

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

**COMMENTARY NUMBER 703**  
**February Nominal Retail Sales and U.S. Dollar, Fed and Markets**  
**March 12, 2015**

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**Retail Sales Collapse Continued,  
Both Monthly and Quarterly, Before and After Inflation**  
**Unusual Monthly Shifts in Seasonal Adjustments Have Masked  
Headline Monthly Sales Contractions Exceeding 1% (-1%)**  
**Underlying Economic Data Closing in on  
Setting a First-Quarter 2015 GDP Contraction**  
**U.S. Economy Cannot Support Current Dollar and Stock-Market Strength;  
Political and Market Positioning of Fed Policy Increasingly Is Untenable**

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*PLEASE NOTE: The next regular Commentary, scheduled for Monday, March 16th, will cover February industrial production and the produce price index (PPI), a further Commentary on March 17th will cover February housing starts.*

*Best wishes to all — John Williams*

**OPENING COMMENTS AND EXECUTIVE SUMMARY**

**Dollar Strength and Current Expectations for Fed Policy Depend on Strong U.S. Economy.** Today's unexpectedly large decline in February retail sales—where a modest gain had been expected—was the type of economic "surprise" that could become the proximal trigger for heavy selling of the U.S. dollar.

After decades of lack of confidence in the U.S. currency, recent flight into what otherwise has been a persistently troubled dollar is not likely to be durable or sustainable in the context of heavy fundamental hits against unsupportable and unraveling expectations.

More "surprises," like the retail sales, loom in the near future. Discussed extensively in [No. 692 Special Commentary: 2015 - A World Out of Balance](#), unsustainable expectations of a recovered and booming U.S. economy have distorted domestic and global markets, creating a false impression of a Federal Reserve beginning to regain control of its monetary policy, and of a domestic U.S. financial system and markets that have regained basic stability. The economic shock still pending for the global markets is that the U.S. system is no better off than the rest of the world and, in many ways, U.S. conditions are worse.

The global markets will come to recognize that and the related implications for Fed policy in a highly politicized U.S. circumstance. Those issues, in confluence with a large variety of U.S.-dollar negatives overhanging the markets (see [No. 692](#) and the *Hyperinflation Outlook Summary*), should place the U.S. dollar under massive selling pressure, with horrendous implications for domestic inflation and financial stability.

***An Increasingly Likely, New GDP Contraction Begins to Unfold.*** With the January trade data suggesting the trade deficit will be a major, negative contributor to first-quarter 2015 GDP activity (see [Commentary No. 702](#)); with the retail sales reporting likely to show a real (inflation-adjusted) contraction in the first-quarter; and with negative surprises a fair bet for both February 2015 industrial production and housing starts in next week's headlines; market expectations quickly could shift to a contracting U.S. GDP. That would be an event inconsistent with much of the hype underlying the current strength of the dollar and the markets.

***Retail Sales Troubles.*** Following the industry 's weakest Holiday Season since the economic collapse in 2008, and in the context of a January monthly plunge of 0.8% (-0.8%), headline February 2015 retail sales dropped unexpectedly by 0.6% (-0.6%). Market expectations had been for a monthly gain of 0.3% [Bloomberg]. That weakness was fundamental, not an artefact of the weather, and it has to have triggered some rethinking of the U.S. economic circumstance, for many in the global markets. This unfolding story will be reviewed next week, following the releases of the industrial production and housing starts details.

If March 2015 retail sales held even with the February headline level of nominal sales, the first-quarter 2015 nominal retail series would suffer an annualized quarterly contraction of 6.06% (-6.06%), versus the fourth-quarter 2014. That would be the weakest showing since the worst of the 2008 economic collapse.

A nominal quarterly contraction here is a virtual certainty, where headline March retail sales would have to rise by a record 5.0% for the month, in order to pull first-quarter 2015 sales even with fourth-quarter 2014. The highest monthly growth ever seen for the series was 2.9% in June 2006, followed by the second strongest growth ever of 2.6%, in April of 1993. The chances of a real (inflation-adjusted) quarterly contraction in retail sales also are extremely high.

Underlying reality likely is much worse. Discussed in the *Seasonal Factor Distortions in the Reporting Detail Section*, the consecutive monthly headline declines for the last three months each likely exceeded 1.3% (-1.3%), versus the headline average of 0.8% (-0.8%), with the differences due to monthly revisions in seasonal adjustments, and inconsistent reporting of same, tied to the concurrent seasonal adjustment process used in preparing the headline data.

**Today's Missive (March 12th).** The balance of today's *Commentary* concentrates on the detail from the February 2015 nominal retail sales data and related liquidity issues. The *Week Ahead* section previews the reporting of the February producer price index (PPI), industrial production and housing starts.

