Job Market Weakens but Home Prices Rise in 'Energy Patch' States

By Ralph DeFranco, Ph.D

It's been a year and half since energy prices began plunging. A barrel of oil that sold for $115 in June 2014 was priced at just $35 around the end of 2015. As we move into 2016, it is worth assessing employment and housing trends in U.S. coal-, oil- or gas-producing regions—the so-called "Energy Patch"—and studying the implications for credit unions.

Overall, lower energy prices are contributing to economic growth, saving the average U.S. family about $550 a year, even as exports have been hurt by a rising dollar and weakness overseas. The U.S. economy is currently generating a healthy 2.5 million net new jobs a year.

Nevertheless, total employment in the Energy Patch (Alaska, Louisiana, New Mexico, North Dakota, Oklahoma, Texas, New Mexico and Wyoming) has been deteriorating and likely hasn't hit bottom yet. (See Figure 1.)

EMPLOYMENT TRENDS

As Figure 1 shows, total employment fell fastest in North Dakota, the state that experienced the largest energy-related boom in recent years. Our analysis suggests that North Dakota is the most vulnerable to home price declines since home prices there are now about 20 percent higher than what we would expect, given the historic relationship between income and home prices.

California, Colorado and Pennsylvania were not included in the Energy Patch charts since their employment growth has not appreciably slowed and energy extraction is a small share of their economic activity.

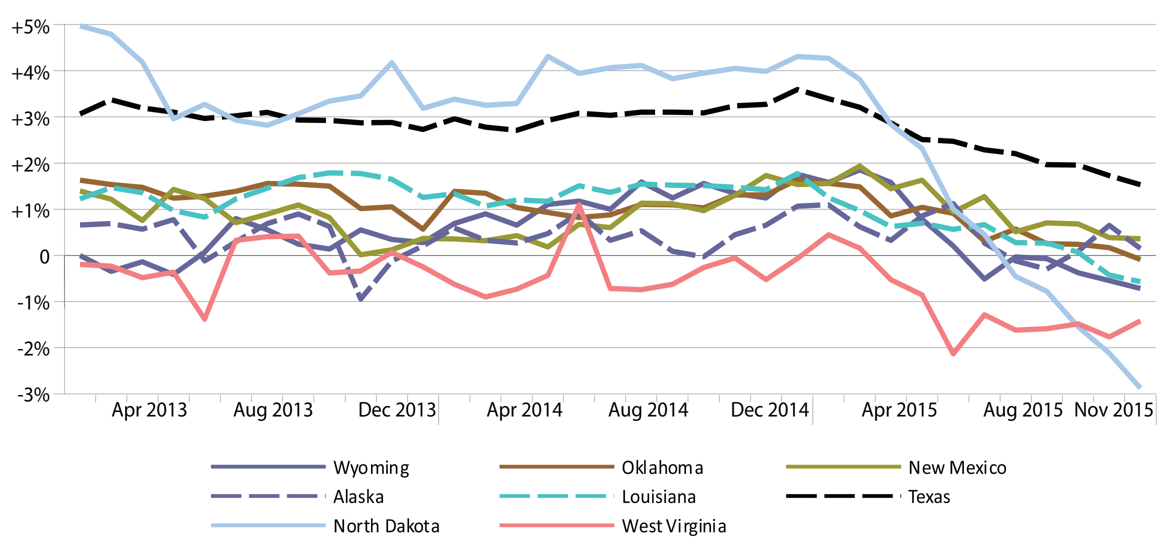
Texas employment is trending downward in similar fashion to neighboring oil- and gas-producing states. In Figure 2, we take a deeper look at several cities in Texas that show the slowdown in broad-based trends.

HOUSING TRENDS

Turning from employment to housing, the situation in the Energy Patch is decidedly mixed:

- Home prices have held up well, growing at about the same rate as the year before.

