

Retailers Discover New Ways to Drive Consistent Margins on Fuel Sales

Improving gasoline margins and throughput volumes remain top-of-mind for convenience store operators, high-volume retailers and grocers

Introduction

Despite challenges including unprecedented fuel price volatility, a demanding economic environment and tight credit markets, one thing remains constant for fuel retailers: the need to create and protect consistent margins within the fuel category.

Among mid-size and nationally branded retailers alike, there is an urgency to create rigor around business processes in order to better control and interpret costs related to the procurement and management of fuel. Concurrently, the difficulties in acquiring credit and working capital constraints have placed CFOs and business unit managers in a difficult position when it comes to predicting operational expenditures.

As the competition intensifies for the fuel dollar, it is now imperative for retailers to deploy more strategic procurement, logistics and financial management solutions in order to drive lower costs, streamline operations and ultimately enhance profitability.

Converting Volatility into Opportunity

For retailers, improving the economics of fuel procurement and management centers on the ability to better capture and minimize fuel costs by understanding demand patterns, centralizing supply contracts, determining best price on market versus contract and reconciling invoicing and taxes--factors driving out costs throughout the fuel supply chain. Yet there remains today a general lack of automation which inhibits developing a detailed understanding of the net landed cost of fuel making it difficult to minimize the costs of fuel ownership. Price volatility further clouds visibility into these operational costs.

Downstream industry expert, Tom Kloza Chief Oil Analyst for OPIS, posits that volatility cycles will persist.

"Despite lower outright prices, 2009 is proving to be by far the most volatile year for gasoline and diesel fuel prices on record. On any given 24 hour period in 2009, more than 60 percent of a gasoline retailer's gross margin can be at risk. We expect this volatility to continue, and the major challenge for marketers is how to handle or even leverage this volatility," said Kloza.

What's more, supply chain complexity coupled with price volatility often obscures the actual cost of a replenishment gallon. Without true visibility into volumes and inventory valuation, retailers face:

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Chief Oil Analyst
OPIS**

- ▼ difficulty driving consistency into procurement due to frequent pricing changes and allocations
- ▼ increased likelihood of retains and run-outs due to inconsistency of logistics and transportation
- ▼ increasing cost and complexity of maintaining regulatory compliance
- ▼ an inability to effectively value inventory and manage in-ground volumes.

FuelQuest's FMS solution squarely addresses these business critical issues by providing automated inventory control and greater access to an array of supply options with all fuel suppliers integrated into one system. FMS is integrated with hundreds of suppliers and carriers, supply terminal and more than 700 fuel carriers within North America. It also acquires and synthesizes nearly one million price feeds from the major pricing providers or directly from suppliers. All told, FMS manages more than 15 billion gallons of fuel annually. This advanced level of industry intelligence and integration to all supply options ensures not only superior leverage to drive consistent and better pricing, but also enables more predictability in supply.

Maximizing Working Capital

Increasingly, the working capital line item on the balance sheet remains both a constant focal point and a moving target. As a result, retailers seeking to minimize credit exposure realize the need for a more systematic approach to working capital management.

Increased credit exposure tied to working capital levels can severely impair the retailer's ability to protect margins if in-ground volumes are not managed and valued appropriately. Without the intelligence FMS provides, retailers tend to err on the conservative side in terms of inventories in order to avoid run-outs. However, overstocking can lead to a marked increase in inventory carrying costs. A national retail FMS customer that recently acquired 80 stores documented an immediate \$1.5M in cost savings by reducing inventories of mid and premium grade products. Through FMS's forecasting and real-time visibility into inventory levels, they were able to reduce conservative safety stock levels.

Minimizing days supply of various grades based on consumption patterns is another method that dramatically reduces working capital. What's more, reducing days supply on hand below the three day mark is critical in terms of credit because the retailer can often procure and sell the fuel before they actually have to pay for it. In one such case, a grocery chain using FMS was able to reduce working capital through a one-time inventory reduction and reduced average daily supply of premium from 12.5 to 2.5 days supply on average. By reducing the supply below three days they minimized their credit exposure and improved payment terms.

