Pensacola Christian College

Case Study: Southwest Airlines

A Project Submitted to
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BA 430
Strategic Management

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Company Overview

Southwest Airlines is one of the strongest companies in the airline industry. Southwest started off in 1971 only flying to three cities in Texas and have been slowly growing ever since. They have focused on short, point-to-point flights. This unique strategy has allowed them to minimize their costs structure, which in turn allows them to be extremely profitable. Even when all other airlines were struggling, Southwest has maintained their profitability. In fact, they have remained profitable for over 40 years. They have also been ranked top airline in almost every category for years. On top of their cheap prices, they have a strong focus on providing the best customer service possible. These factors have allowed them to become a strong competitor in the airline industry in a relatively short amount of time.

However, Southwest is not bound to stay a top competitor forever. Many competitors have attempted to copy Southwest's business model. Although most have failed miserably, JetBlue has successfully adopted Southwest's strategy, and by 2012 JetBlue reported revenues of over $5 billion. If JetBlue can successfully mimic Southwest's strategy, other companies can too. Not only can other companies mimic Southwest, but Southwest's expansion plan has created new obstacles. Southwest has been very strategic with expansion and have picked each city they expand to very carefully. However, Southwest's move to the Northeast has created problems with frequent flying schedules. The bad weather in the winter has caused many delays and has hurt their fast travel times. On top of the threat of imitators and the delayed flight times due to expansion, Southwest also must maintain their culture after the acquisition of AirTran. AirTran was bought out by Southwest in 2010, and has opened Southwest to over 30 new destination, including a couple of new cities internationally. Southwest must be able to maintain their unique culture in the wake of this massive expansion. Southwest's culture has helped to set them apart in the airline industry, and to lose it could hurt their market share. These problems have caused the costs structure of Southwest to rise, and the costs show no sign of going down. Southwest must find a way to keep their market share in light of these industry changes.[1]

Environmental Scanning

Demographic. More people are flying than ever before. In 1971, only 49 percent of the adult US population had ever flown in a plane before. By 2015, that number more than doubled to 81 percent of the adult US population. The same study found that the number of people who have flown in the last year was up 24 percent from 1971 to 2015. The Airline Deregulation Act is partly to be thanked for this incredible increase, as well as Southwest airlines. Southwest has become so known for their cheap prices that the term "Southwest Affect" (when Southwest enters a market, prices tend to drop) has been coined. As prices drop, more people can afford to

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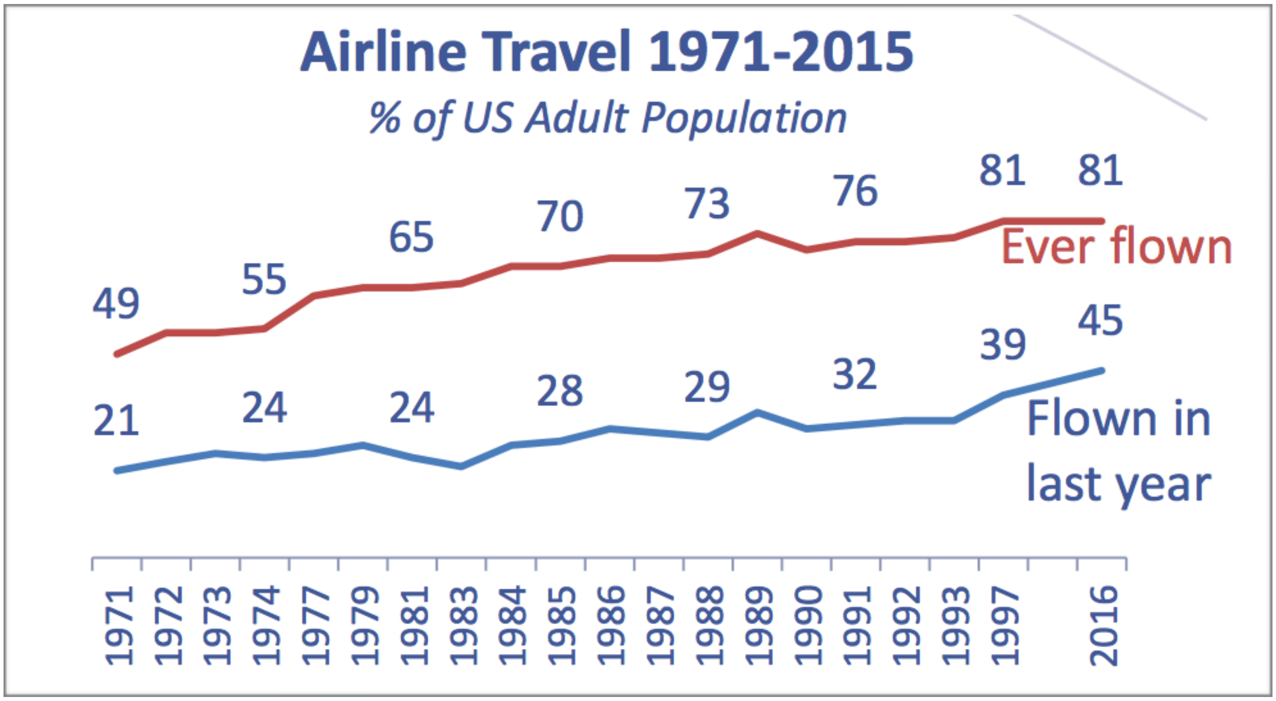
[1] Hitt, Michael A., R. Duane Ireland, and Robert E. Hoskisson. Strategic Management: Competitiveness & Globalization: Concepts & Cases. Boston, MA, USA: Cengage, 2020.

