

THE

Neal Spelce

# AUSTIN LETTER

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Dear Client:

**Texas is in the most enviable electricity position in the US. And it's not just because Texas, with its own, self-contained power grid, cannot be hit by cascading power outages from other states – as happened in the northeast late last week. No, it's even better.**

The Feds, Congress, every state in the northeast – even Canadian provinces – are all wringing their hands trying to figure out what to do in the wake of the largest electrical blackout in the nation's history. As well they should. **But who knows what solutions – and at what cost, to the industry and, ultimately, consumers – will emerge?** And how long will it take to implement whatever changes are recommended? Also, it's not just confined to the northeast. It was only two years ago California experienced rolling blackouts and high energy prices.

**Texas, on the other hand, is in the best position of all states in the union,** and for all practical purposes, controls its own destiny. The Texas power grid operates entirely within the state's borders. Therefore it is not engaged in interstate commerce, and to that extent, it is not under federal jurisdiction.

As far back as 5/11/01, we told you Texas has enough *excess* electrical capacity to power 15 million homes – more than enough to light up New York City. And there are **27 new generating plants, either newly opened or under construction,** throughout the Lone Star State.

Unlike most other states, **Texas charges grid users a flat rate** to move power anywhere in the state. So, power-generating companies are putting plants in **low-cost construction rural areas,** far from their customers. This not only encourages construction, but it keeps Texas customer **rates among the lowest in the nation.**

What we wrote in our 6/7/02 edition is more true today than then: “Serious misfortune – or even the *possibility* of electricity interruptions could work to the advantage of Texas and, specifically, the Silicon Hills of Austin. **When companies or investors make long-term decisions, the ability to do business, without interruption and as economically as possible, is near the top of the short list of considerations.** Places with potential problems: California, New England, New York City, much of the northwest, some Midwest cities and even some areas of the southwest.” You can get more detail by clicking on the “Archives” button on our Web site and calling up the 5/11/01 and 6/7/02 newsletter editions.

## Speaking of electrical power, the nuclear plant that provides Austin with its lowest-cost electricity is back on-line after shutting down for repairs 3/26/03. Is nuclear energy a problem-plagued source of power or the wave of the future?

In a dramatic turnaround, nuclear power may be making a comeback. In fact, there were signs pointing to the revival of nuclear power facilities long before the blackout of 2003. And, with the very **costly changes sure to come about as a result of new regulations and upgrades to the electric utility and distribution industries**, the prospect of cheap nuclear energy will likely gain more impetus and increase its supporters.

**“The nuclear power industry is facing its best prospect for revival in a quarter-century**, thanks to strong support from top legislators, newer technology and skyrocketing natural gas prices,” reported *The Dallas Morning News* a month ago. The August blackout crisis only enhances the nuclear prospects.

The report went on to note “government officials as powerful as Federal Reserve Chairman **Alan Greenspan** are rallying for the development of new nuclear power plants, to promote energy diversity.” For two decades, with little fanfare, nuclear reactors have been the **nation’s second largest source of electricity, behind coal**. Oil is no longer a major source of electricity generation.

But, if the Unit 1 nuclear reactor at the South Texas Project (STP) was offline for more than four months, is this a reliable source of energy? First of all, **the cardinal rule is not to put all your energy eggs in one basket**. Austin Energy, for instance, gets power from coal-fired plants near La Grange, as well as from STP. It is also using wind generation, etc. So when one source needs to be shut down for maintenance, or any other reason, there is always another source – including purchasing some of the massive excess power being generated elsewhere in Texas (see the previous story).

Nuclear power is cheap. As we reported 8/16/02: “For the second year in a row, **the STP nuclear power plant has the lowest average fuel costs of all power plants in the US.**” Austin put up enough construction money for STP decades ago to acquire 16% of the plant’s output. And STP’s twin reactors produce more than 2,500 megawatts of electricity, enough for more than one million homes in Texas.

It’s not likely you’ll see new nuclear power plants in the immediate future in Texas — again, because of the excess capacity that already exists here and the construction of other generating plants already underway. That’s okay. We’ll let other states bear the brunt of the controversy and opposition that will surely arise when a new nuke gets underway. By the way, the reason for STP’s shutdown: an inspection showed a **tiny crack in two (of 58) tubes through which residue the size of one-half of an aspirin tablet had slowly seeped over the course of several years**. The crack was repaired, tested, and put back on online with no injuries or damage to person or property.

