



Public Competition Assessment

6 November 2018

BP Australia Pty Ltd - proposed acquisition of Woolworths Limited's network of retail service station sites

The ACCC's decision

1. On 14 December 2017 the Australian Competition and Consumer Commission (**ACCC**) announced its decision to oppose the proposed acquisition by BP Australia Pty Ltd (**BP**) of Woolworths Limited's (**Woolworths**) network of retail service station sites (the **proposed acquisition**). This Public Competition Assessment outlines the reasons for the decision.
2. The ACCC considered that the proposed acquisition would be likely to contravene section 50 of the *Competition and Consumer Act 2010* (the **Act**).
3. Section 50 prohibits acquisitions that would have the effect, or be likely to have the effect, of substantially lessening competition in any market.
4. The ACCC considered the competitive effects of the proposed acquisition in the following markets:
 - city-wide markets for the retail supply of petrol in metropolitan areas, such as Melbourne, Sydney, Brisbane, Perth and Adelaide
 - local markets (typically around 3km to 10km in radius) for the retail supply of petrol in the vicinity of each Woolworths site.
5. The ACCC issued a substantial number of notices under section 155(1)(a) and/or (b) for information and documents and conducted a large number of examinations as part of this in-depth investigation. The ACCC undertook extensive pricing data analysis, document review and consultation with market participants in reaching its decision.
6. The ACCC found that Woolworths was a vigorous and effective price competitor in petrol retailing and, as a result, exerted competitive pressure on petrol prices in city-wide and local markets. The ACCC also found prices at BP controlled sites were typically significantly higher than Woolworths' prices in the major capital cities. The ACCC formed the view that post-acquisition, BP would be likely to apply its own pricing strategy to the Woolworths sites. As a result, prices

at the Woolworths sites would likely increase if BP acquired them and other petrol retailers would be likely to face less competitive pressure. The ACCC concluded that motorists would be likely to end up paying more for petrol if the acquisition occurred.

7. The ACCC considered that the proposed acquisition would likely affect metropolitan petrol price cycles by making the price increases quicker and more coordinated and by reducing the pressure to discount, with prices not falling as far, or as quickly.
8. The ACCC also considered that competition would be substantially reduced in a number of local areas where BP and Woolworths sites overlap.
9. BP offered an undertaking to divest sites to seek to address the ACCC's competition concerns. Whilst the divestments proposed by BP would have largely addressed the ACCC's specific local market concerns, the ACCC did not consider the divestments would have been sufficient to remedy the city-wide competition concerns.
10. Throughout this Public Competition Assessment, references to market participants and analysis reflect the information obtained by the ACCC in the course of its investigation in 2017 and considered in its decision of 14 December 2017.
11. Please note that this and other public competition assessments are subject to the following qualifications:
 - the ACCC considers each transaction on a case-by-case basis and so the analysis and decision outlined in one assessment will not necessarily reflect the ACCC's view of another transaction, even where that other transaction may involve the same or a related market
 - as assessments are brief and do not refer to confidential information provided by the parties or other market participants, assessments do not set out all of the issues and information considered by the ACCC, nor all of the analysis and reasons of the ACCC.

The transaction and parties

The transaction

12. BP proposed to acquire Woolworths' network of retail service station sites, comprised of 531 sites and 12 sites under development located throughout Australia.
13. If the proposed acquisition proceeded:
 - Woolworths' wholesale supply arrangement with Caltex would have been terminated
 - BP and Woolworths proposed to enter into an ongoing retail convenience, shopper docket discount and customer loyalty partnership (the Commercial Alliance).

