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Life Storage, Inc. (LSI)

Q4 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the Life Storage Fourth Quarter and Full Year 2018 Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference call is being recorded.

It is now my pleasure to introduce your host, Mr. David Dodman, Vice President of Investor Relations. Thank you, sir. You may begin.

David Dodman

Vice President, Investor Relations and Strategic Planning, Life Storage, Inc.

Good morning, and welcome to our fourth quarter 2018 earnings conference call. Leading today's discussion will be Joe Saffire incoming Chief Executive Officer of Life Storage effective later this week; and Andy Gregoire, Chief Financial Officer.

As a reminder, the following discussion and answers to your questions contain forward-looking statements. Our actual results may differ from those projected due to risks and uncertainties with the company's business. Additional information regarding these factors can be found in the company's SEC filings. A copy of our press release and quarterly supplement may be found on the Investor Relations page at lifestorage.com.

As a reminder, during today's question-and-answer session, we ask that you please limit yourself to two questions to allow time for everyone who wishes to participate. Please re-queue with any follow-up questions thereafter.

At this time, I'll turn the call over to Joe.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

Thanks, Dave, and welcome, everyone to our fourth quarter and year end 2018 conference call.

Before we delve into our results, I want to take a moment and recognize Dave Rogers as one of our four founders and for his 35 years of service and commitment to Life Storage. Under Dave, the company changed dramatically. We broadened our scale meaningfully; we diversified the geography of our platform significantly; we added third-party manager capabilities; and we embarked on a number of industry-leading technology initiatives that will put us well ahead of our competitors over time. Dave has been a value leader as CEO and as a pillar in the industry and we are lucky to have him remain on the board, but we can continue to benefit from his perspective.

As I complete my transition this week to CEO, I am thrilled to be working with a driven and passionate team. Thank you, Dave, for your hand in building the platform and the team. We promise to make you proud as we take Life Storage to the next level.

I'm now pleased to turn to our results. We reported fourth quarter and full-year 2018 results late yesterday that were very strong. We achieved core FFO per share of \$1.38 and \$5.51, respectively, for the fourth quarter and the full year. Andy will speak to you about the detail shortly, but both results were at the high end of the guidance range we provided on our third quarter conference call.

On to asset management, we are executing on the portfolio optimization strategy we have discussed on previous calls in order to increase exposure to markets with more attractive demographics and newer properties with higher revenue and better growth prospects. In the fourth quarter, we sold 12 mature assets to a joint venture for approximately \$91 million, contributing \$9 million of those proceeds back into the entity in exchange for a 20% equity stake and reinvested the balance into newer properties with improved growth prospects. We continue to manage these JV properties.

The revamping of our acquisitions team has started to pay dividends. During the fourth quarter, we added six wholly owned properties for \$58 million. Those properties are located in New York, Sacramento, Orlando, St. Louis, and Atlanta. Including the two stores that we acquired in the Boston and Sacramento markets in the third quarter for almost \$20 million, we have successfully redeployed the proceeds of the 12-store asset sale.

With respect to these asset exchanges, we have traded stores that were on average 27 years old for stores that are on average seven years old. We increased the rent per square foot from less than \$12 to nearly \$17. And we moved out of fully mature stores with plus 90% occupancy and moved into ones that are roughly 65% occupied.

We have also improved the revenue per store opportunity from 760,000 per store to over 1 million per store, which is nearly a 50% improvement. We expect to continue to capitalize on favorable market conditions in 2019 and project sales of up to another \$225 million of mature assets with the expectation that those proceeds will be reinvested in properties with improved growth prospects.

On that note, we have continued to identify and act upon opportunities to upgrade our portfolio since the New Year began. In January, we acquired the remaining 60% ownership in a store in Queens, New York from one of our JV partners and we are under contract on 17 additional stores totaling almost \$187 million in various Mid-Atlantic, Midwest and Southeastern markets.

