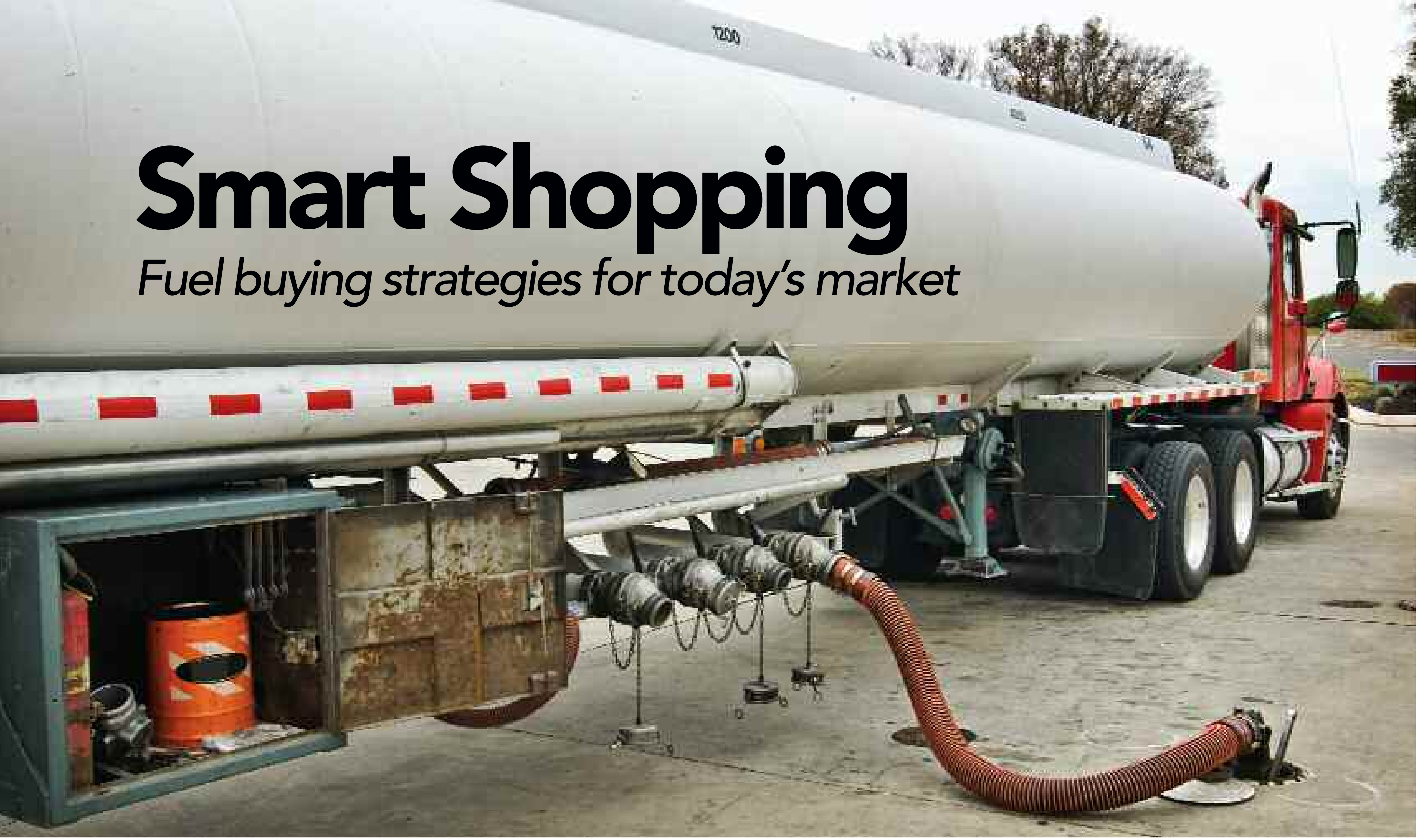

# Smart Shopping

## *Fuel buying strategies for today's market*

BY MINDY LONG

Fuel is one of the largest expenses for fleets and owner operators, so every penny counts. Buying smart while protecting cash flow can ensure retailers deliver the best value to their customers. Industry experts say now is the perfect time to renegotiate contracts and lock in good prices, but contracts are just one piece of the puzzle. By implementing a few proven techniques, NATSO members can secure the lowest fuel prices, negotiate the best contracts, take advantage of the spot market and improve their overall operations while also helping drivers.

