Evaluation of the Customer Management and Relationship Marketing Plan for Southwest Airlines

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Successful firms choose their strategic orientation using a trade-off process (Rust, Lemon & Zeithmal, 2004) to prioritize aspects of their marketing mix in the short and long-term. This marketing mix must balance customer needs and positioning in the market (Best, 2009). Southwest Airlines (SWA), one of the most profitable domestic airlines, has been studied by scholars and practitioners interested in their successful model of value delivery, employee commitment and sustainability. Its dedication to “warmth, friendliness, individual pride, and Company Spirit” (Southwest, 2008) makes SWA an exemplary case of customer management and relationship marketing in action.

This study will address the elements of the strategic orientation of Southwest Airlines through a scholarly approach to assess their choice of marketing strategy (Slater, Olson & Hult, 2006), assess its long-term sustainability, their segmentation and targeting strategies (Weinstein, 2007), value delivery (Parasuraman et al, 1988), their ethical behavior (Freeman, 1988); uses of marketing research (Boguslaski et al, 2004), and the effectiveness of customer relationship strategies (Lacey, 2007). A final section assess SWA theoretical matching and proposes recommendations for best practices for future businesses in the airline industry.

Background

Southwest Airlines (SWA) is a passenger airline operating in the United States, providing point-to-point, low-fare services (Reuters, 2008). Headquarter in Dallas, Texas serves 64 cities in 32 states, operating standardized Boeing 737 aircrafts. Founded in 1967 by Herb Kelleher and Rollin King with the simple principle of getting people to their destination with the lowest cost and in an a fun environment (Middaugh, 2007).
SWA serves short-haul routes with more than 2000 flights per day (Reuters, 2008), more than 100 million passengers in over 1 million flights in 2007, managed by 32,000 employees (Annual report, 2007). Awarded with the Triple Crown for five years in a row for its timeliness, least lost baggage and fewest customer complaints (Quick, 1992). SWA’s mission statement is a real declaration of commitment to their employees acknowledging that through caring and respect, employees will relate to their customers in the same way.

SWA’s revenues of $9.8 billion, operating profit of $791 million and net profit of $645 million in 2007, confirm its profitability. As a leader in low-cost travelling, SWA has the lowest seat mile cost of the industry. Being the only airline rated A in secured debt in 1992 and an impressive market share of more than 65% in the top 100 markets served, complete their outstanding performance (Hallowell, 1996).

Overall Customer Management and Relationship Marketing approach

The customer management and relationship marketing at SWA responds to a decision of creating value for their customers better than their competitors through low cost and using a focused scope of the market (Porter, 1980). Using the typologies of fundamental business strategies, four are the choices for Southwest (Slater et al, 2007): Pioneer, follower, cost-leader and customer centric.

Southwest meets the characteristics of customer centric firms, (Table 1) interested in delivering high value to customers through skilled employees and superior service, and measuring the responses from customers and adapting their offers to those needs (Slater et al, 2005). Success in customer-centric firms is given by their moderate marketing research, focus marketing activities in specific segments, delivering innovative products and durable services, and providing superior service performance.
Table 1  Analysis of Overall Approach to Customer Relationship and Business Strategy

<table>
<thead>
<tr>
<th>Business Strategy</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pioneer</td>
<td>Identifies new products and marketing opportunities, offering innovative products. Have a first-mover advantage</td>
</tr>
<tr>
<td>Fast Follower</td>
<td>Imitates Pioneers successful product and market development but maintains their core of traditional products. Improve pioneers offer</td>
</tr>
<tr>
<td>Cost Leader</td>
<td>Late entrants engaged in aggressive efforts to protect their markets from competitors. Compare their value chain costs with their competitors'. Seek efficiency in value chain</td>
</tr>
<tr>
<td>Customer Centric</td>
<td>Create customer value, offer high quality products, good service at lower prices than Pioneers, but higher prices than fast followers or cost leaders. Create value for buyers and achieve superior performance. Employees are the key in recruitment and training, to provide caring, individualized service to customers</td>
</tr>
</tbody>
</table>

These firms are consistent in their service recruit highly skilled staff to preserve long-term relationships with key customers. Their performance appraisals are based on behaviors grounded in a decentralized decision-making process.

