GREATER HOUSTON PARTNERSHIP 2011 EMPLOYMENT FORECAST

GHP
GREATER HOUSTON PARTNERSHIP
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Recovery to Strengthen in '11 **—** Houston's economy will continue to grow next year, adding more jobs in '11 than in '10. By December, Houston will have replaced many of the jobs lost during the recession and be closer to a full recovery. Growth will be fueled by the ongoing U.S. recovery, growth in the developing world, a weak U.S. dollar and rising oil prices. However, several factors will temper that growth—the drilling moratorium in the Gulf of Mexico, weak natural gas prices, a soft real estate market, and government budget woes.

For Houston, the recovery began in April '09, the first month the Houston Purchasing Managers Index registered an uptick after trending downward for more than a year. Two months later, the North American rotary rig count rebounded. Passenger traffic at the Houston Airport System picked up in August. Cargo shipments through the Houston-Galveston Customs District began to improve in November. Employment, a lagging indicator, began to grow again this February.

Key Economic Indicator	Recession Trough	Current Reading
Purchasing Managers Index	39.0	56.3
Rig Count	876	1,723
HAS Passenger Traffic[1]	47.6	49.3
Customs District Trade[2]	166.1	204.5
Payroll Employment[3]	2.479	2.525

[1] 12-month total, millions of passengers
[2] 12-month total, $ billions in value
[3] million of workers

Sources: *National Association for Purchasing Management-Houston, Baker-Hughes, Houston Airport System, U.S. Census Bureau, Texas Workforce Commission.*

How bad were the losses? **—** From the start of Houston's recession in September '08 to the bottom in January '10, the region lost 135,400 jobs, one in every 19 in the region. Those are seasonally unadjusted numbers. On a seasonally adjusted basis, Houston lost 115,900 jobs or one in every 23 in the region.

Even so, Houston fared better than most other metros. During the recession, Atlanta lost 210,000 jobs, one in every 11; Phoenix lost 235,000 jobs, one in every eight; Miami lost 250,000 jobs, one in every 10; and Los Angeles lost 541,000 jobs, also one in every 10. In fact, of the nation's 20 most populous metro areas, only Washington, D.C. lost a smaller share of jobs than Houston. (All metro comparisons are based on seasonally adjusted data prepared by the U.S. Bureau of Labor Statistics.)

This recession also was not as significant as the one Houston experienced in the mid-'80s. That recession dragged on for nearly five years and saw 221,000 jobs—one in every seven—slashed from local payrolls. The '08-'09 recession lasted 17 months and saw a third fewer jobs lost. The region has already recovered some of those losses. In the 12 months ending October '10, Houston posted a net gain of 6,200 jobs. While that's far off Houston's normal pace of adding 50,000 to 60,000 jobs per year, it is an improvement over the job losses suffered in '09.

Constraints to Growth **—** More jobs would have been created this year if not for several factors affecting local business and consumer confidence. In January, the Obama administration proposed a NASA budget that shifted to the private sector funding for programs run through the Johnson Space Center. In March, Congress passed the

Health Care Reform Act, compelling the local health care community to begin rethinking its business model. In May, the administration placed a moratorium on deepwater drilling in the Gulf of Mexico, idling rigs and workers. The possibility of Congress imposing a cap-and-trade system to reduce greenhouse emissions lingered throughout the year. And Continental Airlines announced it would merge with United Airlines, locating its new headquarters in Chicago. Those factors impacted Johnson Space Center, the Texas Medical Center, the oil and gas industry, the Gulf Coast chemicals and refining complex, and the transportation sector. In light of all the turmoil, Houston's job growth in '10 wasn't nearly as trivial as it might seem.

The recovery that began this year in manufacturing, transportation, wholesale and retail trade, professional services, personal services, hotels and dining services should continue in '11. Energy employment will rise as growth in exploration and production more than offsets shrinkage in oilfield services. Health care employment will continue to grow. Construction will continue to shed jobs. State and local government, including area school districts, will also suffer job losses.

Regardless of the weak real estate market, the de facto moratorium in the Gulf, and government budget woes, Houston will continue to grow for the second consecutive year.

