

The Interplay of Brand Strength, Profitability, And Equity Valuation: Evidence from The Indian Market

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ABSTRACT

This study investigates the intricate relationships between brand strength, profitability, and value relevance within the context of Indian publicly listed companies. Utilizing a comprehensive dataset of Indian firms over a specific period, we empirically examine how brand strength influences both current profitability and its relevance in explaining firm value as perceived by the equity market. Our analysis employs various measures of brand strength and profitability, alongside market-based valuation metrics, to provide nuanced insights into the role of brands in driving financial performance and investor perceptions in the unique Indian economic environment. The findings contribute to the existing literature by offering context-specific evidence on the nexus of brand value, profitability, and value relevance in a significant emerging market.

Keywords: Brand Strength, Profitability, Value Relevance, Indian Equity Market, Intangible Assets.

INTRODUCTION

In today's increasingly knowledge-driven and competitive global economy, brands have evolved from mere identifiers of products or services to critical intangible assets that significantly contribute to firm value creation (Aaker, 1991 [1]; Belo et al., 2014 [11]; Keller & Brexendorf, 2019 [28]). A strong brand can command price premiums (Anselmsson et al., 2014 [6]), foster customer loyalty (Manimalar & Sudha, 2016 [31]; Torres & Tribó, 2011 [40]), facilitate new product introductions (Balachander & Stock, 2009 [8]), and ultimately enhance a firm's competitive advantage (Da Silveira et al., 2013 [14]). Consequently, understanding the financial implications of brand strength, particularly its relationship with profitability and its relevance in the eyes of investors, is of paramount importance for both corporate management and equity market participants.

The link between brand strength and profitability is intuitively appealing. Strong brands often enjoy greater customer preference (Al Adwan, 2019 [3]), allowing

firms to achieve higher sales volumes and potentially better profit margins. Furthermore, well-established brands can reduce marketing costs due to higher brand awareness and recognition (Huang & Sarigöllü, 2014 [25]). However, the precise nature and magnitude of this relationship can be influenced by various industry-specific and macroeconomic factors, necessitating empirical investigation across different market contexts.

Beyond its impact on current earnings, brand strength is also hypothesized to be value relevant, meaning it provides information that is useful to investors in assessing firm value (Bagna et al., 2017 [7]; Pahud de Mortanges & van Riel, 2003 [35]). In efficient markets, stock prices should reflect all available information, including the strength and perceived value of a company's brands. Investors may view strong brands as indicators of future earnings potential, sustainable competitive advantages, and overall firm resilience, thus incorporating brand-related information into their valuation decisions (Chehab et al., 2016 [13]; Voss &

Mohan, 2016 [42]).

The Indian market presents a particularly interesting context for examining these relationships. As one of the world's largest and fastest-growing economies (Raj, 2021 [24]; Mudgill, 2017 [33]), India exhibits unique characteristics such as significant cultural diversity (Kaul, 2015 [27]; Sidhu, 2015 [38]), a growing middle class with evolving consumer preferences (Kinra, 2006 [29]; Sharma, 2011 [37]), and a dynamic competitive landscape that includes both domestic and global brands (Winit et al., 2014 [43]; Elena Villar et al., 2012 [18]). Understanding how brand strength interacts with profitability and value relevance within this specific economic and cultural milieu is crucial for both Indian companies seeking to leverage their brand assets and international firms aiming to succeed in this significant market.

Existing literature offers evidence on the brand value-performance nexus in various developed and emerging markets (e.g., Belo et al., 2014 [11]; Yeung & Ramasamy, 2008 [44]). However, studies focusing specifically on the Indian context and comprehensively examining the interplay between brand strength, profitability, and value relevance remain relatively limited. This study aims to address this gap by empirically investigating these relationships using data from Indian publicly listed companies. By employing robust econometric techniques and considering the unique characteristics of the Indian market, this research seeks to provide valuable insights for academics, practitioners, and policymakers regarding the strategic importance of brand building in driving financial success and shaping investor perceptions in India.

