

Regional

Regional Growth Slows in First Quarter

April 30, 2015

Texas economic growth decelerated in the first quarter, with employment expanding at a 0.7 percent annualized rate, down from 4.5 percent in fourth quarter 2014. Employment in oil and gas extraction and manufacturing sectors was most affected, but other industries also experienced a dip. Low oil prices, a strong dollar and a slowing U.S. economy during the first quarter contributed to sluggish Texas growth.

Headline indexes from the Texas Business Outlook Surveys (TBOS) are significantly below their 2014 levels, consistent with slower economic growth seen in the recent employment numbers. The employment forecast—based on the Texas Leading Index—projects 0.5 to 1.5 percent growth for 2015 (December over December), with the pace of job growth expected to pick up in the second half of the year.

Employment Declines in March

Texas employment fell at a 1.2 percent annualized rate in March, the largest decline since October 2011. On a quarterly basis, employment growth of 0.7 percent was a full percentage point slower than it was for the nation.

First-quarter employment growth appeared segmented, with some sectors still growing and others declining sharply. Five sectors contracted in the quarter, with oil and gas employment falling at an 8.8 percent annualized rate and manufacturing declining 3.5 percent (Table 1). Service-providing activities fared better, with the leisure and hospitality and trade and transportation sectors expanding 3.3 percent and 2.9 percent, respectively. This segmented growth is further demonstrated in Chart 1, which shows a 3.4 percent drop-off in goods-producing employment in the quarter, compared with 1.5 percent growth in service-providing industries.

Texas' unemployment rate fell further in March, to 4.2 percent, its lowest level since July 2007. However, the decline was driven by a reduction in the labor force, not an increase in employment.

Manufacturing Activity Stalls

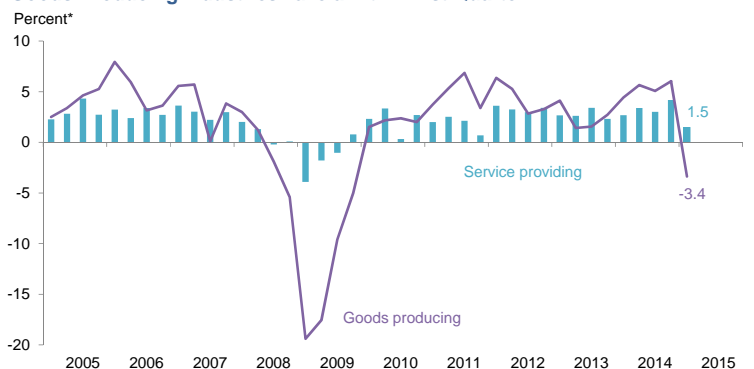
Texas factory activity remained weak in April, according to the Texas Manufacturing Outlook Survey (TMOS). The production index, a key measure of state manufacturing conditions, improved slightly while showing negative growth, inching up from -5.2 in March to -4.7 in April. Texas service sector activity continued to reflect expansion in April, posting its highest reading this year, according to the Texas Service Sector Outlook Survey (TSSOS). Both the manufacturing

Table 1: Employment Growth Declines Across Multiple Sectors

	2014	Q4:2014	Q1:2015
	Dec/Dec % change	Q/Q annual % change	Q/Q annual % change
Total	3.6	4.5	0.7
Total private	4.0	4.9	0.8
Oil and gas + support	9.5	7.4	-8.8
Manufacturing	2.3	4.0	-3.5
Professional & business services	4.7	4.8	-0.9
Construction	7.5	8.1	-0.9
Government	1.5	2.4	-0.2
Information	0.1	1.4	0.4
Financial activities	2.8	3.3	1.4
Educational & health services	3.4	5.3	2.8
Trade, transportation & utilities	3.8	5.3	2.9
Leisure & hospitality	4.4	3.7	3.3

SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

**Chart 1
Goods-Producing Industries Take a Hit in First Quarter**



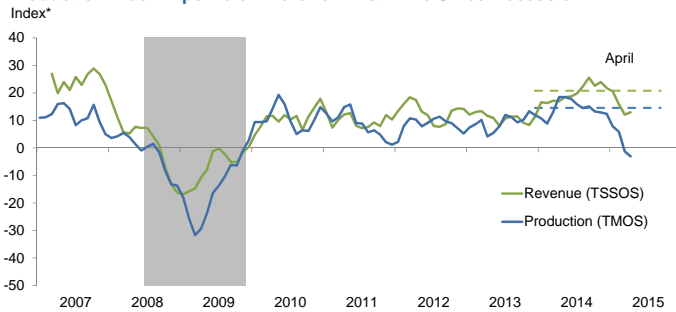
*Quarter/quarter; seasonally adjusted, annualized rate.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

production and service revenue indexes are below their 2014 averages, with the three-month moving average in March for manufacturing going into negative territory for the first time since the recession. It remained negative in April (Chart 2).

Texas Output Growth

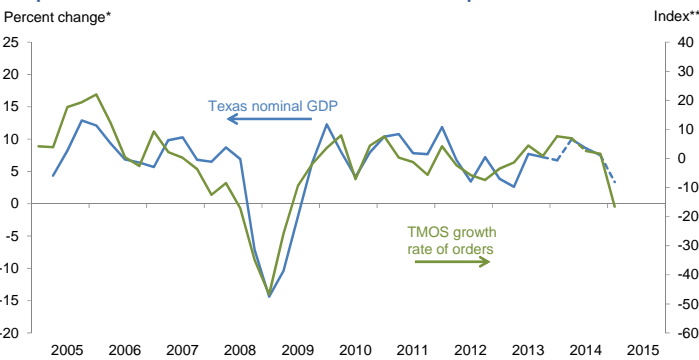
The TMOS growth rate of orders (GO) index—a strong leading indicator of state output growth—plunged in first quarter 2015.¹ Because state gross domestic product (GDP) data are lagged—the latest figure available is for fourth quarter 2013—regression analysis helps to estimate current Texas GDP growth using the GO

Chart 2
Production Index Dips Below Zero for First Time Since Recession



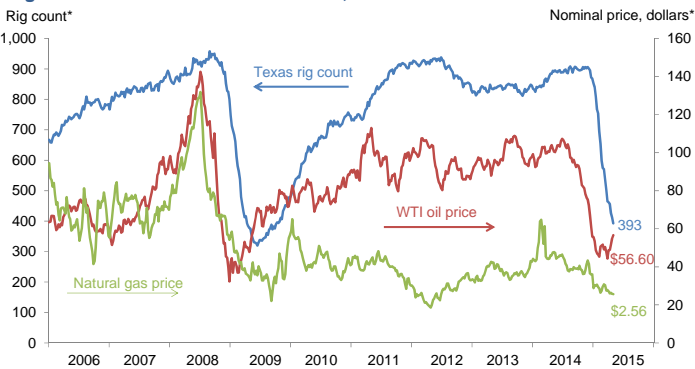
*Three-month moving average; seasonally adjusted.
 NOTES: Shaded area represents Texas recession; dashed lines represent 2014 averages for revenue and production indexes.
 SOURCES: Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS) and Texas Service Sector Outlook Survey (TSSOS).

Chart 3
Drop in TMOS Growth Rate of Orders Indicates Sharp Decline in GDP Growth



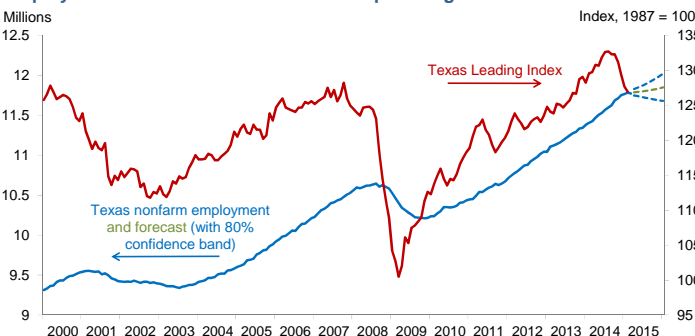
*Quarter/quarter, two-quarter moving average; seasonally adjusted, annualized rate.
 **Quarterly average; seasonally adjusted.
 NOTES: Dashed line represents estimates for first quarter 2014 to first quarter 2015 based on regression. Last data point is fourth quarter 2013 for Texas GDP and first quarter 2015 for TMOS.
 SOURCES: Bureau of Economic Analysis; Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS).

