

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

COMMENTARY NUMBER 651

July 2014 CPI, Housing Starts, Real Retail Sales and Earnings, Monetary Base

August 19, 2014

**Real Retail Sales Contracted for Second Month,
Signaled Deepening Recession**

Real Earnings and Retail Sales Both Fell Below Second-Quarter Levels

July Annual Inflation: 2.0% (CPI-U), 1.9%% (CPI-W), 9.7% (ShadowStats)

Monetary Base Explodes to Record High

Quality of Housing-Starts Reporting Sinks to New Low

PLEASE NOTE: The next regular Commentary is scheduled for Tuesday, August 26th, covering July new orders for durable goods and new- and existing home sales, followed by a Commentary on August 28th, covering the second estimate of, and first revision to, second-quarter GDP.

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Downside Revisions for Second-Quarter GDP; July Data Hint at Third-Quarter GDP Contraction.

July economic reporting has been mixed, so far, but indicative of minor downside revisions pending to second-quarter 2014 GDP growth in its August 28th second estimation. July reporting also generated early suggestions of a potential quarterly contraction in third-quarter 2014 GDP.

Although the reporting of the June trade deficit detail, and the July industrial production and retail sales estimates all suggested some downside revisions to second-quarter activity, the larger downside revisions to second-quarter GDP growth likely will come from the areas that were so heavily guessed at in the “advance” estimate. Specifically, look for negative shifts in, and corrections to assumptions tied to inventory building, healthcare consumption and utility usage: areas discussed in [Commentary No. 646](#).

Keep in mind that the 4.0% annualized “advance” estimate of second-quarter 2014 real GDP growth was a guess by the Bureau of Economic Analysis (BEA). Always shy on early, hard numbers, the BEA used consensus forecasts as a contributing factor to that headline GDP guesstimate. Those consensus forecasts soon should prove to have been overly optimistic, with larger-than-consensus downside revisions pending to the first-revision next week, as well as to the second revision at the end of September.

Although headline July industrial production was relatively strong, dominated by surging automobile production, conflicts with auto sales and inventory reckonings should bring that series more in line with softening retail sales by quarter-end. A new development in production was a continuing reduction in consumer utility usage, reflecting a cooler than usual summer. That should act as a somewhat of damper on aggregate production, for a while. The plus-side for the economy there would be a resulting increase in the discretionary income available to the affected energy consumers.

As discussed in today’s (August 19th) *Commentary*, real retail sales—net of inflation—have turned down anew, again signaling recession. Headline real retail sales and real earnings for July both turned lower versus their second-quarter averages, generating the first solid numbers suggestive of continuing economic contraction in third-quarter 2014. That area will be reviewed in *Commentary No. 653*, in the context of the GDP revision on August 28th.

July housing starts were incredibly strong, but of such poor reporting quality as to be meaningless. Housing activity most likely continues in stagnation, with an unfolding downside. This, too, will be explored in the week ahead.

Today’s *Hyperinflation Watch* covers the ballooning monetary base and includes the regular gold-related graphs. The balance of this missive concentrates on the details of the July CPI and related real retail sales and earnings, housing starts, and consumer liquidity.

Consumer Price Index (CPI)—July 2014—Minimal Inflation Headline Still Topped Moribund Nominal Business Activity. The minimal headline 0.1% consumer inflation reported for July was as expected by the markets, but it also was enough to start pushing retail sales and average weekly earnings into real quarterly contractions—net of inflation—against second-quarter 2014 activity. Annual headline CPI-U inflation held at 2.0% in July, and it should begin pushing higher again in the months ahead, as the effects of oil and other commodity-related inflation continue to spread throughout the broad economy.

CPI-U. The headline, seasonally-adjusted CPI-U for July 2014 rose month-to-month by 0.1% (0.09% at the second decimal point), where the June CPI-U had increased by 0.3% (0.26% at the second decimal point). On a not-seasonally-adjusted basis, the July CPI-U declined by 0.04% (-0.04%), while the June CPI-U rose by 0.19%. Not seasonally adjusted, July 2014 year-to-year CPI-U inflation was 1.99%, versus 2.07% in June.

For the third time this calendar year, seasonal adjustments provided a boost to the headline inflation number. Encompassed by the headline July 2014 CPI-U seasonally-adjusted gain of 0.09% [down by 0.04% (-0.04%) unadjusted], aggregate July energy inflation was down for the month by an adjusted 0.34% (-0.34%) [down by an unadjusted 0.75% (-0.75%)]. In the other major CPI sectors, adjusted food inflation was up by 0.33% for the month (up by 0.27% unadjusted), while “core” inflation rose by an adjusted 0.10% [down by 0.01% (-0.01%) unadjusted]. Core inflation also showed unadjusted year-to-year inflation of 1.86% in July 2014, versus 1.93% in June.

CPI-W. The July 2014 seasonally-adjusted, headline CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.08% in July [down by 0.08% (-0.08%) unadjusted], versus an adjusted monthly gain of 0.30% (up by 0.21% unadjusted) in June. Unadjusted, July 2014 year-to-year CPI-W inflation was 1.93%, versus 2.04% in June.

Chained-CPI-U. Initial reporting of unadjusted year-to-year inflation for the July 2014 C-CPI-U was 1.87%, versus 1.95% in June.

Alternate Consumer Inflation Measures. The ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual inflation was roughly 5.6% in July 2014, versus 5.7% in June. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, eased to about 9.7%, versus 9.8% in June.

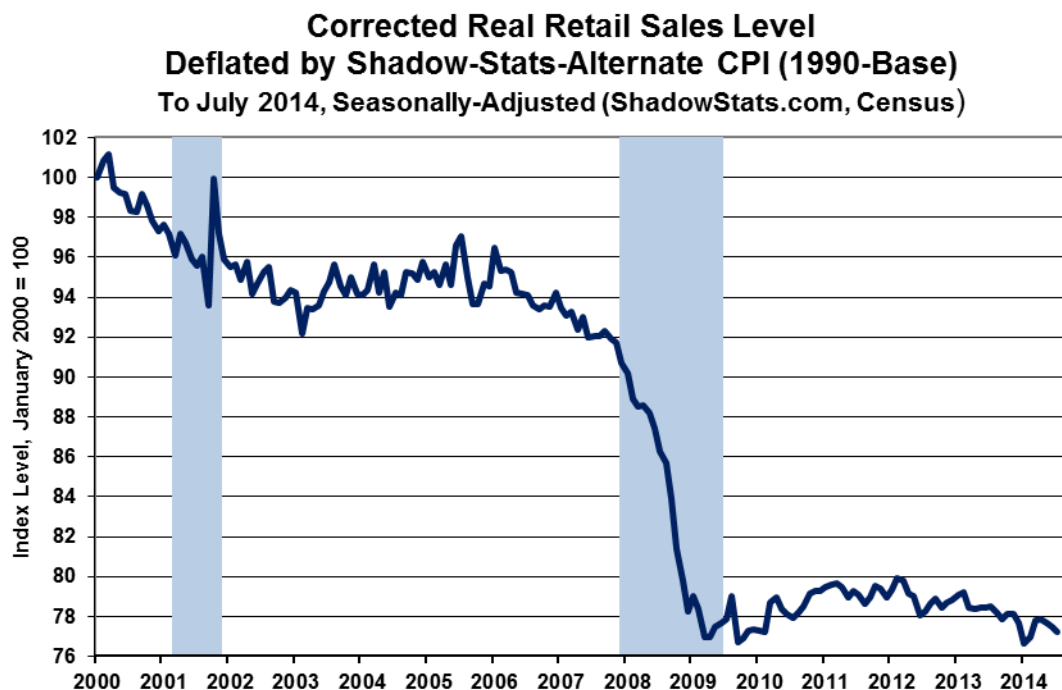
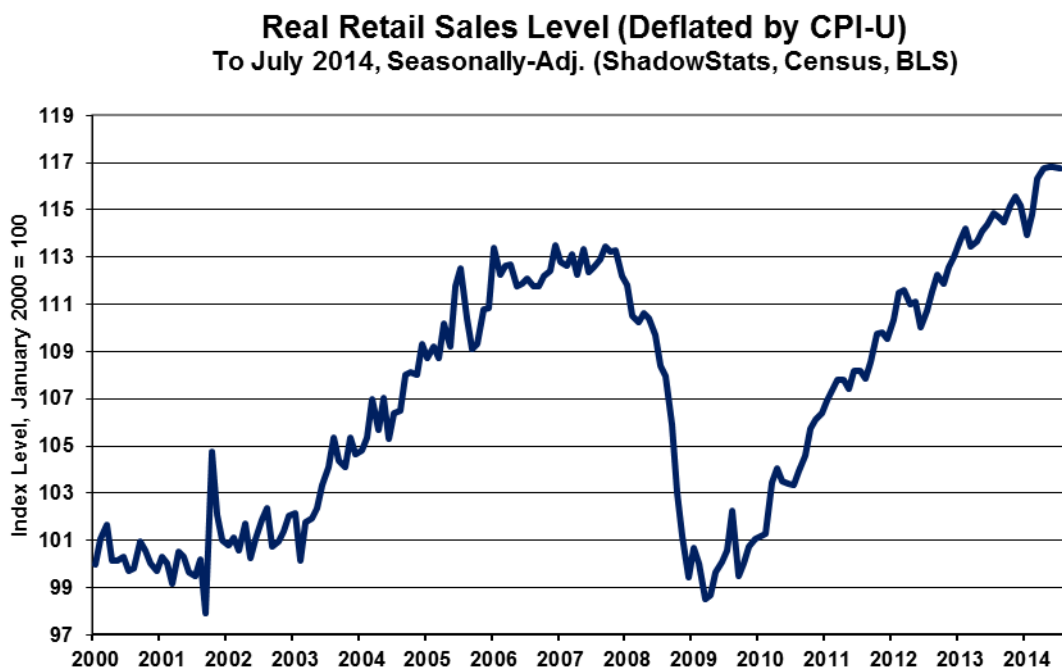
Real (Inflation-Adjusted) Retail Sales—July 2014—Fell Below Second-Quarter Activity. In nominal terms, before adjustment for inflation, headline monthly retail sales rose by 0.04% (unchanged at the one-decimal point headline level) in July, versus a revised 0.24% gain in June (see [Commentary No. 649](#)). Based on today’s reporting of a 0.09% headline monthly gain in the July 2014 CPI-U, and June CPI-U reporting of headline 0.26% monthly inflation, seasonally-adjusted real (inflation-adjusted) monthly retail sales notched lower by 0.05% (-0.05%) in July, following a revised 0.02% decline (-0.02%) in June.

For second-quarter 2014, the annualized pace of quarterly growth in real retail sales revised minimally lower to 6.27%, versus an annualized contraction of 0.97% (-0.97%) in first-quarter 2014. If third-quarter 2014 held at July’s level, the annualized quarterly contraction versus the second-quarter would be 0.17% (-0.17%).

Year-to-year change in July 2014 real retail sales slowed markedly, to 1.65%, well below the traditional recession-signal threshold. That was against an unrevised annual gain of 2.14% in June, and a downwardly-revised 2.37% annual gain in May. In normal economic times, annual real growth falling below 2.0% would signal imminent recession. That signal had been given recently and was regenerated in the initial reporting for July 2014. In the current circumstance, the signal would serve as an indicator of renewed downturn in broad economic activity. The regular graphs of real retail sales activity, both as to level and in terms of year-to-year change, are included in the *Reporting Detail* section. A graph of an index of real retail sales activity and the latest “corrected” real retail sales graph, follow here.

The first of the next two graphs reflects real retail sales as usually reported by the St. Louis Fed, deflated by the CPI-U, but it is indexed to January 2000 = 100. ShadowStats did the deflation using the July 2014 CPI-U and nominal retail sales releases. As seen in that graph, official real retail sales recently recovered its pre-recession high, declined into 2014, hit a new post-recession high in May, and then flattened and has turned down anew, as of July. The headline recovery, though, is a statistical illusion. Where CPI-U

understates inflation (see the [Public Comment on Inflation](#)), its use in calculating real retail sales has the effect of overstating actual inflation-adjusted activity.



