

***Transcript of
Life Storage
First Quarter 2017 Earnings Release Conference Call - Edited
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Participants

Diane Piegza – Vice President Investor Relations
Dave Rogers – Chief Executive Officer
Andy Gregorie – Chief Financial Officer
Ed Killeen – Chief Operating Officer
Paul Powell – Chief Investment Officer

Analysts

Juan Sanabria – Bank of America
Smedes Rose – Citigroup
Todd Thomas – Keybank Capital Markets
Ki Bin Kim – SunTrust Robinson Humphries
David Corak – FBR Capital Markets
Gwen Clark – Evercorp ISI
George Hoglund – Jeffries
Todd Stender – Wells Fargo

Presentation

Operator

Greetings, and welcome to the Life Storage First Quarter 2017 Earnings Release Conference Call. At this time, all participants are in a listen-only mode. A question and answer session will follow the formal presentation. [Operator Instructions]. As a reminder, this call is being recorded.

I would now like to turn the conference over to your host, Miss Diane Piegza, Vice President Investor Relations for Life Storage. Thank you, you may begin.

Diane Piegza – Vice President Investor Relations

Thank you, Melissa, and good morning, everyone. Welcome to the First Quarter 2017 Conference Call. Participating in today's call are Dave Rogers, our Chief Executive Officer; Andy Gregorie, Ed Killeen, and Paul Powell.

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 concerning these factors can be found in the company's latest SEC filings. In addition to our press release, we have added a financial supplement which is available on the Investor Relations page at Lifestorage.com.

At this time, I will turn the call over to Dave.

Dave Rogers – Chief Executive Officer

Thanks, Diane. Welcome, everyone, to our call.

We're calling the first quarter of this year okay. We knew the comparisons to last year's 9.9% Q1 NOI growth was going to be a challenge, especially given the deceleration that occurred in some of our key markets in the back half of 2016. Andy will have the specifics on the metrics, but the part of the operating story that everyone wants to know about is what lies ahead.

So here's what we see for the upcoming three quarters. Same store performance is highly market specific. A number of our markets are strong enough that we won't be using many incentives in Q2 or Q3, most of Florida, Atlanta, St. Louis, Charlotte. As a matter of fact, some of those properties will most likely be turning customers away during the peak season due to lack of available units.

Yet, other markets will see almost 100% use of incentives, even right through the busy season. All of Texas, the Greater New York Metro Area, Raleigh, and the Gulf Coast are specifically in that package.

The second quarter should be our toughest year-over-year quarterly comp. Last year at June 30th, we recorded our highest ever quarter end occupancy of 92.7%. Further, during that quarter we issued only a modest amount of free rent incentives. This year, we will be pulling the free rent lever very hard in at least half of our markets to hold as much occupancy as we can.

Supply continues to increase and we expect our already softer markets to be impacted the worst, especially Dallas, Houston and San Antonio. By the second half of the year, we also expect trouble to hit some of our stronger markets, notably Southeast Florida.

March and now April saw demand drop slightly as measured by call volume. Again, it's a tale of markets. The range goes from positive double-digit percentage in the strong areas to minus 6% in the weaker, but the weighted average skewed to the red.

So with these factors facing us, we felt compelled to bump guidance south a bit. Of course with the busy season underway for less than a week, the actual story of the year is now just unfolding.

So that's the same store outlook. It's soft and it's probably going to be this way for a few quarters. It's a combination of going up against tough comps, growing supply in some of our largest and most important markets, and a touch of a slowdown in demand growth. But fortunately, a lot of what we've done in the past year has made the same store part of our story just that – a part. We positioned our company into a multi-faceted owner operator, providing us with multiple paths to earnings growth, increased value, and future growth potential. Here's that part of the story.

Life Storage Solutions, with our new name and a reinvigorated marketing effort to our third party management platform, we've added more contracts in this quarter than we have in any single whole year in the past, and there's more in the queue. As noted on prior calls, this line of business generates fee income, adds to market exposure and scale, and creates a pipeline for future acquisitions. We missed an opportunity four years ago to jump on the 3 pm bandwagon; we're ready to go this cycle.

Increased activity with our JV partner, this allows us to acquire quality properties in existing markets with minimal capital outlay. We expect to add up to 20 properties by mid-summer as a result of such transactions and hopefully more later in the year.

