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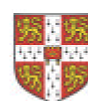
Exploring the moderators on the branding strategy-financial performance relationship

Zyglidopoulos, S.C., Alessandri, S.W. and Alessandri, T.M.



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Author contact details are as follows:

Stelios Zyglidopoulos
Judge Business School
University of Cambridge
szyglidopoulos@yahoo.com

Sue W. Alessandri
S.I. Newhouse Communications Center
Syracuse University
swalessa@syr.edu

Todd M. Alessandri
Martin J. Whitman School of Management
Syracuse University
tmalessa@syr.edu

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Please address enquiries about the series to:

Research Support Manager
Judge Business School
Trumpington Street
Cambridge CB2 1AG, UK
Tel: 01223 760546 Fax: 01223 339701
E-mail: research-support@jbs.cam.ac.uk

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Stelios C. Zyglidopoulos
Judge Business School
University of Cambridge
Trumpington Street
Cambridge, CB2 1AG, UK
Tel.: 44 (0) 1223-760576
Fax: 44 (0) 1223-339701
E-mail: szyglidopoulos@yahoo.com

Sue Westcott Alessandri
S.I. Newhouse Communications Center
Syracuse University
215 University Place, Syracuse, NY 13244, USA
Tel: 1 315 443-5819
E-mail: swalessa@syr.edu

Todd M. Alessandri
Martin J. Whitman School of Management
Syracuse University
721 University Avenue
Syracuse, NY 13244-2450, USA
Tel: 1 315 443-3674
E-mail: tmalessa@syr.edu

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Exploring the Moderators on the Branding Strategy – Financial Performance Relationship

Abstract

This paper explores the moderating roles that corporate reputation and business strategy have on the impact that a firm's branding strategy has on its financial performance. Drawing on the brand management, strategic management, and corporate reputation literatures, we investigate whether brand strategy has an impact on a firm's financial performance, and whether this relationship is moderated by the firm's reputation and business strategy. Our findings are as follows. First, we found that firms following branded strategies tend to outperform firms following monolithic ones. Second, we found that, although prior firm reputation has a positive impact on the firm's performance, it does not interact significantly with its branding strategy. Finally, our findings indicate that there is a fit between differentiation and a branded approach to brand strategy, and equally between low cost and a monolithic approach.

INTRODUCTION

This paper explores the moderating roles that corporate reputation and business strategy have on the relationship between a firm's branding strategy and its financial performance. A firm's branding strategy refers to the way a firm, through its products, presents itself to the world (Aaker, 2004; Aaker & Joachimsthaler, 2000a, 2000b; Olins, 1990). It ranges, according to Olins (1990), from monolithic, where the firm uses its corporate brand as the overarching brand for all its products, to an endorsed strategy, where the firm uses a particular product brand name alongside its corporate brand, and finally, a branded strategy, where the firm develops unique brand names for all of its individual products – also known at the Procter & Gamble approach.

Branding strategy has received an extensive amount of attention in the literature (Aaker, 2004, 1996; Aaker & Joachimsthaler, 2000; Alessandri & Alessandri, 2004; Olins, 2002, 1990), but its impact on financial performance has not been adequately explored. Typically, it is assumed that a strong brand will have a positive impact on the bottom line of the firm, and numerous authors give advice on how firms can achieve such a strong brand (Aaker & Joachimsthaler, 200l; Cliffe & Motion, 2005; Jones & Slater, 2003; Munoz & Kumar, 2004; Yakimova & Beverland, 2005), but the general impact that the overall choice of branding strategy has on financial performance has not been adequately explored. In this paper, we investigate the potential impact that different types of branding strategy have on financial performance. However, this impact cannot be adequately understood unless we also examine the potential moderating effects of the firm's reputation and business strategy. In brief, the main reasons we need to address these two factors if we are to properly investigate the financial performance impact of a

firm's branding strategy are the following. First, not all kinds of branding strategies draw to the same extent on the firm's reputation. For example, it is reasonable to expect that monolithic strategies draw more on the firm's reputation than branded ones (Olins, 1990). Second, the success of a particular branding strategy might depend on its fit with the overall business strategy of the firm. For example, it is reasonable to expect that it will be financially beneficial for a firm following a differentiation strategy (Porter, 1980) to benefit from a branded strategy, as it would be able to fine tune its offerings to its various customer groups. And, in a similar manner, one might also expect that a firm following a low cost strategy (Porter, 1980) to benefit from a monolithic approach, as such an approach would allow it to reap significant economies of scale in advertising and promotion expenses.

