DALLASFED Economic Update
Regional

Region Continues to Grow Despite Renewed Energy Headwinds

October 29, 2015

The Texas economy is growing at a modest pace after slowing from a slight acceleration near mid-year. Employment picked up in September to an annualized 1.4 percent pace after posting essentially no growth in August. The Texas Business Outlook Surveys (TBOS) point to continued weakness in the manufacturing sector and moderate strength in services.

The headwinds of declining energy markets and a strengthening dollar have continued to dampen growth prospects for the region. Metropolitan areas tied to oil and gas, such as Houston, or manufacturing, such as Fort Worth, saw weak job growth in August and September. Despite this, job growth in most other large metro areas remains robust, and growth for Texas overall should remain positive for the remainder of this year and into 2016.

Job Growth Weakens in Third Quarter

Texas job growth came in at a 1.6 percent annualized rate in the third quarter, below the 1.8 percent pace in the second quarter (*Chart 1*). Nevertheless, Texas exceeded the nation's 1.4 percent rate, marking the first time it has outpaced the U.S. since fourth quarter 2014.

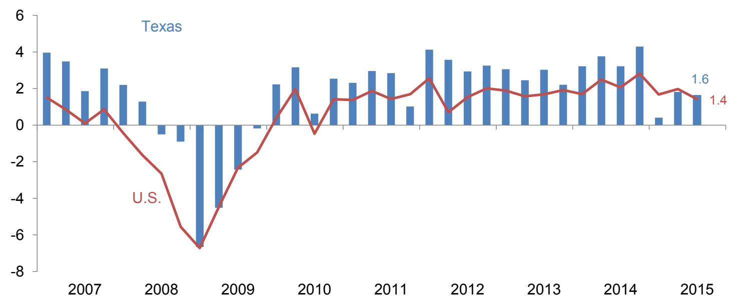
Much of the third-quarter growth occurred in July, before oil prices fell from about $60 per barrel—where they had stabilized in May and June—to about $45—their average since then. Employment growth was weak and mixed across industries in August and September. Overall, the goods-producing sector saw continued declines, but construction employment increased an annualized 4.7 percent and manufacturing and mining sectors shed jobs at a slower rate in September. Most service sector industries continued to grow at a moderate pace in September, albeit more slowly than in the previous three months.

Energy Sector Continues to Decline

West Texas Intermediate crude oil prices have stabilized around $45 per barrel over the past six weeks after experiencing higher volatility in August and early September (*Chart 2*). However, the fall from $60 in June prompted a continued decline in the Texas rig count, which is now at its lowest level since mid-2009.

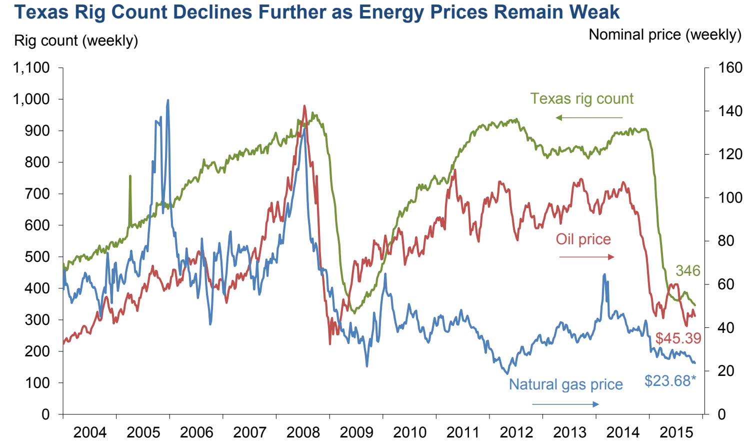
Nevertheless, much of the state has diversified away from energy. Metro areas that have a low employment share in mining (of which the vast majority is oil and gas related) are generally growing at a faster pace than those with a higher employment share in that industry (*Chart 3*). Furthermore, the diversification of the energy industry into petrochemical and refined products, which benefit from low energy prices, has softened the blow of this decline in metros such as Houston.

Chart 1
Texas Job Growth Dips but Exceeds National Rate in Third Quarter
Percent growth, quarter/quarter*



*Seasonally adjusted, annualized rate.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal adjustments by the Federal Reserve Bank of Dallas.

Chart 2
Texas Rig Count Declines Further as Energy Prices Remain Weak

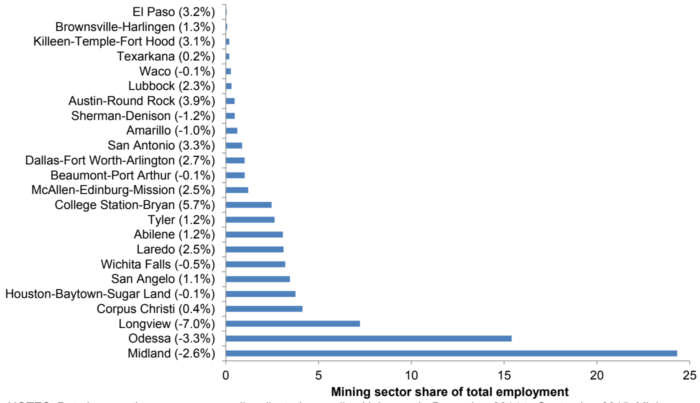


*Natural gas price is multiplied by 10.
SOURCES: *Wall Street Journal*; Baker Hughes; Haver Analytics.

