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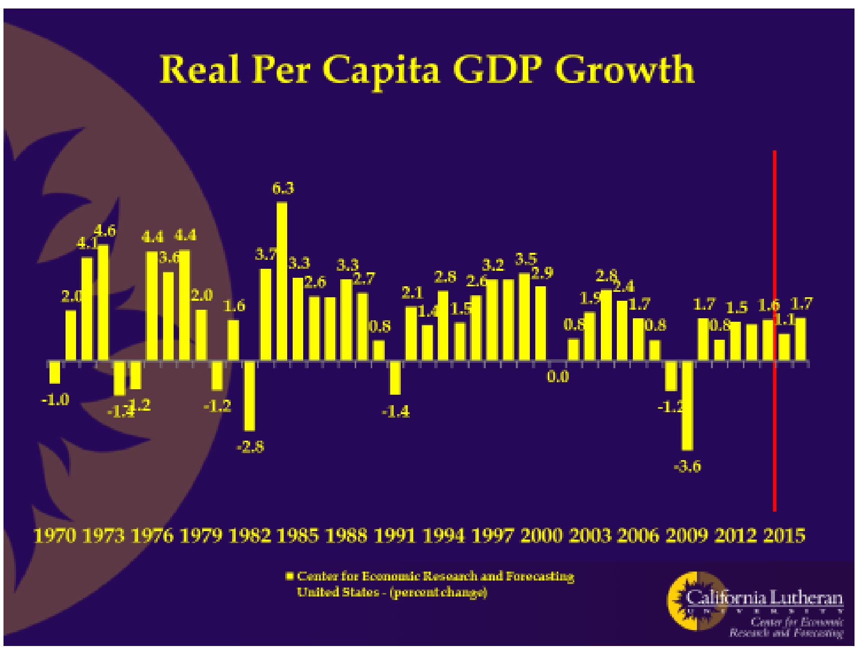
Our forecast had become more optimistic after last fall's oil price decline. Since then, we've seen worse outcomes than preceded the decline. Our forecast errors were large for us. In our United States Economy essay, we discuss why the oil price decline may not have generated the growth we hoped for.

Our new forecast incorporates the dismal winter data, and it's pretty typical of our post-recession forecasts. We expect to see economic growth, but that growth is likely to be slow compared to pre-recession norms.

We would like people to start thinking in terms of Per-Capita GDP growth rather than the traditional GDP growth. As population growth slows, and becomes negative in increasing numbers of countries, GDP growth increasingly becomes a case of comparing apples to oranges. This is because GDP growth includes a population growth component that Per-Capita GDP growth does not include.

The long-run United States GDP annual growth rate is about 3.25 percent, depending on the period used for the calculation. The long-run Per-Capita GDP annual growth rate (1929-present) is about 2.3 percent. So, the long-run GDP growth rate includes about one percent population growth.

How are we doing by this measure? Not so well. Since the recession, annual Per-Capita GDP growth rates haven't even approached two percent. We're not likely to do any better within our forecast horizon.



There is some upside risk to the forecast. That is, the forecast could be low because there is still potential for growth because of lower oil prices. The longer oil prices remain low, the more likely they are to generate gains. Recent jobs data give us a tad bit of hope that this is the case, but monthly data are volatile. So, we shouldn't read too much into it.

Some have claimed that lower oil prices could not generate growth. Their thinking goes like this: Lower oil prices mean less investment in oil wells and infrastructure. Therefore growth will slow.

There is a negative impact from reduced investment in oil infrastructure, but that is smaller than the upside potential from the consumer side. Lower prices for oil are better than a tax cut, because oil price cuts don't carry the implied debt accumulation that tax cuts often imply.

There is also downside risk. That is, the economy could perform significantly worse than our forecast. Europe remains a mess and China is slowing. Recent productivity data also provide reasons for concern. See our United States Economy for more discussion.

If we do slip into recession, it could be tough going.

Central banks across the world have resorted to quantitative easing, to little apparent good, and short-term interest rates are already at zero and even going negative in some countries. In a zero-rate world awash in cash, I see no way for central banks to effectively respond to a recession.

Fiscal authorities, already burdened with high debt levels, also have few effective tools. They'll bail out companies they consider too big to fail, and they'll run up debt in various stimulation projects. For the most part, these will mostly be ineffective in the short run, and detrimental in the long run.

Fiscal and monetary authorities should be working on reversing the extremes that they created in response to the 2007 recession. Fiscal authorities need to reduce their extreme debt. Monetary authorities need to move into solidly positive interest rates while soaking up some of the huge amounts of cash in the economy.

Everyone should be working to eliminate the too-big-to-fail issue. As it is, companies that believe they are too big to fail have increasing incentives to leverage themselves as the economy becomes riskier.

In the meantime, we hope that low oil prices provide a much needed stimulus.

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