



CASE 25

Southwest Airlines in 2016: Culture, Values, and Operating Practices



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In 2016, Southwest Airlines was the world's second-largest airline in terms of total passengers boarded (144.6 million in 2015), trailing only Delta Air Lines, which boarded just over 180 million passengers in 2015 (counting those on flights operated by Delta's regional and international joint venture partners). However, based on the most recent data available from the U.S. Department of Transportation, the number of originating domestic passengers boarding Southwest flights exceeded those of Delta and its other two biggest rivals—American Airlines and United Airlines (see [Exhibit 1](#)). Southwest also had the enviable distinction of being the only major air carrier in the world that had been profitable for 43 consecutive years (1973–2015). In 2015, Southwest was named to *Fortune*'s list of the World's Most Admired Companies for the 22nd consecutive year, coming in at number seven.

EXHIBIT 1

Total Number of Domestic and International Passengers Traveling on Selected U.S. Airlines, 2000, 2005, 2010, 2013–2015 (in thousands)

Carrier	Total Number of Enplaned Passengers (including both passengers paying for tickets and passengers traveling on frequent flyer awards)					
American Airlines (see Note 1)	2000	2005	2010	2013	2014	2015
Domestic	68,319	77,297	65,774	65,070	66,384	93,280
International	<u>17,951</u>	<u>20,710</u>	<u>20,424</u>	<u>19,962</u>	<u>24,444</u>	<u>25,010</u>
Total	86,270	98,007	86,198	85,032	87,828	118,290
Delta Air Lines (see Note 2)						
Domestic	97,965	77,581	90,141	98,590	106,220	114,904
International	<u>7,596</u>	<u>8,359</u>	<u>19,390</u>	<u>18,925</u>	<u>21,798</u>	<u>22,828</u>
Total	105,561	85,940	109,531	117,515	128,018	137,732
Southwest Airlines (see Note 3)						
Domestic	72,568	88,436	106,270	115,323	126,695	142,408
International	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>500</u>	<u>2,167</u>
Total	72,568	88,436	106,270	115,323	127,195	144,575

United Airlines (see Note 4)

Domestic	72,450	55,173	43,323	65,221	64,668	69,179
International	<u>10,625</u>	<u>10,356</u>	<u>9,727</u>	<u>22,209</u>	<u>25,203</u>	<u>25,713</u>
Total	83,075	65,529	53,050	87,430	89,871	94,892

Note 1: American Airlines and US Airways merged in December 2013, but continued to operate under their separate names through 2014. Previously, US Airways had merged with America West in September 2005.

Note 2: Delta Air Lines and Northwest Airlines merged in October 2008; however, combined reporting did not begin until 2010.

Note 3: Southwest Airlines acquired AirTran in late 2010; starting in 2013 and continuing into 2014, AirTran flights were rebranded as Southwest Airlines flights. Southwest's first international flights began when some of AirTran's international flights were rebranded as Southwest flights in 2013.

Note 4: United Airlines acquired Continental Airlines in 2010, and the two companies began joint reporting of passenger traffic in 2012. Prior to 2012, traffic count data are only for United flights.

Source: U.S. Department of Transportation, Bureau of Transportation Statistics, Air Carrier Statistics, Form T-100.

From humble beginnings in 1971 as a scrappy underdog with quirky practices that once flew mainly to “secondary” airports (rather than high-traffic airports like Chicago O’Hare, Los Angeles International, Dallas–Fort Worth International, and Hartsfield–Jackson International Airport in Atlanta), Southwest had climbed up through the industry ranks to become a major competitive force in the domestic segment of the U.S. airline industry. It had weathered industry downturns, dramatic increases in the price of jet fuel, cataclysmic falloffs in airline traffic due to terrorist attacks and economy-wide recessions, and fare wars and other attempts by rivals to undercut its business, all the while adding more and more flights to more and more airports. The number of passengers flying Southwest had increased from 72.6 million in 2000 to 144.6 million in 2015. At year-end 2015, Southwest had a fleet of 704 Boeing 737 aircraft serving 97 destinations in 40 states, the District of Columbia, Puerto Rico, Mexico, Costa Rica, Belize, Jamaica, the Bahamas, Aruba, and the Dominican Republic. Southwest planned to begin flights to Cuba in 2016, if approved by the U.S. Department of Transportation.