### Contracts Vs. Spot Markets

There are pros and cons associated with contracts and the spot market, so many retailers use both. Early this year, fuel demand was down, leading to the oversupply of fuel markets and good prices. "As a result, we have seen refiners reduce the refinery utilization rate over the past several months. In many instances, the oversupply of fuel has resulted in refiners and suppliers dumping fuel products in markets at discounted prices," said Roger Simons, vice chairman of Maxum Petroleum Inc.

When possible, retailers may want to take advantage of the oversupplied markets by entering into short-term and long-term contracts on only a percentage of their overall fuel needs. For additional purchases, retailers can take advantage of aggressive daily rack pricing to lower their fuel costs.

Operators need to evaluate their own situation, but Scott Berhang, director of education and corporate training for OPIS, offered some general advice. "I like to tell people you should lock up 80 percent of what you know you're going to need in a formal supply contract. Buy 20 percent on the spot market to take advantage of the market downturns," he said.

However, buying on the spot market means retailers are buying on the unbranded market. That is appealing when there is abundant supply. "The thing to be careful of in the unbranded market is there are going to be fewer options when the market gets tight," said Brian Milne, refined fuels editor for DTN.

Contracts help ensure operators will have supply. "Down here in the south we have hurricanes. When bad things like that happen we have to prioritize and we naturally take care of our contract customers first," explained John Rettiger, vice president of TAC Energy. Refinery shutdowns due to weather or seasonal maintenance, pipeline outages and fuel terminal issues all affect supply and cost.

Retailers should also examine their local market when weighing the pros and cons of contracts. Bobby Berkstresser, owner of Lee-Hi Travel Plaza in Lexington, Va., buys on contract with Shell and renegotiates every year. For him, buying on contract has removed volatility he faced due to local storage in his area. He explained that the infrastructure and pipelines near him are 30 years old and demand has increased dramatically since they were built.

### Negotiating Contracts

For retailers utilizing contracts, Berhang said this is the best time in five years to renegotiate with suppliers. To get started, he suggests retailers block off several days to look at the way they're buying fuel. "Take out those contracts and read them," he said. "Ten to one those contracts are old."

Milne recommends retailers examine price history. "It will help your negotiations considerably," he said. "In 2007 we saw heavy demand, so you want to go back and do a five-year average. You want to get an idea of what your margin is against the terminals you can source out of."

The most important things retailers should look for in their contracts include lifting allocations, costs and benchmarks. Berhang said, "If they want to verify what they are being charged is correct, they need to have that benchmark in the contract. Specify, specify, specify. Err on the side of dumbing it down."

Retailers typically can choose any benchmark they'd like, whether it is Platts, OPIS or something else. "The more complicated benchmark you use, the more support you have to have on your side to do the accounting," Berhang said, adding that most retailers use a daily benchmark.

### *The best way to save money is to actively manage your inventory.*

### Managing Inventory

Experts agree the best thing retailers can do to save money is actively manage inventory. "You want to minimize your inventory and time your deliveries so you get the lowest price in your tank," Rettiger said. "Depending on your tank size, if you see the market going up and you have an opportunity to get a load before the price changes, you should take advantage."

Learning their local fuel market dynamics and how product is supplied to the local markets can help retailers time deliveries and predict costs. "They need to understand the fuel supply chain from the refinery, to the pipeline system, to the local terminals and finally to their location," Simons said. "It is very important to understand what can disrupt the flow of fuel products as this will be important in managing inventory and may be an indicator of possible price spikes and declines."

Effective inventory management and a just-in-time inventory system allows for quick inventory turnover and reduces the price risk associated with rapidly changing prices, whether they are increasing or decreasing. Simons said, "Retailers should monitor inventory levels closely to create optimal flexibility in the timing of fuel purchases." He explained that by properly managing inventory, retailers can take advantage of refiner or supplier deals or midday price changes when prices are going up and reduce the risk of having high- priced inventory in the tanks when prices are falling.

