

## Research on brand extension feedback effects based on customer equity

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As a strategy for enterprises to expand the scale of their operations, brand extension could also generate feedback effect diluting parent brand's customer equity. This study proposes and estimates a theoretical model examining the influence of brand extension on the drivers of parent brand's customer equity, namely value equity, brand equity, and retention equity using data of 850 questionnaires from ordinary consumers in China. The model indicates whether the drivers of a parent brand's customer equity change after brand extension, and how fit and consumer evaluations of brand extension influence the drivers of the parent brand's customer equity. The results show that firstly brand extension influences the drivers of parent brand's customer equity, secondly fit and consumer evaluations of brand extension directly affect the drivers of parent brand's customer equity, consumer evaluations also perform an intermediary function between fit and the drivers of parent brand's customer equity. Finally, this paper talks about managerial implications of the finding. Limitations and suggestions for future research are also discussed.

### Introduction

With the intensification of competition in the market, the success rate of new products is generally low. For instance, in Chinese market, the average success rate is lower than 5%. But the R&D expenses of new products are pretty high. HUAWEI of China invested 4,5 billion dollars for new product development in 2012. So in order to solve the high-risk and high-cost problems, brand extension strategy, which means that enterprises use established brand name to launch new products in a completely new product category (Aaker & Keller, 1990), becomes increasingly popular.

However, brand extension is a double-edged sword. An inappropriate brand extension may blur consumer perceptions of the parent brand. Recently, scholars have made an intensive study of brand extension feedback effects, which means the effects of brand extension on the parent brand's image (Pina *et al.*, 2010), attitude (Dwivedi *et al.*, 2010), characteristic (Diamantopoulos *et al.*, 2005) and so on, but research on the effects of brand extension on the parent brand's customer equity has received little attention. Customer equity means the sum of discounted value of profit generated from all consumers' (existing and potential) purchase in their life cycle. Consumers' purchase decision rely on their perception of brand (including brand's image, attitude, characteristic etc.) to a large extent, so when consumers' perception of brand change due to brand extension, their purchase decision will change accordingly, parent brand's customer equity will also be different compared with that before brand extension. Therefore this paper tries to explore how brand extension affects the drivers of parent brand's customer equity.

Based on the customer equity model and introducing factors that influence brand extension as exogenous variables, this

paper considers the effects of brand extension on the drivers of a parent brand's customer equity, makes theoretical hypotheses, and constructs a model of the relationship between brand extension and customer equity to identify marketing activities that will dilute customer equity. It also makes theoretical suggestions for companies that wish to introduce brand extension. The model indicates whether the drivers of a parent brand's customer equity change after brand extension, and what factors influence the drivers of the parent brand's customer equity. There may be many factors that can influence the drivers of the parent brand's customer equity, but due to research feasibility, we only choose fit and consumer attitudes towards brand extension (ATT). Future research can continue to study other factors.

The remainder of this article is structured as follows. First, we review the relevant literature about brand extension and customer equity. Then, we propose nine hypotheses and construct our model based on our analysis of the relationship between brand extension and customer equity. Next, we obtain data through questionnaires and conduct an empirical analysis. We conclude with an overview of our findings, the managerial implications, and suggestions for future research.

### Literature review

Previous brand extension studies were conducted mainly from the perspective of consumers, namely how consumers evaluate brand extension and how brand extension affect consumers' perception of parent brand. Over the past 20 years, these studies have achieved fruitful theoretical results.

Specially, the researches on consumers' evaluation of brand extension give much attention to what factors affect their attitudes toward the extension (Aaker & Keller, 1990; Sar *et*

*al.*, 2011; Martinez *et al.*, 2009; Torelli & Ahluwalia, 2012; Meyvis *et al.*, 2012). Studies on brand extension feedback effects mostly explore the factors influencing feedback effects and theoretical mechanism, which consist of fit (Martinez & Chematony, 2004; Sood & Keller, 2012), brand concept (Riley *et al.*, 2013), parent brand awareness (Pina *et al.*, 2010) and motivation (Gurhan-Canli & Maheswaran, 1998) and so on.

Fit is considered as one of the most important variables influencing consumer attitudes towards brand extension (Volckner & Sattler, 2006) and one of the most involved variables in brand feedback effects studies. Fit comprises two dimensions: product category fit (the similarity in product category between a new product and the parent brand) and brand image fit (the consistency in brand image between a new product and the parent brand) (Aaker & Keller, 1990; Sar *et al.*, 2011). Consumer brand extension evaluation is often used to measure the success of a brand extension strategy, which involves a series of emotions and attitudes towards an extended product and is mainly used to measure the success of a brand extension strategy (Aaker & Keller, 1990).

