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APCO SERVICE STATIONS PTY LTD - BACKGROUND AND HISTORY

APCO commenced as an Independent in the late seventies. Over the years it has taken supply from a number of companies including Mobil, Amoco, BP, Ampol, Caltex and Shell. We currently have supply from Mobil and Shell. We now operate 19 outlets with 2 others in the planning and permit stage. All sites are in Victoria except one located in NSW. All sites are high volume with large convenience stores. Some sites are associated with car washes and fast food chains. Our total volume is in the vicinity of 170 million litres per annum. The majority of our sites are in country Victoria and we play a significant role in keeping petrol prices competitive in the rural areas. We have the reputation of a strong discounter and our policy is to use fuel as a basis for high foot traffic for our stores. Sufficient to say that survival today is utterly dependent on convenience store sales.

My experience in the industry extends 45 years; originally working for the Mobil Company then as a distributor in Warrnambool until our move into the retail sector. We are a major Independent retailer throughout Victoria with a vast knowledge of how the industry works. Both my sons are in the business and their collective experience covers at least 40 years. Our reasons for making this submission are our long term survival in the oil industry and our concern over the massive exodus of Independents in recent years. Victorian Independent retailers that have exited the industry are Liberty retail, Better Choice, Citi-Fuel, Oasis, Swift, and United Retail totalling some 100 retail independent sites. Without question the major reason for the diminishing independent retailer is the impact of the predatory supermarket discount docket which has destroyed genuine competition. It should be of major concern that many of the independent sites have gone to the supermarkets. Under the current structure petrol has been prostituted with the margins being confused and hidden.

I will endeavour in this submission to explain the relevant issues covered in the ACCC Inquiry paper. Naturally our submission will be relative to the Victorian market where our experience has been obtained.

THE CURRENT STRUCTURE OF THE INDUSTRY - REFINING AND IMPORTING

The refining capacity of Australia has seen little change over my lifetime in this industry. The last refinery built was in the sixties by Amoco. There have been upgrades over the years but they have not kept pace with the demand resulting in a great reliance on imports. The capacity of the Mobil refinery was I believe reduced from 120,000 barrels a day to 80,000 in the past couple of years. This may be offset by an increase at the Shell refinery presently under way. Of great concern however is the possible closure of the Mobil refinery in Altona. Rumours have been circulating re this for some time since the merger with Exxon. Should this happen Victoria would become more dependent on imports and the resulting tightness of supply would impact on price. The age of existing refineries must be of concern particularly in relation to the new Asian facilities which have capacities far in excess of those in Australia. The closure of the Mobil refinery would I am sure lead to their exiting the retail market which is unprofitable under the present structure. The impact on supply to Independents such as APCO would be serious.

The Major oil companies are the largest importers and to my knowledge the only other significant importer is Trafigura which is based in Sydney and has now exited the Melbourne market. The fact was that they were never competitive with the Majors.

The storage capacity in Victoria is very limited although the Hastings terminal may now be available for operation. It would not be in Victoria's interest for this terminal to fall into the hands of the Majors. There has been no fuel imported by Independents in recent years. Importing of fuel is also impaired by the present Australian Fuel standards and the availability of product to meet the necessary specifications.

There is little doubt that Victoria is badly in need of an importer that has the capacity to be competitive with the Majors. However with the demise of so many Independents it may be debateable whether there is now sufficient volume to ensure a long term supplier. A survey would be necessary to ascertain the market potential. The continued prostitution of petrol will continue to reduce the number of Independents because of their inability to compete against the supermarkets with their discount dockets.

Without doubt the Supermarket discount docket system has inflated the price of both petrol and groceries. At the same time it has also increased the highs of the price cycle. Why this system is not considered third line forcing mystifies many operators in the market. Over 50% of Independents in Victoria have exited the market with the greater % of these sites going to the supermarkets. It is a recipe for long term disaster for the consumer. The alliance of the two Oil Company Majors with the supermarkets has achieved what the Majors could not do; that is the demise of the 'true' Independent.

