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Service Station Sales Fuel Strong Yields

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INTRODUCTION

The automotive fuel retailing industry is responsible for the sale of fuel, including petrol, LPG (Liquefied Petroleum Gas) and lubricating oils via approximately 8,000 service stations across Australia. The number of service stations has declined in recent years as the industry has restructured to meet changing market conditions.

Most service stations are now ‘self-service’ providing limited driveway services but increased store based amenity including a convenience store, supermarket, fast food outlet (or coffee shop), and in some cases, an adjoining automated car wash.

The industry has been rationalised in recent times, with the total number of service station sites decreasing by around 5% since 2000 however, down 50% on the corresponding number 25 years ago. While service stations’ main activity is retail sales of automotive fuel, none rely on fuel sales alone, which account for around 75% of total turnover.

SUPPLIERS

The major petroleum suppliers including Shell, Mobil, BP and Caltex operate – either through a franchise, lease or branding agreement – around 75% of service stations exclusively and supply 85% of fuel sales. The increasing number in recent years is directly correlated with the emergence of the supermarket majors and their partnership in the fuel market.

Wesfarmers Ltd, who owns the Coles brand, has co-branded with Shell and now owns the franchises for 620 Coles Express/Shell service stations nationally. Competitor Woolworths Petrol/Caltex operates nationally across 370 sites. It is in this respect that the industry has experienced major operational change.

According to research undertaken by the Australian Institute of Petroleum (AIP), the number of ‘supermarket network’ service stations totalled 153 at the end of 2000. Estimates of supermarket affiliated sites now represent well over half of total metropolitan fuel sales in Australia.

There are a number of smaller service station operators (including 7-Eleven, Newmanns Fuel, Freedom Fuels, United Petroleum, Peak and Liberty to name a few) that account for around a tenth of the market with the top five retailers encompassing an estimated 89% of the market in 2009.

There exists significant barriers to independent ownership and operation, including high purchase costs for existing sites, high construction costs for new sites, and the large outlay required to purchase considerable quantities of fuel which must be stored on-site.

The following table is an estimation of the key competitors within the automotive fuel retailing industry in Australia in 2009:

Company	Estimated Market Share %
Caltex Australia Ltd***	25%
Wesfarmers Ltd	22%
Woolworths Ltd	15%
BP Regional Australasia Pty Ltd	15%
Exxon Mobil Australia Pty Ltd	12%
Total	**89%**

Source: IBIS World; AIP; m3property Research

***Assumes Caltex acquisition of Mobil service stations is approved. The ACCC is yet to formally authorise Caltex's acquisition of 302 Mobil service stations for $300M in May 2009. The portfolio is located in metropolitan areas along the east coast, no sites will be acquired in Western Australia, Tasmania or the Northern Territory.

OPERATION

Entrance to the industry by the supermarket majors has had a significant effect on existing independent retailers through the offering of fuel discounts with the purchases of groceries or liquor in parent stores and service stations. This has changed the construct of the market, in which the consumer has traditionally exhibited little brand loyalty and instead will always seek the lowest price available.

The enticement to the supermarkets was the opportunity to capitalise on high customer volumes through expanding their operations into 'high profit ancillary convenience food and grocery retailing'. Sales of such ancillary items now account for approximately 16% of annual turnover. Whilst petrol sales are the primary generator of customer traffic, it is convenience retail uses which contribute the majority of profit.

INVESTMENT

Investors are attracted to service stations because of the long term leases in place to high calibre tenants and to their specialised nature offering a relatively high yielding investment. Service stations are generally in the sub-$5 million price range making them more affordable to a range of smaller investors and offer the future potential to redevelop the site into alternative uses.

There are some risks associated with investing in service stations, most notably relating to the potential volatility of income and capital value. Turnover is heavily reliant on easy access and good exposure for motorists while unforseen changes to adjoining roads and traffic flows can substantially impact on passing traffic to the extent that the service station may no longer be viable. When purchasing a service station, an alternative use of the property should always be investigated and considered should the need arise to redevelop or maximise the service station site's future potential.

Additionally, a challenge for investors in service stations can be the difficulty in assessing market rental. Rents can be complicated to analyse given that they are, in reality, a function of the total volume of fuel which is sold as well as any additional lines of business generating income.

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The following table identifies reported sales of service stations nationally in 2009, as detailed below:

Service Station	Sale Details ($M)	Sale Date	Site Area (sqm)	Initial Yield (%)
Woolworths Petrol, Cnr of Mann & Bent St, Nambucca Heads NSW	**$1.92**	Oct 09	942	7.81
7-Eleven, Pacific Hwy, Lisarow NSW	**$2.55**	Oct 09	2,609	9.30
Woolworths Petrol, 172 Thuringowa Rd, Kirwin QLD	**$0.75**	Sep 09	2,601	4.63
Woolworths Petrol, Cnr Bruce Hwy & Gedge St, Ingham QLD	**$0.62**	Sep 09	979	6.50
Woolworths Petrol, 95 Drayton St, Dalby QLD	**$0.64**	Sep 09	2,024	5.78
Woolworths Petrol, 6 Browns Dip Rd, Enoggera QLD	**$0.85**	Sep 09	1,487	4.39
Woolworths Petrol, 15 Warambie Rd, Karratha WA	**$0.67**	Sep 09	1,810	6.85
Volume Plus, 137 Campbell Hill Rd, Chester Hill NSW	**$2.60**	Sep 09	1,340	6.20
Woolworths Petrol, 236-246 Ginn Street, Gungahlin ACT	**$2.16**	Sep 09	4,121	4.57
Coles Express, 20 Clunes Rd, Creswick VIC	**$0.95**	Sep 09	1,750	9.00
Freedom Fuels, 8616 Warrego Hwy, Withcott QLD	**$2.48**	Aug 09	1,577	9.40
Woolworths Petrol, 103 Redbank Plains Rd, Goodna QLD	**$2.93**	Aug 09	6,324	7.87
7-Eleven, 510 Gowan Rd, Sunnybank Hills QLD	**$2.70**	Jun 09	2,255	8.14
Caltex, 126 Warwick Rd, Ipswich QLD	**$1.80**	May 09	3,033	8.01
Caltex, 37 Ilfracombe Rd, Longreach QLD	**$1.35**	Apr 09	2,529	11.30
BP, 162 Pioneer Rd, Wollongong NSW	**$1.08**	Mar 09	1,618	9.07
Freedom Fuels, 282 Ruthven St, Toowoomba QLD	**$3.50**	Feb 09	1,976	8.48
7-Eleven, 1 Broadwater Street, Runaway Bay QLD	**$2.58**	Jan 09	1,475	7.17

Source: m3property Research

OUTLOOK

Australia's service station industry has faced major regulatory changes in recent years to legislation and outlet operation enforcing significant change to the automotive fuel industry. Automotive fuels are generally acknowledged to have low price elasticity (the volume of fuel consumed does not change greatly in immediate response to price changes). Independent service stations have continued to be outpriced in the automotive fuels market and hence the industry is now driven by the major oil companies and the supermarket chains, Coles and Woolworths. Service station investment on long-term leases will continue to be eagerly contested by purchasers, particularly private investors. Many offer the security of a strong lease covenant to multi-national tenants and the longer term development potential for additional uses once the economic life of the site has run out.

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