

COMMENTARY NUMBER 723
First Revision to First-Quarter GDP, April Household Income
May 29, 2015

**Inflation-Adjusted, First-Quarter Real GDP Sank by 0.7% (-0.7%);
Before Inflation Adjustment, Nominal GDP Dropped by 0.9% (-0.9%)**

**Reflecting Net-Negative International Flows in Income,
Broader Gross National Product Showed Real Decline of 1.4% (-1.4%),
Nominal Activity Tumbled by 1.5% (-1.5%)**

Consumer Liquidity Remains Structurally Impaired

**Broad Economic Contraction Continues;
No Pending Second-Quarter Rebound**

PLEASE NOTE: The next regular Commentary, scheduled for Wednesday, June 3rd, will cover the April trade deficit and the annual benchmark revision to same, as well as April construction spending, followed by a Commentary on Friday, June 5th, covering May employment and unemployment.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Headline Contractions in Both First- and Second-Quarter 2015 GDP Should Survive the Headline and Benchmark Reporting of July 30th. Broad economic activity in the United States contracted sharply in first-quarter 2015. Underlying activity was so weak that the heavily-gimmicked and bloated reporting of headline U.S. Gross Domestic Product (GDP) activity showed an outright contraction.

That contraction could deepen in revision, with a subsequent contraction also likely in the reporting of headline second-quarter activity. There is no rebound developing in second-quarter GDP, which should become increasingly evident in the next two months. Leading-indicator signals from real retail sales and new orders for durable goods, as well as early reporting on industrial production, all are consistent with headline, back-to-back quarterly downturns.

That circumstance should be recognized formally as a "new" recession, effectively upon the occurrence of the reporting. Likely timing for that remains July 30, 2015, coincident with the Bureau of Economic Analysis (BEA) release of the "advance" estimate of second-quarter 2015 GDP activity and the annual benchmark revisions to the GDP. As discussed in [No. 692 Special Commentary: 2015 - A World Out of Balance](#), however, the current downturn in business activity remains an ongoing element of the broad economic collapse into 2008 and 2009; it is not a new and separate business cycle.

The headline drop of 0.75% (-0.75%, rounds to -0.7%) in first-quarter real GDP was less than 0.02% shy of rounding to the consensus decline of 0.8% (-0.8%) indicated by Bloomberg. As cash registers recorded business activity, though, nominal first-quarter 2015 GDP contracted at an annualized quarterly pace of 0.87% (-0.87%).

Real final sales (GDP minus inventory change) in the quarter fell by an annualized 1.08% (-1.08%), having risen by 2.32% in fourth-quarter 2014.

Separately, net of deteriorating net global income flows relative to the United States, Gross National Product (GNP)—the broadest measure of U.S. economic activity—contracted at an annualized real pace of 1.40% (-1.40%) in first-quarter 2015, down by 1.54% (-1.54%) in nominal terms.

Reporting Instabilities. Highlighting instabilities in national-income reporting, Gross Domestic Income (GDI)—the theoretical, income-side equivalent of the consumption-based GDP—ran increasingly amok versus its numerical partner, with the statistical-discrepancy between the two series exploding to 1.9% of GDP. Real GDI was up by a headline 1.43% in first-quarter 2015, but that still was down sharply from 3.71% in fourth-quarter 2014.

In terms of the GDP itself, the headline "residual" was \$64.5 billion. That is the difference between the headline aggregate level of the real GDP, and the total GDP-level one gets by adding up all the separate GDP components. The "residual" is an artefact of the deflation process and the chained-weighting of the inflation measures. Putting the \$64.5 billion residual in perspective, the first-quarter headline decline of 0.7% (-0.7%) was generated by a drop of just \$30.6 billion in the quarterly level of real GDP.

Ongoing, Quasi-Official Jawboning to Explain Away Contracting GDP. Discussed in [Commentary No. 721](#) and [Commentary No. 722](#), there have been extraordinary efforts to excuse away the current downturn, by those with a vested interest in not seeing a contracting economy. Various stories have been publicized heavily in the popular financial press and other media.

Indeed, 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.

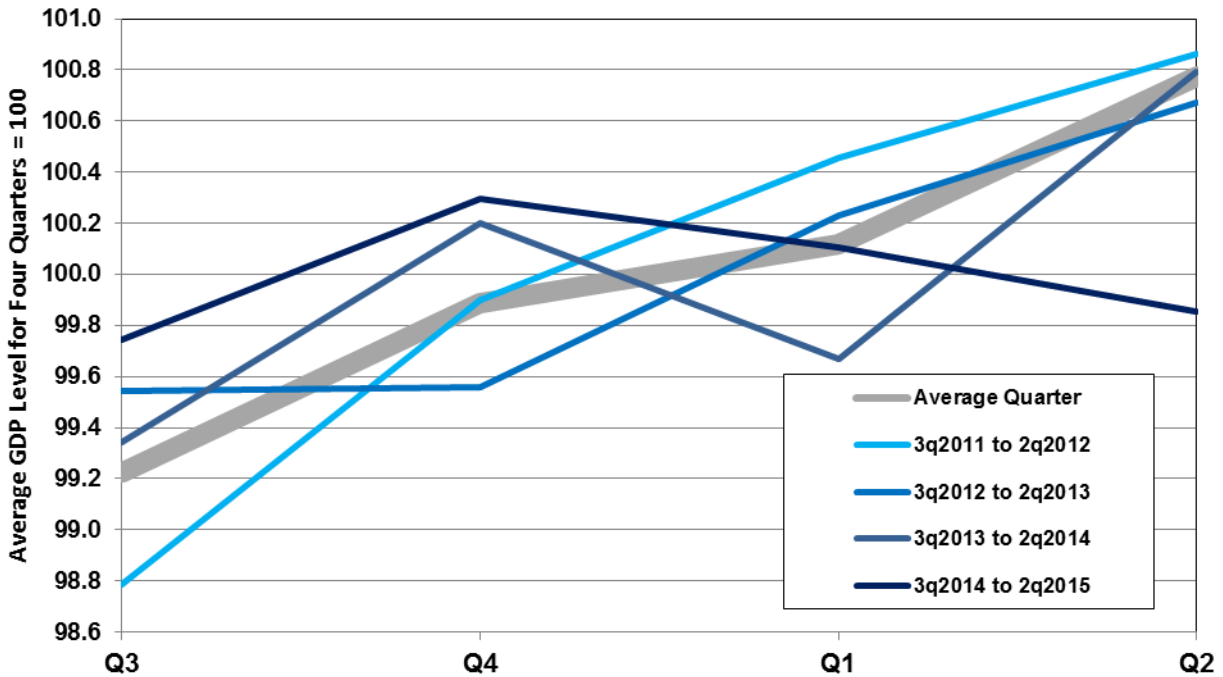
That circumstance evolved over decades, where efforts at controlling the numbers have been in place at least since the days of President Lyndon Johnson. Reportedly, he reviewed the GNP numbers before their

publication, and he would return them to the Commerce Department, if Commerce had gotten them "wrong." He would keep returning the numbers until Commerce got them "right."

Simply put, existing headline GDP reporting significantly overstates actual economic activity on a regular basis. Given all the built-in gimmicks and upside biases, the circumstance now is one where a headline downturn in GDP most likely means that the actual, underlying economy really has suffered a severe contraction, one deep enough to offset all the gimmicks. Such was the case in 2008 and 2009. Also the the case in 2001, subsequent GDP gaming removed much of the downside blip in those numbers.

One recent popular story excusing the current contraction has been that the GDP series suffers residual seasonality patterns that depressed first-quarter 2015 activity. Consider the following graph of GDP activity, explained below.

Real GDP Quarterly Reporting Patterns 3q2011 to 2q2015
 [ShadowStats, Bureau of Economic Analysis]



The level of quarterly real GDP was averaged for each of the four years beginning with the first period of third-quarter 2011 to second-quarter 2012, through the last period of third-quarter 2014 to second-quarter 2015, with the each year's average reset to 100 and the quarterly numbers indexed relative to that level. The four-quarter years were selected to have relative changes visible on both sides of first-quarter activity.

The four-quarter periods were plotted together to see what might exist in repetitive patterns, other than the ongoing growth that gives each line an upward slope. The thick gray line is the average of each of the third quarters, fourth quarters, etc.

The last period (thick dark-blue line), for third-quarter 2014 to second-quarter 2015, includes the headline reporting from today and a ShadowStats estimate of a quarterly contraction in second-quarter 2015. The average line does show some relatively slower growth for the first-quarter, but the average change is positive.

