

Health Care and Financial Services Buoy Houston Economy

Durable Goods Manufacturing Sees Improvement

Analysis and report by Ross Harvison,
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(Houston, Texas) – Area Supply Chain leaders indicate that economic activity in Houston contracted in February for the Fourteenth consecutive month.

The Houston Purchasing Managers Index (H-PMI) fell from its January level of 45.6 to 44.5 in February. The seasonally adjusted Finished Goods Inventory and Prices Paid Indices, the only two indicators that are inversely correlated with economic activity, continue to predict economic expansion near term. All other indicators (Sales/New Orders, Production, Employment, Lead Times, Purchases, and Purchased Inventory) are showing continued contraction.

The Sales/New Orders Index registered 41.3 in February, down 5.4 points from its January reading. The Production Index registered 38.6, down 0.5 points. The Employment Index registered 28.2, down 5.2 points. The Purchases Index registered 38.3, a decrease of 0.4 points. The Prices Paid Index registered 38.2, a decrease of 2.0 points. The Lead Times Index registered 35.5, falling 1.2 points. The Purchased Inventory Index registered 36.8, an increase of 1.6 points. The Finished Goods Inventory Index registered 29.9, a decrease of 0.6 points.

The Health Care sector continues to show significant strength and Financial Services remained strong. Durable Goods Manufacturing improved overall performance to above neutral for the first time since the middle of last year. Construction and Non-Durable Goods Manufacturing have moved to just below neutral overall, joining Wholesale Trade at this level. Oil and Gas exploration and related industries continue to cause the greatest concern for the near term growth of the Houston economy.

INDICES AT A GLANCE

Index	Feb	Jan	Change	Track	Rate	Trend*
Houston PMI	44.5	45.6	-1.1	Contracting	Faster	14
Sales/New Orders	41.3	46.7	-5.4	Falling	Faster	7
Production	38.6	39.1	-0.5	Falling	Faster	7
Employment	28.2	33.4	-5.2	Falling	Faster	13
Purchases	38.3	38.7	-0.4	Falling	Faster	14
Prices Paid	38.2	40.2	-2.0	Falling	Faster	14
Lead Times	35.5	36.7	-1.2	Falling	Faster	13
Purchased Inventory	36.8	35.2	1.6	Falling	Slower	15
Finished Goods Inventory	29.9	30.5	-0.6	Falling	Faster	14

* Months on current track



Commodities Reported Up in Price: Precious metals for catalysts; labor; vaccines

Commodities Reported Down in Price: Steel tubing; transportation fuels; natural gas; computers

Commodities Reported in Short Supply: Custom pharmaceuticals

WHAT OUR RESPONDENTS ARE SAYING AND SUMMARIES BY SECTOR

Oil and Gas Exploration, and Key Support Services:

- The new oil prices continue to adversely affecting upstream margins
- Right-sizing of project workloads and staff levels continue
- Rig counts in Texas are now in the low 200s; we haven't seen these levels since the 1990s
- Overall, respondents in this sector continue to report significant weakness

Construction:

- Respondents in this area report continued weakening ; sales and employment are reported as down by many respondents

Manufacturing - Durable Goods:

- Low energy prices continue to have a negative effect on goods manufactured for the oil and gas industry, there appears to be no relief in the near future
- Overall, respondents in this sector reported sales and production near last month's levels; employment continues to fall

Manufacturing - Non-Durable Goods:

- Margins and production remain positive
- Respondents in this area reported improving sales again this month, production near last month's levels, and employment continuing to decline

Health Care:

- We have observed an increase in hiring of contingent workers throughout the firm
- More orders are being placed with Amazon who recently opened corporate procurement; we are reviewing how this affects our purchasing processes
- More expansions in the medical industry
- This sector continues to report strength; employment and purchases rose again this month

Financial and Professional Services:

- Financial Services respondents report strong growth in current sales and new orders

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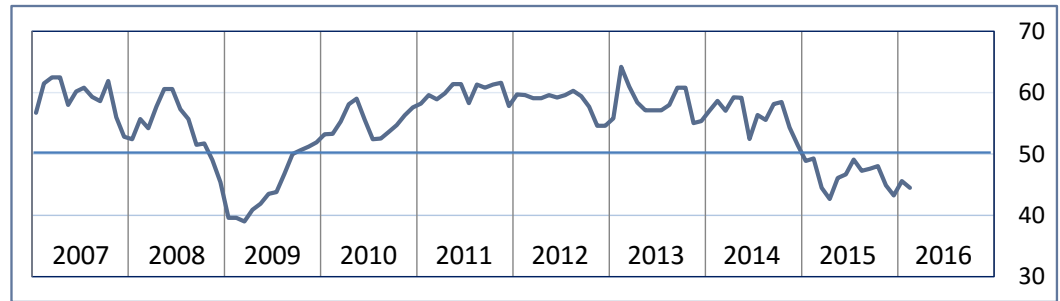


