

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

So, I just have four quick things to tell you about before we jump into this episode on one of my all-time favorite founders, Herb Kelleher.

Number one, I do a terrible job of letting you know, but I have a personal email list. For every book that I read, I take somewhere between 50 to maybe 150 different highlights. For my email list, I whittle those down, and this actually takes a long time to do, to my top 10 highlights.

So if you are interested in getting my top 10 highlights for every single book that I read, and you want me to email those to you, I will leave a link down below. You can also go to founderspodcast.com and put your email on there, and I will email you every single time that I read a new book.

Second thing, I was interviewed recently on the Invest Like the Best podcast. I talked with my friend and the host of Invest Like the Best, Patrick, on what I've learned for the last year and the last 12 months of doing Founders' Podcasts and reading all these biographies.

If you are interested in hearing that long-form interview, I think it's about 90 minutes long, you can search for Invest Like the Best in your favorite podcast player.

Listen to episode 343 in the service of founders.

The third thing I want to tell you about is I'm actually doing a live podcast, a live show with Patrick from Invest Like the Best in New York City on October 19th.

I think that's a little over three weeks from now.

If you have not already got your tickets, that link will also be down below.

If you live in New York, I think it's a no-brainer to come out, but it's also a great excuse to travel to New York City.

The last thing I want to talk to you about is the presenting sponsor of this episode and a product that a lot of my founder friends are using, and that is Vesto.

You can check them out at Vesto.com.

What Vesto is really good at is helping businesses of all sizes invest their cash in US treasuries. You'd want to do that because when your business owns treasuries, that cash is backed by the US government and it earns interest while it sits there.

I have one founder friend who raised a bunch of venture capital money and he uses Vesto as a way to extend his runway.

I have another founder friend who bootstrapped his company and he uses Vesto to get a better rate of return than if that cash were just sitting in his bank account.

If this sounds interesting to you, I highly recommend you go to Vesto.com and check out what they have to offer.

I know the founder Ben actually just saw him again last week.

I've spent a bunch of time with him.

If you schedule a demo, so if you go to Vesto.com and schedule a demo, you actually speak directly to the founder Ben.

I think he's incredibly impressive and I think if you speak to him, you'll be impressed too.

Make sure that you tell him that David from Founders sent you and with that, let's jump into the episode.

I actually read two books to make this episode.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

I hope you enjoy it.

One plan, no matter how well laid out, couldn't possibly respond to all of these situations.

This is why Kelleher does not put much stock in traditional strategic planning.

He explains it this way.

Reality is chaotic.

Planning is ordered and logical.

The two don't square well with one another.

When US Air pulls out of six cities in California, they don't call me and tell me they're going to do that.

Now, if we had established a big strategic plan that is approved by our officers and the board of directors, I would have to go to the officers and the board and tell them that we want to deviate from this plan.

They would want to know why I want to buy six more airplanes.

The problem is we'd analyze it and debate its merits for three months instead of getting the airplanes, taking over the gates and dominating California.

The meticulous nitpicking that goes on in most strategic planning processes creates a mental straight jacket that becomes disabling in an industry where things change radically from one day to the next.

When a financial analyst chided Kelleher about not having a strategic plan, he said, we do have a plan.

It's called doing things.

That is an excerpt from one of the two books that I'm going to talk to you about today.

That is from Nuts, Southwest Airlines' Crazy Recipe for Business and Personal Success that was written by Kevin and Jackie Freberg.

The other book is called Herb's Heroes and it was written by a pilot that worked at Southwest for 37 years.

I have not been able to find a comprehensive biography on Herb Kelleher.

I think one should exist.

I think he was an extraordinary person, a gifted entrepreneur who built the most successful airline in history, which we'll get into today.

To make this episode, I used these two books.

I reread, this is the second time I read the Nuts book.

But I used these two books and I took notes on interviews that Herb did when he was alive.

So what I'm going to do first is I summarized all of my notes from the book Herb's Heroes.

I just want to go over that outline, which I think will give you a good overview as to the type of person Herb was and why he was that way.

So he's born during the Great Depression.

His father worked in a soup factory.

Herb's older brother was killed in World War II.

Herb is 10 years old at this time.

After his brother dies, his father dies unexpectedly the year after.

And then within a few years of that happening, Herb's two surviving older siblings move away for college.

