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A Hectic Year in Tobacco & Nicotine

Much happens in a year in any given product category: Regulations change, new products are launched, consumer trends shift. It's a lot to track. *CSP's* Tobacco Category Digest curates our top-level articles, trends and data in these product segments to give category managers and others studying the behind-the-counter set of the convenience store a convenient and comprehensive glimpse into this evolving market.

In this handbook, you get an at-a-glance look at scan-data trends for tobacco and nicotine products, as well as sales trends as reported by convenience retailers and suppliers.

You'll see how regulation is stifling sales in several segments and how consumers are pivoting to alternatives as a result. You'll see how politics are forcing oversight change and how retailers are reacting in their stores.

This is a year's worth of how suppliers and retailers are adjusting in a category in constant flux. Keep it around all year to help determine where we've been and where we're going as you evaluate new products, marketing efforts, merchandising, trends and more.

Enjoy,

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Content Director
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INSIDE

Facing Hurdles

How COVID-19, regulation is affecting c-store's tobacco sales

BY HANNAH PROKOP AND MELISSA VONDER HAAR

Tobacco category managers are facing mounting regulatory hurdles in 2021; however, the past year has also brought some positive changes. Innovation, especially in smokeless tobacco, has category managers excited for the future. Here's how three convenience-store and tobacco-industry veterans are making it work during a challenging time.

What drives Kevin Harder's passion for the tobacco category is clear: He wants to help customers find products that will transition the category to a smoke-free future.

"It's important for everyone's well-being that we eventually get there, but it needs to be done responsibly, in a way that moves people from smoking to less-harmful forms of tobacco/nicotine usage over time," Harder, tobacco category manager at Des Moines, Iowa-based Yesway, says.

This is challenging, though, as the category faces increasing regulation from the U.S. Food and Drug Administration's (FDA's) premarket tobacco product application (PMTA) process to local and state flavor bans and cigarette warning requirements.

"Solely legislating our way to a smoke-free future would have a tremendous negative impact on our business," Harder says.

Despite the challenges, the category has seen some wins over the past year. Work-from-home and social-distancing measures put in place due to COVID-19 have meant that tobacco and nicotine is much easier to smoke at will, Goldman Sachs Managing Director Bonnie Herzog wrote in a report on the results of the New York-based company's fourth quarter of 2020 retailer survey.

Innovation, like modern oral nicotine, has spurred growth. Spitless tobacco was up nearly 67% in c-store dollar sales for the 52 weeks ending on Dec. 27, 2020, according to Chicago-based market research firm IRI. It was up about 68% in unit sales during that time.

Cigarette dollar sales even took a positive turn. They were up 1.1% in c-store dollar sales for 2020, compared to a 1% decline the previous year, according to IRI. Unit sales for the subcategory, however, remained negative.

The constant evolution of the category is what Cory Robinson, director of marketing at E.J. Pope & Sons' Handy Mart c-stores, likes most about it.

"There is never a dull moment in tobacco and nicotine. Products and programs are constantly evolving, so you have to be agile and versatile to be successful," Robinson says. "I also believe that engaging our suppliers and distributors is critical to success. When there is buy-in from all parties, it allows us to get creative with some of the things we are able to accomplish."

Robinson, who manages the Mount Olive, N.C.-based chain's nearly 40 stores, says his category management philosophy includes three steps: Be continuously and constantly improving, seek out new and better opportunities for the category, and focus on progress, not perfection.

The pandemic changed the category in many ways, he says, and he expects many to stick.

Handy Mart stores served fewer customers in 2020 but benefited from higher average basket sizes. Customers were also more commonly trading up to multipacks of tobacco products, especially at the start of 2020, which Robinson attributes to consumers trying to limit the number of trips outside of their homes due to COVID-19.

"This pandemic has extremely impacted consumer behavior to its very core, in a very short time frame," Robinson says. "It has influenced everything from how much they buy, to how they buy, to when they buy."

The result? Retailers are scrambling to accommodate consumer demands in any way they can, he says.

One way they might be able to do this is through the modern oral nicotine (MON) segment. While these products are in their infancy, Robinson has carried Richmond, Va.-based Swedish Match's Zyn for more than a year and it is doing fantastic, he says. He also recently started selling On from Richmond, Va.-based Altria Group, which is so far having very good results, he says.

Sean Carroll, category and PDI program manager at G&M Oil Co., Huntington Beach, Calif., plans on continuing to make MON a focus for 2021.

G&M's more than 170 stores—which include the Chevron Extramile, Chevron Food Marts and G&M Food Marts brands—sell Zyn and On to give consumers nicotine alternatives, Carroll says.

The modern oral nicotine segment and others, though, are threatened by regulation, Carroll says.

"We are at such an interesting period with this category," Carroll says. "We've seen unbelievable innovation over the last five to 10 years and just as unbelievable regulation and restrictions. The category requires great vision and constant review."

Carroll, who has worked in c-stores for 20

"This pandemic ... has influenced everything from how much [consumers] buy, to how they buy, to when they buy."

67%

Growth in dollar sales of spitless tobacco in c-stores in 2020, according to IRI

years, the last four of which have been in his current position, says his biggest challenges today are local tobacco flavor bans and federal regulation.

In February 2020, the FDA banned the sale of flavored cartridge-based electronic-cigarettes, except for tobacco and menthol flavors. Flavored vaping products could come back on the market legally if the manufacturer submitted a PMTA application by Sept. 9 and the FDA authorizes it. The organization has thousands of applications to sift through, though, so retailers won't know anytime soon.

States have also enacted flavor bans. Massachusetts' flavored tobacco ban took effect in June. California's governor approved a flavored tobacco ban in August; however, opposition collected enough signatures to place the move on a statewide ballot. A referendum is expected to be put in front of California voters in the November 2022 election.

"I've always been a proponent of letting consumers decide what they want to use," Carroll says. "Prohibition was tried in our country and didn't work."

The regulation has taken a toll on the electronic-cigarette category. Vape cartridge sales took a dive in 2020, down 9.8% in shipments to retail through third-quarter 2020, according to data from Pittsburgh-based Management Science Associates Inc. (MSA). However, flavored disposable e-cigarettes, which were allowed to remain on the market, saw shipments to retail rise nearly 97% during the same time frame, MSA said.

Herzog of Goldman Sachs has said she's cautiously optimistic about e-cigarettes but was more bullish on them a couple of years ago when regulation was more limited.

"We've seen unbelievable innovation over the last five to 10 years and just as unbelievable regulation and restrictions."

Meanwhile, cigarette sales declined at a slower rate than many expected during the pandemic. However, retailers and manufacturers who responded to Goldman Sachs' fourth-quarter 2020 survey said they expect volumes to return to historical decline rates in 2021.

This was primarily due to tougher e-cigarette comparisons; a return to normal behavior as people return to offices and therefore, fewer opportunities to smoke; and a shift to alternative nicotine products. About 20% of those surveyed said they expect smokers to seek alternatives, primarily modern oral nicotine options, as well as e-cigarette products.

On the other hand, another 20% of respondents said cigarette volumes will continue to grow in 2021 as consumption habits developed over the pandemic.

Carroll is interested to see how e-cigarettes perform. In particular, he'll be watching Vuse Alto from Winston-Salem, N.C.-based R.J. Reynolds Vapor to see if it can build to a strong second to Juul. According to retail shipment data from McLane, Vuse Alto was the top vapor starter kit distributed in 2020. Juul Classic Menthol Pod 0.7 milliliter four-packs were the top vapor e-liquids shipped by McLane in 2020.

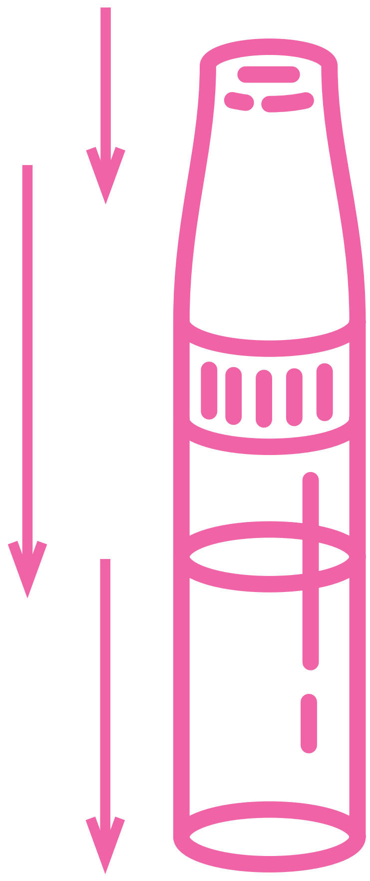
Carroll says through the pandemic, he's been connecting with category captains virtually to stay in touch. This year he added additional areas of partnership relating to loyalty with Altria, R.J. Reynolds and Juul.

Robinson of E.J. Pope & Sons also keeps in close contact with his captains, using their analytics to help determine if any changes he makes are benchmarking properly against the industry. He's even worked with them to install new fixtures together over the past year.

Looking forward, Robinson hopes to continuously improve and work on store-specific category plans along with chainwide category plans, keeping in mind that not all stores are the same.

Whether the world is in a global pandemic or not, tobacco is ever-changing, he says.

"The constant evolution of the category, new items, new programs, new regulations [makes me most passionate about the category]," Robinson says. "There is always something going on with tobacco."



9.8 %

Decline in vape cartridge sales in shipments to c-stores through the third quarter of 2020, according to MSA

Insight: Sept. 9, 2021, is the deadline for the FDA to make final decisions on PMTAs, which largely affect the outlook of the e-cigarette category. However, the FDA has said it is unlikely that the agency will make the deadline.

Where the Gains Are

Tobacco sales increased in convenience stores 2.6% for a total of nearly $73.5 billion, according to IRI, but unit sales dropped by 1.6% in 2020. Dollar sales for cigarettes, the largest segment with $56.1 billion in sales, grew 1.1% but unit sales fell 5%, even as consumers found more occasions to smoke at home amid the COVID-19 pandemic.

While electronic cigarettes saw 14.5% growth in unit sales in c-stores in 2020, it's a significant deceleration from the 59.1% the segment grew in 2019, IRI data shows. The U.S. Food and Drug Administration's ban on flavored cartridges in early 2020 and local and statewide tobacco flavor bans are likely causes of the slowdown.

Spitless tobacco saw significant growth, up 66.9% in dollar sales and 67.8% in unit sales, according to IRI.

NielsenIQ data shows cigarettes down 3% in unit sales in c-stores for 2020. Smokeless tobacco, electronic cigarettes, cigars, tobacco combination packs and shag all grew in unit sales in c-stores, NielsenIQ data shows.

C-store sales, 52 weeks ending Dec. 27, 2020

CATEGORY	C-STORE SALES ($ MILLIONS)	PCYA*	UNIT SALES (MILLIONS)	PCYA*
Cigarettes	$56,107.7	1.1%	7,284.0	(5.0%)
Chewing tobacco/snuff	$7,121.3	2.5%	1,188.8	(6.5%)
Spitless tobacco	$1,009.3	66.9%	195.1	67.8%
Total smokeless tobacco	**$8,130.6**	**7.7%**	**1,383.8**	**(0.2%)**
Cigars	$3,846.4	10.1%	2,432.8	5.4%
Electronic smoking devices	$4,863.2	4.8%	368.5	14.5%
Smoking accessories	$369.8	22.4%	192.4	15.9%
Pipe tobacco	$96.8	(8.3%)	10.7	(15.0%)
Roll-your-own tobacco	$50.1	0.5%	5.9	(8.2%)
Total all other tobacco products	**$146.9**	**(5.5%)**	**16.5**	**(12.7%)**
Total all tobacco products	**$73,464.7**	**2.6%**	**11,678.0**	**(1.6%)**

Source: IRI

C-store sales, 52 weeks ending Dec. 26, 2020

Cigarettes	$52,978.3	3.3%	7,018.3	(3.0%)
Smokeless tobacco	$7,246.3	8.9%	1,222.0	1.0%
Electronic cigarettes	$3,873.7	4.1%	298.3	14.5%
Cigars	$3,449.0	9.2%	2,238.4	4.7%
Pipe tobacco	$120.7	(2.1%)	14.9	(6.3%)
Cigarette tobacco	$32.3	(9.6%)	5.0	(13.5%)
Tobacco combination packs	$13.5	37.4%	0.9	32.1%
Tobacco alternatives-nonvapor	$11.1	(4.3%)	2.1	(1.8%)
Shag	$7.7	10.1%	0.4	12.1%

Source: NielsenIQ

Channel Comparison: Cigarettes

C-stores lost 5% in unit sales of cigarettes in 2020, but other channels lost more. Drug stores were down the most in unit sales with a 19.8% decrease compared to the year prior.

CHANNEL	DOLLAR SALES ($ MILLIONS)	PCYA*	UNIT SALES (MILLIONS)	PCYA*
C-store	**$56,107.7**	**1.1%**	**7,284.0**	**(5.0%)**
Multioutlet**	$10,075.8	(14.7%)	999.5	(13.2%)
Food	$3,706.1	0.1%	423.5	(8.2%)
Drug	$1,620	(12.7%)	190.6	(19.8%)

Source: IRI

Distributor Data: Total Nicotine Share

Wholesale shipments to retail for the 52 weeks ending in quarter three 2020

Tracking shipment levels to stores in all channels, Management Science Associates (MSA) reported that cigarettes gave up less than 1% of its share to other nicotine category subsegments for the 52 weeks ending in the third quarter of 2020 compared to the same time the year prior. Moist smokeless, modern oral nicotine and large cigars are the only subsegments that increased their volume shares, but by small amounts, at 0.2%, 0.5% and 0.3%, respectively.

SEGMENT	FIRST HALF OF 2020 SHARE	VOLUME PCYA*
Cigarettes	79.0%	(0.1%)
Moist smokeless	7.3%	0.2%
Vapor	5.3%	(0.7%)
Paper, tubes, wraps	3.4%	(0.1%)
Large cigars	2.9%	0.3%
Little filtered cigars	1.1%	(0.1%)
Modern oral	0.7%	0.5%
Snus	0.3%	(0.0%)
Pipe tobacco	<0.1%	(0.0%)
Roll-your-own	<0.1%	(0.0%)

Source: MSA

Distributor Data: Cigarette Volume Changes

MSA shipment data shows superpremium, premium and deep-discount cigarette volumes all increased for the 13 weeks of the third quarter of 2020 compared to the same time a year ago. Overall, cigarette volume was up 1.7%, MSA said.

While deep discount saw the largest volume growth, superpremium also grew significantly at 6%.

SEGMENT	VOLUME PCYA*
Superpremium	6.0%
Premium	1.8%
Discount	(5.4%)
Deep discount	10.6%
Total	**1.7%**

Source: MSA

* Percent change from a year ago | ** Includes grocery, drug, mass market, military commissaries and select club and dollar retail chains

Distributor Data: Top Cigarette UPCs

Calendar year 2020

Premium

Newport Menthol Box 100 edged its way into second place among the top premium cigarette UPCs shipped by McLane in 2020. Marlboro brands dominated the list with six of the top 10 spots.

