

THE

Real Estate

AUSTIN LETTER

www.AustinLetter.com

P.O. Box 1905 / Austin, Texas 78767-1905 / 512-498-9495 / Fax 512-327-1976 / e-mail News@AustinLetter.com

Volume 25, Number 41

January 23, 2004

Dear Client:

The metro area of Texas that has traditionally had the highest *unemployment* rate year-in, year-out (McAllen-Edinburg-Mission), had the fastest growing non-farm *employment* rate from August 2002 to August 2003. What's going on here?

Some of what contributed to the 2.7% employment growth rate in the McAllen-Edinburg-Mission metro area also was driving the Austin area's increase in employment. Several fast growing areas in Texas are home to major universities that are benefiting from a **strong demand for higher education**. And, of course, all areas of the state are **creating healthcare jobs** because of increased demand.

But what set the Rio Grande Valley border area apart was the increase in federal government spending. Federal government spending (as well as state increases) has created jobs. **Border patrols** have increased and **growing school systems** have expanded.

In many ways, this illustrates what is happening to jobs during this recovery period. (In a minute, we'll tell you when the bottom hit and the upturn began.) According to economists at the TexasA&M Real Estate Center, growth is being concentrated in these sectors (ranked according to percent of job growth): **education and health services, construction, government and financial services**. Other areas, such as manufacturing, are lagging.

The reason Texas eased into this recovery, rather than surging, is the sectors where most of the jobs are being created are where we are simply *recycling dollars*. "For the most part, **these industries and services are not the ones that bring money into the state's economy from elsewhere**," the TexasA&M researchers point out. When dollars come from outside the state, the impact is greater.

When did the economy hit bottom? Indicators of small business outlook compiled by the National Federation of Independent Business **bottomed out in March 2003**, according to the Texas A&M economists. So did the Texas Index of Leading Indicators, a Dallas Federal Reserve Bank Index. Both are on the rebound. The Texas Stock Index has **rallied since its low in March 2003**. Reinforcing all this, the TexasA&M researchers noted that corporate profits are exceeding levels last seen in 1998. So, when you refer to the recent downturn, you can also talk about the recovery that began last spring.

Caution is still the order of business, but there is more than a glimmer of hope on the horizon for the type of economic improvement in the Austin area that fosters *retail* growth.

This is the assessment of **Eric DeJernett**, who is the retail real estate principal with NAI Commercial Industrial Properties in Austin. NAI CIP points out the Austin retail real estate market maintained a **steady occupancy rate in 2003**, compared to 2002, while also adding 650,000 sq.ft. to the overall market during the last half of the year.

To bolster his view that there is a “more than a glimmer of hope” for Austin area retailers, DeJernett further notes that **retail sales on a local and national level were up during the Christmas season**, and the computer industry (a major employer in Central Texas) and the stock market both experienced strong growth in 2003. Furthermore retail rental rates have increased slightly.

So, who are the active players in the development of retail in the Austin area? As you might expect, they are *not* local – they are the biggies, with aggressive expansion policies. You can count on two hands the number of retailers that currently dominate the Central Texas retail landscape. **“H-E-B, Target, Walgreen, Wal-Mart, Home Depot, Eckerd and Lowe’s are currently driving most retail development** and anchor the majority of the retail centers, which consequently have the highest rates,” reports NAI CIP.

There’s another interesting subplot going on in Austin’s retail movement. **“There is a noticeable lack of grocery store development outside of H-E-B,”** NAI CIP observed. “Randall’s and Albertson’s have been cautious players as H-E-B continues to stake its claim as the dominant grocer, while Target and Wal-Mart vie for their piece of the grocery market.”

Grocery stores are magnets. Retail operators know everybody buys groceries and places that sell groceries generate heavy traffic. **So, when a strip center nails down a major grocer, retailers will follow.** Wal-Mart and Target know the grocery traffic is so important they’re aggressively adding groceries to their stores.

However, any analysis of retail in the Austin area would be incomplete without discussing **the 600-pound gorilla – Simon Properties.** The national mall developer dominates, thoroughly, retail operations here. And it is planning community-type centers in Georgetown, Buda and Bastrop.

That’s not all. **“Simon’s strong relationships with the nation’s top tenants and access to development capital have made them the partner of choice** for the Gateway Shopping Center, the proposed Domain Shopping Center and The University of Texas tract fronting North MoPac – all in the Arboretum trade area,” notes NAI CIP. **Simon is the dominant player bringing new tenants and concepts to Central Texas** as it represents the “safe choice” for cautious retailers looking to expand into the Austin area.

Inflation? What inflation? The rise in *core* consumer prices last year of 1.1%, was the smallest increase in 43 years.

