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Merging American Airlines and US Airways (A)

"Well, it looks like we did it," thought then-CEO of US Airways Doug Parker on February 14, 2013, the day it was announced that US Airways (#5 in the United States) would merge with American Airlines (#3), taking the carrier out of a 15-month bankruptcy process. The combined entity, American Airlines Group (AAL), would be the world's largest airline in terms of passenger traffic[1]—6,700 flights per day to 336 cities in 56 countries[2]—and by rewards program membership (over 100 million people).[3] To Parker and then-President of US Airways Scott Kirby, "the last major piece needed to fully rationalize"[4] the U.S. airline industry left four carriers with a combined 86% market share in 2013: AAL ($39 billion in revenues), United Airlines ($37 billion), Delta Airlines ($36 billion), and Southwest Airlines ($17 billion).

Many previous airline mergers, however, had disappointed investors, staff, and passengers; several had cost CEOs their jobs. To avoid this fate, Parker and his team had to manage a delicate balancing act, establishing an integration architecture that allowed their "minnow" of an airline to swallow the "whale" that was to be its partner. Nor was scale the only challenge. Parker also wanted the integration process to be as smooth and transparent as possible to minimize employees' and external stakeholders' anxieties. "Uncertainty," he observed, "is a lot worse than a wrong decision."

In negotiating the merger, Parker had agreed that while American's Chairman, President, and CEO Thomas Horton would be Chairman for a limited time, he was to be CEO of the new entity and would decide on the composition of the executive team. He was considering two broad alternatives: equal representation, or dominance by US Airways. The recent United and Continental merger agreement, for example, had sought equality. Representation on management teams was therefore shared roughly 50/50 between the two legacy management teams. Yet in the America West/US Airways merger orchestrated earlier by Parker, he had relied on the existing America West executive team to emerge as the new leadership team. Should he use the same approach here, bringing the current set of executives over to American, or should he reshuffle the deck and let some of his longtime US Airways colleagues go in order to incorporate leadership from American? Employees, he knew, were watching the decision carefully. They saw the selection of the senior team as a critical signal of the degree to which this transaction was going to play out as a takeover or as a merger.

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Pursuing the Merger

American Airlines declared bankruptcy in late 2011,[5] having lost $1.9 billion on $24.9 billion in revenue while running 3,700 flights per day. In contrast, US Airways had earned $627 million that same year on revenues of $13.8 billion with 3,200 flights per day. Parker, Kirby, and the US Airways executive team—including the then Chief Operating Officer Robert Isom; Executive Vice President—Corporate Affairs Stephen Johnson; Chief Financial Officer Derek Kerr; and Executive Vice President—People Elise Eberwein—had begun pursuing a merger soon after the bankruptcy. Rebuffed by Horton, Parker and Kirby entered secret talks with American's major employee unions—pilots, flight attendants, mechanics, and fleet service clerks—and with American's most important creditors. Because of bankruptcy court filings, Parker knew what American was offering its unions, which enabled US Airways to make a better offer.[6]

On April 20, 2012, Parker announced, through a press release and an SEC filing, that US Airways had obtained signed agreements with each of the three unions, representing over 50,000 American workers, on what their contracts would look like should a merger take place.[7] (This, in itself, was unusual. Labor rarely supported mergers, since they typically led to job cuts.[8]) American planned to eliminate 13,000 jobs and cut or reduce pension and healthcare benefits. Parker, by contrast, believed he could save at least 6,200 of those jobs.[9] The estimated equity value of the combined company was $11 billion.[10] Annual savings were expected to top $1 billion. (See **Exhibit 1** for routes, **Exhibit 2** for financials, and **Exhibit 3** for operating comparisons.)

"The Band of Brothers" + One

Ten months later, after the three agreements were signed, Parker and his top executives had already made a series of operational and design decisions to prepare for integration. Many key questions were already answered. Among the most important issues that still remained, however, were those involving the senior management team. These were not only critical to the leadership of the new airline, but they were the first step in selecting the "down the line" management that would head the combined operations. Parker would soon have to name his final top team, the one that would complete the integration and run the world's largest airline. In making this call, he faced three interrelated issues.

The first was the extent to which AAL should retain executives who best knew the major operating systems. Given the size difference between the two airlines and the likelihood that many of the operating and organization processes of the "new American" would be based upon existing legacy American systems, Parker had to consider to what degree he needed to retain and leverage key American C-suite executives. Those executives had experience with an airline of global scale committed to multi-country, multi-fleet operations, with deep experience working with unions and large numbers of frontline employees.

The second was Parker's belief in the abilities, camaraderie, and shared experiences of the close-knit management team at US Airways. Together, they had weathered the America West/US Airways merger as well as the successful turnaround of US Airways that followed. Many of them were longtime friends. Isom was a University of Michigan alum and member of the core team from Northwest who had rejoined US Airways as Head of Operations after a short stint at GMAC LLC (the finance arm of General Motors). He and CFO Derek Kerr had been graduate school classmates at the University of Michigan. Parker and Kerr had grown up next door to each other, and Kerr's brother was a high school friend of Parker's. Parker and Isom had worked at Northwest in the early 1990s.

When Parker left Northwest in 1993 for America West, he joined President Scott Kirby who, at the time, was a rising star in the revenue management field. Executive Vice President, Corporate Affairs Steve Johnson was part of the original America West team that recruited Parker. "There is a lot of familiarity and a little bit of competitiveness," Isom noted. "We know what is important and everybody's strengths and limitations. We are all pretty direct and when we fight we know how others will react. Finally, we have great confidence in our ability to execute. Ours is not a traditional CEO to senior team relationship; it is more informal and more familial." Essential to the team was former flight attendant and communications executive Elise Eberwein, who had joined the others at America West in 2003 as Vice President, Communications. By 2009, Eberwein had added overseeing all people, communications, and public affairs for US Airways to her responsibilities. Hailed as the "glue that holds the team together," she was described as the "voice of the frontline employee" on Parker's leadership team.

