THE Neal Spelce AUSTIN LETTER
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Dear Client:

Austinites with weak credit have been having a difficult time getting a home loan for some time and now the squeeze is on for those seeking to buy higher-end homes in the Austin area.

The difficulties in the sub-prime (weak credit) mortgage lending category have been well chronicled. Homeowners and even some mortgage companies have filed for bankruptcy and **the days of exotic loans with no-money-or-very-little-money-down are history**. Up to this point, the impact has been felt on those trying to buy *less expensive* homes. No more.

Austin has a very active, and very large, high-end home buying/selling market. In fact, **you may be amazed at how many million-dollar homes are for sale in the Austin market**. (See the third story in this edition for more detail.) Up to now, these high-dollar homes in Austin have been selling smartly.

But, this week, the nation's credit crunch – and this includes Austin – has expanded to the upper end. **Interest rates for larger home loans – they call loans above $417,000 "jumbo loans" – jumped dramatically almost overnight**. A few weeks ago, the average rate for a jumbo mortgage loan was 6.5%. This week the average is 7.3% and one Austin mortgage company is quoting up to 8.5%. This is a significant increase in anybody's book – and in a very short timeframe!

But this isn't the only part of the credit crunch for the high-end homebuyer. "Stated income" loans are rapidly going away. **Derisively called "liar's loans," a stated income loan qualifies a borrower using the income the borrower *states* on the application form – as opposed to the income the borrower can *document***. While lenders don't check income on a stated loan, they do check the source of income. Ordinarily, they require that a self-employed borrower be self-employed in the same business for two years, and that a salaried employee be employed in the same line of work for two years.

Requiring income records can be a problem for many self-employed and high-end buyers. For instance, many wealthy individuals' tax returns may not truly reflect income due to "creative" tax planning. One Austin lender said a buyer, earning $750,000 a year, only paid taxes on about $50,000 income. A $50,000 income won't qualify for a jumbo loan. Higher interest rates, as well as tighter lending requirements, *could* impact Austin's high-end residential real estate market. We'll watch this for you.

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The Austin area economy is among the best in the nation, but the credit crunch is driven by forces outside Austin – and, as a result, it is outside local control.

So what is happening nationally that is causing this tightening of credit? Well, obviously there have been some **problem mortgage loans**, mostly sub-prime, in other US housing markets that were overheated to begin with. Also **home values skyrocketed on the two coasts** and when that bubble burst, investors and homeowners took some big hits. Much of this was fueled by the lowest interest rates in a generation. All this, and more, has triggered a domino-like effect.

This domino effect has caused some of the financial markets to perform abnormally. For instance, mortgage interest rates historically have followed the 10-year Treasury bond yield. Well, since June, the 10-year Treasury bond yield has actually been going *down*. But the conforming 30-year mortgage rate has not followed suit and now, **the 30-year rate for jumbo mortgage loans, is going up – in the opposite direction.**

Many attribute the anomaly of the rising jumbo rate to the fact that **investors who buy loans and securities backed by mortgages have stopped**, unless the loans are guaranteed by quasi governmental agencies Fannie Mae or Freddie Mac.

The Wall Street Journal reports this means "**lenders must either hold loans, at least temporarily, and face the risk of falling values for them**, or seek out borrowers who qualify for loans that can be purchased by Fannie or Freddie." As a result, there is no market for other types of loans.

There is some hope this is a short-term situation. The "credit crisis" is being acknowledged throughout the financial markets and at the highest political levels. One report this week indicated more than 100 lenders have closed around the nation. In fact, the 10th largest US home mortgage lender in terms of loan volume, American Home Mortgage Investment Corp. was forced to stop lending and laid off most employees last week.

What does this mean for Austin? Home *buyers* are finding it is much tougher to qualify for a loan. As a result, home *sellers* are finding the pool of buyers rapidly diminishing. Lenders, who make money by loaning money, see the number of qualified loan customers drying up.

Builders who have speculative homes nearing completion are starting to worry about how long they may need to keep their homes on the market, increasing their carry costs. What about all the **new downtown condos** coming on the market? You get the drift. The ripple effect is widening throughout the Austin area.

All this is occurring at a time when **million dollar homes have been selling at a brisk pace in the Austin area** and there are hundreds of others still listed for sale. See the next item.

