John Williams'

Shadow Government Statistics

Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 891
May Retail Sales, Earnings, Consumer and Producer Price Indices, FOMC

June 14, 2017

With Increasingly Adverse Economic Data, FOMC Hiked the Fed Funds Rate

May 2017 Nominal Retail Sales Fell by 0.3% (-0.3%), Despite a Gimmicked Monthly Sales Boost of 0.2% from Seasonal-Factor Distortions

Headline Real May Retail Sales Sank by 0.13% (-0.13%), Despite a CPI Contraction of 0.13% (-0.13%)

Recession Signal Intensified Sharply

First-Quarter Real Average Weekly Earnings Held in Annual Decline, Along with Back-to-Back Quarterly Contractions; Despite No Growth in May, Weak Inflation Boosted Second-Quarter Real Earnings Trend

Headline CPI-U Inflation Declined by 0.13% (-0.13%) in May 2017, Pulling Annual CPI-U Inflation Lower to 1.87% (Was 2.20%), with CPI-W at 1.78% (Was 2.14%) and ShadowStats at 9.6% (was 10.0%)

May 2017 Annual Final-Demand PPI at 2.36%, Minimally Backed Off a 62-Month High of 2.45% in April

Annual PPI Inflation Boosted by Poor-Quality Theoretical Constructs, Such as Declining Gasoline Prices Spiking Services Inflation

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PLEASE NOTE: The next regular Commentary *scheduled for tomorrow, Thursday, June 15th, will review the details for May 2017 Industrial Production, including an updated assessment of FOMC policies and the U.S. dollar and gold, with a subsequent missive on June 16th covering New Residential Construction (Housing Starts), including an updated review of Consumer Liquidity Conditions*.

Best wishes to all — John Williams (707) 763-5786

Today's *Commentary* (June 14th). In the context of non-recovering economic activity, reviewed in the ***Opening Comments and Executive Summary*** are summary details of May Retail Sales and the May 2017 Consumer and Producer Price Indices (CPI and PPI).

The ***Reporting Detail*** (beginning page 7) provides extended analysis and additional graphics of the new monthly retail sales and inflation detail.

The ***Week, Month and Year Ahead*** (beginning page 23) reviews recent *Commentaries* and updates the previews of May Industrial Production and Housing Starts to be released in the next two days.

OPENING COMMENTS AND EXECUTIVE SUMMARY

An Increasingly Untenable Circumstance for the Fed. As generally expected by the markets, and despite weaker-than-anticipated headline inflation and collapsing retail sales—increasingly "adverse" economic circumstances—the Federal Reserve Board's Federal Open Market Committee (FOMC) hiked the Federal Funds Rate today (June 14th) by another quarter point. Given a likely rapid, further onslaught of deteriorating economic data, the Fed's position increasingly should be viewed as untenable. With mounting economic woes intensifying banking-system liquidity/solvency concerns, FOMC policy should be forced back towards expanded quantitative easing and asset purchases in the not-so-distant future.

The background and policy implications from this afternoon's FOMC announcement will be reviewed in the *Hyperinflation Watch* of tomorrow's *Commentary No. 892*.

Executive Summary: Retail Sales—May 2017—Monthly Nominal Sales Dropped by 0.3% (-0.3%), Real Sales Declined 0.1% (-0.1%), Amidst an Intensifying Recession Signal. In the context of the recent benchmarking, annual real growth in the Retail Sales series had settled back to, and now has dropped below, two-percent, the traditional low-growth signal of imminent economic recession. Where real annual growth had been pushing three percent, pre-benchmarking, May 2017 detail showed real annual growth slowing to 1.9%.

Nominal Retail Sales (Not Adjusted for Inflation)—May 2017. The "advance" estimate of May 2017 Retail Sales showed a nominal monthly contraction of 0.25% (-0.25%) [rounds to 0.3% (-0.3%)] in May 2017, following monthly gains of 0.43% in April and 0.10% in March. Year-to-year, annual retail sales gained by 3.82% in May 2017, following annual gains of 4.47% in April 2017 and 4.81% in March 2017.

Real Retail Sales (Adjusted for Inflation)—May 2017. Net of the seasonally-adjusted headline CPI-U inflation, real seasonally-adjusted month-to-month Retail Sales declined by 0.13% (-0.13%) in May 2017, gained 0.26% in April and 0.39% in March. Real annual Retail Sales growth slowed to 1.91% in May 2017, versus 2.33% in April 2017 and 2.37% in March 2017.

Real Retail Sales Graphs, Corrected and Otherwise. In the *Reporting Detail*, *Graphs 4* and *6* show the level of real retail sales activity (deflated by the CPI-U), while *Graphs 5* and *7* show year-to-year percent change. The apparent "recovery" of headline real retail sales shown in the following *Graph 1* (see also *Graph 4* in the *Reporting Detail*) generally continued into late-2014. Although headline reporting turned down in December 2014, into first-quarter 2015, it turned higher into the third-quarter 2015, slowed to a near-standstill in fourth-quarter 2015 and contracted in first-quarter 2016, with an uptick in second-quarter 2016, renewed slippage into third-quarter 2016, a further uptick in fourth-quarter 2016 and a generally upside-trending fluttering into 2017, turning down in May.

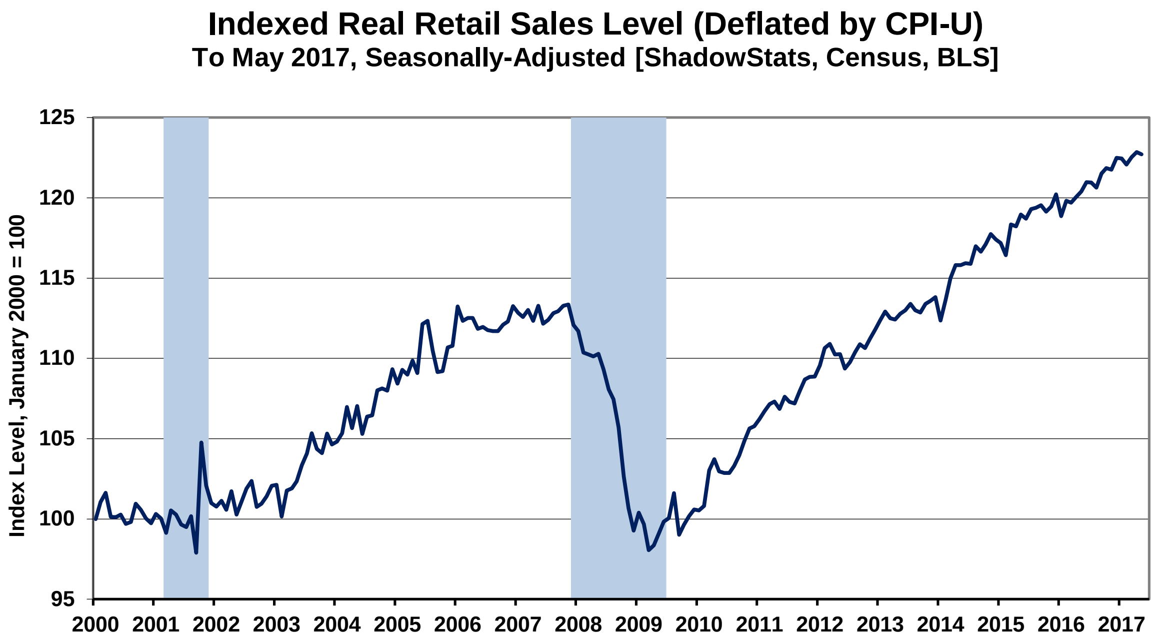
Nonetheless, headline real growth in retail sales continued to be overstated heavily, due to the understatement of CPI-U inflation used in deflating the retail sales series. Discussed more fully in *Chapter 9* of *2014 Hyperinflation Report—Great Economic Tumble* – *Second Installment* and *Public Commentary on Inflation Measurement*, deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

Both of the accompanying graphs are indexed to January 2000 = 100.0 to maintain consistency in the series of graphs related to corrected inflation-adjustment, including the regular plots of the "corrected" industrial production index, the "corrected" new orders for durable goods and the "corrected" GDP (all covered respectively in *Commentary No. 887*, *Commentary No. 889* and *Commentary No. 889*, and also in *No. 859 Special Commentary*).

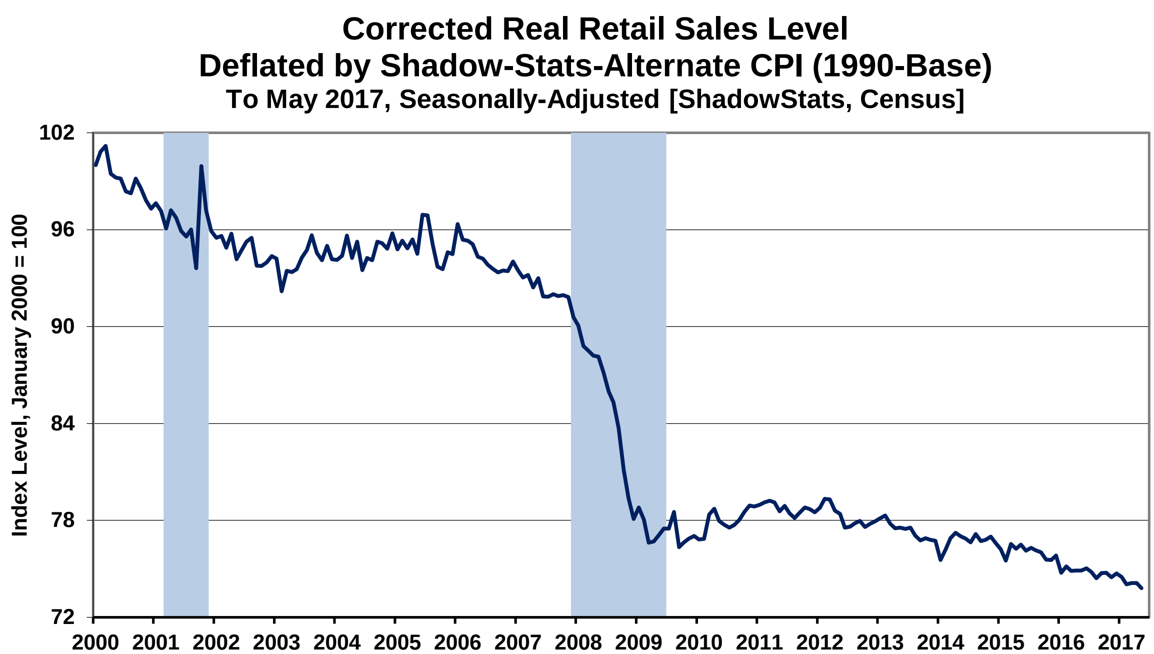
The first graph here reflects the official real retail sales series, except that it is indexed, instead of being expressed in dollars. The plotted patterns of activity and rates of growth are exactly the same for the official series, whether the series is indexed or expressed in dollars, again, as is evident in a comparison of *Graph 1* with *Graph 5* in the *Retail Sales—Nominal and Real* in the *Reporting Detail* section.

Instead of being deflated by the CPI-U, the "corrected" real retail sales numbers—in *Graph 2*—use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation. With the higher inflation of the ShadowStats measure, the revamped numbers show a pattern of plunge and stagnation and renewed downturn. That pattern generally is consistent with consumer indicators such as real average weekly earnings (see *Graph 3* in the next section), faltering consumer liquidity conditions (see *Special Commentary No. 888* and the *ECONOMY* section of *No. 859 Special Commentary*). Extended coverage is found in the *Reporting Detail*.