The impact of these opportunities are consistent with the characteristics I described for the transactions we closed in the fourth quarter; newer, higher rates, lower occupancy and revenue per store greater than \$1 million. We hope to close these additional stores by the end of the third quarter. However, these opportunities remain subject to further due diligence and closing conditions. And therefore, no assurance can be given that they will be purchased according to the currently contemplated terms.

I should add that the majority of the assets that we have closed or are under contract were secured off market thus avoiding competitive auction-like bidding. This is the complement to our ongoing efforts to further develop our relationships throughout the industry. Our asset rotation strategy to systematically prune lower assets while investing in higher growth stores will result in minor FFO dilution in 2019. And Andy will provide details shortly. However, we believe these transactions will better position our portfolio for future growth and improve our overall portfolio cap rate.

Now on to operations. With regard to same store performance, we continue to drive positive trends. We generated favorable revenue growth in 27 of our 33 major markets with the strongest trends in Vegas, New York, New Jersey, New England, Buffalo, L.A., Sacramento, and Cleveland. Our view of supply remains generally unchanged and our watch markets are the same. We continue to see pressure in Chicago, Miami and our Texas markets of Dallas, Houston, and Austin. We are not as exposed to some of the hotspots in the country such as Portland, Nashville, and Denver.

With regard to our third-party platform, we wrapped up a record year with the successful onboarding of 42 high-quality stabilized stores in the Southeast on November 1. All in for 2018, we added 69 stores to our platform and have an additional 22 under contract. As of the year-end 2018, almost 50% of our managed portfolio now includes properties where Life Storage holds no ownership interest. That's an almost 100% increase for two consecutive years. And subsequent to year-end, we added four managed properties in the Greater Toronto area, one of the largest North American markets.

We are excited about the traction we have generated in our third-party management business and we will continue to drive additional business going forward. Our pipeline remains strong. The growth of our third-party platform has also provided us with a robust pipeline of off-market purchase opportunities. In fact, of the acquisitions mentioned above, four were from stores we were managing.

On to Rent Now, we continue to rollout Rent Now, our fully digital rental platform, for customers who prefer to self-serve and skip the counter. As of today, Rent Now is available in 530 stores, and we remain on track to complete a rollout across our owned and managed portfolios in the second quarter. We remain excited about the prospects of this industry-leading new technology platform. We believe we are the leader in providing multiple digital ways to sign a lease. Our customers now have the option to self-serve from the comfort of their homes or anywhere for that matter. We believe this to be a game changer in our industry.

And finally, we continue to invest in Warehouse Anywhere, our differentiated commercial strategy for B2B and B2C customers. Our pipeline continues to grow with the enhanced product portfolio we rolled out in the fourth quarter. Our digital marketing efforts are paying off with the number of views to our warehouseanywhere.com

website expected to grow from just 4,000 views in 2017 to an expected 200,000 views in 2019. More hits and views means more leads. Our Warehouse Anywhere brand continues to gain traction.

We continue to add business development resources to support this business growth. In fact, we are probably the only storage company to recruit and hire executives from traditional logistics businesses such as FedEx. We are a firm believer in the role that traditional storage can play with a last mile delivery component of e-commerce. We are excited that the February issue of the Self Storage Association's Globe Magazine highlighted our Warehouse Anywhere offering. In summary, I'm excited for 2019 though supply concerns remain, we have a great team and strategy in place to continue driving shareholder value.

Andy, over to you.

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

Thanks, Joe. As Joe mentioned, last night we reported adjusted funds from operations of \$1.38 per share, a 3% increase compared to adjusted FFO of \$1.34 per share for the same period in 2017. These results were near the high end of our forecast, driven by better-than-expected same store performance, as well as continued growth at our lease up facilities.

Our same store performance is highlighted by NOI growth of 4.1%, achieved by both improved revenue growth and controlled expenses. Specifically, same store revenue rose 3% over the same period last year, driven by improvement in rental rates. Same store realized rates per square foot increased 3.8% over the fourth quarter of 2017. The 4.1% NOI growth exceeded the high end of our guidance range, which was 3.25%, while the 3% revenue growth achieved the high end of our guidance range.

