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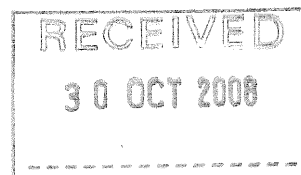
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To: Sen Stephens	From: M Delaney
Date: Econ Ctr	Fax No: 02 6273 2738
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Motor Trades Association of Australia

Senator Ursula Stephens
Chair
Economics References Committee
The Senate
Parliament House
CANBERRA ACT 2600



Dear Senator Stephens

I write in relation your Committee's inquiry into the Effectiveness of the *Trade Practices Act 1974* in Protecting Small Business.

The Australian Competition and Consumer Commission is currently considering a number of issues relating to the petroleum industry. One of those is a third line forcing notification lodged by Eureka Operations Pty Ltd (Notification No N91137). Eureka Operations is the company owned by Coles Myer, established to run the service stations it recently acquired from Shell multi-site franchisees. The third line forcing notification relates to the discount voucher arrangement where customers who spend a minimum amount (currently \$30.00) at a Coles supermarket, Bi-Lo supermarket or Liquorland outlet receive a voucher entitling them to a discount (currently four cents per litre) off the price of fuel at a Shell/Coles service station.

The Commission has consulted with a wide range of parties on the impact of that arrangement. Submissions from those parties, unless granted confidentiality, are placed on the Commission's public register. I have attached copies of two of those submissions which I believe will be of interest to you in relation to your current inquiry into the Trade Practices Act.

Both the submission from the Independent Petroleum Marketers Association of Australia and the file note of a meeting between the Commission and the Service Station Association (an MTAA Member Association) describe the current circumstances facing those in the retail sector of the petroleum industry and also on the issues being considered by the ACCC.

Some of those issues, the move towards a retail duopoly (Woolworths and Coles Myer) and issues of 'below cost selling' and the structural changes that are occurring and will continue to do so, in the petroleum industry are, we believe, relevant to your current inquiry. In fact the underlying issues of market power and the role that independent operators play in the market (be that in the retail petroleum sector, the grocery sector, the liquor sector or many others) are at the core of many of the submissions to your inquiry.

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MTAA's view is that unless there is a recognition of the contribution that small business can make to our society and there are changes to the Trade Practices Act which reflect that view, our economy will be dominated by a few very large corporations and the competitive force of independent operators will have been lost; and that will be to the detriment of consumers.

I trust that you will find the attached papers of interest.

If you require any further information please do not hesitate to contact me.

Yours sincerely



MICHAEL DELANEY
Executive Director

30 October 2003

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Mr Tim Grimwade
General Manager
Adjudication Branch
Australian Competition & Consumer Commission
PO Box 1199
Dickson ACT 2602

19 September 2003

Dear Mr Grimwade,

Re: **Exclusive Dealing Notification No. N91137**
filed by Eureka Operations Pty Ltd ("Eureka")

We refer to the abovementioned Notification as to conduct which potentially falls within sub-sections 47(6) or (7) of the *Trade Practices Act 1974* ("Act"), and to the Commission's invitation to provide comments in relation to same. This letter is intended to serve as a submission on behalf of the Independent Petroleum Marketers Association of Australia (known as the "PMAA") in support of the revocation of Eureka's immunity from prosecution by the ACCC in respect of the third-line forcing conduct proposed in the Notification.

In order to effectively explain the basis of the PMAA's objections to the proposal disclosed by Eureka in its Notification, the PMAA has found it necessary to elaborate upon the broader petroleum market context in which Eureka's proposal is made. Accordingly, the issues which are examined in this submission include fuel pricing cycles generally, the various effects of the introduction into the petroleum retail market of giant retailers Coles and Woolworths and the inadequacies of both present and proposed petroleum retailing legislation.

Further, this submission alludes to the detrimental market outcomes witnessed in Britain as a result of a failure in that country to stymie the push for greater petroleum retail power by the Tesco and Sainsbury's retail chains. The PMAA regards the present marketing strategies of both Coles and Woolworths as analogous to the initiatives taken by Tesco and Sainsbury's in Britain. By comparison, the prohibition on below-cost selling in most states within the United States and also in Ireland has resulted in the retention of significant numbers of independent retailers in the market which is reflected by lower and more competitive fuel prices in those countries.

