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Dear Client:

What is it about the Austin area that puts the region at the nation's forefront of remarkable cities? One factor could be Austin has the best of two worlds – worlds that, on the surface, appear to be polar opposites: a blue *liberal* city in a red *conservative* state. But with the best qualities of each.

Austin has the positive characteristics associated with *blue* city governments – **educated people, tech-oriented industries and racial diversity**. And it takes advantage of being the State Capital of a *red* state government that is **pro business, with low taxes and light regulation**.

Citing these factors, researchers **Joel Kotkin** and **Mark Schill** rank the Austin metro **tops in the nation with the most economic momentum going into 2014**. They point out the Austin area's double-digit growth in Gross Domestic Product (GDP), jobs, population and birthrate since 2007.

The Austin metro “has a very strong hipster reputation, **attracting many of the same people who might otherwise end up in Silicon Valley or San Francisco**, but it also boasts the low taxes, light regulation and reasonable housing prices that keep migrants well past their 30s,” they noted.

Not said was, that while Austin housing prices are rising here, they are still reasonable compared to California and other comparable locations. They also didn't state the obvious that **California's state government was nowhere near as business-friendly as Texas'**.

“Strong local economies attract the most people and create the best conditions for family formation, which in turn generates new demand,” according to Kotkin and Schill. “Strong productive industries drive demand for such things as health care, business services and retail, as well as single family houses, a critical component.”

Interestingly, Kotkin and Schill indicate the nation may be **on the verge of a “birth bounce” as millennials enter their 30s**. If so, they speculate these new families may likely settle in the regions they have already indicated that offer the most potential, such as the Austin area and other Texas metros such as Houston, Dallas-Fort Worth and San Antonio.

Optimistic predictions abound for the 2014 Austin area residential real estate market, but today – January 10th 2014 – marks the beginning of new mortgage guidelines that could have a profound impact on home sales.

Just this week, at a luncheon sponsored by the Austin Board of Realtors and the Homebuilders Association of Greater Austin, expert speakers were **positively glowing about a strong housing market in the Austin area in 2014** (with a few “be careful factors” tossed in). Longtime local economist **Angelos Angelou** spoke about a “growth spurt” in the *Austin American-Statesman*.

When you look at the recent records, the national attention draped around Austin and the local economic momentum, **you can’t really argue with these assessments**. Oh, you can talk about “what-ifs” such as how high will home prices soar and how bad the transportation situation will get. But they are not likely to become a tipping point in 2014.

There *is* one reality that will come into play, starting today. The full impact will not be known right away, but it is a factor to be closely watched. **January 10th is the day the grinding wheels of Dodd-Frank regulation begin to turn on the mortgage market**. Most folks outside of the lending business don’t fully understand what this can mean. Let’s let TexasA&M’s real estate economist **Mark Dotzour** ’splain it to ya.

“The new consumer-friendly mortgage underwriting rules have heavy penalties if the lender makes a loan, and then the homebuyer defaults on the loan,” notes Dotzour. So? **“If the homebuyer defaults on the loan he can prove he was not truly qualified for, he can sue the lender for making the loan in the first place.”** It’s been tough getting a mortgage loan, but it could get even tighter.

“The penalties for making a ‘bad mortgage loan’ are going up substantially for lenders,” Dotzour observed. “We will just have to wait and see how that impacts the sales volumes of homes.”

“There will clearly be growing pains as the mortgage industry adjusts to the new realities. Some will have the stomach for risk, and others won’t,” Dotzour noted. “Let’s hope this transition to the new regulatory regime goes smoothly.” The first key will be to keep an eye on the pending sales volume in January and February and see how those numbers compare with the same month the previous year.

What about those stories indicating some of the **largest banks have been laying off mortgage lending staff**? Was this in anticipation of the new regs? What does this say about the housing market? This reflects difficulties in the mortgage market, not the housing market, according to Dotzour. “What’s happened is that **as mortgage rates moved upward from 3.5% to current levels, the refinancing business collapsed,**” he said.