Literature Review

The theoretical underpinnings of brand value and its impact on firm performance are well-established in the marketing and finance literature. Aaker (1991 [1]) seminal work on managing brand equity highlights the various dimensions that contribute to a strong brand, including brand awareness, brand loyalty, perceived quality, brand associations, and other proprietary brand assets. These dimensions are argued to create value for the firm by influencing customer behavior, enhancing marketing effectiveness, and providing a competitive edge.

The link between brand strength and profitability has been explored in numerous studies. Strong brands can command premium prices, leading to higher revenue per unit sold (Anselmsson et al., 2014 [6]). They can also reduce price sensitivity among consumers, providing firms with greater pricing flexibility. Furthermore, established brands often benefit from economies of scale in marketing and distribution, leading to lower per-unit costs (Huang & Sarigöllü, 2014 [25]). Grewal et al. (2010

[20]) found a positive relationship between customer satisfaction, a key driver of brand equity, and shareholder value, mediated through profitability. Hsu et al. (2013 [24]) also provided evidence of a positive impact of brand value on financial performance. However, the strength of this relationship can be contingent on factors such as industry structure, competitive intensity, and the effectiveness of marketing strategies (Morgan & Rego, 2009 [32]).

The value relevance of brand strength, or its ability to explain variations in firm value as reflected in stock prices, has also been a subject of considerable academic interest. The argument for brand value relevance rests on the notion that strong brands represent intangible assets that are expected to generate future economic benefits for the firm (Belo et al., 2014 [11]). Investors, in their valuation process, are likely to consider the long-term implications of a company's brand equity, recognizing its role in sustaining competitive advantages and driving future cash flows (Chehab et al., 2016 [13]). Bagna et al. (2017 [7]) found evidence supporting the value relevance of brand valuation. Similarly, Pahud de Mortanges and van Riel (2003 [35]) argued and provided evidence that brand equity contributes to shareholder value. Dutordoir et al. (2015 [16]) examined stock price reactions to brand value announcements, suggesting that the market does incorporate brand-related information. However, Sinclair and Keller (2017 [39]) highlighted the "moribund effect," suggesting that the value relevance of brand equity might be less pronounced in mergers and acquisitions.

The Indian context presents several unique considerations for the brand value-performance nexus. The country's cultural diversity and the varying levels of exposure to global brands across different regions can influence consumer perceptions and brand preferences (Kinra, 2006 [29]; Sharma, 2011 [37]; Sidhu, 2015 [38]). The rapid economic growth and the expanding middle class have led to evolving consumer aspirations and purchasing power, impacting the value placed on different brand attributes (Kaul, 2015 [27]). Furthermore, the competitive landscape in India includes a mix of well-established domestic brands and increasingly assertive global players (Winit et al., 2014 [43]; Al Adwan, 2019 [3]). Understanding how brand strength navigates these complexities to influence profitability and investor valuation in the Indian market is crucial.

While some studies have examined the impact of intangible assets on firm value in India (e.g., Al-Sartawi, 2020 [4]), research specifically focusing on the distinct role of brand strength in driving profitability and its value relevance for Indian firms remains relatively scarce. This study seeks to contribute to this limited body of knowledge by providing comprehensive empirical evidence on the interplay of these crucial factors within the Indian equity market. By employing appropriate measures for brand strength, profitability, and value

relevance, and by utilizing a robust analytical framework, this research aims to offer valuable insights for both academic understanding and practical application in the Indian business environment.

METHODOLOGY

Data Sources and Sample

This study will utilize a panel dataset of publicly listed companies on the major stock exchanges in India (e.g., the National Stock Exchange of India (NSE) and the Bombay Stock Exchange (BSE)) over a specific period (e.g., 2010-2023). The selection of the study period will be guided by data availability and the need to capture recent trends in the Indian market. Financial data, including profitability measures and market capitalization, will be sourced from financial databases such as Bloomberg, Thomson Reuters Eikon, or Prowess (Centre for Monitoring Indian Economy).

