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Dear Client:

The Austin area economy is boom-..., uh, better not say it or it might jinx it. But there is no doubt we're in the midst of a major growth period, verging on an economic boom. And a controversial economic development tool has a lot to do with this vibrancy.

You don't need an economist to tell you what your eyes can see. Look around as you drive around – construction is everywhere, as are help wanted signs. Money is being spent, generating jobs. Employers are looking for workers here where unemployment is the lowest of any major metro in the state.

Samsung's plans to build a 300mm Fab facility (one of the largest capital expenditures of its kind in the US) and **Hewlett-Packard's** plans to build not one, but two, data centers here happened because of a controversial economic tool. **Both companies accepted incentives and tax abatements** to locate in the Austin area.

But frankly, these incentives have not been as controversial since 2002 when the local governmental entities started requiring companies to meet **agreed-upon goals for capital expenditures and jobs before any tax abatement was granted**. Also, each project is thoroughly investigated for its history of diversity, benefits provided employees, philanthropic practices, etc. as it is evaluated for incentives.

Also, a “give and get” sheet is prepared for each company. In the City of Austin's case, for example, **energy consumption is considered – because Austin makes money selling electricity**. Sales tax generated is another factor considered. Finally, consideration is given to the impact of the project on other entities in the community, such as the construction trades and smaller, existing businesses.

Let's take one recent example – the aforementioned Hewlett-Packard announcement. The value of the abatement over a ten year period is just more than \$3 million, while the return to the City of Austin alone is just more than \$11 million. **“I would say this is a pretty good deal for the taxpayers,” noted Tim Crowley**, Chairman of the Greater Austin Chamber of Commerce.

In the larger picture, though, you have to be sure the infrastructure is in place – or planned – to keep up with a growing economy. Roadways and educational institutions come to mind. But there is no question, **we're on a dynamic upswing in our economy**. Hang on.

So who are all these people expanding the population of Texas? Well, they are different from those who boosted our growth in the 1990s and this impacts our economic wellbeing.

First of all, Texas population is really growing. Recently released population estimates from the USCensusBureau show a total Texas population of almost 22.9 million as of July 2005. This is an **increase of more than two million, or 9.6%, since April 2000** when the state population was nearly 20.9 million.

According to the state demographer of Texas, **Steve Murdoch, Texas is the second fastest-growing state in numerical terms and the eighth fastest in percentage terms since 2000.** Texas' *numerical* increase was second only to California's, which increased 2.3 million. Florida was third in numerical growth adding roughly 1.8 million. Then it dropped off dramatically to #4 Georgia's increase of some 900,000 and #5 Arizona's 800,000.

In *percentage* terms, Texas' rate of increase lagged Nevada (20.8%), Arizona (15.8%), Florida (11.3%), Georgia (10.8%), Utah (10.6%) and Idaho (10.4%). You'll notice though that all the states (except Florida) have significantly less population than Texas, making it easier for them to generate a high percentage of growth. **"Texas pattern of both rapid absolute and relative growth is continuing,"** observed Murdoch.

But this current growth spurt differs dramatically from the growth Texas has experienced in the past. Murdoch points out in the 1990s, about 50% of Texas population growth resulted from *natural increase* (more births than deaths). Thirty percent of the increase was from *domestic migration* from other states, while 20% came from *immigration* from other nations.

This mix of new population has now changed. From 2000 to 2005, about 58% was *natural increase*, **only about 9% was attributed to domestic migration** and *immigration* from other nations grew to 33% of the total population increase.

When you drill down a little deeper, you find from 2004-2005 *domestic* migration made a dramatic upward turn to where it became 13% of the state's growth. Why is this important? Domestic migrants are what demographers refer to as "positively selected." They tend to have **higher average levels of education and income** than persons in the areas to which they move. As a result, they tend to **substantially increase the markets for various goods and services.**

On the other hand, immigrants tend to be a bimodal group. Some have high levels of education and relatively high-paying jobs; however, a much larger proportion have relatively low levels of education and take relatively low-paying jobs. Put it another way: immigrants are **less supportive of economic growth**, says Murdoch.