Graph 1: Headline Real Retail Sales Level, Indexed to January 2000 = 100



Graph 2: "Corrected" Real Retail Sales Level, Indexed to January 2000 = 100



Consumer Price Index (CPI)—May 2017—Inflation Declined by 0.13% (-0.13%) for the Month, Slowed to 1.87% Year-to-Year. Regular reporting in the first-half of the calendar year shows a pattern of downside seasonal-adjustments to monthly CPI growth, from January through June. The headline monthly contraction in May 2017 of 0.13% (-0.13%) and headline gain of 0.17% in April both were depressed, reflecting continued negative seasonal adjustments to gasoline prices. Not adjusted for seasonal factors, as most people experience life, headline CPI-U inflation rose by 0.09% month-to-month in May 2017, versus a headline gain of 0.30% in April.

Unadjusted, year-to-year CPI-U inflation continued to back off its 60-month high of 2.74% in February 2017, having fallen back to 2.20% in April 2017 and to 1.87% in May 2017. The recent inflation surge had been driven by gasoline prices, not by an overheating economy. Still, the current 1.87% year-to-year inflation is not and has not been quite as low as indicated, when considered in the context of traditional CPI reporting and common experience. Moving on top of the unadjusted annual changes to the CPI-U, the ShadowStats-Alternate Inflation Measures showed May 2017 year-to-year inflation at 5.5%, based on 1990 methodologies, and at 9.6%, based on 1980 methodologies.

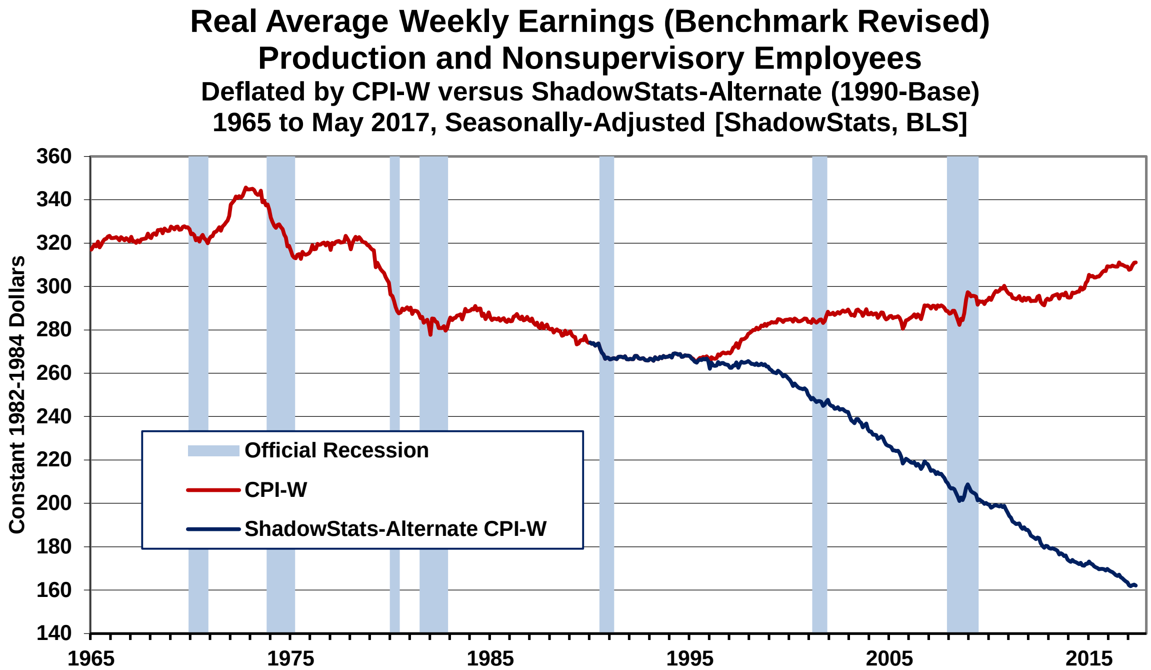
The Consumer Price Index for All Urban Consumers (CPI-U) is the broadest headline consumer-inflation number and is used to adjust numerous economic measures such as Retail Sales for inflation effects as reflected in *Retail Sales—Nominal and Real* of the *Reporting Detail*. The narrower Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) is used for deflating measures such as earnings for production and nonsupervisory employees on private nonfarm payrolls. May 2017 seasonally-adjusted CPI-W declined month-to-month by 0.20% (-0.20%), having gained 0.18% in April. Unadjusted, year-to-year change in the May 2017 CPI-W was 1.78%, down from 2.14% in April 2017.

Real Average Weekly Earnings—May 2017—Month-to-Month Real Earnings Were Flat. In the production and nonsupervisory employees category—the only series for which there is a meaningful history, the regularly-volatile real average weekly earnings were up by 0.04% in May 2017. That was at a much slower pace, virtually flat, versus the monthly gain of 0.44% in April 2017. Year-to-year, the adjusted May 2017 year-to-year change rose to 0.63%, versus 0.54% in April 2017.

Such left first-quarter 2017 in an unrevised 1.13% (-1.13%) annualized real quarterly contraction, with a year-to-year contraction of 0.29% (-0.29%). With initial headline detail in place for April and May 2017, second-quarter 2017 is on early track for annualized real quarter-to-quarter growth of 3.45%, and year-to-year growth of 0.59%.

Graph 3 plots the seasonally-adjusted earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially-weakened CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been in a minimal uptrend for the last two decades (albeit spiked recently by negative headline inflation). Deflated by the ShadowStats (1990-Based) measure, real earnings have been in fairly-regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See the *Public Commentary on Inflation Measurement* for further detail.

Graph 3: Real Average Weekly Earnings, Production and Nonsupervisory Employees, 1965-to-Date



Producer Price Index (PPI)—May 2017—Final Demand PPI Annual Inflation Minimally Backed-Off Its 62-Month High of April. In the context of irregular re-weightings of the component series and poor-quality theoretical constructs, headline "wholesale inflation" or the Producer Price Index was unchanged month-to-month in May 2017. Where the headline PPI Goods inflation dropped by 0.54% (-0.54%) for the month, and Construction Spending inflation rose by 0.09%, the dominant "margins" in the Services sector rose by 0.27%, driven higher by *declining* gasoline prices (see *Services-Side Nonsense* in the *Reporting Detail*). Those combined sectors, generated a month-to-month "unchanged" aggregate PPI Final-Demand (PPI-FD) monthly inflation rate of 0.00% in May 2017, with unadjusted year-to-year inflation easing to 2.36%, versus the 62-month high annual inflation of 2.45% in April 2017.

Nonetheless, other than for April 2017, the annual May 2017 PPI-FD inflation still was at a five-year high. Previously discussed here, the recent spike in annual headline PPI-FD inflation has not reflected an overheating economy, as claimed by some on the FOMC. The headline issue remains energy-price distortions in the last several years that have been rigged heavily through the Federal Reserve's interest-rate jawboning and dollar-propping gimmicks, combined with recent OPEC-supply jawboning. Nonetheless, headline May 2017 energy prices declined or slowed sharply month-to-month and year-to-year, both before and after seasonal adjustment.

Aside from the irregular distortions to the headline detail from estimating wholesale goods inflation in combination with nebulous and inconsistent profit margins in the services sector, regular monthly revisions for January 2017, based on the May 2017 detail, indicated continuing unstable surveying/reporting, particularly in services sector. These inconsistences and a full breakout on monthly and annual PPI inflation detail by major sub-category are found in the *Reporting Detail*.

[The* Reporting Detail *contains extended analysis and graphs.]

REPORTING DETAIL

RETAIL SALES—Nominal and Real (May 2017)

Nominal Sales Dropped by 0.3% (-0.3%), Real Sales Declined 0.1% (-0.1%); Recession Signal Intensified by Slowing Annual Growth. Annual benchmark revisions to Retail Sales on April 26th (*Commentary No. 882*) and subsequent reporting of April Retail Sales on May 12th (*Commentary No. 886*) are incorporated here by reference. In the context of same, the annual rate of real growth in the Retail Sales series had settled back to, now dropping below, two-percent, the traditional low-growth signal of imminent economic recession, where it had been pushing three percent pre-benchmarking. May 2017 detail showed a real annual growth slowing to 1.9%.

Monthly Decline Was Despite Underlying 0.2% Growth Spike from Inconsistent Seasonal Adjustment Factors. For the first time this year, headline monthly numbers appeared to have been skewed significantly by the lack of consistent reporting of seasonally-adjusted retail sales data. As with many series, such as employment and unemployment (see *Headline Distortions from Shifting Concurrent-Seasonal Factors* on page 34 of *Commentary No. 890*) and new orders for durable goods, concurrent seasonal adjustment factors are used with the retail sales. There is nothing wrong with using concurrent seasonal adjustments—where monthly seasonal adjustments are recalculated each-and-every month based on the current headline detail—so long as all data are reported on a consistent, historical basis. Government agencies do not report such detail, however, on a consistent basis.

In the case of retail sales, only the three most recent months (March 2017, April 2017 and May 2017 at present) and two year-ago numbers (April 2016 and May 2016) are revised and reported on a consistent basis. Consistent and related shifts in other prior-activity, though, are not knowable by the public. Where the levels of April 2016 and May 2016 were shifted respectively lower by 0.1% (-0.1%) and higher by 0.1% than previously reported, such was indicative of an out-of-historical-context shift in seasonal factors related to April 2017 and May 2017, with the effect of boosting relatively monthly headline growth by 0.2% on a seasonally-adjusted, but inconsistently-reported basis. That said, headline nominal retail sales declined month-to-month by 0.3% (-0.3%), instead of what otherwise likely would have been a relative drop in the data of 0.5% (-0.5%), again, when viewed based on consistent reporting.

Nominal Retail Sales—May 2017. The Census Bureau reported this morning, June 14th, its “advance” estimate of May 2017 Retail Sales. Headline nominal activity declined by 0.25% (-0.25%) [rounds to 0.3% (-0.3%)] in May 2017, following revised monthly gains of 0.43% [previously 0.39%] in April and 0.10% [previously 0.12%] in March.

That seasonally-adjusted, headline May 2017 decline of 0.25% (-0.25%) +/- 0.59% was not statistically-significant (all confidence intervals are expressed at the 95% level), but the headline April 2017 monthly retail sales gain of 0.43% +/- 0.23% was.

Year-to-Year Annual Change. The May 2017 nominal year-to-year change in Retail Sales showed a statistically-significant increase of 3.82% +/- 0.82%, versus annual gains 4.47% [previously 4.45%] in April 2017 and 4.81% [previously 4.84%] in March 2017.

May Core Retail Sales, Net of Food and Gasoline. Reflecting a real-world environment that in theory should see rising, seasonally-adjusted food prices [up by 0.16% in the month per the Bureau of Labor Statistics (BLS)] and weaker gasoline prices [down by 6.42% (-6.42%) for the month on a seasonally-adjusted basis, per the BLS], seasonally-adjusted grocery-store sales rose month-to-month by 0.06%, with gasoline-station sales down by 2.44% [-2.44%] in May 2017.

