

Wall Street values brands  
higher than Main Street.  
Watch out.



# The Brand

# BUBBLE

**John Gerzema**



**“Time destroys the speculation of men, but it confirms nature.”** —Cicero, 106-143 B.C.

As we leave behind 2008, the numbers are both historic and dismal. The S&P 500 declined by 38 percent, and almost 2 million jobs were lost. The median home price fell by 22 percent, while almost 7 trillion dollars in market value evaporated from the Dow Jones 5000 Index. Taxpayers funded \$700 billion to bail out financial institutions, with another \$17.5 billion to keep General Motors and Chrysler operating into the new year. The credit crisis intertwined virtually every economy and sector in the world, shattering consumer confidence to its lowest point in decades.

The market bubbles in the S&L crisis of the 1980s, the dot-coms of the early 2000s and the home equity markets of today all exemplify the regular and recurring danger of rampant speculation, when unfettered zeal bids prices up to levels that far exceed the real value of the assets they represent. Yet bubbles are, as Shirley Bassey sings, “Just another case of history repeating.”

**Tulipmania.** One of the first bubbles on record occurred some 400 years ago, in Holland. And the asset that perpetrated this bubble was a tulip bulb. The Dutch aristocracy had acquired a particular fondness for a type of tulip from Turkey that grew very well in the fertile lowlands of Holland. Citizens from all walks of life, from businessmen to average

workers and paupers, quickly jumped at the opportunity to invest in tulips. Some even took out a crude form of futures contracts on unplanted tulips.

The market for tulips created such frenzy that no one stopped to question if the cash flows would continue in perpetuity. No one paused to discount the risks inherent in the trade and instead continued to reinvest in more bulbs. And then at some point between 1636 and 1637, the appetite for tulips plummeted. So too did the fortunes of the thousands who had participated in “tulipmania.”

**Snap, crackle, pop.** In early 2007 we identified another bubble, one twice the size of the residential subprime mortgage market and almost \$4 trillion dollars of the S&P 500’s market capitalization. Again, this bubble was created by the reckless run-up of hype, devoid of underlying consumer logic. And, like complex derivatives, it was hidden in black boxes and proprietary modeling. Yet, in this instance, the assets at risk cannot be traded away or hedged against uncertainty. Rather, they are the fundamental drivers of competitive advantage for most organizations: their brands.

Brand value accounts for approximately 30 percent of the market capitalization of the S&P 500 (Millward Brown Optimor, 2007). While this varies by sector, brand value as a percentage of a company’s market value has risen steadily from 5 percent 30 years ago.

## Executive Summary

**The BrandAsset Valuator (BAV) brand study found** that, while brand valuations have risen steadily, consumers are selling brands short: Brand awareness is down 20 percent, brand esteem is sliding by 12 percent, perceptions of brand quality declined 24 percent, and trust in brands has eroded by almost 50 percent. The authors conclude that an entirely new approach to analyzing a company and managing its brands is needed to stave off the inevitable decline in brand value.

### Brand Value

Today, the 250 most valuable global brands are worth \$2.197 trillion dollars, which is larger than the GDP of France. (Calculation is from the 2007 IMF list based on GDP under purchasing power parity.) Even the world's top 10 most valuable brands exceed the market capitalization of 70 percent of U.S. public companies (Booz & Co., 2007). Google's brand value makes up 50 percent of its market capitalization. PepsiCo shows a tangible book value of \$9.8 billion against a market value of \$108 billion, indicating that investors are banking on Pepsi, like thousands of brands that offer products and services to consumers and businesses.

What drives this appreciation in brand value that is reflected in market capitalization? A brand is a promise to its customers. And if brand value is growing, consumers must be deriving greater value from the promises companies are making to them vis a vis their brands. Yet empirical evidence based on thousands of brands suggests the value creation that brands bring to a company's enterprise value is exaggerated: The financial markets think brands are worth more than the consumers who buy them.

Working with professors Robert Jacobson and Natalie Mizik at The University of Washington and Columbia Business Schools, we studied consumer perceptions of thousands of brands across 13 years of data collected through BrandAsset Valuator (BAV), the world's largest global database on brands. Because of its scale and longevity, BAV is recognized as a reliable diagnostic tool for understanding how successful brands are built. We have interviewed more than 500,000 customers in 44 countries across 40,000 brands on more than 70 brand metrics since the study's inception. We conduct surveys in more than 40 languages. From Arabic to Zulu, we ask consumers how they feel about local, regional and multinational brands, media and celebrities. We've invested almost \$115 million dollars in our study, and our data tracks back to 1993.