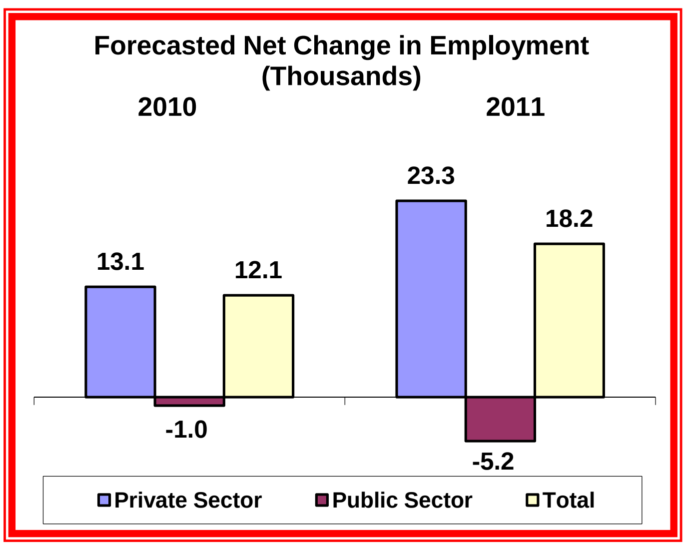
Job Growth Next Year — GHP's forecast calls for the region to add 23,300 private sector jobs in '11, but the improvement will be tempered by the loss of 5,100 public sector jobs. The net gain will be 18,200 jobs. The greatest gains will be in health care and social assistance, 5,700 jobs; professional and business services, 4,300 jobs; accommodation and food services, 3,400 jobs; retail trade, 2,200 jobs; oil and gas extraction, 2,100 jobs; and manufacturing, 2,000 jobs. The greatest losses will be in government, 5,100 jobs; construction, 3,500 jobs; and oil field services, 1,100 jobs.

It should be noted that the value of this forecast lies not in the accuracy of the numbers, but in understanding the trends driving the data. Armed with this knowledge, readers should be able to make better informed decisions in the coming months. Here, in greater detail, are insights into the direction Houston's economy will take in '11.

Natural Resources & Mining — GHP forecasts the exploration and production sector to add 2,200 jobs next year, while oilfield services will lose 1,000 jobs, resulting in a net gain of 1,100 jobs by year's end. Rising oil prices, weak natural gas prices, strong U.S. and global demand for oil and the de facto moratorium in the Gulf of Mexico are factored into GHP's forecast.

The price of oil has more than doubled over the past two years. The spot price for West Texas Intermediate (WTI) was $33.17 a barrel in mid-December '08 and $89.18 mid-December this year. The U.S. Energy Information Administration (EIA) forecasts WTI to average $86.08 next year. Growing demand has helped drive up prices. The United States now consumes 150,000 more barrels a day than it did during the second quarter of '09, at the bottom of the recession. Worldwide crude consumption rose 2.75 million barrels per day during the same period.

Natural gas prices, on the other hand, remain weak. The Friday closing spot market price for Henry Hub natural gas opened the first week of this year at $6 per million cubic feet, held above $5 through the early part of the year, slipped below $5 in the spring, and sold for around $4.50 in mid-December. Much of the gas-directed drilling activity has been supported by contracts guaranteeing a price of $6



and above. The bulk of those contracts will expire by mid-'11. EIA's forecast that Henry Hub gas will average $4.33 in 2011 means there is less incentive to drill for gas next year.

The spread between oil and gas prices has already impacted the rig count. The number of rigs looking for oil in North America has grown 68.1 percent this year, up from 427 rigs the first week of January to 718 mid-December. In contrast, the number of rigs searching for natural gas grew 22.3 percent, from 781 the first week of January to 955 mid-December. Oil-directed drilling now accounts for 43 percent of all rigs in the field, up from 20 percent in mid-May of last year. By the end of '11, more rigs will be drilling for oil than for gas, and the rig count will be 8 to 10 percent higher. The rig count stood at 1,723 the second week of December, up 32.6 percent from the same time last year.

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The shift to onshore oil drilling will not be enough to offset the drop in offshore drilling. Though the drilling ban has been officially lifted, a de facto moratorium imposed through safety regulations and a slow permitting process remains in place. Exploration companies, rig operators and service companies can't wait indefinitely for activity to resume in the Gulf. Some have already shifted resources overseas. As a result, the service side will experience more layoffs next year.

Construction — The construction industry faces a fourth straight year of declining activity. The industry will complete projects valued at $7.9 billion this year, down 5.2 percent from '09 and 43.9 percent below '07's record of $14.1 billion, according to McGraw-Hill Construction. The decline is reflected in the employment numbers: since the onset of the recession, this industry has lost 41,600 jobs—roughly a third of Houston's overall net job loss. Though there has been an uptick in employment—2,100 jobs added in October—GHP expects further reductions in construction employment next year.

