

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

SHADOWSTATS BULLET EDITION NUMBER TWO

March 11, 2019

**Latest Retail Sales, Employment and Monetary Base
Show Increasingly Negative Economic Trends**

**January 2019 Retail Sales Signaled a Downside Revision to
Fourth-Quarter 2018 GDP, Along With an Early
Indication for a First-Quarter 2019 GDP Contraction**

**Annual Growth in February 2019 Payrolls Slowed in a Manner
Consistent With a Faltering First-Quarter Economy**

**February 2019 Saint Louis Fed Adjusted Monetary Base
Declined Year-to-Year by 13.0% (-13.0%), Worst Showing Since
1937 Onset of Great Depression Second Down Leg**

**Reporting of Broad U.S. Economic Activity Signals a New Recession,
While Major Sectors Such as Manufacturing and Construction
Never Recovered from the Last One**

**The FOMC Should Be Feeling Increased Pressure to Ease,
But Action Still Is Not Likely Next Week**

ShadowStats Commentaries, Bullet Editions, Watches and Daily Updates – Going Forward. Many thanks to those who offered comments on the inaugural *ShadowStats Bullet Edition No. 1*. The general reception appears to have been favorable. Going forward the plan for various *ShadowStats* writings is to:

- Update regularly the *Daily Update* on the *ShadowStats* home page (www.ShadowStats.com), posting coverage of major economic releases as released by the issuing authority, usually within two-to-three hours of headline publication, as well as to cover unusual market circumstances.
- Post the *Bullet Edition* several times per month, as dictated by economic reporting and underlying economic developments and financial-market conditions. Simply put, the *Bullet Edition* conveys brief communications and analyses on limited topics of particular near-term significance. The current issue reviews recent signals of slowing economic activity, with an increasingly likely downside revision to the fourth-quarter 2018 GDP and early indications of pending quarterly contractions for first- and second-quarter 2019 GDP, the likely onset of a new recession.
- Post the more-comprehensive *Regular Commentary* about once per month, providing a regular and broader overview of unfolding conditions and likely developments.
- Post updated *Hyperinflation* and *Consumer Liquidity Watches* once per month, alternating updates roughly every other week.

Special Commentary No. 983-B, The Annual Review will be published next week, subsequent to the FOMC meeting on March 20th. Unlike the current week that has a record seven economic releases (four catch up), next week is devoid of major reporting, except for the FOMC meeting. Expectations likely will be for no change in the targeted level of the federal funds rate, although there is some chance of a rate cut, discussed later. *No. 983-B* should be posted within a day of the FOMC.

The *ShadowStats* general outlook has not changed, specifically including a deepening economic downturn, mounting downside pressures on the U.S. dollar and stock market, and upside pressures on gold and silver prices in the weeks and months ahead. *No. 983-B* will incorporate fully all the latest economic and financial data pending in the days ahead.

Your comments and suggestions always are invited.

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

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Intensifying Deterioration in Key Economic Indicators

Signals Mount for an Even Weaker Fourth-Quarter 2018 GDP in Revision

Upcoming Releases Should Take Subsequent Quarters Negative

Continued FOMC Tightening Seen in New Extremes of Monetary-Base Contraction

The FOMC Should Begin to Ease Anew, But Perhaps Not Next Week

Real Retail Sales Showed Early Trend for a First-Quarter 2019 Contraction

Headline Indicators Suggest a Looming Downside Revision to the “Initial” 2.6% Fourth-Quarter 2018 GDP, with Mounting Signals for an Outright Contraction in First-Quarter 2019 GDP. Recent headline reporting of Housing Starts, Payroll Employment and Retail Sales have confirmed the ShadowStats contention that the headline slowing of Fourth-Quarter 2018 GDP annualized real quarterly growth to 2.6%, from 3.4% in Third-Quarter 2018 was far short of what was being indicated by better-quality indicators (see [Bullet Edition No. 1](#) of March 7th).

That ShadowStats position has been supported by subsequent headline reporting in a number of series, particularly the March 8th release of February 2019 Payroll Employment, and today’s (March 11th) reporting of January 2019 Retail Sales, discussed in this section. Consider that in response to the January Retail Sales reporting, the well-respected [Atlanta Fed GDP Now](#) model dropped its estimate for first-quarter 2019 GDP growth from an already-anemic 0.5% to 0.2%. Various senior Fed officials recently have begun warning of little or no economic growth in first-quarter 2019.

As an aside, watch out for some “unexpected” weakness in Friday’s (March 15th) release of February 2019 Industrial Production, which will be followed by *Bullet Edition No. 3* of that date.

Forewarned in [Bullet Edition No. 1](#): “*Housing Starts*. This series usually is nonsensically volatile, but commonly with downside revisions to annual growth in prior reporting. Irrespective of the headline January detail, watch for downside revisions to fourth-quarter activity, which would be reflected in a downside revision to fourth-quarter GDP growth.”

Despite the usual nonsensical monthly jump in the headline month's (January 2019) reporting, fourth-quarter 2018 activity contracted for the third consecutive quarter at a revised, deeper annualized contraction of 24.3% (-24.3%) [previously down by 19.9% (-19.9%)]. This series will be updated through February (caught up) on March 26th, two days before the "final" Fourth-Quarter GDP revision and "final" estimate. Look for those repetitive patterns of downside revisions to the prior numbers.

Not only is real annualized Fourth-Quarter 2018 GDP a good bet to revise lower on the March 28th, it also is a good bet to revise lower, once again, come the annual GDP benchmarking, coincident with the "advance" Second-Quarter 2019 GDP estimate on July 26th.

July 26th also likely will be the day that a "new recession" gains unofficial recognition, with headline Second-Quarter 2019 likely to be reported as a second, consecutive, real quarterly contraction. Formal calling of a recession, however, comes from the [National Bureau of Economic Research](https://www.bea.gov/) (NBER).

January 2019 Retail Sales "Gain" Boosted Sharply by Negative Prior-Period Revisions, Impaling Near-Term GDP Activity; Real Sales Contraction in 4q2018 with Contracting Trend for 1q2019.

