



GARY P. PISANO
ELENA CORSI

Virgin Group: Finding New Avenues for Growth

Anyone who lives within their means suffers from a lack of imagination.

— Oscar Wilde

On May 4, 2011, Stephen Murphy was in front of the London offices of Virgin Management, the managing company for the branded private investment group Virgin, which had interests ranging from transportation, financial services, health and leisure, and media and telecom to space travel. Murphy, the Virgin Group's CEO, was waiting for Sir Richard Branson, Virgin's founder, and Peter Norris, the non-executive chairman since 2009. The two were flying in that same morning from Necker, one of the British Virgin Islands, where Branson had had a home since the 1970s, to discuss the group's growth plans.

Branson had started the Virgin Group in the 1970s when, at the age of 20, he and two friends set up a mail-order record business in London that soon expanded into Virgin Megastore, a chain of popular record stores across the United Kingdom. In 1973, Branson moved into the music production business with the release of singer Mike Oldfield's hit album *Tubular Bells*. Other investments followed, and over the course of 40 years Virgin developed, from scratch, six companies worth more than \$1 billion each and broadened the group's focus from record retailing and music production to airlines, health, financial services, mobile communications, and media. In 2005, Branson decided to set up a charitable foundation, Virgin Unite, and to split his time between the foundation and the Virgin Group's management. He thus appointed Murphy as the group's CEO. Although Branson now dedicated around 75% of his time to Virgin Unite and other philanthropic causes, he remained involved in the Virgin Group's strategy and regularly spoke with Murphy and the other CEOs about the Virgin businesses.

With Branson, Murphy had decided in 2005 that Virgin would focus on two additional pillars of growth: health & wellness, and financial services. The execution of this growth strategy was complicated by the constraints imposed by Virgin Group's private ownership model. Murphy felt that as a family-owned group, Virgin had a capital base too limited to fully take advantage of the expansion possibilities available to it, and that the group needed to develop additional ways of funding the growth. But the strength of the brand and the long-term views of the founder also afforded Murphy several advantages. He said, "At the same time, I have a single shareholder, Richard, interested in creating sustainable and long-term businesses, and I am not subject to the short-term earnings pressure of other companies."

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In the past, Virgin had generally financed its expansion by selling equity in its operating companies. In a few cases, it had sold its full holdings, although the companies had usually kept the Virgin brand through an ongoing licensing agreement. With total branded revenues of around £11.5 billion, the group in 2010 was a loose collection of Virgin companies in which Virgin Group Holdings (the overarching holding company) had majority, minority, or no stakes at all.

As Murphy contemplated the group's growth strategy for the next decade, he faced a number of difficult decisions. First, how should he fund new ventures? He could, for example, sell off the group's successful businesses and keep a brand licensing agreement with these companies. But what were the risks of such a strategy? Second, what kind of opportunities should he seek? Virgin had historically acted as a venture capital firm, nurturing new ventures (often conceived by Branson himself) from cradle to maturity. Now, to "move the needle" at the larger entity, he had to change the group's business focus and invest in larger, more established companies. But was Virgin missing opportunities in smaller ventures? In addition, would it always be able to inject the Virgin culture and turn around the companies in which it invested?

Further, was he sure that entering the health and financial services sectors was a good idea for Virgin and its brand? Murphy thought, "We need to be careful. Our investment choices are changing the demographic profile of our customer base. Following the money has an impact. Do we want to get trapped in a demographic that is getting squeezed right now, and where we may lose our name for innovation and challenge?"

Virgin Group's History

In the early 1970s, low prices, friendly staff, and the welcoming environment of Virgin's stores attracted a young public. Nick Fox, director of corporate affairs, remarked, "This ensured that the chain was a great success." Richard Branson and his partners expanded the store chain and used the cash flow from that business to start up the more lucrative music production business with the launch in 1973 of the album *Tubular Bells*.¹ (See **Exhibit 1** for a summary of Virgin's history.) As Virgin Records signed contracts with bands such as the popular but controversial Sex Pistols and discovered new singers like Phil Collins and Peter Dinklage, Branson regularly received invitations to fund start-ups and made several investments in different sectors, such as nightclubs, filmmaking, and luxury resorts.

A key turning point was when Branson invested in the airline business. Branson recalled, "Airlines didn't think twice about quality, they did not care about their staff . . . and the entertainment was non-existent. . . . I felt it was important to bring the Virgin values to a monopolistic industry."² In 1984, after having convinced his senior team about the venture, Branson leased a jumbo jet for a year and created Virgin Atlantic, a London-New York airline that offered "first-class tickets at business-class prices." Virgin Atlantic brought in innovations such as limousine pickup for its first-class passengers and seat-back video entertainment systems for its economy passengers.

By the mid-1980s, Virgin had grown into a group with investments in record retailing, music production, nightclubs, film production, airlines, luxury resorts, and tourism. In 1986, Virgin organized its investments in two funds: an entertainment fund (music retailing, music production, and filmmaking) and another fund with all of the other investments. Virgin listed the entertainment fund on the London Stock Exchange, raising £30 million.³

While Branson actively promoted the brand with extravagant events, the stock price stagnated, remaining below £2 per share, and dropped to £0.90 during the London stock market crash of 1987. Branson commented, “In many ways, 1987, our year of being a public company, was Virgin’s least creative.”⁴ Convinced that the public markets had undervalued the companies and frustrated because the listing had limited his decision-making power, Branson bought back Virgin’s shares at the original price. In 1988, Virgin was again a private company.

At the beginning of the 1990s, the Virgin Group had debts of more than \$400 million, most of which were personally guaranteed by Branson or subject to cross-guarantees within the group.⁵ In addition, Virgin Atlantic had been going through turbulence: it was under attack from its main competitor, British Airways, and had been buffeted by the recession of the late 1980s. To reduce the accumulated debt, stabilize the airline, and finance further investments, Branson first sold shares in a few Virgin Megastores and then, in 1992, sold all of his equity in the very profitable Virgin Records to Thorn EMI for £560 million.

Buoyed by the cash from the sale of Virgin Records, Branson set out to expand the Virgin Group throughout the 1990s by investing in several small new ventures—such as Virgin Cola, Virgin Brides (bridal wear), Virgin Clothing, Virgin Cosmetics, and the new record label V2—to further expand the brand and its reach. Many of these diversifications were ultimately unsuccessful and provided a valuable lesson in identifying investment opportunities that had a strong fit with the Virgin brand’s core values of customer service and innovation, rather than trying to rely on product-based businesses.

