

Brand Report 2 | 2012



The Rise of Chinese Brand Equity

The Rise of *Chinese Brand* *Equity*

Executive Summary

The strong growth of the Chinese economy and therefore consumers' fast growing purchasing power is consistently increasing their demand for branded goods. In the past, brands were primarily used to demonstrate social status, independently of whether the brands were fake or not. However, Chinese consumers nowadays are becoming more brand-conscious, as they understand that brands are not only about showing off but can also send a useful signal of quality and are able to fulfill their users' increasing need for self-expression. As a consequence, Chinese consumers are looking for authentic brands that have their roots not only abroad but also in their domestic market. On the supply side, Chinese companies increasingly understand the growing importance brands have for the modern Chinese consumer. As a consequence, they are improving their quality management and investing significant resources for professional strategic brand management. Based on these developments, the present study analyzes the past, present and future monetary development of Chinese brand equity. The main focus of the present study lies on determining and explaining the most important value drivers that will support the future positive development of Chinese brand equity. These value drivers are being analyzed from three different angles: the consumers', the companies' and the Chinese government's perspective.

The results of the present study can be of use for different stakeholders. Firstly, the study can benefit whoever is interested in the Chinese market and brand-driven consumer behavior as the results forecast a growing importance of Chinese brand equity in the near and more distant future. Moreover, companies that are interested in expanding their business to China will gain important insights about the changing and increasingly brand-driven purchase behavior of Chinese companies. And finally, analysts and investors willing to finance Chinese companies will be able to better understand how Chinese companies are gradually becoming brand- and reputation-driven firms able to build strong and valuable brands. They will also gain understanding of how the Chinese government is taking important measures to help Chinese companies build and protect their intellectual property such as brands and patents.

Introduction

“Made in China” is still associated with low-end manufacturing, cheap prices and poor quality. After having opened up its markets to the world, China was initially well known as the world’s work labor camp. Many western companies moved their production plants to the Chinese mainland to benefit from the low costs of labor. Since then, China has experienced an unparalleled fast-growing economic expansion, achieving a 9% annual economic growth rate over several years and thus becoming the world’s second-largest economy after the US. As a result of its growing economy and growing prosperity, China has turned into the second-largest luxury goods market and will probably overtake Japan this year. It is forecasted that sales of luxury goods in China will increase by 24% in 2012 and that more than half of this year’s growth in the global luxury market will come from China.¹ It is therefore not a surprise that established luxury brands such as Prada and Gucci owe a third of their global sales to wealthy Chinese buyers.

In the early days of increased Chinese prosperity, wealthy Chinese consumers’ reason for buying brands was basically to flaunt their wealth and to show off, as the people’s pent-up need to be different and of good standing is huge after having been penniless for a long time. Nowadays, the purchase behavior of Chinese consumers has changed as they have gradually become more sophisticated and demanding. Many Chinese are realizing that brands are not only about showing off, but they can also send a useful signal of quality. Especially middle and high-class consumers are striving for a higher life standard and are no longer easily satisfied with cheap products. Consumers in this group are becoming the new generation of trade-up buyers with quality expectations and a new attitude towards brands. This shifting consumer behavior implies more complex brand-related needs that – if well fulfilled – will raise Chinese consumers’ willingness to pay a price premium solely for the benefits of a strong brand. This in turn will benefit Chinese brand equity.

On the supply side, local Chinese companies cannot rest on their laurels any longer. After being successful in the low-end sector, they are now facing tremendous challenges. Multinational corporations from Europe and the US or South Asia have been attracted to the booming Chinese market, competing intensively against Chinese local companies. The cost advantages Chinese companies had in the old days are no longer strong competitive advantages. Hence, Chinese companies are losing significant market shares to foreign counterparts with high-quality products and services that also deliver a higher brand-specific experience to the customers. Strong brands are teaching Chinese consumers to prefer reputable and quality products. More and more local Chinese companies are realizing the implications of this challenge and trying hard to overcome their strategic disadvantage. Nowadays, there is a positive change of attitude towards brand and reputation management, and Chinese companies are becoming more strongly motivated to build valuable brands.

In a first step, the present study will analyze the past, present and future monetary development of the most valuable Chinese consumer goods brands and compare this development to consumer goods brands from the US and Europe. Secondly, the most important value drivers of Chinese brand equity – the factors that support the future positive development of brand values – will be examined. The study will analyze brand value drivers from three different aspects: Firstly, the increasingly brand-driven consumer behavior of Chinese consumers comprises a variety of factors that have an influence on brand equity. Secondly, for Chinese companies there are several brand value drivers that have a potentially strong impact on brand equity. And finally, the Chinese Government can also foster actual and future brand equity by supporting growth and protecting intellectual property.

¹ Source: “The Middle Kingdom”, *The Economist*, February 17th 2011

Brand valuation methodology

In a first step, BV4 analyzed and selected well known and powerful consumer goods brands from China. At the same time, comparable US and European brands were selected and analyzed in order to compare their brand equity to the Chinese one. The 20 most powerful brands of comparable companies were examined for each of the three regions/countries. In a next step, the monetary brand values of the selected brands were assessed. Not only past and actual brand values were calculated: future brand values were also estimated in order to depict the development of the brand values in the three different regions.

For the monetary valuation of the brands, BV4 applied the Discounted Brand Free Cash Flow approach. This is a scientifically founded method accepted in business practice by analysts and investors. This method determines brand value as representing the actual and future earnings of a company that can be attributed to a particular brand. In practice, brand value corresponds to the sum of future brand-specific earnings discounted to present value. The valuation of the analyzed consumer goods brands was executed in three steps:

(1) Derivation of financial figures

In a first step, the financial and income figures of the brands were determined. In doing so, analysts, industry experts, market studies, financial databases and company-specific information were consulted. Future earnings for each company were forecasted on the basis of the past developments of these figures and on the prospective growth opportunities.

(2) Determination of brand strength

In a second step, the brand strength and therefore the “Brand Value Ratio” (BVR) in percent was calculated, i.e. the part of a company’s income achieved solely thanks to a particular brand. A strong brand implies a high BVR, i.e., the higher the BVR, the stronger the influence of the brand compared to the competition. In order to determine brand strength, the analyzed brands were assessed with specific criteria.

The criteria and thus the value drivers used to determine the BVRs for the brands we examined in China, Europe and the US can be classified in three different categories: there are internal, external and market-specific factors that influence brand strength and finally brand equity. Internal factors are value drivers that come from within a company and can, most of the time, be directly influenced by the company itself. For instance, strategic alignment and implemented brand management are important value drivers. From the external perspective, there are factors such as brand awareness, the various stakeholders’ associations with the brand, quality perception, brand loyalty and brand trust. And finally, the market-specific perspective comprises value drivers such as actual and forecasted development of the markets a brand operates in and also the opportunities and threats associated with the specific markets. Furthermore, the market-specific perspective takes factors such as governmental or juridical circumstances into account that potentially have an influence on the evaluated brands.

(3) Determination of brand value

In a last step, the brand-specific earnings of future periods were discounted to present value using a risk-adjusted interest rate. The sum of these values represents the monetary value of the brand. The risks affecting the stability of future brand-specific earnings were assessed individually and taken into consideration in the risk-adjusted interest rate.

In addition to calculating brand values, BV4 also surveyed several experienced economy experts who are familiar with the Chinese market. They were asked for their opinions in regard to the past and future value development of Chinese brands and the most important drivers of this development. The following experts were interviewed: Daniel Bont, Senior Consultant Asia Pacific (Osec – Business Network Switzerland); Claudio Mazzucchelli, Head of Swiss Business Hub China (Federal Department of Foreign Affairs); Hui Wang-Haymoz, Legal and Compliance Luxury Goods (UBS AG); Prof. Dr. Li Choy Chong, Professor and Director of the Asian Research Centre (University of St. Gallen).

