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EXR - Q2 2014 Extra Space Storage Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the second-quarter 2014 Extra Space Storage earnings conference call. My name is Denise, and I'll be the Operator for today. (Operator Instructions). As a reminder, this conference is being recorded for replay purposes.

I would now turn the conference over to Mr. Clint Halverson, Vice President, Investor Relations. Please proceed.

Clint Halverson - *Extra Space Storage Inc. - VP Corporate Communications & IR*

Thank you, Denise . Welcome, everyone, to Extra Space Storage's second-quarter 2014 conference call. In addition to our press release we've furnished unaudited supplemental financial information on our web site.

Please remember that Management's prepared remarks and answers to your questions may contain forward-looking statements as defined in the Private Securities Litigation Reform Act. Actual results could differ materially from those stated or implied, by our forward-looking statements due to risks and uncertainties associated with the Company's business. These forward-looking statements are qualified by the cautionary statements contained in the Company's latest filings with the SEC which we encourage our listeners to review.

Forward-looking statements represent Management's estimates as of today, Thursday, July 31, 2014. The Company assumes no obligation to revise or update any forward-looking statements because of changing market conditions, other circumstances after the date of this conference call.

With that, I would now like to turn the call over to Spencer Kirk, Chief Executive Officer.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Good afternoon, everyone.

We started the year with record high occupancies. And the question was asked: How hard can Extra Space push street rates? Well, street rates were up nearly 5% on average for the quarter. On top of these strong rate increases, discounts decreased by an average of 18%. And, aided by limited new supply, occupancy still climbed 160 basis points to 92.4%.

These factors contributed to NOI growth of 9.9% for the quarter and FFO year-over-year growth of 26%. In addition, we raised the dividend 17.5%. It was another solid result for Extra Space.

Now I'd like to turn the time over to Scott.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Thanks, Spencer. Last night we reported FFO of $0.63 per share for the second quarter. Adjusting for noncash interest and acquisition-related costs, FFO was $0.64 per share. We outperformed our guidance due to better than expected property performance and tenant insurance results.

At the start of this year we added 99 properties to our same-store pool, bringing the total to 443 properties; 90 of these properties were acquisitions and nine came from our legacy development pipeline. This change in our same-store pool added 75 basis points to our revenue growth for the quarter.

The acquisition environment has become increasingly more competitive. We are committed to remaining disciplined in our approach to building long-term value for our shareholders, and during the quarter we acquired eight properties for $91.2 million.

We currently have five properties under contract for $41.4 million, which should close by the end of the third quarter. As of today, we have closed or have under contract, $382.3 million. Included in our year-to-date acquisition totals are two ground-up development properties that we acquired upon completion in Q1. In addition, we have three more development properties under contract that we will acquire upon their completion in 2015 and 2016.

We have revised our full-year 2014 FFO guidance to be from $2.42 to $2.50 per share. These estimates include noncash interest and acquisition-related costs. When adjusting for these items, FFO is estimated to be from $2.46 to $2.54 for the full year.

I'll now turn the time back to Spencer.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Thanks, Scott.

August 12th will mark 10 years for Extra Space as a public company, and it's been an excellent run. We went public with 136 locations and today we have nearly 1,100. I want to take a moment to thank our investors, our management team and, most importantly, our employees. It's a great time to be in storage.

With a distinct advantage on the internet when it comes to customer acquisition and with muted supply, we see continued opportunity for double-digit FFO growth. Our job as a management team is to increase FFO and enhance shareholder value. This quarter's 26% FFO growth marks 15 consecutive quarters of double-digit gains.

Now let's turn the time over to Clint to start the Q&A session.

QUESTIONS AND ANSWERS

Clint Halverson - *Extra Space Storage Inc. - VP Corporate Communications & IR*

Thank you, Spencer. As in the past, in order to ensure we have adequate time to address everyone's questions, I'd ask everyone to keep your initial questions brief and, if possible, limit it to two. If time allows we will address follow-on questions once everyone has had an opportunity to ask their initial questions. With that, we will turn it over to Denise to start our Q&A session.

Operator

(Operator Instructions) Christy McElroy; Citigroup.

