Texas **Service Sector** Outlook Survey

January 2, 2019

Texas Service Sector Activity Decelerates

What's New This Month

For this month's survey, Texas business executives were asked supplemental questions on wages and prices. Results for these questions from the Texas Manufacturing Outlook Survey, Texas Service Sector Outlook Survey and Texas Retail Outlook Survey have been released together.

Texas service sector activity grew at a slower pace 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, fell over 11 points to 10.1 in December.

Labor market indicators reflected an uptick in employment growth and slightly longer workweeks this month. The employment index rose from 8.7 in November to 9.9 in December, while the hours worked index declined from 7.5 to 1.9.

Perceptions of broader economic conditions turned negative, and uncertainty increased this month. The general business activity index fell over 16 points to -5.0, its lowest reading since early 2016, while the company outlook index saw a similar decline from 12.0 in November to -4.4 in December. The outlook uncertainty index rose to a new high of 15.0.

Price and wage pressures eased slightly this month, though they remain elevated compared with historical levels. The wages and benefits index dipped from 20.9 in November to 19.8 in December, while the selling price index fell nearly two points to 10.5.

Respondents' expectations regarding future business conditions softened considerably in December. The future general business activity index plummeted nearly 22 points to -5.0 in December, its first negative reading in over two years, while the future company outlook index fell from 17.3 to 1.6. Other indexes of future service sector activity, such as revenue and employment, also fell but remained positive.

Texas **Retail** Outlook Survey

Retail Sales Growth Weakens

Retail sales grew at a slower pace in December, according to business executives responding to the Texas Retail Outlook Survey. The sales index declined from 13.0 in November to 6.2 in December. Inventory growth picked up, and the inventories index increased nearly three points to 6.4.

Retail labor market indicators were mixed, as employment fell but workweeks continued to lengthen this month. The employment index declined from 2.9 in November to -4.5 in December, its worst reading since 2016. The hours worked index declined nearly four points but remained positive at 2.5.

Retailers' perceptions of broader economic conditions deteriorated notably in December. The general business activity index fell into negative territory, dropping over 24 points to -16.8. The company outlook index fell from 4.1 in November to -15.6 in December, its weakest reading in nearly a decade.

Retail price pressures remained largely steady, while wage pressures eased this month. The selling prices index was unchanged at 12.7, while the wages and benefits index fell from 19.7 in November to 11.1 in December.

Retailers' perception of future economic conditions worsened significantly in December. The future general business activity index fell nearly 14 points to -12.0, while the future company outlook index fell from 0.2 to -11.6, a multiyear low. Other indexes of future retail sector activity, such as sales and employment, also turned negative, suggesting a weakened outlook six months ahead.

The Texas Retail Outlook Survey is a component of the Texas Service Sector Outlook Surveythat uses information only from respondents in the retail and wholesale sectors.

Next release: January 29, 2019

Data were collected December 18–26, and 207 Texas service sector and 50 retail sector 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	10.1	21.4	–11.3	Increasing	108	27.3	55.5	17.2
Employment	9.9	8.7	+1.2	Increasing	106	17.0	75.9	7.1
Part-Time Employment	1.6	3.6	–2.0	Increasing	11	6.1	89.4	4.5
Hours Worked	1.9	7.5	–5.6	Increasing	26	6.5	88.9	4.6
Wages and Benefits	19.8	20.9	–1.1	Increasing	115	22.3	75.2	2.5
Input Prices	26.1	27.0	–0.9	Increasing	116	29.9	66.2	3.8
Selling Prices	10.5	12.2	–1.7	Increasing	34	16.7	77.1	6.2
Capital Expenditures	10.9	11.3	–0.4	Increasing	112	18.5	73.9	7.6

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	–4.4	12.0	–16.4	Worsening	1	13.5	68.6	17.9
General Business Activity	–5.0	11.4	–16.4	Worsening	1	14.0	67.0	19.0

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Outlook Uncertainty†	15.0	12.8	+2.2	Increasing	11	29.4	56.3	14.4

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	32.3	41.4	–9.1	Increasing	118	47.3	37.6	15.0
Employment	20.0	30.0	–10.0	Increasing	117	30.2	59.6	10.2
Part-Time Employment	5.7	10.9	–5.2	Increasing	78	13.5	78.8	7.8
Hours Worked	6.0	6.3	–0.3	Increasing	28	13.0	80.0	7.0
Wages and Benefits	43.4	47.3	–3.9	Increasing	144	47.0	49.5	3.6
Input Prices	47.4	44.5	+2.9	Increasing	144	49.5	48.4	2.1
Selling Prices	29.4	31.7	–2.3	Increasing	116	37.6	54.2	8.2
Capital Expenditures	21.6	27.4	–5.8	Increasing	117	32.0	57.6	10.4

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	1.6	17.3	–15.7	Improving	34	21.5	58.6	19.9
General Business Activity	–5.0	16.6	–21.6	Worsening	1	17.5	59.9	22.5

