Peso Devaluations Impact District Economy

Two devaluations of the Mexican peso this year have disrupted economic activity along the Texas border and have had notable effects elsewhere in the District. The first abrupt drop in the peso against the dollar since 1976 came in February 1982, and this was followed by another sudden decline in August.

Peso Overvaluation Since 1976

The Mexican currency was stabilized after the previous 1976 devaluation at about 22.7 pesos per dollar. It remained there with only minor variation for the next several years, in spite of a widening divergence in the price levels of Mexico and the United States. In mid-1980 the peso was allowed to begin drifting downward at a slowly increasing rate, a policy that continued until early 1982.

The weakness in world oil prices eliminated the major factor that provided an underpinning to the overvalued peso, and in February 1982 the Bank of Mexico, faced with dwindling official dollar reserves and increased dollarization in the private economy, removed its support of the peso. At month end the rate stood at about 45 pesos per dollar, down from about 27 pesos per dollar before the devaluation. Mexico again allowed the peso to drift downward against the dollar, but in early August the announcement of price hikes on several previously subsidized items again triggered downward pressure on the exchange rate.

Effects on the Eleventh District

The two 1982 devaluations have had a significant impact on economic activity in the Eleventh Federal Reserve District. Accompanying each, there was a drastic reduction in retail sales, especially in border cities but also in non-border area stores accepting pesos. Surrounding the August devaluation, initial estimates of devaluation-induced decline in sales ranged from about 20 percent in some non-border areas to 80 percent along the border. Layoffs by affected merchants exacerbated unemployment in these areas, and many stores established shorter hours.

There were few reports from Eleventh District banks of losses attributable to the freezing of dollar accounts in Mexican banks, which accompanied the second devaluation. The possibility of default remains on some loans to Mexican public and private entities, however.

Border city fiscal revenues have also been hit by the 1982 devaluations. Sales tax receipts and bridge revenues have been off, substantially lowering municipal fiscal growth in these cities.

Tourism is one area that demonstrated a quick response to price signals delivered by the devaluations. Mexican outgoing tourism fell off (Continued on back page)

Texas Recession Not Just In Energy

Although the U.S. economic downturn began in July 1981, evidence of a significant recession did not appear in Texas until late in the first quarter of 1982, when the energy-related industries began a steep decline. Buoyed by rapid growth in the energy-related sectors, last year's aggregate employment statistics hid weaknesses in other industries.

An examination of employment changes for these industries suggests that the state's recent erosion in employment was not simply the result of slackness among energy-related firms. Foreign competition, high interest rates, and overly optimistic production schedules all shaped the state's recent economic experience.

International competition in high technology, for example, contributed to a two year decline in Texas' electric and electronic manufacturing employment beginning about mid-1980. Although increased defense contracting has helped to stabilize employment levels in the industry, Texas' July 1982 employment was 9.8 percent (10.6 thousand) below July 1980.

International competition was also one contributor to the decline in the (Continued on back page)
### ELEVENTH DISTRICT CREDIT CONDITIONS

#### ALL MEMBER BANKS

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<th>Year</th>
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<th>Year</th>
<th>Total Deposit Growth</th>
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#### Change* (Millions $) (Percent)

### LOAN GROWTH AT LARGE WEEKLY REPORTING BANKS

#### ELEVENTH FEDERAL RESERVE DISTRICT

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#### Change* (Millions $) (Percent)

* Dollar and percent changes are calculated using quarterly average figures from weekly reported bank data. For 1980 and 1981, growth figures were calculated comparing fourth quarter figures to the previous year's fourth quarter. For 1982, non-annualized growth figures for the first six months were calculated comparing the second quarter of 1982 to the fourth quarter of 1981.

### LOANS CLOSED AT FEDERALLY-CHARTERED S&L's: TEXAS

- 800 MILLION DOLLARS

### NET NEW SAVINGS' AT FEDERALLY-CHARTERED S&L's: TEXAS

- 300 MILLION DOLLARS

1. New savings received less withdrawals, excluding interest and dividends.

The District economy is still fairly weak.

- The seasonally adjusted unemployment rate in Texas rose to 7.0 percent in June and remained there in July, compared to 6.4 percent in May 1982 and 5.1 percent in July 1981.
- The distribution of layoffs by industry has been broad: transportation, transportation equipment manufacturing, electronics, and energy-related manufacturing and services. Many types of workers are unemployed: blue collar, professional, clerical, and sales.
- Loans at member banks rose only 0.1 percent in July after increasing strongly in the first half of the year. The drop-off in loan growth reflects a sharp slowdown in loans to businesses.
- The drilling rig count is still falling, as it has been almost continuously since December.
- Oil refining in Texas slipped to May levels in late summer after climbing through the spring and early summer.
- Farm incomes, already low in 1980 and 1981, have been hard hit by storm-related crop damage and low prices for crops and livestock.
- Trends in residential and nonresidential construction have been moving in opposite directions during most of the past year, but the prospects for both types of construction increased in June and July.
- Sales at surveyed department stores through August were up only 4 percent from the same months last year, and sales in August this year were unchanged from the level a year ago.
PESO (cont.)
greatly, while U.S. tourists traveling to Mexico increased initially. Tourist destinations north of the border were hurt, and monetary uncertainties south of the border later reduced incoming Mexican tourism, too.

The Future of the Peso

After nationalization of the Mexican private banking system in early September, exchange controls were established. A preferential rate of 50 pesos per dollar was set for critical imports and payments on international debt, and another rate of 70 pesos per dollar was set for exports, tourism, and payment of frozen foreign currency bank deposits in Mexico. It is not at all clear how workable the controlled, dual exchange rate will be, and the devaluation aftermath may have more prolonged consequences for the District this time than before.

— Leroy O. Laney

RECESSION (cont.)

state’s farm income, which peaked in 1979. In the wake of declining prices and rising costs, some farmers left agriculture. Others cut employment to save costs, at the same time as they set aside marginal acreage. The result was a 5 percent decline (10.7 thousand) in agricultural employment between June 1980 and June 1982.

In the second half of 1981, longer term employment declines in electronics, agriculture, and aircraft and aircraft parts were joined by reductions tied to the July onset of the U.S. recession. Employment in lumber and wood products, apparel manufacture, and other areas fell significantly below year earlier levels. As it had during the 1973-75 recession, Texas’ 1981 manufacturing employment began a prolonged decline. Even so, during the latter portion of 1981, the state’s manufacturing employment fell more slowly than U.S. manufacturing employment.

And while total U.S. employment fell during the second half of 1981, the state’s employment rose briskly.

In 1982, longer term and recent cyclical pressures joined with the sagging fortunes of energy-related firms to bring a decline in unadjusted nonagricultural wage and salary employment in Texas. During the first seven months of 1982, such employment fell more than twice as fast as the U.S.'s. Employment in oilfield machinery and oil and gas extraction, which had risen rapidly throughout 1981, fell hard after peaking in March 1982. Employment in primary metals, which produces drilling pipe, fell 16 percent between March and July.

The state’s recent employment experience has shown economic weakness, to a significant degree because of problems in the energy-related sectors. But energy is by no means the whole story.

— William C. Gruben