- The inventory of resale homes continues to inch upward. As of November, Houston had a 7.7 month supply of homes for sale—well above the norm of a 6.0 month supply. The inventory of resale homes will grow as more foreclosures enter the market, further reducing the demand for newly built homes.
- In the third quarter of '10, the office market recorded its first positive absorption since the end of '08. Nonetheless, the vacancy rate remains high. According to CB Richard Ellis, an estimated 31 million square feet of office space is vacant in Houston, and another 4.2 million square feet is available for sublease. With an ample supply of office space, there is little need for new general purpose office buildings.
- Another potential weakness in the outlook for construction is that the Texas Medical Center construction boom, which began several years ago, appears to be winding down. In addition, constraints on government budgets will result in reduced spending on road, water and sewer improvements.
- Finally, with the refining industry operating at 85 percent of capacity, there is little pressure to build new plants or upgrade existing facilities.

One bright spot is that Houston will see retail construction as H.E.B., Kroger, Wal-Mart and Whole Foods will move forward with previously announced expansion plans. Retail construction, unfortunately, will not offset declines elsewhere. GHP forecasts the construction industry to lose 3,500 jobs next year.

Manufacturing — The recovery in manufacturing that began in '10 will continue into '11. The durable goods sector, which lost 12,000 jobs during the recession, has added 1,000 jobs since January. That trend should continue as the U.S. and global economies continue to recover.

Through October, the volume of industrial, electrical, and scientific equipment and shipments through the Houston-Galveston Customs District were $1.4 billion or 4.8 percent ahead of the same period in '09. Most economists expect growth in the developing world to exceed that of the U.S. over the next few years, further increasing demand for Houston's exports. The dollar has fallen 13.3 percent against major world currencies since March '09, making the goods and services Houston exports more affordable to overseas buyers.

> ***Sectors Adding Jobs in '11:*** *exploration and production, manufacturing, wholesale trade, retail trade, utilities, transportation and warehousing, information, finance, insurance, real estate, professional and business services, administrative support, educational services, health care and social assistance, arts, entertainment & recreation, accommodation and food services, other services*

> ***Sectors Losing Jobs in '11:*** *oilfield services, construction, government*

Demand for fabricated metal products, mainly structural steel, should remain flat until construction activity rebounds. The Gulf drilling moratorium will reduce the demand for locally produced oilfield equipment. The increase in onshore drilling will not be enough to offset losses in the offshore market. Employment in chemicals and plastics has been flat since before the recession, but low prices for natural gas, a key input in the manufacturing process, may support some marginal growth in employment. As a result, GHP forecasts total manufacturing employment to grow by 5,000 enduring '11.

Transportation and Warehousing — The recession brought a downturn in global trade, which in turn reduced traffic through the region's ports and airports, thereby reducing activity in waterborne, rail, trucking and air transportation services. Reduced manufacturing, construction and retail sales activity had an additional impact on trucking and warehousing. As a result, this sector lost 12,600 jobs in the recession.

The impact of the Continental-United merger on local employment remains unknown. The jobs most at risk are those associated with corporate office functions. Some of these tasks will be transferred to the new headquarters in Chicago, but some tasks performed in Chicago will be transferred to Houston. Employment at Bush Intercontinental could even grow as the combined airline integrates routes and provides additional services through its Houston hub.

All other trends are positive. Through the first nine months of this year, export tonnage through the customs district is up 17.6 percent and import tonnage up 2.8 percent. Nationwide, manufacturing output is up 9.8 percent from its recession trough. Air cargo volume through the Houston Airport System has risen for 13 consecutive months and is now at a record high.

GHP forecasts the transportation sector to gain 1,900 jobs next year, an improvement of 1.7 percent over current levels.

Retail Sales — Three trends bode well for growth in retail employment next year:

- Through June of this year, local cash registers rang up $45.0 billion in gross retail sales, a 13.2 percent increase over the same period last year, according to the Texas Comptroller of Public Accounts.
- The number of new cars, trucks and SUVs sold in the Houston metro area in October rose to 23,222, a 33.7 percent increase from October '09, according to the latest TexAuto Facts Report, published by InfoNation, Inc. of Sugar Land. That performance pushed the gain for the first three quarters above 10 percent.
- Total salaries and wages in Houston exceed $32.7 billion in the second quarter this year, up $400 million, or 1.3 percent, from the same period last year, according to the Texas Workforce Commission.

