Recent Shareholder Activism in the U.S. Convenience Store Industry

Convenience Store & Fuel Products Distribution Investment Banking

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Activist Shareholders Have Been Significantly Influential in the U.S. Convenience Store Industry

Overview & Case Study Takeaways

Shareholder “activism” refers to a range of tactics utilized by shareholders of a public company to influence some desired change in the corporation. High profile examples might include Bill Ackman’s unsuccessful effort to convince the world that the nearly $4 billion company (by revenue), Herbalife, was a deceptive pyramid scheme, inspiring the documentary, Betting on Zero. Other battles involving Automatic Data Processing, Procter & Gamble, CSX, and Buffalo Wild Wings grabbed headlines in 2017. On the less assertive end of the spectrum, a shareholder proposal may be put forth and sponsored by certain engaged shareholder groups (e.g. pension funds) to effect change in governance policies or compensation plans.

Shareholder activism has become a more normalized practice to effect change in a company; currently, direct activist assets under management (AUM) are estimated at approximately $121 billion(1). In 2017, this arsenal was deployed to launch 231(2) public campaigns in the United States, lobbying for changes to companies’ strategic directions, asset mixes and management and/or board compositions, among other demands. As a proxy for their success, over the past decade, activist investors have contributed to the appointment or replacement of more than 1,000 public company board members(3). Demands placed on target companies are significant and activists’ influence cannot be questioned.

In this piece, we analyzed the four most recent, relevant activist campaigns in the convenience store industry and have come to a few important takeaways:

- Empirically, according to research conducted by Raymond James’ Activism Response & Contested Situations (ARCS) practice, roughly one-half of activist campaigns result in a significant corporate event(4) within three years of launch and of those cases, roughly half of the corporate events occurred within one year
- Within the convenience store industry, activist investors, and particularly JCP Investment Management, have registered notable success generating stock price returns and influencing major strategic actions
- Over the prior three campaigns in the industry, target companies were ultimately sold in two instances (CST Brands and The Pantry) and in the third, Marathon Petroleum Corporation undertook efforts to accelerate certain strategic initiatives; along the way, average non-annualized returns to shareholders over the course of the activist campaigns exceeded 30%
- Given the historical “success” (as defined by shareholder returns) of activists in the c-store industry, neither the size of the ownership position in the company (JCP acquired a 1.3% stake in CST Brands during its activist campaign) nor the size of its fund correlates well with the significance of the strategic actions the activist is able to influence – likewise, size should not influence the extent to which a company targeted by activists takes the threat seriously
- Historical success will encourage additional interest in agitating for change (e.g. Casey’s current situation); shareholders will likely welcome activist involvement
- Before becoming targets of activist campaigns, management teams should perform thorough examinations of their existing structural defenses (e.g. staggered board), assess potential vulnerabilities and proactively address weaknesses, and have a response plan and team in place

Summary of Recent Activist Shareholder Activity in the C-Store Space

<table>
<thead>
<tr>
<th>Company</th>
<th>Activist</th>
<th>Duration</th>
<th>Activist Demands</th>
<th>End Result</th>
<th>Pre-Campaign Price</th>
<th>Stock Price at Conclusion</th>
<th>% Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>CST</td>
<td>JCP</td>
<td>1/3/2018 - Current</td>
<td>Explore sale</td>
<td>TBD</td>
<td>$112.39</td>
<td>TBD</td>
<td>N/A</td>
</tr>
<tr>
<td>Marathon Petroleum Corporation</td>
<td>Elliott</td>
<td>November 2016 - December 2017</td>
<td>Eliminate IDR, accelerate dropdowns, split-up company</td>
<td>Elimination of IDR, accelerated dropdowns, Speedway retained</td>
<td>43.31</td>
<td>65.75</td>
<td>51.8%</td>
</tr>
<tr>
<td>Engine Capital LP</td>
<td>JCP</td>
<td>December 2015 - August 2016</td>
<td>Explore sale</td>
<td>Company sold</td>
<td>36.54</td>
<td>48.53</td>
<td>32.8%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>February 2014 - December 2014</td>
<td>Board seats, strategic initiatives</td>
<td>Company sold</td>
<td>16.15</td>
<td>36.75</td>
<td>127.6%</td>
</tr>
</tbody>
</table>

(1) Source: HFR Q1 Global Hedge Fund Industry Report.
(2) Source: FactSet / SharkRepellent.
(4) Defined as a company sale, significant asset divestiture, or a scenario in which the activist was successful in having some or all of its demands met.
Case Study: The Pantry, Inc.

