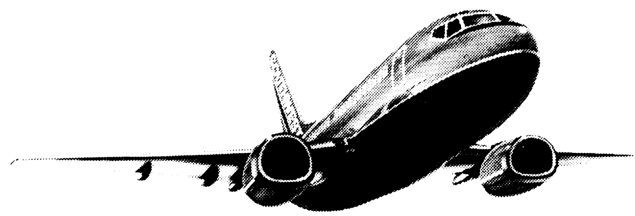
Southwest Airlines: 1993 (A)



SOUTHWEST AIRLINES℠
Just Plane Smart.℠

In the summer of 1993, Southwest Airlines anticipated the immediate delivery of two uncommitted airplanes. As with any scheduling decision at Southwest, Pete McGlade, director of schedule planning, and his team faced the challenges of meeting growth objectives while maintaining focus. "Controlled growth is essential," emphasized McGlade. McGlade reviewed the final candidates before him: adding a new route between Detroit and Phoenix, or initiating service to Dayton or Baltimore. The chairman, CEO, and president, Herb Kelleher would make the decision in conjunction with the scheduling department. As McGlade glanced at his watch, he realized that it was already 2:00 p.m., time for the scheduling department's daily "hackeysack"[1] break. As he walked down the hall to gather his staff for the break, he knew that the final decision would have to preserve the Southwest culture and spirit that had enabled it to be the only major airline in the United States to post a profit in 1992.

History—The Airline "Luv" Built

Although organized in 1967, Southwest's operations were delayed for four years due to court battles brought by competitors over the new carrier's entrance into the Texas intrastate market. The competitors argued that there was inadequate demand to support three carriers. A year and a half after Southwest began operations, those same competitors, now defunct Braniff and Texas International Airlines, initiated a price war that led to a 50% decrease in Southwest ticket prices

[1]Hackeysack" is a game played by a group of people involving a small bean bag. The object of the game is to keep the hackeysack in the air, and players use their feet and other body parts to kick the sack into the air. The game is usually played outside and is a popular beach activity. McGlade and his crew play in the hallway.

Research Associate Roger H. Hallowell prepared this case under the supervision of Professor James L. Heskett as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

between Dallas and Houston to $13. Surviving these early battles, the new airline developed an image as "the underdog" in the eyes of both employees and the Texas public.

Southwest's corporate offices were located at Dallas's Love Field, the city's only airport until the opening of the Dallas Fort Worth International Airport (DFW) soon after Southwest began operations. Love Field was located six miles from downtown Dallas, whereas DFW was located 21 miles from city center. All Southwest flights out of Dallas originated from Love Field.

"Luv" also played a role in the Airline's early marketing. Analyzing the competitive postures of airlines operating in Texas in 1971, Southwest's advertising agency and marketing department developed a theme described as "obviously fun" to differentiate the airline.[2] The theme revolved around a "Love Theme" that featured "Love Machines" (virtually instant ticket writing machines) and "Love Potions" (on-board drinks). Southwest dubbed itself, "The somebody else up there who loves you."

Luv service also involved frequent (often eight or more one-way flights a day on a specific route) and on-time departures as well as low unrestricted fares. Southwest's policy of offering low fares (particularly low unrestricted fares), instituted with its first flight in 1971, enabled business and leisure travelers who might have otherwise driven the distance between the majority of its short-haul city pairs (departure and destination points) to fly instead.

The Airline "Luv" built grew steadily during the 1970s. By the end of the decade, the airline faced the challenge of deregulation and expansion beyond Texas. At the time, industry experts believed that meals, preassigned seats, membership in an airline reservation system, and a hub and spoke route system were critical to the success of an airline going forward. Southwest, which employed none of these, did not add them. Changes, however, were made. Gary Kelly, vice president and CFO, noted, "Management at the time recognized that with deregulation the competitive environment would be less stable. As a result we deleveraged to give us stability and added flexibility."

By April of 1993, Southwest was the seventh-largest (in terms of passengers) airline in the United States and had a history of strong financial performance (see **Exhibits 1** and **2** for financial performance). The airline served the majority of Southwestern markets as well as cities as far north as Chicago and as far east as Cleveland (see **Exhibit 3** for a route map). At the time, the airline was the number one intrastate carrier in California, a market characterized by heavy North-South business and leisure travel and formerly dominated by the largest domestic carriers such as United Airlines, American Airlines, and USAir.

The airline had retained the short-haul, high-frequency, low-cost, "luv" strategy of the 1970s. By 1993, restricted fares, tickets purchased 21 or 3 days in advance, or purchased at half price at least one day in advance under Southwest's "Friends Fly Free" policy, were also available (see **Exhibit 4** for typical discount schedules). All fares were either competitive with, or lower than, other airlines' prices, often leaving Southwest unscathed by fare wars conducted by other airlines (see **Exhibit 5**). Southwest continued to focus on short-haul flights, and in 1993 the average length of a Southwest flight was 65 minutes. Colleen Barrett, executive vice president with responsibility for customers, commented: "We've always seen our competition as the car. We've got to offer better, more convenient service at a price that makes it worthwhile to leave your car at home and fly us instead."

Southwest had won the unofficial "triple crown" of the airline industry 12 times by mid-1993. This comprised the fewest complaints, fewest delays, and fewest mishandled bags (per 1,000 passengers) over the period of one month, based on data the U.S. Department of Transportation began collecting in September 1987. Southwest also won the triple crown for the entire year of 1992.

[2]See Harvard Business School case number 575-060, "Southwest Airlines (A)."

No other carrier had ever won the triple crown, although competitors occasionally made claims disputed by Southwest in its advertisements (see **Exhibit 6**).

The Southwest Model

Southwest achieved remarkable success as the only profitable airline in the United States in 1992 by differentiating itself through its focus on service, operations, cost control, marketing, its people and the corporate culture.

Southwest Service—Family Fun

Southwest differentiated its service in terms of the flair with which it was delivered. An operating manager commented: "We're kind of a big family here, and families have fun together. The passengers are part of the family too, so we have fun with them."

Fun included playing games on board the aircraft, such as "Who has the biggest hole in your sock," as well as games and contests on the ground, particularly if a flight was delayed. A favorite was "guess the weight of the gate agent." Some flight attendants dressed in full-length bunny costumes and handed out colored eggs on Easter. Others hid in the overhead luggage compartments on the jets to surprise unsuspecting passengers with carry-on bags. Fun, however, was kept in its place. Barrett noted, "Business people just want to read their papers first thing in the morning."[3]

Fun was not restricted to passenger-related activities. Employees recalled Herb Kelleher's rap performance in the company's "shuffle" video and his appearance on the cover of *Texas Monthly* magazine dressed as Elvis Presley. Southwest treated employees to a variety of social events including a plane pull, which pitted local fire and police departments against each other.

Southwest made fun a part of day-to-day life. Ann Rhoades, vice president "people," commented:

> We try to hire people who are fun, and that translates to friendly. We want to be sure that they are going to be comfortable here, and we want to be sure that our passengers are going to be comfortable with them. Fun and friendliness come from the heart. We don't want a phony smile. We want a genuinely open spirit, someone who really likes people, and wants to help out.

The airline's management went to great lengths to encourage good relations between employees and passengers. Jim Wimberly, vice president ground operations and provisioning, described an example of this:

> We did an experiment, giving passengers traditional, printed boarding passes (without assigned seats) when they checked in at the ticket counter to drop their bags. That way they didn't have to wait in two lines (passengers ordinarily received boarding passes at a counter near the gate). The problem was that the employee collecting the passes at the gate had to read the print on them, in contrast to just looking at the color of the plastic boarding pass we usually give out. You know what? That employee had to focus on reading, instead of welcoming passengers on board. The employees didn't like it, and neither did the passengers.

