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Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 755
GDP Revision, Broad Economic Outlook

September 25, 2015

Broad Economic Outlook Has Continued to Weaken;
More-Difficult Times Loom

Minimal Revisions Left the Second-Quarter GDP/GDI Story Intact

Gross Domestic Income (GDI) Again Confirmed Stagnant First-Half Economy,
Largely Consistent with Reporting of Industrial Production and Real-Retail Sales

Surging Gross Domestic Product (GDP) Remained Nonsensical

PLEASE NOTE: The next regular Commentary, *scheduled for Friday, October 2nd will cover September labor conditions and August construction spending.*

Best wishes to all! — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Intensifying Economic Troubles Signal Deepening Downturn. Business activity has continued to falter since late-2014, with the stagnant, non-recovering U.S. economy increasingly turning anew to the downside. The Bureau of Labor Statistics (BLS) reported an initial downside benchmark revision of 208,000 in nonfarm payrolls for its base-month of March 2015. In a normal benchmarking process, such would lead to year-end downside revisions of roughly 400,000 jobs to payroll levels (*Commentary No. 753*). With an otherwise softening trend in monthly payroll growth and continuing issues with the accounting for long-term discouraged workers, labor data are beginning to catch up with broad weakness in a number of basic industries (*Commentary No. 749*). Particularly troubled are retail sales (*Commentary No. 752*), industrial production (*Commentary No. 751*) and the housing industry (*Commentary No. 753* and *Commentary No. 754*). Various patterns of contracting quarterly activity and contracting or rapidly slowing annual activity are sending out traditional signals of imminent recession, or of a recession already in place. New orders for durable goods have continued to indicate further downturn ahead in the manufacturing sector (*Commentary No. 754*).

Separately, out of the Census Bureau, an annual contraction and ten-year low in 2014 real median household income, and broad measures of income variance holding at historic extremes, not only signal deteriorating consumer liquidity conditions, but also tend to foreshadow major economic and financial-market upheavals (*Commentary No. 752*). The generally weak patterns of activity seen in recent quarters, months and weeks likely still are just early indications of increasingly-difficult business conditions and deteriorating economic data in the weeks, months and quarters ahead.

Based on the timing of the collapse in industrial production and initial downturn in real retail sales activity, the unfolding "new" recession remains likely to be clocked from December 2014. ShadowStats continues to contend, however, that the current weakness in broad activity remains nothing more than a renewed down-leg in the broad economic collapse and downturn into 2008 and 2009. There never was an actual recovery from that downturn, as discussed in the *Economic Reality* section.

Today's *Commentary* (September 25th). The balance of these *Opening Comments* provides a summary of reporting of the third estimate, second revision to second-quarter 2015 GDP and related detail. The *Hyperinflation Watch* includes an unrevised *Hyperinflation Outlook Summary*.

The *Week Ahead* previews reporting for September employment and unemployment and for August construction spending.

GROSS DOMESTIC PRODUCT—GDP (Second-Quarter 2015, Third Estimate, Second Revision)—With Negligible Revisions, GDI Remained the Better Economic Indicator. Discussed with last month's first revision to second-quarter GDP (see *Commentary No. 747*), the more relevant national-income reporting appeared to be in the initial headline detail of second-quarter Gross Domestic Income (GDI). That circumstance persists with the third estimate, second revision to second-quarter GDP, and the coincident second estimate, first revision to second-quarter GDI.

Negligible revisions to second-quarter 2015 GDP left headline growth at still-nonsensical levels, running counter to the stagnant economy still indicated in the minimally-revised second-quarter 2015 GDI, the GDP's theoretical and a practical equivalent. As was the case last month, the pattern of GDI stagnation for first-half 2015—not the faux surge in second-quarter GDP—remained more consistent with the better-quality monthly reporting seen in economic series such as industrial production and real retail sales.

First-quarter 2015 GDI rose at annualized real rate of growth of 0.42%, with revised second-quarter growth at 0.71%. First-half 2015 versus second-half 2014 GDI growth was at a revised annualized pace

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of 0.57%. The annualized half-year growth rates are calculated using the Federal Reserve's approach of comparing the second quarter in one half versus the second quarter of the previous half.

First-quarter 2015 GDP rose at an annualized pace of 0.64%, with revised second-quarter growth at an annualized pace of 3.92%. First-half 2015 GDP growth was at a revised annualized pace of 2.26%.

The consumption-side GDP is defined as equivalent to the income-side GDI in the national-income accounts, although they rarely are equal and sometimes vary widely in growth, as seen in the current circumstance. Where both the GDP and GDI basically were flat in first-quarter 2015, the GDI held flat again, but headline GDP surged to growth well above average in second-quarter 2015. GDI activity has been effectively stagnant for both the first and second quarters, for the first-half 2015. That broadly was consistent with the first-half 2015 contraction seen in headline reporting of industrial production, and the first-quarter contraction, second-quarter gain (a stagnant first-half 2015) in real retail sales (see *Commentary No. 751* and *Commentary No. 752*).

Gross Domestic Product (GDP)—Headline Detail. The third estimate of, second revision to second-quarter 2015 GDP reflected a statistically-significant, real (inflation-adjusted), annualized, quarterly headline gain of 3.92%, previously estimated at 3.69% and initially up by 2.32% in the "advance" estimate. Such followed the benchmark revised gain of 0.64% in first-quarter 2015, which had been a contraction of 0.17% (-0.17%), pre-benchmarking.

Headline year-to-year real growth in second-quarter 2015 revised to 2.72% but still was down from 2.88% in first-quarter 2015 (see *Graphs 5* and *6* in the *Reporting Detail*). The latest quarterly year-to-year growth remained below the near-term peak of 3.08%, seen in third-quarter 2010. The current-cycle trough in annual change was in second-quarter 2009, reflecting a year-to-year decline of 4.09% (-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 third estimate of second-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was a revised annualized quarterly increase of 2.13%, versus a benchmarked gain of 0.12% in the first-quarter 2015 IPD. Year-to-year, revised second-quarter 2015 IPD inflation was 0.98%, versus a benchmarked 1.01% annual gain in first-quarter 2015.

