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

COMMENTARY NUMBER 655
August Payroll Employment and Unemployment, Money Supply M3

September 5, 2014

Payroll Jobs Growth Faltered in Context of Unusual Seasonal Factor Shifts

August Unemployment Rate: 6.1% (U.3), 12.0% (U.6), 23.2% (ShadowStats)

Downward Notch in Unemployment Rate Reflected Further Loss of Labor Force, Not the Unemployed Gaining Employment

U.3 Rate Was Less than 979 Unemployed People Shy of Holding at 6.2%

August 2014 Civilian Employment Still Shy of Pre-Recession Peak

August Money Supply M3 at 4.6% Annual Growth

PLEASE NOTE: The next regular Commentary *is scheduled for, Friday, September 12th, covering August retail sales.*

Best wishes to all — John Williams

OPENING COMMENTS AND EXECUTIVE SUMMARY

Bad News on the Labor Front. The economy remains in serious trouble, and most upcoming economic releases should tend to confirm that, shy of possible political interventions. In the context of the ongoing, horrendous reporting-quality and consistency issues in the monthly labor-conditions release, today's (September 5th) details on August employment and unemployment held little good news.

Irrespective of any poor-quality reporting, the consensus outlook on the economy likely will be taken down a notch (poor-quality positive labor reporting did little to inhibit the current irrational upside expectations on the economy). That process should accelerate to the downside with further negative reporting surprises, such as with next week's headline estimate on August retail sales (see *Week Ahead Section*).

August 2014 Payroll Employment—A Solid Monthly Contraction of 125,000 (-125,000). The headline August payroll employment gain of 142,000 came in well below market expectations, along with downside revisions to the headline payroll-employment levels of recent months. Without the downside revisions, the headline August gain would have been 114,000. Without the masked shifting of jobs from month-to-month, driven by the changing seasonal adjustments within the concurrent-seasonal-adjustment process used by Bureau of Labor Statistics (BLS), the headline August gain would have been roughly 39,000 less (see the *Reporting Detail* section), or a less-gimmicked headline gain of 75,000 jobs.

Separately, adjusting for the biases built into the birth-death model adjustments (see *Birth-Death Model* section), the headline change in August 2014 payrolls likely was a solid contraction in excess of 125,000 jobs (-125,000).

Where the underlying seasonal-adjustment shifts actually boosted headline August payroll activity from where it would have been otherwise. Similar shifts likely will have positive impact on headline September 2014 payroll reporting, the last such accounting before the November 4th election.

August 2014 Unemployment—No Good News Here. The "good" news of a 0.1% decline in the headline August U.3 unemployment rate was no such thing. The decline in the number of unemployed largely was reflected in a reduction of the headline labor force, not in an offsetting gain of employed individuals. The BLS just continued to write-off those politically-inconvenient individuals who are having problems finding work in this pre-election economic "boom."

Separately, based on the limited data available, the August U.3 unemployment rate was 6.1497%, rounding out to 6.1%, somewhere shy of less than 979 unemployed individuals of rounding up to, and holding at, a 6.2% unemployment rate for a second month.

Reflecting the number of people who are employed, per the household survey, total civilian employment remains several hundred thousand shy of recovering its pre-recession high. In contrast, reflecting multiple-job holders, and boosted by a rising number of part-time jobs, the number of payroll-survey jobs recovered its pre-recession high back in May 2014. Graphs follow later in these *Opening Comments*.

August 2014 Money Supply M3. Discussed in the *Hyperinflation Watch*, year-to-year growth for August M3 notched lower to 4.6%, from 4.7% in June. The monetary base, still near a record high; and a slowing pace of Fed monetization, reflective of continued tapering, also are updated.

Employment and Unemployment—August 2014—The Numbers Begin to Shift. Despite developing new weakness in the employment and unemployment series, both the August 2014 headline jobs growth of 142,000 and headline unemployment rate at 6.1% remained far removed from common experience and underlying reality. As discussed frequently in these *Commentaries*, common experience generally would reflect headline monthly payroll employment changes of flat-to-minus, likely down by more than 125,000

(-125,000) jobs in August, with an unemployment rate—encompassing all short- and long-term discouraged workers—running above 23%.

As was particularly evident in the latest month, the headline employment gains are no more than statistical illusions resulting from hidden shifts in seasonal factors, and from phantom-jobs creation with the Birth-Death Model's upside bias factors (see the *Birth-Death/Bias-Factor Adjustment* and *Concurrent Seasonal Factor Distortions* sections for extended detail).

Further, as seen again with the August 2014 detail, headline U.3 unemployment rates are contained by, and actually "improve" with the BLS removal of increasingly-large numbers of discouraged workers from the counts of the unemployed and the labor force (see *ShadowStats-Alternate Unemployment Rate*). Separately, month-to-month comparisons of these numbers have no meaning; they simply are not comparable thanks to the concurrent seasonal factor process as practiced by the BLS (see *Concurrent Seasonal Adjustment Distortions*).

Payroll Survey Detail. The seasonally-adjusted, month-to-month headline payroll-employment gain for August 2014 was 142,000, significantly below trend and market expectations. In turn, July payrolls rose by a revised 212,000 (previously a 209,000 gain), but do not take that to mean that July's payroll activity was revised higher. The headline seasonally-adjusted payroll level for July revised lower by 28,000 jobs, from 139,004,000 to 138,976,000. Without the prior-period revision, the headline August gain would have been 114,000.

The headline gain in July revised higher by 3,000, only because of an even greater downside revision to June's headline employment level, revised lower by 31,000 jobs, from 138,795,000 to 138,764,000.

Net of the 39,000 jobs-boost from shift in seasonal factors, and net of the 200,000 upside monthly bias built into the Birth-Death Model (again, see related section in *Reporting Detail*), the adjusted 114,000 gain, net of revisions, otherwise looked like a pretty solid 125,000 jobs contraction (-125,000) for the month of August.

Distortions and Inconsistencies Continue on Back in Time. June payrolls rose by a revised 267,000 (previously 298,000), but that also is not an honest picture. Due to the misleading reporting policies used by the BLS, the headline June 2014 gain became non-comparable and inconsistent with the May 2014 data, as of the August reporting. The BLS calculates the prior history on a consistent basis, using concurrent seasonal-adjustment factors based on the current (August 2014 at present) reporting, but it does not publish the detail back in time for more than two months.

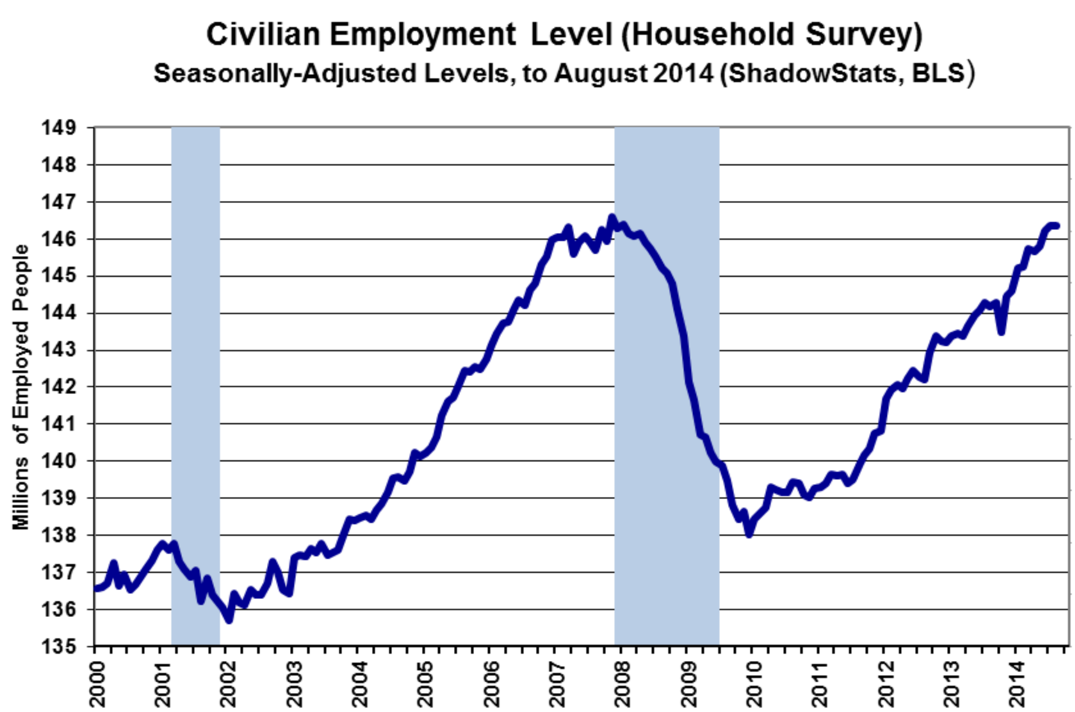
Using consistent seasonal-adjustment details available from the BLS, the actual differential in May to June 2014 reporting can be calculated, and it was a 289,000 increase instead of the headline 267,000 gain. The 22,000 difference is due to a further 22,000 downside revision to the seasonally-adjusted May payrolls. In like manner, with further concurrent downside revision to the April numbers, the headline April 2014 payroll gain, currently published as 229,000, really is 214,000. With revisions flipping direction in March, the existing headline gain of 304,000 for that month, should be 282,000, so as to be consistent with the seasonally-adjusted August 2014 reporting.

