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

COMMENTARY NUMBER 715
First-Quarter GDP, Velocity of Money

April 29, 2015

Initial 0.2% First-Quarter 2015 Real GDP Growth Is on Track for a Quarterly Contraction in First Revision

Games-Playing: Was Initial Real GDP Estimate Set at 0.2%, So Nominal GDP Would Not Fall Below 0.1%?

Real Final Sales (GDP Less Purported Inventory Build-Up) Fell at Annualized Quarterly Pace of 0.5%

Velocity of Money Slowed in First-Quarter 2015

PLEASE NOTE: The next regular Commentary, *scheduled for Tuesday, May 5th, will cover March construction spending, the trade deficit and annual revisions to retail sales, followed by a* Commentary *on May 8th, covering the April employment and unemployment numbers.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

First-Quarter GDP Clearly Contracted, but the BEA Did Not Want to Show Such in Its Initial Estimate. Discussed in *Commentary No. 714*, much like last year's initial estimate of first-quarter 2014 GDP growth, which came in at the lowest possible positive reading of 0.1%, the Bureau of Economic Analysis (BEA) appeared to send a signal, today, to consensus forecasters [Bloomberg late-consensus was 1.0%]. The minimal, reported headline quarterly growth of 0.2% likely meant that real first-quarter 2015 GDP actually contracted, and that downside revisions will follow. If the consensus had been close to or below the BEA internal assessment of first-quarter growth, the BEA would have brought in the headline growth at or above the consensus.

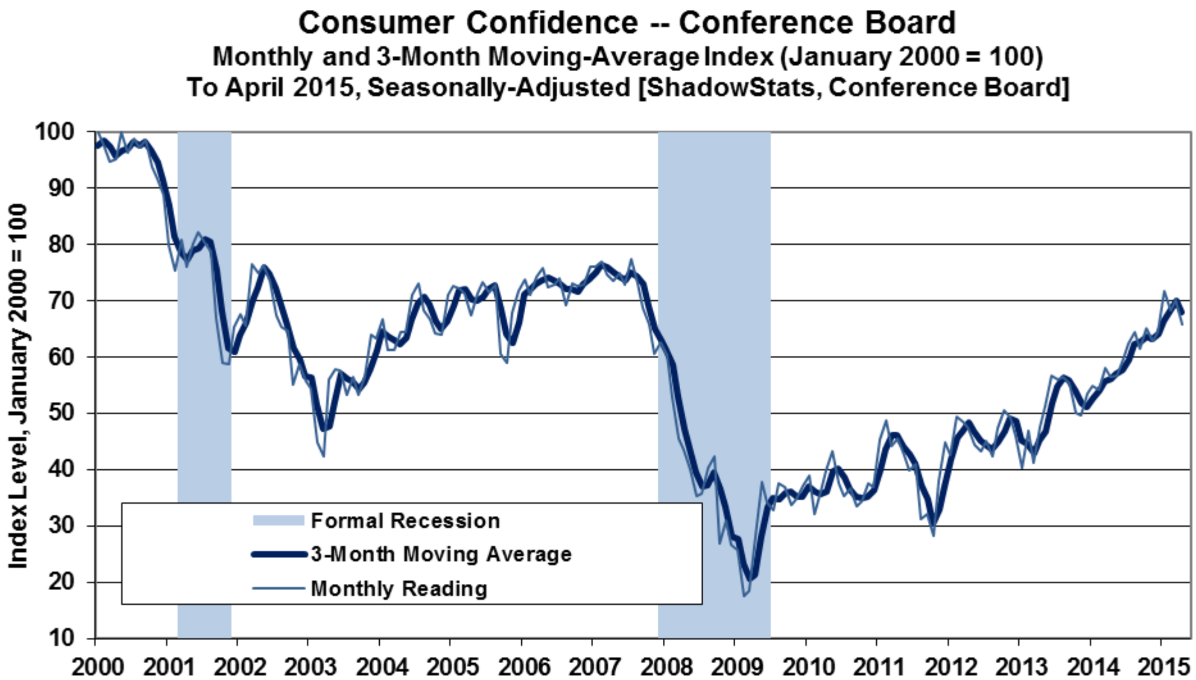
Noted in last year's *Commentary No. 623* of April 30, 2014 [see follow up also in *Commentary No. 631*, where initial first-quarter 2014 growth of 0.1% revised to a contraction of 1.0% (-1.0%) in the first revision, and later to a contraction of 2.1% (-2.1%), after subsequent revisions and benchmarking]:

> The Bureau of Economic Analysis (BEA) has tremendous leeway in the level of growth that it reports in its first or "advance" estimate of headline GDP growth in a given quarter. Usually, the BEA attempts to target the initial headline growth estimate to consensus expectations, moving the internal BEA estimate towards the consensus number. Where the consensus appears to have been about 1.0% coming into this morning's (April 30th) report, and where the BEA gave a 0.1% headline growth estimate—the lowest positive growth rate possible—the message was negative as to what the BEA was seeing in reality. The internal BEA estimate probably was for a quarterly contraction, and the message from the BEA to consensus forecasters likely was that the numbers were worse than they appeared, and that downside revisions are pending.

The pattern seen last year likely will be followed, with a May 29, 2015 first revision to today's headline number into negative territory, although ultimately with a deeper contraction than was seen in first-quarter 2014. Separately, unlike the 2014 experience of a rebounding second quarter, the eventual, headline first-quarter 2015 contraction should be followed by a further quarterly contraction in second-quarter 2015. Such should be signaled increasingly in the headline economic detail of the next month or so, rapidly shifting market perceptions towards the onset of a formal economic recession.

Given Inflation Issues, Headline 0.2% Real Growth Was the Lowest Positive Number the BEA Could Report. With a headline implicit price deflator showing a negative 0.1% (-0.1%) annualized inflation rate in first-quarter 2015, reporting headline real (inflation-adjusted) GDP growth of 0.1% would have left nominal (not-adjusted-for inflation) growth at unchanged. Avoiding negative or unchanged GDP growth headlines, the BEA likely applied its "minimal" positive-growth guidance to the nominal number as well, which pushed the minimal real growth up by 0.1% to a headline 0.2%.

Net of Gimmicks and Distortions, Today's Headline Reporting Was Negative. Reviewed in the *Distribution of Headline Growth* section, net of factors ranging from weather-induced utility usage, to games with the economic impact of the Affordable Care Act (ACA) and with guesses at inventory build-up, headline GDP likely would have shown an annualized real contraction of about 2.0% (-2.0%) in the initial headline reporting. Final sales (GDP net of the inventory build-up) showed a headline quarterly contraction of 0.5% (-0.5%).



Updating Consumer Liquidity Conditions—April 2015 Consumer Confidence Plunged. Fully discussed and detailed in *Commentary No. 711*, and updated in prior *Commentary No. 714* for the sharp monthly drop in March 2015 real median household income, without real growth in household income and the ability or willingness to take on meaningful new debt, the consumer simply has not had the wherewithal to fuel sustainable economic growth.