So now Herb grows up.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

The second half of his childhood is just him and his widowed mom.
And so her influence and the lessons that his mom taught him, he uses his entire life including in building his company.
So they would have late night talks almost every night at the kitchen table.
And even when he was a kid, they're staying up to like two in the morning.
And she's teaching Herb about life.
And one of the most important things that she did was she taught him that adversity is a normal way of life.
This is a woman that lost her son, lost her husband, and yet there was no self pity whatsoever. She said that stress in difficult times was not debilitating, but opportunities to excel and achieve.
And so even from a young age, he starts to find problem solving invigorating.
The reason I've always admired Herb, I've tried to consume as much information about him as possible.
And the reason it came to the top of my mind to make an episode about him right now is because I was reminded of something that he said during a talk.
And this came many years later in his life.
He's already been working on Southwest for multiple decades at the time.
And he was asked, you undergo a lot of stress all the time.
How do you handle it?
And his response is perfect.
He said, I don't handle it.
I like it.
And so that's a maxim that I want to repeat to myself as we're building our companies difficulties and hard times are inevitable.
And I'm just going to remind myself, I don't handle my stress.
I like it.
It completely changes your mindset into like, this isn't something I have to do.
It's something I get to do back to his early life.
He was a gifted athlete in high school.
He ran track, played basketball and football and lettered in all three sports.
Before college, he works at the very same soup factory that his dad had worked at.
And he worked there for six years.
He did every single job at the factory.
This is something he's going to continue to do at Southwest, which we'll talk about later, but this is why I'm telling you this.
He called his six years working in a soup factory, right?
This is a guy that's going to go on to, to, he's really gifted.
Everything does gifted athletics.
He's really good at college, gets a law degree, clerks for the Supreme court, has a successful law practice and at 35 with four kids decides, Hey, I'm going to be an entrepreneur.
I'm going to try to run, I'm going to try to start an interstate airline in Texas.
And so with all that, the fact that he said the six years at the soup factory

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

doing every single job, he called it the best education he ever had.

And so even when he was younger and then throughout his entire career, people say the same thing about him over and over again.

They describe him as a fierce competitor and they said he had a hard work ethic. That is a quote, a hard work ethic.

He was working a hundred hour weeks at the beginning of Southwest because he still had to practice law to pay the bills.

It took them four and a half years between the time they raised money for the company, they served the company and then they're actually allowed to fly their first flight.

Another thing about her, he was old school.

He was hard driving, hard drinking, fast living Texan.

He started every day early, regardless of how late he was out the night before drinking.

This is going to come up over and over again.

Another crazy thing, he smoked five packs of cigarettes a day and drank wild turkey bourbon every day.

He said wild turkey and Philip Moore cigarettes are essential to the maintenance of human life.

When he was in his sixties, he fought and beat prostate cancer.

And then he was asked if he thought his smoking habit contributed to his cancer.

And he said, I do not smoke with my prostate.

He lived until he was 87.

He felt he was born to be an entrepreneur.

He thought the spirit of an entrepreneur was within him.

And he had a great line about this.

He says, if you're crazy enough to do what you love for a living, then you're bound to create a life that matters.

He designed his entire business model to keep costs at the lowest possible level.

He built the most successful airline in history.

Southwest was profitable for 47 straight years.

To put into context about how outrageous that accomplishment is relative to his competitors and peers, he was profitable for 47 straight years.

The next most successful airline was profitable for five.

And when you read about Herb, or if you listen to his interviews, like he's hilarious.

So, and he says, like, I don't take myself too seriously, but I take competition very seriously.

Unsurprisingly, one of Herb's favorite people was Winston Churchill.

He'll quote Churchill all the time.

He'll use Churchill's ideas and talks and speeches to his employees and to his team.

One of his innate talents that jumps out, if you read a book about him, is the fact that he was able to operate on very little sleep.

There's a lot of stories in both books about the fact that he'll be out drinking

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

till like three in the morning and then he'll be at the office at like 7 AM.
He also talks a lot about and repeats the importance of having a business model that endures the hard times, talks about most of the airlines are set up. They'll reap a bunch of profits in good times.
And then yet they give it all back when the inevitable downturn happens. And so one thing he talks about is like, listen, we'll joke around. We'll have a lot of fun.
We're very extravagant in our marketing, but we're very fiscally conservative. We're conservative with debt.
They paid for 80% of their planes out of earnings.
Most other airlines are borrowing that money.
They own the largest amount of planes outright than any other airline. And the quote that came to mind when I was reading about Herb's financial approach to building his company is this fantastic quote from Charles de Gaulle, where he said, all that matters is to survive.
The rest is just words.
Herb was also a gifted storyteller and he was very persuasive. He was not building a company.
He was leading people on a crusade.
He was not hiring employees.
He was converting missionaries.
He says, our indomitable dedication is the core of our success. That is the most difficult thing for a competitor to imitate.
They can buy all the physical things that we have.
The things that you can't buy are dedication, devotion, loyalty.
The feeling that you are participating in a crusade.
And the one thing that Herb was insistent that they do better than anybody else was served.
Listen to what he said.
We are a service company.
We just happen to fly airplanes.
Herb read all the time last week on the Working with Jeff Bezos episode. I mentioned this text I got from a friend where he noticed he'd raised a bunch of money for his company.
He noticed like every single billionaire that he interacts with reads a ton. And they usually read a lot of history and biography.
Herb was the same thing.
You know, he starts off as an attorney before he dies as a billionaire.
He read all the time.
He did it when he was younger, did it when he was older.
History was his favorite subject.
He said, this is why he said he read history.
This is fantastic.
He says, reading history kept me from making the same mistakes that was inside

and outside his own industry.

He definitely knew the, the history of the airline industry.

And he talked about over and over again that you should read the history of the airline industry as a cautionary tale.

That's why the main thing we talked about today is the fact that this guy, very obviously capable of independent thought, his main advantage was the ability to question every single conventional, quote unquote, conventional wisdom in his industry and ask, like, does this make sense or not?

Some of it did make sense.

So he would do that.

But in many cases he realized there was a better way.

And so he would pursue that regardless of what people around him were doing.