Long-term Viability of the Model

The airline industry in the United States is highly complex, with high barriers of entry based on sophisticated customer segmentation, hub-and-spoke models and costly information systems for reservations (Hallowell, 1996), fare wars and intense competition (Quick, 1992). Unlike the industry, SWA uses a point-to-point system, does not have sophisticated systems or hubs, and tap into niches others overlooked using low-cost strategy. Other low-cost carriers like AirTran and Frontier have remained in the hub-and-spoke model and are now in serious financial problems (Chicago Tribune, 2008).

A heterogeneous mix of long and short-haul in very thin segments, passenger density, and per capita income at end points (Bogulslaski et al, 2004) gives SWA competitive advantage.
At the current rate of expansion, 7.8% of long-haul competitors will see their revenues exposed to SWA and 14.4% by 2014 (Boguslaski et al, 2004).

**Market Segmentation Practices**

Southwest Airlines uses a needs-based segmentation based on attractiveness and profitability consistent with their value proposition of friendliness, reliability and low cost (Hallowell, 1996). Using a three-level process (Weinstein, 2006) is possible to replicate SWA segmentation model (table 2). SWA *relevant market* is comprised of domestic passengers who seek affordable air transportation, the *defined market* are domestic passengers with destination to/from secondary airports seeking short-haul flights, while *segmented market* seek friendly, reliable and low cost service.

**Table 2 Apparent Southwest Airlines Segmentation**

<table>
<thead>
<tr>
<th>Market Definition</th>
<th>Southwest Airlines</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>LEVEL I</strong></td>
<td></td>
</tr>
<tr>
<td>Geographic market</td>
<td>North America</td>
</tr>
<tr>
<td>Service Market</td>
<td>Air transportation Services</td>
</tr>
<tr>
<td>Generic Market</td>
<td>Passenger transportation, cargo, business travel, vacations</td>
</tr>
<tr>
<td>Relevant Market</td>
<td>Domestic passengers wanting affordable air transportation</td>
</tr>
<tr>
<td>Penetrated Market +</td>
<td>One third of domestic passengers in top 100 48-state markets and 60% of travellers in most dense markets under 500 miles (Department of Transportation, as cited in Hallowell, 1996, p. 515)</td>
</tr>
<tr>
<td>Untapped market</td>
<td>Non-passengers (customers or not) of air transportation</td>
</tr>
<tr>
<td><strong>LEVEL II</strong></td>
<td></td>
</tr>
<tr>
<td>Defined Market</td>
<td>Domestic passengers in top 100 58-state markets and travellers in most dense markets under 500 miles, in secondary or downtown airports</td>
</tr>
<tr>
<td>Segmented Market</td>
<td>Travelers wanting friendly, reliable, low-cost service on short-haul (under 90 minutes) (Hallowell, 1996, p. 515)</td>
</tr>
<tr>
<td>Target Market</td>
<td>&quot;Business Select&quot;, &quot;Business&quot; and &quot;Wanna Get Away&quot; (Southwest, 2008, p. B-6)</td>
</tr>
</tbody>
</table>

Southwest will only open services to a new city if they can ensure at least eight flights originating there and basically in uncongested airports of downtown areas (Hallowell, 1996) leaving unproductive markets that limit their optimization (Weinstein, 2006).

**Target Marketing**

SWA has defined three target markets reflected in their fare structure: “Business select”, “Business” and “wanna get away” (Annual report, 2007). Defining the target market is a condition to an effective relationship marketing strategy, like the focused-marketing campaign to reward business travelers and increase their productivity (Annual report, 2007).

