

# Austin positioned to hold up as national economy heads toward recession

## Universities, strong companies, state government help stabilize area's outlook.

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The Austin area's booming job market has slowed to a three-year low, and its once sizzling real estate market is cooling fast.

One of the region's few planned initial public offerings has been put on ice, and the biggest purchase of an Austin company in 2007 — Capital One's \$700 million acquisition of NetSpend — was abruptly called off amid the national credit crunch.

Those would not seem to be promising omens for 2008, especially when some experts say that the national economy, battered by plunging home sales, soaring oil prices and a credit meltdown, could be headed for recession. But there are other forces that could sustain Austin's economy, even if the national economy tanks.

**Among the cushions: Strong local companies such as Silicon Laboratories Inc. are expanding, and the region's biggest investment ever, the new \$3.5 billion Samsung Electronics chip plant, is cranking out products at an accelerating pace, bolstering the region's important semiconductor industry. A skilled local work force continues to attract new companies. Google Inc., for example, is on the verge of opening an Austin development center. Venture capital continues to fund promising startup companies in fields ranging from cutting-edge semiconductor design to Web software tools, creating the foundation for more job growth. Austin Ventures, the dominant source of money for local startups, is raising money for a \$600 million fund, its first new fund since 2005.**

But Central Texas won't be able to avoid the national fallout entirely, said Bud Weinstein, director for the Center for Economic Development at the University of North Texas.

"When you've got a national economy with very weak legs, it's a given that Austin will slow down right along with everyone else," he said.

As a result, the region's high expectations could be tested this year, Weinstein said.

"Austin has gotten used to having a supercharged economy and a very low unemployment rate, and when things slow down a bit, you think you're having a depression," he said.

But thanks to Austin's broad technology base, as well as state government and the University of Texas, which keep going even in the worst of times, the region is well-positioned to weather a storm, Weinstein said.

"In reality, it's not gloom and doom by any measure. Of all the markets I'd want to be in given the current economic uncertainty, Austin would be at the top," he said.

Chip plants produce

Last month, Samsung's new Northeast Austin plant, which sprawls over an area bigger than nine football fields, began churning out flash memory chips.

The largest semiconductor factory in North America has created 900 jobs with an average annual salary of \$63,000, and the project is expected to spur an additional 2,800 secondary and support jobs, according to a study for the Greater Austin Chamber of Commerce.

Across town, Silicon Laboratories is also in hiring mode. The chip design company, which has 430 employees at its headquarters on West Cesar Chavez Street, is negotiating to buy a neighboring six-story building.

Although the company hasn't yet said how many workers it's adding, its next wave of growth will happen in downtown Austin, where it is one of the largest private employers, said Jon Ivester, vice president of worldwide operations.

That kind of quality jobs could help buffer the local economy if the national picture gets uglier, said Edward Friedman, a senior economist at Moody's economy.com. The firm puts Austin at the top of the list in its periodic ranking of 381 cities based on the vitality of their economies.

"Given all of the outside factors that have yet to drag you down, Austin is still a powerhouse," Friedman said. "But if the national economy continues to weaken, that's the one thing that could hurt you."

The impact is already clear in the region's job market, which began to lose momentum late last year. In November, it slowed to a 3 percent annual growth rate, down from 4.7 percent a year earlier. Still, the work force was at an all-time high of 761,200.

Central Texas still has a healthier job market than many parts of the country. The national growth rate was 1.1 percent last year, and some economists say it could slow even more this year.

Austin's work force — its brains — will continue to be the region's best weapon against a possible national recession, attracting outside companies eager to tap into its tech savvy labor pool.

Google has declined to confirm the expansion, but it advertised late last year for an engineering director to lead a group of 100 or more employees. Real estate sources said the company is close to signing a lease for office space downtown.

Another factor working in Austin's favor in 2008 is venture capital, which helps determine the rate at which young companies are created and grow.

