BUILDING WEALTH IN CHANGING TIMES

The Solari Report

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The Real Deal on Inflation With John Williams

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C. Austin Fitts: Ladies and gentlemen, welcome to The Solari Report. It's my privilege to welcome back a guest who really needs no introduction, and that is John Williams, head of Shadowstats. You can find him at www.Shadowstats.com. For those of you who have been long-time subscribers, you know that I am a long-time subscriber to Shadowstats. It is one of my core sources of information. Whenever I'm puzzled, in particular about what is going on in the economy, I go to John's website just to sort out what is really happening in the data.

John was a very successful economist, consulting with many major corporations. One day a friend of his asked him to write a series of articles about the quality of government statistics. He had been noticing and tracking that the government statistics were diverging from reality. So, the statistical official reality and the truth were splitting, just like it was in all other aspects of our life.

John decided to write a series of articles about the differences. It was so popular that it exploded into an entirely new line of business and the website. 'Shadow Government Statistics' is what Shadowstats stands for.

John really gets into the nuts and bolts of what is happening inside the economy and trying to express it with mathematical numbers that make sense of a lot of things. It can really help you sort out tracking the economy. Again, it's at www.Shadowstats.com.

John, welcome back to The Solari Report.

John Williams: Thank you for having me.

Fitts: Our production team meets twice a week on the Round-Up. I was questioning what was really happening, and we were puzzling. Our producer said, "Maybe it's time to get John Williams back."

So that is the ultimate compliment. He is the guru who can help you figure out what is really going on.

One of the things that you've been tracking for a long time is the dangers and risks of inflation. So why don't we start there and talk about what you have been writing and saying about inflation over the last couple of years? Bring us to the current situation.

Williams: Inflation probably is a key number that is distorting the system and, among other things, it is driving some very unusual things in the way of activity of the Federal Reserve.

The concept of measuring inflation and measuring the cost of living has been around for centuries. They had consumer price indexes back a couple of hundred years ago that were, in many ways, like they were going into the 1980's.

What people did was put together an index based on a group of products constantly measured over time, and inflation was measured the way people viewed it, and, effectively, it was measuring the cost of maintaining a constant standard of living.

You take a fixed basket of goods. Very crudely, let's say that it's a gallon of gas, a pound of beef, and a loaf of bread. You would price that basket of goods out one year, and then you would price it out the next year. However much the price of that basket changed, that was your rate of inflation; that was how much the cost of living had gone up, and that was how much minimally you needed to have your income go up to maintain your lifestyle.

That was always useful information for people, and something like that was a way that people began targeting wage increases and the government began targeting some of its programs like the cost of living adjustments to social security.

In the 1980's, people in the government and very clever economists figured that you really could get away with understating inflation in terms of the average person, and thus save money for the government. There are a couple of other benefits that I will get into, but there are two basic areas. The first one had to do with quality adjustment. This was in the 1980's. Adjusting prices for quality adjustment under product is perfectly legitimate. The problem is if the consumer recognizes a quality change, it ends up with a change in prices that were lowering inflation the way it was worked, whereas the consumer doesn't recognize the change that is being made.

An early example of government-mandated reformulation of gasoline was to improve air quality. At the time, that added $0.10 per gallon to the cost of gasoline, which was quite a bit, yet the government didn't add it into the CPI because it was deemed a 'quality' improvement.

So, the average person when filling their tank of gas was not saying, "Oh boy! Oh boy! I'm going to have better air quality!" Instead he was 'moaning and groaning' that it was costing him an extra $0.10 a gallon to fill his gas tank before he went to work.

There actually was some furor over that, and they eventually backed off that particular measure, but there is a whole genre of changes that were made with, what they call, 'hedonic quality adjustments'. This is where they had computers estimate what kind of quality improvement the consumer was enjoying, even though the consumer might not recognize that quality improvement.