And then finally, before I jump into the other book, he led from the front.

This is one of the most, one of the most admirable things about him on the busiest day of the year, which is Thanksgiving Eve, you would find Herb out on the tarmac loading and unloading baggage.

And he would do so regardless of the weather.

There's a great story in the book where somebody walks up to him, they just see this really tall guy in a yellow poncho loading and unloading bags.

It's not till he turned around.

They realized that's the CEO and the founder of the company.

Okay.

So now I'm going to put up the book called nuts.

And I'm going to go right into the founding of Southwest at the time.

Remember Herb is 35.

He's an attorney in San Antonio and he's got four kids.

Southwest Airlines was a brainchild of Roland King, a San Antonio entrepreneur who owned a small commuter air service and his banker, John Parker. Parker had complained to King that it was inconvenient and inexpensive to travel between Houston, Dallas and San Antonio and suggested starting an interstate airline.

And so Herb gets involved because he's Roland King's attorney.

And so Roland King goes to Herb and he draws this thing called the Golden Triangle, which shows Dallas, Houston and San Antonio.

It's on a cocktail napkin.

That cocktail napkin is still framed inside of Southwest headquarters.

This is happening during the late 1960s.

This is why they think there's an opportunity.

First of all, they use the word interstate airline, which is fascinating.

So their main goal is, okay, there's different regulations.

You have state regulations if you're only flying within the states and then obviously federal regulations.

Once you go state to state, getting approved to fly inside of state is easier than at the federal level at this time in history.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

Although it was still very difficult getting approved.

This is just like a four year battle.

But the reason what I found fascinating is Roland King had this idea by seeing California already had a successful interstate airline.

And he thought there was a lot of similarities between California and Texas, obviously the size of the states.

But the fact that there was hubs of cities that were experiencing rapid economic and population growth, but they're also far enough apart to make travel by bus or car very inconvenient.

And so at the beginning of their ideas, like, well, why don't we just take what's obviously working in California and do the Texas version of this.

And in one of his interviews, Herb talks about this time.

He's like, why would you want to do something like take this big of a risk when you're 35 years old, you have four kids, you're married.

And he said, the allure of doing something different.

I wanted to do something exciting.

I was curious.

Also, most adults in the US had never flown because it was too expensive.

I believe there was a huge untapped market out there and his assumption that there's a huge untapped market out there was proved correct.

He had to go through four and a half years.

That's to prove that assumption.

He had the first fight through four and a half years of a legal battle and unfair trade practices in the state of Texas.

So he files Southwest application on November 27th, 1967.

And he does so with the TAC, which is the Texas Aeronautics Commission.

They approve it.

They say, yes, you can fly between Dallas, Houston and San Antonio.

What he didn't know at that time was that he inadvertently started a war that would last for years and almost drive Southwest Airlines out of business before it put a plane in the air.

So he had three main competitors, Braniff, Trans-Texas and Continental.

And they immediately sue and they get a temporary restraining order that prohibits the TAC from issuing Southwest a certificate to fly.

This case goes to trial.

They argue, hey, these markets that Southwest wants to serve, they're already saturated, there's no room for another carrier.

The court that they bring it to agrees.

This immediately sparks herbs and Nate like competitive, half to win personality.

And so he appeals that appellate court also says, no, you cannot do this.

So they lose that case too.

At this point, they had raised, so it says the original investors \$543,000.

Remember, that's a 1970 minus a lot of money had been eaten up in legal expenses.

The corporation's liabilities grossly exceeded its assets.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

And there was no prospect of raising new capital without the TAC certificate in hand, which two courts have both denied them.

And so this is Herb's response.

Some members of the board thought it was wise to cut their losses and close down.

At this point, Kelleher street fighting spirit surfaced.

Gentlemen, let's do one more round with them.

I will continue to represent the company in court and I'll postpone any legal fees and I will pay every cent of the court costs out of my own pocket.

The directors agreed to give it one more shot.

And Kelleher argues this case all the way up to the Texas Supreme Court.

And he convinces them to overturn the lower appellate courts decision and Southwest gets its certificate to fly.

And so we go back to this idea that Herb framed life and everything he did is this grand epic, right?

We're not building a company or we're on a crusade together.

It's always a mission bigger than himself.

And he talks about like, he was asked in an interview, like, why would you do this?

Like, why would you willing to fight for years for free?

And he said it's because these other airlines were trying to offend one of his ideals.

He said if other airlines could prevent Southwest Airlines from starting, then that means the free market system is failing.

And one of the things that motivated him was to validate the free enterprise system.

And the other reason he said was that it was very hot competition and I like to win. So then they're able to raise more money.

They buy planes, they wind up starting to sell tickets two days before their first flight, their competitors wind up getting another injunction and they get another restraining order, this time from a different regulatory body that would prevent Southwest from beginning service.

And this was Kelliher's response.

He went straight to the law library and worked all night to decide how to proceed.

He found a president and presented his argument to the court the next morning.

The Texas Supreme Court ruled in Southwest favor again and ordered the lower court judge not to enforce the injunction.

Kelliher then telephoned Muse.

So at the very beginning, he was not running Southwest.

He is still going up for the first years, he's going to be a founder and a board member of Southwest and he's still running his law practice.

