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AMBIT
ASSET MANAGEMENT

MONTHLY NEWSLETTER

NOVEMBER 2021

BRANDING
MAKING IT BIG

Dear Patron,

Gold Spot, Zandu, Krack Cream, Uncle Chips are some of the brands that most of you would have heard of. These were quite famous and still hold a place in consumer's mind. But over the years, these and many other well-known brands like them, either disappeared or failed to scale up beyond a certain threshold.

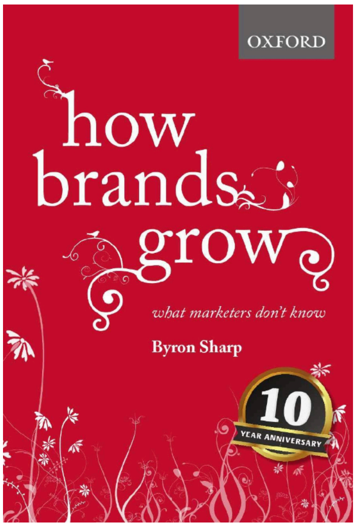
India is a unique, heterogeneous market where starting and building a brand / franchise initially may not be a big challenge, but scaling it up is not that easy. This is because creating a successful consumer-centric business is a combination of three things – (1) Distribution (2) Scale, and (3) Branding. However, in the advent of e-commerce, the industry landscape is changing and these barriers are diminishing. As a result, franchises today are able to scale-up faster compared to a decade back, provided they **Innovate, Brand and Position** their franchise effectively.

Therefore, in this month's newsletter, we thought of writing on branding. We wanted to highlight a few key learning from an interesting albeit less known book - How Brands Grow authored by Byron Sharp.

HOW BRANDS GROW – BY BYRON SHARP

The book is a manifesto on evidence-based marketing, giving real life examples and anecdotes on what works in real life rather than theoretical concepts. The Book also breaks lot of myths which are often regarded as conventional wisdom.

Exhibit 1: How Brands Grow: What marketers don't know by Byron Sharp



Source: Cover copy. How Brands Grow, by Byron Sharp, Oxford University Press Australia & New Zealand

Seven Rules for Brand Growth

The Book also outlines 7 scientifically derived rules for brand growth that can be very useful –

1. **Reach**: Continuously reach all customers via effective communication and distribution
2. **Be Easy to Buy**: Communicate how the brand fits with the users and look out for emerging 'reasons not to buy'
3. **Get noticed:** Grabbing Consumer attention and focusing on brand salience
4. **Refresh and build memory structures:** Understand existing memory structure of the consumer that make the brand easy to notice and subsequently buy
5. **Create and use distinctive brand assets:** Using sensory cues to get noticed easily
6. **Be consistent, yet fresh:** Avoid unnecessary changes. A large part of the art of advertising is telling the same story but in an innovative, new and entertaining way
7. **Stay competitive:** Don't give consumers a reason not to buy!

Key points from the book that we found most interesting

1. Expanding Reach v/s Building Loyalty:

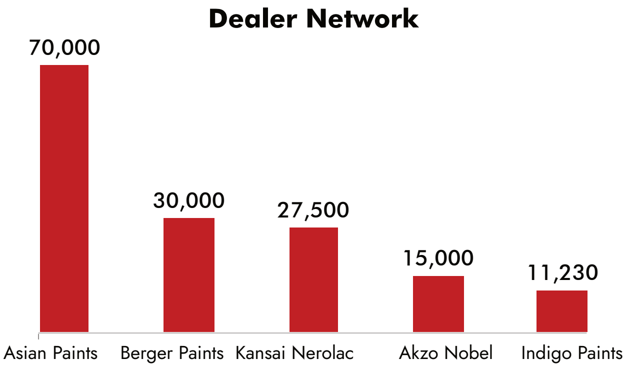
Sales volume of a particular product depends upon two main variables: **(a)Reach** – number of buyers targeted; and, **(b)Loyalty** – The frequency of purchase

- According to the author, the key difference between large and small brands is the focus on Reach rather than Loyalty. While larger brands have slightly higher Loyalty than smaller brands, they enjoy much higher penetration.
- The author argues that customer loyalty is largely a myth since consumer purchases are driven more by **Habit** rather than **Commitment**. For eg: 72% of Coke drinkers in the UK also bought Pepsi.

