

THE

*Neal Spelce*

# AUSTIN LETTER

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Dear Client:

**Austin area retailers are starting to be jolted by consumers. Even though our population has increased substantially in the past year, retail sales in April 2001 in Travis County — for the first time in a long time — actually dipped below the same month in the previous year, as measured by sales tax collections.**

These just-released numbers are the first solid indicators of a significant up-and-down swing in our economy. Sales tax collections were **down 1.70% in Travis County and they fell even more, -2.48%, inside the Austin city limits** in April, compared to the same time frame a year ago. These numbers are sobering because, statewide, sales tax collections were *up* 5.4%.

We've been tracking these numbers for you for some time now. You'll recall on 3/23/01, we pointed out the January 2001 sales tax collections inside the City of Austin were level — up only 0.19%. This miniscule increase caused us to raise the question "Are we looking at **a blip or a trend** in Austin retail sales?"

Then, 4/20/01, we pointed out the February 2001 sales tax collections showed a healthy 9.46% increase inside the City of Austin. At the time, we surmised the January numbers were "a blip, not the beginning of a downturn trend." It may not be a downturn trend, but now it is **starting to swing back and forth**.

Well, you say, folks were paying their income taxes in April and didn't have the extra cash to head to the malls. Good theory, but that doesn't take into account these are comparisons to the same month in the previous year, when taxes were also due. No, any way you cut it, **this is an indicator of a softening in the Austin economy**.

But it's not pervasive. A close analysis of the State Comptroller's report released this week shows **Austin's sales slide is not area-wide**. Williamson County's sales tax collections were up 2.54% in April (although the City of Round Rock's collections were down 1.86%). Bastrop County (+2.62%), Caldwell County (+7.59%) and Hays County (+17.88%) were all up as well.

Did Austin and Travis County swing back into the positive column in May? We won't know until 7/13/01 when the May sales tax collections are reported. For now, you can look for an **anticipated uptick in retail sales in July** when the feds start mailing those income tax checks. As we reported last week, that momentum should carry throughout the summer. Stay tuned.

**The normal method of reporting office space vacancy rates in the Austin area may be a bit deceiving. At last report, the citywide office vacancy rate was 8.9%. Not bad. But, when you factor in the *sublease* space that is available, the vacancy rate climbs quickly to 13%. And it's probably not going to stop there.**

By continuing to factor in sublease space, the overall office vacancy rate *could* (you need to underline *could*) reach 22% by March 2002, according to Mike **Buls** of Buls/Hodge Consulting, who tracks sublease space for the brokerage community. "My current view of the office market is that it is continuing to soften," Buls said.

What's the size of the sublease market? What does it look like? In what part of town can you find the most sublease availability? First of all, according to Buls, **there is more than 2.5 million sq.ft. of space available to sublet.** There are about 10 different available subleases greater than 25,000 sq.ft. About 68% of this space is located in the northwest – pushing the vacancy rate in the northwest to about 19% today.

Is subleasing a viable option for lower-priced office space? You bet. Buls points out sublease "**rates have declined on the average of \$3 per sq.ft. annually,** with higher declines in subleases with terms of less than two years."

So why does Buls think the sublease rate could increase so dramatically to push the overall office vacancy rate as high as 22%? As he puts it: "Based on the 2.7 million sq.ft. sublease space and the **3 million sq.ft. under construction** (of which 1.2 million sq.ft. is pre-leased), the timing of these projects could cause vacancy rates to reach 22% by March 2002."

But there are some mitigating factors which could keep rates from falling and could keep the vacancy rate from bumping up to that 22% number. "**Developers have been shutting down projects under construction,**" Buls notes. "In other words, it's better to have a land problem than a building problem."

Buls also points out that by the very nature of subleases, **building owners are still getting full rents** from their tenants that are offering some of their space on a sublease basis. There is no pressure on the building owners to lower rates for the small amount of remaining space they may have available for rent.

Therefore, the **real pressure to lower rates is on the sublessors.** Also, new construction coming on-line in the immediate future, will face pressure to offer rates that compete with the sublease offerings, Buls believes.

Bear in mind, when you see future office space vacancy listings, you need to realize the availability of subleases is not included in the tally (after all, sublease space is still generating good revenue for the landlord). But, if you are looking for **office space at below-market rental rates,** then you would be wise to check out the sublease market.

