

TECHNOLOGY KEY IN \$22 BILLION VENDING & MICRO MARKET INDUSTRY

Sales revenues showed steady, if modest growth of 2 percent; however, the distance between technology adopters and the rest of the industry is widening.

By Emily Refermat, Editor

CHART 1A: INDUSTRY REVENUE IN BILLIONS

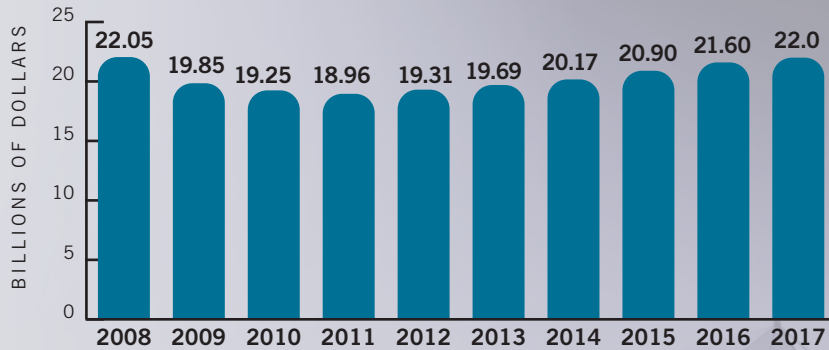


CHART 1B: MICRO MARKET OUTLOOK

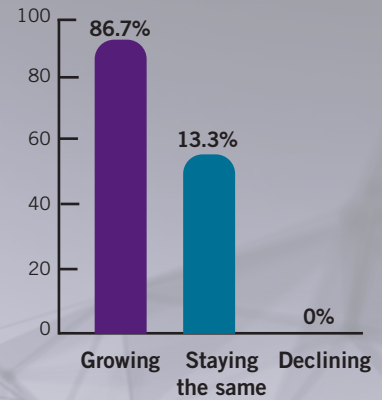


CHART 2: OPERATOR SALES

SIZE	REVENUE RANGE	% OF 2017 OPERATORS	PROJECTED 2017 SALES	% OF 2017 SALES
Small	under \$1M	57.1%	\$1.5B	7%
Medium	\$1M - \$4.9M	23.8	3.9	17.2
Large	\$5M - \$9.9M	4.8	2.4	10.8
Extra large	\$10M +	14.3	14.3	65

The vending, micro market and office coffee service industry is solid. Operators reported 2017 revenues that grew an average of 2 percent over last year, continuing the modest but steady growth the industry has experienced since 2012. As a whole, the independent operators surveyed for this report indicate the industry is a \$22 billion dollar business, with an optimistic outlook for the coming year.

Technology and utilizing it to broaden business in different segments was a key feature to success reported in 2017. When broken down by route and annual revenue, a pattern emerged that showed attitudes towards technologies differed significantly based on reported revenue (chart 6-breakout). For example, prekitting, remote monitoring and a warehouse pick

to light system were given the highest ranking (Great investment/return on investment) by 50 percent of the largest operators surveyed, those making \$10 million or more a year. When all operators were considered, the percentages were 15.6, 15.6 and 9.9 respectively. Diving deeper into the ranking of operators who make less than \$500,000 a year, the percentage dropped down further to 14.3 percent for prekitting and remote monitoring and 0 percent for warehouse pick to light systems. This is not the case for all technologies, however. Cashless got a high ranking by small and large operators, although of the people that marked it as “don’t use it/

4% HIGHER REVENUE GROWTH
was reported by operators whose service included micro markets.