First, at the end of the 1990s, Virgin invested further in transportation. In 1996, taking advantage of the liberalization of the British train network and the deregulation of the world’s airline sector, Virgin launched Virgin Express, a low-cost European airline based in Belgium; in 1997, it took over the franchise on Britain’s West Coast Main Line and launched Virgin Trains; and, in 2000, it launched an Australian airline, Virgin Blue.

Second, the Virgin Group invested in consumer service businesses such as financial services and fitness. In 1995, Virgin partnered with an insurance company to create Virgin Direct, a British financial services company offering retirement accounts, insurance, and mutual funds. Unlike a bank, however, Virgin Direct had no branches and served customers only by phone (and later online). In 1998, Virgin backed a start-up team in the health and fitness sector to launch Virgin Active, and then in 2000 it expanded the business with the acquisition of a failed gym chain in South Africa.

Finally, Virgin invested in telecommunications. In 1999, it launched Virgin Mobile, the United Kingdom’s first virtual mobile network operator, which provided mobile phone services without owning the infrastructure and without its own licensed frequency allocation on the radio spectrum. The model was successful, and Virgin expanded by launching two other mobile virtual operators, Virgin Mobile Australia (2000) and Virgin Mobile USA (2001).

By the mid-2000s, the Virgin Group’s portfolio covered nine main sectors: air travel, rail travel, mobile phones, finance, leisure (Virgin Active), retailing, music retailing (Virgin Megastores), drinks, and online retailing. (See **Exhibit 2** for Virgin’s 2004 structure.)

Virgin’s companies differed with regard to their equity structure. Virgin fully owned only a few companies, such as Virgin Money (whose partner the group had recently bought out). The group held majority stakes in some of its companies (e.g., Virgin Atlantic and Virgin Active), but many of the larger companies were joint ventures. While most of Virgin’s companies were private, a few (Victory Corporation, including Virgin Clothing and Virgin Cosmetics, and Virgin Blue) were

publicly listed. In addition, the portfolio was very diverse in operation and growth: some companies were fast growing, whereas others were stable or stagnating and still others were losing money. Among the fast-growing companies were Virgin Atlantic, Virgin's largest business in terms of revenue and profit, and Virgin's three mobile phone companies, which were particularly important for the group because of their wide customer outreach. (See **Exhibit 3** for the key financials of Virgin's main companies.) Although still small in terms of its revenues, Virgin Active was among the group's fastest-growing companies and had become an international gym chain with operations in South Africa, the United Kingdom, and Italy. Virgin Trains had recently started generating profits.⁶ But the Virgin Megastores chain of 122 stores selling records, books, DVDs, electronic equipment, and event tickets was struggling, challenged by the rise of the Internet and in particular of iTunes, which gave Internet users easy access to music downloads. In addition, a few of the group's smaller ventures—such as Virgin Brides, Virgin Drinks (which included Virgin Cola and alcoholic beverage producers Virgin Vodka and Virgin Spirits), and the online retailing companies (e.g., Virgin Cars, launched in 2000, and Virgin Motorbikes, launched in 2002)—were losing money.

Branson – Stepping Back from Day-to-Day Management

In 2005, as Richard Branson started to step away from executive management, he entrusted the day-to-day management of the Virgin Group to a team of managers who had worked with him for several years, headed by Stephen Murphy. As the new CEO, Murphy planned to not only reduce the group's dependency on aviation and telecommunications but also develop two new pillars of growth—health & wellness, and retail financial services—which were perceived to be more countercyclical than the group's other businesses.⁷ On the move into health & wellness, Murphy explained:

We took this decision on the strength of the performance of Virgin Active, our gym network, which was outperforming our expectations. People today care more about their physical appearance and spend more on their health. The driving forces are the aging of the population [and] the increased economic wealth and the fragmentation of society (i.e., the increased number of single people). The logical next step was to expand our gym network but also to become a health care provider. Some European governments were thinking of making consumers co-pay for at least some of the health care services they received. This meant that new markets were going to open up.

Virgin had already operated in the second pillar, retail financial services, but through Virgin Money's subsidiary Virgin One, which was a joint venture with the Royal Bank of Scotland (RBS) and which had pioneered the offset mortgage in the United Kingdom. Gordon McCallum, CEO of Virgin Management, explained:

With Virgin One, we rented the infrastructure and customer base from RBS. We developed such IT flexibility and creativity around the product that RBS bought us out from the joint venture in 2001. After this success, we felt that we had the brand, and with the return of our former CEO Jayne-Anne Gadhia (from RBS) in 2006, we had the management team to plan to become a bank. In banking, the biggest strategic challenge is to understand life from a customer perspective rather than from the product perspective. This is easier for outsiders. Customers feel that they have been ripped off by the banks; we can make a difference.

Branson concurred: "We are going to get back into the mortgage business and we will become a bank either by acquisition or by getting our own banking license."⁸ In most countries, a bank license was a prerequisite to providing banking services (e.g., deposits and mortgages). Another part of

Murphy's plan was to reduce Virgin's dependence on the United Kingdom, where most of its businesses were operating. Murphy said, "We decided to focus more on the United States because it is a large market with a single currency and our brand was already strong there."

From 2005 to 2008, the Virgin Group invested not only in existing businesses (e.g., by expanding its gym network around the world) but also in new growth areas (e.g., with the launch of the low-cost U.S. airline Virgin America, which was considered a key strategic venture to further penetrate the U.S. market). At the same time, the group loosened its relationship with its telecommunication companies as it sold its stakes in its U.S., Australian, and Canadian mobile companies to their mobile partners. In each case, Virgin retained a brand licensing agreement with the companies. As for Virgin Mobile UK, after accepting an offer to merge it with the U.K. cable-television company NTL:Telewest in 2006, Virgin agreed to rebrand it into Virgin Media, although Virgin owned only 14% of NTL:Telewest's shares.⁹ However, the financial crisis of late 2008 froze the Virgin Group's expansion plans. During the crisis, Murphy moved his attention to saving cash for Virgin's largest businesses and in particular, for its aviation investments. He recounted:

The combined losses for the global aviation industry were about £14 billion. It was bad for us as well. All our cabins were full up to December 2008. Then [after] mid-January 2009 our flights emptied. Luckily, many of our other businesses performed very well. To find cash, we sold our loss-making investments such as Virgin Megastores and Virgin Cosmetics. We also had to close several of our U.S. investments, such as our embryonic financial services and gaming businesses. We also looked closely at Virgin America, but we had already invested heavily in this company and could see that we could establish a real different service in the market, and there were strong early signs of success, so we decided to keep it.