**Nominal Retail Sales—February 2015—Third Straight Month of Plunging Activity, First-Quarter 2015 Sales Downturn Is Unavoidable.** Again, following the weakest Holiday Season since the 2008 economic collapse, and in the context of a January monthly plunge of 0.8% (-0.8%), February 2015 retail sales dropped unexpectedly by 0.6% (-0.6%), for the third straight month. Market expectations had been for a monthly gain of 0.3% [Bloomberg].

Year-to-year nominal growth slowed to 1.7% in February 2015, versus 3.6% in January 2015, the weakest showing since November 2009 and, in terms of being in down-trending annual growth, the weakest since the onset of the economic collapse in 2008. Based on two months of reporting, first-quarter 2015 nominal retail sales are contracting at an annualized pace of 6.1%, versus fourth-quarter 2014, with a quarterly contraction a virtual certainty, as discussed in the preceding opening paragraphs.

The aggregate decline in monthly retail activity was broadly based, dominated by declining automobile sales, with generally negative-to-weak activity across a wide variety of major retail outlets, with sales gains at food services and drinking places, gas stations and at sporting goods and nonstore retailers. The underlying problem with current retail sales activity remains the intense, structural-liquidity woes constraining consumer activity, discussed in the *Consumer Liquidity* section.

**Nominal (Not-Adjusted-for-Inflation) Retail Sales—February 2015.** In nominal terms—before adjustment for consumer inflation—headline February 2015 retail sales declined by 0.58% (-0.58%), which was marginally statistically-significant. Such was in the context of downside revisions to headline activity in December and January. Net of prior-period revisions, the monthly decline in February was 0.63% (-0.63%). The February 2015 monthly decline followed a statistically-significant, revised decline of 0.81% (-0.81%) in January 2015, and a revised December 2014 monthly decline of 0.89% (-0.89%).

**Year-to-Year Annual Change.** Year-to-year sales growth in February 2015 slowed to a statistically-significant 1.69%, versus a revised annual gain of 3.61% in January 2015, and a revised 3.31% in December 2014.

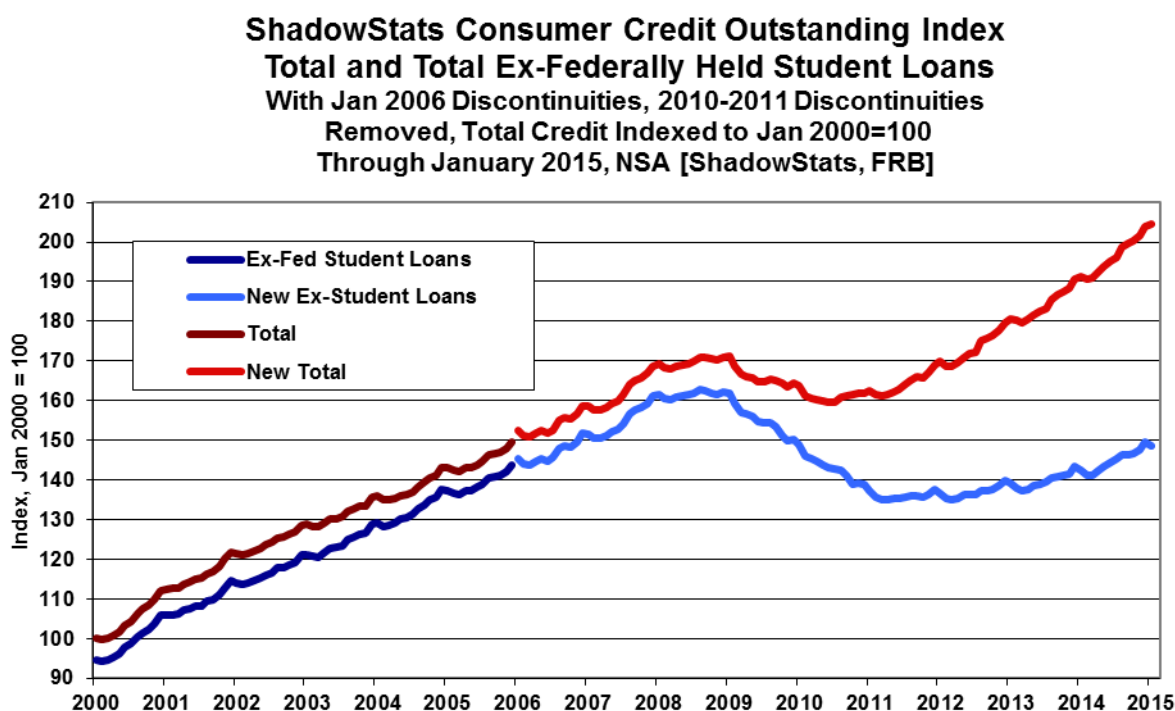
**Annualized Quarterly Growth on Track for a First-Quarter Contraction.** The pace of annualized nominal retail sales change in first-quarter 2015, based solely on the levels of headline nominal activity in January and February 2015, was a contraction of 6.06% (-6.06%). Discussed in the opening paragraphs of this *Commentary*, a first-quarter contraction is a virtual certainty. That is against revised fourth-quarter 2014 versus third-quarter annualized growth of a positive 1.85%, and third-quarter versus second-quarter annualized growth of 4.27%.

