



ELLIOTT INVESTMENT MANAGEMENT L.P.  
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June 10, 2024

The Board of Directors  
Southwest Airlines Co.  
2702 Love Field Drive  
Dallas, Texas 75235

Dear Members of the Board:

We are writing to you on behalf of funds managed by Elliott Investment Management L.P. (together with such funds, “Elliott” or “we”). Elliott has made an investment of approximately \$1.9 billion in Southwest Airlines (“Southwest” or the “Company”), representing an approximately 11% economic interest and making us one of the largest investors in the Company.

Southwest is a legendary airline with a proud history. Since starting service in 1971, Southwest revolutionized the airline industry with an innovative business model built on operational excellence and a commitment to providing customers with a low-cost alternative to the legacy airlines. This winning strategy generated decades of success and allowed Southwest to become the premier U.S. domestic airline, with 47 consecutive years of profitability in a highly competitive and challenging industry. Along the way, Southwest became a beloved brand among customers and a motivating career opportunity for its employees.

Today, however, poor execution and leadership’s stubborn unwillingness to evolve the Company’s strategy have led to deeply disappointing results for shareholders, employees and customers alike. Southwest’s share price has declined by more than 50% in the past three years and has now fallen below the levels at which it traded in March 2020, during the depths of the COVID-related travel shutdowns. And while the U.S. airline industry is seeing record revenues and peer airlines are enjoying very strong profitability, Southwest’s 2024 EBITDAR is expected to be nearly 50% lower than 2018 levels. In addition to negative returns for shareholders, this disappointing financial performance has cost each frontline employee tens of thousands of dollars on average in the form of reduced employee profit-sharing and declines in the value of Southwest stock held by employee retirement plans.

After 18 months of intensive research, we are convinced that Southwest represents the most compelling airline turnaround opportunity in the last two decades. The significant investment we have made reflects our conviction that, with the right leadership, Southwest can regain its status as an industry-leading airline. In this letter and the appended presentation, we lay out our perspectives on how Southwest can reclaim its status and achieve the success that Southwest’s shareholders, employees and customers deserve.

## **Southwest Today**

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Southwest’s rigid commitment to an approach developed decades ago has inhibited its ability to compete in the modern airline industry; this ethos pervades the entire business with outdated software, a dated monetization strategy and antiquated operational processes. This failure to modernize is vividly underscored by the December 2022 operational meltdown that was caused by the Company’s outdated technology, which led to Southwest stranding over two million customers over the holidays.

Southwest's Executive Chairman and its CEO, who have spent a combined 74 years at the Company, have presided over a period of severe underperformance, and they have demonstrated that they are not up to the task of modernizing Southwest. Since his appointment, Southwest CEO Bob Jordan has delivered unacceptable financial and operational performance quarter after quarter, resulting in seven negative guidance revisions in the last 17 months. Operational metrics are pointing in the wrong direction: Southwest's unit costs – a core priority for a low-cost carrier – have ballooned, while unit revenues have lagged peers. Even as the Company's performance has deteriorated, Jordan has demonstrated a surprising level of complacency, describing each quarter as “great” or “strong” while the earnings outlook continues to fall. Despite the management team's assertions that it is “absolutely committed” to bringing per-unit costs under control, management guided costs meaningfully higher for 2024 and revised cost guidance upward again in April.

Southwest's Board has failed to hold management accountable for poor execution and has been unable to catalyze (or permit) the necessary strategic evolution. Instead, the Board has reinforced an insular culture and outdated thinking in the face of indisputable evidence that change is required. The Board includes no directors with external airline experience, and a majority of the independent directors were recruited by Executive Chairman Gary Kelly. This Board has in turn selected a management team that, of the eight most senior executives, includes only one executive with experience at another airline; the rest have worked at Southwest for an average of over 25 years. The mandate from the Board has been clear: Keep doing things the way they have always been done.

The lack of accountability is best reflected in the Company's response to the December 2022 operational meltdown. In a clear display of poor leadership, CEO Bob Jordan declined to testify in front of Congress after the meltdown, despite attending a company rally just 40 miles away in Baltimore the prior day. No senior executives were terminated for their role in the meltdown. Most concerning, and in blatant disregard for the affected customers and employees, the Board nearly doubled the compensation of all key executives in the year after the incident.

We believe that new leadership is required at Southwest. While Southwest has a proud history, that history is not an argument for supporting poor leadership and sticking with a strategy that no longer succeeds in the modern airline industry. Rather, Southwest's legacy *necessitates* evolution and change to regain industry leadership for its customers, employees and shareholders. As one of Southwest's largest investors, we are committed to delivering the necessary leadership changes to achieve this goal.

## **A Stronger Southwest**

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In the accompanying presentation, “Stronger Southwest,” we outline our views on the challenges the Company faces today and our recommendations to drive improved performance, which we summarize below:

- (1) **Enhance the Board of Directors**: The Board should be reconstituted with new, truly independent directors from outside of Southwest who have best-in-class expertise in airlines, customer experience and technology.
- (2) **Upgrade Leadership**: Southwest must bring in new leadership from outside of the Company to improve operational execution and lead the evolution of Southwest's strategy.

- (3) **Undertake a Comprehensive Business Review**: Southwest should form a new management and Board-level committee to evaluate all available opportunities to rapidly restore the Company's performance to best-in-class standards. This review would modernize Southwest's strategy and operations with a focus on increased customer choice, improved cost execution and updating outdated IT systems, among other opportunities, and it should leverage the fresh perspectives of the new directors to help formulate the optimal go-forward plan for Southwest.

By executing on the Stronger Southwest plan, we believe the Company can return to its rightful position as an industry leader, including generating best-in-class margins and compelling returns for its shareholders. **We believe Southwest's stock can achieve \$49 per share within 12 months, representing a highly attractive 77% return during the period.** For the Company's frontline employees who have a meaningful economic stake in Southwest's success, we believe the plan would result in substantial incremental long-term value from additional profit-sharing payouts and appreciation of employee-owned stock.

The Stronger Southwest plan puts the Company on a path to more sustainable performance that will better serve customers, employees and shareholders. The plan modernizes Southwest's approach to ensure that its offering is aligned with customer preferences. It upgrades leadership to improve execution. It drives the efficiency required to continue offering low fares. And it facilitates the necessary investments to run the reliable operation that customers and employees expect.

## Next Steps

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Southwest became a leading airline by innovating and executing. Today, Southwest's failure to execute and evolve has led to deteriorating performance, and the Company simply is not living up to its legacy of efficiency and top-tier results. Nevertheless, we are convinced the issues the Company currently faces are addressable with the right leadership and a comprehensive, unbiased evaluation of the available opportunities.

We look forward to collaborating with Southwest to restore accountability and best-in-class financial performance for the benefit of the Company's employees, customers and shareholders. To that end, we will make ourselves available for a meeting with you at your earliest convenience to discuss these issues in greater detail and to align on the changes that Southwest needs in order to deliver on its significant potential.

Sincerely,



John Pike  
Partner



Bobby Xu  
Portfolio Manager