**Main Street vs. Wall Street.** The brand study found that, while brand valuations have risen steadily, consumers are selling brands short: Brand awareness is down 20 percent, brand esteem is sliding by 12 percent, perceptions of brand quality

declined 24 percent, and trust in brands has eroded by almost 50 percent.

Within 2,500 brands we analyzed, almost 70 percent were stagnant or eroding in brand differentiation. And, of the 30 percent that changed, it was twice as likely that change was negative. Curious as to why, we cross-examined Interbrand's top 100 most valuable brands (2004-2007) with those in our study and found that 45 percent were actually declining in consumer perceptions. Despite this, the top 100 reportedly gained 16 percent in overall value, or approximately \$16 billion dollars. Clearly it was beginning to dawn on us that Wall Street was valuing brands more speculatively than Main Street.

We then turned to other researchers for insight and explanation. And the fact that consumers are losing interest in many brands was reported by several other reputable sources, from the Henley Centre in the U.K., which detailed the decline of Britain's largest iconic brands, to The Carlson Marketing Group, which found the percentage of people who said they were loyal to one brand declined from 40 percent to 9 percent since 2000. Meanwhile, Jack Trout and Kevin Clancy's research reported that brand differentiation declined in 40 of 46 categories as studied by Copernicus/Market Facts.

How can brands account for a growing percentage of market capital when most aren't growing in consumer estimation? Why would brands be failing, and why at this point in time? Interestingly, this diminution of brand value is occurring precisely at the same time that media fragmentation and technology are creating tectonic shifts in how consumers interact with brands. Far from a mere coincidence, it's a canary in a coal mine.

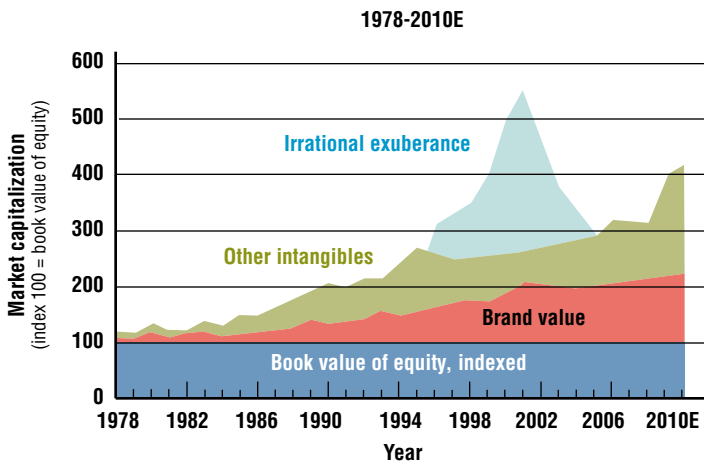
### Where's the Beef?

The rampant speculation in something as ordinary as a brand exemplifies one of the most basic fundamentals in business: the concept of value. Indeed, the core purpose of any business is to facilitate the transfer of value from one entity to another in a way that provides adequate value for customers and adequate returns for shareholders.

The concept of business as a vehicle for value transfer is nothing new, and it is utterly simple. But in today's highly competitive and complicated business environment, it is crucial to understand the repercussions on the way the transfer of value between a business and customer is to (ideally) exist in a steady state of perfect harmony: The business entity keeps the value created by the difference between cost and price, while the customer keeps the value created by the difference between price and perceived utility.

But interesting things happen in the real world, especially when multiple parties perceive the utility of a good, service or asset to be different. In these situations, value corrections, sometimes drastic, must take place. We have seen it multiple times in the past from the dot-coms to most recently the credit crunch. When multiple parties perceive the value of a good, service or asset to be different, we enter into unsustainable conditions encapsulated by the dreaded "B" word: a bubble.

**Exhibit 1** Market capitalization of the S&P 500



**The Accelerated Decay of Brands**

That’s precisely what’s happening again right now. Emboldened by the tools of the new digital world, consumerism is drastically and profoundly changing, which is rapidly accelerating the decay of brands. Fragmentation, social media and digital acceleration are causing a widespread attack on brand value. Consumers are quicker to punish uninteresting and undifferentiated brands. Today, brand equity is decaying in compressed periods of time.

