



## Episode 1,762: No, Consumer Spending Isn't What Drives the Economy

Guest: Mark Skousen

**WOODS:** I want to talk about a couple things, in particular, one that's been associated with your name for quite some time, and a recent development relating to it, and that is the concept of gross output. Now listen, folks. You stay tuned to this episode. Don't think it's technical economics, and therefore, it's not for you. No, it is for you, because this is how you understand what's really happening in the economy, as opposed to the superficial view you might get from let's just say other more frequently used figures. So let's start off with gross output. I think I like Steve Forbes' analogy, where he compares GDP to an X-ray and the gross output figure to a CAT scan.

**SKOUSEN:** Yeah, I like that as well. It's just a colorful metaphor. Another fellow of mine, a friend of mine who's a private economist, his name is Jerry Bauer, he makes a comparison, GDP is the flat land and gross output is the sphere, so you get that three-dimensional look. I prefer something that financial economists and the financial media understand really well, and that is, in financial statements, we have a top line and a bottom line. The top line is sales and revenue, and the bottom line is profits or net income. And no analyst on Wall Street would be worth his salt if he didn't look at both, because you can't have profits over the long term without revenue, and revenue is never sufficient to guarantee profits. So you need to look at both and see which direction they're headed.

And it turns out that economists have only looked at the bottom line for years with GDP. GDP measures spending at the final stage, and that is the consumer stage where business and consumers and government are buying finished goods and services. That's what GDP measures, and it's about \$21 trillion. But what they leave out is the entire supply chain, the goods in process, the intermediate goods from the earliest stage – you could use the example of producing a Starbucks coffee. GDP just measures the value of the final cup of coffee that you're drinking, but it does not measure at all the coffee beans, the crushing, the movement of the production process to the finished good. All of that is left out. The supply chain is completely left out of GDP.

So it creates a lot of misunderstandings, and one of the major misunderstandings is that, since consumer spending as a percent of GDP is like 70% of GDP, so everybody goes to this conclusion that consumer spending is the big elephant in the room, that that's what drives the economy, and if consumers don't spend, then we're in terrible trouble. And they kind of ignore the business sector and what's happening in the supply chain. So what gross output does, because it measures spending at all stages of production and includes the supply chain, then you get a much broader, balanced picture and you see that business spending is actually larger than consumer spending. It's almost double what consumer spending is. So you get a

very different picture of the economy, and you start focusing now on what business is doing rather than what the consumer is doing.

So that's kind of the bottom line of this gross output statistic, which I've been arguing that we need to add this top line to national income accounting ever since I wrote my book *The Structure of Production*, which is an Austrian theme, since 1990.

**WOODS:** One thing that impressed me is that somebody now whose name I've forgotten who comments on stuff like this made what is more or less the standard observation that consumer spending drives the economy. And you hear this over and over. The consumer is key. And you very patiently wrote and said, well, I think you're under a misconception here, and then you explain the concept of gross output. And he realized he had been in error and adopted your view. And I thought, I just can't believe that in this day and age, there's anybody left like this, who looks at the data and looks at the arguments and says, you know what? Maybe I was an error, and I will adopt this correct view. So congratulations. I mean, unfortunately, I'm so upset by everything going on in the world these days that I'm just downright nasty to people. I really have to keep an eye on that and be more like Mark Skousen, because you really attracted someone through honey rather than through vinegar on that one.

**SKOUSEN:** Yeah, and the person who wrote that is a macro economist with the Oxford Club. Matthew Benjamin is his name. And it was very comforting to see that there was someone who was listening to a rational argument that I made, that consumer spending is not the key factor. And the key factor is business. Business spending is much larger. It's like two-thirds of the economy, while consumer spending is really about a third of the economy. And actually, when you look at the employment factors, about 80% of people who are employed are in the intermediate supply-side stages of the economy, working in manufacturing and resources, in wholesale, rather than the retail markets. Retail sales represent only about 20% of employment.

