FUTURES $ OPTIONS

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The lifeblood of your business

President Obama recently stated that, “the flow of credit is the lifeblood of our economy.” There was a good deal of flak taken for that comment—wasn’t it credit that got us into this mess in the first place? Aren’t productivity and investment really the lifeblood? But as with many quotes, things can be taken out of context. However, the debate over that real “lifeblood” got me thinking about our industry, and wondering what the real lifeblood of a retail oil dealers’ business was.

The more you think about it, if you are a retailer, selling heating oil in today’s age, the major differentiator between full-service heating oil dealers is the number of customers that they deliver oil to. Customer Count reigns supreme when oil guys get together to proudly speak of their businesses. That is where the real value is perceived and where it actually lies.

In making a large leap of faith that most companies understand basic economics—i.e. sell the oil for enough money to make sure that ALL of your costs are covered, plus allowing for a reasonable profit—the notion of “Customer Count” cannot be overstated. And, more importantly, doing whatever you can to not allow those customers in “your count” to want to leave you is of the utmost importance.

One question about Customer Count: How many customers might you lose (or, at the very least, irritate) if your customer is being charged $2.00/gallon more than his next door neighbor? Neighbors won’t necessarily gloat over paying 10-, 20- or even 30-cents less than the guy next door, but make that 75-cents, or a dollar or two dollars, then the trash-talking starts!!

There are basically only three ways that oil is priced to homeowners: variably (up and down with the market), fixed (one price for the entire term) and capped (a maximum level that won’t be exceeded—the cap has additional costs, and will have a higher max price level than will the fixed price).

In the past four years (including this winter), twice prices trended lower through the winter (looking at the July price—when a program WOULD HAVE BEEN offered, and comparing to the high or low during the following winter—twice they moved higher. During the two years that prices fell, the variable customers would have benefited by the falling prices, and not had a price-related reason to leave.

However, during the “other” two years—when prices rose about $.45 per gallon, and $1.25 per gallon, I cannot imagine that “variable customers” would have been all that happy to see their capped and/or fixed neighbors protected against those price increases. How much of an impact on Customer Count did that have?

Now, consider for a moment the customers who wanted predictability in their pricing, and were worried about prices moving higher. During those two years that the variable customers—justifiably so—were whining about paying so much more than their neighbors, the fixed customers were not burdened by rising oil prices since their costs were fixed and couldn’t go up. But the “fix” part also means that prices couldn’t go down, and in the two years that prices fell (’06-’07, and ’08-’09), they fell by $.50/gallon, and then by $2.30 per gallon from the summer to the winter. It doesn’t take ANY imagination to understand the impact on Customer Count a delivery that is about $2.00 per gallon away from what others are paying might have.

Lastly, there is the Price Cap. Customers who signed up for the cap program in the two years that prices fell paid more than those who bought on a variable basis, but well under the prices paid by those who had a fixed price. In the two years that prices increased, and the variable customers were streaming for the exits, the fixed price customers most likely paid a lower price. You could accurately say that Price Caps always turn out to be in second place (or, as my sports-crazed son likes to say, “The first loser”). However, the one in third-place (second loser?) always seems to be in third place by a large margin. The good thing about the cap is that in each of those very, very volatile four years, the cap prices were probably close enough to the “better” of the cap or the fixed so that it would not cause much damage to the Customer Count.

Lately, there has been some rumbling about the “bad” programs, and talk of attempting to eliminate them. The talk mostly centers around the fixed-price programs, and the terrible effect that they have had on customers. Let’s be honest, the real concern, and a legitimate one, is the terrible effect that they had this past winter on heating oil companies. The losses of customers and of money related to the fixed price offers were staggering. However frustrating these programs turned out to be, fixed programs are not the same as capped programs, and should not be lopped together, as though they are one in the same. If the customer service, credibility and financial issues are too great for heating oil companies, those companies may CHOOSE to stop offering fixed price programs (and either do what many have, in offering a cap for next winter, or just selling on a variable basis); but how does a mandate to stop programs benefit anyone—other than those who cannot or choose not to compete in a competitive marketplace?

Returning to the cap, and even with the fact that caps are not the “be all and end all” for everyone, there is no way to have a hedge that is absolutely perfect in design or resolution, and the costs (thanks to heating oil prices that have moved by about $3.00 per gallon over the past year) are not low. Customers do not NEED to participate in programs, nor do they NEED to pay the costs to get a capped price. Considering that “the grass is always greener” with the program that worked this past year, it would seem that YOU need to offer something that will consistently allow the customer to know that he/she paid a fair and competitive price, and not allow for a delivery that is so far away from “the market” that it will allow and cause customers to look elsewhere, and for Customer Counts to fall.

The cap can easily be described as the least of all evils, but there are professionals who can clearly guide you through the maze of hedging to put out the right program, and hedge it correctly. Though it might not be easy, it has to be easier than sitting at an industry outing (or in an internal meeting) and explaining why Customer Count is even more volatile than the price of oil.