THE Neal Spelce AUSTIN LETTER

www.AustinLetter.com

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Dear Client:

You are witnessing a major re-shaping of the US economy. **It's moving along speedily**, **almost daily**, **unlike glacial economic shifts of the past**. **What does this mean for the Austin area**?

When you stick your head out and look around as the US finally emerges from the current economic crisis, you will see a **dramatically changed economic landscape**. Forget the political debates for the moment – whether this is good or bad. One thing is certain: it will be different. So it is important to analyze what this re-shaped economy will mean for those who live, work and invest in the Austin area.

> A thinker who has long analyzed future US geographic economic trends, **Richard Florida**, notes the **changing economy** "**depends on generating and transporting ideas**." Writing in *The Atlantic*, Florida says "the places that thrive today are those with the highest velocity of ideas, the highest density of talented and creative people, the highest rate of metabolism." He includes Austin in this mix.

Florida says the housing bubble was the ultimate expression, and perhaps the last gasp, of an economic system some 80 years in the making and now well past its "sell-by" date. "The bubble," he said, "encouraged massive, unsustainable growth in places where land was cheap and the real estate economy dominant. **It encouraged low-density sprawl**, **which is ill-fitted to a creative**, **postindustrial economy**. And not least, it created a workforce too often stuck in place, anchored by houses that cannot be profitably sold, at a time when flexibility and mobility are of great importance."

> He suggests "encouraging growth in the regions and cities that are best positioned to compete in the coming decades: the great mega-regions that already power the economy, and smaller, **talent-attracting innovation centers** inside them – places like Silicon Valley, Boulder, **Austin** and the North Carolina Research Triangle."

Speaking of the rest of the US, Florida has observed that "**different eras favor different places**. We need to let demand for the key products and lifestyles of the old order fall, and begin **building a new economy**, **based on a new geography**." He has previously touted Austin and the other city/regions mentioned above as the wave of the nation's economic future. So, it's comforting to note that, in light of today's seismic economic shift, he is reinforcing Austin's already-proven capacity to be among those that lead the nation economically in the future.

While Austin may maintain its nationally-renown economy after the current crisis, its "landscape and geography" could be altered as a result.

When the current economic crisis is observed from a rear-view mirror, the US economic geography will be changing. "It will likely be **sparser in the Midwest** and also, ultimately, in those parts of the Southeast that depend on manufacturing," predicts **Richard Florida**, a forward-looking thinker and planner. "Its suburbs will be thinner and its houses, perhaps, smaller. Some of its southwestern cities will grow less quickly."

> But not for Texas and the Austin area. "**Its great mega-regions will rise farther upward and extend farther outward**," Florida continued in his lengthy treatise in *The Atlantic*. "It will feature a lower rate of homeownership, and a more mobile population of renters. In short, it will be a more concentrated geography, one that **allows more people to mix more freely and interact more efficiently** in a discrete number of dense, innovative mega-regions and creative cities."
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> "Serendipitously," he went on, "it will be a landscape suited to a world in which petroleum is no longer cheap by any measure. But most of all, it will be a **landscape that can accommodate and accelerate invention, innovation, and creation** – the activities in which the US still holds a big competitive advantage."

Florida says that "if there is one constant in the history of capitalist development, it is the ever-more-intensive use of space. Today, we need to begin making smarter use of both our urban spaces and the suburban rings that will surround them – **packing in more people, more affordably, while at the same time improving their quality of life**."

> If this is the case, then what needs to be done? "That means liberal zoning and building codes within cities to allow **more residential development**, **more mixed-use development** in suburbs and cities alike, the in-filling of suburban cores near rail links, **new investment in rail**, and **congestion pricing for travel on our roads**," he detailed.
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> "Not everyone wants to live in city centers," he acknowledges, "and the suburbs are not about to disappear. **But we can do a much better job of connecting suburbs to cities and to each other, and allowing regions to grow bigger and denser without losing their velocity**."