14. Under the Commercial Alliance:

- BP and Woolworths would have established a pilot program to roll out the *Metro @BP* retail store format. *Metro @BP* stores would have combined BP's retail fuel assets with Woolworths' grocery and food retailing expertise, and was intended to allow BP to sell a variety of food and meal options to consumers. If the pilot program was successful, BP proposed to roll out the format to more than 200 sites.
- Woolworths' shopper dockets would have been redeemable at certain BP Sites, including the sites BP acquired from Woolworths, pre-existing BP company-owned company-operated (**COCO**) sites and some sites operated by BP dealers. This discount would have been partially funded by BP and partially funded by Woolworths.
- BP would have joined the Woolworths Rewards Loyalty Scheme as a key partner. Consumers would have been able to earn and redeem points on fuel and convenience store purchases at BP sites participating in the Woolworths Rewards Loyalty Scheme.

15. Separately, BP and Woolworths applied for authorisation to implement the Commercial Alliance. The ACCC granted those applications for authorisation subject to conditions on 14 December 2017. However, the authorised conduct would have only occurred in the event BP acquired Woolworths' network of service stations. The ACCC notes that on 21 June 2018, BP announced that it would not be proceeding with the proposed acquisition.

The parties

The acquirer: BP Australia Pty Ltd

16. BP (with its related entities) is a vertically integrated refiner-wholesaler of petrol, diesel and automotive liquefied petroleum gas (**LPG**). It is engaged in the exploration for and production of oil, natural gas and LPG and the refining, transportation and marketing of petroleum and lubricant products.
17. At the time of the investigation, BP supplied fuel to approximately 1,400 BP-branded service stations throughout Australia. Of these sites, BP controlled the day-to-day retail price of all fuels at approximately 369 sites. This included approximately 334 of BP's own network of sites referred to by BP as 'company-owned-and-company-operated' (**BP COCO**) and approximately 35 'commission agency' sites (**BP CA**). BP does not set the day-to-day retail price of fuel at the other BP-branded sites, except for diesel at 33 'diesel commission agency sites' (**DCA**).

The target: Woolworths Limited's network of retail service station sites

18. Woolworths entered fuel retailing during the late 1990s, establishing service stations that offer fuel discounts to those purchasing groceries at Woolworths supermarkets.

19. In August 2003, Woolworths entered into an alliance with Caltex Australia Group (**Caltex**) to operate dual-branded (Caltex/Woolworths) service stations. These dual-branded sites are operated by Woolworths and obtain all fuels from Caltex. At the time of the ACCC investigation, Woolworths operated 531 sites and had a further 12 sites in development. There were also 104 Caltex/Woolworths sites operated by Caltex.
20. The ACCC estimated that BP branded sites and Woolworths sites together made up approximately 27 per cent of all sites in Australia. Approximately 14 per cent of all the sites in Australia were BP dealer sites (third party owned and operated petrol sites which on-sell fuel supplied by BP under the BP brand) and the remaining approximately 13 per cent of sites were directly controlled by BP or Woolworths.

Review timeline

21. The following table outlines the timeline of key events for the ACCC in this matter.

Date	Event
15 March 2017	ACCC commenced a public review under the <i>Informal Merger Review Process Guidelines 2013</i>
14 April 2017	Closing date for submissions from interested parties
10 August 2017	ACCC published a Statement of Issues
7 September 2017	Closing date for submissions from interested parties on Statement of Issues
19 September 2017	ACCC published preliminary screening of local markets
28 September 2017	Closing date for submissions relating to local market screening
14 December 2017	ACCC decision to oppose the proposed acquisition

22. The total elapsed time from start to finish was approximately 9 months. The total period net of time taken by the parties to submit information or documents and delays requested by the parties was 130 business days.

Market inquiries

23. The ACCC conducted extensive market inquiries with a range of industry participants, including motoring groups, industry associations, competitors and both corporate and individual consumers. Submissions were sought from all of these market participants.

