

THE

*Real Spelce*

# AUSTIN LETTER

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Dear Client:

**In just a few days, you may see a little up-tick on the publicity screen about the value of tourism. Tourism Week is May 8-16. What you may *not* see is the *extended* value of tourists to Texas.**

Oh sure, you may run across the unfathomable number of **\$2.5 billion in travel-related total spending for the Austin area during 2002** (the latest Texas Economic Development numbers available). But as big as this number is, the economic effect goes beyond those dollars circulated through our five-county metro area. It's what we refer to as the *extended* effect.

Let's use Spring Break as an example. "There are probably some people who consider **Spring Break just a trivial occurrence and a time of non-stop, partying for young people,**" observes Texas economist **Ray Perryman**. Ray understands there are excesses at South Padre in March, but he sees a broad economic impact.

As Perryman recognizes, it's not just the coeds and frat rats from UT Austin, Texas A&M, Texas State, etc. who flock to the beaches: "**Students from over 100 US colleges and universities located in more than 25 states regularly travel to the South Texas area ...** most of the educational institutions represented are in the South, Southwest and Midwest, though there is a sprinkling of Ivy League and New England institutions mixed in among them."

And here's the kicker. "Many college-age students and families from other states are first introduced to Texas during the spring holidays, and **75% of them are likely to return, thus adding the possibilities of further economic benefit,**" Perryman noted. Families also are a big part of this travel influx as young parents take the kids on a Spring Break vacation. The annual tourist season is frequently seen as starting with Spring Break in March.

This Spring Break example illustrates why tourism is so important for the long-term economic benefit to the Austin area and the entire state of Texas. The big bucks the travelers spend as they traverse our area are important, as is the fact tourism is a clean industry and tourists don't place heavy demands on our schools, etc. But the simple fact is **a great majority of those who visit Texas for the first time are likely to return** – bringing more travel dollars and, importantly, many of them move here to become taxpayers and contributing citizens.

**If you're going to borrow money personally, or for your business, sometime in the near future – or if your current loans are tied to prime — you want to know what will happen to interest rates. Here's the best information we could find.**

Long-term, the prime interest rate should rise all the way **from 1%, where it is now, up to about 4% two years from now.** How will it get there? The best word we get out of Washington, where the control-all Fed operates, is you can **look for a quarter percentage point increase** sometime in the August-September time frame this year.

After that, you could see another **quarter-percentage point increase** in the benchmark federal funds rate by the end of the year – probably in December. **This should knock the prime rate up to 1½%.** Then, about every two months throughout 2005 and into 2006, you can look for prime to inch up the same amount – getting to the 4% mark in two years. While this is obviously speculation, it represents some solid analysis. And it should help your planning.

**UTAustin's cost-cutting efforts have kept 70-100 campus employees from being laid off.**

As we reported most recently on 1/30/04, UTAustin made a business decision to save money by **consolidating the purchase of paper, toner cartridges and other items** into a central purchasing system for office supplies. Prior to this decision, university departments purchased office supplies from more than 200 vendors at varying prices. So, under the direction of VP/Financial Affairs **Kevin Hegarty**, UTAustin's CFO, the university's combined purchasing power was negotiated with just two vendors – Office Depot and Hurricane Office Supply.

**The result: a savings of about \$2.5 million – enough to allow 70-100 campus employees to keep their jobs during the past year.** For the Austin economy, this is good news. This means these employees are getting regular paychecks and spending those bucks on goods, services, mortgages, rent, movies, food, etc. – not collecting unemployment checks.

UTAustin took a bit of a chance with this maneuver. It was so confident Hegarty could pull off the savings, it kept the employees on the payroll, rather than laying them off and re-hiring them after the savings were realized. **“Essentially, the money was spent in the budget before we actually were certain the savings would be achieved,”** Hegarty said. The risk paid off.

However, the change didn't come easy. As we told you 1/30/04, Hegarty said: “There was resistance to changing the culture of purchasing, with one obstacle being the thought by some that while **change indeed was needed, it was needed in every area other than their own.**” Other cost-saving moves are on the way. **“We're not done,”** said Hegarty. “Continuous improvement needs to become a part of the fabric of what we call our culture.”