Corrected Real Retail Sales. The apparent “recovery” in the headline real retail sales series—stalled at the moment with a downside trend—is due to the understatement of the rate of inflation used in deflating the retail sales and the other series. As discussed more fully in *Chapter 9* of [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

Instead of being deflated by the CPI-U, the “corrected” real retail sales numbers—in the second of the two accompanying graphs—use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation. With the higher inflation of the ShadowStats measure, the revamped numbers show a pattern of plunge and stagnation and renewed downturn, consistent with patterns seen in real median household income, consumer confidence measures, unemployment and most housing statistics. A topping out in late-2011 and early-2012 reverted to renewed decline in second-quarter 2012 in this series, which had been bottom-bouncing along a low-level plateau of economic activity since the economic collapse from 2006 into 2009. The renewed contraction has deepened, so far, into 2014.

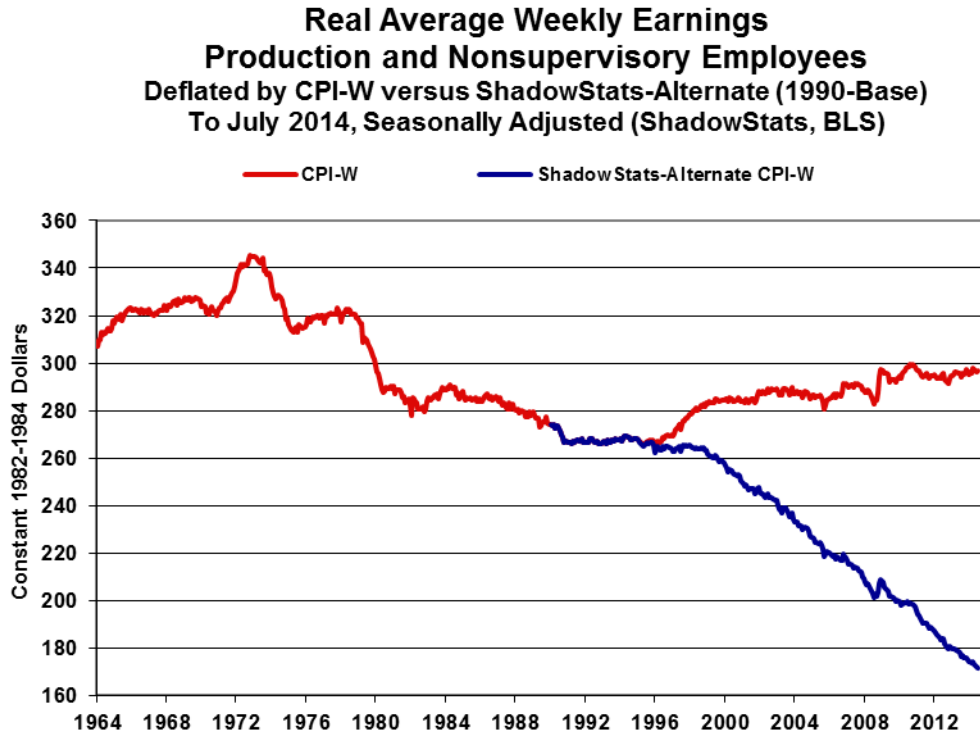
Real (Inflation-Adjusted) Average Weekly Earnings—July 2014—Below Second-Quarter 2014

Average. In the production and nonsupervisory employees series—the only series for which there is a meaningful history—headline real average weekly earnings (deflated by the CPI-W) rose by 0.12% in July, having fallen by a revised 0.16% (-0.16%) in June, and by unrevised declines of 0.14% (-0.14%) in May, and 0.19% (-0.19%) in April.

Net of prior-period revisions, the monthly gain in July was 0.07%, with the level of July earnings holding below the level of May. July’s real earnings also were below the average level for second-quarter 2014.

Year-to-year and seasonally-adjusted, July 2014 real average weekly earnings rose by 0.95% in July, versus a revised 0.28% gain in June, and unrevised gains of 0.28% in May, and 0.32% in April. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility. Prior-period revisions usually are due to the instabilities in the BLS monthly surveys.

Plotted in the regular accompanying graph of this series are the earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-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. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been flat for the last decade. Deflated by the ShadowStats measure, 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 the CPI-W. See [Public Commentary on Inflation Measurement](#) for further detail.



Housing Starts—July 2014—Extreme Volatility in Reporting and Revisions Generates Worthless Headline Data. Following last month’s extreme downside volatility in reporting and revisions, headline July 2014 reporting showed extreme instability on the upside. With horrendously-distorted reporting and seasonal-adjustment issues carrying over from last year’s shutdown of the federal government, the Census Bureau appears to be unable to publish consistent housing starts data on a regular monthly basis. The problem is ongoing, and it has reached a level where the initial headline reporting is virtually worthless. Nonetheless, the headline numbers are graphed and reported here, per official reporting.

As still can be seen in the aggregate graphs, and as should be confirmed generally in subsequent reporting, housing starts activity broadly has continued to stagnate, with the personal housing sector constrained by consumer liquidity issues.

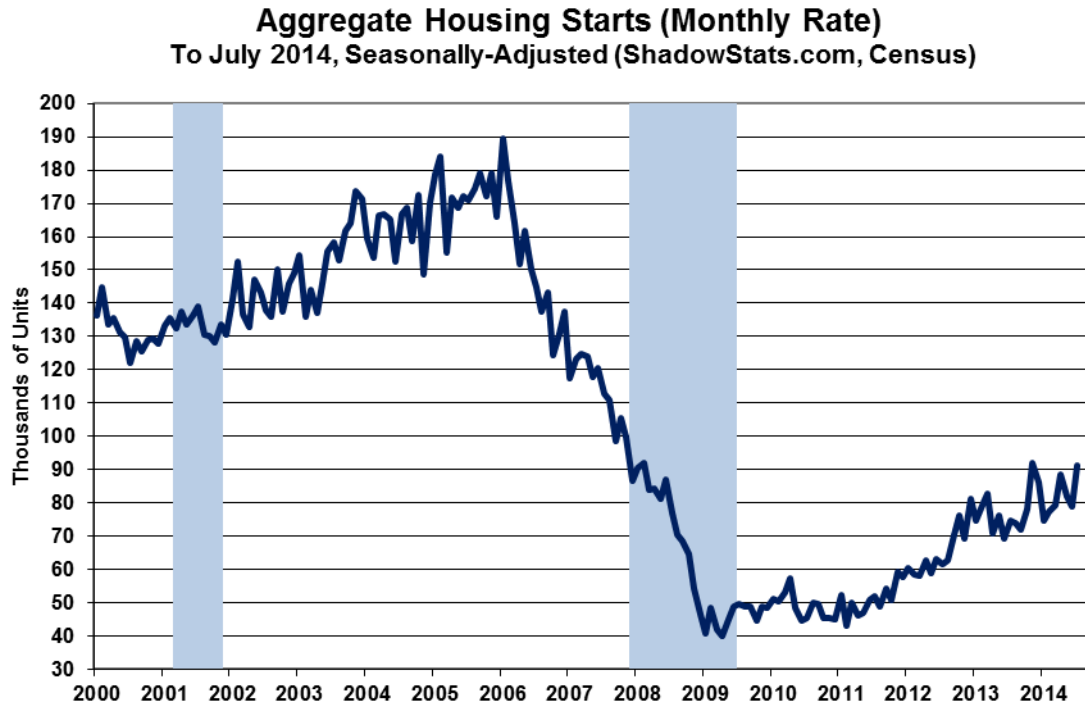
Structurally-Impaired Consumer Liquidity Restrains Housing Market Activity. As touched upon at the end of these *Opening Comments*, the last six-plus years of economic collapse and stagnation have been dominated by consumer activity that has been constrained heavily by intense, structural-liquidity problems. Without real, or inflation-adjusted, growth in income, and without the ability or willingness to take on meaningful new debt, the consumer simply does not have the wherewithal to fuel real growth in private housing or retail sales. The underlying economic fundamentals do not support a sustainable turnaround in the housing industry or in general economic activity.

July 2014 Housing-Starts Reporting. The statistically-significant, seasonally-adjusted headline monthly gain in July 2014 housing starts was 15.7%. That monthly gain was on top of a 5.5% upside revision to the previously-reported level of June activity. The July surge was dominated by a monthly 33.8% jump in

the “five units or more” category and an 8.3% gain in the “one unit” category, but those gains were not separately statistically-significant.

June 2014 housing starts fell by a revised 4.0% (-4.0%) for the month. Net of prior-period revisions, July housing starts jumped by an incredible (as in not believable) 22.4%.

Year-to-year change in the seasonally-adjusted, aggregate July 2014 housing-starts measure was a statistically-significant gain of 21.7%, versus a revised 13.7% annual gain in June 2014.



By-Unit Category. Where the irregular housing starts series can show varying patterns, that partially is due to a reporting mix of residential construction products, with the largest physical-count category of one-unit housing starts—generally for individual consumption—resulting in new home sales, versus multi-unit starts that generally reflect the building of rental and apartment units.

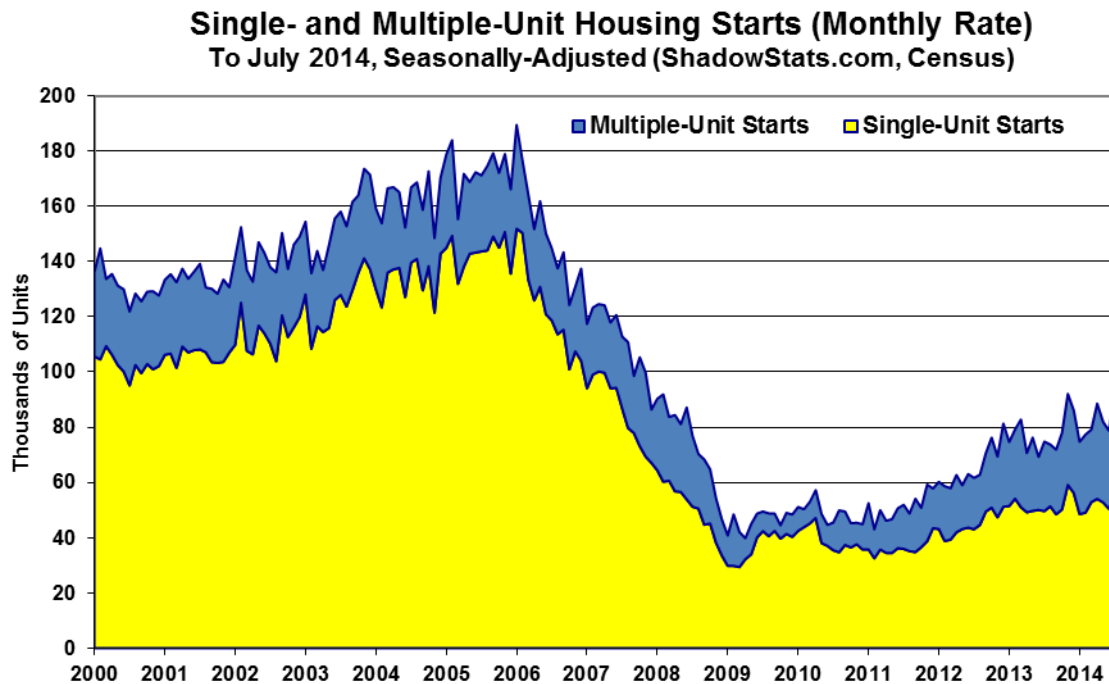
Housing starts for single-unit structures in July rose month-to-month by a statistically-insignificant 8.3%, following a revised headline monthly contraction of 4.4% (-4.4%) in June. July’s year-to-year gain of 10.1% followed a revised year-to-year gain of 0.8% in June.

Reporting of housing starts for apartment buildings (generally 5-units-or-more) in July 2014 jumped by a statistically-insignificant 33.0%, to a level not seen since January 2006. That followed a revised monthly decline of 6.7% (-6.7%) in June. July’s year-to-year gain of 49.5% was statistically-significant, and was against a revised year-to-year gain in June 2014 of 45.2%.