Statement of Issues

24. On 10 August 2017, the ACCC published a Statement of Issues on the proposed acquisition identifying a number of competition issues. In the Statement of Issues, the ACCC stated its preliminary view that the proposed acquisition may substantially lessen competition in retail fuel markets by:
 - removing a strong competitor in fuel retailing with a distinctive competitive strategy

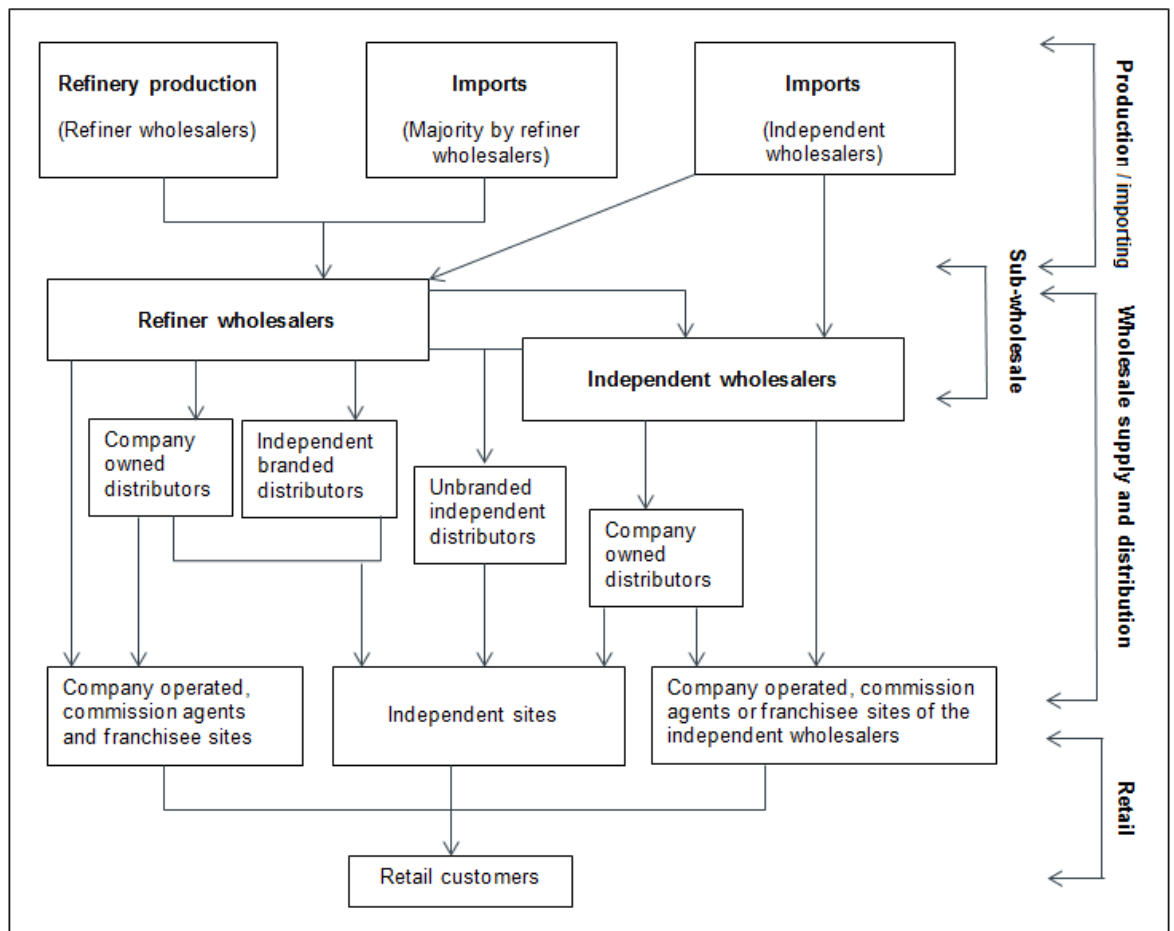
- replacing the more competitive pricing strategy currently used at Woolworths sites with a strategy that tends to increase retail prices earlier in a petrol price cycle, discount later and discount less deeply
 - enabling the remaining fuel retailers to more effectively co-ordinate price increases during the 'restoration' phase of petrol price cycles.
25. The ACCC was also concerned that the proposed acquisition may substantially lessen competition in convenience groceries, through the amalgamation of BP and Woolworths' forecourt convenience offerings.
26. In addition, the ACCC indicated it would publish a preliminary analysis of local retail fuel markets likely to raise competition concerns, and it did so on 19 September 2017.

