



## Texas Service Sector Outlook Survey

DALLASFED

December 30, 2014

### TEXAS SERVICE SECTOR GROWTH CONTINUES BUT LESS OPTIMISM IN OUTLOOK

Texas service sector activity continued to reflect expansion in December, according to business executives responding to the Texas Service Sector Outlook Survey. However, the revenue index, a key measure of state service sector conditions, fell from 25.4 to 20.5.

Labor market indicators reflected steady employment growth and longer workweeks. The employment index came in at a reading of 14.5, similar to November. The hours worked index edged up from 4.4 to 7.3 this month.

Perceptions of broader economic conditions reflected less optimism in December. The general business activity index declined from 17.3 to 12.7. The company outlook index dropped from 17 to 8.6, with 21 percent of respondents reporting that their outlook improved from last month and 13 percent noting it worsened.

Price and wage pressures held steady this month. The selling prices index was mostly unchanged at 8.4, indicating prices increased at a similar pace as in November. The wages and benefits index held steady at 16.9, suggesting labor costs increased at the same pace as last month, although the great majority of firms continued to note no change in compensation costs.

Respondents' expectations regarding future business conditions reflected less optimism in December. The index of future general business activity remained positive but plunged from 33.1 to 17.4, its lowest reading since October of last year. The index of future company outlook fell sharply from 31.1 to 19.6. Indexes of future service sector activity, such as future revenue and employment, remained in solid positive territory this month.



### RETAIL ACTIVITY STRENGTHENS

Retail sales improved notably in December, according to business executives responding to the Texas Retail Outlook Survey. The sales index advanced from 16.7 to 23.3. Inventories increased at a faster pace than last month.

Labor market indicators reflected slightly faster employment growth and longer workweeks. The employment index edged up 2 points to 12.9, indicating retail jobs increased at a faster pace than in November. The hours worked index advanced back into positive territory to a reading of 5.6, suggesting longer workweeks, although the great majority of firms continued to note no change.

Retailers' perceptions of broader economic conditions reflected less optimism in December. The general business activity index retreated 8 points to 18.7. The company outlook index plunged from 25.1 to 9.8, with 20 percent of respondents noting an improved company outlook over the prior month, compared with 10 percent reporting their outlook had worsened.

Retail price pressures eased while wage pressures increased this month. The selling prices index declined from 15.4 to 5.6. The wages and benefits index rose slightly from 14.8 to 16.6, although the great majority of firms noted no change in labor costs.

Retailers' perceptions of future broader economic conditions reflected less optimism in December. After surging last month, the future general business activity index dove 19 points to 22. The index of future company outlook fell sharply from 42.6 to 24.9, its lowest reading in a year and a half. Indexes of future retail sector activity remained in solid positive territory 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.**

The Dallas Fed conducts the Texas Service Sector Outlook Survey monthly to obtain a timely assessment of the state's service sector activity. Data were collected Dec. 15–23, and 246 Texas business executives responded to the survey. 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.

**Next release:** January 27, 2015

## 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	20.5	25.4	-4.9	Increasing	62	36.3	47.8	15.8
Employment	14.5	15.3	-0.8	Increasing	58	21.2	72.1	6.7
Part-time employment	3.9	5.7	-1.8	Increasing	14	10.0	83.9	6.1
Hours worked	7.3	4.4	+2.9	Increasing	11	11.2	84.9	3.9
Wages and benefits	16.9	17.6	-0.7	Increasing	67	19.4	78.1	2.5
Input prices	20.5	25.3	-4.8	Increasing	68	25.6	69.3	5.1
Selling prices	8.4	9.3	-0.9	Increasing	49	13.6	81.2	5.2
Capital expenditures	9.3	9.9	-0.6	Increasing	64	17.5	74.4	8.2
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	8.6	17.0	-8.4	Improving	40	21.3	66.0	12.7
General business activity	12.7	17.3	-4.6	Improving	38	23.3	66.1	10.6
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	42.5	49.4	-6.9	Increasing	70	56.0	30.5	13.5
Employment	26.9	42.6	-15.7	Increasing	69	37.5	51.9	10.6
Part-time employment	7.4	13.1	-5.7	Increasing	30	16.9	73.6	9.5
Hours worked	4.8	5.1	-0.3	Increasing	13	11.9	81.0	7.1
Wages and benefits	42.6	44.1	-1.5	Increasing	96	45.0	52.6	2.4
Input prices	37.8	47.4	-9.6	Increasing	96	45.0	47.9	7.2
Selling prices	27.7	30.8	-3.1	Increasing	68	35.6	56.5	7.9
Capital expenditures	21.4	31.3	-9.9	Increasing	69	33.0	55.4	11.6
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	19.6	31.1	-11.5	Improving	40	36.0	47.7	16.4
General business activity	17.4	33.1	-15.7	Improving	39	31.4	54.6	14.0

\*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.