In 2009, with the markets recovering, Murphy went back to thinking about expansion. Virgin Money acquired a banking license by buying the private bank Church House Trust Plc for £12.3 million in early 2010. At about the same time, following the U.K. government's decision to open up the British primary health care services to private providers, Virgin acquired a 75.1% share in Assura Medical, a health care partnership between a medical real estate owner and several general practitioners, with more than 3 million patients.¹⁰ McCallum explained, "We did not have brand credentials to enter the business alone. Assura Medical has an interesting business model with the doctors who deliver the service. It is almost a federation of people. The U.K. health care [industry] is a £100 billion business and the market is underserved: we can make a difference here." Richard Burrell, Assura's former CEO, added, "This offers us fresh capital, additional management and operational resources, and the considerable benefit of the Virgin brand."¹¹

In 2010, the Virgin Group also started developing a new business by forming a partnership, Virgin Hotel USA, to buy \$500 million worth of property over three years and develop 25 high-end Virgin hotels. The objective was to expand the company's U.S. presence by taking advantage of the U.S. business and leisure-travel rebound after the 2009 recession. An executive director of the new venture stated, "There are a lot of properties out there that were developed in 2007 that are now opportunities for us."¹²

Virgin's Businesses

By 2011, the Virgin Group had moved away from music recording and retailing, although it still had a licensing agreement for some international Virgin Megastores. Of the 400 companies the press often reported Virgin to have, the group tended to focus on the top 20 or so investments. Some of the

companies—including Virgin Atlantic, Virgin Media, and Virgin Blue (rebranded Virgin Australia in 2011)—were multibillion-dollar businesses.

Most of the Virgin companies were in service-oriented businesses rather than product-based ones and covered the middle to upper end of the market. Since 2007, Stephen Murphy had organized the group's companies into six main business sectors, to which it added a seventh following the launch of Virgin Hotels USA. (See **Exhibit 4** for a list of Virgin's key companies by business.)

Aviation and Tourism

Aviation and tourism, Virgin's largest sector, included Virgin Atlantic (51% owned by Virgin), which was the group's second-largest revenue generator. (See **Exhibit 5** for information on Virgin's airlines.) Based in London, the airline operated long-haul services and was the second-largest operator, in terms of capacity, between the United Kingdom and the United States. Richard Branson was particularly attached to this airline, which he believed radically changed the customer's cabin experience.

Other aviation stakes included the recently rebranded Virgin Blue, now called Virgin Australia (in which the Virgin Group held 26% of shares) and Virgin America (in which Virgin held 25% of shares). Murphy commented, "I am not optimistic about the long-term climate for aviation. Several airlines are consolidating to be able to face the increasing and fluctuating costs. This is a business where fuel is 40% of the income statement: the airlines depend on the fluctuating oil prices. These businesses are too big and cyclical, and our capital base too small, to fund continued expansion on our own."

Tourism included the very successful Virgin Holidays and the Virgin Limited Edition, a network of four luxury resorts, a restaurant, a luxury catamaran, and a small submarine.

Telecom and Media

Telecom and media was the Virgin Group's most important sector in terms of brand outreach, since it included the publicly listed Virgin Media, which offered Internet, television, and mobile and fixed-line telephony to 4.8 million customers based in the United Kingdom. The Virgin Group now held a 4.7% stake in this company.

This sector also included Virgin's international mobile companies, although the Virgin Group retained only a 50% stake in Virgin Mobile France and had sold all of its equity in the other main companies. The largest Virgin Mobile company was the U.S.-based one, with 6 million customers. In 2009, Virgin had sold its 28.3% share in this company to one of its partners, Sprint Nextel, for a total of \$483 million and signed with it a brand licensing agreement that gave Virgin Mobile the use of the brand until 2021 for a royalty of \$12.7 million.¹³

Retail Financial Services

Retail financial services, one of Virgin's future pillars of growth, included Virgin Money, which ran the group's U.K. credit card, savings, and insurance business and had full or partial equity in small operations in Australia and South Africa as well as the British charity fund Virgin Money Giving, which was launched in 2009.

Although Church House Trust Plc did not have branches, by acquiring it Virgin Money had obtained a banking license that would allow it to provide banking services—in particular current

accounts and mortgages—without having to rent the infrastructure from a bank.¹⁴ Gordon McCallum said, “Following the 2010 acquisition, we can now build by ourselves the core customer platform. We would still rent parts of the payment system such as access to the ATM system.” The existing Virgin Money companies provided products such as credit cards and insurance in partnership with banks.

Since April 2010, Virgin Money had had a new partner in the American private equity fund Wilbur L. Ross & Co., to which it had sold a 21% stake for £100 million.¹⁵ Virgin Money planned to build a 70-branch Virgin network over the next five years and was exploring further acquisitions,¹⁶ including that of the government-controlled Northern Rock and branches from Lloyds Bank and RBS, both of which were looking to dispose of assets.

Health & Wellness

Health & wellness, Virgin’s second pillar of future growth, included Virgin Active, Assura Medical, Virgin Health Bank, and the U.S. health incentives provider Virgin Health Miles. Virgin Active, by far the largest Virgin company in this sector in terms of revenue, was an international chain of 194 health clubs.¹⁷ With 13 years of uninterrupted profit and revenue growth, Virgin, which now owned 76% of Virgin Active, had tried to float it in 2007 but abandoned the project because it believed that the markets had undervalued the company.¹⁸ In 2010, the Virgin Group looked again at floating the business but was approached by a number of private equity companies interested in taking a stake.

Assura Medical provided health care services in a joint venture with about 30 National Health Service (NHS) general practitioners (GPs), representing more than 30 GP companies. Although Assura was in the red, with 2009 operating losses of £4.4 million, experts estimated that the GP companies would generate revenues of about £27 million in 2010. Virgin planned to invest between £15 million and £20 million in Assura Medical and was considering whether to rebrand the company.¹⁹ McCallum said, “There is big consumer demand for our brand in health care, but it brings with it a significant risk. I personally think that we should rebrand, but some colleagues say, ‘Let’s not rush.’ It is true that we still do not have the brand credentials to operate in health care, while Assura does.”