Industry background

Overview of Australia's downstream petroleum industry

27. Australia's downstream petroleum industry consists of three broad levels – production and importing, wholesale supply and retail supply. This structure is depicted in the figure below.

Figure 1: Australia's downstream petroleum industry



Refining and importing

28. Petrol sold in Australia is either refined from crude oil at local refineries or imported as a finished product from overseas refineries.
29. There are currently four refineries operating in Australia (down from eight in 2003). They are owned and operated as follows:
 - Corio, Geelong (Viva Energy)
 - Kwinana, Perth (BP)
 - Lytton, Brisbane (Caltex)
 - Altona, Melbourne (Mobil).
30. These four companies also operate in wholesale markets and are known as 'refiner-wholesalers.'

Wholesale supply

31. Wholesale supply is dominated by the four refiner-wholesalers and large independent wholesalers including United and Puma Energy. The refiner-wholesalers supply wholesale petrol to their own outlets, as well as to independent wholesale distributors and retailers (including Woolworths and Coles Express).
32. In 2013-14 (the latest data available), the four refiner-wholesalers supplied over 90 per cent of wholesale petrol volumes in Australia.
33. BP supplies wholesale fuel to its COCO sites, independent BP dealer sites and independent wholesale distributors.

Retail supply

34. At the retail level, service stations supply fuel to retail customers. Service stations can be:
 - supermarket operated sites (Woolworths or Coles Express)
 - refiner-wholesaler COCO sites, where the refiner-wholesaler sets retail prices
 - refiner-wholesaler commission agent sites, where the refiner-wholesaler typically sets retail prices
 - refiner-wholesaler franchisee sites, where typically the franchisee sets retail prices, but this may be influenced by wholesale pricing terms from the refiner-wholesaler
 - refiner-wholesaler branded but independently operated sites, where typically the independent operator sets day-to-day retail prices

- independently owned and/or operated sites which range from large independent chains to single-site operations (these may be operated on a COCO, commission agent or franchisee basis).

35. A given site may fit into more than one of these categories.

Other industry participants

Caltex

36. Caltex's business operations include the refining, wholesaling and retailing of transport fuels.
37. Caltex's operations include the retail supply of fuel through its COCO service stations. There were over 1,400 Caltex branded sites across Australia, of which Caltex or its agents operated around half.

7-Eleven

38. 7-Eleven has been retailing fuel since the late 1970s.
39. In 2010, 7-Eleven purchased a large number of retail service stations from ExxonMobil, which significantly lifted its presence in fuel retailing. There were approximately 500 7-Eleven sites across Australia.

United

40. United is an independent, Australian-owned wholesaler and retailer of fuel, and a convenience retailer.
41. United controls terminal facilities in Victoria, New South Wales, Northern Territory and Tasmania which allow it to import fuel from overseas and operate in both wholesale and retail fuel markets in Australia. There were approximately 500 United branded retail sites across Australia (including some operated independently of United).

Coles Express

42. Coles has been retailing fuel since mid-2003, following a commercial alliance with Shell Australia (now Viva Energy Australia Ltd), under which Coles became the owner of franchisee-operated dual-branded service stations Australia-wide.
43. There were approximately 700 Coles Express sites throughout Australia.

BP dealers

44. BP dealers are third party owned and operated petrol retailers which on-sell fuel supplied by BP under the BP brand. BP dealers set their own retail prices for fuel and negotiate their own commercial contracts with non-fuel suppliers. They have access to a buying group, provided by BP, for convenience products.

Other fuel retailers

45. Other major fuel retailers include large regional or single-state retail chains. These include:
- Peregrine, which operates as “On The Run” in South Australia (approximately 130 sites)
 - Freedom Fuels in Queensland (approximately 50 sites)
 - Puma which operates nationally (approximately 400 branded sites, including 260 operated by Puma)
 - Metro Petroleum in the Eastern States (approximately 200 branded sites, including about 120 operated by Metro)
 - Liberty which operates nationally (approximately 100 branded sites).

