

## Changes at Virgin Airlines (Australia) 2000-2012

### Case No: AGSM-13-001

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**Authors: J. Peter Murmann and Julie A. Cogin**

*This case has been compiled from public sources solely for educational purposes and aims to promote discussion of issues that surround the management of change in organisations rather than to illustrate either effective or ineffective handling of an administrative situation.*

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#### **Timeline**

- 2000 - Virgin launches Australian airline Virgin Blue imitating the low-far model of Ryan Air in Europe and Southwest in America with one class and one airplane type, Boeing 737
- 2003 - Virgin moves from no-frills “tin shed” at Sydney airport to terminal 2 space previously occupied by Ansett Airlines
- 2003 - December. Virgin Blue Holdings floated on the Australian Stock Exchange
- 2004 - Virgin Blue creates wholly owned subsidiary Pacific Blue to offer a low-cost service between New Zealand and Australia
- 2008 - Premium Economy Class was introduced throughout its entire fleet
- 2009 - V Australia’s inaugural flight from Sydney to Los Angeles (February) and Brisbane to Los Angeles (April)
- 2010 - John Borghetti (formally Qantas) becomes CEO on May 8
- 2010 - New business strategy - the Game Change program – announced
- 2011 - Virgin Australia is announced as the company’s new name, eliminating brands (Virgin Blue, Pacific Blue and V Australia)
  - Virgin Australia Business Class goes on sale across the domestic network, new lounges open in Melbourne and Brisbane
- 2012 - October, Virgin Australia announced it had purchased a 60% stake in Tiger Airways Australia for \$35 million

## Part 1: Virgin Airlines 2000-2004

Let's start by looking at an excerpt from the companies' 2003 prospectus, which provides an overview of its early business model.

**PROSPECTUS**

*You'll love our company.* 

Joint Global Coordinators Goldman Sachs JBWere and Credit Suisse First Boston

Virgin Blue Holdings Limited ACN 100 686 226



10 November 2003

Dear Investor,

On behalf of the Directors, it is my pleasure to invite you to become a shareholder of Virgin Blue Holdings Limited.

Virgin Blue is an Australian airline which commenced operations in August 2000 with equity funding from the Virgin Group. Its combination of low fares and excellent service represent good value for money for guests. In just three years of operations, Virgin Blue has captured a Total Domestic Market share of more than 28%.

The key competitive strengths of Virgin Blue are its low cost structure as a result of its young and modern aircraft fleet, its low fare offering and strong profitability, its management team, which has significant experience in the airline industry, its strong brand, its unique culture and the enthusiasm, commitment and productivity of its workforce.

Virgin Blue intends to continue to grow its business by increasing frequencies on the routes it already services, launching services on secondary business routes, adding regional leisure routes to its network and commencing international operations within the Pacific Region. Virgin Blue has proven its ability to operate successfully in a competitive market and the Directors are confident that this will continue in the future.

The Directors believe that Virgin Blue's growth outlook, strong profitability combined with low fares, and returns well in excess of its cost of capital represent an attractive investment proposition.

Detailed information about the Offer and Virgin Blue's business, as well as the risks of investing in Virgin Blue, are set out in this Prospectus, which I encourage you to read carefully.

Together with my fellow Directors, I commend the Offer to you and look forward to welcoming you as a shareholder of Virgin Blue.

Yours sincerely,

A handwritten signature in black ink that reads "C. Corrigan".

Chris Corrigan  
Chairman

Virgin Blue Holdings Limited Share Offer





# AUSTRALIA'S LOW FARE, LOW COST AIRLINE

VIRGIN BLUE'S COST STRUCTURE ENABLES  
IT TO OFFER AIR FARES THAT ARE ON  
AVERAGE LOWER THAN ITS COMPETITORS,  
WHILE MAINTAINING **HIGH PROFIT MARGINS.**

Virgin Blue Holdings Limited Share Offer

## AUSTRALIA'S LOW FARE, LOW COST AIRLINE

Virgin Blue has:

- ✈ Captured more than 28% of the Total Domestic Market in just 3 years.
- ✈ Grown from operating two leased aircraft between Brisbane and Sydney, to operating 40 aircraft, servicing 37 domestic routes.
- ✈ A highly competitive cost structure:
  - Modern and efficient aircraft fleet
  - Highly productive and flexible workplace arrangements
  - Efficient sales distribution and ticketing systems

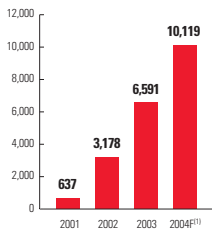


National Coverage: As at 1 November 2003, Virgin Blue operated on 37 domestic routes serving 20 airports in Australia. Pacific Blue's service between Brisbane and Christchurch, New Zealand, is expected to commence in January 2004 and between Melbourne and Christchurch in March 2004.

