

STATEMENT BY:
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Madam Chair and Members of this Sub-committee, as this is my first opportunity to appear before you as the Commander of the Army and Air Force Exchange Service (AAFES), I want to express my sincere gratitude for your steadfast support in preserving a strong and effective exchange benefit for the men and women of the Armed Forces and their Families. I look forward to working with you to ensure AAFES continues to play a significant role in the quality of life of Soldiers, Airmen, and their Families through its operational and financial contributions to military Morale, Welfare, and Recreation (MWR) programs.

I appear today to testify on behalf of AAFES; to share some of our accomplishments from 2007 and update you on our strategies to meet the challenges we face in 2008 and beyond. I am proud to report that AAFES continues to fulfill our nearly 113 year old mission of providing quality merchandise and services at competitively low prices while consistently generating earnings to support MWR programs. AAFES operates more than 3,100 facilities worldwide, in 30 countries, five U.S. territories and 49 states. Perhaps best known for our BX/PX retail stores, AAFES also runs more than 2,200 food and theater operations including 956 name brand fast food restaurants on both a direct and concession basis. These include brands our customers know from home such as Burger King, Taco Bell, Subway and Starbucks.

Since troops were first deployed to the Middle East after 9/11, AAFES has aggressively extended the Armed Forces' exchange benefit to the frontlines. Beyond OEF and OIF theaters, AAFES has also delivered support to Soldiers, Airmen, Sailors, and Marines at Landstuhl Regional Medical Center by providing civilian clothing as part of Public Law 1559. With the 2007 opening of the Center of the Intrepid at Brooke Army Medical Center (BAMC) at Ft Sam Houston, TX, AAFES is taking lessons learned in serving troops recovering from injuries received in a war zone and implementing them at BAMC, to ensure America's "wounded

warriors” have access to all of the essentials available at the BX/PX. AAFES provides a dedicated personal shopper program at BAMC and offers in-room barber/beauty services to inpatients at Walter Reed Army Medical Center. These services allow troops recovering from amputations, burns, and other serious injuries to concentrate on their rehabilitation instead of worrying about how they will get a haircut or a clean pair of socks. AAFES is also assisting those troops recovering from injuries transition into the civilian workforce by taking part in the Department’s “Hiring Heroes” program. AAFES participates in the program’s job fairs and posts AAFES job opportunities on the Hiring Heroes website. These programs are certainly indicative of AAFES’ commitment to America’s troops. Regardless of whether they are at home station, deployed overseas, providing support in the wake of a natural disaster, or even in the hospital, AAFES will be there to serve and support.

When customers cannot get to a store due to contingency deployment or geographic separation, or when they simply prefer shopping from the comfort and convenience of their home, AAFES provides a robust catalog and e-commerce program operated on behalf of all of the military exchanges. In 2007, the All-Services Exchange Catalog and Exchange Online Store offered customers more than 30,000 items via www.aafes.com, thousands of items from vendor partners and hundreds of thousands of items from ExchangeOnlineMall.com partners including Apple, Bose, Books-a-Million and Office Depot.

The scope of our business operations goes well beyond the conventional offerings of civilian retailers. Working with local community businesses and small entrepreneurs to include minority and women-owned businesses, AAFES contracts for a multitude of personal services and commodity sales to supplement the support provided to the military community. Overseas, AAFES operates bakeries and water bottling activities to provide Military Families the same fresh, high quality branded products they would enjoy in the United States: Wonder Bread,

Country Hearth Bread, and Culligan Water, just to name a few. We provide these products for sale in exchanges as well as to overseas commissaries, troop dining facilities, military hospitals, and MWR clubs. As the designated Department of Defense (DoD) School Feeding Authority, AAFES provides 24,000 nutritious meals per day to 92 schools in 9 countries on a break even basis.

