

Thriving Texas Economy Expands Broadly

February 5, 2018

The Texas economy continues its broad expansion. Texas employment growth accelerated in the fourth quarter and was strong across most metros and industries. The Dallas Fed's Texas Business Outlook Surveys (TBOS) showed notable strength in revenue and production in January, with the three-month moving averages of the headline indexes at levels well above their postrecession averages. However, labor markets continue to tighten, and price pressures are mounting.

The Texas economy is benefiting from oil prices above \$60 per barrel, rising exports, business optimism stemming from the new federal tax law and strength in the U.S. economy. Headwinds include uncertainty about North American Free Trade Agreement renegotiations and a tight labor supply damping the potential for even stronger economic growth going forward.

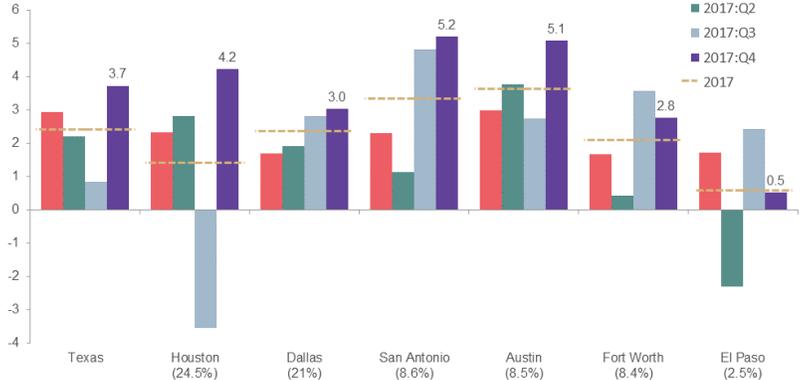
Texas Job Growth Robust in Fourth Quarter

[Texas added jobs](#) at a 2.4 percent rate in 2017, ranking No. 4 in the nation after falling below the national average in 2015 and 2016. The [Dallas Fed forecasts 2018 Texas job growth](#) of 2.8 percent.

Fourth-quarter job growth in Texas was robust and far reaching—spanning all major metros and industries and indicating economic strength beyond the temporary boost from Hurricane Harvey recovery efforts (*Chart 1*). The Houston economy rebounded from a hurricane-induced decline in the third quarter—to 4.2 percent in the fourth quarter. The metropolitan area finished 2017 with 1.4 percent employment growth after two years of flat employment. San Antonio and Austin posted blistering annual growth rates of 5.2 and 5.1 percent, respectively, in the fourth quarter. Austin's 3.6 percent job growth for the year was the highest of the state's major metros.

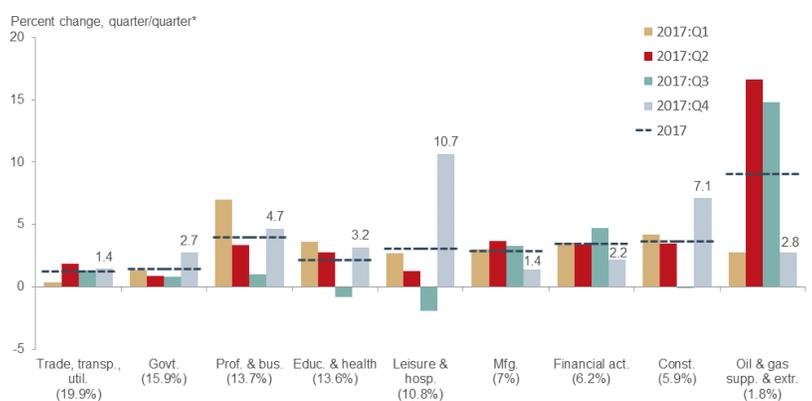
While fourth-quarter employment growth occurred across major industries, energy sector expansion moderated (*Chart 2*). Still, the energy sector experienced the greatest 2017 growth (9.0 percent) among major industries after two years of decline due to the oil bust. Job growth picked up notably in professional and business services in the fourth quarter and surged in leisure and hospitality and in construction—two sectors benefiting from hurricane recovery.

Chart 1
Fourth-Quarter Job Growth Robust Across Most Metros
Percent change, quarter/quarter*



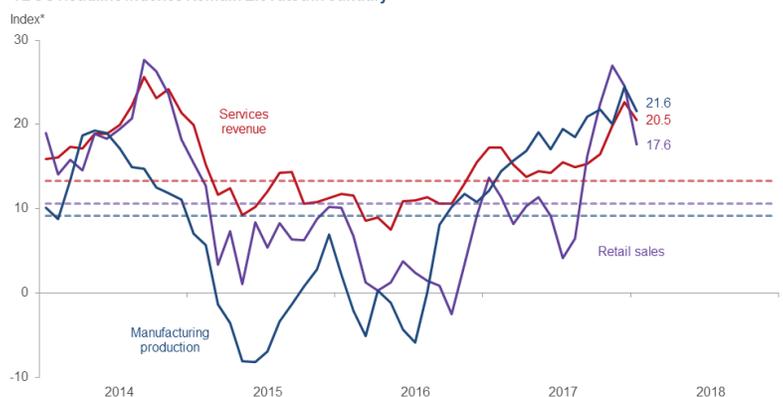
*Seasonally adjusted, annualized rate.
NOTES: Numbers in parentheses are share of Texas employment in December 2017. Dashed lines show 2017 growth (December/December).
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Chart 2
Fourth-Quarter Gains Broad Based Across Industries
Percent change, quarter/quarter*