FIGURE 1 EMPLOYMENT CHANGES IN ENERGY PATCH STATES



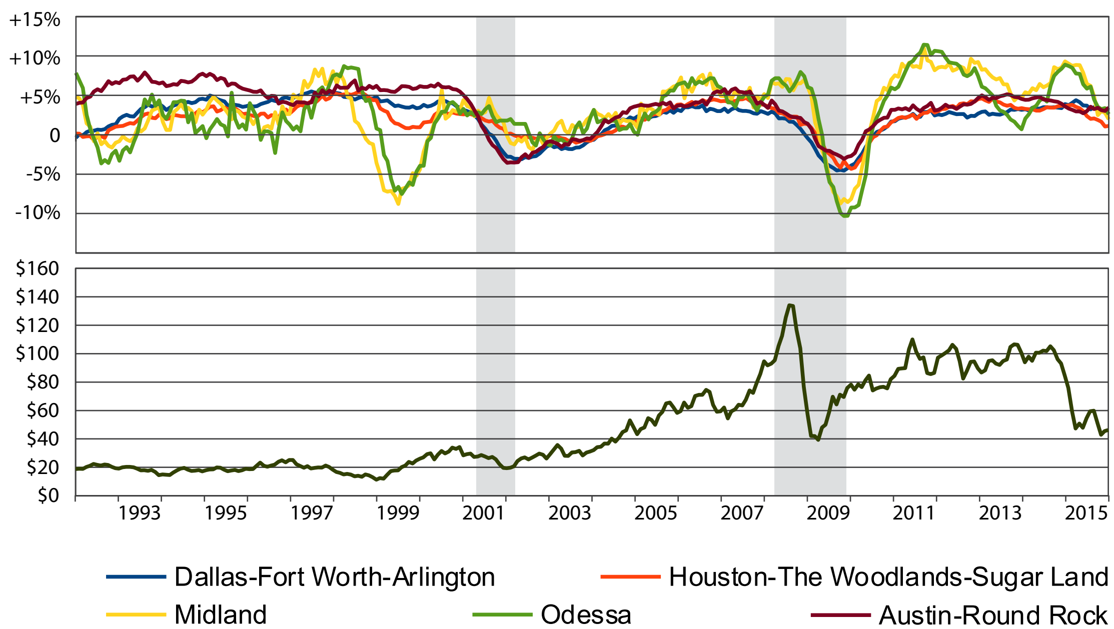
Sources: U.S. Bureau of Labor Statistics, Moody's Analytics, Arch MI

- Mortgage delinquency rates have actually been improving except in Alaska and North Dakota (per the Mortgage Bankers Association 60-day delinquency rate).
- New home builders have been cutting back on production as sales have weakened.

Even though home prices have held up well (Figure 3), it is reasonable to expect home price growth will slow in these states over the next few years.

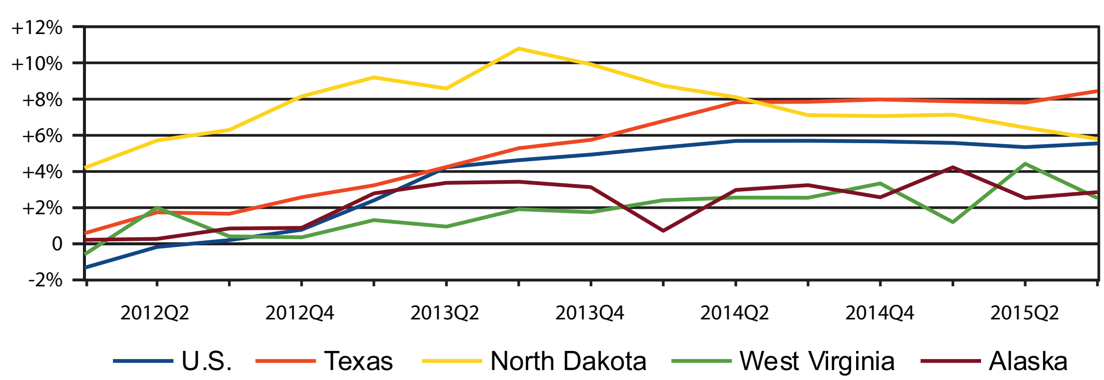
Some boomtowns, such as Williston, North Dakota, are very likely to see home price declines, while most of the larger cities will probably experience anemic growth as other sectors of the economy, such as health care, slowly expand.

