Texas Service Sector Outlook Survey

FEDERAL RESERVE BANK OF DALLAS

November 1, 2011

Texas Service Sector Activity Expands but at a Slower Pace

What's New This Month

For this month's survey, business executives were asked supplemental questions on borrowing conditions and credit availability. See page 7 for results.

Texas service sector activity increased in October, according to business executives responding to the Texas Service Sector Outlook Survey. The revenue index, a key measure of state service sector conditions, fell from 14.1 to 4.7, which is indicative of slower revenue growth.

Labor market indicators reflect more hiring and longer workweeks. The employment index edged up to 4.7, its best reading in six months, although two-thirds of respondents noted no change in employment. The hours worked index rose from 0.9 to 5.2 in October, which is consistent with longer workweeks.

Perceptions of general business conditions were mixed in October. The general business activity index remained negative for the sixth month in a row, but the pace of deterioration slowed, with the index advancing from –10 in September to –5.1 in October. The company outlook index moved back into positive territory after two months of negative readings, rising from –0.4 to 5.7, with 19 percent of respondents reporting their outlooks improved from last month.

Price and wage pressures were not much changed in October. The selling prices index came in at 6.3, about the same as its September reading of 6.5. The wages and benefits index edged up from 10 to 12.1, although the great majority of respondents noted no change in labor costs.

Indexes of future service sector activity improved across the board, and expectations regarding future business conditions were more optimistic. The index of future general business activity moved into positive territory in October after posting two consecutive negative readings and the index of future company outlook advanced from 6.5 to 16.9.

Retail Sales Growth Slows

Retail sales increased in October, according to business executives responding to the Texas Retail Outlook Survey. The volatile sales index fell from 18.6 to 9.2, which is indicative of slower sales growth. Inventories rose for the fourth month in a row.

Labor market indicators reflected more hiring and slightly longer workweeks. The employment index jumped up from 5.1 to 16, with 28 percent of respondents noting employment increased from September. The hours worked index came in at 1.6, after posting a negative reading last month.

Perceptions of general business conditions improved in October. The general business activity index came in at 0.8 after posting six consecutive negative readings. The company outlook index surged to 16.9, its best showing in seven months. A quarter of respondents said their company's outlook had improved from the prior month, compared with 8 percent who noted their outlook had worsened.

Retail prices and wages continued to climb in October. The selling prices index rose from 13.6 to 19.9. The wages and benefits index moved up from 7.8 to 15.6, although the great majority of respondents continued to note no change in labor costs.

Indexes of future retail sector activity moved further into positive territory in October. Future expectations regarding broader economic activity also improved markedly.

The Texas Retail Outlook Survey (TROS) is a component of the TSSOS that uses information only from respondents in the retail and wholesale sectors.

The Dallas Fed conducts the Texas Service Sector Outlook Survey monthly to obtain a timely assessment of the state's service sector activity. Data were collected October 18–26, and 222 Texas business executives responded to the survey. Firms are asked whether revenue, employment, prices, general business activity 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: November 29, 2011

Texas Service Sector Outlook Survey

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
Revenue	4.7	14.1	-9.4	Increasing	24	25.2	54.3	20.5
Employment	4.7	4.4	+0.3	Increasing	20	18.8	67.1	14.1
Part-time employment	0.5	0.4	+0.1	Increasing	2	9.2	82.1	8.7
Hours worked	5.2	0.9	+4.3	Increasing	8	11.7	81.8	6.5
Wages and benefits	12.1	10.0	+2.1	Increasing	25	15.5	81.1	3.4
Input prices	29.2	30.2	-1.0	Increasing	30	32.8	63.6	3.6
Selling prices	6.3	6.5	-0.2	Increasing	10	17.3	71.7	11.0
Capital expenditures	12.4	9.6	+2.8	Increasing	26	21.0	70.3	8.6
General Business Conditions Current								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company outlook	5.7	-0.4	+6.1	Improving	1	18.6	68.5	12.9
General business activity	-5.1	-10.0	+4.9	Worsening	6	14.1	66.7	19.2
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
Revenue	36.5	27.9	+8.6	Increasing	32	49.6	37.4	13.1
Employment	21.4	14.3	+7.1	Increasing	31	33.6	54.2	12.2
Part-time employment	11.2	0.7	+10.5	Increasing	4	15.6	80.0	4.4
Hours worked	3.6	1.2	+2.4	Increasing	26	9.4	84.8	5.8
Wages and benefits	30.2	27.5	+2.7	Increasing	58	33.7	62.8	3.5
Input prices	45.8	43.2	+2.6	Increasing	58	50.4	45.0	4.6
Selling prices	25.3	19.9	+5.4	Increasing	27	33.3	58.7	8.0
Capital expenditures	17.9	15.5	+2.4	Increasing	31	28.6	60.7	10.7
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	16.9	6.5	+10.4	Improving	2	28.7	59.5	11.8
General business activity	6.0	-3.2	+9.2	Improving	1	22.4	61.2	16.4

*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.

