

# It's Getting Better

The U.S. economy continues to improve despite rising interest rates and terror threats

**C**onvenience store retailers' view of the overall U.S. economy appears to support our forecast that 2016 will be a "good" year for American businesses.

"The economy in general is doing quite well," said Maureen Maguire, founder and CEO of *ThinkResearch* and chief analyst for *Convenience Store News'* annual Industry Forecast Study.

However, Maguire pointed out that many of the positive economic signals also have downsides. For example, the reduction in the nation's unemployment rate is offset by the large number of people who have left the labor market or are under-employed. This has provided the Federal Reserve with an impetus to increase interest rates.

Stock market reaction to the interest rate hike last month was muted due to the Fed's transparent communication policies, Maguire noted. "At this point, most market participants expect the Fed to continue to raise rates over the course of at least the next 12 months by 50 to 100 basis points," she said. "Of course, that depends on the labor market and the goal for inflation to come in close to the Fed's annual target of 2 percent. As long as the economy marches toward those two goals, we should expect rate increases."

Forty-one percent of convenience store retailers polled in *CSNews'* exclusive Retailer Forecast Study

said their companies view U.S. economic conditions overall as "slightly positive" for 2016. About 18 percent are "very positive" about the 2016 economic outlook. Almost 30 percent said they feel "neutral" about this new year. However, about 13 percent are "slightly" or "very negative" about business prospects in 2016.

Interestingly, c-store chain respondents are less enthusiastic about the 2016 economic outlook than the industry's single-store operators, 77.8 percent of whom feel "very" or "slightly positive" about this year vs. 51.7 percent of chain retailers.

A real advantage going into this year is that inflation remains low. Maguire pointed out the U.S. Bureau of Labor Statistics reported last month that the Consumer Price Index for All Urban Consumers (CPI-U) was unchanged in November on a seasonally-adjusted basis. Over the last 12 months, the all items index increased 0.5 percent before seasonal adjustment, with the food index climbing 1.3 percent but the energy index declining 14.7 percent.

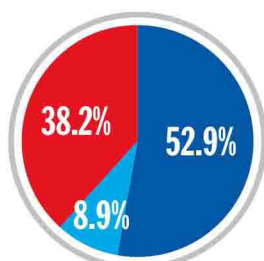
"Going forward, we should expect the inflation rate to tick up slightly toward the Fed's annual target rate of 2 percent," said Maguire. "This is not necessarily a bad thing. It will encourage consumers to purchase goods and services rather than wait for them to be cheaper in the near term."

Maguire ticked off several factors that could dim

## Retailer Forecast: Motor Fuels

■ Volume will increase ■ Volume will decrease ■ Volume will stay the same

Net change: 3.5%



Source: Convenience Store News Retailer Forecast Study, 2016

## Industry Forecast: Motor Fuels

	2014 ACTUAL	2015 ESTIMATED	2016 FORECAST
Average retail price per gallon <sup>1</sup>	\$3.56	\$2.57*	\$2.55*
Gasoline (all grades)	\$3.44	\$2.50*	\$2.46*
Diesel	\$3.93	\$2.72*	\$2.76*
National billions of gallons	182.9	186.7*	187.3*
C-store billions of gallons	148.3	151.4	151.9
National sales of gasoline (\$ billions)	\$650.5	\$479.8	\$477.6
C-store sales of gasoline (\$ billions)	\$527.5	\$389.1	\$387.3

<sup>1</sup> Weighted average price of all grades and diesel fuel

\*Prediction from EIA/Department of Energy, Short-Term Outlook, October 2015

Source: EIA/Department of Energy; Convenience Store News Industry Forecast Study, 2016

the 2016 forecast, including the continued slowing of China's economy; increased terrorist attacks, particularly in the United States; a drastic slowdown in Europe; and a return to higher oil prices.

### MOTOR FUELS

Falling gas prices are *the* story when it comes to motor fuels, and this trend is highly likely to continue. Based on CSNews' Forecast Study estimates for 2015, the average retail price per gallon dropped nearly \$1 to \$2.57. The low-price environment is expected to last for the entirety of 2016, when the average price per gallon is forecasted to decline an additional 2 cents to \$2.55.

Diesel saw an even bigger drop when comparing 2015 estimated figures to actual results posted in 2014. The average price per retail diesel gallon dropped an estimated \$1.21 per gallon in 2015. Diesel prices are forecast to increase slightly by 4 cents per gallon to \$2.76 this year, however.