U.S. Hotels

U.S. hotels, created in 2011, was a new business sector for Virgin. The U.S. hotels joint venture focused on increasing Virgin’s U.S. presence by developing from scratch a network of about 25 Virgin-branded hotels in main U.S. cities. With 150 to 400 guest rooms each, the hotels would offer special services such as breakfast served at any time of day. Virgin Hotels planned to operate as third-party managers, teaming with owners or directly acquiring properties.

Special Situations

The special situations sector grouped several unconnected investments in companies from Virgin Trains to Virgin Galactic, the latter of which was expected to launch its first commercial spaceflights in 2012 or 2013. In 2010, Virgin Trains, in which Virgin held a 51% stake, reported after-tax profits of £39.9 million. The Virgin Group and its partner shared a £32.5 million dividend. In 2011, Virgin was rebidding for the 15-year franchise, which was to expire in December 2012.²⁰

The Virgin Green Fund

The Virgin Green Fund was a private equity fund launched in 2007 to gather all of Virgin's renewable energy and resource efficiency investments. Virgin had started investing in this sector in 2006, when Branson announced that he would use the earnings of the transport companies to develop green companies.

The Virgin Brand

Senior management considered the Virgin brand to be the group's most important asset. Gaurav Batra, corporate development and strategy director of Virgin Management, said, "The brand is the golden goose for us. It is one of our most valuable investment assets and is also very frequently the reason why we can invest."

An unusual aspect of the brand was the degree to which it could be stretched across a broad range of sectors. Most strong consumer brands were heavily identified with a particular product category or industry (e.g., Nike in sportswear, Coke in beverages). Stephen Murphy explained:

Virgin defies the usual "rules" of brand limits. The brand has been successfully applied to businesses as diverse as music, airlines, trains, financial services, fitness centers, mobile telephony, and the Internet. Some ask me: How can a brand that was all about fun and rock & roll in the 1970s be in banking and health care today? The Virgin brand has some core features that are in all of our companies—we try to do things differently, have fun, innovate, provide value for money, and provide great customer service. Every product we create emphasizes or de-emphasizes certain elements. We do not have to have equal elements in everything that we do. For example, in banking, consumers look mainly for value for money because they think they have been ripped off all along, then customer service, and finally a little bit of fun. They would probably not want too much of innovation: people are conservative when it comes to money. In the media business, customers would mainly want fun and innovation.

Virgin's management believed that the brand had a universal appeal. Murphy said, "Virgin is one of the few products (Apple being the only other one I can think of) where you have a 16-year-old willing to say he has a Virgin product, even if his dad has it. The telephone brand Nokia has lost this, for example." Nevertheless, Virgin's customer base was growing old. Murphy continued, "Our average customer is from 35 to 50 years old and usually not on a minimum wage." At the same time, the company was still strongly associated with the image of its founder.²¹ J.P. Moorhead, investment director at Virgin Management, said, "We are working to make the brand identity less dependent on Richard, although this it is not always easy or possible. If Richard announces a new venture, he tends to capture a lot of attention."

The Virgin brand played an important role in the employee recruitment process. Gaurav Batra said, "In the U.K. we are constantly rated as a very good place to work. We attract great people, because talented entrepreneurial teams want to work with our brand. Also, the people we attract understand what our brand is about and agree with its values. This creates a virtuous circle."

In contrast, the brand's strength sometimes challenged Virgin's new investments. A manager said, "We need to rebrand our new businesses because the brand brings in several new customers and helps us in the recruitment process. At the same time, our new companies might be challenged by their sudden popularity, which could interfere with their efforts to deliver high-quality customer services."

The Group's Structure

The Virgin Group is atypical: it does not have the typical lines of authority of a company. It relies more on soft tissue than hard tissue to make it work.

— Neil Berkett, CEO, Virgin Media UK

The Virgin Group was not a single corporate entity, but rather a loose network of holding and operating companies linked primarily by the Virgin trademark. A few companies, such as most of the Virgin Mobile companies, were linked to the group only by a trade licensing agreement, since Virgin had sold all of its equity. Gordon McCallum recalled, "When in 1999 we sold Virgin Cinemas, we felt it was not that critical to leave them the brand although we had made good financial returns. Anyone can replicate having good popcorn and nice seats. Yet in other cases we trusted that the managing teams will continue building the brand and believed we would benefit from the license."

At the head of the group was Virgin Group Holding, which held the group's shares in the companies, and Virgin Management, which managed the companies. The holding company's board of directors—composed of Stephen Murphy, Peter Norris, the chief financial officer Mark Poole, and the non-executive director Carlo Costamagna—approved all of the group's investment decisions. (See **Exhibit 6** for biographies of the board members.) In this task they were helped by the investment advisory committee, composed of Murphy, Poole, McCallum, the media head Robert Samuelson, the commercial director Patrick McCall, and David Baxby, the head of both Virgin Asia-Pacific and the aviation business. In 2010, Virgin had also set up a new committee of external experts who would advise Norris and the board. (See **Exhibit 7** for a list of the new committee's members.) Richard Branson still worked on overall corporate strategy and remained the president of Virgin Atlantic.

Virgin had a decentralized approach to management. J.P. Moorhead said, "Considering all the markets and businesses where we operate, we prefer to run our companies by empowering their management teams and those on the ground. We are a shareholder who adds value, because we are the owners of the Virgin brand and because we reflect the group's long-time experience in different sectors and business models over time."

Virgin exercised influence over the operating companies mainly by having representatives on their boards. At Virgin Management's offices in London, New York, and Sydney, there were about 30 investment professionals organized across seven sector teams. Many of these professionals sat on the boards of about four or five companies' boards. Murphy said, "These are experienced people who spend a lot of time on each company since they need to build the relationships." In addition to these 30 professionals, the head of strategy would sit on the boards of the new ventures while McCallum, Poole, and Murphy sat on the board of a few strategic companies.

Virgin also tried to control the brand through the licensing agreements. These agreements set the terms and conditions of the use of the brand name and were signed with all of the companies that carried the Virgin name. Virgin's human resources, brand, and marketing teams at the management offices were in regular contact with the operating companies to help them in their day-to-day activities. Norris said, "Increasingly, the Virgin brand is used by companies that we do not control financially. So we have had to take a long look at our brand licensing agreements to provide some provisions about how they can use the brand. If a company does not meet its obligations to the brand, in theory we can take the brand away from them, but this is a nuclear option. It would be extremely costly for everyone."