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**Dominick A. Chirichella
Energy Management Institute**

When armed with real-time working capital visibility, retailers can efficiently manage replenishment cycles to mitigate price risk and reduce retains and run-outs. For example, a vertically integrated oil & gas company noted a 66% reduction in retains and

50% reduction in run-outs after deploying FMS which provided an annual benefit of more than \$1 million.

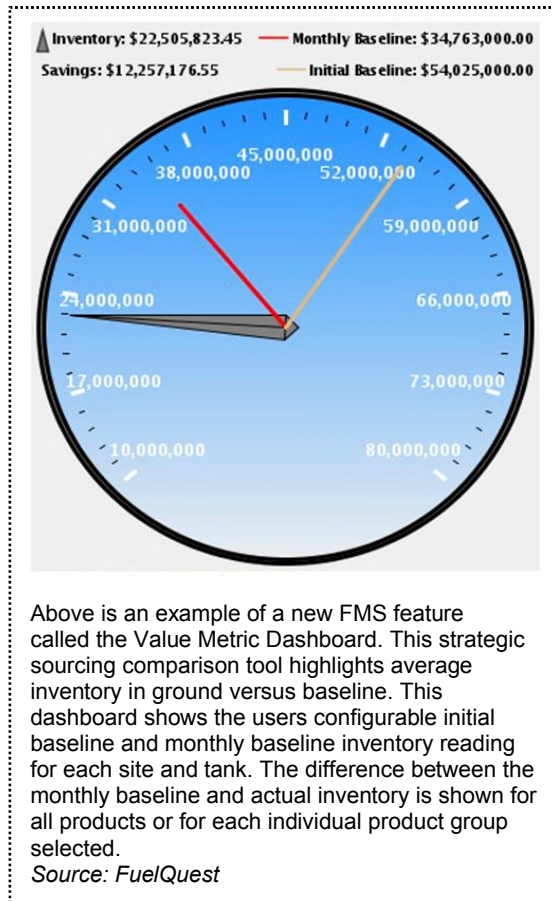
Strategic sourcing a game changer for retailers

By sourcing fuel at the lowest landed cost while managing volume commitments, retailers can truly optimize inventory (working capital), reduce retains and run-outs and improve transportation logistics. OPIS' Kloza goes on to point out, "buying smart, or making the critical decisions on when to dispatch or delay transports of fuel, has never been more critical. Marketers have to vigilantly manage these daily decisions or they will be left in the dust created by inconsistent but wild price swings."

Considering this miniscule margin for error, today's retailer requires a new level of sophistication in terms of forecasting, scheduling and demand fulfillment.

Based on demand patterns, FMS automatically analyzes all given supply alternatives and consistently recommends the lowest cost option. Simply put, the synthesis of this intelligence enables more informed decision-making and enhances the retailer's ability to manage against gross margin requirements.

The FMS solution's "Best Buy" capability determines the best price on market versus contract. By centralizing supply contracts, retailers can monitor their fixed price contract status throughout the month and identify ideal times to accept inventory from the supplier. FMS also presents spot market pricing options, providing a comprehensive dashboard of supply alternatives throughout the month. According to Dominick A. Chirichella of the Energy Management Institute, arming retailers with this supply insight is essential to remaining competitive.



"The time has never been better to work with a portfolio of purchasing options allowing one to fully take advantage of the normal daily divergences that exist between pricing indices, especially during times of high volatility," says Chirichella. "In addition to optimizing one's purchasing capabilities it is an opportune time to begin utilizing all of the risk management solutions that are available for hedging one's upside price exposure."

Because intraday price fluctuations can vary as much as 5%, FMS also recommends delivery windows in order take advantage of significant price swings based on the

customer's unique demand patterns. Once the product is delivered inventory is automatically re-priced to create a real time valuation from a working capital perspective.