In 2015, Southwest earned record after-tax profits of \$2.2 billion on revenues of \$19.8 billion, easily surpassing the 2014 record after-tax profits of \$1.2 billion on revenues of \$18.6 billion. In May 2016, Southwest's board of directors authorized a \$2.0 billion share repurchase program (on top of a recently completed \$1.5 billion share repurchase program announced in May 2015) and increased the quarterly dividend to \$0.10 per share starting June 2016, up from \$0.075 per share (starting in June 2015) and \$0.06 per share in 2014. The June 2016 dividend payment marked the 159th consecutive quarter Southwest had paid a dividend to shareholders.

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COMPANY BACKGROUND

In late 1966, Rollin King, a San Antonio entrepreneur who owned a small commuter air service, marched into Herb Kelleher's law office with a plan to start a low-cost/low-fare airline that would shuttle passengers between San Antonio, Dallas, and Houston.¹ Over the years, King had heard many Texas business executives complain about the length of time that it took to drive between the three cities and the expense of flying the airlines currently serving these cities. His business concept for the airline was simple: Attract passengers by flying convenient schedules, get passengers to their destination on time, make sure they have a good experience, and charge fares competitive with travel by automobile. Kelleher, skeptical that King's business idea was viable, dug into the possibilities during the next few weeks and concluded a new airline was feasible; he agreed to handle the necessary legal work and also to invest \$10,000 of his own funds in the venture.

In 1967, Kelleher filed papers to incorporate the new airline and submitted an application to the Texas Aeronautics Commission for the new company to begin serving Dallas, Houston, and San Antonio.² But rival airlines in Texas pulled every string they could to block the new airline from commencing operations, precipitating a contentious four-year parade of legal and regulatory proceedings. Kelleher led the fight on the company's behalf, eventually prevailing in June 1971 after winning two appeals to the Texas Supreme Court and a favorable ruling from U.S. Supreme Court. Kelleher recalled, "The constant proceedings had gradually come to enrage me. There was no merit to our competitors' legal assertions. They were simply trying to use their superior economic power to squeeze us dry so we would collapse before we ever got into business. I was bound and determined to show that Southwest Airlines was going to survive and was going into operation."³

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In January 1971, Lamar Muse was brought in as the CEO to get operations underway. Muse was an aggressive and self-confident airline veteran who knew the business well and who had the entrepreneurial skills to tackle the challenges of building the airline from scratch and then competing head-on with the major carriers. Through private investors and an initial public offering of stock in June 1971, Muse raised \$7 million in new capital to purchase planes and equipment and provide cash for startup. Boeing agreed to supply three new 737s from its inventory, discounting its price from \$5 million to \$4 million and financing 90 percent of the \$12 million deal. Muse was able to recruit a talented senior staff that included a number of veteran executives from other carriers. He particularly sought out people who were innovative, wouldn't shirk from doing things differently or unconventionally, and were motivated by the challenge of building an airline from scratch. Muse wanted his executive team to be willing to think like mavericks and not be lulled into instituting practices at Southwest that imitated what was done at other airlines.

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Southwest's Struggle to Gain a Market Foothold

In June 1971, Southwest initiated its first flights with a schedule that soon included 6 roundtrips between Dallas and San Antonio and 12 roundtrips between Houston and Dallas. But the introductory \$20 one-way fares to fly the Golden Triangle, well below the \$27 and \$28 fares charged by rivals, attracted disappointingly small numbers of passengers. To try to gain market visibility and drum up more passengers, Southwest undertook some creative actions to supplement its ad campaigns publicizing its low fares:

- Southwest decided to have its flight attendants dress in colorful hot pants and white knee-high boots with high heels. Recruiting ads for Southwest's first group of attendants headlined "Attention, Raquel Welch: You can have a job if you measure up." Two thousand applicants responded and those selected for interviews were asked to come dressed in hot pants to show off their legs—the company wanted to hire long-legged beauties with sparkling personalities. Over 30 of Southwest's first graduating class of 40 flight attendants consisted of young ladies who were cheerleaders and majorettes in high school and thus had experience performing skimpily dressed in front of people.
- A second attention-getting action was to give passengers free alcoholic beverages during daytime flights. Most passengers on these flights were business travelers. Management's thinking was that many passengers did not drink during the daytime and that with most flights being less than an hour's duration it would be cheaper to simply give the drinks away rather than collect the money.
- Taking a cue from being based at Dallas Love Field, Southwest began using the tagline "Now There's Somebody Else Up There Who Loves You." The routes between Houston, Dallas, and San Antonio became known as the Love Triangle. Southwest's planes were referred to as Love Birds, drinks became Love Potions, peanuts were called Love Bites, drink coupons were Love Stamps, and tickets were printed on Love Machines. The "love" campaign set the tone for Southwest's approach to its customers and company efforts to make flying Southwest Airlines an enjoyable, fun, and differentiating experience. (Later, when the company went public, it chose LUV as its stock-trading symbol.)



- In order to add more flights without buying more planes, the head of Southwest's ground operations came up with a plan for ground crews to off-load passengers and baggage, refuel the plane, clean the cabin and restock the galley, on-load passengers and baggage, do the necessary preflight checks and paperwork, and push away from the gate in 10 minutes. The 10-minute turnaround became one of Southwest's signatures during the 1970s and 1980s. (In later years, as passenger volume grew and many flights were filled to capacity, the turnaround time gradually expanded to 25 minutes—because it took more time to unload and load 125 passengers, as compared to a half-full plane with just 60 to 65 passengers. Even so, the 25-minute average turnaround times at Southwest during the 2000–2009 period were shorter than the 30–50 minute turnarounds typical at other major airlines.)
- In late November 1971, Lamar Muse came up with the idea of offering a \$10 fare to passengers on the Friday night Houston–Dallas flight. With no advertising, the 112-seat flight sold out. This led Muse to realize that Southwest was serving two quite distinct types of travelers in the Golden Triangle market: (1) business travelers who were more time sensitive than price sensitive and wanted weekday flights at times suitable for conducting business, and (2) price-sensitive leisure travelers who wanted lower fares and had more flexibility about when to fly.⁴ He came up with a two-tier on-peak and off-peak pricing structure in which all seats on weekday flights departing before 7 PM were priced at \$26 and all seats on other flights were priced at \$13. Passenger traffic increased significantly—and systemwide on-peak and off-peak pricing soon became standard across the whole airline industry.
- In 1972, the company decided to move its flights in Houston from the newly opened Houston Intercontinental Airport (where it was losing money and where it took 45 minutes to get to downtown) to the abandoned Houston Hobby Airport located much closer to downtown Houston. Despite being the only carrier to fly into Houston Hobby, the results were spectacular—business travelers who flew to Houston frequently from Dallas and San Antonio found the Houston Hobby location far more convenient and passenger traffic doubled almost immediately.

- In early 1973, in an attempt to fill empty seats on its San Antonio–Dallas flights, Southwest cut its regular \$26 fare to \$13 for all seats, all days, and all times. When Braniff International, at that time one of Southwest’s major rivals, announced \$13 fares of its own, Southwest retaliated with a two-page ad run in the Dallas newspapers headlining “Nobody is going to shoot Southwest Airlines out of the sky for a lousy \$13,” and containing copy saying Braniff was trying to run Southwest out of business. The ad announced that Southwest would not only match Braniff’s \$13 fare but that it would also give passengers the choice of buying a regular-priced ticket for \$26 and receiving a complimentary fifth of Chivas Regal scotch, Crown Royal Canadian whiskey, or Smirnoff vodka (or, for nondrinkers, a leather ice bucket). Over 75 percent of Southwest’s Dallas–Houston passengers opted for the \$26 fare, although the percentage dropped as the two-month promotion wore on and corporate controllers began insisting that company employees use the \$13 fare. The local and national media picked up the story of Southwest’s offer, proclaiming the battle as a David versus Goliath struggle in which the upstart Southwest did not stand much of a chance against the much larger and well-established Braniff; grassroots sentiment in Texas swung to Southwest’s side.

