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Dear Client:

In the past few years, too much house was bought, too many cars were sold, too much debt was put on credit cards. Then credit tightened. Now it's loosening. So what are your fellow consumers and businesses doing now?

They're sitting tight. In general terms, **the consumer is exhausted and businesses are hoarding cash. They're waiting. Just waiting.** Small businesses and consumers mostly depend upon loans from banks. Tight credit has kept households from spending more and small businesses from hiring more.

Now, after almost two years when banks were bailed out by the Feds, banks seem to be loosening up credit a bit. According to the Federal Reserve Bank's latest quarterly survey of banks' lending practices recorded during July 2010, **for the first time since 2006 banks are making commercial and industrial loans more available to small firms.** And about one-fifth of large domestic banks have eased lending standards.

Want examples? Banks are reporting that they **stopped cutting existing lines of credit** for commercial and industrial firms for the first time since the Fed added the question in its survey in January 2009. Banks are also reporting some are **easing standards for approving consumer loans.**

But where are the borrowers? Hunkering down, that's where. Just when credit becomes more available, **there seems to be little evidence of customers rushing out to go deeper in debt.** In fact, the Federal Reserve Bank of Dallas says the financial services sector throughout Texas found **more companies are making deposits and improving credit quality.**

Different theories abound about why this is true. But "*uncertainty about the immediate economic future*" and "*still feeling the pain from the most recent economic upheaval*" seem to be at the core of this situation. This lack of interest in borrowing has generated other results.

The amount consumers owed on their credit cards during the three months ended in June **dropped to its lowest levels in more than eight years.** Balances are being paid down, or off. At the same time, **personal savings have risen to 6.4% of after-tax incomes.** This is three times higher than it was in 2007. It'll be interesting to see how long all this lasts.

With all this talk about financial gyrations, what about mortgage interest rates? Where are they headed?

Good question. Anybody have a crystal ball? When you get down to it, mortgage interest rates are a major driver of home sales. After all, **the size of the monthly payment triggers whether a buyer can afford to buy a house.** It's really what matters most to many buyers.

Let's look to Mission Mortgage's **Mark Sprague** for some guidance and a little bit of analysis. What about today's rates? "We took today's rates and translated them into a payment on a \$200,000 loan," said Sprague. "We also did the same thing with rates from August 12th 2010 and rates from February 11th 2010."

"Since we have been tracking these numbers, **this is the first time a 30-year loan for a \$200,000 house has dropped below \$1,000 a month**, he said. (He also said "it almost reminds me of those misleading ads from shady mortgage brokers I used to see a few years back.") Then he said that compared to February 11th, a payment is down \$72.17 a month, for a drop of 6.83% — a fairly substantial drop over a six month period.

Okay that's what is going on *now*. But the big question is **where are mortgage interest rates going?** Are they going to continue to drop even more or return to normal levels?

"For now," says Sprague, "it looks like **the government is going to do whatever it can to keep mortgage rates as low as possible**, since the economy is being dragged down by a weak housing market."

"For the time being, it's doubtful that mortgage rates are going to rise," he added. "As long as the economy remains weak and the government remains interested we will see **incredibly low mortgage rates and might see them fall a little further.**"

"It's hard to know how much they could fall since we are in uncharted territory," he points out. "**But once the economy recovers we will see rates rise, perhaps rapidly.** Rates are at an unnaturally low level and they will not stay this low forever."

Yeah, Mark. But let's get to the bottom line. Pull out your crystal ball. **When will mortgage rates begin to move upward?** "We don't know," he said. But he also added this observation for those sitting on the sidelines waiting to buy a home: "If you wait, you may be disappointed when rates turn up."

While the Austin area economy is heavily dependent upon a strong residential real estate market, **the local housing market is in large part driven by forces outside its control — such as interest rates.** So keep an eye on the national picture as you assess the local economy.

Retail sales are an important part of the local economy. If consumers and businesses are spending less because of the uncertainty, what is happening to Austin area retailers?