Christy McElroy - *Citigroup - Analyst*

Spencer, I just wanted to follow up on your comment on street rents. Can you discuss some of the customer behavior that you're seeing when you change the rate at which you're pushing rents sort of at the street level? And are you pushing those rents with the idea that you'd sort of still like to push occupancy further, so you're holding back a little bit? Or are you kind of happy with this level of occupancy such that you're pushing rents as much as you can just to maintain occupancy?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Christy, great question. Philosophically, what we're trying to do is maximize revenue. We obviously like where the occupancy is. I don't know how much higher you could go in a peak season. We feel this quarter we have pushed rates as much as is reasonable and rational. We are coming into the shoulder season and we need to recognize that holding onto our occupancy gains is going to be a primary focal point for us.

To maybe put a little color into it, I can tell you at the end of June the rates were up just about 7%. So as we started the beginning of the year, we were holding the rates down, to build occupancy. As we came into busy season we pushed rates hard and we also got 160 basis points of occupancy gain. And this will come full cycle as we come into the latter half of this year where we're going to maybe moderate some of the push for rate to maintain the occupancy.

Christy McElroy - *Citigroup - Analyst*

So you were 5% on average for the quarter and 7% at the end of June?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Correct.

Christy McElroy - *Citigroup - Analyst*

Okay. Got you. And then, Spencer, I wonder if you could provide your thoughts on the potential threat of aggregators, especially given as a company you've been somewhat vocal on the topic. Do you see Google entering the game anytime soon? And what could be the potential implications for pricing power?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

It's an excellent question. First of all, if you look at the aggregators in the space, they play a role. For Extra Space I can tell you that our cost per acquisition, the CPA, using an aggregator is considerably higher than our own internal cost per acquisition. So we do not use other aggregators to drive our business.

Google has entered other business sectors. They very well could enter the storage sector. Obviously that would change many of the rules. But if Google becomes the source, what we would do is tell Google the profile of the customer we want them to go after. Hence my statement many, many times: The single most valuable asset this company owns is now its data. And with that data I think working with a company like Google we would still probably be in a preferential position because we would have the knowledge to direct Google specifically to the higher value customers that would fit best with what we're doing.

Christy McElroy - *Citigroup - Analyst*

That's helpful. Thank you.

Operator

Todd Thomas; KeyBanc Capital Markets.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Just a question on acquisitions. I know $500 million of deals, still a big number for the year. But I think it's been a little while since we've gone two quarters now without there being some upward pressure on deal volumes around your guidance. So I'm just curious whether something has changed with regard to your underwriting criteria, the quality or pricing of the deals in the market, maybe seller expectations. It just appears that the investment environment has slowed somewhat.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Todd, this is Scott. We have seen the environment get very competitive. I mean, it's not just the four REITs. You're seeing a lot of other money chasing the deals that are out there. So pricing has gotten very competitive. As we've gone through and done our guidance we're still comfortable with the $500 million. One thing that did change is it's pushed more towards the end of the year. And the cap rates have moderated somewhat. We would tell you the cap rates have come down some even since we gave our initial guidance to begin the year.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

How much have cap rates come down versus your initial guidance?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Probably 25 basis points.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay. And then, looking ahead for EXR, do you see acquisition activity continuing to move away from stabilized property to more of these C of O type deals? Is that something that we should expect to continue to see grow in size within the pipeline as you're sort of thinking about it?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We continue to look at these deals. We bought one last year. We bought two in the first quarter of this year. We have a few more under contract that are slated more for 2015, 2016. We'll continue to look at those. We're trying to balance the growth in those properties with also the dilution that comes with those. I mean, one of the things we would consider if it gets too big is to look to a JV partner or something of the sort.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Yes, Todd. This is Spencer. The only additional color I might give you is I think you'll still see Extra Space participating in the open market acquisition environment as well as what I call the off-market, where we've got the JV and the managed assets that have provided meaningful growth for our company over the last several years.

You're going to also see more opportunities for these C of O deals pop up. To expect that there will be no new supply forever in this space is not reasonable. And I think what we're seeing is that there is some supply coming. It's muted, greatly muted at this point. But I think that most of those, the would-be developers, are acknowledging that the landscape for leasing up and operating that property that they helped to build has changed. And they need to align themselves with a larger, more sophisticated organization.

