Texas **Service Sector** Outlook Survey

December 27, 2017

Texas Service Sector Activity Remains Solid

Texas service sector activity continued to increase in December, according to business executives responding to the Texas Service Sector Outlook Survey. The revenue index, a key measure of state service sector conditions, was unchanged at 24.4 in December.

Labor market indicators reflected faster employment growth and longer workweeks this month. The employment index rose from 9.8 to 15.3. The hours worked index edged up to 9.2.

Perceptions of broader economic conditions continued to reflect optimism in December. The general business activity index edged down two points to 18.1. The company outlook index moved up to 19.6, its highest reading this year, with 26 percent of respondents reporting that their outlook improved from last month and 7 percent noting it worsened.

Price and wage pressures increased this month. The selling prices index advanced nine points to 16.6. The wages and benefits index ticked up one point to 20.1, although the majority of firms continued to note no change in compensation costs.

Respondents' expectations regarding future business conditions reflected more optimism in December. The index of future general business activity edged up from 33.0 to 35.0. The index of future company outlook rose slightly from 32.0 to 33.5. Indexes of future service sector activity, such as future revenue and employment, also reflected more optimism this month.

Texas **Retail** Outlook Survey

Retail Sales Expand but at a Slower Pace

Retail sales increased in December, albeit at a slower pace than last month, according to business executives responding to the Texas Retail Outlook Survey. The sales index fell from 30.4 in November to 25.6 in December. Inventories increased at a similar pace as last month.

Labor market measures indicated faster retail employment growth and markedly longer workweeks this month. The employment index jumped 11 points to 13.1. The hours worked index rose sharply from 5.6 to 15.8, its highest reading in over 10 years.

Retailers' perceptions of broader economic conditions continued to reflect optimism in December. The general business activity index fell from 25.4 to 20.9. The company outlook index was similar to last month at 24.7, with 29 percent of respondents reporting that their outlook improved from last month and 5 percent noting it worsened.

Retail price pressures were unchanged while wage pressures eased slightly this month. The selling prices index held steady at 26.0, suggesting prices rose at the same pace as last month. The wages and benefits index dipped two points to 13.9, although the great majority of firms continued to note no change in compensation costs.

Retailers' perceptions of future broader economic conditions reflected more optimism in December. The index of future general business activity jumped 10 points to 31.5. The index of future company outlook advanced from 24.6 to 33.4. Indexes of future retail sector activity also reflected more optimism this month.

The Texas Retail Outlook Survey (TROS) is a component of the TSSOS that uses information only from respondents in the retail and wholesale sectors.

Next release: January 30, 2018

Data were collected Dec. 12–20, and 282 Texas business executives responded to the survey. The Dallas Fed conducts the Texas Service Sector Outlook Survey monthly to obtain a timely assessment of the state's service sector activity. Firms are asked whether revenue, employment, prices, general business activity and other indicators increased, decreased or remained unchanged over the previous month.

Survey responses are used to calculate an index for each indicator. Each index is calculated by subtracting the percentage of respondents reporting a decrease from the percentage reporting an increase. When the share of firms reporting an increase exceeds the share reporting a decrease, the index will be greater than zero, suggesting the indicator has increased over the prior month. If the share of firms reporting a decrease exceeds the share reporting an increase, the index will be below zero, suggesting the indicator has decreased over the prior month. An index will be zero when the number of firms reporting an increase is equal to the number of firms reporting a decrease. Data have been seasonally adjusted as necessary.

Texas Service Sector Outlook Survey

Business Indicators Relating to Facilities and Products in Texas
Current (versus previous month)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Revenue	24.4	24.4	0.0	Increasing	97	35.4	53.6	11.0
Employment	15.3	9.8	+5.5	Increasing	94	21.1	73.1	5.8
Part-Time Employment	5.6	4.8	+0.8	Increasing	18	8.9	87.8	3.3
Hours Worked	9.2	7.9	+1.3	Increasing	14	12.0	85.2	2.8
Wages and Benefits	20.1	19.1	+1.0	Increasing	99	21.7	76.7	1.6
Input Prices	33.3	30.8	+2.5	Increasing	104	33.9	65.5	0.6
Selling Prices	16.6	7.2	+9.4	Increasing	22	22.6	71.4	6.0
Capital Expenditures	13.4	14.8	–1.4	Increasing	100	18.3	76.7	4.9