The customer-centric theory came into being when companies began to pursue profit excessively and oversee the management of cost-causing consumer dissatisfaction and profit declines. Blattberg and Deighton (1996) came up with customer equity theory, holding that customer equity is the discounted lifetime value of all of a company's existing consumers. Rust *et al.* (2004) subsequently argued that customer equity should include not only existing customers, but also potential customers. Scholars continue to use Rust, *et al.*'s definition as standard (Wang, 2005; Skiera *et al.*, 2011), and this study follows suit.

Previous studies have paid much attention to the drivers of customer equity and gained fruitful results (Chang & Wang, 2007; Vogel *et al.*, 2008; Richards & Jones, 2008). Since the definition of customer equity is based on Rust *et al.*' study, and their research on the drivers of customer equity are also very systematic and thorough, so we also based on their work continue the following research. Rust *et al.* (2004) proposed three key drivers of consumer equity, including value, brand and relationship equity. Value equity indicates a consumer's objective evaluation of brand utility; brand equity refers to a consumer's subjective and intangible assessment of the brand, above and beyond its objectively perceived value; relationship equity is defined as the tendency of the customer to stick with the brand, above and beyond the customers' objective and subjective assessment of the brand.

## Research hypotheses

### Brand extension and customer equity

#### Value equity

Value equity has three driving elements: quality, price and convenience. Quality comprises entity products, service products, service delivery and the service environment. The performance of products/service is determined by company's technology and management. Price has three levels: everyday low prices, discounts and payments. A consumer's objective assessment of price mainly involves considering how attractive it is in relation to the company's marketing strategies. Convenience refers to the measures that companies take to help reduce the effort and time a consumer takes to do business with them. It also has three levels: location, ease of use and availability. Companies choose locations mainly for the convenience of consumer purchases. Whether the product is easy to use depends on its performance. Availability is related to the decisions that companies make on opening hours. It is clear that enterprises' brand extension strategy has no influence on the sub-drivers of value equity.

On the other hand, value equity is based on consumers' objective assessment, but previous brand feedback effects research mainly study the effects on parent brand's attitude, image, characteristic, which belong to consumer's subjective perception, so brand extension won't affect objective value equity. Therefore, the following hypothesis is proposed.

*H1: After brand extension, the parent brand's value equity, which comprises quality, price and convenience, remain unchanged relative to before the brand extension.*

#### Brand equity

Brand equity refers to a consumer's subjective and intangible assessment of the brand, above and beyond its objectively perceived value. It has three sub-drivers: brand awareness, attitude towards the brand and corporate ethics. Brand awareness is defined as the extent to which consumers can form knowledge structures and recollections about the brand. Consumer attitudes towards a brand comprise several levels: brand cooperation, brand extension, information communication, celebrity autograph, special event and product display. Corporate ethics refers to specific actions that can influence consumer perceptions of the organization. However, Shao and Zhang (2009) found that Chinese consumers could not distinguish between attitudes towards a brand and corporate ethics. Hence, she proposed changing the three original sub-drivers to brand awareness, reputation and preference. Brand reputation includes the two sub-drivers (attitude towards the brand and corporate ethics) of the traditional model. Brand preference reflects consumer preference for a brand. Because this study is also based on

Chinese consumers, we adopt Shao and Zhang's conceptualization.

As new products enter the market after a brand extension, existing consumers of the brand will develop a deeper understanding of the brand due to their heightened exposure to the products that adopt the brand name. Moreover, some new consumers will also become familiar with the brand name. Consequently, more and more consumers come to know the brand, and brand awareness is promoted (Han & Zhao, 2004). Even when a brand extension is unsuccessful, although the overall effects on the parent brand are unclear, awareness of the parent brand nevertheless improves during the initial phase. Therefore, the following hypothesis is proposed.

As brand extension cannot affect corporate ethics, we focus on its effects on attitudes towards a parent brand. In the consumer's mind, a brand refers to a network of knowledge structures comprising attributes, benefits and attitudes (Milberg *et al.*, 1997). Consumers process information on the new products after a brand extension that affects their cognitive schemas as they relate to the parent brand. So after brand extension, consumers' attitude, image toward parent brand will be different compared with that of before brand extension (Martinez & Chernatony, 2004), so will parent brand's reputation.