For purposes of comparison, headline CPI-U inflation (BLS), seasonally-adjusted, annualized quarter-to-quarter showed a gain of 2.98% in second-quarter 2015, versus a contraction of 3.01% (-3.01%) in first-quarter 2015. Unadjusted, CPI-U inflation showed a year-to-year second-quarter 2015 contraction of 0.04% (-0.04%), versus a 0.10% (-0.10%) year-to-year drop in first-quarter 2015.

Gross National Product (GNP). 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 second estimate of, first revision to second-quarter 2015 GNP showed annualized quarterly real growth of 3.93%, versus a first-quarter 2015 contraction of 0.15% (-0.15%). Year-to-year growth revised to 2.54% in second-quarter 2015 reporting, down from 2.66% in first-quarter 2015.

Gross Domestic Income (GDI). Gross Domestic Income (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.

The second estimate of, first revision to second-quarter 2015 GDI showed an annualized real quarterly growth rate of 0.71%, versus an unrevised 0.42% annualized gain in first-quarter 2015. Headline year-to-year growth was 2.27% in second-quarter 2015, down sharply from an unrevised 3.28% in first-quarter 2015.

Revised Second-Quarter 2015 GDP Growth Distribution. 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 third estimate of annualized quarterly growth in second-quarter 2015 GDP was 3.92% [previously 3.69%, initially 2.32%] versus a first-quarter 2015 annualized real gain of 0.64% [previously a contraction of 0.17% (-0.17%) in the pre-benchmarking environment before July 30th].

The BEA's third guess at real second-quarter GDP growth is detailed in the following aggregation of revisions to contributed growth. The annualized growth number in each sub-category is the additive contribution to the total, headline change in GDP, where 2.42% + 0.85% + 0.18% + 0.46% = 3.91% (a rounding difference). The August 27th *Commentary No. 747* detailed the prior growth-distribution estimate.

Most of the latest round of revisions to second-quarter 2015 GDP growth were minimal, but the upside changes in personal consumption, which more than accounted for the aggregate headline revision, were in areas of limited hard numbers, with traditionally gimmicked and guessed at data such as "health care" and "other."

- ***Consumer Spending Contributed 2.42% [Previously 2.11%, Initially 1.99%] to Second-Quarter GDP Growth; First-Quarter Growth Contribution was 1.19%.*** The upside revisions here largely were in the nebulous healthcare and other-services categories.

- ***Business/Residential Investment Contributed 0.85% [Previously 0.88%, Initially 0.06%] to Second-Quarter GDP Growth; First-Quarter Growth Contribution was 1.39%.*** A downside revision to inventories largely was offset by upside revisions to nonresidential and residential construction.

- ***Net Exports Contributed 0.18% [Previously 0.23%, Initially 0.13%] to Second-Quarter GDP Growth; First-Quarter Growth Subtraction Was 1.92% (-1.92%).*** The minimal revision here reflected somewhat higher imports.

- ***Government Spending Contributed 0.46% [Previously 0.47%, Initially 0.14%] to Second-Quarter GDP Growth; First-Quarter Growth Subtraction was 0.01% (-0.01%).*** There were no meaningful revisions to either federal- or state-and-local-government spending.

Economic Reality. The third estimate of second-quarter 2015 GDP activity showed a minimal, upside revision to headline quarterly growth, to 3.9%, from 3.7%, following a first-quarter gain of 0.6%.

Accordingly, the broad outlook has not changed, and the gist of most of the following text remains along the lines of other recent GDP *Commentaries*. The details and numbers, however, have been updated for the current revisions. Again, discussed in the opening paragraphs of this section, the GDI, which is the theoretical equivalent of the GDP and is just as valid a measure of broad U.S. economic activity, has shown the domestic economy to be stagnant in first-half 2015. More in line with the better-quality monthly economic reporting, that GDI circumstance currently is much closer to reality than is the headline GDP indication.

Discussed in *Commentary No. 739*, which covered the 2015 GDP annual revisions, the annual benchmarkings increasingly are reshaping the GDP-reporting history into a post-2007 collapse pattern of successive multiple dips. By the likely next comprehensive GDP benchmark revision in July 2018, post-2007 historical GDP reporting should be confirming a non-recovering, multiple-dip economic collapse.

That circumstance should encompass the evolving, current downturn in broad, domestic economic activity, discussed previously in *No. 742 Special Commentary: A World Increasingly Out of Balance*. The present "new" recession or multiple-dip downturn still remains likely to be timed from December 2014, although without headline back-to-back contractions of quarterly GDP currently in place, formal recognition of same still could be delayed for months. Recognition of the onset of the December 2007 recession was not formalized until November 28, 2008. Ongoing monthly economic-reporting detail for key series increasingly should confirm the patterns of declining economic activity, which should engender a formal recession call, irrespective of the timing of actual, headline quarterly contractions in real GDP.