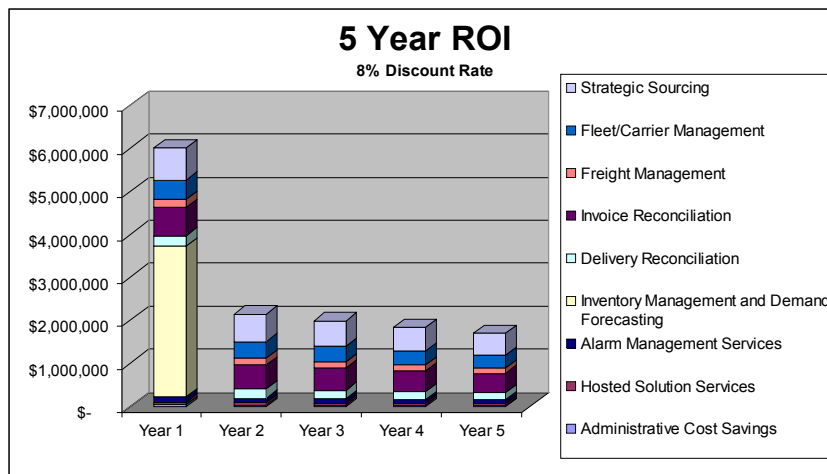
Possessing this level of efficiency and agility is key when considering potential operational expansion. This is where an effective fuel management solution helps scale the business without scaling costs. With on-demand software there is a virtually unlimited ability to manage higher volumes and sites via workflow automation, financial matching and reconciliation. Using FMS, regional supermarket chain Hy-Vee expanded its retail fuel locations from 5 to 86 without adding additional overhead. In fact, a two-person team equipped with FMS was able to manage this level of meteoric growth over a five-year period.

Comprehensive financial management and three-way matching

When dissecting the net landed cost of fuel, the last mile of the fuel supply chain is often the most overlooked. Inaccuracies related to price, volume and freight reconciliation can also erode margins over time. FMS allows a user to seamlessly create and place an order, track delivery, and capture and compare the bill-of-lading (BOL) and invoice to determine the right product, volume and agreed upon price were delivered and that it was properly taxed. This level of automation affords retailers the ability to significantly reduce manual accounting efforts and simplifies management of accruals as well.

FMS's three-way matching feature electronically delivers unrivaled data integrity to provide customized matching of line items for reconciliation and sharp visibility into the total fuel spend. Additionally, the proliferation of split loads and biofuels can be further complicating factors when it comes to reconciling excise taxes. With FMS, the incorporation of biofuels into the fuel stock is now demystified in any scenario and freight and taxes can be calculated within the system. Regardless of the fuel stock composition, carrier, grade or octane the solution automatically takes these variables into account and can re-value inventory accordingly.

Beyond reconciling financial and physical transactions, FMS can provide a scorecard a site's performance versus previous time periods in order to identify volume and pricing trends as well as areas for improvement. Coupled with the three-way financial matching, it delivers true visibility into the net landed cost of fuel, identifies inaccuracies and helps retailers maintain fuel margins despite swings in price volatility.



*Sample 5 Year ROI date for a fuel retailer with 1,000 sites

Source: FuelQuest

FuelQuest provides fuel management solutions and services that enable companies to improve margins, achieve supply predictability and ensure regulatory compliance in the acquisition and management of bulk fuel. FuelQuest's Fuel Management System (FMS) is the largest fuel management network in North America. Find out more at www.fuelquest.com or 713.222.5761.



Mitigating the potential impact of price volatility on gross margin and providing predictability of operating costs is paramount. Retailers are rapidly discovering that deploying proven fuel management solutions improves operational efficiency and management of working capital. As a result, it becomes possible to reduce the total cost of owning a gallon of fuel.

This comprehensive level of supply chain visibility captures the cost of fuel and enables the retailer to price at market and maximizes cost savings, or based on demand elasticity, price slightly below market to drive traffic. Today, some of the most innovative retailers in their respective sectors--ranging from HVRs, to C-stores and grocery chains are seizing this competitive advantage by lowering costs and streamlining operations in order to drive consistent fuel margins.

For more information about FuelQuest and FMS, please visit www.fuelquest.com