DALLASFED Economic Update
Regional

Is the Worst Over? Regional Economy Sees Hopeful Signs

June 18, 2015

The Texas economy had a rough start in 2015, with a sharp deceleration in growth from the end of 2014 to the beginning of 2015. Texas job growth expanded at a 0.8 percent annualized rate through April, down from 3.6 percent in 2014. A number of factors played a role in the sudden slowdown, but the decline in energy prices is foremost among them. Other adverse developments include the first-quarter slowdown in the U.S. economy, the strong U.S. dollar (which hurts Texas exports), the West Coast port strike that crippled Pacific trade (with implications for exporters and retailers in the Texas region), and adverse weather slowing construction activity and retail sales.

Compared with the weak first quarter, the regional economy is looking slightly better in the second quarter. An appropriate analogy might be that the dark clouds over the regional economy are breaking up just enough to let some rays of sunlight through. Texas employment ticked up in April, and initial jobless claims declined for the second month in a row as the unemployment rate held steady. Exports moved up strongly in April, helped by the stabilization of energy prices and a slight weakening of the dollar. And although the rig count is still falling, the pace of decline has slowed markedly.

Some forward-looking indicators show promise. The Texas Business Outlook Survey (TBOS) future headline indexes—the Texas Manufacturing Outlook Survey production index and Texas Service Sector Outlook Survey revenue index—improved. The Dallas Fed's Texas Leading Index edged up in April, the first increase since August 2014. The leading index helps generate the employment forecast for the year, which despite improved data, is still coming in below 1 percent growth in 2015.

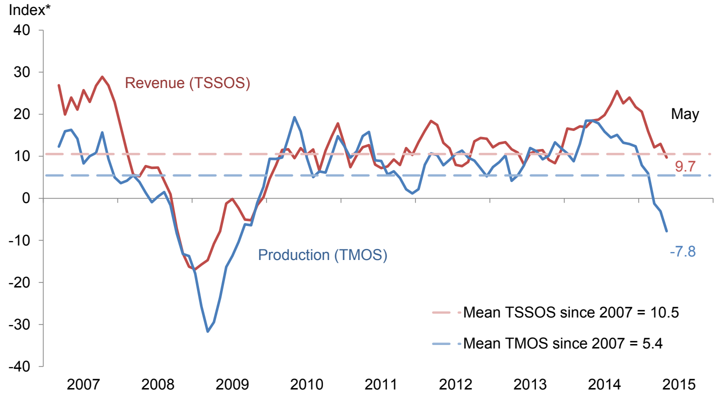
Service Sector Keeps Regional Economy from Sinking

Little timely data are available on state economic output, which is why the TBOS surveys are so important. These monthly surveys of over 350 businesses in Texas provide the most up-to-date information on activity, employment, wages and prices. In May, the TBOS indexes confirmed that service sector revenue continues to expand (albeit at a slower pace), while manufacturing production contracted (*Chart 1*). This is consistent with the energy bust the state has been experiencing. In recent surveys, a significant share of Texas manufacturers have reported being "significantly negatively affected" by the drop in energy prices over the past six months.

Texas Job Growth Resumes—but Not in Houston

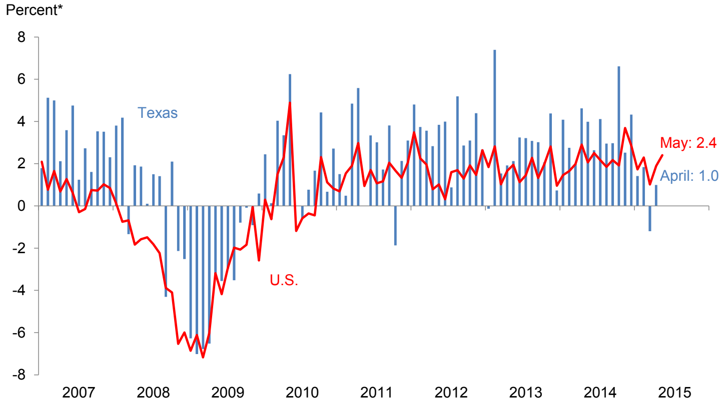
Texas employment growth expanded 1 percent in April after falling 1.2 percent in March (*Chart 2*). March numbers may have been affected by above-average rainfall; wet weather depresses construction, transportation and industries that rely on foot traffic, such as retail.