It's not until the CEO that the founders hired this guy named Lamar Muse, he's going to leave to start a competitor against Southwest.

The CEO that comes after Muse doesn't work out.

And so the boards like Herb, if this is going to, like you have to do this.

And here's an interesting side note for you.

Lamar Muse, who I'm about to introduce you to here, winds up when he leaves and starts Muse Airlines many years later, when he's about to go bankrupt, Herb buys

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

his airline, but that's many years into the future.

Let's go back to this.

So the Texas Supreme Court says, hey, you know, you cannot enforce this injunction.

Kelleher then calls Muse on the phone and says, put the planes in the air.

When Muse confided to Kelleher that he was still concerned about a sheriff showing up to enforce the injunction, Kelleher didn't mince any words.

I told him, you roll right over that son of a bitch and leave our tire tracks on his uniform if you have to.

The very next day, June 18th, 1971, Southwest Airlines was finally off the ground.

And so this is the first mention of something that repeats over and over again, the fact that Herb was a master at turning things into a cause.

So it says, the seemingly insurmountable obstacles thrown at Southwest or what created Kelleher's passionate love for the airline, they would put 12 or 15 lawyers on a case and on our side, there was just Herb.

They almost wore him down to the ground.

But the more arrogant they were, the more determined Herb got.

This airline was going to go into the air and stay there, he said.

Herb is a master at turning things into a cause.

It was an affront to my idealism, he said.

If you're going to let these guys get away with this, it is a radically different type of country than the one I want to believe in.

And he wasn't making all this up.

His competitors were out to get Southwest and they were willing to break the law to do so. Four years later, both Braniff and Texas International were actually indicted by the US government for conspiring to put Southwest out of business and for violating the Sherman Antitrust Act.

In addition to suing him in every single court, they also would behind the scenes, would chase Southwest investment bankers out of their underwriting syndicate when they were trying to IPO.

They would go to Southwest vendors and convince them to boycott and not sell to Southwest. They tried to keep Southwest from using the fuel-hydrant system at Houston's airport and they successfully got Southwest blackballed from membership in the airline credit card system.

To all of these charges, both companies pleaded no contest.

Okay, so once Southwest is up and running, you'll see that a lot of the innovations were forced upon them, necessities, the mother of all invention kind of thing. They're just severely resource constrained.

And so if you're severely resource constrained, you are forced to innovate and the way they do that is like, well, just question assumptions.

And if you keep doing that successfully, you'll lead to finding new markets and new ways to make money.

And so remember, one of Herb's initial hypothesis is that there's this huge untapped market out there because most Americans had never been on a plane yet.

So it says, the company's creative roots go back to its early days.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

Employees came up with clever ideas for keeping the business alive because Southwest had no choice but to become inventive in order to compete with the established carriers. The company simply did not have the money to go head to head with the majors.

They would have to outthink and outmaneuver.

And so anytime I read that word outthink, I always think of Jeff Bezos talking about Zappos in the early days before Amazon bought Zappos.

And he discovers, he goes to the airport and discovers that after 9-11, you have to obviously take off your shoes and you put them into these containers to go through the X machine and Zappos had bought ads, which I think they were the first company to do this, that bought ads saying, hey, you can buy shoes on Zappos as people are putting shoes into those containers.

And he starts like getting pissed off at his team and he yells, they're out thinking us. And he was, you know, obviously right.

So they wanted to buy them. The airlines operated as though there were only two market segments.

So this is going to be one of the main innovations or one of the first innovations that Southwest does.

So the airlines operated as though there were only two market segments, those who could afford to fly and those who couldn't.

This assumption, remember, severely resource constrained, you're forced to innovate and the way you innovate, you question assumptions in this industry.

This assumption guided the operating strategy of the major carriers.

Southwest believed that it could stimulate a tremendous amount of new travel with low fares and superior service.

And they were challenging this assumption from day one.

Remember Herb designed this entire business model to keep costs at the lowest possible level.

Those low costs allowed them to charge less prices.

And so they start running this experiment by flying into the Rio Grande Valley at cheaper than every single other competitor in this region.

This is the result.

The year before Southwest initiated this low cost service, 123,000 passengers flew into the Rio Grande Valley.

Less than 11 months later, the market expanded to 325,000.

So from 123,000 people right at this higher price, they dropped the price because they have a low, obviously low cost structure, low work cost structure, I should say, and that expands the market by more than double, gives them another 200,000 people flying.

So the increase was larger than the entire market was before.

And they only discovered this because they have this commitment to trial and error. This is a Jeff Bezos spoke about this a lot last week.

They have this commitment by trial and error.

