FINDING DOUGH

Without the proper financial support and strategy for your foodservice program, fryers, rollers and broilers can wait.

By Jerry Soverinsky

IT'S NO SECRET that foodservice has emerged as an alluring pursuit for convenience retailers. With gas margins in constant flux, tobacco sales waning and card fees a persistent nuisance, the generous margins associated with the sale of hot dogs, pizza and made-to-order sandwiches have elicited a nearly collective industry declaration that foodservice is no longer an option but an operational mandate.

With much of the discussion focused on execution — grilling versus frying, reducing wait times with digital ordering kiosks and promoting offerings via social media, for instance — overlooked is a more fundamental concern that begins long before the first maki roll, hoagie or hard-boiled egg is served: money. For no matter how salient the offering, without the proper financial backing and strategy, fryers, rollers and broilers can wait.

GETTING THINGS STARTED

"Start with a process," instructed Ed Burcher, president of Burcher Consulting, speaking at last year's NACS Show. "Treating this as a process ensures that it can be repeated, replicated and reviewed ... Setting your foundation, strategy and direction is really important given the commitments you will need to make foodservice successful." Part of the process should include looking at foodservice as distinct from your existing operations; it will help put the challenges into perspective.

"If you're going to do foodservice in a c-store, it's like a totally separate business," said Kay Segal, founder of Segal Insights. The first step, she says, is to decide whether to pursue full-service foodservice or limited service. "There's a lot more labor in full service, but also more margins ... and limited service won't require a lot of extra labor, but you'll have lower margins."

The decision should reflect a careful analysis of your operations — do you have the staff to deliver on the program, do you have adequate space for the requisite equipment, and so on — along with financial projections. "Spend the time and energy for a site propensity study, analyzing what your potential is," Segal said, "It will help if you need to look for funding."

FOODSERVICE SNAPSHOT

	% of Foodservice Sales		*Avg. Store Sales**		*GP Margin $**		*Gross Margin %*	
	2013	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**
Prepared Food	65.5%	65.7%	$256,749	$276,806	$150,676	$159,375	58.69%	57.58%
Commissary	5.7%	5.9%	$22,453	$24,672	$8,803	$9,964	39.21%	40.39%
Hot Dispensed Beverages	13.4%	13.0%	$52,633	$54,678	$29,389	$30,788	55.84%	56.31%
Cold Dispensed Beverages	12.3%	12.2%	$48,310	$51,167	$26,026	$27,356	53.87%	53.46%
Frozen Dispensed Beverages	3.1%	3.2%	$12,217	$13,484	$6,658	$7,235	54.50%	53.66%
TOTAL	**100.0%**	**100.0%**	**$307,467**	**$337,050**	**$173,641**	**$190,270**	**56.47%**	**56.45%**

(Source: *NACS State of the Industry Report of 2014 Data*)
*These numbers do not total as they are based on differing sample sizes by each line item.

According to the NACS Category Definition and Numbering Guide 7.1, foodservice includes five categories of consumables: prepared food, commissary, hot dispensed beverages, cold dispensed beverages and frozen dispensed beverages.

Foodservice is a worthwhile investment for c-stores. Its categories offer some of the highest margins for retailers. Foodservice comprised three of the top five categories in 2014. Prepared food and hot dispensed beverages — mostly coffee — were numbers two and three in terms of gross margin percentage, at 57.6% and 56.3%, respectively.

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HIDDEN COSTS

Integral to the development of financial forecasts must be the recognition that a foodservice investment is not a traditional investment, Burcher said, with myriad unique considerations that can quickly escalate costs. While a traditional NPV (net present value) tool can help guide development and chart expenses that include spoilage, license fees and labor costs, the course is "not that linear," with adequate parking, prep space and storage as "critical factors [that] may increase your investment in the offer as you add capacity and improve your facilities."

Additionally, waste, spoilage, shrink, labor and royalties need to be assessed, though Burcher cautions against underbudgeting for them, as they "are not as easy to estimate or define."

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Will your program require a modest store remodel or a complete rebuild? The costs can vary widely, from $25,000 for what Burcher categorizes as a "facelift" (paint, paper, small equipment) to $1 million or more "raze & rebuild" (entirely new concept).

Be realistic about your total investment, which includes tangible items — equipment, packaging — along with costs associated with infrastructure changes, training, leadership and perhaps most significantly: time. "I'm not trying to scare you folks," Burcher said at the NACS Show educational session. "But knowing there will be other costs allows for the alignment and leadership to build a [successful] program."

