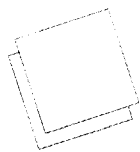


An executive summary for managers and executive readers can be found at the end of this article



The effects of expert quality evaluations versus brand name on price premiums

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Abstract Investigates the extent to which expert evaluations of quality impact price premiums of national brands over the store brands. Using data from Consumer Reports, finds that the average quality of store brands exceeds the average quality of national brands in 22 out of 78 product categories. Yet store brands typically do not charge price premiums, while national brands do (28.7 percent price premium on average). When national brands have higher quality, however, they increase the price premium from 28.7 percent to 50.4 percent on average. Regression analysis predicts that a national brand would command 37 percent price premium over a store brand that offers the same quality, a finding that highlights the handsome returns on building brand equity.

Introduction

A recent issue of *Consumer Reports* (June, 2001) featured an article "Tuna goes upscale", in which canned tuna fish were ranked by quality. The list of brands included both national brands such as Bumble Bee and StarKist as well as store brands[1] from retailers such as Safeway and Albertson. Surprisingly, in the light tuna in water category, the highest quality brand as well as the "CR best buy" was not a national brand, rather a store brand of Safeway's.

Higher quality standards imposed

Although store brands were traditionally perceived to be of lower quality compared with national brands, they have substantially improved their quality in the last decade (DeNitto, 1993; Quelch and Harding, 1996; Dunne and Narasimhan, 1999). Reasons for this improvement include higher quality standards imposed by powerful retailers, the desire of retailers to offer consistent quality, and the increased cooperation between manufacturers and retailers to develop store brands that match consumer tastes. Another factor was the introduction of premium private-label brands. For example, Lablows (the largest Canadian grocery chain) introduced the well known President's Choice brand, which is licensed to retailers in the USA and in other countries. So if a store brand has same or higher quality than a national brand, can it receive a price premium?

Recently, Sethuraman and Cole (1999) and Sethuraman (2000) investigated the factors that influence consumers to pay more for national brands than store brands. These studies show that price premiums of national brands depend on consumer demographics (i.e. gender, education, income) and the perceived quality differential between national and store brands. To



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National brands command significant price premiums

complement and extend this line of investigation. In this paper, we investigate whether "objective" quality differential, as measured by quality evaluations of expert judges of *Consumer Reports*, is related to the price premiums over and above the brand-name effect.

Specifically, this paper seeks to answer the following questions:

- To what extent do store brands possess higher quality compared with national brands?
- Do national brands with quality lower than that of store brands still receive higher prices?
- What price premiums do national brands receive as a function of their objective quality differential?

Using data from *Consumer Reports*, we find that the average quality of store brands actually exceeds the average quality of the national brands in 22 out of 78 product categories. In other words, for one out of four product categories, an average store brand is of better quality compared with the average national brand. In 22 categories where store brands have higher average quality, store brands typically do not receive higher prices and the national brands receive almost a 30 percent price premium. In the remaining 56 categories where national brands have higher quality, the average price premium increases to about 50 percent. Thus, national brands command significant price premiums even when they have a lower average quality than store brands.

Based on the regression analysis, we find that average price premium of national brands relative to store brands decreases as the quality of store brands improves. The estimation also shows that on average national brands receive 37 percent price premium over store brands if their quality is the same. These results suggest that national brands lose some – but not all – of their pricing power as their relative quality decreases.

Price is not a reliable signal of quality

Related literature

Previous research has used quality rankings of *Consumer Reports* to investigate the relationship between market prices and objective quality (e.g. Riesz, 1978, 1979; Gerstner, 1985; Steenkamp, 1988; Bodell *et al.*, 1986; Montgomery and Wernerfelt, 1992; Faulds *et al.*, 1995). Most studies found a positive but weak correlation between price and quality, implying that price is not a reliable signal of quality. However, these studies did not investigate the quality differences between national brands and store brands, and how quality differences influence the price premiums of national brands. In particular, if consumers pay higher prices for branded products, are they always getting a better quality?

Another stream of research was aimed at explaining the variation in penetration and profitability of store brands across product categories (e.g. Hoch and Banerji, 1993; Raju *et al.*, 1995), and across retailers (Dhar and Hoch, 1997). It seems that store brands succeed in product categories that have:

- high margins;
- less intensive brand advertising; and
- presence of high quality store brands.