Fourth quarter same store expenses outside of property taxes were well-controlled, decreasing 1.4%. Our teams continued to identify efficiencies at the stores and this is showing up on the expense side. As we anticipated, the only significant expense pressure was from property taxes, which increased 5.4% in the fourth quarter. That being said, the increase was below expectations as we had significant property tax revaluation wins in Texas.

In addition to the strong performance of our same store portfolio, we continue to see consistent growth trends at the properties that we purchased at certificate of occupancy or very early in the lease-up stage. With quarterly occupancies of 81.4%, these lease-up stores still have room to grow.

We added four lease-up properties in late 2018. And we expect to add additional lease-up properties to this group in 2019. Our overall fourth quarter revenue increase also reflected a 9.6% increase in other operating income, driven by a 24.3% increase in third-party management fees. Our balance sheet remains very solid and we continue to have significant flexibility to capitalize on attractive investment opportunities when they meet our return requirements.

At quarter end, we had cash on hand of \$13.6 million and \$408 million available on our line of credit. In the fourth quarter, we closed on the refinancing of our bank credit facility, which included extending the maturity on the revolver until March of 2023, and reducing the credit spreads by 15 basis points at our current investment grade rating.

Our weighted average debt maturity is 7.1 years and 89% of our total debt is fixed rate. Our debt service coverage ratio was a healthy 4.6 times and our net debt to recurring EBITDA ratio improved to 5.3 times.

Regarding guidance, although we continued to achieve positive trends in our same store pool, we remain cautious due to the impact of new supply. Therefore, we currently anticipate same store revenue growth of 1.5% to 2.5% for the 2019 fiscal year.

Excluding property taxes, we expect operating cost to grow 2% to 3% for the full year, with pressure from payroll and Internet marketing spend. Property taxes are expected to grow 5.5% to 6.5% in 2019. The cumulative effect of these assumptions results in expected same store NOI growth of 1% to 2% for the year. Consistent with our past practice, we are not including in our same store group any stores achieved – or any stores acquired in the early stages of lease-up that were less than 80% occupied at market rates as of the beginning of the prior year.

As Joe explained in his opening remarks, we expect to continue to optimize our asset pool in 2019 by rotating out of mature lower revenue stores with limited growth opportunities into newer stores and markets with more attractive demographics and growth prospects. Specifically, in our projections, we have included \$225 million of acquisition activity for 2019 and \$225 million of dispositions.

Using proceeds generated from the sale of mature properties to acquire newer higher growth potential properties, we expect to incur between \$0.10 and \$0.12 dilution of FFO per share in 2019. However, this asset rotation should provide significant net asset value and FFO growth potential in subsequent years. Including the noted dilution in 2019 from our portfolio optimization strategy, we forecast adjusted FFO per share of \$1.27 to \$1.31 for the first quarter and between \$5.53 and \$5.63 for the full year 2019.

I will now turn the call over to Dave Rogers for a few comments.

David L. Rogers

Chief Executive Officer & Director, Life Storage, Inc.

Thank you, Andy. As Joe noted in his kind remarks, I've been with Life Storage for 35 years, which for its first 10 was a privately held company, and then since 1995 a publicly traded one. This is the 94th quarterly earnings call, I have helped to host. I've been to a combined 47 Nareit REITweeks or Nareit Forums, 21 Citi Conferences and dozens of NDRs and analyst meetings.

Upon completion of our IPO, we had an enterprise value of \$136 million. Today, that enterprise value is well over \$6 billion, more than 45 times original size. And yet, there's a lot of growing still to do. Self-storage industry has millions of potential customers yet to reach. Life Storage's platforms, its people, its innovativeness, our brand, they're all top-shelf. Our leadership team is outstanding, from our recently refreshed and expanded Board of Directors to an engaged and experienced C-suite, including Eddie Killeen, our Chief Operating Officer; Andy here and Joe, so they are extremely competent lieutenants in the property management, marketing, sales, training, finance, HR, IT, construction, legal, and data service departments.