In making this submission to the ACCC, the PMAA urges the ACCC to look beyond the immediate consumer benefits heralded by the price discounts offered by Coles (and also separately by Woolworths), and to adopt a longer term view which considers the real possibility of a market place bereft of

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strong independent competition, possibly within a very short period of time, possibly within months. A number of Victorian independent retailers are already proposing to sell their businesses (for example, see Melbourne Sunday Age article of 14 September 2003 entitled "Petrol Alliances Fuel Industry Shake-Up" which summarises the plight of one independent *Horizon Fuel* operator).

The petroleum market is at a crossroads, and the time is now for the ACCC to assess whether Coles and Woolworths have the market power to quash independent retailers, and to secure for themselves indomitable market power.

The Coles – Shell Joint Venture

It has been possible to ascertain the nature of the commercial alliance which has been struck between Coles and The Shell Company of Australia Ltd ("Shell") from a number of press articles, industry reports and media releases (and also from a separate third-line forcing notification filed in respect of sale of LPG by Shell Gas (LPG) Australia Pty Ltd to Eureka as a condition of the Coles-Shell joint venture). The PMAA's understanding of the alliance, which was announced on 23 May 2003, is as follows:

- Coles has paid a total amount less than \$100 million to acquire from Shell multi-site franchisee operators the rights to operate "Shell's core retail property network" of 584 Shell-branded petrol stations across Australia.
- Eureka, a fully owned subsidiary of Coles, will operate those sites, which will be co-branded "Coles" and "Shell". The alliance will see the creation of a new petrol and convenience store division within Coles, with the vast majority of the existing Shell franchisees staff expected to become part of this new division.
- Coles will set pump prices at all sites as well as supply convenience store products to the Eureka-operated sites.
- Shell will supply fuel products to Eureka, save for LPG, which will be sold to Eureka by Shell Gas (LPG) Australia Pty Ltd. These arrangements are reportedly pursuant to a ten year agreement.
- Customers of Coles, Liquorland and Bi-Lo stores who make a purchase of goods to a certain value (currently \$30.00) will be entitled to receive a discount on fuel purchased at all participating sites (currently 4 cents per litre).

In Shell's media release dated 27 May 2003 (entitled "Customers the Winners from Coles Myer – Shell Alliance"), a summary is provided as to how Coles and Shell believe grocery and petrol retailing competition will increase as a result of the Coles-Shell alliance, which entails the customer discount proposal. The media release states that "Alliance service stations will continue to have competitive pump prices which are viewed as critical to

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attracting and retaining customers", and "the Alliance will increase competition in the supermarket sector now and in the future by allowing Coles Myer to respond directly to discount fuel programs operated by other retailers".

The PMAA would interpret the reference to "other retailers" in the above media release to a clear reference to Woolworths in particular, Woolworths being the only other retailer which could possibly afford to compete with Coles on the scale proposed by Coles' nationwide marketing proposal.

Further, these comments are viewed by the PMAA as evidence of the quite aggressive stance being adopted by Coles and Shell in undertaking this alliance, and of their expectation to rely upon Coles' massive retailing revenue to allow the alliance to keep petrol prices as low as necessary to ensure attracting a large share of the fuel retail market. The PMAA is very aware that most participants in the fuel retail industry are already bracing themselves for the effects of the "price war" which is already being waged (particularly in Victoria) between the Coles-Shell alliance on the one hand, and Woolworths on the other. The forthcoming Woolworths-Caltex alliance will only serve to intensify this dangerous price war. The PMAA is of the firm view that whilst the casualties of this war will surely be a large number of independent fuel retailers, the ultimate casualty in the medium to long term will undoubtedly be the Australian motorist.