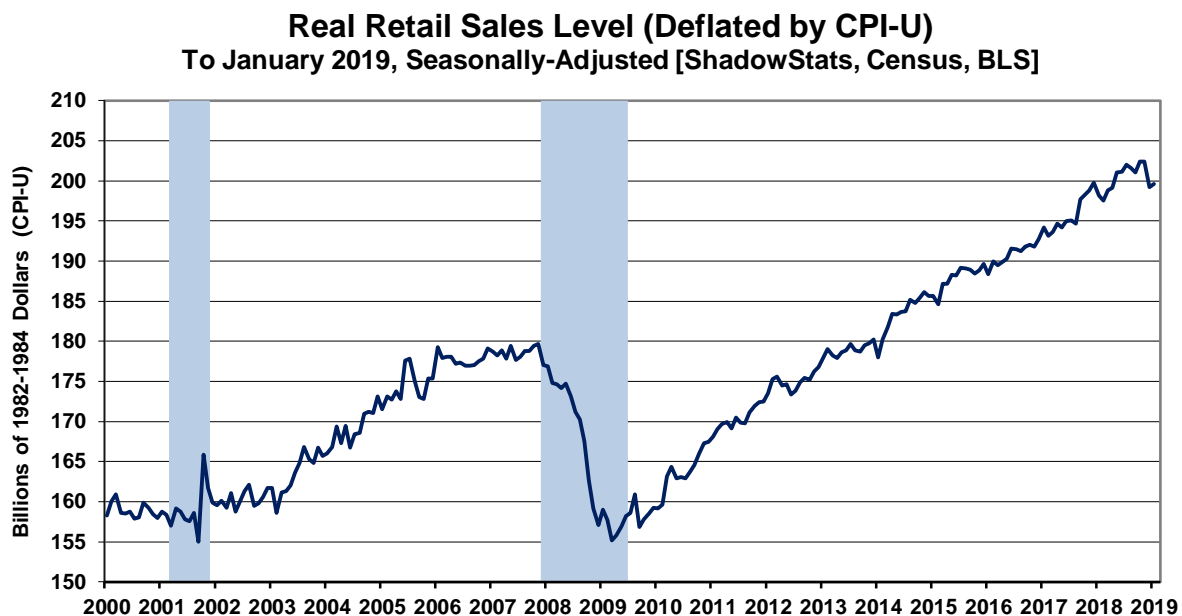
Reviewed in today's *Daily Update* section on the ShadowStats home page (www.ShadowStats.com), nominal Retail Sales gained 0.21% in January, but that was a decline of 0.27% (-0.27%), net of revisions, per the Census Bureau (March 11th). December 2018 sales dropped in the month by a revised, deepened and statistically significant 1.61% (-1.61%) [previously 1.24% (-1.24%)], the worst monthly decline since 2009, with the economy coming out of the depths of the Great Recession. That downside revision to December was on top of downwardly revised November sales, now "unchanged" at 0.00% [previously up by 0.11%]. With headline monthly inflation at minus 0.02% (-0.02%) in January and at 0.01% (-0.01%) in December and November, inflation-adjusted real monthly growth rates, net of CPI-U inflation, as regularly calculated by the Saint Louis Fed, were effectively the same as the nominal changes.

Separately, year-to-year nominal Retail Sales rose to 2.28% in January 2019, versus a revised 1.65% [previously 2.27%] in December 2018, with real annual growth at 0.75% in January 2019, versus a revised annual contraction (not seen since 2009) of 0.29% (-0.29%) [previously a gain of 0.32%] in December 2018. Such low levels of annual growth rarely are seen outside of what become formal recessions.

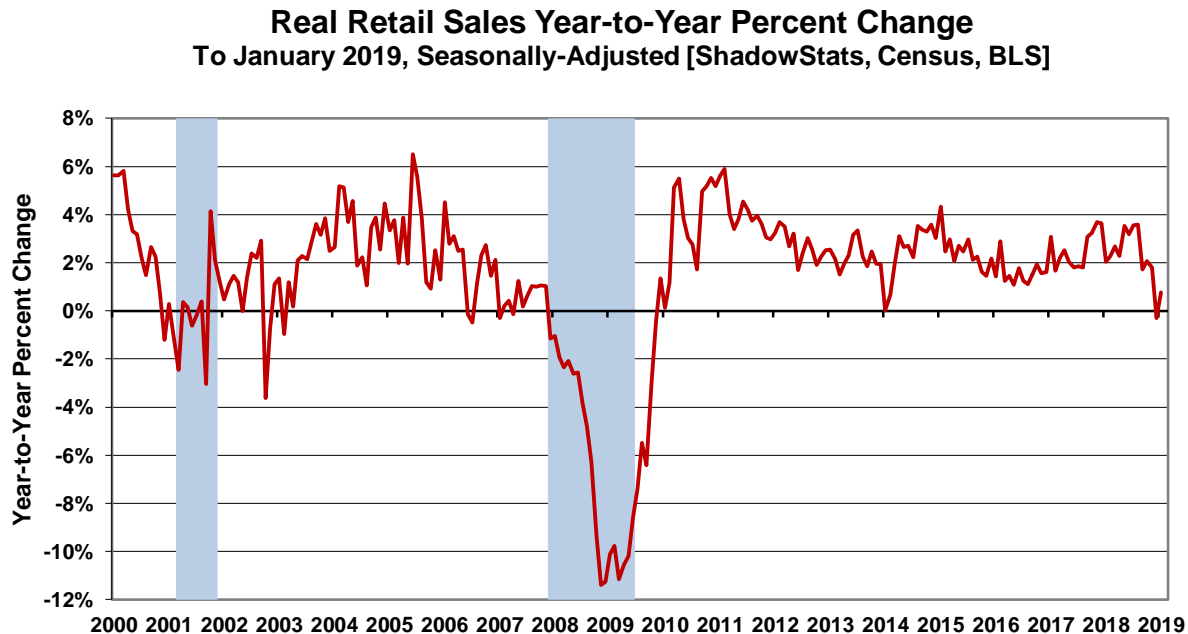
Bad news for GDP reporting: revised real quarterly sales turned negative in fourth-quarter 2018, with the early first-quarter 2019 trend sharply negative. Real annualized quarterly change in 4Q2018 revised from 0.30% to a decline of 0.49% (-0.49%), with the early trend for 1q2019 a contraction of 3.30% (-3.30%). Discussed here regularly, excessive tightening and rate hikes by the Federal Reserve since late 2017 have impaired consumer liquidity, which drives three-fourths of the GDP. The new headline retail numbers should have some downside impact on expected GDP revisions reporting.