We've enjoyed tremendous support from the investment community, including many of you on the call today and we thank you for the confidence you placed in us over these past 24 years. I've enjoyed the many relationships and friendships garnered over that time, and I thank you for those as well. I'm excited to remain a part of this ongoing story as a member of the Board of Directors. The board, my co-founders and I share a great optimism in the prospects for our industry and have the utmost confidence in the Life Storage's ability to deliver strong growth and outstanding results on behalf of all of our shareholders.

And now, operator, would you please open the line to questions for Joe and Andy to answer? Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Shirley Wu with Bank of America Merrill Lynch. Please proceed with your question.

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

Good morning, guys. Best of luck, Dave.

David L. Rogers

Chief Executive Officer & Director, Life Storage, Inc.

A

Thank you.

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

So for my first question, I guess, I just want to talk about your transaction. So given you have so much of visibility into the acquisitions from 2019, could you talk a little about the dispositions you have planned to fund those acquisitions, maybe the markets as well as the timing?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Sorry, Shirley. Was that the acquisitions we have in queue that have not yet closed?

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

Exactly, yeah.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah. As I mentioned in my remarks, they're very similar to the characteristics of what we purchased in the fourth quarter. These are all newer stores, bigger stores. There are markets that we are already present and there are markets with better demographics than the properties that we're looking to dispo. We're excited about them. We think that this is going to continue the transformation of our portfolio.

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

What about the dispositions that you have planned to fund those acquisitions?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

The dispositions, specifically, they're in markets that we've identified previously. We may have talked about them in the past. But they're in markets that are less quality demographics that we look into when we're making acquisitions, they're smaller stores, they're lower rates per square foot, they are markets that unlikely we're looking to buy more assets. So again, these are properties that they're great for cash flow. There's a lot of interest

in them. But for us, they've been holding us back over the last several years in terms of potential growth and prospects going forward.

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

Got it. Could you talk about your street rates in 4Q and even year-to-date as well as your net effective rents?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Hi, Shirley, it's Andy. Street rates in 4Q were up about 1.9%, net effective slightly negative – we do have increased concessions year-over-year. Really, it's a tale of markets. We see Houston with street rates down significantly as we have a tough comp with the hurricane-driven demand we had in late 2017. So that was a tough comp in 4Q and it will continue in Q1, even some into Q2. But and you look on the other side where you have Vegas, where you have net effective rents up 17%, and Buffalo and Upstate up 10%.

So it is a tale of markets. Our biggest market is a tough comp right now. January and February – January was very similar on the street rates side. Concessions were a little easier of a comp compared to last year. So the net effective was still negative, but less negative than it was in the fourth quarter.

Shirley Wu

Analyst, Bank of America Merrill Lynch

Q

Great. Thanks for the color.

Operator: Thank you. Our next question comes from the line of Smedes Rose with Citi. Please proceed with your question.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Q

Hi. Thanks. I was wondering again on the strategy of selling mature properties and buying newer properties. Could you just talk a little bit about the spreads you expect to sell at versus buy? And I think you mentioned some of these are still in lease-up. So what's your confidence that you can get to stabilization within a reasonable timeframe given that – it seems like pricing across the industry is pretty tough right now and will you drive occupancy-led strategy and then look to raise prices later, maybe just some detail around that?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah. Hi, Smedes. Thanks for the question. On the dispos, the conditions have never been better for selling at this time. The price that assets are going for in secondary markets has never been closer to primary market. So it's been a great time. And there's lot of interest for us to look to sell. And what we're buying are really what I mentioned earlier Class A properties in markets we like and in markets we want a bigger presence.

