

THE

*Paul Spelce*

# AUSTIN LETTER

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Dear Client:

**The battle for one of the most important elected offices in Texas is being waged right now. The votes won't be cast until two months after the November 5, 2002 General Election, and you won't get to cast a ballot.** But, you will be directly affected by its outcome, as the seat being filled is one of Texas's most powerful positions — Speaker of the Texas House.

Texas' current Speaker, **Pete Laney**, a Democrat, wants to be re-elected to the job. But, **this run for the Speakership is going to be the toughest the veteran politico has faced**. He has a lot of allies, a lot of support and strong financial backing, but Republicans have built some steep hills for him to climb – hoping to replace him with a Republican Speaker for the first time in a century.

First of all, the Republican redistricting plan has finally been adopted and **it jiggered the boundaries of Laney's district so that it leans more Republican**. Laney has had pretty much of a free ride for election to the House in the past. If Laney climbs that re-election hill, then he has to convince a majority of the newly elected 150-member House to vote for him for Speaker.

That's an even more difficult climb because the same Republican redistricting plan appears to have it set up so that as many as **88 Republicans could be elected to the House – easily a majority**. Laney has been elected in the past with support from both Republicans and Democrats. Since the Reps have not had a majority, there hasn't been a major GOP push to oust him — until now.

And, many of Laney's lieutenants in the House – strong committee chairs – are not seeking re-election, so the **Speaker is losing a lot of field generals** (not to mention their votes) in his campaign battle to retain the presiding officer's post.

Laney keeps one of the lowest public profiles of any powerful politico. And, he rarely speaks publicly about his plans. However, it's generally conceded that – at this time – Laney has many more “pledges” from House members than any other candidate. The Republicans – **Warren Chisum, Tom Craddick, Pat Haggerty, Ed Kuempel, Brian McCall, “Buddy” West** – are hustling other GOP members for pledges. Craddick is pegged as the front-runner, but the GOPers are still fragmented. **You can't vote on the next Speaker**, but you should ask House candidates if they've already pledged their Speaker vote – and, if so, for whom.

**To put the current office market vacancy situation into perspective, consider this: “The last time we were at 80% occupancy was in the early 90’s, like 1990, and it took us ten years to get from 80% up to 95%. Now we’ve gone from 95% back down to 80% in roughly a year.”**

That perspective is courtesy of **Charles Heimsath** who, as president of Capitol Market Research, has been tracking commercial real estate in the Austin area for decades. He describes **the drop in occupancy in the last few months as “precipitous.”** But he’s also quick to point out today’s market is very different from what it was in the mid-to-late 1980s.

Heimsath notes Austin has a much **more diverse economy** now and there are **fewer office building starts** today than there were in the midst of the real estate recession of a dozen years ago. There are many other differences — chief among them is the strength of our financial institutions today.

But the fact remains, as we’ve chronicled for you during this year, the high-priced, tight landlord’s office market in Austin has become more of a tenant’s market. And the trend is still heading in that direction. **The occupancy drop hasn’t bottomed out.** We’ll watch it for you so you can get the first word when it appears to have made a turnaround.

**Don’t you know the execs at Dell Computer in Round Rock are sitting around having a great time as they watch the problems swirling around their arch-competitor, Compaq Computer? Dell benefits from almost any option the Houston-based company chooses — or has thrust upon it.** And, Dell is moving aggressively.

Before the September announcement of the proposed merger between Compaq and Hewlett-Packard, analysts were suggesting **H-P pull out of the PC business** (see our 9/7/01 issue, where we told you “combining two struggling companies don’t necessarily make a stronger company”). **The merger is now on very shaky ground,** because the Packard family foundation and others representing about 18% of H-P’s ownership say they’ll vote against the merger.

As a result, analysts this week are suggesting **Compaq should discontinue its PC line** if the merger collapses. Is that music to Dell exec’s ears, or what? But, all these questions, problems and analysis could have a much more disturbing impact. **Compaq now must deal with a perception that it is a failing company.** This is very serious. If Compaq doesn’t face up to this perception directly (remember, perceptions can be just as strong as reality), **customers will stop buying Compaq products** because they think the company won’t be around to support them.

