

Volume 32, Number 12

June 18, 2010

Dear Client:

Without question, the homebuyer tax credit that expired in April stimulated a certain amount of demand for residential real estate. But something else is going on here. Consumer confidence appears to be returning.

Let's take investment property as an example. **Robert Grunnah's** Castle Hill Investments sells more duplexes, by far, than any other firm in the Austin area. He reports that "90% of our duplex sales in 2008 and 2009 were to owner-occupant buyers taking advantage of 35% down payments via FHA loans. **Investors largely shied away from the market.**"

"However," he said, "**so far in 2010, 20% of the buyers of our listings are again investors.** Owner-occupants buy because they have to have a roof over their heads. *Investors buy because they believe values are going to appreciate.*"

He also pointed out that during the first quarter of 2010, "residential real estate sales volume increased 33% over the same period last year. **More importantly, pending sales are up 47% from last year** (signaling a reduction in supply and near-future price appreciation)."

"What really moves real estate values," he said, "**is economic growth, new jobs and 'in-migration' of the employees required to fill those jobs.**" He exaggerated a bit when he observed that we can't seem to go a day without another company announcing the creation of jobs in the Austin area. But the recent spate of such announcements reinforced his view.

"My prognosis for the remainder of 2010 is best summarized as 'steady as she goes,'" he commented. "Lenders are still for the most part a royal pain in the ass and firstborns are often still being required as additional collateral. **But deals are closing, and buyers with good credit, jobs and a strong stomach are buying properties at a steady clip.**"

"If we finished this year with neutral appreciation (no gains, but no losses), I would be delighted," Grunnah said. "**2011 looks like it will be better than 2010.**"

Grunnah also opined about some "what ifs" that may impact the Austin area real estate market. We'll take a look at those thoughts in the next item.

A couple of “what if” factors may impact the immediate future for return on residential real estate investment – one national, the other local.

According to **Robert Grunnah** of Castle Hill Investments, 2011 will be a much better year for residential real estate investment IF — and this is a big IF — “the government manages to finally get serious about reducing the budget deficit. **Failure to do so,**” he says, “**will likely cause ballooning interest rates, which will in turn make real estate less affordable.**”

“Investors need to watch the budget deficit debate closely after the November elections, because capital gains rates are likely to increase,” he continued. “I expect a flood of sellers when this happens because **the impact of a 10% increase in the capital gains tax could trim \$20,000 off the profit of selling a \$200,000 duplex. Ouch!**”

Another factor that will temper Austin real estate investment values over the next two years is a growing **pent-up supply of inventory that sellers plan to sell** in the near future.

“I have at least 300 clients that are waiting for conclusive proof that prices are going up before they list their properties,” Grunnah said. “When the inevitable increase in values becomes apparent, **this supply of inventory coming on the market will temper price increases for a while** – at least until the pent-up supply has been sold off, and we again have a shortage.” How long will this take? “My guess is this happens again in 2012.”

How has Grunnah done so far this year? “**So far in 2010, we’ve sold 61 duplexes worth almost \$10 million.**” And he said the final sales prices were 99% of list price.

One way to bypass the stringent loan requirements in Austin area residential real estate transactions is through seller-financing. But rumors are going around that, under a law that went into effect a few weeks ago, seller-financing is no longer allowed. Wrong!

Seller financing is still allowed in virtually all residential real estate transactions.

However, as of 5/31/10, anyone who provides seller-financing for a one-to-four family residence must be licensed as a Residential Mortgage Loan Originator (RMLO). There are two exemptions: 1) a person selling his/her primary residence and 2) a person selling to a family member.

Seller-financed transactions involving investment property, second homes, and vacation homes require licensure as a RMLO. This does not mean a real estate agent or a broker be licensed as a RMLO, *unless the seller is also a real estate agent or broker.* The new law applies only to the person providing the seller-financing. (Also, sellers do *not* have to be licensed to provide financing for commercial real estate or unimproved property.)

An interesting struggle is being waged in the skies over the Austin area as two airlines vie for the #3 ranking in total passenger traffic at the Austin airport.

