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THE ROLE OF TRADEMARKS (AND THE BRANDS THEY SIGNIFY) AS A DISTINCT FORM OF ECONOMIC ACTIVITY IN THE GLOBAL ECONOMY

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1. Introduction

From the beginning of time, man has always felt the need to brand as a means of staking claim to his possessions. About 7,000 years ago in Neolithic times, it is thought that the first marks served to show the legitimate owners of livestock.¹ In the middle-ages, craftsmen started to identify their workmanship with a mark and as research shows, documented examples of the economic use of trademarks is found in the Roman Empire, where Roman bricks were stamped with the manufacturer's name, date and place of production.² All of these eventually culminated in the formation of trademark laws in the 1800s which was enacted in France, the United Kingdom and the United States in 1857, 1862 and 1870 respectively.³

In recent times however, a trademark is more than just a means of identifying goods and their owners. As time went on, marks evolved not only to represent the author of an object but also their obligation in assuring the quality of the product. A trademark distinguishes a company from its market rivals. It helps in creating brand identity and gives the firm a mark of authenticity which in turn attracts customers towards it.

This paper aims to explore the importance of trademarks and the brands they represent as a useful marketing tool and how this inadvertently serves as a distinct economic activity in the global economy. This paper will be divided into four sections. The next section of the paper will look at the functions of trademarks and trademarks as a source of marketing power. In doing this it will consider the functions and the economic theories of trademarks, their economic connotations, vis-à-vis the brands they represent. The third section of this paper will look at the marketing power of trademarks and brand based marketing and the fourth section will conclude this paper.

2. Functions of Trademarks and Trademarks as a source of Marketing Power

2.1 Trademarks and Brands

In order to properly understand the market power of trademarks, it is important to understand what a trademark is and the function it serves. Ramello, describes trademarks as a sign, logo, name, word or symbol or a combination of them all used by a producer or vendor to distinguish a particular product or service.⁴ A trademark bestows on the owner the exclusive right "to use it as a means of identifying certain products of the kind for which it has been registered and distinguishing them from others."⁵ Most importantly, a

¹ Giovanni B. Ramello, 'What's in a Sign? Trademark Law and Economic Theory' (2006) Working paper No. 73 Department of Public Policy and Public Choice – POLIS < <http://polis.unipmn.it/pubbl/RePEc/uea/ucapdv/ramello73.pdf> accessed November 20 2014

² Edward S Rogers, 'Some Historical Matter Concerning Trademarks' (1972) Vol 6 239

³ UK Merchandise Marks Act 1862, US Trademark Law 1870

⁴ Ramello (n1)

⁵ Andrew Griffiths, 'Trade marks Plus? The Role of Trade marks in the Global Economy and the Danger of Over Protection' (2007) Liverpool Law Review 107-141

trademark is used to show the place of origin of a particular good or product, which is a common trend which can be deduced from its many varied definitions and history. However, AG Colomer in his opinion to the European Court of Justice on *Arsenal FC v Matthew Reed*⁶ stated that "It seems to me to be simplistic reductionism to limit the function of the trade mark to an indication of trade origin... The trade mark acquires a life of its own, making a statement, as I have suggested, about quality, reputation and even in certain cases, a way of seeing life."⁷

On the other hand, brands can mean different things to different people and they often sometimes go hand in hand with trademarks. Walter Landor said: "Simply put, a brand is a promise. By identifying and authenticating a product or service it delivers a pledge of satisfaction and quality."⁸ As consumers, people have a propensity to make buying decisions based on or by looking for and distinguishing between brands. According to Desai, this difference in consumer preference due to association with brands is no more apparent than in the difference between Coke and Pepsi. He states that part of the reason why people purchase Coke instead of Pepsi isn't solely because it is a different kind of cola, but partly because of the difference in label. Coke with its red field with white cursive "Coca-Cola" scribbled across it and iconic glass bottle invokes the sense of being the classic all American. More aptly put a sip of coke means you are imbibing a whole culture. On the other hand, Pepsi often changed its logo and was seen as a drink of the new generation and is often associated with youth.⁹

The above example shows how trademarks or brands can mean different things to different people and be used to target a particular audience which is just one of their many functions. The following section will look at the marketing power of trademarks.

