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

Bullet Edition Number 16

FOMC Issues and Distortions, Higher Inflation, Deteriorating Economic Outlook

December 15, 2019

**Pending Retail Payroll Revisions Show an Unfolding Recession;
November Real Retail Sales Suggested a Fourth-Quarter 2019 Contraction,
Signaling a Second Consecutive Troubled Holiday Shopping Season**

**November Monthly Growth in Real Average Weekly Earnings for All Employees
Held Unchanged at 0.0% for the Third Straight Month**

**The Fed Knows There Is No Sustainable, Moderate U.S. Economic Growth,
Contrary to Its Happy Hype, Yet the FOMC Is Unable to Cut Interest Rates**

**FOMC Will Continue to Meet Any Unexpected Funding Needs (QE) of Its
Parent Banking System, to Maintain Systemic and Market Stability and Liquidity**

**Where the FOMC Fully Understands the Problems In the
Overnight Funding Markets, It Does Not Want to Go Public with Them**

**FOMC Has Not Been Open About the Major Conflicts and Issues It Faces,
Suggesting Significant Systemic, Financial and Economic Crises May Be at Hand**

**Federal Reserve 2008 Bailout of the Failed Banking System Appears Only to Have
Bought Time; Not to Have Restored a Workable, Stable Financial System, and
Not to Have Allowed a Full, Sustainable Economic Recovery for Main Street, U.S.A.**

Week Ahead: Some Headline Numbers Will Benefit from the End of the GM Strike

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ShadowStats Commentaries

- The ***Daily Update*** posts daily, as needed, on the *ShadowStats* home page: ***www.ShadowStats.com***, right-hand column, providing initial coverage of all major U.S. economic reporting, within two-to-three hours of headline publication, as well as coverage of unusual financial-market or political developments.
- ***Bullet Edition*** publishes each weekend, providing *ShadowStats* primary coverage of the past week's unfolding activity, reviewing economic releases, financial-market, systemic and political developments. [Next planned release: ***Bullet Edition No. 17*** (December 22nd) covering November Industrial Production, Housing Start and the final Third-Quarter 2019 GDP.]
- ***Flash Update***, interspersed with ***Bullet Editions*** is limited in scope, highlighting near-term events or developments—usually same- or next-day—with the economy, financial markets, politics, the Federal Reserve or with other news of significance that should be reviewed in advance of the Weekend ***Bullet Edition*****.** [Next release planned: ***Flash Update No. 17*** (to be determined).]
- ***Special Commentaries*** should publish every quarter or so, providing a more-comprehensive overview of general, broad economic and financial conditions and trends, such as seen in the recently published ***Special Commentary No. 985*****.**
- ***Hyperinflation*** and ***Consumer Liquidity Watches*** will supplement irregularly the weekly ***Bullet Edition***, covering evolving market and consumer circumstances, otherwise with occasional specific data covered directly in the weekly ***Bullet Editions****.*
- ***Economic Surveys of the General Public*** are conducted irregularly and are open to both subscribers and nonsubscribers.
- ***Telephone Consulting*** is included as part of our regular service. If you have a question or otherwise would like to talk, please call John Williams at (707) 763-5786.

All ***Current*** and ***Earlier ShadowStats Commentaries*** (back to 2004) are available in the ***Archives*** (click on *All Commentaries*, then *List Commentaries*) in the left-hand column of the ***ShadowStats Home Page***.

ShadowStats Broad General Outlook Has Not Changed. ShadowStats' Recession Forecast remains in place, with U.S. Economic activity in a deepening downturn, as detailed in the recently published ***Special Commentary No. 985***. Complicated and intensified by deteriorating domestic political and liquidity circumstances, the ShadowStats broad outlook in the weeks and months ahead remains for:

- A rapidly intensifying U.S. economic downturn, reflected in
- Mounting selling pressure on the U.S. dollar, against currencies such as the Swiss Franc,
- Continued flight to safety in precious metals, with upside pressures on gold and silver prices, and
- Increasingly high risk of extraordinarily heavy stock-market selling.

Your comments and suggestions are invited. Always happy to discuss what is happening.

