Ann Rhoades, vice president of people for Southwest Airlines, was packing her briefcase at the end of a 17-hour day. Tomorrow was an off-site meeting with the top nine executives of Southwest Airlines. The agenda for the meeting was to review Southwest’s competitive position in light of recent actions by United and Continental, both of whom had entered Southwest’s low fare market. That day’s *New York Times* (September 16, 1994) had an article that characterized the situation as a major showdown in airline industry:

This is a battle royal that has implications for the industry, said Kevin C. Murphy, an airline stock analyst at Morgan Stanley. The battle will, after all, be as much a test of strategy as a contest between two airlines. United and other big carriers like USAir and Continental have decided that they can lower their costs by creating a so-called airline-within-an-airline that offers low fares, few flights, and frequent service. The new operations are unabashedly modeled after Southwest, the pioneer of this strategy and keeper of the healthiest balance sheet in the industry.²

The reasons for this competition were easy to understand. Over 45 percent of United’s revenues came from passengers who flew through its California hubs. As a market, the California corridor was the most heavily traveled in the United States, which had 80 percent more traffic than the Boston-New York-Washington corridor. Yet United’s share in this market had fallen from 38 percent in 1991 to 30 percent in 1993.

During the same period, Southwest’s share had increased from 26 percent to 45 percent. Other airlines, like Continental, had also been hurt by Southwest’s competition. Southwest’s success

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spawned a number of imitators, including new airlines like Kiwi and Reno Air as well as major airlines like United and Continental. Concerned with this new competition, the market had driven down Southwest’s stock price and analysts were raising questions about how sustainable Southwest’s advantage really was.

Rhoades, a former marketing executive with an MBA from the University of New Mexico and a background in banking, had joined Southwest in 1989 to help transform the People Department (Human Resources in most organizations). Southwest had always believed that an important part of its competitive advantage rested with its people and how they were managed. Ann’s job was to help leverage this advantage. At tomorrow’s meeting she would be asked to review Southwest’s current position in light of the new competition. She had prepared a brief overview of what she saw as the major threats and opportunities of the competition and an assessment of Southwest’s strengths and weaknesses in light of these changes. However, she wanted to reflect one last time on these issues to be sure she was not missing anything. Her major concerns were whether Southwest was getting the most in competitive advantage from its own people, and whether the competition could imitate Southwest’s successful human resource practices.

BACKGROUND

On June 18, 1971, Southwest Airlines, headquartered at Love Field in Dallas, began flying with three Boeing 737 aircraft serving the Texas cities of Dallas, Houston, and San Antonio. Southwest’s competition was Texas International and Braniff, and, to a lesser extent, Continental. Continental used every political and regulatory means to ensure that Southwest would not get off the ground, including keeping Southwest out of the recently built Dallas-Fort Worth airport and waging a four-year legal battle that left Southwest almost bankrupt at the time of its first flight. One outcome of the legal battle was the so-called Wright Amendment, named after James Wright, then Speaker of the U.S. House of Representatives. The Wright Amendment prohibited any air carrier from offering direct service into Love Field from any place beyond Texas and the four contiguous states of Oklahoma, Louisiana, Arkansas, and New Mexico. This law meant that passengers flying into Southwest’s central location at Love Field from destinations beyond these four states would have to purchase separate tickets for each leg of the trip and could not check baggage through to their final destination. Furthermore, neither airlines nor travel agents were permitted to advertise connections through Love Field. Ostensibly, this law was intended to encourage traffic through the new Dallas-Fort Worth hub. In fact, it was aimed at stopping Southwest.

Herb Kelleher, CEO and one of the airline’s founders, and Southwest’s corporate counsel at the time said, “You know, anger can be a great motivator. For me, this became a cause. I was a crusader freeing Jerusalem from the Saracens.”3 More recently, he was quoted as saying, “I have told people that I would retaliate if I became very angry, but now I think I would revise that. Let’s just say that if I become peckish, I will attack.” 4 This aggressive, underdog spirit still pervades the company, especially among longer serving employees. Many see the goal of keeping this spirit alive as one of the firm’s great challenges. Delise Zachry, an instructor from

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the People Training Department, noted, “In 1971, 198 people got together and did something that was impossible. Now we need to update the culture to today’s problems.”

In the early days, Southwest gained attention by putting its flight attendants in hot pants and using its location at Love Field to launch an advertising campaign (“Make Love, Not War”), a theme that is still used today when Southwest refers to itself as the “Love” (LUV) airline. This designator is Southwest’s stock ticker symbol. All Southwest aircraft have a small heart emblazoned on their sides and hearts are used prominently on corporate communications and advertising. From its inception, Southwest has encouraged its employees to identify with others at the company, deliver great customer service, and have fun. They have also pursued a low fare strategy.

In the mid-1980s USAir and American, attempting to increase their share of the valuable California market, purchased Air California and Pacific Southwest Airlines (PSA), two successful regional carriers. However, American soon withdrew from some cities and routes when they could not be served profitably. USAir made a number of marketing and service mistakes and also cut back service in the region. Southwest seized the opportunity to expand in California. From a zero market share in California in 1989, Southwest became the leading airline in passenger boardings in 1993 and by 1995 it served 10 cities in the state with more than a 70 percent average market share for city pairs served.

THE CURRENT SITUATION (1995)

From the beginning, Southwest has maintained the same strategy and operating style that it maintains to the present. It concentrates on flying to airports that are underutilized and close to a metropolitan area—e.g., Love Field in Dallas, Hobby in Houston, San Jose and Oakland in the Bay Area, Midway in Chicago—although it does fly to major airports like LAX and SFO. The company also began flying fuel-efficient 737s, and now has over 200 of them, the only type of aircraft it flies. Southwest service involves frequent on-time departures as well as low cost fares. It emphasizes point-to-point routes, with no central hub and an average flight time of 65 minutes. According to its 1993 annual report, 80 percent of its customers fly non-stop to their final destination. By avoiding a hub and spoke system, Southwest is able to avoid the delays often associated with connecting flights. This makes short-haul trips more attractive to travelers who might otherwise consider driving. It also pays off in shorter turnaround times (70 percent of its flights had a 15 minute ground time in 1991) and higher equipment use. For example, Southwest aircraft spent an average of 11 hours in the air daily compared to an industry average of 8, and it averaged 10.5 flights per gate versus 4.5 for the industry.

Following this strategy, Southwest has always seen itself as competing not so much with other airlines as with surface transportation. For instance, in 1993 the average passenger fare was roughly $60 for a trip of 500 miles. In 1984 the comparable numbers were $49 and 436 miles. In August 1994, the roundtrip fare from Oakland to San Diego, a distance of over 1,000 miles, was $135. Southwest uses these low fares and frequent flights to increase passenger volume two to three times. For example, approximately 8,000 people used to fly between Louisville and Chicago weekly. After Southwest entered the market, that number climbed to 26,000. Southwest dramatically lowered the fares and increased the frequency of flights. In August 1994, it flew 39
times roundtrip daily between Dallas and Houston, 25 times between Phoenix and Los Angeles, and 20 times between Sacramento and Los Angeles. When American moved out its San Jose hub because it was losing money, Southwest moved in and was profitable from the first day of service. In 1992, Southwest was the leading carrier in passenger boardings in 27 of the 34 airports served. In 1994, it dominated most of its major markets, with almost 70 percent of the intra-Texas and over 50 percent of the intra-California markets.