So when you realize there's a lot of these – another factor which I'll mention is the ten leading indicators that the Conference Board puts out. Almost every one of them are in the earlier stages of production, in manufacturing and the stock market and financing and that sort of thing. And consumer confidence is one of the leading indicators, but it's only one out of ten. So it does give you a sense that things are not what they seem.

And the big problem, the real reason why my friend Matthew Benjamin made this mistake is because we just had GDP. That was the only measure of the economy that anybody cares about, and we say that represents total economic output of the economy. People are very loose with these terms. But if they've ever taken a class in econ 101, they know that GDP deliberately leaves out all the intermediate stages and just focuses on the final output, the final goods and services, the finished products that people use, and it ignores all this business spending. It's like going into the grocery store and only noticing the goods that are there that you buy, and you forget about what's in the back room and the trucking and the shipping and the transportation and the manufacturing and the production process, all the way back to the earliest stages. That's totally ignored, and we can't ignore that to have a proper view, a proper balance in the economy.

**WOODS:** What's been going on with the release of this statistic recently that has caused you to be commenting on it further?

**SKOUSEN:** I've had three *Wall Street Journal* articles on this to get the word out. It's been a very slow process. As I mentioned, I suggested this idea of top line and national income accounting gross output in my book *The Structure of Production*, which is kind of my magnum opus on this subject, which I wrote in 1990 and published by NYU Press. And then I would needle from time to time the Bureau of Economic Analysis, the BEA, which is part of the Commerce Department, and said, you know, you really need to have this top line in there because are misunderstanding what GDP is and the fact that they've left out the supply chain and all the factors, causing people to misunderstand that consumer spending drives the economy, and rather that it's business. And if you're looking at economic growth statistics, all of that shows that consumer spending is the effect, not the cause of prosperity. And technology and entrepreneurship and savings and investment, that's what drives the higher economic growth and a higher standard of living.

So finally in April – I'll never forget this – actually, December of 2013, Steve Landefeld, who was the director of the BEA, he emailed me and he says, well, you'll be happy to know after all these years, we've decided to start releasing on a quarterly basis, just like GDP, we're going to release gross output. So I got my first *Wall Street Journal* editorial in *Forbes* magazine, *Barron's*, *Wall Street Journal*, everybody was writing, including articles that I'd written, about this subject. And so I got considerable publicity. I've been on CNBC with Larry Kudlow, who's a big fan of Rick Santelli. Both of them like this idea of gross output a lot.

But it still is an upward battle, because if you go to the BEA website at BEA.gov, you can look on the opening pages, and you cannot find gross output anywhere. It's not listed. And in fact, when the press release comes out, they list it under GDP by industry. So I get emails all the time saying, "Where is this gross output statistic?" So I really had to pressure the BEA to be more forthright. So I think I've won the battle about halfway there. It's still not being accepted by the media. One of the positive developments is that they're now releasing GO and GDP at the same time, but they're not really linking it together as top line, bottom line, which is what I would like them to do, so that the media will pay attention now to gross output. Because right now, they just don't pay attention to it.

**WOODS:** Well, how can it shed light on what's really going on in the economy? I understand the value of it. I understand that the old view of the consumer being the story we need to tell is incomplete and that I do want to know what businesses are spending money on, on non-consumer goods. But is there any way that that can help in our analysis of where we are in the economy?

**SKOUSEN:** Yeah, and that's where the second part of GO is really valuable. The supply chain tells us so much more about what's happening in the economy. For example, in 2008 during the financial crisis, the supply chain collapsed. I mean, it dropped like five times faster than GDP. And so that really reflected how deep and how bad this recession was and why it required all this massive intervention by the Fed to put Humpty Dumpty back together again. And then the Congress got involved with TARP and so forth. So if you looked at nominal GDP, it only fell about like 2% during the financial crisis of 2008, So it doesn't look like it's a serious problem. But when you look at GO dropping 10%, 15%, you say, oh, my gosh, this is really serious. So that's number one.