In the four years shown, the quarters leading into (two up, two down) and out of the first-quarter vary as to pattern. The historical post-recession period effectively is too short to establish meaningful residual patterns, if they existed. Generally, though, the aggregation of seasonally-adjusted data series into the GDP appears to work reasonably well in the context of broad seasonal stability.

There are, however, serious issues with this series. 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 ShadowStats Alternate or "Corrected" Series is described later. See also [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#) for more-extensive detail.

Today's Missive (May 29th). The balance of today's *Opening Comments* concentrates on the detail from the revision to first-quarter GDP and initial reporting on the GDI and GDP, along with an update on consumer-liquidity conditions, including the latest estimates of monthly real median household income, consumer confidence and consumer sentiment.

There is no *Hyperinflation Watch* section in today. The *Hyperinflation Outlook Summary* is being revised for *Commentary No. 724* of June 3rd (see [Commentary No. 722](#) for the most-recent version). The general outlook has not changed, but the updated text will reflect the latest economic and financial-market conditions, a review of unfolding Federal Reserve machinations and related implications for systemic stability or lack of same.

Separately, the *Week Ahead* section previews next week's release of May labor conditions, the April trade deficit and annual benchmark revision, and April construction spending.

Gross Domestic Product (GDP)—First-Quarter 2015, Second Estimate, First Revision—Contracted both Before and After Inflation-Adjustment. The second estimate of, first revision to first-quarter 2015 GDP showed a statistically-insignificant, annualized, headline real (inflation-adjusted) contraction of 0.75% (-0.75%) [rounds to 0.7% (-0.7%)]. That followed headline annualized real growth of 2.22% in fourth-quarter 2014.

Nominal Detail. With headline GDP inflation—the Implicit Price Deflator (IPD)—down by a revised 0.12% (-0.12%) in the first quarter, the headline nominal (not-inflation-adjusted) GDP contracted at a revised annualized pace of 0.87% (-0.87%), versus an annualized nominal gain of 2.38% in fourth-quarter 2014. Year-to-year, nominal annual growth in first-quarter 2015 GDP revised to 3.64%, versus 3.66% in fourth-quarter 2014.

Real Year-to-Year Growth. Shown in *Reporting Detail* graphs, headline year-to-year real growth in first-quarter 2015 revised to 2.73%, versus 2.38% in fourth-quarter 2014. 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.

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 second estimate of first-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was an revised annualized quarterly contraction of 0.12% (-0.12%), versus an annualized gain of 0.16% in fourth-quarter 2014. Year-to-year, first-quarter 2015 IPD inflation was unrevised at 0.89%, versus 1.25% in fourth-quarter 2014.

For purposes of comparison, headline CPI-U inflation (Bureau of Labor Statistics), showed a seasonally-adjusted, annualized quarterly contraction of 3.01% (-3.01%) in first-quarter 2015, versus a contraction of 0.85% (-0.85%) in fourth-quarter 2014. Unadjusted, year-to-year quarterly CPI-U inflation was a contraction of 0.10% (-0.10%) in first-quarter 2015, versus a gain of 1.25% in fourth-quarter 2014.

Gross National Product (GNP). Given the poor-quality of broad economic data available on a timely basis, quarterly reporting of the GNP and GDI traditionally is delayed for release until the second estimate of the GDP (until the third-estimate at the end of the calendar-year).

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

The initial estimate of headline, real first-quarter 2015 GNP showed an annualized contraction of 1.40% (-1.40%), versus a gain of 1.36% in fourth-quarter 2014. Those numbers are weaker than the respective annualized GDP first-quarter contraction and fourth-quarter growth rates of 0.75% (-0.75%) and 2.22%. Year-to-year annual GDP growth was 2.42% in first-quarter 2015, versus 2.05% in fourth-quarter 2014.

In nominal terms, the annualized first-quarter GNP contraction was 1.54% (-1.54%), versus a gain of 1.50% in the fourth quarter. Nominal annual growth was 3.32% in first-quarter 2015, the same level as in fourth-quarter 2014.

There has been a shift in global factor-income trends since third-quarter 2014, likely reflecting some impact from recent U.S. dollar strength. The relatively deeper contractions in GNP activity versus the GDP, in both the first- and fourth-quarter numbers, reflected declining income flows from the rest of the world to the United States, exacerbated by the United States making increased income payments to the rest of the world.

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

Headline, annualized, real first-quarter GDI growth was 1.43%, slowing sharply versus a revised 3.71% gain in fourth-quarter 2014. Year-to-year annual growth increased to 3.56% in first-quarter 2015, versus a revised 3.00% gain in fourth-quarter 2014.

Annualized nominal GDI growth in first-quarter 2015 was 1.30%, versus 3.88% in the fourth-quarter. Year to year nominal growth was 4.48% in first-quarter 2015, versus 4.29% in fourth-quarter 2014.

Also in nominal terms, the statistical discrepancy widened sharply in first-quarter 2015. Highlighting the general insignificance of the GDP reporting, the statistical discrepancy—error—between the GDI and the GDP more than doubled in the last four-quarters from 0.9% of the GDP in second-quarter 2014, to 1.9% of the GDP in first-quarter 2015.

Revised 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 second estimate of annualized quarterly change in first-quarter 2015 GDP was a contraction of 0.75% (-0.75%, rounds to 0.7%), revised from an initial growth estimate of 0.25% (rounds to 0.2%), following 2.22% growth in fourth-quarter 2014.

The BEA's second 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 total, headline change in GDP, where $1.23\% + 0.12\% - 1.90\% - 0.20\% = -0.75\%$. When the June 24th "final" monthly and the July 30th benchmark revisions are in place, headline first-quarter 2015 GDP real growth should remain solidly in negative territory, likely showing an even deeper contraction than indicated in today's detail. [Commentary No. 715](#) discussed the initial estimates of the growth distribution for first-quarter GDP.

- ***Consumer Spending Contributed 1.23%% [Previously 1.31%] to First-Quarter Growth; Contributed 2.98% to Fourth-Quarter.*** The bulk of the downside first-revision in consumer spending was in the "other services" category. As before, the relatively hard detail on personal consumption of goods showed flat growth for the quarter. The positive growth came from the services sector in increased utility usage tied to unseasonably-bad weather (contributed 0.57% to the GDP growth rate), and the ongoing questionable economic growth purportedly being generated by the ACA (contributed well in excess of 0.60% to the GDP growth rate).
- ***Business/Residential Investment Contributed 0.12% [Previously 0.34%] to First-Quarter Growth; Contributed 0.61% to Fourth-Quarter.*** The fudge-factor of inventory building in the first growth estimate, which contributed 0.74% of the initial GDP growth rate, was revised lower to a 0.33% growth-rate contribution. That decline was offset partially by less-negative nonresidential construction and stronger equipment sales. Final sales (GDP minus inventory change) contracted at a revised pace of 1.08% (-1.08%) [previously down by 0.49% (-0.49%)] having risen by 2.32% in fourth-quarter 2014.
- ***Net Exports Subtracted 1.90% (-1.90%) [Previously 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. 716](#), and perhaps suggestive of a still-deeper, first-quarter trade shortfall in pending revision with the April 2015 reporting, deteriorating net exports subtracted

1.90% (-1.90%) from the aggregate quarterly GDP growth rate. Further revision here is possible (see the *Week Ahead* section).

- ***Government Spending Subtracted 0.20% (-0.20%) [previously 0.15% (-0.15%)] from First-Quarter Growth; Subtracted 0.35% (-0.35%) from Fourth-Quarter.*** Where federal government consumption knocked 0.53% off the fourth-quarter's growth rate, such turned neutral in first-quarter 2015. 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 0.21% (-0.21%) in the latest reporting, which encompassed the net revision to this category.

Economic Reality. With the second official estimate of first-quarter 2015 GDP activity showing a contraction of 0.7% (-0.7%), versus 2.2% headline growth in fourth-quarter 2014, the general outlook as to underlying economic reality has not changed. Discussed earlier in these *Opening Comments*, and recently in [Commentary No. 719](#) 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. That includes a likely, further downside revision to first-quarter 2015 activity on June 24th. Monthly economic detail—early in the quarter—already suggests that, and new headline numbers should continue to confirm those patterns in the reporting of May and June headline activity.

In advance of the annual GDP overhaul on July 30th, major benchmark revisions are due in the next month or two for key series such as the trade deficit (next week) and industrial production (mid-July). The historical revisions should continue to be GDP-negative in these government-shutdown-delayed, catch-up reportings. As a result, 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.