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

<u>Version I:</u> Nominal May 2017 versus April 2017 seasonally-adjusted retail sales series—net of total grocery store and gasoline-station sales—declined by 0.08% (-0.08%), versus the official headline aggregate sales decline of 0.25% (-0.25%).

<u>Version II:</u> Nominal May 2017 versus April 2017 seasonally-adjusted retail sales series—net of total grocery store and gasoline-station revenues—declined by 0.07% (-0.07%), versus the official headline aggregate sales decline of 0.25% (-0.25%).

Real Retail Sales—May 2017. The headline detail from today’s (June 14th) coincident release of the May 2017 CPI-U showed a month-to-month decline in seasonally-adjusted inflation of 0.13% (-0.13%), versus a monthly gain of 0.17% in April and a monthly decline of 0.29% (-0.29%) in the March, with year-to-year seasonally-adjusted CPI-U inflation of 1.87% in May 2017, versus 2.20% in April 2017 and 2.38% in March 2017.

Accordingly, real month-to-month retail sales declined by 0.13% (-0.13%) in May 2017, gained 0.26% in April and 0.39% in March. Real annual Retail Sales growth slowed to 1.91% in May 2017, versus 2.33% in April 2017 and 2.37% in March 2017.

<u>Intense Signal of Recession in Annual Real Growth, Shaken Out of Temporary Abeyance by the Annual Benchmark Revisions, Deepened Further in May.</u> During normal economic times, annual real growth in

Retail Sales at or below 2.0% signals an imminent recession. That signal broadly had been in play since February 2015 (the "new" recession likely will be timed from December 2014, based on industrial production, retail sales and other indicators), suggesting a deepening, broad economic downturn.

Where that annual growth recently had moved higher, close to three-percent, ShadowStats had viewed that recession signal as in temporary abeyance. Post-2017 benchmarking, however, annual growth rates shifted lower, towards two-percent, again reviving that recession signal. Again, year-to-year real growth in May 2017 real Retail Sales just sank to 1.91%, from 2.33% in April 2017

First-Quarter 2017 Annualized Real Growth Slowed Sharply versus Fourth-Quarter 2016. Updated for the revisions and latest detail, the first-quarter 2017 annualized quarter-to-quarter real growth in Retail Sales slowed sharply to 1.05% [previously 1.08%], versus an unrevised 3.34% in fourth-quarter 2016, with annual year-to-year real growth for first quarter-2017 at 2.33% [previously 2.43%], versus an unrevised 2.03% in fourth-quarter 2016.

Based solely on April and May headline detail, the second-quarter 2017 early-trend for is for annualized real quarterly growth of 1.40%, with year-to-year quarterly change on track for a gain of 1.91%.

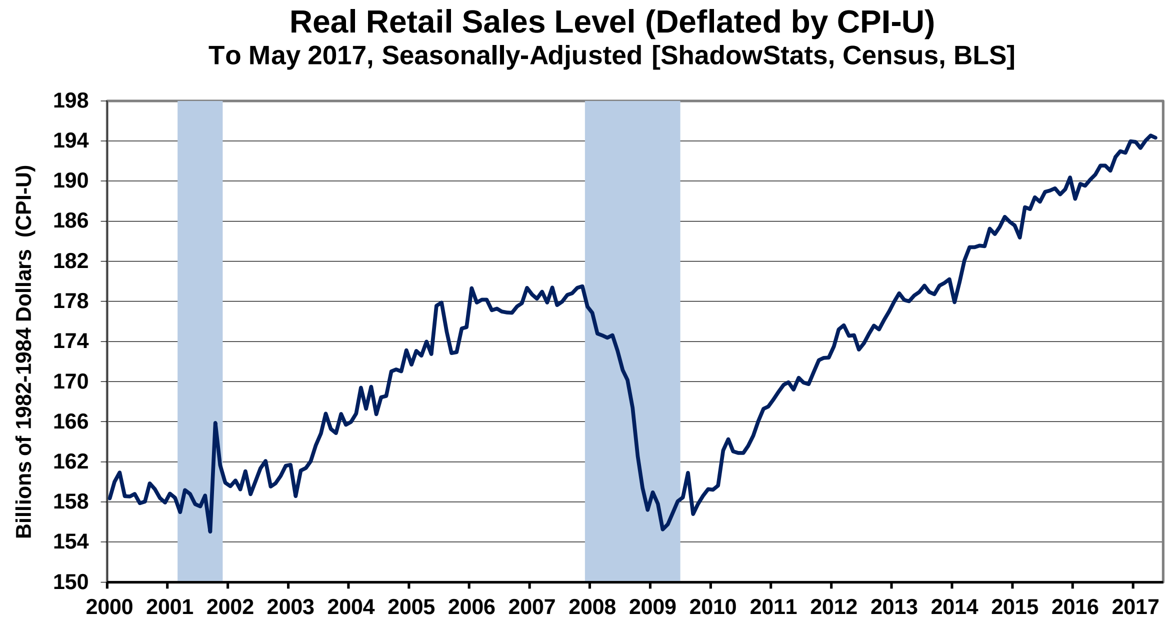
***Structural Liquidity Issues Continue to Impair Retail Sales*.** An extreme consumer-liquidity bind increasingly constrains retail sales activity, as reviewed most recently in the *Consumer Liquidity Conditions* section of *Special Commentary No. 888* and more fully reviewed in the *CONSUMER LIQUIDITY* section of *No. 859 Special Commentary*. Without sustainable growth in real income, and without the ability and/or willingness to take on meaningful new debt in order to make up for the income shortfall, the U.S. consumer remains unable to sustain positive growth in domestic personal consumption, including retail sales, real or nominal. That circumstance—in the last nine-plus years of economic collapse and stagnation—has continued to prevent a normal recovery in broad U.S. economic activity, 70% of which is dependent on personal spending.

As headline consumer inflation generally continues its upside climb in the year ahead, and as overall Retail Sales continue to suffer from the ongoing consumer liquidity squeeze, the real Retail Sales data generally should continue to trend meaningfully lower, in what eventually still should gain recognition as a formal "new" recession.

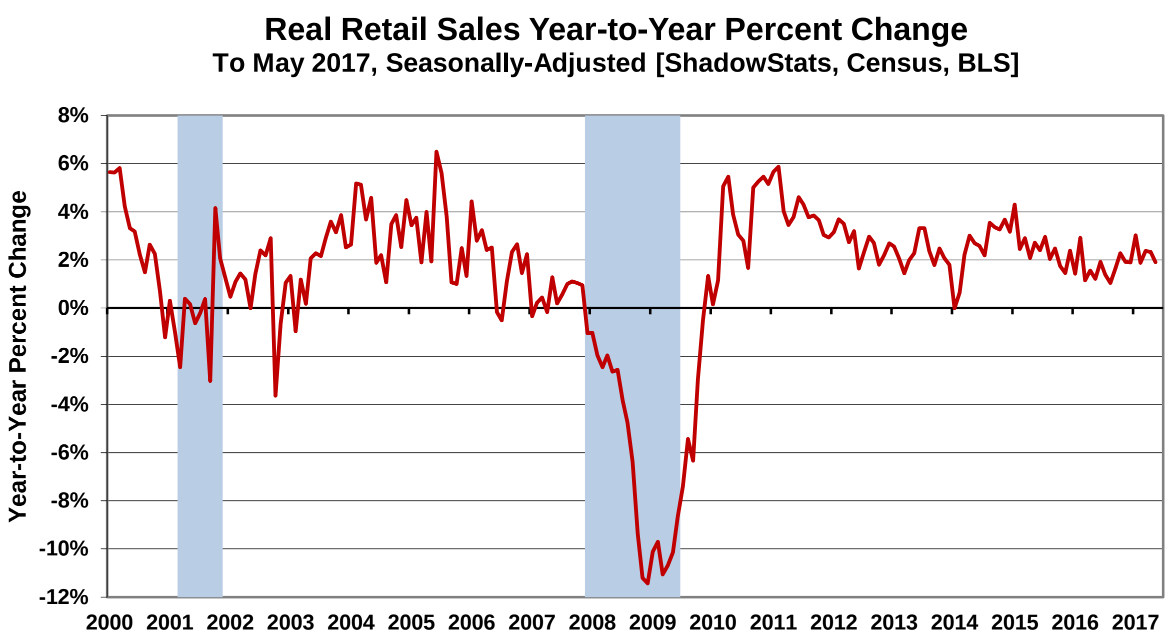
Noted in the *Opening Comments*, *Consumer Liquidity Conditions* will be updated in Friday's *Commentary No. 893*.

Real Retail Sales Graphs. The first of the four graphs following, *Graph 4* shows the level of real retail sales activity (deflated by the CPI-U) since 2000; *Graph 5* shows the year-to-year percent change for the same period. Annual real growth had slowed markedly into fourth-quarter 2015 and 2016, generating an intense recession signal, despite some near-term volatility and revisions with some recent upturn in annual real growth. *Graphs 6* and *7* show the level of, and annual growth in, real retail sales (and its predecessor series) in full post-World War II detail.

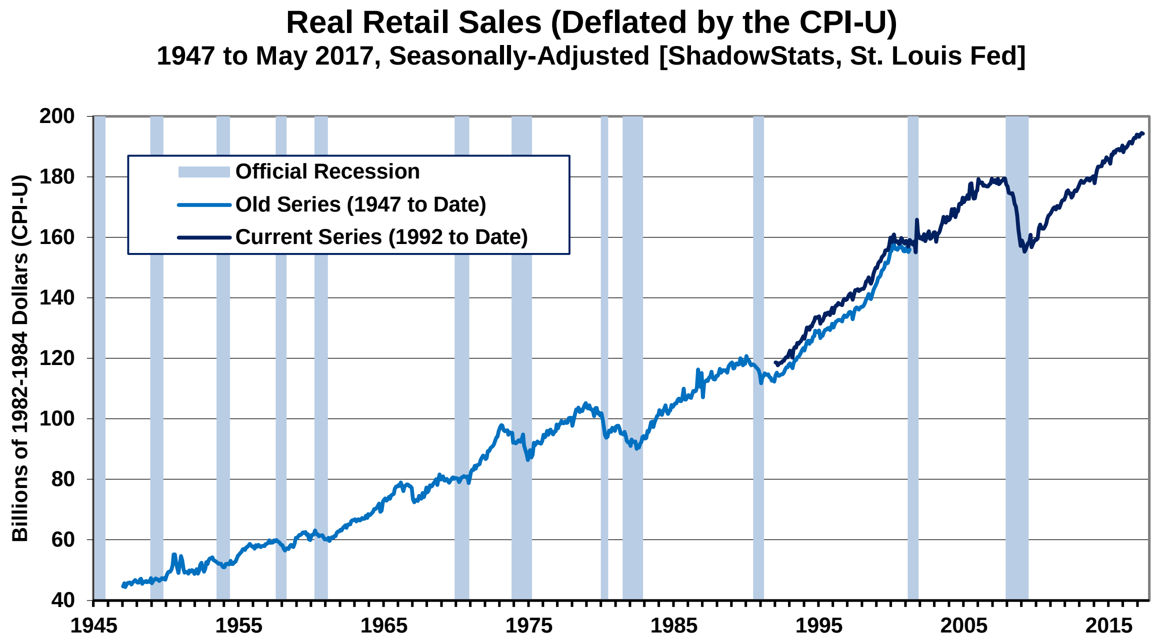
Graph 4: Level of Real Retail Sales (2000 to Date)