Florida says "**we need to ensure that key cities and regions continue to circulate people, goods and ideas quickly and efficiently**. This in itself will be no small task; increasing congestion threatens to slowly sap some of these city-regions of their vitality."

These comments did not reference Austin in particular. But he lumped high-growth Austin into his overall assessment of what the landscape and geography would look like. Food for thought.

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At the peak of the Austin homebuilding market in 2006, there were 25 builders putting up 250 homes or more in the area. Now there nine. How has this impacted the market?

Six of those 16 builders who are no longer slamming hammers in the Austin area have **left the market**, **sold their assets**, **merged or declared bankruptcy**. This represented 23% of the total homebuilding market share. Does a similar fate await some of those still building homes here? **Mark Sprague** heads up the Austin operations of Residential Strategies, a company that provides services to the homebuilding business. Let's get his take.

Lenders pose one of the biggest headaches builders deal with every day. "We continue to see increasing pressure on builders from lenders with regard to renewing (if not, usually reducing) their interim lines of credit," said Sprague. "Lenders want more securities, more guarantees, and we're not sure they are going to get that. **For big builders, this has forced the hand of many of them. Smaller builders not getting their lines of credit renewed really shuts these guys down**."

> "It is an interesting time," Sprague understated. "On one hand, we are sure the government and others are saying banks need to make loans, extend credit, but the reality is **banks are being much more conservative in their underwriting and those extensions of credit. So most builders are really downsizing** and getting in line with the market."

How does this affect a homebuyer? There is an inventory – though diminishing – of unsold new homes on the market. Those willing to buy are demanding excessive discounts. But Sprague warns that a potential homebuyer had better buy soon. "Yes, there are deals in the market today," Sprague admits. "**But once this inventory is gone, it is gone. And builders will not be motivated to offer the same discounts on to-be-built housing**." Fair warning.

One Austin banking institution has taken a dramatic approach to 16 new or partially-built homes it foreclosed upon – it demolished them.

Guaranty Bank of Austin acquired the homes through foreclosure on a builder in California. Guaranty said the cost to finish the houses would well exceed the $100,000 demolition charges, so the backhoes were brought in to knock down the homes in Victorville, CA, northeast of Los Angeles. The homes had other problems, such as vandals, squatters, drug users, etc.

Thirty-year mortgage rates fell to 4.78% last Friday, hitting their lowest level since Freddie Mac started tracking rates in 1970. One-year Adjustable Rate Mortgages (ARMs) were almost the same, at 4.77%.

In a couple of weeks, **if you want to sell a home within the City of Austin that gets its power from Austin Energy, you could bear the cost of a new hurdle enacted by the City Council**.

Homes ten years old or older at the time of sale will be required to have a **home energy audit**, conducted by a certified auditor. The audit will assess the energy efficiency level of the home and it must be **provided to prospective buyers prior to sale**. The Energy Conservation and Disclosure Ordinance goes into effect 6/1/09.

There are certain exemptions, such as condos. Also, homes that have received three energy efficiency improvements or rebates totaling $500 or more within the last ten years through the Austin Energy residential energy efficiency program. But, by and large, **owners of the huge majority of homes sold within Austin after 6/1/09 will have to pay for the audit – and disclose the results to buyers**.

It's not just homes impacted by this ordinance. **All *apartment complexes* ten years old or older are required to have an energy audit by 6/1/11**. And those multifamily units identified as high energy users will be required to make energy efficiency improvements within 18 months to bring the property to within 110% of the average.

And *non-residential facilities* ten years old or older? They are required to **calculate an energy use rating for each building**, **no later than 6/1/11**. Properties with poor energy use rating are encouraged, but not required, to make energy efficiency improvements.

For more info, and for a list of **certified energy auditors** for residential, apartment buildings and non-residential facilities, you can go to www.AustinEnergy.com.

Dr. Louis Overholster says there are three kinds of pension plans: the *defined benefit* plan, the *defined contribution* plan and the one where all of your money goes into the stock market – the *defined poverty* plan!

Sincerely

Neal Spelce

Editor/Publisher