'A Tale of Two Seasons'

Increase in fourth-quarter fuel prices dampens demand, profits

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Fuel-Grade Performance

The industry moved 150.4 billion gallons of fuel in 2007—7.4 billion less than in 2006. While regular-grade fuel continues to command the bulk of sales, it lost 1.5 share points; among gasoline, only midgrade grew share. Without diesel in the picture, regular-grade gasoline delivered 82% of fuel sales.

Top-quartile retailers sold 204,294 gallons of fuel per store per month in 2007, compared to only 105,738 gallons per store per month for those in the bottom quartile and more than 193% the volume. Interestingly, regular grade made up a greater share of top-quartile retailers' total fuel gallons than that of the bottom quartile.

Total Industry	Gallons per store per month		Percent share		Percentage point change
Fuel grade	2006	2007	2006	2007	
Regular	89,406	91,508	70.0%	68.5%	–1.5%
Midgrade	11,420	12,519	8.9%	9.4%	0.4%
Premium	7,467	7,567	5.9%	5.7%	–0.2%
Diesel	19,374	21,971	15.2%	16.4%	1.2%
Total	127,667	133,565	100%	100%	

	Gallons per store per month			
Quartile	Regular	Midgrade	Premium	Diesel
Bottom	68,149	11,194	9,777	16,618
Third	69,288	7,432	5,273	22,451
Second	72,566	16,379	5,598	20,735
Top	151,404	14,307	13,276	25,307

Source: NACS 2008 State of the Industry Survey powered by CSX

Remember the heady days of 2005 and 2006, when September brought margin relief in years blighted with supply issues and price increases? Dick Meyer of Meyer & Associates—and co-founder of the CSX LLC benchmarking database—refers to them as "Septembers to remember."

"CSX data for September 2005 showed pooled national fuel margins for same firms averaging 20 cents for the first time I knew of in our industry," Meyer says via e-mail. "I reminded CSX users … that September 2005 was Katrina-related and fuel marketers saw higher margins at the pump because of the uncertainty of supply caused by that major crisis." In 2006, the industry had another "September to remember," he says, but it, too, was caused by an anomaly—in this case, a fast slide in the cost of product.

After the last quarter of 2006, Meyer cautioned retailers to not presume that last year's per-month fuel margin trends would repeat in 2007, especially for the month of September. "I didn't see another 'perfect storm' coming in

Average Selling Price Per Gallon

The industry's average selling price for fuel rose 11.3% in 2007. Despite this being the fifth consecutive increase, it rose at a much slower pace compared to 2004 and 2005.

Source: NACS 2008 State of the Industry Survey powered by CSX

Effect of Credit-Card Fees on Fuel Margin

Beyond margin as a percent of sales metrics, the only figure not to grow in 2007 in the chart below was net fuel margin per gallon. Holding flat at 10.1 CPG, the metric places the 0.6-CPG growth in actual fuel margin—and doubling of break-even pool margin—in greater perspective.

Metric	2006	2007
Selling price per gallon	$2.57	$2.73
Actual fuel margin per gallon	13.7 cents	14.3 cents
Credit-card fees per gallon	3.6 cents	4.2 cents
Net fuel margin per gallon*	10.1 cents	10.1 cents
Break-even pool margin	10.2 cents	12.1 cents
Net break-even pool margin per gallon*	13.8 cents	16.7 cents
Pretax margin as % of sales	0.8%	0.6%
Net fuel margin as % of sales	5.8%	5.2%

Source: NACS 2008 State of the Industry Survey powered by CSX **After credit-card fees*

2007 and I don't dare project fuel trends, so my conservative thinking was that September margins would return to historical norms, which essentially they did," he says.

In fact, Meyer refers to 2007 as "a tale of two seasons." Average fuel prices during the first nine months of 2007 were up about 3% over the same nine months in 2006, he explains, referring to Energy Information Administration figures. "However, in the last calendar quarter of 2007, average pump prices were up over 30% from the prior year, and that really impacted other dynamics, including consumers' spendable income for other 'stuff' in c-stores."

