

## REPORT 1

### ENERGY INDUSTRY: HOW THE DEMAND AND SUPPLY FACTORS INFLUENCE THE PRICE OF OIL

The world has been relying on oil to be the primary source of energy to guide its development and progress for more than a century now. However it has been observed that oil is an elastic commodity due to the high fluctuation in prices from time to time. The supply and demand changes for oil even for short time periods have had huge influences on the global oil prices. Hence it is important to have knowledge of the supply and demand factors which cause the price of oil to change and thus exercise the power to influence the rate of progress and development of different nations of the world.

Generally it is understood that the prices of a commodity become high if the demand is high and the supply is lesser to it in comparison. Thus the price will be low if the demand is low and the supply of the commodity is high. However, in the case of oil prices this is influenced by the oil futures market where the price of oil for a later date is predetermined after speculating on the trend of demand and supply of oil at a later date. Hedgers involve themselves in the oil futures market after speculating on the demand and supply of oil in the days to come. Organizations like the OPEC have been formulated with the aim to ensure a stable oil market by balancing the supply and demand of oil.

A major supply factor which influences the price of oil is the production capacity of the oil producing countries. Very often the country maintains a balance with the demand such that the demand always stays high to ensure a fair return to the oil producing company for their investment. However since crude oil is rarely used for productive purposes the refineries are mostly made to work below their full potential so that the reserves of oil in the country are not sold out at lower prices (USEIS 2015). For example the surge of shale gas production in America by the end of 2014 led to a fall in oil prices in the country due to the increased supply (Cunningham 2015). If the resultant fall in prices makes the investment unprofitable then it can negatively impact the industry because of which measures are adopted to bring about a balance in the market (USEIS 2015).

The volume of net imports by the countries can also be a major supply factor. It is believed that China will be the biggest importer of oil by 2020 because of which the future price of oil is dependent to a large extent on the prosperity of the Chinese economy which should enable it to import more oil (Cunningham 2015).

The countries with high oil reserves also have a large role in determining oil prices since they will be relied on for the major supply of oil in the future. Saudi Arabia, the country with the largest oil reserves at 267 billion barrels is followed by Venezuela at 211 billion barrels. Many of these countries are members of OPEC which influence oil prices.

The geopolitical factors have a major role to play in determining the supply of oil since many of the oil producing countries face geo political issues. An example of this would be the Iran- Iraq war, the political upheaval of Libya and Iran in the recent past (Mcfarlene 2015). The emergence of ISIS in the Middle East has further contributed to the supply issue.

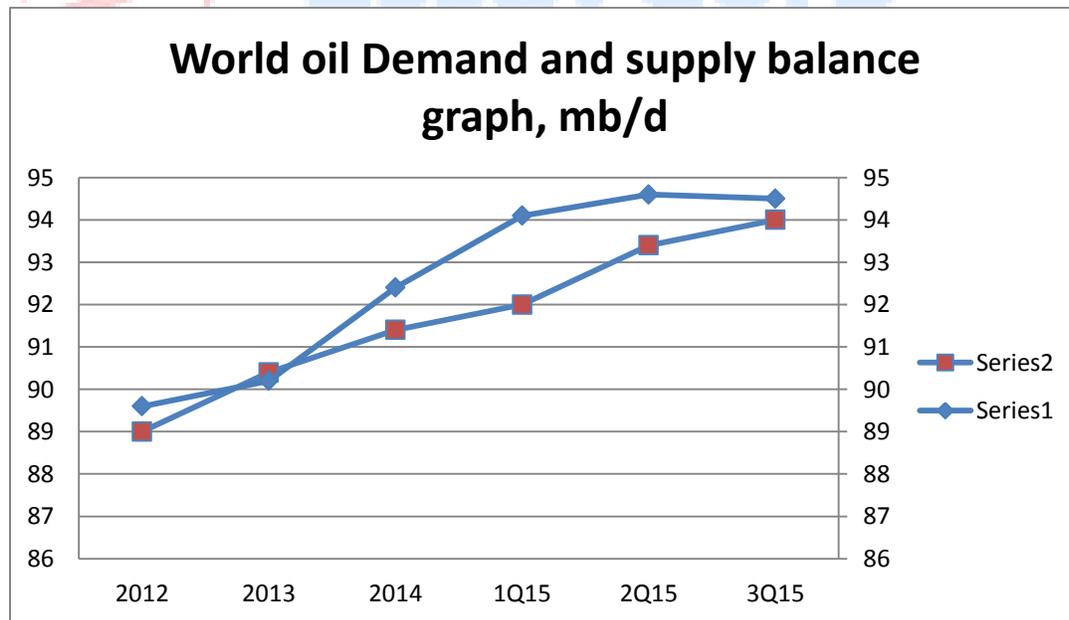
The demand for oil is mainly dependent on the economic status of a country which in turn affects its capability to afford oil imports or its capability to sustain a high demand for the fuel. For example it is understood that in countries like USA the demand will be very high to support its road and air transport. But in those countries where oil is subsidized to make them affordable for the general public may not be able to do it for long which will in turn reduce the demand for oil (Cunningham 2015).