Introducing store brands helps retailers gain concessions

The introduction of store brands is likely to increase retailers' profits in product categories in which the cross-price elasticity between national brands is low, but cross-price elasticity between national and store brands is high. Retailers who introduce store brands perform better when they commit to store brands with high quality (even premium store brands), when they sell a large variety of products with the store brand name, and when they use their own name. Narasimhan and Wilcox (1998) argue that introducing store brands helps retailers gain concessions from the national brand manufacturers.

Our paper is related to research aimed at explaining variations in contribution margins (i.e. price minus variable cost) in the food industry. Wills and Mueller (1989) found that advertising has a positive effect on the price of national brands relative to store brands. Connor and Peterson (1992), who used store brands as a proxy of cost, found that higher industry concentration and more advertising led to higher prices of national brands relative to store brands. These studies did not investigate the impact of quality difference on price differences between national brands and store brands.

Several studies have analyzed the behavioral aspects of the relationships between price and perceived quality and between brand name and perceived quality. Specifically, the meta-analyses of Rao and Monroe (1989) indicate that, for consumer products, the relationships between price and perceived quality and between brand name and perceived quality are positive and statistically significant. The positive effect of store name on perceived quality is small and not statistically significant. However, the type of experimental design and the strength of the price manipulation were found to influence significantly the observed effect of price on perceived quality.

Testimony to the power of branding

More recently, Sethuraman and Cole (1999) and Sethuraman (2000) surveyed consumers for their perceptions of price and quality of national and store brands across 20 product categories. They show that a perceived quality differential increased the ability of national brands to receive price premiums over store brands. We take a different perspective to examine the pricing power of national brands relative to store brands. Specifically, we use objective quality ratings, as judged by experts at *Consumer Reports*, rather than consumers' perceived quality. Our results show that objective quality of store brands reduces the price premium gap, but does not eliminate it – this finding is a testimony to the power of branding. Next we present the data used for this study.

Data

We collected data from various issues of *Consumer Reports* (1990-1997) that included the following variables:

- *National brands vs Store brands.* *Consumer Reports* lists the names of the brands used in its rankings. We used *Brands and Their Companies* (Stetler, 1993) to identify the owner of the brand. If the owner was identified as a producer, we classified it as a "national brand". If the owner was identified as a distributor, we classified it as a "store brand". In a few cases the owner could not be identified, and these brands were omitted from the sample.
- *Quality.* *Consumer Reports* uses laboratory tests and controlled-use tests to evaluate product quality. They adopt a point system of rating product characteristics such as taste, nutrition, convenience of use, safety,

effectiveness, and overall quality. They combine these ratings to construct a single index for quality, which is presented in bar charts in the various issues of *Consumer Reports*. Using a ruler, we measured the length of the quality index in a bar chart on an interval from zero to 3.5cm (which was the longest across all products). For example, the rating of Maull's Smokey Barbecue Sauce is 2.3cm, and we assign it a quality level of 2.3.

- *Price.* A price of an item is based on a nationwide survey of supermarkets conducted by *Consumer Reports*. When the item varies by size or weight, its price per unit size or per unit weight is used. Because larger sizes typically have significantly lower unit prices (Gerstner and Hess, 1987), we included brands with identical or very similar sizes to those of store brands in that product category.

The resulting sample consists of 755 frequently purchased grocery brands from 78 product categories with at least one store brand in each product category. Table I reports the average price and quality premiums (of national brands) for product categories in which quality premium is non-positive (i.e. negative or zero). Table II presents the equivalent information for product categories in which quality premium is positive.

