

# OCS Growth Continues, Tempered By Regional Economics

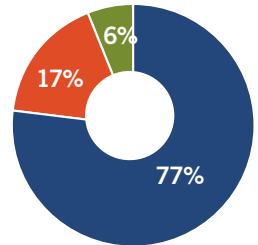
By Emily Refermat, Editor

Revenues reach a new record, but operators in some areas of the South and West are reporting revenue declines.

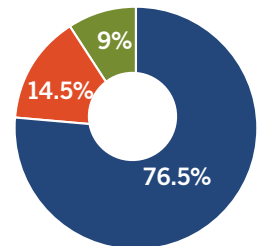


CHART 2: OPERATOR SALES CHANGE, 4-YEAR REVIEW

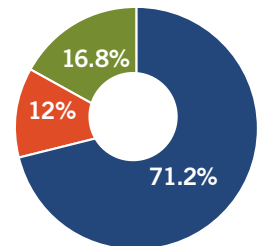
● SALES ROSE ● SALES DECLINED ● NO CHANGE



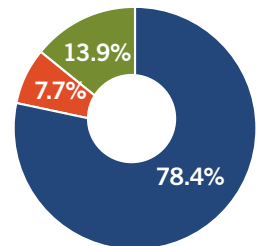
2011/12



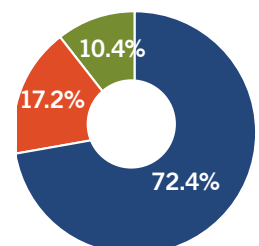
2012/13



2013/14



2014/15



2015/16

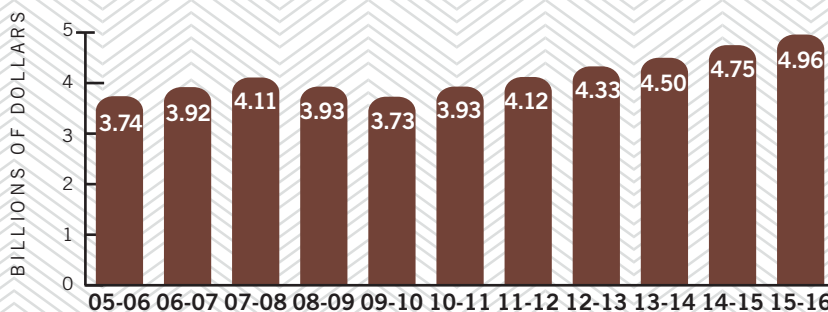
Coffee is still big business. And if you bring it to someone's workplace, it has gotten even bigger with a 4.5 percentage increase from 2015 to 2016. The industry has grown to a new high of \$4.96 billion dollars due to customer demand for premium and gourmet coffees such as fair trade and organic, but also the creation of a coffee house experience with bean-to-cup machines and specialty drinks. In addition to coffee, operators are offering more services than ever before to remain competitive and ensure they are the best one-stop-shop for their customers.

## Areas of decline

Despite the record-breaking revenue growth reported over the past 12 months for the majority of operators, there are some struggling with dropping profits. In the second half of 2015 and the first half of 2016, 17.2 percent of operators who offer OCS reported that their sales declined (chart 2). While