Impaired consumer liquidity and its direct constraints on consumption have dominated the last eight-plus years of economic turmoil, driving the housing-market collapse and ongoing stagnation in consumer-related real estate and construction activity, as well as constraining retail sales activity and the related, personal-consumption-expenditures category of the GDP. Those sectors account for more than 70% of aggregate U.S. GDP activity, and the hard numbers in those sectors were hit heavily in the headline reporting of first-quarter 2015 GDP.

Updating the detail in *Commentary No. 711*, the preceding graph reflects the just-released April 2015 reading on the Conference Board's consumer confidence measure, which pulled back sharply.

The consumer confidence and the consumer sentiment (University of Michigan) series tend to mimic the tone of headline economic reporting in the press, and often are highly volatile month-to-month, as a result. Accordingly, a negative toll from recent reporting on weakening headline economic data likely was a drag on the April confidence measure and likely also will dampen the April sentiment reading.

Smoothed for the irregular, short-term volatility, the confidence series still remains at levels seen typically in recessions. Shown in *No. 711*, as plotted for the last 40 years, the latest readings of confidence have not recovered levels that preceded any of the formal recessions, and generally remain well below, or are inconsistent with, periods of historically-strong economic growth that would rival the recent booming GDP gains of mid-2014.

Today's Missive (April 29th). The balance of today's *Commentary* concentrates on the reporting detail from the initial estimate of first-quarter 2015 GDP activity.

Also reflecting the "advance" estimate of first-quarter 2015 GDP, the velocity of various money supply measures—the effective pace of annual turnover of the money supply in the economy—has been updated in the *Hyperinflation Watch* section. The *Hyperinflation Outlook Summary* has not been revised from *No. 711*. Separately, the *Week Ahead* section previews next week's reporting on March construction spending and the trade deficit, along with the reporting of April employment and unemployment.

Gross Domestic Product (GDP)—First-Quarter 2014, First Estimate—Quarterly Contraction Is Likely in Revision. The first or "advance" estimate of first-quarter 2015 GDP reflected statistically-insignificant, real (inflation-adjusted), annualized, quarterly headline growth of 0.2% (0.25% at the second decimal point, rounds to 0.2%). Discussed in the opening paragraphs, that was the lowest positive real growth rate that the BEA could have used and likely signaled a pending downside revision.

Such followed headline annualized real growth of 2.22% in fourth-quarter 2014, 4.97% real growth in third-quarter 2014, 4.59% real growth in second-quarter 2014, and a real annualized contraction of 2.11% (-2.11%) in first-quarter 2014. All the 2014 numbers probably will face significant downside revisions in the annual benchmarking of July 30, 2015.

Plotted in the graphs of the *Reporting Detail* section, headline year-to-year growth in first-quarter 2015 was 2.99%, versus 2.38% in fourth-quarter 2014, 2.70% in third-quarter 2014, 2.59% annual growth in the second-quarter 2014, and 1.89% in the first-quarter 2014. That headline annual growth number for the first-quarter 2015 also should revise sharply lower, in tandem with the headline quarterly number.

Implicit Price Deflator (IPD). As general guidance, the weaker the inflation rate used in deflating an economic series, the stronger will be the resulting inflation-adjusted growth. The first estimate of first-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was an annualized quarterly contraction of 0.10% (-0.10%), versus an annualized gain of 0.16% in fourth-quarter 2014, 1.38% in third-quarter 2014, 2.15% in second-quarter 2014, and 1.33% in first-quarter 2014.

Year-to-year, first-quarter 2015 IPD inflation was 0.89%, versus 1.25% in fourth-quarter 2014, 1.57% in third-quarter 2014, 1.64% in second-quarter 2014, 1.37% in first-quarter 2014.

For comparison, headline CPI-U inflation (Bureau of Labor Statistics), seasonally-adjusted, annualized quarter-to-quarter showed an annualized contraction of 3.01% (-3.01%) in first-quarter 2015, versus a contraction of 0.85% (-0.85%) in fourth-quarter 2014, and annualized gains of 1.18% in third-quarter 2014, 2.44% in second-quarter 2014, and 2.09% in first-quarter 2014.

Unadjusted, year-to-year quarterly inflation was a contraction of 0.10% in first-quarter 2015, versus gains of 1.25% in fourth-quarter 2014, 1.78% in third-quarter 2014, 2.05% in second-quarter 2014, and 1.41% in first-quarter 2014.

Distribution of Headline First-Quarter GDP Growth. Despite the severely-limited significance of the following detail, it is included for those interested in the reported internal patterns of GDP growth, as guessed at by the BEA. The first estimate of annualized quarterly growth in first-quarter 2015 was 0.25% (rounds to 0.2%), following 2.22% growth in fourth-quarter 2014.

The BEA's first guess at the real first-quarter growth rate is detailed in the following aggregation of contributed growth. Please note that the annualized growth number in each sub-category is the additive contribution to the aggregate, headline change in GDP, where 1.31% + 0.34% - 1.25% - 0.15% = 0.25%. When all the subsequent monthly and the July 30th benchmark revisions are in place, headline first-quarter 2015 GDP quarter-to-quarter growth, again, should be solidly in negative territory.

- ***Consumer Spending Contributed 1.31% to First-Quarter Growth; Contributed 2.98% to Fourth-Quarter.*** The relatively hard detail on personal consumption of goods showed flat growth for the quarter. The positive growth came from the services sector, specifically in increased utility usage tied to unseasonably-bad weather (contributed 0.59% of the GDP growth), and the ongoing questionable economic growth purportedly being generated by the ACA (contributed well in excess of 0.62% of the GDP growth).

- ***Business/Residential Investment Contributed 0.34% to First-Quarter Growth; Contributed 0.61% to Third-Quarter.*** Except for the usual initial growth fudge-factor of inventory building, which contributed 0.74% of the GDP growth rate, the balance of business investment subtracted 0.40% (-0.40%) from the aggregate GDP growth rate. Final sales (GDP minus inventory change) contracted at an annualized pace of 0.49% (-0.49%) having risen by 2.32% in fourth-quarter 2014.

- ***Net Exports Subtracted 1.25% (-1.25%) from First-Quarter Growth; Subtracted 1.03% (-1.03%) from Fourth-Quarter.*** Reflecting the faltering trade deficit discussed in *Commentary No. 709*, deteriorating net exports subtracted 1.25% (-1.25%) from the aggregate quarterly GDP growth rate. Revisions here largely will be set by the March 2015 trade-deficit reporting of next week (see the *Week Ahead* section).

- ***Government Spending Subtracted 0.15% (-0.15%); Subtracted 0.35% (-0.35%) from Third-Quarter.*** Where federal government consumption knocked 0.53% off the prior quarter's growth rate, such turned neutral in the current quarter. What had been a 0.18% positive contribution to the fourth-quarter growth rate from state and local spending, turned to a net-negative contribution of 0.17% in the latest reporting.