AAFES manages the combined exchange in-house brand credit card, MILITARY STARSM Card—a low interest credit card that has unique military features such as: 10 percent off first day's purchases; no annual fee; no late or over limit fees; financial education through statement inserts, statement messages, online resources; 24/7 customer assistance; and exclusive military promotions throughout the year. As part of AAFES' commitment to our patrons and to honor those serving in harm's way, AAFES offers a reduced interest rate and optional payment plan for deployed cardholders and has absorbed more than \$1.85 million in Military STAR Card debt for those killed in action since September 11, 2001. Furthermore, our customers are extended moderate credit limits to give them an opportunity to build good credit which is an important attribute of the program. The MILITARY STARSM credit program is a benefit enhancer that protects military members from predatory credit schemes. The current MILITARY STARSM card interest rate is 10.24 percent compared with interest rates of up to more than 25 percent among competitors' in-house credit programs. Annual sales from the MILITARY STARSM Card are \$1.5 billion across the three military exchange systems. In addition to the direct customer benefits, the joint MILITARY STARSM Card program provides a financial benefit to the exchanges by avoiding merchant fees of approximately \$25 million annually that exchanges would have paid if other commercial credit cards were used. To increase the utility of the Exchange Credit Program, AAFES is piloting a cutting edge dual credit card. This co-branded card combines the features of the MILITARY STARSM line of credit with a MasterCard for use in the exchange and

anywhere MasterCard is accepted. The new MILITARY STARSM Rewards MasterCard[®] provides patrons a competitive interest rate and rewards features that have quickly become an industry standard. Customers will earn two reward points for each dollar spent for qualifying purchases on installation at exchanges, commissaries, and MWR programs. MasterCard purchases everywhere else will earn one point per dollar.

While 2007 was a challenging year for competitive retailers, AAFES continues to demonstrate it is a strong and viable organization with the strategic resilience and financial health to compete in the global marketplace. Revenues for AAFES fiscal year (FY) 2007 were \$8.7 billion, a decrease of \$204 million over FY 2006 in part due to the fact that the retail calendar for FY 06 was 53 weeks versus 52 weeks in FY 2007. Despite this decrease in revenues, AAFES ended the year with earnings totaling \$426 million representing a 27 percent increase from FY 2006. The preliminary results for FY 2007 indicate that AAFES is expected to contribute \$269 million in dividends which support the Army, Air Force, Marine Corps, and Navy service members and their Families. This return represents the highest dividend returned to the Services since 2002. These remarkable results are due to outstanding efforts to improve supply chain efficiencies across the enterprise and in part attributable to Congressional supplemental funding for reimbursement of AAFES expenses in support of the War on Terror. For FY 2007, AAFES was reimbursed \$92 million for actual operating expenses. I want to express my appreciation for this committee's support for this funding which helps offset extraordinary expenses incurred to support Operations ENDURING FREEDOM (OEF) and IRAQI FREEDOM (OIF).

AAFES earnings generate dividends for the military community while simultaneously funding its internal capital reinvestment program to ensure its facilities provide a shopping environment that is world class and an undeniable benefit to the military community. In 2007,

AAFES completed \$344 million in capital improvements at 57 installations worldwide providing shoppers with 496 new or renovated retail, dining, and services destinations. Among these were eight new shopping centers including Ft Campbell, KY, Peterson AFB, CO, and Ft Irwin, CA. More important than the numbers, this investment in AAFES facilities directly impacts more than 951,000 active duty sponsors and Family Members who enjoy an enhanced in-store experience today and for years to come. AAFES continues to address OCONUS construction in support of Soldiers, Airmen and Families, including closely monitoring the Kaiserslautern Military Community Center (KMCC) construction at Ramstein Air Base, Germany.

The current capital program includes construction requirements resulting from the impact of Base Realignment and Closure (BRAC), as well as Global Defense Posture and Realignment (GDPR) and Grow The Army (GTA) initiatives. The Department directed the use of APF for nonappropriated fund (NAF) construction requirements at gaining locations.