CHART 3A: MACHINES BY LOCATION

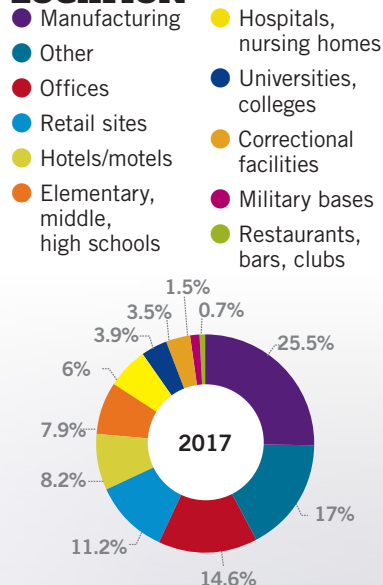


CHART 3B: NUMBER OF LOCATIONS SERVED

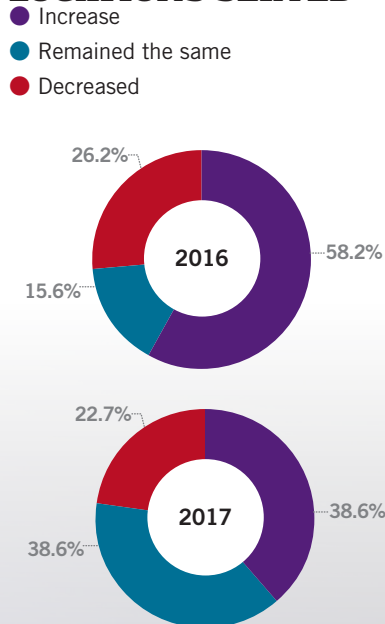


CHART 3C: MICRO MARKETS BY LOCATION

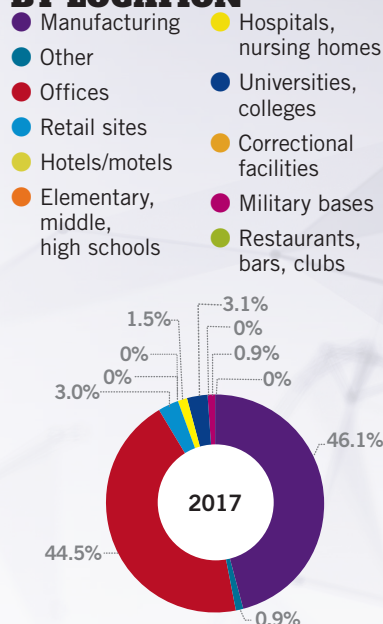
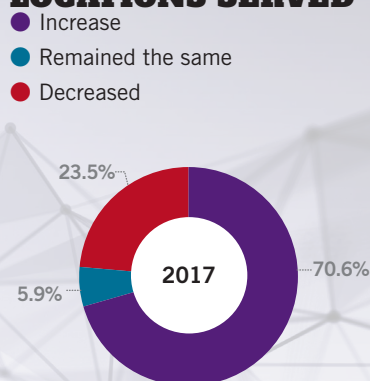


CHART 3D: NUMBER OF MICRO MARKET LOCATIONS SERVED



like it,” 14.3 percent made less than \$500,000 compared to 0 percent for the largest operators. It is important to note that for percentages relating to the smaller operations by revenue, an attempt was made to eliminate those mom and pop operations who can be successful without the use of technology, so only operations with 3 or more routes were counted in the breakout chart. Also, this data does not indicate that the use of technology leads to higher revenues, but it does show a correlation between higher revenues and technology use.

Transition in market share

In 2017 there was an increase in the number of small vending companies (chart 2). From comments, it’s clear many of the new small vending companies are healthy vending and micro market operators entering the mainstream industry, creating a subcategory. Its considered a subcategory because these operators maintain the healthy branding through their company name or marketing materials while placing both traditional and healthy items. The exact percentage that fit this profile is yet unknown, but it is a growing percentage.

Despite higher numbers of small and medium operations in 2017, their percentage of the industry’s overall revenue actually decreased. This group of operators is drawing in 6.4 percent less revenue than they did last year. The extra-large operators, on the other hand, have grown by more than 20 percent in share of revenue. It appears that larger operators are benefitting from their view and use of technology, as well as additional capital to invest in organic growth, new equipment or software, and acquiring competitors.

