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GOING PUBLIC AND UNDERPRICING AS BRAND VALUE ENHANCING TOOLS

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ABSTRACT

After the year 2000, a new trend in corporate finance-related research has been investigating the relationship between Initial public offerings "IPOs" variables from one side and brand value on the other in order to come up with new explanations for the extreme underpricing levels for technological companies. Studies, in particular, connect underpricing as the main IPO variable to product enhancement measures such as brand value. Some studies find evidence that the level of underpricing is positively related to long-term product market strength. This review paper comes to integrate the financial theme of going public and the business theme of brand value. We provide a comprehensive review for the recent seminal work in going public and underpricing, and their relationship to brand value creation in order to draw policy implications for decision-makers.

Keywords: IPOs, Underpricing, Initial return, Marketing, Brand value, Brand creation, Private equity.

Topic Areas: Organizations and financing, Business marketing, Brands.

JEL Classification: G24, M370.

Contribution/ Originality

This study contributes in the existing literature by providing a comprehensive and comparative review of the seminal research work related to one of the least tackled explanations for going public and underpricing in which IPOs attributes are related to brand value creation.

1. GOING PUBLIC

1.1. Introduction

According to Ritter (1998) even the simple question why do companies go public has various answers, and could be an opportunity for research and debate, one of the most dominant answers is the desire to raise equity capital for the firm and to create a public market in which the founders

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and other shareholders can convert some of their wealth into cash at a future date. Another reason is nonfinancial considerations, such as increased publicity, this explanation played only a minor role for most firms in the past, but after the internet bubble it has become hot again. Others argue that liquidity considerations are more important for the issuer than the raised capital itself that have an influence on the cost of capital of the issuer, many researchers considered different motivations for going public. This still leaves the question of why initial public offerings "IPOs" are the best way for entrepreneurs to raise capital, and why the motivation to do an IPO is stronger in some situations or times than in others.

Due to the importance of going public for market agents and researchers, and due to the increasing impact of building strong brands from firms' perspective; this study comes with a principle objective to investigate the relationship between IPO variables, especially underpricing, on one hand and brand value measure on the other to assess whether going public enhances brand value, and try to extract policy suggestions for decision-makers?.

In this study, we review the related literature of the old-new explanation for going public and underpricing which states going public and underpricing create firm's publicity, which, in essence, enhance the firm's position in the product market. This premise was tested by many scholars from different perspectives; Habib and Ljungqvist (2001) argue that underpricing is a substitute for costly marketing expenditures, this result is further supported by the findings of Harasheh and Gatti (2014); DuCharme *et al.* (2001); Demers and Lowellen (2003); Krigman *et al.* (1999); Rajgopal *et al.* (2000) and Stoughton *et al.* (2001) who have started to investigate other explanations for underpricing after the internet bubble late 1990s. In general, with various methodologies used, they find evidence that underpricing is positively related to brand value post-IPO.

Regarding the consideration of raising capital; companies sell their shares mainly for two motives from a financial point, one: is selling existing shares of founders (existing investors) to liquidate their positions as a cash-out strategy, this means proceeds to the pockets of existing founders, this is also referred to "*secondary shares offer*". The other is selling new shares to the public (new investors) while keeping certain percentage with the early investors or founders, this means proceeds for the company, either for investments (working capital or capital investments) or debt reduction, this is also called, "*primary shares offer*".

Market players in the IPOs are mainly three, the issuer who wishes to sell shares to the public, the investment banker that stays in the middle between the issuer and investors, and the last player is the investor who can additionally be classified as informed and uninformed investor.

Moreover, during the sale of the stock in the IPO, there occurs a common frequent financial phenomenon called, "underpricing or initial return", which means that the stock goes above the offer price in the first day of trading in the secondary market.

In this paper, section two reviews underpricing and its theories, section three sheds the light on the relationship between IPOs and brand value creation, section four concerns brands in the scope of finance, and finally, section five is devoted for conclusions and policy implications.

1.2. Theories of Going Public

Theories of going public are well-established in the literature. finance scholars propose and test various hypotheses, however, two theories took the major attention of research, they are life cycle theories, and market-timing theories.

