

## Self-Storage Newsletter

Since the 1980's the self-storage industry has grown significantly to 50,859 facilities nationwide and 2.99 billion square foot of inventory. There are three distinct groups of owners: self-storage REITs, large operators of multiple facilities, and the smaller "mom-and-pop" owners. The market share of the top 10 operators has grown each of the last three years. However, these 10 operators account for only 16.66% of the facilities and 17.76% of the square footage, with "mom-and-pop" operators still owning a lion's share of the industry, allowing significant room for consolidation.

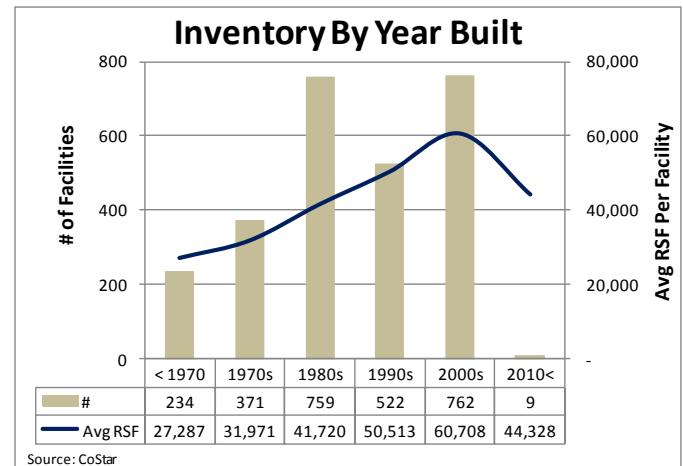
Industry consolidations are allowing larger players to take advantage of economies of scale, most evident with existing large self-storage operators (including the REITs and public companies). Smaller operators are also teaming up with large equity sources to expand their portfolios, and investors from other sectors are attracted to the solid self-storage returns over the last few years.

### Development Trend

With less than 15 percent of the self-storage square feet being built prior to 1980, most of the product is relatively new. However, rapid changes in the industry such as state-of-the-art technology, better security, climate control, wine cellars, recreational vehicle storage, multi-level buildings and the focus on more visible, retail-type locations has often left the older product at a marked disadvantage. The 1990s and 2000s saw nearly 60% of all existing inventory added. Facilities got larger, growing from an average of 41,720 square feet in the 1990s to 60,708 square feet in the 2000s.

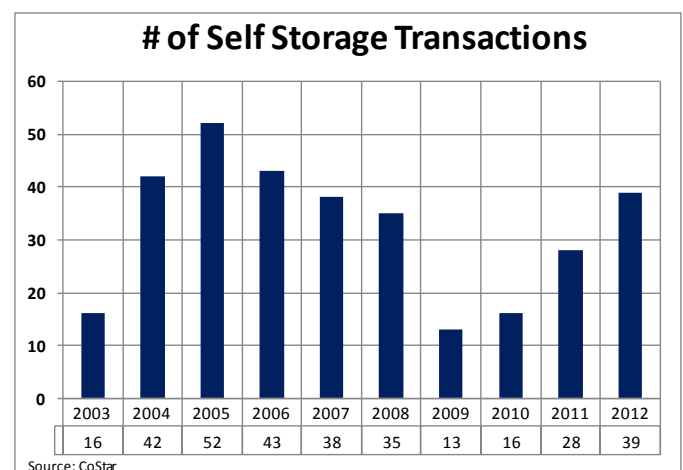
In Florida, development peaked in 2000 at 115 properties and 105 properties in 2001. Between 2002 and 2008, the number of new properties added ranged from 52 to 82 annually. As the real estate market and credit crisis worsened, new projects coming on line dropped to 24 in 2009. Only eight new projects have been developed over the past three years due primarily to the decline of the housing market, the main driver of self storage demand. Based on the research from the 2013 Self-storage Almanac, the national average is 7.55 rentable square feet per person. South Florida is the only Florida market that is under supplied, while Tampa, Jacksonville and Orlando are at or near equilibrium.

The stage is set for new development, particularly in Miami, Tampa, and Orlando. The bottoming out of the housing market and the rebounding population has spurred single and multifamily development.



MARKET EQUILIBRIUM BY CBSA (CORE BASED STATISTICAL AREA)			
CBSA	Number of Facilities	Area Square Footage	RSF per Person
Miami-Fort Lauderdale-Pompano Beach FL	717	33,340,500	5.95
Tampa-St Petersburg-Clearwater FL	450	20,925,000	7.44
Orlando-Kissimmee FL	367	17,065,500	7.72
Jacksonville FL	223	10,369,500	7.59
North Port-Bradenton-Sarasota FL	139	6,463,500	9.07
Cape Coral-Fort Myers FL	131	6,091,500	9.64
Palm Bay-Melbourne-Titusville FL	161	7,486,500	13.59

Source: Self Storage Almanac 2013



As market fundamentals continue to improve for self-storage with higher occupancy and rental levels, the self-storage market is primed for new product.

