

The Southwest Skirts Recession

"[T]he Southwest has outperformed the nation across a broad spectrum of goods and services industries."

As the U.S. economy slipped into recession last year, the Southwest economy continued to grow. Since June 1990, national employment figures have dropped, but employment has increased in the Southwest (*Chart 1*). Although the Southwest has outperformed the nation across a broad spectrum of goods and services industries, the relative performance of the goods-producing sector has been particularly important. (In this article, Southwest refers to Texas, Louisiana and New Mexico.)

Manufacturing, construction and mining represent only about 23 percent of nonfarm employment in the nation; yet, these industries account for about 76 percent of the net jobs lost since June 1990. The

Southwest goods-producing sector, however, has added jobs during this period. Seasonally adjusted statistics indicate that the goods sector lost 1.3 million jobs (5.2 percent) in the nation but gained 22,500 jobs (1.2 percent) in the Southwest.

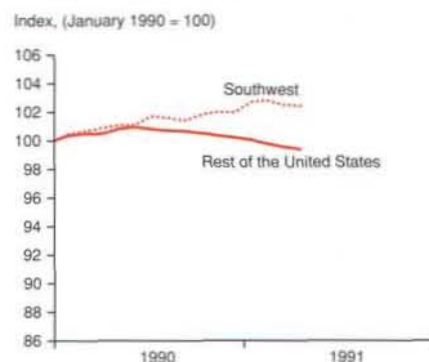
Manufacturing, Construction and Energy: Keys to Growth

Manufacturing. Manufacturing employment has declined in both the nation and the Southwest. However, manufacturing represents 17 percent of employment in the nation and 13 percent of employment in the Southwest, and the region's smaller share has helped limit the decline's impact on the Southwest economy. An even more important factor has been the size of the decline, which has been slight in the Southwest but sharp elsewhere in the nation. One reason the Southwest's manufacturing sector has not declined as much as the nation's is that the Southwest is the national production center for two industries that have performed strongly over the past year—petrochemicals and oil field equipment. Another reason is because the food processing industry's growth has been stronger in the Southwest than in the nation during the past year.

The Gulf Coast is home to 32 percent of the world's and 85 percent of the nation's ethylene capacity (65 percent in Texas and 20 percent in Louisiana).¹ Ethylene is a key building block for plastics and synthetic rubber, and in the late 1980s, a jump in profit margins for the product spurred a boom in the petrochemical industry along the Gulf Coast. Continued strength in petrochemical production has boosted chemical employment in the Southwest, while nationally employment in the chemical industry has declined (*Chart 2*).

The Southwest is the nation's center for production of oil field equipment; 70 percent of the

Chart 1
Nonagricultural Employment



nation's employment in this industry is in the Southwest. Employment in this industry in Texas increased 11.7 percent from June 1990 to April 1991. The industry has drawn much of its strength from increased international drilling and exploration. The boom in oil field equipment production was an important part of a 21.5 percent increase in Texas exports of nonelectrical machinery in 1990. As *Chart 3* shows, employment in nonelectrical machinery in the Southwest has increased strongly over the year, while it has declined nationally.

Unlike the oil field machinery and petrochemical industries, the food processing industry represents a slightly lower share of employment in the Southwest than in the nation. Employment in this industry, however, has grown strongly in the Southwest while increasing only

Chart 2
Chemical Employment

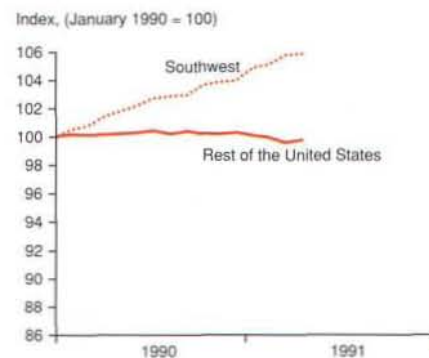
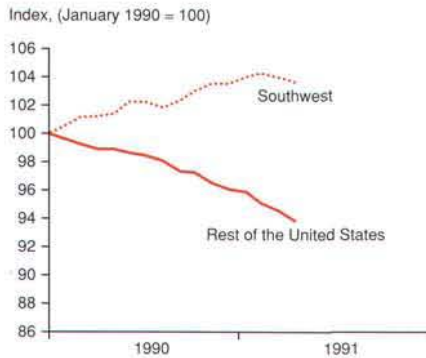


