Brand Valuation: Measuring and Leveraging your Brand

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BRIDGING THE GAP BETWEEN MARKETING & FINANCE™

Brand Valuation: **Measuring and Leveraging your Brand**

A report prepared for the
Institute of Canadian Advertising

Prepared by
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Foreword

"It is now uniformly accepted that companies which are good at marketing produce better results over time for their shareholders than those which aren't. It is our firm belief that the essence of good marketing is the development and promotion of long term brands.Brands add intangible value to products and businesses and redefine the value of their company owners.

A new recognition of the financial value of brand assets is now emerging in company boardrooms and on Bay Street.While the brand owner must take ultimate responsibility for brand fortunes, and the role of the advertising agency in creating and sustaining brand power should not be underestimated.

The debate around brand valuation is a healthy one, in so far as it puts brand discussion firmly on the Boardroom agenda. It can also serve as a useful background to strategic and brand planning and control.In exploring these issues, we are sure that this new ICA booklet will prove invaluable.

David Harrison, Chairman ICA

Rupert Brendon, President ICA

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Brand Finance is a specialist consultancy dedicated to the better understanding of marketing finances. It is entirely independent and offers a highly professional approach to marketing accountability and brand valuation. Brand Finance has developed transparent and accessible brand valuation methodologies grounded in leading-edge marketing and investment practice.

Services designed to maximize value in marketing and branding include brand audits, brand equity research,brand performance forecasting, brand valuation, brand portfolio review, budget allocation strategy, agency remuneration, accounts payable and production cost audit,and advice on related information technology and training.

Brand Finance works for a wide range of blue-chip clients conducting national and international brand valuation and strategy assignments. Sectors covered include food, confectionery, alcoholic drinks, automotive, telecommunications, oil, banking and insurance, chemicals,and leisure/ retail.

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David Haigh read English at Bristol University before qualifying as a Chartered Accountant with Price Waterhouse in London. He worked in international financial management then moved into the marketing services sector, firstly as Financial Director of The Creative Business and then as Financial Director of WCRS & Partners.

He left to set up a financial marketing consultancy which was later acquired by Publicis, the pan European marketing services group, where he worked as a director for 5 years. He moved to Interbrand as director of brand valuation in its London-based global brand valuation practice, leaving in 1996 to launch Brand Finance.

David is a fellow of the UK Chartered Institute of marketing and was a member of the 1998 IPA Advertising Effectiveness Awards judging panel.

He is author of 'Strategic Control of Marketing Finance (FT/Pitman Publishing 1994), 'Brand Valuation - a review of current practice' (IPA, 1996), 'Brand Valuation' (FT - Retail and Consumer Publishing, 1998) and 'Understanding the Financial Value of Brands' (EAAA, 1999).

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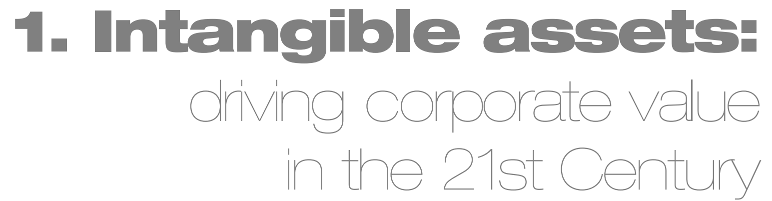


1. Intangible assets:
driving corporate value in the 21st Century

Marketers have been committed to building brands for more than a century. However, operating efficiency and financial performance were the preferred measures of performance in board rooms and investment houses during the bulk of the 20th century. This was an understandable approach in an era when product differentiation was achieved in factories and the bulk of a company's value was reflected by its fixed assets. The era passed, but the financial and operating focus remained.

Advertising budgets increased as communications mediums became more powerful and numerous. This trend was exacerbated by technological developments which resulted in a greater range of similar products, and the resulting difficulty in functional differentiation. The growing budgets were a tacit acceptance that 'advertising works', yet it was not accepted as being at the core of a business by those in control of the purse strings. The shift in the relative importance of tangible and intangible assets escaped the attention of the accounting profession and most investment analysts.

Marketers were silent accomplices to this omission. They focused on their own functional area of expertise, confident in its importance, and measured their performance in terms that were not appreciated by the broader commercial community. Investors and accountants remained unimpressed by measures of brand strength which were measured in perceptual rather than financial terms.

In the late eighties many investment analysts and fund managers were still basing investment decisions on traditional measures of financial health, principally earnings per share, dividend yield and balance sheet asset values. Such measures can fundamentally misstate corporate value.

The main impetus for an acknowledgement of the value of brands, and other intangible assets, came from the corporate raiders and asset strippers of the eighties who targeted brand rich companies and paid significantly more than their net asset value. This resulted in huge 'goodwill' values which had to be accounted for. Alarm bells rang in the boardrooms of many under-performing branded goods companies as directors realized there was a clear need for a method of accounting for brands which would recognize their true value in the balance sheet, and avoid arbitrary write-offs which damaged investor perceptions.

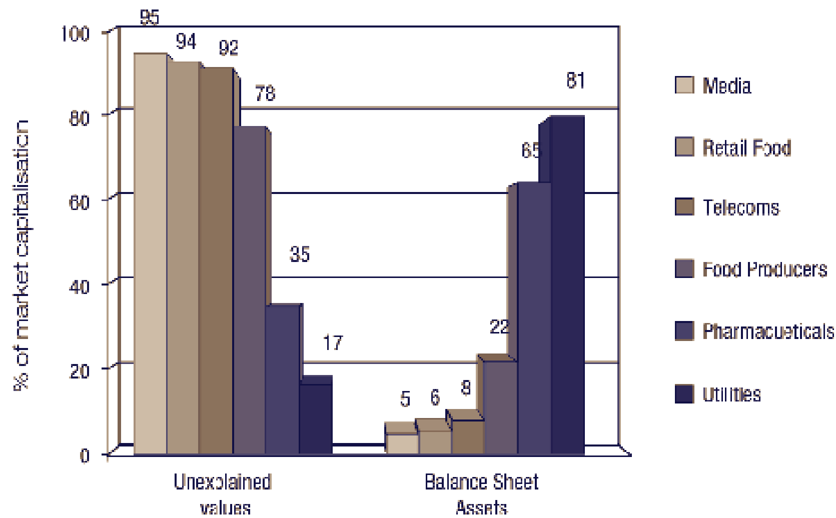
A realization that the full value of brand owning companies was neither explicitly shown in the accounts nor always reflected in stock market values led to a reappraisal of the importance of intangible assets in general, and brands in particular. This in turn raised the question of how such assets should be valued and disclosed. Although the accounting profession has only partially adapted to a world in which intangible assets are the main drivers of value, business leaders and investors have been quicker off the mark.

There is currently a global merger and acquisition boom in progress. Brands have played a significant role in this activity. Mannesmann, for example, has agreed to pay nearly US$20 billion for a mobile phone brand that has only been in existence for five years. Within its home market Orange boasts higher customer acquisition, retention and usage rates than its rivals – all key factors of a successful brand. Orange has achieved that magic ingredient which positions it as a lifestyle brand. It has already been licensed into new geographies and is tipped to move into other product categories.

Instances such as this bring the value of specific brands into the public domain, but the bulk of intangible asset value remains 'off balance sheet'. A recent research study carried out by Brand Finance indicates that brands and other intangible assets now contribute the bulk of shareholder value in many sectors. This UK based study reviewed the annual reports of 344 of the FTSE 350 companies with year-ends up to and including 31st December 1998.

It seems bizarre that 72% of the value of the companies surveyed was not reflected in published balance sheets. This percentage varies considerable by sector highlighting the varied importance of intangible assets between sectors.

Gap between FTSE 350's market capitalization and net asset value at 31/12/98



Brands form a significant part of this 'unexplained value'. Other intangibles such as patents, customer lists, licenses, know how and major contracts also play a role. Patents, for instance, are a major component of value in the pharmaceuticals sector.

Brands will be major drivers of corporate value in the 21st century. Investors and business leaders have recognized this. Marketers are increasingly using brand valuation models to facilitate marketing planning.They should go one step further. Investors need and want greater disclosure of brand values and marketing performance.Marketers should play a lead role in ensuring that such information is adequately communicated to investors, rather than waiting for statutory disclosure requirements to catch up with reality.

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2. Recent developments
in brand valuation

During the last five years,brand valuation has become a mainstream business tool used for the following purposes:

- Merger and acquisition planning
- Tax planning
- Securitised borrowing
- Licensing and franchising
- Investor relations
- Brand portfolio reviews
- Marketing budget determination
- Resource allocation
- Strategic marketing planning
- Internal communications

A particular trend has been the increasing use of brand valuations as a tool to aid marketing management. The focus here is to increase the effectiveness of the marketing effort and aid brand management. A prime benefit in this regard is the fact that a brand valuation model is linked to the company's business model and provides a financial measure that is understood throughout the organization and by investors.

A well-constructed brand valuation pulls together market research, competitive data and forecasts of future performance. This increases the understanding of the brand's value and its contribution to demand in each segment and identifies opportunities for leveraging the brand. A dynamic brand valuation model can be used for scenario planning purposes.

The ability to place a financial value on a brand within each key market segment is not the only output of a valuation study:

- Research into the drivers of demand yields information that aids a range of decisions, including portfolio planning and product positioning. It can help define the focus of the advertising message.
- An identification of causal relationships within the business model facilitate an increase in advertising effectiveness.
- The competitive benchmarking study that forms part of an assessment of the risk attached to future earnings provides a gauge of the brand's strength, in relation to competitors, from segment to segment.

Some examples of internally focused brand valuations that Brand Finance has carried out during the last two years are shown below.

The first example illustrates the use of a brand valuation to help resolve a specific issue. The impetus for the project had been the acquisition by a global financial services company of a number of new brands. This had resulted in a cluttered portfolio which required rationalization. The brand valuation was segmented by product and customer for all of the group's brands in the UK, Europe,Australia, Hong Kong and the US. The project formed the framework to inform brand rationalization and brand architecture decisions.

In the case of a retail bank, a brand evaluation project was carried out in order to assess the contribution of the brand in the corporate, as opposed to the consumer, market segment. The study was also segmented by major product groups. Consumer research was commissioned to quantify the drivers of demand. The study impacted on the allocation of marketing resources between market segments and was applied to measure the effectiveness of marketing investment.

A global insurance company provides an example of a valuation initially carried out for a specific purpose, but that has now been repeated. In this instance, brand valuation and competitor benchmarking techniques were combined to determine the optimal global advertising investment behind the client's corporate brand. The results were used by senior management to set corporate advertising levels. Periodic repetition of the exercise has been used by management to understand and monitor the effect of brand investment decisions on corporate brand value.

In the case of a listed food manufacturer, a brand valuation was conducted in order to communicate the value of the company's main brand to analysts and investors. Management commissioned the study as they believed the shares were undervalued and the company vulnerable to takeover.

A major tobacco company illustrates the use of a brand valuation model on an ongoing basis. The corporate marketing finance team commissioned the constructing of a brand evaluation model to monitor the performance of key client and competitor brands in local markets and at a global level. The brand valuation has been placed on the company's intranet and is supported by a manual which

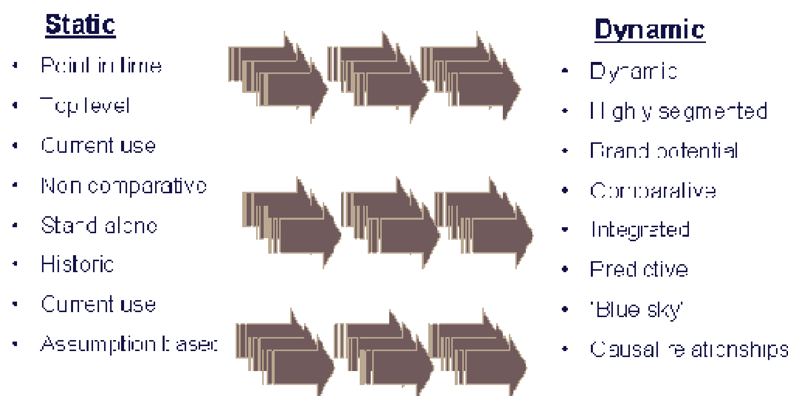
clarifies what information is required to be inputted into the model and how the results can be used.The model is kept up to date by operating companies in sixty countries.The data produced by the model informs local decision making as well as group planning.

These examples show the range of internal uses of brand valuation studies. Further discussion in this regard is provided in section 5.1 of the report.

Many organizations suffer from a surplus rather a than lack of market and consumer information. Unfortunately much of this is gathered and stored in isolation.The old functional boundaries of a bygone era still prevent the effective flow and integration of information. Even if brand tracking data makes it onto the intranet or a shared directory, it tends to remain in ‘research speak’ and tends not to be used by financial and strategic planners.

A successful brand valuation project relies on input from both the financial and marketing teams of a company. It will result in a model that gathers and integrates market, consumer and financial data.The integration of such data into a coherent business model, and the fact that the data sources are ‘cross functional’ make it significantly more useful,and more used, than each of the data sources in isolation.

It must be stressed that the depth and extent of a brand valuation can vary. This is illustrated by the following diagram.



One of the key differences between a static and dynamic valuation model is the extent of consumer research that is used. The simpler valuations only focus on research which enables an assessment of the brand’s contribution to the purchase decision to be made. Dynamic brand valuation models require a more detailed understanding of the consumer’s relationship with the brand. This allows causal relationships within the business model to be identified and quantified. Dynamic brand valuation are discussed in section 4.

The brand valuation model should provide a central framework for a marketing information system.

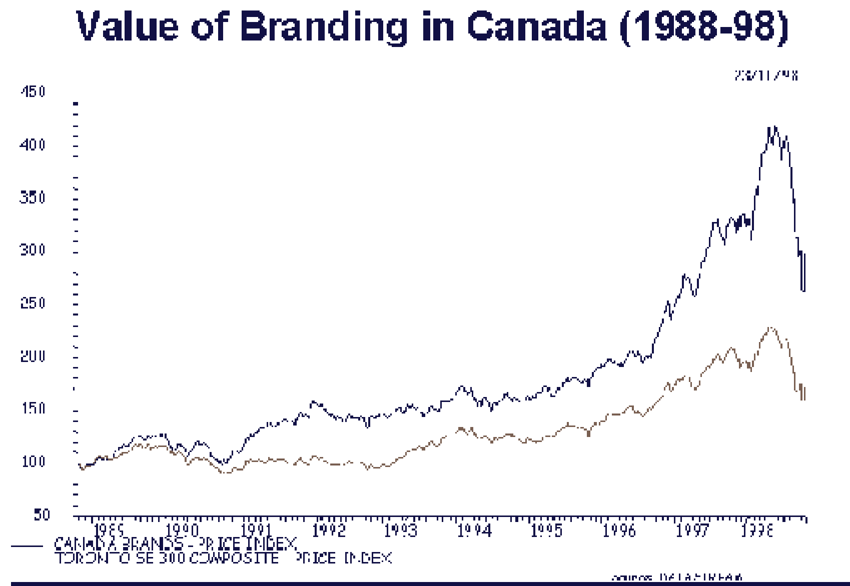
All data within the brand valuation model, as well as the outputs, should be easily accessible either at a top level or through a ‘drill down’ facility.