And so I think you'll see continued acquisition opportunities augmented with some of these C of O deals coming in to provide another growth channel. So I'm actually quite optimistic that this gives us some new, brand spanking new, properties into our system that will complement the existing assets that are fully stabilized that we hope to use to grow the platform.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay, great. And that C of O, the plan is that Extra Space takes over 100% of the ownership?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

That is the plan right now. The ones we've done to date have been 100%. Again, we would potentially look to a JV as the volume increases, where we buy the developer out with a JV partner, not necessarily JV-ing with the developer.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay. Thank you.

Operator

Vikram Malhotra; Morgan Stanley.

Vikram Malhotra - *Morgan Stanley - Analyst*

Thank you. Could you just give us a breakout of the price increase that you saw, the 5% price increase between street trade and existing customers?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

I'm not sure I'm following the question. You're talking the 5% -- so when we say 5%, our street rates were up on average 5%.

Vikram Malhotra - *Morgan Stanley - Analyst*

Sorry. I meant the overall price increase. Could you just break that down into the different components?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Yes. Our revenue growth has grown from several different components. One is the occupancy. Year to date, it's prob- -- it's roughly 2% of our growth has come from that occupancy increase. About 4% has come from pricing. About 0.5% to 1% has come from discounts. And then another 0.5% has come from existing customer rate increases.

Vikram Malhotra - *Morgan Stanley - Analyst*

Okay. And then just on the web-based or the internet-based pricing, was there anything that changed this quarter in terms of the overall strategy? Meaning, I know you've talked in the past about targeting customers even more. But was there anything changed on the web in terms of just pricing more granularly, which may have hurt pricing a bit but also could that help in sustaining a relatively higher level of pricing in the off season?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We have not had any significant changes in this quarter to our web strategy.

Vikram Malhotra - *Morgan Stanley - Analyst*

Okay. Thanks, guys.

Operator

Ki Bin Kim; SunTrust Robinson.

Ki Bin Kim Thanks. So similar to the kind of breakdown you gave just a second ago on same-store revenue growth, given -- could you do a similar exercise for maybe what you expect in the second half of the year? And part of that reason why I ask this question is because mathematically it seems like you're -- seems kind of like guidance is on the surface coming down for the second half and possibly why your stock is reacting the way it is today.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Yes, absolutely. So the two components that would change from what I gave just a minute ago -- we view pricing as staying pretty similar, our rate increases to our existing customers very similar. The occupancy delta will go down. Right now it has been -- it was for the first half of the year closer to 2%. Right now it's closer to 1.5% and we see that dropping.

Then second of all, our discount, while it's been closer to 1%, we see that growing closer to 0.5% as far as the total add.

Ki Bin Kim Okay. And so I guess at the end of the year your occupancy benefit should be maybe closer to 1%?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Correct. So we see it pretty -- correct. You're absolutely right. It started at just over 2%, dropping to 1% at the end of the year.

Ki Bin Kim Okay.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

So call it 1.5% average for the year.

Ki Bin Kim Okay. All right, that's it for me. Thank you.

Operator

David Toti; Cantor Fitzgerald.

David Toti - *Cantor Fitzgerald & Co. - Analyst*

I want to go back to the development topic a little bit, because this is has been an interesting evolution for the Company, hard core developer to no development to acquiring C of O sort of off-balance-sheet mitigating risk. How are you underwriting these deals today that would be differently than, say, how you were underwriting in 2006? And I guess secondly, can we expect an evolution further closer to your historical franchise?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

I would tell you not to look for us to get into full-scale development. I don't see that changing. I think we've said it throughout the whole downturn and into today. We've been pretty consistent in saying we don't want to do development. The beauty of this is it enables us to add new properties to our pipeline. Many of our properties -- as time goes by properties age. So this enables us to bring new product in.