Consistent with its strategy of low costs, low fares, and frequent flights, Southwest also keeps its fares simple. Unlike other airlines that rely heavily on computers and artificial intelligence to maximize flight revenue, Southwest typically offers only two fares on a route, a regular coach fare (there is no first- or business-class) and an off-peak fare. It also tries to price all fares the same within a state (for instance, currently $69 to fly anywhere within California). Southwest has never sold interline connections to other carriers and has been unwilling to pay to be part of other airlines' reservations systems. As a result, only 55 percent of Southwest’s seats were booked by travel agents compared to 90 percent of tickets for major airlines. In 1994, United announced that its Apollo System would no longer carry Southwest’s schedules or issue its tickets. This makes issuing tickets more difficult for travel agents who often have to call the airline rather than work through a computer as they do with other airlines—a clear incentive to travel agents not to book Southwest flights.

To further simplify its operations, Southwest has never offered meal service on its flights. Meals can add $40 per passenger to the cost of a flight. Instead, passengers on Southwest are served beverages, peanuts (referred to as “frill”), and on longer flights, crackers or other light snacks such as cookies. There is no assigned seating. Upon arrival at a Southwest gate, each passenger holding a reservation is given a reusable plastic boarding pass with numbers from 1 to 137, the maximum load of their 737 aircraft. Passengers are loaded in groups of 30 and the boarding passes are collected for use on the next flight. Standby passengers are boarded if seats are available in the order in which they sign up at the departure gate.

Although it is not connected to other airlines’ reservation systems or affiliated with other frequent flyer programs, Southwest does have its own frequent flyer club (“The Company Club”), also a model of simplicity. It is based on the number of trips flown, not the mileage. Members keep a card that is stamped every time a plane is boarded. After accumulating 16 segments, a free ticket is awarded and a Company Club card is issued. The card is then read into the computer system for each trip. This approach economizes on operating costs since it requires no effort to keep track of mileage. Based on some negative advertising by United about Southwest’s frequent flyer program, Herb Kelleher recently sent a letter to all Company Club members detailing how awards from Southwest took less mileage to obtain and were more widely available than other airlines. Kelleher argues that Southwest’s program “is the greatest value because it gives you free travel faster, for much less money, without giving up great service.” For instance, after 50 roundtrips within a 12-month period, a companion flies free with a Company Club member, even if the person is traveling on an award ticket.

Overall, Southwest Airlines has been profitable in every one of the last 21 years, a record achieved by no other major U.S. airline. It was consistently profitable even during the 1991–1992 period, during which some 40 percent of the total capacity of the U.S. airline industry was...
seeking bankruptcy protection or ceased operation completely. (Exhibit I presents selected financial and operating data from 1984 to 1993.) According to Money magazine, for the 20-year period 1972–1992, Southwest’s stock earned the highest returns of any publicly traded U.S. stock—compounded return of over 21,000 percent. Only Wal-Mart came close to being as good an investment over this period.

COMPETITIVE ADVANTAGE

Although the reasons for Southwest’s success were many, one highly visible advantage could be seen in the company’s cost structure. Kelleher recognized that short-haul flying was inherently more costly than longer flights (the plane is taking off and landing more often and has to be handled at every gate). He understood that the lowest-cost provider could leverage that cost advantage most where costs are highest. (Exhibit 2 shows the costs per available seat mile for two comparable quarters in 1993 and 1994.) Southwest’s costs averaged roughly 7.1 cents, while the larger airlines had costs up to 10 cents or more per mile—20 to 30 percent higher. This achievement is even more striking when noting that Southwest’s costs in 1984 were 5.86 cents. So, over a decade its costs had increased by only about 20 percent.

Part of this cost advantage derives from the remarkable productivity Southwest gets from its work force. For example, they routinely turn around an aircraft in 15 minutes from the time it arrives at the gate (see Exhibit 3 for the anatomy of a 15 minute turnaround). United and Continental average 35 minutes. Southwest’s gates are typically manned by a single agent and have a ground crew of six or fewer, rather than the three agents and twelve ground crew that are common at other airlines.

These low costs also come from other sources. Southwest pilots, for example, spend more time in the air than pilots at other airlines. While pilots at United, American, and Delta earn up to $200,000 a year for flying an average of 50 hours a month, Southwest’s pilots average $100,000 a year flying 70 hours a month. Flight attendants and pilots help clean the aircraft or check passengers in at the gate. Harold Sirkin, airline specialist with BCG said, “Southwest works because people pull together to do what they need to get a plane turned around. That is a part of the Southwest culture. And if it means the pilots need to load bags, they’ll do it.”

Southwest’s employees also routinely volunteer to help customers in need. Once a customer arrived at the airport for a vacation trip with his dog in tow, only to learn that he couldn’t bring the dog with him. Rather than have him cancel the trip, the gate agent took care of the dog for two weeks so the fellow could enjoy his holiday. Another employee accompanied an elderly passenger to the next stop to insure that she was able to change planes. Stories of this sort abound.

These efforts pay off in employee productivity. In 1993, for example, Southwest had an average of 81 employees per aircraft while United and American had 157 and 152, respectively. The industry average was in excess of 130. Southwest served an average of 2,443 passengers per employee while United and American served 795 and 840, about the industry average. This

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means that Southwest needs a smaller load factor to break even than the other carriers (usually around 55 percent). Second, the point-to-point strategy and the use of less congested airports improve the efficiency of flight operations and helps insure high levels of aircraft utilization. Finally, by using a single type of aircraft, Southwest was able to save on maintenance and training costs.

But Southwest is not just a low fare/low cost carrier. It also emphasizes customer service. In fact, the word “Customer” is always capitalized in all Southwest corporate communications, whether it is the annual report or an internal newsletter. Colleen Barrett, executive vice president of customers and highest-ranking woman executive in the airline industry, insists on this. She is also adamant about treating employees as internal customers and tries to make sure that Southwest is a comfortable and fun place to work. “If you’re comfortable, you’re smiling more and you give better service,” Barrett says. “It doesn’t take a rocket scientist to figure that out.”

The results are undeniable. In the airline industry, service is measured by on-time performance, having the fewest lost bags, and having the fewest number of customer complaints. If an airline is the best in all three categories in a single month, it wins the so-called “Triple Crown.” Southwest has won the monthly Triple Crown 24 times. In 1992, the Department of Transportation began giving an annual Triple Crown award. Southwest won the award in 1992, 1993, and 1994.

**Leadership at Southwest**

While a number of industry experts attribute Southwest’s accomplishments to its unwavering adherence to its low-cost niche strategy, others disagreed and argued that its real competitive advantage lay in its leadership. A recent *Fortune* article, for instance, was titled “Is Herb Kelleher America’s Best CEO?” The piece cites a U.S. Department of Transportation report that Southwest was the “principal driving force for changes occurring in the airline industry,” and credits Kelleher with much of this. The author quotes Michael Derchin, a veteran airline analyst who has been monitoring Southwest almost from its beginning, who said, “I think Herb is brilliant, charming, cunning, and tough. He is the sort of manager who will stay out with a mechanic in some bar until four o’clock in the morning to find out what is going on. And then he will fix whatever is wrong.” In his view, the difference between Southwest and other carriers is “in the effort Herb gets out of the people who work for him.” The *Fortune* writer, Ken Labich, concluded his article by noting, “The greatest obstacle to long-term prosperity at Southwest may be Kelleher’s mortality.”

