

SELF STORAGE INDUSTRY OVERVIEW

The Market Overview forms a basis for assessing market area boundaries, supply and demand factors, and indications of the subject's position within the market. The following market analysis is based on the review of the 2010 Self-Storage Almanac and specifically the Southeast Region. The Self-Storage Almanac conducts an annual survey of self-storage facilities both regionally and statewide. In addition, we have included the Domestic Self Storage Market overview from the 2nd Quarter 2010 Korpacz Real Estate Investor Survey at the end of this overview.

Customer Base: Per the Self-Storage Almanac, self-storage facilities, although usually falling under industrial zoning regulations, are more like neighborhood shopping centers in that they must draw customers from within a relatively small radius to be competitive. The majority self storage customers seek facilities within a three to five mile radius of their main location. The density of development and the location of competitors in the submarket primarily influence the trade area ring.

Residential customer tenancy has increased from 73.8% in 2008 to 77.1% in 2009, while the commercial tenancy has decreased from 20.6% to 16.5% from 2008 to 2009. Prior to this year, residential tenancy had been shrinking and commercial tenancy had been growing. Given the current recession, this trend is surprising and it is possible that longer tenancies related to downsizing could be affecting customer base totals. The subject's submarket (Southeast) indicates the highest commercial customer base in the nation, at 18.8% and the second lowest residential customer base of 74.8%. This submarket indicated an average stay of approximately 14.4 months for residential tenants. Business customers are an attractive part of the base since the commercial patron typically rents for an average of 24.2 months in the Southeast.

Rental Rates: Rental rates are affected by a variety of factors, from the larger economic picture to occupancy rates, local market dynamics, competition, services offered, incentives, advertising, and the location and age of the facility. Per the Self-Storage Almanac, rental rates in the United States grew robustly in 2009 despite a national recession. Nationwide, rates were up in every size category. Rental rates in the subject region (Southeast) were the lowest of any region in every size category. The following table indicates the average rental rates for each respective size ranging from 5'x5' to 20'x20'. The table summarizes the rates over the period 2004 through 2009, as well as the percentage increase or decrease in the rate over the last year.

SOUTHEAST REGION RENTAL RATES							
Unit Size	2004	2005	2006	2007	2008	2009	% Change 08'-09'
5'x5'	\$31.40	\$30.76	\$38.24	\$35.52	\$40.76	\$40.65	-0.3%
5'x10'	\$43.09	\$44.09	\$52.98	\$51.25	\$55.04	\$57.30	4.1%
10'x10'	\$67.00	\$64.84	\$79.39	\$75.80	\$84.18	\$89.03	5.8%
10'x15'	\$85.39	\$86.74	\$103.92	\$98.97	\$107.95	\$120.90	12.0%
10'x20'	\$104.64	\$103.00	\$125.10	\$117.10	\$133.86	\$129.88	-3.0%
10'x25'	\$123.73	\$125.14	\$145.36	\$137.47	\$154.08	\$132.84	-13.8%
10'x30'	\$138.12	\$145.10	\$166.55	\$169.88	\$173.30	\$149.61	-13.7%
20'x20'	\$197.42	\$187.21	\$189.11	\$200.96	\$202.95	\$207.98	2.5%

Based on the above, rates within the subject's submarket have varied based on unit size. The largest increase occurred in the 10'x15' units (+12%) and the largest decrease occurred in the 10'x25' units (-13.8%).

Occupancy Rates: The self storage industry is known for its ability to withstand economic downturns. However the industry did show signs of the economy's effect in terms of occupancy declines, albeit moderate declines in most regions. With fewer people transitioning into new homes, and facing the increasing costs of necessities, self storage facilities have recently found it more difficult to attract and retain tenants. Nationally, the average occupancy for self storage facilities is 76.7%, down from 80.3% one year ago. In the subject's submarket (Southeast), the occupancy is the lowest of all the regions, at 73.7%.

It has also become more difficult for new facilities to stabilize, or reach the 85% physical occupancy mark. Approximately 32% of new facilities are taking more than 24 months to reach this point. Only 6% of facilities took less than 6 months to reach stabilization and only 14% took 6 months to one year. We were unable to trend this data as the Almanac changed the threshold of stabilized occupancy from 70% to 85% this year.