[Graphs 1 to 4 of Real Retail Sales through January 2019 begin on the next page.]

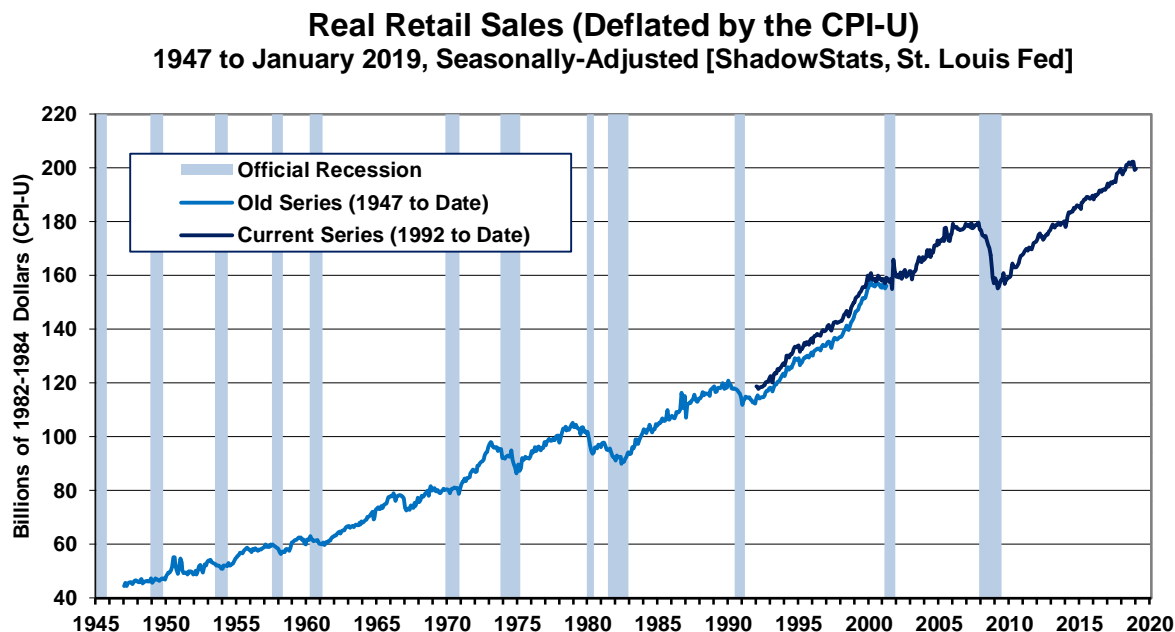
Graph 1: Real Retail Sales (January 2000 to January 2019)



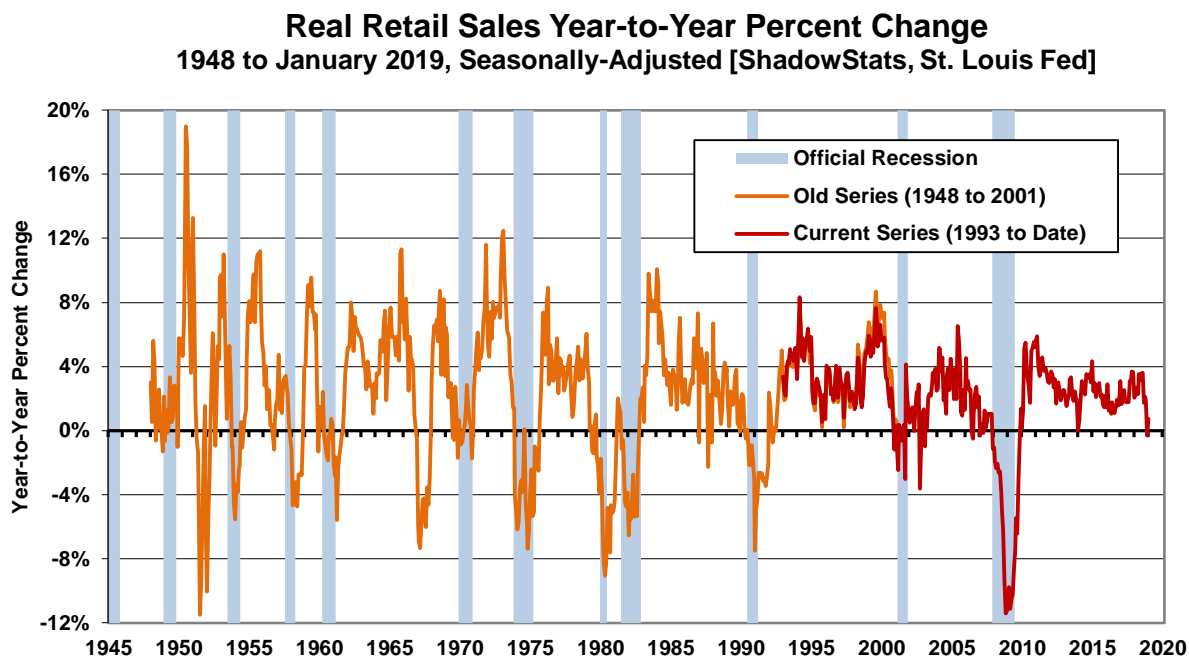
Graph 2: Real Retail Sales, Year-to-Year Change (January 2000 to January 2019)



Graph 3: Real Retail Sales (January 1947 to January 2019)



Graph 4: Real Retail Sales, Year-to-Year Change (January 1948 to January 2019)