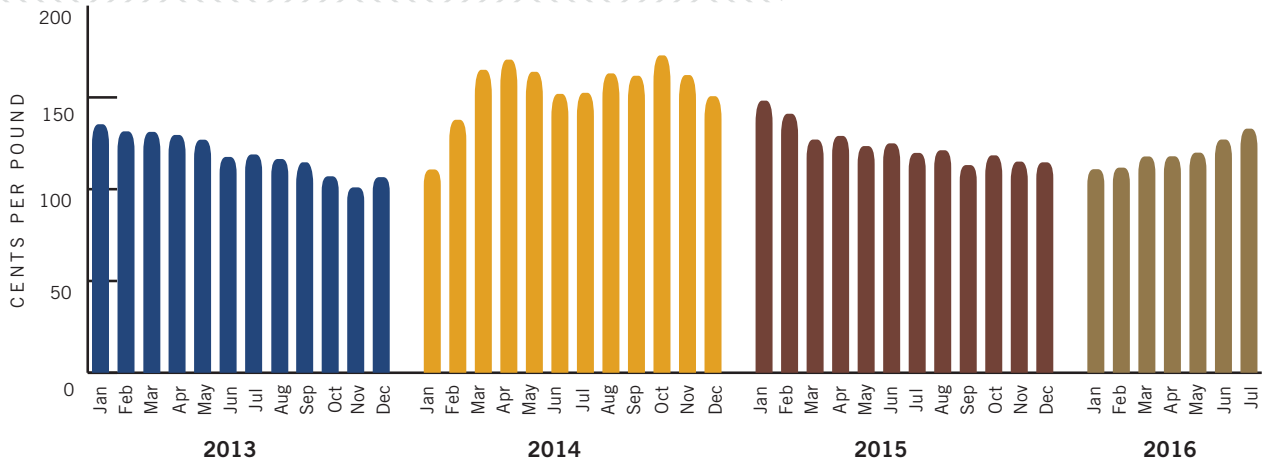
a relatively small number, it jumped nearly 10 percent in one year from 7.7 percent, which could be a cause for concern. Nearly all of the operations affected were smaller businesses that service between 1 and 4 routes and a large portion, 40 percent, are located in the Southeast. Other geographic regions where respondents reported a decline were the

CHART 1: OCS REVENUES – 10-YEAR HISTORY



# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

**CHART 3A: COMPOSITE GREEN COFFEE PRICES, 2013 TO JULY 2016**



Source: International Coffee Organization, London, U.K.

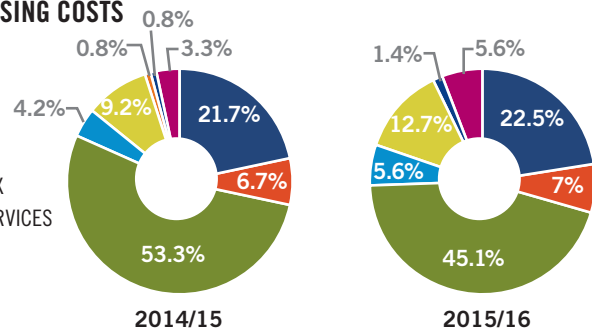
Midwest, Northwest and Southwest. Conversely, large OCS providers did not report the negative sales. In part, this might be because large operations can more easily invest in new products and services that proactively meet consumer needs.

## Green prices rise

While the price of green coffee has increased, it has not been credited with having a significant impact on revenues. The International Coffee Organization (ICO) reports a composite indicator of 132.98 cents per pound for July 2016, up 13.21 cents/pound from July 2015 (chart 3A). This is far from the highs seen in 2011, but the

**CHART 3B: HOW RISING COSTS ARE BEING HANDLED**

- RAISING PRICES
- ABSORBING
- COMBINATION
- ADJUSTING PRODUCT MIX
- SELLING ADDITIONAL SERVICES
- CHANGING WORKFORCE
- DIVESTING BUSINESS
- OTHER



\*Other includes changing product mix, divesting business, workforce changes, etc.

increase has caused OCS providers to raise prices, diversify their services and adjust their product mix.

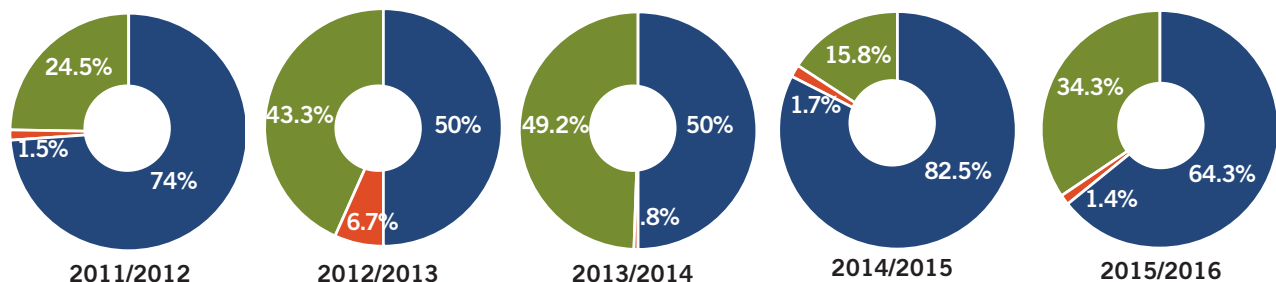
The most significant change in business strategy from last year is operators selling additional services to