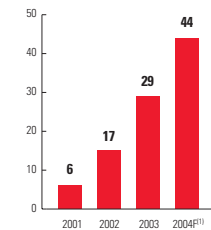


Friendly service in the air.

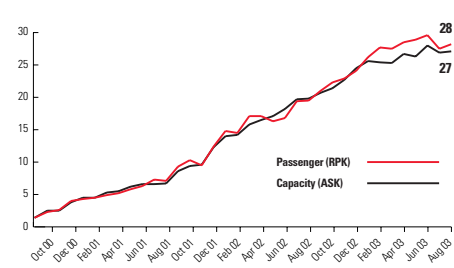
**Number of passengers carried year ended 31 March (thousands)**



**Number of aircraft year ended 31 March (number)**



**Virgin Blue Total Domestic Market Share (per cent)**



(1) See Section 7 for forecast information.



The internet is the cheapest distribution channel for airlines. Currently more than 85% of all Virgin Blue bookings are made over the internet, one of the highest levels of airline internet sales penetration in the world.

Friendly service on the ground and a modern fleet. Virgin Blue's fleet of aircraft is the most modern in Australia and one of the youngest in the world.

Virgin Blue Holdings Limited Share Offer





# *PROSPECTUS*



*You'll love our company.*

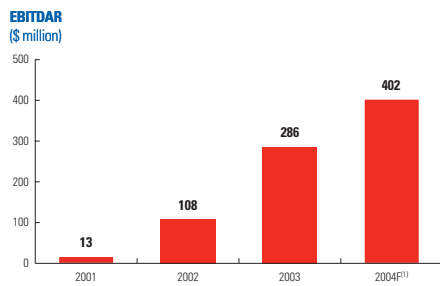


Joint Global Coordinators Goldman Sachs JBWere and Credit Suisse First Boston

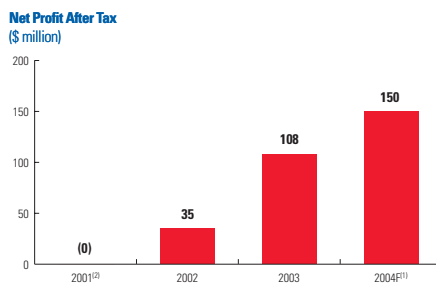
Virgin Blue Holdings Limited ACN 100 686 226

Virgin Blue Holdings Limited Share Offer

## TRACK RECORD OF GROWTH AND PROFITABILITY



(1) See Section 7 for forecast information.



(2) Excludes start up costs of \$10.59 million.



Virgin Blue focuses on those areas which are most valued by its guests such as safety, on-time performance, frequent flights, terminal facilities, booking systems and check-in and in-flight services.

Virgin Blue is committed to delivering low fares together with high quality, friendly customer service.



Virgin Blue Holdings Limited Share Offer





# STRONG BRAND

**CUSTOMERS ASSOCIATE VIRGIN BLUE WITH:  
VALUE FOR MONEY, QUALITY, INNOVATION,  
COMPETITIVE SPIRIT AND FUN.**

Virgin Blue Holdings Limited Share Offer

## STRONG BRAND AND UNIQUE CULTURE



**Life President** Sir Richard Branson, the founder of the Virgin Group which provided the start up capital for Virgin Blue, has been appointed Life President of Virgin Blue.

Management believes that the entrepreneurial spirit of the Company and the enthusiasm, commitment and productivity of its workforce gives the Company an important advantage over competitors.

## PROVEN MANAGEMENT TEAM

Virgin Blue's senior management team:

- ✦ has extensive experience in the Australian and international airline industry
- ✦ has continuity since the start of operations
- ✦ is incentivised by the ownership of shares and options



Virgin Blue's senior management team has extensive airline industry expertise both within Australia and internationally. The senior management team have remained with Virgin Blue since the commencement of operations in August 2000. Back row: David Huttner, Diederik Pen, Rob Sherrard, Scott Swift, Manny Gill, John Raby. Front row: Tim Jordan, Bruce Highfield, Keith Neate, Brett Godfrey, Martin Daley, Nick Brant, Mike Hockin

Holdings Limited Share Offer





# A UNIQUE CULTURE

VIRGIN BLUE'S **ENTREPRENEURIAL SPIRIT** AND ITS WORKFORCE'S ENTHUSIASM, COMMITMENT AND PRODUCTIVITY PROVIDE AN IMPORTANT ADVANTAGE OVER ITS COMPETITORS.



