

Submission for National Fuel Watch Scheme

My name is Wayne Rowe and I have been in the petroleum/convenience store business since 1989. I currently operate four Caltex sites across Western Australia (WA), with three of these sites under a Caltex royalty based franchise agreement and one site under a Caltex fuel commission seller/royalty agreement. The opinions expressed in this document are purely my own and therefore not necessarily supported by Caltex Australia.

I believe that FuelWatch is a complete waste of taxpayer's money in that it does not have a real influence on putting downward pressure on fuel retail prices and is just another example of government introduced legislation that only adds to the already overloaded burden of small business in the area of compliance and regulation, in what is and has for a long time been a highly competitive industry. It does however inform the public of what prices are available to them for a given 24 hour period but that benefit is negated by the market intelligence that is then available to the large oil company networks as well as the new entrants to the petroleum market the supermarket chains

The way the scheme was introduced and is operated is anticompetitive and very much biased against independent businesses in the day to day operation of their enterprise. The bureaucrats that administer the FuelWatch department will bleat from their comfortable government office that the scheme was introduced after much consultation with key stakeholders, which to this I say is rubbish. I attend a lot of forums with other Caltex franchisees and I do not know of any Caltex dealers that were given the opportunity to have any input into the way the scheme was implemented or the rules by which it would operate.

The biggest flaw that I see to the system is the 24 hour rule that forces dealers to sell at a predetermined maximum price with the mistaken belief that sites would therefore always post the lowest possible price, this assumption was held as the people drafting this legislation have absolutely no idea of what makes the fuel industry tick. Having had a meeting with the Minister concerned some time ago (I choose not to name that Minister for legal reasons), I am convinced this to be the case. The Minister made the ridiculous claim that they were after the big oil companies, as the belief was that these large oil companies were making too much money. I suggested he take a look at the share price of Caltex, that at the time were going so far south you could have bought the whole company on your gold visa card, to which he replied they must have been moving their real profits offshore. This is a publicly listed company; these were the sort of people that supported the whole concept of Fuel Watch being the great saviour of WA motorists at the bowser.

The method of notifying the department of your next price movement and indeed changing your price for the day is not very user friendly but I doubt that it was ever intended to be. At present the reality is that there is a time window of between 8:30 am and 2pm in which to log your price if you are going to change your price the next day. For reasons which I will provide a little further down, you will see that this is not always easy on the site operator. Additionally, changing the price at 6am in the morning is not a very good option for a lot of the sites in that it is one of the most expensive times of the day to be paying staff and also in lot of cases the hardest shift of the day to find people willing to work these hours, as well as being the busiest time of the morning for a lot of sites that I am in contact with, as a member of The WA Caltex Franchisee Dealer Council. This equates to more costs to the operator, more compliance because of safety issues with staff having to go out onto the forecourt a lot of times when it is still dark combined with the busiest time of the day, this creates a huge Safety issue, as well as an inconvenience to our customers.

In my opinion, the system should allow you to change your price for the next day as soon as it is available on the web. I support my opinion with the reason that the pricing decision for the site is usually the responsibility of the franchisee 7 days a week and if you are a dealer from the country in a remote location travelling somewhere by car it could mean that you may not have access to internet or mobile phone facilities in the time that is now

given. Put simply if I was in Karratha and had to drive to my site in Carnarvon on Wednesday and at 2.30 pm on Tuesday I go onto the web page and see that I need to do a price change as a competitor has moved their price up or down, I either have to leave Karratha very early to get to Carnarvon on time or wait until 8:30am to do my price change and then travel, either way is an inconvenience to my business operation. Additionally, what if you just want to be organised for the next day so you can have a day to relax away from the pressure of running the business? It is obvious to me that the scheme was devised to make dealers pay by way of being out of a competitive market for 24 hours if they made a bad pricing decision for that relevant day.

It has already been demonstrated that a simple mistake made when your price has been logged cannot easily be rectified. I know of one dealer that made such a mistake and rather than loose 10 cents per litre of fuel sold or risk a fine of up to \$4000.00 for selling above the price he had posted, had to put all his petrol pumps out of order for the day; an inconvenience to his business and his customers.

