Texas Manufacturing Outlook Survey

FEDERAL RESERVE BANK OF DALLAS

June 27, 2011

Texas Manufacturing Activity Rises but at a Slower Pace

What's New This Month

For this month's survey, manufacturers were asked supplemental questions on issues facing their firms and changes in wage and benefits costs. See page 4 for results.

Texas factory activity expanded in June, according to business executives responding to the Texas Manufacturing Outlook Survey. The production index, a key measure of state manufacturing conditions, remained positive but fell from 12.7 to 5.6, suggesting output growth slowed this month.

Other measures of current manufacturing conditions indicated flat activity, while new orders picked up. The capacity utilization index slipped into negative territory but was near a reading of zero, suggesting little change over the prior month. Similarly, the shipments index fell to zero with about 60 percent of manufacturers noting no change in shipment volumes. The new orders index rose from 1.1 in May to 6.4 in June, its eighth consecutive month in positive territory. Nearly one-quarter of firms said order volumes increased from May levels. The growth rate of orders index turned positive after dipping into negative territory last month.

Perceptions of general business conditions were mixed in June. The general business activity index pushed further negative, falling from –7.4 to –17.5. Twenty-eight percent of respondents said activity weakened this month, the highest share in nine months. However, the company outlook index rose from 3.2 to 7.2, suggesting manufacturers were more optimistic about their firms' prospects for the near future. More than 85 percent of respondents said their outlooks were unchanged or improved from last month.

Labor market indicators reflected slower growth in labor demand. The employment index came in at 5.3, with 14 percent of manufacturers reporting hiring new workers compared with 9 percent reporting layoffs. The hours worked index fell to 1.5 in June, down from a reading of 13.2 in May.

Price and wage pressures moderated this month. The raw materials price index retreated from 42.3 to 31.1, suggesting input costs rose but at a slower pace than in May. The finished goods price index was largely unchanged at a reading of 10. More than 50 percent of respondents anticipate further increases in raw materials prices over the next six months, while 28 percent expect higher finished goods prices. The wages and benefits index moved down from 18.5 to 15.5, although the great majority of respondents noted no change in labor costs.

Expectations regarding future business conditions were less optimistic in June. The index of future general business activity was 2.9, its lowest reading since August 2010, and the index of future company outlook remained positive but fell to a 9-month low. Indexes of future manufacturing activity also fell in June, but remained in solid positive territory.

The Dallas Fed conducts the Texas Manufacturing Outlook Survey monthly to obtain a timely assessment of the state's factory activity. Data were collected June 14–22, and 84 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 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: July 25, 2011

Business Indicators Relating to Facilities and Products in Texas Current								
Indicator	Jun Index	May Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	5.6	12.7	-7.1	Increasing	20	23.9	57.8	18.3
Capacity Utilization	-0.8	11.1	-11.9	Decreasing	1	18.5	62.2	19.3
New Orders	6.4	1.1	+5.3	Increasing	8	24.3	57.8	17.9
Growth Rate of Orders	2.3	-5.4	+7.7	Increasing	1	23.1	56.1	20.8
Unfilled Orders	-6.2	-7.8	+1.6	Decreasing	4	12.6	68.6	18.8
Shipments	0.4	8.0	-7.6	Increasing	8	20.5	59.4	20.1
Delivery Time	1.2	0.0	+1.2	Increasing	1	10.7	79.8	9.5
Materials Inventories	6.5	-0.1	+6.6	Increasing	1	21.1	64.3	14.6
Finished Goods Inventories	0.0	-4.3	+4.3	Unchanged	1	14.3	71.4	14.3
Prices Paid for Raw Materials	31.1	42.3	-11.2	Increasing	23	36.1	58.9	5.0
Prices Received for Finished Goods	10.0	8.8	+1.2	Increasing	8	14.0	82.0	4.0
Wages and Benefits	15.5	18.5	-3.0	Increasing	19	16.7	82.1	1.2
Employment	5.3	11.6	-6.3	Increasing	8	14.3	76.7	9.0
Hours Worked	1.5	13.2	-11.7	Increasing	2	16.3	68.9	14.8
Capital Expenditures	2.4	8.7	-6.3	Increasing	8	7.2	88.0	4.8

General Business Conditions Current								
Indicator	Jun Index	May Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	7.2	3.2	+4.0	Improving	9	20.8	65.6	13.6
General Business Activity	-17.5	-7.4	-10.1	Worsening	2	10.1	62.3	27.6

