

## BRAND VALUATION AND LICENSING

Brands and trademarks are valuable intangible assets which, when established and used, are capable of producing revenue in their own right and which can be valued independently of other assets and of management and employees. This chapter contains an overview of applicable brand valuation methodologies for accounting [balance sheet] and other purposes.

### Brands, Valuation and Wealth

It is accepted in the present commercial scenario that brands do create wealth. Maximising brand value is simply a function of maximising shareholder value; a goal that effective managers of all quoted companies recognise. Companies have increasingly come to be recognised and indeed reorganised around brands. Even in classic branded FMCG companies such as Unilever, their importance has been given a higher priority. In their recent reorganisation, premium brands worldwide were specifically named as a key responsibility of the chairman of the operating divisions. This a far from the old model of brand manager control.

Balance sheet issues may have provided the impetus for the development of brand valuation, but its application does not stop there. There is certainly no doubt that more information on brands, brand performance and brand value should be disclosed in financial accounts. Companies are however vary of doing so and of disclosing the kind of information that they feel is competitively sensitive, and unless this is done their statements concerning brands end up appealing 'like idle rhetoric' and of little real use of investors.

Brand valuation can also be used in the planning and structuring of mergers and acquisitions. A significant amount of explicit comment was made by both sides about brand value in the Rowntree/Nestle and Granada/Forte takeovers, with all parties claiming to be able to maximise the value of the brands involved.

A similar role can also be seen in investor relations. Merrill Lynch issued a broker's circular in 1996 that argued that the share price of Burmah Castrol would have to increase by somewhere between 25 percent and 50 percent in order to cover the analyst's estimates of Castrol's 'brand value'. In a similar vein, both P & G and Unilever Annual Reports would not be complete without the (respective) Chief Executives reiterating their commitment to building their portfolios of leading brands. The purpose of such communication can also be focussed for an internal audience, and indeed can be used as explicit benchmarks for performance in rewarding management. Brand valuations of portfolios can also be used to help the crucial task of resource allocation and as a tool for evaluating the success of the decisions made!

Franchising and Licensing transactions, within corporations or with their third parties, are increasingly popular and can also have implications for tax planning. Brand valuations have also been used in supporting negotiations with tax authorities, in supporting court claims for damages in cases of 'passing off' or in defending actions of unfair trading and even in specific use of brands as a securitised asset to back specific borrowing.

Irrespective of its purpose, and recognising that it is only a single measure, it is no exaggeration to say that brand valuation has become an important technique for evaluating businesses. The growing importance of valuation mirrors the growing importance of brands to the companies that own them.

One crucial aspect mentioned is the fiscal implication of charging international/overseas subsidiaries and third-party licensees a proper royalty fee for the use of brands. Organisations worldwide, particularly universities, have yet to realise that the royalty rates they demand are negligible in comparison to the value of the trade mark or service mark asset being licensed. Increasing the royalty rate demanded not only has managerial benefits but also transfer pricing advantages.

This imbalance of power could, be greatly improved in two ways :

- If companies took a more scientific approach to the setting of royalty rates rather than relying on what has been done in the past.
- If companies pooled their royalty rate information so that they were as well informed as the tax authorities with whom they were arguing.

The managerial and fiscal implication of trade mark licensing are profound and that brand valuation has a key role to play in adding method and objectivity to an area which in the past has been plagued by doubt and misunderstanding.

### **BRAND VALUATION: THE ISSUES**

The valuation of brands is a relatively new concept and although brands are bought and sold independently from other business assets, there is no identifiable market in brands as such. Brand valuation is therefore claimed to be in part an art, not an exact science, and necessarily involves judgment. It also involves specialists in three quite separate and hitherto unrelated disciplines – marketing, accountancy and finance, and law. In order to conduct a proper valuation an unusual, even unique, blending of professional skills is therefore required. Also, any methodology must deal both with hard ascertainable factual information (e.g. market shares, sales and profits) as well as rather 'softer' qualitative information and skilled, professional judgement is needed in assessing brand strength and in determining brand-related profit.

The value of a brand as encompassing the particular values attributable to the trade mark, logo, packing and get-up, as well as to the recipe, formulation or raw material mix. In other words, brand value as a term embraces all the proprietary intellectual property rights encompassed by the brand. Thus for the purposes of evaluation a brand has to be understood as an 'active trade mark'; a trade mark actually used in relation to goods or services and which has, through use, acquired associations and value.

The Interbrand methodology, for instance, when used for balance sheet purposes, deals with existing use and does not take account of any unrealized 'stretch' factors (e.g. line extensions or licensing) . Nor is it normally concerned with the break-up value of a company's brands or with the valuation that, under different circumstances, a third party might put on them.

### **ALTERNATIVE SYSTEMS**

When developing an 'existing use' valuation methodology a variety of possible methods have been explored.

#### **Premium Pricing**

This system is based upon the extra price (or profit) which a branded product may command over an unbranded or generic equivalent. However, the major benefits which branded products offer to manufacturers often relate to security and stability of future demand and effective utilization of assets rather than to premium pricing, so premium pricing is rarely an acceptable method of brand valuation. Moreover, a strong brand which the retailer must stock due to customer demand also provides its owner with a platform for the sale of additional products and, at practical level, it should be remembered as well that many branded products (for example, most perfumes) have no generic equivalents and in many instances ( e.g. that of the Mars bar), it is difficult to conceive that a generically equivalent product could be offered at anything like as keen a price as the branded product. Furthermore, selling prices are often related to short-term tactical factors, a factor which makes it difficult to apply any methodology based solely upon this concept. Therefore the value of a brand clearly cannot be determined by premium pricing alone, though evidence of a strong price premium may well serve as a clear indication of brand strength and may therefore play an important part in a valuation.

