

# Slower Growth in the Tenth District

By *Tim R. Smith*

For the Tenth Federal Reserve District, 1985 was a year of sluggish economic growth. Weakness in two major sectors of the district economy—agriculture and energy—kept district economic performance below that of the United States. Growth was slower in 1985 than in 1984 for most district states—Colorado, Kansas, Missouri, Nebraska, New Mexico, and Oklahoma.<sup>1</sup> Only Wyoming, which started from a weak base, showed improvement. In 1986, the pattern of sluggish economic growth is expected to continue in the Tenth District.

## Overview of the district

Economic activity in the district increased in 1985, but at a slower pace than in 1984.

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<sup>1</sup> At the time of writing, the latest available personal income data were through the second quarter. For employment, third-quarter data are estimates based on two months of historical data.

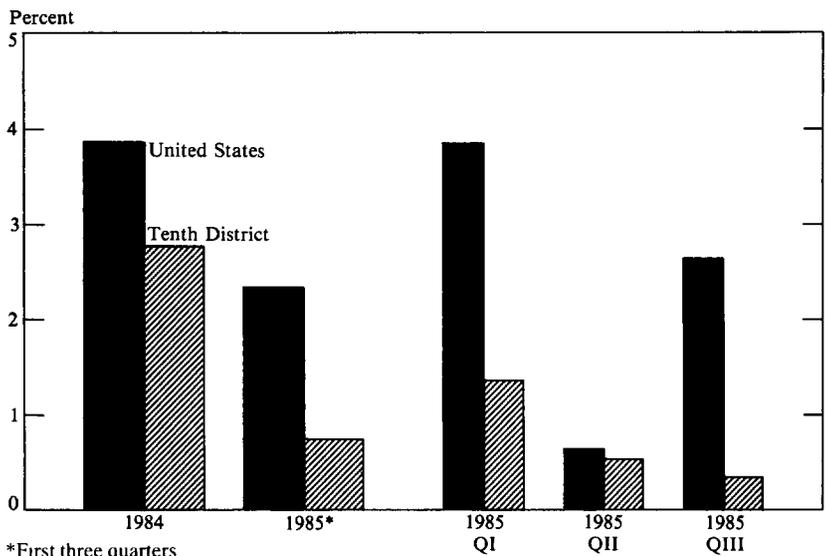
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For example, district employment rose at an annual rate of 0.8 percent in the first three quarters of 1985, compared with a 2.8 percent increase in the year 1984 (Chart 1). Reflecting the slow growth of employment, the district's unemployment rate increased to 6.5 percent in 1985 after declining in 1984. Thus, the gap between the district and U.S. unemployment rates narrowed (Chart 2). Also, real personal income in the district rose at an annual rate of 0.9 percent in the first half of 1985, considerably less than the 4.6 percent gain posted in 1984 (Chart 3). Income and employment growth during the latter part of 1985 very likely continued on the same slow path set earlier in the year.

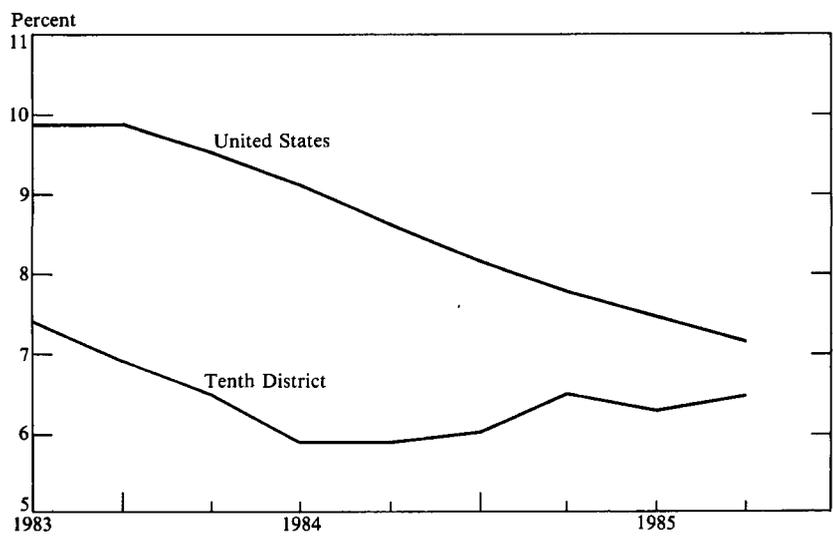
Not only did the district economy slow in 1985, but it also performed less well than the national economy. The district's real personal income growth was only about two-fifths that of the nation's in the first half of 1985, while in 1984 income growth in the district was four-fifths that of the nation's growth. Employment growth was also slower in the district than in the nation during 1985.

