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September Trade Balance, Presidential Election

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September Trade Data Suggest Upside Pressure on GDP Revision

Hurricane Sandy May Have Disrupted Flow of Trade Data

**No Meaningful Shift in Control of U.S. Government,
As Budget-Deficit and Debt-Limit Woes Come to the Fore**

PLEASE NOTE: The next regular Commentary is scheduled for Thursday, November 15th, covering the release of October retail sales, PPI and CPI, followed by a Commentary on Friday, November 16th, reviewing October industrial production.

The Special Commentary now scheduled for Monday, November 12th, will update the broad economic, systemic and inflation outlooks, in the context of the 2012 election results and the latest available detail on economic reporting, federal government fiscal operations, and Federal Reserve monetary activities. Any further publication detail will be posted in the schedule box on www.ShadowStats.com.

Best wishes to all — John Williams

Opening Comments and Executive Summary. The election appears to have resulted in no meaningful shift in control of the United States government. Despite any near-term, post-election niceties by partisan rivals, prospects for meaningful action by the White House and Congress to establish fiscal discipline, or to heal the structural impairments in the U.S. economy, remain nil.

When Congress and the White House last were negotiating “deficit reduction,” the package purportedly being discussed—before negotiations collapsed—was little more than fluff. Now, with the “fiscal cliff” looming at year-end, at least partially as a result of last-year’s failed deficit negotiations; and with the U.S. Treasury indicating that the next increase in the U.S. debt ceiling will be needed around year-end; deficit reduction issues (taxation and spending) will be coming to a head quickly, along with questions of renewed economic stimulus.

There is no reason to expect that renewed efforts at federal budget deficit reduction will result in anything more than the usual smoke and mirrors, further increasing, not reducing, long-term U.S. sovereign-solvency risk. In reality, the U.S. economy has not recovered, and no recovery is pending. Consumer liquidity remains severely impaired, and broad business activity continues to falter anew. As a result, the actual federal budget deficit going forward will be much worse than the relatively rosy numbers being used as the basis for government negotiations.

Accordingly, global market reaction—to a severely deteriorating outlook for U.S. fiscal conditions—increasingly should reflect massive flight from the U.S. dollar and movement into gold and the stronger Western currencies. These circumstances will be explored in detail in the *Special Commentary*. The general outlook put forth in [Hyperinflation 2012](#) has not changed.

September U.S. Trade Balance. The headline September 2012 trade deficit showed an unexpected narrowing to \$41.5 billion from a revised \$43.8 (previously \$44.2) billion in August. The reduced level of deficit, however, may have been an artifact of disruptions to the flow of trade-data reporting from the impact of Hurricane Sandy. While the late-October storm had no impact on actual September trade activity, it appears to have delayed the reporting of some September imports, which could mean a faux reduction the monthly trade shortfall. To the extent there were distortions, the detail should be corrected with next month’s reporting. Actual trade activity in October and November will reflect disruptions to physical imports and exports. Irrespective of near-term reporting distortions, the U.S. trade deficit continues in a pattern of long-term deterioration.

The reported narrowing of the September deficit also worked through to the imputed annualized quarterly trade deficit, adjusted for GDP-related inflation. While real (inflation-adjusted) third-quarter 2012 deficit still appears to have widened relative to the second quarter, the pace of deterioration was not as bad as estimated initially. As a result, the November 29th first-revision to the third-quarter 2012 GDP estimate should see some positive pressure from the September trade results.

[More complete details on the September trade release are found in the Reporting Detail section.]

Hyperinflation Watch—Update Pending. The broad outlook has not changed from that outlined in [Hyperinflation 2012](#), but it will be updated fully in the pending *Special Commentary*. For new subscribers and for anyone else not familiar with my general outlook, the recent summary in the *Hyperinflation Watch* section of [Commentary No. 479](#), and particularly the hyperinflation report (linked above) are suggested as background material.

REPORTING DETAIL

U.S. TRADE BALANCE (September 2012)

Narrower September Deficit (and August Deficit in Revision) Suggests Some Upside Pressure on GDP Revision. The headline September trade deficit narrowed, along with a revised August number that indicated less monthly trade deterioration than had been reported initially. While the impact of these numbers should be a positive contribution to the next GDP revision, that impact could be fleeting. To the extent that the narrower deficit was due to disrupted flows of trade data from the impact of Hurricane Sandy on the daily operations of the data-reporting and compiling government agencies in New York and Washington, D.C., the numbers will be revised in the next reporting cycle.

Nominal (Not-Adjusted-for-Inflation) Trade Deficit. The Bureau of Economic Analysis (BEA) and the Census Bureau reported this morning (November 8th) that the nominal, seasonally-adjusted monthly trade deficit in goods and services for September 2012, on a balance of payments basis, narrowed to \$41.5 billion from a revised \$43.8 (previously \$44.2) billion in August 2012. The September 2012 deficit narrowed from a \$44.5 billion deficit in September 2011.

Although the actual trade activity in September was not affected by Hurricane Sandy—the storm did not make landfall in New Jersey until October 29th—disruptions from the storm may have delayed some reporting of September trade activity (particularly imports), with the likely effect of narrowing the reported deficit. Any such reporting distortions in September activity would be revised with in next month's reporting, and a clarifying comment on the reporting impact of Hurricane Sandy may be released shortly by the Census Bureau.

As noted in [Commentary No. 479](#), however, actual physical disruption to trade activity in October and November would have followed from factors such as the shutdown of the Port of New York. Those effects likely will be seen in a short-lived narrowing of the trade deficits during those months.

