Self-Storage In The Land Of Wonder

Industry Financing In The Australia Marketplace

By Sam Kennard

The self-storage industry in Australia has grown to be in reach of most of Australia's population.

The paradox of Australian demographics is that despite the country's enormous land area (7,692,024 square kilometres) and a modest population of 23.5 million people, Australia is actually one of the most urbanized populations in the world. Eighty-nine percent of Australia's population live in urban areas and it is ranked 17th on the ladder. It is only beaten in urbanization by city or island states such as Singapore, Bermuda, Hong Kong, and Cayman Islands.

It is little wonder then that self-storage has emerged and prospered so well in Australia. Globally, the self-storage idea owes its origins to entrepreneurs in the U.S. Canada quickly followed with Australia being the third to embrace the concept.

In Australia, self-storage began in 1973 when Nevile Kennard (my father) developed the first spaces in the Sydney suburb of Moorebank. Fast-forward 40 years and Australia boasts over 1,000 storage centers, with several major operators and numerous significant second-tier operators.

The major operators and investors can be proud of their sophistication and investment skills, and they compare well with global peers.

Australia has only two REIT's with self-storage assets and only one purely self-storage REIT. One REIT, Abacus Property Group, has the second largest self-storage asset investment portfolio with 49 properties valued at $395 million.

Australia's first self-storage REIT was only born in December 2013. National Storage began with assets valued at $278 million, some of which are leased, some wholly-owned, and some in a joint venture with Chicago-based Heitman LLC. Since listing, National and related entities have acquired nine new storage centers.

The largest owner of self-storage assets in Australia is Kennards Self Storage, owned and operated by my family. Kennards is a privately-owned family business with 82 storage centers currently trading, with a total value exceeding $900 million. The company wholly-owns 66 of these.

Globally, the self-storage idea owes its origins to entrepreneurs in the U.S. Canada quickly followed with Australia being the third to embrace the concept.

Australian Self-Storage Finance Climate

In the wake of the GST, foreign Banks left Australia and non-traditional lenders almost disappeared. Self-storage funding was left with four domestic banks, and until 2012, only three had an appreciation and an appetite for self-storage finance.

In 2012, ANZ joined NAB, Westpac, and Commonwealth Bank to participate in financing the self-storage sector. The additional competition was a pleasing development for self-storage owners but it remains a small field for lending competition.

Owner	Kennards	Abacus	National Storage
Ownership Structure	Private Company	ASX listed REIT (Diversified Real Estate 30 percent Self-Storage)	ASX listed REIT (100 percent Self-Storage)
Number of Self-Storage Centres	82	49	65
Value	$900m+	$395m	$278m

Going-Concern Funding Pictures

The Banks have illustrated they have a much stronger appetite to lend to proven mature self-storage centres than new development.

The banks will consider the cash flow, asset quality value, and borrower track record in their assessment of a loan. Loans are typically limited to 50-55 percent of the asset value, with a covenant limit of 60 percent.

Interest cover ratio (interest as a proportion of EBITDA) is often the more meaningful borrowing constraint. The I.C.R. often imposed by banks is two times or two-and-a-half times (i.e., annual EBITDA must not be less than two-and-a-half times annual interest expense).

In respect of loan security, going-concern lending will typically be non-recourse to the borrower. The asset is the only security the bank has recourse against. Loan margins are refunded to the Bank Swap Rate (BBSY or BBSW). Margins are in addition to the Swap Rate reset monthly, if on a floating interest rate.

In respect of loan security, going-concern lending will typically be non-recourse to the borrower.

New Development Lending

Australian banks have proven much more cautious about funding new self-storage development in the last few years. The banks wear some scars from losses of misguided development and lending provided pre-GFC. They are very concerned about a proponent's track record and backing.

Loan to value ratio does not exceed 50 percent, so there is significant equity required.

ICR has provided a step-up structure to enable rent-up without immediately defaulting, so hurdles must be met at one-, two-, and three-year milestones. In addition, banks will require additional security often in the form of personal guarantees.

Margins over the Bank Swap Rate are typically 220BPS to 300BPS for new project lending. It is clear the banks have tightened their new project lending requirements in a wise attempt to avoid the errors of some pre-GFC self-storage lending.

Margins will depend on asset quality, ICR and borrower capacity, and reputation. Margins range from 150BPS to 250BPS.

Sam Kennard is Managing Director of Kennards Self Storage. Kennards began in 1973 and has 80 locations across Australia and New Zealand, with over 51 hectares of space available. The company remains a private, family-owned and operated business.