

COMMENTARY NUMBER 978 - PART I

October CPI and PPI, Retail Sales, Production, New Orders and Freight Activity

December 1, 2018

**Fed Begins to Waffle on Interest Rates and Tightening?
Watch the Dollar and Gold!**

**Broad Systemic Liquidity and Real Earnings Growth
Have Been Impaired by Federal Reserve Tightening**

**Constrained Consumer Liquidity Has Taken an
Increasing Toll on Economic Activity; GDP Final Sales Revised Lower**

Motor Vehicle Sales Are in a Downward Spiral

**Real Retail Sales, New Orders, Manufacturing,
Residential Construction and Home Sales All Have Weakened**

**Deteriorating Construction-Activity and Residential-Sales
Never Have Recovered Pre-Recession Peak Levels**

**With No End in Sight, October 2018 U.S. Manufacturing Remained
Shy by 4.3% (-4.3%) of Recovering Its December 2007 Pre-Recession Peak**

**The 130 Straight Months of Economic Non-Expansion in Manufacturing
Is Unlike Anything Ever Seen in the 100-Year History of the Series**

Slowdown in Consumer-Driven Activity Looks Like the Onset of a New Recession

**Unadjusted October 2018 Annual Inflation Bounced Back from
Year-Ago Disruptions, but Falling Gasoline Prices Should Offer Some Relief**

PLEASE NOTE: Within a day or so of this *Commentary No. 978 – Part I* going to press, subsequent [Commentary No. 978 – Part II](#) will be posted, providing a full review of October 2018 New Residential Construction (Housing Starts and Building Permits) and New- and Existing-Home Sales, along with the first revision to Third-Quarter 2018 Gross Domestic Product (GDP) and the related initial estimates of Gross Domestic Income (GDI) and Gross National Product (GNP), also touched upon in *Part I*.

Hyperinflation and Consumer Liquidity Watches. Fully updated [Consumer Liquidity Watch No. 5](#) was posted on November 21st. [Hyperinflation Watch No. 3](#) will be updated in the week ahead as *Hyperinflation Watch No. 4*.

DAILY UPDATES. Summary detail and headlines of new economic releases are posted concurrently in the *Daily Update* column, top right hand section of the www.ShadowStats.com home page, generally within two hours of the headline release. Details usually remain posted until covered in a *Commentary*.

The planned ShadowStats Publication Schedule, Schedule Revisions and Notes to Subscribers also are posted regularly at the end of that column.

Your comments and suggestions always are invited.

John Williams (707) 763-5786, johnwilliams@shadowstats.com

Today's (December 1st) Opening Comments briefly discusses late-breaking FOMC considerations and consumer liquidity items, and it reviews the October 2018 CASS Freight Index™ versus October Durable Goods Orders and the Manufacturing Sector of Industrial Production.

The **Reporting Detail** of *Part I* reviews the October 2018 Consumer and Producer Price Indices, CPI-related liquidity measures, Retail Sales, Industrial Production and New Orders for Durable Goods. Today's *Reporting Detail* continues in [Commentary No. 978 – Part II](#), covering October 2018 Residential Construction (Building Permits and Housing Starts), New-and Existing-Home Sales, the second estimate, first revision to Third-Quarter 2018 Gross Domestic Product (GDP) and initial estimates of Gross Domestic Income (GDI) and Gross National Product (GNP).

Part II also will include the **Week, Month and Year Ahead**, updating text of *No. 973 ALERT* for any shifting FOMC considerations, previewing pending economic releases and providing background on recent *Commentaries*.

Commentary No. 978 – Part I contents and graphs, are detailed on the following pages.

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Pending Commentary No. 978 – Part II – Major Section Headings Include:

Please note: Part I has been edited so as to add live links for Part II: [Commentary No. 978 – Part II](#)

REPORTING DETAIL (Continued)

New Residential Construction (October 2018)

New-and Existing-Home Sales (October 2018)

Construction Spending (October 2018)

Gross Domestic Product (Third-Quarter 2018, First Revision)

WEEK, MONTH AND YEAR AHEAD

Exploding Risk of Intense Financial Market Turmoil

Pending Economic Releases

Links to Prior Commentaries, Special Reports and Other Writings

OPENING COMMENTS

Mounting Consumer Liquidity Woes Hit the Economy Hard

In Response, Fed Appears to Waffle on Its Rate Hikes and Tightening?

Financial-Market Risk Intensifies

The Fed Blinks. Touched upon here, hints of a possible easing-shift in Federal Reserve policy have intensified risks of near-term turmoil in the U.S. Dollar and related financial markets. Current developments will be updated fully in the *Week, Month and Year Ahead* section of subsequent [Commentary No. 978 – Part II](#), as well as in pending *Hyperinflation Watch No. 4*.

Despite all the continued happy talk by the Fed of near-perfect economic conditions, at present, if the global financial markets begin to read the current circumstance as a precursor to the Fed backing off reversing its Quantitative Easing programs, heavy selling of the U.S. dollar and buying of gold likely will be among the major financial-market reactions.

A November 28th speech by Federal Reserve Chairman Jerome Powell, generated initial speculation in the financial markets of the possible “dovish” policy shift by the Federal Reserve Board’s Federal Open Market Committee’s (FOMC), in the near future. Such was followed by similar indications in the November 29th release of the [Minutes of the November FOMC Meeting](#):

“A couple of participants noted that the federal funds rate might currently be near its neutral level and that further increases in the federal funds rate could un-duly slow the expansion of economic activity and put downward pressure on inflation and inflation expectations.”

The ShadowStats assessment remains that the FOMC tightening and rate hikes, particularly in the last year have squashed consumer liquidity, pushing the U.S. economy to the brink of, if not already into, a new “recession,” even though the economy never fully recovered from its collapse into 2009. This condition appears to have intensified in recent headline detail, reviewed in current *Commentaries*.

Despite Chairman Powell’s mention of the Fed’s dual Congressional mandate of targeting “maximum employment” and “price stability,” the U.S. Central Bank’s overriding concern and policy since before the 2007 banking crisis has been to keep the U.S. and global banking systems afloat at any and all costs. That policy specifically has ignored or pushed aside any resulting constraints on, or impairment of broad domestic economic activity, again, so long as the existing banking system would survive.

In tandem with the economic collapse into 2009, the U.S. banking system still has not recovered fully from its near-collapse in 2007/2008. The Fed still has no way of bringing continuing systemic banking vulnerabilities under control, despite the costs of its policy actions on domestic economic stability.

In his November 28th address to the New York Economic Club, [*The Federal Reserve’s Framework for Monitoring Financial Stability*](#), Chairman Powell offered introductory remarks suggestive of the FOMC being close to ending its regular, quarterly interest rate hikes. At least, that is how it was advertised on Wall Street. In the context of the current Fed hype of perfect economic conditions, otherwise assessed independently here and in regular ShadowStats *Commentaries*, the following is an excerpt from those remarks. The bold text, which suggested a dovish change in how the Fed officially viewed current interest rate levels, is what triggered the coincident stock-market rally:

“Congress assigned the Federal Reserve the job of promoting maximum employment and price stability. I am pleased to say that our economy is now close to both of those objectives. The unemployment rate is 3.7 percent, a 49-year low, and many other measures of labor market strength are at or near historic bests. Inflation is near our 2 percent target. The economy is growing at an annual rate of about 3 percent, well above most estimates of its longer-run trend.

“For seven years during the crisis and its painful aftermath, the Federal Open Market Committee (FOMC) kept our policy interest rate unprecedentedly low--in fact, near zero--to support the economy as it struggled to recover. The health of the economy gradually but steadily improved, and about three years ago the FOMC judged that the interests of households and businesses, of savers and borrowers, were no longer best served by such extraordinarily low rates. We therefore began to raise our policy rate gradually toward levels that are more normal in a healthy economy. **Interest rates are still low by historical standards, and they remain just below the broad range of estimates of the level that would be neutral for the economy--that is, neither speeding up nor slowing down growth. My FOMC colleagues and I, as well as many private-sector economists, are forecasting continued solid growth, low unemployment, and inflation near 2 percent.**

“There is a great deal to like about this outlook. But we know that things often turn out to be quite different from even the most careful forecasts. For this reason, sound policymaking is as much about managing risks as it is about responding to the baseline forecast. Our gradual pace of raising interest rates has been an exercise in balancing risks. We know that moving too fast would risk shortening the expansion. We also know that moving too slowly--keeping interest rates too low for too long--could risk other distortions in the form of higher inflation or destabilizing financial imbalances. Our path of gradual increases has been designed to balance these two risks, both of which we must take seriously.

“We also know that the economic effects of our gradual rate increases are uncertain, and may take a year or more to be fully realized. While FOMC participants’ projections are based on our best

assessments of the outlook, there is no preset policy path. We will be paying very close attention to what incoming economic and financial data are telling us. As always, our decisions on monetary policy will be designed to keep the economy on track in light of the changing outlook for jobs and inflation.

“Under the dual mandate, jobs and inflation are the Fed’s meat and potatoes. In the rest of my comments, I will focus on financial stability--a topic that has always been on the menu, but that, since the crisis, has become a more integral part of the meal.”

Consumer Outlook Weakens, Auto Sales Tumble and General Motors Shuts Factories and Cuts Employment. Liquidity circumstances and related economic impact have continued to evolve, subsequent to the November 21st posting of [Consumer Liquidity Watch No. 5](#) (CLW-5). Tightening consumer liquidity conditions in CLW-5 were discussed in the context of *Graphs 4* and *5* in today’s *Reporting Detail*. Beyond a continuing collapse in residential construction and home sales (see [Part II](#)), weakening consumer demand for motor vehicles has been particularly severe.

Separately, October Real Monthly Median Household Income (Sentier Research) and the Conference Board’s November Consumer Confidence have been published, with updated graphs provided here (see *Graphs OC-1* to *OC-3*). These series will be updated fully in *Consumer Liquidity Watch No. 6*.

Consumer Liquidity Squeeze Impacts General Motors? On November 27th, [General Motors](#) announced meaningful jobs cuts and plant closings as it “re-designs” itself and its product lines. That said, the action happened to coincide with declining industry motor-vehicle sales, production and orders as reflected in October Retail Sales, Industrial Production and New Orders for Durable Goods and in the revised Third-Quarter 2018 GDP (fully reviewed in [Part II](#)), discussed in those sections of today’s *Reporting Detail*.

While headline real annualized growth in Third-Quarter 2018 GDP was unrevised at 3.50% in its first revision, GDP-component activity shifted around, with a greater build-up in inventories, for example, now accounting for 77.1% of the quarterly increase in the GDP level. Net of inventory change, third-quarter final sales growth slowed to 1.23% from an initial 1.43%, thanks partially to a downside revision in the personal consumption of motor vehicles. Initially, third-quarter consumption of motor vehicles had gained at an annualized real quarterly pace of 3.83%, which now has revised to an annualized real quarterly decline of 1.46% (-1.46%), discussed in the later *Retail Sales* section and in [Part II](#).

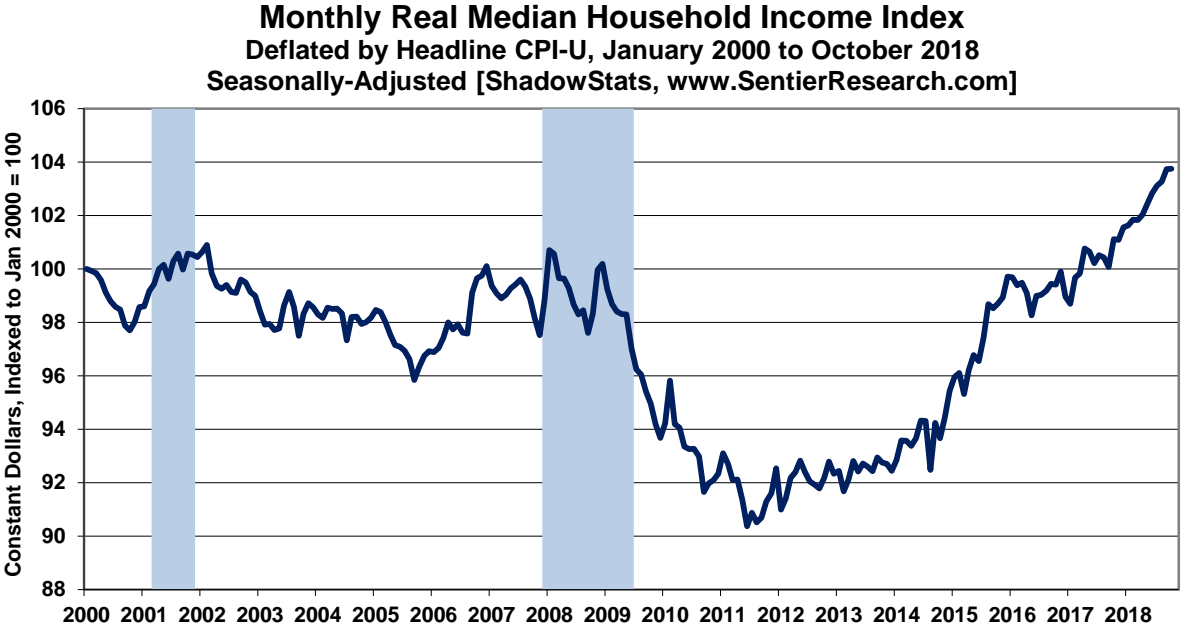
These cascading developments have tended to reinforce the ShadowStats outlook for weakening consumer liquidity conditions and related negative implications for underlying, broad economic activity.

Monthly Real Median Household Income Stalled in October 2018 at a High Level. The October 2018 Real Monthly Median Household Income flattened out, following six straight month-to-month increases, as reported November 28th by Sentier Research (www.SentierResearch.com). Annual growth also slowed in October 2018. Many thanks to Sentier for permission to use these numbers.

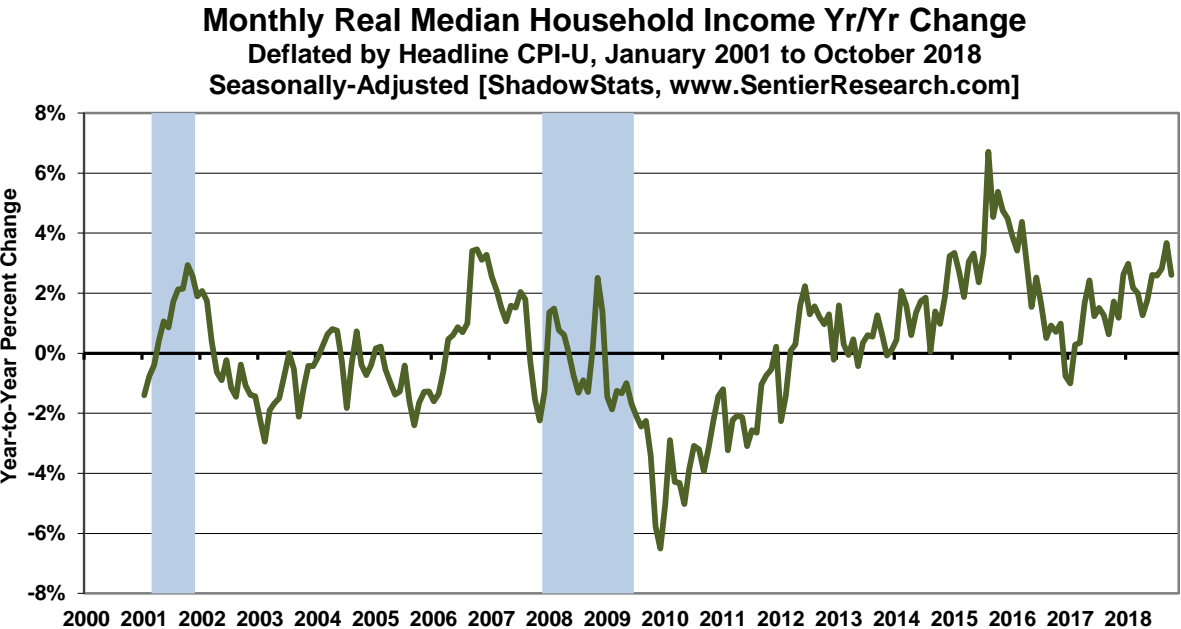
The latest detail is plotted in *Graphs OC-1* and *OC-2*, updating *Graphs 6* and *7* that accompany an extended review of the series in [Consumer Liquidity Watch No. 5](#) (CLW-5). A full update will follow in *Consumer Liquidity Watch No. 6*.

[Graphs OC-1 and OC-2 follow on the next page.]

Graph OC-1: Monthly Real Median Household Income (2000 to October 2018) Index, January 2000 = 100



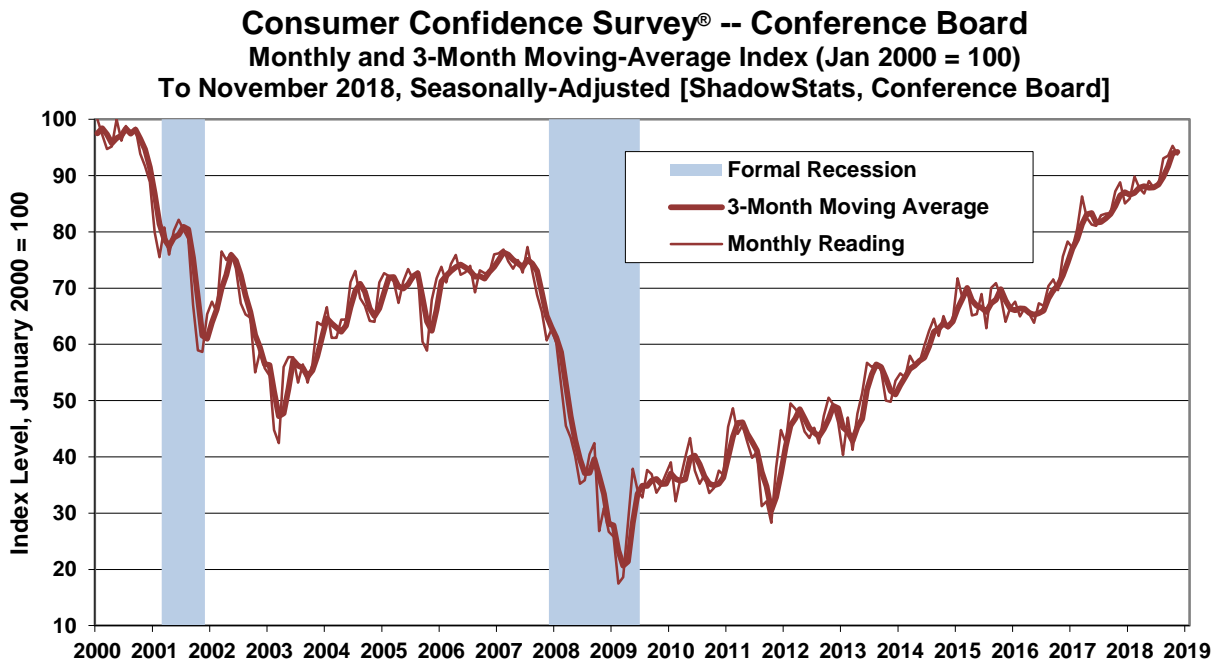
Graph OC-2: Monthly Real Median Household Income (2000 to October 2018) Year-to-Year Change



Consumer Confidence Takes a Hit. Noted in *CLW-5* the Conference Board’s [Consumer Confidence Survey®](#) had experienced some unusual recent volatility, suddenly showing some indication of a renewed, weakening outlook. For example, the Conference Board’s index took a headline jump of 1.9% in October 2018, to its highest level since September 2000, which was happy news on its surface. That reporting, however, was in the context of a sharp downside revision to September’s initial reading that had jumped by a headline 2.7% to its then-highest reading since September 2000. As revised with the October reporting, September was 0.4% above an unrevised August, instead of the initial 2.7%, and although the new headline October reading gained 1.9% in the month, it also was down by 0.4% (-0.4%) from the initial September reporting.

The Conference Board reported November 27th that the initial estimate of Consumer Confidence for November 2018 declined month-to-month by 1.6% (-1.6%) versus an unrevised October reading, largely offsetting the final headline October gain. *Graph OC-3* updates *Graph 2* in *CLW-5*. Again, a full update will follow in *Consumer Liquidity Watch No. 6*.

Graph OC-3: Consumer Confidence (2000 to 2018)



[Coverage of the CASS Freight Index™ begins on the next page.]

Manufacturing, Orders and the Cass Freight Index™ (October 2018)

October 2018 Freight Index Held Shy of Recovering Its Adjusted Pre-Recession Peak by a Narrowing 2.8% (-2.8%), in the Context of a Continuing Uptrend but Slowing Annual Growth. An independent, reliable private indicator of real-world economic activity and shifting business patterns, the October 2018 [Cass Freight Index](#)™ was published November 15th. Again, we thank Cass Information Systems for their permission to use the data.

Patterns Reflected in Other Key Economic Measures. Although uptrending based on its 12-month moving average, the unadjusted freight series held below—still shy of recovering—its post-recession high, amidst some slowing in the year-to-year change of the raw, unadjusted headline monthly reading (see accompanying *Graphs OC-4* and *OC-5*). The improving smoothed series remained shy of full economic recovery, still shy of recovering its pre-recession peak activity by 2.8% (-2.8%). The headline detail here remains as published, not seasonally adjusted and not subject to annual benchmark revisions, unlike some of the purportedly better-quality government numbers, such as New Orders for Durable Goods and the Manufacturing Sector of Industrial Production, which still are heavily modeled and gimmicked (see [Commentary No. 942-B](#) and [Commentary No. 950](#)).

Similar patterns are seen in a variety of major economic measures, including the heavily upside-biased headline GDP, when corrected for the understatement of the headline inflation used in deflating the series (see in particular the recently published *Opening Comments* of [Commentary No. 976](#), and the discussion involving *Graphs OC-3* to *OC-23* there). Other series include New Orders for Durable Goods (updated here in *Graphs OC-6* and *OC-7*) and the Manufacturing Sector of Industrial Production (updated here in *Graphs OC-8* and *OC-9*), and as discussed in today's related *Reporting Detail*. Other series such U.S. Petroleum Consumption, Real Construction Spending and the Employment-Population Ratio, again, were reviewed in [Commentary No. 976](#)).

The October 2018 Cass Freight Index numbers continued in low-level economic non-expansion as otherwise reflected in some elements of broad economic and general business activity, yet they also showed a pattern of positive, uptrending headline activity. The pace of year-to-year growth had eased back some to 6.2% in October 2018, having gained 8.2% in September 2018, versus 6.0% in August 2018, 10.6% in July 2018, 7.2% in June 2018, 11.9% in May 2018, all versus a near-term peak in January 2018 of 12.5% (*Graph OC-5*). The unadjusted monthly level of October 2018 (thin line in *Graph OC-4*) held near the levels of August and September, well off the May 2018 post-recession high and still holding below its pre-recession peak activity.

The 12-month trailing average of activity, however, did hit a new post-recession high, yet it remained well shy of recovering its pre-recession peak. Activity reflected in the 12-month trailing average—used to eliminate seasonality in the unadjusted series (see the *General Background to the Freight Index*)—remained in low-level, uptrending stagnation, down by 2.81% (-2.81%) from recovering its formal pre-recession high, down by 5.89% (-5.89%) from its precursor peak (see *Graph OC-4*).

For the twenty-third consecutive month, the twenty-fourth month in the last twenty-five, year-over-year change in the unadjusted monthly index was positive. Again, it eased back to 6.16% in October 2018, from 8.20% in September 2018, still holding off its near-term peak growth of 12.54% in January 2018 (see *Graph OC-5*).

A consecutive string of nineteen months of annual contraction in the Freight Index began in March 2015. That was consistent with the “new” recession signal following the near-term Industrial Production peak in November 2014 recovered anew in initial March 2018 production reporting, lost again with the annual benchmark revisions to production, only to be regained once more with the headline April 2018 (see the discussion in the *Industrial Production* section of the *Reporting Detail*).

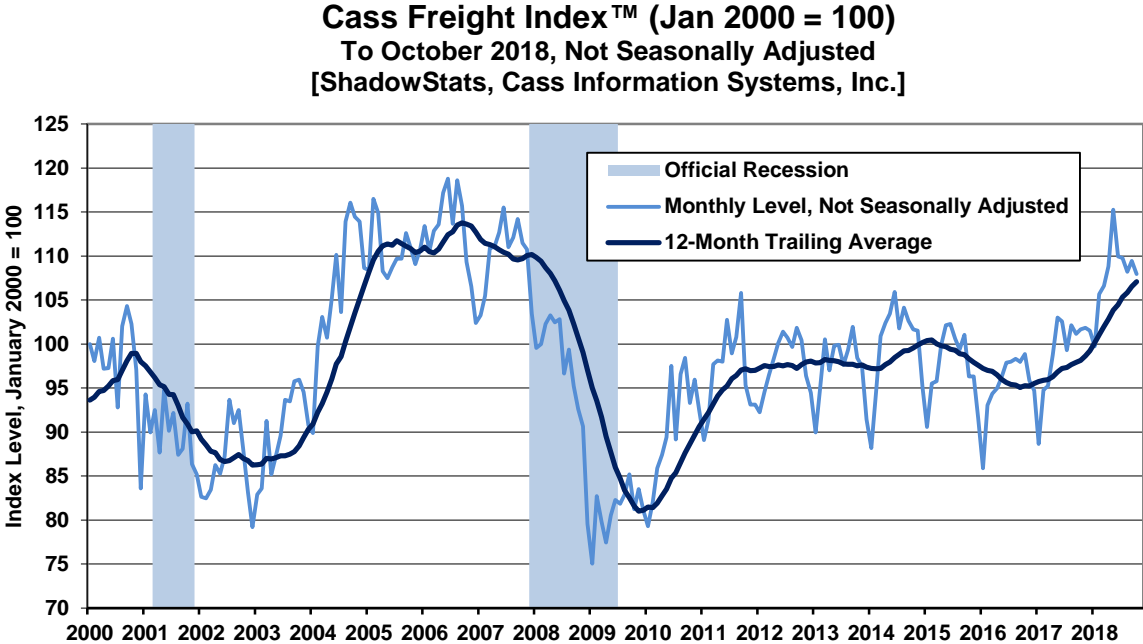
Comparative growth patterns of the Freight Index (*Graph OC-4* of level and *Graph OC-5* of annual change) versus never-recovered, real New Orders for Durable Goods and the dominant Manufacturing Sector of Industrial Production are shown in *Graphs OC-6* and *OC-8* as to level and in *Graphs OC-7* and *OC-9* as to year-to-year change. More-extensive comparisons with other indicators of U.S. economic activity, including the GDP, again, are found in the *Opening Comments* of [Commentary No. 976](#).

The continuing uptrend in the smoothed series, and the ongoing positive, albeit fluctuating annual growth in the Cass Index, indicate that the recession in freight activity has bottomed out, but still has not recovered its pre-recession peak activity. Even with a positive annual gain in 2017 and in the first ten months of 2018, current patterns of smoothed levels of activity have yet to break out of the not-recovered pattern of the last ten-plus years, to enter a period of new economic expansion. Shown in *Graph OC-4*, uptrending monthly activity is not yet fully recovered.

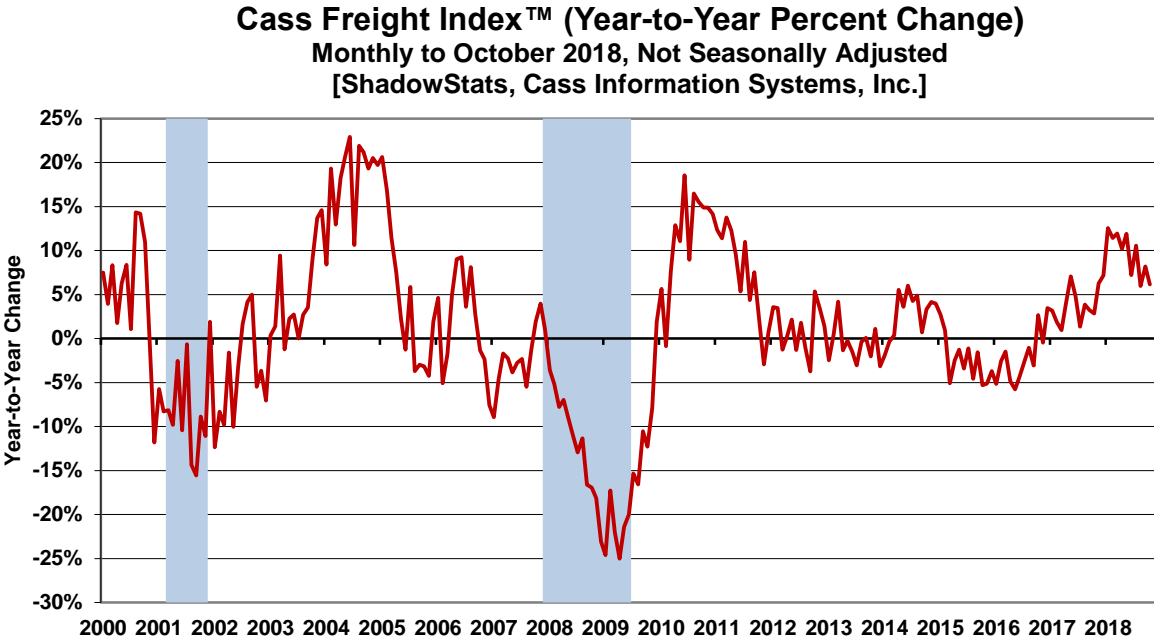
Early Recovery, But No Economic Expansion. When economic activity starts to recover, such positive growth traditionally is not clocked formally as a new economic “Expansion,” until the level of the series breaks above its pre-recession high. This was reviewed in [Commentary No. 875](#) and expanded upon in [Commentary No. 876](#), on the nature of the business cycle.

Noted earlier, the ShadowStats smoothed (12-month trailing average) headline reading on the CASS Freight Index, through October 2018 (*Graph OC-4*) remained down by 5.89% (-5.89%) from “Recovering” its preliminary pre-recession peak of September 2006, down by 2.81% (-2.81%) from recovering its formal “Pre-Recession Peak” of December 2007 (Fourth-Quarter 2007). That also was the formal peak for the Industrial Production, Manufacturing and GDP series. While the “Recovery” receives the benefit of growth off low levels of activity—the recession “Trough”—the deficit in current activity versus the pre-recession peak has to be overcome, before formal, economic “Expansion” begins. Economic downturns eventually hit bottom. The official 2007 recession and related collapse in broad economic activity has been recognized formally from a peak in December 2007 to a trough in June 2009, which appears to be fairly consistent with a number of series, in terms of timing the trough.

