Virgin Finance: Sir Richard Brandson's pursuit of a significant presence in retail financial services

Batiz-Lazo, Bernardo and Kase, Kimio

Bangor Business School, IESE Business School

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Virgin Finance: Sir Richard Brandson's pursuit of a significant presence in retail financial services[1]

Bernardo Bátiz-Lazo
Bangor Business School (Bangor University, UK)

Kimio Kase
IESE Business School (Universidad de Navarra, Spain)

Abstract

This teaching case study tells of the foundation and growth of the Virgin Group over the forty years to 2010. The creation of over 300 business interests in parts as far afield as the UK, South Africa, Australia and the USA resulted from a unique management style. Branson and the Virgin brand often associate with music (such as records and music stores) and travel (airlines, trains and booked holidays) but between August 2007 and February 2008 they were involved in a failed takeover of Northern Rock, a collapsed British bank. However, as this case study details, the Northern Rock affair was one of a long series of steps dating to the 1980s through which Branson and Virgin have been developing capabilities to enter the British retail banking sector.

Introduction

In the forty years to 2010, Virgin Group's Sir Richard Branson (b. 1950) turned from a "high school dropout" to a billionaire and global legend. The creation of over 300 business interests in parts as far afield as the UK, South Africa, Australia and the USA resulted from a unique management style. One he described as "creative", "fun" and ultimately, for him business is:

> "...like painting. You start with a blank canvas. You can paint anything – anything - and there, right there, is your first problem. For every good painting you might turn out, there are a zillion bad paintings just aching to drip off your brush." (Branson 2008, 3).

His style has been affixed labels such as mercurial, maverick and many other positive and not so positive qualifiers . But the fact remains that Branson is the "role model" for many actual and would be entrepreneurs across the globe.

[1] This case was prepared using published source material. It is intended for class discussion rather than as an illustration of either good or bad management practice. A revised version of this teaching case was circulated as SM-1559-E (which includes a teaching note).

Branson and the Virgin brand often associate with music (such as records and music stores) and travel (airlines, trains and booked holidays) but between September 2007 and February 2008 they were involved in a failed takeover of Northern Rock, a collapsed British bank.

As this case study will detail, Virgin Group was keen on entering the finance industry. The Northern Rock affair was one of a long series of steps dating to the mid 1990s through which Branson and Virgin have been developing capabilities and brand awareness to create a significant presence in retail finance. By the end of 2009, Virgin Money provided services such as credit cards, savings and mortgages, as part of a partnership or joint venture with other organisations such as Bank of America and the Royal Bank of Scotland (RBS).[2] A further step was taken in January 2010, with the purchase of Church House Trust, a small regional bank based in Somerset (south east England), for £12.3m while expecting to invest £37.3m into the business.

"The Church House Trust business offers us a strong platform for growth," stressed Sir Richard at the time. At the same time, Jayne-Anne Gadhia, chief executive of Virgin Money, stated that her company would now be in a position to provide consumers with a different type of banking experience: "The financial crisis has tarnished the reputation of many UK banks," she said. Virgin was clearly in a relentless move to expand its repertoire of products and customers while building upon the "core values of quality and fun".

Overstretching of the brand, opacity of the control system, heterodoxy in management, etc., were some of the words used to describe Richard Branson's management style and his straggling business empire.

In order to open discussion on these doubts felt by financial analysts and management researchers the case will first describe the historical development of what is now Virgin Group and then some part of Sir Richard's business philosophy and management style.

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[2] Unless otherwise stated, the reminder of this section borrows freely from "Virgin Money deal paves way for own High Street bank", BBC News, http://news.bbc.co.uk/1/hi/business/8447560.stm (Accessed January 8, 2010).

Baby steps: the making of Sir Richard as an entrepreneur

The genesis of Richard Branson as a business leader is perhaps one of the most often contested areas of the distinctive treats of his entrepreneurial style. The official version of events (Branson 1999; Branson 2008) has found both supporters (Grant 2005a; Dick 2007) and detractors (Jackson 1998; Armstrong 2005; Bower 2008). Differences in interpretation have led to some lengthy (and costly) legal action. Our general approach to avoid dispute here is to start with Branson's autobiography and then present alternative readings using clearly identified sources. For instance, we rely on Bower (Bower 2008) only for direct quotations from the people he interviewed. As to Sir Richard Branson's management thought see Annex 1 - Virgin Group's management statement.

The first steps that led to the creation of over 300+ business empire date back to the late 1960s when he was still at Stowe, a recognised boarding school. He was "a 16-year [old] student who needed to borrow £4 off [his] mother to launch [his] first business venture" (Branson 2003, 1). Together with school friend Johnny Gems, Branson set up a magazine called Student. First published in 1968, it was aimed at Sixth Formers (i.e. seniors at high-school) and undergraduates, that is, to the 16 to 25 year olds. Branson dropped out of school about a year after founding the magazine (for reasons that remain contested, see Bower 2008, 12-16).

The magazine's eclectic style reflected its founder's ability to commission articles by celebrities and to identify subjects not touched by many well established magazines (Grant 2005a, 310). Norman Mailer, Vanessa Redgrave, and Jean-Paul Sartre contributed pieces which appeared among articles on sex, rock music, interviews with terrorists, and proposals for educational reform.

Through the magazine itself never made money and ultimately foundered, the loosely-defined group which gathered around it proved to be a crucial resource in Branson's take-off into entrepreneurship. The magazine's staff was made out of a closely organised cooperative group of friends, acquaintances and hangers-on which were recruited to help with production, distribution and in several occasions, fend off creditors. The group that built around Student served as the nucleus and prototype of a workforce willing to work for low wages in exchange for a lifestyle centre on sexual freedom, drugs and music (Armstrong

2005). It was the culture of this group which generated the ideas for new business on which Branson was able to capitalise (idem).

