Australian Institute of Petroleum
Response to Question on Notice
ACT Fuel Price Inquiry Hearing of 9 May 2019

Question 1

THE CHAIR: Thank you for that. Taking your point about looking at trends and prices over time, we received some information from OPIS last week or the week before about what happened in the six-month period to the end of last year with the terminal gate price: that it was climbing up until the end of October and then fell very sharply.

Mr Barrett: Yes.

THE CHAIR: The Sydney prices also fell very sharply at the same time. There was a delay of a few days, but then it fell sharply. In Canberra they stayed steady for about another month and then started to decline, but there was nowhere near the sharp decline experienced in Sydney. Are you able to help enlighten us?

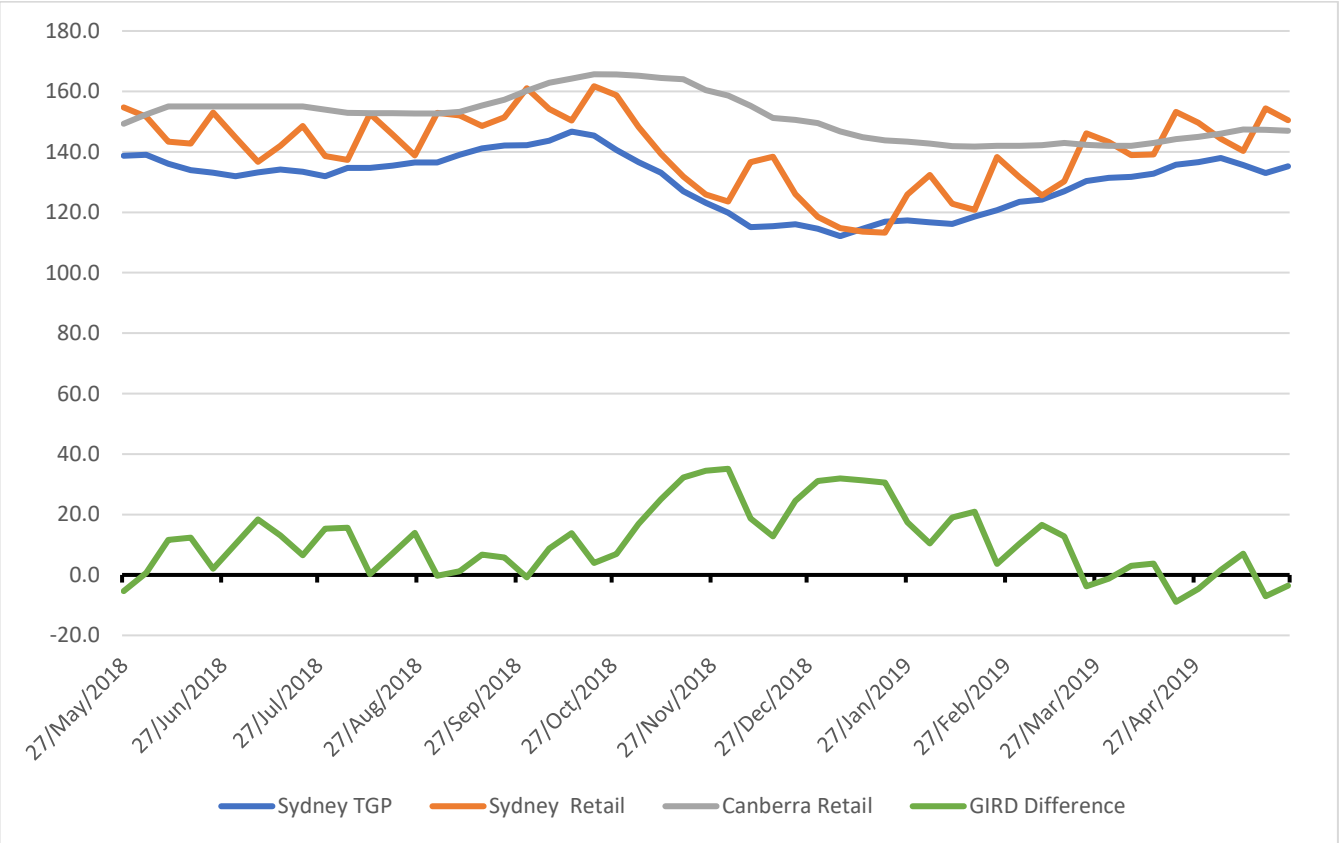
Answer 1

- The period in question is a classic example of the effects of the price lag from the Sydney Terminal Gate Price (TGPs, or the wholesale price) and the Canberra unleaded petrol (ULP) retail price when compared against Sydney retail prices.
- This effect is exacerbated by three key elements:
    - A rapid fall in the TGP
    - That Canberra has a 2-3 week lag from when movements in the Sydney TGP price are realised in the Canberra retail price
        - The Sydney market is much more responsive to movements in the TGP, particularly when movements are significantly up or down. This responsiveness is due to proximity to the terminal gate, as well as greater site throughput.
    - Sydney also has a fuel price discount cycle, whereas Canberra retail prices exhibit price stability more evident in regional fuel markets. The cycle can appear to exacerbate widening of prices when compared with markets that do not have cycles, particularly in the downward phase.
- Movement in Australian TGPs are reflective of commensurate movements in global oil prices and the refined gasoline benchmark price in Singapore (MOPS95). The TGP typically makes up between 85 and 90 percent of the retail price.
- The Sydney TGP (the relevant benchmark TGP for Canberra) was largely flat from Jan 2018 through to April 2018 at around 123cpl, where it then commenced steadily climbing to around 140cpl in May, dropping slightly before climbing to a high of 146cpl in October 2018.
    - The upward movement in the TGP reflected a commensurate move MOPS95.
- The TGP then fell rapidly through to January 2019 losing almost 30c to a bottom of 112cpl.
- This fall in the TGP commenced at the same time Sydney retail prices began the downward part of the discount cycle, leading to a significantly longer period of discounting than is normally the case for the Sydney market price cycle.
    - This is extraordinary unusual as shown in the following chart from end October to early December 2019.
- The ACCC notes that the average Sydney cycle is around 25-30 days. This first cycle during the significant fall in the TGP ran for almost double that, followed by a small rise in early December (where retailers had been selling below cost) and again followed by a discount phase through to the end of January 2019 running for almost 50 days.