AAFES operates in an extremely competitive and ever-evolving global marketplace. In order to compete in 2008 and beyond, we are refining our value proposition to be so clear and convincing that every potential customer understands AAFES is the best and first choice for quality merchandise and services. To “Win the Future,” AAFES is committed to a mantra that captures the essence of our strategies and a “handle” our associates can grasp: Think BIG and act small. Thinking BIG allows us to build on past successes and at the same time move AAFES toward a culture of loyalty, ownership and continuous improvement. Thinking BIG is about changing the productivity performance curve in a way that drives earnings and dividends to historic levels. It is about imagining the possibilities of a new future, setting BIG goals and holding ourselves accountable for delivering results.

Even as we challenge ourselves to think BIG, we also know that our strategies must be turned into executable tactics. Acting small means immediate, proactive action at the lowest

levels of the organization. It means turning our strategic plans and concepts into actionable tactics at the store level. It means flawless execution of all the ideas across multiple fronts and venues simultaneously. It means we understand all retail is local — and we must create life long emotional connections with customers one person at a time. It means every Associate is an owner of this business and held accountable and rewarded for performance. These ideas are built around an operating model with five strategic tenets that support our stated vision and mission. And, each is designed to support our “Winning the Future” plan. These five strategies are: drive enterprise productivity, foster collaboration, get back to basics, leverage enabling technology, and sustain the future.

AAFES is committed to fulfilling the Congressional intent to maintain the quality of life of Military Families by offering an affordable American lifestyle to those serving overseas. We diligently manage our share of the Army’s Second Destination Transportation budget, continually seeking ways to reduce costs while improving service. Over the past few years, AAFES has undertaken a number of initiatives to improve effective management and stewardship of APF; resulting in consistent cost savings through efficiencies and best management practices. We continue to target all phases of the supply chain from procurement to point of sale to ensure AAFES systems, processes, and business rules get the right merchandise to the right customers at the right time in the most efficient way possible. Cost savings realized are passed on to the customer at the register and through increased MWR dividends.

A big part of driving supply chain productivity is building new businesses. AAFES is positioned to accelerate profitable growth by developing innovative lines of businesses and bringing them to market as quickly as possible. For example, we have all witnessed significant changes in the telecommunications industry and AAFES is restructuring this business to match the changing needs of Soldiers and Airmen. AAFES has been in the telecommunications

business for nearly 20 years and our major products – calling cards, payphones, and telephones in barracks – have served our customers well, but their needs continue to evolve. No matter where they serve, Military Families want the same entertainment and communications opportunities found in any major US metropolitan city. AAFES is uniquely positioned to meet this need and is pursuing two new telecom initiatives: wireless and triple play; bundled TV-internet-telephone. These initiatives will give Soldiers and Airmen stationed at US bases overseas access to telecommunication technology available in the United States. For example, many Americans are using Voice over Internet Protocol (VoIP) for their phone service. Our new initiative provides Airmen at Yokota Air Base, Japan, VoIP phone service. For a flat rate of \$29.95, Airmen and their Families can call back to the United States as much as they want. In the first four months of VoIP service, Airmen at Yokota Air Base have already placed more 2.3 million phone calls totaling more than 13.6 million minutes. Our business model allows for the development of a global network for Soldiers and Airmen designed to follow them when they deploy or relocate.

AAFES is exploring another new business concept which will bring new and complementary retail developments to selected military installations in an effort to keep pace with evolving trends in commercial retail development. In recent years, the retail landscape has increasingly shifted away from traditional formats to emerging “Lifestyle Centers”; retail developments reminiscent of the small downtown shopping districts and town centers characterized by a sense of place and spirit of community. Today, Lifestyle Centers and mixed use developments offer a sense of place by bringing a combination of retail, entertainment and convenience to today’s consumer. AAFES is developing a Lifestyle Center concept which will feature a traditional AAFES main store and concessions, a co-located Defense Commissary Agency (DeCA) commissary, MWR activities like casual dining and nationally branded gym,

along with complementing specialty retailers and entertainment venues. This is a great example of how AAFES is working to effectively leverage NAF instrumentality and industry funding for maximum effect and collaborating with our sister resale agencies and commands.