handle raising costs (chart 3B) which has increased 3.5 percent. Of the additional services, the top three offered were micro markets, water service and pantry service. Adjusting product mix and divesting some or all of the

## OPERATOR PRICING ACTIVITY

**CHART 4A: OPERATOR PRICING ACTIVITY, 5-YEAR REVIEW**

- RAISED PRICES
- LOWERED PRICES
- NO CHANGE



# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

business also increased. OCS providers are working to diversify their business and adjust it to the needs of today's workplace.

One of the changes happening is employers eliminating benefits for employees, such as coffee and free food. While this is not a universal trend, indeed some employers are adding services such as free food, it is a challenge for affected operators. Provided the location has a large enough employee base, micro markets can be a solution to offer refreshment, while reducing cost. The variety of products, the ability to pick up and examine the food as well as the more positive perception of micro markets over vending, endears the service to employees and draws in additional customers that would not otherwise use a bank of vending machines.

Even OCS only operators, who do not do vending, have tried micro markets, although they have found the entry challenging. To keep spoilage low, more warehouse management has to be done and attention to reporting to maximize product sales. It has been a challenge for operators unaccustomed to delivering food products to locations.

Water service, especially point-of-use (POU) filtration systems, allows OCS providers to earn more dollars per stop with minimal investment. It has been reported as both a strategy to keep water companies from entering the location, and possibly taking over the OCS, as well as a way to help save a location money by changing to a POU system instead of 5 gallon bottles. OCS providers are advertising POU's sustainability as well and the healthy benefits of better-tasting water for employees to drink at work. Filtering also enhances the taste of coffee and tea, helping OCS providers sell it to locations.

The other top OCS segment addition, pantry service, is popular as either a way to save a location money

**CHART 4B: REVENUE PER CUP IN CENTS PER CUP, FRACTION PACK PLUMBED IN/POUROVER COFFEE, 5-YEAR REVIEW**

	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016
Revenue	11.7¢	11.8¢	12¢	12.4¢	12¢

\*Previous numbers have been adjusted based on additional data

**CHART 4C: REVENUE PER CUP, SINGLE-CUP COFFEE, 5-YEAR REVIEW**

	2011/2012	2012/2013	2013/2014	2014/2015	2015/2016
Revenue	41.8¢	43.1¢	44.9¢	45.5¢	45.3¢

\*Previous numbers have been adjusted based on additional data

**CHART 5A: % OCS SALES BY PRODUCT CATEGORY, 5-YEAR REVIEW**

	11/12	12/13	13/14	14/15	15/16
Private label coffee	28.2%	18.2%	21.8%	12.7%	12.1%
Local coffee			12.5	8.5	8.6
National coffee brands	28.1	24.4	21.9	12.1	10.6
value frac packs			3.5	5.4	6.6
whole bean coffee				4.7	2.4
espresso/cappuccino	3.7	5.4	1.9	4.3	6.6
K-cups			7.9	7.4	5.4
other single-cup			6.0	5.2	3.7
other coffee*	9.9	17.4	4.8	6.0	9.3
<b>Total Coffee</b>	<b>69.9</b>	<b>65.4</b>	<b>80.2</b>	<b>66.4</b>	<b>65.3</b>
Other hot beverages	5.5	6.4	4	3.3	3.1
Soft drinks/juices	5.7	6.6	1.8	4.5	4.0
Bottled/filtered water	4.8	7.3	3.9	5.3	4.6
Creamers/sweeteners	6.6	6.5	5.2	4.5	2.7
Cups/paper products	6.2	6.5	4.5	3.8	2.8
Tea				3.6	3.5
Pantry					8.2
Water service	1.3	1.9	0.4	4.9	5.8
Other				3.6	0.0

\*Includes flavored and varietal.