Although Southwest is headquartered in Dallas, Herb Kelleher isn’t a native Texan. He is not a pilot either. He’s a lawyer who grew up on the East Coast, majored in philosophy and literature, graduated from NYU Law School, clerked for a New Jersey Supreme Court justice, and practiced law in Newark, New Jersey. After visiting his wife’s parents in San Antonio, he announced that he wanted to move to Texas. By the mid-1960s he was happily practicing law in San Antonio. One day in 1966, a client named Rollin King described his experience in California

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7 Labich, “Is Herb Kelleher America’s Best CEO?”
on PSA, a short-haul commuter airline, and suggested that Texas could benefit from a similar operation. The two sketched out some plans, borrowed money, and started Southwest.

From the beginning, Kelleher has adopted a visible, hands on, slightly over-the-top style—always ready to promote a party and have fun. He appeared one Halloween at a Southwest maintenance hanger dressed in drag with a feathered boa imitating Corporal Klinger from the television program, M*A*S*H. He’s also appeared in print advertisements and at company parties dressed as Elvis Presley. (Ann Rhoades suggested that this was fine, but they try not to encourage him to dress like Ethel Merman.) He’s renowned for his love of Wild Turkey bourbon. When Herb met the president of the company that produces it, he told him that he may be just a man to most people, “but to me you are a god.”8 While recovering from minor surgery, he received over 3,000 cards and gifts from employees, including an intravenous drip set-up—but with Wild Turkey rather than saline solution. He also smokes five packs of cigarettes a day. He said, “I’ve always felt that there’s no reason that work has to be suffused with seriousness, that professionalism can’t be worn lightly. Fun is a stimulant to people. They enjoy their work more and work more productively.” He believes that “you don’t have to surrender your individuality to work for Southwest Airlines.” This is seen in the phrase sometimes heard at Southwest, “work is important ... don’t spoil it with seriousness.”9

And Kelleher does have fun. He constantly interacts with customers and Southwest employees. He routinely visits maintenance facilities in the early morning hours. Tom Burnett, the Teamster leader who represents Southwest mechanics and cleaners, said, “Let me put it this way. How many CEOs do you know who come into a cleaners’ break room at 3 a.m. on a Sunday passing out doughnuts or putting on a pair of overalls to clean a plane?”10 Once while rushing to catch a flight at Love Field he stopped his car in the loading zone and began talking with a Southwest employee. After an animated few minutes, he realized he was late and rushed off to make his plane. When he arrived in Houston, a Southwest employee asked him if he knew where his car was? He’d left it idling at curbside. Kelleher has also appeared in television ads for American Express—not because he’s such a big user, but because he has lost more cards during a year than any other AMEX customer. Colleen Barrett is always sticking money in his pockets since he routinely forgets his wallet. Reflecting on Herb’s propensity to engage people in conversation, she says, “I could add four hours to Herb’s day if I could get him to walk and talk at the same time.” One friend says, “There is an unwritten rule that, if you don’t want to stay up all night drinking and talking, then you stay the hell away from Herb.”11

This philosophy pervades the entire company. Serious attention is paid to parties and celebrations. Every year, for instance, each station (city) is given a budget for parties for the employees and their families. Most stations supplement this by doing their own fund raising. Up until several years ago, all Southwest employees used to fly to Dallas for the annual company party. Now that the company has grown too large for that, they hold a rolling party in several cities with Herb and the senior managers moving from one location to another. Celebrations and

8 Labich, “Is Herb Kelleher America’s Best CEO?”
11 Labich, “Is Herb Kelleher America’s Best CEO?”
contests occur continually, including chili cook-offs and Christmas parties. The Love Field corporate headquarters in Dallas is filled with pictures of Southwest employees at parties, awards, trips, celebrations, and banners. In fact, there is no corporate art in the headquarters. All paintings and sculptures, and there are many, are those donated by employees.

Barrett also reflects the relaxed management style. Officially, she is responsible for communication, marketing, public relations, people (human resources), governmental affairs, and scheduling (see Exhibit 4 for an organization chart). She is also heading the merger efforts with Southwest’s recent acquisition of Morris Air. Unofficially, she has been described as a combination of den mother, management guru, and customer ombudsman. She is a stickler for detail and provides the organizational counterweight to Kelleher’s sometime chaotic style. “She’s the backbone of the airline,” said one employee. Barrett claims that “The company is only as good as its people,” and constantly reinforces that theme. “We’ll never jump on an employee for leaning too far toward the customer, but we come down on them hard for not using common sense.”

For instance, about four years ago she became concerned with the size and geographic dispersion of the company and set up a culture committee consisting of 65 people from all levels and regions of the company. This committee meets with Barrett four times a year for a full day to preserve and enhance the Southwest spirit. After determining that some distant locations were operating functionally but without the teamwork that Southwest values, they decided to try to reduce this tendency. One outcome was a systematic effort for groups of employees to express their appreciation to others for their contributions. So, for instance, the pilots held a barbecue for the mechanics on the flight line at 3:00 a.m. Other groups, including pilots, decided to thank the reservations agents by coming in and spending a shift with them. Even the officers and directors of the company have a program, called “Day in the Field,” that requires them to spend one day per quarter working in a front line job. Barrett is adamant that this means really work, not stand around and drink coffee.

The People Department

About five years ago the human resources function at Southwest was renamed “The People Department.” This reflected a concern that the old human resources group was, in the words of John Turnipseed, manager of people services, “a police department.” To counteract this, Ann Rhoades first threw away the 300 page corporate handbook and brought in new people with marketing backgrounds. Currently, to join the department an employee must first have line experience. She sees the role of the People Department as saying “yes” rather than “no” and wants them to “do what it takes to make the Customer happy.” Employees are the customers of her group. Although they deal with approximately 18,000 employees, the People Department has a staff of about 100. All members of the department sign the department’s mission statement, which is prominently displayed in a very large poster on the wall of their headquarters’ office. It reads:

Recognizing that our people are the competitive advantage, we deliver the resources and services to prepare our people to be winners, to support the growth
and profitability of the company, while preserving the values and special culture of Southwest Airlines.

Ann takes this charge seriously and believes in what she calls the two Cs: compassion and common sense. She worries about maintaining the culture and tells people to break the rules if they need to. While in many companies human resources is considered a backwater, the People Department at Southwest is “like the keeper of the flame,” says Treasurer John Owen. Ann notes that, “Most HR people have no courage. They never take a chance. No guts. No capability of making a decision. They’re so afraid of being fired... We need to have confidence in people doing the right thing.” To do this, she believes that it is imperative that you get the right people into HR to begin with. This also underlies the Southwest policy of hiring and firing for attitude. Her department is also continually feeding back information to employees such as on-time performance, turnaround times, number of customers boarded or the cost of a day’s health care for the airline in terms of the number of bags of peanuts served on their flights. The intent is to keep people focused and make them aware of how their actions affect costs.

Recruiting

To insure that it gets the right people, Southwest is extraordinarily selective in its recruiting. In 1993, it had 98,000 job applicants. Of these, roughly 16,000 were interviewed, and 2,700 hired—including one aspiring employee who submitted her resume on the icing of a large sheet cake, demonstrating the creative spirit that Southwest looks for. To insure fit, there is an emphasis on peer recruiting. For example, pilots hire other pilots, often coming in on their day off to do background checks. As Ann noted, “They can get far more information in a phone call to the chief pilot of another airline than anyone else.” They even turned down a top pilot who worked for another major airline and did stunt work for movie studios. Even though he was a great pilot, he made the mistake of being rude to a Southwest receptionist. Teamwork is critical. As Ann noted, “If they say ‘I’ too much in the interview, they don’t get hired.” She described how one group of eight applicant pilots was being kidded about how seriously they were dressed (dark suits and black shoes and socks). They were encouraged to loosen up. Six of them accepted the invitation to wear the standard Southwest Bermuda shorts and interviewed for the rest of the day in suit coats, ties, Bermuda shorts and dress shoes and socks. They were the six hired.