We have a pool of almost two dozen C of O and early stage lease up properties that will provide growth at a significantly greater pace than the same store pool will.

We have another 100+ stores not in the same store pool brought on via the Life Storage acquisition and various one-off transactions in 2016. These stores also have the potential for outsized growth in the next coming two years.

Our expansion and enhancement program continues. This year we're spending \$30 million to add premium, high end buildings and units to 18 stores, and repositioning their visibility and presence in the process.

Our new brand, Life Storage and our new image have been tremendously well received in our markets on the web and with our corporate customers. The marketing and advertising campaigns we've been able to build around Life Storage are awesome. Check out one of the videos at lifestorage.com/because to get an idea of what we're talking about.

Our company is a lot bigger and better and stronger than it was at this time last year. Some of the benefits of this evolution are currently hidden under a bushel because of the headwinds the industry is experiencing and because some of our biggest markets happen to be on the flipside of the cycle right now. But the improvement to our company is real and our important markets will be coming back. In the meantime, we're adding a lot of value to our company by applying the benefits of our platforms to the properties in the non-same store pool. The 3PM and JV acquisition programs allow us to grow our store count and operating scale with a minimal outlay of capital. The Life Storage brand has us all recharged and well positioned to grow our corporate, small business and residential customer market share.

Like Neil Young sings in "My, My, Hey, Hey," there's more to the picture than meets the eye. There's a lot of parts to our story and you're not seeing all of it yet, but it's coming and it's really going to serve us well.

Andy.

Andy Gregorie – Chief Financial Officer

Thanks, Dave. Last night we reported adjusted funds from operations of \$1.26 per share, a result of same store revenue and NOI growth of 3.2%, a 26.7% increase in management fee income, and the performance of our 2016 acquisitions. Drivers behind the same store revenue growth included a 20% increase in average occupancy and a 2.7% increase in rental rates.

Same store occupancy at March 31st was 90.9%, tying a record high for this time of year.

Same store property operating expenses increased 3.2% for the quarter. This was a result of increases in real estate taxes, payroll and benefits, and increased spending on internet marketing as we transitioned to the Life Storage brand.

G&A costs were approximately one million dollars higher this quarter over that of the previous years' first quarter. The main reasons for the increase include the fact that we operated 113 more stores at the end of this quarter as compared to this time last year, the costs associated with our name change and increases in wages in our call center and additional legal fees.

In regards to the 72 stable Life Storage properties acquired in July, these properties are entering the busy season poised for growth with occupancies in the mid-80s and we are putting our platforms to work to fill them up. Additionally, the 11 non stable stores acquired with Life continue to grow occupancy better than expected.

Our balance sheet remains solid. At March 31st, we had \$201 million available on our line of credit, we had no material debt maturities until December 2019 when our line of credit matures. Our debt service coverage was five times and our debt to EBITDA was 5.8 times.

We were not active with our ATM program during the quarter. We do expect to put a new ATM in place this year since our current plan expires at the end of May, but we have no plans to use that program based on our current stock price.

With regard to guidance, although Q1 earnings came in as expected, the lack of occupancy growth, even with increased incentives, gives us pause for the remainder of 2017. However, the company has seen improvements in other areas that we expect will compensate for the lower organic growth, including increases in fees from third party management contracts, contributions from newly formed joint ventures, and the lease up and NOI improvement at the non-same store facilities.

Same store revenue growth for Q2 should be in the 1.5% to 2.5% range. Expenses outside of property taxes should increase between 3.5% and 4.5% for the quarter. Property taxes are forecasted to increase 5% to 6% over 2016's Q2.

Our guidance assumes no additional accretive acquisitions. Our guidance does assume \$0.01 to \$0.03 per share of FFO dilution from the certificate of occupancy deals we have completed to date or that have been previously contracted and are expected to be completed this year.

Based on the above, we are now forecasting annual funds from operations to be between \$5.47 and \$5.53 per share. For the second quarter, we are forecasting funds from operations to be between \$1.32 and \$1.38 per share.

With that, Melissa, we can open the call for questions.

Operator

Thank you. [Operator instructions]. Our first question comes from the line of Juan Sanabria with Bank of America.