Again, 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. 717](#)), monthly real median household income and other consumer measures (see the following *Consumer Liquidity* section). This also has been detailed 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. 720](#) 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 second estimate of first-quarter 2015 GDP.

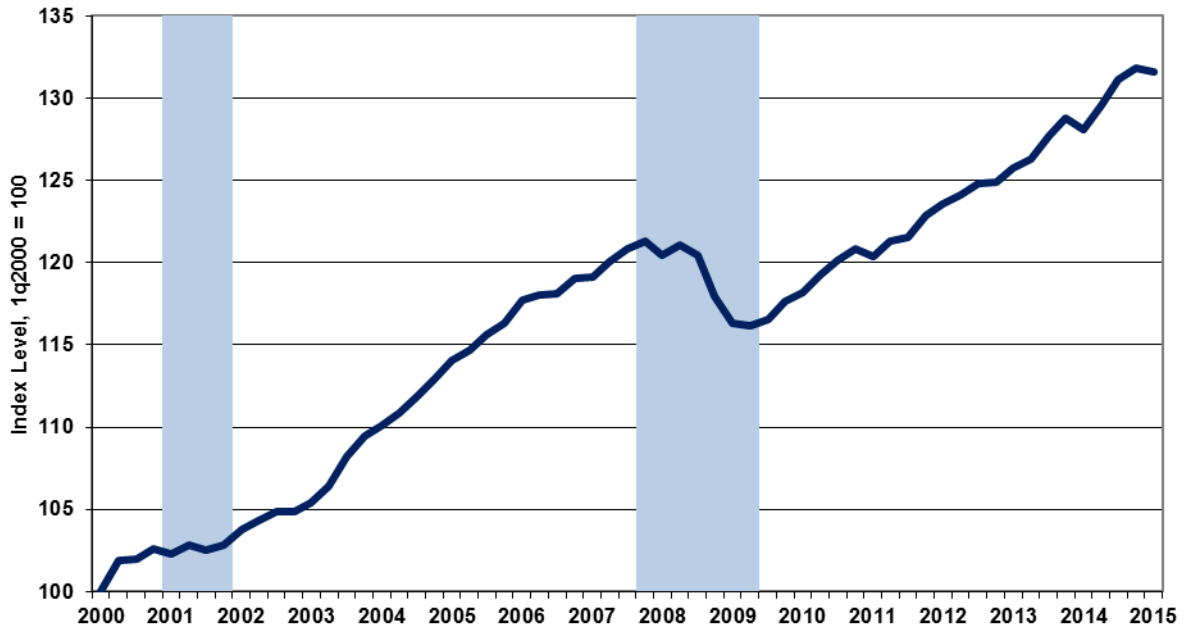
The first set of graphs (2000-to-date) is the one traditionally that has been incorporated in the GDP *Commentaries*, and is expressed on an index base where first-quarter 2000 = 100.0. The second set updates the longer-term graphs (1970-to-date), expressed in billions of 2009 dollars as used in headline 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 (growth interruptions for first-quarter 2014 and first-quarter 2015 excepted). Adjusted for official GDP inflation (the implicit price deflator), the revised level of headline first-quarter 2015 GDP currently stands 8.5% [previously 8.8%] above its pre-recession peak-GDP estimate of fourth-quarter 2007. In contrast, the “corrected” GDP version, in the second graph, now shows first-quarter 2015 GDP activity down by 6.9% (-6.9%) [previously down 6.6% (-6.6%)] from its pre-recession peak of first-quarter 2006.

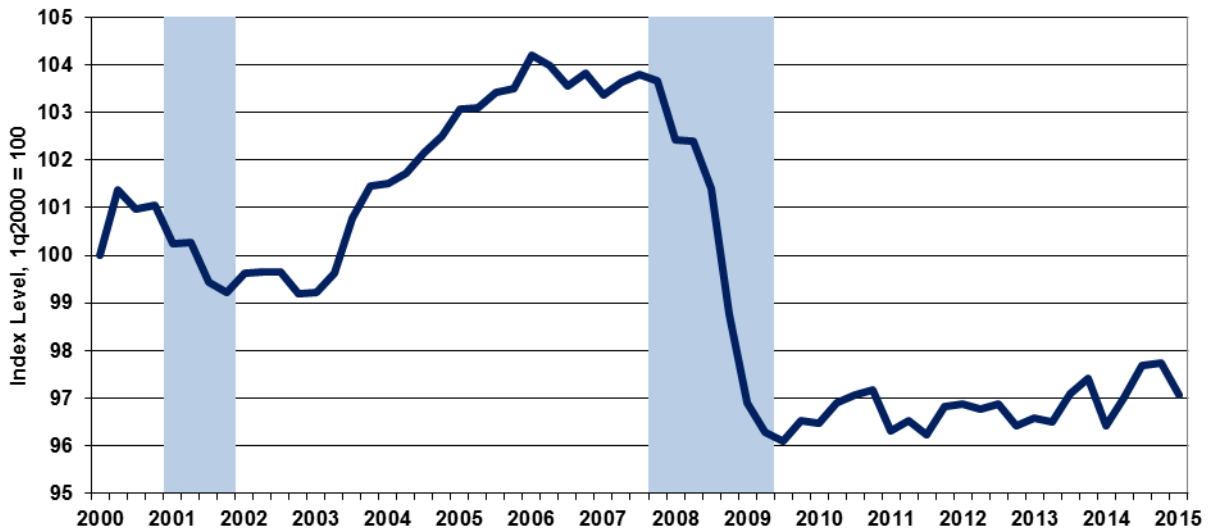
Further, discussed in the second installment of the *Hyperinflation Report*, and again in *No. 692 Special Commentary*, no other major economic series has shown a parallel pattern of official full economic recovery and meaningful expansion thereafter, consistent with the GDP reporting. Such is covered in the recent discussions on industrial production, real retail sales and real durable goods orders in [Commentary No. 719](#), [Commentary No. 721](#) and [Commentary No. 722](#). 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*.

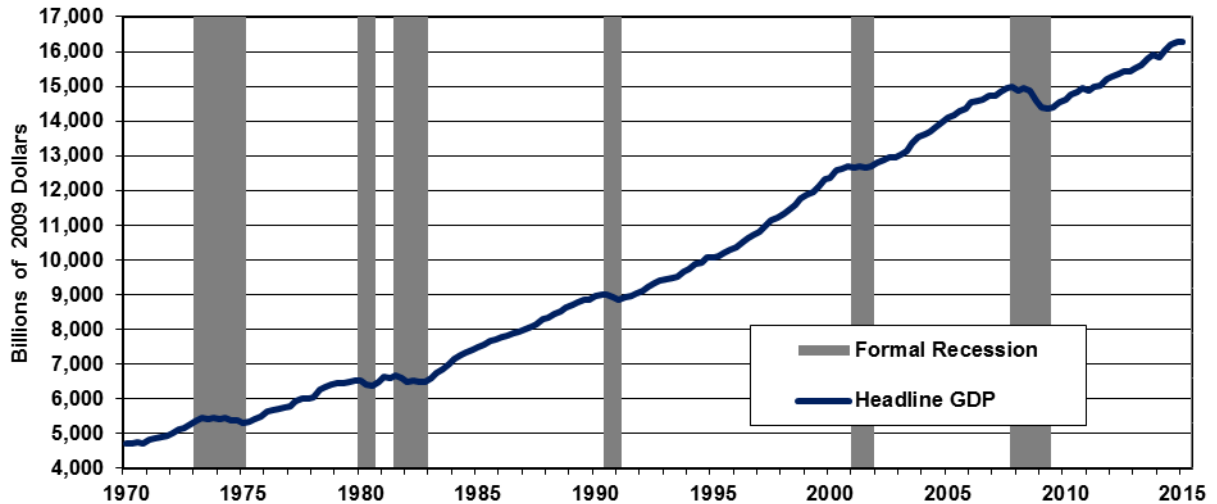
Headline Real GDP
GDP Deflated by Official Implicit Price Deflator
To 1q2015, Seasonally-Adjusted [ShadowStats, BEA]