The third issue was the challenge and likely impact of building a team from combatants who had been on opposite sides of the courtroom in bankruptcy and merger proceedings. Particularly visible would be the prospective role for Horton. He had extensive industry experience and was viewed by many of the legacy American staff as representative of the pride and excellence that they felt for the current American operation. Former American Treasurer Beverly Goulet was widely viewed as highly qualified to be the next CFO. Yet Parker's close relationship with Kerr was such that in the interim, Parker named her to help lead the integration. American's government affairs strategy was also top of mind given longtime American executive Will Ris's visibility and bipartisan respect in Washington. Finally, as legacy American CIO, Maya Leibman knew well the capabilities of the American IT systems and had a broad knowledge of its suite of systems as well as detailed knowledge of its strengths and vulnerabilities. Yet most of the US Airways IT operations were going to remain in Phoenix, while Leibman lived and worked in Dallas.

A Tale of Two Airlines

Whatever the composition of the senior executive team, it was clear to all that they would have to bring together two airlines that were different not just in size but also in values, priorities, and culture. US Airways' management focused on operations and tight cost controls; American, by contrast, was described by Isom and others as a "marketing-driven entity, where marketing trumped everything." Not surprisingly, commercial operations had been a historic strength at American, while technical operations were weaker. One implication was that American management had in the past focused heavily on issues involving in-flight services, amenities, in-airport facilities, and customer comfort and image. US Airways was less concerned with these elements, focusing instead on operational details such as load factors, pricing yields, and on-time arrivals and departures.

The result was, at times, different decision rules. For example, some American captains liked to wait for customers who were delayed, believing they could make up any lost time in the air. American ground staff also preferred to avoid dealing with passengers who had just missed their connections. But at US Airways, Kirby noted, "we try to educate captains and everyone that delaying departures has huge snowball effects across the network, often creating havoc for the rest of the interconnected system." For this reason, the decision of when and how long to wait for customers was centralized at US Airways. Finally, according to Isom, the commitment to "tracking" and "learning from errors" was a lower priority for American. One way equipment got damaged, for example, was when it was pulled into and pushed out of the gate. In 2013, US Airways had a total of 27 aircraft damages from this source. At American, the number was about 9–12 per week, causing huge network issues.

Another difference was in the airlines' culture and employees' time in service. Average tenure at American was 16 years for management (with about 88,000 employees);[11] for the 39,000 or so employees at US Airways, management tenure was lower. The much larger American also had its own distinctive norms and values; several executives described it as analytical, hierarchal, and methodical. "You just did not surprise [ex-American CEO] Bob Crandall," noted Parker. "The management culture and processes were very formal." By contrast, the same executives described the US Airways world as warm, friendly, action-oriented, and heavily dependent on relationships. According to Eberwein, "Doug favored the transparent management culture he had built at US Airways, where the team trumped the person, and collaboration was key." Parker added, "At US Airways, we have long had a family feeling—I knew many who worked at headquarters, and I also knew many of our crew members and frontline employees."

Parker held monthly Town Halls at US Airways' training center so that flight crew members, who are notoriously difficult to reach given the largely mobile aspect of their job, had a regular opportunity to interact with senior leadership. Dubbed Crew News, each one consisted of a 10-minute informal state-of-the-airline introduction and a 50-minute Q&A. These were filmed and then posted on the company website. Parker observed: "There is no replacement for talking to employees. You can see who nods, who doesn't, and what the faces in the crowd convey." At American, top management was seen as more remote. The CEO's office in Dallas was at the end of a long corridor that led to a door where an assistant stood guard. Although the building was secure and required identification card access, all visitors to the executive wing, including employees, were required to display an active employment badge to a security guard. There were also reserved executive parking spaces, something Parker had eliminated at US Airways. "In a meritocracy," he explained, "if you want to park close to the building, you have to get here early."

American had been a fixture in Dallas since the late 1970s. It was one of North Texas's largest employers, with almost 25,000 people. The facility was in the shadows of Dallas/Fort Worth (DFW) International Airport, and the main entrance focused on security, with bulletproof glass, a heavy security gate, and several security guards. US Airways, by contrast, had had very modern, open-space headquarters in Tempe, Arizona (near Phoenix), since the late 1980s. Given that Parker would be CEO of the new American, according to Johnson, "It surprised many of our longtime constituents when we were very quick to announce that Dallas would be the new airline's headquarters."

Designing and Managing the Merger Integration Process

Maintaining the core businesses while simultaneously implementing an integration of this scale was certain to pose difficult challenges. The two companies would need to be ready on day one, immediately after the legal close of the deal, to operate seamlessly as one airline. (**Exhibit 4** provides an overview of the merger negotiation process.)

Airline mergers were generally pursued to expand and improve the network, increase bargaining power (e.g., improving vendor contract renegotiations improved cost control), and scale at reduced cost (e.g., reducing duplication of facilities, reservation systems, and back-office administrative functions, etc.). Mergers could vastly improve routes and plane utilization rates, connectivity, and network planning, which, in turn, created a better network for frequent flyers.[12]

Realizing this potential required careful management of three challenges. The first involved labor—a discontented labor force could result in absenteeism and a variety of operational delays or failures, ranging from lost luggage to unresponsive customer service. The second involved strategy and economics—the need to appreciate and resolve any fundamental differences in the two firms' business models and competitive formulas. The third involved systems integration—the need to effectively combine each airline's large legacy IT systems (themselves often a mix of in-house development and off-the-shelf systems) that governed HR, reservations, labor scheduling, and fleet maintenance.[13] Ris and Johnson noted that a fourth challenge would occur in Washington, DC, where regulators and legislators often analyzed airline service with a critical eye based on their own personal experiences.

In addressing these issues, management teams made a set of decisions that required them to choose among three broad approaches: (1) finalizing the merger as quickly and seamlessly as possible; (2) cutting costs as much as possible at the start of the integration effort to realize and report substantial savings and synergies; and/or (3) putting the best processes in place quickly to create a foundation for future growth. Regardless of the choice, leaders needed to decide on the time frame for results and communicate clearly. Typically, different types of transactions required different designs for the integration efforts. Objectives and concerns varied for different types of transactions, requiring different managerial responses, as described in **Appendix A**.