In life cycle theories, Zingales (1995) by his empirical testing states that going public is a decision taken by entrepreneurs to get more value when the company is a target for acquisition, he observed that it is much easier for a potential acquirer to spot a potential takeover target when it is public. Moreover, entrepreneurs realize that acquirers can pressure targets on pricing concessions more than they can pressure outside investors. By going public, entrepreneurs thus help facilitate the acquisition of their company for a higher value than what they would get from an outright sale. Schultz and Zaman (2001) report that many internet firms that went public in the late 1990s pursued an aggressive acquisition strategy, which they interpret as an attempt to pre-empt competitors. On the other hand, Black and Ronald (1998) show opposite results, they point out that entrepreneurs often capture control from the venture capitalists at the IPO. Thus, many IPOs are considered entry point rather than exits for the entrepreneur as they are for the venture capitalists.

Market-timing theories: Asymmetric information is one of the well-known models explaining going public, Lucas and Robert (1990) worked on this model, and they find that firms postpone their equity issue if they know they are currently undervalued, given the bear marketplaces too low value of firm, hence, entrepreneurs delay their IPOs until a bull market offers more favorable pricing. Supporting the above findings, Choe *et al.* (1993) prove that firms avoid issuing in periods where few other good-quality firms issue. Other theories have argued that markets provide valuable information to entrepreneurs ("information spillovers"), who respond to increased growth opportunities signaled by higher prices, Subramanyan and Titman (1999) and Schultz (2000).

2. UNDERPRICING

2.1. Introduction

The best-known pattern associated with the process of going public is the regular occurrence of large initial returns or underpricing. From an academic point of view, Underpricing: is defined as the difference between the aftermarket price (first-day closing price) and the offer price at the IPO. Underpricing can also be the dollar magnitude by multiplying the above difference by the total number of shares offered (total amount of money left on table), additionally, can be the percentage of the offer price by dividing the difference by the offer price, Logue (1973) and Ibbotson and Jeffrey (1975). Large initial return is commonly perceived as a contradiction to capital market efficiency. However, it is a common phenomenon that has been documented almost in all countries around the world that have stock offerings, Loughran *et al.* (1994). Since the 1960s, this 'underpricing discount' has averaged around 19% in the United States, suggesting that firms leave considerable amounts of money on table. Underpricing has been fluctuating a great deal, averaging 21% in the 1960s, 12% in the 1970s, 16% in the 1980s, and 21% in the 1990s; however, some IPOs have seen first price jumps of 200 to 400 percent during the internet bubble, but the trend started to smooth thereafter.

Researchers and practitioners claim that underpricing is the major opportunity lost by the issuer when going public and money left on the table for other investors. In finance literature, underpricing is also called initial return (IR), which is the percentage of return gained by investors in the first day trading, and most of the time both terms are used interchangeably, but some scholars differentiate between them, Purnanandam and Bhaskaran (2004) show that the average offer price at the IPO is overvalued relative to firms fundamentals, average industry peers, and the three-year long-term performance, therefore, there are various perceptions what underpricing is, but here and after we will try to follow the trend and use underpricing and IR interchangeably.

More importantly and in a remarkable trend in the last decade, the average number of IPOs has declined to 99 IPOs per year since 2000, compared to 310 per year for the period 1980-2000 as documented by Gao *et al.* (2013) this decline in IPO volume is noticed mainly in small firms. Many policymakers, investors, and academics have blamed the Sarbanes-Oxley Act of 2002 and the Global Settlement's effect on analysis coverage for this decline. Researchers have started to investigate the *regulation overreach* hypothesis which claims that small firms stay private due to the increase in the regulatory costs borne by publicly traded companies, and the *market conditions* hypothesis which states that the decline in the IPOs is due to the poor stock market conditions that underestimate the values of IPO firms. But lately some researchers like Gao *et al.* (2013) & Ritter *et al.* (2013) propose and have been investigating another explanation for the decline in IPOs activity after 2000, it is the *economies of scope* hypothesis which states that small firms prefer being under a big umbrella (big company) to be big fast and get more marketability rather than staying independent, which results in small firms being acquired. While Gao *et al.* (2013) study the IPO decline in the US market, Ritter *et al.* (2013) investigate the economies of scope in the major European equity markets. Both studies document numerous facts that are consistent with economies of scope hypothesis and inconsistent with regulatory outreach hypothesis as an explanation for the prolonged drop in IPO activity.

Underpricing as a remarkable ongoing phenomenon inspired a large theoretical literature in the 1980s and 1990s trying to rationalize why IPOs are underpriced. The resulting theoretical models in turn have been confronted with the data over the past thirty years.

2.2. Theories of Underpricing

Theories of underpricing can be grouped under four broad categories: asymmetric information, institutional reasons, control considerations, and behavioral approaches. These model are well-documented and explained in literature as in Ljungqvist (2007); Ritter and Welch (2002) and Agrawal (2008) therefore, we will only discuss them in brief.