Summary of Situation

On 1/23/14, The Pantry, Inc. ("Pantry" or the "Company"), a 1,500 site Southeastern-focused convenience store chain announced that it received notice from two activist investors nominating three candidates to the Company’s Board of Directors. The activist investors argued that the Company was deeply undervalued as a result of poor investment and operational decisions and that the current board had presided over prolonged underperformance. The three board candidates were eventually elected at the Company’s annual meeting after a proxy advisory firm (Glass Lewis) backed the activist investors. On 12/18/14, the Company announced a definitive merger agreement with Alimentation Couche-Tard which valued the Company at $36.77 per share.

Company Response

- The Pantry dismissed the three activist-nominated board candidates as being inexperienced in the industry
- The Company instead announced the Board had nominated Thomas W. Dickson as an independent director
- The Company urged stockholders to disregard the report by proxy advisory group, Glass, Lewis & Co. LLC, in which Glass Lewis recommended that shareholders vote in favor of the activist-nominated board candidates

Activist Considerations

1. Shareholder returns have been significantly lower than peers and the S&P 500
2. The Company has experienced a multi-year decline in cash flows in the fuel business and has instituted a significant capital spending program that, based on historical ROIC, would likely not produce incremental EBITDA
3. The Company has lagged its peers in multiple operational indicators of performance (same-store sales / volume, ROIC, etc.)
4. The Company’s four CEOs in five years have all failed to articulate and execute a plan to prevent further value destruction

Key Dates & Timeline

- **January 23, 2014:** JCP Investment Management nominates candidates for the Board of Directors
- **January 29, 2014:** The Pantry disregards the activist-nominated board candidates and instead nominates Thomas W. Dickson as an independent member of the Board
- **February 5, 2014:** JCP & Lone Star push The Pantry to explore the possibility of creating a real estate investment trust (“REIT”) citing significant real estate value in the Company’s portfolio
- **February 24, 2014:** Glass Lewis recommends shareholders vote in favor of JCP’s nominated board candidates
- **February 25, 2014:** Activist investors send a letter to stockholders discussing The Pantry’s stagnant growth and suggested plans to create shareholder value
- **February 28, 2014:** The Pantry urges shareholders to disregard Glass Lewis report in support of the activist-nominated board candidates
- **March 19, 2014:** The Company announces preliminary results of shareholder vote, approving activist-nominated board candidates who ultimately hire Bank of America to lead to a sale process unannounced to the shareholders
- **December 18, 2014:** The Company announces the signing of a definitive agreement with Alimentation Couche-Tard for $1,726 million (7.8x EV/EBITDA), representing a 27.4% premium to the unaffected share price

Annotated Synopsis of the Campaign

- **1/23/14:** $16.15 JCP and Lone Star are reported to own 1.9% stake in The Pantry and have nominated three candidates to serve on the board of directors
- **2/25/14:** $13.63 JCP Investment Management and Lone Star Value Management send a letter to The Pantry urging shareholders to vote for their nominated directors
- **3/19/14:** $15.44 The Pantry announces that three activist-nominated candidates have been elected to serve as directors who in turn decide to launch a process to review strategic alternatives
- **12/18/14:** $36.48 The Pantry announces definitive merger agreement under which Alimentation Couche-Tard will acquire the Company in an all cash transaction valued at $1,726 million

Source: Publicly-disclosed activist letters, company press releases, Capital IQ and Raymond James’ Equity Research.
Case Study: CST Brands, Inc.

Company: CST Brands, Inc. (NYSE: CST)
Activist: JCP Investment Management, Engine Capital
Announce Date: 12/9/2015
Market Capitalization (at announce): ~$2.8 billion
Activist Ownership (at announce): ~2.3%

Summary of Situation
On 12/9/15, Engine Capital delivered a letter to CST Brand’s (“CST” or the “Company”) Board of Directors expressing concern over the Company’s stock price performance since the spin-off from Valero Energy in May of 2013. On 12/22/15, JCP Investment Management submitted a separate letter citing plans to nominate new directors due to lack of progress on operational initiatives. CST Brands reached an agreement with the activist investors and announced plans to evaluate strategic alternatives due to the perceived disconnect between CST’s intrinsic value and CST’s share price.