But Student's circulation remained low and static. In an attempt to boost sales, he tried to tap into the potential he saw in the sale of records. The idea to form the mail-order record business that would become Virgin Records, came from John Varnom and Tony Mellor, Branson's business partners, not Branson himself (Bower 2008, 1 and 9). Initially they sought to distribute through Student an unedited single song by John Lennon. The song never materialised and Student went out of business soon after, but in the last edition and to test the market, an ad was printed listing only records likely to appeal to young people and offering discounts of up to 15 per cent on store prices. The price difference was enough for a large number of orders and their payment to start coming in, since records were still "overpriced" despite the formal abolition of regulation that allowed manufacturers and suppliers in certain industries to "recommend" prices to retailers.

In thinking of a name for the new venture, Varnom came up with "Virgin" as a combination of sex and subversion (Bower 2008, 2), reflecting values typical of the youth culture of the time, in which authority was challenged, fashion changed rapidly and rock stars were idolised. The name appealed to everyone else and was adopted. But lacking capital for a retail outlet, Virgin Records started trading as a mail order supplier of pop records in April 1970.

To the dismay of everyone at Virgin, strike action by British postal workers over their pay started in January 1971. Although it proved short-lived and only lasted a couple of months[3], it clearly threatened the viability of the new venture. Undeterred, Branson immediately rented retail space while transferring the stock of records to small store in Notting Hill (central London).[4] Virgin Retail was thus born. True to the emergent management style, the

[3]The strike end in March 1971 when 200,000 postal men and women voted in favour of a new pay deal (see http://news.bbc.co.uk/onthisday/hi/dates/stories/march/8/newsid_2516000/2516343.stm, accessed April 30, 2010).

[4] Virgin Records were sold to Thorn EMI in 1992 for £560m. This was used to help finance Virgin Atlantic, the airline established in 1984. In 1999, when Branson sold a 49 percent stake of the airline to Singapore Airlines to relieve a financial squeeze, he valued the business at £1.2bn (Bower 2005).

shop's decor was a mix of outrageous and shabby, attracting customers just interested in enjoying the experience and in spending money (Dick 2007, 3).

At the time, records were manufactured close to the recording studios and there were a large number of tariffs and quotas to international trade. As the mail order business started to attract foreign orders, Branson and colleagues woke up to the possibility of buying records wholesale for export (tax free), drive them to France and re-sold them in London while pocketing unpaid duties (33 percent purchase tax on sales)(Bower 2008, 3). Its seems that early on, the records never actually left London while Branson and company were eventually found out by the H. M. Inland Revenue and Customs (i.e. the tax authority). Branson was released from jail after his parents put their own home as collateral for a £30,000 bail. Formal charges were dropped in return for an out of court financial settlement.

The venture, however, had generated enough cashflow to finance the purchase for £30,000 of a seventeenth-century manor in Shipton in March 1971, a town located about five miles from Oxford (Bower 2008, 24). A room within it was fitted with a recording studio in which by 1973 they had developed a polish composition of Tubular Bells by a then unknown author named Mike Oldfield. It was Simon Drapper's rapport with "alternative" tastes in music which enabled him to pick up the potential of Oldfield's composition (Branson 1999, 105; Bower 2008, 29). But it was Branson's persuasive style that managed to convince several DJs to play the record and these included the very influential John Peel of the BBC's Radio One, who devoted a whole program to the record. Tubular Bells was a hit and rose to be the most selling album of 1973. Atlantic Records bought the US rights and re-sold the music as track record for The Exorcist, a Hollywood blockbuster.[5] The result was that at twenty three, Branson was a millionaire.

Success in the record business (notably with the signing of punk rock group the Sex Pistols in 1976) was accompanied with the expansion of the record shops and the creation of a host

[5] Directed by William Friedkin and adapted from the 1971 novel of the same name by William Peter Blatty. The story tells of the demonic possession of a young girl and her mother's desperate attempts to win back. Released in December 1973, the film became one of the most profitable horror films of all time, grossing $440,000,000 worldwide (equivalent to $810m in 2010 after adjusting for inflation; see further http://www.boxofficemojo.com/movies/?id=exorcist.htm, accessed April 28, 2010). It won two Academy Awards (i.e. Oscars), one of them for Best Sound.

of new successful and unsuccessful ventures such as Virgin Rags, a national cloths chains, a sandwich delivery service, a health-food mega store, Virgin pubs and the sale of a hi-fi systems outlet (Bower 2008, 33-4). This rationale of unbridle diversification was quite simple:

> "… I can be quite persuasive in getting people to accept my point of view. I never do this lightly – but, as I've said, usually go with my gut instinct, disregarding volumes of painstaking research. I would love to be able to tell you that every ace I've played has turned out to be a Virgin Blue or Virgin Mobile. But I can't – which is why I make my senior colleagues at Virgin very, very nervous!" (Branson 2008, 9).

In 1984, age 34, the business empire of the "hippie millionaire" was estimated at £150m (Fishlock 1984, 10). That same year, Sir Richard started an airline with a single, old Boeing 747 purchased from Aereolíneas Argentinas. Thatcher governments' market oriented reforms and the apparent success of US-based Peoples Express[6], what was to become Virgin Atlantic began with a phone call from Randolph Fields, a Californian lawyer, who proposed founding a transatlantic, cut-price airline. To the horror of executives at Virgin Records, Branson joined the drive for cheap-fare air travel to show "... how much better they can satisfy consumers by growing at breathtaking speed." (Branson 1985, 14). Unlike Branson's other activities, not only was the airline business highly capital intensive, it also required a completely new set of business skills, in particular the need to negotiate with governments, regulatory bodies, banks, and aircraft manufacturers (Grant 2005a, 311).