2.2 Functions and Marketing Power of Trademarks

Trademarks and the brands they represent are purely economic in value. This section aims to further buttress the functions of trademarks and also explain the reasons why trademarks have the power they do in attracting consumers to the brands that they represent. In today's market place where consumers have more choices and stakeholder expectations are high, mere ownership of a trademark does not guarantee market power.¹⁰ The difference between success and failure of a product is often leveraged on the edge it has to offer, be it a quality or feature of the product that sets it apart from the competition. It is usually this edge that forms the basis of trademarks and or brand marketing. It is important to note that without legal protection of trademarks it cannot attain marketing power. The protection afforded a trademark is that of exclusivity which means only the owner of a trademark can exploit its marketing power.

Apart from what is believed to be its primary function of identifying the source or origin of a product, a trademark must be able to satisfy and perform several secondary economic functions such as that of representing quality, providing information and advertising.¹¹ A trademark indicates quality as a function of its trade origin. By signifying the trade origin of a good, manufacturers risk consumers assuming that the quality of a product with which they are familiar will remain constant and match or exceed their expectations.¹² Where a trademark indicates consistent quality, it is said to provide consumers with an assurance of the quality of the brand they are about to purchase even though they cannot observe these qualities before purchase.¹³

Trademarks perform the advertising and marketing function by enabling consumers to differentiate a product which in turn is beneficial to the manufacturer of the product because it assists in the prevention of diversion of sales to other products.¹⁴ The ECJ in its

⁶ Case C-206/01

⁷ Available at <http://www.asser.nl/default.aspx?site_id=11&level1=13912&level2=13970&level3=&textid=36583>

⁸ Susan Nelson, 'The price of leadership' (2008) <www.landor.com/thinking/article/653> accessed 20 November 2014

⁹ Deven R. Desai, 'A Brand Theory of Trademark Law' (2010) 1 <<http://ssrn.com/abstract=1585327>> accessed 10 December 2014

¹⁰ M.A. Cunningham, 'A Complementary Existence: An Economic Assessment of The Trademark and Competition Law Interface in the European Community' (1995) 10 TUL Eur & Civ. LF 151

¹¹ Mohammad Amin Naser, 'Re-examining the Functions of Trademark Laws' (2008) Chicago-Kent Journal of Intellectual Property

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¹² Andrew Griffiths, *An Economic Perspective on Trade Mark Law* (2011) Unpublished

¹³ L.N Davis, 'Leveraging Trademarks to Capture Innovation Returns' (2009) Paper presented at DRUID Summer Conference

¹⁴ Naser (n11) 101

ruling regarding *L'Oreal vs. Bellure*¹⁵ recognised that the trademark performs an "advertising function."

The advertising function of trademarks relates to the social planning theory. It has been asserted that this is one of the most important theories justifying trademarks.¹⁶ The social planning theory proposes that trademark systems should be formulated in order to achieve a balanced culture and should aim to do justice to all concerned parties which include the proprietor of the trademark, other traders and competitors.¹⁷ According to this theory, the establishment of trademarks undergoes two stages; the first stage entails the proprietor of the trademark associating the mark with the product, and second stage entails, the public recognising the association between the trademark and the product. A recommended means by which this recognition can be achieved is through extensive advertising.¹⁸ This recognition created through advertising will create and increase a demand for the marked product thereby giving the trademark marketing power. A good example here is that of the study conducted on kids' preference for McDonalds Chicken Nuggets. The study showed that kids with Televisions in their homes who watched commercials had more affinity for McDonalds chicken nuggets than those who did not and that their level of preference was linked with the number of televisions in their houses. This is evidence that advertising causes recognition in the mind of consumers.¹⁹

Griffiths has explained how a trademark can easily become the focus of goodwill.²⁰ Frank Schechter stated that:

