



Submission to National Competition Council of Australia on Applications for Declaration of Jet Fuel Supply Infrastructure Services at Sydney Airport

The International Air Transport Association (IATA) represents some 230 airlines comprising 93% of scheduled international traffic. All the major scheduled airlines operating to Sydney Airport are members of IATA.

IATA fully supports the applications for declaration of services provided by jet fuel supply infrastructure and endorses the submissions made by the Board of Airline Representatives of Australia Inc (BARA) with regards to:

1. **Caltex pipeline** - the service provided by the Caltex pipeline facility, which transports jet fuel from interconnection points with off-site jet fuel storage facilities at Port Botany to the Sydney airport Joint User Hydrant Facility (JUHI); and
2. **Jet fuel storage and pipeline network / JUHI facility** - the services provided by the jet fuel storage facility (including facilities for refueling trucks) and jet fuel hydrant pipeline network facility provided by the JUHI at Sydney airport.

IATA wishes to provide additional inputs to the BARA submissions as follows:

Monopoly infrastructure, power to restrict access and the dominance of vertically integrated companies can compromise the effectiveness of competition among jet fuel suppliers at Sydney Airport and contribute to the problems of inadequate supply reliability and lack of price efficiency.

- Inadequate reliability of fuel supply - Poor reliability was identified by the Sydney Jet Fuel Infrastructure Working Group (SJFIWG) as a concern, evidenced by the increasing number of red and amber lights as well as occurrences of black lights. Since the completion of the SJFIWG report there is continued incidence of red lights at Sydney airport.
- Lack of price efficiency - Airlines have experienced rising fuel differentials (the component of fuel price that is above the international market price). Refueling at Sydney Airport has become significantly more expensive than at other regional airports such as Singapore, Kuala Lumpur, Bangkok and Hong Kong as evidenced in Figure 1 of BARA's application.
- Lack of competition among jet fuel suppliers - The jet fuel supply market to Sydney airport is dominated by a limited number of suppliers. Based on the SJFIWG report the implied market shares between existing oil companies and providers represents a concentrated market, with Caltex providing 55%, Shell 28%, while others (BP and Qantas) supplying about 17%¹. Based on this information, the Herfindahl-Hirschman

¹ In addition to these supplies, small shipments have been provided through trucking. According to the SJFIWG report, the critical supply situation in December 2009 warranted this additional supply method to be utilized to supplement the flow of jet fuel by approximately 0.2 ML per day, which represents about 1.5% of daily pipeline supply capacity.

Index (HHI)² would be about 4000, which is above acceptable levels and raises competition concerns.

- The Sydney JUHI is a natural monopoly - The JUHI infrastructure is the least cost way of providing the services offered by the network infrastructure for any foreseeable demand. As detailed in BARA's submissions, it is not feasible to have a second stand-alone network to provide the services currently offered by JUHI.
- The incumbent suppliers of jet fuel at Sydney Airport have considerable market power and are able to use it to restrict third-party access - There is limited access to services of the jet fuel supply infrastructure provided by JUHI at Sydney airport as participation in the joint venture is a requirement for access. The equity requirement hinders the potential entry of new suppliers by increasing the upfront costs incurred by new suppliers and the time to secure access. Non-discriminatory access to services across the supply network such as throughput agreements, including access to JUHI services, would allow new suppliers to more easily obtain entry into the jet fuel market at Sydney Airport.
- Ability to restrict access by a dominant vertically integrated company - Caltex is a dominant supplier with considerable market power. The dominance of Caltex is further strengthened by the ownership structure within the supply chain through being a vertically integrated company. Caltex produces and imports jet fuel, owns and controls the main jet fuel pipeline to Sydney Airport, is a member of JUHI and provides 'into-plane' services. As a vertically integrated company and particularly as the sole owner of the main jet fuel pipeline into JUHI, Caltex could choose to restrict third-party access to the market through different ways. Port Botany has the only common-user bulk liquids terminal in the region capable of supplying jet fuel to Sydney airport. Despite the capacity to provide 7.9 ML per day through Port Botany, the access restrictions imposed by Caltex³ have resulted in a maximum potential utilization rate of only about 16%.

Recent developments in the Sydney jet fuel supply market raise concerns of further dulling of competition

- Increase of capacity at the Kurnell refinery could lead to further restriction of third party access to services offered through the Caltex pipeline. The announcement by Caltex to increase the capacity of the link between the Kurnell refinery and the rest of the Caltex pipeline would increase throughput capacity from the Kurnell refinery from 5ML to about 10ML per day. Caltex would be in a position to supply a greater share of the throughput capacity compared to current levels. This would effectively mean

² The HHI measures the size of the firms in relation to the industry and serves as an indicator on the amount of competition among them. It is defined as the sum of the squares of the market shares of the 50 largest firms or summed over all the firms if there are fewer than 50. As a point of comparison, the ACCC 2008 Merger Guidelines indicate that in cases of mergers that create market conditions where the HHI is over 2000 it is more likely to identify competition concerns.