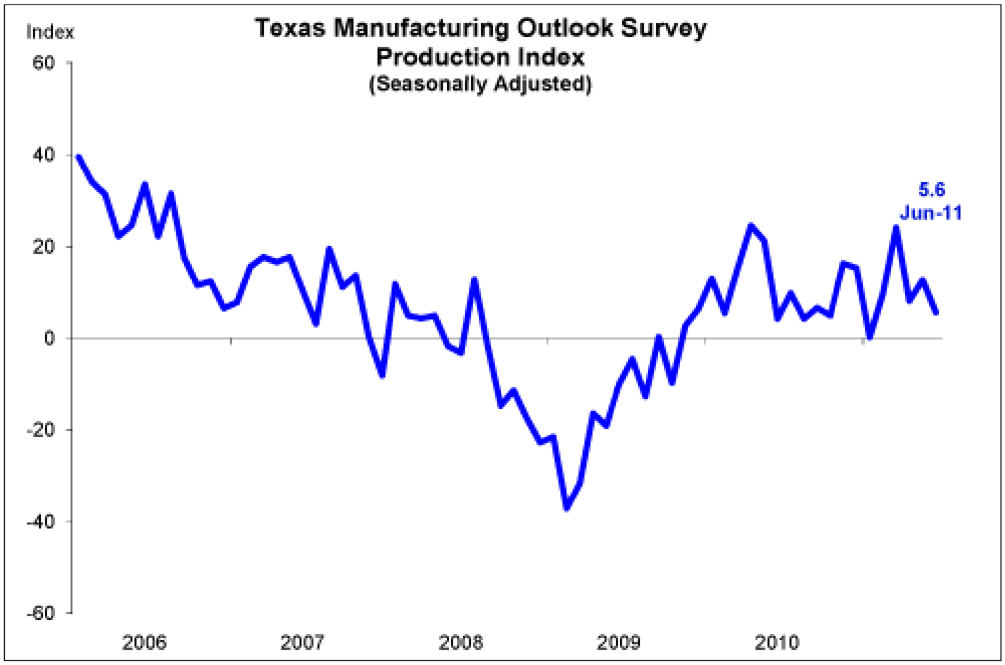
Business Indicators Relating to Facilities and Products in Texas Six Months Ahead								
Indicator	Jun Index	May Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	37.1	41.3	-4.2	Increasing	28	46.7	43.7	9.6
Capacity Utilization	27.4	43.5	-16.1	Increasing	28	38.3	50.8	10.9
New Orders	28.0	40.8	-12.8	Increasing	28	39.0	50.0	11.0
Growth Rate of Orders	22.1	27.7	-5.6	Increasing	28	30.5	61.1	8.4
Unfilled Orders	-7.3	15.4	-22.7	Decreasing	1	9.8	73.2	17.1
Shipments	35.1	43.7	-8.6	Increasing	28	46.4	42.3	11.3
Delivery Time	-6.1	2.2	-8.3	Decreasing	1	8.5	76.8	14.6
Materials Inventories	3.6	9.8	-6.2	Increasing	9	20.5	62.7	16.9
Finished Goods Inventories	2.4	-1.1	+3.5	Increasing	1	19.3	63.9	16.9
Prices Paid for Raw Materials	45.1	51.6	-6.5	Increasing	27	52.4	40.2	7.3
Prices Received for Finished Goods	22.2	25.0	-2.8	Increasing	11	28.4	65.4	6.2
Wages and Benefits	33.5	30.6	+2.9	Increasing	85	34.8	63.9	1.3
Employment	14.5	28.3	-13.8	Increasing	22	26.5	61.4	12.0
Hours Worked	7.3	10.9	-3.6	Increasing	28	15.7	75.9	8.4
Capital Expenditures	21.7	18.5	+3.2	Increasing	19	25.3	71.1	3.6

General Business Conditions Six Months Ahead								
Indicator	Jun Index	May Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	15.6	19.6	-4.0	Improving	25	30.1	55.4	14.5
General Business Activity	2.9	7.9	-5.0	Improving	10	21.5	59.9	18.6

*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.

Nonmetallic Mineral Product Manufacturing

We expect housing to remain sluggish for the next couple of years. This weakness will continue to impact our business levels. The current overhang in housing inventory needs to be absorbed before any significant expansion in building can occur. Our outlook is far from optimistic.

Primary Metal Manufacturing

Our business has been positively impacted by the bankruptcy of a competitor.

Fabricated Metal Product Manufacturing

Our expectation of improved business six months from now is not based on the general economy, but is based on some specific customers that we expect to increase their activity for reasons unique to them.

Machinery Manufacturing

We are seeing some modest improvement in our activity levels (maintenance and industrial services for downstream energy companies). Refining and petrochemical businesses are currently enjoying very strong margins. Overall economic activity still feels like it is slowing down to me—more of an attitude check than being based on specific data.

Chemical Manufacturing

The second and third quarters are normally our strongest quarters. So far, the second quarter has been weaker than we expected. We have seen some seasonal increase but not to the level we had anticipated.

Paper Manufacturing

Business has been stagnant the last few weeks and we aren't seeing any signs of improvement. We have not lost any business; our customers just aren't ordering as we expected for this time of year.

Food Manufacturing

Our sales are strong, but high commodity prices have really hurt us.

Questions regarding the Texas Manufacturing Outlook Survey can be addressed to Emily Kerr at emily.kerr@dal.frb.org.
The Texas Manufacturing Outlook Survey can be found online at www.dallasfed.org/data/outlook.

