DOLLAR STORES

CREDIT RATINGS:
DOLLAR GENERAL: BBB
DOLLAR TREE / FAMILY DOLLAR: BB+

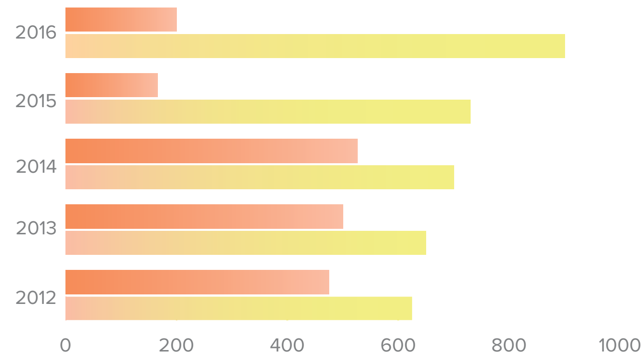
Historically, Dollar General, Family Dollar, and Dollar Tree have been the largest players in the dollar store sector. Since the recession, sales and profits have been on the rise, which has led to tenants incorporating new product mixes into their inventory and a large push to open new locations and expand into new markets.

With new store openings growing at such a rapid pace, there has been a tremendous increase in the number of dollar store transactions each year. Along with the increased transaction volume, we have also observed a strong decrease in cap rates for dollar store sales. While Family Dollar cap rates continue to fall, largely due to their superior lease structure, Dollar General cap rates are actually beginning to rise.

Both Dollar General and Family Dollar have plans to continue opening hundreds, and in Dollar General's case, 1,000 new stores in 2017.

NEW STORE OPENINGS

In terms of new construction stores, the dollar store sector has been the fastest growing. Dollar General has led the charge, opening more than 600 stores each year since 2011, with plans for 900 new locations in 2016 and 1,000 more in 2017. In addition, Dollar General announced plans for 80 new smaller format (6,000 SF) stores which will be focused on densely populated metro markets. In late July, Dollar General announced that it had completed the acquisition of 41 Walmart Express stores, in which they will operate fuel stations at 37 of the locations.

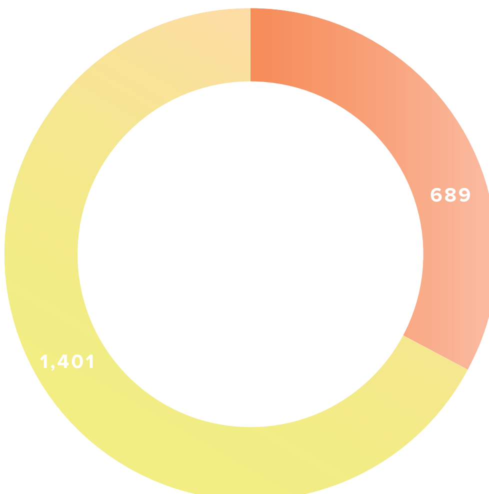


NEW STORE OPENINGS

Family Dollar was not far behind rival Dollar General, opening 500 stores in 2013. Expansion plans slowed drastically with a disappointing second quarter in 2014; which led to news that the company would be shuttering approximately 400 stores. Later that year, Dollar Tree and Dollar General had begun the battle over the acquisition of Family Dollar, which led to more uncertainty and a further halt on expansion. In 2015, Family Dollar opened 166 new stores and plans for approximately 200 new sites this year.

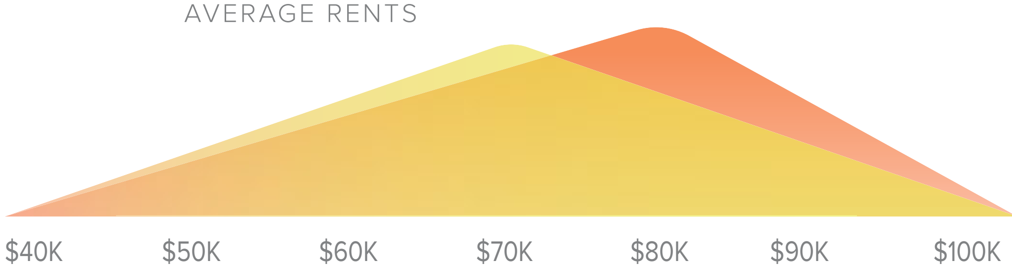
TOTAL TRANSACTIONS

With more than 2,000 stores built over the past 3 years, it would only make sense that Dollar General properties trade more frequently than Family Dollar. In fact, with an estimated 1,400 Dollar General properties sold over the past 3 years, that number is more than double the amount of Family Dollar sites sold.



OF TOTAL TRANSACTIONS
IN THE LAST 3 YRS

AVERAGE RENTS



AVERAGE RENTS

The average rent for a Dollar General has historically been lower than Family Dollar, with an average over the last 3-years of ± $98,500. It comes as no surprise that the rent at new Family Dollar sites are slightly higher, with a 3-year average of ± $109,800. Dollar General's expansion strategy has targeted mostly rural or tertiary markets, while Family Dollars plans include more densely populated urban markets where land values and construction costs are typically higher.