To achieve its goals, the remainder of the paper proceeds as follows. First, we briefly discuss the major concepts of our paper. Second, drawing on the corporate reputation and strategic management literatures, we develop a number of hypotheses with regard to the roles that corporate reputation and business strategy play in the relationship between branding strategy and financial performance. Subsequently in our methods section, we test these hypotheses and report our findings. The paper concludes with a discussion of our findings and their implications for further research and managerial practice.

MAJOR CONCEPTS

Since this research deals with several major concepts, including branding strategy, business strategy, and corporate reputation, in this section we briefly define and discuss

these concepts before we proceed to address their impact on the financial performance of the firm.

A firm's *branding strategy* is synonymous with its brand architecture, which Aaker and Joachimsthaler (2000) define as the "organizing structure of the brand portfolio that specifies the brand roles and the relationships among brand and different product-market brand contexts" (2000: 134). Put more simply, a firm's branding strategy reflects the explicitness of the relationship between the corporate brand and the firm's product brands. Olins (1990) delineates three types of branding strategies that fall along a continuum: monolithic, endorsed and branded.

A firm that chooses to employ the corporate brand as the overarching brand is employing a monolithic branding strategy. In the middle of the continuum, employing the corporate brand alongside a product brand reflects an endorsed strategy, and at the end of the continuum is the branded strategy, using only individual brand names without reference to the corporate brand (also called the Procter & Gamble approach because the emphasis is on the product brands, in some cases to the total exclusion of the corporate brand). A monolithic branding strategy provides firms with the strength of consistency. By employing the corporate brand exclusively, every promotional activity supports the others, which allows the firm to obtain a certain marketing synergy. More importantly, however, many firms choose a monolithic branding strategy because they believe that their corporate reputation might be extended to a large range of product brands (Olins, 1990). Conversely, a branded strategy draws attention away from the corporate brand. Thus, depending on the branding strategy of a given firm, the corporate brand can play either a major or a minor role in the face that the firm presents to the world.

Concerning the *business strategy* of the firm, the term refers to the extent that a firm follows a particular type of generic strategy (Porter, 1980) – low cost, differentiation, and focus – or, the adapted generic strategies that Miller and Friesen (1986a, 1986b) suggested, which separate differentiator companies into product and marketing differentiators. In this paper, we are basically dealing with two possible aspects of business strategy, low cost and differentiation. Briefly, drawing on Porter (1980), a low cost strategy is one where the firm focuses all of its efforts on reducing its cost structure vis-à-vis its competitors and offers a product similar to them, but at a lower cost. A differentiation strategy is where the firm offers a superior/unique product at a premium price.

A firm's *reputation* is a reflection of what stakeholders think and feel about that firm (Ferguson, Deephouse & Ferguson, 2000). Fombrun (1996) writes that a firm's reputation "embodies the general estimation in which a company is held by employees, customers, suppliers, distributors, competitors, and the public" (p. 59). Scholars typically agree that a firm's corporate reputation is formed over time by repeated impressions of the corporate image (Gray & Balmer, 1997, 1998; Markwick & Fill, 1997). However, the reputation of a firm is not a single-dimensional construct, but a multidimensional one, as many have argued (Zyglidopoulos & Phillips, 1999), and it can be discussed with relation to different stakeholders, or different firm traits.

THEORETICAL DEVELOPMENT

In the following sections, we first address the main reasons why we expect that the choice of the firm's brand strategy will affect its financial performance, and proceed

to discuss the moderating impact that corporate reputation and business strategy might have on this relationship.

Brand Strategy and Financial Performance

As discussed earlier, a great part of the literature identifies brand strategy, or brand architecture, as a very important factor in the financial success of a corporation. However, not enough research has addressed the issue of whether brand strategy is linked with the performance of the firm. In other words, do firms following a branded strategy (Procter & Gamble approach), perform better than firms following a monolithic or endorsed approach?