If a brand valuation model is being used for ongoing tracking purposes it is essential that responsibility for inputting new data is clearly designated. It is usually necessary to have both marketing and finance involvement in this, however, in some organizations a single ‘home’, for instance the marketing finance team, is found.

This is not to say that a well constructed brand valuation meets all the information requirements for marketing decision making. Qualitative research and tools such as perceptual mapping will always be necessary. A brand valuation model often provides inputs to other marketing tools and processes.

3. Brand economics:
how brands add value

As illustrated by the following chart, heavily branded companies have a history of outperforming the Canadian market.



A similar performance gap between heavily branded companies and the market index is apparent in the US and UK.

How do brands add value? In economic terms the answer is simple.They impact on both the demand and supply curves.

On the demand side brands enable a product to achieve a higher price at a given sales volume. Strong brands can also increase sales volumes and churn rates. Price and volume impacts are in some instances achieved at the same time. An example, taken from the Economist, is of the GEO Prizm and Toyota Corolla in the US. These vehicles are virtually identical, coming off the same production line and having similar levels of distribution and service levels. However, the Corolla trades at an 8% premium and sells double the volumes.

Brands also establish more stable demand, through their relationship with consumers.They establish barriers to entry. The relationship with consumers is due to both functional and emotional attributes. On the functional side brands ensure recognition and further aid the purchase decision through a guarantee of quality. From an emotional perspective they satisfy aspirational and self-expression requirements.This is most evident in luxury and fashion sectors.

A further benefit of branding which has increased in importance in recent years,is the ability to transfer the equity or values associated with a brand into new product categories. In order for brand stretching to be effective, it is necessary that the core values of the brand are image, rather than product, based.

Whilst there are numerous examples of successful brands that have achieved significant price premiums or higher volumes,the impact of branding on the supply curve is often ignored. Brands tend to shift the supply curve downwards due to the following reasons:

- Greater trade and consumer recognition and loyalty. This results in lower sales conversion costs and more favorable supplier terms.
- Lower staff acquisition and retention costs.
- Lower cost of capital.
- Economies of scale achieved through higher volumes.

There is an increasing body of research supporting the fact that successful brands add corporate value. There are, of course, examples of successful brands that have fallen from grace and branding initiatives that have failed.The challenge is to identify how your brand,or your client's brand, impacts on the business model, and to monitor whether marketing strategies are successful in adding value to the brand.

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4. Best practice
in brand valuation

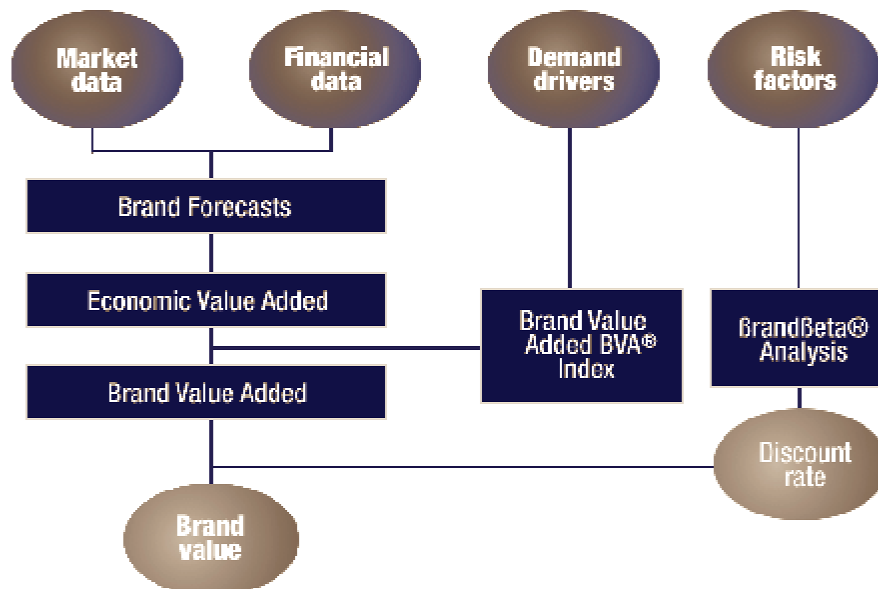
A number of methods can be used to value brands.Cost based brand valuations are rarely used as the cost of creating a brand tends to have little similarity to its current value. Market based comparisons, on the other hand, are unsatisfactory as a primary method of valuing a brand because comparative data is scarce and brands are unique.However, where available, market comparisons are useful for testing primary valuations.

A more commonly used approach is the royalty relief method.This is based on the assumption that if a brand has to be licensed from a third party brand owner, a royalty rate on turnover will be charged for the privilege of using the brand.By owning the brand such royalties are avoided.The royalty relief method involves estimating likely future sales and then applying an appropriate royalty rate to arrive at the income attributable to brand royalties in future years.The stream of notional brand royalty is discounted back to a net present value – the brand value.

Although the royalty relief method is technically sound, it provides little understanding of how and where the brand is creating value. It might therefore be an appropriate method of valuing a brand for balance sheet or tax purposes,but will be of limited use to a marketing director wishing to leverage the value of a brand.

The economic use method integrates consumer research and competitive analysis with the brand's forecast earnings.As such it provides a foundation for brand management in addition to determining the value of the brand by market segment.As this method is of most interest to marketers, and is the most widely used method of brand valuation, it is discussed in more detail.

The Brand Finance methodology has been used by leading brand owners across the world and will be used to illustrate a marketing orientated valuation. A snap shot of this valuation framework is provided below:



The focus is on the return earned as a result of owning the brand – the brand's contribution to the business, both now and in the future.This framework is based on a discounted cash-flow (DCF) analysis of forecast financial performance, segmented into relevant components of value.

The DCF approach is consistent with the approach to valuation used by financial analysts to value equities and by accountants to test for impairment of fixed assets (both tangible and intangible) as required by new international accounting standards.

For some purposes market base valuation or the royalty relief method of valuation may be possible. However, DCF valuation is the most widely accepted approach to brand valuation and provides a greater depth of understanding of the dynamics of the brand.

While brand valuations can be based on a multiple of historical earnings it is clear that past performance is no guarantee of future performance and that investors base value judgements on expected future returns rather than actual historical returns. However, historical results are crucial for accurate valuation mainly because they provide information and data relationships which help to more accurately forecast the future.

Valuations based on projected earnings are therefore our preferred approach with the caveat that forecasts must be credible. Where forecasts are credible the valuation results are both robust and actionable.

A brand valuation study typically consists of four work streams:

- Financial forecasts
- Brand Value Added BVA® - analysis of the brand's contribution to demand
- ßrandßeta® analysis - determination of the risk attached to future earnings
- Valuation and sensitivity analysis.

The BVA® section of the analysis can be extended to incorporate a study of causal relationships within the business model.This facilitates the development of a dynamic brand valuation model, as discussed in section 4.6.

Prior to commencing these studies it is necessary to decide on the most appropriate level of segmentation.

4.1 Segmentation

In applying the valuation framework one of the first and most critical tasks is to determine the nature of the segmentation for valuation purposes. It is then important to identify how internal financial and marketing data, and external market and competitor data, can be obtained in a way which fits with the chosen segmentation.

The principles behind effective segmentation for brand valuation purposes are as follows:

- Homogeneous geographic, product and customer groupings to ensure that the valuations are relevant to defined target markets.
- Clearly definable set of discrete competitors in each segment to ensure that we are comparing apples with apples.
- Availability of market research data to match the chosen segmentation.
- Availability of volumetric and value data for competitor brands to match the chosen segmentation.

There is little point in choosing a valuation segmentation based on an aggregation of product or customer groupings which obscures important underlying differences.

Equally, there is little point in choosing a particular detailed segmentation against which it is impossible to obtain volumetric or value data to the appropriate level of detail. Without these it may be hard, if not impossible,to estimate relative market shares and to compare performance and forecasts against competitors.

Much of the success of a brand valuation lies in the selection and planning of the relevant segmentation and the sourcing of suitable data.

A dilemma in relation to customer segmentation is that below the broad categories lie many more specifically defined demo, socio or psychographic sub-segments. The marketing and market research teams may well want to ‘drill’ down to a more detailed level for NPD or communications planning purposes while the valuation may need for practical reasons to be cut at a higher, more aggregated level. It is often impossible to sub-segment the financial valuation to the same level of granularity that may be desirable for a market mapping segmentation. The brand valuation team therefore needs to ensure that the segmentation for the valuation cascades up from a more detailed underlying segmentation if one is used.

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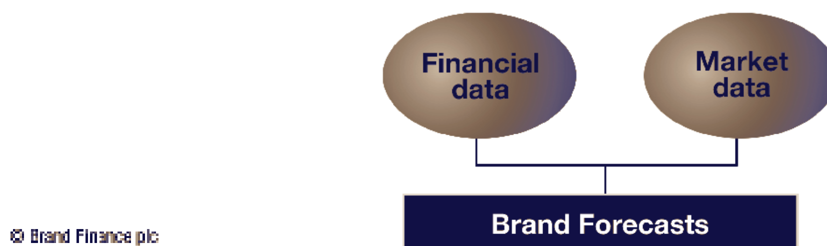
Another difficulty in relation to product segmentation is that volumetric or value measures for each product group may be hard or impossible to obtain particularly in less well developed or defined product and service areas or countries. It is also common to find that in some client segments it is hard to obtain reliable data for total market size, as competitor data may be unavailable. A pragmatic approach and a medium term strategy to populate data gaps may be required, allowing subsequent years valuations to have an increasing level of detailed comparative analysis.

The difficulties of selecting and populating the chosen segmentation with data have been noted to highlight the need for care and experience in planning and constructing the brand valuation.

4.2 Financial Forecasts

Typically, explicit forecasts for periods of 3-5 years are used for such valuations and should be identical to internal management planning forecasts.



An important part of the brand valuation process involves ensuring that forecasts are credible.

Forecast revenues

Macro-Economic Review
It is necessary to conduct extensive due diligence on each of the markets in which the brand operates to ensure the valuation takes into account all the macro-economic factors likely to affect the level of demand for the brand.These could be technological, structural, legislative, cultural or competitive.

The brand valuation exercise needs to consider the likely trends for both volume and value for the market as a whole and for the brand being valued.This often involves detailed discussion between the brand valuation team and internal competitor analysis, corporate strategy, market research and marketing departments.

Micro-Economic Review
It is necessary to consider the factors that have historically affected the performance of the brand in each of its markets.

This can involve econometric modeling or some other form of statistical analysis of past performance to show how certain causal variables have affected revenues.

One of the key issues in terms of branding is to understand the causal relationship between total marketing spend,pricing and sales results. It is equally important to understand the relative effect of different media on the overall level of sales.

The task of the brand valuation team is therefore to ensure that brand and marketing factors are being accounted for properly in the modeling and analysis taking place, and that results are used to obtain the most appropriate forecast sales values.

In the same way that it may be desirable to use econometric analysis of past influences on sales it may also be appropriate to use projective price elasticity research to predict the effect of price on sales.

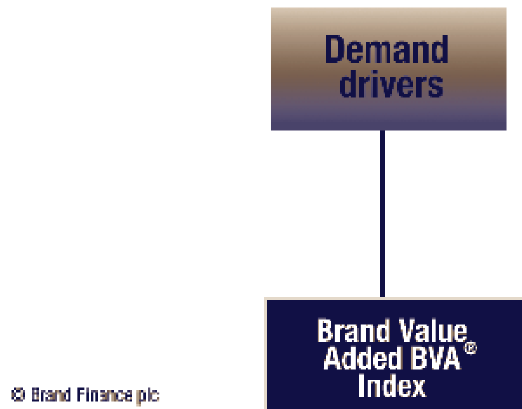
Price elasticity modeling of this type is typically based on large sample quantitative research and is used to improve the accuracy of future sales forecasts. To the extent that this is not already being done we recommend that this should be considered as an input to the brand valuation process to help refine forecast earnings.

Forecast costs

It is necessary to understand fully the basis on which forecast costs have been determined.The brand valuation team will need to confirm that the basis of cost allocation is sensible between each of the geographic, product or customer segments on a current and forecast basis.

The same principle applies to the allocation of capital to different segments and the resulting charges for capital made against the segmented brand earnings streams to arrive at forecast Economic Value Added. Economic Value Added is the starting point for the brand valuation. A proportion of the identified Economic Value Added is ultimately attributed to the brand in the brand valuation calculation.

4.3 Calculating Brand Value Added BVA®



This is the heart of any valuation as it determines the proportion of total Economic Value Added to be included in the brand valuation.

Having selected an appropriate segmentation and populated it with comparative volumetric,value and market research data, we next need to identify, for each of the competitor brands under review, the extent to which the brand contributes to demand. We do this with trade-off analysis based on quantitative market research.

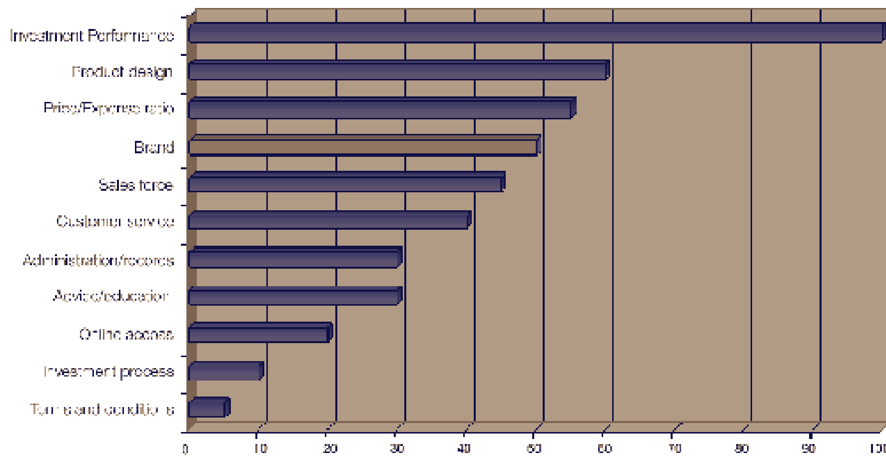
It is usual to first identify the key drivers of demand by reference to existing qualitative and quantitative research or by means of management discussions. It is possible to reasonably estimate the relative importance of different factors in determining demand by means of detailed management workshops.

