

Basic

Advanced

Topics

Publications

 My Research

Interface language:

[Databases selected:](#) Multiple databases...
**Document View**<< [Back to Results](#)

Document 1

[Publisher Information](#) Print Email

Mark Document

 [Abstract](#) ,  Full Text
**THE WALL STREET JOURNAL.**
**Head Winds: Move to Denver Signals Threat To Southwest's Low-Cost Model; Lean Rivals Match Its Fares Into High-Fee Airport; No Frills vs. Full Service; A Hug From the 'Junior Team'**

*Susan Warren*. [Wall Street Journal](#). (Eastern edition). New York, N.Y.: [Nov 29, 2005](#). pg. A.1

» [Jump to full text](#) 

» Translate document into:

» [More Like This](#) - Find similar documents

Author(s): [Susan Warren](#)

Publication title: [Wall Street Journal](#). (Eastern edition). New York, N.Y.: [Nov 29, 2005](#). pg. A.1

Source type: Newspaper

ISSN/ISBN: 00999660

ProQuest document ID: 932862611

Text Word Count 2040

Document URL: <http://proquest.umi.com.ezp1.harvard.edu/pqdlink?did=932862611&sid=1&Fmt=3&clientId=11201&RQT=309&VName=PQD>

**Abstract** (Document Summary)

For some Denver travelers, that's reason enough to stick with the airlines they've grown used to flying. "My premium status, more leg space -- I wouldn't easily give that up just to save a few bucks," said veteran flier Ellen Cervarich, who was waiting to board a United flight to Chicago in Denver recently. Ms. Cervarich noted that when Southwest posted its new low fares to Chicago, "Within two days, United matched. So there was no need to change to get a low fare."

When Southwest's four-person team swept into town July 11, Denver officials were at first deflated. The Denver officials, clad in dark suits and ties, were surprised to see the Southwest crew dressed in golf shirts and khakis. "I don't think anybody was over 35" years old, says Thomas Clark, head of economic development for Denver. "I thought, 'OK. They've sent the junior team.' "

"Pricing is Southwest's big advantage," notes Frontier spokesman Joseph Hodas. "Take that away, and what do they have?" Frontier immediately matched Southwest's introductory Denver fares, and Mr. [Jeffery Potter] maintains the airline can make money at the lower prices.

#### Full Text (2040 words)

*Copyright (c) 2005, Dow Jones & Company Inc. Reproduced with permission of copyright owner. Further reproduction or distribution is prohibited without permission.*

DENVER -- Southwest Airlines has prospered by targeting new cities where the competition is weak and the costs are low. But when it starts flying out of this city in January, success won't be so easy.

Southwest will be going up against two entrenched carriers: Frontier Airlines Inc., a rival low-cost carrier based in Denver; and a newly streamlined United Airlines, which controls nearly 60% of the Denver market, and is set to emerge from bankruptcy early next year.

While Denver International Airport has dramatically reduced airline fees in recent years, the city will be one of the most expensive that Southwest serves. Southwest estimates its airport fees here will run between \$8 and \$9 per passenger, compared with a systemwide average of \$5. That's high for an airline that's begun offering tickets for Denver flights at introductory fares as low as \$59 each way.

Southwest is weathering the industry's financial crisis better than most other U.S. carriers, and is determined to use that advantage to strengthen its market position before the rest of the industry recovers. It has posted an unbroken string of profitable quarters even as other airlines racked up hundreds of millions of dollars in losses. With Denver, it will be entering its third new city in eight months, its fastest expansion pace since 1999.

But Southwest's days as an industry upstart may be drawing to a close. When it began flying in 1971, it terrorized established carriers with rock-bottom fares made possible by no-frills service and shrewd use of secondary airports. But hard times are driving big changes in the industry. With other airlines slashing costs both inside and outside of bankruptcy court, Southwest is losing its industry lock on low fares.

To cope with higher costs and leaner rivals, Southwest is adjusting its distinctive formula. Moving into Denver is one of the bigger risks the airline is taking as it tries to grow before other airlines catch up. "The low-hanging fruit is gone," notes Stuart Klaskin, an industry consultant based in Coral Gables, Fla. "There are only so many markets that are underserved and overpriced, and those markets shrink every day because somebody else is coming to serve them."

