

How Much Can I Afford to Pay for Land?

The simple answer to that question is in how much revenue your improvements will generate. The complex and accurate answer to that question lies in answering the following questions:

1. What will your proposed project generate in revenues on average per square foot per year?

To answer this question, poll your competitors (all facilities within 3 to 5 miles of your proposed project), determine the average price for an ambient (i.e., non climatized) 10X10 storage unit. Multiply that average price by 12 (months) and divide by 100 (square feet) to get the annualized revenue per square foot.

EXAMPLE: Average price \$75 X 12 = 900 / 100 = \$9 per square foot per year. Repeat this process to determine the average annualized revenue (per square foot) for climate controlled space (also use a 10X10 unit).

If your planned facility has both climate controlled and ambient space, determine the percentage of climate controlled space you intend to build.

Average the annualized ambient and climatized revenues you calculated. Example: ambient space in your market rents for \$9 sq. ft. per year. Climate controlled space averages \$12 sq. ft. per year. You decide to build a facility that is one-third climate controlled space and two-thirds ambient space. One-third of \$12 equals \$4. Two-thirds of \$9 equals \$6. Therefore, the annualized revenues for your planned project will be \$10 (\$4 + \$6)

2. How many rentable square feet do you plan to build:

Let's say your feasibility study recommends that you build a facility of 60,000 net rentable square feet (net rentable = gross building square feet MINUS common areas such as office, hallways, etc.)

The normal proforma vacancy factor would be 8%; however, most facilities recover that loss with ancillary income (administration fees, sales of locks and boxes, late charges, etc.) Therefore, for the purposes of this example, you can assume a 100% occupancy rate.

3. How many stories should you build:

Let's assume that your feasibility study recommends a single story project to be most competitive in your market.

A. for single story projects, assume land coverage of 40% to 50% of total land square footage (if the land is rectangular in shape, with no unusual easements, set-backs or over-wide aisles).

EXAMPLE: 3 acres (or approximately 130,000 square feet) would yield net rentable storage of 50,000 to 65,000 square feet.

Multi-story projects:

Land coverage is generally governed by local zoning ordinances. Always consider set-back requirements, FAR (floor to area ratios), total land coverage restrictions and building height restrictions. You will also need to consider at what point a sprinkling system and firewall requirements will affect building dimensions and costs.

The gross square footage of a multi-story building will generally yield a net rentable square footage of 74%.

4. Calculate your planned project's annual gross revenue:

Multiply the rentable square feet times the average revenue figure.

EXAMPLE: 60,000 (sq. ft.) times \$10(per. sq. ft.) = \$600,000 annual gross revenue.

Annual gross revenue should be divided into thirds. One third can be assigned to expenses (e.g., real estate taxes, insurance, manager salaries, management fees, utilities, office supplies, etc.). This assumes the size of your project is between 35,000 and 65,000 net rentable square feet. Smaller projects will have operating expenses HIGHER than 1/3 of gross income. Another third of revenues should be assigned to debt service and the last third to profit.

Debt Service

This is the key element in beginning to determine A) the price you can afford to pay for land and B) the likelihood that a lender will give your project favorable consideration (a financially healthy self storage project will have a breakeven of 65% to 70% of gross revenues).

With \$200,000 (\$600,000/3) of revenue assigned to cover debt service, working backward you can determine the amount of money you can afford to borrow and your equity requirements.

The factors affecting this are: terms of the loan (interest and amortization schedule) and the amount of equity you intend to contribute to the project (normally 20 per cent of the total project cost).

Construction Estimates

Single story self storage projects should cost between \$22 and \$28 per square foot. This is a turn-key construction average including hard and soft costs (foundations, buildings, an access gate and fence, computer, office space, paving and landscaping). For climate controlled space add between \$1 and \$2 per square foot (of the gross rentable square feet that are climitized) to total net rentable. Metal buildings are slightly less expensive and take less time to build than concrete block or tilt-up buildings. Unusually high site preparation costs will affect this number. Consider such items as: rock blasting, fill and compacting, drainage problems, the need for retention walls, removal of toxic fill or debris and vegetative wetland requirements (can you say EPA?)--which in this case translates into Extra Project Agony!

A two-story facility with elevators and climate controlled space will generally cost between \$32 and \$38 per square foot. For three or more stories consult an architect because the number of cost variables increases exponentially.

Development Factors

The factors that determine what you can afford to pay for land are: potential revenues, construction costs, terms of debt service and your equity. To continue our example:

Gross Project Revenues: \$600,000

Construction cost: \$1,500,000

40,000 (gross sq. feet of ambient space;
40,000 net rentable) X \$22.50 = \$900,000.
plus
25,000 (gross sq. feet of climitized space;
20,000 net rentable) X \$24.00= \$600,000.

The \$200,000 that is assigned to debt service can support \$1.76 million in total debt (assuming terms of 15 years). *[If the interest rate is 7%, total annual debt service on \$1.76 million is \$189,833; at 7 1/2% it is \$195,785; at 8% it is \$201,834 and at 8 1/2% it is \$207,977].* With a debt of \$1.76 million (\$1.5 million going to construction cost, leaving \$260,00 toward land) and 20% equity (\$440,000), the total project cost would be \$2.2 million. Working capital is generally 10% of the total cost of the project. In this example working capital would equal \$220,000. so the project dollars remaining for the purchase of land equals approximately \$480,000 (\$260,000 + \$220,000). In our example, you purchased 130,000 square feet of land, therefore that land should cost no more than \$3.69 per square foot.

$$\begin{aligned} & \$1,760,000 - \$1,500,000 = \$260,000 \\ & \qquad \qquad \qquad + \\ & \$440,000 - \$220,000 = \underline{\$220,000} \\ & \qquad \qquad \qquad \$480,000 \text{ divided by } 130,000 \text{ sq. ft.} = \$3.69 \end{aligned}$$

For more information contact:

Capacity Development Corporation
751 Marion Avenue
Highland Park, Illinois 60035

847/433-7510