

THE

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AUSTIN LETTER

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Dear Client:

Texas still stands to benefit economically from California's financial mess – in spite of the fact voters decided resoundingly this week to recall their Democrat governor and replace him with Republican Arnold Schwarzenegger.

Why? Because many believe California's crisis is so bad – and business will still be treated so shabbily – that a whole range of California companies are ripe for recruitment. Don't forget California's state government is spending roughly **\$1 billion a month more than it is taking in, and the new 2004 budget continues this hemorrhage.** The new GOP governor must convince an overwhelmingly Democratic legislature to cut spending, or raise taxes by about \$10 billion a year to make a dent in the state's problem. In the meantime, California is digging itself an even deeper hole by borrowing billions of dollars to stay afloat.

And, the government crisis doesn't take into account California's pricey real estate, workers comp premiums that have run amok, legislatively-mandated liberal paid family leave laws, etc., etc. **As a result, businesses are being aggressively courted to take their jobs to other states** and they are responding (California is actually *losing* population to other states). One small manufacturer is spending \$800,000 to move from LA to Las Vegas and will recoup that in less than a year.

Consider Amarillo, tucked away in the panhandle and hardly the garden spot of Texas. Amarillo is mailing fake million dollar checks to California companies. The checks are an attention-getter for **Amarillo's plan to pay a company \$10,000 for every job created that pays at least \$12 per hour.** The money comes from a half-cent Amarillo sales tax earmarked for economic development.

Is it working? You bet. Irvine, California's AccuPoll will open a service operation center in Amarillo before year's end. **Amarillo will pay the company \$250,000 for the 25 jobs it will create.** Not only that, the California company has leased luxurious office space in the Bank One center downtown for half of what it was paying for a rundown building in a bad location in Irvine.

The new governor will have a tough job. A Democratic legislature is not likely to drastically cut spending. And the state's income tax is the nation's 3rd highest, its sales tax the 6th highest, its corporate income tax the 8th highest. It's a dismal picture, with no real solution in sight.

Speaking of taxes, many other states continue to raise taxes to cope with their financial crisis. Eight of them, including two Texas competitors, Massachusetts and California, are squeezing more this year from individual income taxes.

This information was gleaned from a recent survey in *The Wall Street Journal*. It becomes all the more important when you realize **Texas got through its legislative session without raising taxes and it, of course, has no personal income tax.** The sales tax is the biggest single source of revenue for Texas state government and it was not increased. This really makes Texas stand out among other states – many of them still wrangling with their financial problems.

“For the most part, states are raising other taxes before they raise individual income taxes, largely for fear of political backlash,” *WSJ* reported. “Sales taxes, for instance, went up \$700 million, primarily in Ohio, Indiana and Tennessee. But **significant personal income tax increases have occurred in the 2003 fiscal year** in Massachusetts, Vermont, Ohio, Louisiana, Oklahoma and California. Smaller increases were in Indiana and North Carolina.”

While personal income taxes and sales taxes are big political risks, businesses in other states are viewed by lawmakers as legitimate targets for taxation. Reported the *Journal*: “**The favorite target of more taxes so far: corporations**, which paid out \$1.1 billion more in the second quarter due to increases in California and New Jersey. Overall, corporate tax revenue rose by 18% in the second quarter from the prior year.” This comes at a time many businesses are struggling.

One last note – but an important one – about the difficulty facing **Arnold Schwarzenegger** as he tries to solve California’s financial crisis: **California is one of only three states** (Arkansas and Rhode Island are the others) **to require a two-thirds margin in its legislative bodies to approve a budget.** Democrat **Cruz Bustamante** ran a vocal campaign against Republican Schwarzenegger (losing by 1.2 million votes) and he is still Lieutenant Governor, and both houses of the legislature are controlled overwhelmingly by Democrats. The bodybuilder will need a lot more than muscle to lift this load.

Can one part of Texas survive the loss of an entire industry? Well, yes, if you’re talking about the textile industry that moved to Mexico and to Asia from Texas’s Rio Grande Valley.

At one point, there were 12 cut-and-sew, minimum wage factories around Harlingen — producing pants, dresses, underwear and kids clothes – employing more than 9,000. Now, there are none. *FORTUNE* reports “...businesses other than textiles have been growing, and while it’s hard to generalize, the people in Harlingen don’t appear to have given up or descended into a funk. In fact, they seem ready to move on. **If you’re looking for a laboratory of the country’s massive job losses and the global economic forces triggering them, Harlingen is it.**” Check out the article. It starts on page 193 in the magazine’s 10/13/03 edition.