Virgin had not had many major problems with how operating companies used the brand. McCallum noted, "It is not in the interests of the operating companies to damage the brand. Those who get the use of our brand under our licensing conditions in general understand our brand and know where they want to take it." Neil Berkett, CEO of Virgin Media UK, added, "The real control power of the Virgin group lies in their brand, and not in their presence on the boards or in the brand license agreements. For example, the Virgin brand represents for Virgin Media about 40% of our global revenue footprint and for the Virgin Group a wide customer network. [Neither of us] can afford for the brand to fail and thus we are joined at the hip in a way that it is extraordinarily powerful." For this reason, it was very important for Virgin that the senior managers of its operating companies understood the importance of rejuvenating the business and the brand. Murphy said, "We run an empowered model, but we are also incredibly hands-on investors. We create management teams in the businesses we launch, and spend a lot of time explaining to them the role we would play. We try to make sure that we win their hearts and minds. We are more participative even than a private equity investor. We want to protect our brand and ensure that they do not deviate from it in terms of internal values, and values for the products and consumers."

When launching new companies, Virgin tried to inject five or six people into the new management structure. McCallum explained, "We would usually place people who had worked at Virgin in positions that have to do with the brand, marketing, customer service, and perhaps HR so that they can change the company's DNA. There is not so much mobility between Virgin companies, because in our companies we prefer to have people who know that business."

Even where Virgin did not own a majority, it would negotiate in the licensing agreement the right to at least appoint the CEO. Murphy gave the example of Virgin Media:

NTL:Telewest came to us asking for help. This was a failing and failed organization. Yet we realized that their high-speed fiber-optic infrastructure was an asset. They had a plan and thought our mobile business and brand would fit. We insisted that we should have a share in the new company, but we only got 14%. We sold them Virgin Mobile UK and developed a sophisticated brand license agreement, in which we also wrote that we could pick the CEO and inject a few managers. They accepted because they trusted us. Virgin Media went from being an almost-bankrupt company to one of the most important British operators.

Corporate Strategy at Virgin

In its early years, the Virgin Group defined itself as a branded venture capitalist typically seeking an internal rate of return of 30% or more on investments.²² Gaurav Batra explained, "We are in no small part a reflection of our founder, who is deeply passionate about the Virgin brand, entrepreneurialism, and building valuable businesses." Ideas for new investments came mainly from Richard Branson and from his meetings with friends, entrepreneurs, or colleagues. Gordon McCallum said, "Richard was very opportunistic in his investment decisions. He would wake up one day with a new idea and try to convince us, the investment advisory board, to pursue it. There was a healthy tension between us, with a more traditional approach to business, and him, who was more intuitive and opportunistic." Sometimes Branson overruled his investment advisory board, such as, for example, when he launched Virgin Cola and Virgin Mobile USA despite the negative advice of the board.²³ J.P. Moorhead said, "One of Richard's approaches was to announce an area where he believed there was a potential opportunity for the group. We then often received many interesting proposals from people interested in cooperating in the same area."

Since launching Virgin Atlantic in 1984, Branson had entered many new businesses in partnership with other entrepreneurs or companies to share the capital costs and the risks but also to acquire industry expertise. Yet he usually preferred to have majority stakes in the new ventures and was personally involved in the selection of the senior team. McCallum explained, "He identified people who he thought had the right core skills to develop the business, even if they were new to the industry."

While Branson financed the new ventures mainly by taking on more debt, in the 1990s, the Virgin Group had started raising capital through the sale of its mature companies such as Virgin Records and Virgin Cinema, or by accepting new equity partners in companies like Virgin Atlantic and Virgin Megastore France, or by listing a few of them on the stock market.²⁴ In a few cases, as with Virgin Active, the group sold minority stakes but then bought them back after a few years. This new approach transformed the group's structure. By the mid-2000, the group had become more similar to a private equity company that financed its investments by selling or listing companies.²⁵

At the same time, Virgin's growth approach had become more analytical and strategic. Murphy reasoned, "Richard is brilliant and very instinctive. Yet now consumers and attitudes move so quickly that we have to be more analytical. We need to combine intuition and qualitative analysis with the real quantitative analysis that says, 'This is your demographic and this is your profile, and this is where you go next.'" Murphy and the advisory team would think of the new key growth areas, while the sector teams screened the markets to identify new opportunities in their respective sectors. The head of strategy looked for investments in industries where Virgin was not yet present, such as health care. Gaurav Batra said, "We became much more capital ambitious. We started looking at ourselves as a collection of investment professionals who could grow the businesses, lay the genesis for the next big company, and then sell or float the company." Virgin's equity investment criteria were based on financial returns. Batra continued, "Our criteria were ROI, payback time, project returns, and capital size. And then we had the 'fit with brand' criteria."

The 2007 financial crisis forced Virgin to revise its approach to raising private equity pools of capital. Batra remembered, "The economic environment for raising capital equity changed, and we also started to realize that the private equity model of committing the brand to a group of arm's-length investment managers could be inconsistent with the long-term protection of the brand."

As for new ideas, Virgin still relied on a plurality of sources. J.P. Moorhead explained, "We are relatively agnostic about the sources of new ideas. These can come from Richard, our group management team, our operating companies and their employees, the sector teams, or the large number of proposals we receive from both potential partners and the general public. Ideas can also come from our employees. For example, the idea of the iPad magazine came from a manager in our aviation sector team." Every year Virgin received about 5,000 proposals from potential partners and the general public. Nevertheless, the Virgin Group was doing fewer experiments than in the past, since each investment brought about a risk for the brand, and it carefully selected businesses in which to invest.²⁶ McCallum observed, "In the past, the investments we made that failed, like Cola, failed because we entered a market where there was no consumer dissatisfaction with the incumbents. Today we identify businesses and areas where the market dynamics mean that the consumer is underserved and that there is an opportunity to create value."

Virgin had also devised a new set of equity investment and brand criteria. Murphy explained, "Before investing, we now think: What is the lifetime value of a customer? Can we retain that relationship longer than competition? What is the cost of acquiring a customer? What would be the ideal product price? We would calculate the net present value of what the customer's lifetime value

is and the net margin to us, and invest where we see profits and where we think we can make a difference." Batra added, "In terms of the brand, we ask ourselves: Do we think there is a cultural fit with the management team? Will they sign up to the level of interaction and engagement that we need? Will they keep innovating? What would this partnership bring to the brand?"

