Public Storage (PSA) CEO Joe Russell on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-29-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $1.93 beats by $0.02 | Revenue of $729.34M (3.25% Y/Y) misses by $-2.93M

Earning Call Audio

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Public Storage (NYSE:PSA) Q3 2019 Earnings Conference Call October 30, 2019 12:00 PM ET

Company Participants

Ryan Burke - Vice President, Investor Services

Joe Russell - Chief Executive Officer

Tom Boyle - Chief Financial Officer

Conference Call Participants

Shirley Wu - Bank of America

Jeremy Metz - BMO Capital Markets

Smedes Rose - Citi

Todd Thomas - KeyBanc Capital Markets

Steve Sakwa - Evercore ISI.

Ki Bin Kim - SunTrust

Ronald Kamdem - Morgan Stanley

Eric Frankel - Green Street Advisors

Todd Stender - Wells Fargo

Michael Mueller - JPMorgan

Michael Bilerman - Citi

Jon Petersen - Jefferies

Operator

Ladies and gentlemen, thank you for standing by and welcome to the Public Storage Third Quarter 2019 Earnings Conference Call. At this time, all participants lines have been placed in a listen-only mode. [Operator Instructions].

I will now turn the call over to Ryan Burke to begin. Please go ahead.

Ryan Burke

Thank you, Maria. Hello everyone. Thank you for joining us for the third quarter 2019 earnings call. I'm here with Joe Russell and Tom Boyle.

Before we begin, we want to remind you that all statements other than statements of historical fact included on this call are forward-looking statements that are subject to a number of risks and uncertainties that could cause actual results to differ materially from those projected by the statements. These risks and other factors could adversely affect our business and future results that are described in yesterday's earnings release and in our reports filed with the SEC.

All forward-looking statements speak only as of today October 30, 2019. We assume no obligation to update or revise any of these statements whether as a result of new information, future events or otherwise. A reconciliation to GAAP of the non-GAAP financial measures we provide on this call is included in our earnings release. You can find that press release SEC reports and an audio webcast replay of this conference call on our website publicstorage.com. [Operator Instructions]

With that, I'll turn the call over to Joe.

Joe Russell

Thank you, Ryan, and thank you for joining us. We reported our sixth consecutive quarter with same-store revenue growth between 1% and 2%. In the quarter, our expense growth did accelerate as we utilized marketing to drive volume in our busiest move-in season and our non-same-store property saw another good lease-up quarter with 21% NOI growth.

With that, I'd like to open the call for questions.

Question-and-Answer Session

Operator

[Operator Instructions] Our first question comes from the line of Shirley Wu of Bank of America.

Shirley Wu

Hey, good morning guys.

Tom Boyle

Good morning, Shirley.

Joe Russell

Good morning, Shirley.

Shirley Wu

Good morning. So my first question has to do with the marketing expenses. It continues to be up call it almost 70% in 3Q and this has been a few quarters of elevated marketing already. So as you think about these last few quarters and the effectiveness of marketing versus some of your more traditional levers like the rate side, the discounting, how are you thinking about the strategy going forward whether that's in 4Q or into 2020 on the marketing expense?

Tom Boyle

Sure. Thanks, Shirley. This is Tom. I'll take that one. We used similar mix of tools in the third quarter that we have throughout the year. So I won't go into the details on those in particular, but lower move-ins or lower move-in rates and less promotional discounts year-over-year. But speaking directly to advertising, as we've discussed on previous calls, we've been increasing our spend through 2018 and 2019 as we've grown incrementally more confident in the demand response we've received through that channel.

So advertising was up 70% in the quarter. We pulled pretty hard on this lever this quarter in order to get move-ins during the seasonally busy move-in period in July, August and September. We like the returns we've been getting from advertising third quarter included. The incremental move-ins we're achieving for the incremental cost. As marginal returns are attractive, that advertising expense is upfront, while the customer value will be earned over time.

And kind of stepping back Public Storage has real advantages online and we're taking advantage of those first of which is our brand name synonymous with our product, a top search term within the sector almost half of our paid search volume comes in on brand searches which drive efficiencies as well as conversion. And away from paid channels a meaningfully portion of our move-ins come directly to us unpaid about two-thirds.

The second component is scale. We have top market shares in the top metropolitan markets in the United States, which allows for a better richer shopping experience for our customers and good conversion at the local level. So this lever continues to work with occupancy ending up the quarter 70 basis points. We'll continue to plan to use this lever in coming quarters.

Joe Russell

And again just to amplify what Tom's speaking to we clearly, again strategically made the decision in the third quarter to again increase the spend because we're not confused about the fact we have a very challenging and competitive customer environment, but we knew going into the busy season, we could lever and get good traction. And we're pleased by the amount of activity that we were able to drive through this marketing spend.