But as his group and his profits grew the stage of going for public funding through a stock market flotation in the London Stock Exchange rapidly approached. This was "regrettable", he said, as "it's one thing to worry about staff and yourself, another to worry about shareholders" (Fishlock 1984, 10). By 1985, it was evident that Branson drive for expansion toppled with a transatlantic airfares price war and the investment needs of Virgin Atlantic had created a cash squeeze for Virgin (Grant 2005a, 312). Flotation came November 13, 1986. In this move Virgin's music, retail, and media businesses were combined into the

[6] No-frills air travel took off in 1966 with the establishment of Laker Airways by British entrepreneur Freddie Laker. This venture went bankrupt in 1982 but received much attention during the 1970s. Others companies entered the field inspired by Laker. This included Branson (who eventually invited Laker to the board of Virgin Atlantic) and People Express, which between 1981 and 1987 continued with Lakeraker. This venture went bankrupt in 1982 b

Virgin Group plc, a public corporation with 35 percent of its equity listed in London.[7] Virgin favoured the small investor in deciding share allocations after its offer for sale, which was three times oversubscribed at the 140p per share price (Milner 1986). The price valued the group at £242m and although it compared favourably with the minimum tender price of 120p, it was a little lower than the City[8] had been expecting with many estimates being pitched at around the 150p mark (Milner 1986).

But under the influence of Branson, Virgin was unable to keep up within the rigour and disciplined of a company quoted in a major international stock market. A year later the shares had not had a good ride at 115p per share. There had been notable defections from the board, including the surprised departure of Sir Phil Harris, chairman of Harris Queensway[9]. It was widely believed that Harris was not happy with some aspects of the management of Virgin, at the same time that stock market sources speculated that Cob Stenham, the highly respected head of Bankers Trust's European operations, was also considering resigning his non-executive directorship (Jay 1987).

True to his disinclination to a corseted and rigid management discipline, Branson's dislike of "the onerous demands" from the City was undisguised (Grant 2005a, 312; Bower 2008, 82). Sir Richard grumbled,

> "My dream of taking over EMI Music came to an end there and then. The City of London has misunderstood our business – we would now go off and become one of the largest groups of private companies in the world with several quoted investments to boot."(Branson 2008, 190).

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[7] Following the purchase Euro Belgian Airlines by Virgin Travel in 1996, a second flotation took place in 1997 for the benefit of Virgin Express, as the airline was renamed. Stock was quoted in Brussells, London and the electronic, US-based NASDAQ. See further Dick (Dick 2007, 17).

[8] The City is the historical core within central London from where financial activities grew. It houses the regulators (Bank of England and Financial Services Authority) as well as headquarters and offices of many international banks, Lloyds insurance market and related services (such as accounting, legal, etc.). The concentration of financial activities in the area also known as "the square mile" date to the eighteenth century.

[9] Queensway was was a UK retailer specialised in the sale of carpets and furniture. Established in 1967 by Anthony Parish in Norwich, it was a pioneer of out of town shopping and one of the first retailers in the UK to sell directly to customers from a warehouse. After a boardroom coup the company was sold to Phillip Harris in 1977 and it became Harris Queensway plc. Valued at £450m in 1988, the company was sold to become Lowndes Queensway which then went bankrupt in 1993 due to the recession. See further http://www.gerryparish.co.uk/life_story.php (accessed May 1, 2010).

meaning that stock market analysts failed to see his vision and recognise the potential of his plans. There were clear signs that the market undervalued his company. A conflict thus existed between the financial community's expectations of the chairman of a public corporation and Branson's "laid back" personal style. Within a year of the October 1987 stock market crash, in 1988 Branson raised £248m (£182m in debt) to buy out the Virgin Group's 40,000 small external shareholders. The deal was struck at 140p a share - the same price at which Virgin came to the market two years before. But it ensured that none of Virgin's shareholders - which included the company's staff and pop stars such as Peter Gabriel and Phil Collins - would lose on their original investment (John 1988).

At the time, Branson stated that his decision was "not meant to be a snub to the City" and had been taken purely for business reasons (John 1988). He revealed that they had been planning a further issue of £50m but since Virgin's profits had not matched City expectations and he did not anticipate any dramatic improvement in either its results or the stock market, there were no incentives which might make him stay public (idem). Branson then ended up owning 80 percent of the revamped Virgin. As a private group of companies once again, the Virgin Group continued to expand both its range of business and the geographies where they were active.

The Virgin Empire: Developing checks and balances

There are claims that early on in the development of Branson as an entrepreneur, there was a realisation that his organisation (then still seen as a cooperative venture of like-minded friends and acquaintances) required proper control and systems. It is for this reason that he turns to "... Nik Powell, to help him manage [the buying and selling of music records in bulk], offering in return 40 percent stake in the company. Methodical where Branson was erratic, cautious where Branson tended to overextended himself, Nik Powell was the ideal counterbalance of the fledging business" (Dick 2007, 2). This claim is inconsistent with Branson's own recollection, which places Powell as part of the community around Student in 1968 and then being ousted when a "secret" memorandum from Powell to others in 1970 proposes to relieve Branson of his position as editor and publisher (Branson 1999, 75-5; Armstrong 2005).

The accuracy of the incident around Powell aside, it is clear that Richard Branson increasingly required attracting and retaining talent and skills to help run an increasingly diversified and transnational operation. It is worth nothing here that the Virgin Group is not a single corporate entity.[10] The Virgin empire comprises several holding companies and over 300 stand alone operating businesses which are wholly or majority owned by Sir Richard and those in which he held a minority equity stake. The equity owned by Branson, both individually and through a series of family trusts, is held by Virgin Group Investments Ltd. (Grant 2005a, 314). The linkages between the companies include: the common use of the Virgin trademark, Branson's role as shareholder (both directly and indirectly through the trusts), Branson's role as chairman of the companies (board meetings of which by no means attends regularly, seeDick 2007, 8), and Branson's management role, which is primarily in publicity, public and government relations, and appointing senior executives. Table 1 summarises a selected number of the Virgin group of companies, including some major operating enterprises.

