

VALUE FOCUS

Convenience Stores

SEGMENT FOCUS

Grocery Stores

2017

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Overview

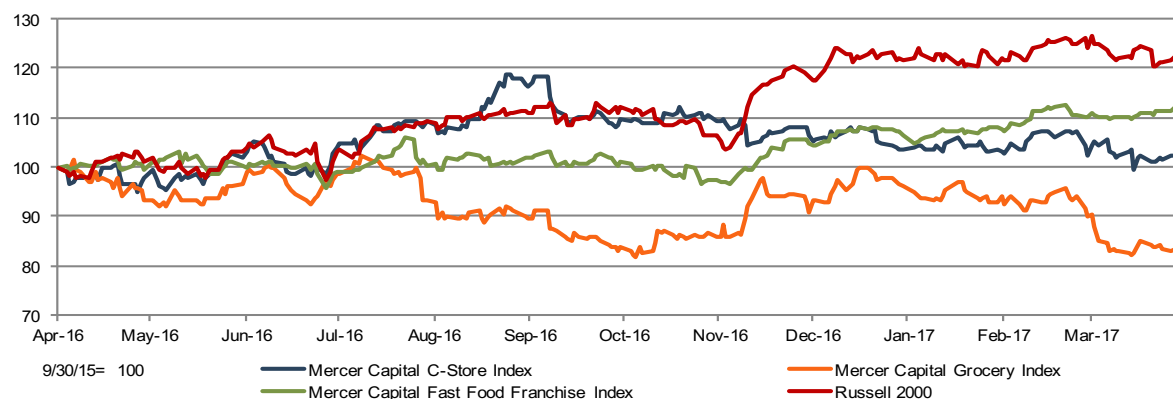
Equity Market Overview

During the quarter ending March 2017, Mercer's convenience store equity index remained virtually flat, underperforming the Russell 2000 which was up 2.1% for the quarter. **MUSA's** stock increased 18.8%, but the increase was offset by **TA** and **CASY's** 14.8% and 6.5% declines, respectively. **ANCUF** was virtually flat. ANCUF's market cap at \$26 billion is by far the largest in the group, accordingly its performance imparts more influence on the index.

The grocery store index posted a 12.5% decrease for the first quarter and is down 15.8% year-over-year. **Kroger**, which has the largest market capitalization in Mercer's grocery index, posted a 15.1% quarterly decline, and was down 22.7% year-over-year. Kroger operates within a competitive industry facing food deflation and potential near-term disruption from evolving rivals. Kroger's significant financial leverage remains a concern for investors, although the grocery store operator's earnings were better than analysts' original estimates. Performance within the grocery index was universally negative with declines ranging from 4.4% to 18.6% as compared to year-end 2016.

The fast food index posted a quarterly increase of 5.7%, and the index is up 13% year-over-year. The fast food index is disproportionately influenced by McDonald's (**MCD**), the largest player in the index. MCD's recent stock price increase is attributed in part to technology enhancements such as self-ordering kiosks and mobile ordering. Restaurant Brands International (**QSR**) is up 45% year-over-year. The increase in QSR's stock price is attributed to consistently beating earnings expectations, a recent acquisition of Popeyes Louisiana Kitchen, and successful integration of new products at Burger King stores.

C-Store, Grocery Store, & QSR Stock Indices



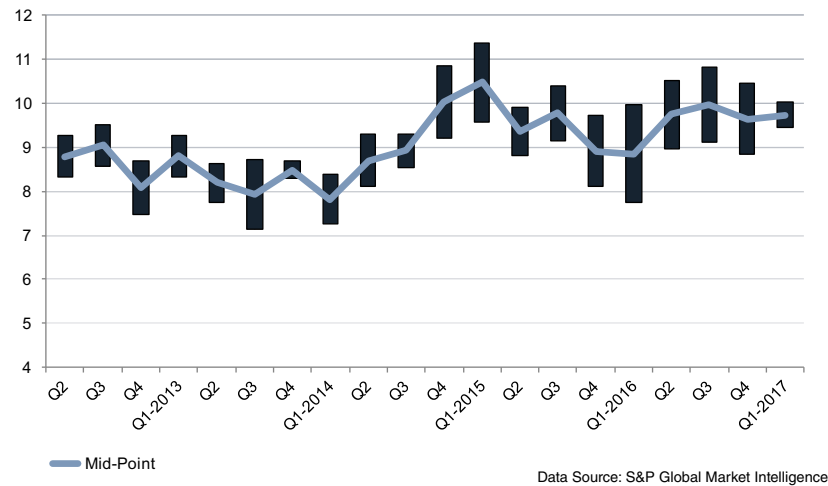
Data Source: S&P Global Market Intelligence / Bloomberg

Overview

Valuations Down, Ranges Hold Steady for C-Stores

EBITDA multiples were up less than 1% for both c-stores and grocery stores, and up 6.3% for fast food operators. Multiples for public c-store operators rose from 9.6x EBITDA at the end of the fourth quarter of 2016 to 9.7x at the end of the first quarter of 2017.¹ C-store multiples remained above their five-year average (9.1x).