To further screen for the Southwest Spirit, customers are sometimes involved in the interviewing for new flight attendants. The process consists of an application, a phone screening interview, a group interview, three additional interviews (two with line employees), and a consensus assessment and a vote. During the interview process, the applicant will come into contact with other Southwest employees. These people are also invited to give their assessments of whether the person would fit in at the company. The entire process focuses on a positive attitude and teamwork. For example, applicants are given crayons to draw a picture that tells the story of their life. Southwest looks for people who are willing to draw outside the lines. Even its advertisements emphasize the Southwest spirit. One ad for people with computer skills showed a picture of a techno-nerd, with tape holding his glasses together, and emphasized that "We're not

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looking for your average computer geek." Other ads convey a sense for the type of employee Southwest wants to attract (see Exhibit 5 for several illustrations).

As befits a company in which selection is important, Southwest has spent a lot of time identifying the key components that comprise effective performance and behavior. For instance, the People Department identified its top 35 pilots and systematically interviewed them to identify common characteristics. One key trait identified was the ability to work as a part of the team. This is now used as a part of their pilot selection process. The company believes that most skills can be learned and doesn’t screen heavily for these except for certain specialist jobs, like pilots and mechanics. Attitudes are what count. Kelleher says, “We draft great attitudes. If you don’t have a good attitude, we don’t want you, no matter how skilled you are. We can change skill levels through training. We can’t change attitude.”

For example, John Turnipseed described an EEO complaint for not hiring a person for a position who had 15 years of experience while selecting a person who had no experience. Southwest successfully made the case that the culture was critical and had to be considered in selection.

An important awareness on the part of the People Department is that the company rejects more than 95,000 applicants each year. These are all potential customers. Therefore, the recruiting process is designed to not make applicants feel inferior or rejected. Ann claims that some people have told her they had a better experience being rejected by Southwest than they did being hired by other companies. Rita Bailey, a corporate employment manager, always tries to call any internal or managerial applicants that are turned down. She uses this as a chance to counsel them, trying to be honest but not damaging their self-esteem. She invites them to call again if they want to talk more. She is concerned not only how well a person will do at the job they are applying for, but also how they’ll do in the next job. She says, “It’s important to do it this way or you're setting people up to fail when they get promoted.”

The company hires very few people with MBAs, and even those that do get hired are selected for their fit, not for their credentials. In fact, they prefer people without extensive industry experience. For example, 40 percent of their pilots come directly from the military, 20 to 30 percent from small commuter airlines, and the rest from the major airlines. To encourage employees to help in the recruitment effort, Southwest offers a free space-available pass (which permits a person to travel free when the plane isn’t full) to any employee who recommends someone who is hired to fill a position that is difficult to fill, such as in finance or information systems. Southwest doesn’t have a nepotism policy (except for officers) and has 481 couples that work for the company. When these people describe the firm as “family,” a common reference throughout the airline, they really mean it.

**Training**

Given the emphasis on selecting for attitudes and fit and the importance of culture, it follows that training is an important part of Southwest. In 1993 alone, 6,500 employees went through Southwest’s University for People. Headed by Liz Simmons and run with a staff of eight, the training group offers a variety of courses ranging from the “New Hire Celebration” (it’s not

called orientation) designed to get new employees enthused and excited, to senior management courses. Delise Zachry believes that “Our level of external service is only as good as our internal service.” She worries that the success of the company may induce a sense of complacency and noted that all the positive press accounts don’t help.

New flight attendants go through four weeks of classes, typically with less than 5 percent attrition. Much of this training is oriented towards customer service—“the care and feeding of customers.” Customer expectations about service are quite high, and these are communicated to both new and experienced employees. All new hires are exposed to the history, principles, values, mission, and culture of the company. They are also told how the company views leadership and management. In all training, there is an emphasis on teamwork and team building, all in good humor. For instance, new hires often do a celebratory skit at the conclusion of their training. One new pilot class donned dark sunglasses and white canes and stumbled into Kelleher’s office.

For managers, there is a three and a half day course on leadership, pricing, revenue management, and on how the business works. A member of senior management always attends a two-hour session and talks openly with the participants. Training is virtually 100 percent internal. “If it ain’t born and bred here, they don’t want any part of it,” said Zachary. Front-line leadership gets a specially designed two-day course each year. These programs are designed to address particular needs, like cross-functional teamwork, and are heavily experiential. They involve managers from different levels and different parts of the organization, but never have a superior and a subordinate in the same session. Each year as the new program begins, the senior team is always the first to go through it. In addition to this special program, supervisors receive 80 hours of training per year. Courses includes the usual offerings of communication, time management, and career planning, as well as others emphasizing the employee’s role in creating legendary customer service and more interpersonal explorations around accepting responsibility and developing trust.

For the past 18 months, training has offered a course called “The Climb,” a two and a half day ropes and outward bound course. This course is open to the entire company, but is attended by intact work teams. Zachary noted that it’s hard to get people to change in their normal work setting. To generate the emotional contact necessary to foster change, the entire team lives for the time together, completely cut-off from phones, cars, and contact with other outside issues. At the end of the program, each team develops an action plan to insure that their new behaviors are transferred to the work setting. The senior executive team attended this course during 1994.

The other highlighted training is “The Front-Line Forum,” in which 12 to 15 individuals with 10 to 15 years experience in the company are brought together to discuss how the company is doing and how it has changed. They meet with top nine officers and explore questions like, “We promised you something around the culture and spirit of the company. Have we delivered?” Although the selection is done randomly, the idea is to assemble some people in the group who may be a bit beaten down to see what needs to be done to keep the culture alive.

Southwest does not have any tuition reimbursement program for taking outside courses. It also tends not to sponsor people to attend outside training.
Overall, it is clear that training is an important form of two-way communication. Not only are the values of hard work, fun, and cost consciousness inculcated, but the training is also used to get internal customer feedback. For Zachary the issue is “To figure out how we can get better everyday, not worry about American Airlines or Delta.”

The Southwest Work Force

The company is 89 percent unionized with nine separate unions, but has had only one six-day walkout by the machinists over a decade ago. Mike Levine, former dean of Yale’s School of Organization and Management and current vice president for marketing at Northwest Airlines notes that “Herb really is an extremely gifted labor-relations talent, especially when you consider he has somehow managed to get union people to identify personally with this company.”

Obviously, those covered by a contract are paid on the basis of seniority. Kelleher insists that there be few work rules in union contracts. Exhibit 6 displays rates of progression over time for a number of different job classifications. These data are from recent contracts and illustrate the general relationship between pay and seniority for those covered by collective bargaining agreements. Part of this includes a system whereby employees can bid for shift and work hours. In almost every job class there are people earning between $40,000 and $60,000 a year. Everyone receives a raise on the anniversary of his or her employment. Libby Sartain, director of benefits and compensation, notes, “There’s no miracle compensation program here. The story is low pay at the beginning and high pay after you get seniority.” Below market wages are offered to clericals and management positions. Most people take a salary cut to join Southwest. One former manager at EDS who left to join Southwest was offered two and a half times his starting salary to stay with EDS.