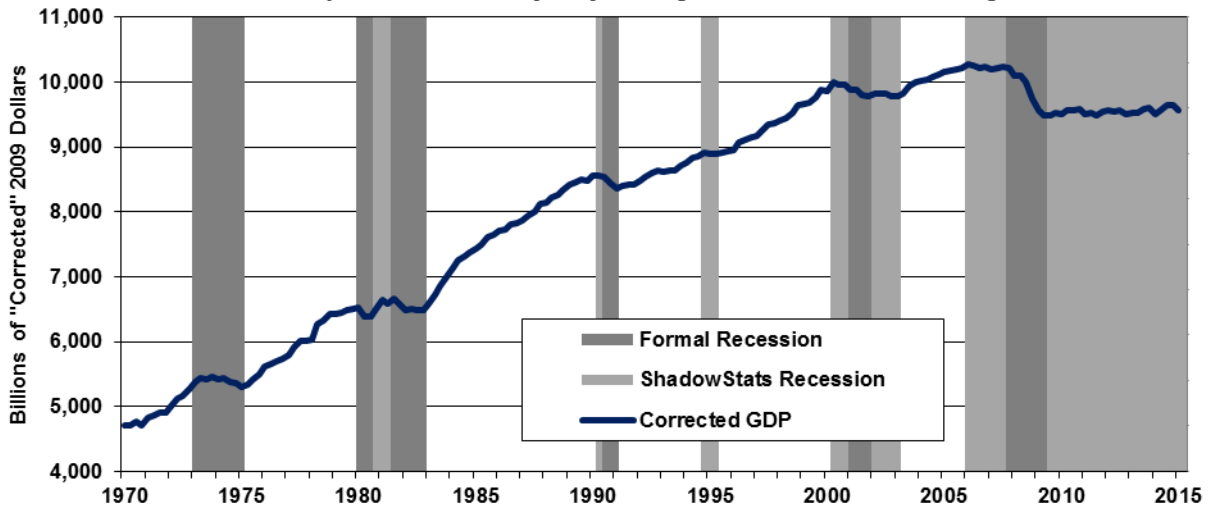
Corrected Real GDP
Nominal GDP Deflated by Implicit Price Deflator Corrected for
Roughly Two-Percentage Point Understatement of Annual Inflation
To 1q2015, Seasonally-Adjusted [ShadowStats, BEA]



Headline Real GDP
 Nominal GDP Deflated by Implicit Price Deflator
 To 1q2015, Seasonally-Adjusted [ShadowStats, BEA]



Corrected Real GDP
 Nominal GDP Deflated by Implicit Price Deflator Adjusted for
 Understatement of Annual Inflation
 To 1q2015, Seasonally-Adjusted [ShadowStats.com, BEA]



Consumer Liquidity Problems Promise Continued Economic Difficulties. Updating [Commentary No. 718](#) of May 13th, and as otherwise discussed regularly in these *Commentaries* (see detail in [No. 692 Special Commentary: 2015 - A World Out of Balance](#)), structural liquidity problems have constrained domestic economic activity, severely, since before the Panic of 2008. Never recovering in the post-Panic

era, limited income, credit and a faltering consumer outlook have eviscerated business activity that feeds off the financial health and liquidity of consumers.

Without real (inflation-adjusted) growth in household income and without 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 restraints on consumption have driven 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. Together, those sectors account for more than 70% of aggregate U.S. GDP activity.

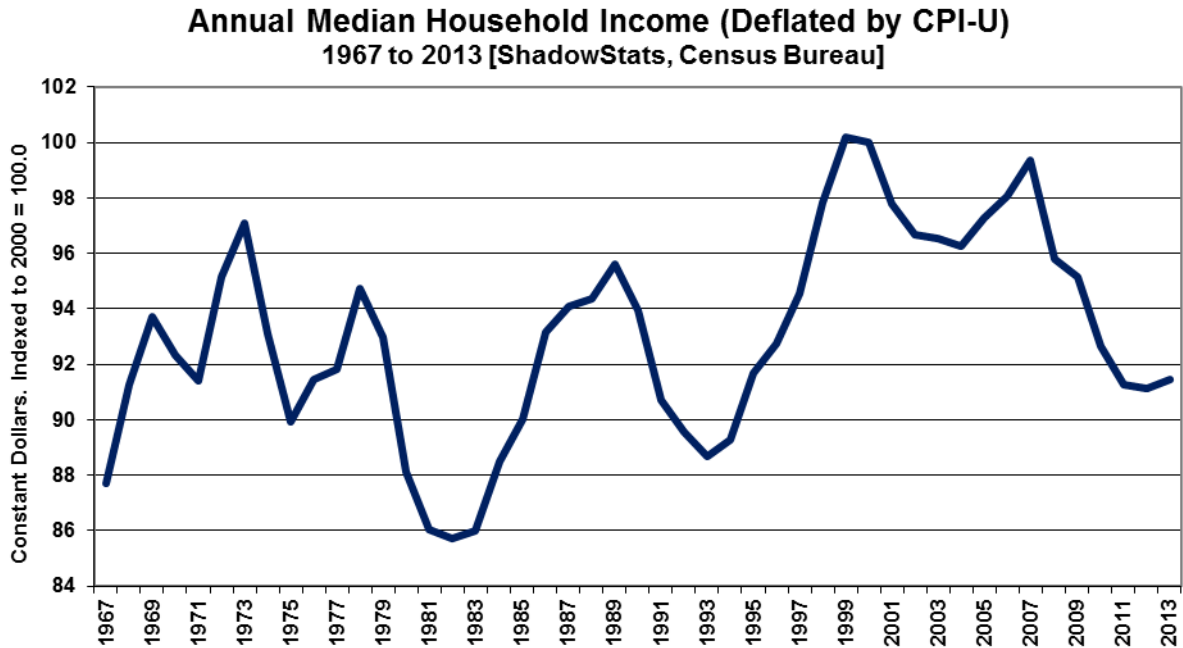
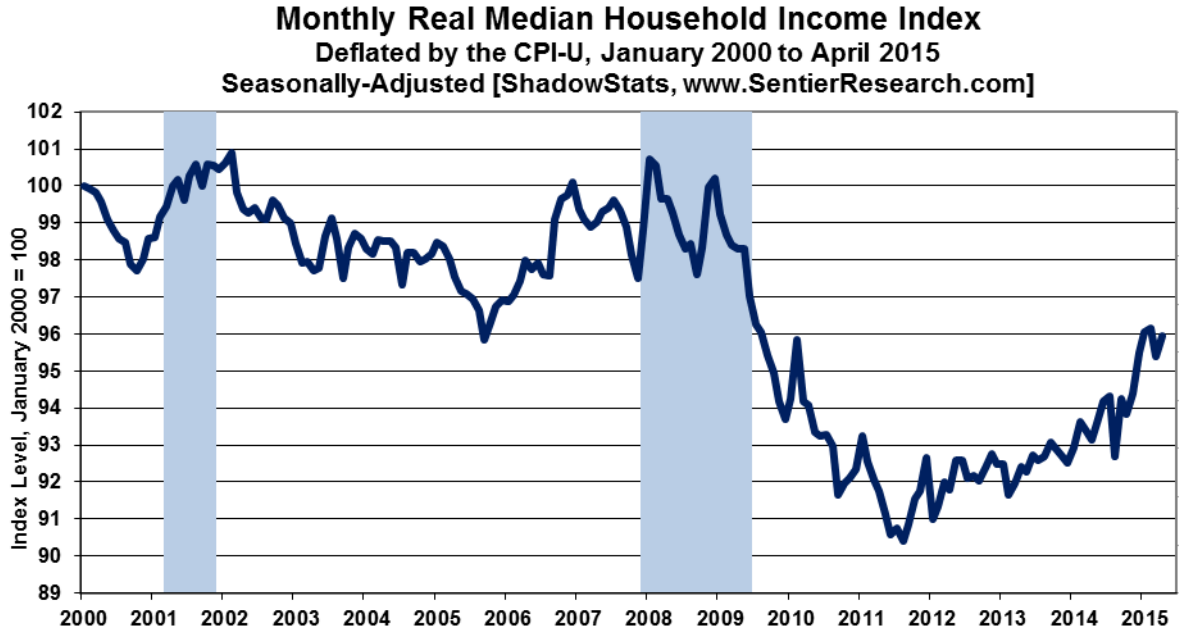
Just-released readings on April 2015 real median household income and May 2015 consumer-confidence and consumer-sentiment are updated here. Also shown are the most-recent readings on consumer credit outstanding and quarterly household sector debt outstanding detail, as previously published. Underlying economic fundamentals simply have not supported, and do not support a turnaround in broad economic activity. There has been no economic recovery, and there remains no chance of meaningful, broad economic growth, without a fundamental upturn in consumer- and banking-liquidity conditions.

Consider the following graphs. The first graph shows monthly real median household income through April 2015, as reported by www.SentierResearch.com on May 28th. The income series has continued in low-level stagnation, remaining off, but still near its cycle low, despite recent up-trending in month-to-month volatility. Where negative inflation boosts the level of real growth relative to nominal growth, the recent relative "strength" in the series largely was fed, temporarily, by gasoline-price-driven, headline month-to-month contractions in CPI-U reporting.