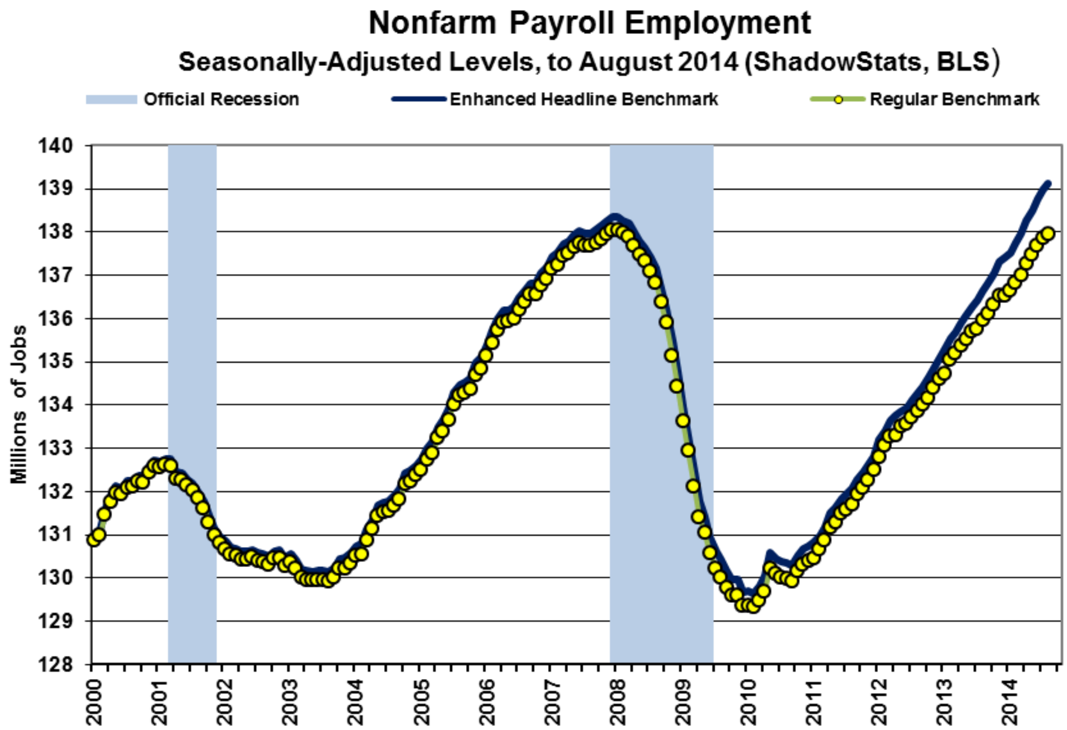
August Numbers Boosted by Invisible Adjustments. Consider, though, that the current headline number for the year-ago month of August 2013, is a monthly gain of 201,000. Due to jobs being shifted to other months by the constantly-changing, but not-reported, consistently-adjusted numbers, the actual headline gain for August 2013 versus July 2013 is 240,000, a difference of 39,000 jobs. The factors that make up the distortions of one-year ago directly affect the seasonally-adjusted levels and headline changes for the current July and August 2014 numbers.

Annual Change in Payrolls. Not-seasonally-adjusted, year-to-year change in payroll employment is untouched by the concurrent-seasonal-adjustment issues, so the monthly comparisons of year-to-year change are reported on a consistent basis, although the redefinition of the series—not the standard benchmarking process—recently boosted reported annual growth in the last year, as discussed and graphed in the benchmark detail of *Commentary No. 598*.

For August 2014, annual growth was 1.84%, versus an unrevised 1.92%—near-term peak annual growth—in July 2014, and an unrevised 1.88% in June. Had the 2013 benchmark revision been standard, not a gimmicked redefinition, year-to-year jobs growth as of August 2014 would have been about 1.5%, consistent with near-term, peak annual growth of about 1.9% in February 2012.

Record Jobs but Not Employment Levels. As seen in the first graph following, the number of employed individuals has yet to recover its pre-recession high, although such could happen in the next several months. That is in contrast to headline payroll employment, where the level of total jobs is at a record. The difference is that the payroll survey count reflects the number of jobs, irrespective of how many jobs an individual holds. The household survey count of employment reflects the number of people who are employed, not the number of jobs.





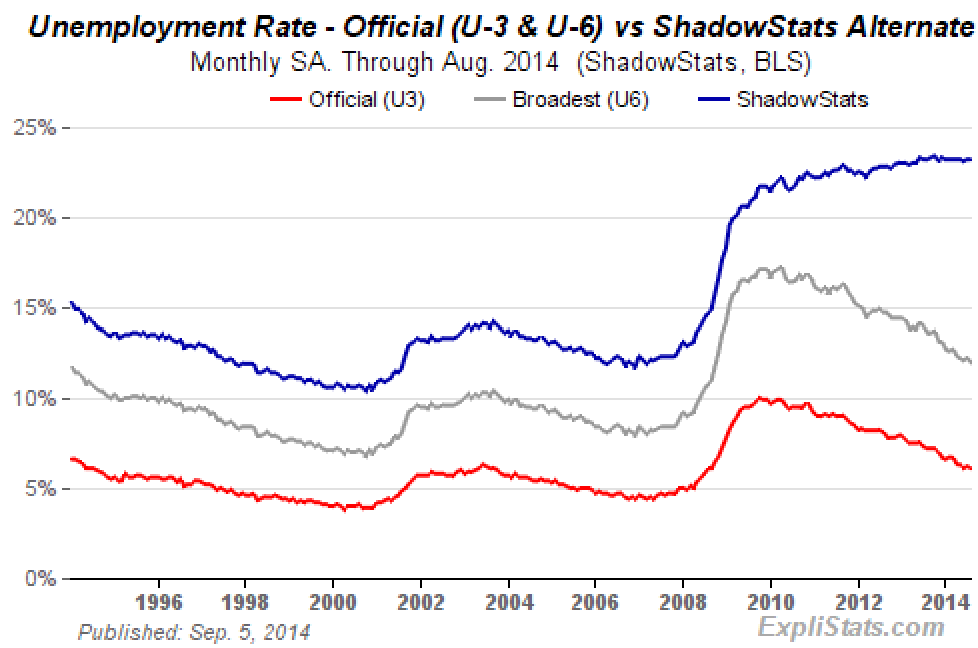
Headline payroll employment recovered its pre-recession high, in May 2014, and has continued to rise. This pattern, however, was accelerated by the payroll levels all being redefined favorably with the January 2014 benchmarking, despite the actual benchmark having been negative. This can be seen in the preceding second graph, of the payroll employment level. The yellow points in that graph reflect the ShadowStats assessment of what payroll employment would be showing, with just a regular benchmarking, rather than the gimmicked redefinition of the series, which added a new upside bias. Even with what should have been a standard benchmarking, however, the pre-recession level likely would be hit in the next month or so. Graphs of year-to-year headline payroll change and a longer-term perspective on headline payroll levels are shown in the *Reporting Detail.*

Counting All Discouraged Workers, July Unemployment Stood at 23.2%. The headline household survey reporting (unemployment-related) is virtually worthless. As previously discussed, the numbers are highly volatile and unstable, inadequately defined—not reflecting common experience—and simply are not comparable on a month-to-month basis. The month-to-month comparability issue again is tied to the concurrent seasonal adjustment process, discussed in the *Reporting Detail* section.

What removes headline-unemployment reporting from broad underlying economic reality and common experience simply is definitional. To be counted among the headline unemployed (U.3), an unemployed individual has to have looked for work actively within the four weeks prior to the unemployment survey. If the active search for work was in the last year, but not in the last four weeks, the individual is considered a "discouraged worker" by the BLS. ShadowStats defines that group as "short-term discouraged workers," as opposed to those who become "long-term discouraged workers" after one year.

Moving on top of U.3, the broader U.6 unemployment measure includes only the short-term discouraged workers. The still-broader ShadowStats-Alternate Unemployment Measure includes an estimate of all discouraged workers, including those discouraged for one year or more, as the BLS used to measure the series pre-1994, and as Statistics Canada still does.

