INVESTMENT REPORT

OKLAHOMA CITY, OKLAHOMA WAL-MART

USF&G REALTY ADVISORS, INC.
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February 20, 1991

WAL-MART
OKLAHOMA CITY, OKLAHOMA

TABLE OF CONTENTS

TABLE OF EXHIBITS

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TO: USF&G Real Estate Policy Committee

FROM: Craig K. Leonard

DATE: February 26, 1991

RE: Wal-Mart Expansion
Oklahoma City, Oklahoma

I. INTRODUCTION

Enclosed for your review is an Investment Summary of the proposed expansion of the Oklahoma City, Oklahoma Wal-Mart. Wal-Mart will expand the existing 62,990 square foot store by 23,665 square feet, increasing the total store area to 86,655 square feet. USF&G will fund $1,700,000 for the expansion and Wal-Mart will increase its base rent from $255,528 to $430,628 per year. The increased rent will generate a 29 percent internal rate of return over five years on the incremental investment of $1,700,000.

Wal-Mart has concluded that the existing property is too small for its growing sales volume, and expansion is essential. Wal-Mart originally intended to finance its own expansion but, because additional land is required, Wal-Mart cannot expand without USF&G's participation. Wal-Mart will move if USF&G declines to fund; however, because Wal-Mart prefers its current location, Advisors was able to negotiate very favorable lease amendment terms. If Wal-Mart vacates the store, it is required under the lease to continue paying the base rent of $255,528 per year, but it will cease paying any percentage rent which is tied to annual sales growth. This proposal allows USF&G to protect its current investment and enhance its overall yield.

Construction of the proposed expansion is scheduled to begin in March with final certificate of occupancy and funding to occur by November 1991. The store will remain open and in full operation during the expansion. The proposed lease modifications are summarized in Exhibit I-1.

II. THE PROPERTY

A. LOCATION

Oklahoma City is the state capital and is located in the center of Oklahoma. The property is east of Bethany and six miles west of the capital building. The property is in the center of 15 square mile area bounded by Interstate 270 to the south, Interstate 44 to the east, the 39th Street expressway to the north and Lake Overhouser to the west. (See City Map attached as Exhibit II-1.)

B. ACCESS AND NEIGHBORHOOD

The property in on the southwest corner of N.W. 23rd street and McArthur Boulevard and has frontage on both roads. There are three out-parcels along N.W. 23rd Street that are leased to fast food restaurants. A Baptist church borders the west side of the property. Wal-Mart holds an option from the church to purchase approximately one acre of land needed for the expansion. The Shamrock Hills Christian Church borders the property to the south.

C. THE SITE

The existing site is 7.03 acres. As part of the expansion, Wal-Mart will purchase an additional one-acre parcel from the neighboring Baptist church.

D. IMPROVEMENTS

The expanded Wal-Mart will be an 86,655 square foot, single story, slab on grade, block building with structural steel support. The expansion will add 74 feet of depth to the rectangular store along the 300-foot rear wall. The expansion will also include an enclosed 1,465 square foot loading dock on the north side of the store.

The interior of the building will be remodeled, and will be divided between the front retail area and the back warehouse and office area. The retail area will have a combination of vinyl tile and commercial grade carpet floor covering, and a suspended acoustical tile ceiling with fluorescent lighting. The store will be fully sprinklered. The warehouse area will have an exposed concrete floor and unfinished block walls. The offices, rest rooms, and employee break room will have vinyl tile floors and a combination of painted block and drywall partitions.

E. SOURCES AND USES OF FUNDS

Total project costs are estimated to be $1,700,000, or $71.84 per square foot. Direct construction costs are $950,000 or $40.14 per square foot. Land costs are $200,000, demolition and costs related to the protection of the existing store are $250,000, and indirect costs are $300,000.

The source of funds is USF&G's equity contribution of $1,700,000. (See Sources and uses of Funds attached as Exhibit II-2.)

III. <u>MARKET OVERVIEW</u>

A. OKLAHOMA CITY

Oklahoma City, population 434,000, is part of a Metropolitan Statistical Area (MSA) that includes six counties surrounding the city. The strength of the metropolitan area's economy is dependent on the performance of a diverse group of industries, including; aviation, agriculture, energy, government, manufacturing, distribution, transportation, recreation, higher education, and medical research.