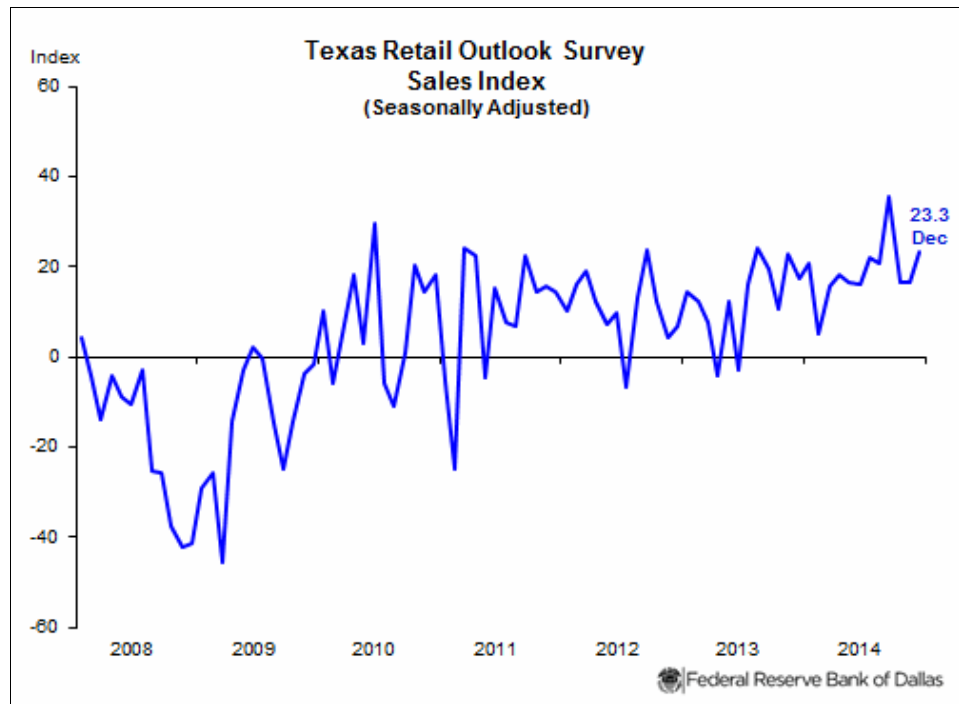
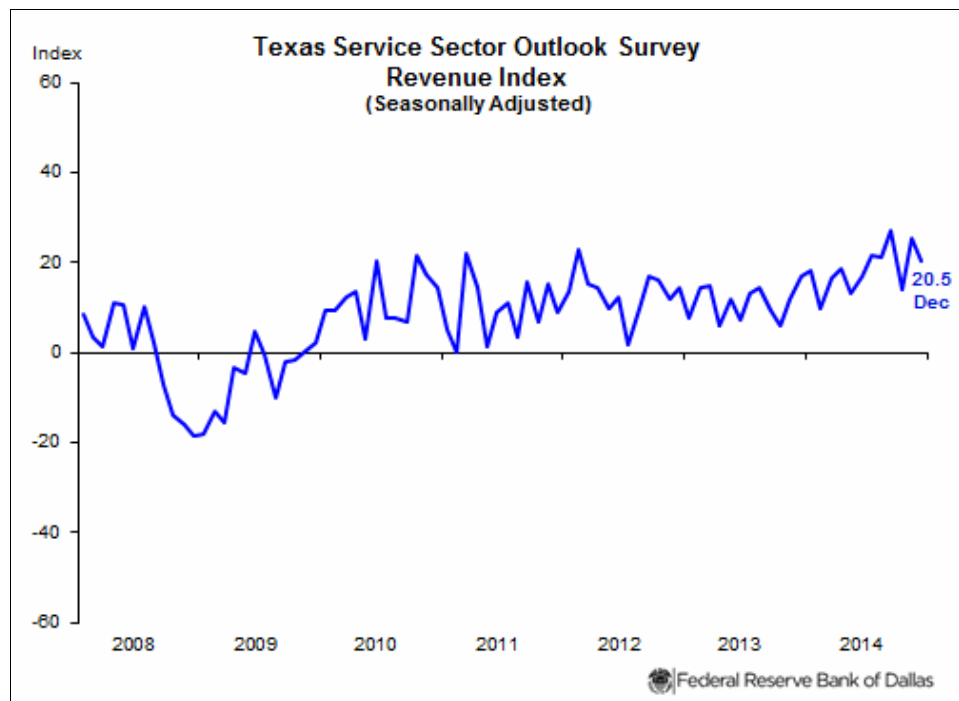
## TEXAS RETAIL OUTLOOK SURVEY

