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Investigation of Strategic Partnership Opportunities
with Iowa Convenience Store Retailers:
Seeking Market Access for Iowa-Based, Value-Added Food
Products

By

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Introduction

Recent stories from the popular press have suggested that convenience stores may be an untapped opportunity for Iowa producers to market local products. The purpose of this study was to investigate the interest that Iowa-based convenience stores (C-stores) may have in purchasing locally grown or locally prepared foods.

Independent Iowa producers appear to be well situated to tap this rapidly growing market segment. Iowa is home to a significant number of C-store operations which span from the single store operator, to mid-sized operations with 5 to 20 stores, to large multi-state enterprises with 100 or more stores across the Midwest.

While convenience stores historically have relied on the sale of gasoline, tobacco and other convenience products to provide three quarters of their revenue, the industry reports new trends toward expanded food offerings as a way to improve both revenue generation and overall store profitability.

Sales of food products in C-stores have been steadily increasing as a proportion of revenue over the past 10 years. In many small rural towns where population declines have led to the closing of local grocery stores, the convenience store has taken its place as both a source of basic sundries and as a community node.

Meanwhile in some urban intercity neighborhoods, mainstream grocery stores have relocated to more lucrative locations leaving C-stores to supply both gas and convenience groceries. In other cases, C-Stores have incorporated fresh produce, gourmet coffee and prepared foods in response to increasing competition from Wal-Mart and other discounters which have migrated into gasoline and groceries.

In March, 2005, The Hartman Group reported on the trend toward more fresh foods in C-stores:

“7-Eleven, for example, recently announced it has rolled out national, computerized supply chain technology that allows it to fill small SKU volumes the next day, using local vendors and warehouses. This is allowing each store to customize its offerings in great detail, much like independent coffee shops do. 7-Eleven is also developing a network of fresh foods kitchens and vendors to supply its stores with daily loads of fresh foods as well.”

And in July, 2005, the Scottish Executive reported that sales of fresh produce in C-stores in the UK have met with success:

“Sales of fruit and vegetables at one participating store rose significantly simply by increasing the space for produce and moving it from the front to the back of the store. The managing director of David Sands, Ltd. in Kennoway, said his store joined the pilot program after a survey of his customers revealed that two-thirds wanted the store to sell more healthy foods.”

The rapid growth of the convenience store industry, coupled with a more focused product line, and the presence of a number of Iowa-based companies led us to believe that this might be a good market channel for local growers.

Major C-store chains based in Iowa or the upper Midwest include:

- Casey's General Stores (Ankeny, IA)
- Handimart (Cedar Rapids, IA)
- Kum & Go (West Des Moines, IA)
- Kwik Shop (Hutchinson, KS)
- Kwik Trip (Wisconsin), and
- Quik Trip (Tulsa, OK)

Casey's General Stores, Inc. owns and operates nearly 1,340 convenience stores in nine Midwestern states. Headquartered in Ankeny, Iowa, Casey's operates C-stores in Iowa, Illinois, Indiana, Kansas, Minnesota, Missouri, Nebraska, South Dakota and Wisconsin. According to the company website, stores offer prepared food items, such as made-from-scratch pizza, donuts, chicken tenders, and sandwiches, in addition to grocery items.

Casey's began in 1968 with its first store locations anchored in small Iowa towns. The small town emphasis continues, and as of July 31, 2004, nearly 60 percent of its stores are located in towns with populations under 5,000; 75 percent of Casey's stores are located in towns with populations under 10,000.

Casey's owns and operates its own distribution center and transportation system. Casey's fleet delivers approximately 70 percent of the gasoline and 90 percent of the in-store products it sells.

In the fiscal year ending April 30, 2004, Casey's sales exceeded \$2.4 billion including more than 990 million gallons of gasoline. Gasoline represented 63 percent of sales and 24 percent of gross profit. Grocery and merchandise represented 29 percent of sales and 50 percent of gross profit, and prepared food 8 percent of sales and a whopping 26 percent of gross profit.

HandiMart Food Stores is locally owned and operated by Nordstrom Oil Company of Cedar Rapids, Iowa. HandiMart currently ranks among the top ten marketers of Phillips 66 products in the United States.

In 1980, Nordstrom Oil Company entered the convenience store business by opening its first HandiMart Food Store in southwest Cedar Rapids. The company currently operates 34 HandiMarts in Cedar Rapids, Marion, North Liberty, Coralville, Iowa City, Hiawatha, Fairfax, Amana, Williamsburg and the Des Moines area.

Nordstrom Oil Company is also involved in several fast food franchises. Currently, there are nine Blimpie Sub and Salad locations in Cedar Rapids, Iowa City, North Liberty and Coralville.