All these moves paid off. The resulting gains in passenger traffic allowed Southwest to report its first-ever annual profit in 1973.

More Legal and Regulatory Hurdles

During the rest of the 1970s, Southwest found itself embroiled in another round of legal and regulatory battles. One battle involved Southwest’s refusal to move its flights from Dallas Love Field, located 10 minutes from downtown, to the newly opened Dallas–Fort Worth Regional Airport, which was 30 minutes from downtown Dallas. Local officials were furious because they were counting on fees from Southwest’s flights in and out of DFW to help service the debt on the bonds issued to finance the construction of DFW. Southwest’s position was that it was not required to move because it had not agreed to do so or been ordered to do so by the Texas Aeronautics Commission—moreover, the company’s headquarters were located at Love Field. The courts eventually ruled Southwest’s operations could remain at Love Field.

A second battle ensued when rival airlines protested Southwest's application to begin serving several smaller cities in Texas; their protest was based on arguments that these markets were already well served and that Southwest's entry would result in costly overcapacity. Southwest countered that its low fares would allow more people to fly and grow the market. Again, Southwest prevailed and its views about low fares expanding the market proved accurate. In the year before Southwest initiated service, 123,000 passengers flew from Harlingen Airport in the Rio Grande Valley to Houston, Dallas, or San Antonio; in the 11 months following Southwest's initial flights, 325,000 passengers flew to the same three cities.

Believing that Braniff and Texas International were deliberately engaging in tactics to harass Southwest's operations, Southwest convinced the U.S. government to investigate what it considered predatory tactics by its chief rivals. In February 1975, Braniff and Texas International were indicted by a federal grand jury for conspiring to put Southwest out of business—a violation of the Sherman Antitrust Act. The two airlines pleaded “no contest” to the charges, signed cease-and-desist agreements, and were fined a modest \$100,000 each.

When Congress passed the Airline Deregulation Act in 1978, Southwest applied to the Civil Aeronautics Board (now the Federal Aviation Administration) to fly between Houston and New Orleans. The application was vehemently opposed by local government officials and airlines operating out of DFW because of the potential for passenger traffic to be siphoned away from DFW. The opponents solicited the aid of Fort Worth congressman Jim Wright, then the majority leader of the U.S. House of Representatives, who took the matter to the floor of the House of Representatives; a rash of lobbying and maneuvering ensued. What emerged came to be known as the Wright Amendment of 1979: no airline may provide nonstop or through-plane service from Dallas Love Field to any city in any state except for locations in Texas, Louisiana, Arkansas, Oklahoma, and New Mexico. Southwest was prohibited from advertising, publishing schedules or fares, or checking baggage for travel from Dallas Love Field to any city it served outside the five-state “Wright Zone.” The Wright Amendment continued in effect until 1997 when Alabama, Mississippi, and Kansas were added to the five-state Wright Zone; in 2005, Missouri was added to the zone. In 2006, after a heated battle in Congress, legislation was passed and signed into law that repealed the Wright Amendment beginning in October 2014. With the repeal of the Wright Amendment, Southwest Airlines increased flight activity from Dallas Love Field by 50 percent to add 20 new nonstop destinations with 180 daily departures to a total of 50 nonstop destinations.

