

How Predictive are Predictive Customers™?

Holly Stark and Marc Lepere

How predictive are Predictive Customers™?

Predictive Customers are a sub-set of consumers who are highly engaged in selective categories, aware of both cultural and marketing trends and who share their knowledge with others. They are knowledgeable, knowledge hungry, experienced and savvy. They are the “expert” consumer, inside the mainstream – **influencing** friends, family & colleagues and **predicting** what they will purchase.

Lepere Analytics is a proprietary methodology pending a US Patent. At its core is the ability to screen and qualify Predictive Customers in specific sectors from the rest of the population and to measure brand momentum 2-6 months in advance. The methodology has been independently tested and verified, in multiple countries, over a 4 year period by Columbia Business School, Zogby International and more recently Brand Keys, Inc.

More information on our methodology is detailed in two white papers: ‘Predicting the Future via Predictive Consumers’ and ‘Forecasting for Profit: Better Science, Better Data’ available on www.lepereanalytics.com

Predictive Customer predictions are continually and independently tested by our clients, Wall Street investment analysts and portfolio managers and by company management and marketing agencies. In Mar-11 for example, a major broker dealer found a 60% correlation between brand momentum and revenue surprises, high & low (4 datasets - 2010). This paper sets out the empirical track record 2008-2011.

Five levels of proof will be examined, working from the micro to the macro:

1. Market share
2. Sales revenues
3. Individual stock performance
4. Portfolio performance
5. GDP forecasts

1. Market share

Market share is an elusive commodity with many different classifications of the market, the competitive set and methods of calculation. Company specific data is proprietary. Lepere Analytics provides a tool to predict brand momentum – a forward looking measure of market share.

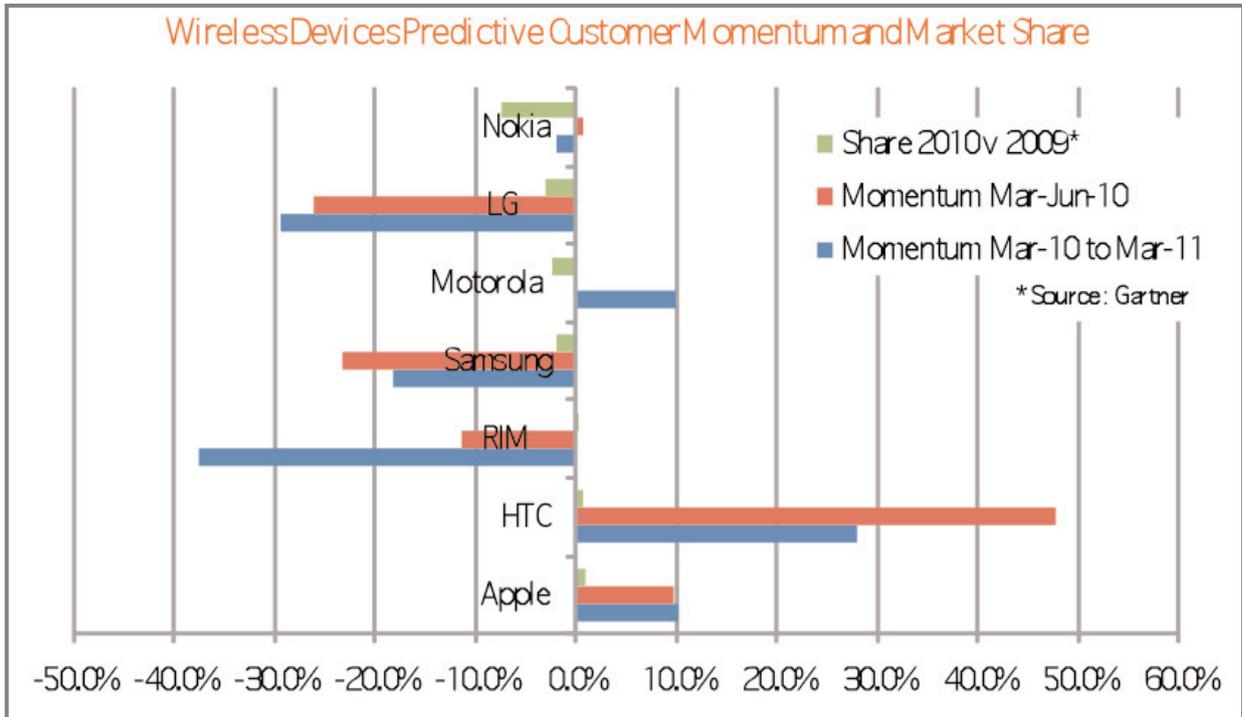
Brand momentum is measured in consumer sectors and subsectors, rather than industry defined or GICS sectors. The aim is to create the real world trade-offs facing consumers. Once a respondent has been classified as a Predictive Customer, they self-select a number of categories where they are most engaged on an ongoing basis. For the major brands in each selected category, the Predictive Customer indicates their view as to whether the brand is moving forward, falling behind or staying the same.

