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Dear Client:

**Much to the surprise of the experts, the Texas economy begins 2006 with momentum. And the Austin area is at the forefront.**

In spite of outside economic blows – such as devastating hurricanes, high energy prices and the financial burden of the war in Iraq – the Austin and Texas economy in 2005 provided enough push to **generate momentum for 2006**. For instance, total personal income in Texas rose at a rate faster than the national average.

**The Austin-Round Rock metro area posted an employment growth rate of 2%** from October 2004 to October 2005, making it the **fastest growing local economy among the five major Texas metro areas**. The others: Houston-Baytown-Sugar Land metro area, up 1.8% ... the San Antonio metro, up 1.7% ... the Dallas-Plano-Irving and Fort Worth-Arlington metros, both up 1.1%.

These percentages reflect *non-farm* employment. And, as we've been reporting throughout 2005, the **Austin-Round Rock unemployment picture has also been the best of the Texas metros**.

The state's economy is expected to grow faster in both output and labor than it did in 2005. To keep this in perspective, remember **Texas' economic output is huge – close to that of Canada** – at more than \$884 billion. A little swing in the numbers goes a long way in an economy as massive Texas's.

**“Thanks to consumers and historically low long-term interest rates**, the economy continues to grow steadily,” noted **Dr. James Gaines**, research economist at the Real Estate Center at TexasA&M, the provider of these figures. And, as you would expect from a real estate economist, Gaines said “the real estate market, particularly the residential market, is one of the reasons” for this growth.

Speaking of residential real estate, the experts at the Real Estate Center say there is no reason to anticipate a housing shortage would drive home prices up. Likewise, they do not expect an oversupply that would depress the market. Overall, they say, Texas' housing market continues to offer **highly affordable homes without excessive price inflation**, with price increases, sales and construction levels in 2006 to be equal or slightly less than the 2005 rate.

**For the first time in a long time, you may see substantial new office construction in the Austin area in 2006.**

The Austin office market is quickly approaching rent and occupancy levels not seen since the late nineties, reports Colliers Oxford, one of the largest commercial real estate firms in the world with a significant Austin presence. **“Continued absorption and rising rental rates** have been the driving force for Austin’s thriving office market,” Colliers Oxford noted.

But there is more to it than that. **“Significant activity in the office investment market** by groups such as Equity Office and Aspen Growth Properties reflect the sentiment that Austin will continue to see a rise in demand which will sustain the increasing rental rates,” observed Colliers Oxford.

The researchers at TexasA&M’s Real Estate Center said “Investors paid record prices for trophy office properties in Austin.” This activity, combined with Austin’s job growth (see the previous story), is leading to speculation that **new office construction will soon be necessary.**

The days of rock-bottom office rental rates are going, going, gone. “Austin is currently in the middle of an **upswing in rental rates and a shift to being a landlord’s market.** Many seasoned commercial real estate professionals feel that Austin’s rental rates will continue to rise reflecting the increasing demand for office using jobs.”

There is one anomaly in all of this. **Sublease space has increased (even though it was diminishing at a steady rate) due to a couple of new large subleases.** PPD Pharmaco is subleasing its former 168,000 sq.ft. campus on Ben White Blvd and Freescale is marketing 276,000 sq.ft. at its North Austin location on Parmer Lane. This skews a sublease market that had seen its vacancy drop every quarter since 1<sup>st</sup> quarter, 2003.

But throwing this much additional sublease inventory into the office leasing market did not significantly slow the trend. At the end of the 4<sup>th</sup> quarter 2005, **overall office occupancy jumped an impressive 3.6 percentage points** from 4<sup>th</sup> quarter 2004 to stand at 86.5%. For the same time period, rental rates jumped \$1.61 a square foot to reach an average of \$20.37/sq.ft.

**Austin remains a popular destination for new companies** by combining low median home prices (once again, see the previous story) and its vibrant economy leading to accolades such as being named #1 in *MSN House & Home’s* Best Big City Places To Live poll in 2005.

