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EXR - Q2 2012 Extra Space Storage Inc. Earnings Conference Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the second quarter, Extra Space Storage, Inc, earnings conference call. My name is Bree and I will be your operator for today. At this time, all participants are in listen-only mode. Later we will conduct a question-and-answer session.

(Operator Instructions)

As a reminder, this conference is being recorded for replay purposes. I would like to turn the conference over to your host for today, Mr. Clint Halverson, Vice President of Investor Relations. Please proceed.

Clint Halverson - *Extra Space Storage Inc - VP, IR*

Thank you, Bree. Welcome to Extra Space Storage's second quarter 2012 conference call. In addition to our press release we've furnished unaudited supplemental financial information on our website. 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, Tuesday, July 31, 2012. The Company assumes no obligation to revise or update any forward-looking statements because of changing market conditions, or other circumstances after the date of this conference call.

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

Spencer Kirk - *Extra Space Storage Inc - CEO*

Thanks, Clint. Hello, everyone, and thank you for joining us today.

With me are Karl Haas, our Chief Operating Officer, and Scott Stubbs, our Chief Financial Officer. It was another very good quarter for Extra Space. We achieved year-over-year FFO growth of 41%. Our properties and our systems are performing very well. During the quarter, we increased same-store revenues 6.7% and reduced expenses, which resulted in double-digit NOI growth of 10.2%. I give credit where credit is due, to our people. I think of our 2,400 employees who have worked hard and dedicated themselves to executing on the fundamentals of our Business.

Our internal and external growth efforts have been highly effective in acquiring quality, well located assets. We have acquired 51 properties so far in 2012, 36 of which are from Prudential, and we have an additional 9 properties under contract. We are disciplined in our acquisition approach and purchase assets when it makes financial sense for our shareholders. As the country's largest third-party management Company, with 519 assets under management, we continue to assert and demonstrate that this is a viable off-market acquisition pipeline.

Of the 51 assets acquired this year, 76% came from these existing relationships. Our Company is driven by an entrepreneurial culture of innovation and growth, and we push for continuous improvement in all areas of our business. The development and implementation of system wide innovations will continue to improve our performance. I would now like to turn the call over to Karl to talk about our operational success in more detail.

Karl Haas - *Extra Space Storage Inc - COO*

Thanks, Spence. As Spencer noted, we saw excellent revenue growth of 6.7% in the second quarter. There are a few primary factors that drove this top-line growth. First, the latest version of our revenue management software is working well. We are gaining a better understanding of the price elasticity of demand for storage at a property level. We are often asked about our rental volume for a given period.

Although the rental volume is significant, it is more important to maximize long-term revenue growth of those rentals, with the correct mix of incoming price, discount, and rate increases over time. Second, we continue to gain market share from our smaller competitors. By leveraging our size, resources, and sophisticated systems, we are driving traffic to our websites and properties. We are capturing more than our fair share of the rentals, while lowering our overall cost per acquisition.

And lastly, we are not seeing any new supply. As we mentioned last quarter, our same-store pull of 282 properties includes 19 sites that are over three years old, and are in the final stages of lease-up. As a result, during the second quarter we received almost a 0.8% of top line benefit from these assets. By stripping these 19 properties out of the same-store pull, our top line revenue growth would have been 5.9% versus the 6.7%.

Same-store year-over-year expenses were down slightly, primarily due to lower utility costs as a result of our investment in sustainability initiatives. We're also seeing lower credit card processing fees thanks to new regulations. While we continue to implement processes and invest in systems that create efficiencies, we don't expect our expense growth rate to continue at the levels it's been at Q1 and Q2. Expenses will return to more normal levels as we move through the year. With occupancy at historically high levels, discounts and promotions are down 11% for the quarter. When combined, all these factors bode well for the remainder of the year. And with that I would like to turn it over to Scott.

Scott Stubbs - *Extra Space Storage Inc - CFO*

Thanks, Karl. Yesterday we reported second quarter FFO of $0.38 per share including $0.01 of lease-up dilution. We exceeded the top end of our guidance by $0.03. $0.02 of this was due to better than expected property and tenant insurance results. The other $0.01 was the result of lower than anticipated interest expense, as we have been able to obtain loans at rates that are at all-time historical lows. During the quarter we sold 8 million shares of common stock for net proceeds of about $225 million. These proceeds have primarily been used to fund acquisitions.

We've seen good traction in the acquisitions market in 2012. During the second quarter, we closed on the acquisition of four properties for approximately $21.3 million. These properties are located in Florida and Maryland. Subsequent to the end of the quarter, we closed on the purchase of Prudential's interest in the PRISA III, joint venture, adding 36 properties to the REIT. As of today, the total number of wholly owned assets is 408, as compared to 304 joint venture properties. This demonstrates our strategy to grow the REIT in a meaningful way. In addition, subsequent to the end of the quarter we have closed on the acquisition of 9 other properties for approximately $71.8 million. These properties are located in California, Colorado, New Jersey, New York, and South Carolina.

In addition to these we have 9 additional properties under contract for approximately $83 million, located in Massachusetts, New Jersey, New York, Texas, Utah, and Virginia. We've updated our acquisition assumptions in our guidance to account for the increase in volume and acquisitions. We've revised our full-year 2012 FFO guidance to be between $1.47 and $1.53 per share, and expect to earn between $0.39 and $0.41 in the third quarter. Key assumptions relating to these estimates can be found in the press release. I will now turn the time back to Spencer for some closing comments.