Brand momentum is the net momentum score i.e. the % of Predictive Customers who believe a brand is gaining ground minus the % who believe it is losing ground. It is a relative measure both to the competitive brand set and to all brands in the study. It is not an absolute or a measure of momentum in the sense of a zero sum gain.

Market share data from the handset market for 2010 illustrates how brand momentum data often predicts market share.

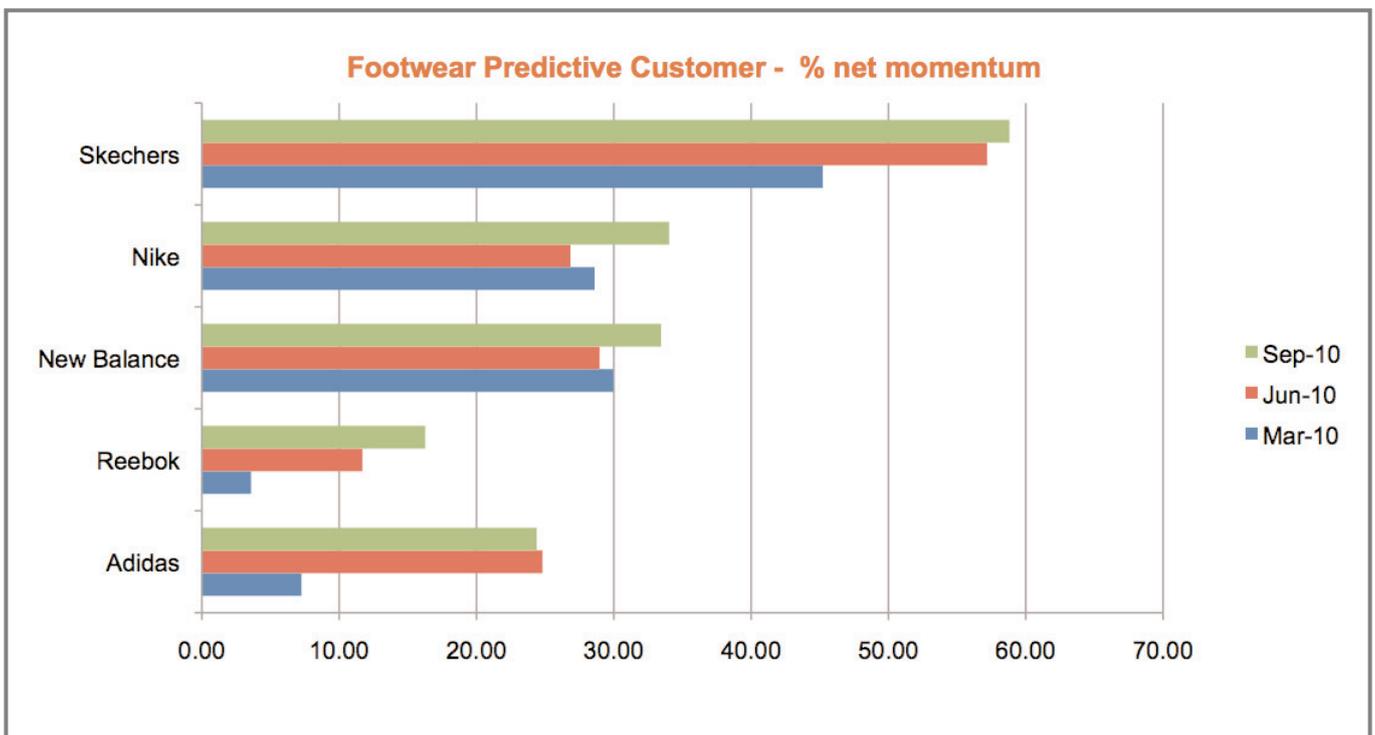
The handset market is complex with market share being dominated by carrier deals as well as direct sales. Despite these complexities, the change in momentum for these leading handset brands between the Mar and Jun-10 studies accurately predicted movements in market share for the whole of 2010, as can be seen below. Also plotted is brand momentum for the full year Mar-10 to Mar-11, which includes the Sep and Dec-10 studies.