[Insert Table 1 around here]

The summary in Table 1 above is not a fully comprehensive listing. This would be nearly impossible given the private nature of most of the Virgin companies. Limited and fragmented public information as well as different financial years for those companies which do offer some details also hamper external efforts to estimate consolidated financial statements. However, there is an overall impression that the financial performance of the Virgin companies as a whole was poor during the 1990s and more recent evidence suggests this was still the case for many individual companies in the 2000s (Bower 2005; Grant 2005a, 312).

As can be adverted from Table 1, most of these businesses have operations within Britain, Australia, South Africa and the USA. The priorities for this group are "transport and tourism, communications and media, financial services, entertainment and music, health and well being, and renewable energy and the environment."(Branson 2008, 82). Consistency on delivery of the brand is seen as key to Virgin's success (Branson 2008, 6). Sir Richard's

[10] Unless otherwise stated the reminder of this paragraph borrows freely from Grant (2004: 314).

business model is based on, firstly, the concept of "developing discrete businesses with their own investors" whenever these businesses "should fulfil or have the potential to fulfil both the emerging public perception of the Virgin brand and provide the shareholders with a good return on their equity investment" (Grant 2005b). Secondly, convergence marketing. This is predicated on the concurrent convergence of e-commerce and mobile telephony technologies and it aims to bundle Virgin's businesses into a one-stop consumer operation – "UK consumers…use their mobile phone to bank, buy or book virtually any service…Travel…financial services and content businesses will be…beneficiaries." (Grant 2005b).

But the entrepreneurial spirit that enabled Sir Richard to build an estimated £4 billion personal fortune, one of the most recognised brands in the world and which took pride on its "win some, lose some" attitude, took a new direction in 2007 {Robertson, 2007 #27}. That year Sir Richard handed day-to-day control of the group to an investment committee of accountants, lawyers and consultants whose aim is to improve the win-loss ratio. Sir Richard adopted the title of "founder" and would continue to promote the brand and develop business ventures for the group, but he effectively gave up executive control (idem).

Virgin calls its pioneering concept "branded venture capitalism" {Robertson, 2007 #27}, that is, as a large private equity concern which not only invests but has a "hands on" approach and shares a common brand and values (Branson 2008, 82-6).[11] The "new" Virgin aspires to operate as a professional manager of assets and sees itself as a consumer-focused private equity group with the financial discipline of a big City or Wall Street firm. The seven-strong investment committee is led by Stephen Murphy, an accountant, who joined the Virgin group in 1993. Gordon McCallum is Virgin's strategy director and the man responsible for developing new ventures.

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[11] In the US, venture capital is taken to mean a very particular form of finance in which specialised financial intermediaries invest in the equity of high risk opportunities typical of the computer and biotechnology sectors. Firms such as Microsoft, Apple, Starbucks and Celegene benefited from venture capital finance at a crucial point in their development. Venture capitalists invest where banks find it difficult to lend because of a lack of track record toppled by the need to be prompt to market (or a competitor's idea will have first mover advantage). Some take an active role in helping manage the company while others adopt a more "hands off" approach and step in only when called (say to help negotiate terms with banks) or when things are going bad. Venture capitalists often exit the firm through floatation in the stock market or by helping to sell the firm to a larger company in the same sector. In Britain, the term is used more loosely to encompass all forms of private equity investment.

In their first media interview, Murphy and McCallum explained Virgin's new direction {Robertson, 2007 #27}. Mr McCallum said: "A brand of our size can take the hits if a business fails because we are famous for being entrepreneurial. But if we keep getting it wrong, we undermine the whole thing, so we think pretty carefully about what we do." (idem). Murphy added: "Because of the publicity that Richard generates, the cost of failure probably is higher, and that is one of the questions we ask before we start." (idem)

This idea of "branded venture capitalism" is reinforced by the flurry of hundreds of business ideas that are pitched to Branson every month (Branson 2008, 6-9). Many come directly through Virgin's website while others internally, through managers and employees. These are then recorded, catalogued and some of them, researched a bit further. A "tiny number" of them are passed on to investment professionals (working in London, Switzerland, New York, Shanghai and Sydney). The most promising ones are invited for a face to face presentation at one of the weekly meetings of Virgin's Investment Advisory Committee. None of the committee members has day to day responsibilities for running a company of the group but they do work closely with top people (as a type of internal management consultants). The meetings usually take place in London, New York and Geneva (but sometimes in Japan or China). The meetings can also be populated by up to six managers with direct responsibilities in companies within the Virgin group and related to the project being presented with the aim of helping to evaluate the proposal.

As is the case for any other venture capital firm, it takes several meetings before a final decision is made. There is a need to review spending plans, marketing budgets, income forecasts, procurement (including identifying potential joint ventures) and exit strategy for Virgin (that is flotation or sale). But more important, Branson is rarely in attendance to the meetings. On the one hand, "the team don't like [his] interruptions and interference" and on the other hand, if Branson likes "your idea, but the investment committee have concerns, then [he] usually asks them to go find solutions to the problem they've have identified." (Branson 2008, 9). Indeed, according to Sir Richard, it was the result of his "persuasion" and constant prodding that are fuelled by his "gut instinct" and disregard of "whole volumes of painstaking research" that Virgin went into mobile phones and the Australian a low-cost airline (Virgin Blue) (Branson 2008, 9).