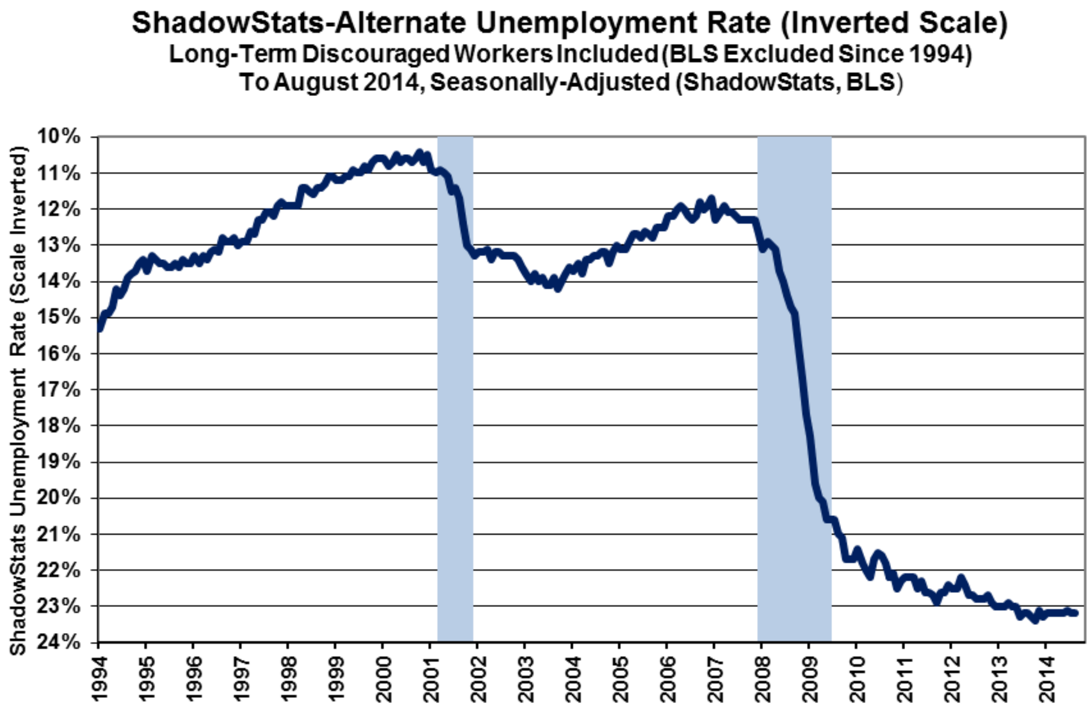
When the headline unemployed become discouraged, they roll over from U.3 to U.6. As the headline, short-term discouraged workers roll over into long-term discouraged status, they move into the ShadowStats measure, where they remain. Aside from attrition, they are not defined out of existence for political convenience, hence the longer-term divergence between the various unemployment rates. Further detail is discussed in the *Reporting Detail* section. The resulting difference here is between a headline June 2014 unemployment rate of 6.1% (U.3) and 23.2% (ShadowStats).

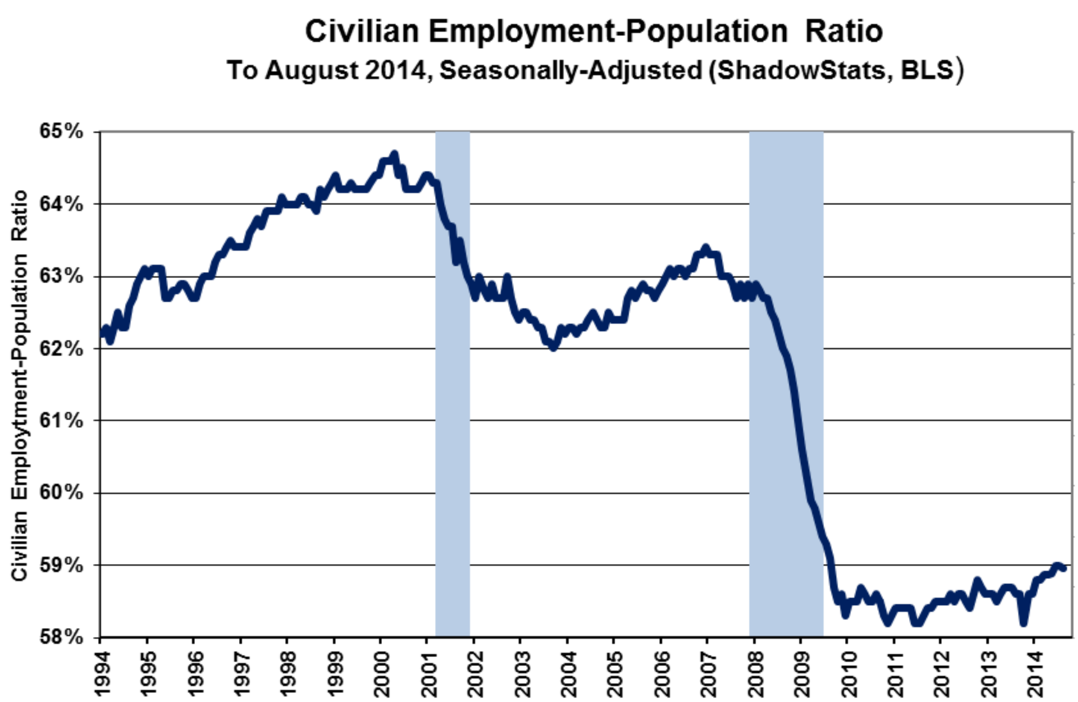


The graph immediately preceding reflects headline August 2014 U.3 unemployment at 6.1%, down from 6.2% in July; headline August U.6 unemployment declining to 12.0%, from 12.2% in July; and the headline August ShadowStats unemployment measure holding at 23.2% for the second month. The October 2013 ShadowStats reading of 23.4% was the series high (since 1994).

Two other graphs follow. The first is of the ShadowStats unemployment measure, with an inverted scale. The higher the unemployment rate, the weaker will be the economy, so the inverted plot tends to move in tandem with plots of most economic statistics, where a lower number means a weaker economy.

The inverted-scale ShadowStats unemployment measure also tends to move with the employment-to-population ratio, which is plotted in the second graph. Discouraged workers are not counted in the headline labor force, which generally continues to shrink. The labor force containing all unemployed (including total discouraged workers) plus the employed, however, tends to be correlated with the population, so the employment-to-population ratio tends to be something of a surrogate indicator of broad unemployment, and it has a strong correlation with the ShadowStats unemployment measure.





The preceding graphs reflect detail back to the 1994 redefinitions of the household survey. Before 1994, data consistent with today's reporting are not available.

Headline Unemployment Rates. Subject to the reporting issues and lack of real-world relevance discussed elsewhere, the headline August 2014 unemployment (U.3) rate fell by 0.05% (-0.05%) to 6.15% (rounds to 6.1%), versus 6.20% in July. Again, though, month-to-month comparisons are meaningless, in the context of the month-to-month reporting-inconsistencies created by the concurrent seasonal factors. On an unadjusted basis, however, the unemployment rates are not revised and at least are consistent in reporting methodology. August's unadjusted U.3 unemployment rate fell to 6.3% from 6.5% in July.

With a minor, seasonally-adjusted decline in people working part-time for economic reasons, and an increase in short-term (unadjusted) discouraged workers, headline August 2014 U.6 unemployment declined to 12.0% from 12.2% in July. Unadjusted U.6 declined to 12.0% in August, from 12.6% in July.

Adding back into the total unemployed and labor force the ShadowStats estimate of the growing ranks of excluded, long-term discouraged workers, broad unemployment—more in line with common experience, the August 2014 ShadowStats-Alternate Unemployment Measure—held at 23.2% for the second month. That still was down minimally from 23.4% in October 2013, which was the series high (back to 1994). The ShadowStats estimate shows the increasing toll of unemployed leaving the headline labor force.

[For further details on the August employment and unemployment details, see the* Reporting Detail *section.]

[Also, various drill-down detail and graphics options on the headline employment data are available to ShadowStats subscribers at our affiliate: www.ExpliStats.com]

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HYPERINFLATION WATCH

Recent Monetary Conditions—Monetary Base Near All-Time High; M3 Growth Notched Lower; Pace of Fed Monetization Slows. Despite increased "tapering," by the Federal Reserve Board, the U.S. central bank's reduced pace of purchases of U.S. Treasury securities has not been matched by a downturn in the monetary base. Still, annual growth in money supply M3 slowed in August, and the effective pace of Federal Reserve monetization of net Treasury issuance has slowed markedly.