As expected with a lower fuel price environment, c-stores continue to sell more gallons of fuel, but the lower price per gallon is causing dollar sales in this category to drop significantly when comparing 2015 estimated data to 2014 actual figures.

Despite fuel dollar sales declining, margins are up and the lower prices are a great boon to operators in other metrics such as in-store sales, as seen in other areas of the CSNews Forecast Study.

On a whole, c-store operators are optimistic about their motor fuel sales in 2016. Fifty-three percent of retailers polled expect their fuel gallon sales to increase this year on a per-store basis, with only 9 percent expecting gallon sales to decrease. This represents a 3.5-percent-age-point increase vs. 2015 on a per-store basis.

The low unemployment rate, strong fuel-based loyalty programs, more travel due to lower gas prices and a milder winter throughout much of the country were cited by retailers as the top reasons why fuel gallon sales should remain robust.

Of note, though, c-store chains are more optimistic regarding fuel sales than their single-store counterparts. Nearly two-thirds of chain retailers expect gallon sales to increase in 2016 on a per-store basis, vs. just 4 percent of chains who expect fuel gallon sales to decrease.

Conversely, only 27 percent of single-store operators expect fuel gallon sales to increase this year. A majority (54.5 percent) expect gallon sales to stay the same as in 2015, while 18 percent expect gallon sales to decline year over year.

## Industry Forecast: Cigarettes (% change)

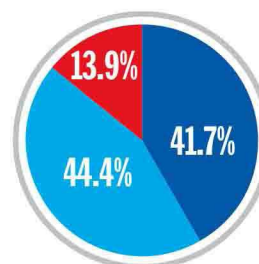
	2014	2015	2016
Unit volume per store	-3.1%	0.7%	0.3%
Industry unit volume	-1.9%	1.5%	1.2%

Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Retailer Forecast: Cigarettes

■ Sales will increase ■ Sales will decrease ■ Sales will stay the same

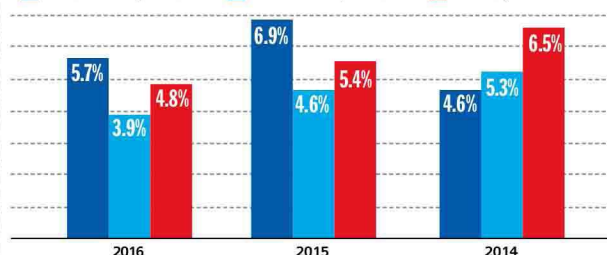
Net change: 3.4%



Source: Convenience Store News Retailer Forecast Study, 2016

## Industry Forecast: Other Tobacco Products (% change)

■ Unit Volume per Store ■ Dollar Sales per Store ■ Industry Dollar Sales

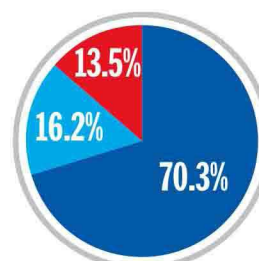


Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Retailer Forecast: Other Tobacco Products

■ Sales will increase ■ Sales will decrease ■ Sales will stay the same

Net change: 5.3%



Source: Convenience Store News Retailer Forecast Study, 2016

## FOODSERVICE

Convenience store operators continue to view foodservice as a growth category that represents a major point of opportunity in the coming year. A total of 82.4 percent of retailers polled believe their foodservice sales, which include prepared food and hot, cold and frozen dispensed beverages, will increase in 2016. This marks a slight uptick from the 81.3 percent who predicted the same one year ago, showing an increased level of optimism.

Even c-store operators that do not expect to see foodservice growth have an overall positive sentiment, as 17.6 percent of respondents expect sales to stay the same. Zero respondents said they expect their foodservice sales to decrease.

"[Foodservice] will only grow for those who do it right," one retailer commented.

Although larger c-store chains have more resources to commit to a foodservice program, retailers of all sizes view the category positively. In fact, more single-store owners expect to see increased foodservice sales than chain stores, at 87.5 percent vs. 80.8 percent respectively.

This positive view of foodservice stems from improving consumer perceptions coupled with execution, according to survey respondents. Customers increasingly view c-stores as a valid meal destination, increasing the demand for quality prepared food and beverages, which in turn validates their perspective.

Foodservice has a "big upside if performed correctly," said another retailer.

Some c-stores are approaching the category cautiously, testing items and adding foodservice only to certain stores rather than a full-scale rollout. Others anticipate a high rate of growth and in fact have created new management positions to spearhead the category.