Information asymmetry models are the most developed among other explanations, they are based on the premise that one player in the market knows more information about the IPO company than others. The players are the issuing company, the underwater, and the investors bidding the stock. Four explanations are included in this group, winner's curse, information revelation, principle-agent, and quality signaling.

Institutional Explanations focus on the institutional setup and the legal framework for the issuer, investment banker, and some related institutions. The institutional explanation includes potential liability avoidance, price stabilization by the underwriter, and some tax incentives.

Ownership and control theories: Going public is, in many cases, a step towards the eventual separation of ownership and control. Ownership matters for the effects it can have on management's incentives to make optimal operating and investment decisions. In particular, where the separation of ownership and control is incomplete, an agency problem between non-managing and managing shareholders can arise, Jensen and Meckling (1976) rather than maximizing expected shareholder value, managers may maximize the expected private utility of their control benefits at the expense of outside shareholders. This group includes retention of control, reducing agency cost, and ownership dispersion hypothesis.

Behavioral explanations: In the late 1990s, initial returns increased substantially. (As indicated in Ritter and Welch (2002)) U.S. issuers left an aggregate of $62 billion on the table in 1999 and 2000 alone. Many researchers are doubtful whether informational frictions, the risk of lawsuits, or control considerations could possibly be severe enough to warrant underpricing on this scale. As a consequence, some argue we should turn to behavioral explanations for IPO underpricing. Behavioral theories assume either the presence of 'irrational' investors who bid up the price of IPO shares beyond true value or that issuers are subject to behavioral biases and, therefore, fail to put pressure on the underwriting banks to have underpricing reduced. Behavioral explanations include cascade "bandwagon" effect, investor's sentiment, and prospect theory and mental accounting.

3. BRANDS IN THE SCOPE OF IPOS

After the extreme levels of underpricing during the internet bubble late 1990s, researchers have started to look for other explanations for why do companies go public? and especially why they leave large amounts of money on the table in terms of initial return on the first day of trading in the secondary market?.

The access to finance and financial markets as the traditional explanation for why do companies go public struggles in explaining the precise nature of the timing of public offerings as issuers have large amounts of cash prior going public. Moreover, the prospectus is usually uninformative about the use of proceeds issue; firms mainly mention that the proceeds will be used for general corporate purposes. Pagano *et al.* (1998) studied the motives for going public on the Italian case; they find that the need to finance investments has little power in explaining the motive of going public.

Initial public offerings have occupied a large space in the finance literature. But the interaction between the IPO decision and the product market has been neglected. Existing IPO research can fall in one of the three main categories (summary of early discussed theories).

First, a group of work that analyzes IPOs assuming the need to go public is given. This work derives the equilibrium price and equity issuance decisions given different kinds of informational asymmetries.

The second category of work endogenizes the decision of whether to go public. Generally private equity issue is considered the alternative for IPO and the reason why firms choose IPO rather than the private issue is because of capital market frictions. The IPO may minimize the transaction costs while financing a project but has no direct influence on firm fundamentals.

The third category of research endogenously explains the IPOs by their potential direct effect on firm fundamentals. An IPO may result in optimal monitoring by shareholders or may allow improved incentive contracts between the firm and the manager.

Moreover, scholars started to investigate another frequent explanation for the decision of going public, specifically, the enhancement company's image and publicity. Some executives mentioned this goal clearly in their missions. Edward McVaney, Chief Operating Officer at J.D. Edwards commented in 1997 that the IPO has led more corporate customers to start thinking of this company as a valid ERP (Enterprise Recourse Planning) competitor. The privately held company gets no respect as he claimed, Brown (1997).

Perhaps the basic notion of this discussion comes from Habib and Ljungqvist (2001) who find the evidence to support the above argument in which marketing expenses and underpricing are substitute costs. They say, "every 1$ of promotion costs, seeks to reduce the promoters' wealth losses by 98%, so the marginal costs of promotion equal the marginal benefits." Furthermore, Frieder and Subrahmanyam (2005) find in their study that investors retain highly visible firms, where visibility is an outcome of investments in the marketing of IPO. Another study by Cook *et al.* (2006) suggests that investment bankers invest in marketing to promote IPO amongst the retail investors for the issuers to retain and attract clients. Additionally, some studies have found evidence that in the case of insufficient pre-offer publicity by the investment banker, issuers change investment bankers.