*Seasonally adjusted, annualized rate.
NOTES: Numbers in parentheses are share of Texas employment in December 2017. Dashed lines show 2017 growth (December/December).
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Chart 3
TBOS Headline Indexes Remain Elevated in January
Index*



*Three-month moving average, seasonally adjusted.
NOTES: Data are through January 2018. Dashed lines denote postrecession averages (January 2010 to present). Readings above 0 indicate expansion.
SOURCE: Federal Reserve Bank of Dallas Texas Business Outlook Surveys (TBOS).

Business Activity Ends 2017 on High Note

The Dallas Fed's [Texas Business Outlook Surveys](#) paint 2017 as a banner year, with a hearty rebound in manufacturing output and strong retail sales growth, particularly during the second half. While the headline indexes dipped in January 2018, the three-month moving averages remained elevated at levels well above their postrecession averages (*Chart 3*).

Manufacturing new orders and general business activity indexes surged to 11-year highs in December. The new orders index edged down in January but remained at its highest point since mid-2006, while the general business activity index strengthened further to its highest level since late 2005.

Looking ahead, Texas firms' optimism picked up notably at year end. In January, the service-sector company outlook index advanced for a second month, while the manufacturing sector company outlook index down but remained elevated.

Additionally, a sharp rise in firms' capital spending plans was seen in the December TBOS and was sustained in the January readings (*Chart 4*). The December survey collection period covered the days that led up to and included the passage of the federal tax code revision, which likely contributed to the jump as the new tax policy includes more favorable deduction rules for capital spending.

Tight Labor Market a Headwind for Stronger Growth

A key question facing the Texas economy entering 2018 is the extent to which the state can add jobs when the labor market is very tight. The [state unemployment rate](#) is near its all-time low at 3.9 percent, and firms responding to TBOS report that labor shortages are impairing their growth. Even Texas' U6 unemployment rate—a measure that includes marginally attached workers and those employed part time for economic reasons—has receded to near prerecession lows, suggesting slack in the broader labor market has largely been absorbed (*Chart 5*).

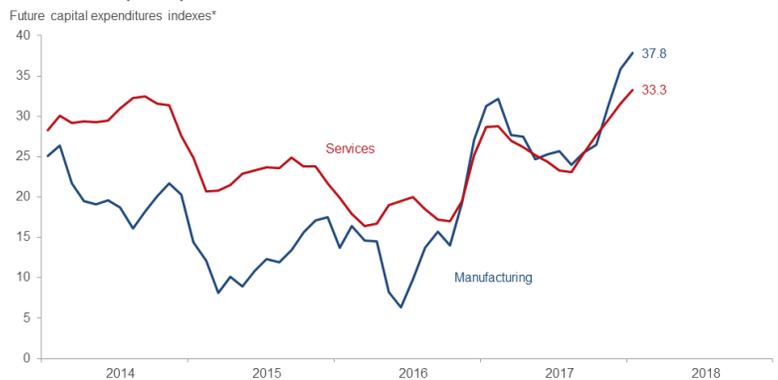
The wages and benefits indexes across the three Texas Business Outlook Surveys remain above average, as an increasingly tight labor market continues to translate into wage inflation. Manufacturers are more bullish about future wages—60 percent of firms expect wages and benefits will be higher six months from now, pushing the future wages and benefits index to 56.9 in January, its second-highest reading since the series began in 2004 and more than 20 points above its postrecession average.

Strong Population Growth Continues in 2017

The Texas population gained nearly 400,000 new residents from July 2016 to July 2017, representing the largest population gain among the states. This 1.4 percent growth rate is the seventh fastest in the U.S. Just over half of the state's population growth was from natural increase (births minus deaths), while the rest was from net international and domestic migration.

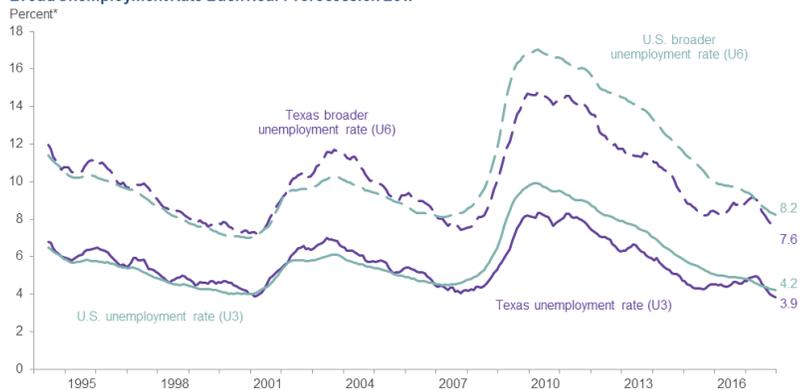
Net international migration to Texas was roughly 110,000 over the period, largely unchanged from