APCO purchases all of its requirements from both Mobil and from Shell ex the refinery at Terminal Gate Price. There is no importer available as an alternative. Even if that was the case we would still be cautious re long term supply which has in the past been our security and the reason we prefer to deal with a Major.

Frankly however it must be obvious that over the years refinery profits have been inadequate and as a result we now have facilities that are substandard to rest of the world and profits are not sufficient to support the level of maintenance required to meet today's standards. It should also be obvious that retail profits have not provided the level of profit needed. As a result two Majors have vacated the market by alliance strategies with the supermarkets. We note the Mobil Oil Company has disposed of most distributorships and exited the Western Australian retail market. It is possible that a further Major could exit the Australian market because of its' unprofitable nature and the inability to compete with the discount docket. These facts alone contradict all the political hype that surrounds petrol pricing. There are no excessive profits being made; in fact the opposite is causing the massive exodus from the industry.

THE RETAIL MARKET

I note the various operating structures defined by the ACCC. The classification of Independents selling under the refiner marketer brand brings no influence into the market. I do not believe these operators can be classified as a 'true' Independent;

1. They use the brand of the Major as a drawcard.
2. They receive significant capital investment from the Refiner (eg pumps, tanks, signage, etc).
3. They rely significantly on the company Fuel card for a major part of their volume.
4. Most purchase at a discount from the terminal gate price.
5. Supply deals may also include price support which by its' nature is a form of price control.

It would be fair to say they have a reduced investment in the industry and are completely dependent on the Oil Company. There is also reluctance by the Majors to supply a branded Independent like Apco. We have first hand knowledge of this reluctance. Fortunately both Mobil and Shell take a different approach.

To survive in today's market it is essential that fuel sales are backed up by top class convenience stores, car washes and fast food tenants if possible. In the last 5 years other sources of income have outstripped petrol income on our sites. Lower volumes due to the loss of the discount market (note this was the Independents bread and butter) have necessitated these changes. Those retailers that have not had the capacity to invest in other non-fuel income streams due to financial constraints are now very vulnerable.

The impact of the changes to the Sites Act of the Oil Code has not been of any benefit to our company in fact, we believe it has had an effect of further reducing competition.

TERMINAL GATE PRICE

The original objective in setting the T.G.P. has never been achieved. The concept originally was to set a price available to all customers in the market. The principle originally proposed that various benefits granted to T.G.P. customers would attract an add on price. For example:

1. Cartage to point of delivery at a cost plus freight with add ons for part tanker loads etc.
2. A terms cost as compared with those paying cash etc.
3. A cost to cover any Oil Company investment of equipment, pumps, tanks, signage, etc.

As an example for a Major account such as Coles, which currently purchase at a discount below T.G.P;

1. They would enjoy significant terms; possibly 30-60 days.
2. Their product is delivered to the site by the Oil Company.
3. They at this stage rely on existing equipment.
4. Provided with price support at the Oil company's discretion

As an Independent we purchase at T.G.P., pay cash (terms are available at a cost) and pick up deliver our own product to our sites and also provide and maintain our own equipment and the capital cost of the service station.

As a true Independent we impose no add on costs to a Refiner. The profit made by the wholesaler at T.G.P. is therefore much higher compared to the selective deals with certain accounts. In simple terms Independents such as APCO subsidise the prices to preferred accounts. The T.G.P. is the maximum price that can be achieved – whereas it should be the minimum to all comers for cash.

A further component here is price support (PS). Usually P.S. is not a contractual arrangement but purely a gentleman's agreement. By its very nature P.S. is predatory as it gives much greater margins to those who already have a preferred arrangement. A much fairer way would be to give P.S. at the gate to everyone. P.S. in addition to preferred account discounts result in a higher T.G.P. subsidised by the smaller players. In addition it provides a form of retail price control by the Oil Company.

The competition for the business of Independents has ceased to a great extent since the supermarkets entered the industry. In the past players such as APCO could command a fair wholesale price off what was called the List Price (now T.G.P.) that price was to compensate them for their investment in the industry. This is no longer the case and both price and product is generally unavailable, unless by an existing arrangement. Approaches for supply are generally refused on the basis of no available product and if available only at T.G.P.

