

Self Storage Investing – By Scott Meyers, CSSM©



Why is Self Storage Suddenly So Hot!

INVESTORS in self-storage stocks finally have some gains to stow away.

The four real estate investment trusts that together own and operate about 12 percent of the facilities nationwide — most of the other properties are mom-and-pop operations — has soared about 31 percent, on average, this year through Thursday, after finishing 2007 with a nearly 25 percent loss.

This year's returns far surpass those of all other property REIT categories as well as the broader stock market. Equity REITs are up around 10 percent so far, on average, while the Standard & Poor's 500-stock index is off about 5 percent.

Why is self-storage suddenly in favor?

Some investors believe that these dividend-paying companies will benefit from the housing crisis. They expect that the ranks of renters will swell as more people leave foreclosed homes or postpone buying their first homes because of tighter credit and falling values, and that those people will need repositories for their excess bric-a-brac.

Industry analysts agree that the sector is likely to hold up well through these economic woes. "It is recession resistant," said Michael Knott, a senior analyst at Green Street Advisors, the investment research firm. "More economic distress causes people to rent more, and, in fact, one of the storage companies said recently that [Detroit](#) was one of the best markets."

Indeed, Detroit had the highest foreclosure rate among the nation's 100 largest metropolitan areas last year, with nearly 5 percent of its households in some stage of foreclosure, according to [RealtyTrac.com](#), the online foreclosure listing service. RealtyTrac put the average nationwide rate at 1.03 percent as of Dec. 31, up from 0.58 percent at the end of 2006. Also high on the list were Las Vegas, [Miami](#) and Denver, along with several boom-and-bust cities in California.

But housing is only part of the story in self-storage, analysts point out. "It correlates to transition," said Michael J. Salinsky, a REIT analyst at RBC Capital Markets.

Demand for storage space is often precipitated by life's passages — marriage, divorce, retirement, enlistment in the military. In addition, use by small businesses has been growing, particularly by those that operate online. "Small businesses need off-site storage, for upsizing and downsizing," Mr. Salinsky said, "and so do people working from their homes."

In the last decade, he said, self-storage revenues have grown 4.4 percent a year, on average, compared with average growth of 3 percent a year for most other commercial real estate sectors.

This steady cash flow, which seems to transcend both good and bad economic times, is attractive to investors. During economic downturns, many investors look for such reliable income, engaging in a "flight to safety."

"This is a cash-flow-driven business that has a low break-even point — expenses are low even if occupancy rates are not high," said R. Christian Sonne, the managing director of the self-storage industry group at Cushman & Wakefield, which provides various consulting services for the sector.

A concrete-and-steel storage facility is typically far less expensive to build and to operate than, say, an office building or shopping center. There are, of course, the standard expenses associated with real estate, like utility costs, property taxes, insurance and payroll, but not too much more.

And after "a huge building boom in the early 2000s," Mr. Sonne said, the development pipeline has been slowing of late, which is also reflected in the newfound resilience of the self-storage sector.

"The barriers to entry are becoming more difficult," Mr. Sonne explained.

For one thing, financing for new structures is harder to get, he said, while zoning is stricter in many communities, which seem to prefer property types that might generate more jobs and tax revenue.

Still, plenty of storage space already exists. By the Self Storage Association's estimate, there are around 51,500 primary facilities nationwide, as well as another 8,400 mini-storage places, or, as the association broke it down, almost seven square feet of rentable space for every person in the United States. A vast majority of this \$220 billion industry, however, is made up of small businesses, making it the most fragmented among commercial property types.

Perhaps because of that fragmentation, "this is probably one of the sectors that is least understood," said David Harris, a REIT analyst at [Lehman Brothers](#).

Mr. Salinsky agreed, though he added that "in storage, you have to be a very dynamic operation to get the returns out of the property." And that might include offering customer incentives like \$1 rents for the first month and ancillary services like moving supplies and truck rentals. (A 10-by-10-foot space rents for less than \$100 a month, on average, according to Mr. Sonne.)

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