I'll give you another example. I am a very simple person technology-wise. I had a computer that I used for my writing and number crunching and not much more than that. I decided that I would replace it after ten years. It had cost me $1,000, and I replaced it at a cost of $1,000. As far as I was concerned, prices had been unchanged for computers.

There were many things that had been done to computers in that timeframe. Now you can watch a movie on your computer, but I never used it for that and I never recognized that as a use for anything that I was paying for, but the government did.

As the government modeled it, according to all of the changes that they made to the prices of computers, I should have been able to buy my computer for $50, but it still cost me $1,000 and only $50 went into the CPI.

They do something like that to give people a reasonable measure, and the idea here is to give people a reasonable measure of their cost of living. So, if you have a big technological change, you just define it as a new product, bring it in as a new product, and you work the other one out of the system or you reduce it, waning over time.

In the 1990's, suddenly there was a big to-do. Alan Greenspan got involved, and Newt Gingrich got involved. There was a mistake in the CPI, and the way that Greenspan explained it was that there was a 'nary of substitution'. He said that if steaks get too expensive, people will buy more chicken or more hamburger instead. So, they're not going to be spending as much money, but the CPI doesn't reflect that.

Of course, it doesn't because the way that the CPI had been designed was to maintain a constant standard of living. As far as I'm concerned, if you have to eat chicken because your steak is getting too expensive, then you are not maintaining the same constant standard of living. But if you use the substitution error and say, "This is something to eat," you can reduce the level of the CPI with that.

So, the government passed legislation to change this CPI and came up with a new measure called the 'Chained CPI', which was just recently tacked onto the tax bill. It officially reduces inflation – at least as it used to be viewed – and is designed to, basically, boost people into higher tax brackets without their knowing what is happening.

The other element, which hasn't been tagged on yet to the cost of living adjustments for social security – but that was one of the major reasons for changing it – was they didn't address the way they calculated the CPI. They went from actually measuring what was happening to, what they called, geometric weighting. So, they mathematically – and did in fact – lower the inflation measurement.

The effect is that you get lower cost of living adjustments. The average person on social security will tell you that he or she is not seeing a real compensation for what has changed in their cost of living when they get the cost of living adjustment to social security. That is deliberate on behalf of the government. Frankly, I think it is criminal. It's effectively a tax increase, and certainly boosting people into another tax bracket is a tax increase.

So, be honest and call it a tax increase. Don't try to gimmick things and penalize people just because they are living on a cost of living adjustment.

Putting that aside, there are two other things that came out of this. One, if you are the government reporting its economic numbers, you usually report the numbers 'net of inflation'. You look at the 'Gross Domestic Product', which is the broadest measure of the economy, that is reported 'net of inflation'. If you are taking something that is a nominal term before inflation adjustment and adjust it for inflation, and if you understate the inflation, you are going to end up overstating the inflation adjusted growth.

If you look at what has happened with the GDP, right now they are understating inflation on the GDP by about two percentage points, which basically wipes out all the headline growth that you have seen in the GDP since the 'Great Recession', as it is now being called.

There are all sorts of games that are being played there. The government just published its estimate of real median household income, and that is also inflation-adjusted. God bless the Census Bureau. They are the only people I know who use this measure, but they were behind pushing the development of, what they call, the 'CPI-U-RS' as being a research series. In the research series they are saying, "We know that the numbers have been changed over time. Suppose that we wanted to do economic research and restate economic history so that the CPI was consistent over time, so that all the CPIs that we used in the past are consistent with the way we report it today. What would it be?"

So, they generated this new series that restates inflation back in time as though they had all the gimmicks in place today. When I saw that, I reverse engineered it, and said, "What happens if you reverse all the gimmicks that they have been putting in, and you report inflation the way that it used to be?"

The difference that it makes is when the government's estimating headline is, "CPI inflation year to year of about 3%," and I have it at about 10%. That is where it would be today if they hadn't made all these changes in terms of substitution and quality adjustment.

Fitts: It's very interesting that you said 10%. I follow something called the 'Chapwood Index'. I don't know if you've ever looked at it.