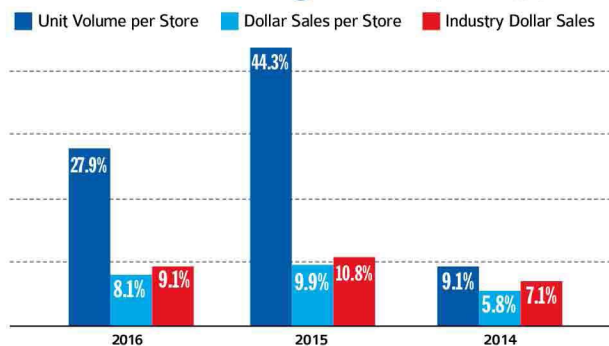
Retailers point to ethnic food as a potential big trend in 2016.

## TOBACCO

Any tobacco retailer knows the category has been faced with some challenges over the past few years, especially with cigarette volumes steadily decreasing and alternative products fighting for space. But 2015 told a different story and 2016 is expected to be a continuation of that tale.

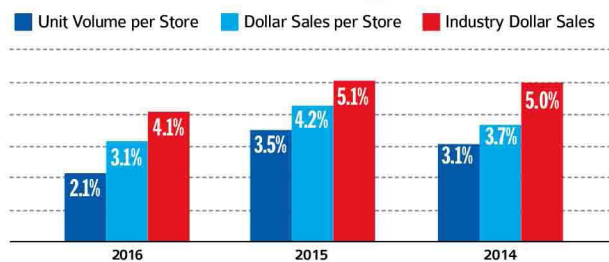
After many cycles of decline, cigarettes rebounded slightly in the past year with unit volume growth per store estimated at 0.7 percent and total industry unit volume growth estimated at 1.5 percent for 2015. That's quite a jump from 2014 declines of 3.1 percent and 1.9 percent respectively.

## Industry Forecast: Electronic Cigarettes (% change)



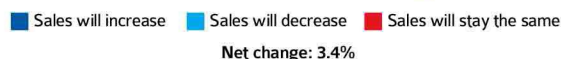
Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Industry Forecast: Beer/Malt Beverages (% change)



Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Retailer Forecast: Beer/Malt Beverages



Net change: 3.4%

Source: Convenience Store News Retailer Forecast Study, 2016

The upswing is expected to continue this year, albeit at a slightly lower rate, according to CSNews' research. Specifically, the 2016 forecast places unit volume growth per store at 0.3 percent and total industry

unit volume growth at 1.2 percent.

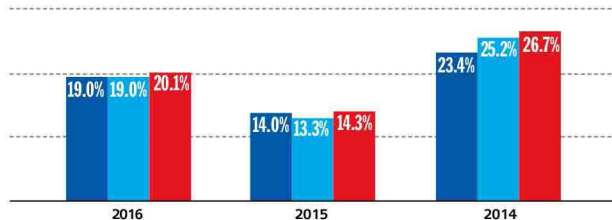
And no surprise here: Cigarette costs are expected to rise again. Manufacturer list prices are forecast to jump from \$36.14 per carton in 2014 to \$38.14 this year. Taxes are also increasing. Federal, state and local taxes combined per carton are forecast to rise from \$20.92 in 2014 to 21.32 in 2016. New York still has the highest state levy at \$4.35 per pack, a number that has held steady over the past few years and almost \$3 more than the average state tax.

From the retailer point-of-view, c-store operators are pretty evenly split on what they think will happen with cigarettes in 2016. Only 13.9 percent believe sales will stay the same.

Meanwhile, other tobacco products (OTP) continues to be a shining star behind the register. When the final numbers come in, 2015 is expected to have been a banner year for OTP. Estimates put unit volume per store at a 6.9-percent increase, with dollar sales per store ticking up 4.6 percent and total industry dollar sales increasing 5.4 percent.

### Industry Forecast: Micro Beer (% change)

■ Unit Volume per Store ■ Dollar Sales per Store ■ Industry Dollar Sales

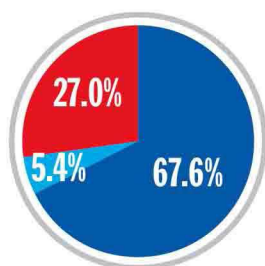


Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

### Retailer Forecast: Packaged Beverages

■ Sales will increase ■ Sales will decrease ■ Sales will stay the same

Net change: 4.0%



Source: Convenience Store News Retailer Forecast Study, 2016

These coming 12 months call for a similar forecast: a 5.7-percent increase in unit volume per store, 3.9-percent increase in dollar sales per store and 4.8-percent increase in total industry dollar sales.