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	6.2	13.0	–6.8	Increasing	8	26.0	54.2	19.8
Employment	–4.5	2.9	–7.4	Decreasing	1	3.2	89.1	7.7
Part-Time Employment	–2.0	3.7	–5.7	Decreasing	1	8.2	81.6	10.2
Hours Worked	2.5	6.1	–3.6	Increasing	18	8.3	85.9	5.8
Wages and Benefits	11.1	19.7	–8.6	Increasing	94	17.7	75.7	6.6
Input Prices	24.2	21.2	+3.0	Increasing	35	33.7	56.8	9.5
Selling Prices	12.7	12.7	0.0	Increasing	21	25.6	61.5	12.9
Capital Expenditures	0.0	5.5	–5.5	No Change	1	12.0	76.0	12.0
Inventories	6.4	3.6	+2.8	Increasing	7	22.8	60.8	16.4
Companywide Retail Activity								
Companywide Sales	9.4	16.8	–7.4	Increasing	8	25.7	58.0	16.3
Companywide Internet Sales	9.6	8.3	+1.3	Increasing	8	18.9	71.8	9.3

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	–15.6	4.1	–19.7	Worsening	1	7.7	69.0	23.3
General Business Activity	–16.8	7.5	–24.3	Worsening	1	6.4	70.4	23.2

Outlook Uncertainty

Current (versus previous month)

Indicator	Dec Index	Nov Index	Change	Indicator Direction*	Trend** (Months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Outlook Uncertainty†	14.0	7.6	+6.4	Increasing	7	32.0	50.0	18.0

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	–1.0	16.4	–17.4	Decreasing	1	25.4	48.2	26.4
Employment	–2.1	10.5	–12.6	Decreasing	1	9.7	78.5	11.8
Part-Time Employment	–1.6	6.1	–7.7	Decreasing	1	9.3	79.8	10.9
Hours Worked	–2.8	–7.5	+4.7	Decreasing	2	14.2	68.8	17.0
Wages and Benefits	24.7	35.6	–10.9	Increasing	120	32.0	60.7	7.3
Input Prices	32.6	23.1	+9.5	Increasing	116	36.7	59.2	4.1
Selling Prices	14.3	21.2	–6.9	Increasing	116	28.6	57.1	14.3
Capital Expenditures	–2.0	11.5	–13.5	Decreasing	1	14.3	69.4	16.3
Inventories	1.1	8.2	–7.1	Increasing	26	20.7	59.7	19.6
Companywide Retail Activity								
Companywide Sales	4.9	18.7	–13.8	Increasing	117	30.4	44.1	25.5
Companywide Internet Sales	6.1	12.8	–6.7	Increasing	29	18.2	69.7	12.1

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	–11.6	0.2	–11.8	Worsening	0	14.1	60.2	25.7
General Business Activity	–12.0	1.9	–13.9	Worsening	1	12.6	62.8	24.6

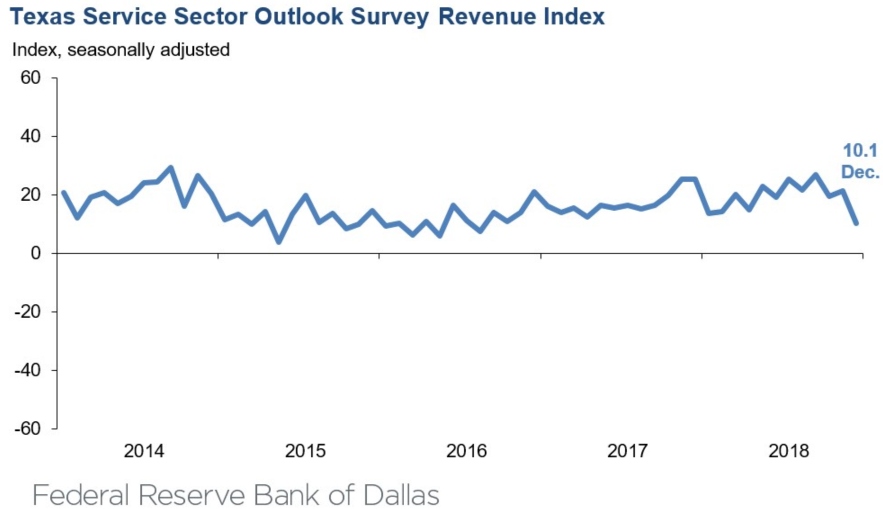
*Indicator direction refers to this month's index. If index is positive (negative), indicator is increasing (decreasing) or improving (worsening). If zero, indicator is unchanged.