Bank financing, however, will be constrained due to concerns about new commercial real estate construction in general. The first projects will be REIT driven or will be additions to existing facilities.

In his fourth quarter Self Storage REIT Report (italicized), Mike Mele of Marcus and Millichap states, "the consensus is that the development pipeline won't affect operations until 2015, but at the same time, it is difficult to predict when the assets under construction will begin to affect pricing in primary markets."

### Transactions

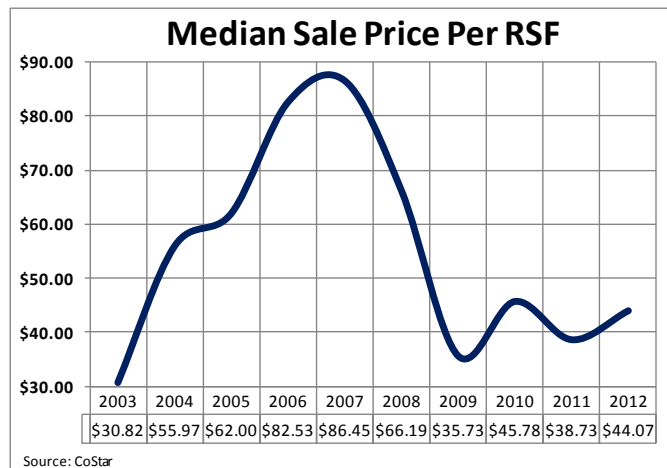
The number of sale transactions greatly increased in Florida during the real estate boom, with 35 to 52 annual transactions between 2004 and 2008. From 2009 to 2010, the pace of transactions dropped by two-thirds, registering 13 and 16 transactions respectively. The volume has increased with 2011 transactions doubling 2009 and 2010 levels at 28 transactions and 2012 has posted 39 transactions. For 2013 industry analysts have reported that several large portfolios may be hitting the market in the third quarter.

### Pricing

In Florida the median price per rentable square foot nearly tripled from \$30.82 in 2003 to a high of \$86.45 in 2007. By 2009, the median had dropped to \$35.73 per square foot due primarily to distressed sales. The rebounding market posted a median of \$44.07 per square foot in 2012.

Current listings reviewed by Beshears and Associates throughout the Southeast US show storage facilities with a physical occupancy of 60% or greater reporting an average list price of \$69.09 per square foot, and those with less than 60% physical occupancy with an average of \$38.42 per square foot. Over the last six months, pricing has seen a marked increase as well-located assets, especially those being pursued by a REIT or large operator, are trading at or near \$100 per square foot. As Mele points out again in his report, "Asset pricing is at record levels for high-quality assets, and it remains to be seen how much longer these prices can continue to increase. Either way, owners bringing assets to market in 2013 will see substantial interest."

Chris Harris of IStorage indicated that smaller operators are moving into secondary and tertiary markets and driving up pricing as they are applying pricing from primary markets.



With a marked distinction in capitalization rates and pricing in secondary and tertiary markets, this approach is putting additional pressure on buyers looking to take advantage of deals in these markets.

Based on interviews with Chip Headley of Flagship Development and industry specialist, Mike Mele of the Mele Storage Group at Marcus & Millichap, the consensus is that deals are hard to find as there are significantly more buyers than sellers.

Four to five years ago, pension funds did not consider self-storage worthy of being part of their real estate portfolio but it is now considered a desirable asset. Pension funds primarily concentrate on the preservation of capital and current income streams. Thus, these investors can be satisfied with lower returns than private equity groups who, in contrast, concentrate more on future growth in the value of the asset. Downward pressure on cap rates makes the higher returns more difficult to achieve.

### Capitalization Rates

As the market heated up, capitalization rates plunged from an average of 11.0% in 2004 to a low of 7.3% in 2007. Capitalization rates trended upward till 2010 peaking at 8.8%, before dropping 200 basis points to a current average of 6.8%. Deals in Florida have dropped from an average of 7.48% between Dec-2011 to Nov-2012 to 6.81% since Dec-2012.

Self-Storage capitalization rates have historically lagged the larger, more active apartment market capitalization rates by 150 to 250 basis points. So far in 2013 this spread has tightened, as buyers are becoming more aggressive in self-storage return requirements.

Most would agree that at some point interest rates will rise, pushing up capitalization rates. There are varying opinions on whether inflation will drive up rental rates enough, thus increasing NOI, to maintain the current values even at higher capitalization rates.

Mele elaborated on capitalization rates compression saying, in addition to the obvious cheap cost of money, the driver for cap rates is the competition for investment dollars. As long as self-storage can remain in demand, capitalization rates will remain low and further compression of rates is certainly possible, even if just 25 basis points.