The only big difference is that at Southwest pilots and flight attendants are paid by the trip. As Kelleher says, “Those airplanes aren’t making any money while they’re sitting on the ground.”

While comparisons are a bit tricky, Fortune reported that for 1992 the average wage at Southwest was $44,305 compared to $45,801 at American and $54,380 at United. Derek Deck of the Air Conference (a trade group that gathers comparable wage data across airlines) believes that Southwest employees may earn less per hour than at other airlines, although they do have the flexibility to work more hours and earn more. Controlling for seniority, he estimates that a flight attendant at Southwest would earn about $18 an hour, compared to $20 an hour at Continental and $23 at USAir. Deck also believes that Southwest personnel can, and often do, fly more trips, giving them 10 to 15 hours more per month.

Executive compensation is modest by some firm’s standards. In 1992, Kelleher earned a salary of $393,042 and a bonus of $120,000. In 1994, he was named one of the five lowest-paid CEOs in Dallas, and the lowest-paid on a performance-adjusted basis, an award he is particularly proud of. He does hold stock worth around $90 million, a paltry sum besides the likes of Larry Ellison at Oracle or Bill Gates at Microsoft. In fact, there was no executive stock option plan until a few

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14 Labich, “Is Herb Kelleher America’s Best CEO?”
15 O’Brien, “Southwest Airlines is a Rare Carrier.”
years ago. There are no country club memberships, no company cars, and officers stay in the same hotels as the flight crews.

However, profit sharing covers all employees who have been with the firm for over a year, and they are required to invest 25 percent of their profit sharing money in Southwest stock in a retirement account. In 1993, those eligible received 8 percent of their salary as a bonus. Employees can also take advantage of a discounted stock purchase program. This has produced several millionaires.

Approximately 80 to 90 percent of the employees own stock in the company, and about 11 percent of Southwest’s outstanding shares are owned by employees. However, Libby Sartain notes that she tries to encourage employees to diversify and not hold too much of the company's stock.

Because of its conservative hiring policies and growth, Southwest has a young work force; the average age is 34. Twenty three percent of the employees are minorities, with 10 to 12 percent at the managerial level. Women are widely represented also at the highest levels of the company. John Turnipseed described how when an EBO audit team arrived in Dallas, he simply gave them an office and pointed out where the files were. In most companies, auditors have to request specific documents, which are then retrieved and brought to the auditors. He acknowledged that they weren’t perfect, but intended to correct any problems. He described how apologetic the auditors were at having to write up several violations.

As might be expected, turnover is low, running 4.5 percent in 1991, less than half that of other major airlines. The company has never had a furlough or layoff. Because of limitations in its labor contracts, it uses few temporary or part-time employees. Southwest does have a pool of ex-employees (e.g., retirees, people who want to stay at home) that it can call on in case of emergencies. All temporary workers are paid benefits on a pro-rata basis. There is little cross training although the company encourages “days in the field” so employees can try front-line jobs. Only in the marketing and reservations departments are there formal teams. The culture, however, promotes informal teamwork and employees routinely help each other out.

The Southwest Spirit

Southwest tries hard to manage and maintain its culture. Wander around the halls at the Dallas headquarters and you will hear several themes over and over: customer service, hard work, equality, cost consciousness, dedication, fun, and, most frequently of all, family. Of course, this invites the cynic in all of us. One employee who had worked at several other large companies said, “I was pretty dubious at first, having been at places where everyone but the top two or three people were considered commodities. Put I have come to appreciate a place where kindness and the human spirit are nurtured.” In addition to the efforts of Colleen Barrett and the culture committee (and its 35 local subcommittees), there are continual efforts to preserve the values that brought Southwest to its current position. John Turnipseed says that trust is built by constantly sharing information. “The level of trust has never been broken. In many

16 Labich, “Is Herb Kelleher America’s Best CEO?”
organizations, everybody’s against someone-union versus management, head office versus the field, etc. Not here.”

The family spirit can be seen in many ways. For instance, there is the catastrophe fund, which in the last two years raised $500,000 in voluntary contributions for distribution to other Southwest employees who needed help. During the last oil crisis, unbeknownst to management the employees raised $130,000 to help defray fuel costs. When a former employee developed a drug problem, the company arranged to pay for his medical care so long as he stayed in the rehabilitation program.

Kelleher and his management team seem acutely aware of the potential problems as they continue to grow. He says, “The bigger we get, the smaller I want our employees to think and act.” Ann Rhoades said, “You have to work at the culture. It doesn't just happen.” Rita Bailey described how there is plenty of peer pressure “not to ‘bad mouth’ the family. Employees don’t put up with a lot of complaining.” Colleen Barrett described how when she talks to people, they are always skeptical and want to know the “real” story. She says, “There are no deep, dark secrets here. It’s so simple. It’s a cult. It’s a religion with us.” Kelleher echoes this view when describing the spirit of Southwest employees. “The people who work here don’t think of Southwest as a business. They think of it as a crusade.” This doesn't mean that people are unrealistic. A pilot indicated, “It’s not a Mary Kay-type atmosphere where we’re all starry-eyed. It’s mutual respect” A longtime observer of the airline industry said, “At other places, managers say that people are their most important resource, but nobody acts on it. At Southwest, they have never lost sight of the fact.”

**THE COMPETITIVE THREAT**

As she finished gathering up papers for tomorrow’s meeting, Ann Rhoades reflected on the airline industry in general and Southwest’s position in particular. The industry overall, with few exceptions, had been characterized by notoriously poor labor relations and authoritarian management. In 1983, Frank Lorenzo led Continental Airlines into bankruptcy so he could rid the airline of its union. Carl Icahn faced numerous strikes during the time he controlled Trans World Airlines, and hired replacement workers during some of them. Eastern Airlines ultimately failed because of the conflict between Lorenzo and the unions. Robert Crandall of American Airlines pioneered the two-tiered wage structure in which newly hired employees would be brought in at lower wages than the currently employed workers. During the 1993 Thanksgiving season, American Airline flight attendants struck in an attempt to roll back wages. In this light, Southwest’s policies stood out—labor peace, trust, non-adversarial relations, open sharing of information, and high productivity.

More recently, several other airlines were undergoing employee buyouts. By 1994, TWA was largely employee owned. Northwest narrowly avoided bankruptcy when its unions agreed to an eleventh-hour swap of wage concessions for an ownership stake. United has followed suit. USAir was offering stock and board seats in return for employee wage concessions. Continental

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Southwest Airlines (A) HR-1A

Airlines had also emerged from Chapter II with what the press claimed was a more employee-oriented management. Executives at Delta said they would announce their plans for a new low-fare strategy in the coming months. The pilots at American suggested a similar strategy to management.

But it wasn’t these general trends that concerned Rhodes as much as two direct threats. Both United and Continental had begun low cost airlines-within-an-airline to challenge Southwest directly. They were not only directly imitating the Southwest strategy, they were also using their policies and procedures. An old adage at Southwest was not to provoke their major competitors. Obviously, they had done more than provoke them; they had challenged them directly.

**Continental Lite**

Under the guidance of CEO Bob Ferguson, Continental Airlines emerged from its second bankruptcy in April 1993. In May, Ferguson announced his plan to split the company into two operations; one that would concentrate on short-haul, low fare flights (named Continental Lite or CALite), and the other that would feature first-class service at business class prices. He believed that because of its low cost structure, lower even than Southwest, Continental would be able to compete successfully. By imitating many of Southwest’s practices, including the use of humor by flight attendants, Ferguson believed that he could attract the business traveler. By concentrating primarily on the East Coast market, he could take advantage of greater density, shorter flights, and avoid competing directly with Southwest, at least in the short-term.