Expanding the multi-unit housing starts category to include 2-to-4-units plus 5-units-or-more usually reflects the bulk of rental- and apartment-unit activity. The Census Bureau does not publish estimates of

the 2-to-4-units category, due to statistical significance problems (a general issue for the aggregate series). Nonetheless, the total multi-unit category can be calculated by subtracting the single-unit category from the total category.

Accordingly, the statistically-significant aggregate July monthly gain of 15.7% was composed of a statistically-insignificant increase of 8.3% in one-unit housing starts, combined with a statistically-insignificant monthly gain of 28.9% in multiple-unit structures (2-units-or-more, including the 5-units-or-more category). These series are shown in the accompanying housing-starts graphs.



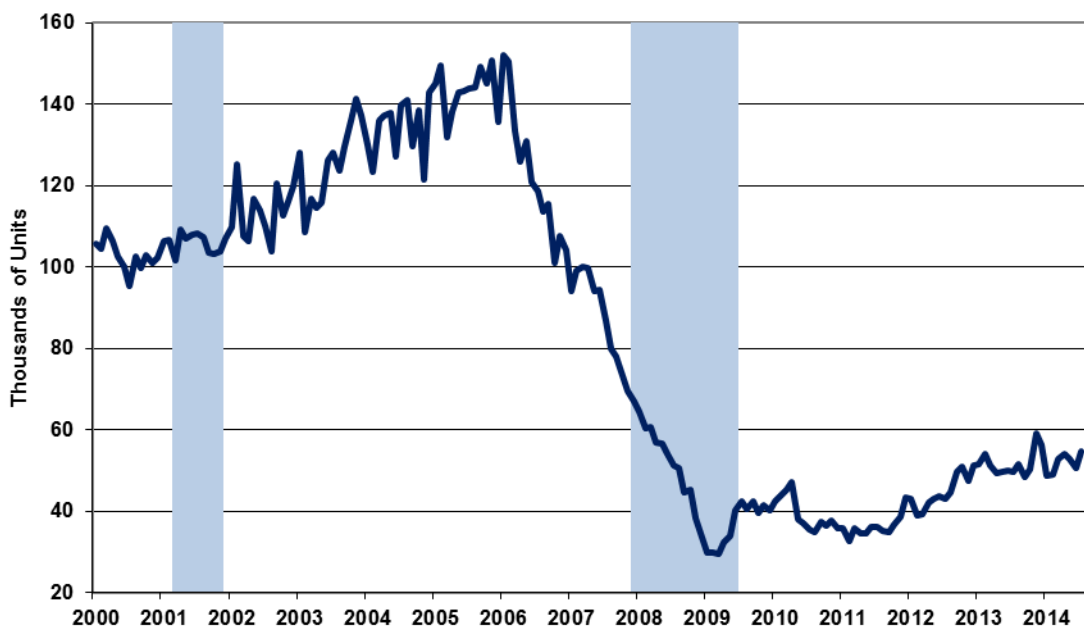
Graphs of Housing Starts Activity. Headline reporting of housing starts is expressed by the Census Bureau as an annualized monthly pace of starts, which was 1,093,000 in July 2014, versus a revised 945,000 (previously 893,000) in June 2014. Those annualized details are used in the graphs of aggregate housing-starts activity in the *Reporting Detail* section.

Given the nonsensical volatility in general reporting, exaggerated by annualizing the monthly numbers in this unstable series—such as was seen with the headline July 2014 reporting—the magnitude of monthly activity, and the changes in same, more realistically is reflected at the non-annualized monthly rate, and that flat monthly rate is the basis for the scales of the graphs in this section.

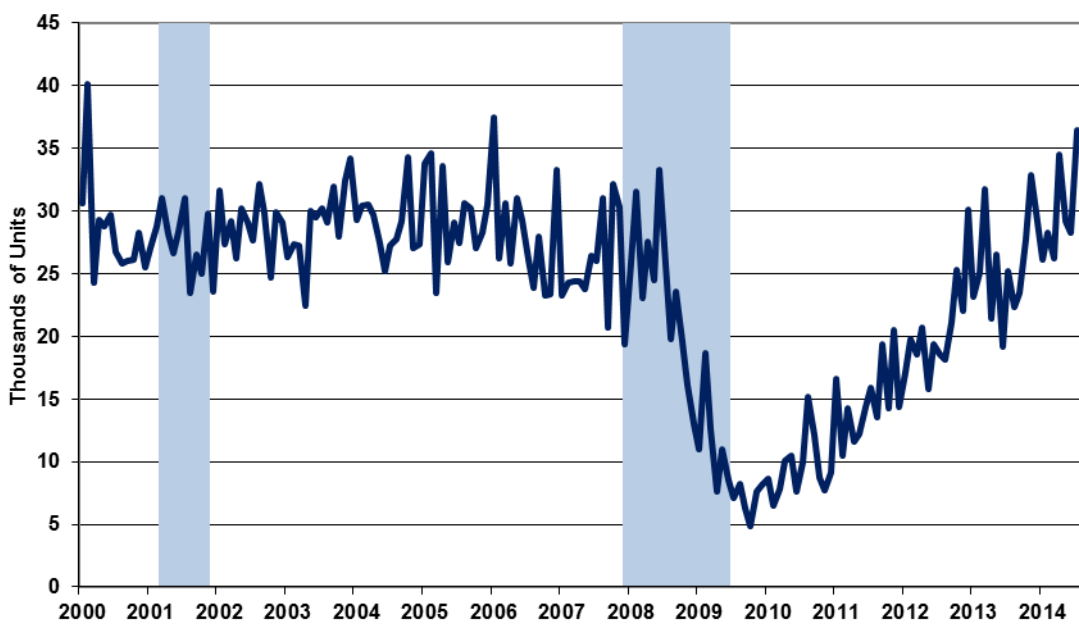
Consider the flat monthly rate of 91,083 in July 2014, instead of the headline level of the 1,093,000 annualized July rate. Based on the annualized numbers, housing starts increased by 148,000 units in July 2014, instead of the flat rate of 12,333 for the month. Yet such an annualized increase of 148,000, by itself, would be more than any single seasonally-adjusted month's total in non-annualized housing starts since June 2006.

Using either scale, however, the appearance of the graph and the relative monthly, quarterly and annual percentage changes are the same.

Single-Unit Housing Starts (Monthly Rate)
To July 2014, Seasonally-Adjusted (ShadowStats.com, Census)



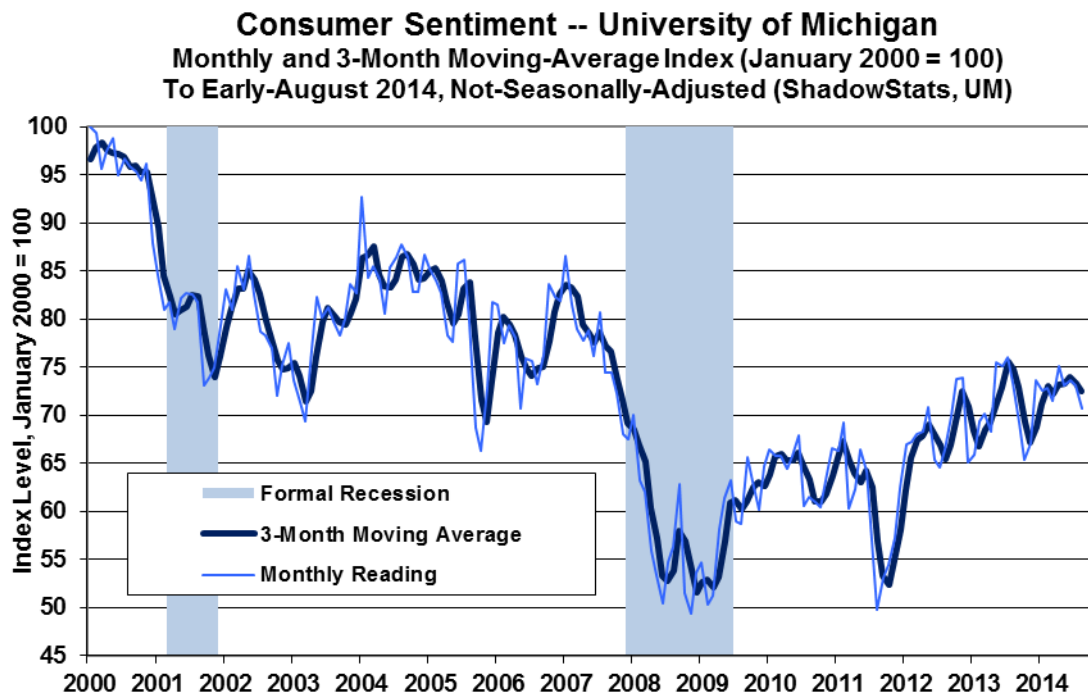
Multiple-Unit Housing Starts (Monthly Rate)
To July 2014, Seasonally-Adjusted (ShadowStats.com, Census)



The record monthly low seen for the present aggregate housing starts series was in April 2009, where the annualized monthly pace of starts was down 79% (-79%) from the January 2006 pre-recession peak. Against the downside-spiked low in April 2009, the July 2014 headline number was up by 98%, but it still was down by 58% (-58%) from the January 2006 series high.

Liquidity Constraints on the Consumer Are Not Easing Up. As discussed in [Commentary No. 649](#), and as noted in the earlier section on July 2014 real earnings (see also the *Reporting Detail* section), ongoing structural and fundamental consumer liquidity problems impair and severely constrain real, or inflation-adjusted, expansion of retail sales, personal consumption and housing activity. Without real growth in income, and without the ability and/or willingness to offset declining purchasing power with debt expansion, the consumer lacks the ability to fuel traditional, consumption-based growth or recovery in U.S. economic activity. The consumer directly drives 72% of estimated GDP activity. There has not been a post-2007 economic recovery, and there is no recovery underway, just general bottom-bouncing that broadly has turned down anew.

The accompanying, updated graph of the University of Michigan's consumer sentiment survey reflects the monthly downturn reported for the advance August 2014 estimate. The current level of consumer sentiment remains deep in traditional-recession territory. The other liquidity measures remain as published in *No. 649*.