Money Supply M3 Annual Growth Eased to 4.6% in August 2014. On track to hit 4.6% annual growth in August 2014, M3's year-to-year percent gain has notched lower from an unrevised 4.7% in July. Monthly year-to-year growth began to slow after hitting a near-term peak of 4.6% in each of the months of January, February and March 2013, the onset of expanded QE3. Growth then fell to a near-term trough of 3.2% in January 2014, but that period of slowing growth had reversed fully as of May 2014, with annual growth then at 4.7%, the highest since the "end" of the recession, in July 2009. Annual growth pulled back to 4.5% in June 2014, but jumped anew to 4.7% in July. The M3 estimates and the first readings of annual growth for M2 and M1 in August 2014 will be posted on the Alternate Data tab of www.ShadowStats.com by tomorrow, September 6th.

Any revisions in the following numbers generally are attributable to recent revisions in underlying data by the Federal Reserve. The seasonally-adjusted, preliminary estimate of month-to-month change for August 2014 money supply M3 was roughly a gain of 0.1%, down from an unrevised 0.6% increase in July. Estimated month-to-month M3 changes, however, remain less reliable than are the estimates of annual growth.

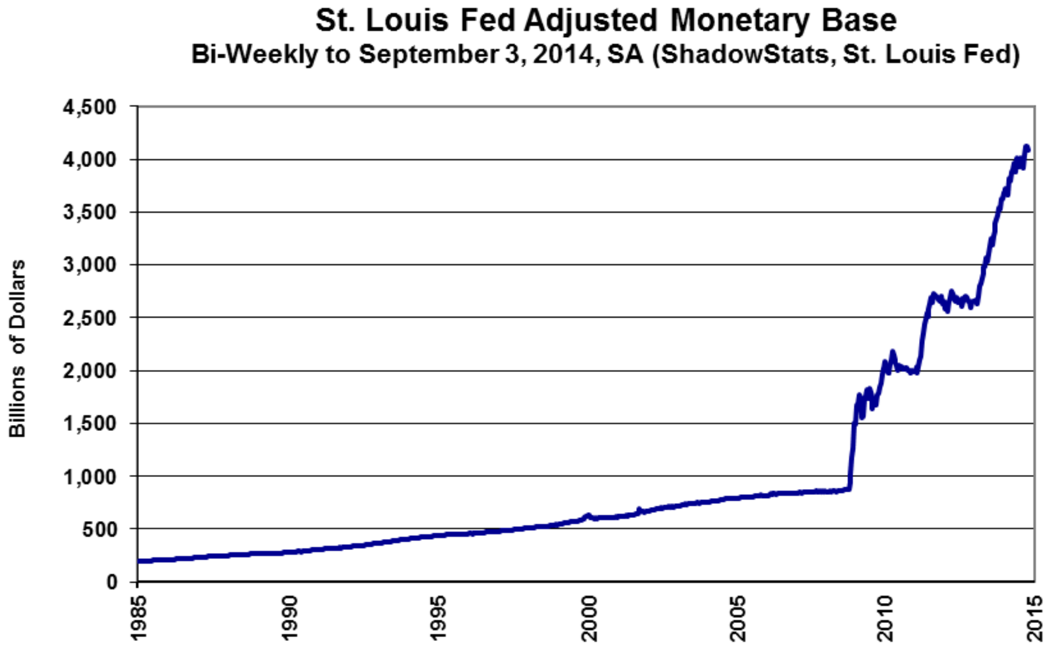
Growth for August M1 and M2. For August 2014, year-to-year and month-to-month changes follow for the narrower M1 and M2 measures (M2 includes M1; M3 includes M2). See the *Money Supply Special Report* for full definitions of those measures. M2 for August 2014 showed roughly 6.5% year-to-year growth, down from a revised 6.7% (previously 6.6%) in July, with a month-to-month gain of about 0.3% in August, versus an unrevised 0.6% increase in July. For M1 in August 2014, year-to-year growth was about 10.1%, versus an unrevised 11.7% in July, with a month-to-month August contraction of about 1.4% (-1.4%), versus a revised July gain of 0.7% (previously 0.8%).

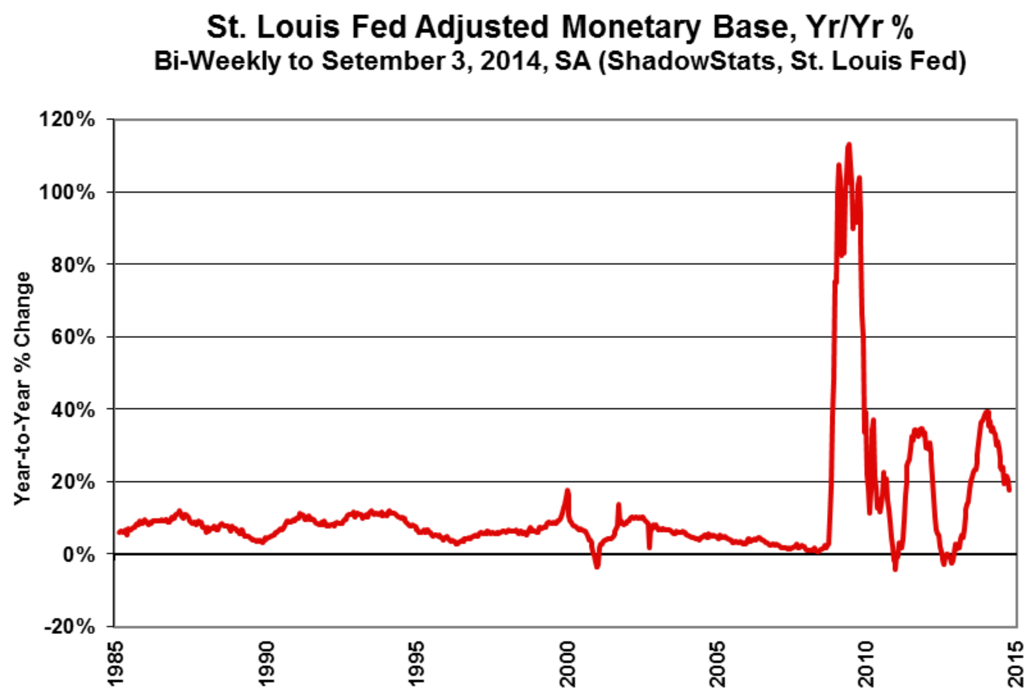
Fed Has Monetized 65.9% of Net Treasury Debt Issuance for the Public, Since January 2013 Onset of Expanded QE3. In the context of rapidly declining purchases of U.S. Treasuries—the continued "tapering" in the Federal Reserve's quantitative easing program QE3—effective monetization of Treasury debt has slowed markedly, as the pace of Fed purchases of Treasury securities finally has dropped below the pace of Treasury issuance.

The Fed's net acquisition of U.S. Treasury securities so far in calendar-year 2014 (through September 3rd), versus net debt issuance of the U.S. Treasury for the public in the same period, has reflected effective monetization of 58.2% of the increase in debt. That pace is down from over 90% just two months back. That is against effective monetization of 69.7% of the net issuance of publicly-held debt in the full calendar-year 2013. From the onset of expanded quantitative easing QE3 in January 2013 to date, the Fed has monetized 65.9% of the increased Treasury debt held by the public.

The ongoing monetization of the Treasury debt likely had been a contributing factor to the recent pickup, albeit minimal, seen in broad money supply (M3) growth. It also has continued 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.

Monetary Base Just off Record High. As reflected in the following graphs, again, despite the "tapering" in debt purchases, the monetary base (St. Louis Fed measure) moved to an all-time high in the two weeks ended August 20, 2014, at $4.125 trillion, but then backed off in the two week period ended September 3, 2014 to $4.084 trillion. Year-to-year growth, with current changes compared to even faster growth the year before, was at 20.3% in the August 20th period, with annual growth at 17.9% in the September 3rd period.





Hyperinflation Outlook Summary. This *Summary* has not been revised since *Commentary No. 654* of August 28th, other than for an updated monetization number discussed in the prior section. The next revision is planned to follow the heavy calendar of economic releases from September 12th through the 18th. 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 second estimate of second-quarter 2014 GDP growth came in at 4.17%, such still heavily overstated actual current economic activity and remained subject to some downside revisions. The "advance" estimate of third-quarter GDP on October 30th will be that last reporting before the midterm election. While third-quarter GDP should show a quarterly contraction within its standard revision cycle, one should not underestimate the ability of the Bureau of Economic Analysis to keep that final pre-election number in positive territory, in initial reporting.

Nonetheless, basic underlying economic series, such as the trade deficit, retail sales and industrial production, even payroll employment, should be showing enough of a downturn or weakness in headline activity during the same timeframe—the next several months—so as to provide consensus expectations with downside shocks. That increasingly should shift the popular outlook towards a "new recession," with negative shifts in the economic 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 58.2% of effective net issuance of the federal debt to be held by the public in calendar-year 2014 (through September 3rd). The pace of effective monetization has been 65.9% 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.