**Marketing Mix**

The marketing mix used to serve SWA target markets may be explained using the SIVA model (Dev & Schulz, 2006). SIVA transforms the 4ps to a customer’s perspective consistent with the customer-centric focus of SWA:

*Solutions (Product):* Short-haul flights with only one stop, at the lowest fare. With an average distance per trip of less than 815 miles, Southwest is able to justify characteristics such as:

1. Standardized 737 Boeing aircrafts
2. No meals to facilitate re-provision
3. No interline baggage transfers to reduce missing luggage costs.
4. No reserved seats to expediting the boarding process.

The trade off is timeliness, less complaints, high frequency of flights, non-traditional destinations, and cheerful attitude (Annual report, 2007).

*Information (Promotion):* Using their own scheduling and reservation system; customers have accurate information about discounts and best deals. SWA does not sell tickets through
online reservation agents and has designed a simple display of their fare schedule on ground and on-line (Garrow et al, 2007).

*Value (Price)*: Southwest uses a simplified prices structure based on “low, unrestricted, unlimited, everyday coach fares” (Annual report, 2007). In 2007 average price reached $106.60 for short flights while for longer flights the highest fee was $399 or walkup fares (Figure 3). The price is bundled in three segments: Business Select, business and “wanna get away”. *Business select* customers are first in boarding, receive “extra rapid Rewards” credit and a free drink.

![Figure 3 Southwest Airlines- Average passenger fare 2003-2007](image)

Rapid Rewards, their frequent flyer program, awards credits per one-way flight and not per mileage. With 2.7 million award tickets redeemed in 2007 this loyalty program represents only 6.2% of the revenue. Freedom Awards is a new reward for trading standard awards for non-restricted flights trades (Annual report, 2007).

*Access (Place)*: SWA satisfies previously marginal markets in uncongested areas serving 64 cities in 411 non-stop city pairs. The innovative boarding system of pre-assignment of boarding groups A, B, or C in a first-come first-serve basis, is now enhanced with assignment of position numbers within the boarding group to reduce waiting time (Annual report, 2008).
Customer Management Practices

Customer experience and delight are keystones of service management (Rust & Chung, 2006) requiring that the firm anticipates the expectations of the customer. Southwest practices a virtuous cycle where LUV and FUN stimulate high productivity and low costs through altruism, humor and fun at work (Quick, 1992). Southwest converts this satisfaction into commitment, expressed in higher likelihood for retention and higher productivity. The higher productivity and decreased costs, supports the ability to offer more routes and more flights per day, increasing targeted services and higher value through lower prices.

*Figure 1  Southwest Airlines Virtuous Cycle*

Using a typology of customer-relationship groups (Renartz and Kumar, 1998) SWA is able to work with high profitable and highly loyal customers or *True friends* (Figure 2). True friends customers are providing Southwest a profit for 2007 of $645 billion, based on their frequent flying and reduction of business costs.
**Figure 2 Typology of Customer-Relationship Groups for Southwest**

<table>
<thead>
<tr>
<th>High profitability</th>
<th>Butterflies</th>
<th>True Friends</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low Profitability</td>
<td>Strangers</td>
<td>Barnacles</td>
</tr>
<tr>
<td></td>
<td>Low Loyalty</td>
<td>High Loyalty</td>
</tr>
</tbody>
</table>

Source: Adapted from Armstrong and Kotler (2008)

**Delivery Effectiveness of Service Value**

Southwest Airlines uses all the elements of a customer-centric organization, formulating and implementing relationship economic drivers to increase the willingness of customers to fly, resources drivers to stimulate customers to choose the brand and social drivers to provide customers with recognition and prestige (Lacey, 2007).

The value delivered to their employees is captured through Trust that generates savings in operational costs. An example is the current practice of trusting the employees ‘word when they take sick days instead of requesting a visit to the doctor to bring a certification (McGee-Cooper et al, 2006).

Using the value-chain approach it is clear that Southwest has created value for three main stakeholders: The customers (through low prices), the firm (through high profits) and the suppliers (or employees through low opportunity costs). This value fluctuates dynamically as the quality of the service changes (figure 4).

