The Bulletin

Self-Storage: The Pandemic and Beyond

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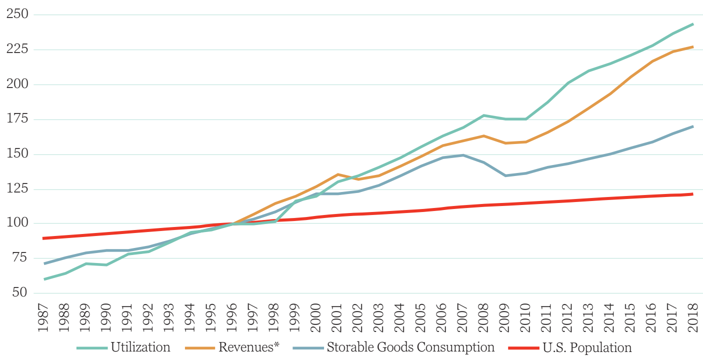
COMING OF AGE

Over the last 60 years self-storage has emerged from being an ugly duckling of real estate into an institutional quality asset class.

Today, it is a ~$40 billion industry[1] with ~50,000 facilities in the United States[2], serving one in every 11 American households. The industry's tremendous growth has been propelled by steady job creation, raising consumer awareness, as well as demographic trends such as urbanization, baby-boomers reaching retirement, and the formation of new households.

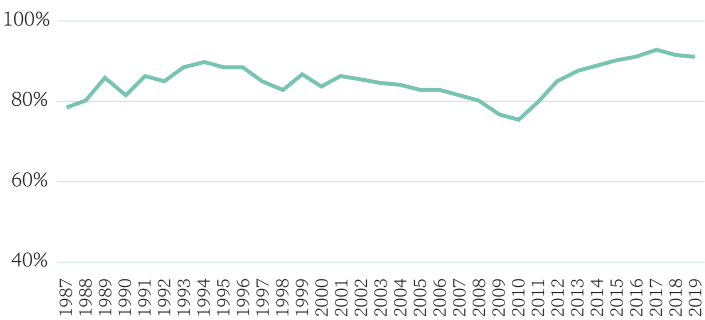
Institutional investors are attracted to self-storage for the strong and stable cash flows, relatively higher yields, low maintenance capex, and high operating margins[3]. Low initial capital investment and short construction time have accentuated the attractive economics of self-storage development and have contributed to the rapid growth of one of real estate's largest alternative sectors.

Self-Storage Demand Trends (Indexed to '96)



Source: Green Street Advisors.
*Public Storage (PSA) same store revenue growth used as the sector proxy.

US National Historical Occupancy



Source: Self Storage Almanac, 2020

US REIT Sectors	Returns from 01/01/2008 to 31/12/2008 (%)	Returns from 01/31/2020 to 15/05/2020 (%)	Average return for 1997- 2019 (%)
Self-Storage	5	-19	15
Healthcare	-12	-39	13
Industrial	-67	-10	13
Lodging	-60	-57	8
Malls	-61	-63	13
Office	-41	-36	11
Residential	-25	-26	13
Manufactured Homes	-20	-18	14
Strip Centers	-39	-51	10
FTSE NAREIT Equity REITs Index	-38	-30	11

Source: Bloomberg, LLC.; Presima Inc.
Note: Property sub sectors represent NAREIT Sub Sector Classifications.

THE PANDEMIC

History highlights resiliency, but near-term challenges exist.

It is widely perceived that, due to inelastic, need-based demand, which remains resilient during economic downturns, self-storage returns are less impacted by the economic cycle.

This proved to be true during 2008 when self-storage outperformed other real estate asset types.

Can the industry prove itself to be immune to the pandemic? The 1Q 2020 earnings season showed that while the industry is more resilient than certain property types, the economic shock caused by the pandemic will nevertheless have an impact on the sector in the near-term. The negative trends, summarized below, are some of the headwinds that the industry is facing.

1. Pandemic strikes during peak season

May-July are the peak leasing season for self-storage, usually driven by college students, home purchases/renovations, and relocations. Uncertainty around the pandemic and stay-at-home orders are delaying customers' moving-in activity, while economic hardship may spur a wave of move-outs when the lockdowns are lifted.

2. Local regulations hinder near-term recovery

With evictions being banned by local authorities and tenants experiencing economic hardship, an increase in bad debt is likely to occur across the industry in the near-term. Recovery of space and re-tenanting may take longer than in previous cycles.

3. Lockdown measures pressure same-store rent growth and margins

During the pandemic self-storage operators have paused rent increases for in-place customers, collection of delayed payments, and charging late fees. This, coupled with new supply that came to the market prior to the pandemic, should slow down rent growth. Additionally, growing expenses such as internet marketing, cleaning, property taxes, and payroll, will likely translate into margin erosion.

