

John Williams'
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Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 412
December Retail Sales, November Trade Balance

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**Make-or-Break Month for Retailers Was Flat-to-Minus,
Both Before and Likely After Adjustment for Inflation**

**Worse-Than-Expected Retail Sales and Trade Data
Should Dampen 4th-Quarter GDP Growth Outlook**

PLEASE NOTE: The next regular Commentary is scheduled for Thursday, January 19th, covering the estimates of December 2011 CPI, PPI, industrial production, real retail sales and housing starts. Publication of Hyperinflation 2012 also is planned for next week. As soon as a firm date is set, such will be posted in the Next Regular Commentary box on www.shadowstats.com and at the [Schedule](#) link.

Best wishes to all — John Williams

Opening Comments and Executive Summary. In advance of next week's heavy economic calendar, the reporting of yesterday's (January 12th) December retail sales and today's November trade deficit were suggestive of a slower pace of economic activity than commonly has been hyped in the popular press. With December industrial production and housing activity also likely to disappoint market expectations, in the week ahead, the usual unwinding of the holiday-season economic hype—otherwise used to encourage consumer buying—should be well underway. Accordingly, market expectations of a relatively

strong fourth-quarter versus third-quarter GDP activity should dampen quickly. The government's first estimate of fourth-quarter economic activity is due for release in two weeks (January 27th).

Retail Sales. The 0.1% (0.09%) headline monthly gain in December 2011 retail sales was not statistically meaningful, and it very likely did not top the pace of consumer inflation during the month. Further, where December is the dominant month of the year for retailers, the numbers net of automobile sales were even bleaker, down 0.21%. Automobile sales have been far removed from normal activity and distorted by government intervention.

The 0.1% headline gain in December followed a revised 0.4% (previously 0.2%) increase in November, with December's year-to-year growth slowing to 6.4% from 7.0% in November.

Trade Deficit. A monthly decline in exports and a monthly increase in imports boosted the November 2011 monthly trade deficit to \$47.8 billion from \$43.3 (previously \$43.5) billion. Net of inflation (including higher oil prices), the numbers suggested a neutral impact of what will be a partially-estimated net-export account on the "advance" estimate of fourth-quarter 2011 GDP growth. Some positive GDP growth impact had been suggested by the initial October trade report.

Hyperinflation Watch—Outlook is Unchanged. The general outlooks on the economy, inflation, financial markets and systemic stability remain unaltered from the discussions in [Hyperinflation Special Report \(2011\)](#). The soon-to-be-published *Hyperinflation 2012* will review fully and expand upon those key issues discussed in the 2011 report.

REPORTING DETAIL

RETAIL SALES (December 2011)

December Retail Sales Gain, Again, Was Not Statistically Meaningful. As has been the case in seven of the last eight months, the monthly change in December retail sales was not statistically meaningful, and likely was flat-to-minus, adjusted for inflation. Those results reflect effectively no month-to-month gain and softening year-to-year sales for what was the dominant retail sales month of 2011. The evidence here continues to be for a bottom-bouncing economy.

Further, the concurrent seasonal-factor issues and broader distortions seen otherwise in seasonal-adjustment factors and sampling methodologies, as discussed in the [Hyperinflation Special Report \(2011\)](#), continue. The stability of the seasonal-adjustment process and sampling methods have been disrupted

severely by the unprecedented depth and length of the current economic downturn in the post-World War II era (the period of modern economic reporting).

Under such circumstances, where the markets effectively are flying blind as to actual economic activity, consideration of broad underlying fundamentals is essential. Consumer income and credit remain structurally impaired and continue to signal economic deterioration, not recovery, with the broad economy remaining in serious trouble (see [Commentary No. 401](#)). Consumer liquidity conditions will be reviewed in the pending *Hyperinflation 2012*.

Nominal (Not-Adjusted-for-Inflation) Retail Sales. Yesterday's (January 12th) report on December 2011 retail sales—issued by the Census Bureau—indicated a statistically-insignificant, seasonally-adjusted monthly gain of 0.09% (up by 0.32% before prior-period revisions) +/- 0.6% (95% confidence interval). December's increase followed a revised 0.41% (previously 0.22%) monthly gain in November.

On a year-to-year basis, December 2011 retail sales were reported up by 6.45%, a slower pace than seen in the revised year-to-year November 2011 gain of 6.99% (previously 6.75%).

Real (Inflation-Adjusted) Retail Sales. Details on real retail sales for December will be published in the Thursday, January 19th, *Commentary*, along with details from the December 2011 CPI-U release. Where December CPI-U inflation likely will be flat-to-positive (see *Week Ahead*), official December CPI-U inflation has the potential to offset fully the nominal (not adjusted for inflation) sales gain.

Core Retail Sales. In December 2011, as in initial November retail sales reporting, both gasoline stations and groceries stores showed small declines in monthly sales (revised November 2011 gasoline station sales now are stronger than October's reading). Assuming that the bulk of non-seasonal variability in food and gasoline sales is in pricing, instead of demand, "core" retail sales—consistent with the Federal Reserve's preference for ignoring food and energy prices when "core" inflation is lower than full inflation—are estimated using two approaches:

Version I: December 2011 versus November 2011 seasonally-adjusted retail sales—net of total grocery store and gasoline station revenues—was up by 0.38%, versus an official gain of 0.09%.

Version II: December 2011 versus November 2011 seasonally-adjusted retail sales—net of the monthly change in revenues for grocery stores and gas stations—was up by 0.29%, versus an official gain of 0.09%.

