



**THE FREEDOM TO FLY  
FROM VISION  
TO REALITY  
TO AFFORDABILITY**

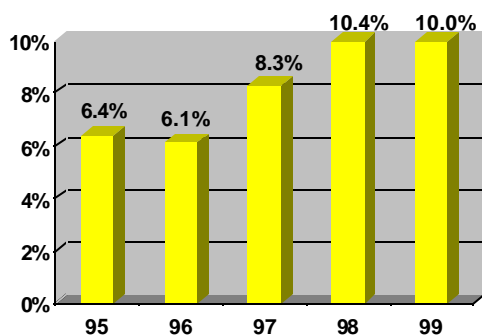
**SOUTHWEST AIRLINES CO. ANNUAL REPORT 1999**

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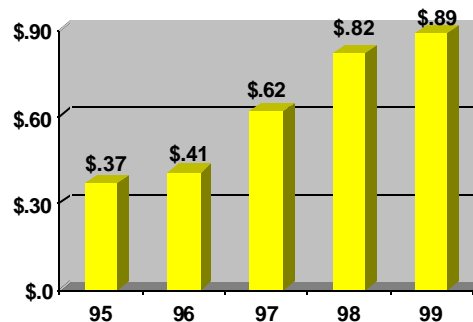
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**CONSOLIDATED HIGHLIGHTS**

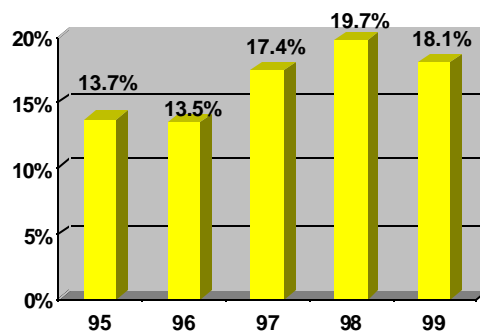
(DOLLARS IN THOUSANDS EXCEPT PER SHARE AMOUNTS)	1999	1998	CHANGE
Operating revenues	<b>\$4,735,587</b>	\$4,163,980	13.7%
Operating expenses	<b>\$3,954,011</b>	\$3,480,369	13.6%
Operating income	<b>\$781,576</b>	\$683,611	14.3%
Operating margin	<b>16.5%</b>	16.4%	0.1 pts.
Net income	<b>\$474,378</b>	\$433,431	9.4%
Net margin	<b>10.0%</b>	10.4%	(0.4) pts.
Net income per share – basic	<b>\$.94</b>	\$.87	8.1%
Net income per share – diluted	<b>\$.89</b>	\$.82	8.5%
Stockholders' equity	<b>\$2,835,788</b>	\$2,397,918	18.3%
Return on average stockholders' equity	<b>18.1%</b>	19.7%	(1.6) pts.
Stockholders' equity per common share outstanding	<b>\$5.62</b>	\$4.76	18.1%
Revenue passengers carried	<b>57,500,213</b>	52,586,400	9.3%
Revenue passenger miles (RPMs) (000s)	<b>36,479,322</b>	31,419,110	16.1%
Available seat miles (ASMs) (000s)	<b>52,855,467</b>	47,543,515	11.2%
Passenger load factor	<b>69.0%</b>	66.1%	2.9 pts.
Passenger revenue yield per RPM	<b>12.33¢</b>	12.62¢	(2.3)%
Operating revenue yield per ASM	<b>8.96¢</b>	8.76¢	2.3%
Operating expenses per ASM	<b>7.48¢</b>	7.32¢	2.2%
Number of Employees at yearend	<b>27,653</b>	25,844	7.0%



Net Margin



Net Income Per Share, diluted



Return On Average Stockholders' Equity

## THE FREEDOM TO FLY

was first envisioned and sketched in the late 15th century by Leonardo da Vinci, the Italian master painter, sculptor, architect, and engineer. At the turn of the 19th century, Leonardo's vision became reality when Orville and Wilbur Wright ushered in the Age of Flight at Kitty Hawk, North Carolina. Seven decades later, Southwest Airlines made commercial flight affordable. As we stand on the threshold of the 21st century, we are proud to be part of a vision that has resulted in one of America's most basic freedoms — affordable flight.

**Southwest Airlines Co.** is the nation's low-fare, high Customer Satisfaction airline. We primarily serve shorthaul city pairs, providing single-class air transportation that targets the business commuter as well as leisure travelers. The Company, incorporated in Texas, commenced Customer Service on June 18, 1971, with three Boeing 737 aircraft serving three Texas cities — Dallas, Houston, and San Antonio. At yearend 1999, Southwest operated 312 Boeing 737 aircraft and provided service to 56 airports in 29 states throughout the United States. Southwest has the lowest operating cost structure in the domestic airline industry and consistently offers the lowest and simplest fares. Southwest

also has one of the best overall Customer Service records. LUV is our stock exchange symbol, selected to represent our home at Dallas Love Field, as well as the theme of our Employee and Customer relationships.



## TO OUR SHAREHOLDERS :

In 1999, our magnificent People brought the Freedom to Fly to 57,500,000 Customers originating their journeys in every geographic region of the United States. Leonardo da Vinci conceived powered flight; the Wright brothers invented powered flight; but Southwest's People have transformed the idea and the invention into an everyday opportunity and reality for the people of the United States. The personal and business lives of the American people have been extended and enriched by this Freedom, and Southwest's People appropriately take immeasurable pride in doing well for themselves by doing great good for others. Our People are, every day and in every way, emotionally engaged in a compelling cause and crusade: to bring the Freedom to Fly to ever more American people. As evidenced by our 57,500,000 originating Customers in 1999, the Freedom crusade of our People is succeeding, and may it ever be thus.

1999 was Southwest's 27th consecutive year of profitability; job security; plentiful Profitsharing; and adding value for our Customers and our Shareholders. It was also Southwest's eighth consecutive year of increased profits. Our 1999 earnings of \$474.4 million (a 9.4 percent increase over 1998), however, would have been substantially greater save for one depressant of seminal significance: the rapid escalation of jet fuel prices in the second half of 1999, bringing them close to 1991 Desert Storm levels at the end of the year and the beginning of 2000.

In fourth quarter 1999, on a year-over-year basis, Southwest's unit revenues (per available seat mile) increased by 1.6 percent and Southwest's unit costs, excluding fuel, decreased by 1.1 percent. The combination of improved unit revenues and improved unit costs would be an ideal harbinger of improved profitability in 2000 were it not for the uncertainty with respect to jet fuel prices over the course of the year.

Since Southwest can neither control nor predict definitively the level of 2000 jet fuel prices, we have embarked upon a program to offset the potentially adverse effects of greatly enhanced jet fuel costs by increasing unit operating revenues while simultaneously decreasing nonfuel unit costs. If jet fuel costs continue at sharply elevated levels, earnings

comparisons will be particularly difficult in the first half of 2000, as our jet fuel expenses in the first half of 1999 were unusually low.

We anticipate that our year 2000 increase in capacity will exceed 12 percent in terms of available seat miles and that we will open at least one other city, in addition to Albany, New York, where service begins to Baltimore/Washington, Orlando, and Las Vegas on May 7, 2000. Our 1999 new city additions of Islip, Long Island; Raleigh-Durham, North Carolina; and Hartford/Springfield, Connecticut, have been exceeding our traffic generation projections.

According to *Fortune* magazine surveys, Southwest has again been voted one of the most admired companies in the world; the most admired airline in the world; and one of the best places to work in America. All of these encomia are attributable to one shining glory: the devoted excellence of our People. They are our preeminent strength, and their presence and dedication make any time the best of times.



Most sincerely,

Herbert D. Kelleher  
Chairman, President, and Chief Executive Officer  
January 23, 2000

**Leonardo da Vinci first envisioned man's flying in the 15<sup>th</sup> century. "A bird is an instrument," he said, "[which is] within the capacity of man to reproduce with all its movements."**



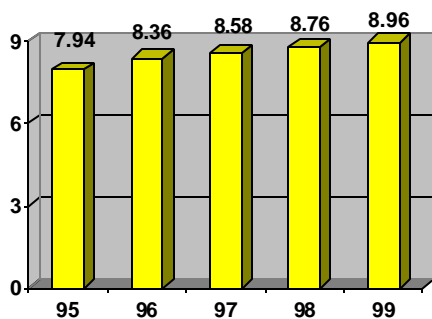
The Freedom to Fly is a 500-year-old dream. The dream that became Southwest Airlines was first envisioned in the 1960s as something very different from other airlines. At the core of the strategy was a belief that shorthaul market needs were not being met. Fares were too high, flight schedules were inconvenient, ticketing was too complicated, and the time required to drive to the airport, park, and takeoff was too long and inconvenient. It was just easier to drive a car. So Herb Kelleher and Rollin King set out to design a shorthaul, intra-Texas airline, with two primary objectives: 1) meeting Customers' shorthaul travel needs and 2) making fares competitive with the automobile.

In shorthaul markets where driving is a viable option, Herb and Rollin knew speed and convenience were essential to success. Therefore, Southwest was designed to minimize total travel time, including ticketing and boarding. Additionally, Southwest served convenient airports, like Dallas Love Field and Houston Hobby.

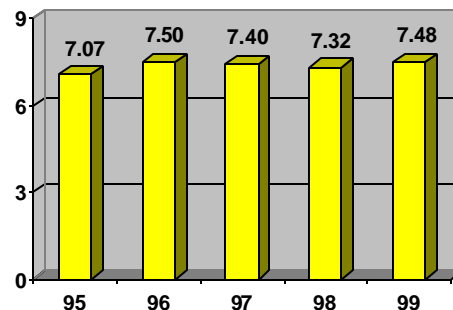
Herb and Rollin recognized that Southwest might not be all things to all Customers. They didn't plan to fly everywhere and didn't plan to build hub or connecting complexes at airports. Instead, they focused on meeting the needs of point-to-point, shorthaul Customers since no other airline was doing a good job of meeting those needs.

Herb and Rollin knew they must have low costs to offer low fares. After all, a business needs to make a profit. So they envisioned an operation that was far superior in terms of efficiency, productivity, and just plain common sense. Since they focused on the shorthaul market niche, they concluded a single aircraft type made sense for Customers and it would certainly be more efficient. Reservations could be made, but seating would be open. Assigned seating was not in the vision because we consider *all* of our seats as "first class!" On short flights, meals aren't necessary. What is necessary for the shorthaul Customer is consistently low fares; reliable, ontime flights; and friendly Employees to assist with travel needs and to ensure that baggage is delivered immediately and without damage.

Herb and Rollin never envisioned that Southwest would be the "biggest" airline, or be the one with the most exotic route system, or operate the biggest airplanes. What they did envision, though, is the Freedom to Fly for our Customers; a safe and high-quality operation; an exceptional Service to Customers; a great place to work; and the most profitable airline.



Operating Revenues Per Available Seat Mile  
Mile (in cents)



Operating Expenses Per Available Seat  
Mile (in cents)



**Wilbur and Orville Wright made Leonardo's dream a reality at Kitty Hawk, North Carolina, on December 17, 1903. Their *Flyer* stayed aloft for 12 seconds and flew 120 feet.**

Southwest Airlines learned a powerful lesson from the Wright Brothers' historic short flight: low fares are even more important in our shorthaul niche. And Southwest was designed and built primarily for shorthaul Customers. We operate on a point-to-point basis, as opposed to hub-and-spoke, focusing on the needs of local Customers. We do not interline with other jet carriers or have any commuter feeder relationships. As a result, 70 to 80 percent of our Customers fly nonstop.

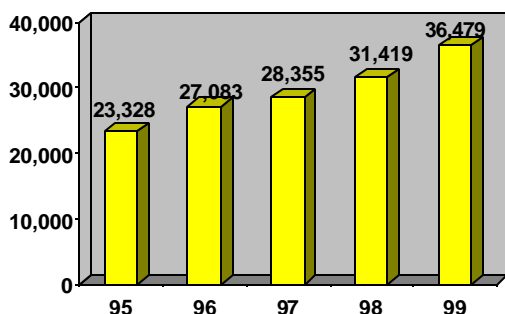
Our extensive point-to-point route system provides more direct routings than hub-and-spoke systems to better serve the needs of business as well as leisure Customers. Business travelers especially want convenience. So we offer frequent flights on our shorthaul routes, on the order of eight or more times a day. For example, Dallas-Houston has 40 roundtrips a day. At the end of 1999, we operated 2,550 daily departures to 56 airports, or 46 departures per airport. Although we do not serve as many airports as our major airline competitors, we generally have substantially more flights over the routes we serve.

Over the last several years, we have added more longhaul flights to our route system. However, the vast majority (almost 90 percent) of our daily departures average less than an hour flight time. Longhaul flights are offered in low frequency; achieve high load factors with our classic low fares; and offer a nice complement to our core high-frequency, shorthaul, business-oriented route structure. After all, our business Customers take vacations, too!

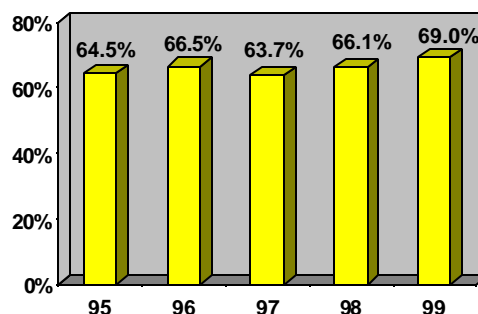
Our scheduling strategy also includes careful airport selection. Our focus is on efficiency and convenience. So we avoid many of the congested, slot-controlled, and hub airports. This contributes to avoiding delays, maintaining high ontime performance, and minimizing our Customers' total travel time. We favor conveniently located satellite or downtown airports such as Baltimore, Burbank, Chicago Midway, Dallas Love Field, Ft. Lauderdale/Hollywood, Houston Hobby, Long Island, and Providence.

As a result of the combination of low fares, high frequencies, convenience, and outstanding Customer Service, we dominate the majority of the shorthaul markets we serve. We consistently rank first in market share in approximately 80 to 90 percent of our top 100 city pairs and, in the aggregate, hold 60 to 65 percent of total market share.