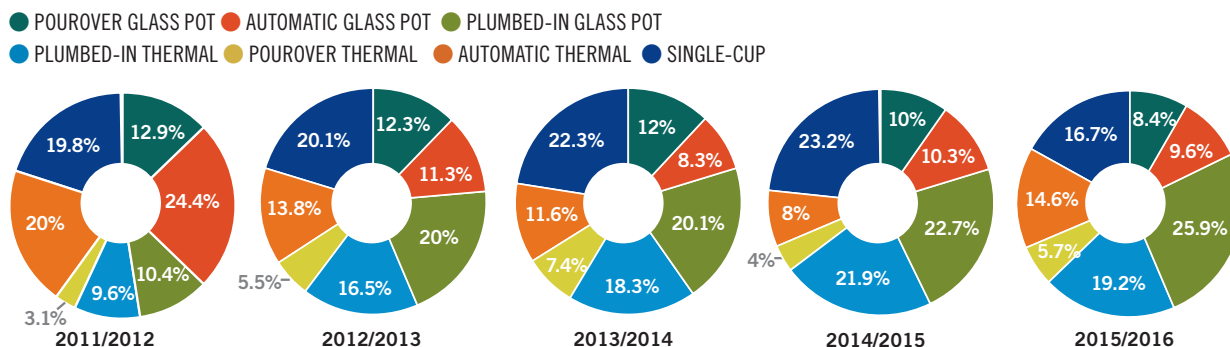
or provide additional benefits. Pantry service as an alternative to a cafeteria is less expensive and wasteful, allowing the OCS provider to help employers save on workplace refreshment costs. Where businesses are trying to lure top employees and provide additional services, it allows snacks, food, and sometimes any product, to be delivered right to work — a convenience and sought after benefit. Pantry service also covers a wide range of services. It can be defined as dropping off snacks and soda for the breakroom to offering online ordering available to the entire company

**CHART 5B: TOP-SELLING OCS PRODUCT FOR PAST 12 MONTHS**

	2015/2016
Local coffee brands	5.7%
Private label	42.9
Value frac packs	8.6
Specialty drinks	0.0
Whole bean	0.0
National brand coffees	20.0
K-Cups	14.0
Single-cup	2.9
Tea	0.0
Pantry	2.9
Water service	0.0
Other	2.9

# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

**CHART 6: PLUMBED-IN, AUTOMATIC AND THERMAL AS % OF TOTAL, 5-YEAR REVIEW**



**CHART 7: ESTIMATED MARKET SHARE OF SINGLE-CUP BREWER PLACEMENTS IN THE U.S., 5-YEAR REVIEW**

MARKETER	PRODUCT(S)	2011/12	2012/13	2013/14	2014/15	2015/16	% Change
Bodecker Brewed	Bodecker	0.3%	0.4%	0%	2.5%	0.4%	-0.9%
Cafection	Avalon	3.9	2	3.3	6.4	9.7	0.5
Cafejo	Cafejo	2.4	2.4	0.0	0.1	0	-1.0
Technologies Coffea	Coffea				0.3	0	-1.0
Crane	Café System, Genesis	1	1.3	0.3	5.2	11.2	1.2
Filterfresh	Filterfresh	1.4	4.7	2.9	1.2	0	-1.0
Grindmaster	Grindmaster	1.4	6.0	0.1	1	0	-1.0
JM Smucker's	Douwe Egberts				2.9	7.5	1.6
Keurig	Keurig	46.2	46.2	39.6	30.0	21.3	-0.3
Kraft	Gevalia, Tassimo Professional	0.8	2.9	3.9	9.8	9.6	0
Lavazza	Espresso Point, Lavazza Blue	1.7	2.1	0.4	5.3	4.8	-0.1
Mars Drinks	Mars Drinks (Flavia)	30.1	23.4	37.5	16.8	9.3	-0.4
Newco	Smartcup, Freshcup, CX-3	0.4	2.2	1.7	4.3	4.9	0.1
Rheavendors	Rhea, Cino	0.3	0.1	0	0	0.2	0
Saeco USA	Saeco, Estro	2.0	0.6	0.0	0.5	0.1	-0.8
Starbucks	Starbucks	0.8	1.6	2.6	2.7	2.4	-0.1
Technologies Coffea	Coffea	0.2	0.0	0.0	0.3	0	-1.0
VE Global Solutions	Brio, Colibri, Cypris, Juno, Koro, Korinto, Kinvivo, Prosy, Venus	1.6	0.1	1.9	4.9	1.8	-0.6
VKI Technologies	Eccellenza Express, Eccellenza Touch, Eccellenza Cafe				1.2	0.1	-0.9
Wolfgang Puck	Wolfgang Puck	0.3	0.3	0.1	0.3	0.2	-0.4
Other		0.2	0.8	0.8	1.1	16.3	13.8

\*Represents OCS provider placements only

that is delivered the next day with the OCS driver. It's a wide variety, but is essentially anything the customer wants, and the operator can deliver.

## Non-coffee fuels growth

Competitive forces are causing OCS providers to alter their product offerings to be more inclusive

of what the market is demanding. That includes non coffee items as much as it does specialty coffee. According to operators, an average of 34.7 percent of their annual revenue is made up of products and services other than coffee (chart 5). Pantry service and water service saw a substantial increase in share

of revenue, currently 8.2 percent and 5.8 percent respectively.

While soda and bottled water appear to be dropping in share of revenue, these product segments are being lumped into pantry service when it's offered by operators. When you add soda, water and pantry service, you get over 16 percent of the

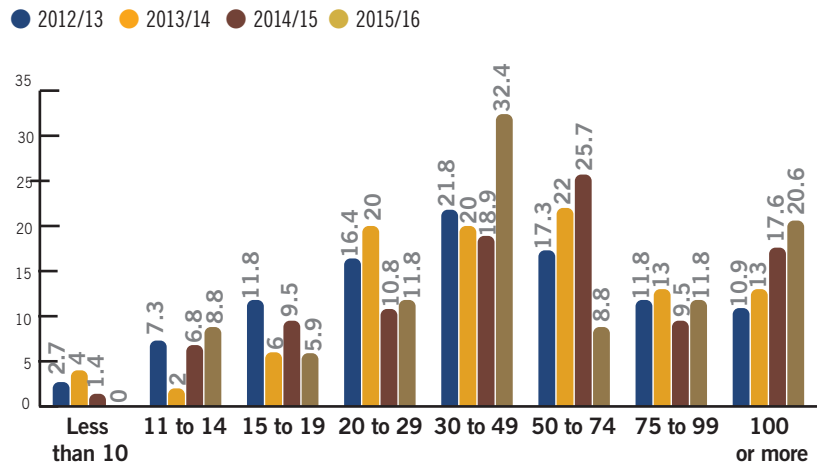
# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

revenue. This may not be what every operator offers, but it's a significant sign that maintaining a strong OCS business means diversifying into non coffee beverages, too.

Coffee can't be underestimated in OCS revenues, however. It still represents 65.3 percent of revenues. Operators who offer espressos, cappuccino and specialty coffees (mentioned in 'other') have increased. These are popular options for the business that is spending money on employee morale, retention and productivity. Specialty coffee is especially popular among companies appealing to Millennials.

Value coffee also spiked in this year's report due to those regions dealing with economic hardships. When asked what impacted their business "a lot" in the past 12 months, 35.7 percent of operators reported it was an area business closing (chart not shown). When combining those that said "a lot" and those that said "a little" it was 92.8 percent of operator respondents who had issues with accounts shutting down. Most operators were able to gain other accounts, but not all.

