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Dear Client:

There may be too much money chasing commercial real estate deals. And it's not limited to the Austin area. Other major Texas metros are caught up in this surge as well. What does this mean, especially when you consider a similar situation developed a half-dozen years ago?

First of all, anytime money is flying around – a lot of it, in this case – is much better than the alternative. **Better to deal with “lotta money” than to worry about “scramblin’ for money.” Make no bones about it, big bucks are being invested in Austin.** Just in the last couple of months, Parkway Properties became one of the largest landlords in the city by acquiring in one fell swoop more than 2.4 million sf of office space, including downtown's Frost Bank Tower.

The Austin area is almost perfectly positioned as this development unfolds. Its *international* reputation among the investor community is well-established. (Check almost any edition of this newsletter over the past few years for validation.)

We intentionally italicized *international* because **Japan, Europe and China have joined the US in printing trillions of new “dollars.”** For the most part, new construction has been stymied by tight credit in the US, so there are trillions of new dollars chasing US real estate – especially in “hot” markets like the major metros in Texas.

Mark Dotzour, Chief Economist/Director of Research for TexasA&M's Real Estate Center says “**the commercial real estate market has rebounded dramatically in just four years.** Prices are high and yields are low. **The asset class is still highly desirable for investors all over the globe.** China has decided US real estate looks a whole lot more attractive than bonds backed by the current US government. Rents are still rising and empty space is being filled.”

Austin provides a good example of what Dotzour is talking about. Consider office space alone. **The occupancy of office space in Austin is at the highest level since 2006** (caution: this was the year before the last recession began!). **Lease rates – at least for the good stuff – are the highest on record.**

“Look for commercial real estate prices to continue to increase in 2014 as more investor money crowds into the market,” he predicts. Check the next item to see which commercial real estate values are increasing at the fastest rate – office, retail, apartments, etc.

While final numbers are not yet available, it looks as if commercial real estate prices for 2013 will show a hefty increase over the previous year. So, where are the strongest price gains – retail, office, apartments?

Price gains generally follow land usage. For instance, land for industrial use is, in most cases, not as pricey as office or retail sites. Given that, it is not surprising that industrial price gains – while increasing at a solid 5% or so, still trail gains notched for other commercial usages, according to the COSTAR Commercial Price Index. **Retail is up by double digits, followed by office, apartments and industrial.** And, as in other cases, values are predicted to continue on an upward trajectory for 2014.

Speaking of apartment construction, could there actually be too much multi-family building in 2013-2014? One person who has been tracking building trends in Austin is raising that question.

Apartment development may start to slow, observes **Mark Sprague** of Independence Title. Multi-family building has surged in the Austin area, “but that’s likely to quiet down in 2015 as supply and demand may have swapped places – **and there may have actually been too much multi-family building in 2013-2014,**” he suggests.

On the residential real estate side, Austin area home starts are climbing and prices are up. But many builders can’t find enough workers.

“Austin and Texas have been adding construction jobs since mid-2012 and **some builders still can’t finish homes on time because framers, plumbers and even cleanup crews are in high demand,**” reports Independence Title’s **Mark Sprague**. “Many skilled workers from before the recession have moved to better paying oil and gas jobs or moved back to Mexico. Potential new workers failed to get into the pipeline because construction woes dragged on for so long.”

Also compounding construction problems is that newcomers aren’t arriving from Mexico, at least not like in the past. They used to be a crucial labor force for fast-growing businesses. **“Builders and subcontractors don’t want to be quoted on immigration, because it’s such a political issue, but they believe it’s a big factor in the labor shortage,”** says Sprague.

When all this is factored into the housing supply equation it just takes longer to build a house. Sprague points out a survey of builders locally shows the **average time it takes to start and finish a home in Austin has climbed from four months to over seven months.** It’s also taking builders longer to get permits because some local municipal governments have cut staff.

Never in the Austin area's recent history have there been so few homes offered for sale. Pause just a minute and think about this. Think about the good and bad economic ripple effects this causes in one of the fastest job and population growth areas in the nation.

Let's be clear. When the Austin Board of Realtors released its year-end figures this week about "so few homes" being offered, it was **analyzing the marketplace dynamics**. Oh sure, years ago, when Austin was much, much smaller, the number of homes offered for sale at a given time was low. But the smaller market was less dynamic and supply and demand was in balance. Not so now. The pressures being felt today were not present at that time.

Inventory is the key ingredient. **Inventory is determined by the length of time it would take to sell all the homes with a For Sale sign stuck in the front yard at the current rate of sales.** Texas real estate economists will tell you that a six-month inventory is the definition of a balanced market: neither the home *seller* nor the home *buyer* has an advantage. The pressures are roughly equal. **Currently the inventory is astonishingly low at two months. This is what is meant by "so few homes offered for sale."** This is a strong seller's market.

As you would expect, **home buyers are scrambling to buy a house and this is pushing prices higher and higher.** During 2013, 19% more homes were sold than in 2012, at a median price that increased by 9% over the previous year.

Well, what about high-dollar homes – those priced above a million dollars? Are their For Sale signs fading while signs at lower-priced homes say "Contract Pending?" Not at all.

All price points are selling. Of course, some are moving at a faster pace than others. But the **Austin area is the hottest big-bucks homes major metro market in Texas**, according to TexasA&M's Real Estate Center.

For the first 10 months of 2013, **439 luxury homes were sold in the Austin area -- up 55% over 2012.** This compares to San Antonio's increase of 8%, Dallas-Fort Worth's hike of 22% and the oil boom town of Houston, up 46%.

UPDATE: It still continues to fly below the radar, but the possibility of a Major League Soccer team in Austin is still very much alive.

Major League Soccer is on an expansion binge. The word is that within weeks a new franchise will be announced for Miami. Three additional new franchises could be added. **San Antonio has been out front in its effort to secure a franchise – Austin not as much.** Wait and see.

An announcement this week from the highest ranks of UT Austin's academia has down-to-earth practical economic consequences for the Austin area. It was the selection of the Dean for the fledgling Dell Medical School.

“Today marks a major milestone in the development of UT's Dell Medical School as we announce the selection of our inaugural dean,” said President **Bill Powers**. “I'm delighted that **Dr. Clay Johnston will lead the creation of a world-class medical school at UT Austin.**” Based upon what he said initially, Dr. Johnston understands the working relationship between academia and economic strength. **He talked about a “system where economics can happen.”**

“The critical element is bringing together businesses and the university to understand the culture and what the other is looking for,” commented the new dean, who will begin duties March 1st. **“It's going to be easy to create opportunities because Austin has tremendous strength in technology and biotech and is strong here and will be stronger.”**

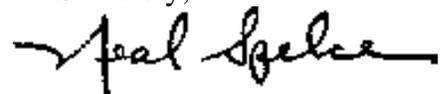
One of the driving forces behind the creation of a medical school, State Senator **Kirk Watson** said “if you talk with Dr. Johnston for five minutes, you can hear his excitement. **He envisions a top-flight medical school, built in partnership with this community around the demands of 21st Century healthcare.**”

Referring to a recent Travis County tax-increase referendum to move ahead with the medical school complex, Watson said **“we've invested a lot of money and emotion in this project,** he's (Johnston) the one who's going to realize that investment.”

“He knows what we hope to achieve. **He's creating a plan for achieving it. And he has the commitment, drive and intelligence to follow through,**” said Watson.

When **Dr. Louis Overholster** told a patient he wasn't sure of the diagnosis, but thought it could be due to alcohol The patient replied: “That's okay, doc. I'll come back when you're sober.”

Sincerely,



Editor/Publisher