#### **Esteem**

There have been moves, particularly in the United States, to develop brand valuation methodologies based principally on measures of brand recognition, esteem or awareness. Although the Interbrand methodology recognizes that awareness and esteem can be critical to a brand's success (and are therefore factors to be considered when assessing the overall strength of the brand), to build a model using as its cornerstone such 'soft' measures is inappropriate.

As balance sheets are traditionally drawn up on an historical cost basis it was necessary to consider valuation systems based upon the aggregate of all marketing, advertising and research and development expenditure devoted to the brand over a period of time. This approach was, however, rejected quite quickly; if the value of a brand is a function of the cost of its development, failed brands may well be attributed high values and skilfully managed, powerful and profitable brands with modest budgets could well be undervalued.

### **Discounted cash flow**

The concept of using discounted cash flow (DCF) techniques to achieve a brand valuation is attractive. Strong brands are, in effect, a form of annuity to their owners, so any system which can accurately assess the value of future cash flows is entirely supportable. The problem of DCF lies in its sensitivity; wide fluctuations can arise from relatively minor shifts in inflation and/or interest rate assumptions. This factor, coupled with the range of cash flows which can result from the differing brand development assumptions, means that DCF, although conceptually a strong system, has to be handled with care. Even when these difficulties can be overcome the valuer has the practical problem that he is generally given little time to complete the valuation and often has to satisfy auditors. In such situations modelling techniques using DCF can be hard to apply.

### **Interbrand's 'multiple approach'**

The approach most frequently adopted by Interbrand (and which is now, it must be said, most widely used by others) is an earnings multiple system, i.e. appropriate multiple is applied to the earnings of the brand. Conceptually the system is sound (the arguments which support a discounted cash flow system apply equally to an earnings multiple system) and, practically, the system is robust, auditable and the valuation can be completed in a relatively short time frame, provided always that the requisite marketing, financial and trade mark legal skills are brought together. The system also has the real advantage that it is based upon hard, proven 'auditable' data.

To determine a brand's value, then, certain key factors need to be determined:

- Brand earnings (or cash flows)
- Brand strength (which sets the multiple or discount rate)
- The range of multiples (or discount rates) to be applied to brand earnings.

In addition, it is necessary of course to check whether or not the brand owner has, in fact, title to the brand and also the quality of this title.

A vital factor in determining the value of a brand is its profitability or potential profitability, particularly its profitability over time. However, to arrive at a balance sheet value it is not enough merely to apply simple multiplier to post-tax profits. Firstly, not all of the profitability of a brand can necessarily be applied to the valuation of that brand. A brand may be essentially a commodity product or may gain much of its profitability from its distribution system. The elements of profitability which do not result from the brand's identity must therefore be excluded. Secondly, the valuation itself may be materially affected by using a singly, possibly unrepresentative year's profit. For this reason, a smoothing element should be introduced; generally, a three-year weighted average of historical profits is used.

The following issues must therefore be taken into consideration in calculating brand earnings:

### **Determining brand profits**

Since it is the worth of the brand to the business which is being valued it is important that the profit on which this valuation is based is clearly defined. For balance sheet purposes this profit must be the fully absorbed profit of the brand after allocation of central overhead costs but before interest charges. Taxation is, of course, also deducted, as will be explained later. For the purposes of evaluating the brand, interest costs are ignored since the basis of funding chosen for the brand is irrelevant to the brand's performance. (Were interest to be included in the calculation, the valuation could be materially affected by changes in corporate financing arrangements; as such arrangements are generally not brand-related they are normally excluded when determining profit).

The elimination of private label production profits. The profits to which an earnings multiple is applied must relate only to the brand being valued and not to other, unbranded goods which may be produced in parallel with the brand but which are not sold under the brand name. These profits may be separately identified by the company through its accounting systems; alternatively, judgment may need to be exercised in assessing the extent of such profits based on production volumes, sales values or other acceptable methods. Insofar as 'allocation' is at the heart of much accountancy, the elimination of 'own label' profits has been found to be entirely feasible.

### **The restatement of historical profits to present-day values**

Since historical earnings from the basis of the valuation these values must be re-stated to present-day figures by adjustments for inflation. This has the effect of ensuring that performance is reviewed at constant levels

A weighting factor is applied to historical earnings so as to determine a prudent and conservative level of ongoing profitability to which to apply an appropriate multiple. Thus once historical profits have been adjusted to present-day values a weighting factor must be applied to each year's brand profits which reflects the importance of those profits to the valuation. In many cases a simple weighting of three times for the current year, twice for the previous year and once for the year before that is used. These aggregate earnings are then divided by the sum of the weighting factors used.