TEXAS RETAIL OUTLOOK SURVEY

Business Indicators Relating to Facilities and Products, Retail Current								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Retail Activity in Texas								
Sales	9.2	18.6	-9.4	Increasing	3	29.4	50.4	20.2
Employment	16.0	5.1	+10.9	Increasing	3	27.6	60.8	11.6
Part-time employment	-1.6	-1.6	0.0	Decreasing	3	8.1	82.3	9.7
Hours worked	1.6	-7.8	+9.4	Increasing	1	12.5	76.6	10.9
Wages and benefits	15.6	7.8	+7.8	Increasing	8	17.2	81.3	1.6
Input prices	30.0	36.2	-6.2	Increasing	15	37.2	55.6	7.2
Selling prices	19.9	13.6	+6.3	Increasing	15	28.0	63.9	8.1
Capital expenditures	17.2	3.1	+14.1	Increasing	7	25.0	67.2	7.8
Inventories	12.9	9.7	+3.2	Increasing	4	26.0	60.9	13.1
Companywide Retail Activity								
Sales	9.9	13.1	-3.2	Increasing	5	30.7	48.5	20.8
Internet sales	2.4	2.1	+0.3	Increasing	4	14.3	73.8	11.9
Catalog sales	-2.6	-5.0	+2.4	Decreasing	2	7.9	81.6	10.5

General Business Conditions, Retail Current								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company outlook	16.9	8.8	+8.1	Improving	2	25.2	66.5	8.3
General business activity	0.8	-9.6	+10.4	Improving	1	20.3	60.2	19.5

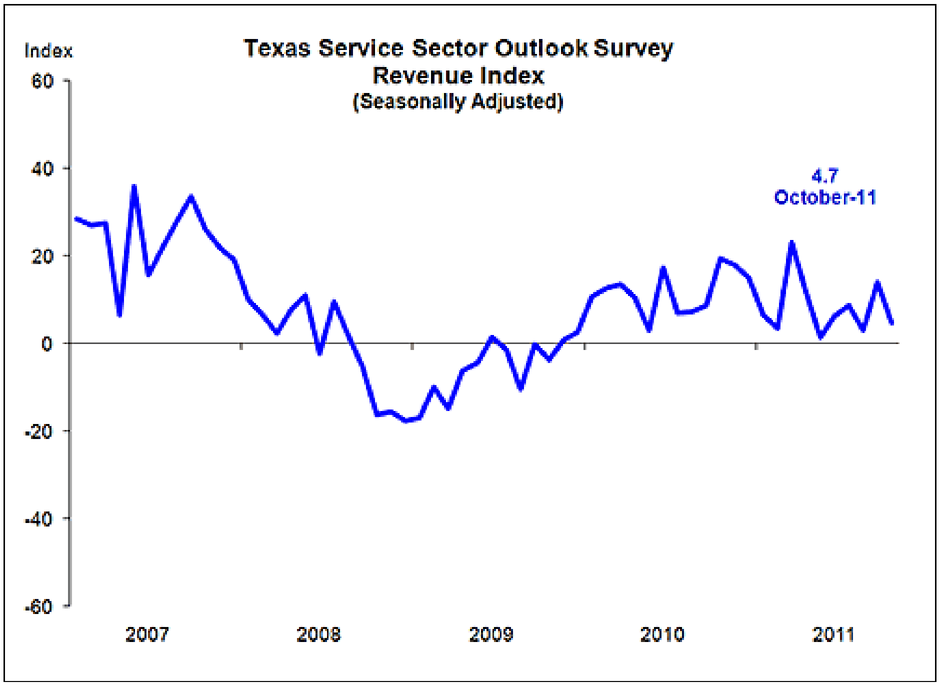
Business Indicators Relating to Facilities and Products, Retail Six Months Ahead								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Increase	% Reporting No Change	% Reporting Decrease
Retail Activity in Texas								
Sales	46.7	23.9	+22.8	Increasing	32	52.2	42.3	5.5
Employment	15.9	12.9	+3.0	Increasing	22	28.6	58.7	12.7
Part-time employment	17.7	-13.3	+31.0	Increasing	1	23.6	70.5	5.9
Hours worked	0.6	-0.4	+1.0	Increasing	1	14.6	71.4	14.0
Wages and benefits	24.6	15.5	+9.1	Increasing	34	28.3	68.0	3.7
Input prices	39.6	38.7	+0.9	Increasing	30	44.4	50.8	4.8
Selling prices	34.9	25.8	+9.1	Increasing	30	39.7	55.6	4.8
Capital expenditures	25.4	3.3	+22.1	Increasing	7	33.3	58.7	7.9
Inventories	6.3	0.0	+6.3	Increasing	1	20.6	65.1	14.3
Companywide Retail Activity								
Sales	47.0	31.4	+15.6	Increasing	31	51.5	44.0	4.5
Internet sales	28.2	21.0	+7.2	Increasing	31	33.3	61.5	5.1
Catalog sales	11.7	5.7	+6.0	Increasing	3	17.6	76.5	5.9

