case sixteen

Richard Branson and the Virgin Group of Companies in 2007

TEACHING NOTE

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■ SYNOPSIS ■

By 2007, Richard Branson's business empire extended from airlines and railways to financial services and mobile telephone services. There was little evidence of any slowing up of the pace of new business startups. During the first seven years of the new century, he had founded airlines in Australia and the US; wireless telecom companies in Asia, the US, and Australia; several online retailing ventures; a space tourism company; and a biofuels producer. Some of these ventures had been highly successful (e.g. Virgin Blue airline and Virgin Mobile); other Virgin companies were looking distinctly sickly (Virgin Cola and Victory Corporation were commercial and financial disasters; Virgin's retail operations and Virgin Rail were unprofitable). Despite Branson's undiminished enthusiasm for launching new companies that would challenge business orthodoxy and seek new approaches to meeting customer needs, skeptics suggested that the Virgin brand had become overextended and that the Virgin empire lacked strategic coherence.

The case outlines the development of the Virgin group of companies from Branson's first business venture and offers insight into the nature of Branson's leadership, the management principles on which the Virgin companies are launched and operated, and the way in which the group is run.

The case offers the opportunity for a strategic and organizational review of Branson's diversified and loose-knit business empire. What strategic logic underlies the wide range of businesses that coexist under the Virgin name? Do all these businesses fit with the resources and capabilities of the Virgin group, or should some be divested? Is there a need for a more formal organizational and management structure to ensure an optimal balance between entrepreneurial drive and effective control within the group?

■ TEACHING OBJECTIVES ■

The case is primarily a case in corporate strategy. Although the Virgin group is not a single corporation, the close linkage provided by the Virgin name and Branson's ownership implies that we can talk meaningfully about a corporate strategy for the group.

The case allows us to address the fundamental features of corporate strategy: what are the common resources and capabilities that create value for companies within the Virgin group? On the basis of this analysis we can evaluate the diversification strategy of the Virgin group and determine the companies and types of company that the group should comprise.

Once we understand how the group creates value for the constituent companies, we can address the structure and management of the group. What systems does the group need to possess in order to ensure that value is created for the constituent companies? What changes to the financial, organizational, and managerial structure can best support the group's strategy?

The case can also be used to address other aspects of strategic management, including entrepreneurship, brand extension, and corporate culture, to mention a few. However, consistent with my approach in *Contemporary Strategy Analysis*, my focus is on corporate-level advantage, which has its foundations in the resources and capabilities that can be deployed across multiple businesses within the diversified corporation.

■ POSITION IN THE COURSE ■

I use this case to address issues of diversification in the corporate strategy section of my strategy course.

■ ASSIGNMENT QUESTIONS ■

1. What common resources and capabilities link the separate Virgin companies?
2. Which businesses, if any, should Branson consider divesting?
3. What criteria should Branson apply in deciding what new diversification to pursue?
4. What is the Virgin business model?
5. What changes in the financial structure, organizational structure, and management systems of the Virgin group would you recommend?

■ READING ■

R. M. Grant, *Contemporary Strategy Analysis* (6th edn), Blackwell Publishing, 2008, Chapter 15.

■ CASE DISCUSSION AND ANALYSIS ■

1. *The common resources and capabilities that link the Virgin companies.* To begin probing the strategy and business rationale of the Virgin group, I ask about the resources and capabilities that are common to the different Virgin companies. The two critical resources are the Virgin brand and Richard Branson. The capabilities of the group reflect the personality and aptitudes of Branson himself: a risk taker, a self-publicist, an entrepreneur, and an anti-establishment provocateur. What does the Virgin brand represent? That too, it quickly emerges, is closely linked to Branson's personality and values. It conveys honesty, value for money, innovative approaches to customer service and satisfaction, and a statement of opposition to conventional wisdom and the power of established business corporations. Through the organization Branson has created he has institutionalized his entrepreneurial and marketing flair into a number of more systematized capabilities – in particular, Virgin's new business development capability, its brand management and promotional capabilities, and its partnering capabilities (e.g. ability to form and collaborate within joint ventures with other companies).

