

Linking Brand Equity to Market Valuation



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Gelb
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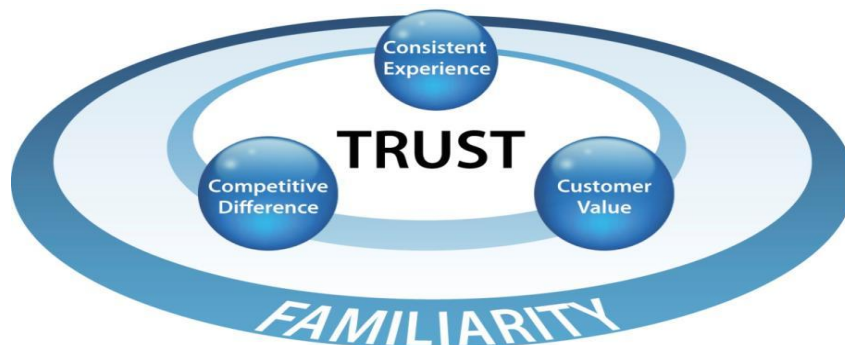
Overview

Are brands truly assets that enable their owners to generate superior returns over time? If the answer to this question is yes, then effective brand-building efforts that enhance the value of a brand should in turn enhance shareholder value. And unlike other competitive advantages such as cost, location or technology where gaps between multinational firms are eroding at an increasingly rapid pace, brands hold the promise of providing a competitive advantage that is sustainable in the longer term.

This paper draws upon a recent Corporate Brand Equity study and describes our methodology for defining and measuring brand equity for oilfield service firms in a way that directly links customer behavior to investor behavior.

Getting Started: Measuring Brand Equity

Going beyond simple "brand strength" analyses, Gelb's Brand Trust model utilizes survey research of a brand's target market to quantify the individual sources contributing to brand equity. Awareness and a certain level of familiarity are prerequisites for consumers to have any predisposition towards a company's products or services. Next comes affinity towards the brand as measured by perceptions of brand reputation, willingness to pay a premium for the brand, and satisfaction with customer brand interactions. The outcome of familiarity and favorability is a level of vesting wherein customers trust the brand and may even be prepared to stake their own personal or professional credibility by recommending the brand to others.



A trusted brand consistently delivers superior value compared to competing brands

Components of the Brand Trust model:

- ❖ **Familiarity:** What is the market's awareness and understanding of what you offer?
- ❖ **Competitive Difference:** How does the market distinguish one brand from another?
- ❖ **Customer Value:** How are options evaluated and decisions made?
- ❖ **Consistent Experience:** How well does the brand deliver on its promise?
- ❖ **Trust:** What is the strength of the relationship with the brand?

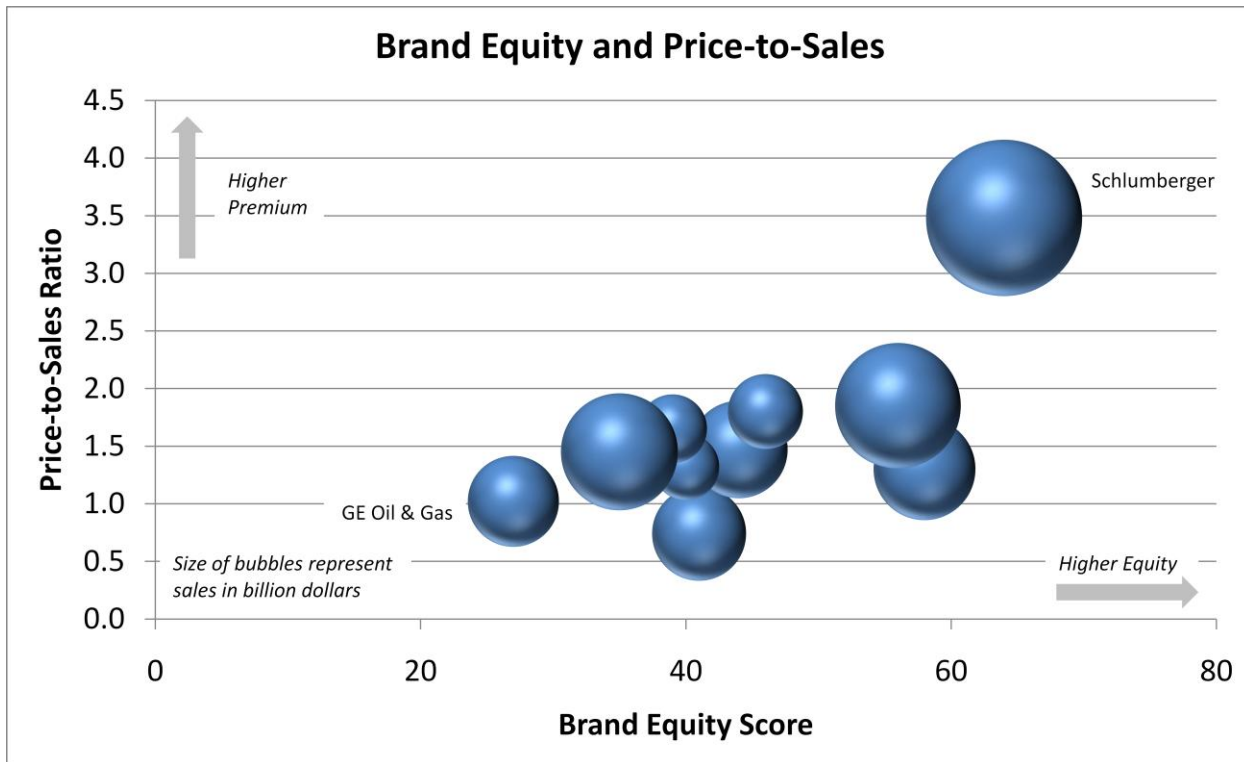
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Gulf Research Corporate Brand Equity