The rapid escalation in the price of crude oil in the 1970's caused unprecedented growth in the energy sector. From 1975 to 1982 wage and salary employment in the oil industry rose by 230% while total employment in the MSA increased by 40%. The energy sector was responsible for 60% of the growth in non-government, wage and salary employment from 1975 to 1982. When energy prices plummeted in 1982, it left an economic void that could not be filled by growth in other sectors of the local economy. By 1989 employment in the energy sector had declined by 20,100 workers from its peak in 1982, accounting for 81% of the total decline in employment in the MSA.

The service and government sectors helped to cushion the economic impact of the shrinking energy sector by collectively adding 18,200 jobs between 1982 and 1990. The manufacturing sector offset the decline by responding to opportunities created by a strong national economy and growing export markets. In comparison, due to its diversity, Oklahoma City's MSA performed much better than other energy intensive regions.

Non-energy related industries will provide the foundation for the region's growth in the 1990's. Economic studies indicate that Oklahoma City's growth potential includes; warehousing and distribution, government, and the aviation industry.

B. COMPETITIVE PROPERTIES

Venture is the discount retailer most competitive with Wal-Mart, but its nearest store is more than five miles from the property. The closest Wal-Mart is across from the Venture store at the intersection of Rockwell Avenue and the Northwest Expressway . (See Competitive Property Survey attached as Exhibit III-1.)

IV. THE DEVELOPER

The developer of the proposed expansion will be Wal-Mart Stores, Inc. Wal-Mart now develops 90 percent of its stores and nearly all of its expansions. The efficiencies and elimination of developer/tenant conflict make this arrangement very attractive to the landlord.

V. RETURN AND RISK

A. RETURN

The advantage of the amended lease is the increased base rent and the expected percentage rent. Advisors has estimated future sales and calculated estimated percentage rents. Sensitivity analysis with varying sales growth assumptions showed little impact on the returns.

The calculations shown in Exhibits V-1 through V-3 are summarized below:

Three-year holding period:

		Finance Expansion	
	Decline Expanison	Total Capital	Incremental Capital
Annual Return	6.2%	8.1%	12.7%
Net Present Value	(1,177,022)	(260,780)	801,582
Internal Rate of Return	0.2%	9.0%	31.5%

Five-year holding period:

		Finance Expansion	
	Decline Expanison	Total Capital	Incremental Capital
Annual Return	6.2%	9.6%	17.8%
Net Present Value	(1,227,551)	101,468	1,329,019
Internal Rate of Return	2.5%	11.3%	28.9%

Ten-year holding period:

	Decline Expansion	Finance Expansion Total Capital	Finance Expansion Incremental Capital
Annual Return	6.2%	14.3%	33.8%
Net Present Value	(1,295,765)	1,161,543	2,457,308
Internal Rate of Return	4.6%	13.3%	25.9%

The discount rates used for the net present value computation reflect the varying degree of risk in the different components of the cash flow. For this analysis a long-term treasury rate of 8.25 percent was assumed. The spreads over treasury reflect those used by MAI appraisers. The base rent is most secure and is discounted 9.25 percent (100 basis points over treasuries). The residual value is discounted at 10.50 percent (225 basis points over treasuries). The percentage rent is dependent on sales and is least certain. It is discounted at 12.50 percent (425 basis points over treasuries).

B. RISK

The major risk faced by a Wal-Mart landlord is that of the tenant vacating the store, leaving the landlord collecting only the base rent. Typically, Wal-Mart vacates stores because it needs a larger facility but it is unable to expand. The proposed 86,655 square foot store should accommodate the tenant through the term of the lease. USF&G's risk is further reduced by the new base rent of $4.97 per square foot compared to the existing base rent of $4.06 per square foot.

Wal-Mart's credit risk is minimal. With estimated sales through January 1991 of $32.5 billion, it is now the nation's largest retailer. More importantly, for the past three years, Wal-Mart has lead all retailers in net income. Recently, while all other retailers have seen sales decline, Wal-Mart continues to grow. A Graphical Summary is attached as Exhibit V-4.

IV. CONCLUSIONS AND RECOMMENDATIONS

By funding the proposed expansion, USF&G will improve its return on its total investment while preventing its existing investment from declining in value. Therefore, Advisors recommends that USF&G enter into a buy/sell agreement with Wal-Mart Stores, Inc. to purchase approximately one acre of land and the building expansion to be completed no later than November 15, 1991, in accordance with the approved construction drawings dated November 21, 1990. USF&G's purchase price will not exceed $1,700,000 and the lease will be amended in accordance with the Lease Modification Summary attached as Exhibit I-1.