| Category | No. of products | Price premium (percentage) ^a | Quality premium (percentage) ^a |
|---|-----------------|---|---|
| 1. Cheese – product (light) | 6 | 100.00 | -43.64 |
| 2. Hot dogs – poultry | 8 | 20.24 | -36.67 |
| 3. Tea – Darjeeling (25oz) bagged | 3 | 18.75 | -25.96 |
| 4. Potato chips – regular non-ridged | 11 | 56.28 | -18.67 |
| 5. Garbage bags – tall kitchen (13 gallons) twist tie | 15 | -16.25 | -14.22 |
| 6. Cola – diet | 8 | 58.82 | -11.79 |
| 7. Garbage bags – trash (30 gallons) tie | 11 | -19.23 | -11.77 |
| 8. Garbage bags – lawn and leaf (39 gallons) – tie | 7 | -20.00 | -11.05 |
| 9. Chocolate chip cookies – packaged (hard) | 17 | 42.45 | -8.58 |
| 10. Tuna – light in oil | 7 | -7.97 | -7.95 |
| 11. Turkey – fresh | 6 | 1.00 | -7.29 |
| 12. Spaghetti (16oz) | 18 | 13.96 | -4.94 |
| 13. Tuna – light in water | 12 | 20.86 | -4.76 |
| 14. Pancake syrups – not maple (24oz) | 12 | 65.77 | -4.59 |
| 15. Fabric softener – dryer sheets (36-40 sheets) | 13 | 59.09 | -3.58 |
| 16. Peanut butter – chunky (regular) | 9 | 14.29 | -2.96 |
| 17. Food wrap – freezer bags (1 gallon) | 9 | 12.50 | -2.88 |
| 18. Yogurt – strawberry (low fat) 8oz | 10 | 69.70 | -2.76 |
| 19. Cheeses – cheese food | 9 | 39.05 | -2.72 |
| 20. Peanut butter – creamy (regular) | 10 | 10.61 | -1.89 |
| 21. Soap bar – normal (hand and bath) (5oz) | 8 | 58.33 | -1.67 |
| 22. Tea – chamomile (20oz) bag | 2 | 33.33 | 0.00 |
| Average | 10 | 28.71 | -10.47 |

Note: ^a The price premium was calculated as follows – for each product category, we computed the difference between the average price of national and store brands, divided it by the average price of the store brand, and then multiplied the result by 100. The quality premium was computed in a similar way

Table I. Price premiums for categories with non-positive quality premiums

| Category | No. of products | Price premium (percentage) | Quality premium (percentage) |
|--|-----------------|----------------------------|------------------------------|
| 1. Spaghetti sauce – meatless (long cooked) (26-32oz) in glass | 7 | 44.71 | 0.78 |
| 2. Pot pie – chicken (7-8oz) | 9 | 29.23 | 1.00 |
| 3. Orange juice – frozen concentrate | 11 | 7.88 | 1.18 |
| 4. Food wrap – storage bags (1 gallon) | 18 | 11.11 | 2.19 |
| 5. Peanut butter – chunky (natural) | 5 | 26.00 | 2.73 |
| 6. Food wrap – plastic wraps | 15 | 16.67 | 3.16 |
| 7. Ice tea – raspberry (bottled and can) – non-diet (16oz) | 7 | 29.81 | 3.33 |
| 8. Ice tea – lemon (bottled and can) – non-diet (16oz) | 9 | 40.70 | 3.38 |
| 9. Sunscreens – SPF 15 (sun block) | 5 | 65.78 | 3.70 |
| 10. Spaghetti sauce – meat (long cooked) (26-32oz) in glass | 3 | 4.55 | 5.17 |
| 11. Dishwasher detergents – powder (50oz) | 14 | 140.25 | 5.47 |
| 12. Fabric softener – detergent softener | 9 | 33.33 | 5.94 |
| 13. Rice – white long-grain (regular) | 11 | 68.75 | 6.09 |
| 14. Food wrap – aluminum foils | 12 | 23.08 | 6.19 |
| 15. Peanut butter – creamy (natural) | 5 | 25.68 | 6.60 |
| 16. Soups – tomato (canned concentrated) (11oz) | 8 | 38.16 | 6.65 |
| 17. Ground coffees – regular (10-13oz) | 25 | 48.61 | 7.10 |
| 18. Tea – black (bags, 48-50oz) non-organic caffeinated | 10 | 33.33 | 7.72 |
| 19. Pot pie – turkey (7-8oz) | 5 | 54.17 | 8.75 |
| 20. Yogurt – strawberry (non-fat) 8oz | 6 | 88.00 | 9.09 |
| 21. Instant coffee – regular (4oz) | 10 | 16.67 | 9.93 |
| 22. Spaghetti (12oz) | 3 | 9.09 | 13.04 |
| 23. Tea – English breakfast (24-25oz) bag | 4 | 28.57 | 13.19 |
| 24. Soups – chicken noodle (canned concentrated) (11oz) | 5 | 44.55 | 14.13 |
| 25. Pot pie – beef (7-8oz) | 6 | 107.69 | 14.47 |
| 26. Low-fat frozen dessert – yogurts (vanilla) | 13 | 113.37 | 15.15 |
| 27. Orange juice, chilled, concentrated | 19 | 7.46 | 15.82 |
| 28. Dishwasher detergents – liquid gel | 7 | 140.91 | 16.22 |
| 29. Ground coffees – decaffeinated (10-13oz) | 20 | 16.47 | 16.47 |
| 30. Bread – whole wheat | 19 | 42.09 | 17.14 |
| 31. Laundry detergents – liquid (64oz) concentrated | 10 | 123.61 | 20.25 |
| 32. Cola – non-diet | 8 | 47.12 | 20.29 |
| 33. Garbage bags – trash (30 gallons) drawstring | 5 | 30.65 | 21.24 |
| 34. Ice-cream – vanilla | 17 | 21.33 | 22.76 |
| 35. Spaghetti sauce – meat (moderately cooked) (26-32oz) glass | 6 | 71.88 | 23.44 |
| 36. Garbage bags – tall kitchen (13 gallons) – drawstring | 5 | -11.11 | 23.96 |
| 37. Low-fat frozen dessert – ice milks (chocolate) | 4 | 69.23 | 25.45 |
| 38. Tuna – white in water (6 1/8oz) | 10 | 8.67 | 25.94 |
| 39. Cheeses – American | 7 | 43.33 | 27.68 |
| 40. Ice-cream – cookie dough | 6 | 250.00 | 30.37 |
| 41. Chilli – canned with beans (15oz) | 18 | 23.41 | 30.43 |