**Real (Inflation-Adjusted) Retail Sales—February 2015.** The headline 0.58% (-0.58%) drop in February 2015 retail sales was before accounting for inflation. Real retail sales change in February will be

reviewed along with the headline estimate of consumer inflation for the February 2015 CPI-U, in the *Regular Commentary* of Tuesday, March 24th.

Although unadjusted gasoline prices rose month-to-month in February, seasonal adjustments likely will turn the adjusted monthly gasoline prices used in the CPI to a monthly decline, with the headline aggregate February CPI-U flat-to-down for the month, as result. Yet, as with December 2014 and January 2015 reporting, real retail sales in February 2015 still should show a monthly contraction. That would be the third straight headline monthly decline in real retail sales, and the first such pattern seen since May 2010. Separately, annual real growth in February 2015 should confirm an ongoing, historical warning signal of imminent recession.

**Consumer Liquidity Update—January 2015 Consumer Credit Outstanding.** The underlying problem with current retail sales activity remains intense, structural-liquidity woes besetting the consumer. That circumstance, during the last seven-plus years of economic collapse and stagnation, has continued to prevent a normal recovery in broad U.S. economic activity, as detailed extensively in [Commentary No. 699](#), [No. 692 Special Commentary: 2015 - A World Out of Balance](#), and as updated in [Commentary No. 702](#). The consumer liquidity series will be reconsolidated and updated fully, including the latest charts from the Federal Reserve's flow-of-funds data, in the *Regular Commentary* of March 17th, covering February housing starts.



Without real (inflation-adjusted) 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 traditional, consumption-based growth or recovery in U.S. economic activity. That activity includes not only retail

sales and the still-dominant personal-consumption account of the GDP, but also residential investment and related construction spending (see *Week Ahead* section). With a significant portion of consumers under financial stress, there has been no basis for a sustainable economic expansion since the Panic of 2008, and there are no prospects for a recovery in the near future.

**Consumer Credit Outstanding.** Updated in the preceding graph is the regular plot of nominal, monthly consumer credit outstanding, through January 2015, reflecting the latest monthly detail from the Federal Reserve Board. Post-2008 Panic, consumer credit has been dominated by growth in federally-held student loans, not in bank loans to consumers that otherwise would fuel broad consumption growth. Before any consideration for inflation, the nominal level of consumer credit outstanding (ex-student loans) has not rebounded or recovered since the onset of the recession. These disaggregated data are available and plotted only on a not-seasonally-adjusted basis.

*[Further background material on February nominal retail sales is found in the Reporting Detail section. Various drill-down and graphics options on the headline labor data are available to subscribers at our affiliate: [www.ExpliStats.com](http://www.ExpliStats.com).]*

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## HYPERINFLATION WATCH

### HYPERINFLATION OUTLOOK SUMMARY

**Economic and Inflation Outlooks Unchanged, Continuing to Unfold.** *[Note: The text in this section largely is as published in the prior Commentary].* Other than for some updated comment on the Swiss franc and the addition of internal references to today's *Commentary* (all changes underlined), the text here is unchanged.

[No. 692 Special Commentary: 2015 - A World Out of Balance](#) of February 2, 2015 updated the *Hyperinflation 2014* reports and the broad economic outlook. Previously, 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 2, 2014, and publication of [2014 Hyperinflation Report—Great Economic Tumble](#) – *Second Installment*, on April 8, 2014. The outlooks also are updated regularly in the weekly *Commentaries*. The *Opening Comments* of [No. 692](#) should be considered in terms of recent circumstances and near-term, proximal triggers for massive dollar selling. The two *2014 Hyperinflation Report* installments, however, remain the primary background material for the hyperinflation and economic analyses and forecasts.

**Primary Summary.** Current fiscal conditions show the effective long-term insolvency of the U.S. government, a circumstance that usually would be met by unfettered monetization of the national debt and obligations, leading to an eventual hyperinflation. The 2008 Panic and near-collapse of the financial system, and official (U.S. government and Federal Reserve) response to same, pulled the elements of the eventual hyperinflation crisis at the end of this decade into the current period. The primary and basic summary of the broad outlook and the story of how and why this fiscal, financial and economic crisis has unfolded and developed over the years—particularly in the last decade—is found in the *Opening Comments* and *Overview and Executive Summary* of that *First Installment Revised* (linked earlier). The following summarizes the underlying current circumstance and recent developments.

Consistent with the above *Special Commentaries*, the unfolding economic 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. Physical gold and silver, and holding assets outside the U.S. dollar, remain the primary hedges against the pending total loss of U.S. dollar purchasing power, despite sharp and generally ongoing rally in the U.S. dollar's exchange rate since mid-2014 and broadly related selling pressures in the gold and silver markets.