**Airlines, so crucial to an area's economic success, are being ranked from best to worst — all the way from “cleared for takeoff” down to those “running on fumes.” Here's an analysis of airline financial status, from industry analyst Eric Torbenson of *The Dallas Morning News*.**

SOUTHWEST, Dallas. “The King of Discounters has seen its kingdom infringed on by upstarts, and it's not particularly happy about it. **But the king is not dead by any stretch.**”

AMERICAN, Fort Worth. “Near-bankruptcy experiences can get a management team's attention. A year later, **sacrifice appears to be paying off.**”

CONTINENTAL, Houston. “Though its swagger is a bit muted, Continental still boasts a great brand and is the **first choice of many business travelers.**”

AMERICA WEST, Tempe, AZ. “Since receiving a government-backed guarantee after the September 2001 attacks, America West has reinvented itself with a **simplified pricing system.**”

ALASKA AIR, Seattle. “It's good to have a niche and Alaska Airlines simply owns big chunks of the Northwest. **It's a favorite of Seattle business travelers for its first-class cabins.**”

ATA, Indianapolis. “Considering that the carrier nearly filed for bankruptcy protection just a few months ago, **ATA's prospects are pretty strong.** ATA has a new fuel-efficient fleet.”

JETBLUE, Queens, NY. “The new textbook example of how to build a brand from scratch, JetBlue Airways **remains the envy of carriers** for becoming the ‘it’ airline in just four years.

AIRTRAN, Orlando. “For now at least, AirTran's **growing just about as fast as JetBlue.** It has fairly low costs, and its planes feature a business-class cabin that tempts travelers.”

DELTA, Atlanta. “**Delta Air Lines' total costs are higher now than American's.** Its pilots earn twice what AirTran pilots get flying the same routes out of Atlanta.”

UNITED, Chicago. “At some point, United Airlines will persuade the banks to give it enough **cash to get out of bankruptcy protection,** but it doesn't appear to be in that big of a hurry.”

NORTHWEST, St. Paul. “**Think of Northwest Airlines as Delta North in terms of its need to cut costs.**”

US AIRWAYS, Arlington, VA. “It's hard to kill an airline, as Trans World Airlines' decade-long spiral into oblivion showed in the 1990s. **US Airways could be on the same path.**”

Conclusion: “**Most industry watchers can't take their eyes off the high-flying low-cost airlines** that will collectively receive several hundred new planes in the next three-to-four years, bringing the pricing war even closer to the majors.” The price wars will heat up. Stay tuned.

**This tech recovery will be different. It'll run at a steady pace for years, without the booms and busts of the past decade.**

This is the considered judgment of our friends in Washington at *The Kiplinger Letter*. They point out businesses are fueling the expansion and flashy, unproven technology will be shunned in favor of investments promising fast returns. **PC sales will lead the tech recovery as shipments are predicted to be up 13% over 2003.** Manufacturers are helping this boost by offering steep discounts. Sales of laptops are expected to increase by 30%, outpacing desktops.

Also high on corporate shopping lists are **more sophisticated servers** that can process growing traffic on company networks and Web sites. Sales of computer chips are also expected to boom as **demand for semiconductors soars** in regard to everything from toasters to DVD players, to cars to cell phones.

It's also predicted that **IT spending will rise 6% this year** and almost that much in each of the next few years. This is a big plus for the economy because IT spending accounts for about 8% of the US Gross Domestic Product.

Firms are also opening up the spigot on software spending – to improve security, customer service, sales and inventory tracking. **Software spending is predicted to grow about 6% this year** – compared to 3% in 2003.

Obviously, this high tech recovery is important for the Silicon Hills of Austin. This recovery should increase the number of jobs locally and, as you know, more jobs in *any* sector impacts almost all areas of our economy. **But the growth in jobs in the tech segment of our community has an outsized impact because most of these jobs are higher-paying than,** say, jobs in government, or bar-tending, or pumping gas, or areas where the main customer communication talent is learning to ask “Want fries with that?”

Speaking of a recovery, our resident philosopher **Dr. Louis Overholster** wisely observes it is hard to make a comeback when you haven't been anywhere!

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