Occupancy at quarter end was up 70 basis points that sets us up very well to go into Q4 and Q1, where we're not likely to see as much leasing activity. Because again, those are traditionally are lowest volume quarters, but we continue to like as Tom said the value and the traction that we get by putting that level of spend into our marketing efforts.

Shirley Wu

Got it. Thanks for the color. So on the volume side, could you speak to what you were seeing in terms of volume-wise in terms of move-ins and move-outs for 3Q? And also a little bit on the rate side as well for the move-in rates and street rates?

Tom Boyle

Sure. So, hitting the volumes first. So, volumes were for move-ins were roughly flat down 0.8% and move-out volume was down more. So, a consistent trend we've seen year-to-date and really through last year as well. Move-outs were down 1.9%. So, we continue to see a very good performance from our existing tenant base as length of stays have extended and move-outs have declined. So, great stable existing tenant base which is really supported by a solid labor and macro environment.

In terms of rate, I mentioned this a moment ago, our move-in rates were down about 5% for the quarter. So, pretty consistent with what we saw in the second quarter; move-out rates were also down modestly 0.6%. So, all of that's disclosed in the 10-Q.

Shirley Wu

Great. Thank you.

Tom Boyle

Thanks Shirley.

Operator

Our next question comes from the line of Jeremy Metz of BMO Capital Markets.

Jeremy Metz

Joe maybe just to start it'd be great to get your broad view on the state of supply as we sit here today. And as we look across your top markets, some of the weaker ones were expected with supply in back more or less generally there.

As we look across your footprint and the impacts of your own specific portfolio, can you maybe talk about where we're at in the current supply cycle relative to your footprints where they may be peaking and may start to recover next year versus where some markets are still in the heat of that battle?

Joe Russell

Okay. Sure. Again what we've been talking to now, obviously, for some time is the elevated level of supply that's been coming into many markets now for a number of years starting in 2016 when about $2 billion nationally came in to the markets and then that doubled in 2017 to $4 billion; 2018, $5 billion; by all accounts 2019 is going to equal 2018.

And our view of 2020 is we will likely see some decrease in, again, deliveries and it may be anywhere from say 10% to 20%. We're hoping clearly as many others are that it's 20% or even better, but we continue to track markets and statistics that are guiding us to about that, again, 15% to 20% down.

So, you take that into consideration holistically, again, over this time period you've seen anywhere from 1,600 to 2,000 new properties in our markets, that's about 120 million square feet. And again market-to-market particularly where this elevated supplies have we see the most commanding headwinds.

So, maybe more specifically to your question Jeremy so where are we today? On the good news front, deliveries have been elevated in markets like Denver, Charlotte, Houston, Austin, and Chicago. Those have all been poster child markets for these elevated level of deliveries and tougher operating markets, but we're now starting to see that supply volume decrease in some cases pretty dramatically. But we're still dealing with the lingering effects of the amount of supply.

So, you take Denver, for instance, in 2018, a little over 2 million square feet went into that market. The good news is it was less than half of that this year and again; it's going to notch down likely in 2020. But holistically that market has seen about a 35% increase of supply in that time period compared to existing base of assets. So, you've got to continue to maneuver around that elevated level of activity.

Again using markets like Charlotte, Austin, Chicago, and Houston as examples where any one of those markets hit $1 million plus level of deliveries; Houston more extreme. It's a big market no question, but it hit about 2.5 million square feet of completions in 2018. It's ratcheted down and we like the impact of that. But again we're going to have to continue to maneuver around, again, how we're dealing with customer acquisition, pricing, et cetera.

The flip side is we're still not out of the woods because you go back again to our prediction about what's going to happen in 2020 with plus or minus about $4 billion of assets coming into the markets. And we're going to see that impact as we're tracking, and again, these are statistics tied to what's under construction and in development, okay? So, this isn't -- these aren't deals that are planned or potentially contemplated. They're in motion, okay? So, you're going to see more impact in Portland, Boston, Seattle, many parts of Florida, D.C., Minneapolis, and New York. So, we're clearheaded about the things that we're likely to need to do there. We've got a good playbook. We're going to continue to drive a lot of the things that we can to maximize revenue opportunity maximize opportunity in customer acquisition.

The third element, I'll talk to as well is the fact that we do have and we like what we're seeing in our own development pipeline. So we've got about $540 million in today's pipeline. We've shifted out of markets like Texas as a whole for the most part where the last two or three years we put a lot of development activity into both Houston and Dallas to a lesser degree into Austin. But now we are going into a broader number of markets where we're seeing again opportunities to get good traction of these new developments.