Some retailers may choose to utilize an outside company to watch inventory. In addition to providing supply, TAC manages inventories for its clients. “They have to provide us the IP address or the phone number that attaches to their underground tank monitor, we dial right in and work with carriers to schedule a load when it is most price advantageous for our clients,” Rettiger said. “In 2008 in over 50 percent of the days there was a price move of more than five cents. We’ve saved customers 2-3 cents a gallon.”

FuelQuest, whose customers include UPS, 7-11 and Fed Ex, has a Web-based fuel management system that monitors and tracks the product inventory at its clients’ locations. “It predicts the necessary stock times and locates the cheapest source of supply,” said Matt Tormollen, FuelQuest president and CEO. FuelQuest also provides financial reconciliation with an automatic three-way match system that looks at the delivery report, the bill of lading and the invoice. Tormollen said, “We just had a retailer say that in one quarter alone they uncovered $800,000 in misbilling.”

### Hedging Your Bets

Once retailers have a handle on their physical inventory, Berhang said it is “critical” that they hedge. He recommends retailers start conservatively and hedge a small portion of their fuel. “The biggest fear that people have when they hear hedging is that it is speculating, and that is not the case,” he said. “When you hedge, you are using different types of financial instruments to offset gains and losses in your physical position.”

Milne explained the differences between hedging and speculating. “If you’re hedging, you are literally buying contracts because you have a physical position. If you are speculating you have no underlying risk, you are just putting your money in,” he said. “If you do hedge, it will smooth out your margins because you know you can use the hedge to protect against any loss if the market turns against you. It is like insurance.”

Operators hedging for the first time should hedge 15 to 20 percent. “As you get better at it and more comfortable, then you start doing more,” Berhang said.

Milne explained that there are risks to hedging. “In addition to the cost to hedge, if the market moves against you, you could be subject to margin calls and you could have to pay up for margins. That is a real problem for cash flow.” Retailers should utilize an experienced, reputable broker or trader.

### Selecting Suppliers

Rettiger recommends operators, particularly independents, work with every supplier in their market. “A lot of independents will be set up with one or two suppliers and that can limit their options for supply,” he said. “They have to be willing to be more flexible as far as when they receive deliveries, and when they buy.”

The high price of fuel and the uncertain economy has led several suppliers to tighten their credit standards and require letters of credit or cash deposits, which has become an important factor for retailers to consider when selecting a supplier. “This can lead to shortened credit terms or no credit availability at all,” Simons said.

Rettiger said more retailers are turning to his company, which buys from a variety of sources and supplies fuel to retailers. “When you have us as your supplier, you have access to every supplier in that market without having to get credit with every supplier in the market. An independent fuel buyer might not have the credit ability to keep those options open with every supplier.”

No matter which suppliers retailers use, the fuel business is built on relationships, “You need to be comfortable with the people you are doing business with,” Berhang said. “You need to like them and you need to have a rapport with them,” he said.

## Info Gathering

“Retailers need to arm themselves with information,” said Scott Berhang, director of education and corporate training for OPIS. Retailers can track local refiner prices and how they relate to other indices such as the NYMEX, Platts and OPIS. “Analyzing the relation between refiner prices and other indices will provide valuable knowledge when negotiating short and long-term contracts. It will also provide insight of when to take advantage of midday price changes and/or day deals,” Simons said.

Bobby Berkstresser, owner of Lee-Hi Travel Plaza in Lexington, Va., watches the futures market daily and recommends every operator train someone in the organization to watch it, even if it is on a small scale. “Even though the independent operator may not be able to buy futures, he can watch the market on a day-to-day basis and save himself thousands of dollars a year on what he buys,” he said. Berkstresser also utilizes third-party tracking services. “Every independent at a bare minimum should subscribe to OPIS so they’re not only finding out what their rack averages are each day, but also so they know what their competition is selling at,” he said.

The Department of Energy’s Energy Information Administration releases its weekly reports every Wednesday at www.eia.doe.gov. “At noon on Wednesday you’ll know what the inventories are and that will have an impact on prices for several days,” Berkstresser said.

Because the price of fuel is so intertwined with other global issues, the weather, inventory reports, the value of the dollar, geopolitical issues and the unemployment rate can all affect costs. Retailers can track those issues simply by watching the news. “It is just paying attention to the basics. If you do that everyday, you can save yourself a lot of money,” Berkstresser said.