Q: Good morning. Thanks for the time. Just a question on guidance. You guys came in at the low end for the first quarter. You talked about the second quarter being kind of the low point of the year, but seems to be a second half pickup implied. What gives you confidence that you can hit these new numbers.

Andy Gregorie – Chief Financial Officer

When we look at the free rent, Q1 our free rent was up about \$350,000. So we knew that was a relatively easy comparable compared to what Q2 would be. Q2 we would expect that free rent to be up, because last year we were aggressive in reducing free rent in the second quarter, in the second quarter of '17 it's hard to see that we can reduce as much as we did last year. So, the free rent is going to be significantly higher than it was last Q2, and that hurts you quickly in the quarter.

On the back half of the year, we did increase incentives in 2016, so the comps easier, so that's what makes us comfortable. We're not baking in a whole lot of occupancy growth. In fact, we right now don't expect to see that but the easier comp with free rent makes us comfortable.

Q: Should you expect free rent to be flat in the second half of '17 versus '16?

Andy Gregorie – Chief Financial Officer

It will be similar with Q1. So if it's \$350,000 higher in Q1 of '17 versus '16, dollar-wise I know some people like to put it as a percentage of revenue, so we're about 2.1% in Q1 of '17 versus 1.8% in Q1 of '16. That number will

grow to maybe 2.4% in Q2 versus 1.3% in last year second quarter. The remainder of the year should be in that 2% range, which is very similar to last year. A little bit above.

Dave Rogers – Chief Executive Officer

We really ramped it up starting in July last year, Juan. That was the surprise we had last year was increase as much as we did. So we were at pretty high levels from July right on through to December of last year. Whereas from April to June, we were really holding back on issuing incentives. So that's why we're saying Q2 is going to be really tough. We're not saying absolute business is going to be much better at all, but we are saying the comp is easier.

Q: Okay. You guys talked about demand and volume. Could you just give us a little bit more color on what you're seeing across the different channels in terms of traffic? Are you seeing any pickup in bad debt?

Ed Killeen, Chief Operating Officer

Well, we're not seeing any pickup at all in bad debt, or at least it's not a material change. I think we're up \$100,000 in bad debt over last year's same quarter.

Looking at traffic and the metrics in regards to traffic, our call volume is down slightly for the quarter year-over-year and our reservations are down slightly as well. But on the positive side, traffic to our web site is actually up year-over-year, albeit it's a slight number, it is up and that just really speaks a lot to the strength of the brand. Where we did lose some traction and ranking, our traffic to our site remains very positive.

Q: One last one for me. How did Street rates trend throughout the first quarter and early into the second quarter?

Ed Killeen, Chief Operating Officer

Street rates end of March they were 2.9%. We were off 2.9%. And in April we're going to be off about 4%.

Q: When you say "off," you mean down 4%?

Ed Killeen, Chief Operating Officer

Yes, down.

Andy Gregorie – Chief Financial Officer

And that is a tale of markets, Juan. That is a tale of markets. There are markets, you see Florida markets up double-digits in Street rate growth. You see Houston down 10%. So it is really a tale of markets. There are some very strong markets; Houston dragging down the overall.

Q: Are those numbers net of concessions or gross?

Andy Gregorie – Chief Financial Officer

That is Street rate.

Q: Okay. That's it for me. Thank you.

Operator

Our next question comes from Smedes Rose with Citigroup.

Q: It's Michael Bilerman here. Dave, I was wondering if you could talk a little bit about Life Storage and how that portfolio is doing? Sequentially, your operating margin came down, so I'm just curious how the more difficult environment that you're talking about is sort of playing into your targeted yield and how we should think about

where that should be for this year. Annualizing first quarter results, you're sort of a pretty low 4% yield, so how should we think about how that trends and how it is relative to where you thought it was three months ago?

