

COLES EXPRESS

PARLIAMENTARY SELECT COMMITTEE INQUIRY INTO FUEL PRICES IN QUEENSLAND

Introduction

Coles Express is a fuel and convenience retailer, delivering one of the best value fuel offers in Queensland through providing quality Shell fuels at competitive board prices as well as a 4-cent per litre fuel discount off the pump price of fuel.

Coles Express was formed in 2003 following the development of an alliance between Coles Myer and Shell. Under this alliance Shell supplies fuel products and Coles Myer, under the banner of Coles Express, operates the fuel and convenience retail business independently of Shell.

Today, Coles Express operates 600 fuel and convenience stores Australia wide, equating to approximately 9% of the 7,000 service stations or fuel retail sites in Australia. Coles Express employs over 5,000 people.

In Queensland, Coles Express operates 111 service stations and employs more than 1000 Queenslanders.

Coles Express is the fuel and convenience business of the Coles Myer Group. Overall, Coles Myer is one of Queensland's largest employer groups, providing jobs for more than 32,000 Queenslanders through its nearly 500 retail outlets across the state. Coles Myer pays approximately \$850 million in state and federal taxes and collects, on behalf of governments, \$1,169 million dollars, including GST.

Coles Express, Fuel Retailing and Factors Contributing to Fuel Prices

Coles Express delivers one of the most competitive fuel offers in Queensland. In addition to providing competitive board prices, Coles Express also offers a 4-cent per litre discount to customers who spend \$30 or more at Coles, Bi-Lo or Liquorland.

Coles Express is also an integral member of the Coles Myer loyalty program, which includes the Coles Myer Source Mastercard, the MyerOne program and FlyBuys. This program provides opportunities for customers to earn further discounts on fuel prices. For example, FlyBuys have recently announced a new promotion offering customers the chance to redeem 1000 FlyBuys points in return for a 10 cent per litre fuel voucher, which when combined with the standard 4 cent per litre shopper docket gives Queenslanders the opportunity to save 14 cents pre litre off the price of fuel.

Australian consumers have enthusiastically embraced shopper docket schemes. In excess of three million docket redemptions occur in the industry each week, and there are now well in excess of 100 fuel discount schemes operating in Australia, offered by retailers and other businesses both large and small.

Consumers across Australia have saved millions of dollars off their fuel bills. Many millions of dockets have been redeemed thus saving Queenslanders millions of dollars off their household budgets.

The Coles Express pricing strategy across Australia is to at least *match* the board price of the lowest priced competitor as often as possible. Successful execution of this strategy provides consumers with confidence that whatever the retail price, they can be assured that Coles Express provides best value. In addition of course, Coles Express also offers a 4 cents per litre discount for those consumers who choose to shop and save at Coles, Bi-Lo and Liquorland outlets.

As the Committee would appreciate, fuel prices in Queensland (and elsewhere in Australia), are determined largely by factors beyond the control of retailers or governments. These factors include:

- The terminal gate price (TGP) set by oil companies and charged to fuel retailers.
- The price of oil, which is set internationally, oscillates on a daily basis in response to international events and demand and supply.
- Crude oil prices and refiners margins have increased significantly in recent times (Coles Express only entered the retail market in 2003) and although now reducing, remain at historically high levels.
- The value of the Australian dollar varies daily and directly impacts the purchase price of oil and the price of the finished product.
- The cost of importing, storing and transportation of fuel will vary from location to location, with more remote and lower volume (critical mass) facilities incurring higher per litre costs.
- Government taxes. Fuel taxes can form between 40-50% of the board price.