In addition, Nordstrom owns one Nordy's Sub and Salad in Amana, one Hot Stuff Pizza and one A&W in Cedar Rapids, and their own Java Creek Cafe in Cedar Rapids.

Kum & Go was founded in 1959 in Hampton, Iowa. Today it has grown to more than 420 convenience stores in 13 states (Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, North Dakota, Oklahoma, South Dakota, Colorado, Arkansas, Wyoming and Wisconsin). In the 1980s, the company was one of the first convenience store operators to add quick serve restaurants. Kum & Go contracted with Blimpie, Taco John's and Burger King to offer the service.

The company now employs more than 4,000 associates. In addition to a wide selection of branded products, Kum & Go has developed its own line of private label products under the Hiland brand name, including gourmet coffee, water, potato chips, sandwiches and snack nuts.

Kum & Go has maintained a tradition of community reinvestment, each year returning 10 percent of its profits to local communities. Kum & Go is the United States 22nd largest convenience store chain.

Kwik Shop is a subsidiary of Kroger, Inc. – one of the largest grocery chains in the United States. Kwik Shop was founded in 1960 and currently operates 795 convenience stores in 16 states under six banners. The Kwik Shop banner, with regional headquarters in Hutchinson, KS, operates in Illinois, Iowa, Kansas and Nebraska. The stores offer a limited selection of private-label Kroger products. Some stores are served by Kroger distribution centers.

New Kwik Shop convenience stores have footprints that range from 1,700 to 4,800 square feet. Stores are typically located on an acre to an acre and a half lot, with 4-8 gas pumps. Kwik Shop prefers to locate convenience stores in small to medium-sized towns near interstate highways. Two-thirds of the stores are located in communities with fewer than 75,000 residents.

Kwik Trip, based in Wisconsin, was started in 1965, and now operates more than 350 Kwik Trip, Kwik Star, Hearty Platter, and Tobacco Outlet Plus stores throughout the Midwest. The **Kwik Star** banner is used in Iowa.

Kwik Trip, Inc. maintains total quality control over a wide variety of products by producing and packaging these items in their own state-of-the-art facilities.

In addition to a corporate support center, which handles the administrative needs of stores and co-workers, they have their own bakery, commissary, dairy, distribution warehouse and vehicle maintenance divisions.

QuikTrip, headquartered in Tulsa, Oklahoma, owns and operates over 450 convenience stores in nine states. There are no franchises. Almost all QuikTrip stores are located in large urban markets. The Iowa division of QuikTrip is based in Des Moines and operates stores in the Des Moines and Cedar Rapids metro markets.

QuikTrip is ranked 38th on the Forbes List of Privately Held Companies. They promote themselves as having strong civic ties and an emphasis on social responsibility, with stores

contributing 5 percent of profits to local charities.

In addition to these medium to large market players, other participants in this study included several smaller, independent operators with 10 or fewer store locations.

Scope of Work

The purpose of this study was to identify and begin to understand the most important market requirements of suppliers to the convenience store channel. By understanding these market requirements, the authors would like to begin identifying opportunities for distributing locally grown or produced value-added food products.

This study was focused on two geographic locations in central Iowa:

- A rural area, consisting of Guthrie and Audubon counties; and
- An urban/suburban area, consisting of Polk and Dallas Counties.

The authors had two primary hypotheses they wanted to test:

- By building strategic relationships with local producer groups supplying high-quality goods, such as prepared foods, meats, fruits and vegetables, convenience store operators could compete against national discounters and other retailers in ways that do not require significant capital investment.
- By building strategic relationships with C-store operators, Iowa-based producers could develop new market outlets for their products.

As described further in the objectives and strategies sections below, this study has identified a number of operators interested in partnership opportunities that could lead to new product introductions by Iowa producers. The survey has yielded some interesting results for exploring the most promising market opportunities in this channel.

Project Team

Project Team Members included:

- Mary Holz-Clause, Iowa State University Extension Value Added Agricultural Program Manager – Principal Investigator. Holz-Clause develops value-added ag businesses, conducts marketing studies.
- John Norwood, Triple Bottom Consulting – Project Manager. Norwood is an expert consultant engaged in the development of new business models, strategies and policies for local food systems.

- Susan Futrell, One Backyard Consulting – Project Consultant.
Futrell is a marketing and food systems consultant with 25 years experience in grocery distribution and marketing in the organic and natural food industry.

Additional support and guidance has been provided by The National Catholic Rural Life Conference and the Iowa Network for Community Agriculture (INCA.)

Method of Survey

The first need of this survey was to identify the appropriate management personnel who could help the project team address the key areas of opportunity and market requirements for Iowa producers and their value-added products.

