

# Research paper on frank lorenzo

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## **A brief review of leadership and achievements**

### **Abstract**

Frank Lorenzo has no parallels in the airline industry. Rising from a modest beginning he went to command the largest fleet in the world, outside the Soviet Union. Using unique fund raising abilities and cutting costs, he capitalized on the deregulation opportunities of the 1970s to the fore. However it was the attitude of a union buster, which made him considerably unpopular which even triggered the collapse of his airline empire. The unfortunate end of his career may not match what he achieved, but despite all these Lorenzo remains more of a myth today and an inspiration to future business leaders. Lorenzo and his Jet Capital Corporation have no precedents and unlikely to have any in future.

History records the achievements of individuals for the mark they leave behind and its significance in that field. These serve as a source of inspiration and knowledge for all those who pursue those activities. The aviation field has witnessed one such personality during the 1970 s and the 80s. His achievements stand out from the rest of his contemporaries, particularly at a time when the airline industry was itself under experimentation and turmoil. The man was Frank Lorenzo, an American businessman associated with the airline industry, who was also a renowned philanthropist. Born on May 19, 1940 to Spanish immigrants in New York, Lorenzo was educated in public schools. In 1961, he graduated from the Columbia University and two years later from the Harvard Business School. Today Lorenzo is particularly noted for his leadership of the Texas Air Corporation between the years 1972 and 1990, a period that saw him bring

several US airlines under his control. Texas Air Corporation became one of the largest Airline Companies in the world, which in turn had immense consequences for the airline industry, during that period. Although Lorenzo's company soon had the free world's largest commercial fleet of over 650 aircrafts, Lorenzo was criticized for his harsh business practices (Chasing the Sun, 2010). His maneuvers were largely controversial and his tactics were at times outrightly confrontational that soon led to chaos in the travel industry. Despite the remarkable achievements, Lorenzo got a nickname as 'the most hated man in America' (Art History, 2012).

The airline industry of today is quite different from that during the 1970s and the 80s. The recessions of the 1970s and the liability crises of the 1980s subjecting aircraft manufacturers to lawsuits, in addition to several major regulatory reforms offered the airline companies with innumerable opportunities together with innumerable new challenges. The liability insurance premiums increased significantly throughout the 1980s. For instance the industry wide liability premium rose from \$24 million in 1978 to \$210 million in 1985 (American Society of Transportation and Logistics, 1995). These two decades were marked significantly by other factors including the oil crises, high inflation rates particularly during the late 70s and high interest rates during the 80s. Demographic changes in pilot community, higher aircraft costs and enhanced aircraft longevity together with the then prevailing economic conditions truly created a havoc on the airline industry of the 70s and the 80s. However it was in this climate that Lorenzo had worked to establish his airline empire that shook the industry. It is possible that the existing climate was favorable to Lorenzo and that he

fully exploited it, but however the fact remains that none of his contemporaries managed to achieve even half of what he achieved. Unfortunately it was his relentless attitude and strategy to bring down unions, that once even rewarded him, saw him fall off. He soon had too many people in the aviation industry who wanted to see him off. There is no doubt that unions shook with fear of Lorenzo, such that whenever he attempted a takeover, they offered considerable support to his rival. The calculative Lorenzo even used this as a part of his strategy in acquisition.

Lorenzo began his professional career working in the finance division of Trans World Airlines and Eastern Airlines, after several other jobs. Lorenzo's first major break in the industry was in 1969 when he joined hands with Robert Carney to form an aircraft leasing company, called the Jet Capital Corporation. The company acquired Texas International Airlines (TXI) in just three years. TXI was an interstate carrier, based in Houston, Texas, which was struggling. Donald Burr was made the vice president of TXI. The combined approach of Burr and Lorenzo realized quick and remarkable results. Burr was focused on reducing airline fares to make the company more attractive, while Lorenzo focused on reducing operational costs, particularly labor costs. TXI was soon in profit making mode. Despite the philosophical differences, the two worked together and in 1977 Lorenzo received the Aviation Week and Space Technology Laureates Award. After the US government passed the Airline deregulation Act in 1978, Burr left TXI to begin his own People's Express.

The Airline deregulation Act was passed as a US federal law in October 24, 1978, which intended to give more freedom to airline companies. The

