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Fuel Supply to Rural Filling Stations

- **Fuel retailing in the UK is a very competitive business with pre-tax pump prices consistently amongst the cheapest in Europe.**
- **In rural areas filling stations tend to have lower throughputs of fuel, coupled with higher logistics and operating costs.**
- **Recently filling station closures have been averaging 420 each year, particularly smaller sites, due to a number of factors including strong competition between fuel retailers and the increasing costs of compliance with environmental regulations.**
- **The pressures on rural filling stations mirror those of other rural services.**

Background

Over the last twenty years the number of filling stations in the UK has reduced dramatically from about 17,000 in 1994 to 8,591 at the end of 2014. In most recent years, around 420 filling stations on average have been closing each year (Figure 1). The pressures on rural filling stations mirror those of other rural services such as shops and post offices, but there are some specific features affecting the fuel sector. Urban, main road and rural sites, whether oil company owned or independent, have all felt the impact of strong competition between fuel retailers, along with increasing regulatory and financial pressures.

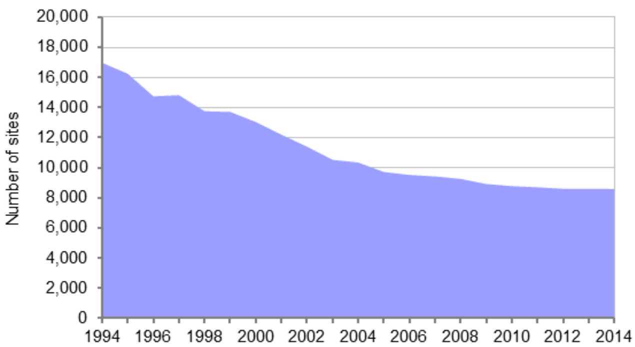

Figure 1: Retail site closures, 1994 – 2014
(Source: Experian Catalist 2006-2014 – EI Retail Marketing Survey 1994-2005)

Fuel Retailing in the UK

Fuel retailing in the UK is a high volume, low margin business, characterised by strong competition. These market conditions have hastened the closure of smaller, less well located sites, as retailers concentrate on higher volume sites capable of surviving in a lower margin environment.

A fuel station's viability is influenced by a function of volume of fuel sold and the difference between the retail pump price and the ex-refinery cost price of the fuel in the open market. This has favoured large service stations with lower overheads per litre sold, whilst many smaller filling stations, particularly in areas with lower population density, have been facing increasing challenges (or have become economically unviable). In recent years, whilst the number of filling stations owned and operated by both oil companies and independent retailers has declined, the number of supermarkets' sites has increased. Their share of the retail fuels' market has grown from 11% in 1992 to over 43.9% in 2014 *(Source: Experian Catalist)*, in an overall market which has seen little volume growth.

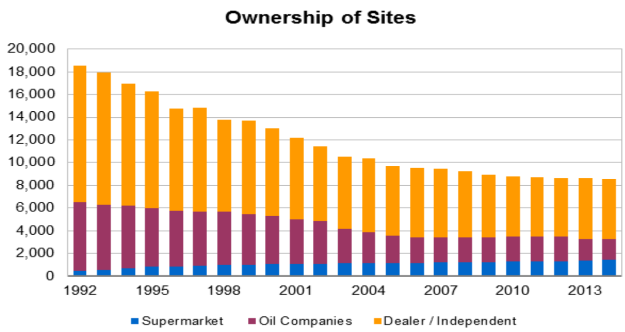

Figure 2: Ownership of Sites, 1992 – 2014
(Source: Experian Catalist 2006-2014 – EI Retail Marketing Survey 1992-2005)

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The supermarkets' growth in market share has coincided with a rapid expansion in the number of large out-of-town stores. The associated filling stations are able to sell large volumes of fuel (>12 million litres per year on average), particularly to people doing their weekly shopping, often cross-promoting a fuel discount to the amount spent in the main store. In comparison, the volume throughput of an average main road filling station may be around 4 million litres per year and that of a typical rural filling station may be less than 1-2 million litres a year (Figure 3).

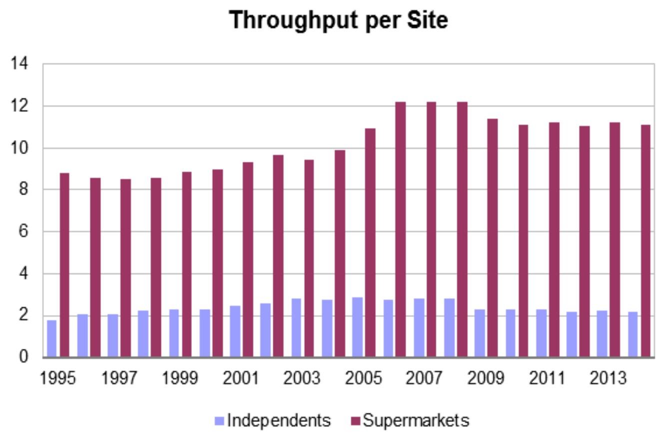

Figure 3: Average Throughput per Site, 1995 – 2014
(Source: DECC/Experian Catalist/EI)

Inevitably, the effect of strong competition together with low margins has come to represent one of the main causes for the closure of smaller or less well located filling stations, particularly in areas with lower population density.