1. Marlboro Gold Box King
2. Newport Menthol Box 100
3. Newport Menthol Box King
4. Marlboro Gold Box 100
5. Marlboro Box 100
6. Marlboro Special Blend Gold Box King
7. Marlboro Silver Box King
8. Marlboro Special Blend Gold Box 100
9. Camel Blue Box King
10. Camel Crush Box King

Discount

Pall Mall led McLane's shipments of discount cigarettes in 2020, with its Red Box 100 and Blue Box 100 UPCs taking the top two spots.

1. Pall Mall Red Box 100
2. Pall Mall Blue Box 100
3. L&M Menthol Box 100
4. L&M Box 100
5. Pall Mall Menthol Box 100
6. L&M Box King
7. Pall Mall Blue Box King
8. Pall Mall Red Box King
9. L&M Menthol Box King
10. L&M Blue Box King

Deep Discount

Eagle 20 Menthol Gold Box 100 and Pyramid Box Menthol Silver 100 were the top two deep-discount cigarette UPCs shipped by McLane in 2020.

1. Eagle 20 Menthol Gold Box 100
2. Pyramid Box Menthol Silver 100
3. LD Red Box 100
4. Pyramid Menthol Gold Box 100
5. Eagle 20 Menthol Gold Box King
6. LD Menthol Box 100
7. Decade Menthol Box 100
8. Eagle 20 Menthol Silver Box King
9. LD Red Box King
10. LD Blue Box 100

Source: McLane Co.

Distributor Data: Cigarettes

Fourth-quarter 2020

Sales per store per week of cigarettes as measured by licensing dollars from McLane grew 4% in fourth-quarter 2020, with private-label brands seeing the greatest percentage increase at 9.3%.

SEGMENT	APSW** (IN DOLLARS)	APSW** (DOLLAR GROWTH)	PCYA*
Premium	$5,957.8	$280.94	4.9%
Generic	$884.42	($13.79)	(1.5%)
Subgeneric	$205.92	$12.83	6.6%
Private label	$60.43	($6.21)	9.3%
Total	**$7,108.58**	**$273.76**	**4.0%**

Source: McLane Co.

14.5%

Unit increase in electronic smoking devices in c-stores in 2020, according to IRI

* Percent change from a year ago | ** Average sales per store per week

Distributor Data: E-Cigarettes

Fourth-quarter 2020 sales

McLane distribution data shows a steep decline in most e-cigarette products in 2020 as the category faced challenges from the U.S. Food and Drug Administration's regulation of local and state flavor bans. E-cigarette cartomizers were up in dollars, though, showing 94.2% growth.

SEGMENT	APSW** (DOLLARS)	APSW** (DOLLAR GROWTH)	PCYA*
Vapor e-liquid	$322.96	($73.59)	(18.6%)
E-cigarette cartomizer	$152.16	$73.82	94.2%
Vapor kits	$32.16	($46.87)	(59.3%)
E-cigarette disposables	$18.60	($2.35)	(11.2%)
E-cigarette starter kits	$3.97	($6.94)	(63.6%)

Source: McLane Co.

96.8%

Growth of wholesale shipments of disposable e-cigarettes to c-store retailers for the third quarter of 2020, per MSA

Channel Comparison: E-Cigarette Volume Change

Wholesale shipments to retail through third-quarter 2020

Vape cartridge sales took a dive in 2020 after the FDA's ban on flavored cartridges—excluding tobacco and menthol flavors—took effect in February. Flavored disposable e-cigarettes, however, were able to remain on the market, which likely accounts for their spike in shipment volume. Disposable shipments to c-stores were up more than 96% in the third quarter of 2020, according to MSA.

SEGMENT	ALL OUTLETS	CONVENIENCE/GAS	TOBACCO OUTLETS	DRUGSTORES	DOLLAR STORES
Cartridges	(15.2%)	**(9.8%)**	(17.8%)	(99.2%)	(93.8%)
Disposables	45.0%	**96.8%**	235.0%	(100.0%)	(100.0%)
Starter kits	(91.9%)	**(91.1%)**	(92.2%)	(100.0%)	(98.5%)
E-liquid	(52.1%)	**(65.1%)**	(51.1%)	(86.3%)	(126.8%)

Source: MSA

Distributor Data: Top Vapor, Disposables

Calendar year 2020

E-Cigarette Starter Kits

Vuse and Logic UPCs were the top two vapor starter kits shipped by McLane in 2020, but Blu UPCs accounted for half of the top 10 list.

ITEM	PCYA*
1. Vuse Alto	N/A
2. Logic Power Rechargeable Kit - Tobacco	(40.2%)
3. Logic Power Rechargeable Kit - Menthol	(90.3%)
4. Blu Plus Express Kit - Tobacco	(86.8%)
5. IQOS 2.4 White	N/A
6. IQOS 2.4 Slate	N/A
7. Blu Starter Pack Classic Tobacco	100%
8. Blu Starter Pack Magnificent Menthol	100%
9. Blu Variety Starter Pack	100%
10. Blu Starter Kit Black	100%

Vapor E-Liquids

Among vapor e-liquids, Juul dominated the list of the top 10 UPCs shipped by McLane in 2020.

ITEM	PCYA*
1. Juul Classic Menthol Pod 0.7-mL, 4-pack	283.5%
2. Juul Virginia Tobacco Pod 0.7-mL, 4-pack	48.87%
3. NJOY Ace Menthol Pod 5%	277.2%
4. Juul Menthol Pod 5% 1.4-mL, 2-pack	144.0%
5. NJOY Ace Tobacco Pod 5%	230.4%
6. Juul Virginia Tobacco Pod 3%, 4-pack	32%
7. Juul Menthol Pod 3% 2.8-mL, 4-pack	***
8. Juul Virginia Tobacco Pod 1.4-mL, 2-Pack	44.3%
9. My Blu Gold Leaf Pod 2.4%	87.1%
10. Juul Virginia Tobacco Pod 3% 1.4-mL, 2-pack	27.4%

E-Cigarette Disposables

Among disposable e-cigarettes, the NJOY and Blu brands led in McLane's shipments to c-stores in 2020.

ITEM	PCYA*
1. NJOY Daily Rich Tobacco	(4.3%)
2. NJOY Daily Rich Tobacco 4.5%	11.5%
3. NJOY Daily Menthol 4.5%	21.4%
4. Blu Tobacco	(22.8%)
5. NJOY Daily Menthol	(30.0%)
6. Blu Cherry Crush	(31.5%)
7. Blu Mint	(29.5%)
8. Blu Menthol	(17.5%)
9. myblu Intense Tobacco Chill 4%	37.1%
10. Blu Vanilla	(44.6%)

Source: McLane Co.

* Percent change from a year ago | ** Average sales per store per week | *** Growth higher than 500%

Where the Gains Are

Sales in c-stores and travel stores in the fourth quarter of 2020 nearly all saw positive growth. Little cigars singles, however, declined 21.6% in dollars.

Distributor Data: Cigar Shipments

Fourth-quarter 2020

SEGMENT	APSW** (DOLLARS SOLD)	APSW** (DOLLAR GROWTH)	PCYA*
Cigar pouches	$159.77	$11.58	7.8%
Cigars, singles	$83.37	$4.37	5.5%
Cigars, packs	$91.90	$15.23	19.9%
Cigars, little packs	$17.45	$0.31	1.8%
Cigar wraps	$4.15	$0.15	3.7%
Little cigars, singles	$0.2	($0.06)	(21.6%)

Source: McLane Co.

Channel Comparison: Cigars

52 weeks ending Dec. 27, 2020

In 2020, c-stores were the only channel that saw growth for both unit and dollar sales of cigars, according to IRI data. Food stores grew cigar dollar sales 1.3% but dropped 1.4% in unit sales.

CHANNEL	DOLLAR SALES ($ MILLIONS)	PCYA*	UNIT SALES (MILLIONS)	PCYA*
C-stores	$3,846.4	10.1%	2,432.8	5.4%
Multioutlet***	$373.9	(7.4%)	174.1	(2.3%)
Food	$103.1	1.3%	55.0	(1.4%)
Drug	$51.6	(4.8%)	16.0	(5.4%)

Source: IRI

10.1%

Growth of cigar dollar sales in c-stores in 2020, according to IRI

Where the Gains Are

C-store sales, 52 weeks ending Dec. 27, 2020

Sales of smokeless tobacco in c-stores rose 7.7% in 2020, according to IRI, with unit sales flat.

When comparing retail channels, drugstores saw the biggest growth in smokeless dollar and unit sales, up 93.9% and 114.5%, respectively, according to IRI.

SMOKELESS TYPE	C-STORE SALES ($ MILLIONS)	PCYA*	UNIT SALES (MILLIONS)	PCYA*
Chewing tobacco/snuff	$7,121.3	2.5%	1,188.8	(6.5%)
Spitless tobacco	$1,009.3	66.9%	195.1	67.8%
Total smokeless tobacco	**$8,130.6**	**7.7%**	**1,383.8**	**(0.2%)**

Channel Comparison: Smokeless Tobacco

CHANNEL	DOLLAR SALES ($ MILLIONS)	PCYA*	UNIT SALES (MILLIONS)	PCYA*
C-stores	$8,130.6	7.7%	1,383.8	(0.2%)
Multioutlet***	$570.7	(14.3%)	74.0	(10%)
Food	$272.1	(0.2%)	43.6	(4.7%)
Drug	$22.3	93.9%	4.3	114.5%

Source: IRI

Distributor Data: Smokeless Tobacco Shipments

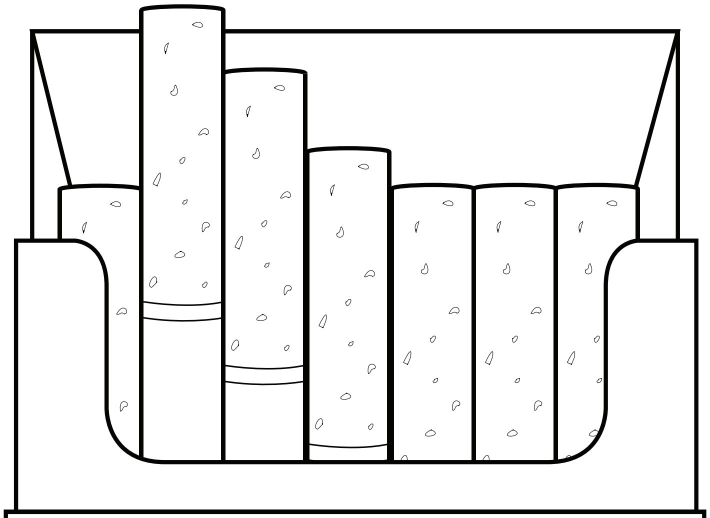
Fourth-quarter 2020

Dollars per store per week of smokeless tobacco from McLane to c-stores were up more than 13% in fourth-quarter 2020, according to McLane shipment figures. Smokeless alternative saw triple-digit growth, up 172.2%.

SEGMENT	APSW** (DOLLARS)	APSW** (DOLLAR GROWTH)	PCYA*
Smokeless tobacco	$600.34	$25.15	4.4%
Smokeless alternative	$102.09	$64.59	172.2%
Snus/sticks/strips/orbs	$35.30	($0.78)	(2.2%)
Total smokeless tobacco	**$737.73**	**$88.96**	**13.7%**
Cigarette tobacco	$3.29	($0.04)	1.2%
Pipe tobacco	$1.12	($0.12)	(10.0%)
Total cigarette/pipe tobacco	**$4.41**	**($0.09)**	**(1.9%)**
Cigarette papers	$9.96	$1.75	21.3%
Cigarette tubes	$0.56	($0.10)	(14.9%)
Total cigarette papers/tubes	**$10.52**	**$1.65**	**18.6%**
Chewing tobacco	$11.75	($0.89)	(7.1%)

Source: McLane Co.

* Percent change from a year ago | ** Average sales per store per week | *** Includes grocery, drugstores, mass market, military commissaries, and select club and dollar retail chains



Fresh Insights From Behind the Counter

Category experts look toward the future, considering unknowns such as PMTAs, COVID-19, taxes and more

BY HANNAH PROKOP

The tobacco and nicotine category faces many unknowns going into 2021. From the effects of the pandemic to regulation of flavored products and the results of the premarket tobacco product application (PMTA) process, manufacturers and retailers are braced for a tenuous year.

However, there are some upsides.

- The smokeless tobacco category, led by spitless tobacco, was up 1.7% in unit sales in c-stores for the 52 weeks ending on Nov. 1, data from Chicago-based market research firm IRI shows.
- Cigars showed a 7.7% increase.
- Electronic smoking devices increased 10.8%.
- Cigarettes, while down 4.2% in unit sales, were up in dollar sales compared to the previous year (1.8%), and decreased less than analysts previously projected, due, in part, to increased consumption amid the pandemic.

For Senior Category Manager Peter Frattarola of La Plata, Md.-based Wills Group Inc.'s Dash In convenience stores, the health of the category is good, and likely will be next year, too. Frattarola says almost all tobacco subcategories are reflecting growth in Dash In's more than 50 stores.

"The demand for tobacco- and nicotine-derived products appears strong, and perhaps resilient, when you look at the seemingly difficult current retail environment for c-stores," Frattarola says.

Here's a look at factors weighing on the category and how key segments might react.

Watching PMTAs

One thing that will remain on retailers' minds in 2021 is what products the U.S. Food and Drug Administration (FDA) will authorize through its PMTA process and when the agency will let retailers know which tobacco products have already submitted applications.

Frattarola says he made sure to speak to his manufacturers about which items they would be submitting for the PMTA process and made changes to Dash In's plan-o-grams based on those conversations.

"Overall, changes were few and far between as we pride ourselves in utilizing data to carry the highest ranked products based on sales and unit movement," he says.

As of press time in late November, with the PMTA deadline months passed, the FDA was still sifting through the applications and working on a public list of which companies have submitted applications.

The FDA's Center for Tobacco Products Director Mitch Zeller told *CSP* in November that the FDA remains committed to releasing a public list of the new tobacco products deemed to be subject to an FDA review, were on the market as of Aug. 8, 2016, and for which a premarket application was submitted by Sept. 9. The list will help convenience-store retailers know which tobacco products to keep on their shelves.

First, though, the FDA must sort through thousands of applications that came in all different forms, including CDs, DVDs, hard drives and some hard copies, Zeller says. And within those applications, some companies are seeking authorization of thousands of products. The FDA will also need to ensure the publishing of any information complies with federal disclosure laws and regulations.

The result is an "extremely labor-intensive manual exercise of unpacking every single application," Zeller says. "But we have lots of people working on this, and we absolutely intend to provide such a list."

There are several ways the agency is prioritizing which applications to process first, Zeller says.

"One of our goals is to transform the marketplace for these unauthorized products into a regulated marketplace," Zeller says. "And the principle that we came up with is to devote a certain percentage of the reviewing resources to those products that have, or are having, the greatest impact on public health, either positive or negative, simply by virtue of share of market."