ACCC's Assessment of the Coles-Shell Discount

It is in relation to the "third-line forcing" aspect of the customer discount deal described above that Eureka filed the Notification which is the subject of this submission on 9 July 2003. Accordingly, statutory immunity in respect of the relevant exclusive dealing conduct commenced on 23 July 2003, and will continue pending the ACCC's determination as to whether the discount proposal is in the public interest.

In accordance with Section 93(3A) of the Act, the assessment which is required to be made by the ACCC in determining whether to continue to extend immunity to Eureka is whether the likely benefit to the public from the proposed conduct will outweigh the likely detriment. This is to say, the ACCC must assess whether the detriment to competition in permitting the exclusive dealing discount offer is outweighed by the cheaper fuel prices which will occur as a result of the discount deal.

The PMAA believes that it would be totally illusory for the ACCC to base its assessment only the effect on petrol prices in the short term. The ACCC must also consider the equally likely reality that fuel discounting conducted on so massive a scale as is proposed by Coles (and also separately by Woolworths) will result in independent fuel retailers being driven from the market, and motorists ultimately being at the mercy of only Coles-Shell and Woolworths-Caltex, and to a much lesser extent BP (industry sources indicate that Mobil is currently embarking on an exit-strategy in respect of its Australian operations). It is critical that the ACCC assess the extent to which the Coles-Shell discounts will have in lessening competition in the medium to long term.

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In order to illustrate the likely medium to short term effect on competition, it is necessary to understand the role played by independent fuel retailers in Australian petrol pricing cycles.

Price Cycles in the Australian Petroleum Retail Market

The Australian Institute of Petroleum ("AIP") provides an explanation on its website (www.aip.com.au/pricing/petrol.htm) of the retail price of petrol in Australia. Firstly, the AIP describes the retail price of petrol as being comprised of the product cost, which includes the cost of purchasing and refining crude oil (usually around 40%), excise (also usually around 40%), GST (10%) and gross retailing margin (up to 10%, but dependant on pump prices from day to day).

Secondly, the AIP provides a succinct summary of the pattern of movements in the pump price across the market, and describes this pattern as a "discount cycle" which unfolds usually on a weekly basis. At the height of this pricing cycle, the retail margin is usually around 9 to 10 cents a litre. One by one, the individual service stations or "brands" discount their price by small amounts in order to attract more customers. Other competing stations and brands quickly match these lower prices in order to remain competitive. Historically, this process continues until the retail margin falls close to, if not momentarily below, cost at which level petrol prices become unsustainably low and sales verge on being unprofitable.

It is at this point when some retailers will lead the market price back up again in order to see whether other retailers will follow them, and thereby restore some profitability to the market. This point in the cycle is therefore characterised by prices across the market taking a sharp jump up by between 6 to 9 cents a litre overnight or in the same day. In this way, the discount cycle commences once again, and so on and so forth.

The description offered by the AIP does not offer the complete picture. The AIP's description omits to mention that it is invariably the major brands ("majors") who cause the price to jump up to the cycle high point, and the independent retailers ("independents") who continually offer subsequent discounts which cause the market price to decrease steadily throughout the week. This is due to the simple fact that the majors, and not the independents, who have the market power capacity to lead the market back up due to their broader market coverage.

The AIP observes that cyclical petrol price fluctuations are a sign that the service stations are competing with each other to attract the motorist, and that this competition keeps Australia's petrol prices amongst the lowest in the world. The AIP states that "this combination of factors leads to a very volatile, but highly competitive market and cheap petrol prices. This is good for motorists." In the Victorian market, for example, where around 45% of fuel retailers are independents, it is easy to see why the independents are at least

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as important as the majors in ensuring that petrol remains competitively priced.

Without independents, the pressure on the relatively small number of majors (including both oil majors and the two dominant supermarket retailers) in the Australian market to reduce prices would be minimal. In fact, if independents played no role in the pricing of petrol in Australia, it is likely that a market oligopoly would subsist between the remaining majors, who would collectively stand to benefit from simply maintaining high prices. Whilst this may seem like a far-fetched scenario in the context of the current Australian petroleum retail market, it is a scenario which has unfortunately become reality in countries such as Britain and France, where retailing practices which have forced independents all but out of the market. We are now beginning to see effectively the same retailing practices being adopted here in Australia.

