Briefs

Ag Economy

World Macroeconomic Growth Positive But Slow

The world economy is now in a gradual recovery driven by U.S. and Asian growth. Despite the Japanese and German recessions, world growth is expected to be about 2 percent in 2002, up modestly from 1.4 percent in 2001. Growth in North America and parts of Asia is accelerating, with Central Europe and the former Soviet Union holding their own. Growth in Europe, Japan, and Latin America is below recent performance and likely to remain that way for the rest of the year. Given a slow world recovery, the dollar will stay strong, oil prices will moderate, and U.S. interest rates will remain low.

Energy Prices Stable

Without a rapid pickup in world and domestic manufacturing, crude oil prices should be stable. The recent surge in crude oil prices, while partly due to production cutbacks, was largely due to strong U.S. and Asian growth. However, oil prices are likely to stabilize or even drop as the usual summer increase in demand for gasoline is met by a drawdown from very high crude oil inventory levels accumulated this winter. The slow manufacturing recovery will keep world industrial fuel demand growth modest. West Texas crude oil prices in 2002 are expected to average $26 per barrel, about the same as in 2001.

U.S. natural gas prices will be lower than winter of 2000/01 levels. Wholesale natural gas prices, which reached over $9 per million British Thermal Unit (Btu) in December 2000, dropped to $2.26 per million Btu by January 2002—largely due to an unseasonably warm winter and a sharp drop in manufacturing output. Although natural gas prices have risen since January, substantial increases in natural gas prices are not expected until late 2002 or early 2003, when world industrial output returns to the 1999 peak. As a result, the average natural gas wholesale price in 2002 is forecast at about $2.85 per million Btu (based on the U.S. Energy Information Administration's commercial natural gas price forecast of April 2002), well below the $3.96 per million Btu average of 2001.

Productivity Up Sharply

The current U.S. economic recovery and recent recession may be the most remarkable since systematic tracking of business cycles began. Federal income tax cuts and increased Federal Government spending coincided with weakness in the economy and aided the overall recovery. In addition, labor productivity rose at an annualized rate of 8.6 percent in the first quarter of 2002—more than triple the trend rate since the end of World War II, and the highest quarterly productivity growth rate in 20 years. Rarely does productivity pick up so sharply in the first quarter of a recovery. However, productivity continued rising throughout 2001, despite the recession. Favorable productivity growth reduced concerns about increased general inflation in 2002, as even relatively large wage increases would not cause substantial inflationary pressure.

Farm Household Impacts Minimal

Although the economic news is generally good, the outlook for farm households remains unchanged. Stable and lower farm input costs are not expected to offset the effects of a strong dollar and limited export growth. Off-farm employment, which is largely generated by the manufacturing sector, is not expected to rebound sharply during 2002.

Increases in the price of manufactured farm inputs in the second half of 2002 should be minimal as the prices of fertilizer and farm chemicals will fall due to declining natural gas prices relative to 2001. Stabilizing fuel and electricity prices reflect stable crude oil and lower natural gas prices. As general inflation is expected to be low, increases in other nonfarm input prices should be modest.

New off-farm rural jobs are likely to be relatively scarce, as recovery in U.S. job markets historically lags recovery in the overall economy. The recovery's high recent labor productivity growth makes slow employment growth even more likely for 2002. Further, since rural employment is disproportionately concentrated in the manufacturing sector, expected slow growth in manufacturing output due to the strong dollar and modest world growth weakens rural job growth prospects. Strength in the dollar, despite small recent weakening, puts downward pressure on farm prices and farm export growth, partly offsetting benefits of lower input costs and exacerbating weakness in off-farm employment.

Indicators To Watch

Prospects for faster world growth depend on strong economic recoveries in Europe and Latin America, even as Japan stagnates. The consensus among major international forecasters is for no improvement in growth until 2003. Most forecasts show continuing strength for the dollar, with a minority expecting a weaker dollar in 2003 or 2004.

The European Union (EU) may require a lowering of short-term interest rates to boost private spending enough to stimulate a full recovery. If German manufactured exports and industrial production surge, the EU will rapidly recover without further stimulus. Latin America, suffering modestly from weakness in Argentina, needs either a surge in foreign direct investment or rapid growth in exports to move back to normal growth. AO

David Torgerson (202) 694-5334
dtorg@ers.usda.gov