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Houston PMI Trend

The Houston PMI indicates likely shifts in production three or four months in advance. Readings over 50 generally indicate production expansion over the near term; readings below 50 show coming contraction.



Trend of Underlying Indicators

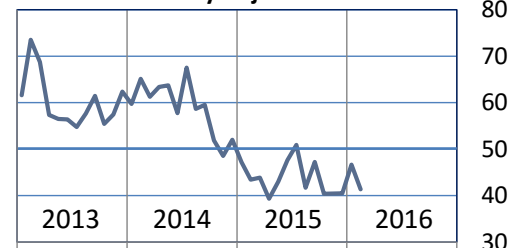
The Houston PMI is based on diffusion indices for eight underlying indicators as shown below. The net value of each of these indicators is simply the percentage of respondents who cite a positive shift from the previous month minus the percentage who cite a negative shift. The diffusion index is calculated based on the percent of respondents reporting higher results plus one-half of those responding the same with a seasonal adjustment based on an X12 ARIMA forecast using the previous 12 years data. Seasonally adjusted values above 50 for the Sales/New Orders, Production, Employment, Purchases, Lead Times and Purchased Inventory indicators point towards expansion and values below 50 signal contraction. The Prices Paid and Finished Goods Inventory indicators are inversely correlated to economic activity, meaning that values below 50 point to expansion and values above point to contraction.

Sales/New Orders

	% Higher	% Same	% Lower	Net	Index
Sep-15	25	45	30	-5	47.2
Oct-15	13	52	35	-22	40.4
Nov-15	14	50	36	-22	40.4
Dec-15	18	42	40	-22	40.5
Jan-16	27	39	34	-7	46.7
Feb-16	23	39	38	-15	41.3

The sales index returned to 4th quarter 2015 levels with durable goods and wholesale trade falling to near neutral. Non-durable goods manufacturing showed strengthening.

Seasonally Adjusted Index

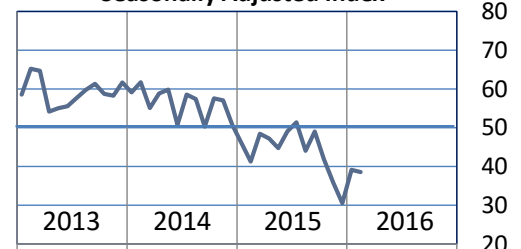


Production

	% Higher	% Same	% Lower	Net	Index
Sep-15	15	70	15	0	49.0
Oct-15	9	65	26	-17	41.8
Nov-15	6	61	33	-28	35.9
Dec-15	0	60	40	-40	30.5
Jan-16	9	61	30	-20	39.1
Feb-16	10	59	31	-21	38.6

The production index remained relatively flat with most industries reporting near neutral. Oil & Gas continues to show significant weakness in this and all other indices.

Seasonally Adjusted Index

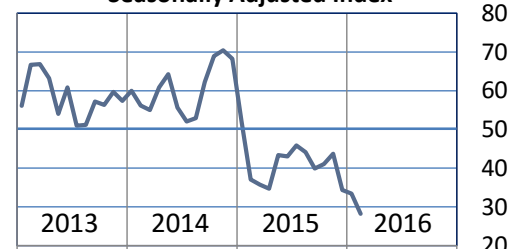


Employment

	% Higher	% Same	% Lower	Net	Index
Sep-15	15	50	35	-20	39.9
Oct-15	11	56	33	-22	41.1
Nov-15	11	61	28	-17	43.7
Dec-15	7	51	42	-35	34.4
Jan-16	11	41	48	-36	33.4
Feb-16	13	31	56	-44	28.2

The employment index fell to it's lowest level since mid-2009 with additional reductions noted in Oil & Gas, Construction, and Manufacturing. Health Care continues to add staff.

