PwC Challenge 2018

SUMMARY OF RECOMMENDATIONS:

Recommendations for Country's Best

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Executive Summary

To espouse Country's Best expansion into the Southeast by 2025, we provide a comprehensive analysis of the significant cost-savings and profit-earning opportunities. By analyzing Country's Best in comparison to its competitors, we base our solution off of success regarding: asset management, fuel and non-fuel revenue, and demographic and geographic factors. After breaking down the pros and cons of three candidate solutions - *Zero, Minimal, and Full Automation* - in terms of three categories summarizing Country's Best company values - *Convenience, Community, and Cost-Savings* - we propose utilizing Full Automation for its superior financial consequences and easy integration. In addition, our strategy incorporates a renovation of the current store layout to promote County's Best as a community hub, simultaneously involving an under $5 cash-only policy to provide further cost-savings during construction and renovation. Lastly, we illustrate our strategies impact on convenience, community, and cost-savings with a detailed investigation, depicting the robustness of our solution as well as the long-term consequences.

Current Business Outlook: Industry Analysis and Asset Management

The U.S Convenience Store industry has experienced gradual increases over the past three decades (NACS 2016). Upon further investigation, Country's Best has a good standing in a healthy and stable industry. Among Country's Best's direct competitors, Casey's General is viewed as the primary competitor because of similarities in demographic, geographic, and operational characteristics. By comparison of financial ratios (Figure 1), Country's Best shares similar trends in terms of asset management and profitability measures. Since Casey's General is a leader in performance, we can conclude that Country's Best is managing its assets effectively.

From the SWOT analysis of Country's Best current situation (Figure 2), we identify Country's Best's main weaknesses as volatility in fuel prices and the fees from customer credit card use. COGS for fuel remains the highest factor contributing to the total cost (Figure 3). The second highest is COGS for Groceries and Merchandise (excluding fuels). Hence, we instigated examination in these areas.

Fuel Sales: Profit Margin Reliability

In Country's Best, stores with fuel generate 20% more revenue[1]. Despite fuel price volatility, profit margin remains reliable[2]. This consistency allows retailers to have a more stable cash flow and project future growth more accurately. Moreover, fuel is a commodity and has a price inelastic demand[2] and offering fuel helps in-store sales because fuel consumers often go inside to make more purchases[1].

Recover Credit Card Fees: Easy, Minimal Risk Cost Savings

Diminishing the fees paid for credit card use - a cost of 2.75% per swipe - will result in $2.7 million in savings each year. To minimize risk, we can post restrictions of cash only for purchases under $5, encouraging consumers to purchase more or use the change they already have. Based on our customer demographics - which mirror Casey's General's, 50% of our customers fall into the characteristics of cash only users: being low-income (Figure 4, Creditcards.com) and making purchases under 10 items. Then, credit purchases must account for at least 50%[5] of our food goods revenue. By normalizing the spread of purchases by Casey's customers, we found the cumulative percentage of purchases between $1 to $5 to be 6.6% (Figure 5). By recovering the fees of 6.6% of our credit purchases in-store, we will save $2.7 million in COGS (Figure 6).

[1]The average revenue per store for food and non-food items excluding fuel is 40%. Most of the stores offer fuel for sale on a self-serve basis with the revenue per store for fuel averaging 60% (Country's Best website).
[2]Over the past five years, retailer gross margins have averaged 6.2%, which translates to $0.19 per gallon (NACS, 2016).
[3] 85% Americans get to work by driving, and the average US household spent around $2,000 on gas in 2015 (NACS, 2016). U.S. gasoline demand also increased from 2.6% to 9.2 million barrels per day in 2015 (U.S Energy Information Administration, Short-Term Energy Outlook).
[4]41% of those who fuel up at a convenience store also go inside the store and 75% of those people purchase food and/or beverages (NACS, 2015).
[5] Credit card purchases tend to result in bigger purchases by consumers (Intuit).

The Solution: Automation, Minimal Automation or Zero Automation

To achieve a 20% expansion in 7 years, we must immunize Country's Best with financial growth. The criteria with which we will evaluate our candidate strategies are *Convenience*, *Community*, and *Cost-Savings*. By evaluating strategies using these core values, we are prioritizing the experience of the Country's Best family, customers, consumers,, and financial growth for their benefit.

The three candidate strategies include: Zero Automation, which maintains the current operation style of Country's Best; Minimal Automation, which utilizes electronic payment in combination with limited cashier-to-customer interaction; and Full Automation, which enhances the employee-customer interaction by the installation of self-service checkout machines while reducing part-time wage expenses. Figure 7 depicts a comparison of the three options in relation to the previously stated criteria.

Therefore, we propose implementing a Full Automation scheme in combination with a redesign of the current store layout (Figures 8 and 9). In this manner, we will be saving money on wages while emphasizing the community aspect of Country's Best by opening up register space for in-store dining and reallocating our remaining labor force to prioritize customer service. This will encourage customers to stay longer, increasing the dollar amount of purchases while cutting significant costs each year. This strategy, in conjunction with the new policy regarding transactions under five dollars, will not only incite profit growth, but also encourage further spending and enjoyment in any given Country's Best experience.

Cost Analysis: No Automation versus Automation

We created a simple projection of the net present value of net income in the coming years using an interest rate of 6.5%[7]. Based on our research on the industry market as well as fuel expectations, we have little reason to expect that our net income from 2016 will decrease significantly. Additionally, with each new store that we construct, we will be making additional net income from goods sold (Figure 10)[8].

If we leave stores unautomated, we will construct 57 new stores every year until 2025. We estimate a Tier 1 construction to cost $1,000,000 (TCT Construction). Although suffering from a loss of $53 million for the first seven years because of construction, Country's Best will still maintain a healthy net income (Figure 11). Despite this, it is only until 2026 that we would recover to make a net income greater than our 2016 net income. This would clearly look dismal to our investors.

Considering automation, we estimate that construction will similarly cost $1,000,000 because no fiscally significant changes will be made related to materials. By utilizing MIT research, we analyzed the costs to install two self-checkout lanes, which allows us to eliminate two part-time employees and two POS systems. While machine and construction costs are only one-time costs, savings from removing employees as well as POS annual fees will accumulate throughout the years, allowing us to surpass the projection of net income of non-automation significantly (Figures 12 and 13).

In 2025, automating Country's Best will make $23 million more than leaving the store model as is. To maintain consistency and convenience throughout the country, we will begin renovating the old stores beginning in 2026. For simplicity, we plan the remodel to take 10 years, averaging the remodel of 200 stores every year. Although we may suffer a downturn in net income initially by doing this, we will achieve a cumulative NPV net income gain of $138 million by the completion of this project (Figure 13).

Conclusion

Upon analyzing the costs and benefits of the three candidate solutions, we propose implementing full automation in combination with tactical remodeling and a cash-only policy for under $5 purchases to supplement Country's Best expansion. Employees, customers, and investors will benefit from the convenience, community, and cost-savings of our strategy (Figure 14), which results in $166 million in cumulative net income growth by the time of completion in 2034.

[7]This is the convenience store industry average borrowing rate (BoeFly).

[8]With automation/the remodeling of the stores, we expect significant increases in sales of freshly prepared food - our biggest profit margin maker - therefore, net income should increase significantly more than leaving the stores as is. However, to keep a lowball, high level estimate of the projections and limit arguable speculation - we will assume that there is no difference.