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Houston Business

A Perspective on the Houston Economy

Driven by Differences: GRP of Houston and Dallas

Houston and Dallas have less in common than their historical rivalry suggests; each carries out important but very different roles in the national and global economies.

The April 1995 issue of *Houston Business* presented an annual data series for gross regional product (GRP) in Houston from 1977 to 1994 with two important qualifications. The first qualification was that data required to produce the estimates are not timely, and some data for recent years were forecast. The second qualification was that Houston-specific data are available only for the contribution of labor and entrepreneurs (about two-thirds of total regional product), and capital consumption was estimated from broader, statewide trends. Despite these qualifications, GRP data provided new insight into the Houston economy's performance and a contrast with the employment data normally used to describe local economic conditions.

This article continues to document Houston's growth using GRP and compares the Houston and Dallas primary metropolitan areas (PMSAs) from 1977 to 1994. The GRP data help retell what has become a familiar story in this newsletter, as earlier issues have examined differences in the two metropolitan areas' economic bases (July 1990), their relative industrial diversity (July 1994) and their trends in local construction activity (May 1994). The bottom line remains the same, however: Houston and Dallas have less in common than their historical rivalry suggests; each carries out important but very different roles in the national and global economies. Continued variations in the relative economic performance of the two cities are simply one more reflection of local economies driven by different exogenous economic forces.

GROWTH IN HOUSTON AND DALLAS

Table 1 compares GRP growth in the Houston and Dallas metropolitan areas with that of the United States from 1977 to 1994. During this period, the Dallas PMSA outperforms Houston's, with average annual growth rates of 4.2 percent versus Houston's 2.6 percent. In 1977, Houston's economy, as measured by GRP, was about one-third larger than Dallas', but by 1994 this lead had slipped to 14 percent (*Figure 1*). Goods and services both grew more strongly in Dallas than in Houston, although services led both economies, growing at a 5.4-percent rate in Dallas and 3.7 percent in Houston.

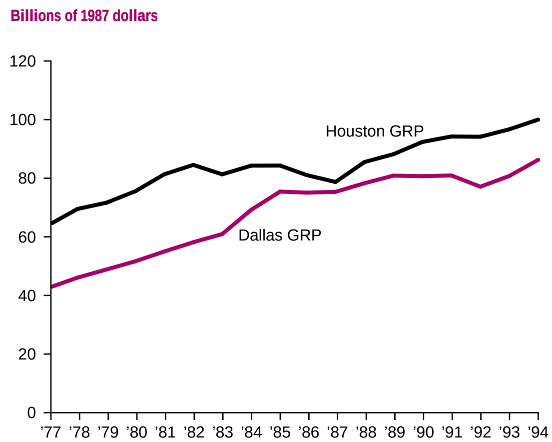
It is difficult to draw many long-term implications from these figures, although the last 17 years clearly have been kinder to Dallas. The big difference in the two economies came during the 1982–87 period. These were the years of the oil bust—a period of significant economic decline in Houston—which carried with it annual rates of decline in gross domestic product (GDP) of 1.4 percent per year and a loss of 225,000 jobs between early 1982 and 1987. Indeed, slow growth rates for goods in Houston in the late 1970s and early 1980s, as measured by the GDP data, seemed to foreshadow the oil bust. In contrast, Dallas enjoyed its strongest growth period from 1982 to 1987, led by a powerful surge in construction and real estate activity.

Table 1
Metropolitan Area Growth Rates:
Gross Product in Houston and Dallas 1977–94
(Percent per year)

	1977–94	1977–82	1982–87	1987–94
Dallas PMSA				
Goods	2.6	1.1	6.7	1.3
Private services	5.4	8.8	5.0	3.4
Total GRP	4.2	6.2	5.3	2.0
Houston PMSA				
Goods	.9	.1	–1.7	3.3
Private services	3.7	9.2	–1.6	3.8
Total GRP	2.6	5.5	–1.4	3.6
United States				
Goods	1.6	–1.4	4.4	1.7
Private services	3.3	2.8	4.4	2.9
Total GRP	2.5	1.3	3.8	2.3

SOURCES: Bureau of Economic Analysis, Regional Economic Information System, and calculations of the authors.