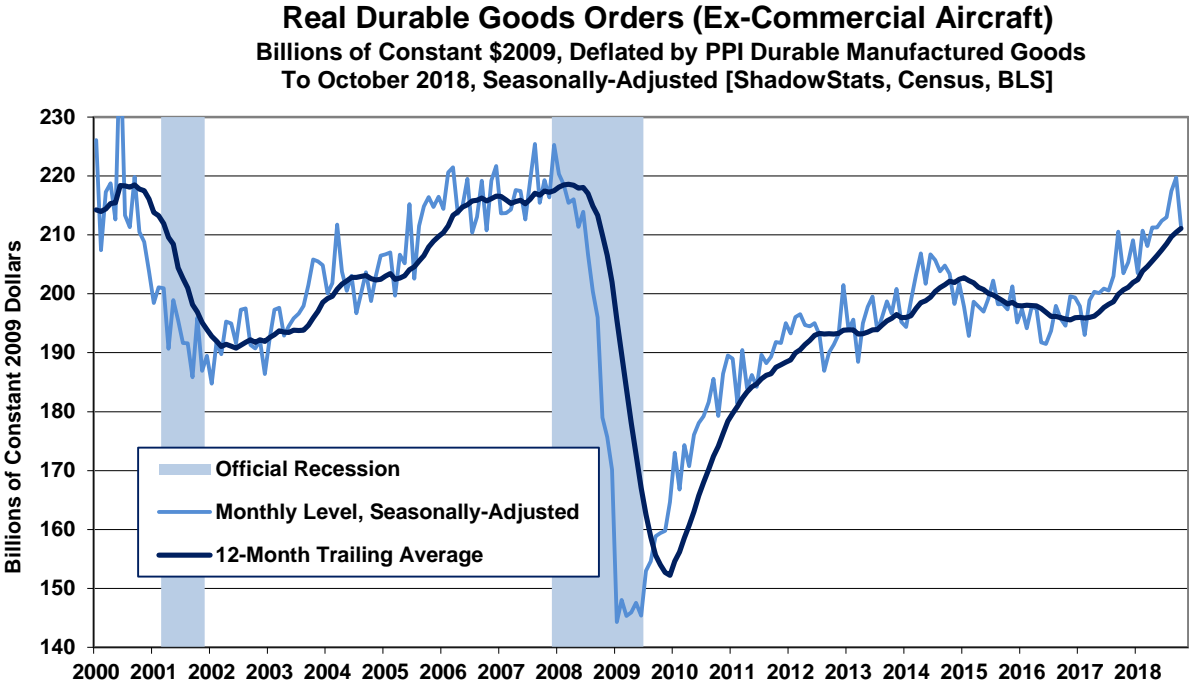
Graph OC-4: CASS Freight Index™ Moving-Average Level (2000 to October 2018)



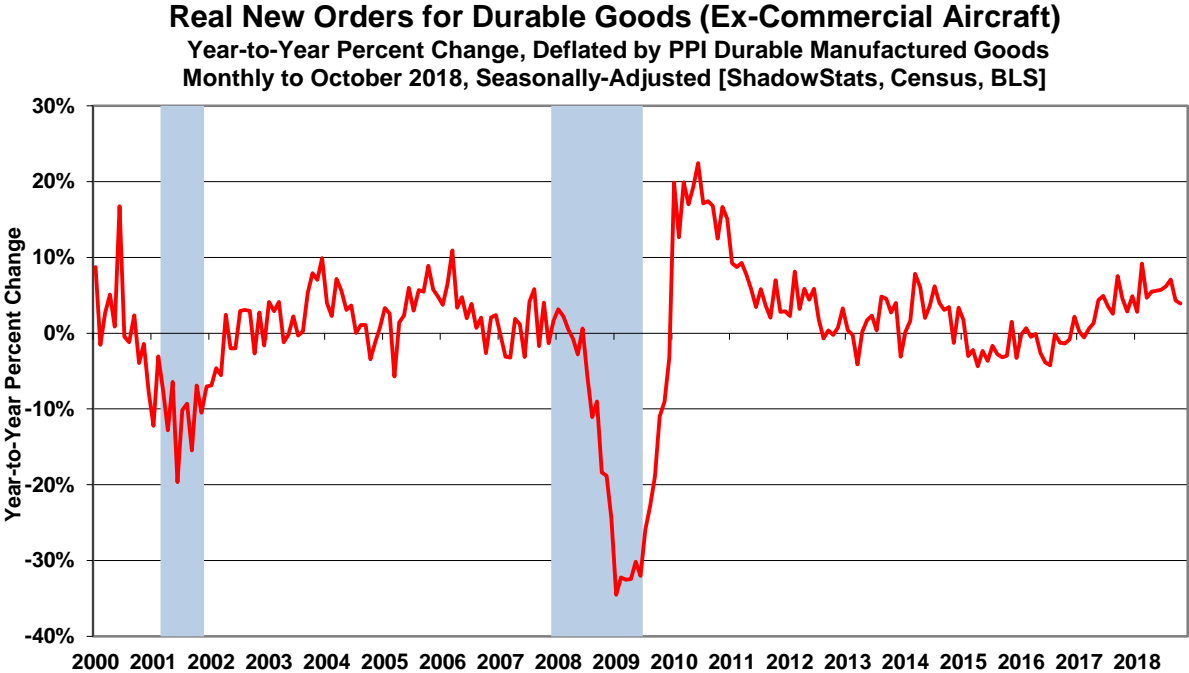
Graph OC-5: CASS Freight Index, Monthly Year-to-Year Percent Change (2000 to October 2018)



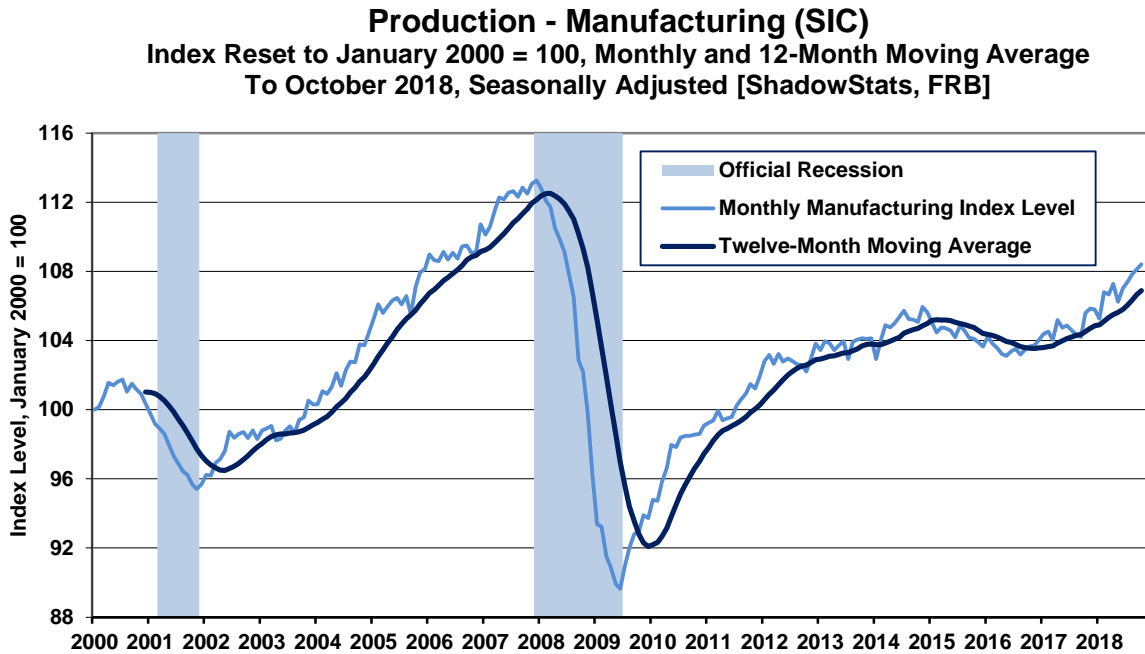
Graph OC-6: Real Durable Goods, Ex-Commercial Aircraft, 12-Month Moving-Average (2000 to October 2018)



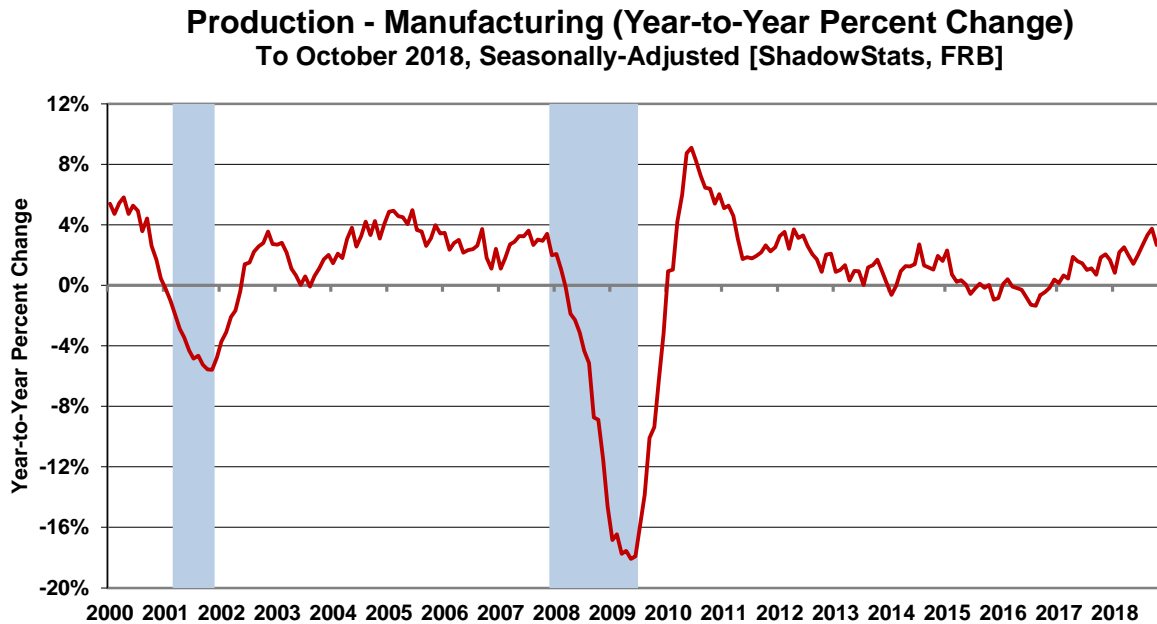
Graph OC-7: Real New Orders, Ex-Commercial Aircraft, Year-to-Year Percent Change (2000 to October 2018)
 (Same as Graph 38 in the Reporting Detail)



Graph OC-8: Industrial Production-Manufacturing, 12-Month Moving-Average Level (2000 to October 2018)



Graph OC-9: Manufacturing, Year-to-Year Percent Change (2000 to October)
 (Same as Graph 21 in the Reporting Detail)



General Background to the Freight Index. [*This section largely is repeated from [Commentary No. 975.](#)*] Beginning with [Commentary No. 782](#) (further information is available there), ShadowStats published the detail on the CASS Index, a measure of North American freight volume as calculated by, and used with the permission of Cass Information Systems, Inc. Freight activity is a basic, underlying indicator of commercial activity and the broad GDP. Of the combined U.S. and Canadian (North American) GDP in 2017, roughly 92% was attributable to the United States.

Graph OC-4 reflects the monthly freight numbers updated through October 2018. While adjusted for factors such as days in a month, the headline monthly detail is not adjusted for broad seasonality patterns, such as retailers stocking for the holiday shopping season. Accordingly, ShadowStats plots the series using a trailing twelve-month average, which tends to neutralize regular seasonal patterns over the period of a year, along with the unadjusted monthly detail plotted in the background. ShadowStats also re-indexed the series to January 2000 = 100, consistent with other graphs used here, where the headline Cass Index plot is based on January 1990 = 100. The plot of the trailing twelve-month average of the freight index shows it hit a near-term peak in February 2015, consistent with the onset of what appears to have been a “new recession” in December 2014. It slowed through September 2016, then flattened out and turned back to the upside through the current October 2018 reading, its highest level of the post-recession period, although still shy of its pre-recession peak (again, see *Graph OC-4*).

The pattern here is broadly consistent with the Industrial Production (Manufacturing) series, although no signs of an aggregate 2015 economic contraction came out of the 2018 comprehensive annual benchmark revisions to the GDP (see [Special Commentary No. 968-Extended](#)), despite indications of a double-dip recession in the Industrial Production benchmarking (see *Graph 12* in today’s *Reporting Detail*).

Another approach to assessing not-seasonally-adjusted monthly detail is to look at year-to-year change by individual month, as plotted in *Graph OC-5*. The unadjusted monthly detail had been in continual year-to-year decline since March of 2015, down at an intensified annual rate of 3.05% (-3.05%) in September 2016. It rallied to an annual gain of 2.66% in October 2016, but fell back into year-to-year contraction of 0.05% (-0.05%) in November 2016, coming back to the plus-side by 3.46% in December 2016, eventually hitting a near-term peak of 12.54% in January 2018, with fluctuating activity through 6.16% in October 2018. In combination, *Graphs OC-4* to *OC-9* remain consistent with a pattern of collapsing economic and business activity into 2009, with subsequent low-level, non-expanding (defined as still holding below prior peak activity), albeit currently in uptrending economic activity.

[The Reporting Detail begins on the next page.]

REPORTING DETAIL

Consumer Price Index (October 2018)

Annual Inflation Jumped Year-to-Year, Reversing Year-Ago Hurricane Distortions

Declining Gasoline Prices Should Offer Some Temporary Respite

Headline Annual CPI Inflation Rose in October 2018, As Distorting Effects of Year-Ago, Hurricane-Spiked Energy Prices Begin to Wane. The October 2018 Consumer Price Index (CPI-U) rose by a seasonally adjusted 0.33% in the month, versus 0.06% in September, spiked by a seasonally adjusted 3.00% gain in October gasoline prices, versus a drop there of 0.21% (-0.21%) in September. Unadjusted, year-to-year CPI-U inflation rose to 2.52% in October 2018, versus 2.28% in September 2018, which had been depressed temporarily by relative year-ago hurricane spikes to oil/energy prices. That was as headlined by the reporting Bureau of Labor Statistics (BLS). The October 2018 ShadowStats Alternate CPI (1980 Base) rose year-to-year by 10.3%, versus 10.0% in September.

By major CPI-U sector, monthly Food inflation dropped by 0.08% (-0.08%) in October having gained 0.03% in September, Energy rose by 2.40% in the month, having declined by 0.46% (-0.46%) in September, while “Core” inflation (net of food and energy) rose by 0.19% in October versus 0.12% in September.

Consumer liquidity stresses mounted sharply as Real Average Weekly Earnings rose month-to-month by an adjusted 0.15% in October 2018, having declined by 0.06% (-0.06%) in September, for all employees, but dropped by 0.09% (-0.09%) in October and by 0.06% (-0.06%) in September for production and nonsupervisory employees. Unadjusted annual changes were sharply negative for both real average weekly series in October 2018, following gains in September 2018.

Plunging Gasoline Prices Should Help Contain Annual and Monthly Inflation in November 2018 and Possibly December 2018, Aiding Consumer Liquidity a Bit. Retail gasoline prices in the last week of November 2018 had declined by 11.9% (-11.9%) since the first week of October, down 9.2% (-9.2%) since the last week of October, with average monthly prices in November 2018 down by 7.0% (-7.0%) from October 2018, per the Department of Energy.

Noted with last month's headline September CPI: "Given the year-ago [hurricane generated] price distortions in gasoline, *and barring extreme gasoline-price gyrations in the next several months* [emphasis added here], unadjusted annual CPI-U inflation should be jumping back to around 3.0% by the November/December 2018 timeframe."

Gasoline-price gyrations in the last month, however, have been meaningful on the downside and are likely to reduce annual headline CPI-U inflation in November 2018 versus October 2018, and possibly further still in December 2018 versus November 2018, as discussed later. The weaker the rate of inflation used in deflating nominal economic activity or income, the stronger will be the inflation-adjusted activity. Declining gasoline prices, as long as they last, will provide some relative liquidity boost/relief to the otherwise liquidity-growth starved U.S. consumer.

As has been the circumstance for oil and gasoline price movements in recent years, where some price movement (decline at present) reflects underlying fundamentals (heavy inventories), the bulk of major price movements usually is driven by external political circumstances, not by domestic economic conditions.

Underlying Common Experience Continues to Confirm Formal Understatement of Headline Inflation, Where Redefined and Understated Inflation Artificially Spikes Inflation-Adjusted Real Growth.

Anecdotally, informal surveying by ShadowStats of consumer views, as to the credibility of headline inflation continues to suggest that most individuals believe headline consumer inflation consistently understates their real-world inflation experience. The informal consensus is in the range of a 3% to 4% understatement of headline annual inflation against common experience. That is consistent with the ShadowStats Alternate CPI (versus 1990-based methodologies), and less severe than the 6% to 8% range suggested by the ShadowStats Alternate CPI (1980-based methodologies).

That latter measure, though, is more accurate in terms of the meaningful methodological changes made to CPI reporting, beginning about 1980, which then began to exclude from housing inflation a component measure of the "cost of buying a house." The revamped series shifted over to assessing housing costs as "homeowners equivalent rent." Those all were "guesstimations" by the BLS as to what homeowners would charge themselves to rent their own properties to themselves. The monthly inflation rate then was determined to be the amount of increase in monthly rent that homeowners would charge themselves.

Where this was and is a completely rigged number, the BLS estimated the change in methodology would have the net effect of reducing the headline annual CPI-U inflation rate by 1.4% (-1.4%) per year from what would have been reported otherwise. Where that annual inflation-rate saving was cumulative, that one change knocked about 13.2% off the cumulative level of the headline CPI-U in the first decade. These issues are discussed in the *Alternate Consumer Inflation Measures* section.

Specifically, with the headline unadjusted annual October 2018 CPI-U inflation up by 2.5%, 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 October 2018 at 6.1%, based on pre-Clinton-gimmicked 1990 methodologies, and at 10.3%, based on 1980 methodologies. Detailed in [Public Commentary on Inflation Measurement](#), inflation based on common experience is much worse than the headlines, both as experienced by individual consumers, as well as by the business community (also see the discussion on Real Average Weekly Earnings and related *Graph 4*).

Longer-Range Inflation Outlook. Despite U.S. dollar strength of recent years, and what had been accelerating, then faltering dollar strength, subsequent to the post-2016 election euphoria, the dollar recently had seen fairly regular and intensifying selling pressure, then a reversal to the upside, and ongoing mixed pressures, amidst the equity markets and mounting expectations of political-system instabilities. Much of what happens here has reflected market expectations of continuing FOMC rate hikes in the United States, and recent indications by the European Central Bank (ECB) that it may hold off another year or so to raise rates (see [Hyperinflation Watch – No. 3](#) and the imminent update to same in *HW-4*). In the context of early indications in recent days of the FOMC shifting to more “dovish” monetary policies (see the *Opening Comments*), downside risks for the dollar are mounting rapidly. The text in the *Week, Month and Year Ahead* section in [Part II](#) of this missive, tied to [Special Commentary No. 973 – ALERT](#) of October 14th, has been updated. Pending *Hyperinflation Watch No. 4* also will update the mixed economic and financial-market pressures, the shifting global and domestic political tensions and the squirrely season discussed previously in [Commentary No. 970](#) of September 26th.

In the context of today’s *Opening Comments*, and as regularly discussed here, a tremendous threat to the dollar, systemic U.S. liquidity and financial-market stability remains tied to the U.S. Federal Reserve’s fundamental inability to resolve the 2008 financial collapse, other than having bought finite time with emergency, stopgap measures and extraordinary jawboning and financial-market interventions. The proximal trigger here for potential shifts in FOMC policies remains tied to the now-unfolding “unexpected” economic weakness. In a related matter, also with potential for triggering crisis-level disruptions in the global currency and financial markets, are rapidly deteriorating, long-term U.S. sovereign-solvency issues and deteriorating political conditions in Washington, D.C..

Recent FOMC tightenings have been despite continued, lack of full-economic recovery from the 2008 collapse. That is in terms of the banking system, where real consumer credit outstanding still has not expanded beyond pre-recession levels, as also confirmed by in the recently-published, second- and third-quarter analyses out of the Federal Reserve and New York Fed (see *Graphs 15 to 16* in [Consumer Liquidity Watch No. 5](#)). These issues also are evident in terms economic activity, with industries such as Manufacturing and Construction, which have yet to expand beyond pre-2007 recession levels.

How can the FOMC boast an expanding economy, when Main Street U.S.A. broadly still is not seeing it, and where Income Variance, as recently published by the Commerce Department (see [Commentary No. 969-Extended](#)) is at extremes rarely seen, except before the greatest financial market calamities?

Headline series such as Retail Sales and Industrial Production are not booming month-to-month (see the later related sections in the *Reporting Detail*). These indicators remain in the realm of “adverse” economic circumstances once feared by former Fed Chair Janet Yellen, which now have begun to unfold for a number of series and appear likely to have triggered some early, cautious talk of pullback by the FOMC in reversing its Quantitative Easing programs.

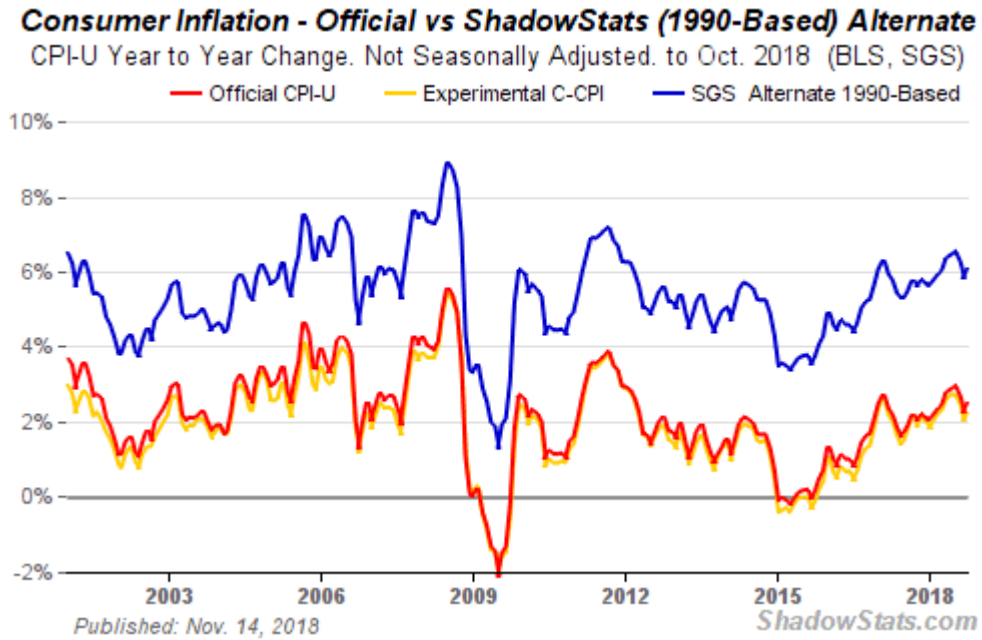
Despite the headline booming third-quarter 2018 GDP, the financial markets, particularly the global currency markets versus the U.S. dollar, increasingly should pick up on renewed faltering of U.S. basic and broad economic activity and on intensifying long-range U.S. Treasury solvency concerns. Where last month’s missive speculated, “Fed Chairman Powell’s response to these unfolding adverse circumstances should be forced within the near future,” such appears to be happening as we go to press, again, as discussed in today’s *Opening Comments*.

Out of necessity, the U.S. central bank has been forced to and continues to prop domestic banking-system liquidity against an ongoing gale of renewed, economically driven, banking-system solvency and liquidity issues. Those pressures were masked, and then intensified, by natural disasters of the last year or so, rapidly intensifying political discord in Washington and mounting global political instabilities. Despite strong speculation and protestations to the contrary, and promised tightening into December 2018, but not beyond, the FOMC likely will end up renewing/expanding Quantitative Easing, early in 2019.

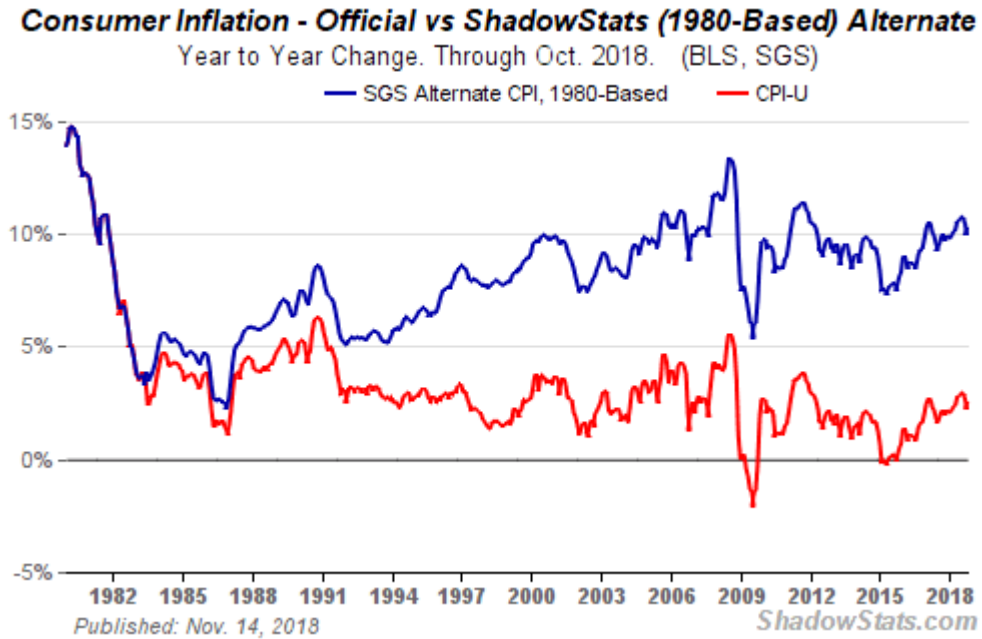
Compounding the high-risk of an increasing near-term run on the U.S. dollar remains what has started as a shift in global markets towards recognition of the Fed's conundrum, again, particularly amidst mounting concerns as to U.S. fiscal and political stability. The Federal Reserve and other central banks 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 intensifying economic and political uncertainties (again, see [Hyperinflation Watch – No. 3](#) and pending update, [Commentary No. 974](#), [Commentary No. 970](#), [Special Commentary No. 888](#) and [Special Commentary No. 935](#)).

[Graphs 1 and 2 begin on the next page.]

Graph 1: Comparative Headline Year-to-Year Change, CPI-U vs. ShadowStats 1990-Based Alternate



Graph 2: Comparative Headline Year-to-Year Change, CPI-U vs. ShadowStats 1980-Based Alternate



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) was an experimental measure—now set to go active, formally, with pending 2017 Tax Reform (see the Opening Comments)—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 November 14th that the headline, seasonally-adjusted October 2018 CPI-U inflation increased month-to-month by 0.3% [up by 0.33% at the second decimal point], having gained 0.1% [0.06%] in September, 0.2% [0.22%] in August, 0.2% [0.17%] in July, 0.1% [0.13%] in June, 0.2% [0.21%] in May, 0.2% [0.22%] in April, declined by 0.1% (-0.1%) [0.06% (-0.06%)] in March, having gained 0.2% [0.15%] in February, 0.5% [0.54%] in January, 0.2% [0.20%] in December 2017, 0.3% [0.34%] in November, and 0.1% [0.08%] in October.

Unadjusted, monthly October 2018 CPI-U gained by 0.18%, having gained 0.12% in September, 0.06% in August, 0.01% in July, 0.16% in June, 0.42% in May, 0.40% in April, 0.23% in March, 0.45% in February, 0.54% in January, having declined 0.06% (-0.06%) in December 2017, having been unchanged at 0.00% in November and having declined in October by 0.06% (-0.06%).

Major CPI-U Groups. The higher October 2018 CPI-U month-to-month inflation reflected a monthly gain in Energy costs, along with a decline in Food prices and an increase in “Core” inflation. By the numbers, the October 2018 CPI-U seasonally-adjusted monthly inflation 0.33% [0.18% unadjusted] was against an adjusted 0.06% [unadjusted 0.12%] September monthly gain.

That encompassed a “Core” (ex-food and energy) October 2018 monthly inflation rate of 0.19% [up by 0.25% unadjusted], previously a monthly September inflation rate of 0.12% [up 0.16% unadjusted].

Monthly Food prices dropped by 0.08% (-0.08%) adjusted [0.01% (-0.01%) unadjusted] in October 2018, versus a gain of 0.03% [0.12% unadjusted] in September.

Despite distortions in annual comparisons, Energy sector inflation jumped in the month of October 2018 by 2.40% [down by 0.18% (-0.18%) unadjusted], versus an adjusted decline of 0.46% (-0.46%) [an unadjusted 0.34% (-0.34%)] in September.

Related gasoline costs jumped by an adjusted 3.00% month-to-month [by 0.63% unadjusted] in October 2018, having declined month-to-month by an adjusted 0.21% (-0.21%) [gained by an unadjusted 0.34%] in September.

Holding within FOMC expectations, unadjusted annual October 2018 “Core” CPI-U topped the targeted 2.0% annual inflation rate for the eighth consecutive month, easing to 2.14% in October 2018, versus 2.17% in September 2018 and 2.20% in August 2018, where August had eased back from 2.35% in July 2018. Such was against annual inflation of 2.26% in June 2018, 2.24% in May 2018, 2.14% in April and 2.12% in March, where the March 2018 annual core inflation had broken above the Fed’s announced 2.0% target for the first time since February 2017. As of February 2018, the “Core” rate had held range-bound for eleven straight months (since April 2017) at 1.8% +/- 0.1%.

Year-to-Year CPI-U. Not seasonally adjusted, year-to-year inflation for the October 2018 CPI-U rose to 2.5% [2.52% at the second decimal point (see the opening discussion in the CPI section on year-ago hurricane disruptions)]. That followed gains of 2.3% [2.28%] in September 2018, 2.7% [2.70%] in August 2018, 2.9% [2.95%] in July 2018, 2.9% [2.87%] in June 2018, 2.8% [2.80%] in May 2018, 2.5% [2.46%] in April 2018, 2.4% [2.36%] in March 2018, 2.2% [2.21%] in February 2018, 2.1% and [2.07%] in January 2018. Annual inflation of 2.1% [2.11%] in December 2017 followed 2.2% [2.20%] in November 2017 and 2.0% [2.04%] in October 2017.

Year-to-year, CPI-U inflation would increase or decrease in next month’s November 2018 reporting, dependent on the seasonally-adjusted, month-to-month change, versus the adjusted, headline monthly gain of 0.34% in the November 2017 CPI-U. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for November 2018, the difference in November’s headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the unadjusted October 2018 annual inflation rate of 2.52%. Given an early guess of a seasonally-adjusted monthly change of 0.0% in the November 2018 CPI-U, that would leave the annual CPI-U inflation rate for November 2018 around 2.2% plus-or-minus (reflecting a decline in gasoline prices in the last month).