Southwest also carries the most passengers in the top 100 U.S. markets despite serving only 45 of them.



Revenue Passenger Miles (in millions)



Passenger Load Factor

**Herb Kelleher and Rollin King didn't invent the airplane. But they did do something that the Wright Brothers must surely have dreamed about. They made flying affordable.**



In 1971, Southwest Airlines made flying affordable. And making flying affordable to Americans is the essence of what we stand for: the Freedom to Fly. Low fares, every seat, every day. And low fares are essential to our shorthaul business strategy, where we compete with ground transportation as well as other airlines.

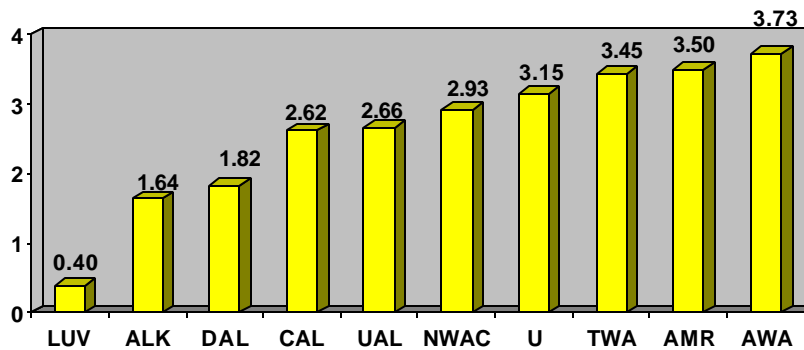
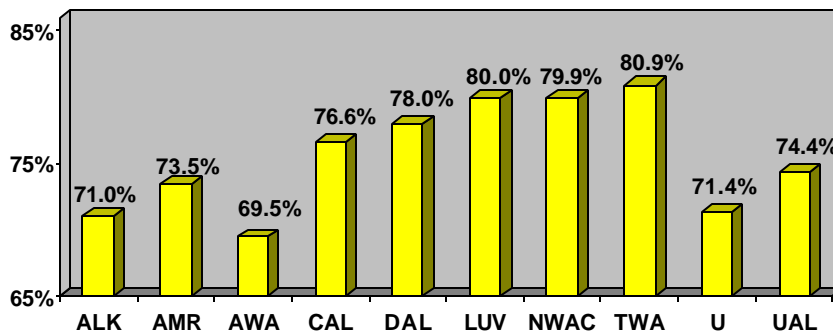
Our fare structure is simple, too. And that makes it easy for Customers to understand and allows maximum flexibility. Currently, we still have few restrictions on tickets: no Saturday night stay requirement and no rebooking or exchange penalty fee if you change your plans. It's simple and it's fair.

We have long held the reputation as THE Low Fare Airline. Customers think "low fares" when they think Southwest. As a result, most Customers contact us directly, either by calling toll-free to one of our nine reservation centers (located in Salt Lake City, Phoenix, Albuquerque, Oklahoma City, Dallas, San Antonio, Houston, Chicago, and Little Rock) or logging onto our web site at [www.southwest.com](http://www.southwest.com), one of the most successful travel sites on the Internet. Our distribution system is easy and convenient for Customers and very cost-effective and efficient for Southwest.

In addition to our low fares, frequent Customers receive Rapid Rewards. After purchasing and flying only eight roundtrips on Southwest, Customers receive a roundtrip ticket, good for travel anywhere on our system for up to a year. And there are no restrictions on the number of Rapid Rewards seats and very few blackout dates around holidays. It's by

far the most generous frequent flyer program in the industry. In fact, our Rapid Rewards program was recently honored at the annual “Freddie” Awards for having the Best Customer Service, Best Award Redemption, and Best Bonus Promotion among all frequent flyer programs. Customers can also earn flight credits through purchases with our travel partners (Alamo, American Express, Budget, Diners Club, Dollar, Hertz, Hilton, Marriott, MCI WorldCom) as well as through the use of the Southwest Airlines Rapid Rewards Visa card.

Ontime Performance (for the year ended December 31, 1999)



Customer Satisfaction

(complaints per 100,000 Customers boarded for the year ended December 31, 1999)



**Leonardo had the dream. Orville and Wilbur made it a reality. Herb and Rollin made the reality affordable. What do you do for an encore? Teach a whale how to fly!**

In 1988, in honor of our historic partnership with SeaWorld of Texas, we painted a Boeing 737 like a killer whale. To be fun, affordable, and profitable takes some doing. It takes low costs. By the 1980s, we were well known as the low-cost producer in the airline



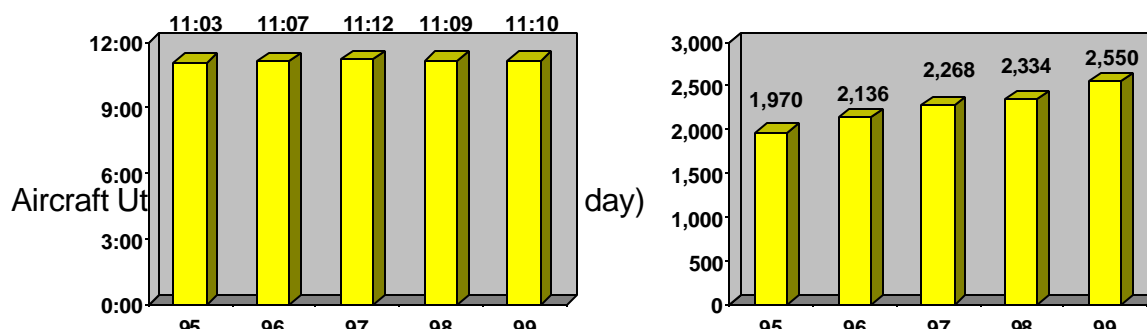
industry. On an equivalent aircraft trip-length, our cost per available seat mile is the lowest in the industry and, in some cases, half of our competitors. Logically, this gives us an enormous competitive advantage to profitably offer the lowest fares.

The key to our low costs is our high productivity. We consistently demonstrate the highest asset utilization of any U.S. airline. Because we schedule point-to-point for local passengers, not connections, we minimize the amount of time the aircraft is at the gate, less than 25 minutes. This results in higher aircraft and airport utilization and, therefore, fewer aircraft and airport facilities than we would need otherwise. And it allows our Employees to be more productive.

One aircraft type, the Boeing 737, is operated by Southwest. This significantly simplifies our operation, in terms of scheduling, staffing, training, and maintenance. And it certainly contributes to lower costs. As the launch Customer for Boeing on the -300, -500, and, most recently, -700 models, we achieve attractive aircraft acquisition costs. This, coupled with our young, well-maintained fleet, allows us to produce low overall costs of ownership.

Our reputation as THE Low Fare Airline, with legendary Customer Service and significant flight frequencies, enables us to lower our distribution costs versus our airline competitors. Almost 70 percent of our seats are sold directly by Southwest versus an industry average of 10 to 15 percent. Almost 80 percent of our seats are sold Ticketless, which eliminates significant paper and back-office processing. Ticketless Travel is also the foundation of sales through our web site at [www.southwest.com](http://www.southwest.com), which has seen another year of spectacular growth. Transaction costs over the Internet are cheaper than any other means of distribution and significantly contribute to our ability to keep costs low.

Our desire for low costs does not sacrifice safety or quality. We operate one of the youngest fleets in the world, despite the fact that old aircraft are significantly cheaper than new. Also we have one of the most extensive and thorough maintenance programs in the world, with an outstanding 28-year safety record to attest. Although our Employees receive competitive compensation packages, our Employee costs are low because we have the most productive and innovative People in the airline industry.





**Colleen Barrett suggested a reward for all the Employees who made us number one in Customer service, ontime performance, and baggage handling five years in a row: Paint a plane in their honor.**

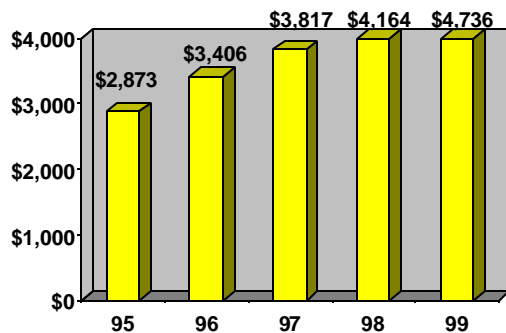
In the 1990s, our focus on Customer Service, ontime performance, and baggage handling earned us an unprecedented five consecutive annual Triple Crowns. To celebrate, we inscribed our Employees' names inside a plane christened *Triple Crown One*. The name "Southwest" became synonymous with Customer Service *and* a great place to work. It's no coincidence, as the two go hand in hand.

It's simply not enough to charge low fares and fly lots of places. To be successful, we have to provide excellent Customer Service. In 1999, more than any other year, there was tremendous scrutiny of the airline industry by the traveling public, the media, and even the U.S. government. At Southwest Airlines, our mission has *always* been dedication to the highest quality of Customer Service. And we're proud to say we conduct our business that way and the results show. In particular, for the last nine years we have led the industry in Customer Satisfaction, according to complaint statistics accumulated and published by the U.S. Department of Transportation. Southwest was also recognized during 1999 as having one of the best corporate reputations among Americans in a study conducted by Harris Interactive Inc. and the Reputation Institute.

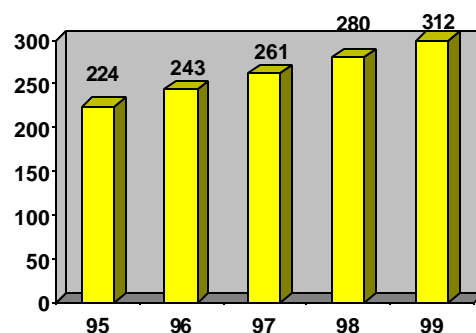
The reasons for our high satisfaction rating are numerous. We charge low fares with few restrictions. As important, we operate a reliable and dependable schedule. Through a combination of efficient aircraft scheduling, careful selection of airports, and our highly motivated and hardworking People, we consistently operate an "ontime airline" and consistently cancel very few flights. In each case, we consistently rank at or near the top compared to other airlines.

Rounding out our Customer Service strategy, we offer quick, simple ticketing and boarding with fast, friendly inflight beverage service. Our all-Boeing 737 fleet is one of the youngest in the world and is clean, safe, quiet, and comfortable. In an all coach configuration with open seating, it's perfectly suited for our market niche.

Finally, and most importantly, Customer Service is delivered by People, not computers or machines. And we have the best in the business. We go to great lengths to hire great People with the right attitude. And because we're well known as a great place to work with great career opportunities and a secure future, lots of People want to work here. That's a distinct advantage in a tight job market. Once hired, we provide a unique and supportive work environment, which encourages our Employees to be creative and have fun. As a result, our People tend to go out of their way to ensure our Customers have an enjoyable flight and are treated like guests. For the past three years, Southwest has been named by *Fortune* magazine as one of the best companies to work for in America. Each year, we've been ranked in the top five. In 1999, Southwest was also recognized by *Fortune* magazine as one of the most admired companies in America and the world and the most admired airline in America and the world. Southwest has the best Employees in America and that's why our Customer Service record is the best in the industry.



Operating Revenues (in millions)



Fleet Size (at yearend)

**Wherever the future takes us, we will always be indebted to the dreamers who gave us our first glimpse of The Freedom to Fly. We will carry your banner proudly.**



Here's to Leonardo, Orville and Wilbur, Herb and Rollin, and all the Southwest People who keep their dreams alive.

We enter the year 2000 with 312 aircraft serving 55 U.S. cities in 29 states. This year marked our 27th consecutive year of profitability and eighth consecutive year of record profits. Earnings growth over the last five years averaged 23 percent. Our return on capital was just below 20 percent versus a cost of capital of under nine percent.

There are many cities we do not serve that offer tremendous growth opportunities. As the specialist in low-fare, point-to-point service, we are unique in the U.S. And over 100 cities have petitioned us for service because they understand the favorable economic impact the “Southwest Effect” would have on their communities. After we enter a market with lots of flights and fares that are as much as two-thirds lower than fares before our entry, passenger traffic explodes, often three- or four-fold. We’ve demonstrated that our expansion is profitable, particularly considering the last five years’ results. So we’re anxious to continue growing.

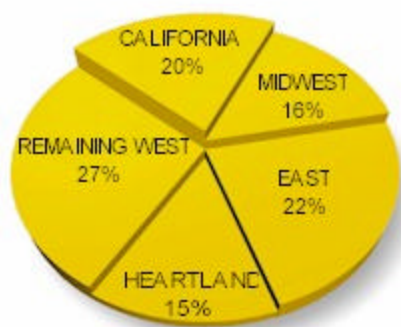
Over the last several years, we have added service to Florida and New England. In 1999, we expanded into Islip, New York, and Hartford, Connecticut. The East Coast is a relatively new region for Southwest and is anchored by Baltimore with 95 daily flights. Currently, the East represents approximately 22 percent of our route system. As the chart below shows, we plan to continue growing our 737 fleet. And with only 55 cities and eight percent of the domestic market, we have opportunities to significantly expand our route system in both new and existing cities. We will add Albany, New York, in May 2000 and at least one other city later in the year.

As a result of our low-fare, high-frequency, point-to-point strategy, we’re the largest carrier at many of the cities we serve. Our low-fare philosophy generates substantial demand which allows us to offer lots of convenient flights. For example, our top ten cities’ daily departures are currently: Phoenix, 177; Houston Hobby, 149; Las Vegas, 149; Dallas Love Field, 139; Los Angeles International, 122; Chicago Midway, 118; Oakland, 112; Baltimore, 95; St. Louis, 88; and San Diego, 78. This is very different from our hub-and-spoke competitors, which have large concentrations of flights at a couple of “hub” cities. Our Heartland region (Texas and surrounding states) constitutes about 15 percent of our capacity, while our Western region is our largest, at 47 percent. The Midwest region rounds out our system at 16 percent.