Gelb with Gulf Research, our joint venture with Gulf Publishing Company, has been tracking brand equity for leading oilfield product and service companies on an annual basis since 2004. The syndicated Gulf Research surveys employ the Brand Trust model outlined on the previous page to provide a standardized score of corporate brand equity. The latest 2009 Gulf Research study is based on responses from more than 600 oilfield professionals worldwide and covers assessments for 10 firms: Baker Hughes, BJ Services, Cameron, FMC Technologies, GE Oil and Gas, Halliburton, National Oilwell Varco, Schlumberger, Smith International, and Weatherford. We use results from this recent study to explore the connection between corporate brand equity and market valuation.

Relationship with Revenue Multiple

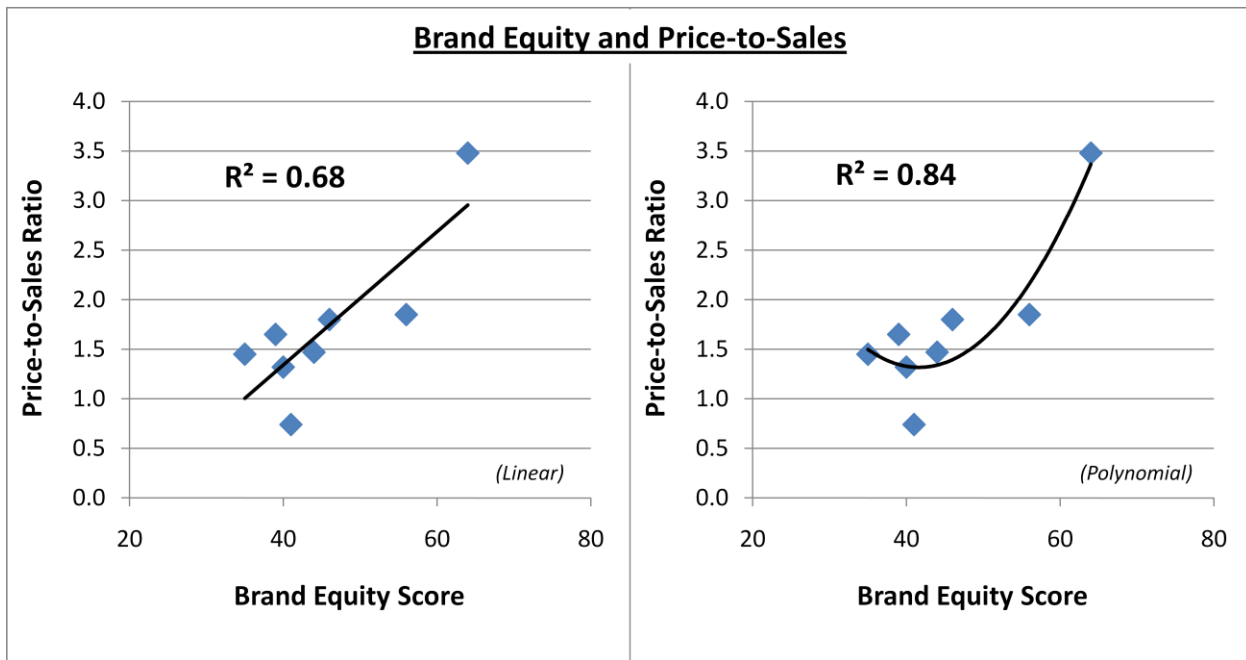
Investors rely on a portfolio of tools to form an opinion on the value of a company or a stock. The “market price” that both buyers and sellers collectively determine is, in most cases, more than just the book value, i.e., the value of the tangible assets—land, buildings, machinery, receivables, etc. Often a price premium is largely in recognition of the intangible assets of a firm, including the future earnings power of the brand. A well-established price multiple used to track valuations in the financial markets is a stock’s price-to-sales ratio. Many investors look at sales revenue as a reliable indicator of a company’s size and growth. In the chart below, we investigate the relationship between the year-end price-to-sales ratios for 10 oilfield service firms with their brand equity performance.