Through the creation of this virtuous cycle, Southwest is able to influence the customers’ willingness to pay by offering a set of services and experiences that offset the costs of the transaction (Hallowell, 1996).
Customer experience matters in the airline industry and Southwest has understood how to address the intangibility, heterogeneity and inseparability of the service provided with each flight (Parasuraman et al, 1988).

_Tangibility:_ To enhance the airport experience SWA remodeled their gate area in more than 40 airports with comfortable seating, power station for electronics and flat screen television with different features for both business travelers and family travelers. Their personnel uses an informal dress code consistent with SWA approachable image.

_Reliability:_ The least late flights, low number of missing luggage, lowest number of customer complaints (Quick, 1992).

_Responsiveness:_ An incontestable 17 minutes of turn-around, while the industry is in 45 minutes. This is the time between disembark, cleaning, and reloading, fueling ad new boarding (Hallowell, 1996, p. 519).

_Assurance:_ Knowledgeable and courteous employees, genuinely interested in delivering FUN during the flight, while inspiring trust and confidence in the transaction (McGee-Cooper et al, 2008).
**Empathy:** Formal divisions of customer care and People department are responsible of facilitating overnight hotel arrangements in sudden interruptions of flights or procure provisions in case of extended delays (McGee-Cooper et al, 2008).

Southwest Airlines has striven to create value for their more than 32,000 employees expressed in their ranking as the top ten U.S. companies to work for, being the only airline in that list (Hallowell, 1996). Direct parameters like management reports account for lower turnovers than the industry and the best labor relations in the industry despite their unionization (Quick, 1992).

Assessment of Effectiveness of Quantitative and Qualitative Research

Marketing research helps SWA to maintain its customer-driven strategy through studies to understand customers’ insights to achieve return on marketing investment (Armstrong & Kotler, 2008). The outcomes of various focus groups resulted in the decision to remodel gate areas for business and family travelers.

Using their marketing automation division, Southwest Airlines observes passenger behavior to estimate fluctuations in the elastic segment of the demand for service, capturing customers that would otherwise drive (Boguslaski et al, 2004). Southwest was one of first three airlines in the world to offer online ticketing. In 1994 the exploration started and in 2000 reached $1 billion web sales, reducing inventory of non-used seats and increasing services to other markets (Tabor & Wajktowski, 2004). Employee satisfaction is also measured constantly and duly rewarded as the core of the relationship marketing approach of SWA.
Assessment of Ethical Considerations and Cross-Cultural Issues

SWA auto-defines as a “Customer service organization” (Barrett, 2008) with a mission that is centered in their external and internal customers. This statement appears consistent with Freeman (1994) core ethical principles, presented on Table 3.

<table>
<thead>
<tr>
<th>Principle</th>
<th>SWA ethics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Principle of entry and exit: Both buyer and seller understand their relationship and accept it.</td>
<td>This is fulfilled completely by Southwest, through their on-site and offline reservation channels.</td>
</tr>
<tr>
<td>Principle of governance: Rules of the game must be agreed on unanimously,</td>
<td>Implicit in the initiation of a relationship with SWA.</td>
</tr>
<tr>
<td>Principle of contracting cost: Parties who contract assume a portion of the costs of contracting.</td>
<td>SWA manages low costs of operations and transfer the benefits to the customers. Customers pay an average low price depending on the bundle selected</td>
</tr>
</tbody>
</table>

Ethical risks of employees wrong-doing are prevented through attraction and maintenance of good employee relations in a flexible environment (Hallowell, 1996). The communication strategy of SWA is not deceptive and is based on accurate information and simplified layouts, reducing the risk of unethical practices of hiding surcharges.

Southwest embraces multiculturalism and collaboration, and the creation of a People Department and Customers and the organization of culture committees responsible for activities to boost the “Positively Outrageous Customer Service” are examples of the formalization of ethics in customer relationships (McGee-Cooper et al, 2006)

Evaluation of Marketing Strategy Effectiveness based on CRM Model

The customer relationship management program at SWA reached first-order and a second-order effects on profitability (Reichheld, Markey and Hopton, 2000). First-order effects derive from 101 million passenger in 2007. Second-order effects are reflected in market share
and revenues from repeat sales and referrals, reduction of acquisition costs and replacement, and increase in employees’ retention (Reichheld et al, 2000; Best, 2009).