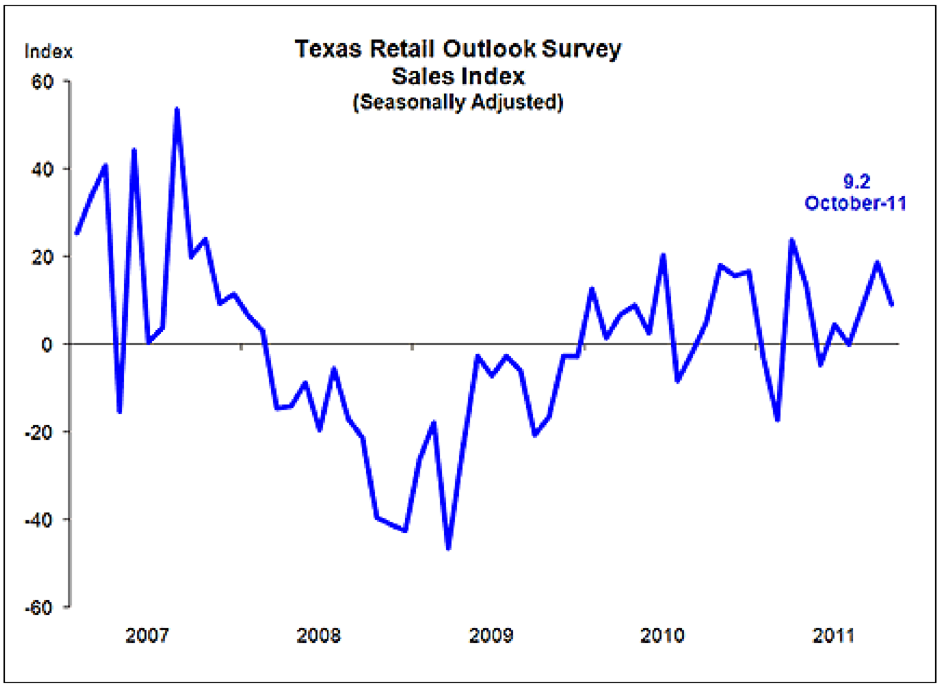
General Business Conditions, Retail Six Months Ahead								
Indicator	Oct Index	Sep Index	Change	Indicator Direction*	Trend** (months)	% Reporting Improved	% Reporting No Change	% Reporting Worsened
Company outlook	28.7	15.1	+13.6	Improving	30	32.4	63.9	3.7
General business activity	11.1	-4.5	+15.6	Improving	1	23.7	63.7	12.6

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

Accommodation

Capital expenditures will increase over the next six months as we are putting in a new RV park and adding 20 to 30 rooms in one of our hotels.

Credit Intermediation and Related Activities

We see light loan demand and a stagnant real estate market, but some recovery of previously charged-off loans. We have been successful in acquiring tenants in previously unoccupied foreclosed real estate properties.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

Retail sales are strong even though drought is hurting agribusiness. Farmer income should be down 30 percent from last year. Concern is growing about 2012 if the drought continues.

We are still fighting cost increases in health insurance, raw materials, property and personal property taxes and the costs to comply with federal and local regulations. It's a tough and unsure environment in which to work.

We are a multifaceted financial services firm. Our insurance business for wholesale and retail space is relatively stable and has seen a small growth. Our residential mortgage business—which provides no subprime loans and deals only with clients with credit scores that exceed 700— is exploding right now. About 30 percent is refinancing, and the rest are new loans. Our real estate development company is almost exclusively in multifamily housing development and doing very well; our average occupancy rate is 97 percent. Our automobile dealerships are also doing very well.

