

THE

Real Spelce

AUSTIN LETTER

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Dear Client:

Storm clouds that have hovered over Central Texas for the past several weeks have been buffeting the Texas-based airline that flies through Austin skies more than any other. But it's a different kind of turbulence causing concern for Southwest Airlines.

For years now, we have written how Southwest Airlines has outclassed the competition since 9/11 crippled the industry. **With lower costs than its rivals, Southwest was one of the few air carriers to remain profitable. It didn't lay off employees** at a time other airlines were reducing employees right-and-left. It smartly locked-in lower jet fuel prices before fuel costs soared out of sight, raising operations costs for other airlines. But highflying Southwest is now coming back down-to-earth as its competitors are copying some of Southwest's practices.

In some ways, Southwest is similar to Round Rock's Dell Inc. Both relied on low operational costs to expand rapidly and now both are struggling as their competitors have cut costs and are coming back strongly. And like Dell, Southwest is going through a major overhaul in its strategy.

To combat lagging profits, low-fare Southwest is adding flights to profitable markets (i.e., **a new nonstop between Austin and Denver**) and trimming 39 flights nationwide. It is not expanding as much as planned, adding only 19 new Boeing737s next year instead of 34. It is revising its marketing strategy to more precisely target corporate travelers. There's more. You get the picture.

In spite of its bent-not-broken model, Southwest maintains its dominance as the airline of choice for Austin air travelers. In May 2007, Southwest carried 270,068 Austin passengers, up 3% compared to May 2006. American Airlines, in 2nd place, tallied 213,757 Austin travelers, up 3.5%. In 3rd place, Continental Airlines, was way back with 95,237, up 9.5%. As befits a dynamic economy, there were more travelers using Austin-Bergstrom International Airport (ABIA) in May 2007 than in any previous month, anytime in history.

May, with a 6% overall increase in travelers, was not an aberration. **Passengers at ABIA have been steadily increasing all year. In fact, through May, the number of Austin air travelers is up 5% compared to the year before.** This includes business and leisure passengers and is indicative of Austin's strong economy. It's important to have a healthy Southwest Airlines, as well as the other airlines, to service the needs of the Austin marketplace.

Sure, you try to shop local Austin merchants when possible but, admit it, you've gone to the "big box" stores when the need arises and now, the major high-volume retailers are fine-tuning their operations for your benefit.

Wal-Mart, Target, Best Buy, Circuit City, Home Depot, Lowe's, Costco, etc. are all tweaking how they serve their customers once the shopper is inside their big box stores. They appear to have heard shopper complaints and, almost in lock-step, these stores are trying different tactics to respond to those complaints. **"Hearing complaints" also means the stores have been hit on the bottom line for the most part and they are shooting for pumped-up profit numbers by catering to customer concerns.**

Such as? Well, Wal-Mart, for instance, found its average shopper spends 21 minutes in the store but **finds only seven of ten items** on his or her shopping list. Bingo! If Wal-Mart can only help its customers find all ten items on the list during that 21 minutes, profits will increase and the customer will be more satisfied.

While this may seem pretty basic, it's not how these huge stores operated from day-one. **Wal-Mart and the other big box stores for years thought the way to grow was simply to build bigger boxes and stuff them with a huge assortment of items at low prices.** That's it. Now a new word is creeping into their planning – *convenience*.

Experimenting in "convenience" is the new emphasis. Best Buy is employing "personal shopping assistants" in 60 stores. They wear button-down dress shirts (so they stand out from the polo-clad salespeople) and they are there to help customers make decisions on complicated purchases such as home theater systems. Not to be outdone, Circuit City has distributed computer tablets to salespeople in 20 of its stores to call up product specs to compare features.

Target and Wal-Mart have clustered all baby items – clothes, diapers, baby food, strollers, even maternity clothes – in one area of their stores so moms don't have to trek from department to department. **Lowe's has installed "Need Help" buttons** in stores for customers to press if they need someone to answer questions. Home Depot already tested the buttons and is installing them in all of its 1,900 US stores. Aisles have been widened and cleared of clutter in many cases to make it easier to find items.

And all the big box stores are trying to deal with the biggest customer complaint of all. You guessed it – slow checkout lines. New cashier schedules are being put into place to handle peak customer shopping times. However, the verdict is still out on the self-checkout system (Target claims one professional checker is as fast as four self-checkout machines).