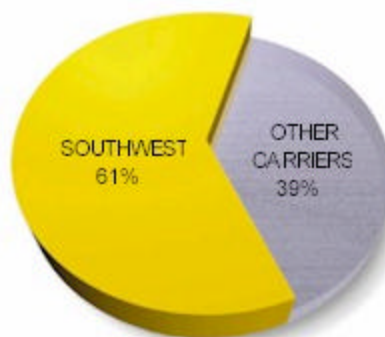
<b>Jet Fleet (at December 31, 1999)</b>			
737 Type	Seats	Average Age (Yrs.)	Number of Aircraft
-200	122	17.9	35
-300	137	8.5	195
-500	122	8.7	25
-700	137	0.9	57
<b>Total</b>		<b>8.2</b>	<b>312</b>

### Boeing 737-700 Firm Orders And Options

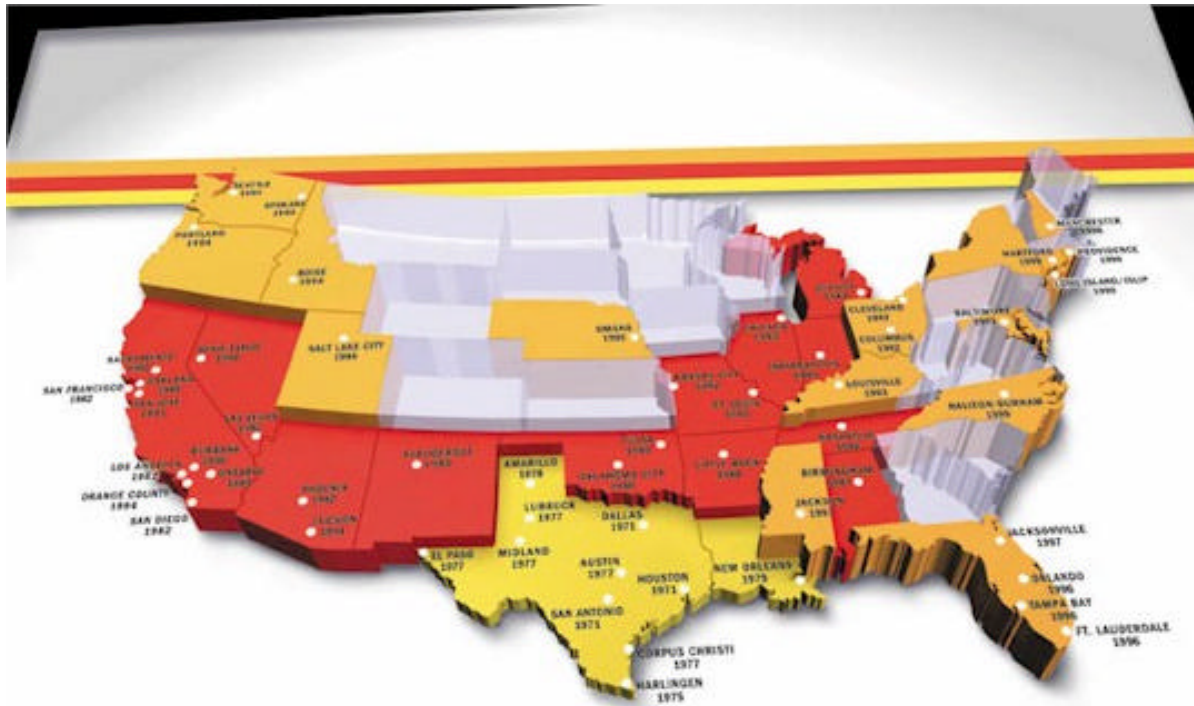
Type	2000	2001	2002	2003	2004	2005	2006	Total
Firm Orders	31	23	21	5	5	–	–	85
Options	–	–	–	13	13	18	18	62
<b>Total</b>	<b>31</b>	<b>23</b>	<b>21</b>	<b>18</b>	<b>18</b>	<b>18</b>	<b>18</b>	<b>147</b>



Southwest's Capacity By Region



Southwest's Market Share  
Southwest's Top 100 City-pair Markets



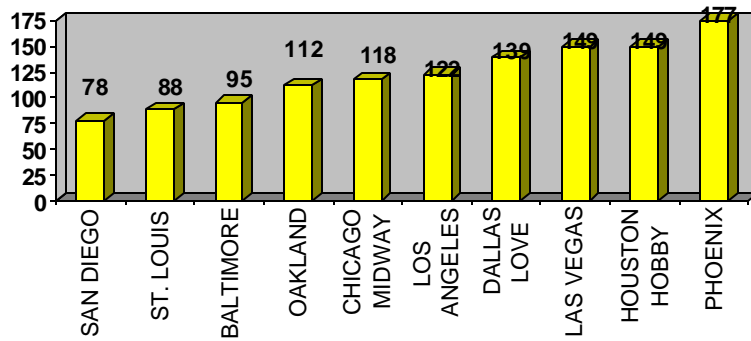
### Southwest System Map

When service starts May 7, 2000

Year	# of Markets	Markets
1971	3	Dallas, Houston (Hobby), San Antonio
1975	1	Harlingen
1977	5	Corpus Christi, Midland, Lubbock, El Paso, Austin
1978	1	Amarillo
1979	1	New Orleans
1980	4	Oklahoma City, Tulsa, Albuquerque, Houston Intercontinental
1982	6	Las Vegas, Phoenix, San Diego, Kansas City, LAX, San Francisco
1984	1	Little Rock
1985	3	Chicago (Midway), St. Louis, Ontario
1986	1	Nashville
1987	2	Birmingham, Detroit Metro
1988	1	Detroit City
1989	2	Indianapolis, Oakland
1990	2	Burbank, Reno
1991	1	Sacramento
1992	2	Cleveland, Columbus

1993	3	Louisville, San Jose, Baltimore (closed Detroit City)
1994	7	Orange County, Portland, Seattle, Spokane, Boise, Tucson, Salt Lake City, Omaha (acquired Morris Air)
1995	1	Omaha
1996	4	Orlando, Tampa Bay, Ft. Lauderdale, Providence
1997	2	Jacksonville, Jackson
1998	1	Manchester
1999	3	Islip, Raleigh-Durham, Hartford
2000	1	Albany (new service starts May 7, 2000)

Southwest's Top Airports 1999  
Daily Departures



# Southwest Airlines Co. Annual Report 1999

## Financial Review

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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#### YEAR IN REVIEW

In 1999, Southwest posted a profit for the 27th consecutive year. The Company posted record operating revenues; record operating income; the highest operating profit margin since 1981 of 16.5 percent; and a record load factor of 69.0 percent. The Company also experienced a record annual profit for the eighth consecutive year. We experienced strong revenue growth and continued strong demand for our product. Fuel prices in fourth quarter 1999 rose to their highest levels since 1991.

At the end of 1999, Southwest served 55 cities in 29 states. We targeted the East Coast for our 1999 expansion, adding service to Islip, New York, on Long Island in March 1999, Raleigh-Durham, North Carolina, in June 1999, and Hartford, Connecticut, in October 1999 and have been very pleased with the results in each of these new Southwest cities. The Company recently announced plans to commence service to Albany, New York, in May 2000 and will begin serving at least one other new city in 2000. In addition, we plan to continue to add flights between cities we already serve.

Capacity is expected to grow approximately 12 percent in 2000 with the net addition of at least 30 aircraft. The Company will purchase 31 new Boeing 737-700s scheduled for delivery during the year and has agreed to a long-term lease arrangement to acquire another 737-700 in March of 2000. In addition, two of the Company's older 737-200s are scheduled for retirement during the year.

#### RESULTS OF OPERATIONS

**1999 COMPARED WITH 1998** The Company's consolidated net income for 1999 was \$474.4 million (\$.89 per share, diluted), as compared to the corresponding 1998 amount of \$433.4 million (\$.82 per share, diluted), an increase of 9.4 percent. The prior years' earnings per share amounts have been restated for the 1999 three-for-two stock split (see Note 8 to the Consolidated Financial Statements). Operating income increased 14.3 percent for 1999 to \$781.6 million.



***OPERATING REVENUES*** Consolidated operating revenues increased 13.7 percent in 1999 primarily due to a 13.5 percent increase in passenger revenues. The increase in passenger revenues was primarily due to a 9.3 percent increase in revenue passengers carried and a 16.1 percent increase in revenue passenger miles (RPMs). The passenger revenue yield per RPM decreased 2.3 percent to \$.1233 for 1999 primarily due to an increase in average length of passenger haul of 6.2 percent partially offset by a 3.8 percent increase in average passenger fare. The Company expects the trend toward gradually increasing lengths of passenger haul to continue in 2000. (The immediately preceding sentence is a forward-looking statement involving uncertainties that could result in actual results differing materially from expected results. Such uncertainties include, but may not be limited to, competitive responses from other air carriers and general economic conditions.)

The 16.1 percent increase in RPMs in 1999 exceeded the 11.2 percent increase in available seat miles (ASMs), resulting in an increase in load factor from 66.1 percent in 1998 to 69.0 percent in 1999. The 1999 ASM growth resulted from the net addition of 32 aircraft during the year. Favorable load factor and revenue trends continued in January 2000. The load factor for January 2000 was 60.1 percent, up .9 points from January 1999's load factor of 59.2 percent.

Freight revenues increased 4.6 percent in 1999 compared to 1998 primarily due to added capacity and modest rate increases. Other revenues increased 31.0 percent in 1999 compared to 1998. Approximately 54 percent of the increase was due to increased revenues from the sale of flight segment credits to marketing partners in the Company's Rapid Rewards frequent flyer program, and approximately 33 percent of the increase was due to an increase in charter revenue. Beginning January 1, 2000, the Company will change its method of accounting for the sale of flight segment credits. See Recent Accounting Developments in Note 1 to the Consolidated Financial Statements.

***OPERATING EXPENSES*** Consolidated operating expenses for 1999 were \$3,954.0 million, compared to \$3,480.4 million in 1998, an increase of 13.6 percent, compared to the 11.2 percent increase in capacity. Operating expenses per ASM increased 2.2 percent in 1999 primarily due to a 15.4 percent increase in average jet fuel prices. Excluding fuel expense, operating expenses per ASM for 1999 increased 0.8 percent.

Based on current trends, unit costs are expected to continue to reflect year over year unfavorable comparisons in first quarter 2000 as a result of higher jet fuel prices. Excluding jet fuel costs, the Company is expecting nonfuel unit cost declines in first quarter 2000 compared to first quarter

1999. (The immediately preceding two sentences are forward-looking statements involving uncertainties that could result in actual results differing materially from expected results. Such uncertainties include, but may not be limited to, the largely unpredictable levels of jet fuel prices and any unscheduled required aircraft airframe or engine repairs.)

Operating expenses per ASM for 1999 and 1998 were as follows:

### OPERATING EXPENSES PER ASM

	1999	1998	Increase (Decrease)	Percent Change
Salaries, wages, and benefits	2.39¢	2.35¢	.04¢	1.7%
Employee profitsharing and savings plans	.36	.35	.01	2.9
Fuel and oil	.93	.82	.11	13.4
Maintenance materials and repairs	.70	.64	.06	9.4
Agency commissions	.30	.33	(.03)	(9.1)
Aircraft rentals	.38	.43	(.05)	(11.6)
Landing fees and other rentals	.46	.45	.01	2.2
Depreciation	.47	.47	—	—
Other	1.49	1.48	.01	0.7
Total	7.48¢	7.32¢	.16¢	2.2%

Salaries, wages, and benefits per ASM increased 1.7 percent in 1999. This increase resulted primarily from increases in benefits costs, specifically workers compensation and health care expense.

Employee profitsharing and savings plans expense per ASM increased slightly due to higher earnings available for profitsharing.

Fuel and oil expenses per ASM increased 13.4 percent in 1999, primarily due to a 15.4 percent increase from 1998 in the average jet fuel cost per gallon. The average price paid for jet fuel in 1999 was \$.5271, including the effects of hedging activities, compared to \$.4567 in 1998. The Company's 1999 average jet fuel price is net of approximately \$14.8 million in gains from hedging activities. Hedging activities in 1998 were not significant. For fourth quarter 1999, the average cost per gallon increased 54.5 percent to \$.6713 compared to \$.4346 in fourth quarter 1998, including the effects of hedging activities. As of February 24, 2000, the Company had hedged its exposure to fuel price increases with combinations of purchased crude oil call options, crude oil collars, and/or fixed

price swap agreements approximating the following percentages of 2000 anticipated fuel requirements: 57 percent for first quarter; 85 percent for second quarter; 100 percent third quarter; and 100 percent fourth quarter. However, the Company is expecting significantly higher jet fuel prices for first quarter 2000 compared to first quarter 1999 due to the historically low prices experienced in first quarter 1999. (The immediately preceding sentence is a forward-looking statement involving uncertainties that could result in actual results differing materially from expected results. Such uncertainties include, but may not be limited to, the largely unpredictable levels of jet fuel prices.) In January 2000, jet fuel prices averaged approximately \$.78 per gallon, including gains from hedging activities. The average cost of jet fuel in January 1999 was \$.3812 per gallon.

Maintenance materials and repairs per ASM increased 9.4 percent in 1999 compared to 1998. Routine heavy maintenance or airframe inspections and repairs represented approximately 74 percent of the increase, while engine inspection and repair costs represented approximately 25 percent of the increase. The increase in airframe inspections and repairs was due primarily to a heavier volume of routine airframe checks scheduled for 1999 versus 1998. Further, a portion of the Company's scheduled airframe checks was outsourced in 1999 as the volume of work exceeded the available internal headcount and facilities necessary to perform such maintenance. In 1998, the Company performed all of this type of routine heavy maintenance internally; thus, the majority of these costs was reflected in salaries and wages. The increases in engine inspection and repair costs were primarily related to the Company's 737-200 aircraft. The Company's 737-200 aircraft engine inspections and repairs are performed on a time and materials basis and are not covered by the Company's power-by-the-hour engine maintenance contract with General Electric Engine Services, Inc. The 737-200 aircraft experienced an increase both in the number of engine inspections and repairs and the average cost per repair. Currently, we expect no material change in unit cost for maintenance materials and repairs in 2000 versus 1999. (The immediately preceding sentence is a forward-looking statement involving uncertainties that could result in actual results differing materially from expected results. Such uncertainties include, but may not be limited to, any unscheduled required aircraft airframe or engine repairs.)