Petrol Prices in Queensland

Fuel retailing is a high volume, low margin business. Retail fuel prices are the outcome of a complex interplay of competitive and operational factors. These factors are peculiar to individual markets and sites and include wholesale prices or the Terminal Gate Price (TGP) set by the oil companies and paid by fuel retailers; taxes; freight; operating costs; trading hours; other on-site income sources; site rental; site throughputs; payment options; promotions; legislative compliance obligations; investment and maintenance needs; competitor initiatives, and of course, product supply and demand. As a result there is no uniform price for fuel in Queensland, or any part of Australia

Metropolitan Brisbane fuel prices (which incorporates Brisbane, the Gold Coast and the Sunshine Coast) at Coles Express have tracked broadly in line with Melbourne and Sydney fuel prices for the past 12 months. Chart One demonstrates that the average fuel price for Brisbane as compared to Melbourne and Sydney is lower as a result of the Queensland Government fuel subsidy.

Refer to Chart One. Data sourced from Coles Express.

Chart Two highlights the competitive nature of the Brisbane retail fuel market.

Refer to Chart Two. Data provided by Informed Sources, Australia's leading independent fuel price monitoring company.

The retail fuel industry is very, very competitive. Fuel retailers of all sizes compete with each other for patronage by motorists seeking the lowest fuel price in the market. This group of consumers are keenly aware of even the smallest price differential – a price measured in tenths of a cent. Fuel prices are transparent for both consumers and competitors. Price changes in the petrol price cycles that we see lead to a rapid response from competitors and an equally rapid transfer in custom by motorists when choosing to buy petrol.

Average margins on retail fuel sales are extremely tight, such that retailers' pre-cost share of the price of fuel is measured in single digit cents in the dollar, the lowest in the retail industry. Chart Three below demonstrates this point, showing average prices as compared to the terminal gate price (TGP) before and after the Queensland Government's Fuel Subsidy.

Refer to Chart Three. Data provided by Informed Sources, Australia's leading independent fuel price monitoring company and Shell Australia

In regional Queensland, retail fuel prices are competitive but tend to be higher than Brisbane because of the smaller volumes sold in regional and remote locations and the higher fuel margins necessary to cover the high fixed costs of operating a service station in these locations.

It is generally accepted in the industry that the larger urban fuel outlets require at least a 3 cents per litre (cpl) gross margin to cover fixed costs. All other things being equal, a typical regional site, selling half the volume, will require a per litre margin twice that amount to cover fixed costs. This is before an allowance for a commercial profit is made and does not take account of other factors such as business risk and costs associated with remoteness (freight, maintenance, higher working capital and extreme seasonal conditions).

Charts Four, Five and Six below demonstrate this point showing the 12-month average price comparison between Brisbane and the regional centres of Townsville, Mackay, and Toowoomba.

Refer to Charts Four, Five and Six. Data provided by Informed Sources, Australia's leading independent fuel price monitoring company, Coles Express and Shell Australia.

Alternative Fuel Sources and E10

In addition to providing a competitive fuel offer for Queenslanders, Coles Express in conjunction with our alliance partner Shell, has recently launched a new fuel, Shell Optimax Extreme, formulated with 5% ethanol.

The launch of Optimax Extreme is aimed at driving consumer acceptance of ethanol as a high performance, quality fuel component. We believe that consumer confidence in the quality and performance of bio fuels is critical and given the negativity associated with ethanol-based fuels in the past, the premium positioning of Optimax Extreme will play a key role in the industry wide challenge to overcome negative consumer sentiment regarding ethanol blended fuels.

While we are doing our part to promote consumer acceptance of ethanol, we are acutely aware that it would take only one negative incident with an ethanol-based fuel to undo growing consumer confidence, jeopardising the bio fuel target and the investment others and we are making to meet these targets.

I'm sure you appreciate that most service stations do not have the tanks and operating equipment on site to manage ethanol-based fuels. Owners of sites across Australia will need to invest in this infrastructure and Coles Express has already begun this process, as have other major chains and oil companies. Managing this investment, in such a low margin business as fuel retailing, is a challenge for the major retailers, let alone smaller independent operators. As such, it is a concern to those of us investing in ethanol that any incidents that undermine the public's confidence, will set the clock back on the rollout of these fuels.