Williams: I've seen the Chapwood Index, and it's independently estimated, but we came up with something that is reasonably close with them.

Fitts: They came up with the same number.

Williams: I actually talked with Ed Butowsky who puts that together, but we didn't know that we were doing the same thing before we talked with each other.

Fitts: What is interesting is that he says it is 8-13% in the US, and if you look at the midpoint of that, which is 10-11%, that is what I have found. I travel a great deal and talk to subscribers all over the world, and that is what I am finding. An 8-12% - or about 10-11% - is dead on and that is what you say.

It is very frustrating if you are running a household budget, and are watching the news saying that it is 2-3% when you are just absolutely getting squeezed.

Williams: And then you have the Fed saying, "Inflation is too low."

We have all sorts of unusual things going on here, and I contend that we had really massive incompetence (I think that is a mild way of putting it) and probably outright fraud. Even the central bank had some knowledge that lead to this near banking collapse in 2008.

I was involved with looking at some ratings at that time, and I saw some of the things that happened. I know some of the people involved in different elements, and there is no way that was not in the cards. It was predictable, and what happened was, effectively, the banking system collapsed. It never has really come back to normal. I will contend that we are still in the state of recovery or stasis from it. That is why the Fed is having all sorts of problems today trying to get things back to normal.

What they did was absolutely extraordinary. It wasn't only the Fed; it was the Federal government as well. They did everything they had to do to bail out the system. They bailed out large corporations like General Motors. The Federal Reserve purchased AIG, the world's largest insurance company. Of course, they were insuring these derivative instruments that were collapsing the banking system.

The Fed bought $5 trillion worth of treasuries and bad debt from the banks. Now, had the Fed wanted to stimulate the economy, had they wanted to create inflation, had they wanted to see an economic recovery, they would have let the banks lend some of that cash back into the system.

The Fed buying up treasuries is the way they used to control the money supply. They would buy treasuries from the banks, the banks would have the cash, the banks would then lend the cash out into the commercial and personal loan markets. Those people would get the cash that they deposited with their banks, and those banks would lend out reserve requirements so that, effectively, whatever amount the bank lent out, you could multiply by ten, and that is how much would end up in the money supply.

With this extraordinary amount of asset purchases by the Fed and if the banks put that into the system, you would have had hyperinflation. The system was not stable, and the Fed mandated that the banks would not lend that money, but rather deposit it back with the Fed as excess reserves, and the Fed paid interest to the banks on that money.

Fitts: They stopped inflation and feathered their friends' nests.

Williams: They had all this talk about the quantitative easing and, "We're doing this to stimulate the economy." the Feds said that their intention was to, "Prop the economy and prevent inflation," which was mandated by Congress.

Fitts: I would say that it was to prop certain parts of the economy. I live in a place where I've seen many economies throughout the country fall apart and die on the vine, and there has been no effort to support those. There is demand destruction by destruction of whole sectors of the economy.

We recently published a 2nd Quarter Wrap Up called 'The Rise of the Asian Consumer'. One of the things we looked at is that the Asian economies are converging in terms of per capita income with the US, and the number of people entering the middle class is significant. For the first two decades of globalization, China was exporting deflation with cheap labor; at least Asia was. Now that is reversing, and they are exporting inflation because you have three times the middle class by 2030 in Asia competing with Europe and the US in the developed world for commodities and resources. Now instead of reinvesting in our cheap goods at Walmart, they are reinvesting in Eurasian along the Silk Road and in Africa, etc.

The deflation export machine is turning into an inflation export machine. I think that is one of the reasons we saw Trump starting the trade war with China. I would like to know whether you see that influence when you look at the inflation numbers.

Williams: The biggest issue in inflation – and I'm talking in terms of what actually gets reported in the CPI – is that the CPI has all sorts of dampers on it, but many of the underlying factors are in there, to a certain extent, proportionally.