### **Provision for decline**

There is a basic accounting rule that benefits should only be taken when they are earned, but that losses should be provided for as soon as they are known. This rule further implies that, in a brand valuation for balance sheet purposes, future brand profitability must be reviewed so as to see whether the profits on which the valuation is based will be maintained. Where the weighted average historical earnings are clearly below the forecast brand profits in future years, no provision for decline is necessary, provided of course that the forecast is reasonable and can be justified. However, it may be necessary to review the weighting allocating if forecast future earnings are significantly in excess of the weighted average profit value and are expected to remain at this level in the foreseeable future. It could well be, for example, that historical profits may have been depressed by factors now brought under control and it may be appropriate therefore to place greater reliance on more recent earnings when arriving at a valuation. Where, however, the weighted average earnings are greater than the forecast future brand profits, a provision for decline may be necessary to reflect the reduced level of future profitability.

### **Remuneration of capital**

For the purposes of a valuation, to apply a multiple to all the profitability of a brand potentially overvalues that brand. Not all the resulting capital sum can be attributed to the brand itself – some of it necessarily reflects the value of the other assets employed in the line, e.g. the distribution systems, the fixed assets, and the management. Or, put another way, if one fails to deduct a suitable return for the other assets employed on the brand there will, arguably, be double counting on the balance sheet.

There are several ways of identifying and eliminating earnings that do not relate to brand strength but the most frequently system is that of charging the capital tied up in the production of the brand with the return one might expect in the production of the brand with the return one might expect to achieve if one was simply producing a generic. Such an assessment obviously requires analysis and judgment, but as a general rule the non-brand-related returns one would expect in an industry where brands play a relatively insignificant role (e.g. heavy engineering) will be greater than those where brands are critical to success (e.g. cosmetics or fragrances). Provided one is dealing with the current cost of assets of real return in the 5-10 per cent range is normal and can be used as a capital remuneration figure.

The multiples we use are applied to the brand's post-tax profit figures. Therefore it is vital that all the reported earnings are collected on the same basis. A tax rate is normally applied which is the medium-term-effective tax rate forecast for the company.

## **BRAND STRENGTH**

The determination of the multiple (or the discount rate in the case of DCF valuations) to be applied to brand profit is derived from an in-depth assessment of brand strength, as it is brand strength which determines the reliability of a brand's future cash flow. The assessment of brand strength requires a detailed review of each brand, its positioning, the market in which it operates, competition, past performance, future plans and risks to the brand. The brand strength is a compromise of seven weighted factors, each of which is scored according to clearly established and consistent guidelines. These key factors are as follows:

**Leadership.** A brand which leads its market sector is generally a more stable and valuable property than a brand lower down the order. The score highly in the area of leadership a brand must be a dominant force in its sector with a strong market share. It must therefore be able to influence its market, set price points, command distribution and resist competitive invasions.

**Stability.** Long-established brands which command consumer loyalty and have become part of the 'fabric' of their markets are particularly valuable and are normally afforded high scores.

**Market.** Brands in markets such as food, drinks, and publishing are prima facie stronger than brands in, for example, high tech. Or clothing areas as these markets are more vulnerable to technological or fashion changes. A brand in a stable but growing market with strong barriers to entry will thus score particularly highly.

**Internationality.** Brands which have proven international acceptance and appeal are inherently stronger than national or regional brands. Significant investment will have been incurred in the geographical development of such brands and they are less susceptible to competitive attack. They are, therefore, more robust and stable assets. Moreover, by no means all brands are capable of crossing cultural and national barriers so those that are must be considered as particularly valuable assets.

**Trend.** The overall long-term trend of the brand is an important measure of its ability to remain contemporary and relevant to consumers, and hence of its value.

**Support.** Those brands which have received consistent investment and focused support usually have a much stronger franchise than those which have not. While the amount spent in supporting a brand is important the quality of this support is equally significant.



Protection. A registered trade mark is statutory monopoly in a name, device, or in a combination of these two. Other protection may exist in common law, at least in certain countries. The strength and breadth of the brand's protection is critical in assessing its strength. Indeed, if the legal basis of the brand is suspect it may not be possible to apply a value to the brand at all for balance sheet purpose.

## **VALUATION APPLICATIONS**

It is perhaps important to examine technical aspects of valuation for balance sheet purposes, both of 'home grown' and acquired brands. There are, of course, many other situations where brand valuations can usefully be used and where the same basic methodology can be applied. The assessment of the strength of the brand, for example, is unlikely to change greatly whatever the situation (and this is the area of the valuation process which normally requires the most detailed and time-consuming investigations) though attributable brand earnings, and the appropriate multiple could vary considerably.

It should also be noted that even when the valuation is based upon notional royalty rates or upon discounted future earnings it is first necessary to identify brand earnings and review carefully the reliability of future income flows. In other words, the key elements of this methodology – the assessment of brand earnings and of brand strength – need to be followed whatever procedure is used to derive a valuation.

## **VALUATION AND LICENSING OF INTELLECTUAL PROPERTY**

The licensing of technological know-how and patents has been long-established and it is accepted that often significant royalties should be paid by licensees for the use of such assets. Moreover, the agreements governing such licenses are often very complex and recognise that the maintenance of the value of the intangible asset is an important task and is the duty of both the licensor and the licensee. Until recently, however, trade mark licenses were not treated as seriously and indeed sometimes were just added in as the 'icing on the cake' of patent/technology licenses. But the increasing awareness of the value of brands has prompted brand owners to wake up to the notion that, although intangible, such properties do have significant value and that their licensing cannot be regarded as a mere formality.

