

# C-STORE VALUATIONS

Dear Reader:

Thank you for your interest in our *Valuation Today* market report. Enclosed is your complimentary copy. We hope you will find it helpful and informative.

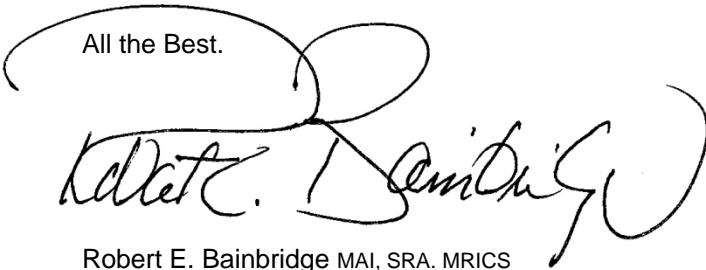
For additional information about current valuation issues in the retail convenience channel, you may wish to visit our website at [www.cstorevalue.com](http://www.cstorevalue.com). On the "Video Insights" page you will find short, appraisal-related video clips on these important topics:

1. Development Process
2. Supply and Demand
3. Hypermarket Competition
4. What Should be in an Appraisal of a C-Store: A Lender's Perspective
5. A Business Appraiser's Perspective
6. Retail Site Analysis
7. Below-Cost Selling

At our website you will also find useful Whitepapers and current valuation metrics.

If we can be of any assistance to you, it would my pleasure to personally serve you. Please let us know and thank you again.

All the Best.



Robert E. Bainbridge MAI, SRA, MRICS  
C-Store Valuations



## VALUATION TODAY

Hypermarkets continue to expand their share in the U.S. retail gasoline market, moving from 6% in 2001 to 12% of all the gasoline sold in 2003. With average annual volumes of 3 to 10 million gallons, each new hypermarket can satisfy the retail demand for a market of 23,000 people.

Hypermarkets are large discount retailers that offer department store merchandise, groceries, and gasoline. Examples include Walmart, Costco, Fred Meyer and Albertsons. Retail channels are now blurred with overlapping competition between hypermarkets, convenience stores and fast-food restaurants.

Gasoline sales competition from hypermarkets continues to be the number one problem facing the convenience industry. In response to this new competition, some industry insiders expect the number of convenience stores in the U.S. to decline to 50,000 by the year 2015. In the early part of this decade, about 125,000 convenience stores were operating in the U.S. This would be a loss of over 50% of the convenience industry's capital asset value.

For example, in response to competition from Walmart's supercenter format, the Winn-Dixie grocery chain filed for Chapter 11. Share prices declined from a high of \$59.38 in the pre-supercenter days to \$1.47 this year. The convenience industry is facing the same competition.

Operating performance benchmarks necessary for c-stores to survive in this new competitive environment are:

- Minimum Fuel Gallonage: 2.5 million gallons/year
- Minimum Fuel Margins: 3 to 5 cpg
- Minimum Inside Sales: \$1.2 million/year

As a spokesman for the troubled Krispy Kreme retailer noted, "If the economics at the store level does not make sense, then the chain cannot make money."

Across the nation, the median convenience store property sale price was \$1,139,298.00 in 2004, a 15% increase from 2003.

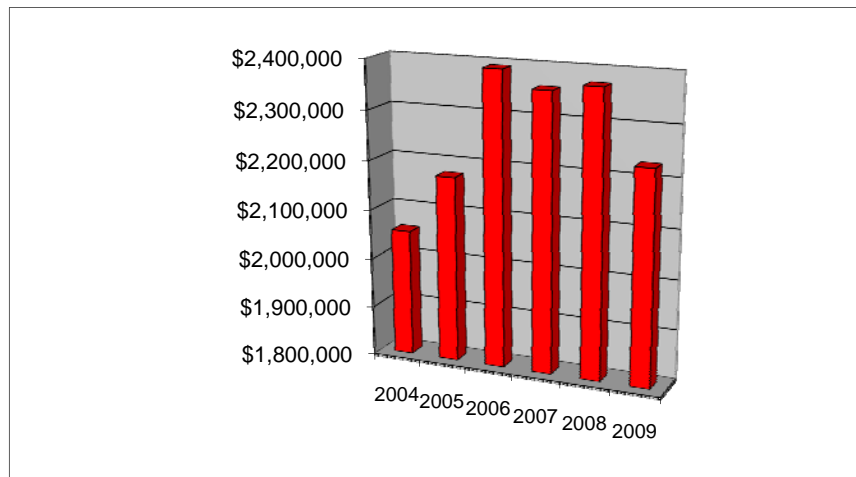
Cap rates for c-stores declined by over 100 basis points from 2003 reaching 7.31% in 2004, which likely accounts for the price increases noted above. In light of the deterioration of industry operating fundamentals, such as declining gross margins and declining pre-tax profits, a significant real estate price correction will have to take place sometime between 2005 and 2010.