Virgin Blue Holdings Limited Share Offer



**PRE LAUNCH DAY 9TH JULY 2000**

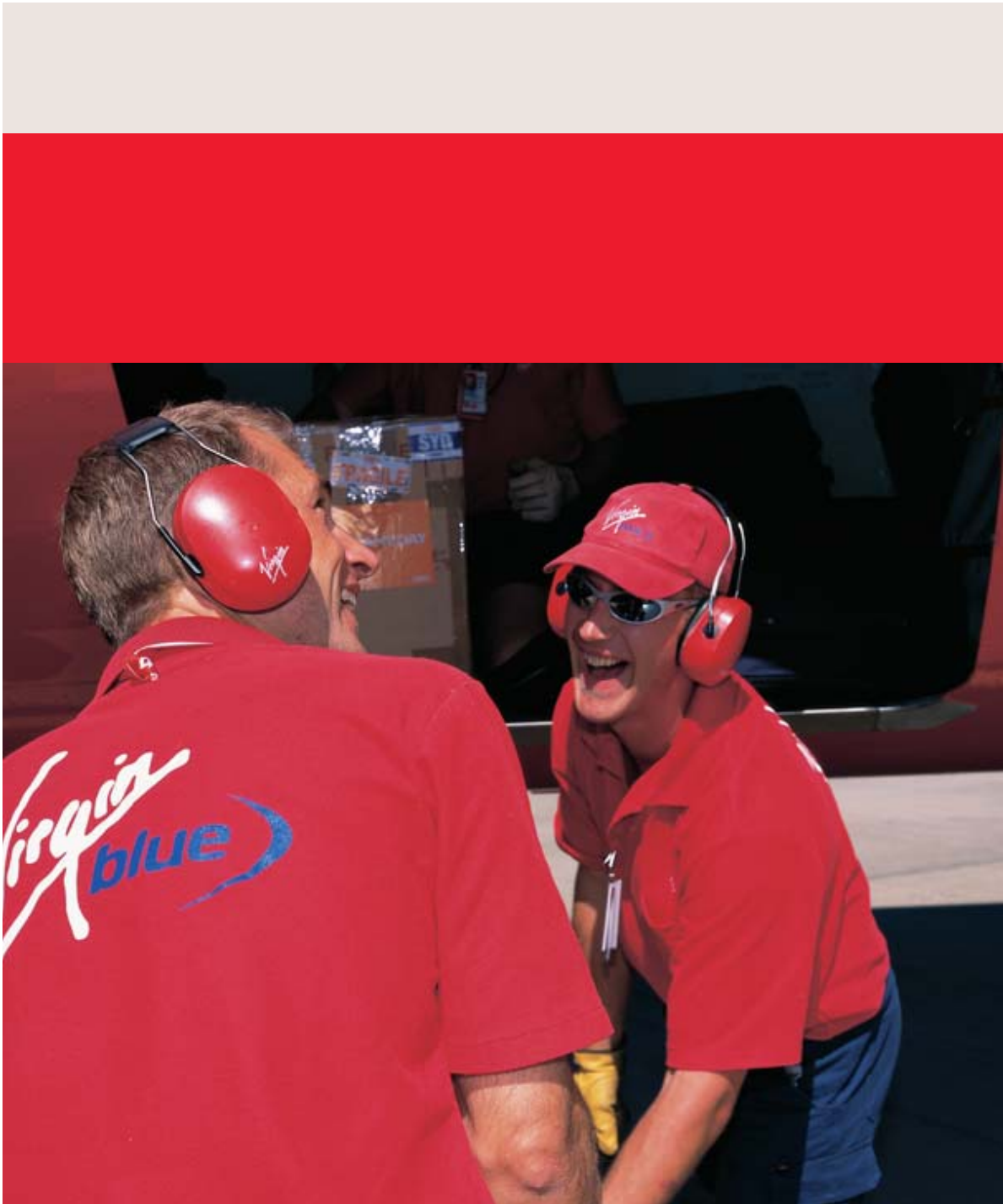
**210 START UP STAFF, TWO RED JETS, ONE  
ENTREPRENEUR AND ONE EXCITING MOMENT  
IN AUSTRALIAN AVIATION HISTORY...**