C-Store EBITDA Valuations // Quarterly Range of Mean Highs & Lows

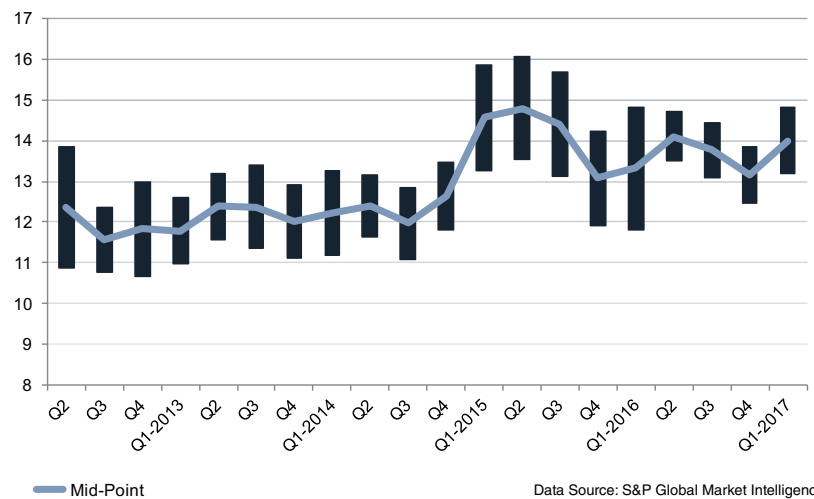


¹ As measured by the average of : (1) the median of the highest EBITDA measure of all the companies in the Mercer Capital index over the entire quarter and (2) the median of the lowest EBITDA measures of all the companies in the Mercer Capital index over the entire quarter. Current and historical multiple data was obtained from Capital IQ. In some prior newsletters, data was sourced from Bloomberg.

