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## Delta Air Lines (B): The Launch of Song

By the July 2002 board meeting, Delta's LCC task force had reached a recommendation: Delta should launch a new "airline within the airline" to help meet the threat of low-cost competition. The board agreed, and just eight months later, the first flight of the new subsidiary – now named Song – lifted off from New York's Kennedy Airport bound for West Palm Beach, Florida.

### Making the Decision

For four months leading up to the board meeting, the LCC task force had worked feverishly. Staff members seconded from network and revenue management, marketing, finance, and strategic planning had relocated from their usual desks to an isolated den of cubicles near the offices of Delta's top executives. McKinsey consultants further cramped the space. White boards filled with tree diagrams charted Delta's options. A "hypothesis-driven approach" led the team to undertake an array of analyses: a market research study, a very thorough review of failed low-cost subsidiaries, analyses of Delta's route network and cost structure, and so forth.

Gradually, options dropped from consideration. A "do nothing" scenario, which charted the financial consequences of inaction, reinforced the team's belief that the status quo was unacceptable. Tweaking Delta Express would also fail, the task force believed: Express would never be cost-competitive, it lacked a distinctive brand, and – perhaps most important – it was too closely tied to "Mother Delta." "Delta Express had no independent spirit," CEO Mullin explained. "We needed an organization that ate, lived, and breathed low costs."<sup>1</sup> As it ruled out options, the task force also recognized some design principles. For instance, the decision to implement any new subsidiary should *not* depend on pilot wage concessions. The subsidiary must not operate in a way that jeopardized labor relations in mainline Delta. The subsidiary should meet and preferably surpass the service and entertainment standards established by JetBlue. "We realized that we needed a distinctive product *and* a lower cost," said task force coleader Balloun. "Unlike Southwest, with JetBlue, you can't just compete with cost. You also need to match the product, or else you'll lose."<sup>2</sup>

By July, the task force had developed a concrete proposal. On matters of route planning and aircraft usage, the proposal was quite specific. The new subsidiary would operate 36 757s, taken primarily from overgauged secondary hubs. It would focus on Northeast-to-Florida routes, with city pairs and flight frequencies already pinpointed. On other matters, however, the proposal was purposely left open. Decisions about customer targets, marketing, pricing, branding, and human

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Professor Jan W. Rivkin and Research Associate Laurent Therivel prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

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resources, the task force felt, were better made by the team that would implement the proposal. "It was a business case, not an implementation plan," Balloun explained. The task force made one final recommendation: the new subsidiary should be a separate organization with its own culture and a strong leader—"a bulldog."

## Making the Airline

John Selvaggio embraced the challenge of turning the proposal into a functioning airline. A veteran of American Airlines, Midway Airlines, and US Airways before joining Delta in 1998, Selvaggio knew the checkered history of low-cost subsidiaries. "Low cost is not enough," he said. "The world is littered with the carcasses of low-cost subsidiaries of legacy carriers. The only thing lower than their costs was their revenue."<sup>3</sup> Delta's new venture would have to do something different than those failed subsidiaries, which would require independent thinking. Selvaggio was, in the words of Mullin, "about as independent a thinker as you can get."<sup>4</sup> As president of Song, Selvaggio quickly recruited a leadership team (whose backgrounds are outlined in **Exhibit 1**). Coordinated by a 3,500-line Gantt chart,<sup>a</sup> the team began to piece together the airline.

**Finding the customer** "You can't do everything," Selvaggio explained. "I like to be really focused and specific in my targets."<sup>5</sup> Accordingly, the construction of the airline began with a search for a target customer. The task force's proposal had focused on Florida, and the 757s would be economical only at high load factors. As a result, the new subsidiary would certainly target leisure customers. Within the leisure market, Selvaggio saw opportunity for further segmentation:

Leo [Mullin] didn't want people to confuse us with mainline Delta. It was important that we be different than, but not less than, the mainline. Mainline Delta had the same target customer as just about every other major airline: the businessperson and, in particular, the *businessman*. We knew we would target leisure travelers, not business travelers. But then we said, "Let's be really different and target *women*." No airline had ever targeted women before. And as we did our research, we found that women booked 75% of all leisure trips and conducted 90% online travel research, and they had different needs than men.

Selvaggio's team dubbed their target the "Discount Diva" (**Exhibit 2**). The Diva was successful; was age 45; had household income of \$75,000-plus; was interested in fashion, health, and design; and was eager to have choices.