**CHART 1**  
**Growth in nonagricultural employment**  
 (seasonally adjusted annual rates)



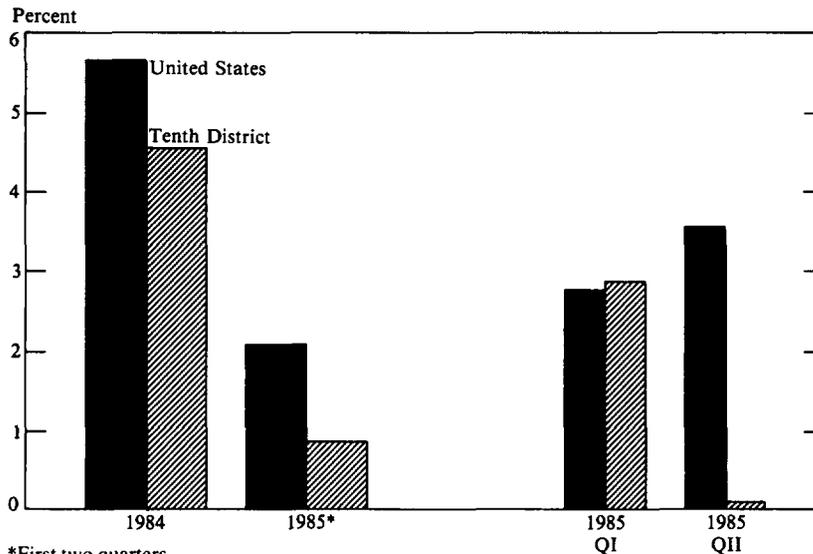
\*First three quarters  
 Source: Data Resources, Inc.

**CHART 2**  
**Unemployment rate**



Source: Data Resources, Inc.

**CHART 3**  
**Growth in real personal income**  
 (seasonally adjusted annual rates)



\*First two quarters  
 Source: Data Resources, Inc.

**Sectoral performance: a mixed bag**

The district's sluggish economic performance in 1985 was tied closely to continued weakness in agriculture and energy. The performances in other sectors were somewhat uneven. The government and service sectors continued to lend some strength to the district economy, but the manufacturing sector's performance was generally weak. Automobile manufacturing, however, remained a bright spot for the district.

**Energy and mining**

The district's energy industry in 1985 was adversely affected by weak world demand, large supplies, and soft energy prices. The downward slide in crude oil prices and a per-

sistent surplus of natural gas led to lower exploration, development, and production activity.

Oil and gas exploration and development activity in the Tenth District decreased markedly during 1985. The weekly average number of operating drilling rigs fell almost a fifth during the first three quarters of 1985 compared with the first three quarters of 1984. This drop, from already low levels, is a widely accepted signal of the failing health of the energy industry.

Energy production also fell in most parts of the district during 1985. Cumulative production of crude oil in the district for the first six months of 1985 was nearly 1 percent less than in the same period in 1984. The district's production of natural gas was off even more. Through June 1985, cumulative marketed pro-

duction of natural gas stood 4.6 percent below production for the same period a year earlier. Coal production rose slightly, as mined tonnage through the third quarter of 1985 was up 3.7 percent from 1984 levels.

There was no recovery in other mining over the past year. Uranium and copper mining was still in the doldrums, with many mines either closed or operating far below capacity. Production of bentonite, soda ash, and precious metals was stable, though at low levels. The molybdenum industry operated at only 60 percent of capacity.

### *Agriculture*

Financial problems continued to mount for farmers in the Tenth District during 1985. They harvested a bumper crop, export markets remained weak, and farm prices continued to slump. Moreover, livestock prices were softer than anticipated, bringing additional financial stress to many areas in the district. Farm lenders came under increased financial stress as loan losses increased and collateral values declined. Most farm communities remained plagued by the prolonged farm recession. Businessmen in rural communities saw farmers further cut their purchases of discretionary items and capital goods as farm income dropped sharply. Sales of tractors, combines, and other big-ticket items were especially soft.

### *Manufacturing*

District manufacturing activity weakened considerably in 1985. Although the automobile industry fared well, energy and agriculture-related manufacturing showed no signs of recovery. Overall, manufacturing employment in the district fell in the first three quarters of 1985 at an annual rate of 1.6 percent, compared with an increase of 4.0 percent in 1984.