And then if you even look at our legacy if you want to call that or the development pipeline that we've delivered since 2013. It continues to lease-up quite well. I mentioned in my opening comment that this quarter we saw about 21% NOI growth in that portfolio. Collectively it's about a $1.4 billion investment and today it's roughly at about 80%. So we like and we'll see very good traction out of that in coming quarters because again we've got more occupancy and we've got the impact of matured revenue opportunities, which again is clearly part of our successful strategy as we again both develop and mature these assets.

Jeremy Metz

And can you just touch on Cali quickly in that context as well?

Joe Russell

Touch on -- I'm sorry what?

Jeremy Metz

Just in the context of where we're at? What kind of -- what are your views on supply for across your California?

Joe Russell

Calling California itself?

Jeremy Metz

Yes.

Joe Russell

So okay. So for the most part California is in very good shape. Now going south to north there's parts of San Diego County we're keeping a close eye on to because there's some elevated deliveries in some of the outer markets within San Diego County.

Orange County and L.A. County for the most part are pretty, I would say inactive from a new development standpoint primarily because there's very little land available and it's very expensive if in fact you're able to find anything here right here in the L.A. metro market may be a little bit more activity out in the Inland Empire.

When you go into the Bay Area again San Francisco -- South San Francisco, again no worries there. A little bit of heavy activity in the San Jose market that we're keeping a close eye on, but again not a big amount of inventory on a percentage of existing base. So we continue to see in our own development pipeline in these markets where we've really had the opportunity to take existing assets for the most part and do some pretty meaningful expansions. And again repeating what I just said around the traction we're getting from that activity the expansions that we're doing are leasing up really well. So we're very pleased by that seeing very good traction and again for the most part I would say California is in pretty good shape.

Jeremy Metz

Appreciate that color. And the second one for me quickly. Just I want to go back to the move-out rates. Tom, you mentioned the 60 basis points here historically or even just looking back to past few years at least you've had a rent roll down which makes sense in the context of rising rents and the in-place bump traction that's now flipped here the past two quarters. So just wondering is that more of a reflection of the overall rents you're bringing customers in at? Or is it a reflection at all in strategy shift and how aggressive you are in pushing in-place rents just given the widening spread to market there?

Tom Boyle

I think it's largely the fact that as folks move-in at lower rates the move-in -- move-outs are coming out at lower rates that's the biggest driver there. No real shifting strategy on existing tenant rate increases. We've talked about modestly lengthening length of stays which has contributed to contribution from existing tenant rate increases, but no real shift in strategy there. So the decrease in Vale rental rates is driven by move-ins coming at lower rates.

Jeremy Metz

Thanks for the time.

Tom Boyle

Thanks, Jeremy.

Operator

Our next question comes from the line of Smedes Rose of Citi.

Smedes Rose

Hi. Thanks. I wanted to ask you in your Q you talk about kind of the appeal essentially of the fifth generation products that are coming to market. And I'm just wondering is there an opportunity to take advantage of what apparently is still very strong pricing for older stabilized assets maybe in your portfolio and redeploy assets in some of the growth markets you talked about earlier with the newer facilities?

Joe Russell

Yes, sure Smedes. So a couple of different areas to talk to there. So first of all, I think, it's well known that one of the benefits of the product type itself is you can go through decades of use on our assets and they can be every bit as vibrant in today's world and even more so in many cases than they were originally developed. So there's very little obsolescence that we're seeing anywhere in the portfolio.

What we're doing though to actually continue to enhance even some of those revenue streams and again amplify performance property to property with some of our older assets is a program we've talked a little bit about which is our property of Tomorrow program where we're going through and putting to your point what we would call fifth-generation attributes into many of these assets where we can again enhance the curve appeal of the asset through more modern paint, scheme signage we're improving the office and customer areas that align with some of the technology issue or technology strategies that we've had. We're at this point going through California from a first-wave standpoint, where we've taken about 125 of our generation one through three or four properties some of which might be say 30 or 40 years old. They're in phenomenal locations. They drive very good occupancy and rent levels, but we're going to hopefully even see that much more opportunity once we've basically taking them – taken them through the various stages of the elements that we would include in our generation brand-new properties.

So that's working quite well. We're getting good reception from both customers and our employees as well. And then, we're also now rolling that program into a number of markets nationally, which will include in the first quarter parts of Florida. We've touched many parts of the boroughs, if not all of those properties we're going to go into other parts of New York. We've already gone into markets like Chicago for instance and the Carolina.

So, anyway we're pretty excited about what we're doing. Now, from a cost standpoint we've talked about this program in the context of ultimately being about $0.5 billion or more once we get through the entire portfolio. 2019 we will have spent about $110 million on the program. And in 2020, we'll likely spend even a little bit more. Again, as we touch the markets I talked to.