Likely Anti-Competitive Outcomes

The PMAA notes that a search of the ACCC public notification and adjudication register reveals that a number of other fuel retailers have been permitted by the ACCC to undertake petrol discount offers which are similar in principle: see *Caltex Australia Petroleum Pty Ltd* C2003/663 - N70630, *Mobil Littlehampton* C2003/525 - N91096, *Camptown Pty Ltd* C2003/414 - N91089, *Julross Pty Ltd* C2003/348 - N91081, *Bowen Petroleum Services Pty Ltd* C2003/285 - N91075, *Pearlday Pty Ltd* C2003/178 - N31214, *BP Broome Central Service Station* C2003/894 - N91138, *BP Australia Pty Ltd* C2003/900 - N91142, N91143, N91144, N91145, N91146, N91147 and others.

The ACCC has not revoked immunity in respect of each of the proposals cited above, each of which has involved a petrol retailer offering discounts to customers on condition that customer produce evidence of purchases from nominated supermarkets and/or grocery retailers. The PMAA regards there to be a huge distinction between each of the above proposals and the Coles-Shell discount offer on the basis of both scale and effect on competition. The above proposals each involve either one single or a small handful of petrol station sites and an equivalent number of grocery or supermarket operators. There is simply no comparison to be made between those other discount proposals and the nation-wide discount offer unleashed by Coles-Shell.

The PMAA argues that the factors militating against the ACCC approving the Coles-Shell discount proposal are as follows:

(a) *the massive market and buying power already wielded by Coles:*

The combined number of petrol station sites in Victoria alone that have become Eureka-operated under the Coles-Shell alliance is 158. This represents around 30% of the total number of petrol station sites in Victoria. This degree of market control translates into Coles selling many times the volume of fuel of its nearest market rivals, and will also place Coles in an ideal position to negotiate wholesale price reductions

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with Shell on the basis of its incomparable buying power. As such, Coles will be able to afford to keep its retail price lower than other fuel retailers due to its likely ability to purchase petrol cheaper than other retailers.

Coles will be giving a further discount to customers who have already poured money into Coles' coffers by purchasing groceries from Coles supermarkets. Should independent fuel retailers team up with other grocery retailers in attempts to compete with the promotional discounts offered by Coles (and also Woolworths), not only will they be unable to match the size of the discounts offered by the larger retailers, they will not be receiving any ancillary benefit in exchange for such discounts in the same way that Coles will.

The PMAA understands that the current proportion of customers purchasing fuel from Coles-controlled sites in conjunction with the discount offer is over 70% (this level is similar in respect of Woolworths' fuel sales). By comparison, members of the PMAA who have attempted to establish similar discount offers in conjunction with other supermarket retailers have achieved a redemption rate of only around 5% of their total sales. The PMAA recommends that the ACCC make its own independent enquiries to Coles in order to verify these market figures.

Independents would only stand to gain by engaging in coupon-style offers in conjunction with other grocery retailers if those offers actually drew high numbers of customers and result in high volumes of fuel sales. This is unlikely, given that, as noted above, independent fuel retailers cannot possibly match the discounts offered by Coles and Woolworths, and the likely redemption rates will be insignificant compared with the rates enjoyed by Coles and Woolworths. Overall, the ability of Coles to reduce its fuel price by around a further 4 cents a litre as part of a campaign that will also see it enjoy higher customer patronage of its supermarkets, will be devastating to other fuel retailers. Quite simply, the market power of Coles creates an unlevel playing field on which smaller retailers cannot compete.

(b) *the open-endedness of the promotion as to timing, and the scale and degree of effect on petrol pricing cycles that could result from sustained discounting:*

The PMAA is aware that sale of fuel generally accounts for only around two-thirds of the total revenue generated by an individual petrol station site, with the other one-third being derived from retail sales of goods from within the store located on the site. The sale of fuel by Coles will account for a much smaller proportion of its total revenue, and is likely to be a mere tiny fraction in the context of the massive retail activities it conducts.