The contest between Continental Airlines and Delta Air Lines is not a quest for total dominance at Austin-Bergstrom International Airport (ABIA). After all, Southwest Airlines has carried that mantle for years and in April 2010, **Southwest carried four times as many passengers as Delta and almost four times as many as Continental.** American Airlines, #2 at ABIA, more than doubles Continental and Delta in passenger traffic.

What is interesting to watch is the race for third place. **Continental is currently in 3rd** at ABIA with a 10.3% market share in April and Delta is close behind with a 9.7% share of the April Austin passenger market. But those percentages don't tell the whole story. **Continental is losing market share while Delta is gaining.**

Look closer at the April tally. **Continental was down 11% while Delta gained a whopping 60%** to lead all airlines in percentage increase at ABIA. And it is not a one-month aberration either. From January through April 2010, Delta's passenger totals are *up* an amazing 80% while Continental's traffic totals are *down* 8% for the year-to-date.

How do the percentages translate into warm bodies in the airline seats? **Year-to-date, Continental carried 269,852 passengers while Delta carried 254,815.** And the gap is narrowing. But there is another twist to the story.

Right now, as we have reported recently, **Continental is in the midst of a merger with United Airlines**, and it is possible a lot of corporate energy has been drained from a local passenger marketing effort. So this could be part of the explanation for Continental's lackluster showing.

However, Delta's rush to gain the #3 Austin market position could be derailed. **And 3rd place could be occupied by an entirely new name.** How? If/when the Continental/United merger is consummated, the new entity will fly under United's banner. And if you add United's year-to-date Austin passenger totals (149,784) to Continental's (269,852), **the combined total of 419,636 for the "new" United would skyrocket past Delta's 254,815.**

Well, would those merged passenger totals be enough to displace American Airlines who has had a lock on the #2 position for years? No, American's totals year-to-date of 553,153 give American a comfortable margin. And, of course, the Big Dawg at ABIA is not worried about losing its lofty perch. Southwest, is far and away the most active ABIA carrier with a year-to-date total of 981,693 and it continues to show increased year-over-year passenger numbers. **So, when the merger is complete, it should stack up this way at ABIA: #1 Southwest, #2 American, #3 United and #4 Delta – all with double-digit market share.** The market share for rest of the ABIA carriers should still be in single-digits.

Okay. With the official forecast that one of the more active hurricane seasons on record is just beginning, what's the Austin area weather outlook for July, August and September? Hot and dry? Or hot and wet?

Hot, for sure. But there's a bit of disagreement over how wet it may or may not be. This week (6/17/10), the National Weather Service's (NWS) Climate Prediction Center issued its monthly and seasonal outlook for temperature and precipitation. For Central and South Texas, **the outlook calls for above-normal temperatures.** "No surprise there," said **Bob Rose**, meteorologist for the Lower Colorado River Authority (LCRA).

But there's some divergence of opinion on *precipitation*. The NWS outlook calls for **above-normal rainfall** for Central, East and South Texas. Weather Service forecasters explain their **forecast for above-normal rain comes in part from a forecast for above-normal tropical activity this summer and fall.** "We shall see," said the LCRA's Rose.

He explained: "**For me this is quite a surprise** since none of the long-range forecast models are calling for above normal rainfall across our region. In addition, the Jet Stream pattern, which set up over the past couple of weeks combined with the growing trend toward La Nina, **both point toward somewhat drier than normal weather.**"

Obviously, the NWS forecast is **predicated on the possibility of tropical storm or hurricane activity in the Gulf of Mexico.** If you look at the NWS map of above-normal precipitation, it follows the arc of the Gulf Coast and covers about 200 miles inland along the arc. Remember, no hurricanes hit anywhere in the US last year. But, the current forecast calls for **eight-to-14 hurricanes to form, with three-to-seven of those bringing sustained winds of 111 mph or higher.** And the greater likelihood of storms brings an increased risk of a landfall.

Dr. Louis Overholster complained to his dentist about the high price for pulling his tooth, saying it was just a few minutes work. The dentist said "Well, Louis, if you prefer, I can pull it out slowly!"

Sincerely



Editor/Publisher