If this recent trend toward a higher increase in domestic migration continues, Murdoch predicts it will have "positive impacts on the Texas economy."

One of Austin's strongest assets has always been its highly-educated workforce. As one wag cracked: "my bartender has more education than I do." How does Austin's educated populace stack up with other major cities around the country? Quite well, thank you.

This goes way back. Long before the techies invaded the Silicon Hills of Austin, bringing with them a focus on brainpower that was attractive to the multitude of high-tech companies that sprang up here, **there was always a high percentage of Austin's population with a college education.** This was true even when there weren't that many good jobs for the well-educated.

Back then, it was a given our best and brightest high school grads who went on to college felt they had to **move to another city to find a well-paying job.** After all, state government – never known for its high salaries – was the major employer force here not so long ago. (Remember, the high-tech revolution didn't start in Austin until 1983.)

But, still, the lure of this area for those who came to UTAustin from other Texas cities, proved too much for many and, **despite low wages, they decided to stay** – taking jobs tending bar or whatever and raising the education level of the workforce. They may have been *underemployed*, but they were educated and they liked the quality of life.

Eventually, **companies started taking notice of the underpaid brainpower in the area** and decided to locate here. It really took off when Austin found its niche in the high-tech field. This attracted even more educated workers from other states, boosting the already impressive quality of the labor force that was available.

Austin now ranks among the nation's elite cities when it comes to "smarts." In fact, Bizjournals.com (the parent of the *Austin Business Journal*) recently conducted a survey with **Austin as #3 on the list of Smartest US Cities.** Seattle and San Francisco are #1 and #2, with Colorado Springs and Minneapolis, #4 and #5. Other Texas cities in the top 53 large US cities: Arlington (#12), Dallas (#35), Houston (#38), San Antonio (#40) and El Paso (#48).

In the Bizjournals.com survey, communities were ranked in three population categories, based on a formula that rewards places with heavy concentrations of college graduates. **The rankings reflect each community's collective brainpower,** which is tied to its residents' abilities to innovate, create, compete – and make money, according to *ABJ*.

"Make money?" A worker with a graduate degree earns 45% more, on average, than a colleague with a bachelor's degree, and 167% more than someone who never went beyond high school, according to the USCensus Bureau.

As a result, not surprisingly, **America's brainpower is concentrated in tech centers, college/university towns, national and state capitals and affluent suburbs.**

Three predictions: 1) What will happen to mortgage rates this year? 2) With sales slumping, what will happen to the Big 3 US automakers and 3) Will pennies be discontinued in the US?

Our friends at *Kiplinger Forecasts* like to look ahead at various facets of business and the economy, so we thought we would share a few of their predictions with you.

Mortgage rates. They won't hit danger levels this year. The 30-year fixed mortgage is predicted to **peak about 7% by fall**. After that, signs of easing inflation and economic growth will put a cap on rates.

Big Three US automakers. One of the three at the end of this year will be a foreign automaker. **Toyota is poised to top DaimlerChrysler in US auto sales** and the Japanese carmaker will be sneaking up on Ford's market share. GM is not immune to Toyota's growth. At year-end, Toyota will also pass General Motors as the world's largest auto firm.

What's happening currently is that **sales of US brands are tanking**. In May, GM was down 13%, DaimlerChrysler was down by more than 8% and Ford was down 2%. Meanwhile, Honda and Toyota racked up 16%-17% gains and Volkswagen saw a 29% jump.

Pennies to heaven? Metal prices are soaring and some groups are suggesting the **government stop making pennies**, requiring all businesses to round their prices to the nearest nickel. Prediction: it won't happen.

The penny problem is all the more interesting because it costs the US government 1.4 cents to mint each penny. Well, then, why not ditch the penny and go to nickels? The nickels cost 6.4 cents each to make. Go figure.

Dr. Louis Overholster swears he saw this sign in a lawyer's office: "Give a man a fish and he'll eat for a day. Teach a man to sue and he'll eat for a lifetime!"

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