Recent job growth, the recovery of the stock market, stable local home values (compared to the rest of the country), and a general sense that the worst is over have bolstered consumer confidence and should feed retail sales growth in Houston. GHP expects the region to add 2,000 retail jobs next year.

Wholesale Trade — Houston's wholesale sector lost 12,800 jobs during the recession. Most of the loss occurred in the durable goods trade, mainly machinery and equipment. With the rebound in global trade, gradual improvement of the credit markets, and growth of the U.S. economy in general, wholesale trade activity should pick up in '11. As a result, GHP expects employment in this sector to grow 0.9 percent and to add 1,300 jobs next year.

Utilities — The utilities sector experienced no net job losses during the recession. GHP forecasts employment to grow 2.0 percent, or 300 jobs, as Houston benefits from industry consolidations and continued population and employment growth.

Information — This sector includes newspaper, magazine, book and directory publishing, motion picture, video and sound recording, software development and publishing, radio and television broadcasting, telecommunications and internet services. With improvements in technology and corporate restructuring, the industry has found it can function with fewer employees. This sector has lost 16,000 jobs since October '00, including 1,600 jobs lost during the recent recession. GHP sees little change in this sector in '11.

Finance and Insurance — Several factors contributed to the loss of 4,000 jobs in finance and insurance during the recession. Some firms became insolvent and folded. Others were forced to consolidate with stronger entities. Banks and S&Ls, which had added nearly 300 branches in Houston the three years prior to the recession, began closing offices. Merger and acquisition activity fell off. Loan activity dried up.

There are signs of improvement, however. The banking industry added 15 new branches in the past year having added only three the year before. If the industry returns to normal growth patterns, it should add 20 or more branches next year.

As the members of the baby boom generation move into retirement, demand for health insurance and long-term-care insurance, as well as annuities and other types of pension products sold by insurance sales agents, should rise. Houston's growing population will continue to stimulate demand for auto and homeowners insurance. As the economy recovers and new businesses are formed, the demand for business-related lines of insurance will grow. GHP forecasts employment in finance and insurance to grow 1.5 percent next year, gaining 1,300 jobs.

Real Estate and Rental and Leasing — This is a relatively small sector, accounting for approximately 50,000 jobs, or 5.0 percent of the area's total. With office and industrial leasing activity off and home sales floundering, this sector lost 3,600 jobs during the recession. Leasing activity has begun to pick up and local real estate firms have begun rehiring. GHP forecasts this sector to grow 0.8 percent next year, adding 400 jobs.

Professional and Business Services — As the U.S. slid into recession, merger and acquisition activity fell. Companies focused on core operations. They postponed IT upgrades, slashed marketing budgets and put expansion plans on hold. Houston's advertising, public relations, law, engineering and accounting firms felt the impact. Billings fell and layoffs followed. This sector lost 17,400 jobs, an employment decline of 9.4 percent.

But the improving business climate has generated more opportunities in recent months. Since May, the sector has recouped 2,400 of those lost jobs. Engineering firms have begun rebuilding their backlogs. Merger and acquisition activity has begun to pick up. Companies are once again looking for ways to upgrade and improve their operations. As a result, GHP forecasts this sector to grow 1.3 percent next year, adding 4,300 jobs.

Administrative Support, Waste Management Services — This sector is a catch-all for corporate administrative functions, firms that provide outsourcing for back office operations, janitorial services and employee leasing firms. On a percentage basis, this sector suffered the worst job losses of the recession. When the layoffs started, contract workers were the first to go. And when the economy didn't improve quickly enough, companies cut outsourced services to the bare minimum. From peak to trough, this sector lost 28,800 jobs, impacting one in every six workers in the industry.

This sector also serves as a gauge for the strength of the recovery. In the early stages, firms tend to rely on contract workers to handle increased workloads before bringing on permanent staff. Once employers are confident the increased activity will continue, their contract workers often transition to full-time, permanent status. GHP forecasts this sector to grow 1.1 percent, adding 1,100 jobs in '11.

Education Services — This sector includes private elementary and secondary schools, business, technical and vocational schools, private universities and educational and testing services. It added 1,000 jobs during the recession as unemployed workers sought to upgrade their knowledge and skills to improve their chances in the job market. This trend should continue. GHP forecasts educational services to grow 1.8 percent and to add another 800 jobs in '11.

Health Care and Social Assistance — Health care and social assistance is one of the few sectors that added jobs throughout the recession. As of October '10, Houston's health care industry had 19,500 more jobs than in September '08, the month the local recession began.