Virgin Money: Diversification into retail financial services

Virgin Freeway: From air miles to credit cards

There is another strand to the intermediation activities of Virgin and these refer to the entry into the provision of retail financial services. Virgin's move to this sector "astonished many, and still raises incredulous eyebrows among some politicians and heads of industry." (Branson 2008, 159).

Speculation of Branson's ambitious drive into branded consumer goods and services expanding into retail finance came first about in October 1994, after Virgin signed a tie-up with American Express through its frequent flyer programme, Virgin Freeway. As many other airlines across the world, Virgin was expanding its Freeway programme to embrace other airlines (namely British Midland, Scandinavian Airlines and Air New Zealand), plus filling stations and Holiday Inns. American Express' Membership Miles (launched in November 1993 by the charge card group), gave customers one point for every £1 they charged on their cards whether they were paying for an airline ticket or a restaurant bill. By linking American Express, Virgin was promised access to its "select group of cardholders" at the same time that cardholders booking with their American Express cards could earn double points, one lot from the card company and another from the airline or hotel booking (Webster 1993).[12]

Entering the credit card business was seen as the next logical step if the group's brand diversification into products such as vodka, cola and computers continued to generate the revenues Branson anticipated. At the time, a Virgin spokesman said: "It is a project that we have looked at and continue to look at but we haven't pushed the button yet." (Harrison 1994).

Set for a debut in 1999, talks for a partnership with Royal Bank of Scotland (RBS) broke up and the card failed to materialise (Prestridge 1999). After searching for alternatives, the card was launched in 2002 in the UK and the USA, 2003 in Australia[13] and 2006 in South

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[12] The extent to which the proposed synergies materialised was questionable, given that the *Membership Miles* programme was open to 34 airlines (Webster 1993). The programme was also vilified by the press as being more expensive than other alternatives to accrue rewards through *Virgin Freeway* (Anderson 1995)

[13] It is interesting to note that *Virgin*'s quick international launch of the credit card was also encouraged by Australia's central bank decision-to shake up the credit card industry by increasing competition and reducing

Africa. As in many other ventures, Virgin aimed to focus on finding new avenues to retain existing customers. Indeed, Branson saw it as a "loyalty card", that is, a way of "keeping in touch" with the myriad of different customers across the sprawling Virgin empire (Hunt 2002). At the same time, partnerships were formed with credit card specialist MBNA in the USA and UK, Westpac in Australia (until 2007) and London-based Standard Chartered in South Africa.

As such, the launch of yet another card slugging it out with 1,500 other in Britain for a slice of the £84 bn market in 2002 would have been unremarkable (Hunt 2002). However, Virgin credit cards in the UK offered a flexible credit programme and allowed customers to choose interest rates, annual fees and rewards from a range of options (Condie 2003). Card users earned points to spend on Virgin products and were offered discounts on Virgin Atlantic flights.

Virgin Direct: Selling pensions, insurance and investment funds

The launch of the financial services group took place on December 1994. On that date a joint venture with an insurance company called Norwich Union was signed with the latter and Virgin putting in £2m each (Branson 2008, 161). The company became operational on March 1995 in the UK as Virgin Direct Financial Services. At the time, Branson said

> "I have identified a sector that was arrogant, complacent and fleecing the customer. I saw an opportunity to shake it up. So I set up Virgin Direct to offer people straightforward financial products that are easy to understand." (Bower 2008, 205).

Branson thus saw an industry "ripe for reform" given, first, poor service, high charges, disreputable practices and dissatisfied customers; but, at the same time, seems to have been influenced by forecasts that the personal finance market was bound to grow as more people took over greater responsibility for their financial security in their old age (Dick 2007, 21). Virgin Direct employed 60 people and sold directly to consumers over the telephone, offering retirement plans called "PEPs" (personal equity plans), income protection insurance and life insurance.

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fees (Condie 2003). This change in regulation also introduced a reduction in wholesale interchange fees banks charge each other for process credit card transactions and freeing up the credit card network to new entrants.

Less than a year later the joint venture was dissolved. According to Branson, "Norwich Union didn't have the appetite for building a bigger business, but Virgin Direct needed the capital to grow." (Branson 2008, 162). So in 1997 Norwich Union sold its 50 percent stake to Australian Mutual Provident (AMP), another insurance company, with Virgin owning 49.9 percent.

By 1997, Virgin Direct had attracted some 220,000 customers and its mutual funds had £1.5 billion under management (German 1997; Grant 2005a, 319). Around this time a joint venture with RBS created a subsidiary of Virgin Direct called Virgin One (Treanor and Cassy 2000). This new company enabled Branson's Virgin to launch a deposit (current/cheque) account called One on November 1, 1997 (German 1997). According to Branson, the idea originated at RBS as they wanted to bring something to Britain that was becoming quite popular in Australia, namely

> "... putting all of a customer's products together. At the end of each evening your net balance is charged interest. Most people have a separate mortgage, current account and savings, and you're paying interest on the whole mortgage. If you roll everything together, you'd have a lower negative balance and you could pay off your home loan more quickly." (Branson 2008, 162).

Unlike most traditional banks there were no high- street branches to be seen. Like Virgin Direct, Virgin One was also a telephone operation based in Norwich (East Anglia), open 24 hours a day throughout the year. About staffing Branson opined

> "[we] recruited people who wanted to help the customer and make a difference – it was a huge part of the training. There were no stifling scripts to follow, or average talk-times to listen to. We just answered questions. We hired people who believed – like we did – that Virgin was one revolutionary crusade to change banking in the UK." (Branson 2008, 163)

Virgin cash cards were usable at all but two of the 22,000 cash dispensers in the UK (the exceptions being those operated by the United Bank of Kuwait) (German 1997). Credits were to be paid in by post but Virgin customers also had access to RBS's retail bank branch system in the UK.[14]

[14] In 2000, RBS engineered what at that point was the biggest takeover in the history of British banking, when RBS acquired National Westminster Bank plc (NatWest) to create one of the three leading financial services providers in the UK and one of the top 10 global banks with a highly diversified portfolio of services for personal, business and corporate customers. Prior to the merger RBS's subsidiaries included Citizen's Bank, a retail bank operation in North America.