Of course, to a great extent, the answer will be product or industry contingent, but even at a more general level, arguments for either position could be made. For example, firms following a monolithic branding strategy enjoy brand consistency, economies of scale in advertising, and can use their corporate reputation in a number of products (Alessandri & Alessandri, 2004; Olins, 1990). On the other hand, a firm following a monolithic strategy might also dilute its corporate brand too much by extending it to inappropriate products, and therefore suffer financially. And, similar arguments can and have been made for branded and endorsed brand strategies. Therefore, even if we cannot reasonably argue for the financial superiority of a branded approach over a monolithic one, or vice-versa, we can expect a link between the firm's brand strategy and its financial performance.

Hypothesis 1: The branding strategy of a firm will be related to its financial performance.

Corporate Reputation and Branding Strategy

The link between corporate reputation and financial performance has long been argued for in the corporate reputation literature for quite some time. A number of research streams have argued and found evidence that a good corporate reputation has a positive effect on the firm's performance and stock market valuation. First, in line with the resource-based view of the firm, some researchers have argued that a good corporate reputation can be seen as a valuable, rare, non-substitutable and inimitable firm resource, and as such a potential source of sustainable competitive advantage (Barney, 1991; Dierickx and Cool, 1989; Deephouse, 2000; Fombrun, 1996; Hall, 1993; Rumelt, 1987). Also, in a survey he conducted with British chief executives, Hall (1992) reported that executives also tend to agree with this position. In particular, the executives in the survey not only identified corporate reputation as their firm's most valuable intangible resource, but also said that it was the one intangible resource that it would take them the longest to replace, if they were to start from scratch.

Second, a number of empirical studies have found a significant relationship between corporate reputation and firm performance. For example, McGuire, Scheeweiss and Branch (1990) found evidence that the firm's reputation for management quality has an impact on financial performance and vice-versa. Roberts and Dowling (1997, 2002) found evidence that firms with good corporate reputations were more likely to attain and sustain superior profitability. Deephouse (2000), using a variant of corporate reputation called media reputation, which he defined as "the overall estimation of a firm presented

in the media" (Deephouse, 2000: 1091), found that a positive media reputation had a significantly positive effect on the firm's financial performance.

Therefore, given the impact that corporate reputation has on the financial performance of the firm, and the fact that different brand strategies utilize this resource to very different degrees, it is reasonable to expect that corporate reputation to play a significant moderating role in the brand strategy-financial performance relationship. In addition, one might expect firms following a monolithic brand strategy to derive the greatest benefit from a solid corporate reputation, since they are already using an existing resource that draws on the brand name.

Hypothesis 2: Corporate reputation will moderate the relationship between branding strategy and financial performance.

Business Strategy and Branding Strategy

Previous management research has focused on the broad relationship between a firm's marketing strategy and its business strategy. Biggadike (1981) highlighted the common notion of market segmentation between business and marketing strategies. Incorporating the traditional 4 Ps of marketing (product, price, place and promotion), Slater and Olson (2001) developed a taxonomy of marketing strategies and matched them with business strategies, with results indicating heightened financial performance when broad marketing strategies are properly aligned with business strategies. As implied by Slater and Olson (2001), for broad marketing strategies, in order to achieve heightened performance, firms must be organized to exploit the promotion of the corporate brand,

and ultimately to enhance the firm's corporate reputation. Previous research has borne this out. Schulze (1994) suggests that firms earn rents by matching resources to market demand, and Blois (1983) writes that a firm's marketing policies and any restructuring of the organization should be inseparable. Finally, Ferguson et al. (2000) suggest that one of the factors that affects a firm's reputation is its basic strategy resources and the resources it uses to serve multiple markets.

Similarly to Slater and Olson (2001), we argue that those firms that "match" their business strategies to their brand strategies will experience better performance. For example, a low-cost business strategy might fit better with a monolithic brand strategy, because a monolithic strategy allows for significant economies of scale in marketing and is easier to administer. On the other hand, one could also build the argument that a differentiation strategy fits better with a branded approach, as such an approach allows for the fine tuning required in each brand to maximize its differentiation value, an approach not always possible with a monolithic or even an endorsed strategy.

Hypothesis 3: Business strategy will moderate the relationship between branding strategy and financial performance.

