

THE

Neal Spelce

AUSTIN LETTER

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Dear Client:

Some federal transportation dollars for the Austin area may be unlocked when the US Congress reconvenes after Labor Day, in a session that is sure to be rife with politics prior to the November Congressional elections.

Keep your eye on the US House of Representatives. That's where the huge \$33.2 billion transportation bill for Fiscal 2003 sits, after passing the US Senate. Texas Senator **Kay Bailey Hutchison**, a member of the Senate Appropriations Committee and the chair of its Transportation Subcommittee, was instrumental in seeing that **approximately \$11 million for Capital Metro** was included in the bill that, incidentally, was nearly \$9 billion more than requested by President **George W. Bush** in his 2002 budget.

Eleven million dollars is literally pennies in a \$33.2 billion spending pot. But, it will mean a lot to Capital Metro. CapMetro says it will use the money for various transportation initiatives in the Austin area, including **hybrid electric buses and new park and ride facilities**. And, the money would be available ASAP because the Fed's fiscal year begins this fall.

It's up to Central Texas Congressmen **Lloyd Doggett** (D) and **Lamar Smith** (R) now. They are sponsoring this funding request in the US House. This will be an interesting test for the two of them because, as we mentioned, politics will play a much heavier role than normal during these next two months of legislative maneuvering — as every member of the US House is standing for re-election November 5th. Also, to give you an idea of the relative importance of this effort as far as Capital Metro is concerned, all you have to know is that the pending \$11 million appropriation compares to last year's allocation of \$1.75 million.

Federal money has already been made available to partly finance design and construction of the Central Texas Turnpike Project. This is a toll highway facility comprised of Loop1/MoPac, SH45 and SH130.

The money, in the form of a loan request from the Texas Transportation Commission to the US Department of Transportation, is **only a fraction of the funds needed** to complete the estimated \$3.2 billion project. But, it will go a long way toward kicking it off properly.

When you go back and carefully analyze one of Austin's economic benchmarks – airline passenger traffic – you find it was in June of 2001 that passenger traffic first fell below that of the previous year.

Prior to that time, almost month-after-month, new records were being set as more business travelers flew into and out of Austin, and leisure travelers with bucks in their jeans were racking up those frequent flier miles. So the **decline was evident months before 9/11/01**, when the bottom dropped out of air travel everywhere.

Since that time, the level of passenger traffic at Austin-Bergstrom International Airport has been **below that recorded in 2000**. However, there may be significant progress before the end of the year.

Looking at the trend lines, it's almost certain that **September's passenger traffic will best that of last year** (when airlines scaled way back and travelers stayed home) – and remain above 2001's total through the end of the year. The key question is **will this economic indicator bounce back above the 2000 level and, once again, start setting traffic records**. We'll keep an eye on this for you.

The talk about a US "invasion" of Iraq (or as the administration likes to say "a change of regime in Iraq") is growing steadily louder. Even though there has also been growing criticism of such a move, most knowledgeable observers believe the US may be militarily involved in Iraq within the next six months – or possibly sooner. What will this mean for your business?

First of all, you know there is a minimal level of defense-related activity in the Central Texas area. Yes, we have the headquarters of the **National Guard located at Camp Mabry**, and the **world's largest military base – Fort Hood** – is just up IH35, near Killeen and Copperas Cove. But, there is not much other economic activity that is affected by military action.

What you can look for is a national economic impact that will filter down to Texas and the Austin area, because much of **our commerce nowadays is inextricably tied to the national economy**. If the military activity is of a short duration, economic growth will slow down. It will be even worse if hostilities continue for many months.

Think back to the Gulf War in 1991. If it was an indicator, consumers will become more cautious. They will spend less of their income in local retail outlets. Also, you can expect **big ticket purchases to slow** – such as investment in a home or a new car. And, some businesses will probably pull back on planned investments. **It could be similar to another downturn**. The risk is that it could tip the US into a recession. But, most economists are suggesting that growth in 2003 should be enough to withstand the impact. You need to watch this carefully.

In this football crazy town, many who read the Sunday edition, 8/25/02, of *The New York Times* probably focused on the front page of the sports section featuring a photo of Mack Brown and Chris Simms and the edition's pick of the Texas Longhorns to win the national championship, 1/3/03, in the Fiesta Bowl. But, on the front page of the *business section*, the same edition also featured some interesting insights about Austin's Michael Dell.

