

THE

Real Estate

AUSTIN LETTER

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P.O. Box 1905 / Austin, Texas 78767-1905 / 512-498-9495 / Fax 512-327-1976 / e-mail News@AustinLetter.com

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Dear Client:

In the past year, the Austin area has seen thousands of layoffs, companies have cut back, dot-com businesses have failed, unemployment is up, commercial and residential real estate values/prices have gone through the roof, and stock portfolios and 401k's have shriveled beyond recognition. So, what's in the economic future for the Silicon Hills of Austin?

Now is a good time to remember the old adage that "everything is relative." (When humorist W.C. Fields was asked, "How's your wife?" he replied, "Compared to whom?") **Where we are today compared to last year is – down. Where we are today compared to the late 1980s is – up.** While that may be little comfort to those who are hurting financially, it is still a valid comparison. Especially when you look at our economic underpinnings.

Most of the economic woes we're suffering today are the result of the Austin area's remarkable successes in the New Economy. The high speed pace of high tech development has been excellent for our overall economic well being. It still is, but it's pausing to catch its breath. But, remember, our **solid infrastructure of government and education jobs has not been hammered by the high tech slowdown.** This is the bedrock that provides stability unmatched by many cities that are high tech centers.

With the twin towers of government and education in sound shape, what about Austin's high tech future? According to **Mark Dotzour**, chief economist for the Real Estate Center at Texas A&M, Austin will continue to be an **attractive location for technology firms because of its skilled workforce and relatively inexpensive real estate.** Wait a minute. Did he say *relatively inexpensive real estate*? Yes, and there's that word "relative" again.

"While Austin office rents may seem pricey at \$30 to \$35 per square foot, **this is a bargain compared to San Francisco at \$74, San Jose at \$68 and Boston at \$46,**" says Dotzour, pointing to other technology centers. It's all relative.

What about *home* prices? Austin home prices have increased substantially in recent years, but **they are still attractive compared with prices in the Silicon Valley.** He says homes in West Austin range in price from \$160 to \$260 per square foot and new homes in the San Jose area sell for \$300 to \$500 per square foot. These are choices high tech companies must make for future planning – and the Silicon Hills of Austin are in great shape, *relatively* speaking.

“In the wake of last week’s megamerger news, at least one thing is perfectly clear: Dell Computer has become the scourge of the PC Industry.” This acknowledgement came just days ago from an influential Silicon Valley tech writer who, less than two years ago, referred to Michael Dell’s projections as part of a “megalomaniacal fantasy.”

The *San Francisco Chronicle*’s **Henry Norr**, who has long written about the high tech surge from his Silicon Valley vantage point, grudgingly acknowledged what we’ve been telling you for sometime now. He’s finally climbed aboard the late train in recognizing Dell’s dominance now – and in the future. Here’s how he phrases it:

“Everyone else in the business is reeling from the combined effects of sagging demand and the scorched-earth price war Dell began this spring. But, **Dell just keeps gaining ground, and I don’t see anything on the horizon that’s likely to slow it down** – certainly not the tag team of **Carly Fiorina** (Hewlett-Packard’s CEO) and **Michael Capellas** (CEO of Compaq).

“In fact, a **market share of 40% no longer looks quite so much like the megalomaniacal fantasy** I thought it was when **Michael Dell**, the Round Rock, Texas company’s founder and chief executive officer, began talking about that target a year or two back.

“And with its largest competitors on the ropes – not just Compaq and Hewlett-Packard’s PC business, but also Gateway and the PC part of IBM, for starters – **Dell appears to be in a position of pick off a lot of their customers over the next year or two**. As Dell said last week, ‘Our teams will be in full account acquisition mode’.”

Norr, apparently is losing some of the smugness, which permeates some Silicon Valley folks as they look at upstart competitors here in the Silicon Hills. **“The most amazing part of this story is that Dell is managing to make money**, sort of, despite the industry downturn and the price war,” Norr noted. **“Dell’s competitors can’t make money on PCs even on an operating basis.”** He further pointed out that Dell Computer **“accounted for virtually all of the computer-systems industry’s operating profits”** during the (second) quarter.”

Norr, still somewhat grudgingly, tried to figure out how Dell does it. “Not by technical innovation, that’s for sure,” he said. **“Dell is the quintessential box-builder** – it generally makes pretty decent PC’s, but they’re just that, conventional Wintel boxes loaded with the latest industry-standard technology and nothing else. **Dell just manages to build, distribute and support these products more efficiently than anyone else.”**

The influential writer admitted he didn’t know much about Dell Computer and its people. So he talked to **industry analysts**. Let’s review what the analysts said about Austin area’s largest private employer that is so important, and vital, for the future of Austin’s economy.