Chart 1
TBOS Indexes Suggest Services Slowing, Goods Sector Contracting



*Three-month moving average; seasonally adjusted.
SOURCE: Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS) and Texas Service Sector Outlook Survey (TSSOS).

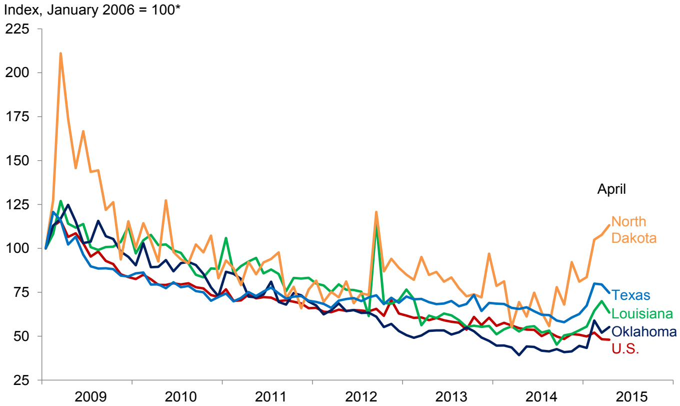
Chart 2
Texas Employment Up Slightly in April After March Dip



*Month over month; seasonally adjusted, annualized rate.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal adjustments by the Federal Reserve Bank of Dallas.

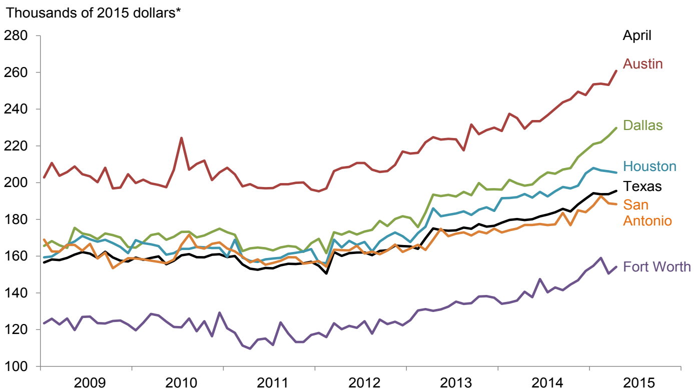
The effects of the energy downturn are apparent in the geographical distribution of job growth. Employment has shrunk 0.4 percent year to date in Houston, the energy capital of the state and the country. San Antonio, which is close to the Eagle Ford Shale, has had two consecutive months without job growth. El Paso employment remains largely flat as well, although this is a long-term trend linked to the decline in federal government spending. In contrast, Dallas and Fort Worth have done relatively well so far this year, although their growth is much slower than it was last year. Austin's employment is up 4.2 percent year to date, by far the fastest growth among large Texas metropolitan areas.

Chart 3
After Spiking, Initial Jobless Claims Declining in Most Energy States



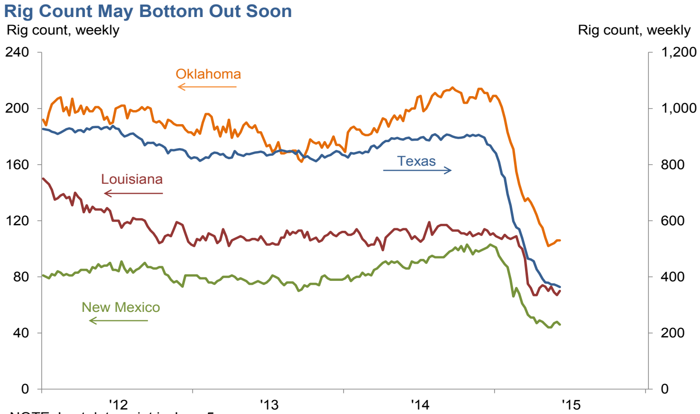
* Seasonally adjusted.
SOURCE: U.S. Department of Labor.