Chart 4
Texas Firms' Capital Expenditure Plans More Bullish at Start of 2018



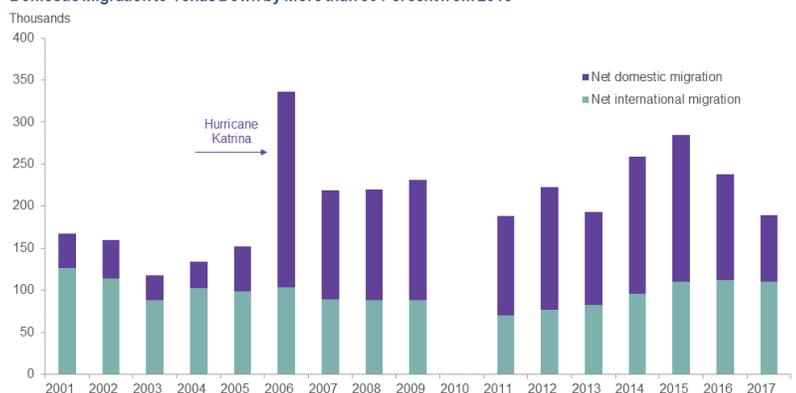
*Three-month moving average.
NOTES: Data are through January 2018. Firms are asked about expectations for capital expenditures six months from now. Services index is seasonally adjusted; manufacturing index is not because it does not exhibit seasonality.
SOURCE: Federal Reserve Bank of Dallas Texas Business Outlook Surveys.

Chart 5
Broad Unemployment Rate Back Near Prerecession Low



*Six-month moving average, seasonally adjusted.
NOTE: Data are through December 2017.
SOURCES: Census Bureau Current Population Survey; seasonal and other adjustments by the Federal Reserve Bank of Dallas.

Chart 6
Domestic Migration to Texas Down by More than 50 Percent from 2015



NOTES: Census Bureau population estimates approximate the population on July 1 of the year indicated and, thus, capture changes from the prior 12 months. Data are not available for decennial census years.
SOURCE: Census Bureau.

the prior two years but up 15 percent from the 12 months ended in July 2014 (*Chart 6*). Texas continues to experience the fourth-largest net inflow of international migrants among the states.

The number of domestic migrants to Texas fell by more than half between the periods of July 2014 to July 2015 and July 2016 to July 2017, as the oil bust damped the Texas economy during a period of relative strength elsewhere in the U.S. Despite the easing in net domestic migration to Texas, the state still recorded the second-largest net inflow of domestic migrants in the most recent period, trailing only Florida. With Texas now once again posting robust job growth relative to the U.S., domestic migration to the state might pick up going forward.

Texas Core Inflation Continues to Accelerate

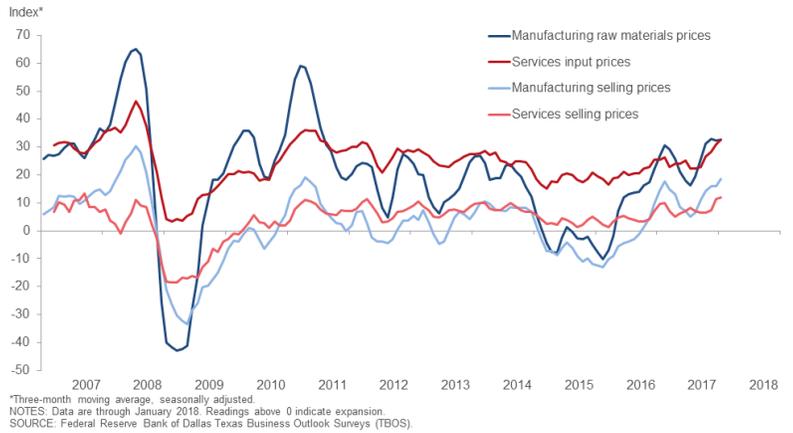
Texas core inflation has picked up slightly in recent months. The 12-month change in Texas core consumer price index (CPI) edged up to 2.2 percent in October and 2.3 percent in November. For Texas headline CPI, the 12-month change ticked up to 2.9 percent in October then edged back to 2.7 percent in November.

Firms responding to TBOS indicate that upward pressure on input and selling prices remained elevated across the board in January, with increases in the three-month moving averages of the input prices index and selling prices index in the manufacturing and services surveys (*Chart 7*). The three-month moving average of the selling prices index reached its highest level since mid-2011 among manufacturers and since September 2007 among services firms.

Looking ahead, the TBOS future price measures suggest inflation in Texas will likely continue rising. The manufacturing survey's six-months-ahead future selling prices index remained elevated in January after reaching a 10-year high in December. The service sector survey's future selling prices index rose for the third month in January, also reaching a 10-year high.

—Stephanie Gullo and Emily Kerr

Chart 7
TBOS Indexes Show Further Price Appreciation



About the Authors

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