“They know what they’re going to do and they do it.” That’s what Andrew Neff of Bear Stearns said about Dell Computer as his company raised the recommendation on Dell’s stock from **“attractive” to “buy” – his firm’s most positive rating.** Neff was responding to the *San Francisco Chronicle*’s columnist, **Henry Norr**, who is just now acknowledging what many of us in the Austin area have felt for a long time – that Dell will emerge as the dominant PC provider when all the dust raised by the economic slowdown, and fierce competition, settles.

Neff credited **Michael Dell** and his board for bringing in new top-tier managers with the skills the company has required at different stages in its growth. “At the competitors, people tend to stay on forever,” he said. As for whether Dell should follow the Hewlett-Packard/Compaq merger with an acquisition of its own, Neff had a strong opinion.

He said there is no point in Dell buying Gateway or IBM’s direct sales operation. As Neff put it: **“Why distract yourself when you don’t have to? For Dell, the Number One priority has to be to take advantage of the dislocation that could occur as a result of the Compaq/HP merger”** – which is exactly what Michael Dell said he plans to do.

A research fellow at Gartner Dataquest, **Martin Reynolds**, attributed Dell’s success largely to its management’s focus on cash flow and velocity: **“Dell concentrates on quick turnover**, even if it has to lower prices and margins to keep sales growing. Its build-to-order manufacturing system and minimal inventory of components lets it recoup its costs in a hurry – sometimes it collects from customers even before it pays suppliers. **They’ve turned cash flow into an aggressive weapon like we’ve never seen before.** It means there’s no cash limit on the company’s growth – the more they sell, the more cash they raise.”

Norr pointed out what has long been the case: Dell’s most obvious advantage is selling directly to customers, over the phone and online. “Michael Dell, who founded the company in his college dorm room 17 years ago and remains its chairman and chief executive officer (**the longest-tenured reign in the industry, by a long shot**) isn’t the only entrepreneur who thought of what’s known in the industry as the ‘direct model’. But you’ve got to give him credit for sticking to his vision,” Norr acknowledged.

“For years most industry pundits, not to mention competitors, insisted that big **business wouldn’t dream of buying PCs over the phone from an upstart in Texas.** Then they said the same about notebooks, and then servers. Even after reality **proved all that wrong**, many argued that the model wouldn’t work with **consumers**, who account for a growing share of PC sales. Now that theory is going up in smoke, too,” Norr concluded.

It’s significant an influential Silicon Valley writer is now, belatedly, recognizing Dell’s impact. **He’s listened to, and respected, throughout the high-tech community on the West Coast.** That’s why we wanted to devote this much space to that acknowledgement.

Let's pause a moment, to reflect on the unspeakable acts of terrorism inflicted on our fellow Americans this week.

While the physical damage did not occur in the Austin area, the emotional impact is felt by all of us here — as well as in all peace-loving, humane, corners of this globe. But, those of us in the Austin area, moreso than in other locations, **know the key US players who will be making the decisions affecting a major war waged by the US against terrorism.** Folks who just last year were our neighbors here in Austin, are involved in the highest level of decision making in this tense time.

Obviously, President **George W. Bush** is where the buck stops. A year ago, he was making decisions from his home in downtown Austin about state government issues. Now, **aided and assisted by many former Austinites**, he'll be making decisions about sending young men and women into war.

His closest advisors from Austin are **Karl Rove** and **Karen Hughes**. There are no others in the administration who are closer to the President. **Joe Allbaugh**, Bush's chief of staff while he was governor, is leading the federal disaster relief and cleanup effort as head of the Federal Emergency Management Agency.

Additionally, former Austinites **Ari Fleischer** and **Scott McClellan** are #1 and #2 in the White House communications and press liaison office. And, there are many other former Austinites working in the White House and at high levels in other federal agencies and departments.

These former neighbors of ours are carrying a heavy burden these days, working long, tension-filled hours. They deserve our strongest support, no matter our political beliefs.

During this time of national tragedy, Dr. **Louis Overholster** likes to remember that **Abraham Lincoln** said "the Declaration of Independence gave liberty not alone to the people of this country, but hope to all the world for all future time."

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