The C-STORE TWILIGHT ZONE

INDUSTRY NUMBERS WERE STRONG IN 2013, THOUGH TRENDS WERE SOMEWHAT SURPRISING AND INEXPLICABLE IN A "TWILIGHT ZONE" KIND OF WAY.

BY JERRY SOVERINSKY

Television icon Rod Serling and his "Twilight Zone" television series took center stage at this year's NACS State of the Industry (SOI) Summit, held April 1-3 in Chicago.

"You unlock this door with the key of imagination," began Serling, creator and host of the popular show from the 1960s, in a clip borrowed from the show's open and shown to Summit attendees. "Beyond it is another dimension. A dimension of sound. A dimension of sight. A dimension of mind. You're moving into a land of both shadow and substance, of things and ideas. You've just crossed over into the Twilight Zone."

And so began the presentation on the Summit's opening morning by Glenn Plumby, vice president of operations for Speedway LLC, and member of the NACS Research Committee, in establishing a theme for 2013's industry performance. Picking up from 2012, which witnessed a six-month performance slide (see *NACS Magazine's* "Tale of Two Halves" from June 2013), Plumby noted gallons increased 0.6%, fuel margins were up 2.3% and in-store sales rose 2.4%. "As a betting man, many of you would just take that," Plumby surmised. "But you know what, things just aren't as they seem," he said.

According to Plumby, Serling's "The Twilight Zone," which thrilled audiences with themes of identity, time, societal roles and out-of-this-world science fiction, perfectly captured the convenience store industry's 2013 performance, while presaging its future.

"One in six men 25 to 54 — a core c-store consumer group — remain unemployed," continued a Serling impersonator in a video that expanded on Plumby's premise. "Median household incomes have dropped 8.3% since 2007. Shifts in income distribution and changes to SNAP programs continue to impact the industry."

Convenience store operators are facing a retail landscape that's dramatically different from just a few years ago and that promises to evolve even further in coming years, Plumby said, whose video ticked off the following:

- Big box retailers are getting smaller while convenience stores are getting larger.
- Competitors come from all corners.
- Gas consumption continues to decline.
- Sales are shifting from cigarettes to foodservice.
- Population trends and demographic markets are changing.

"At times the truth is a world gone mad," the video concluded. "You're not imagining it; this is not a dream. This is reality. You've just crossed over into the Twilight Zone."

Hyperbole dressed as drama? Perhaps. Change is a fact, but it's difficult to get overly concerned when industry inside sales reached a record $204 billion in 2013, which included strong same firm foodservice growth (2.4%) and record-high motor fuels gallons sales (up 0.9% to 132,029 gallons per store per month).

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INDUSTRY KEY METRICS

Snapshot	2012	2013	% Change
Store Count	149,220	151,282	1.4%
Inside Sales	$199.3B	$204.0B	2.4%
Fuel Sales	$501.0B	$491.5B	(1.9)%
Total Sales	$700.3B	$695.5B	(0.7)%
Pretax Profit	$7.2B	$7.1B	(2.4)%
Credit Card Fees	$11.2B	$11.2B	(0.4)%
Gas Consumption (bbl/days)	8.70M	8.75M	0.6%
Employees	1.84M	2.20M	19.5%
Fuel Margin (cpg)	18.1¢	18.5¢	2.3%
Net of CC Fees	12.73¢	13.17¢	3.5%

2013 SALES (SAME FIRM)

Per Store/Per Month	2012	2013	% Change
Fuel Gallons	130,845	132,029	0.9%
Average Selling Price	$3.57	$3.47	(2.9)%
Fuel Sales	$467,390	$457,754	(2.1)%
In-Store Sales	$132,951	$136,265	2.5%
Foodservice Sales	$24,158	$24,726	2.4%
Merchandise Sales	$110,448	$111,866	1.3%
Mdse - Cigarettes	$66,336	$67,944	2.4%
Cigarettes	$46,351	$44,751	(3.5)%
Total All Sales	$497,962	$497,654	(0.1)%

fuel retailing continues to grow, despite economic and retail environment challenges," said NACS Chairman Brad Call, vice president of adventure culture at Maverik Inc. "These numbers show that we continue to meet the needs of our diverse consumers throughout the United States."

But as any veteran SOI follower knows, self-restraint is the hallmark of this annual event, a time to acknowledge, but not bask in success. Complacency is an outcast here, as the convenience store landscape is indeed changing, Plumby said, with eerie shifts that align perfectly with those explored in "The Twilight Zone."

ORDINARY PEOPLE, EXTRAORDINARY CIRCUMSTANCES

"There's a place in this universe where ordinary people meet extraordinary circumstances," Plumby's video announced, with U.S. male unemployment up sharply from 2007-2013:

- 16-19 years old: 28.1% (from 17.6% in 2007)
- 20-24 years old: 16.9% (from 8.9% in 2007)
- 25-29 years old: 9.8% (from 5.3% in 2007)

"Bubba's hurting," Plumby said, referring to the industry's typical customer, whose share of the national income has dropped 15% since 1967. And as he continues to fight unemployment and loses disposable income, "Are we targeting the right customer?" Plumby asked rhetorically, suggesting that the industry reexamine its customer base.

SPACE & TIME

"In a dimension of space and time, big box retailers are getting smaller while convenience store are getting larger," Plumby's video continued. "Competitors come from all corners, while the convenience store industry indisputably owns time, with more than half of what we sell consumed less than an hour after being purchased."

Big box competitor Target offers a number of formats, while Walmart is on its fifth-generation store, Plumby later noted, with one Arkansas location even selling gasoline. "They're competing for the same customers."

While convenience store unit growth increased 1.4% last year, other retail channels saw even faster growth: dollar stores (+6.1%), drug (+1.6%), cigarette outlets (+5.6%) and wholesale clubs (+2.0%) all posted strong gains.