Real Estate

We are not expecting a restoration of certainty to the market until after the 2012 elections. Our confidence will remain low due to uncertainty relative to fiscal and taxing policies.

Professional, Scientific and Technical Services

Any projected improvement is slight. There is still not much optimism in client projections and plans. We anticipate a slight overall salary increase in 2012. We haven't had an across-the-board increase since 2007.

The phone has stopped ringing. The same thing happened in October 2008 when we first went into a slump. People quit buying.

Lack of congressional leadership and direction, along with a fragile uncertain economy, continue to hinder chances of a meaningful recovery in the real estate and building industries.

Some markets are softening due to overall general economic weakness, but activity in the oil and gas shale is growing.

This year has been surprising. Each month we brace for a downturn, and it does not materialize. The activity level, however, is constant, with residential transactions slightly behind last year but better than 2009 and reasonably profitable. Commercial real estate activity is a pleasant surprise with a substantial increase, pushing profitability year to date to a significant increase as well. All of this has been accomplished with fewer employees year to date (no layoffs, just attrition with limited replacement), but we do not have any plans to expand or hire in the coming year. We have also seen an increase in residential refinancing title orders this month as interest rates moved upward slightly, bringing out the waiters to catch the low rates. We don't know if we are poised on the edge of an upturn or a downturn, so we remain cautious to see which way the economy goes.

We really need the tight regulations on banks—especially smaller banks—to be appropriately modified to encourage them to lend on solid deals so we can get some economic activity.

Management of Companies and Enterprises

Federal regulatory burden continues to be the overriding factor that has restricted our company's ability to expand services and employment. We think this is being replicated throughout the business environment across the country.

Administrative and Support Services

Though we have seen an increase in revenue, demand is flat. We are just executing better.

Ambulatory Health Care Services

The uncertainty of the healthcare regulatory reforms continues to be a factor in expenditures. Increasing regulation from the federal government has continued to consume more staffing hours to respond.

Food Services and Drinking Places

Nothing has changed so far into October from September, but that is not particularly good news since our sales softened a couple of months ago and are still very soft. We are up 1 percent over last year on a same-store basis, but we have taken 2 percent in price increases so we are actually down. The costs of goods have moved up so much over the last half year that we have finally given up trying to absorb them and will be taking a price increase —right now estimated to be 1 percent—by mid-November. The increase will not be sufficient to restore our margins completely. We do not feel the market will support the size of increase we actually need to take. We expect a serious increase in the cost of benefits—particularly health insurance—in January. We still hope to see some improvement in the economy in the holiday season—hence the optimistic six-month outlook.

Merchant Wholesalers, Durable Goods

We are investing in technology to increase service levels to our customers. A byproduct of that will likely be further headcount reduction. We just got our health care renewal, which increased 21 percent over last year. We wonder how many employees will be able to afford it and hope we will not lose too many folks because of it.

We are moving forward. We see opportunity and are laying the ground work. Construction of multifamily and single-family homes is improving. Commercial construction is weakening, but bodes well going forward.

Typically, the glass industry sees a spike in business six to 12 months after projects are initiated by the construction industry. However, the unique positive outlook for our company is due to bankruptcies by two of our three main competitors. In our opinion, the construction industry remains short on capital and is still stagnated by a lack of funds for nongovernmental projects that the smaller “storefront business” owners will participate in; these are the businesses that will jump-start jobs to the nation's unemployed.

We suddenly in October have dropped 12 percent across all operations. This would indicate a broad-based slowdown in construction activity. It’s too early to tell if the decline will continue, but it’s certainly something to watch. Otherwise, we are fairly optimistic going into the winter and spring 2012 that business conditions may be better than they were in 2011.

Building Material and Garden Equipment and Supplies Dealers

On the positive side, demand is supporting slightly higher prices. On the negative side, demand is inconsistent. There are several months of good quotes and sales followed by several months of lackluster demand. The result of this misfiring economy is that we are reluctant to start rebuilding our employee base.

Business is still slower than it should be, putting pressure on margins. We'll continue to work hard and make the adjustments necessary to keep things going. It’s not much fun for owners or employees these days.

Motor Vehicle and Parts Dealers

We think that the low interest rates have not been passed to the final users—Main Street businesses or individuals.

Hesitancy to buy is still there. Basically the word tepid describes our business and reflects the attitude of our major customers.