(continued)

Table II. Price premiums for categories with positive quality premiums

| Category | No. of products | Price premium (percentage) | Quality premium (percentage) |
|--|-----------------|----------------------------|------------------------------|
| 42. Ice-cream – chocolate | 11 | 85.32 | 31.56 |
| 43. Hot dogs – beef (8-10 Frankfurters) | 8 | 2.14 | 33.73 |
| 44. Turkey – frozen | 6 | 30.25 | 35.29 |
| 45. Cola – non-diet caffeine-free | 7 | 52.22 | 36.30 |
| 46. Low-fat frozen dessert – yogurts (chocolate) | 10 | 127.94 | 37.19 |
| 47. Bread – commercial white | 14 | 80.77 | 39.47 |
| 48. Low-fat frozen dessert – ice milks (vanilla) | 8 | 115.38 | 44.11 |
| 49. Tea – black (bags, 48-50oz) non-organic decaffeinated | 9 | 13.33 | 46.94 |
| 50. Fabric softeners – rinse liquids (64oz) | 12 | 68.33 | 62.61 |
| 51. Spaghetti sauce – meatless (moderately cooked) (26-32oz) glass | 16 | 28.40 | 67.69 |
| 52. Barbecue sauces (18oz) | 20 | 54.31 | 70.21 |
| 53. Cranberry sauces | 5 | 15.86 | 73.08 |
| 54. Hot dogs – meat (8-10) | 18 | 13.47 | 92.06 |
| 55. Cola – diet caffeine-free | 5 | 70.59 | 142.86 |
| 56. Tea – Earl Grey (25oz) bag | 4 | 28.57 | 337.50 |
| Average | 10 | 50.39 | 29.72 |

Table II.

Two results observed

Results

Table I includes those 22 product categories in which an average store brand has higher quality compared with an average national brand. Table II includes those 56 product categories for which an average store brand has lower quality than an average national brand. Based on Tables I and II, we observe the following two results:

Result 1. The quality premium of national brand over store brands varies substantially across product categories.

Result 2. National brands receive 28.7 percent price premium on average when their average quality is lower than an average store brand. This price premium increases to 50.4 percent when the average quality of national brands is higher.