The renewed downturn in March 2015 reflected the headline CPI-U rising by 0.2% in March 2015, with the headline decline in real median household income (deflated by the CPI-U) a statistically-significant monthly drop of 0.8% (-0.8%). Before inflation adjustment, the nominal reading for median household income still declined by 0.6% (-0.6%) month-to-month for March. In April, with the CPI-U up by just 0.1%, real median household income was up by a statistically-significant 0.6%, with nominal income up by 0.7% in the month.

Where lower gasoline prices have provided some minimal liquidity relief to the consumer, indications are that any effective extra cash has been used to pay down unsustainable debt, not to fuel new consumption. Relief from low-priced gasoline should prove increasingly fleeting, as the U.S. dollar resumes its decline and petroleum prices continue to spike anew.

On a monthly basis, when headline GDP purportedly started its solid economic recovery in mid-2009, household income plunged to new lows and has yet to recover its level seen during the formal recession, or the pre-recession highs either for the 2007 recession or the 2001 recession.

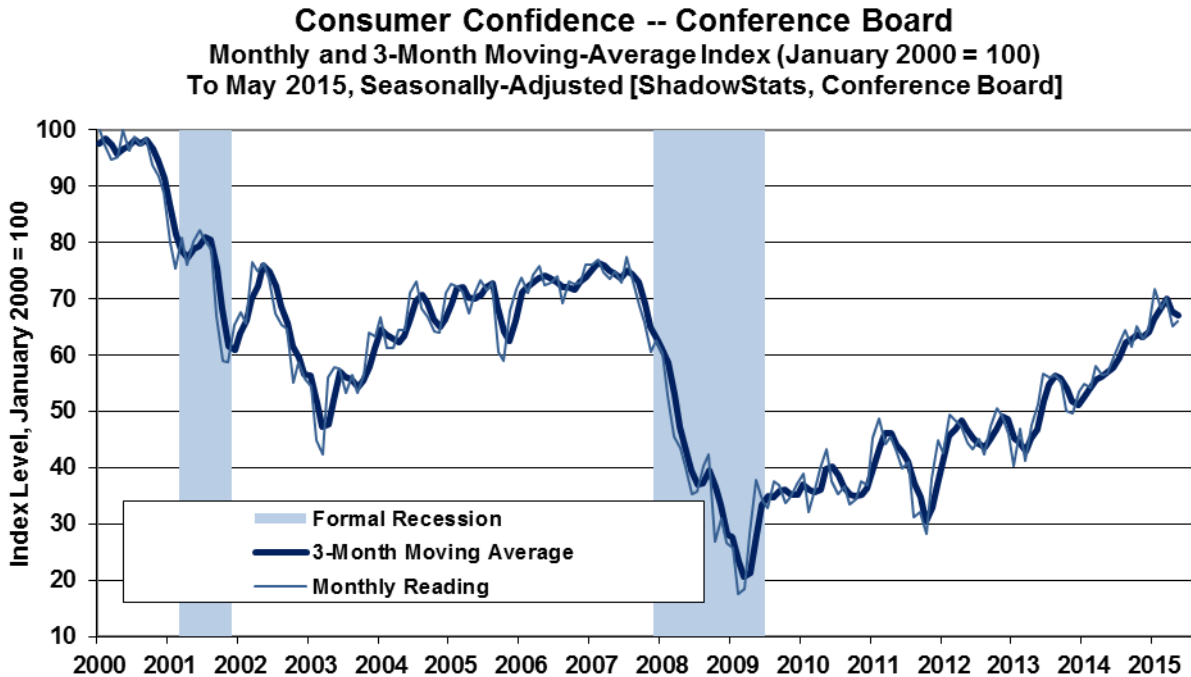


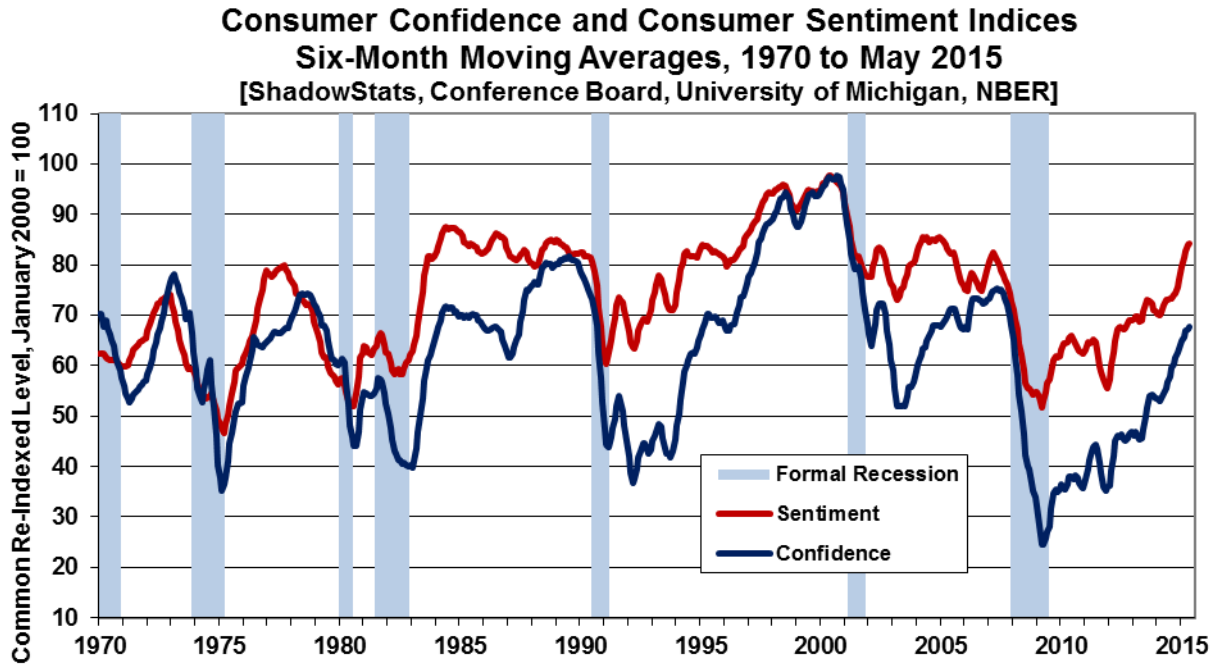
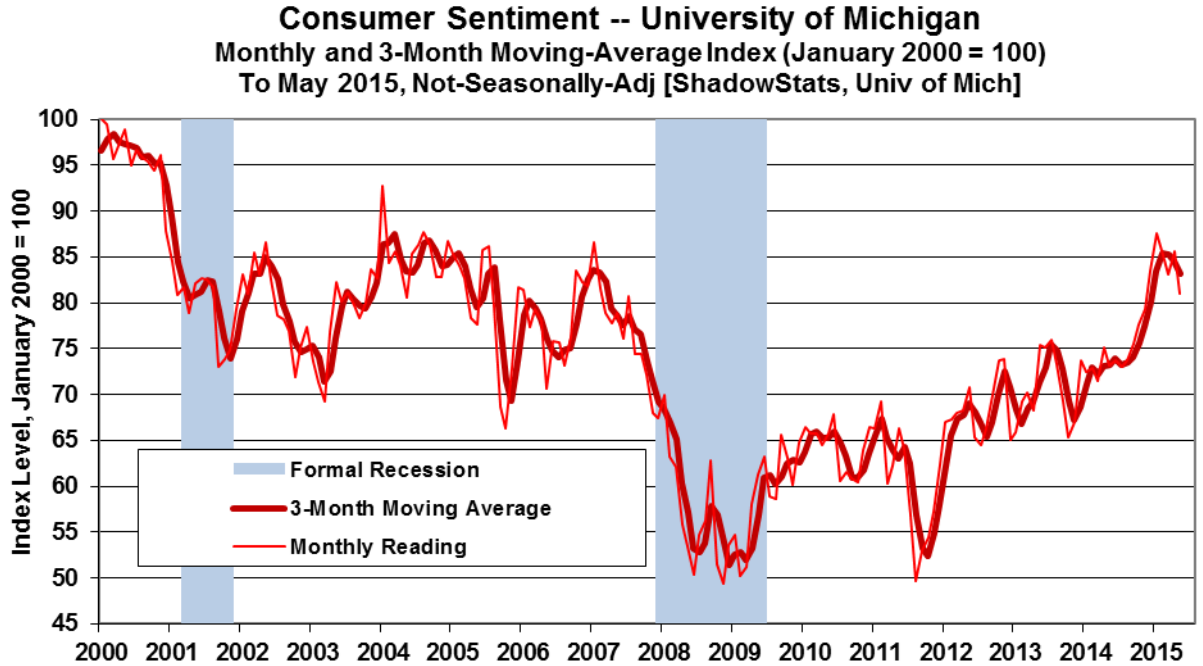
Shown in the second graph (preceding), the same series, published by the Census Bureau on an annual basis, deflated by headline CPI-U, confirmed that in 2013—the latest-available data—annual real median household income continued to hold at a low level of activity. In historical perspective, 2011, 2012 and 2013 income levels were below levels seen in the late-1960s and early-1970s. Such indicates the long-term nature of the evolution of the major structural changes squeezing consumer liquidity and impairing the current economy. Further discussion of these issues is found in [No. 692 Special Commentary](#),

[Commentary No. 658](#), and in [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#) and [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#).

