John Williams'

Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 709
February Trade Deficit, Construction Spending

April 2, 2015

**For Purposes of the Initial First-Quarter 2015 GDP Estimate,
Growth Will Be Hammered by a Quarterly Widening of the Real Trade Deficit
and a Quarterly Downturn in Real Construction Spending**

PLEASE NOTE: The next regular Commentary, *scheduled for tomorrow, Friday, April 3rd, will cover March 2015 employment and unemployment, and the preliminary annual growth estimate for money supply M3. Given the amount of material to be reviewed, that posting likely will be late in the day.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

First-Quarter GDP Increasingly Looks Like a Contraction. The advance estimate of first-quarter 2015 GDP will be published on April 29th, but it will be based on less-than-complete underlying detail. In the case of the trade deficit and construction spending—both series adjusted for inflation—the quarterly data include only the initial headline numbers for January and February 2015, as covered in this *Commentary*. Both series show a pending hit to GDP growth, with a widening first-quarter trade deficit likely to reduce the headline GDP growth rate by a full percent, with a quarterly contraction in the real construction spending, adding further downside pressure to the GDP number.

The latest pending GDP outlook—increasingly looking like a quarterly contraction—will be updated with tomorrow's April 3rd *Commentary*, and the latest detail on March employment and unemployment.

Today's Missive (April 2nd). The balance of today's *Commentary* concentrates on the specifics of the February trade deficit and construction spending. The *Hyperinflation Outlook Summary* section has not changed since *Commentary No. 706*. The *Week Ahead* section previews tomorrow's reporting of the March 2015 employment and unemployment.

Trade Deficit—February 2015—Real Deficit Narrowed in February versus January but Widened for First-Quarter. Headline trade activity reflected a continued decline in oil prices, with the effect of the headline "real" or inflation-adjusted trade deficit for January and February widening enough, versus fourth-quarter 2014 reporting, to generate a negative-growth contribution to the upcoming initial estimate of first-quarter 2015 GDP activity. This was despite a much-sharper narrowing in the headline, February trade deficit, before inflation adjustment.

In the context of a wider January 2015 nominal trade deficit, in revision, the headline nominal (before inflation adjustment) February 2015 deficit narrowed by $7.2 billion to $35.4 billion [Bloomberg consensus was $41.5 billion]. That headline improvement largely was accounted for by a $2.3 decline in imports of oil- and petroleum-related products and a $2.6 billion decline in imports of capital equipment. The headline numbers also may have reflected some labor- and weather-related delays in the movement of goods, both from an import and export standpoint.

Nonetheless, due to the continued plunge in imported oil prices, about half of the headline narrowing of the nominal monthly deficit was due to lower inflation. Adjusted for prices (again, such as declining oil costs), the deficit in oil related transactions actually widened instead of narrowing.

Nominal (Not-Adjusted-for-Inflation) February 2015 Trade Deficit. The BEA and the Census Bureau reported this morning, April 2nd, that the nominal, seasonally-adjusted monthly trade deficit in goods and services for February 2015, on a balance-of-payments basis, narrowed by $7.232 billion to $35.444 billion in February 2015, versus a revised $42.676 (previously $41.752) billion in January 2015, and narrowed versus a $41.891 billion in February 2014.

As to month-to-month trade patterns, the headline $7.232 billion narrowing of February 2015 deficit reflected a $2.990 billion decline in monthly exports, with an even greater offsetting decline of $10.223 billion in monthly imports (there is a minor rounding difference). Again, the decline in imports was impacted heavily by the continuing plunge in prices for crude oil and petroleum-related products.

Aside from temporarily declining oil prices, the ongoing trend should continue to be for significant monthly, quarterly and annual deterioration in the U.S. trade deficit, both before and particularly after adjustment for inflation. Look for a sharp widening of the headline real deficit in March 2015, along with a widening of the February shortfall in the accompanying revision.

Energy-Related Petroleum Products. For February 2015, the not-seasonally-adjusted average price of imported oil continued to plunge, down to $49.53 per barrel, from $58.96 per barrel in January 2015, and down from $91.53 per barrel in February 2014. Also not-seasonally-adjusted, physical oil import volume in February 2015 averaged 6.659 million barrels per day, down from 7.186 million in January 2015, and 7.590 million in February 2014.

Real (Inflation-Adjusted) February 2015 Trade Deficit. Adjusted for seasonal factors, and net of oil-price swings and other inflation (2009 chain-weighted dollars, also as used in GDP deflation), the February 2015 merchandise trade deficit (no services) narrowed to $50.764 billion, from a revised $54.582 (previously $53.616) billion in January 2015. It also widened sharply versus a $48.002 billion real deficit in February 2014.

As now reported, the annualized quarterly real merchandise trade deficit stood at $554.7 billion for fourth-quarter 2013, $587.3 billion for first-quarter 2014, $616.5 billion for second-quarter 2014, $583.2 billion for third-quarter 2014, and $609.5 billion for fourth-quarter 2014.

Based on headline reporting for February 2015 and the revised January 2015—the two months on which the first estimate of first-quarter 2015 GDP will be based—the annualized trade shortfall for first-quarter 2014 was at an annualized pace of $632.076 billion. That is enough of a deterioration versus fourth-quarter 2014 GDP to subtract a full percentage point from the aggregate first-quarter headline GDP annualized growth rate.

Construction Spending—February 2015—Real Spending Contracted in First-Quarter 2015. In the context of a downwardly revised, deeper headline monthly contraction of 2.0% (-2.0%) in January, "real" or inflation-adjusted spending, February 2015 spending declined by 0.2% (-0.2%) for the month On a year-to-year basis, the inflation-adjusted contraction in January 2015 spending was 0.5% (-0.5%), versus a 0.1% gain in February.

