Texas Manufacturing Outlook Survey

FEDERAL RESERVE BANK OF DALLAS

March 26, 2012

TEXAS MANUFACTURING EXPANSION CONTINUES

WHAT'S NEW THIS MONTH

For this month's survey, manufacturers were asked supplemental questions on hiring plans. More than half of respondents expect their firm to increase employment over the next six to twelve months.

Texas factory activity continued to increase in March, according to business executives responding to the Texas Manufacturing Outlook Survey. The production index, a key measure of state manufacturing conditions, held steady at 11.1, suggesting growth continued at about the same pace as last month.

Most other measures of current manufacturing conditions also indicated continued expansion in March, although new orders stagnated. The shipments index rose from 4.2 to 8.6, with more than a quarter of manufacturers noting an increase in shipment volumes. Capacity utilization increased further in March; the index edged up from 10 to 12.3. The new orders index meanwhile fell from 5.8 in February to zero this month, suggesting demand stalled.

Perceptions of broader economic conditions remained positive in March. The general business activity index was positive for the third month in a row, although it fell from 17.8 to 10.8. Twenty-three percent of firms noted improvement in the level of business activity, while 12 percent noted a worsening. The company outlook index posted a sixth consecutive positive reading, but it also retreated slightly, falling to 9.5 from 15.8 last month.

Labor market indicators reflected higher labor demand. Strong employment growth continued in March, although the index edged down from 25.2 to 21.7. Twenty-nine percent of firms reported hiring new workers, while 7 percent reported layoffs. The hours worked index continued to suggest average workweeks lengthened.

Input prices and wages continued to increase in March, while selling prices reversed course and declined slightly. The raw materials price index was 27.7, marginally higher than in February. The March wages and benefits index edged up to 21, its highest reading since mid-2008. In contrast, the finished goods price index dropped to -1.3 in March after two months of sharp increases. The lower index was largely due to a marked decline in the share of manufacturers noting price increases. Looking ahead, 57 percent of respondents anticipate further increases in raw materials prices over the next six months, while 35 percent expect higher finished goods prices.

Expectations regarding future business conditions were more optimistic in March. The index of future general business activity has been positive for six months and rose from 15.9 to 19.1 this month. The index of future company outlook came in at 26.2, up slightly from 24.2 in February. Other indexes for future manufacturing activity also increased.

The Dallas Fed conducts the Texas Manufacturing Outlook Survey monthly to obtain a timely assessment of the state's factory activity. Data were collected Mar. 13–21, and 88 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: April 30, 2012

Business Indicators Relating to Facilities and Products in Texas
Current

Indicator	Mar Index	Feb Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	11.1	11.2	-0.1	Increasing	4	25.7	59.7	14.6
Capacity Utilization	12.3	10.0	+2.3	Increasing	4	25.6	61.1	13.3
New Orders	-0.3	5.8	-6.1	Decreasing	1	21.2	57.3	21.5
Growth Rate of Orders	-0.8	6.6	-7.4	Decreasing	1	18.8	61.6	19.6
Unfilled Orders	0.3	-12.7	+13.0	Increasing	1	16.0	68.3	15.7
Shipments	8.6	4.2	+4.4	Increasing	3	26.2	56.2	17.6
Delivery Time	6.8	3.6	+3.2	Increasing	3	12.5	81.8	5.7
Materials Inventories	-0.3	2.0	-2.3	Decreasing	1	17.6	64.5	17.9
Finished Goods Inventories	-8.0	-5.8	-2.2	Decreasing	2	13.6	64.8	21.6
Prices Paid for Raw Materials	27.7	25.2	+2.5	Increasing	32	31.6	64.5	3.9
Prices Received for Finished Goods	-1.3	16.2	-17.5	Decreasing	1	6.7	85.3	8.0
Wages and Benefits	21.0	18.4	+2.6	Increasing	28	22.0	77.0	1.0
Employment	21.7	25.2	-3.5	Increasing	17	29.0	63.7	7.3
Hours Worked	2.9	7.1	-4.2	Increasing	7	13.5	75.9	10.6
Capital Expenditures	6.3	12.1	-5.8	Increasing	6	14.5	77.3	8.2

General Business Conditions
Current

Indicator	Mar Index	Feb Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	9.5	15.8	-6.3	Improving	6	22.8	63.9	13.3
General Business Activity	10.8	17.8	-7.0	Improving	3	23.0	64.8	12.2