Another major factor is weather related problems which can cause a sudden increase or decrease for oil. An example of this can be how the hurricanes of 2005 resulted in the reduction of supply of petroleum and petroleum products (Cunningham 2015). This is also true of the demand side where low temperatures will increase the demand for oil which will be needed to heat the buildings. Low temperatures can also cause problems for the efficiency of the oil pipelines further restricting the supply. Extreme high temperature can also increase the demand for oil which will be used to provide power to the cooling systems. Such short term issues can lead to increase in global price of oil for the short term (McFarlene 2015).

The figures for supply and demand of oil from 2012 to the third quarter of 2015 (OPEC 2015):

**World oil demand and supply balance graph, mb/d**

	2012	2013	2014	1Q15	2Q15	3Q15
Supply/series1	89.6	90.2	92.4	94.1	94.6	94.5
Demand/series2	89	90.4	91.4	92	93.4	94



It may be observed that during 2014 when the disparity between supply and demand of crude oil was less due to many geopolitical factors the price of oil had increase by a very large margin. However the

high prices of oil which were present even in the first quarter of 2015 were brought down by the second quarter. There has been stable prices of oil in the recent past as the market has not deviated from the consistent path as had happened around 2013-2014 which caused sudden changes in the balance of supply and demand. This is well illustrated by the global price trends showed in the OPEC monthly report of 2015.

The average cost of domestic air travel in USA when adjusted against the 2015 dollar value shows that the value of 2012 (\$384), 2013 (\$383) which showed a slight decrease in 2014 (\$382) has increased in the first quarter of 2015 to be \$388. However this is a major reduction from the comparable rates in the beginning of the 21<sup>st</sup> century when the average rates were above \$400 (Bureau of transportation services 2015). This could be because of better domestic fuel production. The use of refineries to make air turbine fuel further determines the price of ATF which in turn influences the air fares.

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## REPORT 2

### EVALUATING LOW COST AIRLINE MODEL: SOUTHWEST AIRLINES

Southwest Airlines is a very successful low cost airline service operating out of USA which started offering air travel at low air fare in the beginning of 1970s. It is known for its point-to-point services which avoids travel to major hubs to get access to connection flights. It is unique in the fact that it has been able to generate profits for the 42<sup>nd</sup> consecutive year as per its annual report to shareholders for 2014. Its consistent profitability has contributed to its image as a stable participant in the stock markets resulting in increased stock prices over the years recently making it the top performer of the S&P 500 list. Southwest Airlines is the only US Airlines which continues to be investment grade-rated by the three major credit rating agencies. Southwest was recognized as the "2015 Airline of the year" by Air Transport World for its distinguished performance in 2014. For the past 21 years Southwest has appeared in the list of World's most Admired Companies brought out by the Fortune magazine and it is the only airline which was included in the top 10 companies of the list (2014 Annual Report, 2015).

The special services offered by Southwest include vacation deals which offer the best rates for travel as well as accommodation for its customers. While retaining its focus on the provision of low cost services to its customers, the collaboration with other segments which make travel and stay a meaningful experience have increased the overall potential and appeal of the business (Southwest 2015).

The capital of the company is handled in such a way that there is simultaneous focus on both the costs and the revenues. The company resorts to hedging to ensure profitability and protect the airlines against increasing fuel expenses. Priority is given to deriving the maximum out of all the investments, be it maximizing the utilization of the fleet they have at their disposal or in using cost cutting measures while ensuring an enjoyable travel experience to its customers. It employs the method of incremental cost of accounting to provide the customers with the Rapid Rewards Programme. The focus has been to invest only in Boeing 737 aircrafts with a maximum of three crew members and modernizing the existing fleet to cut down on future expenditure. With its recent entry into the international market Southwest hopes to continue to provide air travel at the lowest rates possible. Southwest had a strong cash and short term investment as big as \$3 billion with full access to bank line of credit (2014 Annual Report, 2015).