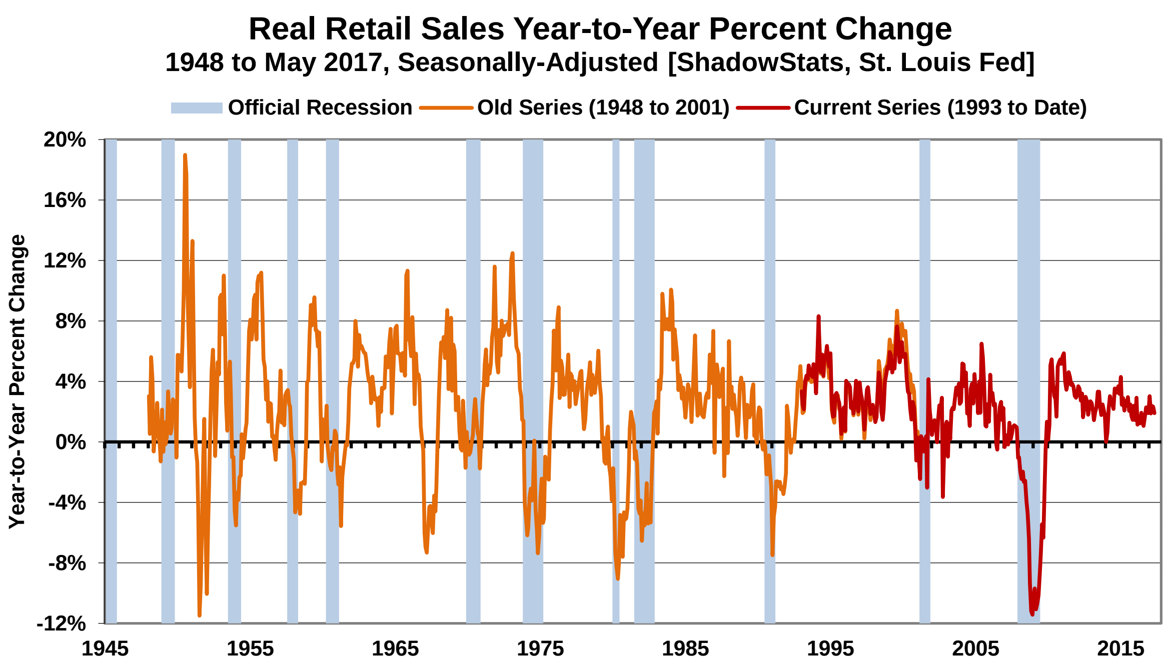
Graph 5: Real Retail Sales (2000 to Date), Year-to-Year Percent Change



Graph 6: Level of Real Retail Sales (1947 to Date)



Graph 7: Real Retail Sales (1948 to Date), Year-to-Year Percent Change



The relative strength seen in the real retail series since the economic trough in 2009 largely has reflected the understatement of the rate of inflation used in deflating the series. Discussed more fully in *Chapter 9* of *2014 Hyperinflation Report—Great Economic Tumble – Second Installment*, deflation by too low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted, real economic growth. Shown in the latest "corrected" real retail sales—*Graph 2* in the *Executive Summary* section—with the deflation rates corrected for the understated inflation reporting of the CPI-U, the recent pattern of real sales activity has turned increasingly negative. The corrected graph shows that the post-2009 period of protracted stagnation ended, and a period of renewed and ongoing contraction began in second-quarter 2012 and continues to date. The corrected real retail sales numbers use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation instead of the CPI-U.

CONSUMER PRICE INDEX—CPI (May 2017)

Headline CPI-U Declined by 0.13% (-0.13%) for the Month, Slowed to 1.87% Year-to-Year. Once again, regular reporting in the first-half of the calendar year has taken its toll on common experience as to headline May 2017 CPI-U inflation, with a regular pattern of downside seasonal-adjustments to month-to-month CPI growth, from January through June. The headline decline in May 2017 CPI-U monthly inflation of 0.1% (-0.1%) [down by 0.13% (-0.13%) at the second decimal point] was weaker than consensus expectations of "unchanged," primarily reflecting continued negative seasonal adjustments to gasoline prices. Not adjusted for seasonal factors, as most people experience life, headline CPI-U inflation rose by 0.09% month-to-month in May 2017.

In contrast to the May 2017 Producer Price Index (PPI), which minimally-backed off its 62-month high in April 2017, unadjusted, year-to-year CPI-U inflation continued to sharply fall off against its 60-month high of 2.74% of February 2017, having fallen back to 2.38% in March 2017, to 2.20% in April 2017 and to 1.87% in May 2017. As with the PPI, what had been the recent inflation surge into February was driven by gasoline prices, not by an overheating economy. Those pressures go both ways and, again, are affected heavily by seasonal adjustments. Consider that in May 2017, the Bureau of Labor Statistics (BLS) reported that gasoline declined by 1.40% month-to-month, unadjusted; that is what people paid at the pump. Seasonally-adjusted, however, headline gasoline prices plunged by 6.42% (-6.42%) month-to-month. Meaningful seasonal adjustments are difficult to work, when most pricing volatility of the last two-to-three years has continued to be largely independent of regular monthly patterns of seasonality.

Separately, with headline annual May 2017 CPI-U inflation at 1.9%, year-to-year inflation is not and has not been quite as low as indicated, when considered in the context of traditional CPI reporting and common experience. Moving on top of the unadjusted annual changes to the CPI-U, the ShadowStats-Alternate Inflation Measures showed year-to-year inflation in May 2017 easing to 5.5% [previously 5.8% in April 2017], based on 1990 methodologies, and to 9.6% [previously 10.0%], based on 1980 methodologies.

Longer-Range Inflation Outlook. Despite U.S. dollar strength of recent years, and what had been accelerating, now faltering dollar strength subsequent to the election and the hype leading into today's quarter-point FOMC rate hike, a tremendous threat to the dollar and systemic liquidity and stability continues, tied to the U.S. Federal Reserve's ongoing inability to resolve fundamentally the 2008 financial collapse, other than having bought limited additional time with its emergency stopgap measures. As will be discussed in the *Hyperinflation Watch* of tomorrow's *Commentary No. 892* (see also *No. 859 Special Commentary*), the latest tightening action was despite continued, unfolding "adverse" economic circumstances, which soon should force the FOMC to revert to expanded quantitative easing, in defense of banking-system solvency problems generated by ongoing economic woes.

Since the 2008 crisis, domestic- and global-banking systems have not been stabilized in a healthy or sustainable manner. Efforts to stimulate a non-recovering U.S. economy, amidst renewed faltering activity, had been nil, up through the advent of the Trump Administration. Given standard lead times, any positive impact from an increasingly-unlikely, economic-stimulus package this year would not have significant effect now until mid-2018, at the earliest, a time lapse fraught with potential disaster created by a still-incapacitated Fed, fighting to the death a battle it already lost in the 2008 panic.

In the context of current economic reporting and signals, faltering economic activity has become increasingly obvious, along with related, increasing stresses on domestic systemic-liquidity and solvency issues, again, pushing the U.S. central bank back towards expanded quantitative easing in the next several months. Such should generate high risk of extreme flight from the U.S. dollar—a massive dollar debasement—threatening an increasingly-rapid upturn in energy and dollar-based commodity inflation, driving headline U.S. inflation much higher.

Compounding the high-risk of a near-term run on the U.S. dollar remains mounting recognition in global markets that the U.S. Federal Reserve and other central banks still have no effective idea as to how to boost current economic activity, how to stabilize global banking-system solvency, or otherwise how to slog their way out of a self-generated quagmire. That circumstance only can be exacerbated by any intensification of systemic-political moves against President Trump by his opposition (see *Special Commentary No. 888*).

Notes on Different Measures of the Consumer Price Index

The Consumer Price Index (CPI) is the broadest inflation measure published by the U.S. Government, through the Bureau of Labor Statistics (BLS), Department of Labor:

*The **CPI-U (Consumer Price Index for All Urban Consumers)** is the monthly headline inflation number (seasonally adjusted) and is the broadest in its coverage, representing the buying patterns of all urban consumers. Its standard measure is not seasonally-adjusted, and it never is revised on that basis except for outright errors.*

*The **CPI-W (CPI for Urban Wage Earners and Clerical Workers)** covers the more-narrow universe of urban wage earners and clerical workers and is used in determining cost of living adjustments in government programs such as Social Security. Otherwise, its background is the same as the CPI-U.*

*The **C-CPI-U (Chain-Weighted CPI-U)** is an experimental measure, where the weighting of components is fully substitution based. It generally shows lower annual inflation rate than the CPI-U and CPI-W. The latter two measures once had fixed weightings—so as to measure the cost of living of maintaining a constant standard of living—but now are quasi-substitution-based. Since it is fully substitution based, the series tends to reflect lower inflation than the other CPI measures. Accordingly, the C-CPI-U is the "new inflation" measure being proffered by Congress and the White House as a tool for reducing Social Security cost-of-living adjustments by stealth. Moving to accommodate the Congress, the BLS introduced changes to the C-CPI-U estimation process with the February 26, 2015 reporting of January 2015 inflation, aimed at finalizing the C-CPI-U estimates on a more-timely basis, and enhancing its ability to produce lower headline inflation than the traditional CPI-U.*

*The **ShadowStats Alternative CPI-U Measures** are attempts at adjusting reported CPI-U inflation for the impact of methodological change of recent decades designed to move the concept of the CPI away from being a measure of the cost of living needed to maintain a constant standard of living. There are two measures, where the first is based on reporting methodologies in place as of 1980, and the second is based on reporting methodologies in place as of 1990.*

CPI-U. The Bureau of Labor Statistics (BLS) reported this morning, June 14th, that headline, seasonally-adjusted May 2017 CPI-U inflation declined month-to-month by 0.1% (-0.1%) [down by 0.13% (-0.13%) at the second decimal point]. That followed an April month-to-month increases of 0.2% [up by 0.17%], monthly decline of 0.3% (-0.3%) [down by 0.29% (-0.29%)] in March, and monthly gains of 0.1% [up by 0.12%] in February, 0.6% [0.55%] in January, and 0.3% [0.26%] in December 2016. The level of the adjusted May 2017 CPI-U also was down by 0.13% (-0.13%) versus the headline January 2017 reading.

Adjusted May 2017 monthly inflation was weakened primarily by negative seasonal adjustments to energy (gasoline) inflation. Where energy-sector inflation rose 0.13% unadjusted, seasonally-adjusted it declined by 2.72% (-2.72%), versus a gain in food-sector inflation of 0.11% unadjusted, a gain of 0.16% adjusted, while the "core" (ex-food and energy) sector rose by 0.08% unadjusted, versus 0.06% adjusted. On an unadjusted basis, monthly May 2017 CPI-U gained 0.09%, versus 0.30% in April, 0.08% in March, 0.31% in February, 0.58% in January and 0.03% in December 2016.

May 2017 seasonal adjustments for monthly gasoline inflation were heavily negative, again, further "depressing" a CPI-U unadjusted monthly decline of 1.40% (-1.40%) in gasoline prices to an adjusted decline of 6.42% (-6.42%). The Department of Energy (DOE) had estimated an unadjusted monthly decline in May gasoline prices of 0.99% (-0.99%).