One of Southwest's main cost advantages over other airlines is likely to melt away over the next few years. When oil prices were low, Southwest shrewdly executed extensive fuel hedges to lock in low prices. For the past 18 months, the benefits have been huge, but they will shrink steadily over the next five years. If oil prices remain high, Southwest

won't be able to negotiate new hedges at attractive prices, bringing its fuel costs more in line with other airlines.

"We've bought ourselves time," Southwest Chief Executive Gary Kelly said in a recent interview. "The advantages we have are immense, and shame on us if we squander them."

Mr. Kelly plays down the difficulties in Denver. He notes that Southwest already competes effectively against other discount carriers in cities such as Phoenix and it flies out of big airports with lots of competition, such as Los Angeles International. "This is not extraordinary for us," he said. "We're a growing airline, and we're very disciplined. It's just what we do."

Frontier and United already have matched the low fares Southwest announced for its flights between Denver and Phoenix, Las Vegas and Chicago, which are scheduled to begin on Jan. 3. With comparable fares, passengers will be choosing between no-frills Southwest and two airlines that unlike Southwest offer assigned seating and premium features such as first-class sections, more legroom and in-flight entertainment.

For some Denver travelers, that's reason enough to stick with the airlines they've grown used to flying. "My premium status, more leg space -- I wouldn't easily give that up just to save a few bucks," said veteran flier Ellen Cervarich, who was waiting to board a United flight to Chicago in Denver recently. Ms. Cervarich noted that when Southwest posted its new low fares to Chicago, "Within two days, United matched. So there was no need to change to get a low fare."

Frontier and United both will see their financial results squeezed by a fare war with Southwest, airline analysts say. Mr. Kelly argues that his airline's low cost base gives it more "staying power" in a low-fare environment. In other words, Southwest hopes to outlast competitors who may not be able to sustain the rock-bottom fares.

Southwest's operating cost, as measured by each seat flown one mile, is a low 7.85 cents. That compares with 8.68 cents per seat mile for Frontier and 10.43 cents for United, in the most recent quarter. But if fuel prices come down, that advantage could shrink. Excluding fuel, Southwest's cost is 6.31 cents per seat mile, compared with Frontier's 5.86 cents and United's 7.11 cents.

Denver, which opened a new airport in 1995, had been courting Southwest for decades. But the airline was deterred by the relatively high fees Denver charged for the use of runways, gates and other facilities, due in part to the debt Denver incurred building the new facility. Airport co-manager Vicki Braunagel eventually led a campaign to pay down debt, freeze staff levels and defer big capital projects like a new parking garage and hotel, which allowed the airport to reduce costs to airlines.

Southwest was too busy expanding along the East Coast and Florida to reassess Denver until recently. Its planning department was gearing up its search for new cities to serve in 2006, and Denver already was on a shortlist, says Mike Van de Ven, Southwest's executive vice president of aircraft operations. Lower airport costs, coupled with Southwest's need to grow by expanding into large new cities, quickly moved Denver up the list.

In June, Southwest surprised Denver by accepting an invitation to send a research team to the city. Denver airport officials scrambled to prepare for Southwest's visit, dubbing it "Project Longhorn" in line with the secrecy Southwest demanded.

When Southwest's four-person team swept into town July 11, Denver officials were at first deflated. The Denver officials, clad in dark suits and ties, were surprised to see the Southwest crew dressed in golf shirts and khakis. "I don't think anybody was over 35" years old, says Thomas Clark, head of economic development for Denver. "I thought, 'OK. They've sent the junior team.' "

Mr. Clark changed his mind when the Southwest team began pelting Denver officials with detailed questions about economic growth and plans for development in the region. What are the demographics for winter skiers? What kind of conventions do you have planned for the next five years? "These are questions we've just never been asked by an airline before," said Mr. Clark.

When they were ready to leave, Southwest representatives told Denver officials that they loved Denver, recalls airport marketing manager Sally Covington. The Southwest team even hugged the city officials. But there were no promises about when -- or if -- Southwest would return.

The next month, Hurricane Katrina demolished the airline's careful planning. Southwest had been running 57 flights a day to New Orleans. The storm knocked out most air service to the city, leaving Southwest with 15 jets sitting on the tarmac, unable to generate revenue.

One possible solution was to quickly launch a new city to take up the slack. Ordinarily, Southwest needs six to nine months between announcing service to a new city and beginning flights. To further complicate matters, a strike at Boeing Co. threatened to delay the delivery of new airplanes Southwest had ordered for 2006. If Southwest didn't get those planes, the idled New Orleans fleet might not be available to use in a new city.