Price premium

Regression analysis

We seek to estimate the differential impact of brand type and quality difference on price premium of national brands. We can then determine the extent to which price premiums are due to branding alone after controlling for quality differences. To this end, we formulate a Hotelling-type economic model of price competition between national and store brands, and derive the regression equation (see Appendix for details):

$$\left(\frac{P-p}{p}\right) * 100 = b_0 + b_1(Q-q), \quad (1)$$

where P and p denote the average price of the national brand and store brand, respectively; Q and q denote the average quality of the national brand and store brand. In equation (1), we use *percentage* price premiums (and not price differences as in equation (6A) in Appendix) so that we can make price comparisons across different product categories as in Tables I and II. The constant b_0 in equation (1) is an average price premium of a national brand when both national and store brands have the same quality (i.e. $Q = q$). We

retain quality difference as the independent variable, consistent with equation (6A) in the Appendix, because quality was measured on the same scale across all product categories. The coefficient, b_1 , captures percentage price premium attributable to a unit increase in average quality difference between national and store brands.

Table III reports the estimates obtained from ordinary least square (OLS) and weighted least squares (WLS) for the parameters of equation (1). The WLS coefficient estimates, which correct for heteroscedasticity, are statistically significant at the 5 percent level[2]. Therefore we conclude that:

Result 3. National brands receive 37 percent price premium on average even when no quality difference exists between national brands and store brands on average.

Result 4. The price premium of a national brand increases with its quality difference.

As store brands improve quality, national brands lose some pricing power

Figure 1 illustrates *Result 3* and *Result 4*. Specifically, *Result 4* indicates that, as store brands improve their quality, national brands lose some of their pricing power and the price premium they can command relative to store brands decreases. This result empirically validates Rao and Monroe's (1996, p. 517):

P1. The magnitude of price premiums will be positively related to the relative quality of the product, *ceteris paribus*.

However, our analysis predicts that the price of national brands is likely to be significantly higher than the price of store brands, even in product categories

| Coefficient | OLS | WLS |
|---|----------------|----------------|
| Constant, b_0 | 0.38 (6.94) | 0.37 (8.07) |
| Quality premium, b_1 | 0.23 (1.89) | 0.30 (2.08) |
| Coefficient of determination, R^2 (%) | 4.42 | 5.45 |

Table III. Impact of quality difference on national brand price premium



Figure 1. Price premium of national brands as a function of quality gap between national and store brands

National brands receive a substantial premium

Buying national brands does not always guarantee higher quality

in which the quality of store brands meets or exceeds the quality of national brand (as in the tuna fish example in the Introduction).

Conclusion

Given the pursuit for quality improvement by store brands, we wanted to determine the extent to which an average store brand exceeds an average national brand in quality, and the impact of quality differences between national and store brands on price premiums. Using data from *Consumer Reports*, we find that quality differences between national brands and store brands vary significantly across product categories and, for one in four product categories, the average quality of store brands was actually higher. In spite of this, national brands receive a substantial premium (30 percent on average) even when the average quality is lower. When the average quality of national brands is higher, the average price premium increases to 50 percent.

Applying regression analysis, we found support for the hypothesis that price premiums of national brands prevail regardless of whether they have a quality advantage over store brands or not. We also found support for the hypothesis that price premiums for national brands increase with their quality difference.

In conclusion, quality improvements do not enable the store brands to charge price premiums, thus highlighting the handsome returns to building brand names (Jones, 1986). Consequently, consumers who are value-oriented should be cautioned that buying national brands does not always guarantee higher quality, and that price premiums for national brands exist even when they are of lower quality.

Notes

1. Store brands are owned or controlled by retailers, whereas national brands are typically owned by manufacturers.
2. We determine the weights by specifying the error variance as power function of the absolute quality differences (i.e. $\sigma^2 = (|Q - q|)^{\alpha}$), and the best fitting model resulted in $\hat{\alpha} = 0.5$.