As far as underwriting them, we feel like anytime you do a development property you have entitlement, construction risk, and lease-up risk. By doing it the way we're doing it, you eliminate two of those three risks. The only risk we really have is lease-up risk. So as we underwrite them, I would say your typical yield is going to be 1.5 -- 150 to 250 basis points. Your cap rate's going to be 150, 200 basis points higher.

David Toti - *Cantor Fitzgerald & Co. - Analyst*

So I guess more specifically, what kind of stabilized yields are you looking for? And what type of lease-up timeline are you looking at in those specific deals today?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

So lease- up yields --

David Toti - *Cantor Fitzgerald & Co. - Analyst*

[When you've underwritten --]

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Yes. When we've underwritten these we've tried to go with our historical average lease-up. So they're usually three- to five-years, kind of depending on where they are, the density and the size of the property. So we're not necessarily projecting today's lease-up. Because if you open something today I think it's going to lease up very quickly. But many of these aren't going to be open for a year or two, so we've tried to be pretty middle of the road on our estimates for lease-up.

Then as far as stabilized yield, I think it's -- we are eventually going to get to the cap rates where they are today. So if something's trading at a 6.5 cap today we're saying it's a 6.5 cap deal at 150 to 250 basis points [to] that.

David Toti - *Cantor Fitzgerald & Co. - Analyst*

Okay. That's helpful. And then, I have kind of a weird question which I never thought I'd ask on a call. Are there any assets or markets where you're seeing such high occupancy levels that you're actually pushing rates so aggressively as to induce move-out and more churn?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Yes, it's a great question. I would say on the margin, David, if I could use an example, I think Seattle might be a reasonable place to say we've had some really strong success up there. We don't like to push out customers. What we don't want to do is push so hard that the customer that has been with you for several years, who has had multiple existing customer rate increases walks out the door.

So it's not so much creating vacancy at the front end. It's with your existing customers where you'd be pushing the rate to create the vacancy. I don't know if that helps.

David Toti - *Cantor Fitzgerald & Co. - Analyst*

Yes, well, I guess maybe said another way is -- do you see a point where there's going to be certain markets where the street rate's going to be so much higher than a lot of your in place that you won't be afraid to potentially dislodge that longer-term customer?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

I can't foresee that. Anything's possible but I think we're on a revenue management system working pretty well in a coordinated fashion to make sure that the street rate and the existing customer rates are where they need to be to optimize revenue, not only a snapshot in time but over a protracted period.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

And to date we really haven't seen a site where street rates grew so fast that they outpaced existing customer rate increases.

David Toti - *Cantor Fitzgerald & Co. - Analyst*

Okay, great. Thanks for the detail.

Operator

Michael [Hillscott]; RBC Capital Markets

Michael Salinsky - *RBC Capital Markets - Analyst*

Oh, that's an interesting one. First question -- you gave some color on acquisitions. You said cap rates are down about 25 basis points on a year to date. Are you seeing the underlying IRRs change? Meaning, is growth keeping pace to support that cap rate compression? Or are people just getting more aggressive in terms of bidding?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We're seeing people being more aggressive in bidding. And, again, it goes to their assumptions on their growth rates. And we don't know what those are. We haven't necessarily changed ours.

Michael Salinsky - *RBC Capital Markets - Analyst*

Okay. Second of all, just as you think about CO buyouts there, obviously being 2015, 2016 that you have a couple coming on line, what level of dilution are you comfortable taking on in the short term for that long term? I mean, how are you thinking about managing that process?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

I think overall, Michael, if you looked at it in terms of we're willing to take 2% or 3% dilution to potentially have bigger growth in the future and to refresh our portfolio.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Yes, so when Scott talks about dilution and you look at the total FFO that we might produce in a year, and we say -- what percent would be tolerate? And it's kind of in that 2% to 3%. What we don't want to do is go back to the days -- which is why we are not going back into full-blown development. I'll take any ambiguity out of that. Because as a public company we never got credit for the developmental pipeline and the drag of the -- development had on our earnings. And we think we can bring a lot of new product to market using a different methodology. And that's with the C of O deal where we've pushed out a lot of the risk, two of the three risk elements that Scott addressed. And even perhaps with a joint venture partner, have much of this, for all intents and purposes, be off balance sheet.