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[3]"How I Did It: Pampering Customers on a Budget," *Working Woman*, April 1993.

Operations

Southwest's operations differed from those of the other major U.S. airlines in several ways. First, Southwest did all of its own ticketing, not making its seats available through computerized systems such as Apollo or Sabre. Travel agents received a standard 10% commission, but had to contact the airline directly to book seats. As a result, only 55% of Southwest's seats were booked through a travel agent in contrast to a 90% average for the industry.

Second, Southwest did not operate a hub-and-spoke route system. Instead, most Southwest passengers flew nonstop origin to destination only. Thirty percent of Southwest passengers remained on flights, continuing to a later destination, usually on the same airplane. Although Southwest did price these flights as through flights (in lieu of two separate flights), it generally did not promote connecting (versus nonstop) service. Executives commented that the airline's expansion beyond its home base in the southwest had resulted in an increase in the number of passengers traveling beyond a single destination.

Third, Southwest generally flew into uncongested airports of small cities or smaller, less congested airports of large cities. Love Field in Dallas, Midway in Chicago, and Detroit City Airport were examples of the latter. Los Angeles International Airport (LAX) was one of the few major, congested airports the carrier served. This reliance on secondary airports in major markets made it difficult for passengers to transfer from other airlines to Southwest flights or vice versa. It did, however, save an average of 15% to 25% of average flight time according to Jim Wimberly. These savings were a result of reduced taxi time, fewer gate holds and less in-air waiting (circling and altitude holds).

Fourth, the airline did not transfer baggage directly to other airlines ("interline baggage"), primarily because, according to one executive, "Southwest doesn't coordinate its services with other airlines."

Fifth, only drinks and snacks, most often peanuts, were served on board.

Sixth, although Southwest had an 84% unionized workforce, its labor relations were, according to Ann Rhoades, "excellent." She continued:

> Southwest people are helpful. We want to get the job done, so everyone helps out. Pilots help flight attendants pick-up the plane between flights, ramp service agents [baggage handlers] notice the condition of the planes, and pilots sometimes carry luggage, especially if it means achieving an on-time takeoff. Our contracts always include the clause, "those duties historically performed by" as part of job definitions, and everyone's always done just about everything here.
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> Occasionally when we enter a new city we lease a gate from another airline. Sometimes that means we have to use their ground handling crew. We try not to let that happen anymore, to a large degree because of the constraints it places on our people. Once, one of our pilots began loading luggage in that type of situation. The other carrier's baggage handler's union filed a complaint against us as a result. We just can't operate that way.

Seventh, Southwest flew only Boeing 737 jets. The company had 150 that, in total, flew an average of 1,500 trips per day. The 737 was the smallest plane in Boeing's fleet, seating 137 passengers. An executive stated that Southwest could buy new Boeing 737s for approximately $27 million and that the average market value of jets in the company's fleet was approximately $20 million each. The 737s had an average life of 20 years. The average age of Southwest's planes was seven years, one of the lowest averages in the industry. Other major U.S. airlines flew a variety of jet aircraft, many having five or more distinct plane types made by Boeing, McDonnell Douglas, or Airbus Industries.

Southwest also differed from its competitors in the time required to "turn" an aircraft. *Turn* referred to the time spent from the moment blocks were placed behind the wheels of an aircraft, signifying its arrival at the gate, to the time those blocks were removed, marking the beginning of push back. This period included the time in which passengers got on and off the plane, baggage was loaded on and off, the lavatories were emptied and cleaned, and the plane was tidied, refueled, provisioned with food and drinks,[4] and inspected. The last step was the signing of the "turn team form." This was a form given to the gate agent, listing the anticipated ground time and the number of passengers for the next flight. Just as the plane was ready to push back (marking the end of block time), the gate agent filled in the departure time and left a copy with the flight crew on board. The information on the form was used to measure a team's ability to turn flights in 15 (or 20) minutes or fewer. Teams consisted of everyone involved in turning the plane.

The U.S. industry average time for these steps (excluding the turn team form, which was not in common use) was 55 minutes. At Southwest, two of three planes were turned in 15 minutes or fewer. This time had been slowly increasing as the airline began flying to a greater variety of airports. The other one-third of flights had 20-minute turns scheduled.

Cost Control

Cost control was a prevailing part of the Southwest philosophy. A number of managers emphasized the Southwest perspective on cost control: "Airlines don't have revenue problems, they have cost problems."

Colleen Barrett commented on cost control at Southwest:

> We're one big family, and the family members expect a lot from one another. Part of that means watching costs carefully. We can't compete unless our costs are as low as, or lower than, our competitors, which means everybody needs to take part. For example, when the price of jet fuel skyrocketed during the Persian Gulf crisis, Herb sent a letter to every pilot asking if he or she would contribute ideas on how to save fuel. The pilots developed a new procedure for takeoffs and landings that was just as safe and saved a significant percentage of the fuel used in those maneuvers.

Jim Wimberly provided another example of cost control in operations:

> We buy fuel from a variety of vendors depending on which one has the best price. We've done business with most of these people for years so they know what our service and safety standards are. If we can get fuel cheaper in Houston than we can in El Paso, and if the price difference warrants carrying that extra fuel, we'll inventory fuel in the planes to take advantage of the lower price.

Pete McGlade, head of scheduling, remarked:

> There are issues of gate costs and landing fees, but those differ everywhere. They average about $2.50 across our system, with small airports coming in around $2.00 per passenger and major airports between $6.00 and $8.00.

[4]Planes were provisioned with food and drinks in 10 of Southwest's 31 cities; in the other cities flights were preprovisioned and ice was brought on board at each stop.

> Another significant cost driver is the number of departures we operate from an airport. We want to be sure that our people and machinery are as productive as possible, so the amount of traffic from an airport is important. We like to see at least 20 departures per day. That's 10 departures from each of two gates, which is about right, at least for us [see **Exhibit 7** for gate crew staffing levels]. This is complicated by the fact that at some airports, mostly the congested ones, we may be able to attract the customers, but not get the gates to serve them.

Herb Kelleher summed up the airline's attitude about costs:

> It's easy to offer great service at high cost. It's easy to offer lousy service at low cost. What's tough is offering great service at low cost, and that's what our goal is. To do it, we have to watch every penny. I personally approve all expenditures over $1,000, not so much because I don't trust our people, but because I know that if they know I'm watching, they'll be just that much more careful.

Southwest's cost per passenger mile was 7.3 cents in 1993. See **Exhibit 8** for additional cost and competitive data.

Marketing

Early Southwest marketing was based on the airline's low prices, convenience (frequency of departure and ease of airport use) and level of service (luv), stressing the airline's underdog and Texan home-grown image. As the airline expanded, it continued to emphasize price, convenience, and service.

An executive described Southwest's marketing for new cities:

> Eight weeks before we initiate service we begin a marketing blitz. We've been very successful in the Midwest by running our "Smart Campaign," a series of advertisements telling a city that it's smart (for example, Louisville, home of the Kentucky Derby and our most recent city, is smart about picking horses) and then pointing out how smart it is to fly Southwest based on our fares, frequency and credibility. We usually contact leaders individually and give them some type of passes. Then we initiate service.

Promotional devices involved public relations. These ranged from a Southwest-sponsored golf tournament, designed to raise money for Ronald McDonald Houses,[5] to painting a new 737 as if it were a Texas flag and dubbing it "The Lone Star over Texas." Other planes were painted to look like Shamu the Killer Whale, highlighting Southwest's relationship with both Sea World of Texas and California (see **Exhibit 9**).