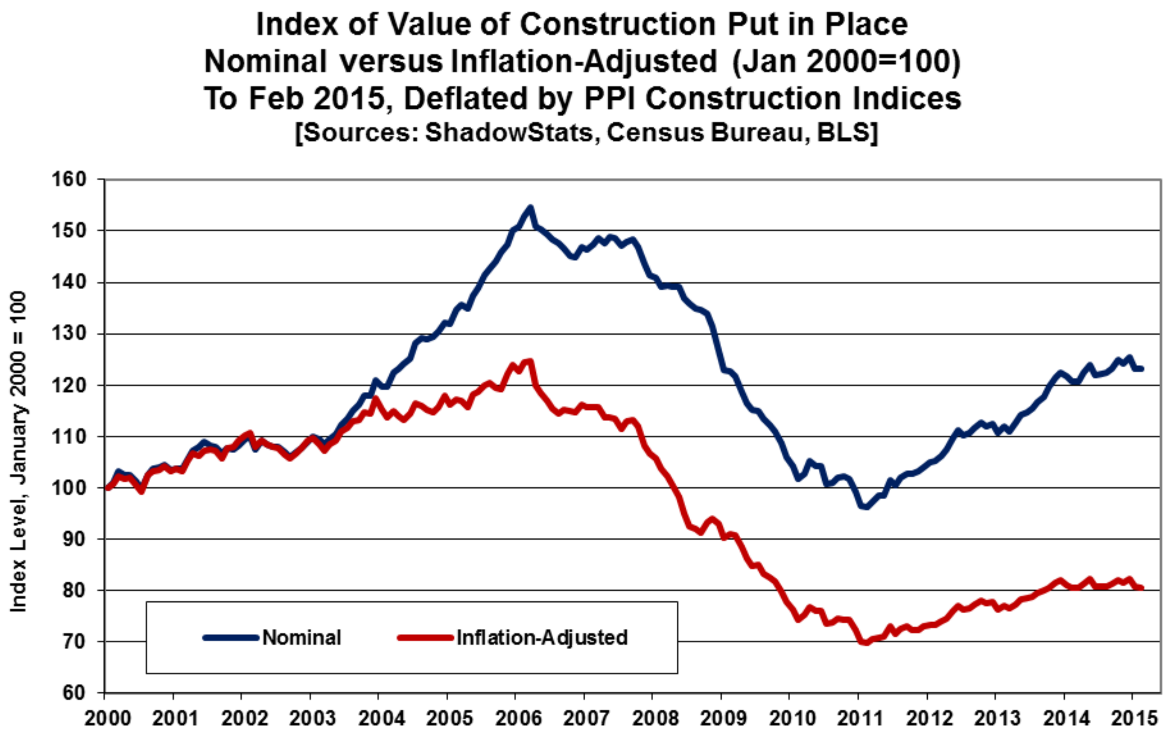
Based on January and February reporting—the only months that will be available for the initial estimate of first-quarter 2015 GDP on April 29th—first-quarter 2015 real spending fell at an annualized quarterly pace of 6.4% (-6.4%), versus an annualized quarterly gain of 4.9% in fourth-quarter 2014. Presently at, or near, the recent low of the down-trending pattern of stagnation, the real construction spending series stood at 35.4% below its pre-recession high of March 2006.

These numbers are reflected in following of graph real and "nominal" or not-adjusted-for-inflation detail. The historical pattern remains one that does not support the headline, real-GDP story of a full economic recovery and post-recession expansion since 2009.

In nominal terms, before inflation adjustment, the headline monthly decline was 0.1% (-0.1%) for February. That decline in activity was not statistically meaningful, as is usual for headline monthly changes to this series. The nominal year-to-year gain of 2.1% in February spending was statistically meaningful, but, again, the gain was due almost entirely to inflation.

PPI Final Demand Construction Index (FDCI). ShadowStats uses the Final Demand Construction Index (FDCI) component of the Producer Price Index (PPI) for deflating the aggregate activity in the construction-spending series. For the historical series in the accompanying graph, the numbers are deflated by the NCI through November 2009, and by the FDCI thereafter (further discussion in *Reporting Detail*.)

For February 2015, the seasonally-adjusted FDCI month-to-month inflation was a positive 0.09%, versus a 0.36% increase in January 2015. In terms of year-to-year inflation, the February FDCI was up by 2.00%, versus 1.91% in January 2015.



Headline Reporting for February 2015. The headline, total value of construction put in place in the United States for February 2015 was $967.2 billion, on a seasonally-adjusted—but not-inflation-adjusted—annual-rate basis. That estimate was down month-to-month by a statistically-insignificant 0.1% (-0.1%), versus a revised $967.9 in January 2015, which was down by a revised 1.7% (-1.7%) from a revised $984.5 billion in December 2014. The revised December spending was up by a revised 1.0%, versus an unrevised November spending level. All the monthly construction-spending data, back through January 2013, will be subject to an annual benchmark revision, along with next month's statistical release on May 1st.

Adjusted for the FDCI inflation measure in the PPI, aggregate real spending in February 2015 fell by 0.2% (-0.2%), following a revised monthly decline of 2.0% (-2.0%) in January 2015, and up by a revised 1.0% for the month in December 2014.

On a year-to-year or annual-growth basis, February 2015 construction spending rose by a statistically-significant 2.1%, versus a revised 1.4% annual gain in January, and a revised 2.4% gain in December 2014. Net of construction costs indicated by the FDCI, however, year-to-year change in spending was an annual gain of 0.1% in February 2015, versus a revised annual contraction of 0.5% (-0.5%) in January 2015, and a revised annual gain of 0.3% in December 2014.

The statistically-insignificant, headline monthly contraction of 0.1% (-0.1%) in nominal February construction spending, versus a 1.7% (-1.7%) monthly drop in January 2015 spending, included a monthly decline of 0.8% (-0.8%) in February public spending, versus a 3.2% (-3.2%) drop in January spending. Private spending rose by 0.2% in February, but fell by 1.1% (-1.1%) in January. Within total private construction spending, the residential sector declined by 0.2% (-0.2%) in February, versus a 0.2% gain in January, while the nonresidential sector rose by 0.5% in February, having contracted in January by 2.4% (-2.4%). These changes are reflected in the graphs in the *Reporting Detail* section.

[The* Reporting Detail *section contains further background material on the trade deficit and construction spending reporting. Various drill-down and graphics options on the headline trade numbers are available to subscribers at our affiliate:* www.ExpliStats.com*.]

