

THE

Neal Spelce

AUSTIN LETTER

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Dear Client:

It's hard to overestimate the importance of the housing industry to an area's economy. All by itself, housing represents about 14% of any economy. Then when you add peripheral businesses, such as furniture, appliances and landscaping, it zooms up to about 20% of the annual production of goods and services. So, let's analyze Austin's housing market prospects.

First of all, as you know, **one of the biggest determinants of the health of the housing industry is the interest rate.** Given that, you need to realize interest rates are usually *peaking* at the beginning of most recessions. This is decidedly *not* the case now. In fact, interest rates are low — and probably going lower.

It's entirely possible the Fed will lower short-term interest rates a quarter percentage point at each of its next two meetings in November and December. Those steps could trigger lower mortgage rates. The National Association of Homebuilders predicts **30-year, fixed-rate mortgage rates could dip to a low of 6.6%** by the end of the year and **adjustable rate financing (ARMs) could dip to 5%**. Talk about an impetus for home sales!

And it's not just home sales that would benefit. If these rates kick in during November and December, they would continue to motivate homeowners to *refinance* existing mortgages — as we end 2001 and begin 2002. This means **families with lower monthly mortgage payments will have more disposable cash to spend**, further stimulating our economy — especially the retail sector.

There is no question the Austin area economy — and that of the entire nation — has taken a hit this year. But, when you look at the underlying strengths of this economy, you see **prosperity could return in less than nine months.** This isn't like the recession of fifteen years ago (more on that in a moment). Even though there have been highly-publicized layoffs, **the jobless rate is low enough (below 5%) for economists to claim there is "full employment."**

That's not all. **Inflation is next to nothing.** Zero, zip. Nil, nada. And, don't forget the more than **\$100 billion in tax cuts** which will continue to help as they kick in. When we talk about low interest rates helping the housing industry, they also **help individuals and businesses as they borrow money** for various needs. Next year, 2002, should see a gradual return to better times for homeowners, homebuilders, Realtors and the economy overall. Hang in there.

Let's put this economic downturn in perspective. It was announced this week the national economy officially contracted in the third quarter. It's also expected to decline in the fourth quarter. Two declining quarters in a row make a recession. So, how do we in the Austin area differ now from the recession of the late 1980s as the decade of the 1990s began?

We mentioned low inflation in the previous story, so let's pick up now with **banking institutions. They are in solid shape.** Not like fifteen years ago when financial institution failures were almost the norm. **Real estate values have not plummeted,** pushing financial institutions to require mortgage holders to come up with additional collateral.

Back then, those factors triggered a domino effect, forcing property owners to default. This, in turn, put undervalued assets on S&L's and bank's books, damaging and **collapsing many financial institutions,** and it caused many property owners to seek **bankruptcy protection.** Today, financial institutions are strong and property values are not declining precipitously.

Interest rates. It was July 1990, well into the downturn, before the Fed started cutting the rate it charges banks for funds (the Fed Funds Rate) from 8.25% to 8%. **This time around, the Fed started chopping those rates long before the start of the recession.** The Fed Fund Rate now stands at 2.5%, very near the lowest it's been in forty years.

Oil Prices. Have you driven around North Austin during the past week? **Gasoline prices have dipped below a buck a gallon.** That's right, less than a dollar a gallon. During the Gulf War, oil prices shot up to about \$40 a barrel and gasoline prices went through the roof, further straining consumer's budgets. It's dramatically different today. Oil prices are now in the \$20 a barrel range.

Unemployment. As we mentioned earlier, there is still "full employment" in the Austin area, the state of Texas and the nation as a whole. This was not true in the late 80s and early 90s. And, as we've reported in recent editions of this newsletter, **many sectors of our local economy are actually growing – adding jobs –** during this downturn.

There are other comparisons we can draw for you. Yes, we have more office space available in Austin now than we had last year and many tenants are subletting space to cut their costs. However, **in the late 80s, Austin had the dubious distinction of having the highest office vacancy rate in the nation.** We're not even close to those dark days today. The same is true with residential real estate. Lots of homes were going begging on the market in the late 80s; financial institutions were selling foreclosed real estate then. Not now. The only homes taking a long time to sell are million dollar mansions. Others are selling at a steady pace.

