



Texas Manufacturing Outlook Survey

Special Questions

April 30, 2018

Texas Business Outlook Surveys

Results below include responses from participants of all three surveys: Texas Manufacturing Outlook Survey (TMOS), Texas Service Sector Outlook Survey (TSSOS) and Texas Retail Outlook Survey (TROS).

Data were collected April 17–25, and 371 Texas business executives responded to the surveys.

The first two questions refer to the federal tax reform bill passed in December 2017.

1. What impact do you expect tax reform to have on your firm's tax bill in 2018?

| | April '18 (percent) |
|-----------------------|------------------------|
| Significant reduction | 25.1 |
| Slight reduction | 33.7 |
| No impact | 29.1 |
| Increase | 3.2 |
| Don't know | 8.9 |

2. What actions have your firm taken in response to tax reform that you weren't otherwise planning to do, if any? Please select all that apply.

| | April '18 (percent) |
|--|------------------------|
| None | 56.4 |
| Increase capital expenditures | 18.9 |
| Increase employees' wages | 16.4 |
| Increase employees' other compensation (e.g. bonuses, benefits, stock) | 14.8 |
| Pay down debt/increase savings | 13.4 |
| Shift planned capital expenditures forward | 9.6 |
| Increase hiring | 7.7 |
| Other | 5.5 |

3. What is the net impact on your firm of the newly announced tariffs and other potential changes to trade policy?

| | April '18 (percent) |
|------------|--------------------------------|
| No impact | 37.3 |
| Positive | 5.1 |
| Negative | 35.1 |
| Don't know | 22.4 |

4. Are your firm's revenues directly linked to the energy industry?

| | April '18 (percent) |
|---------------|--------------------------------|
| Yes, strongly | 16.3 |
| Yes, slightly | 32.9 |
| No | 50.8 |

Texas Manufacturing Outlook Survey

Data were collected April 17–25, and 107 Texas manufacturers responded to the surveys.

The first two questions refer to the federal tax reform bill passed in December 2017.

1. What impact do you expect tax reform to have on your firm's tax bill in 2018?

| | April '18 (percent) |
|-----------------------|--------------------------------|
| Significant reduction | 29.0 |
| Slight reduction | 30.8 |
| No impact | 27.1 |
| Increase | 1.9 |
| Don't know | 11.2 |

2. What actions have your firm taken in response to tax reform that you weren't otherwise planning to do, if any? Please select all that apply.

| | April '18 (percent) |
|--|--------------------------------|
| None | 53.3 |
| Increase capital expenditures | 20.6 |
| Increase employees' wages | 20.6 |
| Pay down debt/increase savings | 18.7 |
| Increase employees' other compensation (e.g. bonuses, benefits, stock) | 17.8 |
| Shift planned capital expenditures forward | 12.1 |
| Increase hiring | 10.3 |
| Other | 2.8 |

3. What is the net impact on your firm of the newly announced tariffs and other potential changes to trade policy?

| | April '18 (percent) |
|------------|--------------------------------|
| No impact | 17.8 |
| Positive | 9.3 |
| Negative | 52.3 |
| Don't know | 20.6 |

4. Are your firm's revenues directly linked to the energy industry?

| | April '18 (percent) |
|---------------|--------------------------------|
| Yes, strongly | 23.4 |
| Yes, slightly | 32.7 |
| No | 43.9 |

Special Questions Comments

These comments have been edited for publication.

Impact of the Tax Reform Bill

Chemical Manufacturing

- We see the new tax laws as a loss due to higher professional fees required to navigate and no real savings. We are a limited liability corporation and have thought about reorganizing but held off since we may divest in a few years.

Nonmetallic Mineral Product Manufacturing

- Tax reform did not reduce taxes for our partnership due to high individual rates, plus the Affordable Care Act tax still exceeds 40 percent.

Fabricated Metal Product Manufacturing

- We are a Subchapter S corporation, so there has been no impact other than withholding for employees has decreased.
- We are doing our best to continue down the same path we had been on prior to tax reform.
- We have a Sept. 30 year-end. We will receive no benefit until our fiscal year starting Oct. 1, 2018.

Machinery Manufacturing

- It will be beneficial to families, but unless or until our product value increases, it will have no impact on us.
- Our business prospects have greatly improved.
- With the significant losses we had in 2015–2016, we don't see our tax bill as a major influence on our business decisions.
- It's too early to tell about the effect of tax reform.
- We will be debt free for the first time in six years. Our business will have doubled over that time and tripled the number of employees, with higher wages and benefits.

Computer and Electronic Product Manufacturing

- We are seeing significantly improved customer confidence.