One of the first effects of this is that license agreements with third parties now pay much more attention to the fact that the property being licensed is valuable. Higher royalty rates are being demanded (and justified) and stricter conditions to ensure that proper use and maintenance of trade marks - both in legal terms and in marketing terms - are put in place. For example, licensees will often now participate with the brand owner in the development of global advertising campaigns and the design of visual identity programme. It is only in this way that the integrity, and thus the value, of a brand can be safeguarded.



But trade mark licenses are not only being used with third parties. Many companies (of which Nestlé is the most famous example) have a policy of owning all intellectual property centrally and charging subsidiaries for its use. Thus, for example, even though many of the brands acquired as part of Rowntree are purely British brands (Quality Street, After Eight, etc.), they are all now owned by the Swiss company and licenses back to the English company. This has a number of implications:

- Use of brands in controlled centrally and directed to the benefit of the whole group and not just of a subsidiary.
- The maintenance of brand rights - such as registering and renewing of trade mark registrations, policing, prosecuting infringement and passing-off actions - is co-ordinated and carried out consistently across the world rather than being left to the interests or abilities of local management.
- The licensing of brands, and the charging of brand royalties, rescues brands from the closed world of the marketing department and makes their value the responsibility also of financial and legal departments. Their position as an asset of the company - rather than a toy given to amuse a junior Brand Manager for a few years - is crystallised.
- International brands, whose marketing may be shared by more than one company within a group or even by more than one division, are centrally co-ordinated to ensure maximum coherence in terms of brand image, product development, advertising, etc. (e.g. Philip Morris' management of the Marlboro brand).
- Brands can more easily be extended into new areas and licensed to other subsidiaries while firm control is still kept on the integrity of brand equity (e.g. Nestlé's extension of the Aero brand through Chambourcy).
- Operating companies are made aware that the brands they use are as much a shared resource, and a property of common value as, say, research laboratories, recipes and patents.
- Country managers can be made responsible for the local maintenance and development of a global brand. Their contribution to brand value is after all a contribution to shareholder value and should be rewarded accordingly.
- Internal licenses, whether within the home country or overseas, increasingly incorporate the payment of a royalty which reflects the true value of the asset being used rather than just being a nominal amount to 'cover administration'. Making a financial charge for the use of a trade mark (or other intellectual property) focuses the user on the value of the asset and the need both to protect and exploit that value.

- The royalties received from licenses to overseas subsidiaries can be used to repatriate funds in return for the use of a genuine piece of property. This can have major fiscal implications.
- New licenses negotiated within the group, with joint venture partners and outside the group, can be placed in a context of genuine brand licensing and realistic royalty rates giving the opportunity to negotiate much higher returns for the use of brands than has been the case commonly in the past.

Brand valuation has made a critical contribution in all of these areas both in raising awareness of the concept of brand value and in putting a monetary value to a brand. Insisting that a brand has value is one thing; being able to state what that value is is the best way to make the maintenance and development of that value part of company strategy. It also helps to communicate to the outside world that the company takes its brands seriously.

One field in which brand valuation and the concept of brand value is beginning to have an impact is the area of trademark licensing. In the recent years there has been a marked increase in the attention given to the licensing of trademarks as well as other intellectual property such as copyright, patents and designs.

The notion of a license is a simple one: the owner of a piece of property allows another party to make [commercial] use of that property in return can expect some form of compensation. The party [individual or commercial entity] issuing the license is called the licensor; the party receiving the license is called the licensee.

Licences need to define a number of elements, especially the following:

- The element of property to be licensed [for example, the right to use the trademark, Orange].
- The entity to whom the property is being licensed [for example, the local education centre now entitled to term itself an NIIT franchisee].
- The geographic extent of the licence [for example, only in India, or a particular state, states or region].
- The commercial extent of the licence [for example, only for the manufacture and distribution of a particular product or class of product].
- The duration [for example, for a period of five years from the date of the licence].

Because of the desire of the owner of the property to safeguard what is being licensed and ensure that the licensee does not undermine its value, licences usually include strict provisions covering quality control for both production and marketing, reporting of performance, collaboration with licensor and other licensees and conditions for termination.



Licenses will also define in one or more of a variety of ways the manner of calculating and remitting compensation. 'Royalty' is assessed as a percentage of sales, mostly as a percentage of gross profit or net profit. Often maximum or minimum amounts are stipulated, and also the rate may decrease or increase with volume on a sliding scale.

It is also important to recognise that the amount of a pure royalty may be reduced or eliminated by the use of other means of gaining compensation for the use of the brand: a management fee, an extra contribution to advertising and promotional expenses, the rent on a retail site or the price of a raw material that the licensee is obliged to purchase. For example, agreements between Coca-Cola and its third-party bottlers does not require an explicit payment for the use of the 'Coke' brand. Instead the licensee will be required to purchase the essential sticky brown concentrate for making a Coke-branded cola at a given price and in certain minimum quantity.

Though the payment for these products may appear to be for a tangible transfer, it is clear that the amount that can be demanded is influenced as much by the trademark rights that go with the product as by the qualities of the products themselves. It is only by buying these ingredients or products that the licensee can make use of the brand, and so the charge for the use of the brand is hidden within the charge for buying the tangible elements.