**Effectiveness of Price Strategy**

Southwest delivers value to the customers, through more than low fares and excellent service, they receive a different airline and airport experience. Passenger behavior was influenced at two levels: *willingness to pay to travel by air*, and *willingness to pay for airline service* (Garrow et al, 2006). Airline customers seek the lowest fares as main factor of their decision to fly (Garrow et al, 2007) and choose SWA because fares are less than $200 per trip for short hauls.

**Effectiveness in Channel Strategy**

In 2007 101 million people flew SWA, showing a growth rate of 36.39% from 2003 (Figure 6). This volume has shown consistent increases. Airline preference is given by price and itinerary level of service with less influence of other factors such as airplane type, legroom, departure time (Garrow et al, 2007). Southwest Airlines is delivering precisely these two first values: price and outstanding service.
Effectiveness in Communications Strategy

An effective communication strategy can resolve 90 to 95% of the dissatisfaction cases reported in business. In 2006 SWA received 60,000 complaints that if not solved properly would yield a replication of 1.5 million indirectly dissatisfied prospects (Freiberg & Freiberg, as cited by Middaugh, 2007). A prompt response from the people department of SWA would transform these figures into only 3,000 (60,000 * 95%). With 300,000 satisfied SWA customers the net promoter score (Promoters – Detractors) would be 297,000 (Best, 2009).

Financial effectiveness

With an average of employees per aircraft lower than the industry, less personnel per 1000 passengers in each station, and aircraft turn times substantially lower than the industry (Hallowell, 1996). Southwest management transforms satisfied employees into committed employees, and committed employees into satisfied customers and profitable performance.

After 34 years with consistent profits in every quarter (McGee-cooper et al, 2008) and a net income $645 million for 2007 (Annual report, 2007), Southwest continues to deliver value to their shareholders. (Figure 7). The average trip length in 2007 was 815 miles and 777 for the past five years, showing that Southwest has remained committed to their targeted segment (Annual report, 2007).
Effectiveness of Relationships with the Industry

Southwest impacts the industry in extraordinary manners: Between 1990 to 1998 markets entered by SWA increased traffic in 174% while prices fell 54% (Boguslaski et al, 2004). The savings that Southwest generates for the industry are reportedly $12.9 billion from low fares (Boguslaski et al, 2004). This is called the Southwest Effect. Figure 8 shows the comparison of operating costs of SWA and other carriers. Southwest has penetrated top 100 destination in 48 states (Annual report, 2007) with 60% market share and 102 million enplaned passengers (Annual Report, 2008).

![Figure 8 Operating costs of Select U.S. Airlines](image)

Theories Manifested in the Service Market Plan

This study has analyzed each aspect of the customer relationship strategy of Southwest with using nine theories of relationship marketing. (Figure 9)

Manifested Theories

The central theoretical model is the typology of fundamental business strategies (Slater et al, 2005) that defined the customer-centric of SWA as guide for this study. Other major supporting models were Porter’s value-chain (Porter, 1980) how value was delivered and captures; the virtuous cycle (Hallowell, 1994) that explained the connection employee-customer. SIVA model (Dev & Schulz, 2007) explained the components of the marketing; Weinstein’s
market definition model replicated SWA segmentation and SERVQUAL (Parasuraman et al, 1988) to evaluate components of service value delivery.