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HYPERINFLATION WATCH

HYPERINFLATION OUTLOOK SUMMARY

General Outlook Unchanged; Intensifying Economic Weakness Begins to Impact Fed Policy and U.S. Dollar Strength. *[Note: The text has not been changed since* Commentary No. 706 *of March 24th, other than for adjustments to internal links.]*

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. One other reference should be considered here, in terms of underlying economic reality, and that is the *Public Commentary on Inflation Measurement*.

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 have been over-estimated heavily by the global markets, and structural faults have started to appear in the foundation underpinning recent U.S. dollar strength (see *Commentary No. 706* and *Commentary No. 705*). Some minor pullback in the dollar has taken place in in recent days, as increasing signs of U.S. economic weakness—unanticipated by the global markets—have begun to threaten the expected near-term hiking of U.S. interest rates by the Federal Reserve.

A crash back to recognition of more-realistic domestic-economic circumstances looms, and it 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 intensify and is of meaningful near-term risk for providing further fuel for 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 has begun to surface in headline reporting and should become increasingly and painfully obvious to the financial markets in the headline detail and revisions of the weeks and months ahead, for series such as real retail sales, production, housing and construction, 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 intensify mounting and eventually massive selling pressures against the U.S. dollar, fully reversing the dollar's gains of the last eight months, pushing the dollar to historic lows. The nascent currency crisis also has meaningful potential 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 *Commentary No. 706*). The highly touted "tapering" by the FOMC ran its course. Future, more-constructive Fed behavior—purportedly moving towards normal monetary conditions in what had been an unfolding, near-perfect economic environment—was pre-conditioned by a continued flow of "happy" economic news. Suggestions that all was right again with world were nonsense. The Panic of 2008 never was 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 near-term 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, if they have not already begun to do so. That said, recent faux market perceptions of domestic economic, financial-system and monetary tranquility had boosted the U.S. dollar's strength significantly in global trading and contributed to savaging the prices of oil and in weakening the prices of precious metals. That process may be reversing.

The January 2015 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 the effect of allowing some temporary upside movement in the dollar prices of gold and silver. Recent intensified weakness in the euro, however, had led to increasingly-negative domestic Swiss interest rates and interventions aimed at depressing the franc, prop the dollar. Such policies usually prove to be fleeting, due to significant undesired side effects on the domestic economy and in financial-market distortions. Again, these markets remain in a state of flux, with recent movement continuing against the dollar.

Strength in the U.S. dollar should continue to reverse, sharply 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, with no potential for recovery in the near-term.*** The circumstance includes a renewed widening in the trade deficit, 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 *Commentary No. 702*). Sharply-negative economic reporting shocks, versus still-unrealistically-positive consensus forecasts, remain a heavily-favored, proximal trigger for the intensifying the unfolding 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 has not 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 are nil. Issues such as non-recovered, faltering economic activity and the consumer liquidity crisis, and addressing the nation's long-range solvency issues should continue to devolve, into 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. Temporary, recent dollar strength may have bought some time versus those who have to hold dollars for various reasons. Nonetheless, developing short-term instabilities 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 handing the hyperinflation crisis and *No. 692 Special Commentary: 2015 - A World Out of Balance*, for other factors afoot in the current environment.

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REPORTING DETAIL

U.S. TRADE BALANCE (February 2015)

Real Trade Deficit Narrowed in February versus January but Widened for First-Quarter 2015. Headline trade activity reflected a continued decline in oil prices, with the effect of the headline "real" or inflation-adjusted trade deficit for January and February widening enough, versus fourth-quarter 2014 reporting, to generate a negative-growth contribution to the upcoming initial estimate of first-quarter 2015 GDP activity. This was despite a much-sharper narrowing in the headline, February trade deficit, before inflation adjustment.

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Nonetheless, due to the continued plunge in imported oil prices, about half of the headline narrowing of the nominal monthly deficit was due to lower inflation. Adjusted for prices (again, such as declining oil costs), the deficit in oil related transactions actually widened instead of narrowing.

Nominal (Not-Adjusted-for-Inflation) February 2015 Trade Deficit. The BEA and the Census Bureau reported this morning, April 2nd, that the nominal, seasonally-adjusted monthly trade deficit in goods and services for February 2015, on a balance-of-payments basis, narrowed by $7.232 billion to $35.444 billion in February 2015, versus a revised $42.676 (previously $41.752) billion in January 2015, and narrowed versus a $41.891 billion in February 2014.

As to month-to-month trade patterns, the headline $7.232 billion narrowing of February 2015 deficit reflected a $2.990 billion decline in monthly exports, with an even greater offsetting decline of $10.223 billion in monthly imports (there is a minor rounding difference). Again, the decline in imports was impacted heavily by the continuing plunge in prices for crude oil and petroleum-related products.

Aside from temporarily declining oil prices, the ongoing trend should continue to be for significant monthly, quarterly and annual deterioration in the U.S. trade deficit, both before and particularly after adjustment for inflation. Look for a sharp widening of the headline real deficit in March 2015, along with a widening of the February shortfall in the accompanying revision.

Energy-Related Petroleum Products. For February 2015, the not-seasonally-adjusted average price of imported oil continued to plunge, down to $49.53 per barrel, from $58.96 per barrel in January 2015, and down from $91.53 per barrel in February 2014. Also not-seasonally-adjusted, physical oil import volume in February 2015 averaged 6.659 million barrels per day, down from 7.186 million in January 2015, and 7.590 million in February 2014.

Ongoing Cautions on Data Quality. Although not obvious in today's headline reporting, labor disruptions at U.S. ports may have had near-term impact on headline imports and exports, with some potential further impact from extreme-weather issues involving transportation on the Great Lakes. Separately, potentially heavy distortions in headline data continue from seasonal adjustments. Similar issues have been seen with other economic releases, such as retail sales and payrolls, where the headline number reflects month-to-month change. Discussed frequently (see *2014 Hyperinflation Report—Great Economic Tumble – Second Installment* for example), the extraordinary length and depth of the current business downturn have disrupted regular seasonality patterns. Accordingly, the markets should not rely too heavily on the accuracy of the monthly headline data.