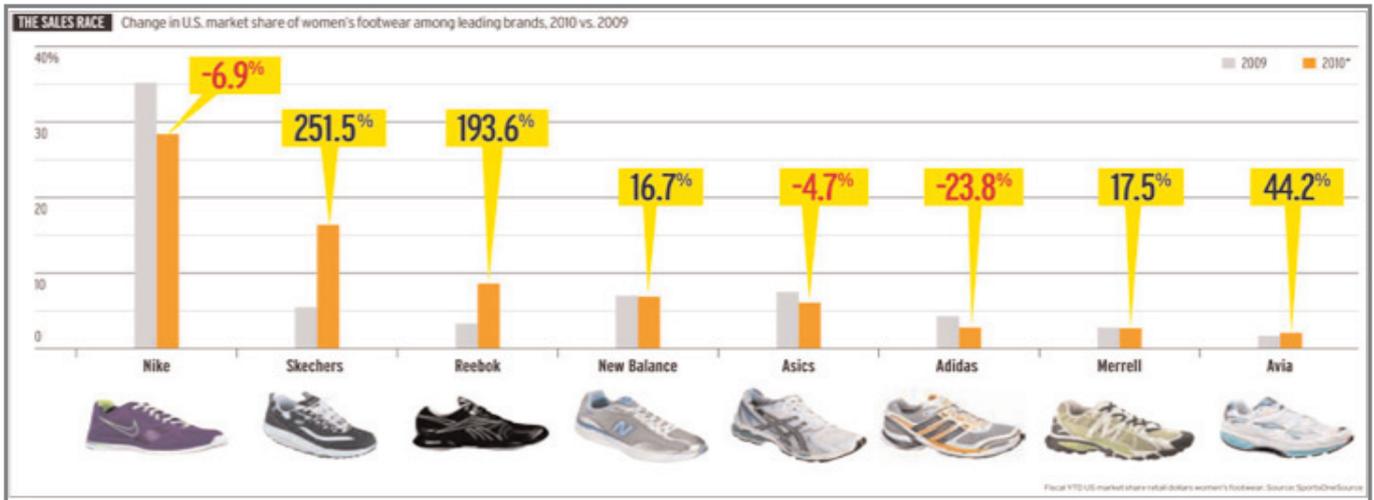
N.B. We are studying these results in hindsight. When they were made these predictions of brand momentum were forward-looking and predictive.



Our 2010 studies also captured the interest generated by the introduction of ‘toning – train as you walk – footwear’ in the US. This innovation dominated the sector in 2010, especially woman’s footwear.