- Task 1 included identifying the universe of convenience stores in the study area (approximately 180) and within that universe the number of unique store owners to contact for inclusion in our survey (approximately 30).

Ownership status ranged from single store owner/operators to multi-chain operations, such as Casey's General Stores (46 stores in study area) and Kum and Go (48 stores in study area). See Table 1.

- Task 2 included a telephone contact to locate the appropriate owner or key management representative. This initial work was followed by a mailing introducing the initiative and inviting participation via in-person or phone interviews.

Where possible, follow-up phone calls were made to schedule in-person or phone interviews. In scheduling the final interviews, many operations required multiple phone calls. In total, (6) in person and (1) telephone interviews were completed.

Survey Participants

Our survey indicated a significant interest in identifying partnership opportunities, given local producer groups ability to meet key market requirements. In total, the seven completed interviews represented approximately 108 stores out of a total universe of 180 stores in the study area (60 percent).

Please see appendix A for a full listing of stores in the study area.¹

¹ Farner-Bocken was mentioned as a major supplier by several of those C-stores surveyed. As an important partner in the C-store distribution channel, it will be important to investigate their market requirements.

Table 1
Survey Participants

	Name of Store Operation (Corporate Ownership)	Headquarters' Location	# Stores in Study Area	# Iowa Stores	Type of Interview
1	Audubon Country Store (Richards Enterprises Corp.)	Irwin	1	10	In Person
2	Blue Jay Market	Perry	1	1	In person
3	Casey's General Store	Ankeny	46	363	In Person
4	HandiMart	Cedar Rapids	6	34	In Person
5	JC's Corner Store (Valley West Oil Company)	West Des Moines	4	4	In Person
6	Kum & Go (Krause Gentle)	West Des Moines	48	237	In Person
7	Sparky's One Stop (Al's Corner Store)	Carroll	<u>3</u>	<u>25</u>	Phone
	TOTALS		108	651	

Findings

In completing the interview process, the research team discovered that there was a great deal of consistency in the answers provided by respondents to the survey instrument. This feedback was distilled into strengths, weaknesses, opportunities and threats associated with the convenience store channel.

Product Lines

Because C-stores often average between 1,000 and 3,500 sq. ft., shelf space is at a premium. Unlike larger discounters or grocery stores which can span from 40,000 to 100,000 sq. ft. or more, typical C-store product categories are highly focused with fewer product choices within most product lines.

Most C-stores feature a selection of convenience-based items that include: "sin" products, such as alcohol and tobacco; dairy products, such as milk, eggs and cheese; refrigerated soft drinks; snacks; grocery items and frozen goods, including ice cream; and a selection of baked or prepared foods, including sandwiches, burritos and pizza. Depending on local demographics, some operations have chosen to expand into additional categories, such as automotive supplies and clothing.

Similarly, the prepared foods category will often vary in size, scope and emphasis depending on the C-store operation and the local demographics. A rural C-store, for example, may include a restaurant with limited seating, or an expanded prepared foods menu to service the community. A number of urban C-stores use freshly prepared pizza and baked goods as a draw.

Fresh products including produce and cut flowers are found in some operations, but keeping those items fresh is a challenge. Many C-stores use regional distributors, such as Farner-Bocken or Loffredo's to supply fresh fruit, such as bananas or apples.

Categories with strong presence in these stores and therefore opportunity for sales of local products include snack foods, baked goods, produce (apples) and milk. Three other product categories also show unexpected promise: 1) hamburger, fresh and frozen; 2) cut flowers; and 3) prepared foods, such as frozen casseroles and other microwavable dinner selections.

Market Demographics

C-stores layouts are largely a function of their local marketplace—location, location, location. From the single store operator up to the multi-store chain, C-stores must remain vigilant to customer wants and needs and how their operation can uniquely serve and retain traffic in the face of stiff competition.

Many C-stores compete with one another other across local markets. One operator noted that up to 90 percent of customer traffic to his highway stores near I-80 and I-29 were “travelers,” while local regular customers comprised about 75 percent of traffic for community stores in rural areas.

In addition, in many rural areas C-stores compete with grocery stores in their immediate market area, particularly those such as Hy-Vee, which are expanding into gasoline service, as well as large-scale discounters such as Walmart that may be able to pull customers from 20 miles away or further.

For example, one operator in a rural Iowa location noted a drop-off in business after a Wal-Mart opened more than 10 miles away. Fortunately for that operator, the bulk of the decline in traffic was temporary.

Competitive Advantage

For the individual operator, his or her competitive advantage may be easier to identify and sustain (e.g., a personal connection with the community or the customer base). For the large operator, competitive advantage can be more elusive; it is often difficult to focus on just one type of competitor because of the wide geography of the store base.