Transportation Equipment Manufacturing

- We are a debt-free company. We are directing increased cash as result of tax reform toward capital expenditures for future growth and hiring more skills in data analytics and industrial automation.

Paper Manufacturing

- We are Subchapter S corporation that had the domestic production deduction, but that is going away, to be replaced by the up-to-20 percent deduction. The offset reduces taxes by 5 percent. Although nice, it's not enough to move the needle—nothing like the C corporation reduction.

Impact of Newly Announced Tariffs and Other Changes to Trade Policy

Chemical Manufacturing

- Our hypothesis is that the tariffs will both harm and help our business, but it is difficult to predict which will have greater impact.
- President Trump is correct to confront China. We have tried to enter China with our goods for years, but high tariffs make us uncompetitive in that market.

Primary Metal Manufacturing

- An aluminum shortage is developing because of Russian sanctions.
- Much higher prices and out-of-stock situations are occurring. H-13 tool steel may disappear due to sanctions and/or go up in price.
- We make steel and steel products. The steel portion of our business appears that it will enjoy large, but temporary, margin increases. The steel products that we make will likely see more imported competition. On balance, we expect improved margins until our end markets adjust their buying to find ways to minimize the higher prices.

Fabricated Metal Product Manufacturing

- It's too early to tell the effect.
- The price for steel other than carbon has gone up and become short term.
- Steel profitability for the steel supply chain (from manufacturing through distribution and fabrication) will be impacted.
- As a manufacturing company, we see that raw goods such as aluminum, steel, etc., have increased to counter tariffs—not good.
- Even if the import product price has not been increased at this point, domestic manufacturers are increasing prices. We are already seeing these price increases.
- I am with the president on fighting for equal trade, but it has been difficult to manage as we are in the metal manufacturing business. We will see how it turns out when it is all settled.
- We experienced significant losses on fixed-price contracts due to substantial steel price increases that followed the tariff announcements. These losses are more than any tax savings we will realize this year. The overall effect is a negative thus far.
- It's too soon to feel the impact to customers.
- The impact has been immediate increases in steel pricing and welding supplies.
- We are still trying to understand the impact on our business and whether or not it will dampen demand. We manufacture pre-engineered metal buildings. The last few months have been fantastic, but we are concerned about the long-term impact.
- Customers have issues with increasing prices on current contracts, and because of the tariffs (and reminders of past tariffs), steel suppliers have included increase provisions in their contracts to us. Therefore, we have to pass on increases to our customers (contractors). But then they have to pass them on to the customers of the project, which never goes over well, especially for future relationships.

Machinery Manufacturing

- Steel prices have risen 50 percent. We only buy U.S. steel—the tariffs were designed to protect those firms. All they have done is gouge their customers as long as they can get away with it. I expected a modest increase, but nothing like what we are seeing.
- We are seeing much higher metal costs immediately. Companies selling metals took advantage of the tariff announcement to increase prices on all metals—in most cases by 50 percent or more.
- We use steel in all of our products that will cost us more in the marketplace, and we export a large percentage of our products, including to China. We get hit in both directions by this insane trade policy.
- Metals are a major component in our finished product. With an increase in costs, our company will either have to eat the cost or pass it on to our end user.
- The Chinese have not previously been confronted on their anticompetitive practices. The long-term effect of forcing China to play by the rules will be good for U.S. businesses.
- Rising steel prices combined with imported products from China are devastating.
- Metals market indexes all have increased significantly.

Computer and Electronic Product Manufacturing

- We have been warned we may see some increase on cabinets we purchase.
- I believe it is a long-term benefit to the country. Short term, it will cause volatility, pain and a lot of workarounds.

- Rising prices for metals will likely increase the cost of electronic components. Certainly, this will impact any product utilizing metal enclosures.

Transportation Equipment Manufacturing

- The announcement of tariffs already resulted in increased costs on raw materials, even before tariffs took effect, with further increases expected based on communication from suppliers and distributors.
- Our aluminum pricing is skyrocketing. This is one of the primary elements of what we build. We are having to add to prices customers are paying.
- The impact could be negative based on what is known, but it's probably needed to accomplish the greater goal of fair trade and address other issues.

Food Manufacturing

- We import a lot of materials, both raw and semiprocessed.
- Any policy adverse to real free trade is a bad policy, and higher prices will trickle down to everyone.

Nonmetallic Mineral Product Manufacturing

- We purchase mostly domestic steel as a raw material. It will raise costs for everyone in our industry, so it should not impact our competitive position. However, it will raise the cost of infrastructure projects and ultimately lower and delay the number of projects that get funded and built.