Figure 1
Houston and Dallas, Gross Product 1977–94



This growth has been described as driven by a lending frenzy by regional financial institutions—many crippled by bad energy loans—that turned to Texas real estate for survival. Houston's real estate problems had already begun to surface by 1982, but Dallas and other cities carried the Texas construction boom through 1986.

Differences in the growth patterns of the two cities continue. While Dallas struggled after 1987, Houston staged a strong recovery from its downturn, returning to previous peak levels of production by 1989 and peak employment by 1990. Over the past three years, however, that pattern has slowly reversed, and in 1994 Dallas again strongly outperformed Houston. For example, the year-over-year growth rate for employment in Houston in 1994 was only 2.2 percent, while Dallas jobs increased by 3.8 percent. GRP estimates show Houston growing a solid 4 percent, with Dallas at an even stronger 6.8 percent.

WHY DIFFERENT PERFORMANCES?

Houston's and Dallas' economies are clearly unsynchronized, with one capable of gaining ground while the other loses. Why such different performances? Table 2 provides several clues from a comparison of the distribution of gross product by major industrial sector in Houston and Dallas. First, Houston's share of mining (mostly oil and gas) is nearly three times that of Dallas. Houston remains America's preeminent oil center, and it serves an important global role in oil services and machinery. Dallas remains the nation's number two oil city, but its oil-related production has slipped steadily to only 26.3 percent of Houston's level. The second major difference comes in the heart of the service sector, especially transportation, communications and public utilities (TCPU); wholesale and retail trade; and finance, insurance and real estate (FIRE). Together, these sectors make up 55.2 percent of Dallas GRP, in contrast to 44.7 percent of Houston's output. The strength in these service industries is the culmination of several trends. Dallas was already an important financial and insurance center when banking consolidation in the late 1980s, together with the decline of energy lending, saw Dallas move strongly to become the banking center for the Southwest.

Dallas' location as a hub for the southwestern United States, symbolized by Dallas/Fort Worth International Airport, has been the key to growth in transportation, distribution and trade. Dallas is a regional economic capital, the center of much of the commerce that flows through the southwestern United States. It is a role much like the one Atlanta plays in the southeastern United States.

Houston's central role remains in oil—still the world's largest industry—and oil remains the dominant feature of the city's economy. Houston is a global technical and operations center for exploration and drilling; it is at the heart of the nation's most important petrochemical and refining belt, and it is home to five of the world's 20 largest industrial and petrochemical builders and contractors. The Johnson Space Center and the University of Texas Medical Center, major technology centers in their own right, contribute their engineering and technical expertise to Houston industry. Much of Houston's recent diversification has come as part of its role in applied technology—in natural gas trading, cogeneration and independent power production, applied software and environmental controls.

Houston is a coastal city, with a major distributional role through its ship channel and the Port of Houston. However, despite being a smaller economy, Dallas surpassed Houston in total GRP from the distributional sectors discussed above (TCPU, wholesale and retail trade, and FIRE) in the mid-1980s. It has not given up the lead, despite Houston's pattern of stronger growth since 1987.

Table 2
Distribution of Houston and Dallas Economic Activity Gross Product, 1994
(Percent)

Sector	Houston	Dallas
Mining	11.0	3.8
Construction	4.8	2.9
Manufacturing	15.6	16.3
TCPU	13.8	16.6
Wholesale	8.0	10.2
Retail	8.4	9.3
FIRE	14.5	19.1
Services	17.1	16.5
Government	6.7	4.9

LOCAL BUSINESS CYCLES

Based on the differences in their industrial structure, it becomes clear why and how Houston and Dallas often find their economic performances at odds. In recent years, Dallas has moved away from its dependence on oil and toward more integration with the southwestern and national economies. It has substantial industrial diversity, as it serves an important national role in manufacturing, as well as the key regional role in many areas of finance and distribution for the Southwest. But Dallas industries are more intertwined with the national economy, which affects their prospects for success.