Spencer Kirk - *Extra Space Storage Inc - CEO*

Thanks, Scott. Let me reiterate that Extra Space has one main theme in 2012, Focus on fundamentals, which simply put is, maximize every revenue opportunity and appropriately minimize every single expense. We're executing at a high level on both fronts. We exceeded our expectations in the second quarter and are pleased with the results. But I again caution that they should not be utilized as the basis for our long-term growth trend.

If you look back over the last several years, it is evident that we are now running on the high end of the growth spectrum. As a team, we can't take our eye off the ball, become complacent or become arrogant. We are keenly aware of the considerable competition that exists in the self-storage sector. With this attitude and approach, I feel confident that we will consistently find ways to increase shareholder value. With that, I would now like to the turn the time over to Clint to start the Q&A session.

Clint Halverson - *Extra Space Storage Inc - VP, IR*

Thank you, Spencer. In order to ensure we have adequate time to address everyone's question, I would ask that everyone keep your initial question succinct and if possible, limited to two. If time allows, we will address follow-on questions, once everyone has had an opportunity to ask their initial question. With that, we'll turn it over to Bree to start our Q&A session.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Swaroop Yalla, Morgan Stanley.

Swaroop Yalla - *Morgan Stanley - Analyst*

Spencer, can you talk a little bit about the source of the deal flow you're seeing? Who is the incremental seller in this market? Is it mom and pop operators or private guys liquidating their portfolios? Maybe on that note if you can discuss the cap rates which these acquisitions are based on?

Spencer Kirk - *Extra Space Storage Inc - CEO*

Let me first of all take the cap rate question. I would say the purchases of the assets we've talked about have ranged from about 6.5 to about 8. And that depends on the quality of the asset. In my mind, a quality score has three components. The physical condition of the asset, the market where that asset is located, and the location within the market. So we try to pay an appropriate cap rate, depending on that three-tiered or three-pronged quality assessment. We're getting buyers from across the board, Swaroop.

Obviously our, what I call quasi proprietary acquisition pipeline is not hurting us in any way, shape or form. 76% of our purchases so far this year have come because of those existing carefully nurtured relationships. And we will continue to work with our partners and provide a fair transaction if and when they decide it's time to exit a particular property or portfolio. We do have mom and pops coming to us at an increasing rate. Many of the smaller operators are acknowledging that they cannot compete against the national operators. They don't have the platform or the systems, particularly with the internet, to really drive traffic like the larger operators do. Some of the mom and pops, however, still are looking for prices that are not realistic, at least not for Extra Space, and we remain a disciplined buyer adding properties when it is accretive to this Company.

Swaroop Yalla - *Morgan Stanley - Analyst*

That's helpful. I wondered, second question I wanted to ask on the rental trends, if you can talk about asking rents, how they've trended this quarter? And then do you track your rents versus overall market rents? Can you talk about the delta between yours and the overall market?

Karl Haas - *Extra Space Storage Inc - COO*

Yes, this is Karl. Our rates are holding quite well. We ended the quarter about 3% above the prior year, and combined with the occupancy delta to last year, which held better than I would have expected, that's what really -- the combination of that is what drove our growth this quarter. As far as the competitors, it's kind of all over the place. Public Storage, Cube and Sovereign, their rates are up and down, and in a lot of cases follow us, or not necessarily follow us, but we are all kind of moving together. The local operators really are -- there's not much variability in their rates. They stay about the same. So we, in this last quarter, I believe we probably closed the gap a little bit with our competitors. We in some cases were above, in some cases were below, but the gap closed a little bit. Because we held our rates probably a little bit more than others, and that's not surprising, because our occupancy is at a better level.

Swaroop Yalla - *Morgan Stanley - Analyst*

Got it. So the local operators are sort of flat for the year, you're saying?

Karl Haas - *Extra Space Storage Inc - COO*

Yes, they really haven't adjusted their rates much at all.

Swaroop Yalla - *Morgan Stanley - Analyst*

Great, thank you.

Operator

Michael Knott.

Michael Knott - *Green Street Advisors - Analyst*

Spencer, I just wanted to ask you, is this as good as it gets, and what else can you guys do to keep this going, both on the internal growth side and on the external growth side as we all look into 2013?

Spencer Kirk - *Extra Space Storage Inc - CEO*

We're certainly not complaining as a management team, looking at the overall economy and reading the bad news, and then looking at what we're able to do in the storage sector. I'm not going to say it's as good as it gets, but it certainly is a very pleasant time to be in this sector and associated with the great team here at Extra Space. It's a very enjoyable time for me personally. The things that I think will continue to propel our performance, Michael, are, number one is, we have a unique structure, and we're not reliant upon just one or two things to help drive our growth. In previous conference calls I've talked about five levers of growth, which are significant, and I think it might be worth repeating, that we believe Extra Space has a unique position. And the five drivers of growth that I think continue to propel performance are, number one, our core property performance, which has been enhanced by superb execution at the site level, which has all been enhanced with very strong technology base to give us the tools to produce what I would consider better than peer performance. I'm very pleased that our development pipeline continues to mature and the lease up assets through 2014 will add value and meaningful cents per share to the FFO. We've got our off market and open market acquisitions. I think as you've seen, nearing $500 million in acquisitions, that have been transacted or announced so far this year, says that we're doing a decent job of working with our partners and also being competitive. In the open marketplace.

