

FACTS ABOUT THE AUSTRALIAN WHOLESALE FUELS MARKET & PRICES

IMPORT PARITY PRICING & WHOLESALE PRICES

Petroleum fuels (e.g. petrol and diesel) are globally traded commodities, and therefore wholesale fuel in Australia reflects relevant international prices.

Australian wholesale fuel prices are closely linked to the Singapore price of fuel.

- ⇒ According to the ACCC, Singapore fuel prices are the relevant Australian benchmark prices because Singapore is the market that the eastern hemisphere refers to, it is the closest major refining and marketing centre and is a common source of imported petrol to Australia.
- ⇒ To meet Australian fuel demand, around 40% of fuel is imported (mainly from Asia and particularly Singapore).

Australian wholesale fuel prices (including spot Terminal Gate Prices or TGPs) are closely linked to Singapore prices through Import Parity Pricing (IPP).

- ⇒ IPP plays a central role in determining fuel price outcomes for petrol and diesel in Australia.
- ⇒ IPP forms the basis for the wholesale prices charged by major fuel suppliers and consequently, changes in the IPP flow through to changes in wholesale and retail prices.
- ⇒ IPP is a pricing methodology used by major fuel suppliers — very similar to that used by the ACCC when wholesale prices were regulated by government.
- ⇒ The ACCC considers that the use of IPP-based pricing in Australia is appropriate with imports continuing to be the marginal source of supply of refined fuel.

The IPP is the 'landed cost' of refined fuel (e.g. petrol) to import terminals around Australia.

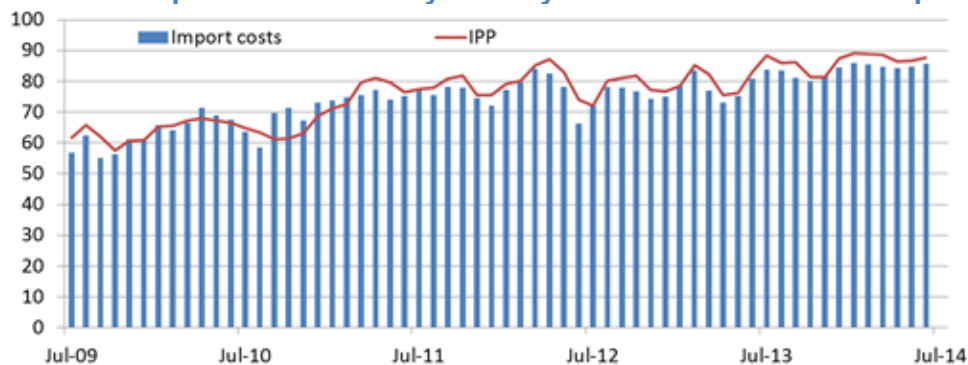
IPP includes:

- ⇒ the benchmark price for refined fuel (e.g. for petrol - MOPS95)
- ⇒ the 'quality premium' for specific Australian and State fuel standards
- ⇒ freight
- ⇒ exchange rate
- ⇒ wharfage, insurance and loss.

The Singapore benchmark price for refined fuel accounts for around 95% of the IPP.

ACCC analysis clearly shows that the actual import costs paid by major fuel suppliers have closely followed the IPP over the past 3 years, with the difference averaging 2.6 cents per litre.

IPP Versus Import Costs Actually Paid By Fuel Wholesalers: Cents per litre



SOURCE: ACCC

The use of IPP, including for sales between major fuel suppliers, provides clear benefits in terms of supply security and economic efficiency, and ensures Australia is not disadvantaged in its ability to access international supplies of crude oil and petroleum products. In addition, with prices set according to IPP, the ACCC considers "*Australian refiners and suppliers have little scope to pass on costs that are out of line with international best practice*".

TERMINAL GATE PRICES (TGPS)

The primary building block of Australian wholesale prices (including TGPs) is the IPP, together with 'wholesaling costs' to store, handle and process the fuel once it arrives in Australia and prior to its distribution to the domestic market.