Conclusion: The self storage industry has historically been less vulnerable to economic downturns. However, the recent data indicated the national occupancy has decreased over the last couple of years. The average occupancy of the subject's region (Southeast) was the lowest in the nation. Nationwide rental rates have reportedly increased over the last year. However, the subject's submarket (Southeast) indicated several unit size categories with decreasing rates. This submarket also indicated the lowest rental rate in every size category of all the regions. Overall, the self storage industry appears to be in much better shape than most other sectors of real estate, and we would expect this segment of the market to improve as the economy recovers over the next few years.

Domestic Self-Storage Market

A RETURN TO 7.25% OVERALL CAP RATES?

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EQUITY CAPITAL IS RETURNING TO THE SELF-STORAGE ASSET CLASS CAUSING AN INCREASE IN SALES VOLUME OF SINGLE ASSETS, A RETURN TO PORTFOLIO SALES, AND BEST OF ALL, A DECREASE IN OVERALL CAPITALIZATION RATES. In fact, the rate of downward movement in overall cap rates (OARs) suggests a return to 7.25% OARs within two years – if market conditions continue to improve and interest rates remain steady. Clearly, investors have an improving outlook for the domestic self-storage industry.

Current players in this sector include nationwide companies like Strategic Storage Trust, W.P. Carey, and various REITs, as well as smaller regional companies, such as Equity Based Services. In fact, most of the four self-storage REITs are in acquisition mode. Public Storage, for example, recently closed on a \$189.0-million portfolio acquisition of 30 self-storage facilities (28 in California and two in Chicago). Another self-storage portfolio of 54 properties is currently

on the market with six buyers vying to close the deal.

Specific acquisition and return requirements for select major players in this sector are summarized below.

◆ Strategic Storage Trust (SST), a nonpublicly traded REIT started five years ago, has raised over \$200.0 million and has a portfolio growing at a pace of one self-storage facility per week with interest in properties nationwide. SST prefers self-storage properties near stabilization, but will consider some upside in rents and absorption. However, it tends to only focus on potential deals involving properties that are at least 60.0% occupied and have a history of positive absorption.

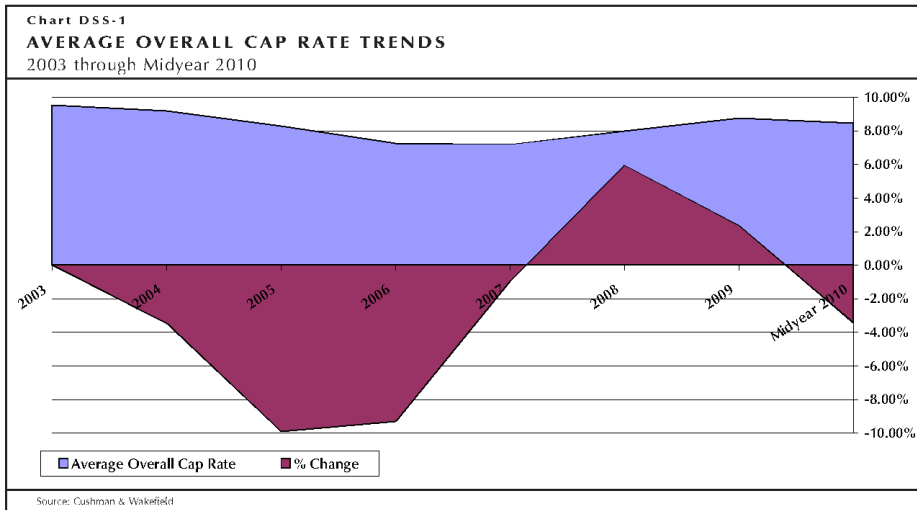
In 2009, a 9.0% overall cap rate on trailing 12 months of income was SST's target. Now, its target OAR has declined 50 to 100 basis points based on a careful analysis of the local trade area of an asset. Strategic Storage Trust is currently the most active buyer of self-storage property in the country.

