

THE

Real Estate

AUSTIN LETTER

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Dear Client:

Looking for office space in Austin? Look out! The office market, remarkably, moved from 91% occupancy at the beginning of the year to 97% by mid-year. That's according to NAI/Commercial Industrial Properties, Inc., in a survey of office buildings 20,000 sq.ft. or larger not entirely owner occupied.

Citywide absorption for the first half of 2000 was 1.8 million sq.ft. That's an amazing 57% increase over the prior six months and **already 85% of the annual absorption in 1999.** Clearly the Austin area office market is as hot as our summertime record-setting temperatures. This indicates a continuingly vigorous economy, but makes it tougher for businesses to find office space – much less, affordable space.

The hottest of the hot areas? Southwest. NAI/CIP reports the **southwest sector is 100% occupied.** Well what about construction underway there? Will that help? An additional 500,000 sq.ft. will be added in the southwest over the next six months, but 94% of those projects are already pre-leased. Not much help there.

The record rate of absorption during the first six months of 2000 soaked up the large bloc of new construction left over from 1999. Citywide, new construction in the first half of 2000 was admittedly low – 260,000 sq.ft. That's estimated to increase by an additional 1.5 million sq.ft. by the end of the year. But you better **move fast if you want to grab some of that office space.** And be prepared to **pay a premium** for that new construction. The projects are 67% pre-leased, with an average rental rate 2.5% higher than average market rents.

What about **downtown?** NAI/CIP reports Class A rental rates are rising above replacement costs (12% in the past six months!) and the vacancy rate is at an all-time low of 3%. It's tighter than a tick and expensive. As expected, this is triggering new office construction downtown. But the first significant new construction will not be available for occupancy until early 2002.

It is clear office space absorption in 2000 will **approach or surpass the historical high of 2.2 million sq.ft. that was absorbed in 1984.** The only hope for businesses seeking affordable office space is to wait and see if any significant vacancy is created in existing buildings as the new construction becomes occupied over the remainder of 2000. But the wise businesses will be checking out the soon-to-be-vacant space well in advance of move-out dates.

The surging strength of Southwest Airlines is contributing to the record-setting passenger traffic at Austin-Bergstrom International Airport. During July, 707,153 passengers traveled through Austin's airport – an impressive 19.20% increase over the prior July. This is a new ABIA record that surpasses the record set in June 2000. For the year, passenger traffic is up 17.80%.

Much of the record-setting pace can be attributed to the phenomenal strength of Southwest Airlines. For years, Southwest has been the market traffic leader here. And when your market leader increases by a greater percentage than any of its smaller competitors, you know you're dealing with the biggest gorilla in the airline jungle. It's easy for a small entity with a small increase in numbers to show a higher percentage increase than a bigger entity with a bigger increase in numbers. Check out July year-to-date passenger numbers (the latest available):

Southwest Airlines totaled 1,626,696 passengers year-to-date, **up 30%! American Airlines (including American Eagle) totaled 1,104,525, up 6%. Delta Airlines (including Atlantic Southeast Airlines) totaled 494,517, up 7%. Continental Airlines totaled 443,911, up 15%. United Airlines totaled 263,654, up 16%. America West Airlines totaled 177,190, up 27%. Northwest Airlines totaled 139,986, up 14%. And TWA totaled 135,184, up 26%.**

Obviously, it's significant that all airlines serving Austin show healthy increases. But, it just makes what Southwest accomplished that much more impressive. Interestingly, a recent national study by **Darryl Jenkins**, Executive Director of the Aviation Institute at George Washington University, predicted **Southwest Airlines will soon overtake Delta Airlines as the largest US airline in numbers of domestic passengers boarded.** Pretty impressive for a little ole Texas upstart cattle-car airline that brags about serving you peanuts, instead of a meal.

The old "Pray For Me, I Drive US183" bumper stickers still have a bit of validity. And it's all due to the seemingly never-ending construction. In fact, get ready for another phase of lengthy roadwork. The new construction project will extend the freeway from Hunters Chase to just past RM620 over the next three years.

The work will result in **six main lanes and six frontage road lanes.** Work on the frontage roads, especially on the northbound side, will begin in earnest in mid-September, giving drivers a better idea of how the road will eventually look. Bulldozers and graders will begin clearing and smoothing the dirt left in the wake of the utility teams.