Our tenant insurance program continues to provide meaningful FFO growth for this Company, because every time we acquire a new property, or push the lease up of an asset or bring a new third party management asset into the pool, we get meaningful new customers. Thousands at a time typically in a quarter. And the last area where we have done well is the third party business continues to grow. We are focusing certainly on those areas where we've got an operational overlay on the footprint, and we think that those ultimately will become acquisition opportunities. Those are the five key levers. Let me had a sixth. There is virtually no new supply coming into the market.

And that bodes well for the existing operators. The question is, with no new supply who captures a disproportionate share of what's available out there, and that's where the power of the internet and the sophistication of our systems and the other national players comes into play. I've said before it. But we have 42 dedicated resources, internally and externally, working on the internet to drive traffic and capture a disproportionate share, and the internet, which was supposed to be the great equalizer for all storage operators, has become the great divider. And I'm pleased to report that our internet strategy is not only robust, it's producing the results that we have invested heavily to capture. So I'd give you the five traditional answers, Michael, and just reemphasize that no new supply and the power of the internet have made the playing field less than level.

Michael Knott - *Green Street Advisors - Analyst*

Okay, Thanks for that. Appreciate that. Then my second question would just be your capital structure and financing strategy as it relates to continued external growth. How do you think about your cost of capital with how successful your stock has been trading and how you might use that to continue your acquisition strategy?

Spencer Kirk - *Extra Space Storage Inc - CEO*

We're going to let Scott answer that question, if I may.

Scott Stubbs - *Extra Space Storage Inc - CFO*

Michael, it's Scott. You know, we obviously, with the stock price trading where it is, and looking at acquisitions and growing there, it's obviously a consideration. You have interest rates at all time lows, but at the same time, I think it's important not to ignore the long term cost of capital. So, while we have become slightly more aggressive on our cap rates and what we're buying right now, it's not significantly more aggressive. We've -- we continue to finance things and buy things on largely a leveraged neutral basis.

Michael Knott - *Green Street Advisors - Analyst*

And which is -- how do you guys think about your balance sheet longer term? Just maybe remind everyone.

Scott Stubbs - *Extra Space Storage Inc - CFO*

From a balance sheet perspective, we look at things as far as being leveraged in the -- probably where we are today, depending on where your stock trades and what your net asset value is you're kind of 30% to 45% range.

Michael Knott - *Green Street Advisors - Analyst*

Your leverage target is 30% to 45%? Is that what you're saying?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It really varies, depending upon the markets. Right now I think that interest rates are very attractive. We're going do things on a secured basis, and not necessarily lever up, but we are not going to -- we are not looking to de-lever right now, so I think it really depends on your net asset value, and your net asset value is going to vary somewhat depending on what cap rates are. So that's why our range is as large as it is.

Michael Knott - *Green Street Advisors - Analyst*

Okay. Just last question. Why not finance more of your growth as you go forward with more equity as opposed to leverage neutral?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's something we're always looking at, Michael. We would look at issuing equity. We would look at, if we have somewhere to put that money.

Michael Knott - *Green Street Advisors - Analyst*

Thanks.

Operator

David Toti, Cantor Fitzgerald.

David Toti - *Cantor Fitzgerald - Analyst*

Spencer, I think you touched on this a little bit, but can you just maybe walk us through what changed so dramatically in the last couple of months. Number one, to push performance where it was relative to your original expectations, and generally what's been taking place that's kind of brightens your view so much? It's a pretty significant move from the last time we had an update from the team.

Spencer Kirk - *Extra Space Storage Inc - CEO*

I think, David, the answer I would give you is, we are really focused on the fundamentals. So we talked about enhancing property performance. And it begins with making sure that we do everything possible to get the right price with the right discount to the right customer at the right time.

And I think we're becoming better at that. I also acknowledged that we're only at the leading edge of that. We've done a better job on our tenant insurance penetration rates. We've done a better job of controlling our utilities expenses and reaping the benefit of the solar investments we've made. It's incrementally, David, in my opinion, an amalgamation of a lot of efforts and investments that we've previously had made where we're starting to see the benefit. And I fully acknowledge that we've had a really good strong rebound coming out of the recession.

Our performance quarter-over-quarter and year-over-year has been a very positive and pleasant surprise for us. But I don't delude myself, nor does this team delude itself into thinking that all is well. There are considerable, significant, negative exogenous forces in the world that could cause disruption. And we want to provide the very best guidance, recognizing that this team is executing exceptionally well, but the operating environment of the overall economy to which the overall health of this business is tied, remains less than certain. And we want to strike that fine balance between recognizing that we're executing well but also knowing that the economy is hardly on the road to recovery or in a position to provide a boost. And with the no new supply and the technological investments that we've made, we're very pleased with the results. Our job as a management team is not to think that it's a give me. Each and every quarter we are working as hard as we possibly can, recognizing that there is no free lunch, and we need to earn our keep every day.

David Toti - *Cantor Fitzgerald - Analyst*

I appreciate that color. Do you think anything has changed on the consumer side? Has there been a loosening of the purse strings? Have you just sort of figured out the psychology a little bit more? Has activity in the housing market perhaps contributed? In order words, has the backdrop of the demand part of the equation improved to sort of map on to your internal efforts?