travel. The dramatic price changes is why the demographics for people who have flown has changed so drastically.[2]



Economic. Like most industries, the success of the airline industry largely depends on how the economy as a whole is doing. An economic downturn could severely cripple the airline industry, but a booming economy could cause the airline industry to soar. Currently there seems to be no sign of slowing down for the airline industry. Revenue passenger kilometers (RPK), which is a measure of the number of passengers carried by an airline, has been steadily increasing since the 2008 recession. Consequently, companies like Southwest have continued to see increasing number of passengers. As long as the economy continues to look up, airlines will continue to see decent economic times.[3]

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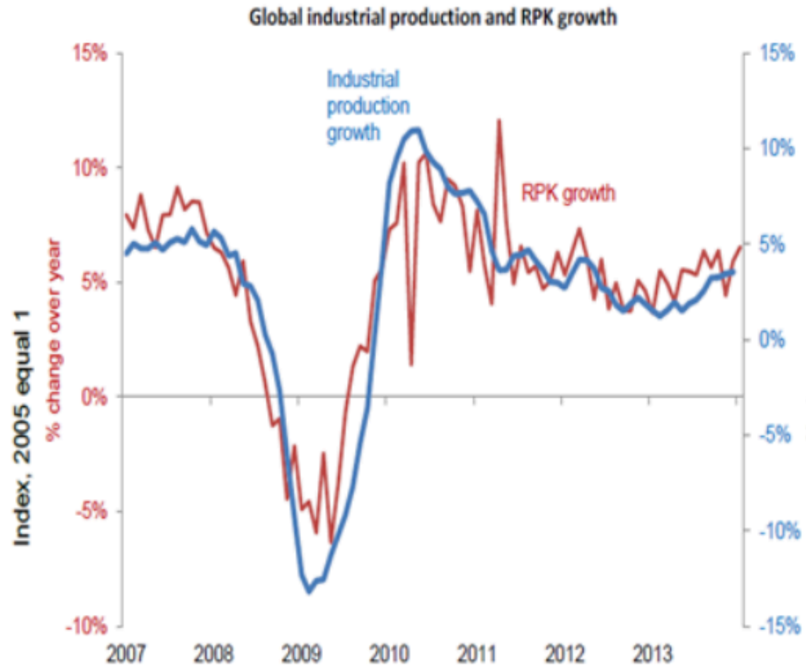
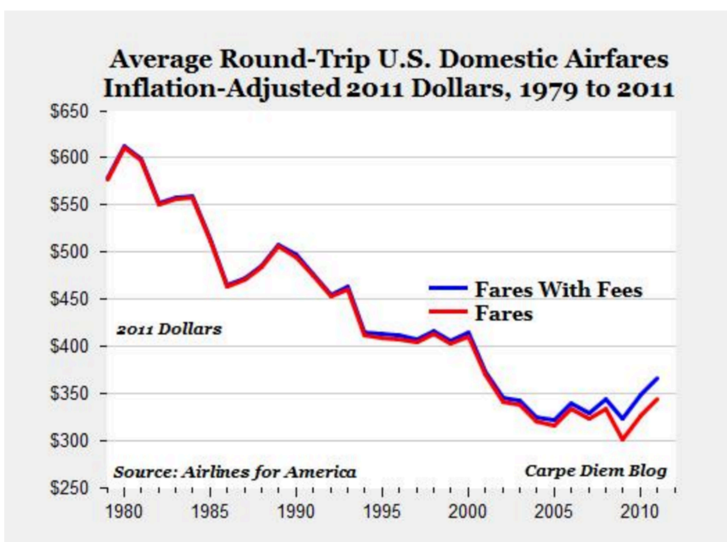
[2] "Airlines For America |." Airlines For America |. Accessed October 1, 2019. http://airlines.org/.

[3] "Why Economic Factors Support Airline Industry Growth." Yahoo! Finance. Yahoo!, September 4, 2014. https://finance.yahoo.com/news/why-economic-factors-support-airline-210029406.html.



Political/Legal. Before 1978, most people could not afford to fly. The high prices were due to extreme government regulation. Washington had a say in everything the airline industry could and could not do, which discouraged competition and created a strong oligopoly. However, in 1978, everything changed when the Airline Deregulation Act was signed into law. Airlines now played in a true free market system. Prices plummeted and have continued to drop ever since then. Below is a chart showing just how much the industry prices have changed since the law was passed.[4]



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[4] Thompson, Derek. "How Airline Ticket Prices Fell 50% in 30 Years (and Why Nobody Noticed)." The Atlantic. Atlantic Media Company, February 28, 2013. https://www.theatlantic.com/business/archive/2013/02/how-airline-ticket-prices-fell-50-in-30-years-and-why-nobody-noticed/273506/.

The deregulation allowed Southwest to thrive, and it is partially responsible for them being so successful today. This goes to show that government regulation of the airline industry has tremendous affects on how successful an airline can be. Airlines, including Southwest, must play close attention to how political leaders attempt to regulated (or deregulate) the industry. In the case of the airline industry, government policy can make or break a company.

