

## Hawaii

### Self-Storage In The Land Of The Aloha Spirit

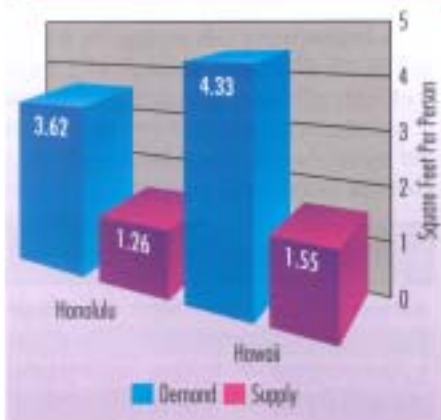
BY R. CHRISTIAN SONNE

“The best part of developing real estate in Hawaii is the Aloha spirit of the people”, says Greg Kreizenbeck of HUCO Pacific Development Company, Inc. The aloha spirit, a well-known reference to the attitude of friendly acceptance, is also indicated in the self-storage market conditions in the State of Hawaii.

#### The Wave of Supply And Demand

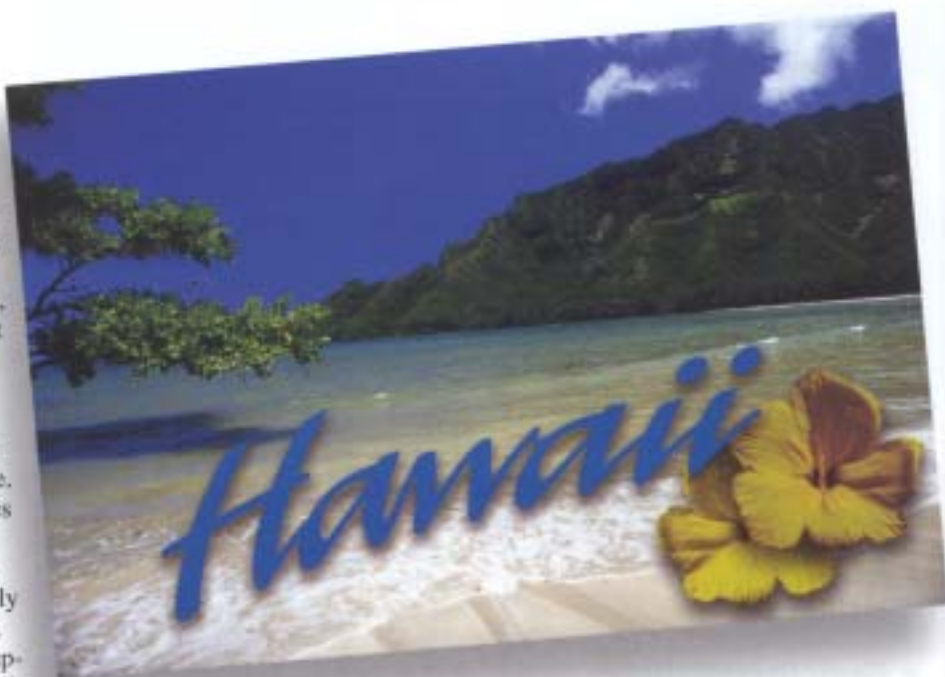
Hawaii is among the most under-supplied states in the nation in terms of self-storage. In peer group analyses of the United States by state, the *2003 Self-Storage Almanac* reports that existing supply is 1.55 square feet per person compared to existing supply nationwide of 4.33 square feet per person. Moreover, Honolulu indicates an under supply of over two square feet per capita. While these factors may seem like self-storage development paradise, local market analyses by trade area are always best. In downtown Honolulu, for example, some neighborhoods are oversupplied with self-storage product.

#### CHART Supply & Demand



Kreizenbeck, who has been successfully developing in Hawaii since 1985, says that

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local market knowledge is critical to a successful project. “The community is environmentally conscious, so there are strict development criteria and a deliberate approval process,” he notes, explaining that characteristics unique to understanding the Hawaii market are high land costs, the wide use of land leases, and unique market trends.

#### Island Land Costs And Leaseholds

Land costs range from \$35.00 to \$50.00 per square foot or 10 times as much as most markets in the United States. According to Guy V. Kidder, a Honolulu broker with Colliers Monroe Friedlander, one recent self-storage development project purchased land at costs reportedly near \$90.00 per square foot. Despite the higher than usual land costs, Kidder notes that “there is a lot of opportunity for self-storage development in Hawaii.”

Myron Liao, a self-storage analyst based in Hilo on the big Island of Hawaii, says that market conditions are good for self-storage in the islands, but like the mainland, self-storage market conditions vary by neighborhood. He says that costs are much higher on the islands, but so are rents. Liao estimates rental rates in Hawaii are “at least double compared to similar units located in California.”