Does this mean big box stores will downsize? Not likely, if these "customer convenience" moves drive profits upward.

Speaking of local merchants, how about the battle between Austin's John Mackey, the CEO of Whole Foods, who is waging a very public war-of-words with a federal agency that can kill his latest merger deal?

Let's say it straight out: **the Federal Trade Commission (FTC) is way off-base trying to prevent the Whole Foods acquisition of the Wild Oats natural supermarket chain on anti-trust grounds.** On the surface, you may say the FTC is right-on trying to keep Whole Foods from gobbling up the chain that is trying (somewhat lamely, in smaller stores) to imitate Whole Foods approach. But the FTC lawsuit doesn't take into account consumer buying habits.

First of all, Whole Foods and Wild Oats do not compete with each other.

Wild Oats has judiciously avoided opening stores where Whole Foods is operating. The two chains may offer many of the same products, but very few if any customers choose between the two when deciding where to shop.

Secondly, Whole Foods is competing with Central Market, H-E-B, Safeway, Kroger, Wal-Mart and other supermarkets – all of whom, in varying degrees, are offering similar products to Whole Foods and are doing so “just down the street,” so to speak. (Who would've thought Wal-Mart would sell organic milk?)

Thirdly, most Whole Foods shoppers also shop in other grocery stores. After all, Whole Foods doesn't stock Diet Cokes, toilet paper, Ritz Crackers or a whole raft of other items that you'll find in most pantries in Austin and around the nation.

In other words, competition is occurring. The FTC's lawsuit claims the merger will curtail competition. Nothing could be further from the truth because the lawsuit doesn't take into account these facts we've just mentioned

Well, as you can imagine, this has royally ticked-off Mackey, the very independent minded Libertarian, who has never been shy about speaking his mind. **Most PR people would've advised Mackey to not sound off with negative comments about the FTC while it held sway over the fate of his merger.**

But the Austinite, who started with nothing when he opened the first Whole Foods market on North Lamar Boulevard and has grown his enterprise to a \$5 billion dollar operation in 27 years, **marches to his own drummer and not to the beat of PR folks.** So, he has roundly criticized the FTC publicly. Where this “food fight” ends up will be interesting to watch.

While we're on the subject of grocery developments, Texas-based H-E-B said this week it will stock a technology product you can attach to food containers that will tell you how long a perishable food item has been in your fridge. A 2-pack sells for \$10.

The fairly-new Austin City Limits Music Festival has hit the big time. How can you tell? Well, there's a VIP special package available for the 3-day September event that will set you back only \$1,950 per person. This offer is limited in more ways than the price tag.

If crowds, hot (and either dusty or rainy) weather, porta-potties for the masses, lines for food and beverages, etc. are not your cup of tea, American Express has a deal for you. That is, if you are an AmEx Platinum Card holder. They call it “**Hot Times and Hot Tunes in Austin, where some of the world's hottest musicians will be at the Austin City Limits Music Festival.**” Here's what you get for almost 2-thousand bucks a pop per person:

You can enjoy the music all weekend from the shade of The Grove – a cool cluster of pecan trees that “serve as a haven for listening.” The AmEx VIP package provides Grove access through the weekend “**along with a backstage meet-and-greet, complimentary food and beverage, access to air-conditioned restrooms**” and other amenities.

AmEx says “celebrations continue into the night on Friday with your invitation to an **after-show party featuring a major Festival artist.**” But it doesn't stop there: “The event ends with a Texas-style Sunday Brunch featuring another Austin band. The fun is unlimited, but the packages are not,” says AmEx.

You are limited to a maximum of six packages per Platinum Card member. There are only 70 of these VIP packages available. The ACL Music Fest is set for Friday-Sunday, September 14-16, 2007. It will *not* compete against a home Longhorn football game at Darrell K Royal – Texas Memorial Stadium. The Horns play a 2:30 pm Saturday game against Central Florida in Orlando. If the \$1,950 per person tab is not to your liking, **you can redeem your American Express Membership Rewards® points – at a cost of 243,750 points per person.** These packages are available now until they are scarfed up.

Taking note of the large number of road closures in Central Texas due to high water, **Dr. Louis Overholster** says it is easy to know which roads are closed: the speed limit on them is 35 knots.

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Sincerely



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