We've been pleasantly surprised. Initially, when we started talking about this strategy about a year ago, we thought the spread between what we're selling and what we're buying would be wider. And so far, we're quite pleased with the first bunch that we sold around a mid-5 cap. And the properties we're buying, again, they're all in various stages of lease-up, but these aren't CO deals. They're already well on their way. We have a better idea of where these properties are pricing now in terms of street rates. But the upside is there. And we have a track

record of really doing well with lease-up property. Most of our lease-up properties are getting to the mature stage. So this is really an opportunity for us to revamp those growth opportunities without taking a ton of risk.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Q

And the ones that you're selling, they'll leave the Life Storage brand, I guess?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

No. So we are going – the ones we sold in the fourth quarter, we kept an equity stake, they will remain in Life Storage. We'll have third party management fees on those. And the intention is to do the same with the next batch.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Q

Okay. And then, can I just ask you on your first quarter guidance? It was below consensus forecasting. Do you attribute that primarily to just maybe more difficult comp than what people had been anticipating? Or is there something going on in the first quarter?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Hi, Smedes. There's a few things going on, right? We still do have that difficult comp in Houston, our largest market. So that is – and part of the first quarter is the dilution from what we did in 4Q, the first dispositions at \$91 million was in December 15 or December 16, so it was the end of December. And what we bought is – it's a 200-basis-point spread between what we are buying and what we sold and the reason there is that 200 basis points is because the occupancy is 65% on what we bought versus the 90% to – 90% of what we sell. So there's some dilution on that \$91 million that's sitting in the first quarter as well.

Smedes Rose

Analyst, Citigroup Global Markets, Inc.

Q

Thank you.

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

You're welcome.

Operator: Thank you. Our next question comes from the line of Todd Thomas with KeyBanc Capital Markets. Please proceed with your question.

Todd M. Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

Hi. Thanks. Good morning. First, Dave, just want to say good luck in retirement and in your future endeavors.

David L. Rogers

Chief Executive Officer & Director, Life Storage, Inc.

A

Thank you, Todd.

Todd M. Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

So I just wanted to follow up again here on the capital recycling activity. So it seems like you're further along on the acquisitions and you've identified the disposition pool. But what's the timeframe to get those sold? What's the timing that's embedded in guidance? And how far along are you – just so we can understand the risk here of sort of buying first and then selling since you'll be increasing leverage a little bit here in the near term it seems like.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah. I think the timing is working out. We probably couldn't have planned it better, Todd. We did a formal process for the second batch of properties we're selling. And we expect – that is moving along very well. And we expect that hopefully if things go well enough and we come to terms, it would close around July – July 1. And the big chunk of our acquisitions that we have under contract would also close around that same time. So really, it couldn't be more ideal.

Todd M. Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. And then, just curious in terms of the projects, the contracts that you're taking over in Canada, you mentioned in the press release about the population, 7 million within the Greater Toronto Area, which felt – or seemed sort of unprompted, maybe a justification to some extent of taking on those four management contracts. Is there more being considered in Canada either for management or for acquisitions by the company?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah. In Canada, as you know, we can see Toronto from Buffalo on a nice day. And it's a sprawling market. It's one of the fastest growing in terms of population. And we've always – we have looked in the past. And what's changed is we have a very strong partner up there that we've been working with in the U.S. for many, many years, one of our longest third-party clients. And it was just the right time for us to go up there and support their growth.

It's a bit of walk before you run. I think there are future opportunities for us down the road. At this time, we're getting comfortable in a foreign country where we're learning how to run, we're learning how to hire, we're understanding the laws. And we're going to do most of our activity with this partner in the foreseeable future. But I would expect to things go well that we would be a bigger player in Canada down the road. It's a great market. Our platforms are well ahead of what they are now. And I think we could make a difference. And the demographics are just something you don't see in the U.S. anymore.

Todd M. Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

And just following up on that then, can you just sort of describe the market in Canada relative to the U.S. a little bit in terms of competition and then the other sort of industry dynamics and how they might differ in Canada versus the U.S.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah In terms of supply, it's about half of what we see on average in the U.S. I think there are around 3 square feet per capita versus the average of 7 in the U.S. The competition, there's a lot of smaller mom and pops, but there's also one large publicly traded company that Storage Vault that we know. And they've been doing some good things up there, and Public is up there. And I believe a couple other U.S. private REITs are up there.