We say this in the context of the forthcoming clean fuel requirements in January 2006 and the removal of the fuel savings grants over the next six months, which combine to add costs in a market place where consumer confidence is finely balanced.

Perhaps, given this situation and in the interests of all fuel retailers and motorists, it is worth extending the Commonwealth's Fuel Savings Grant Scheme, due to be phased out in July 2006. This would be welcomed by motorists in regional areas, where it applies, and help fuel retailers alleviate the costly investment needed for ethanol over the next two years.

We appreciate that the idea of extending Federal Government fuel subsidies requires budgetary and political considerations beyond the capacity of this Committee or the Queensland government.

Profitability and Transparency

Coles Express is one of the few Australian fuel retailers required to report bi-annually information on its turnover and earnings before interest and tax (EBIT).

In September 2005, Coles Express reported that it had earned a 0.6 per cent EBIT margin for every litre of fuel sold, or a net profit of less than one cent in the dollar, further emphasising that fuel is a high volume, low margin business.

Conclusion

Coles Express is proud of its record in providing a competitive fuel offer to Queensland motorists, and seeks to offer competitive prices in every market where it operates. Coles Express also offers motorists the opportunity to save a further 4 cents per litre if they choose to shop at key Coles Myer retail outlets. Offers such as this are helping reduce the price of fuel, and we aim to continue developing innovative offers for the benefit of Queensland consumers.

Coles Express is doing its part to promote consumer acceptance of ethanol in fuel. The investment others, including the Queensland Government, and we are making is critical to reaching this target.

Fuel prices have come down significantly from the peak levels this year, which have lessened consumer concerns. However, Coles Express receive less than one cent in the dollar profit compared to the nearly 50 cents per litre income governments receive in taxes and excise and therefore, as retailers, we have a limited capacity to reduce the price of fuel or pass on any price benefits.

Having said that, fuel prices in Queensland, in Australia, indeed internationally, are determined largely by factors beyond the control of retailers or governments.

Coles Express appreciates the opportunity to provide the Committee with these observations on fuel pricing in Queensland and also uses the opportunity to table specific answers to the Committee's Terms Of Reference.

COLES EXPRESS

PARLIAMENTARY SELECT COMMITTEE INQUIRY INTO FUEL PRICES IN QUEENSLAND - TERMS OF REFERENCE

The following responses addresses aspects of the Terms of Reference relevant to fuel retailing.

- (a) *Consider the extent to which current petrol price increases the competitiveness of alternative fuel sources such as E-10.*

Simplistically, high oil prices do make alternative fuels more attractive to energy users and consumers but the volatile nature of oil prices and the massive investment required to source and distribute alternative fuels to consumers, suggest that the term *current* is not a particularly useful guide to predicting the competitiveness of alternative fuels.

- (b) *Identify the economic and financial consequences of current fuel prices with a particular emphasis on regional Queensland and outer metropolitan areas.*

Coles Express is not qualified to make such a broad assessment. However, many commentators noted the impact of high fuel prices on consumers and business that prevailed during the second and third quarter of 2005. We have no reason to doubt some of these views on consumer spending habits (i.e. the purchase of more smaller cars) and the family budget whether in regional Queensland or outer urban areas.

- (c) *Identify practical ways that consumers can reduce their petrol bills, including through considering whether existing information on the fuel efficiency of different makes of motor vehicles is sufficient.*

Most automotive manufacturers offer a large range of vehicles consumers can choose from. Motoring magazines, daily newspaper columns and other media regularly compare the fuel efficiency of these cars and the choices available. These purchasing decisions, with the trend to smaller cars noted above, are made by the consumer based on a range of factors, including running costs.

- (d) *Consider the extent to which recent fuel increases could be moderated through enhanced domestic competition, including how the ACCC powers could be strengthened to deliver enhanced competition.*

Domestic competition in the retail fuel market (particularly in urban areas) is intense with fuel retailers fighting for market share and constantly discounting fuel prices on a daily basis. Few products are sold to the public where the price is measured in tenths of a cent. Where the price is known to within a cent, on a daily basis, by most motorists and the sellers of this fuel make gross profit margins of less than four per cent and net profit margins of less than a cent in the dollar.