Real (Inflation-Adjusted) February 2015 Trade Deficit. Adjusted for seasonal factors, and net of oil-price swings and other inflation (2009 chain-weighted dollars, also as used in GDP deflation), the February 2015 merchandise trade deficit (no services) narrowed to $50.764 billion, from a revised

$54.582 (previously $53.616) billion in January 2015. It widened sharply versus a $48.002 billion real deficit in February 2014.

As now reported, the annualized quarterly real merchandise trade deficit stood at $554.7 billion for fourth-quarter 2013, $587.3 billion for first-quarter 2014, $616.5 billion for second-quarter 2014, $583.2 billion for third-quarter 2014, and $609.5 billion for fourth-quarter 2014.

Based on headline reporting for February 2015 and the revised January 2015—the two months on which the first estimate of first-quarter 2015 GDP will be based—the annualized trade shortfall for first-quarter 2014 was at an annualized pace of $632.076 billion (it had been $643.392 billion based solely on the initial January reporting). That is enough of a widening versus fourth-quarter 2014 GDP to subtract a full percentage point from the aggregate first-quarter headline GDP annualized growth rate.

CONSTRUCTION SPENDING (February 2015)

Real Construction Spending Showed First-Quarter 2015 Contraction, for GDP Purposes. In the context of a downwardly revised headline monthly contraction of 2.0% (-2.0%) [previously down by 1.4% (-1.4%)] in January real, or inflation-adjusted spending, February 2015 spending declined by 0.2% (-0.2%) for the month. On a year-to-year basis, the inflation-adjusted contraction in January 2015 spending was 0.5% (-0.5%), versus a 0.1% gain in February.

Based on January and February reporting—the only months that will be available for the initial estimate of first-quarter 2015 GDP on April 29th—first-quarter 2015 real spending fell at an annualized quarterly pace of 6.4% (-6.4%), versus an annualized quarterly gain of 4.9% in fourth-quarter 2014. Presently at, or near, the recent low of the down-trending pattern of stagnation, the real construction spending series stood at 35.4% below its pre-recession high of March 2006.

These numbers are reflected in the second graph following of real or inflation-adjusted detail. The historical pattern remains one that does not support the headline, real-GDP story of a full economic recovery and post-recession expansion since 2009.

In nominal terms, before inflation adjustment, the headline monthly decline was 0.1% (-0.1%) for February. That decline in activity was not statistically meaningful, as is usual for headline monthly changes to this series. The nominal year-to-year gain of 2.1% in February spending was statistically meaningful, but, again, the gain was due almost entirely to inflation.

PPI Final Demand Construction Index (FDCI). ShadowStats uses the Final Demand Construction Index (FDCI) component of the Producer Price Index (PPI) for deflating the aggregate activity in the construction-spending series. The previously-used New Construction Index (NCI), was so far shy of reflecting construction costs as to be virtually useless. Although closely designed to match this construction-spending series, the FDCI has two problems. First, its historical data only go back to November 2009. Second, it still understates actual construction inflation. There is no perfect, publicly-available inflation measure for deflating construction. For the historical series in the accompanying graph, the numbers are deflated by the NCI through November 2009, and by the FDCI thereafter.

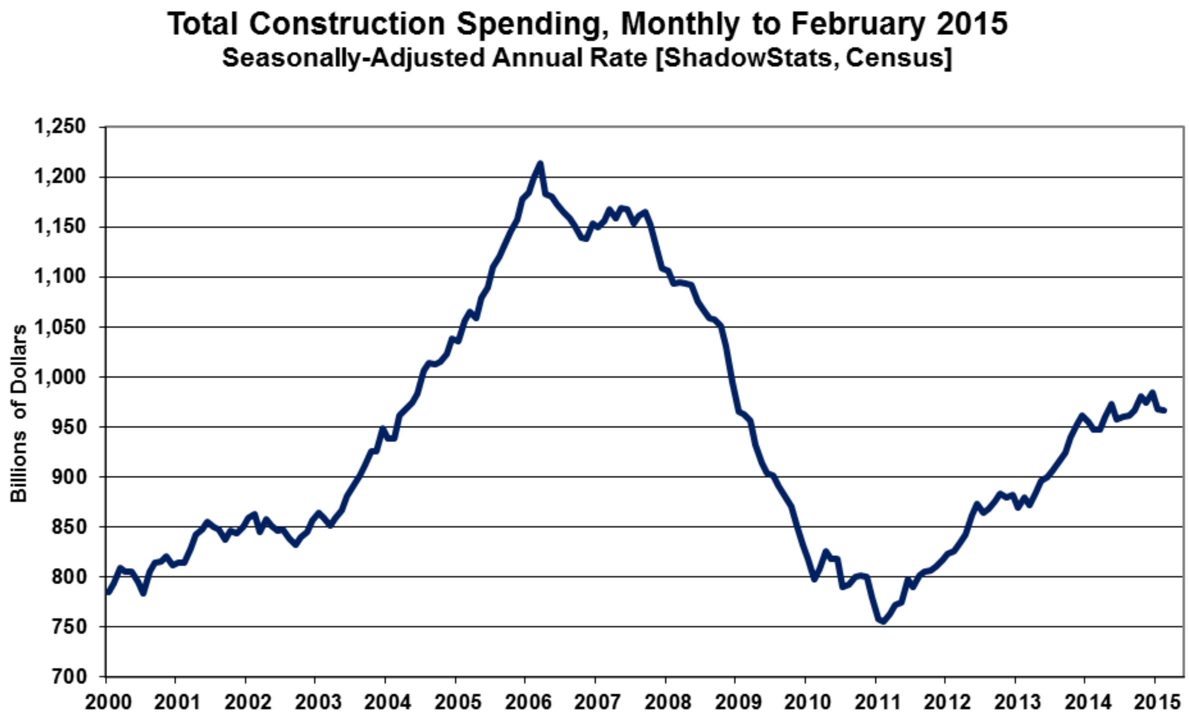
For February 2015, the seasonally-adjusted FDCI month-to-month inflation was a positive 0.09%, versus a 0.36% increase in January 2015. In terms of year-to-year inflation, the February FDCI was up by 2.00%, versus 1.91% in January 2015.