The brand momentum data below again accurately predicted changes in market share. Skechers, Reebok and New Balance – the biggest share gains as it turned out – were all strong in the new technology, while Nike and Adidas, not having a competitive offering lost out on brand trade-offs and subsequent market share.





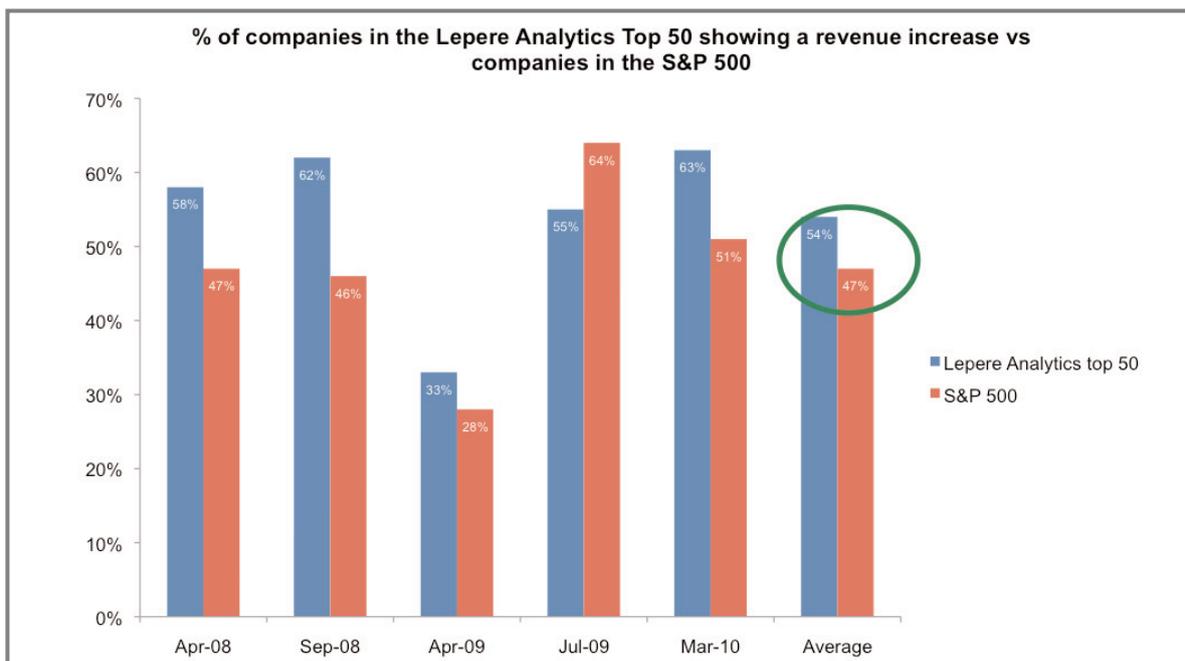
Source: SouceOneSports

2. Sales revenues

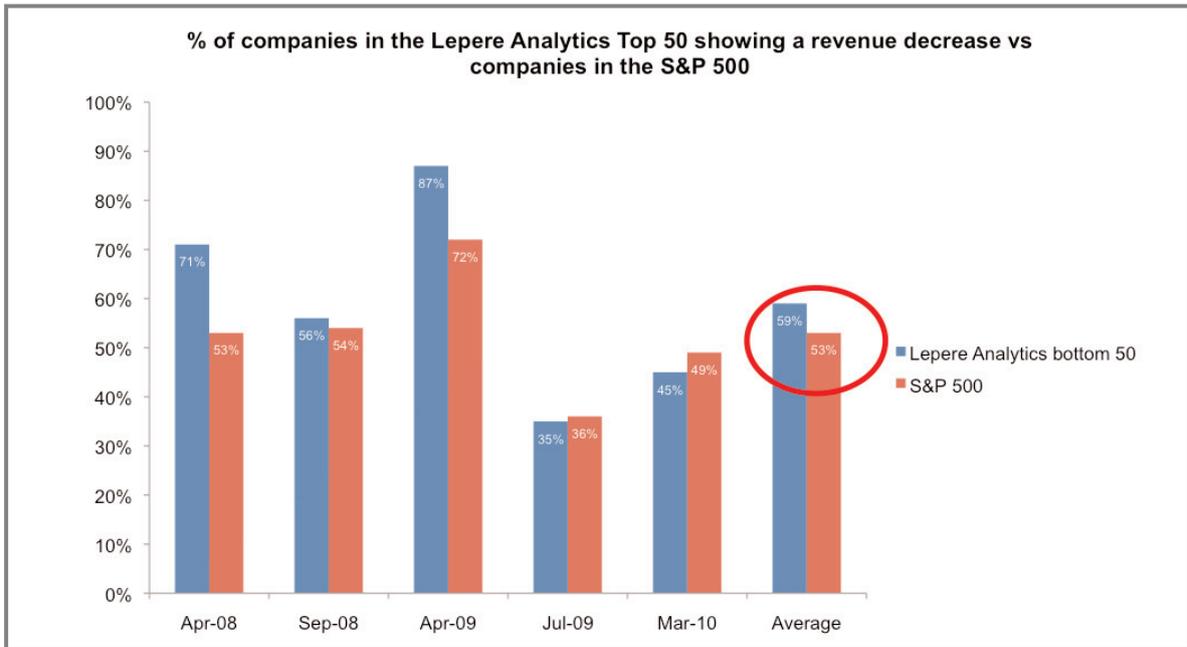
The critical part of the Lepere Analytics methodology integrates brand momentum data from Predictive Customers, with company public data to create Growth Factor© scores. The Growth Factor is calculated for each company individually.

When a company is a single brand company like Starbucks or UPS, for example, the brand and company scores are inter-changeable. But for most companies, like Nestle, for example, different brands, like Perrier and Lean Cuisine, or divisions need to be assigned back to their quoted parent. In doing so, the Growth Factor identifies drive brands or divisions and weights them in line