

Volume 28, Number 3

April 21, 2006

Dear Client:

More apartment units are in the construction process than the Austin area has seen in three years, rental rates are rising and, yet, occupancy dropped in the 1st quarter. What's going on?

History can explain what's happening in these puzzling figures. "Digging back over 14 years of research there is a trend that emerges with few exceptions," according to **Robin Davis**, who tracks such apartment trends through her company, Austin Investor Interests.

"As new Class A developments gain ground with rental rate stabilization, **the 1st quarter of almost every year, back to 1994, has shown a dip in Class A occupancy.** Class B properties have also shown a slight 1st quarter decline, while Class C units have shined," she reports.

So what does this mean in the overall economic picture? "We breathe a sigh of relief that the **occupancy decline is symbolic of a better time in our market's history and not a downward turn.**" With concessions designed to lure tenants declining in value, "the overall effect of this reduction is that tenants are now **shifting back to a more affordable product type,**" she said.

Apartment developers are apparently unwavering. Davis reports during the 1st quarter, more than 1,900 units began construction, while another 1,600 units were submitted into the permitting process. Currently, **there are more than 7,000 units already under construction,** 70% of which are expected to complete during the next 12 months, she noted.

What about this head-long rush into new apartment construction? After all, there is a reported **15%-20% rise in construction costs.** Does this signal good times or does it mean we could be heading right back into an overbuilt market?

"Although this is more units than the market has seen in the past three years, **absorption is not expected to be a problem,**" she said. "Overall, the Austin apartment market is in a good place right now."

Why is she so bullish? "**In-migration and job growth are both on the rise,** providing a broader tenant base than we have seen in several years. The development pipeline is running at a **rapid pace, but is well diversified** among location, product type and completion timelines. If all remains on target," she says, "the market is set for the year."

A new trend is developing in the types of apartment buildings under construction in the Austin area.

When you've seen one apartment building, you *haven't* seen them all. The new development trend in the Austin metro area is toward **mixed-use apartment projects that combine retail, office and/or live-work units.**

Robin Davis's company, Austin Investor Interests, tracks trends in the apartment sector of our economy. She reports: "New construction starts were a good example of this new trend, as three of the new starts are mixed-use development."

"There are now over 1,100 units of this new property type under construction," she said. "Additionally, the next 12-15 months is expected to see the start of nine more projects, with over 2,800 units."

So where is this new trend in apartment development the most prevalent? In total, more than 37% of the mixed-use development is expected in the Central and Central Business District areas, while **48% is in the northern sectors** of the Central Texas metro area, she notes.

Another indication the apartment market is vibrant and healthy is investors seem to be lining up to buy Austin area apartment buildings.

In the past two years, more than 20% of the Austin areas apartment buildings have changed ownership and the 1st quarter of 2006 continued to see a high number of sales, according to **Robin Davis** of Austin Investor Interests. She says there were **17 properties – totaling 3,003 units – that changed hands during the 1st quarter.**

Who is buying Austin apartment buildings? Less than a third of the 1st quarter's transactions were purchased by Texas partnerships, said Davis. The remainder was evenly divided among East and West Coast investors. **Currently, there are 96 properties reported for sale and 15 of those have contracts pending** – so the investor market is still quite active.

When Advanced Micro Devices (AMD) moves its 2,000 employees into its new corporate campus near Oak Hill in mid-2007, a strange thing will happen to Austin traffic patterns.

AMD says that because almost a third of its employees live in Oak Hill neighborhoods and 58% live within ten miles of the new site, **traffic analysis shows that the new campus will reduce the number of traffic miles driven by employees.** The analysis also concluded the traffic generated by the new campus will be counter-cyclical to existing traffic patterns.

Samsung Electronics' official selection of Austin as the site for its new semiconductor plant was significant for a number of reasons. But, for perspective, you need to know only two facts.