Virgin Blue Holdings Limited Share Offer



**A GREAT BEGINNING!**

Virgin Blue Holdings Limited Share Offer



**SECTION 1:**

**SUMMARY OF KEY  
INFORMATION**



# 1. SUMMARY OF KEY INFORMATION

## 1.1 Business Overview

Virgin Blue is Australia's low cost, low fare domestic airline, offering frequent passenger services on routes between all of Australia's major cities. Virgin Blue's aim is to offer fares that are on average substantially lower than those of its competitors and to provide guests with a differentiated, value for money service. Virgin Blue believes that its highly competitive cost structure will allow it to continue to offer low fares while maintaining returns well in excess of its cost of capital.

In just over three years, Virgin Blue has captured a market share of more than 28% of the Total Domestic Market and has grown from a company operating two leased aircraft between Brisbane and Sydney, to operating 40 aircraft servicing 37 domestic routes. Furthermore, Virgin Blue has been able to maintain an operating cost structure that is highly competitive.

In addition to the low fares, guests travelling on Virgin Blue benefit from a service that is differentiated by Virgin Blue's unique culture and high quality customer service.

For the year ended 31 March 2003, Virgin Blue carried 6.6 million guests and generated total revenue of \$915 million, an increase of 136% over the previous year. For the six months ended 30 September 2003, 4.5 million guests were carried resulting in total revenue of \$617 million, an increase of 55% from the previous corresponding period.

Virgin Blue has also achieved strong growth in profits since commencing operations in August 2000. For the year ended 31 March 2003, Virgin Blue generated profit from ordinary activities after income tax expense of \$108 million, an increase of 210% over the previous year. For the six months to 30 September 2003, Virgin Blue achieved \$64 million in profit from ordinary activities after income tax expense, representing a 30% increase from the previous corresponding period.

Virgin Blue's success has come during a period of extremely difficult conditions in the global airline industry with events such as the 11 September 2001 terrorist attacks in the United States, the war in Iraq and the outbreak of SARS significantly impacting demand for worldwide air travel services.

### Selected Operating Statistics

	7 Months Ended 31 March 2001	12 Months Ended 28 March 2002	12 Months Ended 31 March 2003	6 Months Ended 30 September 2002	6 Months Ended 30 September 2003
Passengers	637,337	3,178,423	6,591,120	2,804,543	4,483,032
RPK (millions)	664	3,169	7,194	2,976	5,115
ASK (millions)	891	3,898	9,078	3,870	6,084
Passenger load factor	73.9%	82.2%	79.4%	77.5%	83.8%
Average number of aircraft	4.4	11.0	24.1	20.1	30.3

## 1.2 Competitive Strengths

Virgin Blue's competitive strengths include:

### Low Cost Operations

Virgin Blue's low cost structure is underpinned by:

- its modern, single type fleet of Boeing 737 Next Generation aircraft with a high density, single class seating configuration. Operating a single type of aircraft allows Virgin Blue to minimise the complexity of its operations, take advantage of economies of scale and achieve high aircraft utilisation rates. Virgin Blue's fleet is the youngest in Australia (with an average age of 1.6 years), providing high fuel efficiency and low maintenance costs and down-time;
- its December 2002 agreement with Boeing under which Virgin Blue has agreed to purchase ten aircraft and has been provided with purchase rights to acquire, at highly competitive prices, up to an additional 50 Boeing 737 Next Generation aircraft by 31 December 2013;

- its efficient sales distribution and booking systems. The Company believes the internet is the cheapest distribution channel for airlines. As at 1 November 2003, more than 85% of all Virgin Blue bookings were made over the internet, one of the highest penetration rates of airline internet sales in the world. In addition, Virgin Blue operates a ticketless booking system that allows it to minimise distribution and booking costs;
- the low cost operating environment in Brisbane, where Virgin Blue is based, combined with Brisbane airport's substantial available capacity;
- its competitive, highly productive and flexible workplace agreements; and
- the elimination of expensive, non-essential service add-ons such as "free" meals and traditional frequent flyer programmes.

**Low Fares and High Profitability**

Virgin Blue is committed to offering guests affordable air travel and its fares are on average lower than those of its competitors. The Company believes that its low fares stimulate demand when starting services on new routes and when increasing frequencies on existing routes. Virgin Blue's low cost structure enables it to offer low air fares while maintaining returns well in excess of its cost of capital.