Actually, it has been tied to oil and gasoline. That has been the dominant factor, and the US oil industry is expanding. That is one bright area of the economy, but the oil prices and the volatility that you see there has been driving our headline inflation. Much of that is global in its scope, and it has nothing to do with the domestic demand.

What we are seeing with our headline inflation is that we have been through a very weak period of time in the economy, and I will contend that we have never really fully recovered from the downturn. In fact, if you look at the industries, such as the housing construction market, that is down anywhere from 10-15% from where it was in 2007. We just haven't recovered that level of activity.

If you look at the manufacturing sector, some of the numbers are actually bloated a bit by the headline low inflation numbers, and you are still down by 5% from recovering pre-peak activity back in 2007. The interesting thing with the manufacturing sector and the industrial production of what you are manufacturing is recorded as the biggest component.

The history in that series goes back to the end of World War I. We have a full century of data, and the way that the economy is looked at, you have a peak – which is obvious by what is said, and most people view it as 'peak activity' – and then as the activity falls off, that is a recession if it's a trough. Then it starts to move higher, and that is recovery. It is recovery until you hit the prior peak level. Once you move beyond that prior peak, then you are in an economic expansion.

If you look at the headline GDP, which is heavily gimmicked by these low inflation numbers, it is up 17.5% in recovery. It's around 22% off the trough, but it's expanded beyond it's pre-recession peak by 17.5%. However, there is nothing that shows that, which makes it absolutely not believable.

The strongest series that you see is retail sales, but that is deflated by the headline CPI. So that is about an 8% recovery, but that disappears if you put in realistic numbers.

The economy is not booming as advertised. It may be better than it was, but it is a circumstance which is not really healthy for consumers because their income isn't growing.

You look at the headline numbers, and it gets worse when you start adjusting for accurate inflation. If you look at the headline numbers, for example, and real earnings that get reported with the Consumer Price Index Bureau of Labor statistics, it is flat. We've had three years with negative quarters.

Fitts: The tax reform, and the capital repatriation, and the military expenditure budget increase are all a significant amount of, what I would call, 'economic steroids'.

Williams: Yes, and it would be nice if it flowed through to the consumer. God bless corporate America – you need corporate America for things to eventually turn around – but a lot of what has happened here is that much of the productive element of the US economy has been shipped offshore. I think that is what Trump is trying to move back.

Fitts: Is there any indication in the manufacturing statistics that there is any movement to insource capacity back into the US?

Williams: Not yet. But where we have seen a positive move has been in the petroleum production area. That is blooming ahead, and that is above where we were pre-recession. That has actually pushed aggregate industrial production as reported. Aggregate industrial production has recovered by a full 2% above its pre-recession peak.

Fitts: What I'm seeing is tremendous interest within the military-industrial complex to not be dependent on Asia. They want self-sufficiency within North America on critical industries. I'm seeing a considerable number of signs of insourcing, but if it's not showing up in the statistics, then maybe it's not really happening.

Williams: We are off bottom there, and I think increasingly that is going to be the case. I think that is where the movement is, and you need to do something like that in order to get the domestic manufacturing back up and to get the production jobs up.

I also look at the employment/unemployment numbers, and the big problem here is that many people lost jobs as the manufacturing base was transferred overseas by enough to significantly impact the higher quality production, high-paying jobs.

There are all sorts of reasons people would look to produce offshore. Costs are one reason. Worker's compensation and all the laws that affect your costs with labor and production often can be mitigated by going offshore. That is something that the American people have to be willing to address as to whether or not they are willing to lose part of the productive base in the United States in order to get these cheap products with countries that don't abide by the same standards that we do pertaining to regulations, and safety standards, and pollution standards, and such.

I think that is beyond the scope of what we are looking at here. However, I can tell you that the end of the line reality ends and that the economy has not fully recovered against where it was in 2007. It is growing now, but we have many things to be stabilized here. The Trump Administration has been moving in that area, and the trade one is a big one.

