Brand leverage

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A brand can grow quickly if its owner builds on the foundation of performance, personality, and presence to create innovative strategies for expansion through focus or diversification

BRANDING IS A HOT TOPIC in boardrooms around the world because most CEOs recognize that a strong brand is a powerful driver of shareholder value. Indeed, McKinsey analysis suggests that about half of the market value of the Fortune 250 is tied to intangible assets. For some of the world's best-known companies, the figure is even higher.

Intangible assets include more than just brands, of course. Nonetheless, our research into the connection between brand strength and corporate performance at 130 consumer companies suggests strong brands generate, on average, total returns to shareholders (TRS) that are 1.9 percent above the industry average, while weaker brands lag behind the average by 3.1 percent.

Why do brands "work" for customers? The reasons are familiar: they simplify everyday choices (a shopper who regularly buys Crest doesn't have to agonize continually over toothpaste), reduce the risk of complicated buying decisions (IBM mainframes and Boeing jets are safe choices), provide emotional benefits (Tiffany), and offer a sense of community (Apple Computer and Saturn). Strong brands are therefore enormously attractive to senior managers, whose interest is fed by any number of books and articles on how to get and keep them. But anyone who thinks seriously about branding soon realizes that there are basically two kinds of strong brands: those that are focused and those that are diversified.

Near one end of the spectrum, Dell has maintained a focused link between its brand and its core product line: personal computers. At the other end is Disney. In the 1950s, that company too had a focused brand, which signified world-class animation, mainly for children. Today, Disney's businesses include films, television, publishing, software, theme parks, hotels, cruises, and even

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ABOUT THE RESEARCH

To create a broad research base of large consumer companies, we included all Fortune 250 enterprises deriving a substantial part of their revenue from consumers.* This gave us an initial base of 105 companies. To make sure that performance issues unique to large companies did not skew our sample, we added 25 smaller companies from the Fortune 1000. The whole sample base thus had 130 company brands.

We interviewed 5,000 consumers to assess their perceptions of the brand strength of these 130 companies. Then we proceeded to calculate how leveraged their brands were across different product and service categories – in other words, what percentage of their revenue came from each category. We found that a statistically significant breakpoint was reached when 40 percent of a company's revenue came from outside the core category, and we used this insight to separate brands into more and less leveraged segments. Finally, to control for the different levels of profitability of different industries we calculated the total return to shareholders (TRS) of each company and compared this with the industry average. Where a company operated in a number of industries, we placed it in the category of its dominant business or businesses.

Our approach allowed us to calculate the returns from stronger and weaker brands, as well as the differences between more and less leveraged stronger brands. Exhibit 1 of the text presents this information.

* Brands are important both in consumer and business-to-business marketing. However, given the considerably greater complexity of conducting large-scale research with business customers, we focused on consumer brands.

an entire town (Celebration, Florida). The company's name now represents the broader concept of "wholesome entertainment and living at any age."

Dell has decided to remain focused for now, while Disney elected – and managed – to diversify. The crucial question for CEOs is which camp they want to be in. As these examples show, a strong company can do well in either. But when we broke down the figures showing that strong brands earn total returns to shareholders 1.9 percent above the industry average, we found that focused brands (such as Dell, Levi's, Sprint, and Gillette) earn 0.9 percent more than the average, while diversified brands (such as Disney, GE, and American Express) earn no less than 5 percent more (Exhibit 1).

At least three factors appear to be driving the superior economics of diversified brand leverage. First, leveraging a brand widely tends to spread brand management support costs. Second, the tendency to "convergence," in which hitherto separate industries begin to merge, means that new market opportunities are opening up in many industries. Third, relationship benefits seem to have growing importance for customers; indeed, relationship building (through loyalty programs, better service, and a better understanding of customers) may now count for more than functional benefits. As relationships outstrip products in importance, leveraging brands makes more and more sense.