The other aspect Zeller says the FDA is considering is fairness, giving priority to companies that submitted applications on time, regardless of that company's size or market share. The FDA is also prioritizing e-cigarettes and electronic nicotine delivery systems (ENDS).

Examining E-Cigarettes

At least one analyst says she's "cautiously optimistic" about how e-cigarettes will fare in the future.

However, she acknowledges several burdens on the segment, including the FDA's flavored cartridge ban, state-level tobacco sales bans in places like California and Massachusetts, the THC vaping crisis and a long and expensive PMTA process, all of which stunted the category's growth.

"Certainly, I was a lot more bullish a couple of years ago when regulation was more limited," Bonnie Herzog told retailers in September during a webinar for the National Association of Tobacco Outlets (NATO), Minneapolis.

"Being highly diversified with our tobacco/nicotine offerings will help offset risk/disruption and put us in a position to grow the business."

E-cigarettes, or e-vapor, is about 5% of the total nicotine market, based on 52-week retail dollar sales through Sept. 5, said Herzog, managing director for New York-based Goldman Sachs. While substantial, Herzog notes that just a couple of years ago she expected that number to be double the share it is now.

Nielsen's numbers support this. For the 52-week period ending on Oct. 26, 2019, c-store sales of e-cigarettes saw a 95.3% increase in dollar sales compared to the previous year. For the 52 weeks ending on Oct. 24, 2020, that percentage change was 4.7%.

The curtailed growth will continue, at least in the near-term, Herzog said. One of the consequences of the FDA's flavor regulation was consumers turning back to combustible cigarettes, she said.

"I'm not convinced that that's what the FDA had in mind, but that is reality. And that's also what's helping the broader cigarette category," Herzog said. "We're going to have to wait to see how this plays out as the FDA works through [the PMTAs], which, by the way, is going to take a very long time."

Zeller, however, says a straight line cannot be drawn between the final January guidance to ban flavored pods and increased cigarette use. The guidance was a policy based on the best available data, including the 2019 National Youth Tobacco Survey, he says, which made it clear that certain flavored cartridge-based products were really popular with underaged consumers who were vaping. Tobacco and menthol flavors were excluded from the guidance.

Zeller says the policy was a balancing act between disturbingly high levels of youth using e-cigarettes and technology that could benefit addicted adult cigarette smokers.

"And so with that guidance, when it went into effect, we not only preserved tobacco and menthol flavoring for cartridge-based products, but it didn't affect the availability of flavors in any other form, starting with disposable products," Zeller says.

A Future for Flavors?

How quickly flavored e-cigarettes are allowed back on the market will have a huge impact on the category, though, says Jeff Brown, vice president of sales with Jacksonville, Fla.-based E-Alternative Solutions, a sister company to Swisher, which manufactures products under the Forth CBD, Leap Vapor and Cue Vapor System brands.

"In my view, I think that will have the biggest impact. That's kind of what everyone's waiting for, in particular, the companies that spent all that money and time, like us, to put PMTAs together [and] to meet the requirements. That day is coming," Brown says.

Regardless, there is still much for retailers to be excited about in tobacco, says Frank Vignone, vice president of sales with Louisville, Ky.-based Turning Point Brands Inc., a marketer, manufacturer and distributor of branded products including rolling papers, smokeless and vapor products and more.

"The big challenge for both the stores and manufacturers is how do we make room for all the innovation that is coming while satisfying existing product demands," he says. "Everyone has to get smarter, realigning inventory and making room in the stores. At the same time, manufacturers have to careful about making unrealistic demands on stores to not over-inventory stores with unproven products."

Until PMTAs are authorized by the FDA, it remains to be seen what e-cigarette flavors and brands will be allowed back on shelves. In the meantime, many retailers are focusing their energy on other emerging categories, such as modern oral nicotine (MON) products.

The Others

The other tobacco products (OTP) category, which includes modern oral nicotine, will be a driver of key growth into the fourth quarter of 2020 and beyond, Herzog said, citing a third-quarter of 2020 retailer survey by Goldman Sachs that showed retailers are optimistic about the product segment.

Richmond, Va.-based Swedish Match's nicotine pouch brand Zyn continues to outpace all other brands, growing 34% in the third quarter of 2020, Herzog said. It is followed by Richmond, Va.-based Altria's On, Jacksonville, Fla.-based Swisher's Rogue, Velo and Dryft.

British American Tobacco plc announced in November its U.S. division of the BAT Group acquired the nicotine pouch product assets of Dryft Sciences LLC, a Moorpark, Calif.-based modern oral nicotine product company. BAT will rebrand Dryft's U.S. portfolio under its global modern oral brand, Velo.

Long-term growth in the category is very exciting, says Matt Domingo, senior director of external relations with Winston-Salem, N.C.-based Reynolds America, which is a subsidiary of British American Tobacco. Nicotine pouches are the highpoint right now, he says, and with BAT's recent acquisition of Dryft, the consolidation continues.

"Now that we are seeing this consolidation occur, you'll see the remaining players start striving for category ownership, and you'll see that in terms of what things look like at retail relative to space, pricing and brand program agreements," Domingo says.

Best practices in managing a MON set is a matter of grouping those products together, according to Joe Teller, director of category management with Swedish Match. If retailers have too many supplier programs, MON products could be scattered.

"The good ones are figuring out how to separate e-cig/vape from modern oral so they have discreet sections where shoppers can see the breadth of variety that's available," Teller says.

Frattarola says Dash In stores started carrying Zyn and Velo in August 2019. He added Dryft in the last few months of 2020 and is working to add On, as well, to diversify Dash In's tobacco and nicotine offerings.

"Being highly diversified with our tobacco/nicotine offerings will help offset risk/disruption and put us in a position to grow the business," Frattarola says.

Key Tobacco/Nicotine Category Sales Data

PRODUCT	DOLLAR SALES (IN MILLIONS)	PCYA*
Cigarette tobacco	$32.9	(10.3%)
Cigarettes	$52,599.5	2.7%
Cigars	$3,398.7	8.0%
Pipe tobacco	$118.3	(1.0%)
Shag	$7.7	6.3%
Smokeless tobacco	$7,146.0	8.8%
Total tobacco	$63,316	3.6%
Tobacco alternatives non vapor	$11.7	6.7%
Electronic cigarettes	$3,778.8	4.7%
Total tobacco alternatives	$3,791.3	4.8%

Source: Nielsen U.S. convenience-store data for the 52-week period ending Oct. 24 | *Percent change from a year ago

The COVID Effect

The lingering effects of the coronavirus crisis will affect tobacco into 2021, especially when it comes to consumption levels and taxes.

Total tobacco/nicotine actually performed well in 2020. C-store dollar sales were up 3.6% for the 52-week period ending on Oct. 24, about a point better than 2019 growth, according to Nielsen, Chicago.

Downtrading, or consumers switching to cheaper brands, remains the biggest potential risk for the category, according to Herzog, as unemployment remains high and government stimulus wanes.

The coronavirus pandemic has disproportionately affected lower-income consumers, Nik Modi, tobacco analyst for New York-based RBC Capital Markets, says.

"Those are the core tobacco consumers," he says. "In the absence of stimulus, are we in the situation where those consumers are really under a lot of pressure?"

Cigars have had a good bump due to people being at home so much and dealing with a lot of stress, Teller says. But cigars have faced out-of-stock problems as COVID-induced demand has risen and as manufacturing workplace rules changed to allow for more worker safety.

"If we all could've made enough [cigars], who knows how high the category sales could be," Teller says.

Consumer packaged good (CPG) manufacturers and c-store retailers were seeing pantry loading again as the virus spiked in November, Herzog says, but there are some signs of consumers pulling back in the tobacco/nicotine category.

Potential excise tax increases at the state and federal level are concerns among retailers and tobacco suppliers. Colorado and Oregon voters in November approved measures to increase taxes on tobacco products.

How other local governments hurting from the pandemic react remains to be seen.

"Will they look for the tobacco industry to help fill the coffers again?" Modi asks. "Conversely, could decriminalization of cannabis or states opening up recreational [cannabis] in certain areas and jurisdictions help the tax? Does that fill the gap? That, I think, is going to be an important question. What is the source of those taxes to help states fill their coffers?"

While tobacco sales were strong over the third quarter of 2020, retailers who responded to Goldman Sachs' Nicotine Nuggets survey noted that sales weren't as robust as they had been at the onset of COVID-19, Goldman Sachs Managing Director Bonnie Herzog wrote in an analysis of the survey. As stay-at-home mandates ease and people head back to work or school, pantry-loading spikes leveled off to some extent, likely due to a decrease in usage occasions, Herzog said.

Increased flavor bans at local and state levels, along with more downtrading to discount and deep discount brands as unemployment remains high and government assistance tapers off, also put pressure on tobacco sales. CSP

82%

Percentage of convenience retailers who said tobacco consumption is the same, if not stronger, today vs. a year ago as the COVID-19 pandemic continues to support sales across all tobacco categories

Source: Goldman Sachs

THE FUTURE OF BEHIND THE COUNTER

Tobacco and nicotine segment trends and highlights to watch

BY MELISSA VONDER HAAR
PHOTOGRAPHS BY JASON LITTLE

Typically, when talking about behind-the-counter segment performance, the headline is about how a smaller, newer segment grew ... and how much the key segment of cigarettes declined. But 2020 was not a typical year: Virtually every segment, including cigarettes, saw dollar sales increase. According to Nielsen data ending Dec. 26, total tobacco dollar sales in the convenience channel were up 4.2% compared to 2019. How?

"People were consuming more nicotine overall," says Don Burke, senior vice president of Management Science Associates (MSA), Pittsburgh. "In 2020, total U.S. nicotine consumption in the U.S. was up 3.2%. So clearly the pandemic had an impact on the overall total nicotine delivery category."

So what happens to those consumption patterns after the pandemic?

4.2%

Total growth in dollar sales for the tobacco category in c-stores in 2020, according to Nielsen

"The pandemic has upended consumer purchasing behaviors, some more temporary than others," says Renee Duszynski, vice president of sales for Teaneck, NJ-based JTI USA. "The most interesting part will be to understand how routines have drastically changed during the pandemic, what will hold and how retailers prepare for the future."

According to some, the best opportunity for the future lies in a bevvy of new, noncombustible alternative products.

"Thirty-three percent of tobacco consumers age 21 to 29 are exclusive noncombustible product users, the highest percentage of exclusive use across age cohorts," says George Parman, director of communications for Altria Group Distributing Co., Richmond, Va.

Products like modern oral nicotine/nicotine pouches and other discreet, noncombustible options managed to grow in a year when consumers faced fewer limits on when they could smoke. That bodes well for the future of behind the counter.

"I do think the overall trend to modern oral products—and some other alternatives within the nicotine delivery category—will somewhat abate the decline in nicotine consumption in the U.S. and will, longer-term, benefit the category," Burke says.

Here's a look at what's going on in all the major behind-the-counter segments.

“Now’s the time for spring cleaning the fixture,” she says, “moving out SKUs that won’t move for ones that will.”

Looking to 2021

Because 2020 was a relatively positive year for cigarettes as a whole, many retailers are dubious for 2021, comparatively.

“We saw a very positive year for cigarettes, which we expect will continue at least a little bit into 2021, until we get out of this greater pandemic situation,” Burke says.

Respondents to the Q4 2020 Goldman Sachs tobacco retailer survey largely anticipated that, as the country returns to a new normal post-pandemic, so will cigarette declines. Bonnie Herzog, managing director at Goldman Sachs, outlined factors called out by the survey respondents:

- Tough comps in 2021 vs. 2020’s strong performance.
- “Back-to-normal” behavior meaning fewer smoking opportunities vs. working from home.
- Shifting to alternative nicotine options: Respondents predicted 20% of the cigarette declines will be due to consumers moving to alternatives like modern oral products.

“(Some respondents) expect cigarette volume levels to return closer to historical decline rates as vaccinations allow people to return to work while the category also deals with potential unfavorable regulatory measures, including local flavor bans, higher taxes and minimum price requirements, which could pressure volumes further,” Herzog wrote in a research note.

But all is not lost for the category that continues to be the greatest contributor to in-store sales (more than 30%, per NACS State of the Industry data): Some retailers believe that pandemic purchase behaviors may be more permanent.

“Roughly 20% of (tobacco retailers surveyed) expect cigarette volumes to continue to grow in 2021,” Herzog said. “Many expect consumption habits developed over the pandemic to prove sticky, even as people return to an office setting.”

Time will tell.

CIGARETTES

Strength at the Top and Bottom

Overall, 2020 was an impressive year for the all-important cigarette segment: Nielsen data shows c-store dollar sales were up 3.3% vs. 2019, while units were down 3%. MSA data, which tracks shipments to retail, shows units declining in the first half of the year but up in the second half.

“This is a really good performance because cigarettes typically decline 3%-5% range each year,” Burke says.

Not surprisingly, the premium cigarette subsegment—which accounts for the vast majority of cigarette sales—drove much of the market, up 1.8% annually as of Q3 2020. But it was actually super-premium cigarettes (up 5%) and deep discount cigarettes (up 10.6%) that saw the largest jump.

“It would appear some consumers dropped down from the discount category to the deep discount category,” Burke says, as the discount subsegment dropped 5.4%.

A February Goldman Sachs tobacco retailer survey showed 75% of respondents were seeing this kind of downtrading toward the end of 2020, crediting economic stress for the shift.

Mark Schueller, director of marketing for Raleigh, N.C.-based U.S. Tobacco Cooperative, says the downtrading phenomenon is not unique to the pandemic, but has been happening for years. He specifically cites premium and midtier cigarette price increases that happen multiple times a year and increasing options in deep discount.

“Retailers sometimes think one size fits all,” he says. “However, a thorough evaluation of their present cigarette programs may provide some startling revelations in regards to meeting their customer needs and wants in addition to their company’s goals.”

Duszynski acknowledges that the “premium tier still commands a large segment of the category” but encourages retailers to capitalize on growing interest in super-value brands by giving the segment secured space on the backbar and supporting it with signage.

SMOKE SIGNALS

Cigarettes Get a Chance to Recover

BY STEVE HOLTZ

The coronavirus pandemic has forced many changes to market dynamics and consumer trends in every aspect of convenience retailing and beyond, and the tobacco category is certainly no exception.

In this case, unemployment is an overriding concern as it forced smokers to trade down to discount brands as the stress of the situation has many people smoking more, according to Nik Modi, managing director and analyst for RBC Capital Markets LLC, New York.

"Unemployment and the implications on trade down, we're already seeing it," said Modi during a recent *CSP* Tobacco Update webinar. "We see a pretty consistent increase" in the sale of discount cigarettes.

Specifically, Modi said discount cigarettes' share of the market grew by 10 points in March and another 31 points in April.