Results of the calculated brand values

In order to compare the development of the calculated brand values, the average brand value of the top 20 evaluated brands was calculated for each country/region. The average brand value per country/region was calculated at four different points of time: in the past (2007), at present (2012), in the future (2015) and in the distant future (2025).

The Figure displays the past, present and future average brand values for each of the three countries/regions. As the first measurement in 2007 shows, average brand equity in China is still very low. Chinese brands are still unknown in global markets and most of the time associated with negative values such as low-quality and fake products – so that Chinese companies are not able to achieve a price premium with their brands. By now, Chinese companies have started to catch up thanks to higher brand awareness in domestic and global markets. A more important factor driving Chinese brand equity is that Chinese companies nowadays are more aware of quality issues and also understand that potential flaws and quality defects can have strong and direct impacts on their reputation and brand. Several Chinese companies have not only successfully met this challenge but also become more brand-conscious, understanding consumers' brand-specific needs and adapting to them.

Based on market research studies, company reports, expert interviews and financial analyses, the financial data of the examined brands were extrapolated in order to calculate future average brand values for each of the examined countries/regions. The forecasted growth of the Chinese economy and therefore the fast increasing purchasing power of its consumers and the expansion in consumer spending will give Chinese brand equity a significant boost in

the future. In addition, growing brand-consciousness and affinity will foster increasingly brand-driven consumer behavior, which in turn will result in more brand equity. Assuming that Chinese companies will continue improving their knowledge and understanding of the benefits of strong brands, they will be able to address the brand-specific needs of the Chinese consumers, which in turn will have a positive effect on brand equity. Besides these important brand value drivers, the Chinese government too is responsible for growing brand equity, as the authorities have been developing a sense for the indispensable value of intellectual property and begun to take measures to support, protect and foster those intangible values being created by Chinese companies.

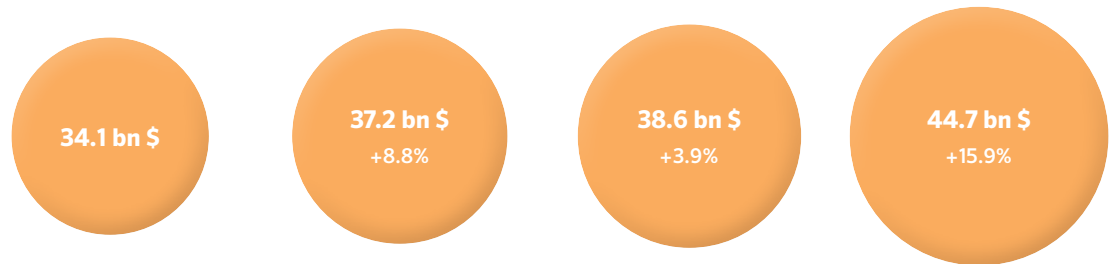
As a result of these developments, it can be assumed that Chinese brand equity will increase at a far higher pace in future than US or European brands. This trend is obvious if we look at the development of the average brand values calculated for each of the three examined countries/regions displayed in the chart. The main part of the present study will now elaborate in detail the most important value drivers supporting the development of Chinese brand equity as illustrated in the chart. The most important value drivers do not apply only for consumer goods brands but also for other Chinese brands with a high potential to create sustainable brand equity in the future. These value drivers are being analyzed from three different perspectives: the consumers', the companies' and the Chinese government's perspective will be taken into consideration.

Please note that we cannot, of course, predict brand equity development as we present it with certainty. External shocks might confound and influence any forecast. However, our results, and especially the deducted brand value drivers, can serve as a useful lens through which to contemplate and understand the future importance of Chinese brands.

Brand equity development of consumer goods brands in China, Europe and the US



US



EU



China



2007

2012

2015

2025

The graphic displays the development of the average brand values (in billion USD) of the most valuable consumer goods brands in China, Europe and the US for the past (2007), present (2012), future (2015) and distant future (2025).

Strong and still growing brand-consciousness of Chinese consumers

During the period of China's total isolation from the rest of the world after the second world war, there were no real brands available, few communication possibilities and nearly no advertising. At that time, most Chinese consumers were characterized by their very limited disposable income, very price-conscious shopping, and self-restraint with regard to their personal desires. The concept of a brand was equivalent to that of a trademark or logo. Nowadays, China's rapid economic development has raised consumers' disposable income and massively transformed their buying behavior, which is now significantly driven by brands and their various benefits.

Strong economic growth as a basis for a prospering society

By 2010, China's economy was three times larger than it had been ten years earlier, surpassing Japan and becoming the second largest economy after the US. Research undertaken by McKinsey suggests that China's GDP will continue to grow, achieving an annual growth rate of 7.9% in the next ten years.² As a comparison, the forecasted figure for the US is 2.8%, while for Germany the estimated annual growth for the next ten years is 1.7%. The great discrepancy can be explained by the fact that the majority of GDP growth is based on consumption rather than on investment activities. More and more Chinese consumers will have a higher purchasing power combined with a quantitatively and qualitatively increasing demand. According to the McKinsey study, the per capita disposable income of urban consumers will double from 4,000 USD to 8,000 USD between 2010 and 2020. This will bring China in line with the current standard of living in South Korea, for instance, but it will still lag far behind developed countries such as the US (with a disposable income of about 35,000 USD).

The growing middle class is driving consumer spending

Economic growth has massively strengthened the purchasing power of the Chinese middle class all over the country. The Chinese consumer's purchase power in urban areas has more than doubled since 2005.³ A huge number of Chinese have become richer and are able to afford a wealthy standard of living. Recent social and economic reforms have transformed and reshaped the industrial, commercial, and regulatory landscapes of China's developing Tier 2 cities.⁴ As living standards and the business environment improve, these cities are gaining an enormous market potential. The growth of Tier 2 cities has resulted in a relentless surge in consumer buying power that is driving consumer spending. McKinsey forecasts that the numbers of middle-class consumers will grow significantly in the coming years and that these so-called mainstream consumers will represent 51% of the urban population by 2020. Even if in absolute terms their standard of living is still low compared with that of consumers in developed countries, this social cluster will become the standard setter for consumption. This group, which will be able to afford family cars and luxury goods, will comprise 167 million households or almost 400 million people by 2020.⁵ Given the dimension and the rapid growth of these "mainstreamers", their increasingly brand-driven purchasing behavior will have a strong impact on the future brand equity.

The evolving role of brands

There are various indicators underscoring the growing importance of brands in Chinese consumers' purchasing behavior. As Chinese consumers evolve from cost-to brand-conscious, brands are bought to show off and impress others. However, brands also start taking on more important roles, for instance as indicators of quality. As a consequence, fake branded products are gradually losing their importance as Chinese consumers begin to strive for authentic brands and products.

However, China's counterfeit market still has significant dimensions. As China has become the world's leader in exporting manufactured goods, it is also said that the

² Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

³ Source: National Bureau of Statistics of China

⁴ Tier 2 cities are secondary provincial capitals (consisting of 23 cities across China)

⁵ Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

country is dominating the global market for luxury fakes.⁶ From the perspective of the brand holders, counterfeit is a double-edged sword. Some say that the distribution of fake branded products helps the original brands because it raises consumer awareness of these brands. Others understandably suggest that strong brand names stand for a quality guarantee that is being undermined by counterfeits.