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Appendix. Theoretical model for equation (1)

We derive the regression equation (1) using a Hotelling-type model (Hotelling, 1929). In the model, there are two firms with two different types of firms – the national brand firm and a competing store brand firm – who differentiate themselves with respect to quality and brand name. The firms set product prices to maximize profit given the quality and brand type of each product. The national firm's product has brand-name recognition, whereas the competing firm's product does not have brand-name recognition. The national brand provides its consumers with a utility that can be separated into two components: utility from quality and utility from brand name. The store brand provides its consumers with utility derived from quality only (no brand-name recognition).

Consumers choose the product that provides them with the highest surplus, which is a function of prices, quality and brand-name recognition. For notational purposes, we use capital letters to denote variables of the national brand, and lower case letters to denote variables of the store brand. Let P and Q denote the price and quality of the national brand, respectively. Similarly, let p and q denote the price and quality of the store brand. Finally, let B denote the brand recognition of the branded product, and that of the store brand is normalized to zero.

Each consumer buys one product based on price, quality and the brand type. The utility of consuming the product is broken into three parts: a basic value ν , the value from quality, and the value from brand recognition, if it exists. That is, the total utility from the national brand is $\nu + \alpha Q + \beta B$, where α denotes the impact of quality on consumer utility and β represents the impact of brand recognition on consumer utility. Similarly, the total utility obtained from consuming the store brand is $\nu + \alpha q + \beta 0 = \nu + \alpha q$.

We assume that the impact of quality is identical for all consumers, and model it by a constant coefficient α . In contrast, we let the value of brand recognition differ across different

consumers, and model this heterogeneous impact by the density function $f(\beta)$. The cumulative distribution function is denoted by $F-\beta$.

Consumer choice

The consumer surplus is the difference between the total value the consumer derives from consuming a product of a given brand and quality and the price paid for it. Thus, the consumer surplus from purchasing the national brand and store brand, respectively, is:

$$\begin{aligned} CS_n &= \nu + \alpha Q + \beta B - P, \text{ and} \\ CS_p &= \nu + \alpha q - p. \end{aligned} \quad (1A)$$

Consumers choose the brand that gives them the highest surplus. That is, they choose the national brand if $CS_n > CS_p$ or equivalently if:

$$\beta \geq \frac{P - p - \alpha(Q - q)}{B} = \tilde{\beta}(P, p).$$

Consequently, the proportion of customers who select the store brand is $F(\tilde{\beta})$, and the market share of the branded product is $[1 - F(\tilde{\beta})]$.

Price-quality relationship in a competitive equilibrium

Each firm simultaneously sets price in a Bertrand-Nash competition to maximize profit. Since quality and brand name are predetermined, the costs of production and branding are sunk; hence we set it equal to zero. Consequently, profit is given by price multiplied by market share. The profit function of the national brand firm is:

$$\Pi(P) = P \cdot [1 - F(\tilde{\beta}(P, p))], \quad (2A)$$

and the profit function of the store brand firm is:

$$\pi(p) = p \cdot F(\tilde{\beta}(P, p)). \quad (3A)$$

Maximizing the profit function in equation (2A) with respect to P for a given p , and the profit function in equation (3A) with respect to p for a given P , we get the first order conditions for both firms. Solving these equations simultaneously, we get the equilibrium prices (indicated by an asterisk), P^* and p^* , as functions of exogenous variables B , Q , and q . To obtain closed-form solutions, we assume that β follows a uniform distribution on the interval $[0, d]$. Then, the resulting equilibrium prices are:

$$P^* = \frac{2d}{3}B + \frac{\alpha}{3}(Q - q), \quad (4A)$$

$$p^* = \frac{d}{3}B - \frac{\alpha}{3}(Q - q). \quad (5A)$$

From equations (4A) and (5A), we obtain equation (6A) that gives the price difference between the national brand and the store brand as a function of brand recognition and quality differences between national and store brands:

$$P^* - p^* = \frac{d}{3}B + \frac{2\alpha}{3}(Q - q). \quad (6A)$$

For estimating the impact of quality differences on price premiums across product categories, we adapt equation (6A) to obtain equation (1) in the text. ■

This summary has been provided to allow managers and executives a rapid appreciation of the content of this article. Those with a particular interest in the topic covered may then read the article in toto to take advantage of the more comprehensive description of the research undertaken and its results to get the full benefit of the material present

Executive summary and implications for managers and executives

Price – a pretty dodgy guide to quality!

