BusinessOutlookSurvey
Manufacturing
Federal Reserve Bank of Dallas

Texas Manufacturing Activity Expands and Business Conditions Improve

October 25, 2010

For this month's survey, manufacturers were asked supplemental questions on borrowing conditions and credit availability. See page 5 for results.

Texas factory activity increased in October, according to business executives responding to the Texas Manufacturing Outlook Survey. The production index, a key measure of state manufacturing conditions, was positive for the second consecutive month and slightly higher than its September reading.

Despite the rise in output, several other manufacturing activity indicators fell again. The new orders and shipments indexes were negative for the fifth consecutive month. The capacity utilization index dipped below zero, with more than one-quarter of respondents reporting a decrease.

Measures of general business conditions improved markedly in October, suggesting the broader economy strengthened. After four months in negative territory, the general business activity index rose sharply from –18 in September to 3 this month. The company outlook index also jumped up, rising from –4 to 13. The advance in the index was largely due to a sharp decline in the share of manufacturers reporting a worsened outlook, falling from 25 percent to 13 percent.

Labor market indicators worsened slightly in October. Hours worked fell for the fourth consecutive month, and the employment index dipped back into negative territory, with 15 percent of firms reporting layoffs compared to 11 percent reporting hiring. The wages and benefits index remained positive and edged up, although 80 percent of respondents noted no change in compensation costs.

Price pressures were mixed in October. Input costs continued to climb, with the raw materials price index rising from 24 to 30. Thirty-five percent of manufacturers saw an increase in prices paid for raw materials, compared with only five percent seeing a decrease. Finished goods prices fell as the index slipped into negative territory after a near-zero reading in September. Over the next six months, 43 percent of respondents anticipate further increases in raw materials prices, while one-quarter expect higher finished goods prices.

Manufacturers' six-month outlook improved further in October. The future indexes for production and capacity utilization rose again, as did the future index for new orders, with more than half of firms expecting an increase in order volume six months from now. The future general business activity index advanced from 5 to 14, and the future company outlook index rose to 27, with more than 90 percent of firms anticipating flat or improved conditions six months from now.

The Dallas Fed conducts the Texas Manufacturing Outlook Survey monthly to obtain a timely assessment of the state's factory activity. Data were collected October 12–20, and 104 Texas manufacturers responded to the survey. Firms are asked whether output, employment, orders, prices 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 of firms 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.

Next release: November 29, 2010

Company Business Indicators Relating to Facilities and Products in Texas Current								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	6.9	4.0	+2.9	Increasing	2	30.6	45.7	23.7
Capacity Utilization	-2.3	3.9	-6.2	Decreasing	1	24.3	49.0	26.6
Volume of New Orders	-4.3	-3.0	-1.3	Decreasing	5	24.6	46.4	28.9
Growth Rate of Orders	-2.5	0.0	-2.5	Decreasing	1	22.2	53.1	24.7
Unfilled Orders	-6.3	-14.0	+7.7	Decreasing	5	13.2	67.3	19.5
Volume of Shipments	-2.3	-1.0	-1.3	Decreasing	5	25.4	47.0	27.7
Delivery Time	-11.5	-9.0	-2.5	Decreasing	5	7.7	73.1	19.2
Materials Inventories	-1.9	-3.0	+1.1	Decreasing	6	17.3	63.5	19.2
Finished Goods Inventories	-12.5	1.0	-13.5	Decreasing	1	14.4	58.7	26.9
Prices Paid for Raw Materials	29.9	24.4	+5.5	Increasing	15	35.0	59.9	5.1
Prices Received for Finished Goods	-3.5	0.5	-4.0	Decreasing	1	11.2	74.1	14.7
Wages and Benefits	10.6	7.2	+3.4	Increasing	11	15.4	79.8	4.8
Employment	-4.1	1.8	-5.9	Decreasing	1	11.2	73.5	15.3
Average Employee Workweek (Hours Worked)	-7.7	-1.0	-6.7	Decreasing	4	13.5	65.4	21.2
Capital Expenditures	-1.9	-12.1	+10.2	Decreasing	2	11.8	74.5	13.7

General Business Conditions Current								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	13.0	-4.3	+17.3	Improving	1	25.9	61.2	12.9
General Business Activity	2.6	-17.7	+20.3	Improving	1	23.3	56.0	20.7