Colleen Barrett was famous within Southwest for saying, "Once Customers fly on us three times they're hooked." Joyce Rogge, director of advertising and promotions, noted, "We have a lot of ambassadors out there—our Customers."[6]

[5]The Ronald McDonald House is a charity developed by McDonald's to enable families of sick children to stay near them during visits to hospitals.

[6]Southwest insisted on the use of a capital "C" in Customers.

People

Ann Rhoades described her People function:

> One of this department's chief functions is to bring in new Southwest employees that will fit into the organization. To do this we use selection devices that help identify attitudes rather than skills, and we put prospective employees through rigorous interviewing. A selection panel selects flight attendants, partly on the basis of responses to questions like, "What is your most embarrassing moment?" asked in front of about fifty other candidates. Customers are an important part of the selection process. They come voluntarily to Love Field, sit on the selection panel, and provide invaluable feedback used in the decision-making process.
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> We've started a program we call peer hiring. Pilots interview pilots and then make a hire or no hire recommendation to a committee. Line employees interview applicants and make a hire or no hire recommendation to management. We have been successful with, and therefore encourage, nepotism. We have 400 married couples out of 13,400 employees. Our only restriction is that relatives can't immediately report to one another. Anyone referred by a Southwest employee is guaranteed an interview.

Rhoades also stated that turnover had averaged 7% throughout the company for the last four years, although it was as high as 40% in California due to cost of living issues (employees received the same pay per job hour regardless of location). These figures, with the exception of California, were well below the industry average. Companywide turnover was projected to be only 4.5% in 1993.

The company was listed as one of the 10 best employers in the United States in 1992,[7] demonstrating employee satisfaction with Southwest. A taxi driver in the Dallas area commented, "Southwest, oh yeah, that's a good place to work. They say it's like one big family there."

Much of Southwest's training centered on team building. Training occurred at Southwest's "People University" which boasted two campuses. Cross-training was offered and employees were encouraged to switch jobs. Broad latitude was given to employees to enable them to serve customers. One rule used by an operating manager was, "Do whatever you feel comfortable doing for a customer." Ann Rhoades stated, "We want people to ask for forgiveness, not for permission." Rhoades continued, citing the example of a manager who made a $100,000 blunder who was promoted a few months later.

Recognition was an important element in employee and managerial motivation. Southwest's corporate offices (where casual dress was the norm all summer and on Fridays, except on or just before holidays when costumes were encouraged) had literally thousands of pictures of employees taken at celebrations, many of them recognition events. People sent a customized birthday card to every employee (and to a very few frequent fliers) and celebrated every other significant event in an employee's life (weddings, children, etc.). Managers' offices were covered with mementos of experiences and recognition, as well as ubiquitous pictures of airplanes.

Eighty percent of all promotions were internal. A manager commented:

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[7]Robert Levering and Milton Mosckowitz's book, *The 100 Best Companies to Work for in America*, had six categories in which they judged a company on a five-point scale. Southwest received a 5 in "Opportunities" and "Camaraderie/ Friendliness," and a 4 in "Pay/Benefits," "Job Security," "Pride in Work/Company," and "Openness/Fairness." The authors also noted that the biggest plus to Southwest was that "it's a blast to work here," and that the biggest minus was that "you may work your tail off."

> By bringing our people up through the ranks to positions their education might prevent them from getting at other airlines, we get the most loyal workforce you can imagine. We also save money, because we may not have to pay quite as much for them as we would if we went outside the organization.

Compensation varied by position. New flight attendants earned $13.37 for each standard one-way trip (fewer than 244 miles) and one-tenth that base amount for each additional 40 miles on longer trips.[8] A manager noted, "We pay our flight attendants at least as much, if not more, than the industry average." Flight attendants could work as many trips as they wanted, and could trade or give trips to other flight attendants. Thus, subject to being able to get another flight attendant to fly assigned trips, flight attendants could dictate their own hours and the number of days they worked. As a result, a manager noted that "some flight attendants fly no trips in some months. On the other hand, I've seen flight attendants work 150 flights in a month, too. It's really up to them." This was not the case at many airlines where work rules limited flight flexibility. Ground crew, ticket agents, and telephone service representatives started at $6.25 an hour, the average employee in these positions earning $20,000 per year.

While overall compensation levels at Southwest are lower than at other major airlines, Southwest managers are committed to their organization. Some managers reported offers from other airlines to double or triple their salaries. Said John Jamotta, manager, Schedule Planning: "The psychological satisfaction I derive from my job here at Southwest more than compensates for any wage differential with the other airlines. I could earn significantly more at a competitor, but I feel a real commitment to Southwest."

All employees were entitled to profit sharing, which was the company's only form of retirement program. Each year a percentage of the company's earnings before taxes was divided among employees based on their wages. In 1992 this amounted to 8.2% of each employee's wages. The money vested after five years of employment, but could not be removed until retirement or separation (although it could be used as loan collateral). Employees could choose among six investment vehicles, one of which was Southwest Airlines stock (ticket symbol LUV, the closing price of which was posted at the headquarters' front door), but were encouraged to diversify if they had too high a percentage in LUV alone. Employees held 10% of Southwest's stock. Employees emphasized that they felt a direct link between their personal involvement and the company's success, and the profit-sharing plan allowed them to share in the company's success.

Corporate Culture—"A Patina of Spirituality"

Herb Kelleher noted that what really set Southwest apart from its competitors was "a patina of spirituality." An observer from outside the organization noted about a visit to Southwest's offices:

> I've never seen so many people hug each other except at a family reunion. No one gets within ten feet of another person without at least saying hello. For the first half hour I was there I thought it was an act, but if it had been, they couldn't have kept it up for my several-day visit.

Members of all headquarters departments ventured into the field on a regular basis. Schedule planners, for example, spent a day working at a Southwest station once every six weeks, "to be sure we stay in touch," according to Pete McGlade, who wore a T-shirt emblazoned with the motto, "SWA = Schedulers With Attitudes."

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[8]Flight attendants were also paid a per diem of $2 for every hour they spent away from their base city, as well as receiving a hotel room for free. Base compensation increased annually to over $30 per flight segment for flight attendants who had been with the company many years.

Ann Rhoades described Southwest's unwritten rules: (1) You have to be compassionate to internal and external customers; (2) You have to have a positive attitude; (3) You have to want to work and use common sense; (4) You have to have a great sense of humor (humor diffuses stress); and (5) You can't be an elitist.

In light of the airline's growth and the increasing geographic diversity of its operations, Colleen Barrett was organizing ways to maintain what she called "the feeling of the place." She commissioned a culture committee, comprising 60 line employees from across the system, representing all departments, job classifications, and regions. The committee met four times a year and had numerous subcommittees that worked on various assignments throughout the year, all aimed at keeping the company's "small family and spirit." Committee members spent a great deal of time building relationships between departments so that (as Barrett put it) "teamwork and cooperative spirit will always be first and foremost in everyone's mind and we are all working toward one common goal." One of the committee's first products was a small paperback book, double-spaced and written in relatively large type, entitled *The BOOK on Service: What positively outrageous service looks like at Southwest Airlines*. The book described legendary acts of service performed for passengers, focusing on the employee performing the act.

In line with the fun culture at Southwest, the company sent all employees copies of Southwest's mission statement disguised as prizes in giant boxes of Cracker Jacks. Ann Rhoades noted, "That way we thought they'd read it."

John Jamotta described the Southwest culture:

> At Southwest, the community is most important. People have to let go of their personal egos. Without the success of the community, you can't have personal success. The U.S. needs a heavy dose of Southwest culture. It needs people who are more community-minded and less self-centered.

Expansion

Growth Strategy

Southwest pursued a conservative growth strategy. Expansion within the current route structure was first priority. As load factors increased, Southwest used new planes to add capacity to the current system or to add nonstop flights between cities previously connected by one-stop service. McGlade estimated that within any given year, 85% of expansion was internal. He estimated that in 1994, 14 of 16 new planes would be used for internal expansion.