#### **VALUATION METHODOLOGIES: A SUMMARY**

One of the core considerations in valuation is 'brand strength': the commercial viability of a brand based on the positive touchpoints and experiential goodwill. Brand Strength is based on attempts to access the relevant beliefs, associations and attitudes that are in consumers' minds:

The explanation of the whole branding phenomenon put great emphasis on the meanings and associations that a brand can create in the mind of the consumer. In other words, the obvious place to anatomize the strength of a brand should be the consumer's mind.

David Aaker, visualizes each brand name as a 'box in the consumers brain', in which are stored away all the bits of information and associations to do with that brand. The whole box is then in turn stored with positive or negative feelings. This is as good an image as any, although like all metaphors for how the mind works it is likely to be too simplistic and we can try to gather about what goes on the consumers mind:

- I. Awareness – whether there is a box for our brand there at all, or whether it is easy to find.
- II. Associations and beliefs – what is in the box? This is a big area in itself with many dimensions to it.
- III. Attitude – how the consumers feel about a brand, positive, negative, indifferent.



Each of these areas can be interpreted to tell us more about an aspect of a brand's strength.' One could say a brand is strong because many people have heard of it or spontaneously think of it, one could certainly say it is strong if many people express great loyalty or affection for it. In their words and actions. Most importantly, a brand can be called strong if it is strongly associated with imagery or functional benefits that we interpret as desirable for consumers.

Brand Strength is based on attempts to estimate the brand's future performance and profit streams, and thus put a financial value on the brand as corporate assets:

There is perhaps, a thin line between asking someone to rate a brand on 'quality' and asking them to express a degree of personal preference for it, but this represents a shift from the respondent's perception of the brand to one about their relationship with the brand.

Ultimately, the bottom – line relevance of all the perceptual material described in the preceding section is that it somehow translates into customer behaviour – it leads to them buying the brand, staying with the brand, perhaps paying more for the brand.

Brand valuations will only even be credible if they are based on reliable forecasts, and reliable forecasts must be informed with statistical valid historical data relationships. When accompanied by sensitivity analysis they indicate the most likely parameters of a brand's performance. When forecasts are backed up with robust evidence, using for example, econometrics modelling data or correlation analysis, valuations become a credible addition to management decision-making.

In recognition of this, the use of market research tracking data to link 'soft ' marketing measures with 'hard' financial measures is one of the fastest growing areas of market research.

#### Brand Equity Tracking Data

Marketing research tracking is an approach that monitors consumer perception of brands via sample based surveys.

Internationally, there are three main sources of the 'brand equity' research:

- i) custom design studies, offered by research supplier firms;
- ii) advertising agencies, many of which have invested in the development and execution of 'brand equity' research;
- iii) proprietary system, developed specifically for the purpose of measuring brand equity, by suppliers with a particular commitment to this field of research.



Proprietary systems are represented by summaries of projects/valuation methods of the developers of prominent valuation techniques, some of which include software:

BrandDynamics from Millward Brown

Brand Building from the NPD Group

Brand Equity Tracking from Tandemar

It should be noted that the following descriptions were obtained from the agency or research firms concerned and are derived from their literature on the subject, including analysis available on the respective web sites.

Young & Rubicam: the Brand Asset Valuator [BAV]<sup>™</sup>

Y & R decided upon a knowledge acquisition strategy that would enable the firm and its operating companies to provide clients with the best brand-leverage opportunities. As part of the implementation of the strategy, the largest worldwide surveys of consumer brand perceptions were undertaken in the Summer of 1993 and Spring of 1998.

The process of building brands, BAV demonstrates, is reflected through a progression of four primary measures:

Differentiation

Relevance

Esteem

Knowledge

These measures are used in BAV to evaluate current brand performance, to identify core issues for the brands, as well as to evaluate brand potential.

Brands can be evaluated by these individual measures. But more important, the relationships between the pillars show the true picture of a brand's health, its intrinsic value, its muscular capacity to carry a premium price and its ability to fend off competitors.



The starting point for all brands is Differentiation. It defines the brand and distinguishes it from all others. Differentiation is how brands are born.

As a brand matures, BAV finds that Differentiation often declines. It doesn't have to happen. Even after reaching maturity, with good management, a brand can perpetuate its Differentiation. A low level of Differentiation is a clear warning that a brand is fading.

Relevance as the next step

Differentiation is the only the first step in building a brand. The next step is Relevance. If a brand isn't relevant, or personally appropriate to consumers, it isn't going to attract and keep them – certainly not in any great numbers.

BAV shows that there is a distinct correlation between Relevance and market penetration. Relevance drives franchise size.

### **Brand strength**

A brand's Relevance and Differentiation viewed in relationship represent Brand Strength, which is a strong indicator of future performance.

Relevant Differentiation – remaining both relevant and differentiated – is the central challenge of every brand. It is critical for all brands all over the world.

The basis of esteem

BAV's third primary measure is Esteem – how much consumers like a brand, hold it in high regard. In the progression of building a brand, it follows Differentiation and Relevance. It's the consumer's response to a marketer's brand – building activity.

Esteem is related to two factors: Perceptions of quality and popularity. The proportions of these factors differ by country and culture.