Business Indicators Relating to Facilities and Products in Texas
Six Months Ahead

Indicator	Mar Index	Feb Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Production	44.0	40.8	+3.2	Increasing	37	48.9	46.2	4.9
Capacity Utilization	41.8	39.1	+2.7	Increasing	37	47.5	46.7	5.7
New Orders	44.0	37.0	+7.0	Increasing	37	50.4	43.2	6.4
Growth Rate of Orders	37.2	32.1	+5.1	Increasing	37	41.6	54.0	4.4
Unfilled Orders	15.1	10.9	+4.2	Increasing	9	22.1	70.9	7.0
Shipments	42.8	42.8	0.0	Increasing	37	48.8	45.2	6.0
Delivery Time	1.2	-1.2	+2.4	Increasing	1	7.0	87.2	5.8
Materials Inventories	11.8	3.7	+8.1	Increasing	5	22.4	67.1	10.6
Finished Goods Inventories	7.0	1.3	+5.7	Increasing	3	16.3	74.4	9.3
Prices Paid for Raw Materials	55.8	45.8	+10.0	Increasing	36	57.0	41.9	1.2
Prices Received for Finished Goods	29.1	22.9	+6.2	Increasing	20	34.9	59.3	5.8
Wages and Benefits	40.3	39.9	+0.4	Increasing	94	40.3	59.7	0.0
Employment	36.9	32.9	+4.0	Increasing	31	40.5	56.0	3.6
Hours Worked	9.6	10.0	-0.4	Increasing	36	17.6	74.4	8.0
Capital Expenditures	25.6	30.5	-4.9	Increasing	28	32.6	60.5	7.0

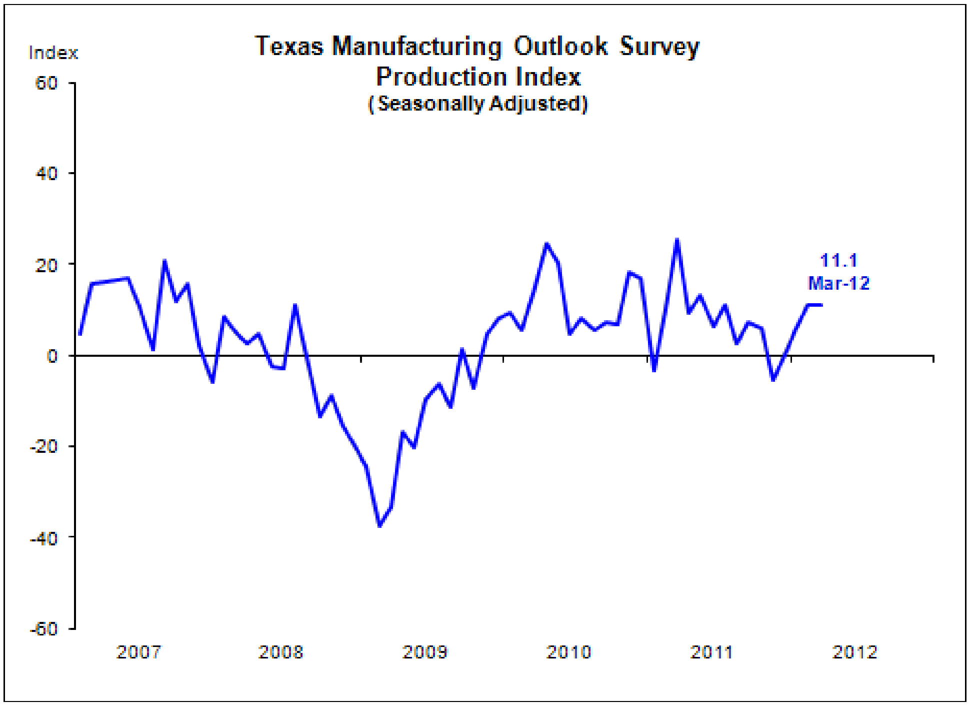
General Business Conditions
Six Months Ahead

Indicator	Mar Index	Feb Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company Outlook	26.2	24.2	+2.0	Improving	35	34.6	57.0	8.4
General Business Activity	19.1	15.9	+3.2	Improving	6	27.6	63.9	8.5

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

Fabricated Metal Product Manufacturing

We have seen a modest improvement in our overall nonresidential markets, led by industrial manufacturing and energy-related projects.

