# Lebanese Gas Stations: Tied with Regulation

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The collapse in global crude oil prices since June 2014 had a significant impact on economies, governments and business. Lebanon was no exception to this rule. One of the local markets to bear the brunt of these changes was the fuel oil industry, which has witnessed several changes in its market dynamics due to not only the economic factors dictating their businesses, but local social factors as well.

The fuel oil industry in Lebanon is a saturated market, with 13 licensed oil importers and distributors. Lebanon's distribution network consists of around 2,200 registered service stations, with a further 1,000 rumored to be operating without the required permits.

This market is dominated by Total, Medco-Phoenicia, and Hypco, which hold a combined market share exceeding 50%. Other remaining significant oil importers control roughly equal shares to complete the market.

In terms of the number of service stations, Medco-Phoenicia ranks first, with 320 stations, followed by Coral with more than 200 stations. United comes third with 189 gas stations, However, this large number has not translated in to a higher market share for United. This can probably be explained by United not operating in more prime locations, such as on main roads and highways.

There exist some barriers to enter the fuel oil market in Lebanon. The potential entrant should comply with the rules set by the Ministry of Energy and Water, obtain a permit to open a gas station, acquire a license to import, attain a terminal on the port, purchase a suitable land, and have the necessary infrastructure for oil importing. However, in the past couple of years, the government has not been authorizing entry to this market. This is due to the presidential vacuum, and the fact that the market is highly saturated with around one gas station every 3 km[1]. One source claimed that Lebanon has 7 times more stations than needed.

Demand for fuel oil in Lebanon is considered inelastic to price fluctuations as it is deemed to be a necessity. Nonetheless, this demand is seasonal, considering the increased demand for fuel during summer and holidays. Average consumption currently stands at 5-6M liters per day. This number has been witnessing an increasing trend over the past 2 years, due to the increase in refugees. However, it has partially faced headwinds due the decrease in tourist activity, where one oil importer claimed it faced a 20% lower demand during the past 2 years.

On the international trade front, imports of mineral products to Lebanon grew by 5.71% year-on-year to 5.99M tons in 2015, however at a 30.07% decline in value to $3.32M. This is caused by the 49.71% plunge in the price of Brent Crude oil. Lebanon imported 21.57% mineral products from Greece, 19.31% from Russia, 10.76% from France, 10.72% from Italy, and 9.26% from Kuwait. Fuel oil is subject to almost 7,000L.L/tank in custom duty and VAT payments.

The selling price of fuel in Lebanon is set by the government. The ministry of energy and water changes the price of fuel every Wednesday. The price is calculated using the four-week average of international prices based on Platts. (Platts is a provider of energy and metals information and a source of benchmark price assessments in the physical energy markets.)

Price Structure (in L.L./tank) as of 8th of February 2016

| | Unleaded 98 Octane | Unleaded 95 Octane | Gas Oil | Diesel Oil |
|---|---|---|---|---|
| **Cost** | 10,580 | 10,020 | 8,040 | 8,240 |
| **Customs** | 4,950 | 5,060 | - | - |
| **Profits of Distributing Company** | 300 | 300 | 300 | 300 |
| **Transportation Costs** | 360 | 360 | 360 | 360 |
| **Profits of Gas Station** | 1,900 | 1,900 | 700 | 700 |
| **Total Cost Excluding VAT** | 18,090 | 17,640 | 9,400 | 9,600 |
| **VAT** | 1,809 | 1,764 | Exempted | Exempted |
| **Selling Price** | 19,900 | 19,400 | 9,400 | 9,600 |

Source: MOEW

To protect themselves against global price fluctuations, oil importers adopt hedging strategies. For instance, one importer stated that it synchronizes its imports based on a 4-week moving average. One source claimed that he does not use any hedging strategy, as no one can predict for sure the movement of international prices. Globally, oil importers typically hedge against change in prices by locking in some of their future imports at favorable prices through swap transactions sold by banks, or by buying options as insurance against change in prices.

[1] As mentioned in the article "What a Gas" in Executive Magazine"

Moreover, gas stations also defend their profits from a change in the regulated selling price. When they expect the government will increase prices, they store more fuel to sell it when the rule is exercised. Similarly, the stations decrease their fuel storage when anticipating a price decline.

Aside from their major fuel-services, many gas stations follow international trends by including small shops, restaurants and ATMs. These non-fuel services constitute a small share of around 6% of the total revenues of gas stations. Due to their ease of access, convenience and being open 24/7, these services are being provided as marketing tools to attract customers.

Many other marketing strategies are being adopted by gas stations in Lebanon. Some gas stations offer their clients loyalty cards, providing services such as car washes and oil changes free of charge. Others use innovative and environmentally-friendly techniques in providing their services, such as laser carwash and gas oil that reduces $CO_2$ emission.

In conclusion, the fuel oil market is over-saturated, with the price fixed by the government and profit margins being relatively small. These small profits do not motivate gas stations to invest in their infrastructure and expand their services. Also, even if global oil prices were to return to previous highs, an event that is becoming increasingly unlikely, gas stations would not be realizing improved profit margins. The expensiveness of prime locations and the increasing lack of availability of such locations would mean that future gas stations would find it difficult to imitate the already low margins being realized. Therefore, most gas stations agree that the industry they work in is not attractive.

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