Calabash Case Notes - Draft

Case: Southwest Airlines 2005
Case #: A07-05-2006
Thunderbird: The Garvin School of International Management

Case Notes

■ Section: Introduction (p. 1)

01. **Breakeven Point:** SWA is a profitable operation. This indicates that the company is operating past the breakeven point (i.e., TR > TC). [para.1]

02. **External Environment - Economic Environment (CERTS):** The economic environment is one of recessions, energy crises, and September 11 terrorist attacks. The 911 attacks could also be viewed as part of the Social environment, in that while the attacks had an impact on the economic environment of the time, it also affected and is rooted in the social/cultural environment. [para. 1]

    The external environment in which a firm operates consists of the following primary categories **-** Competition, Economic Environment, Regulatory Environment, Technological Environment, Social Environment (CERTS). The latter environment, S, deals with the cultural and political nature of the environment.

03. **Market Development:** The company expanded into Philadelphia (PHL) in 2004 and planned to enter Pittsburgh (PIT) in 2005. Both of these actions reflect the Market Development cell of the Marketing Opportunities Matrix - same product, new market). [para. 1]

04. **Alliance:** Entering into a code sharing arrangement with ATA Airlines is a form of alliance with a competitor. Code sharing means that the airline's identifier (e.g., SW, AT, will show up in flight schedules, and on tickets, even though the flight is operated by the other airline. This allows the involved companies to provide a flight at a given time but avoid duplicating the service. An alliance is an agreement between independent firms to co-operate in some way.

    It is interesting that this agreement was formed, since in the past the two airlines refused to recognize the other's tickets and they did not allow "interlining" between the airlines on the tickets they accepted (i.e., you could not have a single ticket coupon for a flight listing both airlines - such as a flight on SW from Detroit (DTW) to Chicago and then connecting to a flight from Chicago (MDW) to Los Angeles (LAX) on ATA). [para. 1]

05. **Efficiency:** The steps taken by SW to become more productive means it became more efficient (Efficiency deals with the relationship between inputs (e.g., man-hours) and output (e.g., number of passengers processed in an hour). One can attempt to increase the output or reduce the input; either approach will lead to an increase in efficiency. [para. 1]

06. **Average Cost:** The reduction in operating costs per unit means that the average cost of operating is lower. Average cost is Total Cost (TC) divided by Units, whatever unit dimension is being used (e.g., number of passengers, revenue miles). Total cost consists of Fixed Costs and Variable costs. [para 1].

■ Section: The U.S. Airline Industry

07. **External Environment - Regulations (CE<u>R</u>TS):** Deregulation deals with the laws or regulations that exist in the environment. [para. 2]

08. **Monopoly, Duopoly, Monopolistic Competition:** The economic structure of the environment varied prior to deregulation. In those markets with one airline, there was a monopoly. In the markets with two airlines, there was a duopoly. In the markets with three airlines, there was monopolistic competition. In the two cases, each firm would use certain aspects of its marketing mix (except price, which was regulated) to attract customers using the strategy of non-price competition (i.e., trying to create a little bit of a "monopoly" based on its uniqueness, even in a duopoly). [para. 2]

09. **Market Segmentation and Target Marketing:** The market for airline travel was segmented at the first level on the basis of economic means (i.e., Can the customer afford purchase the service of air transportation?). Those who could were within the target segment selected as the general target market for the <u>service</u>. Before a customer can be considered to be within a given segment, the customer must be "able" to acquire the product. [Must also be identifiable (measurable) and willing]. [para. 2]

A potential market is first segmented into homogeneous groups based on selected characteristics; then the market decides which segment to go select as the target market(s) for the company - i.e., the group of customers the company want to sell its product or service to. Air transportation is a **<u>service</u>** (intangible) versus a product (tangible). You cannot "touch" a service, only receive the benefits of it, unlike the case with a product.

10. **Elasticity of Demand:** The reduction in airline fares after deregulation indicates that the market was viewed as elastic, otherwise, why would the airlines reduce the fares. [para. 3]

11. **External Environment - Economic Environment:** The fuel crisis, the controllers' strike, and the recession are all aspects of the economic environment. [para. 3]

12. **Breakeven Point/Product-Service Deletion:** The airlines that went into bankruptcy operating below the breakeven point (i.e., Total Cost > Total Revenue) and could not continue to operate (i.e., survive). **Survival** is one of the possible Business Goals of a firm. The removal of the air service from the market reflects the **deletion** stage of product-service development process. [para. 3]

[A business goal is a qualitative statement of what the firm wants to accomplice (e.g., increase sales, increase profit, survive). A business (marketing) objective is a quantitative statement of what a firms wants to accomplish (e.g., increase sales by 10%, increase profit by $2,000,000). A time frame is either implicitly or explicitly included with a business goal or marketing objective (e.g., increase sales by 10% within the next year; open 5,000 more stores within 5 years).]

13. **Horizontal Integration - Intra-Type:** The merger of airlines reflects to what is called horizontal integration (i.e., taking over or joining with another firm at the same level in the channel that are of the same type - e.g. airline vs. airline). Integration is of the "intra-type" nature since it involves a merger of firms that are in the same industry. A drug store competing with a supermarket in the sale of eggs is an example of "inter-type" competition, where the firms are both at the same level in the channel (i.e., retailers), but are in different retail sectors. A merger of firms in the latter case would reflect horizontal, inter-type integration. [para. 3]

To Be Continued