So for us, we think of it as a way to refresh our portfolio, participate in some of the new product that will come to market. And what we offer is a win/win. The developer with local expertise can do things that we never were able to do. They have contacts and relationships in their local markets that we cannot replicate.

On the other hand, we have a platform that once that property is built that developer can never replicate. It's beyond their ability. And it creates a symbiotic relationship where we both win. And we march forward with a mutually beneficial transaction.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Yes. We would say it's going to be tough to really get a huge volume of these, Mike, just in terms of pricing and in terms of actual new product coming on line. I mean, it's a competitive market out there, so to even get 2% or 3% I think is going to be difficult.

Michael Salinsky - *RBC Capital Markets - Analyst*

[Allotted] the two questions there and jump back in the queue. Thank you.

Operator

Todd Stender; Wells Fargo.

Todd Stender - *Wells Fargo Securities - Analyst*

Thanks for the color on how you underwrite the C of O deals. I think it's very helpful. Just to stay on that theme, just one question. Can you tell us what markets the C of O deals you have teed up for 2015 and 2016? Just thinking -- do they need to be located within your existing footprint just to mitigate some of the risk as you build out some level of scale?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

The three we're talking about, two are in Boston, one is in Phoenix. The two that we've bought to date, one is in Texas and the other one is in Connecticut.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Existing footprint, Todd, is very important to us as we look at these opportunities. We don't want to go into a market where we have no operational scale and where we don't have the infrastructure to support it.

Todd Stender - *Wells Fargo Securities - Analyst*

And are you experiencing any inbound flow of questions or you guys are seeking these out from developers you have relationships with?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

It's almost 100% inbound.

Todd Stender - *Wells Fargo Securities - Analyst*

Great. Thank you.

Operator

(Operator Instructions) Tayo Okusanya; Jefferies.

Tayo Okusanya - *Jefferies & Co. - Analyst*

I just had a quick question in regards to mark to market on the portfolio again, this idea of how much you're getting when you get a new tenant moving in versus how much you're losing when an existing tenant moves out, what that spread differential looks like and whether that's still a big drag on the portfolio when it happens.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

So in the past we've always answered this with our street rates are on top of our existing customers, which is still the case. But street rate isn't necessarily what you get. You're usually giving some type of discount or you're coming in at an internet rate or something of the sort. So our typical rollback is, call it, 6%. It's mid-single digits.

Tayo Okusanya - *Jefferies & Co. - Analyst*

Okay, the rollback, okay. That's helpful. And then, from the press release when you kind of talked about markets performing below the Company's average, you do highlight Washington, DC and Baltimore. Just kind of curious that market in particular, because a lot of office properties are having issues there as well as a lot of multifamily -- whether it's just the general economy in Washington, DC/Baltimore that's creating the underperformance or if you are seeing something very specific to self storage

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Spencer Kirk - *Extra Space Storage Inc. - CEO*

Okay, Tayo. This is a really important thematic piece. Storage is a great business. And we can take one of our worst performing markets to date, DC, and the NOI is still a very respectable 5.0% for the quarter. So if you were talking any other asset class you'd say -- great job, guys. And that's one of the worst we have.

So the themes of muted supply and dominance on the internet still play out. And we're very comfortable that this is going to be a solid year in 2014 for Extra Space and for the other larger, more sophisticated operators. Nothing has changed. And I think there has been some concern about a pullback, and of course there's going to be some seasonality to our business. But in terms of the fundamentals of the business it's strong. It's healthy. And DC is just a nice point of illustration to say a poor performing asset is still 5% NOI.

Tayo Okusanya - *Jefferies & Co. - Analyst*

Great. That's helpful. Thank you.

Operator

Dave Bragg; Green Street Advisors.

Dave Bragg - *Green Street Advisors - Analyst*

Returning to the topic of development, when we think about Extra Space and your web platform, your data, your operating platform, we're interested in hearing how you think that these advantages of yours could help you better select sites and hasten the lease-up process.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We obviously hope to outperform our lease-up estimates. And I think that what you're seeing today is very good in terms of lease-up. But as far as projecting that and actually underwriting that, it's not necessarily what we're doing. We'd rather be surprised on the upside. We think we do have the ability to drive rentals. And it is particularly strong in markets where we already exist.