General Business Conditions
Current (versus previous month)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	19.6	14.2	+5.4	Improving	18	26.1	67.4	6.5
General Business Activity	18.1	20.4	–2.3	Improving	16	25.1	68.0	7.0

Business Indicators Relating to Facilities and Products in Texas
Future (six months ahead)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Revenue	56.3	48.9	+7.4	Increasing	106	64.6	27.1	8.3
Employment	30.6	30.5	+0.1	Increasing	105	38.2	54.2	7.6
Part-Time Employment	13.3	12.9	+0.4	Increasing	66	17.8	77.7	4.5
Hours Worked	12.3	8.5	+3.8	Increasing	16	16.2	79.9	3.9
Wages and Benefits	47.6	43.8	+3.8	Increasing	132	50.0	47.6	2.4
Input Prices	51.4	49.6	+1.8	Increasing	132	52.9	45.7	1.5
Selling Prices	37.8	30.1	+7.7	Increasing	104	41.6	54.6	3.8
Capital Expenditures	35.7	28.6	+7.1	Increasing	105	40.1	55.5	4.4

General Business Conditions
Future (six months ahead)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	33.5	32.0	+1.5	Improving	22	40.2	53.1	6.7
General Business Activity	35.0	33.0	+2.0	Improving	22	38.2	58.6	3.2

Texas Retail Outlook Survey

Business Indicators Relating to Facilities and Products in Texas
Retail (versus previous month)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Retail Activity in Texas								
Sales	25.6	30.4	−4.8	Increasing	5	36.5	52.6	10.9
Employment	13.1	2.0	+11.1	Increasing	4	13.2	86.7	0.1
Part-Time Employment	12.1	7.1	+5.0	Increasing	3	13.8	84.5	1.7
Hours Worked	15.8	5.6	+10.2	Increasing	6	16.1	83.6	0.3
Wages and Benefits	13.9	16.0	−2.1	Increasing	82	14.4	85.1	0.5
Input Prices	31.8	31.1	+0.7	Increasing	23	33.3	65.2	1.5
Selling Prices	26.0	26.1	−0.1	Increasing	8	32.5	61.0	6.5
Capital Expenditures	17.3	12.3	+5.0	Increasing	17	20.7	75.9	3.4
Inventories	5.3	4.6	+0.7	Increasing	15	18.6	68.1	13.3
Companywide Retail Activity								
Companywide Sales	25.4	22.1	+3.3	Increasing	5	31.3	62.8	5.9
Companywide Internet Sales	14.3	12.1	+2.2	Increasing	11	17.2	79.9	2.9

General Business Conditions, Retail
Current (versus previous month)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	24.7	24.6	+0.1	Improving	5	29.4	65.9	4.7
General Business Activity	20.9	25.4	−4.5	Improving	7	26.2	68.5	5.3

Business Indicators Relating to Facilities and Products in Texas, Retail
Future (six months ahead)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Retail Activity in Texas								
Sales	41.9	30.8	+11.1	Increasing	106	50.6	40.7	8.7
Employment	22.6	16.8	+5.8	Increasing	7	25.0	72.6	2.4
Part-Time Employment	9.2	8.2	+1.0	Increasing	4	9.9	89.4	0.7
Hours Worked	11.6	4.5	+7.1	Increasing	5	16.5	78.6	4.9
Wages and Benefits	35.3	27.8	+7.5	Increasing	108	37.2	60.9	1.9
Input Prices	47.3	33.9	+13.4	Increasing	104	49.1	49.1	1.8
Selling Prices	43.6	35.7	+7.9	Increasing	104	49.1	45.5	5.5
Capital Expenditures	40.0	17.8	+22.2	Increasing	15	41.8	56.4	1.8
Inventories	16.7	13.3	+3.4	Increasing	14	28.4	59.9	11.7
Companywide Retail Activity								
Companywide Sales	48.4	16.6	+31.8	Increasing	105	53.2	42.0	4.8
Companywide Internet Sales	13.8	17.1	–3.3	Increasing	17	19.4	75.0	5.6