When Motorola announced this week it will spin off its semiconductor unit here in Austin, it came at what could be a very good time.

The semiconductor industry has been in the dumper since the high tech downturn, and the local Motorola unit has been struggling financially. But it looks as if the industry is coming back from its steepest decline ever. **Semiconductor sales jumped 12.5% in August.** It was the sixth consecutive month of growth and the best August since the big bust of 2000.

If you thought this week's proposal to raise tuition at UTAustin created a bit of a stir, wait until later this month when a Task Force will recommend a plan to kick-out students who take longer than five years to get a degree.

The 5-year-degree-or-out plan is rare nationally and you can't find it at all in other higher ed institutions in Texas. But it is a serious move by UTAustin that has, for years, struggled with a way to hold down mushrooming enrollment. As we've told you over the years, **UTAustin has the largest enrollment on a single campus of any university in the nation** – a dubious distinction that many argue impacts the quality of undergraduate education.

Rather than detail the numbers we've reported to you many times (and as recently as 10/3/03), suffice it to say that **less than 40% of UTAustin's enrolling freshmen graduate in four years** and even after six years that number is only about 70%. Different tactics have been tried in the past to speed up the graduation rate, but the anticipated Task Force recommendation will be the most severe.

"A student who's not making good progress after 10 semesters probably should leave the university," President **Larry Faulkner** told *the Dallas Morning News*. "There's enormous demand for this university. It's an obligation of students and an obligation of the institution to push toward graduation in an efficient manner."

In other words: so long, slackers! Well, maybe that's too harsh. But when UTAustin is named the #1 Peter Pan university in the nation (where students "put off dealing with the pressures of the real world by escaping to the perpetual bliss of Never Never Land"), a 17-member Task Force of profs, students and administrators believes something must be done. So a 14-point proposal is being readied for Faulkner. It will likely give administrators discretion in enforcing the "5-year-degree-or-adios" decree but, by and large, it is expected to set a **15-hour per semester minimum class load for UTAustin students.**

Any way you slice it, with increased tuition and greater pressure for students to carry a heavier class load, UTAustin – already a **difficult institution with high standards** – **will become even tougher.** These two items are not yet done deals. But look for them to happen soon.

If you ever had any doubt that the Austin area was in the big leagues as a movie-making center, just check this week's top revenue producing movies. Three of this week's Top Ten grossing movies were directed by Austinites.

This may be the first time in movie history that three directors from Austin each had films in the Top Ten revenue generating category at the same time. **Richard Linklater** was at the top of this week's list with his newly-released movie starring **Jack Black**, *The School of Rock*. A little further down the list at #5 was *Secondhand Lions*, directed by **Tim McCanlies** and starring **Robert Duvall**, **Michael Caine** and **Haley Joel Osment**. And director **Robert Rodriguez** weighed in at #9 with his *Once Upon A Time In Mexico*, starring **Antonio Banderas** and **Salma Hayek**. (Pretty impressive star power, also!)

There is no question this marks a **significant milestone in Austin's burgeoning film making reputation** and is not likely to be repeated anytime soon. But, hang on. There's more. The buzz out of Hollywood is the big Christmas Day epic, *Alamo*, that was directed by another Texan (**John Lee Hancock**) will be a blockbuster. It's the most expensive movie shot in Texas – somewhere north of \$80 million – and stars **Billy Bob Thornton** and **Dennis Quaid**. The entire city of old San Antonio, as well as the Alamo mission, was reconstructed just outside Austin for shooting of the historical drama.

Other movies are being filmed in the Austin area. In fact, if you attended any of the Texas Longhorn home football games so far this season, you may end up in *Cheer Up*, a film starring an award-winning Texan, **Tommie Lee Jones**. The filmmakers were shooting crowd scenes for their movie about cheer leading (Now, wait a minute, you say. Shouldn't they have gotten a signed release to use your image? No, because there was a sign at all the entrances that said by entering the stadium you gave permission for your image to be used in the movie. Didn't see the sign through the throngs? Very few people did, but it was there).

Dr. Louis Overholster says "Let us never forget this 21st Century bit of wisdom: behind every successful corporation is an accountant with his fingers crossed!"

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Sincerely



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