The auto business remains stable with the pipeline back to normal for Japanese-supplied franchises. Unfortunately, good manufacturer incentives and marketing programs are offset by continuing political turmoil and malaise in the economy overall.

Questions regarding the Texas Service Sector Outlook Survey can be addressed to Jesus Cañas at jesus.canas@dal.frb.org.

The Texas Service Sector Outlook Survey can be found online at www.dallasfed.org/research/surveys/tssos.

November 1, 2011

Special Questions

Texas Service Sector Outlook Survey

1. How do borrowing conditions facing your firm compare to those six months ago?

	Oct '10 (percent)	Oct '11 (percent)
Eased substantially	1.9	1.9
Eased somewhat	17.5	11.4
No change	36.3	32.9
Tightened somewhat	12.5	14.6
Tightened substantially	4.4	8.9
Not applicable—haven't sought credit	27.5	30.4

2. To what extent is your business having difficulty obtaining financing for desired long-term uses such as capital expenditures?

	Oct '10 (percent)	Oct '11 (percent)
No difficulty	30.6	32.5
Some difficulty	18.8	21.7
Substantial difficulty	8.1	5.7
Extreme difficulty	3.1	3.8
Not applicable—haven't sought credit	39.4	36.3

3. To what extent is your business having difficulty obtaining financing for desired short-term uses such as paying workers and acquiring inventories of material or supplies?

	Oct '10 (percent)	Oct '11 (percent)
No difficulty	35.8	37.3
Some difficulty	11.9	9.5
Substantial difficulty	3.8	3.2
Extreme difficulty	2.5	2.5
Not applicable—haven't sought credit	45.9	47.5

4. Has your firm's production and/or sales been adversely affected by difficulty obtaining credit?		
	Oct '10 (percent)	Oct '11 (percent)
Yes, significantly	6.9	5.1
Yes, somewhat	14.5	14.6
No	36.5	38.2
Not applicable—haven't had problems obtaining credit	10.1	8.3
Not applicable—haven't sought credit	32.1	34.4

5. Has your firm reduced hiring and/or increased layoffs due to difficulty obtaining credit?		
	Oct '10 (percent)	Oct '11 (percent)
Yes, significantly	3.8	3.2
Yes, somewhat	8.8	14.0
No	46.9	40.1
Not applicable—haven't had problems obtaining credit	8.8	8.9
Not applicable—haven't sought credit	31.9	34.4

Texas Retail Outlook Survey

1. How do borrowing conditions facing your firm compare to those six months ago?		
	Oct '10 (percent)	Oct '11 (percent)
Eased substantially	1.9	2.2
Eased somewhat	19.2	17.4
No change	38.5	30.4
Tightened somewhat	11.5	19.6
Tightened substantially	3.8	4.3
Not applicable—haven't sought credit	25.0	26.1

2. To what extent is your business having difficulty obtaining financing for desired long-term uses such as capital expenditures?		
	Oct '10 (percent)	Oct '11 (percent)
No difficulty	34.6	37.0
Some difficulty	15.4	28.3
Substantial difficulty	9.6	4.3
Extreme difficulty	0.0	4.3
Not applicable—haven't sought credit	40.4	26.1

3. To what extent is your business having difficulty obtaining financing for desired short-term uses such as paying workers and acquiring inventories of material or supplies?	Oct '10 (percent)	Oct '11 (percent)
No difficulty	36.5	47.8
Some difficulty	13.5	15.2
Substantial difficulty	3.8	0.0
Extreme difficulty	1.9	4.3
Not applicable—haven't sought credit	44.2	32.6

4. Has your firm's production and/or sales been adversely affected by difficulty obtaining credit?		
	Oct '10 (percent)	Oct '11 (percent)
Yes, significantly	7.7	2.2
Yes, somewhat	15.4	17.4
No	40.4	43.5
Not applicable—haven't had problems obtaining credit	9.6	13.0
Not applicable—haven't sought credit	26.9	23.9

5. Has your firm reduced hiring and/or increased layoffs due to difficulty obtaining credit?		
	Oct '10 (percent)	Oct '11 (percent)
Yes, significantly	3.8	4.3
Yes, somewhat	7.7	17.4
No	51.9	41.3
Not applicable—haven't had problems obtaining credit	7.7	13.0
Not applicable—haven't sought credit	28.8	23.9

Survey Collection period: 10/11/2011–10/14/2011

Special Questions Comments

These comments have been edited for publication.

