

For Information  
On 26 March 2007

**Legislative Council Panel on Economic Services**

**AUTO-FUEL PRICES AND  
FUEL SURCHARGES ON AIR PASSENGERS**

**INTRODUCTION**

This paper briefs Members on the monitoring of auto-fuel retail prices and approval of fuel surcharge on air passengers.

**AUTO-FUEL PRICES**

**Background**

2. There are eight suppliers operating a total of about 180 Petrol Filling Stations (PFS) in the Hong Kong retail auto-fuel market: ExxonMobil, Shell, Chevron (Caltex), CRC, Sinopec, Chinaoil, Feoso Oil and Concord Oil. The number of PFS under each company as at 1 March 2007 is at Annex I.

Annex I

3. The retail prices of auto-fuels have been a matter of public concern. Some motorists consider that Hong Kong's auto-fuel prices excluding tax are among the highest in the world and that oil companies are prompt in increasing their pump prices when international oil price is rising, but slow in responding when international oil price is falling.

4. While the oil companies declined to supply detailed cost information on grounds of commercial sensitivity, they have provided some general information and comments on their business operation in response to these criticisms as follows –

- (i) all oil products in Hong Kong are imported and for environmental and other reasons, the quality of auto-fuels used in Hong Kong is generally better than other places. In addition, the land and labour costs of local PFS are relatively higher;

- (ii) market demand for unleaded petrol and ultra low sulphur diesel (ULSD) has declined continuously in recent years due to various factors such as the development of mass transit infrastructure and the replacement of diesel by auto-LPG as fuels for taxis and minibuses;
- (iii) with increased competition in a shrinking market as explained in (ii) above, oil companies are offering more discounts in one form or another (such as loyalty points, rebates, discount coupons) and the discount levels have also increased significantly. So consumers are now paying considerably less than the pump prices; and
- (iv) the fixed costs of the oil companies, including land premium and rent, advertising and promotional costs and safety and environmental costs, have increased considerably, while economies of scale have been eroded with the decline in sales volume.

### **Monitoring of auto-fuel retail prices**

5. Retail prices of auto-fuel in Hong Kong are determined by oil companies having regard to international oil prices, commercial practices and their operating costs. We appreciate the impact of the auto-fuel prices on the local economy and therefore have been monitoring whether changes in local pump prices of auto-fuel are broadly in line with trend movements of international oil prices as reflected by prices for Brent Crude oil and Singapore free-on-board (FOB) prices for unleaded petrol and diesel. We note that in recent years, international oil prices have been very volatile. We have all along kept in contact with the oil companies and urged them to reduce their prices once there is room for downward adjustment.

6. However, in a free market economy, the Government does not have the power to dictate the retail prices of auto-fuels. The Government's objectives are to maintain a stable fuel supply, encourage transparency and enhance competition by removing barriers to entry into the fuel market.

### **Oil Price Movements**

7. To enhance transparency, the Census and Statistics Department (C&SD) publishes the monthly average import prices of major oil products

which, despite their limitations<sup>Note(1)</sup>, provide some indications of the trend movements of import prices of oil products. The oil companies have now, at our request, included in their announcement of each intended price adjustment of auto-fuels the rationale for the adjustment. In addition, for all new PFS sites tendered out, there is a new lease condition requiring PFS to display price information boards.

Annexes  
II & III

8. Annex II and Annex III show the respective changes in local retail prices<sup>Note(2)</sup> of unleaded petrol and ULSD since January 2006, as compared with the trend movements of the monthly average Singapore FOB prices, the C&SD's weighted average import prices and the monthly average prices for Brent Crude oil. It is noted that –

- (i) Singapore FOB prices and import prices for unleaded petrol and diesel as well as international prices for Brent Crude oil had been on an increasing trend and reached record high levels around the middle of last year. Since August 2006, international oil prices fell significantly, but recently the trend reversed and oil prices rose considerably in the past few weeks; and
- (ii) From January 2006 to February 2007, retail prices for unleaded petrol at local PFS had been increased six times and lowered five times and retail prices for ULSD at local PFS had been increased six times and lowered four times. There were two occasions in early 2006 when certain oil companies did not follow the increases in pump prices of unleaded petrol made by the other companies.

Generally speaking, changes in local pump prices of auto-fuel have been broadly in line with the trend movements of international oil prices.