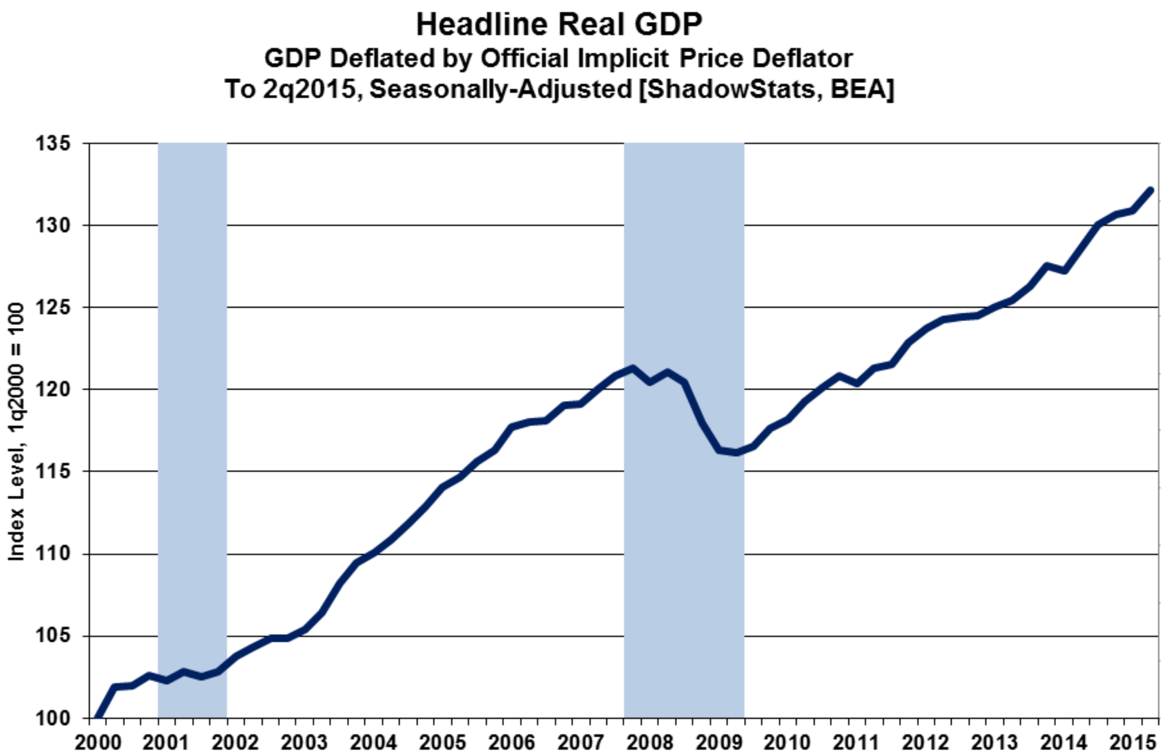
Frequently discussed here, the headline GDP does not reflect properly or accurately the changes to the underlying fundamentals that drive the economy, at present. Fundamental, real-world economic activity shows that the broad economy began to turn down in 2006 and 2007, plunged into 2009, entered a protracted 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 "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 unemployment (see *Commentary No. 749*), monthly real median household income and other consumer measures (see *Commentary No. 752*). This also has been detailed in *No. 742 Special Commentary: A World Increasingly Out of Balance* and *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. 753* and *2014 Hyperinflation Report—Great Economic Tumble – Second Installment*).

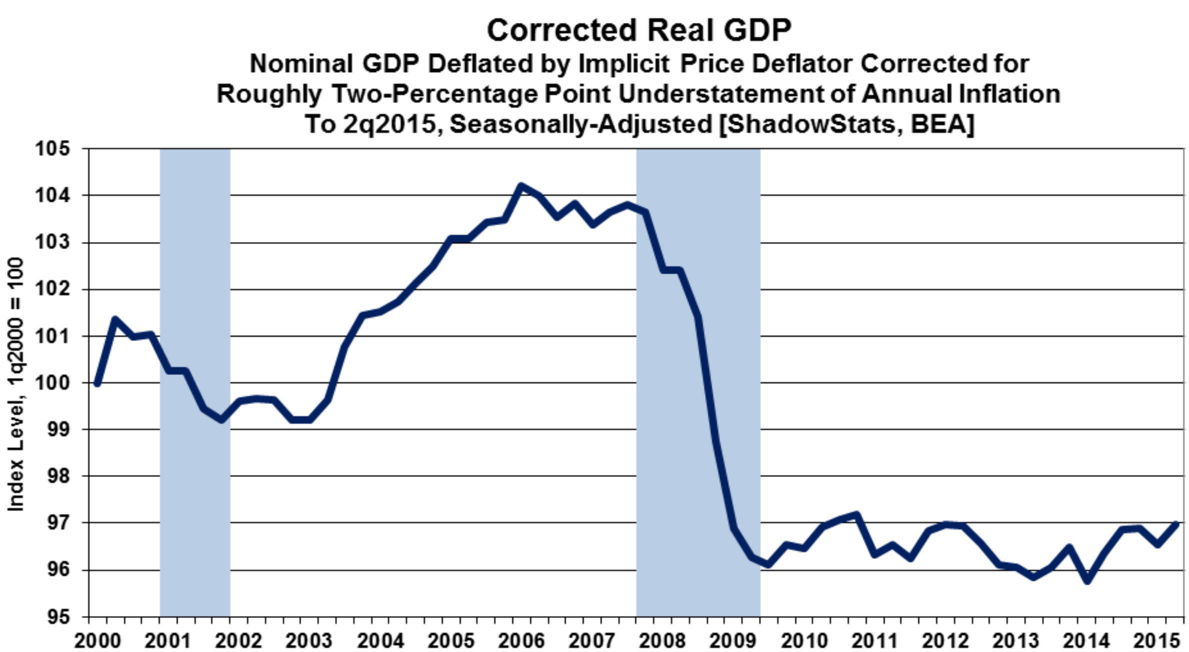
With liquidity-strapped consumers unable to fuel sustainable growth in consumption, a full business recovery could not have taken place since 2009, and a recovery will not be forthcoming until consumer structural income and liquidity problems are resolved.

Official and Corrected GDP. 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 at least partially 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 today's third estimate of second-quarter 2015 GDP.

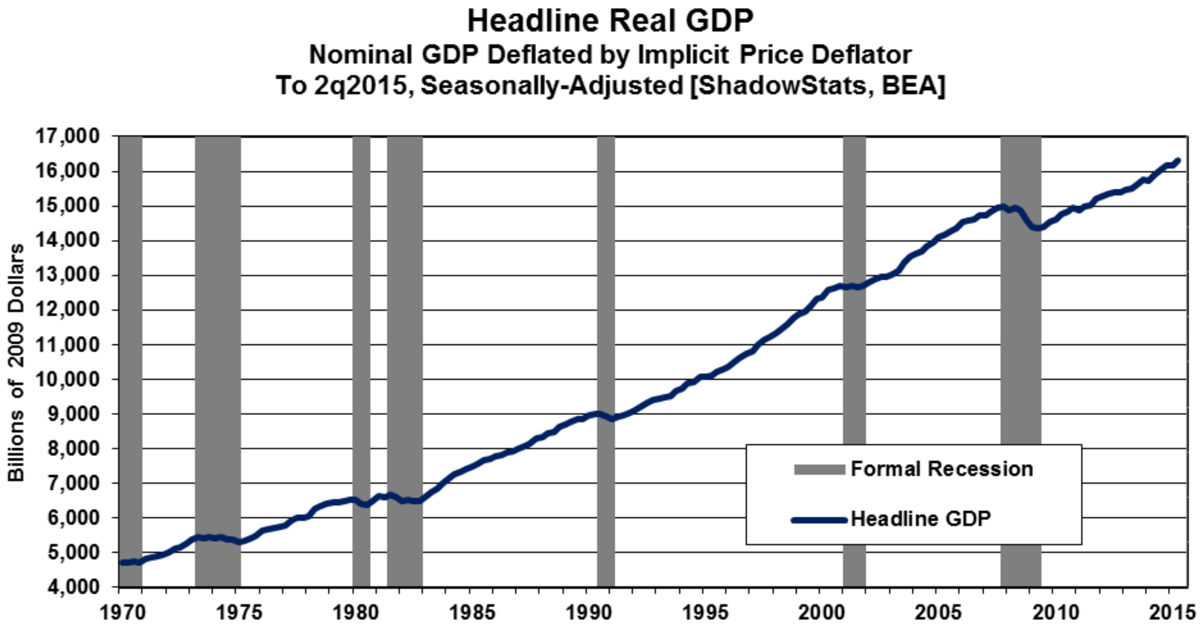
Graph 1: Real GDP Index – Headline Real GDP