Integration Management Leader/Office

One of the central elements of the integration process and a key differentiator in the success of the very challenging process of knitting together two previously independent companies was the choice of the executive(s) to lead the integration process. The characteristics and background of the chosen leader signaled the approach and seriousness of purpose of the integration that would soon follow. For example, picking the CFO as the integration leader often signaled that cost reductions would trump all or that the integration process would be financially driven, while selecting a seasoned but soon-to-retire executive might cast that person as more of a process manager and less of a driver of decisions. The selection of single versus shared (co-)leadership of the integration also suggested the degree of collaboration and joint decision making that might follow. The shorthand for this choice was the question, "Is it a takeover, or is it a merger?" A takeover usually featured a single leader, while a merger [of equals] usually drew on a shared leadership model.

In early April 2013, Parker announced that Isom and Goulet would co-lead the integration process, reporting to a Transition Committee chaired by Horton and Parker (see **Exhibit 5**). Isom was the logical pick to take the lead, in part because his domain (operations) faced the largest integration challenges, and also because he had previous integration experience from his work at GMAC. More surprising, and deeply important to American executives, was the selection of Goulet as co-lead. She knew the company deeply and broadly, had been Horton's former Treasurer and clear second in command during the bankruptcy process, had gone on record as a strong proponent of having American emerge as a stand-alone entity, and was a lead negotiator with US Airways during their hostile deal negotiation. Nonetheless, she had rapidly gained a reputation among the US Airways team for being fair and balanced.

Initial Launch Activity

Striking the right balance at the outset of the integration was key. "Too much confrontation and an airline can descend into chaos. Too nice a guy in the corner office and unions can walk away with all the money," an observer had written in 2005.[14] To that end, shortly after the announcement of the deal, Parker instructed Isom and Goulet to begin working immediately to set up the integration operation. He also asked Isom and Kerr to spend at least three days a week at American headquarters, visible and approachable to employees.

Isom and Kerr quickly began a round of small group meetings and outreach efforts. Kirby and Johnson similarly began to make many trips to Dallas to get more of an operational sense of the challenges that lay ahead, and take the temperature of the local political scene and engage with the business community of the Metroplex. Executive interviews as a prelude to selection of new management began, and the process to select an external consultant to aid in the effort was launched. From the very outset of the deal, Parker said that he would move his family to Texas and began to seek new schools for his children and a new church. Eberwein noted, "Doug says that you have to believe things before others can see them; he and his wife Gwen set the bar for others by taking the step early on to move their family to Dallas/Fort Worth."

Designing, Staffing, and Running the Integration Management Office

Next, Isom and Goulet, with input from Kerr, had to make a critical staffing decision, picking a group of 5 to 10 executives to serve as the core Integration Management Team (IMT). This group would, with the support of consultants, manage the integration process full-time, serving as the nerve center of merger integration and overseeing aspects of all operations of the two merging entities. In essence, the Integration Management Office (IMO) was the central governance structure of the merger. Its goal was to organize, define, and align staff, systems, and processes to reach both short- and long-term integration milestones.

The IMO was normally launched just as the deal was signed in order to most effectively oversee and coordinate the efforts of a large number of teams of employees who now found themselves with part-time integration assignments. All were assigned to functions and operations that had to be planned and integrated for the start of the new company ("Day One plans"). Teams would also determine the plans for meeting synergy goals (i.e., cost savings targets) and recommend how their organizations would be reorganized and integrated after close.

Usually, the IMO remained up and running from the deal announcement through the period of regulatory review and legal close, and often beyond to plan for all the actions that would accompany the need to operate as one company. This could take months or years. To that end, the IMO was tasked with producing the "blueprints" for the new integrated organization. These blueprints described not only the nature of the type of building/organization the new company would use, but also all the connecting "pipes" and systems that were required for the new organization to function. Finally, these plans had to spell out the priority for actions and decisions that would be rolled out to build the new, integrated company.

Integration staging involved matters of timing; deciding, for example, what needed to be done and when to present the new company to customers, which costs to cut at what time, how to combine early synergy wins with appropriate delivery of service in other areas, and so on—was of utmost importance because of the trade-offs that were at stake. Slower integration might yield lower immediate synergies but critical long-term benefits. Before full integration occurred, both entities also had to hew to interim approaches and design effective conflict-resolution processes.[15] (**Exhibit 6** lists early integration principles the IMO team devised from prior mergers).

"One or Two in the Box?"

Isom and Goulet immediately began to lay the groundwork for an integration process that at its peak would directly involve hundreds of employees, working on a wide range of projects to knit the airlines together. They had to decide on the preferred approach to staffing project teams. Team design had implications for framing, symbolism, signaling, and positioning, but all raised the same core issue: was this acquisition going to play out as a takeover or as a merger? According to Goulet, this work had an impact on virtually all 100,000 employees.

Takeovers produced winners and losers, with a clearly designated dominant player. In such settings, each of the smaller integration planning teams would be led by a single executive, typically a member of the acquiring company. This approach provided an unambiguous path forward, minimizing the dysfunctional debates and political maneuvering that so often accompanied mergers of equals, with their commitment to shared leadership. Shared leadership situations, in which the transaction brought together two similar-sized companies and the mindset was more of a blended approach, sent a different message, one of parity and equality. In such settings, project teams were normally headed by co-leaders, one from each company—an approach called "two-in-a-box."

Because co-leadership facilitated the sharing of knowledge about the two legacy operations, it could enable faster and better planning. But because co-leaders knew that one of them would likely lose their job once the planning for integration had concluded, this approach could result in considerable tensions, especially around the question of whose legacy approach was superior. This often had the opposite effect of lengthening the entire integration process. Finally, some executives argued that co-leadership was a distraction; it required more of their time and attention, putting greater pressure on maintaining the continuity of the base business at the same time that executives were increasingly drawn away from their day jobs to lead these integration teams.