Automobile assembly in district states maintained the strong momentum gained during the 1984 model year. Plants in district states recorded an additional increase in production during the 1985 model year. Moreover, these plants continued to operate at capacity as they moved into the 1986 model year.

Performance was again mixed for the district's high-technology industry. Deepening problems in the computer and semiconductor segments of the industry resulted in layoffs and plant closings as firms made further efforts to forestall financial losses. These firms found themselves facing fierce competition from abroad. But defense-related firms performed well, and the application of high-technology production methods to traditional sectors continued to gain importance throughout the district.

Recovery in the district's important general aviation industry remained elusive in 1985. The average quarterly value of aviation production decreased about 10 percent over the first three quarters of 1985 from the same period in 1984. Unit sales of new aircraft were also down about 10 percent in the three-quarter period, but aircraft shipments did improve as the year wore on. That improvement reflected a modest pick-up in sales of moderately priced propeller-driven aircraft. However, in both years, sales were concentrated in more expensive business aircraft. In addition, military contracts helped buoy district general aviation manufacturers in this period of weak demand and strong foreign competition.

Energy and farm equipment-based manufacturing in the district showed no signs of rebounding in 1985. Dormant exploration and development in the oil and gas industry have kept demand for oilfield equipment soft. Farm equipment sales for 1985 continued the downward trend established during the previous three years.

## *Construction*

Despite a weaker-than-expected residential housing market, construction remained a source of strength to the district economy in 1985. The disappointing performance in the district's residential construction industry generally matched the performance of that industry nationwide. Despite lower mortgage rates, district housing starts reached an annual rate of only about 116,000 units in the second quarter of 1985, compared with about 157,000 starts in 1984.

The overall strength in the construction industry in 1985 can therefore be attributed to nonresidential activity. The value of nonresidential construction contracts was up 5.3 percent through the third quarter of 1985 from the same period a year earlier. Cities participating in the growth included Kansas City, Omaha, Colorado Springs, and Albuquerque. Office construction slowed sharply in Denver, a city that appears overbuilt with one of the nation's highest office vacancy rates. Nonresidential construction remained weak in Oklahoma City and Tulsa, due mainly to the energy recession.

## *Services, retail trade, and wholesale trade*

The district's service industry slowed in 1985 after registering solid gains during the previous year. Moreover, growth in services activity in the district remained less than for the United States as a whole. Service employment in the district increased at an annual rate of 2.3 percent during the first three quarters of 1985 compared with 5.5 percent in the year 1984. Nationwide, employment in services increased 3.5 percent during the first three quarters of 1985.

Employment in wholesale and retail trade also improved in the same period, but at a slower rate than employment in services.

Growth in district wholesale and retail trade has been tempered by depressed rural economies across much of the district. Employment in the district's wholesale and retail trade increased 0.5 percent during the first three quarters in 1985 compared with 5.3 percent in 1984. Again, growth was less than for the nation as a whole.

## *Government*

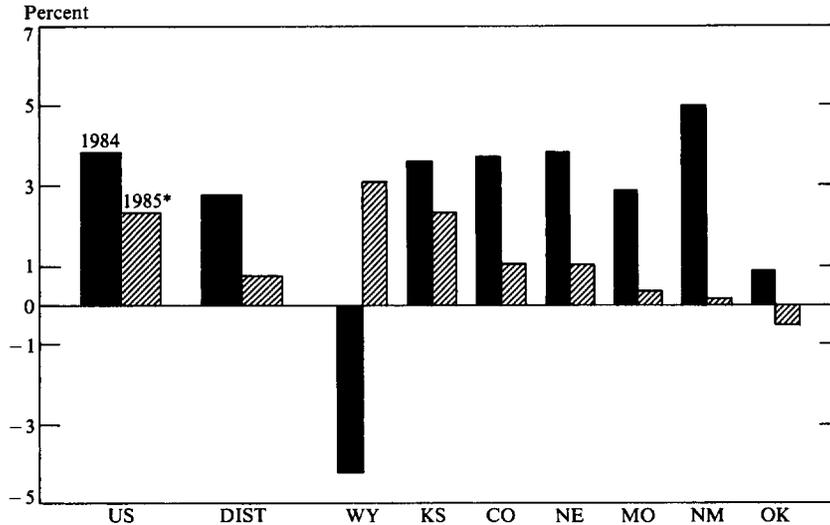
Federal government spending contributed significant strength to many district states in 1985. The Energy and Defense departments accounted for a large part of federal spending in the district. As a proportion of total federal spending, defense spending ranges from a high of nearly 40 percent in Kansas and Missouri to a low of about 15 percent in Nebraska and Wyoming.