Business Indicators Relating to Facilities and Products in Texas, Retail Current (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	23.3	16.7	+6.6	Increasing	18	36.2	50.9	12.9
Employment	12.9	10.9	+2.0	Increasing	5	14.3	84.3	1.4
Part-time employment	1.8	-1.8	+3.6	Increasing	1	12.3	77.2	10.5
Hours worked	5.6	-2.9	+8.5	Increasing	1	8.0	89.6	2.4
Wages and benefits	16.6	14.8	+1.8	Increasing	46	19.7	77.2	3.1
Input prices	7.9	22.4	-14.5	Increasing	53	17.8	72.3	9.9
Selling prices	5.6	15.4	-9.8	Increasing	29	14.8	76.0	9.2
Capital expenditures	13.5	8.7	+4.8	Increasing	14	18.6	76.3	5.1
Inventories	25.7	19.0	+6.7	Increasing	35	32.7	60.3	7.0
Companywide Retail Activity								
Sales	22.8	17.3	+5.5	Increasing	43	35.5	51.8	12.7
Internet sales	9.7	0.0	+9.7	Increasing	1	14.6	80.5	4.9
Catalog sales	14.3	-2.6	+16.9	Increasing	1	14.3	85.7	0.0
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	9.8	25.1	-15.3	Improving	20	19.8	70.2	10.0
General business activity	18.7	26.7	-8.0	Improving	20	27.2	64.3	8.5
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	39.9	54.2	-14.3	Increasing	70	54.6	30.7	14.7
Employment	10.4	32.9	-22.5	Increasing	60	25.0	60.4	14.6
Part-time employment	7.5	4.6	+2.9	Increasing	18	17.5	72.5	10.0
Hours worked	-0.7	6.5	-7.2	Decreasing	1	10.8	77.7	11.5
Wages and benefits	39.6	39.8	-0.2	Increasing	72	43.0	53.5	3.4
Input prices	28.6	35.8	-7.2	Increasing	68	39.3	50.0	10.7
Selling prices	28.6	39.3	-10.7	Increasing	68	41.1	46.4	12.5
Capital expenditures	16.0	35.8	-19.8	Increasing	45	32.1	51.8	16.1
Inventories	21.5	25.9	-4.4	Increasing	61	34.3	52.9	12.8
Companywide Retail Activity								
Sales	50.1	46.8	+3.3	Increasing	69	57.8	34.5	7.7
Internet sales	24.4	29.3	-4.9	Increasing	69	26.8	70.7	2.4
Catalog sales	20.1	11.0	+9.1	Increasing	14	20.1	79.9	0.0
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	24.9	42.6	-17.7	Improving	69	39.7	45.4	14.8
General business activity	22.0	41.3	-19.3	Improving	39	38.7	44.6	16.7

\*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.

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## COMMENTS FROM SURVEY RESPONDENTS

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

### Credit Intermediation and Related Activities

- > The slowdown in oil and gas exploration will impact service jobs for truck drivers and oil rig workers and possibly some service companies dependent on pipe sales to drilling companies. We expect to see a slowdown in fracking and mining, drilling rig manufacturing, water sales and the salt water disposal business. Generally, the savings that consumers realize with lower fuel prices will offset considerably the pullback in the oil industry nationally. We think Texas will slow down some, but our versatility in production and manufacturing will help keep us moving forward. Christmas retail sales will serve as a conduit into January as will the state's huge wild game industry. Goats, cattle and sheep markets are strong with very little change expected since inventory levels will not be replenished for several years.
- > The slide in crude prices has already impacted the employment market in Houston. If we see prices continue to fall, the local economy could really slow. Hopefully, we will see some price stabilization.