Spencer Kirk - *Extra Space Storage Inc - CEO*

I think it's all of the above, David. I visit a fair number of sites. I'm in the field quite a lot, actually, and as I talk to our site managers, yes, I think there's been loosening of the purse strings. There doesn't seem to be the gross negative overhang of two and three years ago. The people are not overly optimistic about the future. The good news in all of this is, storage is a need based product, and those life changing events continue to happen in a tepid economy. And our job as a management team has just been simply to say, look, people will be on the move, they will be in transition. Life changing events will take place. How can we best maximize the value of each and every customer, and how can we target and capture more than our fair share of those people that are going out to the marketplace.

I'll say it again. The internet was thought to be the great equalizer, it is the great divider, and our investment in the internet is paying out a very rich dividend, and we will continue to invest in not only the standard traditional paid and organic searches, but the social media and some of the other evolutions that are coming upon us in the interactive marketing world, are things that we continue to invest in, monitor, and will be prepared when the time comes. So these are the things I think will help to propel the performance in the future.

David Toti - *Cantor Fitzgerald - Analyst*

Great. Thank you for the detail today.

Operator

Christy McElroy, USB.

Christy McElroy - *USB - Analyst*

Your operating today at some of the lowest leverage levels since going public, but your target range extends pretty well beyond that. Are you effectively in sort of a low cost of capital world kind of preparing your balance sheet for the potential of an accelerated level of acquisitions or external growth over the next few years?

Spencer Kirk - *Extra Space Storage Inc - CEO*

I don't know that we're necessarily preparing you for that. I think that we're always prepared to acquire things. We always want to be at a level that serves our shareholders well. If you think about our balance sheet strategy over the past several years, I think it's served us well in good times and bad. We've naturally de-levered a little bit with the dividends so we do have the ability to acquire some things right now, and so, you know, if we have opportunities, we'll use leverage as necessary.

Christy McElroy - *USB - Analyst*

Should we expect that sort of going forward, I know you haven't given '13 guidance yet, but should we expect a similar level of acquisitions?

Spencer Kirk - *Extra Space Storage Inc - CEO*

I think it's hard to expect that. I think we generally put $100 million as kind of our target number and then hopefully exceed that, but I think it's hard to expect that, especially with cap rates decreasing.

Christy McElroy - *USB - Analyst*

And then just with regards to your dividend, how close are you now to your sort of expected taxable income for this year, and given your earnings growth, is it possible that you might have to revisit the payout earlier than the usual Q1?

Spencer Kirk - *Extra Space Storage Inc - CEO*

We're generally very -- we're close to the taxable REIT minimum, so it's something that we'll keep our eye on, and as FFO grows, it's something that obviously may or may not need to be adjusted.

Christy McElroy - *USB - Analyst*

Thank you.

Operator

Ki Bin Kim, Macquarie.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

If you go back to your comments on breaking out your same store revenue growth, thank you for breaking out contribution from unstabilized properties, but I was curious to know if all your unstabilized properties in the past, I don't know how many years, four years, are included that I know 0.8% breakout, or is it only the '07, '08 vintage?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's really a mix, Ki Bin. This is Scott, we added I believe, 29 properties this year. It's really probably about 19 of those properties.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

So how far from a vintage development year standpoint does that go back? Because I know you guys developed probably all throughout the 2000s, so I was curious what -- what bucket of that is captured in your same store?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's really the ones that just got added this last year. Our same store definition is the property has to be open for three years or be 80% occupied for one full year, measured January 1. So the oldest a property could really be is 3 years and 364 days.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

And I don't want to belabor the point, but for the 0.8% of same store revenue coming from unstabilized assets, is that more than one year's worth of development? That's what I'm trying to get at.

Scott Stubbs - *Extra Space Storage Inc - CFO*

It does have a little bit more than one year's of development but it also has some acquisition that was in lease up also.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay.

Scott Stubbs - *Extra Space Storage Inc - CFO*

So it's not just straight development.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay. The reason I was asking was because there is developments from like '05, '06, '07 that are probably still reaching full occupancy that probably helped that number even further than 0.8%. Is that correct?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Even through the downturn our properties have continued to lease up. They haven't necessarily struggled from an occupancy perspective. It's more on the rate side where we've really pushed rates. A few of those properties obviously have struggled some, but for the most part our developments have all leased up fairly well.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay. And just a second question. Going back to your comments about the acquisition cap rate ranging from 6.5 to 8, at would point -- I'm guessing the 6.5 is for the best stuff out there, but at what point -- at what level does that 6.5 rate has to come down to, to maybe justify new development? And would you ever do it? I guess ever is a bad question, but close to it.

Spencer Kirk - *Extra Space Storage Inc - CEO*

Ki Bin, it's Spencer. I'm not going to give you a threshold as to what that needs to come down. We do think that their needs to be a very healthy 250 basis point to 350 basis point spread to do development. To take on the risk of development versus what we can buy in the open market. We think that their needs to be something substantive to make it worthwhile. We exited the development world and currently have no plans to reenter the develop market. Ultimately I would just underpin that and say, we're going to do what is best for the shareholders, but we have been through unprecedented times, and I think our current strategy is providing the highest and best return with the lowest risk profile currently for our shareholders. As the environment evolves, perhaps the strategy with evolve, but I think we've been pretty clear on our direction on that.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay, thank you.

Operator

Eric Wolfe, Citi.