So far we're very pleased. Now, as we're doing this we're also making some technological updates to the properties, where as we speak relighting interior LEDs on assets for both energy efficiency, and again better customer environments. We have begun changing out our access control systems which is now based on a centralized system which we've never had before. It's going to give us a lot of good data that we haven't had around customer activity. We're adding solar to a number of properties. So we've got a number of different elements of the overall program in motion. And like I mentioned we're getting very good feedback from it and like the results.

Smedes Rose

Great. And then I just wanted to ask you too you – last quarter you mentioned that the third-party management platform was largely geared to predevelopment and in development properties. Just given what looks like a continued kind of deceleration in trends across multiple markets is there an opportunity to bring on or convert more independence I guess more aggressively to your platform? Or is that your strategy, there is to -

Joe Russell

Again, we're seeing our pipeline definitely continue to build. The pipeline is dominated by assets that are in various stages of development. That's pretty typical for again this kind of a platform again from what the industry as a whole has seen. We have however also seen some opportunities to bring more stabilized assets into the program too. And again, a number of owners are clearly interested and are anxious to come into our platform because they like and see the amount of revenue generation that we can provide to them based on all the metrics that we're able to again weave into their assets whether again it's purely based on our brand the optimization that we get through, search, our marketing efforts the scale that we've got in markets. So again, it's a program we're pleased relative to the momentum that we've got in it. We signed in the quarter 13 additional assets. So today, we've got about 75 properties in the program. And as I mentioned, the backlog continues to build.

Smedes Rose

Great. Thank you.

Operator

Our next question comes from the line of Todd Thomas of KeyBanc Capital Markets.

Todd Thomas

Hi. Thanks. Thanks for the comments on supply. Just wanted to follow-up on that and on rates. Tom you mentioned move-in rents were down 5% in the quarter. They've been down since late 2017 and the decrease in move-in rent seems to be increasing a bit here. As you think about where we are in the cycle with regards to supply and the absorption of new supply that's taking place across the industry it sounds like you're still seeing some good traction on the occupancy side, but where do you think we are in the process of seeing asking rents adjust any thoughts on that?

Tom Boyle

Yeah. I do think if you go back several years, we've had a consistent trend of using move-in rate in order to drive volume. It really is a market-by-market dynamic. So, as we think about where it's going in future years a lot of it will be dependent on what happens in those markets. So just looking at move-in rates for the third quarter for example, you have markets like Los Angeles or Phoenix, where you're up call it low to mid-single digits on move-in rates given what's going on there. The flip side is, you've got Florida markets like Miami and Tampa, which are being impacted by new supply and those move-in rates are down call it 5% to 10%.

I throw Houston into that bucket as well. And so the move-in rates we're using are not across the board, it's really a tactic to drive volume in areas where we're competing for new customers in a more competitive environment. As we move into – to 2020, we're likely to see the mix of those markets continue to shift. So as we've spoken about in the past looking back at the markets that were more challenged in prior year, we've seen some of those markets actually improve meaningfully to a market like Chicago or Washington D.C. that was maybe more impacted earlier on in the cycle, is seeing better traction this year than they were last year.

As we head into 2020, it's going to be a different mix of markets. But I think I'll let Joe speak to new supply in aggregate by market, but it's a pretty dynamic management on our end as we seek to maximize revenue within those local submarkets.

Todd Thomas

Okay. And then I realize you send out far fewer rent increase letters, I suppose into the off-peak leasing season. But does the current environment that you're experiencing here in the market, does it cause you to consider using up a little bit on the number of customers that you might be sending letters to or the rate at which you might push? And also can you remind us whether there is sort of a governor in place around how much of a percent above Street you'll increase existing customers' rates?

Tom Boyle

Sure. So strategy-wise we plan on using consistent plans through the fourth and next year's first quarter in the slow season. So, we do send rental rate increases throughout the year, and we'll do so in the coming quarters.

In terms of the magnitude and the quantity, we're looking to optimize that at the tenant level. We think we do better on that year in and year out. So, ultimately what we're seeking to do is maximize revenue. So we take into consideration the probabilities of vacates as well as the cost of that vacate and replacing that tenant, et cetera.

So, things vary throughout the year, but consistent strategies and no change or more conservatism or more aggressiveness as we get into the next few quarters.

In terms of a governor, there are things in place that we use in order to make sure that we are maximizing that revenue over time. And so there's different governors in place and different strategies, we use in different types of environments. But certainly, Street rate and the rate with which a new customer would move-in is the key component of the strategy. So, as tenants get higher above Street rate the cost of that tenant leaving is higher.

Todd Thomas

Okay. That's helpful. Thank you.

Operator

Our next question comes from the line of Steve Sakwa of Evercore ISI.

Steve Sakwa

Thanks. Yes, good morning out there. First question I guess is just in terms of the sort of the monthly trends you saw in the third quarter, was there anything noticeable as it relates to kind of the same-store revenue trend that realized occupancy ended kind of on a strong note at the end of the period and average occupancy was up 40%? And I'm just curious kind of how things trended throughout the quarter.