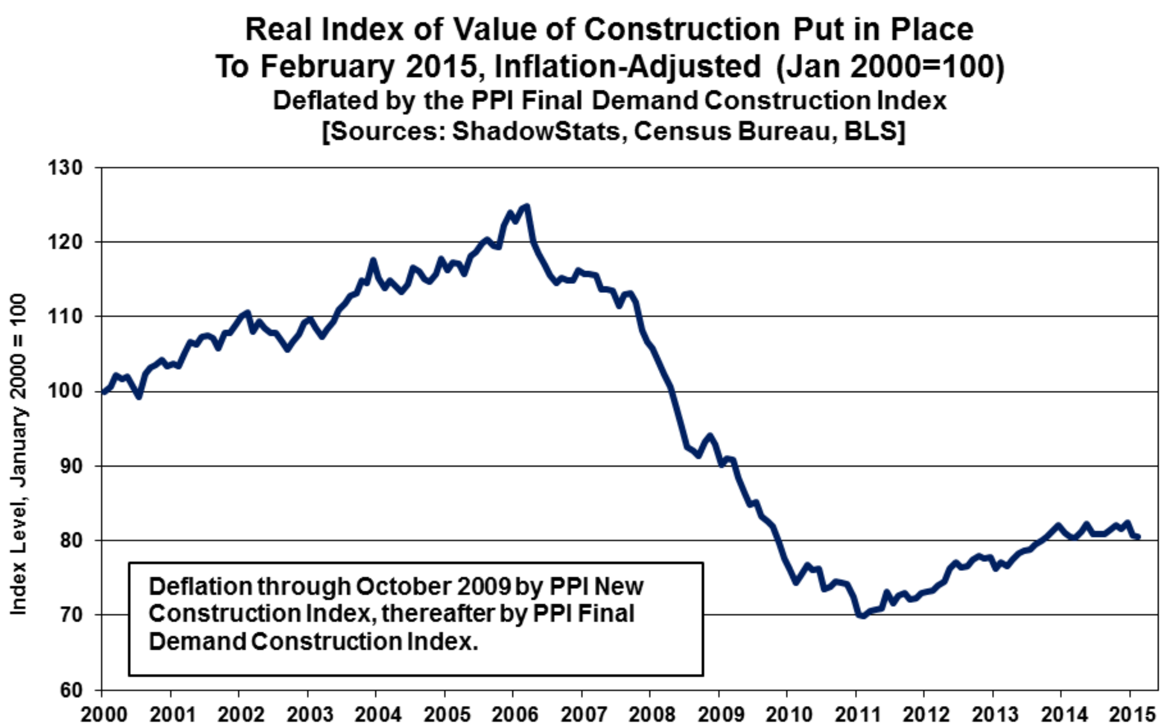
Headline Reporting for February 2015. The Census Bureau reported April 1st that the headline, total value of construction put in place in the United States for February 2015 was $967.2 billion, on a seasonally-adjusted—but not-inflation-adjusted—annual-rate basis. That estimate was down month-to-month by a statistically-insignificant 0.1% (-0.1%) +/- 1.4% (all confidence intervals are at the 95% level), versus a revised $967.9 (previously $971.4) in January 2015, which, in turn, was down by a revised 1.7% (-1.7%) [previously down by 1.1% (-1.1%)] from a revised $984.5 [previously $982.0, initially $982.1] billion in December 2014. The revised December spending was up by a revised 1.0%, versus an unrevised November spending level.

All the monthly construction-spending data, back through January 2013, will be subject to an annual benchmark revision, along with next month's statistical release on May 1st.

Adjusted for the FDCI inflation measure in the PPI, aggregate real spending in February 2015 fell by 0.2% (-0.2%), following a revised monthly decline of 2.0% (-2.0%) [previously down by 1.4% (-1.4%)] in January 2015, and up by a revised 1.0% (previously 0.8%) for the month in December 2014.

On a year-to-year or annual-growth basis, February 2015 construction spending rose by a statistically-significant 2.1% +/- 1.9%, versus a revised 1.4% [previously up by 1.8%] annual gain in January, and a revised 2.4% [initially 2.2%] gain in December 2014. Net of construction costs indicated by the FDCI, however, year-to-year change in spending was an annual gain of 0.1% in February 2015, versus a revised annual contraction in January 2015 of 0.5% (-0.5%) [previously down by 0.2% (-0.2%)], and revised annual gain of 0.3% [initial up by 0.1%] in December 2014.