Since deregulation in the late 1970s, Southwest had been steadily expanding to the West, North, and East. External expansion was often opportunity driven. For example, with the collapse of Midway Airlines in 1991, Southwest had the opportunity to move into Midway Airport in Chicago and establish an anchor in the Midwest. Herb Kelleher made a verbal commitment to the mayor of Chicago to provide 112 daily departures from Midway by 1995. Fulfilling this commitment was a key priority in the scheduling department, even if it meant forgoing other expansion opportunities. **Exhibit 10** shows the growth in weekly departures at Midway and in Southwest's total system.

An executive described a typical Southwest expansion:

> We don't do a lot of market research. Herb and the schedulers choose an appropriate market, then we negotiate for gates. We don't want to take any more gates than we need to open with, but we like to know that we can get more when we

need them, as the market expands. The negotiations are usually pretty straightforward because so many cities are asking us to provide service.

We do, however, have a problem with expansion. We are continually asked to enter new markets, and there is no way that we can meet the demand. We have to grow in a controlled way. Our main constraint is finding enough facilities.

Pete McGlade commented on new cities and routes:

In making a decision we talk to Herb about ground economics, in-air economics, total economics, and the spiritual aspect, what the effect is on our people.

We want to make sure that the way we conduct business in a city we enter will be consistent with the way we conduct business throughout our system. For example, if flights are continually subject to delays, it can bring our people down, it diminishes their work environment and could make them less enthusiastic about delivering outstanding customer service.

We have to feel that we can hire Southwest-type people, in both front-line and managerial positions. We have to believe that the traveling public will warm to our type of service. Not everyone wants to be hustled on and off a plane, or hear about their fellow passengers' socks. We're not for everyone or everywhere.

Market Entry Strategy

Dave Ridley, director of marketing and sales, and one of the executives in charge of pricing, described how the company approached pricing new routes, particularly into and out of a new city:

We're looking to grow the market when we go into a new city. When we enter, air travel has often dwindled as a result of high prices and poor service. We can often quadruple or quintuple the number of passengers on a particular route. At the very least we can always double it. We do it by pricing against ground transportation as much as against existing air service. This results in prices at least 60% below competitive airfares and sometimes 75% or 80% below. One of the tests to see if the pricing is low enough is whether people will talk about our fares at cocktail parties. Of course, we have to be able to sustain and make money at these prices, which we can do because of our low operating costs.

John Jamotta, manager of schedule planning, spoke about Southwest's load factors:

The industry wisdom is that load factors are related to your dominance at an airport. We think about it in a different way. Early in the life of a city with Southwest, we tend to see higher-than-average load factors. When we go in with a low price we expand the market faster than we can add equipment, so demand outpaces supply. If our competitors respond and drop price, that stimulates the market even further, and demand continues to outstrip supply.

Once we've been in a city for a while, we add more and more service and eventually the supply and demand start to balance, which may eventually lead to an average load factor. Different cities mature at different rates, so the timing is hard to predict, but the trend is pretty clear.

Southwest's market-entry strategy had a dramatic impact on many of the markets it entered. For example, Southwest nearly quadrupled the Oakland-Burbank passenger market within two years of its entry. Less than three years after entry, USAir and United, the primary carriers prior to Southwest's entry, were virtually nonexistent in the market and Southwest had captured nearly the entire market. **Exhibit 11** shows the "Southwest effect" on the Burbank-Oakland market. A recent Department of Transportation study stated that the dramatic growth of Southwest had become "the principal driving force" in changes occurring in the airline industry. (See **Exhibit 12** for a summary of the report.)

The Immediate Expansion Decision

Faced with the immediate delivery of two uncommitted 737's, Pete McGlade and the scheduling team reviewed their options.

The first option was to expand within the system and add a new segment directly between Detroit and Phoenix. Over 500 letter writers in each city had requested the Detroit to Phoenix route. A manager noted:

> It appears that there is a strong Detroit-Phoenix business connection, a lot of retired individuals traveling the route and a number of people who are willing to stop in Phoenix, but stay on the flights until they reach their final destinations on the West Coast. I think we can run three round trips a day on this route at our average load factor of 65%. I'm particularly confident about this because of our ability to draw people to a route like this by offering great prices all the way through to the West Coast.

Airport gate and landing fees would be slightly higher than the Southwest system average of $2.50 per passenger. A schedule analyst estimated the fee per passenger would be approximately $2.75 in Phoenix and $3.25 in Detroit.

The second option was to enter the Dayton market. With a population of 970,000, Dayton was 226 miles from Chicago Midway Airport. Initiating service to Dayton would allow Southwest to contribute to its growth goals in Chicago. All destinations would be shorthaul flights, averaging 50 minutes for the foreseeable future. The historical flight pattern between Dayton and Midway had been relatively stable over the past two years, though fares had been climbing. **Exhibit 13** provides market history. The airport was relatively uncongested, and there was adequate room for expansion if required. Airport gate and landing fees would be lower than the Southwest system average of $2.50 per passenger. A schedule analyst estimated the fee per passenger would be approximately $2.00 in Dayton.

The final option was to establish a base on the East Coast, initiating service in Baltimore. With a population of 2.4 million, Baltimore was within an hour's drive or train ride from Washington D.C. **Exhibit 13** shows the market history for the Baltimore area (including D.C. and Northern Virginia) and Chicago Midway. Baltimore is 611 miles from Chicago, longer than the Southwest system average of 375 miles. Flights in and out of Baltimore would average 90 minutes in the near term, given Baltimore's geographic separation from the rest of the Southwest flight system. The airport was uncongested and would allow room for future expansion as an East Coast base. Airport fees were estimated to be in line with the system average.

There were concerns, however, about entering Baltimore. In addition to its geographic separation from the system, many feared that the airline would be unable to find Southwest-type employees on the East Coast. McGlade stressed that Southwest would possibly pass over a city if it could not retain the Southwest "luv" culture. There were additional concerns about the weather conditions on the East Coast. The Southwest model had been so successful in the past because the airline had minimized delays, contributing to decreased costs and improved employee morale and customer service. Southwest had previously entered Denver, and pulled out because the weather in

Denver alone contributed to over 50% of the delays in the entire system. Any entry into Baltimore would have to be gradual to test East Coast weather and people concerns.

Southwest managers discussed possible pricing for their proposed cities, saying, "We have a pricing philosophy, based on mileage, that we won't change to enter a new city or create a new route." See **Exhibit 14** for historical pricing information. Pricing for route lengths of three to three and one-half hours (such as would be the case for Detroit to Phoenix, which was a three and one-half hour flight) generally averaged (all seats) $99 to $129 either way. Managers noted that flights of over three hours experienced 20% to 25% lower total costs due to a number of factors including more efficient use of jet fuel at consistent high altitudes and fewer aggregate airport fees.

Managers also discussed the number of flights they sought to schedule in a new city: "We like to go in with 10 departures a day at first, but we'll hope to expand quickly to 20 departures to use our two gates."

Jim Wimberly discussed ground crews and construction costs:

> I'd want to go into Dayton and Baltimore with a ground crew of about 40 people. With respect to construction costs, it's hard to know without actually getting bids, but in general it will cost approximately $1 million to put in two gates and associated improvements in a major city airport. At a smaller airport the cost might be $500,000.

Southwest leased jets with full crews flying under operating conditions and expenses identical to those experienced in average day-to-day operations for $4,000 an hour which, according to an executive, "provides a reasonable return."