The Emergence of a Combative Can-Do Culture at Southwest

The legal, regulatory, and competitive battles that Southwest fought in these early years produced a strong esprit de corps among Southwest personnel and a drive to survive and prosper despite the odds. With newspaper and TV stories reporting Southwest's difficulties regularly, employees were fully aware that the airline's existence was constantly on the line. Had the company been forced to move from Love Field, it would most likely have gone under, an outcome that employees, Southwest's rivals, and local government officials understood well. According to Southwest's former president, Colleen Barrett, the obstacles thrown in Southwest's path by competitors and local officials were instrumental in building Herb Kelleher's passion for Southwest Airlines and ingraining a combative, can-do spirit into the corporate culture.⁵

They would put twelve to fifteen lawyers on a case and on our side there was Herb. They almost wore him to the ground. But the more arrogant they were, the more determined Herb got that this airline was going to go into the air—and stay there.

The warrior mentality, the very fight to survive, is truly what created our culture.

When Lamar Muse resigned in 1978, Southwest's board wanted Herb Kelleher to take over as chair and CEO. But Kelleher enjoyed practicing law and, while he agreed to become board chair, he insisted that someone else be CEO. Southwest's board appointed Howard Putnam, a group vice president of marketing services at United Airlines, as Southwest's president and CEO in July 1978. Putnam asked Kelleher to become more involved in Southwest's day-to-day operations, and over the next three years Kelleher got to know many of the company's personnel and observe them in action. Putnam announced his resignation in fall 1981 to become president and COO at Braniff International. This time, Southwest's board succeeded in persuading Kelleher to take on the additional duties of CEO and president.



Sustained Growth Transforms Southwest into the Domestic Market Share Leader, 1981–2015

When Herb Kelleher took over in 1981, Southwest was flying 27 planes to 14 destination cities and had \$270 million in revenues and 2,100 employees. Over the next 20 years, Southwest Airlines prospered under Kelleher's leadership. When Kelleher stepped down as CEO in mid-2001, the company had 350 planes flying to 58 U.S. airports, annual revenues of \$5.6 billion, over 30,000 employees, and 64 million fare-paying passengers annually.

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Under the two CEOs who succeeded Kelleher, Southwest continued its march to becoming the market share leader in domestic air travel, growing to 2015 revenues of \$19.8 billion and 49,600 employees, flying 704 planes to 97 airports in 40 states and 7 destinations outside the United States, and transporting some 118 million-plus fare-paying passengers and some 144 million-plus passengers (including those traveling on frequent flyer awards) in 2015. In the process, the company won more industry Triple Crown awards for best on-time record, best baggage handling, and fewest customer complaints than any other U.S. airline. While Southwest fell short of its on-time performance and baggage handling goals in some years, it still led the domestic airline industry in customer satisfaction and received other awards and recognitions, including Best Domestic Airline for Customer Service by *Executive Travel* magazine's Leading Edge Awards, Brand of the Year in the Value Airline Category by the Harris Poll, and the top ranking by *InsideFlyer* magazine for Best Customer Service and Best Loyalty Credit Card.

Exhibit 2  provides a five-year summary of Southwest's financial and operating performance. **Exhibit 3**  provides selected financial and operating data for major U.S. air carriers during 1995–2015.

HERB KELLEHER: THE CEO WHO TRANSFORMED SOUTHWEST INTO A MAJOR AIRLINE

Herb Kelleher majored in philosophy at Wesleyan University in Middletown, Connecticut, graduating with honors. He earned his law degree at New York University, again graduating with honors and also serving as a member of the law review. After graduation, he clerked for a New Jersey Supreme Court justice for two years and then joined a law firm in Newark. Upon marrying a woman from Texas and becoming enamored with Texas, he moved to San Antonio where he became a successful lawyer and came to represent Rollin King's small aviation company.

When Herb Kelleher took on the role of Southwest's CEO in 1981, he made a point of visiting with maintenance personnel to check on how well the planes were running and talking with the flight attendants. Kelleher did not do much managing from his office, preferring instead to be out among the troops as much as he could. His style was to listen and observe and to offer encouragement. Kelleher attended most graduation ceremonies of flight attendant classes, and he often appeared to help load bags on "Black Wednesday," the busy travel day before Thanksgiving. He knew the names of thousands of Southwest employees and was held in the highest regard by Southwest employees. When he attended a Southwest employee function, he was swarmed like a celebrity.

