

Texas Economic Growth Shifts into Slightly Higher Gear

February 2, 2017

Texas economic growth has accelerated somewhat. Employment strengthened in the state and in most major metros in the second half of 2016. Improvement was broad based, with stronger manufacturing output and higher service sector revenue as well as solid real estate activity. The energy sector continued to show signs of improvement.

There is also evidence that this pickup in growth is set to continue. The Dallas Fed's [Texas Business Outlook Surveys](#) (TBOS) company outlook indexes, [job-growth forecast](#) and [Texas Leading Index](#) suggest expansion. However, risks to the positive outlook remain, including a strong dollar and the potential for another drop in oil prices.

Employment Approaching Long-Run Growth Rate

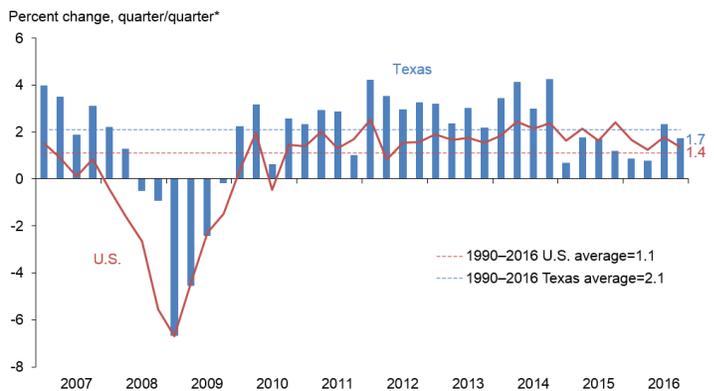
Texas payroll employment grew at a 1.7 percent annual rate in fourth quarter 2016, close to its historical average of 2.1 percent (*Chart 1*). While this is well below the 3.7 percent rate that prevailed in 2014, it represents the second consecutive quarter in which Texas' employment growth surpassed the nation's. In the more volatile monthly data, December employment declined slightly, although November and October figures were revised substantially upward.

Strengthening employment growth in the second half of 2016 was led by San Antonio, whose annualized growth rate rose from 2.4 percent in the first half to 5.0 percent in the second, and Dallas, whose growth rate rose from 2.3 percent to 4.0 percent (*Chart 2*). Houston also turned in a better-than-expected employment performance, rallying from -1.1 percent to 0.9 percent growth amid improvements in the energy sector.

Manufacturing and Services Activity Continues to Grow

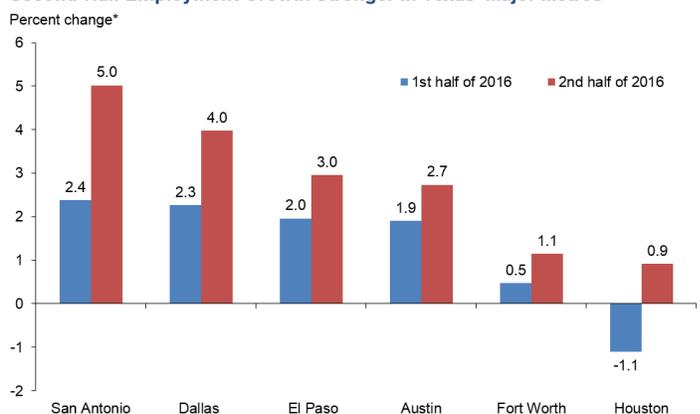
TBOS headline indexes indicate expansion in the past six weeks (*Chart 3*). The headline Texas Manufacturing Outlook Survey (TMOS) production index's three-month moving average edged down in December but ticked up in January, reaching its highest level since October 2014. The three-month moving average of the headline revenue measure from the Texas Service Sector Outlook Survey (TSSOS) rose in December and again in January. The Texas Retail Outlook Survey (TROS) headline sales measure's three-month moving average steadily increased in November, December and January. The latter two indexes are at their highest levels in two years.