Two factors play into continued growth in the health care sector—a growing population and an aging population. Houston adds 100,000 to 120,000 residents each year through natural increase (i.e., the excess of resident births over resident deaths) and net migration. Since '01, the region has added more than one million residents. Houston's population is aging. Since '05, the population over 65 years of age has grown 19.2 percent, to nearly 480,000. An aging population tends to demand more health care services. These trends will carry on, and growth in health care employment will continue.

It is too soon to determine the impact the Affordable Care Act will have on the Houston's health care industry. On one hand, providing for medical coverage for the uninsured increases the size of the potential market. On the other, restructuring the payment and delivery systems reduces profitability, at least in the short term. Consultants have already begun building practices on interpreting the 1,000-page bill for the industry. The impact of state budget woes will be felt much sooner. Half of the institutions in the Texas Medical Center are state-supported. The state also provides $6.4 billion in Medicaid coverage locally. If the state attempts to balance the budget by cutting funds to Medicaid, the potential impact in '12 is large.

In the near future, however, the outlook is upbeat. GHP forecasts that the health care sector will grow 1.1 percent, adding 5,600 jobs in '11.

Arts, Entertainment and Recreation — This sector includes performing arts companies, spectator sports, museums, historic places, nature preserves, amusement parks, arcades, golf courses, marinas, fitness centers, bowling centers and other entertainment venues. After utilities, this sector has the smallest employment base, employing approximately 25,700 people. It also consistently added jobs throughout the recession. As the Texas Gulf Coast continues to develop as a tourist destination and as Houston's population grows and demands more recreational opportunities, this sector will continue to grow. GHP forecasts the sector adding 800 jobs in '11, a 2.1 percent rise.

Accommodation and Food Services — The business community learned in '10 that not all business can be conducted over the phone or via the Internet. They needed "face time" with their clients to hold onto relationships developed prior to the recession. They also realized the need to attend conventions and trade shows to promote their products and establish new relationships. Travel budgets cut in '09 were partially restored in '10. Hotel bookings were up, air travel was up, and taking clients out to dinner was permitted again. By October, Houston had recovered 700 of the 2,400 jobs lost in the accommodation services sector during the recession. Houstonians may have cut their entertainment budgets during the recession, but they didn't altogether eliminate going out to eat. October '10 actually saw 2,700 more food service jobs than a year earlier. These trends should continue into '11. GHP expects accommodation and food services to grow 1.6 percent in '11, adding 3,400 jobs.

Other Services **—** This sector includes people employed in repair and maintenance services (e.g., automotive, electronics, industrial equipment, and household appliances), personal care services (e.g., barber shops and beauty salons), funeral services, dry cleaners, religious and nonprofit associations, professional associations, and miscellaneous personal services. From peak to trough, this sector lost almost 2,500 jobs as people learned to fix it themselves, do it themselves, let it stay broken or do without. The recovery that began in '10 will continue into '11, with this sector adding another 900 jobs by year's end.

Government **—** When the legislature convenes in Austin this January, lawmakers will face a budget shortfall estimated at between $24 and $30 billion. The City of Houston faces a shortfall upwards of $80 million this fiscal year. Harris County must deal with a budget shortfall approaching $40 million. Local school districts face reduction in state education funding as well as declining property tax revenues.

It is unlikely that Congress will enact a second stimulus package to help struggling state and local governments. Washington faces budget challenges of its own. Expenses at all levels will have to be cut. Steps to curtail public spending will start with reducing operating hours, deferring maintenance, eliminating nonessential services and possibly cutting pay. But the budget gaps are too wide to be trimmed through reducing waste, increasing efficiency and paring expenses. Some attrition is inevitable. GHP forecasts the government sector at all levels—federal, state, county, municipal and school districts—will experience job losses in '11. GHP anticipates a net loss of 5,100 jobs in '11, shrinking government employment in the Houston MSA by 1.1 percent.

Long-Term Outlook **—** Though Houston faces some challenges in the near term, the long-term outlook is bright. From '05 to '35, The Perryman Group sees Houston leading the state in population growth, adding 3.53 million residents and 1.325 million jobs and accounting for almost one-fourth of Texas job growth.

The long-term outlook for the Houston metro area is positive, and a return to steady, healthy growth is expected in the near future.

This forecast was prepared by Patrick Jankowski, with research assistance from Marycruz Garcia, Jenny Hsu and Roel Martinez.