Again, as noted last month, “Given the year-ago price distortions in gasoline, and barring extreme gasoline-price gyrations in the next several months, unadjusted annual CPI-U inflation should be jumping back to around 3.0% by the November/December 2018 timeframe.” Discussed earlier, however, gasoline

prices have declined sharply in the last month, down by about 7.0% (-7.0%), on average in November 2018, helping to knock down headline, unadjusted CPI-U year-to-year inflation from 2.5% in October 2018, to around 2.2% in November 2018. December 2018 prices likely are on track for a further year-to-year decline.

Quarterly CPI-U. On a seasonally-adjusted annualized quarter-to-quarter basis, CPI-U rose by 2.00% in third-quarter 2018, having gained 1.66% in second-quarter 2018, 3.51% in first-quarter 2018, 3.31% in fourth-quarter 2017, 2.13% in third-quarter 2017, 0.10% in second-quarter 2017 and 2.96% in first-quarter 2017.

On an unadjusted, year-to-year basis, headline annual inflation by quarter was up by 2.64% in third-quarter 2018, versus 2.71% in second quarter 2018, 2.21% in first-quarter 2018, 2.12% in fourth-quarter 2017, 1.97% in third-quarter 2017, 1.90% in second-quarter 2017 and 2.54% in first-quarter 2017.

Annual Average CPI-U. The unadjusted annual average CPI-U inflation rate was 2.13% in 2017, versus 1.26% in 2016 and 0.12% in 2015.

CPI-W. The October 2018 seasonally-adjusted, headline CPI-W, which is a narrower series than the CPI-U and traditionally has greater weighting for gasoline than the CPI-U, rose month-to-month by 0.40%, following monthly gains of 0.03% in September, 0.27% in August, 0.15% in July, 0.14% in June, 0.23% in May and 0.26% in April, a decline of 0.16% (-0.16%) in March, gains of 0.11% in February, 0.62% in January, 0.19% in December 2017, 0.43% in November and 0.05% in October.

On an unadjusted basis, year-to-year CPI-W gained by 2.69% in October 2018 [again see the earlier discussion in this CPI section on hurricane distortions], having gained 2.34% in September 2018, 2.88% in August 2018, 3.16% in July 2018, 3.09% in June 2018, 3.00% in May 2018, 2.59% in April 2018, 2.44% in March 2018, 2.32% in February 2018, 2.14% in January 2018, 2.18% in December 2017, 2.32% in November 2017 and 2.05% in October 2017.

Quarterly CPI-W. On an annualized quarter-to-quarter basis, seasonally-adjusted CPI-W rose by 2.04% in third-quarter 2018, versus 1.57% in second-quarter 2018, 3.70% in first-quarter 2018, 3.75% in fourth-quarter 2017, 2.26% in third-quarter 2017, having declined by 0.26% (-0.26%) in second-quarter 2017 and having gained by 3.04% in first-quarter 2017.

On an unadjusted year-to-year basis, annual inflation by quarter rose by 2.79% in third-quarter 2018, versus 2.89% in second-quarter 2018, 2.30% in first-quarter 2018, 2.18% in fourth-quarter 2017, 1.96% in third-quarter 2017, 1.80% in second-quarter 2017 and 2.56% in first-quarter 2017.

Annual CPI-W. The unadjusted annual average CPI-W inflation rate was 2.13% in 2017, versus an average gain of 0.98% in 2016 and an average contraction of 0.41% (-0.41%) in 2015.

Chained-CPI-U. The headline C-CPI-U is not seasonally adjusted, and standardly is revised quarterly for the prior year. In the July 2018 reporting, year-to-year inflation rates revised lower by 0.175% (-0.175%) for each month back through September 2017. October 2018 headline details also underwent quarterly revisions, but they were unusually minimal, with upside revisions of 0.052% in annual inflation for October 2017 and 0.004% for November 2017, followed by subsequent downside annual revisions of 0.014% (-0.014%) to 0.015% (-0.015%) in each month from December 2017 through September 2018.

The unadjusted annual inflation rate for the C-CPI-U in October 2018 was 2.26%, versus a revised 2.03% [previously 2.04%] in September 2018, 2.46% [previous 2.48%] in August 2018, 2.70% [previously 2.71%] in July 2018, 2.53% [previously 2.54%] in June 2018, etc. This ongoing accounting fraud was set up during the Clinton Administration and the Congress of the time, along with the support of the Greenspan Federal Reserve. The openly stated intent of introducing the C-CPI-U was to reduce (artificially reduce, deliberately understate) the annual Cost of Living Adjustments (COLA) for Social Security recipients, as it had been defined and intended originally, as well as to boost taxpayers artificially into higher tax brackets.

Through multiple downside quarterly revisions, the level of the headline C-CPI-U Index has been reduced by 0.35% from its original headline reporting level, beyond the initially understated headline reporting. These quarterly “revisions” clearly are plug numbers, not actual revisions to underlying calculations with better numbers. While these bogus numbers indeed now are boosting taxpayers artificially into higher tax brackets, the Congressional miscreants have not had the courage, yet, to debase further the COLA for Social Security, although the C-CPI-U initially was designed specifically for that purpose. Give them time. Other gimmicks, however, have been used in the interim.

Discussed last month, based on the currently-defined CPI-W (otherwise artificially understated in recent decades) Social Security COLA adjustment will be 2.8% for 2019. It would have been 2.4% if the intended C-CPI-U, based on last month’s reporting, were fulfilling its intended role.

Given the current revisions, that still would be 2.4% (2.39% versus 2.41% if the detail were calculated to the second decimal point).

Quarterly C-CPI-U, Year-to-Year. On an unadjusted, year-to-year basis, annual inflation by quarter was up by 2.39% [previously 2.41%] in third-quarter 2018 (planned future COLA calculation basis), 2.36% [2.37%] in second-quarter 2018, 1.81% [1.82%] in first-quarter 2018, 1.71% [1.69%] in fourth-quarter 2017, 1.56% in third-quarter 2017, 1.50% in second-quarter 2017 and 2.30% in first-quarter 2017.

Annual Average C-CPI-U. The annual average C-CPI-U inflation rate was 1.76% in 2017, versus 0.93% in 2016 and contraction of 0.12% (-0.12%) in 2015. Again, for contrast, the heavily gimmicked and understated CPI-U showed unadjusted annual average CPI-U inflation rate at 2.13% in 2017, versus 1.26% in 2016 and 0.12% in 2015.

See the *Opening Comments* of [Commentary No. 945](#) and [Commentary No. 920](#) as to the impact of the adoption of this measure and its costs to the tax-paying public in the recent overhaul of federal income taxes. Also, see discussions in the earlier [Commentary No. 721](#) and in the opening notes in the *CPI Section* of [Commentary No. 699](#) as to the most-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 increasingly 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 6.1% in October 2018, versus 5.9% in September 2018, 6.3% in August 2018, 6.5% in July 2018, 6.4% in June 2018, 6.4% in May 2018, 6.0% in April 2018, 5.9% in March 2018, 5.8% in February 2018, 5.6% in January 2018, 5.7% in December 2017, 5.8% in November 2017 and 5.6% in October 2017. Those data are reflected in *Graph 1*.

The October 2018 ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, was at about 10.3% (10.29% at the second decimal point), versus 10.0% (10.03%) in September 2018, 10.5% (10.48%) in August 2018, 10.8% (10.75%) in July 2018, 10.7% (10.67%) in June 2018, 10.6% (10.59%) in May 2018, 10.2% (10.23%) in April 2018, 10.1% (10.12%) in March 2018, 10.0% (9.96%) in February 2018, 9.8% (9.81%) in January 2018, 9.8% (9.85%) in December 2017, 9.9% (9.95%) in November 2017 and 9.8% (9.78%) in October 2017. Those data are reflected in *Graph 2*. Historical monthly detail and a related inflation calculator are found in the [CPI](#) section of the Alternate Data tab of the ShadowStats home page: www.ShadowStats.com.

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 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 the [Public Commentary on Inflation Measurement](#) and the discussion prior [Commentary No. 969-Extended](#) for further details).

[Details on Gold and Silver Prices versus Inflation Measures follow on the next page.]

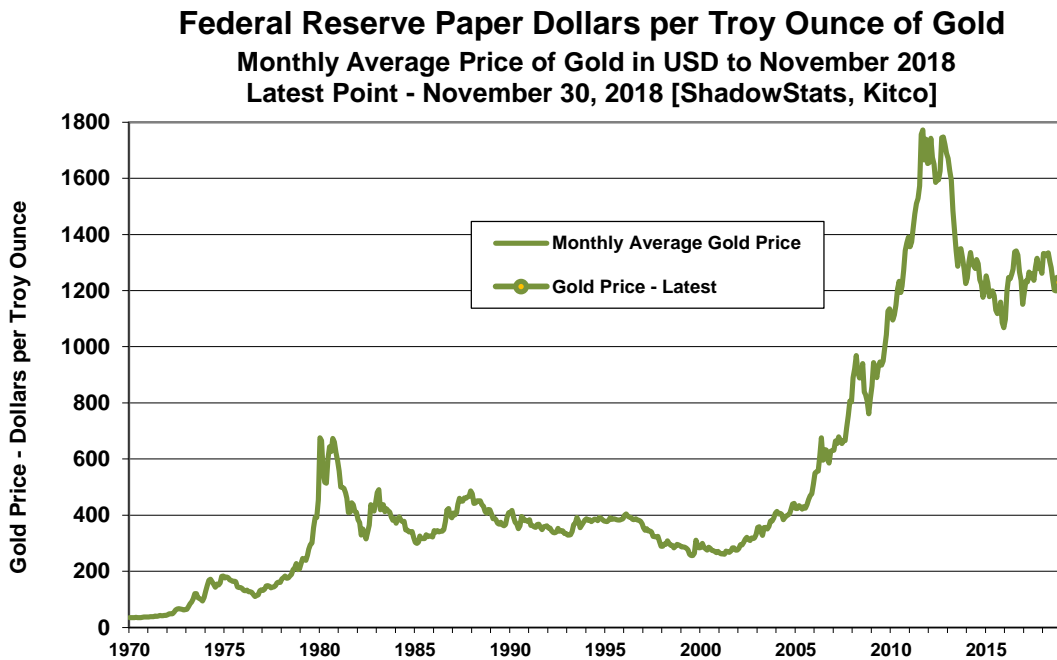
Gold and Silver Historic High Prices Adjusted for October 2018 CPI-U/ShadowStats Inflation

CPI-U: GOLD at \$2,763 per Troy Ounce, SILVER at \$161 per Troy Ounce
ShadowStats: GOLD at \$16,171 per Troy Ounce, SILVER at \$941 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 \$2,763 per troy ounce, based on October 2018 CPI-U-adjusted dollars, and \$16,171 per troy ounce, based on October 2018 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 October 2018 CPI-U inflation, the 1980 silver-price peak would be \$161 per troy ounce, \$941 per troy ounce in terms of the October 2018 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

Graph 3: Monthly Average Gold Price in Dollars (Federal Reserve Notes)



Graph 3 shows the regular historical plot of nominal gold prices, usually published along with monthly CPI Commentary, with extended graphs in the [Hyperinflation Watch – No. 3](#) (and *Hyperinflation Watch – No. 4 [HW-4]* pending). As economic expectations increasingly take hits in the weeks and months ahead, the dollar should continue to back off its recent strength, losing ground against both gold and the stronger currencies such as the Swiss Franc (CHF). Recent, relative short-term U.S. dollar strength has proved somewhat fleeting (again, as will be expanded upon in pending *HW-4*), in what quickly could become a highly inflationary circumstance for those living in a U.S. dollar-denominated world.

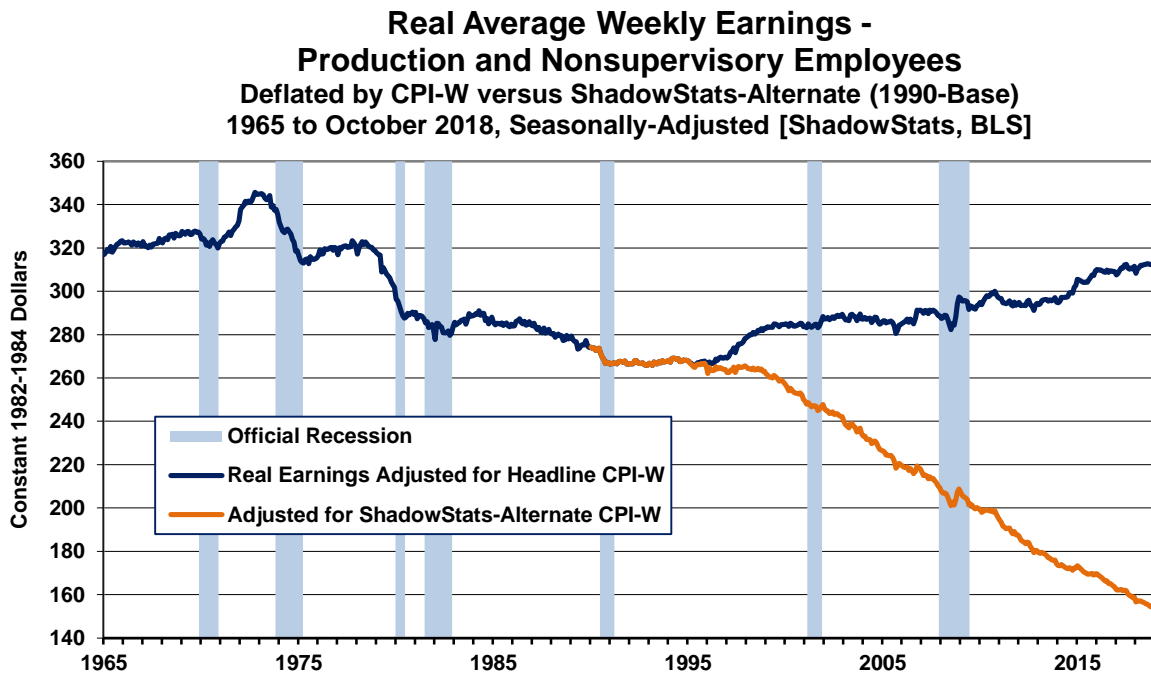
Shown in *Table 1* on page 47 of [No. 859 Special Commentary](#), and in *Table INFLATION-1* on page 46 of [Special Commentary No. 935](#), over the decades, the increases in gold and silver prices have compensated for more than the loss of the purchasing power of the U.S. dollar as reflected by CPI inflation. The precious metals also (particularly gold in the last year) 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).

Real Average Weekly Earnings—October 2018—Continued to Falter for Both the “Production and Nonsupervisory Employees” and “All Employees” Categories. Consumer liquidity stresses intensified in October 2018, with continued faltering of Real Average Weekly Earnings, as reported November 14th by the Bureau of Labor Statistics (BLS) along with the headline CPI-W and CPI-U. These series also were updated in [Consumer Liquidity Watch No. 5](#) of November 21st.

Deflated by CPI-W inflation, real average weekly earnings for the “Production and Nonsupervisory Employees” category dropped by 0.09% (-0.09%) in October 2018, having declined by 0.06% (-0.06%) in September, with unadjusted annual real earnings falling year-to-year by 1.08% (-1.08%) in October 2018, having gained 2.22% in September 2018.

Against a first-quarter 2018 annualized quarterly contraction of 1.22% (-1.22%) in real earnings and unadjusted 0.06% year-to-year growth then, second-quarter 2018 showed an annualized quarterly gain of 2.87%, up by an annual 0.45%, with third-quarter 2018 annualized growth dropping to 0.63%, up by 0.82% year-to-year. The early trend for fourth-quarter 2018 real earnings was for an annualized quarterly contraction of 0.36% (-0.36%), with a year-to-year decline of 0.41% (-0.41%).

Graph 4: Real Average Weekly Earnings, Production and Nonsupervisory Employees, 1965-to-Date
(Graph 5 in [Consumer Liquidity Watch No. 5](#))



That first-quarter 2018 quarterly contraction was the third-consecutive annualized contraction in real average weekly earnings, the fifth quarterly decline in the prior six quarters. Fourth-quarter 2017 earnings showed an annualized drop of 0.39% (-0.39%), versus a minimal decline of 0.03% (-0.03%) in third-quarter 2017, a gain of 3.48% in second-quarter 2017, and contractions of 0.84% (-0.84%) in first-quarter 2017 and 0.18% (-0.18%) in fourth-quarter 2016.

The production and nonsupervisory category is the only series for which there is a meaningful history, and *Graph 4* plots those seasonally-adjusted earnings as officially deflated by the BLS (blue line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (orange 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. Mathematically, when understated inflation is used to deflate income or economic growth, it ends up overstating the inflation-adjusted growth rate.

Nonetheless, official real earnings today still have not recovered their headline 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 or temporarily weakened headline inflation). Deflated by the ShadowStats Alternate CPI-W (1990-Based), 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 deflation using the BLS's headline CPI-W. See the [Public Commentary on Inflation Measurement](#) for further detail.

All Employees Detail. In the broader “All Employees” category (deflated by the CPI-U), which has a more-limited history than the “Production and Non-Supervisory Employees” category, real weekly earnings increased month-to-month by an adjusted 0.15% in October 2018, having declined by 0.06% (-0.06%) in September. Those same real earnings dropped year-to-year for all employees in October 2018 by 1.26% (-1.26%), after gaining 2.72% in September 2018.

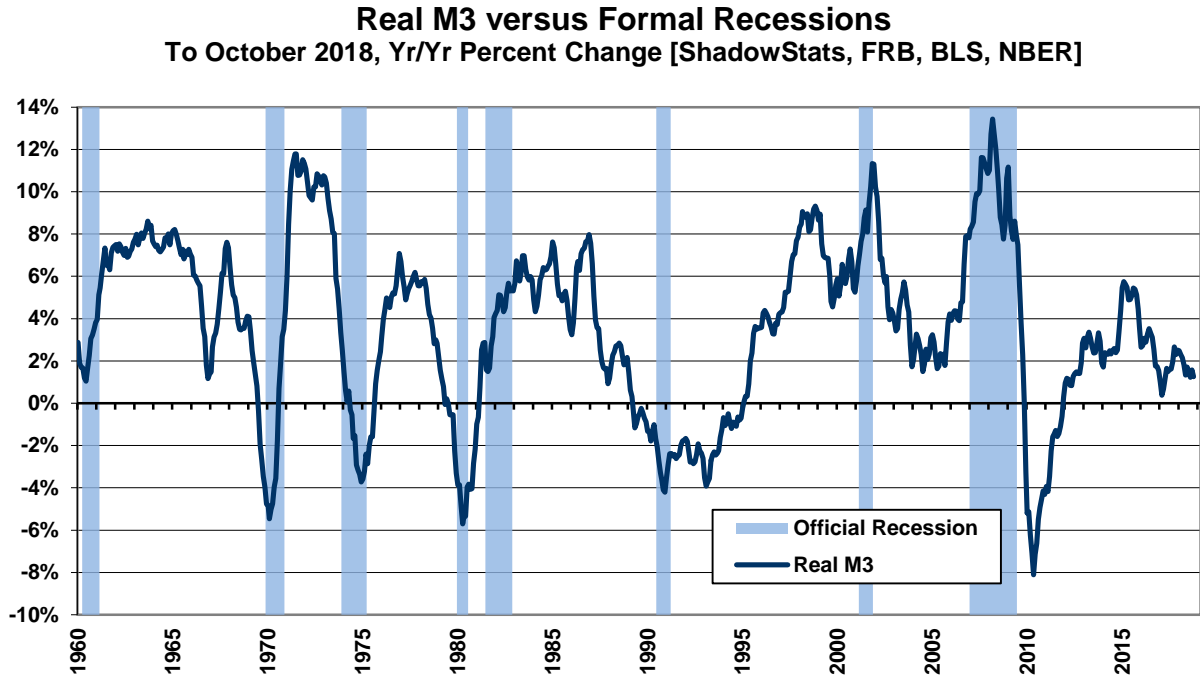
Having followed a broadly similar pattern in 2018 to the reporting of the “Production and Nonsupervisory Employees” in the first three quarters of 2018, the “All Employees” varied in its early trend for fourth-quarter 2018 real earnings, increasing at an annualized quarterly pace of 0.63%. The early trend in year-to-year growth, however, also was for a year-to-year decline, down by 0.35% (-0.35%).

A Leading Indicator to Broad Economic Activity, Real Money Supply M3—October 2018—Annual Change Dropped to 1.26% from 1.58% in September 2018. Annual growth in nominal October 2018 M3, notched lower, but annual CPI-U inflation notched higher, although still somewhat depressed by short-lived, year-ago hurricane-induced disruptions to oil and gasoline prices. Accordingly annual real growth in Money Supply M3 declined to 1.26% in October 2018, from 1.58% in September 2018, versus a sixteen-month low 1.22% August 2018. August 2018 M3 annual growth had declined at a faster pace than annual CPI-U inflation, which also was depressed artificially on the downside (meaning that comparable headline annual inflation would have been higher/real M3 annual growth lower) by year-ago hurricane distortions. Nonetheless, annual growth in real October 2018 M3 dropped back close to the August near-term low.

Nominal annual growth in October 2018 M3 eased to 3.78%, from a revised 3.86% [previously 3.92%] in September, and a revised 3.92% [previously 3.96%, initially 3.97%] in August 2018 and an unrevised 4.44% in July 2018. At the same time, year-to-year change in the October 2018 CPI-U rose to 2.53%

from 2.28% in September 2018, versus 2.70% in August 2018 and 2.95% in July 2018. That combination reduced the level of real or inflation-adjusted annual M3 growth to 1.26% in October 2018, from 1.58% [previously 1.65%] in September 2018, versus 1.22% [previously 1.26%, initially 1.27%] in August 2018 and an unrevised 1.49% in July 2018. Net of the year-ago hurricane distortions that suppressed current headline annual inflation, the series was close to generating a “hard” signal for recession, and would also have come close to such a signal in September 2018, despite the boost in the real headline growth rate.

Graph 5: Real Annual M3 Growth versus Formal Recessions (1960 to October 2018)



For the month of October 2018, annual real growth in Money Supply M3 was 1.26%. On a quarterly basis, third-quarter 2018 annual real growth in Money Supply M3 stood at 1.43%, down from 1.61% in second-quarter 2018, the weakest since 0.68% in first-quarter 2017, which was the weakest seen since a long series of outright monthly year-to-year contractions throughout 2010 and 2011. Net of year-ago hurricane disruptions to current annual CPI inflation, third-quarter 2018 annual real growth in Money Supply M3 would have been 1.22% (instead of 1.47%). The system is close to generating a formal recession signal.

The signal for a double-dip, multiple-dip or simply protracted, ongoing recession, based on annual contraction in the real broad money supply (M3), had been re-triggered/intensified over a year ago, in February 2017. Yet, that signal then softened or flattened out with a contrary bounce from May 2017 into December 2017, turning down anew after the Federal Reserve’s Federal Open Market Committee (FOMC) began more-aggressive tightening in December 2017. The previous recession signal of December 2009 had remained in place, despite real annual M3 growth having rallied into positive territory post-2011.

[Note: If realistic, not headline, inflation numbers were used here, there would be no question of an ongoing negative real annual growth in M3, or a renewed deepening of the economic collapse into 2009, as discussed in [Commentary No. 957](#) and [Public Commentary on Inflation Measurement](#).]

FOMC Policy Is Setting Up a Formal, “New” Economic Downturn. A formal recession signal from low-level or negative annual real money supply growth has become increasingly likely in the near term. That reflects a continued, general weakening trend in nominal annual M3 growth, driven by FOMC policy, in combination with a continued (renewed) pick-up in annual CPI inflation, ex-temporary hurricane distortions. Headline inflation generally has surged recently, driven by unstable political/supply conditions in the oil markets, not by an overheating U.S. economy that the FOMC likes to tout as the reason for its continued spiking of interest rates.

Reflected in *Graph 5*, and noted in prior section, third-quarter 2018 annual real growth in Money Supply M3 stood at 1.47%, its weakest showing in more than year, closing rapidly on signaling a downturn, when annual inflation reporting returns to normal.

What recently had been higher, albeit tepid, real annual growth likely was a temporary reversal in the pattern of plunging annual growth, which had held at levels last seen in plunging growth into the 2009 economic collapse, a level never seen outside an economy falling into, or already in a recession. Today’s *Opening Comments* are relevant here.

The Signal. The signal for a downturn or an intensified downturn in economic activity 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](#), [Commentary No. 902-B](#) and the latest GDP coverage in [Commentary No. 957](#)). 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 a recession signal.

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, from which 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. Actual post-2009 economic activity has remained at relatively low levels—in protracted stagnation—with negligible recovery that already may be sinking anew due to current FOMC policies (see [Commentary No. 970](#) and today’s *Week, Month and Year-Ahead* section.)

[Coverage of the Producer Price Index (PPI) begins on the next page.]

Producer Price Index (October 2018)

October 2018 Goods-Sector PPI Annual Inflation Rose to 3.6% from 3.2% in September 2018, Boosted by Rebounding Energy Prices. Resurgent energy prices and rising Trade Services Margins boosted the October 2018 aggregate Producer Price Index-Final Demand (PPI-FD) inflation to a seasonally adjusted monthly increase of 0.60%, versus 0.17% in September, with unadjusted annual PPI-FD jumping to 2.89% in October 2018, versus 2.64% in September 2018. Annual inflation increased across all three major subsectors: Services, Goods and Construction.

Services Sector. In the somewhat nebulous but dominant (most heavily weighted) Services Sector, broadly affected by profit margins instead of prices, monthly services inflation jumped by an adjusted 0.69% in October, versus 0.26% in September. October 2018 annual inflation rose to 2.44% versus 2.37% in September 2018. The October increase in services inflation reflected surging monthly Trade Services margins for Machinery and Equipment sales. That area involves broadly non-consistent definitional issues, discussed regularly in the *Bulk of Headline PPI Reporting Is of Little Practical Use* section. Accordingly, the index of primary significance in this series, as an indicator of headline inflation, is the Goods Sector, as follows.

Goods Sector. Dominated by Energy prices, PPI Goods monthly inflation jumped by an adjusted 0.61% in October, versus a drop of 0.09% (-0.09%) in September, with annual inflation up by an unadjusted 3.57% in October 2018, versus 3.21% in September 2018.

By subsector, the pattern of increasing annual growth in October 2018 PPI Goods, again, was dominated by the Energy Sector, where unadjusted annual inflation rose to 12.45%, from 9.68% in September 2018. Annual inflation in the “Core” Goods Sector declined to an unadjusted 2.46% in October 2018, from 2.74% in September 2018. Foods Sector annual inflation declined by an unadjusted 0.69% (-0.69%) in October 2018, narrowed from a drop of 1.37% (-1.37%) in September 2018.

Construction Sector. In the Construction Sector, adjusted monthly inflation rose by 1.90% in October, boosted by new quarterly estimates of construction profit margins, versus 0.08% in September, while unadjusted annual inflation jumped to 4.75% in October 2018, versus 3.41% in September 2018. That pattern largely was a repeating artefact of the quarterly update to estimated construction-industry margins, published in the first month of each calendar quarter. As discussed later, where the month-to-month numbers are not comparable, the year-to-year numbers by month generally are.

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, rather than as the hybrid measure of the headline Producer Price Index Final Demand, the aggregate headline series here (ShadowStats separates the analyses of those sectors by sub-category) 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 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. When 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 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 ten years of post-2008-panic data) to establish any meaningful relationship to general inflation or other economic or financial series.

Headline Details of the October 2018 Final-Demand Producer Price Index and Its Major Sub-Sectors. The Bureau of Labor Statistics (BLS) reported Friday, November 9th, that the seasonally-adjusted, month-to-month, headline Producer Price Index Final-Demand (FD-PPI or PPI-FD) inflation for October 2018 was a gain of 0.60%, following a monthly gain of 0.17% in September, having declined by 0.09% (-0.09%) in August, having been unchanged at 0.00% in July and having increased by 0.26% in June.

On a not-seasonally-adjusted basis—all annual growth rates are expressed unadjusted—year-to-year PPI-FD inflation in October 2018 rose to 2.89%, from 2.64% in September 2018, versus 2.83% in August 2018, 3.27% in July 2018 and an 83-month high of 3.28% [previously 3.37%] in June 2018, versus 3.11% in May 2018 and 2.66% in April 2018. October, September and August 2018 annual change numbers here were skewed lower by year-ago hurricane disruptions to (boosting of) oil and gasoline prices, although that effect is waning.

In summary, for the three major subcategories of the October 2018 PPI-FD, which showed an adjusted monthly gain of 0.60%, and an unadjusted 2.89% annual inflation; headline monthly Goods inflation was an adjusted gain of 0.61%, up by an unadjusted 3.57% year-to-year; Services “inflation” (profit margins) gained month-to-month by 0.69%, up by 2.44% year-to-year; and Construction “inflation” was up by an inconsistent 1.90% in the month, up by 4.75% year-to-year.

Final Demand Goods (weighted at 33.02% of the Aggregate Index). Running somewhat in parallel with the old Finished Goods PPI series, headline month-to-month Final Demand Goods inflation in October 2018 gained 0.61%, having declined by 0.09% (-0.09%) in September and having been unchanged at “0.00%” in August. There was positive impact on the aggregate goods monthly reading from underlying seasonal-factor adjustments (tied largely to energy). Not-seasonally-adjusted, October inflation was up by 0.35% for the month. Unadjusted, year-to-year goods inflation in October 2018 showed an annual gain of 3.57%, versus 3.21% in September 2018 and 3.86% in August 2018.

Seasonally-adjusted monthly changes by major components of October 2018 Final Demand Goods:

- “Foods” inflation (weighted at 5.72% of the total index) in October 2018 gained month-to-month by 1.05%, having declined by 0.61% (-0.61%) in September and by 0.60% (-0.60%) in August. Seasonal adjustments were positive for the October change, which was an unadjusted monthly gain of 0.52%. Unadjusted and year-to-year, annual October 2018 foods inflation declined by 0.69% (-0.69%), having declined by 1.37% (-1.37%) in September and by 1.03% (-1.03%) in August.
- “Energy” inflation (weighted at 5.58% of the total index) gained month-to-month in October 2018 by 2.69%, having declined by 0.80% (-0.80%) in September and having gained by 0.36% in August 2018. Seasonal adjustments were positive in October, with unadjusted energy showing a monthly gain of 0.26%. Unadjusted and year-to-year, October 2018 energy prices gained 12.45%, versus 9.68% in September 2018 and 13.62% in August 2018.
- “Less foods and energy” (“Core” goods) monthly inflation (weighted at 21.72% of the total index) was “unchanged” at 0.00% month-to-month in October 2018, having gained 0.17% in September 2018 and having been “unchanged” at 0.00% in August. Seasonal adjustments were negative for monthly “Core” inflation, with the unadjusted monthly October inflation up by 0.34%. Unadjusted and year-to-year, October 2018 “Core” PPI inflation rose by 2.46%, versus 2.74% in September 2018 and 2.65% in August 2018.