Studies have shown that loyalty is directly related to lack of opportunity. Light buyers have less opportunity to be disloyal. Also, customers shopping from stores with fewer brands (typically in rural areas) automatically have fewer choices / options and so they may appear more loyal.

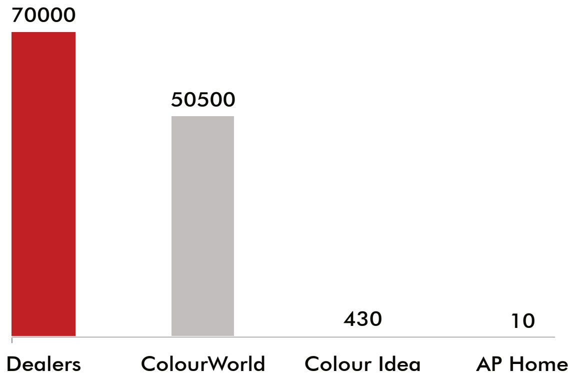
Therefore, it makes more sense for brands to invest in finding innovative ways to reach customers than creating loyalty programs. Brands should try to place their products in front of as many eyes as possible. We highlight an example of Asian Paints (APNT) – one of our portfolio companies – that has been able to execute this strategy over the years (Refer to Exhibit: 2,3).

Exhibit 2: Asian Paints dealer network is 2x its nearest competitor and has 46% of dealer share of top-5 players



Source: Ambit Asset Management, Indigo Paints DRHP

Exhibit 3: APNT offers its products across multiple store formats, thus further expanding reach



Source: Ambit Capital Research, Company

2. Marketing focus on 'light' buyers rather than 'heavy' buyers:

The typical thought process of companies is to segment the market and focus on 'heavy buyers' and as a result, they try to target marketing efforts towards that user segment.

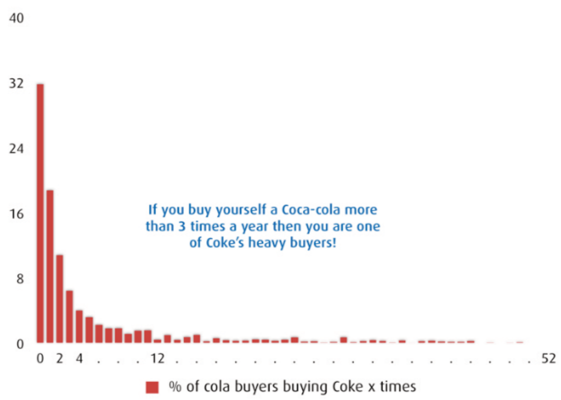
The Author highlights that for a specific product / brand, 20% of heaviest buyers contribute 50% of sales and 50% of light and middle buyers as they account for 50% of sales. Therefore, companies cannot grow if they ignore these light and middle buyers as they account for 50% of sales. Moreover, focus on 'heavy buyers' may not be that useful as they are already consuming at or near their full potential.

Mass marketing, which feels like a thing of the past, actually helps in recruiting light buyers, who become heavy overtime. Brands that have been able to make it BIG have a universal appeal, and mass marketing with a reach-optimised single simple message, works the best.

Recruiter Packs – Premiumization, affordability and flexibility: An interesting Case Study in Mass Marketing.