**Designing the experience** From a list of 600 candidates, the name "Song" was chosen for the new subsidiary. The name, Selvaggio explained, would appeal to the Diva and, since everyone has her own favorite song, it would be emblematic of choice. The Diva's experience with Song would begin with booking a flight. She could call a dedicated Song reservation agent, working in a separate call center from Delta agents, or she could use the Web site flysong.com. Song executives hoped that over 70% of tickets would be booked online (vs. 45% for mainline Delta). Prices would have a simple structure, with an everyday-low-pricing policy. Once at the airport, the Diva would have a fairly conventional ground-service experience, though she might note that Song operated with one gate agent rather than Delta's two.

On board, the Diva would take a leather seat in the all-coach cabin and might notice the festive décor of the plane's interior. As of late 2003, her seat would have a personal digital television

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<sup>a</sup> A Gantt chart is a project-planning tool. Each line represents a discrete task that must be performed before the project is complete.

monitor with 24 channels and video games. Though superior to JetBlue's analog television, the Song television service would have a cost comparable to JetBlue's because of technological progress since JetBlue installed its system. The Diva's seat would have 33 inches of legroom, one inch more than on JetBlue and other low-cost carriers. She would notice that Song flight attendants were less conservative and more outgoing than attendants on most legacy carriers—"high style, high fashion, frisky and fun, but not goofy" in the words of one Song flight attendant.<sup>6</sup> In addition to complimentary beverage service, the Diva would have the option to buy food on board. Organic food, for instance, was being prepared under the guidance of gourmet chef Michel Nischan, and branded indulgences such as Snickers chocolate bars would be available. Food prices on board were comparable to airport prices, and gross margins were 25%.

Joanne Smith, Song's vice president of marketing, explained, "We want to be a lifestyle brand, not merely an airline brand."<sup>7</sup> Song's credo echoed that sentiment, repeating the phrase "We are not an airline" (**Exhibit 3**). Marketing material consistent with the brand was being developed for Song's first advertising campaign in September 2003.

**Staffing the airline** Song staffed its flight decks with pilots from mainline Delta, working under the same contract and at the same pay rates as mainline pilots. Flight attendants were employees of Song itself, as were ground personnel at Song's three busiest airports. Invitations to apply for jobs at Song went out to Delta's flight attendants, including the 3,000 individuals who had been furloughed by Delta. (Furloughed employees were mostly ones with shorter tenure at the airline.) One in three applicants received an interview, or "audition," in which his or her personality and ability to "act" were assessed. Seventy percent of interviewees received an offer.

Flight attendants came to Song under two arrangements. Some "renounced their Delta citizenship," in Selvaggio's words, becoming full-fledged Song employees and leaving the seniority rolls at Delta.<sup>8</sup> Others remained on the Delta seniority list and might later "flow back" to the mainline. Once hired, flight attendants attended a three-day training session at a Disney facility. Through discussions with senior managers and games, flight attendants learned the business model of Song, its flexible work rules, its mission and brand, selling techniques, and so forth. During a "party with a purpose," trainees learned from a "mixologist" how to prepare and sell drinks. A wellness session taught attendants how to lift luggage into overhead bins safely; Song flight attendants were encouraged to help passengers with their bags, in part to speed the boarding process. Flight attendants were introduced to their new uniforms, developed exclusively for Song by well-known designer Kate Spade. Finally, the training session featured a performance of the house band "Johnny and the Flourishes," with John Selvaggio on the flugelhorn. In part, said one Song executive, the training was designed to "de-Delta-fy" the new hires.

Flight attendants were paid less per hour at Song than at mainline Delta but were allowed to work more hours. By June 2003, 60% to 70% of flight attendants were working enough hours that they took home a larger paycheck at Song than they would have at mainline Delta.

**Operating the service** Song aimed to lower its costs significantly by flying 757s at high load factors on hauls of roughly 900 miles. The aging 737-200s of Delta Express would be shifted to Delta's overgauged hubs. Seating on board Song's 757s was rearranged to accommodate 199 seats, the maximum allowed with four flight attendants. (A typical Delta 757 flew with 183 seats in two classes and with six flight attendants.) The management team planned 50-minute turnarounds, allowing Song to have its planes in the air 13 hours per day, roughly 20% more than an average Delta mainline 757. Overall, Song hoped that it would ultimately attain CASMs 20% to 30% lower than those of mainline Delta. In total, Song would offer 50% more capacity, or available seat miles, on the Northeast-to-Florida routes than Delta Express had.

