PER

TEXAS BUSINESS REVIEW

Bureau of Business Research
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The Texas Economic Climate

The typical dog days of late summer, seasonally predictable if not necessarily economically debilitating to Texans and those in the Southwest, were negatively compounded this year by recessionary forces as serious as any experienced since the Great Depression of the 1930s. The dry heat of August will inevitably give way to fall's cooler and more benign conditions. Whether improvements in the state's economy can be, with comparable certainty, expected to occur is a question to which many yet see no positive answer.

The repetitive regularity of seasonal forces, in the absence of unusual conditions such as sharp and sustained temperature drops or heavy spring flooding, results in the development of response mechanisms in society that serve to minimize the costs or pains associated with those changes. Knowing that winter is coming, for example, generates purchases of heavier coats in the back-to-school sales of August and September.

More serious movements in economic activity are often associated with cyclical forces. Older views once held that business cycles were nearly on a par with annual seasonal changes in terms of their inevitability. More modern attitudes would suggest that cyclical changes can be influenced and dampened by judicious monetary and fiscal policies. Such attitudes are not fundamentally inconsistent with widespread and proper skepticism that swings in employment, output, and prices can be virtually eradicated by enlightened public policies in societies that retain reliance on free market forces. While the economics profession came close in the early 1960s, the day on which economics will be widely regarded as the most successful and effective social science will not soon return, if indeed it ever came at all.

Market forces inherently involve excesses of activity. Equally inherent are the mechanisms that work toward a return to stability. Harris County realtors will be less underemployed, for instance, when Houston home prices fall sufficiently to invite purchases from those no longer able to resist the bargains. Vultures do, after all, help clean up. And cleanliness is a state to be sought.

Since markets do a remarkable job of self-correcting, there is some hope for the region's economy in the foreseeable future, even though that process will continue to generate the type of financial pain that is revealed by the high and rising numbers of foreclosures, personal bankruptcies, and business failures, not to mention the magnitude of the state's budget deficits. Not to put too much of a "Pollyanna" touch to the point, bankruptcies, it may be remembered, are ways of ending a losing game in order to start another afresh. New starts are a measure of restored vitality.

A look at the standard set of economic indicators for Texas, however, gives no real comfort yet that major strides are being made on the path of self-correction toward prosperity. The more pessimistic observers are asking whether there are secular forces at work that are not accompanied by an "internal" adjustment device that will sooner or not too much later set things right. Whether these forces are geopolitical—and global as well—or ethical and philosophical (e.g. moral decay, decline of the work ethic, the pervasive destruction of a drug culture, etc.), it is difficult to ignore entirely their impact on the Texas economy and the ability of the state's business enterprises to be persistently competitive.

Economic historians can still be roused to debate the question of whether the U.S. economy would have worked its way out of the Great Depression on its own devices. Was that decade not something more than the grandaddy of all business cycles? Were there not secular changes under way, then as now, that must be analyzed and understood if any accurate business conditions forecasting is to be done? The answer is self-evident.

