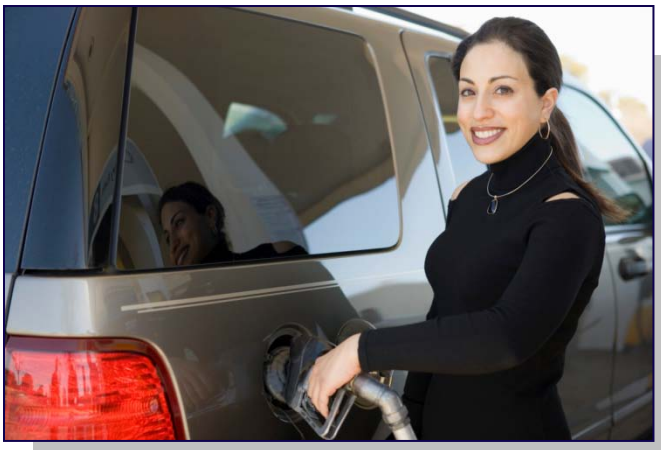
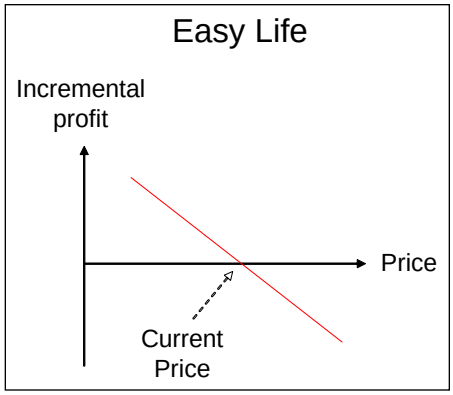
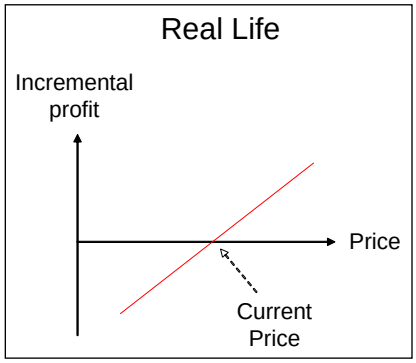


DRIVING STORE TRAFFIC THROUGH COMPETITVE FUELS PRICING STRATEGIES

Retailers face the challenge of how to increase gross profit while maintaining market share, revenue and volume. In an ideal world, a price reduction would lead to both increased profit and increased volume.



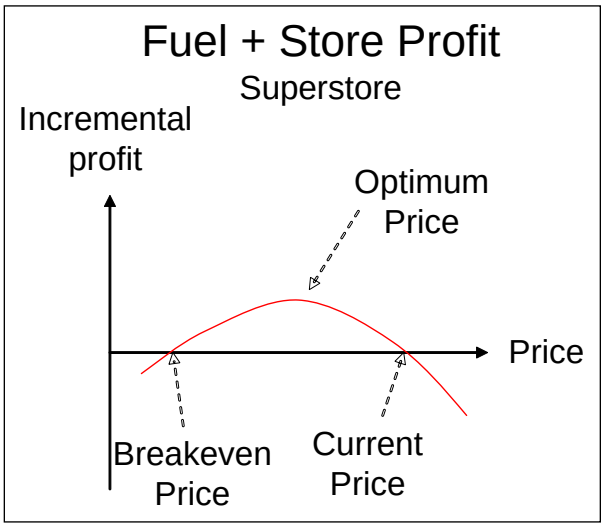
These 'easy life' conditions do appear periodically, when unit margins are high enough, but they do not persist. In such situations, everyone reduces price to get more profit and the market moves back to normal 'real life' conditions, where it is necessary to increase price to get more profit, but the retailer is constrained from doing so because a price increase leads to reduced volume and makes them uncompetitive in the market. The hard reality of the rapid turnover environments of fuel and grocery retail is that, for most of the time, price reductions or promotions can grow volume, but at the cost of lower gross profit.



Price your fuel to meet a combined fuel + store objective

For fuel retailers who also sell grocery and convenience items, there is a potential route to changing the slope of the profit-price curve and moving from the 'real life' scenario into the 'easy life' scenario depicted above. It is to base your fuel pricing strategies on the maximization of combined fuel + store gross profit, rather than just fuel profit. For this to work, the extra fuel customers that you gain through more competitive fuel pricing have to generate more in-store profit than you have lost through discounting the fuel.

For superstores, the in-store spend per extra fuel customer is usually enough to make this proposition work and to reverse the gradient of the profit-price curve as shown in the next graph.