If you have any questions or if you would like to discuss this report, please call me.

Section I
proposal

EXHIBIT I-1
LEASE MODIFICATION SUMMARY

	Existing	Proposed
Size:	64,990 sf	88,655 sf
Base Rent:	$255,528 ($4.06 psf)	$430,628 ($4.97 psf)
Percentage Rent:	None (Wal-Mart will move)	1% over 1993
Lease Expiration:	1/31/2010	1/31/2010
Total Investment:	$4,100,000	$5,800,000
IRR on 5-year hold:	2.5%	28.9%

Section II
The Property

Exhibit II-1
City Map

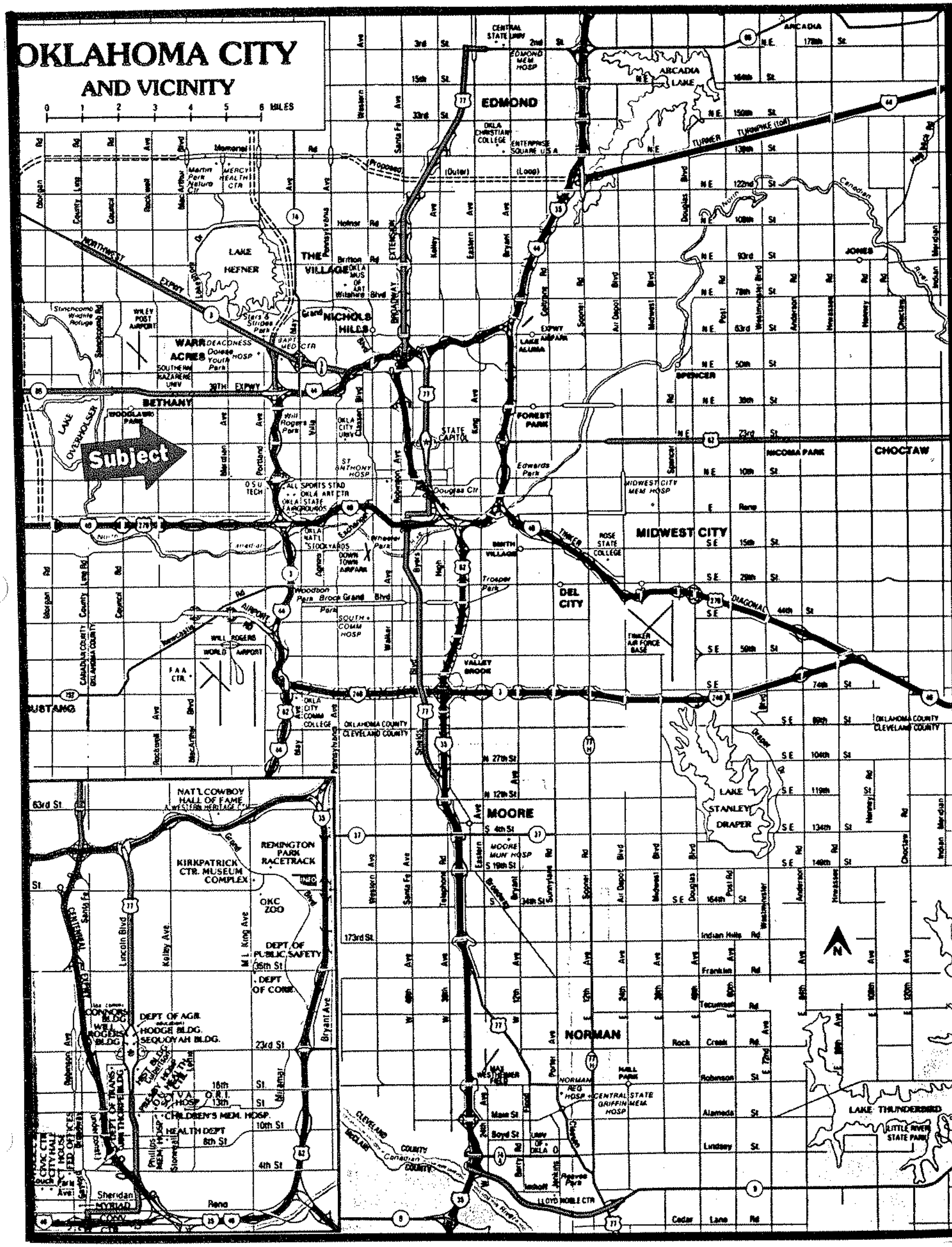
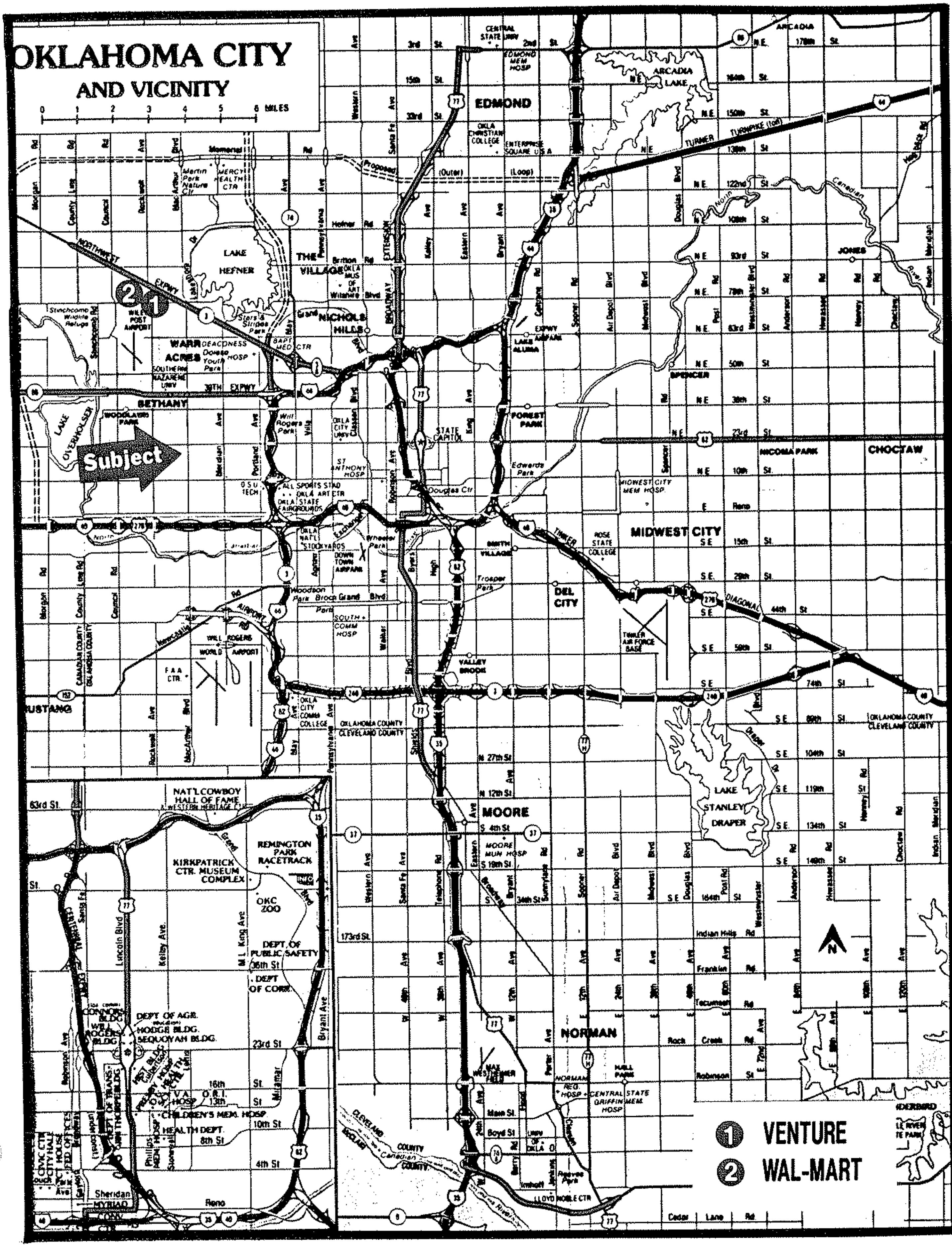