Thus, wholesale prices equals IPP plus:

- ⇒ government taxes (fuel excise and GST)
- ⇒ terminal capital and operating costs
- ⇒ a small wholesale margin/profit (where competitively possible - see below)

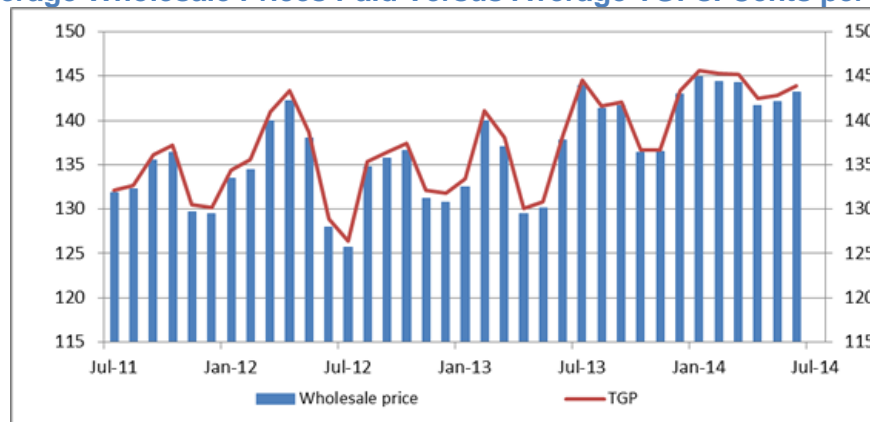
According to ACCC, most fuel wholesalers in Australia build TGPs on the basis of this formula, with the IPP being the largest component which tracks TGP closely.

- ⇒ IPP plus government taxes is almost the entire TGP price (above 95%).
- ⇒ Australian taxes include excise (38 cents per litre) and GST (10%).

Average wholesale prices paid by customers can vary slightly from TGP (averaging 0.7 cents per litre over the last 3 years). According to the ACCC, this variance is due to any volume discounts that might apply to contracted customers and large fuel orders, types of services included in the transaction.

- ⇒ Some wholesale fuel purchasers receive a suite of services with their fuel purchase including delivery, branding and price support. These transactions, according to the ACCC, tend to attract a higher price, compared to the lower prices paid by 'fuel only' customers and contracted customers, and those receiving 'large volume' discounts.
- ⇒ This ACCC analysis is based on their Formal Price Monitoring activities under the Competition and Consumer Act 2010, where they examined, for example, the details of millions of wholesale petrol transactions undertaken by refiner-marketers with other wholesalers, retailers, independent distributors.

Average Wholesale Prices Paid Versus Average TGPs: Cents per litre



SOURCE: ACCC

The TGP typically comprises around 95% of retail prices, but retail fuel prices vary across metropolitan and regional areas reflecting local area factors and competition.

Wholesale market operation and price transparency in Australia is assisted by the publication of Terminal Gate Prices for petrol and diesel by all AIP members.

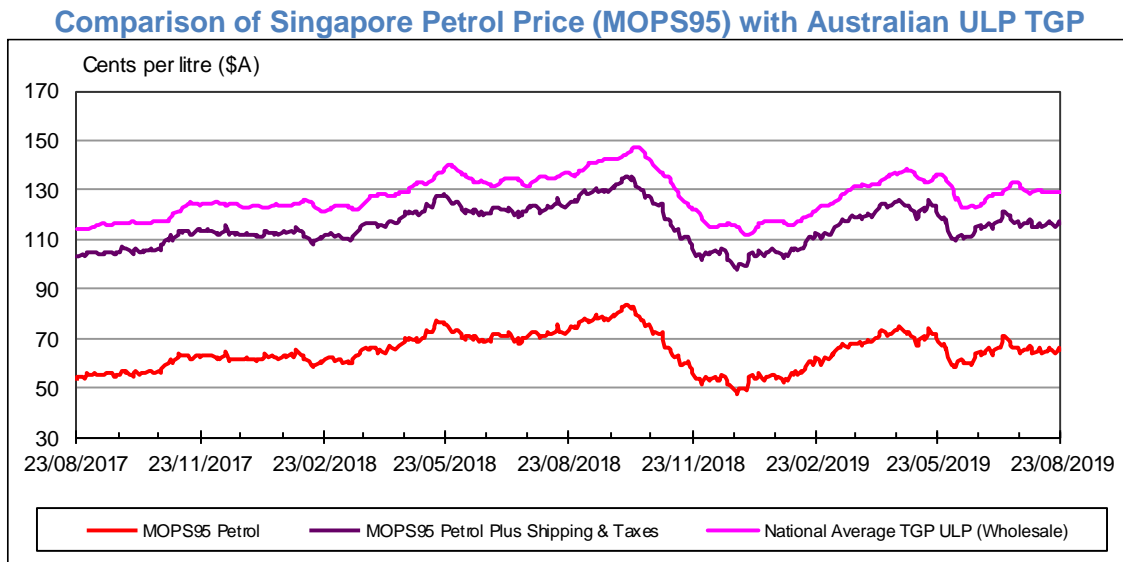
- ⇒ Australian Government Oilcode regulations require the publication of TGPs by all wholesale suppliers on a daily basis.
 - TGP is the spot price at which any person with the necessary safety clearances can purchase bulk fuel from a fuel terminal by the tanker load.
- ⇒ Daily average TGP data are published on the AIP website at www.aip.com.au/pricing/tgp.htm.