The next three graphs reflect the latest headline activity in consumer confidence and sentiment. The Conference Board's Consumer Confidence Index (updated on May 26th) and the University of Michigan's Consumer Sentiment Index (updated today, May 29th) respectively notched higher and lower for the full month of May 2015. Both series continued to pull back in their three-month moving-average readings. The confidence and sentiment series tend to mimic the tone of headline economic reporting in the press, and often are highly volatile month-to-month, as a result. An increasingly-negative toll from in headline economic reporting should be seen in continuing hits to both the confidence and sentiment readings in the months ahead.

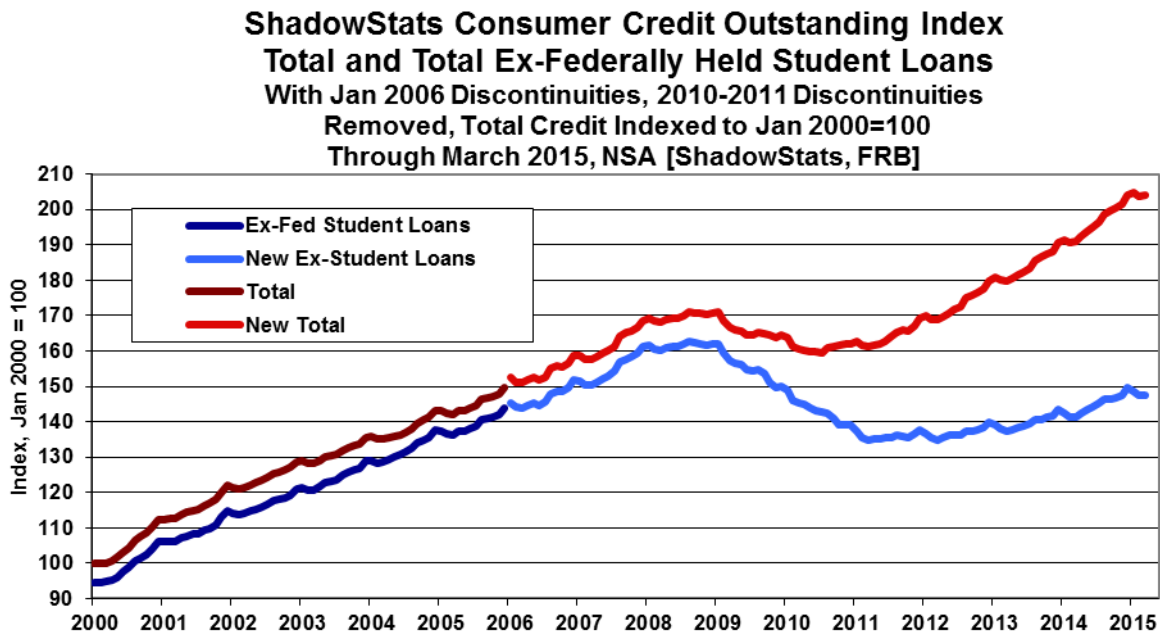
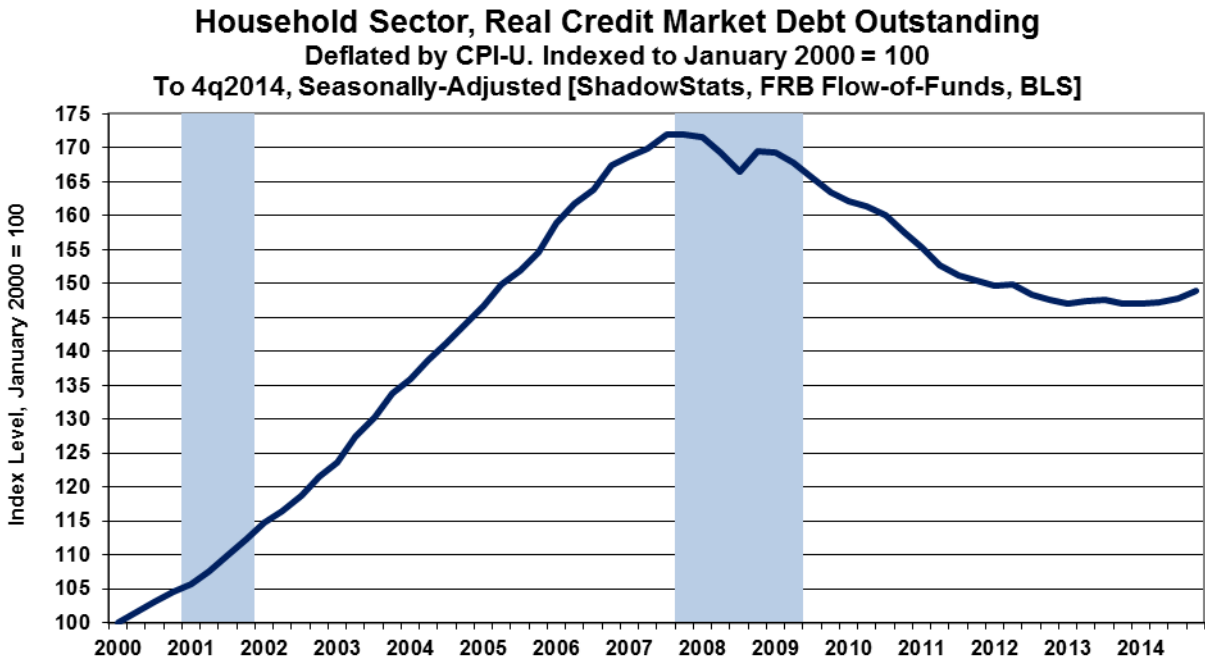
Smoothed for the irregular, short-term volatility, however, the two series still remain at levels seen typically in recessions. As suggested in the third graph, as plotted for the last 40 years, the latest readings of confidence and sentiment generally have not recovered levels that preceded any of the formal recessions of the last 40 years, and generally remain well below, or are inconsistent with, periods of historically-strong economic growth that would rival recent booming, headline GDP gains of recent quarters in 2014.





The final two graphs in this section address consumer borrowing. Debt expansion can help to make up for a shortfall in income growth. Shown in the first graph of *Household Sector, Real Credit Market Debt Outstanding*, household debt declined in the period following the Panic of 2008, and it has not recovered. The series includes mortgages, automobile and student loans, credit cards, secured and unsecured loans, etc., all deflated by the headline CPI-U. The level of real debt outstanding has remained stagnant for

several years, reflecting, among other issues, lack of normal lending by the banking system into the regular flow of commerce. Updated through fourth-quarter 2014, the graph reflects the most-recent detail available from the Federal Reserve's flow-of-funds data.



The second graph shows the regular plot of nominal consumer credit outstanding, updated through March 2015. Post-2008 Panic, it has continued to be dominated by growth in federally-held student loans, not in

bank loans to consumers that otherwise would fuel broad consumption growth. Before consideration for inflation, the nominal level of consumer credit outstanding (ex-student loans) has not rebounded or recovered since the onset of the recession. These disaggregated data are available and plotted only on a not-seasonally-adjusted basis.

Again, consumer liquidity woes remain the basic constraint on broad economic activity in the United States, which remains heavily consumer oriented. Without real growth in income and/or debt expansion and willingness to take on new debt, and with consumer confidence and sentiment at levels consistent with a significant portion of consumers under financial stress, there has been no basis for a sustainable economic expansion since the Panic of 2008. There are no prospects for a recovery in the near term.

[The Reporting Detail section includes further information on the GDP revision.]