Initially the account was available only to Virgin's existing customers (through Virgin Direct) but was to open up to the general public as soon as practical.[15] At the time, a spokesmen for Sir Richard said that the venture aimed to operate profitably from the start and was not be used as a "loss leader" to siphon off business from existing banks and building societies (i.e. mortgage specialists that also accepted retail deposits) to later rack up charges when the business had been built up (German 1997). By October 1998, there were 2000 accounts, increasing to 9000 in 1999 and 15000 the year after that (Branson 2008, 163). While reflecting on this success Branson said:

> "I admit it was difficult to start because the UK public weren't used to the idea of putting all their eggs in one basket, however safe it may be.... [But the] dinner-party brigade became our best promoters. Doctors, lawyers and professional people were converting to its merits; they told their friends, and the idea began to spread through recommendation. We heard that people would take their Virgin One cards out at meals with friends and sell the idea. In business terms, this is pure gold. You can't buy this kind of advocacy." (Branson 2008, 162).

Shortly after, AMP and Virgin decided to rename Virgin Direct as Virgin Money. The change of name took place in 2001 (Dick 2007, 18). This move coincided with the amalgamation of Virgin Direct with Virgin-money.com. The latter was an independent, on-line stock trading website launched in 1999. Virgin Money was to be the single brand name and umbrella company for all of Virgin's financial services. Accordingly, it reorganised into three main units, namely: Virgin Direct Life (life insurance and retirement plans), Virgin Unit Trusts Manager (managed mutual funds); Virgin One; and Virgin Credit Card (Grant 2005a, 319).

Virgin Money's financial services were characterized by three features. First, they are low cost (Grant 2005a, 319). Virgin's credit card interest rates, fund management charges, and other fees tended to be below those of the major financial institutions. Second, Virgin's products offer several ease-of-use features (Grant 2005a, 319). For example, the Virgin One account allowed a number of products – home loans (i.e. mortgages), savings account, checking account, credit card debt – to be pooled into a single account offering significant administrative and interest cost conveniences.[16] Third, they are all joint ventures in which

[15] The Virgin One account was launched internally to Virgin staff in October 1997 and rolled out to the public throughout 1998 (Branson 2008, 162).

[16] The sale of Virgin One to RBS on December 2006, included a clause where Virgin would not enter the mortgage market for two years (Branson 2008, 164). The financial crisis of 2007-9 then limited market

Virgin outsources critical capabilities. For instance risk management which results in that, ultimately, most debts sit in someone else's balance sheet. Says Branson:

> "Virgin Money undertakes the marketing and designs the products – credit cards, savings and investments, life and general insurance – while partners provide the rest. (Bank of America operate [sic] our credit cards[17], which means the cards are on Bank of America's Balance sheets, not Virgin's!)" (Branson 2008, 165).

In spite of the apparently having broken new ground in personal finance through an innovative and simple offering, Virgin Money continued to lose money. Indeed, the amalgamation of Virgin Direct with Virgin-money.com had been an attempt to strengthen the asset base of the joint venture with AMP (Treanor and Cassy 2000). In July 2001, Virgin sold its 25 percent stake in Virgin One to RBS for £45 million (Grant 2005a, 319; Dick 2007, 18; Bower 2008, 360). Continuing poor performance in Virgin Money together with looses elsewhere prompted AMP to dismantle its banking operation and to divest non-core businesses (Condie 2003). Not surprisingly, in April 2003 AMP announced its intention to divest its 50 percent stake. In April 2004, Branson purchased AMP's 50 percent equity of Virgin Money for £90m (Grant 2005a). This after AMP sources reckon to have invested £144m in the venture (Condie 2003).

But in spite of the financial travails, Virgin Money pressed ahead and unveiled operations in the USA in 2008. Virgin Money USA was based in Boston, MA and powered by 30 employees. The rationale for this new outlet was familiar: "We can give American mortgage companies, banks and credit card companies a run for their money" said Sir Richard (Bower 2008, 389-80).

Virgin Queen: Attempt to take over Northern Rock

On September 14, 2007 the news broke that Britain's firth largest bank (in terms of total assets), Newcastle-based Northern Rock, had appealed to the government in desperate need of greater liquidity. The days that followed saw Armageddon. The media was full of

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possibilities for these activities to be undertaken. Hence, Virgin had not been able to get back into the mortgage business since selling Virgin One (Branson 2008, 165).

[17] In 2005, Bank of America Corp. acquired MBNA Corp. for $35 bn. The deal created one of the world's largest credit card issuers (called Bank of America Credit Card Services) but also resulted in a loss of 6,000 jobs of former MBNA employees (http://www.msnbc.msn.com/id/8414809/, accessed May 13, 2010).

images of long queues of ordinary people outside its retail branches, all of them waiting to withdraw their deposits. This was the first run on a British bank in over a century.

The idea to take over "the Rock" came from Jayne-Anne Gadhia (b.1961), chief executive (CEO) of Virgin Money. She graduated in history from Royal Holloway (one of the colleges of the University of London) and then pursued an accounting qualification while working at Ernst & Young, from here she moved to Norwich Union. She was introduced to Branson in 1994 by Rowan Gormley, her colleague at Norwich Union and who had just become head of Virgin Direct (Branson 2008, 160).[18] She then moved to the joint venture but left as part of the purchase of Virgin One by RBS in 2001. At RBS she rose to become the head of consumer finance in charge of a mortgage book worth £67 bn (Armitstead 2007). Branson then asked her back as CEO in February 2007.