**Number of months moving in current direction.

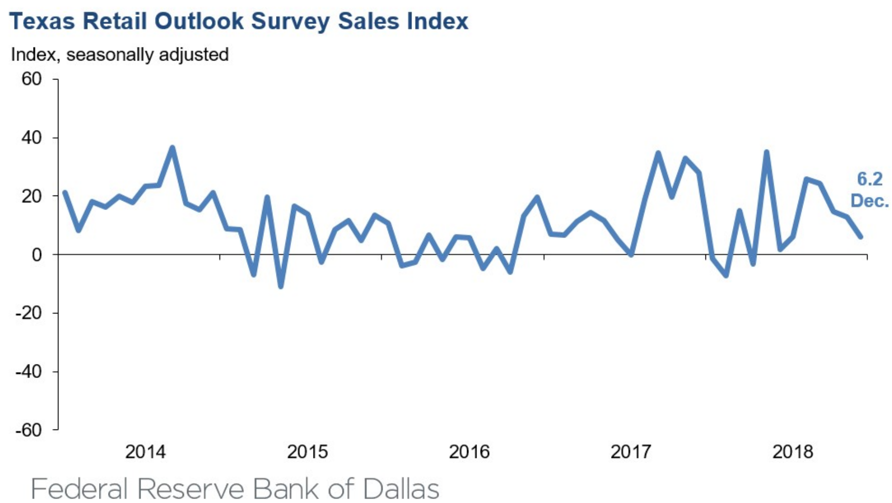
†Added to survey in January 2018.

Data have been seasonally adjusted as necessary, with the exception of the outlook uncertainty index which does not yet have a sufficiently long time series to test for seasonality.

Texas Service Sector Outlook Survey



Texas Retail Outlook Survey



Texas Service Sector Outlook Survey

January 2, 2019

Comments from Survey Respondents

These comments are from respondents' completed surveys and have been edited for publication.

Utilities

- We typically see a decrease in our product revenue due to seasonality.

Specialty Trade Contractors

- We still see solid orders; however, we are concerned about lead times for equipment and the economy slowing in 2019.

Pipeline Transportation

- Our uncertainty is primarily related to trade/tariff issues. Remove those and everything seems in good shape for 2019.

Support Activities for Transportation

- We are proceeding with an expansion of our cruise ship line of business with a deal for a third cruise terminal. We have seen an increase in lay and bunkering services. Our grain export line of business is still down due to tariffs.

Credit Intermediation and Related Activities

- Uncertainty in longer-term (six to 12 months) markets is pausing the general business expansion thoughts of mid-size business, especially those with some international trade exposure. Input cost increases are causing concerns for many.
- Current decisions are being very thoroughly vetted in light of the stock market decline and increasing recession vulnerabilities.
- The most recent news locally that will ultimately impact the economic environment in our area will be the announcement of impending closure of three sand mines in McCulloch County. The total employment to be lost would be 360 employees. This will affect the local small businesses, and the property and ad-valorem tax base will change drastically in time as a result of the elimination of valuation once the mining plants are dismantled and the land reclaimed. This negative event will have a lagging negative impact that might result in a slower absorption phase. If the community can attract another industry, it would help possibly replace or preserve a portion of the tax base. For our community and surrounding communities, it is going to be challenging to replace that many salaried employees. The start of the second phase of the wind farm has been delayed one year, but construction is expected to start in 2020 with the pause related to the increase in cost and availability of wind-generator parts from China, supposedly.

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

- Our company is tied to machinery and equipment in the oil and gas industry. This side of the oil and gas business has not generally participated in the increased production in the West Texas/Eastern New Mexico areas. Pricing of oil and natural gas still gives pause and concern in the industries. Expenses and material price increases continue to be announced, almost daily. Property taxes, insurance and general expenses continue to rise. There is really a squeeze on the bottom line.
- We see steady growth in retail sales and construction, although job growth is down slightly.

Insurance Carriers and Related Activities

- We continue to witness consolidation of local businesses into larger regional firms. Growth in a mid-sized city like Texarkana is losing out, I fear, to the (Dallas–Fort Worth) metroplex and I-35 corridor where growth and the inflow of people from other states is significant.

Real Estate

- Continuing uncertainty over the tariffs and trade talks, lack of passage of the new NAFTA [North American Free Trade Agreement] and continuing immigration issues are a constant drag on business.

Professional, Scientific and Technical Services

- Political uncertainty is an issue.
- As the price of oil decreases, the prospects for my business in the energy sector decreases. The insane tariff/trade war further decreases energy investment as materials cost more.

- While one expects some volatility in the market given current market uncertainty, the current swings being experienced are terribly troubling. I know many of my peers were no doubt surprised by the increase in economic activity in 2018— had really expected just under 3 percent—but we did believe what we saw was ephemeral given the drivers of that increased activity. Those drivers are of course waning, and the reality of much more moderate growth is finally sinking in. Where we once thought 2019 might be a modestly good year, we are less optimistic now, and more volatility is coming; I understand the reasoning with the Fed's [Federal Reserve] actions, but we are coming down off a level of support never seen before, and there is no optimum model to address. Who has any real idea what neutral even looks like anymore? Bottom line, there is a great deal of uncertainty here in the U.S., and a shift in political power in D.C.— balance welcome—will likely create even more uncertainty. Issues overseas with Brexit, and unrest in other parts of continental Europe, as well as continued tensions with China and trade, will only make things more challenging. A chill is in the air and will be here for a while.
- Low energy prices will impact our business if sustained.
- The drop in oil prices has our clients pulling back the checkbook, so our opportunities have shrunk over the last two months.
- Uncertainty increased due to leading indicators pointing to softening of the economy in 2019 albeit without recession. It is unclear what the economic condition will do to our consulting engineering business, but the uncertainty is making us be more cautious about 2019.
- The residential real estate market seems to have leveled off and stabilized after declining for most of the year while the commercial market has far exceeded our forecast. We are a little concerned about where this market is heading in 2019 due to the volatility of the stock market and the political unrest but hope to have a better understanding after the first quarter of the new year.
- The end of the year always has its slowdown for our industry. But the stock market downturn and the world's economic conditions cause severe uncertainty for firms. It seems like trust in Trump is waning. And the political lack of civility just keeps getting worse.
- We anticipate a market slowdown. However, legal services tends to lag the market by six months, so we believe that we will be able to manage into it if it does occur.