Eric Wolfe - *Citigroup - Analyst*

I just wanted to follow up on David's line of questioning about sort of what's changed relative to your guidance. If you look at the different components of your revenue growth, occupancy renewals, street rates et cetera, what specifically has surprised you relative to your guidance that you gave last quarter, and does that change your strategy at all going forward?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Eric it's Scott Stubbs. The guidance we gave last quarter was at a time when we were looking at April, and April was all right but you wasn't that strong. If you look at the year, we were right on budget at that time, or very close to budget. During the second quarter, we have exceeded our budgets and therefore adjusted our remainder -- our estimates for the remainder of the year, when it comes to our properties. If you think about, we just exceeded by $0.03, we then adjust our remainder of the year slightly. I think it didn't make sense in the current environment, not to increase our guidance.

Eric Wolfe - *Citigroup - Analyst*

I know you're very focused on revenue maximization so you're not so focused on just building occupancy or pushing the rate, but if you look at where you sort of ended up this quarter from an occupancy perspective and rate perspective, is there any sort of noticeable difference there versus what you had initially conceived, or is it pretty much just everything's stronger across the board?

Karl Haas - *Extra Space Storage Inc - COO*

This is Karl. We're pleased with the occupancy delta being as high as it is. And it was somewhat unexpected because we have been more aggressive on rates. I think in the prior two calls I've tried to prepare everybody for that occupancy delta to close, and at some point it will, but we're out there with the system doing what it determines is the best store-by-store way to maximize revenue. And it's just played out that while we push rates, we've been able to hold the occupancy as well. And from the surprise standpoint, or the thing that probably helped us the most is that we knew we were pushing rates, but we were very pleased that our occupancy held.

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Eric Wolfe - *Citigroup - Analyst*

Right. That's very helpful. Last question. Looking at your guidance for the remainder of the year, specifically on the revenue growth side, you would seem to be dropping from, call it the high 6's, 6.7, second quarter to sort of the low 4's. Is it just sort of a conservative take on occupancy that takes you down there, that gap might not hold quite as much? Because I'm just trying to figure out what can take from you that high 6's to the low 4's in such a short period of time.

Karl Haas - *Extra Space Storage Inc - COO*

Well, I think it's a combination of looking at 2011. I mean, when we do our budgets, and we come up with our numbers, one of the final things I look at is a graph that plots what we're doing this year compared to what we've done in the prior couple of years. And a couple of things come into play. Last year, we had an odd phenomenon, and the graphs I had went back four years, five years. We've never had a year where you didn't have a downturn in the fourth quarter, last year it did not downturn.

I don't expect that, that's a permanent trend. So, when you look at the gap and you look at the numbers we're continuing to go against, we just feel like that's a pretty realistic estimate. And going back, when we look at our performance even so far this year, our -- we've actually hit pretty close to our budgeted numbers. We've beat on expenses by a lot more than we have on the revenue side as far as our actual budgeted numbers.

Eric Wolfe - *Citigroup - Analyst*

Got you. That's very helpful detail. Thank you.

Operator

Smedes Rose, KBW.

Smedes Rose - *Keefe, Bruyette & Woods - Analyst*

On properties that you have acquired that were in lease-up or some of your newer properties that are continuing to lease-up, are you seeing the demand coming incrementally faster given that occupancies have held up better than what you thought? Are you seeing that across the board or is it in more mature markets or denser markets?

Karl Haas - *Extra Space Storage Inc - COO*

This is Karl. It's kind of all over the place, and I think two years ago we were seeing a much slower than expected rent-up, and that's kind of what is impacting, like these 19 properties. They were -- they took longer to rent-up. Normally in the past it's been a three year rent-up to four year rent-up. Now it's become, during this recession, a four to five year rent-up, but, I mean, all in all, we're pleased with the rent-up of the properties that are in -- that are in that phase right now. And -- but it varies by market, and actually even within the market, it varies. We've got a good number of properties in Florida that are in that rent-up group, and recently they've done very, very well.

Smedes Rose - *Keefe, Bruyette & Woods - Analyst*

Okay. And then I just wanted to ask you, on your tenant reinsurance program, it looks like it was running a little better than at least what we had estimated. What sort of penetration does that program have at this point?

Karl Haas - *Extra Space Storage Inc - COO*

We're in between 65% and 70%, and we're pretty much hitting our target. The growth rate is -- the speed that we're able to increase the overall penetration has definitely slowed down. We're maturing. What helps is when we are able to add new properties, and especially the new third party managed properties which come in with very, very low penetration and we can grow those pretty significantly.

Smedes Rose - *Keefe, Bruyette & Woods - Analyst*

Great. Thank you.

Operator

Todd Thomas, KeyBanc Capital Markets

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Just a follow up question, actually, on the acquisitions. Outside of the Pru deal, I just wondering what the average cap rate and where occupancy is for the properties acquired and the 9 under contract.

Scott Stubbs - *Extra Space Storage Inc - CFO*

This is Scott. It's been pretty similar. Your cap rates will range from 6.5 to 8 and your occupancy, for the most part we're buying stabilized assets. And it's the same for the properties under contract.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay. And then, Karl, I think you noted earlier that asked rents were 3% higher versus last year. I was just wondering where are asking rents across the portfolio relative to inline rents? And also, do you have the growth in net rent per occupied square foot for the same store pull year-over-year? In the supplement you give that number. I see it for the different segments, but there's no year-over-year comp, and obviously the pools have changed over the course of the year.

Karl Haas - *Extra Space Storage Inc - COO*

As far as, I guess, Q '11 -- Q2 2011, $13.52. Q2 2012, is $13.97. As far as the asking rates versus in place rates, they're relatively even. I actually haven't looked at it real, real recently, but that's become kind of a non issue for us.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay. And then just lastly, did you -- do you have occupancy as of today, the last day of the month?

