

Houston Economic Update

July 2012



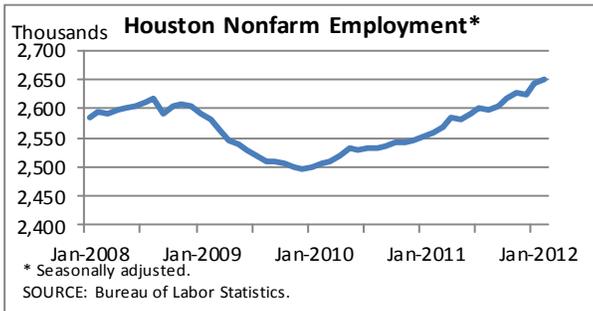
FEDERAL RESERVE BANK OF DALLAS, HOUSTON BRANCH

Houston Business Cycle



Economic activity in the Houston metropolitan area, as measured by the Federal Reserve Bank of Dallas business-cycle index, grew at an annualized rate of 2 percent in May, but April growth was revised up to 10 percent. Houston's connection to the global economy does pose some risks as expected slowdowns materialize around the world, but trends in hydrocarbon industries and manufacturing continue to drive a diversity of economic activity in the region. Thus, the outlook for Houston remains solidly positive.

Employment

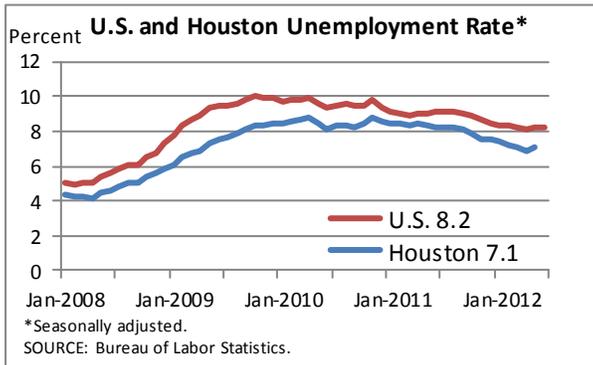


Nonfarm payroll employment grew at an annualized rate of 1.13 percent in May to nearly 2.66 million jobs. That is slower than the three-month average of 2.85 percent growth. On a percentage basis, financial activities had the largest one month gain with an annualized 25 percent jump, adding 2,900 jobs. The hospitality and manufacturing sectors were distant followers. The seasonally adjusted unemployment rate rose slightly from a revised 6.9 percent in April to 7.1 percent in May on a slight fall in the number of employed and a growing labor force. The U.S. unemployment rate held at 8.2 in June with no change in the labor force. Revisions to the prior two months were a wash, leaving the employment picture largely unchanged.

Employment Changes

Construction & mining	4.7
Manufacturing	5.3
Prof. & business services	0.0
Trade, transport, utilities	0.0
Leisure & hospitality	12.3
Other services	2.5
Information	2.6
Financial activities	9.6
Government	-2.0
Education & health services	3.2

Figures are three-period-average annualized monthly growth rates, ordered by descending industry percent contribution to real wage growth in third quarter 2011. Data are from the Bureau of Labor Statistics, seasonally adjusted by the Federal Reserve Bank of Dallas.



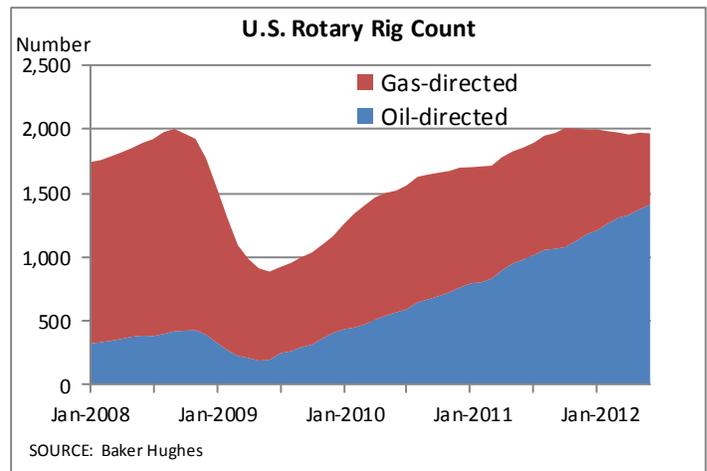
Manufacturing

Annualized manufacturing employment growth has been holding near 5 percent for the three months ending in May. Fabricated metal products continue to dominate growth in that sector with an unadjusted 17.8 percent increase in May, accounting for nearly half of all manufacturing jobs added. Manufacturing activity continues to grow, with demand for factory tools strong, but the skilled labor supply in the region is a significant constraint on local growth. The Houston purchasing managers index rose to 59.6 in May; the June reading for the U.S. fell again to 51.8. This would indicate a national slowdown and continued growth in the U.S. and Houston.