Conclusion

As McGlade and the scheduling team deliberated the scheduling decision, they considered the importance of focus and consistency in Southwest's success formula. John Jamotta emphasized that there were 13,000 schedule planners[9] at Southwest:

> Every schedule decision we make must be consistent with our strategy. Our employees need to internalize the strategy, and consistency is necessary to ensure that everyone understands the scheduling decisions.

McGlade echoed these sentiments: "If there is confusion about the service, then there is confusion on the front line. If you have multiple messages, how can you expect an agent to carry out both?"

As the team examined the options, they faced issues more difficult to quantify than ground and air economics. How would the decision fit with the Southwest model? With the growth strategy? What impact would it have on the Southwest "patina of spirituality?" How would Herb react to their recommendation?

[9]There were approximately 13,000 employees at Southwest.

Exhibit 1 Southwest Airlines Co.—Consolidated Statement of Income ($ in thousands except per share amounts)

	Years Ended December 31,		
	1992	**1991**	**1990**
Operating revenues:			
Passenger	$1,623,828	$1,267,897	$1,144,421
Freight	33,088	26,428	22,196
Other	28,262	19,280	20,142
Total operating revenues	$1,685,178	$1,313,605	$1,186,759
Operating expenses:			
Salaries, wages and benefits	501,870	407,961	357,357
Fuel and oil	243,543	225,463	242,001
Maintenance materials and repairs	120,578	97,598	82,887
Agency commissions	106,372	81,245	72,084
Aircraft rentals	64,169	49,171	26,085
Landing fees and other rentals	102,717	83,177	61,167
Depreciation	101,188	86,202	79,429
Other operating expenses	262,105	219,852	183,870
Total operating expenses	$1,502,542	$1,250,669	$1,104,880
Operating income	$182,636	$62,936	$81,879
Other expenses (income):			
Interest expense	58,941	43,939	32,001
Capitalized interest	(15,350)	(15,301)	(13,738)
Interest income	(10,344)	(10,631)	(7,595)
Nonoperating losses (gains), net	2,552	1,089	(3,542)
Total other expenses	$35,799	$19,096	$7,126
Income before income taxes and cumulative effect of change in accounting principle	$146,837	$43,840	$74,753
Provision for income taxes	55,816	16,921	27,670
Income before cumulative effect of change in accounting principle	$91,021	$26,919	$47,083
Cumulative effect of change in accounting principle	12,538	-	-
Net income	$103,559	$26,919	$47,083
Per share amounts:			
Income before cumulative effect of change in accounting principle	$.97	$.31	$.55
Cumulative effect of change in accounting principle	.13	-	-
Net income	$1.10	$.31	$.55
Pro forma amounts assuming the new method is applied retroactively:			
Net income	$91,021	$27,109	$47,538
Net income per share	$.97	$.32	$.56

Exhibit 1 (continued) Southwest Airlines Co.—Consolidated Balance Sheet ($ in thousands except share and per share amounts)

	December 31, 1991	December 31, 1990
Assets:		
Current assets:		
Cash and cash equivalents	$411,036	$260,856
Accounts receivable	51,787	47,507
Inventories of parts and supplies, at cost	30,758	23,036
Prepaid expenses and other current assets	12,505	8,602
Total current assets	$506,086	$ 340,001
Property and equipment, at cost:		
Flight equipment	1,842,517	1,551,519
Ground property and equipment	287,923	218,522
Deposits on flight equipment purchase contracts	212,904	182,932
	$2,343,344	$1,952,973
Less allowance for depreciation	559,052	458,779
	$1,784,292	$1,494,194
Other assets	2,599	3,096
	$2,292,977	$1,837,291
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$78,358	$54,970
Accrued liabilities	216,648	150,870
Air traffic liability	55,850	42,069
Income taxes payable	6,744	377
Current maturities of long-term debt	10,760	6,583
Total current liabilities	$368,360	$254,869
Long-term debt less current maturities	699,123	617,016
Deferred income taxes	133,430	105,757
Deferred gains from sale and leaseback of aircraft	224,645	222,818
Other deferred liabilities	13,166	8,310
Commitments and contingencies		
Stockholders' equity:		
Common stock, $1.00 par value: 200,000,000 shares authorized: 92,472,755 shares issued in 1992 and 42,437,922 shares in 1991	92,473	42,438
Capital in excess of par value	155,938	81,987
Retained earnings	605,928	507,259
	$854,339	$631,684
Less treasury stock, at cost (2,904 shares in 1992; 217,732 shares in 1991)	86	3,163
Total stockholders' equity	$854,253	$628,521
Total liabilities and stockholders' equity	$2,292,977	$1,837,291

Exhibit 2 Southwest Airlines Co.—Ten-Year Summary (in thousands except per share amounts)

	1992	1991	1990	1989	1988	1987	1986	1985[h]	1984	1983
Selected Consolidated Financial Data										
Operating revenues:										
Passenger	$1,623,828	$1,267,897	$1,144,421	$973,568	$828,343	$751,649	$742,287	$656,689	$519,106	$433,388
Freight	33,088	26,428	22,196	18,771	14,433	13,428	13,621	13,643	12,115	10,357
Other	28,262	19,280	20,142	22,713	17,658	13,251	12,882	9,340	4,727	4,491
Total operating revenues	$1,685,178	$1,313,605	$1,186,759	$1,015,052	$860,434	$778,328	$768,790	$679,672	$535,948	$448,236
Operating expenses	1,502,542	1,250,669	1,104,880	917,426	774,454	747,881	679,827	601,148	467,451	379,738
Operating income	$182,636	$62,936	$81,879	$97,626	$85,980	$30,447[e]	$88,963	$78,524	$68,497	$68,498
Other expense (income), net	35,799	19,096	7,126[b]	(13,356)[c]	620[d]	1,374[g]	$23,517[f]	17,740	649	4,927
Income before income taxes	$146,837	$43,840	$74,753	$110,982	$85,360	$29,073	$65,446	$60,784	$67,848	$63,571
Provision for income taxes	55,816	16,921	27,670	39,424	27,408	8,918	15,411	13,506	18,124	22,704
Net income	$91,021[a]	$26,919	$47,083	$71,558	$57,952	$20,155	$50,035	$47,278	$49,724	$40,867
Net income per common and common equivalent share	$.97[a]	$.31	$.55	$.79	$.61	$.21	$.51	$.51	$.56	$.46
Cash dividends per common share	$.05300	$.05000	$.04835	$.04665	$.04415	$.04335	$.04335	$.04335	$.04335	$.04335
Total assets	$2,292,977	$1,837,291	$1,471,138	$1,415,096	$1,308,389	$1,042,640	$1,061,419	$1,002,403	$646,244	$587,258
Long-term debt	$699,123	$617,061	$36,956	$354,147	$369,541	$251,130	$339,069	$381,308	$153,314	$158,701
Stockholders' equity	$854,253	$628,521	$604,851	$587,316	$567,375	$514,278	$511,850	$466,004	$361,768	$314,556
Consolidated Financial Ratios										
Return on average total assets	4.4%[a]	1.6%	3.3%	5.2%	5.1%	1.9%	4.8%	5.6%	8.1%	8.1%
Return on average stockholders' equity	11.7%[a]	4.4%	7.9%	12.4%	10.8%	4.0%	10.3%	11.4%	14.7%	14.2%
Debt as a percentage of invested capital	45.0%	49.5%	35.1%	37.6%	39.4%	32.8%	39.8%	45.0%	29.8%	33.5%
Consolidated Operating Statistics										
Revenue passengers carried	27,839,284	22,669,942	19,830,941	17,958,263	14,876,582	13,503,242	13,637,515	12,651,239	10,697,544	9,511,000
RPMs (000s)	13,787,005	11,296,183	9,958,940	9,281,992	7,676,257	7,789,376	7,388,401	5,971,400	4,669,435	3,893,821
ASMs (000s)	21,366,642	18,491,003	16,411,115	14,796,732	13,309,044	13,331,055	12,574,484	9,884,526	7,983,093	6,324,224
Load factor	64.5%	61.1%	60.7%	62.7%	57.7%	58.4%	58.8%	60.4%	58.5%	61.6%
Average length of passenger haul	495	498	502	517	516	577	542	472	436	409
Trips flown	438,184	382,752	338,108	304,673	274,859	270,559	262,082	230,227	200,124	175,421
Average passenger fare	$58.33	$55.93	$57.71	$54.21	$55.68	$55.66	$54.43	$51.91	$48.53	$45.57
Passenger revenue yield per RPM	11.78¢	11.22¢	11.49¢	10.49¢	10.79¢	9.65¢	10.05¢	11.00¢	11.12¢	11.13¢
Operating revenue yield per ASM	7.89¢	7.10¢	7.23¢	6.86¢	6.47¢	5.84¢	6.11¢	6.88¢	6.71¢	7.09¢
Operating expenses per ASM	7.03¢	6.76¢	6.73¢	6.20¢	5.82¢	5.61¢	5.41¢	6.08¢	5.86¢	6.00¢
Fuel cost per gallon (average)	60.82¢	65.69¢	77.89¢	59.46¢	51.37¢	54.31¢	51.42¢	78.17¢	82.44¢	85.92¢
Number of employees at year end	11,397	9,778	8,620	7,760	6,467	5,765	5,819	5,271	3,934	3,462
Size of fleet at year end[i]	141	124	106	94	85	75	79	70	54	46