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SPECIAL QUESTIONS

1. To what extent do the following issues pose a problem for your firm?

	No problem (percent)	Relatively minor problem (percent)	Relatively major problem (percent)
Weak sales	25.0	28.9	46.1
Input costs	10.4	44.2	45.5
Supply chain disruptions	36.4	36.4	27.3
Labor costs - wages	33.8	50.6	15.6
Labor costs - benefits	16.9	48.1	35.1
Finding qualified workers	20.8	48.1	31.2
Government regulation	13.0	23.4	63.6
Business taxes	13.0	40.3	46.8
Availability or cost of credit	57.1	28.6	14.3
Uncertain business outlook	5.2	37.7	57.1

2. How do you estimate wage per employee will change during 2011 compared with 2010?

	Percent
Decrease	2.6
Stay at 2010 levels	23.4
Increase less than 2.5%	28.6
Increase 2.5% to 5%	44.2
Increase more than 5%	1.3

3. How do you estimate benefits per employee (employer contribution only) will change during 2011 compared with 2010?	
	Percent
Decrease	5.3
Stay at 2010 levels	21.1
Increase less than 2.5%	11.8
Increase 2.5% to 5%	25.0
Increase more than 5%	36.8

4. If wages or benefits costs are increasing, is the increase larger than you expected or budgeted for?	
	Percent
Yes	48.0
No	52.0

Survey collection period: 6/6/2011–6/9/2011

Special Questions Comments

These comments have been edited for publication.

Plastics and Rubber Products Manufacturing

We are still busy running at nearly 90 percent of capacity. We are not seeing much of a slowdown, but our customer base is located in North Texas/Dallas. Nationwide, it must be slower from what we read.

Located in Fort Worth, Texas, we are a nationwide supplier of manufactured products to the housing industry. We are concerned that the beginning of the recovery period may be 18 to 24 months out unless something is done to absorb the current inventory of single-family homes on the market and to stimulate new single-family home construction. We do not see any increase for our business sales during the remainder of 2011.

Employer-provided health insurance costs continue to be a problem. These costs must be dealt with. Income taxes for the small business are not an issue.

Nonmetallic Mineral Product Manufacturing

The most significant issue appears to be government regulation and policy. Also, the current housing crisis has resulted in weak demand for our products, which in turn limits our ability to increase selling prices in the face of rising costs. There is upward pressure on commodity prices in both the metals and energy markets. This affects our primary inputs, i.e., aluminum and PVC. Higher energy costs have significantly impacted both outbound and inbound freight costs as well as caused energy surcharges on virtually all material inputs, including office supplies. Government regulation regarding energy efficiency has helped drive costs up in product development and product costs at a point in time when there is no pricing leverage due to the weak demand. This has resulted in margin compression. Wages have been frozen now for three years, and benefits programs have been modified in an effort to limit cost increases.

Fabricated Metal Product Manufacturing

Raw material costs have seemed to stabilize over the last few weeks, meaning that we believe prices are not continuing to rise. There seems to be uncertainty in most of the industries that we build products for. Our company has created an apprenticeship program for recruiting and training unskilled workers into skilled workers to operate specialized equipment. This program seems to be working very well for us. So far, we're on our second group of workers and have only had one in 10 drop out of the program. We are feeling wage pressures internally;

everyone is talking about it, but no one is leaving the company. We believe that gas prices had a lot to do with these pressures. Health benefits are out of control. Every year we tweak our health insurance program to avoid the systematic year-over-year escalation of our health insurance premiums.

Our biggest hiring challenge is finding machinists who truly are qualified and have a good work ethic. Secondary to that is finding qualified electronic maintenance technicians. We are not having any problem with entry-level labor.

The uncertainty of the economy is what is really hurting us today. Our customers do not know what to do, and we cannot tell our suppliers what is going to happen.

The great number of new and pending regulations (EPA, NLRB, Dodd–Frank, health care) is weighing heavily on businesses. The impact of talk about raising taxes lands very negatively on small businesses, including Subchapter S.

Machinery Manufacturing

We are in the farm machinery manufacturing business. The drought, which is primarily in West Texas but is also affecting other parts of the south and western U.S., will begin hurting our business in the next few weeks.

We are budgeting 3 percent merit increases this fiscal year, up from 2 percent last year and zero percent two years ago. We plan to restore our 401(k) match this year. Due to the weak general economy, the state unemployment taxes are dramatically higher this year in many states (both rate and salary cutoff level).

Computer and Electronic Product Manufacturing

Input costs are a major problem for us, as freight costs and commodity costs are increasing. Labor costs are also a major problem with regard to doing business in the U.S. High costs force us to move more work overseas. Business income tax is a major problem as well. It forces us to do more business outside the U.S.

Furniture and Related Product Manufacturing

The lack of sales is our largest problem, compounded by uncertainty. Rising material costs and taxes affect our competitiveness in some areas.

Food Manufacturing

High prices for diesel and commodities are really hurting us. Additionally, the high price of gas is hard on our employees.