While early-June 2017 retail gasoline prices (DOE) are running minimally lower month-to-month, versus May, negative seasonal adjustments to June 2017 gasoline suggest a still further, seasonally-adjusted aggregate monthly decline in the June CPI-U.

Major CPI-U Groups. Encompassed by the seasonally-adjusted monthly decline of 0.13% (-0.13%) in May 2017 CPI-U [up by an unadjusted 0.09%], May food inflation rose by a seasonally-adjusted 0.16% [up by 0.11% unadjusted], energy inflation fell by a seasonally-adjusted 2.72% (-2.72%) in May [up by an unadjusted 0.13%], while the adjusted May "core" (ex-food and energy) inflation rate rose by 0.06% [up by 0.08% unadjusted].

Running contrary to FOMC hopes and expectations, core CPI-U inflation showed unadjusted year-to-year inflation of 1.73% in May 2017, down from 1.88% in April 2017, 2.00% in March 2017, 2.22% in February 2017, 2.27% in January 2017 and 2.20% in December 2016.

Year-to-Year CPI-U. Not seasonally May 2017 year-to-year inflation for the CPI-U fell back to 1.9% [1.87% at the second decimal point], from 2.2% [2.20%] in April 2016, 2.4% [2.38%] in March 2017 and from a 60-month high of 2.7% [2.74%] in February 2017, versus 2.5% [2.50%] in January 2017 and 2.1% [2.07%] in December 2016.

Year-to-year, CPI-U inflation would increase or decrease in next month's June 2017 reporting, dependent on the seasonally-adjusted month-to-month change, versus the adjusted, headline gain of 0.20% in June

2016 CPI-U. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for June 2017, the difference in June's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the May 2017 annual inflation rate of 1.87%. Given an early guess of a seasonally-adjusted 0.1% [-0.1%] decline in the monthly June 2017 CPI-U, that would leave the annual CPI-U inflation rate for June dropping to about 1.6%, plus-or-minus, depending on rounding.

CPI-W. The May 2017 seasonally-adjusted, headline CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, declined month-to-month by 0.20% (-0.20%), following a monthly gain of 0.18% in April, a decline of 0.37% (-0.37%) in March, and gains of 0.06% in February, 0.61% in January and 0.29% in December 2016.

On an unadjusted basis, year-to-year CPI-W rose 1.78% in May 2017, versus 2.14% in April 2017, versus 2.35% in March 2017, 2.82% in February 2017, 2.51% in January 2017 and 1.99% in December 2016.

Chained-CPI-U. The headline C-CPI-U is not seasonally adjusted, but it is revised quarterly for the prior year, as was seen with minor downside adjustments to annual inflation in the prior, headline April 2017 reporting. Headline May 2017 C-CPI-U annual inflation came in at 1.73% in May 2017, versus 2.09% in April 2017, 2.28% in March 2017, 2.74% in February 2017, 2.43% in January 2017 and 1.92% in December 2016.

See discussions in the earlier CPI *Commentary No. 721* and in the opening notes in the *CPI Section* of *Commentary No. 699* as to recent changes in the series. More-frequent revisions and earlier finalization of monthly detail broadly have been designed to groom the C-CPI-U series as the new Cost of Living Adjustment (COLA) index of choice for the budget-deficit-strapped federal government, as discussed in the *Public Commentary on Inflation Measurement*.

Caution: Artificially-low inflation numbers estimated by the U.S. Government and used in fields ranging from Social Security COLAs (see the 2017 CPI-W estimate discussion in *Commentary No. 841*) to determining income-tax brackets, have been redesigned in recent decades specifically to help reduce the federal deficit. They are harmfully misleading to anyone using a government CPI estimate as a meaningful cost-of-living measure for guidance on income or investment purposes.

Alternate Consumer Inflation Measures. The ShadowStats-Alternate Consumer Inflation Measures are constructed on top of the unadjusted CPI-U series. Adjusted to 1990 methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—year-to-year annual inflation was roughly 5.5% in May 2017, versus 5.8% in April 2017, versus 6.0% in March 2017, 6.3% in February 2017, 6.1% in January 2017 and 5.7% in December 2016.

The May 2017 ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, was at about 9.6% (9.60% at the second decimal point), versus 10.0% (9.95%) in April 2017, 10.1% (10.14%) in March 2017, 10.5% (10.53%) in February 2017, 10.3% (10.27%) in January 2017 and 9.8% (9.81%) in December 2016. Detail, along with an inflation calculator will be found in the CPI section of the Alternate Data tab of the www.ShadowStats.com home page.

Note: The ShadowStats-Alternate Consumer Inflation Measures largely have been reverse-engineered from BLS estimates of the anticipated impact on annual CPI inflation from various changes made to CPI reporting methodology since the early 1980s, as also incorporated in the CPI-U-RS series. That series provides an official estimate of historical inflation, assuming that all current methodologies were in place going back in time. The changes reflected there are parallel with and of the same magnitude of change as estimated by the BLS, when a given methodology was changed.

The ShadowStats estimates are adjusted on an additive basis for the cumulative impact on the annual inflation rate from the various BLS changes in methodology (reversing the net aggregate inflation reductions by the BLS). The series are adjusted by ShadowStats for those aggregate changes, but the series otherwise are not recalculated.

Over the decades, the BLS has altered the meaning of the CPI from being a measure of the cost of living needed to maintain a constant standard of living, to something that neither reflects the constant-standard-of-living concept nor measures adequately what most consumers view as out-of-pocket expenditures. Roughly five percentage points of the additive ShadowStats adjustment since 1980 reflect the BLS's formal estimate of the annual impact of methodological changes; roughly, two percentage points reflect changes by the BLS, where ShadowStats has estimated the impact not otherwise published by the BLS. For example, the BLS does not consider more-frequent weightings of the CPI series or shifting the nature of retail outlets to be changes in methodology. Yet those changes have had the effect of reducing headline inflation from what it would have been otherwise (See Public Commentary on Inflation Measurement *for further details.)*

Gold and Silver Historic High Prices Adjusted for May 2017 CPI-U/ShadowStats Inflation—

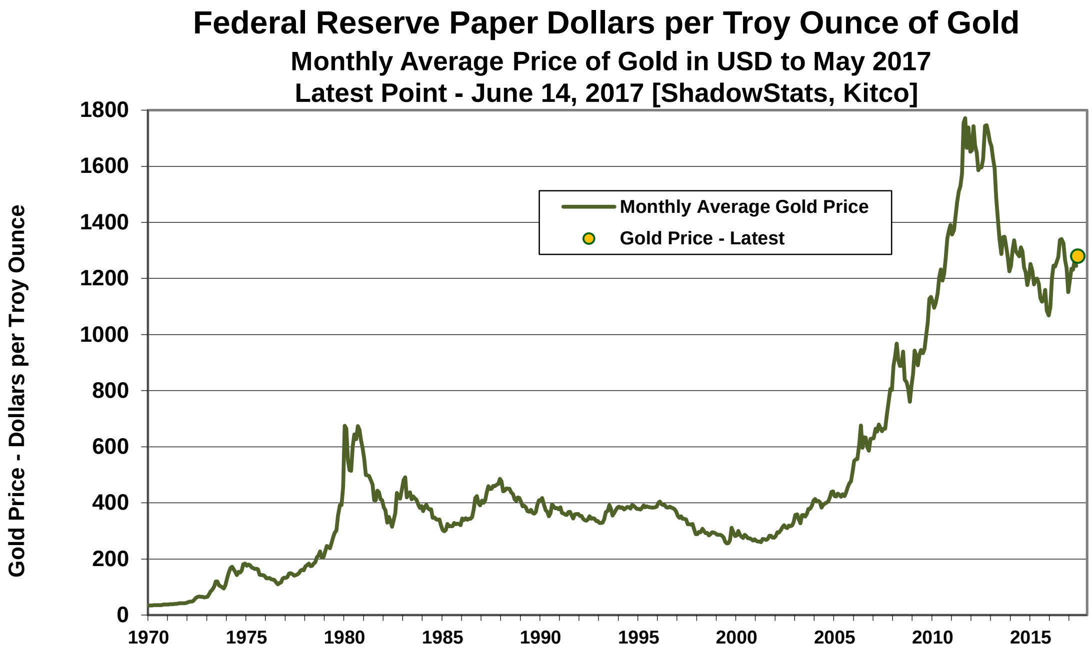
CPI-U: GOLD at $2,674 per Troy Ounce, SILVER at $156 per Troy Ounce
ShadowStats: GOLD at $14,152 per Troy Ounce, SILVER at $823 per Troy Ounce

Despite the September 5, 2011 historic-high gold price of $1,895.00 per troy ounce (London afternoon fix), and despite the multi-decade-high silver price of $48.70 per troy ounce (London fix of April 28, 2011), gold and silver prices have yet to re-hit their 1980 historic levels, adjusted for inflation. The earlier all-time high of $850.00 (London afternoon fix, per Kitco.com) for gold on January 21, 1980 would be $2,674 per troy ounce, based on May 2017 CPI-U-adjusted dollars, and $14,151 per troy ounce, based on May 2017 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (all series here are not seasonally adjusted).

In like manner, the all-time high nominal price for silver in January 1980 of $49.45 per troy ounce (London afternoon fix, per silverinstitute.org)—although approached in 2011—still has not been hit since 1980, including in terms of inflation-adjusted dollars. Based on May 2017 CPI-U inflation, the 1980 silver-price peak would be $156 per troy ounce and would be $823 per troy ounce in terms of the May 2017 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

Shown in *Table 1*, on page 47 of *No. 859 Special Commentary*, over the decades, the increases in gold and silver prices have compensated for more than the loss of the purchasing power of the U.S. dollar as reflected by CPI inflation. They also effectively have come close to fully compensating for the loss of purchasing power of the dollar based on the ShadowStats-Alternate Consumer Price Measure (1980-Methodologies Base).

Graph 8: Monthly Average Gold Price in Dollars (Federal Reserve Notes)



Real Retail Sales—May 2017—Growth Sank to a Real Monthly Contraction of 0.13% (-0.13%), Despite Declining, Headline CPI-U Inflation. Real Retail Sales are detailed in the prior *Retail Sales - Nominal and Real* section.

Real Average Weekly Earnings—May 2017—May Real Earnings Were Flat. The headline estimate for May 2017 real average weekly earnings was published coincident with today's June 14th release of the May CPI-W. In the production and nonsupervisory employees category—the only series for which there is a meaningful history, the regularly-volatile real average weekly earnings were up by 0.04% in May 2017, at a much slower pace, virtually flat, versus the revised monthly gain of 0.44% [previously 0.39%] in April 2017, at a slower pace than the unrevised monthly gains of 0.55% in March 2017, 0.07% in February, versus the 0.47% (-0.47%) contraction in January, which had been the sixth consecutive monthly decline for the series.

Year-to-year, the adjusted May 2017 year-to-year change rose to 0.63%, versus a revised 0.54% [previously 0.49%] gain and annual declines of 0.01% (-0.01%) in March 2017, 0.39% (-0.39%) in February 2017 and 0.46% (-0.46%) in January 2017.

Such left first-quarter 2017 in an unrevised 1.13% (-1.13%) annualized real quarterly contraction, versus a fourth-quarter 2016 contraction of 1.36% (-1.36%), third-quarter 2016 growth of 1.48%, a second-quarter 2016 contraction of 0.11% (-0.11%) and first-quarter 2016 annualized growth of 1.81%.