Based on cognitive psychology, preference is an attitude or tendency (Crites *et al.*, 1994). Consumer preference emerges when consumers learn about the difference of brand equity and then appear differentiation attitude toward the products/service of brand (Kotler, 2006), which will be influenced by the attractiveness of brand value (including consumers' perception value of brand and its importance) (Czellar & Palazzo, 2004). So after brand extension, consumers' attitude toward parent brand will be affected, so will brand preference.

Therefore, the following hypothesis is proposed.

*H2: After brand extension, some sub-drivers of parent brand's brand equity, such as brand awareness, increases relative to before the brand extension, while other sub-drivers, like brand reputation and brand preference, decreases relative to before the brand extension.*

### Relationship equity

Relationship equity includes five sub-drivers: special recognition and treatment, loyalty programs, affinity programs, community-building programs, knowledge-building programs. Because Chinese enterprises pay little attention to affinity programs and community-building programs resulting that consumers can't distinguish affinity programs from community-building programs, so we combine these two elements into one element: consumer group activity (Shao & Zhang, 2009).

Knowledge-building programs refer to the activities that can create structural bonds between the customer and the firm, making the customer less willing to recreate a relationship with an alternative provider. In a sense, brand extension can be considered as a knowledge-building program, since it can help enterprise better understand consumer tastes according to the extended product's consumption information, consumers will also have a better understanding about the brand because of the new extension information. So due to brand extension strategy knowledge-building programs will increase.

Consumer trust refers to a consumer's confidence in a trading partner's reliability and honesty and his/her willingness to trust in and rely on the enterprise (Moorman *et al.*, 1992). Although trust is not included as a driving element in the consumer equity model, it is an important index in their empirical research. Besides, consumer trust has an important effect on the formation of customer equity (Butler & Berry, 2002; Shao *et al.*, 2012), so we consider consumer trust to be a sub-driver of relationship equity. In essence, consumer trust is a state of mind, which will be affected by consumers' attitude toward company. After brand extension, consumers' attitude toward parent brand will be different, and then consumer trust toward parent brand will also change accordingly.

Therefore, the following hypothesis is proposed.

*H3: After brand extension, some sub-drivers of parent brand's brand equity, such as special treatment, loyalty programs and consumer group activities, remain unchanged relative to before the brand extension, while knowledge-building programs increases relative to before the brand extension, and consumer trust decreases relative to before the brand extension.*

### Fit, ATT and customer equity

Since brand extension doesn't affect value equity, there is no need to discuss the relationship between fit, ATT and value equity.

### Fit and brand reputation

Fit refers to the similarity of extended product and parent brand on product category, attribute, brand image and concept. After brand extension, consumers will form fit perception based on the relationship between extended product and parent brand. Then consumers will measure the degree of change of parent brand's mental schema based on fit perception. consumers' attitude, image toward parent brand are higher when there is a high degree of fit, meaning the information on the extended products and parent brand have much in common, parent brand's reputation is also higher (Martinez & Chernatony, 2004; Pina *et al.*, 2010). However, when there is a low degree of fit, their mental schemas change substantially.

Consumer evaluations of a parent brand are also based on the perception of the company's credibility (Aaker & Keller, 1990). Consumers use their existing brand knowledge to deduce whether a company has the ability to produce certain extended products. If there is a big difference between the parent brand and the extended product in terms of manufacturing technology or performance, consumers become suspicious of the company's motive in producing the low-fit product and its ability to produce high-quality extended products. After a comprehensive evaluation in which consumers assume that the company is unfairly attempting to capitalize on its reputation or is mistakenly stretching too far in the extension, they come to doubt the company's ability to use its existing technical equipment to produce high-quality products, and their confidence in the company is weakened.

#### *Fit, ATT and brand reputation*

Based on classification theory, when an enterprise launches a brand extension, consumers evaluate the fit between the extended products and the parent brand. If the degree of fit is high, it is easier for consumers to transfer their attitudes and feelings towards the parent brand to the extended products, and then a positive brand extension evaluation will form (Volckner & Sattler, 2006; Sar *et al.*, 2011; Meyvis *et al.*, 2012). Otherwise, if the degree of fit between the extended products and parent brand is low, consumers experience uncertainty about whether they can be classified into one category, and tend to evaluate the brand extension gradually. In this situation, any association consumers have with a parent brand and its extension influences their evaluation. Therefore, the fit between a parent brand and its extended products is considered an important factor in consumer brand extension evaluation.