**Experienced and Proven Management Team**

Virgin Blue's senior management team, led by Brett Godfrey (the Chief Executive Officer) and Rob Sherrard (the Chief Operating Officer and Deputy Chief Executive Officer), has extensive airline industry expertise both within Australia and internationally. Brett and Rob have held the same positions with Virgin Blue since they co-founded the airline.

Brett and Rob conceived and developed the business model for Virgin Blue and selected the core senior management team to launch the business. The core of the senior management team they selected for start up has remained with Virgin Blue since the commencement of operations in August 2000, ensuring consistency and commitment to the development and growth of the Company.

**Strong Brand**

Virgin Blue believes that its competitive position has been assisted by public awareness of the Virgin brand. In the period since the Company's inception, the "Virgin Blue" brand has itself become a well recognised brand in Australia. The Company has differentiated itself from its competitors and believes that its guests associate Virgin Blue with the airline's core brand ideals of quality, value, reliability, innovation, competitive spirit and fun.

**Unique Culture**

Virgin Blue believes that the entrepreneurial spirit of the Company and the enthusiasm, commitment and productivity of its workforce give the Company an important advantage over its competitors. A contributing factor to this culture is Virgin Blue's tailored recruiting procedures, continuing training programmes, performance based remuneration policies and a belief by the staff in the values of the Company.

**High Quality Customer Service**

Virgin Blue is committed to delivering low fares together with high quality, friendly customer service. Virgin Blue focuses on those areas most valued by its guests such as safety, on-time performance, frequent flights, terminal facilities, booking systems and check-in and in-flight services.

**Strong Capital Structure**

Virgin Blue believes that, following the Offer, its capital structure will enable it to continue to take advantage of growth opportunities and that it has sufficient resources to effectively compete and provide some financial protection against any temporary deterioration in business conditions.

Virgin Blue Holdings Limited Share Offer

## 1. SUMMARY OF KEY INFORMATION (CONTINUED)

### 1.3 Strategy

Virgin Blue's strategy is to continue to leverage its existing business model to provide high quality, low fare, low cost airline services and to take advantage of growth opportunities. Virgin Blue's aim is to offer fares that are on average substantially lower than those of its competitors, and to provide guests with a differentiated, value for money service. Key elements of Virgin Blue's strategy include:

- increasing frequencies on existing routes, including the key business routes between Sydney, Brisbane and Melbourne;
- launching new services on secondary business routes;
- launching new services on regional leisure routes;
- commencing international operations in the Pacific Region within the flying range of its current fleet under the name Pacific Blue; and
- introducing new value-added, user pays service enhancements, which at a minimum are cost neutral to the Company.

### 1.4 Key Investment Considerations

Key investment features of Virgin Blue include:

- **Australia's Low Fare, Low Cost Domestic Airline**  
In just three years, Virgin Blue has captured a market share of more than 28% of the Total Domestic Market.
- **Solid Track Record of Growth and Profitability**  
Virgin Blue has achieved significant growth in profits since the commencement of operations in August 2000. Its EBITDAR margin is among the highest in the airline industry.
- **Attractive Growth Opportunities**  
Significant growth opportunities exist through an increased competitive focus, demand stimulation on new domestic routes and on existing domestic routes through increased flight frequencies, introduction of international services, add-on user-pays service initiatives and holiday packages.
- **High Returns on Capital Invested**  
High levels of aircraft utilisation, high profit margins, and optimal aircraft financing allow Virgin Blue to achieve comparatively high returns on invested capital. The Company believes its business model will continue to deliver comparatively high returns on capital as it continues to grow.
- **Strong Competitive Position**  
Virgin Blue is the lowest cost national airline operator in Australia. Virgin Blue's business model is focused on maintaining a low cost base to be able to offer lower air fares to passengers, while retaining attractive profit margins.
- **Experienced and Proven Management Team**  
Virgin Blue's senior management team has extensive experience in the airline industry, both within Australia and internationally.

### 1.5 Summary of Financial Information

The summary historical financial information below should be read in conjunction with, and is qualified by reference to, the information contained elsewhere in this Prospectus and the historical financial information contained in Appendix A. The historical financial information included in Appendix A has been prepared in accordance with the recognition and measurement principles prescribed in Australian Accounting Standards and other mandatory professional reporting requirements in Australia.