It would seem to me that a lot of politicians and regulators do not understand the fuel industry and the way it operates and I would like to point out some factors that are relevant when discussing this whole issue, as in my opinion too many commentators and people in positions to make decisions that affect this industry have no idea how the industry actually functions.

The fuel industry has, in my opinion, three distinct channels that I would describe as Refinery, Reseller and Retail Refinery, as detailed following.

Refinery

In Australia there are three major players in the Refinery business, it is my belief that these refineries are currently running at maximum capacity as we as a country currently have to import diesel fuel. Therefore you would hope these players are generating reasonable profits for their respective companies, for without profits they could not reinvest in the business to keep up with the ever changing business environment, due mainly to changes in government legislation and the very competitive nature of the business itself. I would expect that these operations would have their own performance and profit targets that are completely divorced from the other two operations. It is opportune for me to point out, at this time of the gas crisis in West Australia, that we could have a similar supply situation within the petroleum industry if say we had an international incident, terrorist event or aggressive neighboring country, or if adverse weather was to affect a couple of tanker deliveries. If an unexpected situation such as these arose, there could definitely be supply issues especially in WA as we only have one refinery and because of the highly competitive nature, we as an industry are mostly running on empty with not a great deal of surplus storage at the retail or wholesale level.

Unfortunately, most people are conditioned by the media to view the purchase of fuel for their car as the most important economic decision of their week. I believe we need to become a bit more mature than that and see petroleum for what it really is; a diminishing energy source that is currently a vital cog in most economies of the world and the basic cost of the product the world over, only really varies according to currency variations and government taxes and charges, which in Australia is at the higher end of the scale when compared to the rest of the world. I believe that refineries are currently able to attain a healthy profit margin for no other reason than the law of supply and demand, in Australia the oil companies buy crude oil at the ruling barrel price and sell to the Australian market at the current Singapore spot price, this is because of the legislated parity pricing regime that we have in Australia. Currently demand is extremely high because of the growing economies of China and India, we therefore have a situation that exists whereby even though the barrel price is high, local refineries are still able to make a reasonable profit because of government policy. This situation has only been the case for the last couple of years and could turn the other way in a heartbeat, I believe there is a refinery being built in India that once completed will be able to handle as many barrels a day as all our current refineries put together

Reseller

Across Australia there are a number of reseller operations that not only sell fuel to wholesale customers, government departments, airline companies and the like but also compete in the retail markets alongside the oil company run sites, supermarket chains, independent dealers and franchised dealers. In the late seventies and early eighties there were hundreds of these resellers around the country with at least one in every town with a district population of over 350 people. Due to the costs, a lot of these resellers have disappeared and there now tends to be resellers operating out of major centers and servicing a lot larger territories. The reason I believe this is relevant to the message I am trying to convey is that we had a lot of little fuel depots around the country that would generally have a minimum of two weeks fuel on hand for their respective customers. Nowadays some of the bigger depots would not have a week's storage on hand to satisfy the need and demand of their customers. Some of the current day resellers operate multiple retail sites and are following the trends of the industry, in that they are targeting the convenience market with a modern retail offer as well as running promotional programs. There are however a large number that still offer a basic fuel retail offer that has no shop just fuel bowsers that are either manned by office staff at the local depot or they may have an automatic card reader where there is no human interaction for the whole transaction. These operations are mainly in regional or county centers. The impact of these operations in some markets is to put downward pressure on pump prices because they would generally have lower operating cost

Retail

The petroleum retail market in Australia is very dynamic and unique in its own right, in that most sites in Australia are able to trade 24 hours a day seven days a week if they so choose or if required to if they are operating under a franchise agreement. The industry is forever moving ahead to try to find new profit centre's as in a lot of the sites selling fuel is at best cost recovery only or in a lot of cases a lost leader. This would be the only industry in Australia where the major product of the business is sold under these terms. The fact that sites are able to trade 24 hours has enabled the business to develop a true convenience offer where you may pick up a loaf of bread at 10:30 pm at night or a bottle of milk at 4:30 am in the morning, in some locations even a battery for your car but most importantly, in an emergency situation; a tank of fuel if you need one in a hurry. The sites that operate 24/7 will generally have a higher turnover than those that don't, they would however have much higher operating costs. There are a number of different players in this segment that all operate under different models, and terms and conditions and this is where public perception about the pricing of fuel is so wrong and the reason why regulators and the media all get up on the soap box without actually having any idea of how the industry operates.