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

- > About 60 percent of our business is servicing equipment for the oil and gas industry. The price of oil is resulting in less demand for our services.
- > Job growth has stopped, and retail sales are flat in our area. Agricultural sectors are doing well, but we see no bounce in the Panhandle.

### Funds, Trusts and Other Financial Vehicles

- > The uncertainty and volatility of oil prices has created concerns.

### Publishing Industries (except Internet)

- > The price of oil bears a real risk for our operations. If we begin to see layoffs in the production fields, the corresponding decline in retail spending in our smaller markets will result in even quicker reductions in retail advertising spending. In turn, our outlook of an improved situation in six months would likely not materialize.
- > We are experiencing big jumps in our health insurance costs. If our old plan did not get grandfathered in, either our rates would have gone up more than 30 percent or our employees' benefits would have dramatically worsened.

### Real Estate

- > We think oil prices in the \$50 per barrel range will definitely change the residential real estate market by mid-2015. The extent of the impact will depend on how long oil stays below \$70 per barrel.

### Rental and Leasing Services

- > Much of our Texas economy and sales are directly or indirectly tied to the energy industry. If that industry continues to free fall, next year will be a very tough year with many idle assets and personnel layoffs. We know how fast our revenue line can flatline in an energy bust, and as large as we are now, we will have to act quickly and aggressively to reduce expenses—meaning terminate employees quickly. If the bonus depreciation tax incentive is not extended, we will use our total line of credit to borrow to pay taxes next year, rather than growing our company, which will further promote a sorry year.

### Professional, Scientific and Technical Services

- > We believe oil prices in the \$60 per barrel range are going to wreak havoc on Houston.
- > We are very focused on oil prices. Being a firm with a material interest in the energy markets, we will see how collapsing oil prices impact the market and our customers. We believe activity will be muted somewhat as this plays out during the first few quarters of next year.
- > Although we've seen only one project delayed so far, we are anticipating a decline in local commercial real estate activity due to depressed oil prices.
- > Low energy prices may be great for some parts of the country, but we think they are going to cause a major jump in unemployment in Texas if they stay down.

### Management of Companies and Enterprises

- > It will be interesting to see the longer-term impact low crude prices will have on the Texas economy. So far so good, but we can't help but expect a slowdown in everything from hospitality to retail.
- > Our biggest concern is federal regulations. We have no clue what is going to change in the regulatory arena, so we're waiting for more certainty.

### Administrative and Support Services

- > The oil industry is a very important component of the general economy here. We think the decline in oil prices will likely reduce activity. The Affordable Care Act will have an effect as well.
- > The luxury end of travel has seen a pullback due to world events, tax bills coming due and the overall mood of the wealthy for their future expendable income levels.
- > Falling oil prices are having a negative impact on our industry. We anticipate a temporary dip in revenues but are optimistic sales will pick up by second quarter 2015.
- > We expect to see improved customer sales as the restaurant sector improves. Investments in new systems should reduce expenses,

and new services should improve overall revenue. The real estate sector is mixed as rents improve, but competition and sales of properties put pressure on expenses.

### **Hospitals**

- Governmental regulations and reductions in funding continue to negatively impact rural hospitals.
- We expect declining oil prices to have a moderating impact on economic growth in the months ahead, but there have been no impacts so far.

### **Social Assistance**

- We are closely tied to government defense spending, which is definitely up.

### **Amusement, Gambling and Recreation Industries**

- The biggest issue in Austin in our business is the lack of employees. There are huge hotels opening and new restaurants and lots of construction. All the above severely reduce the available number of employees. The cost of labor and the related tax and benefits costs have gone up for us by 6 percent this year so far. We are anticipating further increases in the near future. In addition, the cost of living in Austin has gone way up, which means available employees live further and further away from the central business district. The price of beef is also spiking. We have not, as of yet, seen any relief from the lower gas prices.

### **Religious, Grantmaking, Civic, Professional and Similar Organizations**

- Our outlook has worsened due to the falling price of crude oil.