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Accordingly, Coles has the capacity to sell fuel as a "loss leader" (a product earmarked for below-cost sale in order to attract customers, who will invariably purchase other goods at the same time as purchasing the discounted item), in the same way as they can "loss lead" with other staple goods in a supermarket, such as milk and bread, etc. Unlike independent retailers, Coles will never depend on fuel sales for two-third of its revenue, and as such it will be able to afford to keep the price of its fuel much lower and for much longer than any independent fuel retailer. If Coles (especially in the context of a national fuel war with Woolworths) should decide to actively lead the fuel retail market near to or below wholesale cost for any sustained period of time (which it easily has the capacity to do), independent retailers will very quickly be forced to cut their losses and opt out of the market altogether. As noted above, we are already seeing this happen in Victoria.

To illustrate how competition in the fuel retail market works, the AIP uses the metaphor of children playing around by seeing who can hold their breath the longest at the bottom of a swimming pool. The independents cannot hold their breath for anywhere near as long as the two giant retailers, and Coles must be well aware of this reality.

In the event that the ACCC is able to secure some form of undertaking from Coles that it will not lead the market below cost, the ACCC should take the discount (presently 4 cents per litre) into account in determining whether such undertaking has been breached at any time. It is the PMAA's view that the advertised price of fuel sold by Coles should be deemed by the ACCC to be below cost if the price together with the discount results in an ultimate below cost price being available to the motorist.

Further, when assessing the impact of the Coles-Shell discount on average prices during a specific period of time, it would be totally misleading to focus on state-wide figures, as the only way to obtain an accurate picture is by looking at competition within specific regions, and in particular metropolitan districts, where competition is fiercest. Retail prices of fuel in country areas are almost always quite higher than metropolitan areas, due to the relative lack of competition in country regions. As such, country prices bring the state-wide average fuel price up and tend to distort the reality in city regions.

The PMAA has obtained informal industry intelligence to the effect that since the introduction in Victoria in late July of this year (Victoria being the first state in which the Coles-Shell alliance has been "rolled-out") of petrol discounting by Coles, the volume of petrol sales experienced by Shell has increased by 60%. This is compared with an average reduction of around 30 % of fuel sales by all other competitors for the same period. The PMAA strongly urges the ACCC to seek independent verification of these figures from both Coles-Shell and also appropriate industry and/or government sources. These figures

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amply demonstrate the dramatic market power controlled by the Coles-Shell alliance, and quite explicably have caused independent retailers to commence selling their businesses.

In light of such rapid and huge increase in market sales shifts and volume, the PMAA does not believe that it is feasible for the ACCC to take the option of allowing the Coles-Shell discount proposal to proceed now with a view to perhaps reviewing the effects on competition some nominal time into the future. The effects on competition of the proposal have already had stark and obvious consequences for those independents who are selling up and getting out.

Clearly, the ACCC must consider the overall medium to long-term effect on the overall market rather than simply approve of these promotional strategies on the basis of their obvious financial benefit to Australian motorists in the immediate short-term future.

- (c) ***the fact that such promotions are leading Coles and Woolworths to adopt advertising practices which are confusing and possibly misleading.***

The fuel price board currently being used at Coles-Shell petrol sites is possibly misleading to motorists in that it displays the current undiscounted price, the discounted price and the offer of a 4 cent discount. This is misleading because it is not clear to motorists as to which price the 4 cent discount applies. Further, the "rider" advising that, inter alia, 'conditions apply' is very small and is therefore inappropriate as it effectively constitutes a failure to properly disclose the fact that the offer is conditional.

In order to ascertain how price board advertising may develop if the Coles discount proposal is permitted to proceed, it is worth comparing the current advertising method used by Coles-Shell as described above, with the advertising proposed to be used by Woolworths-Caltex in the context of the current price war.

The ASX Woolworths-Caltex joint venture announcement contains diagrams of the proposed petrol price boards which are proposed to be used as from later on this year. They go one step further than the price boards already being used by Safeway and Coles in that they do not even show the current undiscounted fuel price. The proposed pricing boards merely advertise the 4 cent discount together with the already discounted petrol price. The combination of these two pieces of information would lead a motorist to conclude that a 4 cent discount would apply to the advertised price, whereas the price advertised is an already discounted price.