EXHIBIT II-2
SOURCES AND USES OF FUNDS

	Total	Per Sq Ft Building
Sources of Funds		
USF&G Equity Contribution	$1,700,000	$71.84
Uses of Funds		
Land	200,000	8.45
Direct Construction Costs	950,000	40.14
Demolition	250,000	10.56
Indirect Costs	300,000	12.68
Total Uses of Funds	$1,700,000	$71.84

Section III
The Market

Exhibit III-1
Competitive Property Survey



Section V
Risk and Return

EXHIBIT V-1
DECLINE EXPANSION
DISCOUNTED CASH FLOW
THREE, FIVE, AND TEN YEAR HOLDS

Year		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Base rent		255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528
Percentage Rent		93,701	0	0	0	0	0	0	0	0	0	0
Effective Gross Income		349,229	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528
Annual Return			6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%
Sales Proceeds (3 yrs.)*					3,006,212							
Sales Proceeds (5 yrs.)*							3,006,212					
Sales Proceeds (10 yrs.)*												3,006,212
Book Value	4,100,000											
Capital Investment												
Net Cash Flow (3 yrs.)	(4,100,000)	349,229	255,528	255,528	3,261,740							
Net Cash Flow (5 yrs.)	(4,100,000)	349,229	255,528	255,528	255,528	255,528	3,261,740					
Net Cash Flow (10 yrs.)	(4,100,000)	349,229	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	255,528	3,261,740

IRR (3 yrs.)	0.2%
IRR (5 yrs.)	2.5%
IRR (10 yrs.)	4.6%

	Discount Rate	Present Value
Base Rent	9.25%	823,317
Percentage Rent	12.50%	83,290
Residual	10.50%	2,016,371
Present Value		2,922,978
Less Cost		4,100,000
Net Present Value (3 yrs.)		(1,177,022)

	Discount Rate	Present Value
Base Rent	9.25%	1,137,784
Percentage Rent	12.50%	83,290
Residual	10.50%	1,651,376
Present Value		2,872,449
Less Cost		4,100,000
Net Present Value (5 yrs.)		(1,227,551)

	Discount Rate	Present Value
Base Rent	9.25%	1,718,560
Percentage Rent	12.50%	83,290
Residual	10.50%	1,002,385
Present Value		2,804,235
Less Cost		4,100,000
Net Present Value (10 yrs.)		(1,295,765)

* Wal-mart properties with flat base rents are currently selling at capitalization rates approximately 75 basis points above ten to thirty year treasury bond yields. For this analysis, an

8.25 percent long-term treasury bond rate was assumed.

EXHIBIT V-2
FINANCE EXPANSION - TOTAL CAPITAL
DISCOUNTED CASH FLOW
THREE, FIVE, AND TEN YEAR HOLDS

Year		1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Base rent		284,711	430,628	430,628	430,628	430,628	430,628	430,628	430,628	430,628	430,628	430,628
Percentage Rent		93,701	0	0	41,159	84,091	128,167	172,545	221,570	275,388	334,587	399,706
Effective Gross Income		378,412	430,628	430,628	471,787	514,719	558,795	603,273	652,198	706,016	765,215	830,334
Annual Return			7.4%	7.4%	8.1%	8.9%	9.6%	10.4%	11.2%	12.2%	13.2%	14.3%
Sales Proceeds (3 yrs.)*					6,055,514							
Sales Proceeds (5 yrs.)*							7,097,327					
Sales Proceeds (10 yrs.)*												10,527,087
Book Value	4,100,000											
Capital Investment		1,700,000										
Net Cash Flow (3 yrs.)	(4,100,000)	(1,321,588)	430,628	430,628	6,527,301							
Net Cash Flow (5 yrs.)	(4,100,000)	(1,321,588)	430,628	430,628	471,787	514,719	7,656,122					
Net Cash Flow (10 yrs.)	(4,100,000)	(1,321,588)	430,628	430,628	471,787	514,719	558,795	603,273	652,198	706,016	765,215	11,357,422

IRR (3 yrs.)	9.0%
IRR (5 yrs.)	11.3%
IRR (10 yrs.)	13.3%

	Discount Rate	Present Value
Base Rent	9.25%	1,368,590
Percentage Rent	12.50%	108,985
Residual	10.50%	4,061,644
Present Value		5,539,220
Less Cost		5,800,000
Net Present Value (3 yrs.)		(260,780)