[a]Excludes cumulative effect of change in accounting principle of $12.5 million ($.13 per share).
[b]Includes $2.6 million gains on sales of aircraft and $3.1 million from the sale of certain financial assets.
[c]Includes $10.8 million gains on sales of aircraft, $5.9 million from the sale of certain financial assets, and $1.2 million from the settlement of a contingency.
[d]Includes $5.6 million gains on sales of aircraft and $3.6 million from the sale of certain financial assets.
[e]Includes TranStar's results through June 30, 1987.
[f]Includes $10.1 million net gains from the discontinuance of TranStar's operations and $4.3 million from the sale of certain financial assets.
[g]Includes a gain of $4 million from the sale of aircraft delivery positions
[h]Includes the accounts of TranStar since June 30, 1985.
[i]Includes leased aircraft

Exhibit 3 Southwest Airlines Route Map: Summer 1993

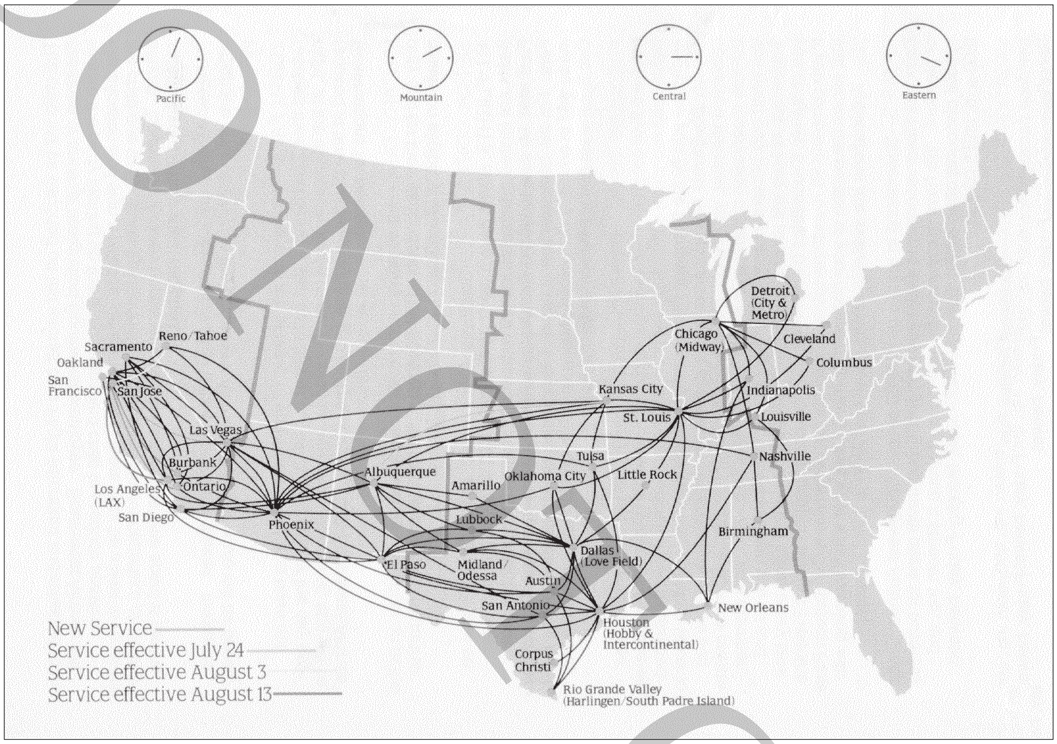

Exhibit 4 Typical Southwest Airlines Discount Schedule

Route: Phoenix to El Paso

Unrestricted fare: $59 (roundtrip fare $118)

3-day advance purchase roundtrip fare: $98 (no one-way fare available)

21-day advance purchase one-way fare: $44 (roundtrip fare $88)

Friends Fly Free roundtrip fare: $118 (for two tickets, no one-way fare available)

Route: St. Louis to Detroit

Unrestricted fare, Monday-Friday before 7:00 p.m.: $79 (roundtrip fare $158)

Unrestricted fare, Monday-Friday after 7:00 p.m. and weekends: $69 (roundtrip fare $138)

3-day advance purchase roundtrip fare: $112 (no one-way fare available)

21-day advance purchase one-way fare: $46 (roundtrip fare $92)

Friends Fly Free roundtrip fare: $158 weekdays before 7:00 pm/$138 other times (for two tickets, no one-way fare available)

The availability of reduced-rate seats differed on all flights, based on the airline's efforts to maximize revenue.

Exhibit 5 Southwest Advertisement

Exhibit 6 Southwest Advertisement

Exhibit 7 Ground Crew Staffing Levels

Jim Wimberly gave an approximation of the number of necessary Southwest groundcrew based on the number of departures at an average Southwest city:

10 Departures, 35 People

20 Departures, 45 People

30 Departures, 60 People

60 Departures, 120 People

He added, "Beyond thirty departures you don't save a lot because you have flight times overlapping, so you have to keep adding people, that goes for ramp and gate agents, and ticket counter staff too. Actually, it's not too bad because our average competitor runs with a least three times as many ground crew as we do."