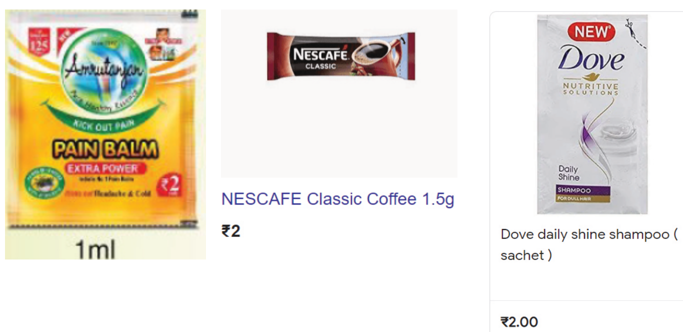
Indian FMCG companies have used 'Recruiter Packs' – small 2ml/5ml sachets/bottles often costing <Rs10 to reach out to 'light buyers'. This strategy has worked well especially in rural areas where consumers have aspirations but are not deep-pocketed. These recruiter packs serve two purposes for companies – (1) Provide a cost effective product demo and expand Reach **(Ref to Point 1: Reach v/s Loyalty)** by recruiting new 'light buyers' without worrying about repeat purchases (2) Provide a good nudge for transitioning from 'unbranded' to 'branded' categories, as seen in case of Cigarettes where smaller 64mm packs aided this shift.

Exhibit 4: A Coke buyer on average purchases 12 times annually But very few customers buy 12 or more bottles. This is due to high contribution from 'light' customers



Source: Ambit Asset Management, Kantar World Panel, UK 2005

Exhibit 5: Some examples of Recruiter Packs by FMCG companies which cost Rs.2



Source: Ambit Asset Management, Google, FY21 Annual Report

3. Our customer v/s your customer – How significant is Brand Loyalty?

Brands believe that they appeal to a particular type of customer in terms of demographics, psychographics, attitudes, and media habits. However, research shows that there is very little difference in the type of customer among competing brands in a similar category. For Eg, Mercedes sells to the same customers as BMW or Audi does. Also, variations across brands are usually quite obvious, especially for luxury brands that generally cater to more wealthy customers. This opens up growth opportunities as companies have a larger set of potential customers and can also attract 'loyal' customers of other brands.

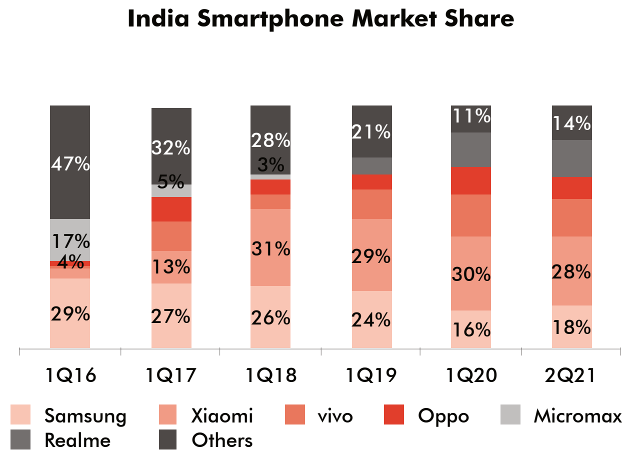
This counters Kotler's idea that individual brands sell to distinctly different segments of buyers. According to the Author, segmentation studies exaggerate small differences and assumes that brands with different features would sell to very different people.

Busting the Brand Loyalty myth

- Think about it – If brand loyalty was strong among consumers then what was the need for CONSISTENT product innovation? Apple, for eg, – which has the highest brand loyalty globally – spends $18.8bn or Rs1.4 Lac Cr on R&D. This is equivalent to 7% of its 2020 Sales and entire Market Cap of Tech Mahindra.
- Another example is the entry of Pantanjali toothpaste which disrupted the market share of established players like Colgate

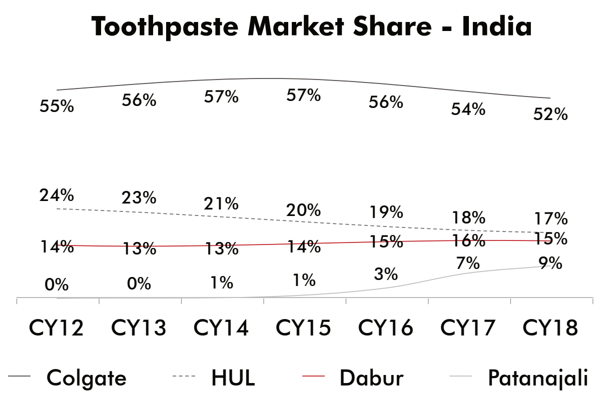
As e-commerce gains more traction, especially post-COVID, physical distribution will no longer be a barrier – both for consumers and brands. Today, one can easily get a good quality Red Tape shoe in the hinterlands of UP/MP. Therefore, smaller brands that are not that prominent today will be able to gain much better traction going ahead, while incumbents can easily lose their Brand 'loyalty'. Hence constant innovation will be much more essential to maintain the Right-To-Win.

