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The '90s have been kind to the Texas economy. Though employment growth has surged and slowed, it remained positive throughout the decade, and, furthermore, it consistently outperformed the nation. The last time this occurred, everyone wanted to move to Texas and wear a cowboy hat and a big belt buckle, especially the unemployed rust belt factory worker. Today, while the state's economy prospers, it's not the type of counter-cyclical performance typical of the oil boom. The economic makeup of Texas largely mirrors the United States as a whole and, as a consequence, the things that threaten to further slow the national economy also will affect Texas.

According to the Texas Comptroller of Public Accounts, Texas ranks number one in the nation in crude oil and natural gas production and exports to Mexico.

The Lone Star State is second in population, third in gross state product, fourth in Fortune 500 companies, fifth in fertility rate, sixth in percent of population of school-age children, seventh in average household size, ninth in per-capita export-related jobs, tenth in civilian unemployment rate and thirteenth in percent of population living in metropolitan areas.

Also, we are 33rd in median household income, 39th in percent of persons 25 or older who are high-school graduates, 44th in percent of households owning their own home and 48th in median age.

These rankings portray the strengths and challenges facing Texas. The state is big, young and well tied into international trade. It is not highly affluent nor well educated.

What does this mean for real estate markets and those who make a living from them? This special Outlook and Review issue of *Tierra Grande* addresses that question. In the articles that follow, the research staff at the Real Estate Center discuss key trends in real estate markets, including:

- **The Economy.** General prosperity supports the vitality of most real estate markets. What must happen to keep the state's growth on track?
- **Housing.** Will the markets cool? What are the early signals of a slowdown?
- **Mortgage finance.** Does the Federal Reserve's determination to prevent inflation mean the end of affordable mortgages?
- **Commercial properties.** With skittish bond markets and backpedaling REITs, is it time for a cyclical downturn for investment properties?
- **Land.** How can rural land prices rise if farmers are hurting? Will Texas cities be able to grow relatively unfettered in the future?

These articles do not offer forecasts, in the strict sense of the word. They present key trends and indicators rather than educated guesses as to what might happen. Accordingly, the articles offer explanations of current trends and what might affect the markets in the near future. As that future unfolds, it will be worthwhile to keep in mind the important factors that determine what direction the markets will take.

The Comptroller of Public Accounts forecasts the slowing that began in 1998 to continue through 2000. A number of culprits are to blame.

- Growth in recent years has been the result of irrepresible consumer spending, fueled in large part by affordable credit and the "wealth effect" of soaring stock and housing values. This linkage places prosperity at risk from rising interest rates and falling asset prices. Furthermore, many worry about the continuing heavy debt load that consumers carry.
- With Asian economies on the rebound, the trend of falling commodity prices and cheap imports may be ending. This could raise prices in this country, which would not only hamper consumers but could goad the Federal Reserve into raising interest rates further. The resulting higher interest rates would be expected to slow the economy.
- Fears and uncertainty over the "Y2K" problem have caused disruptions. If nothing else, the cost of debugging and redesigning computer systems has been a dead-weight loss on the economy.
- Much of Texas' growth is concentrated in the construction and financial (which includes real estate) sectors. In fact, each is coming off of cyclical peaks. Both of these industries require growth to maintain their current level and scale back as growth rates slide.

With such dire outlook on the fundamentals, why is a recession not in the forecast? Because there are some positive trends as well.

Long-term and Recent Employment Growth in Selected Sectors of the Texas Economy

Sector	Employees (000)	Percentage change 1980-98	Percentage change 1999*
Mining	153.4	-33.4	-8.5
oil and gas	144.9	-30.4	-8.9
Construction	522.9	16.1	5.6
Manufacturing	1097.7	3.8	-0.8
non-durable	424.8	-0.1	-1.8
durable	672.9	6.4	-0.2
Transportation-communication	560.6	46.3	4.0
Wholesale trade	532.0	20.3	2.8
Retail trade	1615.8	52.2	1.8
Finance	512.0	42.6	3.9
real estate	220.7	48.7	5.2
Services	2621.8	141.2	4.6
business services	1048.4	266.8	7.0
health services	694.3	139.2	1.9
Government	1559.9	44.4	2.4
local government	1050.5	51.9	3.8