Chart 1
Texas Employment Growth Accelerates in Second Half



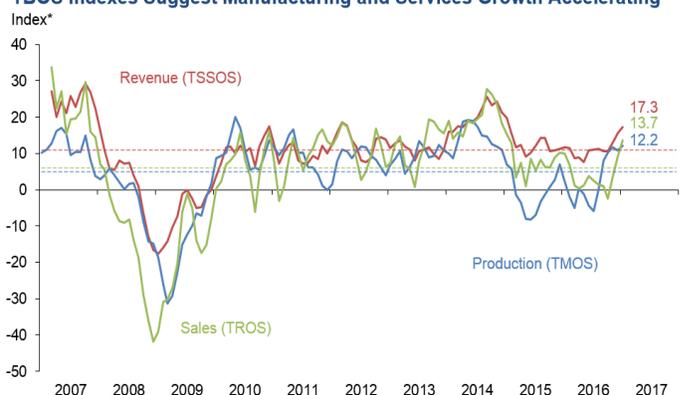
*Seasonally adjusted, annualized rate.
NOTE: Quarterly data are the last month of the quarter.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Chart 2
Second-Half Employment Growth Stronger in Texas' Major Metros



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

Chart 3
TBOS Indexes Suggest Manufacturing and Services Growth Accelerating



*Seasonally adjusted; three-month moving average.
NOTES: Last data point is January 2017. Dotted lines represent averages for January 2007–January 2017.
SOURCES: Federal Reserve Bank of Dallas' Texas Business Outlook Surveys (TBOS); Texas Manufacturing Outlook Survey (TMOS), Texas Service Sector Outlook Survey (TSSOS) and Texas Retail Sector Outlook Survey (TROS).

Housing Market Solid Overall

Residential housing demand strengthened somewhat after a relatively soft summer. Existing-home sales show improvement across the state, with DFW especially strong (Chart 4). Months of inventory remain well below the six-month mark that traditionally connotes a balanced market, though Houston's rate stands at a four-year high.

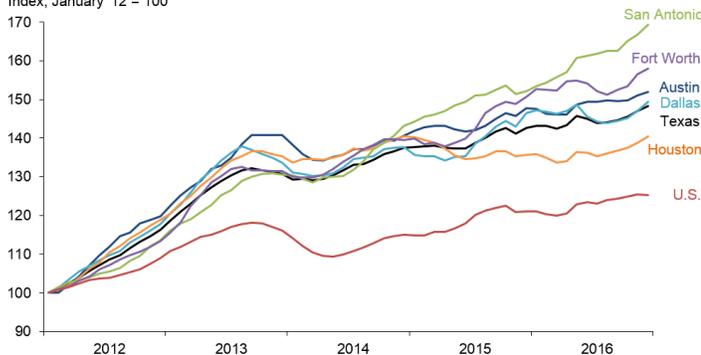
Energy Sector Strengthens, Albeit from Low Levels

Oil prices have risen slightly over the past six weeks to \$52.50 per barrel in January, their highest level in a year and half. While still at less than half their 2011–13 heights, energy prices have gradually recovered from their 2015–16 depths and sent the Texas rig count to a 14-month high (Chart 5). Well permits—a precursor to possible future drilling—jumped from 581 in November to 909 in December, reaching their highest level in two years. This is consistent with the [Dallas Fed Energy Survey](#), whose indexes improved markedly in the fourth quarter. Notably, both the business activity and capital expenditures indexes were positive, suggesting that energy firms expect somewhat higher activity to continue over the medium term.