- (e) *Examine whether Queensland receives its fair share of road funding.*

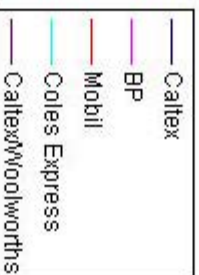
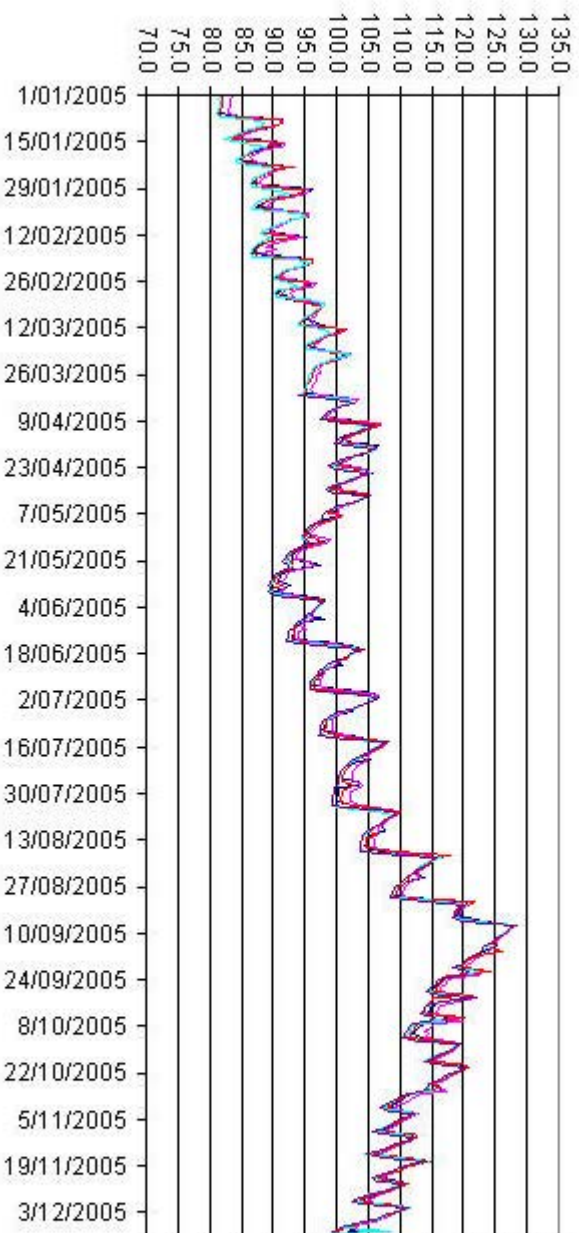
Coles Express is not qualified to make a judgement or assessment of whether this is or isn't the case.

- (f) *Identify the capacity and benefits of the federal government reducing fuel excise to ameliorate the impact of high fuel prices on families and business, and*
- (g) *Identify whether Queensland motorists are receiving the full benefit of the 8.354 cents per litre subsidy and examine the efficiency of administration for the bulk end users scheme.*