**CHART 8: ACCOUNT POPULATIONS BY SIZE**



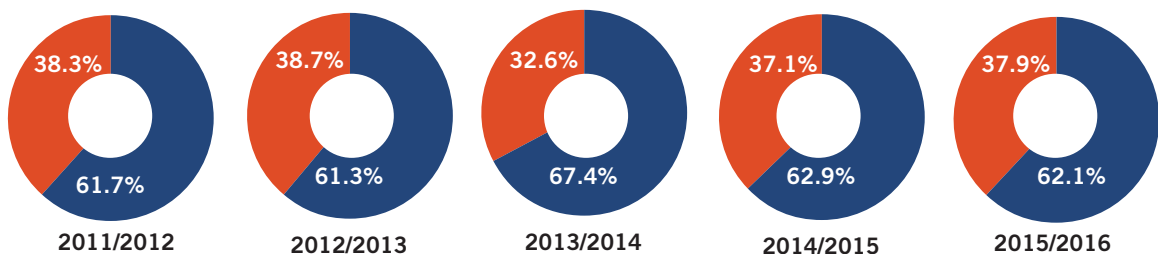
**CHART 9: ACCOUNTS BY TYPE, 5-YEAR REVIEW**

	2011/12	2012/13	2013/14	2014/15	2015/16
Offices	55.8%	48.8%	45.0%	47.4%	46.6%
Industrial plants	18.7	15.1	17.3	17.1	12.9
Restaurants, delis, bakeries	4.5	6.3	7.3	8.5	7.1
Convenience stores	5.2	7.2	8.3	4.7	8.8
Government/military	3.3	5.4	3.5	3.3	1.7
Schools/colleges	3.8	5.2	5.4	6.7	7.7
Retail outlets	1.9	2.11	2.7	5.8	6.2
Other (health care/hotels)	6.9	10.1	10.5	6.5	8.9

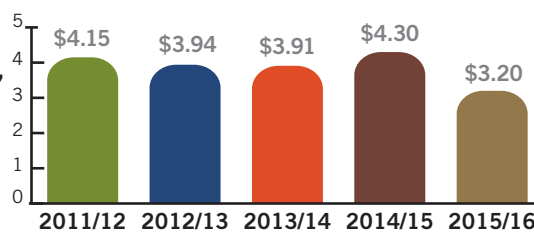
## FUEL CHARGE ACTIVITY

**CHART 10A: COMPANY BILLED CUSTOMERS FOR FUEL, 5-YEAR REVIEW**

● YES ● NO



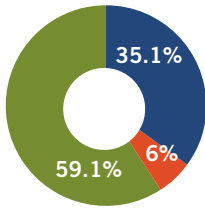
**CHART 10B: AVERAGE AMOUNT CHARGED FOR FUEL PER DELIVERY, 5-YEAR REVIEW**



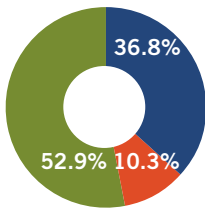
# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