Cashless reaches a new high

The industry has now reached a turning point in cashless connections with more than 50 percent of

CHART 4A: PERCENTAGE OF EACH TYPE THAT MAKES UP PLACED VENDING MACHINES

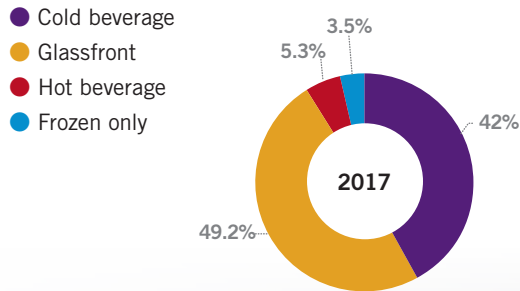


CHART 4B: ESTIMATED TOTAL VENDING MACHINES

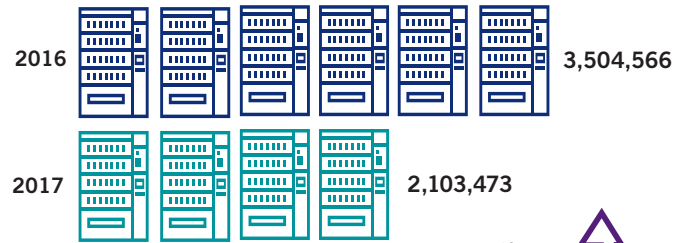


CHART 4C: ACTIVE MICRO MARKET LOCATIONS

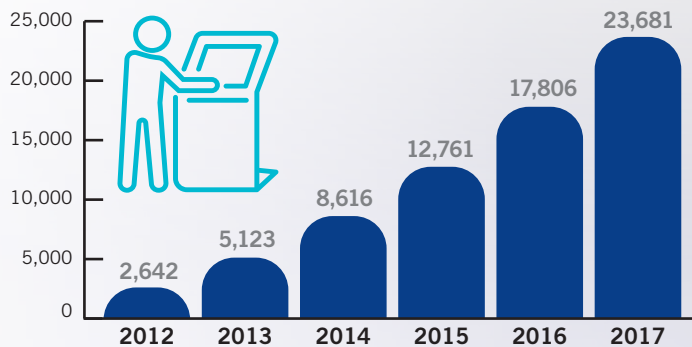


CHART 4E: AVERAGE SHRINKAGE RATE IN MICRO MARKETS

2017	
0%	0%
1%	13.3
2%	33.3
3%	20.0
4%	6.7
5%	6.7
6%	0
>7%	6.7
I don't know	13.3

CHART 4D: SMALLEST LOCATION WHERE A MICRO MARKET IS CURRENTLY PLACED

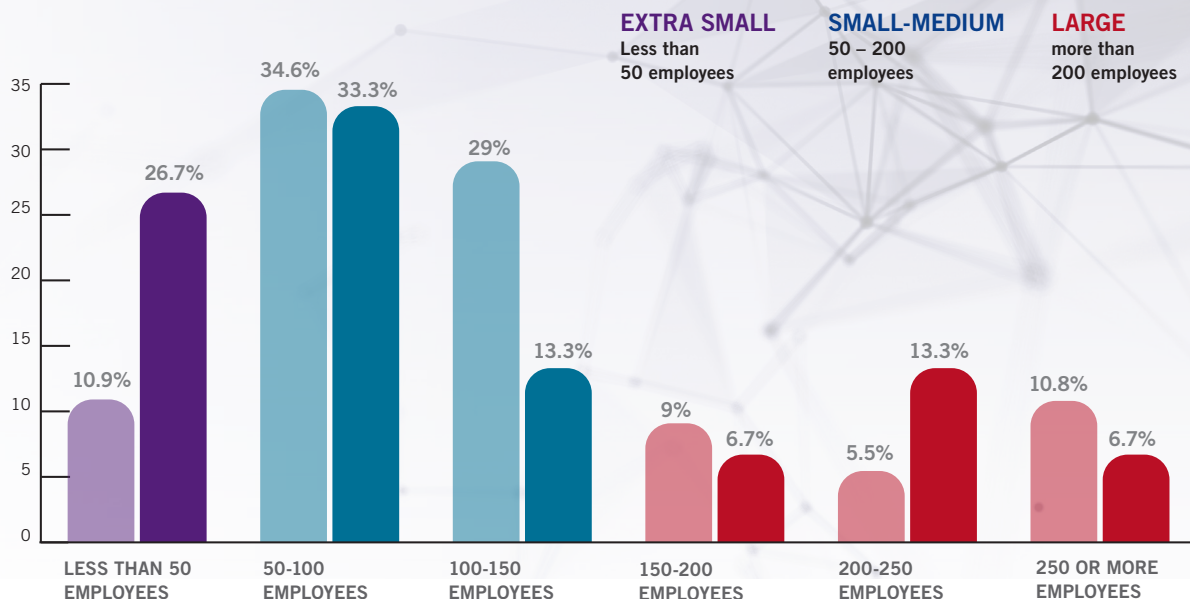


CHART 5A:

ACQUIRED OR DIVESTED BUSINESS

● 2013 ● 2014 ● 2015 ● 2016 ● 2017

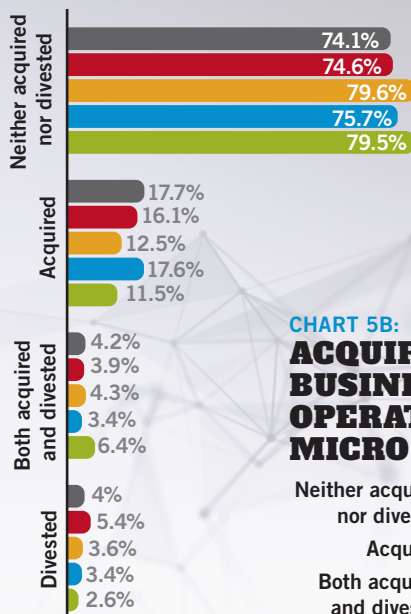
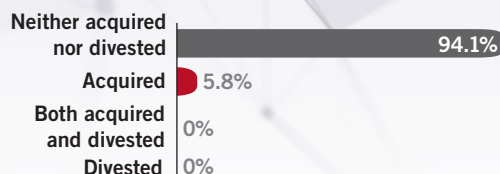


CHART 5B:

ACQUIRED OR DIVESTED BUSINESS BREAKOUT FOR OPERATORS ALSO SERVING MICRO MARKETS IN 2017

vending machines owned by independent and franchise operators accepting some form of cashless payment (chart 6). The rate of cashless adoption has been accelerating the past few years, but this is the first time a majority, even a slight majority, of vending machines placed in the U.S. accept credit or debit cards or mobile payments. While the percentage is increasing, it is important to note that the number of vending machines continues to drop due to the placement of micro markets and better reporting tools that indicate locations where revenues will not support the service (chart 4). From the latest survey, vending machine estimates are around 2 million. Most of those machines continue to be closed front cold beverage machines or glassfront vending machines which can hold a greater variety of beverages and snack items.

Operator comments indicated that in many areas, locations are the driving force behind upgrading to cashless payments. This makes sense as 77 percent of Americans have at least one credit card, according to the FINRA 2016 Investor Education Foundation's National Financial Capability Study, and 34 percent of cashless users opt to pay with debit/credit card most of the time and only occasionally pay with cash says a 2017 study by Statista. New vending machines come with cashless payment options, and there are additional benefits to the technology. By connecting a vending machine or kiosk to the internet to accept cashless payment, it can also be connected to transmit sales data. Most credit and debit card readers also accept mobile wallets, which is how many mobile wallet users prefer to pay for snacks. According to a chart from Nation's

Restaurant News, restaurant and snack purchases ranked second in top mobile purchases by mobile app users. It's a segment consumers are willing and wanting to use cashless in, both cards and mobile payments.