	Discount Rate	Present Value
Base Rent	9.25%	1,783,886
Percentage Rent	12.50%	218,871
Residual	10.50%	3,898,712
Present Value		5,901,468
Less Cost		5,800,000
Net Present Value (5 yrs.)		101,468

	Discount Rate	Present Value
Base Rent	9.25%	2,762,638
Percentage Rent	12.50%	688,776
Residual	10.50%	3,510,130
Present Value		6,961,543
Less Cost		5,800,000
Net Present Value (10 yrs.)		1,161,543

* Wal-mart properties with percentage rent potential are currently selling at capitalization rates approximately 80 basis points below ten to thirty year treasury bond yields. This low capitalization rate reflects Wal-Mart's strong credit rating and value of percentage rents. For this analysis, a

8.25 percent long-term treasury bond rate was assumed.

EXHIBIT V-3
FINANCE EXPANSION - INCREMENTAL CAPITAL
DISCOUNTED CASH FLOW
THREE, FIVE, AND TEN YEAR HOLDS

Year	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Base rent	29,183	175,100	175,100	175,100	175,100	175,100	175,100	175,100	175,100	175,100	175,100
Percentage Rent	0	0	0	41,159	84,091	128,167	172,645	221,570	275,388	334,587	399,706
Effective Gross Income	29,183	175,100	175,100	216,259	259,191	303,267	347,745	396,670	450,488	509,687	574,806
Annual Return		10.3%	10.3%	12.7%	15.2%	17.8%	20.5%	23.3%	26.5%	30.0%	33.8%
Sales Proceeds (3 yrs.)*				3,049,302							
Sales Proceeds (5 yrs.)*						4,091,115					
Sales Proceeds (10 yrs.)*											7,520,876
Book Value											
Capital Investment	1,700,000										
Net Cash Flow (3 yrs.)	(1,670,817)	175,100	175,100	3,265,561							
Net Cash Flow (5 yrs.)	(1,670,817)	175,100	175,100	216,259	259,191	4,394,382					
Net Cash Flow (10 yrs.)	(1,670,817)	175,100	175,100	216,259	259,191	303,267	347,745	396,670	450,488	509,687	8,095,682

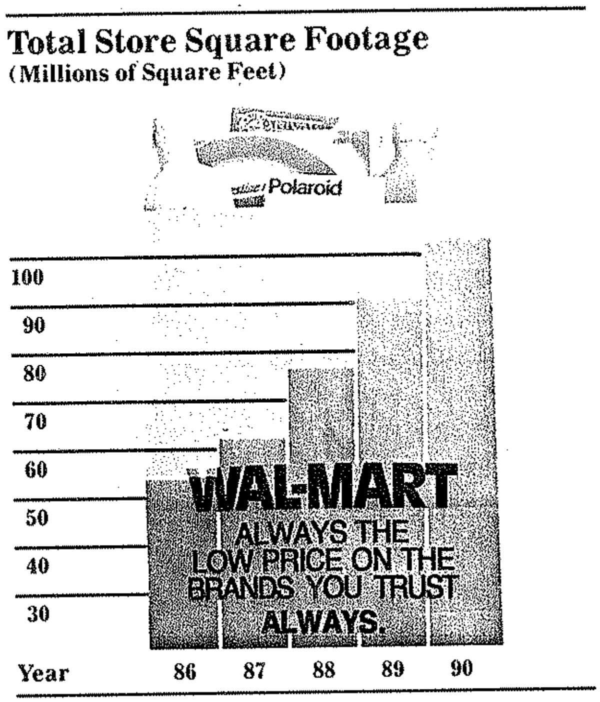
IRR (3 yrs.)	31.5%
IRR (5 yrs.)	28.9%
IRR (10 yrs.)	25.9%