Further, the price boards proposed to be used by Caltex and Woolworths establish a new practice of using not one price board, but two. The first price board contains a description of the discount and states the already

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discounted price as discussed in the previous paragraph, and the second board (placed a few metres away) displays the undiscounted price. This separation of these pieces of information is a further basis on which, taken as a whole, the manner of advertising proposed by Caltex is wholly misleading.

The original price board advertising used by Woolworths is the same form as that which is currently being used by Coles. If Woolworths is permitted to pursue the modified form of advertising as proposed in the Woolworths-Caltex ASX announcement (described above), it is extremely likely that Coles will very quickly follow Woolworths' lead as it has done in the past.

Fuel Retail Legislation: Retaining Strong Market Competition to Protect the Motorist

Governments have a choice between restricting pump price movements, which will result in higher prices, or continuing to allow prices to move freely, which keeps prices volatile to rapid change, but generally low. It is clear that our free market is a critical component of our liberal democracy. As such, no Federal Australian Government is likely to introduce regulation of petrol prices as this would undoubtedly lead to higher fuel prices at least some of the time and would ultimately lessen competitive outcomes. In such circumstances, independent fuel retailers play a critical role in the market and their continued participation should be encouraged and promoted.

The PMAA stresses that it advocates the enhancement of the role of independent fuel retailers not as an end in itself, but rather as the most effective means to ensure protection of the Australian motorist from totally unnecessarily high fuel prices. Due to the inadequacies of current fuel retail and franchising legislation, which are documented more extensively elsewhere, a greater role in curtailing rampant retail giants operating within the fuel industry necessarily falls to the ACCC.

The general monitoring of competition levels within the petroleum market conducted by the ACCC occurs in conjunction with the regulation of retail (or "downstream") control by suppliers within the petroleum industry which is undertaken by the Federal Department of Industry, Trade & Resources. The Department administers, *inter alia*, the *Petroleum Marketing Sites Act 1980 (Cth)* ("Sites Act") and the *Petroleum Retail Marketing Franchise Act 1980 (Cth)* ("Franchise Act") as part of its role in this regard.

The Sites Act places a restriction on fuel refiner-marketers such that these entities cannot control and operate the retailing of fuel refined and distributed by them at any more than 5% of sites at which their fuel is sold by retail. This "5% Rule" has historically been evaded to great effect by refiner-marketers by way of entering into licence and franchise agreements with separate operators. In this way, franchisee multi-site operators have already been operating sites actually owned by oil companies for some years.

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In 1998 the Federal Government released details of its petroleum industry reform package, which included the repeal of both the Sites Act and the Franchise Act, for reasons including the obsolescence of the 5% Rule.

The Draft *Trade Practices (Industry Codes – Oilcode) Regulations 2003 (Cth)* ("Oilcode"), made pursuant to Section 51AD of the *Trade Practices Act 1974 (Cth)*, are proposed to commence upon repeal of the Sites Act and the Franchise Act. Oilcode has been developed with a view to ensuring the better governance of contractual relations between petroleum resellers (including retailers) and suppliers. However, the drafters of Oilcode have totally failed to envisage the introduction into the fuel retail market of mass retailers such as Coles and Woolworths.

In particular, Clause 10 of Oilcode prohibits refiner-marketers who retail fuel from retailing fuel at below cost, the cost price being defined as the Terminal Gate Price in place at any given time. By establishing alliances with Coles and Woolworths respectively, both Shell and Caltex have avoided the effects of Clause 10 of Oilcode, leaving BP and Mobil (until such time as it finally leaves the Australian market altogether) to be caught by the Clause 10 prohibition. The PMAA is of the strong view that Coles and Woolworths ought to be subject to Clause 10 of Oilcode as they will represent an estimated 50% of the Australian fuel retail market once the Woolworths-Caltex alliance takes effect.