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<sup>Note(1)</sup> These data have their limitations. For instance, as the C&SD's figures reflect the average value of imported consignments declared by the oil companies in a particular month, they may differ from the actual prices of the consignments of individual oil companies. Moreover, the consignments involved may not be purchased or sold in the retail market in the month when the declarations are made. As C&SD needs time to collect and process the information, there is also a time lag of about four weeks between the time of declaration and the availability of such data.

<sup>Note(2)</sup> The prices quoted represent the month-end prices of one of the major oil companies. There were minor variations in the pump prices of unleaded petrol or ULSD among the oil companies generally in the range of about \$0.01 and a difference in the effective dates of each price adjustment in the range of about 1 to 3 days.

9. Nevertheless, prices of refined oil products (such as unleaded petrol and ULSD) are affected not only by crude oil prices, but also subject to various factors, such as the supply and demand in the market, the productivity of the refinery, the costs of raw materials and refinery process as well as the transportation costs etc. Therefore, changes in prices of unleaded petrol and ULSD may not be exactly the same as those of crude oil prices.

10. Moreover, local pump prices of auto-fuel include not only the import costs and duty, but also discounts offered by oil companies and other operating costs. Therefore, although the adjustments in local pump prices should be broadly in line with trend movements and magnitude of changes in import prices, their respective percentage changes will not be exactly the same as such percentages are calculated on different bases.

### **Enhancing Competition**

11. Apart from monitoring oil prices, the Government has taken measures in the past few years to encourage new operators to tender for PFS sites –

- (i) since July 2000, existing PFS sites are put up for tender upon lease expiry instead of automatically renewing the tenancy as it had been the case previously; and
- (ii) since June 2003, PFS sites are tendered in batches to facilitate potential new entrants in acquiring a critical mass of PFS sites to achieve economy of scale. Two new players, Sinopec and Chinaoil, have since won tenders and entered the market. As at 1 March 2007, 11 and 5 PFS are being managed by Sinopec and Chinaoil respectively.

12. In view of the public's concern about the local auto-fuel retail market, the Competition Policy Advisory Group (COMPAG) commissioned a consultant in 2005 to conduct a comprehensive study on the competition situation in the auto-fuel retail market in Hong Kong. The consultant's report was released in April 2006. The consultant concluded, after detailed examination of the structure, operating costs and retail pricing of the local auto-fuel retail market, that there was no clear evidence of collusion by the oil companies in setting prices for auto-fuels. Nevertheless, the consultant recommended that the Government should consider preventive measures against cartel behaviour through competition laws.

13. In parallel, the COMPAG appointed a Competition Policy Review Committee (CPRC) in June 2005 to review Hong Kong's competition policy. Taking into account the consultant's report on the competition situation in the auto-fuel market in Hong Kong, the Committee completed its review and released its report in July 2006. It recommended that Hong Kong should introduce a cross-sector competition law targeting anti-competitive conduct and that such a law should be enforced by an independent Competition Commission. The Government has carefully considered the relevant recommendations and issued a public discussion document in November 2006 for a three-month public consultation. We have analysed views expressed by stakeholders during the discussion process and compiled a report on the feedback, on which we will brief this Panel. Any future measures against anti-competition behaviour should also apply to the auto-fuel retail market.

## **FUEL SURCHARGES ON AIR PASSENGERS**

### **Background**

14. In March 2003, having taken account of the sudden rise in aviation fuel prices at the time, the Civil Aviation Department (CAD) approved for the first time applications from seven airline operators to collect passenger fuel surcharges. The approval was valid for three months, and was not renewed upon expiry when fuel prices returned to more or less the original level. Subsequently, as aviation fuel prices rose again, approval was given in June 2004 to airline operators to collect passenger fuel surcharges. The approval has since been reviewed regularly<sup>Note(3)</sup>, taking account of changes in aviation fuel prices and other relevant factors which are discussed below.

### **Factors Applicable to Determination and Approval**

15. Fuel surcharge allows airline operators to partially recover the increase in operating cost due to fluctuations in aviation fuel prices. In accordance with the existing bilateral air services agreements, airline operators should consider all relevant factors including their operating costs, the passenger interests and the tariffs charged by other operators on the same routes in determining their tariffs, and shall only levy the tariffs with

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<sup>Note(3)</sup> Initially at tri-monthly intervals, which was subsequently changed to bi-monthly in December 2004 in order to follow more closely changes in aviation fuel prices.

the approval of the relevant aeronautical authorities. CAD will take into account changes in the prices of aviation fuel, the justifications provided by the airline operators and other relevant factors when approving passenger fuel surcharge applications.

