

# Introduction

Mine Yücel



The economic landscape of Texas is changing. The state lost more than 200,000 jobs during the tech bust and recent recession. A majority of these jobs were in the high-tech sector, which was the main driver of the Texas economy in the 1990s. With the decimation of the tech sector, which industry will be the driver of the Texas economy in the future? This monograph doesn't attempt to answer that question, but we explore some of the ways the Texas economy has been changing and some of the current issues facing it.

The state has gone through boom and bust cycles before, but each downturn has been followed by a stronger and more diverse economy. The oil bust was particular to Texas and hurt the state's economy, while low oil prices helped the rest of the nation. The tech bust, on the other hand, was experienced similarly in Texas and the nation. Texas bore a larger brunt because it had a higher share of high-tech manufacturing and service industries than the nation.

While the drivers of the economy may change, one constant is the close relationship the state has with the Mexican economy. The interconnection is crucial to the border economies and is a big factor in the changing demographics of Texas.

## Structural Change

The articles in this publication discuss some of the changes in the economic landscape of our state. Mine Yücel looks at the Texas economy's performance during the most recent recession and explains why it was different from previous recessions. She argues that unlike previous recessions, the most recent recession was primarily due to a high-tech bust rather than an oil price shock. Although oil prices were relatively high during the recession, they did not benefit Texas as much as in the past because the state has diversified away from oil. In addition, she shows that the high-tech sector grew very fast in Texas in the 1990s, to a share higher than the national average. Texas' higher share of industries that were hit hard in

this recession was a major factor in the state's prolonged downturn.

Pia Orrenius, Jason Saving and Priscilla Caputo survey the weak jobless recovery after the most recent recession and suggest that it may be caused by structural change in the Texas labor market. They note that structural change is not new to Texas. The state went through structural change in the 1980s after the oil bust and may be going through another one now. They show that the high-tech and apparel industries are undergoing structural losses, while the health care, education and government sectors are undergoing structural gains. But, just as the oil industry decline paved the way for the diversification and growth of the Texas economy a decade later, the structural change going on today will pave the way for a more dynamic and prosperous Texas.

## Oil's Impact

The oil industry has been undergoing change for the past 20 years, shrinking while other sectors of the Texas economy have grown. The Texas economy's diversification away from energy and the energy sector's declining importance prompt Stephen Brown and Mine Yücel to ask whether high oil prices are still a benefit to the Texas economy. They show that higher energy prices still benefit the state—even though it is by less than in the boom years of the 1970s and early '80s. They also find evidence that the Texas economy has become less sensitive to fluctuations in oil prices than it was in the '70s and '80s. First, oilfield activity has become less sensitive to fluctuations in energy prices. Second, the energy industry makes up a smaller share of the Texas economy than it used to. Together these factors mean that Texas output is about 15 percent as sensitive to oil price fluctuations as it was from 1970 to 1988. Texas employment no longer seems to be positively affected by oil price fluctuations.

## Business Mix

Laila Assanie and Mine Yücel outline the importance of industry agglomeration to an economic growth. They highlight the key clusters in Texas and its six major metropolitan areas through economic base analysis. They find that oil and gas extraction and its support activities, pipelines, natural gas distribution, refining and oil-

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field-machinery manufacturing are still agglomerated in Texas. However, high-tech and transportation industries have been added to this mix. Computers, telecommunication services, semiconductors and air transportation firms now have a larger presence in Texas than in the nation as a whole.

Bill Gilmer analyzes per capita income growth in various regions of the Texas economy. He shows that the state economy has been growing rapidly since 1969, either matching or exceeding the nation's growth. But the Texas Triangle cities of Houston, Dallas/Fort Worth, Austin and San Antonio grew faster than average. Outside the Texas Triangle, income growth was much slower, although population growth was not. Especially after 1989, the Texas Triangle cities contributed three-fourths of the state's income growth. Gilmer notes that the Mexican border area represents a challenge to state economic development because the border cities' average per capita income is only 50 to 60 percent of the national average. The border saw explosive gains in the '90s following the passage of NAFTA and the growth of the maquiladora industry, but high population growth and high in-migration rates kept income per capita low in this area. The article also explains that the growth in wages and salaries after 1989 came through a change in industry mix as the economy shed low-wage jobs and replaced them with better-paying ones.

### Border Influence

Texas border cities are a unique blend of U.S. and Mexican cultures, languages and customs and follow the ups and downs of the Mexican and U.S. economies. Keith Phillips and Roberto Coronado look at how border cities on the Texas side benefit from cross-border traffic by consumers from their sister cities on the Mexican side. They estimate retail sales in four metro areas along the Texas–Mexico border. They find that in 2001, retail sales to Mexican nationals accounted for nearly 20 percent of retail sales in border metros. Laredo had the highest share, with 41 percent of its retail sales going to consumers from across the border. Phillips and Coronado also show that unexpected changes in the peso's real value affected these border metros

because retail sales strength varied closely with peso strength, especially in Laredo and McAllen.

Another perspective on border cities is presented by Jesus Cañas, Roberto Coronado and Bill Gilmer. They show how expansions and contractions of the maquiladora industry have affected Texas border cities. NAFTA's passage and the peso devaluation in the early '90s led to maquiladora growth and the relocation of component parts and material suppliers to Texas cities along the border. Texas border cities developed rapidly in the '90s as part of this supply chain. Cañas, Coronado and Gilmer observe that proximity to the U.S. market becomes a crucial advantage for the maquiladoras when there is a short inventory cycle, when the weight-to-value ratio of goods is high, when there is frequent retooling, when quality is more important than price and when intellectual property rights are critical. However, they note that the state is unlikely to repeat the banner performance of the '90s as foreign competition slows the growth of Texas border-city suppliers to the maquiladora industry. Hence, Texas may see less stimulus in the future from maquiladora expansion.

### Population Shift

Finally, D'Ann Petersen and Laila Assanie discuss Texas' changing demographic makeup and how it will shape the economy. Texas' population is faster growing, younger and more ethnically diverse than the nation's. The Hispanic population will be the dominant force in Texas by 2020. The authors demonstrate that there are large disparities between ethnic groups in income and education. Such disparities may imply a decline in real income and a lower-skilled and less-educated labor force in Texas compared with the nation. On the other hand, the young and fast-growing population also means Texas' housing market may continue to be vibrant even as the baby boomers age. Texas' challenge is to reduce the disparities and make our differences work for us.

*Yücel is a senior economist and vice president in the Research Department of the Federal Reserve Bank of Dallas.*