TALE OF TWO HALVES

The Numbers

After a strong start in 2012, industry numbers began dropping, only to finish out the year about even.

BY JERRY SOVERINSKY

In the 2013 Super Bowl, the Baltimore Ravens amassed a commanding 28-6 lead over the San Francisco 49ers by the third quarter, before a power outage in the Superdome halted play for more than 30 minutes. After the lights were restored, San Francisco stormed back by 17 points, a dramatic momentum shift that Baltimore was able to survive — barely — and win the game 34-31.

Baltimore's performance — eking out a victory after an overwhelmingly strong start —neatly parallels the convenience store industry in 2012, commented Glen Plumby, vice president of operations at Speedway LLC, at the NACS State of the Industry (SOI) Summit in April, in assessing what last year's industry performance looked like.

"We limped to the finish line in 2012 from a sales perspective," Plumby said. "We did have a tale of two halves." (Not to be confused with "One Shining Moment," on page 28.)

How Things Began

Things started out strong in 2012, with first quarter year-over-year, same-store sales up in nearly every major category:

- Fuel sales: **+11.3%**
- Fuel gallons: **+1.9%**
- In-store sales: **+6.0%**
- Foodservice sales: **+11.2%**
- Merchandise sales, less cigarettes: **+8.4%**
- Cigarette sales: **+0.3%**
- Transactions: **+5.0%**
- Pump transactions: **+9.5%**

Combined, these contributed to a robust first quarter sales lift of 10.4%, an auspicious beginning to 2012.

How Things Finished

Beginning in the second quarter, if not before, numbers started dropping across many major categories:

- Fuel sales: **Q2: -1.0%, Q3: -0.2%, Q4: +2.7%**
- Fuel gallons: **Q3: -0.7%, Q4: -0.8%**
- Cigarette sales: **Q2: -0.5%, Q3: -2.4%, Q4: -2.0%**
- Transactions: **Q3: 0.0%, Q4: -0.7%**
- Pump Transactions: **Q3: -0.1%, Q4: +2.7%**

Final Tally

It wasn't a complete downward spiral as in 2008, but the downward trend among key industry drivers concerned Plumby, who conceded he could not explain the phenomenon. "I got nothing," he said. "And I'm not sure it's over."

Despite the foreboding, one was hard-pressed to suppress satisfaction at the overall performance in 2012, with numbers that included several industry highs (up from 2011):

- Total industry sales: **$700.3 billion (+2.7%)**

- In-store sales: **$199.3 billion (+2.2%)**
- Motor fuels sales: **$501 billion (+2.9%)**
- Pretax profit: **$7.2 billion (+3.0%)**
- Foodservice sales (per store/month): **$24,191 (+8.7%)**

So it was a tale of two halves for some categories. Except that others stayed strong throughout the year. Meanwhile, most recorded an overall win. And all are back in 2013.

Got that? Let's dig deeper.

Running Out of Gas

The industry's top performers continued to set a high bar last year, with top quartile and top decile numbers further distancing themselves from their colleagues, especially significant among categories that show steady declines — like fuel.

TOP TEN MERCHANDISE CATEGORIES
Same Period GP$ Change YOY

PER STORE/PER MONTH	Q1	Q2	Q3	Q4
CIGARETTES	(7.2)%	(4.7)%	(4.7)%	(2.3)%
PACKAGED BEVERAGES	8.5%	8.0%	5.9%	5.9%
BEER	10.1%	8.7%	5.2%	1.5%
OTP	2.4%	3.3%	0.8%	5.3%
SALTY SNACKS	18.1%	12.9%	8.6%	7.1%
CANDY	10.1%	3.3%	3.5%	3.1%
PACKAGED SWEET SNACKS	16.7%	11.0%	5.2%	0.9%
MILK	16.9%	21.2%	15.8%	2.3%
ICE CREAM	18.6%	12.4%	4.1%	6.6%
GENERAL MERCHANDISE	5.1%	17.3%	(2.1)%	8.0%

(Source: *NACS State of the Industry Report of 2012 Data*; CSX LLC)

For the industry in 2012, total fuel consumption (barrels per day) was down 0.6% to 8.7 million barrels, movement that "scares the heck" out of Plumby, who reported that since 2007, total fuel consumption is down 7.4% for the industry — behavior "that's very concerning."

