The NEAL SPELCE AUSTIN LETTER

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Dear Client:

Is Austin's nation-leading fast population growth outstripping the ability to provide housing for those who live here? If so, could this push prices to the point that fewer can afford a home or even meet the rising apartment rents? Will Austin keep traveling down this road?

The key trend lines of **population growth** coupled with a **strong job market** along with **high demand** and **low housing inventory** indicate this could rapidly turn into a serious situation. And the ripple effect could have a significant impact throughout much of the Austin area economy – not just in the housing sector.

How serious is it? Consider that "in February 2013 Austin recorded one of its **lowest months of inventory since the year 2000**," said **John McClellan**, Branch Manager for Supreme Lending in Austin and the host of radio's *Real Estate Zone*. "**Inventory is at record lows and demand is surging**. This imbalance of supply and demand is causing **home prices to move up sharply** and, in conjunction, lack of supply on the rental side is causing **rental rates to spike**."

People need a roof over their head, so many will suck it up and pay the increasing costs (thank goodness mortgage rates are still low!). So the demand is not likely to subside anytime soon as long as Austin's population keeps increasing at what seems like warp speed.

However, in addition to the impact on buyers, sellers, renters and landlords, consider just one "ripple effect" factor: for most households, **the more money spent on housing, the less funds are available for other pursuits** – such as a new car, appliances, clothing, dining out, entertainment, etc.

Homebuilders are scrambling to put new homes on the market. But they have a long way to go to catch up. McClellan points out **new home starts declined from 17,000 in 2006 to 12,000 in 2007 and averaged only about 6,500 units per year between 2008 and 2011**. For additional perspective, the USCensus Bureau calculated the **City of Austin population averaged *increasing 70 people per day*** prior to 7.12.13. And while more recent numbers are not available, you can make a good case the pace is quickening. Talk about digging out of a hole that seems to get deeper, the harder and faster you try to clamber out! McClellan is concerned this may "**test the boundaries of affordability**. Yet, affordability in the Austin metro area is one of the things that makes it so desirable."

One positive element that helps tamp down the upward pressure on housing affordability is low interest rates. But mortgage rates have been inching up, to hit a high not seen in a year. Then, mid-week, Federal Reserve reports indicated, maybe, you ain't seen nothing yet.

During the last few weeks, long-term rates have been creeping higher. Nothing earthshaking, yet. But the **trend has moved from "level" to "rising**." So, what is likely to happen to this part of the all-important housing affordability equation?

The Mortgage Bankers Association noted mortgage interest rates rose last week to their highest point in a year due to an improving economy. The Federal Reserve's bond purchases have helped to **keep interest rates low and lure buyers back into the market**. As a result, all eyes were on Fed Chair **Ben Bernanke**'s pronouncements when the Fed met this week (Wednesday). So, what happened?

For now, nothing changes. The Fed said this week it will continue to purchase $85 billion a month in Treasury securities and **purchase mortgage-backed securities, in addition to holding short term interest rates near zero**. However, Bernanke laid out a timetable when he said the Fed will stop buying bonds.

And that caused the stock market to dramatically nosedive immediately! The Fed head said it will probably **end its bond purchases *entirely* by the middle of *next* year** – if unemployment continues to decline at the pace the Fed expects. And that's not the only negative.

Bernanke likes to use driving-a-car analogies. He said it will be like letting up on the gas pedal. That means **pulling back on asset purchases later *this* year**. And this apparently scared the beejeezus out of the stock market! **Their fear is that interest rates – car loans, business loans, mortgages – will rise quickly**.

What should you look for? Bernanke said the Fed plans to continue the asset purchases **until the employment rate falls to about 7%**. (The national rate stood at 7.6% in May.) This is **the first time the Fed has specified an economic objective** for bond-buying. In a separate forecast issued at the same time, Fed officials predicted the unemployment rate will decline more quickly than they had previously expected, **falling to 6.5%-6.8% by the end of 2014**.

The Austin area is more than doing its part to pull down the nation's unemployment rate. The metro's 5.1% unemployment in April was waaaay below the national average.

In fact, the 5-county Central Texas metro tally **dropped from 5.6% at the same time a year ago**, while the entire state of Texas notched a 6.1% unemployment. Houston and San Antonio are leading the big-metros-other-than-Austin parade. Check out the next item.