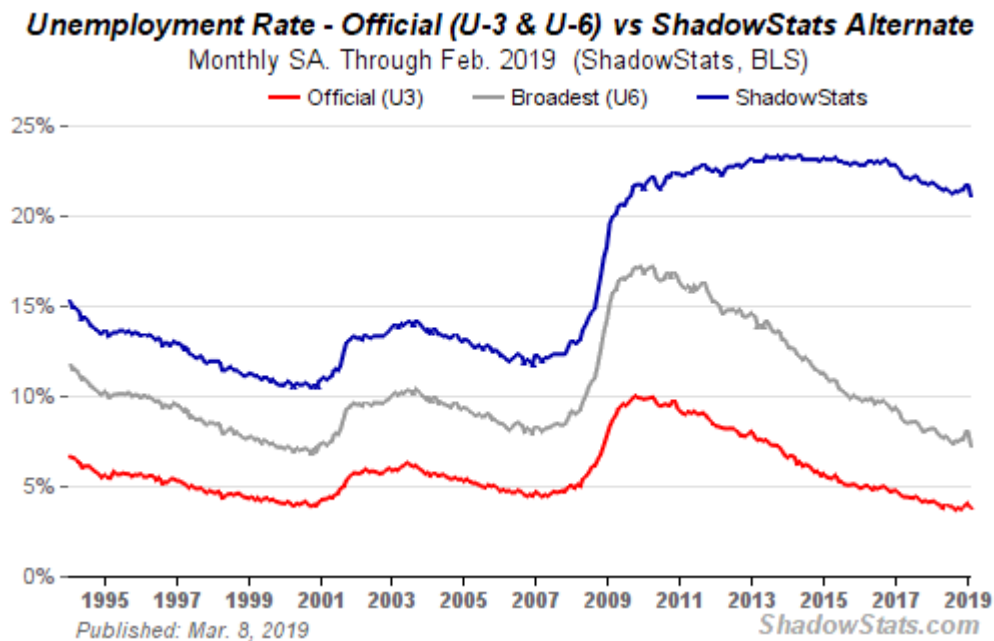


Slowing February Annual Payroll Growth Suggested Weaker Than Previously Indicated Economic Activity; The Drop in February Unemployment Rates Largely Reversed Shutdown Impact.

Reported by the Bureau of Labor Statistics (BLS) on March 8th, February 2019 labor data showed a reverse impact on the February Household Survey numbers from the government shutdown having been in effect for the January survey period, but the shifts in monthly and annual payroll data largely reflected slowing economic growth.

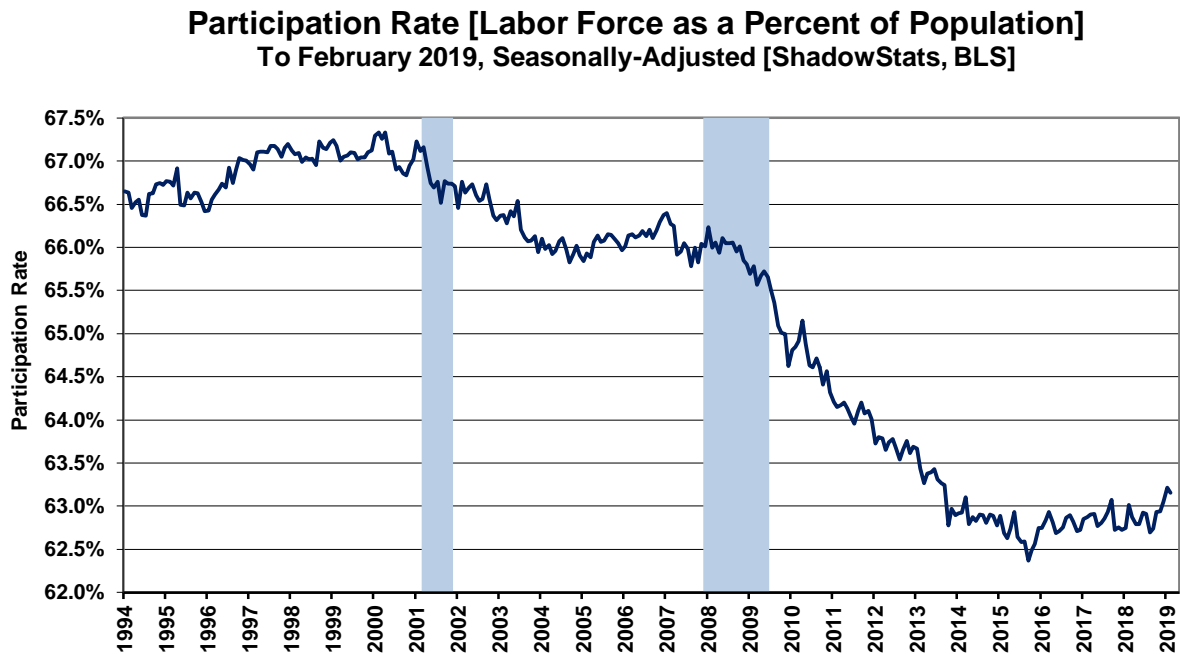
On the unemployment front, U.3 Unemployment fell to 3.82% from 4.00% in January, returning close to the pre-Shutdown December level of 3.86%. ShadowStats previously had estimated that January U.3 would have been 3.89% without the government shutdown. The broader January U.6 unemployment rate had jumped to 8.07% in January, from 7.59% in December, along with a jump in discouraged workers and those “unemployed for economic reasons.” Reversing that pattern in February, U.6 backed off to 7.27%, indicating that the bulk of the January U.6 surge also was shutdown related. On top of U.6, the ShadowStats Alternate Unemployment Estimate, including the long-term discouraged/displaced workers not counted by the BLS, rose to 21.8% in January from 21.4% in December, backing off to 21.1% in February, largely in tandem with U.6. The headline jumps in January unemployment from the government shutdown backed off in the February 2019 detail seen in *Graph 5*.

Graph 5: U.S. Unemployment Rates U.3 and U.6 vs. ShadowStats Alternate Unemployment (1994 to Date)