SHOW ME THE MONEY

For those going it alone with proprietary foodservice, money can be difficult to secure, especially for an independent operator. "Banks can be very difficult to work with these days; they don't want to do the smaller loans," explained Anita Baron, president and CEO of Baron Business Lending, who has facilitated roughly $60 million in loans and leases for the c-store and

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fuel industry over the past 16 years. "It can be difficult for convenience stores to find traditional financing for smaller deals, because their collateral doesn't have a lot of value."

Working closely with retailers to understand their unique needs, she matches them with the right funding source. "I do equipment loans and leases and capitol loans starting at $4,000," she said. "Whether it's making sure a retailer can get the equipment they need or refinance their debt ... I locate the money source ... I can find non-traditional sources [of funding] ... I'm the hand holder who finds the right match."

Such was the case for Larry Jackson and his Good to Go Markets (in Columbia, Maryland), when he looked to incorporate his Bullhead Pit Beef catering business with his convenience store by way of a food truck (his store doesn't have the space for the full-service offer he was seeking). "While I have a lot of lender contacts in the gas station industry, I couldn't find anybody who was interested [in working with us]," he said. "Banks turned us down; they were hesitant because we were an unknown entity and there was no way to show potential. They tried to relate it back to our convenience store business but that wasn't accurate."

Jackson ended up working with Baron who located a lender that made the deal possible. "It's going to be set up under a lease and not a traditional loan," he said. "It's more expensive in the long run but I wouldn't have been able to do it without the investment."

THIRD-PARTY ASSISTANCE

For those looking for a more turnkey foodservice option, partnering with a recognizable brand can help with every aspect of a program, along with financing. "Some companies will fund almost 100% of the equipment if you use their products exclusively," Burcher said.

So You Want to Start a Foodservice Program...

Burcher Consulting's Ed Burcher offers these best practices tips for launching a foodservice program:

- **The emperor's new clothes:** Take a look at your company from an open and honest viewpoint.
- **Opportunity knocks:** After assessing a marketplace opportunity, make sure you have the internal capability and management commitment to pursue it.
- **Buckle down:** Be prepared for a two-year process at minimum before you will see a profit.
- **Seek help:** Just because you can make a sandwich in your kitchen doesn't mean you can make hundreds of those in your stores over and over again. Get outside advice to make sure you're prepared for the challenge.
- **Follow a process:** Following a structure will eliminate redundant errors.

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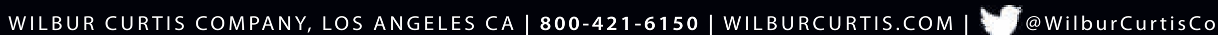

Nashville-based Hunt Brothers Pizza is one such company, which has been working with convenience stores for more than 25 years. "We make it easy for stores to execute, especially on the financial side," said Keith Solsvig, vice president of marketing for Hunt Brothers. "We developed our program so that it's modular and fits into different footprints. We also work with retailers in terms of how they want to build their program. They can get in at a lower level and as their sales build, they can add more equipment and storage space."

Hunt Brothers offers two primary financing options: Either adding a product upcharge until an equipment loan is paid off or offering 90 days same-as-cash deals. "The quicker they can buy the equipment, the quicker they'll make money," Solsvig said.

Marty Mylor went the upcharge route when his Sparta Quick Stop (in Sparta, Kentucky) began working with Hunt Brothers more than 25 years ago. "I had just one employee at the time [and] we were barely scraping by," he said. Recognizing that he needed to distinguish himself from other local stores to attract customers, he decided to launch a foodservice program with the Hunt Brothers brand. "Back then, our investment was minimal," he said, as Hunt Brothers provided his store with the requisite equipment. "It was kind of a rent-to-own thing. They put in the equipment and I paid them a buck a pizza—that's how we ended up paying for the oven. It was a great way to start."

Since then, Sparta's foodservice program has grown steadily and today incorporates conveyor ovens for his burgeoning foodservice business. "This year, we spent close to $10,000 in upgrades," he said. "We own all of our equipment now and just buy product." (He continues to work with Hunt Brothers.)

Burcher offers a couple of caveats for those partnering with a third party: There may be restrictions to carrying only that brand's offerings, which could impact future expansion opportunities, and the length of the commitment could also impact future operations. "Most people don't ask that going into an agreement [with a third party]," Burcher said. "Find out the buyout cost on depreciated equipment."

LEARN FROM YOUR MISTAKES

No matter your offerings and business model, while the need to get into foodservice is great, it's critical to follow a deliberate and thoughtful process in order to find success. "People tend to want to do things quickly," Burcher said. "But what ends up happening is that they end up having to fix it at a great expense.

"Getting it correct the first time is important." NACS

Jerry Soverinsky is a Chicago-based freelance writer. He's also a NACS Magazine contributing writer.

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