Activist Considerations
1. CST’s stock is valued below its peers (Casey’s, Speedway, and Alimentation Couche-Tard)
2. CST has experienced below-industry average merchandise margins and stagnant same-store sales comps
3. “Inadequate” return on capital on the Company’s new store builds
4. “Mismanagement” of CrossAmerica Partners (CST owns the GP interest in CAPL)
5. Staggered board with “inadequate” shareholder representation

Company Response
- A planned launch of a sale-leaseback strategy to spur greater liquidity to invest in large-format NTI stores
- Maintain strategy to add premium retail chains at valuations similar to Nice N Easy (Canastota, NY) and Flash Foods (Waycross, GA)
- Reiterated plan to continue returning funds to investors while continuing to fund its stated growth plan
- Creation of two new senior positions: President of Retail Operations and President of Growth and Strategy

Key Dates & Timeline
- **December 9, 2015:** Engine Capital (1.0% ownership) delivers letter to CST’s Board of Directors expressing concern over poor performance since spin-off from Valero Energy in May of 2013
- **December 22, 2015:** JCP Management (1.3% ownership) delivers separate letter to CST announcing plans to nominate new director candidates, citing the lack of progress in operational initiatives
- **March 3, 2016:** To appease JCP and Engine, CST Brands hires Bank of America and JP Morgan to evaluate strategic alternatives for the Company
- **May 5, 2016:** CST announces its divestiture of California and Wyoming assets to 7-Eleven for $408 million
- **August 22, 2016:** CST announces agreement with Alimentation Couche-Tard for acquisition of CST for $4.4 billion or $48.53 per share, representing a 27.6% premium to the unaffected share price

Annotated Campaign Timeline

Source: Publicly-disclosed activist letters, company press releases, Capital IQ and Raymond James’ Equity Research.
Company: Marathon Petroleum Corporation (NYSE: MPC)  
Activists: Elliott Management Corporation  
Announce Date: 11/21/2016  
Market Capitalization (at announce): ~$24.9 billion  
Activist Ownership (at announce): ~4%

Case Study: Marathon Petroleum Corporation

Summary of Situation
On November 11, 2016, Elliott Management, owning ~4% of the common stock of Marathon Petroleum Corporation (“Marathon” or the “Company”) sent a letter recommending specific actions be taken to add $14 – $19 billion of value for shareholders. Elliott recommended that Marathon immediately drop down all MLP-qualifying income to MPLX, the Company’s midstream energy infrastructure MLP subsidiary. Additionally, Elliott suggested conducting a full strategic review giving careful consideration to a potential spinoff of Speedway, the Company’s convenience store operating segment. Marathon initially signaled disagreement with Elliott’s plan, but later announced steps to pursue value-creating actions including substantial dropdowns to MPLX, as well as conduct an independent review of Speedway. Elliott eventually voiced its support for Marathon’s decision to retain Speedway.

Activist Considerations
1. Marathon is severely undervalued and readily available steps could unlock a 60 – 80% increase to the Company’s stock price
2. Marathon should immediately drop down all MLP-qualifying assets to MPLX (in other words, a sale of assets by the parent entity to the MLP subsidiary)
3. Marathon should exchange incentive distribution rights for LP units in order to simplify current distribution structure and lower its cost of capital
4. Marathon should conduct a full strategic review of its current structure, giving careful consideration to whether a tax-free separation of Speedway or a tax-free separation of the Company into three standalone business (Speedway, Refining Co., Midstream Co.) would be beneficial

Company Response
• Upon reviewing the letter, Marathon hired Evercore Partners to assist with a strategic review
• Marathon reiterated its previously announced plans to schedule substantial drop downs to MPLX citing tax issues and other impediments to an immediate drop down
• Marathon pushed back on the idea of spinning off Speedway and echoed previous comments made by the Company that Speedway has and will continue to deliver substantial value to shareholders

Key Dates & Timeline
• November 21, 2016: Elliott Management sends a letter to MPC outlining the readily available steps that Elliott believes would unlock $14 – $19 billion in value for shareholders (~60 – 80% increase to share price); that same day, Marathon hires Evercore Partners to advise on its activist defense strategy with Elliott
• September 5, 2017: Marathon’s Board of Directors announces a decision to keep its Speedway retail arm after an independent review of strategic alternatives, specifically citing the segment’s ability to help generate long-term returns for shareholders; a decision that Elliot ultimately supported
• September 1, 2017: The Company drops down four subsidiaries to MPLX
• November 14, 2017: The Company drops down its refining and fuel distribution assets to MPLX
• December 15, 2017: Marathon decides to remove its incentive distribution rights in MPLX for additional limited partnership interests

Annotated Campaign Timeline

Source: Publicly-disclosed activist letters, company press releases, Capital IQ and Raymond James’ Equity Research.
Case Study: Casey’s General Stores

Company: Casey’s General Stores (NASDAQGS: CASY)
Activists: JCP Investment Management, BLR Partners, and Joshua Schechter
Announce Date: 1/3/2018
Market Capitalization (at announce): ~$4.2 billion
Activist Ownership (at announce): ~1.1%

Activist Considerations
1. Casey’s shares are significantly undervalued
2. Casey’s has missed earnings estimates for seven consecutive quarters due in part to decelerating same-store sales and “bloated” operational expenses
3. Casey’s would likely be valued between $150 and $170 per share to a potential strategic acquirer given significant synergy potential and real estate value

