Drilling Industry Influences  
Business Loan Demand at Texas Banks

A positive relationship has existed between the growth of commercial and industrial loans at the large Texas banks and the strength of the drilling industry. An examination of the two drilling cycles from mid-1976 to present indicates that an increase in drilling activity is a leading indicator of growth in business lending. This is understandable because the large Texas banks are major energy lenders. This relationship partially explains the slowing in business loan growth during 1982 and 1983.

Drilling's Effect on Lending

In the last seven years, the drilling industry has experienced two complete cycles of expansion and contraction. During these cycles, changes in the rig count have preceded changes in business loan growth (see overleaf). The lag in the response of business lending to the turning points of the drilling cycle varies from one to four quarters. The lag may be the result of the type of drilling that occurs at different stages of the drilling cycle. Exploratory wells are drilled early in a cycle. Banks typically do not finance these explorations for new oil. Banks tend to finance the development drilling that occurs later in the cycle, using proven reserves as collateral.

Slow drilling activity is a partial explanation of the slowdown in business loan growth over the last two years. The drilling rig count peaked in late 1981 and declined until April 1983. Business loan growth began to slow early in 1982. The nation's recession also contributed to slower business loan growth. Loan growth measured from year-end to year-end slowed from 44.5 percent in 1981 to 17.5 percent and 7.8 percent in 1982 and 1983, respectively.

Analysis of past trends in the relationship between loan growth at large Texas banks and drilling activity suggests that the demand for business loans at these banks is likely to remain sluggish in the near term. Though conditions in the drilling industry are improving, a major increase in the rate of investment in that sector is unlikely.

The active drilling rig count in the U.S. began rising in May 1983, but the drilling industry still has substantial excess capacity. Only 52 percent of the operative rig fleet is presently active, and inventories of oilfield equipment such as drill pipe are plentiful.

Total Loan Growth Showed Strength

Despite the sharp slowdown in business lending, growth of total loans has slowed more moderately. By allocating funds into real estate lending,

The Economic Outlook for New Mexico

New Mexico's economy lagged the U.S. into the last recession. When the state's economy finally turned down, in 1982, several of New Mexico's economic indicators showed their worst performance in more than two decades. By late 1983, however, New Mexico's economy was clearly recovering. The outlook for 1984 is positive, overall, but some New Mexico industries and regions will see only modest improvement.

A Mining Recession

By most measures, New Mexico's recession was not as serious as the nation's. Even so, several of the state's most important economic sectors suffered severe setbacks. Mining, which accounts for about four times the share of New Mexico's employment as that of the U.S., was particularly hard hit. Copper, uranium, potash, and coal mining, as well as oil and gas extraction, all suffered. Together with mining's downturn, declines in construction and manufacturing activity and in federal government employment led to rising unemployment rates and the State's smallest increase in nominal personal income since 1968.

When the New Mexico economy began to turn up, its recovery lagged both that of the U.S. and of some of the other portions of the Eleventh District. During the last recession, the U.S. unemployment rate peaked in December 1982 and Texas' rate reached its high point in March 1983, while New Mexico's rate never exceeded the 10.5 percent it reached in July of 1983.

A Slow Recovery

New Mexico's nonagricultural wage and salary employment finally turned up last September, three months after
DEPOSITS—LARGE WEEKLY REPORTERS
Eleventh Federal Reserve District
35 PERCENT\(^1\) (NOT SEASONALLY ADJUSTED)

1. Percent change from same quarter in previous year.
SOURCE: Federal Reserve Bank of Dallas.

LOANS—LARGE WEEKLY REPORTERS
Eleventh Federal Reserve District
60 PERCENT\(^1\) (NOT SEASONALLY ADJUSTED)

1. Percent change from same quarter in previous year.
SOURCE: Federal Reserve Bank of Dallas.
DISTRICT BRIEFS

- The Texas Industrial Production Index fell in December after reaching its 1983 high in November. At least some of the decline may have resulted from weather-related shutdowns. Production of nondurable goods showed the largest drop. The TIPI for December, however, was 8 percent above a year earlier.