And they just realized we have to be comfortable with innovating through

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

trial and error that means being comfortable with the error part. There's a bunch of examples in the book where people make mistakes. Sometimes cost company \$400,000, \$500,000, and Herb refuses to fire them because he's like, that's the point. We have to be comfortable with the error part of trial and error. So they take this, they extend this idea. They're like, okay, all signs are pointing to the fact that people are price sensitive, that if we keep lowering the price, we'll expand the amount of customers that we have is another way we can continue to segment our existing and then potential customer base. And so they come up with something that is going to be copied by every single other airline. It's crazy that no one uses this point. So they perfect system-wide, two-tier, peak and off-peak airline pricing. They start off knowing their base is the frequent business traveler. The person that is in Houston, but needs to get to San Antonio in a meeting and then can be back home in time for dinner, right? They are less price sensitive. What they didn't know is how big is the leisure traveler segment of this market because you can't know that because it's too expensive for the leisure traveler. Keep that in mind as we get to this. Like many of its innovation, Southwest two-tier fare system was not the outcome of a sophisticated long range planning retreat. It was a result of good old fashioned trial and error. Just five months into operations, one of Southwest planes was in Houston, but needed to get to Dallas for routine maintenance over the weekend. Normally they would just fly the plane with a crew, but no passengers. And so they're like, let's test this idea. Normally a flight at this time is like, let's say \$26. They're like, what if we just cut it to like a third? What if we say it's, if you fly out on this Friday night flight, the has to fly anyways, if you're not on the plane or not, it's 10 bucks. Worst case scenario, we generate some revenue that hopefully helps offset the cost of faring in a completely empty plane. And immediately it works. Passengers quickly caught on and Southwest had to start turning people away only two weeks into the offer. And so this is when they realized, wait, there's not one type of traveler. There's really two types of travelers that Southwest has to satisfy. So you have the convenience oriented business traveler. This is the person that is more time than price sensitive. They want a lot of business hour flights and the price sensitive leisure traveler who primarily wanted lower fares and had more flexibility about when to fly. So they immediately have two fare structures.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

They say, listen, if you're flying during the weekday up until 7pm, you're likely a business traveler, we're going to charge you \$26.

If you fly after 7pm or if you fly on the weekends, it's half that it's \$13.

And this is the result.

Passenger traffic skyrocketed.

Southwest had first defined a special market niche consisting of short haul passengers and then further segmented those short haul passengers by need into time sensitive business travelers and dollars sensitive leisure travelers.

This idea would become one of the most widely emulated marketing innovations in airline history, system wide peak and off peak pricing.

And so this idea was so successful that their main competitor, Braniff, immediately copied them, right?

And this is hilarious because in one of his interviews, he talked about the fact that one of his competitors lowered prices and called it an introductory fare, even though they had been in business for 40 years and serving the exact same markets for 40 years.

And so this is what I mean about having forced like they're just unbelievably creative and open to all kinds of new ideas.

So they went up keeping their prices the same and then told customers, if you pay a higher fare, we'll give you a free bottle of whiskey.

And so for a few months, they became the largest liquor distributor in the state of Texas.

Oh, so and this is the important part.

They went directly to their customers and explained to them what was going on.

The fact that, hey, this bigger existing competitor with a lot more resources, they're trying to put us out of business.

This is not going to be good for you.

This, if you ever studied David Ogilvy, he talks about this over and over again, and Claude Hopkins, probably the best copywriter in history, that tell the truth in your ads, speak one person to another, tell the people why you're doing what you're doing.

The truth will resonate with the buying public and they may act in ways that surprise you.

Here's an example of that.

So says the ad explained how Braniff was trying to put Southwest out of business and then went on to say the Southwest would not only match Braniff's fare, he would also offer every passenger a choice.

Travelers could choose the \$13 fare.

So this is during the week, right?

They're taking their off-peak price and temporarily putting it during peak, right?

So says, hey, listen, that's fine.

We'll match them.

But here's why they're doing what they're doing.

Now, we also have an idea for you.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

Travelers could choose the \$13 fare or buy a regular \$26 ticket and receive a complimentary bottle of alcohol.

So you could choose from Scotch, whiskey or vodka.

Now, why is this going to work?

Who is traveling during the week?

These are business travelers.

They are not paying for their own ticket.

Business travelers loved it.

They could charge a \$26 fare to their expense accounts and go home with a free bottle of liquor.

For a few month period, Southwest was the largest distributor of alcohol in the state of Texas.

To Braniff's dismay, 76% of Southwest passengers paid the \$26 and took the gift.

Tell the truth in your ads.

Communicate person to person.

Tell them what you're doing.

This is a result.

Two years later, Braniff terminated its Dallas Houston Hobby Airport service.

This is the route that they were competing on.

Braniff thought they were going to run Southwest out of business off this route.

And in turn, they ran themselves out of business off this route.

And so now we go into more principles that her built Southwest with.

First is you should know your niche better than anybody else.

So he starts this with asking and making sure everybody in your company asks and knows, what is your fundamental reason for being?

Why does your company exist?

When you identify that, make sure everybody else knows it and then stick to it.

And here's why.

When you have a vision and someone comes to you with some convoluted idea, you can hold it up to the vision and ask, does it fit?

If not, don't bother me.

Southwest exercises the discipline not to stray from its strategy.

It does not, for example, buy jumbo jets, fly international routes, or go head to head with a major carrier.

So he's talking about the difference in their behavior compared with every single, at this point, every single other competitor that they have.

While other carriers have been lured by the temptation to step outside their niche,

Southwest Airlines has maintained the discipline to stay focused on its fundamental reason for being.

And one thing that Herb repeated from the very beginning is like,

I don't give a damn about market share.

I want profits.

In fact, let me put the book down for one second.

I want to read some of the ideas he has and why he was thinking about this.