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

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Overview

A Flummoxed Fed Versus Unfolding Economic and Systemic Reality

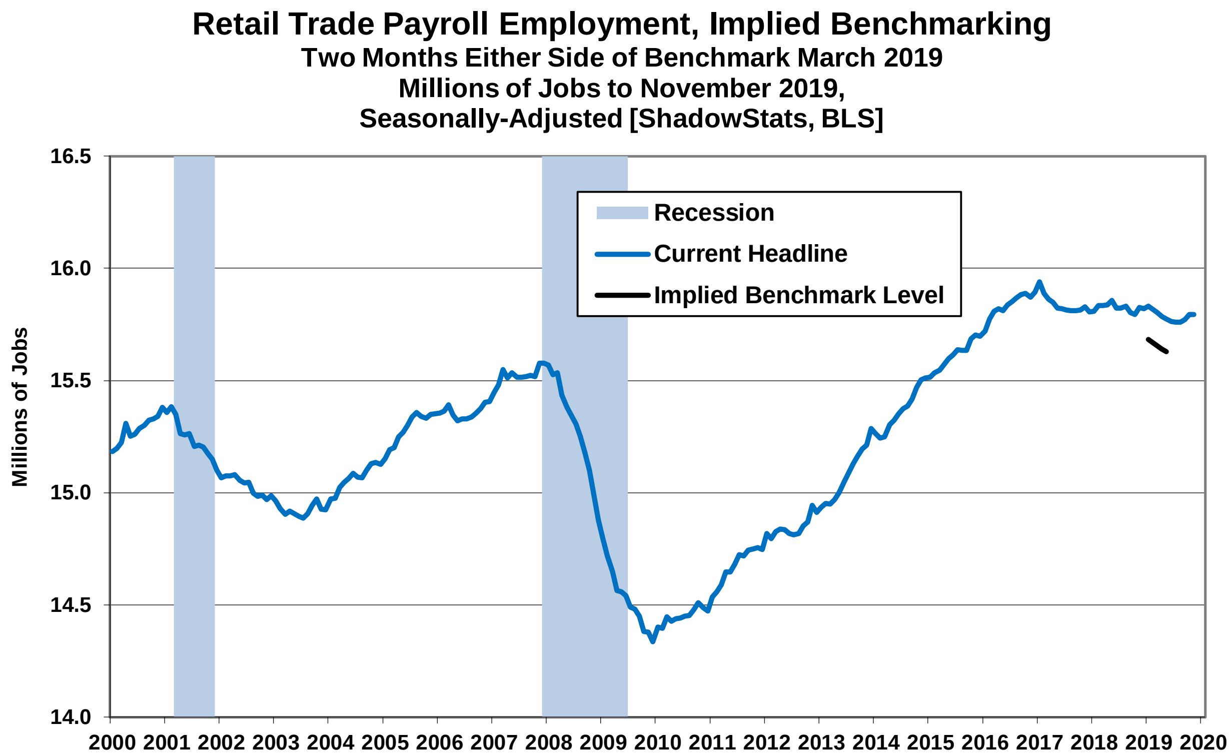
FOMC Unwillingness to Come Clean on Underlying Economic Reality and Systemic Liquidity Issues Suggests Severe Financial System Crises Could Be at Hand. When one knows, or strongly fears, that if certain knowledge were imparted to the public, or to the investment community, that a financial panic and economic turmoil would ensue, entities such as the Federal Reserve or the U.S. Treasury usually would tend to keep that knowledge under wraps, hoping to find ways of mitigating a difficult circumstance. The Federal Reserve Chairman's Press Conference on December 11th, confirming ongoing positive and stable moderate economic growth, along with something to the effect of "Don't worry, we have year-end funding needs covered," literally had my hair standing on end. Continued expansion of funding and lack of rational explanation for same puts the lie to the second point.

Consider in particular, though, the first point: not easing because of a healthy economy. If the U.S. economy indeed is falling into recession, as I contend, the FOMC delaying a needed rate cut will make the eventual rate cut that follows less effective than it would have been earlier, forcing more aggressive action than would have been needed earlier. Granted, the headline Federal Funds Rate is low, but it still can go quite a bit lower, as the FOMC has done in the past. I know enough about the fine economists in the Federal Reserve System that they know U.S. employment, let alone the economy, is not as hyped.