Grocery Store EBITDA Valuations // Quarterly Range of Mean Highs & Lows



Fast Food (QSR) EBITDA Valuations // Quarterly Range of Mean Highs & Lows



Publicly Traded Companies

Ticker	LTM Price Range			Equity Market Cap	Enterprise Value	Revenue			TEV / LTM EBITDA	EBITDA		EBITDA Margins			
	Price for 3/31/17	High	Low			LTM	2017 Est.	2018 Est.		Estimated Growth From		LTM	2017 Est.	2018 Est.	
										LTM to Current Year	Current Year to Next Year				
Convenience Stores															
Alimentation Couche Tard Inc	ANCUF	\$45.40	\$52.84	\$39.33	\$25,782	\$30,551	\$33,586	\$34,680	\$39,126	12.96	-3.2%	13.9%	7.0%	6.6%	6.6%
Casey's General Stores Inc	CASY	\$120.15	\$135.97	\$98.43	\$4,707	\$5,595	\$7,044	\$7,129	\$7,657	9.82	-0.9%	3.0%	8.1%	7.9%	7.6%
TravelCenters of America LLC	TA	\$7.16	\$12.67	\$6.41	\$278	\$1,024	\$5,470	\$5,656	\$6,501	9.64	13.9%	28.1%	1.9%	2.1%	2.4%
CST Brands Inc	CST	\$48.09	\$48.31	\$29.64	\$3,639	\$5,422	\$10,980	\$9,472	\$10,819	10.57	-24.8%	11.1%	4.7%	4.1%	4.0%
Murphy USA Inc	MUSA	\$71.36	\$80.44	\$51.68	\$2,795	\$3,473	\$11,807	\$11,817	\$13,548	8.80	11.9%	0.9%	3.3%	3.7%	3.3%
Average C-Stores					\$7,440	\$9,213	\$13,777	\$13,751	\$15,530	10.36	-0.6%	11.4%	5.0%	4.9%	4.8%
Median C-Stores					\$3,639	\$5,422	\$10,980	\$9,472	\$10,819	9.82	-0.9%	11.1%	4.7%	4.1%	4.0%
Grocery Stores															
Village Super Market Inc	VLGEA	\$32.01	\$33.00	\$22.85	\$454	\$498	\$1,603	na	na	7.59	na	na	4.1%	na	na
SpartanNash Co	SPTN	\$28.92	\$33.72	\$17.39	\$1,085	\$1,577	\$7,650	\$7,703	\$7,788	7.99	16.9%	4.3%	2.6%	3.0%	3.1%
Weis Markets Inc	WMK	\$53.00	\$55.49	\$36.69	\$1,426	\$1,426	\$2,915	na	na	8.20	na	na	6.0%	na	na
Ingles Markets Inc	IMKTA	\$39.54	\$56.92	\$31.49	\$801	\$1,699	\$3,785	\$3,790	\$3,866	7.11	0.4%	2.9%	6.3%	6.3%	6.4%
Whole Foods Market Inc	WFM	\$28.35	\$35.26	\$27.54	\$9,891	\$10,943	\$15,666	\$15,737	\$16,453	8.59	5.1%	1.4%	8.1%	8.5%	8.2%
SUPERVALU Inc	SVU	\$4.99	\$7.84	\$3.94	\$1,322	\$3,807	\$17,318	\$17,588	\$17,308	5.38	9.7%	-7.1%	4.1%	4.4%	4.2%
Kroger Co/The	KR	\$29.68	\$42.34	\$29.49	\$28,641	\$41,061	\$112,409	\$109,914	\$115,218	7.11	-1.6%	4.1%	5.1%	5.2%	5.1%
Average Grocery Stores					\$6,231	\$8,716	\$23,049	\$30,947	\$32,127	7.42	6.1%	1.1%	5.2%	5.5%	5.4%
Median Grocery Stores					\$1,322	\$1,699	\$7,650	\$15,737	\$16,453	7.59	5.1%	2.9%	5.1%	5.2%	5.1%

Source: Bloomberg

Publicly Traded Companies (continued)

Ticker	Price for 3/31/17	LTM Price Range		Equity Market Cap	Enterprise Value	Revenue			TEV / LTM EBITDA	EBITDA		EBITDA Margins			
		High	Low			LTM	2017 Est.	2018 Est.		Estimated Growth From		LTM	2017 Est.	2018 Est.	
							LTM to Current Year	Current Year to Next Year							
Fast Foods (QSR)															
McDonald's Corp	MCD	\$115.36	\$129.99	\$94.22	\$98,437	\$124,447	\$25,125	\$24,439	\$22,892	13.69	2.7%	4.0%	36.2%	38.2%	42.4%
Wendy's Co/The	WEN	\$10.80	\$11.25	\$8.23	\$2,844	\$5,353	\$1,690	\$1,417	\$1,171	12.13	-10.6%	-1.3%	26.1%	27.8%	33.2%
Yum! Brands Inc	YUM	\$90.81	\$91.99	\$63.88	\$36,233	\$41,596	\$13,005	\$13,251	\$13,043	14.68	7.2%	3.1%	21.8%	22.9%	24.0%
Dunkin' Brands Group Inc	DNKN	\$52.08	\$52.22	\$35.73	\$4,777	\$7,221	\$820	\$840	\$865	19.05	20.0%	5.1%	46.3%	54.1%	55.2%
Panera Bread Co	PNRA	\$194.72	\$224.15	\$165.17	\$4,627	\$5,025	\$2,740	\$2,799	\$3,019	13.12	6.3%	10.2%	14.0%	14.5%	14.9%
Chipotle Mexican Grill Inc	CMG	\$423.50	\$757.00	\$384.77	\$12,345	\$12,345	\$4,047	\$4,038	\$4,730	26.22	-33.4%	96.3%	11.6%	7.8%	13.0%
Jack in the Box Inc	JACK	\$95.94	\$102.68	\$61.34	\$3,134	\$4,030	\$1,555	\$1,599	\$1,571	13.25	5.9%	13.2%	19.6%	20.1%	23.2%
Restaurant Brands International Inc	QSR	\$44.58	\$49.12	\$28.96	\$10,420	\$22,449	\$4,035	\$4,146	\$4,401	14.23	19.0%	8.1%	39.1%	45.3%	46.1%
Sonic Corp	SONC	\$26.18	\$36.08	\$22.52	\$1,253	\$1,855	\$619	\$616	\$562	10.76	0.5%	2.0%	27.8%	28.1%	31.4%
Average Fast Foods					\$19,341	\$24,925	\$5,960	\$5,905	\$5,806	15.23	1.9%	15.6%	26.9%	28.8%	31.5%
Median Fast Foods					\$4,777	\$7,221	\$2,740	\$2,799	\$3,019	13.69	5.9%	5.1%	26.1%	27.8%	31.4%