In general, people feel more secure. Manufacturing opportunities continue to improve for U.S. companies. Challenges in finding skilled workers, high employment taxes and medical insurance affect competitiveness and limit small- to mid-size company growth.

Pricing for new work remains very competitive, with little or less margin on newly awarded contracts. Requests for quotations are still plentiful, indicating increased activity. However, some desired work is being awarded to competitors at amounts below profitable levels for our company. We are experiencing difficulty adding new workers at all skill levels.

Machinery Manufacturing

Demand in our line of business (maintenance services for downstream/midstream energy facilities) remains fairly strong. We expect active turnaround seasons both this spring and next fall. Regarding the general economy, we are confused by conflicting data. The employment data look good, but how is that sustainable with low GDP growth? We are maintaining a cautious overall market outlook.

Higher gasoline and diesel prices will increase cost of service crews, salesmen travel and freight of raw material and finished goods. These fuel costs will reduce profits. Higher gas prices effectively reduce all of our associates' take-home pay. This is not good for associates' spirits and morale when they are working more and seeing less disposable income.

The agricultural machinery business is very good. We are currently increasing our manufacturing capacity to try to meet demand.

Business activity continues to grow slowly; however, rising gas prices may again stall retail spending.

Chemical Manufacturing

We feel like the level of business activity, which appeared to be picking up in the latter half of 2011, is softening some and has lost momentum. It could be that higher oil prices are tempering enthusiasm and clouding the future outlook.

If our customers are correct, we are in for a very strong year.

Plastics and Rubber Products Manufacturing

We are encouraged by the number of companies who are bringing molding back from China to the U.S. There appears to be a growing desire to have more products manufactured in the U.S.

Nonmetallic Mineral Product Manufacturing

We are seeing some modest improvement in business levels, which appear to be seasonal in nature. Mild weather conditions appear to have helped business levels in both February and early March. We are guarded in our expectations, although we are more positive than in recent months. Concern for the impact of oil prices on raw material and delivery costs weighs on our margin expectations, as demand has not improved enough to provide any pricing leverage.

Computer and Electronic Product Manufacturing

The first quarter of 2012 has been disappointing relative to volume of new orders. Our outlook for the third quarter and beyond appears to be a bit brighter.

Food Manufacturing

A very short supply of cattle is limiting our supply.

The cost of diesel shows up in everything we buy.

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

Sign up for our free e-mail alert to be automatically notified as soon as the latest Texas Manufacturing Outlook Survey is released on the web.

The Texas Manufacturing Outlook Survey can be found online at www.dallasfed.org/microsites/research/surveys/tmos/.

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FEDERAL RESERVE BANK OF DALLAS

March 26, 2012

Special Questions

1. Do you expect your firm to increase employment, leave employment unchanged, or decrease employment over the next six to twelve months?

	Mar. '12 (percent)	Jan. '11 (percent)
Increase	56.3	47.7
Leave Unchanged	37.5	41.9
Decrease	6.3	10.5

2. If your firm is planning to increase employment, what are the three most important factors behind this decision? Please rank the three factors in order from most important to third most important.

	Most important (percent)	Second most important (percent)	Third most important (percent)
Expected growth of sales or revenue is high	71.1	19.5	10.8
Current staff are overworked	11.1	34.1	24.3
Need skills not possessed by current staff	11.1	19.5	35.1
Labor costs have fallen	0.0	0.0	2.7
Decreased economic or financial uncertainity	2.2	12.2	13.5
Firm's financial position has improved	2.2	9.8	5.4
Other factors	2.2	4.9	8.1

3. What are the three most important factors, if any, restraining your hiring plans? Please rank the three factors in order from most important to third most important.

	Most important (percent)	Second most important (percent)	Third most important (percent)
Expected growth of sales or revenue is low	31.7	12.3	5.6
Current staff are underutilized/working reduced hours	6.7	17.5	1.9
Cannot find qualified workers	16.7	7.0	14.8
Labor costs are high	8.3	10.5	7.4
Uncertainity about the cost of health insurance	13.3	12.3	22.2
Uncertainity about other regulations or gov't policies	11.7	36.8	24.1
Firm's financial position has deteriorated	0.0	1.8	14.8
Other factors	11.7	1.8	9.3

Survey Collection period: 03/06/2012–03/09/2012

Special Questions Comments

These comments have been edited for publication.

Paper Manufacturing

We are not seeing enough people applying for our open positions, and most are not qualified. We have talked to others in our industry; they too are not seeing enough qualified applicants to fill open positions. We wonder if extended unemployment benefits are a contributing factor.