And this is when he was a much older man looking back at this time.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

And so he says, we may be flamboyant from a marketing perspective, but we are very conservative from a fiscal standpoint. This is when he talked about paying for the majority of his airplanes out of revenue. And this is why he says, this means that you're not taking on debt. When there are bad times, you aren't threatened by debt payments. And debt payments are what put other airlines in and out of bankruptcy forever. Again, study the history of the industry is like, why do you guys keep making the same mistake over and over again? Let me just avoid that. Do not worry about market share. Worry about profit. I told anybody, if they mentioned market share, I'd punch them in the nose. Just look at what's going on in the industry. These big companies are fighting over market share and they're losing money. They were firing their employees. Let's focus on profits. If we have 4% of the market and we are profitable, that is better than having 90% of the market and being unprofitable. And that kind of thinking leads us into this. Southwest Airlines is obsessed with keeping cost lows to maximize profitability instead of being concerned with increasing market share. Kelleher believes that confusing these two concepts has derailed many other airlines. Market share has nothing to do with profitability, he says. Market shares just says, we just want to be big. We don't care if we make money doing it. That is what misled much of the airline industry the past 15 years. In order to get an additional 5% of the market, some of these companies increase their costs by 25%. That is really incongruous if profitability is your purpose. Southwest is willing to forego revenue generating opportunities in markets that would disproportionately increase its costs. And so we're going to get into a few ideas to help them keep their costs low. Before I get there, I came across something else that I love, that you need to know what you compete with, not just who. From the very beginning, if you go back to the Golden Triangle, they're like, hey, driving between these three destinations is a pain in the ass. He knew from the jump the fact that most people are not flying, that ground transportation is his competitor, not other airlines. When Brandon's price between Dallas and San Antonio was \$62, Southwest charged 15. One of Southwest shareholders approached Kelleher and asked, don't you think we could raise our prices just two or three dollars? You don't understand, said Kelleher. We're not competing with other airlines. We're competing with ground transportation.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

At \$15, you're going to fly maybe at 20 or 22 or 24,
which is still way less than 62, right?

Maybe you don't.

The calculus changed.

Kelleher had the discipline to know what he was competing with, not just who.

And so one of their main ideas that differentiated them from many of their other competitors is the fact that they refuse to diversify on what kind of plane they would only fly the Boeing 737.

Other airlines had multiple different aircrafts.

And this is why this idea was so valuable to them.

And I guess before I read this to you, what was fascinating is if you compare how many employees does Southwest need for every aircraft that they own?

So the rest of the airline industry, this is not just people that work on the plane, obviously the administrators, everybody else in the company, right?

The rest of the airline industry ranges from 115 to 160.

115 to 160 employees per aircraft.

Southwest had 84 employees per aircraft at the high end of their industry, 160.

That means they're half.

They need half the amount of employees.

So it says flying one type of aircraft has a strong impact on the bottom line.

Training requirements are simplified.

Pilots, flight attendants, mechanics, and provisioners concentrate their time and energy on knowing the 737 inside and out.

All Southwest pilots are qualified to fly.

All flight attendants are qualified to serve in.

All maintenance people are qualified to work on.

And all provisioning crews are qualified to stock every plane in their fleet.

This makes it easy for them to substitute aircraft.

Reschedule flight crews are transfer mechanics quickly and efficiently.

With only one type of aircraft, the company will reduce its parts inventory and simplify its record keeping, which also results in savings.

It also helps the company negotiate better deals when acquiring new planes because they're only going to buy the Boeing 737.

And so this commitment to being cost-conscious to watching their costs is preached up and down in the organization.

And so this is happening in 1989.

At this point, you actually got physical receipts or physical tickets.

And so for the last 15 years of their existence or something like that, they would just issue, your ticket was your receipt.

So Southwest issued cash register receipts as tickets.

Now here's the problem.

It's growing.

More people, they're getting, they're expanding the market.

They're getting more new customers that are unfamiliar with the way Southwest does things.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

And since no other airline was using the receipt as the ticket, sometimes these customers would throw, accidentally throw away their receipt, therefore accidentally throwing away their ticket.

And so they're having a meeting like, oh, what are we going to do?

And again, it's amazing how much the behavior of peer companies is just going to be imitated. In fact, there's a great line about this in Warren Buffett shareholder letters. Let me read it to you real quick.

He says, the behavior of peer companies, whether they are expanding, acquiring, setting executive compensation or whatever will be mindlessly imitated. You have to remember that because what happens?

They have a problem.

Oh man, we have people are throwing away their tickets.

What's the solution?

And so they go around like, well, what is everybody else doing?

They're using these super expensive, multi-layered airline ticket systems. We'll just go out and buy one of that.

That is our solution.

So it says an obvious alternative.

We should buy a multi-million dollar system that produced a traditional multi-layered airline ticket.

In other words, let's mindlessly imitate the behavior of our peer companies. Somebody spoke up in the meeting.

They're like, that doesn't make any sense.

There has to be a cheaper way to solve the problem than spending \$2 million.

And so he said, why don't we just print, this is a ticket in big, bold, red letters on the receipt instead of spending \$2 million to follow the rest of the industry.

Southwest modified its ticket stock with the caption and it worked.

And the people inside and outside your company come up with this because they all know what they do best.

They know their niche.

