THE Neal Spelce AUSTIN LETTER

www.AustinLetter.com

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Dear Client:

For almost two years we've kept you ahead of the curve on the declining Austin *office* market (for instance, rental rates are now back to where they were at year-end 1999). But, what about *retail* space? Now that's a whole other story.

At mid-year 2002, the office market has dropped to an 85% direct occupancy level. And, industrial space is even lower – 81% occupancy. But retail? **Retail is recording an overall 95% occupancy rate**. Even with the dot-com downturn and other economic problems, the retail real estate market has remained stable. Retail rental rates have remained flat and the stability in rates has much to do with the lack of oversupply.

What's going on here? "Central Texans are still shopping for consumer items, although they are more cost – and value – conscious," observed **Eric DeJernett**, Retail Specialist with NAI Commercial Industrial Properties Company (NAI CIP), the company that provide these figures to us.

Does this cost/value retail situation drive development activity? You bet. "We are seeing ongoing development activity from Wal-Mart, Target, Kohl's, Home Depot, Lowe's, H-E-B, Walgreen's and other retailers who **deliver quality products at a competitive price**," he said. "Demand for existing retail space and new, retail development is still very strong for quality retail properties."

This obviously means a strong demand for future retail *land*, particularly sites located at major intersections. But, guess what? Few good developable sites are still available in Austin. So what's happening? "Developers and investors now have to look to future roadway construction for good sites," says **Joyce Jane Weedman**, Land Specialist at NAI CIP. "We are focusing on SH130, SH45 and the MoPac and Parmer Lane extensions, as well as neighboring communities. IH35 remains in high demand, with developers always looking for the next ring out."

Weedman is really optimistic. "We are encouraged by the long-term demand for well-located mixed-use development sites. **Developers believe that the market will be extremely strong three to four years out**, and they are positioning themselves for that time frame," she noted.

There's also another major market force at work here. Check out the next item.

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Investment property is a hot commodity in Austin right now. **Everything – good and bad – that's happening right now** (**nationally and in Austin**) **seems to be working to make investment properties very attractive**.

Current changes in supply and demand have had no overall dampening effect on the investment real estate market in Austin. Why? Well, as supply has exceeded demand, interest rates have fallen. And, as the rental market has softened, **investors are increasingly seeing this as an opportunity to buy**.

Owners of well-leased properties have been able to sell at prices based on lower "cap rates," while buyers have the ability to finance at historically low interest rates. "We are seeing declining cap rates on properties leased to high-credit tenants," says **Fred Higgins**, Investment Specialist at NAI Commercial Industrial Properties (NAI CIP).

It doesn't stop there. "Multi-tenant properties that are not perceived as having leases with rental rates high above current market are also in demand," Higgins pointed out. "**Because at today's low interest rates**, **buyers are able to achieve attractive positive cash flow leverage**."

All this is happening as the doom-and-gloom headlines blare at you each day from Wall Street. "With declining returns on financial instruments such as stocks, **otherwise average real estate returns appear stellar by comparison**," concludes Higgins.

Even as we told you in our first item about developers and investors looking at new roadways for future retail sites, **a relatively new and growing environmental organization is also targeting those same roadways**. **The group is called Scenic Austin and it's the local affiliate of a statewide group called Scenic Texas and the national group**, **Scenic America**.

The state group's 2003 legislative objectives are **no new billboards** in the state, and it is lobbying for 1% of TxDOT's road construction budget to be set aside for **landscaping** of highways. In 2001, the group was successful in getting legislation that insured there would be no new billboards on 13 Texas roads, including US290 between the western city limits of Austin and the eastern city limits of Fredericksburg.

Scenic Austin has other specific goals such as "protection of new Central Texas highways from visual blight, in particular SH130." Other targets: "**Protect all Central Texas roadways from new billboard construction** — in particular US71, US281, SH16 south of Kerrville, SH29 and SH46." To find out more about Scenic Austin (a list of its local leadership, goals, etc.), you can go to www.ScenicAustin.org. Once there, Scenic Austin provides a link so you can check out the state and national organizations.

"When the *Statesman* says this deal is 'excellent,' or some such, they're nuts. When SOS urges you to rally at the Council to save Barton Springs, they're lying." This unexpected quote from an opinion leader in the environmental community signifies the continuing changes taking place in Austin politics.