Chart 3
Nonelectrical Machinery Employment

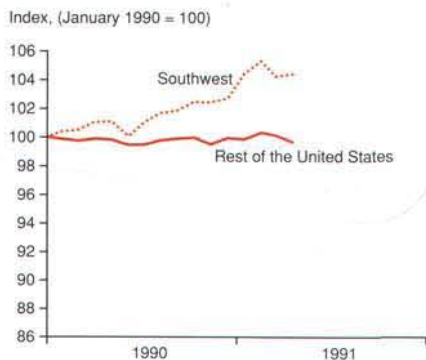


slightly in the nation (*Chart 4*). One reason for the recent strength is that Texas was one of several states that supplied the military rations for the soldiers in the Persian Gulf.

Construction. During the current U.S. recession, construction has been one of the weakest industries in the U.S. economy. In the Southwest, however, this industry has continued to grow, largely because of expansion in petrochemicals (*Chart 5*). In mid-1989, more than \$3 billion in petrochemical plant expansion was under way in the Houston area alone. The petrochemical expansion continued throughout 1990 and into 1991, and billions of dollars worth of new plants are currently being built.

Residential construction has also been relatively healthy. Between 1987 and 1989, the Southwest experienced steady economic growth and minimal residential

Chart 4
Food Processing Employment



construction. By 1989, residential occupancy rates and rents in many major metropolitan areas in the Southwest had risen significantly and a mild rebound began in residential construction. Although consumer uncertainty about the Middle East crisis caused some mild declines in residential construction in the Southwest during the second half of 1990 and early 1991, this sector continued to perform significantly better in the region than in the nation.

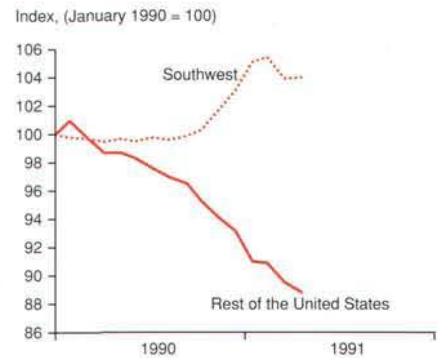
Energy. While the Southwest economy is much less dependent on the energy sector than it was in the early 1980s, this sector has provided an important stimulus to the region over the past year. The drilling rig count in the Southwest increased in the fourth quarter in response to higher oil prices but has since declined sharply because of declines in oil prices and continued weakness in natural gas prices. However, increased overseas exploration and development by energy companies in the Southwest has allowed oil and gas extraction employment in the region to rise 2.3 percent since June 1990.

Outlook: Many Industries Set to Rebound

While the Southwest has managed to skirt a recession, employment growth has weakened since January, as shown in Chart 1. Respondents to a Dallas Fed survey of Southwestern businesses in mid-April noted a significant decline in orders from states outside the region. Declines were particularly noticeable in industries that serve the national construction and auto markets, such as lumber and wood products, primary metals and plastics.

The recent weakness, however, is unlikely to continue, and the Southwest most likely will avoid a recession. Construction and oil field equipment production should continue to increase over the second half of 1991. Although

Chart 5
Construction Employment



chemical production is likely to weaken because of current high inventories and food processing should decline because of decreased demand for military rations, many industries are set to rebound. Responses from a Dallas Fed survey in late May indicate a mild but broad upswing in orders and a more optimistic outlook at many businesses. Also, the Texas leading index, produced by the Dallas Fed, increased in March and April, indicating some improvement is likely to begin in the third quarter.

— Keith R. Phillips

¹ Figures are from 1989 and were derived from *Oil and Gas Journal*, Sept. 4, 1989, pages 56–60.

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