

Texas Economy Expanding at Moderate Pace

The state's economy continues to grow, but the latest readings suggest a mixed bag, with some sectors growing and others faltering. Texas nonfarm payroll employment grew 2.2 percent in April and 1.7 percent for the first quarter—a decline from the 3 percent pace of the previous six months (*Chart 1*).

Slowing job growth usually shows up in the unemployment statistics. Yet, the Texas jobless rate fell to a seven-year low of 4.2 percent in April, and other indicators of labor market conditions, such as initial claims for unemployment insurance, have been favorable in recent months (*Chart 2*). The Dallas Fed's Beige Book survey of business leaders supports the notion that labor markets are tighter than the payroll data indicate.

Sectors whose employment growth has been especially strong include mining and natural resources, professional and business services, and leisure and hospitality. Retail sales and consumer confidence are holding up reasonably well.

Tentative signs of stabilization are showing up in technology industries. Texas high-tech service employment grew 5.8 percent in

the first quarter, compared with 1.2 percent for the nation. High-tech manufacturing employment has stalled after an encouraging January, although its growth rate remains slightly ahead of the nation's.

Cautionary Signs

Significant weakness has emerged in manufacturing. Factory employment, a source of strength just a year ago, has been softening for several months. It fell 1.7 percent in April and 3.5 percent for the first quarter. One positive development over the past six weeks is a marked upturn in the petrochemical sector, driven mainly by unusually strong demand.

Construction-related manufacturing continues to falter, a reflection of the general slowing in the industry. Construction contract values plunged in the first quarter, albeit from high levels (*Chart 3*). The decline was broad based, with residential, nonresidential and nonbuilding (road and bridge) construction all falling.

Texas' exports came in lower than expected over the past few months, probably contributing to the lull in manufacturing

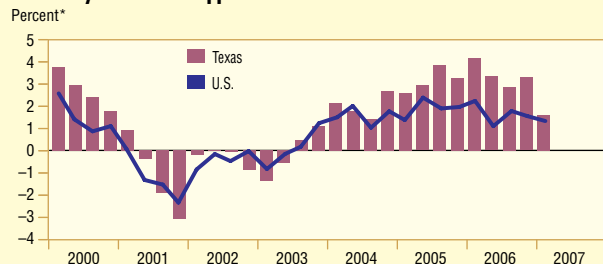
employment. For the first quarter, the state's overseas sales slipped by 3.3 percent, ending five straight quarters of strong growth. With the notable exception of China, Texas exports were down to all major trading partners, with Mexico off 3.7 percent and Canada 2 percent. Industrial production has been stagnant or falling in America's two North American Free Trade Agreement partners, which account for nearly half of Texas' exports.

Beige Book reports show retail sales stronger than expected. In line with this, real, seasonally adjusted sales tax revenue has performed well over the past several months, suggesting continued strength on the consumption side.

Consumer confidence in the West South Central census region remains the highest in the nation, bolstering Texas' medium-term outlook. This confidence is reflected in rising sales tax receipts and barometers of future economic activity. While flat in recent months, the Texas leading index remains above the national reading (*Chart 4*).

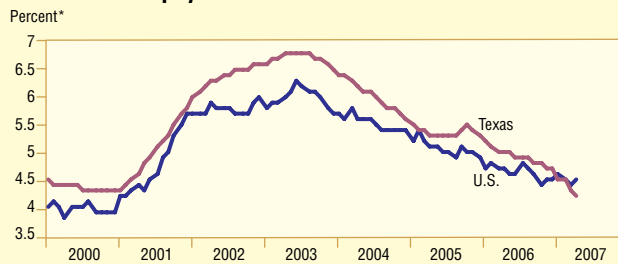
—Jason L. Saving

Chart 1 Payroll Growth Appears to Downshift in the First Quarter



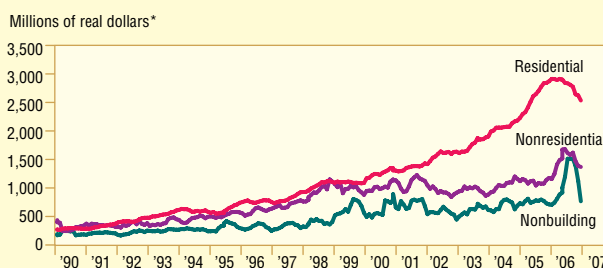
* Quarter-over-quarter, seasonally adjusted annual rate.
SOURCES: Bureau of Labor Statistics; Texas Workforce Commission; seasonal adjustment by Federal Reserve Bank of Dallas.

Chart 2 Texas Unemployment Rate Falls Below U.S. Rate



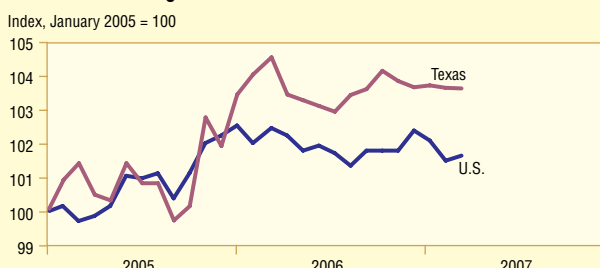
* Seasonally adjusted.
SOURCE: Bureau of Labor Statistics.

Chart 3 Texas Construction Contract Values Fall Across the Board



* Five-month moving average, seasonally adjusted.
SOURCES: McGraw-Hill Dodge Construction; Bureau of Labor Statistics.

Chart 4 Texas Leading Index Flat but Above Nation's



SOURCE: Federal Reserve Bank of Dallas.