Virgin's investments usually focused on service-based businesses. Murphy explained, "The Virgin brand helps us attract new customers. Our marketing costs as a percent of revenues in any business is always less than the competition. This is relevant in particular in the businesses where marketing is a big element of the cost structure, such as in mobile telephony. Instead, in businesses like aviation, where marketing is only about 2% of the costs, or health care, where you are not even allowed to advertise, the advantage is limited."

In addition, Virgin was investing in fewer but larger ventures and was quicker to pull out of an investment when it was not profitable. Batra recounted, "From 1995 to 2000, we launched 34 new companies; today we do about 5 investments per year. Start-ups are time-consuming and do not help in moving the needle and changing the group's focus. To shift the needle we would need to do 100 start-ups per year. Even if we had the capital, we would not have the managerial bandwidth to do this. Yet this also means that we rule out start-ups that 20 years ago we probably would have done, just because they are too small." In order to be able to "move the needle," Virgin was mainly buying existing companies. Murphy said, "Our average life to monetization for a start-up is seven years. This is too long. If you have the right strategy, leadership, and catalytic ingredient (i.e., our brand), you can turn around failing companies." Virgin had positive examples in the past (e.g., its train, media, and gym ventures) but also some failures (e.g., the airline Virgin Express).

Virgin was also cautious when transferring the brand to its new investments. McCallum said:

In the past we were less cautious. When we launched Virgin Mobile UK, we were new to the business. We hired 20 people and asked them to create a marketing front-end product, without touching the infrastructure behind that. We virtualized the telecom model in a way that had never been done before, and did it under the Virgin brand. The only investment we had been cautious about was Virgin Media UK, which we rebranded only after one year, once we felt that they were delivering a base level of service that we were willing to stand behind. Nevertheless, we never had any doubt that we would do that. Today, there are a few senior executives who do not want to rebrand our health business.

It was hard to decide when a company was ready to adopt the brand. Neil Berkett explained:

When Virgin Media UK rebranded, we had hit all the metrics such as if the governance and my authority were in place. Yet the soft tissue was probably not there yet. Were we ready to be Virgin? We are ready today [in] that we have the size and the products to be game-changing, and in a Virgin way. Yet this is a bit like the chicken-and-egg dilemma. If you lean forward and become Virgin, this will probably drag you further. But if you do this too early, you might harm the brand. It is not easy to decide when a company is ready to become Virgin.

To finance its investments, Virgin was less reluctant to sell its companies and lease the brand. Berkett explained the risk of such an approach: "There is a risk in the classic private-equity funding structure that you have to sell to buy. The organization that is being sold might think that Virgin does not believe in them anymore." In addition, it was harder for the Virgin Group to control the brand without the equity. McCallum gave the example of Virgin Mobile USA:²⁷

In 2009, our partner made an interesting offer to acquire our U.S. company. In addition, how can you say “no” to your partner? Yet their culture is very different from ours. In the past they even had a bad reputation with customers. To attract and retain people of the caliber we expected was difficult because they were not our employees anymore. Other companies followed a different approach. For example, Optus, the only owner since 2006 of Virgin Mobile Australia, has set up a completely stand-alone management team of 20 people in a different building. Today we have a good relationship with Virgin Mobile USA, but it is true that we do not call each other very often: there are fewer occasions to be in touch. Our relationship gets weaker every day. We need to be careful, because in 20 years time we might discover that the Virgin brand has changed and that we have lost the magic that we have today.

The Virgin Group was also considering entering new businesses without owning any shares in the chosen companies. McCallum said, “This is one of the ways to continue to get bigger without the capital base. We did a couple of small experiments like Virgin Gaming in Canada, where we gave them the brand and some managerial expertise in exchange for a royalty.” Stephen Murphy concluded:

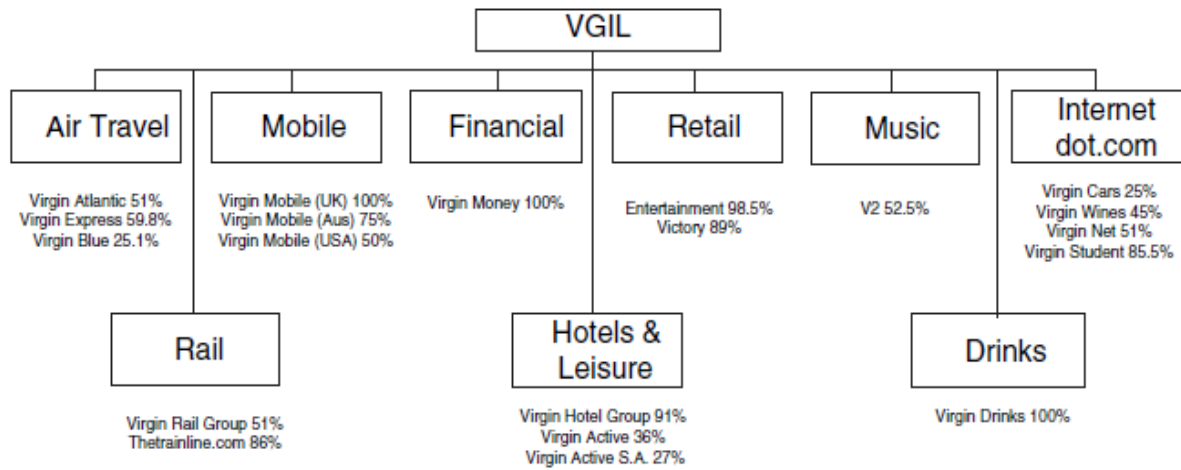
The question we are asking ourselves now is: In the next ten years, would we be better placed to create two \$5 billion or another ten \$1 billion businesses? Which are the businesses we believe are going to be the ones that we should focus on? What are we prioritizing? Personally, I would do far fewer start-ups unless they have a very clear route to scale and market power in a very near time frame, and [would instead] focus on our gym, banking, and health sectors.

Murphy knew that while developing the Virgin Group’s new growth strategy, the group’s managers first and foremost had to decide what kind of company they wanted Virgin to become.