Credit Intermediation and Related Activities

The regulatory environment is causing the restriction in credit. Banks are less prone to loan money due to concerns with regulators.

Food Services and Drinking Places

Securing credit for any transaction has been very challenging due to tighter banking regulation.

Water Transportation

We are an investment rated company, which makes a difference.

Ambulatory Health Care Services

We have been asked for additional corporate level guarantees from large vendors on purchases that we wouldn't normally expect to provide such information.

Management of Companies and Enterprises

This questionnaire does not really apply to us since we are a bank and don't really borrow money like most businesses or consumers. However, new regulations on mortgage loans and strict fair lending requirements are going to cause us to lend less money. We are not tightening our standards due to the economy. We are tightening them due to regulations. We have to do that or risk violating a regulation and putting the bank at risk.

As a bank, we can tell you that we are lending to manufacturers and small businesses. We are underwriting cautiously, but most applications are approved. There is still tepid demand.

Professional, Scientific, and Technical Services

What we have seen over the past months is that credit and loans seem to be more plentiful and more numerous. Residential refinancing has recently increased dramatically. Although commercial activity is good, we have not observed an increase that is as dramatic as we see in residential; but credit seems to be out there, being administered in a thoughtful and reasonable manner.

Our business is directly related to the global capital markets. With the uncertainty in the current economic climate, the commercial mortgage-backed security market has continued to slow down, thus slowing our business flow.

Administrative and Support Services

Although we have not executed a loan, we have asked the bank for a substantial line of credit while we search for a larger building. The bank had no problem with that situation.

While the difficulties in the debt markets haven't affected our sales or hiring yet, they will if they continue into 2012.

Truck Transportation

The only difficulty we are seeing at this time seems to be a tightening in the depth of diligence from our banking partners. We recently had a six-person meeting to discuss a single month variance of .04 on a single element of a loan covenant.

Real Estate

The ability of the consumers that we represent to get credit has been increasingly difficult. This has a noticeable impact on our sales.

Securities, Commodity Contracts, and Other Financial Investments and Related Activities

We are in the financial service business, which includes all forms of insurance, wealth management, real estate development/multifamily housing and mortgage banking. The only two areas where we borrow money are commercial real estate and the mortgage banking area. We've been fortunate and haven't had any issues. We build Class A multifamily housing. We've had some problems finding lenders/partners in developing new projects, even though the multifamily housing market is very hot right now. We own properties in Pearland, Austin, Dallas and San Antonio. We are almost at capacity at all of our properties, averaging 97–98 percent rentals. Of course, this is due to so many people having difficulty qualifying for residential mortgages.

Insurance Carriers and Related Activities

We are a local community bank; therefore, we are generally aware of credit availability in this region. We believe there is much more lending capacity than there is demand in the system. Reluctance on the part of qualified borrowers to add debt to their balance sheets is a primary factor limiting economic growth, not availability of credit.

Building Material and Garden Equipment and Supplies Dealers

Credit is still tight as restrictions on asset-based loans still seem strict. We see that only a small percentage is being loaned for inventory and receivables. We will have to renew our line of credit at end of this month; we will see then how tight credit is for our business.

Merchant Wholesalers, Durable Goods

We have not had much difficulty in getting credit; however, we have had to go through much greater detail in our financials. Large down payments are required for any real estate, and more bank fees are being requested. We are putting off our real estate expansion because of tightening credit.

From our perspective, banks make it very difficult for businesses to conduct commerce. In the construction industry, there are many significant projects that are on hold due to the lack of reasonable financing available. Also, many businesses have significant equity tied up in real estate that cannot be monetized due to banks and other financial institutions not making funds available for real estate financing. The use of this untapped equity can allow business to recapitalize, grow and hire more people.

We manufacture cooling equipment so because of the extreme heat we had this year, we had a great year. After a difficult 2009, we had strong growth in 2010 and 70 percent growth this year.

Motor Vehicle and Parts Dealers

The problem is not obtaining credit. The problem is the desire to do anything that requires credit for fear that the federal government will come up with a requirement that makes any expansion not profitable because of government regulations, fees and taxes.

We are not having difficulty in obtaining credit for our company. Also, we are able to obtain financing for all of our customers who have reasonable credit scores of 580 and above.

Our company is exceptionally strong financially, and credit is not an issue. The auto industry seems to be relatively better than the general economy, and credit is available.

General Merchandise Stores

We haven't been in the market since May. Indications are that the market has tightened on availability, terms and spreads. We do believe that there would be credit availability, but at higher spreads than six months ago.