BAV tracks the ways in which brands gain Esteem, which helps us consider how to manage consumer perceptions. Through BAV, one could identify opportunities for leveraging a brand's Esteem.

### **Knowledge is the successful outcome**

If a brand has established its Relevant Differentiation and consumers come to hold it in high Esteem, Brand knowledge is the outcome and represents the successful culmination of building a brand. Knowledge is not a consequence of media weight alone. Spending money against a weak idea will not buy knowledge. It has to be achieved.

As Brand Strength was found between Relevance and Differentiation, Brand Stature is discovered in the combination of Esteem and Knowledge.

Brand Stature indicates brand status and scope – the consumers response to brand. As such, it reflects current brand performance and is a strong strategic indicator. For example, Esteem rises before Knowledge for a growing brand. If the data shows the opposite relationship, a problem has been identified.

The BAV points out the wisdom of looking at brands in the entire brand landscape, which will lead us to consider new possibilities for the brand, rather than risking the dangers of a narrow vision of the category. The overarching truth here is that, properly managed brands can exist eternally. And BAV gives us the diagnostic framework to help our clients build, leverage and maintain the power of their brands.

### **Millward Brown: Brand Dynamics™**

BrandDynamics measures and explains a brand's consumer equity – consumers' predisposition towards a brand as distinct from other factors that contribute to the brand's financial equity (e.g. distribution strengths, production, efficiencies, patents etc.)

BrandDynamics provides both consumer equity measurement and the diagnostic understanding to inform tactical and strategic decision-making. BrandDynamics is built on over 20 years of continuous brand health tracking research and 8 months of R&D investment. Key measures are validated against sales.

Launched in 1996, customized BrandDynamics studies have been completed over 1300 brands in 15 categories across 19 countries. In 1998 one single study looked at 8 – 10 brands in each of 50 categories in 7 countries around the world – providing a data base on over 3500 brands by markets.

The functioning of Brand Dynamics

This is a research-based measure, built on 4 key components:

- The consumer's predisposition toward the brand – their likelihood of purchasing that brand next, share of requirements (for packaged goods)
- The size of the brand – big brands achieve more sales for any given level of consideration (i.e. consumers' consideration 'underestimates' actual purchasing of big brands)
- The type of consumer – Are they more attitudinally disposed to brands, or do they see the category as a commodity where price is the key issue?



- The brand's relative price (i.e. consumers' consideration 'overestimates' actual purchasing of expensive brands)

These four factors can be combined together in a mode to predict the likelihood of each consumer buying the brand – a respondent level prediction of brand loyalty. Then category expenditure data is added to provide consumer value – which is strongly correlated with value market share.

For categories where sales data are unreliable or unobtainable, Consumer Value is of significance in its own right as a valid indicator of sales. Some clients place more faith in consumer value than market share which can be distorted by promotions.

The importance of having a validated, respondent – based measure is to explain why some consumers are more valuable than others. This is done via five equity building blocks which form a Brand Pyramid. Consumers at each level of the Brand Pyramid can be targeted via advertising and other marketing activity. BrandDynamics provides specific and practical diagnostics – driven marketing guidance.

### **Presence**

The first step is to stimulate active knowledge of the brand – Presence. By active knowledge we mean unaidedly aware, have tried brand, or an endorsement of the brand on key image dimensions which show they have an understanding of what the brand promises.

### **Relevance**

To get to the next level the consumer has to feel that the brand could meet their needs – and do so at an acceptable price for them. Relevance can be thought of as a hurdle that the consumer has to pass over before a stronger relationship with the brand can be developed.

### **Product Performance**

The brand does not have to be better than its competitors. But it does have to offer an acceptable level of product delivery. If a brand has a genuinely superior product and consumers are aware of this, then this will form a brand advantage.

### **Advantage**

Many brands may be acceptable, but for the brand to be more valuable to the consumer it needs some form of 'perceived advantage'. This can be a direct extension of some unique aspect of the product delivery; however in many categories brands have little genuine product differentiation. For these brands, softer aspects such as saliency, emotional appeal, personality and popularity can provide the advantage.



## **Bonding**

The more the consumer feels that the brand is the only one that offers key advantages within their repertoire, the greater the bond between the consumer and the brand, and the more loyal they are likely to be.

The pyramid is the starting point for the analysis of the brand's strengths and weaknesses. For example, we can see below that Brand A has a similar level of presence, relevance and product acceptability as Brand B, but has higher advantage and much higher bonding.

## **Source of Revenue**

Does position in the Pyramid matter? Certainly. As might be expected, Bonded consumers typically generate a disproportionate share of the brand's revenue. As shown below, Brand A's revenue comes primarily from Bonded and Advantage groups. The generic brand gains much of its business from consumers who stumble across the brand in store and by it on price – consumers for the generic has no Presence.

## **Brand Strength**

Future revenue is an important component of a brand's equity; it demonstrates how a brand's market share is underpinned by the consumer's predisposition toward certain brands. While Consumer Value tells us about the worth of the brand now, it is not a measure of market share robustness, i.e. brand strength. However, a brand's conversion profile does provide a measure of its relative strengths and weaknesses.