### Rental Rates and Occupancy

Rental rates peaked in 2009 for nearly every category type. Rates began declining in 2010 and 2011 before rebounding in 2012. Overall rental rates are, on average, off 9.9% from their high point. However, rental rates are up 1.8% compounded annually since 2007.

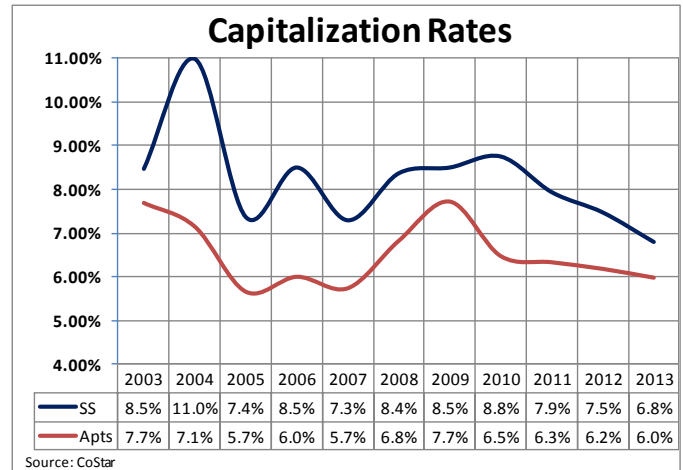
Occupancy rates, both physical and economic, have improved since their low point in 2010. Physical occupancy is up over 10% and economic occupancy nearly 15%.

As owners continue to search for ways to increase revenue, many have turned their attention to tenant insurance. In his 4Q Self Storage REIT report, Mike Mele reported "REITs continue to build revenue by pushing tenant insurance, which is being purchased by 90% or more of new renters. Across the board, tenant insurance is generally held on only 60% of units, so even without substantial physical occupancy gains, revenue and NOI growth can be achieved by replacing uninsured tenants with new tenants not only at higher rates, but also paying for insurance."

### Outlook

Brokers and market participants expect capitalization rates to remain at low levels or even possibly compress due to strong demand from investment dollars, increasing rental and occupancy rates and limited new construction. The number of transactions is being held back by the amount of inventory for sale, but as bank REO portfolios and distressed assets are winding down, the low hanging fruit has been largely purchased.

Overall, we expect this to be a good year for self-storage owners in Florida. Sellers must answer the question, "if I sell my storage facility and pay the taxes, where am I going to reinvest my money and get similar returns?" Some owners are electing to refinance at historically low rates, as the market is awash in capital from, Life Companies, CMBS and banks. For buyers, we expect a tough market, but the silver lining is if you are lucky enough to get a deal it will most likely still be below replacement costs and there are plenty of attractive financing options.



Southeast Occupancy Trends				
	2009	2010	2011	2012
Economic	73.60%	61.30%	71.20%	75.50%
Physical	77.10%	69.20%	76.80%	79.90%

Source: Self-Storage Almanac

Southeast Rental Rate Trends (Non-Climate)						
	2007	2008	2009	2010	2011	2012
5x5	\$ 35.52	\$ 40.76	\$ 46.19	\$ 43.56	\$ 42.19	\$ 42.76
5x10	\$ 51.25	\$ 55.04	\$ 60.96	\$ 54.69	\$ 52.36	\$ 52.83
10x10	\$ 75.80	\$ 84.18	\$ 85.62	\$ 80.42	\$ 79.59	\$ 81.90
10x15	\$ 98.97	\$ 107.95	\$ 115.72	\$ 108.50	\$ 107.99	\$ 107.84
10x20	\$ 117.10	\$ 133.86	\$ 132.57	\$ 132.00	\$ 122.90	\$ 123.94
10x25	\$ 137.47	\$ 154.08	\$ 182.39	\$ 160.25	\$ 161.38	\$ 158.11
10x30	\$ 169.88	\$ 173.30	\$ 195.25	\$ 181.36	\$ 181.89	\$ 185.34
20x20	\$ 200.96	\$ 202.95	\$ 243.78	\$ 215.24	\$ 246.33	\$ 216.71

Source: Self-Storage Almanac

### ABOUT OUR FIRM

Beshears and Associates is a commercial appraisal firm located in Tampa, Florida. In addition to covering apartments, office, industrial, land, and retail, we have specialty practices in gas stations, self-storage, hotels and bank branches. Our staff of 12 appraisers complete over 600 appraisals annually in Florida and Georgia.



If you have questions about the newsletter or our practice, please contact David Beshears, MAI at 813.204.2885 x204 or [dbeshears@beshears.net](mailto:dbeshears@beshears.net).



### SELF STORAGE VALUATION GROUP

You may also contact John Cordova, Director of the Self Storage Valuation Group, at 813.254.2885 x207 or [jcordova@beshears.net](mailto:jcordova@beshears.net).

Past newsletters can be found at [www.beshears.net](http://www.beshears.net)