Current relative U.S. economic strength and the relative virtuousness of Fed monetary policy versus major U.S. trading partners are seriously over-estimated (*see today's Opening Comments*). A crash back to recognition of realistic domestic-economic circumstances likely will be accompanied by a crash in the U.S. dollar versus major currencies, such as the Swiss franc, Canadian dollar and Australian dollar; related rallies in precious metals and oil; and related sell-offs in the domestic stock and bond markets. Further, a sharp deterioration in near-term domestic U.S. political stability continues to develop and is of meaningful near-term risk for triggering heavy selling of the dollar.

**Current Economic Issues versus Underlying U.S. Dollar Fundamentals.** U.S. economic activity is turning down anew, despite overstated growth in recent GDP reporting. GDP and other major economic series face heavy downside-benchmark revisions through the end of July. Weak, underlying economic reality also should become increasingly and painfully obvious to the financial markets in the reporting and revisions of the weeks and months ahead for series such as retail sales, production, the trade deficit and payroll employment.

As financial-market expectations shift towards renewed or deepening recession, that circumstance, in confluence with other fundamental issues, particularly deteriorating domestic political conditions, should reverse recent buying pressures, to mounting and massive selling pressures against the U.S. dollar, as well as potentially to resurrect elements of the Panic of 2008.

Unexpected economic weakness intensifies the known stresses on an already-impaired banking system, increasing the perceived need for expanded, not reduced, quantitative easing (*see Opening Comments*). The highly touted "tapering" by the FOMC ran its course. Future, constructive Fed behavior—purportedly moving towards normal monetary conditions in the currently unfolding, near-perfect economic environment—is pre-conditioned by a continued flow of "happy" economic news. Suggestions that all is right again with world are nonsense. The Panic of 2008 never has been resolved, and the Fed soon will find that it has no easy escape from its quantitative easing (QE3), which continues. Only overt expansion of QE3 ceased; QE4 will become the question.



The economy has not recovered; the banking system is far from stable and solvent; and the Federal Reserve and the federal government still have no way out. Significant banking-system and other systemic (*i.e.* U.S. Treasury) liquidity needs will be provided, as needed, by the Fed, under the ongoing political cover of a weakening economy—a renewed, deepening contraction in business activity. The Fed has no choice. Systemic collapse is not an option for the Board of Governors. This circumstance simply does not have a happy solution.

Accordingly, any renewed market speculation as to an added round of Federal Reserve quantitative easing, QE4, could become a major factor behind crashing the dollar and boosting the price of gold. The Fed has strung out its options for propping up the system as much as it could, with continual, negative impact on the U.S. economy. The easings to date, however, appear to have been largely a prop to the increasingly unstable equity markets.

In the event of a QE4, any resulting renewed boost to U.S. equities would be a fleeting illusion, at least in terms of real value (purchasing power of the dollar). Such gains would tend to be losses, in real terms, with the stocks valued in terms of Swiss francs, for example, or valued against what would become a rapidly-increasing pace of domestic U.S. inflation.

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. Current fiscal "good news" is from cash-based, not GAAP-based and accounting projections.

All these crises should combine against the U.S. dollar, likely in the very-near future. That said, recent faux market perceptions of domestic economic, financial-system and monetary tranquility have boosted the U.S. dollar's strength significantly in global trading and have contributed to savaging the prices of oil and in weakening the prices of precious metals.

The recent shift in the Swiss franc due to the elimination of the effective pegging of the franc to the euro and, by default to the U.S. dollar, also had had the effect of allowing some upside movement in the dollar prices of gold and silver. Recent intensified weakness in the euro, however, has led to increasingly negative domestic Swiss interest rates and interventions aimed at depressing the franc. Such policies usually prove to be fleeting, due to significant undesired side effects on the domestic economy and in financial-market distortions.

Again, strength in the U.S. dollar should reverse, in the context of underlying reality outlined here and in the sections that follow. The actual fundamental problems threatening the U.S. dollar could not be worse. The broad outlook has not changed; it is just a matter of market perceptions shifting anew, against the U.S. currency. That process, again, started with the shift in Swiss National Bank policy. Key issues include, but are not limited to:

- ***A severely damaged U.S. economy, which never recovered post-2008, is turning down anew and shows no potential for recovery in the near-term.*** The circumstance includes a renewed widening in the trade deficit (see [Commentary No. 702](#)), as well as ongoing severe, structural-liquidity constraints on the consumer, which are preventing a normal economic rebound in the traditional, personal-consumption-driven U.S. economy (see [Opening Comments](#)). Sharply-negative economic reporting shocks, versus unrealistically-positive consensus forecasts, remain a heavily-favored, proximal trigger for the pending dollar debacle.