**Coordinating with the mainline.** From the perspective of the customer, the connection between Song and Delta was not very visible. Song's passenger check-in desks, plane exteriors and interiors, and gate signage were distinct. Song and Delta shared automated check-in terminals, Song flights were described on gate message boards and in on-board announcements as "operated by Delta," and Song passengers earned frequent-flyer miles in Delta's SkyMiles program. Behind the scenes, however, were more connections. Pilots and flight crews were shared, and pilots operated under the mainline Delta labor contract. Maintenance was performed by Delta personnel. Routes, flight frequencies, schedules, and prices were set by the network and revenue management personnel of Delta, albeit with input from—and in negotiation with—Song's leadership team. Song monitored metrics such as load factors, realized prices, meal purchases, and costs, and Song's management team felt that this gave them the ability to work very effectively with their corporate counterparts. Discussions with corporate were complex, in part because of route overlap. For instance, a passenger could fly from Hartford to Orlando on mainline Delta through Atlanta, on a Delta regional jet, or nonstop on Song.

While connected to Delta, Song enjoyed far more independence than Delta Express had ever experienced. Song managers controlled virtually all decisions related to branding, in-flight experience, and flight attendant management. Headquartered across the street from Delta's corporate offices, the organization was incorporated as a wholly owned but separate subsidiary with its own profit-and-loss statement. The compensation of Song's top management team—as well as that of Delta's corporate managers—was tied in part to Song's profitability.

Fred Reid, COO of Delta as a whole, described coordination between Song and the mainline:

The relationship is reasonably tension free. Even without a separate subsidiary, everything is connected in this business—marketing, operations, planning—everything. Every button you press will set off effects elsewhere. You don't stay in this business unless you have a pretty high tolerance for abstraction and coordination. It's human nature to pursue your own agenda. In fact, we want people to fight for their own agendas, just in a consensual way. At the end of the day, everyone knows that I have absolutely no tolerance for suboptimization. If we have a problem, we sit down with the people and the facts, and we figure out what is best for the company as a whole.<sup>9</sup>

As an example, Reid described the decision of whether to let Song fly into Delta's Atlanta hub, an opportunity that Delta Express never had. "I said, 'Is there a federal law that says a low-fare subsidiary can't fly into an airline's hub?'"<sup>10</sup> Ultimately, Song was granted permission to fly from New York to Atlanta.

Song personnel managed their informal relationships with mainline personnel with care. "Not a day goes by when we don't try to make Delta feel like it's their baby," said David Pittman, Song's vice president of finance. "We've got to make sure Delta people and leaders feel like they gave birth to Song."<sup>11</sup> In Selvaggio's words, "Only Delta could deliver Song."<sup>12</sup>

## Judging Success

Outside analysts estimated that Delta had invested \$65 million to launch Song.<sup>13</sup> Delta and Song executives reflected on how they would judge the success of the investment:<sup>14</sup>

Michele Burns, chief financial officer, Delta: "We'll look at market penetration and ask, have we retained and grown the target segment? And have we done so at a decent ROI? I'd love to

see Song exceed the cost of capital. You'll know that Song is a success if we expand it beyond the 36 aircraft in the initial plan."

Vicki Escarra, chief marketing officer, Delta: "I'll consider Song a success if we have a product that is loved by customers and is considered the airline of choice, if we deter LCC growth, if we reduce costs, and if employees are happy and engaged."

Fred Reid, chief operating officer, Delta: "What do we want out of Song? We want to be big. We want to be powerful. We want to play offense and defense. And we want to make money."

Joanne Smith, vice president of marketing, Song: "The number one test is whether Song has improved Delta's bottom line. We'll know we're on the way to success if we are profitable in 2004 as we plan to be, if we grow beyond 36 planes, and if we begin to realize increases in average ticket prices, that have been steadily declining in recent years."

Subodh Karnik, senior vice president of network and revenue management, Delta: "I'll ask a few questions to figure out if Song was a success. Did it make money and contribute to Delta's bottom line? Did it accelerate the rebuilding of the core Delta product? And did it protect and grow our share in markets and, more importantly, in the cities where it was deployed?"

Leo Mullin, chairman and chief executive officer, Delta: "Song will be a success if we have met the enemy at the gates and driven them back. Short-run profitability is a secondary concern. I want to effectively compete with those low-cost carriers and make them know that they won't pull one over on Delta."

**Exhibit 1** Backgrounds of Song Leaders

**John Selvaggio, President:** more than 30 years of airline experience, primarily at American Airlines (eventually President and Chief Operating Officer of subsidiary Wings West Airlines), Midway Airlines (eventually President and Chief Executive Officer), and US Airways (head of Express division). Joined Delta in 1998 and served as Senior Vice President of Airport Customer Service.