Economic Reality. With the initial, official estimate of first-quarter 2015 GDP growth at 0.2%, versus 2.2% headline growth in fourth-quarter 2014, the general outlook as to underlying economic reality has not changed. Discussed briefly, earlier in these *Opening Comments*, and recently in *Commentary No. 714* and *No. 692 Special Commentary: 2015 - A World Out of Balance*, the broad economy is turning down anew, and that likely will be reflected in back-to-back headline contractions of first- and second-quarter 2015 GDP reporting. Obviously, that includes a pending downside revision to the initial growth estimate for the first-quarter 2015. A wide variety of monthly economic detail already suggests that, and new headline numbers should continue to confirm those patterns in reporting of the next several months.

In advance of the annual GDP overhaul on July 30th, major benchmark revisions are due in the next couple of months for key series such as retail sales (tomorrow), industrial production and new orders for durable goods. The historical revisions should be massively negative in these government-shutdown-delayed, catch-up reportings. Related, serious downside revisions to recent and current GDP reporting also are likely with the annual GDP benchmark revisions. With the ShadowStats broad outlook unchanged, the gist of much of the following text remains along the lines of other recent GDP *Commentaries*, but the details and numbers are updated for the latest reporting.

Discussed frequently, the GDP does not reflect properly or accurately the changes to the underlying fundamentals that drive the economy. Underlying real-world economic activity shows that the broad economy began to turn down in 2006 and 2007, plunged into 2009, entered a protracted period of stagnation thereafter—never recovering—and then began to turn down anew in recent quarters. Irrespective of the reporting gimmicks introduced in the July 2013 and July 2014 GDP benchmark revisions, including a recent pattern of inclusion and estimation of highly-questionable data on the Affordable Care Act (ACA), a consistent, fundamental pattern of faltering historical activity is shown in the accompanying sets of "corrected" GDP graphs.

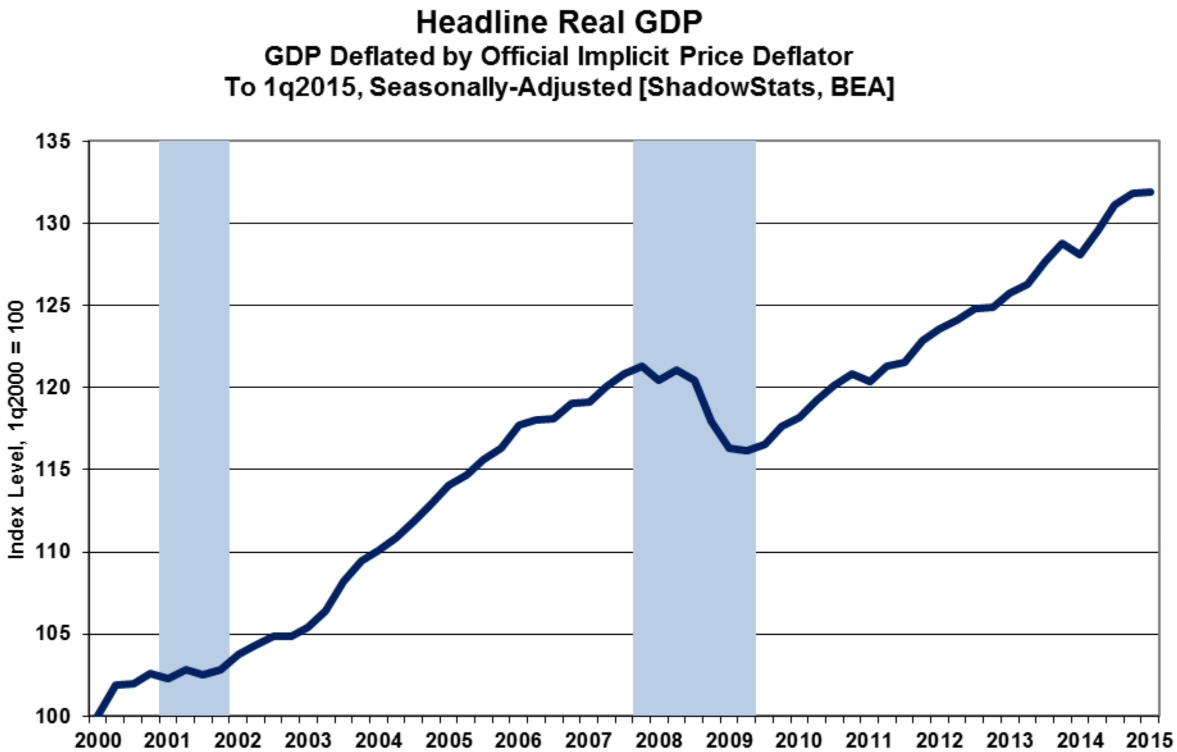
Please note that the pattern of activity shown for the "corrected" GDP series is much closer to the patterns shown in the graphs of employment (see *Commentary No. 710*), monthly real median household income and other consumer measures (see earlier *Consumer Conditions* section). This has been detailed most recently in *Commentary No. 711* and in *No. 692 Special Commentary: 2015 - A World Out of Balance*. Similar patterns are found in recent indications of annual consumer expenditures (see *Commentary No. 656* and *Commentary No. 673*) and economic series not otherwise reliant on understated inflation for their reported growth, such as housing starts (see *Commentary No. 713* and *2014 Hyperinflation Report—Great Economic Tumble – Second Installment*).

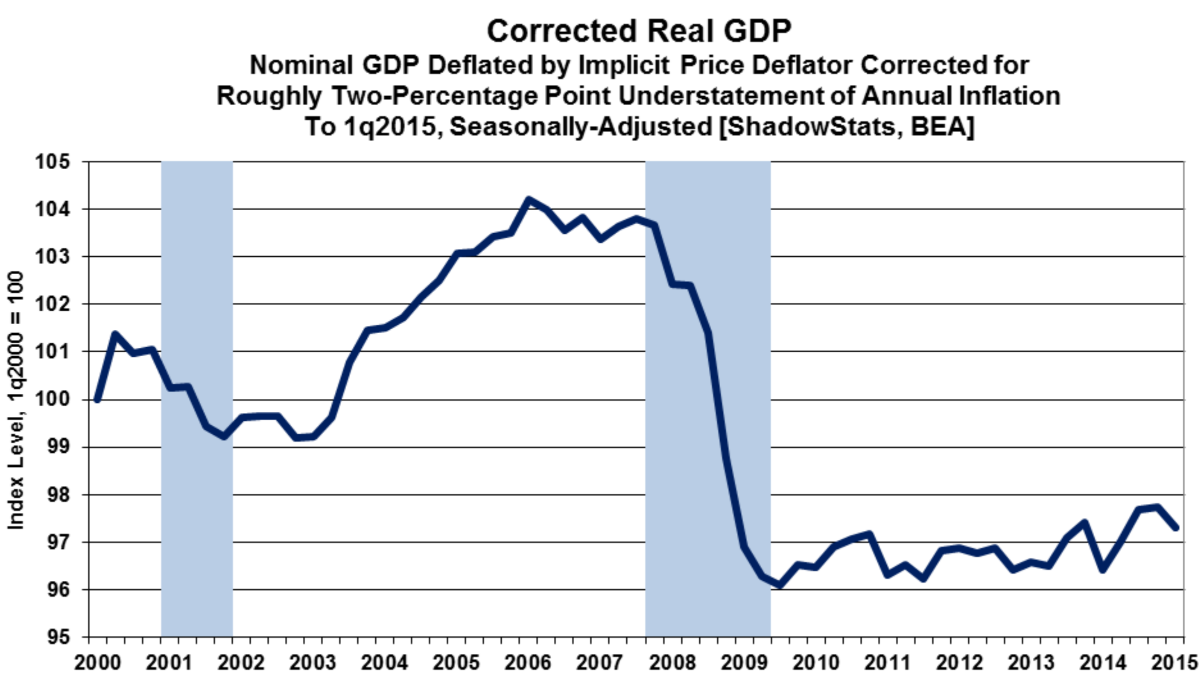
With liquidity-strapped consumers unable to fuel sustainable growth in consumption, a full business recovery could not have taken place since 2009, and a recovery will not be forthcoming until consumer structural income and liquidity problems are resolved.