Agency commissions per ASM decreased 9.1 percent in 1999 compared to 1998, primarily due to a decrease in the percentage of commissionable sales to 34.8 percent of total sales in 1999 compared to 39.8 percent in 1998. Based on recent trends, the Company expects agency commissions to decrease on a per ASM basis in 2000. (The immediately preceding sentence is a forward-looking statement involving uncertainties that could result in actual results differing materially from expected

results. Such uncertainties include, but may not be limited to, changes in passenger revenue levels and/or consumer ticket purchasing habits.)

Aircraft rentals per ASM decreased 11.6 percent in 1999 compared to 1998, primarily due to a lower percentage of the aircraft fleet being leased. Approximately 30.8 percent of the Company's aircraft fleet were under operating lease at December 31, 1999, compared to 35.4 percent at December 31, 1998.

Depreciation expense per ASM was flat for 1999 compared to 1998. Although the Company owned a higher percentage of its aircraft fleet in 1999 versus 1998, unit cost was flat due to a change in the estimated useful lives of the Company's Boeing 737-300/-500 aircraft from 20 years to 23 years. See Note 2 to the Consolidated Financial Statements. This change in accounting estimate was made January 1, 1999, and resulted in a decrease in depreciation expense of approximately \$25.7 million for 1999. As the Company's fleet ownership percentage continues to increase in 2000 compared to 1999, the Company anticipates an increase in depreciation expense per ASM. (The immediately preceding sentence is a forward-looking statement involving uncertainties that could result in actual results differing materially from expected results. Such uncertainties include, but may not be limited to, a change in the Company's aircraft financing strategy.)

Other operating expenses per ASM increased 0.7 percent in 1999 compared to 1998. This increase was primarily due to increased credit card processing costs resulting from a higher percentage of the Company's ticket sales purchased with credit cards.

**OTHER** "Other expenses (income)" included interest expense, capitalized interest, interest income, and other gains and losses. Interest expense decreased 3.8 percent in 1999 primarily due to the February 1998 redemption of \$100 million of senior unsecured 9 1/4% Notes originally issued in February 1991. Capitalized interest increased 22.2 percent in 1999 as a result of higher 1999 progress payment balances for scheduled future aircraft deliveries. Interest income for 1999 decreased 18.9 percent primarily due to lower invested cash balances. Other losses in 1999 resulted primarily from a write-down associated with the consolidation of certain software development projects. Other gains in 1998 primarily consisted of contractual penalties received from Boeing due to delays in the delivery of 737-700 aircraft.

**INCOME TAXES** The provision for income taxes, as a percentage of income before taxes, increased slightly to 38.68 percent in 1999 from 38.53 percent in 1998.

**1998 COMPARED WITH 1997** The Company's consolidated net income for 1998 was \$433.4 million (\$.82 per share, diluted), as compared to the corresponding 1997 amount of \$317.8 million (\$.62 per share, diluted), an increase of 36.4 percent. Both of the earnings per share amounts have been restated for the 1999 three-for-two stock split (see Note 8 to the Consolidated Financial Statements).

**OPERATING REVENUES** Consolidated operating revenues increased by 9.1 percent in 1998, compared to 1997, primarily from an 8.9 percent increase in passenger revenues. The increase in passenger revenues was primarily a result of a 10.8 percent increase in revenue passenger miles (RPMs) offset by a 1.7 percent decrease in passenger revenue yield per RPM. While Southwest's passenger revenues increased 8.9 percent in 1998, the RPM yield decline resulted from higher load factors, a 6.0 percent increase in passenger trip lengths, and higher federal excise taxes on domestic tickets.

The 10.8 percent increase in RPMs in 1998 exceeded the 6.9 percent increase in available seat miles (ASMs), resulting in an increase in load factor from 63.7 percent in 1997 to 66.1 percent in 1998. The 1998 ASM growth resulted from the net addition of 19 aircraft during the year.

Freight revenues increased 3.9 percent in 1998 compared to 1997, which fell short of the 6.9 percent increase in ASMs for the same period. United States mail revenue declined 2.5 percent in 1998 and 9.4 percent for fourth quarter 1998 as the postal service shifted business away from commercial carriers. Other air freight revenues increased 8.5 percent in 1998 due to increased capacity.

Other revenues increased 22.7 percent in 1998 to \$101.7 million, compared to \$82.9 million in 1997. This increase was primarily due to increased revenues from the sale of flight segment credits to companies participating in the Company's Rapid Rewards frequent flyer program.

**OPERATING EXPENSES** Consolidated operating expenses for 1998 were \$3,480.4 million, compared to \$3,292.6 million in 1997, an increase of 5.7 percent, compared to the 6.9 percent increase in capacity. Operating expenses per ASM decreased 1.1 percent in 1998, compared to 1997, primarily due to a 26.9 percent decrease in average jet fuel cost per gallon. The decrease in average jet fuel prices was offset by a \$36.1 million increase in Employee profitsharing and savings plan contributions and an increase in maintenance costs primarily due to unusually low aircraft engine inspection and repair costs in the first half of 1997.

Salaries, wages, and benefits per ASM increased 4.0 percent in 1998. This increase resulted primarily from a 6.9 percent increase in 1998 average salary and benefits cost per Employee. The increase in average salary and benefits cost per Employee primarily is due to higher effective wage rates, lower productivity in 1998 caused by Boeing aircraft delivery delays, and increased health care and workers' compensation costs.

Employee profitsharing and savings plans expense per ASM increased 16.7 percent in 1998, primarily due to higher earnings available for profitsharing.

Fuel and oil expenses per ASM decreased 26.1 percent in 1998, primarily due to a 26.9 percent decrease from 1997 in the average jet fuel cost per gallon. The average price paid for jet fuel in 1998 was \$.4567 compared to \$.6246 in 1997.

Maintenance materials and repairs per ASM increased 10.3 percent in 1998, compared to 1997, primarily as a result of an unusually low number of aircraft engine inspections and repairs in the first six months of 1997.

Agency commissions per ASM decreased 5.7 percent in 1998, when compared to 1997, primarily due to a decrease in the percentage of commissionable sales.

Aircraft rentals per ASM decreased 4.4 percent in 1998, compared to 1997, primarily due to a lower percentage of the aircraft fleet being leased.

Depreciation expense per ASM increased 6.8 percent in 1998, compared to 1997, primarily due to a higher percentage of the aircraft fleet being owned.

Other operating expenses per ASM increased 2.1 percent in 1998, compared to 1997, primarily due to increased costs resulting from the Year 2000 remediation program and increased revenue-related costs such as credit card processing and communications, partially offset by lower insurance costs.

*OTHER* "Other expenses (income)" included interest expense, capitalized interest, interest income, and other gains and losses. Interest expense decreased \$7.2 million in 1998 primarily due to the February 1998 redemption of \$100 million of senior unsecured 9 1/4% Notes originally issued in February 1991. Capitalized interest increased \$5.8 million in 1998 as a result of higher 1998 progress payment balances. Interest income for 1998 decreased primarily due to lower invested cash balances. Other gains in 1998 primarily included contractual penalties due from Boeing as a result of aircraft delivery delays.

**INCOME TAXES** The provision for income taxes, as a percentage of income before taxes, was unchanged from 1997 to 1998.

## **LIQUIDITY AND CAPITAL RESOURCES**

Net cash provided by operating activities was \$1,001.7 million in 1999 compared to \$886.1 million in 1998. Also, during fourth quarter 1999, additional funds of \$256 million were generated from two separate financing transactions. See Note 5 to the Consolidated Financial Statements for further information on these borrowings. Cash generated in 1999 was primarily used to finance aircraft-related capital expenditures and provide working capital.

During 1999, net capital expenditures were \$1,167.8 million, which primarily related to the purchase of 32 new 737-700 aircraft, four used 737-300 aircraft, five used 737-200 aircraft, and progress payments for future aircraft deliveries. The five 737-200 aircraft were previously on lease by the Company prior to being purchased.

At December 31, 1999, capital commitments of the Company primarily consisted of scheduled aircraft acquisitions and related flight equipment. As of December 31, 1999, Southwest had 85 new 737-700s on firm order, including 31 to be delivered in 2000, with options to purchase another 62 737-700s during 2003-2006. Aggregate funding required for firm commitments approximated \$1,965.7 million through the year 2004, of which \$687.9 million related to 2000. See Note 3 to the Consolidated Financial Statements for further information on commitments.

On September 23, 1999, the Company announced its Board of Directors had authorized the repurchase of up to \$250 million of the Company's common stock. Repurchases will be made in accordance with applicable securities laws in the open market or in private transactions from time to time, depending on market conditions, and may be discontinued at any time. As of December 31, 1999, 5.6 million shares had been repurchased at a total cost of \$90.5 million.

The Company has various options available to meet its capital and operating commitments, including cash on hand at December 31, 1999, of \$418.8 million, internally generated funds, and a revolving credit line with a group of banks of up to \$475 million (none of which had been drawn at December 31, 1999). In addition, the Company will also consider various borrowing or leasing options to maximize earnings and supplement cash requirements.

The Company currently has outstanding shelf registrations for the issuance of \$318.8 million of public debt securities, which it may utilize for aircraft financings in 2000 and 2001.

## MARKET RISK

Southwest has interest rate risk in that it holds floating rate debt instruments and has commodity price risk in that it must purchase jet fuel to operate its aircraft fleet. To the extent the Company does not have hedges in place, jet fuel will be purchased at prevailing market prices. Southwest also has market sensitive instruments in the form of the types of hedges it utilizes to decrease its exposure to jet fuel price increases in addition to its debt instruments. The Company also operates 103 aircraft under operating and capital leases. However, leases are not considered market sensitive financial instruments and, therefore, are not included in the interest rate sensitivity analysis below. Commitments related to leases are disclosed in Note 6 to the Consolidated Financial Statements. The Company does not purchase or hold any derivative financial instruments for trading purposes.

Airline operators are inherently dependent upon energy to operate and, therefore, are impacted by changes in jet fuel prices. Jet fuel consumed in 1999 and 1998 represented approximately 12.5 and 11.2 percent of Southwest's operating expenses, respectively. Southwest endeavors to acquire jet fuel at the lowest prevailing prices possible.

Prior to December 1998, the Company hedged its exposure to jet fuel market price risk primarily with purchased "out of the money," crude oil call options. In December 1998, in order to take advantage of historically low jet fuel prices, Southwest increased its fuel hedging activity by entering into fixed price swap agreements hedging approximately 77 percent and 56 percent of its jet fuel needs in first and second quarter 1999, respectively. In January 1999, the Company increased its hedging position for second quarter 1999 to 74 percent. During the second half of 1999, the Company did not have a significant portion of its fuel purchases hedged as futures prices were substantially higher than then-current prices.

Since mid-1999, energy markets and prices have changed radically. As a result, the Company has adjusted its hedge strategy. The Company utilizes financial derivative instruments for both short-term and long-term time frames when it appears the Company can take advantage of market conditions. At December 31, 1999, the Company had a mixture of purchased crude oil call options and fixed price swap agreements in place to hedge approximately 10.1 percent of its 2000 total anticipated jet fuel requirements. The Company had also entered into fixed price swap agreements to hedge a small percentage of its 2001 and 2005 anticipated requirements. See Note 7 to the Consolidated Financial Statements. In January and February 2000, the Company increased its hedging position by adding fixed price swap agreements and crude oil collars. As of February 24, 2000, the Company's total positions



to approximately 57 percent for first quarter 2000, 85 percent for second quarter 2000, 100 percent for third quarter 2000, 100 percent for fourth quarter 2000, 50 percent for first quarter 2001, 50 percent for second quarter 2001, and 20 percent for third quarter 2001. The Company's fuel hedging strategy could result in the Company not fully benefiting from certain fuel price declines.

The fair values of outstanding fixed price swap agreements and purchased crude oil call options related to the Company's jet fuel market price risk at December 31, 1999 and 1998, and during the year ended 1998, were not material. For 1999, the Company realized approximately \$14.8 million in gains from hedging activities. A hypothetical ten percent increase or decrease in the underlying fuel-related commodity prices from the December 31, 1999, prices would correspondingly change the fair value of the derivative commodity instruments in place and their related cash flows by approximately \$3 million.

Airline operators are also inherently capital intensive, as the vast majority of the Company's assets are aircraft, which are long lived. The Company's strategy is to capitalize itself conservatively and grow capacity steadily and profitably. While Southwest does use financial leverage, it has maintained a strong balance sheet and "A-" or equivalent credit ratings on its senior unsecured fixed-rate debt with three rating agencies (Standard & Poor's, Moody's, and Duff & Phelps). The Company's Aircraft Secured Notes (\$200 million) do not give rise to significant fair value risk but do give rise to interest rate risk because these borrowings are effectively floating-rate debt. The Company's \$56 million in secured borrowings completed in 1999 does not give rise to significant fair value risk because these borrowings are also floating-rate debt. Although there is interest rate risk associated with these secured borrowings, the risk is somewhat mitigated by the fact that the Company may prepay this debt on any of the semi-annual principal and interest payment dates. See Note 5 to the Consolidated Financial Statements for more information on these 1999 borrowings.

As disclosed in Note 5 to the Consolidated Financial Statements, the Company had outstanding senior unsecured notes totaling \$500 million at December 31, 1999, and at December 31, 1998. These long-term notes represent only 10.0 percent and 12.1 percent of total noncurrent assets at December 31, 1999 and 1998, respectively. The unsecured long-term debt currently has an average maturity of nine years at fixed rates averaging 8.3 percent at December 31, 1999, which is comparable to average rates prevailing over the last ten years. The Company does not have significant exposure to changing interest rates on its unsecured long-term debt because the interest rates are fixed and the financial leverage is modest.