Retailers paid more than double their total profits in 2007 in credit-card fees alone, which jumped up to $7.6 billion.

New Lows and Highs

Total fuel volume dropped 4.9% in 2007 to reach 150.4 billion gallons, or 127,667 gallons per store per month, according to NACS 2008 State of the Industry Survey powered by CSX.

Fuel pool margin grew 4.4% to hit 14.3 cents per gallon (CPG)—before factoring in credit-card fees. After the 4.2 CPG of credit-card fees, pool margin shrank to 10.1 CPG, no change from the prior year. Break-even pool margin grew 18.6% to reach 12.1 CPG; with credit-card fees removed from the equation, break-even rose to 16.7 CPG, up 21% from the year prior.

Examined across 2007, fuel margins net credit-card fees tracked higher in seven of the 12 months over 2006 figures; the notable exceptions were February through April, and late summer/early fall, where the greatest dichotomy was a 2.7 CPG margin shortfall in September 2007 vs. September 2006, according to the NACS SOI Survey.

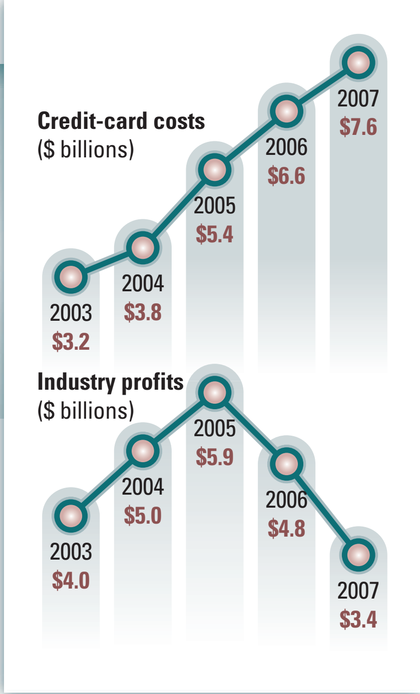
Fuel margins in 2007 shrank to half their level from only eight years ago, settling at 5.2%, according to the survey—the lowest level in the past 20 years. Increasing inventory costs and slumping demand helped shave off the profits.

Fuel gallons sold in 2007 followed the seasonal curves of 2006, although sales in January 2007 showed a greater drop into February than the year prior, while they spiked higher in August. Among

Plastic vs. Profits

Beginning in 2005, credit-card fees changed direction from industry profits. As the fees reached an all-time high in 2007, profits sank toward levels not seen since the turn of the millennium.

Source: NACS 2008 State of the Industry Survey powered by CSX



the same-firm sample, sales per store per month rang up at 119,374 gallons, up 2.0% from the year prior.

Examining fuel volume by quartile, the difference between those retailers who fall in the bottom 25% by store operating profit and those who made the top 25% is stark. Top performers churned through nearly double the volume per store per month, or 204,294 gallons. Regular-grade volume alone for top-quartile retailers was more than twice that of all other quartiles.

Excluding diesel, regular grade commanded 82% of fuel volume in 2007, according to NACS SOI Survey figures, a 0.6% drop from the year prior. Midgrade share, meanwhile, rose 0.7% to hit 11.2% of total fuel volume, excluding diesel, or 12,519 gallons per store per month. Diesel itself provided 16.5% of fuel volume, a 1.3% increase from 2006.

Always considered a seasonal business, fuel proved to be even more so in 2007. Every month of 2007 beat the average fuel price per gallon of the previous year, with the fall and winter months witnessing the greatest distance. Put another way, the average selling price for fuel was up about 42 CPG during the fourth quarter of 2007—triple the approximate 14-16 CPG average difference between the first nine months of 2007 vs. 2006. This truly made 2007 a tale of two seasons for retailers. ■