Exhibit 8 1992 Results/Productivity: Major Carriers

Airline	Alaska 106	American 106	Delta	Northwest 106	Southwest	UAL Corp. 106	USAir Inc. 106	Average	Chapter 11 Carriers: America West	Continental	TWA
Revenue (000)	$908,286	$13,581,000	$11,579,200	$7,963,785	$1,685,178	$12,889,700	$6,235,622	$7,834,682	$1,294,840	$5,403,313	$3,634,493
Operating expenses (000)	$1,009,299	$13,658,000	$12,401,300	$8,272,589	$1,502,542	$13,427,500	$6,611,167	$8,126,057	$1,368,952	$5,559,331	$4,039,093
Operating profit (000)	$(101,013)	$(77,000)	$(822,100)	$(308,804)	$182,636	$(537,800)	$(375,545)	$(291,375)	$(74,112)	$(156,018)	$(404,600)
Operating margin	-11.12%	-0.57%	-7.10%	-3.88%	10.84%	-4.17%	-6.02%	-3.72%	-5.72%	-2.89%	-11.13%
Interest expense	$33,747	$386,000	$168,900	$171,783	$58,941	$327,800	$229,643	$196,688	$55,826	$138,807	$110,096
Net profit before FASB 106	$(76,534)	$(274,000)	$(568,800)	$(275,149)	$91,021	$(417,200)	$(589,676)	$(301,477)	$(131,760)	$(299,429)	$(403,003)
Net profit after FASB 106	$(81,101)	$(735,000)	NA	$(386,203)	NA	$(956,800)	$(1,228,498)	$(677,520)	NA	NA	NA
Net margin	-8.93%	-5.41%	-4.91%	-4.85%	5.40%	-7.42%	-19.70%	-8.65%	-10.18%	-5.54%	-11.09%
Interest as % of expenses	3.34%	2.83%	1.36%	2.08%	3.50%	2.44%	3.47%	2.42%	4.08%	2.50%	2.73%
Wages, benefits, etc. (000)	$305,035	$4,690,000	$4,705,600	$2,745,796	$501,870	$4,562,500	$2,492,424	$2,857,304	$324,255	$1,310,035	$1,475,840
Wages as % of expenses	30.22%	34.34%	37.94%	33.19%	29.78%	33.98%	37.70%	35.17%	23.69%	23.56%	36.54%
Fuel (000)	$145,109	$1,862,000	$1,581,500	$1,236,704	$243,543	$1,679,500	$726,605	$1,069,952	$186,042	$829,763	$613,846
Fuel as % of expenses	14.38%	13.63%	12.75%	14.95%	14.45%	12.51%	10.99%	13.14%	13.59%	14.93%	15.20%
Cost per ASM[a] (cents)	10.5	8.93	9.44	9.09	7.03	9.6	10.83	9.35	7.1	8.39	9.04
Wages, benefits per ASM	3.17	3.07	3.58	3.08	2.35	3.32	4.18	3.32	1.68	1.93	3.31
Yield (cents)	14.5	12.21	13.33	11.78	11.78	12.2	16.49	13.18	10.31	10.77	10.22
Employees	6,659	102,400	74,600	47,256	11,397	83,900	48,900	53,587	10,233	38,300	25,500
Fleet	72	672	555	373	141	536	440	398	86	319	172
Passengers (000)	6,249	86,007	83,117	43,443	27,839	66,692	54,655	52,572	15,173	38,358	22,391
RPMs[b] (000)	5,537,000	97,425,000	80,495,297	58,226,330	13,787,005	92,690,000	35,097,000	54,751,090	11,780,568	43,072,000	28,882,000
ASMs (000)	9,617,000	152,996,000	131,388,505	89,141,911	21,366,642	137,491,000	59,667,000	85,952,580	19,271,353	67,977,000	44,651,000
Revenue per employee	$136,400	$132,627	$155,217	$168,524	$147,862	$153,632	$127,518	$146,204	$126,536	$141,079	$142,529
Operating profit per employee	$(15,169)	$(752)	$(11,020)	$(6,535)	$16,025	$(6,410)	$(7,680)	$(5,437)	$(7,242)	$(4,074)	$(15,867)
Net profit per employee	$(12,179)	$(7,178)	$(7,625)	$(8,173)	$7,986	$(11,404)	$(25,123)	$(12,643)	$(12,876)	$(7,818)	$(15,804)
Average wage per employee	$45,808	$45,801	$63,078	$58,105	$44,035	$54,380	$50,970	$53,326	$31,687	$34,205	$57,876
Interest burden per employee	$5,068	$3,770	$2,264	$3,635	$5,172	$3,907	$4,696	$3,670	$5,455	$3,624	$4,317
Passengers per employee	938	840	1,114	919	2,443	795	1,118	981	1,483	1,002	878
RPMs per employee	831,506	951,416	1,079,025	1,232,147	1,209,705	1,104,768	717,730	1,021,715	1,151,233	1,124,595	1,132,627
ASMs per employee	1,444,211	1,494,102	1,761,240	1,886,362	1,874,760	1,638,749	1,220,184	1,603,969	1,883,255	1,774,856	1,751,020
Employees per aircraft	92	152	134	127	81	157	111	134	119	120	148

Source: Commercial Aviation Report, May 15, 1993.

Notes: 106 Denotes carrier affected by FASB 106 accounting charge (related to pension funding).
All companies listed are for airline units only, except UAL Corp which does not break out United.
Delta Air Lines for calendar 12 months ended December 31, unaudited; DAL FY is June 30, 1993.
Net profit margin and net profit per employee are after FASB 106 charges, where applicable.

May not foot to figures in the case due to the use of disguised figures.

[a]Airplane Seat Mile.
[b]Revenue Passenger Mile.

Exhibit 9 Southwest Airplanes

Exhibit 10 Weekly Departures

	Total Departures	Midway Departures	Midway %of Expansion	Midway % of Total Departures
January 1991	7,141	276		4%
January 1992	7,868	306	4%	4
January 1993	9,063	399	8	4
January 1994	10,521	494	7	5

Exhibit 11 Southwest Effect on Burbank-Oakland Market

Airline	1989 1	1989 2	1989 3	1989 4	1990 1	1990 2	1990 3	1990 4	1991 1	1991 2	1991 3	1991 4	1992 1	1992 2	1992 3	1992 4
Burbank-Oakland Number of Passengers (10% sample)																
American	5	7	14	11	12	1	0	1	1	3	2	1	1	1	1	0
Alaska Airlines	1,149	788	560	372	322	1,739	586	457	620	537	464	586	313	371	0	0
Delta	1	2	0	1	1	0	1	0	0	0	1	0	1	1	1	0
America West	4	1	11	18	18	19	47	15	12	6	38	36	53	25	10	2
Other	3	14	21	19	0	5	5	3	22	14	12	9	10	0	0	0
United Airlines	14	30	31	23	17	3,414	6,008	4,930	6,751	6,757	7,014	6,058	4,628	5,259	396	108
Unknown	2	13	2	0	1	1	3	2	1	0	6	0	5	6	3	1
USAir	4,507	6,532	5,813	5,620	4,415	8,060	8,478	6,756	4,170	1,115	0	0	0	1	0	0
Southwest	0	0	0	0	0	14,159	11,761	8,745	10,764	11,457	11,989	12,763	14,079	15,999	18,125	17,283
Total	5,685	7,387	6,452	6,064	4,786	27,398	26,889	20,909	22,341	19,889	19,526	19,453	19,090	21,663	18,536	17,394
Southwest share	**0%**	**0%**	**0%**	**0%**	**0%**	**52%**	**44%**	**42%**	**48%**	**58%**	**61%**	**66%**	**74%**	**74%**	**98%**	**99%**
Burbank-Oakland Revenues (000), (10% sample)																
American	1	1	1	1	1	0	0	0	0	0	0	0	0	0	0	0
Alaska Airlines	119	61	37	26	32	77	24	18	20	20	18	22	15	18	0	0
Delta	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
America West	1	0	1	2	1	2	4	2	1	1	4	3	5	2	1	0
Other	0	1	1	1	0	0	1	0	2	1	1	1	1	0	0	0
United Airlines	2	2	2	2	1	155	273	225	285	302	308	284	224	278	19	4
Unknown	0	1	0	0	0	0	0	0	0	0	0	0	0	1	0	0
USAir	433	466	407	461	462	419	402	352	201	51	0	0	0	0	0	0
Southwest	0	0	0	0	0	648	516	406	428	460	494	543	597	718	884	899
Total	556	532	449	493	497	1,301	1,220	1,003	937	835	825	853	842	1,017	904	903
Southwest share	**0%**	**0%**	**0%**	**0%**	**0%**	**50%**	**42%**	**40%**	**46%**	**55%**	**60%**	**64%**	**71%**	**71%**	**98%**	**100%**

Exhibit 12 Department of Transportation Press Release

U.S. Department of Transportation

News:

Office of the Assistant Secretary for Public Affairs
Washington, D.C. 20590

FOR RELEASE TUESDAY
May 11, 1993

DOT 35-93
Contact: Ed O'Hara
Tel.: (202) 366-5571

SOUTHWEST CARRIES MORE PASSENGERS
IN MAJOR MARKETS, DOT STUDY FINDS

Southwest Airlines has become the dominant airline in the nation's busiest markets, a Department of Transportation study has found.