However, it is preferable to eliminate the inherent subjectivity of this approach by using large sample customer based research.It is ultimately more robust for justifying a financial valuation and more useful as a barometer of the relative importance of different factors which drive sales demand. It is therefore more useable as a line management decision-making tool rather than simply a valuation technique.

A top level illustration of the output of this approach follows. This indicates the contribution of the brand to the purchase decision in a US mutual funds business.

Drivers of demand

Example: Mutual Fund Brand A (11% Brand Contribution)

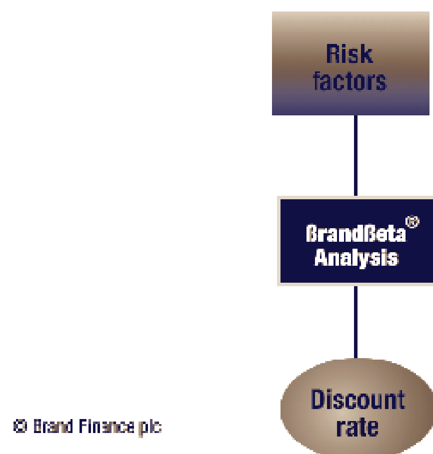


Trade-off analysis of this type can be conducted at a number of levels to identify the importance of the brand to the purchase decision from:

- one brand to another,
- one time period to another,
- one target audience sub-segment to another and
- one product class to another.

It is an invaluable,statistically robust means of attributing income to the brand in a brand valuation. In addition, it can be used for tracking the changing importance of different drivers in given markets,for planning resource allocation behind different drivers of demand and for tracking the effect such resource allocations may have on the profile of factors affecting demand for the brand. It can also be used to assist in anticipating future demand.

4.4 Assessing Brand Risk



The final step in the brand valuation is to determine the appropriate discount rate to use in the DCF analysis. At Brand Finance we have developed an approach to discount rate determination which is a transparent adaptation of the Capital Asset Pricing Model. We build up the appropriate discount rate from first principles as follows:

- Discount rate = [ßrandßeta® adjusted cost of equity x (proportion of equity funding)]
  + [cost of debt x (proportion of debt funding)]

- ßrandßeta® adjusted cost of equity = risk free rate + (equity risk premium
  x sector beta x ßrandßeta®)

The 10 year risk free borrowing rate in the geographic market under review is the starting point. The equity risk premium is the medium term excess return of the equity market over the risk free rate. This can be obtained from investment data providers and a number of risk evaluation services. So too can the sector beta which is used to determine an average implied discount rate for all brands in the sector under review.

This sector specific discount rate is finessed to take account of the relative strength of different brands in the given market. We call this ßrandßeta® analysis and base it on 10 key criteria for which data is usually available and which in our view represent the best indicators of risk.

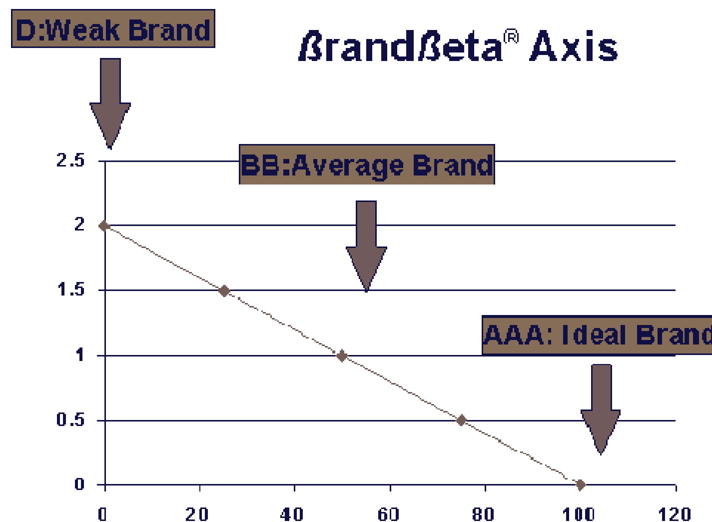
The generic list of ßrandßeta® attributes used by Brand Finance is shown below. It must be stressed that these are evaluated in each instance to ensure the most appropriate grouping of risk measures for a specific sector is identified.

A standard ßrandßeta® scoring template:

Attribute	Score
Time in the market	0 -10
Distribution	0 –10
Market share	0 –10
Market position	0 –10
Sales growth rate	0 –10
Price premium	0 –10
Price elasticity	0 –10
Marketing spend	0 –10
Advertising awareness	0 –10
Brand awareness	0 –10
Total	**0 - 100**

Careful planning will be required to define which competitors need to be monitored and evaluated and in which sectors. There may also be a need to change the competitor set over time if the focus of the business shifts into new areas.

A score of 50 implies that the brand offers average investment risk in the sector under review and therefore attracts a ßrandßeta® of 1. This means that the discount rate used in the valuation will be the average composite rate for the sector.



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A score of 100 implies a theoretically risk free brand which would be discounted at the risk free rate. A score of 0 implies a particularly weak brand which doubles the equity risk premium.

The review of data for the ßrandßeta® analysis provides invaluable insights into the competitive position of the brand in its market and acts as a useful focus for a balanced scorecard for the brand.

Where available perceived quality of brands is a strong alternative to simple 'brand awareness' in the ßrandßeta® scorecard.The scorecard is data driven, transparent and produces supportable discount rates.

4.5 Point-in-time valuation

The result of the foregoing analysis is a Branded Business Value for each segment identified. The Branded Business Value expresses the full net present value of the intangible earnings in each segment. In addition, we produce a detailed competitive review with risk scoring and a robust estimate of the contribution the brand makes in each segment. This is used to drive a value for the brand alone within the total value of the branded business.

We typically also produce a sensitivity analysis indicating the impact on value of altering certain key assumptions.

An important philosophy behind a brand valuation exercise is that the model should become a simple and comprehensible rallying point for the whole brand team not a sophisticated model for the initiated only.

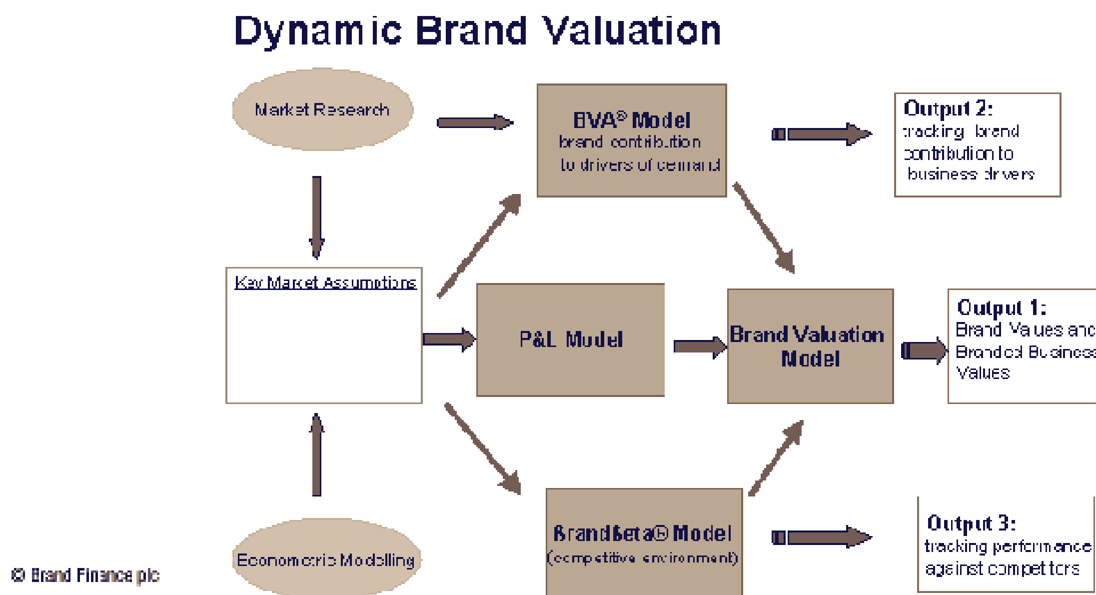
Example valuation sheets for both Branded Business Value and Brand Value are as follows:

Branded Business Value (Segmented)

		Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Net Sales		500	520	550	580	620	650
Operating Earnings		76.0	73.0	82.6	87.0	93.0	97.5
Tangible Capital employed		250	300	275	290	310	325
Charge for Capital @ 15%		37.5	39.0	41.3	43.5	46.5	48.8
Earnings		37.5	39.0	41.3	43.5	46.5	48.8
Tax Rate		33%	33%	33%	33%	33%	33%
Tax		12.4	12.9	13.6	14.4	15.3	16.1
Post tax Earnings		25.1	25.1	27.6	29.1	31.2	32.7
Discount Rate		15%					
Discount Factor		1.0	1.15	1.32	1.52	1.75	2.01
Discounted Cash-flow			22.7	20.9	19.2	17.8	16.2
Value to year 5		96.8					
Annuity		108.3					
Growth	0%						
Enterprise Value		205.1					

4.6 Dynamic brand evaluation

A dynamic valuation process can be expressed pictorially as follows:



The point-in-time valuation methodology discussed thus far provides a robust point in time brand valuation model drawing directly on financial, analytical and market research activities which either are or should be in place already. In a sense it merely brings together existing measures and processes in a coherent way.

It is therefore a suitable way of producing valuations on a periodic basis by and for internal management. In our experience it is often preferable to create a static valuation model, then increase the sophistication of the model and introduce a scenario planning capacity.

The section of the report entitled 'Brand Economics' discussed how brands can result in price premiums,increased volumes, reduced churn rates and cost savings. It concluded by stating that the challenge is to identify these relationships and to track whether marketing strategies are successful in adding value to the brand.

This is the purpose of a dynamic brand valuation model. To incorporate causal relationships into a brand valuation model; use the model to carry out scenario planning in order to select the most appropriate strategy, and then track the impact of the selected strategy.

Such a model can be used for considering and comparing the level of marketing investment behind the brand in different segments. It can be used for flexing key assumptions on the basis of hypotheses and testing the value impact of changes to brand activities. It will show where brand and corporate value is being created and destroyed together with the intermediate measures that cause the growth or decline.

Econometric modeling and Brand Value Added (BVA®) research are used to identify historic and predictive cause and effect relationships between marketing inputs and sales volumes. Both these and market assumptions can be built into a dynamic brand evaluation model in such a way that the likely impact of marketing actions on short term profitability and long term value can be established.

Such a tool sounds like the marketing holy grail, however, it must be remembered that the predictive ability of the model will only be as good as the research that has been used to determine the causal relationships. Even in the absence of ideal research, we have found that the process of estimating cause and effect relationships and assessing the sensitivity of the business model to changes in these assumptions to be an extremely useful process.

5. Applications of brand valuation

5.1 Strategically orientated brand evaluations

Portfolio review and brand architecture

Portfolio reviews have a tendency to become clouded by emotional and subjective factors.The overriding consideration should be the identification of the portfolio that maximizes shareholder value. Once this has been determined, strategic implications can be considered.A brand valuation model will allow the profit and value implications of all options to be considered.

Case Study: Financial Services

A global financial services company which had acquired a number of new brands through a corporate acquisition used brand valuation to rationalization their brand portfolio.

The brand valuation was segmented by product and customer for all of the group's brands in the UK, Europe, Australia, Hong Kong and the US.

The project formed the framework to inform brand rationalization and brand architecture decisions. It identified the strength and value of each brand in all market segments.This provided a quantified basis for restructuring the brand portfolio.

Resource allocation

As brand valuation has become a widespread measure of management performance,so it can produce relevant quantitative data that provides common ground for marketing and finance departments. This assists in budgeting decisions and provides a movement away from a reliance on short term variables or intuition to a more systematic basis for decision making.

Understanding brand values can also be useful in managing portfolios of brands. For example when allocating advertising budgets between brands, launching new brands, setting discount policies or extending brands to new territories.

Case Study: Fazer

Fazer is a large Finnish confectionery company with a wide portfolio of brands. As the trade barriers between Finland and the EU were brought down in the wake of Finland's entry into the EU it became clear that Fazer's portfolio of brands would need to be reviewed to compete in the new era of pan-European competition.

A review was needed to identify 'strategic' and 'tactical' brands and to identify which geographical markets offered the best potential value enhancement for the total Fazer portfolio.

Over a number of years Fazer consistently applied brand valuation methodologies to its portfolio to help identify which brands should be invested in most heavily, which would be allowed to continue and which might more profitably be discontinued. On the international stage Fazer wanted a consistent benchmark for deciding which European markets offered the greatest potential.

The brand valuation process was built into a brand value management information system which was used as the basis for negotiation between sales, marketing and financial personnel and as an input to the strategic planning process.

Performance tracking

Brand valuations are increasingly being used as a management tool. Strategic use of brand valuation techniques is becoming more prevalent in many blue-chip organizations allowing senior management to compare the success of different brand strategies and the relative performance of particular marketing teams.

Case Study: Grand Metropolitan

Prior to its recent merger with Guinness to form Diageo Grand Met had a portfolio of brands including names as prominent as Smirnoff, Baileys, Haagen-Dazs,Green Giant and Burger King.

In 1988 Grand Met had shocked the financial world by including its acquired brands as intangible assets on its balance sheet. Being so rich in name brands it was little surprise that senior management appreciated their importance to the long term health of the organization and wished to reflect this in the company accounts. The 1988 balance sheet included brands with a cost of £608m.

To the board of Grand Met the fact that a series of expensive and high profile acquisitions might not have been included in the accounts seemed an absurd contradiction and would have left the company perilously undervalued.

An anomaly remained. Only acquired brands were included on the balance sheet despite the obvious value to Grand Met of its internally generated brands. Similarly, early valuations were based on historical earnings multiples, a method not currently seen as accurately reflecting the true worth of a brand.

Grand Met's response to this problem and evidence of a real bridge being built between marketing and finance functions was the introduction of its "brand equity monitor". The purpose of this was not to place a historical value on a brand, but to give management an idea of the performance of brands. The factors measured could not be measured in purely profit and loss terms and the monitor included both economic, consumer and perceptual measures of performance,which together formed a subtle and responsive mechanism for tracking both brand health,and if necessary financial brand value.

The process has been extended from its early beginnings and Diageo now monitors a number of key financial and marketing drivers to establish the level of brand equity. These drivers focus management's attention on gaining customer awareness, loyalty, market share and the brand's ability to charge a price premium. It is this premium which communicates the value of a brand to the company's stakeholders.

