

# Arizona Update

## Seasons Change In The Desert

By R. Christian Sonne, MAI

**E**ven in the desert state, seasons change. Market conditions in Arizona are described as over-supplied, but with positive emerging market trends. Specifically, statewide occupancy is currently stable at 80.26 percent but the average rent on a 10-by-10 unit has increased 5.39 percent over 2003 to \$77.53. Although occupancy is less than ideal, rising rents suggest improving market conditions.

Self Storage Economics compiled survey research and presented the results in connection with the Arizona Mini Storage Association (AMSA) Conference and Trade Show May 6-7, 2004 in Phoenix, Ariz. A survey of over 700 self-storage owners throughout Arizona was sent earlier this year, with nearly 250 responses (over twice as many as 2003). The survey included 37 detailed questions regarding occupancy, rental rates, security, and market trends. Market conditions in Arizona are summarized in the table below.

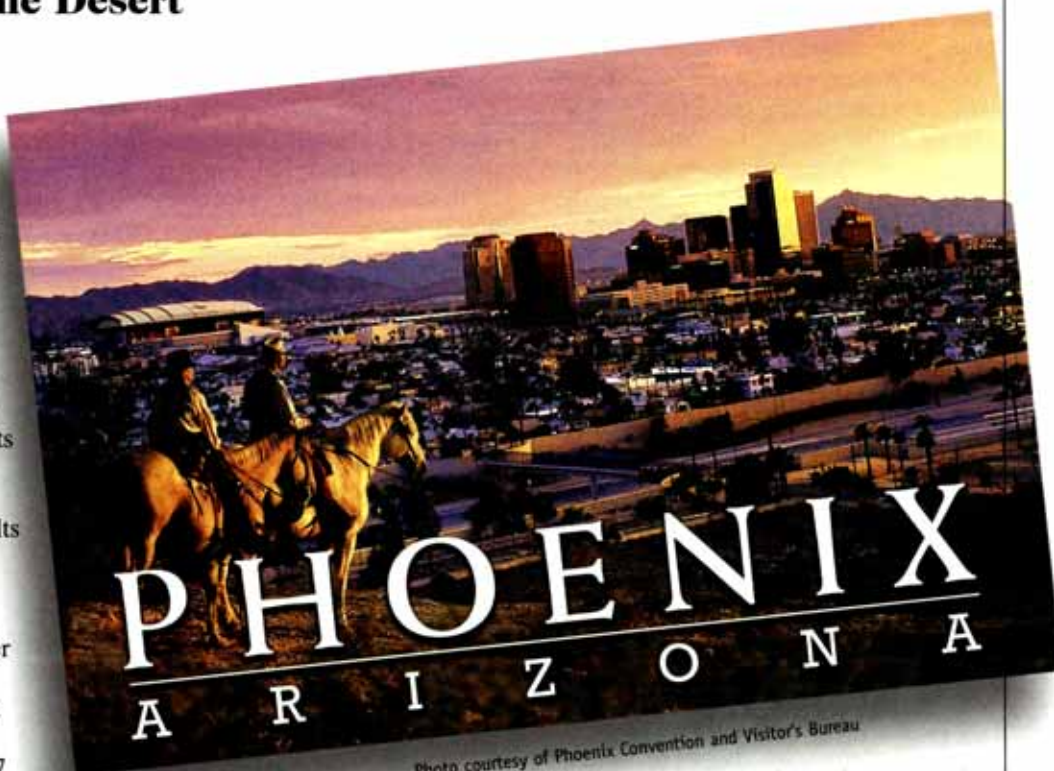


Photo courtesy of Phoenix Convention and Visitor's Bureau

Storage Economics for the 2004 Self Storage Almanac published by MiniCo Inc. Due to strong economic conditions such as population growth, the over-supply is

forecast for 2.43 years in the Phoenix MSA. This suggests rising occupancy and income over the next three years. However, this forecast assumes building is moderate and below the pace of the past few years. Given the abundance of capital available at historically low interest rates and proclivity to build to maxi-

mize profits in the asset class, it is difficult to forecast the pace of new construction.

However, like the rising tide of the ocean, interest rates will rise over the next 18 months. This results in either a rise in the trend of cap rates, or a decline in the return to the equity component. The forecasted potential is for at least a 200-basis-point rise in interest rates by the end of 2005, primarily due to inflationary pressures. As noted in *The Economist* (June 19, page 19), inflationary pressures in the United States include a GDP (gross domestic product) of seven percent over the past year with a current inflation rate of approximately three percent, suggesting short-term interest rates near four percent. In reality, as anyone with any kind of a savings account knows, the

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### ARIZONA MARKET CHARACTERISTICS

Area	State	Phoenix
Average Occupancy - Units	80.72%	78.64%
Average Occupancy - Square Feet	82.92%	81.14%
Average Occupancy - Economic	80.26%	77.28%
Average 5x5	\$30.69	\$30.74
Average 5x10	\$45.53	\$47.11
Average 10x10	\$72.74	\$77.53
Average 10x15	\$96.27	\$102.51
Average 10x20	\$113.41	\$120.76
Average 10x30	\$160.54	\$169.72

Source: Self Storage Economics

The statewide survey responses represented 241 facilities or nearly 12 million square feet of self-storage property representing 111,647 units. Based on the survey, an average facility in Arizona contained 461 units with 49,337 square feet or an average unit size of 107 square feet.