◆ W.P. Carey & Co. (WPC) was founded in New York in 1973 as an investment management company. Current assets exceed \$10.0 billion and the company is publicly traded on the New York Stock Exchange. In 2004, a partnership among WPC affiliates completed a \$312.0-million acquisition of 78 U-Haul self-storage and truck rental facilities located in 24 states. Since December 2006, WPC has acquired 13 self-storage properties for approximately \$60.0 million.

Table DSS-1 DOMESTIC SELF-STORAGE MARKET First Half 2010			
	FIRST HALF 2010	SECOND HALF 2009	FIRST HALF 2009
DISCOUNT RATE (IRR)^a			
Range	10.00% – 13.00%	10.00% – 13.00%	10.00% – 12.00%
Average	11.50%	11.50%	11.25%
Change (Basis Points)		0	+25
OVERALL CAP RATE (OAR)^a			
Range	7.00% – 10.00%	7.00% – 10.00%	7.00% – 10.00%
Average	8.45%	8.75%	8.55%
Change (Basis Points)		-30	-10
RESIDUAL CAP RATE			
Range	8.00% – 10.50%	8.00% – 10.50%	8.00% – 10.50%
Average	8.75%	9.00%	8.75%
Change (Basis Points)		-25	0
MARKET RENT CHANGE RATE^b			
Range	1.00% – 5.00%	1.00% – 5.00%	1.00% – 5.00%
Average	3.50%	3.00%	2.00%
Change (Basis Points)		+50	+150
EXPENSE CHANGE RATE^b			
Range	2.00% – 5.00%	2.00% – 5.00%	2.00% – 5.00%
Average	3.00%	3.00%	3.00%
Change (Basis Points)		0	0
AVERAGE MARKETING TIME^c			
Range	3.00 – 12.00	3.00 – 12.00	3.00 – 12.00
Average	8.00	11.00	9.50
Change (%)		-27.27	-15.79

a. Rate on unf leveraged, all-cash transactions b. Initial rate of change c. In months

Source: Cushman & Wakefield



More recently, WPC has formed a joint venture with Harbert Management Corporation and contributed \$50.0 million to buy additional self-storage assets. The venture is pursuing self-storage opportunities in all 50 states and will consider properties in need of absorption. The target overall cap rate is mid-8.0% on a stabilized basis, but only after analysis of the competition in the local trade area.

◆ Equity Based Services (EBS) is raising private equity funds with a plan to create a nonpublicly traded self-storage REIT called Universal Self Storage Acquisitions. EBS seeks properties in the southwest region of the United States. While it focuses on Class-A locations, it will consider Class-B product with expectations of an 8.0% to 8.5% overall cap rate.

EBS also considers sub-8.0% OARs if there is upside or value-add potential (at least 75.0% occupancy) through management or limited capital expenditures. EBS has \$50.0 million in an equity fund and hopes to acquire \$120.0

to \$140.0 million in self-storage assets over the next year.

OVERALL CAP RATE TRENDS

Overall cap rate trends for the U.S. self-storage industry are shown in Chart DSS-1. It is interesting to see that the rate of compression occurring now in this sector is similar to the slope of the rate of increase experienced during the bull market. If analyzed as a regression line, the trend suggests that overall cap rates for the self-storage industry will near 7.25% within two years.

While most investors appear confident that interest rates will remain stable through 2010, many believe that interest rates will eventually rise to combat concerns of inflation over the long run. However, equity dividend requirements may decline. Thus, the impact to long-term overall cap rates is uncertain. For now, the trend for the self-storage industry is declining overall cap rates with some investors expecting OARs to be “8.0% or lower by the end of this year.”

CONCLUSION

The high number of investors and private equity pursuing self-storage assets has put downward pressure on overall cap rates. Although most investors still prefer to acquire stable self-storage assets, a growing number of buyers are once again interested in self-storage properties with absorption needs and more aggressive pricing requirements. The growing desire to target such assets suggests that investors remain confident in this sector's long-term performance and its ability to reach targeted returns. ◆

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