Tom Boyle

Sure. So in terms of the operating trends through the quarterly, we actually did see improving trends from July through September. We did do some things in September that aided that including our typical Labor Day sale that we extended a bit this year to drive traffic, and ultimately we like that from a revenue standpoint both in the quarter as well as moving forward. So, we did see a modestly improving trends through the quarter from July through September, and as we head into October, generally consistent trend. So nothing really to speak to other than…

Steve Sakwa

Okay. And I realize you guys don't provide guidance, but historically kind of the guidepost for revenue growth has been to kind of look at that annual contract rent per foot and sort of look at the average occupancy and the end of period occupancy. And for the third quarter that kind of gave you a range of 1.3% to 1.6% and that the actual number came in a little bit below that. And as you look at the fourth quarter it's kind of penciling in for call it 50 -- excuse me, 50 basis points to about 80 basis points, which would be sort of further slowdown. Is there something we're sort of should be thinking about as we head into Q4 and into next year?

Joe Russell

No. Steve what I would point you to that those are metrics that we think create guidelines. I mean, there can obviously be some variation in and out of different conditions. But at the end of the day, they're relatively within the zone. And what I would point to as well, Tom mentioned that through October, we've seen consistent occupancy impact. And again, that's intentional meaning we saw that in the quarter 70% or 70 basis point increase.

And at the moment, it's in about that same zone. So it ties to the strategic things that we're continuing to do. And again, a tough acquisition -- customer acquisition environment to do something that others may be don't have the same capabilities do which is really still in this environment lift occupancy with a broader intent of that ultimately gives us many things we like around revenue generation. So, we're continuing to do that. And I think we've set the stage for Q4 pretty well as we intended to do.

Steve Sakwa

Okay. And I guess just lastly on the marketing expense, is there any way to sort of just help separate kind of the actual cost per click or the actual cost from kind of the Google search versus kind of the increased usage of the Google search and sort of search paid advertising type stuff. So I'm just trying to sort of disaggregate the pricing increases versus I guess volume of usage?

Tom Boyle

Sure. I would -- without getting into specifics around keyword bid strategies or otherwise, I would say it's a good mix of both increased cost per click as well as increased bids to drive volume. So a good mix of both.

Steve Sakwa

Okay. Thanks. That's it for me.

Tom Boyle

Thank you.

Operator

Our next question comes from the line of Ki Bin Kim of SunTrust.

Ki Bin Kim

Just wanted to follow-up on Steve's questions. First on the expense. This elevated level is obviously purposeful, shouldn't be a surprise. I'm curious though, as we head into next year, as we comp these higher numbers, is this the new norm and we should expect increases from here this level on up? Or is this level just kind of artificially high because it's part of a unique -- part of the strategy for today that might normalize lower going forward?

Tom Boyle

Sure. So Ki Bin I think there's a couple of things I'd highlight. One is clearly we pulled on this lever pretty hard in the third quarter and just spoke to some of the strategy thinking behind it from a revenue standpoint. But I think stepping back it's managed very much dynamically at the local keyword level. And so, as we monitor what the returns are, we're going to oscillate our strategies thereafter. So we can't predict exactly what's going to happen going forward.

I would kind of step back in terms of advertising spend and you think about where we are and what we're battling from a customer acquisition standpoint and just provide a little historical context.

So if you go back in time advertising as a percentage of revenue for Public Storage, at the end of the last cycle beginning of the cycle hover between call it 2% and 3% of revenue. As the customer acquisition environment, got very healthy and certainly fundamentals were very solid in the beginning and middle part of this cycle, we decreased our advertising spend. In 2016, for example, advertising spend was just a touch over 1% of revenue in the same-store pool.

We're looking now year-to-date it's hovering just under 2%. So it gives you some context that yes, while we've been increasing marketing spend, we've been doing so from a low base in what was a very attractive customer acquisition environment in 2014, 2015, 2016. And now we're in a certainly a more challenging and competitive environment and we're using that tool like we have in the past to drive new move-ins and occupancy.

Ki Bin Kim

Okay. That's helpful. And going back to the revenue question and Street rates. So this quarter your move-in rates were down 5.3%. You extended the Labor Day sale a little bit longer. You got the occupancy gains that you're looking for with lower rates and higher advertising.

So I'm just curious, if you're setting yourself up for same-store revenue growth to potentially reaccelerate in the fourth quarter? Because maybe your -- the customers you've drawn into your company are paying that 50% off rate. Some will move-out, some will stay and they'll get the higher rent. Maybe the occupancy isn't cash flowing day one. So maybe there's some built-in gains to recapture in the fourth quarter. I know that's a big question but it just maybe feels like 4Q might look better than 3Q?