Despite the risks, Isom and Goulet chose the two-in-a-box approach. Several factors prompted their decision. First, American's dominant size and the realization that the new entity would most likely be adopting a high percentage of its systems meant that legacy American executives had to be actively involved and motivated to provide essential information and participate in the design process. Second, Parker felt that forward momentum was essential given the circumstances. Legacy American employees had to shift their loyalties quickly, visibly, and virtually overnight, becoming outspoken supporters and committed disciples if the integration plan was to have any chance of success.

Initially, 29 teams began the pre-integration analysis. All reported to the IMO. Within four weeks, this design proved to be too complicated and unwieldy, and in May 2014 teams were regrouped under four broad headings. The headings, called "towers," included Commercial, Operations, Customer, and Corporate. Each had its own designated leader to increase accountability. These teams then established a regular meeting cadence. Each week, one of the four key towers was reviewed, and outstanding issues were debated and resolved. Every six weeks, towers held all-day integration summits. They included all members of the towers so everyone could, in the words of one of the consultants involved, "hear the entire story. It also allowed people to let off steam."

Consultants supported the integration teams. Because of their experience, they were able to provide an important reality check, "to whisper, sometimes loudly," a partner noted, that a certain deadline on which a group was counting was likely to slip and why. The consultants also made sure the sessions were interactive and not just slides or classroom-style presentations. Videos, small group work, and other adult learning-based approaches for sharing information helped disparate groups understand each other's issues. For example, the commercial side could better understand the operational impact of schedule changes by going through a mock simulation rather than just sitting through a presentation. One participant observed, "This is like a Rubik's cube, with people pulling one way and some pulling the other. There were lots of meetings and heated debate but ultimately a lot of learning."

"Adopt and Go" or "Best of Both"?

A related design question arose very early in project team meetings: to what extent should optimization be the goal? The issue was central to the choice of blueprints for the combined operations/organization. Should teams simply choose an existing legacy process from either US Airways or American? If so, using what criteria? Alternatively, was this a unique opportunity to step back and, for at least some critical systems or processes, come up with a redesign and reconfiguration that would lead to new, improved approaches with best-in-class status?

Parker was familiar with, and advocated for, an approach called "adopt and go," which involved identifying the best legacy systems, adopting them largely unchanged, and then moving forward as quickly and seamlessly as possible to integrate the resulting operating, managerial, and IT approaches.

The alternative to "adopt and go" was called "best of both" and was based on a different logic. Each airline first studied every individual system's strengths and weaknesses and then engaged in a creative effort to combine both operations to get superior process performance and results. The two approaches were in many ways mirror images of one another. "Adopt and go" was more pragmatic, and the goal was speed and ability to implement. "Best of both" was more long-term oriented; it focused on optimizing system performance. With "adopt and go," Leibman explained, "We choose the path of least resistance, with fewer customers and employees to disrupt and retrain. This approach helps give people a roadmap and eliminates much of the debate about why 'my system is better than yours.'"

By selecting "adopt and go," however, a third option—zeroing in on a few essential processes and making targeted improvements—was discouraged if not eliminated altogether. Also, by treating each decision as a "one-off" to be dealt with on its own, complementary, reinforcing decisions might well be missed. In particular, it was not all clear that the combination of choices, when all were aggregated, would be completely consistent with the strategic vision for the new airline. Finally, because American's legacy systems were likely to dominate the "adopt and go" trade-offs, many legacy American executives could see this as the endorsement of the American way of doing things and thus be resistant to Parker's new operational and cultural vision.

"Integrate Now, Innovate Later" or "Redesign for the Future"?

A major issue in the design and launching of the integration was determining the proper speed, scope, and timing of the changes required to create the "new American Airlines." Here, the critical trade-off involved short- versus long-term commitments, especially those actions and decisions that had high visibility and symbolism but required large, up-front investments of time and money. According to a consultant, "There are major constraints in the short run since the immediate goal is to get the new airline up and running quickly. The more you plan for big changes, the more you take executives' attention away from running the base business. You also need considerable investment capital to enact changes to major IT and operating systems, or the relocation of large number of people, or even the introduction of new capability-building programs."

In particular, once the "adopt and go" decision had been made, the next major choice point was when and to what extent key systems should be redesigned. Once a system was selected, management still had to decide whether to pursue improvements immediately or in the future. Clearly, both airlines ran legacy systems that would eventually require updating regardless of the merger. And given the financial history of the industry, the lack of investment in both airlines' infrastructures was compelling. The merger would increase the urgency of these problems by dramatically increasing the scale and complexity of the tasks being performed. Not only would the new airline be substantially larger; it would also need to lay the groundwork for aggressive future growth and improved customer and employee experiences.

The question was thus when to innovate and improve: sooner or later? Innovating early would decrease the speed of the integration and require new capital investments but would improve performance immediately. Innovating later would allow for faster integration, albeit with the likely use of parallel systems as well as an increased need to retain legacy veteran American executives who already knew the systems.

The difficulty with a deferred approach for the merger was that it pushed the need for virtually all major changes in operating systems far into the future, when resistance to change was likely to have solidified. Without the catalytic effect of the merger process, the need to take care of business as usual tended to delay needed redesign efforts. It was for precisely this reason that many acquisitions used the period of disruption and unfreezing that accompanied their merger announcements to make much-needed investments that might prove too tough to do otherwise. This was the case at American. Goulet noted: "Folks were eager to begin moving to new state-of-the-art systems and applications."

Mindful of Parker's desire for speed, Isom, Kerr, Goulet, and Leibman decided to forgo the immediate redesign of major core processes. Instead, they followed the guideline of "integrate now, innovate later." The aim was to integrate the airlines as soon as possible with existing systems and postpone any investments in improvements and innovations to a later time when the needs of the new airline would be clearer. A smooth, error-free cutover to a single airline became the unambiguous goal.