There's been a lot of development in Toronto. But again, the supply is low. The rates are very good. But again, we think that the platforms in general are behind what we see in the U.S. A lot of the competitions don't publicize their rates online. There's nothing on the web. It's hard to scrape the web. So there's an immense opportunity to go in there with our platform such as Rent Now, our revenue management systems and so forth, and really improve the performance of our partner stores. And then, again, once we get to know how to run up there, which so far it's been fantastic, I can't thank our team for doing this pretty quickly and getting up there and running on January 2. But we like what we see. And we think it could be a great market for us going forward.

Todd M. Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. Thank you.

Operator: Thank you. Our next question comes from the line of Ki Bin Kim with SunTrust Robinson Humphrey. Please proceed with your question.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thanks. Good morning, and Dave, congrats and definitely going to miss you. Joe, can you talk about the incremental changes that you're contemplating for LSI and what we can expect where you would focus more on?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

I think what you've seen over the last year, 18 months and what really the company has been doing over the last few years, the biggest priority is to continue to recycle our assets. Again, we want to have larger stores in markets with better prospects. And we've talked a bunch about that today. We're going to continue to do that. I think we're always going to be looking to add talent to our team. We've got a great team in place, but you know the world is changing. We just hired our first Head of Data Science. And we'll be looking at ways we can improve our company from the talent perspective. We're doing things like Warehouse Anywhere and attracting businesses every day. So we're looking for different types of people that traditionally wouldn't join a traditional storage company such as the – people from FedEx and so forth.

So I see us looking at talent. And then, most importantly, we're going to continue to invest in technology. I think our platforms as we've demonstrated are innovative, best-in-class. We have a great team here and we're going to continue to invest in technology.

And then, the last thing I think which we pretty much started last year, when we brought our acquisitions team in-house, the importance of developing relationships in the industry. That's something that has gone over very well. And we're going to continue to do that. I think it's important. It helps us find opportunities for JVs, for acquisitions, and obviously, for third-party management. And we're going to continue to really develop these relationships.

People like to work with Life Storage, they like our team, they like our culture. And everything seems to be aligned for further growth going forward.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Okay. And you guys made a pretty big change to the existing customer rate increase program last year by allowing customers who get a rent increase letter to be above market. And I think the second incremental change was how much above market should we let these – should we let that rent increase letters go above? And I would have just thought, obviously, you saw nice positive impact to your same store revenue last year. But I thought you would have maybe carried forward into 2019. So maybe, can you talk about implicitly what is in your same store revenue guidance and the contribution from the ECRI program, and if there's a little bit more outsized growth embedded in 2019 guidance or not?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Hi, Ki Bin. Regarding the in-place strategy, we're going to remain aggressive as you saw – as we were in 2018. You just got to continually monitor that and tweak that, and we will. We would expect the contribution to be 1% to 2%. And it's not a perfect science doing that calculation, because when somebody moves out and how it affects, what happens with the specials on those spaces where somebody moves out, what it does to rates through the algorithm, it's not exact science. But 1% to 2% is what we would expect to get out of the in-place rent increases.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

So if I take that, does that mean implicitly what you're looking for street rates in 2019 as probably slightly negative – net effective?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

I would think we're going to start the year that way especially with where our biggest market is at - Houston, but again, that comp gets easier as we go through the year. I would think same thing with the occupancy, it will become an easier path as we go through the year, but we won't expect to see occupancy increases. So most of it will come from the in-place strategy.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Okay. Thank you.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Ki Bin, just with the new supply coming on, from 2017, 2018 those are still on lease-up mode, and then we are seeing a bunch of deliveries expected for 2019. Fortunately, we believe 2019 is somewhat the peak of new deliveries; in construction, we're seeing a bit of a slowdown in what we monitor in terms of planning. But there is an absorption phase. So we feel that's going to pressure street rates.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

And just a follow-up on that. When you said 2019 would peak in new deliveries, is that for the industry as a whole, or for what impacts your portfolio?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Well, we monitor what we – what's in our three-mile, five-miles store radius. So we don't necessarily follow as closely as some of the other markets we're in such as Portland where it's quite hot. But from our stores and from what's affecting our stores, we believe 2019 is peaking.