"This is something that I think is going to be a big topic of focus for a lot of the big cigarette players," he said. "We already know Altria is vigilant to this and trying to be proactive with price gaps. We think Marlboro Special Blend will play a significant role here to help them combat from the trade-down pressure. This is happening right now because we don't have a lot of stimulus money that is being circulated into the economy to the smokers that need it."

On the plus side for retailers, “You are seeing an improvement in household penetration for cigarettes,” Modi added.

Data from Numerator, a market intelligence firm based in Chicago, shows that over the past 12 months, the number of new cigarette buyers increased by 21.5%, but in the latest two months, that number has increased by 2 percentage points to 23.5%.

“This could be because people are migrating away from electronic cigarettes,” Modi said.

Numerator data also shows that despite trading down, smokers are spending more money per visit during the COVID-19-driven economic downturn. Spending on cigarettes rose more than $5 to $21.81 per trip in April from $16.29 a year earlier. Modi expects that to continue.

“That is being primarily driven by the fact that you’re seeing fewer purchase trips but more cartons vs. single packs over the coming months, because gas prices are going to be low and stimulus money will begin hitting the consumer,” he said. “Per capita consumption tends to go up when there’s more inventory in the home. So my suspicion is that we could have a positive undertone for the cigarette category over the coming months.”

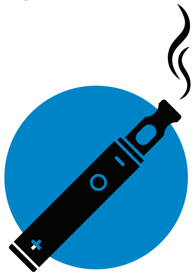
That positive effect is already playing out. RBC data shows cigarette sales volumes, while still on the decline, hit their lowest decline point in the first quarter of this year since 2017.

“The category has been improving,” Modi said. “We view this as confirmation that outsized volume declines over the past few years were driven by non-sustainable e-cigarette growth, minimum age regulations, excise taxes and pricing.”

With those elements quieted for the time being, cigarettes are finding a opportunity to at least level off, he said.

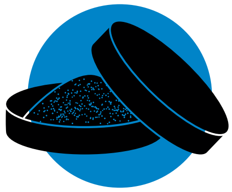
Beyond Cigarettes

In a presentation during a CSP Tobacco Update webinar, RBC Capital’s Nik Modi predicted cigarette volume will decline by 5% in 2020, and Joe Teller, director of category management for Swedish Match North America, Richmond, Va., predicted sales volumes of other tobacco products (OTP) will grow 5.6% over the coming 52 weeks. Here’s a look at expectations for four specific nicotine and tobacco segments.



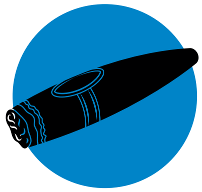
VAPING

“E-cigarette volume will remain under pressure,” Modi said, noting e-cigarette sales peaked in 2018. He cites the change of the federal legal age to buy such products from 18 to 21, momentum to ban flavored pods and continued pressure on Juul as headwinds for the segment.



MST

“For moist smokeless tobacco (MST), the trends are suddenly getting worse,” said Teller, adding that after years of resilience, MST is finally giving up share to vape products and nicotine pouches. “I’m hoping MST volume is flat for the next year.”



CIGARS

After growing “gangbusters” for years, the cigar segment took a hit over the past 24 months or so, Teller said. “It was homogenized tobacco leaf (HTL) products that took the hit,” he said, leaving rolled-leaf and natural-leaf cigars to make up the difference. “Retail is still too heavy with HTL regular items,” he said, leaving him to predict an “upside to only 1.2% volume growth” in 2020.

NICOTINE POUCHES

This young segment has grown by more than 500% over the past year or so, but off a very small base and with presence in only about half of the c-stores in the United States, according to Teller. As retailers begin to wrap their arms around the products, he loosely predicts 165% growth over the next 52 weeks. This is “still growing too fast to get a good next-year projection,” Teller said. “Dedicated nicotine pouch sections will help.”

2.2
Average number of cigarette units purchased per store visit in April 2020, up from 1.8 units a year earlier

3.7
Average monthly cigarette purchase frequency in April 2020, down from 4.7 visits a year earlier

$21.81
Average cigarette spend per trip in April 2020, compared to $16.29 per visit a year earlier

–5%
Expected cigarette volume decline for full year 2020

Sources: Numerator, RBC Capital Markets

E-CIGARETTES

Adapting and Rebounding

Unlike cigarettes, electronic cigarettes had a rough go in 2020.

"For the first time since 2015, we saw a decline in the overall vapor category," says Burke. "The category was down approximately 4% in 2020."

The declines came from factors almost entirely independent of the pandemic: namely, the focus on youth vaping and THC-vaping lung disease in late 2019 and the FDA action in early 2020 that banned all flavored cartridge products.

"We saw cartridges decline by 12% in 2020," Burke says. "That was for many years the strongest growth subcagtegory within vapor."

"A lot of flavored pod products took the brunt of that beating, and the availability of those products evaporated in most cases," says Matt Domingo, senior director of external relations at Reynolds American Inc., Winston-Salem, N.C. "Consumers had to make decisions: either go to vapor products that were still available or revert back to something they were using before."

As it turns out, many *did* choose to go to vapor products that were still available: namely disposable e-cigarettes, which were not subject to the FDA's flavor ban. MSA data shows disposables grew by 70% across all channels in 2020 and enjoyed over 100% growth within convenience.

Much of that growth came from new players within vapor.

"To take advantage of the flavor ban for the pod-type systems, we did see that many new manufacturers did enter the disposable market with flavored products," Burke says. "In terms of major players, we did not see many that reentered."

Data Reality

Though 100%-plus growth is impressive, disposables still account for only 14% of the vapor category, according to Nielsen data. And the boom may be plateauing, especially as the FDA begins cracking down on the disposable market. Last July, the agency issued 10 warning letters instructing manufacturers like Puff Bar to remove flavored disposable products from the market because they did not have proper premarket approval.

"While the refill market recovers, the much smaller e-cig disposable market has begun to contract as the FDA go after non-compliant market participants," Herzog wrote in a February research note, adding that disposable sales were down 2.9% for the two weeks ending Feb. 20, 2021. During that same time period, the overall e-cig category grew by 19%, which Herzog credits to refillable products—approximately 82% of category sales.

Tobacco retail survey data by Goldman Sachs suggests that retailers are largely positive that the category will continue to recover—albeit perhaps not to the double-digit growth it has typically enjoyed. Herzog noted that respondents expect e-cig volumes to grow by 5.9% in 2021 (vs. just 2.7% growth predicted in the October 2020 survey).

"One respondent noted that e-cigs were their strongest category in 2020, both in terms of dollar sales and volume," Herzog said. "That said, while most respondents expect e-cig momentum to continue, some noted that they have reduced shelf space on e-cigs to improve merchandising of oral nicotine products, which continue to demonstrate significant growth."

Heat-Not-Burn

Falling somewhere in between the cigarette and e-cigarette category is the new heat-not-burn segment, which to date in the U.S. consists of New York-based Philip Morris International's IQOS portfolio (which is distributed by Altria Group distribution Co.). The IQOS system heats the proprietary Marlboro HeatSticks instead of burning them like traditional cigarettes. Unlike electronic cigarettes, the HeatSticks use compressed tobacco, and not a nicotine solution.

While Philip Morris first launched IQOS in select Asian markets more than five years ago, the technology only first showed up in the U.S. after the FDA granted market authorization in April 2019, with the first IQOS store opening in Atlanta that October. Since then, Altria Group has expanded into Richmond, Va., and Charlotte, N.C., though the rollout has admittedly been hampered by the pandemic. IQOS stores in Atlanta and Richmond temporarily closed last March, and the Charlotte launch was delayed because of stay-at-home orders.

During a September presentation for the National Association of Tobacco Outlets, Herzog said the pandemic and the fact that the FDA had not yet approved the latest IQOS 3 products had likely slowed down the progress of heat-not-burn growth.

"It has been more of a slow rollout and that has a lot to do with the fact that the technology that has been approved in the U.S. is older technology of IQOS," she said. For context, Nielsen showed HeatStick unit sales in the Atlanta, Richmond and Charlotte markets were down 0.4% in the two weeks ending Feb. 20, 2021, flat over the previous four weeks, and up 2.2% over the previous 12.

But there are lots of reasons for optimism around IQOS, including:

- As of July 2020, the FDA granted permission to market IQOS as a modified risk tobacco product.
- As of December 2020, the FDA approved IQOS 3, which offers technological improvements, including longer battery life, to the original.
- Altria and its subsidiary Philip Morris USA is expanding IQOS availability greatly in 2021: IQOS and HeatSticks will be sold statewide in Georgia, Virginia, North Carolina and South Carolina by April and expand into the next metro market (Northern Virginia) in Q2 with plans for an additional three metro markets in the second half of the year.

100%+

Growth of disposable vape pens in c-stores in 2020, according to MSA

"PM USA is maximizing its first-mover advantage with IQOS, responsibly expanding its availability and the availability of Marlboro HeatSticks to densely populated metro areas, and then expanding outwards as the user base grows," says Altria's Parman.

However, perhaps more than accessibility, it's the ability to market IQOS as a lower-risk alternative to cigarettes that will be key to the success of this new category.

"Based on our research, approximately 40% of smokers would be interested in switching to a product based on an FDA-authorized reduced-exposure claim," Parman says. "We believe smokers' understanding of the harm-reduction benefits of noncombustible products relative to cigarettes will be an important factor in their decision to switch."

Retailers have been a little more muted. As of September, 17% expected to have IQOS in their stores by the end of the year, 17% expected to have it by Q1 2021 and more than half didn't know when they'd be offering IQOS or HeatSticks.

Herzog is still optimistic, predicting that by 2025, IQOS will account for as much as 12.2% of Altria's volumes. "It's probably still a little too early, but I expect to hear more behind IQOS as we move out of this pandemic," Herzog said.

THE STATE OF VAPING

Vapor Sales an Open Question After 'One-Two Punch' of Regulation

BY HANNAH PROKOP

What the state of vaping will be in the next year is the million-dollar question—and one convenience-store retailers may not have the answer to soon.

There are ways tobacco category managers can prepare, though, for vaping's future, even without knowing yet what flavors and products will be legal.

Experts in the field who spoke to *CSP* say that while the category may never go back to the skyrocketing growth it once saw—before the THC vape crisis of 2019, Tobacco 21, the premarket tobacco product application (PMTA) process and the U.S. Food and Drug Administration's (FDA's) flavor ban—vape products are still a valuable segment.

"It is going to be a growth category in the tobacco industry, but not nearly as strongly as it has in the past," Don Burke, senior vice president of Pittsburgh-based Management Science Associates (MSA), says. "But

still a growth category, so still a category that retailers need to pay attention to."

Chris Dillard, tobacco category manager at Spinx c-stores in South Carolina, says Tobacco 21 and the FDA's flavor ban had a huge effect on his e-cigarette set.

On Dec. 20, 2019, then-President Donald Trump signed legislation to amend the Federal Food, Drug and Cosmetic Act, raising the federal minimum age for the purchase of tobacco products, including vape, from 18 to 21 years.

Then in January 2020, the FDA announced that it would be barring the sale of most flavored vape products, with the exception of tobacco and menthol, from unauthorized cartridge-based e-cigarettes. Companies that want to legally sell flavored cartridge-based e-cigarettes had to submit a PMTA for the product by Sept. 9, 2020, to be considered by the FDA.

As of press time, the FDA had yet to approve any flavored vapor products through the PMTA process.

Because vaping attracted a younger adult tobacco consumer, the age change and the FDA's flavor ban was a "one-two punch" to the segment, Dillard says.

And with flavored cartridges out, disposable e-cigarettes started to grow, Burke says.

"While disposables prior to the flavor ban had been declining, since the flavor ban, they have been growing because if a vaping consumer has wanted a flavor the only way they could get it would be to go to disposables, in the conventional classes of trade," Burke says.

Disposable shipments to c-stores were up more than 96% in the first three quarters of 2020, according to data from MSA tracking wholesale shipments to retail. Cartridge, starter kits and e-liquid shipments all declined in all outlets: c-stores, tobacco outlets, drugstores and dollar stores. Only disposables showed growth, up 45% in all outlets, 97% in c-stores and 235% in tobacco outlets, MSA data shows.

While many c-store retailers have embraced disposable vapor products, Dillard, of Greenville, S.C.-based Spinx, is holding off on most SKUs for now. He carries blu's disposable products but is waiting for FDA authorization before considering more brands.

"I'm not adding any incremental items to my vapor set at this point. Not until we come out the other end of the PMTA and there's some kind of clear direction on what's going to make it, what's not going to make it," Dillard says.

Photograph courtesy of Spinx

The back bar at Spinx stores has adjustable shelves that allow for flexibility in the tobacco set.

The FDA's Center for Tobacco Products Director Mitch Zeller gave an update on the PMTA process in February. At that time, the FDA had only published a list of the exemption from substantial equivalence requests (EX REQ) and substantial equivalence (SE) reports that were submitted by the Sept. 9, 2020, deadline.

Most e-cigarette and vapor products, though, were submitted through the PMTA pathway, and the FDA says it will need more time to sort through those applications due to the volume. As of press time, the FDA said it had processed PMTAs for more than 4.8 million products from 230 companies.

The THC vaping crisis is another ongoing threat to the category, Burke says. On Sept. 6, 2019, the U.S. Centers for Disease Control and Prevention (CDC) held a press conference to discuss an outbreak of dozens of lung illnesses in 33 states, including at least three deaths, tied to the use of vaping devices [*CSP*—Feb. '20, p. 22]. The CDC later said the outbreak was likely tied to illicit sources of product made with tetrahydrocannabinol (THC), the psychoactive element in marijuana, and a compound called vitamin E acetate. By then, e-cigarette companies like Juul had already suspended the sale of their flavored vaping pods.

"We've got ways to be flexible in a very quick manner with the physical merchandising on our backbar."

"Retailers are seeing the impact from that continuing today," Burke says. "It typically takes that a year or two to sort of abate. That happened in fourth quarter 2019; [by the] fourth quarter 2020 I do think we started to see a little bit of improvement in the vaping category at that time, and it will continue to improve."

Changes to the Prevent All Cigarette Trafficking (PACT) Act could also affect retailer's vape sections moving forward, says Sharan Kalva, COO of C-Store Master, a Huntsville, Ala.-based distributor that works with nearly 3,000 c-stores.

As part of the COVID-19 relief bill signed into law on Dec. 27, Congress amended the PACT Act with the Preventing Online Sales of E-Cigarettes to Children Act. This modifies the definition of cigarettes in the PACT Act to include electronic nicotine delivery systems

(ENDS), or vape products.

The change requires online cigarette sellers to verify the age of customers for all purchases, an adult with an ID to be present for delivery, shipping package labels to show they contain tobacco and that they comply with all state and local tobacco tax requirements.

Kalva says retailers need to make sure their distributors have a plan to still provide c-stores with their vapor products, even with the PACT Act changes, which could affect vapor supply.

"The PACT Act impacts every single player in the market, every manufacturer, every distributor out there," he says. "There is a significant impact."