Management of Companies and Enterprises

- Rising interest rates are having negative effects on consumers and small businesses needing loans while they are still trying to recover from Hurricane Harvey damage. Lower ag commodity prices, caused in part by trade tariffs along with rising interest rates, are causing operational margin challenges for ag producer borrowers.
- Seems as if the Texas economy is slowing down somewhat. While capital expenditure in plant expansion is huge in our area, the ability of plant workers to purchase homes is limited by a shortage of affordable housing. Credit standards are hampering some purchases, but most of the problems surround qualifying.

Administrative and Support Services

- Shortage of labor is an issue.
- We have cut our fixed expenses and merged two offices with other existing offices, which can service two areas. Customer demand has caused an increase in temporary employee pre-employment drug screens. Due to the added expense, we now give the tests in-house. Other cost savings are also taking place. Increases in salary to full-time employees is competitive and given as performance merits.
- Assume that rates stabilize around 5 percent, Dallas–Fort Worth growth continues, unemployment remains low, that should afford some weekly predictability. An unknown is stock/oil prices; if rates stabilize, stocks should also.
- Our government contracts have generated more sales this year. We expect an increase in the next four months. Therefore, we will increase the number of personnel.

Educational Services

- I am concerned as President Trump is that rate hikes may have been too fast and too soon. This is beginning to hamper growth prospects and hinder growth going forward. We will see if the course is changed.

Ambulatory Health Care Services

- This month's analytic limerick: "December brought the fourth rate hike after the big three; Continuing rate normalization and reversal in QE [quantitative easing]; Fed governors are all quite wise; Mandate says prevent inflation rise; But market freefall may cause syncope."

Hospitals

- The cost for independent health systems to compete with larger ones and increased regulations are putting a strain on community health systems.

Nursing and Residential Care Facilities

- A lot of uncertainty in financial markets provides headwinds in health care since there is already increasing uncertainty about the regulatory environment and the potential impact of a recent federal court decision about the constitutionality of the Affordable Care Act. We are experiencing an upward trend in bad debt and charity care and face uncertainty about potential changes to the Medicaid 1115 waiver in Texas.

Amusement, Gambling and Recreation Industries

- The unemployment rate is very low, and this is affecting so many things, not just the direct effect on doing our actual business. It is very difficult to get people to do plumbing, for example. Several of our delivery companies are also having trouble getting employees, so alot of times, our deliveries are late or not delivered at all. Several of the companies will no longer deliver. Believe it or not, this has caused us to do much more ordering online when we can order ahead and it is not perishable. We are calling this the 'trickle up effect'; for instance, if we cannot hire enough dishwashers, then the cooks have to step in to help. If they are too busy, then it falls to the sous chefs, then to the chef and then to the managers. In the long run, I do not think this is good for productivity growth.

Accommodation

- We have some business going away, but hopefully this will be offset by some new clients.
- With all that is happening in Washington and the uncertainty brought on, our view is that over the next six months, we will start to feel the impact of a significant decrease in business and leisure travel.

Food Services and Drinking Places

- This update reflects progress on our recovery from Hurricane Harvey, though there is still much difficulty and uncertainty in navigating the insurance claims process.
- Availability of labor is still a very serious issue.

Religious, Grantmaking, Civic, Professional and Similar Organizations

- The recent ruling by a federal judge in Fort Worth on the Affordable Care Act, while a long time to take effect, provides uncertainty and risks, especially for hospital and health care providers in providing services to insured patients. This could have a serious effect on their planned capital investments.

Merchant Wholesalers, Nondurable Goods

- December is always better due to Christmas. In-store retail business is less this year than last year, and internet sales have not offset in-store decreases. There continues to be increased pricing pressure and manufacturers are all increasing their selling prices at the beginning of the year. There will be a continued shift to part-time employees with an overall reduction in hours. There is no shortage of available workers. The U6 unemployment rate is far more indicative of conditions, showing 7.6 percent for November.