The fiscal position of several district states tightened in 1985, reflecting the generally weak economic conditions in the district. For example, state legislatures in Kansas and Oklahoma announced plans to impose substantial restraints on state spending. The spread between revenues and expenditures has been narrowed in some states by shortfalls in the collection of severance taxes resulting from the decline in crude oil prices.

## **The states: varied performance**

As in the district as a whole, economic activity in most district states slowed in 1985. For all states except Wyoming, growth in employment during the first three quarters of 1985 was slower than during the year 1984 (Chart 4). Real personal income grew more slowly during the first half of 1985 than in 1984 in all district states (Chart 5). Though growth was slow overall, there was some variation in the rates of change in income and employment across individual states.

**CHART 4**  
**Growth in nonagricultural employment**  
 (seasonally adjusted annual rates)



\*First three quarters  
 Source: Data Resources, Inc.

### Wyoming

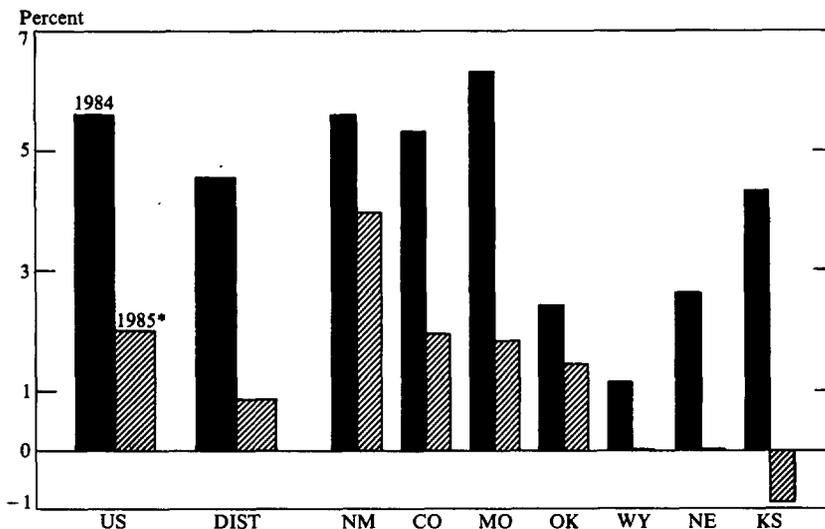
Wyoming's economy staged a modest recovery in 1985, despite its heavy reliance on natural resources. Employment growth, though moderate, improved substantially compared with the decline experienced in 1984. This growth was stimulated by a stronger tourist industry and growth in the state's service sector. On the other hand, real personal income was flat during the first half of 1985, reflecting continued weakness in mining and agriculture.

Tourism rebounded in Wyoming in 1985 after two weak years. The state's national parks had a good year, dispelling fears that a downward trend in tourism had been established. Tourism made a substantial contribution to overall growth in the state's service sector during 1985.

Performance in the state's mining industry was mixed in 1985. Though production of oil, gas, and coal increased, production levels were still low compared with earlier years. Production of oil and gas increased more than 10 percent during the first six months of the year. However, the number of drilling rigs in operation averaged 15 percent less in the first three quarters of 1985 than in the same period in 1984, reflecting expectations that general weakness in the energy industry will persist. Other mining activity in the state remained stable. Production of both soda ash and bentonite remained about the same in 1985 as in 1984.

Construction activity was also mixed in 1985. A surge in nonresidential construction offset a very weak residential market. The nonresidential construction activity was mainly associated with natural gas and carbon

**CHART 5**  
**Growth in real personal income**  
 (seasonally adjusted annual rates)



\*First two quarters  
 Source: Data Resources, Inc.

dioxide processing in the southwestern part of the state.

Agriculture contributed little to economic growth in Wyoming in 1985. Since agricultural sales in the state are dominated by livestock and livestock products, soft cattle prices brought additional financial troubles to Wyoming's ranches.

**Kansas**

Evidence of economic growth in Kansas was mixed in 1985. While employment grew at a moderate rate and above the average for all district states, real personal income fell. Also, economic performance as measured by changes in employment and income was weaker than in 1984. Growth in income did not occur during the first half of 1985 as it did during 1984 due partly to reduced farm

income. Employment growth fell less sharply than income, reflecting uneven performance across sectors. Automobile manufacturing contributed solidly to growth during 1985, but the energy and general aviation industries showed little strength.