Source: Bloomberg

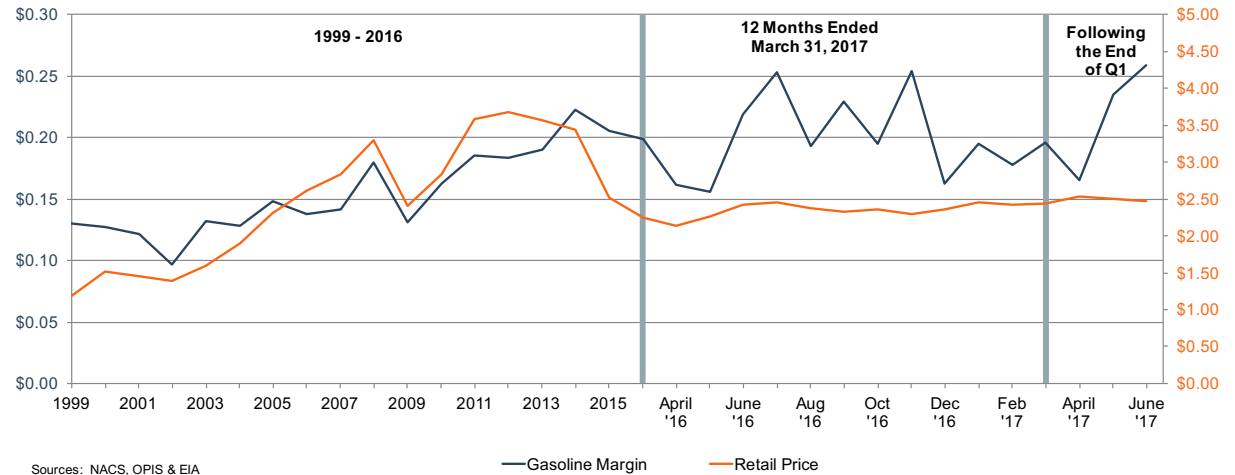
C-Store Trends

Margins

According to OPIS, nationwide retail gasoline margins ended the first quarter of 2017 at 18.9 cents per gallon, up from 18.0 cents per gallon 12 weeks earlier, and below the running five-year average of 20.0 cents. Between the end of the first quarter and the time of this publication, retail fuel margins have fluctuated, but are now 28.4 cents per gallon, the highest level of 2017, reflecting a general decline in fuel prices over the last few months. Average margins for the first three months of 2017, approximately 19 cents per gallon, are slightly lower than year-to-date margins from the same time last year. At the time of this publication, the EIA's weekly statistics revealed strong gasoline demand, but crude oil stocks and gasoline inventories have continued to rise as compared to December 2016. Nationwide, gasoline prices are approximately five cents per gallon lower than June 2016.

Diesel margins ended the fourth quarter at 33.3 cents per gallon, up from 21.6 cent margins posted 12 weeks earlier. The chart below presents the relationship between retail gasoline prices and margin.

Gasoline Price and Spread Per Gallon



²National Association of Convenience Stores 2016 Retail Fuels Report.

C-Store Trends

Margins

Generally, over 70% of a c-store's sales are motor fuels; however, fuel typically contributes only one-third of total convenience store gross margin dollars. Despite periodic fluctuations, fuel margins have been relatively consistent on an annual basis, averaging 20 cents per gallon from 2012 to 2016. There is a relatively modest delay between the time crude oil prices increase and the time that fuel pump prices rise. Similarly, retail price reductions typically lag when wholesale prices drop. To reduce the risk of retail consumer price shopping, fuel marketers tend to reduce their fuel markups to absorb a portion of escalating crude oil and wholesale fuel costs. Conversely, when costs are declining, retailers tend to leave their pump prices elevated – leading to increased fuel margins – until competition ultimately forces pump pricing downward. The time lag between cost changes and retail price adjustments, as well as the duration of cost trends, are significant influencers of operator margin. On average, it costs retailers approximately 12 to 16 cents to dispense a gallon of fuel. The average five-year markup on gasoline has been approximately 20.0 cents; this translates to a typical four to eight cents per gallon of fuel profit.