Final Demand Services (weighted at 65.33% of the Aggregate Index). Headline Final Demand Services inflation rose month-to-month by 0.69% in October 2018, versus 0.26% in September and having declined month-to-month by 0.09% (-0.09%) in August. The overall seasonal-adjustment impact on headline services inflation was negative, with an unadjusted monthly gain in October of 0.86%. Year-to-year, unadjusted October 2018 services inflation was 2.44%, versus 2.37% in September 2018 and 2.19% in August 2018.

The headline monthly changes by major component for October 2018 Final Demand Services inflation:

- “Services less trade, transportation and warehousing” inflation or the “Other” category (weighted at 40.56% of the total index) rose by 0.17% in October 2018, versus 0.26% in both September and August. Seasonal-adjustment impact on the October detail was negative, where the unadjusted

monthly gain was 0.34%. Unadjusted and year-to-year, October 2018 “other” services inflation was up by 2.64%, versus 2.74% in September 2018 and 2.65% in August 2018.

- “Transportation and warehousing” inflation (weighted at 4.48% of the total index) rose month-to-month by 0.57% in October 2018, versus 1.81% in September and a decline of 0.57% (-0.57%) in August. Seasonal adjustments were negative for October, against an unadjusted monthly gain of 1.06%. Unadjusted and year-to-year, October 2018 transportation inflation rose by 5.82%, versus 5.88% in September 2018 and 5.62% in August 2018.
- “Trade” inflation (weighted at 20.29% of the total index) rose month-to-month in October 2018 by 1.64%, having gained by 0.09% in September and having declined by 0.85% (-0.85%) in August. Seasonal adjustments had a negative impact, where the unadjusted monthly change was a gain of 2.06%. Unadjusted and year-to-year, October 2018 trade inflation increased by 1.54%, versus 0.87% in September 2018 and 0.78% in August 2018.

Final Demand Construction (weighted 1.64% 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 increased by 1.90% in October 2018, bloated as usual for the new quarterly estimate of profit margins, a change posted only in the first month of a quarter. That followed monthly gains of 0.08% in September and August, versus a revised 0.33% [previously 0.41%] in July, a revised 0.17% [previously 0.08%, initially 0.17%] in June, an unrevised 0.08% in May, having jumped by 1.09% in April, by 0.08% in March, 0.08% in February and 0.76% in January. Again, these monthly changes reflect a regular, nonsense monthly distortion in the first month of each quarter, when the BLS introduces new quarterly profit-margin estimates for the sector.

The impact of seasonal factors on the October 2018 Construction reading was neutral, as usual, where the unadjusted monthly change also was a gain of 1.90%. 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.

On an unadjusted basis, year-to-year construction inflation rose to 4.75% in October 2018, versus 3.41% in September 2018, 3.24% in both August 2018 and July 2018, versus a revised 4.23% [previously 4.15%] in June 2018, an unrevised 4.15% in May 2018, 4.24% in April 2018 and 3.57% in March, February and January 2018. Unlike the month-to-month data, the annual changes are reasonably comparable. Annual change here recently has moved closer to the estimates of private surveying and other government estimates (GDP deflators), which usually have shown higher construction-related inflation than does the PPI. Discussed in [Commentary No. 829](#), the Construction Sector PPI has little relationship to real world activity. ShadowStats constructed a Composite Construction Deflator (CCD) used in deflating the Census Bureau’s monthly estimates of Construction Spending Put in Place in the United States (see [Commentary No. 964-A](#)).

PPI-Inflation Impact on Pending Reporting of October 2018 New Orders for Durable Goods. As to the relative reductions in inflation-adjusted real growth, versus the nominal reporting of October 2018 New Orders for Durable Goods, PPI inflation for manufactured durable goods (reported only on a not-seasonally-adjusted basis) increased month-to-month by 0.29% in October 2018, versus 0.17% in September, 0.11% in August, a revised 0.23% [previously 0.17%] in July, a revised 0.29% [previously 0.35%] in June, 0.46% in May, 0.35% in April, 0.41% in March, 0.35% in February and 0.41% in January.

Year-to-year annual inflation eased to 3.24% in October 2018, versus 3.31% in September 2018 (the highest level since 3.29% in August 2011), 3.25% in August 2018, 3.20% in July 2018, a revised 2.90% [previously 2.96%] in June 2018, 2.66% in May 2018, 2.19% in April 2018, 2.08% in March 2018, 1.84% in February 2018 and 1.79% in January 2018. October 2018 New Orders for Durable Goods (both nominal and real) are discussed in the related section later in this *Reporting Detail*.

[Coverage of Retail Sales begins on the next page.]

Retail Sales (October 2018)

Headline October Real Retail Sales Generated an Intensified Recession Signal; Amidst Collapsing Auto Sales, the Headline Monthly Gain Largely Reflected Prior-Period Downside Revisions.

Although increasingly impaired by deteriorating consumer liquidity conditions, the October 2018 headline nominal monthly sales gain of 0.76% beat strong consensus expectations. Yet, that gain was 0.48% net of the downside revision to September activity (August revised lower, too). Those negative revisions were dominated by collapsing auto sales. Net of CPI-U inflation, as calculated by the Saint Louis Fed, the headline real October gain was 0.43%, 0.15% net of revisions.

Net of the CPI-U, annualized third-quarter Real Retail Sales gained a downwardly revised 2.50% [previously 3.05%]. Real annual growth was 1.98% in October 2018, versus 1.89% (previously 2.39%) in September 2018 and 3.59% (previously 3.72%) in August 2018, a pattern of slowing year-to-year growth most commonly seen at the onset of a recession.

Surging automobile sales dominated nominal October headline activity, possibly spiked by insurance-funded hurricane replacements. Yet that gain also was on top of sharp downside revisions to auto sales in September and August, which affected the first revision to third-quarter GDP.

Revised Nominal Motor Vehicle Sales Contracted Third- versus Second-Quarter 2018, Previously Unchanged; Activity Deteriorated Further in October As reported by the Census Bureau, the three-month moving average of nominal motor vehicle sales through October 2018, contracted by 0.6% (-0.6%) versus the three-month moving average through August 2018.

That circumstance deteriorated versus the three-month moving average of nominal motor vehicle sales through September (third quarter) 2018 compared with the three-month moving average through July (second-quarter) 2018, which contracted by a downwardly revised 0.5% (-0.5%) [previously unchanged at 0.0%].

Although month-to-month October 2018 nominal motor-vehicle sales gained 1.2% against downwardly revised activity in September 2018 [a gain of 0.1% net of revisions], October sales dropped by a headline 0.7% (-0.7%) versus year-ago October 2017 sales. Both current and year-ago periods likely reflected some hurricane-recovery boost.

Collapsing and Downwardly Revised Auto Sales and the First Revision to Third-Quarter 2018 GDP. The net first revision to Third-Quarter 2018 Gross Domestic Product (GDP) was zero in aggregate, with annualized real third-quarter growth at 3.50%, unrevised at the second decimal point. Fully discussed in the GDP coverage in [Part II](#), however, there were some meaningful shifts in underlying activity. Again,

personal consumption of motor vehicles revised from an initial third-quarter 2018 annualized real gain of 3.83%, to an annualized real quarterly decline of 1.46% (-1.46%), broadly in line with the retail sales revisions. Inventories rose in revision, with the effect that the unrevised, annualized real third-quarter GDP growth of 3.50%, net of upwardly revised inventory saw annualized real Final Sales growth revise lower, to 1.23% from 1.43%.

Headline Nominal Retail Sales—October 2018. The Census Bureau reported its “advance” estimate of October 2018 [Retail Sales](#) on Thursday, November 15th. The headline, seasonally-adjusted month-to-month gain of 0.76% +/- 0.59% formally was statistically-significant (all confidence intervals are expressed at the 95% level), but such was in the context of unusually negative, prior-period revisions. Net of revisions, the monthly gain was 0.49%, which would not have been significantly different from zero.

The October nominal monthly gain of 0.76%, followed downside revisions that shifted September and August Retail Sales into respective monthly contractions of 0.05% (-0.05%) [previously a gain of 0.10%], and 0.07% (-0.07%) [previously a gain of 0.06%, initially 0.09%]. Unrevised nominal monthly changes held at 0.61% in July, 0.24% in June, 1.24% in May, 0.34% in April, 0.72% in March, 0.10% in February and a contraction of 0.12% (-0.12%) in January.

Year-to-Year Annual Nominal Change. The October 2018 nominal year-to-year change in Retail Sales showed a statistically-significant increase of 4.57% +/- 0.82%, versus revised annual gains of 4.21% [previously 4.72%] in September 2018, 6.37% [previously 6.51%, initially 6.64%] in August 2018 and unrevised annual gains of 6.62% in July 2018, 6.11% in June 2018, 6.38% in May 2018, 4.76% in April 2018, 5.09% in March 2018, 4.53% in February 2018 and 3.95% in January 2018.

October 2018 “Core” Retail Sales, Net of Food and Gasoline. In theory, the nominal October 2018 retail sales environment should have been flat-to-negative for grocery stores, with seasonally-adjusted food prices declining by 0.08% (-0.08%) in October, but positive for gasoline stations, with seasonally-adjusted gasoline prices up by 3.00%, per the Bureau of Labor Statistics (BLS). That said, adjusted retail sales grocery-store sales rose by 0.16%, per the Census Bureau, with seasonally-adjusted gasoline-station sales up by 3.52%.

Given the extreme volatility in headline gasoline prices and sales volume, seasonally-adjusted and otherwise, one has to wonder as to the nature, consistency and significance of the headline reporting and seasonal adjustments being used between these two series, as combined by the Saint Louis Fed in its monthly calculations of Real Advance Retail Sales. Consistent reflection of headline gasoline prices versus gasoline-station sales would have resulted in weaker Real Retail Sales growth in May, June and July and stronger sales growth in August and September, about right for October.

That said, under normal conditions, the bulk of non-seasonal variability in fundamental food and gasoline sales is in pricing, instead of demand. Consistent with the Federal Reserve’s historical preference for ignoring food and energy prices (as though people can live without consuming same), when “Core” inflation is lower than full inflation (at times when the Fed is looking to downplay inflation), “Core” retail sales are estimated here using two approaches:

Version I: Nominal October versus September 2018 seasonally-adjusted retail sales series—net of total grocery store and gasoline-station sales—gained 0.55%, versus the official headline aggregate sales gain of 0.76%.

Version II: Nominal October versus September 2018 seasonally-adjusted retail sales series—net of the monthly *change* in grocery store and gasoline-station revenues—gained by 0.44%, versus the official headline aggregate sales gain of 0.76%.

Frequently discussed, here the seasonal adjustments commonly are unstable, particularly tied to the volatile gasoline-station sales, where neither the Bureau of Labor Statistics (BLS) nor the Commerce Department (Commerce) seems able to come up with meaningful, consistent or stable seasonal adjustments tied to the otherwise erratic gasoline prices.

Structural Liquidity Issues Continue to Impair Retail Sales. An extreme and intensifying consumer-liquidity bind increasingly appears to be constraining retail sales and other consumer activity (see particularly the earnings and consumer credit details in [Consumer Liquidity Watch No. 5](#) and updates in today's *Opening Comments*. Without sustainable growth in, with ongoing patterns of consecutive contractions or no growth in real earnings, and without the ability and/or willingness to take on meaningful new credit 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, at least in theory. That circumstance—in the last ten-plus years of economic collapse and stagnation—has continued to prevent a normal recovery in broad, inflation-adjusted U.S. economic activity.

Of note, the consumer-dependent 72.7% portion of second estimate of third-quarter GDP held even versus the second-quarter 2018, but down from 72.8% in first-quarter 2018, and from 73.1% in fourth-quarter 2017 real GDP activity, reflecting mounting constraints on both consumer consumption and investment. The consumer drives the economy, and a pullback there increasingly should be reflected in almost all other sectors of the economy.

As headline consumer inflation resumes its upside climb in the year ahead, and as overall headline Retail Sales should continue to suffer from the continuing consumer liquidity squeeze, real Retail Sales growth should continue to trend meaningfully lower as seen in the October 2018 detail.

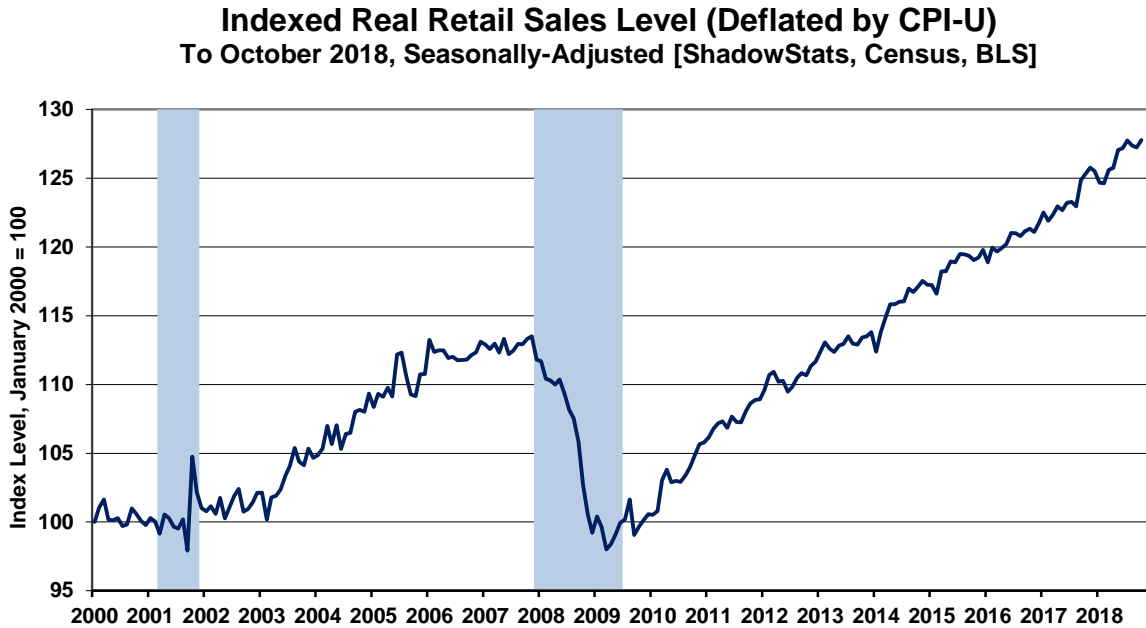
Real Retail Sales Corrected for Understated Inflation and Otherwise. *Graphs 8 and 10* show the headline levels of inflation-adjusted Real Retail Sales activity (deflated by the CPI-U), while *Graphs 9 and 11* show year-to-year percent change. Headline real retail sales peaked with the broad economy (GDP) in fourth-quarter 2007 (December 2007) and collapsed into 2009. The March 2009 trough was followed by a “recovery” into 2012, with headline real retail sales recovering its pre-recession high, and an “expansion” 2013-to-date, with headline activity moving beyond its pre-recession peak level. Those patterns also are reflected here in *Graph 6*.

That “recovery” and “expansion” shown in the headline graphs, however, largely reflected the U.S. government’s deliberate understatement of headline CPI-U inflation. Most economic numbers are viewed net of inflation, so as to get a sense of underlying physical activity and volume in the economy.

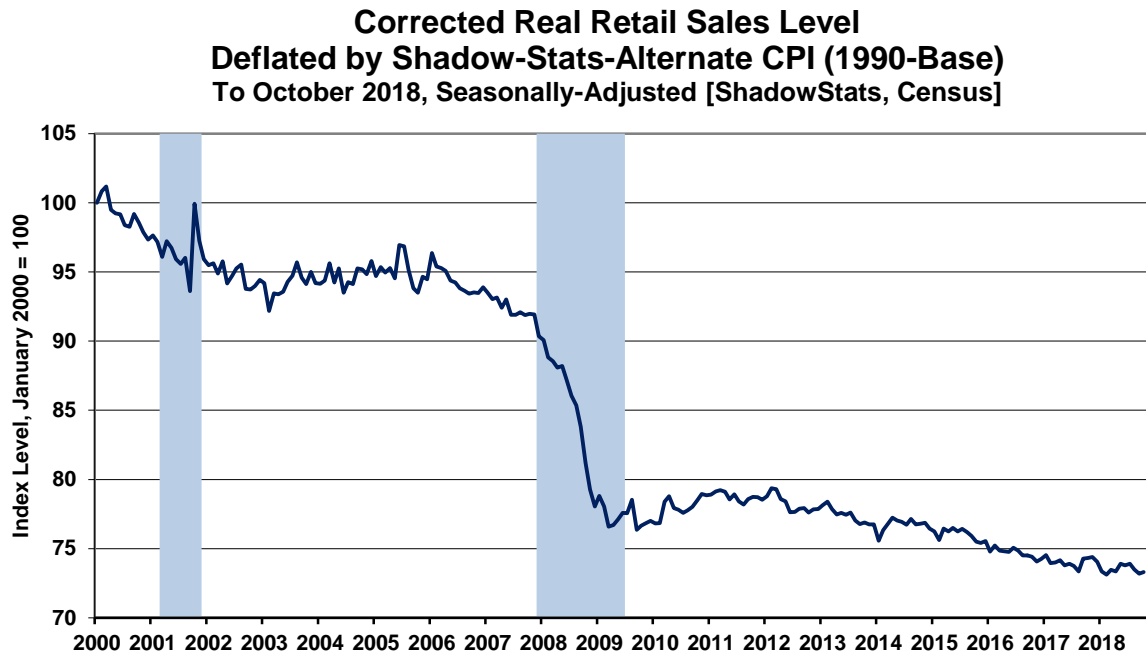
For example, if a retail storeowner noted that sales in October 2018 were up year-to-year by 3.5% from the year-before, there would be some value in knowing that 2.5% of that gain was in inflation, with physical sales (real sales) volume up by 1.0%.

If the inflation estimate used were understated, the resulting “real” or “inflation-adjusted” growth would be overstated. Using the prior example, if sales were up by 3.5%, but inflation was really 4.0%, instead of 2.5%, physical sales volume would have declined by 0.5% (-0.5%) instead of having gained 1.0%.

Graph 6: Headline Real Retail Sales Level, Indexed to January 2000 = 100



Graph 7: "Corrected" Real Retail Sales Level, Indexed to January 2000 = 100



Graphs Reflecting Alternate Inflation-Adjustment. Discussed in the [Public Commentary on Inflation Measurement](#), the U.S. government began changing CPI reporting methodologies back in 1980s so as to reduce headline inflation and inflation-adjusted government outlays, such as Cost of Living Adjustments for Social Security recipients. Also see *Chapter 9* of [2014 Hyperinflation Report—Great Economic](#)

[Tumble](#) – *Second Installment*. These inflation-adjustment issues are separate from seasonal-adjustment issues discussed elsewhere in this section.

Both of the accompanying *Graphs 6* and *7* of Real Retail Sales are indexed to January 2000 = 100.0, so as to maintain consistency with the series of graphs related to corrected inflation-adjustment. Parallel, regular plots of the ShadowStats “corrected” Industrial Production Index are found in that section (see *Graphs 13* and *14*), with “corrected” New Orders for Durable Goods found in that section, *Graphs 37* to *42*. In [Part II](#) of *Commentary No. 978*, see *Graphs 76* and *83* covering the GDP series.

Headline Real Retail Sales—October 2018—Real Sales Rose Monthly by 0.43%, by 0.15% Net of Revisions, With Annual Growth Holding at a Recession-Signal Level of 1.98%. Calculated by the Saint Louis Federal Reserve, [Real Retail Sales](#) deflates the Commerce Department’s Nominal Retail Sales numbers using the headline [Consumer Price Index CPI-U](#), as published by the Bureau of Labor Statistics on November 14th, and covered earlier in this *Reporting Detail*. The headline levels of, and year-to-year changes in, monthly Real Retail Sales are plotted in *Graphs 8* to *11*.

The October 2018 Consumer Price Index showed the seasonally-adjusted CPI-U up month-to-month by 0.33%, versus 0.06% in September, 0.22% August and 0.17% in July.

Year-to-year seasonally-adjusted CPI-U gained by 2.53% in October 2018, versus 2.26% in September 2018, 2.68% in August 2018 and 2.89% in July 2018.

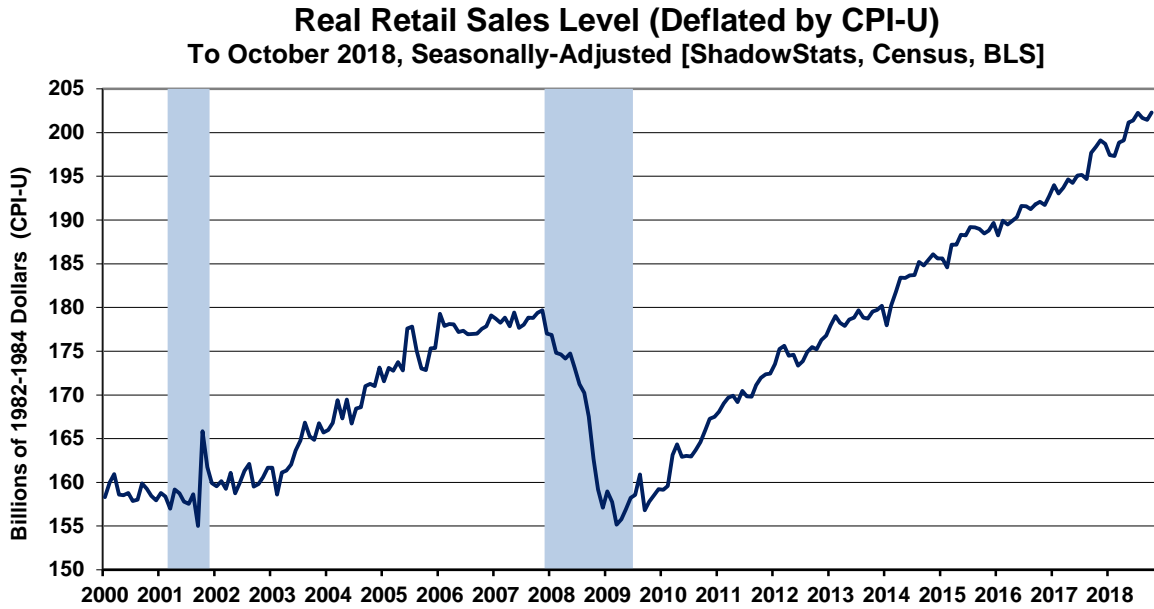
Deflated by the CPI-U, October 2018 Real Retail Sales rose month-to-month by 0.43% [up by 0.15% net of prior-period revisions], having declined in revision by 0.11% (-0.11%) [previously a gain of 0.04%], having declined in August by a revised 0.29% (-0.29%) [previously 0.17% (-0.17%), down initially by 0.14% (-0.14%)] and having gained an unrevised 0.43% in July.

Deflated by the adjusted annual CPI-U, October 2018 annual Real Retail Sales rose by an adjusted 1.98%, versus a revised 1.89% [previously 2.39%] in September 2018, a revised 3.59% [previously 3.72%, initially 3.85%] in August 2018, and an unrevised 3.63% in July 2018. Standardly, annual real growth falling below 2.00% is a solid signal of pending recession.

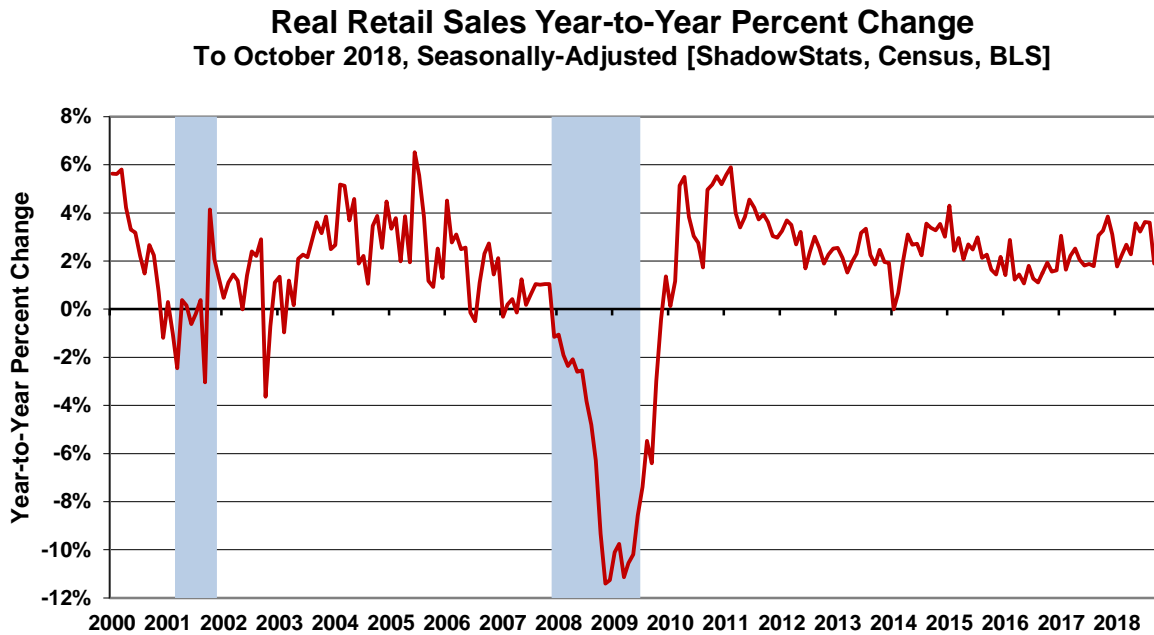
Inconsistent Seasonal-Adjustment Revisions Knocked 0.15% (-0.15%) Off Headline October 2018 Activity. In the context of inconsistent headline reporting of year-ago revisions, just for September 2017 (downside) and October 2017 (even greater downside), year-to-year real growth was depressed artificially by 0.15% (-0.15%) in October 2018. The underlying ShadowStats outlook of minimally-recovering, non-expanding broad economic activity, based partially on key headline reporting being systematically overstated, has not changed (see the earlier *Real Retail Sales Corrected for Inflation Understate and Otherwise* section).

Real Retail Sales Graphs. The first of four graphs following, *Graph 8* shows the level of Real Retail sales activity (deflated by the CPI-U) since 2000; *Graph 9* 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. Again, with recent volatility, including natural-disaster-recovery activity and the related near-term peak in annual real growth in November 2017, that recession signal had been put in temporary abeyance. Yet, with first-quarter 2018 real annual growth at 2.2%, a near-recession signal had been restored, only to disappear anew with year-to-year Real Retail Sales growth in second-quarter 2018 at 3.0% and at a revised 3.0% [previously 3.2%] in third-quarter 2018.

Graph 8: Level of Real Retail Sales (2000 to Date)



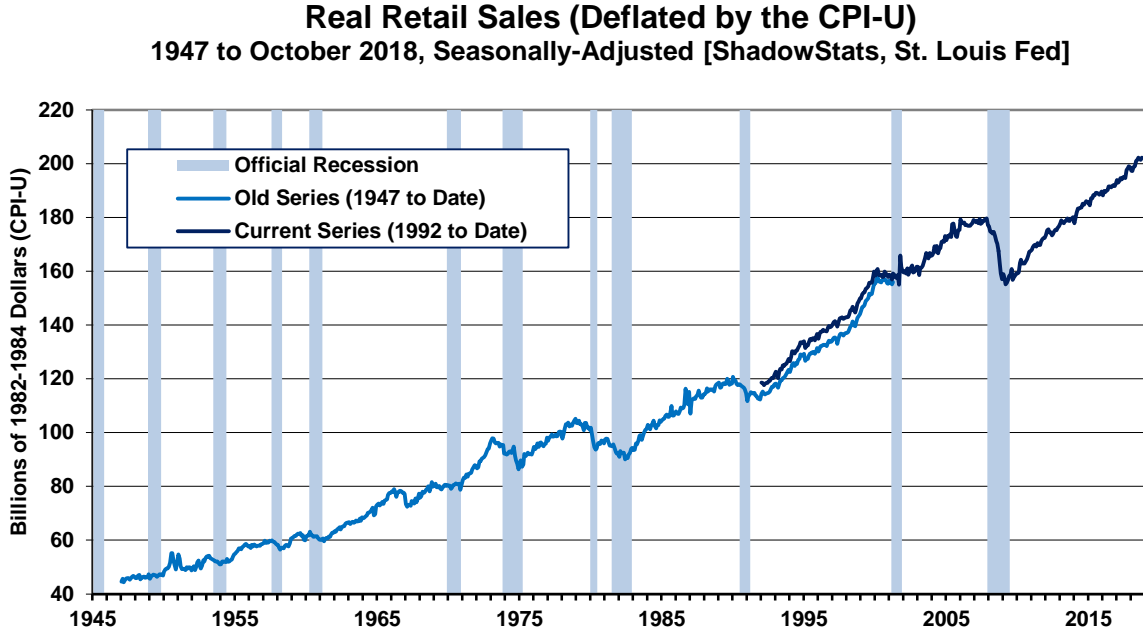
Graph 9: Real Retail Sales (2000 to Date), Year-to-Year Percent Change



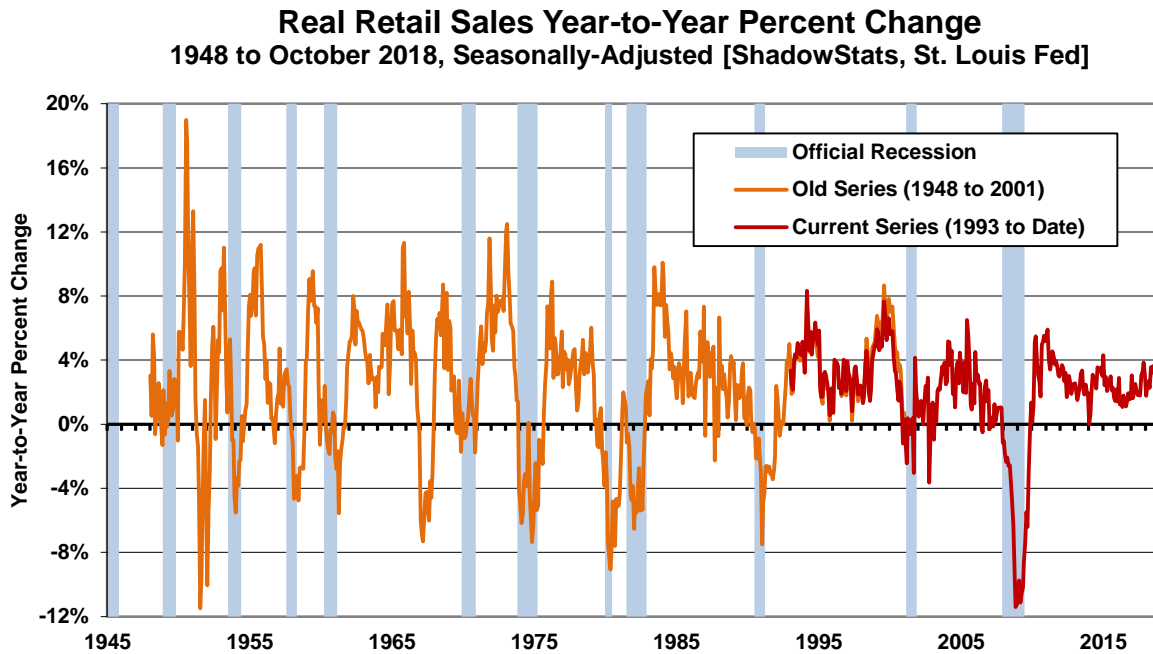
That said, fourth-quarter 2018 is on early track for year-to-year real growth of 1.80%, which, if it holds, would be a solid recession signal. On a monthly basis, real annual growth held at a recession-signal level of 1.98% in October 2018, confirming the intensifying, revised recession signal of 1.89% [previously

2.39%] in September 2018, both harbingers of fourth-quarter activity. *Graphs 10 and 11* show the level of, and annual growth in, real retail sales (and predecessor series) in full post-World War II detail.