Additionally, the Company does not have significant exposure to changing interest rates on invested cash, which was \$419 million and \$379 million at December 31, 1999 and 1998, respectively. The Company invests available cash in certificates of deposit and investment grade commercial paper that have maturities of three months or less. As a result, the interest rate market risk implicit in these investments at December 31, 1999, is low, as the investments mature within three months. The Company has not undertaken any additional actions to cover interest rate market risk and is not a party to any other interest rate market risk management activities.

A hypothetical ten percent change in market interest rates over the next year would not have a material effect on the fair value of the Company's debt instruments or its short-term cash investments. See Note 7 to the Consolidated Financial Statements for further information on the fair value of the Company's financial instruments. Because of the floating rate nature of the Company's secured borrowings, a ten percent change in market interest rates as of December 31, 1999, would correspondingly change the Company's earnings and cash flows by approximately \$1.4 million. However, a ten percent change in market rates would not impact the Company's earnings or cash flow associated with the Company's publicly traded fixed-rate debt or its cash investments.

## **IMPACT OF THE YEAR 2000**

The Company has completed all significant aspects of its Year 2000 project. The Company's Year 2000 project encompassed information technology systems as well as embedded technology assets along with assessments of material third-party relationships and associated risks.

All of the Company's internal systems and software, including virtually all software and services provided by third parties, appropriately handled the Year 2000 date changeover and the Company's operations were also unaffected. While the Company has experienced no Year 2000 related disruptions to date, there are remaining risks associated with the Year 2000 issue and the Company continues to monitor possible future implications of Year 2000 issues. Based on currently available information, management believes that Year 2000 related disruptions, if any, will not have a material adverse affect on the Company's financial condition or results of operations.

## SOUTHWEST AIRLINES CO. CONSOLIDATED BALANCE SHEET

<i>(In thousands except per share amounts)</i>	DECEMBER 31,	
	1999	1998
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 418,819	\$ 378,511
Accounts receivable	73,448	88,799
Inventories of parts and supplies, at cost	65,152	50,035
Deferred income taxes (Note 11)	20,929	20,734
Prepaid expenses and other current assets	<u>52,657</u>	<u>36,076</u>
Total current assets	631,005	574,155
Property and equipment, at cost (Notes 3, 5, and 6):		
Flight equipment	5,768,506	4,709,059
Ground property and equipment	742,230	720,604
Deposits on flight equipment purchase contracts	<u>338,229</u>	<u>309,356</u>
	6,848,965	5,739,019
Less allowance for depreciation	<u>1,840,799</u>	<u>1,601,409</u>
	5,008,166	4,137,610
Other assets	<u>12,942</u>	<u>4,231</u>
	<u>\$5,652,113</u>	<u>\$4,715,996</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 156,755	\$ 157,415
Accrued liabilities (Note 4)	535,024	477,448
Air traffic liability	256,942	200,078
Current maturities of long-term debt (Note 5)	7,873	11,996
Other current liabilities	<u>3,872</u>	<u>3,716</u>
Total current liabilities	960,466	850,653
Long-term debt less current maturities (Note 5)	871,717	623,309
Deferred income taxes (Note 11)	692,342	549,207
Deferred gains from sale and leaseback of aircraft	222,700	238,412
Other deferred liabilities	69,100	56,497
Commitments and contingencies (Notes 3, 6, and 11)		
Stockholders' equity (Notes 8 and 9):		
Common stock, \$1.00 par value: 1,300,000 shares authorized; 505,005 and 335,904 shares issued in 1999 and 1998, respectively	505,005	335,904
Capital in excess of par value	35,436	89,820
Retained earnings	2,385,854	2,044,975
Treasury stock, at cost: 5,579 and 5,402 shares in 1999 and 1998, respectively	<u>(90,507)</u>	<u>(72,781)</u>
Total stockholders' equity	2,835,788	2,397,918
	<u>\$5,652,113</u>	<u>\$4,715,996</u>

See accompanying notes.

## SOUTHWEST AIRLINES CO. CONSOLIDATED STATEMENT OF INCOME

<i>(In thousands except per share amounts)</i>	<b>YEARS ENDED DECEMBER 31,</b>		
	<b>1999</b>	<b>1998</b>	<b>1997</b>
<b>OPERATING REVENUES:</b>			
Passenger	\$4,499,360	\$3,963,781	\$3,639,193
Freight	102,990	98,500	94,758
Other	<u>133,237</u>	<u>101,699</u>	<u>82,870</u>
Total operating revenues	4,735,587	4,163,980	3,816,821
<b>OPERATING EXPENSES:</b>			
Salaries, wages, and benefits (Note 10)	1,455,237	1,285,942	1,136,542
Fuel and oil	492,415	388,348	494,952
Maintenance materials and repairs	367,606	302,431	256,501
Agency commissions	156,419	157,766	157,211
Aircraft rentals	199,740	202,160	201,954
Landing fees and other rentals	242,002	214,907	203,845
Depreciation (Note 2)	248,660	225,212	195,568
Other operating expenses	<u>791,932</u>	<u>703,603</u>	<u>646,012</u>
Total operating expenses	3,954,011	3,480,369	3,292,585
<b>OPERATING INCOME</b>	781,576	683,611	524,236
<b>OTHER EXPENSES (INCOME):</b>			
Interest expense	54,145	56,276	63,454
Capitalized interest	(31,262)	(25,588)	(19,779)
Interest income	(25,200)	(31,083)	(36,616)
Other (gains) losses, net	<u>10,282</u>	<u>(21,106)</u>	<u>221</u>
Total other expenses (income)	7,965	(21,501)	7,280
<b>INCOME BEFORE INCOME TAXES</b>	773,611	705,112	516,956
<b>PROVISION FOR INCOME TAXES</b>			
<b>(NOTE 11)</b>	<u>299,233</u>	<u>271,681</u>	<u>199,184</u>
<b>NET INCOME</b>	<u>\$ 474,378</u>	<u>\$ 433,431</u>	<u>\$ 317,772</u>
<b>NET INCOME PER SHARE, BASIC (NOTES 8, 9, AND 12)</b>	<u>\$ .94</u>	<u>\$ .87</u>	<u>\$ .64</u>
<b>NET INCOME PER SHARE, DILUTED (NOTES 8, 9, AND 12)</b>	<u>\$ .89</u>	<u>\$ .82</u>	<u>\$ .62</u>

See accompanying notes.

**SOUTHWEST AIRLINES CO. CONSOLIDATED STATEMENT OF STOCKHOLDERS'  
EQUITY**

<i>(In thousands except per share amounts)</i>	<b>YEARS ENDED DECEMBER 31, 1999, 1998, and 1997</b>				
	<b>Common Stock</b>	<b>Capital in Excess of Par Value</b>	<b>Retained Earnings</b>	<b>Treasury Stock</b>	<b>Total</b>
Balance at December 31, 1996	\$145,112	\$181,650	\$1,321,550	\$ -	\$1,648,312
Three-for-two stock split (Note 8)	73,578	(73,578)	-	-	-
Issuance of common stock upon exercise of executive stock options and pursuant to Employee stock option and purchase plans (Note 9)	2,517	37,818	-	-	40,335
Tax benefit of options exercised	-	9,806	-	-	9,806
Cash dividends, \$.0147 per share	-	-	(7,207)	-	(7,207)
Net income – 1997	<u>-</u>	<u>-</u>	<u>317,772</u>	<u>-</u>	<u>317,772</u>
Balance at December 31, 1997	221,207	155,696	1,632,115	-	2,009,018
Three-for-two stock split (Note 8)	111,894	(111,894)	-	-	-
Purchase of shares of treasury stock (Note 8)	-	-	-	(100,000)	(100,000)
Issuance of common and treasury stock upon exercise of executive stock options and pursuant to Employee stock option and purchase plans (Note 9)	2,803	24,434	(10,184)	27,219	44,272
Tax benefit of options exercised	-	21,584	-	-	21,584
Cash dividends, \$.0189 per share	-	-	(10,387)	-	(10,387)
Net income – 1998	<u>-</u>	<u>-</u>	<u>433,431</u>	<u>-</u>	<u>433,431</u>
Balance at December 31, 1998	335,904	89,820	2,044,975	(72,781)	2,397,918
Three-for-two stock split (Note 8)	167,954	(89,878)	(78,076)	-	-
Purchase of shares of treasury stock (Note 8)	-	-	-	(90,507)	(90,507)
Issuance of common and treasury stock upon exercise of executive stock options and pursuant to Employee stock option and purchase plans (Note 9)	1,147	7,811	(45,134)	72,781	36,605
Tax benefit of options exercised	-	27,683	-	-	27,683
Cash dividends, \$.0215 per share	-	-	(10,289)	-	(10,289)
Net income – 1999	<u>-</u>	<u>-</u>	<u>474,378</u>	<u>-</u>	<u>474,378</u>
Balance at December 31, 1999	<u>\$505,005</u>	<u>\$35,436</u>	<u>\$2,385,854</u>	<u>\$(90,507)</u>	<u>\$2,835,788</u>

See accompanying notes.

## SOUTHWEST AIRLINES CO. CONSOLIDATED STATEMENT OF CASH FLOWS

<i>(In thousands)</i>	YEARS ENDED DECEMBER 31,		
	1999	1998	1997
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income	\$474,378	\$433,431	\$317,772
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	248,660	225,212	195,568
Deferred income taxes	142,940	108,335	81,711
Amortization of deferred gains on sale and leaseback of aircraft	(15,172)	(15,251)	(15,414)
Amortization of scheduled airframe inspections and repairs	28,949	22,763	20,540
Changes in certain assets and liabilities:			
Accounts receivable	15,421	(12,269)	(3,090)
Other current assets	(31,698)	1,589	6,243
Accounts payable and accrued liabilities	64,335	53,194	8,751
Air traffic liability	56,864	46,737	(4,757)
Other current liabilities	156	19,293	(4,204)
Other	<u>16,877</u>	<u>3,101</u>	<u>7,468</u>
Net cash provided by operating activities	1,001,710	886,135	610,588
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Purchases of property and equipment	<u>(1,167,834)</u>	<u>(947,096)</u>	<u>(688,927)</u>
Net cash used in investing activities	(1,167,834)	(947,096)	(688,927)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Issuance of long-term debt	255,600	-	98,764
Payment of long-term debt and capital lease obligations	(12,107)	(118,859)	(12,665)
Payment of cash dividends	(10,842)	(9,284)	(6,593)
Proceeds from Employee stock plans	64,288	44,272	40,335
Repurchase of common stock	<u>(90,507)</u>	<u>(100,000)</u>	-
Net cash provided by (used in) financing activities	<u>206,432</u>	<u>(183,871)</u>	<u>119,841</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	40,308	(244,832)	41,502
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<u>378,511</u>	<u>623,343</u>	<u>581,841</u>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<u>\$418,819</u>	<u>\$378,511</u>	<u>\$623,343</u>
<b>CASH PAYMENTS FOR:</b>			
Interest, net of amount capitalized	\$ 26,604	\$ 33,384	\$ 42,372
Income taxes	131,968	147,447	107,066

See accompanying notes.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1999

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

***BASIS OF PRESENTATION*** Southwest Airlines Co. (Southwest) is a major domestic airline that primarily provides shorthaul, high-frequency, point-to-point, low-fare service. The consolidated financial statements include the accounts of Southwest and its wholly owned subsidiaries (the Company). All significant intercompany balances and transactions have been eliminated. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. Certain prior year amounts have been restated to conform to the current year presentation.

***CASH AND CASH EQUIVALENTS*** Cash equivalents consist of certificates of deposit and investment grade commercial paper issued by major corporations and financial institutions. Cash and cash equivalents are highly liquid and have original maturities of three months or less. Cash and cash equivalents are carried at cost, which approximates market value.

***INVENTORIES*** Inventories of flight equipment expendable parts, materials, and supplies are carried at average cost. These items are charged to expense when issued for use.

***PROPERTY AND EQUIPMENT*** Depreciation is provided by the straight-line method to estimated residual values over periods ranging from 20 to 25 years for flight equipment and 3 to 30 years for ground property and equipment. See Note 2 for further information on aircraft depreciation. Property under capital leases and related obligations are recorded at an amount equal to the present value of future minimum lease payments computed on the basis of the Company's incremental borrowing rate or, when known, the interest rate implicit in the lease. Amortization of property under capital leases is on a straight-line basis over the lease term and is included in depreciation expense. The Company records impairment losses on long-lived assets used in operations when events and circumstances

indicate that the assets might be impaired and the undiscounted cash flows to be generated by those assets are less than the carrying amounts of those assets.

**AIRCRAFT AND ENGINE MAINTENANCE** The cost of scheduled engine inspections and repairs and routine maintenance costs for aircraft and engines are charged to maintenance expense as incurred. Scheduled airframe inspections and repairs, known as “D” checks, are generally performed every ten years. Costs related to “D” checks are capitalized and amortized over the estimated period benefited, presently the least of ten years, time until the next “D” check, or the remaining life of the aircraft. Modifications that significantly enhance the operating performance or extend the useful lives of aircraft or engines are capitalized and amortized over the remaining life of the asset.

**REVENUE RECOGNITION** Passenger revenue is recognized when transportation is provided. Tickets sold but not yet used are included in “Air traffic liability,” which includes estimates that are evaluated and adjusted periodically. Any adjustments resulting therefrom are included in results of operations for the periods in which the evaluations are completed.

**FREQUENT FLYER PROGRAM** The Company accrues the estimated incremental cost of providing free travel awards earned under its Rapid Rewards frequent flyer program. The Company also sells flight segment credits and related services to companies participating in its Rapid Rewards frequent flyer program. The revenue related to the sale of flight segment credits is recognized when the credits are sold (see Recent Accounting Developments).

**ADVERTISING** The Company expenses the costs of advertising as incurred. Advertising expense for the years ended December 31, 1999, 1998, and 1997 was \$137.7 million, \$119.7 million, and \$113.0 million, respectively.

**STOCK-BASED EMPLOYEE COMPENSATION** Pursuant to Statement of Financial Accounting Standards No. 123 (SFAS 123), *Accounting for Stock-Based Compensation*, the Company accounts for stock-based compensation plans utilizing the provisions of Accounting Principles Board Opinion No. 25 (APB 25), *Accounting for Stock Issued to Employees* and related Interpretations. See Note 9.