There are a number of checks used by Diageo staff to assess the trends in brand equity. A sample of these measures includes awareness,advertising spend, market penetration and share of display.

Management is able to gauge the relative health of brands from a flow of consistent and reliable data. The fact that the vast majority of this data will never be included in the company accounts is irrelevant, it provides instead a degree of strategic and operational control over the group's most valuable assets.

The catalyst for these developments was the need to adequately reflect,from solely a financial reporting perspective, the value of brands.

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Case Study: Telecoms

Brand Finance recently carried out a brand evaluation project for a global telecoms company. The project focused on the company's home market and had the following objectives:

- to understand the role of the brand by customer and product segments,and against key competitors
- to develop a tracking and evaluation model to assist the drive towards a customer-orientated, brand-conscious culture
- to provide a financially robust value for the brand,for the purposes of internal communications and for comparison with a brand valuation carried out two years previously.

The financial valuation was of less significance than developing an understanding of how and where the brand was adding value to the company, and how this could be leveraged.

Given the rate of change within the telecoms market the issue of market segmentation was essential in order to develop brand strategies appropriate to and for the future.The evaluation was segmented by product categories within customer type.The brand evaluation model consisted of three work studies, namely:

(i) Competitive Analysis

In order to determine the competitive profile of the brand,and the risks attached to future earnings,a competitive benchmarking study was carried out in each market segment.Although the client collected a significant amount of competitive data, this had not previously been collected and analyzed in such a systematic manner. Ten attributes were used to measure and track competitive performance; these were specifically determined for each product segment.

(ii) Consumer Research

A trade-off research study was used to determine the Brand Value Added (BVA®).This is a measure of the brand's contribution to earnings. The trade-off data was analyzed to determine the weighting of the drivers of demand.In other words, the relative importance of brand,price, inertia, reach and several service attributes was determined.The brand contribution, and other driver weightings,were compared across market segments and with key competitors. Service driver weightings were compared to consumer ideals.

(iii) Financial Forecasts

The company's financial forecasts were segmented by product category within customer segment.

The three studies were integrated in a computerized model.Whilst the output of each study yielded extremely useful information, it was the combination of outputs that had the most significant strategic implications. Market segments were simultaneously compared against the following criteria: forecast earnings growth, the brand's contribution to earnings, and its competitive position. Given the rapid change in the relative importance of product categories,this type of analysis provided actionable input to marketing strategy and brand architecture decisions.The brand evaluation model is also being used to track brand performance.

New product development

There has been a trend to stretch brands into new categories and geographies during the last few years. Such actions can have significant value implications – both positive and negative.

The development of a financial model that incorporates an understanding of the brand's impact on volumes and price aids such decision making.This needs to be informed by predictive research into the brand's contribution in the new areas of activity. Some assumptions are likely to be necessary in developing an NPD evaluation model. Sensitivity analysis will determine which are the crucial assumption within the model.

Internal communications

Brand valuations are growing as an internal measure having been used as a means of explaining performance and as a means of motivating management. Similarly, the use of internal ro yalty rates based on brand values makes it clear to domestic, associated and foreign operations the value of the corporate assets which they are using.This enhances the growing demand for marketing accountability.

5.2 Financially focused brand valuations

In the last ten years brand valuation techniques have become accepted in a wide range of applications. This is illustrated by the examples and case studies that follow.

Balance sheet reporting

Current accounting practice is outlined earlier in this document. It is clear the trend will be for companies to disclose more brand value information than the required minimum. Corporate analysts have realized the value of marketing generally and brands in particular. Details of recent research in this area are shown in section 9 of this report.

There is nothing to prevent companies including additional information in their Annual Reports and this seems likely to happen. The Operating and Financial Review and Notes to the Accounts are almost certain to include far more information on such matters in future, whether or not internally generated and revalued assets appear on the face of the balance sheet.

The areas where it seems clear that far more information will be provided in future include:
- Segmentation of results by brand, region and consumer group
- Qualitative and quantitative analysis of marketing investment
- Revaluation of brands, both acquired and internally generated
- Long as well as short term forecasts of performance

There is increasing pressure for companies to show 5 or even 10 year forecasts in their reports to analysts. Some commentators are now arguing for 'value reporting' which would incorporate historic and prospective information of both a quantitative and qualitative nature.

Litigation support

Brand valuation techniques have frequently been used in legal cases to defend the brand value, whether it is against the illicit use of a brand name or, in the event of receivership, against the under valuation of assets by insolvency practitioners.

Case Study: Pocklington Foods (Gainers Inc)

This recent case in Canada highlights the use of brand valuation as a part of expert testimony in court cases.

The food company had run into trading difficulties and was unable to meet the terms and conditions of its borrowing facilities. The Alberta Government foreclosed on the business and operated it until it was sold to a third party. However, the price achieved for the company assets and brands did not cover the outstanding loans and the Government sued the former owner of the company to recover the balance.

Far from agreeing to pay up, the former owner argued that in terms of the financing agreement in place between himself and the Government, the Government was obliged to pay him the 'value' of the shares of the company. He argued that the company was worth more than the government had sold it for because the sales price did not adequately reflect assets such as trademarks, customer lists, brand names and shelf space. He felt that the 'true' value of the company exceeded the liabilities. The former owner took legal action and a protracted legal action ensued with expert brand valuations being used as evidence for both sides in the case.

In the lawsuit, the former owner said the company was worth about $136-million, while the province put its debts at about $116-million.

In February 1998, an Alberta judge ruled against the claim by the former company owner that the value of the company was $20-million more than it's liabilities, and that the Government should pay him the surplus value. He found that the plant was worth more than the $77-million that the province valued it at, but that there still wasn't enough of an intangible asset base to overcome the $114-million actually judged to be owed.

In his final ruling, the judge said the company was actually worth about $95-million, and its debts were about $114-million.

Fair trading investigations

Brand valuation techniques have been used as evidence in fair trading investigations where it has been held that high market share is the result of unfair trading. In such situations brand valuation techniques have been useful as a way of explaining to non-marketing audiences the role of brands,and the importance their value has for the companies which spend so much acquiring and maintaining them.

Case Study: Nescafé

A great deal of expert witness evidence was used when Nescafé was subject to a Monopolies and Mergers Commission enquiry into the soluble coffee market. Its lawyers ultimately demonstrated that the reason for Nescafé's high market share was less to do with unfair trade practices and more to do with strong brands heavily and consistently advertised.

Tax planning

In the past many companies had allowed their affiliates to use their brand names for little or no charge,but as the realization has grown of the profit generating powers of brands,companies have increasingly taken to charging royalties for their use. This has alerted tax authorities around the world, with many now asking companies to charge their subsidiary operations for the use of their brands.

Case Study: Major US courier company

In the US one large organization was recently hit with a retrospective tax charge for imputed royalties not levied on its foreign affiliates. In the opposite direction, several international companies have been accused of charging excess brand royalties to their US affiliates as a way of expatriating profits earned in the US. The net result is that more and more international organizations are actively planning the most effective domicile for their brand portfolios and are planning their tax affairs with branded royalty streams in mind.

Merger and acquisition planning

Brand valuation techniques now play a significant role in merger and acquisition activity. Potential acquirers of branded goods companies, and their investors and bankers, increasingly use brand valuations to provide comfort that the price being paid for a company can be substantiated by reference to the value of specific intangible assets as well as the tangible assets being acquired.

Case Study: Corsodyl and SmithKline Beecham

One example of this phenomenon was the acquisition of Corsodyl by SKB. In this case a higher price was paid than might have been suggested by a normal valuation because Corsodyl was a unique brand, with a tremendous heritage, the gold standard for mouth infections, recommended by both doctors and dentists. Corsodyl integrated perfectly with the rest of the SKB oral hygiene range, creating the platform for merchandising other dental products on the same trade sales calls as the popular Corsodyl brand.

Not only was it possible to estimate a value of the Corsodyl brand on existing products in existing markets. It was also possible to estimate the value of line extensions and favorable portfolio effects of other SKB oral hygiene brands.

Very similar arguments applied at a consumer level with the acquisition of Rowntree confectionery brands like Kit Kat by Nestlé. In that case huge ‘option’ value lay in new applications in both confectionery and in related areas such as ice creams.

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External investor relations

As major companies like Grand Metropolitan have stated that building a portfolio of world class brands is one of its central objectives,so the banking sector has become more concerned that a company's brand strength is reflected in its share value. Brand valuations can be used in this context as a means of providing hard numbers in what is currently a soft argument.

Case Study: Burmah Castrol

On 9th February 1996 Burmah Castrol's share price leapt 51p to a record 1039p high. The reason for this was a document entitled "Barbarians at the Gates of Swindon", a circular produced by the company's broker Merrill Lynch.

During the 1970's the price of Castrol's stock had plummeted to the equivalent of 40p per share. The Wiltshire based company had survived that crisis and continued to trade successfully.

However, analysts at Merrill Lynch were concerned the Burmah Castrol share price did not reflect the true value of the company. Although there did not appear to be any predators at the time,the relatively low value of the company would have made it an attractive target for a corporate raid.

Merrill Lynch estimated that the break-up value of the organization was in the region of £20 per share. The analysts believed the share price did not reflect the true earning potential of the Castrol brand of lubricant nor the company's growth into emerging markets. Cadbury Schweppes' recent acquisitions of the well-known American brands Dr Pepper and A&W provided the basis for Merrill's estimates.

While acknowledging that the confectionery industry and the petrochemicals industry were not directly comparable,the analysts applied similar multiples to those applied in the Cadbury deals. The critical factor was that Castrol was regarded as an internationally recognized premium brand.

As well as ensuring that the value of Burmah Castrol's shares rocketed immediately after publication, the content of Merrill's circular raised questions about the ability of the market to ensure that the "real" value of a public limited company is reflected in its share price.

The market's key weakness was that it had assumed Burmah Castrol was just another oil production company. The report quoted a Burmah Castrol company director who, when asked whether his organization was a motor oil company or a chemicals company, answered as follows,

"Neither....Burmah Castrol's key strength is in international marketing of specialized products,with a strong technology input, tailored to meet specific country needs."

The market was attempting to compare Burmah's stock against companies with which it shared few similarities. The reality is that Burmah is a branded goods company not a conventional oil company.

Licensing and franchising

Where companies allow associates to use brand names or are involved in the external licensing or franchising of their brands, brand valuation allows a realistic set of charges to be created. These charges reflect the value of the asset being licensed. The ultimate effect of recharging for the use of a brand name is exactly the same as charging for the use of central research facilities or shared production facilities.

Securitised borrowing

As brands have increasingly become recognized as assets, the opportunity to use them to back specific borrowing lines has increased, especially in the United States where companies as significant as Disney have borrowed major sums against their brand. A new market is opening up for the insurance of brand assets with a number of major insurers creating products tied to the capital value of brands and if such risk-oriented insurance products take hold there is likely to be an increase in securitised loans,because lenders will know that preferential rates will be underwritten by catastrophe risk insurance.

Case Study: Walt Disney Corporation

The entertainment industry is one particularly well suited to the use of brands as security on debt and this has been demonstrated by the Walt Disney Corporation on more than one occasion.

Disney has a range of characters and products that are instantly recognizable across the world. That the Disney brand was not carried as an absolute figure on the balance sheet did not dissuade management from exploiting its inherent value by using the Disney name as a means of raising new streams of finance.

Tokyo Disneyland is owned and operated by Oriental Land Co, a Japanese organization that pays royalties to Disney.

In a transaction arranged by Citicorp Investment Bank and the Long-Term Credit Bank of Japan, Disney ensured that its future earnings from the Tokyo park would not be effected by fluctuations in the dollar-yen exchange rate. Disney monetized a substantial portion of the park's expected future royalties. Bonds were issued that were securitised against the park's performance over a period of twenty years.

The deal was structured so that investors would bare any shortfall in the projected royalty streams while surplus amounts would be received in their entirety by Disney. Disney could not lose.

The total net proceeds of the issue of the bonds were approximately US$725m in what was widely described at the time (1988) as the "deal of the decade". The markets had demonstrated unshakeable faith in the Walt Disney brand. In the event park attendance soared above the agreed limits. Disney had achieved this without any loss of control over its business.

Given the success of its previous effort it was no surprise that Disney returned to the markets in 1992. A $400m bond was launched through Citibank and Lehman Brothers which offered investors a return linked to the profits of a pool of future movies.

The seven year unsecured notes were rated as a safe bet by the market who, once again, demonstrated their appreciation of the power of the Disney brand by ensuring that it was well taken up.

One Japanese banker even ventured the opinion that Mickey Mouse was a lower risk than the US government.

Advertising agency performance evaluation

Just as a significant minority of marketing directors believe that part of their rewards should be linked to long-term brand values some clients also believe that advertising agencies should be rewarded, at least in part, according to the value they add to the brands they serve,rather than on the number of awards they win or the amounts they spend in the media

Whether a single measure of brand value will ever become the benchmark for management and agency performance it is no exaggeration to suggest that brand valuation has become an important technique for strategic decision making. Its growing importance mirrors the growing importance of brands to the companies which own them.

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6. How can advertising agencies contribute to the brand valuation process?

The brand valuation process requires

a. Market understanding
b. Brand knowledge
c. Understanding of data relationships
d. Detailed financial analysis

To a greater or lesser degree it is quite natural for advertising agencies to be involved in all of these stages.The extent of the agencies involvement will be determined by the purpose for which the valuation will be used and the range of its skills. If the brand valuation is for the purposes of M&A planning, balance sheet reporting, tax planning or, of course, evaluation of the agency's own performance, an independent valuation specialist should be used.

a. Market Understanding

It is a prerequisite of sound account planning that the planner on a particular brand should have all the latest market trend data available in the agency information library or from proprietary sources. Some agencies commission their own market studies to better understand the markets in which their clients operate. This could represent a vital information source for any brand valuer.

It should be understood that the key requirement in a brand valuation is large amounts of data about the brand, both internal and external. While this is often available from different departments of the client, data gathering is usually the single most difficult stage in a brand valuation. It can be time consuming,incomplete and fraught with frustration. Brand valuations are often conducted for particular short term reasons and under time and cost pressure.

Any agency, acting in its rightful role as 'brand guardian' can facilitate and simplify the process by ensuring easy access to all relevant information for the valuation. This should not simply be an administrative service to the client or the professional valuer but should form the bedrock of better client understanding.

b. Brand Knowledge

Although a lot of detailed and robust numerical analysis is involved,brand valuation is of necessity a judgemental process. Brand valuation provides information about asset values at a point in time and a perspective on how value might be enhanced over time.