Motor Vehicle and Parts Dealers

- New vehicles continue to barely break even as more competition and shopping by customers continues. The factory incentives change frequently and some dealers' advertising is less than honest. Our focus is on our customer service, which is thriving, and we hope to overcome the internet purchasing that many customers have been enticed to do.
- Our industry is heavily affected by increases in interest rates (automotive floor plan). Profitability is directly affected as we are unable to pass along increased costs to the customers. We have given additional consideration to cost control (including personnel).
- Our business model continues to be very challenging. I don't believe the Fed [Federal Reserve] understands our flawed business model. We can't survive if margins continue to erode as expenses dramatically increase. I don't need to explain the impact of this and last year's increases on our business. I strongly suggest the Fed review the impacts on our industry.

Building Material and Garden Equipment and Supplies Dealers

- Business among our customer base is really mixed. Some are doing better than in the past, others are flat and many are complaining it has slowed for them. Negativity in the news about every topic imaginable is affecting attitudes and business. Uncertainty about the future tone going forward has people nervous.
- There is increasing concern about the deteriorating economic environment.

Clothing and Clothing Accessories Stores

- The trend in department store sales continues to be lower.

Questions regarding the Texas Service Sector Outlook Survey can be addressed to Christopher Slijk at christopher.slijk@dal.frb.org.

Texas **Business** Outlook Surveys

Special Questions

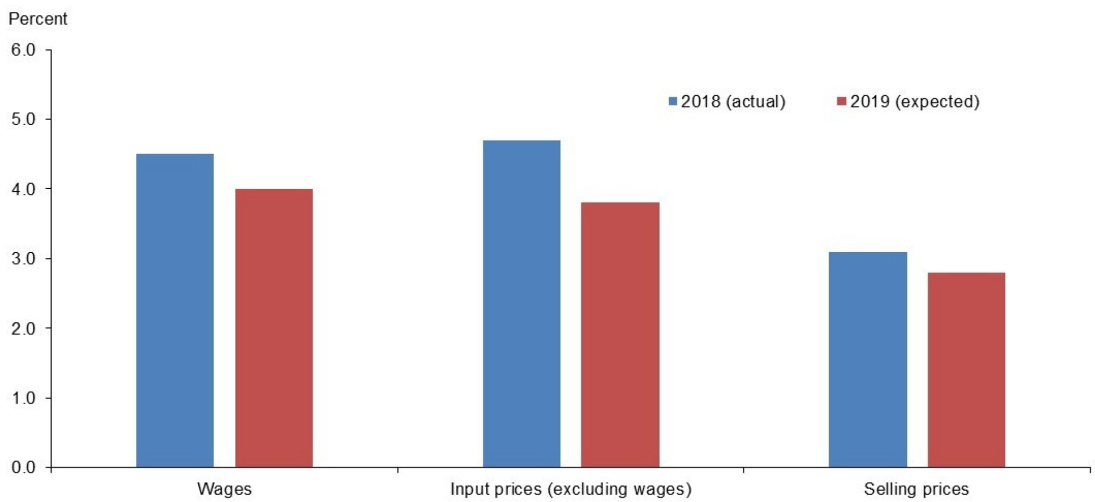
December 31, 2018

Results below include responses from participants of all three surveys: Texas Manufacturing Outlook Survey, Texas Service Sector Outlook Survey and Texas Retail Outlook Survey.

Texas Business Outlook Surveys

Data were collected Dec. 18–26, and 317 Texas business executives responded to the surveys.
See data files with a full history of results.

What annual percent change in wages, input prices, and selling prices did your firm experience in 2018 and what do you expect for 2019?



NOTE: Shown are trimmed means with the lowest and highest five percent of responses omitted.
SOURCE: Federal Reserve Bank of Dallas Texas Business Outlook Surveys

	2018 actual (percent)*	2019 expected (percent)*
Wages	4.5	4.0
Input costs (excluding wages)	4.7	3.8
Selling prices	3.1	2.8

If costs (including wages) are increasing, to what extent are you passing the higher costs on to customers in the way of price increases?

	Dec. '18 (percent)
None	24.4
Some	49.2
Most	18.1
All	8.4

If costs (including wages) are increasing, how has your firm's ability to pass those increases on to customers changed over the past six months?

	Dec. '18 (percent)
Much easier now	1.4
Somewhat easier now	18.9
Similar to six months ago	39.5
Somewhat harder now	23.7
Significantly harder now	16.5

How has your firm's operating margin, defined as earnings before interest and taxes (EBIT) as a share of total revenue, changed over the past six months?

	Dec. '18 (percent)
Increased substantially	7.2
Increased slightly	23.1
Remained the same	24.4
Decreased slightly	34.2
Decreased substantially	11.1