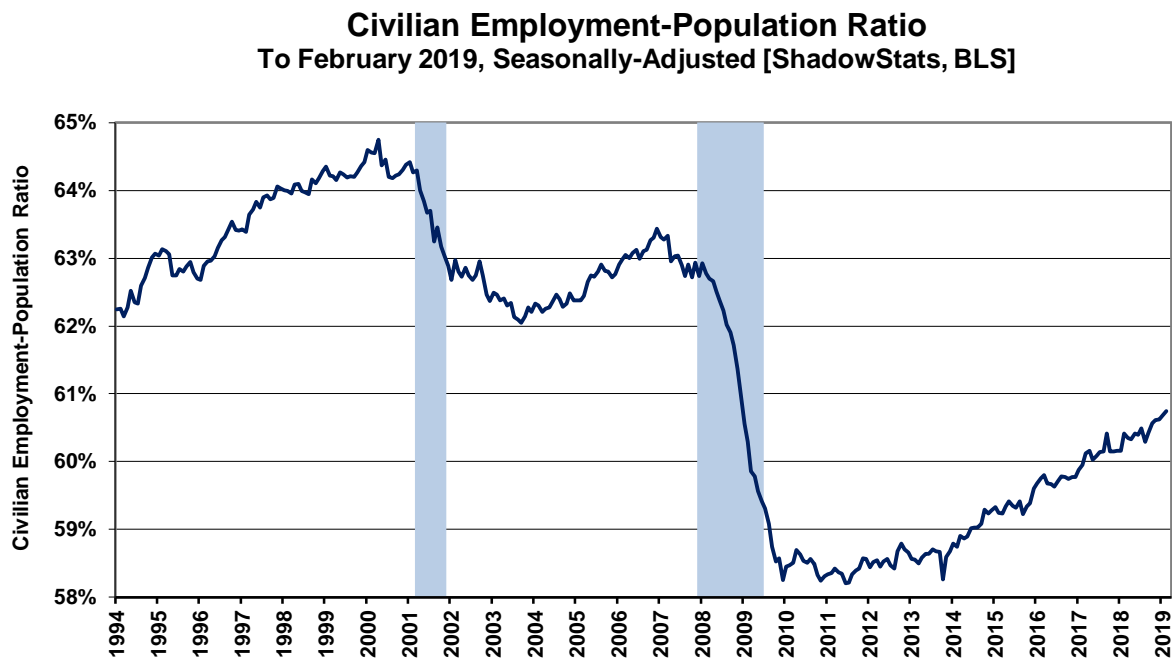


Graphs 6 and 7 are the regularly published plots of employment-market stress in the Participation Rate (labor force as a percent of population), and the employment-to-population ratio. The lower the rate or ratio, the higher the labor-market stress and the higher the unemployment rate should be, at least historically. Contrary to the unemployment rates plotted with the inverse scale in *Graphs 8 and 9*, the current levels of labor-market stress are much more compatible with high levels of the ShadowStats Alternate Unemployment (again a reverse scale in *Graph 8*) than the near-record low headline U.3 unemployment rate of *Graph 9* (again a reverse scale). These data suggest that current headline economic strength is not quite as advertised (see the *Labor Supplement* in [Commentary No. 982](#)).

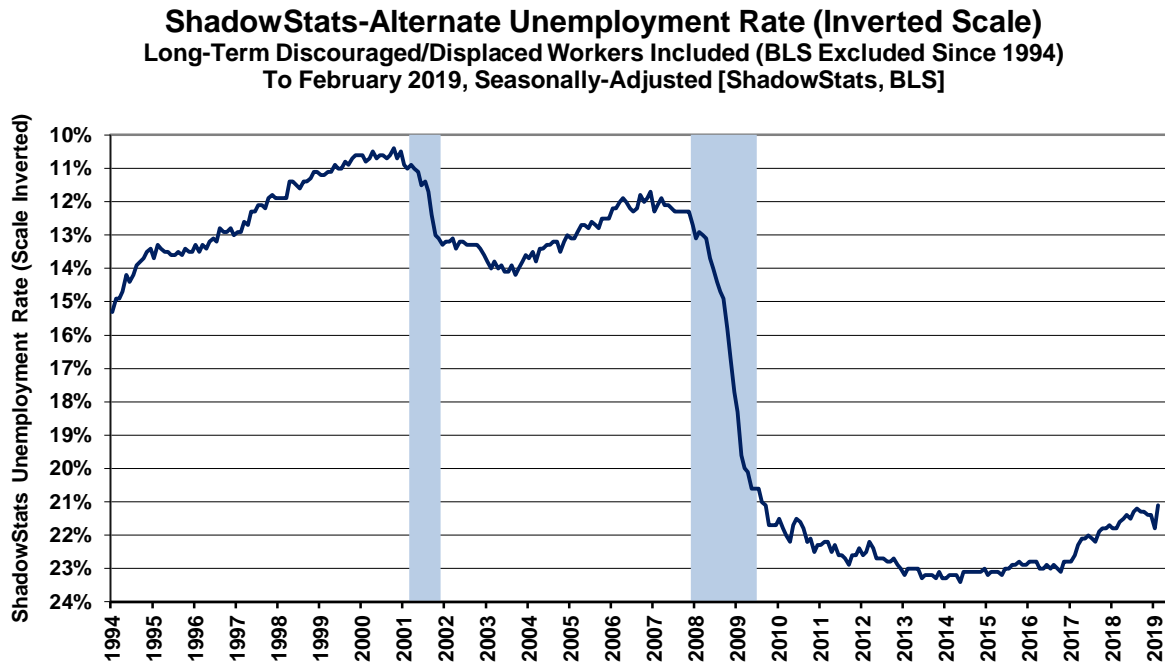
Graph 6: Participation Rate - Labor Force as a Percent of Population (1994 to Date)



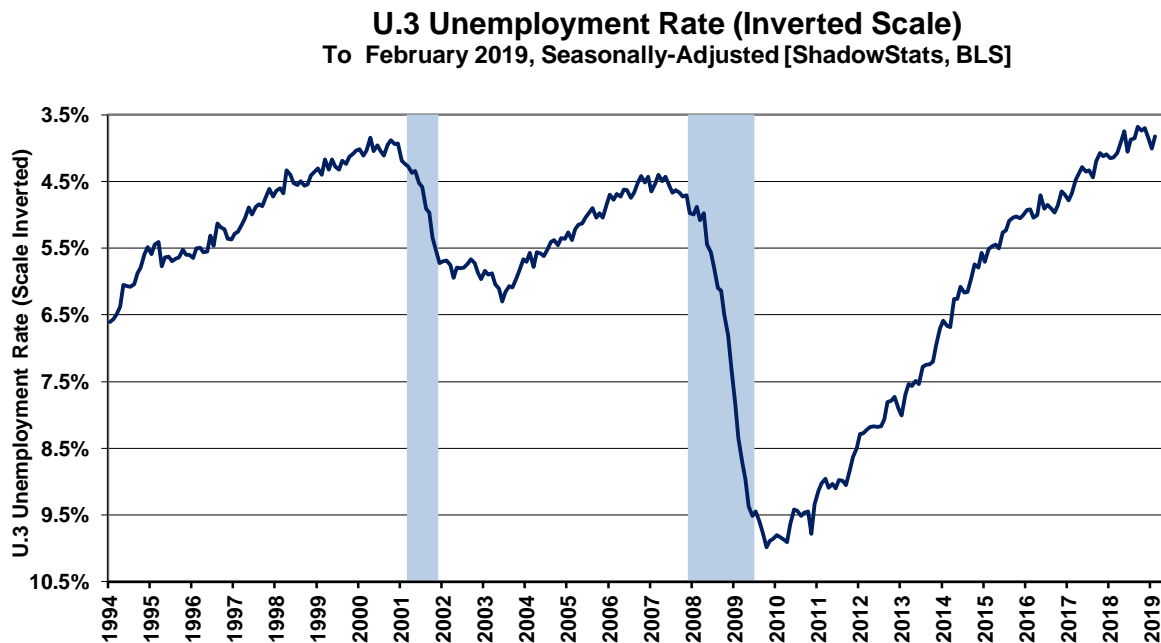
Graph 7: Civilian Employment-Population Ratio (1994 to Date)