A detailed understanding of the brand and its business potential is therefore vital to the process. Who is better able to interpret and assess what particular brands are capable of than the agency which may have lived with and built the brand for longer than the average brand manager or even marketing director.

Brand valuers may be able to pick up key information on the brand very quickly but it is unlikely that their accumulated knowledge will beat an experienced advertising agency planner's knowledge about his or her brand. Such knowledge and opinions are often vital in completing a robust valuation. In practice, agency planners already participate in valuations because clients often source much of the detailed data from the agency and then pass it on to the brand valuer.

Undoubtedly this informal approach can be made more formal in many cases. One example of the value agencies can bring is in the debate about which brand equity tracking technique to use and what the results tell us about the future potential of the brand.

c. Understanding Data Relationships

If the valuer is to estimate likely future sales of the brand it is vital to understand historical data relationships. This may be based on observation, market research, correlation or regression. Studies may be conducted by the valuer or by the client but could equally be conducted by the agency. In fact, there is already an increasing tendency for agencies to conduct econometric modeling exercises for clients (particularly for media agencies). This is of vital assistance in building the business case or cases on which brand valuations are based. Such analysis gives credibility to the underlying assumptions. It creates the framework within which dynamic and option valuations can be based

d. Detailed Financial Analysis

Although agencies should have a reasonable understanding of the underlying financial case behind their clients business, it is unusual for them to have the required level of financial expertise to perform this aspect of a valuation.

In future, agencies will increasingly be involved in brand valuation, providing information and interpreting results.

7. Current accounting
treatment of brands

Despite the fact that a number of powerful brands have been in existence for more than a century, the accounting profession was slow to accept the fact that brands can be built, purchased and valued in a similar fashion to the tangible assets around which businesses were traditionally built.

The Accounting Standards Board of the Canadian Institute of Chartered Accountants is the standard setting body. Accounting for brands and intangibles is covered by section 3060 (Capital Assets) of the Canadian Institute's handbook.

Acquired brands are carried at cost less accumulated depreciation on company balance sheets. Internally generated brands are theoretically accounted for in the same manner as acquired brands to the extent that costs of creation can be identified and 'future benefits are reasonably assured'. In practice few, if any, brands appear on the balance sheet via this route.

The relevant International Accounting Standard is IAS 38. This requires the capitalization of purchased goodwill and acquired intangible assets such as licences, franchises, publishing titles, patents and brands. It does not allow internally generated brands to be capitalized.

In most countries accounting standards assume that brands have limited useful lives. Capitalized values are required to be amortized over the 'expected useful life' of the brand.

Within Canada there is a maximum amortization period of 40 years. The amortization methods employed are flexible, but must reflect the decrease in the future benefit of the brand to the company. The US, Japan and Germany also insist that all intangible assets have finite lives. IAS 38 adopted this conservative approach and requires that all intangibles must be amortized, generally over 20 years.

On the other hand, Britain, France, Netherlands and Australia reluctantly accept that intangibles can have indefinite lives. In the UK annual impairment reviews are required if the 20 year economic life presumption is rebutted.

Within Canada there is no specific requirement for brands to be valued by independent experts. Auditors will inspect supporting documentation for evidence of the purchase price of a brand. The auditors will evaluate the reasonableness of the useful life of the asset based on an estimate of the future benefit of the brand to the company.

Accounting statements only partially address the disclosure of intangible assets. Two anomalies result in company accounts failing to reflect the full asset value of companies:

- The pressure to amortize acquired brands, and other intangibles, lacks a clear logic. Brands are bought as investments and are usually maintained and developed at great expense. Well managed brands tend to gain rather than lose value, and many brands have outlived the companies that created them.

- Capitalization of internally generated brands is not permitted by either of the statements. The costs of creating internally generated brands are required to be treated as expenses when they are incurred. There are clearly problems in accounting for internally generated brands, however, having no disclosure of their value is far from ideal.

The anomaly of 'partial disclosure' of valuable brands is well illustrated in the UK by Diageo which can represent acquired brands like Smirnoff on their balance sheet yet have to exclude internally generated brands like Baileys. This is despite a significant contribution by Baileys, and indeed Diageo's other internally generated brands, to turnover and profits. Acquired brands to the value of £5billion were reflected in Diageo's financial statements at 30 June 1999. Investor and analysts were, however, left in the dark as to the value of the 'home grown' brands.

This anomaly largely explains the significant gulf between balance sheet assets and market capitalization. As discussed in section 1 of this report, a study by Brand Finance indicated that at 31/12/98 the market capitalization of London's FTSE 350 companies exceeded their net asset value by 72%. The bulk of this value gap is explained by intangible assets which were not reflected on the balance sheet.

8. Investor requirements
in terms of marketing disclosure

During the last three years Brand Finance has researched equity analysts requirements in terms of marketing disclosure.Although this research has, to date,focused on the UK the findings are pertinent to marketing and investor relations directors around the world.

In the area of brand value reporting analysts have an increasing interest in greater disclosure. 71% of the 154 analysts polled in 1999 thought that more information should be published on brand values.This was a 5% increase on the previous year.

Other key findings were:

- 75% of analysts interviewed thought that public companies should publish more information on marketing expenditure
- 73% felt that brands are becoming more important in merger and acquisition activity
- 65% of analysts endorsed the statement 'It would be helpful if annual valuations of internally developed brands were provided by way of the Notes to the Accounts'
- 81% endorsed the statement 'Brand valuations on acquisition and any subsequent re-valuations should be conducted by independent professional valuers'.

A notable feature of the research over the last three years has been that although the sample of analysts has progressively included more and more respondents from traditionally unbranded sectors,the demand for marketing and branding information has continued to increase.This appears to reflect a trend among traditionally unbranded companies to accept branding as a source of competitive advantage in price, service or specification driven businesses. For example, branding is rapidly becoming a board agenda item in businesses as diverse as utilities,specialist materials, bulk paper and engineering.

In short,equity analysts appreciate that knowledge of marketing performance and strategies is essential in order to assess the company's prospects.They also believe that companies are not currently providing them with the necessary information.

Ironically, the marketing, brand and advertising information wanted by analysts can often be obtained from other sources, such as independent research companies and competitive trade intelligence. Yet companies are reluctant to pre-digest and explain such information for investors.

There will be increasing pressure over the next few years for companies to go beyond the minimum statutory reporting requirements with regard to brand value and brand performance.Companies have the choice of being reluctant followers of this pressure, or adopting a more pro-active and confident approach to marketing disclosure.

If the board appreciates the value of its brand portfolio and is confident that its marketing strategy will deliver increased value, this information should be disclosed to analysts and investors. If it is not disclosed, the market will base its valuation of the company on incomplete information, or analysts will 'fly kites' based on rumor rather than fact.

In our experience, those companies that are placing the most attention on marketing disclosure tend to be in situations of stress - subject to a hostile bid or experiencing a dip in share price.It seems preferable, providing that internal marketing processes and strategies are sound, to make a statement of intent and ensure that investors appreciate the current and potential of the brand portfolio.

Brands will be major drivers of corporate value in the 21st century. Investors and business leaders have recognized this. Marketers are increasingly using brand valuation models to facilitate marketing planning. They should go one step further. Investors need and want greater disclosure of brand values and marketing performance. Marketers should play a lead role in ensuring that such information is adequately communicated to investors, rather than waiting for statutory disclosure requirements to catch up with reality.

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Appendix 1
Brand Equity

A1. Introduction

In a recent paper entitled “The business value of brands”, Paul Feldwick, Executive Planning Director of BMP DDB Needham in the UK,highlights the difficulty of finding any single,integrated measure of ‘brand equity.’

“The word ‘equity’ has been borrowed from finance, and its popularity reflects a general realization that a brand can be an asset.The reason I personally dislike it is that it is used, in practice, to refer to descriptive aspects of a brand, its symbols or consumer imagery; and because of its financial origin, it frequently implies, the financial valuation of a brand.This is dangerous,because it suggests to the unwary that all these things are essentially the same.

Most companies,if you push them into a statement of their overall business objective, will come up with something like ‘long term profitable growth.’ In other words, their owners and stockholders are not just interested in this year’s profits, but in a secure expectation that those profits will continue,and grow, for a number of years to come.An established and successful brand name is one of the best mechanisms for delivering this long term profit stream. Sales that are not associated with a strong brand (e.g. supplying a retailer’s own brand) are relatively vulnerable to competitors, to innovation and to price wars. But a strong relationship between the brand and its end consumers is not so easily disrupted,although eventually it can be eroded.

That is why brand names are often bought and sold for considerable sums of money – prices which reflect, not the tangible assets of the brand, the bricks and mortar and machinery, which are usually pretty small, but the expectation of continuing the brand’s level of sales into the foreseeable future.The prospect is associated with the brand name and its meaning to the public.

It is not, of course, guaranteed.A brand name is not necessarily an annuity and those who imagine it is often come unstuck. No brand is so strong that it cannot be seriously challenged by environmental change or by determined competition, and even the best brand can be destroyed extremely rapidly by inspired mismanagement. But within certain limits it is a sound bet that a brand’s sales will continue well into the future, and this is why brand names are worth money.

We should recognize at the outset, then, that there is no single dimension on which we could all agree to define ‘brand strength.’ What we can do is understand the nature of a brand’s relationship with its public on a number of different dimensions,and on these dimensions we can quantify trends and compare it with other brands in its own category, and in some cases with brands in other categories. We can, if we wish, create a single measure to represent our overall estimation of brand strength, but this will necessarily be a somewhat artificial and arbitrary concept, like indices of ‘standard of living’ or ‘national prosperity’ used by economists – such a measure might have its uses but we should not forget its limitations.”

Defining Brand Equity

Feldwick therefore rejects the term ‘brand equity’ as a catchall phrase which is frequently used to describe three quite different aspects of brand performance:

The first aspect covers the images, associations and beliefs consumers have about particular brands.

For example, a brand may be ‘young’, ‘green’ or ‘exciting’. Feldwick refers to this as ‘brand description.’ Because these associations and beliefs vary from consumer group to consumer group it is unlikely that simple measures and comparisons will ever be appropriate. However, they provide vital information for brand planning and may be connected with more numerical performance measures.

A great deal of ‘brand equity modeling’ has been done in the US charting the relationship between brand associations and quantifiable brand performance.Advertising agencies have an interest in demonstrating the relationship between image shift and brand performance.

The second aspect is the measurement of consumer loyalty to particular brands.

This may be measured in terms of price elasticity, demand volume, purchase frequency, attitudes or awareness. Feldwick refers to this as 'brand strength.' There are many different ways of tracking 'brand strength.' Econometric modeling of empirical data, experimental trade-off analysis and 'Share of Category Requirements' analysis are just a few of the techniques available. Research into quality perceptions and category saliency are just two examples of attitudinal and awareness measures.

'Brand strength' comparisons can be made between brands but a number of different measures need to be considered side-by-side rather than identifying one single measure.

The third aspect of brand measurement is financial evaluation of brands as separable assets – referred to by Feldwick as 'brand value.'

In his view, while it may be necessary to value brands for financial transactions and for the balance sheet, such valuations are only one way of measuring the long-term health of brands.

Because brand valuations are based on estimates of future profits and depend on assumptions made about ownership, usage and cost structures...'there is no such thing as an absolute value for a brand.'

Measuring Brand Strength

Feldwick suggests there are three broad categories of measuring brand strength:

Brand Strength based on observation of how the brand is currently performing in the marketplace;

Discussions of 'brand strength' or 'equity' sometimes suggest that these are abstract values, somehow quite separate from the brand's actual sales in the marketplace. Certainly we are assuming there are aspects of the brand's 'strength' that may not be apparent just by looking at its marketplace performance.But this should not blind us to the fact that the most obvious evidence of a brand's relationship with its public is normally to be found in its sales.A brand that is struggling in the marketplace can only be said to be 'strong' in specific and limited ways, if at all.

This is underlined by the fact that most forms of financial brand valuation, whether for sales or balance sheet purposes,start by looking at the brand's current sales and profit.

In one sense it is always true to say that a big, successful brand is a strong brand. But only in the tautological sense that we have made size and success our definition of strength.And this does not really help very much in addressing the management needs we explained earlier. What we are interested in is interpreting sales data so that it may tell us something extra about the brand's strength in a way that is not merely tautological.

The main possibility here is to define brand strength as the strength of consumer demand for our brand,relative to its competitors. 'Demand' and 'sales' will normally march in step, but not necessarily. In other words, we need to make some allowance for factors that might be influencing aspects of sales without actually improving consumer demand.The most important ones are price and distribution.

Brand Strength based on attempts to access the relevant beliefs, associations and attitudes that are in consumers' minds:

Our original 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. So the obvious place to anatomize the strength of a brand should be the consumer's mind.

David Aaker of the University of California,Berkley, 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 therefore runs the risk of sometimes being misleading.It will serve however to introduce some basic categories of information that we can try to gather about what goes on in 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's 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.' You could say a brand is strong because many people have heard of it or spontaneously think of it; you could certainly say it is strong if many people express great loyalty or affection for it,in their words and actions. In between, 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 based on attempts to estimate the brand's future performance and profit streams, and thus put a financial value on the brand as a corporate asset:

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 consumer behaviour – it leads to them buying the brand, staying with the brand, perhaps paying more for the brand. It is possible to observe the results of this behaviour directly in the form of sales, but this alone still begs a question highly relevant to the original issue of brand strength; they may be buying our brand today, but how likely are they to go on buying it tomorrow? Are they simply buying out of habit and inertia, or so they actively value it and feel close to it? How easy would it be for a competitor to take away our sales?

What is being asked for here is a measure of the consumer's overall attraction to the brand.This is also commonly called 'loyalty', though as we shall see this can be defined in different ways. (It is worth thinking about what the word loyalty meant, before it was borrowed by marketing people. A 'loyal' follower of the King was not just one who fought on his side,but one who would resist bribes or threats to betray him or run away. A 'loyal' football supporter goes to every game, home or away. A 'loyal' friend stands by you when others find a reason to desert you.) Or we could describe what we are looking for here as the consumer's 'attitude' to the brand, in the original and proper (dictionary) sense of the word:

'A mental and neural state of readiness, organized through experience, exerting a directive or dynamic influence upon the individual's response to all objects and situations with which it is related.'

Getting from Theory to Practice

It is easy to understand Feldwick's reservations about finding a simple connection between the different aspects of 'brand equity.' It is also easy to understand his reservations about the crudeness of turning complex and subtle brand measures into one financial number using brand valuation techniques.