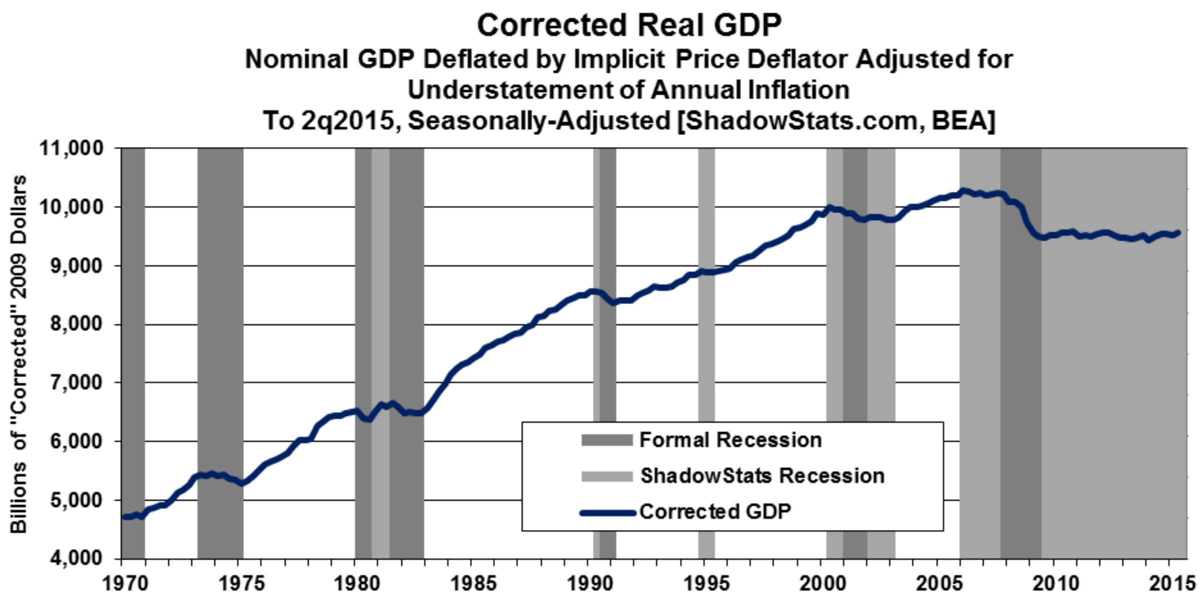
Graph 2: "Corrected" Real GDP Index



Graph 3: Real GDP Index (1970-2015)



Graph 4: "Corrected" Real GDP (1970-2015)



The first set of graphs (2000-to-date) is the one that traditionally has been incorporated in the GDP *Commentaries*. *Graphs 1* and *2* show short-term detail, expressed on an index base where first-quarter 2000 = 100.0. The second set of graphs (*Graphs 3* and *4*) updates the longer-term detail (1970-to-date), expressed in billions of 2009 dollars as used in the headline GDP reporting, and as detailed and published initially in *2014 Hyperinflation Report—Great Economic Tumble* – *Second Installment*. The graphs also show official periods of recession as shaded areas, with ShadowStats-defined recessions indicated by the lighter shading in *Graph 4*, the second graph of the second set.

Shown in the first graph of each set (*Graphs 1* and *3*) 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 pauses or interruptions for second-half 2012 and first-quarter 2014 excepted). Adjusted for official GDP inflation (the implicit price deflator - IPD), the headline second-quarter 2015 GDP currently stands at 9.0% above its pre-recession peak-GDP estimate of fourth-quarter 2007. In contrast, the "corrected" GDP version, in the second graph of each set (*Graphs 2* and *4*), now shows second-quarter 2015 GDP activity down by 6.9% (-6.9%), from its pre-recession peak of first-quarter 2006.

Further, discussed broadly in the second installment of the *Hyperinflation Report*, no other major economic series has shown a pattern of official full economic recovery and meaningful expansion thereafter, consistent with the headline GDP reporting. Such is covered in the recent discussions on industrial production, real retail sales and real durable goods orders respectively in *Commentary No. 751*, *Commentary No. 752* and *Commentary No. 754*. 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."

Again, the second graph in each series (*Graphs 2* and *4*) 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, also as discussed in the *Hyperinflation Reports*.

[The* Reporting Detail *section includes expanded detail of the GDP Revision.]

HYPERINFLATION WATCH

HYPERINFLATION OUTLOOK SUMMARY

Broad Outlook Is Unchanged: Economy Remains in Downturn; Questions Mount on Systemic Stability; Dollar Faces Massive Decline with Ongoing Implications for Hyperinflation. This *Summary* has not been revised from the prior *Commentary*, other than for updated internal references or links and minor language corrections.

Background Documents to this Summary. Underlying this *Summary* are *No. 742 Special Commentary: A World Increasingly Out of Balance* of August 10th, and *No. 692 Special Commentary: 2015 - A World Out of Balance* of February 2, 2015, which 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 two *2014 Hyperinflation Report* installments, however, remain the primary background material for the hyperinflation and economic analyses and forecasts. In terms of underlying economic reality, one other reference is the *Public Commentary on Inflation Measurement*. The regular *Commentaries* also update elements of the general outlook, as circumstances develop.

