They say where there’s smoke, there’s fire. But in the case of e-cigarettes, there’s no smoke and plenty of fire—as in a hot category that is rapidly capturing space in convenience-store tobacco sets.

Invented in China in 2003, e-cigarettes have surged in popularity and selection in recent years, with users now numbering 2.5 million and almost 20 million cartridges and 10 million disposables sold weekly in the United States, according to the Tobacco Vapor Electronic Cigarette Association.

A recent Wall Street Journal article estimated the e-cig segment as a $200 million to $500 million industry. Lorillard Inc. CEO Murray Kessler recently estimated the industry size as approximately $300 million in retail sales, a number expected to grow to $1 billion in the coming years.

But gaudy numbers do not necessarily guarantee success. Experts say convenience retailers must educate themselves on the different profiles to understand that no two e-cigarettes are exactly alike. And toward that end, they need to determine whether to carry only the lower-cost disposables or rechargeables, or both.

**Two Types, Multiple Benefits**

A disposable e-cigarette includes a battery, atomizer and a prefilled nicotine cartridge (flavored or unflavored) that can’t be reused once it is empty. It generally produces the equivalent of 300 or more puffs, or one to two packs of conventional cigarettes. They’re available in singles or multipacks and are often preferred by consumers for their lower price: typically under $10 each.

Rechargeable e-cigarette starter kits, conversely, usually include multiple rechargeable batteries, an atomizer, USB and wall chargers, and a pack of prefilled nicotine cartridges. Depending on the brand, refills in the kit are equal to a carton of cigarettes. Rechargeable starter kits range in price from approximately $30 to $80.

Leading brands available as disposable and starter kits include NJOY, blu, Krave, 21st Century, Logic and Metro.

“Typical e-cigarette users are attracted to the product for its health benefits, convenience and lower cost compared to traditional cigarettes,” says Bonnie Herzog, managing director of Wells Fargo Securities LLC, New York. “These are often current smokers who are trying to quit or cut down for health purposes as well as current smokers who use e-cigarettes as a means to smoke in areas with smoking bans.”

Based on the results of a Tobacco Talk Survey (TTS), published in May and conducted by Wells Fargo Securities, 73% of the tobacco retailers and wholesalers polled indicated that e-cigarettes are here to stay and will continue to grow aggressively. In fact, more than one-third of respondents expect sales to grow at least 40% annually.

And there was especially positive news for the c-store industry. The study reveals...
that convenience stores are the most popular e-cigarette distribution channel (56%), followed by tobacco shops (22%) and online (20%).

“E-cigarettes are to tobacco what energy drinks are to beverages,” Herzog says. “They’re profitable, capturing more shelf space and acceptance from consumers, and growing as an important new niche category for retailers.”

**Puffing on Success**

An early e-cig adopter, the Speedee Mart chain began retailing the product at its 21 Las Vegas stores in 2007 after Nevada passed a strict ban on smoking in many public places, including inside c-stores. Today it carries Gamucci, NJOY and Metro brands.

“Gambling is allowed in Vegas c-stores, and many people like to smoke when they gamble,” says Ray Johnson, Speedee Mart’s operations manager. “We experienced a 30% drop in gaming revenue after the Nevada smoking ban went into effect.”

That’s where e-cigs come into play.

“We tried to find an alternative that would encourage people to gamble longer, and electronic cigarettes were that alternative,” Johnson says. “We now give them out free to select customers who gamble within our Vegas-area stores.”

Five years ago, Speedee Mart stores offered only one product, a disposable pack priced at $24.99. As other manufacturers entered the market, the chain was able to lower its prices to $14.99, and Speedee Mart is now preparing to roll out its most inexpensive brand yet: Metro Seven disposables for $5.99 each.

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**Bonnie Herzog**

Wells Fargo Securities

Far from Vegas, Southeast chain Kangaroo Express sells three e-cigarette brands in all of its 1,650 locations across 13 states: NJOY, Metro and Logic.

“Carrying three brands allows us to reach a wider audience of guests,” says Chris Colon, category manager for The Pantry Inc., the Cary, N.C.-based parent company of Kangaroo Express. “You can compare this facet of e-cigs to that of traditional cigarettes—there are many different brands with different flavors, and each guest chooses their favorite.”

“We’re enjoying double-digit (e-cigarette) sales increases over prior months,” says Bruce Earhart, vice president of marketing for Handee Marts, Inc., a Pittsburgh-based 7-Eleven franchisor with 62 stores, many of which have been selling Xhale O2 and NJOY brands, the former since 2011. “It’s definitely a growing subcategory for us.”

**Short-Term Hit or Long-Term Kit?**

Colon believes both rechargeables and disposables deserve store presence, but says, “Disposables seem to have the greatest interest today.”

This scene is repeating itself across the convenience landscape.

“Disposables are outperforming (rechargeable) kits right now by a 3-to-1 ratio in our stores,” says Earhart. “But the advantage of offering kits is that, if you can get the customer to buy into the concept, you’ll have a customer who will be more loyal to you.”