Year-to-year change in first-quarter 2017 real earnings contracted by an unrevised 0.29% (-0.29%), the first annual or year-to-year quarterly contraction since fourth-quarter 2012, when the real GDP effectively was unchanged quarter-to-quarter. The signal there highlighted financial stresses on the consumer and major downside risk to headline real GDP reporting.

With initial headline detail in place for April and May 2017, second-quarter 2017 was on early track for annualized real quarter-to-quarter growth of 3.45%, and year-to-year growth of 0.59%.

The 2015 rally in real annual income and the subsequent slowdown in latter 2016 were tied directly to the impact of collapsing gasoline prices, and a subsequent rebound in inflation-adjusted income.

While these usually heavily-revised and seasonally-adjusted monthly changes are without much, if any, meaning in the near-term—effectively reporting garbage—over the longer term and quarterly, and particularly the benchmarked trends tend to be of some substance. As with the BLS reporting tied to the nonfarm payrolls, the headline seasonally-adjusted monthly data here are not comparable due to reporting issues with concurrent seasonal factor adjustments (see *Headline Distortions from Shifting Concurrent-Seasonal Factors* on page 34 of *Commentary No. 890*).

Separately, the CPI-W deflated reporting here also is biased versus the CPI-U-deflated series, where the CPI-W—more heavily weighted with gasoline prices—tends to have much deeper, negative headline inflation, with resulting stronger headline, real growth than would be seen with the CPI-U, when gasoline prices are falling, and vice versa. Such was true again, in the May 2017 detail, where lower, seasonally-adjusted gasoline prices generated a headline, seasonally-adjusted CPI-W decline of 0.20% (-0.20%), month-to-month, versus the parallel CPI-U decline of 0.13% (-0.13%).

Found in the *Executive Summary* section, *Graph 3* plots this series, showing the seasonally-adjusted earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-line). When inflation-depressing methodologies of the 1990s began to kick-in, the artificially-weakened headline CPI-W (also used in calculating Social Security cost-of-living adjustments) helped to prop up the reported real earnings. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been in a minimal uptrend for the last two decades (albeit spiked recently by negative headline inflation). Deflated by the ShadowStats (1990-Based) measure, real earnings have been in fairly-regular decline for the last four decades, which is much closer to common experience than the pattern suggested by the CPI-W. See the *Public Commentary on Inflation Measurement* for further detail.

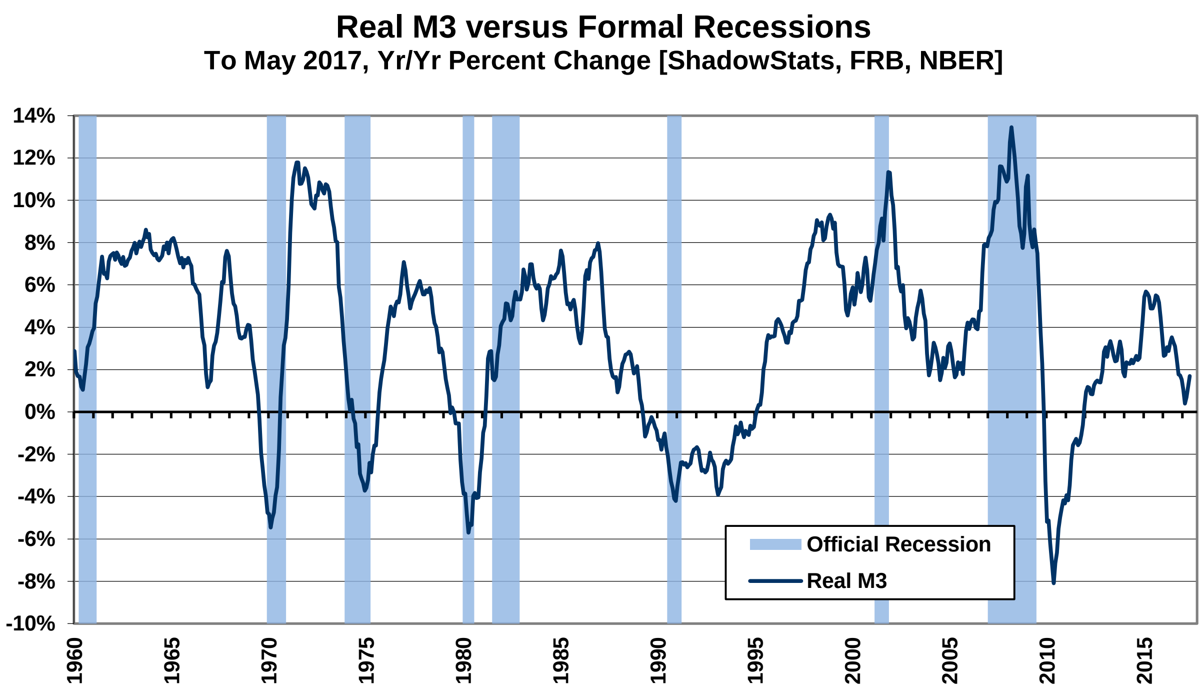
Real (Inflation-Adjusted) Money Supply M3—May 2017—Annual Growth Continued to Rebound. The signal for a double-dip, multiple-dip or simply protracted, ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), recently had been re-triggered/ intensified, but that signal has softened with a continuing, contrary bounce in May 2017. The previous signal had been, and has remained in place, despite real annual M3 growth having rallied into positive territory post-2010.

Shown in *Graph 9*—based on May 2017 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in May 2017 M3 was 1.69%, versus an upwardly revised 1.19% [previously 1.15%] in April 2017, and unrevised annual real gains of 0.69% in March 2017, 0.40% in February 2017 and 1.05% in January 2017, all down from prior peak growth of 5.69% in February 2015. The May gain reflected both an upturn in nominal May 2017 M3 growth, as well as a slowing in headline annual CPI-U growth (see today's CPI-U headline detail and *Commentary No. 890*); earlier-month rebounds primarily reflected declining annual CPI-U inflation.

The recent monthly upticks in annual growth still reflected a likely temporary reversal in the pattern of plunging annual growth, still at levels last seen in plunging growth into the 2009 economic collapse, and at a level always seen going into or already in a recession.

The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first slows sharply, approaches zero and turns negative in a given cycle; the signal is not dependent on the depth of the downturn or its duration. Breaking into positive territory does not generate a meaningful signal one way or the other for the broad economy. The previous "new" downturn signal was generated in December 2009, even though there had been no upturn since the economy purportedly hit bottom in mid-2009. The ongoing issue here confounding the regular signal is that the U.S. economy never has recovered fully from its collapse into 2009 (see [Commentary No. 877](#)). The initial economic downturn never evolved into a meaningful or sustainable recovery. The current level and pattern of real annual M3 growth generally has been followed by annual contraction and recession signal.

Graph 9: Real M3 Annual Growth versus Formal Recessions



Again, when real M3 growth breaks above zero, there is no signal; the signal is generated only when annual growth moves to zero and into negative territory, where it has backed off at present. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of economic series have continued to the present, with significant new softness in recent reporting. Actual post-2009 economic activity has remained at relatively low levels—in protracted stagnation, with no actual recovery (see *Graphs 2* and *3* in the *Executive Summary*, [*Commentary No. 889*](#) and the *ECONOMY* section of [*No. 859 Special Commentary*](#)).

Despite the purported, ongoing recovery shown in headline GDP activity, a renewed downturn in official data is underway that likely still will gain official recognition as a "new" recession, in the months ahead. Underlying reality remains that the collapse into 2009 was followed by a plateau of low-level economic activity—no meaningful upturn, no recovery from or end to the official 2007 recession—and the unfolding "new" downturn remains nothing more than a continuation and re-intensification of the downturn that began unofficially in 2006.

PRODUCER PRICE INDEX—PPI (May 2017)

May 2017 Final Demand PPI Annual Inflation Notched-Off Its Prior 62-Month High in April. In the context of irregular re-weightings of the component series and poor-quality theoretical constructs, headline "wholesale inflation" or the Final Demand Producer Price Index was unchanged in May 2017. Headline PPI Goods inflation dropped by 0.54% (-0.54%) month-to-month, with Construction Spending inflation up by 0.09% and the dominant "margins" in the Services sector rising by 0.27% (driven higher by declining gasoline prices—see *Services-Side Nonsense Detail*). Those combined factors, generated a month-to-month "unchanged" aggregate PPI Final-Demand (PPI-FD) monthly inflation of 0.00% in May 2017, with unadjusted year-to-year inflation easing to 2.36%, versus the 62-month high annual inflation of 2.45% seen in April 2017. Nonetheless, other than for April 2017, headline annual May 2017 PPI-FD inflation still was at a five-year high.

Recent Annual Inflation Spike Not Due to Overheating Economy. With headline annual inflation still at a five-year high, and as previously discussed here, the recent jump in annual headline PPI-FD inflation has not reflected an overheating economy, as claimed by some at the Fed. The headline issue remains energy-price distortions in the last several years that have been rigged heavily through the Federal Reserve's interest-rate jawboning and dollar-propping gimmicks, combined with recent OPEC-supply jawboning. That said, headline May 2017 energy prices declined sharply month-to-month, with slowing annual growth, both before and after seasonal adjustment.

Services-Side Nonsense Detail. The headline monthly PPI Final Demand inflation generally still reflects neither real-world activity, nor common experience, except by possible coincidence. As structured, the monthly wholesale inflation rate remains dominated by the services sector, which remains of negligible common-experience or theoretical value, as discussed in the following *Bulk of Headline PPI Reporting Is of Little Practical Use* section. It also has proven to be highly unstable in its surveying and related reporting. Consider that the monthly PPI detail is subject to revision five months after its initial reporting.

For the January 2017 PPI revision, released with the May 2017 reporting, the headline monthly change revised from an initial month-to-month gain of 0.5% to a monthly increase of 0.6%. With a net neutral impact from the goods side, the revision reflected an upside revision in the dominant services area from a monthly gain of 0.2% to 0.4%, with upside revisions across all the unstable and, again, theoretically-challenged services sector (see *Inflation That Is More Theoretical than Real World*).

Bulk of Headline PPI Reporting Is of Little Practical Use. *[The background text here and in the next subsection is as published previously.]* Beyond the broad issues with general inflation measurement (see *Public Commentary on Inflation Measurement*), indeed the bulk of the PPI is covered by the "services" sector, where inflation is determined largely by shifting profit margins. Discussed in the next subsection, profit-margin inflation estimates generally are handled in a manner counter-intuitive to the more-traditional measurement of inflation in goods and services, otherwise calculated as a measurement of change in prices. Accordingly, the headline detail here increasingly has a limited relationship to real-world activity.

The conceptual differences between goods inflation and services profit margins do not blend well and are not merged easily or meaningfully in the current version of the PPI. While, the dual measures are more meaningfully viewed independently than as the hybrid measure of the headline Producer Price Index Final Demand—ShadowStats separates the analyses of those sectors by sub-category—the aggregate headline series here also is reviewed and covered within the headline reporting conventions of the Bureau of Labor Statistics (BLS).

Inflation That Is More Theoretical than Real World. Effective with January 2014 reporting, a new Producer Price Index (PPI) replaced what had been the traditional headline monthly measure of wholesale inflation in Finished Goods (see *Commentary No. 591*). In the new headline monthly measure of wholesale Final Demand, Final Demand Goods basically is the old Finished Goods series, albeit expanded.

