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Houston Business

A Perspective on the Houston Economy

Finding New Ways to Grow: Recovery in the Oil Patch

A pattern of local and city-specific accommodation to adversity allowed the Southwest to return to the forefront of national expansion.

In recent issues of *Houston Business*, we developed a list of 29 oil cities from various sources, looked at the role and performance of the oil industry in each city and analyzed how the oil industry affects local industrial structure. We found that oil industry employment in these cities continued to decline after 1987, largely in response to healthy and profitable trends in technology and productivity. The oil centers that gained most from these recent trends (or were hurt the least) were the largest oil cities, especially Houston. These large cities offered industry-specific knowledge, skills, and the sophisticated suppliers needed to function in a complex and global industry.

Our examination of the industrial structure of oil cities showed them to be less distinctive than popularly believed. The presence of a large oil extraction industry pulled the industrial profile of oil cities away from the norm for the United States, but many other cities—steel cities, auto cities, electronics cities, gambling cities—are pulled from the norm in the same way. With a few exceptions, these 29 cities showed significant concentrations of non-oil activities, suggesting that if oil were damaged, there were other paths available to economic growth and regional development.

This article looks at the economic recovery of Texas and Louisiana after 1987, and particularly at the role of regional oil cities as part of growth in these states. With some exceptions, the oil cities led the region's growth after 1987, and collectively they outperformed that of the United States. The rebound from a serious regional recession may exaggerate 1987–93 growth rates because such recoveries typically bring rapid growth. However, this is exactly the point: that recovery throughout the Southwest included cities tied closely to oil.

Houston provides us with a large and successful example.

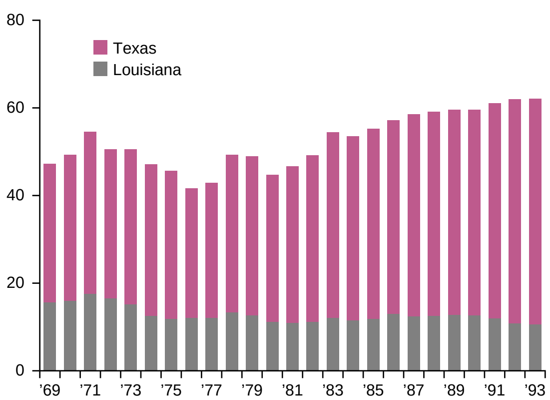
GROWTH IN 16 OIL CITIES

To examine recent growth trends we narrowed our focus from 29 oil cities to 16 located in Texas and Louisiana. Except for Tulsa, cities outside Texas and Louisiana have played a smaller and smaller role in the oil industry. The older corporate headquarters cities such as New York, Chicago, Los Angeles and Pittsburgh have given way to cities such as Houston, New Orleans and Dallas. Telecommunications diminished the need for immediate physical access to trading floors or Wall Street finance; specialized suppliers (advertising agencies, printers) proved willing to follow old customers to new headquarters cities in the Southwest.

Figure 1 shows total wages, salaries and benefits paid by the Texas and Louisiana oil industry from 1969 to 1993, and expresses it as a share of the U.S. oil industry. Between 1981 and 1987, Texas' share grew from 36 to 46 percent, and since 1987 it has grown to 52 percent. All of these percentage gains for the two states came from Houston and Dallas.

Table 1 shows our list of 16 oil cities and the increase in personal income that took place for each from 1987 to 1993, with the figures adjusted for inflation. Led by Laredo's NAFTA-induced expansion of 71.0 percent, four cities with many oil extraction employees were at the forefront of the regional economic recovery. Houston had the second-most-rapid growth with 31.3 percent, followed by Fort Worth and Corpus Christi with about 23 percent each. Ten cities grew faster than the 14.8 percent registered by the United States economy during this period, and real personal income in all 16 cities averaged 21.3 percent.

Figure 1
Oil Industry Wages in Texas and Louisiana
(Share of U.S. Wages, 1969–93)



SOURCE: Bureau of Economic Analysis.