Ki Bin Kim

Analyst, SunTrust Robinson Humphrey, Inc.

Q

Okay. Thank you.

Operator: Thank you. Our next question comes from the line of Jeremy Metz with BMO Capital Markets. Please proceed with your question.

James Shin

Analyst, BMO Capital Markets (United States)

Q

Hey, good morning, guys. This is James Shin on for Jeremy. I just had a question.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah.

James Shin

Analyst, BMO Capital Markets (United States)

Q

It looks like expansions was a roughly 50-basis-point benefit to rental income in 2018. Do you expect a similar benefit in 2019? And then, based on your guidance for a higher spend this year, \$40 million to \$50 million, should we expect that then to widen in 2020?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Hi, James. The contribution to the same store is very difficult to calculate. The back of the envelope you can get to that 50 basis points. But we're knocking down buildings when we're putting new buildings in place. So as we constantly do that, the impact year-over-year years has been pretty constant. So there's not really that impact until we stop that process. We expect the spend to be very similar. We had some delays in getting some things actually opened in the fourth quarter and some of those will hit in Q1. I think we only completed \$20-or-some-odd-million during the year that we opened up expansions. So openings will probably have more in 2019, but the total spend on them will be very consistent. So any impact should be very consistent year-over-year.

James Shin

Analyst, BMO Capital Markets (United States)

Q

Got it. And then, for disposition, of the \$225 million, how much is on the market right now? And then, do you look to contribute some of those to a similar JV that was done in 4Q.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

So that full 225 is what we're – we have on market right now. And we expect to do a similar JV, not necessarily with the same party, but a similar structure. That's our intention.

James Shin

Analyst, BMO Capital Markets (United States)

Q

Got it. And then, I guess, if they're going to be put into a JV, does the \$0.10 to \$0.12 dilution include management fees on the JV?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yes it does.

James Shin

Analyst, BMO Capital Markets (United States)

Q

It does?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Yeah.

James Shin

Analyst, BMO Capital Markets (United States)

Q

Okay. All right. Thanks, guys.

Operator: Thank you. Our next question comes from the line of Steve Sakwa with Evercore ISI. Please proceed with your question.

Steve Sakwa

Analyst, Evercore Group LLC

Q

Thanks. I guess, two questions. First on this development, Joe, you mentioned that you are starting to see supply abate a bit. And I'm just curious, if you guys look to work with people or look at development yields, where would you guess that they are in your core markets today? And I guess that's the first question.

The second one is really on the corporate business and just what you're seeing, and it sounds like you're pretty excited about that, but I'm not sure how much of that you baked into that top line revenue growth for 2019?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Again, I'll start with the second question, Steve. The B2B business as you know is something we focused on for a number of years. We spent several years building out the 10,000 store network that we have. So we believe that's quite difficult for anyone to copy. And now we're really building out the actual product suite and delivery of that and attracting hits on the web and gaining that sort of recognition.

We have some great clients who are advancing through our portfolio suite and expanding their reach. But again, this is an early-stage business. It's growing. I think all in, it's about \$11 million when you include the rent and the fees. And conservatively, we think we can grow this at least 30% going forward.

In terms of the development yields, yes, we are working with a number of developers. We don't develop ourselves. We've talked about doing some early investments in some developments. But again I think the expectations of the yield is still around 7% in the markets we're looking to participate in.

Steve Sakwa

Analyst, Evercore Group LLC

Q

Okay. Thanks.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

A

Okay.

Operator: Thank you. Our next question comes from the line of Eric Frankel with Green Street Advisors. Please proceed with your question.

Eric J. Frankel

Analyst, Green Street Advisors LLC

Q

Thank you. Dave, best of luck in your new journey; congratulations on a long fulfilled career.

David L. Rogers

Chief Executive Officer & Director, Life Storage, Inc.

A

Thank you, Eric.

Eric J. Frankel

Analyst, Green Street Advisors LLC

Q

One question. Can you – sure. Can you just go through the dilution calculation that \$0.10 to \$0.12? That seems a little bit high just relative to the trades and what you're describing in terms of the relatively narrow cap rates spread. So maybe you can just talk through that. Thank you.