GHP FORECAST FOR HOUSTON MSA NONFARM PAYROLL EMPLOYMENT (000)

Note: Some columns may not add up due to rounding	**Employment as of**		**Net Change**		**% Change**	
	Dec '10	**Dec '11**	**'09**	**'10**	**'09**	**'10**
Total Nonfarm Payroll Jobs	***2541.6***	***2559.8***	***12.1***	***18.2***	***0.5***	***0.7***
Total Private	***2165.9***	***2189.2***	***13.1***	***23.3***	***0.6***	***1.1***
Goods Producing	***484.4***	***484.2***	***6.3***	***-0.2***	***1.3***	***0.0***
Service Providing	***2057.2***	***2075.5***	***7.1***	***18.4***	***0.3***	***0.9***
Natural Resources and Mining	91.1	92.2	3.4	1.1	3.9	1.2
Oil & Gas Extraction	51.9	54.0	2.5	2.1	5.0	3.9
Support Activities for Mining	38.3	37.2	1.2	-1.1	3.3	-3.0
Construction	171.5	168.0	-0.8	-3.5	-0.5	-2.1
Manufacturing	221.8	224.0	3.7	2.1	1.7	0.9
Durable Goods Manufacturing	143.2	144.8	6.0	1.6	4.3	1.1
Nondurable Goods Manufacturing	78.7	79.2	-2.2	0.5	-2.7	0.6
Wholesale Trade	128.6	129.9	-0.9	1.3	-0.7	1.0
Retail Trade	277.3	279.5	1.6	2.2	0.6	0.8
Transportation, Warehousing and Utilities	105.2	107.1	-2.7	1.9	-2.5	1.7
Utilities	16.5	16.8	0.0	0.3	0.0	2.0
Air Transportation	23.8	24.0	-0.3	0.2	-1.2	1.0
Truck Transportation	19.0	19.4	0.5	0.5	2.5	2.4
Pipeline Transportation	8.8	8.9	0.0	0.1	0.0	1.0
Balance, incl Wrhsng, Water & Rail Transport	53.6	54.7	-2.9	1.1	-5.1	2.0
Information	32.2	32.2	-1.6	0.0	-4.7	0.0
Telecommunications	17.2	17.2	-0.7	0.0	-3.9	0.0
Finance & Insurance	86.6	87.9	-0.5	1.3	-0.6	1.5
Real Estate & Rental and Leasing	50.0	50.4	-0.6	0.4	-1.1	0.8
Professional & Business Services	349.5	354.1	-0.5	4.6	-0.1	1.3
Professional, Scientific & Technical Services	170.5	173.6	-3.1	3.1	-1.8	1.8
Legal Services	*22.8*	*23.1*	*-0.4*	*0.3*	*-1.7*	*1.5*
Accounting, Tax Preparation, Bookkeeping	*15.7*	*16.0*	*-1.5*	*0.3*	*-8.6*	*2.0*
Architectural, Engineering & Related Services	*61.4*	*62.6*	*0.9*	*1.2*	*1.4*	*2.0*
Computer Systems Design & Related Services	*23.5*	*23.7*	*-0.4*	*0.2*	*-1.7*	*1.0*
Admin & Support/Waste Mgt & Remediation	158.5	159.6	-0.9	1.1	-0.6	0.7
Administrative & Support Services	*151.4*	*153.7*	*-0.2*	*2.3*	*-0.1*	*1.5*
Educational Services	43.7	44.5	1.2	0.8	2.9	1.8
Health Care & Social Assistance	266.7	272.3	6.0	5.6	2.3	2.1
Arts, Entertainment & Recreation	27.5	28.3	1.5	0.8	5.8	3.0
Accommodation & Food Services	206.0	209.4	2.2	3.4	1.1	1.6
Other Services	91.6	92.5	1.0	0.9	1.1	1.0
Government	375.7	370.5	-1.0	-5.1	-0.3	-1.4
Federal Government	28.7	28.6	0.3	-0.1	1.1	-0.3
State Government	71.8	70.7	1.2	-1.1	1.7	-1.5
State Government Educational Services	*38.7*	*38.2*	*1.0*	*-0.5*	*2.7*	*-1.2*
Local Government	275.3	271.2	-2.4	-4.1	-0.9	-1.5
Local Government Educational Services	*187.9*	*186.0*	*-3.3*	*-1.9*	*-1.7*	*-1.0*

SOURCE: GHP Research Department based on Texas Workforce Commission data