RESEARCH METHODOLOGY

Data Sources

Overall, three sources of data were used: the America's Most Admired Companies (AMAC) survey, COMPUSTAT, and firm annual reports. The AMAC survey measures corporate reputation along eight dimensions and has been conducted by

FORTUNE magazine yearly since 1983. Given the limited sources of longitudinal reputation data, we drew on this survey for initial data collection. More specifically, our initial sample consisted of the 410 companies that appear in the AMAC database in 1995 – the latest year for which we had AMAC data. However, given that we needed to match data for these companies with data drawn from their annual reports for the years 1996, 1997, or 1998, our usable sample was reduced for a number of reasons[1] to 101 data-points[2].

Variables and Analysis

Our *dependent variable*, financial performance, was measured through the use of the average ROA for the financial years of 1996, 1997, and 1998, drawn from Compustat. We used ROA to measure the financial performance of the firm because of its "stability and comparability across firms" (Kim, Hwang, and Burgers, 1989). We selected the years 1996-1998 as the period immediately following our 1995 measurement of reputation: we would expect the brand strategy a firm used during these three years to draw on the prior (1995) reputation of the firm.

As *control variables*, we used firm size and firm visibility in the media. Data for firm size were drawn from COMPUSTAT, and the variable was measured as the natural logarithm of the average employee number for the three years under investigation. Data for visibility were drawn through ProQuest, and the variable was operationalized by the number of articles in newspapers, trade magazines, and business magazines which mention the name of the particular firm for the relevant years.

[1] The greatest limiting factor was that annual reports for the relevant years could not be located.
[2] Also one data point was an outlier and was eliminated from the sample.

Finally, as *independent variables*, we used brand strategy, corporate reputation, and business strategy. First, brand strategy was measured with the help of raters, who after reviewing a firm's annual report from one of the three years under investigation, rated the firms with respect to three dimensions developed by Alessandri and Alessandri (2004). See Appendix A for more details of the specific items rated. To ensure interrater reliability, two raters were used to rate about 50% of the firms. The Cronbach alpha for the firms rated by both raters was about 80 %. Second, corporate reputation was measured through the rating that the AMAC database provided for the year 1995, a measurement of reputation that has been used regularly in the field. The ratings for 1995 were used to make sure that corporate reputation predated the firm's brand strategy, and therefore it would be reasonable to assume that the firm's brand strategy drew on the reputation and not vice-versa. Third, the firm's business strategy was measured using a similar procedure as we used with brand strategy. Drawing on 10 out of the 15 dimensions Kim and Lim (1988) developed to measure whether a firm followed a particular generic strategy, and following a similar factor analysis procedure, we identified two business strategy dimensions that characterized the business strategies of the firms in our sample: differentiation and low cost (See Appendix A).

Finally, we tested for the above hypotheses through seven forced entry regression models.

FINDINGS

Insert Table 1 about here

Table 1 contains the correlations of the main variables involved in our analysis, and Tables 2 and 3 the results of our analysis. As can be seen from Table 2, Model 1, we did find support for hypothesis 1, which states that a firm's brand strategy would affect its financial performance, and more specifically, given the negative sign of the standard coefficient for brand strategy, it seems that firms following a branded strategy approach tend to outperform firms following monolithic or endorsed strategies.

Second, from Table 2, Models 2, 3, we found no support for hypothesis 2 Reputation does have, as expected, a significant impact on the firm's financial performance, but it does not interact with its brand strategy, as the interaction effect is not significant in Model 3.

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Insert Tables 2 and 3 about here

Third, from Models 4, 5, 6 and 7, we did find support for hypothesis 3, which states that a firm's brand strategy would interact with its business strategy. More specifically, we found that differentiation had a significant negative interaction effect with the firm's brand strategy, indicating that there is a fit between a branded approach and differentiation. Also, we found that low cost had a positive interaction effect with the

firm's brand strategy, indicating that a monolithic approach fits better with a low cost one, as expected.

Discussion and Conclusion

There are at least two ways in which the findings from this paper contribute to the literature of strategic management. First, our findings offer support for the position that a fit between a firm's marketing strategy and its business strategy has positive implications for financial performance (Slater and Olson 2001). More specifically, our findings indicate that monolithic approaches to brand strategy fit better with low cost business strategies, probably because these brand strategies allow for significant cost savings through economies of scale in marketing. However, branded approaches to brand strategy seem to fit better with a differentiation strategy. Most likely, this finding indicates the limits of the monolithic approach to brand strategy, as it is reasonable to expect that firms following such an approach cannot "stretch" their corporate brand adequately to effectively differentiate their product offerings to highly specialized, and potentially financially rewarding, segments or markets. In other words, a branded strategy allows differentiators to better fine tune their brand to fit their product offering. Of course, this is a more expensive approach, as a firm has to build and rebuild brand after brand, but one that seems to be worth the expense for firms following a differentiation strategy.

