

THE

*Real Estate*

# AUSTIN LETTER

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Dear Client:

**The solution to stop the national housing market from falling is simple. Decrease supply and increase demand. Yeah, but how do you do that? There's the rub.**

While real estate transactions have slowed markedly in the Austin area, **local home values have been holding steady**. In fact, if you look at the recent tax appraisal on your property, many would **think the values have risen dramatically**. (One wag suggested you should take your appraisal to the tax office and ask if this is an offer to buy your property and then pull out a sales contract for them to sign!)

Nationally, it's a much different story from what is happening in Austin. For instance, did you know that **home prices in Phoenix are down 50.8% since the market peaked in June 2006?**

Wow! What if *your* home had dropped 50% in value in just three years! **Phoenix is the most extreme situation in the US**, according to the Standard & Poor's Case-Shiller Home Price Index that measures major metros. But what is happening there, in the nation's 12<sup>th</sup> largest metro area, is not an isolated case.

Other big metros are not far behind. **Home prices in Las Vegas are down 48%. Prices are down 45% in Miami and down 40% in Los Angeles and San Diego.** Those are humongous drops.

And some economists say **home prices will fall further** — maybe dropping as much as 5%-10% more — as potential buyers, worried about the recession and rising unemployment, postpone big decisions like buying a new home.

Thank your lucky stars you live in the Austin area. But, of course, **economic policies that are the result of what is happening nationally are being enacted and forced upon Austin**. Just ask anyone who has tried to get a home loan these days. Talk to a lender. They will tell you how the financial institution ball game has changed as a result of what has happened nationally. This is not to diminish the specific local problems you see — such as declining retail sales. But it does indicate factors that are *not* the result of the local situation play a big role. **So, what is the solution to this “supply and demand” problem?** In the next item, you will see what a Texas economist, who specializes in real estate, suggests is the way out of the morass.

**There are four ways to decrease supply and increase demand in the housing market. If they are implemented, problem solved, according to a Texas real estate economist.**

The chief economist at the Real Estate Center at TexasA&M University, **Dr. Mark Dotzour**, proposed these four steps last year (see our 12.12.09 issue). And he's sticking to his guns after four months of major moves on the national level. Here's how he puts it today:

**Curtail the supply of new homes.** As we pointed out in the previous item, virtually everyone agrees that falling home prices are at the center of the current economic and financial crisis. Yet, Dotzour points out that **new homes are still being built in cities where prices are collapsing and foreclosures are skyrocketing.** When new homes are sold with massive price concessions, prices for all homes in those communities trend downward.

**Decrease the number of homes coming back into the market through foreclosures.** Dotzour claims government efforts to do this have not worked so far. He points out that if you are a homeowner 90 days delinquent on your mortgage and the government reduces the principal amount of your mortgage and lowers your mortgage payments significantly, **what incentive do you have to get back on track?** He also points out that if "one homeowner in your neighborhood gets lower principal and lower payments, **won't the other five owners on your block want the same thing?**"

**Increase demand for homes and do it quickly.** How can the government do that? Simple, says Dotzour. "It needs to **give investors an incentive to purchase vacant homes and rent them to tenants.** There must be adequate down payment so the investor has a big incentive to keep the house. Additional incentives could be created by **lowering the depreciation schedule to five to seven years** for investors who buy foreclosed houses. To solve the problem extremely quickly, the federal government could **offer these investors zero percent capital gains tax** if they hold the properties for more than five years."

**Mortgage rates are way too high.** The spread between the 30-year mortgage rate and the ten-year Treasury rate increased after the government intervened. And Dotzour blames "a complete lack of confidence in the financial integrity of Fannie Mae and Freddie Mac ('Frannie')." He suggests the government should tell the world that **Frannie mortgage bonds are guaranteed by the full faith and credit of the US government** and, if that happens, he thinks all Americans could refinance with a **30-year mortgage around 3.75%.**

Dotzour says these four steps are as important in May as they were last December. And he goes further by referencing the steps that have been taken since then by saying that "**simply printing money is a temporary bandage that only delays the inevitable.**"

**Want to lease office space in the Austin area? Or renegotiate an existing lease? You can probably cut a pretty good deal. More space is available and rates are dropping.**

In 1<sup>st</sup> quarter 2009, the overall **vacancy rate increased nearly one percentage point** from the previous quarter to 20.34%. And the overall **average quoted rental rate dropped 55-cents per square foot (psf)** to \$26.04 psf. These numbers are courtesy of Oxford Commercial. But if you are to get a good deal, it depends upon the location.