This is not to say that every company should pursue a leveraged strategy. BIC started out marketing a very successful basic 19-cent ballpoint pen. It then tried – unsuccessfully – to leverage its value position into such luxuries as fragrances and such necessities as pantyhose. Hindsight suggests that the company should have stayed put. Likewise, in the 1980s Gucci went through a period of almost unfettered licensing: at one point, 22,000 items bore the company's name in up to ten logo formats. Sales plunged. Gucci cut back its licensing, increased prices, tightened controls over the brand's premium quality, concentrated distribution, and increased its advertising. Sales rose, though moderately.

Every company should think about whether it can leverage what might be its most important intangible asset. With this reality in mind, McKinsey surveyed more than 5,000 consumers about their impressions of 130 moderate-to-strong consumer brands in six industry sectors: retailing, clothing, financial services, telecommunications, media and entertainment, and computers and electronics (*see* boxed insert, "About the research"). We also took an in-depth look at several dozen companies to understand how they leveraged existing brands into new opportunities. The findings illuminate the vital issues: whether a company should stay focused or diversify with confidence, what a company stuck between these positions should do, the key elements for each strategy, and how to get going.

Brand leverage – when and how?

Leveraging a brand means using the initial brand platform to move into other opportunities.

Ivory Soap, for example, has used its base – manufacturing bars of soap – to move into shampoo and washing powders. Both obviously leverage the core brand's essential characteristics. Virgin, by contrast, appears to have leveraged its brand in quite unrelated ways, into airlines, financial services, and cola drinks. The unifying factor that resonates across all of these businesses is the idea of Virgin as a fun and exciting company, still something of a rebel against the system.

Some companies leverage their brands much more quickly than other companies do. Charles Schwab evolved from a discount brokerage into a PC trading environment in only ten years. Ralph Lauren (neckties to menswear) and Amazon.com (books to music and video) lever-

Exhibit 1

Total return to shareholders relative to industry, 1993–97

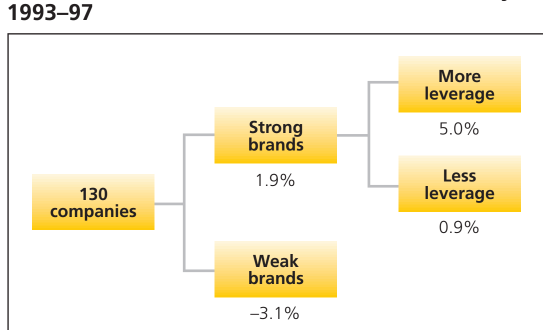
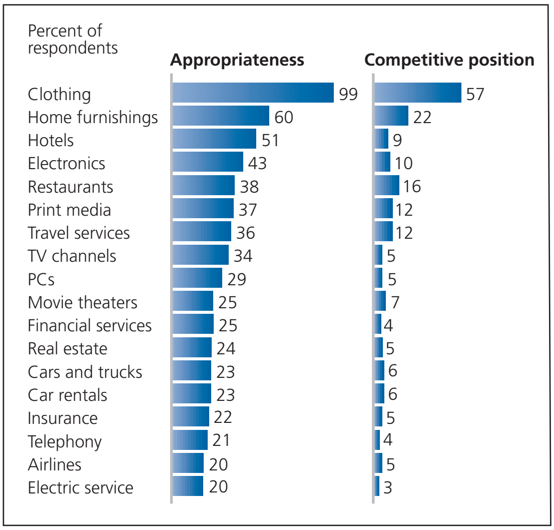


Exhibit 2

Exploiting the potential for brand leverage outside core category: Ralph Lauren



aged their brands even more quickly. By comparison, GE spent 40 years focused almost entirely on lighting products before leveraging its brand name into appliances, and Gillette waited 25 years to move from razors to shaving cream.

What, then, are the key factors for successful brand leverage? Which brands can be leveraged widely and which cannot? To find out, it is necessary to determine where a brand starts – its basic value proposition or performance characteristics, as well as its "personality." Respondents to our survey were invited to react to 30 performance characteristics of the 130 brands. In retailing, for example, they were asked about product selection, the availability of products, and the convenience of locations; in personal financial services, the questions dealt with accuracy, interest rates, and front-line service. Respondents were also asked to react to 25 corporate personality characteristics, including "fun," "useful," "trusted," and "respected."