As marketers we take for granted the fact that a successfully promoted “national” brand enjoys a price premium over own label or store brands. It is why we set such store by the concept of branding and it justifies the extravagance of advertising. In its essence a brand means that the consumer is buying something other than the product – the intangible “benefits” that the brand contains.

Because of this situation – where price premium is unwarranted in terms of quality – many observers have argued that the age of the brand must end as consumers become more sophisticated and better informed. Why but Brand X when I can buy essentially the same product at 30 percent less cost?

Apelbaum et al. investigate the relationship between expert quality evaluations (as reported in Consumer Reports) and price. The authors’ focus is on the differential in price premium between national and store brands. The central finding is that national brands enjoy a price premium over store brands and that this premium remains even when expert assessments of quality reveal store brands to be superior.

What I say three times is true

The essence of advertising lies in the repetition of a message – we believe a given brand to be superior because its advertising reminds of this fact repeatedly. “Objective” assessment by experts may undermine this situation but the perception still remains. The story of “new” Coke reminds us of this fact. Despite outperforming Pepsi and “classic” Coca-Cola in taste tests, “new” Coke proved a flop. “Objective” assessment was not enough to break the hold of the existing brand premium.

Apelbaum et al. remind us that being good is not sufficient to break down established brand attachments especially when the established brands persist with their advertising efforts. Indeed the authors note that one situation where store brands succeed is when brand advertising is less intensive. When brand owners stop or slow down the promotion of their brand through advertising the results are almost always negative. This reduction in positive perception makes it more difficult to retain the price premium.

Put simply, the brand owner has to persist with advertising in order to retain the premium and the premium allows the brand owner to afford such persistence (most of the time). Crucially, the advertising matters more than maintaining a real quality advantage since, as Apelbaum et al. describe:

... national brands command a significant price premium even when they have a lower average quality than store brands.

But quality does matter, doesn’t it?

The second of Apelbaum et al.’s significant findings is that price premium of a national brand “increases with its quality difference”. Indeed, the authors’ study suggests that the average price premium where the national brand is of superior quality is nearly double (50.4 percent compared to 28.7 percent) the premium when the product is assessed as inferior. Advertising may be more important to maintaining the brand’s position but quality really does matter.

Indeed, the impact of superior quality on profits will far exceed the differential described. If the brand makes \$1 gross margin at a 25 percent

price premium and 90 percent of this covers distribution and advertising, at 50 percent price premium the contribution to profits increases from 10 cents to \$1.10. This assumes that increases in quality are cost neutral (which they probably are not) but it does demonstrate the conflict between investing in product quality and investing in brand equity.

Investing in quality makes sense for the national brand (and by contrast less sense for the store brand) since the national brand will always (*ceteris paribus*) be sold at a higher price than the store brand. Store brands grew on the back of price-conscious consumers who by definition are less concerned about quality than the average. This situation calls into question the strategies described by Apfelbaum et al. where retailers invest in the quality of the store brand. The argument is that this investment reduces the premium gap thereby increasing store brand margins and profits. The risk is that this strategy leaves open the opportunity for others to target the value-conscious consumer undermining the justification for the store brand.

However, the evidence suggests that better quality store brands are more successful. This suggests that retailers need to strike a different balance in their market strategies to the national brand. The focus should be on cost-neutral or low cost improvements in quality alongside persistent promotion of the price advantage. It probably remains the case that the price advantage for store brands is their main selling point but improved quality allows for the targeting of those consumers who buy national brands because of their perception that such brands are of superior quality.

Brands are not dying but they have to work a lot harder to succeed

The contention that sophisticated consumers and increased amounts of "objective" product information will destroy brands seems to be unsupportable. However, national brands are challenged by commodity brands and store brands making it more difficult to rely on superior advertising (and bigger spend) and comprehensive distribution.

In the end brands will have to "justify" their premium and the only way to do this is to achieve and sustain an advantage in terms of both actual and perceived quality. The ad spend must be maintained (or else the brand will die) but there is also a need to match perceptions of quality with reality – and this requires sustained investment in the quality of the product.

(A précis of the article "The effects of expert quality evaluations versus brand name on price premiums". Supplied by Marketing Consultants for Emerald.)