And by the way, one of the interesting things that we just looked at, and one reason I wrote this *Wall Street Journal* article on October 3rd is that this time, it was different. This time, gross output fell about the same as GDP. They both fell about 8% in the second quarter. So

you didn't get this collapse, super collapse in the supply chain like you had in 2008. So it's a bit more optimistic, I think, in our analysis and that effect.

So the final thing I will say about this, Tom, is that gross output is a leading indicator. The supply chain is a leading indicator, because it is saying where we're headed, business confidence. What is being produced down the supply chain will end up on what they think is going to happen to consumers. So a lot of my private investors are saying gross output is a leading indicator. It tells you what GDP will do in the next quarter, about three months down the road. So for all these reasons, GO is a valuable new statistic that I'm hoping BEA will start releasing much sooner, because they've had these delays. And I'm not sure – they're rather quiet why it's so difficult to get this gross output statistic out at the same time as GDP when they do their first estimate, which is coming out at the end of October. But it's just taking them a while.

So my hope is that they will recognize GO as the top line and release it at the same time as GDP and put it on the front page, just like publicly traded companies put on their – when they release their financial statement, they release the top line and bottom line, sales and profits at the same time. We need to do the same thing with national income accounting. And then I will say I've achieved my goal, and it's 20 years and counting, but we're coming closer and closer to everyone realizing GO and GDP is a great way – and by the way, it's getting into the textbooks as well. So it's a long, hard process. There's the old saying that science progresses one funeral at a time, and I'm hoping that in my lifetime, I'll be able to see this goal achieved.

**WOODS:** Now, let's bring this up to the present day. In what way can this concept help us make sense of exactly what's happening in the economy right now? Obviously, you have commentators – because we're going to very – I hate to use the word *unprecedented* because it's so overused, but really economically, this is an unprecedented situation, because outside of wartime, I can't think of cases where huge sectors of the economy have been shut down or restricted in this way. And everybody's trying to understand what the numbers mean and what's happening. What kind of light, if any, can GO shed on that?

**SKOUSEN:** I think it's really important that GO – now again, understand that they just released second quarter GO, so while we don't know what's happening in the third quarter, which was just finished, we'll know what we see with GDP – if you look at GDP now that's put out by the Atlanta Fed, it shows a dramatic recovery about equal to the collapse. And that suggests to me that this was all artificial, that the lockdown was artificial, that it was unnecessary, and that we can recover. And yes, restaurants and entertainment and travel and all this sort of thing has collapsed, but they can come back just as fast.

And the gross output statistic I think is going to say that, because in the second quarter, like I said, the supply chain did not collapse three or four times faster than GDP, which is what it did in 2008. That gives me a sense of optimism that it's going to be fairly easy to turn this around and get a V-shaped recovery in the economy. Now, as long as they keep imposing these lockdown restrictions on travel and leisure and sporting events and concerts and entertainment and restaurants and education, as well, rather than getting back to what it used to be like, then we're going to have a U-shaped recovery rather than a V-shaped recovery, is the way I look at it.

**WOODS:** Now, I want to go back in time a bit because of something you've sent me and I was not aware of. I was aware of, of course, Black Monday, October 19th, I guess 1987, when there was a stock market crash, a very severe one. And apparently, you – and you have not done this in the 33 years since, but three weeks beforehand, you sent out a notice to your newsletter subscribers. Talk about that.

**SKOUSEN:** Yeah, and before I do, let me just mention, going back to gross output, I do have a website that people can go to called GrossOutput.com, which will give everybody the latest press releases, my *Wall Street Journal* articles, and so forth. On that subject on the Black Monday crash of October 19th, 1987, you know, it's something that is in the distant past for most people, but for me, it was very telling because I celebrated my 40th birthday on that day. So every time October 19th comes up, people send me an email and refer to me as the crash baby. And I did actually six weeks – not three, but six weeks prior to the crash, I did send out an alert to all my subscribers to sell all stocks.