As indicated by the occupancy level (economic) of 77.28 percent, the Arizona market is clearly over-supplied. This is consistent with the econometric demand model and forecast prepared by Self



#### Market Profile:

##### Arizona State

Total Population: 5,580,811  
 Median Household Income: \$40,558  
 Homeownership Rate: 68.0%  
 Owner Occupied Homes: 1,293,556  
 Renter Occupied Homes: 607,771

##### Phoenix

Total Population: 1,321,045  
 Median Household Income: \$40,919  
 Homeownership Rate: 69.4%  
 Owner Occupied Homes: 282,670  
 Renter Occupied Homes: 183,164

#### Coming Next Month:

Market Watch  
 Oregon

short-term interest rates are around 1.0 percent. This gap suggests the supply of money available is too high (or monetary policy supports an inducement to borrowing and spending). Moreover, with a record setting budget deficit near half a trillion dollars, the fiscal policy means the government is competing with the private sector for the money supply. The result of all this economic stuff? The tide is rising and interest rates will shortly follow. For the Phoenix MSA, this should slow down the pace of new construction and assist the market to return to equilibrium.

**The tide is rising and interest rates will shortly follow. For the Phoenix MSA, this should slow down the pace of new construction and assist the market to return to equilibrium.**

The survey included other data queries regarding expenses, facility age, security and miscellaneous fees. Operating expenses, analyzed without real estate taxes, indicate a range in Arizona from \$0.40 to \$8.54 per square foot with an average of \$3.09 per square foot. In Phoenix, operating expenses (without real estate taxes) mirror the state with an average of \$3.11 per square foot. Comparatively, the 2004 *Self-Storage Expense Guidebook* indicates average expenses of \$3.57 per square foot (including taxes) in the Western Region and \$3.23 per square foot nationwide.

Self-storage real estate taxes in Arizona and Phoenix are significantly higher than regional and national data. For example, according to the survey, the Arizona average expense in real estate taxes is \$0.93 per square foot per year. In comparison, the nationwide data indicates an average of \$0.44 per square foot. The data is represented graphically in the chart to the right, which demonstrates that average real estate taxes in Arizona and Phoenix are higher than comparable data in the Western Region and nationwide.

As to refundable deposits, the survey indicates a range from \$5 to \$50 with an average of \$16.88. Similarly, administration fees indicate a fairly tight range from \$1 to \$35, but respondents in the state indicate an average administration fee of \$10.92. As to concessions, approximately half the respondents

indicate they are used (such as discounted or free rent).

The question regarding security asked respondents which methods are utilized among 11 categories from computerized gate access to guard dogs. The results, along with other data, is summarized in the tables to the right.

In summary, the survey research indicates occupancy lower than ideal suggesting a market described as over-supplied. Fortunately, Arizona enjoys continued, robust population growth. With average rents increasing over last year above the inflation rate,

market conditions are forecast for recovery over the long run.

In the meantime, it is important to remember that these snapshots provide interesting and important data on a macro basis. However, the self-storage asset class is a microeconomic business and market conditions in a local neighborhood or trade are much more important than city, state, or regional data. Even in the local neighborhood, the market will distinguish winners and losers among the competitive supply. MSA data can be utilized as an important first step or view into general market conditions of a major city or metropolitan area. 🏠

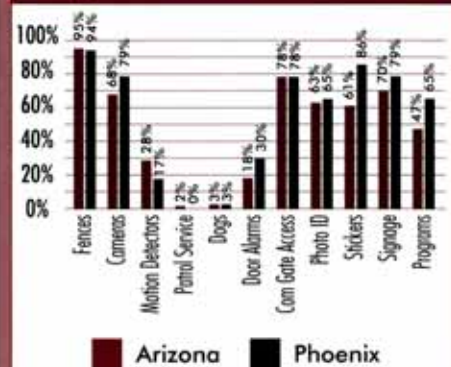
R. Christian Sonne, MAI is principal of Self Storage Economics, a full service real estate consulting company specializing in appraisal and market study of the self storage asset class.

**SUPPLY & DEMAND**



Source: Self Storage Economics

**SECURITY**



Source: Self Storage Economics

**OCCUPANCY REPORT**

Average Occupancy-Units (%)	78.64%
Average Occupancy-Square Feet (%)	81.14%
Average Occupancy-Economic (%)	77.28%

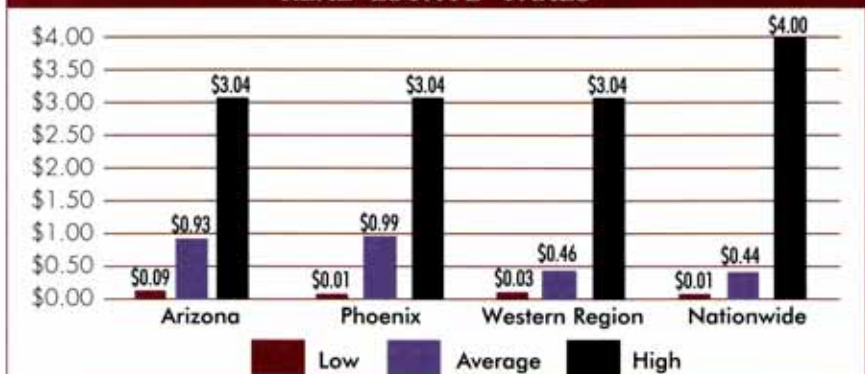
Source: Self Storage Economics

**UNIT RENTAL RATES (Per Month)**

	Lowest \$/Mo	Highest \$/Mo	Average \$/Mo
5 x 5	15	47	31
5 x 10	30	77	47
10 x 10	50	130	78
10 x 15	70	185	103
10 x 20	82	236	121
10 x 30	49	457	170

Source: Self Storage Economics

**REAL ESTATE TAXES**



Source: Self Storage Economics