*May 1998 to May 1999

Source: Texas Comptroller of Public Accounts

Texas-U.S. Employment Distribution (Percent of Total Employment in Each Industry)

Industry	Texas 1980	Texas 1998	U.S. 1998
Mining	4.2	1.9	0.5
Construction	7.1	5.5	4.8
Manufacturing	17.7	12.4	14.9
Transportation-communication	6.1	6.1	5.2
Trade	24.5	23.6	23.1
Finance	5.8	5.5	5.4
Services	17.3	28.1	29.8
Government	17.4	16.9	15.8

Source: Bureau of Labor Economics

- Exports are an important component of the Texas economy. In the first quarter of 1999, the state's exports to Asia, Europe and South America declined by 7 percent. Much of this decline was caused by weaker demand for oil and the equipment used to produce petroleum products. Improved global economies should boost demand and reinstate exports as a positive growth force.
- Fluctuations in the oil market no longer have the ability to roil the Texas economy the way they did years ago. Although still important to some regions, oil no longer holds a dominant position in the state-wide economy. Production of crude oil in 1998 was 459 million barrels, compared to 872 million barrels in 1982. In fact, in recent years, the Texas economy has performed best when oil prices were weakest. Breaking the link to oil means less future volatility.
- Much growth in recent years has been spurred by widespread technological change. One ongoing event is the expansion of the fiber optic network within the state and the improvement in communication speed it will provide.
- Similarly, the coming deregulation of public utilities will change the operation of utilities in the state and already has stimulated construction of power generating facilities,

especially in rural areas where there are few environmental constraints.

The long-term fate of the state's economy will depend on several key resources:

- **Water supplies.** Some areas face limitations and heavy cross-basin importing of water may run into political impediments. As supplies become more restricted and demand grows, expect water to become a more expensive commodity in many areas. Regions with ample clean water will have a clear advantage.
- **Clean air.** Growth and sprawl are blamed for the poor air quality in several of Texas' large cities. Implications include impact on the ability to expand and recruit new industries and the ability to build new highways. Either could crimp growth in several regions.
- **Labor.** While labor is in short supply, it is the educated and skilled employees that are in demand. Texas has a young, ethnically diverse population and will need to find ways to provide the skills sought by the desirable growth industries. ♣

Dr. Harris is a research economist with the Real Estate Center at Texas A&M University.



What a year for Austin. Bolstered by the fast-growing computer industry, the city also is getting positive vibes from its traditional base of state government and the University of Texas. In 1998, Austin was named the number one boomtown in the nation by *Fortune* magazine.

Fastest Growing Texas Economies

Metro Area	Employment July 1999 (000)	Percentage Change Past Year
1. Austin-San Marcos	696.1	4.1
2. Tyler	89.3	4.0
3. Fort Worth-Arlington	893.7	3.4
4. Laredo	68.9	3.3
5. Texarkana	54.3	3.2
6. Dallas	1895.7	2.9
7. Waco	99.6	2.6
8. Bryan-College Station	72.5	2.5
9. San Antonio	759.1	2.4
10. El Paso	266.3	2.3

Source: U.S. Bureau of Labor Statistics

Note the prominent placement of large metros in the top ten list. Most have diversified economies that may benefit from growth in a number of industries. Somewhat notable is the appearance of El Paso, which has done well to counter the well publicized shut down of a major Levi Strauss plant.

The smaller cities on the list have benefited from their location and function as regional service and trade centers. Employment has been boosted as well by both residential and industrial construction.

Slowest Growing Texas Economies

Metro Area	Employment July 1999 (000)	Percentage Change Past Year
1. Odessa-Midland	117.8	-3.7
2. Brazoria	100.1	-0.7
3. Galveston-Texas City	117.6	-0.3
4. Corpus Christi	168.9	0.4
5. Lubbock	120.5	0.7
5. Victoria	42.1	0.7
7. Brownsville-Harlingen-San Benito	114.1	0.8
8. Houston	2103.6	1.0
8. San Angelo	51.5	1.0
10. Amarillo	111.8	1.2

Source: U.S. Bureau of Labor Statistics

The slow-growth economies (see table) suffered job losses in the manufacturing sector. In addition, those with significant numbers in the oil and gas extraction business lost ground. These metros suffered from plant shutdowns, declining oil drilling activity and dwindling trade and service demand in their regional markets. ♣

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