    - A climb in the cycle consistent with normal the normal number of days in the Sydney cycle would have seen average prices and GIRDS remain consistent with Canberra retail prices.
- By January 2019, the TGP had already commenced a steady climb and retailers in Sydney were left selling at negative GIRDs for almost 2 weeks in anticipation of further falls in the TGP.
- Throughout this entire period, Canberra retail prices lagged the fall in the TGP by some 14 to 21 days (commencing their decline around the middle of November). The fall continued through to early February by which point TGPs had commenced rising.

- Fuel purchased by retailers toward the end of December were beginning to reflect the rise in TGPs which stopped the Canberra price decline and then flattened the Canberra price in February following the same 14-21 day lag period from December TGPs.

- While Sydney prices have continued to climb in line with the TGP, and consistent with recent historical price cycles, Canberra prices have been almost flat since this time with only modest increases.
- This is consistent with historical regional and metro pricing trends where TGPs begin to rise while metro prices, particularly in Sydney, are much more responsive to movements in the TGP.
- Furthermore, where Gross Indicative Retail Margins (GIRDS) widened between Sydney and Canberra during the rapid falls in the TGP, the GIRDS during the upward trend have significantly narrowed to the point where Canberra GIRDs have been in negative territory (indicating lower prices in Canberra). Again, this is due to the TGP-retail lag.
- Ultimately, this event is an anomaly of Sydney retail prices and price cycles, not Canberra prices.
- AIP anticipates that GIRD differences between Sydney and Canberra are likely to return to the historical norm consistent with the period prior to October 2018 assuming no further extreme upward or downward movements in the TGP.

The above explanation is demonstrated in the following Chart.



Note:

- Average prices have been used in this analysis. There will, however, always be differences across towns and across retail sites within towns due to a range of local area competition and business factors.
- The GIRD difference is the Sydney GIRD subtracted from the Canberra GIRD.
- GIRDs are not a measure of retailer profit. As described by the ACCC, GIRDs are:

  *GIRDs are a broad indicator of gross retail margins. They are calculated by subtracting average wholesale prices (as indicated by published terminal gate prices (TGPs)) from average retail prices. TGPs are the prices at which petrol can be purchased from wholesalers in the spot market and are posted on a regular basis on the websites of the major wholesalers. TGPs vary across brands and cities. TGPs reflect the wholesale price of petrol only, and exclude other retail operating costs (such as freight, branding, rent, labour and utility costs). As GIRDs include these costs, they should not be confused with actual retail profits (*ACCC, Report on the Australian Petroleum Market, March Quarter 2019).