Retail petrol price cycles

46. Price cycles are a prominent feature of retail petrol prices in Australia’s largest cities. Wholesale prices do not exhibit similar cyclical movements. Price cycles have at least two distinct phases:
- a. a substantial increase in prices that generally occurs across a metropolitan area (the **restoration phase**), and
 - b. a more prolonged phase of decreasing prices (the **discounting phase**).

Restoration phase

47. The restoration phase is generally initiated by one or two of the major retailers increasing prices substantially at a number of retail sites in a metropolitan area. If other retailers respond to this move with similar increases, then the increased price usually spreads across most retail sites within a metropolitan area in a matter of days.
48. Some retailers follow shortly after the first mover raises prices; others take longer to follow the price increase. This is because there is a short-term incentive for individual retailers to delay their price response during the restoration phase of the price cycle, thereby potentially gaining a temporary increase in sales and reputation for low prices. The risk for retailers who delay is that the first mover (or those that follow quickly) may abandon their attempt to increase prices, and return their prices to the previous, lower levels. The longer other retailers delay in following an attempted restoration, the greater the likelihood that the first mover or early followers will abandon their price increase.
49. Generally during the restoration phase, retailers increase prices to the same or a similar price point across different local areas within a metropolitan area.

Discounting phase

50. The discounting phase involves a slower process of fuel retailers undercutting and matching each other's prices on a local basis in small decrements. This process can take a number of weeks.
51. During the discounting phase, the rate at which retailers reduce their prices from the cyclical peak tends to vary on a site-by-site basis depending on factors that include the prices at nearby sites. As a result, during the discounting phase, there will often be a degree of price variability between a retailer's sites across a city.

Relevant markets

52. Market definition establishes the relevant field of inquiry for merger analysis. The ACCC's starting point for delineating relevant markets, to assess the competitive effects of the proposed acquisition, involved identifying the products and geographic regions actually or potentially supplied by the parties to the proposed acquisition. The ACCC then focused on areas of activity where competitive harm could occur as a result of the proposed acquisition. These are discussed below.

Product dimension

53. Three types of fuel products are commonly sold at retail service stations in Australia: petrol (including regular unleaded (**RULP**), premium unleaded and ethanol blends), diesel and automotive liquefied petroleum gas (**LPG**).
54. In this matter, the ACCC did not consider it necessary to assess the proposed acquisition in separate markets for petrol, diesel and LPG. All these fuel types are supplied at most sites, and it is unlikely that the separate consideration of each fuel type would have affected the ACCC's analysis.
55. For simplicity, the ACCC focused on the effect of the proposed acquisition on competition in the retail supply of petrol.
56. In considering future acquisitions of retail service stations, the ACCC may consider it appropriate to specifically consider markets for the supply of any or all of petrol, diesel and LPG.

Geographic dimension

Local markets

57. The ACCC considers that competition in local markets is an important determinant of retailers' pricing decisions, particularly in the discounting phase of the price cycle.
58. The ACCC understands that location is an important factor in consumers' fuel purchasing decisions. Consumers generally have a preference for purchasing petrol from petrol stations located close to their residence, work or along their regular routes of travel.
59. Major retail petrol chains generally set fuel prices at each of their sites centrally (rather than prices being determined by individual site managers). When setting

prices at a site, retailers often monitor the prices at a number of other competing sites in the same local area. These are commonly known as 'marker sites'. Marker sites are frequently located close to the site at which the price is being set, hence local competition is important.

