

PROFILE: PAPCO INC.

**OIL PRICES HAVE BOTTOMED
BUT THERE STILL IS MUCH TO DO**

ESTABLISHING AN EXIT STRATEGY

SIGMA'S 2015 TOP LEGISLATIVE PRIORITIES

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AMERICA'S LEADING FUEL MARKETERS

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Many companies mark their fiftieth anniversary by celebrating the past.

While PAPCO Inc. of Virginia Beach, Virginia, honors its heritage, however, at its golden anniversary in 2008 the company was focused on moving forward. “As early as 2007 we decided to significantly expand beyond our home base for, really, the first time in our company’s history,” recalls chairman and CEO John Malbon, whose father C. Roger Malbon founded Princess Anne Petroleum in 1958. “Through acquisitions we started expanding into central and northern Virginia, North Carolina, and Maryland. So on our fiftieth anniversary, without forgetting our past, we were looking very much to our future.”

In 1976, Princess Anne Petroleum purchased CAPCO, a small residential and commercial business bought at auction on Southern Boulevard in Virginia Beach, VA. This was the start of PAPCO, a new company named from a blend of the two previous company names; first year sales were just under a million dollars.

Today’s PAPCO is a multifaceted petroleum marketing company whose commercial fueling services extend across 15 states, that supplies retail dealers in five states, and continues to supply lubricants, commercial propane, home heating oil, and marine fuels to the Hampton Roads region of Virginia.

PAPCO president Gary Gilmore believes the roots of his company’s transformation date back to the late 1980s. “By then we realized that we would eventually saturate our market,” he observes. “But to maximize that potential we had to differentiate ourselves. So we started hiring people who understood price risk management, gaining experience in that area so that we could protect our customers against price volatility.”



Company founder C. Roger Malbon, and sons John (CEO/co-founder) and Charlie Malbon, 1988.

Bolstered by increasing expertise in fuel buying, PAPCO grew significantly throughout the 1990s. During the decade, the company entered the lubricants business and acquired a small chain of convenience stores. PAPCO also established a retail division that today supplies some 170 dealers in Virginia, North Carolina, South Carolina, Maryland, and Delaware with Shell, BP, Exxon, Mobil, Citgo, Valero, and unbranded product. By the end of the decade, PAPCO’s yearly volume topped 80 million gallons. “But at

the same time,” adds Malbon, “we had just about saturated our home market and had to think about expanding our footprint.”

In 2002, PAPCO started putting in place the human resources needed to expand by hiring new management positions in sales, moving the sales department into a standalone complex, and upgrading back-office computer systems companywide. In 2007, PAPCO invested in the technology required—onboard truck computers, automated dispatching, web-based reporting—to provide additional value for customers and bundle its service offerings.

Between 2000 and 2007, PAPCO also acquired five local and regional oil companies. Everything was in place to expand—the people, the expertise, the technology, and the capacity. As for capital, says Gilmore, “By the 2000s we’d been trading on the oil markets for 20 years. To get the credit we needed to expand, we had fortunately developed lots of contacts in the international banking community.”

While PAPCO strives to limit debt and fund growth through cash flow, notes Gilmore, ►

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◀ “We’ve also used our banking contacts selectively to take advantage of opportunities that present themselves.”

The remaining piece of PAPCO’s expansion puzzle, continues Malbon, “was to bring all our operations under a common PAPCO brand identity, so that we could effectively market ourselves in new territories.” In 2011, consultants were brought in to survey the company’s workforce and customer base. The goal, Malbon states, was to “launch a major strategy shift by redefining our future path and poising our brand for rapid growth by serving customers better.” To meet customers’ current and future needs, PAPCO in 2012 acquired the commercial



Colonial Pipeline, Inc., one of the many strategic partners in the PAPCO fuel supply chain.

and governmental fuels divisions of ISO bunkers, thereby extending the PAPCO trading area from New York to Florida. That year the company also began shipping product on the Colonial Pipeline, creating new opportunities for their customers and for growing its service areas along the eastern United States.

“But in addition to identifying customers’ needs, our surveys taught us something just as important,” continues Malbon, “We thought that we did a good job of communicating our mission and vision internally, to our own employees. But we found out that we needed to do better.”

Starting in 2011, PAPCO not only redesigned its customer offerings but also “discovered new ways to align our entire organization with the value proposition we wanted to offer our customers,” explains Gilmore. By 2013 the company implemented corporate training programs for all employees to communicate the new PAPCO brand identity and, he explains, “train all our people in how to deliver a consistent and newly aligned service experience for customers across 15 states.”

PAPCO uses the term “brand” not in the traditional petroleum industry sense of a

fuel brand. Rather, the company uses the term in the broader sense of what it stands for. “Our brand is about the total experience we deliver to our customers,” says Malbon, “and that experience is summed up in our corporate tagline: Solutions for Success.”