Chinese consumers with a growing purchase behavior have a strong appetite for brands. According to a market study conducted in 2007 by TNS, one of the world's leading market research companies, 60% of polled Chinese consumers said that they use luxury goods to demonstrate social status, and 65% claimed that people who own luxury goods are "successful". Besides a brand's function to demonstrate social status, self-reward is the second most important motivation of Chinese consumers to buy and use branded products. Moreover, study results suggest that less than 2% of respondents regard owners of luxury brands as "superficial", and more than half of the respondents said that they longed to purchase luxury goods even though they could not afford them at present. Another very important result of this study underlines the growing importance of brands and its value-adding characteristic that will positively influence Chinese brand equity: less than 30% of the surveyed consumers objected to paying a price premium for a luxury brand.⁷

Despite the enormous supply of fake products in the domestic market, Chinese consumers are no longer likely to fulfill their status-oriented needs with fake brands. There seems to be a growing recognition among Chinese middle-class consumers that brands cannot bring social status anymore if everyone owns the same copied branded goods.⁸ According to Claudio Mazzucchelli (Head of Swiss Business Hub China, Federal Department of Foreign Affairs), "the status symbol given by known brands is an important factor in Chinese life (at least in the middle and high class). And Chinese prefer original products rather than fakes. They also want the quality and they know that fake products often lack in quality." These findings are underlined by recent

research studies. A study about China's luxury market conducted by the consultancy firm Bain concludes that "demand for counterfeit products is decreasing fast".⁹ Another study by McKinsey has found that consumers' willingness to buy fake jewelry is diminishing: the proportion of polled consumers' willingness to buy fake jewelry decreased from 31% in 2008 to 12% last year.¹⁰

Growing demand for authentic brands

Wealthier Chinese consumers are looking for authentic brands that can't be copied and afforded by anyone else. Many travel to Europe and buy "the real thing" after having queued outside luxury stores in Italy or France to buy branded products. According to a study, there are two more reasons why Chinese consumers buy overseas to satisfy their growing demand for authentic brands:¹¹ on the one hand, buying the products at the original flagship stores guarantees that the products are not counterfeit, something that is not sure when shopping in a Chinese mall. On the other hand, higher taxes and duties increase the price of the goods about 30% when they are bought in the Chinese market. This growing demand for authentic products reveals that Chinese consumers are realizing that brands can also send useful signals about quality. A survey conducted by graduate students in Beijing in July 2011 states that respondents defined a brand as being consumer-focused and reliable. Moreover, 100% of the respondents considered quality first when evaluating brands.¹²

Chinese consumers' quality expectations of a brand come along with other important and more sophisticated needs a brand has to meet: brands have to fulfill a certain promise that is associated with the brand. Of course, brands have to be associated to high social status, but consumers also expect a brand to be authentic, reliable and trustworthy. Chinese consumers want brands to become carriers of life style and allow them to fulfill their dreams. This is more than delivering a high quality product: it is also about offering an emotional customer

6 Source: "Fake luxury goods have sinister tag", *China Daily*, May 21st 2005

7 Source: "Luxury brands in China", KPMG, Monash University, TNS, 2007

8 Source: "Chinese puzzle", *Brand Finance Journal*, March 2012

9 Source: "Luxury Goods Worldwide Market Study, Spring 2012 Update", Bain & Company, 2012

10 Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

11 Source: "Luxury brands in China", KPMG, Monash University, TNS, 2007

12 Source: "Thanks, but no thanks' to Made in China?", *Knowledge@Wharton*, 2012

experience that goes beyond delivering a functioning product, trust and identity.

With regard to consumers' trust, the latest McKinsey survey shows that Chinese consumers reckon that companies selling a wider range of products are more trustworthy than companies marketing goods in one or two segments.¹³ As the research study denotes, Chinese companies have already taken this fact into consideration by selling various products on different price scales but under the same umbrella brand. Furthermore, companies like Coca-Cola or P&G use the same tactic and emphasize the corporate brand more than they do in other countries. The results also confirm the growing emotional and individual needs that brands are expected to fulfill. Brands are expected to give the consumers emotional benefits and allow them to express themselves. This is not only the case for high involvement goods such as cars and jewelry, but also for low involvement products such as milk and toothpaste. As an example, 7% of polled Chinese consumers say that the best detergent should not only clean clothes but also make them feel special (this value was at 2% in the survey of 2009).

The new tendency about brands addressing individual needs was also pointed out in a study conducted in 2007:¹⁴ this research found out that in China the consumption of luxury branded goods was very much item-driven. That is, consumers search for the latest collection or products. However, the study forecasted that Chinese consumers, like consumers in more developed countries, would tend to seek experiences or products catering more closely to their personal tastes.

In light of these above-mentioned research results and arguments, this new trend of Chinese consumers' desire to express their individuality with brand-driven purchases seems to confirm the actual and growing demand for authentic brands that deliver emotional and custom-tailored experiences.

Social-cultural factors driving brand affinity

There are interesting phenomena in modern Chinese culture that underline a growing brand affinity of the Chinese consumers and their willingness to change their behavior according to brands.

Chinese culture is characterized by a strong collective behavior, group orientation and hierarchical social relations. For instance, Chinese consumers tend to share and exchange information informally among their peers. Chinese consumers tend to rely more on word-of-mouth communication because of the high contact rate among peer members.¹⁵ Thus, information about a given product or brand is quick to circulate within these informal channels. With regard to the usage of branded products and services, peer group pressure is very strong, so that inferior peers try to enhance their status by buying products with well-known and strong brands recommended by higher-status members of the peer group. A recent study described the peer pressure phenomena in Chinese society with the concept of "face consumption": in order to fulfill certain social needs, Chinese consumers are much more likely to buy branded luxury goods to improve their status or even keep face even if they do not have enough money to buy food or pay their rent. The authors describe the concept as "the motivational process by which individuals try to enhance, maintain or save self-face, as well as show respect to others' face through the consumption of products".¹⁶

When it comes to brands, Chinese consumers can develop a strong sense of national pride. As Chinese consumers also consider the country of origin of the brands they use, their brand-driven behavior is also affected by political events: on the occasion of the Olympic Games in Beijing in 2008, pro-Tibetan protests took place during the Olympic torch relay in Paris. As a consequence, Chinese consumers boycotted Citroën and Carrefour, and some reports say that sales of French cars in China dropped 25% during the Olympic Games. Moreover, there were protests in front of Carrefour markets in China.¹⁷ These boycotts underline the sensitivity of the consumers' brand preferences and their attitude towards foreign brands. However, Chinese consumers' sense of patriotism also indicates a certain

¹³ Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

¹⁴ Source: "Luxury brands in China", KPMG, Monash University, TNS, 2007

¹⁵ Source: "Brand Effect on Consumer Behavior in China", *Fibres & Textiles in Eastern Europe*, April/June 2004

¹⁶ Source: "How face influences consumption: a comparative study of American and Chinese consumers", *International Journal of Market Research*, 2007

¹⁷ Source: "Chinese puzzle", *Brand Finance Journal*, March 2012

affection towards their own country and culture that domestic companies could exploit in their favor when creating indigenous brands.