Four growth centers provide the foundation of Houston's economy—upstream oil, downstream oil, the space center and the medical center. Houston's industrial base is less diversified than Dallas', but these four centers bring additional factors into play. The national economy matters locally—and always has—but less than it does in Dallas. Oil and natural gas markets still move the Houston economy, as do chemical markets and public policies on health care and manned space flight. The international economy spills into Houston as well, affecting markets for oil, oil services, chemicals and international construction. Although it is less industrially diversified, Houston's economic growth and the risks to growth are spread over a different and wider range of outside forces than Dallas'.

NOTE: Jun Ishii, a student at Rice University, contributed to this article.

Houston employment data showed strong growth in the first quarter of 1995, according to the Texas Employment Commission, and the city has added 56,000 new jobs over the past 12 months. During the past year, the unemployment rate has fallen from 7 to 5.2 percent, and labor shortages and wage increases are being reported for some construction, clerical and blue-collar workers. Houston has not experienced its current growth rate of construction and manufacturing jobs since the Persian Gulf war ended.

RETAIL TRADE AND AUTO SALES

Individual retailers report improved performance in April, following a weak March. Stores with multiple locations in Texas continue to report that Houston is their slowest market, with any improvement in sales doing little more than matching inflation. At the same time, the sales tax report for Houston's first quarter showed one of the sharpest gains in citywide sales in four years. Retail problems seem to be related to overcapacity and not to weak demand. National retail chains continue to bring discount outlets to Houston, despite the existing high level of retail space per capita.

Local auto sales slowed down over the course of the first quarter, and April auto sales were 10.3 percent below those of April 1994. On a year-to-date basis, auto sales lag 1994 by 2.3 percent. For auto dealers, the poor April data are a disappointing start to the important spring sales period.

OIL SERVICES AND MACHINERY

Oil prices rose from $17 to $20 dollars per barrel in late March and April, offsetting some of the negative effects of weak natural gas prices. Prices for natural gas delivered to Gulf Coast pipelines rose about 30 cents in early March but have remained at a disappointing $1.65 per thousand cubic feet. The domestic rig count has lagged last year's drilling activity by about 7 percent, primarily because of weak gas prices. However, local oil service companies report that increased foreign drilling activity has more than compensated for revenue lost in the domestic market. Latin America—especially the countries of Argentina, Chile and Venezuela—is reported to be a strong drilling market. Activity in the Gulf of Mexico slowed in the first quarter but is expected to return to high levels of activity in coming months.

REFINING AND PETROCHEMICALS

Refining margins improved sharply in recent weeks, led by strong demand for gasoline. Oil product markets are recovering slowly from the effects of a warm winter and weak demand for fuel oil. A strong driving season pushed gasoline prices up faster than crude prices, and gasoline reached the highest prices seen in over two years. The recovery in profit margins started at very depressed levels, however, and refinery margins remain weak on historical standards.

Demand for petrochemicals remains very strong, both in domestic and export markets. Profits remain excellent, although prices for olefin products such as ethylene and propylene have leveled off in recent months. Prices have jumped for products related to synthetic fibers because of the run-up in cotton prices. Respondents were concerned about the apparent slowdown in autos and housing but reported they did not see it yet in orders, inventories or prices.

CONSTRUCTION AND REAL ESTATE

Building permits for the city of Houston were up 67 percent over last March and up 35 percent in the first quarter. Apartment construction and small- to medium-sized commercial construction activity led this improvement. Demand for warehouse/distribution center space remains very strong throughout the city, although a growing shortage of quality space has slowed leasing activity. Mexico's economic problems and disappointed expectations about the North American Free Trade Agreement (NAFTA) did not seem to affect demand for distribution facilities. Over a million square feet of industrial space is under construction in Houston. Home sales remain slow locally, with April sales of existing homes off 18 percent compared with last year. Sales of existing homes were weaker in April 1995 than in any April during the 1990s.

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