Despite the challenges vape products face, category managers are finding ways to have a profitable category.

Distributor Kalva says tobacco category managers need to take a close look at the e-cigarette brands they're working with and ask important questions.

"How far is the brand going toward meeting the commitments set forth by the FDA? Are they going above and beyond what the FDA is recommending? How proactive is the company in trying to mitigate any regulatory risk? Or how well are they compliant to the FDA rules?" Kalva says.

It's important to not carry too many vapor brands, he says. Pick a few and try to grow them. That reduces complexity and allows retailers to make sure they're compliant with the brands they carry.

Kalva also recommends c-stores carry disposable products because that's what's growing.

"We try smaller brands and see which are the up-and-coming brands. We, as a smaller, more agile company, can experiment with it. As long as they have the right credentials and legal and they're compliant, we will try them out," Kalva says.

Burke agrees, saying that retailers should have a reasonable level of disposable SKUs that appeal to vapor customers who are still seeking flavors. While cartridges aren't doing as well, c-stores still need to maintain their cartridge offer, too, since that is really the bulk of the vapor business.

For Dillard of Spinx, the key is being flexible. He invested heavily in his backbar shelving and fixtures so he could change things up if needed. For example, he has vape shelves that could be adjusted from 3 feet long to 1 foot, and vice versa.

"We've got ways to be flexible in a very quick manner with the physical merchandising on our backbar," Dillard says. "So that's something we have done to try and get ready for what may come out on the other side with vapor."

He's also investing in products outside of vape, like modern oral nicotine (MON), which includes nicotine pouch brands like Zyn, Velo, Rogue and On. Margins for the pouches are good, Dillard says, and he's seeing complementary usage in the category, so it's not hurting another segment.

"That's where I see a lot of my incremental growth coming from in 2021," Dillard says.

Dillard's e-cigarette category is still showing volume and share growth, but he says it has slowed down a bit in the first quarter of 2021. He thinks it will continue to grow, but at a slower pace.

One thing helping e-cigarettes is good promotions and brand extensions. Dillard points to R.J. Reynolds Vapor Vuse line. The company recently expanded its selection to include four-pod packs nationally in Vuse Alto Golden Tobacco 5% and Alto Menthol 5%.

"The quad pack is just dominating out of the gate for Alto," Dillard says.

He also says c-store promotions for vape tend to give discounts on the vapor devices, but he is investing specifically in vapor pods, placing promotions on those to grow sales.

Even with some success in the category, Dillard is playing it safe when it comes to vaping. He says he had to pay restocking fees when he had to pull flavored cartridges last year, and that's something he's not willing to risk losing money on again.

In what sounds like a wise strategy, he summarizes, "We're poised to take advantage of whatever comes out of the other side."

Views on Vaping

CSP asked tobacco/vape manufacturers: What do you think the state of vaping will be in the next 12 to 18 months and why?

"FDA market orders **may potentially impact flavored pod SKUs available** (i.e., reintroduce them to the market after final guidance forced market removal in February 2020). In the event FDA authorized the return of flavored pods, one can expect an uptick in retail vapor demand, particularly on closed-system products as flavors are clearly important to adult smokers."

—**Chris Howard**, vice president, general counsel and chief compliance officer, E-Alternative Solutions (EAS), Jacksonville, Fla.

"We think the **public health debate should strike a balance** between preventing youth access to vape and all tobacco products, with the needs of adult smokers seeking alternatives. If that happens, vaping can live up to its promise."

—**Niraj Patel**, president and CEO, Bidi Vapor LLC, Melbourne, Fla.

"As a result of recent developments, including the PACT Act and FDA's progress on PMTA submissions, **I generally expect a consolidation of nationally available vapor products**. This means that retail and trade partners will become more educated and confident in knowing what is and is not worth stocking."

—**Leila Medeiros**, senior vice president of new categories for Reynolds, Winston-Salem, N.C.

"**PACT Act enforcement will severely limit shipping vapor products directly to adult consumers**. You're going to see adult consumers who once exclusively bought their vapor products online come into your stores. Logic's own loyal adult consumers are going to need to find products at retail—and you'll have a new opportunity to increase market basket sales."

—**Renee Duszynski**, vice president of sales, Logic Technology Development LLC, Teaneck, N.J.

LARGE CIGAR CATEGORY

Q&A WITH KAREN SABER

SWISHER'S VP BUSINESS ANALYTICS & STRATEGIC SALES INNOVATION

Q: THE LARGE CIGAR CATEGORY HAS BEEN EXPERIENCING GAINS EVEN THROUGH THE PANDEMIC, DO YOU THINK THE CATEGORY WILL MAINTAIN THAT MOMENTUM OVER THE NEXT COUPLE OF YEARS?

A: COVID impacted an individual's ability to physically go to work, and thusly enabled adult consumers to enjoy combustible tobacco products at their leisure, in their own space, with fewer restrictions. As a result of this new work from home infrastructure that many organizations have put in place, **Large Cigars have been able to realize growth throughout 2020 and much of 2021**. As the industry sees all time volumetric highs, we expect to experience a slowdown in growth to approximately 2%-4% in the back half of 2021 for the Large Cigar category, with overall growth for the year of 6%-8% being realized. Additionally, we expect this level of respectable growth to continue into 2022, as adult consumers continue to embrace this long-standing segment.

Q: WHICH SEGMENTS ARE MAKING THE MOST IMPACT IN TERMS OF VOLUME AND GROWTH?

A: In terms of the Large Cigar category, there are several trends, which continue to evolve. **The adult Large Cigar consumer is quite savvy, and they know what they want.** There are so many options being offered today, but they continue to demand quality, variety and value. When the consumer is introduced to a premium quality cigar, they are willing to spend more for this luxury and are willing to trade up. For example, **the Natural Leaf (NL) Segment continues strong growth**, both in the Traditional and Rough-Cut formats. Swisher is proud to have several great brands with solid performance in these areas – Swisher Sweets Leaf (NL – Rough Cut); Optimo (NL – Traditional) and Goodies (NL – Traditional). We are also seeing **the mini segment rise in sales, distribution and awareness**. The smaller size gives the adult consumer another option for enjoying their tobacco. We want to continue engaging with the adult consumer and offering them opportunities to enjoy their cigar experience in a multitude of blends. **Swisher is the leader in this area with 80% share of the mini cigar segment.**

Q: HOW ARE PREMIUM CIGARS CONTRIBUTING TO THE CATEGORY'S OVERALL GROWTH?

A: Premium Cigars are an important component of a retailer's marketing mix. **It is critical to offer a multitude of price points to appeal to a variety of adult consumers and occasions.** There are those individuals who are looking for that indulgence/luxury, and they are willing to spend a bit more on their cigar experience. This is evident as the segment continues to grow +7% vs. YAG. In particular, Drew Estate adds revitalization to the category as it grew 40% vs. YAG and accounted for over 40% of the segment's growth for this same period.

Q: ARE THERE ANY TRENDS THAT YOU'RE SEEING IN THE CATEGORY THAT RETAILERS SHOULD BE AWARE OF?

A: Regardless of the category, adult consumers want to see tobacco segments evolve; variety, modernization and expansion are key. **One has to offer an optimized product mix allowing the adult consumer to choose from multiple categories, brands, blends and formats.** Additionally, today's adult consumer has evolved in the way they shop and digest information. You have seconds to interact with them at the counter and it is critical to communicate your messaging and value proposition in an effective and impactful manner. One should not underestimate the weight strong category management carries, as it relates to POS, planograming, partnering and pricing.

Data provided MSAi Database: 8/14/21

SWISHER SWEETS

ORIGINALS NEVER REST.

WHAT'S DRIVING CONTINUED GROWTH IN OTP?

LARGE CIGARS, MON AND BEYOND.

BIG PICTURE AND THE LINGERING EFFECTS OF COVID-19

Across OTP in 2020, **the COVID-19 pandemic caused adult consumers to change shopping and buying patterns**. This resulted in volume increases, which are holding steady or continuing growth trajectories in 2021. This is particularly true in the large cigar and modern oral nicotine (MON) categories.

LARGE CIGARS

The large cigar category experienced tremendous growth in 2020, as adult consumers reached for tried-and-true products and purchased more items in fewer trips. Despite more adult consumers returning to the office and their normal lives, post the height of the pandemic, the category is still performing exceptionally well. In the last 52 weeks ending 8/14/21, **the large cigar category increased over 9%**. A look at what is happening in various segments of the large cigar category provides deeper understanding and context for the growth and what's driving the most gains.

TOTAL LARGE CIGAR MANUFACTURER VOLUME PERFORMANCE

VOLUME IN MILLIONS – YTD THROUGH 8/14/21

Manufacturer	Volume
SWISHER	1,627.8
ITG	1,156.8
JMC	1,065.2
SMNA	1,107.3
GOOD TIMES	349.7
SHOW	142.3
ALL OTHER	151.9

LARGE CIGAR SALES INCREASE

C-STORE VOLUME IS UP **+9.4%** IN THE LAST 52 WEEKS

+142k C-STORES AVERAGING 725 SPSPW

As more of the country opens up and adult consumers are once again interacting, **C-Store volume continues to rise**, now averaging 725 sticks per store per week.

As the fastest-growing segment, **rough-cut natural leaf cigars are making significant contributions to category growth.**

ROUGH-CUT NATURAL LEAF

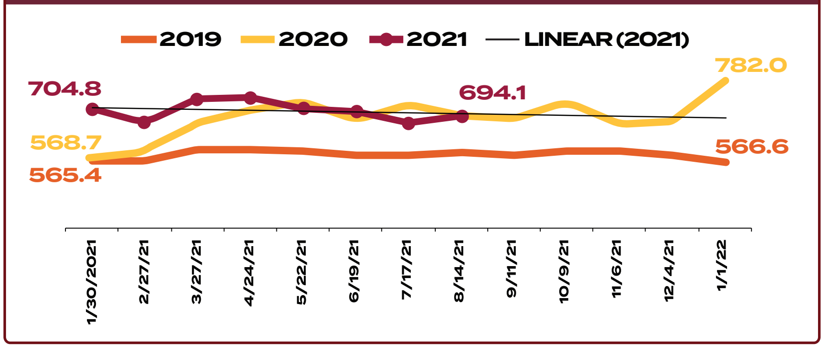
+39.9% VS YAG

NON-TIP HTL

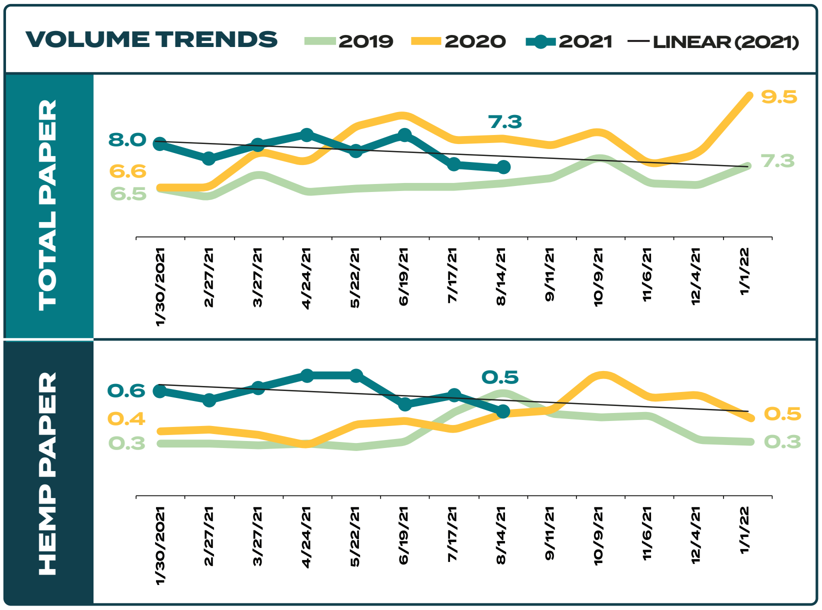
+5.3% VS YAG

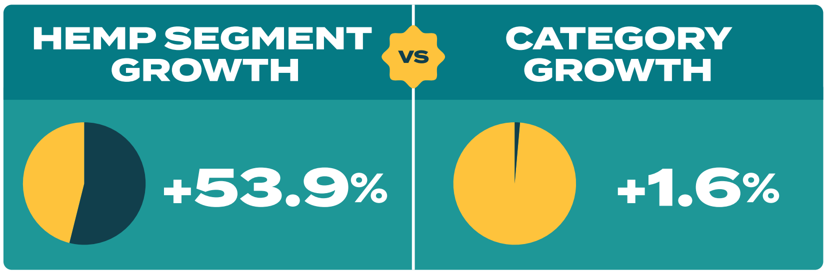
SWISHER

TOTAL LARGE CIGAR CATEGORY VOLUME TREND
4 WEEK INCREMENTS – VOLUME IN MILLIONS



HEMP PRODUCTS are experiencing strong demand from adult consumers as the pandemic has put more everyday focus on natural or plant-derived products. We are seeing this play out in both the rolling papers and wraps categories as **hemp products outperform category growth**.





(YTD AS OF 8/14/21)

PRE-PRICED VS. NON-PRICED PRODUCTS

For nearly 10 years margin and profit dollars in the cigar segment have been constrained. This begs the question of whether it is time to consider making the move to non-priced products to help lift margins. We caught up with Swisher's Senior Manager of Category Management, Victor Cavanaugh, to help answer the question.

With pre-priced products, it can be difficult for retailers to manage their margins since they can't adjust pricing in the face of tax or other local market implications. Another challenge is creating adult consumer excitement since **pre-priced products are seen as everyday pricing vs. value pricing in the minds of buyers.**

On the other hand, **non-priced products give retailers the power to find the "sweet spot" with their product pricing.** Realizing pricing is another component of category management, it can be strategically implemented to suit unique stores or geographies. These products also allow for **promotional activities that can generate excitement and capitalize on adult consumer demand for trusted brands** to help create higher profit margins.

Currently pre-priced large cigar items are expected and do not effectively drive adult consumer demand, so it may be time for a change in strategy. **Non-priced items give retailers another tool in the quest to optimize volume and profits for their business.**

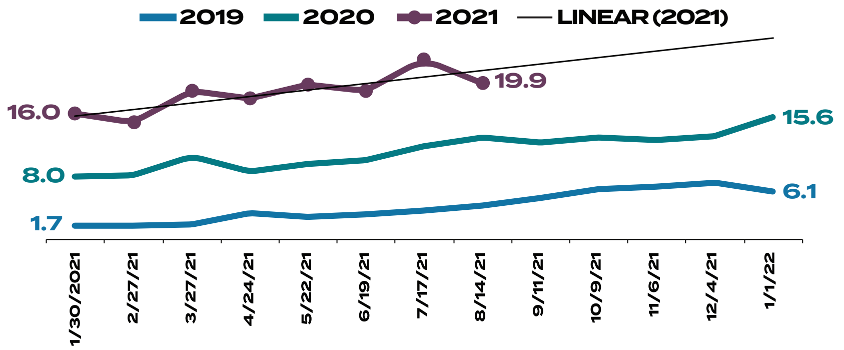
SWISHER

MODERN ORAL NICOTINE (MON)

As adult consumers increasingly discover modern oral nicotine products, the category has seen extraordinary growth which is expected to continue in 2022.