Once again, despite attempts to address concerns relating to inappropriate concentration of market power within the petroleum sector, forthcoming legislation in the form of Oilcode is set to prove inadequate. Accordingly, the ACCC may be one of the few effective means of restraining the Coles-Shell alliance from accruing the kind of market power which could allow it to achieve uncompetitive outcomes through possible misuse of market control.

Whilst this is perhaps an argument which should be made separately to the Department, or which may already have been assessed by the Mergers and Assets Sales division of the ACCC in relation to the Coles-Shell alliance, the PMAA also regards it as a legitimate matter for consideration by the ACCC in the context of assessment of the current Notification.

Conclusion

The discount deal currently offered by Coles clearly benefits Australian motorists in the immediate future. These offers will create opportunities for motorists to purchase fuel at very low prices, and will force competitors to match those prices.

It is in the medium to long term, however, that smaller retailers will simply not be able to continue to compete. A number of these smaller retailers are beginning to speak out about the effects that the Coles-Shell discount (and also the similar Woolworths-Caltex discount) is having on their businesses.

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Without independents, the fuel market would be without its chief means of achieving the levels of competition which have historically allowed Australian motorists to enjoy some of the lowest petrol prices in the world. At that point, in a market unregulated by price restriction, nothing would prevent the remaining majors to establish an oligopoly, a market consisting of such few sellers as to allow them to set fuel at any price with the effective, but informal, co-operation of one another. Even consumer bodies such as the RACV are now beginning to form the view that this possibility is not at all far-fetched.

This is a bleak picture, but not an unrealistic one, and the picture will begin to take shape with the ACCC's approval of these joint venture exclusive dealing proposals. The PMAA requests that the ACCC consider seriously the contents of these submissions when determining whether to grant immunity to Coles (and also Woolworths for that matter) in respect of the discount offer which is possibly central to the short-term success of the alliance.

The PMAA would be pleased to respond to any queries that the ACCC may have or to provide any further details in relation to this submission. Mr Rocco Pratico, Secretary of the PMAA, may be contacted at any time on mob. 0419 530 822.

Yours faithfully,
Independent Marketers Association of Australia

Rocco Pratico
Secretary

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FILE NOTE***Meeting between ACCC and Service Station Association (SSA)******26 August 2003******10am*****Attendees:**

ACCC	Graeme Samuel Jennifer McNeill Stephanie Chenoweth Stefance Lovett Alistair Davey
SSA	Richard Halstead (President) Ron Bowden (CEO)

The meeting was called by the SSA to discuss some of their concerns in relation to a number of issues currently facing the petrol retailing and wholesaling industries.

Petrol industry

Ron Bowden (RB) started the meeting by providing a brief overview of petrol refining. He noted that though petrol is the most refined substance in the world – it is very capital intensive and large costs involved – the end product is still very cheap relatively speaking.

RB said that the new fuel standards which will commence from January 2004 are necessary to ensure better fuel consumption and will enable car manufacturers to design more fuel efficient cars. RB said that at this stage it was expected that most importers wouldn't comply with the new fuel standards until around 2006.

Entrance of supermarkets into petrol retailing

RB said the recent introduction of Coles into the petrol market had seen a dominant player move into the marketplace in a short space of time. He noted that when Woolworths had previously entered the market, it had provided the industry participants with sufficient time to adjust to the new entrant in that its current 12% market share had been gained through a gradual roll out over 5-6 year period.

RB said that one of the biggest problems caused by the dominance of alliances such as Coles/ Shell and Woolworth/ Caltex is the issue of below cost pricing. He noted that the independents' core business is petrol and that pure petrol retailers will find it difficult to compete with players who have a core businesses elsewhere (i.e., supermarket retailing) who can effectively cross subsidise the petrol business.

In addition to the entrance of Coles into the industry, RB said that the recently announced joint venture between Caltex and Woolworths will amount to Woolworths having a market share of between 16 and 20%. RB noted that Woolworths'

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throughput per site is higher than the industry average, and that around 80% of this consumption would be from customers using shopper docket discounts (SDD).