Wholesale Changes

Providing successful solutions for fuel resellers has made PAPCO a supplier of choice in 15 states. “We leverage our market expertise to develop customized supply and price risk management programs for our customers,” explains Eric Rosenfeldt, vice president of sales, supply, and trading.

“PAPCO acquires its own fuel supply,” continues Rosenfeldt, “from various branded suppliers—ExxonMobil, Citgo, Shell, Hess, BP—but also by buying directly from independent refineries and unbranded suppliers. We’ve literally bought fuel from every source available to us—again, leveraging our experience to provide solutions for customers. Also, by being a shipper on the Colonial Pipeline with inventory locations throughout the East, we offer more control over pricing and provide a secure supply.” ▶

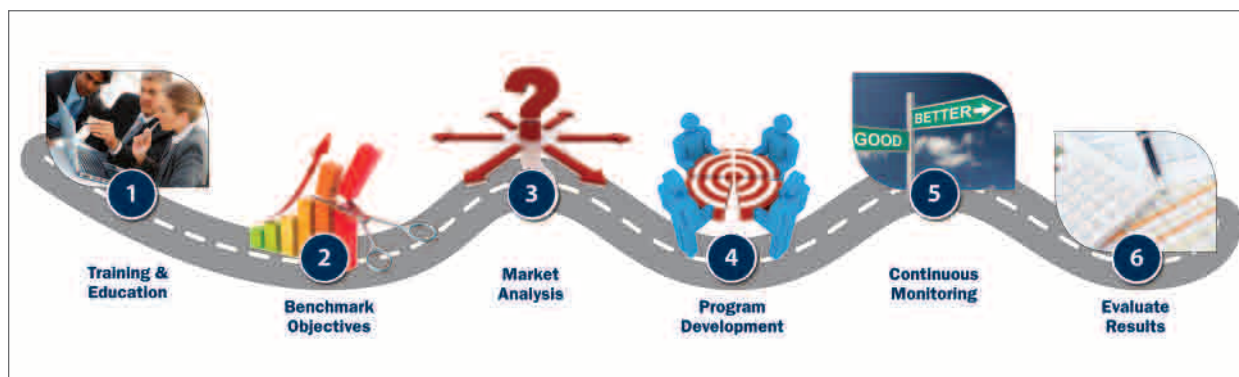
The big picture at PAPCO is rounded out by its lubricants and home heating divisions.



PAPCO brand and logo circa 1987.



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◀ “From market swings to geopolitics to extreme weather,” adds Rosenfeldt, “PAPCO customers are protected.” Security of supply is also aided through a network of longstanding PAPCO transportation partners. “We can ship by rail, barge, and truck,” he states, “to make sure our customers get product where and when they need it.”

PAPCO is licensed to operate in Delaware, Florida, Georgia, Indiana, Kentucky, Maryland, New Jersey, New York, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, Virginia, and West Virginia. Products include all grades and blends of gasoline as well as on-road and off-road diesel, biofuels, marine fuels, heating oil, and kerosene.

In addition to fuel wholesalers, PAPCO serves commercial end users and government accounts. The latter range from federal and state agencies to local school districts and mass transit authorities. These customers likewise look to PAPCO for customized supply and price risk management programs. “We use the term ‘structured deal’ to describe what we do,” relates Gilmore. “We do more than say, ‘Here’s our price, so come and get it.’ What differentiates us from competitors is that we can do everything—from pricing

options to onsite fuel delivery - that meets the different needs and risk tolerance of each customer.”

For example, PAPCO can design an automated inventory management program to replace manual ordering and thus improve efficiency and reduce labor costs. “We’ve got the latest technology to monitor inventory levels so that delivery schedules are optimized and product outages are prevented,” explains Rosenfeldt. “And if a customer is worried about the cost of carrying inventory, we offer consigned fuel programs so they’re only billed for fuel as they use it.”

Another fuel management tool is the PAPCO Universal Fleet Card powered by the Voyager Network. Accepted at more than 230,000 locations nationwide, the card allows fleet owners to organize fuel costs and reporting, capture and store electronic receipts, control driver accounts and individual card usage, and set restrictions by driver or vehicle. These data are then accessible through an online reporting system that also monitors transactions in real time.

Perhaps the greatest value-added proposition that PAPCO brings to the table,

however, is its price risk management services. “We explain our program to customers in six simple steps,” says Rosenfeldt.

“First, we train the customer’s key staff in the basics of price risk management and provide them complete access to our resources. Second, we work with the customer to create benchmarks such as budget objectives, risk tolerances, timing, and price points. Third, we analyze the market and guide the customer through their options. Fourth, we develop and execute a risk management strategy tailored to the customer’s needs, goals, and risk profile. Then the last two steps are continuous monitoring and evaluation of results.”

While most customers are familiar with fixed-price agreements, PAPCO’s suite of risk management tools include market index pricing, NYMEX triggers, index discounts with price floors, price caps, and Department of Energy indexing.