Much of the costs in inflation will be tied to the currency. There you've had recently a very strong dollar, but, basically, I think we have a much weaker dollar ahead. You have all sorts of games that are being played here by the Fed. The problem with the Fed is that they are unstable. They are talking about it, and they want to get interest rates higher. Interest rates now are still artificially low.

Normally are set on top of inflation. If you are going to lend money, you want to get back a greater return on your money than the rate of inflation.

It used to be that you could estimate where rates were going to be based on how inflation was doing. Well, the inflation numbers are nonsense right now. Even as reported, the treasuries in most instances are giving a negative real return.

Fitts: _If your inflation is 10% and your income growth is 1-2%, and the yield on your treasuries is 1-2% and your expenses are rising 10% a year. That is what I call the slow burn, and that is what we have been doing for quite a while now.

Interest rates have been rising a little, and the Fed tightening. I don't know if you looked at the latest statistics on US debt and the interest expense, but the interest expense is accelerated and compounding the additions to the debt by a very significant number.

Williams: That is to be expected because the debt has expanded quite a bit and the Fed has been behind a fair amount.

It's not a stable circumstance. I will contend that what the Fed has done here and everything it has had to do to keep the banking system afloat was its primary concern, not getting the domestic economy back in any sense of normal functioning. If they could do that, it would be fine, but you look at the banks, and they are still not lending normally.

People still have problems getting mortgages. The banks have been liquefied, but until they are functioning normally and lending normally, I'm not quite sure what it's going to take to get it going.

Fitts: I think their way of minimizing is to keep the excess liquidity circulating to the insiders and keeping it away from the outsiders. So, if you could shut off lending and equity investment on Main Street, and Main Street is starved for capital, then you can husband it all for the corporations.

I think that you are talking about, basically, channeling all the capital in the system to the big corporations and also trying to channel the market share to the corporations. The more market shares the big companies can take away from the little companies, the more contributions flow into the politicians, and around and around we go.

I've done a great deal of work over the last 20 years on the money disappearing from the Federal government. I call it the 'missing money' but it is undocumentable adjustments, and the Federal government has refused since 1998 to comply with the laws related to audits or publishing financial statements. It has blatantly broken the law as related to financial management in both the Constitution and the financial management legislation.

We have now created whole websites documenting all the laws broken and all the money missing. We now have, from fiscal 1998 to 2015, government documents supporting over $21 trillion of undocumentable adjustments, which I submit.

I have no idea what the real number is, but I think that trillions are really spent and missing.

Williams: I think you are right on the mark there. The Treasury publishes an annual statement that is prepared by the General Accounting Office, or what is now the Government Accountability Office.

If you look at those numbers, they do an audit, and the auditors won't give any opinion, or they will tell you why they won't give an opinion.

Fitts: I'm not sure if you know this, but the Federal Accounting Standards Board just came out with a policy that would allow the Department of Defense to not include classified projects in their audit. If you look at the wording, it is very cleverly done.

They came out with a press release at the time and made the statement, "If we don't do this, then we would have to redact the entire DOD financial statements, which means that we would have to redact the entire US government's financial statements."

Williams: I was not aware of that. I can tell you the last financial statement that I saw – and it's a thing that dooms the system – is they do estimate the net present value of unfunded liabilities, and there are all sorts of assumptions you can make on that. Generally, if you take the present value of the unfunded liabilities of the government tied to things such as Medicare and social security and its current bonds, you are looking at $100 trillion needed in today's money to cover the obligations the government has already taken on.

There is just no way they can possibly do that.

What that does is eventually gives us a worthless currency – a hyperinflation, so to speak. I don't care what they do with the reporting, but you're not going to be able to buy much with it.

Fitts: If you look at the rise in the debt expense; I wonder if part of the trade war with China is not a hyperinflation fear. If China continues to compete directly for capital and resources and export inflation instead of deflation, then the US cannot handle the inflation that is going to result.

Williams: I think that is a fair point. You have a circumstance that is something that needs a reorganization of the government and the entitlement programs. If it's not addressed soon, we will have a crisis much sooner than later. Things are going to blow apart, and I think you are going to end up in that hyperinflationary financial crisis.