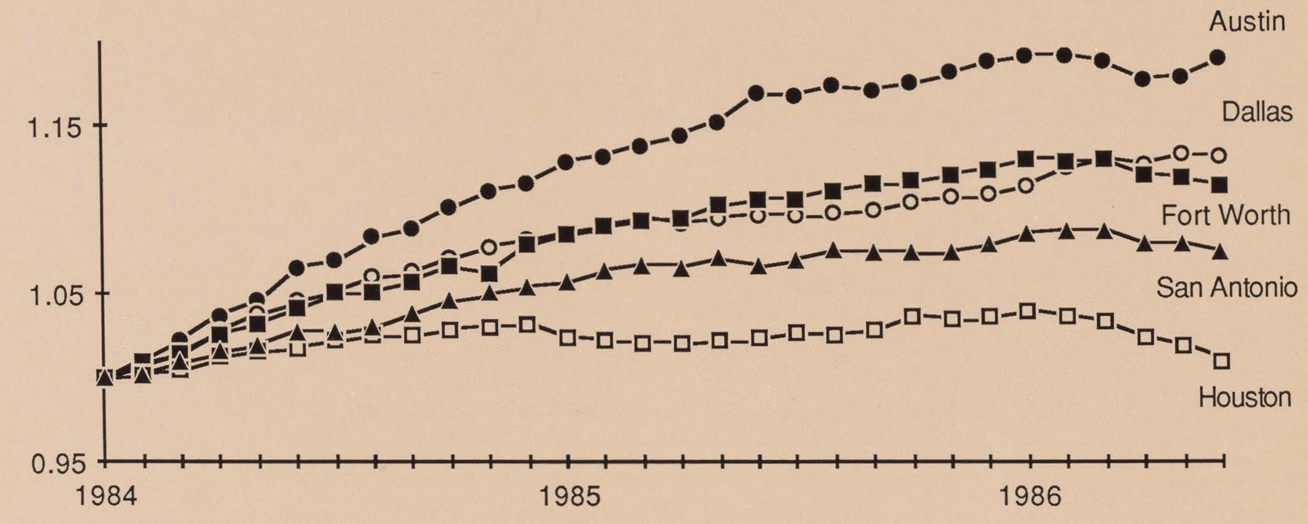
Thinking about the state's current economic malaise against the backdrop of the 1930s does produce some interesting comparisons, many of which speak well to how much better off we truly are today. The recent business press, for example, has made much of the bank failures that have occurred in Texas so far this year and of the supervisory reactions to the plight of many thrift institutions caught with portfolios jammed with mortgage loans underwritten when legitimate appraisals produced values conspicuously higher than those prevailing in today's market place. Note, though, that depositors have not lost a penny, thanks to the continued effectiveness of two 1930s creations, the FDIC and the FSLIC. Clearly, neither federal deposit insurance fund is overfunded; a bill that would provide major recapitalization of the FSLIC is currently under review by the U.S. Congress. But the effectiveness of the regulatory and supervisory apparatus attached to the system of depository institutions has been sorely tried in this region and *not* found wanting.

Work-out specialists (not those who dance aerobically before videotapes of svelte movie stars) will face major challenges in assisting Texas' financial institutions. As of this writing, bills before the special session of the Texas legislature to ease the state's entry into interstate banking and to relax the long-standing restrictions against branching will be, if passed, of no small significance to those regulatory officials whose ultimate objective is the preservation and enhancement of public confidence in the state's system of depository institutions.

On the industrial front, the Bureau's *Texas Industrial Expansion* newsletter has revealed a marked decline in the new and expanding manufacturing operations in Texas reported in the issues dated January 1986 through September 1986. This obviously reflects the impact of plummeting oil prices, continued foreign competition, and the prolonged semiconductor slump on the state's industrial growth. The newsletter reported 196 new plants and expansions during that period against 257 for the same period in 1985. Furthermore, *Industrial Expansion* reported 40 plant closings or production cutbacks and 70 layoffs or work-force reductions for the first nine months of 1986 against 18 and 32 for the same period the year earlier. The average size of the 1986 layoff is about 300 and is predominantly in oil-related activities. Layoffs were recorded in all depressed industries—steel, rubber, textile, and semiconductors.

A major source for new and expanding industry material for the newsletter, Texas Economic Development Commission's quarterly report on industrial revenue bond activity in the state, has shown severe declines

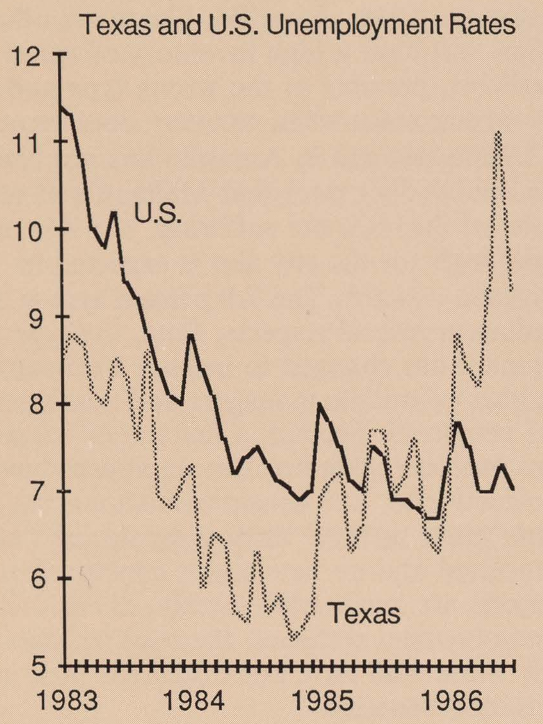
Nonagricultural Employment in Five Largest Texas Metropolitan Areas (January 1984=1.00)