However, in the real world we are only interested in brands and 'brand equity' to find persuasive connections which will allow reliable business valuations to be arrived at and sensible business decisions to be made

This is why such a huge effort is being made to find statistical relationships between the types of data we have been considering even if the relationships found are only persuasive rather than definitive.And despite the obvious problems with volatility and separability, brand valuation seems to provide the most practical framework for expressing the effect of those statistical connections back into the language of business and finance.

Brand valuations will only ever 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 modeling 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.

The following section,compiled in conjunction with the ICA, examines some Canadian and international approaches to ‘brand equity’ tracking.

Brand Equity Tracking Data

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

In Canada, as in the U.S. and U.K., 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.

A custom design study may indeed be a viable option in some circumstances. The unique focus and approach prevents us from providing examples in this presentation – indeed,descriptions are often unavailable due to the confidentiality of buyer-supplier agreement.

Advertising agencies’ knowledge and systems are generally not openly marketed, but rather, restricted to current clients or advertisers somehow linked to an agency. Although this applies to research conducted by Young & Rubicam, extensive description of their research has been made available for general review. A summary description of Y&R’s Brand Asset Valuator research has been included in our presentation – both for the value of its contribution and also,because it illustrates the kind of contribution being made by advertising agencies.

Proprietary systems are represented by summaries of three Canadian suppliers’ approaches:

- BrandDynamics™ from Millward Brown
- Brand Building from The NPD Group
- Brand Equity Tracking from Tandemar

It should be noted that the following descriptions were provided by the agency or research firms concerned and are not the opinions of either Brand Finance or the ICA.They are included as a showcase of Brand Equity approaches.

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.

How brands are built

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.

Differentiation is first

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 comes next

Differentiation is 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.

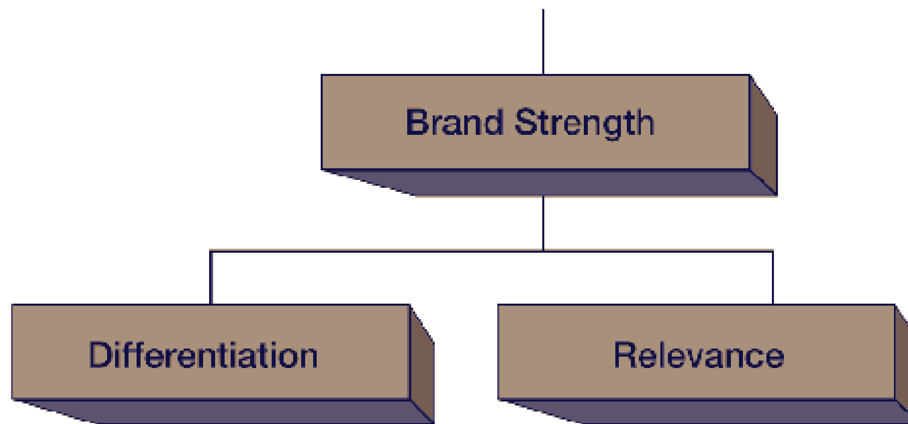
Brand strength

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. And the proportions of these factors differ by country and culture.

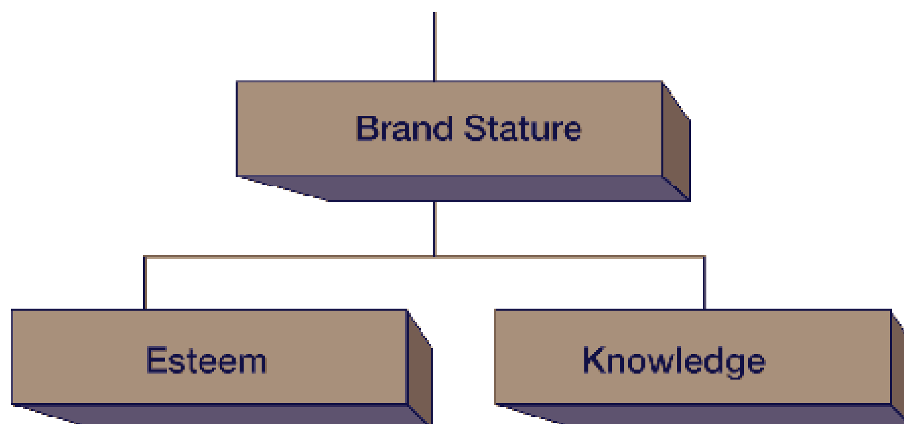
BAV tracks the ways in which brands gain Esteem,which helps us consider how to manage consumer perceptions. Through BAV, we can identify opportunities for leveraging a brand's Esteem.

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.

Brand stature

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.

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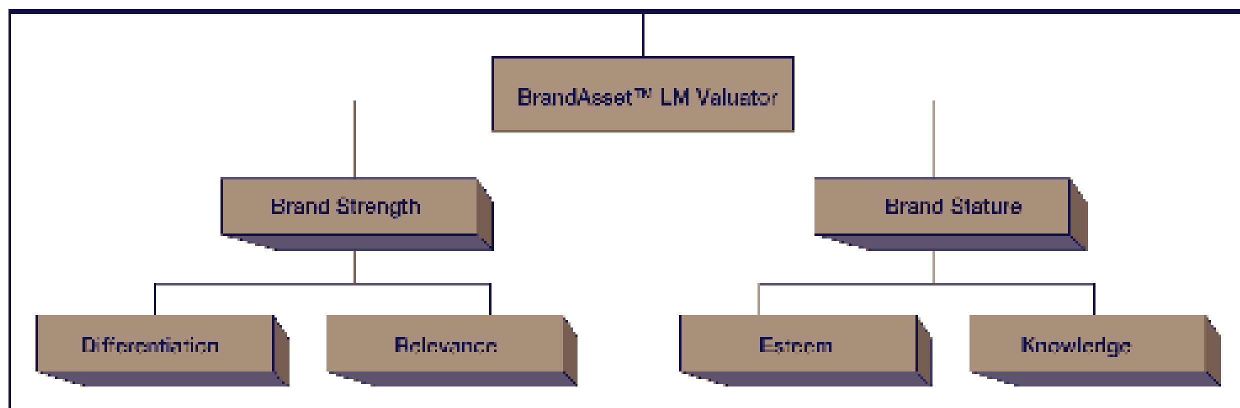
Relationships tell the story

By plotting all four measures - Differentiation,Relevance, Esteem and Knowledge - BAV serves as an exceptional diagnostic tool for building and managing brands.

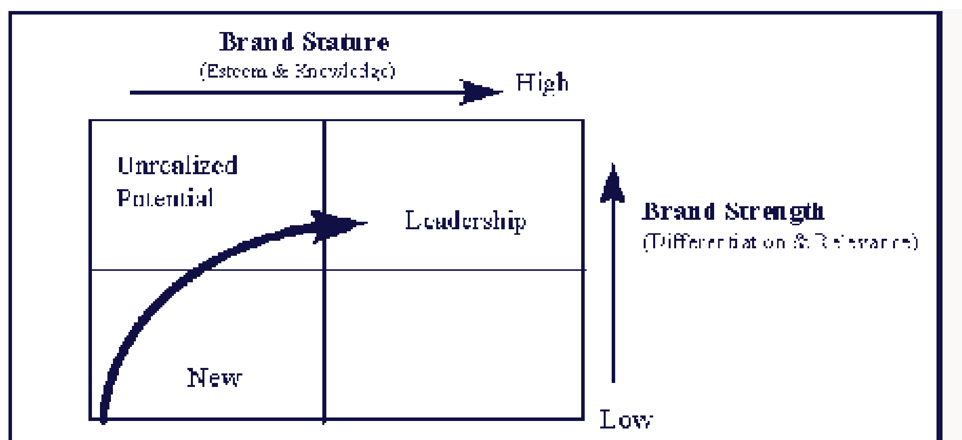
BAV's Power Grid sets the strategic process in gear by showing the strengths and weaknesses of a brand. It identifies the strategic direction to maximize brand strength and helps clarify the role of elements in the marketing mix.



The power grid

On the vertical axis, we plot each Brand's Strength - its level of Relevant Differentiation. Along the horizontal axis,we plot each brand's current Stature - its Esteem and Knowledge levels.

Brands begin life in the lower left corner, where they first establish their Differentiation, their reason for being. Most of the movement here is upward. The process of growth starts with Differentiation, then Relevance, while the brand is not yet held in Esteem or is not widely known.

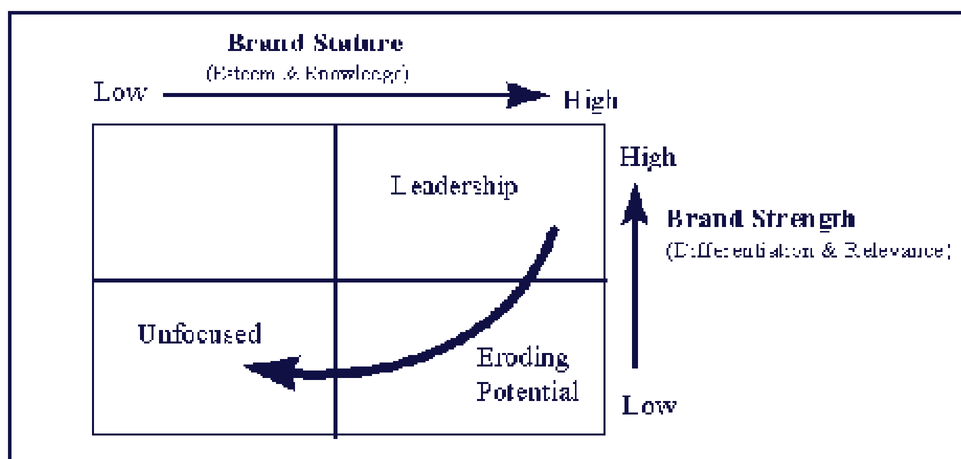


Enough Strength boosts the brand into the upper left quadrant. This quadrant represents the potential for a brand. Strength is still building and the challenge here is to translate this Strength into Stature for the brand.

Brands can stay in the upper left quadrant,establishing themselves as successful niche players. Or from this position, a brand can launch its attack. From a marketer's standpoint, it is also an area of yet unrealized potential. Current brand leaders need to recognize the brands in this quadrant as their emerging competition.

The upper right area is populated by the brand leaders. The strongest brands are here, those with megabrand potential and, in many cases, the megabrands themselves. A key finding of BAV is revealed in the Power Grid. Both older and relatively younger brands are found in this upper right quadrant. The implication is tremendous - brands can hold a position of power, virtually forever, if managed properly.

Finally, the bottom right quadrant is the trouble spot for brands, and an indicator of eroding potential. These brands have failed to maintain their Relevant Differentiation, their core Strength. If unattended long enough, their stature will begin to fall and the franchise decline.



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 overreaching 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.

A3. Millward Brown:

BrandDynamics™

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 (eg 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 18 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.

How does BrandDynamics™ work?

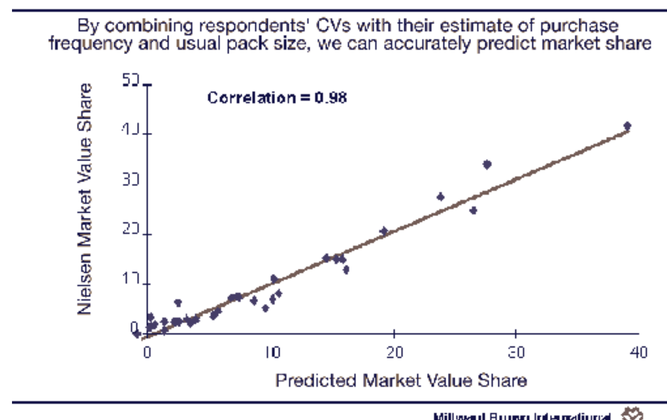
For each brand the system has two key components - Consumer Value, which is a measure of the sales value of each respondent to the brand, and the Brand Pyramid which is a systematic way of diagnosing the factors driving that value. Both are derived from a proprietary set of questions asked within a short survey interview among a random sample of category users.

Consumer Value

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 model 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.



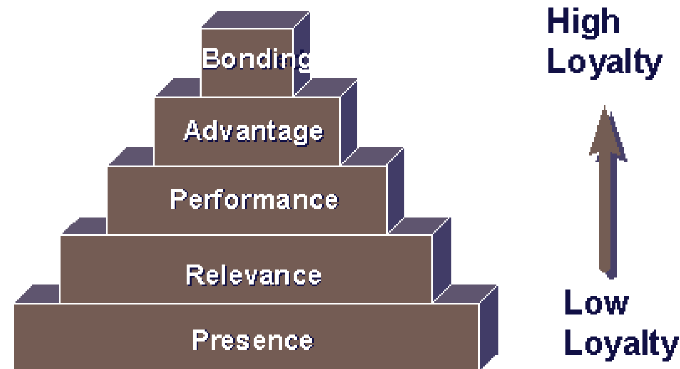
For categories where sales data are unreliable or unobtainable, Consumer Value is of significance in its own right as a valid indicator of sales.Some clients place more faith in consumer value than market share which can be distorted by promotions.

Brand Pyramid

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.

BrandDynamics™ PYRAMID

The Brand Pyramid is the framework for defining how consumers relate to brands



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.

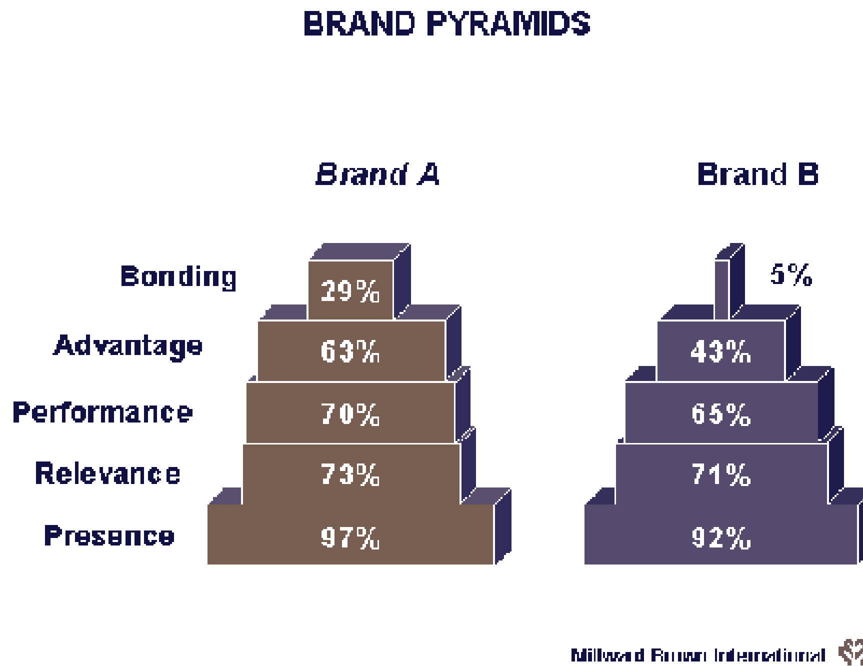
Product Performance
The brand does not have to be better than its competitors. But it does have to offer an acceptable level of product delivery. If a brand has a genuinely superior product and consumers are aware of this,then this will form a brand advantage.