REPORTING DETAIL

GROSS DOMESTIC PRODUCT—GDP (First-Quarter 2015, Second Estimate, First Revision)

First-Quarter 2015 Real (Inflation-Adjusted) GDP Contraction of 0.7% (-0.7%) Fell by a Nominal 0.9% (-0.9%), before Inflation Adjustment. *[The text here through the "Notes on GDP ..." section largely is repeated from the Opening Comments section.]* Broad economic activity in the United States contracted sharply in first-quarter 2015. Actual activity was so weak as to push the heavily gimmicked and bloated reporting of headline U.S. Gross Domestic Product (GDP) activity into an outright contraction. That contraction should deepen in revision, with a subsequent headline contraction likely in second-quarter activity.

There is no unfolding second-quarter rebound in activity, which should become increasingly evident in the reporting of the next two months. Recent leading-indicator signals from series such as real retail sales and new orders for durable goods, as well as early reporting on industrial production, are consistent with headline, back-to-back quarterly downturns.

That should be recognized formally as a "new" recession, effectively upon the occurrence of such headline reporting. That could happen on July 30, 2015, coincident with the "advance" estimate of second-quarter 2015 GDP activity and the annual benchmark revisions to the GDP. As discussed in [No. 692 Special Commentary: 2015 - A World Out of Balance](#), however, the current downturn in business activity still is an ongoing element of the broad economic collapse into 2008 and 2009.

Coming in at a drop of 0.75% (-0.75% or -0.7% at the first decimal point) the headline contraction in first-quarter real GDP was less than 0.02% shy of rounding to the expected decline of 0.8% (-0.8%) indicated by Bloomberg. Final sales (GDP minus inventory change) contracted at a revised annualized pace of 1.08% (-1.08%), having risen by 2.32% in fourth-quarter 2014.

As the cash register recorded business activity, nominal first-quarter 2015 GDP fell at an annualized quarterly pace of 0.87% (-0.87%).

Net of deteriorating net global flows relative to the United States, Gross National Product (GNP)—the broadest measure of U.S. economic activity—fell at an annualized real pace of 1.40% (-1.40%) in first-quarter 2015, down by 1.54% (-1.54%) in nominal terms.

Reporting Instabilities. Highlighting instabilities in national-income reporting, Gross Domestic Income (GDI)—the theoretical, income-side equivalent of the consumption-based GDP—ran increasingly amok versus its numerical partner, with the statistical-discrepancy between the two series exploding to 1.9% of GDP. Real GDI was up by a headline 1.43% in first-quarter 2015, but that still was down sharply from 3.71% in fourth-quarter 2014.

In terms of the GDP itself, the headline "residual," which is the difference between the headline aggregate level of the real GDP and the total one gets by adding up all the separate GDP components, was \$64.5 billion. The "residual" is an artefact of the deflation process and the chained-weighting of the inflation measures. Putting the \$64.5 billion residual in perspective, the headline decline of 0.7% (-0.7%) in first-quarter activity was generated by a drop of just \$30.6 billion in the headline quarterly level of real GDP.

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 then 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 $1.01 \times 1.01 \times 1.01 \times 1.01 = 1.0406$ or 4.1%, instead of $4 \times 1\% = 4\%$.

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

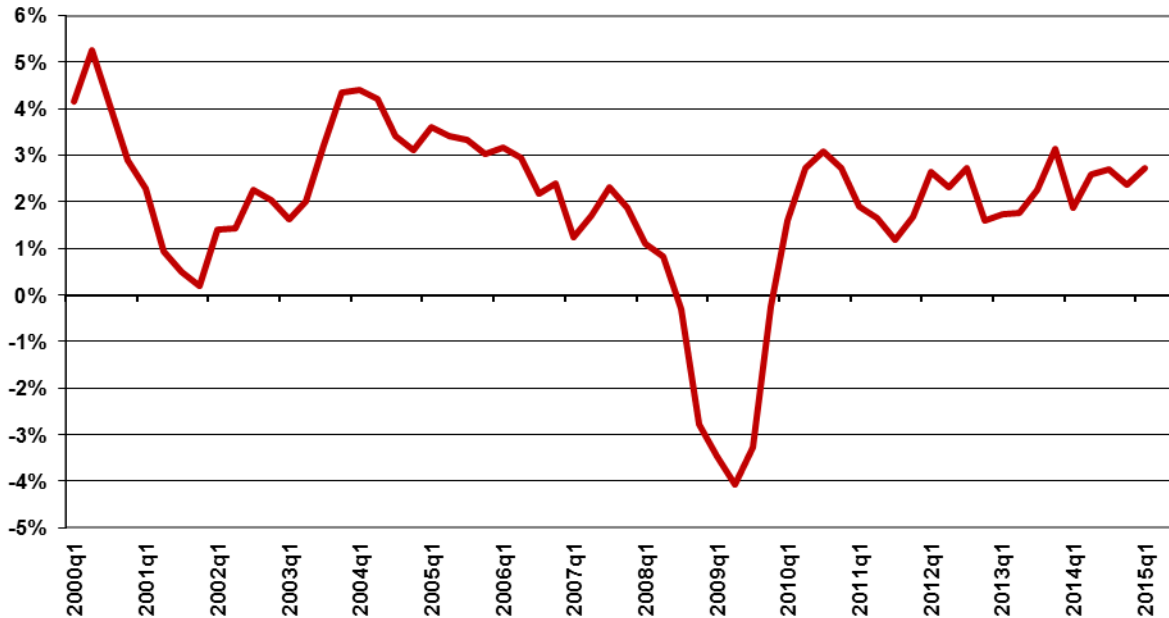
Gross Domestic Product (GDP). Published today, May 29th, by the Bureau of Economic Analysis (BEA), the second estimate of first-quarter 2015 GDP reflected a statistically-insignificant, real (inflation-adjusted), annualized, quarterly headline contraction of 0.7% (-0.7%) [down by 0.75% (-0.75%) at the second decimal point, rounds to 0.7% (-0.7%)] +/- 3.5% (95% confidence interval). The earlier, first estimate, had indicated a quarterly gain of 0.2% (0.25% at the second decimal point, rounded to 0.2%).

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 revised headline first-quarter 2015 GDP growth is outlined in the *Opening Comments*.

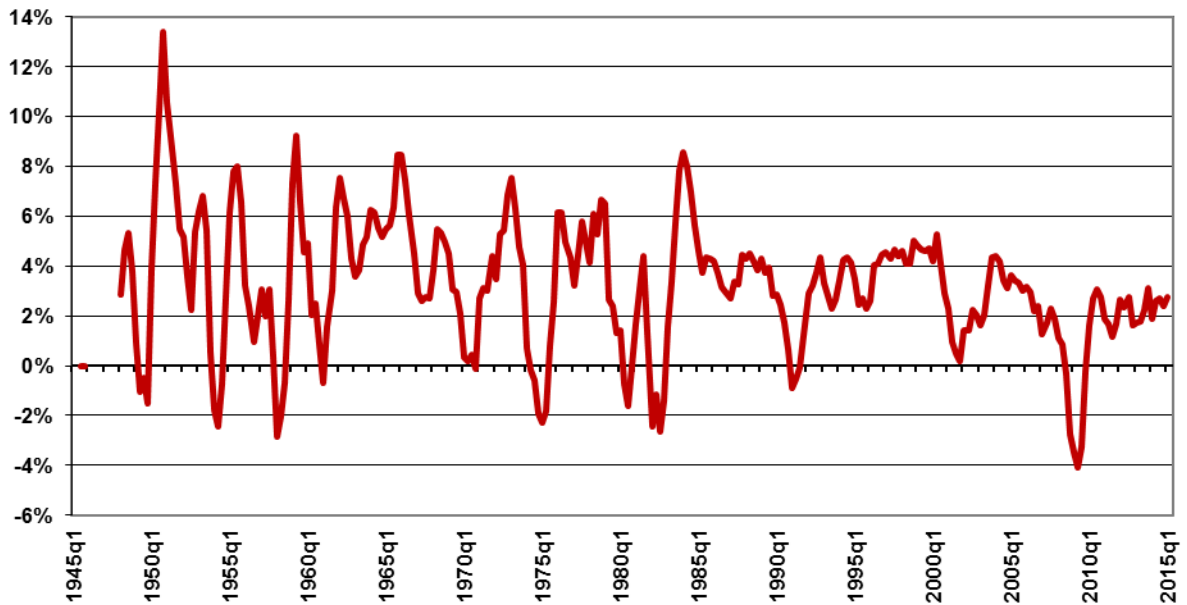
Nominal Detail. With headline GDP inflation—the Implicit Price Deflator (IPD)—down by a revised 0.12% (-0.12%) in the first quarter, the headline nominal (not-inflation-adjusted) GDP contracted at a revised annualized pace of 0.87% (-0.87%) [previously up by 0.14%], versus an annualized nominal gain of 2.38% in fourth-quarter 2014. Year-to-year, nominal annual growth in first-quarter 2015 GDP revised to 3.64% (previously 3.91%), versus 3.66% in fourth-quarter 2014, 4.31% in third-quarter 2014, 4.27% in the second-quarter 2014 and 3.28% in the first-quarter 2014.