government control over fixing of airfares, flying routes, and the entry of new airlines in commercial aviation were totally removed. The powers of the Civil Aeronautics Board (CAB) were to be gradually phased out (AV Stop. com, 2009). Airlines now had the right to fix their own routes and fares. It was perceived that the public would benefit from the competition. However what many didn't realize was that the deregulation offered newer prospects to those airline executives who were familiar with the business transactions, underlying the business. The Act gave newer possibilities to entrepreneurs like Frank Lorenzo who didn't hesitate to exploit it (Chasing the Sun, 2010). Although Lorenzo had competed successfully with the other carriers in the unregulated interstate segment, he would now be exposed to major airlines and that too in an environment of high fuel prices and interest rates. Non-union airlines like Donald Burr's People's Express, that emerged, were soon offering reduced airfares, which unionized airlines couldn't compete with. However Lorenzo resorted to cutting costs, particularly labor costs and undertook junk bond financing as a means to create an airline empire (Art History, 2012). There was reorganization and reevaluation of strategies everywhere and an atmosphere of speculation prevailed over the airline industry. The susceptibility of the giant companies became evident in 1979 when Lorenzo entered into a bidding war with the then iconic Pan American World Airways to acquire National Airlines. Pan American Airways, the original company, was once the United States' official international airline. The Pan Am Building was at one point of time, the largest commercial building in the world. Pan Am was keen to enter the US domestic market and under its chairman William Seawell defeated Lorenzo and successfully bid for

National Airlines. Unfortunately the acquisition occurred at a huge cost of \$400 million, and the merger had a disastrous effect on Pan American. Having paid up more than its actual worth, Pan American slipped into deeper debt, and was soon accumulating loss due to a lack of synergy in its operations with National Airlines. National's operations were concentrated on Florida and there was incompatibility in fleet and route networks. Some of its assets including its iconic building were sold out. For Lorenzo, the turn of events were very fortunate and proved greatly profitable.

In 1980, Lorenzo started a new company Texas Air Corporation, under the control of Jet Capital. Texas Industries (TI) was thus replaced as the holding company of TXI and much of its assets and infrastructure including gates, airport slots, aircrafts and funds were moved to begin a new venture called New York Air. The new venture was based in New York City and gained popularity for being a completely non-union carrier. Apart from reducing labor costs sharply, Lorenzo used New York Air as a threat to the TXI pilots, threatening them with moving away operations from TXI. However an aggressive counter offensive campaign saw the pilots boycott New York Air which brought immense negative publicity for Lorenzo.

Lorenzo continued to systematically acquire airline companies. In 1982 TI was merged with the Denver, Colorado based Continental Airlines and moved its base to the Houston Intercontinental Airport. Within months Texas Air gained a majority control over Continental Airlines. Not wanting to cede to union demands and led by his business acumen, Lorenzo filed for bankruptcy on behalf of Continental and was overwhelmingly rewarded. The court asked the striking workers to report to work and all existing union

agreements were ceased with immediate effect. A new agreement came into affect with the wages of employees cut to almost half, apart from stricter work rules and longer work hours. The tactic adopted by Lorenzo was later mentioned by the Supreme Court in an unrelated case, as being fair.

Although Continental was rescued from liquidation, labor relations and employee morale deteriorated as customer services were affected (Chasing the Sun, 2010). But Lorenzo slashed fares drastically which raised an airfare war throughout the industry. Airline companies were left with no options but to merge with other in order to remain operational and competitive. TWA acquired Ozark while the Northwest acquired Republic Airlines and the Delta acquired Western Airlines. Lorenzo was determined to have a major stake of the airline industry and was focused on more acquisitions. Critics accused Lorenzo of buying struggling airline companies with an eye on their assets and not with an interest of reviving it.

Lorenzo's expression of takeover bids itself had ripple effect. Unions were afraid of Lorenzo that they were willing to offer concessions to his rival bidders. This was exactly what happened when Texas Air tried to take over Trans World Airlines (TWA) in 1985. There was a counter bid from Carl Icahn and TWA unions approached Icahn with support in the form of concessions and the TWA board accepted Icahn's offer though it was lower. Lorenzo soon became well experienced in the science of bidding and takeovers. In October 1985 he went into a bidding war with his former colleague Burr, whose People's Express was in race to acquire Frontier Airlines. Although People's Express acquired it, it paid a high cost, funded by debt. People's Express was soon forced to file for bankruptcy and both People's Express and Frontier

Airlines were acquired by Lorenzo (Art History, 2012). In February 1987, People's Express, New York Air and several other carriers were merged into Continental Airlines.

Lorenzo was soon involved in negotiations with another struggling carrier, Eastern Airlines. To gain control over the workforce, its chairman Frank Borman threatened the employees of selling the airlines to Texas Air. The threat backfired with the union declaring a strike. The ensuing uncertainty aided Lorenzo to acquire Eastern for \$615 million in 1986. Despite acquiring it for a substantially low cost, Lorenzo also had access to an extensive new computerized reservation network. By the end of 1986, Lorenzo was controlling the largest airline company in the world, outside of the Soviet Union. Much of Eastern's assets were transferred to Texas Air and the company was reorganized into divisions that could be sold. Continental planes and their non-union pilots were put on Eastern routes. However Lorenzo failed to get a control on the workforce and tensions were high. The Texas Air plan for Continental was that with Continental's low operational costs, it would drive earnings while Lorenzo would concentrate on Eastern's huge labor costs. Lorenzo unfortunately did not have any plans for synergizing operations with Eastern, although Eastern's assets, routes and planes were transferred to Continental. Many of the new employees were not trained to operate jetways, ticketing, or reservation computers. There were now 13 different types of aircrafts under the control of Continental that required newer standardization procedures necessary to realize mega carrier efficiency (Ennis, 1985). Unfortunately Texas Air only worsened the situation by transferring senior personnel amidst the ongoing



union crises.