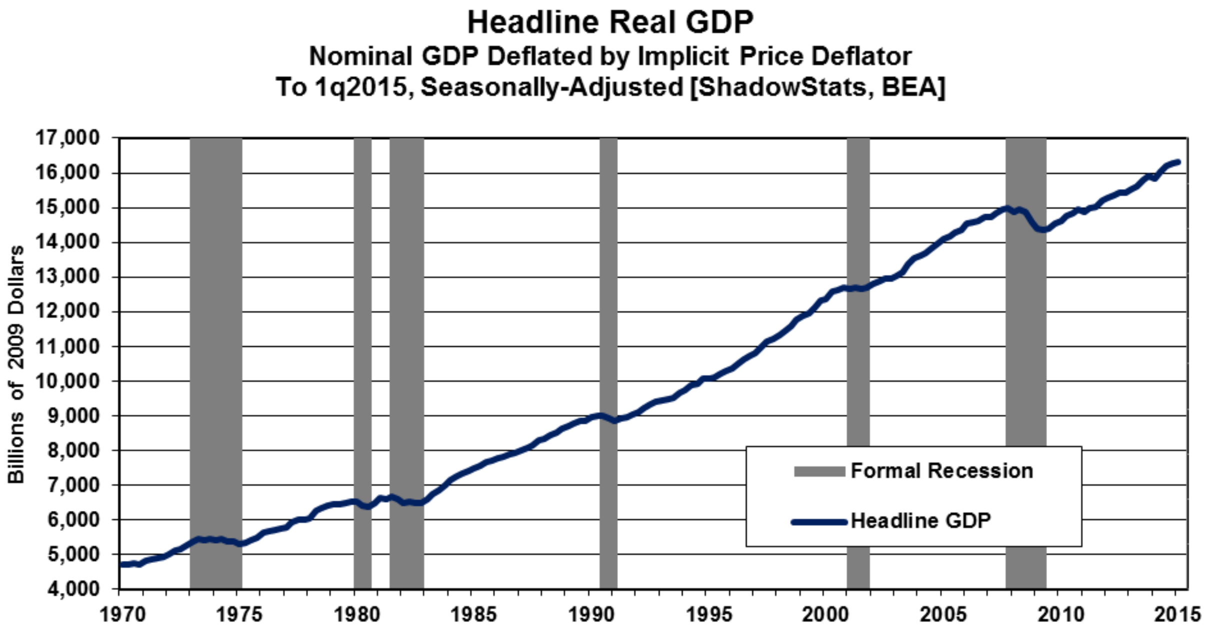
Official and Corrected GDP. As usually discussed in these *Commentaries* covering the quarterly GDP reporting and monthly updates, the full economic recovery indicated by the official, real GDP numbers remains an illusion. It is a statistical illusion created by using too-low a rate of inflation in deflating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

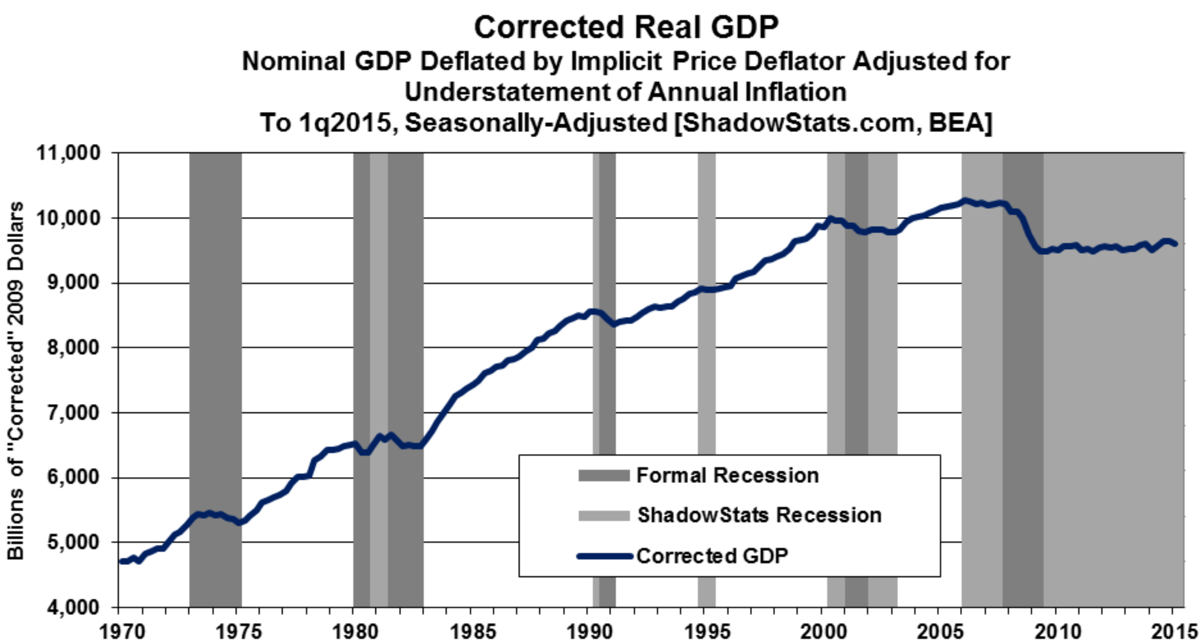
The first set of graphs (2000-to-date) is the one traditionally that has been incorporated in the GDP *Commentaries*, and is expressed on an index base where first-quarter 2000 = 100.0. The second set updates the longer-term graphs (1970-to-date), expressed in billions of 2009 dollars as used in headline GDP reporting, and as published initially in the second installment of the *Hyperinflation Report* and updated in *No. 692 Special Commentary* (both linked above). The graphs also show official periods of recession as shaded areas (the ShadowStats-defined recessions are indicated by the lighter shading in the second graph of the second set).

Shown in the first graph of official *Headline Real GDP*, GDP activity has been reported above pre-2007 recession levels—in full recovery—since second-quarter 2011, and headline GDP has shown sustained growth since (a growth interruption for first-quarter 2014 excepted). Adjusted for official GDP inflation (the implicit price deflator), the initial level of headline first-quarter 2015 GDP currently stands 8.8% above its pre-recession peak-GDP estimate of fourth-quarter 2007. In contrast, the "corrected" GDP version, in the second graph, shows first-quarter 2015 GDP activity at 6.6% (-6.6%) below its pre-recession peak of first-quarter 2006.