Karl Haas - *Extra Space Storage Inc - COO*

Yes. We're a little over 90%.

Todd Thomas - *KeyBanc Capital Markets - Analyst*

Okay, great, thank you.

Operator

RJ Milligan, Raymond James Associates.

RJ Milligan - *Raymond James - Analyst*

The updated acquisition guidance I guess would imply pretty minimal activity for the rest of the year and I was wondering if that's a function of maybe a smaller sort of short term pipeline, if that's a issue of expected closing dates or if that's just sort of being conservative.

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's based on what we have that we're looking at currently and what we have under LOI. So, you know, right now we don't have a ton in the pipeline.

RJ Milligan - *Raymond James - Analyst*

Okay. And then getting --.

Spencer Kirk - *Extra Space Storage Inc - CEO*

RJ, it's Spencer. One other comment. Realistically by my math you've got four months left in the year if you take out the holiday season and all this other stuff. So if it's not under contract, you're under a substantive discussion right now, the likelihood that you are going to transact something that's material between now and the end of the year is going to become increasingly more difficult. So I think as you look at our guidance for the rest of the year, I think you are going to find it to be pretty accurate, because we're not in any type of dialogue with people that will provide something that pops. Now that could change, but right now there's nothing in the pipeline that's going to be a surprise between now and the end of the year that we would be able to highlight.

RJ Milligan - *Raymond James - Analyst*

Okay. Thank you. And my second question is more for the -- on the supply side. I'm curious, how much do you think rents can go higher before we start to see new supply, and is it purely a mathematical question before we start to see new supply, or are there other barriers, financing, entitlements, et cetera?

Scott Stubbs - *Extra Space Storage Inc - CFO*

We would tell you that the main barrier right now not only is the yield, but also financing, which obviously financing is part of the yield. Banks haven't loosened their purse springs, so to speak, to the smaller operators. If you think about the development that took place, in 2003 to 2007 call it, we were developing more than any of the other public companies and we were doing 10 to 15 a year. So, we were a very small portion of what was being added, so until the smaller operators are able to get attractive bank loans, we don't see it changing significantly.

RJ Milligan - *Raymond James - Analyst*

And then if there was access to the financing, how far do you think you could push rents before you started to see the smaller developments -- developers come in and start building?

Spencer Kirk - *Extra Space Storage Inc - CEO*

The way to look at this, RJ, would be to say, all right, if banks turned on the lending spigot, say 12 months from now, you've got to get through the entitlement stuff, because some of those will go stale, and will you have to get that. So that's one to two years, a year to construct and then three to five year to lease up. So, when we talk about no new supply, I think we've got a comfortable cushion. But it all depends, I think primarily when banks start to lend, because that will signal to the smaller guys that it's time to get back in the game.

Let me give you a data point just to underscore what Scott said. I did a quick back of the napkin sketch of developments in 2003, 2004, 2005, 2006, 2007. 13,011 self storage facilities were built in the United States, by one measure. That's 2,600 a year. And Extra Space is the most prolific public company developing, it was producing 12 to 15. Hardly a drop in the bucket against that backdrop of 2,600 year on average. So, a lot of things can and will change but the lending environment for the small guy hasn't changed a lot. We'll just have to see how things play out.

RJ Milligan - *Raymond James - Analyst*

Okay, great, thanks, guys.

Operator

Paula Poskon, Robert W Baird.

Paula Poskon - *Robert W. Baird & Co. - Analyst*

I want to follow up on the lease-up assets discussion throughout the call, and maybe ask this in a different way. So often you all have had a slide in your investor presentations talking about the -- what the stabilization of those lease-up assets would add to FFO through 2014. Is that still true, or is some of the occupancy gains that we've seen an acceleration of that lease-up stabilization?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's still the same. It's still about $0.07.

Paula Poskon - *Robert W. Baird & Co. - Analyst*

Okay. Thank you, Scott. And any thoughts about moving to an unsecured financing strategy?

Scott Stubbs - *Extra Space Storage Inc - CFO*

It's something we'll look at. Unsecured obviously is an option, we're not looking to go to a completely unsecured financing strategy.

Paula Poskon - *Robert W. Baird & Co. - Analyst*

That's all I have. Thank you.

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Operator

Michael Salinsky, RBC Capital Markets.

Michael Salinsky - *RBC Capital Markets - Analyst*

Scott, first question. As you look at the second half of the year what are you guys expecting in terms of real estate tax appraisals, maybe on a year-over-year basis? And also, looking at financing costs, just curious where you guys could issue new secured today, what kind of terms you're hearing from the banks as well as insurance companies, things of that nature?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Our property tax consultants have -- we've used a number of about 4% for year-over-year increase on property taxes. So far it's been running fairly close to that as the assessments come in. As far as new secured financing, after the subsequent to the end of the quarter we did a tranche of seven year money at just under 3.2%.

Michael Salinsky - *RBC Capital Markets - Analyst*

What was the LTV on that?

Scott Stubbs - *Extra Space Storage Inc - CFO*

About 70%.

Michael Salinsky - *RBC Capital Markets - Analyst*

Okay, and that was 10 year, right?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Seven year money. So, you know, if you compare that to unsecured, it's quite a bit lower interest rate right there.

Michael Salinsky - *RBC Capital Markets - Analyst*

Okay. And, Karl, my follow up question, you talked about renewal and street rents. What is the delta right now between move in rents and move out rents?