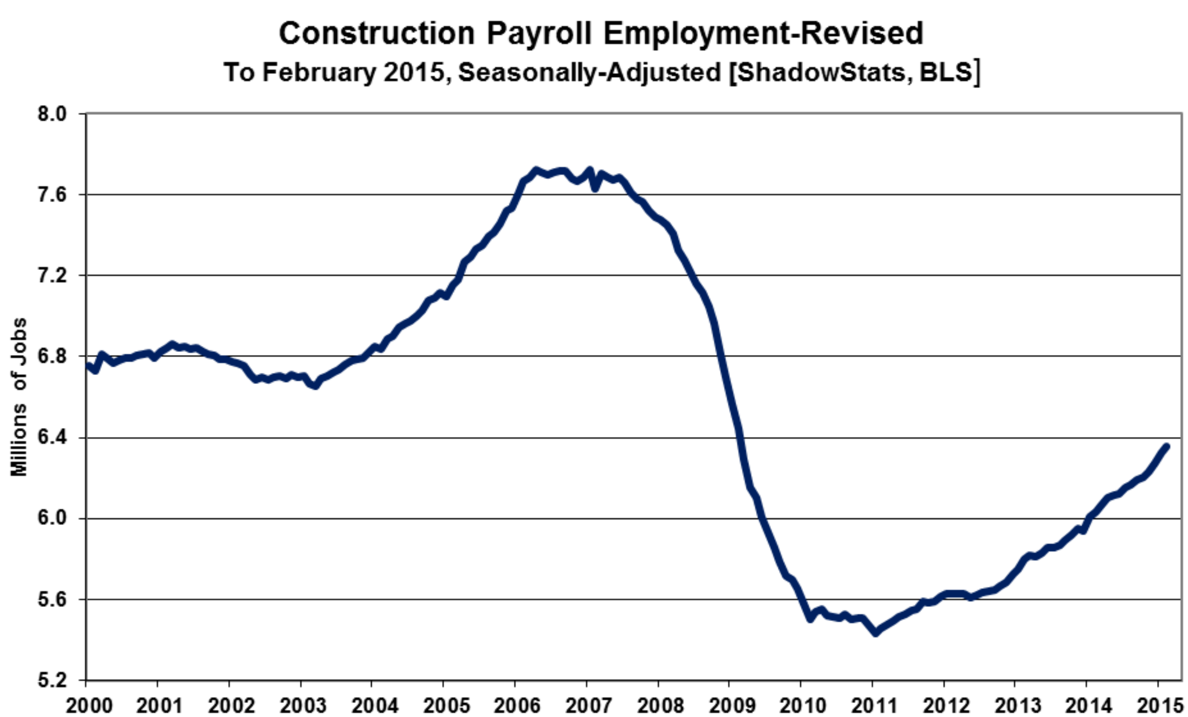

Total Construction Spending, Monthly to February 2015
Seasonally-Adjusted Annual Rate [ShadowStats, Census]
Billions of Dollars
1,250
1,200
1,150
1,100
1,050
1,000
950
900
850
800
750
700
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015


Real Index of Value of Construction Put in Place
To February 2015, Inflation-Adjusted (Jan 2000=100)
Deflated by the PPI Final Demand Construction Index
[Sources: ShadowStats, Census Bureau, BLS]
Index Level, January 2000 = 100
130
120
110
100
90
80
70
60
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015
Deflation through October 2009 by PPI New Construction Index, thereafter by PPI Final Demand Construction Index.

The statistically-insignificant, headline monthly contraction of 0.1% (-0.1%) in nominal February construction spending, versus a 1.7% (-1.7%) monthly drop in January 2015 spending, included a monthly decline of 0.8% (-0.8%) in February public spending, versus a 3.2% (-3.2%) drop in January spending. Private spending rose by 0.2% in February, but fell by 1.1% (-1.1%) in January. Within total private construction spending, the residential sector declined by 0.2% (-0.2%) in February, versus a 0.2% gain in January, while the nonresidential sector rose by 0.5% in February, having contracted in January by 2.4% (-2.4%). The following graphs show the latest extended detail.

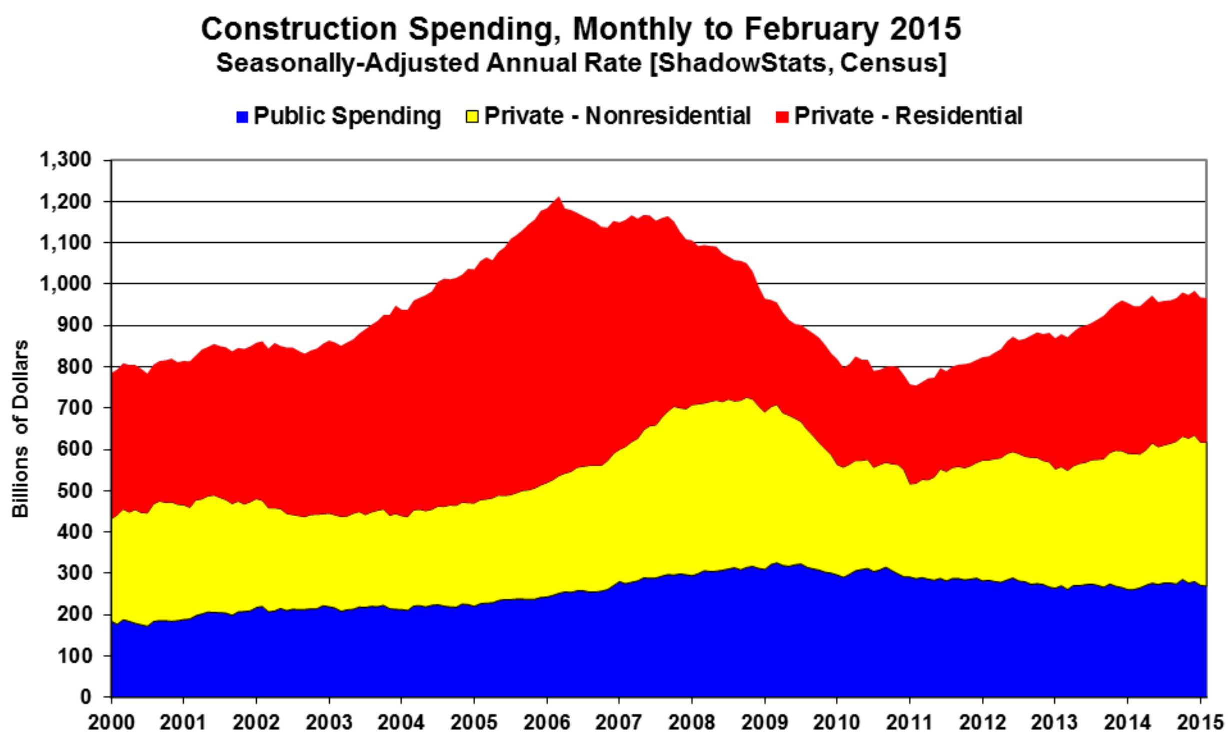
Construction and Related Graphs. The preceding two graphs reflect total construction spending through February 2015, both in the headline nominal dollar terms, and in real terms, after inflation adjustment. The inflation-adjusted graph is on an index basis, with January 2000 = 100.0. Adjusted for the PPI's NCI measure through October 2009 and the PPI's Final Demand Construction Index thereafter, real construction spending showed the economy slowing in 2006, plunging into 2011, then turning minimally higher in an environment of low-level stagnation, trending flat since late-2013, and notching lower in the most-recent headline reporting

The pattern of inflation-adjusted activity here—net of government inflation estimates—does not confirm the economic recovery indicated by the headline GDP series (see *Commentary No. 708* and *No. 692 Special Commentary: 2015 - A World Out of Balance*). To the contrary, the latest construction reporting, both before (nominal) and, more prominently, after (real) inflation adjustment, shows a pattern slightly variable stagnation, now declining, where activity never has recovered pre-recession highs.