When consumers form a positive evaluation of a brand extension, the new information related to extension has little influence on parent brand's mental schemas, consumers' attitude, image toward parent brand are higher (Martinez & Chernatony, 2004; Dwivedi *et al.*, 2010; Pina *et al.*, 2010), then parent brand's reputation will be higher; on contrary, when they evaluate a brand extension negatively, they may dislike the brand and even refuse to buy its products, then parent brand's reputation will be lower. So the following hypotheses are raised according to this analysis.

#### *Fit, ATT and brand preference*

We discussed that brand preference is an attitude, after brand extension, consumers' attitude toward parent brand will be affected, so will brand preference.

Therefore, the following hypothesis is proposed.

*H4: Fit has a positive and direct influence on some sub-drivers of parent brand's brand equity, like brand reputation and brand preference, after an extension.*

*H5: ATT have a positive influence on some sub-drivers of parent brand's brand equity, like brand reputation and brand preference, after an extension.*

*H6: ATT perform an intermediary function related to the fit and some sub-drivers of parent brand's brand equity, like brand reputation and brand preference, after an extension.*

#### *Fit, ATT and consumer trust*

We talked that after brand extension, some sub-drivers of parent brand's brand equity, such as special treatment, loyalty programs and consumer group activities, remain unchanged relative to before the brand extension. So here we only study the relationship between fit, ATT and consumer trust.

Consumer trust is a state of mind, which will be affected by consumers' attitude toward company. After brand extension, consumers' attitude toward parent brand will be different, and then consumer trust toward parent brand will also change accordingly. Moreover, consumers' attitude toward parent brand can be influenced by the perception of the company's credibility, if consumers believe that the company is unfairly attempting to capitalize on its reputation or is mistakenly stretching too far in the extension, then their confidence in the company will be weakened, and consumer trust toward parent brand will also be negatively affected.

Therefore, the following hypothesis is proposed.

*H7: Fit has a positive and direct influence on consumer trust after an extension.*

*H8: ATT have a positive influence on consumer trust after an extension.*

*H9: ATT perform an intermediary function related to the fit and consumer trust after an extension.*

Considering the above hypotheses, our conceptual models can be obtained as shown in Figure 1.

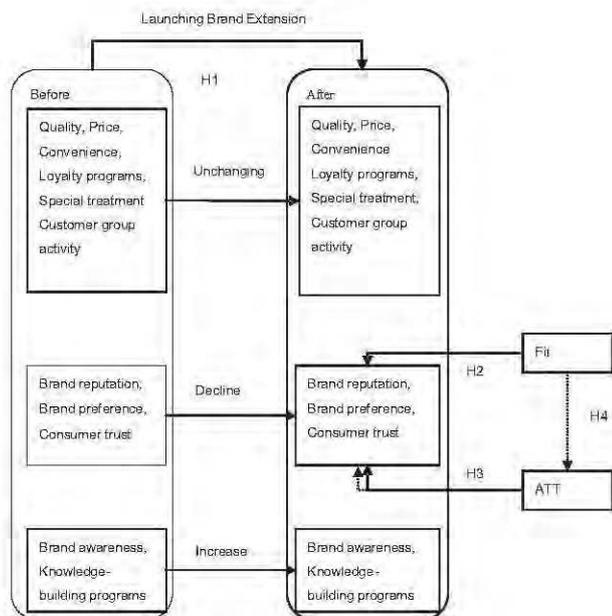


Figure 1: Conceptual model

Method

Measures

The variable index systems used in this study are taken from previous relevant studies. The index system for customer-equity-driving elements refers to the study by Rust *et al.* (2004). The index system for fit and ATT come from the study of Aaker & Keller (1990), Park *et al.* (1991), Taylor & Bearden (2003).

Sample and data

In empirical brand extension studies, marketing scholars have often adopted existing brands and virtual extended products as study objects, thus we also chose to follow this method. Based on four standards raised by Aaker & Keller

(1990), combing them with characteristics of the Chinese market, we selected two brand name in the fields of mobile phones and fashion: Nokia and Nike. The virtual extended mobile phone products were a Nokia digital camera (high fit) and a Nokia bicycle (low fit), and the virtual extended fashion products were Nike sportswear (high fit) and a Nike MP3 player (low fit).

Ordinary consumers in China were chosen as survey participants. 850 questionnaires were distributed and 802 were returned. After removing invalid questionnaires, 708 remained for analysis, resulting in an effective response rate of 83,29%.

Results

Reliability and validity

Cronbach's  $\alpha$  for the scale was greater than 8,5, and removing any of the items from the scale did not increase this value, thus indicating good reliability and internal consistency.