Printing and Related Support Activities

- Quite a few materials and supplies come from overseas, and we are already hearing excuses on these pending tariffs as the reason for price increases.
- It has disrupted our supply chain.

Link to Energy Industry

Chemical Manufacturing

- We manufacture high-purity petrochemical solvents.
- The cost to operate our plant is affected by the energy industry. Our raw materials and their costs are directly related to the cost of power, so we would expect changes in the energy industry to affect them. Our products are also used in a small portion of the energy industry.

Nonmetallic Mineral Product Manufacturing

- We provide materials to the oil and gas exploration and drilling sectors, as well as to coal-fired power plants.

Primary Metal Manufacturing

- We buy lots of gas and electricity.

Fabricated Metal Product Manufacturing

- A small portion of our work is industrial work on pipe racks and steel used in the oil and gas industry.
- About one-third of our business is related to the energy industry.

Machinery Manufacturing

- We manufacture the drives (or drive train) used on most drilling rigs.
- Fuel costs are impacting freight expense.
- Seventy-five to 80 percent of our product goes to the oil and gas industry and the remaining to industrial power generation.

- We are directly related to trucking. If fuel prices are low, rates are too low. If prices are high, margins are too low. This directly affects our sales.
- Plastic prices can vary depending on the price of oil.

Transportation Equipment Manufacturing

- We provide product directly to oilfield service companies—we are directly correlated to the rig count and investments in exploration and production activity.
- We are strongly linked because our primary customer base is in Texas and almost all municipalities are heavily tied to energy.

Food Manufacturing

- Local wages are heavily influenced by the energy sector in the region.

Texas Service Sector Outlook Survey

Data were collected April 17–25, and 264 Texas business executives responded to the surveys.

The first two questions refer to the federal tax reform bill passed in December 2017.

1. What impact do you expect tax reform to have on your firm's tax bill in 2018?

| | April '18 (percent) |
|-----------------------|------------------------|
| Significant reduction | 23.5 |
| Slight reduction | 34.8 |
| No impact | 29.9 |
| Increase | 3.8 |
| Don't know | 8.0 |

2. What actions have your firm taken in response to tax reform that you weren't otherwise planning to do, if any? Please select all that apply.

| | April '18 (percent) |
|--|------------------------|
| None | 57.8 |
| Increase capital expenditures | 18.2 |
| Increase employees' wages | 14.7 |
| Increase employees' other compensation (e.g. bonuses, benefits, stock) | 13.6 |
| Pay down debt/increase savings | 11.2 |
| Shift planned capital expenditures forward | 8.5 |
| Increase hiring | 6.6 |
| Other | 6.6 |

3. What is the net impact on your firm of the newly announced tariffs and other potential changes to trade policy?

| | April '18 (percent) |
|------------|------------------------|
| No impact | 45.2 |
| Positive | 3.4 |
| Negative | 28.1 |
| Don't know | 23.2 |

4. Are your firm's revenues directly linked to the energy industry?

| | April '18 (percent) |
|---------------|------------------------|
| Yes, strongly | 13.4 |
| Yes, slightly | 33.0 |
| No | 53.6 |

Special Questions Comments

These comments have been edited for publication.

Impact of the Tax Reform Bill

Data Processing, Hosting and Related Services

- Our firm's decisions for the actions listed above are not driven by a response to tax reform but instead are driven by the market for attracting talent and marketplace competition.

Credit Intermediation and Related Activities

- We are surprised that we are in a unique situation—our U.K. enterprise is profitable and we will now be taxed at 21 percent on its net income even though we are not distributing any funds back to the U.S. Our U.S. operations are in a net operating loss so we don't get any offsetting foreign tax credit for the tax we owe on the U.K. enterprise. So we might actually see an increase in our effective tax rate.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

- We are scared about the increasing deficit and continued growth of entitlements programs.

Insurance Carriers and Related Activities

- Clients have more disposable income for spending and retirement planning.

Rental and Leasing Services

- We are a subchapter S-Corp, so the tax bill did not help us that much. We have discussed extensively changing back to a C-Corp after 30 years of being an S-Corp, but we do not believe the tax laws and rates will remain as they are for long so we have chosen to stay the S-Corp for 2018 and revisit after November.

Professional, Scientific and Technical Services

- Generally, tax reform increases tax bills for service providers such as lawyers and accountants.
- The tax cuts may provide a short-term economic benefit. However, the resulting increased deficits (not including proposed expenditure increases) will ultimately have a bigger and longer-term negative effect on the economy and our business in particular.

Management of Companies and Enterprises

- The tax reform allows us to be more competitive when offering our services since less of our gross margin will be going to pay our tax bill.