- ***U.S. government unwillingness to address its long-term solvency issues.*** Those controlling the U.S. government have demonstrated not only a lack of willingness to address long-term U.S. solvency issues, but also the current political impossibility of doing so. The shift in control of Congress does not appear to have altered the systemic unwillingness to address the underlying fundamental issues, specifically to bring the GAAP-based deficit into balance. Any current fiscal "good news" comes from cash-based, not GAAP-based accounting projections. The GAAP-based version continues to run around \$5 trillion for the annual shortfall, while those in Washington continue to increase spending and to take on new, unfunded liabilities. The history and issues here are explored in the first installment of the *Hyperinflation Report*, as previously linked; the initial fiscal-2014 details were discussed in [Commentary No. 672](#), and the official GAAP-based financial statements for 2014 will be discussed fully, soon (see [Commentary No. 702](#)).
- ***Monetary malfeasance by the Federal Reserve, as seen in central bank efforts to provide liquidity to a troubled banking system, and also to the U.S. Treasury.*** Despite the end of the Federal Reserve's formal asset purchases, the U.S. central bank monetized 78% of the U.S. Treasury's fiscal-2014 cash-based deficit (see [Commentary No. 672](#)). The quantitative easing QE3 asset purchase program effectively monetized 66% of the total net issuance of federal debt to be held by the public during the productive life of the program (beginning with the January 2013 expansion of QE3). The monetization process was completed with the Federal Reserve refunding the interest income it earned on the Treasury securities to the U.S. Treasury. With highly tenuous liquidity conditions for the banking system and the Treasury, it would not be surprising in this period of increasing instability to see covert Federal Reserve activities masked in the purchases of Treasury debt by nations or other entities financially friendly to or dependent upon the United States. Renewed expansion to quantitative easing remains likely, given ongoing banking-system stresses, vulnerable stock markets and weakening, actual U.S. economic activity. As has been commonplace, the Fed likely would seek political cover for new or expanded systemic accommodation in any "renewed" economic distress.
- ***Mounting domestic and global crises of confidence in a dysfunctional U.S. government.*** The positive rating by the public of the U.S. President tends to be an indicative measure of this circumstance, usually with a meaningful correlation with the foreign-exchange-rate strength of the U.S. dollar. The weaker the rating, the weaker tends to be the U.S. dollar. The positive rating for the President is off its historic low, but still at levels that traditionally are traumatic for the dollar. Chances of a meaningful shift towards constructive cooperation between the White House and the new Congress, in addressing fundamental issues appear to be nil. Issues such as non-recovered, faltering economic activity and the consumer liquidity crisis, and addressing the nation's long-range solvency issues still could devolve rapidly into an extreme political crisis.
- ***Mounting global political pressures contrary to U.S. interests.*** Downside pressures on the U.S. currency generally are mounting, or sitting in place, in the context of global political and military developments contrary to U.S. strategic, financial and economic interests. Current conditions include the ongoing situation in Ukraine versus Russia and extremely-volatile circumstances in the Middle East. U.S. response to the Ukrainian situation may be behind part of the recent strength in the U.S. dollar and related weakness in oil prices, with U.S. actions aimed at causing financial distress for Russia. The situation has yet to run its full course, and it has the potential to reverse rapidly.



- ***Spreading global efforts to dislodge the U.S. dollar from its primary reserve-currency status.*** Active efforts or comments against the U.S. dollar continue to expand. In particular, anti-dollar rhetoric and actions have been seen with Russia, China, France, India and Iran, along with some regular rumblings in OPEC and elsewhere. Recent dollar strength may have bought some time versus those who have to hold dollars for various reasons. Nonetheless, any short-term instability and a quick reversal in the dollar's strength could intensify the "dump-the-dollar" rhetoric rapidly.

When the selling pressure breaks massively against the U.S. currency, the renewed and intensifying weakness in the dollar will place upside pressure on oil prices and other commodities, boosting domestic inflation and inflation fears. Domestic willingness to hold U.S. dollars will tend to move in parallel with global willingness, or lack of willingness, to do the same. These circumstances will trigger the early stages of a hyperinflation, likely in the year ahead.

Both the renewed dollar weakness and the resulting inflation spike should boost the prices of gold and silver, where physical holding of those key precious metals remains the ultimate hedge against the pending inflation and financial crises. Investors need to preserve the purchasing power and liquidity of their wealth and assets during the hyperinflation crisis ahead. Again, see Chapter 10, [\*2014 Hyperinflation Report—Great Economic Tumble\*](#) for detailed discussion on approaches to handling the hyperinflation crisis.