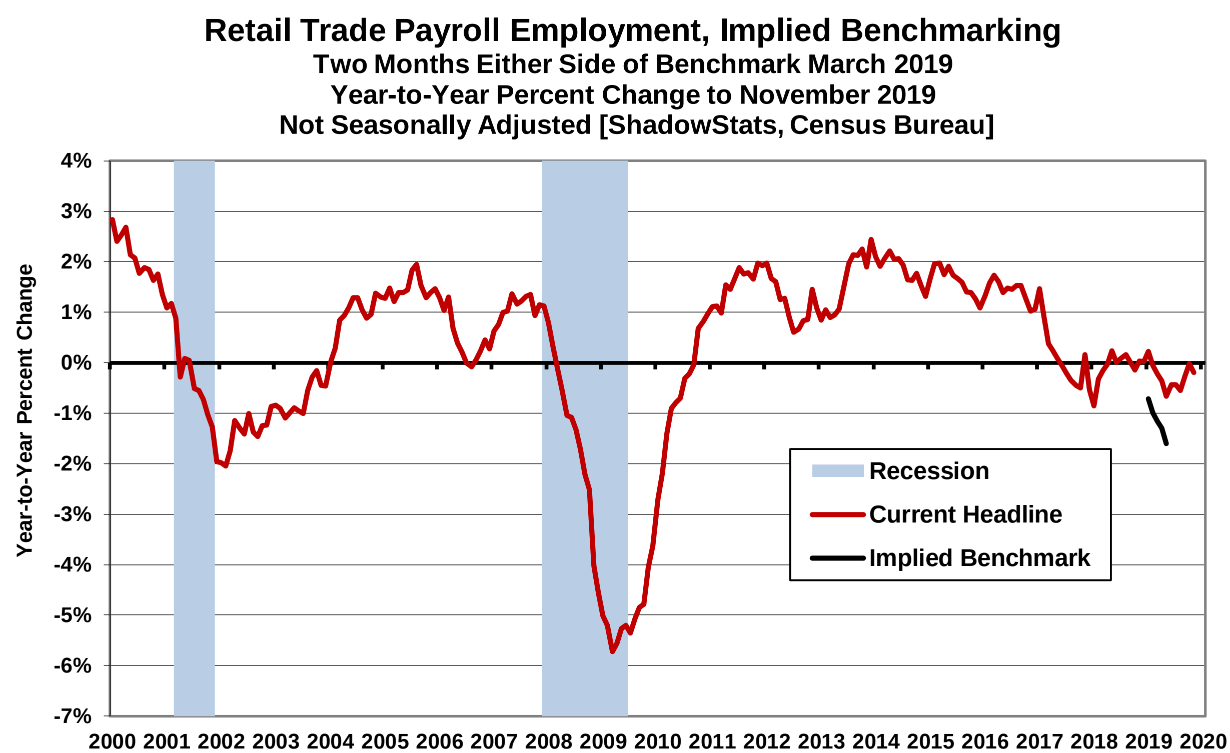
The happy-employment pabulum fed to the public at the December 11th FOMC Press Conference encompassed strong payrolls. Yet, the Bureau of Labor Statistics announced its ***2019 Initial Payroll Employment Benchmark Revision*** of a negative 501,000 (-501,000) jobs on August 11, 2019, which knocked off 20% of the headline payroll growth of the prior year. The final benchmarking and related day of reckoning is scheduled for February 7, 2020. The Retail Trade Sector, by itself, was revised lower by 146, 400 (-146,400) jobs, plotted in ***Graphs 1*** and ***2*** on the next page, reflecting both the headline data, as well as the net benchmarking plotted around the benchmark month (two months on either side), reflecting both the level and year-to-year growth in the series. In particular, ***Graph 2*** clearly shows a pattern consistent with unfolding recession. Discussed later, November Real Retail Sales, not yet corrected for the benchmarking, is trending for a real Fourth-Quarter 2019 quarterly contraction.

Federal Reserve Appears to Have Lost Control of the System. Discussed in ***Special Commentary No. 983-B***, the Fed's bailout of the failed banking system bought time, but it never resolved the banking system instabilities, and never allowed for any approaching a normal economic recovery for Main Street, U.S.A. Consider as well, the more recent issues covered and previewed in ***Special Commentary No. 985***, ***Bullet Edition No. 15*** and reviewed ***Flash Update No. 16***.

Graph 1: Retail Sales Payroll Employment, January 2000 to November 2019 **[Implied Benchmarking]**



Graph 2: Retail Sales Payroll Employment, Year-to-Year Change, January 2000 to November 2019



Economic Activity – Latest Numbers

November Retail Sales, Consumer and Producer Price Indices

Real Retail Sales on Track for a Fourth-Quarter 2019 Contraction

Real Earnings Were Unchanged for the Third Straight Month

Fourth-Quarter 2019 Real Retail Sales Are on Track for Its First Quarterly Contraction Since Fourth-Quarter 2015 and the 2014-2016 Mini-Recession. Weaker-than-expected November Retail Sales showed the Holiday Shopping Season to be in trouble, with fourth-quarter Real Retail Sales on track for its first quarterly decline in five years. November Retail Sales activity was not quite in the happy mode of the December 11th Federal Reserve's Federal Open Market Committee (FOMC) announcement of continuing "sustainable moderate economic growth," given the Census Bureau's reporting of December 13th.

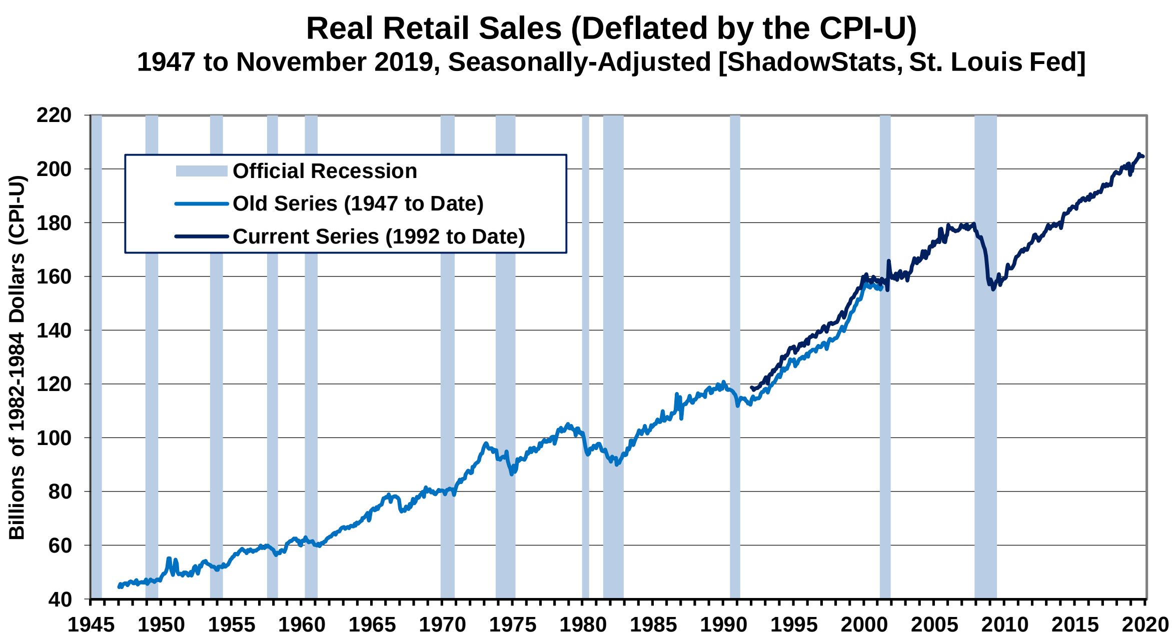
Against offsetting negative and positive revisions to September and October 2019 activity, headline November 2019 Nominal Retail Sales showed a monthly gain of 0.19%, against an expected gain of about 0.5%. That was negative month-to-month in inflation-adjusted real terms, adjusted against headline monthly CPI-U inflation of 0.26%, standardly calculated by the St. Louis Fed. As signaled last month, the Holiday Shopping Season remained on track for a second consecutive weak showing.

