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Dear Client:

Energy has long been the driver of the Texas economy and in the New Year it should pick up steam, keeping the state at the forefront. But water may be the biggest challenge facing the Austin area and the state. These two interrelated issues are essential to 2013's success. Let's look first at the energy component of the economy.

Once again, Texas is in the midst of a tremendous oil and gas boom. In fact, one estimate indicates 576,000 new jobs have been created so far and, talk about picking up steam, **nearly a million jobs are predicted by 2020.**

This same national analysis said the boom in Texas so far has also generated \$22 billion in new government revenue this year, with about half going to the federal government in personal and corporate income taxes. **The rest went to the State of Texas, local governments and the UTSystem's Permanent University Fund.**

Much of this boom time activity is occurring in the **Eagle Ford Basin that stretches from Austin to Laredo and across South Texas toward the Gulf of Mexico.** Hardly any oil was produced in this area in 2010 but now it yields more than 370,000 barrels a day of crude oil and condensates. And this boom is directly attributable to hydraulic fracturing, or "fracking," a controversial process that recovers oil and gas from miles below the surface.

With much fanfare, the Texas Legislature will reconvene in a matter of days in Austin for its every-two-year session and, thanks to the oil and gas boom, there will be **much more money in the state's coffers for the legislators to spend funding the needs of a fast-growing state.** And that's where Austin will get a disproportionate economic share. For instance, instead of laying-off state workers, it is likely state agencies will have expanding responsibilities. Even though the GOP-controlled House and Senate are expected to be miserly with state appropriations, the continuing fast increase in population may dictate a bigger budget.

Bernard Weinstein with SMU's Maguire Energy Institute was quoted in the *Dallas News* as saying "there's no question that the shale boom has been a real tonic for the state's economy. **It's a good thing for the state of Texas and it should continue unless policymakers in Washington screw things up**" with costly regulations. Speaking of policymakers, check out the next item about the Texas Legislature and the state's water problem.

With the Austin area's water supply low and getting lower and the state's prospects for rain dim for 2013, the Rainy Day Fund may be tapped by the Texas Legislature.

If early moves by the state's leadership come to fruition, the so-called Rainy Day Fund could easily be re-named the *No Rain-y Day Fund*, **at least for the portion that would be set aside for a proposed Texas Water Infrastructure Bank.** The Texas Legislature convenes in Austin 1/8/13 and one of the major agenda items concerns the state's dwindling water supply.

You don't have to go far to see an example of what is causing concern over most of the state. Nearby **Lake Travis**, the source for the city of Austin's water supply – as well as businesses, farms and residences all the way to the Gulf Coast -- is **currently about 37 feet below its monthly average.**

And because Central Texas is in the midst of a Severe Drought, Lake Travis is **projected to drop within five feet of its historical low set back in the drought of the 1950s.** That low, set 8/14/51, was almost 55 feet below the monthly average. So Travis could be 50 feet below average by June 1st with the dry July and August months still ahead.

Incidentally, the Lower Colorado River Authority (LCRA) that controls the water flow is moving apace to increase the availability of water in this area. This month, the LCRA board is likely to vote to **build a new reservoir in Wharton County and to pump groundwater from Bastrop County.**

Drought conditions are currently much worse in parts of West and South Texas. But it is a big deal to take \$1 billion or \$2 billion (as has been proposed) out of the \$7 billion Rainy Day Fund. **It would take a two-thirds majority of a penny-pinching conservative GOP House and Senate to approve Rainy Day Fund expenditures.** And the last four sessions of the legislature have tried and failed to fund a major water effort such as being proposed.

But the two men who wield the gavel and set the agenda in the Legislature – LtGov **David Dewhurst** and House Speaker **Joe Straus** -- are both on the record calling water a high priority. There are many moving parts to this water plan, but the effort is in a serious talking stage.

Interestingly, water and oil and gas are inextricably intertwined especially in the worst drought stricken parts of West and South Texas. The fracking process to drill wells takes about a million gallons of water per well.