Chart 4
House Prices Down from January Highs in Several Metros



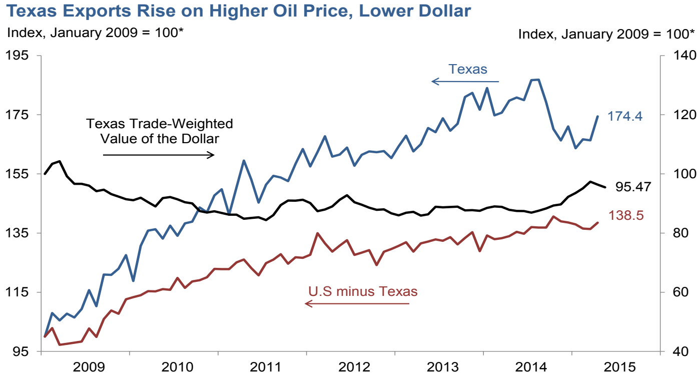
*Seasonally adjusted.
SOURCES: Multiple Listing Service; adjustments by the Federal Reserve Bank of Dallas.

Chart 5
Rig Count May Bottom Out Soon



NOTE: Last data point is June 5.
SOURCE: Baker Hughes.

Chart 6
Texas Exports Rise on Higher Oil Price, Lower Dollar



*Real dollars, seasonally adjusted.
NOTE: The last data point for exports is April. The Texas Trade-Weighted Value of the Dollar for April and May is estimated using the U.S. Trade-Weighted Value of the Dollar.
SOURCES: Census Bureau; WISERTrade; Federal Reserve Bank of Dallas.

State Initial Jobless Claims May Have Peaked

With the exception of North Dakota, initial claims for unemployment benefits in the nation's major energy-producing states appear to have peaked (*Chart 3*). While the energy sector is responsible for about a tenth of continuing jobless claims in Texas, the sector has accounted for 40 percent of the increase in continuing claims since December. By either measure, the energy sector is overrepresented in the claims data given that oil and gas jobs represent less than 3 percent of state employment.

The rise in initial and continuing claims is not yet reflected in the Texas unemployment rate, which remains at its recent low of 4.2 percent. This is partly due to a declining state labor force. In the Bureau of Labor Statistics' household survey, most of this year's decline in employment has been offset by a decline in the total number of workers.

Slowing House Price Gains Likely; Houston Office Vacancy Rises

House price appreciation should slow as a result of weaker economic growth this year and the expectation of higher interest rates. This development is not yet apparent in aggregate data for the state, but median home price data by metropolitan area suggest house prices may be on their way down in Houston and San Antonio (*Chart 4*).

With respect to construction activity, single-family and multifamily permits rose 1.9 and 0.8 percent in April, respectively, although there is reason to think multifamily building in the state may be slowing after an incredible run since permits year to date are below their 2014 monthly average.

Overall, commercial real estate markets in Texas remain solid, with some signs of softening in the Houston office market. According to CBRE data, the office vacancy rate in Houston increased in the first quarter but remains low at 12.6 percent; only Austin has a lower vacancy rate among the large Texas metros.

Oil Prices Inch Up, Rig Counts Edge Down

Crude oil and natural gas prices have risen slightly since hitting recent lows in March. West Texas Intermediate oil prices fell from over $100 per barrel in summer 2014 to below $50 by March. While the oil price has ticked up, it remains around 40 percent below where it was at this time last year. Price volatility has also eased somewhat. The Texas rig count continues to fall, but rig counts appear to be bottoming out in some neighboring states (*Chart 5*). The decline in crude prices has contributed to lower retail gasoline prices, which should spur spending on other goods.

Exports on the Rise

Texas exports rose 4.9 percent in April, posting their biggest monthly gain since October 2013 (*Chart 6*). That said, state exports are still down 2.9 percent from this time last year, which reflects three developments: lower oil prices, weaker global demand and a higher dollar. U.S. exports excluding Texas also increased in April, but the rise was not as big. Texas' stronger performance likely reflects the beneficial impact of the recent rise in oil prices on the value of petroleum product exports—the state's largest export category.

—Emily Gutierrez and Pia Orrenius

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