Short-Term Economic Forecast

With a Real Estate Emphasis

City of Austin

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Near-Term Economic Context

National Overview

- U.S. economy continues to expand at solid pace, but concerns remain about sustainability.
- On the upside: business investment, profits, and consumer spending (partially due to historically low interest rates) have contributed to economic growth that is comparable to the late 1990s.
- On the downside: rising prices (especially for energy), sluggish hiring, and tighter monetary policy all suggest that recovery is somewhat fragile.
- Near-term forecast: GDP up 3% this year, with growth in the 2.5-3% range over the next five years.

Near-Term Economic Context

Austin Overview

- All aggregate indicators of the Austin economy are very positive at this point – job growth, tax revenue, retail sales, building activity, etc.
- Virtually every sector is growing, with the exception of manufacturing – should change in the near future.
- In-migration and economic recovery have combined to create record levels of activity – reminiscent of several past booms.
- Real estate and construction are especially hot, and deserve more detailed attention.

Near-Term Economic Context

Real Estate Focus: Single-Family

- Volume of homes sold and median/average prices reached record highs in 2005 – no sign of slowdown this year.
- Months of available inventory (3.8 currently is the lowest in Texas) is dwindling to levels of the late ’90s – suggests that demand continues to outstrip supply, and 2006 will therefore see more price increases.
- Underlying fundamentals remain solid – economic growth should help offset any impact associated with higher interest rates.
- Diversity of product continues to increase – both in the aggregate and in different parts of the region.

Near-Term Economic Context

Real Estate Focus: Housing Market Comparisons

	Change in Housing Inventory	Recent Price Trend	Employment Outlook
Atlanta	15%	▲	Strong
Austin	-12%	▲	Very Strong
Chicago	28%	▲	Average
Dallas	0%	▲	Very Strong
Denver	19%	▼	Strong
Detroit	46%	▼	Very Weak
Houston	3%	▲	Very Strong
Las Vegas	24%	▼	Very Strong
Los Angeles	149%	Flat	Weak
Miami	236%	Flat	Weak
Minneapolis	43%	▼	Weak
New York	70%	▼	Weak
Philadelphia	39%	Flat	Weak
Phoenix	282%	▼	Very Strong
Seattle	5%	▲	Very Strong
Washington, DC	230%	Flat	Strong

Near-Term Economic Context

Real Estate Focus: Apartment

- Rents, occupancy, and absorption all set records during 2005.
  - Year-end occupancy at 94.4%, up 1.7% from June.
  - Average rents at $0.85/sq.ft., up $0.03 from June.
  - 6,243 units absorbed during 2005.
- At this point, projects under construction are scheduled to deliver 2,820 units during 2006, suggesting that occupancy and rents will both continue to rise.
- Rising interest rates could tilt demand slightly back toward renting, although may not be a discernable impact.

Near-Term Economic Context

Real Estate Focus: Office

- Rents, occupancy, and absorption all set records during 2005.
  - Year-end “direct” occupancy at 85.7%, up 2.6% from June.
  - Total absorption of over 1,058,000 sq. ft during last six months of 2005.
  - Rents rose 4.1% over the same period.
- At year’s end. Class A averages $23.61, Class B at $17.82, Class C at $14.17. CBD has highest rates, at $25.10 for Class A.
- Inventory of sublease space has fallen to a four-year low of just over 270,000 sq. ft., underscoring the return to more normal market conditions.

Near-Term Economic Context

Real Estate Focus: Retail

- The ten-year trend of retail defying the cyclical pattern of office and industrial continues, with strong rents and occupancy
  - Year-end “direct” occupancy at 93.27%, down slightly.
  - Total absorption of over 1,180,680 sq. ft during last six months of 2005, again slightly down from previous six months.
  - Rents rose $0.28 over the same period.
- Job and population growth should continue to stimulate development – watch for growth in the middle and outside the “donut.”

Austin Forecast

Near-Term

- Continued growth in the national economy, economic development success, and migration to the region should all contribute to strong growth for the foreseeable future.
- Economic activity begins to replace the impact of low interest rates – no signs of change in the near term.
- Forecast is for MSA job growth this year to be up 3.4% (23,700 jobs). Personal income will rise 8.2%; MSA population will reach 1.45 million.
- Most rapid growth is in sectors related to trade and development, but all sectors projected to have employment rise by at least 2%.

Austin Forecast

Longer-Term – Keys to Future Success

- *Continued migration to the region and downtown*.

  Population growth tends to follow the local economic cycle to some degree, the longer-term outlook is for Austin to remain an attractive site for relocation, especially for those whose income is not tied to the local economy. Attraction of people is arguably as important to Austin's economic future (and tax base) as attraction of firms.

- *Maintenance of the current "hard" technology base*.

  Given the increasingly competitive environment for semiconductors and other manufactured technology products, the recent announcements of several expansions and relocations bodes well for the future of "hard" technology in Austin.

- *Growth in activity related to research and development and creative industries*.

  While the creative sector has hit Austin's economic development radar screen, the business side of the equation has yet to reach its full potential. Meanwhile, activity related to medicine may soon join more traditional areas of R&D where Austin enjoys a concentration of activity.

- *Regionalization of the "local" economy*.

  A number of regional events will have an economic impact on Austin, as the Toyota and Washington Mutual locations to San Antonio, ongoing growth of higher education in the area (witness Texas State in Williamson County), and efforts to enhance transportation infrastructure (both rail and highway) will all influence the longer-term outlook.