**“The Austin office market is back to normal** after seeing high vacancies, large subleases, and free rent from 2001 to late 2003. The New Year is expected to bring continued positive absorption and the possibility of new office development,” Colliers Oxford predicts.

**Austin topped all Texas cities in film and television total production budgets in 2005 – for the sixth consecutive year.**

Not only did Austin recapture the #1 spot, it did it by beating all the other Texas cities combined. **The Austin area tallied approximately \$78 million in film production budgets, 56% of all the film budgets** spent in the Lone Star State during 2005, according to the Texas Film Commission. Dallas/Fort Worth came in second with \$43 million. Houston, San Antonio and the rest of Texas, in this order, divided up the remainder.

Why is Austin such a mecca for filmmakers? “Austin leads the list each year because the factors that make the city a great place to film are unwavering,” says **Gary Bond**, director of the Austin film office. “It is **inexpensive** for filmmakers to shoot here, our **local crew base is extremely talented** and producers and directors who live here champion it for filming.”

Twenty projects were shot in the Capitol City last year, including the feature films *How to Eat Fried Worms*, *Infamous*, *The Return* and *The Texas Chainsaw Massacre: The Origin*. Additionally, television series *Austin City Limits*, *Real World Austin* and *Roller Girls* were taped here. Austin has had bigger years. For instance, when *The Alamo* was filmed here, its budget alone – plus-or-minus \$100 million – surpassed the total for all productions shot here in Austin in 2005. But, hey, who is counting?

**Don't stock up on several years worth of stamps to cover the price hike that just went into effect. Why? Another price increase is already scheduled.**

As we alerted you months ago, the price of a first class stamp went up this week (1/8/06) from 37-cents to 39-cents. Other mailing and shipping charges were raised at the same time by the US Postal Service.

The increase this year was about 5.4% across-the-board. Next year, the US Postal Service has already indicated it will double this hike for 2007 – probably between another 10% to 12% for business mailers. All the details have not been officially announced, but you can **look for the price of a first class stamp to set you back about 42-cents in 2007.**

Postal Trivia: Austin has had a long history of having key people in high places at the US Postal Service. Currently **Carolyn Gallagher** is serving on the Service's Board of Governors that sets policy and oversees the operations of the Post Office. **Sam Winters** and **Bob Hardesty** are other Austinites who have served in a similar capacity. They both still live here. Prior to their service, the first dean of the LBJ School of Public Affairs, the late **John Gronouski**, was US Postmaster General, the executive head of the Post Office.

**Are you keeping up with the times? Every pair of Levi's you've ever owned had a watch pocket in the front. Guess what the pocket is now being re-designed to do?**

Levi Strauss announced this week it is the first company to make **iPod-compatible jeans, featuring a joystick in the watch pocket to operate the device.** Not only that, the Levi's RedWire DLX Jeans for men and women, which will be available this fall, also have a built-in docking cradle for the iPod and retractable headphones. Oh, my.

It seems almost sacrilegious to mess with a staple of American clothing that has been around since the 1850s with roughly the same design and fabric. But Levi Strauss apparently took note when **Apple Computer revealed it has sold 42 million iPods to date.** 42 million! And, even with those big numbers, iPod sales jumped 63% in holiday quarter sales.

While Levi Strauss may be the first jeans manufacturer to hop aboard the iPod bandwagon, other clothing manufacturers have also picked up on this trend. Some men's jackets sold at Macy's (for between \$275 and \$350) feature iPod controls on the sleeve and we understand that there is now a **waterproof iPod-compatible snowboarding jacket.**

But, Levi's? **The American icon, the original jean.** The jeans worn by those working the gold mines as California was becoming a state. The red tag on the hip pocket. The leather label, with the waist and length sizes printed on the belt area for all to see.

Oh sure, Levi's have been modified over the years. After all, you have button-fly and zip-fly, etc. But a joy stick in the watch pocket? And a built-in docking cradle? Somehow it doesn't seem to fit. Or maybe it is the wave of the future. We'll wait and see.

After surviving a lot of speeches where the speaker wrapped up by saying "in conclusion," **Dr. Louis Overholster** is convinced that a conclusion is the place where you got tired of thinking!

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