

BUSINESS BRIEFING

2010 SELF-STORAGE INVESTOR SURVEY

RESILIENT ASSET CLASS GAINS TRACTION

THE OUTLOOK IS FOR CONTINUED IMPROVEMENT IN SELF-STORAGE MARKET CONDITIONS

SEPTEMBER 2010 | A VALUATION & ADVISORY PUBLICATION

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EXECUTIVE SUMMARY

Investors are returning to the self-storage asset class and demanding more data and research analytics to support their decision processes. Cushman & Wakefield's *2010 Self-Storage Survey* expands on results found in reports such as the *Korpacz Investor Survey*, published by PricewaterhouseCoopers LLP (2Q 2010), to include market optimism, marketing time, absorption time and other elements that characterize the current market conditions for the asset class.

BACK IN THE GAME

The market through mid-year improved significantly in 2010, with over \$1 billion in equity money chasing yield in self storage. Public and private REITs, as well as large national and regional self-storage companies, are back in the game. As an example, Public Storage completed the first significant portfolio transaction in two years in March by purchasing 30 assets from A-American Self Storage. The portfolio is comprised primarily of Class B properties and was reportedly purchased at just under an 8% cap rate. The properties were operating on a stabilized basis and located mostly in Southern California with two assets in Chicago. Nationwide, single asset transactions are up 20% or more over last year. Furthermore, low-leveraged financing is available from banks and life companies for properties with strong balance sheets.

The results of Cushman & Wakefield's survey, completed in Summer 2010 by over 50 respondents in investment, brokerage and other related industries, corroborate with other findings that show increased optimism for the asset class and slightly lower cap and yield rates. Marketing times are declining and absorption times improving, as new construction is at a 10-year low. The survey results are detailed in the following table.

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CHART 1: SUMMER 2010 SELF-STORAGE KEY INDICATORS

Time	2010	2009	2008	2007	2006	2005	2004	2003
Trade Area (radius)								
Range	1 - 5	2 - 5	2 - 5	2 - 5	1 - 5	1 - 5	1 - 5	1.5 - 5
Mode	3	3	3	3	3	3	1.5	1.5
Average	3.15	3.21	3.25	3.33	3.14	3.3	2.8	2.82
Change	-1.87%	-1.2%	-2.4%	6.05%	-4.85%	17.86%	-0.71%	-
Demand (sq. ft. per person)								
Range	1 - 8	1 - 8	1 - 10	3 - 10	2 - 10	3 - 12	2 - 12	2 - 8
Mode	7	6.5	6	6	5	5	4	4
Average	6.98	6.73	6.52	6.12	5.7	5.36	5.27	4.87
Change	3.71%	3.22%	6.54%	7.37%	6.34%	1.71%	8.21%	-
Capitalization Rate								
Range	6.5% - 9%	6.5% - 9.5%	6% - 9%	6% - 9%	6% - 9%	7% - 10%	7.5% - 11%	8.25% - 11%
Mode	8.5%	8.5%	7.5%	7.25%	7%	8.5%	9%	9.5%
Average	8.45%	8.55%	7.55%	7.19%	7.26%	8.28%	9.19%	9.52%
Change	-10 Basis Points	+100 Basis Points	+36 Basis Points	-7 Basis Points	-91 Basis Points	-91 Basis Points	-33 Basis Points	-
Absorption Time (months)								
Range	24 - 48	24 - 48	20 - 40	18 - 36	18 - 43	12 - 44	18 - 40	18 - 36
Mode	36	36	36	30	30	24	24	24
Average	35	34	33	32	30	27	24	23
Change	+1	+1	+1	+2	+3	+3	+1	-
Marketing Time (months)								
Range	1 - 12	1 - 12	1 - 12	1 - 12	1 - 6	1 - 12	1 - 6	1 - 12
Mode	6	8	4	4	4	1	1	1
Average	6.15	7.75	4.31	3.66	3.14	3.06	2.89	3.95
Change	-1.65	+3.44	+0.65	+0.52	+0.08	+0.17	-1.06	-
Profit (on cost only)								
Range	10% - 15%	10% - 20%	10% - 20%	10% - 25%	15% - 25%	10% - 30%	8% - 25%	8% - 30%
Mode	12%	15%	15%	18%	20%	20%	20%	20%
Average	12.5%	14.96%	15.86%	17.63%	20.13%	20.14%	17.10%	14.34%
Change	-16.44%	-5.67%	-10.04%	-12.42%	-	17.78%	19.25%	-
Optimism Index (1 - 10)								
Range	3 - 9	1 - 8	3 - 9	3 - 9	3 - 9	3 - 9	5 - 10	5 - 10
Mode	6	5	6	6	7	6.5	7	7
Average	6.15	5.5	6	6.25	6.5	6.65	6.9	6.83
Change	11.82%	-8.33%	-4%	-3.85%	-2.26%	-3.62%	1.02%	-
Market Conditions								
Undersupplied	10%	10%	10%	6%	15%	15%	3%	6%
Oversupplied	60%	65%	63%	52%	50%	50%	54%	47%
Equilibrium	30%	25%	27%	42%	35%	35%	40%	47%
Strategy								
Buy	40%	20%	27%	15%	18%	20%	27%	28%
Sell	45%	60%	55%	60%	50%	60%	46%	26%
Build	15%	20%	18%	25%	32%	20%	27%	30%
Discounted Cash Flow								
Usage	33%	36%	33%					
Discount Rate (IRR)								
Range	10% - 12%	10% - 12%	10% - 12%					
Average	11.25%	11.5%	10.75%					
Change (Basis Points)	25	75	25					
Rental Growth Rate	3%	2%	3%					
Expenses Growth Rate	3% - 4%	3% - 4%	3% - 4%					
Terminal Cap Rate	+50 bp	+50 bp	+50 bp					
Cost of Sales	4%	4%	4%					
Holding Period	10 years	10 years	10 years					