***Slowing Real Growth*.** Inflation-adjusted Real Retail Sales declined month-to-month by 0.07% (-0.07%) in November 2019, gained a revised 0.09% in October [previously down by 0.9% (-0.9%)] and dropped by 0.44% (-0.44%) [previously down 0.35% (-0.35%)] in September. Year-to-year real annual growth slowed to 1.28% in November, from 1.45% [previously 1.31% in October] and 2.21% [previously 2.30%] in September.

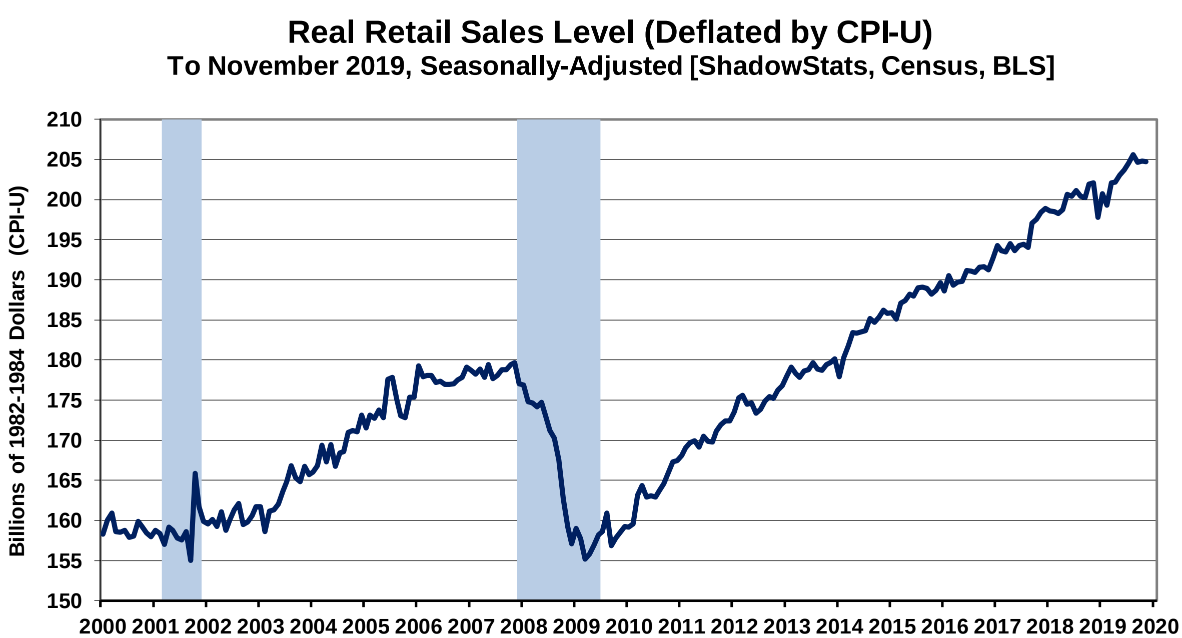
Quarterly Real Retail Sales growth slowed from an annualized 4.6% in Second-Quarter 2019, to a revised 3.8% [previously 4.0%] in Third-Quarter-2019, with Fourth-Quarter 2019 on early track (two-months of reporting) for a quarterly decline of 0.3% (-0.3%).

Graphs 3 to ***6*** show the traditional long-term and short-term plots of headline Real Retail sector, both as to level and as to year-to-year percent change. Related plots of Retail Trade payroll employment, as headlined and as pending annual benchmarking are shown earlier in ***Graphs 1*** and ***2***. The Leisure and Hospitality sector, which combines with the Retail Trade sector to cover the Retail Sales series, is pending a parallel, major downside benchmark revision on February 7, 2020.