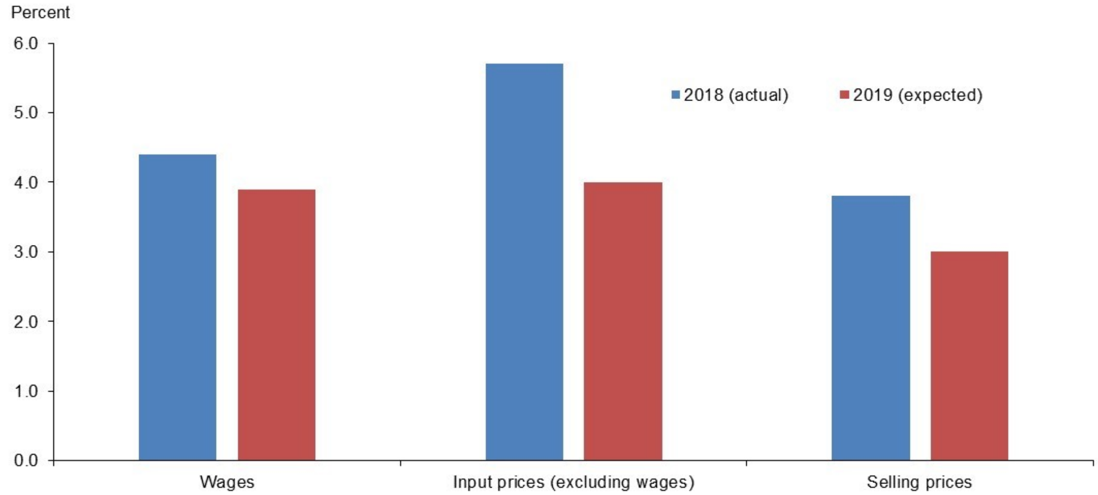
*Shown are trimmed means with the lowest and highest 5 percent of responses omitted. A similar question was posed in May 2018 asking about wages and prices in 2017 (actual) and 2018 (expected).
NOTES: Survey respondents were given the opportunity to provide comments. These comments can be found on the individual survey Special Questions results pages

Texas Manufacturing Outlook Survey

Data were collected Dec. 18–26, and 100 Texas manufacturers responded to the survey.

See data files with a full history of results.

What annual percent change in wages, input prices, and selling prices did your firm experience in 2018 and what do you expect for 2019?



NOTE: Shown are trimmed means with the lowest and highest five percent of responses omitted.
SOURCE: Federal Reserve Bank of Dallas Texas Manufacturing Outlook Survey

	2018 actual (percent)*	2019 expected (percent)*
Wages	4.4	3.9
Input costs (excluding wages)	5.7	4.0
Selling prices	3.8	3.0

If costs (including wages) are increasing, to what extent are you passing the higher costs on to customers in the way of price increases?

	Dec. '18 (percent)
None	17.2
Some	50.5
Most	23.2
All	9.1

If costs (including wages) are increasing, how has your firm's ability to pass those increases on to customers changed over the past six months?

	Dec. '18 (percent)
Much easier now	1.0
Somewhat easier now	26.5
Similar to six months ago	35.7
Somewhat harder now	20.4
Significantly harder now	16.3

How has your firm's operating margin, defined as earnings before interest and taxes (EBIT) as a share of total revenue, changed over the past six months?

	Dec. '18 (percent)
Increased substantially	11.1
Increased slightly	24.2
Remained the same	17.2
Decreased slightly	35.4
Decreased substantially	12.1

*Shown are trimmed means with the lowest and highest 5 percent of responses omitted. A similar question was posed in May 2018 asking about wages and prices in 2017 (actual) and 2018 (expected).

Special Questions Comments

These comments have been edited for publication.

Food Manufacturing

- Cost decreases are per ton and are driven by volume and low commodity prices. The current crop is much smaller, and per-ton costs will be rising in the coming months.
- The increase in EBIT [earnings before interest and taxes] is a result of significant growth on the top line.

Apparel Manufacturing

- We are getting to be more efficient the longer we have military sewing projects.

Printing and Related Support Activities

- Increases in unit wage and raw material costs are primarily offset with increased productivity in this manufacturing business. Wage increases have not outpaced volume and production rate increases.

Fabricated Metal Product Manufacturing

- Some utility companies understand and will accept some price increases due to steel price and shipping cost increases. However, some large privately funded and federal jobs are now sourcing their steel structures from foreign sources, causing us to be price uncompetitive.
- There is strong competition for the work that we do. Margins have continued to narrow due to excess capacity and firms willing to bid work at or below costs to maintain production capacity.
- Operating margin has increased, primarily due to capital investments in manufacturing equipment. With these investments, we have improved efficiency while maintaining head count.

Computer and Electronic Product Manufacturing

- We had contraction in the latter half of 2018 and kept key employees in anticipation of expanding in 2019. We are starting to see significant expansion for 2019.

Electrical Equipment, Appliance and Component Manufacturing

- Our industry is finally realizing that you have to pass on cost increases in good times, and our improved profitability in the last 18 months is commendable. We did a salary survey of companies and found we were low on starting pay for our hourly workforce. Eighty-five percent of our people are hourly. We are making adjustments in January to be competitive and hopefully cut turnover and attract better candidates. Ten percent is a guess on the total impact to our wage rates.