Graph 10: Level of Real Retail Sales (1947 to Date)



Graph 11: Real Retail Sales (1948 to Date), Year-to-Year Percent Change



Inflation-Adjusted Series Showed a Catch Up Quarterly Slowing in Third-Quarter 2018, Still Well Off a Sharp, First-Quarter Quarterly Contraction. As reported by the Saint Louis Federal Reserve in its regular deflation of nominal retail sales using the CPI-U, the headline, inflation-adjusted or real first-quarter 2018 Retail Sales contracted at a revised, annualized quarterly pace of 1.75% (-1.75%) [previously 1.67% (-1.67%)], the weakest quarter since second-quarter 2012. Such at least partially reflected a sharp easing from fourth-quarter 2017 natural-disaster-recovery boosts. With second-quarter 2018 reporting showing a rebound to an unrevised 5.53%, the second estimate of third-quarter 2018 activity backed off to a revised 2.50% [previously 3.05%], with the first estimate of October 2018 activity suggesting an early slowing of fourth-quarter 2018 annualized real activity to 1.05%.

[Coverage of Industrial Production begins on the next page.]

Industrial Production (October 2018)

October 2018 Auto Production Collapsed, While Annual Growth Slowed Sharply Across All Major Production Sectors, Despite Heavily Distorted, Massive Upside Revisions to August Mining.

October Industrial Production saw unusually large upside revisions to August 2018 oil and gas production (Mining Sector) and other areas, which altered certain recent headline production patterns (detailed in *Table I*). Nonetheless, October 2018 year-to-year growth slowed sharply not only in the aggregate production series, but also in each of the Manufacturing, Mining and Utilities Sectors, against heavily bloated September 2018 annual growth rates, both before and after the sharp upside revisions.

What had been an annualized third-quarter 2018 production gain of 3.3% revised higher to 4.7%. Still, year-to-year production slowed to 4.11% in October 2018, versus a revised 5.60% (previously 5.14%) in September 2018. The upside revision to the September 2018 annual growth by 0.46% reflected the cumulative impact of unusual upside revisions to Mining and Manufacturing in August 2018. October Headline Production gained a weaker-than-expected 0.10% (up 0.54% net of revisions) month-to-month.

October 2018 Manufacturing gained 0.28% (up 0.53% net of revisions) in the month, despite collapsing automobile production [assemblies were down by 4.2% (-4.2%) in the month]. Year-to-year growth, however, eased to 2.68%, from an upwardly revised annual gain of 3.76% (previously 3.50%) in September 2018. That annual growth upside revision reflected the aggregate impact of upside revisions to the Manufacturing Sector in July through September.

October Mining declined by 0.31% (-0.31%) in the month, having gained 1.18% net of revisions. Year-to-year change in October 2018 Mining slowed to 13.14%, from a revised 15.12% [previously 13.42%] in September 2018, and from a revised 16.76% [previously 14.35%] in August 2018. Some of the monthly spike to August Mining, which was a revised monthly gain of 2.42% [previously 0.38%], appears to have been shifted around or taken back in September and October 2018. Again, where monthly October 2018 declined by 0.31% (-0.31%), September declined by 0.14% (-0.14%) [previously having gained 0.46%].

Driven largely by unusual weather patterns and disruptions, October Utilities dropped by 0.48% (-0.48%) [down 0.42% (-0.42%) net of revisions], having declined by 0.13% (-0.13%) [previously 0.01% (-0.01%)] in September, with annual growth slowing to 1.73% in October 2018, versus a revised 5.48% [previously 5.42%], again, as detailed in *Table I*.

Table I: Industrial Production and Its Major Sectors

Table I: Index of Industrial Production (IIP) and Major Sectors to October 2018 by Month, 2012 = 100.000 for All Indices								
Measure	Weight	Oct '18	Sep	Aug	Jul	Jun	May	Apr
IIP Index	100.0%	109.065	108.953	108.785	107.908	107.464	106.778	107.662
- Prior		--	108.482	108.209	107.823	107.457	106.781	107.662
Mo/Mo		0.10%	0.15%	0.81%	0.41%	0.64%	-0.82%	1.14%
- Prior		--	0.25%	0.36%	0.34%	0.63%	-0.82%	1.14%
Yr/Yr		4.11%	5.60%	5.42%	4.14%	3.56%	2.96%	3.81%
- Prior		--	5.14%	4.86%	4.06%	3.55%	2.96%	3.81%
Manufacturing	75.5%	105.378	105.086	104.814	104.372	104.014	103.274	104.267
- Prior		--	104.820	104.564	104.300	103.999	103.277	104.267
Mo/Mo		0.28%	0.26%	0.42%	0.34%	0.72%	-0.95%	0.56%
- Prior		--	0.24%	0.25%	0.29%	0.70%	-0.95%	0.56%
Yr/Yr		2.68%	3.76%	3.34%	2.67%	2.03%	1.43%	1.98%
- Prior		--	3.50%	3.09%	2.60%	2.02%	1.44%	1.98%
Mining	14.1%	126.315	126.711	126.892	123.897	122.790	120.660	119.455
- Prior		--	124.844	124.276	123.810	122.825	120.702	119.455
Mo/Mo		-0.31%	-0.14%	2.42%	0.90%	1.77%	1.01%	0.88%
- Prior		--	0.46%	0.38%	0.80%	1.76%	1.04%	0.88%
Yr/Yr		13.14%	15.12%	16.76%	13.35%	12.11%	11.22%	10.75%
- Prior		--	13.42%	14.35%	13.27%	12.15%	11.25%	10.75%
Utilities	10.4%	104.738	105.244	105.377	104.233	104.078	105.729	108.490
- Prior		--	105.183	105.195	104.065	104.076	105.687	108.490
Mo/Mo		-0.48%	-0.13%	1.10%	0.15%	-1.56%	-2.55%	5.77%
- Prior		--	-0.01%	1.09%	-0.01%	-1.52%	-2.58%	5.77%
Yr/Yr		1.73%	5.48%	4.78%	2.09%	2.86%	2.88%	8.08%
- Prior		--	5.42%	4.60%	1.93%	2.86%	2.84%	8.08%

Sources: Federal Reserve Board, ShadowStats

Manufacturing Sector Showed a Record 130th Straight Month of Economic Non-Expansion. Indeed, October 2018 Manufacturing gained 0.3% in the month, yet headline Manufacturing activity still held shy by 4.3% (-4.3%) of recovering its pre-recession peak on both a monthly basis against December 2007, and by 4.6% (-4.6%) on a quarterly basis for third-quarter 2018 versus fourth-quarter 2007. Such is in contrast with the headline third-quarter 2018 GDP, which stands at a headline 18.5% above its fourth-quarter 2007 pre-recession peak.

Accordingly, the dominant Manufacturing Sector of the Industrial Production series now has logged a record string of 130 straight months of economic non-expansion, a circumstance never before seen in the 100-year history of Industrial Production reporting, as reflected in *Graph 22*.

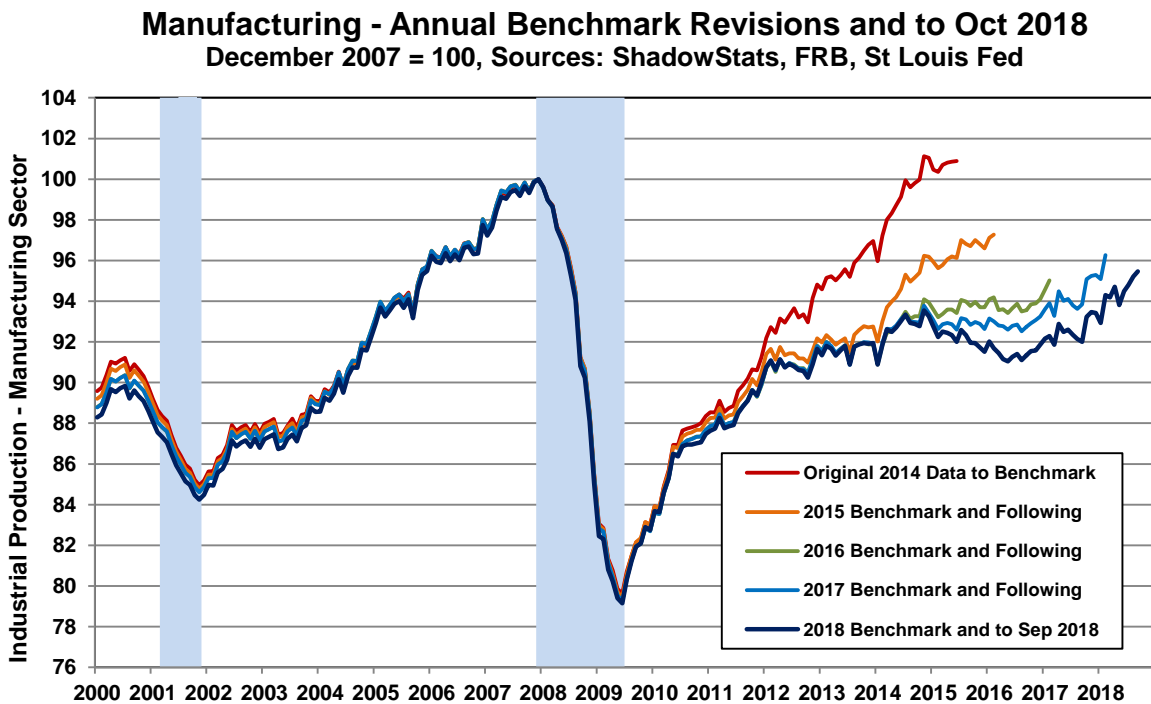
Headline Monthly and Annual Details. The November 16th publication of the headline change in October 2018 Industrial Production activity by the [Federal Reserve Board](#) came in below expectations,

but that was in the context not only of upside revisions to the levels of September 2018, but also of sharp declines in October 2018 year-to-year growth versus September 2018 annual gains. The October 2018 aggregate Industrial Production headline monthly gain of 0.10%, followed a revised 0.15% [previously 0.25%] gain in September and a revised 0.81% [previously 0.36%, initially 0.44%] in August.

Year-to-year, October 2018 Industrial Production gained 4.11%, versus a revised 5.60% [previous 5.14%] in September 2018 and a revised 5.42% [previously 4.86%, initially 4.88%] in August 2018.

The easiest way to review these numbers is look at the revised detail in *Table I*, particularly the index levels, as opposed extensive descriptors used in the text, which likely would not give as clear a picture as simply looking at the numbers.

Graph 12: Annual Benchmark Revisions to the Dominant Manufacturing Sector of Industrial Production



Growth by Major Sector. Detailed by major industry group (see *Graphs 18, 20, 27 and 29*), the October 2018 aggregate Industrial Production monthly gain of 0.10%, broke out by component sector as a monthly gain of 0.28% in Manufacturing, and declines of 0.31% (-0.31%) in Mining and 0.48% (-0.48%) in Utilities.

In the wake of the July 27th Comprehensive Benchmark Revision to GDP, the ShadowStats estimate of the GDP Series Corrected for Understatement of Headline Inflation (as plotted in *Graph 73* of pending *Part II*, and which is virtually identical to *Graph OC-8* in *Commentary No. 976*) increasingly resembled patterns of activity seen the in Manufacturing Sector and Real New Orders for Durable Goods Ex-Commercial Aircraft, as plotted and compared in today's *Opening Comments* section with the CASS Freight Index™ (*Graphs OC-4 to OC-9*), see also *Sections I and II* of *Special Commentary No. 968-*

[Extended](#) of September 6th for the comparative details with the benchmarked GDP and Real New Orders for Durable Goods, Ex-Commercial Aircraft and other series).

Separately, the recent comprehensive GDP Benchmarking showed no obvious impact to the aggregate historical GDP activity from the recent downside benchmarking of Industrial Production, Manufacturers' Shipments and New Orders for Durable Goods, etc., such as reflected here in prior *Graph 12*.

Production Activity and Graphs—Corrected and Otherwise. Reflecting the broadly-negative, March 23rd annual benchmark revisions to Industrial Production, and subsequent monthly revisions through the headline October 2018 detail, index-level and annual-growth production details are found in and plotted in *Graphs 16 to 19*, along with the drill-down graphs of major subcomponents of the production series in *Graphs 20 to 35*.

The level of headline production showed a topping-out process in third- and fourth-quarter 2014, followed by deepening quarterly downturns into first- and second-quarter 2015, with the second-quarter 2015 also beginning a string of quarterly year-to-year contractions into second-quarter 2016, dropping sharply into negative quarter-to-quarter growth and continuing year-to-year decline. Third-quarter 2016 growth was positive on a quarter-to-quarter basis, but continued in annual contraction. That pattern repeated in fourth-quarter 2016. That seventh straight quarter of annual contraction was a circumstance never seen in industrial production reporting outside of periods that eventually were recognized formally as recessions. Looking at the accompanying post-benchmarking *Graph 13*, and the longer-term *Graphs 16 and 17*, it looks like there was a missing recession call beginning at the end of 2014, but, again, nothing like that was suggested in the GDP benchmark revisions.

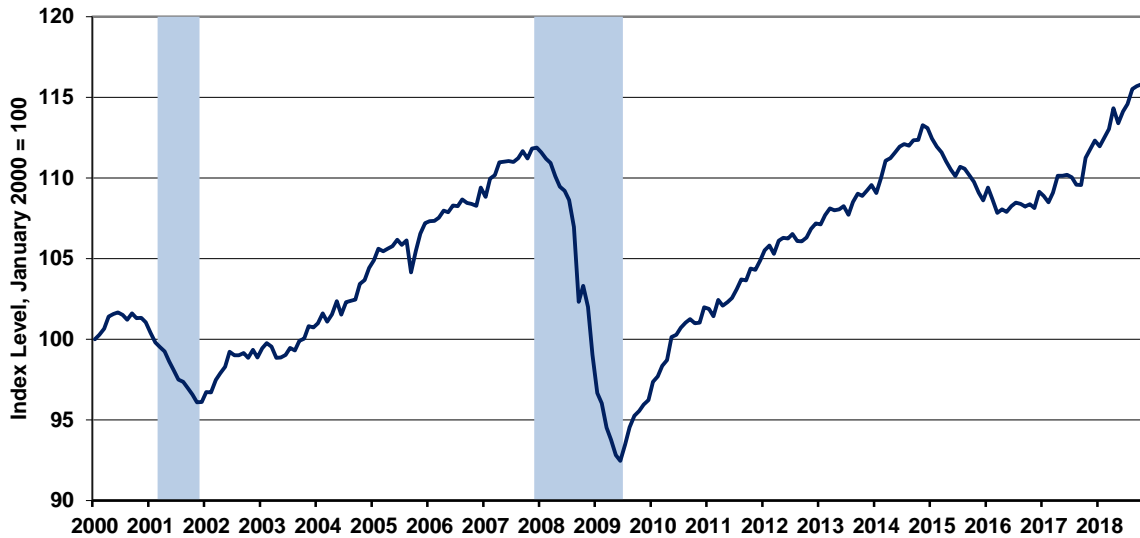
With the reporting of quarterly details in 2017 and the first-three quarters of 2018, production showed both annual and quarterly gains, except for a hurricane-disrupted quarterly contraction in third-quarter 2017. The headline activity still remained below pre-recession highs seen in 2007, except for a brief recovery in third-quarter 2014, and one-quarter's expansion in fourth-quarter 2014, below which first-quarter 2018 fell, although second- and third-quarter 2018 now have recovered.

On a monthly basis, the pre-recession high of November 2007 was recovered briefly in June of 2014, with October and November 2014 a short-lived peak. October 2017 reporting recovered the monthly pre-recession high, for a second time, with a reset to December 2017, in the context of the recent benchmark revisions. Given that benchmarking and subsequent reporting, the initial first-quarter 2018 Industrial Production reporting, the series had regained the fourth-quarter 2014 recovery peak for second time, albeit only by 0.12%, having lost that status in the March 2018 benchmarking. As of the October 2018 reporting, that level had been topped by 2.25%, last regaining that peak in revised April 2018 reporting.

Graphs 13 and 14 address reporting-quality issues tied just to the overstatement of headline growth in the total Industrial Production series that results directly from the Federal Reserve Board using too-low an estimate of inflation in deflating some components of its production estimates into real-dollar terms, for inclusion in the Index of Industrial Production. Hedonic quality adjustments to the inflation estimates understate the inflation rates used in deflating those components; this overstates the resulting inflation-adjusted growth in the headline industrial production series (see [Public Comment on Inflation](#) and [Chapter 9 of 2014 Hyperinflation Report—Great Economic Tumble](#)).

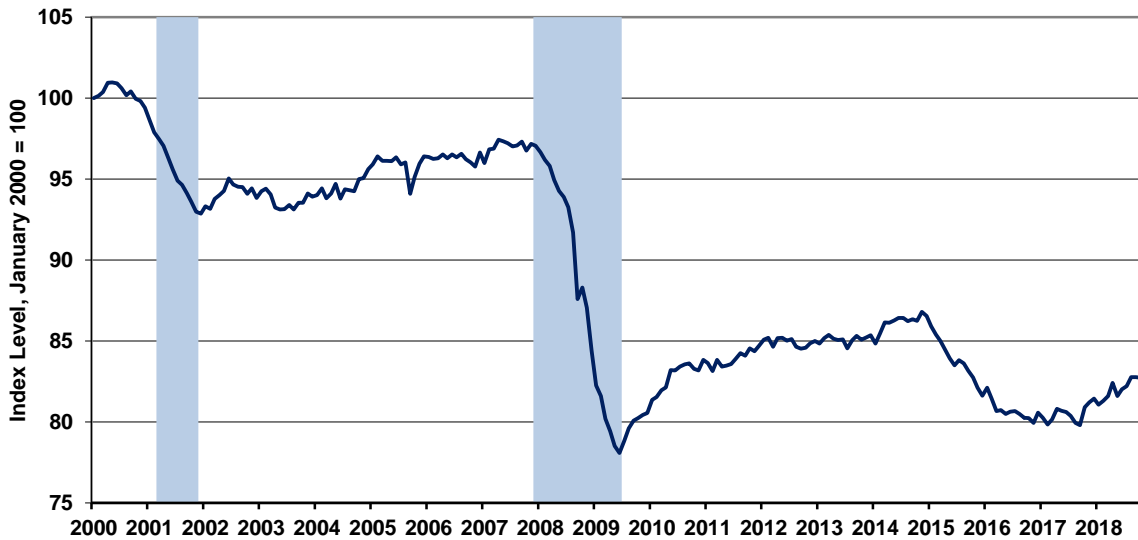
Graph 13: Indexed Headline Level of Industrial Production (Jan 2000 = 100)

**Industrial Production, Re-Indexed to Jan 2000 = 100
Through October 2018, Seasonally-Adjusted [ShadowStats, FRB]**



Graph 14: Headline ShadowStats-Corrected Level of Industrial Production (Jan 2000 = 100)

**ShadowStats-Corrected Industrial Production
Hedonic-Adjusted Inflation Understatement Removed, Index Jan 2000 = 100
Through October 2018, Seasonally-Adjusted [ShadowStats, FRB]**



Graph 13 shows official, headline industrial production reporting, but indexed to January 2000 = 100, instead of the Fed’s formal index that is set at 2012 = 100. The 2000 indexing simply provides for some consistency in the series of revamped “corrected” graphics including, Real Retail sales (see *Graphs 6 and 7* in the prior *Retail Sales* on page 40), and as discussed there in the *Graphs Reflecting Alternate Inflation-*

Adjustment section. The indexing does not affect the appearance of the graph or reported growth rates (as can be in comparing *Graph 13* here to later *Graph 19*, which has the standard, headline indexing).

Graph 14 is a recast version of *Graph 13*, corrected for the estimated understatement of the inflation used in deflating certain components of the production index. Estimated hedonic-inflation adjustments have been backed-out of the official Industrial Production deflators used for headline reporting.

This “corrected” *Graph 14* shows some growth in the period subsequent to the official June 2009 trough in production activity, but that upturn has been far shy of the short-lived full recovery and the renewed expansion reported in official GDP estimation (see [Commentary No. 869](#) and the *Economy* section of [Special Commentary No. 935](#)). Unlike the headline Industrial Production data and the headline GDP numbers, “corrected” Industrial Production levels never recovered their 2007 pre-recession highs, although, again, the headline aggregate Production index quickly backed off its official “recovery” in late-2014 in the March 2018 benchmarking, only to recovery the 2014 highs again with in April 2018 detail. That said, the dominant manufacturing sector of industrial production never has recovered its December 2007 pre-recession peak, a record period of 10-plus years of economic non-expansion in the 100-year history of the Industrial Production series.

Noted earlier, the now 130-straight months of Manufacturing non-expansion, indeed remains unprecedented in its duration within the 100-year history of the Industrial Production series. While the recently-benchmarked GDP and its initial third -quarter 2018 real GDP reporting showed that series to have expanded by 18.5% above its pre-recession peak, the dominant Manufacturing Sector of Industrial Production still holds shy of recovering its pre-recession high by 4.6% (-4.6%) as of third-quarter 2018, and by 4.3% (-4.3%) on a monthly as of October 2018, versus December 2007.

Quarterly and Annual Production Changes. In the context of March 23, 2018 benchmark revisions sharply to the downside for annual growth and annualized quarterly growth, and the initial estimate of third-quarter 2018 numbers, year-to-year growth rates in quarterly production had continued to slow and then decline, ranging from a positive 1.76% in first-quarter 2015, to year-to-year declines of 0.92% (-0.92%) in second-quarter 2015, 1.49% (-1.49%) in the third-quarter 2015 and 3.37% (-3.37%) in fourth-quarter 2015.

Annual declines continued, down by 2.99% (-2.99%) in first-quarter 2016, by 2.25% (-2.25%) in second-quarter 2016 and by 1.91% (-1.91%) in third-quarter 2016. Fourth-quarter 2016 production contracted year-to-year for the seventh-straight quarter by 0.55% (-0.55%).

First-quarter 2017 annual change rose by 0.16%, the first annual gain since first-quarter 2015. Second-quarter 2017 production gained year-to-year by 1.93%, with third-quarter 2017 showing a hurricane-impaired annual gain of 1.20%.

Reflecting detail published with the headline October 2018 numbers, fourth-quarter 2017 growth was a hurricane-boosted 2.99%, with first-quarter 2018 reporting showing annual growth of 3.38% and second-quarter 2018 showing a fourth estimate of 3.44%. Based on the second full third-quarter 2018 reporting, annual growth was 5.05%, with one-month of fourth-quarter reporting suggesting an early trend of 3.60%.

Annualized Quarter-to-Quarter. Going back to first-quarter 2015 industrial production contracted at an annualized quarterly pace of 3.22% (-3.22%), having gained by 2.74% in fourth-quarter 2014. That was followed by a quarterly contraction of 5.04% (-5.04%) in second-quarter 2015, with a third-quarter 2015

contraction of 0.27% (-0.27%) [previously a gain], followed by a fourth-quarter 2015 contraction of 4.71% (-4.71%).

The first-quarter 2016 annualized quarterly contraction was 1.86% (-1.86%), with second-quarter 2016 down at an annualized 2.09% (-2.09%). Third-quarter 2016 gained at an annualized pace of 1.11%, the first quarterly gain in seven quarters, followed by a gain of 0.70% in fourth-quarter 2016.

The first-quarter 2017 annualized quarterly gain was 0.98%. The second-quarter 2017 gain was 5.01%, with hurricane-disrupted third-quarter 2017 growth now showing an annualized quarterly contraction of 1.54% (-1.54%).

Reflecting detail published with the headline October 2018 numbers, the fourth-quarter activity was up by an unrevised, disaster-recovery-boosted 7.75%, with the first-quarter 2018 at 2.52%, second-quarter 2018 at a revised 5.26% [previously 5.25%, 5.12%, initially 5.96%] and with an second initial estimate of third-quarter 2018 at 4.73% [previously 3.29%], and an early fourth-quarter 2018 indication of 1.92%.

Production Graphs. The regular two sets of long- and short-term plots of industrial production levels and annual growth rates (*Graphs 16 to 19*) set the background for the drill-down detail graphs of various components of the aggregate industrial series (*Graphs 20 to 35*).

Graphs 16 and 17, and *Graphs 18 and 19* show headline industrial production activity to date. *Graph 17* shows the monthly year-to-year percent change in the aggregate series, in historical context since World War I. Post annual benchmarking revisions of recent years, annual growth has slowed consistently as seen in *Graphs Benchmark-1 to 4* in [Commentary No. 942-B](#).

Graph 16 here shows the monthly level of the production index since its inception, post-World War I, with a topping-out and renewed downturn—deepening quarterly contractions in first- and second-quarter 2015 and now, benchmark-revised into second-quarter 2016, turning to the plus-side in second-half 2016 into second-quarter 2017 and third-quarter 2017 hurricane disruptions and accompanying near-term volatility, with mixed reporting into October 2018. Such patterns of monthly and quarterly year-to-year declines post late-2014 to the onset of 2017 (see *Graph 17*) were seen last in the economic collapse into 2009, and historically never seen outside of what would be recognized as formal recessions. *Graphs 15 and 19* show the same series in near-term detail, beginning in January 2000. Such remains in the context of a hurricane-impaired third-quarter 2017 reading and a hurricane-boosted fourth-quarter 2017 into slowing first-quarter and mixed second- and third-quarter 2018 activity.

Seen most clearly in *Graph 20*, year-to-year activity dipped anew in 2013, to levels usually seen at the onset of recent recessions, bounced higher into mid-2014, fluctuated thereafter, turning negative, again, into 2015 and through 2016 as seen previously only in formal recessions. Such suggests a “missing recession call” with a pre-recession peak of fourth-quarter 2014, but that did not surface in the current GDP benchmarking. In the context of the 2018 production benchmark revisions, year-to-year growth remained well off the recent relative peak for the series, which was 8.46% in June 2010, going against the official June 2009 trough of the economic collapse. Indeed, as shown in *Graph 17*, the June 2009 (the end of second-quarter 2009) year-to-year contraction of 15.33% (-15.33%) was the steepest annual decline in production since the shutdown of wartime production following World War II.

Still Fighting the Great Recession. Headline October 2018 Industrial Production currently is relatively stagnant at a minimally-recovered level, versus its pre-Great Recession peak. Third-quarter 2018

production activity was up by 3.30% versus its fourth 2007 pre-recession peak, while third quarter 2018 GDP stood at 18.46% above its fourth-quarter 2007 pre-recession peak.

Following its fourth-quarter 2007 peak, the quarterly production series declined through its cycle trough of second-quarter 2009. That was down by 16.68% (-16.68%) from its pre-recession high. The GDP quarterly trough had the same timing, down by 3.98% (-3.98%) from its pre-recession high.

Production and Underestimated Headline Inflation. Versus the pre-Great Recession peak, official headline production levels have moved higher since their June 2009 trough, showing a pattern of stagnation in slow upside trend, since 2009, with irregular quarterly contractions interspersed. The slow uptrend continued into a topping out pattern in late-2014. Headline growth—purportedly already neutered of any inflation impact—contracted in both first- and second-quarter 2015, moved minimally higher into 2016 through mid-2017, with hurricane hit quarterly contraction, then generally boosted into late-year, by hurricane-recovery boosted activity, with a slowing uptrend into May and June 2018, picking up steam into September 2018, slowing in October 2018

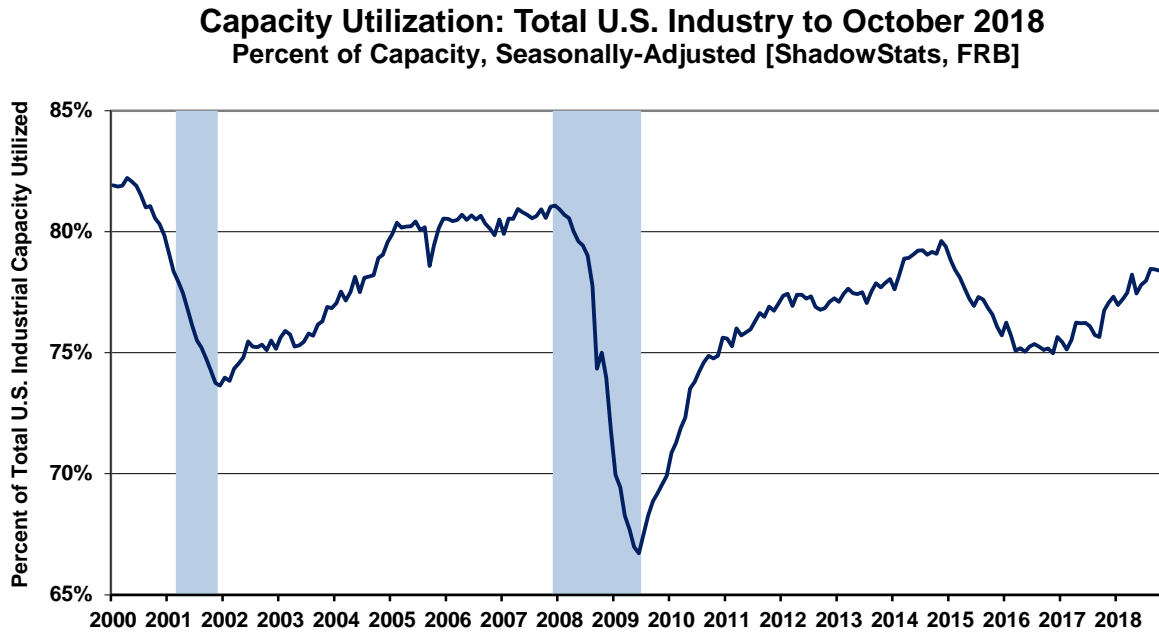
Yet, corrected for the understatement of inflation used in deflating portions of the industrial production index, as shown earlier in *Graphs 13 and 14*, that series contracted quarter-to-quarter throughout 2016 and with some bottoming, leveling off and minimal uptick in 2017, with an upturn/uptrend in the post-disaster recovery into 2018, but still well shy of recovery or expansion.