The next step was to explore how receptive consumers were to the idea of leveraging brands. Industry experts examined the expansion opportunities for each of them, and that appraisal was used to develop leverage options. Respondents were then asked two questions about the options of each brand, both within and beyond its current category*: first, would it be appropriate for this brand to offer a product or service in a particular area and, second, would respondents expect the brand to perform better, the same as, or worse than currently available brands?

Ralph Lauren was one of the brands. Consumers believed that within the men's clothing market it would be appropriate for Ralph Lauren to increase its presence in accessories (78 percent), casual clothing (73 percent), and business clothing (71 percent). But they thought leverage would be less appropriate in the women's clothing sector and less still in children's clothing, travel, and linens. On the performance side, taking accessories as an example, 39 percent of the respondents said that they thought Ralph Lauren would perform better than did existing brands. The combination of these factors –

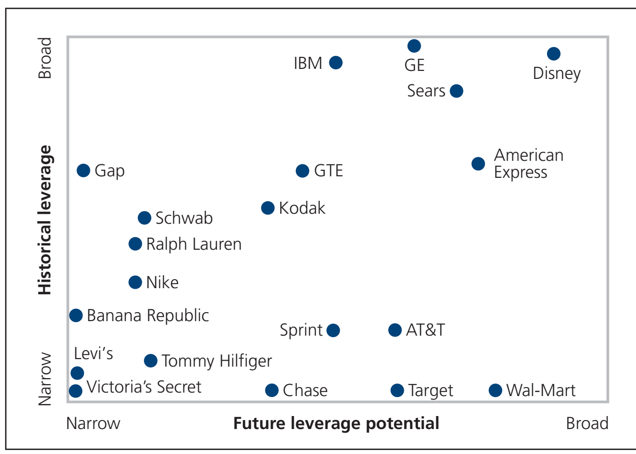
* Credit cards, say, would be within State Farm's core category; real estate or travel services would be outside it.

appropriateness and competitiveness – helps indicate how successful Ralph Lauren might be in leveraging its brand in a variety of related areas (Exhibit 2).

Looking beyond the core category, Ralph Lauren was rated for its ability to move out of its own industry and into 17 others, including most leading consumer categories. To establish a benchmark, the brand was first rated in its own category – clothing – where it scored 99 percent. It went on to score moderately well in home furnishings but fell off steadily in hotels, electronics, restaurants, print media, and travel services. Thereafter it became relatively weak.

Exhibit 3

Historical brand leverage and potential for future brand leverage



We worked through this analysis for all of the brands. Then the consumers' perception of the leverage potential of each was mapped against its current degree of leverage (Exhibit 3). To consumers, brands that in the past have been focused, such as Levi's and Victoria's Secret, should remain narrowly focused. By contrast, consumers think that Disney, IBM, and Sears – all widely leveraged in the past – can leverage themselves widely in the future.

Of course, there are other interesting brand positionings in Exhibit 3. The research suggests, for instance, that Wal-Mart and AT&T, which are less leveraged than some other companies, do indeed have considerable license from consumers to leverage brands into new areas. Whether these companies exploit that potential remains to be seen.

In general, however, it seems that the two ends of the spectrum are the key areas of the map shown in Exhibit 3. Focused brands, with narrow historical and future leverage potential, must focus primarily on their core categories while seeking to capture closely related leverage opportunities. Diversified brands, with broad historical and future leverage potential, have opportunities to build a broader brand across many products and categories.

This may seem like an elaborate way of saying that if a brand has done well with a focused strategy it should stay focused, while if it has diversified successfully it should continue to do so. However, many companies do not have a clear idea about the best way to manage a focused or diversified brand.

Furthermore, the problem is often the fact that a brand is stuck in the middle. To know what to do, companies must understand the key elements of a focused and a diversified strategy.