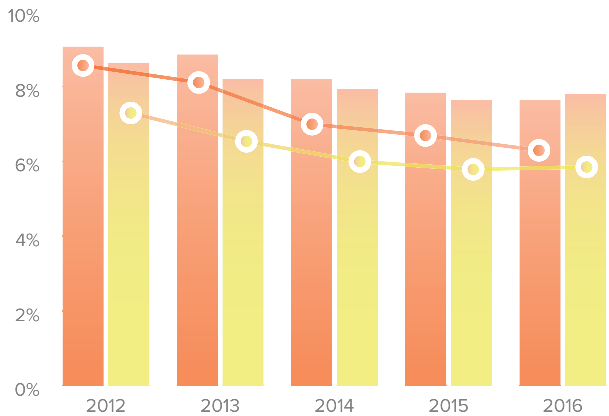
AVERAGE CAP RATES

From 2000 – 2010, both Dollar General and Family Dollar had very similar lease structures; 10-year base terms, on a NN lease. The only difference between the two were a few nuances in regards to landlord CAM responsibilities. Over the past 5 years, their lease structures began to differ in many aspects, directly effecting the sales caps for the two tenants.

Around 2012, Dollar General started signing 15-year, absolute NNN leases, which led to a compression of cap rates. Over the past 3 years, Dollar General cap rates have stayed fairly consistent at the low-to-mid 6% range.

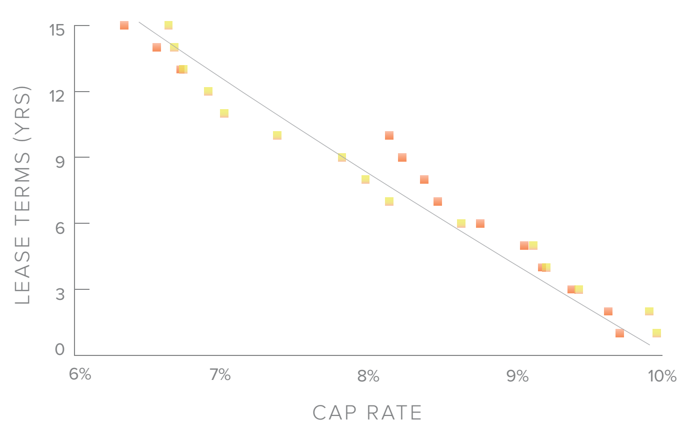
While Dollar General was signing longer term, NNN leases, Family Dollar continued signing 10-year, NN leases. It wasn't until the later part of 2014 that Family Dollar started signing 15-year, NNN leases like their rival Dollar General. New Family Dollar leases have one very important aspect that the Dollar General leases are lacking: rent increases. With their new lease structure and tendencies to locate in more urban markets, Family Dollar cap rates have sunk drastically over the past year . In 2016, the average cap rate on a new construction Family Dollar sale has been 6.30%, with many of the stores trading sub 6%.

AVERAGE CAP RATES



* BARS REPRESENT AVG CAP RATES
* LINES REPRESENTS AVG CAP RATES FOR NEW CONSTRUCTION

CAP RATE CORRELATION



CAP RATE CORRELATION

The data shows a steady decrease in cap rates for both Dollar General and Family Dollar since 2011, with Dollar General caps starting to taper off over the past couple years. As previously discussed, the average cap rates for Dollar General sales have been historically lower than those of Family Dollar sales. One of the major factors is that Dollar General has generally been considered the stronger tenant, due to their strong financial performance, in addition to the more favorable lease structure. Over the past year we have witnessed cap rates for Family Dollar sales drop below those of Dollar General sales, which is directly correlated to their new lease structure that incorporates rent increases in the base term.

One important thing to note is that it is impossible to analyze the correlation between a 15-year NNN dollar store versus a 5-year NNN dollar store, because a 5-year NNN dollar store does not yet exist. The first NNN dollar store was opened in late 2010 to early 2011, which means the shortest lease term on a NNN dollar store is approximately 9 – 10 years. It will be interesting to see this correlation down the road, but one would assume it will be similar to that of Advance Auto Parts because of their similar lease structure and credit rating.

When looking at the correlation between a 10-year NN dollar store versus a 5-year NN dollar store, the spread is more comparable to a similar national tenant, such as Advance Auto Parts. A 10-year NN dollar store typically trades in the low-to-mid 7% cap rate range, while a 5-year NN dollar store typically trades 100-150 bps higher.

Data source: Costar & Real Capital Analytics
*All 2016 data is year to date

FUTURE OUTLOOK

Both Dollar General and Family Dollar have their greatest presence on the East Coast with a large concentration of stores located in the Southeast. While both tenants have started their expansion westward, there is a massive opportunity for growth into the Pacific Northwest, which Dollar General is already looking to capitalize on by opening stores in Oregon and Northern California.

The outlook on the dollar store sector remains stable for the foreseeable future. Average cap rates are trading in the mid-to-low 6% cap rate range for both tenants. Family Dollar properties are trading at historic lows, with many of the well located sites in major MSAs trading sub 6%. It is likely to see a slight increase in cap rates for Dollar General properties for a variety of reasons. The first and most obvious is supply and demand, Dollar General plans to open 900 new locations this year (nearly 2.50 new stores per day) while the demand for these assets remains stagnant. Second, many investors are flocking to Family Dollar properties for their 1031 exchange. The shift is largely due to the fact that Family Dollar is targeting more desirable urban locations and has incorporated rent increase into their new lease structure. It is no secret that rent increases are the only way to hedge against inflation and offset a rise in cap rates in the retail world, that being said, investors are favoring Family Dollar's new lease structure over the flat 15-year lease of their rival Dollar General.

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