This is a success "Tale of Two Texas Cities" not named Austin. Houston (obvious) and San Antonio (maybe not quite so obvious) are gaining almost as much national notoriety for economic prowess as Austin.

The headline in a recent national issue of *The Atlantic* magazine said it all: "**Houston Is Unstoppable: Why Texas' Energy Juggernaut is America's #1 Job Creator**" **…** among the ten largest metros in the US (Dallas, by the way, was #2 on this list -- but that's another story).

> The article went on to exult: "The ten largest metros have recovered 98% of the jobs lost during the recession, on average. But Houston, the first major city to regain all the jobs lost in the downturn, has now **added more than two jobs for every one it lost after the crash**. That's incredible."
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> So, how come, asked *The Atlantic*? "With its proximity to oil and Mexico, **Houston is blessed by topography and geography**. But the secret sauce of the city's success might be something else: history – and an **ability to learn from past mistakes**." The past mistakes referred to the previous oil boom/bust and the real estate recession in the 1980s.

San Antonio is also a whole 'nother success story, especially because many seem to think of The Alamo City as driven by **tourism**, **military bases** and **manufacturing**. This is still the case, but the "new" San Antonio has added **big oil**, a billion dollar **hosting and cloud-computing company**, along with a strong base of **healthcare** and **high tech industries**.

> Big oil? San Antonio? Yep. San Antonio is emerging as the **de facto HQ** for companies involved in the **wildly-successful Eagle Ford shale oil play** in South Texas, and it claims this oil role has created at least 4,000 jobs in San Antonio. Health care jobs have expanded greatly, especially because of UTSanAntonio's emphasis and reputation in that area.
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> Additionally, some are saying the hosting and cloud computing company, **Rackspace**, **is to San Antonio what Dell Inc**. **was to Austin in the early 90s**. It was reported that from 2006 through 2011 San Antonio notched a 23.6% growth in high tech jobs, while the national rate was 1.4%.

Obviously there's much more to bolster the economic success tales of these two Texas cities. Take that as a given, then add Austin, Dallas, Fort Worth and even El Paso to this mix and you get a situation *The Atlantic* described this way: "**Texas is killing it**. **It dominated the recession** … **crushed the recovery**."

Texas has six of the nation's 20 biggest cities (Austin just moved into the #11 spot). It's well-documented the **big cities are major magnets for job growth and population increase**. And each of the Big Six Cities in Texas has its own personality, with economic success in common.

Seems like everywhere you go, you see retail giants Walmart and Target, don't you? Well there is another national retailer catering to the value shopper that has 37 outlets in the Austin metro, and the odds are you can't quickly call its name. Okay, time's up.

And the reason you may not quickly identify this national retailer is that its stores go where Walmart and Target seldom go. **Small communities. In some cases, *really* small communities.** Like those with less than 1,000 population, many with only 300-500 residents. Give up? We're talking about the "**Dollar**" **stores that have roots going back to the five-and-dime Woolworth's that opened for business in 1878 under the banner "Woolworth's Great Five Cent Store.**"

There are more "Dollar" names than you can shake a stick at. **In Texas, Dollar General is most common (1,109 stores), followed by Family Dollar (946 stores), then Dollar Tree (268 stores).** The remainder are all over the ballpark – Lucky Dollar, Dollar Savers, Dollar Depot, King Dollar, Just a Dollar, Dollar Plus, etc. A total of well over 2,000 in Texas alone and 20,000 nationwide.

And here's the neat thing about this. Walmart and Target can't make a go of it in really small towns. **So the Dollar stores meet the needs of those who choose to live in smaller towns.** After all, those residents need to shop, too.

Based on one measure of retail viability, **the Austin metro could support more Dollar stores.** In fact when you consider the entire state of Texas the Austin metro has more people per store than any other metro in Texas. **The average population per Dollar store in Texas is 8,256. Austin's 37 stores serve 21,362 per store**, according to the TexasA&M Real Estate Center.

Dollar General states the median income of a community in which a store will be located must be ***less* than $75,000.** Interestingly, **there is no *lower* threshold, only an *upper* one.**

Dr. Louis Overholster suggests that shopping is cheaper than a psychiatrist and he agrees with **Oscar Wilde** who said that anyone who lives within their means suffers from a lack of imagination!

Sincerely,

Neal Spelce

Editor/Publisher