Isom recalled, "When it comes to systems, we agreed that whatever was best for the company to bite off to get us moving should be the path we take. We might lose out customer service-wise. But to get something launched, you have to make tough trade-offs. We needed to get the merger done and integrate the organizations." In some instances, no management system was perfect, and the team had to make tough calls. "We probably did adopt and go in 75% of the cases around operating systems and policies and procedures," Goulet estimated. In other cases, real-time readjustments were needed. For example, there were unexpected problems in the case of the HR system into which all US Airways employees were to be imported. It was too slow, information was hard to find, decades of customization had occurred, and a workaround was needed for approvals. Eberwein observed, "We thought we would simply deploy US Airways' data into American's systems since US Airways HR had handled far fewer employees. It turned out that some of the American HR systems and processes were customized for an era bygone, and would take us backwards, not to mention the stability of the American system was such that we all had valid concerns it could scale to the new company's anticipated size."

Implementation was problematic in other areas as well. In the case of revenue accounting, neither airline had a state-of-the-art system. "In some instances, we debated too much and let some of that churn happen in the interest of being nice and letting people get to know each other," Leibman noted. "We debated which 'ugly pig' we would choose. In the end, a lot comes down to the business leader, what they are used to, and the process they want to adopt." Here too, the legacy US Airways system was picked because staff responsible for revenue accounting were coming from US Airways. They were familiar with a specific process and had a real desire to maintain it.

Systems such as the general ledger system and procurement were transitioned at once. In the case of reservation systems integration, the team wanted to make sure that this cutover would be smooth, but they also struggled with how to best stagger changes, set priorities, and invest to "get it right first and make it cheaper later." Parker and his tight-knit group of top managers brought a great deal of prior merger experience to this particular system change. What most seared their memory were the challenges of 2005 after merging America West with US Airways. The integration of the two carriers' reservation systems had disappointed, and a replacement reservation system was considered ineffective. Passengers at the time faced long lines; only 30% of planes arrived on time.[16] Parker and his team drew many lessons from this merger around the primacy of systems and cultural integration. "At the time," said Kirby, "we thought we could run it all better. After a while we realized that we had underperformed in the places in which America West's people were better. You have to be honest with yourself and try to improve."

In this instance, three sponsors—airports and reservations, revenue management, and IT—were responsible for making it a success. They had decided to separate the reservations integration from all other integration efforts, even though it would have been easier to combine the frequent flyer systems integration with the reservations systems. The team debated the pros and cons of a "drain-down" versus "knife-edge" transition. In a "drain-down" transition, the process was more gradual, which made it possible to transition different parts of the airline's passenger information system at different times. The airline would essentially be running parallel systems over longer periods of time, and the integration team would be opting to postpone harvesting potential synergies, which in this instance promised to be about $1 billion. In a knife-edge transition, several systems (e.g., passenger information, frequent flyer, and reservations) transitioned at once. "On balance, a drain-down, although more expensive, is helpful because it allows us to separate giant events in time," Leibman said. The team was focused on avoiding failure on the passenger-facing side. The transition involved turning functionality off for US Airways travelers who used to be able to rebook themselves.

Leading a New Culture

Central to any integration was the need to adapt the culture of the legacy operations so that they were well matched to the chosen vision of the new company. Often, the cultural challenges were postponed to less urgent times or assigned to a separate "culture change team." Based on his experience, Parker believed that both approaches were doomed to failure. In his eyes, the choice of the executive team would be a far clearer signal of the preferred culture and style of the new organization.

To that end, senior management had to move forward on four fronts. First, they had to align the new company's operating systems so that they had the maximum influence on driving the culture in the desired direction. Second, they had to ensure through their choice of executives and staff that they had people in place with the capability to adopt and execute the mindsets they sought to instill in the new airline. Third, they had to have a compelling story that captured not just the heads but also the hearts of the broad array of employees that made such a complex organization work. Fourth, they had to model the desired behavior themselves in their own actions and in how they spent their time.

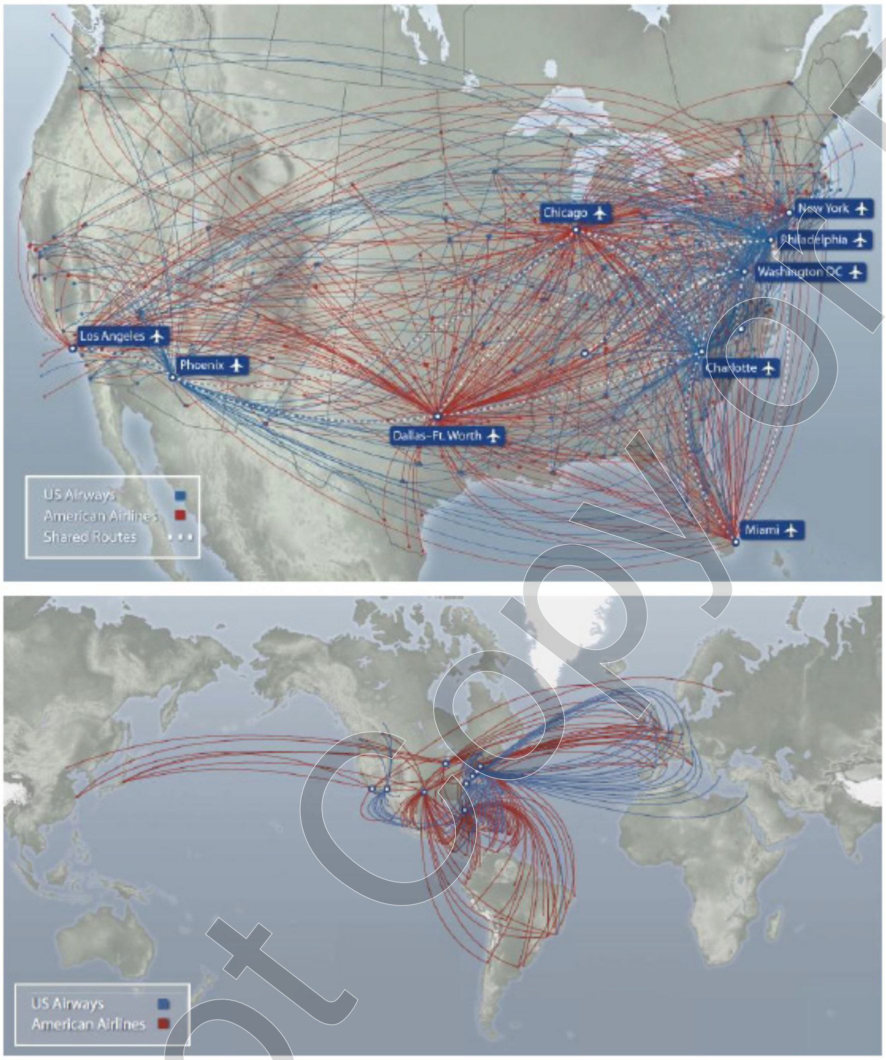
To facilitate this process, Parker put the spotlight on changing how people worked together. He used the integration process to signal an openness to engage in dialogue and debate, asking for candor in discussions and insisting on transparency in monthly integration meetings that now included some 350 people. Subsequent tiers of management were expected to reflect this more informal, empowered mindset in their own behavior. "As these executives travel around," Eberwein explained, "we encourage them to introduce themselves to the crew and hear how things are going. This has been an evolution in behavior, and we have spent a lot of time modeling this behavior and communicating with the frontline. It is important for employees to hear directly from Doug and other members of the senior team. With 100,000 employees, a handful of executives cannot do all the communication effectively."