Graph 8: ShadowStats-Alternate Unemployment Rate, Inverted Scale (1994 to Date)

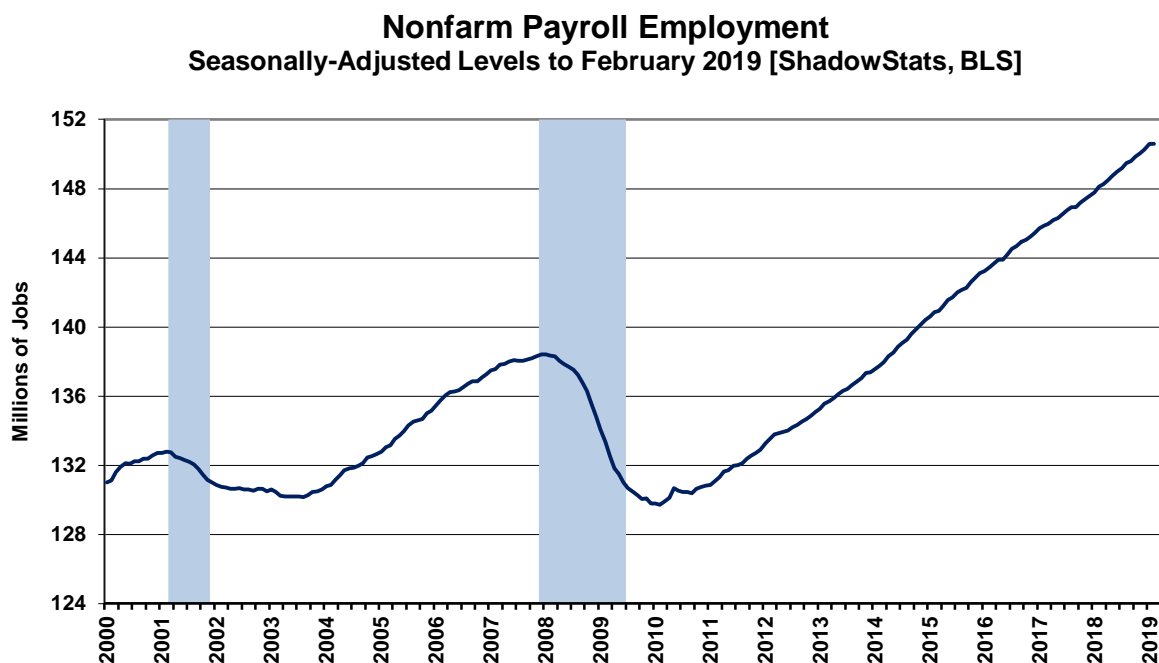


Graph 9: Headline U.3 Unemployment Rate, Inverted Scale (1994 to Date)

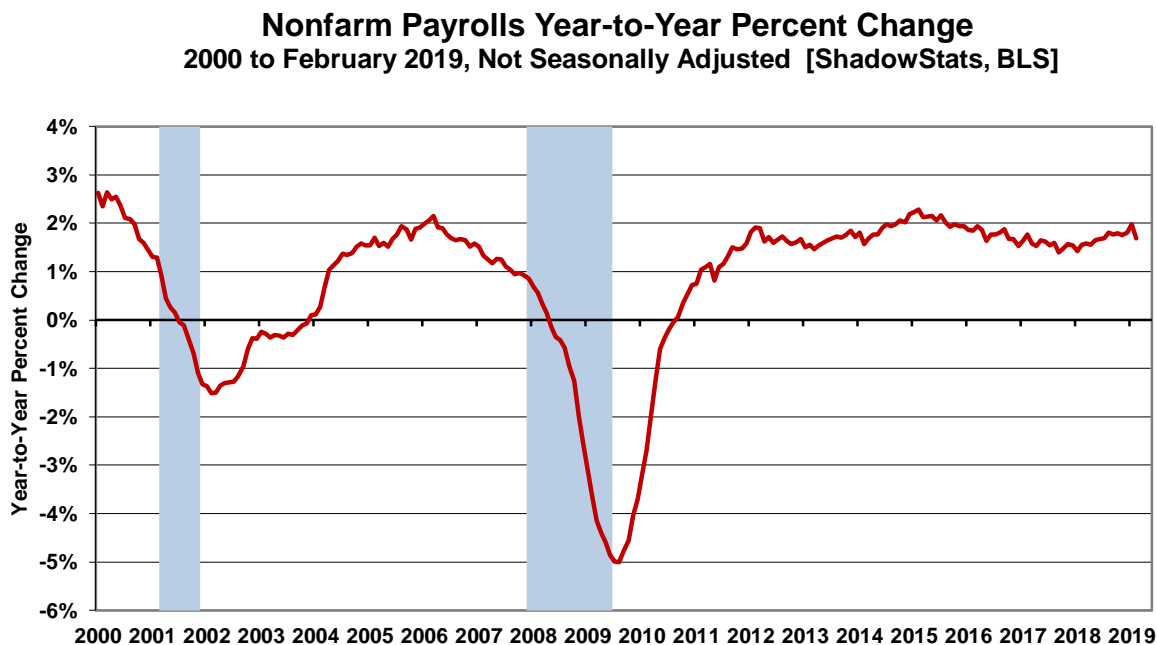


In contrast to the Household Survey, the levels of the Payroll Survey tended to reflect economic activity, where the flattening of payrolls and slowing annual payroll growth rate in February 2019, were reflective of slowing current levels of payrolls and annual growth in same, against periods outside the government shutdown, consistent with an economic downturn (see *Graphs 10 and 11*).

