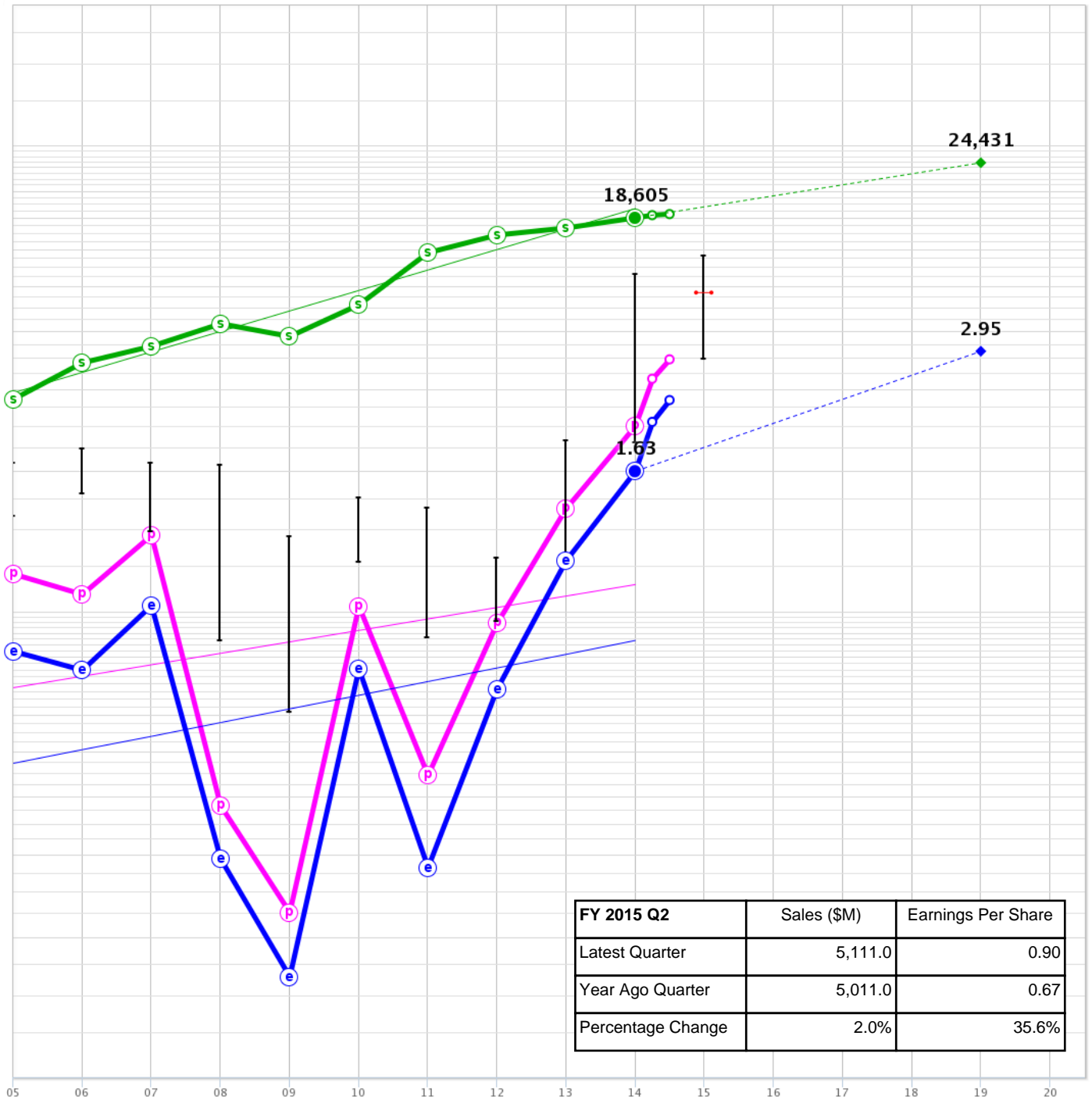


|  |                    |              |                 |               |     |
|--|--------------------|--------------|-----------------|---------------|-----|
| Company                                | Southwest Airlines |              | Date            | 09/18/15      |     |
| Prepared by                            | DIKEMAN            |              | Data taken from | BI Stock Data |     |
| Where traded                           | NYS                | Industry     | Airlines        |               |     |
| Capitalization --- Outstanding Amounts | Reference          |              |                 |               |     |
| Preferred (\$M)                        | 0.0                | % Insiders   | % Institution   |               |     |
| Common (M Shares)                      | 673.0              | 0.8          | 77.0            |               |     |
| Debt (\$M)                             | 2,687.0            | % to Tot Cap | 27.3            | % Pot Dil     | 1.2 |

# Stock Selection Guide

Symbol: LUV

## 1 VISUAL ANALYSIS of Sales, Earnings, and Price



- |                                   |       |  |       |
|-----------------------------------|-------|--|-------|
| (1) Historical Sales Growth       | 10.7% | (3) Historical Earnings Per Share Growth       | 7.0%  |
| (2) Estimated Future Sales Growth | 5.6%  | (4) Estimated Future Earnings Per Share Growth | 12.6% |

## 2 EVALUATING Management

Southwest Airlines

|                         | 2005  | 2006  | 2007  | 2008  | 2009  | 2010  | 2011  | 2012  | 2013  | 2014  | Last 5 Year Avg. |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------------------|
| Pre-tax Profit on Sales | 11.5% | 8.7%  | 10.7% | 2.5%  | 1.6%  | 6.2%  | 2.1%  | 4.0%  | 6.8%  | 9.8%  | 5.8%             |
| % Earned on Equity      | 7.9%  | 7.2%  | 8.9%  | 3.6%  | 1.8%  | 7.4%  | 2.7%  | 5.8%  | 10.5% | 14.8% | 8.2%             |
| % Debt To Capital       | 23.0% | 20.8% | 23.2% | 42.5% | 39.1% | 35.1% | 35.3% | 33.5% | 29.8% | 28.4% | 32.4%            |

## 3 PRICE-EARNINGS HISTORY as an indicator of the future

This shows how stock prices have fluctuated with earnings and dividends. It is building block for translating earnings into future stock prices.