### **Food Services and Drinking Places**

- We closed a store in the San Antonio area in early December, which is causing the drop in sales. Comparable store sales are actually up double digits. In February 2015, we will open another location in the El Paso area that will result in increased sales. Overall business is very strong, which is probably due to lower gas prices. Cheese prices have also pulled back, improving our cost of sales, and forecasts are for lower cheese prices throughout 2015. Health care costs are up due to increased enrollment under the Affordable Care Act—we had 30 percent participation in our plan, which is now offered to hourly employees with more than 30 hours, and increased participation from our management group, which has always been eligible but didn't take coverage.
- Starting in mid-December, we jumped from a mediocre holiday season to very strong sales—this is the first incident of nearing seasonal record highs in a long time. Wages and benefits costs are up because of the large benefit cost increases, particularly for health care, effective now for the 2015 benefits package. Costs of goods sold have been flat lately, but we know we have some substantial increases to face in just a couple of weeks with the expiration of annual contracts for several high volume products we use, particularly proteins. We took a 1.3 percent price increase because of the health care increases and the expiration of the commodities contracts on Jan. 1. Capital expenditures are up because we just completed remodeling one store and are building a new one. We have a better outlook mostly because of the recent jump in sales. If we can exceed some seasonal peaks from last year through the remaining portion of the holiday season, we may very well be heading into next year with a solid chance of sales increases over the price increases in place.
- With the drop in oil prices, Texas will experience some tough times in 2015, and maybe 2016.
- We suspect the lower cost of gasoline has increased retail activity.

### **Repair and Maintenance**

- It remains to be seen what the lower oil prices will do to the Texas Panhandle and surrounding area economy. So far, our customers are still going ahead with plans to build out infrastructure for the natural gas and natural gas liquids being produced in this area. We predict that drilling may slow, but gas prices seem to be holding up better than oil prices, so business activity should remain strong in this area.

### **Truck Transportation**

- While fuel prices have improved, the drop in oil prices has hurt some segments of our business.

### **Transit and Ground Passenger Transportation**

- Lower energy prices are the driving force behind our anticipated lower costs.

### **Pipeline Transportation**

- The dramatic decrease in oil prices will have a marginal indirect impact on our midstream business—not significant, but noticeable. The impact on exploration and production and service and supply companies will be direct and material and will result in layoffs and reduced capital expenditures. As a result of momentum in the system already, any meaningful impact on midstream activities will likely be delayed for six months or so.

### **Support Activities for Transportation**

- Lower oil prices are expected to reduce our revenue beginning in about six to nine months.

### **Merchant Wholesalers, Durable Goods**

- The oil price drop is catching the market by surprise. Builders are probably a little confused as to the impact on home buyers. We think everyone will be excited about the drop in gasoline prices at first and then will resume their normal everyday lives with a little more money in their pockets. They will spend, and this improves the housing outlook. Also, housing affordability is improving, meaning first-time buyers will be able to afford to enter the market, giving the construction industry a boost, which we have not

had. We believe the market may pull back and slow down a little, but we see a gradually increasing rate of construction throughout 2015. We expect Texas starts to be up over 12 percent next year.

- 2014 was a heavy capital expenditure year, and we do not expect the same level of activity in 2015.

### **Merchant Wholesalers, Nondurable Goods**

- We will have substantial additional costs to comply with the Affordable Care Act beginning in January.

### **Food and Beverage Stores**

- Our expectations for hiring and construction across most of Texas have turned down dramatically.

### **Health and Personal Care Stores**

- We believe the cost associated with the employer mandate of the Affordable Care Act will begin to negatively impact business expenses and ultimately increase consumer costs over the foreseeable future beginning in mid-year 2015.

### **Nonstore Retailers**

- With the ongoing drop in fuel prices, we're still worried about smaller oil companies and the impact on them if prices don't stabilize soon. For now, we are still seeing improved demand for our services.

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Questions regarding the Texas Service Sector Outlook Survey can be addressed to Amy Jordan at [amy.jordan@dal.frb.org](mailto:amy.jordan@dal.frb.org).  
The Texas Service Sector Outlook Survey can be found online at [www.dallasfed.org/microsites/research/surveys/tssos/](http://www.dallasfed.org/microsites/research/surveys/tssos/).

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