"Today the trademark is not merely the symbol of goodwill but often the most effective agent for the creation of goodwill, imprinting upon the public mind an anonymous and impersonal guarantee of satisfaction, creating a desire for further satisfactions. The mark actually sells the goods. And, self-evidently, the more distinctive the mark, the more effective it's selling power."²¹

This is because a trademark is easily identifiable and recognisable and its use is usually consistent. In addition to this, its use is exclusive to the firm which owns it. These qualities of a trademark make it easily imprinted in the mind of consumers and it will act as a signifier to the consumer.²² When consumers begin to get acquainted with a particular marked product, it undergoes a transformation as an indicator that can cause its market power to increase substantially. This transformation is a two part process as Griffiths explains in his book. First, the marketing power of trademarks is attained because consumers are more likely to be aware of the existence and availability of marked products when searching for products of a particular type and are more likely to connect these products with their own experience or other sources of information. Through these transformations, a trademark is no longer just a mark for identifying a product but is "familiar reference point" and "a source of information in its own right."²³

Trademarks also attain market power by serving as a source of information to consumers due to information asymmetry; a situation whereby a seller has more information about the unobservable features of goods being sold than the buyer.²⁴ Trademarks reduce the cost of searching to the consumer, thereby enabling their purchasing decisions.²⁵ Further buttressing this point is renowned Economist Nicholas Economides who states that:

"The economic role of a trademark is to help the consumer observe unobservable features of the trademarked product. This information is not provided to the consumer in analytic form such as an indication of size or a

¹⁵ [2009] E.T.M.R. 987 at [58].

¹⁶ Nasser (n11) 102

¹⁷ Ibid

¹⁸ Ibid

¹⁹ Editorial, Stanford School of Medicine available at < http://med.stanford.edu/news_releases/2007/august-first-food.html accessed 24 November 2014

²⁰ Andrew Griffiths, 'Information and Product? Trade Marks as a Source of Economic Benefit' (2006) *Common Working Papers in Law and Economics* 3

²¹ Frank Schechter, 'The Rational Basis of Trademark Protection' *Harvard Law Review* (1927) Vol. 40 No. 4 514

²² A. Griffiths, *An Economic Perspective on Trade Mark Law* (Edward Elgar Publishing, 2011)

²³ Ibid

²⁴ George A. Akerlof, 'The Market for "Lemons": Quality Uncertainty and the Market Mechanism' (1970) 84 *Quarterly Journal of Economics* 489

²⁵ Nasser (n11) 102

listing of ingredients, but rather in summary form, through a symbol which the consumer identifies with a specific combination of features. The trademark identifies both quality and variety features of the product; i.e., both features like freshness, more of which is desirable by all and features like sweetness, over which consumers have varying preferences, some preferring little of it while some prefer lots of it"²⁶

Economides goes further to explain that the degree of success of these functions is based on the frequency of purchase of the particular goods by the consumer and the inability of others to confuse it with similar marks which is a huge possibility because of the lack of adequate information available to consumers in many markets around the world. He also states that these unobservable features are key determinants of the value of the goods.²⁷

Furthermore, marked products gain recognition in the minds of the consumers, concerning its quality and other characteristics which is formed from their collective experience of the goods and other available information.²⁸ Harry D. Nims states that "[t]rade-marks may serve as indications not only of source but also of quality or of uniformity of quality".²⁹ A trademark acquires market power based on the reputation it gains in the minds of consumers in relation to the likely quality and other characteristics of marked products. This reputation is based on the experiences of consumers and their expectations or on other sources of information.

2.3 Law and Economic Theory of Trademarks

The economic theory of the marketing power of trademarks is based on view that trademarks confer some sort of competitive advantage or monopoly power on the owners. In explaining this issue, trademark laws have to be understood first. Trademarks are a form of intellectual property and therefore the laws that guide them can be said to fall under those that govern intellectual properties. The law aims to protect owners of intellectual properties, but when it comes to trademarks there seems to be a bit more than little discrepancy. A major difference which is evidenced is that which lies in the legal basis and economic function of trademarks.³⁰

Where trademarks just provide the information about the goods sold; the others actually involve the exchange of the said goods. An argument that has been put forward by trademark scholars such as Sean Morris about the marked difference between trademarks and traditional intellectual property (copyrights, patents) protection is that the latter aims to create incentives for the creator. In essence, maximise profit and provide economic benefits whilst the former do not necessarily require any form of innovativeness.³¹ He explains that this argument does not sit well with trademark owners who believe that economic incentives are accrued from their brands.