Second, our findings contribute to the corporate reputation literature that investigates the significance of corporate reputation. In particular, our findings indicate that there is no interaction between a firm's brand strategy and its corporate reputation, as one might expect. Of course, there is a need for further research on this topic, as it is

possible that corporate reputation influences different brand strategies in a different way, something not visible when one aggregates firms following different strategies.

In conclusion, our major findings from this study can be summed up as follows. First, we found that firms following branded strategies tend to outperform firms following monolithic ones. Second, we found that, although prior firm reputation has a positive impact on the firm's performance, it does not significantly interact with its branding strategy. And, our findings also indicate that there is a fit between differentiation and a branded approach to brand strategy, as there is one between low cost and a monolithic approach.

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Table 1

Correlations

	Size	Visibility	Brand Strategy	ROA	Differentiation	Low Cost	Reputation
Size	**1**						
Visibility	**0.177**	**1**					
Brand Strategy	**0.043**	**0.255**	**1**				
ROA	**0.046**	**0.225****	**-0.172**	**1**			
Differentiation	**0.310****	**0.330*****	**0.194**	**0.309****	**1**		
Low Cost	**0.310****	**0.046**	**0.144**	**0.027**	**0.000**	**1**	
Reputation	**0.333****	**0.287****	**0.058**	**0.418*****	**0.370*****	**0.259***	**1**

Table 2

Regression Analyses – Brand Strategy and Reputation

	Model 1 Brand Strategy		Model 2 Brand Strategy and Reputation		Model 3 Brand Strategy Reputation and Interaction	
Variables	Std. Coefficient	T	Std. Coefficient	t	Std. Coefficient	t
Firm Size	0.006	0.053	-0.121	-1.203	-0.123	-1.234
Visibility	0.289	2.661**	0.187	1.834*	0.158	1.514
Brand Strategy	-0.244	-2.279**	-2.75	-2.808**	-1.093	-1.586
Reputation			0.437	4.206***	0.095	0.314
Brand Strategy X Reputation					0.949	0.234
F	3.332**		7.419***		6.254***	
Adjusted R^2	0.074		.228		0.232	

Table 3

Brand Strategy and Business Strategy

	Model 4 Brand Strategy and Differentiation		Model 5 Brand Strategy, Differentiation and Interaction		Model 6 Brand Strategy and Low Cost		Model 7 Brand Strategy, Low Cost and Interaction	
Variables	**Std. Coefficient**	**t**	**Std. Coefficient**	**t**	**Std. Coefficient**	**t**	**Std. Coefficient**	**t**
Firm Size	-0.076	-0.724	-0.71	-0.736	-0.006	-0.053	-0.026	-0239
Visibility	0.188	1.717*	0.275	2.636*	0.290	2.658**	0.304	2.855**
Brand Strategy	-0.277	-2.688**	-0.464	-4.297***	-2.248	-2-291**	-0.242	-2.290**
Differentiation	0.323	2.896**	1.633	4.492***				
Low Cost					0.037	0.333	-0.766	-2.096**
Differentiation X Brand Str.			-1.365	-3.758***				
Low Cost X Brand Str.							0841	2.297**
F	4.815**		7.286***		2.5**		3.159**	
Adjusted R^2	0.149		0.265		0.065		0.110	

Appendix A

Brand Strategy

1. To what extent does the company use its corporate identity on its individual branded products?
2. To what extent does the company use its corporate identity in advertising?
3. How important is the public's knowledge of the corporate parent in the firm's product branding strategy?

(1 – not at all, 7 – a great deal)

Business Strategy

Drawing on a scale developed by Kim and Lim (1988), we used 10 variables from their original list. More specifically, we asked our raters to answer the following question after reading over the firms' annual reports: to what extent has the firm been using the following activities in their business strategies? (1 – not at all, to 7 – a great deal)

Product differentiation, New product development, High-price product, Advertising, Market differentiation, Image building of the firm and products, After service, Pursuing operating efficiency, Pursuing cost advantage in raw material procurement, Pursuing economies of scale.