**CHART 11A: HAVE ADDED OR REDUCED STAFF IN THE LAST 12 MONTHS**

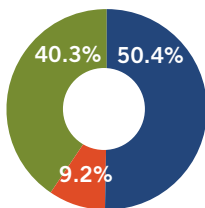
● ADDED ● REDUCED ● NO CHANGE



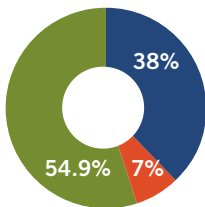
2012/2013



2013/2014



2014/2015

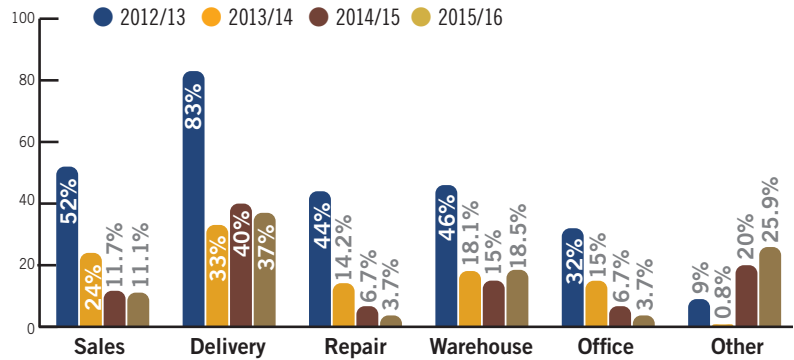


2015/2016

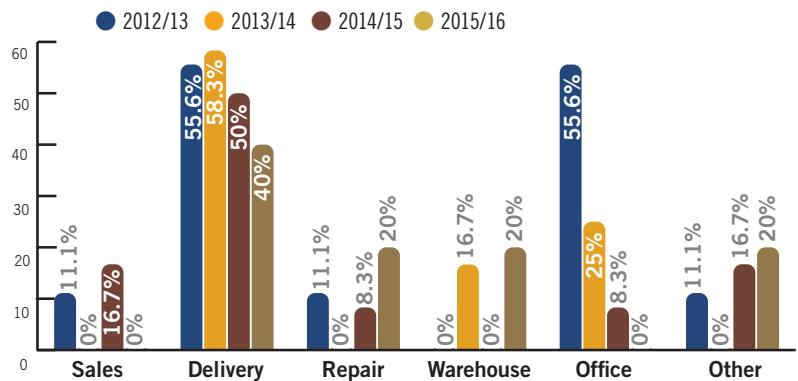
The continuing low price of oil and gas have added to the strain in regions that rely on this industry. In these struggling areas, value becomes a prime selling tool as well as offering other services that can save money, such as POU water systems.

Unlike vending and micro market focused business, those operations that center on OCS feel that they have an appropriate number of drivers and driver applicants available to them. In the State of the Vending Industry Report, find-

**CHART 11B: IF ADDED STAFF, IN WHICH AREAS?**



**CHART 11C: IF REDUCED STAFF, WHICH AREAS?**



ing and retaining top quality drivers was identified as a challenge, but this obstacle was ranked very low by OCS providers. Implementing and using technology was also ranked low in terms of challenges for OCS providers.

## Single-cup hits a slump

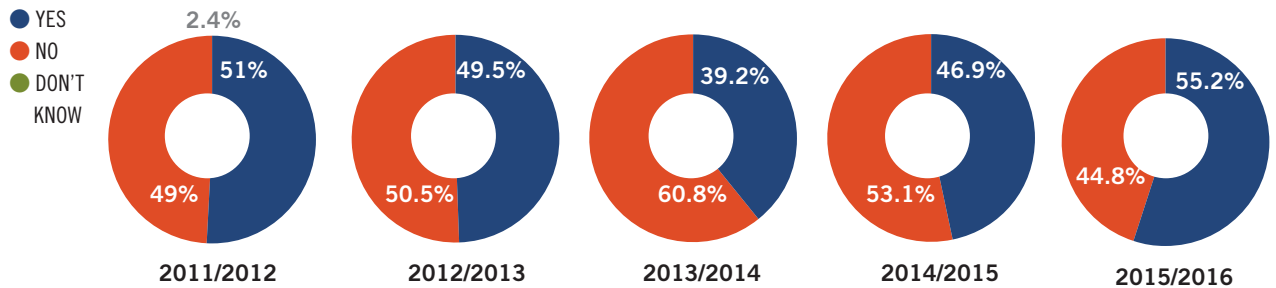
Last year single-cup was driving growth. This year, it has stalled, losing both percentage of revenue and single-cup brewer placements. According to operators, this is due to a combination of factors. First, in regions struggling to keep business, the pricing of single-cup and the number of competitors that sell on price drive down the profitability of single-cup accounts. The price charged for single-cup has actually decreased a few tenths of a cent to 45.3 from 45.5 cents per cup,

despite few operators reporting they lowered prices in 2015/2016 (chart 4). Instead coffee brewed in automatic thermal brewers is doing well. Automatic thermal brewers almost doubled in placements in 2015/2016 (chart 6). Plumbed in brewers still represent the bulk of placements.