Further, discussed in the second installment of the *Hyperinflation Report*, and again in *No. 692 Special Commentary*, no other major economic series has shown a parallel pattern of official full economic recovery and meaningful expansion thereafter, consistent with the GDP reporting. Such is covered in discussions on the industrial production, real retail sales and real durable goods orders series in *Commentary No. 712*, *Commentary No. 713* and *Commentary No. 714*. Either the GDP reporting is wrong, or all other major economic series are wrong. While the GDP is heavily modeled, imputed, theorized and gimmicked, it also encompasses reporting from those various major economic series and private surveys, which still attempt to measure real-world activity. Flaws in the GDP inflation methodologies and simplifying reporting assumptions have created the "recovery."

The second graph in each series plots the *Corrected Real GDP*, corrected for the understatement inherent in official inflation estimates (see *Public Commentary on Inflation Measurement*), with the deflation by the implicit price deflator (IPD) adjusted for understatement of roughly two-percentage points of annual inflation in recent years. The inflation understatement has resulted from hedonic-quality adjustments, as discussed in the *Hyperinflation Reports*.

[Further detail on the first-quarter GDP estimate is found in the **Reporting Detail** ***section.]***

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HYPERINFLATION WATCH

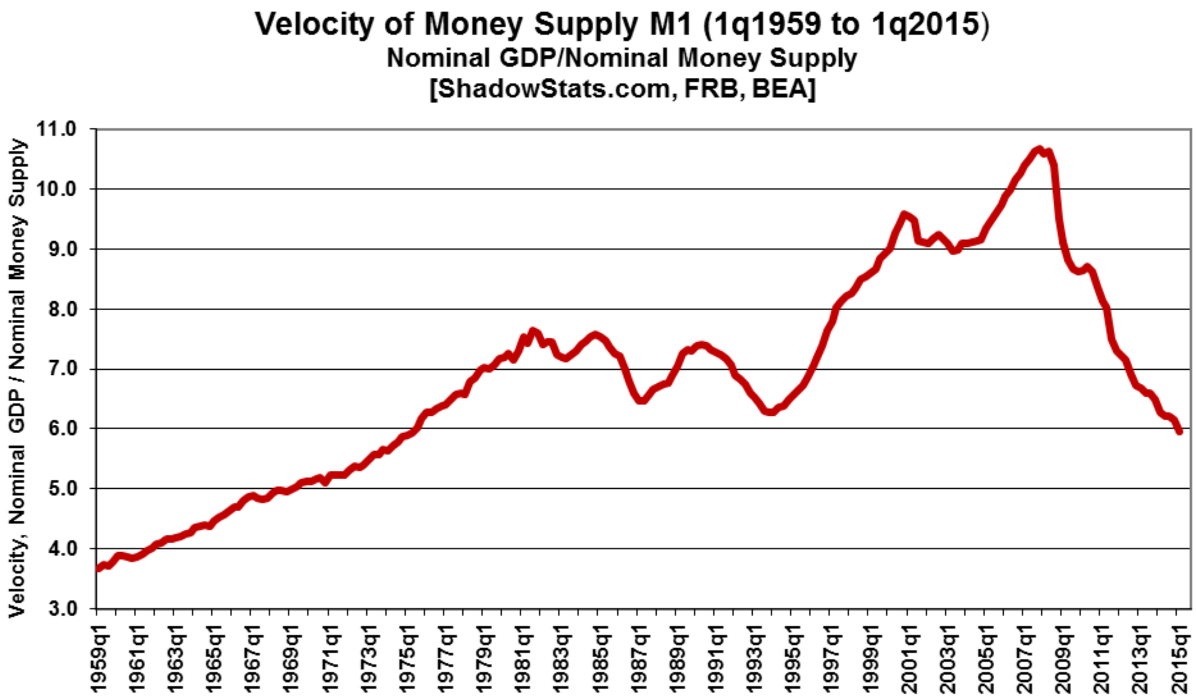
MONEY SUPPLY VELOCITY

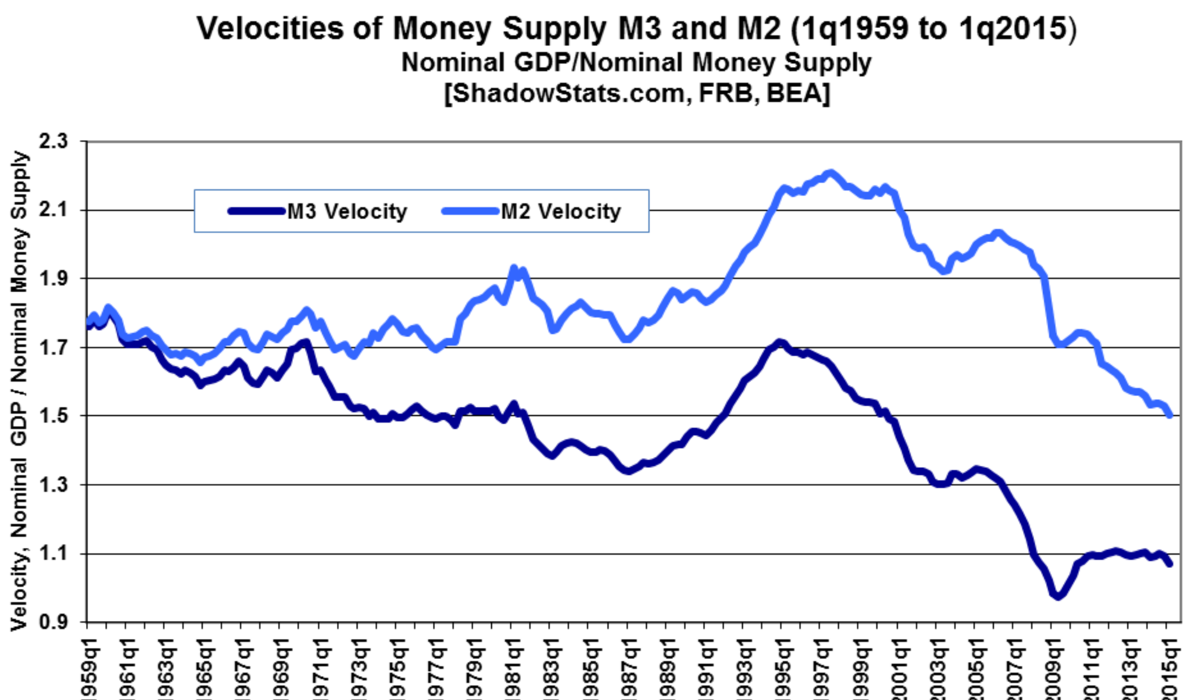
Money Supply Velocity Slowed in First-Quarter 2015. Incorporating the initial new nominal data on first-quarter 2015 GDP, as well as continued and regular Federal Reserve benchmark revisions to money supply-related data, graphed below are updated estimates for the velocity of money, broken out for money supply M1, M2 and M3 (ShadowStats Ongoing-M3 Measure).