Exhibit 6: Samsung lost its leadership and market share to Chinese manufacturers that offered better value proposition



Source: Ambit Asset Management, counterpointresearch.com

Exhibit 7: Colgate & HUL – leading Toothpaste brands in India – saw their market share decline post Patanjali's entry



Source: Ambit Asset Management

4. Creating unique features v/s distinctive brand identity/positioning

Most of the marketing strategies are centred on creating a meaningful differentiation (uniqueness) in the consumer's mind. However, the author argues that most brands (of similar product category) have very little differentiation in terms of the product itself. According to the author, buyers of the brand don't often think that their brand is different or unique. While it may sound surprising, but choosing a brand is a trivial task for customers. They usually don't spend a lot of time comparing brands in a category.

The core purpose of branding is to easily identify the source of the product or service. Therefore, rather than creating unique product differentiations, brand managers should strive to create distinctive brand recall through colors, logos, taglines, characters and celebrities. These distinct assets are used on packaging, advertisements, in-store displays to build and reinforce consumer memory structures. Distinctiveness makes it easy for customers to notice, recognize and buy the product. Also, to build these distinct assets, brand should consistently communicate to consumers across media.

Some examples in Indian Consumer industry context where the advertising or branding of the product was not around any unique characteristics of the product but rather distinct emotional connect that was created:

- Surf – "Daag acche hai" tagline encouraging kids to play outdoor full-heartedly
- Sundrop Oil – 'Maa ke Haath ke Jalebi' is what clicked with consumers rather than any cooking oil characteristics
- Relaxo – Salman Khan walking the ramp with Relaxo chappal in its commercial. Again, no mention of any special product feature.
- Ariel #ShareTheLoad – "Why is Laundry only a Mother's Job" –linking this deep social message with the Brand Ariel.

Conclusion

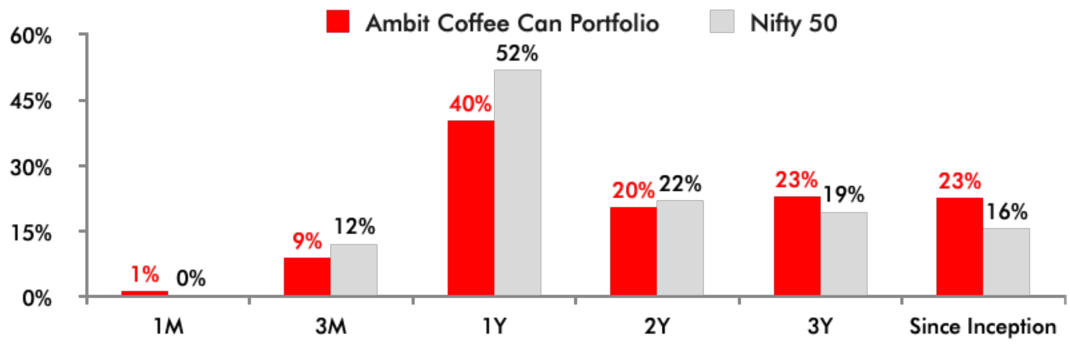
Till now, creating a large consumer centric franchise in India, beyond a certain threshold, say Rs100Cr sales, was not that easy. While creating Brand awareness may not have been a challenge, expanding Distribution and successful Scale-up, especially in a geographically diverse country like India, was difficult.