> We believe that self-storage REITs have a chance of emerging stronger in the post-COVID-19 world.

THE OUTLOOK

We believe that there is light at the end of the tunnel.

This pandemic represents a shock for many real estate sectors, and self-storage is not an exception. However, when we look beyond the current situation, we believe that self-storage REITs can emerge stronger on the other side of the pandemic.

1. REITS' digital platforms are set to further polarise the storage landscape

Due to fear of infection, the online platforms that minimize human interactions are more important than ever. Industry players that underinvested in contactless tools of leasing and payment prior to the pandemic risk losing market share. We believe that REITs with highly developed internet marketing, revenue management, credit card processing, automation, and maintenance tools will be better positioned to attract customers.

2. Better access to capital can further drive self-storage REITS' external growth

With strong balance sheets, better access to capital, and established third party management platforms, self-storage REITs are better positioned to take advantage of distressed opportunities. With the five largest self-storage REITs controlling ~27% of the market, we believe there is room for further consolidation.

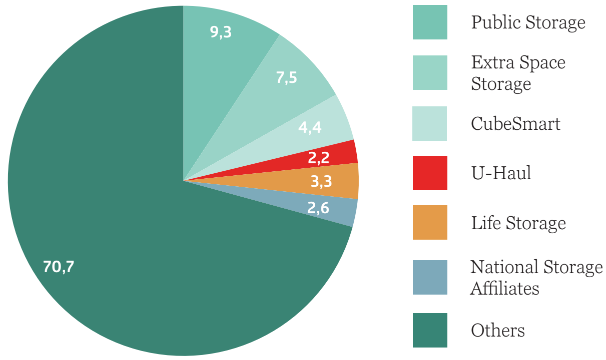
3. The pandemic may improve supply and demand dynamics

Between 2016 and 2019 the industry experienced significant new supply which put downward pressure on rents. Now, with rental rates and margins under pressure and development financing more expensive and difficult to obtain, national development pipelines should diminish[4]. In addition, the pandemic and corresponding economic turmoil will likely trigger life-changing events for many people, stimulating demand for self-storage. Additional demand may also come from business customers looking for space due to disruptions in the supply chain, bankruptcies, onshoring, higher stocking requirements, etc.

4. Strong institutional demand for self-storage likely to support valuations

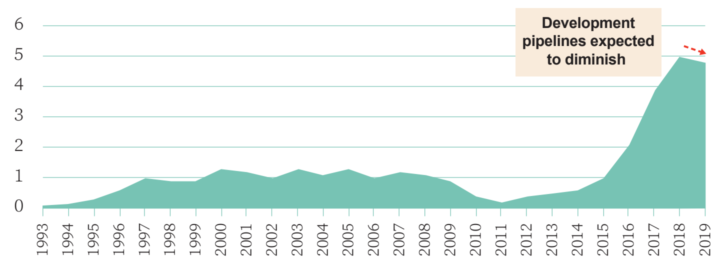
As self-storage shows relative resilience versus other sectors, interest from institutional investors is likely to remain strong. This can support valuations, particularly for stabilized assets with strong cash flows, which make up ~90% of the facilities of self-storage REITs[5].

U.S. Market Share by Square Footage (%)



Source: Self-Storage Almanac 2020, Respective company data (1Q 2020)

U.S. Self-Storage Construction Spending ($ bn)



Source: U.S. Census Bureau

CONCLUSION

While self-storage REITs were also swept up in the broader pandemic-driven REITs' sell off, the sector has fared relatively well versus other real estate sectors. Thus, we believe that self-storage REITs have a chance of emerging stronger in the post-COVID-19 world.

Self-storage REITs with developed digital platforms are better set to attract customers in a post-pandemic world. Better access to capital could help REITs take advantage of distressed opportunities, leading to further industry consolidation. An expected slowdown in new supply development may help the REITs to improve their pricing power. And, finally, strong institutional demand for stabilized assets should help support valuations. We believe that the self-storage sector is poised to yield attractive investment opportunities as the world progresses toward a new normal.

REFERENCES

1. Sparefoot. "U.S. Self-Storage Industry Statistics", 2020.
2. Behrens, P.; Lucas, D. and Shatzer, E. "2020 Self-Storage Almanac." Poppy Behrens, 2020.
3. Sonne, Christian. "Self Storage Economics." *The Appraisal Journal*, Appraisal Institute of Chicago, 2013.
4. Yardi Matrix webinar presentation. Yardi Matrix expects deliveries to decrease by ~40% over the next five years.
5. Based on companies' disclosures.

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