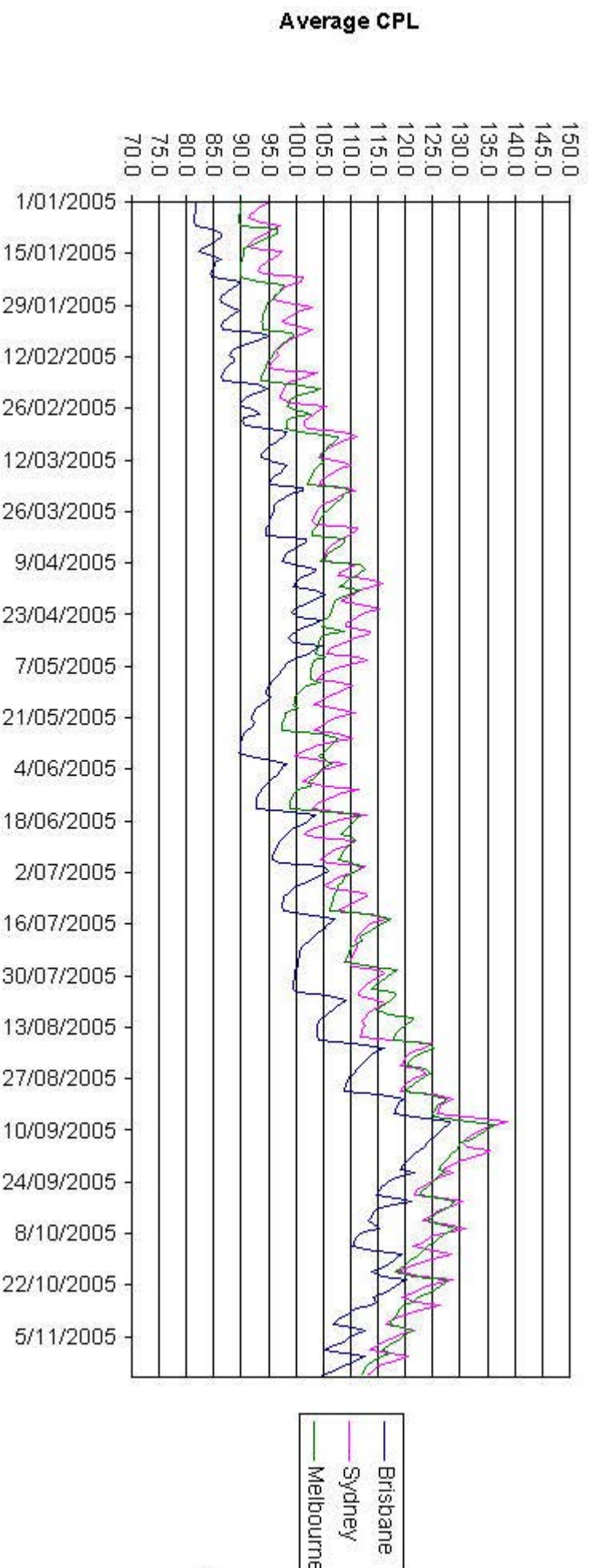
Coles Express is not qualified to make a judgement or assessment on these last two questions but notes that a lower tax level compared to other states, while welcomed by motorists, is relative. The level of tax on fuel is still extraordinarily high and approaching 50 per cent of the cost of fuel for motorists.