Karl Haas - *Extra Space Storage Inc - COO*

Relatively -- well, it's -- I don't have it right in front of me. We could get it for you. It's probably -- move out rates are probably a little bit more than the move in rates. But we bring people in at aggressive rates, and then raise their rates. So it doesn't stay -- that gap doesn't remain all that long.

Michael Salinsky - *RBC Capital Markets - Analyst*

If you could provide that offline, I'd greatly appreciate it, but how does that compare right now versus, call it a year ago, that delta? How much would say that has narrowed?

Karl Haas - *Extra Space Storage Inc - COO*

It is close because our existing customer rate increases have not changed dramatically, but our rates are starting to climb -- our street rates are starting to climb. So -- based on that, it has to be closing.

Michael Salinsky - *RBC Capital Markets - Analyst*

That's all from me, guys, thank you.

Operator

Omotayo Okusanya, Jefferies.

Omotayo Okusanya - *Jefferies & Co. - Analyst*

With your overall strategy working so well I'm just kind of curious how, what you're seeing in regards to how your competition is basically reacting to what you're doing, not necessarily the public guys, but a lot of the local guys that are in your market that make up the bulk of the market?

Karl Haas - *Extra Space Storage Inc - COO*

This is Karl. They really don't react very much. They haven't adjust their rates, they are afraid to lose occupancy. They aren't as aggressive with existing customer rate increases, because they're afraid of losing occupancy, and so we really haven't seen, you know, we have seen our public competitors follow a lot of the things that we're doing, and every once in awhile we follow what they're doing. But the bulk of the sites out there continue their -- they're making money. They're not in trouble, and they're not unhappy with their results.

Omotayo Okusanya - *Jefferies & Co. - Analyst*

At would point do your prices become so far away from their prices that customers actually start to notice that and focus on that differential when they're thinking of taking a new unit?

Karl Haas - *Extra Space Storage Inc - COO*

Well, our prices aren't out of line with their prices. Where we make up for it is we've been able to gain occupancy, and our existing customer rate increases for the customers, once they're inside. Because people don't move out until they don't need it anymore. So our price is competitive. You go on, and the other thing that's a little bit different is that we have an internet price, and we did lead the industry in this. We have two tiers of pricing.

We have an internet price, and we have a street rate. And so when you walk into the site, those people are less sensitive to prices, and so they're quoted a higher price. If they push back or they walk out, or if they've checked the internet, they'll get the internet price, which can be as much as 15% lower. So when people are comparing us on the internet, us to our competitors, they see that internet price. And that's a very aggressive price. And very competitive price.

Omotayo Okusanya - *Jefferies & Co. - Analyst*

Got it. That's very helpful. Thank you.

Operator

Ki Bin Kim, Macquarie.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Going back to your commentary about the second quarter strength you are seeing, and maybe if we use the occupancy gains as the measuring stick, so from the 270 basis points gain, if you had to break that up into just overall industry occupancy pick up versus market share gains, how would that look like?

Karl Haas - *Extra Space Storage Inc - COO*

Ki Bin, this is Karl. I have no idea, but we can get back to you.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay. And just a second question. I know you said developments probably still far away, especially given financing markets and what not, but if you had to look at the most viable site in your portfolio or where you're located, where would stabilized development yield, based on today's market dynamics be, for the most viable site?

Karl Haas - *Extra Space Storage Inc - COO*

Manhattan. We don't have any sites in Manhattan, but if you could do a site in Manhattan, things would be great.

Scott Stubbs - *Extra Space Storage Inc - CFO*

I think it's going to vary just by market, just because it depends on what the land is selling for. It depends on what the self-storage densities are like in that market, then obviously it depends on the yield you are going to get. So it's pretty variable. The only place you would ever really consider obviously is a place with high barriers to entry.

Karl Haas - *Extra Space Storage Inc - COO*

Long term, the northeast has proven to be a very, very good, strong, long term market for us, and we love that. Chicago has turned out to be pretty good, but it hasn't probably in the long term, it hasn't been as great as it's been recently.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay. Well, I guess I was guessing -- what I was asking, are yields just close to where you can buy assets at, which [fly is still] far away, or how does that relationship look like?

Karl Haas - *Extra Space Storage Inc - COO*

We haven't looked at it significantly, so it would be difficult to comment on that.

Ki Bin Kim - *Macquarie Research Equities - Analyst*

Okay, fair enough, thanks.

Operator

Michael Knott, Green Street Advisors.

Michael Knott - *Green Street Advisors - Analyst*

Hey, guys, I guess this one would be for Karl. I think we've had a few variations of this question. I don't think anyone has asked this one just yet. But year-over-year change in street rates for, I guess, maybe the end of 2Q compared to, I guess, the end of 2Q of '11, and then maybe how that differs from the same year-over-year comparison at 1Q '12 versus 1Q '11?

Karl Haas - *Extra Space Storage Inc - COO*

That's a tough one. 3.5% at the end of Q2. I think it was around 3% at the end of Q1. I don't remember what it was at the end of -- in 2011, but it was probably less than that. It's gone up and down. We're constantly -- I mean, I wish I could say that I set it, but the system really, it evolves based on our system.

Michael Knott - *Green Street Advisors - Analyst*

And then I guess with the proliferation of internet rentals, I guess when we even ask about street rents on these calls, is that literally just the -- are you talking now those numbers you just gave, are those literally the street rents in the stores, or is that a blend of your asking rents at the store level and on the internet?