The utility work is what you've witnessed so far. Contractors are slaving away in the summer sun, digging trenches and laying pipe for storm water drainage along the path of the extended freeway. By the way, normally drainage utilities are pushed to the outside of the frontage roads, where future work won't interfere with traffic. But along this stretch of US183, much of the piping will end up between the main lanes and frontage roads – not a perfect situation.

Whiskey is for drinking, water is for fighting! That adage of the Old West doesn't necessarily apply in Central Texas these days, as cooperation seems to be the water watchword. At the same time, the Lower Colorado River Authority (LCRA) is emerging as a key, and very powerful, player across many governmental boundaries.

There have been a number of significant developments in recent months that, when taken together, provide a very interesting – and history-making – turn of events related to our most precious commodity, water. It seems especially timely as Texas suffers from a severe drought which has imposed water use restrictions on many residents and businesses. Look at what's happening while you've been concerned about watering your lawn only every five days.

The LCRA cut a deal with the City of Austin to give **Austin** a 50-year guaranteed supply of water. The LCRA cut a deal to build a treatment plant and distribution system to provide water to parts of **Travis County** and **Hays County**. The LCRA cut a deal with the Brazos River Authority (BRA) to sell the BRA water for re-sale to **Georgetown** and **Round Rock**. The LCRA cut a deal with small water districts along **Lake Travis** to take over treatment and distribution of water to them.

That's not all. The LCRA is cutting a deal with **San Antonio** and rice farmers near the **Gulf Coast** to build reservoirs to trap more water to benefit the Alamo City and farmers – and at the same time, retain more water in the Highland Lakes. And the LCRA is cutting a deal to lend **Blanco** \$3.3 million to design, build and operate a water pipeline to Canyon Lake.

In the frontier days of Texas, "wars" were waged over water. But, as these recent actions indicate, instead of warring over water, this part of Texas is working out arrangements to share water – **for a price**. Obviously, the common ingredient in all of these deals is the LCRA, a quasi-governmental regional agency. And that's where the power lies – and is growing.

Keep an eye on how this power is used. Remember, the LCRA is not restricted by the normal city/county governmental boundaries. For instance, if the City of Austin refuses to extend water to an area to control growth, would the LCRA step in to "cut a deal" with the area? One thing for sure, the LCRA is fast-becoming a **very powerful, major player in the development of this area**. And it is playing with the biggest trump card of all – water.

Now's the time to put in your two-cents worth on how political boundaries will be drawn, affecting who will represent you in the Legislature and Congress for the next ten years.

The Texas Senate and House Committees on Redistricting will hold a joint public hearing in Austin at 10:30 am, in the Senate Chambers, 9/22/00. This is one of the first steps that will lead to the slicing and dicing of districts when the Legislature convenes in Austin 1/9/01.

As Dell Computer Corporation enters what one writer calls “a sobering midlife crisis,” facing a growth slowdown in the PC industry, what’s next for the largest private employer in Austin? Michael Dell “believes that the same low-margin, high-velocity strategy that propelled Dell’s PC sales can work in high-end computing and data storage,” reports the *Wall Street Journal*.

“Dell is targeting **small servers** for Internet start-ups and corporate Web sites, with plans to move into **bigger, more complex computers**,” reports the *Journal*. “By using the lean production it has developed over the years, Dell hopes to underprice rivals and gain market share. At the same time it moved toward servers, the company clamped down on hiring and shook up its sales force.”

What Dell will do is of **immense importance to Austin and the Austin economy**. Whatever it does, however, is not expected to match past history. As many Dellionaires will proudly tell you, Dell was the single best-performing stock of the 1990s, with a 97% average annual price increase. This year, it’s stock is down 22%. And Dell revenues fell short of Wall Street’s expectations three out of the past five quarters.

But don’t confuse the mighty Dell Computer Corp with any high-flying Internet startup. “Dell this year should add nearly **\$7.6 billion in new sales**, more than the \$7 billion last year and the \$6 billion of two years ago,” reports the *WSJ*. “What’s more, Wall Street estimates this year’s **profit will rise 38%**, to \$2.56 billion from \$1.86 billion last year.”

Even with all its investment and initial costs to move into new areas, Dell Computer Corporation boasts of **\$4.32 billion – in cash** – on its balance sheet. And through its Dell Ventures unit, it has invested a billion dollars into 100 different companies ranging from Internet commerce to storage software. Obviously all Dell’s eggs are not in one computer box.

Dr. Louis Overholster just returned from an extended summer trip to Europe. He won’t say how much it cost, but he said his credit card bill arrived in an envelope marked OPEN SLOWLY!

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