Texas S&Ls Expand and Diversify Lending in Current Recovery

Since the economic recovery began, Texas savings and loan associations (S&Ls) have expanded and diversified lending activity. The 1983 housing boom produced rapid growth in lending in the traditional S&L market, residential mortgage lending, at S&Ls in both Texas and the nation as a whole. Texas S&Ls, however, also diversified their lending by increasing their presence in nontraditional markets, such as nonresidential mortgages and consumer and commercial loans. The increase in lending in these areas offset the decrease in residential lending accompanying the 1984 downturn in home building and helped S&Ls maintain asset and income growth.

Housing Cycle Affected Lending

Texas S&Ls financed much of the state’s housing boom that began in 1982. S&Ls make mortgage loans to finance both the purchase and the construction of residences. During 1983, residential construction spending rose $3.2 billion, and S&Ls increased their residential construction lending $3.7 billion while loans for purchasing homes grew $2.3 billion. Growing business credit demands in 1984, however, pushed up interest rates, which led to a decline in the housing industry. Both home construction spending and residential mortgage lending fell $1.6 billion in 1984. The decline in lending was primarily in apartment and condominium construction financing that followed overbuilding in some Texas markets.

Expansion into Nontraditional Areas

Texas S&Ls have also utilized expanded asset powers to increase both nonresidential mortgage lending and nonmortgage lending, including commercial and consumer lending (Table 1). Lending to finance retail shopping establishments and other nonresidential projects rose $4.3 billion in the last two years, and nonmortgage lending increased $2.4 billion in 1983 and $1.9 billion in 1984. In 1984 the increases in nontraditional lending more than offset the decrease in residential lending resulting from the sharp downturn in the Texas housing industry. Total loans closed have not fallen with the decline in housing permits, as in the past (Chart 1).

Diversification Has Positive Effect

This diversification has helped support asset and income growth at Texas S&Ls. Assets grew over 30-percent in each of the last two years. In the future, however, regulatory changes will limit growth to 25 percent at most.

Residential Construction in Texas Adjusts to Slower Migration

After a spectacular performance in the early 1980s, residential construction—measured by the number of housing permits issued—suffered a major slowdown in Texas during 1984. The large decreases in net migration to Texas during both 1983 and 1984, following the migration boom of 1982, were primary forces leading to the slowdown. Because of the negative effects of slowing population growth, stimulative factors in 1985, such as falling interest rates, are unlikely to boost residential construction above its 1984 level.

Home Building Responds to Migration

During the early 1980s, residential construction was stimulated by large net inflows of people into the state. Net migration was responsible for about two-thirds of the 1 million-person increase in the state’s population between 1980 and 1982 (Chart 2). The rapid influx of new residents sharply increased the demand for housing, and home construction in Texas, especially building of multifamily dwellings, rose with a lag of 8 to 12 months (Chart 3). Supply-side forces, such as the tax incentives of the Economic Recovery Tax Act of 1981, also contributed to this surge in building.

More recently, decreases in net migration have curbed residential construction. From 1982 to 1984, net migration to Texas fell over 90 percent to reach its lowest level since 1967. This drop occurred despite continued high growth in some metropolitan areas. The recovery of the national economy and the slump in the Texas economy have contributed to this slowdown in building.

(Continued on back page)
Table 1
LOANS CLOSED AT FSLIC-INSURED SAVINGS AND LOAN ASSOCIATIONS IN TEXAS
(Dollar amounts in millions)

<table>
<thead>
<tr>
<th>Type of loan</th>
<th>1983</th>
<th>1984</th>
<th>Absolute change</th>
<th>Percent change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mortgage</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Residential</td>
<td>$11,790</td>
<td>$10,170</td>
<td>-$1,620</td>
<td>-13.7</td>
</tr>
<tr>
<td>Nonresidential</td>
<td>4,682</td>
<td>6,008</td>
<td>1,326</td>
<td>28.3</td>
</tr>
<tr>
<td>All other</td>
<td>3,745</td>
<td>5,599</td>
<td>1,854</td>
<td>49.5</td>
</tr>
<tr>
<td>Total</td>
<td>$20,217</td>
<td>$21,777</td>
<td>$1,560</td>
<td>7.7</td>
</tr>
</tbody>
</table>


Chart 1
INDEXES OF TOTAL LOANS CLOSED AT S&Ls AND TOTAL HOUSING PERMITS ISSUED IN TEXAS


U.S. Department of Commerce, Bureau of Census.

