BRAND·FINANCE ®

Principles of BrandEconomics™

- Adding Brand Value

Brands start life as simple trademarks and related legal rights. Through careful management and skilful promotion they come to exert a powerful influence over consumer behaviour. Brands create both legal and psychological barriers to competition in an increasingly commoditized world. We live in a world where tangible assets and production capacity are in surplus. Brands and related intangibles create differentiation, which drives consumer demand and superior shareholder returns.

How do brands shift the demand curve?

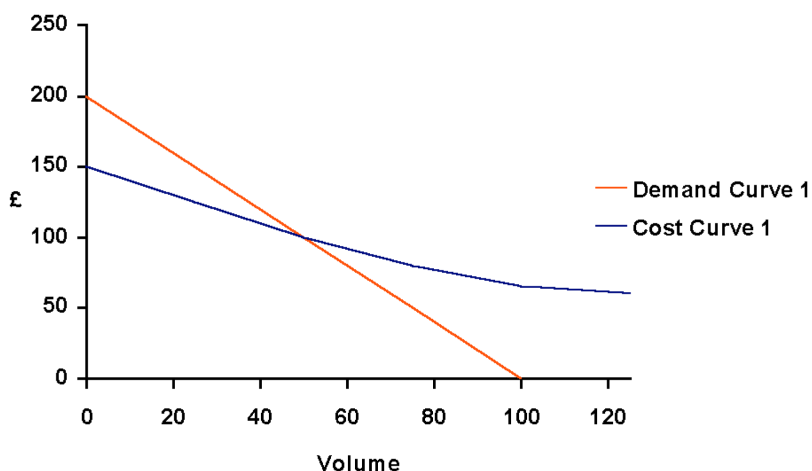
- growing the total market
- new-user acquisition
- switching-user conversion
- existing customer retention
- share of requirements
- cross-sell new products
- like-for-like price premium

The following charts illustrate the principles of how branding affects the demand curve and the profits of an organization.

The volume of demand for a commodity increases as the price drops. The gradient of the line indicates how price elastic the commodity is. A very price elastic commodity will have a flat line with the volume demanded increasing rapidly as price drops, and vice versa (Figure 1).

The average cost of producing a commodity creates a second curve. Where the two lines meet is the break even point.

Figure 1: Economic model for commodity product:



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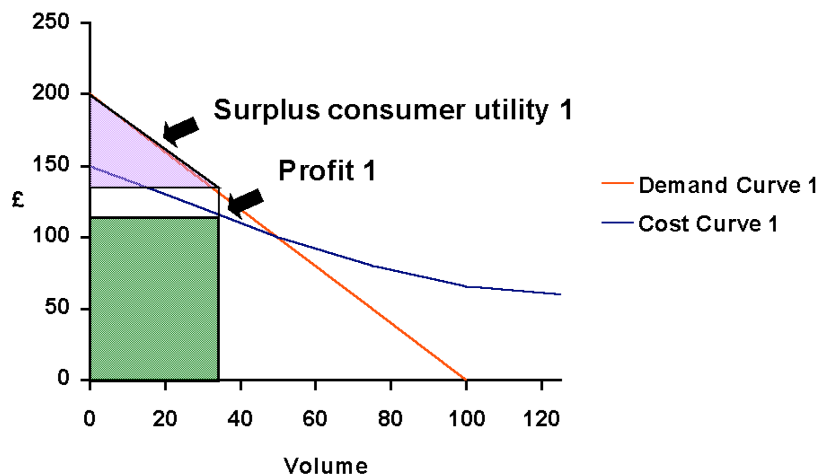
Trading at a price and volume above breakeven results in a profit (Figure 2).

Surplus consumer utility represents the extra value given to those consumers who buy but would have been willing to pay more.