Core consumer prices *exclude* food and energy. But even adding those back into the equation, the rate of inflation in 2003 was just 1.9%. So, for now, rising prices are not a threat to the economy. With signs that the economy continues to gain ground, analysts expect the Federal Reserve will **hold short-term interest rates at 1%** when they meet next week. In fact some economists believe rates will **stay where they are for the rest of this year and into 2005**. Caveat: there are those who say *if* the economy goes gangbusters, the Feds could start nudging up rates as early as later this year. What went up and what went down last year? **Computers, cars and clothes were cheaper**, while medical care, beef and energy prices were up.

Hold the presses! Man Bites Dog! *Texas Monthly* founder/publisher (and all-around gadfly) Mike Levy is actually praising someone at Austin's City Hall.

"This City Council is in the enviable position of having the very best city manager for Austin since I started observing local politics back in 1976," exclaims Levy (Levy always "exclaims"). "In fact, I'd bet that **Toby Futrell is probably the best city manager in the country today**. She's smart, blessed with wisdom and common sense. Unlike so many of her predecessors, Toby has no personal agenda beyond trying to do what's right for the town she loves so much."

But then Levy lapses back into his normal attack mode. "The bad news is Toby inherited from her predecessor a bunch of **managers that are consummate bureaucrats who simply do not do a very good job**. Most have yet to figure out citizens and taxpayers are their 'customers,' and that their mission is to figure out how to serve the needs and interest of their customers," Levy exclaims (again!).

Leave it to Levy, though, to have advice for the Austin City Council: "If you were members of the board of a privately held company, and Toby was your chief operating officer, **you'd be encouraging her to clean house**."

Levy bolsters his suggestion by exclaiming(!): "Look at Toby's track record for appointments since she's been manager. **The people she's put in place are all All Stars, without exception**, especially in comparison to many of the hacks hired by Toby's predecessors."

"There are very few certainties in this most uncertain life of ours, but here is Mike Levy's personal guarantee: if Toby does clean house with the Council's blessing and encouragement, the pain and noise will last for about 60-to-90 seconds, and then **the City will run better and more efficiently** with the reduced resources now available to our city government. The Council will be heroes. And just maybe even our traffic lights will get fixed," Levy finally exclaimed.

In spite of difficult times in the airline industry, a number of new non-stop flights are being added to Austin's airport schedule. But, in keeping with new trends, much of the new service is on smaller aircraft – even for long hauls to both coasts.

One new non-stop to San Francisco (SFO) and two to Washington Dulles (IAD) will be added to United Airlines' Austin schedule in February. But it will be on United *Express* and the equipment will be a Mesa **64-seat aircraft**, in spite of the long flying times. If the smaller, slower aircraft don't pose a problem for you, you'll appreciate the **SFO service that starts 2/27/04. The IAD schedule kicks in with the first non-stop on 2/20/04** and the second 2/27/04. The addition of these routes will bring United's daily Austin departures to twelve.

Also using smaller equipment, Frontier will add a **third non-stop to Denver 2/8/04**. The new flight will be flown on a **70-seat Frontier Jet Express** operated by Horizon Airlines. While not new, you may not be aware that Trans States Airlines is providing **two daily non-stops to St. Louis from Austin on 50-seat regional jets**. The reason you may not be aware of this is these flights are operating as American Connection and are booked through American Airlines.

Finally, another **new non-stop will start out of Austin 3/1/04 to the second most popular destination for Austin fliers — Las Vegas**. And America West is using full-size equipment, with first class seating for the high-rollers, as it becomes the second airline to offer non-stop flights to Vegas from Austin.

Obviously, it's good news anytime Austin travelers get a choice of new non-stop flights to popular destinations. And, to some extent, it's a **vote by the airlines for an improving economy in the Austin area**. But, just be sure when you book a flight, you ask about the equipment to be used, so you won't be surprised if the aircraft is smaller and more cramped than you were expecting – especially on the longer segments.

Speaking of air travel, **Dr. Louis Overholster** is old enough to remember when the only bomb he had to worry about on long haul airline flights — was the movie!

NEAL SPELCE AUSTIN LETTER (ISSN 1071-0612) is published weekly, except last two weeks of the year, for \$150 (plus tax) per year or \$249 (plus tax) for two years. To subscribe, call 512-498-9495. Periodical Postage Paid at Austin, TX 78767 by Austin Letter, Inc., 1407 Wild Cat Hollow, Austin, TX 78746. POSTMASTER: Send address changes to: Neal Spelce Austin Letter, P.O. Box 1905, Austin, TX 78767-1905.

Sincerely



Editor/Publisher