Dave Rogers – Chief Executive Officer

The big part about the story with Life was we were forecasting pretty decent growth in markets like Sacramento and Las Vegas and better than our same store pool in the other big markets of Chicago and some of the Texas cities. What's happened in 2017 is while expected those revenues were going to be offset pretty mightily by tax increases, property tax increases due to Prop 13 in the California stores and Chicago being Chicago. So what we've done is we've started accruing those taxes as of January 1, the whole shot. So we're taking the big punch for the four quarters of this year of property taxes as expected with the growth to grow, and we're in the slow season obviously right now. So I think we're happy overall with certainly Las Vegas, with the California properties, Sacramento. Chicago is good. Texas has got the headwinds, we've talked about this in the last couple of quarters. So I think overall, as Andy mentioned, we spent the last half of last year getting these properties ready for the busy season. They are ready. The markets I mentioned are doing as planned.

I think really the only miss in the story out of a lot of positives is the headwinds that we're facing in Texas. Those stores, the Life stores are doing better than our same store pool, but they're caught in the wind as well. So there's 19 stores in that pool that we're watching closely. That's offset a little bit, or actually a decent amount by the progress that the 11 lease up stores are making. So we're behind a little bit in terms of where we want to be, we want to be about three months faster into this, and probably 10 to 20 basis points behind in terms of yield by the time we get through with the third quarter.

Q: So where would yield be by the end of the year if it's at a 4.1% today just annualizing first quarter results?

Andy Gregorie – Chief Financial Officer

If we annualize Q4, we expect to be at a 4.7, so the whole year should work to be about a 4.5. That's both the stable and the lease up.

Q: You also cut your expense growth excluding property taxes and that was down 1.25%. What's that coming from?

Andy Gregorie – Chief Financial Officer

In Q1 we had some better results, obviously, snowplowing and repairs and maintenance came in better than we expected. So, some of it was Q1, some of it's utilities coming in under what we expected, so it's a combination of things. We expected a little bit bigger increase in the insurance side. We will see that, it renewed March 1, so we will see that starting Q2 the full effect of the insurance increase, but it wasn't as big as we thought. So we had some savings there on the expense side. And just our continually putting in more efficient lighting and HVAC systems helping on the utility side.

Ed Killeen, Chief Operating Officer

I think something else to keep in mind in regards to the legacy locations is these properties started off with a pretty high occupancy and it was sort of a false occupancy. We cleaned up A/R and we really replaced those low yield customers with high yield customers, and we're now at a very clean 86% occupancy. That's going to give us a great runway throughout the remainder of the year.

Q: Can you just go through the specifics of breaking out the guidance change? So if you're down \$0.03 to \$0.07, call it \$0.05 at the mid-point, and you noted a number of different things in the press release, it sounds like same store could be upwards of \$0.07 negative. Can you just walk through each of these pieces? And then I don't know if things have changed in terms of contribution for Life Storage or not, it sounds like they're certainly a little bit weaker than you had thought, just so that we can isolate the different items for our model?

Andy Gregorie – Chief Financial Officer

Sure. We can quickly go through a couple of things. You're about right with the \$0.07 from the same store, offset by higher management fees. I think you'll see that number north of \$9 million in management fees is what our projections are. So really the offset was from the new management contracts, the new joint ventures offsetting some of that same store change.

Q: Thank you.

Operator

Our next question comes from Todd Thomas with Keybank Capital Markets.

Q: Thanks. First, are you able to provide occupancy at the end of April for the same store and what that is on a year-over-year basis?

Andy Gregorie – Chief Financial Officer

April, we saw an increase from March. March of '17 to April '17, we saw a 50 basis point increase. Now that compares with 80 basis points we saw last March to April. So we fell back about 30 basis points. The last April was a little bit of a head [indiscernible], if you remember. April was very strong last year. So we are comparing to a very strong April, but occupancy was up 50 basis points from quarter end this March to April versus 80 last March to April.

Q: Then a follow up on the demand. So it sounds like traffic to the website is up year-over-year, but conversions or reservations are down slightly. Are you able to track or understand why the capture rate is falling? Do you have any sense?

Ed Killeen, Chief Operating Officer

We track it on a market by market basis, but it really is difficult to identify precisely why. I mean, there are some, again, as both Dave and Andy suggested, it really is a sort of tale of markets. There's many markets where both the close rate and the reservations that come our way are extremely high, and it seems to be with a strong correlation with the new comps that come into these markets. So I would say there's a little bit of a rate fatigue. We've been pushing rates for 20 some odd quarters now, so I think there's a bit of that. But demand still remains steady and I think that's got to be a major takeaway here. This isn't the same picture as it was maybe years ago. It remains steady. It certainly isn't through the roof, but again, there are some markets where demand is very strong and intros are strong and calls are strong as well.