The generally favorable article, headlined "On A Roll, Dell Enters Uncharted Territory," contains some **interesting personal insight into Chairman/CEO Michael Dell's attitude and approach these days**. The article is too lengthy to capsule here, but it is recommended reading if you're interested in the future of Austin's largest private employer. However, let's focus here on the comments illuminating the 37-year-old computer whiz's personality.

The business writer, **Steve Lohr**, noted Dell "offered a matter-of-fact explanation for why his company was certain to **move inexorably beyond the desktop and corporate data centers, selling more large computers** and attacking the business stronghold of IBM, Hewlett-Packard and Sun Microsystems. And, as he does when things are going well, Mr. Dell peppered his comments with dry, caustic humor."

"At one point, he observed that **8 of the 10 largest corporations in the 2001 Fortune 500 bought Dell data-serving computers** – the machines that power corporate networks and the Internet. The two noncustomers, Mr. Dell added, were **IBM, an archrival, and Enron**. 'I just love that,' he said."

After quoting a number of nay-sayers who questioned whether Dell's PC manufacturing business model could be a winner in the mainstream corporate computing world of servers, storage and services, Lohr observed that "whenever Dell has entered a new market – notebooks, work stations or server computers – **rivals have predicted it would get its comeuppance**. They were wrong." "I've seen this movie before," Mr. Dell said. "Hey, order the popcorn. I'm going to enjoy it."

One analyst was quoted as saying that Dell is known as a "fast follower" in the industry. "Dell doesn't pioneer markets; it milks them," he claimed. Dell has been criticized for not spending as much on Research & Development as others. Dell says his company builds on the foundation laid by the \$8 billion that Microsoft and Intel spend on R&D, delivering tangible benefits to customers. What does Michael Dell think about the R&D criticism? "I think the **idea that our competitors have an advantage because they spend more on R&D is complete nonsense**," he said. Okay.

The *NYTimes* article made it seem like **Michael Dell is feeling his oats** a bit these days as his company becomes stronger, expands further and gets more power over rivals, while gaining more independence from partners. For instance, Dell was quoted as saying "We like Microsoft. But, we do things for the benefit of our customers and our shareholders. **If Microsoft doesn't like some of those things, they can go jump in the Pacific Ocean!**" Interesting insight.

Just as railroads were essential to commerce and economic vitality as we moved into the 20th Century, airlines are even more so here at the beginning of the 21st Century. That's why we need to keep a close eye on the health of the airlines that serve the Austin area, especially since three of them are headquartered in Texas.

Only one airline, **Dallas-based Southwest**, is profitable this year. It *posted a profit* of \$102 million in the 2nd quarter and has year-to-date earnings of \$124 million. And, as if to underscore its core operating model of efficiency, **Southwest is the only airline that has not made major layoffs or cutbacks** since the tragic 9/11 attack on the US a year ago. It's hard to overemphasize what this means for the airline industry as a whole – and for your future travel.

Look at the other airlines serving Austin. The nation's largest airline, **Fort Worth-based American**, lost \$495 million in the 2nd quarter and \$1.07 billion in the first half of 2002. **Houston-based Continental** lost \$139 million in the 2nd quarter, bringing its year-to-date losses to \$305 million.

The other major carriers serving Austin are also hemorrhaging money. **United Airlines** lost \$341 million in the 2nd quarter and its first half losses total \$851 million. **Delta**, the nation's third biggest carrier, lost \$186 million in the 2nd quarter and \$583 million for the year.

These five airlines have carried 83.9% of the Austin passengers so far this year. Interestingly, the profitable airline, Southwest, carried the lion's share – 36.4%, followed by American's 25.2%, Delta's 11.2% and Continental's 11.1%. You've seen the recent announcement that American will be dramatically modifying its hub-and-spoke airport concept to gain more operating efficiency — like Southwest. Look for more announcements like this from more airlines. Airline success is essential for Austin's success.

Dr. Louis Overholster says you have to feel sorry for the people involved with the lying and evasion and double-dealing of a corporate scandal: "I mean, where can they go next, short of running for Congress!"

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