Transportation Equipment Manufacturing

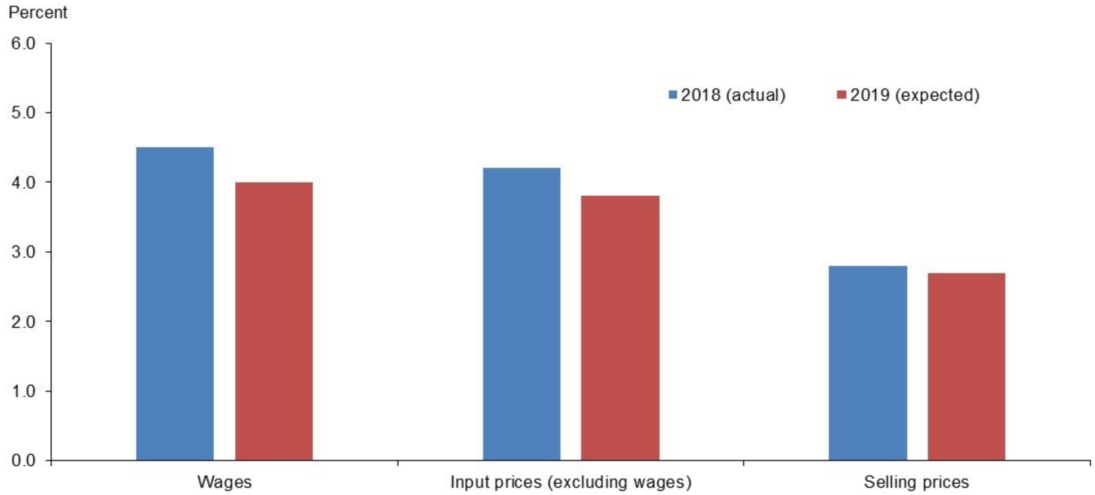
- Competition from India, China and South Korea has resulted in a substantial decrease of business for us. Although raw steel has tariffs on imports, the finished goods resulting from the raw materials do not. This has given our foreign competition a very unfair advantage over U.S. manufacturers.
- Our ability to pass increases in costs (including wages) along to customers is somewhat harder because new contracts and agreements require extended price guarantees for multiple years, with one exception. Increases in raw material costs remain easy to pass along. Operating margins have decreased slightly in the past six months because revenue declined unexpectedly while investment in personnel (additions and advanced training) increased in line with performance in the first half of 2018. However, this margin is a substantial increase from the previous year.

Texas Service Sector Outlook Survey

Data were collected Dec. 18–26, and 217 Texas business executives responded to the survey.

See data files with a full history of results.

What annual percent change in wages, input prices, and selling prices did your firm experience in 2018 and what do you expect for 2019?



NOTE: Shown are trimmed means with the lowest and highest five percent of responses omitted.
SOURCE: Federal Reserve Bank of Dallas Texas Service Sector Outlook Survey

	2018 actual (percent)*	2019 expected (percent)*
Wages	4.5	4.0
Input costs (excluding wages)	4.2	3.8
Selling prices	2.8	2.7

If costs (including wages) are increasing, to what extent are you passing the higher costs on to customers in the way of price increases?

	Dec. '18 (percent)
None	28.0
Some	48.5
Most	15.5
All	8.0

If costs (including wages) are increasing, how has your firm's ability to pass those increases on to customers changed over the past six months?

	Dec. '18 (percent)
Much easier now	1.6
Somewhat easier now	15.0
Similar to six months ago	41.5
Somewhat harder now	25.4
Significantly harder now	16.6

How has your firm's operating margin, defined as earnings before interest and taxes (EBIT) as a share of total revenue, changed over the past six months?

	Dec. '18 (percent)
Increased substantially	5.3
Increased slightly	22.6
Remained the same	27.9
Decreased slightly	33.7
Decreased substantially	10.6

*Shown are trimmed means with the lowest and highest 5 percent of responses omitted. A similar question was posed in May 2018 asking about wages and prices in 2017 (actual) and 2018 (expected).

Special Questions Comments

These comments have been edited for publication.

Credit Intermediation and Related Activities

- The majority of the increase in earnings is attributable to the lower corporate tax rate.
- It is all about pricing and that is influenced by competition, resulting in very thin prices over cost. Liquidity is a precious commodity in a heated lending environment, resulting in higher rates paid for deposits and expanding efforts by the too-big-to-fail banks into smaller communities for attracting local deposits.

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

- It remains hard to pass price increases on to customers. Most customers are pushing hard for price decreases with their supply chain targets.
- The competitive landscape in wealth management is very difficult. Input costs of regulation and compliance continue to increase. Our ability to maintain our advising fee to clients is weak. Pricing in our industry is continually under pressure.

Insurance Carriers and Related Activities

- We are managing growth in routine operating expenses, but health care expenses are killing us. We have an aging workforce and we are self-insured—looking like a bad idea as health care costs and utilization of services increase.

Rental and Leasing Services

- We are a very capital-intensive business, so with 100 percent bonus depreciation, I can determine my year-end profit by what I add or do not add to my $222 million equipment rental fleet.

Professional, Scientific and Technical Services

- 2018 was a greatly improved year for selling services, passing along costs and improving margin.
- The uncertainty and the political unrest are hurting business.

Administrative and Support Services

- We were awarded new contracts.