Q: Then in the markets, some of the weaker markets where you're starting to offer more free rent, are you seeing that starting to drive demand? As you begin to ramp up the free rent offers, are you starting to gauge the competition or are you starting to see some of the competition start to offer more free rent or increase their use of discounts to match your pricing at all?

Ed Killeen, Chief Operating Officer

There's always a bit of price matching, but consumers, by and large, they do react favorably to discounting. As we go into the peak season, depending on where we are with rates and where our true comps are with rates, we do play around with our rates. But certainly, customers are reacting to the heavy discounting and we're able to hold occupancy for that reason.

Q: Lastly, moving over to Texas, Houston and Dallas in particular. I was just wondering if you could just talk about those two markets in terms of rent growth and how new supply is trending. And then for Dallas in particular, revenue growth decelerated there; it sounds like you're expecting some weakness in Dallas. Do you

expect that market to go negative? I was also just wondering, with Houston if you could just provide a guidance update for revenue and NOI growth?

Andy Gregorie – Chief Financial Officer

Regarding Dallas, many new comps coming in. We tracked 25 new comps within 5 miles that have opened within the last year. So Dallas is one. It's been on our watch for a while. We said that after Houston that would probably be a big market that could go negative. So it has great demand. The phone is ringing, but the new supply and the discounting's will hurt Dallas until those stores fill up. So a little bit of overbuilding going on in Dallas and hopefully that quiets down next year, but this year with those 25 stores opened within the last 18 months, that's going to drag that probably over the next two quarters into the negative territory.

But it's a great market. It will come back pretty strong. We just have to absorb that new supply. Demand is doing alright.

Houston, it's a tough read on Houston with rates down 10%. We're holding occupancy, but we have to get through this busy season. It's hard to tell where Houston could end up. It's not going to turn around any time soon. We expect another two or three quarters with the deceleration on the revenue line.

Q: Any update to the guidance on Houston for the full year?

Andy Gregorie – Chief Financial Officer

It's so fluid, it is tough to update that guidance and that's why we didn't put in the press release. So it's hard to tell right now. The new supply is not too bad right now in Houston. We've had it in the past. It's actually new supply two years ago was worse than it was in the last 18 months, so from a supply point of view, I think we're going to be alright there. We have to absorb what did come on, but the rates need to come back, we need to reduce specials and we don't see that any time soon.

Q: Thank you.

Operator

Our next questions from the line of Ki Bin Kim with SunTrust Robinson Humphries.

Q: Good morning. So quick one on Life Storage. When I look at your reported numbers on the stable properties, the 72 properties, it looked like occupancy in the first quarter actually dipped down versus Q4 '16. I understand there's always a little bit of seasonal element to this, but also curious to know what happened with that, because I think that would still be increasing with the lower number.

Andy Gregorie – Chief Financial Officer

There's nothing out of the ordinary there. It's a normal January, February, March. We would expect that to now start to coming up nicely. We have a lot of runway in those markets and we would expect those properties now—you'll see as we go through the busy season, they'll start to fill up.

Q: If I look at your proxy and then the board compensation, the two of the founding board members, Bob Attea and Ken Myszka, they were roughly receiving in the past about \$2.5 million of comp. I'm not here to debate the comp number for founders. What I did notice is that for Bob Attea two years ago that that level of payment ceased to a more normal level and for Ken Myszka, 2015 was the last year he got that \$2.5 million comp number. So, I was just curious if you could talk a little bit about what is happening and what caused that?

Dave Rogers – Chief Executive Officer

That was part of a program that we put in place actually three years ago when the guys surrendered their gross ups and some other benefits, and Bob, starting in 2015, went on a three year plan to have his consulting fee paid through the end of 2017, not eligible for bonuses or incentives. Ken started the asset plan similar to that in 2016. So Bob's plan burns off at the end of this year and Ken's burns off at the end of next year, and there's no agreements post that, although they may or may not sit on the board. But essentially they were sunset agreements three years each at \$570,000 per year, '15, '16, '17 for Bob; '16, '17, '18 for Ken.