Kelleher had an affinity for bold-print Hawaiian shirts, owned a tricked-out motorcycle, and made no secret of his love for smoking and Wild Turkey whiskey. He loved to make jokes and engage in pranks and corporate antics, prompting some people to refer to him as the "clown prince" of the airline industry. He once appeared at a company gathering dressed in an Elvis costume and had arm-wrestled a South Carolina company executive at a public event in Dallas for rights to use "Just Plane Smart" as an advertising slogan.⁶ Kelleher was well known inside and outside the company for his combativeness, particularly when it came to beating back competitors. On one occasion, he reportedly told a group of veteran employees, "If someone says they're going to smack us in the face—knock them out, stomp them out, boot them in the ditch, cover them over, and move on to the next thing. That's the Southwest spirit at work."⁷ On another occasion, he said, "I love battles. I think it's part of the Irish in me. It's like what Patton said, 'War is hell and I love it so.' That's how I feel. I've never gotten tired of fighting."⁸

While Southwest was deliberately combative and flamboyant in some aspects of its operations, when it came to the financial side of the business Kelleher insisted on fiscal conservatism, a strong balance sheet, comparatively low levels of debt, and zealous attention to bottom-line profitability. While believing strongly in being prepared for adversity, Kelleher had an aversion to Southwest personnel spending time drawing up all kinds of formal strategic plans, saying “Reality is chaotic; planning is ordered and logical. The meticulous nit-picking that goes on in most strategic planning processes creates a mental straightjacket that becomes disabling in an industry where things change radically from one day to the next.” Kelleher wanted Southwest managers to think ahead, have contingency plans, and be ready to act when it appeared that the future held significant risks or when new conditions suddenly appeared and demanded prompt responses.

EXHIBIT 2**Summary of Southwest Airlines's Financial and Operating Performance, 2011–2015**

	Year Ended December 31			
	2015	2014	2013	2012
Financial Data (in millions, except per share amounts):				
Operating revenues	\$19,820	\$ 18,605	\$17,699	\$17,088
Operating expenses	<u>15,704</u>	<u>16,380</u>	<u>16,421</u>	<u>16,465</u>
Operating income	4,116	2,225	1,278	623
Other expenses (income) net	<u>637</u>	<u>409</u>	<u>69</u>	<u>(62)</u>
Income before taxes	3,479	1,816	1,209	685
Provision for income taxes	<u> </u>	<u>680</u>	<u>455</u>	<u>264</u>
Net income	1,298	\$1,136	\$ 754	\$421
Net income per share, basic	\$ 3.30	\$ 1.65	\$ 1.06	\$0.56
Net income per share, diluted	\$ 3.27	\$ 1.64	\$ 1.05	\$0.56
Cash dividends per common share	\$0.2850	\$0.2200	\$0.1300	\$0.0345
Total assets at period-end	\$ 21,312	\$ 19,723	\$19,345	\$18,596
Long-term obligations at period-end	2,541	2,434	2,191	2,883
Stockholders' equity at period-end	7,358	6,775	7,336	6,992

Operating Data:

Revenue passengers carried	118,171,211	110,496,912	\$ 108,075,976	109,346,509
Enplaned passengers	144,574,882	135,767,188	133,155,030	133,978,100
Revenue passenger miles (RPMs) (000s) ⁽¹⁾	117,499,879	108,035,133	104,348,216	102,874,979
Available seat miles (ASMs) (000s) ⁽²⁾	140,501,409	131,003,957	130,344,072	128,137,110
Load factor ⁽³⁾	83.6%	82.5%	80.1%	80.3%
Average length of passenger haul (miles)	994	978	966	941
Average length of each flight (miles)	750	721	703	693
Trips flown	1,267,358	1,255,502	1,312,785	1,361,558
Average passenger fare	\$154.85	\$159.80	\$154.72	\$147.17
Passenger revenue yield per RPM (cents) ⁽⁴⁾	15.57¢	16.34¢	16.02¢	15.64¢
Operating revenue per ASM (cents) ⁽⁵⁾	13.98¢	14.20¢	13.58¢	13.34¢
Passenger revenue per ASM (cents) ⁽⁶⁾	13.02¢	13.48¢	12.83¢	12.56¢
Operating expenses per ASM (cents) ⁽⁷⁾	11.18¢	12.50¢	12.60¢	12.85¢
Operating expenses per ASM, excluding fuel (cents)	8.61¢	8.46¢	8.18¢	8.07¢
Operating expenses per ASM, excluding fuel and profit sharing (cents)	8.17¢	8.19¢	8.01¢	7.98¢