**CLOSING PRICE** 39.5 (9/18/2015)

**HIGH THIS YEAR** 47.17

**LOW THIS YEAR** 28.40

|                                   | A     | B    | C         | D                    | E                                 | F         | G           | H            |  |
|-----------------------------------|-------|------|-----------|----------------------|-----------------------------------|-----------|-------------|--------------|--|
| Year                              | Price |      | Earnings  | Price Earnings Ratio |                                   | Dividend  | % Payout    | % High Yield |  |
|                                   | High  | Low  | Per Share | High A / C           | Low B / C                         | Per Share | F / C * 100 | F / B * 100  |  |
| 5 2010                            | 14.3  | 10.4 | 0.61      | 23.3                 | 17.0                              | 0.02      | 2.9         | 0.2          |  |
| 6 2011                            | 13.6  | 7.2  | 0.23      | 59.1                 | 31.1                              | 0.02      | 7.8         | 0.3          |  |
| 7 2012                            | 10.6  | 7.8  | 0.56      | 19.1                 | 14.0                              | 0.04      | 6.3         | 0.5          |  |
| 8 2013                            | 19.0  | 10.4 | 1.05      | 18.1                 | 9.9                               | 0.13      | 12.4        | 1.3          |  |
| 9 2014                            | 43.2  | 18.8 | 1.63      | 26.5                 | 11.5                              | 0.22      | 13.5        | 1.2          |  |
| AVERAGE                           |       | 10.9 |           | 29.2                 | 16.7                              |           | 8.6         |              |  |
| CURRENT/TTM                       |       |      | 2.32      |                      |                                   | 0.30      | 12.9        |              |  |
| AVERAGE PRICE EARNINGS RATIO 22.9 |       |      |           |                      | CURRENT PRICE EARNINGS RATIO 17.0 |           |             |              |  |

## 4 EVALUATING RISK and REWARD over the next 5 years

Assuming one recession and one business boom every 5 years, calculations are made of how high and how low the stock might sell. The upside-downside ratio is the key to evaluating risk and reward.

### A HIGH PRICE - NEXT 5 YEARS

Avg. High P/E 22.9 X Estimate High Earnings/Share 2.95 = Forecasted High Price \$ 67.6

### B LOW PRICE - NEXT 5 YEARS

(a) Avg. Low P/E 16.7 X Estimate Low Earnings/Share 1.63 = Forecasted Low Price \$ 27.2

(b) Avg. Low Price of Last 5 Years 10.9

(c) Recent Market Low Price 10.4

(d) Price Dividend Will Support  $\frac{\text{Indicated Dividend}}{\text{High Yield}} = \frac{0.22}{1.25\%} = 17.5$

Selected Forecasted Low Price \$ 28.4

### C ZONING using 25%-50%-25%

Forecasted High Price 67.6 Minus Forecasted Low Price 28.4 = 39.2 Range. 25% of Range 9.8

Buy Zone 28.4 to 38.2

Hold Zone 38.2 to 57.8

Sell Zone 57.8 to 67.6

Present Market Price of 39.47 is in the **HOLD** Zone

### D UPSIDE DOWNSIDE RATIO (POTENTIAL GAIN VS. RISK OR LOSS)

$\frac{\text{High Price} - \text{Present Price}}{\text{Present Price} - \text{Low Price}} = \frac{67.6 - 39.47}{39.47 - 28.4} = \frac{28.2}{11.1} = 2.5$  To 1

### E PRICE TARGET (Note: This shows the potential market price appreciation over the next five years in simple interest terms.)

$\frac{\text{High Price} - \text{Closing Price}}{\text{Closing Price}} = \frac{67.6 - 39.47}{39.47} = 1.71$  X 100 = 171.39 - 100 = 71.4 % Appreciation

## 5 5-YEAR POTENTIAL

This combines price appreciation with dividend yield to get an estimate of total return. It provides a standard for comparing income and growth stocks.

**A**  $\frac{\text{Indicated Annual Dividend}}{\text{Closing Price}} = \frac{0.22}{39.47} = 0.01 = 0.8\%$  Current Yield

### B AVERAGE YIELD - USING FORECAST HIGH P/E

$\frac{\text{Avg. \% Payout}}{\text{Forecast High PE}} = \frac{8.6\%}{22.90} = 0.4\%$

### AVERAGE YIELD - USING FORECAST AVERAGE P/E

$\frac{\text{Avg. \% Payout}}{\text{Forecast Average PE}} = \frac{8.6\%}{19.80} = 0.4\%$

### C COMPOUND ANNUAL RETURN - USING FORECAST HIGH P/E

Annualized Appreciation 11.4 %  
Average Yield 0.4 %  
Annualized Rate of Return 11.8 %

### COMPOUND ANNUAL RETURN - USING FORECAST AVG P/E

Annualized Appreciation 8.2 %  
Average Yield 0.4 %  
Annualized Rate of Return 8.6 %