There was no doubt it was a big deal. Even though the decision had been telegraphed weeks in advance, **everybody from the governor on down to local elected officials and economic development advocates unleashed the superlatives.** The *Austin American-Statesman* gave prominent play to the announcement for three days running. And, frankly, all this attention was deserved because of its significance. The two facts you need to know:

Samsung's announcement represents the largest single investment by a foreign company in the United States.

This is the first 300mm semiconductor wafer fab facility in our area and there are only six either operating or under construction in the US.

The world's second largest chip maker currently has invested \$1.9 billion in their 300-acre site in Northeast Austin where it employs 1,100 workers. **The new 300mm semiconductor plant will be built near the existing plant** and Samsung will have invested even more in the new facility by the time it opens its doors with around 1,000 employees. Yes, it is a big deal.

"Move over, California; bye-bye, New York. For the first time, Texas has more FORTUNE 500 companies than any other state. The place has earned its spurs."

This was the headline in the 4/17/06 edition of *FORTUNE* magazine, the issue that annually ranks the top 500 companies in the US. **This is a major milestone in the evolution and maturation of the Texas economy.** With 56 of the *FORTUNE* 500 companies headquartered in the Lone Star State, Texas tops New York (55) and California (52). It's a three-way cluster at the top with the #4 state, Illinois, dropping off sharply to 32 companies.

Think about it. The longtime bastions of commerce – with key cities such as New York City, Los Angeles and Chicago – have now been eclipsed by a state many outlanders still think revolves around cotton and cattle.

Space doesn't permit us to list all 56. The Texas Top Four — **Exxon Mobil**, Irving (#1 on the *FORTUNE* 500), **ConocoPhillips**, Houston (#6), **Valero Energy**, San Antonio (#15) and **Marathon Oil**, Houston (#23) – are energy companies. **Dell Inc** (#25) is here in Central Texas. Also headquartered here in Austin is **Freescale Semiconductor** (#368), **Temple-Inland** (#433) and **Whole Foods Market** (#449). The remainder companies with headquarters in Texas are clustered, by and large as you would expect, in Houston (with 23) Dallas (with 11) and San Antonio (with 5). If Austin had one more HQ, it would have tied with Santone, Cleveland, Denver, Seattle and others to make the nation's Top 21. This is also a local milestone.

While planning your summertime air travel, you need to be aware that some airport are reporting three-hour security lines are possible. The problem: staffing shortages.

As of this writing, no such problems are being reported for Austin-Bergstrom International Airport (ABIA), but when you head home to Austin you may need to **add several hours to your return itinerary** if you are hopping a plane at any of about eight US airports (including some popular vacation destinations).

The federal agency that handles US airport security, the Transportation Security Administration (TSA), has shifted to local direct hiring from a national contract. In the process, **Orlando and Los Angeles are already short on screeners** and other airports warn they will be in the same boat soon – just in time for the heavy vacation air travel summertime crunch. Compounding the problem, TSA says its attrition rate is about 20% per year for screeners.

Besides the current shortage at Orlando and Los Angeles, six other airports have issued press releases trying to hire screeners. Take this as a warning (because the hiring process is quite lengthy and cumbersome). Those airports are **Chicago, San Diego, Boston, Phoenix, San Jose and Detroit**. Most of them have heavy traffic bound for Austin on any given day.

How hard is it to be a TSA screener? First you take a Web-based exam that tests object recognition and an understanding of English. Then color vision is tested, a medical exam is conducted and the applicant is finger-printed and asked to fill out more forms for background checks. And, of course, there is the standard employee interview process. **TSA, despite what the airports report, is saying not to worry, it will be ready.** But, with this summer air travel season expected to be the busiest since 2000 (before 9/11), you would be well-advised to keep a close eye on the eight airports mentioned here and plan accordingly.

Dr. Louis Overholster says “Today I’d like to pay tribute to the world of science. A hundred years ago, who would have ever guessed that so many things could be bad for you!”

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., 4105 Bee Creek Rd, Spicewood, TX 78669. POSTMASTER: Send address changes to: Neal Spelce Austin Letter, P.O. Box 1905, Austin, TX 78767-1905.

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