³ Limiting access to the Caltex pipeline from Port Botany to 60 days per year

that Caltex would have even more incentive to limit third-party access to the services it provides through the Caltex pipeline from the Port Botany terminal.

- Given the high industry concentration, the transformation of the Clyde refinery to an import-only terminal is unlikely to lead to higher competition under current market conditions.
 - One scenario is if Shell is unable to increase throughput of jet fuel from the Clyde facility. That would lead to further strengthening of the dependence on the Caltex pipeline.
 - Another scenario is if Shell is able to marginally increase supply through its pipeline, Caltex would be in a position to counter such increases through either reducing its sales and/or restricting access of other suppliers to the Caltex pipeline. Despite potential losses in revenue if Caltex chooses to decrease sales in the short term, it would likely be in a position to recover these losses in the medium to long term due to projected growth in jet fuel demand at Sydney Airport. However, given Shell's position in the market as the second largest supplier, it is unlikely to choose to compete aggressively on price with Caltex to expand sales because that would likely lead to a fall in total profits.

Promoting competition through open access to services of the supply infrastructure for qualified entities wishing to supply jet fuel to the Sydney airport would drive price efficiency, enhance security of supply and allow for timely infrastructure investment.

- Uneconomic to develop another pipeline facility – As detailed by BARA in the application for declaration and its supplementary submission of 4 November 2011, it is uneconomical for anyone to develop another pipeline facility into JUHI to provide the service.
- Driving price efficiency - Open access to services of the supply infrastructure is an essential component to promoting overall competition in the Sydney airport jet fuel market. With the exception of Qantas, which is engaged in the market primarily for self-supply, there has not been entry of a new supplier at Sydney airport for many years. This is in part attributed to a lack of options for new suppliers to bring imported fuel into the airport. As pointed out earlier, Port Botany has the only common-user bulk liquids terminal in the region capable of linking to the jet fuel supply infrastructure to Sydney airport. While this facility has the needed infrastructure to supply significant quantities⁴ of jet fuel to Sydney airport, access restrictions to the services of the Caltex pipeline have proved to be a limiting factor. For a true open access environment to exist there has to be common-use infrastructure that provides non-discriminatory access to services across the entire supply network to any qualified entity wishing to supply fuel to the airport. Open access ensures increased competition that drives price efficiency. To complement that and avoid restriction of

⁴ The Caltex pipeline is capable of transferring 7.9 ML per day from the Vopak facility in Port Botany. Vopak advised the SJFIWG that it is in a position to further upgrade its pipeline to a pumping capacity of 10 ML per day from the Vopak storage facility to Sydney Airport if sufficient access is granted to the Caltex pipeline.

access through excessive service pricing or other measures, all fuel logistical facilities should have non-discriminatory access, including on airport fuel storage and hydrant system operations. Extending open access to services of the supply infrastructure at the airport, in conjunction with supply services off-airport, would give the certainty needed to potential third-part entrants to enter the market.

- Enhanced security of supply – Open access to JUHI services coupled with open access to services of the supply infrastructure leading to the airport provides greater confidence to potential new entrants and encourages a larger number of suppliers to enter the market. This will enhance supply reliability given that the system would not be reliant on stocks provided by a fixed number of suppliers. While there is sufficient potential jet fuel storage capacity off-airport,⁵ access to these storage facilities is constrained by access to the Caltex pipeline, particularly at the Vopak and ExxonMobil facilities. By opening access to the services of the Caltex pipeline it would be possible to realize the opportunity to access higher quantities of storage capacity off-airport, which would further contribute to enhanced security of supply. In the longer term, if access remains constrained, these terminals may reallocate storage capacity away from jet fuel thereby shrinking off-airport jet fuel storage capacity.
- Allowing for timely infrastructure investment –
 - The SJFIWG identified availability of access to the Caltex pipeline from Port Botany as critical to ensuring that jet fuel supply to Sydney Airport will be adequate to meet projected jet fuel demand requirements particularly in the short term – till 2019, but also in the longer term. Given that Port Botany is operating close to its economic optimum utilization there are plans to supplement it with a second berth in approximately 2012. In this context, the availability of open access to the Caltex pipeline can help facilitate the planning of investments, which can further contribute to promoting security of supply and driving price efficiency.
 - The SJFIWG report also identified insufficient on-airport storage capacity to meet the storage capability criteria from 2014, requiring significant capital investment. Investments are also envisioned to be needed in the short and more significantly in the long term for the on-airport hydrant system. Increasing certainty on access terms to JUHI services and reliability of supply can strengthen confidence in revenue projections and catalyze needed investment, not only from incumbent suppliers but potentially also other investors. An added benefit from improved price efficiency is that it would boost demand on jet fuel which may further contribute to increasing revenues from JUHI services and incentivize needed investment.

⁵ The SJFIWG estimated that theoretical maximum off-airport storage capacity at the Clyde refinery, Kurnell refinery, Vopak facility and ExxonMobil terminal currently totals 196 ML of which a significant portion is at the Vopak facility (91ML) and the ExxonMobil terminal (18ML).