The new otherwise dominant Final Demand Services sector largely reflects problematic and questionable surveying of intermediate or quasi-wholesale profit margins in the services area. To the extent that profit margins shrink in the services sector, one could argue that the resulting lowered estimation of inflation actually is a precursor to higher inflation, as firms subsequently would move to raise prices, in an effort to regain more-normal margins. In like manner, in the circumstance of "increased" margins—due to the lower cost of petroleum-related products not being passed along immediately to customers—competitive pressures to lower margins would tend to be reflected eventually in reduced retail prices (CPI). The oil-price versus margin gimmick works both way. In times of rapidly rising oil prices, it mutes the increase in Final Demand inflation, in times of rapidly declining oil prices; it tends to mute the decline in Final Demand inflation.

The current PPI series remains an interesting concept, but it appears limited as to its aggregate predictive ability versus general consumer inflation. Further, there is not enough history available on the new series (just seven years of post-2008-panic data) to establish any meaningful relationship to general inflation or other economic or financial series.

May 2017 Headline PPI Detail. The Bureau of Labor Statistics (BLS) reported June 13th, that the seasonally-adjusted, month-to-month, headline Producer Price Index Final-Demand (PPI-FD) inflation for May 2017 was unchanged at 0.00%. That was against a monthly gain of 0.54% in April, a contraction of 0.09% (-0.09%) in March, and a revised gain of 0.18% [previously 0.27%] in February, due to the five-month revision to January 2017, which now shows a monthly gain of 0.63% [previously 0.54%].

On a not-seasonally-adjusted basis—all annual growth rates are expressed unadjusted—year-to-year PPI-FD inflation in May 2017 was up by 2.36%, versus 2.45% in April 2017, 2.28% in March 2017, 2.19% in February 2017, and a revised 1.73% [previously 1.64%] in January 2017.

For the three major subcategories of May 2017 PPI-FD, headline monthly Goods inflation declined by 0.54% (-0.54%), Services "inflation" (profit margins) gained by 0.27% and Construction inflation rose by 0.09%, with respective unadjusted annual growth rates of 2.88%, 2.07% and 1.05%.

Final Demand Goods (weighted at 33.81% [previously 33.84%] of the Aggregate Index). Running somewhat in parallel with the old Finished Goods PPI series, headline month-to-month Final Demand Goods inflation in May 2017 declined by 0.54% (-0.54%), having gained 0.45% in April and having declined 0.09% (-0.09%) in March. There was negative impact on the aggregate goods headline reading from underlying seasonal-factor adjustments. Not-seasonally-adjusted, May inflation declined month-to-month by 0.27% (-0.27%).

Unadjusted, year-to-year goods inflation in May 2017 showed an annual gain of 2.88%, following gains of 4.03% in April 2017 and 3.96% in March 2017.

Headline seasonally-adjusted monthly changes by major components of the May 2017 Final Demand Goods:

- "Foods" inflation (weighted at a revised 5.40% [previously 5.43%] of the total index) declined by 0.17% (-0.17%) month-to-month in May 2017, having gained month-to-month by 0.95% in April and 0.87% in March. Seasonal adjustments were negative for the May headline change, which was up by 0.26% unadjusted. Unadjusted and year-to-year, annual May 2017 foods inflation rose by 0.95%, having gained 1.48% in April 2017 and 0.26% in March 2017.
- "Energy" inflation (weighted at a revised 5.50% [previously 5.49%] of the total index) declined month-to-month by 3.03% (-3.03%) in May 2017, having gained by 0.81% in April and having declined by 2.87% (-2.87%) in March. Seasonal adjustments were negative, with unadjusted monthly energy inflation down by 1.82% (-1.82%) in the month. Unadjusted and year-to-year, May 2017 energy prices gained 7.65%, versus 14.34% in April 2017 and 15.18% in March 2017.
- "Less foods and energy" ("Core" goods) monthly inflation (weighted at a revised 22.91% [previously 22.92%] of the total index) rose by 0.09% in May 2017, having gained 0.27% in April and 0.36% in March. Seasonal adjustments were positive for monthly core inflation, with unadjusted monthly inflation unchanged at 0.00%. Unadjusted and year-to-year, May 2017 showed an annual gain of 2.17%, versus 2.26% in April 2017 and 2.27% in March 2017.

<u>Final Demand Services (weighted at a revised 64.12% [previously 64.09%] of the Aggregate Index).</u> Headline monthly Final Demand Services inflation rose by 0.27% in May 2017, versus a gain of 0.44% in April and a decline of 0.09% (-0.09%) in March. The overall seasonal-adjustment impact on headline May services inflation was positive, with an unadjusted monthly gain of 0.18%. Year-to-year, unadjusted May 2017 services rose by 2.07%, versus annual gains of 1.80% in April 2017 and 1.53% in March 2017.

The headline monthly changes by major component for May 2017 Final Demand Services inflation:

- "Services less trade, transportation and warehousing" inflation, or the "Other" category (weighted at an unrevised 38.87% of the total index), declined month-to-month by 0.09% (-0.09%) in May 2017, having gained 0.81% in April and having declined by 0.09% (-0.09%) in March. Seasonal-adjustment impact on the adjusted May detail was neutral, where the unadjusted monthly reading also showed a decline of 0.09% (-0.09%). Unadjusted and year-to-year, May 2017 "other" services inflation was up by 2.18%, having gained 2.09% in April 2017 and 1.45% in March 2017.
- "Transportation and warehousing" inflation (weighted at a revised 4.99% [previously 4.94%] of the total index) declined by 0.52% (-0.52%) month-to-month in May 2017, having gained 0.69% in April and having declined by 0.17% (-0.17%) in March. Seasonal adjustments were positive for the headline May reading, versus an unadjusted monthly decline of 0.77% (-0.77%). Unadjusted and year-to-year, May 2017 transportation inflation was up by 2.22%, having risen by 2.20% in April 2017 and 1.31% in March 2017.

- "Trade" inflation (weighted at a revised 20.26% [previously 20.28%] of the total index) rose month-to-month in May 2017 by 1.14%, reflecting surging margins for those selling fuel at declining prices, having declined by 0.35% (-0.35%) in April and 0.09% (-0.09%) in March. Seasonal adjustments had a positive impact here, where the unadjusted monthly change was a gain of 0.96%. Unadjusted and year-to-year, May 2017 trade inflation jumped to 2.03%, versus 1.06% in April and 1.50% in March 2017.

Final Demand Construction (weighted at a revised 2.07% [previously 2.08%] of the Aggregate Index). Although a fully self-contained subsection of the Final Demand PPI, Final Demand Construction inflation receives no formal headline coverage. Month-to-month construction inflation rose by 0.09% in May 2017, having gained 0.43% in April and 0.17% in March. The impact of seasonal factors on the May reading was neutral, as usual, where the unadjusted monthly gain also was 0.09%. The issues here are a combination of monthly headline cost changes along with a quarterly estimate of contractor profit-margin changes that have little connection to real-world activity. The latter circumstance was addressed in *Commentary No. 829* of September 2, 2016.

On an unadjusted basis, year-to-year construction inflation rose by 1.05% in May 2017, versus 0.96% in April 2017 and 1.50% in March 2017. Private surveys and other government estimates tend to show much higher construction-related inflation than is reported in the PPI, by an order of magnitude of a couple of hundred basis points, such as reflected in the privately-published Building Cost and Construction Cost Indices [Dodge Data and Analytics (McGraw Hill) *Engineering News-Record*] and in construction-related price deflators in the National Income Accounts, such as the Gross Domestic Product (GDP). Discussed in *Commentary No. 829*, ShadowStats has constructed a Composite Construction Deflator (CCD) now used by ShadowStats in deflating the Census Bureau's monthly estimates of Construction Spending Put in Place in the United States.

PPI-Inflation Impact on Pending Reporting of May 2017 New Orders for Durable Goods. As to the upcoming reporting of May 2017 New Orders for Durable Goods, monthly inflation (reported only on a not-seasonally-adjusted basis) for new orders for manufactured durable goods in May 2017 was unchanged at 0.00%, versus monthly gains of 0.24% in both April and March. Year-to-year annual inflation backed off to 1.75% in May 2017, versus 1.87% in April 2017 and 1.75% in March 2017. May 2017 durable goods orders (both nominal and real) will be reported and calculable on June 26th, with coverage in the ShadowStats *Commentary No. 895* of that date.

WEEK, MONTH AND YEAR AHEAD

Rapid Economic Weakening, Stagnation and Downturn Still Should Compromise Fed Policies, Pummeling the U.S. Dollar and Boosting the Price of Gold. *[Please Note: Other than for the* Pending Economic Releases *section and this paragraph, text here has not been changed meaningfully from prior*

Commentary No. 890 and Special Commentary No. 888.*]* The impact and implications of today's quarter-point rate hike by the Federal Reserve's Federal Open Market Committee (FOMC) will be reviewed more fully in the *Hyperinflation Watch* of tomorrow's (June 15th) *Commentary No. 892*. As discussed in the opening section of the CPI coverage in the *Reporting Detail*, the tightening was despite a rather rapid escalation in the development of "adverse economic circumstances" that should push the FOMC back to expanded quantitative easing in the near future, with severely negative implications for the U.S. dollar and related domestic inflation, and coincident upside pressures on gold and silver prices.

Otherwise, recent benchmark revisions to the Trade Deficit (see *Commentary No. 890*), Industrial Production (*Commentary No. 877*), Manufacturers' Shipments (*Special Commentary No. 888*), Housing Starts (*Commentary No. 887*) and Retail Sales (*Commentary No. 882*) broadly have confirmed that recent historical activity has been overstated and/or that it is turning down anew, despite near-term improvement in some headline details, such as the May unemployment rate and April industrial production. Reporting patterns likely will continue to weaken in the next month or so, which should trigger anew financial-market concerns as to the direction of pending Fed policy actions. Adding uncertainty are risks of political surprise, as discussed in *Special Commentary No. 888*. Otherwise, the broad outlook has not shifted.

In the context of the *Opening Special Comments* of *Special Commentary No. 885*, and as discussed in the *Opening Comments* of *Commentary No. 883*, the still-unfolding downshift in economic expectations increasingly should move market expectations for Federal Reserve policy away from rate hikes and the normalization of the Fed's balance sheet, towards renewed quantitative easing. The problem for the U.S. central bank remains that faltering domestic economic activity stresses banking-system solvency. Aside from formal obligations of the Fed to maintain healthy domestic economic and inflation conditions, the central bank's primary function, in practice, always has been to keep the banking system afloat. The near-absolute failure of that function in 2008 remains the primary ongoing and unresolved problem for the Fed, and it is one of the ongoing primary issues preventing the return of U.S. economic activity to normal functioning.

The outlook for future FOMC activity was updated in the *Hyperinflation Watch* of *Commentary No. 886*, and remains otherwise as reviewed in the *Opening Comments* and *Hyperinflation Watch* of *Commentary No. 880*, and as previously reviewed in *Commentary No. 873*. The circumstances and outlook remain as broadly outlined in *No. 859 Special Commentary*.