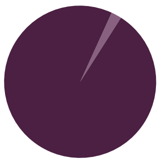
The MON category is up 88.5% vs. YAG and is expected to grow 64% to 245 million units in 2021, which represents approximately $1.1 billion in retail sales.

TOTAL MON CATEGORY UNITS TREND
4 WEEK INCREMENTS – UNITS IN MMS



Pouches are driving the MON category. Other formats are generally gaining volume and distribution but still only account for less than 3% of the volume.

FORMAT SHARE OF TOTAL MON



POUCHES 97.9%

	52-WEEK VOLUME	VOL. DIFF VS. YAG	% CHG
MON POUCH	209,551.9	99,944.1	91.2%
ROGUE	15,460.1	11,762.4	318.1%
ON!	32,100.2	22,131.1	222.0%
VELO/ DRYFT	22,456.6	11,219.4	84.8%
ZYN	139,407.7	56,567.0	68.3%

As the category and distribution grows, **adult consumers are discovering new brands** and contributing to growth across the pouch segment.

MOIST SMOKELESS TOBACCO (MST)

MST Volume has been impacted by the high demand of the MON category.

MST CATEGORY GROWTH

-18mm CANS VS YAG

Branded Value drives category gains as economic uncertainty drives adult consumers to seek value products.

BRANDED VALUE MST VOLUME IS UP

+5%

WHILE PREMIUM MST IS DOWN -2.7% VS YAG

MST TUBS' GROWTH FAR EXCEED THE CATEGORY

+12.3%

+9.4mm CANS

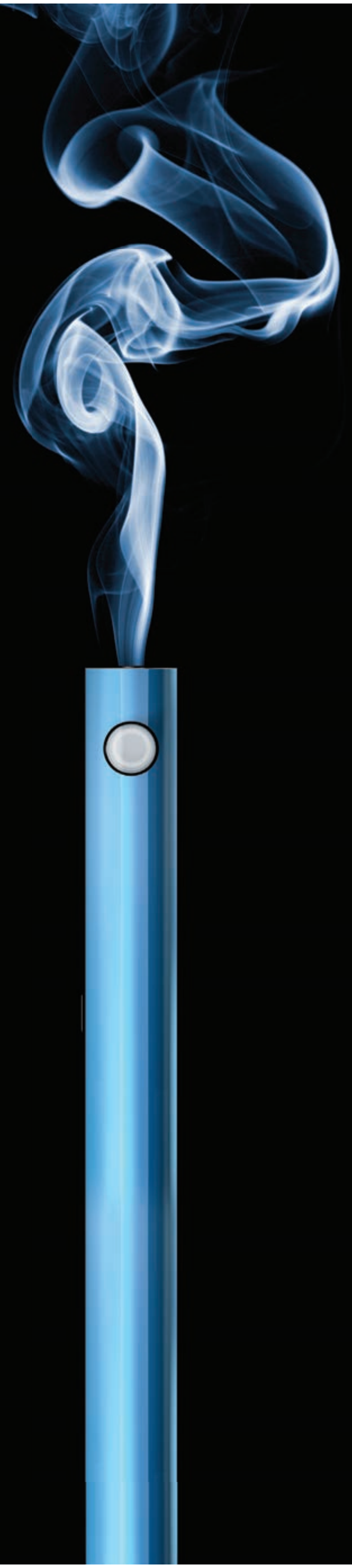
All data from MSAi Database as of 8/14/21 unless otherwise noted.

DISTRIBUTED BY SWISHER

PEN & VAPOR

Disposable E-Cigarettes: The Darlings of the Vaping Segment

BY HANNAH PROKOP



Customers gave little to no attention to the disposable e-cigarette category before a year ago, says Nik DiMambro, category manager for Nouria Energy Corp.

That's when the U.S. Food and Drug Administration's (FDA) guidance banning flavored vapor cartridges took effect. And while flavored disposables have been popular for years for some category managers in convenience stores, many attribute the subcategory's recent spike to the FDA's new rule enacted in February 2020.

"We have seen tremendous growth year over year," DiMambro told *CSP* in late December. "We're seeing upwards of 82% growth in disposables."

Nouria Energy only carried blu disposables, from Greensboro, N.C.-based ITG Brands, until the FDA changed its rules. Th
prompted the Worcester, Mass.-based cha
of about 120 stores to add Jacksonville, Fl
based E-Alternative Solutions' (EAS) Le
Go disposable e-cigarette.

Nouria Energy's spike in disposable sal
following the FDA's move mirrors the n
tional trend.

Disposable e-cigarettes took in mo
than $453.5 million in dollar sales and 44
million in unit sales in c-stores for the 5
week period ending on Nov. 21, according
Nielsen, Chicago.

Unit sales grew 211.8% during that pe
od, Nielsen said. That's compared to 12.3
growth in 2019 and 4.7% growth in 2018.

With the huge demand in the subcategory, c-store retailers must determine which products they're comfortable carrying, if any, and continue to navigate ongoing regulation.

Dinner Lady sells the Vape Pen Max and a tobacco-free nicotine vape pen in a variety of flavors.

In January 2020, the FDA announced flavored cartridge-based e-cigarettes—excluding tobacco and menthol—must be pulled from shelves. Those products can come back on the market only if the FDA authorizes them through the premarket tobacco application (PMTA) process.

The FDA's guidance resulted in a slew of new disposable e-cigarette companies hitting the market and taking advantage of what some call a loophole to fill the gap in flavored vaping products.

"Those products for the most part didn't exist at retail in any consistent manner a year ago," says Kraig Knudsen, tobacco category manager at Circle K's Heartland Division, Lisle, Ill. "All those companies said, 'Here's a loophole. I'm going to just create a disposable, have any kind of flavor I want and sell a boatload of them.' It's worked for them."

The FDA noticed. Beginning in July, it started cracking down on e-cigarette companies that sell fruity, disposable products that the agency says appeal to youths.

Results from the 2020 National Youth Tobacco Survey, released in September, said that while fewer U.S. youth are using e-cigarettes compared to 2019, there was an "alarming uptick" in the use of disposable e-cigarettes by youth.

Another safeguard to keep flavored disposables out of the hands of youth is through the Preventing Online Sales of E-Cigarettes to Children Act, which Congress passed in December and will take effect in early 2021. The bill requires that online e-cigarette retailers verify the age of customers for all purchases, require an adult with ID to be present for delivery, label shipping packages to show they contain tobacco products and comply with all state and local tobacco tax requirements.

"We feel brick-and-mortar is the best place for restricted items, not online," says, Mark Hopkins, owner and president of Little Rock, Ark.-based Max Distributing, which has submitted a PMTA for its MNGO disposable vape sticks. "We think [the new law] will only help the safety of the product and keep it out of the wrong people's hands."

Chris Howard, vice president, general counsel and chief compliance officer at EAS, says he thinks the FDA will continue to act against bad players and provide a pathway to enable flavored products back on the market, but it will take time.

"If that drags on much longer, it's a problematic situation because of course there's confusion at retail and, more significantly, the companies that are following the rules are really suffering as a result," Howard says.

Knudsen of Circle K agrees that there are some very good products in the disposable e-cigarette space, but lesser quality products are giving legitimate companies a black eye. He also worries about those products that the FDA does not approve, leaving the retailer stuck with the cost of its products.

Knudsen carries NJOY Daily from Scottsdale, Ariz.-based NJOY and blu disposables in the Heartland Division's stores. He would like to expand his disposable set—if the FDA authorizes a product.

DiMambro of Nouria Energy doesn't believe the FDA will crack down on disposables until the PMTA process is completed.

"Right now, the concern for the category is the PMTA process," DiMambro says. "If the FDA starts approving non-disposable items that have flavors, the whole disposable scene could change."

As such, manufacturers that have filed PMTAs want to assure retailers they can be confident in selling their products.

"I foresee demand for disposable and cartridge-based vape products growing tremendously," says Andrew Laron, vice president of sales with Ziip Lab, San Francisco-based maker of ZSticks. "More and more individuals will replace traditional cigarettes with vape products."

John Taylor, chief marketing officer with manufacturer Dinner Lady, says part of what's driving the trend in disposables is that the devices require no expert education for either retailers are consumers.

Dinner Lady, based in Blackburn, U.K., sells the Vape Pen Max and a Tobacco Free Nicotine Vape Pen in the U.S.

CIGARS

Go Big Or ...

In many ways, the cigar category was not hugely affected by the pandemic, at least when it comes to what's selling and what's not.

"In the overall cigar category, there's a real dichotomy: Cigarillos, what we call large cigars, continued very strong growth in 2020 and were up about 13%; little filtered cigars declined by almost 10%," says Burke. "Those trends are very similar to what we've been seeing over the past several years."

In the convenience channel specifically, large cigars were up 16% last year, reaching an all-time high of 9 billion units, according to MSA data.

"Cigarillos are a bright spot for this category," Burke says. "They have been for several years." Which isn't to say cigarillos weren't at *all* impacted by the pandemic. Many retailers reported production delays or access problems with cigarillos specifically last year.

"There were production issues in 2020 for several of the cigarillo manufacturers, but despite that, the growth continued," says Burke.

As those issues resolved, large cigars/cigarillos grew further. MSA data shows large-cigar units within convenience were up more than 25% year over year as of Feb. 27, 2021.

"It is widely understood that these growth trends will normalize at some point in time as purchase patterns more readily resemble prior years," says Saber of Swisher. "However, volume levels are still expected to increase in the near future."

Roll Away

As to which large cigars are selling, Teller of Swedish Match called out rolled-leaf cigars as a hot spot. Nielsen shows rolled-leaf volumes are up 43% over the past six months. Teller says this is good news for the c-store industry, as the most popular rolled-leaf products come in five-packs, a higher-priced and more profitable option than traditional, prepriced homogenized tobacco leaf (HTL) cigarillos.

"This is a yearslong consumer shift away from HTL cigars that is only picking up more steam," he says. "The category has been dominated by prepriced products for years, so it is great for the trade to see huge growth coming from rolled-leaf products."

Saber agrees that moving away from prepriced products will be an important shift for the future of the industry, especially as costs continue to rise for both retailers and suppliers.

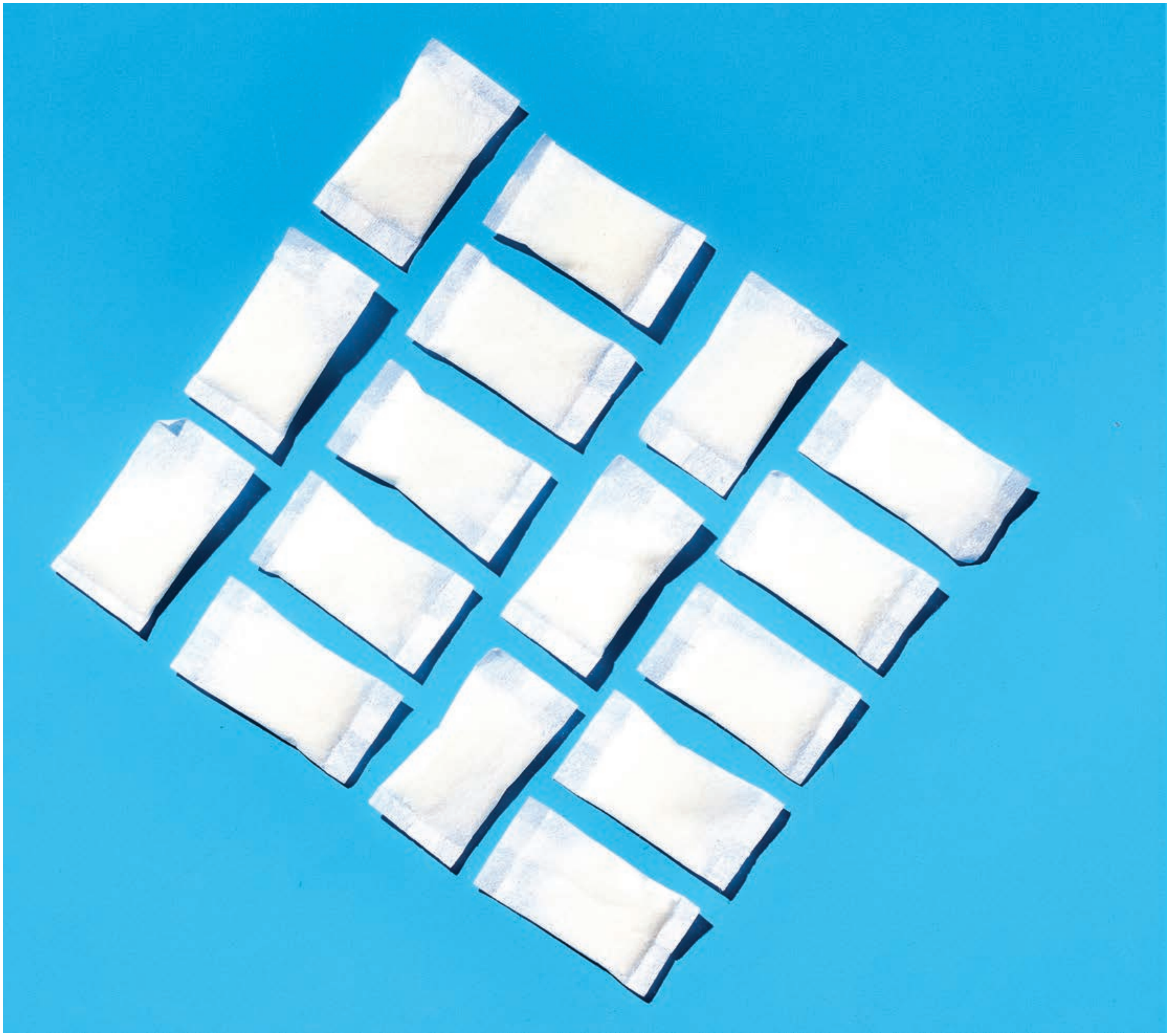
"Prepriced within the large-cigar category has been a challenge for retailers and manufacturers alike for over a decade," she says. "It is estimated in the near future, more and more organizations will need to move away from the prepriced model and migrate toward a nonpriced model."

Volume sales jump of cigars, mid-March through May 2020

20%

Volume sales of large cigars jumped a remarkable 20% in convenience stores during the COVID-19 period from mid-March through May, according to data from Swisher International, Jacksonville, Fla. The increase, which Swisher says is the result of adult consumers returning to tried and true products, provided a reversal of fortune for non-tip homogenized tobacco leaf (HTL) cigars, which were down 1.6% before the pandemic and grew a healthy 12.5% year over year through the pandemic period.