C-Store Trends

Government/ Regulatory and Industry Trends

Taxes

The Ryan-Brady plan proposes a consumption tax and a 20% border tax adjustment on imports. The **National Retail Federation** believes either of these proposals would likely increase costs to consumers which would in turn negatively impact retail spending. Instead, the group favors reforming the existing federal income tax system.

Menu Labeling

The enforcement of menu-labeling rules for chain restaurants and other food establishments was delayed by the FDA for the third time on May 1st. The rules that were slated for enforcement starting on May 5th are now set for enforcement on May 1, 2018. Although the delay was celebrated by the c-store industry, many c-stores had already begun posting nutrition information in expectation of enforcement, so industry-wide the action might not have saved as much money as an earlier delay might have.

Tobacco

Two proposals have been introduced in Congress which aim to reverse the Obama-era's "deeming rule." Essentially, e-cigarettes and vaping devices would no longer be subject to the same regulations as cigarettes.

Swipe Fees

The new Republican-majority congress has been attempting to pass legislation reforming regulation of the financial services industry, including an effort to repeal swipe fee reform. In late May, the effort to repeal Dodd-Frank's debit card swipe fee reform was reportedly abandoned.

Recent M&A Activity

The following table summarizes M&A activity since the publication of our last newsletter. In addition to the major transactions listed, there were several transactions involving 50 or fewer units since our last publication. 2014 and 2015 were busy in terms of M&A activity, but activity seemed to slow in 2016. The largest acquirers (7-Eleven, Couche-Tard, and Marathon/Speedway) continue to gain market share. Couche-Tard alone made three large acquisitions in 2016, and its purchase of CST Brands is pending.

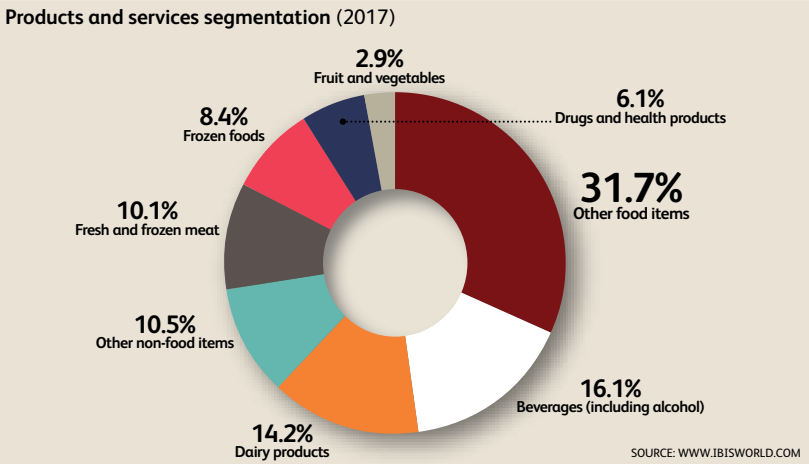
Acquirer	Target	# of Stores	Locations	Comments
7-Eleven	Sunoco LP	1,108 convenience stores	United States	This deal will bring 7-Eleven's total store count to 9,815 worldwide. 7-Eleven also operates franchises or licenses more than 62,000 stores in 17 countries. The deal is expected to close in the second half of 2017.
Andretti Petroleum Group and Lane Colvin	Colvin Oil Company	54 retail locations and three cardlocks	Oregon, Washington, and California	The enterprise will continue to operate under the name Colvin Oil.
Brookfield Business Partners, LP	Loblaw Cos. Ltd.	213 gas stations and grocery store kiosks	Canada	The stores are expected to rebrand as Mobil stores.
Parkland Fuel Corp.	Chevron Canada Ltd.	129 c-stores	Vancouver, British Columbia	The deal also includes cardlocks, marine locations, a refinery, and a wholesale business.