Average Brisbane Coles Express and COMP ULP Prices

Average CPL

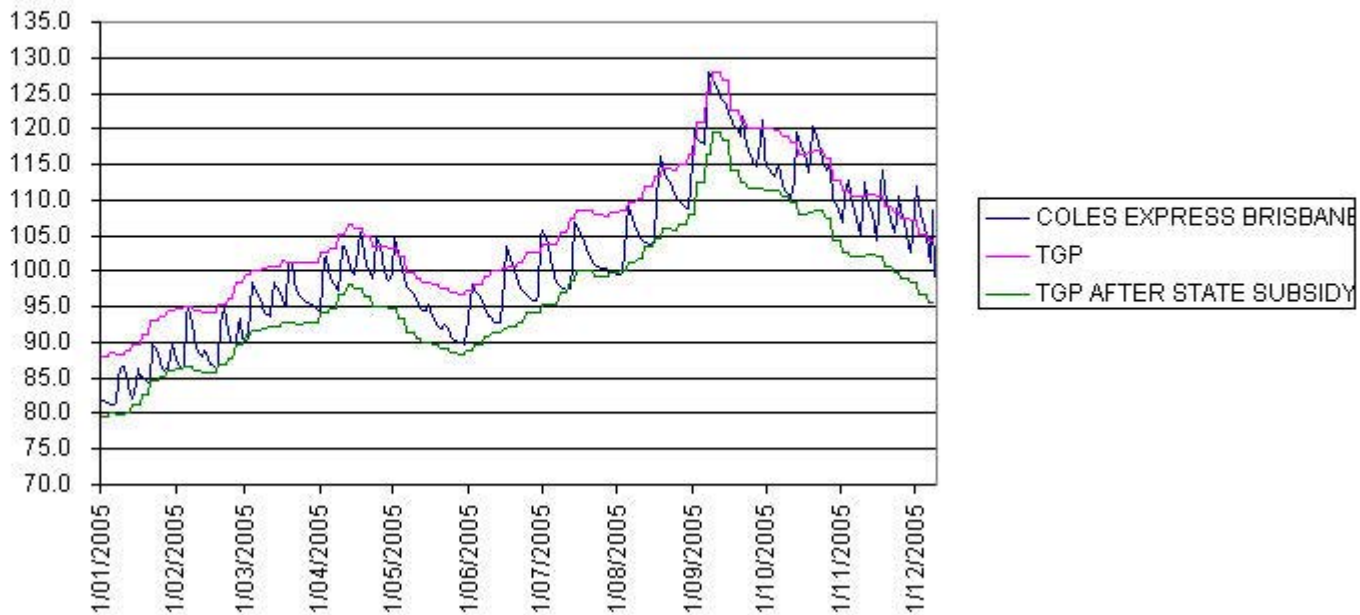


Coles Express Average Brisbane, Sydney and Melbourne

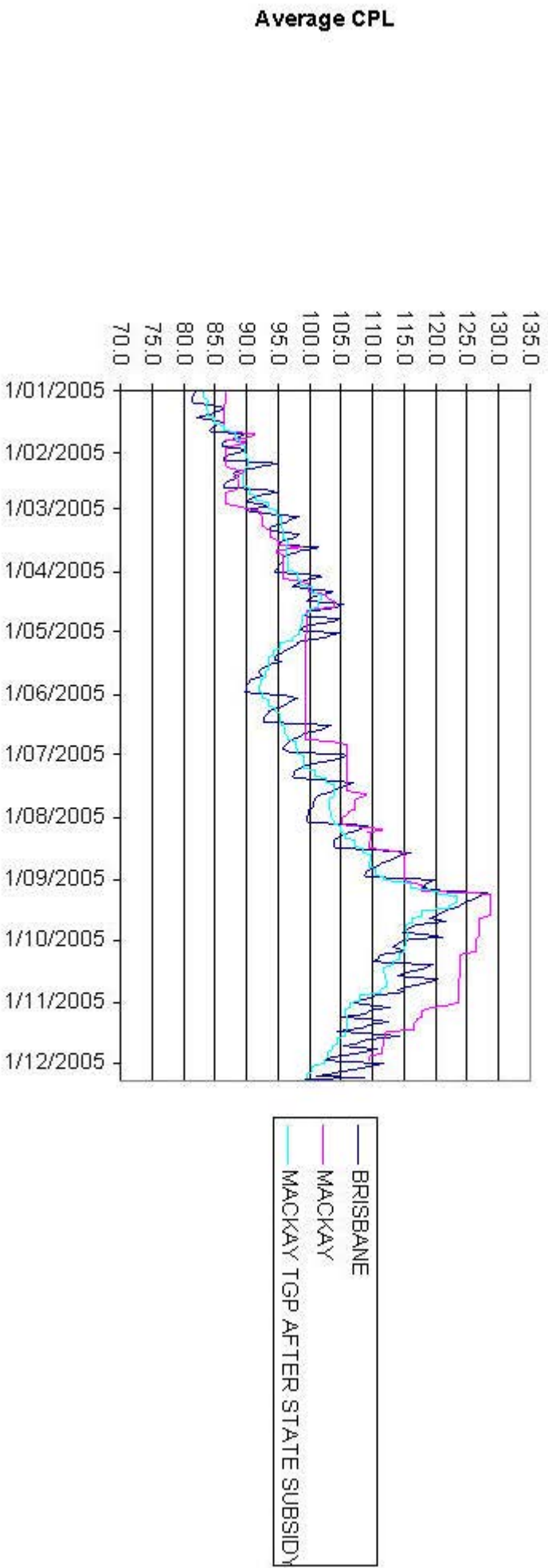


