



Sydney Petrol Prices

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*This is a guest post from **Sean Carmody** of [A Stubborn Mule's Perspective](#).*

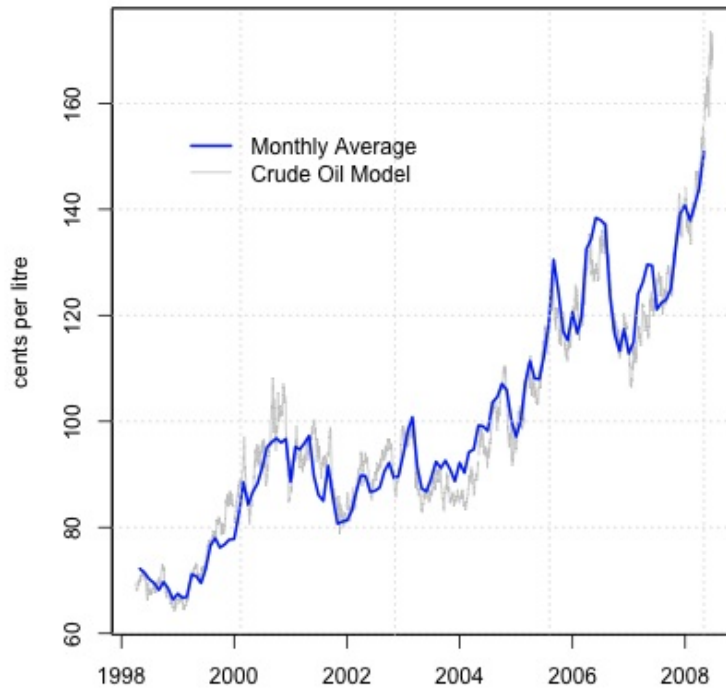
Soaring petrol prices have led to all sorts of calls for action to help reduce prices. The Opposition called for a [5 cents per litre reduction in the excise on petrol](#), which currently stands at 38.1 cents per litre. One Victorian Liberal MP, Chris Pearce, went further and [called for a 10 cent reduction in petrol excise](#). The Rudd Government initially claimed that there was nothing more that they could do, but then buckled to the pressure and has proposed the introduction of a [national FuelWatch scheme](#) aimed at promoting price transparency at the bowser. The Minister for Competition Policy & Consumer Affairs, Chris Bowen, [has indicated](#) that this scheme is expected to save around 2 cents per litre. So, what is going on with petrol prices and what are the merits of these proposals?

As a starting point, it is useful to have a look at the breakdown of the price at the pump. The retail price of petrol is basically equal to

Price of Crude Oil + Refining Margin + Excise + Retailer Margin + GST

This is a bit of an oversimplification and bundles together the cost of refining and profit under “refining margin” and the retailer’s costs (such as transport) and profit under “retailer margin”. Given all the media attention, it is hard to miss the fact that the price of crude oil has been skyrocketing and simple regression analysis confirms that this is the primary driver of petrol price rises. Refining and retailer margins have been far more stable, opportunistic service station proprietors are not really the root cause of the problem.

The chart below shows a comparison of Sydney average monthly petrol prices with prices from the regression model (for the statistically-minded, the R^2 is 96%). The slope of the regression confirms the commonly quoted rule of thumb that a US \$1 increase in the price of a barrel of crude oil will result in an increase of 1 cent per litre at the pump (more precisely the model says 0.87 cents, but that’s close enough to 1 cent: it is a crude model after all...no apologies for the pun).



Regression Model of Sydney Petrol Prices (unleaded)*

The average price of unleaded petrol in Sydney in May was 150.8 cents per litre. Yesterday our local service station was charging 163 cents per litre, so prices are already up more than ten cents in a month. Based on Friday's crude oil price, the model is suggesting that there is another 10 cents to go on top of that. Last week [comments from Libya](#) about restricting oil supply helped push the price up crude oil up by US \$5 per barrel (up 5 cents at the pump). A week earlier, [moves by China to decrease fuel subsidies](#) triggered a US \$4 price fall (down 4 cents at the pump). So the realpolitik of oil is triggering larger moves in petrol prices on a daily basis than either the anticipated 2 cent saving of FuelWatch or even the 4 cent GST reduction proposed by the Opposition. These ideas start to look like a drop in the ocean, and expensive drops as that!

According to the [most recent Federal budget](#), Government income from excise on petrol is forecast to be almost \$7 billion per year, so cutting petrol excise by 5 cents could cost around \$900 million per year in tax revenue for the Commonwealth. Chris Pearce's more extravagant proposal would cost the Commonwealth more than \$1.5 billion a year in excise revenue! If diesel is included, the figures would be doubled. That is a lot of tax dollars to spend on savings at the pump which could be blown away by a casual remark to the world press by Libya, China or Saudi Arabia.

By contrast, FuelWatch almost seems like a bargain as [it is expected](#) to cost taxpayers a mere \$20 million. But is that really \$20 million well-spent? Complying with the scheme will cost petrol retailers money and, as their margins are already fairly slim, that is a cost that will certainly end up being passed on to drivers. So I am not convinced that the touted savings will materialise, but even if they do, will anyone notice? If oil prices keep rising, so will petrol prices and by much more than 2 cents. If it turns out that we are in the middle of a speculative bubble, oil and petrol prices will collapse at some point and everyone will forget we ever had a problem (for a while at least).

Either way, the best thing that I can find to say about the FuelWatch scheme is that it is the cheapest of the pointless initiatives that our politicians have come up with. If there is \$20 million dollars of budget surplus up for grabs, surely there are better ways to spend it!

* Data Sources: Sydney Petrol Prices from the [Australian Automobile Association](#), Brent crude oil



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