Velocity generally slowed in first-quarter 2015 for each money-supply measure, as shown in the accompanying graphs, having plunged into 2014 for M1 and M2. Since the end of 2010, M3 velocity had been steady through third-quarter 2014. Where velocity simply is the ratio of the nominal GDP to the nominal money supply, the recent declines in the ratios generally have reflected somewhat stronger money growth than GDP growth.

As to M1, consider that perhaps 70% or more of the cash-in-circulation component of that measure (with cash accounting for about 43% of M1) could be physically outside the United States, per the Federal Reserve. Where that has been an increasing trend, a true measure of domestic M1 velocity well could be showing a significant uptrend. In like manner, where M1 includes cash, M2 includes M1, and M3 includes M2, M2 and M3 velocities also would be somewhat higher (cash is 11% of M2, 8% of M3).

M3 versus M1 and M2 had been showing opposite patterns since 2011, because growth in M3 had been weaker than growth in M1 and M2. The reason behind that difference was that much of the relatively stronger M1 and M2 growth reflected cash moving out of M3 categories—such as large time deposits and institutional money funds—into M2 or M1 accounts. The clarity of what happened there is why ShadowStats still tracks what had been the broadest money measure (M3) available.





Subscribers often ask for specifics on the velocity of the money supply, with the result that this section has become a standard feature for *Commentaries* covering the first GDP reporting of a given quarter. The nature of velocity is discussed in some detail in the 2008 *Money Supply Special Report*. Velocity simply is the number of times the money supply turns over in the economy in a given year, or the ratio in nominal terms (not adjusted for inflation) of GDP to the money supply. It is a residual number, not otherwise open to calculation or independent surveying.

Velocity has theoretical significance. In combination with money-supply growth, it should be a driving force behind inflation. Yet, since velocity is a ratio of two not-particularly-well or realistically-measured numbers, its actual estimate is of limited value. As an inflation predictor, it has to be viewed in the context of accompanying money-supply growth, and vice versa, generally as a coincident indicator. Again, full definitions can be found in the *Money Supply Special Report*.

HYPERINFLATION OUTLOOK SUMMARY

General Outlook Is Unchanged; Intensifying Economic Weakness Has Begun to Impact Market Perceptions of Fed Policy and U.S. Dollar Strength. The *Hyperinflation Outlook Summary* has not been revised from *Commentary No. 711*, other than for updated internal links or references.

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.

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 *Opening Comments* and *Commentary No. 711*). Consistent with the above referenced *Special Commentaries*, the unfolding, weakening domestic-economic circumstance, in confluence with other fundamental issues, has begun to raise doubts in the markets as to the sustainability of the purported U.S. economic recovery, and as to the imminence of meaningful monetary tightening by the U.S. Federal Reserve. As result, the U.S. dollar has backed off its recent highs, with some related upside pressure having been seen on oil prices.

Domestic economic data should continue to falter, increasingly moving market expectations towards an imminent new recession, not only further pummeling expectations for a significant tightening in Fed policy, but also renewing expectations for a more-accommodative Fed. While such may help to fuel further stock-market mania, any resulting rallies in equity prices likely will be more than offset in real terms, by percentage declines in the exchange-rate value of the U.S. dollar or in the eventual increases in headline consumer inflation.

Faltering expectations on more-conservative Federal Reserve policies and on the direction of domestic economic activity, should place mounting and eventually massive selling pressure on the U.S. dollar, as well as potentially resurrect elements of the Panic of 2008. Physical gold and silver, and holding assets outside the U.S. dollar, remain the ultimate primary hedges against an eventual total loss of U.S. dollar purchasing power. Initially, these circumstances should unwind the sharp and generally ongoing rally in the U.S. dollar's exchange rate since mid-2014, and broadly related selling pressures seen in the gold and silver markets.

A crash back to recognition of more-realistic domestic-economic circumstances appears to have begun, 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. Further, a sharp deterioration in the near-term outlook for domestic and global political stability continues and is of meaningful near-term risk for providing further fuel to 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, payroll employment and increasingly the headline GDP.

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 nine months, pushing the dollar once again to historic lows. Again, 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. 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, purportedly 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 increasingly is finding 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.

Unexpected economic weakness—a renewed downturn—also savages prospective federal budget deficit prognostications (particularly the 10-year versions). It also throws off estimates of U.S. Treasury funding needs and estimates as to how long the Treasury effectively can dodge the limits of the recently re-imposed debt ceiling. Current fiscal "good news" remains from cash-based, not GAAP-based and accounting projections and is heavily impacted by changes in business activity.

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 significant, renewed market speculation as to an added round of Federal Reserve quantitative easing, QE4, may 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 thought 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.

Again, 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.

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 appears to have begun to reverse.

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 may have started with the shift in Swiss National Bank policy early in the year, but it has become dominated by increasingly-negative global perceptions of stability in U.S. economic activity and Federal Reserve monetary 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. 711*). Sharply-negative economic reporting shocks, versus softening consensus forecasts, still 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 did not alter the systemic unwillingness to address 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 many in Washington look to continue increasing 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*). This circumstance now is operating in the context of the formal constraint of a renewed debt ceiling.

- ***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 versus Russia and extraordinarily-volatile circumstances in the Middle East. U.S. response to Russian activity in the Ukrainian situation likely was 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. These situations have yet to run their full courses, and they have the potential for rapid and massive negative impact on the financial and currency markets.

- ***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 should 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

GROSS DOMESTIC PRODUCT—GDP (First-Quarter 2015, First or "Advance" Estimate)

First-Quarter 2015 Real GDP Growth of 0.2% Was the Lowest Positive Number Possible, Given Inflation Issues. *[Note: The first four paragraphs here largely repeat or reflect the beginning of the* Opening Comments *section.]* Coming in at 0.2%, well below consensus [1.0% growth per Bloomberg], the headline first-quarter 2015 number likely was a signal to consensus forecasters by the Bureau of Economic Analysis (BEA), that the first-quarter GDP contracted and will be revised lower (into contraction) on May 29th. Discussed in the *Opening Comments*, this pattern appears to be repeating from the year before. What is not likely this time around, though, is a rebound in second-quarter GDP.

Indeed, the headline 0.2% first-quarter growth was the lowest real growth rate the BEA could have used, without raising issues of no growth or outright contraction. Where the headline implicit price deflator showed a negative 0.1% (-0.1%) annualized inflation rate in first-quarter 2015, reporting headline real (inflation-adjusted) growth of 0.1% would have left nominal (not-adjusted-for inflation) growth at flat. The BEA likely applied its "minimal" positive-growth guidance to the nominal number as well, which pushed the real minimal growth up to a headline 0.2%.

Reviewed in the *Distribution of Headline Growth* of the *Opening Comments* section, net of factors ranging from weather-induced utility usage, to games with the economic impact of the Affordable Care Act and with guesses at inventory build-up, headline GDP likely would have shown an annualized real contraction of about 2.0% (-2.0%) in today's initial headline reporting. Final sales (GDP net of the inventory build-up) showed a headline quarterly contraction of 0.5% (-0.5%).