Virgin Blue's corporate structure has changed since the commencement of the airline's operations in Australia. Certain adjustments and reclassifications have been made to present the historical financial information included in this Prospectus on a basis that is consistent with Virgin Blue's current structure and operations. Information regarding these adjustments and reclassifications is provided in Sections 6.1 and 6.3 and Notes 1(a) and 1(b) to the historical financial information contained in Appendix A.

The forecast financial information comprises the Aggregated Forecast statement of financial performance for the year ending 31 March 2004. This information should be read in conjunction with, and is qualified by reference to, the information contained elsewhere in this Prospectus and the forecast financial information contained in Section 7.

**Summary of Financial Information**

	<b>7 Months Ended 31 March 2001</b>	<b>12 Months Ended 28 March 2002</b>	<b>12 Months Ended 31 March 2003</b>	<b>6 Months Ended 30 September 2002</b>	<b>6 Months Ended 30 September 2003</b>	<b>12 Months Ending 31 March 2004  Aggregated Forecast<sup>(1)</sup></b>
<b>\$ Thousand</b>	<b>Pro Forma</b>	<b>Pro Forma</b>				
Total Revenue	74,775	388,297	914,567	398,291	616,669	1,386,306
EBITDAR <sup>(2)</sup>	13,170	107,625	285,924	124,837	173,606	402,086
EBITDAR Margin	17.6%	27.7%	31.3%	31.3%	28.2%	29.0%
EBIT <sup>(3)</sup>	(236)	44,479	146,939	67,590	85,997	212,215
Profit from Ordinary Activities after Income Tax Expense <sup>(4)</sup>	(10,802)	34,764	107,799	49,544	64,175	150,000

**Notes:**

- (1) In accordance with customary practice in offerings in Australia, this Prospectus includes forecast financial information. The forecast financial information has been prepared by the Directors and comprises a forecast statement of financial performance for the six month period ending 31 March 2004 (the "Directors' Forecast") and an aggregated forecast statement of financial performance for the year ending 31 March 2004 (the "Aggregated Forecast"). The Aggregated Forecast represents the addition of the statement of financial performance for the six month period ended 30 September 2003 and the forecast statement of financial performance for the six month period ending 31 March 2004. The forecast financial information is necessarily based upon a number of estimates and assumptions that, while presented with numerical specificity and considered reasonable by the Company, are inherently subject to significant business, economic and competitive uncertainties and contingencies many of which are beyond the control of the Company, and upon estimates and assumptions with respect to future business decisions which are subject to change. These estimates and assumptions are discussed in greater detail in Section 7. The inclusion of forecast financial information in this Prospectus should not be regarded as a representation or warranty with respect to its accuracy or the accuracy of the underlying estimates or assumptions or that the Company will achieve or is likely to achieve any particular results. The forecast financial information presented in this Prospectus may vary from actual results, and these variations may be material.
- (2) EBITDAR is defined as earnings before interest, income tax, depreciation, amortisation and aircraft rentals. Virgin Blue believes that EBITDAR provides useful information but should not be considered as an indication of, or alternative to, profit from ordinary activities after income tax expense as an indicator of financial performance or as an alternative to cash flow as a measure of liquidity. Other companies may calculate EBITDAR in a different manner than Virgin Blue.
- (3) EBIT is defined as earnings before interest and income tax.
- (4) Profit from ordinary activities after income tax expense for the seven months ended 31 March 2001 includes start up costs of \$10,590,000.

**1.6 Dividend Policy**

Virgin Blue will not pay any dividends from the time of listing on ASX in relation to the year ending 31 March 2004. The Company's dividend policy in future years will be at the sole discretion of the Directors and dependent upon the Company's earnings, financial condition, financial arrangements, financing requirements for future growth, the competitive environment and any other factors the Directors may deem relevant in the circumstances.

**1.7 Structure of the Offer**

The Offer is structured as follows:

- the Retail Offer, which consists of:
  - the General Public Offer, open to Australian resident retail investors and the trustee of the Key Employee Performance Plan (the "KEPP Trustee");
  - the Employee Offer, open to certain employees as described in Section 2.6; and
  - the Broker Firm Offer, open to Australian resident retail investors who have received a firm allocation from their broker;
- the Institutional Offer, which consists of an invitation to bid for Shares made to certain Institutional Investors in Australia, New Zealand and certain other overseas jurisdictions;
- the Patrick Offer, which consists of an offer to the Patrick Shareholder to subscribe for a number of New Shares in the Offer such that, on completion of the Offer, its shareholding in Virgin Blue will be 45% of the issued share capital of Virgin Blue on a fully diluted basis. See Section 2.5 for additional information;
- the Executive Offer, which consists of an invitation to Existing Option Holders to receive Shares in consideration for the cancellation of Existing Options granted pursuant to the Existing Option Plan; and
- the Employee Gift Offer, which consists of an offer of \$1,000 worth of New Shares to Gift Offer Employees based on the Final Price.