Administrative and Support Services

- The tax reform is very positive for employees.
- We are concerned with details in the plan; we are not quite sure where the pitfalls are yet in the details.

Educational Services

- By decreasing the corporate tax rate, our tax-exempt private placement bond became partially "unhedged," which now leaves us exposed to interest rate changes.
- As a nonprofit, the tax reform bill could impact individual donations negatively since the threshold to be able to itemize deductions about doubled from the 2017 level.
- Overall tax reform will affect our business because as economic activity and less regulation take hold, more people from around the country will flock to our state. That will have a positive effect on our business of educating students.

Ambulatory Health Care Services

- We are making two large capital purchases this year rather than one as we'd planned.

Nursing and Residential Care Facilities

- The impacts are unknown at this time; we are a 501(c)3 organization.

Social Assistance

- Wage inflation is causing us to increase wage costs to acquire talent, while we are expecting an increase in performance per man hour.
- As a nonprofit organization, we expect donations to decrease.

Amusement, Gambling and Recreation Industries

- We are a tax-exempt organization. Perhaps we will see an increase in business if our members have more money to spend.

Food Services and Drinking Places

- The deficit increase is bad.

Religious, Grantmaking, Civic, Professional and Similar Organizations

- As a not-for-profit, the tax reform has little effect.

Impact of Newly Announced Tariffs and Other Changes to Trade Policy

Support Activities for Transportation

- Tariff increases in China might bring back some business to Mexico, which would be positive for us. However, we still don't know the extent of NAFTA (North American Free Trade Agreement) changes, which could also negatively and materially impact our business.

Warehousing and Storage

- If these tariffs impact Mexican exports/imports, it would make a negative impact for industry tied to the transportation and logistics world.

Data Processing, Hosting and Related Services

- We only sell our software service domestically.

Credit Intermediation and Related Activities

- At the moment, the biggest concern is the impact on agriculture commodities—primarily beef exports and soybeans.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

- Pricing of our purchased materials (raw and manufactured) is increasing, particularly for chemicals and metals.
- The possible impact on agriculture is a concern.

Funds, Trusts and Other Financial Vehicles

- Impact is indirect in that market values of investments made on behalf of clients have declined. Company revenues are calculated as a percent of those market values, so revenues have declined correspondingly.

Real Estate

- This creates uncertainty for our clients that results in a fall in confidence and willingness to invest.

Professional, Scientific and Technical Services

- Developers are very concerned about rising cost of steel in an economy where labor and supplies for construction are much higher than they were in 2016 or 2015. We have talked to many business owners who say this is going to have a dramatic effect on their profitability. However, it could be temporary and in the long run could boost our economy.

- The noticeable increase in steel prices is having a damping effect on construction.
- The projects we provide designs for rely on significant quantities of steel and aluminum. Some projects may be delayed or canceled due to the increase in construction costs.
- We employ highly skilled programmers on NAFTA work visas.
- Cost increases in building materials will cause some owners to cancel, delay or reduce scope of planned construction projects. The impact will be a reduction in our workload.
- This is likely to have a negative impact on business in Texas, which is not good for our law firm.

Management of Companies and Enterprises

- It is too early to say.

Administrative and Support Services

- We have reduced our import business in significant ways over the last decade in order to focus on domestic manufacturing. However, there are certain products that will be affected in the future, but we cannot determine how much.
- Clients have halted projects, impacting hiring.

Waste Management and Remediation Services

- Our main imports are from Mexico.

Ambulatory Health Care Services

- We could be indirectly affected if the tariffs cause a drop in agricultural exports of grains, beef and dairy as these are all significant revenue producers in our market area.

Hospitals

- This will impact local manufacturing negatively, which will impact jobs—already 31 percent of our adult population is uninsured.

Nursing and Residential Care Facilities

- This will increase costs of construction materials.
- Amusement, Gambling and Recreation Industries
- We are uncertain yet what effect this will have, particularly with the cost of food.

Food Services and Drinking Places

- We had difficulty getting steel for our roof and other repairs.

Religious, Grantmaking, Civic, Professional and Similar Organizations

- The planned tariffs could potentially drive up our operating costs.

Link to Energy Industry

Truck Transportation

- Fuel cost is a large part of our expenses. As the price of fuel goes up or down, so does our bottom line.

Credit Intermediation and Related Activities

- Our region is slightly dependent on oil service companies, and there has been a boost in revenues with renewed activity in the oilfields, primarily the Permian Basin. Trucking activity is booming, and there is a huge demand for qualified truckers.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

- While the energy market is getting stronger, the need for more additional equipment is lagging behind.

Insurance Carriers and Related Activities

- Our link is only in terms of related job growth and housing demand.