### U.S. Historical Price Movement 2000 to 2009

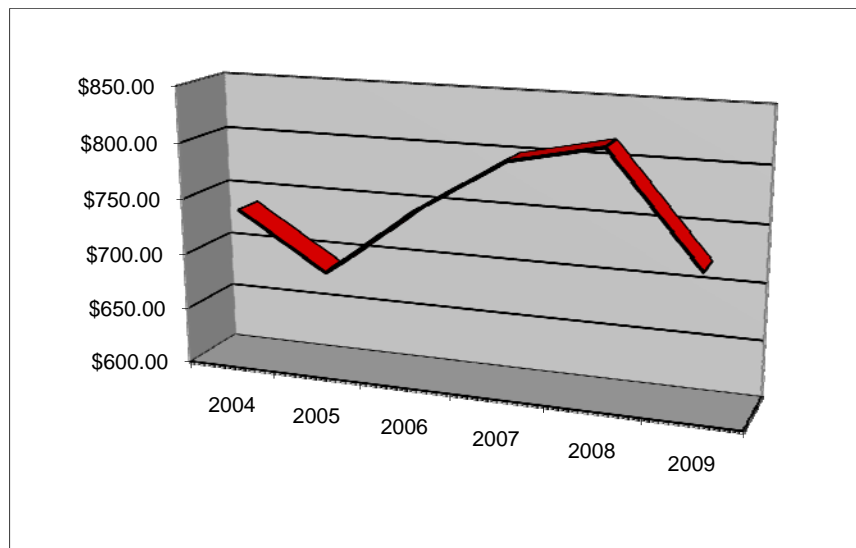
According to Co-Star, the average price of a convenience store with fuel service was \$2,055,965.00 in 2004 and \$2,229,525 in 2009.

The average price per foot was \$738.06 in 2004. Yearly increases in the median price per foot appeared to begin to level off in 2006.

### U.S. CONVENIENCE STORES AVERAGE PRICES 2004 to 2009 SOURCE: COSTAR COMPS



### AVERAGE PRICE PER FOOT: 2004 TO 2009



## Convenience Industry Conclusion

The convenience industry has come through the most difficult period it has ever experienced. Hypermarkets today are approaching a 15 percent share of the U.S. gasoline market.

The convenience industry is changing, becoming less dependent on fuel profits. This was achieved by growing in-store sales. But, because the fuel customer drives in-store sales, the fuel customer is still important. Hypermarkets are expanding their market share and will continue to do so in the coming years. This has the potential to divert fuel customers away from traditional convenience stores.

Currently, the largest issues affecting property values are at the local level. When a hypermarket enters a local trade area, the supply and demand fundamentals are significantly changed. That is why it is more important than ever for convenience stores analysts to carefully examine the local trade area for a traditional convenience store.

### ***NACS: Strategic and Competitive Issues***

The National Association of Convenience Stores (NACS), the largest convenience industry trade group, has identified what they see as the major issues affecting the this industry as stated in the *2007 State of the Industry Report* on page 17:

#### 1. Reducing Credit and Debit Card Costs

When credit and debit cards costs exceed overall industry pretax profits and inexorably grind away at motor fuel margins as prices rise, the time for action is now. Unfairly draining billions of dollars from our industry makes it hard for retailers to compete. Cards are universal and rules need to be transparent with respect to payment issues.

#### 2. Increasing Motor Fuel Margins

An industry that endures eight consecutive years of declining motor fuel margins as a percent of sales is flirting with a future financial crisis. If the profitability model is not working, eventually there will be a traumatic change in the investment equation. In the search for better motor fuel margins/profitability, firms will be forced to cut costs, reduce service, reduce cost via consolidation, rationalize their investment portfolio of stores or exist the business. It is hard to subsidize losses over the long term or make it up on in-store sales.

#### 3. Fighting Alternative Format Competition for Customers

For a long time convenience stores were the only game in town when it came to convenience. Adding motor fuel accelerated growth by bringing in repeat customers. Now all retail formats are looking at the convenience model and not only providing it but in many cases also exceeding the expectations of customer segments

#### 4. Managing Labor Costs for Both Costs and Productivity

It makes no sense to pay above minimum wages and not have benchmarks for efficiency, productivity and employee satisfaction. Attracting, training, retaining and motivating employees is key to long-term success. Facing the healthcare issue as part of this equation is critical.

#### 5. Working to reduce Governmental Regulation

The convenience store industry depends on two key categories: cigarettes and motor fuel and both are under fire from governmental authorities. What should be the industry response to higher excise taxes on cigarettes and possible FDA regulation of the category? Rising motor fuel prices tempts the government to get involved, usually for the worst. Alternative fuel subsidies send inefficient price signals to the marketplace.



### ***Fitch Ratings Current Outlook***

Fitch Ratings is one of the nation's premier risk assessment consulting firms, advising equity market investors and lenders.

Regarding franchise loan performance, Fitch Ratings' 2007 Structured Finance report states,

“Fitch Ratings' 2007 outlook for the franchise loan sector remains negative, indicating that downgrades are expected to exceed upgrades.” With regard to convenience stores and gas stations, “Fitch remains concerned about operator profitability in an environment of higher gas prices, increasing sales of gasoline through hypermarkets and intensifying competition from nontraditional retail outlets for the sale of convenience items.”

This succinct statement accurately summarizes our own industry analysis and conclusions.