Accordingly, Fleischer (2006) conclude that the concept of branding rarely appears in academic research in corporate finance and corporate governance. Finance scholars focus their attention on the relationship between the firm and its investors and creditors who supply financial capital, and its managers who supply human capital. IPO contracts are efficient when they properly align incentives; a good contract design is one that allows managers to raise capital cheaply and deploy it effectively. Consumers enter the discussion only as the emotionless buyers who make up the product markets, which serve as a potential indirect check against agency costs. Additionally, from a traditional corporate finance perspective, the goal of a properly-structured IPO is to manage the information asymmetry between the issuer and potential buyers in order to raise the most amount of money possible per share of stock sold. From this perspective, the success of the Google's deal is questionable. Few would call the deal elegant or efficient. But this is not really what the Google's IPO structure was about, or at least it is not the full story. When Google structured its IPO as an auction, it reinforced Google's identity as an innovative, egalitarian, playful, and trustworthy company.

In a related work, some finance scholars studied the link between advertising expenses and intangible assets from one side and stock return for publicly traded companies on the other side. Thus, investigating the properties of different types of intangible capital is useful to better understand the impact of intangible capital on asset prices. For example, both the firm's stock of human capital, skills and brand name contribute to the firm's total stock of intangible capital, but these two assets are likely to have different risk properties. Human capital skills are partially embodied in the firm's labor force. Because this stock of human capital is not fully owned by the firm, shareholders are exposed to the risk that a worker may leave a firm, and hence decrease the firm's stock of human capital skills. In contrast, a firm's brand name is firm-specific because the firm fully owns the property rights to its brands. In this manner study the implications of customer capital for firm value and investment dynamics. They emphasize the importance of adjustment costs in creating customer capital. Brand capital and customer capital are related because both measures capture the effect of customer loyalty on firms' performance.

Belo *et al.* (2013) investigate the impact of brand capital on asset returns through structural estimation. They consider a fully specified economy in which prices and quantities are endogenously determined. Through calibration and simulation, their focus is thus on the understanding the economic determinants of the endogenous risk premiums associated with the brand capital stock.

Moreover, Previous studies document empirical links not only between advertising expenditures and stock returns, but also between advertising expenditures and seasoned equity offerings (SEO). For example, Chemmanur and Yan (2009); Lou (2011) and Belo *et al.* (2013) document that the advertising expenditures by firms are unusually large during SEO's years. Similarly, stock returns tend to be unusually high during SEO's years, but unusually low in the following year.

The motivation for examining the link between advertising, stock returns, and SEOs follows Merton (1987) who shows that when investors only invest in securities that they know about, firm value is increasing in the degree of investor recognition of the firm.

More importantly, empirical evidence on product market implications of going public has been the subject to several studies, Slovin *et al.* (1995) document an average negative announcement effect on the rival firms. They find that rivals' stock price reaction for conventional IPOs is statistically negative. By contrast, Ward (1997) finds that the average effect of IPO announcements on rival firms depends on the motive stated in the prospectus.

The product market explanation can also be extended internationally by explaining foreign shares listing, Pagano *et al.* (2001) find that the propensity of firms to cross-list their shares on foreign markets increases with the percentage of export sales.

Almost all studies relating IPO and underpricing to product market and publicity were applied on internet and technological companies that went public in the 1990s. These companies have raised about $26 Billion from the mid-1990s to 2000, but they left about $27 billion in terms of initial return, Loughran and Ritter (2002). In an attempt to answer why they left these amounts as a free lunch for secondary market investors, Krigman *et al.* (1999) claim that startups seem to ignore pricing and select their underwriters based on their ability to attract media attention. Selling off a part of their firm is as much a "branding" event as it is a source of equity financing. Branding is a means of establishing a start-up Internet firm's identity, name recognition, and even customer loyalty by making the company name an everyday household word. Further, if these Internet firms intend to return to the capital markets at a later date, they can make up this offering shortfall (by issuing more shares to their loyal institutional investors at a higher price in a secondary offering). Confounding this mispricing phenomenon is another stylized fact reported in Krigman *et al.* (1999). They claim that for stocks launched between 1988 and 1995, those that increased more than 60% (initial return) on the first day were actually the worst performers over time

In this regard, one of the early studies that related directly IPO characteristics to product market of the issuer is the one of Stoughton *et al.* (2001) they explore the product market motive for going public. They develop a model where consumers distinguish product quality from the stock price. The model predicts that, only better-quality firms will go public. Moreover, they find that effects of IPO announcements on rival firm's stock prices are related to inferences about market size and market share, their model also predicts that the likelihood of "hot issue" market depends on the distribution of market size, uncertainty and the degree of network externalities present in consumer preferences.