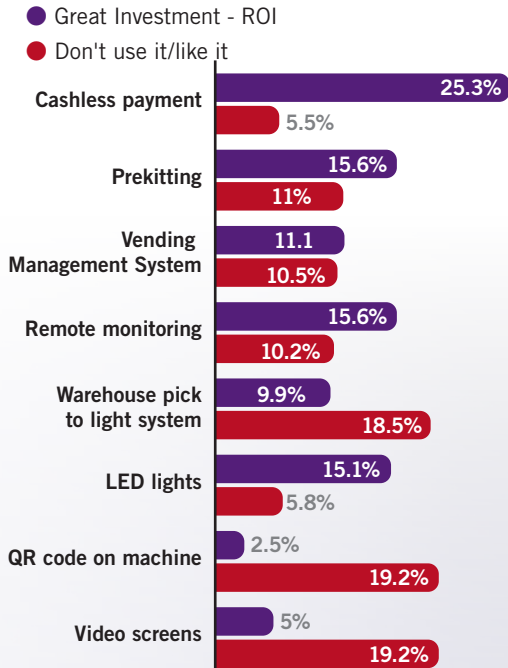
Micro market transactions are also mostly cashless, with cards being used at the kiosk as well as mobile scan and pay options. Joe Hessling, CEO of 365 Retail Markets shared that "75 percent of all 365 micro market transactions are cashless. Cash is rarely used unless it is to fund a stored value account." Additionally, 365 is opening 400 mobile locations per month with its app checkout solution. That number has been increasing rapidly.

Locations remain steady

The make-up of location types operators serve didn't change much in 2017. As a whole, manufacturing facilities remained the bulk of an operator's business representing 25.5 percent in 2017 (chart 3). Moving up to second place was the other category, which includes local businesses such as dog salons, warehouses, and local gyms as well as government buildings. Running a close third was offices, although the percentage did move down 3 percentage points, with hotels and motels gaining nearly 4 percentage points. Interestingly, many of the gains were not in places where micro markets would be placed. This demonstrates the relevance of vending machines to some extent, but also that operators are taking machines replaced by micro markets and finding other locations for them. This can lead to better route density, so a driver can deliver to more machines or stops on a single route.

When asked specifically about micro market locations, operators reported that the vast majority were in manufacturing facilities or offices in 2017. In some areas, such as Northern Indiana/Ohio, micro

CHART 6A: TECHNOLOGY RANKINGS, AVERAGED



Percentage of vending machines that accept cashless payment, such as debit cards, credit cards or mobile wallets

50.7%

CHART 6C: VENDING DATA COLLECTION TRENDS

- Telemeter or cashless device remotely/using the cloud
 ● Manual process (such as paper and pencil) on location
 ● Handheld device on location
 ● Smartphone or Tablet (Apple or Android) on location

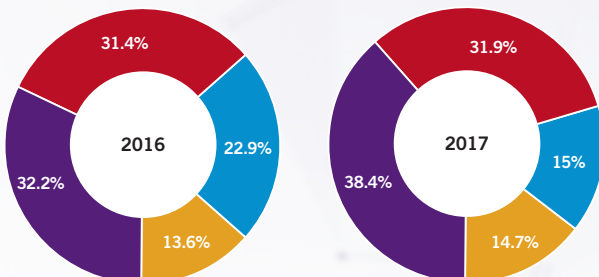
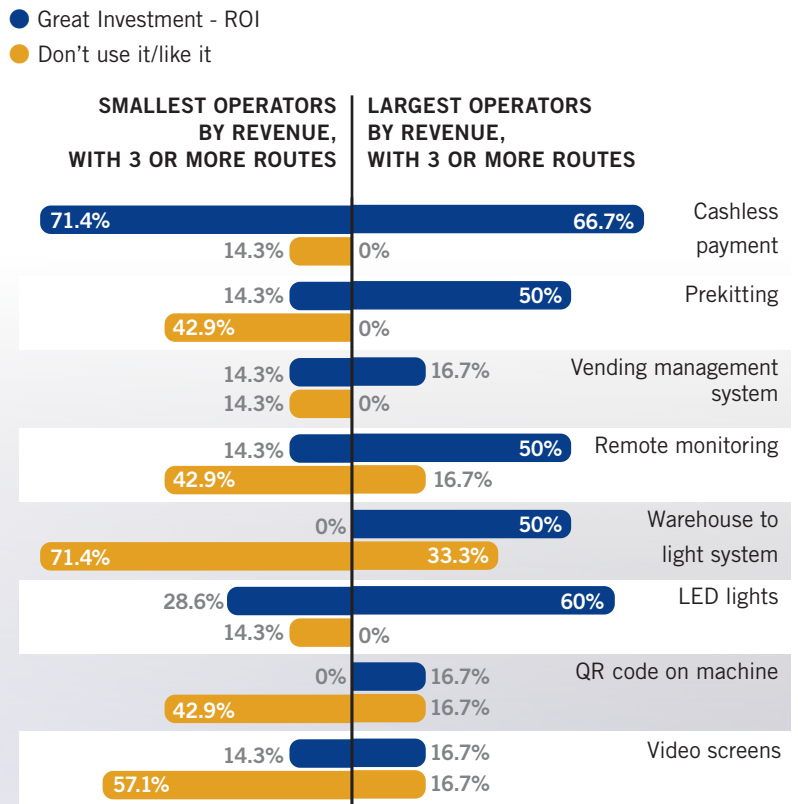