They know the importance of having the lowest cost structure possible.

And so this is something that Keller will repeat over and over again.

The way I think about this is like the maxim I use in my own life is if you go to sleep on a win, you'll wake up with a loss.

Keller has said on many occasions, a company is never more vulnerable to complacency than when it's at the height of its success.

The number one threat is us, he would say.

We must not let success breed complacency, cockiness, greediness, laziness, indifference, preoccupation with non-essentials, bureaucracy, or hierarchy.

We will let our niche define how we operate.

And this is what he says.

We don't care whether we fly to Paris.

We don't care whether we have a 747.

What we're focused on is being profitable and job secure.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

If people didn't pay much attention to Southwest Airlines because it appeared to be a much smaller regional carrier, it was just immaterial to us.

We set ourselves up to go into a specific niche.

And the heading he uses to describe the idea of what he's talking about is know what you do best. He elaborates on this idea a few pages later.

We never try to be like other airlines, Keller heard said.

From the very beginning, we told our people question it, challenge it.

Remember, decades of conventional wisdom has led the airline industry into massive losses. So you and I talked at the very beginning, if you looked at how Herb Keller ran his company, he was individual opportunity driven to use another line from Buffett.

And he said that reality is chaotic and that planning is orderly and logical and the two don't square well with another.

And the fact that US Air, if they're going to go out of business and have six planes for sale and some gates that Southwest can take over, they don't call him and tell them before him. So Keller has this like fierce hate and dislike for bureaucracy and he prefers flexibility and maintaining that flexibility is what allows him to go after these individual opportunities as they appear.

And so here's another example of that.

The Southwest team arrived at midnight.

They just flown into Chicago from Texas and turned on the televisions in the hotel rooms just in time to hear Midway Airlines announce that it was out of cash and closing its doors, confirming the rumors that had brought them to Chicago on this sudden trip.

Speed, another thing that Herb would optimize for.

They pounce on deals quickly and they close deals quickly.

So that happens the night before.

At midnight, the night before, the rumors confirmed.

9am the next morning, Southwest team started negotiating with city officials in Chicago for the use of the bankrupt airline's gates.

By 2.30 that afternoon, they hammered out a deal.

They agreed they'd give them \$20 million to have immediate use of the gates.

By 3pm, there's a press conference with the mayor of Chicago to announce the deal with Southwest.

And there's a great question that happens at this press conference.

A reporter asks, when Chicago could expect to see some sign of Southwest commitment to the expansion?

The reply, go to the airport.

You'll see it right now.

Southwest had already gone to the gates, started installing their computers, started rebuilding the podiums and then started putting up their signs right over the top of the midway airlines signs.

The company was able to capitalize on this opportunity because Southwest was, in the words of their COO, nimble, quick and opportunistic.

And so this next quote from Bill Gates actually combines two of these ideas that is a main reoccurring theme in the life and the career and in this book of Herb Keller.

The fact that he wants to be flexible so he can adapt to new opportunities as they arise

and he wants to spend time learning from history so he could avoid their mistakes.

And this is what Bill Gates says in this book.

When we look back at the last 20 years, it is obvious that a number of large companies were so set in their ways that they did not adapt properly and lost out as a result.

20 years from now, we'll look back and we'll see the same pattern.

And so one practice that helps Southwest be opportunistic and be individual opportunity driven is they have these meetings that they call future scenario generation.

And essentially just getting a bunch of people in a room and just asking a bunch of what if questions and trying to say, hey, what if this hypothetical scenario happens?

How would we respond? Southwest prepares for the future by practicing the art of what if.

Future scenario generation is the technical name for this process.

They create future scenarios in which the airline could find itself.

These situations include a lot of what if questions.

What if we open one or two new cities in the New England area?

How will the competition respond?

What if Chicago builds a new airport?

How many airplanes will we need and where will we get them?

How will this affect the business?

The result of these discussions is a set of multiple plans that reduces the likelihood that Southwest would get caught off guard.

So a love of speed and a bias for action or traits that her would require from everybody working in Southwest.

Sometimes people would come in from large companies and not realize the pace that he wanted to push.

And the way to think about this is if you're going to be small, which they're much smaller than most other airlines at this point, you have to be fast.

So says Kelliher illustrates the speed with which Southwest moves by telling a story about Don Valentine, a former vice president of marketing.

Valentine had just joined Southwest from Dr. Pepper when the marketing group met in January, remember the word January, to discuss a new television campaign.

Valentine was ready with his timeline for producing these spots for these new TV ads, right?

The commercial could be scripted by March.

They're in January for God's sake.

So they're having this meeting in January.

He's saying the commercial could be scripted by March.

Script approval could be completed in April, 30 days to approve a script, good God.

The casting would happen in June, I don't know what the hell they did for those two months, and the company could start shooting in September.

What are you doing?

When Valentine finished outlining his schedule, Kelliher said, Don, I hate to tell you, but we're talking about next Wednesday.

The new vice president quickly became accustomed to the speed with which Southwest operates. This guy came in and thought nine months away was fine.