In a parallel effort, DuCharme *et al.* (2001) investigated the three main explanations for the hyper underpricing level of the internet firms during the 1990s: (1) media hype drives underpricing; (2) Internet firms leave money on the table to be able to follow up underpriced IPOs with follow-on financing offers; and (3) underpricing is a branding event designed to increase consumer awareness of the Internet company. They examine the relation between the extent of Internet IPO underpricing and proxies to test the three explanations. Proxies for branding include whether the firm is a Business to Consumer Company (B2C) and the extent of revenue increase post-IPO.

They conclude that media hype and the desire to return to the capital market are strongly associated with Internet IPO underpricing. Although underpricing is higher for B2C firms, sales increase post-IPO is not significantly related to the extent of underpricing.

In another seminal work, Demers and Lowellen (2003) investigate the potential marketing benefits of going public and IPO underpricing. They examine the impact of IPO underpricing on website traffic, which is a direct measure of product market performance for internet firms, they argue that if underpricing attracts media attention and creates valuable publicity, they expect an increase in web traffic following the IPO. They find that web traffic growth in the month after the IPO is positively and significantly associated with initial returns, and the effect is economically significant. Additionally, they investigate media reaction to initial returns for a broader sample of IPOs. They suggest that the marketing benefits of underpricing extend beyond the internet sector and the ''hot issues'' market of the late 1990s.

In the same vein, following Demers & Lewellen, Harasheh and Gatti (2014) investigate directly the relationship between IPO variables and brand value for the top 500 international brand companies. Their study is considered the first to explore directly the correlation between the level of underpricing and brand value. They find that brand value is positively related to the level of underpricing and that on average current brand companies had not been recognized as strong brands at the time of their IPOs, which supports their hypothesis that underpricing enhances brand value ex-ante rather than top brand companies tend to underprice more, they also find a strong positive relationship between private equity and brand value.

In the same regard, some law scholars have started to investigate the role of IPO contract design and process in enhancing the brand value ex-ante. Some case studies by Fliescher (2006; 2007) on Google and MasterCard exploring the IPO branding effect on both companies.

According to the author, Google achieved a great success in terms of marketing and branding aspects besides the financial aspects in spite of the challenges Google faced during their IPO process. The legal infrastructure of a deal can have a branding effect: the design of the deal may change the brand image of the company. The structure of the deal affects not only the relationship between the firm and its investors, but the relationship between the firm and its customers. Google innovation was the use of auction structure and not the Bookbuilding, but the true innovation was not the auction itself; auctions have been used to sell stock before. The true innovation was how the structure of the deal was employed as a marketing tactic, enhancing Google's image. The structure allowed us to peer through the corporate veil and spy the values of the company's founders. Innovative deal structures are striking, and they can marginally affect the set of mental associations that make up brand image. Google is not just a network of connected contracts; it is playful and innovative, (according to the author).

Some playful messages were embedded in Google's IPO. The amount of money that Google sought to raise, $2,718,281,828, was a bit of "geek humor." 2.718281828 is the mathematical constant e, which is the base of the natural logarithm function. Google continued winking at the nerds in its follow-on offering in August 2005, selling 14,159,265 shares. The number represents the first eight digits after the decimal in the mathematical constant pi.

At the end and as concluded by the author, the structure of the Google IPO affected how consumers think about the company. Having staked its claim as a playful, innovative, trustworthy company – through the IPO structure and other strategic moves – Google is now held to a higher standard in the court of public opinion. Its ability to maintain its lofty image will be tested as it faces regulatory challenges and privacy concerns. One thing seems clear, though: the auction structure may have left some money on the table in the short run, but pre-IPO shareholders would hardly complain now.

MasterCard is another successful brand building through its IPO; the case study analyzed the legal infrastructure of the MasterCard IPO. The author argues that the goal of the deal's design was both to reduce antitrust exposure and enhance the company's image as a safe, secure brand that facilitates a middle-class consumer lifestyle. Two central actions helped to accomplish these goals.

First, the design of the unusual "reverse" dual-class voting structure, which allowed the member banks to reduce their formal control over the firm while maintaining a significant economic stake. Second, they designed a charitable foundation to serve as a powerful corporate governance device as well as to potentially serve altruistic ends.

After reviewing the seminal work related to the relationship between IPOs and underpricing, and brand value creation; a sound group of finance and marketing scholars, and practitioners seem to agree that IPO process and underpricing enhance brand value ex-ante.