Over the years there has been a lot of literature dedicated to the functions that the laws governing trademarks perform. There are varying schools of thought proposed by scholars on the subject of the economics of protecting trademarks, such as those proposed by Landes and Posner which is supported by the Chicago school, and those proposed by Economides amongst many others. This section of the paper aims to highlight these different thoughts and draw its conclusion from them.

The issue of monopoly is not one taken lightly by operators within the economy, and for very good reasons, with the major one being that the consumer is at the mercy of the manufacturers or suppliers especially in terms of price fluctuation. The issue therefore arises that does protecting trademarks create monopolies? Economides concedes that competition is not always to the benefit of the society.³² He based this theory on perception advertising. The premise put forward is that firms can use trademarks together with persuasion advertising to shield itself from the normal tenets of competition by persuading

²⁶ Cunningham (n10) 527

²⁷ Nicholas S. Economides, 'The Economics of Trademarks' (1988) 78 Trademark Rep 523, 527

²⁸ Griffiths book here chapter 3, pg 11)

²⁹ Elmer W Hanak, 'The Quality Assurance Function of Trademarks' (1974-1975) Fordham L Rev 363

³⁰ P. Sean Morris, 'The Law and Economics of Trademarks; Product Differentiation, Market Power and New directions in Anti-trust' (2010) 3 available at <http://works.bepress.com/p_sean_morris/20>

³¹ ibid

³² Economides (n27) 523

consumers that the products represented by their trademarks are different and superior to their low priced substitutes and on this basis use this power to achieve monopoly or engage in price discrimination practices.³³

The Chicago school of thought's theory on the other hand is based on achieving efficiency by the use of trademarks. It argues that use of trademarks reduce the search costs which accrue to consumers, by providing them with information relating to the quality of the product ergo enhancing purchasing decisions, thereby creating a competitive equilibrium.³⁴ This is a view also supported by Landes and Posner³⁵ propose that protecting trademarks can be beneficial, because it enhances innovativeness when it comes to firms differentiating their products, thereby leading to more economies of scale and providing the consumers with more choices. They explain further that if a trademark is able to perform the vital function of reducing the communication and search cost to consumers by providing private signalling devices, thereby enabling its owners to charge a higher price in the market than its competitors, then it is in fact good for competition, because it benefits consumers and increases social welfare.³⁶

3. The Marketing Power of Trademarks and the Evolution of Brand based Marketing

Trademarks generate value for firms because they provide the legal basis for brand loyalty, one which subsequently confers a competitive advantage on them as owners of the trademarks. Once brand loyalty is established, firms may maintain this loyalty for a long time, as long as consumers are not disappointed or confused. However, the trademark may not in itself ensure that the value of the brand is maximized; this depends on the firm's advertising and marketing strategy³⁷ and also on the goodwill of the consumers. Consumers make buying decisions by looking for and recognising trademarks. Consumers are attracted to products based on their identification with trademarks attached to them.³⁸ This situation creates a scenario where such goods sell more quantities than others similar to it and go for a much higher price. This ultimately creates a competitive advantage that is consistent with the manufacturer's aim of achieving unrivalled competition.

The need to create brand awareness and recognition amongst consumers has led to the evolution of brand based marketing. This is because in order for firms to make the best use of the marketing power of their trademarks, they need to create recognition in the mind of consumers and they can do this by marketing. When there are marks that are easily identifiable, consumers will recognise it and buy it. Simply put brand based marketing functions effectively because trademark and brand owners can distinguish their products for marketing purposes.³⁹

The use of brand based marketing has been successful in raising sales as far back as the 1930s.⁴⁰ When the British confectionary firm Rowntree was caught in a period of slow sales and fierce competition, the firm developed key brands such as aero and kit-kat and engaged in a consumer focused marketing of the brands. They marketed the brands by highly differentiating them from their competitor's brands and reversed the ill fortunes of the firm.⁴¹ The marketing power and legal protection of trademarks is what afforded the firm the opportunity on brand based marketing. If there was no protection and marketing power of trademarks they could not have achieved this.

