



Regional Economy Continues to Pick Up Steam

May 3, 2010

Economic conditions have firmed up in Texas over the past six weeks, and new data and anecdotal evidence suggest that a recovery is under way in the state. Texas payroll employment is growing at a modest pace, and the Texas Business-Cycle Index has increased for three consecutive months. Factory output is expanding, residential real estate is firming up, and retail sales and exports are rising. The Texas Leading Index continues to show gains, consistent with gradual improvement.

However, risks to the recovery remain. Improvement in the residential real estate market continues to be buoyed by the homebuyer tax credit, which expired on April 30. The commercial real estate sector remains weak and is unlikely to see a significant turnaround for some time.

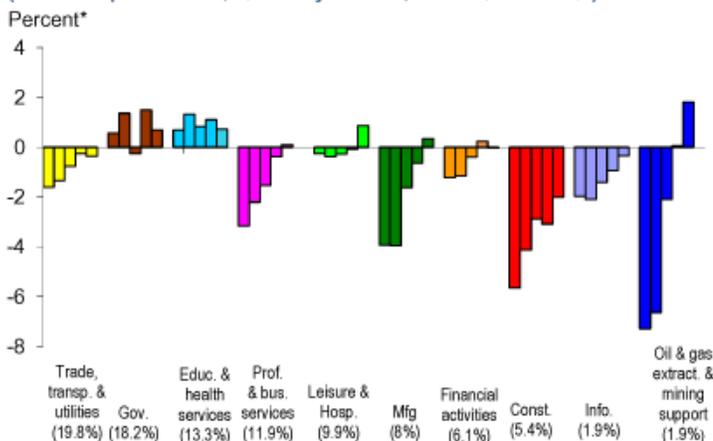
Economic Activity Expanding

The state's business-cycle index, which tracks movements in employment, the unemployment rate and state GDP, rose 1.5 percent (annualized) in March. The increase marked the third consecutive month of positive growth in the index, signaling that the state's economy is in recovery (*Chart 1*).

Labor Market Firms Up

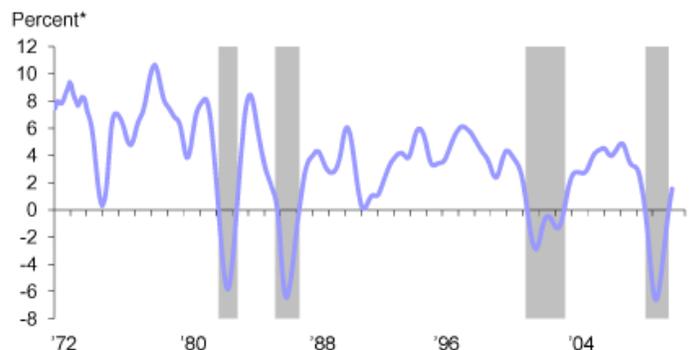
Texas employers continued to expand their payrolls in March, adding 8,200 jobs. This increase puts first quarter job growth at 1 percent (annualized), twice the nation's increase of 0.5 percent (*Chart 2*). Job gains were widespread across industries in the first quarter (*Chart 3*).

Chart 3
Job Gains Becoming Widespread Across Sectors
(NAICS Super Sectors, Quarterly Growth, 2009:Q1–2010:Q1)



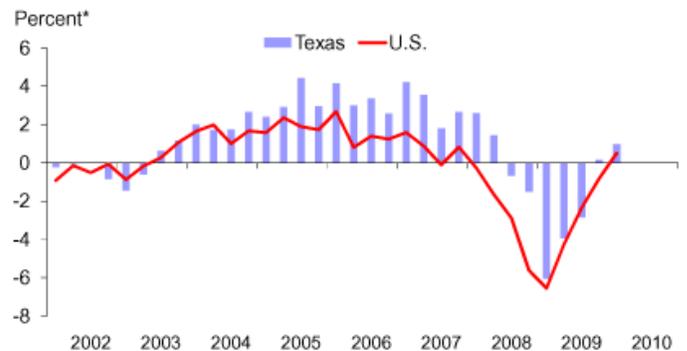
*Quarter/quarter, seasonally adjusted.
SOURCES: Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Chart 1
Texas Recovery Under Way
(Texas Business-Cycle Index)



*Month/month, seasonally adjusted, annualized rate.
NOTE: Shaded areas indicate Texas recessions.
SOURCE: Federal Reserve Bank of Dallas.

Chart 2
Texas Job Growth Positive in First Quarter



*Quarterly job growth is the annualized change of the final month of the quarter from the final month of the previous quarter.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

The Texas unemployment rate has held steady at 8.2 percent for five straight months and remains below the national average of 9.7 percent. Unemployment claims continue to decline, however, and currently are at their lowest level since late 2008, suggesting that the unemployment rate is near or at its high point.

Residential Real Estate Sees Continued Improvement

Boosted by the first-time homebuyer tax credit, affordable home prices and relatively low mortgage rates, existing-home sales climbed 10.9 percent in March and are 12.5 percent above year-ago levels. Sales activity is strong across all major metros.