You don't have to be a mathematician to understand that a creator of this positive economic climate in the state, **the current oil/gas boom, may be threatened if water solutions are not found and funded.** Also, the president of the Texas Association of Business **Bill Hammond** was quoted in the media as saying "clearly not having an adequate water supply will harm us in terms of bringing jobs to Texas."

The nuclear power plant that generates electricity for Austin, and is a major user of Central Texas water, is entering a process that could determine if it gets a 20-year extension on its licenses to operate its two nuclear reactors.

Two meetings will be conducted 1/15/13 in Bay City by the Nuclear Regulatory Commission to gather public comment for a key report that could determine the future operations of the South Texas Project. **One meeting covers environmental issues and the other will examine the plant's safety.** Because environmentalists opposed an aborted attempt to build two additional reactors at the STP site, it is anticipated environmental groups will speak in opposition.

Austin co-owns the STP along with San Antonio's CPS Energy and NRG Energy. **The City of Austin utilizes 16% of the plant's output to provide low-cost electricity for customers of Austin Energy.** The nuclear power plant is involved in a double-whammy as far as Austin's infrastructure is concerned.

Additionally, under contracts negotiated back in the 1980s, the Lower Colorado River Authority (LCRA) **releases water downstream from Lakes Travis and Buchanan to cool the plant's two nuclear reactors** in Matagorda County located on the Colorado River near the Gulf coast.

While this license renewal process is key to the ongoing operations of the STP, **the 20-year renewals would not go into effect until 2027 and 2028**, when the current licenses expire. Obviously no decisions are expected in the immediate future.

Just a few weeks ago, one of Austin's biggest employers that is pumping billions of dollars into its Austin operation, publicly reaffirmed its expansion commitment. However, rumors this week that are running rampant in Silicon Valley could impact Samsung Austin, if true.

As we have reported previously, it is known that Samsung Austin is manufacturing low-power processing chips for mobile products and other devices. **And it is generally accepted that Apple is one of Samsung Austin's biggest customers.** In fact an Apple exec confirmed as much without naming names in a recent *Wall Street Journal* report.

Now the rumor mill, fueled by a report in a newspaper in Taiwan, is that **production of the A6X chip that powers 4th generation iPads is to be shifted away from Samsung** to the Taiwan Semiconductor Manufacturing Company.

The reason this rumor is being given more credence than normal is there are probably **no two tech companies more at war with one another than Apple and Samsung.** They both have billions of dollars tied up in lawsuits against each other on multiple continents. And yet, Samsung produces most of the chips that power Apple's devices. Until now? Stay tuned.

Texas should have the largest residential influx of any state in 2013 for the ninth year in a row and, for the Austin area, this means pricey homes and apartments that are hard to find.

In many quarters, the Austin area could be said to have a healthy residential real estate situation. **Homes are quick to sell, apartments are quick to be rented.** Homebuilders are scrambling to build new homes, apartment developers are rushing to bring new units online.

Jobs, many of them good paying, are plentiful – attracting folks from all over the US seeking a better life. And yet, even as they move here by the hundreds, they gobble up the jobs so fast that the area unemployment rate dropped below 5% before the end of 2012.

This healthy economic situation is the envy of many. But it creates problems – problems practically every metro would love to have, but problems just the same.

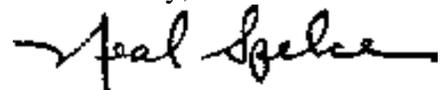
For instance, **there may not be enough shelter for those moving to the area** and this situation – based on construction timetables compared with the pace of incoming residents – **could continue for at least three years.**

As for prices, **the median and average prices of Austin area homes are already higher than those in Houston and Dallas.** Think about this. Those big humming metropolises are selling homes comparable to those in the Austin area for less than what sellers are receiving here. And, while the Austin area home prices are not soaring out of sight, they are **moving steadily upward with no sign of slowing** in the immediate future.

It will be interesting to see if the national rankings of the “best this” and “best that” for metros hold up once *current* figures are used in their calculations. But, for now, it is an example of the economic vibrancy of the area.

Dr. Louis Overholster’s New Year’s Resolution for 2013 is to take life with a grain of salt... plus a slice of lemon... and a shot of tequila.

Sincerely,



Editor/Publisher