But in the advent of Digital commerce, especially post COVID, these entry barriers are disappearing. Everything from Manufacturing to Supply Chain and Logistics can now be outsourced, thus making it easier for newer brands to scale-up. As a result, proper product Branding and positioning is of utmost importance for both new players, as well as incumbents. **Focusing on (1) Customer Reach (2) Mass Marketing Strategy (3) Brand Innovation (4) Creating a Distinct Brand image, are some key points for newer and existing brands to focus on.**

AMBIT COFFEE CAN PORTFOLIO

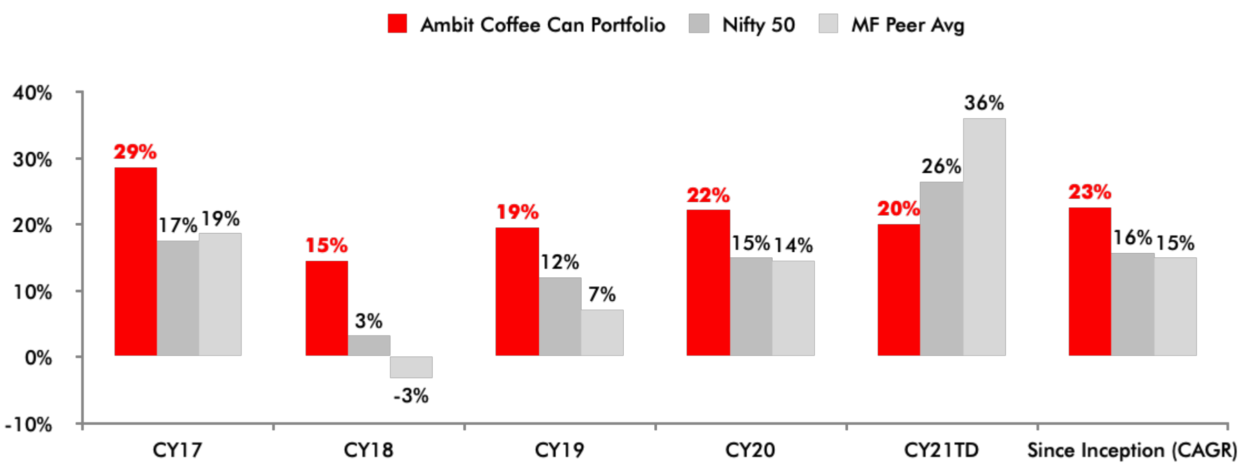
At Coffee Can Portfolio, we do not attempt to time commodity/investment cycles or political outcomes and prefer resilient franchises in the retail & consumption oriented sectors. The Coffee Can philosophy has unwavering commitment to companies that have consistently sustained their competitive advantages in core businesses despite being faced by disruptions at regular intervals. As the industry evolves or is faced by disruptions, these competitive advantages enable such companies to grow their market shares and deliver long-term earnings growth.

Exhibit 8: Ambit Coffee Can Portfolio point-to-point performance



Source: Ambit; Portfolio inception date is March 6, 2017; Returns as of 31st Oct, 2021; All returns are post fees and expenses; Returns above 1 year are annualized; Note: Returns prior to Apr'19 are returns of all the Pool accounts excluding non-aligned portfolio, and returns post Apr'19 is based on TWRR returns of all the pool accounts.

Exhibit 9: Ambit Coffee Can Portfolio calendar year performance



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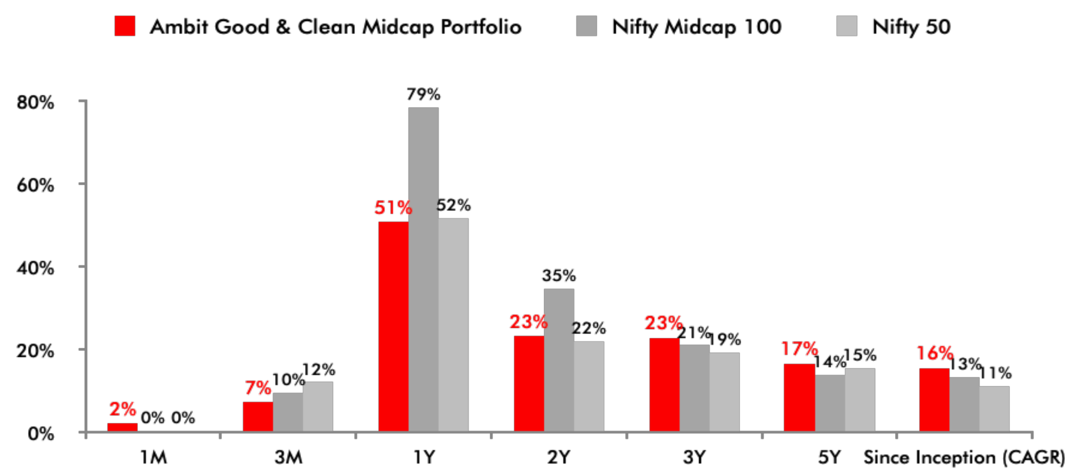
AMBIT GOOD & CLEAN MIDCAP PORTFOLIO