City-wide metropolitan markets

60. While there are areas of close local competition between fuel retailers, it is also relevant to consider the competitive dynamic in petrol retailing across broader geographic markets.
61. In metropolitan areas where retail petrol prices follow cycles, price outcomes can depend on behaviours of fuel retailers across the city. Cyclical price increases typically occur across the city as a whole. In the restoration phase, retailers generally increase prices to the same or a similar point across the city, regardless of differences in local area competition. If a price increase fails to 'stick', it is most likely because one or more major retailers decide not to follow the increase on a city-wide basis, or are slow to do so.
62. The ACCC assessed the likely effects of the proposed acquisition on competition in:
 - retail supply of petrol in city-wide metropolitan markets, and
 - retail supply of petrol in local areas (within metropolitan and regional areas) in the vicinity of each Woolworths site.

Competition analysis

Overview of the ACCC's concerns

63. The ACCC considered there were a range of potential effects that would occur in both city-wide markets and local markets. To this end, the ACCC examined:
 - the removal of Woolworths as a vigorous and effective competitor in petrol retailing, and
 - local impacts arising from common-ownership of a high proportion of sites in a local area.

The removal of Woolworths as a vigorous competitor

Woolworths' competitive pricing strategy

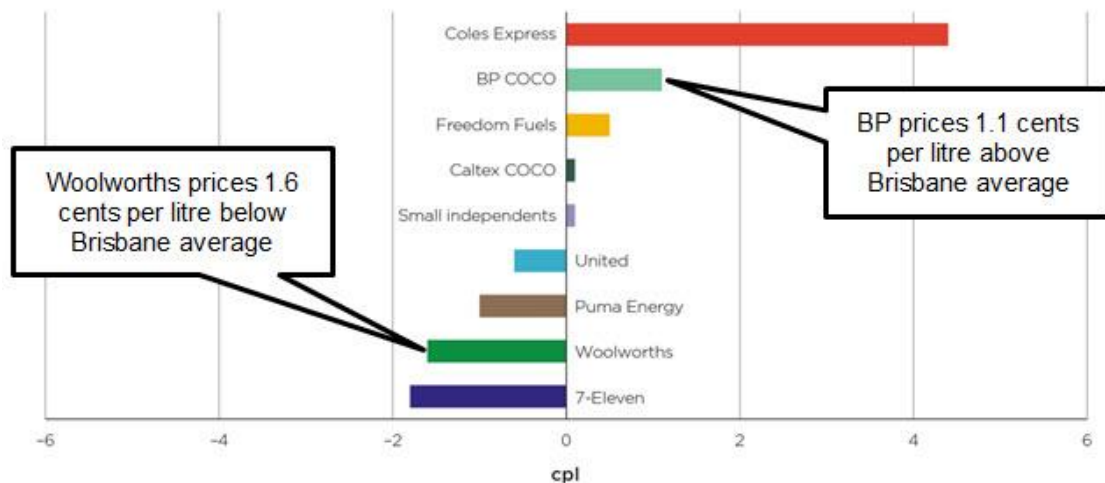
64. The ACCC found Woolworths was a vigorous competitor in petrol retailing with a distinct competitive strategy.
65. Analysis of information, including documents from the parties, indicated that Woolworths' retail fuel business model had a competitive pricing strategy to support its shopper docket offer and drive supermarket sales. In the absence of the proposed acquisition, the ACCC considered that Woolworths was unlikely to change its competitive pricing strategy.

66. The ACCC analysed large volumes of price data and marker site data for petrol retailers (the price data). Based on that analysis the ACCC concluded that, in metropolitan markets, Woolworths was generally a fast follower in the discounting phase of the price cycle, and slower to restore in the restoration phase.
67. Based on those findings and the analysis of other material before the ACCC, the ACCC considered that Woolworths was a vigorous price competitor. Because of the size and scope of its retail petrol network and the volume of petrol it sells, Woolworths had a significant competitive impact on retail petrol markets.