Sociocultural. As social media continues to connect people throughout the world, companies must keep up. Social media is a prime platform for getting to know customers's wants and needs. The airline industry is no different. "As social media takes precedence in the overall customer relationship management pie, airlines will need to look at building a large and robust resource pool that can respond to customer queries, complaints, posts and tweets round the clock." Southwest has kept on top of this trend. Their social media profiles are extremely active, and they even occasionally have trivia to get customers involved. Social media is an excellent tool to get involved with customers, and Southwest has managed to create a solid social media presence in response to the sociocultural changes.[5]

Technological. Southwest has differentiated themselves in the airlines industry by being on top of technological changes. In fact, Southwest was the first airline company to have a website. This move was critical in bringing in more customers as more people are willing to buy a ticket through a website than anywhere else. Online ticket ordering makes up about 80% of Southwest's ticket sales, which are bought directly from their own website. Southwest also has the "Low Fair Calendar" feature, which helps customers on their website find the lowest airfare "based on availability across an entire month." These features have encouraged people to buy directly from the Southwest website and not from a third-party vendor, which increases Southwest's income on each flight. By being on top of technological changes, Southwest has grown their market share substantially.[6]

Global. When Southwest acquired AirTran, they were able to increase their international presence. Before AirTran, Southwest flew to only three international locations (Nassau, Aruba and Montego Bay). The AirTran acquisition allowed Southwest to substantially increase their international footprint with flights to several more cities in Mexico. With the Latin international market growing each year, Southwest is in a strategic position to begin to grow their market share in Latin America. The international expansion also promises to increase Southwest's growth in the future.[7]

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[5] "5 Trends for the Global Airlines Industry." Article : 5 Trends for the Global Airlines Industry. Accessed October 1, 2019. https://www.wns.com/insights/articles/articledetail/62/5-trends-for-the-global-airline-industry.

[6] "Southwest Corporate Fact Sheet." Southwest Airlines Newsroom. Accessed October 1, 2019. https://www.swamedia.com/pages/corporate-fact-sheet#distinctions.

[7] Team, Trefis. "Southwest's Expanding International Service Will Lift Its Growth In The Coming Years." Forbes. Forbes Magazine, August 20, 2014. https://www.forbes.com/sites/greatspeculations/2014/08/20/southwests-expanding-international-service-will-lift-its-growth-in-the-coming-years/#4ec94d5473b9.

Physical/Sustainable. As more people become eco-friendly, Southwest has pledged to become as green as possible. They have invested $175 million to increase flight pattern accuracy, which is key in eliminating greenhouse gas emissions. Southwest has also made strides to improve their fuel efficiency, which saw a 2.1 percent increase from 2007 to 2008. Southwest also started a efficient recycling program. This program "diverted more than 450 metric tons of waste from landfills" in 2008, and has continued to divert tons of waste ever since. Below is a chart detailing the waste reduction through their recycling program.[8]

RECYCLING & ENERGY RECOVERY*		
Recycled Materials	**Recycled Solid Waste (Metric Tons)**	**Energy Recovery (BTUs)**
Cardboard, paper, plastic, aluminum	217.8	
Lamps	0.6	
Batteries	118.3	
Electronics	106.6	
Used Oil	–	4,541,545,000
Filters, liquid & solid paint waste	11.8	285,240,000
	455.1	**4,826,785,000**

Although the airline industry has a bad reputation of polluting the environment, Southwest has done an excellent job of becoming more sustainable with each passing year.

Stakeholder Analysis

Capital Market Stakeholders. The capital market stakeholders for Southwest are similar to the rest of the corporate world. These stakeholders are made up of shareholders as well as major suppliers of capital. Some major shareholders include PRIMECAP Management Co. and Berkshire Hathaway, which hold 13 and 10 percent stakes, respectively. These companies are highly interested in the success of Southwest due to their high stakes. Southwest's major suppliers of capital are their shareholders.[9]

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[8] "Annual Reports." Annual Reports – Southwest Airlines. Accessed October 1, 2019. http://investors.southwest.com/financials/company-reports/annual-reports.

[9] "LUV." CNNMoney. Cable News Network. Accessed October 1, 2019. https://money.cnn.com/quote/shareholders/shareholders.html?symb=LUV&subView=institutional.

Product Market Stakeholders. Southwest's product market stakeholders are made up of their customers, suppliers, host communities, and unions. Southwest does all they can to make sure that customers are satisfied with their flights. Southwest also tries to maintain good relationships with their suppliers. As discussed in the sustainable section, Southwest does all they can to provide a clean environment for they host communities and the rest of the world. Most Southwest employees are unionized, so Southwest must have a good relationship with union leaders as well. Ultimately, Southwest treats their product market stakeholders very well.[1]

Organizational Stakeholders. Organizational stakeholders for Southwest are made up of the employees (both managers and non managers). Southwest tries to provide the best care for their employees as possible. In fact, they pay much better than most airlines, which will be discussed later. By paying above the industry standard, Southwest does all they can to provide the best living conditions for their employees.[1]

Industry Analysis

Industry definition. Southwest Airlines falls in the airline industry, which is NAICS number 48111. According to the NAICS, the airline industry is comprised of "establishments primarily engaged in providing air transportation of passengers or passengers and freight over regular routes and on regular schedules." Airplanes make up the biggest percent of the flights for the airline industry.[10]