## Part 2: Virgin Airlines after 2010

Here are excerpts from news articles that describe changes to the Business Model of Virgin in recent years.

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### **Virgin Australia CEO declares “Game on” in battle with Qantas**

Virgin Australia is launching the second phase of its three-year ‘Game Change’ transformation from the low-cost Virgin Blue to a full-service Qantas competitor – and the new war cry is ‘Game on’.

“We are now almost a year ahead of schedule on the (Game Change) strategy, having achieved the majority of our goals” said Virgin Australia CEO John Borghetti on today’s release of the airline’s 2011-2012 financial results, which reveal a post-tax profit of \$22.8 million, compared to last year’s loss of \$67.8 million, and based on \$3.9 billion revenue.

“Today’s result gives us the confidence to reach for the next phase of the Game Change Program – it is now ‘Game On’.”

Borghetti won’t be drawn on specifics but says “In this phase, we will introduce further innovative product and service enhancements to establish a superior position in customer experience.”

Virgin reports that the profitable corporate and government travel market now makes up 20 per cent of its domestic revenue, a milestone which Borghetti described as “a tipping point which we believe effectively creates a new competitive norm.”

Borghetti also wants to dramatically boost the number of members of its Velocity Frequent Flyer scheme in the next three years, transforming it “from a frequent flyer program to a broad-based loyalty program in its own right” (see our full report <http://www.ausbt.com.au/virgin-australia-s-big-plans-for-velocity>).

### **New lounges**

The first stage of Virgin’s new ‘flagship’ lounge at Sydney Airport will open by year’s end, in the form of the all-new upstairs level, however the complete two-level lounge won’t be open “until March 2013”, Borghetti told Australian Business Traveller.

Also on the slate for 2013 is a new lounge for Virgin’s shiny new terminal at Canberra, along with Hobart and Cairns.

### **New planes for 2013-2017 and beyond**

By mid-2013 Virgin expects to have taken on 10 new Boeing 737-800s and its sixth Airbus A330, with the later feeding into the plan to run transcontinental flights from Sydney and Melbourne to Perth as A330-only services.

By June 2015 the airline plans another eight 737-800s plus two more A330s, and Borghetti again hinted that the A330s could appear on international routes, saying they “could be deployed in any market as the market demands.”

Borghetti recapped the airline’s plans to order 23 fuel-efficient Boeing 737 MAX 8 aircraft, which will enter the fleet from 2019, and will place an order for either the Boeing 787 or Airbus A350 within the next 12 months.

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**Source:** <http://bit.ly/Wonhrc>

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## Game Change for Virgin Australia

November 25, 2011

By: eGlobal

For the Virgin Blue Holdings Limited, the 2011 Financial Year marks the first year of their three year Game Change Program strategy and the Virgin Australia's goal of transforming into airline of choice is fast becoming a reality.

The company is maintaining a tight control on costs and is heavily focused on future opportunities to drive revenue growth. Strong progress is already being reflected in the uplift in corporate and government revenue year on year.

As part of its continuous improvement process, the company has established a Board Safety and Operational Risk Review Committee that will directly supervise the safety performance. This will guarantee that safety remains the number one priority, in all departments from the day-to-day operations of the engineers and crew, to the strategic decisions of the management and board.

In December 2010, the Directors formalized a vision for the airline to become a sustainability leader in the aviation industry and have done considerable work this year on reaching the current position and goals. The company has a number of fuel and operational efficiency initiatives underway, including investments in a six year \$2.5 billion fleet renewal program which will see average aircraft age reduce from 4.9 years to 4.1 years by the end of the 2012 Financial Year.

The company is however confident that the Game Change Program is the right course of action. In the first quarter of the current financial year, they are profitable and tracking ahead of budget and on last year.

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**Source:** <http://bit.ly/Woj5rs>

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## Sky's the limit. An interview with John Borghetti

Tuesday August 28, 2012

By Anthony Black - Bigpond Money

To successfully run a business in challenging times requires a mix of priorities rather than a narrow focus, according to Virgin Australia chief executive John Borghetti.

He says too many aviation chief executives around the world are fixated on cutting costs, believing the axe is the only way to mend their balance sheets.