Brand equity is not the protective insulation it once was. After all, brand equity is only what a brand has achieved up until this point. What consumers are telling us is that past

reputation seems to mean very little. Consumers are fatigued more quickly with brands that can’t adapt and evolve. The clutter of the marketplace combined with the “old models” for brand management that strive to build awareness and reputation are actually backfiring in that they are slowing a brand’s ability to keep pace with a consumer who is moving faster than their marketing strategies. And the emergence of a new digital consumer only amplifies the “d” problem: differentiation in a brand (or lack thereof).

**Brand differentiation.** Today a sea of sameness engulfs the marketplace. Consumers have more choice than they know what to do with. Yet they’re emotionally invested in fewer brands than ever before. According to Datamonitor, 58,375 new products were introduced worldwide in 2006, more than double from 2002. The report points out that “despite the fact that advertising spending was up from \$271 billion in 2005 to \$285 billion in 2006, 81 percent of consumers could not name one of the top 50 new products launched in 2006, an all-time high for lack of recognition and a huge leap up from 57 percent in the previous year.”(Datamonitor: Schneider/Stagnito Communications/IRI *Most Memorable New Product Launch Survey*)

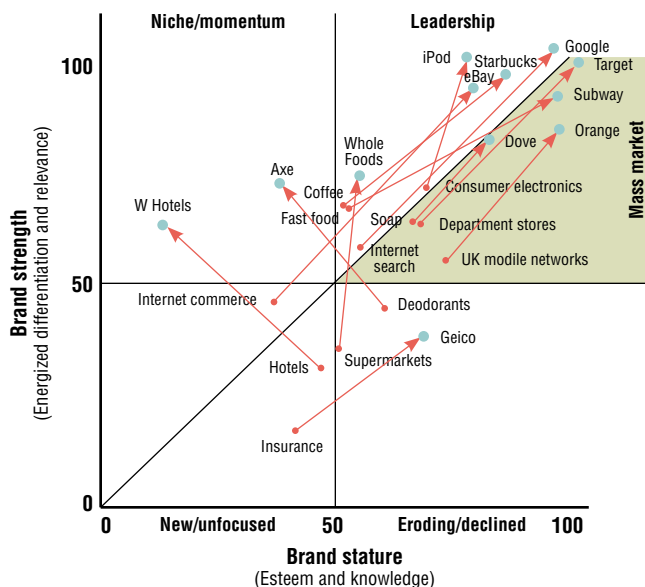
Brands were originally built and sustained on the backs of mass media, repetition and consumer monologue, but media fragmentation, coupled with the Internet on steroids (e.g., broadband), enabled low-cost competitors to attack from any geography without the need for access to massive capital. Suddenly, all these changes became the catalyst for consumers to morph into different creatures.

In fact, let’s call it Consumerland—a Disneyland-like broadband-fueled world of limitless consumer potential and endless control. The result is that, with so much access to content and information, creativity became the currency. And brands that don’t have it become boorish and mere commodities in their eyes. Consumerland embraces and demands creativity. From buying “cheap chic” in Target to posting films on YouTube, consumers have raised their creative expectations of brands. Yet most brands exist in state of rational, repetitious and persuasive selling propositions. Without creativity, there is no true differentiation. Today it takes emotion to differentiate and be desirable.

Consumers are also losing trust in brands. Because of the parade of Enrons, product recalls, dogfights, steroids and political scandals, the consumer has had enough already. In fact, consumers now trust each other more than they trust brands. Media Edge/CIA found that 76 percent of people rely on what others say versus 15 percent on advertising. And 92 percent of consumers now cite word of mouth as the best source for product and brand information, up from 67 percent in 1977 (Universal McCann study, 2007). No wonder review sites, such as Digg and Reddit, have become the third-most-common use of the Internet after e-mail and search.

Given the patterns of concern emerging in our data, we began a second study to understand which brands were outperforming the marketplace in their ability to create greater loyalty, pricing power and impact on the financial

**Exhibit 2** Brands that best their peers



performance for their firms. In so doing, we uncovered that consumers are looking for something more.

### A Brand Is a Direction, Not a Place

Brand differentiation is integral to business performance by capturing consumer respect and loyalty and ensuring sustainability. However, we identified a more powerful form of differentiation, which affects the future financial performance of the firm.