Now, I have not done this before or since for a couple of reasons. One is that I found it panicked people so much that they never got back in, even though the bottom was achieved in the stock market the very next day. The market recovered. Subsequent to that time, when you have sell-offs like that, we've had nothing since there that is equivalent to a 22% decline – that would be like a 6000 drop in the Dow. And so I have argued that for a number of reasons, a sell-all, get-out-of-everything doesn't make sense.

Number one reason is when people do that, they have a hard time getting back in. I know people who never got back in the stock market after that, and never got back into the market after the 2000 collapse in the NASDAQ stocks or 2008 when the stock market fell 55%. People get so rattled by this that they never get back in, and so they miss out on the bull markets. And we've had primarily bull markets, not bear markets since the '87 crash.

The second thing is the government is extremely fast in responding to these crashes and these bear markets. When the economy is tanking, they engage in rapid, aggressive, anti-inflation monetary and fiscal policies, and they're spending money – just like now, spending money like crazy, running deficits, the Fed lowering interest rates to zero, buying up all kinds of assets. And when they're doing that, the crash is avoided. You can get a 5% decline in a day, but you're not going to get 22% because the government's too willing to intervene.

So those are the reasons why – I mean, they haven't outlawed bear markets. We are going to have bear markets. But I think a 22% decline in one day is highly unlikely anymore.

**WOODS:** I'm just thinking, though, given – so in other words, looking back at 1987, do you think you did the – well, apart from the problem of spooking people, do you think that was the correct call strategically?

**SKOUSEN:** Well, actually, looking back, of course, I was somewhat young as far as inexperienced. I had been writing my newsletters since 1980, so this was in my eighth year. I'm now in my 40th year. And looking back on this, it probably was a mistake, because if I had held people's hand during the crisis, and said, listen, this was just a short-term, unexpected crash due to computer-generated trades and irrational exuberance, if you will, to use Alan Greenspan's term, we would have been fine. We should have stayed in it. So it was an important lesson for me, and especially since it took me like a year before I got back in.

So even as an investment advisor, yes, I can say I called the crash, but equally I could say I failed in getting people back in at the bottom. So my attitude has really changed. I've become more conservative, if you will. I never give a sell signal for everything. We use stop orders and stuff like that to build a cash position, but we never give an all-out sell signal, because I've found that it's too disruptive to people's psyche and their psychology, because once you get into a large cash position, then you're constantly worried, well, am I missing out on something? When do I get back in? It's just difficult to manage a portfolio where you're 100% in or 100% out. Some people try to do it, but I don't think people feel comfortable with that strategy.

**WOODS:** I feel like, given that the election is coming up in less than two weeks now, it would be wrong of me to have you on and not – well, as a matter of fact, when this airs, it'll be a week from tomorrow – and not ask you for your assessment of Trump in terms of the economy. Now, I think, of all the presidents we've had in our lifetimes, he's the trickiest one to assess. Because I think he's the least ideological in some ways. Maybe I'm looking at this superficially, but what overall would you say if you had to summarize it?

**SKOUSEN:** Well, if it wasn't for this pandemic, the so-called pandemic of 2020, he would be reelected probably in a landslide, because it's all about the economy, as Bill Clinton pointed out, and the economy was doing really well. Unemployment was at extremely low levels. Unemployment among blacks and minorities, at the lowest level in 30 or 40 years. Largely a deregulatory environment. The tax cuts were very beneficial, especially for business with the corporate tax rate down to 21%. Inviting lots of businesses to return to America. I think overall, it was a real – I'd give him a very high grade. If you just kind of ignore the Twitters and this undiplomatic and unpresidential statements that Trump makes, I think if you just look at policies and kind of ignore his rhetoric, it all made sense.

Now, I'm not a fan of his fair trade, protectionist views, but I do think it was valuable to go after China for intellectual property rights violations. But to say NAFTA was the worst trade deal ever is just nonsense. All the evidence is overwhelming that it was beneficial to both sides. So I think that's a checkered record.