Wood Product Manufacturing

Our revenues are directly related to home building and the resultant commercial building. There is still too much supply chasing too little demand in these economic segments. Therefore, both margins and sales volumes are constrained.

Chemical Manufacturing

We have maintained jobs for more people than we needed over the past couple of years because we didn't want to lose good, trained employees. We still have excess capacity.

Plastics and Rubber Product Manufacturing

Last year was our first good sales/profit year in the past three years. We did not cut our employment during the slow years and have supplemented our production workforce with temporary workers in the moderate- to low-skill level. Temporary workers are great in our business where there are some seasonal fluctuations and economy slowdowns from time to time. We did add three skilled position employees last year and will keep them in our workforce.

Our hiring is based strictly on economics. Sales increases at current prices require more workers. If we choose to increase investments in additional product lines at profitable margins, we will hire more people, regardless of government regulations or policies. Cost of government regulations and policies will be included in the costs used to determine margins and pricing.

We have had openings for skilled workers (toolmakers, robotics technicians, etc.) for over a year and cannot fill the positions.

We continue to find sources for labor outside of the U.S. Our business is growing; however, our headcount is not. The labor climate in the U.S. is not really conducive to continued hiring for us. We are somewhat unique in that we do not require skilled workers, and as such, we find few people who are willing to perform this unskilled work.

Nonmetallic Mineral Product Manufacturing

Economic uncertainty will continue through the election, which will limit improvement in consumer confidence. Too many risks associated with new regulations and onerous governmental policies will keep hiring low, which in turn will limit job growth and wealth creation, which will then limit improvement in consumer spending. The business community needs longer-term stability in the rules before it can make prudent economic investments.

We are in the building materials supply business, and we anticipate the amount of new home construction to increase. Our employment levels are in direct correlation to home building activity. With increasing home building activity comes our expectation of increased employment and therefore our expectations for increased sales or revenue growth. The introduction of a new product line will lead to increased market share for our company. That said, we will not hire unless absolutely necessary. We have made significant investment in automated equipment to reduce the need for hiring. We have moved jobs offshore so that we do not have to deal with the quickly increasing health care mandates and costs. It will soon be too expensive to do business in our industry with lots of employees.

Instability in the current economic environment continues to have a negative impact on consumer confidence, which is holding back the housing segment of the economy. This instability is being caused primarily by government regulations and policies, as well as certain world events. We are cautiously optimistic that the recovery will continue, albeit at a slow rate of growth.

Fabricated Metal Product Manufacturing

We are bidding a large increase of potential orders. However, they are taking a long time to award since most potential orders are with public entities, which remain very concerned over funding issues.

The overall nonresidential markets we serve are expected to only grow by 2 percent in volume this year, off the lowest levels for new construction starts in 50 years. In fact, for the first three months of our fiscal first quarter ending in January, market volume was down on a year-over-year basis by 5.4 percent. The policies being pursued by federal agencies, healthcare costs and tax uncertainties do most certainly affect our willingness to take risk by investing in growth more aggressively. Therefore, growth is held back and hiring is restrained.

Machinery Manufacturing

We still have great concerns about mandated health coverage and its related increased medical costs. Also, we have great reluctance to hire new people because of the seemingly endless federal government rules. The city of Houston’s deficit spending along with the city’s very large unfunded pension liabilities will likely cause local tax increases and more fees and permits. Also, there still is no federal government budget and no plan to decrease huge federal deficits. We fear further monetary problems in Europe and the U.S.

Employment can only come with additional revenue. With our current customers as a group and the general marketplace experiencing very little growth, our growth must come from taking customers from our competition.

Finding qualified employees with good work habits (come to work every day on time, for example) is the biggest problem we face on a day-to-day basis.

We balance human resources with business activity levels. Our outlook is positive.

While some moments are extremely positive, others are a little more precarious. The price of gas and cost of goods sold make us fearful of hiring.

Transportation Equipment Manufacturing

We are hiring now to meet immediate demand due to increased business, but we are exercising prudent restraint due to uncertainty beyond the next 12 months.

Food Manufacturing

While we see strong growth and ample sources of potential employees, we are investing in technology to equip our plant for the increased volume while keeping our labor force steady. This will mitigate any uncertainty regarding regulations and increased health insurance costs.

The high prices of gas and diesel hurt us, our customers and our employees. It acts as a drag on the entire economy.