Key Dates & Timeline
- March 7, 2017: Casey’s falls short of earnings consensus in Q3 FY 2017
- June 6, 2017: Casey’s falls short of earnings consensus in Q4 FY 2017
- December 11, 2017: Casey’s falls short of earnings expectations in Q2 FY 2018 mainly driven by less than expected same-store sales growth; Casey’s stock price decreased 11.6% upon earnings announce
- January 3, 2018: JCP Investment Management, BLR Partners, and Joshua Schechter send a letter to the Company suggesting that the company is significantly undervalued
- January 4, 2018: Casey’s acknowledges the letter and announces that they will review its contents thoroughly
- March 7, 2018: Casey’s falls short of earnings consensus in Q3 FY 2018

Summary of Situation
On 1/3/18, JCP Investment Management, BLR Partners, and Joshua Schechter issued an open letter to Casey’s General Stores ("Casey’s" or the "Company") shareholders suggesting the public convenience store chain is significantly undervalued and urging the board to engage a financial advisor to explore all strategic alternatives, including a potential sale. According to the letter, Casey’s earnings guidance misses and decelerating same-store sales growth have hampered share price performance in recent quarters. Casey’s issued a statement on the same day the open letter was received indicating they were surprised by the letter, but would review the contents thoroughly. JCP, a frequent activist investor in the space, was instrumental in the sales of The Pantry and CST Brands to Alimentation Couche-Tard.

Company Response
- The Company’s five year total shareholder returns ("TSR") of 121% exceeded the TSRs of the S&P 500 Index (108%) and the S&P Retail Index (46%) over the same period
- JCP had met with Casey’s in Summer 2017; during their discussion, JCP did not suggest that Casey’s explore strategic alternatives
- Although the Company disagrees with the letter, they will review the content of the letter thoroughly

Source: Publicly-disclosed activist letters, company press releases, Capital IQ and Raymond James’ Equity Research.
ABOUT RAYMOND JAMES ACTIVISM RESPONSE & CONTESTED SITUATIONS (“ARCS”)

- Established in 2016 as the only middle-market investment banks to offer a dedicated practice advising corporate clients on investor activism preparedness and response, contested M&A, shareholder engagement and corporate governance matters

- A recent survey of activists conducted by law firm Schulte Roth & Zabel LLP showed that 68% saw little or no opportunity in mega-cap companies, while 67% saw “a lot” of opportunity in small-cap stocks

- In both 2016 and 2017, half of the overall universe of companies targeted by activists had a market cap between $50 million and $1 billion

Recent Defense Mandates

<table>
<thead>
<tr>
<th>Month</th>
<th>Event Description</th>
</tr>
</thead>
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<tr>
<td>February 2018</td>
<td>Defense advisory against Sierra Capital Investments</td>
</tr>
<tr>
<td>June 2017</td>
<td>Proxy fight defense against Macellum Capital</td>
</tr>
<tr>
<td>May 2017</td>
<td>Defense advisory against Elliott Management</td>
</tr>
<tr>
<td>April 2017</td>
<td>Defense advisory against two separate shareholder activist groups</td>
</tr>
<tr>
<td>July 2016</td>
<td>Defense advisory against Orange Capital Ventures and MM Asset Management</td>
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Meet the Expert

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- Duncan has more than 15 years of transactional experience and specific expertise in contested M&A, shareholder activism, takeover defense and corporate governance

- He previously served in Credit Suisse’s contested situations practice, where he was responsible for advising both domestic and international clients across all sectors on contested matters

- Prior to Credit Suisse, Duncan was an M&A lawyer at Paul Weiss Rifkind Warton & Garrison, based in its London office, where he specialized in structuring and executing cross-border transactions

- Duncan received his J.D. from Harvard Law School and his MBA from London Business School

- He is a CFA charterholder and a member of the State Bar of California

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ABOUT RAYMOND JAMES CONVENIENCE STORE & FUEL PRODUCTS DISTRIBUTION INVESTMENT BANKING

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- Maintain deep relationships with key equity investors, specialty lenders, sale-leaseback providers and other capital sources
- As M&A specialists, we understand the concerns of buyers and sellers and how to drive value for our clients

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- Commercial Fuel & Lube Distributors
- Truck Stop and Travel Center Operators
- Alternative Fuel Providers
- Propane Distributors
- Terminal Operators
- Merchandise / Foodservice Distributors
- Mobile Fueling

Representative Transactions

What Our Clients Say

“Raymond James managed the sale of our company’s convenience store assets in a knowledgeable and professional way. They saw the transaction to the finish line and helped realize the best value for our family. We definitely chose the right investment bank”

Ken Dwelle // COO and Owner, Flyers Energy, LLC

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