The one OTP segment that seems to be struggling a bit lately, though, is cigars. Unit volume per store saw

## Key Economic Factors for 2016

**Labor** — Long-term unemployment reached historically high levels following the Great Recession of 2007–2009. Both the number and share of the unemployed who are long-term unemployed typically continue to increase after a recession ends, before falling during a labor market recovery, explained Maureen Maguire, chief analyst for *Convenience Store News*' annual Industry Forecast Study. Following this cyclical pattern, long-term unemployment has fallen in recent years, although it remains high by historical standards. Five years after the Great Recession ended, the number of long-term unemployed still makes up a larger share of unemployment than during any previous recession.

The unemployment rate has dropped to 5 percent, which is five percentage points lower than the cyclical peak reached in October 2009. The last time it registered 5 percent was in April 2008.

"We should see a continuation of moderate strength in the number of jobs created and the unemployment rate ticking down slightly to 4.8 percent by the end of 2016," predicted Maguire.

**GDP** — The growth in Gross Domestic Product (GDP) has been very moderate during most of the current recovery and is likely to be constrained going forward by lower exports due to the rising value of the dollar, coupled with slower growth abroad. Economists are looking for GDP growth to come in around 2.6-2.8 percent for 2016.

**Income** — At the end of 2015, real disposable personal income had grown by approximately 3.5 percent. Economists expect slightly slower growth in 2016 with inflation increasing. However, household net worth is likely to rise slightly given the increasing tightening of the labor market.

**Housing** — While the housing markets continue to strengthen, many of the statistics are still well below over-inflated peaks of the past. Starts are expected to rise by approximately 1.1 million this year and increase by about 100,000 units annually. Although demographics are placing an increased demand for housing, still-tight lending standards are forcing consumers to have exceedingly good credit and income to participate in the market.

a 6.6-percent increase in 2014, yet the segment was only estimated to post a 5-percent increase in 2015. 2016 forecasted growth is even lower at 2.6 percent.

Still, c-store retailers remain bullish on OTP. Roughly 70 percent of the retailers *CSNews* polled expect their OTP sales to increase in 2016, with only 16.2 percent predicting a decrease.

Retailers do agree on one thing: OTP performance in 2016 hinges on regulation, specifically the Food and Drug Administration's final deeming rule, which will impact electronic cigarettes and cigars as well as other segments of the tobacco category.

### COLD VAULT

When it comes to their cold vault prospects in 2016, c-store operators hold a largely optimistic view, with nearly one in seven (67.6 percent) believing their packaged beverage sales — including carbonated soft drinks, bottled water, sports and energy drinks — will rise, as opposed to 5.4 percent who expect sales to drop. The net change forecasted by retailers is 4 percent.

Chain retailers have a slightly more favorable outlook on the category, with 70.4 percent expecting to see a sales increase this year, compared to 60 percent of single-store owners.

Retailers note that much of packaged beverages' success this year will stem from the bottled water segment, for which a 7-percent increase in dollar sales per store is forecasted.

For packaged beverages overall, the per-store prediction for dollar sales is 6.5-percent growth, a little higher than what retailers are anticipating.

C-store operators are pretty equally optimistic about the beer/malt beverages category, as 63.6 percent of those polled expect their sales to increase this year. The net change forecasted by retailers is 3.4 percent. That's pretty close to what *CSNews*' research is forecasting: a 3.1-percent increase in dollar sales per store for 2016.

Delving deeper into the various segments of beer, one retailer commented: "Imports and craft dominate growth. ... Premium beer is flat (which is an improvement!)."

As consumers seek more diverse flavor profiles and new beverage innovation, micro beer (a.k.a. craft beer) is generating a lot of growth and excitement, albeit off a still-small base.

