MARKET WATCH:
NEW YORK CITY

Self-Storage In The Big Apple

By Marc J. Nakleh, MAI

New York City is commonly known as "The City That Never Sleeps." It seems you can get anything you want, at any time, and in abundance. Bagel stores, pizzerias, taxis and hot dog carts are everywhere and demand for them is constant. True to this tradition, investors' demand for quality self-storage operations within the five boroughs of New York City is formidable. While local residents may think that there are plenty of self-storage facilities available, according to the 2010 Self-Storage Almanac, the New York-Northern New Jersey-Long Island CBSA, has a significantly lower amount of rentable square feet of self-storage space per person than New York State and the entire United States.

New York City Economy

New York City consists of five counties at the mouth of the Hudson River in the southeast area of New York State. The borough of Manhattan, also referred to as New York County, forms the political, financial and cultural core of the city. It is the economic growth engine of the Greater New York Region. The city's other boroughs are Brooklyn, Queens, Staten Island and the Bronx, otherwise known as Kings, Queens, Richmond and Bronx counties, respectively. The massive regional transit system in the area connects New York City to Upper New York State, New Jersey, Long Island and Connecticut. New York City has a population of 8.5 million people and the greater New York-Northern New Jersey-Long Island CBSA contains approximately 19 million people.

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New York City is a global economic center, with major emphasis on finance, insurance, real estate, media and the arts. The city is home to 42 of Fortune 500 companies, including JPMorgan Chase, Citigroup and Goldman Sachs. In addition to these businesses, New York City depends heavily on tourism.

While New York City weathered the recession better than the country as a whole, it did lose approximately

COMING NEXT MONTH:
Georgia

Big Apple Market Conditions (SF/Person)

Market	Existing Supply	Forecast Demand	Variance	Condition
New York	3.2	7.31	4.11	Under-Supplied*
New York-Northern New Jersey-Long Island, NY-NJ-PA	2.25	2.45	0.20	Under-Supplied

Source: Cushman & Wakefield's Self Storage Industry Group and *2010 Self-Storage Almanac*

*Compared to National Average

185,000 or 4.8 percent of its jobs. These jobs were in all sectors and cut across the social spectrum. The trend of economic recovery begun last year, recouping about 60,000 jobs, is expected to continue in 2011. However, wages are not expected to rise significantly and some cause for concern persists. Namely, the cost of living in New York City is high, about 27 percent higher than the national average, and has outpaced median household income growth. As a result, many middle class families have been forced to leave the city for more affordable areas. Property tax increases have also contributed to the flight.

One outcome of increasing costs is many residents are continuing to rent in lieu of buying homes or condominium/cooperative apartments. Moreover, tenants are adding roommates with whom to share expenses. According to Claritas, Inc., 66.4 percent of the housing stock in New York City was renter occupied in 2010. This statistic is a key metric to self-storage operators, as many buildings in the city do not have sufficient storage space for their tenants.

Self Storage Market Trends

As mentioned earlier, the New York-Northern New Jersey-Long Island CBSA contains a much lower per capita amount of rentable square feet of self-storage space than the country does as a whole. As can be seen on the table below, the CBSA contains 2.25 square feet of self-storage space compared to the New York State and national equivalents of 3.20 and 7.31 square feet per person, respectively.

Limited numbers of development sites, high construction costs and lack of local knowledge are the major barriers to entry in the New York City self-storage market. Many of the buildings that house existing facilities once were used for warehousing and manufacturing. Many of these industrial businesses have left New York City for areas with a newer industrial building stock, better access to local and regional highways, more loading docks, and higher ceiling heights. As these businesses vacated, self-storage operators seized the opportunity to acquire buildings that have loading areas, large floor plates and are typically overbuilt based on the current zoning code. Another barrier to entry is the specialized knowledge of converting older industrial buildings to modern self-storage facilities.

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A typical self-storage facility in New York City is a multi-story, climate-controlled building with approximately 70,000 square feet of net rentable area and 1,200 units, which indicates an average unit size of 58 square feet. Typical unit-mixes are highly skewed toward smaller unit sizes, with the 5-by-5 and 5-by-10 units highest in demand. Most of the units are interior, and a very small proportion of the units are drive-up. Facilities typically do not have on-site manager apartments; however, security is an important issue to customers. Most facilities are well lit and have security access codes preventing customers from accessing other floors in the building. Newer facilities have individual alarms on each unit, alerting the front desk when a unit is open. Given the lack of vacant land, few facilities offer parking for boats, recreational vehicles or other motorized vehicles.

Annual rental rates range from $30 to $70 per square foot, with the higher amount for smaller units. Occupancy levels at most established facilities are in the 80 to 90 percent range. Many operators now utilize a revenue management system, allowing them to increase or decrease rates for certain unit types when occupancy hits a certain level. A typical concession is one month free rent; however, this can vary based on the occupancy levels of the specific unit type.