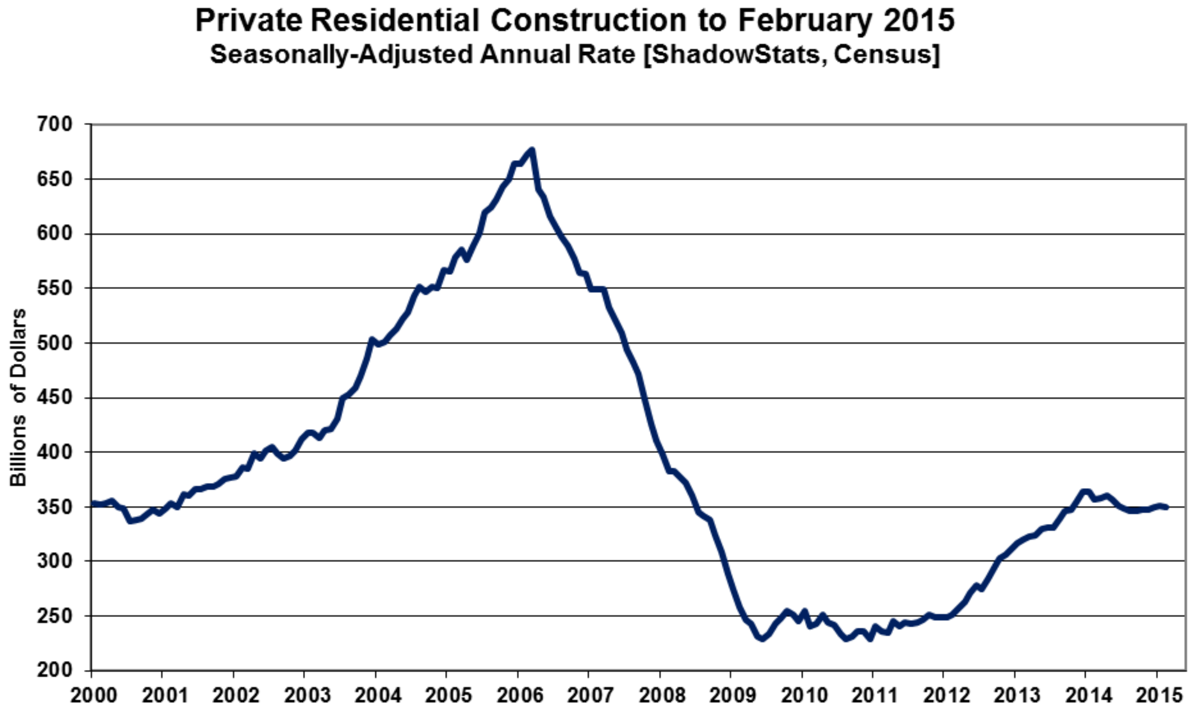
The preceding graph shows February 2015 construction employment (see *Commentary No. 702*). The construction employment numbers and the graph will be updated through March 2015 in tomorrow's April 3rd *Commentary No. 710*. In theory, payroll levels should move more closely with the inflation-adjusted aggregate series, where the nominal series reflects the impact of costs and pricing, as well as a measure of the level of physical activity.

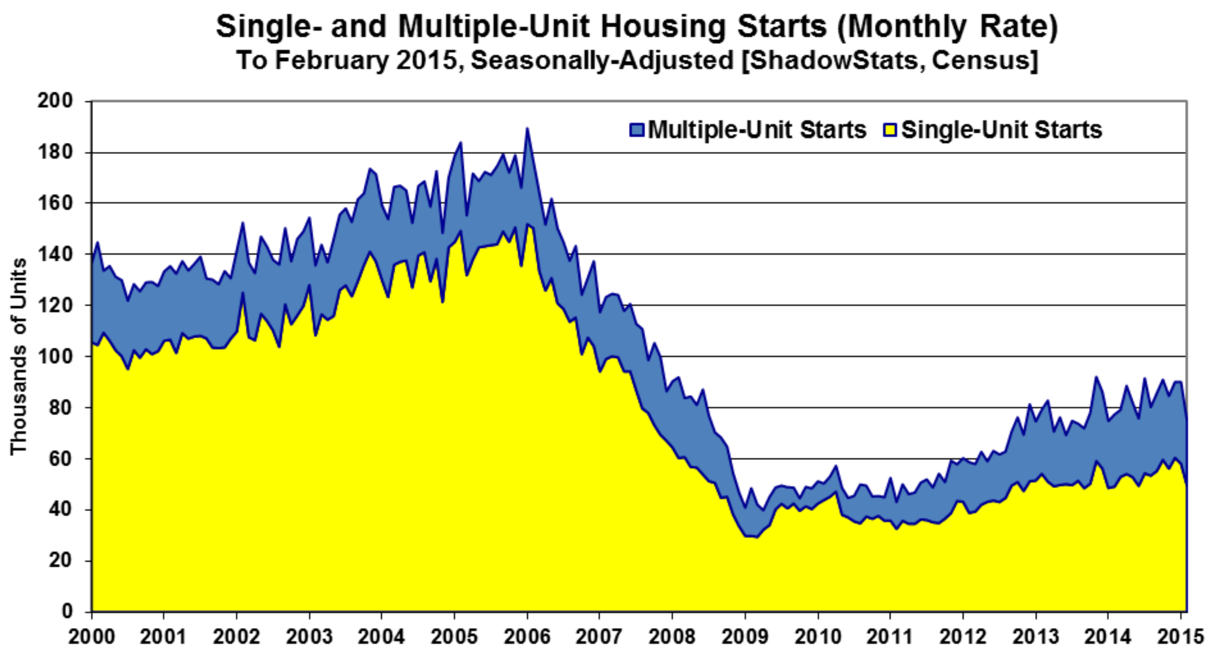
The following plot shows total nominal construction spending, broken out by the contributions from total-public (blue), private-nonresidential (yellow) and private-residential spending (red).