Primary Summary. The U.S. economy remains in ongoing downturn, while the U.S. dollar still faces a massive decline in the wake of an extraordinary rally seen since June 2014, and in the context of a renewed economic downturn, ongoing domestic fiscal imbalances and ongoing financial-system instabilities. Financial-system concerns likely are the primary reason behind the inability or unwillingness of the Federal Reserve's Federal Open Market Committee (FOMC) to raise interest rates. Those factors have implications for a meaningful upturn in domestic inflation, eventually evolving into a great hyperinflationary crisis.

Indeed, symptomatic of a financial system in serious distress, the FOMC remains unable or unwilling to move decisively on raising interest rates, to move the financial system towards monetary normalcy. Continued inaction or waffling by the Fed has begun to shift the focus and concerns of domestic and global investors away from what appears increasingly to be perpetual moribund economic activity into the areas of systemic instabilities, prospective or otherwise, that are so troubling to the U.S. central bank (see *Commentary No. 750* and *Commentary No. 754*). Fed policy inaction, if anything, has exacerbated the long-term economic stagnation and renewed business downturn, where the quantitative easings always were intended as covert bailouts for the banking system, under the political cover of a weak economy (see for example, the *Monetary Conditions* section in *Commentary No. 749*).

Current fiscal conditions show the effective long-term insolvency of the U.S. government, a circumstance that usually would be met by eventual, unfettered monetization of the national debt and obligations, leading to a hyperinflation. As first estimated by ShadowStats in 2004, such hyperinflation appeared likely by 2020. That time horizon for the hyperinflation forecast was moved to 2014, because of the 2008 Panic, the near-collapse of the financial system, and official (U.S. government and Federal Reserve) responses to same. That hyperinflation forecast remains in place, but it has been adjusted into 2015 or 2016, as discussed in *No. 742* and *No. 692*.

The basic 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 the *2014 Hyperinflation Report—The End Game Begins—First Installment Revised*.

Dollar Circumstance. Discussed in the background documents, the U.S. dollar rallied sharply from mid-2014 into early-2015, and despite some fluttering, into August. Initially, the rally reflected likely covert financial sanctions and oil-price manipulations by the United States, aimed at creating financial stresses for Russia, in the context of the Ukraine situation. Relative U.S. economic strength, and the relative virtuousness of Fed monetary policy versus major U.S. trading partners, were heavily picked-up on and over-estimated by global markets looking to support the dollar.

The still unfolding, weakening domestic-economic circumstance in 2015, in confluence with other fundamental issues, had begun to raise doubts, and more recently to confirm fears 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 a result, the U.S. dollar briefly backed off its highs, with some related upside pressure having been seen on oil prices. Pressures reversed recently, spiking the U.S. dollar—also hitting oil prices anew—with false domestic economic strength being touted by Wall Street, and with some in the Fed indicating that interest rates would be raised in September, irrespective of negative indications on the economy (such did not happen). Coincident, with these events, not-so-covert central-bank actions appear to have driven the price of gold lower, also in the context of mounting global financial-market instabilities.

The U.S. economy remains in contraction (see *Commentary No. 747*, *Commentary No. 751* and the *Opening Comments*), with a variety of key indicators, such as industrial production, real retail sales and revenues of the S&P 500 companies continuing to show recession. Although formal recognition could take months, consensus recognition of a "new" recession should gain relatively rapidly, in tandem with a variety of monthly, quarterly and annual data reflecting the downturn in business activity. When formal recognition comes, timing of the onset of the recession likely will be December 2014.

As market expectations move towards an imminent, new recession, such not only should reduce expectations for a significant tightening in Fed policy, but also should renew expectations for a more-accommodative or newly-accommodative Fed. While such could help to fuel further stock-market mania, any resulting rallies in equity prices should 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 the direction of domestic economic activity, also would 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. These circumstances should unwind what has been the sharp and generally ongoing rally in the U.S. dollar's exchange rate since mid-2014, and the broadly-related selling pressures seen in the gold and silver markets. Further, oil prices should spike anew, along with a sharp reversal in the dollar's strength.

A crash back to recognition of more-realistic domestic-economic circumstances looms, possibly in the weeks and certainly in the months ahead. It should be accompanied by a crash in the U.S. dollar versus major currencies, such as the Swiss franc, Canadian dollar and Australian dollar (currencies with some perceived ties to gold); and 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 risk for fueling further heavy selling of the dollar. Once in heavy downturn, the dollar's gains since June 2014 should reverse fully, pushing the exchange-rate value of the dollar to new historic lows. Again, the nascent currency crisis also has meaningful potential to resurrect elements of the Panic of 2008.

Unexpected economic weakness intensifies 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—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. Fed tightening likely is not now on the horizon until after the 2016 presidential election. Suggestions that all was right again with world were nonsense. The Fed's games likely now will be played out as far as possible, with hopes, once again, of avoiding a financial-system collapse.

Inaction by the FOMC on September 17th was telling. The Panic of 2008 never was resolved, and the Fed increasingly has found that it has no easy escape from its quantitative easing (QE3), which continues; only overt expansion of QE3 ceased. If the Fed does not act quickly to extricate itself from prior actions, QE4 will become the near-term question. Again, despite loud promises now of higher rates before year-end or next year, banking-system issues (not the economy) may keep the "pending" interest rate hike in a continual state of suspension. The economy certainly will supply continuing political cover for the Fed's "inaction," with the U.S. central bank having lost control of the system.

Unexpected economic weakness—a renewed downturn—also savages prospective federal budget deficit prognostications (particularly the 10-year versions). Such 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 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 in the near future, 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 banking system and to the increasingly unstable equity markets. While higher domestic interest rates would tend to act as a dollar prop, a hike in rates also could crash the stock market, as some on Wall Street fear, triggering a round of other systemic problems. Again, there is no happy way out of this for the Fed.

The 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, increasingly against the U.S. currency. That process likely will become dominated by deteriorating global perceptions of stability in U.S. economic activity and political system, and the ability of the Federal Reserve to control its 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 and contracting production, 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. 752*). Sharply-negative economic reporting shocks, versus softening consensus forecasts, remain a heavily-favored, proximal trigger for intensifying the pending dollar debacle.