The most important point that is not understood is the way fuel is sold at the wholesale level where I assume there is various pricing structures and because of legislation that deals with price collusion within Australia, we as dealers can only assume about wholesale pricing but some things would be very obvious and different models of operation within the retail sector would purchase at different prices, of which I will point out the obvious, that this is some of the reason why you have people misunderstanding pricing variations at the retail level. Resellers operating within the retail market may choose to use some of their reseller margin to offer a cheaper price to the public. This margin could be part of a margin that is allowed for upkeep of equipment, advertising, marketing, brand or cost. To do this 365 days of the year would not be sustainable but could be used in different periods to gain short term market share or in worse cases hold onto market share against an aggressive competitor.

Independent Retailers

Prior to changes in legislation that lead to the current clean fuels policy, a lot of independents were sourcing their product out of Asia cheaper but not as clean as the local product but sold to the same market that was offering to the public a superior product, that cost more to produce. However, the majority of public perception was then as it is now; that a litre of fuel is a litre of fuel and barring transport cost the price should be the same wherever it is sold, this unfortunately will never be the case. In the current market there are several different models of independents from the larger size such as Gull in WA to single site operators that operate under supply agreements from major oil companies. Once again I would assume that dealers operating under a supply agreement would buy fuel cheaper than Franchised dealers, as they more than likely would be paying for the maintenance of their own dispensing equipment as well as their underground storage and the buildings that they operate out of, as with the reseller they would probably use some of that margin to gain or hold market share at different times by discounting to the public

Most of the independents have also increased their shop offer to try to generate non fuel profits they also have to contend with an ever shrinking retail margin on fuel products. Supermarket Chains, are the latest entrant into the fuel retail market and probably the ones that will cause the demise of most of the small service stations across Australia. Coles entered the market with the purchase of the Shell network in the late nineties and operate under the Coles Express brand, they were soon followed by Woolworths who operate their own sites as well as a JV operation with Caltex, these sites are branded Caltex Woolworths and this was followed by IGA doing a shop a docket deal with Peak. I am not sure on exact figures but I believe that between Coles and Woolworths, they would now have 50% or better market share in Australia, in the business petroleum retailing This has been achieved through aggressive pricing and the shopper docket scheme which to my amazement the public have been and are still being, with the assistance of FuelWatch in WA, absolutely conned. Most of the Woolworths sites are very high volume fuel sites with not many ancillary services added to the store offer and in a lot the stores customers queue up to first of all get to the pump and also to pay at the end such is the power of the perceived value in the four cent per litre discount and some times higher, as they are regularly giving fuel discounts for liquor purchases.

For the past five years in WA the public have been conditioned by the media to expect that food prices are going to rise for various reasons and at the same time have been bombarded with negative messages about the fuel industry and fuel prices. It is not hard to work out the way the shopper docket is commercially viable for the big supermarket chains. The average suburban car that is probably filled up once a week to 60 litres gets a discount four cents per litre saving \$2.40, it is not hard for the supermarket chains to get that back as they are all operating shop a docket schemes and it is no surprise to me that in that last five years most of the fresh product range in the supermarkets have risen in price, in some cases ten times the CPI rate. During this period most primary producers have had their prices reduced because of the market power of the supermarket giants. This I know to be true as I operate a small vegetable plantation in Carnarvon WA and the old rule of supply and demand is not always the way business is done, if any regulator cared to check in the right places instead of turning a blind eye to what is going on something would be done about this.

In the current market in WA, Woolworths are currently selling diesel in several locations at up to 10 cents per litre below the cost of a lot of their competitors. I know this to be true as I operate one site at Kalgoorlie and one at Busselton and it has been happening there for some time. In the metro market Woolworths may also have a retail price difference of up to 2 cents per litre between their own sites and the sites that they operate in the JV with Caltex, as Woolworths set the board price in these sites that are mostly run by franchisees with a fuel commission agency agreement. There may even be a case of predatory pricing but as a person involved in the fuel industry you learn to accept that you will get no help from the regulators as they will say this is good for competition.