Continental Lite was rolled out in October, 1993, with 173 daily departures from 14 cities. By summer, it had expanded to 28 percent of Continental’s capacity, with plans to ultimately grow to 40 percent. Fares were cut dramatically. For example, the Newark-Greensboro went from $273 to $99 and the Greensboro-Greenville from $226 to $59. The early results, however, were mixed. CALite currently is flying with about 59 percent of its seats filled. Customer reaction is not always positive. Some frequent flyers were miffed that there was no priority boarding or meal service. Flight attendants were concerned about the increased workloads (like Southwest, they clean cabins between flight segments) and lack of breaks between flights. Ground crews were trying hard, but turnarounds were still taking over 30 minutes rather than the hoped for 20. Even the pilots were upset until the company began providing meals for them during their busy schedules. (In one instance, a flight was delayed while the pilots ate in the airport terminal.) In March 1994, Continental had the worst marks of any domestic airline in terms of customer complaints, on-time performance, and mishandled baggage.

Financial results were also not yet up to expectations. Continental lost $38.5 million on revenues of $3.9 billion from April 1993, when it emerged from bankruptcy protection, through the end of 1993. Management expected to break even in the second half of 1994 and did not see these results as a disaster. Chief Financial Officer Daniel Garton said that only 20 percent of CALite’s routes were losing money and noted that because USAir and Delta responded aggressively to Continental’s fare cuts, profits have been weaker than expected.19 Some airline industry observers believed that Continental’s costs may still be too high.

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This is also complicated because CALite still relied more heavily on one-stop and connecting passengers than did Southwest. The clear trend in the industry has also been for fewer business travelers. In 1982, over 50 percent of travelers paid full-economy fare or higher (e.g., business-class). In 1995, that figure was less than 40 percent. Gordon Bethune, Continental’s COO, said, “Up to a two-hour flight, it’s already a commodity business. A $10 difference will grab anybody’s passenger these days.”

Flights of up to two hours represent over 60 percent of domestic traffic.

Ferguson, whose style has been described as “harsh and uncommunicative,” was undeterred. A 1972 graduate of Lehigh University with a degree in finance, he began his career at Bankers Trust making loans to the airline industry. He left Banker’s to move to one of his clients, Braniff International, and subsequently left it to join Frank Lorenzo at Texas Air. While there, he helped Lorenzo buy People Express, a successful low-fare carrier in the early 1980s that failed in 1986 after over expanding. Ferguson was known to drive executives away. Since taking over in 1991, at least a dozen top managers have left. One commented on his management style by noting that, “It’s very pointed, even nasty. If he doesn’t like an idea, he seems to go out of his way to ridicule it.” Another said, “He can’t resist reverting to Lorenzo-style management.” Ferguson admitted to not suffering fools easily and said, “I will not tolerate not doing a good job. I will tell you in front of yourself, 20 people, or 100 people.”

A person familiar with his style claimed that, “Ferguson has to become more people-oriented and depend more on the recommendations of his management team.” He denied that he has people-skill problems and has plans to give as much as 4 percent of the stock to employees. He has also hired Donald Valentine as marketing chief for CALite; Valentine was previously head of marketing for Southwest. Ferguson conceded that CALite has had some start-up pains and hasn’t operated very efficiently so far but saw this as just the usual problems of changing the organization.

**United’s Shuttle**

On July 28, 1994, United announced what had been the year’s worst-kept secret: On October 1, it would begin its own airline-within-an-airline on the West Coast. The goal of this operation, named “The Shuttle,” was to cut costs by 30 percent on these routes and regain the market share that Southwest had captured. To do this, United aimed at reducing its costs per available seat mile to 7.4 cents. The Shuttle was scheduled to begin with 184 daily flights on 13 routes, expanding to almost 300 flights by year-end. United announced that it would match the going price on all routes on which it went head-to-head with Southwest. Service would include advance seat assignments, a first-class cabin, and United’s frequent flyer mileage program.

“People want to fly us because they can consolidate their frequent flier miles and get better service,” said United’s senior vice president for planning.

Kelleher referred to United’s announcement as a “declaration of war” and intimated that Southwest might begin flying other United routes to drain revenue. He also talked about raising

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22 Ibid.
fares on longer routes to generate revenue to lower the bar without hurting Southwest’s own profits. On August 30, Kelleher sent a memo entitled “Commencement of Hostilities” to all Southwest employees detailing Southwest’s response to United’s challenge. This memo concluded:

Southwest’s essential difference is not machines and “things.” Our essential difference is minds, hearts, spirits, and souls. Winston Churchill stated: ‘Success is never final.’ Indeed, success must be earned over and over again or it disappears. I am betting on your minds, your hearts, your souls, and your spirits to continue our success. Let’s win this one and make aviation history again!

The president of America West, a Phoenix-based low-fare airline that had been bloodied by Southwest, said, “Taking on Southwest head-to-head is unwise for anyone.”

On July 12, United had completed negotiations for an employee buyout. In return for 55 percent of the company, employees, excluding the 17,000 flight attendants who voted not to participate in or agree to work rule changes, promised $4.9 billion in wage cuts and productivity gains. As a part of this agreement, Steve Wolf, the former CFO, was required to step down and was replaced by a Chrysler executive, Gerald Greenwald, who had no previous airline industry experience, but who was reputed to be a good people-person. Wolf claimed that he left United in good financial shape with great success on its overseas’ routes and a fleet that was only nine years old on average. Wolf estimated that the $1 billion in losses in 1992 would have been a $700 million profit if United hadn’t been competing with Southwest. “We just need to come up with a strategy that will offset their competitive advantage,” he said.

Unfortunately, not everyone is sure that The Shuttle can succeed. The culture at United is almost the opposite that of Southwest. One pilot claimed, “We live by the letter of the law, in every way.” Another noted that, “Mechanics and pilots have always had a rift between them... That’s a conflict as old as aviation history.” Another worried, “As for management, I don’t know if they can change their culture. There’s a lot of dinosaurs over there at headquarters. There are a lot of power struggles over there, and they worry more about those than they do running the airline.” One cynic claimed, “Most of the expansion we’ve done over the past few years a blind man could have accomplished. I wouldn’t really credit Steve Wolf with any of that.” These sentiments were not restricted solely to the pilots. Based on interviews around the airline, Ken Labich at Fortune reported mixed opinions about the future among United employees.

“You’ve also got to hope that the way we do things will change. [United] is the kind of place where management usually thinks they are way up there, and the rest of us are way down here. They want to make sure the shareholders get what they want, but they don’t care much about the employees. All that’s got to change.”