General Business Conditions, Retail
Future (six months ahead)

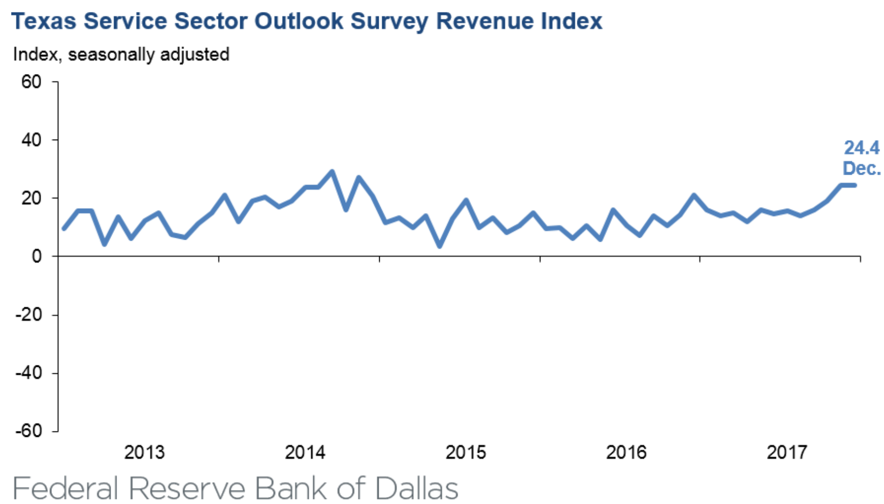
Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	33.4	24.6	+8.8	Improving	13	37.2	59.0	3.8
General Business Activity	31.5	21.4	+10.1	Improving	16	34.4	62.7	2.9

*Indicator direction refers to this month's index. If index is positive (negative), indicator is increasing (decreasing) or improving (worsening). If zero, indicator is unchanged.

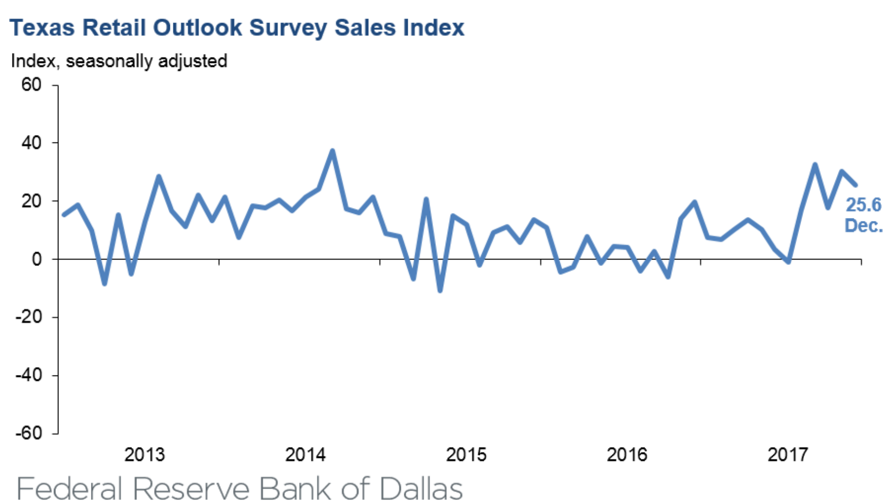
**Number of months moving in current direction.

Data have been seasonally adjusted as necessary.

Texas Service Sector Outlook Survey



Texas Retail Outlook Survey



Texas Service Sector Outlook Survey

December 27, 2017

Comments from Survey Respondents

Telecommunications

- We are starting to see some improvements in growth and revenue since the flooding in late August and early September. New-home construction has increased along with new-lot construction. There is still significant concern with large companies leaving Houston due to three floods in less than 24 months.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

- We rely on the oil and gas industry. New products in different markets, when combined with an uptick in the oil and gas industry, give us a better outlook for the present and the next few months.