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REPORTING DETAIL

EMPLOYMENT AND UNEMPLOYMENT (August 2014)

Seriously-Flawed Headline Reporting of Jobs Growth and Unemployment Continues, Month-after-Month. Both the August 2014 headline jobs growth of 142,000 and headline unemployment rate at 6.1% remained far removed from common experience and underlying reality. As discussed frequently in these *Commentaries,* common experience generally would reflect headline monthly payroll employment changes of flat-to-minus, likely down more than 125,000 jobs (-125,000) in August; with an unemployment rate, encompassing all short- and long-term discouraged workers, running above 23%.

As was particularly evident in August, headline employment gains are no more than statistical illusions resulting from hidden shifts in seasonal factors, and from phantom-jobs creation with the Birth-Death Model's upside bias factors (see the *Birth-Death/Bias-Factor Adjustment* and *Concurrent Seasonal Factor Distortions* sections for extended detail).

Further, as seen in August reporting, headline U.3 unemployment rates are contained by, and actually "improve" with the BLS removal of increasingly-large numbers of discouraged workers, from the counts of the unemployed and the labor force (see *ShadowStats-Alternate Unemployment Rate*). Separately, month-to-month comparisons of these numbers have no meaning; they simply are not comparable thanks to the concurrent seasonal factor process as practiced by the BLS (see *Concurrent Seasonal Adjustment Distortions*).

PAYROLL SURVEY DETAIL. Published today, September 5th, by the Bureau of Labor Statistics (BLS), the seasonally-adjusted, month-to-month headline payroll-employment gain for August 2014 was 142,000 +/- 129,000 (95% confidence interval), significantly below trend and market expectations. In turn, July payrolls rose by a revised 212,000 (previously a 209,000 gain), but do not take that to mean that July's payroll activity was revised higher. The headline seasonally-adjusted payroll level for July revised lower by 28,000 jobs, from 139,004,000 to 138,976,000. Without the prior-period revision, the headline August gain would have been 114,000.

The headline gain in July revised higher by 3,000, only because of an even greater downside revision to June's headline employment level, revised lower by 31,000 jobs, from 138,795,000 to 138,764,000.

Net of the 39,000 jobs boost from the shift in seasonal factors discussed below in *August Numbers Boosted by Invisible Adjustments*, and net of the 200,000 upside monthly bias built into the Birth-Death Model (see related section following), the adjusted 114,000 gain, net of revisions, otherwise looks like a at least a 125,000 jobs contraction (-125,000) for the month of August

Distortions and Inconsistencies Continue on Back in Time. June payrolls rose by a revised 267,000 (previously 298,000, initially a 288,000 gain), but that also is not an honest picture. Due to the misleading reporting policies used by the BLS, the headline June 2014 gain became non-comparable and inconsistent with the May 2014 data, as of the August reporting. The BLS calculates the prior history on a consistent basis, using concurrent seasonal-adjustment factors based on the current (August 2014 at present) reporting, but it does not publish the detail back in time for more than two months.

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August Numbers Boosted by Invisible Adjustments. Consider, though, that the current headline number for the year-ago month of August 2013, is a monthly gain of 201,000. Due to jobs being shifted to other months by the constantly-changing, but not-reported, consistently-adjusted numbers, the actual headline gain for August 2013 versus July 2013 is 240,000, a difference of 39,000 jobs. The factors that make up the distortions of one-year ago directly impact the seasonally-adjusted levels and headline changes for the current July and August 2014 numbers.

Where the current employment levels have been spiked by misleading and inconsistently-reported concurrent-seasonal-factor adjustments, the reporting issues suggest that a 95% confidence interval around the monthly headline payroll gain should be well beyond +/- 200,000 around the formal modeling of the headline gain, instead of the official +/- 129,000.

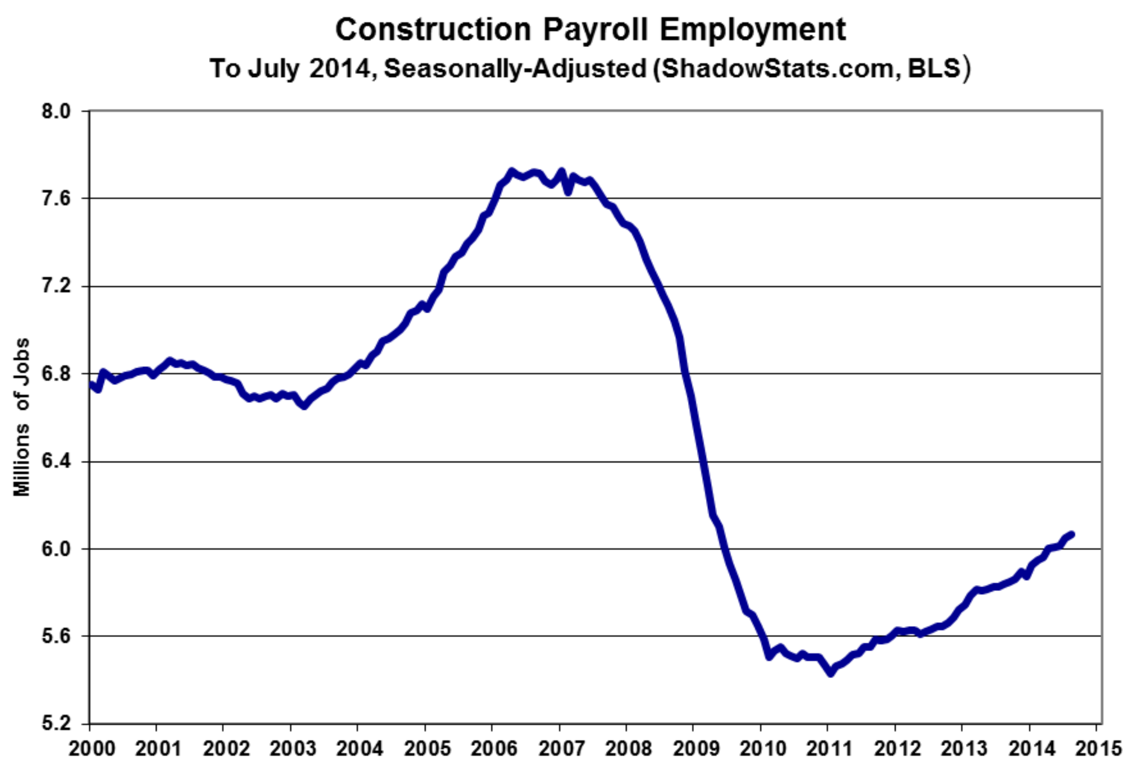
"Trend Model" Estimate and Consensus Overestimated August Jobs Gain. As discussed in *Commentary No. 647*, and as described generally in *Payroll Trends*, the trend indication from the BLS's concurrent-seasonal-adjustment model—prepared by our affiliate www.ExpliStats.com—was for an August 2014 monthly payroll gain of 247,000, based on the trend structured into the BLS modeling of July's actual reporting. The late-consensus for August appears to have been about 225,000, where the headline gain came in at 142,000.

Reporting Shortfalls versus BLS Trend. As to the trend built into the BLS seasonal-adjustment modeling, which suggested a headline gain of 247,000 jobs for August, versus the headline gain of 142,000, the 105,000 jobs shortfall in reporting versus the government's trend model was distributed over a number of areas, but two sectors accounted for 62,000 of the reporting "surprise." Manufacturing was shy by 19,000, while trade, transportation and utilities fell 43,000 jobs short of the government's modeling. The latter number was dominated by a 23,000 shortfall in jobs for food and beverage stores, with a reported loss of 17,100 jobs there, versus an expected trend gain of 5,900 positions.

Full detail on the headline payroll data, including various drill-down and graphics options are available to ShadowStats subscribers at ShadowStats-affiliate www.ExpliStats.com.