Add the above problems to the retail price posted by the Independent, matched by the subsidised price of the preferred account with a further discount docket and it is obvious that most Independents are in trouble if they cannot access other areas of income.

The level playing field does not exist in the Industry and no protection is provided to those who risk all in the trade. Certainty of supply should be a right. No wholesaler should be able to refuse supply at T.G.P. which should be the cash price. Present legislation does not.

A full enquiry into price support should be conducted and the long term consequences of its unfair advantage given serious thought.

While it may appear on the surface to add to competition – it is clearly obvious in the market that it is discriminative. On page 21, section 3.10 of the Senate Report comment is made upon the ability of the retailer to compete and acknowledges that it depends on his ability to access the lower price and conditional price support. I would contend that the market presently does not provide this competition to Independents.

Our opinion on this is supported by the M.T.A.A. see Senate Report page 37 section 4-11.

In answer to the questions raised by the ACCC – retailers cannot really negotiate prices – nor can they readily change supplier because of the lack of supply. The supply is controlled and there is no surplus to be disposed of.

The simple result is that all of us depend entirely on our present supplier and cannot purchase elsewhere.

THE PRICE CYCLE

The price cycle in Victoria has been in action for up to 15 years, probably triggered in its early days by Independents such as Solo then Liberty in establishing their brands. Picked up by other independents that endeavoured to attract the discount customer, it accelerated in the mid 90's. Oil companies joined in to curtail the volume losses to the Independents. The basic problem with the price cycle is that it reaches unsustainable lows on the board price that need to be recovered at the top. The result of course is an excessive price at the top end of the cycle.

With discounting now being controlled by the supermarkets and the inability of the Independents and the two Majors to match the discount docket, prices are not going to the previous lows as no advantage can be gained in the market. At the higher end of the market the cycle remains in an endeavour to lower the 4cpl advantage of the discount docket. There is no doubt however that it has impacted at the top of the cycle as the supermarkets and Majors endeavour to recover the 4cpl. I note in the Senate Report page 48 section 4.55 a quote that the supermarket share is 40%, not sure how that was arrived at but it is far in excess of 40% as other sources claim it to be in fact as high as 60%.

One would have to be naïve to believe that the docket has not affected grocery prices. In section 4.64 page 50 the Senate questioned Mr McMahon of Coles Express re their selling of fuel below the wholesale (T.G.P.) price. His answer is utterly misleading. Greater volumes if sold below cost only increase the losses unless they are heavily subsidised below the gate price and also receive price support. His answers re transactions in their convenience stores are also questionable. It is common knowledge from suppliers that the convenience stores of the Coles/Shell chain have fallen significantly. Also our experience has proven without doubt that queue's for fuel impact detrimentally on store sales.

Losses on fuel at the lower end of the cycle can only be recovered by an increase in price of groceries or by a higher price at the top of the cycle which has now been achieved. There is little doubt that the consumer is now paying far more at the top than in the past.

I am sure that it would be far better to sell fuel at a price average of the cycle as APCO does in many country areas avoiding the extraordinary highs.

METHODS TO ADDRESS THE CURRENT NATURE OF THE MARKET AND TO IMPROVE COMPETITION

1. A level playing field needs to be established at the terminal gate.
2. Price support should be passed to all accounts if necessary at the T.G.P. or outlawed as discriminative (in theory this should lower the T.G.P.)
3. More competition needs to be introduced for the Independent market (eg. Supply should not be refused by any Refiners).
4. Ensure that the T.G.P. is fully transparent to all players.
5. Selling below cost or alternatively the T.G.P. should be considered predatory and likely to reduce competition.
6. Appointment of an ombudsman with experience in the industry and the power to resolve differences.

In presenting this submission we would appreciate the opportunity to be consulted on this matter. As a significant Independent player with extensive industry experience we believe we can contribute far more than documented in this submission.

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