Another fact underlines the Chinese brand-driven purchasing behavior: Chinese consumers seem to have a high willingness to change their consumer attitude based on the advertising messages they receive. Until a couple of years ago, chocolate was bought exclusively as a gift. However, chocolate producer Mars has cleverly repositioned the Dove chocolate bar: the advertisement campaigns animated Chinese consumers to indulge themselves and to buy the chocolate bar for their own pleasure. Mars' efforts in the Chinese market have paid off: nowadays Mars is one of the most successful chocolate producers in China.¹⁸

Despite the persuasive power of brands, Chinese consumers have a high knowledge about products and brands.¹⁹ They are eager to see what is available, and they invest a great deal of time seeking information. In Chinese cities, window-shopping and browsing are favorite weekend pastimes. This behavior implies that consumers are exactly aware of what a brand stands for and know the values and promises it represents. The brand and its values are therefore crucial to purchase decisions and consumers expect that brand promises will be fulfilled. Like window-shopping, shopping in malls for pleasure is an increasingly popular pastime in China.²⁰ Shopping malls are important touchpoints where brands are able to build awareness and develop a positive perception. It can be assumed that Chinese consumers enjoy this new mall culture because it allows them to experience the physical and emotional experiences that brands are able to create.

The one-child policy introduced in 1978 by the Chinese government has also had curious consequences on consumer buying behavior and ultimately on brand-driven consumption. Because of the one-child limitation, many women are free from taking care of large families and have therefore been able to invest their resources in a job. As a consequence, Chinese women have a high workforce participation: 67% compared to 48% in Japan or 58% in the

US (values from 2009).²¹ Furthermore, the percentage of women working in offices increased from 43% in 2003 to 47% in 2010.²² Given this development, Chinese female consumers have become more independent, as they earn relatively high wages and have a high purchasing power. Combined with the need for showing and confirming their social status and with women's high affinity for brands, it can be assumed that these women's purchasing behavior will become even more brand-driven in the future. This is therefore another socio-cultural development that will significantly foster Chinese brand equity.

Social media as driver of brand preference

Social media have a very strong and increasing importance in China. In terms of brand equity, social media as a communication channel can be seen as a significant value driver with the capacity to influence brand awareness and brand perception in an incredibly short period of time. Furthermore, they are an important platform for brand-conscious consumers to exchange information about their brand preferences and expectations. Chinese companies frequently use social media as a communication platform: as an example, Chinese companies use their Weibo account – and not a www address – to sign off their billboards or advertising spots.

The statistics of Chinese Internet users and their usage of social media are impressive: the number of Chinese Internet users has increased by 2100% since 2000 to 513 million users. A research study forecasts that in 2015, a total of 700 million Chinese users will have access to the Internet – that is as many as in India, Japan, Russia, the US, and Indonesia together.²³ The study goes on to state that during the last year, Chinese consumers spent 1.9 billion hours a day online resulting in an average of 3.6 hours a day per user (circa one hour more than US Internet users). Another recent survey has found that 95% of Chinese consumers living in Tier 1, Tier 2, and Tier 3 cities are registered on a social media site. Statistics about the use of e-commerce also reveal that Chinese e-shoppers

18 Source: "Das Jahr des Drachen soll den Konsum befeuern", *Finanz und Wirtschaft*, February 8th 2012

19 Source: "Consumer Knowledge and its Consequences: an International Comparison", *International Journal of Consumer Studies*, 2008

20 Source: "Luxury brands in China", KPMG, Monash University, TNS, 2007

21 Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

22 Source: "New Study Finds the Solution to China's Talent Crunch is in the Hidden Talent Pool of Educated Chinese Women", Center for World-Life Policy, 2011.

23 Source: "Listening to China's Digital Generations", The Boston Consulting Group, 2012

are frequent users of social media.²⁴ According to a study published by BCG, over 40% of Chinese online shoppers read and post product reviews online.²⁵ A recent study published by McKinsey reveals that China's e-commerce market is expected to grow significantly, becoming the world's largest by 2015.²⁶

These impressive statistics of social media and e-commerce usage in China have two important implications for Chinese brand equity. Firstly, the brand equity of social media brands benefits from their users' behavior. Secondly, social media platforms are a very potent communication channel that can efficiently benefit brand strength and brand equity of companies.

In terms of social media brands, the high number of users and the intensive daily use of the platforms positively influence their brands' perception and strength. Chinese Internet users spend a lot of time on the platforms and are therefore constantly exposed to the brands. Social media brands can therefore benefit from the so-called multiplicative brand effect. This effect describes the fact that through this omnipresence, the brand achieves a high level of awareness. Furthermore, given that social media platforms facilitate and promote social and emotional interaction between users and their peer groups, this positive experience influences the brands' perception and connotes it with positive values and associations. As a consequence, a social media company can build strength and value by fostering a trustful and loyal relationship with its users. As e-shoppers are frequent users of social media and the e-commerce business is forecasted to boost in the near future, the social platforms and their brands are going to benefit significantly from this trend. As reported by McKinsey, by 2020, 14 to 15% of retail sales will be transacted online. For consumer electronics this ratio could even be as high as 30 to 40%.²⁷ Chinese social media brands are therefore very valuable brands, and their value will continue to increase. According to the ranking of "The Most Valuable Social Media Brands 2012" published by BV4, three Chinese social media brands are amongst the top ten: Qzone is on position four, followed by Sina Weibo (on position five) and Tencent Weibo (on position eight). The most valuable

Chinese social media brands that are among the top thirty of the ranking achieve a total brand equity of 28 billion USD.²⁸

In terms of communication opportunities, social media brands offer powerful communication channels used by many of their registered users, not only to read and post product reviews online but also as an important brand- and product-related information source for consumers. A recent survey states that Chinese social media sites are already nearly as important as portals as an entry point to obtain content: 40% of the users stated that portals are their preferred sites to obtain information whereas 36% preferred social media sites for the same purpose.²⁹ An illustrative example shows how social media can be strong catalysts of brand awareness: during a thunderstorm in Beijing in June 2011, pictures of a young man putting on Durex condoms over his shoes were posted on Weibo, a very well-known social media platform. The post was then picked up by the official Durex Weibo account and went viral, reaching an estimated 50 million users throughout China.

In the light of the above-mentioned arguments, we see that social media are an important driver of brand strength and value – for the social media brands themselves as well as for other brands. Chinese consumers' high and still growing affinity and loyalty to social media have a strong impact on how Chinese consumers perceive brands and build their preferences. Consequently, social media brands are important brand equity drivers as they influence consumers' brand-driven consumer behavior.

To sum up, the strongly growing Chinese economy has increased the living standard of middle and high-class consumers in China. As a consequence, Chinese consumers' behavior has evolved from being cost-conscious to being brand-conscious. Their affinity to brands is strongly increasing, so that new and sophisticated brand-specific needs arise. The quoted trends, examples and attitudes of changing consumer behavior clearly underscore the growing importance that brands have in the consumer decision process. Not only status, but also quality and lifestyle are needs that brands need to fulfill. However, this increasing brand-consciousness can be converted to brand equity only if Chinese companies can fulfill these new expectations.

²⁴ Source: "China, a Social Media Country", *Forbes India*, July 2012

²⁵ Source: "China's Digital Generations 3.0: The Online Empire", *The Boston Consulting Group*, 2012

²⁶ Source: "China's social-media boom", *McKinsey&Company*, 2012

²⁷ Source: "Meet the 2020 Chinese Consumer", *McKinsey&Company*, 2012

²⁸ Source: "The most valuable social media brands 2012", *BV4 – Brand Valuation Experts*, 2012

²⁹ Source: "China's social-media boom", *McKinsey&Company*, 2012

Certainly, Chinese consumers have the needed purchase behavior and are also willing to pay a significant price premium solely because of the brand and its benefits.