Fitts: Let's talk about how that happens because what we are talking about is a situation where the world is not going to be buying US treasury securities and dollars, and they are less likely to take dollars. So, the Fed is going to have to, essentially, be the bank, printing them, and so you get into debasement of the value of the dollars they print. The debasement accelerates, and what that means is the trade deficit skyrockets.

To a certain extent, that could be what is happening with the trade deficit now.

Williams: It will reflect, to get to the bottom line, is that the US dollar will have no real purchasing power for those who are living in a world dominated in US dollars.

When Standard & Poor's downgraded the treasuries about ten years ago, the ex-Fed chairman, Greenspan, made the very salient point, "Well, the debt that the US owes is in dollars, and we can spend as many dollars as we want with no chance of defaulting."

That is true from that standpoint. Debasing a currency with hyperinflation is generally not an event of default in the treasury securities, but hyperinflation does give you worthless currency . That's what he is promising and where we are headed.

If you are looking to turn the situation around, I would have approached things a little differently than President Trump coming into the office – claiming economic victory on day one. He didn't have a corporate Congress, which is a problem that might get addressed some in this upcoming election.

Fitts: If you were the President, what else would you do to try to turn this around?

Williams: I contend that Trump got elected and surprised all the pundits because Main Street USA voted for him. Main Street USA is feeling the economic pain that we are discussing here. You can play around with it in the press and have all sorts of happy news to report, but if people don't believe it-the reason they don't believe it is because they're not experiencing it- they will vote for change. That is what happened.

With that kind of an entrée, this is something that can still be done. You address the country and say, "We all know there is a major problem here. We are financially bankrupt as things currently stand. We need to do something to address the problem today to have a future for our children. It may require some financial pain on the part of all of us to bring this into the balance, but if we can come up with a way of structuring our long-term fiscal condition so that the United States is solvent, so that the US Treasury is solvent, then we will have the strongest currency in the world, we can bring a lot of investment into the United States, and we can stabilize the dollar."

If you can get the currency markets to buy and the US long-term is stable, then the dollar will be fundamentally strong.

Fitts: You would need something in the United States where the general population – particularly the middle class – trusts the leadership. I would say that the leadership trust is extremely low.

Certainly in the heartland, the election improved the sense of trust. Small business in the heartland feels much more trustworthy, and that is what the surveys and polls say. But I would say that if you look at the productivity statistics, productivity is not growing, and I can tell you why it's not growing. I run a small business, and the cost of compliance with regulations is out of control.

I have two companies and one company had an audit. If you look at the methodology they use for costing out the price of an audit that is dictated by the SEC, the cost of the audit was more than my total revenues for the year.

If you look at what I spend on regulatory tax, compliance, legal, and litigation, I would say that 50% or more of my overhead goes into that office, the SEC That is because there is a war on small business led by government.

Every time the bad guys steal, they load up more regulatory requirements on the honest guys – as if that is some kind of solution, and it's not.

Productivity is going down in this country, and it's going down because of the economic warfare. I believe it is totally intentional, and it is meant to destroy productivity. The way that you protect against inflation is cycle the money to the insiders, but then you drown the outsiders with so much regulatory burden, and surveillance, and suppression. They are spending all day complying with Paperwork Reduction Act requirements.

Williams: It's difficult to argue with you there. With the overwhelming paperwork that the average business has to put up with just to comply with all the regulations and the like, I think that is one thing that resulted in the change in direction in the presidency as far as the public is concerned.

Fitts: Absolutely.

Williams: President Trump has done paramount work where he can do things by executive order and such. It's difficult when the Congress doesn't cooperate and you have a system here that has been working to push its system one way for so long and it is so embedded in that direction.

It is truly an extraordinary political circumstance. I've never seen anything quite like this.

Fitts: What you are doing is channeling the process to the big guys. There are thousands of different ways of doing it, and it is highly complex. But when you add it all up, it is moving all the earnings into the big guys and popping it in the stock market and leveraging it with derivatives. It generates lots of money for a variety of players and it's an inside game.