FIGURE 2 NON-FARM EMPLOYMENT CHANGES IN TEXAS & LIGHT SWEET CRUDE FUTURES PRICE PER BARREL



Sources: U.S. Bureau of Labor Statistics, U.S. Energy Information Administration, Moody's Analytics, Arch MI. Gray bars indicate recessions.

FIGURE 3 HOME PRICE GROWTH IN KEY ENERGY PATCH STATES



Source: FHFA All-Transaction Index, Moody's Analytics, Arch MI.

CONCLUSIONS

Figure 5 summarizes our views on which of the Energy Patch states are most at risk of experiencing price declines and why.

We are most concerned about the less populated states of Alaska, North Dakota and Wyoming because of their high share of employment in energy extraction and weakness in the jobs market.

We also are concerned about coal mining areas such as West Virginia, since competition from natural gas has hurt coal prices. Other states worth watching are Louisiana, Oklahoma, New Mexico and Texas.

Employment and housing conditions will likely remain weak and probably worsen somewhat in most of the Energy Patch for several more years, particularly in Alaska, North Dakota, Wyoming and West Virginia.

Certainly home sales will continue to lag and the risk of price declines are elevated, but a widespread housing bust is not the most likely scenario.

Fortunately, direct employment in fracking was relatively small, except in thinly populated areas such as western North Dakota. It is true that boomtowns like Williston, North Dakota, are in for a protracted contraction, but that isn't true for most of the larger cities in the Energy Patch states. Since the fracking boom only lasted three or four years, it didn't create a widespread housing bubble. Home valuations are far more reasonable now than before the large "Oil Patch" bust in the 1980s. The notable exception is North Dakota, where we estimate that home prices are overvalued by roughly 20 percent.

We expect several years of substandard growth, but not a repeat of the regional-wide recession that occurred in the 1980s. Conditions are stronger now than in the 1980s, thanks to a more diversified employment base, a well-capitalized financial sector (a regional financial crisis greatly exacerbated the problems in the 1980s), still-affordable home prices and spillover benefits of solid employment growth from the United States overall.

Clearly, credit unions that are highly concentrated in Energy Patch states need to be especially vigilant with credit guidelines and loan quality control, and should carefully monitor housing market conditions in their footprint.

Ralph DeFranco, Ph.D., is the Housing Economist for Arch Mortgage Insurance Company.

FIGURE 5 RISK OF HOME PRICE DECLINES *

State	Probability of Home Price Declines	Annual Change in jobs** (Nov 15)	Comments
North Dakota	46%	-2.9%	We estimate home prices are highly overvalued due to the fracking boom.
Wyoming	37%	-0.7%	Mining employment in the nation's largest coal producer has fallen to 10-year lows.
Alaska	33%	0.1%	Home price growth is decelerating as low energy prices have waylaid the most oil- dependent economy in the nation.
West Virginia	33%	-1.4%	Coal prices and employment are hurt by competition from cheap natural gas.
New Mexico	31%	0.4%	At risk of a recession due to government- and energy-related job losses.
Oklahoma	28%	-0.1%	Total employment fell in the past 3 months and home prices are decelerating.
Louisiana	28%	-0.6%	Economy is still growing, but new home construction is down.
Texas	26%	1.5%	Employment growth remains weak, but positive in recent months. Home prices growing faster than the national average.

** Source: Arch MI. The Arch MI Risk Index® estimates the probability home prices will be lower in two years, times 100. It comes from a statistical model based on regional unemployment rates, affordability, net migration, housing starts, the percentage of delinquent mortgages, the difference between actual and estimated fundamental home prices (based on income), and judgmental adjustments. We do not predict the size of potential home price declines, just the likelihood of prices being lower by any amount two years from now*

*** Total year-over-year change in total employment as of November 2015.*