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## REPORTING DETAIL

### RETAIL SALES (February 2015)

**Retail-Sales Plunged for Third-Month, First-Quarter Downturn Is Set.** Following the industry 's weakest Holiday Season since the economic collapse in 2008, and in the context of a January monthly plunge of 0.8% (-0.8%), headline February 2015 retail sales dropped unexpectedly by 0.6% (-0.6%). Market expectations had been for a monthly gain of 0.3% [Bloomberg]. This type of economic "surprise" is the type of event that could become the proximal trigger for heavy selling against the U.S. dollar. More "surprises" like this loom in the near future.

Year-to-year nominal growth slowed to 1.7% in February 2015, versus 3.6% in January 2015, the weakest showing since November 2009 and, in terms of being in down-trending annual growth, the weakest since the onset of the economic collapse in 2008. Based on two months of reporting, first-quarter 2015 nominal retail sales are contracting at an annualized pace of 6.1%, versus fourth-quarter 2014, with a quarterly contraction a virtual certainty, as discussed in the opening paragraphs of the *Opening Comments*.

The aggregate decline in monthly retail activity was broadly based, dominated by declining automobile sales, with generally negative-to-weak activity across a wide variety of major retail outlets, with sales gains at food services and drinking places, gas stations and at sporting goods and nonstore retailers.

***Structural Liquidity Issues Constrain Consumer Economic Activity.*** The underlying problem with current retail sales activity remains intense, structural-liquidity woes besetting the consumer. That circumstance—in the last seven-plus years of economic collapse and stagnation—has continued to prevent a normal recovery in broad U.S. economic activity, has been discussed extensively in [Commentary No. 699](#), [No. 692 Special Commentary: 2015 - A World Out of Balance](#), and as updated in [Commentary No. 702](#) and today's *Opening Comments*.

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 traditional, consumption-based growth or recovery in U.S. economic activity, including retail sales and the still-dominant personal-consumption account of the GDP. With a significant portion of consumers under financial stress, there has been no basis for a sustainable economic expansion since the Panic of 2008, and there are no prospects for a recovery in the near future.

***Nominal (Not-Adjusted-for-Inflation) Retail Sales—February 2015.*** In nominal terms—before adjustment for consumer inflation—today's (March 12th) report on February 2015 retail sales—issued by the Census Bureau—showed a statistically-significant, seasonally-adjusted, headline monthly decline, for a third month. February sales fell by a marginally-significant 0.58% (-0.58%) +/- 0.58% (this and all other confidence intervals are expressed at the 95% level). Such was in the context of downside revisions to headline activity in December and January. Net of prior-period revisions, the monthly decline in February was 0.63% (-0.63%).

The February 2015 monthly decline followed a statistically-significant, revised decline of 0.81% (-0.81%) +/- 0.35% [previously down by 0.79% (-0.79%)] in January 2015, and a revised December 2014 monthly decline of 0.89% (-0.89%) [previously down by 0.86% (-0.86%), initially down by 0.94% (-0.94%)].

***Year-to-Year Annual Change.*** Year-to-year sales growth in February 2015 slowed to a statistically-significant 1.69% +/- 0.53%, versus a revised gain of 3.61% [previously up by 3.33%] in January 2015, and a revised 3.31% annual gain [previously up by 3.34%, initially up by 3.17%] in December 2014.

***Annualized Quarterly Growth on Track for a First-Quarter Contraction.*** The pace of annualized nominal retail sales change in first-quarter 2015, based solely on the levels of headline nominal activity in January and February 2015, was a contraction of 6.06% (-6.06%) [based only on initial January reporting, that previously was a contraction of 4.81% (-4.81%)] (see opening paragraphs in *Opening Comments*). Fourth-quarter 2014 versus the third-quarter sales rose at a revised annualized pace of 1.85% [previously up by 1.88%, initially up by 1.77%], with third-quarter versus second-quarter growth at a 4.27% annualized pace.

***February Core Retail Sales—Stabilized Gasoline Prices.*** In an environment of generally rising food prices, and with an unadjusted 4.21% monthly gain in gasoline prices, seasonally-adjusted monthly grocery-store sales rose by 0.46% in February 2015, with gasoline-station sales gaining 1.45% for the month.

Under normal conditions, the bulk of non-seasonal variability in food and gasoline sales is in pricing, instead of demand. “Core” retail sales—consistent with the Federal Reserve’s preference for ignoring food and energy prices when “core” inflation is lower than full inflation—are estimated using two approaches:

Version I: February 2015 versus January 2015 seasonally-adjusted retail sales series—net of total grocery store and gasoline station sales—reflected a monthly decline of 0.93% (-0.93%), versus the official headline drop of 0.58% (-0.58%).

Version II: February 2015 versus January 2015 seasonally-adjusted retail sales series—net of the monthly change in revenues for grocery stores and gas stations—reflected a monthly decline of 0.75% (-0.75%), versus the official headline contraction of 0.58% (-0.58%).

***Real (Inflation-Adjusted) Retail Sales—February 2015.*** The headline 0.58% (-0.58%) drop in February 2015 retail sales was before accounting for inflation. Real retail sales change in February will be reviewed along with the headline estimate of consumer inflation for the February 2015 CPI-U, in the *Regular Commentary* of Tuesday, March 24th.