Nonagricultural Employment and Total Unemployment Rate by Metropolitan Area

Area	Nonagricultural employment (thousands) July 1986	July 1985	Percentage change	Unemployment rate July 1986
Abilene	51.9	52.5	-1.1	10.0
Amarillo	80.8	81.2	-0.5	6.9
Austin	364.4	354.7	2.7	5.8
Beaumont-Port Arthur	128.0	136.7	-6.4	15.6
Brazoria	57.1	58.5	-2.4	12.0
Brownsville-Harlingen	65.5	64.2	2.0	16.2
Bryan-College Station	47.0	47.3	-0.6	7.6
Corpus Christi	133.1	134.9	-1.3	12.5
Dallas	1,347.8	1,312.4	2.7	5.9
El Paso	177.7	176.5	0.7	12.3
Fort Worth-Arlington	509.2	503.9	1.1	7.0
Galveston-Texas City	71.8	72.1	-0.4	11.7
Houston	1,469.8	1,491.1	-1.4	10.8
Killeen-Temple	68.9	67.1	2.7	8.2
Laredo	35.0	34.6	1.2	16.5
Longview-Marshall	67.2	68.7	-2.2	13.5
Lubbock	89.2	90.3	-1.2	7.1
McAllen-Edinburg-Mission	81.8	79.6	2.8	19.6
Midland	46.4	49.3	-5.9	12.5
Odessa	46.6	52.7	-11.6	17.9
San Angelo	36.2	37.1	-2.4	8.4
San Antonio	483.6	479.3	0.9	7.5
Sherman-Denison	37.2	37.1	0.3	8.3
Texarkana	45.2	46.2	-2.2	9.4
Tyler	63.0	63.0	0.0	8.7
Victoria	27.9	30.1	-7.3	11.9
Waco	76.6	77.3	-0.9	8.4
Wichita Falls	51.3	51.6	-0.6	8.5
Total Texas	6,666.6	6,684.5	-0.3	9.3

Note: These data reflect the Bureau of Labor Statistics' redefined metropolitan areas in Texas. Figures for total Texas nonagricultural employment reported in the August issue were incorrect; for the correct figures, call 471-5180.
Source: Texas Employment Commission.

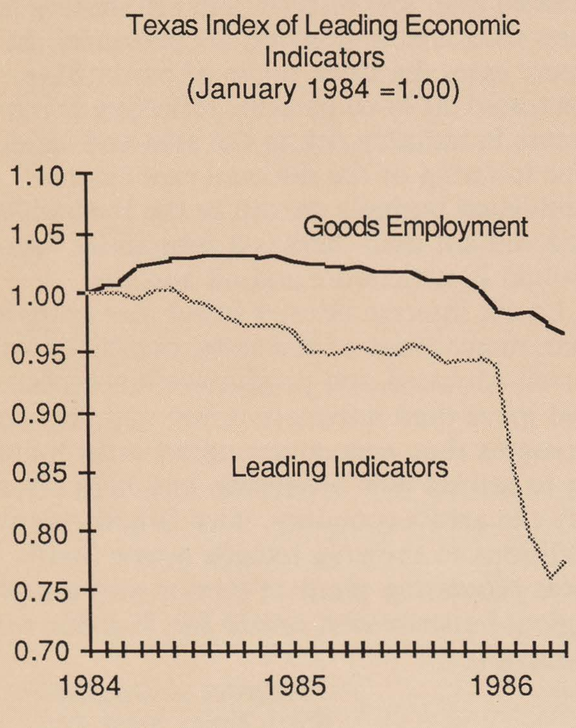


Source: U.S. Bureau of Labor Statistics.

Components of the Texas Index of Leading Economic Indicators (March 1986 - May 1986)

Measure	Mar.	Apr.	May
Manufacturing weekly hours	41.29	41.40	41.50
Retail sales (billions of 1967 dollars)	2.47	2.48	2.54
New housing permits (thousands)	9.53	8.61	7.87
U.S. wellhead price of oil (1967 dollars per barrel)	3.92	3.33	3.37
Initial claims for unemployment insurance (claims per thousand employees)	13.22	15.91	14.42
Leading indicators index (January 1984 = 1)	0.79	0.76	0.77

Note: All figures are seasonally adjusted.
Sources: Texas Employment Commission, U.S. Bureau of the Census, and U.S. Department of Energy.



and no growth at all in the manufacturing sector since the first of the year.

The defense industry has been the best performer this year, with major contracts being awarded to Bell Helicopter, LTV Corporation, and General Dynamics, all of which have major manufacturing operations in the Dallas-Fort Worth area. In fact, Boeing Electronics and Bell Helicopter are expanding significantly in the Dallas area, the latter in direct response to the $500-million Pentagon contract for Osprey aircraft.