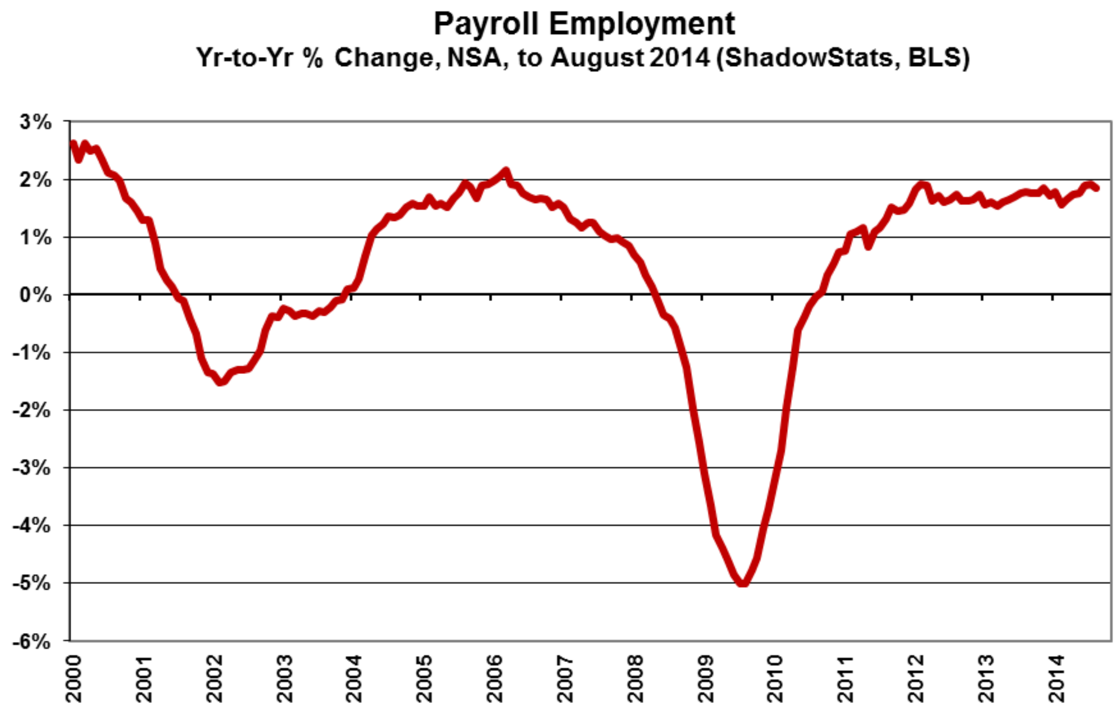
September Trend Estimate. Based on the August 2014 BLS seasonal-adjust modeling, the trend number built into the BLS calculations is for a headline gain of 224,000 in September 2014. The consensus outlook for September, eventually, most likely will settle-in around that number.

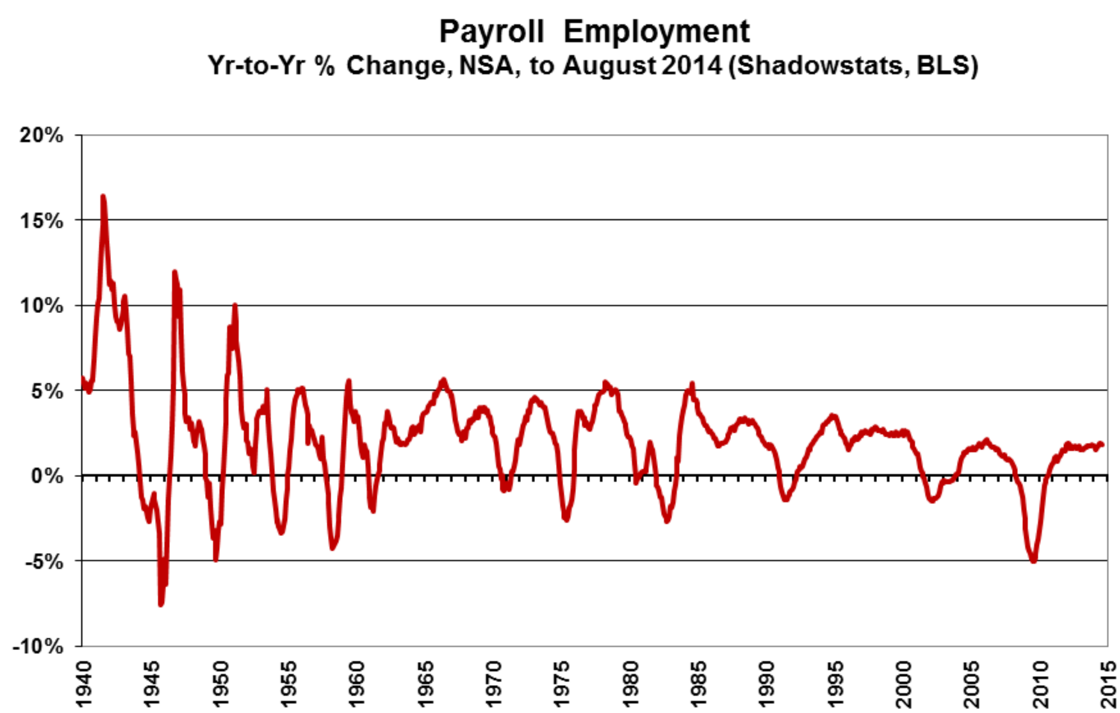
Construction Payrolls. In the context of a revision to July activity, headline August 2014 construction employment rose by 20,000 in the month, following a revised 31,000 (previously 22,000) gain in July, and a revised 8,000 (previously 10,000, initially 6,000) gain in June. Total August 2014 construction jobs still were 21.5% shy of the pre-recession peak for the series in April 2006.



Annual Change in Payrolls. Not-seasonally-adjusted, year-to-year change in payroll employment is untouched by the concurrent-seasonal-adjustment issues, so the monthly comparisons of year-to-year change are reported on a consistent basis, although the redefinition of the series—not the standard benchmarking process—recently boosted reported annual growth in the last year, as discussed and graphed in the benchmark detail of *Commentary No. 598*.

For August 2014, annual growth was 1.84%, versus an unrevised 1.92%—near-term peak annual growth—in July 2014, and an unrevised 1.88% (initially 1.87%) in June. Had the 2013 benchmark revision been standard, not a gimmicked redefinition, year-to-year jobs growth as of August 2014 would have been about 1.5%, consistent with near-term peak annual growth of about 1.9% in February 2012.



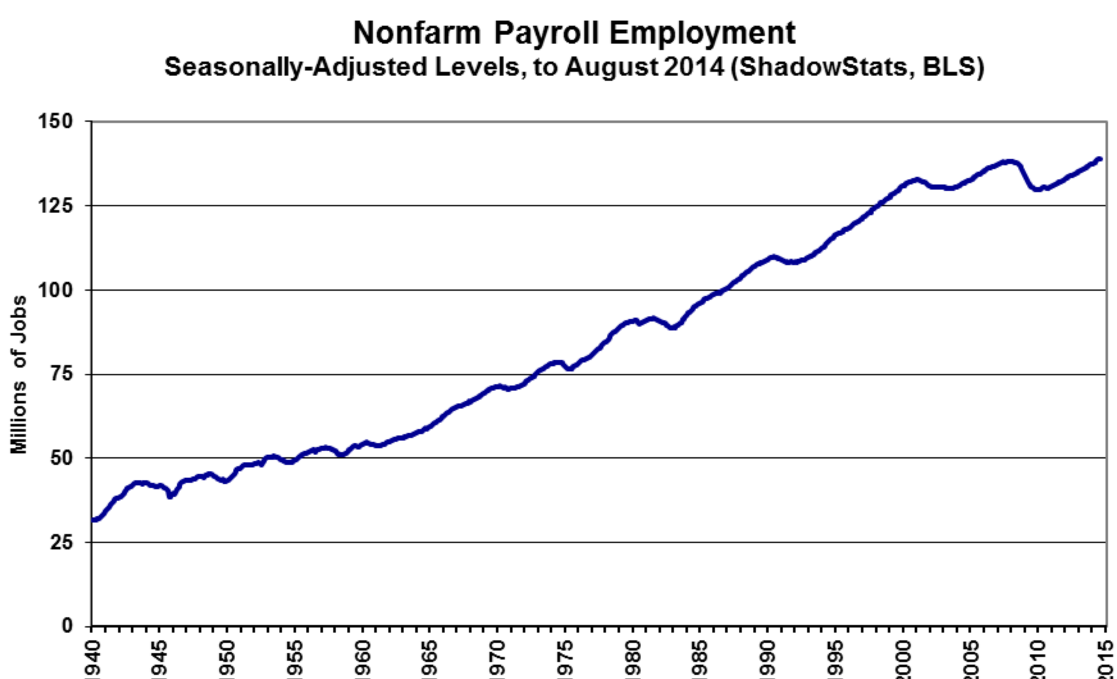


With bottom-bouncing patterns of recent years, current headline annual growth has recovered from the post-World War II record 5.02% decline seen in August 2009, as shown in the accompanying graphs. That 5.02% decline remains the most severe annual contraction since the production shutdown at the end of World War II (a trough of a 7.59% annual contraction in September 1945). Disallowing the post-war shutdown as a normal business cycle, the August 2009 annual decline was the worst since the Great Depression.

Historical Payroll Levels. Headline payroll employment moved to above its pre-recession high in May 2014, and it has continued to rise, although, as discussed in the *Opening Comments*, the number of employed individuals has yet to reach that milestone. The difference is that the payroll survey count reflects the number of jobs, irrespective of how many jobs an individual holds. The household survey count of employment reflects the number of people who are employed, not the number of jobs.