**DERIVATIVE FINANCIAL INSTRUMENTS** The Company utilizes purchased crude oil call options and fixed price swap agreements to hedge a portion of its exposure to fuel price increases. The cost of purchased crude oil call options and gains and losses on fixed price swap agreements, including those terminated or settled early, are deferred and charged or credited to fuel expense in the same month that the underlying fuel being hedged is used. The Company recognized gains of \$14.8 million in 1999 from hedging activities. The gains are recorded as a reduction of fuel and oil expense. Gains and losses on hedging transactions for 1998 and 1997 were not material.

In 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 133 (SFAS 133), *Accounting for Derivative Instruments and Hedging Activities*. In 1999, the FASB issued SFAS 137, which delayed the effective date of SFAS 133 by one year. SFAS 133 is required to be adopted in years beginning after June 15, 2000. SFAS 133 permits early adoption as of the beginning of any fiscal quarter after its issuance. The Company expects to adopt the new Statement effective January 1, 2001. SFAS 133 will require the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value will be immediately recognized in earnings. The Company has not yet determined what the effect of SFAS 133 will be on the earnings and financial position of the Company.

**RECENT ACCOUNTING DEVELOPMENTS** In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101 (SAB 101), *Revenue Recognition in Financial Statements*. This statement gives specific guidance and clarification on the conditions that must be met before an entity may recognize revenue. SAB 101 must be adopted no later than the first fiscal quarter of the fiscal year beginning after December 15, 1999. The Company will adopt SAB 101 effective January 1, 2000, and change its method of accounting used to recognize revenue for the sale of flight segment credits to companies participating in its Rapid Rewards frequent flyer program.

Prior to the issuance of SAB 101, the Company recorded revenue to Other Revenue when flight segment credits were sold, which is a commonly used method of accounting within the airline industry. However, in accordance with SAB 101, revenue received from the sale of flight segment credits and associated with future travel will be deferred and recognized as the ultimate free travel awards are flown. Also as part of this change, this revenue will be classified as Passenger Revenue in the Company's Consolidated Statement of Income.

As of January 1, 2000, the cumulative effect of this accounting change will reduce first quarter 2000 net income by approximately \$22.1 million (net of provision for income taxes of approximately \$14.0 million). Adopting this new method of accounting for 1999, 1998, and 1997, would have produced the following pro forma results: Net income would have been reduced by \$3.9 million, \$5.0 million, and \$5.5 million, respectively (net of provision for income taxes and profitsharing of approximately \$2.5 million, \$3.1 million, and \$3.5 million, respectively). Earnings per share, basic and diluted, would have been reduced by \$.01 per share for each year, except 1999 basic earnings per share would not change. However, while pro forma amounts will be presented in future financial statements, these years will not be restated.

## **2. CHANGE IN ACCOUNTING ESTIMATE**

Effective January 1, 1999, the Company revised the estimated useful lives of its 737-300 and -500 aircraft from 20 years to 23 years. This change was the result of the Company's assessment of the remaining useful lives of the aircraft based on the manufacturer's design lives, the Company's increased average aircraft stage (trip) length, and the Company's previous experience. The effect of this change was to reduce depreciation expense approximately \$25.7 million and increase net income \$.03 per diluted share for the year ended December 31, 1999.

## **3. COMMITMENTS**

The Company's contractual purchase commitments consist primarily of scheduled aircraft acquisitions. Thirty-one 737-700 aircraft are scheduled for delivery in 2000, 23 in 2001, 21 in 2002, five in 2003, and five in 2004. In addition, the Company has options to purchase up to 62 737-700s during 2003–2006. The Company has the option, which must be exercised two years prior to the contractual delivery date, to substitute 737-600s or 737-800s for the 737-700s scheduled subsequent to 2001. Aggregate funding needed for fixed commitments is approximately \$1,965.7 million, subject to adjustments for inflation,

due as follows: \$687.9 million in 2000, \$520.1 million in 2001, \$515.8 million in 2002, \$152.8 million in 2003, and \$89.1 million in 2004.

#### 4. ACCRUED LIABILITIES

<i>(In thousands)</i>	<b>1999</b>	<b>1998</b>
Employee profitsharing and savings plans (Note 10)	\$138,566	\$123,195
Aircraft rentals	131,219	121,868
Vacation pay	62,937	54,781
Other	<u>202,302</u>	<u>177,604</u>
	<b><u>\$535.024</u></b>	<b><u>\$477.448</u></b>

#### 5. LONG-TERM DEBT

<i>(In thousands)</i>	<b>1999</b>	<b>1998</b>
9.4% Notes due 2001	\$100,000	\$100,000
8 3/4% Notes due 2003	100,000	100,000
Aircraft Secured Notes due 2004	200,000	-
8% Notes due 2005	100,000	100,000
7 7/8% Notes due 2007	100,000	100,000
French Credit Agreements	55,844	-
7 3/8% Debentures due 2027	100,000	100,000
Capital leases (Note 6)	123,834	133,190
Other	<u>1,886</u>	<u>4,481</u>
	<b>881,564</b>	<b>637,671</b>
Less current maturities	7,873	11,996
Less debt discount	<u>1,974</u>	<u>2,366</u>
	<b><u>\$871.717</u></b>	<b><u>\$623.309</u></b>

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In fourth quarter 1999, the Company issued \$200 million of floating rate Aircraft Secured Notes, due 2004. The Notes are funded by a bank through a commercial paper conduit program and are secured by eight aircraft. Interest rates on the Notes are based on the conduit's actual commercial paper rate, plus fees, for each period and are expected to average approximately LIBOR plus 36 basic points, over the term of the Notes. Interest is payable monthly and the Company can prepay the Notes in whole or in part prior to maturity.

Also in fourth quarter 1999, the Company entered into two identical 13-year floating rate financing arrangements, whereby it effectively borrowed a total of \$56 million from

French banking partnerships. For presentation purposes, the Company has classified these identical borrowings as one \$56 million transaction. The effective rate of interest over the 13-year term of the loans is LIBOR plus 32 basis points. Principal and interest are payable semi-annually on June 30 and December 31 for each of the loans and the Company may terminate the arrangements in any year on either of those dates, with certain conditions. The Company has pledged two aircraft as collateral for the entire transaction.

On February 28, 1997, the Company issued \$100 million of senior unsecured 7 3/8% Debentures due March 1, 2027. Interest is payable semi-annually on March 1 and September 1. The Debentures may be redeemed, at the option of the Company, in whole at any time or in part from time to time, at a redemption price equal to the greater of the principal amount of the Debentures plus accrued interest at the date of redemption or the sum of the present values of the remaining scheduled payments of principal and interest thereon, discounted to the date of redemption at the comparable treasury rate plus 20 basis points, plus accrued interest at the date of redemption.

On March 7, 1995, the Company issued \$100 million of senior unsecured 8% Notes due March 1, 2005. Interest is payable semi-annually on March 1 and September 1. The Notes are not redeemable prior to maturity.

On September 9, 1992, the Company issued \$100 million of senior unsecured 7 7/8% Notes due September 1, 2007. Interest is payable semi-annually on March 1 and September 1. The Notes are not redeemable prior to maturity.

During 1991, the Company issued \$100 million of senior unsecured 9.4% Notes and \$100 million of senior unsecured 8 3/4% Notes due July 1, 2001, and October 15, 2003, respectively. Interest on the Notes is payable semi-annually. The Notes are not redeemable prior to maturity.

In addition to the credit facilities described above, Southwest has an unsecured Bank Credit Agreement with a group of banks that permits Southwest to borrow through May 6, 2002, on a revolving credit basis, up to \$475 million. Interest rates on borrowings under the Credit Agreement can be, at the option of Southwest, the greater of the agent bank's prime rate or the federal funds rate plus .5 percent, .17 percent over LIBOR, or a fixed rate offered by the banks at the time of borrowing. The commitment fee is .08 percent per annum. There were no outstanding borrowings under this agreement, or prior similar agreements, at December 31, 1999 or 1998.

## 6. LEASES

Total rental expense for operating leases charged to operations in 1999, 1998, and 1997 was \$318.2 million, \$305.2 million, and \$296.5 million, respectively. The majority of the Company's terminal operations space, as well as 96 aircraft, was under operating leases at December 31, 1999. The amounts applicable to capital leases included in property and equipment were:

<i>(In thousands)</i>	<b>1999</b>	<b>1998</b>
Flight equipment	\$164,957	\$230,486
Less accumulated amortization	<u>85,722</u>	<u>133,073</u>
	<u>\$79,235</u>	<u>\$97,413</u>

Future minimum lease payments under capital leases and noncancelable operating leases with initial or remaining terms in excess of one year at December 31, 1999, were:

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<i>(In thousands)</i>	<b>Capital Leases</b>	<b>Operating Leases</b>
2000	\$ 16,871	\$ 278,328
2001	17,391	261,419
2002	17,561	235,601
2003	17,750	210,667
2004	17,650	186,500
After 2004	<u>102,399</u>	<u>1,832,541</u>
Total minimum lease payments	189,622	<u>\$3,005,056</u>
Less amount representing interest	<u>65,788</u>	
Present value of minimum lease payments	123,834	
Less current portion	<u>4,384</u>	
Long-term portion	<u>\$119,450</u>	

The aircraft leases generally can be renewed, at rates based on fair market value at the end of the lease term, for one to five years. Most aircraft leases have purchase options at or near the end of the lease term at fair market value, but generally not to exceed a stated percentage of the lessor's defined cost of the aircraft.

## 7. FINANCIAL INSTRUMENTS

The Company has historically utilized purchased crude oil call options and fixed price swap agreements to hedge a portion of its exposure to fuel price increases. During 1999, the Company recognized gains of \$14.8 million from hedging activities. At

December 31, 1999, the Company had hedged positions in place to limit its exposure to fuel price increases at the following levels:

Period	Approximate % of Expected Requirements Hedged	Approximate Gallons Hedged	Type of Hedge Instrument
First Quarter 2000	27%	63.0 million	options
Second Quarter 2000	—	—	—
Third Quarter 2000	5%	13.7 million	swaps
Fourth Quarter 2000	10%	26.3 million	swaps
First Quarter 2001	9%	23.1 million	swaps

The fair value of these agreements at December 31, 1999, representing the amount the Company would receive if the agreements were settled early, was not material.

Any outstanding call options or fixed swap agreements expose the Company to credit loss in the event of nonperformance by the counterparties to the agreements, but the Company does not expect any of the counterparties to fail to meet their obligations. The credit exposure related to these financial instruments is represented by the fair value of contracts with a positive fair value at the reporting date. To manage credit risks, the Company selects counterparties based on credit ratings, limits its exposure to a single counterparty, and monitors the market position of the program and its relative market position with each counterparty. At December 31, 1999, the Company had an agreement with one counterparty containing a bilateral collateral provision whereby cash deposits are required if market risk exposure exceeds a specified threshold amount. Neither the Company nor the counterparty exceeded the threshold amount at December 31, 1999. The Company is in the process of negotiating similar agreements with other counterparties.

The Company does not hold or issue any financial instruments for trading purposes.

The carrying amounts and estimated fair values of the Company's long-term debt at December 31, 1999, were as follows:

<i>(In thousands)</i>	Carrying Value	Fair Value
9.4% Notes due 2001	\$100,000	\$103,330
8 3/4% Notes due 2003	100,000	104,160
Aircraft Secured Notes due 2004	200,000	200,000
8% Notes due 2005	100,000	101,460
7 7/8% Notes due 2007	100,000	100,730
French Credit Agreements	55,844	55,844
7 3/8% Debentures due 2027	100,000	92,680

The estimated fair values of the Company's long-term debt were based on quoted market prices. The carrying values of all other financial instruments approximate their fair value.

## **8. COMMON STOCK**

The Company has one class of common stock. Holders of shares of common stock are entitled to receive dividends when and if declared by the Board of Directors and are entitled to one vote per share on all matters submitted to a vote of the shareholders.

At December 31, 1999, the Company had common stock reserved for issuance pursuant to Employee stock benefit plans (97.9 million shares) and upon exercise of rights (602.9 million shares) pursuant to the Common Stock Rights Agreement, as amended (Agreement).

Pursuant to the Agreement, each outstanding share of the Company's common stock is accompanied by one common share purchase right (Right). Each Right entitles its holder to purchase one additional share of common stock at an exercise price of \$4.94 and is exercisable only in the event of a proposed takeover, as defined by the Agreement. The Company may redeem the Rights at \$.0033 per Right prior to the time that 15 percent of the common stock has been acquired by a person or group. If the Company is acquired, as defined in the Agreement, each Right will entitle its holder to purchase for \$4.94 that number of the acquiring company's or the Company's common shares, as provided in the Agreement, having a market value of two times the exercise price of the Right. The Rights will expire no later than July 30, 2006.

On September 25, 1997, the Company's Board of Directors declared a three-for-two stock split, distributing 73.6 million shares on November 26, 1997. On July 22, 1998, the Company's Board of Directors declared a three-for-two stock split, distributing 111.9 million shares on August 20, 1998. On May 20, 1999, the Company's Board of Directors declared a three-for-two stock split, distributing 168.0 million shares on July 19, 1999. Unless otherwise stated, all per share data presented in the accompanying consolidated financial statements and notes thereto have been restated to give effect to the stock splits.

During third quarter 1998, the Company completed a \$100 million common stock repurchase program, resulting in the repurchase of 7.3 million shares at an average cost of \$13.65 per share. All of the acquired shares were subsequently reissued under the Employee stock option and purchase plans.

As of September 23, 1999, the Company's Board of Directors authorized the Company to repurchase up to \$250 million of its outstanding common stock. As of December 31, 1999, this program had resulted in the repurchase of 5.6 million shares at an average cost of \$16.22 per share. All of the acquired shares are held as common stock in treasury, less shares reissued under the Employee stock option and purchase plans. When treasury shares are reissued, the Company uses a first-in, first-out method and the excess of repurchase cost over reissuance price, if any, is treated as a reduction of retained earnings.