Source: MSAi database via Swisher International



SMOKELESS

Strong and Modern

Before getting into the smokeless category overall, it's important to address the increasing gray area about one of the most exciting product categories within Behind the Counter. While everyone can agree that modern oral products like ZYN, on! and Rogue are all the rage, there's little agreement on where these products belong. MSA, Goldman Sachs and Altria all categorize them as smokeless, or "overall oral," products. Others, including Nielsen, categorize them as "alternative tobacco," putting them in the same company as e-cigarettes. There's even some disagreement on *what* the segment is called, with Joe Teller of Swedish Match noting it really should be nicotine pouches, a segment that has been around for over four years and is not "so modern anymore."

For the sake of this report, modern oral nicotine products will be included with smokeless and largely referred to as modern oral nicotine, or MON for short.

Cross-Category Consumers

In looking at smokeless as a whole, which includes moist, snus and MON, MSA shows the category was up 6.5% in 2020, specifically:

- Moist products sales up approximately 1%.

- Snus down 2.5%.
- Modern oral up more than 162%.

Burke of MSA says it's important to remember that modern oral in total sales is roughly the same size as the snus segment, so much smaller than the moist segment. But still, the segment is "driving that 6.5% growth in overall oral nicotine category. It's the No. 1 growing category within tobacco/nicotine."

Nielsen data shows convenience modern oral unit sales grew by 90% in the six months ending Feb. 6, 2021, with dollar sales up more than 100%.

"The OTP category is still growing (unit volume was up 5% the last six months), with nicotine pouches accounting for 73% of that total category unit growth," says Teller, director of category management for Richmond, Va.-based Swedish Match, which manufacturers ZYN.

In terms of what's driving consumers to switch to modern oral products like ZYN, on!, Velo and Rogue, most agree that these products offer three key points of differentiation:

1. They're spitless and thus more discreet than moist smokeless.
2. They're noncombustible and so more discreet and a perceived health advantage to cigarettes.
3. They come in flavors, unlike many e-cigarettes, cigarettes or other smokeless options.

"As adult consumers look for nicotine products that fit their unique needs, it's no surprise that MON products are in the spotlight," says Karen Saber, vice president of business analytics and strategic sales innovation at Swisher International, Jacksonville, Fla. Swisher manufacturers Rogue MON. "The unique proposition is that these products come in a variety of formats, shapes, sizes and strengths so the adult consumer can choose the product that best meets their busy lifestyle."

But where is that growth coming from? Other smokeless products are probably the answer.

"The watchout would be the traditional smokeless category: One's much cleaner and ultimately more discreet," says Domingo of Reynolds, maker of Velo. "We've seen a lot of interaction and movement between those two categories."

"Products should be grouped together so that consumers can see the full breadth of flavors and nicotine strengths available."

[redacted]

Parman of on! maker Altria adds that of the approximately 1 million nicotine-pouch consumers, most are coming from dippers and smokers. That means the growth in MON isn't coming *just* at the expense of other smokeless products.

"Female smokers have been more engaged with oral nicotine pouches than with moist smokeless," Parman says. "(Women) make up approximately 25% of oral nicotine pouch consumers as opposed to 5% (for moist)."

"Another thing to keep in mind in modern oral is that it offers flavors," Burke says. "So some of the vape consumers that were strong flavor consumers have moved to modern oral because they could still get a flavor they may have particularly liked."

Smokeless Strategies

With modern oral drawing consumers from virtually all parts of the back bar, many industry watchers believe merchandising is key to driving awareness of the new space.

"It's very helpful to merchandise all nicotine pouch products together in a dedicated section, instead of the brands being scattered throughout the tobacco backbar," says Teller. "Since the category is still new, the products should be grouped together so that consumers can see the full breadth of flavors and nicotine strengths available."

162%

Growth in sales of modern oral nicotine products in 2020, according to MSA

The category merchandising could become all the more important as modern oral expands beyond nicotine pouches. "Although currently the majority of products reside in pouch format, tablets, gums and lozenges are gaining notable traction," says Saber.

A growing modern segment doesn't mean retailers should sleep on other smokeless products. Nielsen data shows traditional smokeless tobacco products netted approximately $7.36 billion sales in convenience during the 52 weeks ending Feb. 27, 2021. That's nearly twice the sales of all the tobacco alternatives Nielsen tracks, which includes modern oral and e-cigarettes.

Burke says that while moist smokeless had enjoyed a 3%-10% growth rate between 2006 and 2016, the category was mostly flat from 2017 to 2019.

"As more noncombustible products came on the marketplace and gave more options to the moist consumer, we did see that category begin to decelerate, though it remains a very strong category," Burke says.

Then came COVID-19.

"In 2020, we saw a 1% increase in the category," Burke says. "Probably due to the pandemic situation and consumers being able to use the product more often at home."

As for what happens post-pandemic, Burke predicts moist smokeless will remain strong, but flat as in years past. He adds, however, that the industry is only just scratching the surface with nicotine pouches and other innovation. It's important to remember that modern oral's triple-digit growth numbers came during a year when some of the segment's key attributes—discreet and smoke-free—were less important because consumers were largely working from home.

"As consumers adjust to a noncombustible method for nicotine consumption, it's highly likely that the modern oral category will continue to grow more," Burke says.

COUNTER PROGRAMMING

Nicotine Pouches: Tobacco's Fast-Growing Subcategory

BY HANNAH PROKOP

Chalk it up to low barrier of entry, the discreet nature of product use or even bad PR some other nicotine products have received. Any way you look at it, nicotine pouches appear to be the next "hot spot" for the tobacco category.

While the subcategory is still very small in volume, "It's a bright side. It's the hot spot," says Kraig Knudsen, tobacco category manager at Circle K's Heartland Division, Lisle, Ill.

"It's growing so fast and it's selling so well that it has had a large impact on moist snuff, which has been declining for several months," says Joe Teller, director of category management with Swedish Match, maker of Zyn Nicotine Pouches.

The numbers tell the story: Total other tobacco product (OTP) unit sales were up 7% in convenience stores for the 24 weeks ending on May 30, while moist snuff declined 5.9%. Winning segments during this time period predominantly were e-cigarettes, up 26%, and nicotine pouches, which grew a staggering 498%, according to Nielsen.

Similarly, nicotine pouch dollar sales in convenience stores were up 470% in 2020, according to Nielsen data for the six months ending in July. And while the nicotine pouch sales are really taking off, it should be noted that most products only entered the market in the last couple of years, Teller says.

Richmond, Va.-based Swedish Match's Zyn was the first nicotine pouch brand sold in the United States and is the best-selling today, accounting for 76% of total nicotine pouch can volume, according to the company. Swedish Match rolled out the product after an initial test in Denver and West Coast markets starting in 2016.

While modern oral nicotine (MON) may be taking share from moist smokeless tobacco sales, it has a diverse adult customer base in c-stores, Karen Saber, vice president of business analytics with Swisher International, says. About 91% of sales are made at c-stores.

"There's an opportunity [for retailers] to showcase something that is familiar yet novel at the same time. Lozenges, gums, tablets and pouches are all familiar products, but the idea that these formats deliver various levels of tobacco-free nicotine are a great alternative for the next adult customer approaching the counter," Saber says. "Rogue can be either a complement or a substitute to a traditional tobacco sale."

Nicotine pouches account for the majority of total MON category volume and have driven growth in the category, but opportunities also exist within emerging subsegments of gum, lozenges and tablets, Saber says. Swisher's Rogue brand has all four types.

Rogue's nicotine pouches last for up to an hour, the gum 30 minutes, lozenges about 10 minutes and tablets two to three minutes, Saber says. The products are considered ideal for travel or professional situations where long-lasting and quick-use options are preferred, Saber says.

When looking at the total market, the average weekly volume of MON sold has gone from 99,000 units in January 2018 to more than 2.5 million as of mid-July, according to data provided by Swisher.

Knudsen of Circle K says many retailers may only carry two or three brands of Nicotine Pouches but he carries four—for now. He says Zyn is No. 1 because it was first to market, but he'd like to give all products a chance to see what ultimately becomes the top brand.

"As these newer modern oral nicotine products have come on and become more common, the consumer's going to decide which one deserves the No. 1 share position. I don't want to make that decision prematurely and lock out consumer preference," Knudsen says.

Nicotine pouches are usually merchandised in a retailer's backbar, if there's room, or on counter displays, Knudsen says. He has a

Smokeless Tobacco Sales

For the 52-week period ending June 27, nicotine pouches showed the most growth in dollar sales of the smokeless tobacco category, according to Nielsen convenience-store data.

PRODUCT	DOLLAR SALES (MILLIONS)	PCYA*
Cut	$4,251.6	4.3%
Dry Snuff	$8.4	12.3%
Loose Leaf	$34.1	3.0%
Moist Snuff	$52.0	(7.7%)
Pouch	$1,774.9	24.9%
Remaining Smokeless Tobacco	$811.1	(4.5%)
Total smokeless tobacco	**$6,936.2**	**7.6%**

Source: Nielsen c-store data for the 52 weeks ending on June 27

*Percent change from a year ago

Top brands and their sales during the four weeks ending on July 11, according to Swisher, include:

Zyn	8.3 million units
On from Richmond, Va.-based Altria Group	1.4 million units
Rogue from Jacksonville, Fla.-based Swisher International	615,000 units
Velo from Winston-Salem, N.C.-based R.J. Reynolds Vapor Co.	607,000 units
Dryft from Moorpark, Calif.-based Kretek International	175,000 units

TOP BRANDS

Zyn


On

Rogue

Velo

Dryft

SKU selection of each brand but can't fit them all, as some, such as On, have more than 25 styles of nicotine levels and flavors.

How well the nicotine pouches do also depends on geography, Knudsen says.

"In the state of Pennsylvania, a store might only average 10 cans a week for the entire subcategory. In Illinois, we're looking more at 20 to 25 cans a week," Knudsen says. "But when you get into markets like Colorado and Montana, it is a totally different scenario. Colorado has stores that are doing 300 to 400 cans a week of these products. They're selling as much of this as they are standard smokeless tobacco."

With a full set of nicotine pouch brands available, the segment now lands in watch-and-see territory as some products succeed, others fall victim to poor sales and opportunity for new entries is limited.

As part of the highly regulated tobacco category, manufacturers have limited opportunity to introduce new products.

Specifically, any tobacco or nicotine product put on the market or modified after Feb. 15, 2007, must be reviewed by the FDA to determine whether it can stay on stores shelves. The deadline for manufacturers to submit subsequent equivalence (SE) and premarket tobacco applications (PMTAs) now stands as Sept. 9, but has changed several times, most recently due to the COVID-19 pandemic.

> **"There's an opportunity [for retailers] to showcase something that is familiar yet novel at the same time."**

For example, the FDA has already accepted and filed substantive PMTAs for 35 On products, according to Altria. Altria submitted more than 66,000 pages of documentation, including six primary studies, to the FDA, the company says.

"We believe the scientific evidence in these applications demonstrates that the marketing of On is appropriate for the protection of public health," says Paige Magness, senior vice president of regulatory affairs for Altria Client Services. "On Nicotine Pouches are a key part of our vision to responsibly lead the transition of adult smokers to a non-combustible future."

It's now up to the FDA to undertake a scientific review of the applications for Altria's products and many others. In the meantime, the products can remain on the market.

What Are Nicotine Pouches?

Swedish Match brought the nicotine pouch segment to the United States in 2015. Like snus, the products first gained popularity in Europe, according to retailer Kraig Knudsen of Circle K. Typically sold in tin or plastic containers of 15 pouches, nicotine pouches do not contain tobacco, but rather nicotine salt combined with food-grade ingredients, a significant differentiator from moist-snuff pouches. In the industry, they are often referred to as part of the modern oral nicotine category, or MON. Nicotine pouches are non-spit products, Knudsen says, which adds to their draw and is the reason they're likely taking away sales from the moist-snuff category.

Tobacco Sales Amid the Pandemic

While Modern Oral Nicotine (MON) products are a fast-growing new product, the total tobacco category has done well amid the COVID-19 pandemic—and some retailers, like Murphy USA, saw the strongest sales in cigarettes.

An informal survey of CSP readers done in late March showed tobacco and packaged beverages were two categories in which respondents saw the most increases in dollar sales in the early days of the coronavirus crisis. And by June, total nicotine volume sales for the two weeks ending June 13 increased 1.4%, indicating consumption continues to pick up, according to a report from Bonnie Herzog, managing director for Goldman Sachs, New York.

More immediately, tobacco nicotine volume decreased by 1.7% for the two weeks ending on July 11, Herzog said, suggesting some pressure followed a price increase that went into effective in late June.

Retailer Murphy USA reported strong cigarette gains for the first half of 2020.

Tobacco contribution increased 19.2% at Murphy USA on a same-store basis due to higher unit volumes, generating higher sales and margin during the period, President and CEO Andrew Clyde said on the El Dorado, Ark.-based company's second-quarter 2020 earnings call.

"Our multipack and carton cigarette offers have become a destination trip for consumers, and second-quarter results compare strongly against the already impressive high-single-digit contribution gains we put up last year," Clyde said, noting Murphy USA's tobacco business did not correlate with fuel traffic, which has been down throughout the pandemic.

Aside from cigarettes, vapor and alternative nicotine products are also delivering a substantial margin uplift, Clyde said. Second-quarter total merchandise contribution margin was up about $13 million compared to the prior year. Of that increase, $11 million came from tobacco. Of that $11 million from tobacco, about $8.3 million came from cigarettes and about $2.3 million came from other tobacco products (OTP).

Nicotine Pouches represent 5% of Murphy's OTP category, Clyde said.

RESET ROULETTE

Retailers Find Flexibility a Must for the Backbar

BY HANNAH PROKOP

Retailer Smoker Friendly typically resets its plan-o-gram for cigars in the first quarter of the year. But in a year shaken up by the coronavirus pandemic and related supply shortages, the Boulder, Colo.-based convenience- and tobacco-store chain has pushed its resets back for 2021, says Jeremy Weiner, category director for cigars and premium products.

"We've delayed doing any sort of plan-o-gram or store reset in that category until we're comfortable that product will be back in stock to be able to justify the time that it takes to do a new plan-o-gram," he says.

The COVID-19 pandemic, premarket tobacco product application (PMTA) process, emerging products and more forced tobacco retailers to be more flexible than ever with their backbars during the past year. Tobacco category managers, suppliers and shelving manufacturers told *CSP* how c-store retailers are navigating these challenges.

While a full reset of cigars is on hold at Smoker Friendly, Weiner has still made many changes to the backbar over the past year.

He works around distribution problems by keeping in close contact with manufacturers to see what will be available and double-facing some of the top-selling cigars so shelves look full—even when some flavors are out of stock.

Smoker Friendly also adjusted its vapor and nicotine pouch set over the past year, says Tim Greene, category director for general merchandise and tobacco.

In most of its 160 stores—which operate as tobacco stores, cigar lounges, liquor stores and gas stations under banners including Smoker Friendly, Tobacco Depot and Gasamat—there is a 4-foot vapor section on the backbar. That space was adjusted depending on what products submitted PMTAs to the U.S. Food and Drug Administration (FDA) by the Sept. 9 deadline, Greene says. Deemed tobacco products not submitted by that deadline are subject to FDA enforcement.

