

THE

Real Estate

AUSTIN LETTER

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Dear Client:

Right now, this may be one of the best places in the US to buy a home – especially a brand-new home. A number of forces have come together to create this situation. But it will not last.

To understand what is happening, you need to put yourselves in the position of **big national homebuilders, whose profits have been slammed horribly by the national housing crisis and whose stock has been battered unmercifully.** To survive, these builders have put the brakes on new home construction to focus on rebuilding their bottom line.

While this is in reaction to the *national* home markets that are suffering, **big national homebuilders operating in Austin – where we have a healthy real estate market – are bound by national policies established by their corporate headquarters.**

Those policies require them to generate revenue by selling off the new homes that have already been built and, at the same time, scale back on new construction. **The big builders are on a really short leash when it comes to *new speculative construction* and they are slashing prices to reduce their financial carrying costs on *completed, but unsold* homes.**

If you are in the market for a new home that is just waiting for you to move in, these factors spell o-p-p-o-r-t-u-n-i-t-y. There are deals to be had on those new homes just sitting there. **Price slashing, free upgrades, special considerations, etc. are there for the buyers' asking.** Austin representatives of the big builders are ordered to unload those homes. So, now is the time for buyers to cut a deal.

One of the reasons this is such an opportunity is the Austin real estate market is still very healthy, with values and pricing of new homes *increasing* each month. It's not as if this is occurring in a "down" market, like elsewhere in the US. So, **Austin homebuyers can take advantage of the troubles elsewhere, with less associated risk.** It's a heckuva deal.

But this is not going to last very long. These big builders are dealing with a finite amount of inventory. Once the speculatively-built homes are gone, they are gone. **Builders will not be motivated to offer the same discounts and deals on to-be-built housing,** according to Residential Strategies Inc., an Austin company that provides services to these builders. Now is the time for buyers to strike to get the best possible deal on a newly-built home in Austin.

The only fly in the ointment in the homebuyers' opportunity is that the *nationally-generated* tightened mortgage requirements affect Austin metro buyers just as they do everyone else.

Hey, it is a lot tougher to get a mortgage loan now than it was a year or so ago. The lenders are shying away from loans that lean to the risky. For instance, it is **very difficult get a "no down payment" home loan if your FICO (credit) score is less than 760.** And, in the past, **buyers could just simply "state" their level of income, without providing supporting documents.** Now those who are seeking "modest" down payment loans must furnish documentation – such as IRS tax reports and W-2s certifying income history.

What does this mean? Well, Residential Strategies Inc. (RSI) is reporting that Bank of America's research indicated that these **tightened mortgage qualification standards are increasing the percentage of buyers who will *not* be able to qualify for a loan.**

RSI says BofA thought 10% of the buyers that purchased in the "loose requirements" year of 2006 would not qualify today. Now, it points out **these new restrictions increase non-loan-qualifiers to 35%.** This is a huge reduction in the marketplace of potential home buyers.

Another development is occurring that has not been widely reported. **Lending institutions are really clamping down on home appraisals,** even those from appraisal firms that are working for the lenders. In Austin, this is causing some serious problems. For instance, we know of one Austin deal where three different buyers submitted qualified offers on a unique upper-end home in one of Austin's most desirable neighborhoods. But the buyers' lender balked.

Willing seller, willing and well-qualified buyers – agreement on value. But the lender initially rejected the loan based on an appraisal from a local appraisal firm hired by the local mortgage broker due to the lack of "cookie cutter" sales comps in line with nationwide appraisal standards. More and more area homes are being subjected to sharp scrutiny by lenders if they do not fit a set mold for neighborhoods.

Which brings us to our key point. Austin is a *positive* anomaly in the national picture. According to RPI, **Austin is one of the least risky housing markets in the US and the median home price in the Austin area continues to increase** – unlike other markets for which national lending policies have been set. Yet, the Austin area – in some respects – is being lumped in with the problem markets.

The analogy used by RPI seems most apt in this situation. RPI says residential real estate is like the weather: "We hear about the *national* weather, but we dress for the *local* conditions. Yes, there may be 'fronts' that blow in from the West Coast. **But it doesn't matter to us if there is stormy weather in California – as long as the sun is shining in Texas!**"

The Austin area economy continues to do well according to one important overall measurement. But two other Texas metros are outstripping Austin so far this year.