—Mechanic

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24 Ibid.
26 Ibid.
‘I’m afraid a lot of people are still looking at the situation as us versus them—management versus labor, union versus non-union; there are clearly union people out there who are saying, ‘Wait till we take over.’ I don’t know how we will ever get out of that.”
—Planner

“We’ve always been treated like angry children who don’t deserve what they get. Upper management has been adversarial and confrontational with us for over 10 years now; I don’t think Mr. Wolf liked the flight attendants at all. We are managed differently from the other groups. We’re disciplined if we’re sick more than 3 days per month or if we arrive late for a flight... We’re the only group that has to hop on a scale every month. Pilots certainly aren’t held to those standards. When it comes to the boys in the cockpit, things are different. The pilots stay in downtown hotels, and we’re stuck out at the airport. When we have to deadhead, they fly in first class and we’re in the back of the plane. That says it all... The irony, of course, is that the bosses ought to think a lot harder about how we feel if they want to keep their customers happy. We’re the people who spend all the time with the passengers. To the public, we are United.”
—Flight Attendant and Union Representative

“People think a reservation job is easy, but it’s actually very difficult. Customers aren’t nice on the phones any longer, like they were when I came here 15 years ago... they’re rude to us. Then we get so busy, with so many calls on hold, that we can’t spend time with people and provide the good service.”
—Reservation Agent

“I’d say there has been an intense lack of trust toward management among the people I work with. We feel that they haven’t been dealing straight with us for a long time. They wanted to satisfy shareholders and if people lost their jobs—well, that’s business these days... There’s been turmoil since 1985, when people on Wall Street started looking at us like we were some cash cow they could milk.”
—Ramp Agent

Although the head of the new airline had not yet been announced, the betting was on Alan “Sky” Magary. Magary, a veteran with 24 years in the industry, was an innovator, credited with ideas such as footrests and smoke-free flights. A former Northwest executive described how when Magary was there, he came up with the idea of using patterned fabrics for the seats to disguise coffee stains. Magary had spoken publicly about the potential for The Shuttle and United’s plans to reduce costs to 7.4 cents a seat mile. There was some skepticism about this goal among industry analysts, one of whom commented that, “Only a deranged MBA could have thought this up.”

The Off-Site Meeting

As Ann Rhoades pondered the situation, she wondered if this competitive threat could seriously damage Southwest, and what actions, if any, Southwest’s senior management should take. Could United and Continental really imitate the Southwest approach? Of course, the threat was made more complicated because of the size and growth of Southwest. With 14,000 employees, it was no longer the small firm it had been. She worried that this could affect the family feeling. She also worried about the overconfidence Southwest’s success could breed. Kelleher had been quoted in a recent interview as saying, “We have to be the world’s first company to refute the

old law that companies die from excessive prosperity.**28 How could they avoid these attitudes? There was also the tricky problem of succession. Kelleher had been at the head of the company since 1963. How would the organization deal with this problem if it became necessary? It was clear to her that the success of the company really did rest with the human resources, and her job was to insure that these were managed effectively. But what should the management team be doing to deal with these problems? Well, she had seven hours before tomorrow’s 7 a.m. meeting to reflect on her options.

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28 Banks, “A Sixties Industry in a Nineties Economy.”
### Exhibit 1

**Ten Year Financial Summary, 1984–1993**

#### Selected Consolidated Financial Data

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<tr>
<td>Total operating revenues</td>
<td>$2,296,673</td>
<td>$1,802,979</td>
<td>$1,379,286</td>
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<td>Operating income</td>
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<td>Net income</td>
<td>$154,284</td>
<td>$97,385</td>
<td>$33,148</td>
<td>$50,505</td>
<td>$74,505</td>
<td>$57,952</td>
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<td>Net income per common and common equivalent share</td>
<td>$1.05</td>
<td>$0.68</td>
<td>$0.25</td>
<td>$0.39</td>
<td>$0.54</td>
<td>$0.41</td>
<td>$0.14</td>
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<td>$0.34</td>
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<td>Cash dividends per common share</td>
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<td>$0.03533</td>
<td>$0.0333</td>
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<td>Total assets</td>
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<td>Long-term debt</td>
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<td>$327,553</td>
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<td>$369,541</td>
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<td>$381,308</td>
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<td>Stockholders' equity</td>
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<td>$607,294</td>
<td>$617,434</td>
<td>$635,793</td>
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#### Consolidated Financial Ratios

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<td>Return on average total assets</td>
<td>6.2%</td>
<td>4.6%</td>
<td>2.0%</td>
<td>3.0%</td>
<td>5.5%</td>
<td>5.1%</td>
<td>1.9%</td>
<td>4.8%</td>
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<td>Return on average stockholders’ equity</td>
<td>16.0%</td>
<td>12.9%</td>
<td>5.3%</td>
<td>8.4%</td>
<td>12.9%</td>
<td>10.8%</td>
<td>4.0%</td>
<td>10.3%</td>
<td>11.4%</td>
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<td>Debt as a percentage of invested capital</td>
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<td>45.5%</td>
<td>49.3%</td>
<td>35.0%</td>
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<td>39.4%</td>
<td>32.8%</td>
<td>39.8%</td>
<td>45.0%</td>
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#### Consolidated Operating Statistics

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<tr>
<td>Revenue passengers carried</td>
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<td>27,839,284</td>
<td>22,669,942</td>
<td>19,830,941</td>
<td>17,958,263</td>
<td>14,876,582</td>
<td>13,503,242</td>
<td>13,637,515</td>
<td>12,651,239</td>
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<td>Load factor</td>
<td>68.4%</td>
<td>64.5%</td>
<td>61.1%</td>
<td>60.7%</td>
<td>62.7%</td>
<td>57.7%</td>
<td>58.4%</td>
<td>58.5%</td>
<td>60.4%</td>
<td>58.5%</td>
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<tr>
<td>Average length of passenger haul</td>
<td>495</td>
<td>498</td>
<td>502</td>
<td>517</td>
<td>516</td>
<td>577</td>
<td>542</td>
<td>472</td>
<td>436</td>
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<tr>
<td>Trips flown</td>
<td>546,297</td>
<td>438,184</td>
<td>382,752</td>
<td>338,108</td>
<td>304,673</td>
<td>274,859</td>
<td>270,559</td>
<td>262,082</td>
<td>230,227</td>
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<td>Average passenger fare</td>
<td>$59.97</td>
<td>$58.33</td>
<td>$55.93</td>
<td>$57.71</td>
<td>$54.21</td>
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<td>$55.66</td>
<td>$54.43</td>
<td>$51.91</td>
<td>$48.53</td>
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<td>Passenger revenue yield per RPM</td>
<td>11.77e</td>
<td>11.78e</td>
<td>11.22e</td>
<td>11.49e</td>
<td>10.49e</td>
<td>10.79e</td>
<td>9.65e</td>
<td>10.05e</td>
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<td>Operating revenue yield per ASM</td>
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<td>7.89e</td>
<td>7.10e</td>
<td>7.23e</td>
<td>6.86e</td>
<td>6.47e</td>
<td>5.84e</td>
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<td>Operating expenses per ASM</td>
<td>7.25e</td>
<td>7.03e</td>
<td>6.76e</td>
<td>6.73e</td>
<td>6.20e</td>
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<td>5.61e</td>
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<td>Fuel cost per gallon (average)</td>
<td>59.15e</td>
<td>60.82e</td>
<td>65.69e</td>
<td>77.89e</td>
<td>59.46e</td>
<td>51.37e</td>
<td>54.31e</td>
<td>51.42e</td>
<td>78.17e</td>
<td>82.44e</td>
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<tr>
<td>Number of employees at year end</td>
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<td>11,397</td>
<td>9,778</td>
<td>8,626</td>
<td>7,760</td>
<td>6,467</td>
<td>5,765</td>
<td>5,819</td>
<td>5,271</td>
<td>3,934</td>
</tr>
<tr>
<td>Size of fleet at year end</td>
<td>178</td>
<td>141</td>
<td>124</td>
<td>106</td>
<td>94</td>
<td>85</td>
<td>75</td>
<td>79</td>
<td>70</td>
<td>54</td>
</tr>
</tbody>
</table>
### Exhibit 2
Airline Costs per Available Seat Mile