Industry Competitive Structure. The airline industry is an oligopoly due to its high barriers of entry. An oligopoly is an industry in which few giants dominate the entire industry. The price of operating an airline (planes, hangers, pilots, ect.) is simply too much for most people, and the fluctuating economy for airlines continues to scare potential new entrants away. Southwest's main competitors are American, Delta, and United, with a few smaller airlines taking up a small portion of the market share. Below is a chart that shows the industry's market share for each company[11]:

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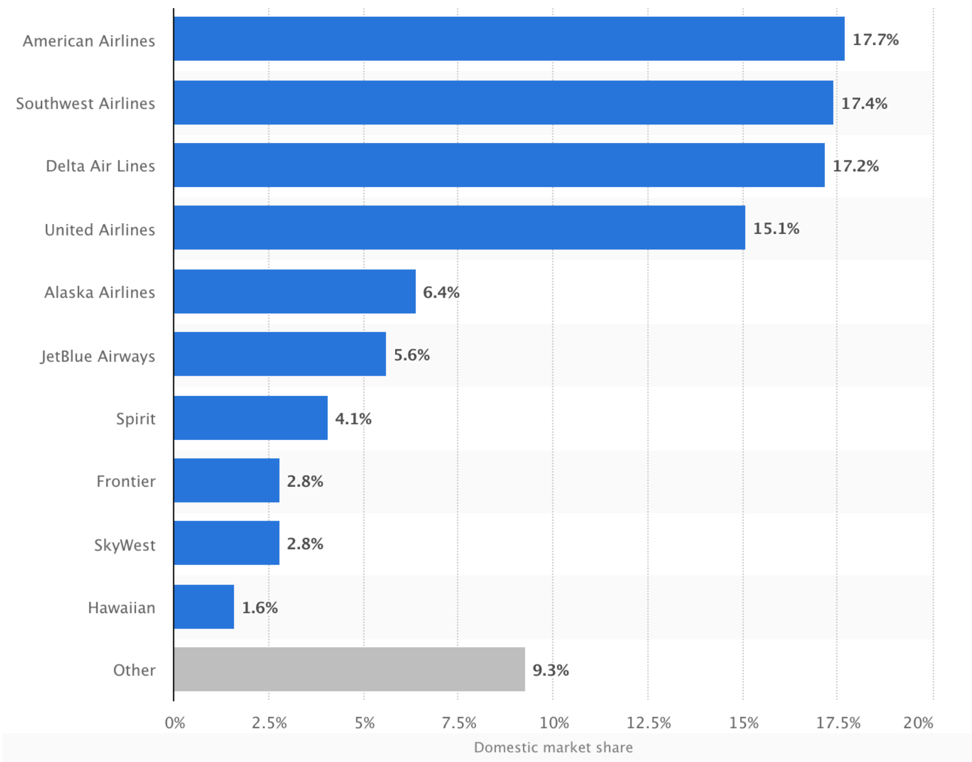
[10] "NAICS Code: 481111 Scheduled Passenger Air Transportation." NAICS Association. Accessed October 1, 2019. https://www.naics.com/naics-code-description/?code=481111.

[11] "U.S. Airline Industry Market Share 2019." Statista. Accessed October 1, 2019. https://www.statista.com/statistics/250577/domestic-market-share-of-leading-us-airlines/.



Industry Life Cycle. The airline industry as a whole is in the maturity stage. The industry is still growing, but not at the rate that it once did. That being said, it it showing no signs of declining in the near future. The airline industry is here to stay, unless a greener method of fast travel comes along. Until that day, the airline industry will remain in the maturity stage.

The airline industry is a standard-cycle market, which means that "the firm's competitive advantages are partially shielded from imitation, and imitation is moderately costly." There are only so many ways to differentiate oneself in the airline industry. Differentiation strategies can be implemented after a decent amount of time, but are not as cheap to replicate as a fast-cycle market. That being said, they can be imitated faster and at a lower costs than the slow-cycle market. Southwest's low costs structure set helped to set them apart for years as companies unsuccessfully tried to imitate them, but it has been achieved by JetBlue. The fact that it can be replicated is a sign that the industry is a standard-cycle market.[1]

Porter's Five Forces Model.

Threat of New Entrants - *Barriers to Entry.* The barriers to entry are high for new entrants into the airline industry. For one, startups are not able to even come close to the *economies of scale* that big airlines have. Secondly, *product differentiation* is difficult to achieve for new airlines. Snacks, internet access, friendly service, and free movies, which were once perks of choosing specific airlines, are now expected by most passengers. Most differentiation techniques become commodities before too long. Thirdly, new entrants will not have the same *access to distribution channels* as legacy carriers. The prices that suppliers offer to new entrants are typically higher due to relationships with older customers as well as how much bulk bigger companies can afford to buy in. Fourthly, there are many *cost disadvantages* for new entrants. Starting an airline is not cheap. Fuel prices make up nearly half the cost of running an airline and are getting more expensive each year. With limited space in airports, the entrenched companies have already secured the prime locations, and any new locations that pop up are bound to be snatched up by the highest bidder (which is probably a legacy airline). Fifthly, *government policy* makes starting a new airline difficult. Although much better than it once was, airlines are still much more regulated than the average industry. These high regulations can keep new entrants grounded until they meet the necessary government regulations. Ultimately new startups face extremely high costs, limited space, and tough competition. These factors make the threat of new entrants extremely low.[12]