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.

Using BrandDynamics™ to inform Strategic Decision-Making

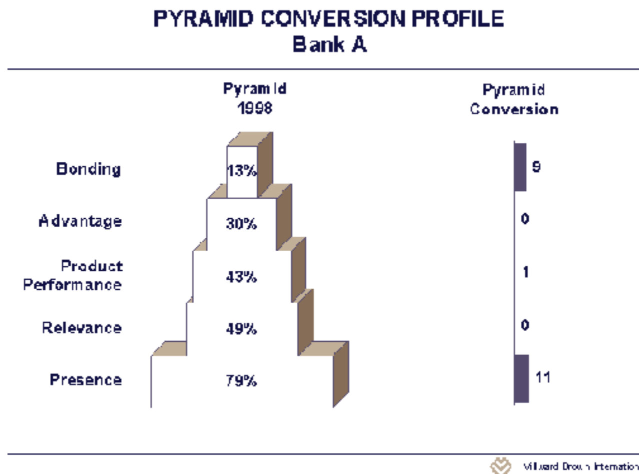
The pyramid is the starting point for the analysis of the brand's strengths and weaknesses. For example, we can see below that Brand A has a similar level of presence, relevance and product acceptability as Brand B, but has higher advantage and much higher bonding.

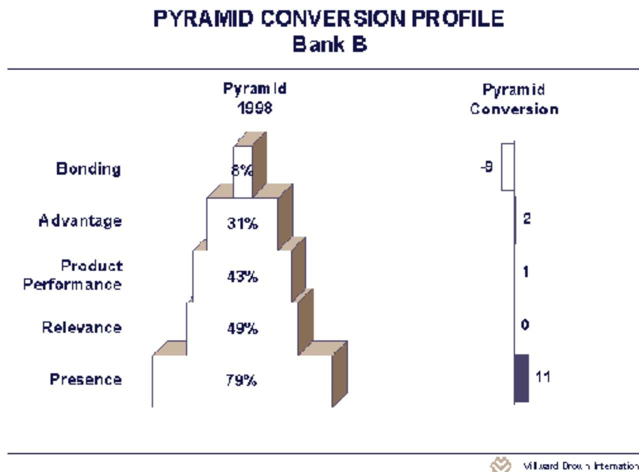


This is a useful finding, BUT as with most marketing data relating to brands, we have to remove the brand size effects to uncover the brand's core strengths and weaknesses. We do this via a profiling technique at the category level. This technique produces a strength and weakness analysis for each brand by comparing the conversion from each level up the pyramid with the other brands in the category.

This is the start point for understanding the strategic options available to the brand and it is a key input to measuring BRAND STRENGTH (described shortly).

While the overall pyramids for these two Canadian banks look quite similar, the conversion profiles reveal stark differences - both of which reflect their recent communications programs. Bank A has communicated its appreciation for its core customer's business and how it is working to make banking easier for them. Bank A enjoys higher levels of Bonding.





Bank B concentrated its communication on overall bank visibility leaving itself with fewer Bonded customers - current customers felt neglected by the communications. Is this important? Bank B has a much higher rate of past to present customers than Bank A; it has been much less successful in keeping its customers.

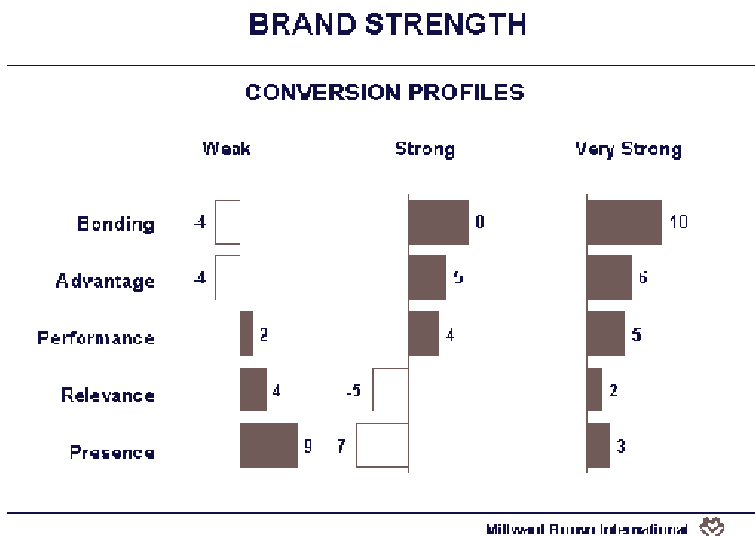
Source of Revenue

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.



This pattern is significant because brands with the left-handed profile tend to be brands which have been declining,brands in the middle tend to be new (and hence gaining share) or niche (often able to command a premium),and those with right-hand profile tend to be brand leaders. It makes intuitive sense that brands with relative strength toward the top of the pyramid, and hence a stronger relationship with their consumers,would over time fare better in the market place. And indeed when we score this profile with a higher weighting (ie based on the consumer loyalty of respondents at each level) to the pyramid levels toward the top, we find that it does have a clear correlation with share change. A correlation which does not exist for brand size.

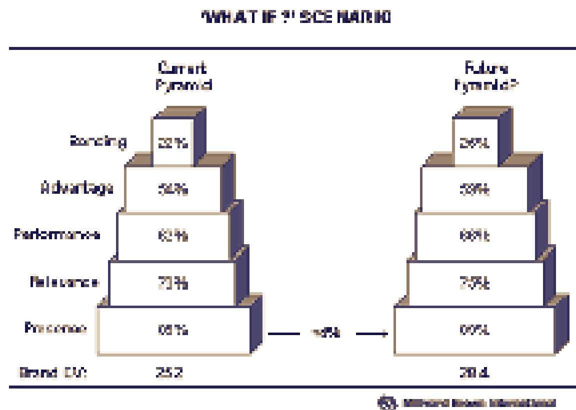
In summary, the BrandDynamics™ conversion profile provides the basis for a consumer-based measure of brand strength. This measure can be shown to have a positive correlation with changes in future value share. This provides clear evidence that brands which consumers feel to have either rational, but more often emotional or saliency based, advantages in the category are likely to be worth more to their owners in the future than ones which are bought purely on the basis of availability. This provides continued evidence for the value of long-term brand-building activity.

'What if' Scenarios

One of the key tools for strategic decision-making is being able to play 'What if' scenarios. Over the past six months MBI have been developing a sophisticated micro model based on the raw inputs to the Brand Pyramid. This model allows the user to examine the impact of changing each of the equity building blocks such as trial,saliency or emotional appeal. For each change the model will estimate the expected change in the Brand Pyramid, Consumer Value (and by extension underlying brand share),brand strength.

One of the key features of this system is that the model uses the relationships in the data for your brand, rather than assuming that it is like all the other brands in the category.

The following chart shows the effects of a 4% increase in Presence and how the pyramid levels change as well as the increase in CV (which in turn would be equivalent to share increase).



Based on this kind of "what if" analysis and detailed diagnostics to guide marketing investments, clients have been able to successfully grow market share, as predicted. We are starting to use BrandDynamics™ to look at mergers and to provide marketing budget guidelines. With these kind of metrics,effectively managing brand equity is becoming possible.

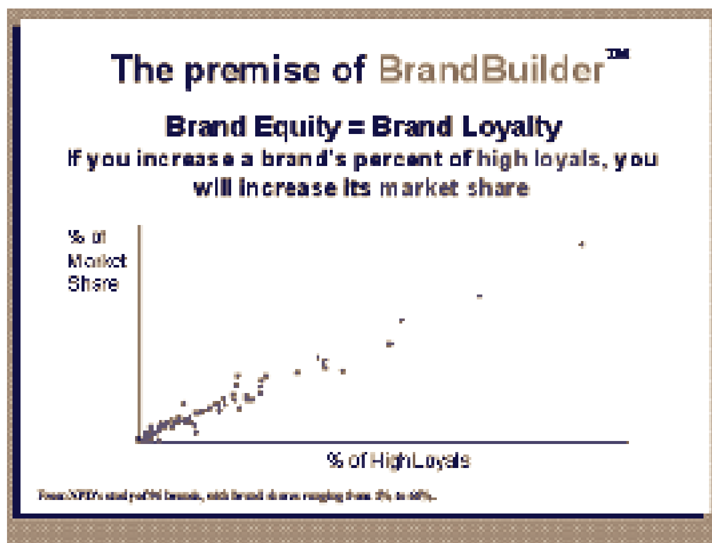
Summary

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 do I 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 a high proportion of their needs.These behaviorally 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.

Analysis of category dynamics reveals that a direct relationship exists between market share and appropriate loyalty measures.



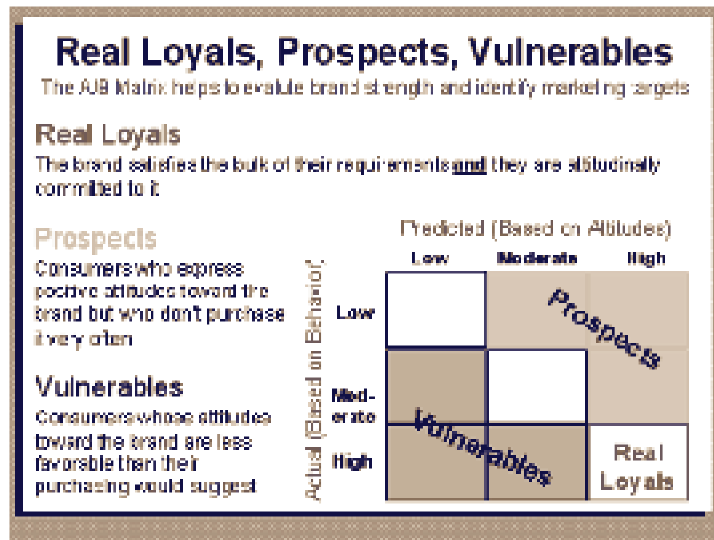
This is not to suggest that gaining brand trial or penetration is unimportant. Rather, it indicates that the key to long term profitable growth for the brand lies in the creation of an ever-growing base of loyal buyers.

The Link Between Attitudes and Behavior

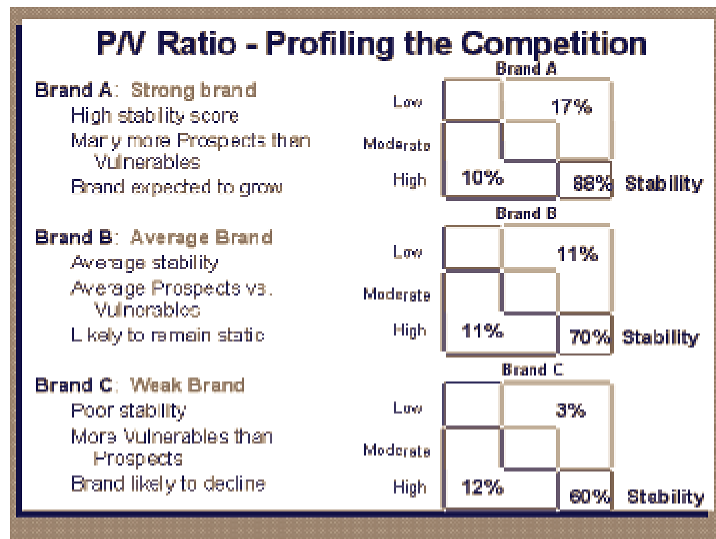
Not all repeat buyers are equally committed to the brand. Some hold beliefs about the brand that are consistent with their loyal purchase behavior; they are the brand's "core" franchise. Core consumers are truly committed – behaviorally and attitudinally – to the brand.

Others hold attitudes that are out of synch with their observed behavioral loyalty to the brand. We call those with attitudes less positive than their purchasing behavior "vulnerable",because their repeat purchasing is tied too strongly to price, or the attitudes that drive their behavior 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: to identify and size these buyer groups via a unique modeling process that fuses survey data with behavioral data, and to identify the specific dynamics and attributes that drive brand loyal behavior.



This matrix is produced for every major brand in the category under study. Based on BrandBuilder projects conducted in over 50 individual product categories, a normative database has been constructed.



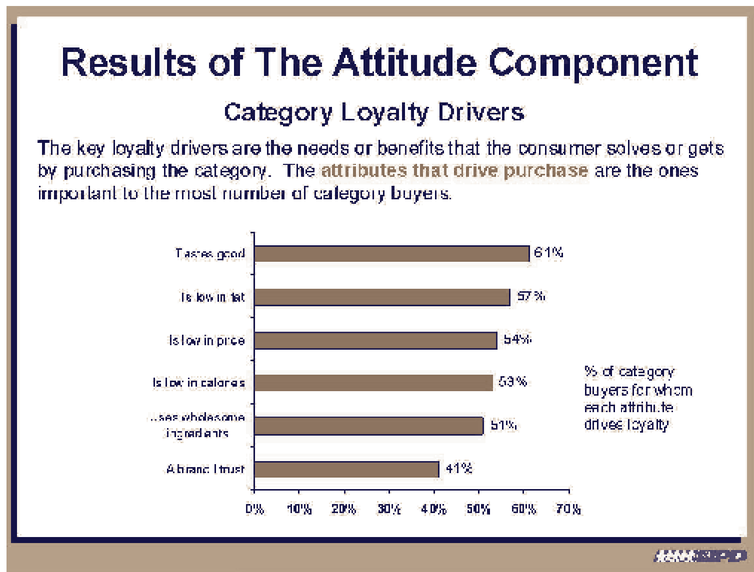
For example, we know that approximately 70% of the typical brand's loyal buyers are "core" or "real" brand loyals. In other words, about seven out of ten of the loyal buyers of the typical brand will hold positive attitudes towards the brand.

In the examples shown above, brand A is a strong brand,poised to increase its market share: it has an above-average "Stability Score", meaning that a very high proportion of its loyal buyer base, 88%, hold strong attitudes towards the brand. In addition, it is poised for further growth since a relatively high proportion of currently-non-loyal buyers hold strong attitudes (i.e., it has an above-normative level of Prospects). Brand B is an average, or static, brand, since it achieves only normative levels of its behavioral-to-attitudinal profile. Brand C is a weak brand, since its core franchise is relatively weak attitudinally, and since it has a relatively high proportion of "Vulnerable" buyers, or current buyers with weak attitudes.