Q: In terms of where your stock is trading, your NAV is fluid and is always in the eye of the beholder, but it's [indiscernible] about 7%. How does that configure into your plate of options when it comes to capital deployment in terms of when do you start thinking about buying back stock versus, well, I guess you're not going to do many acquisitions, but when does stock repurchases become more realistic?

Second, I know you guys sound pretty excited about Life Storage and the positive aspects of the business that you're seeing, but at what point do you start to think about if it doesn't play out to plan and maybe Life Storage continuously yields lower, and you don't get the kind of big uplift in this big deal that you've done, when does exploring other possible strategic alternatives come into play?

Dave Rogers – Chief Executive Officer

We always have the latter in play and our board is always, we have an annual planning sessions and we're not aware of seeing, we did not plan for this. Let me tell you that. I'll be straight up and say we did not plan for our share price of \$76 or \$75 or whatever it is, but I would hope that would recover, but that's something we're aware of, we know it's part of the game.

The share buybacks we've talked about before. We have something in the range of \$75 million of free cash flow. We did have some one-time uses this year with regard to the rebranding, but we also are deploying, as I said, some \$30 million to E&E's. We have our share of the JV contributions which range anywhere from, I think we have somewhere in the range of \$35 million to \$45 million this year to put in play. So we have use of this year.

At this price it's compelling, but also we are very aware that we get a pretty nice benefit from having a BBB rating on our debt, so we're cognizant of that, that we're not going to overleverage the spend, but the free cash flow and the sale of a couple of properties, we're always looking at the priority of what to do with our deployable cash. And absent a shift in [break in audio] opportunities are not attractive, that's certainly an arrow we have to boost return.

Q: Not to belabor the point, but how are you thinking about the business today? Is this kind of just small, this deceleration in your mind is very temporary and as supply gets absorbed things will get back to normal so there's no real sense of urgency to do anything strategic? It's nowhere near the prices? I'm just trying to get a sense of where's your mental leeway.

Dave Rogers – Chief Executive Officer

As part of the prepared remarks, we talked about what we did with the company in the last couple of years, last year especially. We built an overall owner operator program and we have a lot of places to go. We're really ramped up third party management, we really have the opportunities to use other capital to add to the brand. And we've always talked about this being a scale game and it certainly is, and we're knocking on 700 stores now. It's great. I mean, we can do things that even at 400 we couldn't do. We can do things that 89% of the industry can't do.

So, our tools are here. We have this really nice, tight company with now a resurgent brand that I really do think is going to give a lot of benefit to us not seen today in terms of better customer acceptance across all the platforms – the commercial customers, the small business users, and certainly the residential homeowner. So I think we've built a company now that the headline is always same store sales and we're hurting. It's been 24 quarters of

phenomenal same store growth. We're paying the price in a few markets for perhaps having some customer fatigue and a little bit of, a lot of tough comps.

But this is after 33 years, we're in a really good spot right now and the industry is taking a pause, I think. But we're set to go and grow the next wave.

Q: Thanks, Dave.

Operator

Our next question comes from David Corak with FBR Capital Markets.

Q: Good morning. I apologize if I missed this. But when we were together in February, Andy, I believe you mentioned that the 40% of customers were below Street rates; 8% were at the Street and 52% were above. Obviously there's some seasonality there, but would you mind updating those numbers for us at the end of April and then maybe what that was at the end of April of last year?

Andy Gregorie – Chief Financial Officer

Sure. I actually don't have it at the end of April, I have it at the end of March, which is usually the low point, but we had 46% were below the current Street rate as of the end of March; 46% were above; and 8% were at. Compared to the last Q1 where 59% were below and 32% were above, 8% or 9% were at. So a little bit of a switch there, but still a significant number of our customers are below the current rent. And our average paying customer is below our street rent right now.

Q: Then based on your previous guidance, you guys noted 150 bps or so of revenue growth was going to come from in place customers kind of baked in the guidance that you gave in February. What do you think that number is today? Is it still around 150 bps?

Andy Gregorie – Chief Financial Officer

A little bit less; not much less. That customer is still sticky; very sticky. We only had in the first quarter 11.7% move out, that compared to the last first quarter that was very similar, so the customers are taking those rent increases. A little bit different than looking for new customers with new comps, those current customers are happy with us and their rates we're adjusting them to, they're sticking.