Fuel costs per gallon, including fuel tax	\$ 1.90	\$ 2.93	\$ 3.16	\$ 3.30
Fuel consumed, in gallons (millions)	1,901	1,801	1,818	1,847
Active full time equivalent employees	49,583	46,278	44,381	45,861
Aircraft in service at period-end ⁽⁸⁾	704	665	681	694

⁽¹⁾A revenue passenger mile is one paying passenger flown one mile.

⁽²⁾An available seat mile (ASM) is one seat (empty or full) flown one mile. Also referred to as "capacity," which is a measure of the space available to carry passengers in a given period.

⁽³⁾Revenue passenger miles divided by available seat miles.

⁽⁴⁾Calculated as passenger revenue divided by revenue passenger miles. It represents the average cost paid by a paying passenger to fly one mile.

⁽⁵⁾Calculated as operating revenue divided by available seat miles. It is a measure of operating revenue production based on the total available seat miles flown during a particular period.

⁽⁶⁾Calculated as passenger revenue divided by available seat miles. It is a measure of passenger revenue production based on the total available seat miles flown during a particular period.

⁽⁷⁾Calculated as operating expenses divided by available seat miles. Also referred to as "unit costs" or "cost per available seat mile," this is the average cost to fly an aircraft seat (empty or full) one mile.

⁽⁸⁾Includes leased aircraft and excludes aircraft that were not available for service, in storage, held for sale, or held for return to the lessor.

Sources: Southwest Airlines 10-K report, 2013, 2015.

EXHIBIT 3**Selected Operating and Financial Data for Major U.S. Airline Carriers, 1995, 2000, 2005, 2010, 2013–2015**

	1995	2000	2005	2010	2013	2014	2015
Passengers (in millions)	559.0	666.2	738.3	720.5	740.9	761.0	796.9
Flights (in thousands)	8,062	9,035	11,564	9,521	9,152	8,954	8,895
Revenue Passenger Miles (in billions)	603.4	692.8	778.6	798.0	834.8	858.0	899.0
Available Seat Miles (in billions)	807.1	987.9	1,002.7	972.6	1,004.1	1,028.5	1,073.1
Load Factor	67.0	72.4	77.7	82.0	83.1	83.4	83.8
Passenger Revenues (in millions)	\$69,470	\$93,622	\$93,500	\$103,978	\$120,641	\$128,705	\$126,170
Operating Profit (Loss) (in millions)	\$ 5,852	\$ 7,014	\$ 447	\$ 10,517	\$ 12,519	\$ 16,674	\$ 30,777
Net Profit (Loss) excluding one-time charges and gains (in millions)	\$ 2,283	\$ 2,486	(\$5,782)	\$ 3,665	\$ 12,711	\$ 8,502	\$26,398
Total Employees	546,987	679,967	562,467	531,224	552,581	558,368	576,139

Sources: Air Transport Association, *2005 Economic Report*, p. 7; U.S. Department of Transportation, Bureau of Transportation Statistics, Airline Traffic Data Press Releases, various years.

Kelleher was a strong believer in the principle that employees—not customers—came first:⁹

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You have to treat your employees like your customers. When you treat them right, then they will treat your outside customers right. That has been a very powerful competitive weapon for us. You've got to take the time to listen to people's ideas. If you just tell somebody no, that's an act of power and, in my opinion, an abuse of power. You don't want to constrain people in their thinking.