On Sept. 29, the month-long Boeing strike was resolved. Bob Montgomery, Southwest's vice president of properties, was dispatched immediately on a two-week tour of the top five airports on Southwest's secret expansion shortlist. Mr. Montgomery arrived in Denver on Oct. 7 to assess whether the airport could support a quick start-up. He found that most of what Southwest needed -- terminal space, gates, baggage handling -- was already in place.

By the following week, Mr. Montgomery had narrowed the list to two cities. One of them was Denver. Southwest's planning team crunched numbers and concluded the airline could keep costs in Denver to less than \$9 a passenger. Although that was considerably higher than the \$5 systemwide average, it was less than the \$10 Southwest was paying in Seattle. The airline figured that despite the presence in Denver of low-cost Frontier, it could set fares 30% to 50% lower than rivals for certain routes, and still make money.

There was one last consideration about the timing. New cities can take 12 months to become profitable for Southwest. Absorbing the costs of a Denver start-up in one calendar year, rather than spreading them over two, would make it harder for Mr. Kelly to meet his goal of 15% earnings growth in 2006.

In the end, Mr. Kelly decided 15% growth was still achievable, and that rushing Denver was worth the risk. On Oct. 20, he announced that Southwest would launch service to the Mile High City, beginning in January. One week later, Southwest began selling tickets.

Frontier Chief Executive Jeffery Potter caught wind of Southwest's move the night before the announcement, he recalls. Mr. Potter knew that other airlines, including Alaska Airlines, had successfully competed against Southwest in some cities, and felt reassured that Frontier compared favorably to those airlines, he says.

Southwest has a near-mythic reputation in the industry as an airline that usually can't be beat. Airlines far bigger than Frontier, including US Airways Group, had decided to cut back service to cities that Southwest entered.

Mr. Potter stayed late at his office composing a letter to rally his employees. "We are not about to cower or back away," Mr. Potter wrote, assuring his employees that "not everything you have heard about Southwest is necessarily true."

In an interview, Mr. Potter argued that fliers will prefer Frontier's extras, such as more legroom in its seats and

personal television screens that offer programs and onboard movies for a fee. He maintained that fliers are turned off by Southwest's first-come- first-serve seating, which sometimes results in long lines of passengers waiting to board.

"Pricing is Southwest's big advantage," notes Frontier spokesman Joseph Hodas. "Take that away, and what do they have?" Frontier immediately matched Southwest's introductory Denver fares, and Mr. Potter maintains the airline can make money at the lower prices.

Mr. Kelly contends that Southwest's battle-tested approach will continue to work in Denver, even if there is no difference in fares. Southwest's core advantage is its performance, he argues. Southwest has a long record of superiority in categories such as on-time flights, baggage handling, frequency of complaints and canceled flights.

In recent years, though, low-cost rivals have been beating Southwest in some categories. Frontier, for example, had a better on-time record in the third quarter than the much larger Southwest, according to Department of Transportation data.

Mr. Kelly says Southwest won't be resting on its laurels and is willing to make changes to stay competitive.

United executives also are working out a response. Like other traditional airlines, UAL Corp.'s United has slashed costs and reduced domestic service to concentrate on expanding overseas. It posted its biggest loss ever in the third quarter, but that was due to \$1.84 billion in restructuring costs as it prepares to exit bankruptcy in the spring. Now, United is expecting to turn profitable by the end of 2006.

Sean Donohue, a United vice president in charge of its Ted Airlines discount operations, contends that Denver customers of both Ted and United will remain loyal, partly because of United's frequent-flier program. Accumulating mileage on United allows passengers to fly all over the world, while on Southwest, "you can go to Lubbock or Amarillo," Mr. Donohue snipes. Southwest now flies to 61 cities nationwide.

Southwest still has the lowest costs of any major airline. But Mr. Donohue notes that other airlines have been bringing costs down, reducing Southwest's advantage.

"I'm not trying to be arrogant here in saying Southwest is not a fierce competitor, because they are," says Mr. Donohue. "But things are changing. And things are changing pretty significantly."

#### More Like This - Find similar documents

Author(s): Susan Warren  
Language: English  
Publication title: Wall Street Journal

[^ Back to Top](#)[<< Back to Results](#)

Document 1

[Publisher Information](#)

Mark Document

 ,

[Text-only interface](#)