Many market participants were interested in determining how the self-storage industry would fare during the recession. With the worst of the recession receding behind us, most owner/operators agree that the industry survived the recession fairly well. One set of customers looking to cut monthly expenses, decided to forgo their self-storage unit. Another set of customers traded down to smaller living quarters, or moved back home with their families— this move helped reduce monthly expenses significantly. As new living situations resulted in less storage space, their savings permitted rental of storage units. The departure of one set of customers was offset by the arrival of another set. Overall, most operators indicated they lowered asking rents slightly and increased use of concessions during the recession. Last year, that trend seems to have been reversed.

Investment Outlook

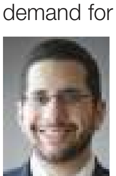
The self-storage sales market in 2009 was virtually non-existent, with just one sale occurring during the year. However, in 2010 the market picked up with five transactions taking place. All of these sales were fully operational facilities that were at or close to stabilized occupancy. One reason for the limited amount of transactions was the lack of facilities available for sale. During the recession, there was a major disconnect between buyers and sellers as to the valuation of the facilities. This disconnect eased during 2010, helping to facilitate the transactions.

The buyers in these 2010 transactions were national storage operators looking to gain an increased presence in the New York City market. The 2010 transactions indicated sales prices between $200 to $250 per square foot of net rentable area, averaging $220 per square foot of net rentable area. The indicated capitalization rates for these transactions ranged from 5.21 percent to 7.20 percent, averaging 6.05 percent. Comparatively, transactions between 2004 and 2008 (prior to the collapse of Lehman Brothers) indicated prices of $119 to $369 per square foot of net rentable area, averaging $243 per square foot of net rentable area. The capitalization rates for these transactions ranged from 5.24 percent to 7.90 percent, averaging 6.61 percent. While the average sales price per square foot is lower than the average of the transactions between 2004 and 2008, the average capitalization rate indicated for these transactions is lower than the average of the 2004 to 2008 period. Additionally, the capitalization rates reported for the 2010 transactions are lower than the 7.75 percent average capitalization rate percent reported in the fourth quarter 2010 PwC Real Estate Investor Survey for the Domestic Self Storage Market. These capitalization rates highlight the strength of the local market, and investors' belief that it will continue to remain strong. Financing and refinancing were available for established owners/operators at an average loan-to-value ratio of 65 percent.

Discussions with local market participants indicate that the trend of lower capitalization rates for quality facilities is expected to continue into 2011. As the New York City economy continues to recover, storage operators believe occupancies and rental rates will continue to rise. Investment sales brokers indicate strong demand exists for established facilities in areas with high population densities.

The Overall View

Throughout its history, New York City has been a leader in finance, fashion and other trends. The self-storage investment industry stands to gain from the city's rebound. Sophisticated investors in self-storage are looking to acquire properties in areas of high population and a strong economy—New York fits the bill. While New York City may never have as many storage facilities as pizzerias, the current deficit of facilities and development sites ensures strong demand for quality facilities.



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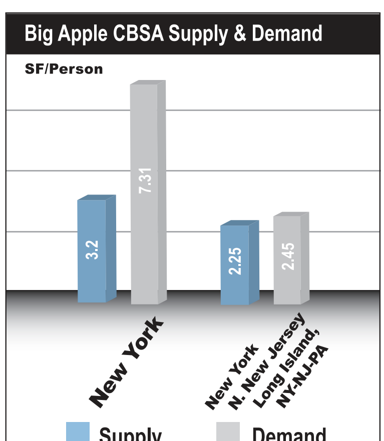
BIG DEMAND IN THE BIG APPLE

There is big demand for self-storage facilities in the Big Apple. The supply is so low in relation to the demographics, that the demand analysis is skewed to the low end. Consequently, an outlook of robust growth in collections is forecast as the regional economy improves.

The demand forecast by the Self Storage Industry Group of Cushman & Wakefield is based on a proprietary, econometric model that uses a mathematical regression of demand variables to existing supply in order to forecast stabilized demand in a CBSA (core based statistical area) or trade area. The model compares all top 100 CBSAs based on four key demographic criteria: total population, percentage of renters, average household size and average household income. New York has so much population in relation to the rentable area of self-storage property that stabilized demand is skewed to the low end.

The Big Apple or New York City CBSA has the right demographics for self-storage: high population in a dense living area (lots of apartments). The city has limited land available for development and new construction is costly and time consuming in urban areas. As a result, the market is largely supply constrained. Most "new" self-storage is a function of adaptive re-use of existing buildings (new highest and best use of the property).

Self-storage performance in the Big Apple is forecast for robust improvement as the regional economy improves. The market fundamentals of supply and demand indicate a market that is clearly under-served. Over the long run, rents and occupancy are likely to increase, particularly in urban, in-fill trade areas. Due to supply constraints to new development, big demand is forecast for the Big Apple.



Source: Cushman & Wakefield's Self Storage Industry Group and 18th Annual Self-Storage Almanac 2010

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