By the end of the year, we will be proclaimed to be officially in a recession. But, **this is a very mild recession** where we are coming down from a very high plateau. Nothing like the late 80s.

Yes, the 5-county Austin-San Marcos metro area's September unemployment zoomed up to 4.6% from only 2.0% a year ago. But, did you know there are cities in our metro area, and other cities in our trade area just to the west, with unemployment in the 2% range right now?

If you live and/or work in certain small, but vibrant, towns here in Central Texas, you're probably wondering what's with all this fuss about folks who are out of work. **Each of seven cities, all within an easy drive of Austin – an hour at most – has September unemployment stats in the 2% range.** Buda (2.3%), Lakeway (2.6%), Leander (2.6%) Dripping Springs (2.0%), Fredericksburg (2.4%), Blanco (2.9%) and Marble Falls (2.8%) are not feeling the effects of the upheaval in jobs. You don't hear much about these thriving communities.

But, if those cities are racking up impressive numbers, then there obviously are others with a **more troubling situation.** Taylor (7.0%), Bastrop (6.4%) and Killeen (7.0%) come to mind. And there are other Central Texas communities with higher-than-average tallies in September – Elgin (5.9%), Cedar Park (5.6%), Lockhart (5.7%), Kyle (5.4%), Canyon Lake (5.2%) and Copperas Cove (5.0%).

The bigger cities of Austin (5.2%) and San Marcos (5.2%) are in this over 5% range as well. This is important because, as we told you earlier, **under 5% is considered to be full employment.** When you start ooching higher than 5%, then those on the unemployed rolls start to make an impact.

It's important to understand how this closely-knit Central Texas area **varies from city to city.** Round Rock is doing quite well at 3.8% unemployment. So is New Braunfels (3.7%) and Kerrville (3.7%). Llano (4.5%) is closest to the average and Georgetown is right at the full employment level – 5%. Keep this variance in mind as you see the single number released each month for the Austin metro area unemployment. It's an uneven picture here in Central Texas.

An Austin operation is providing free training for those lacking computer skills. Despite our high tech emphasis, there are many still without the necessary computer skills for job advancement. Who is lacking in key skills? Those who've been out of the job market for a while, a worker forced to change jobs and job seekers making a career change are just a few.

Austin Free-Net is a non-profit corporation that provides public access to the Internet and emerging technologies and computer resources. **Any Austin resident** can visit any of 35 sites to use a computer and the Internet free of charge. Volunteers and site staff also offer the opportunity for people to **develop their computer skills** through free training classes.

Austin Free-Net is a **partnership between private business, government agencies and non-profits.** The 35 sites are located in public libraries, churches, affordable housing developments, job training centers and City of Austin facilities.

Site Selection magazine recently surveyed **100 corporate execs to rank the best labor markets in the US. Austin made the Top Ten, locking in the #7 slot.**

The execs were quizzed on what they thought about **labor quality, labor availability, and the breadth of the work force training resources** available. Labor is right at the top of the list for all companies seeking a location for their next operation or if they're thinking about moving operations. Their Top Ten, in order: Dallas, New York City, Boston, Atlanta, Chicago, San Francisco, Austin, Raleigh-Durham, San Jose and Washington, DC. This how the execs *perceive* these cities, but, as you know, perception is oftentimes much stronger than reality.

In spite of the shutdown of air operations following the September 11th terrorist attack, international air cargo shipments in and out of Austin-Bergstrom International Airport (ABIA) showed a major increase during the month of September.

Passenger traffic, as we reported 11/26/01, was down dramatically (-34%) – as expected – following the plane hijackings that killed thousands in the northeast. **General Aviation operations at ABIA fell by the same percentage.** And overall air cargo operations took a dive, by 42%, from September 2000.

But, inexplicably, *international* air cargo went counter to the trend. **Cargo shipments to and from foreign destinations totaled 1.1 million pounds for September – up more than 150% over September a year ago.** And, for the year, *international* air cargo is up more than 300% compared to the same time frame last year. We'll keep an eye on the October numbers for you. They are usually not reported until the 25th of the following month.

Dr. Louis Overholster has a recommendation for parents of very active young children. “When the kids become wild and unruly, you should use a nice safe playpen. Then, when they've finally calmed down, you can simply climb out of the pen!”

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Sincerely



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