- ***U.S. government unwillingness to address its long-term solvency issues.*** Those controlling the U.S. government have demonstrated not only a lack of willingness to address long-term U.S. solvency issues, but also the current political impossibility of doing so. The shift in control of Congress 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, with total net obligations of the U.S. government pushing $100 trillion, including the net present value of unfunded liabilities. Still, many in Washington look to continue increasing spending and to take on new, unfunded liabilities. This circumstance now operates in the context of the formal constraint of a renewed debt ceiling that is within a month of being in crisis.

- ***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 2014 monetization process was completed with the Federal Reserve refunding the interest income it earned on the Treasury securities to the U.S. Treasury, but more of that lies ahead. If the Fed does not move soon to boost interest rates, it may be trapped in a renewed expansion of quantitative easing, 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 any new or expanded systemic accommodation in the intensifying 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 fiscal and economic issues remain nil. Issues such as non-recovered, faltering economic activity, the consumer liquidity crisis and the nation's long-range solvency issues should continue to devolve into extreme political crises.

- ***Mounting global political pressures contrary to U.S. interests.*** Downside pressures on the U.S. currency generally are intensifying, 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 global financial instabilities and a quick, significant reversal in the dollar's strength should intensify the "dump-the-dollar" rhetoric rapidly. Consider that China has been selling some of its U.S. Treasury debt holdings to raise cash in for its near-term financial needs. Again, much of the rest of the world also has been backing away from holding U.S. treasury securities. Slack demand for U.S. Treasuries always can be taken up by the Federal Reserve's renewed monetization of the debt.

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, still 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. See Chapter 10, *2014 Hyperinflation Report—Great Economic Tumble* for detailed discussion on approaches to handing the hyperinflation crisis and *No. 742*, for other factors afoot in the current environment.

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REPORTING DETAIL

GROSS DOMESTIC PRODUCT—GDP (Second-Quarter 2015, Third Estimate, Second Revision)—The GDI Remained the Better Economic Indicator. *[Note: The text in the next several paragraphs largely repeats material otherwise in the* Opening Comments*]*. Discussed with last month's first revision to second-quarter GDP (see *Commentary No. 747*), the more relevant national-income reporting appeared to be in the initial headline detail of the second-quarter Gross Domestic Income (GDI). That circumstance persists with the third estimate, second revision to second-quarter GDP, and with the coincident second estimate, first revision to second-quarter GDI.

Negligible revisions to second-quarter 2015 GDP left headline growth at still-nonsensical levels, running counter to the stagnant economy still indicated in the negligible revision to second-quarter 2015 GDI, the GDP's theoretical and a practical equivalent. As was the case last month, the pattern of GDI stagnation for first-half 2015—not the faux surge in second-quarter GDP—remained more consistent with the better-quality monthly reporting seen in economic series such as industrial production and real retail sales.

First-quarter 2015 GDI rose at annualized real rate of growth of 0.42%, with revised second-quarter growth at 0.71%. First-half 2015 versus second-half 2014 GDI growth was at a revised annualized pace of 0.57%. The annualized half-year growth rates are calculated using the Federal Reserve's approach of comparing the second quarter in one half versus the second quarter of the previous half.

First-quarter 2015 GDP rose at an annualized pace of 0.64%, with revised second-quarter growth at an annualized pace of 3.92%. First-half 2015 GDP growth was at a revised annualized pace of 2.26%.

The consumption-side GDP is defined as equivalent to the income-side GDI in the national-income accounts, although they rarely are equal and sometimes vary widely in growth, as seen in the current circumstance. Where both the GDP and GDI basically were flat in first-quarter 2015, the GDI held flat again, but the GDP surged to growth well above average in second-quarter 2015. GDI activity has been effectively stagnant for both the first and second quarters, for first-half 2015. That broadly was consistent with the first-half 2015 contraction seen in headline reporting of industrial production, and the first-quarter contraction, second-quarter gain (a stagnant first-half 2015) in real retail sales (see *Commentary No. 751* and *Commentary No. 752*).

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," and would keep doing so until Commerce got the numbers "right."

Nonetheless, despite all the upside biases and gimmicks built into the GDP reporting, the real world occasionally surfaces in formal GDP estimates. With major monthly economic series, such as retail sales, industrial production and durable goods orders showing regular contractions, underlying reality has become weak enough, once again, for headline GDP or GDI to signal the onset of a "new" recession.

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.*

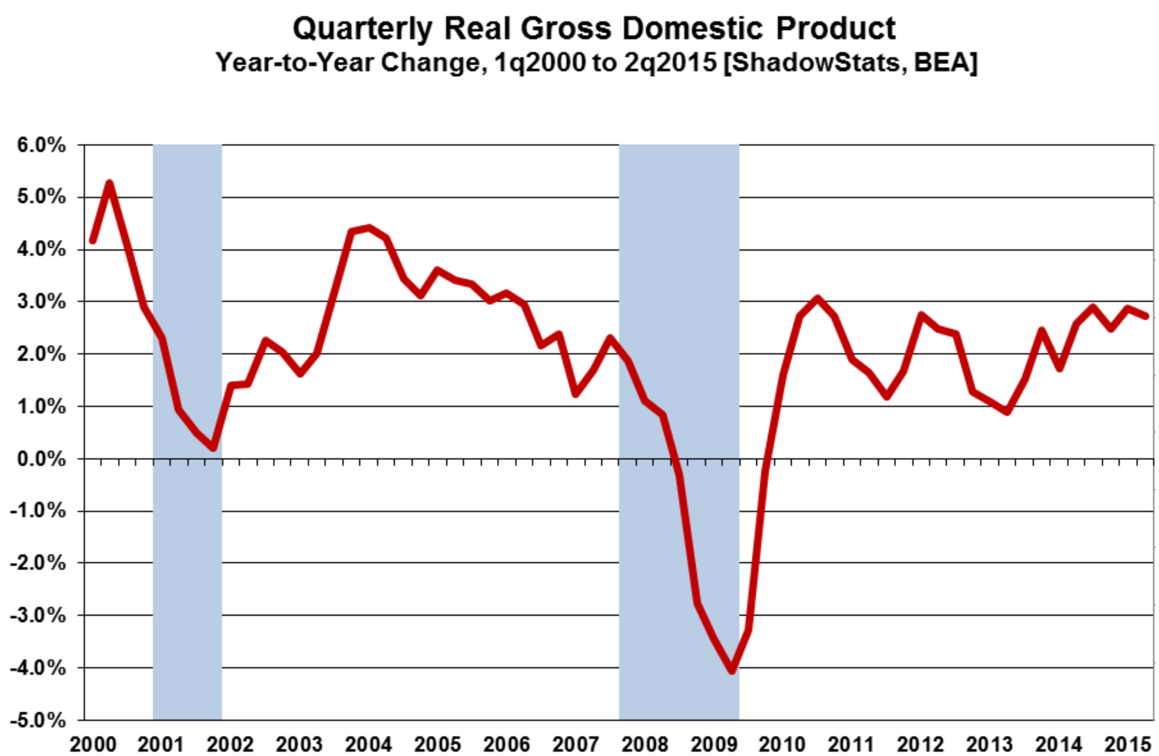
Gross Domestic Product (GDP). Published today, September 25th, by the Bureau of Economic Analysis (BEA), the third estimate of, second revision to second-quarter 2015 GDP reflected a statistically-significant, real (inflation-adjusted), annualized, quarterly headline gain of 3.92% +/- 3.5% (95% confidence interval). Previously reported up by 3.69% [initially up by 2.32%], the second revision to second-quarter GDP growth followed a benchmark revised gain of 0.64% [a pre-benchmarking contraction of 0.17% (-0.17%)] in first-quarter 2015. Distribution detail of the revised second-quarter 2015 GDP growth is outlined in the *Opening Comments*.