COLES EXPRESS BRISBANE AVG ULP BOARD PRICE / TGP/ TGP AFTER STATE SUBSIDY

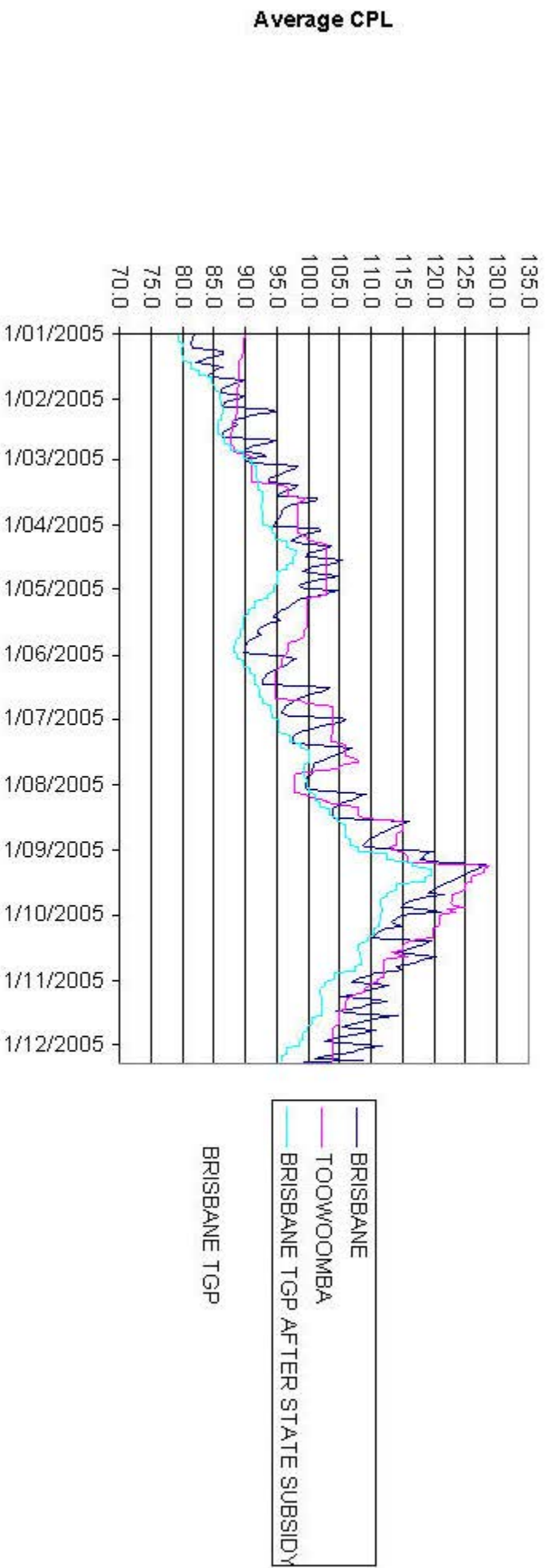
AVERGAE CPI



Coles Express Mackay and Brisbane Metro

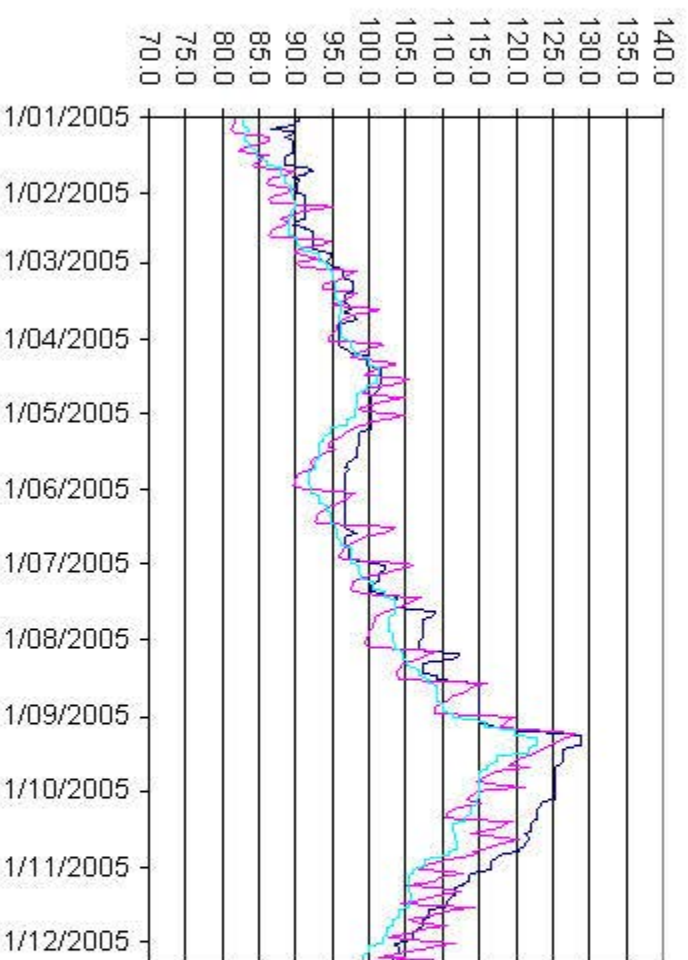


Coles Express Toowoomba and Brisbane Metro