16. When approving passenger fuel surcharges, CAD would ensure that the revenue so generated would not exceed the additional costs borne by the airline operators due to increased aviation fuel prices during the corresponding period.

17. Given the fluctuation in aviation fuel prices, CAD only approves passenger fuel surcharges to be levied on a short term basis, in general over a two-month period. The present fuel surcharges will lapse on 31 March 2007.

18. Over the period from June 2004 to February 2007, the fuel surcharges levied on passengers by airline operators were adjusted on 13 occasions, nine of which were upward and four of which downward adjustments. Since June 2004, the amount of passenger fuel surcharges collected by airline operators represents approximately half of the additional costs borne by the airlines for passenger carriage which have arisen due to increased fuel prices over the same period.

### **Latest Situation**

19. According to information provided by CAD, at the international level, the average fuel surcharges levied in other places on major routes stood at about \$260 (for short haul flights) and \$560 (for long haul flights) per passenger, whereas the fuel surcharges by the major Mainland airlines operating to international destinations (other than Hong Kong) stood at about \$310 (short haul) and \$470 (long haul) per passenger. Against these figures, the fuel surcharges levied in Hong Kong on major routes as from February 2007, at \$106 (short haul) and \$438 (long haul), are at a reasonable level.

20. Currently, 58 airlines operating services to and from Hong Kong have obtained approval to levy passenger fuel surcharges.

## Annex I

### Petrol Filling Stations in Hong Kong (as at 1 March 2007)

	<u>No. of Stations</u>	<u>%</u>
ExxonMobil HK Ltd. (埃克森美孚)	52 <sup>(Note)</sup>	28
Shell HK Ltd. (蜆殼)	49	26
Chevron HK Ltd. (加德士)	47	25
CRC Petrol Filling Station Co., Ltd. (華潤)	13	7
Sinopec (HK) Ltd. (中國石化)	11	6
Chinaoil (HK) Corporation Ltd. (中國石油)	5	3
Feoso Oil Ltd. (東方石油) (operated under brand name of Esso and Feoso)	7	4
Concord Oil (HK) Ltd. (協和石油)	1 —	1 —
	<u>185</u>	<u>100</u>

Note : Including 1 PFS owned by joint venture of ExxonMobil and Concord.

## Comparison of Movements of Pump Price of Unleaded Petrol against Relevant Indicators

Month	Pump Price of Regular Unleaded Petrol as at Month End (Ron 98) (Note 1) HK\$/litre	No. of Adjustments	Monthly Average Singapore FOB Unleaded Petrol Price (Ron 97) (Note 2) HK\$/litre equivalent	Monthly Weighted Average Import Cost of Unleaded Petrol (for reference) (Note 3) HK\$/litre	Monthly Average Mid Price of Brent Crude (for reference) (Note 4) HK\$/litre equivalent
Dec 2005	12.69		3.04	3.37	2.79
	+0.30	(2 ↑)	+0.33	+0.33	+0.33
Jan 2006	12.99		3.37	3.70	3.12
	-0.10	(1 ↓)	-0.06	+0.04	-0.18
Feb 2006	12.89		3.31	3.74	2.94
	+0.00		+0.20	+0.11	+0.12
Mar 2006	12.89		3.51	3.85	3.06
	+0.60	(3 ↑)	+0.57	+0.47	+0.39
Apr 2006	13.49		4.08	4.32	3.45
	+0.20	(1 ↑)	+0.28	+0.51	+0.00
May 2006	13.69		4.36	4.83	3.45
	+0.00		-0.18	-0.12	-0.07
Jun 2006	13.69		4.18	4.71	3.38
	+0.00		+0.13	+0.00	+0.24
Jul 2006	13.69		4.31	4.71	3.62
	+0.00		-0.17	+0.00	-0.01
Aug 2006	13.69		4.14	4.71	3.61
	-0.40	(2 ↓)	-0.77	-0.85	-0.53
Sep 2006	13.29		3.37	3.86	3.08
	-0.15	(1 ↓)	-0.20	-0.16	-0.22
Oct 2006	13.14		3.17	3.70	2.86
	+0.00		+0.05	-0.09	+0.01
Nov 2006	13.14		3.22	3.61	2.87
	+0.00		+0.21	+0.12	+0.19
Dec 2006	13.14		3.43	3.73	3.06
	-0.15	(1 ↓)	-0.31	-0.08	-0.39
Jan 2007	12.99		3.12	3.65	2.67
	+0.00		+0.27		+0.17
Feb 2007	12.99		3.39	Not yet available	2.84
<b>Net movement since 2006</b>	<b>+0.30</b>		<b>+0.35</b>		<b>+0.05</b>