A validity analysis includes criterion, content and structural validity. Because selecting an appropriate criterion in a practical study is quite difficult, this study did not test criterion validity. The questionnaire adopted in this study was an existing scale that has been verified by marketing scholars as having good content validity. An analysis of the questionnaire's structural validity revealed that the KMO value was greater than 0,9 and that the Bartlett test was significant at the level of 0,000, indicating that the scale had good validity.

Rationality test of extended product selection

To test whether the selection of the extended products was reasonable, we assessed the difference in the degree of fit of these four extended products based on analysis of the questionnaire data. Table 1 shows the results obtained from a paired samples T-test.

Table 1: Paired samples test

	Mean	Std. Deviation	Paired Differences			t	df	Sig. (2-tailed)
			Std. Error Mean	95%Confidence interval of the Difference				
				Lower	Upper			
F camera F bicycle	0,702	0,855	0,046	0,611	0,793	15,247	344	0,000
F casual dress - FMp3	0,911	1,019	0,056	0,800	1,021	16,205	328	0,000

There was a considerable difference in the mean values of the extended products, and the difference was significant at the 0,05 level, indicating that the four extended products were reasonable.

## T-test

Hypotheses 1-3 are concerned with whether the various driving elements of parent brand customer equity change before and/or after brand extension. Paired samples T-tests were used to test the hypotheses. Table 2 shows the analysis results. For brand extensions with high fit, the p values for brand awareness, brand reputation, knowledge building programs and consumer trust were significant at less than 0,05. The values for others were greater than 0,05 and thus non-significant. The results indicate that after the brand

extension, notable changes occurred in the sub-driving elements of quality, brand awareness, brand reputation, brand reference, knowledge building programs and parent brand consumer trust relative to before the extension, but the other seven sub-driving elements were not influenced by the extension. But for low fit extensions, quality and brand reference were also not influenced. In conclusion, Hypothesis 1 is tenable, and parts of Hypotheses 2 and 3 are tenable.

**Table 2: Paired samples test**

	Before	Mean	After	t	Sig.
<b>High fit</b>					
Quality	4,05		4,02	1,134	0,257
Price	3,41		3,44	-0,861	0,390
Convenience	3,85		3,84	0,282	0,778
Brand awareness	3,20		3,55	-9,066	0,000
Brand reputation	3,67		3,47	8,665	0,000
Brand preference	3,21		3,19	-0,514	0,608
Loyalty programs	3,28		3,35	-1,805	0,072
Special treatment	3,06		3,10	-1,402	0,162
Customer group activity	3,15		3,18	-0,580	0,562
Knowledge-building programs	2,58		2,77	-5,782	0,000
Consumer trust	3,78		3,53	7,909	0,000
<b>Low fit</b>					
Quality	4,05		3,76	7,531	0,000
Price	3,41		3,35	1,764	0,079
Convenience	3,85		3,80	1,408	0,160
Brand awareness	3,20		3,43	-5,830	0,000
Brand reputation	3,67		3,27	11,816	0,000
Brand preference	3,17		3,02	3,497	0,001
Loyalty programs	3,28		3,32	-1,023	0,307
Special treatment	3,06		3,07	-0,293	0,770
Customer group activity	3,15		3,14	0,333	0,739
Knowledge-building programs	2,58		2,77	-6,008	0,000
Consumer trust	3,78		3,33	10,050	0,000

## Regression analysis

For Hypotheses 4-5, 7-8, we conducted a regression analysis. The results in Tables 3 and 4 show that the p value for the model F test was 0,000, indicating the regression

equation was ideal. The p value for the independent variables and constant term T was also 0,000, indicating that the regression coefficient was significant. Therefore, Hypotheses 4-5, 7-8 are all tenable.

**Table 3: Regression**

Independent Variable	Dependent Variable: Brand Reputation		Dependent Variable: Brand Preference		Dependent Variable: Consumer Trust	
	B.	Sig.	B.	Sig.	B.	Sig.
(constant)		0,000		0,000		0,000
<i>ATT</i>	0,488	0,000	0,406	0,000	0,452	0,000

**Table 4: Regression**

Independent Variable	Dependent Variable: Brand Reputation		Dependent Variable: Brand Preference		Dependent Variable: Consumer Trust	
	B.	Sig.	B.	Sig.	B.	Sig.
(constant)		0,000		0,000		0,000
<i>F</i>	0,451	0,000	0,361	0,000	0,378	0,000

### Test of intermediary effect

This study adopted the method described by Wen *et al.* (2006) to test Hypothesis 4. The independent variable was fit (*F*), the mediating variable was ATT and the dependent variables were brand reputation, brand preference and consumer trust. The above regression analysis showed that the independent variable had a notable influence on the dependent variables, and that the mediating variable had a

notable influence on the dependent variables. Therefore, we continue to analyse the relationship between fit and ATT.