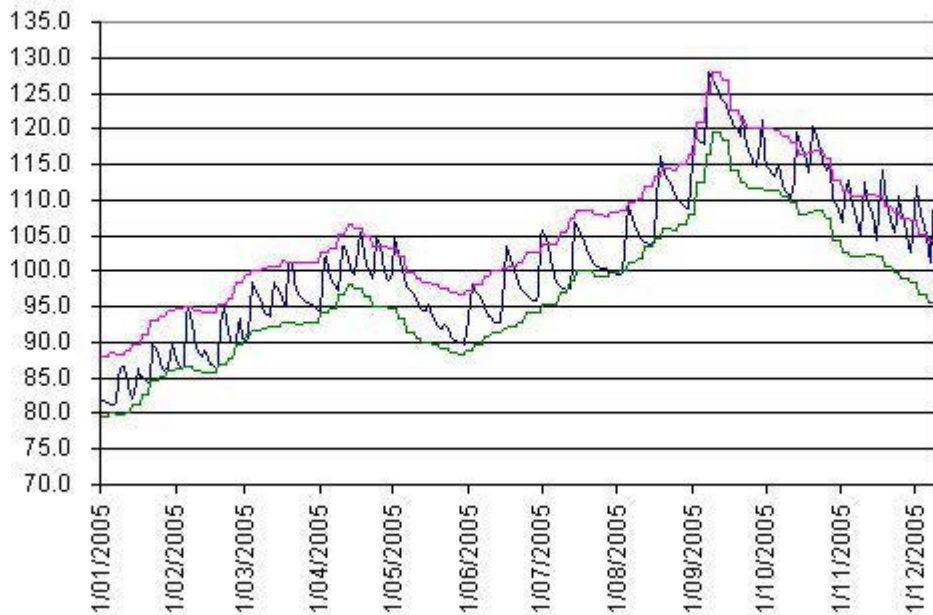
Coles Express Townsville and Brisbane Metro

Average CPL



COLES EXPRESS BRISBANE AVG ULP BOARD PRICE / TGP/ TGP AFTER STATE SUBSIDY

AVERGAE CPI



COLES EXPRESS BRISBANE
TGP
TGP AFTER STATE SUBSIDY