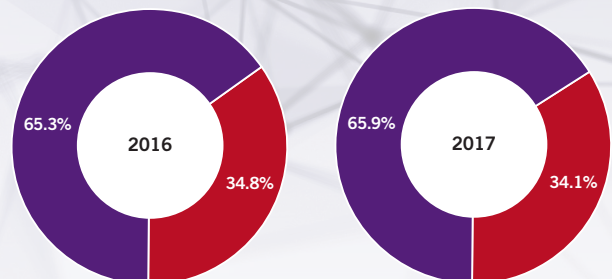
CHART 6B: TECHNOLOGY RANKINGS - BREAKOUT



* As this is a smaller sample size, there can be greater variance in the data

CHART 6D: VENDING MANAGEMENT SYSTEMS

- Use a VMS
 ● Don't use a VMS



Percentage of operators who reported having no cashless devices

12.3%

markets are not allowed in public-accessible locations due to concerns about food tampering and food safety. These issues have also been raised in the Conference for Food Protection, which is recommending that within the Food and Drug Administration's official Food Code, part of the definition for micro markets, which it calls Unattended Food Establishments, be "Entry is not accessible by the general public." The effect on the segment if this happens is unknown, as the Food Code is not law, but used as guidelines by local health departments.

Another dividing trend among operators is the level of saturation of micro markets. Operators who adopted micro markets early are now experiencing an environment full of micro markets, forcing them to be more creative in where they place the solution. It has driven the employee counts for micro markets down from the original 250 employee mark to some locations with 50 employees or less (chart 4). Those solutions are usually smaller with a tablet-sized kiosk, small snack rack and countertop cooler. For both small and full-size micro markets, how best to display products and avoid shrinkage remain top issues.

Operators diversify services

When asked about services, operators responded that 66.2 percent of their sales in 2017 came from vending, which is a decrease from the year before, but still higher than in 2014 and 2015. The micro market and OCS categories picked up part of revenue difference, but in this year's survey we also added an additional option, pantry service, which changes the percentage breakdown from the previous year, making it difficult to do a direct comparison.

However, by looking at the mix of services offered in the last several years, operators appear to be diversifying their businesses, trying out new

CHART 7A: VENDED SHARE OF SALES BY PRODUCT CATEGORY

- Cold beverages
- Snacks
- Candy
- Confections
- Healthy
- Food
- Hot beverages
- Ice cream/frozen
- Other*

