case fifteen
Richard Branson and the Virgin Group of Companies in 2004

Teaching Note

Synopsis

By 2004, 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. In the first 4 years of the new century, Virgin had founded a new airline in Australia; retail ventures in Singapore and Thailand; wireless telecom companies in Asia, the US, and Australia; and a wide variety of online retailing. While several of these new ventures had been very successful (the Australian airline Virgin Blue and Virgin Mobile in particular), the financial health of several other Virgin companies was looking precarious. Several of Branson's startups had been financial disasters – Virgin Cola and Victory Corporation in particular. Other more established members of the Virgin group (such as Virgin Rail and Virgin Atlantic) required substantial investment, while yielding disappointing operating earnings. While Branson's enthusiasm for supporting new business ideas and launching companies that would challenge business orthodoxy and seek new approaches to meeting customer needs seemed to be undiminished, skeptics suggested that the Virgin brand had become overextended and that Branson was losing his golden touch.

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

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management principles upon which the Virgin companies are launched and operated, and the way in which the group is run.

The case also 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 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?

POSITION IN THE COURSE

I use this case to address issues of diversification in the corporate strategy section of the 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 changes in the financial structure, organizational structure, and management systems of the Virgin group would you recommend?

Reading

R. M. Grant, *Contemporary Strategy Analysis* (5th edn), Blackwell Publishing, 2005, chapter 15.

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 antiestablishment 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.

2. *Which businesses 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 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, and possibly financial services.

3. *What criteria apply 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 upon 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 should be made 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 coordination and controlling 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 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.

Summary of Issues

The Virgin case can be approached from a number of angles and used to illustrate a variety of ideas and concepts (entrepreneurship, brand extension, corporate culture, to mention a few). My approach focuses on corporate-level advantage, which has its foundations in the resources and capabilities that can be deployed across businesses. (Ultimately, this raises the key issues of economies of scope and transaction costs, although typically I address these concepts in a more systematic manner after discussing the case.)

To summarize the learning on corporate strategy, I begin with the resource/capability foundation. What are the resources and capabilities that are common to the different Virgin companies? To what extent do these constitute a strategic logic ("dominant logic" in the terminology of Prahalad and Bettis[1]) that provides a rationale for the existence of the Virgin group and defines the key elements of its corporate strategy? What does this strategic logic then imply about the kinds of industries and product markets that Virgin should be engaged in? Finally, can we then be more explicit about defining the corporate strategy in terms of identifying the business model (i.e., the basis upon which the Virgin group is able to generate value), the criteria for diversification and divestment decisions in the future, and the kind of organizational structure, management systems, and management style through which the strategy should be implemented?

UPDATING THE CASE

For current information on the Virgin companies and products, log on to the Virgin web site: www.virgin.com.

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.