2. *Which business should Virgin divest?* The simple answer is: those businesses that are performing badly. However, we encounter several problems here. First, because most of Branson's ventures are private companies, we do not have good information on their financial performance. Second, current and past performance is not a good guide to future potential. Most of Branson's new ventures lost money in their early years and, even for an established business, poor current performance does nothing to indicate whether that performance can be turned around. To approach the question at a more fundamental level, we need to take a strategic approach – in particular, consider the characteristics of the businesses where Virgin's common resources (Branson and the Virgin brand) have the potential to add value. Students should be capable of generating a list of the "strategic characteristics" of the kinds of businesses where Virgin's resources seem to be capable of creating competitive advantage. These include:

   - consumer businesses (as opposed to businesses serving producers);
   - startup businesses (Branson's skills are in building businesses from scratch, not acquiring established businesses);
   - businesses where there is the potential for novel and innovative approaches to customer service;
   - businesses where there is a dominant, but preferably staid and sleepy, established player against which Virgin can position itself as the innovative upstart (the "David and Goliath" scenario).

   Such criteria would tend to rule out rail services (not startups; Virgin is the established regional monopolist), cola drinks (not much scope for innovative customer service; the dominant players are hardly staid and sleepy), designer clothes and toiletries, biofuels, and possibly financial services.

3. *What criteria for new diversification?* The above "desirable characteristics" for Virgin businesses identify the sectors and types of enterprise where Virgin can create competitive advantage. Beyond these, Virgin needs to

appreciate the limits to its brand's appeal. To what extent is the appeal of Branson and the Virgin brand limited to Brits of a certain generation? The development of the Virgin group seems to have followed the same life cycle as the Branson generation: pop music in the 1970s, foreign travel in the 1980s, pension funds and investment products in the 1990s. (What next? Old people's homes and funeral parlors?) The other key criterion is industry attractiveness: Virgin needs to enter businesses that have the structural characteristics conducive to good profit margins. What kinds of businesses might fit these criteria – health clubs, medical services through private clinics and hospitals, online retailing?

4. *What is the Virgin business model?* These issues concerning the content of the Virgin business portfolio (and the next set of issues that concern the structure of the Virgin group) focus attention on the identity of the Virgin business model. Possible alternatives include:
   - A brand licensing organization. If the key resource is the Virgin brand, is brand licensing to other companies the primary means by which the group creates value (in the same way the fashion houses of New York, Paris, and Milan are primarily brand licensing operations)? The problem here is that the Virgin brand is closely associated with the personality and character of Branson and separating the two may be difficult.
   - A venture capital organization. If Virgin's core competence is the identification, financing, and launching of new companies, then perhaps the Virgin strategy should focus on seeking business ideas from outside and developing the most promising prospects through minority shareholdings and consulting support.
   - A diversified corporation – the continuing management and coordination of a set of related, diversified businesses in the same way as diversified corporations such as GE, Tyco, and Sara Lee.
   - A new form of network enterprise that links aspects of all the above.

5. *What changes in the financial, organizational, and management structure of the Virgin group?* To recommend changes in the group's structure it is important to identify the current structure of the group. The Virgin companies have very little in the way of formal structure: the operating companies are linked by a number of holding companies (mostly offshore-registered companies) but these are entirely financial conveniences and have no management role. The primary formal linkage between the companies is Branson, who, as founder and major shareholder, is chairman of the companies in which he and his family own a controlling interest. Apart from Branson, there is an informal corporate structure made up of Branson's closest business associates within the Virgin group. While these individuals' primary roles are as executive officers of the individual Virgin companies, they also offer advice and coordination in the management of inter-company issues.