Table 1
Increase in Income in 16 Southwest Oil Cities, 1987–93
(Percentage Increase in Inflation-Adjusted Dollars)

Grew faster than Texas and Louisiana	
Laredo	71.0
Houston	31.3
Fort Worth	23.6
Corpus Christi	23.2
Grew faster than United States	
Dallas	19.4
Lafayette	18.7
San Antonio	18.6
Tyler	16.7
Longview–Marshall	16.7
Houma	15.1
Grew slower than United States	
Midland–Odessa	10.6
Amarillo	9.1
New Orleans	8.3
Wichita Falls	8.2
Shreveport	7.8
Abilene	3.2
16 oil cities	21.3

SOURCE: Bureau of Economic Analysis, Regional Economic Information System and author's calculations.

BROADER COMPARISONS

Table 2 summarizes other measures of growth, and it makes comparisons to the earlier downturn from 1982 to 1987. The top of the chart summarizes the real income figures just discussed, and income in these 16 cities necessarily lagged the United States from 1982 to 1987. Income growth rates were one-third those of the United States during the oil bust, and the growth of total employment was similarly slow. Turning to the 1987–93 period, however, these results turn in favor of the oil cities.

The growth of income of the self-employed, or entrepreneurial income, was at the forefront of southwestern recovery. Table 2 shows the growth of both the income and the number of self-employed individuals in the 16 oil cities and the United States. From 1982 to 1987, the growth in the number of self-employed in the Southwest was at a rate nearly double that for the nation, a regrettable result of the shrinkage in the number of wage and salary jobs. At the same time, growth in the income of the self-employed was half that of the United States.

As widely predicted, however, these numbers turned around between 1987 and 1993. At the time, one of the oft-repeated maxims of the oil bust was that recovery would result from businesses established by competent and skilled people laid off during the downturn; new businesses were the seeds left by the forest fire, and economic renewal would grow from innovation and the success of their owners. At the time it may have seemed to be whistling in the dark, but Table 2 suggests this maxim was exactly right. From 1987 to 1993, the growth rate for self-employment in the 16 cities fell sharply to 8.2 percent, while the growth of entrepreneurial income jumped to 53.8 percent, a rate more than triple the 15.7 percent enjoyed nationwide. Table 4 shows that seven of the 16 oil cities had entrepreneurial income growth higher than that of Texas and Louisiana, and all but one city outperformed the United States.

CONCLUSION

On our list of 16 cities, there stands no better example of adjustment to adversity than Houston. The city lost more than one job in eight from 1982 to 1987, and then added all of them back by early 1990. The transformation of Houston's upstream oil industry to a stable white-collar, technology-based business has been the subject of recent newsletters. Low energy prices also meant low feedstock prices for Houston-based petrochemical producers, and by 1987 chemicals were in demand around the world. A huge expansion in petrochemical capacity along the Houston Ship Channel became a dominant feature of Houston's recovery years.

Houston's recovery also benefited from strong health-care-related job growth, and from the delivery of a major new space station project at the Johnson Space Center. The growth of companies such as Compaq, American General, BFI and BMI Software have let Houston share in national growth trends as well. The oil bust was a one-time mistake, an overdependence on an industry briefly subject to speculative excesses. The recovery exposed and proved the underlying strength of the city's economy.

We can tell similar stories for the other cities on our list. In Laredo, prospects for NAFTA meant trucking and warehousing would replace oil as the No. 1 industry. Also, if we could have extended the data to 1994, Dallas would fare much better in our comparison tables. The Southwest city best integrated into the national economy, Dallas enjoyed an excellent year as the U.S. economy heated up and added 3.3 million jobs in 1994. A pattern of local and city-specific accommodation to adversity allowed the Southwest to return to the forefront of national expansion.

Table 2
Growth of Real Income and Employment

	1982–87	1987–93
Personal income		
16 southwestern cities	7.0	21.3
Texas and Louisiana	6.5	20.4
United States	22.7	14.8
Total employment		
16 southwestern cities	5.9	11.2
Texas and Louisiana	5.5	11.3
United States	13.9	8.2
Self-employed income		
16 southwestern cities	34.9	53.8
Texas and Louisiana	29.4	46.5
United States	61.7	15.7
Number of self-employed		
16 southwestern cities	33.5	8.2
Texas and Louisiana	27.1	6.3
United States	15.7	12.4

SOURCE: Same as Table 1.