“If you don’t do anything to manage market volatility, you’re allowing an unpredictable and unstable market to set your fuel budget,” explains Rosenfeldt, “and one of the most effective tools to ▶

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◀ manage volatility is hedging, which is basically a way to transfer risk. Using carefully selected hedging products isn't speculating on the market or gambling on the price of fuel. It's a way to offset, or hedge against, inevitable fluctuations in the energy markets."

Let's Make a Dealer

On the retail side, PAPCO has exited its former company-operated sites and instead has developed a retail strategy that is focused on serving a growing network of 170 dealers in five states. "We look, most of all, at the character and quality of potential dealers," says Malbon. "Then we can help them get off the ground, open up for business, and provide ongoing site support as well as fuel supply. If their business grows, so does ours."

In the initial stages, PAPCO can aid dealers in evaluating a site, choosing a fuel brand, selecting vendors, procuring equipment bids, and evaluating financing options. To get a new, remodeled, or rebuilt site up and running—and then to monitor ongoing performance—PAPCO can help set up and maintain systems to manage equipment, inventory, and imaging.

Dealers can opt for a branded retail fuel program through PAPCO's longtime relationships with BP, Citgo, ExxonMobil, Shell, and Valero. "We not only supply the fuel," states Malbon. "We're unique in that we provide our branded dealers with the services of onsite marketing specialists. They can advise these dealers on everything from co-op advertising to point-of-purchase systems and even employee uniforms."

Yet PAPCO dealers can also opt for a customized unbranded retail fuel program. "To succeed as an unbranded marketer, you need to present a razor-sharp alternative to the majors and their national brand identities," observes Malbon. "We can help by tailoring a program—unique to each dealer—that combines ratable supply, competitive pricing, a clean image, and a flexible credit card program."

Both branded and unbranded PAPCO dealers are provided online account management, merchandising and promotional support, fuel inventory monitoring and management, industry news and updates, and a paid membership in the National Association of Convenience Stores.

In addition to fuel marketing, PAPCO's big picture is rounded out by its lubricants and home heating divisions. The company provides Mobil lubricants to commercial, automotive, and industrial customers across southeastern and central Virginia and northeastern North Carolina. Meanwhile, Malbon admits, "Home heating is a declining business, given the inroads made by natural gas. However, it is one of our legacy businesses, and we will continue to service customers that still rely on oil for their homes." ▶



By rail, barge, and truck, PAPCO gets product to customers when and where they need it.



The PAPCO Management Team in 2015.

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◀ What Lies Ahead

PAPCO's expansion has brought both rewards and challenges. "We identify ourselves as a petroleum marketing company that's involved in many channels. That affords us a certain comfort zone because it evens out the peaks and valleys in our company overall. When one business unit is down, another one is always bound to be up."

Yet as Malbon concedes, "The tradeoff is that the complexity of our business has really increased. Now that we've expanded into so many new markets, we have to deal with the fact that every jurisdiction has different taxes and different gasoline formulations. How do we store and ship the correct product at the correct time? It's a question that affects us every day. And of course, the petroleum industry itself is always changing."

To stay on top of developments and learn from others, PAPCO has been a member of SIGMA since the late 1990s. "You get out of a professional membership what you put into it," believes Gilmore. "But as we've participated in SIGMA over the years, we've gotten back even more than what we've put in. The information, the networking, the share groups—we've used all the programs that SIGMA offers. Though SIGMA members might sometimes compete, we've been so glad that our fellow marketers are always so willing to share their ideas."

Looking to the future, PAPCO is emerging from a substantial expansion cycle and taking stock of what comes next. "We started expanding more than a decade ago because we'd saturated our home

market," recounts Malbon. "But now we market all along the Colonial Pipeline and only have limited shares of our newer markets. So there's still a lot of room for growth in just the 15 states where we've expanded. Then, too, fuel demand isn't as robust as it once was—and the 2016 CAFE [Corporate Average Fuel Economy] standards are likely to continue that trend."

Another aspect of PAPCO's recent history is a decision some years ago to take the company out of family ownership. Today, Malbon and Gilmore are the owners and both have committed themselves to leading the business well into the 2020s. "We both enjoy the business and the industry," says Gilmore, "and are excited about them both."

Yet the two men admit the inevitable will come someday and that the time to start thinking about it is well in advance. "We want to build the value of the company, but not just to maximize any sale price," states Malbon, "which is why we believe in 'polishing the apple' every day."

"We are approached regularly with opportunities to improve our business, and we evaluate any potential business combinations as they present themselves," continues Malbon. "As always, any opportunity we consider must align well with our culture, values and customer value proposition, while creating value and opportunities for customers, employees and shareholders alike." **igm**



Retail strategy focuses on growing network of 170 dealers in five states.



Surveys in 2011 guided PAPCO to improve their employee engagement and customer experience.