Graph 10: Nonfarm Payroll Employment (1994 to Date)



Graph 11: Nonfarm Payroll Employment, Year-to-Year Percent Change (1994 to Date)



Monetary Base Is Collapsing Like It Is 1937

March FOMC Meeting Looms, Any Easing?

What to Watch for in the Week Ahead

Beware the Ides of March!

February Industrial Production Will Be the Last “Big” Number Before the March 20th FOMC.

Discussed here, February Labor data and various catch-up reporting of the shutdown-delayed Trade Deficit, Retail Sales, Housing and Construction numbers have indicated a pending downside revision to the 2.6% “Initial” (combined first and second estimates of) Fourth-Quarter 2018 GDP, which had slowed from 3.6% in Third-Quarter 2018, along with developing indications for contracting First-Quarter 2019 GDP activity. Where consensus expectations for February Industrial Production appear to be in the 0.3% to 0.5% range, plus or minus, risk is fair for an outright monthly contraction and/or meaningful prior-period downside revisions. A much weaker-than-expected number would intensify pressure at the March 20th FOMC meeting for some form of easing action. If such “unexpected” action should occur, watch for heavy selling of the U.S. Dollar, a rally in precious metals prices and some selling of U.S. stocks in tandem with flight from the dollar.

ShadowStats Continues to Predict First- and Second-Quarter 2019 GDP Contractions. Some downside revision is likely in the final estimate of, and still catch-up reporting to fourth-quarter 2018 GDP. ShadowStats continues to forecast a formal recession, beginning in first- and second-quarter 2019, which (or anticipation of which) likely will force the Federal Reserve back into an easing mode, irrespective of any current comments offered by the FOMC or the Fed Chairman.

Economic Indicators Should Turn Increasingly Negative. Between now and the second and “final” estimate of Fourth-Quarter 2018 GDP on March 28th, a variety of indicators will be published that should pressure that “final” growth estimate to the downside, in revision, and likely will take expectations for First-Quarter 2019 GDP increasingly negative, before its “advance” release on April 26th.

Subsequent to the February 28th “Initial” (combined first and second) estimate of Fourth-Quarter 2018 GDP, releases of December Construction Spending and New-Home Sales, February Labor Conditions

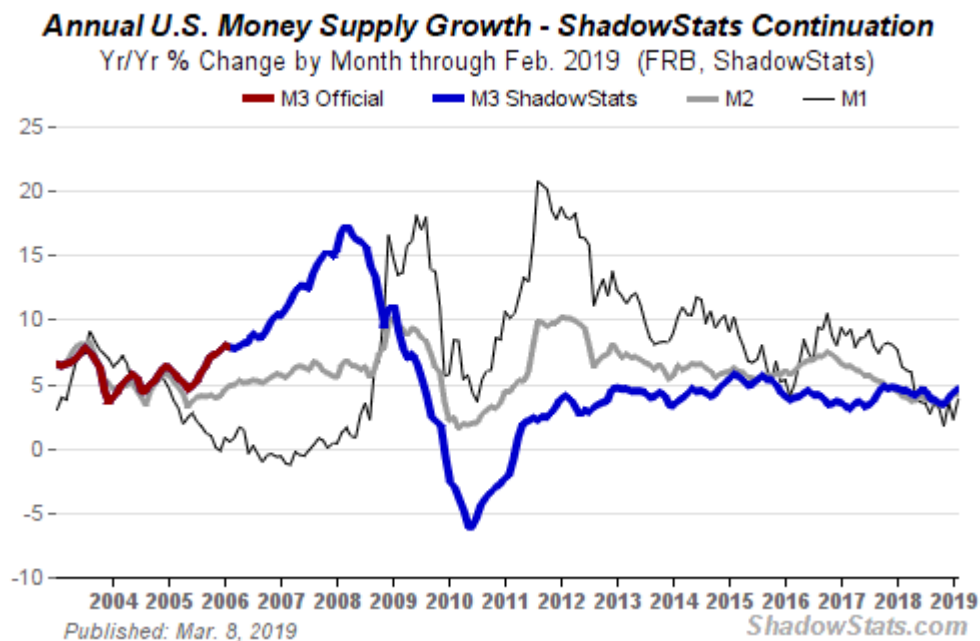
and January Housing Starts signaled downside revisions to the fourth-quarter GDP estimate and negative trends into first-quarter 2019. Beyond the CPI, PPI and Production numbers, the shutdown-delayed data normally would have been in place (and more negative) for the “Initial” fourth-quarter GDP estimate:

Date	Series	Agency
12 Mar	Consumer Price Index, February 2019	Bureau of Labor Statistics
13 Mar	Producer Price Index, February 2019	Bureau of Labor Statistics
13 Mar	New Orders for Durable Goods, January 2019 (Delayed)	Census Bureau
13 Mar	Construction Spending, January 2019 (Delayed)	Census Bureau
14 Mar	New-Home Sales, January 2019 (Delayed)	Census Bureau
15 Mar	Industrial Production, February 2019	Federal Reserve Board

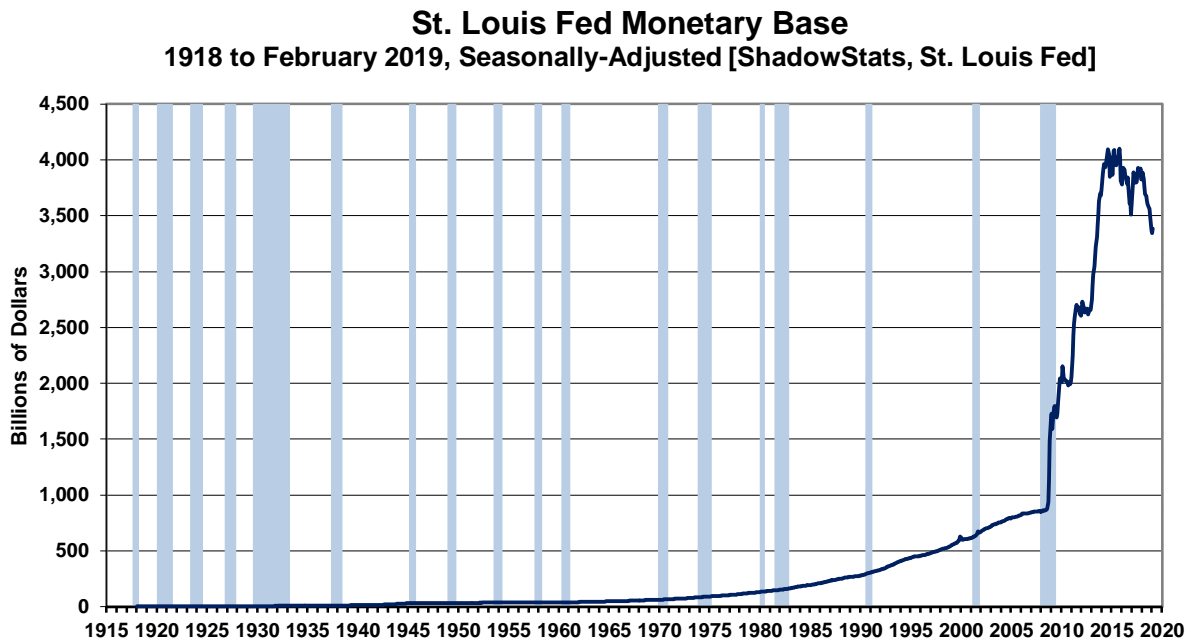
Annual Money Supply Growth Has Been Reasonably Stable, Yet the Related Monetary Base Is Seeing An Annual Collapse That Last Triggered the Second Down Leg of the Great Depression.