Posted TGPs provide market transparency and enable the market and consumers to readily follow trends in wholesale prices.

The ACCC has concluded that "by virtue of its transparency and the fact that it represents a fuel-only charge, TGP is a useful benchmark for analysing wholesale prices."

WHOLESALE PRICE MOVEMENTS

The close link between Singapore petrol prices and Australian ULP TGPs is shown below.



Generally there is a time lag of 1-2 weeks between changes in international (Singapore) prices and changes in Australian TGPs or other wholesale prices.

- ⇒ The lag can be seen above (i.e. the slight delay in the peaks and troughs in the pink line (TGP for ULP) compared to the purple line (MOPS95 plus Shipping & Taxes).

Importantly, this time lag occurs whether prices are going up (when the lag slows price rises to consumers) or prices are going down (when the lag delays price falls).

- ⇒ The lag is a result of using a rolling average of Singapore fuel prices as part of the IPP pricing approach — very similar to that used by the ACCC when wholesale prices were regulated by government. The use of rolling averages smoothes day-to-day price volatility.
- ⇒ According to the ACCC, “the lag may be longer during times of significant (international) price volatility”.

Not accounting for this time lag leads to incorrect conclusions about how Singapore fuel prices flow through to prices in Australia.

The ACCC formally monitors fuel prices in Australia, and the prices paid, costs and profits of major fuel suppliers, under the *Competition and Consumer Act 2010* and the latest ACCC Report, which analyses in detail the Australian wholesale market and prices, is available from www.accc.gov.au.

WHOLESALE PROFITS OF MAJOR OIL COMPANIES

The wholesale fuels market is a high-volume, low margin business. The wholesale fuel profits, if any, made by fuel suppliers are volatile (due to the nature of the market) and are typically a very small proportion of the final wholesale price.

For example, the ACCC has estimated that for each litre of fuel sold to motorists and other users the wholesale sector received an average annual net profit of 1.7 cents per litre over the past 12 years.

BULK FUEL TERMINALS

Bulk fuel 'terminals' are central to the wholesale market; they are large storage facilities from which fuel is sold to other wholesalers, distributors and retailers and to large end-users.

Terminals are categorised as either:

- ⇒ *import terminals* - connected to a port to receive fuel from ships
- ⇒ *refinery terminals* - connected to refinery to receive finished petroleum products
- ⇒ *marketing terminals or depots* - typically stand alone, receiving fuel via pipeline, road or rail.

Import terminals have significantly lower turnover than terminals connected to a refinery, since import terminals typically receive their fuel from ships (ie. shipping turnaround is a key factor).

- ⇒ In 2013–14 Australian import terminals averaged a terminal petrol turnover of 7 times, compared to 27 times for refinery-pipeline terminals, according to the ACCC.

The main types of terminal ownership are:

- ⇒ terminals owned and operated by refiner marketers (including joint ventures)
- ⇒ terminals owned and operated by independent fuel importers
- ⇒ terminals owned or operated by independent terminal operators

There are two main types of storage arrangements that provide access to terminals for parties other than the terminal owners:

- ⇒ *hosting* or providing access to another company to store and load product at the terminal for a market-based usage charge either on a spot or long term basis
- ⇒ *leasing* of storage capacity, typically long term agreements based on a commercial return on capital and operating costs.