Plumby attributed the loss to more fuel-efficient vehicles on the roads and a decrease in miles driven, factors he doesn't see changing anytime soon. Individual store performance therefore becomes increasingly critical in this category — stemming the losses despite changing consumer preferences.

Considering each year's fuel consumption a fixed pot, with stores vying for increasing market share, top performers are pulling away. In 2011, top quartile performers sold 181,425 gallons, or 1.7 times greater than the bottom quartile performers, which sold 107,944 gallons.

Meanwhile, in 2012, top quartile performers sold 165,378 gallons, an 8.8% drop from 2011, 1.8 times greater than the bottom quartile performers, which sold 89,843 gallons.

Not to be outdone, top decile performers sold 225,090 gallons — 2.5 times more than the bottom quartile performers and 1.4 times greater than the top quartile. And equally significant, this group realized a 4.3% lift in gallons sold, a sizable increase during an overall down year.

Their growth was touched on at last year's Summit, as breakeven-cents-per-gallon were analyzed. And in this key metric, top decile stores continued to impress with a breakeven of 6.65 cents versus 7.53 cents for the top quartile as a whole. For the industry, this was also a "shining moment" metric, improving 12% to 9.21 cents and avoiding one of Plumby's "watch outs" from the 2012 Summit.

Up in Smoke

Same-firm monthly cigarette sales dropped $476 to $51,863 in 2012, a 0.9% loss that Plumby flagged as a "watch out" at last year's Summit, and one that is a continued threat to retailers.

"That consumer (smoker) is a very valuable consumer for our industry when you look at the basket around a carton of cigarettes," Plumby said. "As cigarette units continue to fall, that certainly threatens inside growth of our stores."

Furthermore, same-firm cigarette margins fell 2.7% last year, which "is going to force us to work a lot harder inside the stores to recapture those sales," Plumby said. Meanwhile, cigarettes are on the decline but OTP is climbing, with in-store sales year-over-year up 6.5%.

Food, Glorious Food!

Foodservice continued its solid growth path, with same-firm sales up 8.7% to $24,191 per store per month, representing 15.8% of total in-store sales. This bodes especially well for retailers focusing on this category, as foodservice contributed 27.1% to in-store gross profit dollars.

While the upsides in running a successful foodservice operation are not news for retailers, Plumby framed them in the context of overall QSR market share and what's still available. "If you look at McDonald's, they're averaging roughly $225,000 per month, and Pizza Hut is averaging $60,000 per month in equivalent sales dollars," Plumby said. "Our top quartile averages $32,000 per month. So roughly, a Pizza Hut does twice as good on foodservice sales as

SAME PERIOD SALES CHANGE

Same Firms

PER STORE/PER MONTH	Q1	Q2	Q3	Q4
TOTAL ALL SALES	10.4%	0.4%	0.6%	2.6%
FUEL SALES	11.3%	(1.0)%	(0.2)%	2.7%
FUEL GALLONS	1.9%	1.6%	(0.7)%	(0.8)%
AVERAGE SELLING PRICE	9.3%	(2.6)%	0.5%	3.5%
IN-STORE SALES	6.0%	4.4%	2.1%	1.5%
FOODSERVICE SALES	11.2%	10.4%	6.6%	7.0%
MERCHANDISE SALES	5.1%	3.5%	1.4%	0.5%
MDSE LESS CIGARETTES	8.4%	6.4%	4.0%	2.7%
CIGARETTES	0.3%	(0.5)%	(2.4)%	(2.0)%
TRANSACTIONS	5.0%	1.4%	0.0%	(0.7)%
PUMP TRANSACTIONS	9.5%	3.4%	(0.1)%	2.7%