Looking across the region, the production cost advantage held by the Permian Basin continues to be felt, aided by new technologies that enable drillers to access Permian

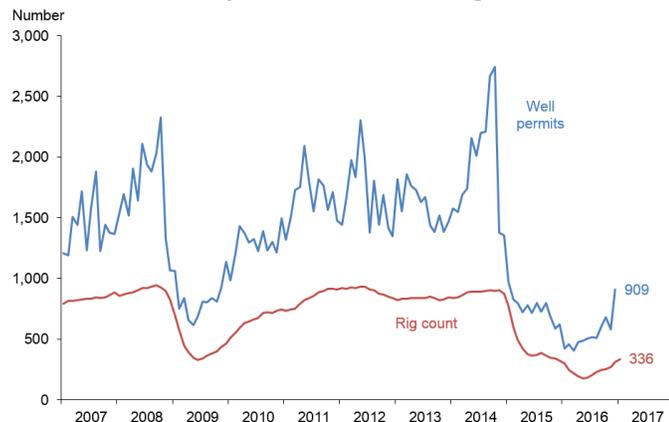
Chart 4
Existing-Home Sales Improve

Index, January '12 = 100*



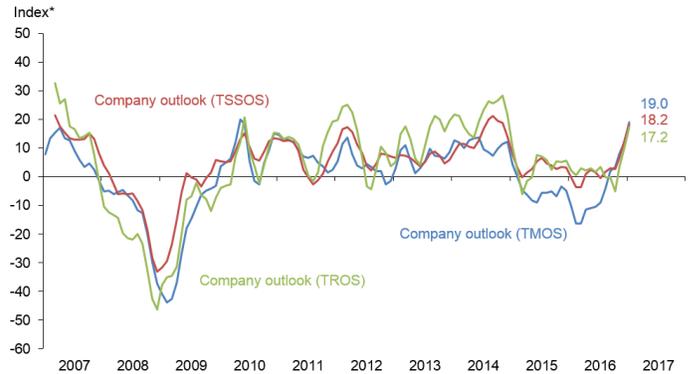
*Six-month moving average.
NOTE: Last data point is December 2016.
SOURCES: Multiple Listing Service; seasonal adjustments by the Federal Reserve Bank of Dallas.

Chart 5
Texas Well Permits Jump from 581 to 909, Their Largest Gain in Two Years



NOTE: Last data point is December 2016 for well permits and January 2017 for the rig count.
SOURCES: Baker Hughes; Texas Railroad Commission.

Chart 6
TBOS Company Outlook Indexes Surge



*Seasonally adjusted; three-month moving average.
NOTE: Last data point is January 2017.
SOURCES: Federal Reserve Bank of Dallas' Texas Business Outlook Surveys (TBOS); Texas Manufacturing Outlook Survey (TMOS); Texas Service Sector Outlook Survey (TSSOS) and Texas Retail Outlook Survey (TROS).

resources more efficiently. Eagle Ford production fell an estimated 2.7 percent in December and another 1.9 percent in January, continuing a trend that began as oil prices started their 2014–15 plunge. A thus-far-sustained oil price in the low \$50s has led to Permian production increases throughout the fourth quarter and into first quarter 2017, including an estimated 1.1 percent in December and 1.6 percent in January.

Improved Outlook

The overall weight of the evidence suggests regional economic growth has shifted into a slightly higher gear and will likely be faster in 2017 than it was in 2016. The Texas Leading Index's first estimate ticked up in December, and the Dallas Fed's employment forecast stands at 1.9 percent, which would be the state's strongest growth since 2014.

Outlook measures from TBOS also point to greater economic strength in the months ahead, with all three series rebounding from their 2014–16 doldrums to near postrecession highs (Chart 6). The three-month moving average of the TMOS company outlook index is at its highest point since 2010, while the TSSOS and TROS company outlook indexes' three-month moving averages are at their highest levels in over two years. Notably, the six-month-ahead TMOS company outlook index rose in January to the highest level in 12 years.

The Texas economy grew at a somewhat faster pace at year-end amid increasing evidence of a stronger 2017. This acceleration has been broad based across both sectors and regions, with DFW soaring and Houston faring somewhat better than expected. Declining oil prices and a stronger dollar remain the most significant risks to the outlook.

—Stephanie Gullo and Jason Saving

About the Authors

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