Households:
The United States will add more than 1.3 million households in 2016, an expansion of 1.1 percent from year-ago levels. Healthy household formation will intensify underlying demand for storage, particularly in urban employment hubs where growth is strongest.

Vacancy:
Strong job growth will intensify demand for self-storage with the national vacancy rate on pace to reach 10.1 percent by the end of 2016, down 110 basis points year over year. As of midyear, the weighted average self-storage REIT vacancy is 5.6 percent.

Climate-Controlled Rents:
Following a rent increase of 3.2 percent last year, the climate-controlled segment will record a 3.6 percent rate hike in 2016 as tenants pay an average of $1.62 per square foot.

Non-Climate-Controlled Rents:
Healthy rent improvements will continue for non-climate-controlled units with the average rent expected to reach $1.29 per square foot in 2016, up 4.0 percent. Last year, a rent increase of 4.3 percent was recorded.
National Economic Overview

Employment: Aside from a misstep in May, job growth has been robust in the first half of 2016 with the nation creating more than 1 million jobs in the past six months. On a year-over-year basis, the U.S. workforce expanded 1.7 percent through the addition of nearly 2.5 million positions.

Population: In 2016, the total U.S. population will expand 0.8 percent year over year, an increase of nearly 2.5 million people. The bulk of these gains will come from those age 55 and older. This cohort will grow 2.6 percent or by 2.3 million people, which may benefit self-storage as baby boomers retire and downsize.

Income: Steady job growth and rising wages will drive a 2.4 percent increase in the median household income, which will reach $57,500 by the end of 2016.

Retail Sales: In 2016, annual retail sales volume will swell 3.6 percent from year-ago levels as residents leverage their greater disposable income to ramp up consumption.

Regional Overview

West

Vacancy: The West boasts the lowest vacancy among all the regions as healthy population growth and the robust tech sector lift demand for self-storage. The regionwide vacancy rate will fall 100 basis points year over year, reaching 9.2 percent by the end of 2016.

Rents: Declining vacancy will put upward pressure on rents. The average asking rent for climate-controlled facilities will climb 3.3 percent this year to $1.60 per square foot. Meanwhile, average asking rent for non-climate-controlled units will jump 4.5 percent to $1.49 per square foot.

Prices: The average sale price surged 8.9 percent in the past 12 months to roughly $88 per square foot in June, the highest price point since 2000.

Cap Rates: Buyer and seller expectations are beginning to widen as cap rate compression levels off. The average first-year return nudged up 25 basis points year over year to the mid-6 percent range in the second quarter.

Southwest

Vacancy: The Southwest vacancy rate will fall 100 basis points to 10.4 percent this year, led by robust operations in the Texas markets. Fort Worth and Houston are particularly tight and will see rates compress to the low-9 percent range.

Rents: Non-climate-controlled units will record a 3.9 percent rent increase in 2016, reaching 98 cents per square foot. Meanwhile, the average asking rent at climate-controlled centers will jump 3.4 percent to $1.38 per square foot.

Prices: The average price per square foot surged in the last 12 months, reaching an average of $72 per square foot. This is more than 40 percent greater than the pre-recession peak set in 2006.

Cap Rates: The average first-year return for a Southwest storage facility remained flat in the last 12 months, hovering in the high-6 percent area.

* Forecast
** Through July
Sources: Moody’s Analytics; REIS Services, LLC.
Regional Overview

Northeast
Vacancy: High multifamily rents are bolstering demand for self-storage as residents struggle to find enough space to house their belongings. As a result, vacancy in the Northeast will drop 120 basis points to 10.7 percent in 2016.

Rents: The Northeast boasts the highest rents among all regions. It is led by New York City, the most expensive metro in the country. Average rents in the region will climb 3.5 percent to $2.08 per square foot and 3.8 percent to $1.61 per square foot for climate- and non-climate-controlled units, respectively.

Prices: The Northeast has the priciest facilities in the country by a wide margin. Investors paid an average of $142 per square foot at midyear, up 17 percent from year-earlier levels.

Cap Rates: The tremendous compression of cap rates recorded in the past few years has bottomed out with returns posting a modest uptick in the last 12 months to a midyear rate in the high-6 percent range.

Midwest
Vacancy: The regionwide vacancy rate will decrease 100 basis points to 11.3 percent in 2016 as the Midwestern economy continues to make gains. The Ohio markets registered the greatest drop with Cleveland and Columbus falling 200 basis points and 160 basis points, respectively.

Rents: The average asking rent for climate-controlled complexes will swell 2.8 percent year over year to $1.48 per square foot in 2016. Concurrently, non-climate-controlled rents will rise 3.4 percent to $1.03 per square foot.

Prices: The rise in valuations for Midwestern self-storage units has moderated with the average price essentially remaining flat in the past year at $64 per square foot.

Cap Rates: The Midwest posted the strongest compression of cap rates of all regions. The average first-year yield dropped 75 basis points in the last four quarters, reaching the high-7 percent range in June.

South Atlantic
Vacancy: Following a 120-basis-point contraction in 2015, the South Atlantic region will tumble another 120 basis points, reaching 10.2 percent by the end of the year. Nashville and the Florida markets remain highly compressed.

Rents: Climate-controlled facilities will register a 4.3 percent rent increase this year with tenants paying an average of $1.59 per square foot. Non-climate-controlled rents will jump 3.8 percent to $1.17 per square foot in 2016.

Prices: South Atlantic valuations surpassed the prior cycle peak as buyer demand remains intense. The average price per square foot rose 4.2 percent in the last year to nearly $74 as of the second quarter.

Cap Rates: An aggressive buying environment continues to exert downward pressure on cap rates; however, yields will likely firm up in the coming months. In June, the average first-year return reached the high-6 percent band.
Capital Markets

By WILLIAM E. HUGHES, Senior Vice President, Marcus & Millichap Capital Corporation

Lenders remain keen to provide financing to the self-storage sector; however, capital providers have become increasingly selective as they reassess credit risk amid global economic uncertainty. Underlying demand for storage space is intact as an improving job market and healthy demographics drive occupancy and rent gains. Deals with strong underwriting in primary and secondary markets will have access to capital, but tertiary locations or oil-reliant markets may give lenders pause.

CMBS remains the primary source of self-storage loans and all-in rates typically start in the low 4-percent range. Spreads here have narrowed approximately 50 basis points since earlier in the year. With Treasuries currently in the mid-1 percent range, CMBS is an attractive 10-year alternative for this product. These deals are typically underwritten to produce LTVs of around 70 percent with debt yield ratios at 8.5 to 9 percent. It looks as though CMBS has moved beyond concerns over the imposition of new risk retention standards as recent issues structured with a retention component have been received well with strong interest. Bridge lending for expansion or repositioning purposes has become more prevalent; however, loan terms are stringent, particularly in the $1 million to $5 million range, and uncertainty surrounding the length of the expansion cycle may sow further caution.

2016 Metro Outlook

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<tr>
<th>Metro</th>
<th>Vacancy</th>
<th>Y-O-Y % Change</th>
<th>ACC* Rents</th>
<th>Y-O-Y % Change</th>
<th>ANCC** Rents</th>
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* Through July
Sources: Marcus & Millichap Research Services; CoStar Group, Inc.; Real Capital Analytics; Federal Reserve Board.

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