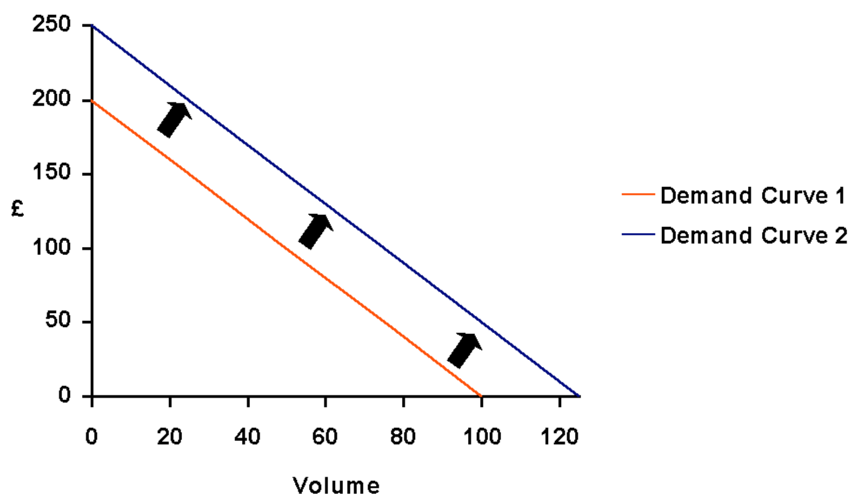
Above the breakeven point both consumers and the company are satisfied.

Figure 2: Economic model for commodity product:



By introducing a strong brand the demand curve moves out to the right (Figure 3).

Figure 3: Strong brand equity shifts the demand curve:



This means that at a given price consumers will buy more of the branded product or service increasing profits (Figure 4).

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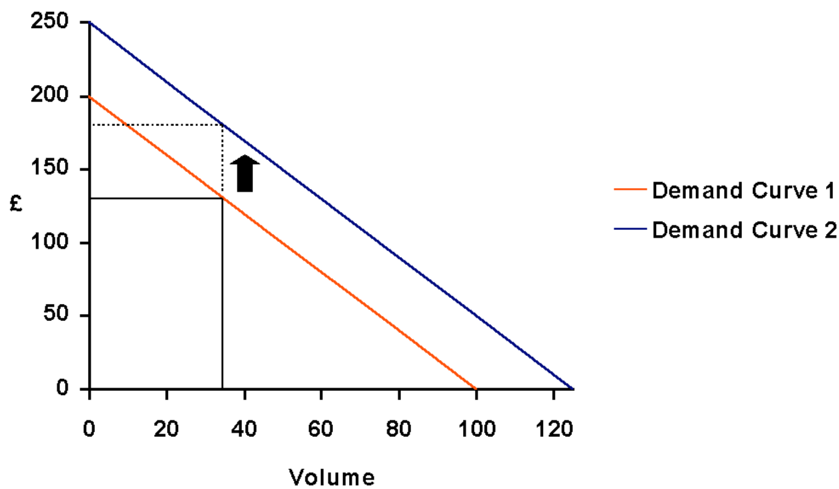
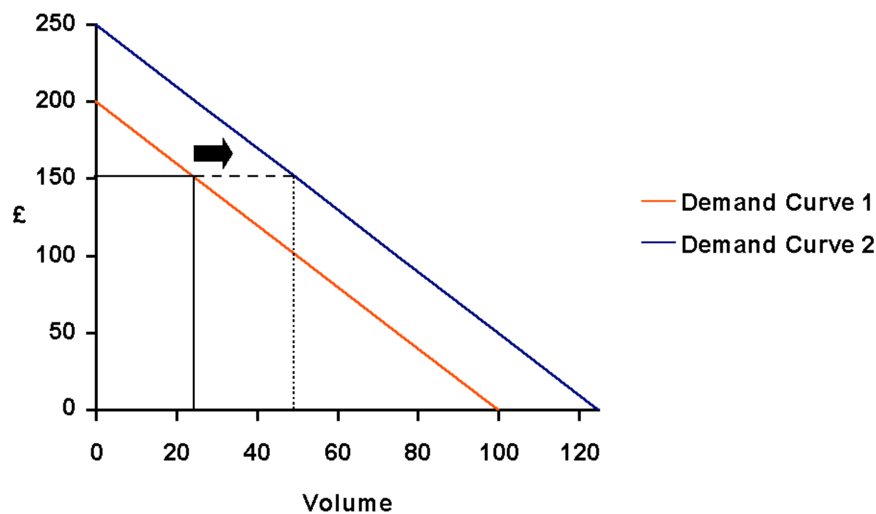
Figure 4: Same price; higher volume:



In most cases the demand curve also becomes more inelastic. In other words the volume consumers buy remains stable even as the price increases. They do not switch to another commodity product because this cannot deliver the intangible benefits created by the brand (Figure 5).