Tom Boyle

So Ki Bin maybe what I'd say is, we obviously like the strategies we used in the third quarter. Some of them have short-term impacts. Certainly, we're looking to manage medium- to longer-term revenue and ultimate customer lifetime value through that lifetime.

In terms of whether where we're accelerating or decelerating, we continue to face real challenges from an operating standpoint, particularly on move-ins in many of our supply impacted markets, that's not going to change as we get into the fourth quarter and we continue to see that through October.

You're looking at certain markets that have been more challenging and you look at markets like Atlanta for example that has had a more challenging third quarter and into the fourth quarter. And we're going to continue to see markets like that that will be a drag on both move-in volumes as well as revenues we get into the fourth quarter.

Ki Bin Kim

Okay. Thank you.

Operator

[Operator Instructions] Our next question comes from the line of Ronald Kamdem of Morgan Stanley.

Ronald Kamdem

Hey, two quick ones for me. First is just you sort of did a good job laying out some of the markets that you mentioned or maybe seeing elevated supply. Just out of -- do you have a sense of -- when I think about private equity and private capital investors, has the appetite for the product from their standpoint changed at all? Or is it still pretty attractive sort of asset class even in those markets that may have had maybe too much supplier early on in the cycle?

Joe Russell

Yes, Ronald, I think again that investor type continues to look at self-storage as a product in very positive terms. We're seeing more entrants either come into or basically kind of scout the industry in a variety of different ways where we're seeing again that type of investment vehicles come in to a variety of different markets. More often than not they're looking for scale, which can be challenging from time to time. Cap rates really haven't adjusted for the most part, but yes there's definitely a fair amount of capital that still wants to come into the market. And some of those buyers maybe thinking in terms that I would say, could be somewhat risky because they may be basing it off of proformas that may or may not make sense.

May be based on levels of traction that were seeing one or two years ago that have certainly continued to change. So it's a new and different dynamic that's come into the sector. And by all accounts we don't see that shifting anytime soon.

Ronald Kamdem

Great. My second question, I think on previous calls you sort of mentioned that sort of the acquisition opportunity maybe had increased. I think you mentioned buying some assets off of auction. Just maybe can you give an update on that? Is that something you seeing? And what does that mean for potential acquisition volumes next year? Is this something we could see ramp significantly?

Joe Russell

Sure. So again statistically obviously you can see -- again through, what we've done in the third quarter and then what we've got in our pipeline and whether we've already closed or under contract for the fourth quarter. We're likely to acquire plus or minus about $375 million of assets this year. And that's 2x of what we did from our acquisition volume in 2018 for instance.

And as I've talked to in the last couple of quarters, we do see more and more owners coming to us in a variety of different stages whether they've already built assets. They may be in the first year or two of lease-up. They're not making either pro formas or revenue projections and they've got some level of -- I would call it anxiety. I wouldn't call it pronounced flat-out stress at this point, but there's definitely more anxiety-related conversations that we're having.

By virtue of that we're seeing sellers being far more reasonable around valuations. That's clearly what has led to some of the acquisition volume that we've already done this year and continue to see come our way. We've been able to capture some really nice assets in a number of markets that we wanted to build scale into. And we're anticipating that there is more of that to come.

And the other factor that I would tell you that is starting to percolate a bit more than we've seen recently is even what I would call, entitled land, whether an owner again may have acquired a piece of property 1, 2 or 3 years ago. Again anticipating proformas that they felt confident about 1 2 or 3 years ago, clearly things have shifted. They're reassessing their own development returns and we're seeing more opportunities to actually engage and particularly -- and potentially find some interesting opportunities there.

Ronald Kamdem

Helpful. Thank you.

Joe Russell

You bet.

Operator

Our next question comes from the line of Eric Frankel of Green Street Advisors.

Eric Frankel

Thank you. I don't want to beat the marketing expense issue to death, but I would like to maybe to better understand the rise in the cost per click phenomenon. Is that just related to just larger more overall supply and some more competitiveness on the market that's causing people to be more aggressive marketing space? Is it valet storage? Is it something else? What do you think is the issue? Or is it something -- or is it just a monopoly practice of search?

Tom Boyle

No. I think it's a good mix of a lot of the factors you highlighted. It's a combination of your traditional operators being willing to spend more to acquire more customers. As we've increased our spend, we've seen incremental volume and I suspect others have as well.

And so there's a component of your existing folks being more competitive. Certainly the Google platform is a great one and the fact that its action based. So they let us compete within their sandbox. And so the environment is more competitive and you see folks being more aggressive in their cost per click.

There are also not only your big public REITs, but also your regional operators that have been more aggressive as well as some of your nontraditional storage folks like valet for instance with some of those operators have been more aggressive in cost per click as well.