BP's pricing strategy

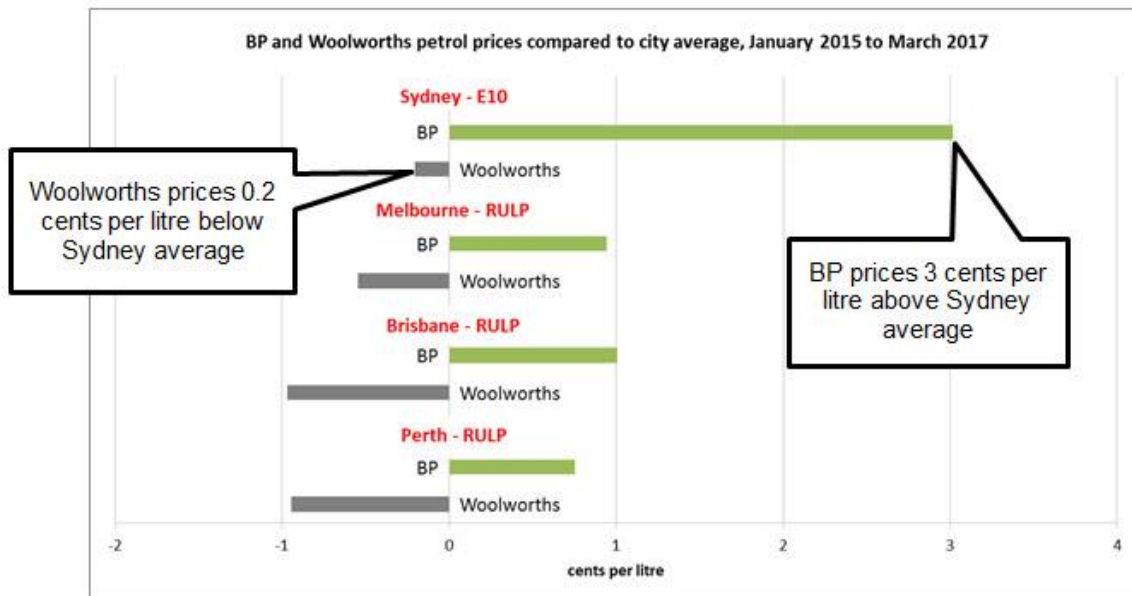
68. The ACCC considered that BP's pricing approach was underpinned by a business model that was different to Woolworths'. BP is a vertically integrated refiner-wholesaler with a large branded dealer network.
69. The ACCC's view after its analysis of the price data was that:
 - BP's prices were on average higher than Woolworths' prices during the restoration phase of the price cycles – reflecting that BP typically (but not always) increased its prices at its sites during price restorations before Woolworths
 - BP's prices were on average higher than Woolworths' prices during the discounting phase of the price cycles. This reflected that BP typically was slower than Woolworths to reduce its prices and did not always reduce its prices as low as Woolworths did at the bottom of the cycle.
70. The ACCC's data analysis was consistent with other material before the ACCC.
71. Figure 2 (published in October 2017 when the ACCC released its study into the Brisbane petrol market) highlighted the difference between BP's and Woolworths' pricing strategies in Brisbane.

Figure 2: Difference between major retailers' average regular unleaded petrol (RULP) prices 1 January to 30 April 2017



72. The ACCC's data analysis at Figure 3 (published in December 2017) made a similar point across each of the major capital cities. BP's prices were on average around 2cpl higher than those of Woolworths.

Figure 3: BP and Woolworths petrol prices compared to city average, January 2015 to March 2017¹



73. The ACCC's view was that the price differences observed between BP and Woolworths did not appear to be driven by particular features of the sites they operated or local factors so much as by BP's and Woolworths' different pricing strategies.

Pricing at Woolworths sites post acquisition

74. Post acquisition, Woolworths would be removed as a competitor from the relevant markets. This would reduce the number of competitors and the competitive constraint on all retailers in local markets and across city-wide metropolitan markets.
75. The ACCC considered that the material before it showed that BP was likely to increase prices at the Woolworths sites post-acquisition by applying its own pricing strategy to the acquired sites.
76. As a consequence, the ACCC considered that the effects of the change in the pricing of Woolworths sites would be substantial given the number of such sites and their significance in determining how competitors price in response.