   To recommend changes in the group's structure, it is important to recognize the tasks that that need to be performed in the coordination and controlling of the Virgin companies. These include:
   - Protecting the Virgin brand. At present it is not clear who owns the Virgin trademark and what the terms are under which each of the companies uses the brand. At minimum, the brand needs to be protected through ensuring control over how the brand is presented and ensuring consistency in the image that the Virgin brand projects across the different companies.
   - Financing the companies. The financial data available in the case is limited and somewhat dated. However, there is evidence pointing to the financial precariousness of the Virgin group. The financing arrangements of the Virgin companies remain something of a mystery. While Branson claims that one of the strengths of his group is that each company is independently financed, this raises the possibility, first, that the cost of capital to the companies is higher than it need be and, second, that an unexpected cash shortfall at one company could have dire consequences. These eventualities might suggest either the creation of a single holding company, or launching the most capital-intensive of the Virgin companies as IPOs.
   - Ensuring management control and management continuity. Only Branson exercises formal management control across the Virgin companies. Given the size of the Virgin group and the risk that Branson might fall out of one of his balloons, it is possible that a more formal corporate level of management control is needed. This would monitor the performance of each company, advise each company board on appointments, and identify and advise on matters involving inter-company coordination. Would such a structure require the consolidation of the Virgin companies into a single corporation? Not necessarily – such a group could operate informally and act as an advisory unit that liaises with the board of directors of each Virgin company. This unit might also be responsible for business development. The danger of merging the Virgin companies into a single corporation is that the group loses its entrepreneurial culture.

■ KEY TAKE-AWAYS FROM THE CASE DISCUSSION ■

Fundamental to this case is analysis of competitive advantage at the corporate level. This has its foundations in the identification and understanding of the resources and capabilities of the company and the potential for deploying these across multiple businesses.

Virgin is a particularly interesting case for analyzing the resources and capabilities that confer corporate-level competitive advantage because at first glance the Virgin companies have little in common with one another. This leads to a discussion of the nature of "relatedness" in diversification.

This approach also sheds light on the processes of value creation. Analyzing diversification strategy (whether for Virgin or for other diversified companies) requires that we recognize the processes through which value is created and appropriated. This is what we mean by the "business model" of the diversified corporation. In the case of Virgin, value is created primarily in using the Virgin brand and its business development capabilities to start up and grow new businesses. The business model comprises the strategic logic of the company. Bettis and Prahalad use the term "dominant logic" to describe this concept.[1] Dominant logic is the rationale for the existence of a diversified company and defines the key elements of its corporate strategy.

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Finally, having defined the c[illegible] l/logic/processes through which value is created, we can then be specific about the organizatio[illegible] cture, management systems, and leadership style appropriate to the corporate strategy being pu[illegible] how below:

DOMINANT LOGIC / BUSINESS MODEL
- **Create value by business startups that pursue innovative differentiation in underserved markets with sleepy incumbents, using partners' finance and operational capabilities**

MARKETS / INDUSTRIES THAT CONFORM TO THIS LOGIC
- **Consumer market with a dominant incumbent**
- **Scope for innovative customer service**
- **High entry barriers to other startups**
- **Branson/Virgin image appeals to customers**

KEY RESOURCES:
- **Virgin brand**
- **Branson**
  - **– charisma/image**
  - **– PR skills**
  - **– networking skills**
  - **– entrepreneurial flair**

KEY CAPABILITIES:
- **New business development**
- **Brand management, promotion**
- **Business partnering**

NOTE

DESIGNING THE CORPORATE STRATEGY AND STRUCTURE
- **What's the strategy model? (Entrepreneurial, venture capital, related-diversified corporation?)**
- **Which businesses to divest?**
- **Criteria for future diversification**
- **What type of structure? Need for corporate center to protect brand, monitor performance, transfer managers and knowledge**

NOTE

1. C. K. Prahalad and R. A. Bettis, "The dominant logic: a new linkage between diversity and performance," *Strategic Management Journal*, 7, 1986, pp. 485–501. See also, R. M. Grant, "On dominant logic, relatedness, and the link between diversity and performance," *Strategic Management Journal*, 9, 1988, pp. 639–42.

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