Parker also wanted employees engaged in business decisions and to feel greater ownership of his vision of the new American. One way to do this was by using the occasion of the change in livery for the airline (effectively rebranding every aspect of the visual presentation of the airline). In January 2013, legacy American executives had unveiled a new logo and plane exterior. The new design had been chosen after a long, expensive, and secretive internal process driven by the executive team. Horton had personally chosen the final logo and paint scheme. Parker, however, saw a major opportunity to involve the entire combined employee base in the choice of the design. To the shock of many members of the team, he announced that he would not simply accept all the design work that had been done; rather, he was going to collect input from the employees and have a vote on whether to keep the old or adopt the new design. He understood that even if the visual outcome were suboptimal there would be lasting and enduring value from a cultural standpoint. The result, as one observer put it, was that "Parker was able to read the tea leaves." Employees picked the new logo.

Picking the Team

For the merger to succeed, it was key that Parker be equally effective in building the new management team. Members would have to come together to work across the various dimensions to build a healthy enterprise. Should Parker use some of these principles, especially around "adopt and go" and "integrate now, innovate later," for his management team, too? He could not announce the team until the merger received Department of Justice approval, which was expected to come 8 to 10 weeks into the integration effort. As he pondered his options, Parker remembered a comment Isom had made a few months back: "Companies that fail in mergers are the ones that struggle with making quick, effective personnel decisions at the top of the house. We need to be directed, motivated, and aligned going in. We could learn from what did and did not work in past efforts—ours such as America West and those of others such as United/Delta." It was with his US Airways team that Parker had learned all these lessons; however, it was the American executives who knew most of the systems that were to be retained.

Exhibit 1 American Airlines and US Airways Routes, 2013



Source: Company documents.

Note: US Airways primarily served the East Coast and Europe. American had more widespread U.S. coverage, but with significant East Coast gaps in service. Among U.S. carriers, American was the market leader for Latin American coverage. Also, while American had some Asian flights, it was a much smaller player in that region than other U.S. competitors.

Exhibit 2a American Airlines Group Statements of Operations ($ millions, 2004–2013 reflects pre-merger, 2014 post-merger)

Year-end December 31	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Total Revenue	18,645	20,712	22,563	22,935	23,766	19,917	22,170	23,979	24,855	26,743	42,650
Cost of Goods Sold	14,003	15,696	16,583	16,900	19,214	15,985	17,064	19,606	19,743	19,797	30,620
Gross Profit	4,642	5,016	5,980	6,035	4,552	3,932	5,106	4,373	5,112	6,946	12,030
Selling General & Admin Exp.	1,107	1,113	1,076	1,028	997	853	976	1,102	1,058	1,158	1,544
Depreciation & Amort.	1,292	1,164	1,157	1,202	1,207	1,104	1,093	915	845	853	1,295
Other Operating Exp./(Income)	2,366	2,577	2,687	2,714	3,024	2,720	2,729	2,637	2,674	2,969	4,118
Other Operating Exp., Total	4,765	4,854	4,920	4,944	5,228	4,677	4,798	4,654	4,577	4,980	6,957
Operating Income	(123)	162	1,060	1,091	(676)	(745)	308	(281)	535	1,966	5,073
Net Interest Exp.	(725)	(743)	(722)	(605)	(589)	(668)	(766)	(785)	(606)	(836)	(856)
Unusual and other	97	(276)	(107)	(30)	(853)	(55)	(13)	(913)	(1,805)	(2,964)	(1,335)
Net Income	(751)	(857)	231	456	(2,118)	(1,468)	(471)	(1,979)	(1,876)	(1,834)	2,882
Supplemental Items											
Advertising Exp.	146	144	154	162	153	153	165	186	153	166	100
Selling and Marketing Exp.	1,107	1,113	1,076	1,028	997	853	976	1,102	1,058	1,158	1,544
Maintenance & Repair Exp.	961	985	971	1,057	1,237	1,280	1,329	1,039	1,158	1,260	2,051

Source: Capital IQ, accessed April 2014.