Austin area retailers saw a nice uptick in sales in November 2013 (the latest data available and just released Wednesday), according to sales tax reports. This is important because it marked the much-hyped beginning of a shortened holiday selling season.

Retailers report November sales tax receipts to the State Comptroller in December and the Comptroller rebates the local portions of that sales tax revenue in January. While there is revenue included in this report other than those from retailers, it is by and large a good trackable barometer of retail sales. **The report this week indicated a 3.9% increase statewide**, compared to the same period the previous year. By the way, this is the 45th straight month that Texas sales tax revenues have increased over the same period the year before.

The City of Austin's November 2013 sales tax revenue numbers outperformed the state by a whopping margin. **The amount of revenue rebated to Austin was almost 16% higher than for the same timeframe in 2012.** The increases varied widely throughout the 5-county Austin-Round Rock-San Marcos metro area – but almost all recorded dramatic increases.

Consider this random review of the increase in sales tax rebates, compared to the same revenue period a year ago: **West Lake Hills, up 19.5% ... Cedar Park, up 19.9% ... Leander, up 19.1% ... Pflugerville, up 12.9% ... Round Rock, up 7.1% and San Marcos, up 7.1%.** Impressive, indeed.

It will be interesting to check the December sales tax revenue numbers when they are released a month from now to see if this momentum continued for the rest of the retail selling season. Remember, for many small-profit-margin retailers, **the year-end holiday sales mark the difference between annual profits or losses.**

Once again, Austin ranks near the top of a national Top 100 list. But do you want to brag about inclusion as one of the nation's "drunkiest cities!" No kidding.

Men's Health magazine came out with a list of the 100 Drunkiest Cities in America. How did the mag come up with this designation? Well, it researched data that included **DWI arrests, binge drinking rates and incidents of liver disease.** Then it ranked them, with the drunkest city being #100.

Austin ranked 93rd! Only 7 other US cities were "drunker," including San Antonio that came in at 99th. Corpus Christi was 88th and El Paso 84th. The drunkest city in the nation, at #100, Bakersfield, Ca. The most "stone cold sober" town in Texas? The Dallas suburb of Plano, ranked 4th.

It's doubtful this list will be mentioned by those who tout Austin's assets.

The year-end announcement that Texas was one of six federal test sites for drones was greeted with huzzahs in the Lone Star State. Rightly so, because it was a vigorous competition.

The official name for drones is Unmanned Aviation Systems (UAL). The six states selected by the Federal Aviation Administration (FAA) , after detailed presentations, were Texas, Alaska, Nevada, New York, North Dakota and Virginia. **The impetus for the FAA initiative was primarily military in nature. But the results of the research will have enormous commercial implications as well.**

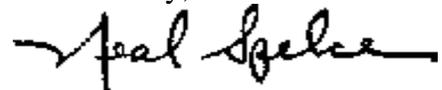
TexasA&M-Corpus Christi will manage the project that will be conducted over **11 Texas test ranges that incorporate diverse terrain and weather conditions**, such as Big Bend, Victoria, Bryan-College Station, Beeville and even the Gulf of Mexico. The kicker: the Feds didn't provide any money, so TexasA&M-Corpus Christi is rushing to raise about \$50 million to conduct this research. US Secretary of Transportation **Anthony Foxx said "these test sites will give us valuable information about how best to ensure the safe introduction of this advanced technology into our nation's skies."**

Drones are already in skies over Austin and elsewhere. **You may remember, the commercial development of drones is already taking place in Austin.** Go to the Archives button at the top of the page and click on Volume 35, Number 8, May 17th 2013 to read our in-depth report on why Austin and Texas were predicted to be on the leading edge of drone development.

This drone testing project is a big deal for Texas. For instance, **the state of Washington lost out on the bidding and it had a 10-member consortium making the pitch**, including the governor's office, several educational institutions, a national lab and two ports.

When **Dr. Louis Overholster** learned Amazon was considering using drones to deliver your orders, he wondered if, after your first drone arrives, five others will arrive with items Amazon thought you might also like.

Sincerely,



Editor/Publisher