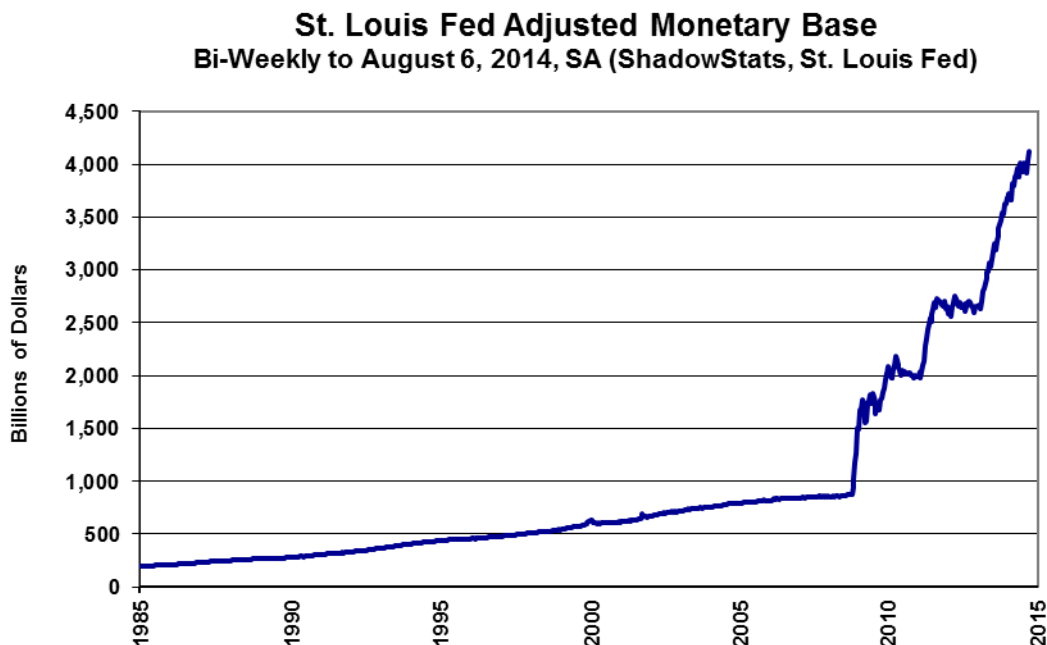


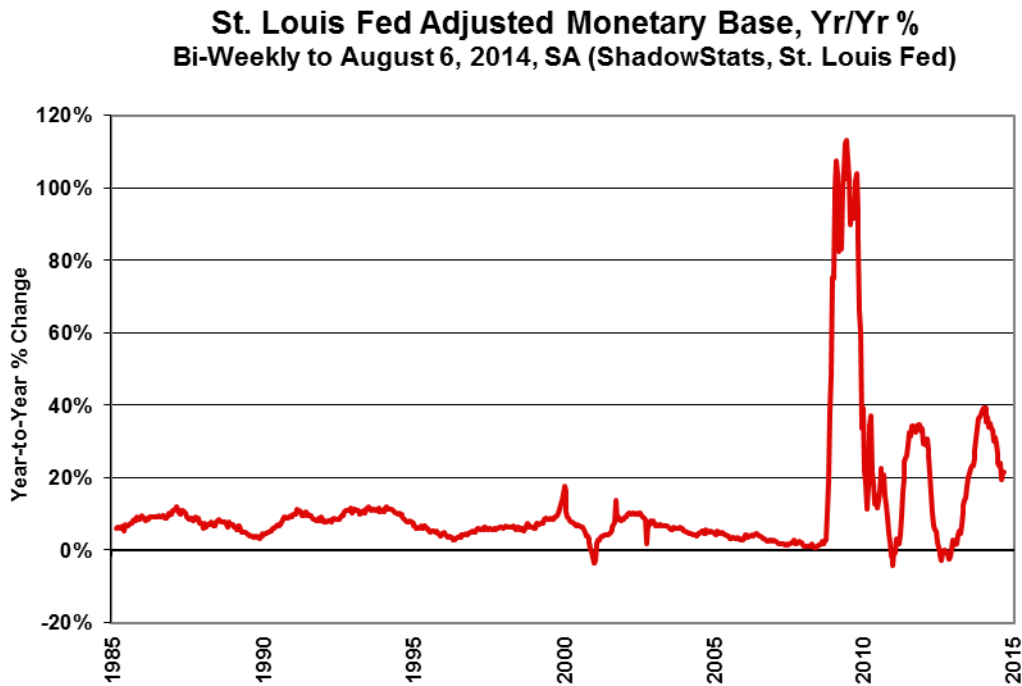
[For further details on July CPI, real retail sales and earnings, and housing starts, see the Reporting Detail section. For drill-down and graphing options for the headline CPI and residential construction data, see ShadowStats affiliate www.ExpliStats.com.]

HYPERINFLATION WATCH

Monetary Base Moves to New High. Reflected in the following graphs, despite the “tapering” in debt purchases by the Federal Reserve, the seasonally-adjusted monetary base (St. Louis Fed measure) moved to an all-time high of \$4.121 trillion, in the two weeks ended August 6, 2014, up at an annualized pace of 66.5% from the previous record level of \$4.041 trillion in the prior two-week period. Year-to-year growth had started to slow recently, with what had been flat-to-minus levels of current activity measured against a year-ago period of rapid growth. Annual growth held at 21.4% in the latest reading, little changed from the elevated 21.5% of the prior period, which had broken that recent downtrend in the annual growth rate.

Intensifying Banking-System Woes? Given a “strong” economy and ongoing Fed tapering, the renewed surge in the magnitude of the monetary base—with only a negligible pick up in broad money supply (M3) growth—suggests an intensifying problem with banking-system health and solvency. More will follow here in the weeks ahead. The ongoing systemic liquidity crisis should intensify in an environment of falling economic activity (see *Opening Comments*).





Fed Has Monetized 71.4% of Net Treasury Debt Issuance for the Public, Calendar-Year-to-Date. In the context of reduced purchases of U.S. Treasuries and sharply-increasing net issuance of Treasury securities in the last two weeks, the effective monetization of Treasury debt continues, but at a slower pace than seen at the end of July.

The Fed's net acquisition of U.S. Treasury securities so far in calendar-year 2014 (through August 13th), versus net debt issuance of the U.S. Treasury for the public in the same period, has reflected effective monetization of 71.4% of the increase in debt (previously at 91.2% as of July 30th, partially reflecting what had been some slowing of debt issuance). That still is a higher portion than the effective monetization pace of 69.7% in the full calendar-year 2013.

In aggregate, since the onset of expanded quantitative easing QE3 in January 2013 to date, the Fed has monetized 70.2% of the increased Treasury debt held by the public. Against the net increase in total gross federal debt, the Fed effectively has monetized 69.4% of the net debt increase in 2014, 59.0% of the total in 2013, and 61.7% of the aggregate net debt issuance since the onset of expanded QE3.

The ongoing monetization of the Treasury debt likely has been a contributing factor to the recent pickup, albeit still minimal, seen in broad money supply (M3) growth. It also continues to confirm that the market in U.S. Treasury securities remains anything but free and open, with artificially-depressed yields and artificially-inflated bond prices.

Hyperinflation Outlook Summary. *[UNREVISED from Commentary No. 649, except for updated monetization details as discussed in preceding section.]* The long-standing hyperinflation and economic

outlooks were updated with the publication of [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), on April 2nd, and publication of [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), on April 8th, along with ongoing updates in the regular *Commentaries*, including a review in [Commentary No. 639](#).

Primary Summary. The primary and basic summary of the broad outlook and the story of how and why this crisis has unfolded and developed over the years—particularly in the last decade—is found in the *Opening Comments* and *Overview and Executive Summary* of that *First Installment Revised* (linked above). The following section summarizes the underlying current circumstance.

Consistent with the above *Special Commentaries*, the unfolding economic circumstance, in confluence with other fundamental issues, should place mounting and massive selling pressure on the U.S. dollar, as well as potentially resurrect elements of the 2008-Panic. Physical gold and silver, and holding assets outside the U.S. dollar, remain the primary hedges against the pending total loss of U.S. dollar purchasing power.

Current Economic Issues versus Underlying U.S. Dollar Fundamentals. U.S. economic activity has turned down anew, with headline first-quarter 2014 GDP having contracted at an annualized real pace of 2.11% (-2.11%), following 3.50% fourth-quarter 2013 growth, per the July 30th GDP benchmark revisions. Although the initial headline second-quarter 2014 GDP growth came in at 3.95%, such was overstated heavily and subject to major downside revisions. By the time the now-unfolding headline third-quarter 2014 GDP growth is reported in contraction, the second-quarter GDP growth estimate should have revised to close to flat, if not worse. Consensus expectations still face downside shocks in the months ahead, moving the popular outlook towards a “new recession,” with the shifts in the consensus likely to disrupt stability in the financial markets.

As financial-market expectations increasingly shift towards renewed or deepening recession, that circumstance, in confluence with other fundamental issues, should place mounting and massive selling pressures on the U.S. dollar, as well as potentially resurrect elements of the 2008-Panic.

Unexpected economic weakness intensifies the known stresses on an already-impaired banking system, hence a perceived need for expanded, not reduced, quantitative easing. The highly touted “tapering” by the FOMC is pre-conditioned by a continued flow of “happy” economic news. Banking-system and other systemic (*i.e.* U.S. Treasury) liquidity needs likely still will be provided, as needed, by the Fed, under the ongoing political covering of a weakening economy—a renewed, deepening contraction in business activity.

Unexpected economic weakness also savages projections of headline, cash-based, federal-budget deficits (particularly the 10-year versions) as well as projected funding needs for the U.S. Treasury. Current fiscal “good news” is from cash-based, not GAAP-based accounting projections, and comparative year-ago cash numbers are distorted against U.S. Treasury and government activity operating *sub rosa*, in order to avoid the limits of a constraining debt ceiling.

All these crises will combine against the U.S. dollar, likely in the very-near future.

In general, summary, the fundamental issues threatening the U.S. dollar could not be worse. They include, but are not limited to:

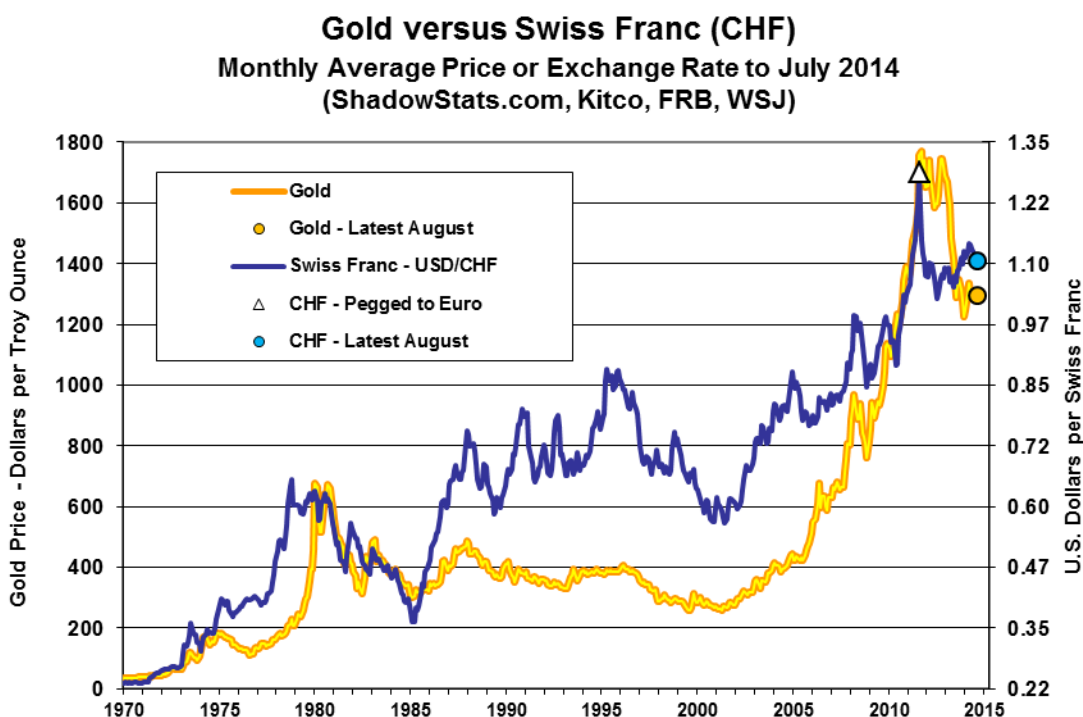
- A severely damaged U.S. economy, which never recovered post-2008 and is turning down anew. The circumstance includes a sharply widening trade deficit, as reflected in headline first- and second-quarter reporting, as well as ongoing severe, structural-liquidity constraints on the consumer, which are preventing a normal economic rebound in the traditional, personal-consumption-driven U.S. economy.
- U.S. government unwillingness to address its long-term solvency issues. Those controlling the U.S. government have demonstrated not only a lack of will to address long-term U.S. solvency issues, but also the current political impossibility of doing so. Any current fiscal “good news” comes from cash-based, not GAAP-based accounting projections. The GAAP-based version continues to run in the \$6-trillion-plus range for annual shortfall, while those in Washington continue to increase spending and to take on new, unfunded liabilities.
- Monetary malfeasance by the Federal Reserve, as seen in central bank efforts to provide liquidity to a troubled banking system, and also to the U.S. Treasury. The current pace of the Fed’s monetization is at 71.4% of effective net issuance of the federal debt to be held by the public in calendar-year 2014 (through August 13th). The pace of effective monetization has been 70.2% since the January 2013 expansion of QE3.
- Mounting domestic and global crises of confidence in a dysfunctional U.S. government, where the relative positive rating by the public of the U.S. President tends to have a meaningful correlation with the foreign-exchange-rate strength of the U.S. dollar. Positive ratings for both the President and Congress are pushing, if not at, historic lows.
- Mounting global political pressures contrary to U.S. interests. Downside pressures on the U.S. currency generally are increasing, in the context of global political and military developments that have been contrary to U.S. strategic, financial and economic interests.
- Spreading global efforts to dislodge the U.S. dollar from its primary reserve-currency status.