As reflected in common experience, actual U.S. economic activity generally continues in stagnation or downturn, never having recovered fully its level of pre-economic-collapse (its pre-2007-recession peak). While the latest headline GDP shows economic expansion of 12.5% since that series purportedly recovered its 2007-pre-recession high in 2011, no other "recovered" economic series has come close to showing that expansion either in terms of magnitude or in the purported brevity of the depression. Most of the better-quality series have remained in continuing, not-recovered status, in a period of protracted downturn that now rivals that of the Great Depression (see *Commentary No. 887* and *Commentary No. 869*). With intensifying signals, near-term economic woes, the FOMC soon should come under pressure to shift policies, once again, reverting to some form of quantitative easing, in an effort to address related, intensifying solvency risks in the domestic banking system.

Discussed in *No. 859 Special Commentary*, the Trump Administration continues to face extraordinarily difficult times, but has a chance to turn the tide on factors savaging the U.S. economy and on highly negative prospects for long-range U.S. Treasury solvency and stability and strength in the U.S. dollar. Any forthcoming economic stimulus faces a nine-month to one-year lead-time, once in play, before it meaningfully affects the broad economy. Delays from political discord continue to push targeted programs back in time. Needed at the same time are a credible plan for bringing the U.S. long-term budget deficit (sovereign solvency issues) under control, and action to bring the Federal Reserve under control and/or to reorganize the banking system. These actions broadly are necessary to restore domestic-economic and financial-system tranquility (see *No. 859*), but they will not happen without the cooperation of Congress.

Prior General Background. *No. 859 Special Commentary* updated near-term economic and inflation conditions, and the outlook for same, including the general economic, inflation and systemic distortions evolving out of the Panic of 2008 that have continued in play, and which, again, need to be addressed by the new Administration in the immediate future (see also the *Hyperinflation Watch* of *Commentary No. 862* and *Commentary No. 869*).

Contrary to the official reporting of an economy that collapsed from 2007 into 2009 and then recovered strongly into ongoing expansion, underlying domestic reality remains that the U.S. economy started to turn down somewhat before 2007, collapsed into 2009 but never recovered fully. While the economy bounced off its 2009 trough, it entered a period of low-level stagnation and then began to turn down anew in December 2014, a month that eventually should mark the beginning of a "new" formal recession (see *General Commentary No. 867*).

Coincident with and tied to the economic crash and the Panic of 2008, the U.S. banking system moved to the brink of collapse, a circumstance from which U.S. and global central-bank policies never have recovered. Unwilling to admit its loss of systemic control, the Federal Reserve had been making loud noises of continuing to raise interest rates, in order to contain an overheating economy, but that "overheating" activity has started to fade. As this ongoing crisis evolves towards its unhappy end, the U.S. dollar ultimately should face unprecedented debasement with a resulting runaway domestic inflation.

Broad economic and systemic conditions are reviewed regularly, with the following *Commentaries* of particular note: *Special Commentary No. 885*, *Commentary No. 869*, *No. 777 Year-End Special Commentary* (December 2015*)*, *No. 742 Special Commentary: A World Increasingly Out of Balance* (August 2015) and *No. 692 Special Commentary: 2015 - A World Out of Balance* (February 2015). Those publications updated the long-standing hyperinflation and economic outlooks published in *2014 Hyperinflation Report—The End Game Begins* – *First Installment Revised* (April 2014) and *2014 Hyperinflation Report—Great Economic Tumble* – *Second Installment* (April 2014). The two *Hyperinflation* installments remain the primary background material for the hyperinflation circumstance. Other references on underlying economic reality are the *Public Commentary on Inflation Measurement* and the *Public Commentary on Unemployment Measurement*.

Recent Commentaries (Covering Recent Headline Details and/or Special Features). *[Pease Note: Complete ShadowStats archives, from 2004 forward, are found at www.ShadowStats.com (left-hand column of home page).]*

Commentary No. 890 covered the negative-downside annual benchmark revisions to the trade deficit, the May 2017 estimates of labor conditions, ShadowStats Ongoing Money Supply M3, The Conference

Board Help Wanted OnLine® Advertising and April 2017 estimates of the Cass Freight Index™, and the monthly trade deficit and construction spending.

Commentary No. 889 reviewed the second-estimate, first-revision to first-quarter 2017 GDP, and the April 2017 estimates of New Orders for Durable Goods and New- and Existing Home Sales.

Special Commentary No. 888 discussed evolving political circumstances that could impact the markets and the economy, reviewed the annual benchmark revisions to Manufacturers' Shipments and New Orders for Durable Goods and updated Consumer Liquidity Conditions.

Commentary No. 887 reported on the April 2017 detail for Industrial Production and Residential Construction (Housing Starts), with some particular attention to historic, protracted periods of economic non-expansion, of which the current non-recovery is the most severe.

Commentary No. 886 reviewed the headline details of the April 2017 CPI and PPI detail, along with headline reporting of nominal and real Retail Sales, real Average Weekly Earnings and regular monthly review of U.S. dollar conditions and prospects.

Special Commentary No. 885, entitled *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*, reviewed the unusual nature of the headline reporting of the April 2017 employment and unemployment details.

Commentary No. 884 reviewed the March 2017 details for the U.S. Trade Deficit and Construction Spending and the Conference Boards' reporting of April 2017 Help Wanted OnLine.

Commentary No. 883 covered the headline detail for the "advance" or first-estimate of first-quarter GDP, along with an update to *Consumer Liquidity Conditions*.

Commentary No. 882 summarized the annual benchmark revisions to Retail Sales and reviewed the March 2017 releases of New Orders for Durable Goods and for New- and Existing-Home Sales.

Commentary No. 881 reviewed the prior March 2017 Industrial Production, Housing Starts and the Cass Freight Index™, along with an economic update in advance of the initial first-quarter 2017 GDP estimate.

Commentary No. 880 detailed the prior March 2017 headline reporting the of both Real and Nominal Retail Sales, Real Earnings, the CPI, the PPI and updated Consumer Liquidity, where mounting stresses on consumer income and credit are signaling major economic issues ahead.

Commentary No. 879 covered March 2007 Employment and Unemployment, Help-Wanted Advertising and an update on monetary policy and Money Supply M3 (the ShadowStats Ongoing Measure).

Commentary No. 877 outlined the nature of the downside annual benchmark revisions to industrial production, along with implications for pending annual revisions to Retail Sales, Durable Goods Orders and the GDP.

Commentary No. 876 current headline economic activity in the context of formal definitions of the business cycle (no other major series come close to the booming GDP, which is covered in its third revision to fourth-quarter activity. Also the February 2017 SentierResearch reading on real median household income was highlighted.

Commentary No. 875 assessed and clarified formal definitions of the U.S. business cycle, which were expanded upon significantly, subsequently, in *No. 876*. It also provided the standard review of the headline February 2017 New Orders for Durable Goods, New- and Existing-Home Sales and the Cass Freight Index™.

Commentary No. 873 discussed prospects for future tightening and/or a return to quantitative easing by the FOMC, along with the prior review of the February 2017 Residential Construction reporting.

Commentary No. 872 offered some initial comment on the FOMC rate hike, in conjunction with the review of last month's February 2017 Retail Sales (real and nominal), Real Earnings and the CPI and PPI.

Commentary No. 871 covered prior reporting of February Labor Conditions, updated Consumer Liquidity and the ShadowStats Ongoing M3 Measure for February 2017, and a revised FOMC outlook.

General Commentary No. 867 assessed mixed signals for a second bottoming of the economic collapse into 2009, which otherwise never recovered its level of pre-recession activity. Such was in the context of contracting and faltering industrial production that now rivals the economic collapse in the Great Depression as to duration. Also covered were the prior January 2017 New- and Existing Home Sales.

Commentary No. 864 analyzed January 2017 Employment and Unemployment detail, including benchmark and population revisions, and estimates of December Construction Spending, Household Income, along with the prior update to Consumer Liquidity.

Commentary No. 861 covered the December 2016 nominal Retail Sales, the PPI, with a brief look at some summary GAAP reporting on the U.S. government's fiscal 2016 operations. The GAAP-detail will be reviewed in a *Special Commentary*.

No. 859 Special Commentary reviewed and previewed economic, financial and systemic developments of the year passed and the year or so ahead.

Note on Reporting-Quality Issues and Systemic-Reporting Biases. With some historical detail updated recently *Special Commentary No. 885*: *Numbers Games that Statistical Bureaus, Central Banks and Politicians Play*, 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 inflation and to overstate economic activity—as generally viewed in the common experience of Main Street, U.S.A.—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 eleven 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, with the use of concurrent seasonal adjustments (as seen with retail sales, durable goods orders, employment and unemployment data). That issue is discussed and explored in the labor-numbers related *Supplemental Commentary No. 784-A* and *Commentary No. 695*.

Further, discussed in *Commentary No. 778*, a heretofore unheard of spate of "processing errors" surfaced in 2016 surveys of earnings (Bureau of Labor Statistics) and construction spending (Census Bureau). This is suggestive of deteriorating internal oversight and control of the U.S. government's headline economic reporting. That construction-spending issue now appears to have been structured as a gimmick to help boost the July 2016 GDP benchmark revisions, aimed at smoothing the headline reporting of the GDP business cycle, instead of detailing the business cycle and reflecting broad economic trends accurately, as discussed in *Commentary No. 823*.

Combined with ongoing allegations in the last year or two of Census Bureau falsification of data in its monthly Current Population Survey (the source for the BLS 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*). John Crudele of the *New York Post* has continued his investigations in reporting irregularities: *Crudele Investigation*, *Crudele on Census Bureau Fraud* and *John Crudele on Retail Sales* (worth a review in the context of the recently-published 2017 retail sales benchmarking).

PENDING ECONOMIC RELEASES: *Updated* - Index of Industrial Production (May 2017). The Federal Reserve Board will publish its estimate of May 2017 Industrial Production activity tomorrow, Thursday, June 15th, with coverage in *Commentary No. 892* of that date. In the context of negative benchmark revisions to New Orders for Durable Goods and soft reporting of same in April (see *Special Commentary No. 888* and *Commentary No. 889*), production is a good bet to show a month-to-month decline in May 2017 as well as some downside revision to activity in recent months. Consensus expectations appear to have settled around a monthly headline gain of 0.1% to 0.2%.

***Updated* - Residential Construction—Housing Starts (May 2017).** The Census Bureau will release May 2017 residential construction detail, including Housing Starts, on Friday, June 16th, to be covered in *Commentary No. 893* of that date. In line with common-reporting experience of recent years, monthly results are likely to be unstable and not statistically meaningful, holding in a general pattern of down-trending stagnation. That said, in the wake of the nonsensical extreme swings in recent months and relatively meaningless annual benchmark revisions, almost anything remains possible in this unstable series in a given month, despite what are relatively strong, positive catch-up consensus expectations for the headline detail.

Irrespective of the usual meaninglessness of the headline detail, the broad pattern of housing starts still should remain consistent with the low-level, stagnant activity, as seen at present, where last month's, downside April 2017 activity was down by 48% (-48%) from recovering the pre-recession high of the series. That stagnation is particularly evident with the headline detail viewed in the context of a six-month moving average. Again, this series remains subject to regular and extremely-large, prior-period revisions.

Per the updated *Consumer Liquidity Conditions* in *Special Commentary No. 888*, without sustainable growth in real income, and without the ability and/or willingness to take on meaningful new debt in order to make up for an income shortfall, the liquidity-strapped U.S. consumer remains unable to sustain growth in broad economic activity, including demand for residential construction. A further update to liquidity conditions will follow in Friday's accompanying *No. 893*.