Expected Retaliation. Airlines do not like new competition, so they do all they can to eliminate new entrants as soon as possible. A good portion of the few startups that make it past their first five years get bought up by bigger airlines. Many airlines do all they can to make sure new entrants never get started at all. To illustrate, Southwest had to go to court twice to get approval to start flying due to roadblocks placed by their competitors. With low margins being a standard in the industry, established airlines will do anything to keep new entrants from stealing more of their market share. The expected retaliation also helps to drive down the threat of new entrants.[1]

Bargaining Power of Suppliers. There are very few suppliers for the airline industry. In fact, there are only eight major airline manufacturers. These manufacturers are Airbus, Boeing, Bombardier, Dassault, Embraer, Gulfstream, Pilatus, and Textron. These manufacturers supply almost all of the commercial airplanes today. Because of the few suppliers, price competition is relatively low, which means that the costs of airplanes remain relatively high. Naturally, there are no substitutes for an airplane to the airline industry. Airlines must buy from one of these companies in order to do their job. This means that the bargaining power of suppliers is extremely powerful in the airline industry.[13]

Bargaining Power of Buyers. Like any industry, airlines want to be able to keep as many customers as possible and build customer loyalty. However, buyers do not hold much power over the airline industry. Everybody needs to fly in today's culture. Vacations, business trips, and family visits are commonplace in our society. The alternative to flying could mean days in a car or a train. Because flying is a necessity, customers must go to the few airlines that exists in order to have their needs met. On top of this, Southwest has the advantage of being the low-costs provider in many markets, which drives switching costs up and only further dwindles the bargaining power of buyers. Ultimately, the bargaining power of buyers is low for the airlines industry.[1]

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[12] Mouawad, Jad. "The Challenge of Starting an Airline." The New York Times. The New York Times, May 25, 2012. https://www.nytimes.com/2012/05/26/business/start-up-airlines-face-big-obstacles.html.

[13] Bjtonline. "The Major Airplane Manufacturers at a Glance." Business Jet Traveler, March 28, 2019. https://www.bjtonline.com/business-jet-news/the-major-airplane-manufacturers-at-a-glance.

Threat of Substitute Products. The threat of substitute products is very high in the airline industry. The alternatives to flying are driving, riding in a boat, or riding in a train (depending on the destination). Most of the time, these alternatives take much longer and after food and hotels end up being more expensive anyway. Since there are no real alternatives, people must stick to flying. Naturally, there is only so many ways to differentiate ways to fly a plane, so almost all airlines can be substituted for another (minus a couple of unique perks that come with each airline). The lack of differentiation make substituting one airline for another simple, which makes the threat of substitute products high.[1]

Intensity of Rivalry Among Competitors. Competition in the airline industry is extremely intense. For one, there are several *competitors that are equally balanced*. Besides Southwest, companies like American, Delta, and United have similar market shares and are equally balanced for the most part. Secondly, *industry growth* is moderate. Because the industry is not booming, competitors become more scrappy over fewer customers. Thirdly, there are very *high fixed costs*. As mentioned earlier, fuel costs are only going up, which makes up half the costs of running an airline. Fourthly, there is *lack of differentiation and low switching costs* for airlines. Fifthly, there are *high strategic stakes* as each airline must maintain there market in order to stay afloat. Sixthly, there are *high exit barriers*. Once an airline company starts up, chances are they will remain an airline until they close down or are bought out. All of these factors combine to make intensity of rivalry among competitors extremely high.[1]

Company Analysis

Vision/Mission/Strategic Intent. Southwest's vision is "To become the world's most loved, most flown, and most profitable airline." They intend to be profitable while not sacrificing quality service. Their mission is "dedication to the highest quality of Customer Service delivered with a sense of warmth, friendliness, individual pride, and Company Spirit."[14] They strive to be extra friendly and to give their customers what they want.

Current Goals/Objectives. Southwest's goals is to be as profitable as possible while providing the best possible service to customers. They have a strong focus on providing the best customer service as well as bringing in plenty of money for their shareholders. They also strive to treat their employees fairly and provide them with competitive wages.[14]

Strategies. Southwest's strategies include having a robust route network. They are carrying the most US passengers out of all their competition and have the most daily departures in the world. Secondly, their strategy is to have compelling brand appeal. They strive to have the best customer service possible to keep customers coming back. Thirdly, their strategy is to be in the

[14] "Purpose, Vision, Values, and Mission." – Southwest Airlines. Accessed October 1, 2019. http://investors.southwest.com/our-company/purpose-vision-values-and-mission.

most superior financial position. They strive to have a competitive cost advantage in order to return as much to the shareholder as possible.[15]

Philosophical/Value Base. Southwest has two values, to live and to work the "Southwest Way". To Live the Southwest Way means having a warriors spirit, a servant's heart, and a fun-loving attitude. To work the Southwest Way means working with safety and reliability, with friendly customer service, and with low costs.[14]

Core Competency/Competitive Advantages. Southwest's competitive advantage lies within their affordable prices and their extraordinary customer service. As mentioned earlier, when Southwest enters a market prices tend to drop. This affect has occurred so many times that it has been coined the "Southwest Affect". The Southwest Affect exists because of Southwest's extremely low prices. These low prices attract more customers which consequently grows their market share. Another core competency Southwest possesses it their unparalleled customer service. Southwest always will try to go above and beyond whenever possible. Southwest employees have even been known to dog-sit for owners who forgot their dog crate and let people stay at their house when they had no one else to stay with. Southwest strives to maintain this distinct competitive advantage.[1]

Unfortunately these core competencies may not be sustainable. Lower prices and more friendly customer service are beginning to become commodities in the airline industry as competitors are attempting to mimic Southwest. JetBlue appears to have successfully mimicked Southwest's strategy perfectly. If JetBlue can do it, others certainly can too. Unless Southwest can find new core competencies or hold off their competitors, they will eventually lose their competitive advantage.