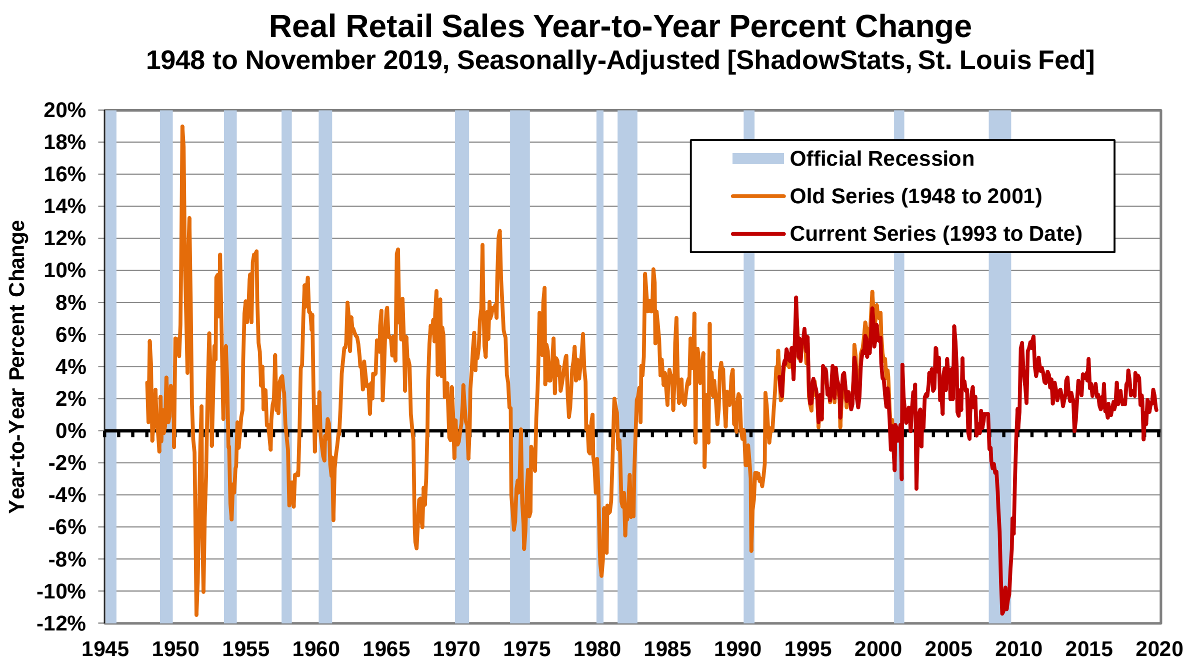
Graph 3: Real Retail Sales, 1947 to November 2019



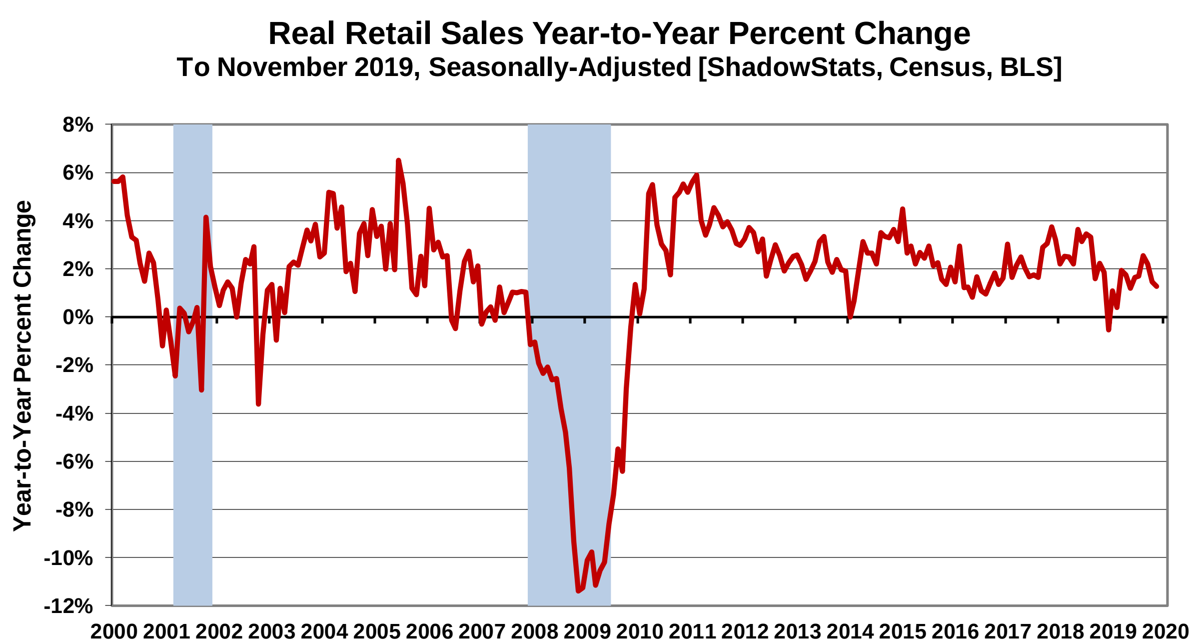
Graph 4: Real Retail Sales, 2000 to November 2019