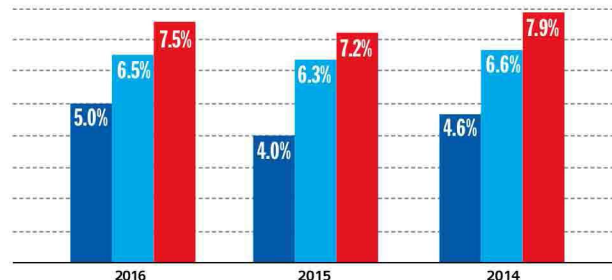
### CANDY

Expectation that the candy category will grow this year is down sharply from one year ago. Only 46.2

## Industry Forecast: Packaged Beverages (% change)

(includes carbonated soft drinks, bottled water, sports drinks, energy and other beverages)

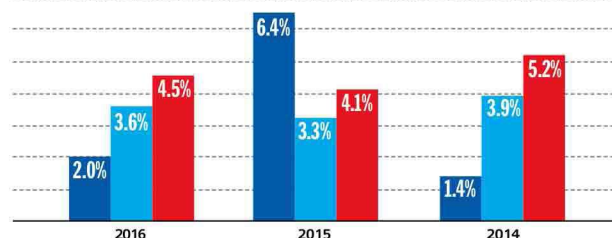
■ Unit Volume per Store ■ Dollar Sales per Store ■ Industry Dollar Sales



Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Industry Forecast: Candy (% change)

■ Unit Volume per Store ■ Dollar Sales per Store ■ Industry Dollar Sales

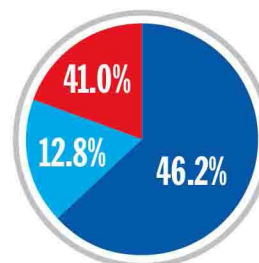


Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Retailer Forecast: Candy

■ Sales will increase ■ Sales will decrease ■ Sales will stay the same

Net change: 2.2%



Source: Convenience Store News Retailer Forecast Study, 2016

percent of c-store retailers believe their candy sales will grow in 2016, down from the 60 percent who said the same last year. However, the number of retailers that expect their sales to stay the same jumped from 19.6 percent last year to 41 percent this year.

Only 12.8 percent of retailers expect candy sales to decrease within the next 12 months.

Chain retailers hold a more favorable view of the category, as 46.2 percent of chain respondents anticipate a sales increase compared to only 33.3 percent of single-store owners.

"[There is] innovation, but nothing to really move the needle," one c-store operator remarked. "[The] value equation vs. other snacks is getting out of whack."

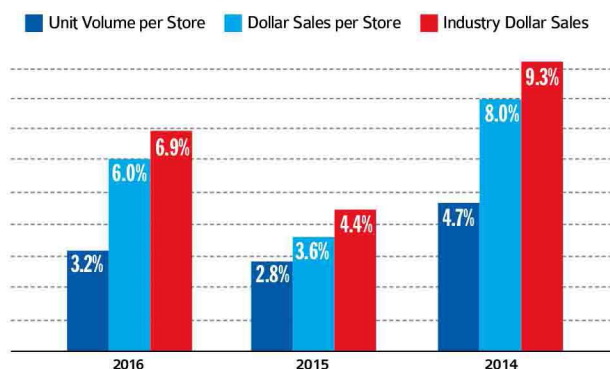
Retailers predict the net sales change will be 2.2 percent. According to the *CSNews* forecast numbers, per-store unit volume growth will slow to 2 percent for total candy, gum and mints in 2016, down from the estimated 6.4-percent growth for 2015. However, dollar sales growth per store is forecasted to see a slight increase of 3.6 percent.

Chocolate is expected to have another year of declining unit volume at -2.9 percent. The good news is this decline will still represent an improvement from 2015's estimated -6.2 percent. Dollar sales are expected to remain flat year over year.

In contrast, while growth of non-chocolate is slowing, unit volume per store is forecasted to increase 7.1 percent while dollar sales per store are forecast to increase 9.2 percent.

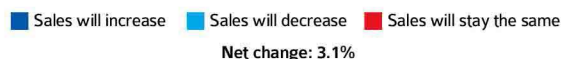
Meanwhile, the mints segment is forecasted to increase unit volume per store by less than 1 percent and dollar sales by 2.2 percent, both up from 2015 estimates. Unfortunately, gum is likely to see

## Industry Forecast: Salty Snacks (% change)



Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

## Retailer Forecast: Salty Snacks



Source: Convenience Store News Retailer Forecast Study, 2016

## Political Power

Looking ahead to the November 2016 presidential election, c-store retailers recently polled in *Convenience Store News*' exclusive Retailer Forecast Study expect a contest between Florida Senator Marco Rubio and former Secretary of State Hillary Clinton.