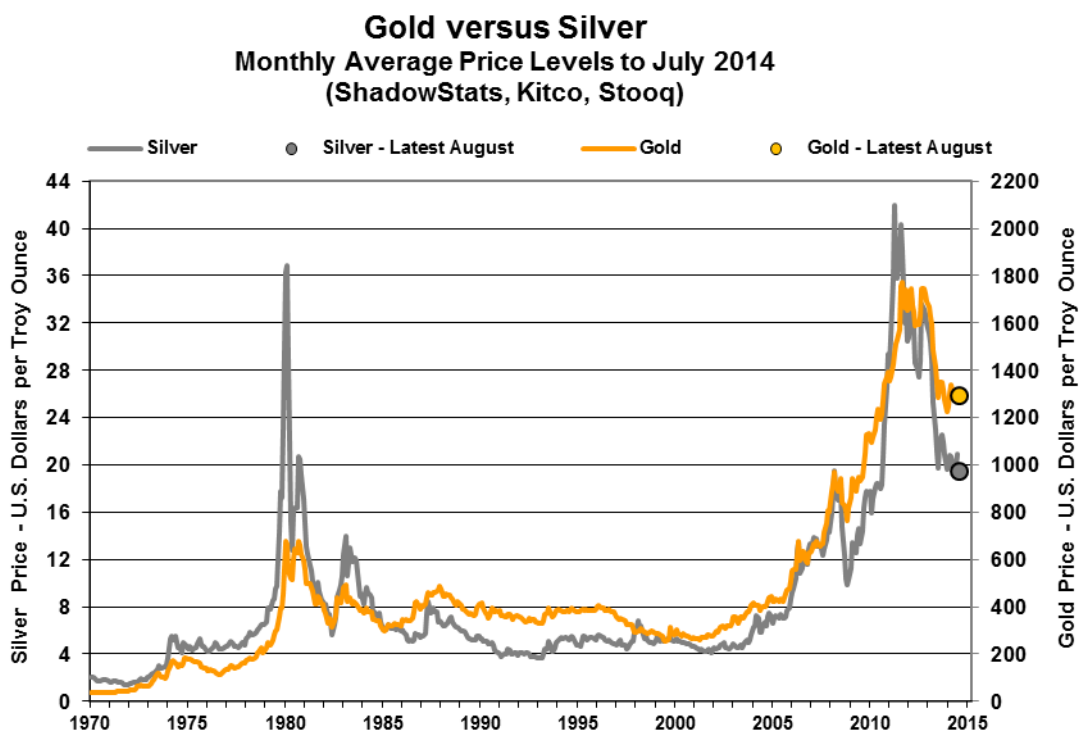
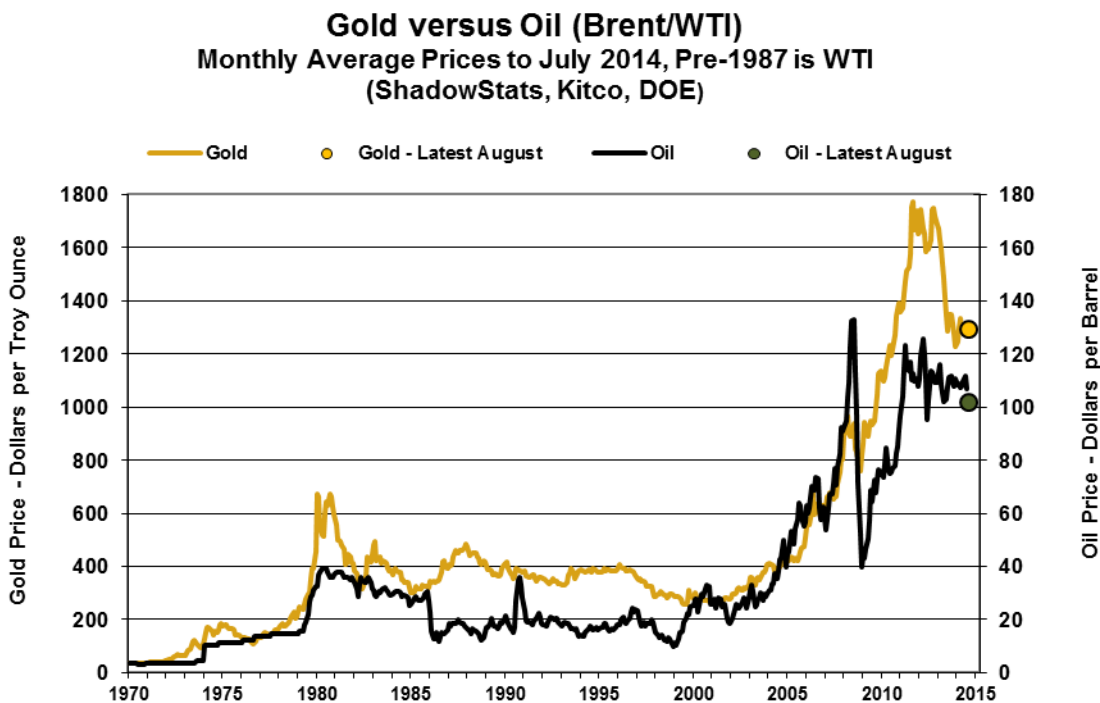
Renewed and intensifying weakness in the U.S. dollar will place upside pressure on oil prices and other commodities, boosting domestic inflation and inflation fears. Domestic willingness to hold U.S. dollars will tend to move in parallel with global willingness, or lack of willingness, to do the same. Both dollar weakness and the resulting higher inflation should boost the prices of gold and silver, where physical holding of those key precious metals remains the ultimate hedge against the pending inflation and financial crises.

Monthly Gold Graphs. Following are the graphs of gold prices versus the Swiss franc, oil prices and silver prices that usually accompany the *Commentary* on the monthly CPI release. Volatile markets continue, amidst mounting and shifting global political tensions, a rapidly weakening U.S. economy and nascent recognition of rising inflation. Related market fears also center on worsening fiscal and monetary instabilities, and rapidly deteriorating domestic political circumstances. All these issues have sharply negative implications for the U.S. dollar, which still remains a good bet to be an early casualty. Precious metals and oil prices would benefit from a weakened U.S. dollar.

As discussed in the two installments of the *2014 Hyperinflation Report*, linked above, the underlying fundamentals could not be much weaker for the U.S. dollar, and they could not be stronger for gold and silver, irrespective of unusual price volatility in the last year or two. Market movements increasingly should reflect those fundamentals. More-recent oil price volatility has reflected intensifying global political instabilities, but oil prices also will face significant, separate upside pressure when the U.S. dollar comes under heavy selling pressure.

The “latest August” points in the following graphs reflect approximate conditions as of late-afternoon New York time, August 19th.





REPORTING DETAIL

CONSUMER PRICE INDEX—CPI (July 2014)

Even Minimal Headline Consumer Inflation Is Topping Moribund Nominal Business Activity. The minimal headline 0.1% consumer inflation reported for July was as expected by the markets, but it also was enough to start pushing retail sales and average weekly earnings into real quarterly contractions—net of inflation—against real activity in second-quarter 2014. Annual headline CPI-U inflation was 2.0% in July. That reading should begin pushing higher in the months ahead, as the effects of oil and other commodity-related inflation continue to spread throughout the broad economy.

Going forward, and as discussed in [2014 Hyperinflation Report—The End Game Begins](#) – *First Installment Revised* and in the *Hyperinflation Watch* section, risks of a massive flight from the U.S. dollar threaten upside energy and global-commodity inflation, which would drive headline consumer inflation much higher. Nascent dollar problems could surface and accelerate at any time, with little warning. Renewed financial-market turmoil surrounding deteriorating global and domestic political, fiscal and monetary instabilities, and rapidly worsening economic activity, all should pummel the U.S. dollar. Ongoing economic and financial-system-liquidity crises still threaten systemic instabilities that, as with their 2008 Panic precursors, cannot be contained without further, official actions that have serious inflation consequences.

As a separate issue, inflation—generally perceived by the public from the standpoint of personal income or investment use—continues to run well above any of the government’s rigged price measures. Related methodological changes to the CPI series in recent decades were designed to understate the government’s reporting of consumer inflation, as discussed in the [Public Comment on Inflation Measurement](#).

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)** is an experimental measure, 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 considered by Congress and the White House as a tool for reducing Social Security cost-of-living adjustments by stealth.*

*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 this morning, August 19th, that the headline, seasonally-adjusted CPI-U for July 2014 rose month-to-month by 0.1% (0.09% at the second decimal point), where the June CPI-U had increased by 0.3% (0.26% at the second decimal point). On a not-seasonally-adjusted basis, the July CPI-U declined by 0.04% (-0.04%), while June CPI-U rose by 0.19%. For the third time this calendar year, seasonal adjustments provided a boost to the headline inflation number.

Monthly Gasoline Prices. The BLS used a 1.5% decline (-1.5%) in not-seasonally-adjusted gasoline prices for July, versus a 2.1% decline (-2.1%) indicated by the more-comprehensive, industry-based surveying of the Department of Energy. In line with last year’s numbers showing a seasonally-adjusted boost to gasoline prices, that 2.1% unadjusted drop (-2.1%) narrowed to a 0.3% decline (-0.3%) in gasoline prices, seasonally adjusted. Seasonal adjustments were positive across the board, for headline energy inflation, food inflation and “core” inflation, net of food and energy price increases.

Major CPI Groups. Encompassed by the headline July 2014 CPI-U seasonally-adjusted gain of 0.09% [down by 0.04% (-0.04%) unadjusted], aggregate July energy inflation was down for the month by an adjusted 0.34% (-0.34%) [down by an unadjusted 0.75% (-0.75%)]. In the other major CPI sectors, adjusted food inflation was up by 0.33% for the month (up by 0.27% unadjusted), while “core” inflation rose by an adjusted 0.10% [down by 0.01% (-0.01%) unadjusted]. Core inflation also showed unadjusted year-to-year inflation of 1.86% in July 2014, versus 1.93% in June.

Year-to-Year CPI-U. Not seasonally adjusted, July 2014 year-to-year inflation for the CPI-U was a gain of 1.99%, versus 2.07% in June.

Year-to-year, CPI-U inflation would increase or decrease in next month’s August 2014 reporting, dependent on the seasonally-adjusted monthly change, versus an adjusted 0.08% gain in the monthly inflation reported for August 2013. The adjusted change is used here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for August 2014, the

difference in August's headline monthly change (or forecast of same), versus the year-ago monthly change, should be added to or subtracted directly from the July 2014 annual inflation rate of 1.99%.

CPI-W. The July 2014 seasonally-adjusted, headline CPI-W, which is a narrower series and has greater weighting for gasoline than does the CPI-U, rose by 0.08% in July [down by 0.08% (-0.08%) unadjusted], versus an adjusted monthly gain of 0.30% (up by 0.21% unadjusted) in June.

Unadjusted, July 2014 year-to-year CPI-W inflation was 1.93%, versus 2.04% in June.

Chained-CPI-U. Initial reporting of unadjusted year-to-year inflation for the July 2014 C-CPI-U was 1.87%, versus 1.95% in June.

[The balance of the C-CPI-U discussion is unchanged from the prior Commentary covering the CPI.] The recent, two-year budget deficit agreement (see [Commentary No. 581](#)) cut cost-of-living adjustments (COLA) for certain military retirees by one-percent. The Congressional negotiators did not use the Chained-CPI as had been threatened otherwise for Social Security, etc., where the idea had been that the chained series would cut COLAs by about one-percent on an annual basis, versus existing calculations. The approach taken is more open about what is being done, as opposed to the prior subterfuge of trying to pass off a fully-substitution-based CPI as a legitimate COLA measure.