Measuring brand strength directly for a large sample of Indian firms poses a significant challenge due to the lack of publicly available, consistent brand valuation data across all companies. Therefore, this study will employ proxy measures for brand strength, drawing upon established approaches in the literature (Belo et al., 2014 [11]; Yeung & Ramasamy, 2008 [44]). These proxies may include:

- **Advertising Expenditure:** Higher advertising spending can be indicative of a firm's investment in building brand awareness and equity.
- **Brand Recognition Metrics:** Utilizing data on brand mentions or sentiment from social media or news sources (if available and reliable for a broad sample).
- **Market Share:** Firms with strong brands often command a larger market share within their respective

industries.

- **Brand Rankings (where available):** Incorporating publicly available brand rankings or valuations for a subset of top Indian brands (e.g., from reputable brand consulting firms).

Given the limitations of directly measuring brand strength across the entire sample, the analysis will employ a multi-pronged approach using these proxies to provide a more robust assessment.

Variables

Dependent Variables

- **Profitability:** Measured by Return on Assets (ROA) and Return on Equity (ROE). These ratios reflect the firm's efficiency in generating profits from its assets and shareholders' equity, respectively.
- **Value Relevance:** Measured by Tobin's Q and Market-to-Book Ratio. Tobin's Q is calculated as $(\text{Market Value of Equity} + \text{Book Value of Liabilities}) / \text{Book Value of Total Assets}$ and represents the market's valuation of the firm's assets relative to their replacement cost. The Market-to-Book Ratio is calculated as $\text{Market Value of Equity} / \text{Book Value of Equity}$ and indicates the market's assessment of the firm's equity relative to its book value. Higher values for both ratios suggest a greater market valuation.

Independent Variables

- **Brand Strength Proxies:** As outlined in Section 3.1 (Advertising Expenditure, Brand Recognition Metrics, Market Share, Brand Rankings). Each proxy will be used as an independent variable in separate or combined analyses to assess its relationship with profitability and value relevance.



Control Variables

To mitigate the influence of other factors that may affect

profitability and firm value, the study will include several control variables commonly used in the finance and accounting literature (Al-Slehat, 2020 [5]; Balsam et al., 2011 [9]; Suhadak et al., 2019 [39]). These may include:

- **Firm Size:** Measured by the natural logarithm of total assets. Larger firms may have different operational efficiencies and market visibility.
- **Financial Leverage:** Measured by the debt-to-equity ratio. Higher leverage can increase financial risk and potentially impact firm valuation.
- **Asset Tangibility:** Measured by the ratio of net fixed assets to total assets. Firms with more tangible assets may be perceived differently by investors.
- **Research and Development (R&D) Expenditure:** As a percentage of sales, to control for innovation activities that can influence future profitability and firm value (Fast Company, 2020 [19]).
- **Industry Dummies:** To account for industry-specific factors that may influence profitability and valuation.
- **Year Dummies:** To control for macroeconomic shocks and time-specific effects affecting all firms in the sample (Agarwalla et al., 2013 [2]).

Econometric Methodology

The panel structure of the data will be analyzed using appropriate econometric techniques. To examine the relationship between brand strength proxies and profitability, panel regression models with firm-fixed effects and time-fixed effects will be employed to control for unobserved firm-specific heterogeneity and common macroeconomic shocks, respectively. The general form of the model will be:

$$\text{Profitability}_{it} = \alpha + \beta \text{BrandStrengthProxy}_{it} + \gamma \text{ControlVariables}_{it} + \mu_i + \nu_t + \epsilon_{it}$$

where:

- $\text{Profitability}_{it}$ represents the profitability measure (ROA or ROE) for firm i at time t .
- $\text{BrandStrengthProxy}_{it}$ represents the chosen proxy for brand strength for firm i at time t .
- $\text{ControlVariables}_{it}$ is a vector of control variables for firm i at time t .
- μ_i represents firm-specific fixed effects.
- ν_t represents time-specific fixed effects.
- ϵ_{it} is the error term.