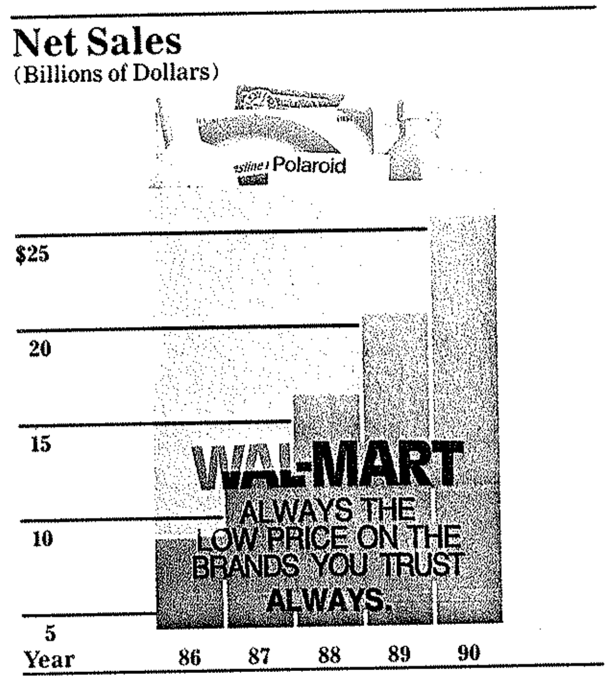
	Discount Rate	Present Value
Base Rent	9.25%	430,614
Percentage Rent	12.50%	25,695
Residual	10.50%	2,045,273
Present Value		2,501,582
Less Cost		1,700,000
Net Present Value (3 yrs.)		801,582

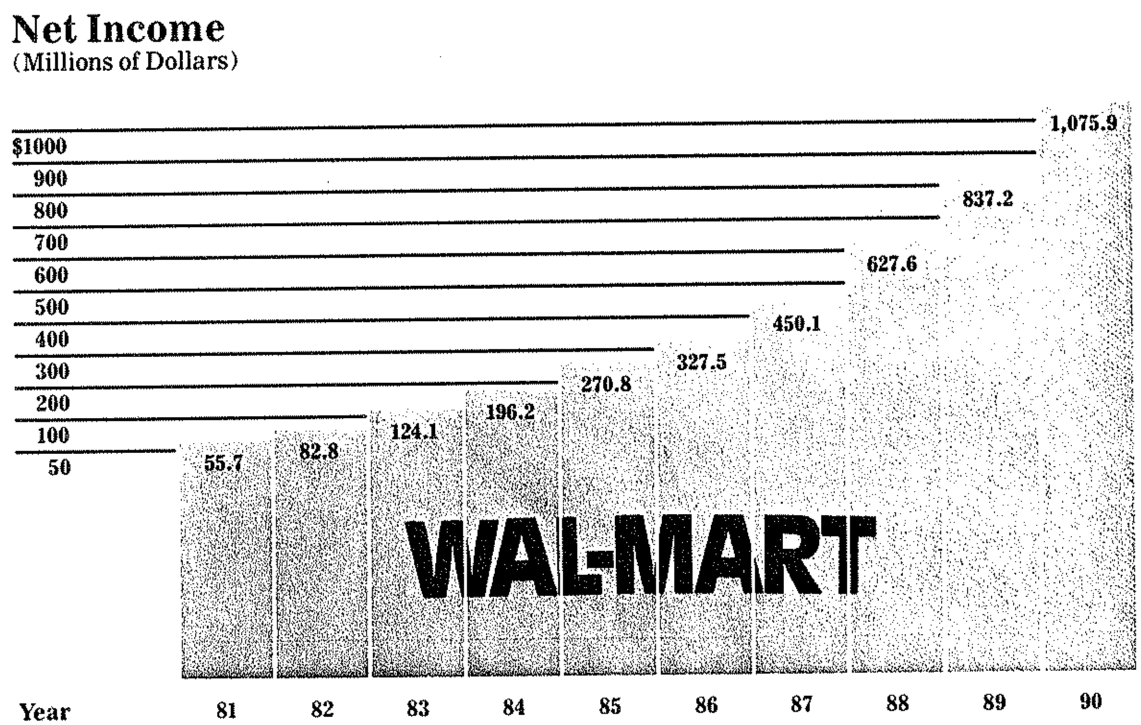
	Discount Rate	Present Value
Base Rent	9.25%	646,102
Percentage Rent	12.50%	135,581
Residual	10.50%	2,247,336
Present Value		3,029,019
Less Cost		1,700,000
Net Present Value (5 yrs.)		1,329,019

	Discount Rate	Present Value
Base Rent	9.25%	1,044,077
Percentage Rent	12.50%	605,486
Residual	10.50%	2,507,745
Present Value		4,157,308
Less Cost		1,700,000
Net Present Value (10 yrs.)		2,457,308

Exhibit V-4
Graphical Summary







* Source: Wal-Mart Annual Report 1990