Finally, when it comes to time, convenience store offerings continued a steady trend of offering instant gratification. Whereas 79.8% of convenience store offerings were consumed in less than an hour in 2009, that number reached 83.5% in 2013. "Time is something that we own and something that we can and will continue to leverage."

KNOWN VS. UNKNOWN

"From unpredictable industry sales, to industry card thieves and motor fuels trends, all while gas consumption continues to decline," began a video segment exploring the known and unknown, familiar territory for Serling and one that is becoming common for convenience store retailing.

"Gallons are up, margins [were] third best in the last seven years, sales are up more than they were in 2012, yet our profitability is down," Plumby said. "That's kind of the Twilight Zone-ish impact the numbers have," the most notable that included:

- **Overall sales were $695.5 billion (-0.7%)**, which included in-store sales ($204 billion, a record high) and motor fuels sales ($491.5 billion).

2013 GROSS PROFIT $ (SAME FIRM)

Per Store/Per Month	2012	2013	% Change
Fuel Pool Margin	18.22¢	18.64¢	2.3%
Margin - CC Fees	12.73¢	13.17¢	3.4%
Fuel Gross Profit	$23,845	$24,616	3.2%
In-Store	$42,617	$44,514	4.5%
Foodservice	$12,760	$13,081	2.5%
Merchandise	$30,372	$31,606	2.8%
Mdse Less Cigarettes	$24,245	$25,381	4.7%
Cigarettes	$6,927	$6,532	(5.7)%
Total Gross Profit	$64,938	$67,769	4.4%

- **Pretax profit fell 2.4% to $7.1 billion**, which followed several growth years.
- **Credit card fees declined 0.4%**, "and the gap between profit and card fees has stabilized," Plumby said, a result of the Durbin Amendment.
- **Motor fuels sales climbed 0.9%** to 132,029 gallons per store per month (record high) — though total gas consumption inched upward only 0.6%. "Don't get overconfident," Plumby said, noting that it has fallen 7.4% since 2007, the result of better fuel efficiency and alternative fuels.
- **Foodservice sales grew 2.4%**, not nearly enough. "We have to do better than that," Plumby said. "This is our way to make hay and offset some of the cost issues."
- **Employee count rose 19.5%**, led by part-time employee headcounts, which spiked 32.2%, a trend that Plumby attributed to the Affordable Care Act. Additionally, 20 states have enacted or have pending minimum wage increases. "We need to be concerned," Plumby said.
- **Fuel margins increased 2.3%** to 18.5 cents per gallon.
- **Cigarette margin was down 5.7%** from 2012.
- **Core operating expenses rose 5.1%**, driven by wages and benefits. "When your margins are up and expenses are up, that's a problem," Plumby warned, adding that lowering expenses is a critical mission for 2014 "because it's only going to get worse."

The session was a collage of numbers, ones that Plumby summed up as inconclusive and somewhat conflicting. "Fuel was a hero ... profitability was down ... but many retailers had record years for income," Plumby said. "So from a 'Twilight Zone' [perspective], there's a disconnect," which he attributed somewhat to variations in regional performance.

STORE OPERATIONAL PRODUCTIVITY

2013	Top 10%	Top Quartile	Bottom Quartile
Motor Fuels Gallons Sold	221,815	170,268	107,281
Merchandise Sales	$163,213	$132,106	$76,102
Foodservice Sales	$45,703	$34,572	$9,712
In-Store GM %	32.0%	32.7%	27.3%
Cigarette GM %	12.8%	13.5%	14.1%
Average Square Feet	2,136	2,477	2,494
In-Store Sales/Sq. Foot	$97.42	$67.09	$33.99

UNEXPECTED ENDINGS, MASS HYSTERIA

"In this new world, this new dimension, there's the ironic twists and unexpected endings, swings in inside sales versus expenses, shifts from cigarettes [to] foodservice sales, shifts in population trend and new demographic markets," the video continued.

Plumby reinforced the theme moments later, noting the gap between top quartile and bottom quartile stores fell in 2013 for motor fuels gallons sold and merchandise sales, mainly due to decent cigarette sales at bottom quartile stores, whose gross margin percent was 14.1%, compared to 13.5% for top quartile performers (the gap in margin percentage is contracting, Plumby noted).

Finally, what "Twilight Zone" would be complete without screaming masses cowering for assistance. "A dimension of mass hysteria continues to overtake the industry, from menu labeling placards to data security to dramatic increases in average fuel economy and renewable fuel standards," the video concluded, a lead-in to Plumby's discussion of recurring industry nightmares.

SOLUTIONS

"The final dimension that the 'Twilight Zone' talks about is solutions," Plumby concluded. "We've got a lot of solutions; we call them things that keep you up at night."

For data security, Plumby said Conexxus (formerly PCATS) is the first industry technology body to have adopted X9 standards for encrypting card data at all fuel and points of sale, which protects card data from flowing through convenience stores.

Plumby framed last year's results as key learnings for succeeding in 2014 and beyond. "The customer has and will continue to change," he said, and it's imperative to know what your customer wants. "Is Bubba [even] the customer we need to target?" he asked. And if not, we need to "look at loyalty and everything we have in our toolbox ... to understand and target our consumer."

Cigarette sales are waning, and while food is growing, "It must grow faster," he emphasized. "We have to be better at food."

Finally, there's the uncertainty of government regulation — tobacco, e-cigarettes, menu labeling, swipe fees — the unknowns that underscore "The Twilight Zone" and its surprise endings. "2013 was a pretty good year; but the big gorilla in the room is regulation."

He paused briefly, while the ominous music swelled. "Keep calm and expect the unexpected." NACS