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Business

Oil price woes ensnare manufacturers

Companies that supply equipment to the energy industry say demand for their products has dropped off

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Drilling rigs stand idle, or stacked, in a yard near Odessa in Texas' Permian Basin, where drillers have taken almost 200 rigs offline since October. (Photo: Perry Management, Market Watch)

The ripple effect of low crude prices is reaching Texas manufacturers that fashion iron and steel into oil field equipment, the Federal Reserve reported Monday, as drilling budgets shrink and job cuts spread.

A key measure indicating the level of manufacturing activity in Texas remains essentially flat for the second consecutive month, the Fed reported, and manufacturers that supply equipment to the oil industry reported falling demand for their products.

"You can see the weakness the past couple of months," said Emily Kerr, business economist at the Federal Reserve Bank of Dallas. "There's clearly this downward pressure from low oil prices."

The price of West Texas Intermediate, the U.S. crude benchmark, fell \$1.36 Monday to \$49.45 per barrel, less than half of its price last summer. Brent, the international crude standard, fell \$1.32 to \$58.90.

The Fed's findings were based on the results of a monthly survey of 150 Texas manufacturers.

The study found that the production index - a measure of manufacturing output - measured 0.7 in February as well as January. A positive number represents increasing activity in the sector, while a negative number represents a decrease.

The latest figure means manufacturing activity in Texas is mostly flat and just barely growing, Kerr said. The index is now at its lowest level in almost two years.

Less Equipment

Many U.S. energy producers have announced plans to pull back dramatically on drilling activity in 2015, betting they can make more money selling oil and get better prices from their vendors if they temporarily pump the brakes.

That means exploration and production companies, as well as the services companies that perform work on their behalf, don't need as much equipment to pull oil from the ground.

Tenaris, a manufacturer of steel pipes, said Monday it will suspend operations at its welded tubes mill in Conroe and lay off 230 workers there, in part due to a slowdown in drilling activity. U.S. Steel Corp. said last month it would lay off more than 750 employees - including 142 in Houston - as a result of falling oil prices. And earlier this month, GE said it would lay off 330 workers in its East Texas manufacturing operations.

"Oil at \$50 per barrel is painful," one respondent in the Fed survey said, noting his employer laid off a quarter of its workforce because of slowing demand. The Fed withholds survey respondents' names in order to encourage candid responses.

Requests on Pricing

Greg Bright, owner of Houston-based equipment manufacturer Ocean Fab, said in an interview with the Chronicle that customers have started sending him form letters requesting lower prices in light of crude oil's decline.

"We're working with them," said Bright, who wasn't part of the Fed survey. "We all want to survive this. But at the end of the day, their business is down. It doesn't matter how much of a discount we give them, they're slowing."

Bright said his company is diversified - upstream oil producers only represent 30 to 40 percent of his business - so he isn't too worried yet.

"I don't think it's the doom and gloom out there that people are proclaiming," he said.

'Very much affected'

But other manufacturers are less sanguine.

"We are very much affected by the crash in oil prices," a fabricated metal manufacturer said in the Fed's survey. "At the beginning of the month there was a wave of projects that were either canceled or placed on hold by the customer."

Just last week, the head of the National Association of Manufacturers, Jay Timmons, touted the industry's success before an audience at Rice University but also acknowledged that "new obstacles to our potential have affected this region significantly."

Workers Vulnerable

Radha Radhakrishnan, an assistant professor at the University of Houston, said manufacturing workers are especially vulnerable to layoffs during downturns because they represent greater ongoing costs than idle equipment.

"They're saying, 'I don't have the business, so I have to readjust my capabilities,'" Radhakrishnan said.

Tenaris, the Conroe pipe maker, was among several companies serving the energy sector that reported layoffs Monday. Oil field services company Archer Ltd. said it was cutting 1,000 jobs, or 11 percent of its workforce, as it faces a slowdown in drilling activity in the U.S. and the North Sea. The company, which is based in Bermuda, has its main U.S. office in Houston.

The slowdown is "most prominent in the U.S. land market, which at the current price of oil is uneconomical in many basins," Archer CEO David King said Monday during a conference call. King said the decline probably will continue throughout the first half of this year, though its duration is hard to predict.

The Texas Workforce Commission said Monday that it has received notice of 69 West Texas job cuts by Midland-based service company Advanced Stimulation Technologies and 58 layoffs in East Texas by Amega West Services, a Houston-based oil-tool rental company.

Positive Signs

Kerr, the Fed economist, said the survey did contain some positive signs. An index that shows manufacturers' predictions of business activity six months into the future switched from negative to positive this month.

Tony Bennett, president of the Texas Association of Manufacturers, said while manufacturers serving oil field customers are suffering temporarily, **low oil prices are benefiting those that make components for petrochemical plants.** And manufacturers that don't directly serve the energy sector at all "are still holding their own," he said.

But for those that do work with upstream oil and gas companies, the question remains how long the slowdown will persist. "This may last a year, or it may last 18 months," Bennett said. "It's anybody's guess."



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