Energy Workers' Departure Helps Explain Low Unemployment

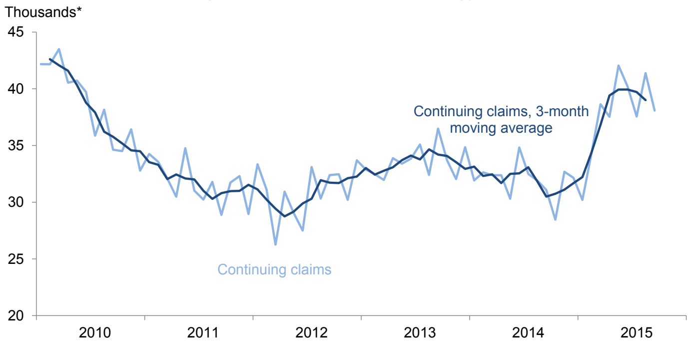
Despite continued job losses in mining and manufacturing, the Texas unemployment rate has been persistently low, inching up just slightly to 4.2 percent in September. Much of this is attributable to the decline in the labor force—some workers who had migrated to Texas during the energy boom have left the state. An indication of this is the spike in continuing claims for unemployment paid to workers who have moved out of state (*Chart 4*). The 28 percent rise in continuing claims from January to March, a period when 19,000 mining jobs were shed, suggests that some laid-off workers moved out of Texas and thus out of the state's labor force.

Chart 3
Energy Sector's Size Explains Much of Job Growth in Large Metros



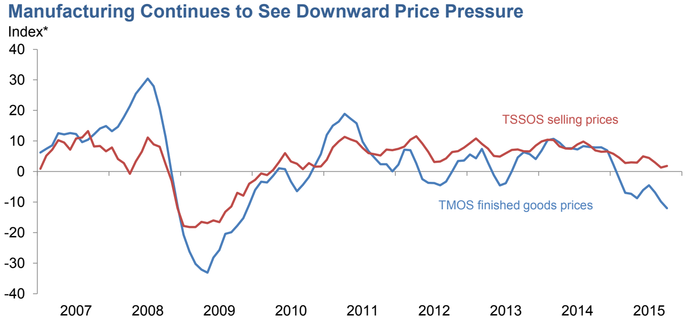
NOTES: Data in parentheses are seasonally adjusted annualized job growth, December 2014 to September 2015. Mining share data are as of 2014.
SOURCES: Texas Workforce Commission; Bureau of Labor Statistics; Federal Reserve Bank of Dallas.

Chart 4
Out-of-State Continuing Claims Pick Up Since Energy Bust



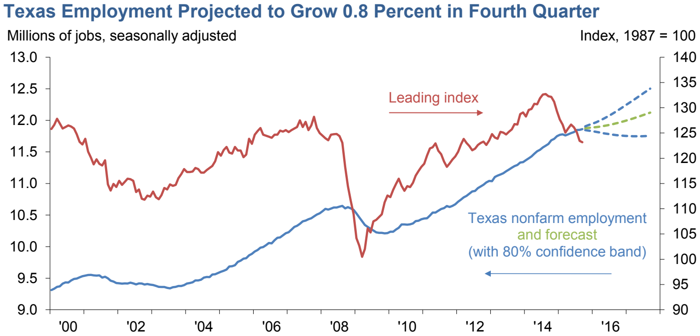
*Seasonally adjusted.
SOURCES: Texas Workforce Commission; seasonal adjustment by the Federal Reserve Bank of Dallas.

Chart 5
Manufacturing Continues to See Downward Price Pressure



*Seasonally adjusted, three-month moving average.
SOURCE: Federal Reserve Bank of Dallas' Texas Manufacturing Outlook Survey (TMOS) and Texas Service Sector Outlook Survey (TSSOS).

Chart 6
Texas Employment Projected to Grow 0.8 Percent in Fourth Quarter



SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; Federal Reserve Bank of Dallas.

Residential Real Estate Activity Robust in Major Metros

As suggested by the rebound in third-quarter construction activity, real estate markets remain strong in the state. Residential home inventories are still lean in all major markets and are at a low 3.4 months' supply in the state. The health of commercial real estate is mixed across markets, but even in softening metros such as Houston, office vacancy rates have not increased to an extent that would indicate distress.

Manufacturing and Services Price Pressures Diverge

The strong dollar and renewed fall in energy prices have put further downward pressure on prices. TBOS questions on current finished goods prices indicate that manufacturing respondents faced price declines for the 10th consecutive month in October (*Chart 5*). While service sector prices continue to rise, the number of respondents indicating price decreases has picked up considerably since last year.

Outlook Dampened but Positive for 2015

The Texas Leading Index (TLI) fell 0.2 percent in September on the heels of a sharp 1.4 percent decline in August. Appreciation in the Texas Trade-Weighted Value of the Dollar and weakness in the stocks of Texas-based companies have been the primary drivers of the TLI decline since July. The health of the U.S. economy has continued to contribute positively to the index, and a slight uptick in well permits mitigated some of the decline in September.

The Texas employment forecast is for 1.2 percent growth for 2015. The forecast for the rest of the year is for annualized growth of 0.8 percent, which is slightly weaker than the 1.3 percent rate thus far this year (*Chart 6*). This indicates that growth will likely fall back below the national rate in the fourth quarter.

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About the Authors

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