As we reported 9/14/01 “For Dell, the Number One priority has to be to take advantage of the dislocation that could occur as a result of the Compaq/H-P merger, which is exactly what **Michael Dell** said he plans to do.”

**If you're concerned about federal tax policy being enacted on Internet transactions, you can circle 11/3/03 on your calendar. The tax moratorium has been extended to that date.**

The moratorium **prohibits taxes on Internet access and multiple taxes on Internet transactions**. The moratorium expired 10/21/01, but the USHouse and USSenate extended the moratorium in a bill signed by President **George W. Bush** just a few weeks ago. By the way, the bill also allows eleven states, including Texas, to continue charging access fees that were enacted prior to 1998.

**If you were driving in parts of North Austin this week, your eyes may have popped at seeing signs advertising gasoline at 89-cents a gallon. It's been a long, long time since prices have dipped this low. So, who do you thank for these lower prices? How about the Russians.**

It's not just gasoline prices that are dropping to low levels. **Diesel fuel** prices are still dropping. And **heating oil** (so important to our neighbors in the colder sections of the US worried about heating their homes this winter) is also going down in price. **Natural gas** prices are going down as well. And the experts upon whom we rely think **this trend will continue** at least through the winter.

What's happening is that **overseas oil producers are continuing to flood the market**, in spite of weak demand. But, what about OPEC? The middle eastern oil producing countries have usually kept a tight hand on the oil spigot so they could control the prices. But here, we have oil gushing — seemingly uncontrolled.

Overproduction is being triggered by the Russians. **Russian oil exports are booming**. In fact, Russia is flooding the oil market in such great volume that Russia is now second only to Saudi Arabia in oil exports. As a result, OPEC is pumping and pumping — just to keep up with the Russians. And the Russians aren't blinking.

As long as **Russia keeps up this capitalistic (!) competition**, you can expect prices of oil and oil derivatives to stay low. Kind of interesting, isn't it?

**Speaking of Russia, its booming oil business is helping keep its economy afloat during a difficult time. It's newfound friendship with the West, particularly the US, may help offset the fact that most factories remain inefficient there. But, you need to be concerned about Japan.**

Japan is a major market for many Austin companies and, frankly, Japan's economy is a basket case. The formally strong economic giant is in its 4<sup>th</sup> recession in the past ten years. Keep an eye on Japan. It may be years, 2003 at the earliest, before it returns to economic stability.

**Despite the fact that every airline in the US is down by every conceivable measure, one Texas-based carrier has moved up the list of the nation's largest carriers. Not because of its growth, but because of the steadiness it has shown while other carriers are in decline.**

Southwest Airlines, the dominant airline in the Austin market, has leapfrogged past USAirways to become the nation's **sixth largest carrier in terms capacity and passenger traffic**. The rankings, by passenger traffic, in November: American is #1, followed by United, Delta, Northwest, Continental, Southwest, USAirways and America West. And, if you measure **domestic passenger miles, Southwest now ranks #4 on the list.**

What's happened is pretty clear. As we've reported to you, **the other airlines reduced their capacity**. American cut available seat miles by 26%, United by more than 29%, Delta by 19%, Northwest and Continental by just over 17%, USAirways and America West by more than 23%. What did Southwest do? Its reduction was barely more than 5%.

These percentages and rankings are important because they reflect a dynamic that is taking place in the midst of a severe airline crisis – **Southwest is capturing market share right and left, while the others are struggling to keep flying with the hope of a return to profitability**. Make no mistake, Southwest isn't growing. Like the others, it is still feeling the effects of the September 11<sup>th</sup> terrorism attack. But, since it has shrunk much less than its competitors, it is gaining market share.

This situation brings to mind Dr. **Louis Overholster's** story about two guys in the woods who come face to face with a bear. One starts putting on his running shoes while the other tells him he's crazy, that he can't outrun a bear. The reply: **"I don't have to outrun the bear, just you!"** Southwest is facing the same bear as the other airlines, but is outrunning the other guys.

As has been customary for our 22 years of publishing this newsletter, we're taking off the last two weeks of the year. Our next edition will be dated 1/4/02. In light of this year's tragedies, we wish you and your family a season of unparalleled closeness and generosity.

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Sincerely



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