She returned with a mandate to re-launch the mortgage portfolio "and propel the [Virgin Money] brand into the big league." (Farndon 2007). Ramping up sales of financial products by organic growth would take years. But when it was evident that Northern Rock was to lose its independence, she saw a chance to shortcut the process and transform the business overnight. Initially she called Gordon McCallum, strategy director, who politely turned her down. Undeterred she then blasted off a follow up email that same evening to McCallum and Stephen Murphy, head of the Investment Committee,

> "Hi there.
> Call me insane, but I have been thinking hard about how we might take some advantage from the current situation at Northern Rock – and help out at the same time. I think there are a number of opportunities – ranging from the possible to the outrageous:
> 1. Accept that the big balance sheet providers will take the assets and look to take the systems etc for a decent price.
> 2. Do a deal with a Citi [Citi Group] or BOA [Bank of America] where they buy the company but we put in the brand so they get a Virgin-branded retail presence in the UK.

[18] Early in 2000, Rowan Gormley, the founder of the ground-breaking business, was replaced as chief executive by Mark Lund and moved to set up Virgin Wines, an internet wine retailer. Lund was the former managing director of Henderson Investors, which was part of AMP activities in the UK. Lund was said to have been brought in with a mandate to turn Virgin Direct's losses into a profit (Treanor and Cassy 2000). The move was also seen as abandoning the original plan for it to turn a profit within five years with an option for flotation by 2003 (Treanor and Cassy 2000). However, Lund left the company after less than six months in the job and for reasons that remain obscure (Senior 2000). There were no immediate plans to appoint a new CEO while the company was run by the managing directors of its three divisions (Virgin Direct, Virgin Money and Virgin One) (Senior 2000). This set up seems to have remained in place at least until the sale of Virgin One to RBS in 2001.

3. Talk to Northern Rock and the Bank of England direct. Richard could be used as frontman to make some sense of the crisis. Northern Rock could be rebranded Virgin and the Bank of England stand behind the current loan facility. We could withdraw from mortgages from the time being and focus on savings to rebalance the balance sheet – and with Richard fronting a saving campaign – Branson making sense of the current crisis – it's all now about increasing savings and reducing debts, etc.
4. Whatever happens, I think we should do some research into who people would trust with financial services now. I bet the answer will be - Richard Branson.

On the one hand I know that this all sounds batty, but on the other hand – discontinuities in the system make it right for change – and I think we could do something. If Richard was able to speak to [Alistair Darling, Chancellor of the Exchequer] or [Gordon Brown, Prime Minister] to ask how we could help.

What do you think? I've restrained myself from copying this to Richard until I got your views.

J-A." (Branson 2008, 196-7).

McCallum's reply was still not very enthusiastic and asked for a discussion the following morning. But Gadhia pressed on and called Sir Richard directly, who after hearing her out embraced the idea whole heartedly.

When the idea became public, the popular press awarded Gadhia the nickname of "Virgin Queen" in remembrance of the capture of the Rock of Gibraltar and the marital status of Queen Elizabeth I (Farndon 2007; Watson 2007).[19] Publicly, she would admit to have long admired Northern Rock's efficient business model and innovative approach to mortgages: "when I was at RBS, we always looked with interest at Northern Rock", she said (Farndon 2007). But the point the financial press really wanted to make with the nickname was whether she was up to the job as she had little experience running a "blue chip" company (Farndon 2007).

The differences in size and scope between the two were substantial: before its collapse, Northern Rock was FTSE 100 business with 6000 staff.[20] Virgin Money employed 240 staff

[19] As is widely known, Elizabeth I (1533-1603), the last ruler of the Tudor dynasty, remained a maiden for all her reign (crowned 1558). But thinking that the original "Virgin Queen" could take over "the Rock" was inaccurate as it was until 1704 when an Anglo-Dutch expedition first took control of the town Gibraltar during the War of Spanish Succession (1701-1714). Gibraltar was ceded for perpetuity to Britain with the signing of the Treaty of Utrecht (1713). Gadhia, however, was married to a former tax-accountant, who as house-husband took care of their five year old daughter.

[20] The FTSE index tracks the movements in the price and volume of shares in the most highly capitalised companies in the London Stock Exchange. Capitalisation is measured by multiplying price times the number of shares outstanding of a public company. It is typically used as a measure of business prosperity.

and had a £200m annual turnover. Gadhia argued that as head of consumer finance at RBS she was in charge of a mortgage book worth £67 bn, roughly the same size of Northern Rock's which was valued at £90 bn in 2007. She explained

> "The problem was that 75 percent of [Northern Rock's] balance sheet relied on external funding. The fact that this dried up could be seen as unlucky. But what can't be down to luck bit a point of management is the acquisitions that Northern Rock made in the first half [of 2007]. During that time the bank took vast market share which then got into trouble with the credit crunch. Growth at all costs will go wrong." (Armitstead 2007).

A credible bid for Northern Rock had to raise at least £26 bn, in order to pay £16bn for the loan from the Bank of England plus another £10bn or so to keep funding levers up. Although Branson was to invest a significant amount of cash and assets into the venture (that is, £1.25 bn in new cash plus Virgin Money), the bulk of Virgin's bid was backed by insurance giant AIG; buyout firm WL Ross; private investment firm Toscafund, led by Martin Hughes and Sir George Mathewson (the former CEO of RBS); and Hong Kong investor First Eastern Investment; with debt finance from RBS; and Sir Brian Pitman, former CEO and chairman of Lloyds-TSB (the third banking group in the UK in terms of assets) as non-executive chairman. There were of course, competitors such as that put together by buyout firms JC Flowers and Cerberus.