Influences on final pump prices

The UKPIA briefing paper [‘Understanding Pump Prices’] explains the market mechanisms affecting pump prices. Pre-tax pump prices in the UK are consistently amongst the cheapest in Europe. However, it is clear that final pump prices do vary and location and size are a significant influence.

Price differentials between areas of dense population and rural locations will also, in part, be due to the increased delivery costs associated with supplies to outlying service stations, and complex logistics. Given that the volume of fuel sold by service stations in the extreme rural fringe will inevitably be low, there is a cost implication due to distance from the refinery - or main terminal - and the requirement to receive more frequent deliveries in less than full loads.

These higher costs along with other overheads such as fixed costs for staff, rent, rates, heat, light, water, maintenance and repair etc. can be expected to have an impact on the final pence per litre pump price.

However, rural sites are not alone in experiencing these economic dynamics. Service stations across the UK, below a viable volume throughput/shop turnover, have been closing in recent years.
The retail/ex-refinery price spread has ranged between 3 and 7 pence per litre (Figure 4) over the last nineteen years. This is not the final profit that the retailer makes; it is simply the difference between the cost of the wholesale price of fuel on the open market and the selling price on the forecourt. This has to cover fuel storage and delivery costs, the costs of running the filling station, as well as providing a return for the fuel supplier and retailer.

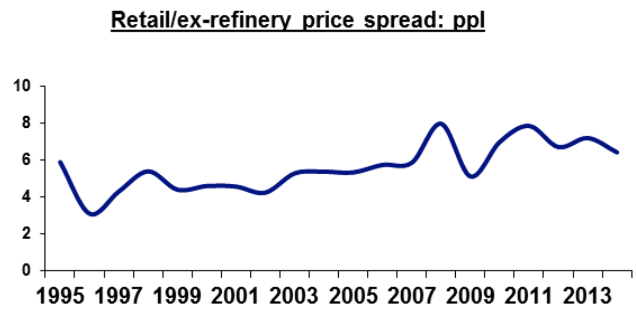

Figure 4: Retail/ex-refinery spread 1995 - 2014
(Source: Department of Energy & Climate Change using data from the European Commission Oil Bulletin)

Other Challenges

The increasing cost of compliance with environmental legislation – UK and EU - is a challenge for all sites but often presents an additional pressure for smaller/rural sites. Indeed, changes or updates associated with infrastructure – tanks, lines, pumps etc. – are often not viable for many sites. Whilst capital expenditure is easier to justify for larger retailers and supermarkets, as they sell enough volume, many smaller retailers struggle to justify the capital expenditure based on projected turnover and profitability levels.

Cost of product, as well as working capital, are also a challenge for the smaller/rural fuel retailer. The volatility of the retail price has a greater impact on retailers that sell lower volumes of fuel. For instance, in a declining market smaller retailers are often left with product bought some time ago at a high price. Whilst higher volume retailers might be able to sell at a lower price, the smaller retailer faces a loss or the possibility of keeping a higher price with low sale volumes. On the other hand, when prices are higher the small retailer may struggle to finance a load of fuel.

Over the years, a number of studies have looked at the impact of rural filling stations' closures – economic, social and environmental – and at measures that could be implemented to slow the rate of decline of smaller sites. Amongst a number of options that have been examined are: fuel duty and VAT differentials, above ground tanks/mobile petrol stations, unmanned stations and so on.

On 1st March 2012, the Rural Fuel Rebate Pilot Scheme came into force for the Inner & Outer Hebrides, Northern Isles, Islands in the Clyde and Isles of Scilly. Fuel retailers on the islands who have been able to apply for the scheme receive a 5p a litre rebate on the petrol and diesel they purchase; the full saving have to be passed on to the customer within 60 days.

In January 2014, it was announced that an application by the government to the European Commission was submitted for seventeen of the most rural areas in mainland UK to receive an up to 5 pence per litre (ppl) fuel duty discount. The application was approved by the EU Commissions on 15th January 2015 and by the Council of the European Union on 5th March 2015. The rebate was introduced on 31st May 2015.

Conclusions

There are a number of key factors that affect changes in the fuel retail market, such as competition, cost of product and working capital, along with the increasing cost of compliance with environmental legislation. These have particularly impacted smaller/rural filling stations in areas of lower population density. These factors are also reflected on the final pump price, which inevitably varies between areas of dense population and rural locations due to increased associated costs vs lower volumes of fuel sold.

Conclusions

Intense competition in fuel retailing is the major influence on the viability of rural filling stations. Regulatory pressures can also be a deciding factor in the decision to close individual sites.

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