The future, brand-oriented Chinese consumer

Based on the results, conclusions and assumptions from internal research and the external studies, articles and best practice examples quoted above, the mainstream consumer in China who will significantly influence China's brand equity in the future can be characterized by the following three main characteristics:

- Pragmatic
- Brand-focused
- Self-expressive

The pragmatic consumer

Chinese consumers are pragmatic - and that will not change in the future despite China's increasing prosperity. The pragmatic consumer is conservative, is eager to see what is available and willing to invest a lot of time to seek information about the desired brand and product. The Chinese will remain smart shoppers, and as price comparisons become easier to make, they will get even cleverer. Chinese consumers are constantly looking for "value for money" during their purchase process. However, this does not mean that brands are not relevant in their purchase decisions. On the contrary: they also evaluate brands on the basis of this "value for money" concept. They are willing to pay a price premium for strong brands, but, in return, they expect the brand to fulfill its promise and the consumers' emotional and individual needs.

The digital, brand-focused consumer

Despite Chinese consumers' passion for brands, they are actually less loyal consumers than their western counterparts, preferring to choose from among a variety of their favorite brands. Only 46% say they stick with a particular brand of a product they like, compared with 71% in the United States.³⁰ The research study also suggests that the young and affluent have greater brand loyalty. However, it can be assumed that brand loyalty will certainly rise as Chinese companies increasingly promote the emotional benefits of their goods in order to differentiate themselves. When in a more mature market Chinese companies are able to move up the value pyramid and offer unique emotional

benefits associated with a brand, consumers will become more loyal towards brands and continue to benefit from the advantages of the brand they chose.

Furthermore, more and more Chinese consumers will make their purchases online as shopping trips to malls will sooner or later lose their novelty and be replaced by other leisure activities that come along with increasing prosperity. As stated above, the e-commerce in China is growing fast, and it is also boosted by the rising numbers of Internet users and their affinity to social media. Furthermore, evolving lifestyles are increasing shoppers' demand for convenience. Additionally, mobile shopping applications and trustworthy online payment systems will increasingly boost purchases made via e-commerce. It can therefore be assumed that Chinese consumers could become very dedicated and sophisticated online shoppers.

The self-expressive consumer

Emotional considerations will strongly affect the buying decisions of most Chinese consumers – particularly whether a brand considers the consumer's need for individuality. Based on the McKinsey study, for instance, only 8% of consumers buying chocolate in 2009 thought that concepts such as "showing my status" or "this is a brand for people like me" were important. Today that figure stands at 19% on average and 24% for wealthier consumers.³¹ Consumers' sense of individuality (for both low and high involvement goods) will certainly become more important as the income continues to grow. In other words, Chinese companies will also need to satisfy this desire for individuality in commodity categories such as milk and toothpaste. With this growing need to express individuality, it can also be assumed that Chinese consumers are more willing to try out lesser-known Chinese brands in order to differentiate themselves from other consumers, therefore giving these brands a chance to develop their brand strength and value.

In the long run, Chinese consumers will not be satisfied only by pragmatic and convenient purchases. Individual needs – needs addressed by a brand's emotional aspects, easier price comparisons, a unique assortment of products, quality and services as well as social networking experiences – will increase. Preferences will become more varied and especially increasingly brand-driven.

³⁰ Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

³¹ Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

Chinese Companies Are Catching Up

Beginning in the 1980s, many ambitious Asian companies from different industries were successfully selling products not only in their home markets but also in the global market. Japanese companies such as Toyota and Honda succeeded in the automobile industry using their competitive advantage of a lean but also quality-conscious management. Later, brands from Korea such as LG and Samsung or Acer and Asus from Taiwan also succeeded in the global market. All these brands created and maintained specific competitive advantages: efficient logistics management and low-cost production combined with a high degree of innovation and – most important – with a superior level of quality. All of this had a strong and positive impact on brand perception.

“Made in China” – a great burden to overcome

Even if many Chinese companies have been able to develop some of the above-mentioned qualities, only few firms have so far succeeded on a global level. The most challenging obstacle to overcome seems to be the “Made in China” label that is globally associated with negative values such as low-quality and fake products. “In the past, Chinese products were known for their low-added value and often for their poor quality. Now things have changed but the “Made in China” label still suffers from this reputation”, says Claudio Mazzucchelli (Head of Swiss Business Hub China, Federal Department of Foreign Affairs). Consumers’ lack of confidence in the quality and reliability of products manufactured by Chinese companies is not unfounded: in 2008 for instance, several products of the Chinese national dairy giant Mengniu were found tainted with the industrial chemical melamine. The poisoned milk killed six babies and sickened about 300,000 children. Even after Mengniu apologized to the consumers and said the tainted products involved had been destroyed, again in 2011 a batch of Mengniu milk was found to contain excessive levels of flavacin - a substance linked to liver cancer. In the same year, quality authorities in south China’s Guangdong Province said Mengniu ice-cream contained high levels of bacteria, and that 251 pupils had fallen ill after having drunk Mengniu milk at school.

World number one in exports but low global brand awareness

The series of bad experiences severely lowered the quality and trust perception Chinese consumers had with regard to domestic companies. This phenomenon has a halo effect, so that the negative image is transferred to other companies and industries and also lowers the strength and the value of their brands. “Chinese products are often labeled as bad quality. This sometimes is true, but not always, especially not for the products exported to US and EU markets”, says Hui Wang-Haymoz (Legal and Compliance Luxury Goods, UBS AG). It is therefore interesting to see that despite the low global success of Chinese brands in terms of awareness and image, China leads the world in exports, sending goods worth 399 billion USD to the US alone last year.³² In each and every corner of the world you can find products that are labeled “Made in China”. But almost all Chinese products sold outside the country are marketed under another company’s name, and the Chinese manufacturers are acting either as contractors making goods to an externally supplied design or as “original equipment manufacturers” (OEMs). These findings are confirmed by a research study: outside China, there is a general lack of awareness of Chinese brands across international markets, including in Asian countries. Even when consumers say they are aware of Chinese brands (the average awareness is under 5%), the ability to correctly name a specific Chinese brand in a particular product category is extremely low, with as many Japanese or Korean brands being mistakenly thought of as Chinese.³³ Clearly China’s export market is the main driver of the rapidly growing economy, but it seems ironic that the country’s growing prosperity is based on its immense export activities of products they refuse to buy themselves.

Quality perception as a crucial brand value driver

Given these circumstances it appears that the main challenge of Chinese companies is perceived rather than actual quality. Foreign markets seem to value the quality of the exported goods – otherwise the export market would not be so successful. Still, achieving and sustaining a high quality standard of Chinese products is as crucial for their success as raising quality and brand perception.

More and more local Chinese companies are now realizing the disastrous consequences of such perception and

³² Source: Office of the United States Trade Representative

³³ Source: “China Brand Opportunity”, Accenture, 2008

reputation problems. Chinese companies have to follow strict quality programs to avoid scandals and to raise and maintain the quality standard of the produced goods. In the same way as their counterparts in Japan or Korea did in the past, Chinese companies have to create a corporate culture that stresses quality from within. Each and every employee has to be conscious of the crucial importance of quality in every step of the value chain and also be aware of the positive impact this quality-orientation has on consumer perception of both the products and the brand. This knowledge about the benefits of a strong brand perception certainly exists in upcoming Chinese companies. They just have to learn that building up a brand is a long-breath effort and something that cannot be achieved by merely copying European or US companies.