One bright note for single-cup is the popularity of multiple types of brewers. Many operators noted that pod brewers are becoming more accepted by end users, and represent a better profit margin for operators than many cartridge or flat pack style brewers. Also single-cup brewers, especially bean-to-cup systems, are associated with gourmet and premium hot beverages, which deliver a more coffee-house experience. These types of brewers also allow for sales of solubles; choco-

# STATE OF THE OFFICE COFFEE SERVICE INDUSTRY

**CHART 12A: HAVE ADDED PRODUCTS THAT ADDRESS ENVIRONMENTAL CONCERNS, 5-YEAR REVIEW**



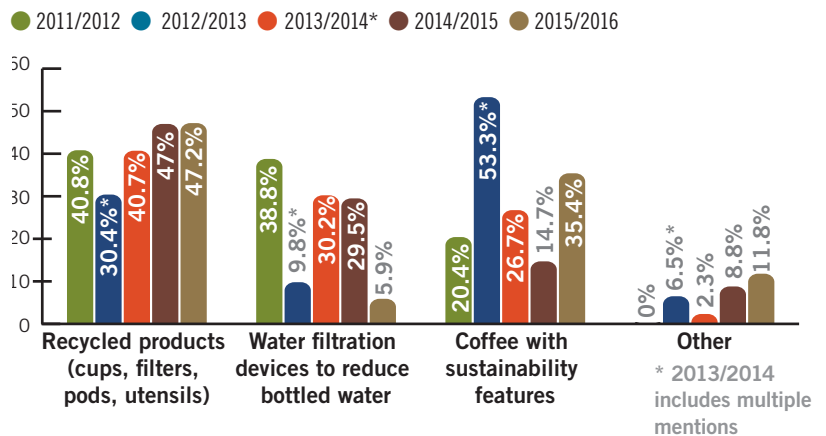
lates and milk powders to help build the ticket, or increase revenue. This type of brewer is still sought after by many locations, and will likely increase in areas where the economy is booming. Bean-to-cup was reported by 43 percent of OCS providers as the most significant single-cup brewer to affect revenues. It allows for a premium bean and freshly made quality coffee which consumers demand.

## Diversifying locations

Offices still represent the majority of locations OCS providers service (chart 9), with the bulk having between 30 and 49 employees (chart 8). That location size grew significantly from last year, as the 50 to 74 employee locations shrunk. This illustrates the challenging economics and location closings in certain areas. The largest locations also showed fluctuation, but not as dramatically.

The number of industrial plants and military bases where OCS is provided dropped in the end of 2015 and beginning of 2016, according to operator reports. Instead, OCS providers are picking up locations in the convenience store segment, as well as some in retail, schools and hospitals. OCS providers are getting better at expanding their search for profitable OCS locations outside the traditional workplaces. However, from comments, the changes in ser-

**CHART 12B: PRODUCTS ADDED THAT ADDRESS ENVIRONMENTAL CONCERNS, 5-YEAR REVIEW**



vice and different product mix often come from customer requests or in reaction to competition. Few OCS providers were proactive in offering additional services and products in 2015 and 2016, especially among smaller operations. At the other end of the spectrum, OCS leaders have been able to get out in front of the curve and offer what their customers want before being asked. This has allowed them to maintain a top service position, earn the best prices and drive record revenues.

The industry's growth is cause for celebration. Coffee will continue to be a desired benefit for the foreseeable future. Challenges from business closures and companies eliminating free coffee are troubling, but hopefully won't continue into 2017. | ◀

## Methodology

The *Automatic Merchandiser State of the Office Coffee Service Industry Report* is compiled from a survey sent to OCS operators, as well as operator interviews. The 2016 report is based on a 5 percent response rate to the survey and includes full-service vending operators who offer OCS as well as operators who only provide coffee service.