**Median home prices were on a roll in the 2<sup>nd</sup> quarter 2003, rising 7.4% nationwide. But not in Austin. The home valuations here stayed essentially flat until July 2003.**

If you look at the current National Association of Realtors numbers for the previous quarter compared to the year before, you would say inflation in home valuation has leveled off in the Austin area. And, it appears to have leveled off at a time **the rest of the nation – and all major metros in Texas – have shown increased valuations.**

**Home prices in Austin edged up only 0.2% in the 2nd quarter** (though in July 2003, the Austin median sales price popped up to \$167,000), **bringing the median price of homes sold to \$161,200.** The national median, with an impressive 7.4% rise, was \$168,900. Other major Texas metros all had higher percentage increases than Austin.

What this reflects is a cooling off of what was once a red-hot housing market in Austin. **If you go back twenty years to 1983, you'll note median home sale prices in Austin jumped a staggering 30.94%.** The closest Texas city to Austin was way back – Fort Worth, at 13.31%. Even more significant is Houston's median home prices are *down* 4.15%, compared to 1983.

To put the twenty-year numbers in perspective, you have to realize that during the real estate recession that clobbered Austin and other Texas cities in the late 1980s and early 1990s, home prices fell dramatically. **So the twenty-year increase you're seeing has really happened in the last half of that two-decade period.** As a result, this current cooling off in Austin was no more than a blip, if the July upward spike turns out to be a trend.

**The trend lines look good as the jobless situation in Austin continues to improve. While still a long way from the go-go days when Austin was among the nation's leaders with unemployment regularly hovering around 2%, the picture is getting better monthly.**

In July 2002, the Austin metro notched a 6.2% unemployment number. **This July, Austin's unemployment has dipped to 5.9%.** It's still higher than healthy, but it's moving in the right direction – and it is better than other big Texas metros and the state as a whole.

For instance, **the state's July jobless rate was 6.6%.** Dallas came in at 7.4%, Fort Worth-Arlington at 6.7%, Houston at 7.2% and San Antonio matched Austin with 5.9%. Other large metros: Corpus Christi, 7.1%, El Paso, 9.9% and Waco, 5.7%.

The jobless rate is going down because **more people are finding work** (not necessarily leaving the area). The fall numbers will be interesting to watch because state government's new fiscal year may show declining jobs as a result of a pared budget. We'll keep an eye on it for you.

**A major Austin area company, as well as a Dallas company that dominates the Austin market, set benchmark records during this downturn that should become a business school case history.**

Dell and Southwest Airlines have one key ingredient in common, though they approached their industry downturns differently in other ways. It's the **commonality that should be the focus** of the B-schools, because Dell and Southwest have risen above their competitors in the process.

By now you know the stories. When the downturn slammed the high tech industry, Round Rock based Dell became leaner and meaner. Layoffs, common in the high tech industry worldwide, were especially painful in the Austin area as **Dell, our largest private employer, scaled back its workforce.**

Southwest, on the other hand, when the airline industry was shell-shocked by the 9/11 airline terrorist attack on top of earlier cutbacks in business and leisure travel, went totally contrary to every other airline – it did *not* lay off any employees. **All other airlines, citing a huge drop in passengers, cut staff. Not Southwest.**

So Dell and Southwest approached their industry crises differently in those respects. But, instead of hunkering down and waiting for better times, Dell and Southwest got aggressive during the hard times. And it paid off. **Dell became the largest seller of PCs in the world and Southwest became the #1 airline in the nation** in May in terms of passenger loads.

Dell increased market share through aggressive ad spending and marketing, while its competitors pulled back. Southwest stole passengers from its competitors by keeping fares low and adding flights and destinations. **The common thread was aggressiveness during a downturn.** It helped that both companies were financially strong going into the downturn. But the “**strike while your competitors are reeling**” was the common approach that paid off.

Speaking of enterprises located in Round Rock, **Dr. Louis Overholster**, never much for federal intervention, said the Round Rock Express poor baseball season record was the result of the team joining the Federal Hitless Protection Program! Groaannnn!

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