Graph 5: Real Retail Sales, Year-to-Year Percent Change, 1948 to November 2019



Graph 6: Real Retail Sales, Year-to-Year Percent Change, 2000 to November 2019

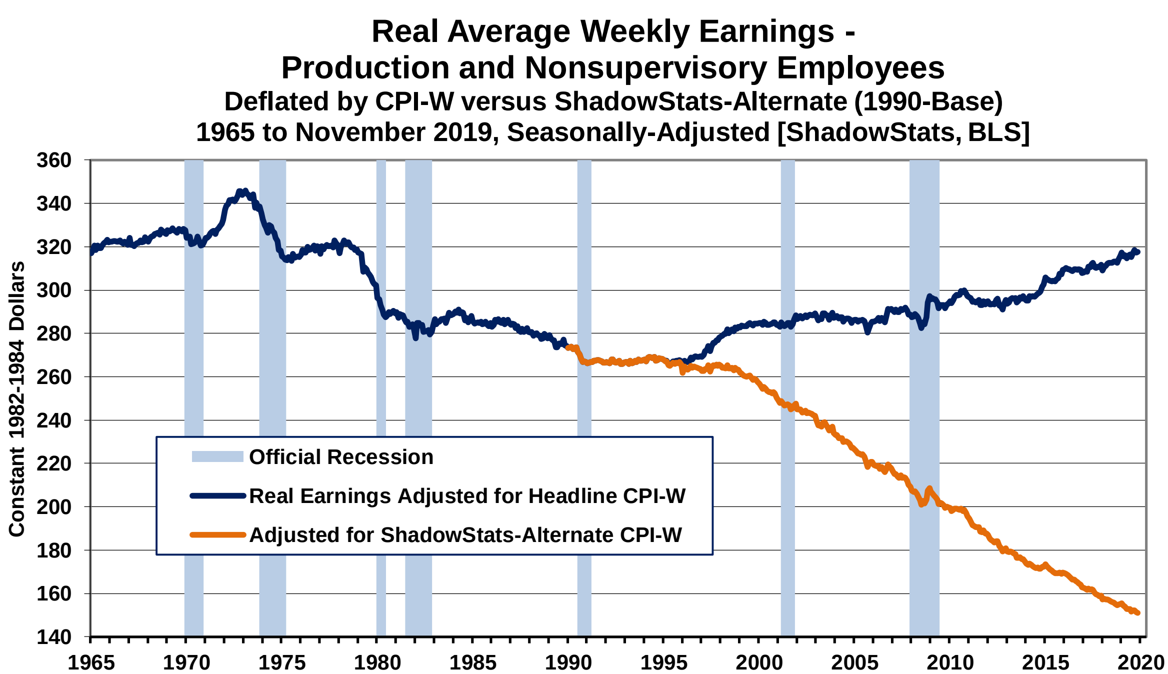


Real Earnings for All Employees Were Unchanged for Third Straight Month

Combine Lack of Real Growth in Earnings and Low Levels of Non-Recovered Consumer Credit, and the U.S. Consumer Is in a Weak Position to Boost Broad Economic Activity. As discussed and graphed previously in ***Flash Update No. 16***, for the third straight month, both inflation-adjusted *Real Average Hourly Earnings* and *Real Average Weekly Earnings* were stagnant month-to-month, unchanged at zero (0.0%) for *All Employees* (uses the CPI-U for deflation), not a particularly happy circumstance coming into the Holiday Shopping season. Accompanying ***Graph 7*** shows the narrower and more volatile *Production and Nonsupervisory Employees* sub-category, which has a longer history, back to 1965. Adjusted for headline CPI-W inflation, which the BLS uses here, headline inflation-adjusted real activity in November 2019 held 8.2% (-8.2%) shy of its February 1973 historic high, in today's real earnings, when headline unemployment then was at 5.0%, instead of today's 3.5%.

With any luck, growth in headline inflation-adjusted Consumer Credit can make up any difference in real income shortfall as to consumer liquidity. Yet, as broadly measured by the Federal Reserve, the inflation-adjusted level of Consumer Credit never has recovered its pre-Great Recession high, still shy minimally by 10% (-10%). Is there something here the FOMC could do to help the consumer? Purportedly, nothing further is needed with "sustainable, moderate economic growth."

Graph 7: Real Average Weekly Earnings, Production and Nonsupervisory Employees (1965 to November 2019)