Table 5 shows that the effects of the independent variables on the dependent variables were generated partly through the intermediary variables. Table 6 shows that ATT performed an intermediary function related to fit and brand reputation, brand preference and consumer trust following an extension. Therefore, Hypothesis 6 and 9 is tenable.

**Table 5: Regression**

Model	Unstandardized Coefficients		Standardized Coefficients	<i>t</i>	Sig.	<i>F</i>	Sig.
	<i>B</i>	Std. Error					
(constant)	0,862	0,055		15,755	0,000		
<i>F</i>	0,769	0,016	0,782	47,194	0,000	2227,299	0,000

**Table 6: Regression**

Independent Variable	Dependent Variable: Brand Reputation		Dependent Variable: Brand Preference		Dependent Variable: Consumer Trust	
	<i>B.</i>	Sig.	<i>B.</i>	Sig.	<i>B.</i>	Sig.
(constant)		0,000		0,000		0,000
<i>F</i>	0,178	0,001	0,111	0,043	0,064	0,238
<i>ATT</i>	0,349	0,000	0,319	0,000	0,402	0,000

### Discussion and limits

After an enterprise launches a brand extension, various driving elements of the parent brand's customer equity change to varying degrees.

For value equity, price and convenience are not influenced by any brand extension strategy. Quality is not influenced in high-fit brand extensions. However, in low-fit brand extensions, consumer quality evaluations of a parent brand decline after the extension. This is not fully consistent with the initial hypothesis, perhaps because consumer evaluations of product quality are not based solely on rational and objective evaluations, as described in the value equity definition. Emotion is also an influencing factor. When an enterprise launches a low-fit brand extension, consumers may consider that the enterprise is launching a transition extension. Their confidence in the enterprise declines, and thus they start to doubt the quality of the parent brand's product.

In terms of brand equity, parent brand awareness after an extension increases relative to before the extension, and brand reputation declines. Brand preference remains unchanged when the brand is extended into a high-fit product field, but declines when the brand is extended into a low-fit product field. The scale adopted in this study has been used mainly in Western studies. The formation of brand preference is related to social concepts and popular attitudes to some degree. In traditional Western culture, personal concepts are more open and people often pursue independence and diversity, whereas China's traditional culture is relatively conservative, narrow and advocating the straight. Therefore, if enterprises launch a brand extension,

consumer preference for parent brand changes only when the extended product is highly dissimilar to the parent brand.

In terms of relationship equity, as the hypothesis states, loyalty programs, special treatment and consumer group activities are not influenced by brand extension, knowledge-building programs increase relative to before the extension, and consumer trust declines.

These conclusions have some reference value for managers. When enterprises decide whether to launch a brand extension, they should consider not only the success rate of the new product, but also the negative influence of brand extension on parent brands. Achieving new product success at the cost of a negative influence on the parent brand is not an advisable strategy, and will obscure consumer understanding and perceptions of the brand. When launching a brand extension, enterprises should avoid such a seesaw effect and strive to realize mutual benefits for both the parent brand and the new product.

Fit and ATT have a positive influence on the parent brand's reputation, brand preference and consumer trust after a brand extension. At the same time, consumer attitudes towards a brand extension perform an intermediary function related to fit and brand reputation, brand preference and consumer trust after the extension. When an enterprise launches a brand extension, it should avoid low fit in its extended products. Instead, the enterprise should adopt successive brand extension strategies, and the fit of each extended product should change only a little compared with that of the last extension. When the enterprise chooses to enter an unrelated product market, it should select related

products as a bridge and finally make the transition to the target field.

Although this study has some practical significance in guiding enterprises to launch brand extensions, it has some limitations. First, it analyses only the function of fit and ATT when considering the factors that influence parent brand customer equity. Future studies may include the influence of other factors. Second, the study adopted two brands, Nokia and Nike. Because numerous factors such as the degree of consumer intervention are different for other brands in other industries, further research into whether the conclusions of this paper are universally applicable is required. Finally, this study is based on Chinese consumers. Future studies may consider its conclusions in relation to different cultural backgrounds.

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