U.S. TRADE BALANCE (November 2011)

November Trade Deficit Widened Beyond Expectations. Reflecting some possible catch-up from prior underreporting of the trade shortfall, the November trade deficit widened enough to neutralize what had looked initially to be a positive element for fourth-quarter 2011 GDP reporting. Going forward, underlying fundamentals still indicate an ongoing deterioration in the U.S. trade balance.

Nominal (Not-Adjusted-for-Inflation) Trade Deficit. The Bureau of Economic Analysis (BEA) and the Census Bureau reported today (January 13th) that the nominal, seasonally-adjusted monthly trade deficit in goods and services for November 2011, on a balance of payments basis, widened to \$47.8 billion, up from a revised \$43.3 (previously \$43.5) billion in October. A deteriorating trade deficit is a net negative contributor to domestic economic activity, and November's deterioration was worse than had been expected by consensus forecasters.

As has become the standard caution here, heavy distortions likely continued in the seasonal adjustments, much as has been seen in other economic releases, such as retail sales, where the headline number reflects month-to-month change. As has been discussed frequently (see the [Hyperinflation Special Report \(2011\)](#) for example), the extraordinary length and depth of the current business downturn have disrupted regular seasonality patterns. Accordingly, the markets still should not be relying heavily on the accuracy of monthly headline data.

Against the revised October numbers, the reported seasonally-adjusted November trade balance reflected the combined economic negatives of declining exports and rising imports. Rising oil prices and increased physical volume were factors in the import increase.

Crude Oil and Energy-Related Petroleum Products. For the month of November 2011, the not-seasonally-adjusted average price of imported oil rose to \$102.50 per barrel, down from \$98.84 in October, and was up from \$76.81 in November 2010. In terms of not-seasonally-adjusted physical oil imports, November 2011 volume averaged 8.874 million barrels per day, up from 8.490 million in October 2011, and up from 8.596 million in November 2010.

Real (Inflation-Adjusted) Trade Deficit. Adjusted for seasonal factors and net of oil price swings and other inflation (2005 chain-weighted dollars as used in reporting real GDP), the reported November merchandise trade deficit came in at \$47.5 billion, a larger deficit than the revised \$44.0 (previously \$44.2) reported for October.

Based on today's reporting of the second of three months in fourth-quarter 2011, an initial estimate of the annualized fourth-quarter real trade deficit—used as a base for the GDP's net export account—would be \$549.2 billion, little changed from the annualized real third-quarter 2011 trade deficit of \$552.0 billion. Where the initial October reporting annualized to a deficit of \$530.3 billion for the fourth-quarter, and where the November estimate disappointed market expectations, it is likely that today's trade reporting will dampen expectations for the BEA's initial guess at fourth-quarter GDP on January 27th. Fourth-quarter trade factors now likely will be largely neutral in their contribution to reported fourth-quarter economic activity, rather than the positive contribution initially suggested by October's reporting.

Week Ahead. Recognition of an intensifying double-dip recession as well as an escalating inflation problem still is sporadic. The political system would like to see the issues disappear until after the 2012 election, the media does its best to avoid publicizing unhappy economic news during the holiday shopping season, and the financial markets will do their best to avoid recognition of the problems for as long as possible, problems that have horrendous implications for the markets and for systemic stability.

Until such time as financial-market expectations move to catch up fully with underlying reality, or underlying reality catches up with the markets, reporting generally will continue to show higher-than-expected inflation and weaker-than-expected economic results in the months and year ahead. Increasingly, previously unreported economic weakness should show up in prior-period revisions.

Industrial Production (December 2011). December 2011 industrial production is due for release on Wednesday, January 18th, and could be flat-to-minus for the month, net of revisions, as some reporting catch-up versus previously overstated growth seems to be working itself into various year-end data. Odds are good for a downside surprise to what likely will be a relatively strong consensus outlook. The consensus likely will have been inflated some by seasonally misadjusted strength reported in the December purchasing managers (manufacturing) survey.

Producer Price Index—PPI (December 2011). The December 2011 PPI is due for release on Wednesday, January 18th. Given mixed monthly oil prices and a seasonal boost to reporting of adjusted energy costs, the irregularly volatile PPI likely will show a gain in wholesale prices for December 2011. As has been the case since the onset of QE2, the effects of higher oil prices also continue to spread within broad domestic economic activity.

Consumer Price Index—CPI (December 2011). The December 2011 CPI is due for release on Thursday, January 19th. Once again, inflationary pressures from the ever-widening spread of the impact of high oil prices into the broad economy should generate upside inflation pressures. Not seasonally adjusted, monthly gasoline prices dropped by 3.4% in December (Department of Energy). That should be offset largely by Bureau of Labor Statistics seasonal factors. In December 2010, a 4.5% unadjusted monthly gain in gasoline prices was turned into an 8.5% monthly gain, after seasonal adjustment. Reporting risk likely is to the upside of what should be a fairly flat consensus outlook.

Year-to-year total CPI-U inflation would increase or decrease with the December 2011 reporting, dependent on the seasonally-adjusted monthly change, versus the 0.43% gain in the adjusted monthly level reported for December 2010. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for December 2011, the difference in December's headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from November 2011's reported annual inflation rate of 3.39%.

Residential Construction (December 2011). December 2011 housing starts are due for release on Thursday, January 19th. The general downside bottom-bouncing seen in the series should continue. As usual, any upside movement likely would not be statistically meaningful.