The major office submarkets in the **southwest and far northwest** have had millions of new office square footage delivered over the past year and a half. As a result, the **landlords in those submarkets could be in a position to wheel and deal** to lease an abundance of vacant office space.

But the Central Business District (CBD) is a different story. Downtown is a much more vibrant office market. Rates are rising. **“With healthy demand in the CBD and the absence of surplus supply, it is not surprising to see CBD rental prices going in the opposite direction from the other major office submarkets,”** Oxford observed.

Oxford suggests that tenants will remain cautious during 2009 and not rush into a lease arrangement. As a result, office space seekers could probably find even better deals if they wait awhile. Oxford predicts that **vacancy rates will increase throughout 2009 and that rental rates will decrease.**

**Supply will continue to outweigh demand and landlords will drop rates to attract tenants.** “We should continue to see rental rates decline as landlords compete for business,” is the way Oxford put it. Oxford’s **Brent Powdrill** phrased it this way: “We will begin to see which landlords are creative enough to come out as winners as we pace through 2009.”

**Industrial space in the Austin area is experiencing much of the same situation as office space.**

Shrinking businesses are giving back space to the market in order to cut costs in response to the declining national economy, reports Oxford Commercial. **The overall vacancy rate for industrial product spiked up to 17.8% at the end of the first quarter.** This is a sizable increase from the overall vacancy rate of 11.8% Austin experienced a year ago.

So what can be anticipated? Vacancy should remain level as construction activity halts and leasing activity slows. **Asking rental rates will fall slightly as landlords try to attract and retain tenants.** The positive spin on this market decline, from **Mike Tipps**: “It is a solid time for users to lock in their long-term real estate positions and significantly lower operational costs. Likewise, investors should have some excellent acquisition opportunities.

**Austin's airport traffic is trending downward during this national recession. How does this compare to other air travel facilities?**

Austin-Bergstrom International Airport (ABIA) opened for business as a brand-spanking-new airport ten years ago, 5/23/99 (click the "Archives" button at the top of this page to read about ABIA's development in Volume 31, Number 2, 4/10/09). **Using 1999 passenger totals, ABIA was the nation's 50<sup>th</sup> largest facility. In 2007, ABIA ranked 45<sup>th</sup> in the nation** — the last year for which the FAA's all airports tabulation is available, according to Austin Chamber VP/Research, **Beverly Kerr**.

ABIA's first *full year* of passenger service in 2000 saw **7.66 million passengers**, she reported. And a total of **9.05 million** were served in 2008.

Kerr also noted that since 2005, Austin's annual percent change in enplanements has consistently surpassed the national growth rates. "If you compare 2008 to 2004, **Austin has seen a 26% increase in enplanements, while enplanements nationally have only increased by 9%**," she pointed out.

It is also interesting to note that while the San Antonio metro has a larger population (2.03 million) than the Austin metro (1.65 million), **the level of passenger traffic at ABIA has surpassed that of San Antonio's airport since 2003**.

And if you compare the Silicon Hills of Austin with the Silicon Valley, here's an interesting little statistic: **Mineta San Jose International Airport's (SJC) passenger traffic dropped 23% compared to last year. ABIA dipped 14%**.

**Dr. Louis Overholster** was a bit perturbed when he pushed his grocery cart into the Express checkout lane to see that the person in front of him was pushing a cart piled high with groceries. It turned out to be a pleasant surprise when the cashier looked at the almost overflowing cart, then said, politely, to the customer with the packed grocery cart: "So, which six items would you like to buy?"

Sincerely



Editor/Publisher