

Title: FUEL PROVISIONS VERSUS HEDGING USING FORWARD CONTRACTS: WHICH IS THE OPTIMAL STRATEGY?

Author: WEKESA MIRIAM KHAKASA

ABSTRACT

Over the past years, the ever increasing prices of jet fuel have been a source of risk for the airline industry. Jet fuel is the second largest operating expenditure for airlines. It is for this reason that airlines need to find an effective way to control these costs since a small increase in jet fuel prices could result to a great increase in the operating expenditure.

This dissertation examined the use of forward contracts and provision funds in hedging against jet fuel price volatility so as to establish which of the two methods is more effective. Historical data on fuel prices, average volumes of fuel consumption, KSHS/ USD exchange rates and risk free rates were used to carry out the analysis.

The results of the savings obtained from the use of purchasing forwards and setting up a provision fund indicated that hedging with the use of forward contacts is more effective.