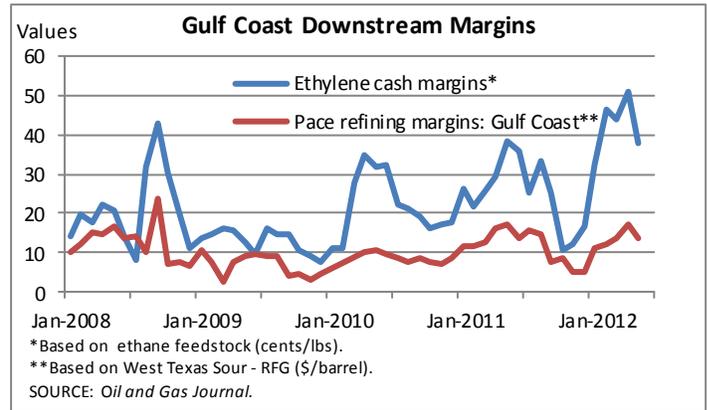
Upstream

The average daily price of West Texas Intermediate fell to \$82.30 last month, and the Seaway Pipeline reversal has yet to appreciably affect the discount of WTI relative to other crudes. The Henry Hub average spot price of natural gas climbed to \$2.46, making oil 5.7 to 6.7 times the price of gas on an energy-equivalent basis. The June average U.S. rig count fell to 1,970 on fewer gas rigs. Firms are moving human and physical assets seamlessly into liquids rich plays, and oil prices have room yet to fall before they begin affecting that activity. Oil now makes up nearly 73 percent of U.S. rig activity. Natural gas inventories are beginning to fall on decreased production, rising electricity demand and substitutions away from coal gas, but both crude oil and gas inventories remain above their five-year ranges.



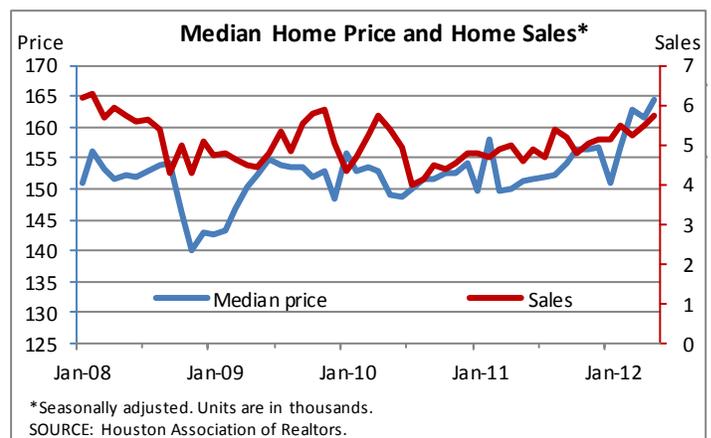
Downstream

Refiner margins remain healthy despite price declines, thanks to falling oil prices and low inventories of gasoline and diesel whose prices fell over 9 percent in June to average \$2.51 and \$2.67 on the Gulf Coast. U.S. consumption of gasoline and other refined petroleum products improved on seasonal strength and lower prices. Resin prices are flat to down over June, inventories are high and railcar loadings are down. Softening global demand, lower feedstock prices, a strengthening dollar, and the recovery of capacity from unplanned plant outages have all contributed significantly to recent price moves. Despite falling prices, margins in the ethane-polyethylene product chain are largely unaffected.



Real Estate

The growth rate of existing-home sales, averaged over the last three months and seasonally adjusted, fell to 1.5 percent in May. New single-family housing starts have climbed for three consecutive months, and permits declined in June. Both permits and starts remain in positive growth trends on a seasonally adjusted basis. Foreclosure sales remain a disconcertingly high proportion of total sales. Housing inventory fell to 5.1 months in Houston, a very healthy number. Commercial real estate continues to boom, particularly in office space. Trends in rents and occupancy for industrial, office and retail properties all remain in healthy territory as spillovers from the Shale Revolution continue to draw firms from nearly all sectors to the city.



Forecasts: Expectations for most of the world have eroded, Texas still likely to outpace the U.S.

- The Federal Reserve Bank of Dallas forecast of employment growth in Texas this year was revised down to between 2.5 and 3 percent.
- Expectations were revised down in July for the U.S. The second half of the year is expected to see acceleration to an annualized fourth-quarter real growth rate of 2.3 percent.
- July's Blue Chip Economic Consensus Forecasts of 2012 growth were 8 percent for China, 3.7 percent for Mexico, 2.6 percent for Brazil and -0.5 percent for the euro zone.