For the multi-store operator, customer retention may focus around management's efforts to maximize the customer experience through its brand positioning: the product mix, the level of product quality (e.g. made from scratch pizza,) or the presence of certain branded products, such as nationally recognized branded gas.

Some multi-store operators will customize store layouts to suit local market conditions. One such operator broke out the store base into six types, each with its own unique store footprint and product mix: 1) Urban; 2) Resort; 3) Neighborhood; 4) University; 5) Rural; and 6) Interstate.

Local Food – Opportunities

Virtually without reservation, survey respondents expressed an interest in carrying more local foods. Said one operator, “That’s our customer.”

Most operators cited as their #1 reason the importance of supporting the local economy and #2 fulfilling customer requests for more local foods.

Others felt a local foods presence could help differentiate the store from competitors or result in a better quality, fresher product provided there was sufficient customer demand.

Local Food—Constraints

There are a number of hurdles facing those who want to supply C-stores with local products. These include:

- **Unreliability of Supply** – One of the most often cited reasons why C-store operators do not purchase local products. In addition, for those who have had some past experience with local producers, quality of the supply and the ability to maintain freshness have also been a concern.

Because inconsistent quality can negatively impact store operations and drive up operating costs, operators usually try to limit the number of suppliers with whom they choose to do business. However, despite the prevalence of company policies which serve to minimize the number of individual vendors, most operators expressed a willingness to try something new at least once.

The level of freedom that individual store managers have to purchase products varies significantly by operation, location, product category and the terms of delivery. Sometimes the decision making about whether to carry a new product is made at the corporate level – the reasons for this may have to do with supply logistics, accounting controls or ensuring store-to-store consistency.

At other times, individual store managers with Profit & Loss responsibility may have the freedom to test market new items. If the product is successful, the corporate office may explore the feasibility of standardizing the product across stores to ensure greater brand cohesion.

- Limited Shelf Space – Most C-stores have very limited shelf space. It is important that the items turn frequently and have a reasonable margin. Many of the locally produced items such as fruits and vegetables may not meet these standards.

Many C-stores also require point of purchase material to support the product and expect the supplier to identify the appropriate location and positioning of the product within the store. Noted one operator, “Tell us where we put the product in the store. Who furnishes the equipment and promotional support? How do we ensure freshness if that is a concern?”

- Price – Prices which are too high can impact product turnover and profitability.
- Regulatory concerns – Suppliers to C-stores normally need to carry product liability insurance and have the ability to meet regulatory requirements for food safety.
- Distribution – In addition to locating product space in the store, getting the product to the store can be an issue. Warehouse shelf space is limited and distributors may not be willing or able to carry perishable products with low margins.

Many fresh, local products do not have a long enough shelf life to be placed in the warehouse or do not have a high enough profit margins or volume to justify handling costs. In those situations, direct store delivery may be required.

Recommendations

Product development is an ongoing process in the convenience store channel. There was widespread interest in participating in a pilot program with local growers or food producers. Even the largest operators expressed a willingness to start small.

As one operator noted, “We’re always willing to try something new....we need to figure out what works. We don’t have a problem working with a new vendor as long as they are reliable.”

However, it is clear from the research that successful C-store operators are very mindful of the competitive environment. There’s a balancing act between the need to identify new ways to attract and/or retain customers and the desire to minimize operational risks.

The challenge for the local grower or food producer is to identify emerging areas of opportunity, as well as a potential solution that will meet the needs of C-store operators and their customer base.

For example, many of the convenience stores are offering ready-to-eat items such as sandwiches, rolls and pizzas. There exists a potential market to be either an ingredient supplier for these products, or to produce finished products, fresh or frozen.

Since meeting supply and quality standards can be an impediment to entering the C-store channel, independent producers may need to join together collectively in producing, marketing

and distributing product. Important considerations include product positioning, pricing, placement and promotion. Guaranteed sales and/or the willingness to replace aging product could help with store introductions.

Another consideration related to production is how to improve and ensure product quality and consistency. This can be done through more intensive and decisive management, as well as better control (shipment, refrigeration/cooling) of the product after it is prepared or produced.

Next Steps

In order to access the convenience store market, the individual producers or manufacturers will need to consider business relationships, structure and models that can deliver consistency, quantity of product and product support (transportation and marketing) demanded by retailers.

The longer-term business development challenge in bringing new value-added products to the market place will be to attract the necessary capital, the management expertise, and partnership arrangements that will maximize the chances of operational success, while also ensuring that economic benefits flow through to the producer and reward his/her sustainable farming practices.

The Alces Foundation has provided additional funding that may be used for model development, pilot testing and further model expansion.