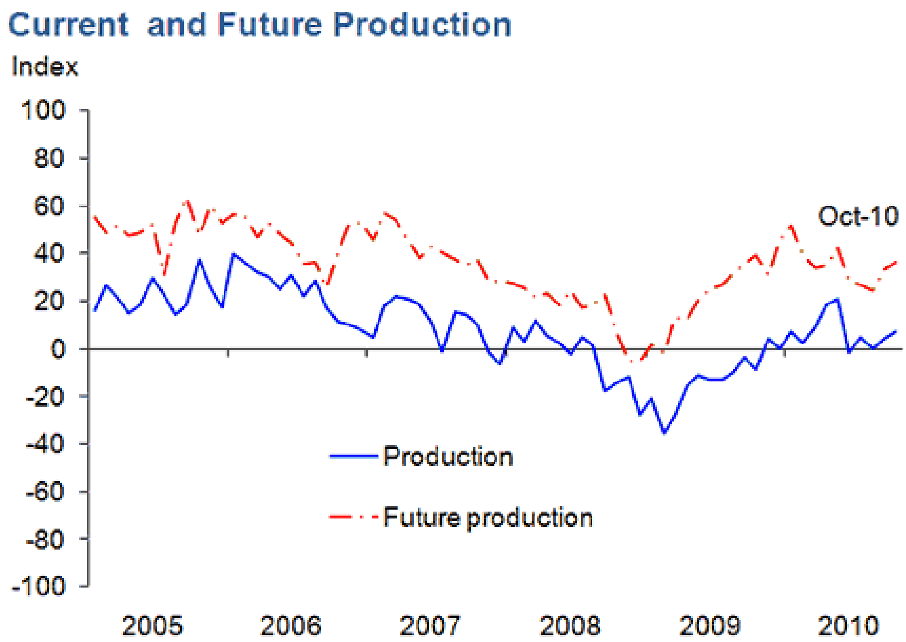
Company Business Indicators Relating to Facilities and Products in Texas Six Months Ahead								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	36.2	33.1	+3.1	Increasing	20	45.6	45.0	9.4
Capacity Utilization	36.0	25.3	+10.7	Increasing	20	43.8	48.4	7.8
Volume of New Orders	40.2	35.8	+4.4	Increasing	22	51.0	38.2	10.8
Growth Rate of Orders	35.4	22.5	+12.9	Increasing	20	43.4	48.6	8.0
Unfilled Orders	10.0	8.2	+1.8	Increasing	3	18.0	74.0	8.0
Volume of Shipments	34.9	30.8	+4.1	Increasing	20	43.5	48.0	8.6
Delivery Time	-5.0	-5.1	+0.1	Decreasing	7	5.9	83.2	10.9
Materials Inventories	2.0	-4.1	+6.1	Increasing	1	19.0	64.0	17.0
Finished Goods Inventories	-5.9	-10.3	+4.4	Decreasing	5	12.9	68.3	18.8
Prices Paid for Raw Materials	35.7	31.9	+3.8	Increasing	19	42.6	50.5	6.9
Prices Received for Finished Goods	11.0	19.8	-8.8	Increasing	3	25.0	61.0	14.0
Wages and Benefits	23.8	25.0	-1.2	Increasing	77	24.6	74.6	0.8
Employment	13.0	8.2	+4.8	Increasing	14	23.0	67.0	10.0
Average Employee Workweek (Hours Worked)	17.9	5.2	+12.7	Increasing	20	24.8	68.3	6.9
Capital Expenditures	10.1	6.2	+3.9	Increasing	11	18.2	73.7	8.1

General Business Conditions Six Months Ahead								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	26.9	13.5	+13.4	Improving	17	36.5	53.9	9.6
General Business Activity	14.2	5.2	+9.0	Improving	2	27.3	59.6	13.1

*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.



COMMENTS FROM SURVEY RESPONDENTS

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

Paper Manufacturing

We've seen an uptick in orders, although they are still off from 2007 levels. We anticipate a normally slow November through January; then we expect things to pick up again.

Food Manufacturing

We are still very adversely affected by high dairy prices and by record-high sugar prices.

Chemical Manufacturing

September was a record month for us. We think some of what we have seen is that many of our customers depleted their inventory and needed to restock. This has now been accomplished, so orders will be flat. The rig count will determine how things move forward. If it holds steady, then business will be steady, but if the rig count drops off substantially, then business will drop as well.

Nonmetallic Mineral Product Manufacturing

Business conditions continue to stagnate. There is continuing pressure on operating margins from excess capacity in the marketplace.

Current economic conditions remain lackluster at best. In light of the expected increase in foreclosures, we do not foresee any significant improvement in the home building industry until 2012.

Fabricated Metal Product Manufacturing

Our incoming orders have been decreasing for several weeks, and September bookings were less than August. We believe this is because our customers have completed restocking their inventory levels after the drastic drawdown of 2009. Some of our markets are yet to wake up, but our most substantial market of oil and gas drilling is strong and continues to grow as measured by the Baker Hughes rig count, which is now only 15 percent below its 2008 high for the U.S. and Canada. We feel we will slow some over the next few months, but not drastically.

We are experiencing a seasonal slowdown, but we also feel that normal activity is slowing.

There seems to be a slowing in the fourth quarter due to uncertainty regarding the election outcome and the impact of tax and health care changes. We continue to see positive signs that a movement is growing recognizing the importance of made-in-America for job creation and a strong stable economy. Therefore, we believe growth opportunities exist for American manufacturers who demonstrate best practices and strive to compete.

Computer and Electronic Product Manufacturing

Today our business outlook is positive but as in the past, it could change very quickly.

Questions regarding the Texas Manufacturing Outlook Survey can be addressed to Emily Kerr at emily.kerr@dal.frb.org.