The Chained-CPI-U currently is not designed as a benchmark cost-of-living indicator, with the series subject to revisions for two years, before the inflation-rate reduction is realized fully. Despite White House and Congressional considerations of making the chained index the new cost-of-living-adjustment (COLA) measure for programs such as Social Security, the system cannot be made workable as a concept for using a substitution-based CPI measure as a COLA, without the new index becoming even more of a sham than it already is. For further detail, see the [Public Commentary on Inflation Measurement and Chained-CPI](#), and the C-CPI material posted on the BLS site, apparently in anticipation possible political uses for the measure: [Chained CPI](#).

Alternate Consumer Inflation Measures. Adjusted to pre-Clinton methodologies—the ShadowStats-Alternate Consumer Inflation Measure (1990-Base)—annual inflation was roughly 5.6% in July 2014, versus 5.7% in June. The ShadowStats-Alternate Consumer Inflation Measure (1980-Base), which reverses gimmicked changes to official CPI reporting methodologies back to 1980, eased to about 9.7% (9.73% for those using the second decimal point) in July, versus roughly 9.8% in June.

[The balance of the text in this Alternate Consumer Inflation Measures sub-section is unchanged from the prior CPI Commentary.]

Note: The ShadowStats-Alternate Consumer Inflation Measure largely has been reverse-engineered from the BLS's CPI-U-RS series, which provides an official estimate of historical inflation, assuming that all current methodologies were in place going back in time. The ShadowStats estimates effectively are adjusted on an additive basis for the cumulative impact on the annual inflation rate of various methodological changes made by the BLS (the series is not recalculated).

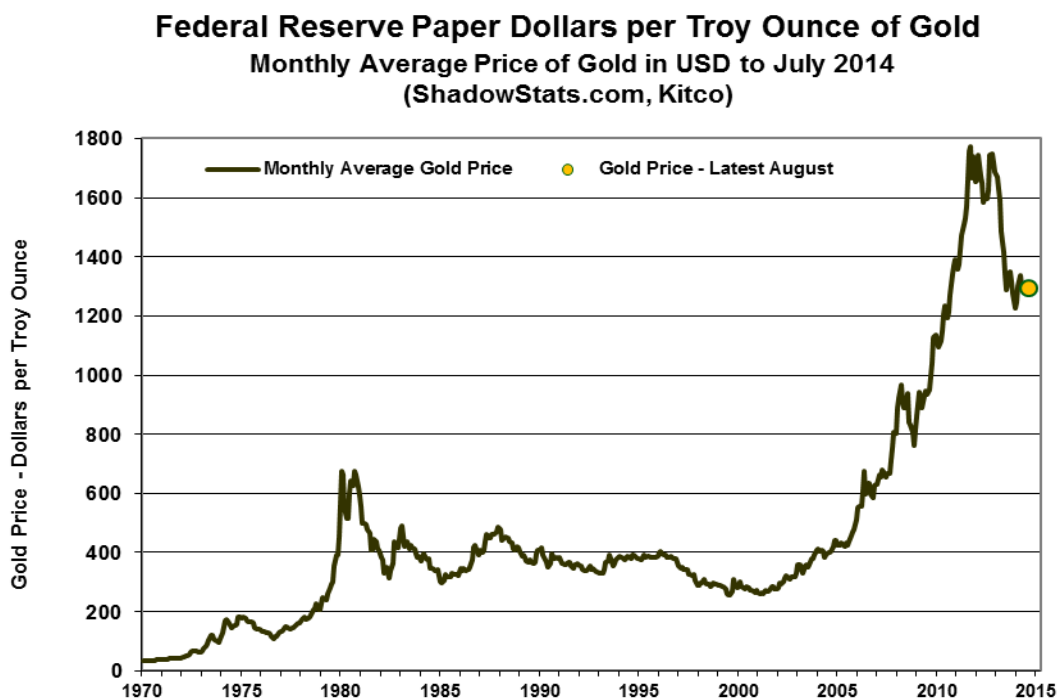
Over the decades, the BLS has altered the meaning of the CPI from being a measure of the cost of living needed to maintain a constant standard of living, to something that neither reflects the constant-standard-of-living concept nor measures adequately what most consumers view as out-of-pocket expenditures.

Roughly five percentage points of the additive ShadowStats adjustment 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. (See [Public Commentary on Inflation Measurement and Chained-CPI](#) for further details.)

Gold and Silver Highs Adjusted for CPI-U/ShadowStats Inflation. 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 \$2,603 per troy ounce, based on July 2014 CPI-U-adjusted dollars, and \$11,270 per troy ounce, based on July 2014 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (all series 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 July 2014 CPI-U inflation, the 1980 silver-price peak would be \$151 per troy ounce and would be \$656 per troy ounce in terms of July 2014 ShadowStats-Alternate-CPI (1980-Base) adjusted dollars (again, all series not seasonally adjusted).

As shown in Table 1, on page 31 of [2014 Hyperinflation Report—The End Game Begins – First Installment Revised](#), 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, while they 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 (Inflation-Adjusted) Retail Sales—July 2014—Below Second-Quarter Activity. In nominal terms, before adjustment for inflation, headline monthly retail sales rose by 0.04% (unchanged at the one-decimal point headline level) in July, versus a revised 0.24% (previously 0.25%) gain in June (see [Commentary No. 649](#)). Based on today's reporting of a 0.09% headline monthly gain in the July 2014 CPI-U, and in the context of the prior June CPI-U reporting of a headline 0.26% gain, seasonally-adjusted real (inflation-adjusted) monthly retail sales notched lower by 0.05% (-0.05%) in July, following a revised decline of 0.02% (-0.02%) in June, which previously had seen a decline of 0.01% (-0.01%).

For second-quarter 2014, the annualized pace of quarterly growth in real retail sales revised minimally lower to 6.27% (previously 6.42%), versus an annualized contraction of 0.97% (-0.97%) in first-quarter 2014. If the third-quarter 2014 held at July's level, the annualized quarterly contraction would be 0.17% (-0.17%).

Year-to-year change in July 2014 real retail sales slowed markedly, to 1.65%, well below the traditional recession-signal threshold. That was against an unrevised annual gain of 2.14% in June, and a downwardly-revised 2.37% (previously a 2.42%, initially a 2.07%) annual gain in May, as shown in the second and fourth graphs following. In normal economic times, annual real growth falling below 2.0% would signal an imminent recession. That signal had been given recently and was regenerated anew in initial reporting for July 2014. In the current circumstance, the signal likely will serve as an indicator of the renewed downturn in broad economic activity.

Real Retail Sales Graphs. The first of the following four accompanying graphs shows the level of real retail sales activity (deflated by the CPI-U) since 2000; the second graph shows year-to-year percent change for the same period. The level of monthly activity turned down sharply in December 2013 and January 2014 with a bounce-back into May, but now flattening out and turning lower. Year-to-year activity, which had plunged to a near-standstill in January and February, also bounced back some in March and into the second-quarter, pulling back sharply in June and July. The third and fourth graphs show the level of and annual growth in real retail sales (and its predecessor series) in full post-World War II detail.

The apparent “recovery” in the real retail sales series and industrial production (as well as in the GDP) is due to the understatement of the rate of inflation used in deflating retail sales and other series. As discussed more fully in *Chapter 9* of [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#), deflation by too-low an inflation number (such as the CPI-U) results in the deflated series overstating inflation-adjusted economic growth.

As shown in the latest “corrected” real retail sales graph, in the *Opening Comments*, with the deflation rates corrected for understated inflation, the recent pattern of real sales activity has turned increasingly negative. The corrected graph shows that the post-2009 period of protracted stagnation ended, and a period of renewed contraction began in second-quarter 2012. The corrected real retail sales numbers use the ShadowStats-Alternate Inflation Measure (1990-Base) for deflation instead of the CPI-U.

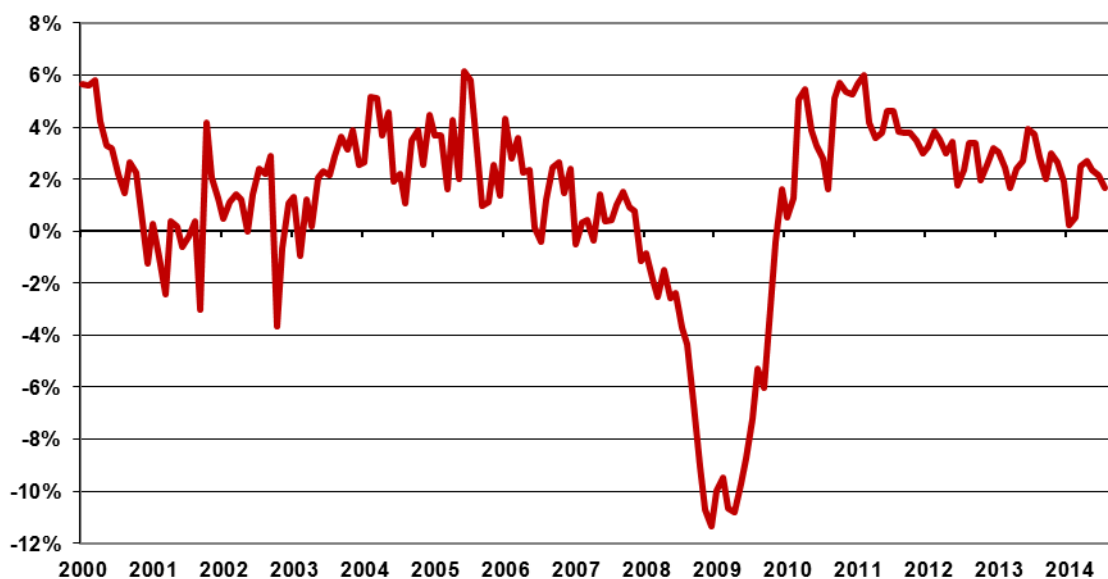
In addition, as discussed at the end of the *Opening Comments*, there has been no change in the underlying consumer-liquidity fundamentals. With low levels of stagnant, real household income and lack of the ability and/or willingness of the consumer to offset limited income with debt expansion, there is nothing that would support a sustainable turnaround in retail sales, personal consumption, housing or general

economic activity. There never was a broad economic recovery, and there is no recovery underway, just general bottom-bouncing that has begun turning down anew.