[Transcript] Founders / #322 Herb Kelleher (Southwest Airlines)

And Kelliher was like, no, dude, you got six days, nine months is way too slow. And so let's go back to another reoccurring belief that Herb Kelliher had, the fact that you should take your competition very seriously. In fact, he would imbibe his company directors with a lot of Winston Churchill references. He talked about wanting his company to have a battle of Britain kind of mentality, and he was constantly hammering this fact that success must be earned over and over again, or it disappears. If you go to sleep on a win, you'll wake up with a loss. And so they have this giant, the biggest airline in the world now taking aim at them. And so he writes this letter to all of his employees and he called it commencement of hostilities. And it says these excerpts show the intensity with which he can create a sense of urgency. Now this is Herb talking. United Airlines has become the largest airline in the world seven times the size of Southwest. The world's largest airline has recently announced that it will launch its initial direct assault against Southwest in the western part of our route system. The initial attack will utilize 25 new planes. An additional hundred airplanes are in reserve to be hurled against us at a later date. United has on hand over a billion dollars in cash. Southwest has nowhere near that at this point. So he says our stock price, our wages, our benefits, our job security, our expansion opportunities and foremost our pride of accomplishment as one of the nation's best airlines are all on the line. At its beginning Southwest routed Braniff, Trans Texas and Continental with three airplanes. Southwest can thwart United's actions against us with our 200 airplanes. The crucial elements are the vigor, the dedication, the energy, the unity and the devotion to warm, hospitable, caring and loving customer service of all of our people. Winston Churchill stated success is never final. Indeed, success must be earned over and over again or it disappears. I am betting on your minds, your hearts, your souls, your spirits to continue our success. Let's win this one and make aviation history again. And you see that Keller realizes that it's really important to use memorable language. I'm sure you've read a bunch of letters from the CEO of the founder that's boring as hell. That there's a lot of things but it's not boring. So he constantly over and over again, there's a ton of examples of Herb intentionally using memorable language. And then I just love this story really talks about the benefits of curiosity, the fact that the benefits of curiosity are unpredictable. And if you read a lot, your life will just be more interesting. As a result, you'll also be better at your job. It's such low hanging fruit. It's amazing. Keller is a voracious reader who digs deeply into issues to understand them thoroughly. It is not unlike him to go on a book buying binge and spend \$400 or \$500 at his favorite bookstore. When his son David was studying physics in college, Keller started reading up on the subjects so the two of them could converse. Keller once bought a 300 page history of Richmond, Virginia, and read it before speaking there. So he's going to speak in an event. What does he do? He reads an entire 300 page history before he goes to this area. And this is the result he ends up having dinner at some old line Virginians home talking about the history of Richmond. They go around the city and herb is pointing out places of historical importance. He didn't do it to show off he did it because he was going to a new place and he loves history. And on the very same page is a great quote, the illiterate of the future will not be the person who cannot read, it will be the person

who does not know how to learn. And after more than 20 years of running a successful profitable company, Keller was asked if he had any advice for other chief executive officers, his reply, spend more time with your people and less time with other CEOs. Our motto was only the strong survive because our balance sheet was conservative, because our operating costs were low, because our

customer service was legendary, and because our people have the hearts of lions, the strength of elephants, and the determination of water buffaloes. We did indeed survive.

And that is where I'll leave it for the full story. You can read both books. I don't think there is a perfect, I think there's a gap in the market. There has yet to be and there should be a comprehensive book on herb, Kelleher. But if you do want more and you're willing to read a lot to get it, I will leave links for both books down below. If you buy the books using the links in the show notes on your podcast player or at founderspodcast.com, you'll be supporting the podcast at the same time. Another great way to support the podcast is join my email newsletter. For every book that I read, I send you my top 10 highlights that is the entire email. If you haven't already joined that, that link is down below and available at founderspodcast.com. That is 322 books down 1000 to go. And I'll talk to you again soon.

I'm glad you made it to the end. Founders listeners are not quitters. If you have not already signed up for the Founders AMA private feed, I highly recommend doing that right now. I will leave a link down below, but it's also always available at founderspodcast.com, because the insane amount of research that I have done over the last seven years for this podcast, I have a very unique set data set that's available nowhere else.

There's over 20, I've read over 100,000 pages where like 315 books or something like that. I have somewhere between like 20 and 21,000 highlights and notes from this project. 90% probably over 90% of my highlights and notes never make it onto the podcast. Yet the information contained in them is excessively valuable. So what I did is like I constantly getting questions all the time, right? And I look at them like they're unique prompts to try to get some of this information out of my head and out into the world. So it's actually useful to you. And one way to do this. So everybody benefits is by actually making a private AMA feed. So if you become a member, you'll be able to ask me questions directly. There's a private email address that you get in the confirmation email after you sign up. Do not share that email address because I read every single one of these emails myself. I don't have an assistant doing it. I'm the only one that has access to that email. So I read every single one myself. Now the questions that I get from these emails I turn I answer and I turn them into short AMA episodes. So that allows other members to learn

from the questions of other members. You can also add a name and link to your website with your question so that other members can check out what you're working on. I've already got I've already heard from subscribers to the AMA feed that they've actually got new paying customers from people that discovered their business from an AMA question. I plan on making several new episodes every week. If you are an enthusiast of Founders Podcast, I highly recommend that you become a member. You can join by using the link that's in the show notes on your podcast player or we're going to FoundersPodcast.com.