So, for instance, the properties in Boston should do very well because we have a very strong web presence there. So as we focus or look at any development certificate of occupancy type deal, it's going to be important for us to have a presence there. And for this property we have a very good location.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

So one other comment on that, Dave. I talked about data being a valuable asset for this company. So when a C of O deal gets plopped into the middle of one of our core markets, we obviously have a lot of data as to what to expect on rate and transactional velocity. And we can and will use that to optimize the performance of that lease-up asset so that we end up with a better result than had we not applied the data to the assumptions and to the operations. So I think it goes hand in hand.

Dave Bragg - *Green Street Advisors - Analyst*

And along those lines, Spencer, do you think that the lease-up pace that you'll experience will exceed that of your prior ventures into development?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

It depends completely on the product, as Scott said, the size, the market, the square foot per capita and a host of issues that would cause me to say -- Dave, I'm not even going to speculate. I'm going to tell you that we're going to underwrite it to the best of our ability to prognosticate. And we'll see what the result is.

Dave Bragg - *Green Street Advisors - Analyst*

Okay. But all those things equal, is your process better? Is your data better? Looking to understand if this will provide you an advantage as compared to others looking at similar deals.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We think it's better. I think the major difference for us is there's less new supply today than when we were developing. I mean, there's a significant difference in the amount of properties coming on line today. Obviously we're more sophisticated than we were then. So I think on the margins we should do better.

Dave Bragg - *Green Street Advisors - Analyst*

Thank you.

Operator

Ki Bin Kim; SunTrust Robinson.

Ki Bin Kim - *SunTrust Robinson Humphrey - Analyst*

Just a couple quick follow-ups. In your guidance have you fully baked in the fact that when you have higher street rates, the negative mark to market, or negative [rollout,] I should say, from a tenant that's been getting rent increase letters then when they move out and where it gets marked to, that benefits as well and that's the benefit of street rates improving? That becomes better. And also, you're existing customer rate increases makes a more meaningful impact as your street rates go up. Is your guidance fully baking in these couple of other positive elements of higher rates?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

Yes. I think that we have baked all of that in. Obviously as street rates go up it enables us to raise existing customers more and we've included that as we've given our guidance.

The one point of note here in our guidance, clearly our properties have done better than we originally estimated. But our acquisitions have done probably -- they've been slower and later in the year than we estimated . So part of that benefit of the properties doing better has been offset by slower acquisitions or acquisitions that took place later in the year.

Ki Bin Kim - *SunTrust Robinson Humphrey - Analyst*

Okay. And last question for me. What is the -- if I look at -- if I think about self storage, the one part that hasn't got a lot of attention is maybe the downtime it takes when you have a customer leave and the days it takes for you to lease it back up. Even if there is demand, there's always going to be a structural delay. What does that look like for, maybe, your 10 by 10 category, which is probably the hottest segment? How many days does it stay in the inventory before you can lease it out, even if there is demand? And have you looked at ways to cutting that down further?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

It all depends on the size of the facility, the square footage per capita, the number of competitors with comparable product to offer. There are a whole host of issues, Ki Bin, and we have not measured it. All I can tell you is usually the unit is swept out, the light bulb is changed, and it's put back into the system ready to rent. And so it's just a function of -- what's the seasonality? What was the customer searching for on an internet search? What solution did we serve up at what price point and promotion?

So this is one where we think that being ready to rent the unit as quickly as possible has been an operational focus. We don't want it offline. But when you figure that 6% or 7% of the total inventory of a storage facility turns over every month -- so if you have 600 units in a facility of say, 70,000 square feet and 6% or 7% of that turns over in a month, that's somewhere between 36 and 42 rentals divided into 42 -- into 20 or 21 business days. So you might end up with 1.75 or 2.0 rentals per day. And then what -- 5 by 5, 5 by 10, 10 by 10, 10 by 15, 10 by 20, 10 by 30, indoor, outdoor, upstairs, downstairs, climate-controlled, non-climate-controlled -- that's a really tough question to answer, Ki Bin. I'd like to give you an answer, but I don't have one.