Graph 12 reflects year-to-year change in headline Money Supply M1, M2 and M3, where M3 is the ShadowStats Alternate estimate published since 2006, when the Federal Reserve ceased publishing its then-broadest measure of the money supply. Nominal annual growth has been reasonably flat on average in recent years, although inflation adjusted growth has been slowing recently, a traditional leading indicator to weakening activity. The FOMC has done much to insulate money supply in recent years from crisis-related movement in the monetary base, which otherwise has been the Fed’s traditional tool for targeting money supply growth.

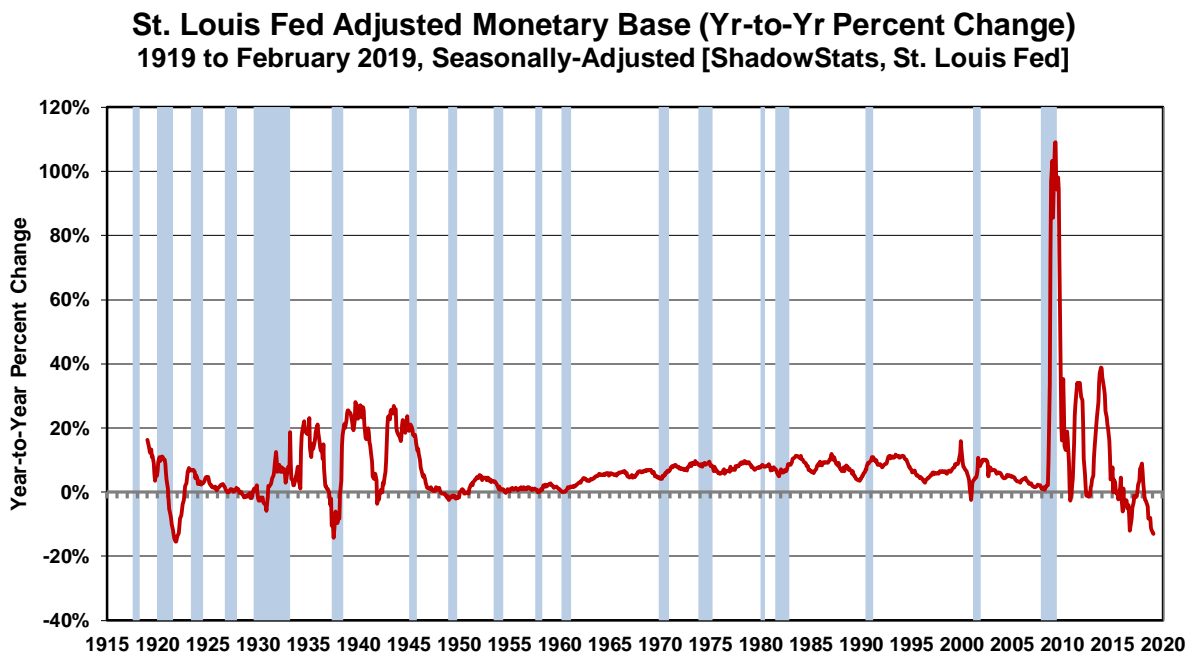
Graph 12: Comparative Money Supply M1, M2 and M3 Yr-to-Yr Changes through February 2019
(Same as *Graph 55* in *Pending Commentary No. 983-B*)



Graph 13: Saint Louis Fed Monthly Monetary Base, Billions of Dollars (Jan 1918 to Feb 2019)
(Same as Graph 55 in Pending Commentary No. 983-B)



Graph 14: Yr-to-Yr Percent Change, Monthly Saint Louis Fed Monetary Base (Jan 1919 to Feb 2019)
(Same as Graph 56 in Pending Commentary No. 983-B)



The Federal Reserve traditionally has used its control of the monetary base to set money supply growth, which recently has been historically low/declining in real terms (usually a leading indicator to the broad

economy), and what recently has been seen with only limited historical precedent. Shown in *Graphs 13* and *14* are plots of the monthly average level of the monetary base back to 1919 and the founding of the Federal Reserve. While the Fed generally did not begin targeting the Monetary Base until the 1960s, its growth historically always has had a strong leading relationship to economic activity.

In the context of what has been the FOMC's recent tightening stance, year-to-year change in the St. Louis Fed's measure of the adjusted monetary base declined year-to-year by 13.0% (-13.0%) in February 2019. This was the steepest annual decline since the collapse of the monetary base into July 1937, when it hit an annual decline trough of minus 14.3% (-14.3%) and broadly was credited with triggering the second down leg of the Great Depression.

That said, excessive (continuous quarterly) Federal Reserve rate hikes since December 2017, combined with the Fed's efforts at balance sheet liquidation have strangled consumer liquidity and triggered the unfolding economic downturn. With the Fed beginning to recognize the problem, will they reverse policy? Early signals are that further rate hikes and tightening are on hold. Yet, never having fully resolved the issues of the 2008 banking crisis, the FOMC likely will not only have to return to quantitative easing to forestall "new" risks of systemic collapse, but they likely will enter into some form of quasi-permanent quantitative easing, until such time as a debilitating financial panic (or an Act of Congress) forces a systemic overhaul. That circumstance is discussed in the pending *Special Commentary No 983-B*.

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