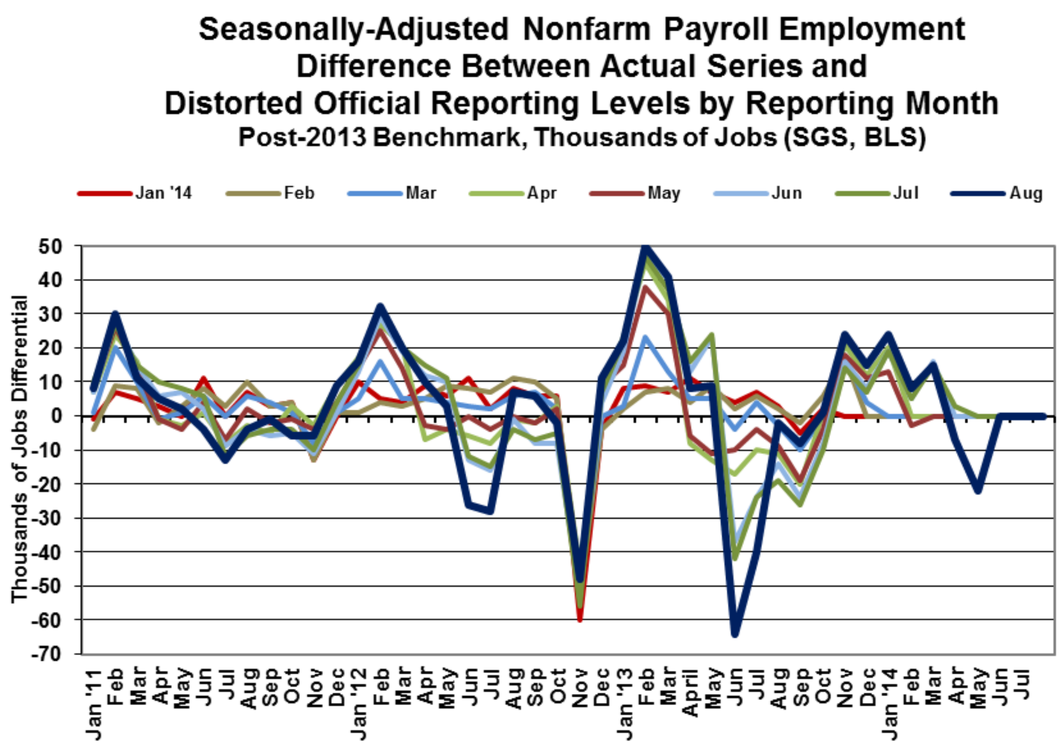
The pattern of recovery in the payroll level count was redefined favorably with the January 2014 benchmarking, despite the actual benchmark having been negative. This can be seen in the shorter-term graph of payroll employment level (again see *Opening Comments*). The yellow points in that graph reflect the ShadowStats assessment of what payroll employment would be showing, with just a regular benchmarking, rather than the gimmicked redefinition of the series, which added a new upside bias. Even with what should have been a standard benchmarking, the pre-recession level likely will be hit in the next month or so.

In perspective, the following longer-term graph of the headline-employment level shows the extreme duration of what had been the official non-recovery in payrolls, the worst such circumstance of the post-Great Depression era.



Concurrent Seasonal Factor Distortions. There are serious and deliberate reporting flaws with the government's seasonally-adjusted, monthly reporting of both employment and unemployment. Each month, the BLS uses a concurrent-seasonal-adjustment process to adjust both the payroll and unemployment data for the latest seasonal patterns. As each series is calculated, the adjustment process also revises the monthly history of each series, recalculating prior reporting for every month, going back five years, on a basis that is consistent with the new seasonal patterns of the headline numbers.

The BLS, however, uses and publishes the current estimate, but it does not publish the revised history, even though it calculates the consistent new data each month. As a result, headline reporting generally is neither consistent with, nor comparable to earlier reporting, and month-to-month comparisons of these popular numbers usually are of no substance, other than for market hyping or political propaganda.



The BLS explains that it avoids publishing consistent, prior-period revisions so as not to "confuse" its data users. No one seems to mind if the published earlier numbers are wrong, particularly if unstable seasonal-adjustment patterns have shifted prior jobs growth or reduced unemployment into current reporting, without any formal indication of the shift from the previously-published historical data. The preceding, accompanying graph shows how far the monthly data have strayed from being consistent, as of the latest August 2014 reporting, versus the most recent benchmark revision to the series. Note the shifting patterns coming into the current reporting, and the sharp upside revision to August 2013, which has an implied parallel in the seasonals for August 2014 (see *Opening Comments*).

Note: Issues with the BLS's concurrent-seasonal-factor adjustments and related inconsistencies in the monthly reporting of the historical time series are discussed and detailed further in the ShadowStats.com posting on May 2, 2012 of Unpublished Payroll Data.

Birth-Death/Bias-Factor Adjustment. Despite the ongoing, general overstatement of monthly payroll employment, the BLS adds in upside monthly biases to the payroll employment numbers, as discussed in the. The continual overstatement is evidenced usually by regular and massive, annual downward benchmark revisions (2011 and 2012, excepted). As discussed in the benchmark detail of *Commentary No. 598*, the regular benchmark revision to March 2013 payroll employment was to the downside by 119,000, where the BLS had overestimated standard payroll employment growth. At the same time, the BLS separately redefined the payroll survey so as to include 466,000 workers who had been in a category not previously counted in payroll employment. The latter event was little more than a gimmicked, upside fudge-factor, used to mask the effects of the regular downside revisions to employment surveying, and likely is the excuse behind the increase in the annual bias factor, where the new category cannot be surveyed easily or regularly by the BLS.

Indeed, particularly unusual here is that despite the BLS modeling having overstated recent jobs creation by 119,000, adjustment to the annual upside biases added into payroll estimation process each month was increased by about 150,000 on an annual basis, instead of being reduced, which would have been expected otherwise (see short-term graph and comments on payroll levels in the *Opening Comments*).

Historically, the upside-bias process was created simply by adding in a monthly "bias factor," so as to prevent the otherwise potential political embarrassment to the BLS of understating monthly jobs growth. The "bias factor" process resulted from such an actual embarrassment, with the underestimation of jobs growth coming out of the 1983 recession. That process eventually was recast as the now infamous Birth-Death Model (BDM), which purportedly models the effects of new business creation versus existing business bankruptcies.

The BLS will publish its estimate for the 2014 benchmark revision on September 18th.

August 2014 Bias. The not-seasonally-adjusted August 2014 bias was a monthly add-factor of plus 102,000, versus what was (post-benchmark) a plus 99,000 bias in August 2013, versus a plus 80,000 add-factor in July 2014. The aggregate upside bias for the trailing twelve months was 740,000, from the pre-benchmark 624,000 twelve-month aggregate as of December 2013, or to a monthly average of 62,000 (52,000 pre-benchmark) jobs created out of thin air, on top of some indeterminable amount of other jobs that are lost in the economy from business closings. Those losses simply are assumed away by the BLS in the BDM, as discussed below.

Problems with the Model. The aggregated upside annual reporting bias in the BDM reflects an ongoing assumption of a net positive jobs creation by new companies versus those going out of business. Such becomes a self-fulfilling system, as the upside biases boost reporting for financial-market and political needs, with relatively good headline data, while often also setting up downside benchmark revisions for the next year, which traditionally are ignored by the media and the politicians. Where the BLS cannot measure meaningfully the impact of jobs loss and jobs creation from employers starting up or going out of business, on a timely basis (within at least five years, if ever), or by changes in household employment that just have been incorporated into the redefined payroll series, such information is guesstimated by the BLS along with the addition of a bias-factor generated by the BDM.

Positive assumptions—commonly built into government statistical reporting and modeling—tend to result in overstated official estimates of general economic growth. Along with these happy guesstimates, there usually are underlying assumptions of perpetual economic growth in most models. Accordingly, the functioning and relevance of those models become impaired during periods of economic downturn, and the current, ongoing downturn has been the most severe—in depth as well as duration—since the Great Depression.

Indeed, historically, the BDM biases have tended to overstate payroll employment levels—to understate employment declines—during recessions. There is a faulty underlying premise here that jobs created by start-up companies in this downturn have more than offset jobs lost by companies going out of business. Recent studies have suggested that there is a net jobs loss, not gain, in this circumstance. So, if a company fails to report its payrolls because it has gone out of business (or has been devastated by a hurricane), the BLS assumes the firm still has its previously-reported employees and adjusts those numbers for the trend in the company's industry.

Further, the presumed net additional "surplus" jobs created by start-up firms are added on to the payroll estimates each month as a special add-factor. These add-factors are set now to add an average of 62,000 jobs per month in the current year. In current reporting, the aggregate average overstatement of employment change easily exceeds 200,000 jobs per month.