The editor of the alternative weekly *The Austin Chronicle*, **Louis Black**, wrote those words about the pending Austin City Council action **to approve a deal with Stratus Properties** for a scaled-back development in Southwest Austin. The past few weeks were reminiscent of old Austin, as hundreds, organized by SOS, packed council chambers to argue about the environmental harm that could come from the deal.

Black's newspaper has been the (sometimes strident) voice of the environmental community for decades. But, listen to Black now: "Wrap yourself in seaweed, read a dozen poems and sing every chorus of 'Barton Springs Forever,' it isn't going to save the Springs. **Stratus can develop its land**; **the question is how much and how densely**." This is a sea change.

"The tools are compromise, which SOS hates; land swaps, which SOS doesn't trust; purchasing land, which isn't going to garner a lot of support in these economically strained times; or **negotiating to preserve as much land as possible**," says Black. Negotiating. That's where Black is coming down now.

"People have certain rights in regard to their land," he notes. "There is an enormous amount of land that impacts the Aquifer and the Springs. The development is happening and will continue to happen. **Silly rallying cries to the masses to get the council to stop it won't work**. The council can't stop it. There isn't a simple way to say no."

"The problem isn't evil developers and corrupt politicians," says Black. "The problem is that people want to buy houses. The problem is that landholders have rights. The problem is that buildings and roads have a negative impact on nature." So what does Black, coming from the left, suggest? "**This is a time for a sad maturity**. **Let us save what we can save**."

How? "Let us build coalitions among developers, environmentalists, and politicians that will work," he urges. "I'm not defending this deal, but let's not naively attack. **It is time to respect the negotiators**, **stop the polemical speeches**, **and begin sincere**, **intelligent negotiation**." This is the direction former SOS leaders **Robin Rather** and **Brigid Shea** have been heading. But, **Bill Bunch** and **Kirk Mitchell**, the current SOS leaders, are more confrontational.

Now don't get the idea the *Chronicle* has lost its edge. In the same issue where Black penned his words, his City Editor **Mike Clark-Madison** wrote a column under the headline "**Daryl Slusher Is Dead**. **You Can Stop Yelling At Him Now**." Slusher was a former *Chronicle* writer who was elected to the City Council as a champion of environmental issues. Slusher voted for the Stratus compromise and has now earned the enmity of his former enviro supporters.

Several million dollars have already been sunk into a new movie version of "The Alamo," including upfront script costs and a big Alamo set being constructed just outside Austin. But, the project is on hold. Here's the *real* reason why.

It's coming down to a battle of bucks inside Walt Disney Co. "It will be either a $135 million, R-rated epic that reunites a high-priced Academy Award-winning team, or a PG-13 film that costs half as much and is directed by a little-known up-and-comer," according to *The Wall Street Journal*. These options underlie a standoff between **Ron Howard** and Disney.

The big budget blockbuster re-telling of "The Alamo" would be directed by Howard, produced by Howard and **Brian Grazer**, and starring **Russell Crowe**, reuniting the team that ran away with the Oscars last year for "A Beautiful Mind." But, Disney doesn't like the cost and the violence quotient in Howard's "Alamo."

There's some squabbling over the script, but money's at the bottom line. Howard is demanding, as most A-List Directors do, his **hefty salary** (**$10 million**) **plus a cut of box office and other revenue**. The studio balked at the percentage part of the deal and Howard cut off negotiations. The studio's alternative is to hire director **John Lee Hancock**, who worked here in the Austin area with Disney's hit, "The Rookie," to better ensure a profit for the battered studio.

There's no doubt a mega-budget R-rated (for violence) film is risky. There's enormous pressure on big publicly-held media companies like Disney to make a buck. And they worry that **paying out so much of a film's revenue to big names** (which help make it a blockbuster), **it's difficult to make a decent return on its investment – even if the movie is a big hit**. A decision will probably be made soon. But, whether Disney will suck it up, pay the big bucks and hold its corporate breath, or scale it back and shelve the Maalox, the movie will likely be made here in the Austin area. We'll just have to wait and see.

Dr. Louis Overholster admired the most stunning diamond ring he'd ever seen. His patient said it was the famous Hannigan diamond, but it came with a curse. "What's the curse?" "Mr. Hannigan!"

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Sincerely

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