High land costs are a function of being an island state with a limited supply of real estate. Consequently, land leases are common and “leasehold interests” are much more common in Hawaii. A builder may lease a parcel of land for a long term of 30 years or more, then build the self-storage project creating a leasehold interest. The advantage, according to developers, is to spread the land

*Are there self-storage opportunities in this island paradise? You may be surprised by the answer.*  
Photos courtesy of Hawaii Visitors and Convention Bureau

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costs out over the economic life of the buildings. Local experts point out that this may limit financing to local institutions that are familiar with the lending criteria on leasehold estates. According to local analyst Liao, an annual land lease is typically calculated as a ratio of the market value of the land. For a parcel of land with a cost of \$50.00 per square foot and an 8 percent return to the land, the annual lease rate on a net basis would be \$4.00 per square foot ( $\$50.00 \times .08 = \$4.00$ ).

Unique market trends in Hawaii relate to the unusual types of product. For example, one self-storage facility is located in a parking garage under a condominium tower. Another project is located on the fourth level of a parking structure. Much of the product is comprised of older, metal industrial buildings converted to self-storage use. Additionally, container storage is common. All projects have interior units with many two and three level facilities. Some projects include units in a stacked configuration with access only by ladder. An average project in the State of Hawaii has over 650 units and encompasses about 35,000 square feet. The average unit size in Hawaii is 52 square feet, approximately half the size of most units located on the mainland. Because of their small size, storage units are often called lockers.

#### CHART 2 Hawaii Ownership



**Ownership And Operations Aloha Style**  
Ownership of Hawaiian self-storage is also unique. For example, according to the 2003 *Self-Storage Almanac*, there are some 54 facilities in Hawaii. These are distributed over the four islands of Oahu, Hawaii, Maui and Kauai. As seen in the chart above, the distribution of ownership suggests a highly fragmented industry with significant growth opportunities. For example, there are over 30 different owners of self-storage property in

Hawaii. The largest owners of property include Public Storage, the Glendale, Calif.-based REIT, and Los Angeles, Calif.-based A-American Self Storage, a company that has been listed among the top 10 on the *Mini-Storage Messenger* Top Operators list for the past two years. Both Public Storage and A-American operate four facilities in Hawaii.

**An average unit of 50 square feet in Hawaii currently leases for anywhere between \$65 to \$164 per month with an average rental rate of \$118 (\$2.36 per square foot per month) on a full-service basis.**

Yet, despite the unique characteristics of self-storage supply in Hawaii, market conditions are described as very strong. Vacancy is less than 10 percent in the market and most trade areas are described as under-supplied. An average unit of 50 square feet in Hawaii currently leases for anywhere between \$65 to \$164 per month with an average rental rate of \$118 (\$2.36 per square foot per month) on a full-service basis. Rental rates on select units are delineated in the table below. Most self-storage facilities in Hawaii offer units as small as 2-by-2 feet with a four-foot or eight-foot height, at average rates near \$25 per square foot per month or more than \$6 per square foot per month!

TABLE 1 Monthly Rental Rates in Hawaii

Unit Type	Low	High	Average
5 x 5	\$25.00	\$125.00	\$75.00
5 x 10	\$65.00	\$164.00	\$118.00
10 x 10	\$111.00	\$300.00	\$232.00

Kidder, the local broker, reports that Public Storage has built two large facilities approaching 100,000 square feet within the last five years. However, two facilities in Honolulu have also been closed as a self-storage facility for single tenant, industrial uses. These facilities are older, in poor condition and located in emerging markets. Consequently, a higher and better land use is possible for

self-storage in Hawaii, but this largely depends upon zoning and entitlements of the underlying land. While land costs may scare away developers, Kidder says "there is a lot of opportunity for self-storage development in Hawaii."

Self-storage facilities rarely change ownership in Hawaii. Transaction trends indicate one purchase for alternate use (owner user conversion from self-storage) and purchase of leasehold interests (land lease and building improvements) in wide price ranges.

Recently, a warehouse was reportedly purchased in Hilo on the Big Island for self-storage conversion. However, just like the land, pricing measured per square foot is among the highest in the country.

Due to high land costs, overall capitalization rates can be 100 basis points or more lower than transaction data on the mainland. Expenses are also higher in Paradise—as much as 50 percent of effective gross income (after vacancy) and has high as \$15 per square foot (on average). Comparable expense data in Hawaii demonstrates that with higher land values and higher costs come higher rents and higher expenses. Unique to the Islands is an excise tax of 4.167 percent on all goods and services.

#### Riding The Wave

At first glance, the expense data can seem like getting hit by a 10-foot wave at the Bonzai Pipeline! However, one project in Honolulu analyzed by Self Storage Economics demonstrates a net operating income per square foot annually of nearly \$15! Such high returns are rarely matched in the self-storage asset class.

In summary, market statistics compiled by Self Storage Economics indicate that the self-storage market conditions in Hawaii are strong, characterized by high rental rates at vacancy rates of less than 10 percent statewide. Like all self-storage, however, the market must be analyzed carefully within each local trade area.

The Hawaii market is more complex than most mainland markets with a diverse supply of product, high land costs and strict development criteria. Nevertheless, local analysts are unanimous in expressing optimism for self-storage opportunities in Hawaii. Surf's up in Paradise!