Chart 2
POPULATION CHANGE AND NET MIGRATION IN TEXAS

600 THOUSANDS OF PERSONS


1. Percent change from same quarter in previous year.


Chase Econometrics.

Chart 3
INDEXES OF HOUSING PERMITS AND NET MIGRATION IN TEXAS

NOTE: Quarterly values interpolated from annual data.

SOURCES: U.S. Department of Commerce.
Federal Reserve Bank of Dallas.

LOANS—LARGE WEEKLY REPORTERS
Eleventh Federal Reserve District

DEPOSITS—LARGE WEEKLY REPORTERS
Eleventh Federal Reserve District

1. Percent change from same quarter in previous year.

SOURCE: Federal Reserve Bank of Dallas.
The District's economic expansion continues but at a very gradual rate.

- The slowing of economic growth within the District is evident in the slight gains in total nonagricultural employment. In the first quarter of 1985, the increase in Texas employment was substantially smaller than in the fourth quarter of 1984. Even so, Texas employment grew significantly faster than Louisiana's. Employment expansion in New Mexico has proven stronger than in the other District states.
- Manufacturing activity in Texas is flat, broadly following the national trend. The prime reasons for the sluggish performance are competition from imported goods and the slowing of the U.S. economy, which has dampened demand. In Texas the weakness is most severe in durable goods manufacturing.
- As the weakness in oil prices continues, the drilling rig count has yet to show the normal seasonal upturn that usually occurs during the spring. The Texas drilling rig count has been falling steadily and is now more than 20 percent below last year's level. After increasing throughout much of 1984, employment in oil field machinery manufacturing has dropped.
- The recent decline in interest rates has stimulated residential construction in the nation as a whole. In the District, however, the surplus of residential units has, to date, prevented a resurgence in construction. The weakness in the District is widespread, affecting both multifamily and single-family units. Nonresidential construction continues strong.
- Loan growth at the District's large banks is slowing, reflecting the state of the economy. The volume of business loans actually fell in April compared with a year earlier. Both real estate and consumer loans continue to increase, although the rate of growth is slowing.
- Prices for agricultural products sold by District farmers are considerably below a year earlier. Expanded production has led to an 18-percent decline in the Texas all crops price index.
- Inflation in the District is running at a slightly lower level than in the nation as smaller increases in housing costs hold down the local increases in the consumer price index. Compared with a year earlier, inflation in April increased 3.6 percent in Dallas-Fort Worth and 2.9 percent in Houston. For the same period the national rate was 3.7 percent.
Texas S&Ls (cont.)

The increased lending activity has generated higher interest income and substantial fee income in the form of origination and servicing fees for loans sold to other investors. Fee income rose 67 percent in 1983 and grew at an annual rate of 40 percent in the first half of 1984.

The Outlook Is Mixed

The outlook is for continued growth of lending at Texas S&Ls. The 185-basis-point fall in mortgage interest rates since their peak in 1984 will generate increased home sales and mortgage lending. In addition, year-to-date nonresidential construction spending in Texas is 13 percent above the comparable 1984 level. On the other hand, S&L delinquency rates have risen, and increases in nonperforming assets could place downward pressure on earnings in 1985.

—Robert T. Clair

Construction (cont.)

energy sector have made migration to Texas less attractive by curtailing employment opportunities in the state relative to the nation as a whole. The large declines in net migration have resulted in smaller increases in the demand for housing and a slowdown in the pace of residential construction. A record number of housing permits were issued in Texas in 1983, but the number of multifamily permits fell about 35 percent in 1984 while the number of single-family permits fell approximately 18 percent. In each of the first three months of 1984, the numbers of multifamily and single-family permits issued were substantially below their corresponding levels in the previous year. Also, the Texas share of multifamily permits issued in the United States declined from about 28 percent in the first quarter of 1983 to just over 10 percent in the first quarter of 1985. The Texas share of single-

family permits issued fell from about 12 percent to just over 7 percent. These reductions reflect the large declines in net migration.

Outlook

Although other forces might work to offset the current downturn in residential construction, the industry, especially the multifamily sector, probably will not top last year’s performance. Declining mortgage interest rates could dampen the negative effect of the declines in net migration. Any strengthening of the state economic recovery could provide some stimulus to residential construction as well. It is unlikely, however, that the combined positive effect of these additional factors in 1985 will outweigh the lagged effect of last year’s large decline in net migration.

—Jeffery W. Gunther and William T. Long III

The views expressed are those of the authors and do not necessarily reflect the positions of the Federal Reserve Bank of Dallas or the Federal Reserve System.