I believe the future belongs to those who build relationships and collaborate. This includes creating synergies with industry partners as well as the entire military resale community. We want to be recognized as an enabling business partner and a great place for our Associates to grow and contribute. For example, for the second year in a row, AAFES has been recognized by DiversityBusiness.com as one of America's Top Government Organizations for multicultural business opportunities. We intend to continue to increase participation and partnerships with minority- and women-owned businesses. Diversity helps build our business while helping others grow theirs. Like all sustainability ideas, diversity not only makes good business sense, it is good business.

AAFES is also continuing to strengthen relationships with other members of the defense resale system, including our sister exchanges, through exchange cooperative efforts. A sustained focus on cooperative efforts between AAFES, the Marine Corps Exchange (MCX), and the Navy Exchange Service Command (NEX) is paying off for Military Families who are now able to redeem AAFES, NEX and MCX-specific gift cards at any Army, Air Force, Navy, or Marine Corps exchange facility. The exchanges have already redeemed over 3,000 exchange gift cards totaling more than \$82,000 that were originally purchased in one of the other exchanges. Other ongoing efforts are focused on three core cross-functional teams in the areas of Logistics, Indirect Procurement, and Enterprise Architecture (EA). The Logistics team is working on seavan sharing for Pacific operations and van stuffing. The Indirect Procurement Team is focusing on cost reductions through economies of scale. In 2007 they implemented a joint contract for PCs, servers, and laptops which achieved an average 17.6 percent savings or

\$1.37 million annually for all exchanges. Enterprise Architecture provides a conduit for developing long term joint strategies by identifying and scoping opportunities for interoperability. Establishing offices in each exchange, the EA team completed the foundation phase of the collaborative EA project and defined the collaborative supply chain taxonomy.

Exchanges continue to experience success of the jointly developed private label, Exchange Select, for a variety of consumable merchandise items such as health and beauty, automotive, and snack food. This private label provides a strong military brand identity, which allows a broader assortment for improved product selection, as well as for a favorable pricing strategy for our military customer. With annual sales of \$51 million, this joint program provides for lower cost products for military patrons, which may not have been possible without the combined purchasing power of the three exchanges in developing the private label products. It is clear we can accomplish more together than we can independently.

AAFES has built strong relationships with our MWR and resale partners outside of the exchange system. We recently launched an initiative to identify and develop partnership opportunities beneficial to both AAFES and Army MWR. In our first major project, AAFES and Army MWR-Europe are collaborating to develop a program for MWR to place orders via the internet for AAFES delivery direct to specific MWR locations. Although AAFES has provided items to MWR for some time, this new effort eliminates the need for MWR to maintain a warehouse, thus reducing a significant inventory investment and operating costs. Army MWR-Europe anticipates savings in reduced overhead and inventory investment. AAFES benefits by increasing our warehouse volume and leveraging our fixed costs.

We continue to work with DeCA on a number of successful cooperative efforts. We have long recognized the synergies realized through joint sales, but the 2007 Thanksgiving holiday advertising efforts yielded extraordinary results. Cross promotions resulted in largest ever

“Black Friday” sales for AAFES and provided DeCA with its highest single day sales—\$26.8 million—over the weekend prior to Thanksgiving. Other efforts, like using AAFES backhaul capability in Europe are driving costs out of the supply chain. We are committed to continuing these types of efforts that truly strengthen the value of the entire military resale system for our joint patron base when the initiatives make good business sense.

One key to getting back to basics in retailing is to listen to the voice of the customer. AAFES shoppers let us know how we are doing through the American Customer Satisfaction Index (ACSI) survey, an independent survey conducted annually by the University of Michigan. Since we adopted the ACSI as our corporate customer metrics in 1996, our scores have steadily improved. The 2007 results show that AAFES score of 72 out of 100 represented a 2.9 percent increase over 2006 and a 4.3 percent improvement since AAFES shoppers were initially surveyed. AAFES is gaining ground on the industry standard score of 73 and is committed to meeting and exceeding that benchmark.