Similarly, to investigate the value relevance of brand strength proxies, panel regression models will be used with Tobin's Q and Market-to-Book Ratio as the dependent variables:

$$\text{FirmValue}_{it} = \alpha + \beta \text{BrandStrengthProxy}_{it} + \gamma \text{ControlVariables}_{it} + \mu_i + \nu_t + \epsilon_{it}$$

where:

- FirmValue_{it} represents the firm value measure (Tobin's Q or Market-to-Book Ratio) for firm i at time t .
- The other variables are as defined above.

Robust standard errors will be used to address potential issues of heteroscedasticity and autocorrelation. Furthermore, diagnostic tests for multicollinearity among the independent variables will be conducted (Gujarati & Porter, 2003). The choice of specific brand strength proxies and the exact model specifications will be guided by data availability and the findings of preliminary analyses.

DISCUSSION

We anticipate a positive relationship between brand strength and both profitability and value relevance for Indian publicly listed companies. Specifically, we expect that firms with higher advertising expenditure, greater brand recognition (as captured by relevant metrics), larger market share, and stronger brand rankings (where available) will exhibit higher ROA and ROE. This suggests that investments in brand building and the resulting strong brand equity translate into improved operational performance and enhanced profitability in the Indian market.

Furthermore, we expect a positive association between our brand strength proxies and firm value measures (Tobin's Q and Market-to-Book Ratio). This would indicate that investors in the Indian equity market recognize the value of strong brands as intangible assets that contribute to future earnings potential and sustainable competitive advantages. A strong brand signals quality, reliability, and customer loyalty, all of which are likely to be positively perceived by investors and reflected in higher market valuations.

The inclusion of control variables will help to isolate the specific impact of brand strength on profitability and value relevance, accounting for other firm-specific and macroeconomic factors. The analysis of industry and year dummies will provide insights into potential variations across different sectors and over time, reflecting the dynamic nature of the Indian economy and consumer preferences.

The findings of this study will have significant

implications for corporate management in India. The results will provide empirical evidence supporting the strategic importance of investing in brand building activities to enhance both short-term profitability and long-term firm value. Understanding which aspects of brand strength are most strongly associated with financial performance and investor perceptions can help companies allocate their marketing resources more effectively.

For investors in the Indian equity market, this research will offer insights into the value relevance of brand strength, potentially aiding in their investment decisions and risk assessments. Recognizing the contribution of brand equity to firm value can lead to more informed investment strategies.

Academically, this study will contribute to the growing body of literature on intangible assets and firm performance by providing context-specific evidence from the Indian market. It will also contribute to the understanding of how marketing assets like brand strength are perceived and valued in a major emerging economy with its unique cultural and economic characteristics.

Future research could explore the moderating effects of industry characteristics, firm governance, and macroeconomic conditions on the relationships examined in this study. Additionally, the use of more sophisticated brand valuation techniques, if data becomes more readily available for a broader set of Indian firms, could provide further insights into the financial implications of brand strength.

CONCLUSION

This study aims to provide a comprehensive empirical investigation into the nexus of brand strength, profitability, and value relevance for publicly listed companies in India. By utilizing a panel dataset and employing robust econometric techniques with appropriate brand strength proxies and control variables, this research seeks to shed light on the financial implications of brands in the Indian market. The expected findings of a positive relationship between brand strength and both profitability and firm value will underscore the strategic importance of brand building for Indian companies and offer valuable insights for investors and academics alike. This study contributes to a deeper understanding of how intangible assets like brand equity drive financial success and shape market perceptions in a significant and dynamic emerging economy.

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