Credit Intermediation and Related Activities

- With hunting, the holiday season and the wind-generator field construction, traffic is heavy. Local sales tax revenues increased 17 percent for the month versus October. In addition, there is a new power line coming through the county. The school districts are developing plans for new expansions as a result of the impending increase in tax revenue from increased taxable value of the wind farm. All we really need is a good rain now and in six months.
- Capital expenditures are due to Hurricane Harvey.

Insurance Carriers and Related Activities

- We are insurance brokers and we are seeing insurance prices going up in property due to hurricanes and wildfires. Business auto insurance is going up due to worsening experiences contributed to somewhat by distracted driving.

Real Estate

- This time of year is slow for real estate sales.

Professional, Scientific and Technical Services

- The overall business climate and customer purchases are very, very strong. After eight years, we are seeing huge growth numbers in 2017 like we saw last in 2007 and part of 2008.
- A year-end revenue push will help with December results, and we are now ahead of previous-year revenue numbers. With some progress in Washington, particularly with the impending passage of the new tax plan, we believe increased activity experienced in 2017 will carry into 2018. There is a lot to watch next year, and risks do exist but seem somewhat contained for the immediate future. We will have to watch earnings closely, along with Fed action. There may be a few global bumps perhaps but most seem to be understood for now.
- We reduced employees due to a change in a customer agreement.
- Notwithstanding the political headwinds, both nationally and in Texas, both we and the clients that I have spoken with are a bit more bullish on 2018. Tax reform could spark some increased merger and acquisition activity, and energy prices seem to be stabilizing and trending toward increase, all of which can help the legal services business.
- The level of major projects coming from Fortune 100 companies picked up in the fourth quarter. We don't expect any changes going into December but expect that the improved project volume of the fourth quarter will continue into most of 2018.
- The commercial real estate market has cooled off slightly over the past year, and the high-end residential market continues to slow down. We do not anticipate a significant correction in the market, but we are forecasting a 5 to 10 percent reduction in revenue for 2018.
- General business activity is up, and we plan to see strengthening in 2018 based upon an improved oil and gas market and increased domestic production due to improved international market penetration.

Management of Companies and Enterprises

- The uncertainty of regulation coming from the federal level has many people frustrated and sitting on the sidelines.
- I'm not sure the overall business environment is as strong as the Federal Open Market Committee (FOMC) thinks. I find it interesting that the FOMC continues to raise short-term rates at a time when the yield curve is getting very close to an inversion, and the raising of interest rates is having no impact on the much-desired inflation rate sought by the FOMC.

Administrative and Support Services

- We may be seeing a fundamental change in the IT staffing industry where most companies of any reasonable size have their own recruiting personnel. They are hiring both full-time and contractor employees but are doing it directly.
- Our operations have slowed down in all sectors since November, and this is not our normal seasonal change. Since October 2017, the trend has been a 7.2 percent decrease in sales. My professional opinion is that companies are not wanting to invest, divest, make, repair or order anything until they have to and are waiting on some direction from the government as to what will happen in the future regarding regulations, wars and monetary policy. Tax reform, if it passes and I hope it does as a business owner, will be an immediate fix to this short-term problem; long term, I have my doubts. The aviation sector overall has decreased by 4.6 percent since October; this is outside our normal decrease of 1.8 percent seen at this time. The corporate jet sector has remained consistent, with the majority of the loss being in heavy commercial and aircraft part manufacturing facilities. The industrial sector has remained flat, with no change in request for quotes (RFQs) or sales. We see very little on the horizon as far RFQs being submitted by the end of 2017. The military-part manufacturing facilities' sales have declined 3 percent since October. We are told by our customers in this sector that in January 2018, we should see a pickup in their submittal of RFQs.
- We have lost several long-term clients in the restaurant business due to poor performance requiring cutbacks. We continue to see opportunity in the real estate sector.
- Lack of labor prevents growth.

Educational Services

- I feel the optimism in the air from the top to the bottom. I am looking forward to tax cuts, more regulatory rollbacks and controlling spending.

