Q2 2019

Self Storage Investor Survey

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 end of July 2019. 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 20 Self Storage Practice 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 market place

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

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	Class A	Class B	Class C
Going-In Capitalization Rate			
Average Low	4.71%	5.80%	6.78%
Average High	5.75%	7.17%	8.38%
Average Overall	**5.23%**	**6.49%**	**7.58%**
Terminal Capitalization Rate			
Average Low	5.64%	6.08%	7.10%
Average High	6.77%	7.50%	9.60%
Average Overall	**6.21%**	**6.79%**	**8.35%**
Discount Rate			
Average Low	7.33%	8.43%	9.80%
Average High	9.33%	10.67%	12.00%
Average Overall	**8.33%**	**9.55%**	**10.90%**
Average Marketing Time (Months)	3.17	3.89	5.00
Average Rent Growth	3.50%	3.38%	3.63%
Average Expense Growth	2.13%	2.22%	2.13%

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

Market Trends

- The cumulative impact of excess supply continues to put downward pressure on occupancy rates and market rents, as facilities fight for market share in the near term. In trade areas where this is happening, it is uncertain whether the rates will stay at these lower rates or will increase to previous levels in the long term. Certainly more sophisticated operators will work to push these rates upwards as soon as the market allows.
- Buyers and lenders continue to recognize the risk of new supply entering the market and are more conservative in their underwriting where there is a significant potential for new supply. Most market participants report supply-side issues impacting the underlying fundamentals.

- Capitalization rates have stabilized, but could slightly compress in the near term due to the recent decrease in interest rates. There is still a considerable amount of capital looking to be placed within the sector.
- Investor demand for Class A trophy properties remains strong. Interest in Class B and Class C properties continues as investors are looking to place capital and available Class A and B+ product is limited.
- REITs have shifted their focus from acquisitions to joint ventures and third-party management platforms due to concerns of new supply and increasing development costs. This allows them to control a larger percentage of the market while not outright purchasing the properties.
- As REITs continue to expand their third-party management platforms, off-site management fees (historically 6% for REIT operators) appear to have lowered to 4% or 5% for some owners and/or markets due to the increased competition.

Development Trends

- Lease-up projections have softened. Economic absorption had typically been between 24 and 36 months, but recently expanded to 48 months for larger projects located in areas with new supply concerns. Facilities in lease up and entitled land are slow to sell due to the new supply uncertainties.
- A major topic of market industry participants continues to be new supply, which was expected to crest in 2018; however, it now appears it will peak in 2019. While there is not a single source of reliable development data, markets such as Dallas, Charlotte, Denver, and Austin are consistently discussed as being markets with a high amount of new supply in the pipeline. Markets such as Los Angeles, San Francisco, and New York are still viewed as favorable development markets due to the high barriers to entry and population density. However, because self storage remains a trade area specific business, it is difficult to quantify any large MSA as being over-supplied.
- Construction costs continue to increase, causing some development projects to be abandoned, particularly as supply-side issues are impacting market fundamentals.

Conclusion

The first half of 2019 has been a cautionary time for the self storage industry as most markets and trade areas have experienced new supply which has impacted rental rates and occupancy rates. These issues are widely viewed as being short term in nature. However, there is uncertainty if and when rental rates will return to previous levels. Demand is still strong for Class A and Class B properties, as current market participants are looking to add to their existing footprint, and new investors are looking to enter the space. New construction is now expected to peak in 2019, with a decline expected in 2020 due to supply issues and an increase in construction costs. We expect the market to remain cautious in 2019.

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About Cushman & Wakefield

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