But 2020, no president has ever won reelection in the midst of a great recession. I mean, we're still facing some real serious problems due to this lockdown. So I'm in the camp that thinks it's more against Trump than pro-Joe Biden. Look, it's possible that he pulls a rabbit out of the hat like he did in 2016 and wins reelection, but there's a lot of Republicans who aren't going to vote for him this time that voted for him in 2016. Election betting odds are predicting over a 60% chance that Biden wins and only 37% for Trump. However, recall that in 2016, election betting odds had 80% chance that that Hillary Clinton would win and only 20% chance that Trump would win, and Trump ended up winning. So we have to look at the voting in the battleground states. And there, it's still fairly close, but I was skeptical of Trump winning in 2016, and I'm even more skeptical that he'll win in 2020.

The biggest fear that we all have is that the Democrats will sweep and take over all three branches of government. And if that's the case, that's when they push through the bad agenda. When Obama had control of both houses and was the president, what did he do? He passed Obamacare. He passed Dodd-Frank, and both of these are disastrous as far as regulatory control of the government and healthcare. So if the Democrats get in, together they're going to push through tax increases. He's no friend of investors. He wants to eliminate the long-term capital gains rate, meaning that the rate will go from 23.9% to over 40%, maybe

even 50%. I mean, he has to get all of this stuff through Congress, but it still sounds to me like a disaster if, in fact, the Democrats end up controlling everything. And that will change our portfolio. I mean, even this year, we've had to focus on gold and silver and technology stocks and play down our income stocks, because they still haven't recovered.

**WOODS:** Well, we're just going to have to see. Of course, we're going to see pretty darn soon exactly what happens. I think if maybe – it's hard to know, because what I keep saying and I have been saying for at least a couple of years is that Trump, you know, he barely won. Several of the key states he barely won by razor-thin margin. So it was going to be difficult to pull that off a second time anyway. He's got every possible power center against him, but the key thing is, I don't think he's done enough to build beyond his base during the four years. And I think he needed to do that in order to have any chance to win. And so I'm not saying it's impossible for him to win, because you never know with this guy, but I don't think he's succeeded in doing that.

And moreover, I think if he had had a clearer and frankly more combative position on reopening the country, where he armed himself not just with a lot of tweets, but with ten Scott Atlases and sent them all over the country and did media blitzes and did press conferences with the to make clear that there's perfectly respectable scientific opinion that says Fauci's full of it, you know, I think that he'd be in better condition.

**SKOUSEN:** Yeah, I agree with you. And things have changed since 2016. We are in recession. People don't like this kind of uncertainty. They're not sure about the leadership that Trump has had. You also have this mail-in voting. It's like a third of the people have already voted, and that's after seeing the first presidential debate where Trump was embarrassingly – I mean, he didn't smile, he was insulting people right and left. He may have had the virus at that point, but you do have that problem with the mail-in order. And you also have a lot of Republicans, he keeps insulting his own senators and congressmen and stuff, and I just have some real problems with that kind of approach.

So I know there's a number of people that are going to have events right after the election. We're having one in person, as a matter of fact, on November 6th and 7th in Las Vegas, if people are interested in joining us for that. If they go to FreedomFest.com, they can get some details on that meeting. It's going to be a private meeting. It's going to be off the record, and John Fund is going to be one of our speakers, so it'll be pretty interesting.

**WOODS:** Okay, absolutely, so we'll encourage people to check that out. Is that *Wall Street Journal* article, the one that you sent me, the most recent one – is that viewable without a subscription?

**SKOUSEN:** Yes, and people can read that if they go to GrossOutput.com. I just reprinted the entire article, because otherwise you have to subscribe in order to read it.

**WOODS:** All right, I'll make sure and link to that at TomWoods.com/1762, our show notes page for today. All right, well, again, congratulations on the triumph of gross output. And for people who are paying attention, it will help them understand better what's going on and not be tied up with this very superficial view that it's just dollars leaving the consumers' hands and going into retail shops that account for everything. So very, very important. So thanks for your time, Mark, and I look forward to seeing you again soon.

**SKOUSEN:** All right, Tom, thank you.