Source: Convenience Store Decisions

SEGMENT FOCUS

Grocery Stores

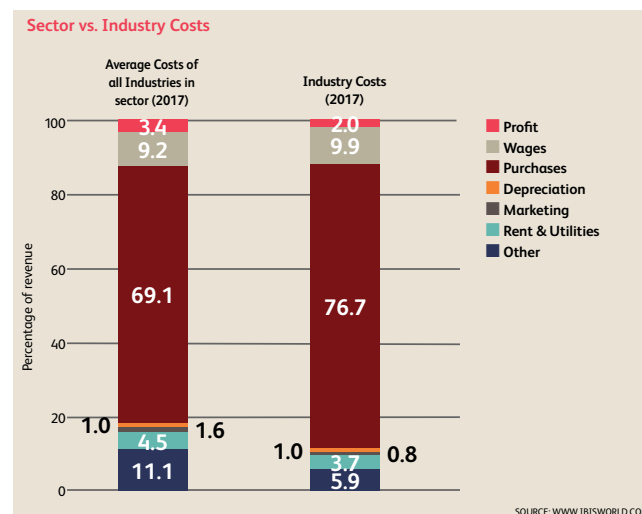
The Supermarkets and Grocery Store industry makes up the largest food retail channel in the United States. Industry revenue totaled approximately \$611.9 billion in 2016, and profit was \$12.2 billion. The following chart presents the products and services segmentation for the industry as estimated for 2017 by IBISWORLD.



This industry has grown over the past five years, benefitting from a strengthening economy and the trend toward organic and all-natural brands, especially as consumer spending has increased. However, the industry is mature, and revenue is expected to grow at a rate below national GDP over the next five years (0.8%, annualized) as compared to annualized growth of 1.0% from 2012 to 2017. The top three operators (Publix, Kroger, and Albertsons) account for roughly 30% of industry revenue. Competition from superstores and warehouse clubs intensified during the recent recession, and remains high. On the other end of the spectrum, more consumers are gravitating toward specialty grocers like Aldi and Trader Joe's. Online competition has become especially prevalent in recent years.

Grocery Stores (continued)

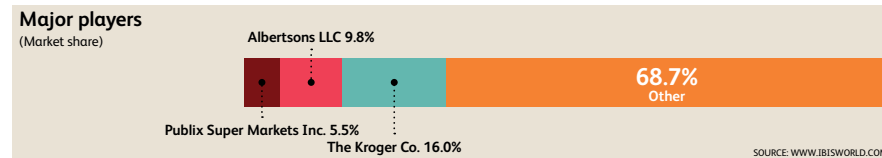
As shown below, other sector operators enjoy modestly lower costs than grocery store retailers. They also tend to offer a convenience factor given that they stock a range of nonedible goods such as clothing and household supplies. This competition, coupled with widespread food deflation, has led to stagnating profitability within the industry.



The industry is mature and continues to consolidate. Merger and acquisition activity among the larger players has been high in the past few years. Most notably, Amazon announced in late June its intention to purchase Whole Foods for \$13.7 billion. The price represents a 27% premium to Whole Foods' stock price prior to the announcement. In response, analysts have voiced many different opinions on what the acquisition will mean for the traditional grocery industry. There is an expectation that Amazon will integrate sophisticated technology into the Whole Foods platform, and delivery is expected to be a prime component of the new relationship.

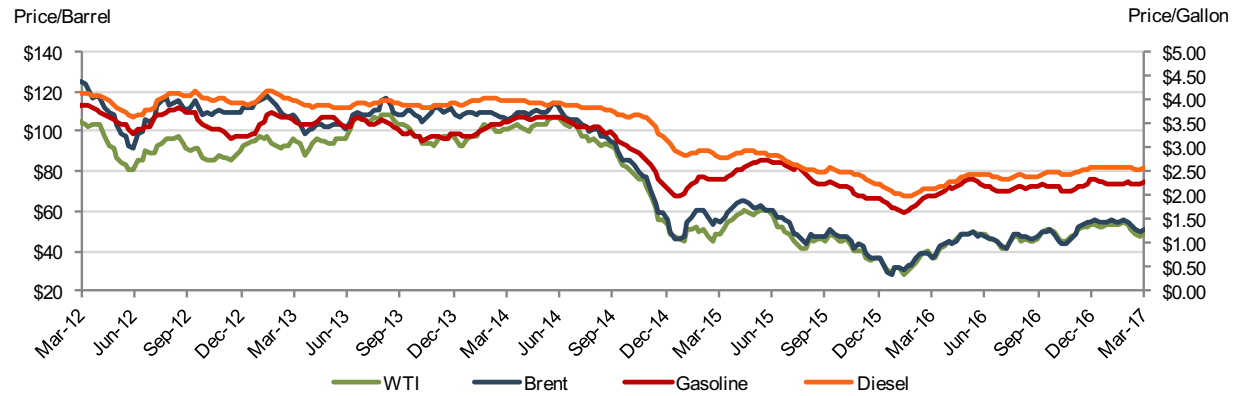
Grocery Stores (continued)