But while others planned to break up the Northern Rock, lay off several hundreds of employees and sell its assets, Sir Richard and Gadhia insisted in trying to keep things together by not only by avoiding any sale of the assets but also not having any lay-offs (at least not until the recession was over). They also promised to allow existing shareholders to take part in any rights issue on preferential terms as well as promised to pay all debts to the government by 2010 {Branson, 2008 #2@202-3}. Said Gadhia,

> "We want to rebalance Northern Rock into a building society, diversify the products and put the Virgin brand on top. We are confident this can work out." {Farndon, 2007 #25}.

But in spite of all, Virgin's bid was seen as a poor offer. It never got the full backing of the financial press. It was criticised in Parliament by David Cameron (at the time leader of the opposition and to become Prime Minister in May, 2010) and Vince Cable (at the time, deputy leader of the Liberal Democrats and to become Business Secretary with responsibilities for banks in May 2010) {Branson, 2008 #2@207-8}. For Sir Richard, the final "nail in the coffin" came in February 2008 when bad publicity in the media following his trip to China with Gordon Brown, the then Prime Minister, made unsustainable the sale to Virgin, at that point the sole bidder, and Brown nationalised Northern Rock {Branson, 2008 #2@208-9}. However, one must also consider that as the credit crisis progressed, the cost of funding the operation was becoming ever more expensive for everyone {Branson, 2008 #2@204}. Indeed, rising cost of external funding and accumulated losses would ultimately led to the collapse of AIG (September 2008) and RBS had to receive financial support of the British government (October 2008) and was virtually privatised (January 2009).

But as the purchase of Church House Trust in January 2010 suggested, the Northern Rock affair was not going to dampen the enthusiasm for a greater presence in retail banking. The newly elected Conservative-Liberal Democrat coalition government had yet to decide what to do with their large equity stakes in Northern Rock, RBS, and the enlarged Lloyds Group (resulting for the amalgamation of Lloyds-TSB and Halifax-Bank of Scotland). So it looked very much that it was only a question of time before Virgin Money became a significant presence in the British retail financial sector.

Annex Virgin Group's management thought[21]

"Virgin is a leading branded venture capital organisation and is one of the world's most recognised and respected brands. Conceived in 1970 by Sir Richard Branson, the Virgin Group has gone on to grow very successful businesses in sectors ranging from mobile telephony to transportation, travel, financial services, media, music and fitness.

Virgin has created more than 200 branded companies worldwide, employing approximately 50,000 people, in 29 countries. Global branded revenues in 2008 exceeded £11 billion (approx. US$17 billion).

We believe in making a difference. Virgin stands for value for money, quality, innovation, fun and a sense of competitive challenge. We deliver a quality service by empowering our employees and we facilitate and monitor customer feedback to continually improve the customer's experience through innovation.

[21] http://www.virgin.com/about-us/ accessed on May 3, 2010.

When we start a new venture, we base it on hard research and analysis. Typically, we review the industry and put ourselves in the customer's shoes to see what could make it better. We ask fundamental questions: is this an opportunity for restructuring a market and creating competitive advantage? What are the competitors doing? Is the customer confused or badly served? Is this an opportunity for building the Virgin brand? Can we add value? Will it interact with our other businesses? Is there an appropriate trade-off between risk and reward?

We are also able to draw on talented people from throughout the Group. New ventures are often steered by people seconded from other parts of Virgin, who bring with them the trademark management style, skills and experience. We frequently create partnerships with others to combine industry specific skills, knowledge, and operational expertise.

Contrary to what some people may think, our constantly expanding and eclectic empire is neither random nor reckless. Each successive venture demonstrates our devotion to picking the right market and the right opportunity.

Once a Virgin company is up and running, several factors contribute to making it a success. The power of the Virgin name; Richard Branson's personal reputation; our unrivalled network of friends, contacts and partners; the Virgin management style; the way talent is empowered to flourish within the group. To some traditionalists, these may not seem hard headed enough. To them, the fact that Virgin has minimal management layers, no bureaucracy, a tiny board and no massive global HQ is an anathema. But it works for us! The proof of our success is real and tangible.

Our companies are part of a family rather than a hierarchy. They are empowered to run their own affairs, yet the companies help one another, and solutions to problems often come from within the Group somewhere. In a sense we are a commonwealth, with shared ideas, values, interests and goals.

Hopefully exploring the activities of our companies through this site demonstrates these ideals well, but if you have any comments or feedback, feel free to post them.

Managing the Virgin group is a pretty full time job and we have developed a canny way of doing it that keeps it fresh and lively whatever the company does and wherever it is based.

At the centre, Virgin Management Ltd (VML) provides advisory and managerial support to all of the different Virgin companies and our specialist Sector teams around the world. Our people in London, New York and Sydney offer regional support and between us and the Sector teams we manage Virgin's interests across the whole of the Virgin Group.

VML's fastidious number-crunchers get to manage Virgin's financial assets in the group, our cheeky marketeers and spin doctors get to protect and maximise the value of the Virgin brand and our touchy-feely people teams ensure Virgin is an employer of choice

Seeing as the Virgin businesses are all so diverse and independent, we pretty much practice a collaborative and supportive style of custodianship. Some of us would like to wear special uniforms.

We give birth to new Virgin companies, encourage them to walk, hold their hands and then watch them on their way as they become fully-fledged members of the Virgin family. It can sometimes get quite emotional.

To help manage the growth and development of our Virgin family we have set up sector teams, each run by a Managing Partner. These bigwigs look after interests in aviation, media & telecom, financial services, health & wellness, leisure, and Green (clean technology) investments. The specialists keep our companies on their toes and ensure we keep developing better experiences and world beating products."

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