Although unadjusted gasoline prices rose month-to-month in February, seasonal adjustments likely will turn the adjusted monthly gasoline prices used in the CPI to a monthly decline, with the headline aggregate February CPI-U flat-to-down for the month, as result. Yet, as happened in December 2014 and January 2015, adjusted for negligible or negative inflation, real retail sales in February 2015 still should be in monthly contraction. That would be the third straight headline monthly contraction in real retail sales and the first such pattern since May 2010.

Annual real growth in February 2015 should confirm an ongoing, historical warning signal of imminent recession.

***Retail-Sales Benchmark Revision on April 30th.*** The Census Bureau has scheduled its annual retail-sales benchmark revision for April 30, 2015. The revisions there likely will play catch up on the downside, where consideration of some negative-revision detail was excluded from last year’s benchmarking, due to lingering impact from the shutdown of the federal government in October 2013.

***Seasonal-Factor Distortions and Other Reporting Instabilities.*** The usual seasonal-factor distortions were at play, again, in February 2015 reporting, where the headline data reflected concurrent seasonal adjustments. Given Census Bureau reporting procedures, the headline detail is not comparable with most earlier reporting. Accordingly, current data can reflect growth shifts from earlier periods, without the specifics being published. The principles and reporting issues with the way the government reports economic series adjusted by concurrent seasonal factors were explored, in-depth, in [Commentary No. 695](#). The adjustment issues here are the same as with the employment and unemployment series.

As has been the common pattern, the year-ago numbers for January 2014 and February 2014 were revised, along with the publication of the February 2015 data and revised detail on December 2014 and January 2015. The year-ago revisions simply were junk reporting, due solely to shifts in their seasonal adjustments that resulted from the unique calculations of the seasonal factors producing the headline February 2015 detail, not due to the availability of any new historical data back in early-2014. Where all

other seasonally-adjusted historical numbers also were revised, though, those details were not published. Only the new details for January and February 2014 were provided for the earlier numbers.

Specifically, a 0.3% (-0.3%) downside revision to January 2014 and a 0.5% upside revision to February 2014 sales indicated meaningful shifts in current headline seasonal-adjustment factors. They likely were enough to mitigate the headline February 2015 contraction by 0.8%, enough to widen the headline February 2015 monthly decline of 0.6% (-0.6%), to a monthly decline of 1.4% (-1.4%). The same gimmick last month was enough to mute the headline January decline to 0.8% (-0.8%), instead of what otherwise would have been a 1.3% (-1.3%) decline (see [Commentary No. 696](#)). That same pattern also was seen in December 2014 revisions. All this happens without the specifics as to where headline activity has been shifted month-to-month. Full detail is available internally to the Census Bureau, but the Bureau chooses not publish the detail.

The current reporting process allows for invisible shifts in seasonally-adjusted current activity, which are not consistent with published historical reporting. Further, the stability of the seasonal-adjustment process (particularly the concurrent-seasonal-adjustment process used with retail sales) and sampling methods have been disrupted severely by the unprecedented depth and length of the current economic downturn in the post-World War II era, the period of modern economic reporting.

Again, retail sales reporting suffers the same inconsistency issues seen with other series, such as payroll employment, the unemployment rate, and durable goods orders. The highly variable and unstable seasonal factors here continued to cloud relative activity in the December 2014-to-February 2015, and in the January 2014-to-February 2014 periods, five months that are published on a non-comparable basis with all other historical data.

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## WEEK AHEAD

**Headline Reporting and Revisions Should Trend Much Weaker versus an Overly-Optimistic Economic Consensus; Inflation Will Rise Anew, Following the Bottoming of Oil-Prices.** Shifting some to the downside, again, amidst wide fluctuations in the numbers, market expectations for business activity remain overly optimistic in the extreme. They exceed any potential, underlying economic reality. Downside corrective revisions and an accelerating pace of downturn in broad-based, monthly headline economic reporting should hammer those expectations heavily through mid-year. Recent GDP excesses will not face downside revisions until the July 30, 2015 GDP benchmark revision, other than for the one monthly revision still pending for fourth-quarter 2014 GDP.

Headline consumer inflation—recently driven lower by collapsing prices for gasoline and other oil-price related commodities—likely hit or was close to a near-term low in January 2015 reporting. Significant upside inflation pressures should resume as oil prices rebound, a process that already appears to be

underway, and one that would accelerate rapidly with an eventual sharp downturn in the exchange-rate value of the U.S. dollar. These areas, the general economic outlook and longer range reporting trends are reviewed broadly in [No. 692 Special Commentary: 2015 - A World Out of Balance](#).

