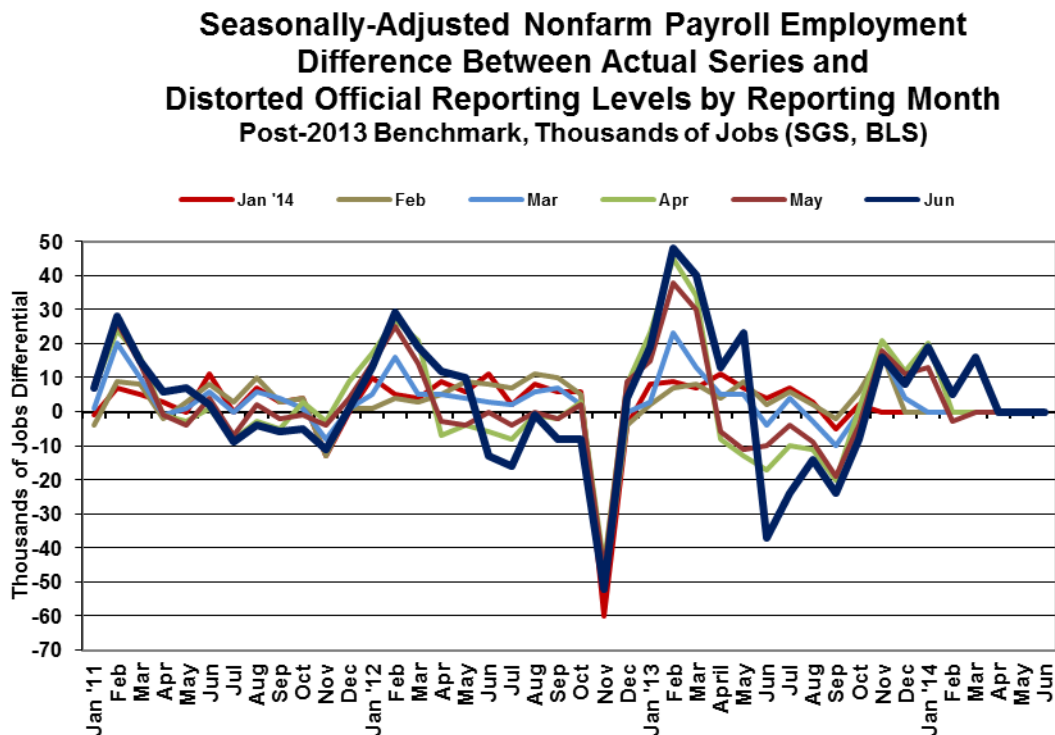
As noted in the prior *Commentary's* text, "...the seasonally-adjusted, month-to-month headline payroll employment gain for June was 288,000 +/- 129,000 (95% confidence interval), above market expectations and the trend model (which was closer than the consensus). The updated trend model will be discussed in next regular *Commentary*. In turn, May payrolls rose by a revised 224,000 (previously 217,000), while April payrolls rose by a revised (also bloated by shifting seasonal factors) 304,000 (previously 282,000,

initially 288,000). Due to the misleading reporting policies used by the BLS, the headline April 2014 gain became non-comparable and inconsistent with the March data as of the June reporting.”

Indeed, the latest headline gain of April 2014 versus March 2014 of 304,000 was wrong. On the basis of comparable month-to-month reporting, the March-to-April gain was 288,000, reflecting consistent reporting of seasonally-adjusted data. Enough detail is available for a third party, such as ShadowStats-affiliate ExpliStats, to calculate the consistent detail.

“Trend Model” Was Closer than the Consensus to Headline Payroll Gain. As discussed in [Commentary No. 633](#), and as described generally in [Payroll Trends](#), the trend indication from the BLS’s concurrent-seasonal-adjustment model—prepared by our affiliate www.ExpliStats.com—was for a June 2014 monthly payroll gain of 243,000, based on the trend structured into the BLS modeling of May’s actual reporting. The late-consensus for June appeared to have been about 220,000, where the headline gain came in at 288,000.

Based on the June 2014 BLS reporting, the trend number built into the BLS seasonal-adjustment model is for a headline gain of 232,000 in July 2014. The consensus outlook for July 2014 most likely will settle around that number.



Concurrent Seasonal Factor Distortions. There are serious and deliberate reporting flaws with the government’s seasonally-adjusted, monthly reporting of both employment and unemployment. Each month, the BLS uses a concurrent-seasonal-adjustment process to adjust both the payroll and unemployment data for the latest seasonal patterns. As each series is calculated, the adjustment process

also revises the monthly history of each series, recalculating prior reporting for every month, going back five years, on a basis that is consistent with the new seasonal patterns of the headline numbers.

