VALUATION & ADVISORY

Self Storage Investor Survey

Fourth Quarter 2016

The survey data was collected as part of an online questionnaire that was sent to key self storage market participants during a two-week period at the beginning of October 2016. The market participants were asked to segregate their responses by Investment Class (A, B & C). Furthermore, the data collected is corroborated by the experience and knowledge of the Self Storage Industry Group team members at Cushman & Wakefield.

Cushman & Wakefield defines the Investment Classes as follows:

Self Storage Investment Classes

Class A

- Located in a top 50 MSA
- Market has high barriers to entry (through either lack of developable land or a lengthy entitlement process)
- Generally newer facilities in good condition with state of the art amenities including climate controlled units and secured facilities with gated access
- Professional on-site and off-site management
- Minimum size of approximately 75,000 square feet
- Good location with access to attract tenants willing to pay rents in the upper percentile in the marketplace

Class B

- Located in a top 100 MSA
- Market has typical barriers to entry
- Generally facilities built since 1980 in average to good condition with amenities typical for its market including secured facilities with gated access
- Full-time on-site and off-site management
- Minimum size of approximately 40,000 square feet

Class C

- Either located in a smaller market or in less desirable areas of a top 50 MSA
- Generally 1970s or 1980s vintage properties in average to below average condition
- Generally managed by the owner and may not have an on-site manager
- May or may not have typical amenities such as gated access, security cameras and/or climate controlled units
- May have secondary, less desirable locations with generally below average access and/or limited visibility

Cushman & Wakefield Self Storage Investor Survey Fourth Quarter 2016

	Class A	Class B	Class C
Going-In Capitalization Rate			
Average Low	4.54%	5.46%	6.44%
Average High	6.13%	6.73%	7.77%
Average Overall	**5.33%**	**6.06%**	**7.11%**
Terminal Capitalization Rate			
Average Low	5.35%	6.15%	6.96%
Average High	6.65%	7.27%	8.21%
Average Overall	**6.00%**	**6.71%**	**7.59%**
Discount Rate			
Average Low	7.95%	8.83%	9.50%
Average High	9.69%	10.46%	11.50%
Average Overall	**8.72%**	**9.55%**	**10.43%**
Average Marketing Time (months)	2.77	3.18	4.36
Average Rent Growth	5.07%	4.45%	4.22%
Average Expense Growth	2.75%	2.81%	2.60%

Source: Cushman & Wakefield Valuation & Advisory Self Storage Practice Group

Market Trends

- Capitalization rates have and are expected to continue to decline, although at a slower rate. As expected, the spread between each of the three classes range between approximately 50 and 100 basis points. The rates from our previous survey (Q2 2016) corroborate this conclusion, as the rates are slightly lower in each category.
- While overall portfolio transaction activity has slowed due to a limited supply of product coming to market, the sector experienced one of the largest portfolio transactions (iStorage) in the 3rd Quarter at $630 million dollars.

- Smaller portfolio transactions, particularly in the Class A and B+ product, have slowed due to the lack of good-quality supply. Therefore, interest in the acquisition of Class B quality portfolios has increased as investors are looking to place capital.
- There continues to be a significant amount of capital looking to be placed in the sector. High returns from the self storage REITs have attracted new market participants, and brokers report upwards of 10+ bids on good quality Class A and B asset sales.
- Buyers are recognizing the risk of new supply entering the market and may avoid deals where there is a significant potential for new supply.
- In trade areas experiencing new supply, some operators report that actual and market rents have decreased to maintain occupancy.
- Due to the influx of new supply, the REITs have lowered their growth projections for the foreseeable future. While the growth forecast has been tempered, self storage REITs are still projecting returns that are amongst the strongest of all the asset types.

Development Trends

- New construction continues to be at the highest levels since 2006. According to FW Dodge, the most active development markets include: New York-Newark-Edison (29 facilities), Phoenix-Mesa-Scottsdale (20), Denver-Aurora (19), Dallas-Fort Worth-Arlington (14), Miami-Fort Lauderdale-Miami Beach (14), Washington-Arlington-Alexandria (10), Nashville-Davidson-Murfreesboro (10), Houston-Baytown-Sugar Land (10), Charlotte-Gastonia-Concord (10) and Chicago-Naperville-Joliet (10). It is important to note that this information reflects the minimum number of potential facilities currently under construction, as F.W. Dodge does not report everything that is being built. Detailed information regarding the development pipeline is included in the Self Storage Performance Quarterly report produced by Cushman & Wakefield.
- The new facilities constructed in the top 50 MSAs are approximately double the size of the facilities built in secondary markets; these facilities also required higher direct construction costs on a per square foot basis. In addition to new facilities, expansion of existing facilities is also at record highs.
- In some new projects, physical absorption can be fast (12 months); however, economic absorption remains between 24 and 36 months for most projects.
- Acquisition when the Certificate of Occupancy (CofO) is received continues to be a popular option for both developers and operators, as the risk of construction and lease up is divided respectively.

Conclusion

The success of the self storage REITs continues to benefit the sector as a whole. Capital continues to enter the market, compressing capitalization rates and increasing values; however, the compression appears to be stabilizing. New market participants, as well as large operators, have started partnerships with developers to build new storage facilities. The supply of new self storage facilities is at levels not seen since the mid-2000s. With that, new supply is starting to impact the decisions of market participants; buyers may be wary of markets with potential new facilities, and developers are concerned about multiple new facilities in a trade area.

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