It's obvious. Central Texas retailers are not thriving. But, according to one important indicator, **area retailers may be bucking the national trend.** On Tuesday, a report was issued that pointed out US retail sales rose for a second consecutive month – but at a slow rate. It's a different situation in Austin.

Sales tax receipts are a great indicator of what is going on at the retail level.

After all, these are cash dollars paid in large part by consumers to retailers and then that money is sent to Austin for the State Comptroller to disburse a share of the income back to the different taxing entities such as cities.

It is an indicator that lags by a few months. **The latest numbers reflect sales in July**, sent to the state in August and reported in September. The August sales results will not be released by the Comptroller until October 8th 2010. So the just-released sales tax figures do **not reflect the normally-high back-to-school sales.**

Still, the picture is brighter than it has been. For instance, **the City of Austin's sales tax allocations that reflect July sales are 8.4% greater than July 2009.** Travis County's rose 7.7%. While it may be interesting to compare to the previous month, that comparison is not as meaningful as analyzing the change from last year because retail sales go in cycles throughout any given year (*big end-of-year holiday sales, slow first-of-year retail sales, etc.*).

This impressive increase is not limited to the City of Austin and Travis County. For instance, **Georgetown's receipts were up 15.2%, to lead the immediate Austin area.** Bastrop weighed in with a 7.3% increase, while the burgeoning retail sector in **Bee Cave** contributed a 6.8% increase in receipts over the same period a year ago. The other area increases were recorded in **San Marcos**, with more sales than any city other than Austin and Round Rock (because of several outlet malls, +3.7%), and growing **Pflugerville** (+2.7%).

As with almost any economic study, for whatever reasons, **some areas do not fare as well as others**, even though they are in close proximity. **Marble Falls** was off -2.0% from a year ago, **Cedar Park** was down -5.5% and **Round Rock**, that relies heavily on taxes from sales by Dell, Inc., was down -17% from a year ago.

From a state of Texas perspective, this report closed out the state's fiscal year. And the **sales tax collections for the state were about 7% below what as projected.** The state, of course, budgets in two-year cycles and as this wraps up the first year of the biennium, there is still one more year to play "catch-up." But the "catch" is that the Texas Legislature meets in January to work on the next two-year budget. As a result, there may be some adjustments ahead.

What can you look for in the Texas Governor's race as the pace picks up in a dash to the finish line Election Day, November 9th? Absent an October Surprise, the betting odds favor Rick Perry's re-election.

One of the reasons for this suggestion is that Perry will soon start to hammer home the strategy that led him to a surprisingly-large margin of victory over USSenator **Kay Bailey Hutchison** in the GOP primary. And if you thought it worked well against Hutchison, it could be **much more effective against his Democratic opponent, former Houston Mayor Bill White.**

Hutchison ranked very high in the polls prior to the primary and she labeled herself a conservative, but **Perry linked the GOP Senator to everything that a Texas voter could thing was wrong with Democrat-controlled Washington.**

Just imagine what Perry's campaign strategists will do to White, a Democrat who served in a Democratic administration in Washington prior to serving as Houston's mayor. One GOP wag suggested that when the race ends, **you will think Bill White and President Obama are joined at the hip**, even though White studiously avoided being seen with Obama on a recent Texas visit.

Up to this point, the race for governor has jogged along slowly around such **lukewarm issues** as "will Perry debate?" and "will White release his tax returns?" — *not* topics that drive voters to the polls. But hang on. This is about to change.

According to the latest UTAustin/*Texas Tribune* poll, Perry is ahead by 6 points, with a large 22% undecided. Most of the "undecideds" are independents who are not moved by "debating" and "tax returns." But they are moved by the mood being expressed nationally, **summed up simply as anger at Washington.** Here is where Perry should have a big edge over White with those independent undecided Texas voters. Keep an eye on this.

Dr. Louis Overholster points out political name-calling has always been with us, noting what Theodore Roosevelt said about William Taft: "He is a fathead with the brains of a guinea pig!"

Sincerely



Editor/Publisher