4. BRANDS IN THE SCOPE OF FINANCE

Before the term "brand" has become an important issue in finance, it had been the main subject for marketing scholars and executives. The theme of branding has occupied a sizable literature and research by marketing scholars since sixties of the twentieth century. A brand can be defined as: "the name, associated with one or more items in the product line, which is used to identify the source of the character of the item(s)" (Kotler, 2000). While The American Marketing Association (AMA) defines the brand as "a name, term, sign, symbol, or design, or a combination of them, intended to identify the goods and services of one seller or group of sellers and to differentiate them from those of competitors" (p. 404). Within this view, as Keller (2003) says, "technically speaking, then, whenever a marketer creates a new name, logo, or symbol for a new product, he or she has created a brand" (p. 3). He recognizes, however, that brands today are much more than that. Based on many definitions of brands, we conclude that the bottom line function of a brand is to be an identifier.

Traditional marketing considers brands as another step in the whole process of marketing to sell products. Kotler (2000) mentions branding as "a major issue in product strategy" (p. 404). As the brand was only part of the product, the communication strategy worked towards exposing the brand and creating a brand image. In the same manner, Aaker and Erich (2000) mention that within the traditional branding model, the goal was to build a brand image; a tactical element that drives short-term results. While Kapferer (1997) mentions that "the brand is a sign -therefore external-whose function is to disclose the hidden qualities of the product which are inaccessible to contact" (p. 28). The brand served to identify a product and to distinguish it from the competition. According to Kohli and Mrugank (1997) the challenge today is to create a strong and distinctive image.

Moreover, marketing executives have been very concerned about the value of the brand from a financial perspective, which is also called brand equity, even branding itself is considered a marketing activity, Ambler (2003).

Brand equity, as first defined by Farquhar (1989) is "the 'added value' with which a given brand endows a product" (p. 24). Later on, three main perspectives of brand equity have emerged, consumer-based brand equity (CBBE), market-based brand equity (MBBE), and the financial-based brand equity (FBBE):

Customer-based brand equity (CBBE): is defined as "the differential effect of brand knowledge on consumer response to the marketing of the brand", Keller (1993). Market researchers have always been trying to find the appropriate metrics for consumer differential effect. Many metrics have been developed, but all share three common dimensions of brand equity: brand strength includes brand differentiation and the relevance of the brand to the consumer, whereas brand stature considers the brand's esteem and consumer's knowledge (awareness and understanding) of the brand, Agres and Dubitsky (1996). And brand energy which captures the degree to which a brand is perceived as innovative and dynamic, Mizik and Jacobson (2008).

Market-based brand equity (MBBE) "Product Market": A second perspective on brand equity is based on market-level indicators. Some researchers claim that no matter how brand equity is measured or for what purposes measurement serves, the marketplace should be the ultimate driver of the value of the brand, Hoeffler and Keller (2003). Proxies of marketplace performance of the brand include price premium, revenue premium, increased advertising elasticity, and the ability to obtain distribution channel and shelf space, in addition to traditional market performance measures such as sales, profit, and market share, Boulding *et al.* (1994). The price premium is the most commonly used indicator measuring the premium consumers willing to pay more for a branded product over non-branded one, Aaker (1992;1996); Chaudhuri and Holbrook (2001). Firm's profit can be increased by price premium derived from a strong brand and provide resources to reinvest in the brand, Aaker (1992). In another effort, Ailawadi *et al.* (2003) propose revenue premium as another market level measure of brand equity. Similar to the price premium, revenue premium is the difference in revenue for a branded good versus a private label good. Even MBBE is considered a successful measure of branding efforts, but executives at publicly traded companies are more concerned about the link between branding and shareholders' value at the market level. Still, MBBE proxies are relatively easy to calculate and fully reflect the top-line performance measures that serve as standing goals for a majority of marketing managers but they fall short in linking branding with the ultimate firm performance metric of shareholder value.

The link between CBBE and MBBE models to demonstrate that customer mindset measures affect the brand's performance in the market have been studies in few research (e.g., (Srinivasan *et al.*, 2010)). Ailawadi *et al.* (2003) were in favor of revenue premium as a measure of brand equity because it is not only stable but reflects changes in brand value over time; stock performance impact, however, is not considered. Kim *et al.* (2003) find that brand's perceived quality, image, and loyalty are positively associated with firm revenues within the hotel industry. A few studies examine the market valuation impact of MBBE focusing mostly on top-line performance, e.g., Pauwels *et al.* (2004) however, more research is needed in this area. The overall conclusion is that the MBBE is, on average, positively related to firm value, Srinivasan *et al.* (2011).