SWOT Analysis.

Strengths	Weaknesses
• Superior Customer Service • Low Costs Structure • Low Prices • Quick Flight Turnaround	• Fewer Markets than Most Competitors • No Hubs • Limited International Travel

[15] "Proven Business Strategy." – Southwest Airlines. Accessed October 1, 2019. http://investors.southwest.com/our-company/proven-business-strategy.

Opportunities	Threats
• Chance To Grow Market Tremendously with AirTran Acquisition • Acquisition Creates International Opportunities	• Acquisition Could Cause Southwest to Lose Their Unique Culture • Rising Costs Could Drive Up Prices and Cause Southwest To Lose Price Advantage • Competitors Imitating Southwest's Costs Structure • Costs Structure Could Become Obsolete with Addition of Hubs and Bigger Planes

Porters Value Chain

Supply-Chain Management. Southwest does an excellent job of supply chain management. Southwest only flies one kind of plane, the Boeing 737, in order to reduce costs. By specializing in one kind of plane, Southwest is able to get better deals on that plane because they can buy in bulk. On the other hand, most companies buy several different kinds of planes, and by doing so miss out on specific bulk pricing. On top of the potential for bulk pricing, the use of the 737 cuts costs because of its size. Boeing 737's are relatively light, small planes. This cuts the costs of fuel significantly. These factors contribute to Southwest having such a low costs structure.[1]

Operations. Southwest also does an excellent job in their operations. As mentioned earlier, their flights have an excellent turnaround time. Once a plane lands, it is able to get back in the air much faster than many other airlines. This strategy allows Southwest to fly less planes while maintaining the same number of flights. By flying less planes, they have less overhead to account for. This strategy is yet another part of Southwest's ability to make flying cheaper for the average person.[1]

Distribution. Southwest's distribution is run like most airline companies. Distribution in the airline industry refers to how airlines manage their gates. Gate management is usually pretty standardized in the airline industry, and Southwest runs theirs no differently, except for the possibility of better customer service from a Southwest gate.[1]

Marketing. As discussed before, Southwest has long held an advantage in selling tickets over the airline industry because they were the first airline to open a website. This website allowed customers to buy tickets online. Although you can purchase a ticket online from almost any airline, Southwest differentiated themselves by being the first mover on a new ticket selling technique. Southwest proved that they are not afraid to try different ways to make the customer experience as simple and as easy as it can possibly be. Besides doing all they can to make the customer experience simple, Southwest has built strong brand recognition. The brand recognition has helped to build customer loyalty, which has further increased sales. These two factors have given Southwest an advantage in marketing.[1]

Follow-up Service. Follow-up service in the airline industry is almost non-existent, except for an occasional survey sent to the customer's email. In this regard, Southwest runs their follow-up service very similar to the rest of the industry. Surveys are customarily sent out to customers who have given their email addresses to Southwest (which includes every customer who bought their ticket online). Once the survey is filled out, Southwest will take the customer's recommendation into account to see what they can change in the future.[1]

Finance. Southwest has a major advantage in terms of their finances due to their low costs structure. They have operated on the lowest unit costs for years. However, in recent years costs have risen at rates much higher than the industry average. Unless change is taken, Southwest's unique cost structure might be at risk. These factors will be discussed in greater detail in the Case Analytical Insights section.[1]

Human Resources. Southwest's Human Resources department does an excellent job of hiring employees. The average Southwest employee is more pleasant than the typical airline employee and will go out of their way to ensure customers enjoy their flight. The Human Resources department is responsible for hiring and training the best candidates for employment. By doing so, they deserve all the credit for the friendly environment that Southwest employees help to create.[1]

Management Information Systems. There is a lot of information that must be managed for the airline industry. Customer information, flight times, logistics for employees, fuel, and planes, customer baggage tracking among connecting flights, and so on. Airlines require advanced information systems to keep track of all this information among thousands of flights that take off daily. Southwest has sophisticated technology that allows them to be able to keep track of all of these moving parts. In doing so, they assure that customers get to where they want to go with their luggage in a timely fashion.[1]

Strategic Analysis

Corporate Level. As discussed earlier, Southwest bought out AirTran in 2010. The acquisition came at a costs of $1.4 billion. The acquisition allowed Southwest to expand their reach into over 30 new markets. The purchase of AirTran also gave Southwest access to a couple of new international cities in Mexico and the Caribbean. However, Southwest has maintained that the new access to foreign markets will not distract them from their current strategy. They are determined to focus on their domestic markets for the next couple of years. They will continue to invest in expanding internationally once the full acquisition with AirTran is successful.[1]

Business Level. Southwest operates under a mixed, or "stuck in the middle", category. Unlike most companies in the mixed category, Southwest manages to do it well. For one, they are one of the cheapest airlines in the industry, which could put them in the cost-leadership category. But the prices are not the only thing Southwest has going for them. Southwest is also known for their excellent customer service. They go above and beyond whenever the opportunity arrives. Their extremely friendly customer service could put them in the differentiation category, but combined with their cost-leadership they get put into a mixed group. This "stuck in the middle" approach has given Southwest the best of both cost-leadership and differentiation, which has allowed them to become a leader in the airline industry.[16]