Karl Haas - *Extra Space Storage Inc - COO*

One follows the other. So there's a gap, but one follows the other.

Michael Knott - *Green Street Advisors - Analyst*

Okay.

Karl Haas - *Extra Space Storage Inc - COO*

What our internet -- our internet price is 15% below our street rates. So when we say it's 3.5%, both would be up 3.5%.

Michael Knott - *Green Street Advisors - Analyst*

Got you. Okay. Then just one real quick one. I think you gave a number of occupancy was a little over 90% at the end of July. How does that compare to the end of July of 2011?

Karl Haas - *Extra Space Storage Inc - COO*

It's still up about more than 2.5%. Actually, about 2.7% on our own pull and 2.9% on the big pull.

Michael Knott - *Green Street Advisors - Analyst*

So does your revised guidance consider that maybe that occupancy gap won't close as quickly as you thought?

Karl Haas - *Extra Space Storage Inc - COO*

No. I mean, it's a combination of what we can get with rate. We also are getting a little bit more aggressive with rate, and I expect to see that drive down that -- we haven't taken -- I don't think we've taken seasonality out of our business, and we will see a drop in occupancy, and the delta should close because we are at a very high level of occupancy, and probably a little higher than we expected to be, and, you know, it could be -- I mean, one scenario could play out. We're going push rates, and if the occupancy holds that would certainly help us reach the top end of our guidance. And that will be a good thing. But I wouldn't want to go and guarantee that.

Michael Knott - *Green Street Advisors - Analyst*

Okay. Thank you.

Operator

David Toti, Cantor Fitzgerald.

David Toti - *Cantor Fitzgerald - Analyst*

I think you may have been asked this, but just in case I missed it, when was the last time the portfolio was over 90%? And do you think this is a relatively sustainable level at this point?

Karl Haas - *Extra Space Storage Inc - COO*

Never, and hopefully, you know, well, I mean, remembering that it's seasonal, and we're not going to be 90% year round, but this is the highest level we've been. We're up 6%, 7% from three years ago. It's been a pretty good run.

David Toti - *Cantor Fitzgerald - Analyst*

Assuming the world doesn't get a whole lot worse, is it conceivable that the portfolio could stabilize above 90% at this point?

Karl Haas - *Extra Space Storage Inc - COO*

Anything is conceivable.

David Toti - *Cantor Fitzgerald - Analyst*

Thanks, guys.

Operator

(Operator Instructions)

Eric Wolfe, Citi.

Michael Bilerman - *Citigroup - Analyst*

It's Michael Bilerman. I may have missed this, I jumped on a little bit late. But, just in terms of, on the operating expenses, which you have been able to control pretty well during the year, when you sort of look at, at least, what was the same store guidance of 3 to 4 that you had provided originally when you put out 2012 guidance, and obviously that went down to 1 to 2.5 last quarter and is now down to 0 to 1.5, what is sort of driving almost 300 basis points of savings on the expenses? And just looking at the total portfolio, if you're getting the same sort of savings, it's about $3 million. I'm just curious if you can sort of bucket it a little bit in terms of categories for us?

Karl Haas - *Extra Space Storage Inc - COO*

Well, this is Karl, if you go back to our Q1 call, a big chunk of it was explained there, and that was, we had an unbelievably mild winter, and we had almost no snow removal, and that was -- that is a big chunk. It's one quarter. It doesn't obviously carry over into the rest of the quarters, but also utilities. It's a mild winter, our utilities were dramatically down, and those were the -- by far the biggest drivers and the biggest surprise from our before the year began guidance to what we're ending up with. Those don't repeat, and now what we're getting the benefit from is our investment sustainability, which we're seeing ongoing benefit on the utility expense, but nowhere near the level we were seeing earlier, or in the first quarter. And we will continue through about October, getting the benefit of the reduced credit card fees, because that started actually last year in the -- I believe October, November. So that will equalize and balance out.

Michael Bilerman - *Citigroup - Analyst*

And you're seeing that through all the entire portfolio, whether it be same store, the core, or the unstabilized, and also the assets that you manage?

Karl Haas - *Extra Space Storage Inc - COO*

Yes.

Michael Bilerman - *Citigroup - Analyst*

Is the margin on the tenant reinsurance is obviously higher as you keep on driving that. Is that affecting the same store numbers at all?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Helping it slightly, but it's in our guidance 0.3%.

Michael Bilerman - *Citigroup - Analyst*

So when looking at the same store revenue growth, that bumping up from what was 4.25 to 5.375 at the midpoint, a good portion of that is the tenant reinsurance going up $3 million from your original forecast, correct?

Scott Stubbs - *Extra Space Storage Inc - CFO*

Marginally, it's helping, but the majority of it is the properties themselves performing better. Tenant reinsurance adds, call it 50 basis points.

Karl Haas - *Extra Space Storage Inc - COO*

Actually, I think it's going down. I think it's like 0.3 now.

Michael Bilerman - *Citigroup - Analyst*

Okay, thank you.

Spencer Kirk - *Extra Space Storage Inc - CEO*

Great. Thank you, Michael. We've hit the top of the hour, ladies and gentlemen. Great questions. Good dialogue today. We appreciate your interest in Extra Space. We'll look forward to next quarter's call. Thank you.

Operator

Ladies and gentlemen, that concludes today's conference. You may now disconnect and have a great day.