Seasonally Adjusted Index



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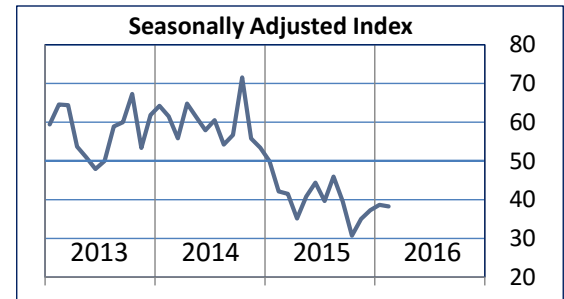
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Purchases

	% Higher	% Same	% Lower	Net	Index
Sep-15	30	25	45	-15	39.6
Oct-15	17	31	52	-35	30.7
Nov-15	17	36	47	-31	35.0
Dec-15	22	27	51	-29	37.3
Jan-16	30	20	50	-20	38.7
Feb-16	31	15	54	-23	38.3

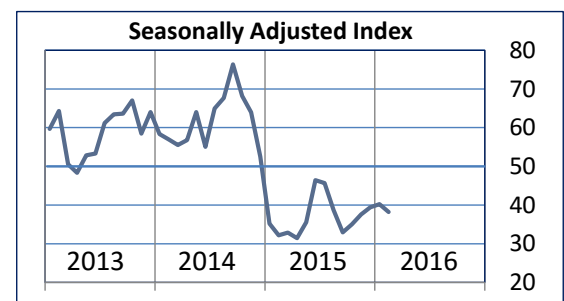
Purchases continued to contract with health care being the only sector reporting significant strength.



Prices Paid

	% Higher	% Same	% Lower	Net	Index
Sep-15	0	65	35	-35	32.9
Oct-15	0	70	30	-30	35.0
Nov-15	3	69	28	-25	37.6
Dec-15	7	64	29	-22	39.4
Jan-16	7	68	25	-18	40.2
Feb-16	5	67	28	-23	38.2

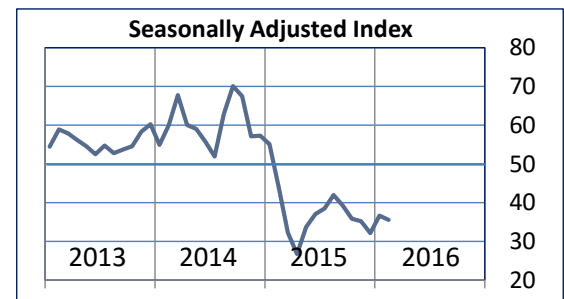
Price contraction changed minimally this month with all industries reporting results in line with last month.



Lead Times

	% Higher	% Same	% Lower	Net	Index
Sep-15	0	75	25	-25	39.2
Oct-15	0	70	30	-30	35.9
Nov-15	0	69	31	-31	35.2
Dec-15	0	64	36	-36	32.1
Jan-16	0	70	30	-30	36.7
Feb-16	5	62	33	-28	35.5

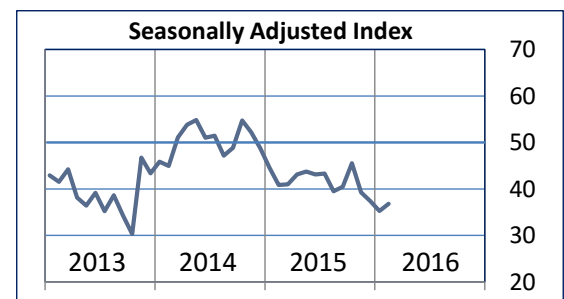
Lead times overall fell again this month. Health Care, and to a lesser extent Non-Durable Goods Manufacturing, are now seeing moderate increases in lead times.



Purchased Inventory

	% Higher	% Same	% Lower	Net	Index
Sep-15	5	65	30	-25	40.4
Oct-15	2	72	26	-24	45.5
Nov-15	3	72	25	-22	39.2
Dec-15	4	63	33	-29	37.4
Jan-16	5	65	30	-25	35.2
Feb-16	8	61	31	-23	36.8

Purchased inventories continue to fall.



Finished Goods Inventory

	% Higher	% Same	% Lower	Net	Index
Sep-15	5	60	35	-30	37.2
Oct-15	4	59	37	-33	40.6
Nov-15	3	72	25	-22	36.8
Dec-15	0	64	36	-36	30.9
Jan-16	9	48	43	-34	30.5
Feb-16	10	41	49	-38	29.9

Finished goods inventories also continued to fall with the index reaching its lowest level since the survey began. Respondents are clearly working to minimize working capital.