Exhibit 2b US Airways Group Statements of Operations ($ millions, 2004–2013)

Year-end December 31	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Total Revenue	2,757	5,069	11,557	11,700	12,118	10,458	11,908	12,987	13,765	14,607
Cost of Goods Sold	2,299	4,392	9,049	9,424	10,967	8,499	9,257	10,761	11,084	11,289
Gross Profit	458	677	2,508	2,276	1,151	1,959	2,651	2,226	2,681	3,318
Selling General & Admin Exp.	153	232	446	453	439	382	421	451	463	480
Depreciation & Amort.	54	88	175	189	215	242	248	252	257	302
Other Operating Exp./(Income)	287	453	1,302	1,002	1,599	1,534	1,197	1,079	1,074	1,130
Other Operating Exp., Total	494	773	1,923	1,644	2,253	2,158	1,866	1,782	1,794	1,912
Operating Income	(36)	(96)	585	632	(1,102)	(199)	785	444	887	1,406
Net Interest Exp.	(72)	(117)	(142)	(105)	(175)	(280)	(316)	(323)	(341)	(346)
Unusual and other	19	(324)	(139)	(104)	(938)	274	33	(50)	91	(668)
Net Income	(89)	(537)	304	423	(2,215)	(205)	502	71	637	392
Supplemental Items										
Advertising Exp.	10	13	16	16	10	11	10	11	11	11
Selling and Marketing Exp.	153	232	446	453	439	382	421	451	463	480
Maintenance & Repair Exp.	206	349	653	711	857	781	750	913	832	839

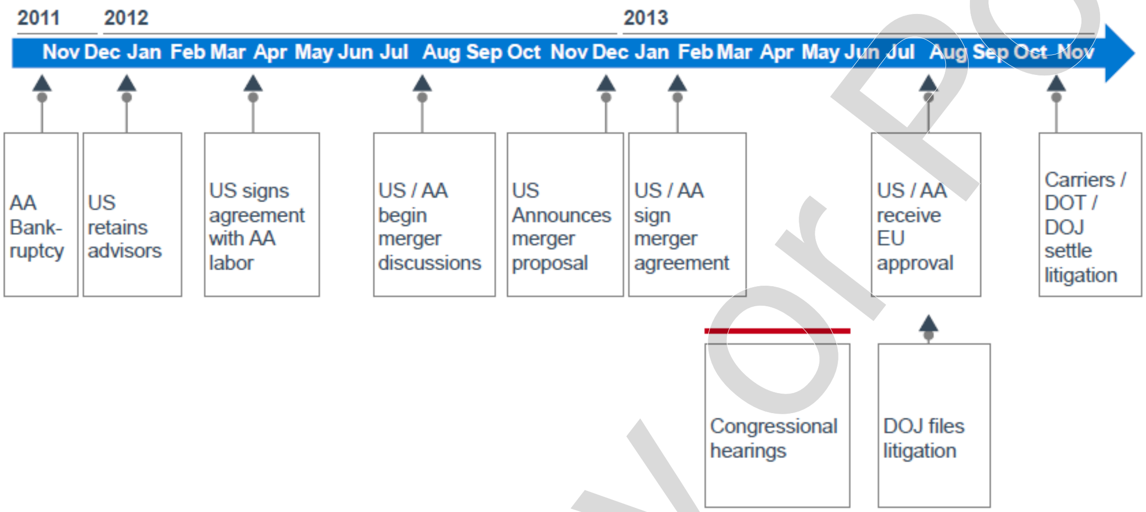
Source: Capital IQ, accessed April 2015.

Exhibit 3 Operating Comparisons

	American Airlines			US Airways		
	2011	**2012**	**2013**	**2011**	**2012**	**2013**
Fuel Consumption and Expense						
Fuel Expense	8,304	13,302	13,217	4,456	4,587	4,533
Fuel Avg. Cost per Gallon ($)	3.01	3.19	3.08	3.11	3.17	3.04
Fuel Consumed ('000s of Gallons)	2,756	4,170	4,295	1,433	1,447	1,489
Capacity and Utilization						
Enplaned Passengers	107.2	190.5	193.7	80.6	82.5	85.0
Revenue Passenger Miles (RPM)	136,386	209,938	215,541	71,321	73,318	76,663
Available Seat Miles (ASM)	167,828	254,648	259,914	86,673	88,425	91,574
Passenger Revenue Yield per RPM	15.16	16.17	16.49	16.20	16.76	16.98
Passenger Revenue Yield per ASM	12.32	13.33	13.67	13.33	13.90	14.22
Operating Expenses per ASM	14.46	9.55	9.53	14.47	14.56	14.42
Load Factor (%)	81.3%	82.4%	82.9%	82.3%	82.9%	83.7%
Number of Hours Flown	2.15	3.35	3.45	1.22	1.21	1.25
Stage Length (mi)	1,429	1,183	1,190	991	1,004	1,013
Number of Trips Flown (Departures)	671,000	1,113,000	1,140,000	452,000	449,000	457,000
Aircraft Information						
Total Number of Aircraft	889	862	1,278	623	622	621
Aircraft Owned	590	586	671	139	152	171
New Aircraft Added	-	1	82	13	15	23
Aircraft Retired during the Year	-	-	66	12	15	20

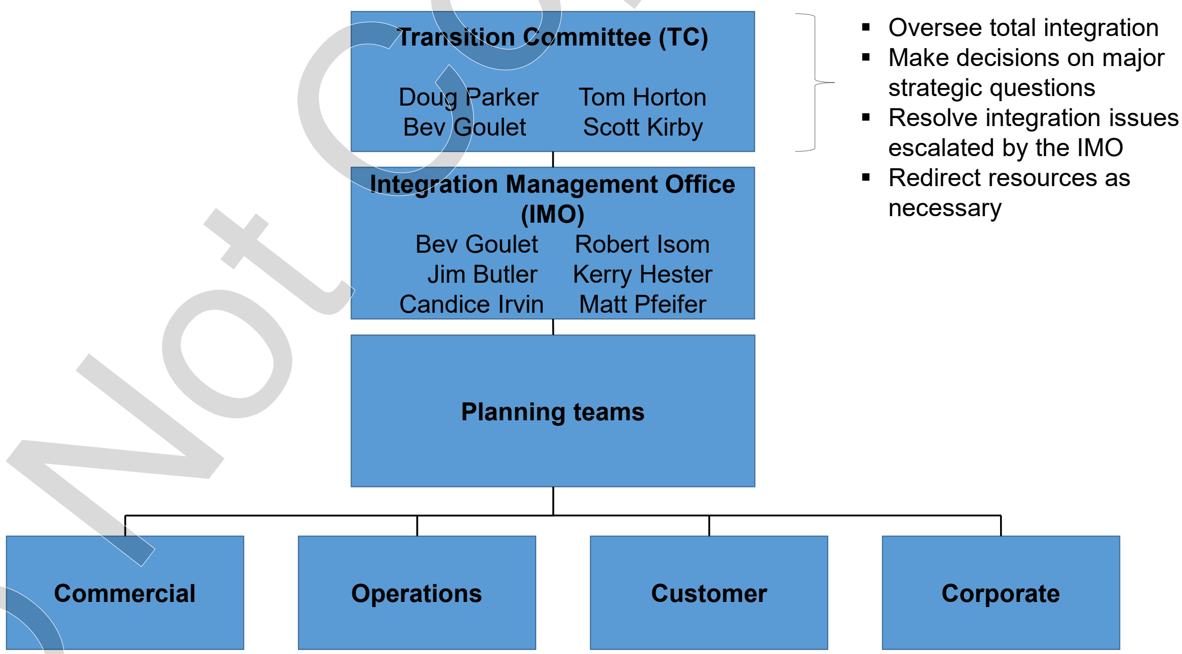
Source: Capital IQ, accessed April 2015.