The state's manufacturing sector continued to draw strength from the thriving automobile industry based in the Kansas City area. Automobile production continued at capacity throughout the 1985 model year after increasing 22 percent during the 1984 model year. In addition, plans were announced for a new highly automated automobile assembly plant that will represent a \$750 million investment.

General aviation, another manufacturing industry important to Kansas, did not perform nearly as well. Production over the first three quarters of 1985 averaged less than for the same period a year earlier, though the quar-

terly levels trended upward. The industry continued to face stiff competition from foreign producers, while the strong U.S. dollar also limited sales abroad of new aircraft. However, military contracts and large civilian air transports did provide some resilience.

Energy and mining failed to provide strength to the Kansas economy. Following significant increases in production during 1984, oil and gas output was flat in 1985. Cumulative production of coal in Kansas during the first three quarters of 1985 was almost 22 percent lower than in the same period a year earlier.

### *Colorado*

The Colorado economy made only modest gains in 1985, whether measured by growth in employment or income. The 1985 performance is in contrast with the relatively strong growth in 1984. Both employment and real personal income in the state grew at annual rates during the first three quarters of 1985 that fell short of the rates in 1984. Colorado's diverse economic resources provided some economic stability in 1985. The service sector had a strongly positive effect on growth, while manufacturing and mining lost ground.

High-technology activity, centered along the Front Range from Fort Collins to Colorado Springs, slowed significantly during 1985. High technology had been a strong stimulus for the state in both 1983 and 1984. Layoffs and plant closings became commonplace as the demand for computers, component parts, and peripheral equipment continued to soften. These developments were reflected in slower overall growth in manufacturing employment. Defense-related manufacturing, however, remained a source of stability to the manufacturing sector.

Construction activity also slowed considera-

bly in 1985. High vacancy rates for office space in downtown Denver brought nonresidential construction to a near standstill there. Moreover, residential construction in Colorado, as in the nation, was disappointing despite lower mortgage rates.

The important recreation industry fared well in 1985. Visits to national parks and monuments in Colorado increased, and the 1984-85 ski season was very successful. A 5 percent gain in skier visits, compared with the previous season, made 1984-85 the third consecutive record season for the Colorado ski industry. As a result, many larger ski areas announced ambitious expansion plans in addition to major improvements put in place during the summer.

Federal government spending, particularly for military purposes, remained a stabilizing force in the Colorado economy in 1985. For example, continued development of the Consolidated Space Operations Center in Colorado Springs spurred growth there during the year.

### *Nebraska*

The Nebraska economy had another difficult year in 1985. There was a modest percentage gain in employment during the first three quarters of the year, but no gain was made in real personal income. Thus, income growth was weaker than most other district states and substantially weaker than during 1984, when the PIK program benefits boosted farm income to Nebraska farmers. Most of the moderate economic growth in Nebraska was fueled by growth in services, while manufacturing remained weak.

Reduced farm income in 1985 added to the serious levels of financial stress that were evident in 1984. Sales of farm equipment were down again, accounting for the continued weakness in the state's farm equipment manu-

facturing industry. Food processing, the largest manufacturing industry in Nebraska, had a solid year but showed less strength than in 1984. This was most likely due to slower growth in the national economy and the associated weaker national market for food products.

Problems in agriculture have affected rural areas more than urban areas in the state. While nonmetropolitan Nebraska is heavily dependent on agriculture and thus depressed, metropolitan areas such as Omaha and Lincoln are more diversified. In these cities, growth in services, particularly finance and telemarketing, has contributed to overall employment growth.

### *Missouri*

The Missouri economy, as in 1984, showed growth that roughly matched growth for the district. Accordingly, growth in income and employment slowed in Missouri as it did across the district. Sluggish performance in these economic measures reflects poor performance in the state's agricultural and manufacturing sectors, coupled with residential construction that was weaker than expected.

Automobile production ranks first among Missouri's manufacturing industries. Though automobile plants operated at capacity throughout the 1985 model year, the strong U.S. dollar remained an obstacle for other manufacturers such as electrical machinery producers. In general, high technology did not contribute as much to growth in manufacturing in 1985 as it did in 1984.