A second example of successful brand based marketing as a result on the marketing power of trademarks was the marketing and branding of Horlicks during the interwar period. Horlicks, used highly innovative advertising and original use of imagery amongst other means. Consequently, Horlicks was able to charge a premium price, far in excess of its competitors Ovaltine and Cadbury's Bournvita.⁴² What both studies show is that brand

³³ Jerre B. Swann, *The Trademark Reporter as Catalyst* (2011) Vol. 101 TMR page 83

³⁴ Morris (n30)

³⁵ William A Landes and Richard A Posner, 'Trademark Law: An Economic Perspective' (1987) Vol 30 Journal of Law and Economics 257

³⁶ *ibid*

³⁷ Dorothy Cohen, 'Trademark Strategy' *The Journal of Marketing* (1986) Vol. 50 No. 1 61

³⁸ Ralph S. Brown Jr, 'Advertising and the Public Interest: Legal Protection of Trade Symbols' (1948) 1187

³⁹ Griffith (n5)

⁴⁰ Michael Heller, 'Corporate Brand Building at Shell-Mex Ltd in the Interwar Period' (2008) CGR Working Paper 23 <<
<http://www.busman.qmul.ac.uk/cgr>

⁴¹ *ibid*

⁴² *ibid*

based marketing is beneficial to a firm in a competitive market. However, more important is the fact that this is only possible because of the existence and functions of trademarks. The exclusivity of trademarks, its informative, communication, quality and advertising function which give it its marketing power make brand based marketing possible.

In addition, because a trademark is distinct and easily identifiable firms even use familiar brands to break into new markets. This is done through brand extension or brand stretching and this brand based marketing can be related to the trademarks capacity to provide reassurance to consumers. Accordingly, rather than introducing a new mark or brand the firms use the existing brands to break into a new market because the marks and the brand they represent have secured a reputation with consumers.⁴³

4. Conclusion

This paper explored the function of trademarks and how they acquire market power. Trademarks have their major function in indicating the trade source of marked goods, but on an economic front tend to serve many more functions such as communicating, advertising and providing information. The paper discussed how these functions enable the trademark gain recognition the consumers mind and acquire market power. These functions of trademarks are believed to consequently reduce the cost of search to consumers, serving as a source of information and efficiency, all of which enable it to attract customers and gain market power.

This paper also discussed the economic theory of trademarks. The secondary functions of trademarks have been proposed to confer competitive advantage on firms such as monopoly of the market or huge market shares that deflect sales from other products. While some scholars have said that this is somewhat bad for the economy and doesn't foster good competition, one cannot ignore salient arguments of the monopolist view based on the fact that it fosters innovativeness. This innovativeness leads to a vast array of differentiation techniques and increases economies of scale thereby creating more choices for the consumers. Regardless of the stance taken on either argument above, one thing that is for certain is trademarks provide information about the trade origin of goods. For consumers, realising the trade origin of a good and identifying with it is a basis for good decision making.

This paper also discussed how the market power acquired by trademarks has led to the evolution of brand based marketing as an economic activity. The foundation of brand based marketing is rooted in the use, protection of trademarks and the market power they acquire. The incentive for a firm to market based on brands is as a result of the recognition of the trademarks and the brands they signify by customers which ultimately make the consumers choose those products. This recognition of trademarks and brands has also given rise to the marketing strategies such as brand extension and brand stretching. Brand based marketing is targeted at increasing demand for products and this paper cited two instances in which brand based marketing has successfully been used by firms to attract customers and gain a competitive advantage.

⁴³ Davis A Aaker and Kebin Lane Keller, 'Consumer Evaluation and Brand Extensions' (1990) *Journal of Marketing* 27