The BLS, however, uses and publishes the current estimate, but it does not publish the revised history, even though it calculates the consistent new data each month. As a result, headline reporting generally is neither consistent with, nor comparable to earlier reporting, and month-to-month comparisons of these popular numbers usually are of no substance, other than for market hyping or political propaganda.

The BLS explains that it avoids publishing consistent, prior-period revisions so as not to “confuse” its data users. No one seems to mind if the published earlier numbers are wrong, particularly if unstable seasonal-adjustment patterns have shifted prior jobs growth or reduced unemployment into current reporting, without any formal indication of the shift from the previously-published historical data. The preceding, accompanying graph shows how far the monthly data have strayed from being consistent, as of the latest June 2014 reporting, versus the most recent benchmark revision to the series.

Note: Issues with the BLS’s concurrent-seasonal-factor adjustments and related inconsistencies in the monthly reporting of the historical time series are discussed and detailed further in the ShadowStats.com posting on May 2, 2012 of [Unpublished Payroll Data](#).

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 are 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 sharp pace of economic decline seen in real first-quarter 2014 GDP, which 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, which likely would follow the reporting of a headline contraction in second-quarter 2014 GDP real growth.

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, when concurrent seasonal adjustments are used (as with retail sales, durable goods orders, employment and unemployment data). These issues have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series.

PENDING RELEASES:

Retail Sales (June 2014). The Census Bureau’s June 2014 retail sales estimate is scheduled for release on Tuesday, July 15th. As discussed in the updated section on *Consumer Liquidity Conditions*, the consumer remains in an extreme liquidity bind. Accordingly, odds favor headline retail sales reporting coming in well below market expectations, which appear to be for a relatively strong headline monthly gain of about 0.6%, boosted at least partially by rising consumer inflation. Even so, an outright month-to-month contraction in seasonally-adjusted nominal sales remains a fair possibility. Separately, the headline June CPI-U (due for publication on July 22nd) is a good bet to top any headline nominal gain in sales, pushing inflation-adjusted or “real” retail sales growth into monthly contraction, if the nominal reporting has not done so already. Watch out for downside revisions to prior-period reporting.

Index of Industrial Production (June 2014). On Wednesday, July 16th, the June 2014 index of industrial production will be released by the Federal Reserve Board. Market expectations appear to be for a small headline gain of 0.2% to 0.3%, but fundamental weakness and downside surprises to market expectations are likely, as companies continue reducing excessive inventory levels, in line with softening consumption. As usual, this series is subject to large prior-period revisions, which should tend to be to the downside.

Producer Price Index—PPI (June 2014). The June 2014 PPI also is scheduled for release on Wednesday, July 16th, by the Bureau of Labor Statistics (BLS). A month-to-month increase is likely, reflecting a broad spectrum of goods-related inflation, including energy, food and “core” inflation components (ex-food and energy). Depending on the oil contract followed, not-seasonally-adjusted monthly-average oil prices were up by 1.3% to 3.5% for the month of June, along with a 0.4% unadjusted

monthly increase in average retail gasoline prices. PPI seasonal adjustments for energy costs should be strongly to the plus-side in June.

The wildcard in this revamped PPI remains the newly-added services sector, which largely is unpredictable, volatile and of limited meaning due to its inflation measurements having minimal relationship to real-world activity. Although the new series is less dependent on the increasingly “antiquated” concepts of oil, food and “core” (ex-food and energy) inflation, services costs should see continuing inflationary pressures—and shrinking profit margins—from rising prices in the “hard” economy. Accordingly, the aggregate headline June PPI inflation most likely will show at least a minimal headline monthly increase.

Residential Construction—Housing Starts (June 2014). On Thursday, July 17th, the Census Bureau will publish its estimate of June 2014 housing starts. Despite extreme monthly volatility seen regularly in the reporting of this series, and despite near-perpetual wishful upside market expectations for housing starts—although June expectations appear to be for close to a headline “unchanged” reading—month-to-month change likely will continue a pattern of statistical-insignificance, with ongoing stagnation and renewed downturn or downside revisions. As usual, this series is subject to large prior-period revisions.

In the wake of a 75% collapse in aggregate activity from 2006 through 2008, and an ensuing five-year pattern of housing starts stagnation at historically low levels, little has changed. Again, as was discussed in the updated section on *Consumer Liquidity Conditions*, there remains no chance of a near-term, sustainable turnaround in the housing market, unless there is a fundamental upturn in consumer and banking-liquidity conditions. That has not happened and does not appear to be in the offing.