Lorenzo's tactics that helped him to break Continental's union just three years back had now failed to do the same with Eastern. His strong arm tactics only ended up in a permanent grounding of the entire Eastern fleet. Lorenzo had received a \$20 million bonus as per the takeover deal he had with Eastern. However when he took over, the demands of the workers intensified, and he used the same set of executives that were involved in dismantling Continental union (Summa, 1989). Eastern Airlines earlier had an innovative plan and agreement with the union that gave union access to the company records and also a role in management decisions. But when Lorenzo took over, he unilaterally cancelled these privileges given to the union.

With an eye on profits, Lorenzo wanted the machinists of Eastern Airlines to accept a pay cut. The machinist union however rejected the request, bringing them into a confrontation with the management. The mechanists union IAM (International Associations of Mechanists) and Aerospace Workers declared a strike in March 1989 which was also supported by the flight attendants and the pilots. As a result of the strike, there were air passenger delays and the company began losing millions of dollars in daily revenues (AVStop. com, 2009). Lorenzo filed for bankruptcy after a creditor had filed a suit against Eastern Airlines. The bankruptcy court being aware of Lorenzo's labor management tactics, appointed Martin Shugrue as a temporary custodian of Eastern. Meanwhile the National Mediation Board recommended appointing a presidential emergency board to resolve the strike, but President George W. Bush did not endorse it. Ultimately the airline was

unsuccessful in coming out of its financial debacle and was forced to shut operations.

The case saw the judge ruling that Lorenzo was not fit to run the operations. Lorenzo was accused by many as having siphoned off Eastern's Pension Fund. Amidst a declining personal image in the airline industry and among the general public, Lorenzo was forced to sell off much of his investments with Continental Airlines by summer 1991, to Scandinavian Airline System. Scandinavian Airlines insisted that Lorenzo resign from Continental. Lorenzo was also asked to give an undertaking that he would stay away from the airline industry for seven years.

However after this, Lorenzo tried to start afresh with a new airline, which he called the Friendship Airline. Lorenzo was determined to show the world that he can run a profitable airline even in 1990s. However the unions wanted him to be barred from the industry. The Airline Pilots Association was also up in arms too, with plans to protest, in case Friendship Airline is permitted. The communications director of the pilot's union Don Skiado noted that no one associated with Lorenzo had won except Lorenzo himself. Don also added that if Lorenzo comes back, he would create more losses and leave. Lorenzo responded in an interview saying that the unions had a plan of projecting him as a destroyer and that the American public was smart and would see him through. But the Department of Transportation rejected his application on grounds of previous safety and compliance irregularities during his leadership of Eastern and Continental. Lorenzo appealed the decision with the Appeals Court but the court ruled the decision by the Department of Transportation as being right, and reiterated that Lorenzo was unfit to begin

a new airline.

Lorenzo has been credited as the first airline chief to offer fares at a discount, the first to attempt hostile takeovers of airline companies and ironically also the first to take manageable airline companies into bankruptcy to suppress labor demands. The airline history has no equivalent precedents nor shall ever have any. There is no doubt that Lorenzo soon became the face of airline deregulation and was easily a super star among business celebrities of the 80s. However unlike many other businessmen of his time, the person inside Lorenzo remains greatly a mystery. Lorenzo rarely gave interviews and adamantly refuses to respond to personal questions. Even the public image of Lorenzo is definitely incomplete in case if it isn't wrong. His image of a union buster and a hungry cost-cutter is something which he refuses to admit. The Columbia University connections describe him as a wonderful team player and always wanting to charm disgruntled employees (Ennis, 1985). His family life includes his wife and four children who lived in a considerably modest house in Houston suburbs, which itself speak more of the person Lorenzo is. The legend of Lorenzo much like the debts he accumulated overtime has been concealed under the veil of myth. Lorenzo is today embedded with every aspect of the airline industry, be it commercial, operations or labor management. As the airline industry evolves with time, future airline leaders would be taught on how to respond appropriately to the changes and demands of the industry. Each of these leaders would then be told of the way Lorenzo reacted or would react in equivalent situations. Through opportunities, forecasting, opponent maneuvering and resorting to courts, Lorenzo used everything in his favor.

Although his forced exit from the airline industry and him being described as ‘ unfit to lead’ would be always associated with his reputation, these would also be questioned with what he had once achieved. Rising from modest and ordinary beginnings to command the largest airline fleet in the free world is no ordinary feat. The myth of Lorenzo would no doubt inspire many entrepreneurs, not just in aviation, but in all other fields too. It is an irony that a man who saw such success at one point of time should be labeled as ‘ the most hated man in America’.

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