There does appear to be a pickup in activity in the past six weeks, led by the Dallas and Houston areas. Whether this is a random blip in the record of the state's economic performance or a welcome signal that the self-corrections are indeed well under way remains to be seen.

—Robert D. Mettlen
Acting Director and
Lamar Savings Centennial
Professor of Finance

Tough Times in the Panhandle

The wishful optimism of spring has given way to the realities of economic recession in the Panhandle. The underpinnings of economic growth and stability in this area are under severe stress with the break in worldwide oil prices, continued misery in the agricultural sector, and the consequent rippling effect on financial and service companies. Recovery from these conditions is not just around the corner.

Even if oil prices for the benchmark West Texas Crude were to end the year on or near the predicted average range of $14 to $15 per barrel, up from lows of $7 to $8, the Panhandle oil industry would not show any growth in rig counts or exploration activity. The recent OPEC agreement, while welcome, is viewed with a cautious eye. If the agreement does hold, it will stabilize a floor price, not necessarily give impetus to growth in exploration and production. Refineries will take advantage of current pricing conditions; consequently, supplies of petroleum products should remain plentiful. Natural gas pricing is likely to turn around faster than oil prices, as the current gas bubble is predicted to work itself out in approximately two years.

The long-term outlook for West Texas agriculture has not improved in the past three quarters. Even with the weakening of the U.S. dollar, American agricultural products are competing for sales against those of many countries that are subsidizing farm sales. The cattle industry is still under pressure from a decline in the beef eating habits of the public and an oversupply of beef.

The full impact of overbuilding in commercial and retail real estate is just beginning to show up. Mortgage defaults are starting to inch upward and will quicken in the fourth quarter. Even with the flurry of refinancing, the increasing unemployment figures will flow through to mortgage defaults. This will not only weaken the current real estate markets but will add to the financial pressure on area lending institutions. The Amarillo area real estate market will begin to resemble that of Midland, Borger, and even Houston. After the enactment of the federal tax laws, real estate will not be able to spur the type of growth we have seen in past years because that growth was based on tax advantages more than on investment values. Amarillo, like many other cities, will have a high inventory of space available, possibly of the wrong type and in the wrong place when recovery does come.

Unemployment in Amarillo has not reached the double-digit rates that Midland and other areas of the state are suffering, but it is historically high for the city and is expected to continue upward. The 7.9 percent rate is misleading in several respects. First, the type of claimant has changed to include a substantial number of middle managers and administrative personnel. Second, a few major construction projects being brought on stream have provided jobs, but unemployment statistics will again move upward when these projects are completed and no new major construction projects are anticipated. Lastly, as with all unemployment statistics, the numbers show only those who have not exhausted their compensation benefits.

Area financial institutions have been hard hit with two major banks being closed—one in Midland and one in Borger. While these banks were reopened under new ownership, they are indicators of the problems area banks are continuing to have. Many major banks have increased loan loss reserves and are shoring up loan standards and laying off personnel. In many cases the stock prices of banks have decreased 50 to 60 percent, reflecting the increase in industry risk in the area and state. The lowering of the discount rate has not stimulated business growth in the Panhandle and will not until there is a substantial turnaround in agriculture and oil and gas.

Lower interest rates, a lower cost of living than many areas of the state, combined with a well-educated and productive labor pool and more than adequate power supplies are strengths that area communities must build on to attract new businesses and help diversify the area's economy. Two bright recent additions to the area include a new Swift meat processing plant in Pampa and a new regional distribution center for Wal-Mart in Plainview.

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The Bureau of Business Research serves as a primary source for data and information on Texas and on the dynamics of change. The Bureau's research program concentrates on the determinants of regional growth and development and investigates specific issues for clients. The information services division answers inquiries by telephone and mail, responds to walk-in visitors, and offers computerized data from the 1980 census of the population and on manufacturing firms in Texas. The publications division produces periodicals, directories, books, and monographs on a variety of topics that shape the development of the Texas economy.

Announcements

In September James F. Smith joined the Bureau staff as senior economist and associate director. Dr. Smith, formerly the director of regional services for Wharton Econometric Forecasting Associates, will serve as acting director for the remaining period of Dr. Victor Arnold's appointment with the Select Committee on Higher Education. The Bureau staff is grateful to Dr. Robert D. Mettlen, who was acting director from December 1985 until September 1986, for his leadership during the past months.

Preliminary 1985 population estimates by county have been released by the U.S. Bureau of the Census. Contact (512) 471-5180 for more information.