Another indication of the importance that Kelleher placed on employees was the message he had penned in 1990 that was prominently displayed in the lobby of Southwest's headquarters in Dallas:

The people of Southwest Airlines are "the creators" of what we have become—and of what we will be.

Our people transformed an idea into a legend. That legend will continue to grow only so long as it is nourished—by our people's indomitable spirit, boundless energy, immense goodwill, and burning desire to excel.

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Our thanks—and our love—to the people of Southwest Airlines for creating a marvelous family and a wondrous airline.

In June 2001, Herb Kelleher stepped down as CEO but continued on in his role as chair of Southwest's board of directors and the head of the board's executive committee; as chair, he played a lead role in Southwest's strategy, expansion to new cities and aircraft scheduling, and governmental and industry affairs. In May 2008, after more than 40 years of leadership at Southwest, Kelleher retired as chair (but he remained a full-time Southwest employee until July 2013 and carried the title of Chairman Emeritus in 2016).



EXECUTIVE LEADERSHIP AT SOUTHWEST: 2001–2016

In June 2001 Southwest Airlines, responding to anxious investor concerns about the company's leadership succession plans, began an orderly transfer of power and responsibilities from Herb Kelleher, age 70, to two of his most trusted protégés. James F. Parker, 54, Southwest's general counsel and one of Kelleher's most trusted protégés, succeeded Kelleher as Southwest's CEO. Another of Kelleher's trusted protégés, Colleen Barrett, 56, Southwest's executive vice president—customers and self-described keeper of Southwest's pep rally corporate culture, became president and chief operating officer.

James Parker, CEO, 2001–2004

James Parker's association with Herb Kelleher went back 23 years to the time when they were colleagues at Kelleher's old law firm. Parker moved over to Southwest from the law firm in February 1986. Parker's profile inside the company as Southwest's vice president and general counsel had been relatively low, but he was Southwest's chief labor negotiator and much of the credit for Southwest's good relations with employee unions belonged to Parker. Parker and Kelleher were said to think much alike, and Parker was regarded as having a good sense of humor, although he did not have as colorful and flamboyant a personality as Kelleher. Parker was seen as an honest, straight-arrow kind of person who had a strong grasp of Southwest's culture and market niche and who could be nice or tough, depending on the situation. When his appointment was announced, Parker said:¹⁰

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There is going to be no change of course insofar as Southwest is concerned. We have a very experienced leadership team. We've all worked together for a long time. There will be evolutionary changes in Southwest, just as there have always been in our history. We're going to stay true to our business model of being a low-cost, low-fare airline.

Parker retired unexpectedly, for personal reasons, in July 2004, stepping down as CEO and vice chair of the board and also resigning from the company's board of directors. He was succeeded by Gary C. Kelly.



Colleen Barrett, Southwest's President, 2001–2008

Barrett began working with Kelleher as his legal secretary in 1967 and had been with Southwest since 1978. As executive vice president—customers, Barrett had a high profile among Southwest employees and spent most of her time on culture-building, morale-building, and customer service; her goal was to ensure that employees felt good about what they were doing and felt empowered to serve the cause of Southwest Airlines.¹¹ She and Kelleher were regarded as Southwest's guiding lights, and some analysts said she was essentially functioning as the company's chief operating officer prior to her formal appointment as president. Much of the credit for the company's strong record of customer service and its strong-culture work climate belonged to Barrett.

Barrett had been the driving force behind lining the hallways at Southwest's headquarters with photos of company events and trying to create a family atmosphere at the company. Believing it was important to make employees feel cared about and important, Barrett had put together a network of contacts across the company to help her stay in touch with what was happening with employees and their families. When network members learned about events that were worthy of acknowledgment, the word quickly got to Barrett—the information went into a database and an appropriate greeting card or gift was sent. Barrett had a remarkable ability to give gifts that were individualized and connected her to the recipient.¹²

Barrett was the first woman appointed as president and COO of a major U.S. airline. In October 2001, *Fortune* included Colleen Barrett on its list of the 50 most powerful women in American business (she was ranked number 20). Barrett retired as president in July 2008.