Exhibit 1 Timetable of Virgin's Main Acquisitions and Sales

1970	Virgin is created as a mail-order record company.
1971–	Launch of Virgin's first record shop in London and of Virgin's first Recording Studio .
1972	
1973	Launch of Virgin Records (music recording label).
1979	Acquisition of the homosexual nightclub Heaven in London and of Necker Island .
1980	Virgin Records goes international.
1981	Virgin buys the Kensington Roof Gardens , including a restaurant and private club, launch of British video game publisher Virgin Games ; Necker Island becomes luxury resort.
1983	Launch of Virgin Vision film distributor.
1984	Launch of U.S. airlines Virgin Atlantic Airways and Virgin Cargo .
1985	Launch of the U.S. tour operator Virgin Holidays .
1987	Launch of new TV satellite channel British Satellite Broadcasting , of postproduction facility for commercials and pop videos 525 , and independent producer of music programs Music Box .
1987	Expansion of Virgin Games through acquisition; acquisition of Rushes Postproduction ; launch of Virgin Airship & Balloon , and of Mates condoms to promote condoms to young adults.
1988	Acquisition of British Olympic Studios , launch of record label Virgin Classics and of Virgin Broadcasting ; sale of Virgin's equity in BSB .
1991	Launch of publishing house Virgin Books .
1992	Sale of Virgin Records to Thorn EMI.
1993–	Virgin Radio hits the airwaves with Virgin 1215AM.
1994	Launch of beverage companies Virgin Vodka and Virgin Cola .
1995	Launch of financial company Virgin Direct ; acquisition of Belgian airline and launch of Virgin Express ; launch of music label V2 Music and of U.K. cinema network Virgin Cinemas .
1996	Launch of Internet service provider Virgin.Net , bridal wear company Virgin Brides , and Virgin Trains ; acquisition of majority shares in London Broncos rugby team; floating of Virgin Victory .
1997	Sale of Virgin Radio ; launch of Virgin Cosmetics .
1998	Launch of telecom company Virgin Mobile UK .
1999	Acquisition and launch of gym networks Virgin Active in South Africa, the United Kingdom, and Italy; sale of London Broncos and Virgin Cinemas .
2000	Launch of Australian airline Virgin Blue , energy utility Virgin Energy , Virgin Cars , Virgin Mobile Australia , Virgin Mobile USA , and boutique luxury-hotel chain Virgin Limited Edition ; sale of Rushes Postproduction .
2002	Rebranding of Virgin Direct as Virgin Money ; launch of online motorbike retailer Virgin Bikes .
2003	Launch of Virgin Mobile France ; initial public offering of Virgin Blue ; sale of nightclub Heaven .
2004	Launch of commercial space company Virgin Galactic ; sale of Virgin Cars and Virgin Bikes .
2005	Merger of Virgin Express with Brussels Airlines; Virgin retains minority share
2006	Launch of clean fuel producer Virgin Fuel and of Virgin Active Spain ; sale of Virgin Mobile Australia ; partnership between financial company Virgin Money South Africa and a local bank.
2007	Launch of Virgin Active Portugal , Virgin Health Bank , Virgin Media , airline Virgin America , Virgin Radio Italia , and Virgin Money USA ; purchase of 20% stake in AirAsia X ; sale of Virgin Megastores in the United Kingdom and Ireland; closing of Virgin Digital (Virgin now sells music downloads through Virgin Media's website).
2008–	Launch of Virgin Healthcare and of Virgin Money Giving , sale of 50% stake in Virgin Mobile
2009	Canada and Virgin Mobile USA ; sale of a 32% stake in Virgin Galactic ; sale of Virgin Cosmetics (Virgin Vie at Home since 2006).
2010	Launch of Virgin Racing (Formula One team) and sale of controlling stake; launch of video-game service Virgin Gaming ; launch of film and television development, packaging, and production company Virgin Produced ; launch of iPad magazine Project , a digital magazine for Apple's iPad; dissolution of Virgin Money .
2011	Acquisition of health care provider Assura Medical and of Scottish bank Church House Trust Plc by Virgin Money; launch of submarine manufacturer Virgin Oceans and of hotel chain Virgin Hotels USA .

Source: Company data.

Exhibit 2 Structure of Virgin Group Investment Ltd. (VGIL), 2004

Notes: Virgin Entertainment included all the Virgin Megastores and the few Virgin Cinemas that the group had not sold yet; Virgin Victory included Virgin Clothing and Cosmetics; Virgin Net was both an Internet service provider and a portal offering a variety of content and retailing opportunities in different sectors (e.g., sale of cars and motorbikes); "Virgin Hotel Group" stands for Virgin Limited, the group of luxury resorts owned by Virgin Group; "Rail" stands for trains; Virgin Brides was part of retail.

Source: Robert M. Grant, ed., "Richard Branson and the Virgin Group of Companies in 2004," Case Study 15, in *Contemporary Strategy Analysis* (Oxford: Blackwell Publishing, 2005), pp. 308–334, <http://www.blackwellpublishing.com/grant/docs/15Virgin.pdf>.

Exhibit 3 Key Information on the Virgin Group's Most Important Companies (1999 and 2000 data)

Company	Revenue (\$ million)	Profit (Loss) (\$ million)	Ownership (%)
Virgin Atlantic	2,042	25	51
Virgin Mobile UK	480	8	50
Virgin Rail	442	12	51
Virgin Express Holdings	185	(21)	58
Victory Corporation	92	(13)	85
Virgin Travel*	2,028	73	51
Virgin Entertainment Group*	67	(21)	100
Virgin Money*	872	(62)	100
V2 Records*	72	(65)	66
Virgin Hotels*	38	(0.7)	100
Virgin Trading**	100	(6)	100
Virgin Bride**	30	(0.4)	100
Virgin Net**	20	(7)	51

Source: Adapted from Robert M. Grant, ed., "Richard Branson and the Virgin Group of Companies in 2004," Case Study 15, in *Contemporary Strategy Analysis* (Oxford: Blackwell Publishing, 2005), pp. 308–334, <http://www.blackwellpublishing.com/grant/docs/15Virgin.pdf>.

Note: Virgin Trading stands for Virgin Drinks; Virgin Rail for Virgin Trains.

* 2000 data.