Figure 5: Higher price; same volume:



How do brands shift the supply curve?

- trade/ consumer recognition and loyalty
- lower sales conversion costs
- lower average broker commissions
- lower staff acquisition/ retention costs
- more favorable supplier terms
- lower cost of capital
- production economies of scale

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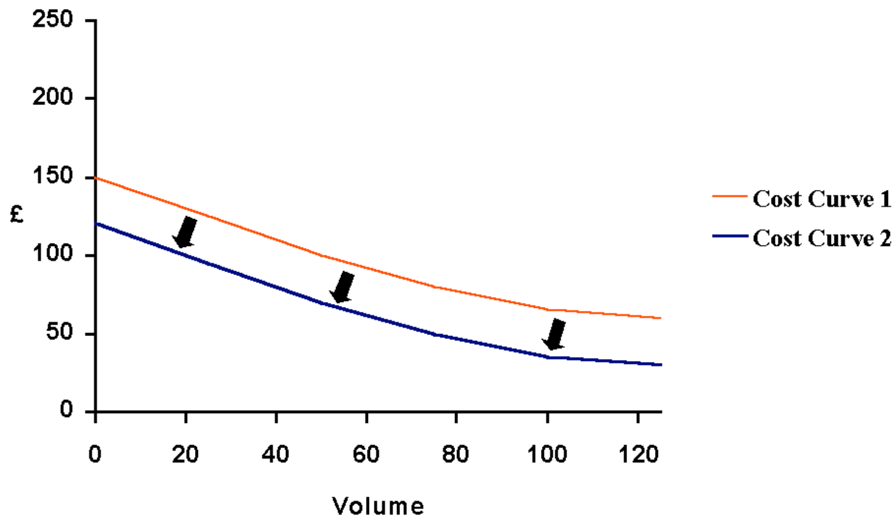
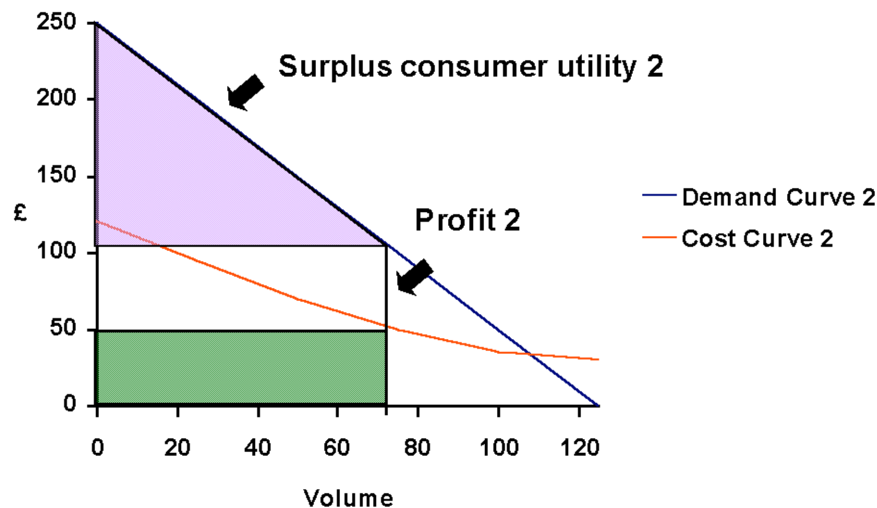
Branding also affects the cost curve. Suppliers, staff and providers of capital are all willing to provide their factors of production for less if there is a brand they wish to deal with (Figure 6).

Figure 6: Strong brand equity shifts the supply curve:



The net result is a win for both consumers and the company. Because the demand curve has moved in one direction while the cost curve has moved in the other it is possible to sell at the same or a lower price while making greater profits and creating greater surplus consumer utility (Figure 7).

Figure 7: Economic model for power brand:



This simple model is at the heart of all branding.

In practice, these effects are complex and require detailed statistical regression and financial analysis. **Brand Finance** has been helping clients understand and clarify the effects of branding on their economic performance since 1996. We bring professional skills and a clear vision to help clients identify the simple equation that adds most brand and shareholder value.

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