Chart 4
Rig Count and Gas Prices Fall Further; Oil Prices Stabilize



*Weekly.
 NOTES: Natural gas price series is multiplied by 10. Data are through week of April 24, 2015.
 SOURCES: Baker Hughes; Wall Street Journal; Energy Information Administration.

Chart 5
Employment Forecast Shows a Flatter Slope Going Forward



NOTE: Shaded areas represent Texas recessions. Last data for for leading index is February 2015.
 SOURCES: Bureau of Labor Statistics; Federal Reserve Bank of Dallas; authors' calculations.

index (Chart 3).² The analysis suggests that Texas GDP declined sharply in first quarter 2015 after steadily growing in 2014.

Oil Rebounds to Above \$50; Energy Sector Weak

The rig count and demand for oilfield services continued to decline in the region, with losses concentrated in the Permian Basin and Eagle Ford areas. The rig count stood at 393 during the fourth week of April, its lowest level since October 2009. Natural gas prices continued falling—averaging \$2.56 per MMBtu during the same week, while crude oil prices appeared to stabilize, rebounding to \$56.60 per barrel (Chart 4).

Exports Rise in February

Texas exports grew 1.3 percent month over month in February after falling 4.5 percent in January. The export decline this year has been broad based, led by petroleum and coal products. However, due to intra-industry trade with North American Free Trade Agreement partners—48 percent of Texas exports are to Canada and Mexico—Texas trade will likely be less affected by the stronger dollar than other U.S. states. Texas exports to Mexico and Canada fell on average only 5 percent in fourth quarter 2014, while exports to Latin America, China and the European Union declined 11 percent.

Wage and Price Pressures Ease

While upward wage pressure persists, TMOS and TSSOS wages and benefits indexes indicate that slower job growth in the region during the first three months of the year may have contributed to declines in these indexes to below their 2014 averages. The TBOS wage indexes are consistent with reports from Beige Book contacts, who noted that wage pressures were either stable or had eased in a majority of surveyed sectors.

Prices in Texas are also falling, according to the Texas consumer price index and TBOS. The TMOS prices for finished goods index continued to contract, while the April TSSOS selling prices index remained below the 2014 average.

Outlook Is for Slower Growth

Expectations regarding future business conditions continued to be fairly weak in April for both the manufacturing and services sectors. The TMOS general business activity index remained in negative territory for the fourth consecutive month in April, reflecting increased pessimism. The TSSOS general business activity index also remained negative in April, an indication of worsening expectations among service sector respondents.

The Texas Leading Index fell 0.6 percent in February after declining 1.3 percent in January; the forecast anticipates employment growth with a much flatter slope going forward (Chart 5). The monthly forecast based on the leading index shows progress in employment growth toward the second half of the year, implying that the regional economy may sustain the worst of the strong dollar and oil price shocks during the first six months of the year. Nevertheless, the current employment forecast projects only 0.5 to 1.5 percent growth for 2015 (December to December).

—Jesus Cañas and Sarah Greer

Notes

1. "Texas Manufacturing Outlook Survey: Survey Methodology and Performance," by Jesus Cañas and Emily Kerr, Federal

Reserve Bank of Dallas Research Department Working Paper
no. 1416.

2. Regression specification was
 $\Delta NGDP_t = \beta_0 + \beta_1 * GO + \beta_2 * \Delta NGDP_{t-1} + e$, where $\Delta NGDP_t$ is
the log difference in nominal Texas quarterly GDP and GO is
the quarterly average of the TMOS growth rate of orders
index.
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