<table>
<thead>
<tr>
<th>Airline</th>
<th>3rd Quarter 1993</th>
<th>3rd Quarter 1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Southwest</td>
<td>7.13</td>
<td>7.03</td>
</tr>
<tr>
<td>Continental</td>
<td>7.64</td>
<td>7.56</td>
</tr>
<tr>
<td>United</td>
<td>8.11</td>
<td>8.32</td>
</tr>
<tr>
<td>American</td>
<td>8.06</td>
<td>8.08</td>
</tr>
<tr>
<td>TWA</td>
<td>9.23</td>
<td>8.66</td>
</tr>
<tr>
<td>Delta</td>
<td>8.66</td>
<td>8.95</td>
</tr>
<tr>
<td>Northwest</td>
<td>9.36</td>
<td>9.79</td>
</tr>
<tr>
<td>USAir</td>
<td>10.94</td>
<td>10.74</td>
</tr>
</tbody>
</table>

Source: Company reports
Exhibit 3
Anatomy of a 15-minute Turnaround

7:55 Ground crew chat around gate position
8:03.30 Ground crew alerted and moved to positions
8:04 Plane begins to pull into gate; crew moves toward plane
8:04.30 Plane stops; jetway telescopes out; baggage door opens
8:06.30 Baggage unloaded; refueling and other servicing underway
8:07 Passengers off plane
8:08 Boarding complete; most of ground crew leave
8:15 Jetway retracts
8:15.30 Pushback from gate
8:18 Pushback tractor disengages; plane leaves for runway

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Exhibit 4
Southwest Airlines
Organization Chart

Chairman, Pres. & CEO
Herb Kelleher

Corporate Services
John Denison
Exec Vice President

- Finance
- General Counsel
- Reservations
- Revenue Mgmt
- Systems

Customers
Colleen Barrett
Exec Vice President

- Corporate Communications
- Customer Relations
- Executive Office
- Marketing
- People
- Public Relations
- Special Marketing

Internal Audit
Al Davis
Vice President

- Internal Audit
- Corporate Security

Operations
Gary Barron
Exec Vice President

- Flight Operations
- Fuel and Administrative Services
- Ground Operations and Provisions
- Maintenance and Engineering
- Schedule Planning
Exhibit 5
Southwest Recruiting Advertisement

WORK AT A PLACE WHERE WEARING PANTS IS OPTIONAL.

Not to mention high-heeled shoes, ties, and panty hose. Because at Southwest Airlines, we do things a little differently. And it's obvious just by looking at us. Especially when we don't wear pants on weekends. You'll see us in tailored walking shorts and golf shirts or colorful pullovers. Plus, the ever popular tennis shoes. Which not only makes Southwest Airlines people look a little more hip, but feel a lot more comfortable. And when we feel good, it's contagious.

We're always looking for people who take their jobs seriously. But not necessarily themselves. So if you're a bit of a ham and unusually allergic to stuffy uniforms, call our People Department. Job Hotline at (214) 904-4803. Or send your résumé to P.O. Box 36644, Dallas, Texas 75233-0644. Attention: No Pants. And come to a place where you'll enjoy working your pants off.
Exhibit 5 (Cont’d.)

BRIAN SHOWS AN EARLY
APTITUDE FOR WORKING AT
SOUTHWEST AIRLINES.

Wouldn’t you know it. The one who gave Miss Canfield the most trouble ended up working at Southwest Airlines. And he fit in quite nicely, thank you very much.

You see, at Southwest Airlines, you get check pluses for breaking the mold. For “coloring outside the lines.”

Guess that’s why we’ve ended up with flight attendants who occasionally break into song. Pilots who do halfway decent impersonations. And a CEO who does—well, you never know what he’s going to do.

All friendly, motivated people dedicated to hard work and what we call “Legendary Customer Service.”

It’s a different way to run a company. But it must be working. Because in our short 20-year history, we’ve become one of the most successful airlines in the world with the lowest employee turnover rate in the business. And it doesn’t hurt any that we also offer outstanding profit sharing and lots of great places to live.

If Southwest Airlines sounds like a place you’d like to work, call our jobline at (214) 904-4803. Or just send your resume to P.O. Box 36644, Dallas, Texas 75235-1611. Attn. HR. And if you do it in crayon, don’t worry about staying inside the lines.
Exhibit 5 (Cont’d.)

No doubt about it, Southwest Airlines has a distinct personality. For instance, how many major airlines have the King of Rock and Roll for a CEO? Or pilots who do impersonations, flight attendants who sing or ticket agents who do stand-up comedy? And how many have a success story to rival ours? In fact, we’re one of the fastest growing companies around, which means we’re always looking for more fun-loving, friendly people. 

The qualifications? It helps to be outgoing. Maybe even a bit off-center. And be prepared to stay awhile. After all, we have the lowest employee turnover rate in the industry. We also offer outstanding growth opportunities, profit sharing, and lots of neat places to live. If this sounds good to you, just phone our jobline at 214-994-4803. Or just send your resume to P.O. Box 3661, Dallas, Texas 75235-3661, Attention: Elvis.

If you come aboard, we can’t promise a free Cadillac, but there’s a good chance you’ll meet the King if he’s dressed as Elvis Presley, ignore him. We’re trying to break him of it.
### Exhibit 6
Pay Scales for 3 Selected Jobs

<table>
<thead>
<tr>
<th>Period</th>
<th>Flight Attendant</th>
<th>Reservation Agent</th>
<th>Customer Service Agent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1&lt;sup&gt;st&lt;/sup&gt; 3 months</td>
<td>$13.37</td>
<td>$5.75</td>
<td>$6.00</td>
</tr>
<tr>
<td>2&lt;sup&gt;nd&lt;/sup&gt; 3 months</td>
<td>13.37</td>
<td>6.25</td>
<td>6.50</td>
</tr>
<tr>
<td>2&lt;sup&gt;nd&lt;/sup&gt; 6 months</td>
<td>14.99</td>
<td>6.75</td>
<td>7.00</td>
</tr>
<tr>
<td>2&lt;sup&gt;nd&lt;/sup&gt; year</td>
<td>16.06</td>
<td>7.50</td>
<td>7.79</td>
</tr>
<tr>
<td>3&lt;sup&gt;rd&lt;/sup&gt; year</td>
<td>17.13</td>
<td>8.15</td>
<td>8.41</td>
</tr>
<tr>
<td>4&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>18.20</td>
<td>8.68</td>
<td>8.82</td>
</tr>
<tr>
<td>5&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>19.27</td>
<td>9.12</td>
<td>9.27</td>
</tr>
<tr>
<td>6&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>26.20</td>
<td>9.57</td>
<td>9.73</td>
</tr>
<tr>
<td>7&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>28.17</td>
<td>10.05</td>
<td>10.22</td>
</tr>
<tr>
<td>8&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>33.06</td>
<td>10.56</td>
<td>10.73</td>
</tr>
<tr>
<td>9&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>34.03</td>
<td>11.09</td>
<td>11.26</td>
</tr>
<tr>
<td>10&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>34.96</td>
<td>11.64</td>
<td>11.83</td>
</tr>
<tr>
<td>11&lt;sup&gt;th&lt;/sup&gt; year</td>
<td>35.88</td>
<td>12.22</td>
<td>12.42</td>
</tr>
</tbody>
</table>

Flight attendant pay progression ends after the thirteenth year. Customer service and reservation agent salary increases stop after the eighteenth year of employment, although after that time they are eligible for a bonus based on the cost of living index and a profitability factor for the company.