Based on the results from the initial BrandDynamics studies, three main types of pyramid profiles were observed. These are shown below. The profile on the left shows the brand to have relatively high Presence and Relevance, but relatively low advantage and bonding. In contrast, the middle profile shows the brand to be low at presence and relevance – but once past these hurdles to have a relatively high conversion to Performance, Advantage and Bonding. The third profile is one where the brand is positive all the way up the pyramid (with the possible exception of Relevance) – particularly at Performance, Advantage and Bonding.

## **Summary**

BrandDynamics provides both a validated measurement of consumer equity and the diagnostic understanding to inform tactical and strategic decision-making. And, it does this in a way that is readily accessible to senior marketing professionals.

## Background

BrandBuilder was created in 1992 in order to address a variety of questions of strategic importance to brand marketers: What's happening in my category? Why is it happening? How to create and maintain the consumer loyalty to my brands necessary to grow them, extend them, shield them from competitive threat, thus making them – and keeping them- profitable? At the heart of every successful brand is a core franchise of loyal buyers for whom the brand satisfies high proportion of their needs. These behaviourally loyal buyers often account for a disproportionate amount of the brand's share and profits, as they seek out the brand – and purchase it repeatedly – even in the face of competitive pressure.

### The Link between Attitudes and Behaviour

Not all repeat buyers are equally committed to the brand. Some hold beliefs about the brand that are consistent with their loyal purchase behaviour; they are the brand's "core" franchise. Core consumers are truly committed – behaviourally and attitudinally – to the brand.

Others hold attitudes that are out of synch with their observed behavioural loyalty to the brand. We call those with attitudes less positive than their purchasing behaviour "vulnerable", because their repeat purchasing is tied too strongly to price, or the attitudes that drive their behaviour are important to few category buyers, making the brand vulnerable to competitive offerings. Conversely, growing/strong brands typically "own" critical attributes among consumers that are not yet buyers. These "prospects" often become loyal buyers to the brand over time.

The essence of BrandBuilder, then, is to identify and size these buyer groups via a unique modelling process that fuses survey data with behavioural data, and to identify the specific dynamics and attributes that drive brand loyal behaviour.

### Attributes driving brand loyalty

It is not sufficient to merely determine which brands are strong, and which are weak. In order to provide information to help brand marketers shift their brands' positioning in the proper direction, it is vitally important to ascertain the specific attributes that drive behaviour at three levels:

- (1) At the category level,
- (2) At the segment/form/usage occasion, demographic group level, and
- (3) At the brand level.



On the other hand, it is generally unnecessary, and may even be inaccurate; to ask consumers to rate the importance of attributes themselves. It is far better to derive the importance of attributes indirectly, through the measurement of behavioural loyalty on the one hand, and consumer's associations of specific characteristics of attributes with brands on the other. The BrandBuilder model uses a logic regression procedure to determine the key drivers of behaviour at each of these three levels.

#### Key Principles on What Drives Behaviour

The attitudes measured must be tailored to the category, and must include all key dimensions.

The larger the brand, the more likely it will be that the category drivers and the brand drivers are the same. A brand that "owns" unimportant attributes can be described as a "niche" brand. A "niche" brand can also be a "strong" brand, provided that the base of consumers "driven" by its attributes is growing, or if its share of that niche grows over time.

#### Category Equity

In order to arrive at a complete view of the client's proper strategy, it is also critical to determine the extent to which the category itself is strong or weak. The BrandBuilder defines category equity as follows:

##### Category Equity Definition

The tendency of buyers in the category to buy based purely on brand

Preferences ("Brand Driven") on price along ("Price Driven"), or to

Expect to be able to buy their favourite brand, and still get an attractive

Price ("System Beaters").

##### **Some Category Loyalty Principles**

Consumers are driven by Brand preferences in some categories, and price in others; very few are Brand Driven, or Price Driven, across categories.

Historical patterns of marketing spending (e.g. high advertising spend), product quality differentiation, and strong brand imagery, can all move a category into the "high equity" quadrant.

Conversely, high levels of promotion spending, or erosions in product quality/perceptions/differentiation, are likely to move categories into the System Beaters quadrant, or into the Price quadrant.

It is easier to leverage a brand into a related category, than to category than to category distant to it; if the target category has a similar pattern to the base category, consumer expectations in the 2 categories will assist the brand transfer.



Despite the category's pattern, an individual brand's buyers may act differently; a brand may be Brand Driven in a Price category or Price Driven in a Brand Driven category.

### **Validation evidence**

In order to validate the predictive relationship between attitudes and behaviour, an R & D study was conducted. It is discussed in detail in a series of Journal of Advertising Research articles (Baldinger and Rubinson, 1996, 1997). It was found, in this work, that strong brands tend to increase in market share from one year to the next, while weak brands tend to decline in share.

In summary, BrandBuilder addresses the key branding questions:

How many loyal buyers exist, at the category, segment and brand level?

What are the key attitudinal drivers, in the category segment and brand?

Which brands are strong, and which are weak, based on their patterns of behaviour and attitude? and

What changes should be made in brand positioning, the product itself, or marketing support, to improve the health of the brand?

### **Tandemar: Brand Equity Tracking Program™**

Tandemar launched its Brand Equity Tracking program, with a focus on brand health measurement, based on extensive exploratory research and validation work.

Tandemar's Brand Equity Tracking program provides both attitudinal and loyalty measures to quantify a brand equity score, and is supported by a strong set of diagnostic measures to tell you what communication strategies will work or will not work to strengthen the equity of the brand.