So that all adds to a higher cost per click environment which as we look at our spend that's a component of it. But then we need to again at the local level do we like the bids and the volumes that we're seeing? What do we get if we increase? What do we get if we decrease? And that's what we're managing.

And ultimately as I spoke earlier, we like the returns. We'll see whether the rest of the environment and the rest of our competitors like the returns as cost per click continue to go higher, but we like what we're seeing.

Eric Frankel

Okay. Just another quick follow-up regarding I guess, the valet storage. It's obviously quite a new initiative that UPS announced their -- an initial foray into sort of a valet storage business. Do you have any thoughts on how that might impact the self-storage industry going forward, if that model is to expand that model?

Joe Russell

Yeah, Eric definitely an interesting announcement. And we've tracked. We've experimented. We've done a variety of different customer surveys around this whole concept of valet on-demand type platform. And thus far we continue to see very little disruption and/or change in our own customer behavior, because we continue to see pretty distinct differences between what that product offering is compared to what traditional self-storage is.

So the one thing that UPS, obviously, has that others prior have not is more of a logistical network. The platform right now is based on a bin concept. So not clearly understanding what way it might evolve over time. They're testing it out in one market. So we're going to continue to watch and understand as we have with the other platforms.

But overall the whole valet model, we continue to see as one that might be more akin to a traditional moving and storage type customer versus a traditional self-storage customer. A big difference to a self-storage model is you literally pay for access each and every time you want your goods. And then at the end of the day, you don't even know where they are.

So those are two pretty big hurdles relative to what, again a core self-storage customer traditionally wants, which is access and basically again knowing that they can again get to their goods without having to pay fees to do so. So we'll continue to track it and see what evolves.

Eric Frankel

Okay. Thank you.

Joe Russell

You bet.

Operator

Our next question comes from the line of Todd Stender of Wells Fargo.

Todd Stender

Hi, thanks. Just back to the elevated marketing spend, it definitely tipped into negative same-store NOI territory, it's hitting the stock today as you know. But just wanted to get a sense of where you guys are thinking about guidance, maybe just for some key metrics to set the right expectations? Obviously, you're not running your business on a quarterly basis it's for the long-term. But when you get an outsized expense item like this that pops up that does contribute to you guys trending negative, just wanted to get a sense of maybe setting the right expectations going forward?

Tom Boyle

Sure. So you're right, we don't provide guidance and we don't manage for the short-term and we've talked about how we thought about the advertising spend for the quarter. In terms of line by line expectations for expense growth, I would point you to our 10-Q particularly in the MD&A, where we do walk through what the trends are within each of those items. I won't go through it in detail because, obviously, the folks on the phone can go through and read it.

But I think the expense pressures generally continue to mount be it property taxes, property level payroll and the like. So even away from marketing expenses, there's no question that operating expenses have been more under pressure this year and we think that's likely to continue for many of those line items. But I'd point you to 10-Q in terms of some guidance as to where we're headed.

Todd Stender

Got it. Thank you.

Tom Boyle

Thank you.

Operator

Our next question comes from the line of Michael Mueller of JPMorgan.

Michael Mueller

Yeah, hi. Just going back to the other topic of rent growth and realized rent growth. I mean, what I guess was different in Q3 compared to Q2? Because if we look at the prior quarter going from Q1 to Q2, we saw a pickup in the growth rate. We saw a pickup in REVPAF as well, but then it ended up even with the marketing spend coming in maybe a little bit better than half of what the Q2 was. So I guess was there anything abnormal in hindsight that you see in that Q2 print? Or was there something abnormal and what appears to be the -- in print the Q3 levels of -- with a 0.7% realized rent growth and 1.1% REVPAF growth?

Tom Boyle

Sure. I wouldn't point to anything in particular. As you move through the second quarter and into the third quarter, the busy season with lower move-in rates that is a big drag through those quarters on contract rent growth. And you've seen that this year, you've seen it in previous years as well. So there's nothing really new there.

Maybe pointing to one factor that maybe made in the second quarter a little bit better and the third quarter maybe a little bit worse if you look at discount trends for example, which are a component of revenue, discounts were down almost 7% in the second quarter were down, about 4% in the third quarter.

So there's lots of moving pieces there, but generally if you look back while we've been battling this new supply between second quarter and third quarter, we've seen contract rent growth decelerate over that time period pretty simply because we've been using lower rates in many of our markets in order to drive that volume as those folks move in during the summer that contract rent growth declined.

Michael Mueller

Got it. That’s helpful. Okay, thank you.

Tom Boyle

Thank you, Mike.

Operator

Our next question comes from the line of Smedes Rose of Citi.