HOUSEHOLD SURVEY DETAILS. Generally, the seasonally-adjusted household-survey data are meaningless in terms of month-to-month changes or comparisons. The monthly concurrent-seasonal-factor adjustment process used in generating the headline numbers regenerates all seasonal factors every month, unique to the most-recent month. Yet, the revamped and consistent historical detail is not published, except once per year, in December. All the historical data shift anew with subsequent monthly reporting, but that new consistent detail never is published.

Where, for example, the seasonally-adjusted headline unemployment rate for August 2014 of 6.15% (rounds to 6.1%) was based on a set of seasonal adjustments unique to August 2014, and the adjusted unemployment rate for July was revised along with the August seasonal-adjustment calculations, the new historical and comparable result for July was not, and never will be, published. The prior headline reporting of 6.20% for the July 2014 unemployment rate remained in place, although it now is inconsistent and not comparable with the August 2014 number, even though the consistent July estimation is available internally to the BLS. This is true for every month going back for at least five years of BLS accounting, and it is done deliberately by the BLS, even though the consistent and comparable, historical data are calculated by and known to the Bureau.

Headline Household Employment. The household survey counts the number of people with jobs, as opposed to the payroll survey that counts the number of jobs (including multiple job holders more than once). As covered in the *Opening Comments*, headline employment has yet to recover its pre-recession high.

On a not comparable basis, headline August 2014 employment rose by 16,000, following an unrevised and not comparable 131,000 gain in July. The employment changes were in the context of a decline in unemployment of 80,000 (-80,000) in August, versus a non-comparable 197,000 increase in July. With the headline August labor force declining by 64,000, the bulk of the so-called reduction in unemployment was due to individuals leaving the labor force, as opposed to finding jobs.

Again, though, the reporting here is virtually worthless. The household-survey numbers are highly volatile and unstable, inadequately defined in that they do not reflect common experience, and simply are not comparable on a month-to-month basis.

Headline Unemployment Rates. In the context of the preceding background, the headline August 2014 unemployment (U.3) rate declined by 0.05-percentage point (-0.05%) to 6.15% (again, rounds to 6.1%), versus 6.20% in July.

Technically that was not a statistically-significant change, where the official 95% confidence interval around the monthly change in the headline U.3 rate is +/- 0.23-percentage point. That is absolutely meaningless, however, in the context of the comparative month-to-month reporting-inconsistencies created by the concurrent seasonal factors.

On an unadjusted basis, the unemployment rates are not revised and at least are consistent in reporting methodology. August's unadjusted U.3 unemployment rate declined to 6.3% from 6.5% in July.

U.6 Unemployment Rate. The broadest unemployment rate published by the BLS, U.6 includes accounting for those marginally attached to the labor force (including short-term discouraged workers) and those who are employed part-time for economic reasons (*i.e.*, they cannot find a full-time job).

With a minor seasonally-adjusted decline in people working part-time for economic reasons, and a minor increase in short-term (unadjusted) discouraged workers, headline August 2014 U.6 unemployment declined to 12.0% in August 2014, from 12.2% in July. The unadjusted U.6 declined to 12.0% in August from 12.6% in July.

Discouraged Workers. The count of short-term discouraged workers (never seasonally-adjusted) rose to 775,000 in August, up from 741,000 in July, from 676,000 in June 2014, and 697,000 in May 2014. The current, official discouraged-worker number reflected the flow of the unemployed—increasingly giving up looking for work—leaving the headline U.3 unemployment category and being rolled into the U.6 measure as short-term "discouraged workers," net of those moving from short-term discouraged-worker status into the netherworld of long-term discouraged-worker status. It is the long-term discouraged-worker category that defines the ShadowStats-Alternate Unemployment Measure. There appears to be a relatively heavy, continuing rollover from the short-term to the long-term category, with the ShadowStats measure encompassing U.6 and the short-term discouraged workers, plus the long-term discouraged workers.

In 1994, "discouraged workers"—those who had given up looking for a job because there were no jobs to be had—were redefined so as to be counted only if they had been "discouraged" for less than a year. This time qualification defined away a large number of long-term discouraged workers. The remaining short-term discouraged workers (those discouraged less than a year) were included in U.6.

ShadowStats-Alternate Unemployment Rate. Adding back into the total unemployed and labor force the ShadowStats estimate of the growing ranks of excluded, long-term discouraged workers, broad unemployment—more in line with common experience, as estimated by the ShadowStats-Alternate Unemployment Measure—held at 23.2% in August and July, versus 23.1% in June, and at 23.2% for the prior five months. That still was down minimally from 23.4% in October 2013, which was the series high (back to 1994). The ShadowStats estimate reflects the increasing toll of unemployed leaving the headline labor force. Where the ShadowStats-Alternate estimate generally is built on top of the official U.6

reporting, it tends to follow its relative monthly movements and its annual revisions. Accordingly, the alternate measure often will suffer some of the same seasonal-adjustment woes that afflict the base series, including underlying annual revisions.

[The remaining text in this Household Survey *section is unchanged from the* Commentary *covering the July 2014 labor data.]* As seen in the usual graph of the various unemployment measures (in the *Opening Comments*), there continues to be a noticeable divergence in the ShadowStats series versus U.6, and the ShadowStats series and U.6 versus U.3. The reason for this is that U.6, again, only includes discouraged workers who have been discouraged for less than a year. As the discouraged-worker status ages, those that go beyond one year fall off the government counting, even as new workers enter "discouraged" status. A similar pattern of U.3 unemployed becoming "discouraged" and moving into the U.6 category also accounts for the early divergence between the U.6 and U.3 categories.

With the continual rollover, the flow of headline workers continues into the short-term discouraged workers category (U.6), and from U.6 into long-term discouraged worker status (a ShadowStats measure). There was a lag in this happening as those having difficulty during the early months of the economic collapse, first moved into short-term discouraged status, and then, a year later into long–term discouraged status, hence the lack of earlier divergence between the series. The movement of the discouraged unemployed out of the headline labor force has been accelerating. While there is attrition in long-term discouraged numbers, there is no set cut off where the long-term discouraged workers cease to exist. See the *Alternate Data* tab for historical detail.

Generally, where the U.6 largely encompasses U.3, the ShadowStats measure encompasses U.6. To the extent that the decline in U.3 reflects unemployed moving into U.6, or the decline in U.6 reflects short-term discouraged workers moving into the ShadowStats number, the ShadowStats number continues to encompass all the unemployed, irrespective of the series from which they otherwise may have been ejected.

Two further related graphs, also found in the *Opening Comments* section, are of the ShadowStats-Alternate Unemployment Measure, with an inverted scale, the employment-to-population ratio, which has a high correlation with the inverted ShadowStats measure.

Great Depression Comparisons. As discussed in the regular *Commentaries* covering the monthly unemployment circumstance, an unemployment rate above 23% might raise questions in terms of a comparison with the purported peak unemployment in the Great Depression (1933) of 25%. Hard estimates of the ShadowStats series are difficult to generate on a regular monthly basis before 1994, given the reporting inconsistencies created by the BLS when it revamped unemployment reporting at that time. Nonetheless, as best estimated, the current ShadowStats level likely is about as bad as the peak actual unemployment seen in the 1973-to-1975 recession and in the double-dip recession of the early-1980s.

The Great Depression unemployment rate of 25% was estimated well after the fact, with 27% of those employed working on farms. Today, less than 2% of the employed work on farms. Accordingly, a better measure for comparison with the ShadowStats number would be the Great Depression peak in the nonfarm unemployment rate in 1933 of roughly 34% to 35%.

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 Trends. 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 strong bounce-back estimated by the Bureau of Economic Analysis (BEA) for headline second-quarter GDP still should face some downside revision, with a likely GDP contraction eventually seen 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:

Retail Sales (August 2014). The Census Bureau has scheduled the release of August 2014 retail sales for Friday, September 12th. As discussed in the *Opening Comments* to yesterday's September 4th *Commentary No. 654*, the consumer remains in an extreme liquidity bind. Accordingly, odds continue to favor ongoing weak headline retail sales reporting, which not only should continue to disappoint market expectations, regularly, but also should be negative, net of inflation, in the August reporting. That said, market consensus already appears to be around "unchanged" for the headline nominal monthly activity.

August CPI-U (due for publication on September 17th) will determine the level of inflation-adjusted, or real, retail sales for the month. The headline CPI-U likely should be weak, but on the plus-side for August, placing some minimal downside pressure on real retail sales reporting. A month-to-month contraction in inflation-adjusted August retail sales significantly would increase the chances of an outright third-quarter 2014 contraction both in real sales and in real GDP.

Separately, watch out for downside revisions to prior-period reporting.