Discussed in *No. 692 Special Commentary: 2015 - A World Out of Balance*, headline GDP reporting simply is not credible. Contrary to common experience, second- and third-quarter 2014 growth estimates were the strongest in more than a decade. Even at less than half the pace of the preceding quarters, headline fourth-quarter growth still significantly overstated economic reality; it should have been flat-to-minus. Downside revisions to recent periods await the July 30, 2015 annual GDP revisions, yet current underlying economic detail already has been weak enough so that even the regularly-bloated headline GDP reporting should turn negative, quarter-to-quarter, in the current and upcoming quarters.

Discussed frequently, the GDP does not reflect properly or accurately the changes to the underlying fundamentals that drive the economy. Underlying real-world economic activity shows that the broad economy began to turn down in 2006 and 2007, plunged into 2009, entered a protracted period of stagnation thereafter—never recovering—and then began to turn down anew in recent quarters.

The GDP simply remains the most worthless of the popular government economic series, in terms of determining what really is happening to U.S. business activity. The series is the most heavily-modeled, politically-massaged and gimmicked government indicator of the economy. It has been so since at least the days when President Lyndon Johnson reportedly reviewed the numbers before their release, and would return them to the Commerce Department, if Commerce had gotten them "wrong."

Notes on GDP-Related Nomenclature and Definitions

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

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

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

Gross National Product (GNP) *is the broadest measure of the U.S. economy published by the BEA. Once the headline number, now it rarely is followed by the popular media. GDP is the GNP net of trade in factor income (interest and dividend payments). GNP growth usually is weaker than GDP growth for net-debtor nations.*

Games played with money flows between the United States and the rest of the world tend to mute that impact on the reporting of U.S. GDP growth.

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

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

***GDP Implicit Price Deflator (IPD)** is the inflation measure used to convert GDP data from nominal to real. The adjusted numbers are based on "Chained 2009 Dollars," as introduced with the 2013 comprehensive revisions, where 2009 is the base year for inflation. "Chained" refers to the substitution methodology, which gimmicks the reported numbers so much that the aggregate of the deflated GDP sub-series missed adding to the theoretically-equivalent deflated total GDP series by $60.4 billion in "residual," as of the second estimate of fourth-quarter 2014.*

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

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

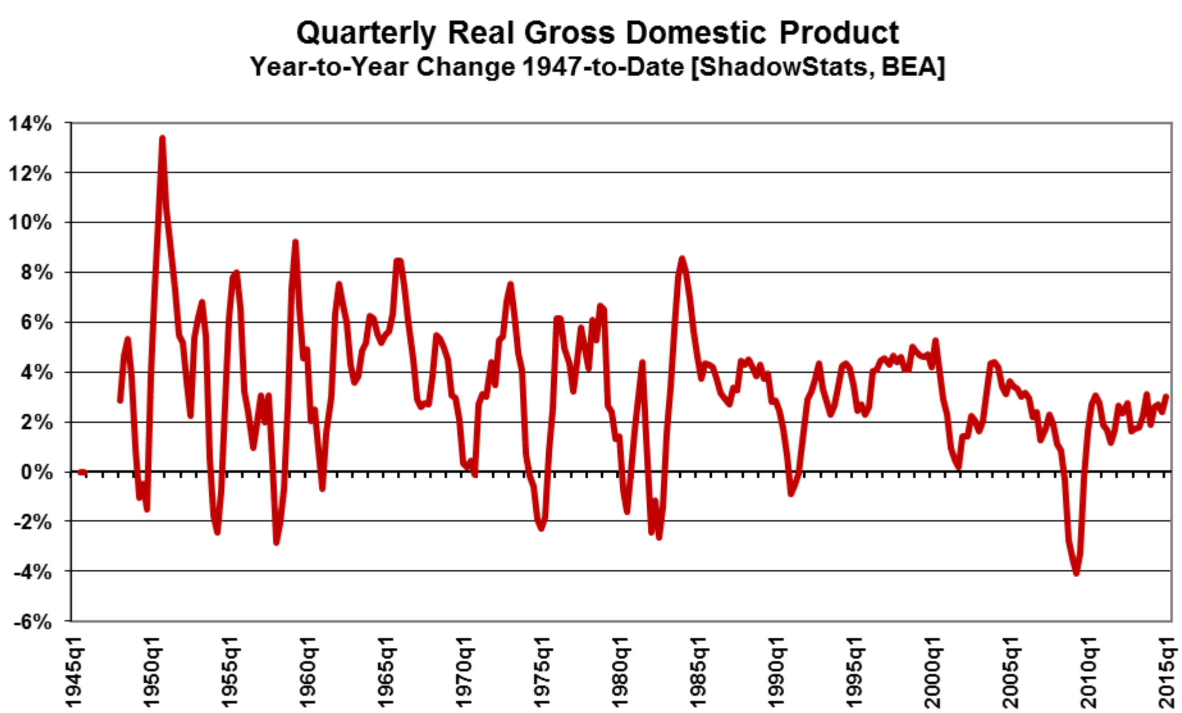
Gross Domestic Product (GDP). Published today, April 29th, by the Bureau of Economic Analysis (BEA), the first estimate of first-quarter 2015 GDP reflected a statistically-insignificant, real (inflation-adjusted), annualized, quarterly headline growth of 0.2% (0.25% at the second decimal point, rounds to 0.2%) +/- 3.5% (95% confidence interval).

That followed headline annualized real growth of 2.22% in fourth-quarter 2014, 4.97% real growth in third-quarter 2014, 4.59% real growth in second-quarter 2014, and a real annualized contraction of 2.11% (-2.11%) in first-quarter 2014. All the 2014 numbers face likely, significant downside revisions in the annual benchmarking of July 30, 2015. Distribution detail of the headline first-quarter 2015 GDP growth is outlined in the *Opening Comments*.

Shown in the accompanying graphs, headline year-to-year growth in first-quarter 2015 was 2.99%, versus 2.38% in fourth-quarter 2014, 2.70% in third-quarter 2014, 2.59% annual growth in the second-quarter 2014, and 1.89% in the first-quarter 2014. The headline annual growth for the first-quarter 2015 also should revise sharply lower.

The latest quarterly year-to-year growth remained below that near-term peak of 3.13% seen in fourth-quarter 2013. The current-cycle trough in annual change was in second-quarter 2009, at a 4.09% pace of decline (-4.09%). That was the deepest year-to-year contraction for any quarterly GDP in the history of the series, which began with first-quarter 1947.

The first graph following shows current year-to-year quarterly detail, from 2000-to-date, where the second graph shows the same series in terms of its full quarterly history.



Implicit Price Deflator (IPD). As general guidance, the weaker the inflation rate used in deflating an economic series, the stronger will be the resulting inflation-adjusted growth. The first estimate of first-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was an annualized quarterly contraction of 0.10% (-0.10%), versus an annualized gain of 0.16% in fourth-quarter 2014, 1.38% in third-quarter 2014, 2.15% in second-quarter 2014, and 1.33% in first-quarter 2014.