Success strategies for focused brands

Two main strategic imperatives have helped focused brands succeed. The first is to strive to "own" the category and to lead in its development, which means making a brand's personality thoroughly distinct and then constantly seeking to broaden the way consumers think about the category and the brand. The second is to establish the brand as truly pervasive by seeking out every possible sales opportunity – "swarming" sales channels and geographies to maximize penetration – and using alliances to build presence quickly.

Owning and broadening the category

Respondents to the survey were asked to rate brands according to 25 personality characteristics. In the case of focused brands, six characteristics were cited with particular frequency: "youthful," "fun," "adventurous," "exclusive," "outdoorsy," and "romantic." High-potential focused brands performed remarkably better on these dimensions than did other brands. Victoria's Secret, obviously a romantic brand, actually scored a whopping 72 percentage points more on the romance scale than did other brands of clothing. Levi's scored a robust 40 points more as an outdoorsy brand.

Besides developing distinct personalities, focused brands should always seek to broaden the definitions of their categories. Although they are constrained by the way consumers think about those categories, they can, cautiously at least, do things to change those ideas. Gillette moved from a tight focus on razor blades into shaving cream and aftershave, effectively redefining its (still narrow) category as men's grooming products. Then it added women's shaving and grooming products to make the business fit into the personal care category.

Redefining categories opens the playing field for a category brand. Coca-Cola managed to redefine its category from cola to carbonated soft drinks to liquid refreshment. Dell broadened its category in the direct computer business from low-end personal computers to expensive servers.

Capturing all occasions

Focused brands also drive shareholder value by going after every possible opportunity. Coca-Cola is one of the best examples of a company that swarms sales channels and geographies – not only vending machines, fountain service, supermarkets, and convenience stores, but also movie theaters, video stores, and even taxis, where the company places coolers.

Nike too has pushed its way into new channels. Its single-brand superstore Nike Town (a channel it effectively invented) powerfully reinforces the company's brand image. Nike has also pursued geographic breadth: since 1994, it has expanded into more than 100 nations across the Asia-Pacific, Europe, Latin America, and North America.

Focused brands can create additional value by using alliances to expand their presence rapidly. Starbucks has teamed up with United Airlines and the bookseller Barnes and Noble; Wal-Mart has formed alliances with international retailers, including Cifra, its partner for expansion in Mexico. Meanwhile Intel, perhaps the classic example of a company that uses alliances, has collaborated with PC hardware manufacturers to establish the first and strongest real brand in the computer chip industry.

Success strategies for diversified brands

At the other end of the spectrum, successful diversified brands pursue three strategies: they find and constantly reinforce the golden thread that knits together their diverse businesses; they invest in building high-credibility personalities; and they systematically leverage their brands by cross-selling products to customers and by restructuring industries where existing brands are weak.

Creating the golden thread

For Sony, the simple, elegant design of all its products is the golden thread. Design defines a core part of the brand's personality and ensures that customers always experience the brand in a consistent way. Disney's golden thread is the concept of wholesome fun.

Building "high-credibility" personalities

All brands must have characteristics that enhance their credibility and inspire trust in consumers. But broadly diversified brands seem to distinguish themselves most in the areas of trustworthiness, leadership, and intelligence.

> Successful diversified brands find and constantly reinforce the golden thread that knits together their businesses

IBM and AT&T, which are both significantly stronger in such elements than their competitors, illustrate the point well. The two companies communicate confidence: consumers feel that if they buy these brands, they will not go wrong; as the saying goes, "Nobody ever got fired for buying IBM." For a few years, when IBM seemed to have forfeited its leadership of the computer industry, this precept may have been untrue. But it is a measure of the brand's underlying strength that after a few strong years the company is back on top.

Companies with diversified brands reinforce their personalities with broad corporate image advertising on these themes. You can "do more" with American Express. IBM offers "solutions for a small planet." And though any number of companies could claim to "bring good things to life," it is GE that has successfully used this phrase as an advertising slogan.