Exhibit 4 Overview of Major Negotiation Process



Source: Company documents.

Exhibit 5 Structure of the Integration Planning Effort as of April 2013



Source: Company documents.

Note: This represented about 250 employees that were at least involved part-time.

Exhibit 6 Early Principles for Integration

<table>
<tr><td>Focus on the Customer</td><td>- Plan and execute the integration to minimize the risk of customer disruption
- Communicate with customers to build understanding of changes
- Train people to successfully take care of customers as systems, processes change
- Identify opportunities for the merged airline to deliver better customer experience</td></tr>
<tr><td>Recognize Employees as the Key to Success</td><td>- Keep people informed, engaged, excited about their role in our success
    o Over-communicate with goal of "enrolling" people in success of the merger
    o Listen throughout the process and address what's on people's minds
    o Communicate consistent information across both companies
    o Be transparent about the integration and team selection process
- Plan and execute integration to minimize disruption to employee work processes
- Involve subject-matter experts in decisions and plans
- Deliver thorough and effective training to ensure successful change management</td></tr>
<tr><td>Make Fast, Effective Decisions</td><td>- Set and achieve aggressive targets
- Prioritize efforts to simplify integration and achieve greatest value (80/20)
- “Adopt and go” with bias towards the larger carrier unless there is a compelling reason to do otherwise
- Integrate and stabilize first, enhance later
- Focus on the must-haves now; address nice-to-haves later</td></tr>
<tr><td>Realize the Value</td><td>- Prioritize activities to accelerate and maximize value capture
- Focus on creating a competitive financial advantage to Delta Airlines and United Airlines
- Build momentum by achieving quick hits</td></tr>
<tr><td>Run Two Great Airlines throughout the Integration Process</td><td>- First priority (sole focus for most employees):
    o Maintain performance on core safety, reliability and customer experience metrics</td></tr>
</table>

Source: Company documents.

Appendix A M&A Strategies: Distinct Activities Mean Differing Challenges

According to a 2001 article on mergers and acquisitions, acquisitions occurred for five major reasons: (1) "to deal with overcapacity through consolidation in mature industries"; (2) "to roll-up competitors in geographically fragmented industries"; (3) "to extend into new products or markets"; (4) to serve as a "substitute for R&D"; and (5) "to exploit eroding industry boundaries by inventing an industry."

	Overcapacity M&A	Geographic Roll-Up M&A	Product or Market Extension M&A	M&A as R&D	The Industry Consolidation M&A
Example	Raytheon buys Hughes; Daimler acquires Chrysler	T-Mobile and Orange in the United Kingdom	Gillette and P&G	Merck and Schering Plough	Lenovo and IBM PC
Strategic Objectives	The acquiring company (part of an industry with excess capacity) will eliminate capacity, gain market share, and create a more efficient operation.	A successful company expands geographically; operating units remain local.	Acquisitions extend a company's product line or its international coverage.	Acquisitions are used in lieu of in-house R&D to build a market position quickly.	A company bets that a new industry is emerging and tries to establish a position by culling resources from existing industries whose boundaries are eroding.

Because the varying deal archetypes shown above each sought to deliver different sources of competitive value, the operation/organization levers managers had to pull to build that competitive advantage varied accordingly. For this reason, it was critical that the aspirations of the deal be clear before a merger integration approach was designed. The sources of the desired competitive advantage of the merged entities had to be similarly identified early in the process, as did needed changes to the organization and operations required to deliver that aspiration. Only then could an integration approach be chosen, as the list below suggests:

Overcapacity: These types of transactions required maintaining the core part of businesses that brought competitive advantage as executives sought to merge legacy companies together, take advantage of scale effects, and eliminate duplicative operations, facilities, and staffs.

Geographic roll-up: In these transactions, one had to retain and grow the attractive geographical marketing and sales operations of an acquired company while melding the culture and core processes of the acquired company with those of the more dominant acquiring firm.

Product or market extension: Often described as a "bolt-on acquisition," these transactions involved extracting the competitively advantaged products/services in contiguous markets that would build the growth profile of the acquiring company while simultaneously consolidating cultures and core processes as well as securing scale-based synergies.

M&A as R&D: In this type of transaction, management had to extract the essence of the R&D operations and maintain/grow acquired intellectual property that was often embedded in key executives. This had to be done while discarding or selling the other parts of the operations the acquirer did not require or desire to retain.

Industry Consolidation: This type of transaction involved the acquisition of a direct competitor, usually in order to extract maximum cost synergies and garner scale benefits that increased the competitive advantages of the now larger acquiring company.

Source: Adapted from Joseph L. Bower, "Not All M&As Are Alike--and That Matters," *Harvard Business Review* 79, no. 3 (March 2001): 94–95, Business Source Complete (EBSCOhost), accessed March 2016. Examples by casewriters.

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