Ki Bin Kim - *SunTrust Robinson Humphrey - Analyst*

(Laughter) Lot of (inaudible) there. All right. And, okay, that's it for me.

Operator

Michael; RBC Capital.

Michael Salinsky - *RBC Capital Markets - Analyst*

Want to talk about street rates. Any change you're noticing in duration? Or is there any change to lease structure maybe where you're trying to lengthen lease duration a bit?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

No, we're not changing our lease at all. But there is -- the average length of stay is slightly longer than it was five years ago. But no significant change.

Michael Salinsky - *RBC Capital Markets - Analyst*

Okay. And then the second question -- I know you touched about no supply on a broad base across the US. But are you seeing any markets where you're seeing supply ramp up in particular?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Yes, New York City. Texas is another one we're seeing a lot of. Chicago.

Michael Salinsky - *RBC Capital Markets - Analyst*

Any thoughts to potentially recycling maybe a bit ahead of that?

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

We're always kind of looking at our portfolio. And we're not necessarily looking to sell a significant number, but we would selectively look at selling a few properties. So it's always on the table.

Michael Salinsky - *RBC Capital Markets - Analyst*

Thank you.

Operator

Todd; KeyBanc Capital Markets.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

You talked about new supply being muted in part because the developers realize they cannot lease up the facilities once they're developed. You also talked about cap rate compression you're seeing in the competitive environment on the acquisitions side for operating property. So on the acquisition side, how deep is the buyer pool of investors that have the necessary sophisticated systems and the operating expertise, and an appropriate cost of capital? Who are the buyers that are entering the mix here?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Todd, it's Spencer. Buyers are coming from every walk of life. And one of the things that has amazed me recently is buyers with a less sophisticated platform thinking they can extricate the same performance. And just because somebody has money doesn't necessarily mean that they're going to achieve the same result out of a less sophisticated platform. It's possible, but there's a big question mark in my mind.

So I would tell you there are a lot of buyers, trade buyers, nontrade buyers, and everything in between. And for us, we just need to make sure that when we buy an asset at Extra Space, it's accretive, it fits our footprint, and operationally it puts us in the best possible position for keeping our product relevant in the market -- hence, some of our efforts to refresh and renew our assets, whether they be 10, 20, or 30 years of age. We want to make sure we've got something that, as new developments come on or as others come into the space, that what we have is compelling for the customer to look at Extra Space as the first solution.

Scott Stubbs - *Extra Space Storage Inc. - EVP & CFO*

And, Todd, the other thing I would add is you're seeing obviously the REITs looking to buy things. You're looking at funds looking to buy things. Some of those funds are having their assets managed by us or by other REITS. You're also seeing private REIT money chasing it. So it's a pretty diverse crowd.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Well, that's a good transition, I guess. My next question was I saw the third-party management you were up about a dozen contracts. Are you seeing -- are you getting more inbound calls from these investors? Do you think that we'll see growth accelerate in that line of business for you?

Spencer Kirk - *Extra Space Storage Inc. - CEO*

Yes, there are a lot of inbound calls. What's interesting as we've looked at this, Todd, it seems to go in waves. Last year we had 91 that we added into the system. We're not running quite at that pace, but all it takes is just one institutional buyer, somebody out there saying -- look, I'm a financial buyer. I don't want to operate these. And you could be back at last year's pace.

So for us there's still a lot of interest in the third-party management. It continues to be a major strategic thrust for us, because strategically we ultimately want to end up owning a high percentage of those that we manage -- not necessarily every one, but a high percentage.

And we're going to continue to promote and sell the benefits of being part of a larger platform. It'll appeal to some folks. It won't appeal to others. But no, it's still very healthy and growing and the pipeline of folks that we have been talking to is quite robust right now.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay. Thank you.

Operator

We have no further questions. I would now turn the call back over to Management for closing remarks. Please proceed.

Spencer Kirk - *Extra Space Storage Inc. - CEO*

It's Spencer. Thank you very much everyone for your interest in Extra Space today. We'll look forward to the Q3 earnings call in 90 days. Thank you.

Operator

This concludes today's conference. You may now disconnect. Have a great day.