Slower and lesser discounting

77. During the discounting phase of a price cycle, discounting occurs when one competitor reduces its price at a site and other competitors reduce their prices

¹ E10 is regular unleaded petrol blended with between 9% and 10% ethanol.

either to match the first mover's price or to ensure their price is within a certain differential.

78. The ACCC considered the proposed acquisition was likely to result in less and slower discounting due to, as discussed above, the elimination of Woolworths and its pricing strategy being replaced by BP's.
79. The ACCC found that Woolworths' pricing was an important influence on the discounting behaviour of many other fuel retailers across metropolitan areas and in local markets in which there was a Woolworths site. By following price discounting by other retailers rapidly, Woolworths increased the competitive pressure on retailers to lower their prices.
80. The ACCC also considered that there would be less pressure on other retailers to reduce prices nearer the bottom of the price cycle, as BP did not always reduce its prices as low as Woolworths did.
81. The ACCC found that BP's pricing typically had little influence on the discounting behaviour of many other fuel retailers across metropolitan areas and in local markets in which there was a BP-controlled site.
82. The ACCC concluded that the overall effect of the proposed acquisition would be likely to be higher average prices than would otherwise have occurred.

Faster and more coordinated price increases

83. The ACCC also considered whether the proposed acquisition would be likely to result in faster and more coordinated increases in the restoration phase of the price cycle.
84. The ACCC considered that the acquisition would likely cause the price restoration phase of the cycle to occur earlier (i.e. shortening the discounting phase), to occur quicker and potentially to result in higher prices at the peak. This was the case for three main reasons.
85. First, by removing a large independent competitor, the proposed acquisition would reduce the uncertainty of other retailers during the restoration phase of the cycle. In turn, this was likely to encourage the first mover of the price restoration to move earlier and for other retailers to follow more quickly.
86. Second, the ACCC found that BP was often quicker than Woolworths to increase prices at its sites during the restoration phase of price cycles. A factor other competitors consider when choosing to increase prices at their sites is how many of their rivals have already done so. If BP increased prices at the acquired Woolworths sites more quickly, other retailers would be encouraged to do the same.
87. Third, the proposed acquisition would have significantly increased the retail presence of BP, giving it a greatly expanded network of sites with which to contribute to a restoration, thereby making it easier for the restoration to gain the momentum to be successful.
88. The ACCC considered that prices across metropolitan markets and in local markets were likely to stay at a higher level for longer as part of each price cycle,

and as a result consumers would be likely to have paid higher prices on average for petrol post-acquisition.

Local overlaps

89. Beyond the broader metropolitan-wide markets, the ACCC considered whether the proposed acquisition would have been likely to result in a substantial lessening of competition in any local area where BP and Woolworths sites were both present.
90. Where the parties overlapped in local markets, the competition between their sites would have disappeared. BP could have raised prices after the acquisition, unless there were enough local competitors remaining who would have constrained BP.
91. The ACCC was concerned that there would not be sufficient constraint on BP sites in a number of local areas, many in regional areas, where both BP and Woolworths sites were present.
92. For metropolitan areas or built-up areas, the ACCC tended to focus on competition within a geographic area of approximately 3 kms around each Woolworths site as a starting point, although it had regard to local geography, traffic flows, speed of travel and other indicators, so the boundaries of the relevant local market varied in each case. In regional areas, the starting point was generally around 10 kms around each Woolworths site, due to faster travel times.
93. BP offered to divest a significant number of sites that largely resolved the ACCC specific local market concerns. BP also offered to divest some metropolitan sites to address the city-wide market competition concerns. However, the ACCC did not consider that these divestments sufficiently addressed the city-wide competition concerns.

Conclusion

94. Based on the above analysis, the ACCC concluded that the proposed acquisition of Woolworths' network of retail service station sites by BP would be likely to have the effect of substantially lessening competition in a number of markets, as discussed above.