The year started on a shaky note, with venture investing in Austin companies hitting a nine-year low. But it ended on a positive note, with investing picking up and the arrival of three new Austin venture firms: Santé Ventures raised \$130 million to invest in medical technology and health care services, Emergent Technologies closed a \$27.1 million fund to commercialize technology developed in the University of Texas System, and PTV Sciences garnered \$190 million to invest in medical technology companies.

Money from those firms has already been invested in at least five Austin startups, with more to come.

"You're talking about a significant amount of funding looking at early stage deals, and that's where (Austin) has needed dollars for the longest time," said Tom Kowalski, president of the Texas Healthcare and Bioscience Institute, a trade group.

Housing weakens

What could trip Austin up? A weakening housing market is high on the list, and that appears to be happening. Builders are pulling back in the Austin area as the national housing market continues to struggle, according to recent reports.

**New home starts in 2007 were down nearly 20 percent compared with 2006, according to the latest analysis from Residential Strategies Inc. Starts for new homes haven't been that low since 2004.**

Home starts are expected to bottom out in 2008, said Mark Sprague, Austin partner for Residential Strategies. "What's happening is the rest of the national market is pulling us down," he said.

As lenders tighten their standards, buyers who once qualified are getting turned down. That means Texas, which never had housing bubbles like the East and West coasts, will still feel the pinch.

The region's housing slowdown led to the demise last month of a planned upscale 1,400-home subdivision near Parmer Lane.

Dallas-based builder Centex Homes canceled its contract to buy 465 acres of the 750-acre Pearson family ranch, where it was going to spend \$275 million to build one of the largest master-planned communities in Central Texas.

The resale market has been softening for months. October was the fifth straight month of declining home sales amid continued fallout from the national mortgage crisis.

**Sales of single-family homes** were down 15.4 percent compared with October 2006 and **were off 6 percent for the year to date**, according to the latest figures from the Austin Board of Realtors.

Austin's commercial real estate market, meanwhile, remains a wild card.

Office rents rose in the fourth quarter compared with a year earlier, but vacancies were up as well. Rents and vacancies are a key economic indicator because job growth fuels demand for office space.

Citywide, the vacancy rate was 14.4 percent, up from 12.5 percent a year earlier, according to Oxford Commercial. Rents citywide averaged \$25.98 per square foot, up from \$22.43 a year earlier.

The higher vacancy rate is due in part to new buildings that have no tenants yet. They include the Park at Barton Creek, two buildings totaling 210,000 square feet at South MoPac Boulevard (Loop 1) and Capital of Texas Highway (Loop 360).

Diana Holford, president of the Central Texas office of the Staubach Co., said it will take time for those buildings to fill.

"As you drive around Austin, you see a number of new office buildings under construction. Most of those buildings do not have any tenants signed up," she said. "If the economy picks up and Austin adds lots of

new jobs, there will be workers to fill those buildings. Otherwise, some buildings may sit empty for a long time."

2 public offerings set

Uncertainty also defines Austin's outlook for public offerings.

Creditcards.com, which allows consumers to search for, compare and apply for credit cards, had planned to raise up to \$185 million. But it delayed its offering in November, citing an unenthusiastic response from investors.

Two Austin companies remain on deck for initial stock offerings: Capstar Acquisition Corp., a shell company formed to acquire other businesses, has filed to raise up to \$230 million; and Convio Inc., which sells software for nonprofit groups, has filed for an offering that could raise \$86 million.

But those IPOs are about the only items on the agenda so far for 2008. Unlike last year, there are no new megadeals, no new Samsungs or giant retail projects such as Hill Country Galleria on the horizon.

Getting deals done — from public offerings to acquisitions to venture capital — will be challenging in 2008, at least in the first part of the year, said Nick Fox, an attorney with Vinson & Elkins who works with startups.

"Investors are being cautious, and they're reluctant to write checks until they know where the economy is headed," he said.

"I'm seeing them step to the sidelines, and it's going to take solid indicators that the economy's improving to get them back in the game."

**Courtesy of JB Goodwin**