While the continued strength in sales is encouraging, it is likely that growth in home sales will pause in a few months with the expiration of the tax credit. As long as a binding sales contract was signed by April 30, a home purchase completed by June 30 will qualify.

Single-family housing permits and contract values bottomed out in spring 2009 and have been rising strongly since. Single-family contract values rose 1.8 percent in March and are up 54 percent from their levels a year ago. Single-family permits were up 43 percent in March from year-earlier levels. The sharp rise suggests that homebuilders ramped up construction in hopes of sales and closing before the expiration of the tax credit.

Commercial Real Estate May Be Nearing Bottom

Recent anecdotal reports suggest that the commercial real estate sector may be nearing bottom. In the April Beige Book, contacts noted that lower rental rates have spurred leasing activity in the office, apartment and industrial markets. While absorption has improved, contacts do not expect construction to pick up any time soon. Building activity continued to decline in March, and contract values for office buildings, warehouses and hotels were down significantly compared with year-ago levels.

On the investment side, business contacts note that property sales activity remains at a low level but is slowly ticking up.

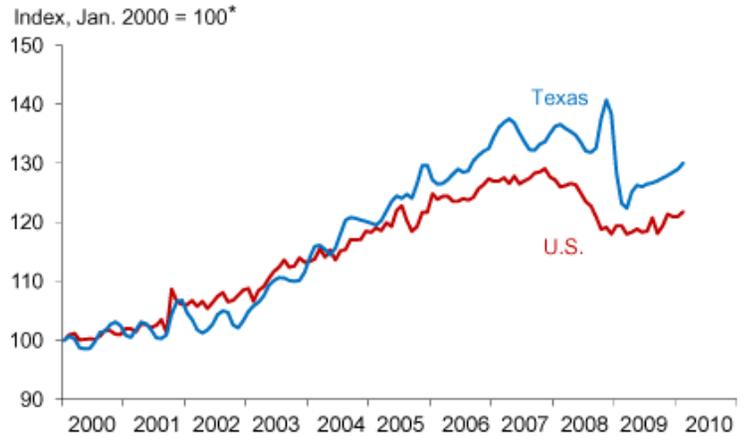
Retail Sales Surge

Texas real retail sales grew a solid 9.7 percent (annualized) in February, marking the eighth straight month of growth. After falling steeply, Texas sales began recovering in spring 2009 and currently are above year-ago levels (*Chart 4*). Increases in sales reflect improved consumer confidence.

Manufacturing Activity Rebounds

The April Texas Manufacturing Outlook Survey confirmed that the state's manufacturing sector is rebounding after a prolonged decline. The survey's production index expanded

**Chart 4
Texas Retail Sales Rising**



*Seasonally adjusted real dollars.
SOURCES: U.S. retail sales data are from the Census Bureau and have been deflated using the Bureau of Economic Analysis retail sales deflator. Texas retail sales estimated by the Federal Reserve Bank of Dallas; data are benchmarked quarterly to retail sales produced by the Texas Comptroller of Accounts.

for the sixth straight month and rose to its highest level since mid-2007. Other survey indexes such as new orders and shipments, although volatile from month to month, have been positive for two consecutive months, signaling moderate growth in the sector. Business sentiment in the sector has also improved, with the survey's business activity and company outlook indexes rising sharply in both March and April.

Exports Are Rising

Aided by the falling dollar and a pickup in global demand, real Texas exports climbed 7.6 percent in February, following an increase of 20.3 percent in the second half of 2009. Anecdotal reports from the April Beige Book confirm this increase, with transportation service contacts in cargo, rail and intermodal trade noting continued improvement in demand.

Conclusion and Outlook

The Texas Leading Index rose 1 percent in February and has increased 12.5 percent since its March 2009 low (*Chart 5*). Most components of the Leading Index have ticked up since December, reflecting broad-based improvements in the regional economy. Continued strength in this index suggests Texas will likely see modest employment growth between 1.5 and 2.5 percent this year.

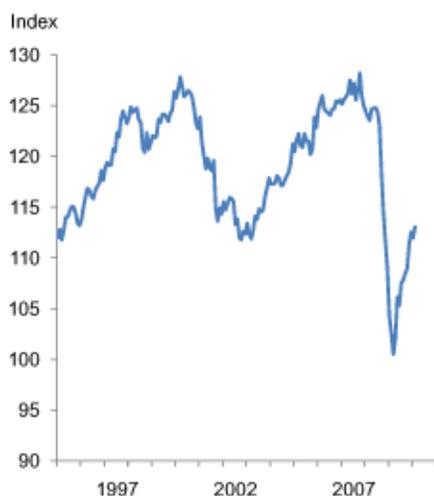
—Mike Nicholson and Laila Assanie

About the Authors

Nicholson is a research analyst and Assanie is an associate economist in the Research Department at the Federal Reserve Bank of Dallas.

Regional Economic Update can be found online at www.dallasfed.org/research/

**Chart 5a
Texas Leading Index Continues to Climb**



SOURCE: Federal Reserve Bank of Dallas.

**Chart 5b
Texas Leading Index 3-Month Change**