Revised, Total U.S. Industrial Capacity Eased Minimally in September and October 2018, Versus Its New, Revised Near-Term Peak of August 2018. The Federal Reserve’s Capacity Utilization is an estimate of total Industrial Production versus total Productive Capacity of the United States. ShadowStats has reservations as to the Fed’s ability to measure or estimate productive capacity accurately, as reinforced recently by the nature of the revised plots of Capacity Utilization in the benchmark revisions of [Commentary No. 942-B](#). Accompanying *Graph 15* of the series has been updated for the October 2018 Capacity Utilization Rate of 78.39% versus a revised 78.45% [78.11%] in September and a new near-term high of 78.48% [78.06%] in August 2018, against the prior near-term peak of 78.23% in April 2018.

Against its December 2007 pre-recession peak level of 81.10%, October 2018 Capacity Utilization reading held shy of recovering that peak *level* by 3.23% (-3.23%), or by 271 (-271) basis points in terms of the peak *percentage number*. That is despite October 2018 Industrial Production holding at 3.57% above its December 2007 pre-recession peak, and with the October 2018 Manufacturing Sector holding shy of recovering its December 2007 pre-recession peak by 4.28% (-4.28%).

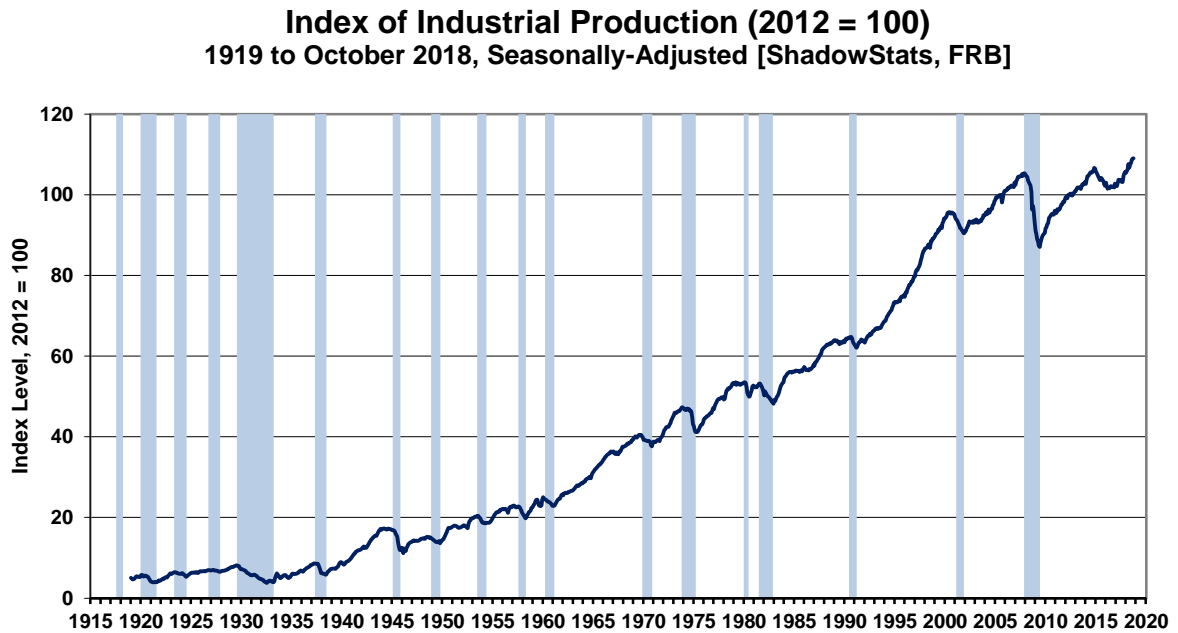
Sharp Downturns in Capacity Utilization Usually Signal the Onset of a Recession. Where sharp downturns in Utilization historically usually mark onsets of formal recessions, such would support the concept of a renewed “headline” recession, a double-dip downturn that began at the end of 2014, as indicated by the Industrial Production series. That remains ShadowStats’ estimate of the timing of a likely “headline” double-dip recession, which formally began at the end of 2007, bottomed in 2009, peaked in late in 2014 and then bottomed anew in 2016, although nothing confirming that showed up in the 2018 comprehensive GDP benchmarking. Contrary to consensus hype of fully recovered and expanding economic activity, as seen in the Manufacturing Sector, much of the headline U.S. economy never has recovered fully from the 2007 downturn.

Graph 15: Utilization of Total U.S. Industrial Production and Manufacturing Capacity (2000 to Date)

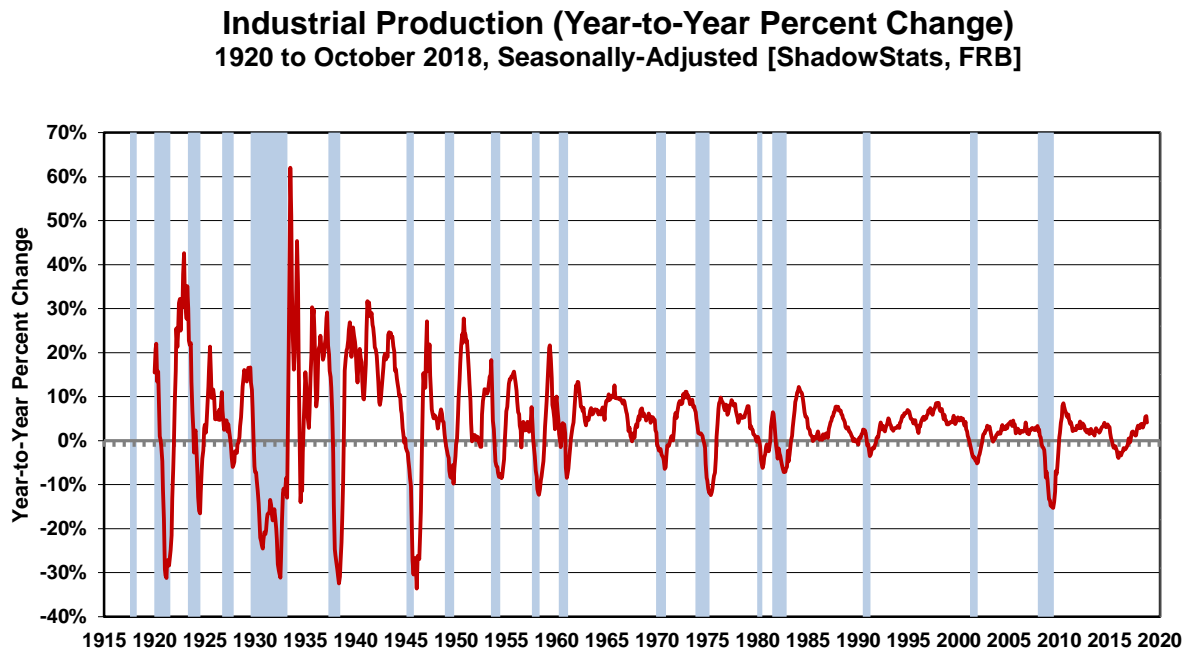


[Graphs 16 to 19 begin on the next page.]

Graph 16: Index of Industrial Production, Full Historical Series 1919 to Date

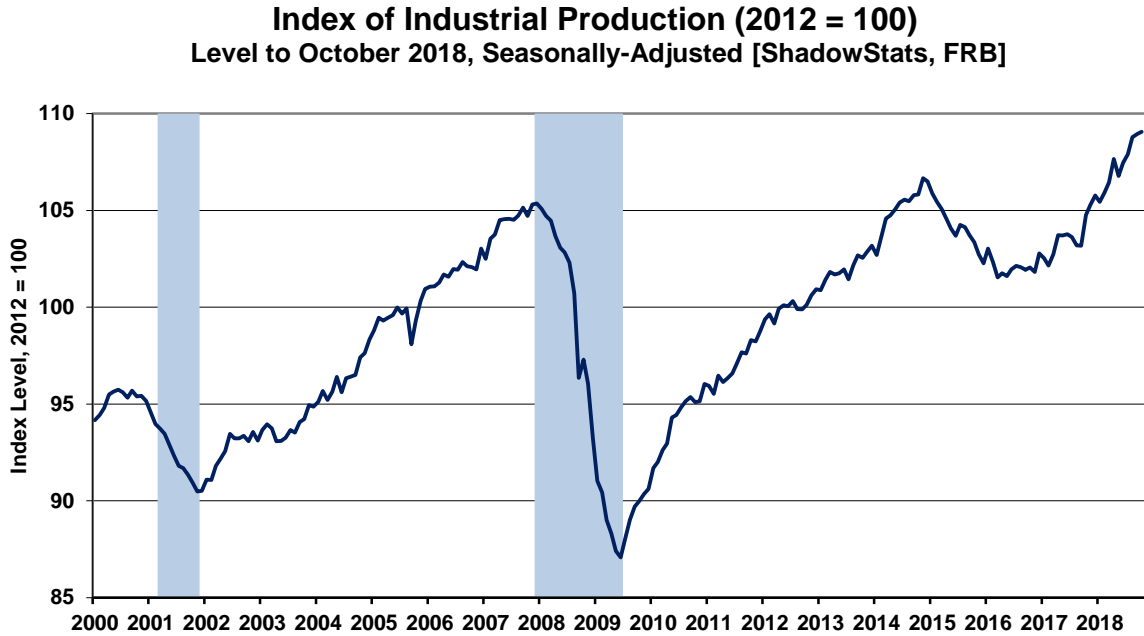


Graph 17: Industrial Production, Year-to-Year Percent Change, Full Historical Series Since 1920

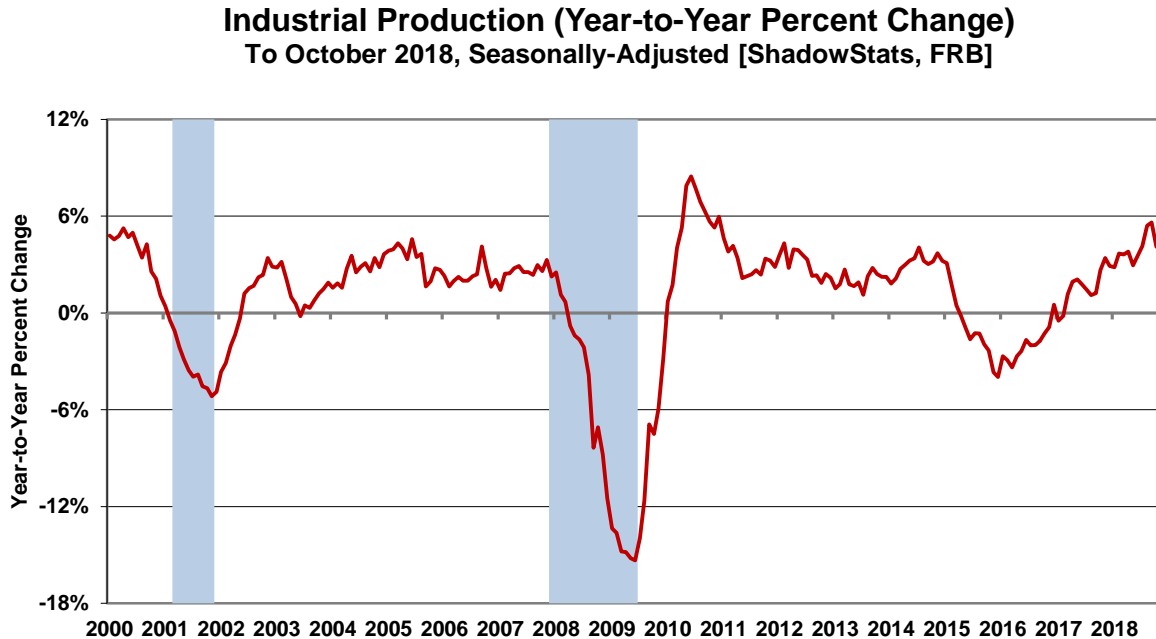


Drilling Down into the October 2018 U.S. Industrial Production Detail. Graphs 18, 20, 26 and 30 show headline industrial production and its major components January 2000 through October 2018.

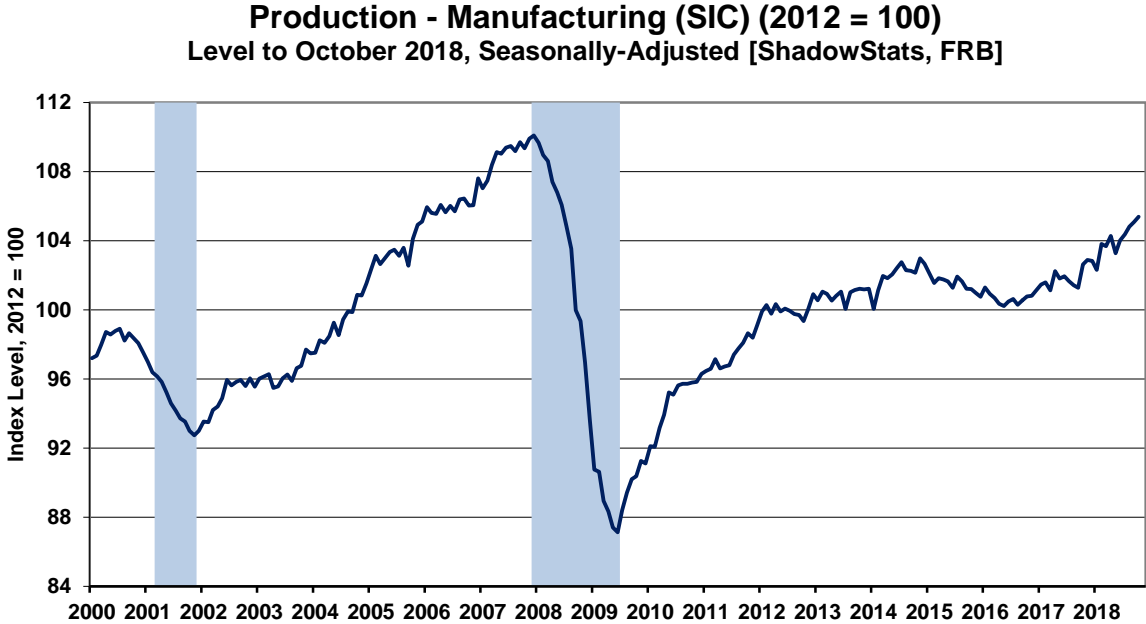
Graph 18: Index of Aggregate Industrial Production, Since 2000



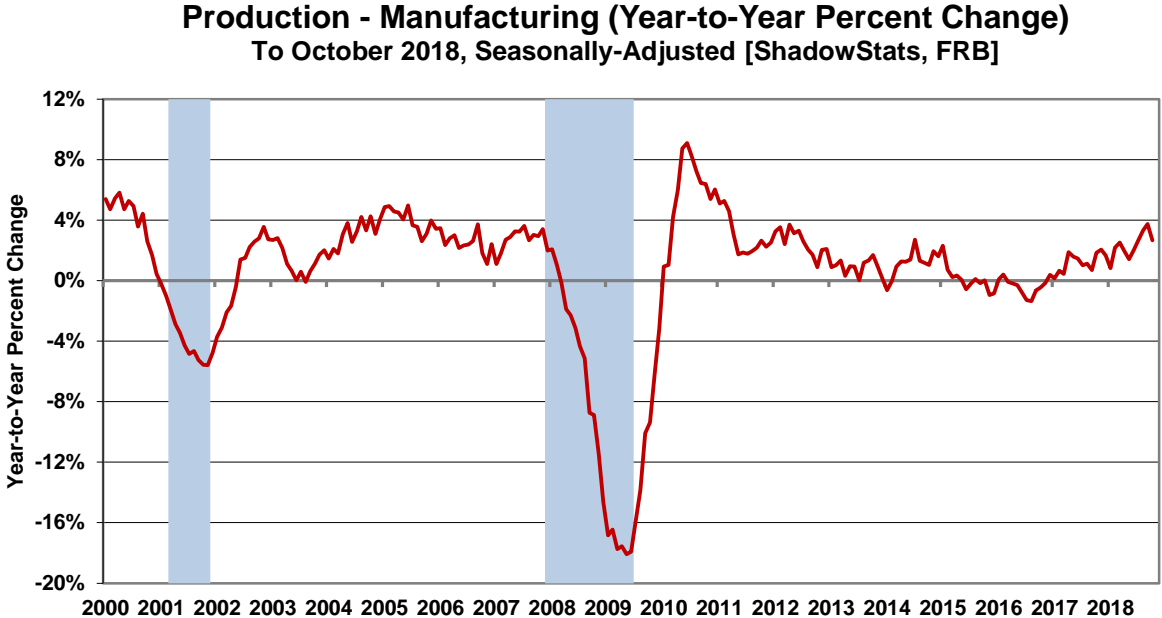
Graph 19: Aggregate Industrial Production, Year-to-Year Percent Change, Since 2000



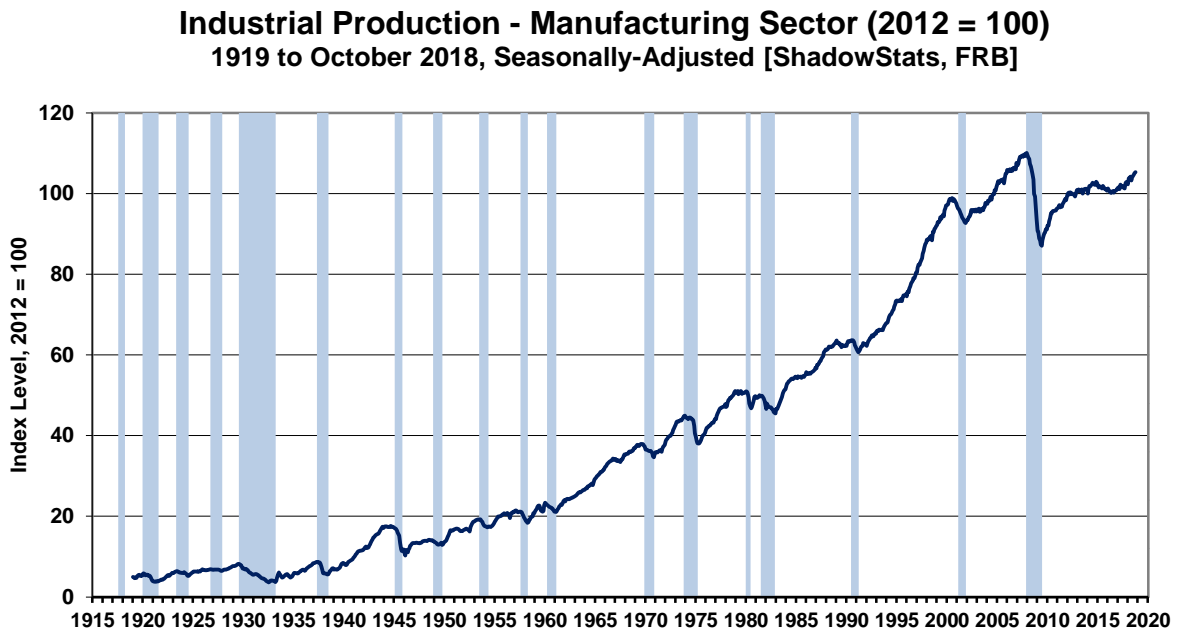
Graph 20: Industrial Production - Manufacturing (75.5% of the IIP in 2017), Since 2000



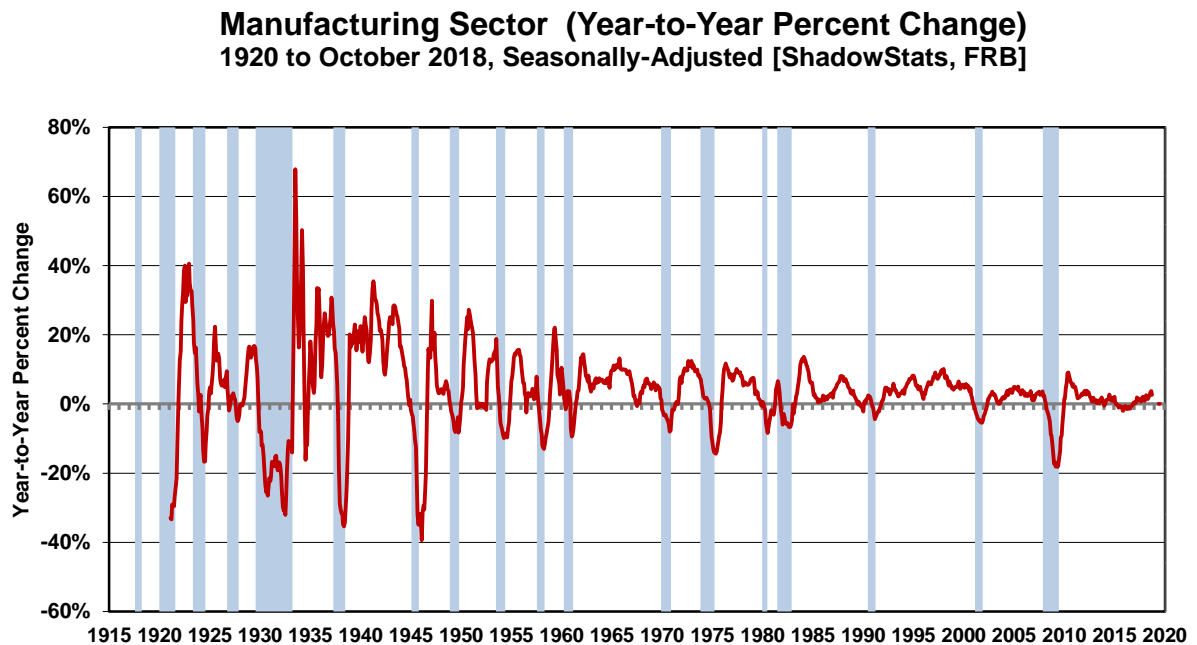
Graph 21: Industrial Production - Manufacturing, Year-to-Year Percent Change, Since 2000
(Same as Graph OC-9 in the Opening Comments)



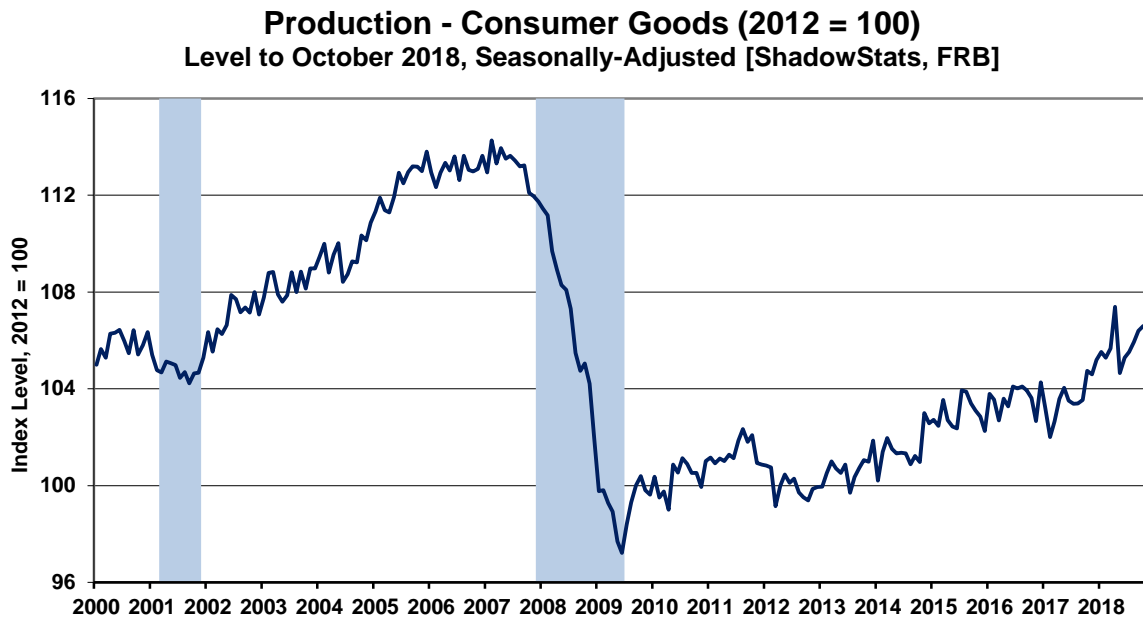
Graph 22: Industrial Production, Manufacturing, Full Historical Series 1919 to Date



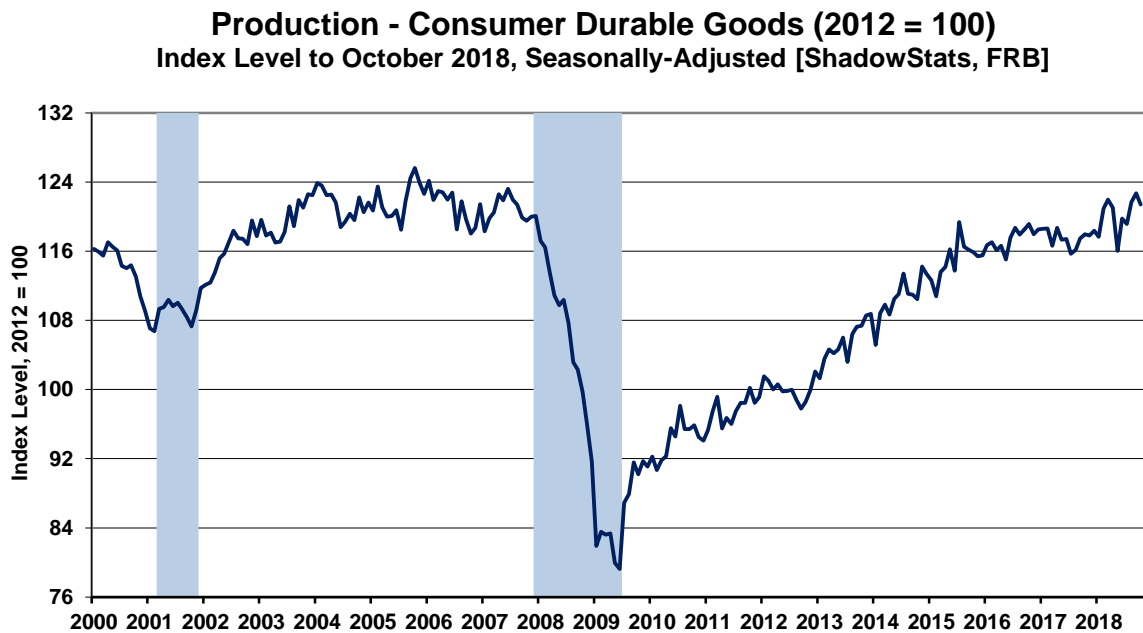
Graph 23: Manufacturing Year-to-Year Percent Change, Full Historical Series Since 1920



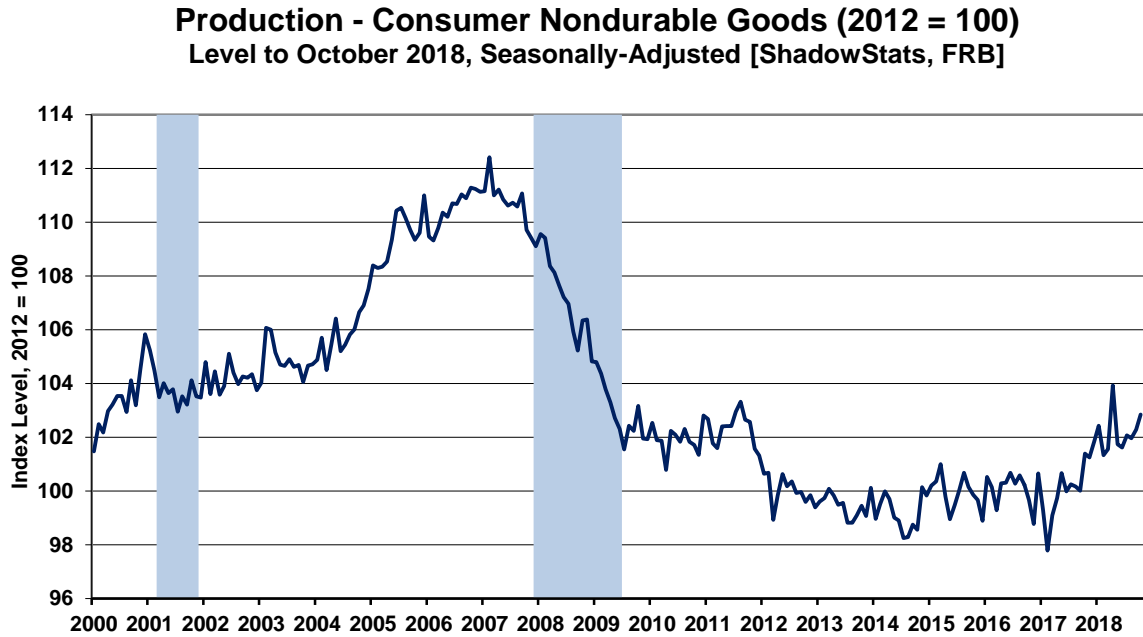
Graph 24: Consumer Goods (28.0% of the Aggregate in 2017), Since 2000



Graph 25: Durable Consumer Goods (6.3% of the Aggregate in 2017), Since 2000



Graph 26: Nondurable Consumer Goods (21.7% of the Aggregate in 2017), Since 2000



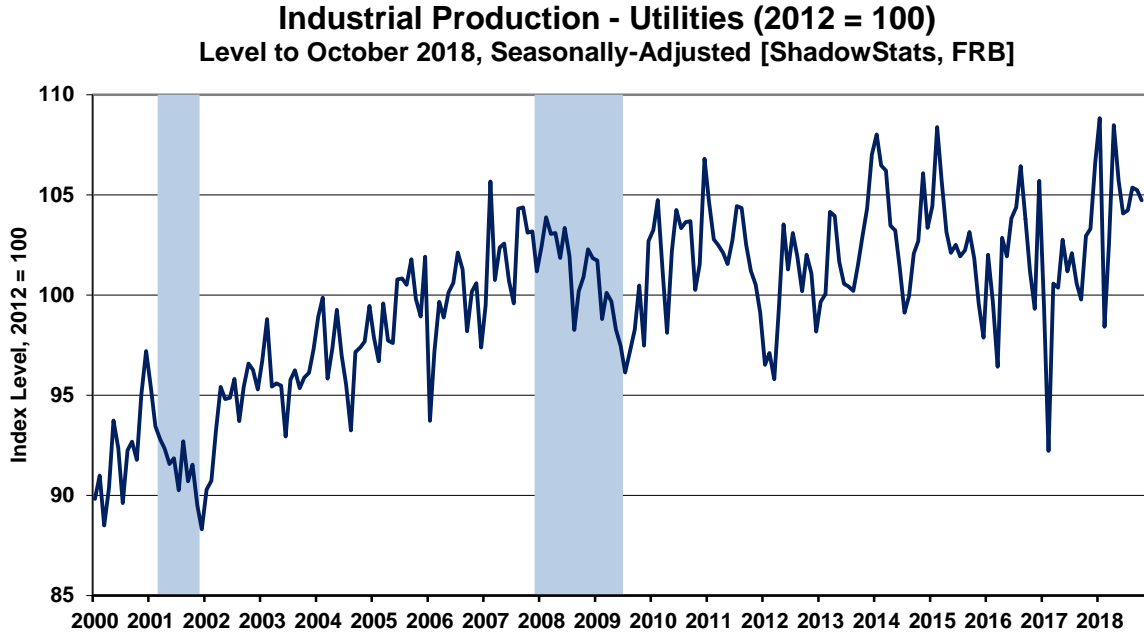
The aggregate production index (*Graph 18*) contracted quarter-to-quarter for six consecutive quarters, from first-quarter 2015 through second-quarter 2016. Year-to-year declines by quarter were seen for seven consecutive quarters, from second-quarter 2015 through fourth-quarter 2016, with first-quarter 2017 activity positive on both a quarterly and annual basis, flipped to fluctuating monthly and quarterly volatility and gains by lingering and varied hurricane disruptions and then waning recovery from same in first-half 2018. Nonetheless, activity generally has continued to pick up going into October 2018.