November 2019 Consumer and Producer Price Indices

Annual CPI-U Inflation Rose to a 12-Month High of 2.1%

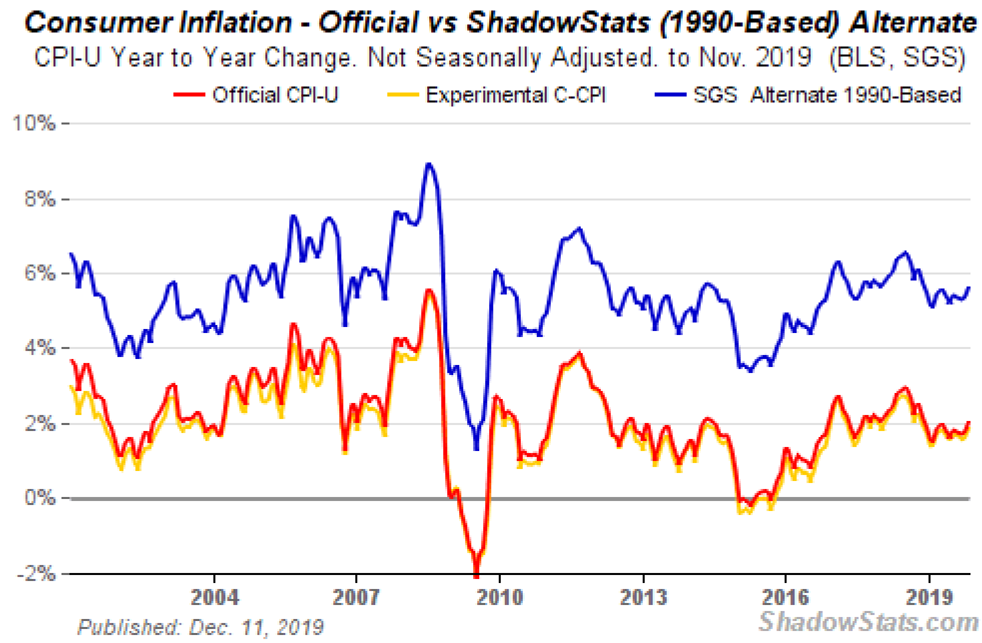
November 2019 Consumer Price Index (CPI) Rose 0.26% in Month, 2.05% Year-to-Year. Also as discussed previously in ***Flash Update No. 16***, reported by the Bureau of Labor Statistics on December 11th, where monthly CPI-U inflation slowed to 0.26% in November, from 0.36% in October, annual inflation jumped to a twelve-month high of 2.05% in November 2019 versus 1.76% in October. The year-to-year increase in annual inflation was an artefact of extreme volatility seen in gasoline prices one-year ago.

By major category, November Food inflation rose by 0.12% in the month, but declined 0.06% (-0.06%) year-to-year, against monthly and annual gains of 0.24% and 2.07% in October. November Energy inflation rose by 0.80% month-to-month, down by 0.59% (-0.59%) year-to-year. That was against a 2.70% monthly gain in October and an annual decline of 4.17% (-4.17%), with November "Core" Inflation (net of Food and Energy) up by 0.23% in the month and 2.32% year-to-year, against monthly and annual gains of 0.16% and 2.31% in October.

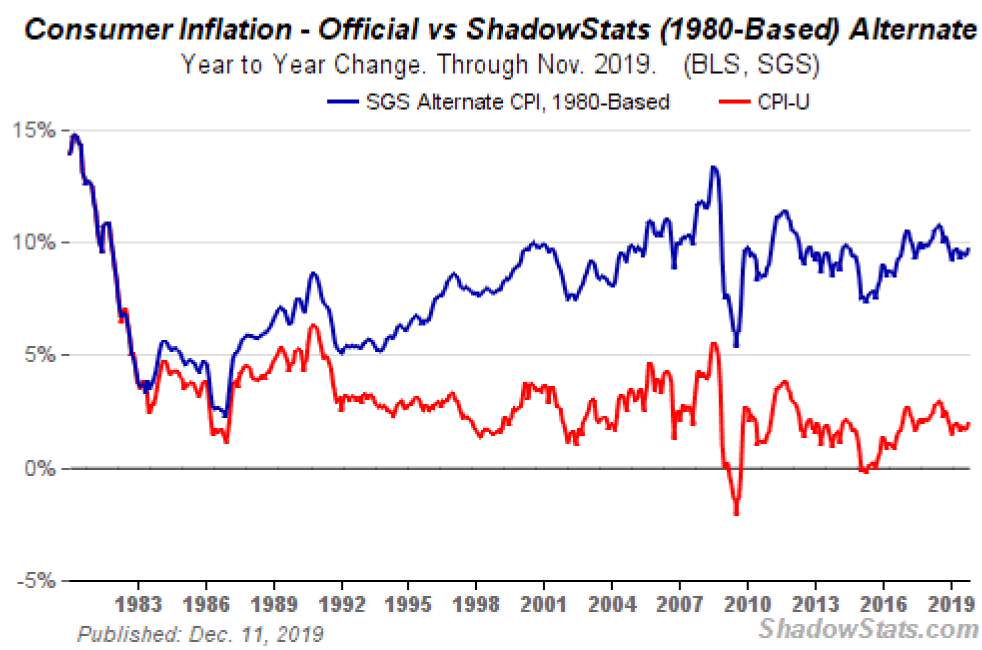
The November 2019 ShadowStats Alternate CPI (1980 Base) jumped to 9.8% year-to-year, versus 9.5% in October and 9.4% in September, reflected in ***Graphs 8*** and ***9***. Further detail is also is found on the ***Alternate Data tab of the ShadowStats Home Page***, including links there to the latest data, inflation calculator and the background detail provide there in ShadowStats' ***Public Comment on Inflation Measurement***.

[Graphs 8 and 9 of Headline Annual CPI-U Inflation versus the ShadowStats Alternate Inflation Measures follow on the next page.]