The next two graphs following cover private residential construction along with housing starts (combined single- and multiple-unit starts) for February 2015 (see *Commentary No. 705*). Keep in mind that the construction spending series is in nominal (not-adjusted-for-inflation) dollars, while housing starts reflect unit volume, which should tend to be more parallel with the real (inflation-adjusted) series. Where the private residential construction spending had been in recent upturn through most of 2013, it turned slightly lower in 2014, and has been basically down-trending or stagnant coming into 2015, even before adjustment for inflation.

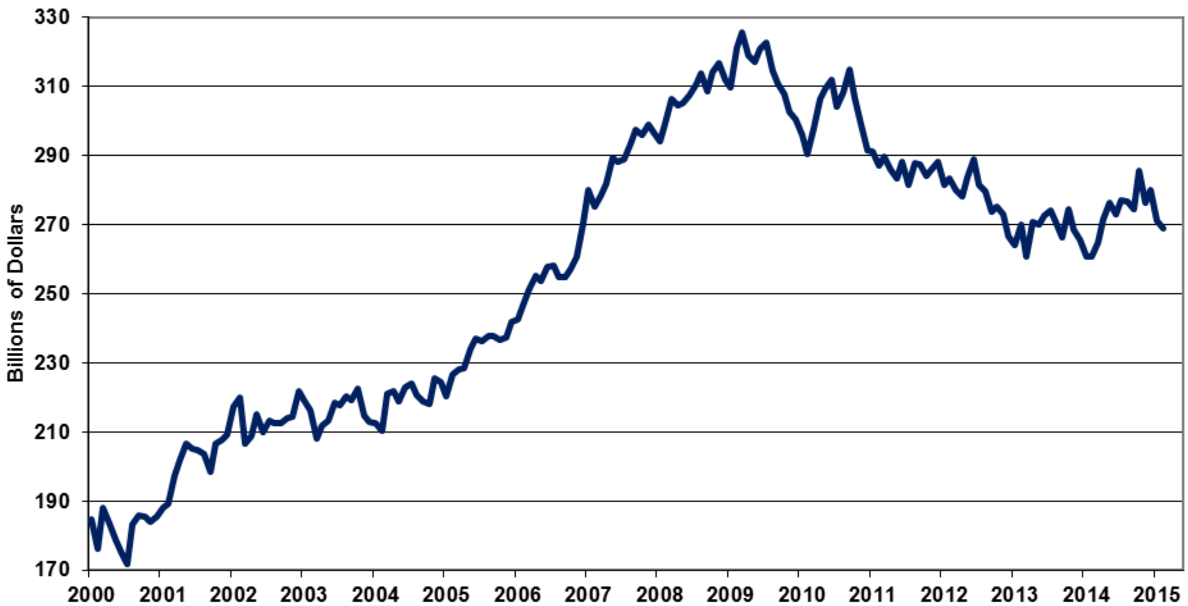
The final set of two graphs, the third and fourth, following, show the patterns of the monthly level of activity in private nonresidential construction spending and in public construction spending. The spending in private nonresidential construction remains well off its historic peak, but had bounced higher off a secondary, had near-term dip in late-2012, and then heading higher, again, with a topping pattern seen recently. Public construction spending, which is 98% nonresidential, had continued in a broad downtrend, with intermittent bouts of fluttering stagnation and some recent upturn that also appears to be topping out.





Nonresidential Construction, Monthly to February 2015
Seasonally-Adjusted Annual Rate [ShadowStats, Census]

Public Construction, Monthly to February 2015
Seasonally-Adjusted Annual Rate [ShadowStats, Census]



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 have been, and still remain overly optimistic in the extreme. They still exceed any potential, underlying economic reality, even though downside corrective revisions and an accelerating pace of downturn in broad-based, monthly headline economic reporting already have begun to hammer those expectations. Recent GDP excesses will not face downside revisions now until the July 30, 2015 GDP benchmark revision.

Headline consumer inflation—recently driven lower by collapsing prices for gasoline and other oil-price related commodities—likely hit its near-term low in January 2015, moving minimally off bottom in February. 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:

***Updated for Consensus*—Employment and Unemployment (March 2015).** The Bureau of Labor Statistics (BLS) will release its March 2015 labor data tomorrow, Friday, April 3rd. Both employment and unemployment are due for negative, headline surprises, given the general tone of the reporting of most other regular economic series. Established monthly distortions to payroll employment (excessive upside biases, and publishing irregularities with the concurrent-seasonal-factor process) continue, however, as do the regular monthly distortions to headline unemployment (definitional issues with "discouraged workers," and publishing irregularities with the concurrent-seasonal-factor process).

Early market expectations appear to be for a pullback in monthly payroll growth from February's initial headline jobs gain of 295,000 and for no change in the headline U.3 February unemployment rate of 5.5%, with Bloomberg showing a 5.5% consensus.

As with the narrowing of the headline unemployment rate in February, any further narrowing of the headline March U.3 unemployment rate likely would encompass more employed being redefined off the unemployment rolls and out of the headline labor force, rather than gaining new employment. Underlying economic fundamentals continue to suggest deterioration in the broader unemployment rates such as U.6 and the ShadowStats Alternate Unemployment measure, as well as slowing or negative month-to-month growth in headline payrolls.

Monthly Payroll Bias Is Weaker than Early Expectations. As published previously by ShadowStats-affiliate www.ExpliStats.com, in its analysis of the biases built into the concurrent-seasonal-factor modeling of the headline February 2015 payroll employment, the implied built-in-bias trend for March 2015 is for a headline jobs gain of 243,000 (see *Commentary No. 702*). Late expectations appear to be closing in on that trend, with Bloomberg showing a consensus 247,000 headline jobs gain.

To the extent that underlying fundamentals eventually will shine through all the regular monthly volatility and distortions, headline activity increasingly should much favor much weaker-than-expected payroll gains, and higher-than-expected unemployment rates.