Shown in *Graphs 20, 27* and *29* are the levels of activity in the three major industry sectors, Manufacturing, Utilities and Mining, where all but Utilities gained month-to-month in September, often affected by revisions to prior index levels as reflected in earlier *Table I*.

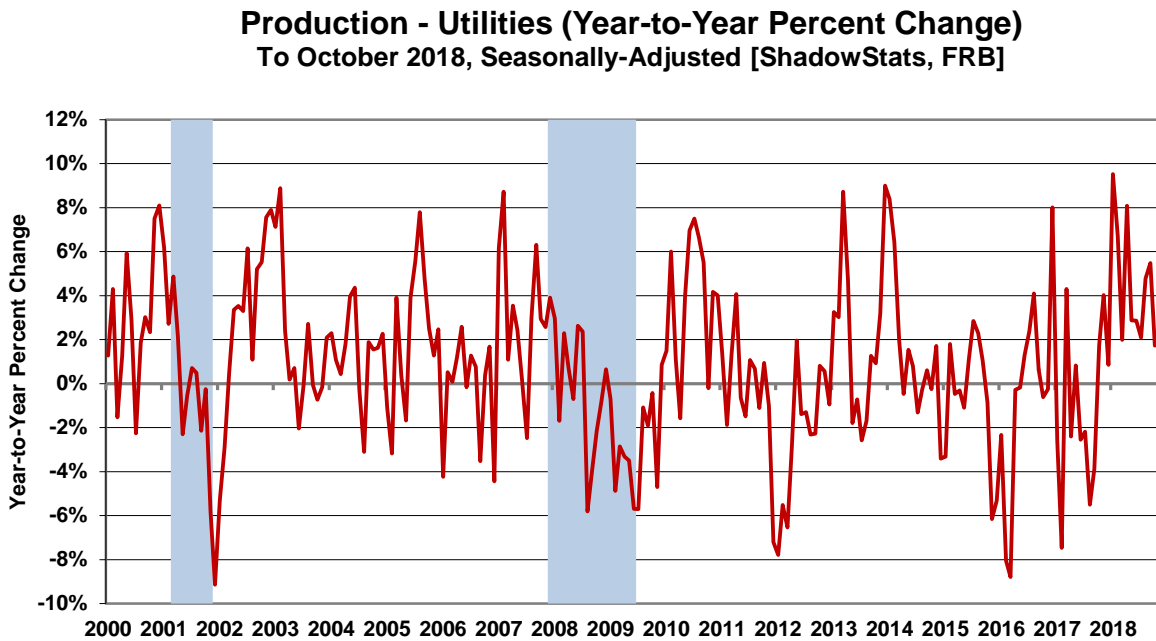
The Manufacturing graphs precede this, while the graphs of Utilities and Mining follow, all updated for the latest detail. *Graphs 21, 28* and *30*, show the respective plots of year-to-year change for those series. The preceding Manufacturing *Graphs 20* to *26* include various levels of consumer goods production (*Graphs 24* to *35*). The next two *Graphs 27* and *28* reflect Utilities activity, massively volatile as a result of regularly unstable weather patterns.

[Graphs 27 to 30 begin on the next page.]

Graph 27: Industrial Production - Utilities (10.4% of the Aggregate in 2017), Since 2000



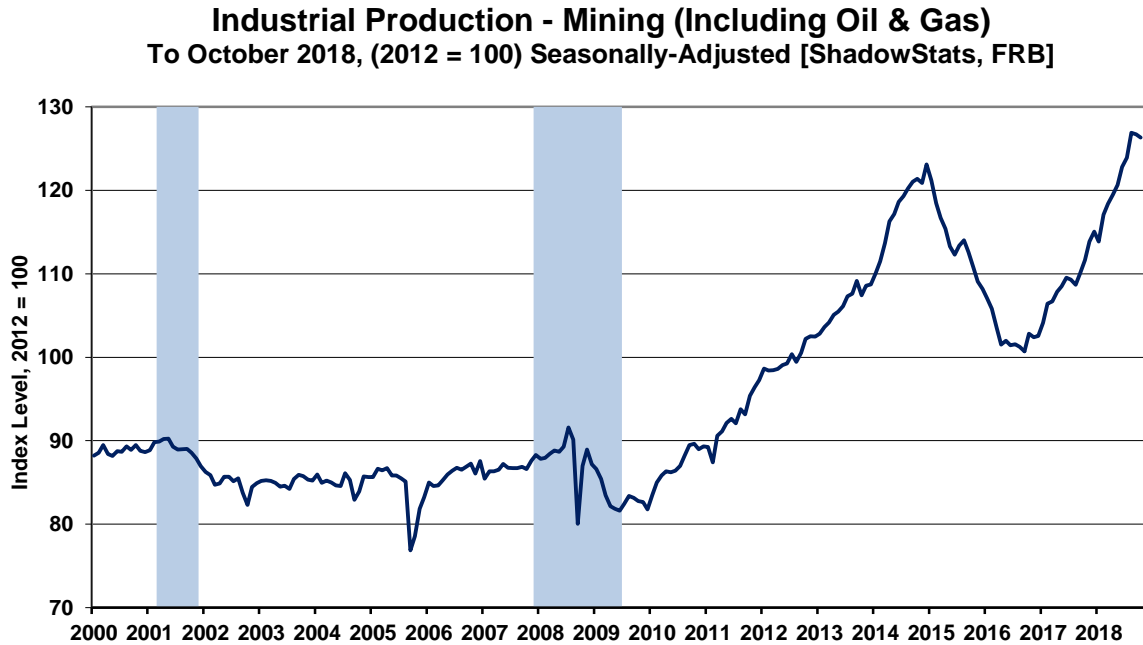
Graph 28: Industrial Production - Utilities, Year-to-Year Percent Change, Since 2000



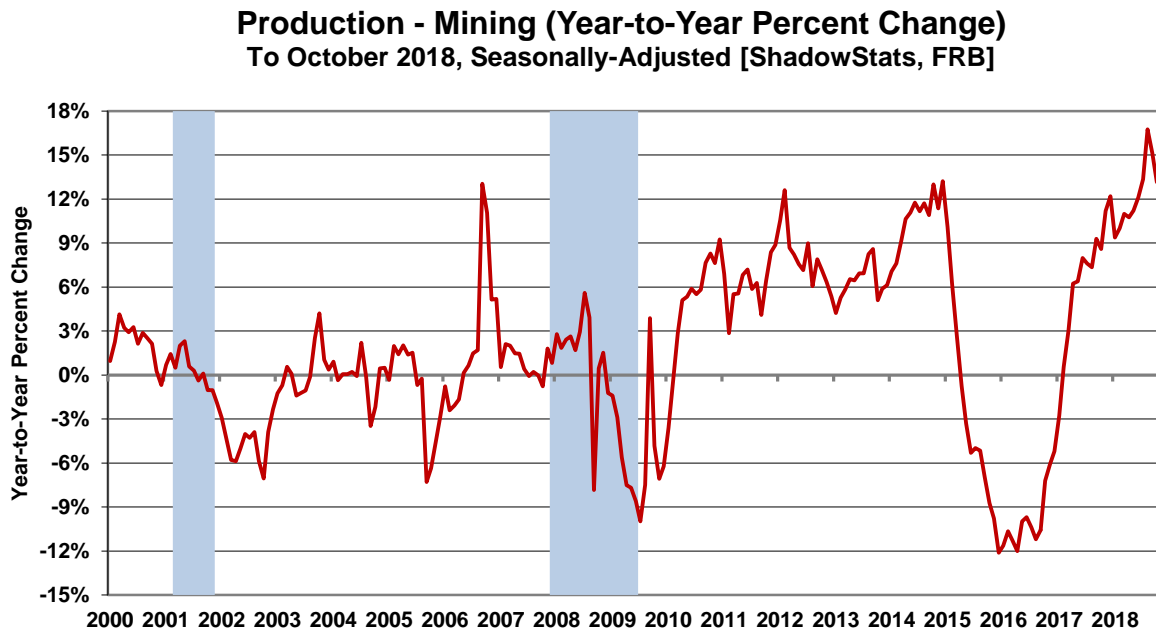
The final set of Mining *Graphs 29 to 35*, encompasses plots of related mining/oil production or exploration activity. Gold and Silver mining (*Graph 31*) increased month-to-month by 1.91% in October, having declined by a revised 7.22% (-7.22%) [previously a gain of 0.81%] in September, but was down year-to-year by 11.74% (-11.74%) in October 2018, having declined by a revised 16.00% (-16.00%)

[previously by 8.78% (-8.78%) in September 2018. Coal Mining activity (*Graph 32*) declined by 5.05% (-5.05%) in October 2018, having gained 0.94% in September 2018. Respective rates of annual change were a decline of 2.85% (-2.85%) in October 2018, versus a gain of 3.17% in September 2018.

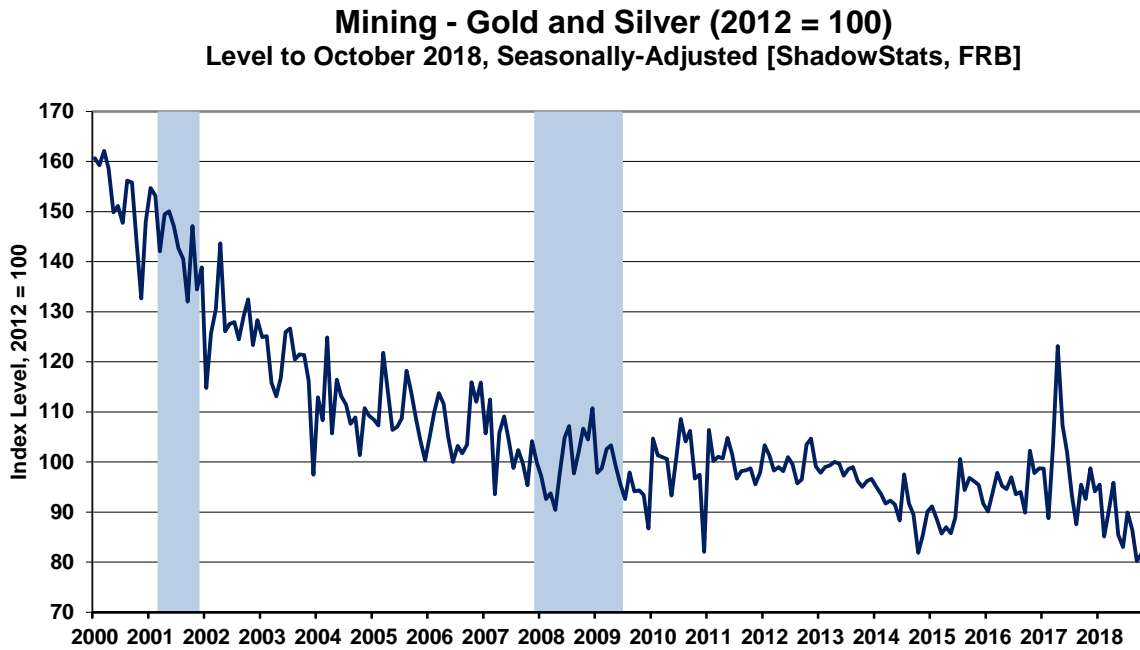
Graph 29: Industrial Production - Mining, Including Oil and Gas (14.1% of the Aggregate in 2017), Since 2000



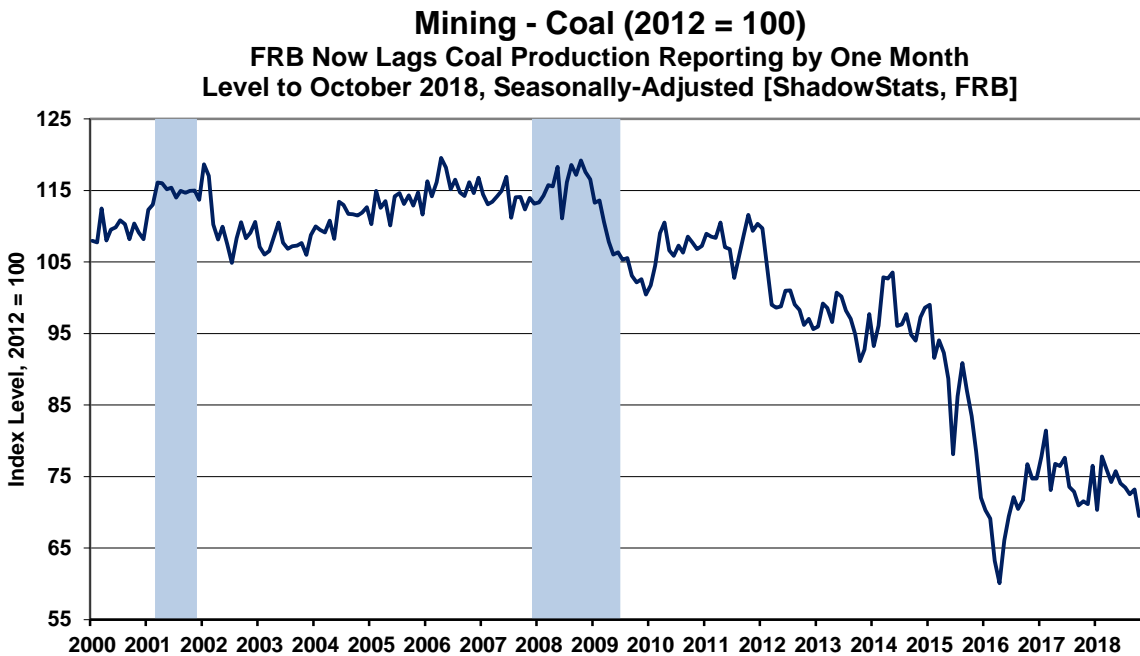
Graph 30: Industrial Production - Mining, Year-to-Year Percent Change, Since 2000



Graph 31: Mining – Gold and Silver Mining (0.2% of the Aggregate in 2017), Since 2000

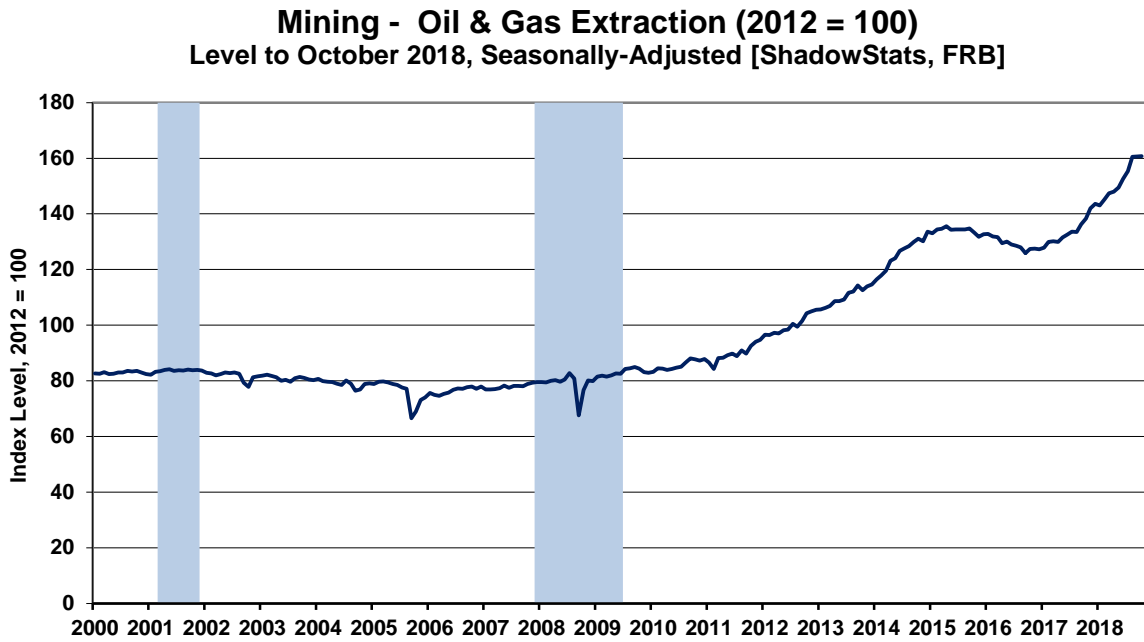


Graph 32: Mining - Coal Mining (0.8% of the Aggregate in 2017), Since 2000

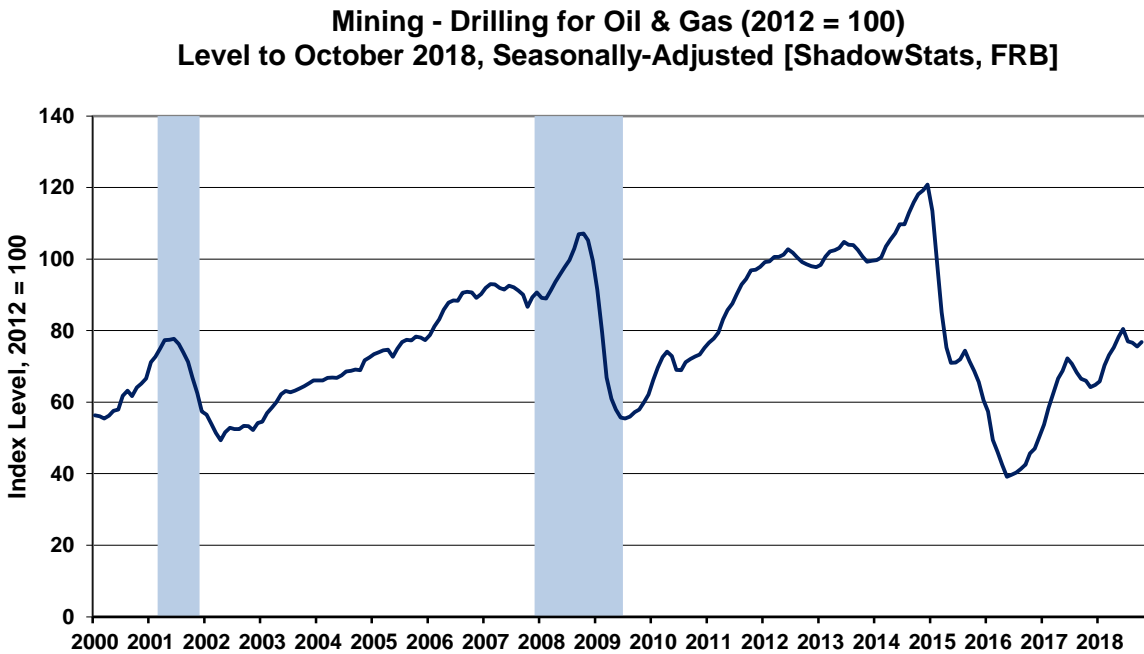


Usually dominated by monthly and annual growth from Oil and Gas Extraction and Exploration (all minimally positive in October 2018), the Mining Sector declined 0.31% (-0.31%), having declined by a revised 0.14% (-0.14%) in September, with Mining activity up year-to-year by 13.14% in October 2018, versus a revised 15.12% 14.35% (see *Table I*), also complemented by activity in Gold and Coal mining.

Graph 33: Mining – U.S. Oil & Gas Extraction (10.3% of the Aggregate in 2017), Since 2000



Graph 34: U.S. Drilling for Oil & Gas - Exploration (0.5% of the Aggregate in 2017), Since 2000

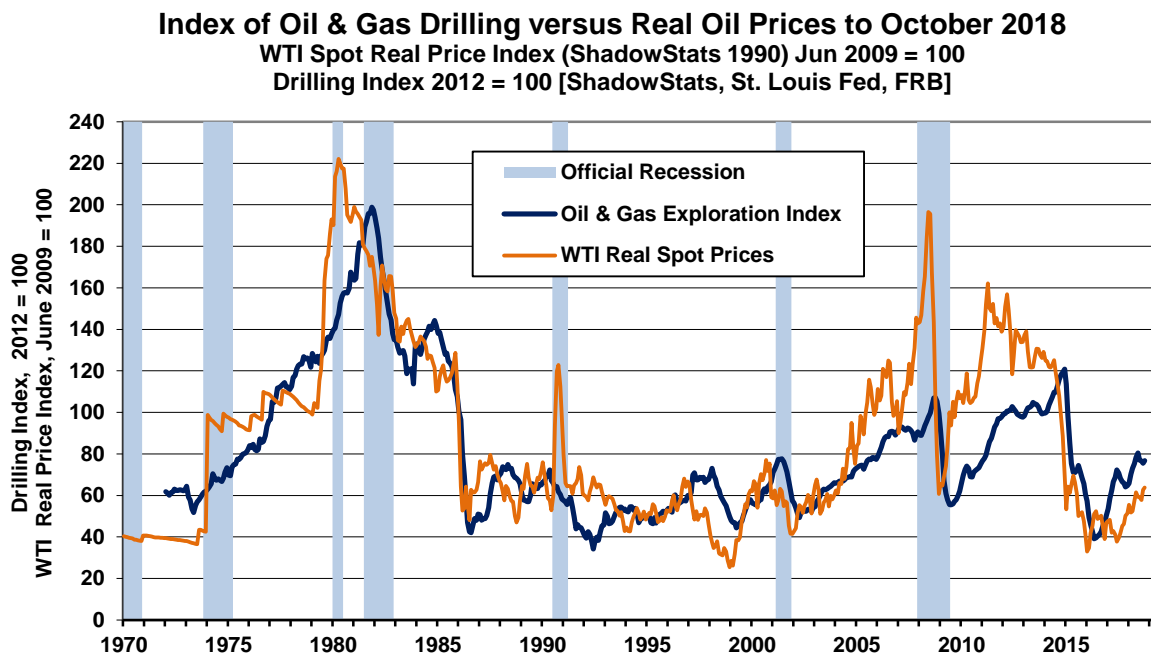


Often boosted by rising oil prices, currently in decline, the dominant oil and gas mining sector rose month-to-month for extraction, and gained for drilling and exploration (see *Graphs 33 to 35*), with Oil and Gas Extraction up by 0.04% for the month and 16.18% year-to-year, with Oil and Gas Drilling

declined up by 1.61% for the month and by 16.42% year-to-year. Year ago activity still reflects impact from last year’s Gulf Coast hurricane activity.

With some lag following sharp movements in oil prices (*Graph 35*), oil and gas exploration tends to move in tandem, and an upswing in exploration had been in place with what was at least a short-term bottoming in oil prices in early-2016. Prices rallied into mid-2016, but moved lower into 2017, with oil and gas exploration easing in July 2017 versus June 2017, the first month without a sharp month-to-month gain, since the boost from the 2016 upturn in oil prices. Yet, oil prices have risen strongly in recent months. Nonetheless, hurricanes and their after effects disrupted exploration in August through November 2017. That turned with an uptick in exploration in December 2017, with surging monthly growth into June 2018. The oil price index used here is for the West Texas Intermediate (WTI) monthly average spot price, deflated using the ShadowStats Alternate CPI measure (1990 Base).

Graph 35: Mining – U.S. Drilling for Oil & Gas versus Real Oil Prices (WTI ShadowStats 1990 Base), Since 1970



Indeed, rising oil prices tend to increase oil and gas exploration. When the dollar weakens, dollar-denominated oil prices also begin to strengthen, as had been seen recently, even in circumstances with excess supply conditions. With the U.S. dollar in a faltering upswing, albeit still off its recent bottom, oil prices have been firming, more heavily impacted recently by intensified global political tensions, particularly in the Middle East. At such time as the U.S. dollar meaningfully resumes its decline—ShadowStats looks for a massive sell-off in the dollar in the year ahead—U.S. dollar-denominated oil prices should rally sharply in response (see the [Hyperinflation Watch – No. 3](#) and soon-to-be-updated *HW-4*). Yet, again, beyond the dollar, recent movement in oil prices appears most-heavily impacted by, and reflective of political developments at home and abroad. Nonetheless, oil prices recently have risen sharply, on top of having rallied enough and for a long-enough period to induce continuing increases in domestic exploration and extraction activity, in the near future, as also has been seen at present.

New Orders for Durable Goods (October 2018)

Distorted by Wildly Gyrating Defense Aircraft Orders, Nominal New Orders for Durable Goods Plunged in October by 4.42% (-4.42%), On Top of Downside Revisions to September Activity. In nominal terms, before adjustment for inflation, October 2018 New Orders for Durable Goods dropped month-to-month by 4.42% (-4.42%), on top of downwardly revised September activity, now in contraction by 0.08% (-0.08%), previously a gain of 0.76%. Driving most of the monthly decline in October orders was a plunge of 59.34% (-59.34%) in defense aircraft orders, which had gained a revised 117.05% [previously 119.13%] in September.

The report still generally was weak. Removing just the nominal Defense Aircraft Orders from the nominal new orders, October New Orders declined by 1.9% (-1.9%) in the month, instead of the headline drop of 4.4% (-4.4%). On the same basis, September New Orders ex-Defense Aircraft declined month-to-month by 2.5% (-2.5%) instead of the revised headline 0.1% (-0.1%). Previously, headline New Orders in September had gained by 0.8%.

Allowing for Erratic One-Month Defense Orders Distortions, Real New Orders for Durable Goods Took a Monthly Hit of 3.8% (-3.8%), Just Ex-Commercial Aircraft. Commercial Aircraft are regularly volatile and unstable in their reporting, which is why ShadowStats standardly looks at total new orders in real terms, net of inflation, and net of Commercial Aircraft. Those October 2018 orders declined by 3.78% (-3.78%) in the month [(down by 3.50% (-3.50%) in nominal terms], versus a downwardly revised 1.05% (previously 1.82%) real monthly gain in September.

Of some separate substance in the October 2018 headline new orders detail, reflecting consumer liquidity stresses, nominal motor vehicles orders rose by a tepid 0.18% in October, which was down month-to-month by 0.21% (-0.21%) net of downside revisions to September orders, consistent with downside revisions to monthly retail sales and production.

Real October New Orders Dropped by 4.69% (-4.69%), Down by 3.78% (-3.78%) Ex-Commercial Aircraft Orders. Reported by the Census Bureau on November 21st, total nominal New Orders for Durable Goods, again, were savaged by one-month hard hit to defense aircraft orders. Total nominal orders declined month-to-month by 4.42% (-4.42%) in October 2018, following a revised monthly decline

of 0.08% (-0.08%) [previously a gain of 0.76%] in September, having gained a revised 4.69% [previously 4.65%, initially 4.45%] in August.

In the context of an October 2018 monthly decline of 21.40% (-21.40%) in highly volatile Commercial Aircraft Orders, following a revised decline of 19.27% (-19.27%) [previously 17.51% (-17.51%)] in September, shifting from an unrevised 63.67% jump in August, New Orders for Durable Goods Ex-Commercial Aircraft were declined by 3.50% (-3.50%) in October 2018, versus a revised gain of 1.22% [previously 2.00%] in September and a revised 2.19% [previously 2.15%, initially 1.71%] gain in August.

Table II: Summary Detail of October 2018 New Orders for Durable Goods

Table II: New Orders for Durable Goods (October 2018 Reporting)					
Month	Nominal Millions of Current Dollars			Real Millions of Constant 2009 Dollars	
	Total New Orders	Commercial Aircraft	Ex- Commercial Aircraft	Total New Orders	Ex- Commercial Aircraft
Aug 18	260.223	16.547	243.676	232.188	217.423
Sep 18	260.015	13.358	246.657	231.604	219.705
Oct 18	248.520	10.499	238.021	220.733	211.408
Percent Change					
	Mo/Mo	Mo/Mo	Mo/Mo	Mo/Mo	Mo/Mo
Aug 18	4.69%	63.67%	2.19%	4.57%	2.07%
Sep 18	-0.08%	-19.27%	1.22%	-0.25%	1.05%
Oct 18	-4.42%	-21.40%	-3.50%	-4.69%	-3.78%
Prior M/M					
Aug 18	4.65%	63.67%	2.15%	4.53%	2.03%
Sep 18	0.76%	-17.51%	2.00%	0.58%	1.82%
	Yr/Yr		Yr/Yr	Yr/Yr	Yr/Yr
Aug 18	12.10%		10.58%	8.56%	7.09%
Sep 18	7.00%		7.79%	3.57%	4.34%
Oct 18	6.65%		7.26%	3.31%	3.90%
Prior Y/Y					
Aug 18	12.06%		10.54%	8.52%	7.05%
Sep 18	7.86%		8.57%	4.40%	5.09%

Sources: Commerce Department, BLS, ShadowStats.com

Real Durable Goods Orders—October 2018. ShadowStats uses the Producer Price Index (PPI) component inflation measure “Durable Manufactured Goods” for deflating the new orders for durable goods series. Published only on a not-seasonally-adjusted basis, the related October 2018 PPI series

(2009 = 100) showed headline month-to-month inflation of 0.29%, versus 0.17% in September, 0.11% August, 0.23% in July, 0.29% in June, 0.46% in May, 0.35% in April, 0.41% in March, 0.35% in February and a 0.41% gain in January. Related year-to-year annual inflation was 3.24% in October, versus 3.31% in September 2018, 3.25% in August 2018, 3.20% in July 2018, 2.90% in June 2018, 2.66% in May 2018, 2.19% in April 2018, 2.08% in March 2018, 1.84% in February 2018 and 1.79% in January 2018 (see the *Producer Price Index* section earlier in this *Reporting Detail*).

Preceding *Table II* summarizes the monthly numbers presented here, by category and inflation-adjusted or not-inflation-adjusted status.

Adjusted for that 0.29% month-to-month inflation reading in October 2018 and the respective inflation rates in earlier months, and as reflected in the accompanying graphs, real aggregate durable goods orders in October 2018 declined by 4.69% (-4.69%), having declined by 0.25% (-0.25%) in September and having gained 4.57% in August. October real orders held shy of recovering their pre-recession peak by 11.61% (-11.61%). Ex-commercial aircraft, real month-to-month orders declined by 3.78% (-3.78%) in October 2018, having increase by 1.05% in September 2018 and by 2.07% in August. Ex-commercial aircraft, October 2018 real orders remained shy of recovering their pre-recession peak by 6.15% (-6.15%).

Real total new orders gained year-to-year by 3.31% in October 2018, by 3.57% in September 2018 and by 8.56% in August 2018. Ex-commercial aircraft, October 2018 real orders rose year-to-year by 3.90%, versus 4.34% in September 2018 and 7.09% in August 2018.