Superstore operators of course know this already, and the in-store merchandise teams frequently demand that the fuel merchandise department discount their fuel in order to drive store traffic. However, there is usually neither scientific management of the size of discounts, nor monitoring of the value generated in-store by a given level of discount. For this type of end user, there is scope to apply fuel demand forecasting and fuel-store modeling science to identify the optimal level of fuel discount required to maximize fuel + store profit on a site by site basis, and to adjust this in real time in light of

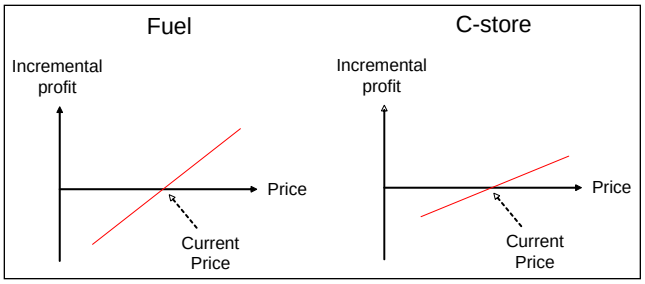
changes in fuel demand, costs, competitor pricing and fuel to store correlations. It is also possible to identify the maximum sensible fuel discount corresponding to the breakeven point at which further gains in fuel customer numbers generate less in-store profit than is required to offset the loss of fuel profit.

Give away less in convenience store promotional pricing

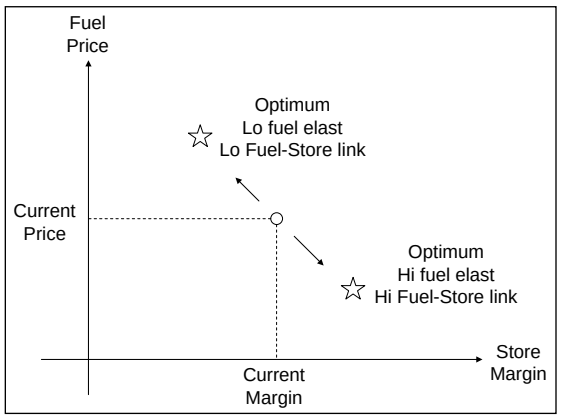
For fuel sites with convenience stores, the in-store spend per customer is often not high enough to reverse the slope of the profit-price curve and create a scenario where fuel price reductions alone are profitable, even when profit is measured on a combined fuel + store basis. However, convenience store operators are typically already giving away a significant amount of in-store gross profit margin through regular promotional pricing of the main convenience store categories – cigarettes, milk, beer, soft drinks, etc. Therefore there is scope to increase overall fuel + store profit by combining fuel price reductions, which drive more store traffic, with reduced in-store promotional pricing, thus using the extra store customers delivered by the fuel price discounting to maintain store volume at lower levels of in-store promotional pricing.

The steps required to implement such a strategy are as follows:

- Estimate the correlation between fuel volume and store traffic
- Segment sites into quadrants by high/low fuel to store correlation and by high/low fuel price elasticity
- At those sites with high fuel to store correlation and high fuel price elasticity, we get the following type of picture



- The high fuel price elasticity means that the cost in gross fuel profit of a given increase in fuel customers is relatively cheap
- The high fuel to store correlation means that a relatively high proportion of those customers go into the store
- The increase in store traffic creates scope to reduce in-store promotional pricing, i.e. increase main category prices and thereby increase store gross profit margin, whilst maintaining store revenue and volume.
- Application of appropriate demand forecasting and optimization science determines the required combination of fuel price reductions and reduced in-store promotional pricing such that the profit given up on the fuel side is offset or exceeded by the profit gained in the store, whilst maintaining store revenue and volume.
- For those sites with low fuel to store correlation and low fuel price elasticity, there is scope to apply the opposite strategy of increasing fuel prices to gain profit, in the knowledge that the consequent reduction in fuel volume will be relatively low and the impact on store traffic will also be low. In some cases, the gain in fuel profit may be enough to fund further in-store promotional pricing to drive store volume
- Over the network as a whole this will result in a shift in optimal price-volume positions as shown in the following picture



Currently retailers who sell both fuel on a forecourt and grocery items in a convenience or superstore, tend to manage the pricing of each separately. When viewed in separate silos, the retailer is faced with two instances of the same conundrum, namely that attempts to increase gross profit through higher pricing come at the cost of lower volumes, revenues and market share. By looking at the two silos together, the retailer can find opportunities to buy volume cheaply on one side, and use these extra customers to maintain volume whilst increasing margins on the other side.

ABOUT KSS FUELS

KSS Fuels is the leading global provider of pricing software, analytics and consulting services to fuel retailers and wholesalers in the oil & gas, convenience store, grocery and retail industries. Providing "Knowledge beyond the numbers," KSS Fuels helps fuel marketers and distributors implement effective pricing solutions and increase profitability through the use of knowledge and numbers. The company's US headquarters are located in Florham Park, New Jersey, and its international headquarters are based in Manchester, United Kingdom. For more information about KSS Fuels, please visit www.kssfuels.com.