The Federal Reserve Bank of Dallas tracks what is going on in the various local economies around the Lone Star State and it compiles its results in a matrix called the **Texas Business Cycle Index (TBCI)**. **This Index offers a good overall snapshot.** Texas metros can get a feel for how they are doing year-over-year and how this compares with other local metros. (Don't worry. We're not going to dive into the dull details. We'll just give you the results.)

Houston is the state's growth leader. One business leader who has operations throughout much of Texas said this week that "Houston is drowning in money," speaking about the energy boom. The Fed's TBCI confirms his observation. **Houston's economy had a 5.3% increase** in its business cycle index from April 2007 to April 2008 – **far and away the best growth in Texas.** For comparison purposes, you need to know that **Houston's April 2008 index was 263.9.**

San Antonio is #2 in growth. The Alamo City experienced a 3.9% increase in the index, to close out at 243.3. **Austin is #3,** with a 3.1% increase to reach 414 in the index. **Fort Worth was #4,** with a 2.8% increase to reach 248.2 in April. **Dallas, at #5,** showed less of an uptick, 2.4% to reach 248.2 in the index.

The Fed's index is a measurement of the region's current economic conditions. It analyzes reports from nonagricultural employment as well as the *unemployment* rate. It also includes inflation-adjusted wages and inflation-adjusted retail sales. In other words, it is a fairly **comprehensive overview of the economy of a given area.**

And looking at the growth percentages for the past year, these **five major Texas metros all performed very well** – especially when you realize that during this same measurement period, there was much debate about whether the US was moving toward, or actually in, a recession.

Austin and Texas metro area retailers are doing a bit better so far this year than last – which means residents of these areas are spending money. But there is a slowdown underway.

Sales tax collections are one way to measure the spending habits of residents in a metro area. As expected, Houston residents are spending money at a greater rate than other major Texas metros. **Houston sales tax collections through the first six months of the year are up 7.1%.** Fort Worth was up 6.3%, Dallas up 2.4% and San Antonio's sales tax collections were up 2%. **Austin is lagging the others by this measure. Sales tax collections in Austin were up only 1.5%,** compared with the first six months of 2007. This bears watching in Austin because the area not only is moving at a slower pace than the others, but the 1.5% increase is a big drop from last year when double-digit increases were recorded. We'll keep an eye on it for you.

With the word this week that the oppressive heat has pushed the demand for electricity from Austin Energy to record levels – with more record peaks likely this summer – it raises an all-important question: does Austin Energy have enough capacity for the future?

It's important to understand that when the all-time peak electricity usage record was set this week, the previous record was set in September 2006. **This level of peak usage has only occurred in the past in August and September – when the temperatures are the hottest and the demand is the greatest**, as schools and universities crank up to full capacity. So, it gets your attention when something this dramatic occurs this early in the “swelter season.”

Austin Energy will tell you not to worry for now. It will point out that it has plenty of generation capacity to meet demand in Austin. And, if for some reason Austin Energy's capacity falls short, the Electric Reliability Council of Texas (ERCOT) also has plenty of generation available that Austin could tap.

But what about down the line? The Austin area is one of the fastest growing areas in the nation. Look what's ahead. **More people, more businesses, more living units, more public buildings – all needing more and more electricity.** We may have enough electricity (or we may not) to get through what is shaping up as a long, hot summer. (Don't even mention blackouts or brownouts.)

It takes years to build and deliver more electrical generating capacity. And it is very costly. What fuel will be used to generate additional electrical capacity? Coal, natural gas, wind, solar, nuclear? **The Austin City Council just weeks ago delayed making a decision on whether to contract for more electricity from the soon-to-be-expanded nuclear facility** that already generates the cheapest electricity Austin is currently using. All indications are that Austin Energy will **continue to set all-time peak records this year** as this month is shaping up to be the hottest June on record, with predictions for a warmer-than-normal summer. Decisions on Austin's energy future will need to be made sooner, rather than later.

Dr. Louis Overholster says 99% of politicians give the rest a bad name!

Sincerely



Editor/Publisher