Real Year-to-Year Growth. Shown in the accompanying graphs, headline year-to-year real growth in first-quarter 2015 revised to 2.73% [up previously by 2.99%], versus 2.38% in fourth-quarter 2014, 2.70% in third-quarter 2014, 2.59% in the second-quarter 2014 and 1.89% in the first-quarter 2014.

**Quarterly Real Gross Domestic Product
Year-to-Year Change 1q2000-to-1q2015 [ShadowStats, BEA]**



**Quarterly Real Gross Domestic Product
Year-to-Year Change 1947-to-Date [ShadowStats, BEA]**



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 preceding 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 second estimate of first-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was an annualized quarterly contraction of 0.12% (-0.12%) [previously down by 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 unrevised at 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 CPI-U inflation was a contraction of 0.10% (-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). Given the poor-quality of broad economic data available, quarterly reporting of the GNP and GDI traditionally are delayed for release until the second estimate of the GDP (until the third-estimate at the end of the calendar-year). Accordingly, initial estimates for first-quarter 2015 were published today (May 29th) for both series.

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.

Headline, real first-quarter 2015 GNP contracted at annualized pace of 1.40% (-1.40%), versus a headline gain of 1.36% in fourth-quarter 2014. Those numbers are weaker than the respective annualized GDP first-quarter contraction and fourth-quarter growth rates of 0.75% (-0.75%) and 2.22%. Year-to-year annual GDP growth was 2.42% in the first-quarter 2015, versus 2.05% in fourth-quarter 2014.

In nominal terms, the annualized first-quarter contraction was 1.54% (-1.54%), versus a gain of 1.50% in the fourth quarter. Nominal annual growth was 3.32% in the first-quarter 2015, the same level as in fourth-quarter 2014.

There has been a shift in global factor-income trends since third-quarter 2014, likely reflecting some impact from the recent relative strength in the U.S. dollar. The deeper contractions in GNP activity versus the GDP in both the first- and fourth-quarter numbers reflected declining income flows from the rest of the world to the United States, exacerbated by the U.S. making increased income payments to the rest of the world.

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

Headline, annualized, real first-quarter GDI growth was 1.43%, slowing versus a revised 3.71% (previously 3.15%) gain in fourth-quarter 2014. Year-to-year annual growth increased to 3.56% in first-quarter 2015, versus a revised 3.00% (previously 2.86%) in fourth-quarter 2014.

Annualized nominal GDI growth in first-quarter 2015 was 1.30%, versus 3.88% in the fourth-quarter. Year to year nominal growth was 4.48% in first-quarter 2015, versus 4.29% in fourth-quarter 2014.

Also in nominal terms, the statistical discrepancy widened to -328.3 billion dollars in first-quarter 2015, from a revised -231.6 (previously -207.2) billion dollars in fourth-quarter 2014. Highlighting the general insignificance of the GDP reporting, the statistical discrepancy—error—between the GDI and the GDP more than doubled in the last four-quarters from 0.9% of the GDP in second-quarter 2014, to 1.9% of the GDP in first-quarter 2015.

ShadowStats-Alternate GDP. The ShadowStats-Alternate GDP estimate for first-quarter 2015 GDP remained a year-to-year contraction of 1.3% (-1.3%) versus the revised headline first-quarter GDP year-to-year gain of 2.7% [previously up by 3.0%]. 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 0.7% (-0.7%) annualized quarter-to-quarter contraction for first-quarter 2015 most likely was much weaker, deeper contraction, net of all the regular reporting gimmicks. 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 Economic Reporting and Revisions Should Trend Much Weaker versus Overly-Optimistic Expectations; Inflation Will Rise Anew, Following Higher Oil Prices. Although shifting increasingly to the downside, amidst largely-negative reporting and surprises in headline numbers, market expectations for business activity still tend to fluctuate with the latest market hype, with the effect of still holding at overly-optimistic levels. They 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 been hammering elements of the consensus outlook. GDP excesses from 2014 will face downside revisions in the July 30, 2015 GDP benchmark revision, and expectations for headline growth estimates of, or further revisions to first- and second-quarter 2015 should continue shifting to the downside, increasingly into negative territory, shy of upside-jawboning of the data in the press, as discussed in the *Opening Comments* of [Commentary No. 722](#).

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, but dropping by 0.2% (-0.2%) in April 2015. A large jump in gasoline prices for May 2015 and a softening of negative seasonal-adjustments for gasoline promise a headline jump in May 2015 monthly CPI-U inflation, with annual inflation likely pulling at least even with zero.

Significant upside inflation pressures are building, as oil prices rebound, a process that should 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. Again, see the [Commentary No. 722](#) as to market and political pressures on the Bureau of Economic Analysis (BEA) relative to pending, headline GDP reporting. Any meaningful, overt shifts by the BEA in headline GDP reporting methodology, other than those already planned for the July 30, 2015 benchmark revision, would be extraordinary in terms of BEA behavior and are not likely, although some gimmicked, less-negative summary numbers already have been planned for publication.

Beyond the pre-announced gimmicked changes to reporting methodologies of the last several decades, ongoing headline reporting issues are tied largely to systemic distortions of monthly 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, explored in the 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:

Construction Spending (April 2015). The Commerce Department will release its estimate of April 2015 construction spending on Monday, June 1st. Detail will be covered by ShadowStats in *Commentary No. 724* of Wednesday, June 3rd.

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 [MarketWatch early-consensus is for a 0.7% monthly gain], the detail tends to be in down-trending stagnation, net of inflation. Related inflation gained 0.09% month-to-month and 1.72% year-to-year, in April 2015, on a seasonally-adjusted basis, consistent with the headline construction spending number.

U.S. Trade Balance (April 2015) and Annual Benchmark Revision. The Commerce Department and Bureau of Economic Analysis (BEA) will release their estimate of the April 2015 trade deficit on Wednesday, June 3rd. The detail will signal potential further revision to first-quarter 2015 GDP and help set the tone for second-quarter 2015 GDP activity. The benchmark trade revisions—back to 2012—should do much to shape the annual benchmark revisions to the GDP—back to 2012—on July 30th.

Early-market expectations appear to be for a narrowing in the nominal (not-inflation-adjusted) headline April monthly deficit, versus the catch-up surge seen in the March detail that reflected the end of labor disputes at some ports.

Lingering effects from the labor disruptions still may be seen in the April numbers. Where the BEA had some April trade detail available to it for today's GDP revision, the new GDP detail would favor some widening of the headline first-quarter 2015 trade deficit, in revision.

Where some narrowing of the headline April monthly deficit indeed is likely, the nominal deficit in April should remain wider than the current headline \$43.3-billion seasonally-adjusted average for first-quarter 2015. In real (inflation-adjusted) terms, a widening of the monthly deficit relative to the first-quarter

average also is likely, and that would generate a negative signal for real growth in second-quarter 2015 GDP.

In general, look for a wider-than-expected headline April deficit, along with some further deterioration of the March shortfall, in revision, in both nominal and real terms. The broad trend going forward should be for regular monthly and quarterly deteriorations in the real trade deficit.

Employment and Unemployment (May 2015). The Bureau of Labor Statistics (BLS) will release its May 2015 labor data on Friday, June 5th. Both employment and unemployment numbers remain 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 [MarketWatch] are for a slightly slower pace of payroll growth in May 2015, up by 210,000 versus the initial headline gain of 223,000 jobs in April, with May's headline U.3 unemployment rate holding at 5.4%.

As with the narrowing of the headline unemployment rate in recent months and years, any further narrowing of the headline May 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.

Early Expectations Are Close to the Monthly Payroll Bias. As published previously by ShadowStats-affiliate www.ExpliStats.com, in its analysis of the biases built into the BLS's concurrent-seasonal-factor modeling of the April 2015 payroll-employment reporting, the built-in bias trend for May 2015 is for a headline monthly employment gain of 214,000 (see [Commentary No. 717](#)), where the current level of early-consensus expectations effectively has settled.

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.