Retailers give the nod on the Republican side to Rubio (29.4 percent), slightly ahead of Ben Carson (23.5 percent) and Donald Trump (17.6 percent). On the Democrat side, Clinton leads by a wide margin with 82.9 percent of respondents, compared with only 14.3 percent for Sen. Bernie Sanders. Of course, the election is still almost a year away.

another rocky year of largely flat volume and dollar sales.

According to retailer feedback, the introduction of new products is expected to have an impact on the candy category in 2016, as will an increase in health awareness as consumers keep a closer eye on what they put into their bodies.

## SNACKS

Consumers' tendency to replace regular, full meals with on-the-go snacking is nothing but good news for the convenience retail channel. After slower sales growth in 2015, the salty snacks category, which includes potato chips, tortilla chips, pretzels, ready-to-eat popcorn, nuts and seeds, is expected to rebound and show stronger growth in 2016.

Total industry dollar sales grew an estimated 4.4 percent in 2015, according to the *CSNews* Forecast



Study. This was a drop from the actual 9.3-percent growth the category saw in 2014, but total dollar sales are forecasted to rebound in 2016 and reach nearly 7-percent growth.

On a per-store basis, unit volume is forecasted to grow 3.2 percent in 2016, marking a slight increase over 2015's estimated 2.8-percent increase. Higher prices have boosted dollar sales, which are forecasted to show nearly twice the growth at 6 percent per store, up from an estimated 3.6 percent in 2015.

Retailers expect the continued popularity of snacking to contribute to the growth of salty snack sales this year, with 64.1 percent of retailers saying they believe their sales in this category will increase and 25.6 percent expecting sales to stay the same. Chain retailers are even more bullish, with nearly three-quarters believing their sales will increase.

The new year will also bring "increased variety and less dependence on large suppliers with low margins," one retailer predicted.

Other retailers expect awareness of and innovation in healthy items to have a big impact.

#### EDIBLE GROCERY

More convenience store retailers are putting an emphasis on fresh and healthy eating and with that comes a focus on expanding edible grocery offerings. The trajectory over the past few years is noticeable. In 2014, retailers grew the category at a mere 1.6 percent in overall dollar sales and notched only a 0.4-percent uptick in dollar sales per store.

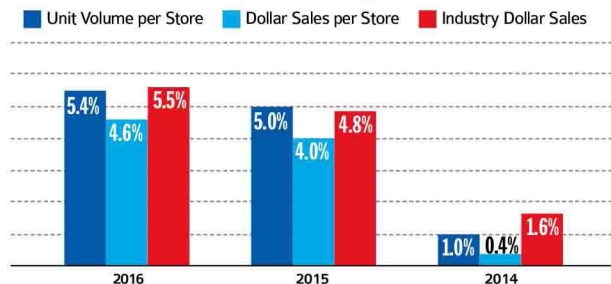
What a difference 12 months made. The numbers for 2015 put the estimated growth at 4.8 percent in total industry dollar sales and 4 percent in dollar sales per store. Unit volume is also estimated to have increased 5 percent last year.

2016 looks to bring more of the same. According to the *CSNews* results, edible grocery unit volume per store is forecasted to increase 5.4 percent, with dollar sales per store up 4.6 percent and total industry dollar sales growing by a healthy 5.5 percent.

The almost mirror images of 2015 and 2016 follow in line with c-store retailers' expectations. Nearly half of all retailer respondents to *CSNews*' study anticipate their sales in the category to remain the same this year, while only 15.8 percent expect sales to dip.

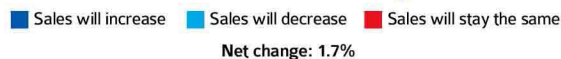
Within those numbers, approximately one-third of chain operators are penciling in an increase in 2016 sales, and single-store operators are even a little more optimistic.

### Industry Forecast: Edible Grocery (% change)



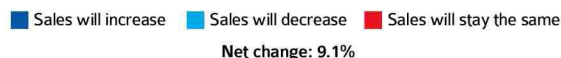
Source: Convenience Store News Industry Forecast Study, 2016  
2014 figures are actual; 2015 are estimated based on nine months; 2016 are forecast.

### Retailer Forecast: Edible Grocery



Source: Convenience Store News Retailer Forecast Study, 2016

### Retailer Forecast: Foodservice



Source: Convenience Store News Retailer Forecast Study, 2016

As for which trends retailers see having an effect on the category, many cite an increase in healthy product awareness as a positive trend. On the negative side, some do note that the smaller size of their stores do not allow for much in grocery offerings.