In more traditional mergers, The Kroger Company merged with Harris Teeter in 2014 to expand within the Southeast and Mid-Atlantic market areas and create a network of over 2,600 stores. Kroger also acquired Roundy's in 2015 adding 151 stores to its network. Safeway and Albertsons merged in early 2015 to create a nationwide network of over 2,200 stores. There are plans for Albertsons to eventually go public. Delhaize America merged with Ahold in mid-2016. Trader Joe's, ALDI U.S., and Publix Super Markets have focused on organic expansion rather than acquisitive growth. This is an industry in which economies of scale are crucial; larger size helps enterprises better compete with mass merchandisers by lowering per-unit costs. The grocery store industry has been facing increasing competition from superstores and discount warehouse clubs, such as Wal-Mart. Supermarkets are also increasingly facing competition from convenience stores, food service providers, and dollar stores.



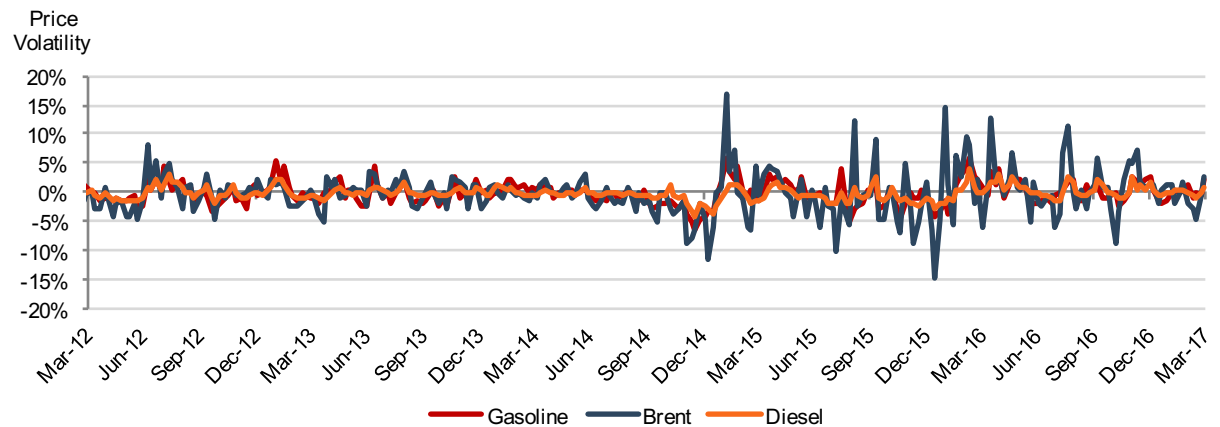
Fuel Pricing & Supply Charts

Wholesale and Retail Prices



Data Source: Calculated by Mercer Capital from raw data obtained from the US Energy Information Administration (EIA.gov)

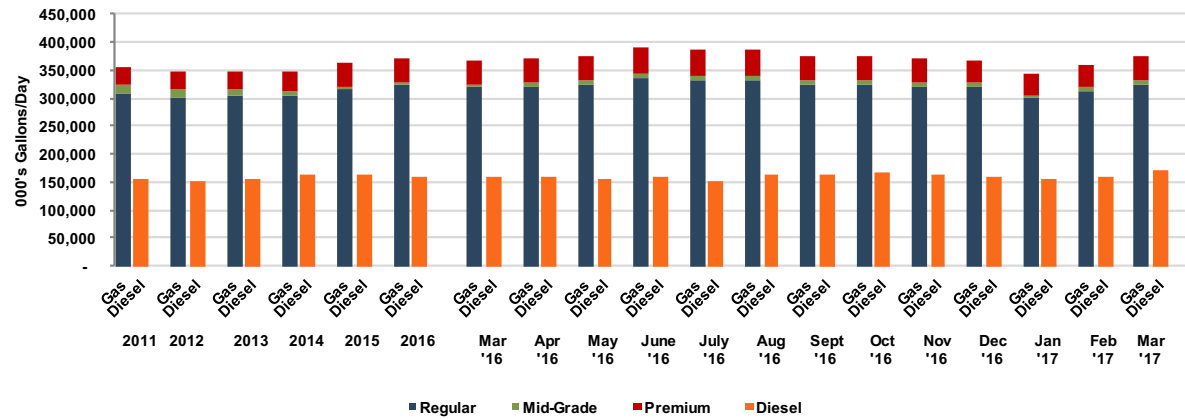
Motor Fuel and Brent Crude Price Fluctuation