Q: Okay. So tell me if I'm thinking about this right. Let's call it 125 or 150 basis points of the new 2.5% revenue guide is going to be driven by in place, which I guess would mean there's an increased reliance on renewals relative to new leases in your new guidance? Is that true? Then further, it would seem that there's now a higher percentage of your tenants that are, or at least a comparable percentage of your tenants that were above street rates. Is that a fair way to think about it?

Andy Gregorie – Chief Financial Officer

I think it's somewhat fair. I mean, I think overall we expect to have a little more occupancy growth this year from the initial guidance then we think we're going to see now. But otherwise, very similar; 100-125 from the current customer rent increases. Not a whole lot of change there, but a little bit of a change.

Q: Thanks.

Operator

Our next question comes from Gwen Clark with Evercorp ISI.

Q: Good morning. Can you talk about [talking over each other] demand? You mentioned possible renter fatigue. Have you seen any uptick in delinquencies or anything on that front?

Ed Killeen, Chief Operating Officer

No, Gwen, there hasn't been any material change in delinquencies. As a matter of fact, it's been up, for the quarter it was up \$100,000. We don't see, while things are a little bit soft right now, we don't see any evidence of erosion of consumer confidence at all. As a matter of fact, merchandise sales on a per move-in basis are up as well, so people are continuing to not only look for storage, but they're shopping with us as well.

Q: On the marketing front, it looks like you're doing some pretty interesting stuff, both in regards to social media website things. Also, it looks like you may be doing radio advertising? Can you talk about how that has actually affected demand and do you think those efforts are going well?

Ed Killeen, Chief Operating Officer

The social promotion of that content and creating that content, that doesn't necessarily drive click through. What it does is it improves our domain authority, our relevancy. So Google just looks at that type of activity, whether it's creating content through a video content or any social media campaigns or Facebook campaigns, Google just simply recognizes that our company is doing those things and it looks at us as being more relevant. And when you're more relevant, you get a boost in ranking. So it doesn't necessarily translate into click through for move-ins, it translates into greater relevancy, which therefore translates into ranking.

Q: That's helpful. Then just one last thing, on the third party business, can you talk about how you're winning business when competing with your peer group? Do you charge the same fees?

Dave Rogers, Chief Executive Officer

It's a pretty commodity-driven business. There are different ways that different companies capture, for example, insurance premiums, how the insurance programs work, how I pay for some of the upfront capital costs. Part of it has to do with the market you're in, part of it has to do with the relationship building. There are some markets we're probably never going to get into and then there are some that we don't even try to get into. So, I have to say that a big part of our changing our name had to do with inroads to both commercial tenants as well as third party managed prospects. You have to change your name to ours if you're store owner and we just had some resistance on the Uncle Bob's name, but the Life brand has won us some business right out of the chute.

So, it's competitive, there's not only three REITS who play in the game, but there's another half a dozen regional guys who do it as well. But as far as compensation goes, I think most of the packages are pretty similar.

Q: Thank you.

Operator

Our next question comes from George Hoglund with Jeffries.

Q: Good morning. I'm not sure if I missed this earlier, but did you mention what existing customer rent increases are?

Andy Gregorie – Chief Financial Officer

Existing rent increases in Q1, they averaged 9.9%. Q1 is pretty light for the number of customers they get, only 2% of our customers receive those in Q1. Q2 we've already sent out the rent letters and they were double what they were last year. That average increase is 8% to 9%.

Q: Thanks. Also, as far as your discounting is concerned, I guess you're offering it to more customers, but as the actual discounts themselves changed?

Andy Gregorie – Chief Financial Officer

The discounts are still the same. It's one month free, half a month free or waive the administration fee. So there's those three different discounts we could offer. The average discount per move-in, those that receive the discount went up from \$62 up front to \$71 from Q1 of '16 to Q1 of '17. So, I'd say there has been more free rent. There's more full months out there, but the nature of those specials has not changed.

Q: One last one. There's one lease up property in Chattanooga where occupancy went down, actually, year-over-year from 94.5 to 86.5. What was going on with that property?