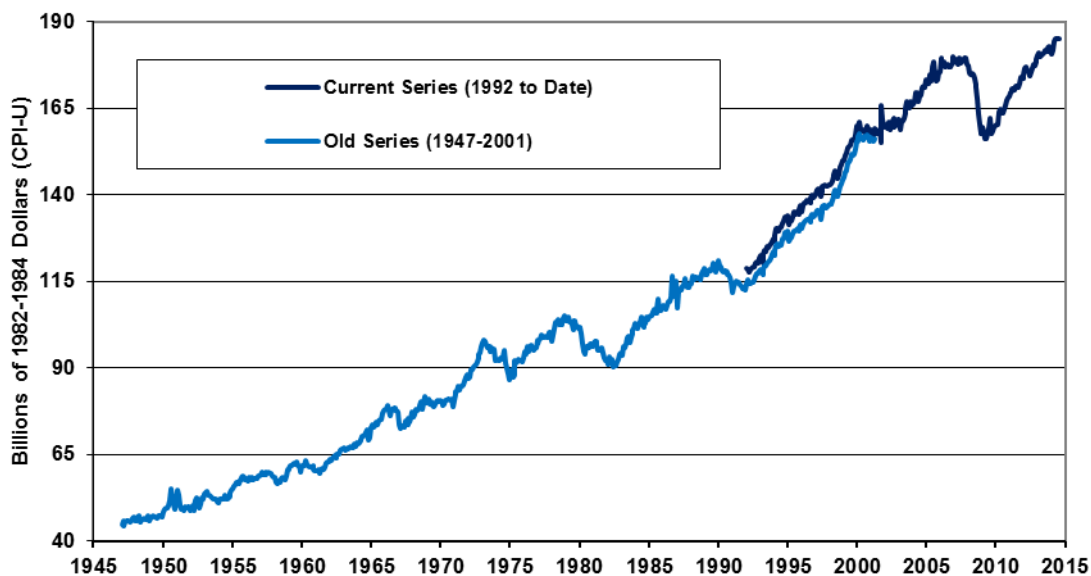
Real Retail Sales (Deflated by CPI-U), Revised
To July 2014, Seasonally-Adj. (ShadowStats, Census, BLS)



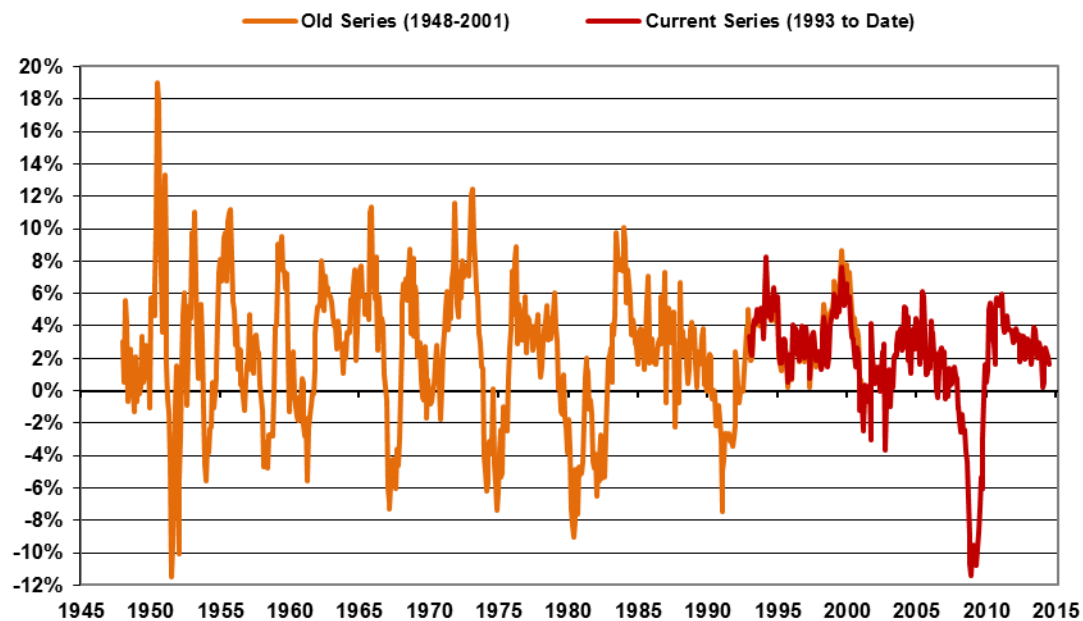
Real Retail Sales Year-to-Year % Change
To July 2014, Seasonally-Adj. (ShadowStats, Census, BLS)



Real Retail Sales (Deflated by CPI-U)
To July 2014, Seasonally-Adj. (ShadowStats, St. Louis Fed)



Real Retail Sales Yr/Yr Percent Change
To July 2014, Seasonally-Adj. (ShadowStats, St. Louis Fed)



As official consumer inflation continues its upturn in the months ahead, and as overall retail sales continue to suffer from the ongoing consumer liquidity squeeze—reflected partially by continued real earnings difficulties, discussed in the next section—these data should continue to trend meaningfully lower, in what still rapidly should gain recognition as a formal new or double-dip recession (again, see *Opening Comments*).

Real (Inflation-Adjusted) Average Weekly Earnings—July 2014—Below Second-Quarter 2014

Average. Coincident with today's July 2014 CPI-W release, the BLS also published real average weekly earnings for July. In the production and nonsupervisory employees series—the only series for which there is a meaningful history—headline real average weekly earnings (deflated by the CPI-W) rose by 0.12%, having fallen by a revised 0.16% (-0.16%) [previously down by 0.11% (-0.11%)] in June, versus unrevised declines of 0.14% (-0.14%) in May, and 0.19% (-0.19%) in April.

Net of prior-period revisions, the monthly gain in July was 0.07%, with the level of earnings holding below the level of May. July's real earnings were below the average level for second-quarter 2014.

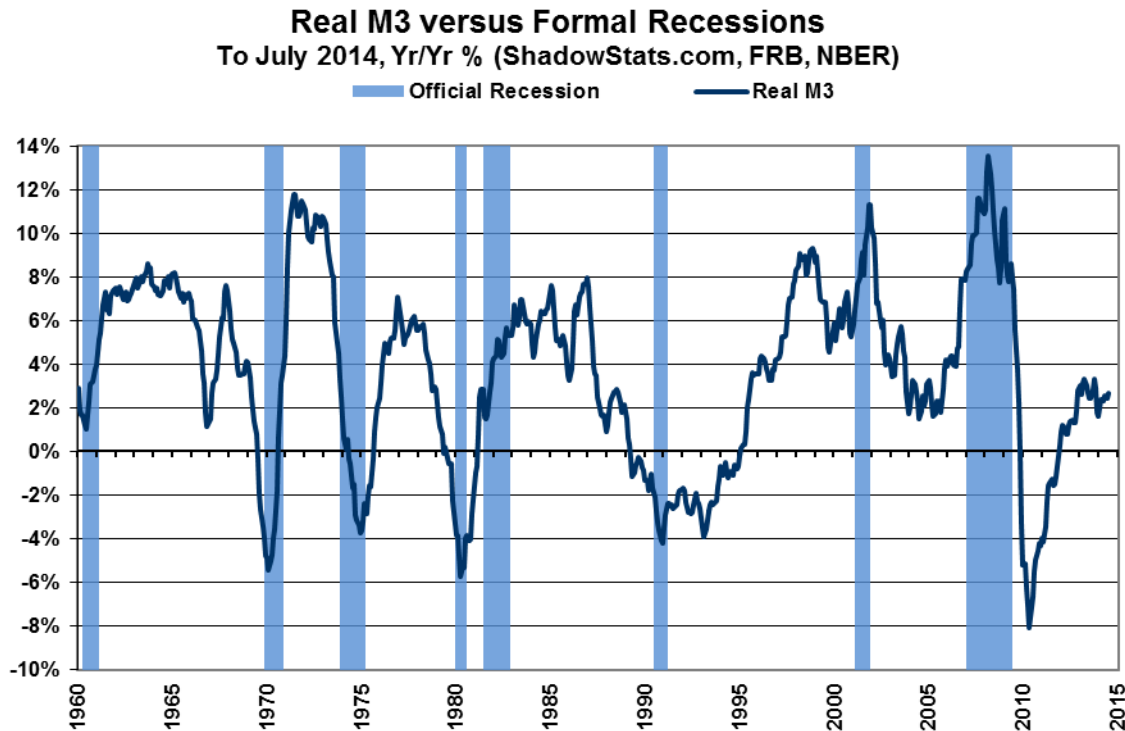
Year-to-year and seasonally-adjusted, July 2014 real average weekly earnings rose by 0.95% in July, versus a revised 0.28% (previously 0.24%) gain in June, an unrevised gains of 0.28% in May, and 0.32% in April. Both the monthly and annual fluctuations in this series are irregular, but current reporting remains well within the normal bounds of volatility. Prior-period revisions usually are due to the instabilities in the BLS monthly surveys.

The regular graph of this series is in the *Opening Comments* section. As shown there, the graph plots the earnings as officially deflated by the BLS (red-line), and as adjusted for the ShadowStats-Alternate CPI Measure, 1990-Base (blue-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. Official real earnings today still have not recovered their inflation-adjusted levels of the early-1970s, and, at best, have been flat for the last decade. Deflated by the ShadowStats measure, 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 the CPI-W. See [Public Commentary on Inflation Measurement](#) for further detail.

Real Money Supply M3—July 2014. The signal for a double-dip or ongoing recession, based on annual contraction in the real (inflation-adjusted) broad money supply (M3), remains in place and continues, despite real annual M3 growth holding in positive territory. As shown in the accompanying graph—based on July 2014 CPI-U reporting and the latest ShadowStats-Ongoing M3 Estimate—annual inflation-adjusted growth in M3 for July 2014 moved higher to 2.7%, from an unrevised 2.4% in June. The pick up in the July annual growth rate reflected a stronger gain in annual headline M3 growth, with headline annual CPI-U inflation easing to 2.0% from 2.1% in June.

The signal for a downturn or an intensified downturn is generated when annual growth in real M3 first 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 current downturn signal was generated in December 2009, even though there had been no upturn since the economy hit bottom in mid-2009. The broad economy tends to follow in downturn or renewed deterioration roughly six-to-nine months after the signal. Weaknesses in a number of series

continued into 2011 and 2012, with significant new softness in recent reporting. Actual post-2009 economic activity has remained at low levels—in protracted stagnation.



A renewed downturn in official data appears to be underway, and that eventually should lead to official recognition of a “new” or double-dip recession. Reality remains that the economic collapse into 2009 was followed by a plateau of low-level economic activity—no upturn or recovery, no end to the official 2007 recession—and the unfolding renewed downturn remains nothing more than a continuation and re-intensification of the downturn that began unofficially in 2006. Further discussion of this issue is found in *Chapter 8* of the [2014 Hyperinflation Report—Great Economic Tumble – Second Installment](#).

RESIDENTIAL CONSTRUCTION (July 2014)

Extreme Volatility in Reporting and Revisions Leaves Initial Estimates of Housing-Starts Meaningless.

Following last month’s extreme downside volatility in reporting and revisions, headline July 2014 reporting showed extreme instability on the upside. With horrendously-distorted reporting and seasonal-adjustment issues carrying over from last year’s shutdown of the federal government, the Census Bureau appears to be unable to publish consistent housing starts data on a regular monthly basis. The problem is ongoing, and it has reached a level where the initial headline reporting is virtually worthless. Nonetheless, the headline numbers are graphed and reported here, per official reporting.

As still can be seen in the graphs, and as should be confirmed generally in subsequent reporting, housing starts activity broadly has continued to stagnate, with the personal housing sector constrained by consumer liquidity issues.

Structurally-Impaired Consumer Liquidity Restrains Housing Market Activity. As touched upon at the end of the *Opening Comments* section, the last six-plus years of economic collapse and stagnation have been dominated by consumer activity that has been constrained heavily by intense, structural-liquidity problems. Without real, or inflation-adjusted, growth in income, and without the ability or willingness to take on meaningful new debt, the consumer simply does not have the wherewithal to fuel real growth in private housing or retail sales. The underlying economic fundamentals do not support a sustainable turnaround in the housing industry or in general economic activity.

July 2014 Housing-Starts Reporting. The Census Bureau reported today, August 19th, a statistically-significant, seasonally-adjusted headline monthly gain in July 2014 housing starts of 15.7% +/- 12.8% (all confidence intervals are at the 95% level). That monthly gain was on top of a 5.5% upside revision to the previously-reported level of June housing starts. The July surge was dominated by a monthly 33.8% jump in the “five units or more” category and an 8.3% gain in the “one unit” category, but those gains were not separately statistically-significant.

June 2014 housing starts fell by a revised 4.0% (-4.0%), previously down by 9.3% (-9.3%), month to-month. Net of prior-period revisions, July housing starts jumped by an incredible (as in not believable) 22.4%.

Year-to-year change in the seasonally-adjusted, aggregate July 2014 housing-starts measure was a statistically-significant gain of 21.7% +/- 12.5%, versus a revised 13.7% (previously 7.5%) annual gain in June 2014.

By-Unit Category (See Graphs in the Opening Comments). Where the irregular housing starts series can show varying patterns, that partially is due to a reporting mix of residential construction products, with the largest physical-count category of one-unit housing starts—generally for individual consumption—resulting in new home sales, versus multi-unit starts that generally reflect the building of rental and apartment units.