TGP and below cost pricing

RH said that the SSA is concerned with Terminal Gate Pricing (TGP) where the price at which franchisees are buying their fuel and other participants such as Coles should in theory be the same. However, in practice under the TGP, independents and regional fuel sites have to pay freight costs, and the further out they are and the smaller the volume consumed, the higher the costs that must be borne by independents in rural and regional areas. He added that a number of the small traditional sites are disappearing, and once you throw in the SDD, the bigger independents will also start exiting the market.

RB said that where chains such as Shell/ Coles or Caltex/Woolworths sell petrol with the SDD at below cost price, the SSA considers that this could be an exertion of market power. RB said that when Woolworths entered the market, some sites competing near a Woolworths site were no longer profitable, and in certain areas the independents dropped out, but there was still scope for them to move away from the supermarket area and open other independent retail petrol outlets. With the size of the Shell/ Coles network, there will be less scope for independents to do this.

RH said that the market share of the two supermarket chains in the petrol retail industry looks like becoming around 50%. RB added that a 20% market share for Woolies would still have been a problem, but it would have been more manageable. He said that on current estimates, over 50% of petrol will be supplied by supermarkets by mid next year, with 70-80% of that purchased with a SDD.

In looking at whether independents can survive below cost pricing, RH said that there is some margin in the cycle - the independents can make some money in the 'in-between' spot, which may result in smaller groups of independents getting together to form chains. To this end, independents can sustain the cycle, but only down to the point where you are selling petrol at the price you paid for it. Independents can't compete with below cost pricing and therefore can't compete with SDDs.

RH said that the TGP was supposed to represent the true cost of the product, and that retail sites were not supposed to have their board price below the TGP cost of the product. He added that they are not wholly opposed to the SDD system per se but rather are against the ability of the supermarkets to subsidise one product for the other and compete on that basis with independents if they try to set their own price.

Supply issues

RB said that in the past where there was surplus volume, such volume could be sold to independents. This was where the ability of imports to supply the market became important - independents could choose to source their petrol from imports, which may result in a competitive price, but most independents would be likely to buy their product from Australian refineries, as the refineries would match the import price offered to the independent. This was generally the case so that the Australian refinery could guarantee the sale and get rid of their excess supply.

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The Australian market is now facing a situation where, due to the reduction in imports and a decrease in the amount refined in Australia, the competitive source of supply was being removed for independents. RH said Caltex and Shell now control a large amount of distribution also, and would not be open to selling to independents at discounted prices.

Market consolidation

RB said that most independents cannot match the SDD; they need to go and secure their own arrangement. RH said that supply will get tight once the new fuel standards are implemented and importers can no longer supply fuel, especially where, for example, Caltex is now supplying fuel to Woolworths on top of its normal distribution, and this would result in less fuel being available for other independents. He added that Liberty Oil supplies some independents, but they also receive their fuel from Caltex.

RB and RH argued that the situation would lead to a duopoly in both grocery and fuel retailing, with Coles/ Shell and Woolworths/ Caltex dominating both markets. GS asked why Australia couldn't have the following groups of industry participants: Coles/Shell, Caltex, Caltex/Woolworths, BP/Metcash, BP/Foodland and then Liberty and the other independents. RH said that the market will still come out with only two main suppliers - Shell and Caltex - who will also want to ensure that their retail networks are also dominant.

The SSA agrees that five, six or even seven major groups could still remain in operation post the "supermarket revolution". However, the SSA is concerned that any entity that is dominated by an oil company or a supermarket won't compete in the same way that independents have traditionally competed.

This can be easily explained by examining each entity's pricing policy. For example, Woolworths' standard pricing policy is for each site's "headline price" (ie, before discount) to match the lowest oil major competitor in the same area. The problem is that all the other majors have a similar policy and they only lower their prices when independents force them down. Without a significant presence of active independents, there will not be sufficient pressure on the major players to lower their prices.

The SSA stated in summary that its not the number of competitors that counts, it's the way they compete that really matters.

The meeting ended with the Commission agreeing to send a copy of the meeting notes to the SSA for its clarification/further comments prior to them being put on the public register.