Import Terminals — Ownership: 2013–14

Refiner Marketers:	
- Sole Ownership	41
- Joint Venture	3
Independent	14
Total	58

SOURCE: ACCC

Terminal capacity and throughput are two key measures of terminal usage.

- ⇒ The key determinants of terminal 'capacity' are the operating conditions that apply at individual terminals and in the supply network. These include the number and size of tanks, demand patterns, mode of supply and related infrastructure, shipping schedules, berth capacity and load-out facilities.
- ⇒ Similarly, 'throughput' depends on a range of factors such as demand patterns, shipping and delivery schedules and loading, storage and supply capacity.
- ⇒ **Independent operators now own more import storage capacity for petrol than the major oil companies and petrol imports by independent importers have increased six-fold since 2007-08.**

Import Terminals — Capacity and Throughput (Petrol): 2013–14

	Capacity (ML)	Throughput (ML)	Turnover (times)
Independently Owned	337	1965	6
Refiner-Marketer Owned	280	2446	9
AUSTRALIA	617	4411	7

SOURCE: ACCC

BULK FUEL SALES: 'INTO' AND 'OUT' OF TERMINALS

There is significant wholesale market competition in Australia.

There is competition for bulk fuel supply both 'into terminal' and 'out of terminal' to wholesalers, resellers, retailers and other major fuel users.

Contracts for sales of fuel 'into' terminals, whether from domestic or international sources, are based on Import Parity Pricing (IPP).

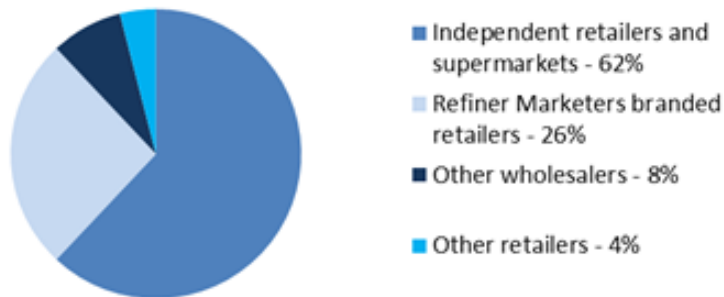
Sales of fuel 'out' of terminals are negotiated on commercial terms mainly to contracted wholesale and retail customers, although spot purchases occur.

Contracts are typically based on IPP or TGP, while spot purchases are on the basis of the Terminal Gate Price (TGP). Terminal operators seek to recover the terminal's capital and operating costs including taxes and other charges. Discounts or premiums may apply to customers depending on the volume, contract term, and any branding or marketing support provided.

Oil companies and independents often buy petroleum products from each other in markets where they do not own refineries or where they do not directly import through hosting arrangements. This is an economic and efficient way to service their customers in these markets. Such transactions are based on IPP and according to the ACCC closely track IPP with only a fraction of a cent difference.

The underlying pricing approaches in bulk fuel contracts and transactions are generally the same for all wholesale fuel customers.

Wholesale Petrol Sales by Refiner-Marketers: 2013–14



SOURCE: ACCC

TERMINAL INFRASTRUCTURE ADEQUACY AND COMPETITION ISSUES

As Australia's demand for fuel continues to grow, ongoing investment in bulk fuel terminal infrastructure becomes more important in ensuring supply security. Major independent and government reviews of Australia's petroleum import infrastructure and investment have concluded that:

- ⇒ significant industry investment in new or expanded facilities has been occurring and more is under construction or planned;
- ⇒ there is significant spare capacity to meet future demand and import growth, particularly in some independently owned import terminals;
- ⇒ there are a range of economic supply options in Asia to efficiently import fuel meeting Australian quality standards to terminals; and
- ⇒ the current terminal operating environment and access arrangements do not impose a constraint to competition for importers nor to ongoing investment.

This investment environment will ensure ongoing fuel supply security and competitive fuel prices to consumers and major fuel users. However, AIP supports reforms to ensure that planning, approval and regulatory processes are efficient, timely and nationally consistent, to support longer term investment in import terminals and storage facilities.