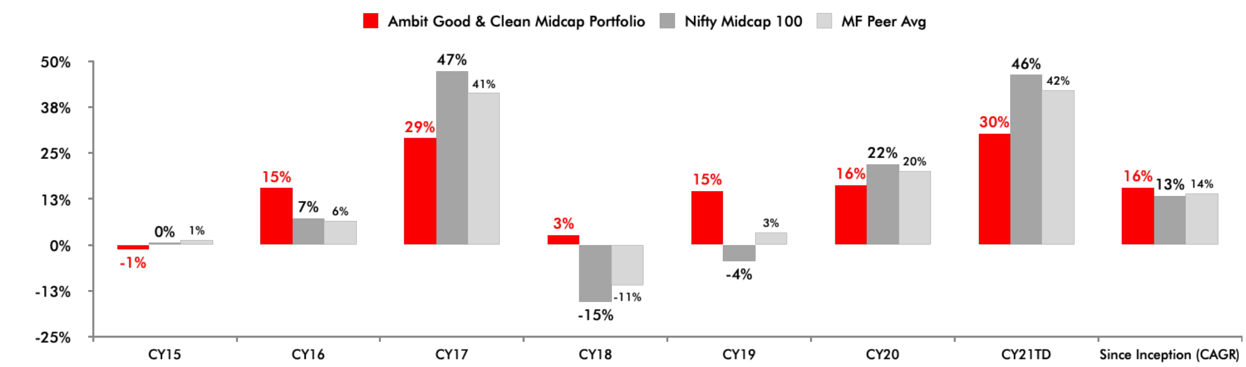
Ambit's Good & Clean strategy provides long-only equity exposure to Indian businesses that have an impeccable track record of clean accounting, good governance, and efficient capital allocation. Ambit's proprietary 'forensic accounting' framework helps weed out firms with poor quality accounts, while our proprietary 'greatness' framework helps identify efficient capital allocators with a holistic approach for consistent growth. Our focus has been to deliver superior risk-adjusted returns with as much focus on lower portfolio drawdown as on return generation. Some salient features of the Good & Clean strategy are as follows: Process-oriented approach to investing: Typically starting at the largest 500 Indian companies, Ambit's proprietary frameworks for assessing accounting quality and efficacy of capital allocation help

Exhibit 10: Ambit Good & Clean Midcap Portfolio point-to-point performance



Source: Ambit; Portfolio inception date is March 12, 2015; Returns as of 31st Oct, 2021, All returns above 1 year are annualized. Returns are net of all fees and expenses