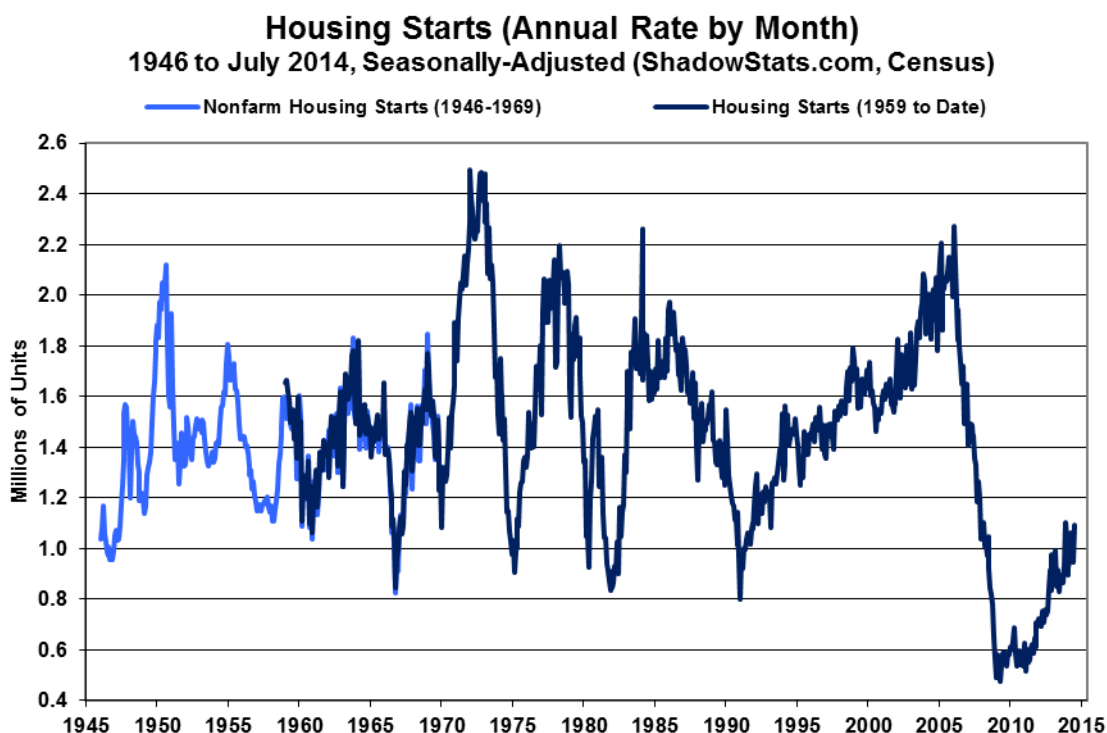
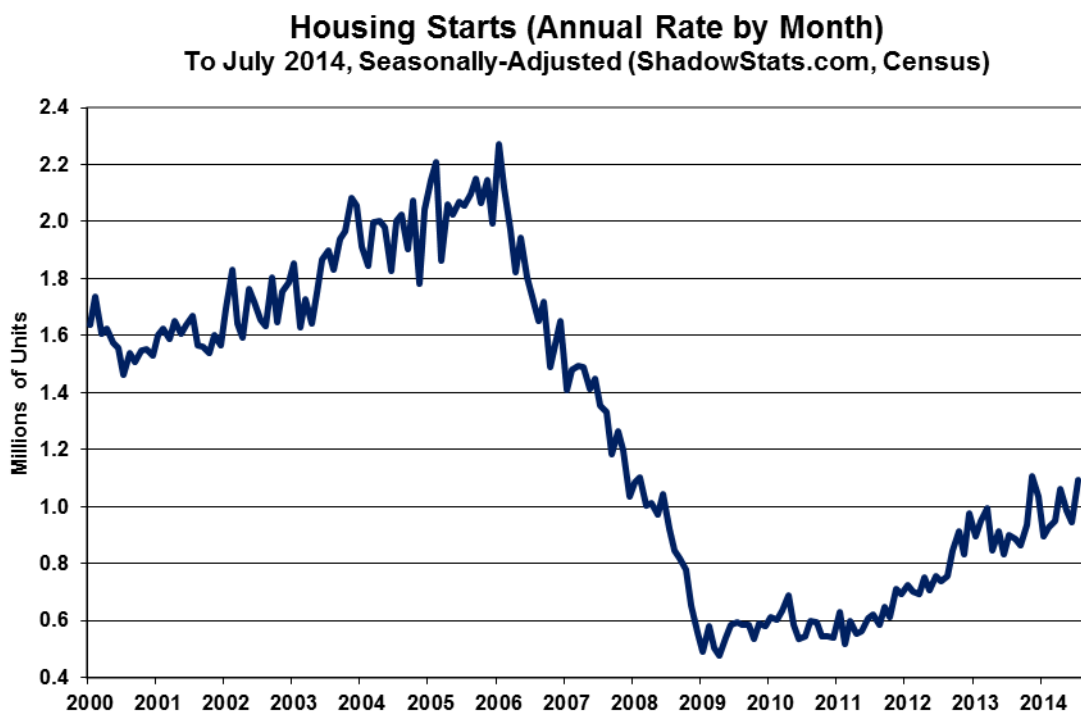
Housing starts for single-unit structures in July rose month-to-month by a statistically-insignificant 8.3% +/- 12.1%, following a revised headline monthly contraction of 4.4% (-4.4%), previously down by 9.0% (-9.0%), in June. July’s year-to-year gain of 10.1% +/- 15.3% followed a revised year-to-year gain of 0.8% in June, which previously had been reported with an annual contraction of 4.3% (-4.3%).

Reporting of housing starts for apartment buildings (generally 5-units-or-more) in July 2014 jumped by a statistically-insignificant 33.0% +/- 39.5%, to a level not seen since January 2006. That followed a revised monthly decline of 6.7% (-6.7%) in June, which previously had been down by 11.3% (-11.3%). July’s year-to-year gain of 49.5% +/- 39.3% was statistically-significant, was against a revised year-to-year gain in June 2014 of 45.2% (previously up by 39.3%).

Expanding the multi-unit housing starts category to include 2-to-4-units plus 5-units-or-more usually reflects the bulk of rental- and apartment-unit activity. The Census Bureau does not publish estimates of the 2-to-4-units category, due to statistical significance problems (a general issue for the aggregate series). Nonetheless, the total multi-unit category can be calculated by subtracting the single-unit category from the total category.

Accordingly, the statistically-significant aggregate July monthly gain of 15.7% was composed of a statistically-insignificant increase of 8.3% in one-unit housing starts, combined with a statistically-

insignificant monthly gain of 28.9% in multiple-unit structures (2-units-or-more, including the 5-units-or-more category). These series are graphed in the *Opening Comments* section.



Graphs of Aggregate Housing Starts Activity. Headline reporting of housing starts is expressed by the Census Bureau as an annualized monthly pace of starts, which was 1,093,000 in July, versus a revised 945,000 (previously 893,000) in June 2014. Those annualized details are reflected in the preceding, aggregate graphs.

Nonetheless, given the nonsensical volatility in reporting and the exaggerated effect of annualizing the monthly numbers in this unstable series—such as was seen with the headline July 2014 reporting—the magnitude of monthly activity, and changes in same, more realistically is reflected at the non-annualized monthly rate. For example, the monthly rate of 91,083 in July 2014, instead of the annualized headline 1,093,000 annualized July rate, is used in the scales of the graphs in the *Opening Comments* section. Based on the annualized numbers, housing starts increased by 148,000 units in July 2014. Yet such an increase by itself is more than any single seasonally-adjusted month's non-annualized total monthly housing starts since June 2006.

With the use of either scale, however, the appearance of the graph and the relative monthly, quarterly and annual percentage changes are the same.

The record monthly low seen for the present aggregate series was in April 2009, where the annualized monthly pace of sales was down 79% (-79%) from the January 2006 pre-recession peak. Against the downside-spiked low in April 2009, the July 2014 headline number was up by 98%, but it still was down by 58% (-58%) from the January 2006 series high.

WEEK AHEAD

Against Overly-Optimistic Expectations, Pending Economic Releases Should Be Much Weaker; Inflation Releases Should Be Increasingly Stronger. Although shifting to the downside, again, amidst wide fluctuations, market expectations for business activity generally remain overly optimistic, well above any potential, underlying economic reality. Market outlooks should be hammered, though, by ongoing, downside corrective revisions and by an accelerating pace of downturn in headline economic activity.

Longer-Range Reporting. The initial stages of the process shifting economic-growth expectations to the downside already have been seen in the recent headline reporting of many major economic series (see [*2014 Hyperinflation Report—Great Economic Tumble – Second Installment*](#)), including the sharp pace of economic decline seen in real first-quarter 2014 GDP, which largely survived the GDP benchmark revisions. The initial strong bounce-back guessed at by the Bureau of Economic Analysis (BEA), for

headline second-quarter GDP, should prove to be fleeting, both with looming downside revisions, and with a likely GDP contraction in third-quarter 2014.

Indeed, weakening, underlying economic fundamentals indicate still further deterioration in business activity. Accordingly, weaker-than-consensus economic reporting should remain the general trend until the unfolding “new” recession receives broad recognition, which likely would follow the next reporting of a headline contraction in real GDP growth.

A generally stronger inflation trend remains likely to continue, as seen in recent months. Beyond the spread of earlier oil-based inflation pressures into the broad economy, upside pressure on oil-related prices should continue and be rekindled from the intensifying impact of global political instabilities and a likely near-term weakening of the U.S. dollar in the currency markets. Again, food inflation also is picking up, partially due to supply issues. The dollar faces pummeling from the weakening economy, continuing QE3, the ongoing U.S. fiscal-crisis debacle, and deteriorating U.S. and global political conditions (see [*Hyperinflation 2014—The End Game Begins \(Updated\) – First Installment*](#)). Particularly in tandem with a weakened dollar, reporting in the year ahead generally should reflect much higher-than-expected U.S. inflation in a broad range of areas.

A Note on Reporting-Quality Issues and Systemic-Reporting Biases. Significant reporting-quality problems remain with most major economic series. Ongoing headline reporting issues are tied largely to systemic distortions of seasonal adjustments. The data instabilities were induced by the still-evolving economic turmoil of the last eight years, which has been without precedent in the post-World War II era of modern economic reporting. These impaired reporting methodologies provide particularly unstable headline economic results, when concurrent seasonal adjustments are used (as with retail sales, durable goods orders, employment, and unemployment data). These issues have thrown into question the statistical-significance of the headline month-to-month reporting for many popular economic series.

PENDING RELEASES:

Existing- and New-Home Sales (July 2014). July 2014 existing-home sales are due for release on Friday, August 21st, from the National Association of Realtors, with the July 2014 new-home sales report from the Census Bureau due on Monday, July 25th.

A pattern of stagnation or intensifying downturn appears to be in play for both the existing- and new-home sales. Weakened existing-home sales activity has shown some recent relative stability, despite continuing year-to-year declines. While monthly changes in home-sales activity usually are not statistically-significant, still-unstable reporting and revisions (both likely to the downside) also remain a fair bet for the new-home sales series, which took a hit in June reporting. Both series remain highly volatile, but increasingly should move to the downside in activity.

New Orders for Durable Goods (July 2014). The reporting of July 2014 new orders for durable goods is scheduled for Tuesday, August 26th, by the Census Bureau. Recently, new orders generally have been stagnant, plus or minus, particularly net of inflation. Sharp and irregular volatility in commercial aircraft orders should dominate the numbers anew in the next several months. Commercial aircraft orders usually

are booked years in advance with relatively minimal impact on near-term production activity. Net of the unstable aircraft reporting, some intensification in downside activity is likely, coincident with slowing activity seen recently in the broad economy. Market expectations appear to be strongly to the upside for the July activity, with headline reporting generally a fair bet to disappoint expectations on the downside.

Gross Domestic Product—GDP (Second-Quarter 2014, Second Estimate, First Revision). On Thursday, August 28th, the Bureau of Economic Analysis (BEA) will publish its second estimate of, and first revision to second-quarter 2014 GDP. The initial guesstimate of 4.0% annualized, quarterly real growth was overstated by a massive amount (see [Commentary No. 646](#)), and it should revise significantly lower in this revision and the next. Market expectations appear to be for a negligible, downside revision. Eventual downside revisions should be much worse than expected, as discussed in today's *Opening Comments* section.