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Sure, Eric. Two pieces to that dilution. First is the \$91 million that we put to work. So we sold at the end of 2018, put that to work. The dilution on that – at least the upfront dilution – obviously, the yields will be great going forward. But the upfront will be 250 basis points on a \$91 million for the whole year. So in the guidance is that dilution for the whole year. The \$225 million is the same thing. There's about a 250-basis-point spread, the assets we're buying are 50% occupied or so. So if it all closes in mid-year, and so we took the calculation on a \$225 million for half a year, 250 basis points of dilution on that.

Eric J. Frankel

Analyst, Green Street Advisors LLC

Q

Okay. Thanks. And then, just a quick follow-up on the dispositions. I assuming you probably keep it a similar 20% stake in what you're selling, is that correct? Would it be lower or higher?

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

By around 20% is our goal.

A

Eric J. Frankel

Analyst, Green Street Advisors LLC

Okay. Great. Thank you.

Q

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

Thank you.

A

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Jonathan Hughes with Raymond James. Please proceed with your question.

Jonathan Hughes

Analyst, Raymond James & Associates, Inc.

Hey, good morning. Just curious what the impact of the same store definitional change was directionally on 2019 revenue in NOI growth rates. I assume positive given some more less stabilized assets are added sooner, but I know it can vary for same store NOI given taxes and other factors on the expense line.

Q

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

Hi, Jonathan. We really didn't change the definition – the stores that were in our C of O group. And there's 14 of them that will be added to the same store in 2019. They were stable at the end of 2017 at stable rates. So at the end of 2017, they were stable. We did not add them in 2018. So we add them in 2019. So they will be added in 2019. And there's 14 of those – you can see them on the schedule and the supplement all the ones that were greater than – most of them were greater than 90%, but the ones greater than 80% as of the beginning of – or at the end of 2017. So they will be added.

A

And then, there were three other stores that suffered damage back in 2016 – 2016, and they were stable at the end of 2017. So they will be added as well. So small change in the pool, we would not expect. And you'll see it because we – as we always do, we show the different pools each quarter. I would not expect it would be 10 basis points or less difference between the new pool and the old pool.

Jonathan Hughes

Analyst, Raymond James & Associates, Inc.

Okay. Yeah. I just had gotten a little confused, because last quarter it said those would be added after the second year of achieving 80% occupancy in this quarter, it said they'd be added after the first year, so...

Q

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

Yeah. We'll correct that – we'll clarify that going forward. But that's the case. It's really the same definition.

A

Jonathan Hughes

Analyst, Raymond James & Associates, Inc.

Q

Okay. All right. That's helpful. And then, I guess what's the contribution from the new same store assets and revenue and NOI growth guidance, and how should that trend throughout the year?

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

The addition of those...

Jonathan Hughes

Analyst, Raymond James & Associates, Inc.

Q

I know it's expected to grow by 2.5% or so, but any numbers around that would be helpful.

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

A

Yeah. Like I said, the change in the pool won't affect the stores much. But we would expect with the new supply, first of all, Q1 will have a tough comp with Houston after that new supply, we would expect to continue to put pressure on rates and the revenue line.

Jonathan Hughes

Analyst, Raymond James & Associates, Inc.

Q

Okay. I'll follow up. I appreciate the time. And Dave, congrats again on your retirement.

David L. Rogers

Chief Executive Officer & Director, Life Storage, Inc.

A

Thanks, Jonathan.

Operator: Thank you. We have reached the end of our question-and-answer session. I would like to turn the call back over to Mr. Saffire for any closing remarks.

Joseph V. Saffire

Chief Investment Officer & Incoming Chief Executive Officer, Life Storage, Inc.

Okay. Well I want to thank you all for dialing in today and we look forward to seeing you all at the various shows this year.

Andrew J. Gregoire

Chief Financial Officer, Life Storage, Inc.

Have a good day.

Operator: Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.

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