Michael Bilerman

Hey. It’s Michael Bilerman on Smedes. Last couple of years you've tapped the unsecured debt market, right? So you're sitting on about $1.5 billion of U.S. unsecured and you've put some capital out in Europe from a natural hedge for your stake in Shurgard as well. Sort of curious what your appetite today is to take in additional debt? I know you redeemed the preferred and reissued, but I didn't know if there was an appetite given how low rates are to raise that capital?

Tom Boyle

Sure. Thanks, Michael. I think as we've talked about in the past, we do have appetite to add incremental debt as well as incremental preferred as we have uses of capital. So, so far this year, we've issued over $1 billion of capital. As you've highlighted, our preferred activity is largely been to refinance existing preferreds, and we're hopeful we have the opportunity to continue to do that. As we move through the fourth quarter, there's a series that becomes callable in the fourth quarter.

But stepping back from a strategy standpoint, we plan on using both unsecured debt, which we can get attractive rates to your point, as well as preferred stock which is a higher cost. But historically speaking right now is offering a very historically attractive coupons, sub-5% is what we achieved in September. So, we like both markets and we plan on using both going forward.

Michael Bilerman

I guess is there an appetite to maybe take advantage of the spreads you can get to increase cash flow when your operating fundamentals are a little bit weaker, right? So, take advantage of being able to lock in 10, 20 or even 30 year paper refinancing preferreds capture 250 basis points of positive spread and at least help offset some of the dilution from a weaker core portfolio?

Tom Boyle

Sure. So, we have been reducing the cost of our preferred portfolio by refinancing it. We like the $4 billion of preferred we have outstanding. We think it's a very good source of permanent capital. Taking what you said to the extreme, we could use the revolver and redeem some preferreds. But from our standpoint, we like that permanent capital in the stack. We will seek to refinance it to better rates. And going forward, in order to fund acquisition and development activity, we will be using both debt as we did earlier in the year as well as preferred.

Michael Bilerman

And then, just going back to the Vale discussion, it's a mix basis combination with Iron Mountain from a strategic perspective gave them the distribution and logistics network that others didn't have before. Have you seen any impact at all, as they've gone deeper into a lot of the markets you're in?

Joe Russell

Yeah. Michael, I wouldn't say we've seen anything pronounced and different. It still goes back to the way I characterize the product as a whole. So again, we've seen very little disruption and again change in -- again the core customer that continues to look for all the benefits of a self-storage product. So, we're going to continue to monitor and see what comes from any of these realignments that are going on. It's interesting that Clutter actually went in a different direction and actually bought hard assets, which is very different even from a traditional Vale model. So again, there seems to be a lot of movement in that space as a whole and we'll continue to see what evolves from it.

Michael Bilerman

And then, sorry, my last one just -- and I recognize there's a lot of fires going on within California right now. And I do hope all of your friends, family and coworkers are safe. Disaster unfortunately is one of the drivers of your demand. Is there any sort of thought in terms of what this could be doing, A, from just perhaps a lack of demand because maybe your facilities are closed and there is no power? And then does it drive anything else given California is your largest market?

Joe Russell

Yeah. Again, we're obviously keeping a close eye on this and I appreciate the good wishes because yeah, there's a lot of stress in some of the areas both northern and southern California with the fire season that we have at hand. But at the moment, we haven't seen any direct impact to our own portfolio. And what can be unusual with fire events is traditionally they in themselves really don't create a lot of elevated activity. So obviously, it's always dependent upon where the specific fires are. And to what degree -- what comes with it.

They seem to be like-for-like very different events. And say a hurricane, where we see a lot more, broader disruption or impact to a particular market. But we're keeping our fingers crossed that California can get through this, in a good way. But it's -- there's a lot of stress out there.

Michael Bilerman

Yeah. Thanks for the time.

Tom Boyle

Sure. Thanks, Michael.

Operator

Our last question will come from the line of Jon Petersen of Jefferies.

Jon Petersen

Great, thanks. But I make it good one. So you've got a like a few public players out there that do that lend to some of the other self-storage owners. I'm wondering, if that's something you guys have considered doing possibly as a way to grow your third-party management business to leverage your cost of capital, and just given your position in the industry?

Joe Russell

Yeah, Jon, I wouldn't tell you that's an intentional focus point of ours right now. There is a lot of capital that's in the space at large. So we are going to continue to be more focused on growing our own portfolio through our own direct investments et cetera.

And really haven't tapped into kind of a lending arm. And you see far more different things that we can continue with our balance sheet.

Jon Petersen

Okay, got it. Thank you.

Joe Russell

Thank you.

Operator

And that was our final question. I'd like to turn the floor back over to management for any additional or closing remarks.

Ryan Burke

Thanks Maria. Thanks to all of you for joining us today. Look forward to seeing many of you in a couple of weeks.

Operator

Thank you. Ladies and gentlemen, this does conclude today's conference call. You may now disconnect.