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KEY SURVEY FINDINGS

This year's survey suggests trade areas remain within a typical three-mile ring. This has been corroborated by hundreds of appraisals completed by our Self Storage Industry Group, which draws from zip-code studies of existing self-storage customers. It is interesting to note that demand per person continues to rise, while supply remains relatively stable. By some estimates, less than 200 new facilities will be constructed in 2010, adding less than one half of one percent to the existing supply nationwide.

Cap and yield rates have shown modest declines. At the end of last year, it appeared cap rates were headed for 9% territory. With new capital (equity and debt), cap rates have stabilized and now appear to be declining. As the industry continues to grow in sophistication, so does the use of Discounted Cash Flow Analysis. This is particularly important for facilities battling absorption in challenging economic conditions – in fact, in some over-supplied markets, it can take so long to reach stabilization that there is no upside to current value. On the other hand, for well-located facilities in absorption phase, cap rates on income in place has been less than 5% on recent transactions. This reflects the upside in the facility and confidence by investors in the asset class over the long run.

The forecast of absorption to stabilization is showing very small declines and remains just under three years. In the boom years, the variance between a stabilized self-storage asset and a vacant facility was very small. Now, variances of up to 20% are typical, reflecting investor desire for profit at the risk of investment in value-add facilities. On the other hand, the gap between buyers and sellers is narrowing, resulting in a decline in the estimate of total marketing time to sell a facility.

Profit estimates on new construction continue to decline, suggesting limited opportunities for feasible new development (assuming construction financing is available at all). However, an increase in the overall “optimism index” in this year's survey underscores the strong performance of the asset class during a recession. Even the estimate of market conditions, which wasn't considered “over-supplied,” suggests an improved outlook by self-storage investors.

Perhaps most intriguing is the number of respondents who indicated that a “buy strategy” is best in the current environment. This strategy may not indicate robust market conditions, but it does support a long-term view of stabilization and improvement. More important, this was a significant and positive change from the attitudes expressed in last year's survey.



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THE EMPHASIS IS ON CASH FLOW

Anecdotally, one REIT chairman said at the end of last year that it “feels like 1994 all over again.” This implied that it was an opportune time for acquisitions below replacement costs, especially with interest rates at historic lows. In this regard, investors are placing increasing emphasis on equity dividends beginning at 7% and equity (levered) yields beginning at 15%. The focus is clearly on cash flow on income in place. Recently, cap rates on existing income decreased for properties with upside potential in rents or occupancy.

Operational management continues to become more sophisticated. Wise operators are using complex modeling to raise rents on existing tenants, resulting in rents-in-place or economic occupancy being higher than physical occupancy. With management efficiencies associated with multi-asset ownership, it appears industry consolidation will continue to take place with fewer owners operating more facilities. One non-publicly traded REIT buyer said that as much as a 50-basis-point premium (or reduction to cap and yield rates) is warranted for portfolios of 10 or more properties over single-asset acquisitions due to efficiencies and savings on transaction costs.

For now, investors are returning capital to storage with an eye on interest rates. The direction and magnitude of rates and yields will be a function of Fed policy, as equity requirements remain stable and firm. Based on the first half of 2010, the outlook is for continued improvement in self-storage market conditions for the balance of the year. However, a game strategy is hard to quantify with economic and financial market uncertainty. Continued focus on property management, discipline and a growing sophistication in due diligence will increase over the next year as the market continues to separate the winners from losers.



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