Against the revised August detail, the seasonally-adjusted September 2012 trade balance reflected an increase in both exports and imports, with export growth outpacing in increase in imports. Again, that pattern may have been exaggerated by the reporting issues.

Crude Oil and Energy-Related Petroleum Products. For the month of September 2012, the not-seasonally-adjusted average price of imported oil rose to \$98.88 per barrel, from \$94.36 in August, but it was down from an average \$101.00 in September 2011.

In terms of not-seasonally-adjusted physical oil imports, September 2012 volume averaged 8.222 million barrels per day, versus 8.835 in August, and it was down from 9.423 million barrels per day in September 2011.

Other Cautions on Data Quality. Beyond possible short-lived disruptions from weather impact, the standard caution here for the monthly detail is that heavy distortions likely also continue in the seasonal adjustments, much as has been seen in other economic releases, such as retail sales and payrolls, where the headline number reflects month-to-month change. As has been discussed frequently (see [Hyperinflation 2012](#) for example), the extraordinary length and depth of the current business downturn have disrupted regular seasonality patterns. Accordingly, the markets should not rely heavily on the accuracy of the monthly headline data.

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 September 2012 merchandise trade deficit (no services) came in at \$46.8 billion, versus a revised \$48.2 (previously \$48.4) billion in August. September 2012, however, showed slight deterioration versus the September 2011 estimate of \$46.6 billion.

With full third-quarter 2012 estimates in place, along with revisions to second-quarter 2012, the real third-quarter deficit now annualizes out at \$568.2 billion (previously \$572.6 billion, initially \$558.6 billion). With the annualized pace of the second-quarter 2012 trade deficit now revised to \$563.5 (previously \$562.4) billion, the latest data suggest that the trade numbers still should have a small negative impact, albeit less-negative than initially, on the net-export account in the GDP estimate. Accordingly, that less-negative third-quarter trade number is consistent with some upside-revision pressure to the first revision of the third-quarter 2012 GDP, on November 29th.

Week Ahead. Whether or not manipulation has taken place in recent labor and GDP reporting, there are significant reporting-quality problems with a number of widely followed series. Headline reporting issues are tied largely to systemic distortions of seasonal adjustments, distortions that have been induced by recent, unprecedented economic turmoil in the post-World War II era of modern economic reporting. These distortions have thrown into question the statistical-significance of many popular monthly headline data. In any event, where numbers are too far removed from common experience, they tend to be viewed by the public with extreme skepticism.

Still, recognition of an intensifying double-dip recession has taken a stronger hold, while recognition of a mounting inflation threat has been rekindled a bit by recent Fed monetary policies and rising headline inflation numbers. The political system would like to see the issues disappear; the media does its best to avoid publicizing unhappy economic news or, otherwise, it puts a happy spin on the numbers; and the financial markets 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 catch up fully with underlying reality, or underlying reality catches up with the markets, reporting generally should continue to show higher-than-expected inflation and resume indicating weaker-than-expected economic results in the months and year ahead.

Increasingly, previously unreported economic weakness should continue to show up in prior-period revisions.

Retail Sales (October 2012). Scheduled for release on Wednesday, November 14th, by the Census Bureau, the headline October 2012 retail sales number has a fair shot at an outright monthly contraction, disappointing already-weak market expectations. The monthly headline number would appear even weaker, after adjustment for headline October CPI inflation. Structural liquidity problems besetting the consumer continue to cap sustainable consumption growth at a level below the pace of official inflation.

Producer Price Index—PPI (October 2012). The October 2012 PPI is scheduled for release on Wednesday, November 14th, by the Bureau of Labor Statistics (BLS). The headline October PPI likely will be positive, but well below the 1.1% reported in September. Depending on the oil contract followed, oil prices were down month-to-month in October by one-to-five percent, on average. That drop in energy prices should be offset largely, if not fully, by supportive seasonal adjustments in the month. Higher food prices in combination with still relatively strong “core” inflation should help to generate a net gain in month-to-month October wholesale inflation.

Consumer Price Index—CPI (October 2012). The release by the Bureau of Labor Statistics (BLS) of the October 2012 CPI numbers is scheduled for Thursday, November 15th. Headline CPI inflation rate is due for a more subdued rise, on both a monthly and annual basis, than was seen in September 2012 (headline monthly gain then of 0.6%), reflecting positive seasonal adjustments to otherwise declining gasoline prices and rising food and “core” inflation. Headline inflation reporting likely will top a minimal gain expected by the markets.

Unadjusted monthly average gasoline prices declined by 2.5% in October 2012 (Department of Energy). October seasonal-adjustment factors, however, tend to boost energy-price inflation, where an unadjusted 4.3% monthly decline in October 2011 gasoline prices became a 3.1% decline after seasonal adjustments.

Year-to-year total CPI-U inflation would increase or decrease in October 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the virtually unchanged (a 0.03% contraction) reading in the adjusted monthly level reported for October 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for October 2012, the difference in October’s headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from the September 2012 annual inflation rate of 1.99%. For example, if the headline October CPI-U gained 0.2% for the month, annual inflation would be about 2.2%

Industrial Production (October 2012). Due for release on Friday, November 16th, by the Federal Reserve, the headline October 2012 industrial production number is likely to show an outright decline, reflecting increasing efforts at reducing undesired business inventories. The headline growth most likely will be weaker than minimal plus-side market expectations. These numbers, however, remain subject to massive and irregular revisions that can distort the latest month’s reporting.