* Includes non edible items

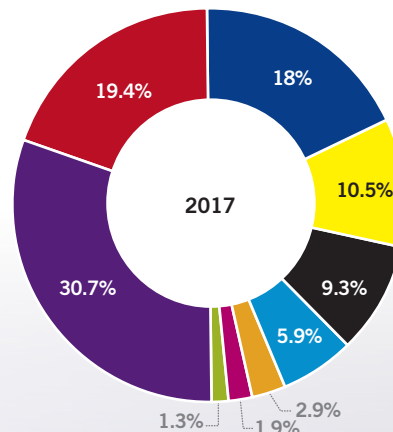
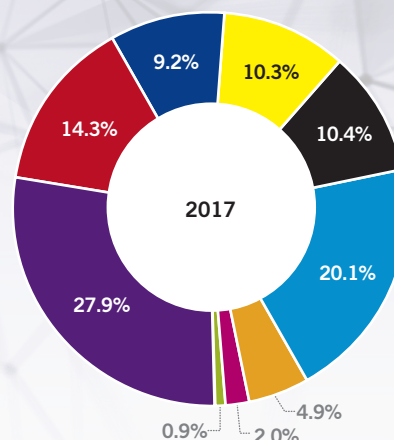


CHART 7B: MICRO MARKET SHARE OF SALES BY PRODUCT CATEGORY

- Cold beverages
- Snacks
- Candy
- Confections
- Healthy
- Food
- Hot beverages
- Ice cream/frozen
- Other*

* Includes non edible items



lines of service to match the evolving demands of customers and to insulate their businesses from declines in any one specific segment. OCS, in 2017, experienced a resurgence after three years of dropping. The percentage of annual revenue operators assigned to OCS was 7.3 percent. However, in previous years, pantry service would have also been in the OCS category. If pantry services' 2.8 percent is added, we can see that OCS is representing 10.1 percent, almost double 2016. There may also be

**FOOD
REPRESENTS
20.1%**
*of annual revenues
for micro market
operators.*

CHART 7C: SHARE OF SALES BY SERVICE CATEGORY, COMBINED SERVICES

	2014	2015	2016	2017
Vending	60.1%	54.6%	78.1%	66.2%
Micro Markets	8.9	10.2	12.9	15
OCS	13.3	6.8	5.2	7.3
Water service	1.9	2.0	1.0	4
Other	4.2	9.5	0.7	2.9
Bulk vending	2.0	2.3	0.7	1.6
Manual foodservice	7.6	9.1	0.9	0.2
Music	1.1	1.9	0.3	0
Games	0.8	3.0	0.3	0
Janitorial Supplies	0.1	0.7	0.1	0

CHART 8: PROJECTED SALES BY CATEGORY, IN BILLIONS

VENDING PRODUCTS	2017	MICRO MARKET PRODUCTS	2017
Vended cold beverages	\$4.5B	Micro market cold beverages	\$0.9B
Vended candy/snacks/confections	7.0	Micro market candy/snacks/confections	1.1
Vended other	1.5	Micro market other	0.4
Vended food	0.9	Micro market food	0.7
Vended hot beverages	0.4	Micro market hot beverages	0.2
Vended ice cream/frozen	0.3	Micro market ice cream/frozen	0.1

SERVICES	2017	% CHANGE
Vending	\$14.6B	-13.6%
Micro Markets	3.3	17.9
OCS	1.6	45.4
Water Service	0.9	340.0
Manual foodservice	\$44M	-78.0
Pantry Service	0.6	-
Other	0.6	66.6
Bulk Vending	0.4	300.0

cross over between micro markets and pantry service among operators. Hessling sees operators utilize the existing backend inventory and reporting of micro market systems (such as Nanomarkets and mobile scanning) to better manage pantry service. It's an area that will only grow in his opinion. "Pantry will continue to grow as businesses use convenience services to attract the best talent in our current environments of low unemployment," he

said. Indeed, the unemployment rate was trending down as of the publishing of this report with 3.8 percent in May 2018. Retaining and finding talented employees is a top challenge for human resource managers, according to the Society for Human Resource Management, especially among medium and large sized companies.

Micro markets are another service type used to enhance the employee experience. This in part led to the

segment's gain in share of operation revenue, which increased to 15 percent in 2017. The majority of operators with micro markets, 86.7 percent, report micro markets are still growing (chart 1). This has pushed the number of micro market locations upwards as well, with approximately 23,681 locations, a 6 percent increase from the year before. With more than one terminal at many locations, this could put the actual kiosk numbers in the 30,000s.