The unique work culture at Southwest ensures satisfied labour which is reflected through its policy of 'Employees first, customer second'. The employees are instilled with the warrior spirit, motivating them to be proactive in providing assistance to the customers and evolving innovative and cost cutting measures to make air travel enjoyable. The cordial workforce is also extended flexible working hours to ensure their job satisfaction and thus in turn improve their work efficiency (Southwest 2015).

For a long time Southwest had operated only at mid-sized cities and secondary airports to avoid the congestion at the main airports and also as a cost cutting measure. But recently Southwest has reconsidered its practice and acquired some assets from ATA airlines in 2008 at \$7.5 million to gain access to the 14 landing slots it had at La Guardia Airport at New York. It has also acquired slots at

Washington Reagan national. Southwest is seeking to cover new grounds by accessing the areas previously catered to by AirTran which it acquired (2014 Annual Report, 2015).

The entrepreneurship at Southwest focuses on creating a brand name and ensuring that they remain the airlines providing the lowest airfares to such an extent that it has been feared by other low fare airlines that if Southwest reduces its travel fare any further , it will drive the others out of business.

Entrepreneurship has prioritized the fact that luxury can be compromised and alternate entertainment can be provided through low cost measures and by making all purchases while onboard using credit cards only so that all customers are ensured maximum satisfaction. Excluding bags from extra charges, travelling without tickets, allowing pets into the aircraft, not providing complementary meals onboard and maximum utilization of the existing workforce and fleet is done for improving the appeal of its services to the customers (Southwest 2015). The entrepreneurship also ensures that the existing fleet is modernized, the destinations are chosen carefully and in phases such that ticket charges for short distance destinations can be comparable to travel expense by road (2014 Annual Report, 2015).

The technology being relied on by Southwest from the beginning of its services is the Boeing 737. The annual report of 2014 says that Southwest aims to have 700 Boeing 737 aircrafts by the end of 2015. In its attempt to expand its market in the domestic front as well as internationally, Southwest aims to acquire more Boeing 737's in addition to modernizing its existing fleet to avoid unnecessary expenditure and wastage (2014 Annual Report, 2015).

<p style="text-align: center;"><b>Strengths</b></p> <ul style="list-style-type: none"> <li>Maximum utilization of fleet</li> <li>Lowest possible airfare rates</li> <li>Satisfied workforce</li> <li>Cordial employees to ensure customer satisfaction</li> <li>Uncontested leader among low cost airlines in USA</li> <li>New international service looks promising</li> <li>New acquisitions have great contributing potential</li> <li>Higher frequency of flights</li> <li>Rapid Rewards Programme</li> </ul>	<p style="text-align: center;"><b>Weaknesses</b></p> <ul style="list-style-type: none"> <li>Service is limited to low cost air travel</li> <li>Complete dependence on Boeing for its technology</li> <li>International services are few</li> <li>Majority of its employees are members of unions</li> <li>Revenue is mainly dependent on passenger travel alone</li> </ul>
<p style="text-align: center;"><b>Opportunities</b></p> <ul style="list-style-type: none"> <li>New opportunities being explored through new acquisitions</li> <li>Expanded reach to new international markets and destinations</li> <li>Improving domestic tourism scenario</li> <li>Can start streamlined air travel services in other segments</li> <li>Expand into long distance domestic flight services</li> <li>Increasing preference for air travel whenever possible</li> <li>Explore options beyond Boeing to reduce</li> </ul>	<p style="text-align: center;"><b>Threats</b></p> <ul style="list-style-type: none"> <li>Increasing competition in the market</li> <li>Fluctuating air turbine fuel prices which are dependent on many geopolitical and weather related developments across the world</li> <li>Similar services provided by the competitors</li> <li>Changing government regulations</li> <li>Ever present fear of terrorism</li> <li>Prevalence of adverse macroeconomic conditions in the country can directly affect the business</li> <li>Unforeseen increase in operational costs can adversely affect the business</li> </ul>

vulnerability

Any problem with Boeing can affect the image of the company

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### REPORT 3

#### PRICE AND NON-PRICE COMPETITION IN OLIGOPOLY MARKETS

Oligopoly market is one where there are very few competitors in the market, at times even as low as two competitors. This leads to a highly concentrated market with only a limited number of players having direct access to certain produce. Small firms can also exist in the oligopoly market with other firms which may be dominating the market. In such a situation, the supply is controlled by few competitors such that the price increase or decrease by one competitor affects the other. There is interdependence in a lot of factors like variety of products, price of the products, and services offered. This ensures a fair stability of prices in the oligopoly market. They also offer a wide variety of products to the customer to maximize its appeal. This creates a great challenge for any party who wants to join the market as a competitor since he will be expected to meet the services, products and prices offered by the existing competitors just to survive in the market, apart from providing extra services which may be formulated with the target of making the new competitor more appealing to the customers (EO 2015).