We were looking to identify whether there might be a key correlation between various brand attributes and unanticipated stock returns. We found that a few brands were absolutely stellar, doing exceedingly well among consumers and advancing far ahead of their competitors. Some were leaping out of the category in terms of brand equity. We observed consumers being captivated by a quality that reflected a more exciting, dynamic and creative experience. Consumers concentrated their passion, devotion and purchasing power onto an increasingly smaller portfolio of brands simply because they kept surprising and evolving.

In studying these brands, we discovered a key consumer perceptual component of brands that was in fact highly related to movements in stock price.

Through further exploration of these brands with the greatest sense of momentum in the marketplace, we were able to quantify this quality in BAV and named it Energy. This metric of Energy captures the consumer's perception of motion and direction. Consumers, in acting like investors, actually seek out brands with momentum and command over navigating consumers into the future. To gain a better understanding of how BAV attributes clustered in energized brands, we used multidimensional scaling and uncovered three perceptual territories reflecting the following:

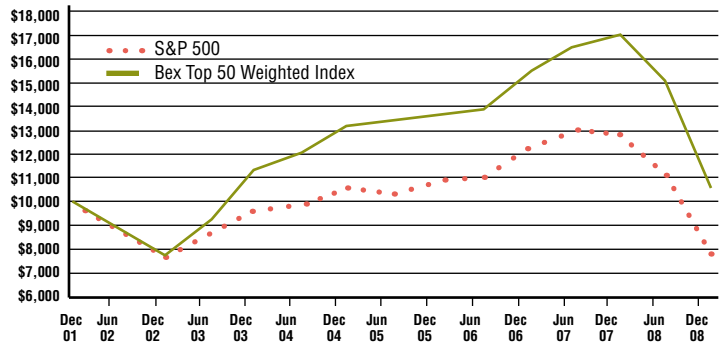
- **Vision:** the brand's purpose and aspirations, often originating from its leadership, convictions and reputation of the company behind the brand
- **Invention:** the most tangible dimension, demonstrating the brand's vision through product/service innovation, design, content and other tactile brand experiences
- **Dynamism:** how the brand expresses its vision in a dynamic way in the marketplace to create persona, emotion, advocacy and evangelism through its marketing and other forms of conversations with consumers

This in turn told us that consumers evaluate a brand from every vantage point, not just traditional marketing as we think of it. In order for a brand to create and sustain its real value, it can't just be different; it has to keep being different. Consumers constantly re-evaluate brands and are drawn to ones that are continuously innovating and reengaging; that provide a sense of direction and creativity.

Modeling of our BAV data demonstrated that Energy plays a significant role in protecting and enhancing brand

### Exhibit 3 The brand value equation

The BAV fund of the fifty energy-gaining brands netted \$10,527 (+5%) vs. S&P 500's \$7,867 (-21%) on \$10,000 investment made in 2001.



	FH 2002 return	SH 2002 return	FH 2003 return	SH 2003 return	FH 2004 return	SH 2004 return	FH 2005 return
S&P 500	-13.8%	-11.1%	10.8%	14.1%	2.6%	6.2%	-1.7%
BAV top 50 index	-9.8%	-14.0%	18.9%	23.3%	5.9%	9.4%	2.0%

	SH 2005 return	FH 2006 return	SH 2006 return	FH 2007 return	SH 2007 return	FH 2008 return	SH 2008 return
S&P 500	4.78%	1.76%	11.66%	6.00%	-2.3%	-12.8%	-29.4%
BAV top 50 index	1.1%	2.2%	11.2%	7.3%	2.9%	-11.6%	-30.2%

differentiation. Then a new, more powerful form of differentiation emerged, which we called Energized Differentiation. It reflects a brand's questing spirit for continuous change and evolution. These brands aren't just different—they keep being different by utilizing motion, momentum and creativity. Indeed, when we look into our BrandAsset Valuator brand database, brands with high levels of Energized Differentiation break away from their categories. (See Exhibit 2.) BAV measures the multiples these brands have over their category averages:

- Axe: 3.6 times the level of Energized Differentiation
- Dove: 1.6 times the pricing power
- eBay: 3.15 times the emotional commitment
- Geico: 2.8 times the momentum
- Google: 2 times the behavioral commitment
- iPod: 2.5 times the emotional commitment
- Orange: 1.6 times the usage and preference
- Starbucks: 2 times the pricing power
- Subway: 2.4 times the usage and preference
- Target: 2.3 times the emotional commitment
- W Hotels: 1.4 times the pricing power
- Whole Foods: 2 times the pricing power

In terms of correlations, when we examined BAV consumer data (stated responses on which brands they prefer, feel loyal to and would be willing to pay a premium price for, among other things) we found that, the more energy a brand has, the greater its consideration, loyalty, pricing power and brand value (as a percentage of firm value). And we observed the expectations of brand-driven financial performance were in line with consumer perceptions. We modeled a portfolio of the 50 top energy-gaining brands each quarter over a five-year period and found they cumulatively beat the S&P 500 by more than 30 percent.

And yet while brands have never been more important, there are fewer “important” brands. The percentage of brands in our study that beat the S&P 500 index actually declined by 36 percent from 2002 to 2007. This means a smaller number of brands now account for a significantly greater share of market capitalization. And, conversely, more brands may be overvalued.

## Takeaways for Management

**The CEO manages brand value as integral to business value.** Given that one-third of all shareholder value is brand value, this growing disconnect should be of urgent concern to CEOs, marketers, analysts and investors. Brands now account for an increasingly dominant share of total business value, which means that CEOs are making promises to shareholders of future earnings through their brands. But are those earnings going to be there in the future? Have most companies properly discounted the risk on their rising brand values?

It’s up to the CEO to assess the level of disconnect between the value of the brand and the Wall Street valuation of the enterprise. How much is their brand value contributing to, or detracting from, the value of the company? Then the CEO must not only rethink the brand’s role in the firm’s overall business strategy, but look at marketing in an entirely new context.

**Marketing is not a cost, but a fiduciary responsibility to shareholders.** When future earnings are in question, it’s more than a brand problem; it’s a business problem. Most of the discussion surrounding the tectonic shifts in the digital, consumer and media landscape has been held at the marketing and brand level. By examining these phenomena through the lens of brand value, we aim to draw in managers of all levels to understand and internalize their role as marketers, brand managers and creators of brand (i.e., business) value.

As brand value approaches enterprise value, brand marketing becomes integral to the strategy of the entire enterprise. The CEO must protect future earnings by placing marketing at the forefront of business strategy, treating it not as a cost, but as an essential means of discounting the risk on the firm’s rising brand values. We offer a detailed method to organizing the company around its brand and consumer in our book, *The Brand Bubble: The Looming Crisis in Brand Value*.

The CEO as “brand manager in chief.” The CEO’s brand now secures a growing proportion of future earnings in the eyes of today’s investment community. But a brand begins first

## The BAV Model

The BAV model is constructed around four pillars that help us identify the movement and success of a brand:

- **Energized Differentiation:** a brand’s unique meaning, with motion and direction (relates to margins and cultural currency)
- **Relevance:** how appropriate the brand is to you (relates to consideration and trial)
- **Esteem:** how you regard the brand (relates to perceptions of quality and loyalty)
- **Knowledge:** your intimate understanding of the brand (relates to awareness and consumer experience)

The four pillars are paired in two categories: Brand Strength (composed of Energized Differentiation and Relevance) and Brand Stature (composed of Esteem and Knowledge). Brand Strength is a leading indicator that predicts the future growth value of the brand, while Brand Stature is a lagging indicator that reflects the current operating value of the brand (i.e., what the brand has achieved up until today).

as a promise in the mind of the consumer. Many are failing to keep their promises. Far from an isolated incident, this pattern exists in thousands of brands in our data, leading us to think of brand equity in terms of a massive sector of our global economy that’s in distress. And yet, unlike other industries, brands are entirely intangible and dependent largely on the shifting whims of consumer sentiment.

Sounds a lot like shareholders, doesn’t it? In order to align the enterprise around the needs of the brand, the 21st century CEO must become the “brand manager in chief.” This CEO must treat consumers and shareholders as investors, both of whom must be continuously courted with active listening and fast reaction management. They must both jointly see the farthest horizons of the company’s (brand’s) vision, including its product and service innovation and command over the future. The time is ripe for an entirely new approach to analyzing a company, managing its brands and optimizing its future through a more holistic and forward-looking vision of marketing. Nothing short of this will stave off the inevitable decline in brand value. ●

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