(Source: *NACS State of the Industry Report of 2012 Data*; CSX LLC)

STORE OPERATIONAL PRODUCTIVITY

2012	TOP 10%	TOP 25%
MOTOR FUELS GALLONS SOLD	225,090	165,378
MERCHANDISE SALES	$171,757	$132,225
FOODSERVICE SALES	$46,142	$33, 978
IN-STORE GM%	30.9%	32.1%
CIGARETTE GM%	12.6%	13.6%
AVERAGE SQUARE FEET	2,062	2,535
IN-STORE SALES/SQ. FOOT	$105.02	$64.66

(Source: *NACS State of the Industry Report of 2012 Data*; CSX LLC)

our top quartile. And as an industry total, our sales are $22,500 — a Pizza Hut does about three times as much as we do as an industry selling food."

Why is this encouraging? "If we can get more conversion from the people either fueling or more conversion from the people buying [in-store] ... we have tremendous upsides," Plumby said.

Top performers continue to outpace the rest of the pack here: Top quartile operators generated $33,978 in foodservice sales last year — a 40.5% jump over the $24,191 industry average. But top decile performers went even further, recording $46,142 in sales — a 35.8% jump over top quartile operators and a 90.7% lift from the industry average. Notable is the jump top decile operators recorded over top quartile operators: Last year, top decile operators were 29.3% more productive than those in the top quartile, versus 35.8% this year.

The "Tale of Two Halves" held true in nearly every foodservice category, said Kevin Smartt, CEO of Kwik Chek Food Stores Inc. "Why is that?" he asked rhetorically. "We don't know," he said, before speculating that the fiscal cliff, taxes, a sustained drought, and Hurricane Sandy all played a role.

The performance differences between top and bottom quartile performers within the foodservice category were wide last year, with prepared food (2.4x), hot dispensed beverages (4.4x) and cold dispensed beverages (2.3x) all registering large gaps. This year, for the top quartile firms, prepared food was 2.9x, hot dispensed beverages were 7.0x and cold dispensed beverages were 3.5x the bottom quartile. And top decile performers distanced themselves even further from the pack, outgaining top quartile performers in foodservice (1.3x), hot dispensed beverages (1.6x) and cold dispensed beverages (1.2x).

I'll Drink to That

Among the 28 in-store categories that NACS tracks, 22 posted sales gains last year, Smartt said, with beverages near the top. Liquor (+11.6%), cold dispensed beverages (+11.3%), frozen dispensed beverages (+7.5%) and packaged beverages (+7.0%) all rang up strong year-over-year sales growth, with packaged beverages ($21,117) a strong second behind cigarettes ($51,863) in sales dollars per store/per month, among all merchandise categories.

"Packaged beverages is our golden category right now," Smartt said, noting its 20% growth in sales and 19% growth in margin since January 2010. In 2012, every subcategory of packaged beverages generated positive sales growth. "There's no doubt, on this one, we've hit a home run."

What About Plastic?

While total credit and debit card fees set another industry record — $11.2 billion, surpassing industry profits for the seventh consecutive year — there's relief in sight, Plumby said, with the gap between pretax profit and card fees shrinking. Additionally, the Durbin Amendment did save roughly $320 million in debit card fees, while the rate of increase slowed to 1.5%, far less than the 23.0% increase recorded between 2010 and 2011.

ABCs of CTP

Since 2009, the NACS Convenience Tracking Program (CTP) has been studying the reasons why consumers shop in convenience stores. Distilling data from thousands of onsite "moment of truth" shopper interviews each year immediately pre- and post-shopping trip, CTP provides actionable insights for retailers based on, among other things, customer perception, category drivers, opportunity gaps and conversion factors.