Haier, a Chinese multinational consumer electronics and home appliances company, started its success story on the basis of a complete commitment to quality. They recognized that any mistake or flaw across the whole production chain could burden the company with a bad reputation of low-quality products and with negative associations to the “Made in China” label. In order to underline and demonstrate this to his employees, Zhang Ruimin, CEO of Haier, once pulled 76 faulty refrigerators off the production line and ordered the staff to smash them to pieces. Besides this quality commitment, the company executed a series of technological innovations, M&As, and multinational expansion moves over a period of more than two decades. In the course of these events, it developed a successful branding strategy that consisted in creating localized Haier brands in every non-China target market. This new branding strategy helped Haier to achieve a sustainable development by realizing win-win profits with suppliers and customers. Their efforts have paid off: in 2009 the company became the world’s largest manufacturer and increased its market share to 7.8% in 2011.³⁴

Strategies to build domestic and global brand equity

In the last few years, Chinese companies have started to realize that not only good quality but also consumers’ positive brand perception, trust and brand loyalty are vital foundations to be successful and benefit from brand-driven purchase behavior. In order to address consumers’ newly developed brand-consciousness, Chinese companies

choose two different approaches. The first is acquiring established foreign companies and benefit from their technological knowledge but also from their strong brands. The second approach is to build indigenous brands and establish leading positions in their domestic market and then expand abroad on the basis of this strong domestic brand equity. Of course, the first approach is relatively easier, but bought brands can be difficult to integrate or can take a long time to pay off (as Tata Motors is actually discovering with Jaguar). Consequently, the second approach is a more sustainable strategy that has a higher potential to build brand value on the long run.

The Lenovo brand is a good example of how a Chinese company has managed to build a competitive and valuable global brand by acquiring an already established foreign brand. However, even before Lenovo’s acquisition of IBM’s PC business, the Chinese company had a strong domestic base of technological know-how that enabled Lenovo to capture a growing share of the Chinese domestic PC market. Facing intensive foreign competition, Lenovo capitalized on its low-cost advantage and positioned its product price above the prices of other domestic brands but below global brands, allowing the company to operate with financial efficiency. In 2005, Lenovo announced its 1.25 billion USD purchase of the IBM ThinkPad line of personal computers. By repositioning itself as a focused, global producer, Lenovo followed the path of a new strategy based on high-quality products and world-class service. This acquisition and the company’s new strategic orientation made Lenovo a global player and helped it increase its global market share from almost zero to 9% within six months. Several strategic brand decisions gave the brand an additional boost in terms of awareness and positive perception: Lenovo became a worldwide sponsor of the Olympic Games in 2006 and 2008 as well as a sponsor of the National Basketball Association (NBA). Furthermore, the Chinese computer firm has now announced a deal to sponsor the National Football League in the US. Today, Lenovo gets 42% of its sales from China and has 40 times more stores in China than Apple has worldwide.³⁵

Another exemplary Chinese takeover was the recent acquisition of Volvo Cars by the Zhejiang Geely Holding Group in 2010. The two car brands won’t be officially merged and will be run separately. However, this decision has a solid strategic background, as the newly acquired reputed Swedish brand is expected to have a positive halo effect on the

³⁴ Source: Haier, *News & Press*, 2012

³⁵ Source: “Brand new”, *The Economist*, August 4th 2012

Chinese car brand, which is rather seen as a traditional brand for the mass Chinese market. Chinese companies are actively looking for well-established international brands, not only to expand globally but also to improve their market position in the domestic market. There are several other examples of Chinese companies buying western brands to enhance their domestic and international business and positioning. These transactions clearly evidence the improving understanding of Chinese companies for brands striving to address brand-conscious Chinese consumers. The same trend is visible in the fashion industry: a Hong Kong-based investor bought Aquascutum, a British trench-coat producer, and is now selling products across China many years after the brand lost market shares in the home market.

Moving up the value pyramid

In the context of the second approach, Chinese companies can fulfill consumers' brand-driven needs by creating their own indigenous brands. "The key is to cultivate and develop a brand that is specific to China. Consumer education is also necessary, as Chinese consumers are still relatively new to the free market", says Prof. Dr. Li Choy Chong, Professor and Director of the Asia Research Center at the University of St.Gallen. At the moment, the most promising approach is to build, maintain and improve the equity of Chinese brands in the long run.

In order to analyze the current and future development of domestic Chinese brands, the so-called value pyramid is a helpful concept.³⁶ The brand evolution model suggests that a company has to "climb up" five levels in order to become a reputed brand that not only stands for a certain lifestyle but also takes social responsibility: (1) In a first step, a brand has to gain awareness by becoming a manufacturer reference. (2) In a second step, the brand has to guarantee the quality of the goods it represents in order to win consumers' trust. (3) The third step of the value pyramid is the guarantee of exclusive use, which can only be achieved if the brand is completely successful on the two precedent levels. A brand can guarantee exclusive use by offering unique product performance and/or by delivering emotional content that addresses the need for emotional benefits in consumers' purchase decisions. Going even further (4), brands that represent lifestyles and are able to create a brand-specific

culture; examples of this are Harley Davidson or Apple, have become carriers of lifestyle. And finally (5), it should be a brand's ambition to be recognized and respected as the carrier of social responsibility.

With regard to Chinese brands, the challenge of most of domestic brands is to achieve and – most importantly – to maintain the first two levels of the value pyramid. The next significant step is then to achieve the third level and being perceived as a brand that guarantees exclusive use of the offered good. This is where professional strategic brand management has the power to build a strong image through consistent and unique brand positioning. Consequently, Chinese companies have to address the newly aroused consumers' needs of brands as carriers of a lifestyle that meet their individual expectations, and they have to respond to the growing importance of emotional considerations during the purchase and usage of their brands.

Even if this strategic branding challenge faced by many up and coming Chinese brands is very ambitious, the signs of an upward trend on the value pyramid are good: China's counterparts Japan and South Korea struggled with similar problems at the beginning of the history of their successful brands. Brands such as Nissan from Japan (formerly Datsun) or Hyundai from South Korea both started selling low-price products with unknown brands. Over the years they have become powerful global players and today they possess some of the most valuable brands in the world. Nowadays, Chinese companies have a strong position as manufacturer references, underlined by their prospering export market. As they move up the value pyramid, Chinese companies will be producing more complex products on a higher quality level. In order to move even further, companies will have to create and manage brands that foster positive quality perception and also give the product an emotional component. If Chinese companies that are already on a relatively high level of the value pyramid manage their brands with a professional know-how, there should be no reason why they should not follow in the footsteps of their Japanese or Korean counterparts.

The rising value of Chinese brands is also demonstrated in recently published rankings of various consulting and market research companies. In June 2012, World Brand Lab published the 500 most valuable Chinese brands. China Mobile, with a brand value of 37.47 billion USD, overtook the Industrial and Commercial Bank of China and became

³⁶ Source: "Valore e valori della marca. Come costruire e gestire una marca di successo", Giampaolo Fabris, 2004

the most valuable Chinese brand of 2012.³⁷ The brand value of China Mobile is comparable to the value of well-established western brands such as General Electrics or Intel. It is also impressive that, according to the research company Millward Brown, thirteen Chinese brands are amongst the Top 100 most valuable global brands. They include China Mobile, Tencent and Industrial and Commercial Bank of China as well as two newcomers – Sinopec (oil and gas company) and Moutai (liquor producer). This ranking also states that China Mobile, with a monetary value of 47 billion USD, is the most valuable Chinese brand. The study reports that the combined value of the most valuable Chinese brands is 258 billion USD, and that it accounts for roughly 11% of the total value of the 100 most valuable global brands. Among emerging BRIC nations, China has the most brands represented in the ranking. In 2006 China had only two brands represented in the ranking, while in 2012 there are a total of 13 Chinese brands amongst the most valuable brands across the world.³⁸

The growing importance of indigenous brands

Smaller and less globally known indigenous brands are also becoming stronger and more valuable. A few Chinese brands have even become more reputable than comparable western brands. The recently launched luxury brand “Shang Xia” serves as a good example. The brand promises a “unique encounter with the heritage of Chinese design and craftsmanship” and strongly promotes the kind of Chinese culture that often appears to be lost in the country’s economic rush. One of the strategies that sets Shang Xia apart from other luxury brands is that it prioritizes time over profits with goals set in a 100 to 200-year timeline.³⁹ The success of Chinese companies that put Chinese culture and its values in the focus of branding indicates a growing interest and demand for such authentically Chinese branded products – both in China and abroad.