Ambulatory Health Care Services

- As a health care provider in a deflationary market sector, we have no control over reimbursement and only know that it continues to go down a bit every year.
- The health care industry continues to be an increasing wage and operating cost model with a punitive reimbursement model that is eroding margins and leading to significant consolidation in the health care industry.

Nursing and Residential Care Facilities

- Health care is a regulated market with limited price elasticity, yet we continue to face wage pressure and cost pressure on top of new market entries who extract the few commercial and/or self-pay patients from an already stressed community hospital. Expect to see more hospital closures in 2019.

Amusement, Gambling and Recreation Industries

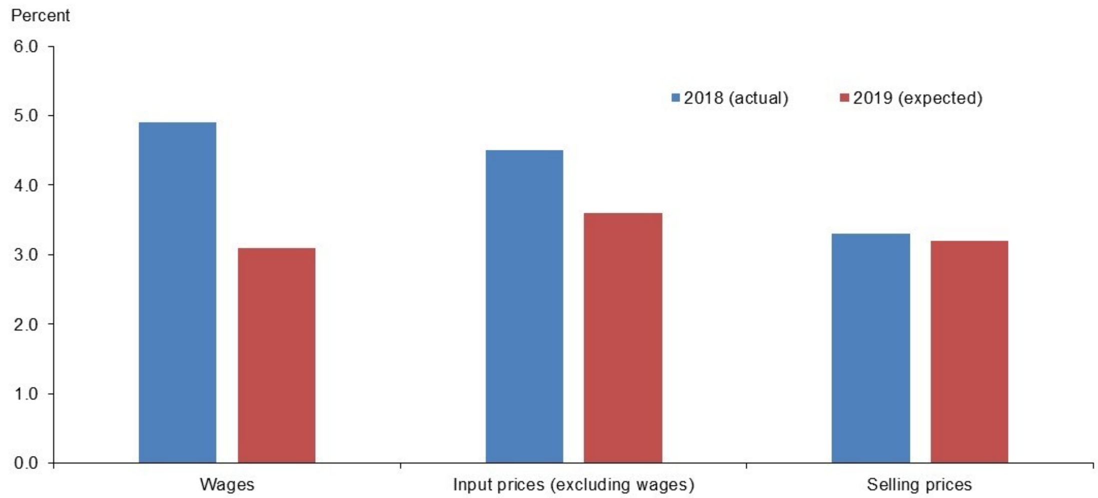
- The projections for 2019 are very difficult. We are not only having to raise wages but also increase benefits to attract and keep good employees. All other companies are having to do the same thing, so our cost of goods is going up all the time too.

Texas Retail Outlook Survey

Data were collected Dec. 18–26, and 41 Texas retailers responded to the survey.

See data files with a full history of results.

What annual percent change in wages, input prices, and selling prices did your firm experience in 2018 and what do you expect for 2019?



NOTE: Shown are trimmed means with the lowest and highest five percent of responses omitted.
SOURCE: Federal Reserve Bank of Dallas Texas Retail Outlook Survey

	2018 actual (percent)*	2019 expected (percent)*
Wages	4.9	3.1
Input costs (excluding wages)	4.5	3.6
Selling prices	3.3	3.2

If costs (including wages) are increasing, to what extent are you passing the higher costs on to customers in the way of price increases?

	Dec. '18 (percent)
None	18.4
Some	52.6
Most	15.8
All	13.2

If costs (including wages) are increasing, how has your firm's ability to pass those increases on to customers changed over the past six months?

	Dec. '18 (percent)
Much easier now	5.3
Somewhat easier now	7.9
Similar to six months ago	28.9
Somewhat harder now	36.8
Significantly harder now	21.1

How has your firm's operating margin, defined as earnings before interest and taxes (EBIT) as a share of total revenue, changed over the past six months?

	Dec. '18 (percent)
Increased substantially	2.6
Increased slightly	10.3
Remained the same	23.1
Decreased slightly	41.0
Decreased substantially	23.1

*Shown are trimmed means with the lowest and highest 5 percent of responses omitted. A similar question was posed in May 2018 asking about wages and prices in 2017 (actual) and 2018 (expected).

Special Questions Comments

These comments have been edited for publication.

Merchant Wholesalers, Nondurable Goods

- Property taxes exceed any inflation. Manufacturers are all increasing prices due to wage pressures and potential tariffs. Customers remain very price sensitive. Increased interest rates will bring on the recession. The Federal Reserve has completely misread the data it is using.

Motor Vehicle and Parts Dealers

- There is continued pressure on fixed overhead—like insurance, property taxes, maintenance—as it relates to our brick-and-mortar locations.
- Internet pricing is causing severe downward pressure on new and used vehicle prices.
- Internet pricing is affecting all retail sales outlets. The automobile industry is especially changed because of the many makes and models and the many factory incentives that are hard for customers to compare and comprehend. Many buyers are being misled by internet ads and internet pricing. Factory incentives are based on total sales, so that large dealers have more discounts than small dealers because of volume of sales. Operating margins will continue to drop until this trend has stopped.

Questions regarding the Texas Business Outlook Surveys can be addressed to Emily Kerr at emily.kerr@dal.frb.org,