Beverages lead vending sales

This year, products were surveyed based on how they were delivered, either through vending machines or micro markets. This makes direct comparisons to past years difficult. One trend that still remains is that cold beverages is one of the largest product segment by sales, representing 30.7 percent of vending revenues. Larger size soft drinks gained the most in 2017 over the year before according to data provided by USA Technologies/Cantaloupe Systems. Energy drinks and bottled water/non carbonated beverages, in the 12 ounce size, also did well.

When just micro markets were considered, operators reported a slightly lower percentage of revenue for cold beverages, 27.9 percent (chart 7). It is still the highest performing product category, however food items come a close second representing 20.1 percent of micro market revenues.

Vending food on the other hand, decreased in share of sales again in 2017, from 8.9 percent to 5.9 percent. It continues to be a challenge for operators as consumers judge food items in a vending machine with trepidation that does not exist when they can pick up and examine the food.

In addition to the consumer perception challenge, as more locations are converted to micro markets, operators are removing food machines in favor of food coolers.

CHART 9: CANDY/SNACK/CONFECTION - VENDING ESTIMATE TOTALS BY CATEGORY AND SUBCATEGORY

	2017 REVENUE	% SALES OF TOTAL
CANDY	\$2.6B	
Chocolate	\$1.8B	70.7%
Non-chocolate	431.6M	16.6
Bag candies	195M	7.5
Gum & mints	135.2M	5.2
SNACKS	\$4.4B	
Bagged snacks	\$272.8M	6.2%
wafers, cookies, nuts, brownies, pretzels, fruit clusters, bagged gum, yogurt bites		
Chips	2.3B	53.1
Cookies & crackers	391.6M	8.9
Food snacks	127.6M	2.9
Cheese sticks, meat sticks, meat bites,		
Nutritious snacks	145.2M	3.3
Bean chips, granola, fruit snacks, organic items, specialty crackers/pastries/cookies, dark chocolate, bars, dried fruit, hummus		
Nuts and seeds	136.4M	3.1
Pastry	994.4M	22.6
Cupcakes, coffee cake, pies, honey buns, brownies, doughnut, muffins, danish, pastries		
DRINKS	\$4.5B	
Energy drinks, 12oz	\$112.5M	2.5%
Non-carbonated, 12oz	90M	2.0
Soda, 12oz	1.1B	24.0
Energy drinks, 16-20oz	288M	6.4
Non-carbonated, 16-20oz	760.5M	16.9
Soda, 16-20oz	2.2B	48.2

Source: Extrapolated from data courtesy of USA Technologies/Cantaloupe Systems, Inc.

In vending, the candy/snack/confections segment performed well in 2017, together representing \$7 billion dollars (chart 8). Chocolate items represented the bulk of the candy sales, 70.7 percent, while chips were the strongest snack contender with 53.1 percent of sales (chart 9). Pastry achieved 22.6 percent of sales.

One area that has gotten a lot of attention in 2017 is healthy products in both vending and micro markets. The category represented 9.3 percent of revenues in vending and 10.4 percent in micro markets for 2017. From comments, it's clear finding healthy items is a primary concern for operators and considered part of maintaining a good product mix.

Overall, 2017 ended on a positive note for vending and micro market operators. The core of the industry remains vending, which is showing positive signs for the future. Micro markets are also growing, bringing excitement and more opportunity to many operators. However, as you look deeper, it becomes clear that there are two sets of operators, ones that have embraced micro markets and technologies that make vending more efficient. These operators were many of the early adopters who now aim for integrated inventory and prekitting systems, are dealing with limited new locations that satisfy the requirements for a micro market and are considering how best to renew markets while controlling shrinkage.

On the other side, there are operators who prefer the old ways, using manual processes or once innovative handhelds (chart 6). This groups limits their investment in technology and new service solutions, such as micro markets and pantry service. It's a disconnect that continues to widen in 2018. ◀

Methodology

The *Automatic Merchandiser* State of the Industry Report is compiled from a survey sent to operators in Spring as well as operator insights and supplier input. The 2018 report is based on a 2.5 percent response rate, and includes small, medium, large and extra-large full service operations as well as snack and soda operators.