## **9. STOCK PLANS**

At December 31, 1999, the Company had eight stock-based compensation plans and other stock options outstanding, which are described below. The Company applies APB 25 and related Interpretations in accounting for its stock-based compensation. Accordingly, no compensation expense is recognized for its fixed option plans because the exercise prices of the Company's Employee stock options equal or exceed the market prices of the underlying stock on the dates of grant. Compensation expense for other stock options is not material.

The Company has seven fixed option plans. Under the 1991 Incentive Stock Option Plan, the Company may grant options to key Employees for up to 30.4 million shares of common stock. Under the 1991 Non-Qualified Stock Option Plan, the Company may grant options to key Employees and non-employee directors for up to 2.5 million shares of common stock. All options granted under these plans have ten-year terms and vest and become fully exercisable at the end of three, five, or ten years of continued employment, depending upon the grant type.

Under the 1995 Southwest Airlines Pilots' Association Non-Qualified Stock Option Plan (SWAPA Plan), the Company may grant options to Pilots for up to 60.8 million shares of common stock. An initial grant of approximately 49.2 million shares was made on January 12, 1995, at an option price of \$5.93 per share, which exceeded the market price of the Company's stock on that date. Options granted under the initial grant vest in ten annual increments of ten percent. On September 1 of each year of the agreement beginning in 1996, additional options will be granted to Pilots who become eligible during that year. Additional options granted on September 1, 1999, 1998, and 1997, vest in five annual increments of 20.0 percent, six annual increments of 16.7 percent, and seven



annual increments of 14.3 percent, respectively. Options under all grants must be exercised prior to January 31, 2007, or within a specified time upon retirement or termination.

Under the 1996 Incentive Stock Option Plan, the Company may grant options to key Employees for up to 20.3 million shares of common stock. Under the 1996 Non-Qualified Stock Option Plan, the Company may grant options to key Employees and non-employee directors for up to 1.9 million shares of common stock. All options granted under these plans have ten-year terms and vest and become fully exercisable at the end of three, five, or ten years of continued employment, depending upon the grant type.

Under the 1998 Southwest Airlines Employee Association Non-Qualified Stock Option Plan (SAEA Plan), the Company may grant options to Dispatchers for up to 1.6 million shares of common stock. An initial grant of 1.1 million shares was made on September 10, 1998, at an option price of \$13.08 per share, which exceeded the market price of the Company's stock on that date. Options granted under the initial grant vest in annual increments of varying percentages, depending on seniority level, through 2006. On December 1 of each year of the agreement beginning in 1998 and through December 1, 2008, additional options will be granted to Dispatchers who become eligible during that year. No options were granted on December 1, 1998 or 1999. Options under all grants must be exercised prior to June 30, 2012, or within a specified time upon retirement or termination.

Under the 1999 Southwest Airlines Professional Instructors' Association Non-Qualified Stock Option Plan (SWAPIA Plan), the Company may grant options to Professional Instructors for up to 525,000 shares of common stock. An initial grant of approximately 229,500 shares was made on May 20, 1999, at an option price of \$22.60 per share, which exceeded the market price of the Company's stock on that date. Options granted under the initial grant vest in ten annual increments of ten percent. On January 1 of each year of the agreement beginning in 2001, additional options will be granted to Professional Instructors who become eligible during that year. Options under all grants must be exercised prior to June 30, 2012, or within a specified time upon retirement or termination.

Under all fixed option plans, except the SWAPA, SAEA, and SWAPIA Plans, the exercise price of each option equals the market price of the Company's stock on the date of grant. Under the SWAPA, SAEA, and SWAPIA Plans, for additional options granted

each September 1, December 1, and January 1, respectively, the exercise price will be equal to 105 percent of the fair value of such stock on the date of the grant.

Information regarding the Company's seven fixed stock option plans, as adjusted for stock splits, is summarized below:

<i>(In thousands except exercise prices)</i>	INCENTIVE PLANS		NON-QUALIFIED PLANS	
	OPTIONS	AVERAGE EXERCISE PRICE	OPTIONS	AVERAGE EXERCISE PRICE
Outstanding December 31, 1996	21,046	\$4.90	50,639	\$5.94
Granted – Incentive Plans	5,524	6.45	-	-
Granted – SWAPA Plan	-	-	1,984	8.79
Granted – Other Non-Qualified Plans	-	-	327	6.45
Exercised	(2,592)	4.02	(3,987)	5.90
Surrendered	<u>(1,507)</u>	6.48	<u>(223)</u>	6.04
Outstanding December 31, 1997	22,471	5.27	48,740	6.06
Granted – Incentive Plans	4,108	11.81	-	-
Granted – SWAPA Plan	-	-	1,354	12.91
Granted – SAEA Plan	-	-	1,107	13.08
Granted – Other Non-Qualified Plans	-	-	384	11.79
Exercised	(3,541)	4.18	(3,782)	6.05
Surrendered	<u>(1,252)</u>	7.01	<u>(371)</u>	6.63
Outstanding December 31, 1998	21,786	6.59	47,432	6.46
Granted – Incentive Plans	3,064	17.56	-	-
Granted – SWAPA Plan	-	-	1,306	17.52
Granted – SAEA Plan	-	-	-	-
Granted – SWAPIA Plan	-	-	230	22.60
Granted – Other Non-Qualified Plans	-	-	303	17.46
Exercised	(3,197)	4.55	(2,313)	6.31
Surrendered	<u>(1,102)</u>	8.14	<u>(440)</u>	7.07
Outstanding December 31, 1999	<u>20,551</u>	\$8.46	<u>46,518</u>	\$6.92
Exercisable December 31, 1999	5,279	\$6.86	22,174	\$6.50
Available for granting in future periods				
	15,981		9,279	

The following table summarizes information about stock options outstanding under the seven fixed option plans at December 31, 1999:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE		
	OPTIONS OUTSTANDING AT 12/31/99	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED-AVERAGE EXERCISE PRICE	OPTIONS EXERCISABLE AT 12/31/99	WEIGHTED-AVERAGE EXERCISE PRICE	
\$1.78 to \$2.31	3,182	1.1 yrs	\$1.85	1,664	\$1.92	
\$3.36 to \$3.57	606	2.1	3.56	245	3.57	
\$5.57 to \$8.06	50,132	6.8	6.13	22,246	6.06	
\$8.80 to \$13.08	8,484	8.1	11.48	2,633	11.26	
\$15.72 to \$22.60	<u>4,665</u>	8.6	17.80	<u>665</u>	17.73	
\$1.78 to \$22.60	<u>67,069</u>	6.7 yrs	\$7.40	<u>27,453</u>	\$6.57	

The Company has granted options to purchase the Company's common stock related to employment contracts with the Company's president and chief executive officer. Depending upon the grant, these options have terms of ten years from the date of grant or ten years from the date exercisable and vest and become fully exercisable over three or four years. No options were granted in 1999, 1998, or 1997. At December 31, 1999, 1998, and 1997, total options of 5.0 million, 5.5 million, and 5.9 million were outstanding, respectively. At December 31, 1999, total options of 4.5 million were exercisable at exercise prices ranging from \$1.00 to \$6.96 per share. Options for 570,000, 342,000, and 531,000 shares were exercised in 1999, 1998, and 1997, respectively.

Under the 1991 Employee Stock Purchase Plan (ESPP), at December 31, 1999, the Company is authorized to issue up to a balance of 1.3 million shares of common stock to Employees of the Company at a price equal to 90 percent of the market value at the end of each purchase period. Common stock purchases are paid for through periodic payroll deductions. Participants under the plan received 649,000 shares in 1999, 677,000 shares in 1998, and 990,000 shares in 1997 at average prices of \$16.24, \$11.63, and \$7.11, respectively.

Pro forma information regarding net income and net income per share is required by SFAS 123 and has been determined as if the Company had accounted for its Employee stock-based compensation plans and other stock options under the fair value method of SFAS 123. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants under the fixed option plans in 1999, 1998, and 1997, respectively: dividend yield of .12 percent, .16 percent, and .22 percent; expected volatility of 35.66 percent, 38.20 percent, and 38.23 percent; risk-free interest rate of 6.68 percent, 4.66 percent, and 5.80 percent; and expected lives of 5.0 years for all periods. Assumptions for the stock options granted to the Company's president and chief executive officer were the same as for the fixed option plans except for the weighted-average expected lives of 8.0 years.

The weighted-average fair value of options granted under the fixed option plans, except the SAEA and SWAPIA Plans, during 1999, 1998, and 1997 was \$7.45, \$4.78, and \$2.72, respectively, for the incentive plans; \$6.79, \$4.76, and \$3.41, respectively, for the SWAPA Plan; and \$7.39, \$4.77, and \$2.72, respectively, for other non-qualified plans. The weighted-average fair value of options granted in 1998 under the SAEA Plan was \$4.83. The weighted-average fair value of options granted in 1999 under the SWAPIA Plan

was \$8.81. The weighted-average fair value of each purchase right under the ESPP granted in 1999, 1998, and 1997, which is equal to the ten percent discount from the market value of the common stock at the end of each purchase period, was \$1.75, \$1.29, and \$0.79, respectively.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including expected stock price volatility. Because the Company's Employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its Employee stock options.

For purposes of pro forma disclosures, the estimated fair value of stock-based compensation plans and other options is amortized to expense primarily over the vesting period. The Company's pro forma net income and net income per share is as follows:

<i>(In thousands except per share amounts)</i>	<b>1999</b>	<b>1998</b>	<b>1997</b>
<b>NET INCOME:</b>			
As reported	\$474,378	\$433,431	\$317,772
Pro forma	\$459,669	\$421,097	\$306,553
<b>NET INCOME PER SHARE, BASIC:</b>			
As reported	\$.94	\$.87	\$.64
Pro forma	\$.91	\$.84	\$.62
<b>NET INCOME PER SHARE, DILUTED:</b>			
As reported	\$.89	\$.82	\$.62
Pro forma	\$.86	\$.79	\$.60

As required, the pro forma disclosures above include only options granted since January 1, 1995. Consequently, the effects of applying SFAS 123 for providing pro forma disclosures may not be representative of the effects on reported net income for future years until all options outstanding are included in the pro forma disclosures.

## **10. EMPLOYEE PROFITSHARING AND SAVINGS PLANS**

Substantially all of Southwest's Employees are members of the Southwest Airlines Co. Profitsharing Plan. Total profitsharing expense charged to operations in 1999, 1998, and 1997 was \$138.3 million, \$120.7 million, and \$91.3 million, respectively.

The Company sponsors Employee savings plans under Section 401(k) of the Internal Revenue Code. The plans cover substantially all full-time Employees. The amount of matching contributions varies by Employee group. Company contributions generally vest over five years with credit for prior years' service granted. Company matching contributions expensed in 1999, 1998, and 1997 were \$53.7 million, \$46.4 million, and \$39.7 million, respectively.

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## 11. INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The components of deferred tax assets and liabilities at December 31, 1999 and 1998, are as follows:

<i>(In thousands)</i>	1999	1998
<b>DEFERRED TAX LIABILITIES:</b>		
Accelerated depreciation	\$782,341	\$641,673
Scheduled airframe maintenance	47,168	40,073
Other	<u>110,638</u>	<u>95,485</u>
Total deferred tax liabilities	940,147	777,231
<b>DEFERRED TAX ASSETS:</b>		
Deferred gains from sale and leaseback of aircraft	101,960	107,157
Capital and operating leases	64,704	61,275
Other	<u>102,070</u>	<u>80,326</u>
Total deferred tax assets	<u>268,734</u>	<u>248,758</u>
Net deferred tax liability	<u>\$671,413</u>	<u>\$528,473</u>

The provision for income taxes is composed of the following:

<i>(In thousands)</i>	1999	1998	1997
<b>CURRENT:</b>			
Federal	\$137,393	\$143,989	\$102,938
State	<u>18,900</u>	<u>19,357</u>	<u>14,535</u>
Total current	156,293	163,346	117,473
<b>DEFERRED:</b>			
Federal	128,984	96,237	75,990
State	<u>13,956</u>	<u>12,098</u>	<u>5,721</u>
Total deferred	<u>142,940</u>	<u>108,335</u>	<u>81,711</u>
	<u>\$299,233</u>	<u>\$271,681</u>	<u>\$199,184</u>

The Company received a statutory notice of deficiency from the Internal Revenue Service (IRS) in July 1995 in which the IRS proposed to disallow deductions claimed by the Company on its federal income tax returns for the taxable years 1989 through 1991 for the costs of certain aircraft inspection and maintenance procedures. The IRS has proposed similar adjustments to the tax returns of numerous other members of the airline industry. In response to the statutory notice of deficiency, the Company filed a petition in the United States Tax Court on October 30, 1997, seeking a determination that the IRS erred in disallowing the deductions claimed by the Company and there is no deficiency in the Company's tax liability for the taxable years in issue. It is expected that the Tax Court's decision will not be entered for several years. Management believes the final resolution of this controversy will not have a material adverse effect upon the financial position or results of operations of the Company.

The effective tax rate on income before income taxes differed from the federal income tax statutory rate for the following reasons:

<i>(In thousands)</i>	<b>1999</b>	<b>1998</b>	<b>1997</b>
Tax at statutory			
U.S. tax rates	\$270,764	\$246,789	\$180,935
Nondeductible items	6,664	5,099	5,893
State income taxes, net of federal benefit	21,356	20,445	13,166
Other, net	449	(652)	(810)
Total income tax provision	<u>\$299,233</u>	<u>\$271,681</u>	<u>\$199,184</u>

## 12. NET INCOME PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

<i>(In thousands except per share amounts)</i>	<b>1999</b>	<b>1998</b>	<b>1997</b>
<b>NUMERATOR:</b>			
Net income, available to common stockholders	<u>\$474,378</u>	<u>\$433,431</u>	<u>\$317,772</u>
<b>DENOMINATOR:</b>			
Weighted-average shares outstanding, basic	503,065	500,013	492,947
Dilutive effect of Employee stock options	<u>32,862</u>	<u>29,736</u>	<u>18,836</u>
Adjusted weighted-average shares outstanding, diluted	<u>535,927</u>	<u>529,749</u>	<u>511,783</u>

**NET INCOME PER SHARE:**

Basic	<u>\$ .94</u>	<u>\$ .87</u>	<u>\$ .64</u>
Diluted	<u>\$ .89</u>	<u>\$ .82</u>	<u>\$ .62</u>

The Company has excluded 259,700 and 1,141,355 shares from its calculations of dilutive earnings per share in 1999 and 1997, respectively, as they represent antidilutive stock options for the respective periods presented. There were no antidilutive stock options in 1998.

