Extra Space CEO Spencer Kirk: Internet Is ‘Great Divider’ in Self-Storage

JOHN DONEGAN JUNE 20, 2013 2

To all those mom-and-pop operators in self-storage who think the Internet can level the playing field, Extra Space Self Storage Inc. CEO Spencer Kirk has this message: The biggest teams on the field also are the strongest ones.

“The larger, more sophisticated operators seem to have a significant, pronounced advantage when it comes to the Internet,” Kirk said. “The Internet is not the great equalizer. The Internet is the great divider.”

He attributes this divide to the scale, size and sophistication of the major players.

According to Kirk, two macroeconomic issues ensure the big self-storage operators (Extra Space, Public Storage Inc., Sovran Self Storage Inc. and CubeSmart) will remain on top: the Internet and the lack of new supply in the marketplace. At the recent NAREIT’s Investor Forum, Kirk said: “We don’t see abatement to these two macro issues.”

Here are some other issues Kirk addressed at the NAREIT event.

No New Supply
“There’s virtually no new supply in our space.”

From 2003 through 2007, more than 13,000 self-storage facilities were constructed, putting the total supply at around 50,000. However, far fewer facilities are being built today. According to the most recent McGraw Hill Construction Dodge report, 196 facilities were under construction at the end of 2012.

With the U.S. population increasing each year by roughly 1 percent, or 3 million people, Kirk said that "we would need well over 500 (newly constructed) properties just to keep pace with the population increase." Thus, self-storage demand is outpacing supply.

The Internet

"The Yellow Pages are dead. We don't use it."

With few Americans still using the phone book, ExtraSpace and other larger operators have allocated more money to Internet marketing, including SEO and PPC initiatives. Extra Space spends more than $34,000 every day on "interactive marketing." Back-of-the-envelope math puts this spending at more than $12.4 million a year.

"More than 60 percent of our newcomers use the Internet at some point during the purchase decision," Kirk said. "What that means is if you're a larger, more sophisticated operator and have the wherewithal to compete on the Internet, you can capture a disproportionate share of the traffic."

Online Pricing

"If you don't offer a hyper-competitive price, they'll click away."

Generally speaking, online customers are much more sensitive to price than walk-up customers are. In fact, self-storage operators usually can charge higher rents to walk-up customers. More than 40 percent of the time, Extra Space facilities gain higher rental rates from walk-ups.

Aggregators

At the NAREIT Investor Forum, moderator Christy McElroy of UBS asked: “What’s your view of some of the aggregators that have surfaced to help some of the smaller operators compete? Is that a threat to (your) market-share gain?”

Kirk passed off that question to Chief Financial Officer Scott Stubbs, who replied: “We don’t necessarily see aggregators as a threat. We use them on occasion. We see it as another acquisition channel. Basically, it’s another shot at a customer–what we’ve found is people that shop using aggregators are typically a different kind of customer. They’re generally more price-sensitive.”

Despite Stubbs’ assertion that aggregators don’t pose a threat, it’s clear that McElroy thinks aggregators do, in fact, help mom-and-pops compete.

Management Consolidation

As Sovran CEO David Rogers has said, self-storage operators don’t necessarily make money through third-party management. But that’s really not the point. Third-party management provides insight into facilities’ books and often leads to acquisitions.

Kirk and Stubbs concur. They also believe in the benefits of third-party management and expect to see more of what they call industrywide “management consolidation.”

“I think (management consolidation) is largely driven by the fact that the little guys are having a harder time competing on the Internet,” Stubbs said. “So, they come to us and join our management program, and we rebrand the properties as ExtraSpace.”

He added: “We are seeing more and more (mom-and-pops) interested in that. They’re looking at ways to compete. Aggregators is one way, and management is another.”

Rent Increases
Kirk said ExtraSpace has “probably been the most aggressive” major self-storage operator when it comes to rent increases.

ExtraSpace uses what you could call a “5-9-9-9 system.” After a customer has been with ExtraSpace for five months, his or her rent is hiked. That’s followed by rent increases at subsequent nine-month marks. On average, about 50,000 ExtraSpace customers are hit with a 9 percent rent increase every month.

Development
On a risk-adjusted basis, self-storage development doesn’t make much sense to Kirk. For ExtraSpace, it’s more prudent to buy existing properties.

For starters, it takes a year to construct a facility. Then, Kirk said, “it takes two years to get an entitlement. Why? Because a city planner wants to stick you at the end of the cul-de-sac next to the industrial warehouses. That’s death for self-storage. We want to be next to Walmart or Home Depot–in the retail corridor.” After that, it takes two to four years to lease to capacity. All told, it takes five to seven years to bring a facility to capacity.

Acquisitions
All things being equal, ExtraSpace prefers deals that involve an entire portfolio of properties, although

Stubbs said the REIT considers smaller deals as well. “A lot of people add a portfolio premium,” Stubbs said, “so the one-offs are sometimes the best cap-rate deals that we find.”

Second image courtesy of ewaste411.com