Shown in *Graphs 5* and *6*, headline year-to-year real growth in second-quarter 2015 revised to 2.72% [previously up by 2.66%, initially up by 2.32%], but still was down from 2.88% in first-quarter 2015. The latest quarterly year-to-year growth remained below the near-term peak of 3.08% in third-quarter 2010. The current-cycle trough in annual change was in second-quarter 2009, reflecting a year-to-year decline of 4.09% (-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.

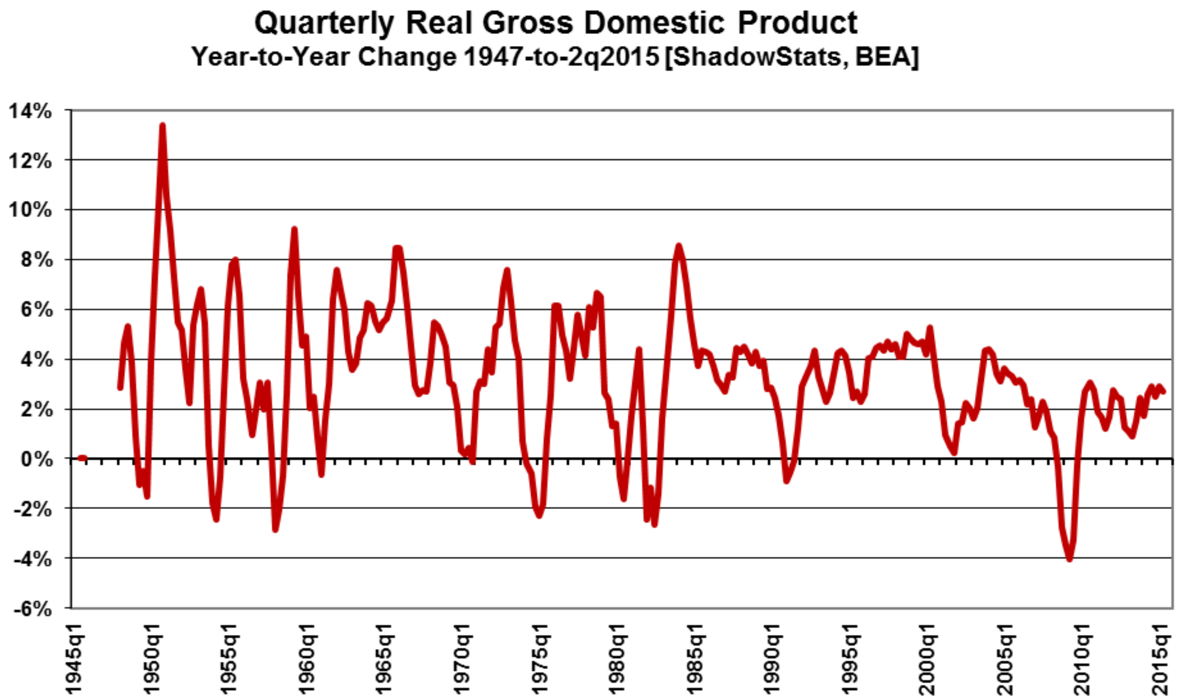
Graph 5 shows current year-to-year quarterly detail, from 2000-to-date, where *Graph 6* shows the same series in terms of its full quarterly history back to 1947.

In terms of first-half 2015 versus second-half 2014, annualized GDP growth revised to 2.26% [previously up by 2.15%].

Graph 5: Quarterly GDP Real Year-to-Year Change (2000-2015)



Graph 6: Quarterly GDP Real Year-to-Year Change (1947-2015)



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 third estimate of second-quarter 2015 GDP inflation, or the implicit price deflator (IPD), was a revised annualized quarterly increase of 2.13% [previously 2.09%, initially 2.04%], versus a benchmarked gain of 0.12% in the first-quarter 2015 IPD.

Year-to-year, revised second-quarter 2015 IPD inflation was 0.98% [previously 0.97%, initially 0.96%], versus a benchmarked 1.01% annual gain in first-quarter 2015.

For purposes of comparison, headline CPI-U inflation (Bureau of Labor Statistics), seasonally-adjusted, annualized quarter-to-quarter showed an annualized gain of 2.98% in second-quarter 2015, versus a contraction of 3.01% (-3.01%) in first-quarter 2015. Unadjusted, year-to-year quarterly CPI-U inflation showed a year-to-year second-quarter 2015 contraction of 0.04% (-0.04%), versus a 0.10% (-0.10%) year-to-year drop in first-quarter 2015.

