Case Project

Lesser Antilles Lines: The Island of San Huberto (A)

Phillip E. Pfeifer, James V. Gelly

Synopsis

"Lesser Antilles Lines" is written by an MBA student based on his experiences the summer after graduation. Lesser Antilles Lines (LAL) was one of two shipping firms engaged in a vicious price war over the market for the shipping of large, trailer load containers to the small island of San Huberto. Because the lower prices had not increased primary demand, the war had served only to bring mounting losses to both firms. The case describes LAL's planning for the end of the price war.

Questions

Using this case study (Lesser Antilles Lines: The Island of San Huberto (A) by Phillip E. Pfeifer, James V. Gelly available here (Links to an external site.)) answer the following questions:

1- What are the assumptions behind the table in case Exhibit 4? How realistic are those assumptions? Build a spreadsheet to reproduce profit calculations in Exhibit 4 of the case. Your spreadsheet should use formulas on page 6 of the case to calculate KL and LAL contribution for both companies, given any pair of prices. (**how to submit?**: Please submit your work in a Microsoft Excel Workbook)

   a. **The assumptions are that the Market share for KL is 60% and LAL is at 40%, market size, and costs. Vaughn did extensive research and interviews, which would make this information more realistic. In addition, KL being the first in the San Huberto market makes the 60% market share realistic and because it has a smaller fleet so the costs being slightly hire to make up for inefficiencies is also plausible. What isn't realistic is that they haven't priced each other out of the market.**

2- Accepting the assumptions in Exhibit 4. What action would you recommend to LAL management about how it should set its price. Given your recommendation, what will be LAL's profit? What will be KL's profit?

   a. **The Nash equilibrium is when KL is priced at 1400 and LAL is priced at 1300, giving a profit of 1,008k and 895k respectively. Because of this, I would recommend that LAL sets its price to $1300. It will be where the price settles and while it seems that they might make more money if they raise the price, KL will just drop the price and LAL would end up charging $1300 anyway.**

KL Price												
1,900	0	0	0	0	0	0	397	793	1,190	1,587	1,983	2,380
	-160	230	620	1,010	1,400	1,790	1,962	2,056	2,072	2,010	1,870	1,652
1,800	0	0	0	0	0	358	715	1,073	1,431	1,788	2,146	2,503
	-160	230	620	1,010	1,400	1,611	1,744	1,799	1,776	1,675	1,496	1,239
1,700	0	0	0	0	319	637	956	1,275	1,593	1,912	2,230	2,549
	-160	230	620	1,010	1,260	1,432	1,526	1,542	1,480	1,340	1,122	826
1,600	0	0	0	280	559	839	1,119	1,398	1,678	1,957	2,237	2,517
	-160	230	620	909	1,120	1,253	1,308	1,285	1,184	1,005	748	413
1,500	0	0	241	481	722	963	1,203	1,444	1,684	1,925	2,166	2,406
	-160	230	558	808	980	1,074	1,090	1,028	888	670	374	0
1,400	0	202	403	605	807	1,008	1,210	1,411	1,613	1,815	2,016	2,016
	-160	207	496	707	840	895	872	771	592	335	0	0
1,300	163	325	488	651	813	976	1,138	1,301	1,464	1,626	1,626	1,626
	-144	194	434	606	700	716	654	514	296	0	0	0
1,200	247	371	495	618	742	865	989	1,113	1,236	1,236	1,236	1,236
	-128	161	372	505	560	537	436	257	0	0	0	0
1,100	254	339	423	508	592	677	762	846	846	846	846	846
	-112	138	310	404	420	358	218	0	0	0	0	0
1,000	183	228	274	319	365	411	456	456	456	456	456	456
	-96	115	248	303	280	179	0	0	0	0	0	0
900	33	40	46	53	60	66	66	66	66	66	66	66
	-80	92	186	202	140	0	0	0	0	0	0	0
800	-194	-227	-259	-291	-324	-324	-324	-324	-324	-324	-324	-324
	-64	69	124	101	0	0	0	0	0	0	0	0
LAL Price	800	900	1,000	1,100	1,200	1,300	1,400	1,500	1,600	1,700	1,800	1,900

3- LAL is considering a Price Match Guarantee (PMG) to its customers. This is a commitment to match KL's price. Should LAL go ahead with the PMG? Justify your recommendation (Show your calculation in determining the Nash equilibrium prices).

a. **I don't recommend doing the price match guarantee as it will not maximize profits or market share. While both companies are less likely to drop down to 800 because they would both be losing money, LAL would not be making enough profit to justify the price guarantee… unless both actually discussed pricing, but since they are bitter rivals and that would be more of a cartel situation (ethically/legally questionable), that wouldn't be the case. The Nash Equilibrium, which is shown and discussed in question 2, if LAL prices at 1300 and KL prices at 1400 that would be the best option here. It may not be the most profitable for either company, but it is the best option given the information.**

Definition of Price Match Guarantee (PMG): "If a rival offers the same product for a lower advertised **price**, the company will either **match** the lower **price** or refund the difference if the customer has already purchased the product from it". Here is a very interesting article providing insights on [Why Price Match Guarantees Can Be Bad For Consumers (Links to an external site.)] by Rafi Mohammed.