Graph 8: CPI – Official vs. ShadowStats (1980-Based), Year-to-Year Percent Change



Graph 9: CPI – Official vs. ShadowStats (1990-Based), Year-to-Year Percent Change



November Final Demand PPI Was Unchanged in the Month Due to Its Seriously Flawed Construct

Monthly Goods Gained 0.35%, Reflecting Higher Food, Energy and "Core" Prices

Annual PPI-Goods Inflation of 0.17% Was the First Gain in Four Months

The Heavily Flawed November 2019 Producer Price Index, Final-Demand, Dropped to "Unchanged" at 0.00% in the Month, from 0.42% in October, Holding at a 39-Month Year-to-Year Low of 1.11%. The headline Producer Price Index – Final Demand (PPI-FD) is constructed to reflect inflation in both Goods and Services, but the dominant Services measurement is definitionally inconsistent with most inflation calculations, measuring coincident profit margins instead of prices in its "Trade" sector.

As a result, usual data disruptions are seen there with highly volatile gasoline prices, where large price increases/decreases are mathematically offset by decreases/increases in current-month profit margins for gas stations. As reported by the Bureau of Labor Statistics (BLS) on December 12th, that phenomenon in November was seen particularly with rising food prices and falling margins at grocery stores. As a result, Goods inflation rose by 0.35% in the month, but dominant Services declined by 0.33% (-0.33%) in the month, with a net 0.00% "no change" in the aggregate PPI-FD.

By major sector, the 1.11% year-to-year inflation in aggregate November and October PPI-FD reflected annual Goods inflation of 0.17% in November versus a negative 0.60% (-0.60%) in October, with annual Services inflation respectively of 1.45% versus 1.95%, and Construction inflation of 3.71% versus 3.88%, with Construction down from its series high of 5.52% annual inflation in September 2019.

[The Week Ahead Section begins on the next page.]

Week Ahead: Varied Impact from the End of the General Motors Strike

Yet It Should Show as a Net Negative Factor for Fourth-Quarter GDP

November 2019 Industrial Production

An Overhaul to the CASS Freight Index?

Third Estimate of Third-Quarter GDP

General Motors Strike Impact: November Industrial Production (Tuesday, December 17th) Should See Some Rebound (or Less Negative Growth), Something Likely Less than the 0.5% Corrective Boost Indicated by Earlier Federal Reserve Estimates of the Cost to Headline Production and 0.8% to Manufacturing. Growth should hold well shy of consensus estimates of 0.8% or more in aggregate Production. Keep in mind that broad areas of Production have turned lower in Manufacturing, as well as in Oil and Gas Exploration in Mining. Certain parameters of the strike and effects on recent economic data include:

- The General Motors Strike began September 15, 2019 and ended on October 25th
- With reduced imports, it narrowed the Trade Deficit in September and October, with implications of a widening Trade Deficit in November.
- Reduced Manufacturing employment by 42,000 in October, added 41,000 jobs in November.
- Hit Industrial Production (Manufacturing) hard in September and October, with implications for reversing boosts in November of 0.5% to monthly Production in and 0.8% to monthly Manufacturing.

November Cass Freight Index™ (Likely in the Week Ahead) Should See Some Positive Impact on Freight, But the Series Is Going Through Changes. ***Changes to Cass Freight Index*** have been announced in terms of new partners joining in the analysis and reporting of what I consider one of the highest quality economic indicators available. The first edition of the new reporting likely should take place in the week ahead. We wish all the parties involved good luck and good fortune with their new venture, and look forward to expanded and continuing, reliable and high-quality information that should be forthcoming. Expanded current freight activity here would on a relative basis, where the headline monthly freight numbers currently are not seasonally adjusted.

November New Residential Constriction: Housing Starts and Building Permits (Tuesday, December 17th). This series usually is nonsensically volatile in its initially reporting, subject to massive revisions in the next month or two following. Headline numbers are almost never statistically significant. Expectations for Starts are on the upside, but to the downside on Permits, but again, the numbers are without meaning in their initially reporting.

Third Estimate of Third-Quarter 2019 GDP (Friday, December 20th) Is Expected at 2.1% to 2.2%, Versus 2.1%. The Bureau of Economic Analysis already has built in its impact of the GM strike to last month's estimate. I would expect it to hold at 2.1%, or revise lower to 2.0%. The trade revisions did not boost it, because they went back to include the second quarter, which also narrowed:

Noted December 5th (Bullet Edition No. 15): October 2019 Trade Deficit Narrowed by $4.2 Billion, Encompassing Impact of the General Motors Strike. Reported by the Census Bureau and Bureau of Economic Analysis on December 5th, the sharp narrowing of the October Trade Deficit to $47.2 billion, from a revised $51.1 (previously $52.5) billion in September largely reflected reduced imports due to the GM strike, which also contributed to the $2.4 billion narrowing of September deficit. While a narrowed deficit boosts GDP, the full impact of the GM strike still will be a net negative for the GDP (see discussion of Industrial Production impact in ***Special Commentary No. 985***). Separately, where the monthly trade deficits narrowed in revision back to April, the relative Third-Quarter 2019 versus Second-Quarter 2019 deficit narrowed only minimally, with minimal positive-revision implications for the third-estimate of Third-Quarter 2019 quarterly GDP growth.

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