Gross National Product (GNP). 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 second estimate of, first revision to second-quarter 2015 GNP showed annualized quarterly real growth of 3.93% [previously up by 3.41%], versus a first-quarter 2015 contraction of 0.15% (-0.15%).

Year-to-year growth revised to 2.54% [previously up by 2.41%] in second-quarter 2015 reporting, down from 2.66% in first-quarter 2015.

Gross Domestic Income (GDI). Gross Domestic Income (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.

The second estimate of, first revision to second-quarter 2015 GDI showed an annualized real quarterly growth rate of 0.71% [previously up by 0.63%], versus an unrevised 0.42% [initially up by 0.28%] annualized gain in first-quarter 2015. Headline year-to-year growth was 2.27% [previously up by 2.25%] in second-quarter 2015, down sharply from an unrevised 3.28% [initially 3.25%] in first-quarter 2015.

In terms of first-half 2015 versus second-half 2014, annualized GDI growth revised to 0.57% [previously up by 0.53%].

ShadowStats-Alternate GDP. The ShadowStats-Alternate GDP estimate for second-quarter 2015 GDP remained a year-to-year contraction of 1.2% (-1.2%) versus the unrevised (at the first decimal point) headline second-quarter GDP year-to-year gain of 2.7% [previously 2.3%]. That was against a ShadowStats estimate of a first-quarter 2015 year-to-year contraction of 1.3% (-1.3%), versus the headline first-quarter GDP year-to-year gain of 2.9% (see the Alternate Data tab).

While the annualized, real quarterly growth rate is not estimated formally on an alternate basis, the headline revised 3.9% [previously 3.7%, initially 2.3%] annualized quarter-to-quarter gain in second-quarter 2015 most likely was much weaker, net of all the regular reporting gimmicks. An actual quarterly contraction appears to have been a realistic possibility for inflation-adjusted GDP in most quarters since the official, second-quarter 2009 end to the 2007 recession (see the discussion in the GDI section).

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 (see *Graphs 2* and *4*), updated from *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, here, which reflects reversing additional methodological distortions ("Pollyanna Creep") of recent decades.

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WEEK AHEAD

Economic Reporting Generally Should Trend Much Weaker than Expected; Inflation Will Rise Anew, Along with a Renewed Rebound in Oil Prices. Still in a fluctuating trend to the downside, amidst mixed reporting in headline data, market expectations for business activity nonetheless tend to move with the latest economic hype in the popular media. That general effect holds the consensus outlook at overly-optimistic levels, with current expectations still exceeding any potential, underlying economic reality. Again, the expectations trend generally has continued to soften.

Headline reporting of the regular monthly economic numbers increasingly should turn lower in the weeks and months ahead, along with likely downside or otherwise much weaker-than-expected reporting for at least the next several quarters of GDP (and GDI and GDP) into 2016.

CPI-U consumer inflation—driven lower earlier this year by collapsing prices for gasoline and other oil-price related commodities—likely has seen its near-term, year-to-year low. It turned positive in June 2015, for the first time in six months, notched somewhat higher in July and still somewhat higher in August, despite a headline monthly decline in gasoline prices and a minimal decline in the headline monthly CPI-U.

Upside inflation pressures should continue to build, particularly as oil prices begin to rebound, once again, a process that eventually should accelerate rapidly, along with a pending sharp downturn in the exchange-rate value of the U.S. dollar. These areas, the general economic outlook and longer range reporting trends were reviewed broadly, recently, in *No. 742 Special Commentary: A World Increasingly Out of Balance*, *No. 692 Special Commentary: 2015 - A World Out of Balance* and in the *Hyperinflation Outlook Summary*.

A Note on Reporting-Quality Issues and Systemic-Reporting Biases. Significant reporting-quality problems remain with most major economic series. Beyond the pre-announced gimmicked changes to reporting methodologies of the last several decades, which have tended to understate actual inflation and to overstate actual economic activity, ongoing headline reporting issues are tied largely to systemic distortions of monthly seasonal adjustments. Data instabilities—induced partially by the still-evolving economic turmoil of the last eight-to-ten years—have 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, discussed and explored in the labor-numbers 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*).

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PENDING RELEASES:

Construction Spending (August 2015). The Commerce Department will release its estimate of August 2015 construction spending on Thursday, October 1st. Detail will be covered by ShadowStats in *Commentary No. 756* of Friday, October 2nd.

As usual, the headline monthly changes should not be statistically-significant, while previous data will be subject to large and irregular revisions. Irrespective of almost perpetually-positive market expectations for this series [MarketWatch early-consensus is for a 0.8% monthly gain], the detail tends to continue in down-trending stagnation, net of inflation.

In what will be mixed impact on nominal (not-inflation-adjusted) growth, relative to real (inflation-adjusted) growth, related inflation (PPI – Final Demand Construction) fell by 0.09% (-0.09%) month-to-month, but rose by 1.80% year-to-year for August 2015, on a seasonally-adjusted basis, consistent with the headline construction spending number.

Employment and Unemployment (September 2015). The Bureau of Labor Statistics (BLS) will publish its September 2015 labor data on Friday, October 2nd. Both employment and unemployment numbers remain due for heavily-negative, headline surprises, given the ongoing general weak tone of recent reporting of most other, regular monthly 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). The advance estimate of the 2015 benchmarking for payroll employment indicated a downside revision of 208,000 (-208,000) jobs to the base March 2015 payroll employment levels (see *Commentary No. 753* of September 17th).

Early-market expectations (MarketWatch) are for a somewhat faster pace of payroll growth in September 2015, up by 190,000 jobs versus the initial headline gain of 173,000 jobs in August, with September's headline U.3 unemployment rate expected to hold at 5.1%, versus the 5.1% estimate in August.

As with the narrowing of the headline unemployment rate in recent months and years, any further narrowing of the September 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-September Payroll Gain Expectations Hold Below 200,000 and Below the Implied Monthly Trend. 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 August 2015 payroll-employment reporting, the built-in-bias trend for September 2015 is for a headline monthly employment gain of 252,000 (see *Commentary No. 749*). Where consensus forecasts usually settle-in near the trend level, the early-consensus expectations level is more than 60,000 jobs shy of the trend number, at present. Such suggests the BLS modeling may hold some upside surprises against developing payroll expectations.

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

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