"We pulled quite a bit of product off the shelves," Greene says. "Obviously, before the deadline, we sold as much as we could at a discounted rate. And we pulled off what we knew wasn't submitted. There's still some brands out there we're not exactly sure what was submitted and what wasn't submitted, so even today we're still trying to get clarification on what was submitted."

Modern oral nicotine (MON) pouches—a current bright spot behind the counter—helped fill the space of pulled products, he says. Smoker Friendly carries Zyn, Rogue, On and Velo. Previously, MON was merchandised on countertop displays, but has since moved to a 3-foot area on the backbar.

Changing shelves has been easy, Greene says, because outside of some cigarette and moist tobacco fixtures, Smoker Friendly's backbar uses a slat wall, which allows for shelves to be moved in and out without having to nail anything to the wall.

"We [react] quickly to analyze new opportunities or environmental changes."

photograph courtesy of Harbor Convenience Retail

Harbor Convenience Retail's Infinity fixtures are designed to provide flexibility to backbars with adjustable shelves and out-of-stock technology.

Adjustable pushers were key to Kum & Go's expansion of MON, also called oral tobacco-derived nicotine (TDN), Senior Category Manager for Tobacco Travis Welsh says. When the FDA banned flavored cartridge sales in February 2020, the Des Moines, Iowa-based c-store also voluntarily removed flavored disposables from its set, leaving plenty of room for pouches.

Having adjustable pushers in their sets allowed Kum & Go to put different sized and shaped products in the same spot, making it easy to switch a rectangle flavored e-cigarette for a round nicotine pouch container, for example.

Kum & Go took a staged approach to filling those empty spaces. In addition to adding TDN, it added product assortments within the non-flavored tobacco space and brought in some limited time offers in other segments.

The buildout of Kum & Go's backbar sets allows for a lot of flexibility, Welsh says.

"The methodology at which we look at our business around performance of products and new and emerging segments has really built a strong foundation that we can leverage to quickly analyze a new opportunity or environmental change," Welsh says.

Backbars need to be kept simple to allow c-store staff to make those necessary changes, says DeAnn Campbell, head of research and insights at Grand Haven, Mich.-based Harbor Convenience Retail. C-store backbars are in a constant state of flux, she says, which is why Harbor's shelving systems allow for flexibility, such as pushers that accept virtually any packaged size.

These days, c-stores must shift quickly without going through a complete store reset, she says. And one way to do that is through flexible shelving.

Harbor Convenience Retail's Infinity fixture includes a variety of pusher options, finished end panels, storage doors and security doors. It's also easy for employees to move shelves up and down and change their width, Campbell says. Recently, Harbor also started incorporating technology into the shelving systems that allows retailers to see when stock gets low.

"It's important that you keep things simple so your staff can clearly and easily know what they have to do, because it's going to have to be done by staff," Campbell says. "It's also important to start adding in flexibility, different kinds of pushers, exploring the technology, so that you can make that a little more automated in the future because it is going to be changing very, very frequently."

Changes in tobacco over the past few years is what led ImageWorks Display to create its Impact system, which has been on the market since 2019, says Mike Purviance, vice president of sales.

The Winston-Salem, N.C.-based company's Impact product incorporates 1-foot shelving that can be vertically adjusted without the need to reconfigure the frame, Purviance says. A continuous frame also eliminates gaps found in other systems, which allows for a clean presentation in the backbar and eliminates lost space that can result in fewer manufacturers on contract, he says.

"As we look to the future, we anticipate a continuation and escalation of the pronounced transition of the backbar with decline of the traditional categories such as combustibles and OTP (other tobacco products), while the innovations category will see a continued and rapid rise in popularity, especially coming out of the pandemic," Purviance says. "We also have our eyes on emerging categories within THC and CBD, preparing retail for what will certainly be an onslaught of demand as legislation is introduced."

Typically, retailers will reset their backbar units about every 10 years, Purviance says, more reason why retailers need a system that can be modified as needed.

ImageWorks Display's Impact unit provides versatility by incorporating 1-foot shelving, vertical adjustability and a patented frame system.

The backbar is worth investing in because it's valuable space, and the last thing a customer sees when they walk out the door, says Sarah Rogers, account executive at Plain City, Ohio-based Midwest Retail Services, which is a supplier of shelving units, including Harbor's Infinity system.

Retailers should make sure they are using a platform for tobacco that the manufacturers are always going to be making solutions for, she says. Having shelving that allows for quick changes also allows retailers to quickly capitalize on new trends.

"We know convenience-store customers are super loyal, so once they know they can get [a particular product] with you, they're not going to go anywhere else," Rogers says.

At the end of the day, making sure the tobacco-set fixtures are flexible is a base requirement to have a successful category, Welsh says.

"There is a huge amount of opportunity within tobacco," Welsh says. "The advice I'd give any retailer is: Focus on the core mission of your organization. Spend the time to understand your customers and the industry as a whole. And then invest in the points where all those things intersect."

Beefing Up the Backbar

CSP asked tobacco manufacturers for tips for creating a flexible backbar.

"Retailers need to reevaluate their backbar space in new builds and existing stores. Any products that can be moved to the selling floor, should be. This would help increase the flex space available for retailers to offer consumers new and different products they feel have potential."

—Howie Heylmun, zone manager north for E-Alternative Solutions, Jacksonville, Fla.

"The linear space and category allocation of that space for the backbar of yesteryear will need to evolve to accelerate emerging categories. Looking beyond the traditional space with digital technologies and assets will complement this evolution. How much of the linear and total space is dedicated to new categories today? What is preventing you from making the change?"

—Daniel Harrington, senior director of retail at Reynolds Marketing Services Co., Winston-Salem, N.C.

"Swisher feels it is critical to consistently review tobacco category and subcategory performance for results. Retailers can utilize this knowledge, to change shelf space allocations and product mix to items that are trending and providing exceptional margins. …. Building good product assortments focused on adult consumers' purchase patterns should be first and foremost in the decision-making process."

—Karen Saber, vice president of business analytics and strategic sales innovation at Swisher, Jacksonville, Fla.

"Retailers need to balance space on the backbar for innovative products that are experiencing rapid growth and ensure inventory capacity to support sales for the large and profitable traditional tobacco products, e.g. cigarettes and moist smokeless tobacco. … The AGDC Marketplace e-commerce site offers one-stop shopping for back-bar merchandising resources."

—Jessica Pierucki, managing director of trade marketing–innovation, Altria Group Distribution Co. (AGDC), Richmond, Va.

photograph courtesy of imageworks display

BAN ON THE RUN

Retailers Grapple With a Possible Ban of Menthol Cigarettes and Flavored Cigars

BY HANNAH PROKOP

Convenience retailers may have to grapple with significant changes to their tobacco sets if the U.S. Food and Drug Administration (FDA) succeeds in prohibiting menthol as a characterizing flavor in cigarettes and flavored cigars.

However, these changes could take years and would likely face legal challenges. Following the FDA's announcement in late April, *CSP* talked to c-store retailers about what these changes would mean for their stores.

Menthol cigarettes make up about 25% of cigarette sales at Yesway convenience stores, says Kevin Harder, the chain's tobacco category manager. Fort Worth, Texas-based BW Gas & Convenience Holdings owns and operates more than 400 convenience stores in the Midwest and Southwest under the Yesway and Allsup's brands.

"Nobody wants to give up even 5% of their business, let alone 20-plus percent," he says.

But c-stores and other tobacco retailers might have to if the FDA succeeds in prohibiting menthol as a characterizing flavor in cigarettes. The Silver Spring, Md.-based agency announced on April 29 that banning menthol cigarettes was one of its highest priorities.

The FDA also says it intends to ban flavored cigars, including menthol. The decision is based on clear science and evidence establishing the addictiveness and harm of these products, the FDA says.

FDA Rulemaking Process

The FDA's rulemaking process for a menthol cigarette ban would follow similar steps to a proposed new nicotine standard, says analyst Bonnie Herzog of Goldman Sachs. Here's a brief look at those steps:

- The FDA issues a notice of proposed rulemaking.
- The Office of Management and Budget assesses the economic consequences of any proposed rule.
- Once the FDA issues a proposed rule, the comment period starts.
- Before issuing a final rule, the FDA must address all comments received, and consider and resolve a range of issues.
- If a final rule is ultimately issued, there is a mandatory one- to two-year delay before it can be legally implemented.
- A final rule could face legal challenges.

"Banning menthol—the last allowable flavor—in cigarettes and banning all flavors in cigars will help save lives, particularly among those disproportionately affected by these deadly products," says Acting FDA Commissioner Janet Woodcock. "With these actions, the FDA will help significantly reduce youth initiation, increase the chances of smoking cessation among current smokers and address health disparities experienced by communities of color, low-income populations and LGBTQ+ individuals, all of whom are far more likely to use these tobacco products."

Menthol is a flavor additive with a minty taste and aroma. It may reduce the irritation and harshness of smoking when used in cigarettes, the FDA says; however, research suggests menthol cigarettes are harder to quit than nonmenthol cigarettes, particularly among African American smokers. More than 19.5 million people are current smokers of menthol cigarettes, according to the FDA.

Tobacco companies disagree, however, on the risks of menthol cigarettes and effectiveness of prohibition.

"Reynolds will evaluate any proposed regulation and will participate in any consultation and the rulemaking process by submitting robust, science-based evidence," Kaelan Hollon, spokesperson for R.J. Reynolds Tobacco Co., Winston-Salem, N.C., says. "The scientific evidence neither shows a difference in health risks between a menthol and a nonmenthol cigarette, nor does it support that menthol cigarettes adversely affect initiation, dependence or cessation."

Richmond, Va.-based Altria, which owns Marlboro and Virginia Slims cigarette maker Philip Morris USA, says the company shares the goal of moving adult smokers from cigarettes to potentially less-harmful alternatives—but prohibition does not work.

"Criminalizing menthol will lead to serious unintended consequences. A far better approach is to support the establishment of a marketplace of FDA-authorized noncombustible alternatives that are attractive to adult smokers," George Parman, director of communications for Altria Client Services, says. "Finally, youth smoking rates, including menthol cigarettes, are at historical lows, and science and evidence does not support such a ban."

Travis Welsh, senior category manager for tobacco at Des Moines, Iowa-based Kum & Go, told *CSP* his first reaction to the news on menthol cigarettes was to not overreact.

"There's a pretty lengthy process that this has to go through in order to be fully put into place," Welsh says. "And that lengthy process is going to make sure that the science is listened to, make sure the right steps are taken [and] make sure that those of us in the industry have the time to react."

Welsh says that while a ban would affect cigarette sales, he's hopeful consumers would shift to other categories.

When it comes to the U.S. cigarette category, New York-based Goldman Sachs Managing Director Bonnie Herzog says menthol is about 33% of total volume.

While there is some risk a federal ban of menthol cigarettes could reduce smoker initiation and prompt smokers to quit, menthol cigarette users may also convert to nonmenthol cigarette or reduced-risk products with a menthol variant like e-cigarettes or a heat-not-burn device, she says in a research note.

"Nobody wants to give up even 5% of their business, let alone 20-plus percent."

It's too early to change c-store tobacco sets now in reaction to the menthol ban, Welsh says. But Kum & Go has already taken steps to highlight modern oral nicotine (MON) and other noncombustible products, he says.

Yesway has made similar efforts.

"We're supporters of people transitioning to alternative or noncombustible forms of tobacco in general anyways, so there's a potential if the e-cigarette side is left open with flavors, or at least menthol, from a vapor standpoint, we could see the speeding up of transition to adopt e-cigarettes or other products," Harder says.

If a menthol cigarette ban were to be implemented in several years, Herzog says she would expect a minimal negative impact on the total nicotine pool if smoker conversion to reduced-risk products accelerates.

"The FDA's guidelines require that, for this menthol ban on cigarettes to be implemented, it needs to be proven that it is science-based and does not have any unintended consequences, and this makes for a lengthy process and uncertain outcome," she says.

The lengthy process is why Chris Li, analyst with Desjardins Securities, Montreal, says in a research note that a menthol cigarette and flavored cigar ban could affect Laval, Quebec-based c-store retailer Alimentation Couche-Tard Inc.'s business long term but would be limited for the short term. Li estimated a ban on menthol cigarettes and flavored cigars would affect the owner of Circle K c-stores by 2% to 3% earnings per share long-term.

CATEGORY MANAGER OF THE YEAR 2021

KEVIN HARDER:

TOBACCO AFICIONADO

After 11 years with Reynolds American, Kevin Harder came to the c-store industry with some advanced insights in the tobacco category. For the past two and a half years, he has led that category for Yesway, whose parent company, BW Gas & Convenience Holdings, owns and operates more than 400 c-stores in the Midwest and Southwest.

What do you like most about the tobacco/nicotine category?

There is always change, from regulation and taxation to manufacturer price increases to new innovative products. The category is filled with opportunity to make changes and make a difference.

Describe your category management philosophy.

Make the category shoppable. It should be easy for our customers to know what we have to offer and what our prices are, which ultimately drives sales.

How did the pandemic change the category?

Purchase habits appear to have changed, with more customers buying rolls and cartons than before. With more people working from home, usage opportunities have increased, which has led to increased consumption. If the work-from-home movement sticks, there may be less decline than in pre-pandemic years. Production issues have really hurt certain segments like cigars, but at some point they will overcome their issues.

What are your category goals for 2021?

Continue to make our stores more shoppable for our customers through new fixture initiatives, SKU rationalization, space optimization, and execution of our marketing and promotional plans with impact.

What are some of the most promising new products?

Zyn, On! and Rogue nicotine pouches continue to grow, and the promotional spend of the manufacturers is making the battle between these products fun to watch.

What are your biggest challenges today?

Ordering and inventory management. Turnover in c-stores has always been an issue, but COVID-19 has presented additional challenges. One of those is ensuring we have additional staff at stores who are trained to handle ordering responsibilities.

How have you partnered with your category captains?

Communication about important issues, including product availability, has increased.

What makes you most passionate about this category?

Helping our customers find products that will transition the category to a smoke-free future. It's important for everyone's well-being that we eventually get there, but it needs to be done responsibly in a way that moves people from smoking to less harmful forms of tobacco/nicotine usage over time. Solely legislating our way to a smoke-free future would have a tremendous negative impact on our business.


ORIGINALS NEVER REST.
2 CIGARS
OPTIMO
CIGARILLOS
SWEET
NATURAL LEAF
2 CIGARS
SWISHER SWEETS
2 TIP CIGARILLOS
BLK
SMOOTH
2 CIGARS
SWISHER SWEETS
CLASSIC
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CIGARILLOS
SWISHER SWEETS
LEAF
AROMATIC
3 CIGARS
ALL NATURAL TOBACCO
NOW THE SHIELD
SWISHER SWEETS
MEANS MORE