Financial-based brand equity (FBBE) "Financial Market": A third approach for measuring brand equity is based on financial market performance (Amir and Lev, 1996). Here, brand equity is estimated by the difference between total firm's market value and the value of tangible assets, Simon and Sullivan (1993). This method separates firm's assets into tangible such as equipment, plants, and other tangible assets, and intangible assets such as goodwill. From an accounting perspective, brand equity is an accumulated intangible asset enhanced by marketing expenditures and brand management tools, Ambler (2003) that generates future cash flows or reduces the volatility of future cash flows. Brand value appears to be taken into account by investors in their stock evaluations, Barth *et al.* (1998).

One of the most recognized financial-based brand equity metrics is the "price-earnings multiple" which is derived from a combination of consumer-based and market-based measures of the brand. This methods is used by Inter-brand LTD (a UK-based firm specializing in valuing brands) and considers branded earnings (i.e., economic profits attributable to brand) times brand strength (as an indication of the discount rate for future brand revenue streams). The Inter-brand valuation metric thus combines the subjective consumer mindset of brand equity with objective brand performance in the product market. FBBEs are subject to criticisms of subjectivity and lack strong theoretical underpinnings.

Regarding the relationship between brand value estimates and advertising expenses, Barth *et al.* (1998) find that they are significantly positively associated. Additionally, brand value estimates and shares prices are significantly positively related. They provide influential evidence relating to the reliability of estimates of brand values based on the methodology developed by Inter-brand. Furthermore, using Inter-brand's estimation of brand equity, Kerin and Sethuraman (1998) find that there is a positive relationship between financial brand value and market-to-book (M/B) ratio.

In a similar endeavor, a seminal work comes from a different perspective and supports the above-mentioned context; Madden *et al.* (2006) compare an ex-ante portfolio of the top 111 brands between 1994 and 2001 to a benchmark to discover firm value creation through brands. They show that companies can create greater shareholder value with less risk by investing in branding and cultivating strong brand assets. Mizik and Jacobson (2009) show, however, that the predictive power of firm value is improved significantly by taking into account brand measures that consider accounting variables such as sales. Even though there is a current debate for recognizing financial value of the brand in the accounting statements, Barth *et al.* (1998) and Lev and Sougiannis (1996) there is little disagreement that brands operate as intangible assets of a firm.

The link between brand value and firm's value has been a subject to many investigations. As indicated by Srinivasan *et al.* (2011) there are two main linkages, the direct one is through enhancing directly the cash flows of the firm by considering the brand as an asset, and the indirect rout that considers brands as information rather than assets.

Regarding the first rout, research suggests that investors' perceive incremental information on branding activities as contributing to expectations of future cash flows, Srinivasan and Hanssens (2009). Moreover, Doyle (2001) proposes that brands are intangible assets that increase the level of cash flows and reduce the vulnerability of these flows. Srivastava *et al.* (1998) propose that market-based assets such as brands can increase shareholder value through (1) an acceleration of cash flows, (2) an increase in the level of cash flows, (3) a decrease in the volatility and vulnerability of cash flows, and (4) an enhancement on the residual value of cash flows. Under the efficient markets model, Fama (1970) stock prices at any point in time fully reflect available information and provide an expectation of discounted future cash flows. For example, when there is a brand extension announcement, investors will decide to buy or sell company stock based on outlook how the brand extension will affect future cash flows, Lane and Jacobson (1995). If investors value such brand extensions, this will result in increases in stock price.

The second path is brand as information signaling tool; as documented by previous research, stock markets represent a sphere of information asymmetries between different agents in the market, Myers and Majluf (1984). In the same regard, Spence (1973) in his signaling framework shows that the relevant information owned by management and insiders will be revealed by the market through different signals, and the brand related information is one of these signals. Keller (2007) defines a brand as a collection of associations that communicate information with consumers. Brand positioning is the strategic discipline through which brand information is summarized, but all brand actions send signals of brand meaning and equity to consumers and investors of the firm. Furthermore, the socio-cultural view of branding and the role of brand as a signaling device was also supported by Holt (2004) and McCracken (1988).

Supporting the above argument, many studies investigated the premise of brands-as-information, and document consistent findings, in particular, they studied the impact of brand signaling on firm stock price, Agrawal and Kamakura (1995); Lane and Jacobson (1995); Mathur and Mathur (1996). Other studies investigated the relation between brand equity and stock ownership and investors' concentration; they find that firms with high brand equity as gained through increased advertising expenditures have a larger breadth of ownership of the firms' stock because investors perceive greater and more accurate information flows about such companies, Grullon *et al.* (2004). Similarly, firms with strong brands are well-known and this reputation effect signals lower risks of the firm's stock to the investors, McAlister *et al.* (2007) and Rego *et al.* (2009).