Table 3
Increase in Income of the Self-Employed
(Percentage Increase in Inflation-Adjusted Dollars)

Grew faster than Texas and Louisiana	
Laredo	133.5
Amarillo	93.7
Dallas	70.1
Fort Worth	65.3
Houston	59.7
Wichita Falls	57.6
Midland–Odessa	48.8
Grew faster than United States	
Longview	42.8
Tyler	40.5
Corpus Christi	37.2
San Antonio	36.8
Abilene	28.3
Lafayette	23.1
New Orleans	16.7
Shreveport	16.2
Grew slower than United States	
Houma	10.7
16 oil cities	53.8

SOURCE: Same as Table 1.

Houston respondents to the *Beige Book* survey continue to indicate a strong local economy. The combination of a healthy national economy and strong energy markets is producing robust retail sales, auto sales and home sales. The outlook is for an equally strong finish to 1996.

RETAIL AND AUTO SALES

Retailers are seeing an improving market in Houston, and most stores are seeing their sales running well ahead of last year on a same-store basis. Pricing remains difficult and heavy promotion is necessary, but customers are spending their money for goods that are properly positioned in a highly competitive retail market.

Auto sales for May lagged last year's levels by 1 percent, but it was still one of the best May performances of the last 10 years. This follows a very strong spring season for local auto dealers, with auto sales for the first five months running 6 percent ahead of last year.

OIL AND NATURAL GAS PRICES

Natural gas prices steadily improved in recent weeks, primarily because of the need to refill storage fields depleted by the cold winter. Prices are expected to stay over $2 for the summer as producers run at or near maximum levels to refill storage by next fall. A heat wave in Texas and other parts of the Southwest pushed spot prices at the Henry Hub in Louisiana to $2.60 in mid-June.

Crude prices fell from over $22 to near $20 in late May with the announcement that Iraq would re-enter world oil markets on a limited basis and for humanitarian purposes. Prices have been surprisingly resilient since that time, holding near $20 despite growing inventories. Wholesale gasoline prices initially stayed up as crude prices fell, giving refiners good profit margins; however, as crude prices stabilized in June, wholesale gasoline prices fell sharply. The result has been reduced refining margins and very low profits, especially on the Gulf Coast.

Crude prices are expected to fall further over the summer. Prices at the pump have been much slower to fall than wholesale prices, leaving retail margins strong even as refiners have struggled. However, a weaker-than-expected driving season may soon put downward pressure on pump prices.

PETROCHEMICALS

Chemical demand is strong and improving, inventories are in good shape, and contract prices are slowly increasing for ethylene, styrene and propylene. The industry remains profitable despite higher costs for oil and natural gas feedstocks. Demand is uneven across product lines, but strong demand for packaging materials such as bags, milk cartons and soda bottles is producing a tight market for polyethylene and polypropylene.

OIL SERVICES AND MACHINERY

Since the May *Beige Book*, domestic drilling is running 90 rigs ahead of last year, and Texas drilling is up by 40 rigs. Add growing international demand, the end of the spring thaw in Canada, and maximum levels of drilling in the Gulf of Mexico, and the market for oil field services and machinery is very strong. Natural gas drilling leads the improvement in domestic activity, especially in the Gulf of Mexico, which is wellpositioned to deliver gas to profitable East Coast markets. Both the Gulf of Mexico and the North Sea are constrained by equipment shortages, and rigs in the North Sea are now booked through most of 1997.

HOUSTON HOUSING MARKETS

High apartment occupancy, good job growth, and still-low interest rates drive a strong Houston housing market. Existing home sales hit the highest level for any May in the history of Houston, a 13 percent increase over last year, and one of the best months in the city's history. Median prices have shot up, primarily because the strongest activity has moved to the $200,000 to $500,000 range. New home sales were down slightly from April, but 6 percent ahead of last May. For the first five months of this year, new home sales were up 25 percent over last year. The inventory of new houses fell by 3 percent in May.

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