



SELF STORAGE SALES NETWORK

Is Now the Time?

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by Michael L. McCune

In our previous column, I described the economic terrain for those that presently own a storage facility in an effort to help owners be aware of the rocks in the landscape that appear in such lousy real estate markets. However, there is a different view of this market and that is of the potential buyer seeking to take advantage of the highest returns we've seen in years. There are some very good facilities on the market and at low prices (in terms of cap rates) that we haven't seen in a while! Also, many properties on the market are being valued unrealistically and there are even a few properties that may be available from foreclosures. This market is different than the real estate market of the 1980s when there were many good deals available on foreclosed properties. Let's therefore explore where we are at, when it will be the right time to buy and how we can get some properties bought.

The reality is that we haven't seen this market fully unwind yet. The number of foreclosures in self storage is very small, unless of course it is yours. Lately, we have been working with banks and loan servicers on troubled assets and find that for the most part, the number of problem loans is also relatively small, except that some of the REIT's and larger partnerships are now facing large loan expirations within the next few months. In the past, the banker's credo was, "Your first loss is your best loss," meaning it was better to foreclose than to wait for the property's value to further decline. It appears to us in this early stage of the game that banks and CMBS servicers may well be willing to make significant concessions to avoid foreclosures; keeping them from writing off the loan and recording the loss on their books. Thus, it is not yet clear that the foreclosure mode is going to produce many good buys in the immediate future, principally because the banks are unsure of values, or they may believe that the government TARP program may be a better buyer in the end.

There are a number of sellers in the market right now. Not unlike the banks, many of these sellers are "holding out" for high prices that do not reflect the market. These sellers may be relying on old appraisals from 2007 or they may be thinking that the listing price is as low as they'll go to sell the property. Some however may be desperate to sell, thus forcing flexibility. What this usually means is that a tortuous negotiation may be at hand where the asking price and selling price are determined. We suggest that for buyers to be effective in a market as unsettled as this one, they should first think about the listed property or properties that they would like to own. In other words, try to buy properties you believe are quality properties, not those that you *might* buy because they are cheap. Whatever criteria you use to assess value (location, type of construction, demographics, or excess land), stick to those same criteria when you are evaluating properties. This keeps you from buying something cheap that you didn't really want!

The next step in buying a property is to sit down with a banker or a mortgage broker specializing in self storage to make sure there is money to borrow to pursue any deals. You cannot simply assume that there will be money available for a purchase. We are presently seeing rigorous value underwriting (12 months trailing income, 60% to 70% as max loan to value ratios, full recourse, real net worth), short amortizations and shorter terms. In this market having your financing relationships tied down is probably the single most important thing you can do, both for yourself and to convince the seller that you have the financial capacity to do the deal; it will make the negotiations easier and close faster. Once you have this data, you can then run your numbers and develop values that you think are appropriate for the deal. We are seeing deals in cap rate ranges anywhere from 9% to 11% and maybe more in some instances. Give yourself a little room because the current market is so unique and volatile that there are very few sales where an exact cap rate is easily determined. Choose your property picks and rank them according to preference and start calling the listing broker for more information.

When talking to the listing broker, tell him or her all you can about your experience and financial capacity and let them know that you have studied the information and are a serious buyer. Next, visit the property, review everything that is available, ask all your questions and then make a formal offer in writing. Ask

the broker (and owner if possible) to sit down with you and explain how you arrived at the offering price. Both the owner and the broker will appreciate you being forthcoming about your methodology and they may even see that either the market has changed, or their original valuation is off the mark. These are difficult decisions for a seller too as many owners have strong emotional ties to a property. Therefore, give the seller a reasonable timeframe to agree to the deal, a reasonable due diligence timeframe in the contract and as short of a closing as possible to get the loan done. Very likely the owner will counter with a lower price (this should be expected). If you get a reasonable counter, then you counter back. You may, however, decide that you are too far apart on price to counter, in which case you should say that you “really like the property and would like to buy it, but this is the price I can pay.” Tell him that you will leave the offer open for another week (two weeks?) if he would like to accept the offer. What you are waiting for is the seller to reconcile the reality of selling the property at your price or not selling at all. If he doesn’t want to sell, then move on to the next property on your list, and always have a property on your list so your desire to “do a deal” doesn’t compromise your financial or quality goals.

Michael L. McCune is President of the Argus Self Storage Sales Network, a self storage real estate brokerage and development company based in Denver. Argus also operates www.selfstorage.com, a marketing medium for owners in the self storage industry. For more information call 800-55-STORE or visit www.selfstorage.com.