Tandemar has conducted Equity Reviews in over 50 different sectors in Canada, and has an extensive database of Canadian norms and case studies to draw on for analysis purposes.

Tandemar's Brand Equity model is an evaluative framework which provides a way of assessing the overall strength of consumer attitudes towards a brand. It is quantifiable, measurable, and consistent from category to category. Canadian norms are available, based on hundreds of case studies.

The parameters of the model are based on the learning from several international studies (including market mix modelling), and have been supported by our own large scale study of Canadian brands. Uniqueness and relevance are key brand delivery components, while familiarity and knowledge are rooted in the salience of the brand to consumers. The interaction of these dimensions indicate brand strength of 'health' brand opportunities and brand vulnerability. These dimensions have been proved to correlate with purchase loyalty in a variety of international studies, and have been validated by Tandemar in a large-scale quantitative study in Canada.

There are many different proprietary approaches and systems for measuring 'brand strength' and 'brand equity'. In this chapter, certain key resources have been highlighted, but there are numerous other, less well known approaches. Their validity is to a great extent dependent upon the nature, complexity and structure of the market, whether it is a Consumer or Business to Business market and whether the product or service is a frequent or an infrequent purchase.

In 'fast moving consumer goods' markets consumers tend to have a repertoire of brands, which are often almost interchangeable, and the 'share of requirements' for a particular brand may vary for a whole range of relatively unpredictable reasons. By contrast, in many financial or 'durable goods' markets purchase frequency is very low and inertia is a massive influence on sales.

With many of these studies the number of respondents limits segmentation of the sample results while timing of the research can affect the validity of the conclusions.

Therefore, there is no one brand equity tracking model which is a 'world beater' in all categories. Before approaching the consultant involved, the client should consider a number of factors.

- Why the final information is required
- The level of details of the information required
- The timescale in which the information is required
- Whether static or rolling data is required
- The amount that they are prepared to spend on the report
- The level of reliance they are prepared to place on the results

The key to success of the models described is arguably to marry simplicity and user-friendly with a detailed and intensive information gathering engine. Category segmentation is a key. The ideal model inevitably analyses a brand's strength by segment i.e. by geography, by lifestyle, by personality or by organizational associations.

### **David Aaker: Managing Brand Equity**

David Aaker advocates a flexible approach to brand equity evaluation which he calls the Brand Equity Ten.

He identifies what he believes to be the ten key aspects of brand performance which illustrate the components of brand strength. He recommends that brands should be scored against the following template.

Loyalty Measures

#### 1. Price Premium

Measuring the additional price that consumers are prepared to pay for a brand. For example, a structured questionnaire may be used to establish the relationship between cost and stated consumer preference for a number of similar goods. Or empirical evidence may be available to demonstrate from historical data the actual relationship.

#### 2. Satisfaction/Loyalty

Researching the customer's level of satisfaction with a brand and the level of price sensitivity allows the market to be segmented into 'loyal users, price chasers and those in between.'

Perceived Quality/Leadership Measures

#### 3. Perceived Quality

Statistical models can be used to correlate perceived quality and financial measures such as returns on investment and stock return. The changes in perceived quality scores can be measured across a variety of different sectors, allowing a comparison of relative brand health.

#### 4. Leadership / Popularity

Leadership scales attempt to measure whether the brand is "a category leader, is growing more popular or is respected for innovation".

### **Associations / Differentiation Measures**

#### 5. Perceived Value

This measures whether a brand represents value for money and whether consumers have a reason to choose one brand over its competitors. In the latter sense it is a similar measure to perceived quality.

#### 6. Brand Personality

This is a particularly important factor where there are apparently only minor functional differences between different brands in a market. Brand personality "says something" about the consumers of different brands. The soft drinks market is an example of this. There may be little discernible difference in taste between Pepsi and Coca Cola, so the marketing functions in each company concentrate their efforts upon differentiating the products through image.

#### 7. Organizational Associations

Brand strength often goes beyond the product brand to the corporate brand which underlies it. For example, companies might seek to gauge how consumers react over time to statements such as:

This brand is made by an organization I would trust.



I admire the brand X organization

I would be proud (or pleased) to do business with the brand X.

Awareness Measures

#### 8. Brand Awareness

A simple measure of the distinctiveness of a brand's personality and the effectiveness of its advertising and communication campaigns. Loyalty and purchase build from this platform. Performance relative to competitor brands is a key indicator of brand health.

Market Behaviour Measures

#### 9. Market Share

Measuring a brand via market share can be a clear indicator of consumers' perceptions and satisfaction with that brand. A falling market share is usually a good indicator that the brand is slipping in the consumers' estimations, although distinctions clearly need to be made between volume and value share.

#### 10. Market Price and Distribution Coverage

Brand strength can be measured by distribution percentage. Unlike market share these measures are easier to define and are less subject to short term blips that may be caused by price promotions.

Measures like the percentage of shops stocking the brand, and the brands accessibility to the percentage of consumers, are often used to judge a brand's performance.

Aaker's recommended approach to brand equity evaluation, outlined in more details in his book 'Building Strong Brands' (Free Press Business, First Edition, 1996), focuses principally on consumer-oriented measures of brand strength, although it also looks at market oriented measures.