What Attributes Drive 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 behavior at three levels:

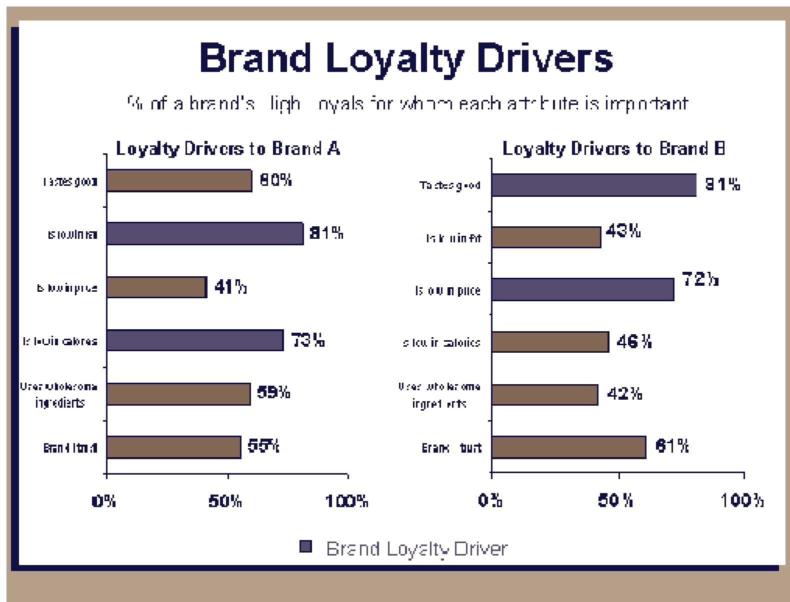
(1) At the category level,
(2) At the segment/form/usage occasion, demographic group level, and
(3) At the brand level.



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 behavioral loyalty on the one hand, and consumers' associations of specific characteristics of attributes with brands on the other. The BrandBuilder model uses a logit regression procedure to determine the key drivers of behavior at each of these three levels.

This chart shows how the attitudinal drivers might be displayed, in a given category. From analyses of the key category drivers, in dozens of product categories, certain key principles have begun to emerge:

Key Principles on What Drives Behavior
• 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.



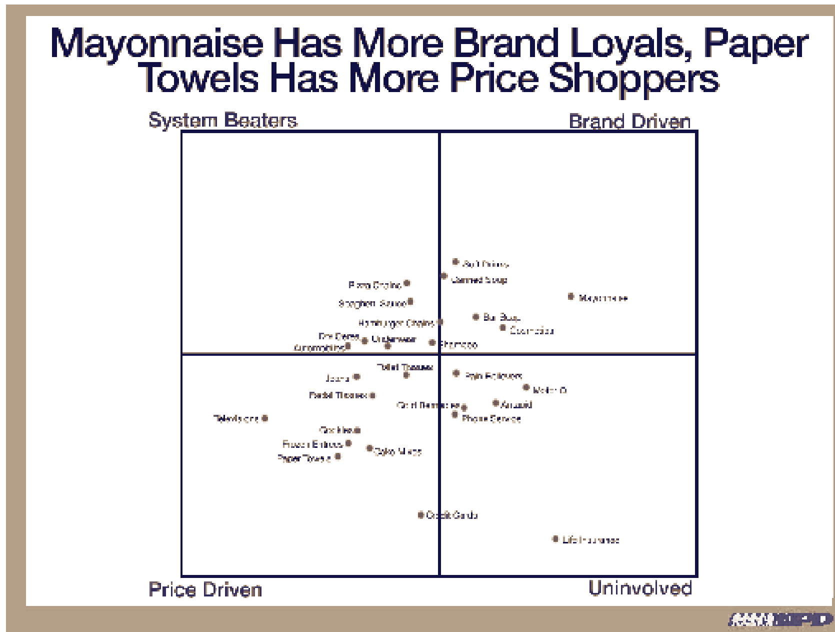
In the example shown above,Brand A is driven by "health" attributes, while Brand B is a "taste/value" brand.Without changing its position,Brand A is likely to grow if its attributes grow in importance over time, and/or if its share within the health segment increases.

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. We define category equity as follows:

Category Equity Definition
The tendency of buyers in the category to buy based purely on brand preferences ("Brand Drivens"),on price alone ("Price Drivens"), or to expect to be able to buy their favourite brand, and still get an attractive price ("System Beaters").

The map that follows displays the placement of categories, based on NPD's internal R&D database of categories. Certain categories, such as Mayonnaise and Beer, contain unusually high proportions of Brand Driven buyers. Others, such as Spaghetti Sauce and Pizza Restaurant chains, tend to contain above-normative levels of System Beaters. Still others,such as Paper Towels, and Frozen Vegetables, tend to contain above-average percentages of pure Price Driven buyers.



The normative proportions of each buyer group, across our database of 100+ categories is as follows:

Buyer Group	Definition	USA Category Norm
■ Brand Driven	Consumers whose purchase decisions are driven mostly by brand preference and less by price and deal.	34%
■ System Beaters	Consumers who have definite brand preferences, but also expect to buy their brands at bargain prices	32%
■ Price Drivens	Consumers who are driven mostly by price	25%
■ Uninvolved	Consumers who have low brand preferences, and do not expect to buy on price	9%

Why is Category Loyalty Important?

An understanding of the pattern of buyer group tendencies at the category level has important strategic implications. For example:

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

A5. Tandemar:
Brand Equity Tracking

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.

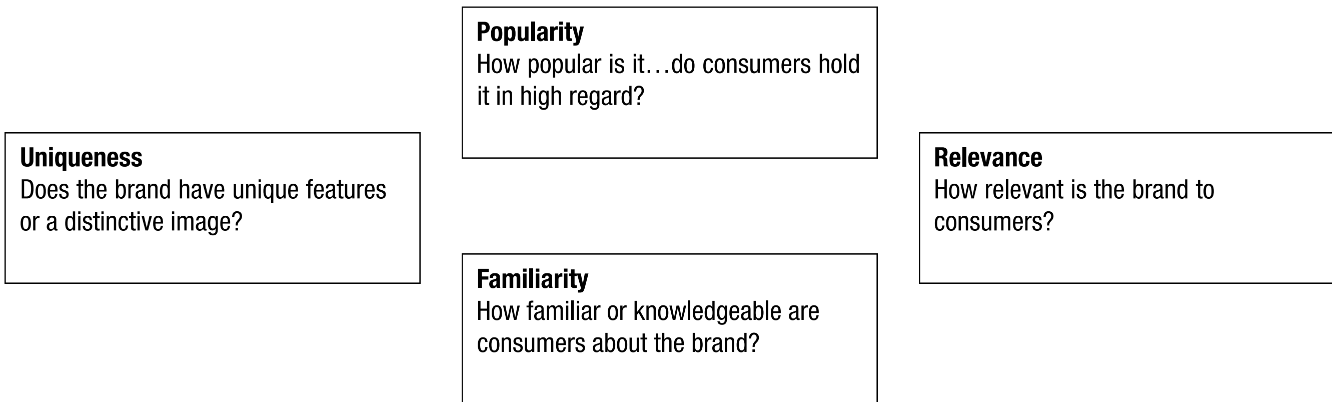
Tandemar has conducted Equity Reviews in over 50 different industry sectors in Canada, and has an extensive database of Canadian norms and case studies to draw on for analysis purposes.

Brand Equity – The Brand Strength Measure

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.

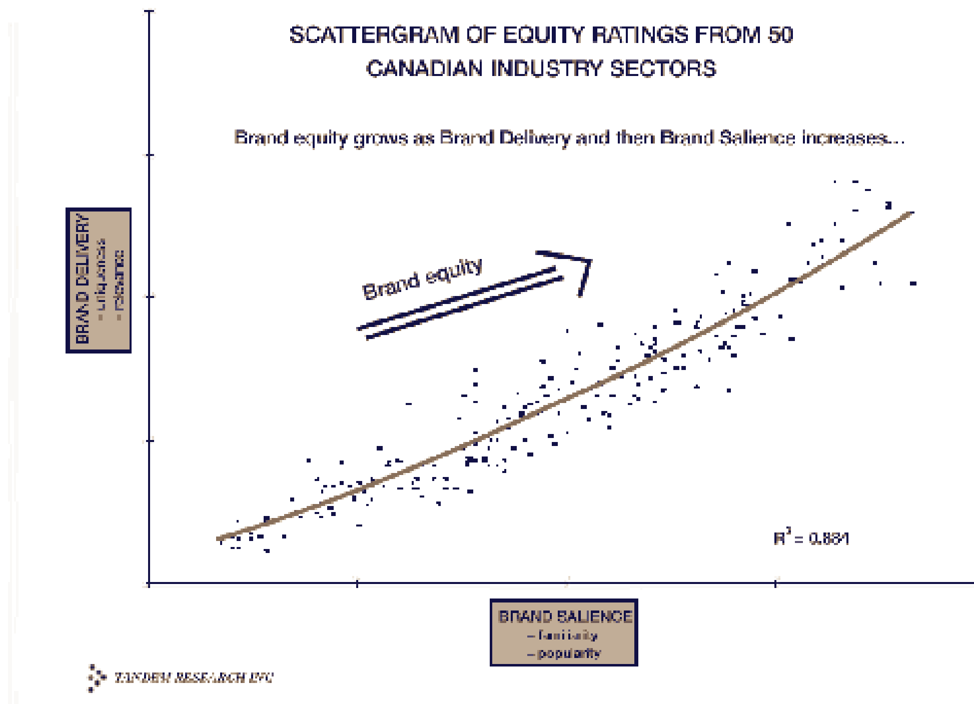
The parameters of the model are based on the learning from several international studies (including market mix modelling), and have been supported by our own large scale study of Canadian brands. Uniqueness and relevance are key brand delivery components, while familiarity and knowledge are rooted in 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 proven 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.

The four parameters of brand equity



A fifth parameter is the degree of attachment that consumers have towards a brand, which ranges from low to sometimes extraordinary levels of commitment.

A short series of attitude ratings is used to measure performance on these parameters.Plotting Brand Delivery ratings against Brand Sallence ratings produces the Equity Curve which, provides a powerful framework for diagnosing a brand's competitive position.



The Brand Equity Index is a combination of these attitudinal measures, indexed to Canadian database norms.This provides a single, evaluative brand equity measure which can be compared to competitors, market leader industry norms,Canadian brands in general, and tracked over time to assess brand equity initiatives.

A key advantage of this model is that questioning procedures are simple and consumer friendly, and centre on consumer's attitudes. These equity attitude statements were developed based on extensive pilot-testing in Canada.They adapt well to both mail and telephone methodologies.

Our Brand Equity model is validated against purchase behaviour measures, including loyalty. Thus provides a vital measurement system for tracking whether marketing efforts are strengthening brand loyalty, and hence profitability.

Loyalty – The Ultimate Goal

Strengthening positive attitudes about a brand is not enough.Equity advertising initiatives are only effective when they have an impact on commitment levels or purchase behaviour – that's loyalty building.

In our tracking programs respondents are classified by their relationship to the brand on a scale from unfamiliar to 100% loyal.The size of each group can be measured and tracked over time.It also provides useful direction for determining targetting opportunities, and is insightful for segmenting brand equity and imagery.

In addition,respondents' level of loyalty toward a brand is recorded, based on its share of category requirements.

It should be recognized that purchase loyalty is influenced by factors other than just a healthy brand equity. Ehrenberg's exhaustive research into loyalty, which is based on very sound analytics of behavioral data, indicates that penetration level is the key driver of profitability while loyalty level is only a poor discriminator between brands.

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“The evidence is that customers of Brand A are usually likely no more loyal to A than customers of Brand B are to B…as we see the evidence,there are no strong brands or weak brands,but only big brands and little ones.”
Ehrenberg, 1997

The good news is that our Equity tracking work suggests that Ehrenberg is only partially correct.Thus our Equity database supports the view that penetration levels are a key factor of brand strength, and hence building penetration is an important objective for nearly all brands. However, we also have clear evidence that loyalty levels can and do vary between brands of similar size, and that these variations are driven by the equity of and/or attitudes about the brand.

Brand size and strength of brand equity drive loyalty level.

	Small brands		**Medium size brands**		**Big brands**	
	Lower equity	Stronger equity	Lower equity	Stronger equity	Lower equity	Stronger equity
Loyalty Index	100 = 100		170 ➔ 230		190 ➔ 360	

Thus,both brand size (penetration) and loyalty levels can respond to advertising equity initiatives. Tandemar Brand Equity tracking will help ensure that realistic loyalty goals are set, and that key behavioural and loyalty levels are measured.

Diagnostic Measures – The How and Why

While the Brand Equity model quantifies the strength of the brand,its practical advantage comes from learning which brand characteristics support or drive greater equity, Tandemar's diagnostic measures answer the important underlying questions,and help explain why consumers rate the brand the way they do. Is the brand's positioning well understood? Do consumers perceive other brands as viable alternatives? Is the image of the brand consistent with its positioning?

Of particular importance is a detailed brand imagery assessment which determines the drivers of positive (and weaker) brand equity ratings.This driver analysis provides the diagnostic understanding to identify which marketing activities and communication strategies to concentrate on.

Test Procedures

Brand Equity tracking studies can be conducted…

- As custom designed tracking studies
- Through Tandemar's Annual Syndicated Brand Equity tracking study
- By integrating the Brand Equity module into an existing tracking study.

All three methods provide valid monitors of Brand Equity, but differ in their scope of category evaluation (number of brands covered) and depth of diagnostic data.

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A6. Using Brand Equity research in Brand Valuations

As we have seen there are many different proprietary approaches and systems for measuring ‘brand strength’ and ‘brand equity’. We have considered a handful in detail 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 detail 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 results 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.

A7. The Brand Equity Ten
(David Aaker)

Bearing this in mind David Aaker, Marketing Professor at the University of California,Berkeley, advocates a flexible approach to brand equity evaluation which he calls the Brand Equity Ten.

He identifies what he believes to be the 10 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.

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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 Behavior 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 detail in his recent book 'Building Strong Brands' (The Free Press),focuses principally on consumer-oriented measures of brand strength, although it also looks at market oriented measures.

He recommends that brand owners seeking to evaluate the historical and future performance of their brands should adopt a flexible and pragmatic approach to brand equity evaluation.

He acknowledges the difficulty of defining one simple,single score or measure of Brand Strength. He is not prescriptive about the weightings or scores which should be applied to each attribute but recommends that brand management should tailor the general approach to its own specific circumstances.

Aaker is persuasive in his advocacy of the Brand Equity Ten and it is hard not to endorse his mixture of attitudinal, behavioral and market measures of brand equity.

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