** 1999 data.

Exhibit 4 The Virgin Group's Most Relevant Companies by Sector, 2010 (in £ millions unless otherwise stated)

Business	Company	2010 Revenues	2010 EBITDA	Equity (in %)
Aviation & Tourism	Virgin Atlantic	2,357	-56	51
	Virgin Australia*	1,873	185	26
	Virgin America **	469	-1	25
	Virgin Limited Editions	n.a.	n.a.	100
Telephone & Media	Virgin Media UK	3,876	1,457	4.7
	Virgin Mobile USA,	n.a.	n.a.	0
	Virgin Mobile Canada	n.a.	n.a.	0
	Virgin Mobile Australia	n.a.	n.a.	0
	Virgin Mobile France	233	-19.3	n.a.
	Virgin Mobile South Africa	n.a.	n.a.	55
	Virgin Radio (licensing contracts)	n.a.	n.a.	0
	Virgin Produced	n.a.	n.a.	n.a.
Retail Financial Services	Virgin Money UK	91	38	79
	Virgin Money Australia	2	-3	100
	Virgin Money South Africa	ZAR4	ZAR-	n.a.
			7	
	Virgin Money Giving (charity fundraising)	n.a.	n.a.	100
Health & Wellness		n.a.	n.a.	n.a.
	Virgin Active (UK, Australia, Italy, Spain, Portugal, South Africa)	445	115	76
	Assura Medical	n.a.	n.a.	75.1
U.S. Hotels		n.a.	n.a.	n.a.
	Virgin Hotels USA	n.a.	n.a.	n.a.
		n.a.	n.a.	n.a.
Special Situations	Virgin Galactic	n.a.	n.a.	67
	Virgin Oceans	n.a.	n.a.	n.a.
	Virgin Trains	721	70	51
	Virgin Racing	n.a.	n.a.	n.a.
Green Fund	Renewable energy companies Gevo, Odorsun, and Solyndra			
	Energy Efficiency companies Metro Light, Wildcat, and Green Road			
	Resource management companies Durathum, Quench and Seven Keys			

Source: Compiled by casewriters from company data and company's websites.

Note: Virgin Atlantic includes Virgin Holidays.

*Original figures in AU\$ converted using the average 2010 exchange rate of 0.6281 for AU\$ to £ (oanda.com).

**Original figures in US\$ converted using the 2010 average exchange rate of 0.6473 for US\$ to £ (oanda.com).

Exhibit 5 Virgin's Airlines, 2010 (in £ millions)

	Revenues (in £ m)	EBITDA in £m/(Loss)	Destinations	Fleet
Atlantic	2,357	(56)	35	39
America*	469	(1)	15	40
Australia**	1,873	185	31	85

Source: Company data and respective companies' websites.

*Original figures in US\$ converted using the 2010 average exchange rate of 0.6473 for US\$ to £ (oanda.com).

**Original figures in AU\$ converted using the average 2010 exchange rate of 0.6281 for AU\$ to £ (oanda.com).

Exhibit 6 Virgin Group: The Board, 2011

Stephen Murphy (CEO, age 55)	Murphy started his career in finance. He held senior positions at Ford Motors (September 1977 to February 1978), Unilever (March 1978 to September 1982), Mars Group (September 1982 to February 1986), Burton Group (March 1986 to September 1991), and Quaker Oats Company (December 1991 to April 1994). He joined Virgin in 1994 as group finance director of Virgin Management Limited. From May 2000 to November 2001, he left the Virgin Group to be chairman and chief executive of IP Powerhouse Limited, a provider of Internet services to large telecom companies. He returned to Virgin in November 2001 as executive director of transportation, supervising all of Virgin's investments in this sector. Appointed CEO of Virgin Management Limited in July 2004, he became the group's CEO in 2005. Murphy is a director of Virgin Atlantic Limited and Virgin Blue Airlines Pty. Ltd., and a co-chairman of Virgin Trains Group Holdings Limited. He holds directorships at a number of other companies within Virgin. Murphy earned a BA with honors in economics and accounting from Liverpool University (1977) and qualified as a chartered management accountant in September 1981.
Peter Norris (Chairman, age 56)	Norris began his career at Barings in 1976. In 1984, he joined Goldman Sachs, returning to Barings in 1987 to head corporate finance in Southeast Asia. In 1994, he became CEO of Barings Investment Banking Group, charged with integrating the securities and corporate finance divisions. In 1995, he established a corporate finance consultancy, P&T Norris, constructed around the needs of a group of owner-entrepreneurs, which became the core business of New Boathouse Capital, which he co-founded in 2000. He became CEO of Quayle Munro Holdings on its acquisition of New Boathouse Capital in 2007. Norris began an advisory role to Richard Branson and the Virgin Group in 1996. In 2002, he became chairman of Virgin Active, and in late 2009 he took on the role as chairman of Virgin Group. Norris graduated from Oxford University in 1976 with a first-class degree in modern history and modern languages.
Mark Poole (CFO, age 48)	Poole joined the Virgin Group in 1991. He had served as a corporate tax consultant to the Virgin Group since 1990 and as its group tax director. In 2000, he became the Virgin Group's chief financial officer, and in September 2005 he became the deputy group chief executive officer. Poole has been non-executive director of Virgin Express Holdings since July 27, 2000, and director of Virgin Mobile USA since June 2007. Poole serves as a non-executive director of the Virgin Group, including Virgin Group Holdings Limited (group holding company), Virgin Atlantic Limited, SN Airholdings and Virgin Retail Limited, Virgin Hotels Group Limited, and Virgin Active Group Limited, among numerous other companies. He serves as a director of Corvina Holdings Limited. He is a chartered accountant and has been a member of the Institute of Chartered Accountants in England and Wales since 1989, following five years with BDO Binder Hamlyn. Poole graduated from Bristol University in 1983 with a bachelor of science in civil engineering.
Claudio Costamagna (age 54)	Costamagna has been a director at the Italian eyewear company Luxottica since 2006 and is a member of the board of directors of several companies. He has held important offices in Montedison, Citigroup, and Goldman Sachs, where he served for many years as chairman of the Investment Banking division for Europe, the Middle East, and Africa. He is currently chairman of a financial advisory boutique he founded. He holds a business administration degree from Bocconi University, Italy.

Source: Compiled from company data.

Exhibit 7 Virgin Group's New Advisory Committee

Name	Former Position
Claudio Costamagna (chairman)	Former head of Goldman Sachs's investment banking business in Europe
Bill Morrow	Former U.S. utility boss
Baroness Morgan	Former British government minister
Todd Stitzer	Former CEO of Cadbury
Richard Sykes	Former CEO and chairman of Glaxo Wellcome, a medicine wholesaler

Source: Company data.

Endnotes

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