The Business Outlook Survey can be found online at www.dallasfed.org/data/outlook.

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Special Questions

October 25, 2010

	Oct. '10 (percent)
1. How do borrowing conditions facing your firm compare to those six months ago?	
Eased substantially	2.7
Eased somewhat	13.5
No change	43.2
Tightened somewhat	5.4
Tightened substantially	5.4
Not applicable—haven't sought credit	29.7
2. To what extent is your business having difficulty obtaining financing for desired long-term uses such as capital expenditures?	
No difficulty	35.6
Some difficulty	12.3
Substantial difficulty	8.2
Extreme difficulty	1.4
Not applicable—haven't sought credit	42.5
3. To what extent is your business having difficulty obtaining financing for desired short-term uses such as paying workers and acquiring inventories of materials or supplies?	
No difficulty	36.1
Some difficulty	11.1
Substantial difficulty	5.6
Extreme difficulty	1.4
Not applicable—haven't sought credit	45.8
4. Has your firm's production and/or sales been adversely affected by difficulty obtaining credit?	
Yes, significantly	2.7
Yes, somewhat	9.5
No	29.7
Not applicable—haven't had problems obtaining credit	18.9
Not applicable—haven't sought credit	39.2
5. Has your firm reduced hiring and/or increased layoffs due to difficulty obtaining credit?	
Yes, significantly	1.4
Yes, somewhat	5.4
No	40.5
Not applicable—haven't had problems obtaining credit	14.9
Not applicable—haven't sought credit	37.8

Survey collection period: 10/19/2010–10/22/2010

Special Question Comments

These comments have been edited for publication.

Chemical Manufacturing

We have sufficient working capital to handle any accounts receivable or inventory needs internally. We only had one occasion in the last year to put together a long-term credit facility, and we had no trouble finding three banks to participate. We invited about seven banks to work with us, and we got three takers.

Plastics and Rubber Products Manufacturing

Borrowing conditions haven't changed, but the overall health of our business has improved such that we are no longer struggling to access credit. The irony is that we no longer need the credit facilities we sought during 2009 and early 2010. To further exacerbate the hiring issue, we let people go as a result of not being able to retain these needed credit facilities. Now, we will not be rehiring those let go. We'll supplement our needs with contract manufacturing elsewhere.

The biggest hiring barrier is finding people with the right skill set for an increasingly technical work environment.

Nonmetallic Mineral Product Manufacturing

The issue of obtaining credit for business purposes is not the problem. The problem rests with the uncertainty as to government policy and actions.

Fabricated Metal Product Manufacturing

Currently banks are knocking fervently on our door. They seem to have initiatives to reduce exposure in real estate and increase it in blue collar industrial business. Owner-occupied real estate does not seem to be a problem for these new bankers as long as we have remained profitable. We are worried now about our existing banking relationship and what might happen if another bank were to take over. We have a banker who fully understands our business and the direction we're leading the company.

We have used the same bank for over 10 years. Due to our relationship, we have not encountered any issues.

In the years prior to 2009, we were profitable. Our output is other companies' inventory, so the vast reduction of inventories in 2009 severely impacted our business and we had a horrific year. Once that ran its course, over the course of six months we regained a decent sales level and resumed profitable operations. However, due to the 2009 experience, we are currently unbankable. We placed our working capital line with an asset-based lender at a higher interest rate. When we talk to bankers about our situation, they are uniformly afraid to take us on at the present time. For our current year, which ends Oct. 31, we are actually more profitable than pre-2009, but nonetheless we are not bankable.

Credit entities are very risk adverse even when a company has demonstrated multiple years of profitability. There is an increased length of time to find someone willing to lend, and the lending process is also much longer. Manufacturing is a capital-intense industry, and it is difficult to grow (job creation) and compete without the latest technology equipment. Suppliers of materials continue to require shortened payment terms, which may reflect their difficulty in obtaining credit.

Our customers are primarily nonresidential subcontractors. Their inability to maintain operating credit facilities requires significantly more financing on us, the manufacturer, if we intend to remain a viable market leader.

Lines of credit have been substantially reduced, and loan covenants have been added, which are not achievable at this current level of production and lower-margin business. Overall, business is off 40 percent from 2009, and we are operating at unprofitable and unsustainable levels.

Machinery Manufacturing

We have an existing credit facility that has been adequate, so we haven't had any reason to renegotiate it in the past few years. We have been told it will not be difficult to renew it next year, but that the interest rates will be higher.

We have a large line of credit, and as long as we have been able to meet our objectives, which we have been doing, we haven't had any problems. We are with a big bank, so the objectives are reasonable but tough, and we have had a good year so there haven't been any problems.

Computer and Electronic Product Manufacturing

The underlying problem is the uncertainty facing the business community today. Despite the fact that the recovery started a year ago, we don't see any evidence of its substance. The uncertainty of the tax status for the future makes both businesses and individuals unwilling to spend in the near term. Even if credit were easy, there is no demand to drive investment.

Miscellaneous Manufacturing

We have a long-term banking relationship with a strong financial sheet, so we have not seen any changes in our credit facility.