**There is a pervasive notion that Austin is a town where careers can be kicked off, jumpstarted, or even rejuvenated. This may account for the fact that 43% of Austin newcomers arrive each year *without a job*. And, as recently as last month, 98.1% of those newcomers have been quickly absorbed into the workforce.**

How many newcomers are we talking about? **“The number of people who have come to Austin in the past ten years actually exceeds the entire population of the city in 1960,”** observes **Rob Balon**, CEO of The Benchmark Company. This information is incorporated in Benchmark’s recent survey called “Austin at The Crossroads.”

Who are these newcomers? “Of those roughly 300,000 people who have poured into the greater Austin area, **27% are working in the technology sector,**” said Balon. **“Fifty-nine percent are under the age of 34** and 55% have at least a college degree. Twenty-three percent of the people who’ve moved to Austin have returned a second time.”

So how are these young newcomers who came to Austin because of a “sense of possibility” reacting to the slowdown in the economy? “For many younger workers under age 34, this was the **first time any of them had witnessed the end of a business cycle in their adult lives**. They had seen the Austin area as a place where non-stop growth was almost assured,” said Balon. But now, 58% of tech workers said they knew someone who had been laid off this year and 43% said they were more concerned about job security than a year ago.

These job losses have focused more attention on the continuing escalation of what Benchmark terms the **“expectation deficit”** – that is, the percent of workers who say **the Austin area has not been what they expected it to be**. In the past four-year period that Benchmark has been tracking this data, the expectation deficit has grown from 5% to over 16%.

“In relative terms, 16% compared to other cities is still a fairly good number,” Balon says. “But, if the expectation deficit continues to rise to say, 30%, it will have a significant impact on **Austin’s ability to retain its best and brightest.**”

Balon says his research shows that one of the elements “driving” the growing expectation deficit is “an increased perception that Austin is suffering from gridlock: **too much traffic and too many infrastructure problems**. The infrastructure problems that Austin has experienced as a result of rapid growth are not uncommon among tech cities. However, according to the workers surveyed, **Austin companies have an ability to significantly reduce the gridlock.**”

More than 30% of the respondents surveyed suggested *flex time* and *staggered hours* as quick ways to reduce the traffic crunch. Other suggestions included increasing the number of workers who *telecommute* and designing better systems for mass transit (including light rail). “It’s clear from the research that **workers expect Central Texas companies to give the problem more than lip service**. They want to see some immediate solutions,” concludes Balon.

**If you would like to meet the President of Mexico, Vicente Fox, and showcase your business before a group of Mexican business leaders, then the Greater Austin Chamber of Commerce has a deal for you.** The dates of the mission to Mexico City are August 22-24, 2001.

The Chamber, in collaboration with the State of Texas-Mexico office, will be taking a few select companies interested in **exporting, forming strategic alliances**, or otherwise expanding their operations globally on this trade and investment mission. The Chamber promises “your company will be connected with specific matchmaking opportunities with Mexican businesses, share a booth with the Chamber at the ‘Invest In Texas Networking Forum,’ have access to all of the events and **participate in a meeting with President Fox** at the conclusion of the trip.”

Special discounts will be offered for the first few registrants and registration is limited. For more info, contact **Traci Solomon** at 512-322-5608 or e-mail [tsolomon@austinchamber.org](mailto:tsolomon@austinchamber.org).

**UTAustin has about 200 non-teaching positions it needs to fill and will host a job fair 7/21/01 to recruit a “diversely talented population” to fill a variety of jobs.** The 10am-3pm event at the Erwin Special Events Center will feature booths with reps from various departments describing opportunities for full-time and part-time employment. About 1,500 participated in a similar job fair at UTAustin in January and 22 applicants were hired on the spot. For info, contact **Patsy Julius** at UTAustin’s Human Resource Services, 512-471-3656 or 800-687-8086.

**CORRECTION:** Our 6/8/01 issue contained the sentence “We’re the envy of most of the nation’s metro areas, because we’ve been in the 2 percentile range since 1977.” It should have read: 1997.

**Dr. Louis Overholster** got his comeuppance after a disastrous, frustrating round of golf. He said angrily to his caddie: “You must be the worst caddie in the world!” The caddie calmly replied: “I don’t think so. That would be too much of a coincidence!”

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