Leveraging aggressively

Having found the golden thread and built a personality around it, diversified brands move both to cross-sell and to claim as their own new industries where brand intensity is low – and where their brand thus enjoys a competitive advantage.

American Express is a good example of cross-selling. It markets a range of products and services – from financial advice to investment products and travel packages – to its 26 million cardholders. Sears, meanwhile, has been successful developing new businesses outside its core retail activities. Almost 75 percent of the company's growth over the past ten years has come from nonretail sources.

Consumers are cautious when hitherto focused brands move into unrelated product areas

The Sears Home Central service business, for example, repairs appliances, replaces windows and doors, repairs air conditioning and heating equipment, and provides pest control services, among other things. Branding in the market is weak and competition is fragmented, which means that Sears, with a relatively low market share, is already the leader in each segment. It remains to be seen whether the company can truly restructure these industries, but results so far suggest that its base of 70 million households could propel it into a strong lead.

Sears is not alone in following this strategy. Many strong companies are using their brands to move quickly into industries with low brand intensity. Disney in cruise lines and Hewlett-Packard in computer printers are just two such companies.

Given the economics of leverage, why shouldn't every brand try to diversify? Remember two things. First, consumers are cautious when hitherto focused brands move in to unrelated product areas, so if a company plans to take this route it should do so with extraordinary energy, commitment, and effort. Second, companies should make sure that they have exhausted the possibilities close to home before expanding out of it. The most successful focused brands have shown great creativity in steadily broadening the definitions of their categories – an approach that might be described as a slow but sure diversification within the original focus.

Help for those stuck in the middle

What is the right leverage strategy for those companies that sit somewhere in the middle between the fucused approach and the extended one? There are two strategic themes to keep in mind.

First, a company should determine how many businesses that are underdeveloped or have low brand intensity it could compete in successfully. If a business is underdeveloped, and it appears that consumers would respond well to better quality, consistency, and credibility, a leverage strategy beckons. But if competitors are deeply entrenched, the safer course might very well be to stay narrowly focused and try to expand the company's category in the minds of consumers.

Second, the personality of a brand may affect the choice of direction the company takes. Brands that rate well on such high-credibility measures as leadership and trustworthiness can move beyond their core businesses. Brands that score better on lifestyle themes might be wise to follow a more focused strategy.

Companies considering the diversified approach should also think about whether they have customer bases that are sufficiently large and loyal to provide cross-selling opportunities. A critical mass of this sort may be the bridge that makes it possible for focused brands to make the transition to a diversified future.

Our research suggested a strong relationship between the degree of a company's success and four organizational elements:

1. Build brand stewardship. A successful company views its brand as a treasured asset and treats it as such. Among the more focused brands, driven CEOs like Phil Knight at Nike, Howard Schultz at Starbucks, and Charles Schwab at Schwab can be an important factor.

2. Embed brand leverage issues in planning. It is critical to ensure that brand leverage is explicitly considered at the most basic level of corporate planning, where the art of branding meets the science of branding and creativity meets fact-based reality.

3. Develop supporting capabilities. Focused brands (such as Nestlé with its brand managers) build organizations that effectively manage possible conflicts between sales channels and countries. Diversified brands (for example, Disney with its strategic planning group and Sears with its relentless focus on cross-selling) know how to develop new businesses and cross-selling opportunities.

4. Put appropriate metrics in place. The least developed area of organizing for brand leverage is metrics. Emerging ones include measures for the size and growth of a franchise (such as The Gap's clothing consumption benchmark), for a company's share of wallet (Sears's annual survey of where consumers spend their money), and for progress in building a desired image. Sharpening this sort of metrics will become increasingly important in the future.

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The branding game is shifting from brand building to brand leverage. A brand can grow quickly if its owner maintains its performance, personality, and presence and builds on this foundation to create innovative strategies for expanding the business through focus or diversification. And as the game shifts, so does responsibility for planning it – from the brand manager's office to the boardroom. Q