Ambulatory Health Care Services

- We are expecting a decline in revenue based on insurance and Medicare fee adjustments. We expect to see an increase in benefit costs, but 5 percent or less.
- Revenue and overall company growth are fueled mostly by a broader range of services to existing clients, plus an expectation for new-client growth as a result of increasing our service offerings. Increases in revenue are offset by reductions in government health care reimbursement rates. Capital expenditure spending is almost double this year's level as we invest in infrastructure to support growth.
- In the health care sector, with the advent of managed Medicare, many patients are not able to afford their deductibles and are foregoing their care. Managed Medicare plans are suitable for healthy Medicare beneficiaries. But for the ones who need to go to the hospital or need home health or hospice services, individual deductibles range from $500 to $5,000 (sold in order to lower the premium). Patients unable to meet their deductibles when they need it most results in them ending up in emergency rooms.

Hospitals

- Congress continues to pass legislation taking dollars from rural health systems—we are going to start seeing more and more health systems fail as the insurance companies merge into health care.

Nursing and Residential Care Facilities

- There is continued uncertainty in the health care marketplace, largely driven by inconsistent, variable Medicare/Medicaid funding mechanisms and disruption in physician practices. Wage pressure is escalating and spot supply shortages, particularly medication shortages, are stressing health care providers. We are experiencing a modest seasonal uptick in volumes, due largely to localized increases in upper respiratory, gastrointestinal and influenza illnesses.

Amusement, Gambling and Recreation Industries

- Besides the continuing problem with the city of Austin's concept of eliminating parking downtown and no good public transportation alternatives, these are our latest issues: the city wants to make businesses provide guaranteed sick pay to full- and part-time employees; it is virtually impossible to hire construction workers, and when you can get people, they are more than likely not as qualified as we would need them to be to do a good job; because the construction industry is so short-handed (with many going to Houston after the hurricane) bids to do jobs are skyrocketing; and the price of real estate in downtown Austin is so high that property taxes have gone through the roof—in the last two years, our property taxes have increased by over $2,000 a month.

Food Services and Drinking Places

- We are in the midst of recovery from Hurricane Harvey. We are projecting a partial reopening to be in April.
- We have continued the strong sales increases in December that we have had for the last couple of months. It definitely looks like more than a short-term bounce, and we have shifted our longer-term outlook a little higher as a result. We are doing more sales with no more labor. We are at that point where the higher volume is letting us be more efficient with the labor we already have scheduled rather than having to add much in the way of additional labor. We will have a substantial increase in the cost of benefits starting Jan. 1.
- We are cautiously optimistic.
- We are still short labor.

Personal and Laundry Services

- Hiring and retaining quality stylists and barbers has been a recent challenge, so I had to evaluate and change the compensation plan from an hourly wage to a commission system. This, in turn, will reward the most productive employees but will also increase my labor expense by 8 to 12 percent. I had to do this to stay competitive in my industry.

Support Activities for Transportation

- Currently, our business is down for the year—the last quarter in particular has seen a drop in revenue.
- Our outlook depends on the NAFTA negotiations. We need for the agreement to remain in place and to get improved.

Merchant Wholesalers, Durable Goods

- We will continue to invest in technology to meet the ever-growing demands of the digital world.
- Our Houston market is very strong right now and appears to be increasing in strength. Seasonally, this is our slow time, and across the state we are up over last year.

Merchant Wholesalers, Nondurable Goods

- Insurance premiums under the Affordable Care Act are up for 2018. Employee benefit costs are rising. Retail competition from the internet continues to increase. Labor and labor costs are the main areas where costs can be reduced.
- We see price increases coming from our suppliers that we hope to pass on to our customers in the first quarter of 2018. Time will tell if it happens.

Motor Vehicle and Parts Dealers

- Margins on new-vehicle sales continue to decline.
- Our six-month outlook will be influenced by tax reform. Increases in interest rates are a concern for our business. Any increase impacts us because of inventory.

Building Material and Garden Equipment and Supplies Dealers

- Possible income tax changes currently under Congressional consideration are not expected to have a material impact on any of our business indicators.

Clothing and Clothing Accessories Stores

- Retail sales in oil patch markets have stabilized versus last year.

Questions regarding the Texas Service Sector Outlook Survey can be addressed to Amy Jordan at amy.jordan@dal.frb.org.