Leroy Kelsey, director of industry analytics at NACS, explained to Summit attendees that CTP tallied 15,000 interviews at 600 stores across 40 states in 2012.

After assessing intended versus actual purchases and addressing the notion of shopping missions — the reasons why a consumer made a particular convenience store trip — he offered a shopping mission matrix profile that analyzed trip share and spend percentage among eight identified missions or purposes: treat, distressed, planned, snack, fuel, meal, entertaining and services.

The visit vs. spend relationship is significant, Kelsey noted, because of sharp disparities revealed between the two;

TOP TEN MERCHANDISE CATEGORIES			
PER STORE/PER MONTH	SALES $	MARGIN $	GM %
CIGARETTES	$51,863	$7,409	14.3%
PACKAGED BEVERAGES	$21,117	$8,311	39.4%
BEER	$16,506	$3,043	18.4%
OTP	$6,571	$2,007	30.5%
SALTY SNACKS	$6,297	$2,408	38.2%
CANDY	$4,481	$2,119	47.3%
PACKAGED SWEET SNACKS	$3,306	$1,101	33.3%
MILK	$2,301	$685	29.8%
ICE CREAM	$2,132	$977	45.9%
GENERAL MERCHANDISE	$2,020	$798	39.5%

(Source: *NACS State of the Industry Report of 2012 Data*; CSX LLC)

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information that speaks to profitability and opportunities.

"Treat" was the most popular shopping mission, according to CTP data, representing 29.9% of all consumer trips, but the category returned only 22.0% of sales dollars. Compare this to entertaining, which represented 4.4% of all trips and a 7.5% spend.

Specifically, fountain carbonated drinks drove 30% of the treat mission, making it the highest treat mission driver. (Incidentally, "cold, hot and packaged beverages added together were 61.2% of our touches," Kelsey said.) The opportunity for retailers is to convert these consumers looking to treat themselves — fully one-third of them driven by fountain — to higher margin snacks or meals through bundling or other offers.

While Kelsey offered at-a-glance summaries of other opportunities, he also expanded in more detail, quantifying what's at stake for retailers when it comes to meal conversions — but for Summit attendee eyes only! (Be sure to attend next year's Summit to get the inside scoop on CTP data firsthand.)

Putting It All Together

The ability to convert customers to make food purchases is the true challenge for retailers, Kelsey said, one that requires constant retooling to discover what resonates.

"We have to use category drivers and missions and gap analysis to figure out which tuning knobs to use to dial in to the right frequency," Kelsey said. "And over time, you refine your offer in a way that can grow your business [and] grow expectations."

While no one could identify the precise reasons for the sales drop in many key categories as 2012 unfolded, Plumby, Smartt, Kelsey and others made sure that retailers had the data and insights necessary to minimize the risk for a repeat performance in 2013. And indeed, the first three months of 2013 were already showing strong sales lifts in many categories, including gasoline consumption and gasoline margins, according to Plumby.

Yes, there were missed tackles and even a fumble or two last year, but despite the hiccups and by all objective standards, the convenience store industry recorded a solid win in 2012. NACS

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Benchmarking Resources

Top-decile and top-quartile retailers didn't reach their lofty status by accident. They invested time and thought into setting realistic, achievable goals and developing benchmarks to guide them on their path to success.

The annual ***NACS State of the Industry Report*** is the industry's premier benchmarking tool and most comprehensive collection of firm-level, store-level and category data and trends based on the convenience and fuel marketing industry's prior year performance.

The **CSX LLC** database allows users to view financial and operational benchmarks, determine opportunity gaps by comparing their own data and track their progress, all in one user-friendly web-based application. The subscription-based service offers limitless opportunities to benchmark against key industry metrics.

For more information on the *NACS State of the Industry Report*, contact Bob Swanson at NACS at (703) 518-4219 or rswanson@nacsonline.com. For more information on the CSX benchmarking database, contact Chris Rapanick at (703) 518-4253 or crapanick@csxllc.com.