The foundation of our customer-centric strategy is listening to, learning from and leveraging their collective input as well as providing the product selection in the categories of merchandise military shoppers expect. I would like to thank this committee for taking action to raise cost limits on restricted merchandise to ensure the exchange benefit is not diminished by the eroding impact of inflation. I look forward to working together to ensure there are no barriers to keep Military Families from making major purchases utilizing the low prices and the favorable credit terms that only the exchange can deliver.

Another foundation of basic retailing is ensuring we use technology to drive results and create sustainable business platforms. My predecessors have been sharing the story of Project Retek and the implementation of Oracle Retail with you during the last few years. I am pleased to report the implementation of Project Retek successfully went “live” in February 2008. The

four-year endeavor came within approximately \$1.5 million of the \$177 million budget with earnings estimated to increase by \$261.4 million by the end of 2010. The completion of Project Retek is a major accomplishment, not just because it was the largest enterprise architecture systems project in AAFES history, but because of the lasting benefits Project Retek will bring to AAFES.

The key benefit to this implementation is AAFES can centralize more processes and facilitate sound business decisions based on easy access to inventory information worldwide. Simply put, Oracle Retail is improving visibility and control over the entire supply chain. Today, the rollout of automatic replenishment is about to begin at select distribution centers and pilot main stores. Post rollout, AAFES can expect increased sales, reduced inventory, decreased operating costs, and improved gross profits as reflected in our 5 year strategic plan.

AAFES is continuously taking advantage of new emerging “green” initiatives that will reduce AAFES negative impact on the environment and strengthen the exchange benefit for our patrons. AAFES sustainability goals include reducing energy and water consumption, waste, fleet dependency on fossil fuels and increasing sustainable buildings, procurement of goods and services that use sustainable environmental practices, and efficient use of electronic products. Key sustainability programs include a utility consumption tracking program, Shoppette LED canopy lighting, main store re-lamping program, increase use of Energy Star drink vending machines, conversion to use of energy efficient walk-in coolers, pursuing Energy Star equipment with food franchises, and waste recycling. The U.S. Green Building Council has accepted 3 Shopping Center projects into their LEED retail pilot test program; Ft. Polk, LA, Randolph AFB, TX, and Ft. Belvoir, VA. These sustainability initiatives will bring long term improvements to the environment, reduce energy consumption, complement Service and installation energy goals, and ultimately protect the exchange MWR dividend from energy cost increases.

Determined not to rest on our laurels, AAFES is continually searching for ways to sustain the future. A key component of realizing AAFES' highest potential is building a bench for the future. We have renewed our focus on identifying, mentoring, and training leaders who will provide powerful leadership into the next decade and beyond. Improving their capacity to learn and grow, as well as broadening their work experience with critical jobs today, will help ensure our leaders can tackle the challenges of tomorrow.

Sustaining the future is also demonstrated by our ongoing commitment to service members to "Go Where You Go", a pledge that our team fulfills everyday in supporting deployed military operations as they execute their missions around the world. AAFES is entering its fifth year of support to forces deployed in OEF and OIF. We are recognized not only as a "market multiplier" – a value added business partner, but also a "combat multiplier" enhancing the effectiveness of America's war fighters. AAFES currently operates 82 exchanges, 207 name brand fast food operations, 528 concessions activities, and 36 unit-operated imprest fund activities throughout OIF and OEF with a forward deployed team of 430 associates, many of whom are on their second or third tours of duty. In addition to our operations in Southwest Asia, AAFES support is also in place for Europe Command's Joint Task Force East exercises in Bulgaria and Romania, and we continue to support forward deployed troops in Bosnia and Kosovo. Our support to Southern Command's Operation NEW HORIZONS is underway in Trinidad, Tobago and Suriname as our forces are involved in building a school and hospital in those areas. Within the continental United States, AAFES' fleet of tactical field exchanges remains engaged in support of mission training, exercise support, and support to populations of troops moving to reposition under the GDPR plan. This fleet of mobile exchange facilities remains ready to respond 48 hours or less to contingency events or natural disaster relief operations anywhere in CONUS.