Residential construction activity was weaker than expected in 1985. Housing starts remained flat through the first three quarters without showing improvement over 1984. Nonresidential construction remained healthy, stimulated by resurgent office construction in

Kansas City and St. Louis. The value of non-residential construction contracts through the third quarter of 1985 was 18 percent higher than a year earlier.

Depressed farm earnings in the state reflected a large harvest nationwide, weak export markets, and low commodity prices. These conditions contributed to a worsening of financial problems in Missouri's agricultural sector.

### *New Mexico*

Economic growth in New Mexico was moderate in 1985, after relatively strong performance in recent years. Employment growth during the first three quarters of the year was considerably slower than in 1984. Although real personal income growth remained healthy, it nevertheless slowed during the first half of 1985 compared with rates achieved in 1984. This moderation in growth can be attributed to some slowing in all important sectors.

Weak national and international markets for semiconductors and computers dampened New Mexico's economic growth in 1985. In the past few years, both manufacturing and construction had benefited from a movement toward new high-technology industries. High-technology firms least affected by the slowdown were those engaged in national defense research and contracting. Defense-related activities remained especially important in Albuquerque, Las Cruces, Alamogordo, Santa Fe, and Los Alamos. These communities also benefited from the increased importance of commercial applications of defense research.

Mining activity slowed sharply in 1985, the result of continued weakness in copper and uranium mining. Most copper mines in New Mexico remained closed or underutilized and uranium production was almost nonexistent due to depressed mineral prices. Production of

oil, gas, and coal lent some strength to the mining sector in 1985, though not as much as in 1984.

Given the problems in mining and high technology, the New Mexico economy was healthier than might have been expected. Government, financial services, and nonfinancial services such as those associated with tourism lent some strength. Though more sluggish than in 1984, the service industry provided stability to metropolitan areas of the state. Federal spending remained a major contributor to New Mexico's economic growth through the substantial number of military installations in the state and the large number of defense contracts let to the state's high-technology firms.

### *Oklahoma*

The Oklahoma economy was weak overall in 1985. Employment fell slightly and real personal income growth slowed in 1985. This slowing can be attributed to weakness in the two anchors of the Oklahoma economy—energy and agriculture.

The energy sector was a drag on the state's economy in 1985. Falling crude oil prices led to a sharp reduction in exploration and development activity. The result was overcapacity in drilling and associated declines in the value of oilfield equipment. In addition, cumulative production of both crude oil and natural gas through the first six months of 1985 were below levels for the same period in 1984. Consequently, there was no recovery in the state's oilfield equipment manufacturing industry.

As in other states, financial problems for Oklahoma's farmers continued to mount in 1985. These problems especially affected the economic climate of rural areas of the state.

Automobile production continued at a

healthy pace in 1985, partially offsetting the weakness in energy and agriculture. Oklahoma remained second among automobile-producing states in the district in 1985, after doubling production during the 1984 model year.

### **The outlook for 1986: more of the same**

The economy of the Tenth District is expected to remain sluggish in 1986. The moderate economic growth expected for the nation in 1986 will add little additional strength to district performance. Thus, district income and employment can be expected to continue growing at a relatively slow pace. Moreover, persistent weakness in energy and agriculture will likely cause overall district growth to continue to lag behind that of the nation.

Ongoing financial problems for energy and agriculture will figure importantly in the sluggishness of the district economy. Although spot crude oil prices remained firmer than expected in late 1985, due partly to reduced shipments from the Persian Gulf and the Soviet Union, they are expected to be lower by spring. Increased supplies of OPEC and non-OPEC oil and soft crude oil prices are expected to combine with continued surplus conditions in the market for natural gas to prevent any significant improvement in energy exploration and development activities in the district.

Nor are conditions in the district's agricultural sector expected to improve much in 1986. Continued large stocks and weak exports will keep crop prices low. Farm income may weaken somewhat in 1986, adding to already high levels of financial stress. Livestock prices, however, are expected to firm in 1986, bringing relief to some areas in the district.

The manufacturing sector will likely grow only slowly in 1986. The combined weakness in energy and agriculture will forestall improvement in oilfield and farm equipment manufacturing. Continued softness in general aviation and high-technology manufacturing also suggests sluggish performance in the manufacturing sector.

Performance in 1985 is a good indicator of

individual state performance in 1986, since no big changes are expected in overall economic growth in the district. While most states will experience sluggish growth as in 1985, those states with more diversified economies—Colorado, Missouri, and New Mexico—will likely do better than states that depend more heavily on agriculture and energy—Kansas, Nebraska, Oklahoma, and Wyoming.