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**REPORT OF ERNST & YOUNG LLP INDEPENDENT AUDITORS**

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**THE BOARD OF DIRECTORS AND SHAREHOLDERS  
SOUTHWEST AIRLINES CO.**

We have audited the accompanying consolidated balance sheets of Southwest Airlines Co. as of December 31, 1999 and 1998, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Southwest Airlines Co. at December 31, 1999 and 1998, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1999, in conformity with accounting principles generally accepted in the United States.

ERNST &amp; YOUNG, LLP

Dallas, Texas

January 18, 2000

## QUARTERLY FINANCIAL DATA (UNAUDITED)

<i>(In thousands except per share amounts)</i>	THREE MONTHS ENDED			
	MARCH 31	JUNE 30	SEPT. 30	DEC. 31
1999				
Operating revenues	\$1,075,571	\$1,220,432	\$1,235,166	\$1,204,418
Operating income	166,617	254,331	206,463	154,165
Income before income taxes	156,102	256,598	207,949	152,962
Net income	95,847	157,757	126,978	93,796
Net income per share, basic	.19	.31	.25	.19
Net income per share, diluted	.18	.29	.24	.18
1998				
Operating revenues	\$942,653	\$1,078,841	\$1,094,830	\$1,047,656
Operating income	111,693	208,548	203,919	159,451
Income before income taxes	114,057	216,547	211,055	163,453
Net income	70,008	133,393	129,645	100,385
Net income per share, basic	.14	.27	.26	.20
Net income per share, diluted	.13	.25	.24	.19

## COMMON STOCK PRICE RANGES AND DIVIDENDS

Southwest's common stock is listed on the New York Stock Exchange and is traded under the symbol LUV. The high and low sales prices of the common stock on the Composite Tape and the quarterly dividends per share, as adjusted for the August 1998 and July 1999 three-for-two stock splits, were:

PERIOD	DIVIDENDS	HIGH	LOW
1999			
1st Quarter	\$.00500	\$22.92	\$14.92
2nd Quarter	.00550	23.58	19.54
3rd Quarter	.00550	22.29	14.38
4th Quarter	.00550	18.81	15.00
1998			
1st Quarter	\$.00445	\$14.28	\$10.22
2nd Quarter	.00445	13.81	11.22
3rd Quarter	.00500	15.58	11.46
4th Quarter	.00500	15.83	10.21



## TEN-YEAR SUMMARY

### SELECTED CONSOLIDATED FINANCIAL DATA (1)

<i>(In thousands except per share amounts)</i>	1999	1998	1997	1996
Operating revenues:				
Passenger	\$4,499,360	\$3,963,781	\$3,639,193	\$3,269,238
Freight	102,990	98,500	94,758	80,005
Other	133,237	101,699	82,870	56,927
Total operating revenues	4,735,587	4,163,980	3,816,821	3,406,170
Operating expenses	3,954,011	3,480,369	3,292,585	3,055,335
Operating income	781,576	683,611	524,236	350,835
Other expenses (income), net	7,965	(21,501)	7,280	9,473
Income before income taxes	773,611	705,112	516,956	341,362
Provision for income taxes (3)	299,233	271,681	199,184	134,025
Net income (3)	\$474,378	\$433,431	\$317,772	\$207,337
Net income per share, basic (3)	\$.94	\$.87	\$.64	\$.42
Net income per share, diluted (3)	\$.89	\$.82	\$.62	\$.41
Cash dividends per common share	\$.02150	\$.01889	\$.01471	\$.01303
Total assets	\$5,652,113	\$4,715,996	\$4,246,160	\$3,723,479
Long-term debt	\$871,717	\$623,309	\$628,106	\$650,226
Stockholders' equity	\$2,835,788	\$2,397,918	\$2,009,018	\$1,648,312

### CONSOLIDATED FINANCIAL RATIOS (1)

Return on average total assets	9.2 %	9.7 %	8.0 %	5.9 %
Return on average stockholders' equity	18.1 %	19.7 %	17.4 %	13.5 %

### CONSOLIDATED OPERATING STATISTICS (2)

Revenue passengers carried	57,500,213	52,586,400	50,399,960	49,621,504
RPMs (000s)	36,479,322	31,419,110	28,355,169	27,083,483
ASMs (000s)	52,855,467	47,543,515	44,487,496	40,727,495
Passenger load factor	69.0 %	66.1%	63.7%	66.5%
Average length of passenger haul	634	597	563	546
Trips flown	846,823	806,822	786,288	748,634
Average passenger fare	\$78.25	\$75.38	\$72.21	\$65.88
Passenger revenue yield per RPM	12.33¢	12.62¢	12.84¢	12.07¢
Operating revenue yield per ASM	8.96¢	8.76¢	8.58¢	8.36¢
Operating expenses per ASM	7.48¢	7.32¢	7.40¢	7.50¢
Fuel cost per gallon (average)	52.71¢	45.67¢	62.46¢	65.47¢
Number of Employees at yearend	27,653	25,844	23,974	22,944
Size of fleet at yearend (9)	312	280	261	243

## CHART CONT'

1995	1994	1993	1992	1991	1990
\$2,760,756	\$2,497,765	\$2,216,342	\$1,623,828	\$1,267,897	\$1,144,421
65,825	54,419	42,897	33,088	26,428	22,196
<u>46,170</u>	<u>39,749</u>	<u>37,434</u>	<u>146,063</u>	<u>84,961</u>	<u>70,659</u>
2,872,751	2,591,933	2,296,673	1,802,979	1,379,286	1,237,276
<u>2,559,220</u>	<u>2,275,224</u>	<u>2,004,700</u>	<u>1,609,175</u>	<u>1,306,675</u>	<u>1,150,015</u>
313,531	316,709	291,973	193,804	72,611	87,261
<u>8,391</u>	<u>17,186</u>	<u>32,336</u>	<u>36,361</u>	<u>18,725</u>	<u>6,827 (6)</u>
305,140	299,523	259,637	157,443	53,886	80,434
<u>122,514</u>	<u>120,192</u>	<u>105,353</u>	<u>60,058</u>	<u>20,738</u>	<u>29,829</u>
<u>\$182,626</u>	<u>\$179,331</u>	<u>\$154,284 (4)</u>	<u>\$97,385 (5)</u>	<u>\$33,148</u>	<u>\$50,605</u>
\$.38	\$.37	\$.32 (4)	\$.21 (5)	\$.08	\$.11
\$.37	\$.36	\$.31 (4)	\$.20 (5)	\$.07	\$.11
\$.01185	\$.01185	\$.01146	\$.01047	\$.00987	\$.00955
\$3,256,122	\$2,823,071	\$2,576,037	\$2,368,856	\$1,854,331	\$1,480,813
\$661,010	\$583,071	\$639,136	\$735,754	\$617,434	\$327,553
\$1,427,318	\$1,238,706	\$1,054,019	\$879,536	\$635,793	\$607,294
6.0 %	6.6 %	6.2 % (4)	4.6 % (5)	2.0 %	3.5 %
13.7 %	15.6 %	16.0 % (4)	12.9 % (5)	5.3 %	8.4 %
44,785,573	42,742,602 (7)	36,955,221 (7)	27,839,284	22,669,942	19,830,941
23,327,804	21,611,266	18,827,288	13,787,005	11,296,183	9,958,940
36,180,001	32,123,974	27,511,000	21,366,642	18,491,003	16,411,115
64.5%	67.3 %	68.4 %	64.5 %	61.1 %	60.7 %
521	506	509	495	498	502
685,524	624,476	546,297	438,184	382,752	338,108
\$61.64	\$58.44	\$59.97	\$58.33	\$55.93	\$57.71
11.83¢	11.56¢	11.77¢	11.78¢	11.22¢	11.49¢
7.94¢	8.07¢	8.35¢	7.89¢	7.10¢	7.23¢
7.07¢	7.08¢	7.25¢ (8)	7.03¢	6.76¢	6.73¢
55.22¢	53.92¢	59.15¢	60.82¢	65.69¢	77.89¢
19,933	16,818	15,175	11,397	9,778	8,620
224	199	178	141	124	106

(1) *The Selected Consolidated Financial Data and Consolidated Financial Ratios for 1992 through 1990 have been restated to include the financial results of Morris Air Corporation (Morris)*

(2) *Prior to 1993, Morris operated as a charter carrier; therefore, no Morris statistics are included for these years*

(3) *Pro forma for 1992 through 1990 assuming Morris, an S-Corporation prior to 1993, was taxed at statutory rates*

(4) *Excludes cumulative effect of accounting changes of \$15.3 million (\$.03 per share)*

- (5) *Excludes cumulative effect of accounting change of \$12.5 million (\$.03 per share)*
- (6) *Includes \$2.6 million gains on sales of aircraft and \$3.1 million from the sale of certain financial assets*
- (7) *Includes certain estimates for Morris*
- (8) *Excludes merger expenses of \$10.8 million*
- (9) *Includes leased aircraft*

## CORPORATE DATA

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### **TRANSFER AGENT AND REGISTRAR**

Registered shareholder inquiries regarding stock transfers, address changes, lost stock certificates, dividend payments, or account consolidation should be directed to:

Continental Stock Transfer & Trust Company  
2 Broadway  
New York, New York 10004  
(212) 509-4000

### **STOCK EXCHANGE LISTING**

New York Stock Exchange  
Ticker Symbol: LUV

### **INDEPENDENT AUDITORS**

Ernst & Young LLP  
Dallas, Texas

### **GENERAL OFFICES**

P.O. Box 36611  
Dallas, Texas 75235-1611

## **ANNUAL MEETING**

The Annual Meeting of Shareholders of Southwest Airlines Co. will be held at 10:00 a.m. on May 17, 2000, at the Southwest Airlines Corporate Headquarters, 2702 Love Field Drive, Dallas, Texas.

## **FINANCIAL INFORMATION**

A copy of the Company's Annual Report on Form 10-K as filed with the U.S. Securities and Exchange Commission (SEC), as well as other financial information, may be obtained without charge by writing or calling:

Southwest Airlines Co.  
Investor Relations  
P.O. Box 36611  
Dallas, Texas 75235-1611  
Telephone (214) 792-4908

Company documents filed electronically with the SEC can also be found on the SEC's web site (<http://www.sec.gov>). A copy of this Annual Report and other financial information can be found on Southwest's web site (<http://www.southwest.com>).

**DIRECTORS**

SAMUAL E. BARSHOP  
Chairman of the Board, Barshop & Oles Co., Inc.,  
San Antonio, Texas;  
Audit and Compensation (Chairman) Committees

GENE H. BISHOP  
Retired, Dallas, Texas;  
Audit, Compensation, and Executive Committees

C. WEBB CROCKETT  
Shareholder and Director, Fennemore Craig,  
Attorneys at Law, Phoenix, Arizona;  
Audit Committee

WILLIAM P. HOBBY  
Chairman of the Board,  
Hobby Communications, L.L.C.;  
Former Lieutenant Governor of Texas;  
Houston, Texas;  
Audit and Compensation Committees

TRAVIS C. JOHNSON  
Partner, Johnson & Bowen,  
Attorneys at Law, El Paso, Texas;  
Chairman, Audit Committee

HERBERT D. KELLEHER  
Chairman of the Board, President, and  
Chief Executive Officer of Southwest Airlines  
Co.,  
Dallas, Texas; Executive Committee

ROLLIN W. KING  
Retired, Dallas, Texas;  
Audit and Executive Committees

WALTER M. MISCHER, SR.  
Managing Partner,  
Wheatstone Investments, L.P.,  
Houston, Texas (Real Estate Development);  
Audit and Compensation Committees

**OFFICERS**

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Chairman of the Board, President,  
and Chief Executive Officer

COLLEEN C. BARRETT\*  
Executive Vice President — Customers and  
Corporate Secretary

GARY A. BARRON  
Executive Vice President

JOHN G. DENISON\*  
Executive Vice President — Corporate  
Services

JAMES C. WIMBERLY\*  
Executive Vice President — Chief Operations  
Officer

CAROLYN R. BATES  
Vice President — Reservations

DONNA D. CONOVER  
Vice President — Inflight Service and  
Provisioning

GREGORY N. CRUM  
Vice President — Flight Operations

ALAN S. DAVIS  
Vice President — Internal Audit and Special  
Projects

MICHAEL P. GOLDEN  
Vice President — Purchasing

GINGER C. HARDAGE  
Vice President — Public Relations and  
Corporate Communications

ROSS W. HOLMAN  
Vice President — Systems

CAMILLE T. KEITH  
Vice President — Special Marketing

GARY C. KELLY\*  
Vice President — Finance,  
Chief Financial Officer

PETE MCGLADE  
Vice President — Schedule Planning

JAMES F. PARKER\*  
Vice President — General Counsel

RON RICKS\*  
Vice President — Governmental  
Affairs

DAVE RIDLEY\*  
Vice President — Ground  
Operations

JOYCE C. ROGGE\*  
Vice President — Marketing

JAMES A. RUPPEL  
Vice President — Customer  
Relations

ROGER W. SAARI  
Vice President — Fuel Management

ELIZABETH P. SARTAIN\*  
Vice President — People

JM SOKOL  
Vice President — Maintenance and  
Engineering

KEITH L. TAYLOR  
Vice President — Revenue  
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JUNE M. MORRIS

Founder and former Chief Executive Officer  
of Morris Air Corporation,  
Salt Lake City, Utah; Audit Committee

ROBERT E. JORDAN  
Controller

LAURA H. WRIGHT

Treasurer

\*Member of Executive Planning Committee

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