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That was a comp that opened last June, literally a stone's throw away from us. They have just a multitude of very small spaces. They captured some of the student storage business. We're very close to UTC. Since then, we've made up that occupancy. Our current occupancy at that store is 93%. So what they did is they filled up some of their 5x5's and we continued to chug along, and they took some of that student business for us. But the higher yield customers are the ones that are taking larger spaces, anyway. And it's already happened. It's a non-event.

Q: Thanks. I'll look forward to seeing you guys next week.

Dave Rogers – Chief Executive Officer

George and Jeffries are bringing a team through on an Investor Day next week, in case anybody's interested. We promised George not to have happen what happened to the team from Evercore, Steve and Glenn, and the group that came up. Some got snowbound, unfortunately. But it's May and I think we should be safe. So May 11th should not be a snow day.

Operator

[Operator instructions]. Our next question comes from Todd Stender with Wells Fargo.

Q: Thanks. I just want to look at your underwriting requirements, maybe just to get up to date. You have the Charlotte C of O deal that's under contract. Maybe just how that compares to something you would have underwritten 12 months ago, if you could just share return requirements, lease up expectations, stabilized yields, stuff like that?

Dave Rogers – Chief Executive Officer

I'll let Paul talk to it, but we actually underwrote it more than 12 months ago and there's been some construction delay.

Paul Powell – Chief Investment Officer

Todd, we keep a close eye on this market; it's downtown Charlotte. There's been a lot of new planned competition coming in. So far, based on what we've seen, there's still nothing within a mile. So, we're comfortable with how we underwrote it. We still expect it to lease up in 3, 3.5 years max. So we're still comfortable with our underwriting, and as I mentioned, we don't see any new comp coming in that would change our underwriting model at this point.

Dave Rogers – Chief Executive Officer

I think, Todd, what you might be getting at is how are we underwriting C of O's now?

Q: Yes. What are your yield expectations and how would that change if you underwrote something right now?

Paul Powell, Chief Investment Officer

Right now we're not looking at doing any CO deals, but of course depending on which market it's in, we were looking at 150 basis points over today's stabilized yields, we would probably still look for that if not 175 basis points. So, I haven't really looked at any recently, so we haven't done any modeling at this point.

Dave Rogers – Chief Executive Officer

We do look at some on behalf of JV partners and the spread ask is still pretty wide. I guess that goes for existing properties as well, the spread ask is pretty wide. But the CO stuff was really great three years ago, as we've talked about on other calls where we were looking at for a little while 300 basis point spreads, and our pool of a dozen or so CO properties have shown that. They've leased up very well, they've been great contributors to us.

To do one today with almost any developer, you don't see that and that's why we're sort of on the sidelines with CO deals.

Q: Can you, just switching gears, talk about the JV assets you've acquired? Maybe talk about cap rates, occupancies and just compare LA with Sacramento?

Dave Rogers – Chief Executive Officer

As we did in our press release, we purchased five properties in the first quarter with our JV partners; four of them were in California. Our year one cap rate was in the low 5's that we underwrote. The other one was a new development in Long Island City, so that one's a little bit slow in the initial startup but we think that's going to do well going into the busy season.

We do have three properties under contract still with the JV partner. Two of them are in California and another one is in California as well, San Jose. Then also at this time we are negotiating contracts on another 21 properties for about \$370 million that we hope to sign up in the next few weeks.

Then there's another \$100 million, \$110 million that we're looking at with JV partners as well that we hope to negotiate a PSA over the next month or two.

Q: Are they going to the JV because of growth expectations might not be as high as for wholly-owned stuff or is the cap rates too low? What defines going into those?

Dave Rogers – Chief Executive Officer

I think pretty much our capital position right now and our share price. We are looking for alternative ways to grow the company and to have this many flags with the dollar investment that we're talking about makes it work. We would not be able to bring down certainly a \$300 million deal at this point without – we could, but we'd probably twist our leverage out to a range that we don't want to be. So we're more comfortable at this point and it's like this is more us driven than it has been in the past, but it's basically a way to bring flags into the company without deploying as much capital as we ordinarily do..

Q: Thank you.

Operator

There are no further questions at this time. I'll turn the floor back to you for final remarks.

Dave Rogers – Chief Executive Officer

Thanks, everyone, for your attention to our company and your time. We look forward to seeing you at NAREIT or May 11th. Take care.