Year-to-year, first-quarter 2015 IPD inflation was 0.89%, versus 1.25% in fourth-quarter 2014, 1.57% in third-quarter 2014, 1.64% in second-quarter 2014, 1.37% in first-quarter 2014.

For purposes of comparison, headline CPI-U inflation (Bureau of Labor Statistics), seasonally-adjusted, annualized quarter-to-quarter showed an annualized contraction 3.01% (-3.01%) in first-quarter 2015, versus a contraction of 0.85% (-0.85%) in fourth-quarter 2014, and annualized gains of 1.18% in third-quarter 2014, 2.44% in second-quarter 2014, and 2.09% in first-quarter 2014.

Unadjusted, year-to-year quarterly inflation was a contraction of 0.10% in first-quarter 2015, versus gains of 1.25% in fourth-quarter 2014, 1.78% in third-quarter 2014, 2.05% in second-quarter 2014, and 1.41% in first-quarter 2014.

Gross National Product (GNP) and Gross Domestic Income (GDI). Neither the advance estimate of first-quarter 2015 GNP nor the advance estimate of first-quarter GDI will be published until next month (May 29th), because adequate information is not available for the BEA to hazard a meaningful guess on those numbers. In like manner, today's BEA guesstimate of the "advance" first-quarter GDP was not meaningful. As a service to the public and the financial markets, the BEA would do well to delay release of the initial GDP estimate by at least one month, on a regular basis.

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

GDI is the theoretical income-side equivalent of the consumption-side GDP estimate. The GDP and GDI are made to equal each other, every quarter, with the addition of a “statistical discrepancy” to the GDI-side of the equation, but the discrepancy just as easily could be added to the GDP number.

ShadowStats-Alternate GDP. The ShadowStats-Alternate GDP estimate for first-quarter 2015 GDP was a year-to-year contraction of 1.3% (-1.3%) versus the headline first-quarter GDP year-to-year gain of 3.0%, at the first decimal point. Those first-quarter 2015 estimates were against a ShadowStats estimated 1.6% (-1.6%) year-to-year contraction and a headline year-to-year gain of 2.4% in fourth-quarter 2014 GDP (see the Alternate Data tab).

While the annualized, real quarterly growth rate is not estimated formally on an alternate basis, the headline 0.2% annualized quarter-to-quarter gain for first-quarter 2015 most likely was much weaker, in contraction net of all the regular, initial reporting gimmicks. See the *Opening Comments* for a discussion on likely, near-term revisions to first-quarter data. Separately, downside quarterly-growth revisions to earlier quarters should follow, with the July 30, 2015 annual benchmark revision. That remains the most likely vehicle for moving recent, gimmicked headline quarterly growth rates to more-reasonable levels. An actual quarterly contraction appears to have been a realistic possibility for the real GDP in most quarters since the official, second-quarter 2009 end to the 2007 recession.

Adjusted for understated inflation and other methodological changes—such as the inclusion of intellectual property, software and recent accounting for the largely not-measurable and questionable impact of the Affordable Care Act (ACA)—the business downturn that began in 2006/2007 is ongoing; there has been no meaningful economic rebound. The "corrected" real GDP graph, and the longer-term "corrected" graph updated from *No. 692 Special Commentary: 2015 - A World Out of Balance* and *2014 Hyperinflation Report—Great Economic Tumble – Second Installment* (see the *Opening Comments* section) are based on the removal of the impact of hedonic quality adjustments that have reduced the reporting of official annual GDP inflation by roughly two-percentage points. It is not the same measure as the ShadowStats-Alternate GDP, which reflects reversing additional methodological distortions ("Pollyanna Creep") of recent decades.

WEEK AHEAD

Headline Reporting and Revisions Should Trend Much Weaker versus a Still Overly-Optimistic Economic Consensus; Inflation Will Rise Anew, Following the Bottoming of Oil-Prices. Shifting more to the downside, amidst increasingly-negative fluctuations in the numbers, market expectations for business activity have been, and still remain, overly optimistic. 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 until the July 30, 2015 GDP benchmark revision, but expectations for headline growth estimates (or revisions to) of first- and second-quarter 2015 should continue shifting to the downside, into increasingly negative territory (see *Opening Comments* and *Commentary No. 711*).

Headline CPI-U consumer inflation—recently driven lower by collapsing prices for gasoline and other oil-price related commodities—likely is close to its near-term, year-to-year low, having shown monthly declines in annual inflation of less than a full 0.1% (-0.1%) in the three months through March 2015. Significant upside inflation pressures should resume as oil prices rebound, a process that already may be underway, tentatively, and one that would accelerate rapidly with the 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 RELEASE:

Construction Spending (March 2015). The Commerce Department will release its estimate of March 2015 construction spending on Friday, May 1st. Detail will be covered by ShadowStats in the *Commentary* of Tuesday, May 5th.

The headline monthly changes, as usual, should not be statistically significant, while previous data will be subject to large and unstable revisions. Most frequently, revisions here are to the downside. Irrespective of almost perpetually-positive market expectations for this series [Bloomberg consensus is for a 0.4% monthly gain], the detail tends to be in down-trending stagnation, net of inflation.

U.S. Trade Balance (March 2015). The Commerce Department and Bureau of Economic Analysis (BEA) will release their estimate of the March 2015 trade deficit on Tuesday, May 5th. Early market expectations appear to be for a large widening in the nominal headline monthly deficit, following a large narrowing the month before. The February narrowing reflected collapsing oil prices. The March deficit could see some stabilization in that area.

As usual, a wider-than-expected trade deficit (at least after inflation-adjustment) is a good bet. The March detail, net of inflation adjustment, will help set the tone for the first revision (May 29th) to first-quarter 2015 GDP, where the headline first-quarter GDP estimate was based on the trade detail for only January and February 2015. A monthly deterioration in the inflation-adjusted March deficit, with negative implications for the first-quarter GDP revision, is a good bet.

A wild card in the pending reporting remains any effects of trade-flow disruptions from labor disputes and work slowdowns at major ports in The United States, or possibly in ice-related disruptions to Great Lakes-based commercial shipping traffic in recent months.

Look for a widening of the headline March deficit, along with some widening of the February shortfall, in revision, in both nominal and real terms. The general trend going forward should be for regular monthly and quarterly deteriorations in the real trade deficit.

Employment and Unemployment (April 2015). The Bureau of Labor Statistics (BLS) will release its April 2015 labor data on Friday, May 8th. Both employment and unemployment still are due for negative, headline surprises, given the ongoing, weak general tone of recent 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 jump in monthly payroll growth from March's lower-than-expected initial headline jobs gain of 126,000, and for perhaps a continued minimal reduction in the headline U.3 from the March rate of 5.5%, which was within a hair's breadth of rounding to 5.4% with the March estimation.

As with the narrowing of the headline unemployment rate in recent months and years, any further narrowing of the headline April 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 Near 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 March 2015 payroll employment, the implied built-in bias trend for April 2015 is for a headline jobs gain of 237,000 (see *Commentary No. 710*). Early expectations appear to be running slightly above trend.

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