There are several other successful examples of indigenous brands that have achieved a strong position in the Chinese market. They can be considered as pioneers that understood the changing Chinese consumer behavior and were able to implement branding strategies that fit with the needs of its target groups. A brand worth mentioning in this context is

Belle International, the country’s market leader for women’s shoes with an actual domestic market share of 22%. At the end of June 2011, Belle International served 13,000 point of sales all over the country.

A research study conducted in 2007 already identified some luxury brands that were perceived as being luxury on a local scale – and that had succeeded in portraying themselves as international even though their main market was domestic. Such brands include Goldlion (a company engaging in the sale of fashion apparel and accessories as well as in property investment and development), and the jewelry brands Chow Tai Fook and Tse Sui Luen. In view of improved design trends and increased government support, the study forecasted that many more Chinese luxury brands could emerge in the next few years.⁴⁰

This forecast was right, as exemplary shown by the luxury brand Herborist. Based on the traditional importance of medicinal herbs in Chinese culture, the Herborist brand is one of the new Chinese high-end cosmetics brands that are associated with traditional medicine and long-term results. The strong domestic brand has also successfully expanded to European countries. Their success is shown by their 1,000 flagship stores across the country, their newly opened 120 sales outlets in France and the sale of their products in other European countries such as Italy, Spain, the Netherlands and Turkey. Thanks to its aggressive expansion strategy, the company was able to increase its 100 million USD turnover in 2005 to almost a billion today.

Chinese sports brands recently achieved high global awareness and gained respect in the sports world thanks to the last Summer Olympic Games in London. Even though the 2008 Olympic Games were held in Beijing, Chinese brands were much more successful in using the latest Games in London as a platform to present themselves to the world. Among sports brands such as Li-Ning or Peak, the Anta sports brand had the best Olympics in terms of brand awareness and exposure.⁴¹ Founded in Fujian in 1994 as NTA (Fujian) Shoes Industry Co., Ltd, Anta grew slowly but surely, opening its first retail store in Beijing in 2001. By 2004 it had stores in all provinces, and by 2012 it had 7,807 stores in China and achieved a gross half-year profit of 264.5 million

37 Source: “The 9th China’s Most Valuable Brands 2012”, World Brand Lab, 2012

38 Source: “2012 BrandZ Top 100”, Millward Brown, 2012

39 Source: “Chinese puzzle”, Brand Finance Journal, March 2012

40 Source: “Luxury Brands in China”, KPMG, Monash University, TNS, 2007

41 Source: “Olympic Gold For Chinese Sportswear Brand. No, not Li-Ning, the Other One”, Brandchannel, August 17th 2012

USD through the first six months of 2012. However, Anta is little known outside China. But in the domestic market, it has ranked first in sportswear market share for the last 11 years.⁴² The 2012 Olympics offered a huge opportunity for Anta: they were the official partner of the Chinese Olympic Committee, outbidding competitors like Adidas or Li-Ning. During the Olympics, it was impossible to overlook the Anta logo, also thanks to its partnership with the Olympic team and other retailers. As an example, McDonald's employees in China all wore Anta-branded Olympic shirts throughout the Games. Moreover, the athletes repeatedly posted photos of themselves on the social media platform Weibo wearing Anta sportswear. Anta is a good example of how an already established domestic brand used the right communication means and channels to promote global awareness while enforcing their brand strength at home.

Recent and actual success stories of Chinese brands clearly confirm that Chinese companies have the potential to build strong brands that are valued both in the domestic market and outside the country. It can therefore be assumed that many other companies will learn from these best practice examples and successfully start building their own individual brand culture.

Rapidly growing patent applications and trademark registrations

Another trend underlines the growing importance of intellectual property to support the future growth of Chinese brand values: the rising number of patent applications. The World Intellectual Property Organization (WIPO) registered an 11% global growth of patent applications for the 2010-2011 period. China, Japan and the US are responsible for over 80% of this growth, with China exhibiting the highest growth rate (33.4%), followed by Japan (21%), Canada (8.3%) as well as South Korea and the US (both 8%). With an absolute increase of 985% in patent applications, the Chinese company ZTE – a multinational telecommunications equipment and systems company – clearly leads the ranking of the companies with the most patent applications in 2010-2011.⁴³

With regard to trademarks, the number of registered marks in China has made the biggest leap among growth markets

in recent years. Between 1989 and 2009, more than 550,000 trademarks were registered in China. Since 2000, the number of marks registered in China has increased by more than 450%. Furthermore, the cumulative growth of Chinese trademark registrations has far outpaced that of other nations.⁴⁴ Given the wide spread of counterfeiting and infringement, it is even more surprising that trademark registrations have significantly increased in the last few years.

The strong increase in trademark applications is a clearly positive indicator of future Chinese brand equity, as it shows that Chinese companies are aware of the importance of brands and the necessity to register them in order to protect them. However, the complex intellectual property infrastructure in China requires detailed local knowledge and constant vigilance to sustainably protect trademarks. A main obstacle to trademark registration is the fact that China has 45 different trademark classes. If a brand wants to be well protected, it therefore needs to file across all the classes, which of course requires a lot of time, money and patience. If not, brands leave themselves exposed to opportunistic registrations by trademark squatters who secure trademarks in the hope that they will then be bought off by the real companies for high prices. Another challenge of trademark registration is that companies have to think three dimensionally: in order for a trademark to be successful in China, the form, sound and meaning of the brand all need to be protected separately.⁴⁵

There is no doubt that the fast growth in patent applications and trademark registrations is having a positive impact on actual and future Chinese brand equity. However, other prerequisites also have to be fulfilled so that this development finally results in sustainable brand equity. For instance, the complex intellectual property infrastructure makes it difficult for companies to fully protect their intellectual property. As theory and practice of brand valuation suggest, the complete value potential of a brand can only be achieved if the trademark is integrally secured and therefore immune to the risk of counterfeiting, which could potentially diminishing brand equity. Therefore, the Chinese government should engage in making the intellectual property infrastructure more efficient and transparent, and it should also facilitate the registration process so that Chinese brands can develop their overall brand equity potential.

⁴² Source: China General Chamber of Commerce

⁴³ Source: "Chinesische Firmen melden immer mehr Patente an", NZZ, March 6th 2012

⁴⁴ Source: "Research Confirms China Leads World in Patent Applications, Trademark Filings", Thomson Reuters 2011

⁴⁵ Source: "Trademarks in China", Thomson Reuters, 2011

Success factors to build sustainable Chinese brand equity

Based on the results, conclusions and assumptions of our own internal studies and of the external studies quoted above, on media articles and on best practice examples, we can derive important success factors for Chinese companies to build strong and valuable brands. The success factors can be classified into four categories:

- Local knowledge
- Innovation
- Brand-building
- Global expansion

Local knowledge

First, Chinese companies have to exploit and expand their local knowledge about how Chinese consumers' behavior is changing and affecting their business. Furthermore, they need to develop and implement efficient diffusion strategies so that their goods successfully reach their targeted consumers. In order to build brand awareness, this also includes creating product diffusion lines which entice the less affluent and raise brand recognition among aspiring young shoppers. To expand knowledge among their local consumers, Chinese companies will have to focus on consumer education. As Chinese consumers rate their domestic brands among the most successful ones in meeting their expectations,⁴⁶ Chinese companies can exploit this trust by educating and influencing their needs. For instance, the concept of luxury need not be the same as in western culture. China also has its definition of luxury that can be found in the traditional Chinese culture. Chinese companies need to create a luxury culture environment, giving ample opportunities to Chinese customers to practice their taste for a luxury lifestyle and build emotional connections with their brands.