Note: Price-to-Sales ratio for GE used as proxy for GE Oil & Gas

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A visual examination of the chart on the previous page suggests that there indeed exists a relationship between brand equity and the premium investors place on the share price of a company relative to its peers. To better understand the strength of this relationship, we first identified and removed two outliers from our final analysis. (The outliers were omitted on the basis of the majority of the company's business activities being outside of the oil & gas industry in one instance—comparing price-to-sales ratios across industries is not recommended due to typically different capital structures—and involvement in a large acquisition in the other case.)



As the charts above illustrate, there is a moderate to strong degree of correlation between corporate brand equity as measured by the Gulf Research studies and the price-to-sales multiple for oilfield service companies. The strength of this correlation varies depending upon the type of regression model (linear or polynomial) applied. The stronger fit statistic (R^2) for the polynomial function suggests there is an increasing level of premium associated with leading companies that are able to clearly distinguish themselves from their peers.

Relationship with Earnings Multiple

Another valuation metric that is perhaps even more popular is the price-to-earnings multiple or P/E ratio. The trouble with the P/E ratio is that earnings are a complicated "bottom-line" number, sometimes reflecting non-recurring events. Market volatility, especially during the last few years, further muddies the waters. Nonetheless, when viewed over the longer term, share prices and earnings volatility should smoothen out and one should be able to discern patterns between leading companies. With this hypothesis in mind, we reviewed the historical mean P/E ratios over the last 10 to 15 years for some of the leading oilfield service firms and present them in the table on the next page.

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Oilfield Service Company	Net Promoter Score	Historical Mean P/E Ratio
Schlumberger	22	26
Baker Hughes	14	24
Halliburton	5	20

*Source for P/E ratios: BofA Merrill Lynch Global Research
Historical P/E multiples measured from 1996 (SLB & HAL) and 1999 (BHI)
Net Promoter is a registered trademark of Satmetrix Systems, Inc., Bain & Company and Fred Reichheld*

The Gulf Research oilfield brand equity studies have consistently found that companies with the highest brand equity performance, measured according to our proprietary brand trust model, are highly correlated with customer loyalty. Trust and advocacy are important indicators of loyalty. In the table above, we include an advocacy metric, the Net Promoter Score, which is the result of subtracting those customers who will recommend a company or brand to others from those who would not (detractors). The table highlights a positive relationship between the number of net promoters and the historical mean P/E ratios for the three companies—as the number of advocates increases, so does the P/E ratio. Clearly, organizations with high brand equity and customer trust have been rewarded by investors with higher premium multiples benefiting their share prices over the long term.

Taking Action

Corporate brands are living assets that can grow or wither. Gelb's analytical approach to measuring brand equity in the Gulf Research studies provides oilfield service firms with a wealth of actionable information that has proven useful in nurturing brands and more importantly, enhancing shareholder value. Armed with data on brand equity performance for themselves and their competitors, marketers are able to make smart decisions about their current strengths and opportunities for improvement, build customer loyalty, and command premium pricing. In addition to measuring brand equity at the corporate level, Gelb's brand trust model is being used to measure brand equity at the market-sector level for oilfield service firms, as well as in other industries outside of oil and gas such as finance, industrial companies and healthcare.

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About Endeavor

Endeavor Management, is an international management consulting firm that collaboratively works with their clients to achieve greater value from their transformational business initiatives. Endeavor serves as a catalyst by providing pragmatic methodologies and industry expertise in Transformational Strategies, Operational Excellence, Organizational Effectiveness, and Transformational Leadership.

Our clients include those responsible for:

- Business Strategy
- Marketing and Brand Strategy
- Operations
- Technology Deployment
- Strategic Human Capital
- Corporate Finance

The firm's 40 year heritage has produced a substantial portfolio of proven methodologies, deep operational insight and broad industry experience. This experience enables our team to quickly understand the dynamics of client companies and markets. Endeavor's clients span the globe and are typically leaders in their industry.

Gelb Consulting Group, a wholly owned subsidiary, monitors organizational performance and designs winning marketing strategies. Gelb helps organizations focus their marketing initiatives by fully understanding customer needs through proven strategic frameworks to guide marketing strategies, build trusted brands, deliver exceptional experiences and launch new products.

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