***A Note on Reporting-Quality Issues and Systemic-Reporting Biases.*** Significant reporting-quality problems remain with most major economic series. Beyond gimmicked changes to reporting methodologies of the last several decades, ongoing headline reporting issues are tied largely to systemic distortions of seasonal adjustments. Data instabilities were induced partially 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. The severity and ongoing nature of the downturn provide particularly unstable headline economic results, when concurrent seasonal adjustments are used (as with retail sales, durable goods orders, employment, and unemployment data, see the prior labor data related [Commentary No. 695](#)). Combined with recent allegations of Census Bureau falsification of data in its monthly Current Population Survey (the source for the Bureau of Labor Statistics' Household Survey), these issues have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series (see [Commentary No. 669](#)).

#### ***PENDING RELEASES:***

**Producer Price Index—PPI (February 2015).** The February 2015 PPI is scheduled for release tomorrow, Friday, February 13th, by the Bureau of Labor Statistics (BLS). The PPI-release detail will be covered in the ShadowStats *Commentary* of Monday, March 16th. With the collapse in oil and gasoline prices having bottomed out in February, at least temporarily, some rebound in the headline monthly PPI also is likely. With that turnaround in energy prices, late-market expectations are for a moderate headline gain in the February PPI of 0.3% [Bloomberg]. Such expectations are reasonable, perhaps slightly on the high side.

The energy sector, once again, should be the dominant component in the headline data, but on the upside in February 2015, for the first time since June 2014. Oil prices peaked in June and then turned down as the U.S. established overt and covert financial sanctions against Russia, related to the circumstance in Ukraine.

Based on the two most-widely-followed oil contracts, not-seasonally-adjusted, monthly-average oil prices rose by 7.1% and by 21.6% in the month of February, along with a 4.2% increase in unadjusted monthly-average, retail-gasoline prices (Department of Energy). PPI seasonal adjustments for energy costs in February usually are negative, but not enough to turn the Final Demand Energy component of the February Final Demand Goods inflation measure negative on a headline monthly basis.

Inflation in food, “core” goods (everything but food and energy), some still-spreading inflationary impact from hard-goods into the soft-services sector, all should help on the plus side. Perversely, though, rising energy costs should help to reduce services margins, which tends to be deflationary in the headline services reporting.

The wildcard in the PPI remains the services sector, which largely is unpredictable, volatile and of limited meaning, due to its inflation measurements having minimal if any relationship to real-world activity.



Nonetheless, the services sector has a greater weighting in the PPI calculation than does the old goods sector.

The services series, in theory, is much-less dependent on the increasingly "antiquated" concepts of oil, food and "core" (ex-food and energy) inflation of the "hard" production-based economy. Services "inflation" recently has shown upside movement, due to rising profit margins. Perversely, the rising profit margins and "inflation" were due to energy costs falling faster than any related price decreases were being passed along to the next level of distribution or consumption. The process should see some reversal in February's reporting. Such is disconnected from the goods-related inflation and from common experience. The general approach here to "wholesale" inflation remains of highly-questionable merit.

**Index of Industrial Production (February 2015).** On Monday, March 16th, the Federal Reserve Board will release its estimate of the index of industrial production for February 2015. Early market expectations appear to be for a modest (less than 0.5%), headline monthly increase, but risks are high for a downside reporting surprise in headline activity, very possibly a monthly contraction and/or significant downside revisions to prior reporting of recent months.

Whatever the headline results, activity most meaningfully is viewed net of extreme swings in utility usage, resulting from, or reversing, the prior month-to-month effects of "unseasonable weather." Weather patterns have been unusual recently and have added to monthly volatility of the series.

**Residential Construction—Housing Starts (February 2015).** The Census Bureau will release February 2015 residential construction detail, including housing starts, on Tuesday, March 17th. In line with common reporting experience of recent years, monthly results are likely to be unstable, not statistically meaningful, but generally consistent with down-trending stagnation in the series, particularly when viewed in the context of a six-month moving average of activity. This series also is subject to regular and extremely-large prior-period revisions.

As discussed in [Commentary No. 660](#) on the August 2014 version of this most-unstable of monthly economic series, the monthly headline reporting detail here simply is worthless, again, best viewed in terms of a six-month moving average. Not only is month-to-month reporting volatility extreme, but also those headline monthly growth rates rarely come close to being statistically-significant. Early-market expectations appear to be for a decline in February reporting, probably reflecting weather concerns. Even so, that still is well shy of what—until recently—would have been expectations of a headline monthly gain. Market expectations increasingly are shifting towards renewed decline in residential construction.

In the wake of a 75% collapse in aggregate activity from 2006 through 2008, and of an ensuing five-year pattern of housing-starts stagnation at historically low levels, little has changed. Discussed frequently in these *Commentaries*, there remains no chance of a near-term, sustainable turnaround in the housing market, until there is a fundamental upturn in consumer and banking-liquidity conditions. That has not happened and does not appear to be in the offing, as discussed in the *Opening Comments*.