He disagrees. "All they (other airline CEOs) want to talk about is cutting costs," he says. "Of course, that's normal business. But very few of them talk about how to improve their airline's revenue streams, their service, or how to engage more with their customers or staff."

Borghetti says a clear and concise strategy will drive bigger revenue streams and profits. "Run the business right and the consequence will be good numbers," he says. This is his long-held belief, and Borghetti wasted no time implementing his aptly-named "game change" plan when he became chief executive in May 2010.

After devising a strategy, he suggests sticking to it and giving it time to work. "It might need tweaking here and there, but it has to be consistent," he says. "Don't

drastically change it every two or three months, that's a certain highway to failure."

Borghetti is a hands-on operator, who expects and relies on clear and honest communication with senior managers. When it comes to managing budgets, he says "transparency is the secret".

"I hate surprises," he says. "I want to know from my staff if the numbers are good or bad – and in real time.

"I want to know what the situation is now, not what it was a month ago. I don't want to be told, 'it's too early to tell what the last three weeks have been like'. Staff need to make considered judgments. They need to be flexible and disciplined."

He suggests all business leaders should keep a close eye on investment returns. "You have to squeeze the most out of every dollar," he says. "If the plan is to invest, say \$1, to make \$10, then check to see if it's happening or has happened. If the \$1 only made \$9, then examine why it's not \$10. If that's the case, it's time to think a bit harder."

Central to Borghetti's three-year game change strategy was to diversify the company's revenue streams. Virgin Blue, as it was previously known, was almost totally dependent on the leisure market, exposing the company to big losses from natural disasters.

In a six-month period, Virgin lost more than \$100 million due to the Christchurch earthquakes, Queensland floods and volcanic ash clouds. Borghetti says 52 per cent of Australia's domestic network flies in, or out, or within Queensland.

Depending almost entirely on the leisure market carried too much risk. Borghetti's blueprint included competing against Qantas in the more lucrative business segment. Qantas dominated the business travel segment before Virgin entered the space in January 2011.

To entice business travellers, Virgin started a price war, undercutting Qantas business fares by 27 per cent, which Borghetti says is sustainable over the longer term. "We're gaining on Qantas," he says. "We now have about 30 per cent of capacity in the market while Qantas has about 65 per cent. Take out Jetstar, and Qantas has about 45 per cent. I don't call it a price war, I call it competition. Qantas had a monopoly in business class for 10 years, so they didn't have to discount their prices, but now they do. We haven't cut fares for the short term."

To capitalise on the business segment, Borghetti also increased the number of flights between Melbourne and Sydney from the low 20s to 31 a day, and introduced new regional routes from capital cities in the same state. He established a global network with strategic alliance partners, enabling co-operation on pricing, scheduling, co-ordination and reciprocity in terms of frequent flyer programs.

"So now we have a global network that can fly you into more than 400 destinations around the globe, to destinations on other people's airlines with our code and passengers can still earn frequent flyer points," he says. "Diversifying our revenue base has led to a more stable earnings profile."

Borghetti considers himself a people's man and makes a point of personally talking to staff and customers. "I'm on a plane at least once a day," he says. "You have to talk to people – they know more about things than you do. I talk to passengers in lounges and ask where we can improve and how we can make them more comfortable. They may be very basic questions, but the feedback delivers a lot."

Before his Virgin appointment, Borghetti spent more than 35 years at Qantas, where he held several senior executive positions. He considers hard work, vision, commitment and luck as essential ingredients for landing the top job. He says those

with ambition should gather as much experience as possible to advance their careers.

“The more you learn about different aspects of a business puts you in a better position,” he says. “Any form of training that hones your people and operational skills is an advantage.

“Importantly, you have to be able to rise above the situation and simplify the issue. Successful people need the detail, but they rise above the detail to simplify the problem and find a solution.”

Many people strive to become a company chief executive some day, but are overlooked for any number of reasons. Perhaps, this is a reason. Borghetti explains: “Too many people worry about their next job, when they should be worrying about their current one. If you’re focusing on your current job, promotions will come.”

**Source:** <http://bit.ly/WomLJK>



**2a. Exercise Question:**

Articulate the changes to Virgin’s business model from when they first entered the Australian market until now. What changes did Virgin make to the Customer Value Proposition, the Profit Formula, the Key Resources and Key Processes?

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**2b.Exercise Question:**

Compared to other changes to business models that you have encountered in the readings for SM4, is the change to Virgin Business Model relatively small or relatively large? What challenges does this create?

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