Eli Alelov, president and CEO of Logic Technology Development LLC, makers of Logic disposable e-cigarettes, says based on research his company has conducted, only 25% of consumers who purchase rechargeable kits return to a c-store to buy refills; the rest obtain refills online either directly from the vendor or from countless Chinese websites.

“Once a customer goes online, the c-store has lost that end user, because the customer can get a refill for a third of the price online,” says Alelov, whose products are sold in 15,000 retail locations, including many 7-Elevens.

Admittedly, as a manufacturer of disposables exclusively, Alelov comes with a possible bias. But the question he asks is one that experts say is important for retailers to consider, based on their particular demographic.

“These are guys looking to buy candy, potato chips, coffee, etc. They’re the best spenders in the store,” Alelov says. “So why would you offer them a rechargeable product that will only bring them into your store once a week for a refill?”

Tobacco analyst Herzog disagrees, arguing that retailers would be doing themselves a disservice by stocking only disposables or rechargeables.

“Each appeals to potentially two different kinds of consumers,” she says. “One
may want to try it and thus gravitate to a disposable or lower price point, while the other may want to commit to the category and buy a rechargeable option. It makes sense to have multiple price points to attract various kinds of consumers to a growing category.”

Pricing Is Paramount
Ultimately, the question may center on turns and penny profit.

“Do you want to maximize your margin in the short term, or experience long-term success with lower margin and higher volume? The lower the price, the higher the volume,” says Greg Doyle, chief operating officer for Wheat Ridge, Colo.-based Nicotek LLC, makers of Metro brand e-cigarettes. “When it comes to price point, the consumer is very conscious. In a category that is still so new, brand awareness and brand loyalty have not been established yet. Therefore, price is everything.”

The sweet spot for disposables in c-stores, Doyle insists, is $10 or less, which explains his company’s recent launch of the lower-priced Metro Seven disposables. The cost for kits can, in some cases, be too high for the convenience channel, making rechargeables better suited for tobacco shops, online stores, grocery and mass retailers, Doyle says.

Johnson of Speedee Mart recommends aiming for a product price point roughly equivalent to two packs of cigarettes for disposables and no higher than a carton of Marlboros for a rechargeable kit.

“Higher price point and lack of consumer knowledge is why we haven’t offered rechargeable products until now,” says Johnson, who adds that Speedee Mart stores will soon carry a rechargeable kit for the first time. “We expect them to appeal mostly to men.”

Johnson anticipates Speedee Mart’s female customers, on the other hand, to be drawn to Metro’s Chick Stick designer pack rechargeable—featuring a small vanity mirror on the case’s inside flap—which the chain is also preparing to stock.

On or Behind the Counter?
Alelov believes c-stores should carry at least three different brands to project a perception of variety (including an entry-level as well as a premium product), and that all e-cigarette brands should be positioned together, ideally on and around (not behind) the counter.

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Sixty-nine percent of TTS respondents said that “on the counter” is the most common spot for e-cigarettes in stores, followed by “behind the counter,” next to both smokeless tobacco products and cigarettes. Also, 65% of those polled indicated that e-cigarettes are not taking significant shelf space away from traditional tobacco products.

Speedee Mart locations often stock e-cigarettes behind the counter, but some reserve POS space on the front counter. To discourage theft, Johnson suggests employing a clear plastic case that can be accessed only from the back by employees.

Handee Marts stores employ acrylic towers showcasing e-cigarette products at checkout, adjacent to lighters, providing a value and premium-priced brand at, respectively, $6.99 and $8.99.
Herzog agrees that the counter is the ideal spot to merchandise e-cigarettes. But she warns that, at some point, these products will probably be more strictly regulated—meaning retailers could be required in the future to stock them behind the counter.

“You may not want to condition consumers to see them only in one place, only to have to move them later,” she says. “Consequently, it may be best to position the products in both locations—on the counter and behind it.”

Smoke Signals on the Horizon

As retailers and store clerks explore their options and grow their knowledge, competition among e-cigarette makers should be fierce in the coming years, considering how quickly the industry is changing in the wake of buyouts and impending moves by big tobacco companies. Lorillard recently acquired blu; rumors continue to swirl that R.J. Reynolds Tobacco Co. will eventually enter the e-cigarette market; and Philip Morris USA announced in June that it plans to sell new types of cigarettes by 2017 that are supposedly safer alternatives to smoking traditional cigarettes.

“The day the big players come out with their own e-cigarette brands will mark the beginning of the end for the small guys,” says Johnson, who predicts that the category makers and brands available could be vastly different within two years. Right now, however, “Convenience retailers have reached a critical point where prices are attractive and customer awareness is increasing.”

Helping to drive sales and popularity is minimal regulation. Right now there are no federal or state excise taxes imposed on e-cigarettes (which has helped keep prices low compared to conventional cigarettes), and only a few states have enacted laws limiting e-cigarette sales to minors.

Also, few municipalities have thus far imposed bans on public smoking of e-cigarettes. Many experts, however, expect increased regulatory scrutiny and taxation of e-cigarette products in the future.

“The category is still being defined,” says Colon of The Pantry. “The e-cigarette market is currently flooded with fly-by-night companies and distributors. Once the FDA begins [to regulate this category], we will start to see definitively who the players are.”