The research on the impact of brands on firm's financial aspects have not stopped on stock prices and returns, it has also extended to mergers and acquisitions (M&A), brands play a major role in M&A and their cash flow expectations can drive significant price premiums from acquiring firms. The M&A setting is also useful for understanding brand equity effects on firm value. Additionally, in response to the importance of brands in M&A, the SEC in 2001 requires the reporting of intangible brand assets in M&A transactions, thus granting a finance-based indicator of brand equity value to the firm. Accordingly, Bahadir *et al.* (2008) study the drivers of brand value in M&A and its impact on firm value and hence shareholders value. They investigate 133 M&A transactions among U.S.-based public firms from 2001 to 2005, and they consider both the characteristics of the target brand and the less-considered acquirer's perspective on brand value, the authors find that the brand marketing capabilities of both the acquirer and target companies have positive effects on the target firm's brand value.

Brands are always attached to long-term perception by investors and consumers, thus it is important for firms to build a brand strategy. A brand strategy refers to the long-term plan for the efficient development of brand equity to enable the achievement of brand objectives and thereby increase shareholder value. Here, we consider five main strategic mechanisms designed to enhance brand performance and drive firm value: trademark and licensing strategy, brand extension strategy, brand alliances, brand portfolio strategy, and brand crisis management.

Besides, marketing literature documents various tools to enhance brand building such as advertising, and promotions, each one has a different way how to influence brand equity and hence firm value. Moreover, previous studies show contrasting results for each tool in affecting brand equity and firm value. In this regard, one of the key issues in this study is to investigate going public (IPOs) and underpricing as other financial market-based tools for building a long-term brand equity.

In the same manner, brand equity as a concept has been developed early 1990s, Aaker (1991). Still, how to value a brand has been the debate by researchers and managers. Malhotra *et al.* (1990) conclude that future research should focus on further measurements of the brand equity. They also proposed that a generally accepted measure could add more understanding of the strategic role of brand equity in extending the brand and how to benefit the firm financially. While there are a number of approaches available to managers, it is still uncertain which approach is best, and the discount rate, growth rate and useful life of the brand are among the main concerns in brand valuation, Kapferer (1994).

Assessing the correct brand value will ensure an efficient resource management that maximizes the overall value of the firm, particularly in optimizing a brand portfolio. All decisions regarding the brand such as the evaluation of brand manager performance, and the decision whether to build a strong brand will be simplified. Additionally, finding the correct brand value facilitates the execution of deals such as M&A. Furthermore, an accurate brand equity valuation ensures that brand-licensing fees correctly reflect the benefits received (Keller, 1998).

5. IN CONCLUSION

In present review paper, we present a comprehensive review of the literature regarding the relationship between IPO variables, especially underpricing from one side, and brand value on the other. We can say that the book of theories explaining underpricing has not closed yet, the validity of each group of theories is a function of time and market and country-specific factors. This review study comes to shed the light on one of the least tackled explanations, it is underpricing as a brand value enhancing or image improving tool. Furthermore, we show how close is the relationship between financial markets and product markets, and how companies may use financial markets as product marketing channels. We also show a strong and positive relationship between private equity and brand value. Investors, moreover, seem to discount brand values when investing in the IPOs which gives a support how brands affect firm's value through discounting future cash flows attributed to brands and accordingly, we provides some managerial implications such as:

1. Based on the facts regarding the decline in the IPO activity after 2000, going public with strong fundamentals reveals the good side of the company and enhances its value, and

maybe in this case, running independently is better than being acquired by a bigger peer that can reenergize the IPO market again which is positively related to macro-economic activity.

2. Management should not be scared of leaving money on table since underpricing is more image enhancing than overpricing. Facebook Company was overpriced with respect to its peers; it started to be out of the top brands directly after it went public.
3. If the management is confident of the current corporate fundamentals and future prospects, they should not be reluctant to challenge the market. Google Company challenged the market by using auction rather than a book-building approach that does not favor institutional investors, now it enjoys almost the highest globally brand value of $63 billion.

At the end, we hope that the issues discussed in this paper encourage other researchers working in this area to carry out related research on different settings or time periods and produce findings that may give answers to above issues. Further research is needed to support which companies underprice more, business to business “B2B” or business to consumer “B2C”. Additionally, more case studies are very important to give a stronger insight on the relationship between IPOs and brand values on ad-hoc basis.

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