Company Operated Sites

In today's market in WA, Caltex operate a large number of sites mainly contained within the metro area as well as some down the southwest corridor. These sites are generally very modern with a big focus on convenience retail with products as diverse as a gourmet sandwich to a premium brand of chocolate. Across Australia, the combined Caltex retail network is recognised as the market leader with around 32% market share of the convenience sector. With the abolition of the PRMF act and the introduction of Oil code there is now no limit to the number of sites that an oil company can operate themselves and to this end, in WA we witness BP and Caltex expanding their network of company run sites, this and the fact that Coles already run their entire retail network with I would assume the ability to set the retail price right across Australia being able to be authorised by a very small number of people and with the aid of market intelligence supplied by a national fuel watch scheme be very easy for a situation to develop where then information posted on fuelwatch could be used in a way that would not necessarily give the public true competition

Franchise Sites

When talking about this channel I do so from my own perception as a Caltex Franchisee perspective, as we are really the last surviving major oil company franchise network. Our last model of operation was a royalty based franchise underpinned by buying Caltex fuel and participating in the Caltex Shop Programme; our buying price determined by the daily CRP price and in most markets selling to the public at a price that for most of the time is sold below our actual cost, with price support assistance from Caltex to be able to match our various competitors. There are several reasons for this some I have already alluded to. Not every litre of fuel at wholesale is sold at the same price, also with Caltex the Franchisor we pay a premium for the Caltex brand as well as marketing and equipment costs and as independent business people we have to weigh this up as against say operating your own freehold site or an independent business with little or no brand recognition. There are also some other reasons that come into consideration, for example Caltex the Franchisor may be tied to a particular site with a head lease deal and a change in circumstance (new competitor or a road layout change) could affect that sites economic viability necessitating a price structure to hold volume to maintain shop sales. Both the Caltex operated and franchise sites compete vigorously with each other as well as all other players in the market.

What I have tried to demonstrate with this submission is the simple fact that there is a mistaken belief amongst the public, that every litre of fuel sold in this country is the same product with the same cost to everybody that is retailing and therefore the markets should not behave as they do. When the fact that they do behave as they do clearly demonstrates that at the retail level there is definitely intense competition and a national FuelWatch scheme will have no impact on the price fuel is sold at, just the same as it has had no real impact in WA. Testimony to this is the fact that we still have a big price difference between metro and country and we still have price cycles.

What also needs to be recognised is that in WA, market intelligence is very easily obtained, simply log on to FuelWatch see what your competition is doing and if they have moved their price up or down make your decision. Previous to FuelWatch you had to actually leave your site to see what competitors were doing. I have heard stories of dealers prior to FuelWatch phoning their fuel companies with bogus claims of a competitor moving the price down so bingo that dealer gets a rebate, discount or price support and he is the cheapest in his area until the next dealer cottons on and does the same thing. Nowadays that does not happen as one person with the help of FuelWatch could keep an eye on retail price movements in multiple markets just by going online so I suspect that the oil companies actually like FuelWatch as it guarantees them accurate market intelligence. With the number of independent players participating in the industry dwindling, by way of unfair competition especially from the supermarket chains, you could with the help of a poorly legislated and implemented FuelWatch scheme such as the one in West Australia and the

lack of transparent TGP, be delivering the power to less than a dozen people, the ability to set the daily price for fuel in the mass markets of New South Wales and Queensland.

When talking about fuelwatch and the possibilities that it could be good for competition in that it may lead to downward pressure on prices regulators need to take all of the above into consideration as I have tried to demonstrate that there are a lot of reasons that determine the retail price of fuel in this country.

There should also be some consideration to some of the other influences at play that effect the price of fuel such as the effect of the gst on fuel put simply when a litre sold for a dollar the revenue for government was 09 cents per litre on top of excise, with the current prices heading above \$1.60 per litre that has now risen to over .14 cents per litre.