Exhibit 11: Ambit Good & Clean Midcap Portfolio calendar year performance

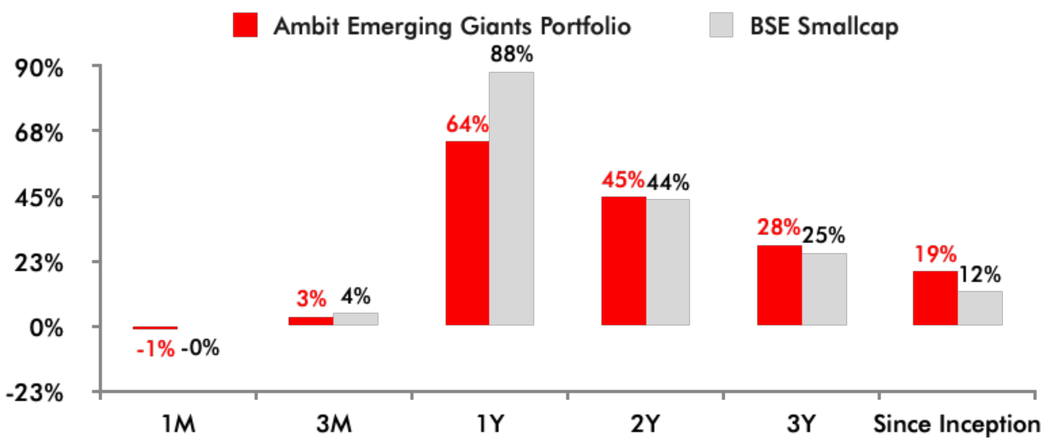


Source: Ambit; Portfolio inception date is March 12, 2015; Returns as of 31st Oct, 2021. Returns are net of all fees and expenses

AMBIT EMERGING GIANTS

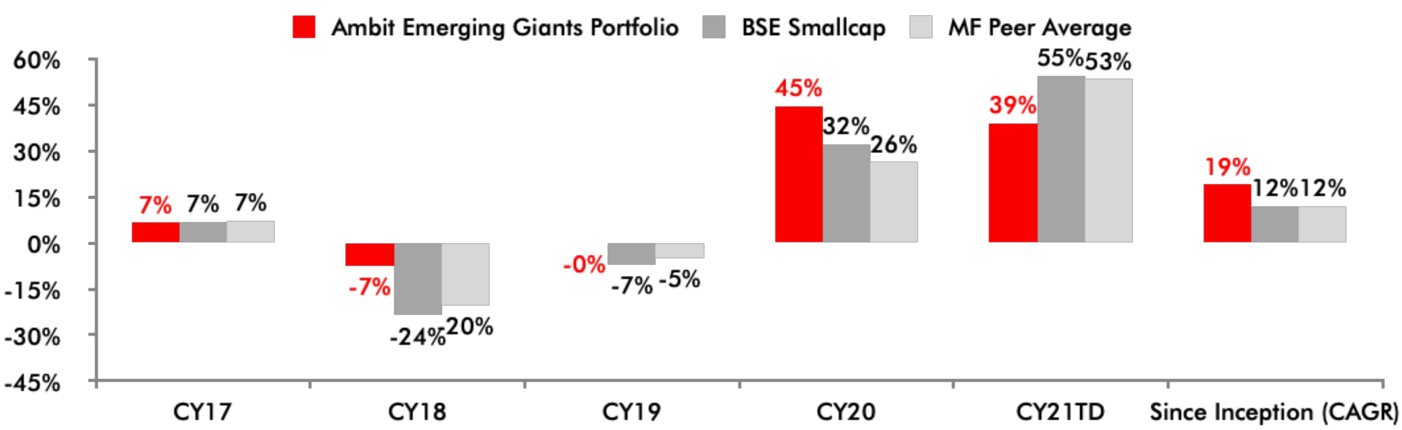
Smallcaps with secular growth, superior return ratios and no leverage Ambit's Emerging Giants portfolio aims to invest in small-cap companies with market-dominating franchises and a track record of clean accounting, governance and capital allocation. The fund typically invests in companies with market caps less than Rs. 4,000cr. These companies have excellent financial track records, superior underlying fundamentals (high RoCE, low debt) and ability to deliver healthy earnings growth over long periods of time. However, given their smaller sizes these companies are not well discovered, owing to lower

Exhibit 12: Ambit Emerging Giants Portfolio point-to-point performance



Source: Ambit; Portfolio inception date is December 1, 2017; Returns as of 31st Oct, 2021; All returns above 1 year are annualized. Returns are net of all fees and expenses

Exhibit 13: Ambit Emerging Giants Portfolio calendar year performance



Source: Ambit; Portfolio inception date is December 1, 2017; Returns as of 31st Oct, 2021. Returns are net of all fees and expenses

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