The issues faced by price competition in the oligopoly market are many. Inflation can be a deterrent for people who previously wanted to buy products from the oligopoly market since this would reduce their buying capacity. Slow growth of economy can lead to slower generation of money in the market, less competition, slower rate of production and resultant unemployment which can reduce demand for products offered by the oligopoly market. The sudden changes in prices of international products which are procured from other countries can create competition between the major players of the oligopoly markets for a short while till prices are stabilized between the competitors. Sudden policy changes by the government through annual budget or through other means which can change the taxes on some goods and thus the resultant overall price, can bring short term competition among the competitors till stabilization of price is achieved between them.

The issues faced by non-price competition in oligopoly markets are varied in nature. Natural disasters like earthquakes, heat wave, tsunami and floods as well as adverse weather developments in areas can negatively impact the market. This is also true of those societies where there is social unrest and upheaval resulting in an environment non conducive to business growth and competition. The lack of government support to oligopoly market can act as an impediment in its path of progress whereas any unfavorable policy regulations enacted by the government which restricts the activities of the oligopoly market can adversely affect its growth. Incidents of terrorism, extremism and internal and external violence in the country can also cause problems in the smooth functioning of the oligopoly market. The ban imposed by the government and its agencies or by certain organizations in the society can limit the possibilities of the market.

One of the major oligopoly markets of the contemporary world is the online retail market. The problem with price competition in oligopoly markets is that the interdependence between the players to

maintain stability of prices cannot be relied on as it goes against the basic rule of competition (EO 2015). There will be constant attempt on the part of all players to provide as low prices as possible to its customers to attract more customers. The new products which are launched in the market can be retained at high competitive prices by the oligopoly market. The inclusion of even the latest products available in the market into its fold allows the online retail provider to offer a product at varied price ranges to cater to maximum number of customers. Quality assurance of the products being delivered helps to retain the customer base of the online retailer since the customer grows to have trust that products have good value for money paid. The swiftness with which there is remittance of failed financial transaction also adds to the desirability and brand image of the online retailer. Assuring authenticity of the delivery made to the customer and implementing remedial measures without financial loss to the customer helps to retain maximum customers within its fold and cultivating a loyal customer base.

The strategies which can be employed to get a competitive edge over the other online retailers through non-price competition are numerous. The competitor with maximum number of products and services at their disposal will be most sought after by the customers as it offers them more variety to choose from. This also enables the online retail business to target a larger group of customers rather than restricting oneself to a limited clientele. The time duration taken for delivery of the product and the differences in delivery charges are major determinants which can change customer's choices. The time duration and procedure adopted for the return policy of the product are also important factors. The availability of sellers and services at remote areas helps to maximize number of customers. The promotion code provided along with products act as added incentive to choose certain products from some online retailers. The frequency of advertisement as well as the different modes of advertisement relied on like phone calls, emails and advertisements in print media help to reach out to customers belonging to different income segments and regions. The handling of the products ordered by the customer through proper packaging as well as the proper access to customer care services and prompt redress of grievances make online retailer more attractive. The good behavior of delivery personnel also helps to retain customers.

In Ebay, the Apple iPhone 4S 16GB Factory unlocked smartphone white is priced at 94.99 pounds whereas it is priced at 109.99 pounds at Amazon. Ebay has sold out the same model in black which has the same price tag. Hence customers prefer EBay to Amazon when it comes to this particular model as EBay offers it at a lower price. Burberry Weekend aftershave spray 100ml is priced at 32.91 pounds at Ebay while at Amazon it is at 33 pounds. Through this it is clear that Ebay seeks to capture maximum customers by offering products at prices which are slightly lower than those offered by Amazon. Both the online retailers offer selling option and deals on a daily basis as non-price competition factor. However Amazon seeks a competitive edge through offering gift cards to its customers which is not provided by Ebay.

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