**Tim Mapes, Managing Director of Marketing:** recruited to Delta from Delta's advertising agency, BBDO Worldwide, in 1992. Responsible for international and domestic advertising and promotional efforts. Prior to joining Song, served as Managing Director of Customer Products and Services as well as Managing Director of Delta Express.

**David Pittman, Vice President of Finance:** joined Delta in 1984 and held positions in internal auditing, treasury, cost accounting, domestic and international accounting, and financial reporting. Served as Chief Financial Officer of Delta Technology, responsible for all areas of finance within the subsidiary.

**Joanne Smith, Vice President of Marketing:** previously an officer in marketing and planning divisions of Reno Air, Midway Airlines, AMR Eagle, and Wings West. Joined Delta Song from DHL, where she was Vice President of Marketing and Planning.

Source: Company.

**Exhibit 2** Song's "Discount Diva"

She's married.

She works.

Her husband works.

She has a household income of \$75K-plus (and likely \$150K-plus).

She has kids (likely three).

She values nutrition, has personal style and follows entertainment.

She's busy, doesn't have enough time (she's also tired).

She doesn't want cheap, she wants luxury for less.

She's looking to elevate her family's lifestyle by shopping well (being savvy).

Beyond demography, the core target:

- is extremely discerning.
- wants to be a hero for her family.
- is value conscious.
- loves to shop.
- likes stores like Nordstrom and Neiman Marcus but also shops at Target and Old Navy.
- thinks her favorite brands simplify her life.
- sees style and design as important in providing added value in relatively undifferentiated product categories.

Source: Song executives.

### Exhibit 3 Song's Credo

We are not an airline, we are a culture.

A culture founded by optimists—and built by believers.

We are not an airline,

We are listeners, innovators and technology creators,

We are not an airline,

We are magicians, acrobats and sprinters focused on a single goal: to give style, service and choice back to the people who fly.

That's why we've "cast" our talent—to make sure each and every one is attentive and gracious.

Why we offer everyone 24 channels of real time, satellite TV and CD quality MP3 audio.

Why we handpicked a socially conscious chef—to prepare fresh meals and cater to diverse tastes.

Why Kate Spade designed a collection for our talent, why we created exclusive programming for families, and offer cosmopolitans in the air.

All in all, it's why we offer more. And now it's time to dig deeper.

You see, we realize our difference doesn't lie solely in the choices we offer, but also in how we offer them.

This means paying attention to those subtle, all-important details that give someone or something a certain specialness.

This means understanding that style isn't just about the uniforms we wear, but in how we wear them.

It means remembering not only to say please and thank you—but how old is your son and happy birthday.

It means recognizing that some guests desire a sense of well being and other—a sense of humor.

It's knowing that smiling is contagious, technology is empowerment and that some people like their martini—ice cold—with olives—shaken not stirred.

It's each and every day—in the lobby, the parking lot, on the web site and in the plane—demonstrating that we truly understand the frustrations our guests have with airline travel and exceeding their expectations with choices that are special and surprising.

Here, lies the Song difference.

Because in the end, as we all know, the proof is in the pudding.

And if that needs to be a low fat, organic pudding—so be it.

We are in tune with our guests.

We are not an airline. We are Song.

Source: Song company document.

## Endotes

<sup>1</sup> Leo Mullin, chairman and chief executive officer, Delta Air Lines, interview by author, Atlanta, Georgia, July 15, 2003.

<sup>2</sup> Mark Balloun, vice president of corporate strategic planning, Delta Air Lines, interview by author, Atlanta, Georgia, July 15, 2003.

<sup>3</sup> John Selvaggio, president, Song, interview by author, Atlanta, Georgia, July 31, 2003.

<sup>4</sup> Interview with Mullin.

<sup>5</sup> Interview with Selvaggio.

<sup>6</sup> Amy Diluna, "Fashion in Flight," *New York Daily News*, April 10, 2003, p. 60.

<sup>7</sup> Joanne Smith, interview by author, Atlanta, Georgia, July 15, 2003

<sup>8</sup> Interview with Selvaggio.

<sup>9</sup> Fred Reid, chief operating officer, Delta Air Lines, interview by author, Atlanta, Georgia, July 31, 2003.

<sup>10</sup> Interview with Reid.

<sup>11</sup> David Pittman, vice president of finance, Song, interview by author, Atlanta, Georgia, July 31, 2003.

<sup>12</sup> Interview with Selvaggio.

<sup>13</sup> "Song Song Blue," Unisys R2A Scorecard: Airline Industry Cost Measurement, May 2003, p. 12.

<sup>14</sup> Interviews by author, Atlanta, Georgia, July 15 and July 31, 2003, and by telephone in August 2003.