Cultural Assessment. Southwest's culture is unique. Their culture is made up of three values: Work should be fun, enjoy it; Work is important, don't spoil it with seriousness; and People are important, teaching one makes a difference. Employees are encouraged to enjoy their work and keep up a fun environment. Employees are also encouraged to train others whenever they need to. Most companies lack these lighthearted culture aspects and instead focus on making as much money as possible. These values have allowed Southwest to create a unique culture that focuses on customer service while keeping up a relaxed atmosphere.[16]

Organizational Structure. Southwest's organizational structure closely resembles that of a Functional Structure. At the top sits the President, CEO, and COO. Below them sits Executive Vice Presidents, followed by Senior Vice Presidents, followed by Vice Presidents, and so on. Each President is in charge of a certain department and is in charge of several lower-level presidents beneath them. It most closely resembles to Functional Structure for Implementing a Differentiation Strategy in the book *Strategic Management.*[17]

Firm Leadership. Southwest Airlines is led by Gary C. Kelly, the Chairman of the Board and CEO. Kelly has been instrumental in Southwest's success. He "has pioneered the airline's transformation through several major initiatives, including the acquisition of AirTran Airways, the repeal of the Wright Amendment, the launch of international destinations for the first time in Southwest's history. . . all while staying true to the Company's core values and People-centric Culture." Kelly has help make Southwest one of the top airlines in the country. All major initiatives and new plans must first get approval from his desk. Kelly is extremely important in Southwest's strategic management.[18]

Functional-Level. Southwest has been able to become so successful because they are have superior qualities in several areas. For Production, Southwest has created a superior network for getting flights off the ground in a timely manner. Their flights are "primarily short-haul (less than 500 miles), point-to-point, a fleet consisting of only Boeing 737s [relatively light, small planes],

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[16] Quick, James Campbell. 1992. "Crafting an Organizational Culture: Herb's Hand at Southwest Airlines." *Organizational Dynamics* 21 (2): 45–56. doi:10.1016/0090-2616(92)90063-S.

[17] "Senior Management Committee." Southwest Airlines Newsroom. Accessed October 1, 2019. https://www.swamedia.com/executives.

[18] "Gary C. Kelly." Southwest Airlines Newsroom. Accessed October 1, 2019. https://www.swamedia.com/pages/gary_kelly.

high frequency flights". This strategy allows them to land, refuel, and get back in the air faster than most other airlines.

For Marketing, Southwest has done an excellent job of selling people tickets through their website. As discussed previously, Southwest was the first airline to have a website, and their website is now the main source of selling tickets. Southwest's ability to see what people want drove them to create a very successful website.

Southwest has created superior value in Human Resources by their excellent recruiting. Southwest employees are each handpicked by the Human Resources department. These employees must be outgoing and friendly in order to fit in with Southwests's commitment to customer service. By hiring better employees, Southwest ensures that more customer will be satisfied with their flights.

Southwest has created superior value in their Finance department through their low costs structure. Their unit costs is one the the cheapest in the industry, and their unit costs without labor is by far the cheapest in the industry. These factors will be covered in greater detail in the Case Analytical Insights section.[1]

Strategy Formulation

First, I would recommend for Southwest to focus on ensuring the AirTran integration into Southwest goes smoothly. Southwest's biggest issue at this point in time appears to be the merger with AirTran. The merger is not a bad thing by any stretch, but it does pose several risks. The rapid expansion might cause Southwest to lose some of their culture as well as their low costs structure. By flying different planes that AirTran previously flew instead of the standardized 737's, Southwest potentially could lose a differentiation strategy that allowed them to cut down on costs as well as ensure fast flight turnarounds. The list of potential threats goes on. In order to avoid these threats, Southwest needs to take things slow and focus on integrating AirTran. This means that Southwest should not focus on expanding their fleet into new markets, but focus heavily on AirTran's markets to ensure they can adopt the "Southwest Way". Southwest might have to train AirTran employees on how Southwest operates and how they are expected to treat customers. The AirTran employees need to adopt Southwest's culture and be fully sold out for their new company. Any employees who do not get on board need to be let go and replaced with people who are a good fit. The AirTran acquisition has the potential to break Southwest, so they need to make sure it is done properly.

Secondly, once everything appears to be going smoothly after taking over the fleet and flight plans from AirTran, I would recommend for Southwest to start to integrate the AirTran brand into the Southwest brand. AirTran needs to disappear to be replaced by Southwest. Uniforms need to be replaced, gates need to be redesigned, planes need to be repainted, and so on. The AirTran brand must be fully replaced by Southwest in order for people to not differentiate the two brands. By integrating the two brands together, Southwest does not have to worry about maintaining the perception of two separate brands. Southwest should not have to compete with themselves.

Thirdly, I would recommend to start expanding again after the AirTran acquisition has been completed. Once AirTran's markets become synonymous with Southwest, it is safe to start expanding again. With new access to foreign markets thanks to AirTran, Southwest can increase its international presence. Start with tourist markets (Cozumel, Falmouth, Havana, etc.), then move to big markets that exist in Mexico and Canada. However, do not expand too fast into international markets. Focus on big cities that have high travel rates. These markets have a much higher chance of success and create customer awareness in these countries. Once Southwest becomes a household name in these countries, it will be safer to move to smaller markets. The key to success is to take international expansion slow.