*Figure 1 Conceptual Framework for CRM Evaluation - Southwest Airlines*

<table>
<thead>
<tr>
<th>CRM Environment</th>
<th>Strategy Formulation and Implementation</th>
<th>Marketing Strategy Components</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value Chain (Porter, 1980; Virtuous cycle (Hallowell, 1994))</td>
<td>Marketing Strategies</td>
<td>Loyalty-based Marketing (Reichheld et al, 2000)</td>
</tr>
<tr>
<td>Strategic Orientation</td>
<td>Typology of Fundamental Business Strategies</td>
<td>Customer Management Practices</td>
</tr>
<tr>
<td>Trust and Commitment Theory (Morgan &amp; Hunt, 1996); Customer Relationship Drivers (Lacey, 2007)</td>
<td>Strategic Orientation</td>
<td>SIVA Model: Solutions, Information, Value and Access (Dev &amp; Schulz, 2007)</td>
</tr>
<tr>
<td>Trust and Commitment</td>
<td>Market definition Model (Weinstein, 2006), Best (2009)</td>
<td>Target Marketing</td>
</tr>
<tr>
<td>Hofstede (1988); Quick (1992)</td>
<td>Cultural Values and Beliefs</td>
<td>Market Segmentation</td>
</tr>
<tr>
<td>Stakeholder Theory (Freeman, 1984); Theory of Marketing Ethics (Hunt &amp; Vitell, 1986)</td>
<td>SERVQUAL Model (Parasuraman et al, 1988); EXQ Experience Quality (Klaus &amp; Maklan, 2007)</td>
<td>Price sensitivity model (Garrow, Jones &amp; Parker, 2007)</td>
</tr>
<tr>
<td>Ethics and Cross Cultural issues</td>
<td>Effectiveness of Value Delivery</td>
<td>Marketing Research</td>
</tr>
</tbody>
</table>

*Suggested Models*

One theoretical model that could be used by Southwest Airlines is the EXQ Experience Quality (Klaus & Maklan, 2007) based on the theory of customer experience and service quality (Parasuraman et al, 1988) to measure the impact of customer experience on the brand. Customer experience is considered a predictor of customer “satisfaction, advocacy and purchasing behavior” (Klaus & Maklan, 2007) and relies in at least seven factors (Figure 10)
This model, if quantified, will address the integrated customer experience that SWA passengers receive not only during the flight, but in their waiting rooms, when booking or checking in online, when selecting their carrier and at their original decision point of whether flying or driving.

**Recommendations for Future Businesses of this Nature**

Considering the intensive competition in the airline industry and the complex barriers of entry, it is essential for future participants to accurately define their market potential. Best (2009) proposed a market development Index MDI for this purpose; MDI below 33% means that entering the market will benefit the firm; if MDI is greater than 67% entry will require innovative strategies to attract customers. SWA’s focus strategy of entering non-saturated markets has boosted its success.
However, focus marketing strategies are risky and require clear identification of the segments of the market that are unattended or marginal (Olson et al, 2005). Given the high costs of energy and fuel, potential travelers would be more willing to consider to fly than driving if an airline offers competitive prices for short distances.

In terms of culture, the FUN and LUV environment of SWA is not difficult to follow, but it requires commitment and inspirational leadership and must be accompanied by economic and non-economic rewards for the employees. Trust is another lever of the strategy and firms must strive to earn it through behaviors that signal care for the needs of customers (Seidman, 2008). By doing this, they will increase the willingness to do business with the firm.

Conclusions

Southwest Airlines has been analyzed in various dimensions of customer management and relationship marketing strategy in this study. An inimitable culture that privileges employees and customers is the core of SWA business strategy. Their customer-centric orientation (Slater et al, 2006) is operationalized through different mechanisms of segmentation and target marketing. The application of the SIVA model (Dev & Schulz, 2005) demonstrated that the firm delivers solutions, information, value and access to their external customers.

The relationship with the internal customers –employees- is the most salient characteristic of Southwest and supports their sustainability for the past three decades. An environment of joy and fun at work appeared to increase the productivity and decrease the costs of transaction and operation. Through this capture of value, Southwest has delivered value in a virtuous cycle that benefits the customer as the core of their marketing strategy.

Southwest has evolved from a late-entrant in the industry to a focus strategist with clear definition of target markets and optimal service value delivery.
References