AAFES supports the military community through our Military Family employment programs. More than 10,000 military Family Members have joined AAFES ranks, representing more than one-fifth of our entire 45,000-person workforce. To attract and retain military spouses and Family Members, AAFES offers a generous reinstatement program that ensures military Family Members who move from installation to installation are eligible to compete with current associates for in-house jobs. Recognizing those married to an active duty military member are often required to adapt to varied geographic demands, AAFES offers a Spouse Employment Preference program that provides additional preferential considerations to military spouses who apply for positions with the exchange.

Over the past year, AAFES has focused on energizing our outreach efforts to communicate the value, benefit and capabilities of the exchange. We recognize the pivotal role National Guard and Reserve troops are playing as they transition from a strategic force to an operational force. We are taking steps to reach out to these Citizen Soldiers to ensure they understand the value of their exchange benefit; on the installation, on-line and down range. In cooperation with TriCare, AAFES, is airing public service announcements through AAFES Exchange Television (EXTV) and Radio Network to convey critical health issues targeted to active duty Military, Guard, Reserves and their Families. These messages on topics such as eye health, nutrition and cancer prevention will communicate information to encourage a healthier military. The Patriot Family Connection is a group of programs that helps strengthen the relationship between deployed service members and those they love. Operation Forward is a gift giving program offering customers a way to send gifts back home to family and friends on holidays and special occasions. Collectable trading pins, e-cards and online contests create a sense of community and connection between deployed military members and those they have left back home.

To assist American citizens in expressing their support for our service members, the joint service “Help Our Troops Call Home” program allows any American to purchase a Prepaid Phone Card at www.aafes.com for delivery to deployed service members serving in OEF or OIF. The “Gifts From the Homefront” program provides a similar link on the website for the purchase of gift certificates that can be redeemed in any exchange around the world. These programs build relationships, enhance morale, and ensure Military Members appreciate and experience the support of family, friends and the American people.

Since I assumed command of AAFES last summer, I have seen first hand the importance of providing the exchange benefit to the “best customers in the world.” Each day we serve those who gallantly lay their lives on the line as America continues to fight the global war on terror and defend our country. Our courageous Family Members waiting at home puts them in a special category of American heroes willing to demonstrate self-sacrifice. In addition to active and retired forces, this benefit can be extended to include all of our military warriors including wounded or disabled, without impacting our ability to provide world-class customer service. AAFES customers are truly unique, they deserve the very best we have to offer.

I am tremendously proud of AAFES Associates who are providing the services we deliver to both kinds of heroes: Military and Family Members. The volunteer Associates currently deployed into the OEF and OIF theaters of operations are working hard alongside our America’s Joint Warriors, sharing some of the same risks, while providing a level of service unmatched in the retail industry. At home, AAFES Associates are dealing with the impact of BRAC, huge deployments, and tremendous competition in the marketplace. More importantly, they are doing all this while striving to meet the needs of Military Family Members. In some cases, our Associates are providing these critical services while their own children or spouses are deployed in harm’s way. Every story of exceptional service and support that works its way up to

my office truly warms my heart and makes me grateful that I have been given the chance to command such a fine organization.

I have addressed AAFES' success in delivering the exchange benefit and how our mission gives our team the unique opportunity to stand with one foot in the business world and with the other foot along side our armed forces. While performance metrics are important to both business and military communities, I must admit it is extremely difficult to measure the importance of what AAFES does every day. Enjoying a taste of home in a fast food activity in Afghanistan, purchasing snacks and sodas in Iraq, browsing PowerZones before turning in after a hard day in either location; these things have been described as "mini R & Rs." I can tell you it was important to me and my troops while deployed for a year to the Theater in 2006. As the AAFES Commander, I am proud to play a role in furthering the immeasurable legacy of value, service, and support to Military Members and their Families around the globe. On their behalf, I thank each of you and the entire House Armed Services Committee for your continued support.

I look forward to your questions.