How many homes have sold for more than a million dollars in the Austin area since the first of the year? 50? 100? 150? How about 217 as of this week? And it may surprise you to know there are more than 500 homes priced at more than a million dollars still on the market.

That's right. Those in the market to pay more than a million dollars for a home in the Austin area have many more than 500 from which to choose. The Austin Board of Realtors Multiple Listing Service (MLS) shows there were **513 homes listed for $1,000,000 and above on the market this week, but this is a low number**. Many builders who are slapping up million-dollar speculative manses right and left are not listing them on MLS or that 513 number would swell considerably – especially in the $2,000,000 or $3,000,000 and above category.

Of the 513 million dollar homes listed with MLS, 448 are in Travis County. If you break this list down to homes in the $2-$3 million category, 97 are listed for sale with MLS (92 of those in Travis County). And in the $3,000,000-and-up price range, you can pick and choose from 64 different homes with a "For Sale" sign in the front yard (60 of them in Travis County).

Sure, there are a lot of pricy homes on the market. But up to the point when the "credit crunch" hit, they had been *selling* as well. As we said **217 homes with a million dollar price tag have sold since the first of the year (202 in Travis County)**. Of this number, 23 MLS listings were sold in the $2-$3 million range (22 in Travis County) and 14 homes priced above $3,000,000 were sold since January (13 in Travis County). The average selling price of this latter category — $4,159,000 and the homes averaged 7,867 sq.ft. in size.

There are two newly-developed neighborhoods where you can find a high concentration of these mansions. Both of them are chock full of large, new homes erected by builders with no buyer commitments in sight – spec homes, they are called. And most are *not* listed on MLS.

Take a drive through **Seven Oaks**, just west of Austin close-in on Bee Caves Road. **There are 23 – count them, 23 – brand new multi-million dollar homes for sale**, most of them built speculatively by builders. Five are listed at more than $3,000,000, 15 between $2-$3 million, and 3 between $1-$2 million. **The most expensive: $3,850,000; the least expensive; $1,250,000.**

Or try **Spanish Oaks**, a gated community on Hwy71W, near Southwest Parkway. There are five new spec homes priced between $1-$2 million and six on that list are more than $2,000,000. **The range: $1,595,000 to $2,495,000.**

In addition to Seven Oaks (Eanes School District) and Spanish Oaks (Lake Travis School District), most of the other high-dollar homes are concentrated on Austin's west side and in the Lake Travis/Western Travis County area. There are also homes with eight digit price tags. It will be interesting to see how/if the credit crisis affects these pricy properties.

Tourism, growing in the Austin metro area at a 5.3% rate, has now replaced manufacturing as the fifth largest economic sector.

Long-touted as a desirable "clean" industry, tourism is coveted by cities worldwide as an economic bell-weather. **Tourists bring dollars into an area from outside** – dollars that ultimately circulate through the local economy in the form of profits to local businesses, taxes paid to governmental entities, and salaries paid to employees of hotels, restaurants and other tourist attractions. A local government doesn't have to educate the children of tourists and only has to provide minimal fire and police support for them while they are visiting. In other words, **there is a great return from tourism, with a relatively small investment.**

The most recent figures gleaned from a comprehensive analysis of the benefits of travel and tourism in the Austin-Round Rock metro area show the number of travelers – both business and leisure – to the metro area jumped to 19 million in 2006. **Those travelers generated an economic impact of $2.8 billion**.

The increase since 2003 was 12% when 17 million visitors were counted. This increase has provided the support to **create 10,000 new jobs – from 65,500 jobs in 2003, to more than 76,400 jobs in 2006**, a 5.3% annual growth rate. For comparison purposes, the employment increase in the metro area averaged 3%.

Tourists are defined as visitors who stay overnight or travel in excess of 50 miles one way for a day trip. **Leisure travelers account for 55% of the market, with business travelers rounding out the remaining 45%**. The balance has shifted slightly toward more business travelers since 2003. The Austin Convention & Visitors Bureau (ACVB) commissioned Global Insight to perform the analysis.

"These figures certainly validate Austin as one of the country's emerging premier destinations," said **Bob Lander**, President/CEO of the ACVB.

Dr. Louis Overholster says the problem with sub-prime is — sometimes it refers to hamburgers!

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Sincerely

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