In the top 100 city-pair markets with the most passengers in the 48 contiguous states, Southwest now carries more passengers than any other airline, including each of the Big Three airlines, the study found. These 100 markets represent about one-third of domestic passengers. In terms of passengers carried, Southwest now ranks fifth among U.S. airlines.

The dramatic growth of Southwest has become "the principal driving force" in changes occurring in the airline industry, the report said. Southwest has much lower operating costs than most airlines and its presence has resulted in fares that are on the order of one-half those charged in short-haul markets where Southwest does not operate. The airline focuses on providing frequent service in busy markets of less than 500 miles, such as Chicago-St. Louis and Los Angeles-Phoenix.

The study found that Southwest affects the prices paid by one out of three passengers in the largest U.S. markets. Because of the low-cost competition from Southwest, the largest airlines rarely try to compete with the Dallas-based airline.

As Southwest continues to expand, other airlines will be forced to develop new low-cost service in short-haul markets.

The study suggests low-cost new entrant airlines will have an important role to play in the future. They could serve as a discipline for Southwest's pricing and could replace other airlines that are scaling back service in markets dominated by Southwest.

The study found that air fares in markets served by Southwest were dramatically lower than in other short-haul markets. For the year ending Sept. 30, 1992, the average one-way fares for markets

(continued on next page)

Exhibit 12 (continued)

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where Southwest does not operate for distances of less than 250 miles and for 251-500 miles, were $110 and $130, respectively. In Southwest markets of similar distances, the average prices charged by all carriers were $56 and $58, respectively.

In the past year, DOT has seen an increase in new carriers. Some 16 new jet carriers have begun operations, including five providing scheduled passenger service. Three more have received approvals to operate, and applications from nine new jet carriers are pending before the department.

The DOT study also found:

o In its own top 100 markets, Southwest has an average 65 percent share compared with less than 40 percent for most airlines in their own top markets, except for Northwest which has 43 percent.

o Experience in the California Corridor, the busiest domestic market, shows how quickly Southwest can gain a dominant presence in busy markets. After several years of trying to compete for market share against Southwest's low-cost service, other airlines have given up such efforts.

o The unit costs of other airlines are 50 percent to 70 percent higher than Southwest's, except for America West, with unit costs that are 20 percent higher.

The study grew out of the department's regular monitoring of the competitive structure of the airline industry. In 1990, DOT completed a comprehensive study of airline competition and issued its findings. Since then, it has periodically updated that study. In the past year, Southwest has become a larger and more important player in the industry. This study analyzes the airline's effect on prices and service.

Copies of the report, prepared by Randall D. Bennett and James M. Craun, are available from the DOT Office of Aviation Analysis, P-50, U.S. Department of Transportation, Washington, D.C. 20590.

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Exhibit 13 Market Histories

	1Q92	2Q92	3Q92	4Q92	1Q93	2Q93
Detroit-Phoenix						
Detroit (City and Metro airports)-Phoenix:						
Originations and Departures (O&D's)[a]	6,669	6,579	6,199	5,940	6,705	6,859
Average one-way fare	$157	$151	$139	$157	$171	$166
Dayton						
Dayton-Chicago (Midway and O'Hara):						
Originations and Departures (O&D's)[a]	2,093	2,396	2,238	1,958	1,833	2,149
Average one-way fare	$146	$125	$131	$146	$174	$162
Dayton-Philadelphia:						
Originations and Departures (O&D's)[a]	978	1,138	982	1,035	991	1,316
Average one-way fare	$185	$144	$141	$157	$192	$164
Dayton-St. Louis:						
Originations and Departures (O&D's)[a]	624	740	698	571	646	681
Average one-way fare	$185	$145	$148	$156	$188	$167
Baltimore						
Baltimore (BWI, DCA, IAD)[b]-Chicago (Midway and O'Hara):						
Originations and Departures (O&D's)[a]	22,552	30,677	27,998	25,025	22,718	32,379
Average one-way fare	$187	$149	$146	$165	$187	$166

	1989	1990	1991	1992
O&D[a] breakout by airport—				
Chicago (Midway and O'Hara) and:				
BWI	22,104	23,607	24,825	24,809
DCA	65,728	65,310	65,538	67,085
IAD	14,134	14,048	14,037	14,258
Total	101,966	102,965	104,400	106,152
Cleveland and:				
BWI	7,076	6,772	6,563	5,889
DCA	13,825	13,181	10,539	7,864
IAD	3,777	3,653	4,074	3,225
Total	24,678	23,606	21,176	16,978
Louisville and:				
BWI	2,458	2,327	2,490	2,357
DCA	7,312	7,312	6,797	6,995
IAD	415	511	616	510
Total	10,185	10,150	9,903	9,862

[a]Extrapolated from a ten percent sample. An "origination" (or a "departure") represents one individual flying one-way.

[b]BWI (Baltimore Washington International Airport) is located south of Baltimore, between Baltimore and Washington, D.C.; DCA (Washington National Airport) is located in D.C.; IAD (Washington Dulles Airport), is located about 30 minutes outside D.C. in suburban Virginia.

Exhibit 14 Southwest Pricing

Southwest's commitment to low fares as a long-term business strategy is demonstrated by the average fares for the fourth quarter of 1992 (as reported in DOT Form 41 data) in Southwest's original markets, which have been served for almost 22 years:

DALLAS-HOUSTON	$ 51.90	(239 miles)
DALLAS-SAN ANTONIO	48.10	(248 miles)
HOUSTON-SAN ANTONIO	50.20	(192 miles)

It is interesting to compare these with the average fares in comparable-distance markets not served by Southwest. For example:

LAGUARDIA-WASH. DC	$ 95.70	(214 miles)
LAGUARDIA-BOSTON	92.60	(185 miles)
MIAMI-TAMPA	107.80	(204 miles)
ST. LOUIS-MEMPHIS	156.90	(256 miles)
ATLANTA-NASHVILLE	160.00	(214 miles)
ATLANTA-CHARLOTTE	163.60	(227 miles)

Even in smaller markets, where Southwest has for years provided service as the *sole* air carrier, our low-fare business strategy has precluded the temptation to raise fares indiscriminately. Our average fares (for the fourth quarter of 1992) in the following markets, which are served only by Southwest, are illustrative:

KANSAS CITY-TULSA	$ 49.00	(223 miles)
KANSAS CITY-OKLA. CITY	47.40	(312 miles)
EL PASO-LUBBOCK	49.40	(294 miles)
EL PASO-MIDLAND	49.30	(246 miles)
AUSTIN-MIDLAND	54.40	(290 miles)
ALBUQUERQUE-AMARILLO	49.00	(277 miles)
ALBUQUERQUE-LUBBOCK	46.20	(289 miles)

Average Southwest fares for longer-haul markets included:

LOS ANGELES-ALBUQUERQUE	$ 74.00	(677 miles)
ALBUQUERQUE-ST. LOUIS	100.00	(934 miles)
PHOENIX-SAN ANTONIO	95.00	(843 miles)

Source: Company document.

Exhibit 15 Southwest Airlines Co. Organizational Chart