Fourthly, I would recommend for Southwest to start opening hubs. As will be discussed in the case analytical insights, it is clear that Southwest's low costs model is not as effective as it once was. Although Southwest still operates on the lowest costs in the airline industry (only falling behind Delta), Southwest's costs are increasing much faster than the industry average. Opening a hub appears to be a viable way to cut costs. Granted, Southwest would lose their advantage of quick flight turnaround times and would have to integrate a new system to deal with the new flight patterns, but it would end up saving money in the long run. The rising costs are telling us that Southwest's way of doing things is becoming obsolete. Hubs would help cut those costs back down in the long run. The point to point system just does not work as effectively in today's market as it used to.

Fifthly, I would recommend for Southwest to invest in better in-flight entertainment that is free for the customers [this point is for 2013 Southwest, back when entertainment had to be bought on every airline]. Customers who fly long distances want to be entertained. By providing customers with free entertainment, Southwest would gain customer loyalty as well as differentiate themselves from among the competitors. Free wireless internet, movies, and TV shows would costs Southwest money; but proving these services would pay off. Customers would flock to an airline that not only had some of the cheapest prices but also provided free entertainment. Eventually this differentiation would become a commodity across the industry, but in that time Southwest could develop lifelong customer loyalty.

Case Analytical Insights

Exhibit 2. Southwest maintained some of the highest operating margins compared to all major US airlines for years. However, Southwest's margins dropped in 2007, 2008, and 2009, but started climbing again in 2010. Unfortunately, they were no longer the leader, but were tied at a little over 8% with United and US Airways. Delta held a strong lead in operating margins with over 12%.

Exhibit 3. Southwest has by far the lowest average RPM's per passenger (also know as average mileage per passenger flight) for major US cities. Most flights were around 900 miles in 2010. The closest competitor, US Airlines, had an average of a little under 1,150. These low numbers are due to Southwest's strategy of shorter flights. However, these numbers for Southwest have been steadily climbing since 2002, which is mirrored across the entire industry. This is probably due to continued expansion for Southwest and is nothing to be alarmed about.

Exhibit 4. Southwest also was a leader per RPM (computed by dividing passenger revenues by revenue passenger-miles) in 2010. The numbers were steadily climbing until 2009, when the entire industry took a hit due to the recession. However, the industry shot back up in 2010, with

Southwest far outpacing their competitors. Southwest was clocking in around 14.75 cents in 2010, while American, the closest competitor, only had around 13.75 cents in the measurement.

Exhibit 5. Southwest has also maintained the lowest load factor out of all the major US airlines. The load factor is a measure of the stress put on the plane by passengers and luggage. The load factor has been increasing across the entire airline industry since 2002. However, Southwest's load has been growing much faster than the industry average. In 2002, Southwest's load was nearly six percent less than the closest competitor. By 2010, Southwest was around four percent away from the closest competitor. If Southwest's load factor continues to grow at this rate, they will soon by passing many of their competitors.

Exhibit 6. For years, Southwest's unit costs was far lower than any of their competitors. in 2002, Southwest unit costs in cents were around 7.5 cents, and the closest competitor was at about 9.4 cents. Southwest had such a large advantage due to their low costs structure. However, Southwests unit costs has been rising at an alarming rate. By 2010, Southwest came to about 11.1 cents, and was just beat out by Delta, which sat at around 11 cents. Although Southwest remained one of the lowest out of the US major airlines, the high growth rate for the unit costs was much more than all of the existing airlines.

Exhibit 7. The story for unit costs without labor is very similar to the unit costs paragraph above. Industry costs have been rising across the board. However, Southwest's unit costs without labor grew as a slower rate than the normal unit costs. From 2002 to 2010, Southwest went from around 4.5 cents to around 6.7 cents. Southwest remained the lowest in the industry for unit costs without labor in this time period.

Exhibit 8. Total labor costs per ASM (available seat miles) were in flux in the airline industry from 2002 to 2010. Many airlines bad dropping labor costs while some had growing labor costs in the same time period. For the most part, however, the industry saw total labor costs drop from 2002 to 2006, and begin to increase from 2007 to 2010. During this same period, Southwest has actually seen consistent price increase, with a slight drop that held steady from 2004 to 2008. By 2010, Southwest had the second most expensive labor costs in the industry. Southwest's labor costs are so high because Southwest strives to treat their workers better than most other airlines. In doing so, they raise their total labor costs.

Exhibit 9. Because Southwest is paying their employees so much, they higher fewer workers. While most airlines have held a steady number of workers per plane, Southwest has been decreasing the number of employees per plane since 2002. In 2002, they had a little less than 9 employees per plane, and by 2010, the number was down to a little over 6. Southwest has been decreasing the number of employees per plane to maintain their low costs structure and avoid any unnecessary expenses.

Exhibit 10. Most airlines are in debt at any given point, and most airlines tend to keep the same amount of debt they have. From 2002 to 2010, most airlines debt levels hovered around the same place. During this same time, Southwest was the only airline to maintain no debt. During the recession, Southwest incurred some debt, but by 2010 all debt was completely paid off. Most airlines carried a tremendous amount of debt during this time period. Southwest has done an excellent job of maintaining excellent financial records in their history.[1]

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