New Orders, Production and North American Freight Activity and Broad Domestic Economic Activity. ShadowStats concentrates on the inflation-adjusted real New Orders for Durable Goods series, ex-commercial aircraft, as a leading indicator to the dominant Manufacturing sector of Industrial Production, as well as its relationship with the CASS Freight IndexTM, a key private-sector indicator of broad activity. Those relationships are highlighted in today's *Opening Comments* (see *Graphs OC-4 to OC-9*).

Graphs of Inflation-Adjusted and Smoothed Durable Goods Orders and Recent Benchmark Revisions. The headline September 2018 New Orders for Durable Goods of November 21st and accompanying revisions all were in the broad context of prior, meaningful, downside annual benchmark revisions (through March 2018) of May 17th, discussed primarily in [Commentary No. 951](#) and [Commentary No. 950](#). Intervening headline monthly details for April to September 2018 were discussed in [Commentary No. 957](#), [Commentary No. 961](#), [Commentary No. 967](#), [Commentary No. 971](#) and [Commentary No. 976](#), with the October details updated in *Graphs 36* and *37*.

In the context of those benchmark revisions, *Graphs 43* and *44* show the current headline monthly detail, as well as the six-month moving-average activity for both the aggregate new orders series and the same series net of the irregularly-volatile commercial-aircraft orders. The broad pattern of smoothed, real activity generally has remained at a low-level of non-recovered, but uptrending stagnation.

The moving-average levels in *Graphs 36* and *37* turned lower into year-end 2014, and after an uptick in mid-2015—some smoothed bounce-back—the trend turned down anew into late fourth-quarter 2015, with continued minor fluttering into third-quarter 2016, and initially a small uptick in fourth-quarter 2016. Activity continued on the upside into 2017 and 2018, although softened by the downside benchmark revisions (again, see *Graphs 43* and *44*). Starting with August and September of 2017, however, broad

orders activity was spiked temporarily by natural-disaster recovery, a pattern that largely had passed in early 2018, but that could be returning a bit, in the wake of September 2018 hurricane damage.

Three sets of inflation-adjusted graphs (*Graphs 36 to 38*, *Graphs 39 and 40*, and *Graphs 41 and 42*) follow. The first set shows the headline monthly detail, as well as the six-month moving-average activity for both the aggregate new orders series and the series net of irregular commercial-aircraft orders. It also shows annual growth for the real series (net of commercial aircraft). The moving-average levels in both the durable goods series (*Graphs 36 and 37*) had turned lower into year-end 2014 and the first two quarters of 2015, with some smoothed bounce-back into third-quarter 2015, followed by renewed downturn into 2016 with a late-year uptick continuing into March 2017, which largely was revised away with the May 2017 benchmarking. Along with a period of uptrending stagnation, boosted by disaster recovery, the same pattern of growth and downside benchmark revision largely was repeated through May 2018, as can be seen in *Graphs 43 and 44*.

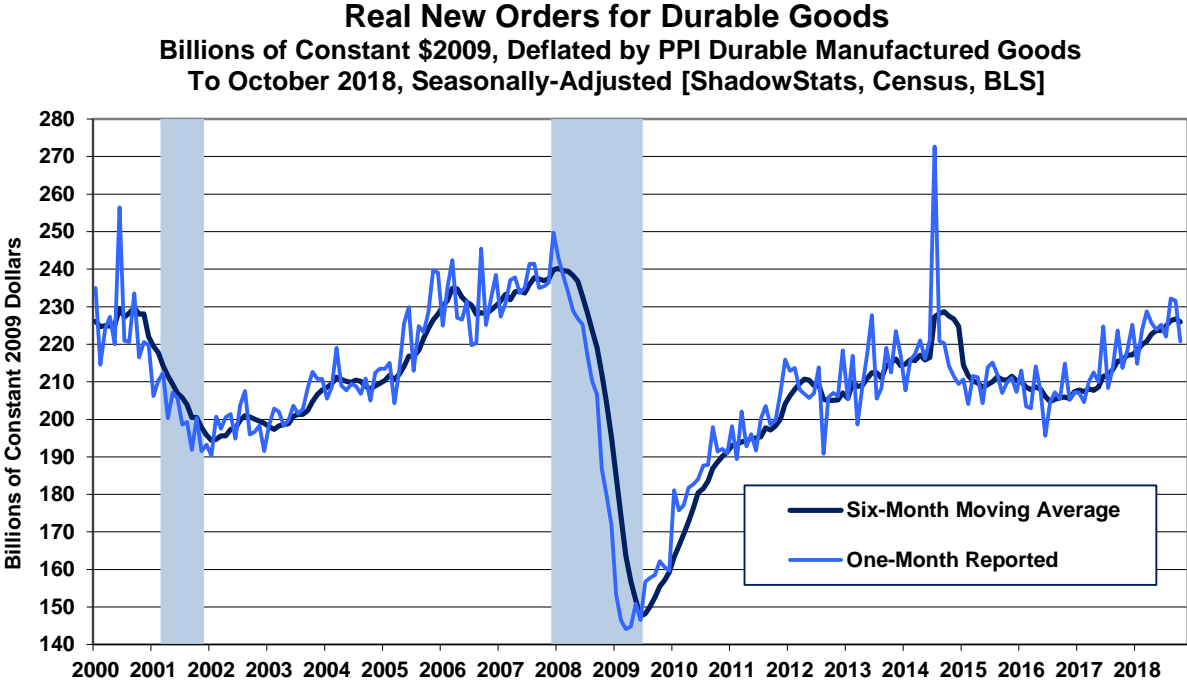
The second set of graphs (*Graphs 39 and 40*) shows the patterns of six-month moving averages of historical, headline real new orders for durable goods (net of official inflation), as well as that pattern “corrected” for understatement of that inflation (and for the corresponding overstatement of official, inflation-adjusted growth). The third set of graphs (*Graphs 41 and 42*) shows largely the same patterns, although they are for the aggregate durable goods orders series, net of commercial aircraft orders.

Broad Patterns of New Orders Activity. There has been a general pattern of stagnation or bottom-bouncing evident in the orders of recent years—clearly not the booming recovery seen in official GDP reporting. The real monthly and six-month moving-average levels of new orders in September 2018 remained below both the pre-2007 recession high, as well as the pre-2000 recession high for the series. The pattern of low-level stagnation and fluctuating trend in the annual inflation-adjusted series since mid-2014—net of the irregular aircraft-order effects—again is one that most commonly precedes and/or coincides with a recession or non-economic expansion, as is the current circumstance. These series remain in non-recovered, non-expanding, low-level, albeit uptrending stagnation (see the *Opening Comments* of [Commentary No. 966](#)).

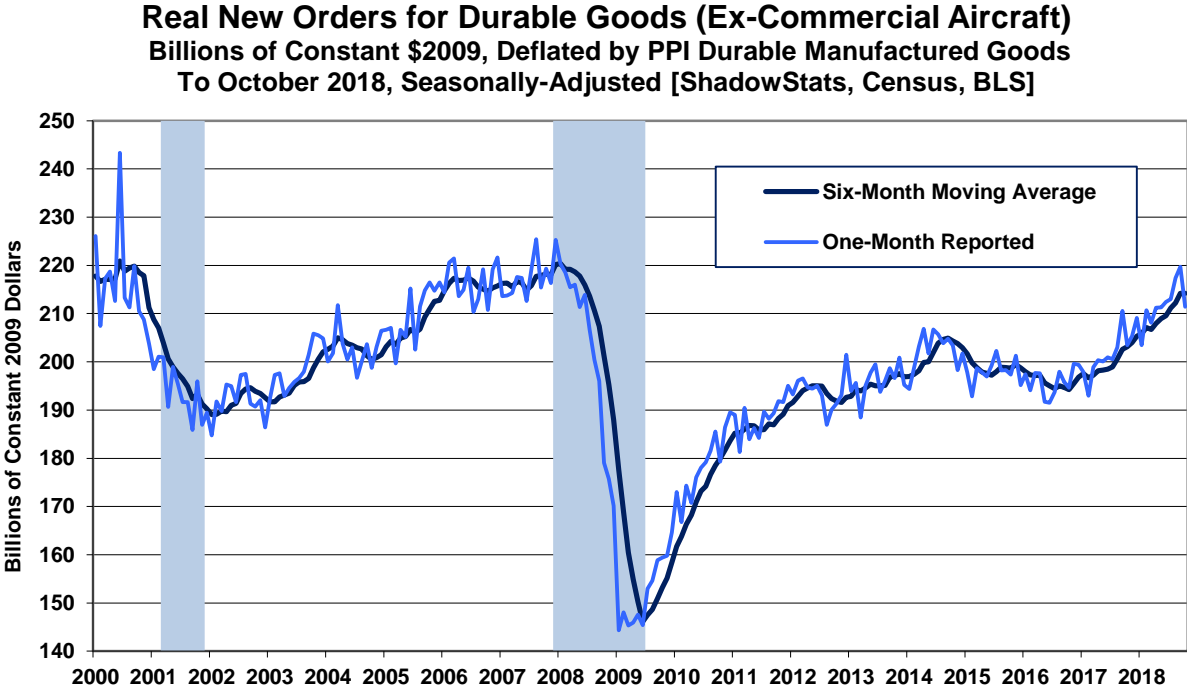
[Graphs 36 to 38 begin on the next page.]

Headline New Orders Detail, Aggregate and Ex-Commercial Aircraft

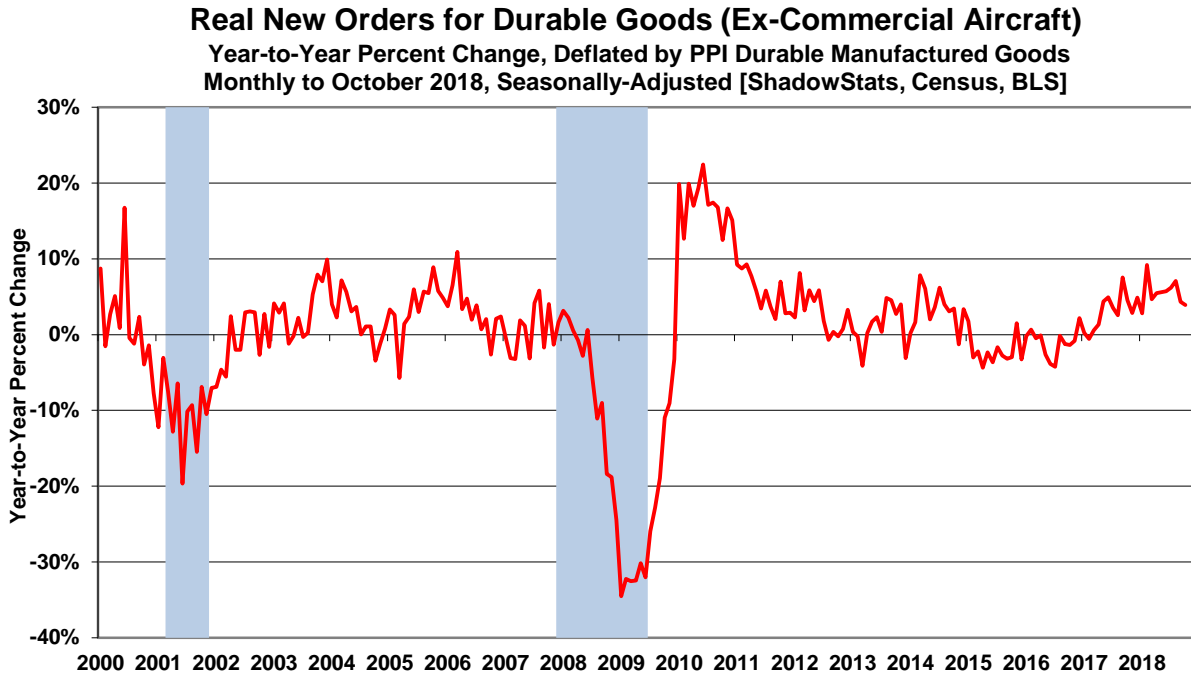
Graph 36: Real Total New Orders for Durable Goods to Date



Graph 37: Real New Orders for Durable Goods – Ex-Commercial-Aircraft Orders to Date



Graph 38: Yr-to-Yr % Change, Real New Orders for Durable Goods – Ex-Commercial Aircraft (2000 to Date)
 (Same as Graph OC-7 in the Opening Comments)



The Real New Orders Series “Corrected” for Inflation Understatement. As with other economic series distorted by deflation using official government inflation measures, headline estimates of inflation-adjusted growth in new orders for durable goods generally are overstated, due to the understatement of official inflation. Among other issues, that understatement comes from the government’s use of hedonic-quality adjustments—quality issues usually not perceived by the users or consumers of the involved products—in justifying a reduced pace of headline inflation used in deflating some series (see [Public Commentary on Inflation Measurement](#)).

As done for other series such as Industrial Production, Retail Sales and the GDP (see *Graphs 14* and *7* earlier in this *Reporting Detail*, and *Graph OC-3* in [Commentary No. 976](#), ShadowStats publishes an experimental, corrected-inflation version of the graph of real New Orders for Durable Goods. Real activity, in this case, is corrected for the understatement of the inflation used in deflating the new orders series with the headline PPI inflation for manufactured durable goods.

Two sets of graphs follow. The first set (*Graph 39* and *Graph 40*) shows the aggregate series or total durable goods orders; the second set (*Graph 41* and *Graph 42*) shows the ex-commercial aircraft series. The aggregate orders series in *Graphs 39* and *40* includes the monthly commercial aircraft orders. Placed years in advance, aircraft orders are a better indicator of long-range production activity, than they are as a near-term leading indicator of production activity. Again, *Graphs 41* and *42* are shown net of those volatile commercial aircraft orders.

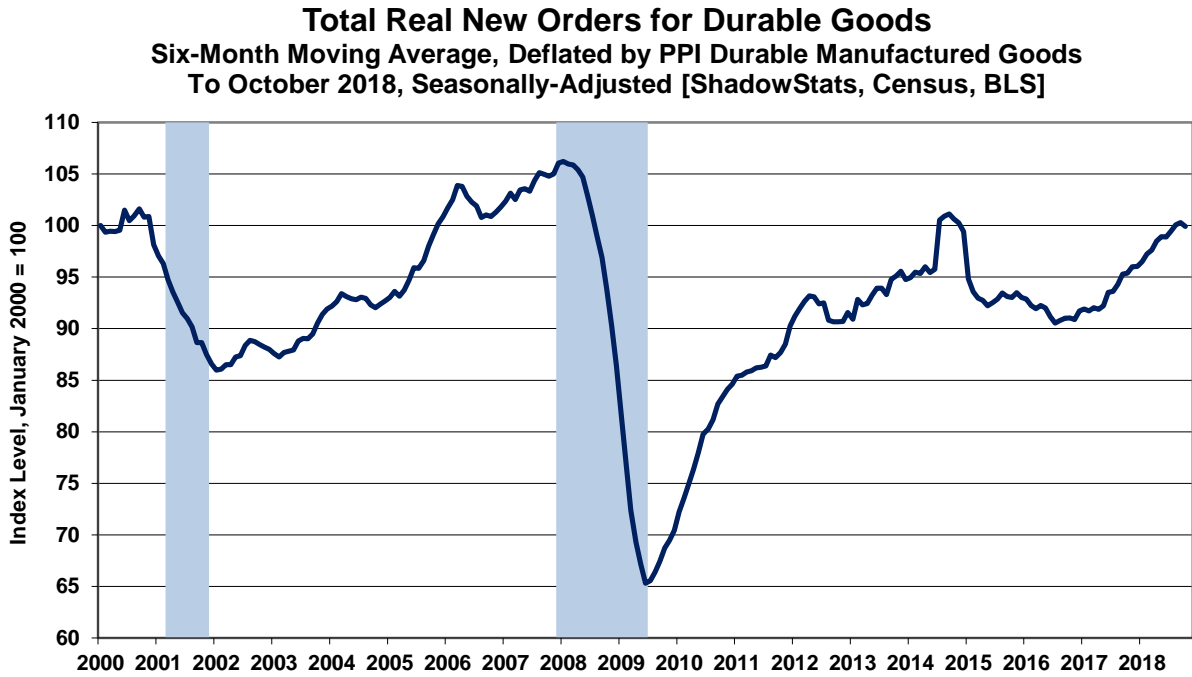
The first graph in each of the two sets shows the official six-month moving average, the same heavy dark-blue line shown in *Graph 36* and *Graph 37*, along with the light-blue thin line of monthly detail. The

second graph in each set is the same six-month, moving-average series shown in the first graph, but it has been re-deflated to correct for the ShadowStats estimate of the understatement of the PPI manufactured durable goods inflation measure used in the headline-deflation process. The “corrected” graphs all are indexed to January 2000 = 100.

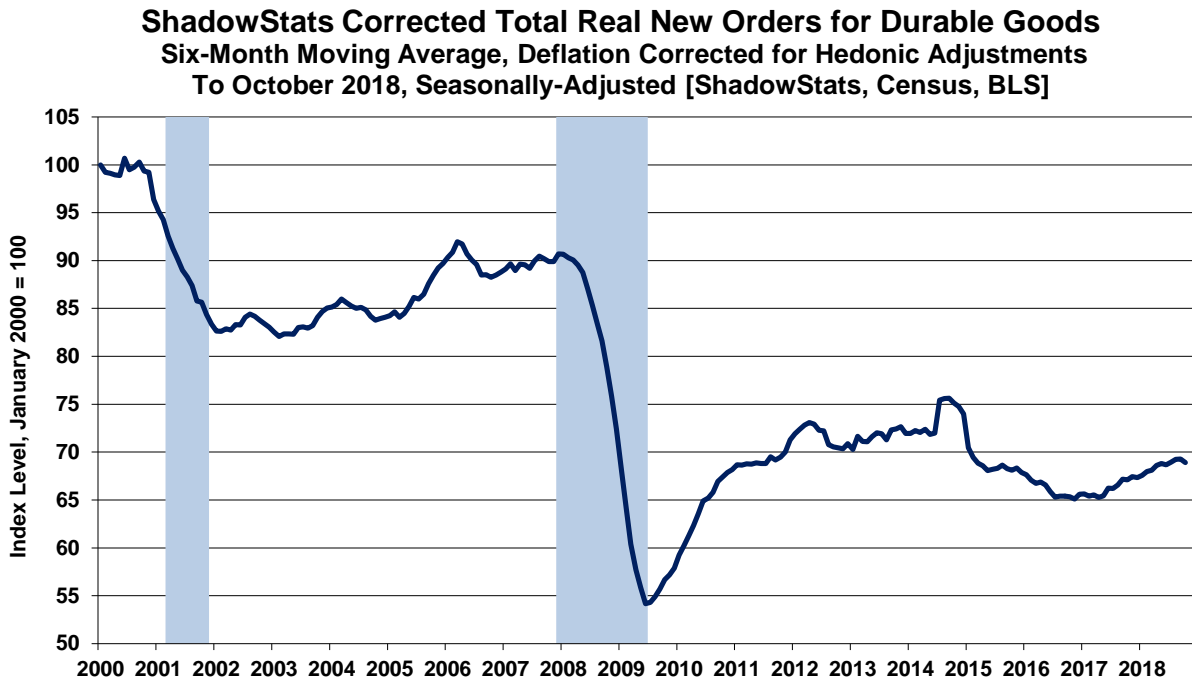
The 2000 indexing simply provides for some consistency in the series of revamped “corrected” graphics such as Retail Sales and Industrial Production, discussed in their respective sections of [Commentary No. 975](#), the GDP, discussed in the next section. The indexing does not affect the appearance of the graph or reported growth rates (as can be seen with a comparison of the moving average in *Graph 36* to the later *Graph 41*, which has the standard, headline indexing).

[Graphs 39 to 42 begin on the next page.]

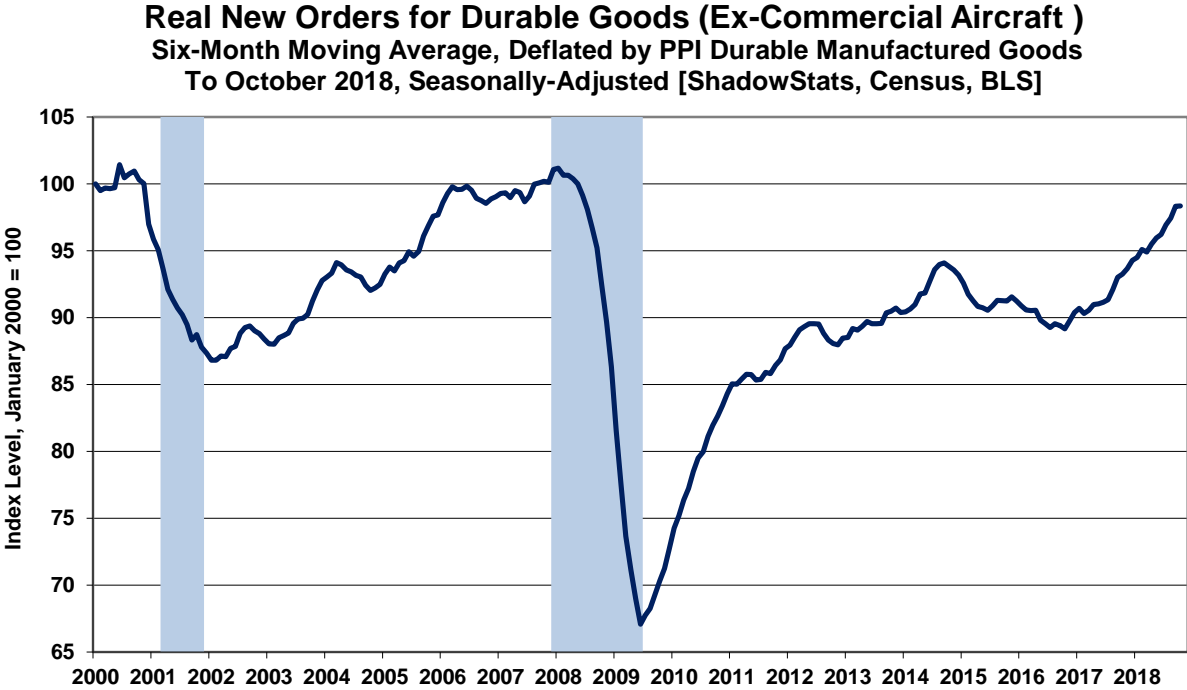
Smoothed Real Series and Real Series Corrected for Inflation-Understatement
Graph 39: Index of Real Total New Orders for Durable Goods, 6-Month Moving Average



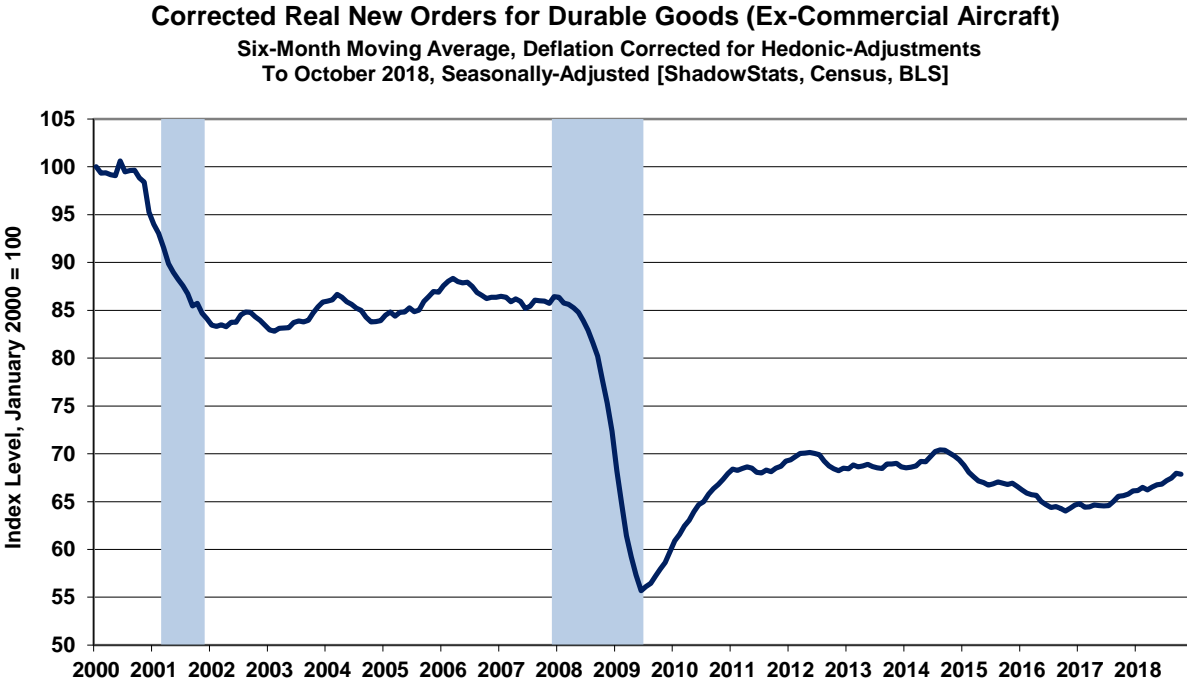
Graph 40: Corrected Index of Real Total New Orders for Durable Goods, 6-Month Moving Average



Graph 41: Index of Durable Goods Orders – Ex-Commercial Aircraft, 6-Month Moving Average



Graph 42: Corrected Index of Durable Goods Orders – Ex-Commercial Aircraft, 6-Month Moving Average



Caution: Beyond Regular Upside Biases Built Into Headline Reporting, Seasonally-Adjusted Month-to-Month Data Simply Are Not Comparable. The Census Bureau published its 2018 annual benchmark revisions to Manufacturers’ Shipments, and the subsidiary series New Orders for Durable Goods on May 17th, which broadly were to the downside. They also largely were consistent with major downside revisions to the Industrial Production series in its March 23rd benchmarking and in its unusual monthly revisions of May 16th (see [Commentary No. 951](#), [Commentary No. 950](#) and [Commentary No. 942-B](#)), and suggestive of some likely parallel hits in the GDP revisions. Yet, there was no clear, parallel impact on the recently-published GDP “comprehensive” benchmark revisions discussed in [GDP Special No. 968](#).

This circumstance has been the common experience in economic reporting of recent years and decades. Discussed in [Special Commentary No. 885](#), there is a broad upside bias often built into the underlying assumptions that drive the headline reporting of many, widely-followed and politically-sensitive economic series.

As an example of the regular, annual downside restatement of recent activity in the New Orders for Durable Goods series, consider accompanying *Graphs 43* and *44* of both aggregate (*Graph 43*) and ex-commercial aircraft (*Graphs 44*) real new orders for durable goods. The plots reflect the net revisions to the six-month moving averages of those two series for the 2018 benchmarking, as well as for the three prior benchmarkings, along with subsequent headline reporting through the October 2018 headline detail.

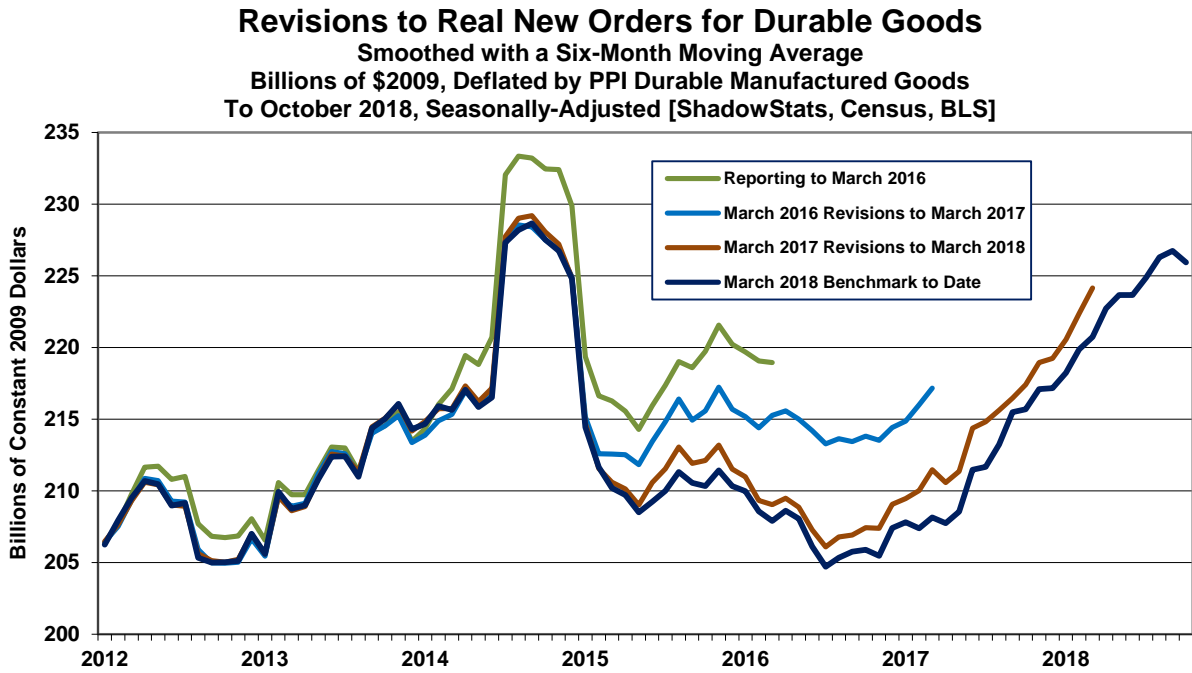
For a substantive review of the last two years of benchmark revisions to New Orders for Durable Goods, and the parent Manufacturers’ Shipments series, see [Commentary No. 951](#), [Commentary No. 950](#) and [Special Commentary No. 885](#).

Current headline durable-goods reporting remains subject not only to the upwardly-biased sampling assumptions seen in the pre-benchmarking reporting, but also to the concurrent-seasonal-adjustment problems commonly seen with series such as retail sales, and payroll and unemployment reporting. Unusual seasonal-factor volatility raises issues as to the significance of comparing reported seasonally-adjusted changes, be they monthly or quarterly, or on a year-to-year basis. While those issues were brought into balance, for a period of eight days, with the annual benchmark revision to durable goods orders through March 2018 on May 17, 2018 (again see [No. 950](#)), that consistency ceased with the May 25th release of the headline April 2018 detail.

For all monthly reporting from the April 2018 detail until the next annual benchmarking in May 2019, unpublished, monthly historical seasonal-adjustment revisions, calculated along with each new current headline month’s detail, and with each month to follow, make the latest detail (September 2018) inconsistent with all the headline historical numbers. (See the related discussion in *Supplemental Labor-Detail Background* in [Commentary No. 977](#)).

[Graphs 43 and 44 follow on the next page.]

Graph 43: Benchmark Revisions to Real Total New Orders for Durable Goods, Smoothed for 6-Month Moving Avg



Graph 44: Benchmark Revisions to Real Total New Orders for Durable Goods, Ex-Commercial Aircraft