Innovation

The second success factor is innovation. Being and especially being perceived as innovative is a strong differentiation opportunity also in regard to foreign brands entering the Chinese market. Chinese companies are already doing a good job by pushing their innovation processes, as reflected in the quick growth in patent applications. Haier's innovation strategy is already very successful, as the company keeps producing new ideas such as fridges with locks on them (to keep dormitory mates from snaffling food), compact washing machines (for the clothing of pampered pets)

and freezers with compartments that keep ice-cream soft (for impatient ice-cream aficionados).⁴⁷

Brand-building

In order to move up the value pyramid, it is indispensable for Chinese companies to deliver an emotional content to their consumers guaranteeing them exclusive use of the goods and services offered. It is therefore crucial that Chinese companies invest in old-fashioned brand building. As most Chinese companies are still characterized as price players, Chinese brands should focus on developing multi-faceted brands that address their various targeted segments individually. This of course implies that Chinese companies have to be aware of and exactly understand the purchasing behavior patterns and arising needs of the different segments they want to address. As also suggested by the McKinsey study, brands (or sub-brands) will in future have to be positioned to target narrower consumer segments and offer more tailored value propositions.⁴⁸ And finally, promoting a brand-specific brand culture seems to be an important success factor for Chinese companies in order to take into account the importance of emotional elements in Chinese consumers' purchase decisions and also to address their increasing love of self-expression.

Global expansion

Once a company has established a strong position in the domestic market, a logical and important step for building additional brand equity is global expansion. That is easier said than done, as Chinese brands are perceived differently in various countries. In general, the world associates Chinese brands first and foremost with affordable prices and value for the money. However, Chinese brands are sometimes also recognized for their quality, reliability, and attractiveness. Interestingly, certain markets are more open to Chinese brands and products than others. Growth markets like Argentina and Brazil seem to offer the warmest welcome, with the United States, Canada and Mexico more reserved but also welcoming.⁴⁹ Especially during the awareness and distribution-capability building phases, Chinese companies should be selective in choosing their markets. For each of the markets they choose to tackle, Chinese marketers will need to examine the best methods for building effective and stable awareness so that further brand equity

46 Source: "China Brand Opportunities", Accenture, 2007

47 Source: "Brand new", *The Economist*, August 4th 2012

48 Source: "Meet the 2020 Chinese Consumer", McKinsey&Company, 2012

49 Source: "China Brand Opportunities", Accenture, 2007

can be built. Once established in markets where they are better perceived, Chinese brands could leverage this equity as a qualifying asset in their more reluctant neighboring markets.

The role of the Chinese government

After considering the two main categories of brand value drivers, there is another element that also plays a very important role in the Chinese brand value development, namely the Chinese government. Until now, the Chinese government has been focusing on increasing economic growth and achieving social stability. The awareness of building intellectual property and developing Chinese brands has just begun. Hence, several actions have been started to assist Chinese companies in terms of investing in technology and R&D and giving financial advances to local companies. Furthermore the government has charged research institutions with the task of building research centers for intangible assets as well as for brand management, as evidenced by the recent foundation, in February 2012, of the first Chinese IP-Research Centre at Ren Min University (one of the top ten universities in China). In 2008, Prof. Wang from Beijing University founded the Brand Value Research Center in Beijing, supported by Beijing University and several state-based institutions. The purpose of all these efforts is clear: Chinese companies should pay more attention to the importance of building up their own brand value, not only to meet the changing needs of Chinese consumers, but also to become more competitive in the global market.

Even the current prime minister of China, Wen Jia Bao, has recognized that besides innovation in scientific technology, building up Chinese brands is also an important value driver for the growing economy. In his opinion, Chinese companies should on one hand build up their own intellectual property or rather their own brands by developing new product ideas. On the other hand they should become more competitive in the global market and improve product quality by reducing costs and enhancing efficiency on the basis of technological innovation so that they are able to outpace their competitors.

Parallel to the positive development of patent applications and trademark registrations (as stated above), the Chinese government is striving for higher protection of intellectual property. In the past few years, China has adopted new or massively rewritten laws in a wide range of areas covering economic relations such as patents, bankruptcy and product liability (to name but a few of these areas). In the context of intellectual property, Chinese companies have started to realize that owning IP is better than stealing it. Many Chinese entrepreneurs are asserting their IP in court and therefore making money out of it.

This growing perception of the value of intellectual property has its source in activities of the Chinese government. Their decision to start investigating China Telecom and China Unicom for abusing competition law sent a strong signal to consumers, showing that Chinese law can also be used to benefit consumers. In the past, IP piracy was a strong driver of economic growth in China. However, long term prosperity can only be achieved with self-created and strongly protected IP. A recently published article in the Financial Times says that “China will change when it can make more money by creating IP than by stealing it – and that this day is probably closer now than at any time for 30 years”.⁵⁰

IP protection is a crucial pillar for creating brand equity. Based on the international norm “Requirements for monetary brand valuation” (ISO 10668:2010), a valid and objective brand valuation requires not only the analysis of financial and behavioral aspects that have an influence on the monetary value of the brand. The legal aspect is also relevant when assessing brand value. That is, brand equity can only be created and sustainably maintained when IP is holistically protected by adequate laws. A changing attitude towards Chinese IP legislation is therefore an indispensable requirement to build strong domestic brand equity.

⁵⁰ Source: “Role of law breaks out in China”, Financial Times, December 13th 2011

Conclusion

Today most Chinese domestic brands still perform weakly compared to those from Europe and the US. At the same time, Chinese brands are facing huge challenges as Chinese consumers' needs are changing and more consumers are becoming mature and demanding, and because Chinese consumers are paying more attention to integrated factors related to products, such as brand, quality, price, and service. More and more multinational companies with higher brand awareness are entering the Chinese market and obtaining the confidence of Chinese consumers by providing them with branded quality products and a series of added values. Chinese local brands have to make big efforts to do the same, as they have been lacking in technology and suffering from poor image for a long time. Hence, Chinese companies have to become more competitive in their home market. But these challenges could turn out to be a great chance for Chinese domestic companies. Indeed, Chinese domestic brands are catching up. With the help of the Chinese government and the efforts of Chinese companies to catch up, Chinese brands are improving and brand values are growing. Nowadays, local brands are increasingly getting Chinese consumers' attention. Chinese brands have to adapt to new consumer needs such as delivering an emotional content along with the products that allows the Chinese to express their individuality. There are already several best practice examples of Chinese brands that have fruitfully implemented need-oriented brands and that have successfully positioned themselves in both the domestic and the global markets.

The new brand-driven behavior of Chinese consumers, the shifting attitude of Chinese companies towards brand-oriented management and the strong interest and support of the Chinese government in building strong domestic brands are the most promising factors for a substantial growth of Chinese brand equity in the future. Based on these factors, the assumption can be made that Chinese brand values will keep growing at a higher pace compared to already established brands in developed markets. The future of Chinese brand equity looks bright, providing that Chinese companies understand the indispensable value of strong and valuable brands and adequately adapt their brands and products to the demands of sophisticated consumers.

BV4

As independent Swiss brand valuation experts, BV4 calculates the financial value of brands and other intangible assets using both scientifically founded and standardized methods. BV4 also develops sector and client-specific brand management models. Thereby, BV4 combines the expertise and knowledge of finance specialists as well as brand experts and marketing professionals.

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