The problem is that it is stripping the real economy, and it is stripping the vitality and the diversity of the economy.

I don't know how closely you follow the stock market, but in 2017 Jeremy Grantham threw in the towel and he basically said that monopolies are being engineered politically, and it's not economic and it doesn't reflect market economies; it's an engineered centrally-controlled economy. When Jeremy Grantham throws in the towel and says that, you know it's bad.

Williams: There is one fallacy in that broad thinking, and that is you still need a consumer to drive the economy.

Fitts: Absolutely! Henry Ford knew that if his workers couldn't buy cars, it wasn't going to work.

Williams: That is what they are doing now and what the Fed is doing now. They are squeezing the consumer, and it's going to be self-defeating. We are headed for a great crisis here.

The Fed has allowed that it can come back in and do some more quantitative easing if the economy softens – not that they want to stimulate the economy. It means that if the economy turns down, which I think it is doing, it is going to stress the earnings of the banks again. They will use the quantitative easing to keep the banks afloat.

Frankly, I think that they should have let the banks collapse in 2008 and reorganize the system.

The Fed was behind a lot of what happened there. If you read the literature out of the Fed at the time, they were encouraging all these wonderful derivative instruments that would enable the banks to share in the risks of the insurance industry, and the insurance industry to share in the risks of the banks, and they did.

Fitts: I have a different take on this because I was the Assistant Secretary of Housing and then Lead Financial Advisor to HUD. The mortgage securities fraud was absolutely massive, and it was engineered top-down by the Fed and the New York Fed member banks. They all knew, and it was absolutely engineered.

What they did was issued, what I would say was $20+ trillion in fraudulent securities, and then they stuck the bill to the taxpayer, which meant that somebody got off with a large amount of money free and clear.

I would say that it was a bank robbery, and the banks came out with a much bigger market share. The market share of the banks that engineered that is now much bigger, they have much more of the Federal credit to use, and they are fat and happy.

Williams: You can only be fat and happy for so long if the instrument that you are milking continues to provide only a little milk.

Fitts: They were always planning to replace the US consumer with the gold consumer, and I think that is why they are so angry about China closing out the American companies because it's not quite working. I think that is what 'Make America Great Again' is. We need more earnings in our home base.

Williams: That we do.

Fitts: John, you've been very generous with your time. Over the next six months, if people can have the time to watch three indicators – including on your website – what should they keep an eye on to follow inflation and know how the economy is doing?

Williams: Right now, I would look at the two weak elements that are very difficult to have weak and have a strong economy: One is manufacturing, and the other is construction and the housing industry. If the construction and housing continue as they are and are down 50% from where they were in 2007, and are not rebounding, and are beginning to flatten out and turn down, and manufacturing is beginning to turn down again, you're going into a nosedive in the broad economic activity.

They puff up the numbers with some newly created things – not that the concepts are new, but putting them into the GDP, such as intellectual property.

You add $1 billion to the economy by taping the Olympics and Korea. That is now a new intellectual property. That actually was in the trade deficit – intellectual property. I'm sure they're going to watch that again.

Fitts: This is why we have to maintain our state of amusement.

You can find John Williams at www.Shadowstats.com and can subscribe. There is a great deal of information for free at www.Shadowstats.com. Check out the website and the subscription is very reasonable for what you get.

This is a man who can make sense out of the puzzle palace of government statistics and all the economic statistics. You make it remarkably easy for us non-economists to follow and see what is happening. It's a great website, and I just want to tell you that I am a loyal subscriber. I am going to be with you as long as you are willing to do this.

I want to thank you.

Williams: I thank you, Catherine, and I follow your material and greatly enjoy it.

Fitts: Have a great day.

Williams: Same to you.

MODIFICATION

Transcripts are not always verbatim. Modifications are sometimes made to improve clarity, usefulness and readability, while staying true to the original intent.

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