Note (1) : The prices quoted represent the month-end prices of one of the major oil companies . There were minor variations in the pump prices among the oil companies (generally in the range of about \$0.01) and a difference in the effective dates of each price adjustment in the range of about 1 to 3 days.

(2) : Source : Argus Media -  
As Singapore FOB price for unleaded petrol of Ron 98 is not available, that of Ron 97 has been used as the benchmark for monitoring the trend movement of unleaded petrol pump prices in Hong Kong.

(3) : Source : The Census and Statistics Department (C&SD) -  
The monthly figures reflect the average values of imported consignments declared by the oil companies in a particular month. The consignments involved, however, may not be purchased or sold in the retail market in the month when the declarations are made.

(4) : Source : bloomberg.com

(5) : There were two occasions in early 2006 when certain oil companies did not follow the increases in pump prices of unleaded petrol made by the other companies:

(i) On 27 January 2006, one oil company did not follow the increase of pump price of \$0.10/litre made by other oil companies included in the above table.

(ii) On 25 February 2006, one oil company made an increase of \$0.10/litre, but other companies did not follow and the same company reversed the increase on 15 March 2006. These adjustments by only one oil company were not reflected in the above table.



## Comparison of Movements of Pump Price of ULSD against Relevant Indicators

Month	Pump Price of ULSD as at Month End (0.005% Sulphur) (Note 1) HK\$/litre	No. of Adjustments	Monthly Average Singapore FOB Diesel Price (0.5% Sulphur) (Note 2) HK\$/litre equivalent	Monthly Weighted Average Import Cost of ULSD (for reference) (Note 3) HK\$/litre	Monthly Average Mid Price of Brent Crude (for reference) (Note 4) HK\$/litre equivalent
Dec 2005	8.07		3.13	3.34	2.79
Jan 2006	8.27	+0.20 (2 ↑)	3.40	3.64	3.12
Feb 2006	8.17	-0.10 (1 ↓)	3.24	3.65	2.94
Mar 2006	8.27	+0.10 (1 ↑)	3.54	3.84	3.06
Apr 2006	8.87	+0.60 (3 ↑)	4.07	4.22	3.45
May 2006	8.87	+0.00	4.13	4.45	3.45
Jun 2006	8.87	+0.00	4.21	4.48	3.38
Jul 2006	8.87	+0.00	4.23	4.50	3.62
Aug 2006	8.87	+0.00	4.23	4.49	3.61
Sep 2006	8.72	-0.15 (1 ↓)	3.73	4.15	3.08
Oct 2006	8.57	-0.15 (1 ↓)	3.49	3.80	2.86
Nov 2006	8.57	+0.00	3.43	3.63	2.87
Dec 2006	8.57	+0.00	3.42	3.64	3.06
Jan 2007	8.37	-0.20 (1 ↓)	3.25	3.51	2.67
Feb 2007	8.37	+0.00	3.46	Not yet available	2.84
<b>Net movement since 2006</b>	<b>+0.30</b>		<b>+0.33</b>		<b>+0.05</b>

Note (1): The prices quoted represent the month-end prices of one of the major oil companies. There were minor variations in the pump prices among the oil companies (generally in the range of about \$0.01) and a difference in the effective dates of each price adjustment in the range of about 1 to 3 days.

(2): Source : Argus Media. ULSD with 0.005% sulphur level used in Hong Kong is not commonly used in Asia. Singapore FOB price for diesel of 0.5% sulphur level has been used as the benchmark for monitoring the trend movement of ULSD pump prices in Hong Kong.

(3): Source : The Census and Statistics Department (C&SD). The monthly figures reflect the average values of imported consignments declared by the oil companies in a particular month. The consignments involved, however, may not be purchased or sold in the retail market in the month when the declarations are made.

(4): Source : bloomberg.com