Data Source: Calculated by Mercer Capital from raw data obtained from the US Energy Information Administration (EIA.gov)

Fuel Pricing & Supply Charts (continued)

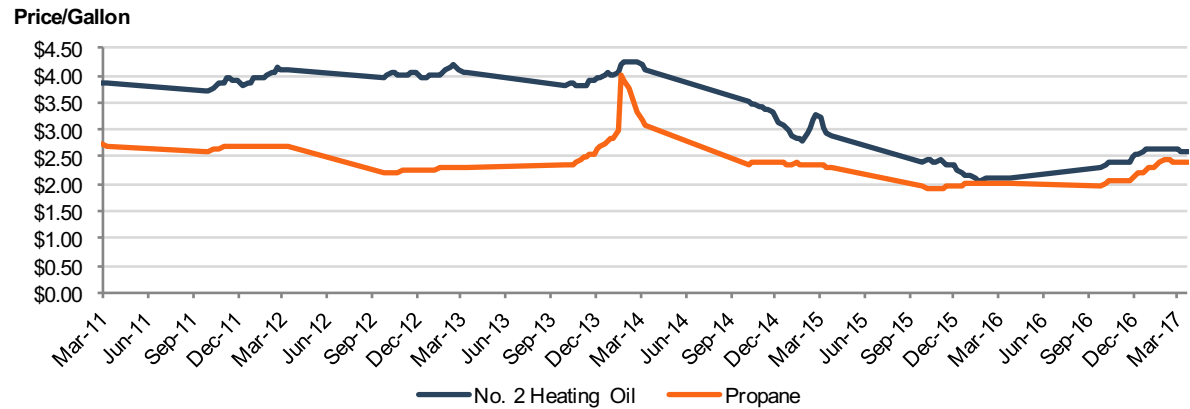
Prime Supplier Sales Volumes



Data Source: US Energy Information Administration (EIA.gov)

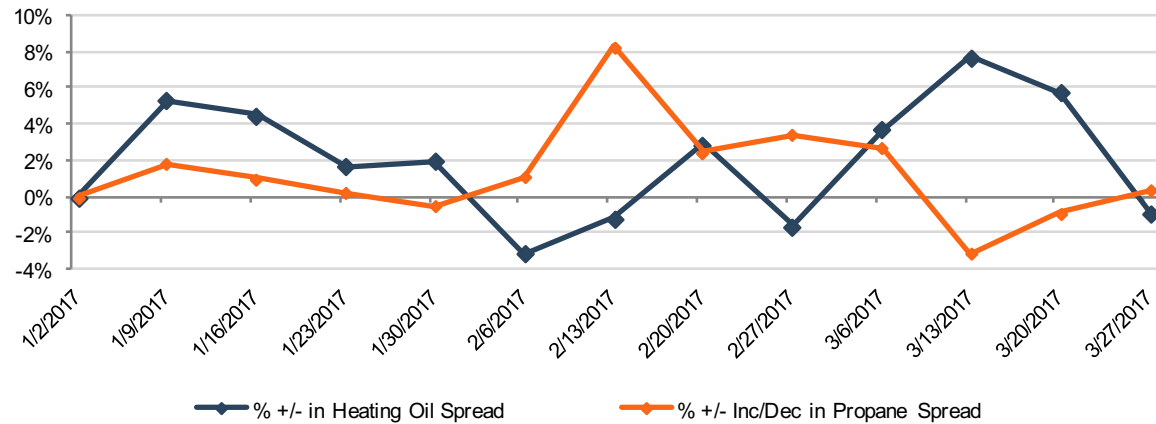
Fuel Pricing & Supply Charts (continued)

Non-Motor Fuel Prices



Data Source: US Energy Information Administration (EIA.gov)

Percentage Change in Non-Motor Fuel Spread by Month



Data Source: US Energy Information Administration (EIA.gov)

Mercer Capital

Convenience Store
Industry Services

Mercer Capital provides the multi-unit retailing and QSR industries with corporate valuation, financial reporting, transaction advisory, and related services.

Industry Segments

Mercer Capital serves the following industry segments:

- Motor Fuels
- Grocery Stores
- Alternative Fuels & Consumer Transportation
- Foodservices

Mercer Capital Experience

- Family and management succession planning
- Buy-side and sell-side transaction advisory assistance
- Conflict resolution and litigation support
- Trust and estate planning
- Buy-sell agreement valuation, design, and funding advisory

Contact a Mercer Capital professional to discuss your needs in confidence.

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