- Between December 1982 and December 1983, the consumer price index increased 3.8 percent in the United States, 0.8 percent in Houston, and 4.7 percent in Dallas-Fort Worth. The differential between the inflation rates in Houston and Dallas-Fort Worth was spread across a wide range of goods and services, but it was particularly pronounced in housing costs. The price of shelter rose 6.5 percent in Dallas/Fort Worth and fell 1.9 percent in Houston.

- The Texas rig count dipped to 865 during the week of February 13. This level was the lowest since early October and was more than 11 percent below the peak for 1983.

- On a seasonally adjusted basis, Texas housing permits fell by slightly more than 18 percent in December. The decline was led by a 22 percent drop in multifamily permits.

- The Texas unemployment rate fell in January to 6.9 percent from 7.7 percent in December and it was 1.3 percentage points below its year-earlier level. December's relatively high rate resulted from a larger increase in the labor force than in jobs. November's unemployment rate was 6.7 percent.

- Year-over-year growth in business loans at large weekly reporting banks has been declining since the second quarter of 1982. This has been partly offset by increases in real estate lending. The growth rate in total loans at large weekly reporting banks, on a year-over-year basis, increased in both the third and fourth quarters after a decline in the second quarter.

- Deposit growth slowed at all financial institutions in the Eleventh District in 1983. Quarterly gains in total deposits on a year-over-year basis averaged 15.8 percent, down from average quarterly gains of 17.0 percent in 1982.

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UNEMPLOYMENT RATE

<table>
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<th>ELEVENTH DISTRICT STATES</th>
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<td>4%</td>
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<tr>
<td>1983</td>
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<td>3%</td>
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1. Louisiana, New Mexico, Oklahoma, and Texas.

SOURCES: Texas Employment Commission.
Federal Reserve Bank of Dallas.

CONSUMER PRICE INDEX

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<th>YEAR</th>
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<tr>
<td>1983</td>
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1. Percent change from same quarter in previous year.

Federal Reserve Bank of Dallas.

HOUSING PERMITS: TEXAS

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Federal Reserve Bank of Dallas.

TAXAS INDUSTRIAL PRODUCTION INDEX

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SOURCE: Federal Reserve Bank of Dallas.
Drilling Industry (cont.)

the Texas banks have been able to maintain a rate of loan growth well above that of large banks in the nation. In 1983, loans grew nearly 16 percent at the large Texas banks compared with a 5.3-percent increase at large banks in the U.S. More than half of the 1983 increase in total loans at large Texas banks was in real estate loans.

Outlook for 1984

Texas banks may not be able to maintain this difference between their loan growth rate and that of large banks in the nation in 1984. Loan growth at large banks in the U.S. is projected to pick up this year. Business loan demand typically increases during the second year of a recovery. Texas banks expect business loan demand from their non-energy related borrowers to increase. Increases in total loan growth will be moderate, however, because of the continued weakness in the energy sector.

—Robert Clair

New Mexico (cont.)

the U.S., and was up 1.5 percent for 1983 after a 0.3 percent decline in 1982. Growing defense contracting, rising civilian demand for electronic equipment, and a jump in construction activity all contributed to the turnaround. The start of a recovery in oil and gas drilling and coal mining also helped to reverse the state’s sagging fortunes.

This year will probably see continued improvement in the New Mexico economy, but the strength of the recovery will vary greatly across industries and regions within the state. Albuquerque will continue to benefit from growth in high-technology manufacturing tied to defense contracting and to rising civilian demands, but the mining-dominated areas of New Mexico are unlikely to fair as well. The state’s copper and potash producing areas have already seen some improvement, as workers have begun to be recalled in both industries. Economic recovery in these areas is likely to be much slower and less stable than that of Albuquerque. This is partly the result of intense foreign competition aggravated by the high value of the dollar. Oil and gas drilling in New Mexico is likely to continue to grow, although modestly, after the usual seasonal weakness during the first quarter. However, rig activity at rates common in 1981 will not occur in 1984. Uranium mining will continue to suffer because of problems in the nuclear power industry.

In sum, because of its industrial composition, the economic recovery in New Mexico may not be as strong as the U.S. recovery. The importance of mining and those portions of non-durable goods manufacturing that also are being negatively affected by foreign competition will dampen economic growth in the state. The prospects of a boom this year for the New Mexico economy appear slim, but the state will continue to recover.

—William C. Gruben