Rental and Leasing Services

- The Permian Basin is the hottest oil patch in the industry right now, and it is our hottest market. We cover all of Texas except Corpus and the Valley with 23 locations. However, our labor cost is increasing at a fast pace since we have to compete with oil companies for workers.

Professional, Scientific and Technical Services

- We have diverse clients, so energy is a key focus area, but one of many.
- The construction industry in Texas is still dominated by the energy industry. We are in the building design industry so many if not most of our clients are directly or indirectly related to energy.

Administrative and Support Services

- We have a significant fleet, and the cost of fuel can have a negative impact on expenses.
- If energy industry declines and results in layoffs or higher unemployment, it usually impacts revenues.
- Sixty percent of our revenue is directly linked to the energy industry and companies supporting it.

Ambulatory Health Care Services

- The energy industry is a big employer for most of our market, providing health insurance to its employees. It is also a large revenue source for a significant number of investors who live here.
- We are a provider of outpatient medical imaging services. Our niche is high-quality imaging with subspecialty reads. We compete with hospitals on quality but offer substantial cost savings to patients.

Hospitals

- Our community is very dependent on the energy industry.

Nursing and Residential Care Facilities

- Changes in the energy industry have no direct impact on our revenues but could impact our expenses via higher energy prices.

Social Assistance

- We use a significant amount of fuel to operate our fleet. An increase in fuel cost will lower our net income.

Food Services and Drinking Places

- We have operations in Houston, which means we are a byproduct of the local economy.
- Tourism activity in Texas seems to correlate strongly to employment in the oil and gas sector.

Texas Retail Outlook Survey

Data were collected April 17–25, and 52 Texas retailers responded to the surveys.

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| | April '18 (percent) |
|-----------------------|------------------------|
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| Slight reduction | 38.5 |
| No impact | 17.3 |
| Increase | 3.8 |
| Don't know | 3.8 |

2. What actions have your firm taken in response to tax reform that you weren't otherwise planning to do, if any? Please select all that apply.

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| Don't know | 21.6 |

4. Are your firm's revenues directly linked to the energy industry?

| | April '18 (percent) |
|---------------|------------------------|
| Yes, strongly | 20.0 |
| Yes, slightly | 48.0 |
| No | 32.0 |

Special Questions Comments

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Impact of the Tax Reform Bill

Merchant Wholesalers, Durable Goods

- There will be a minimal impact for us.
- We will not feel the full effects until our next fiscal year.

Motor Vehicle and Parts Dealers

- We expect more CPA work to take advantage of some new allowances.

Building Material and Garden Equipment and Supplies Dealers

- We just converted from a C- to an S-Corp so income flows through to partners who are at a higher tax rate. We do get a 20 percent pass-through on income but are not sure how that will work at this time.
- Corporate tax reduction is considered temporary due to the unsustainable negative impact of the federal deficit. The ensuing uncertainty drives most business and investment decisions to be short term.

Clothing and Clothing Accessories Stores

- We expect that we will report a loss for the year, so taxes will not be a factor.

Nonstore Retailers

- We currently incur tax losses and have net operating losses, so we have no immediate impact from the tax reform.

Impact of Newly Announced Tariffs and Other Changes to Trade Policy

Merchant Wholesalers, Durable Goods

- There will be a very small negative impact.
- We use a lot of steel in our boilers.

Motor Vehicle and Parts Dealers

- We don't have a final plan to determine the effects.
- The automotive retail business is slow to respond to this.

Furniture and Home Furnishing Stores

- Too many large increases with cost of materials may slow down development and construction.

Building Material and Garden Equipment and Supplies Dealers

- We import lumber and plywood items from Canada and China and have seen significant price hikes.
- Trade policy proposals are causing uncertainty and confusion in our industry. There will be a potential negative impact on product costs and innovation.

Clothing and Clothing Accessories Stores

- The impact depends on how our suppliers are impacted and whether they pass along any cost increases.

Nonstore Retailers

- If there are impacts, they are negligible and we are unaware of them. Our supplier pricing typically is set for a year, so we won't likely feel any impact until 2019.

Link to Energy Industry

Merchant Wholesalers, Nondurable Goods

- The Houston division always is affected by the energy industry. If they do well, we do well and vice versa.

Motor Vehicle and Parts Dealers

- We sell products with high fiberglass and aluminum content.
- We have seen more truck sales for energy-related business.

Clothing and Clothing Accessories Stores

- We have over 300 stores located in energy markets.
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Questions regarding the Texas Business Outlook Surveys can be addressed to Emily Kerr at emily.kerr@dal.frb.org.