with their contribution to the P&L, strategy, revenue potential, etc. Companies with sufficient data (e.g., no M&A, bankruptcy) were ranked in order of their Growth Factor score to create a top 50 and bottom 50.

The graph below looks at the top 50 companies and compares them with all companies in the S&P 500. The blue bars indicate how consistently Predictive Customers accurately predict companies with revenue increases vs the total of all S&P companies who did actually grow in each period.



Predictions of revenue decline are similarly consistent between Apr-08 and Mar-10.



3. Individual stock performance

Lepere Analytics uses proprietary algorithms to integrate brand momentum data with company data to create Growth Factor scores. The Growth Factor is calculated for each company individually. It is a weighted measure of a company’s revenue potential and a lead indicator of company operational health.

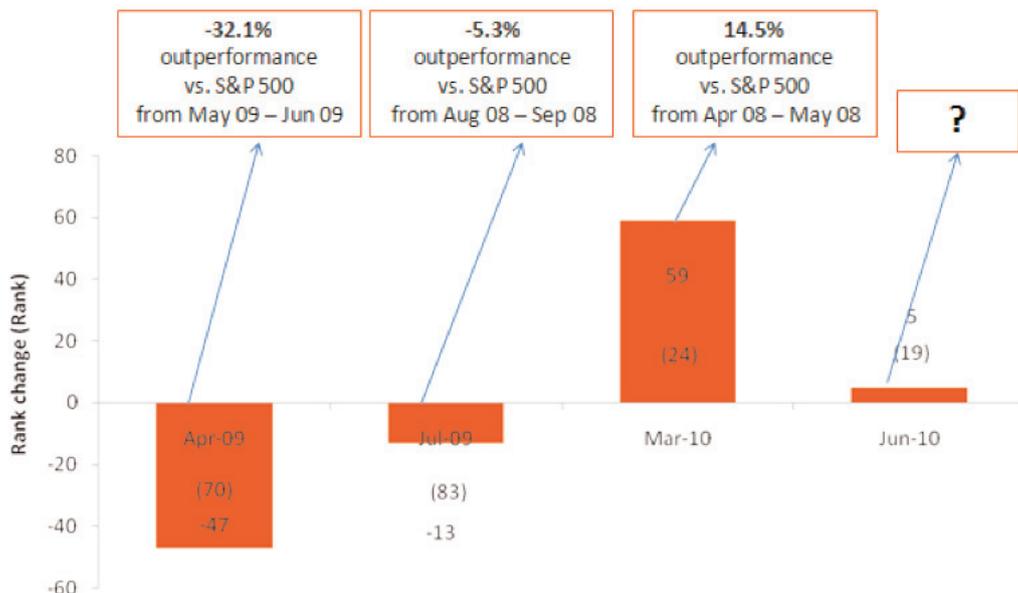
The Predictive Customer report for Underarmour (**UA**) in Jun-10 predicted strong stock performance:

- “**UA** had the second highest Growth Factor of 303 listed companies at 2.09.
- We believe strong brand momentum and consumer sector leadership will deliver healthy revenues. The Underarmour brand leads both the ‘Sports Gear’ and ‘Sportswear-General’ consumer sectors . The 32%+ momentum lead over nearest rival Nike is up from +20% in March 2010 in both consumer sectors and is a compelling indicator”.

The following 3 month return (Jun-30 to Sep-30) on Underarmour (UA) was **35.9%**.

The Jun-10 study also predicted strong stock performance for Harley-Davidson (**HOG**):

- “**HOG** should outperform the S&P500 due to its continued improvement in growth factor rank. Since April 2009, HOG’s stock performance vs. the S&P 500 has moved in line with the direction of its rank changes.

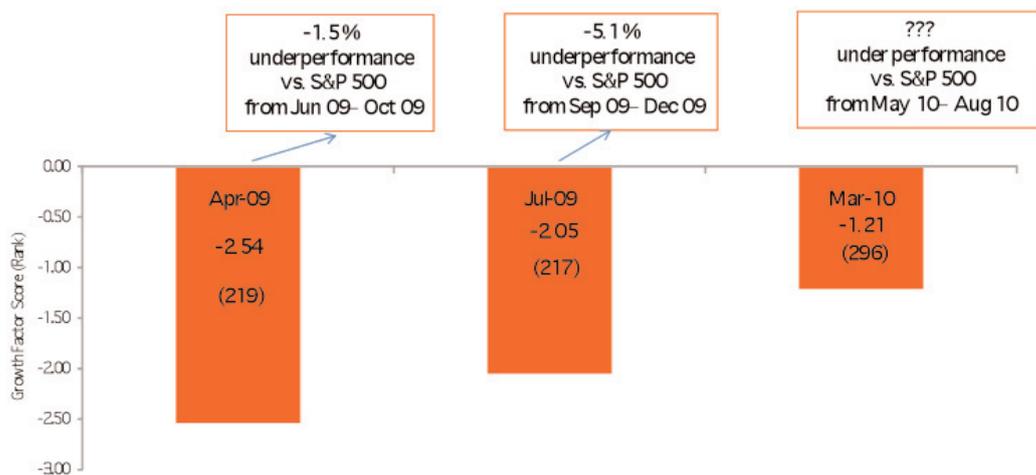


- In our most recent June 2010 poll, **HOG** has moved up a further 5 places into the Lepere Analytics top 20.
- Our forecast is further supported by the continued #1 position of the Harley – Davidson brand within the Motorcycle sector which has resulted in a positive % brand momentum.

The following 3 month return (Jun-30 to Sep-30) on Harley-Davidson (HOG) was **27.9%**.

On the short side, the Mar-10 study predicted continued underperformance for Earthlink (**ELNK**):

- “Historically, **ELNK** has underperformed the S&P 500 due to its poor Growth Factor score and bottom quintile ranking. Although scores are improving we expect this trend to continue.



- Our expectation is also supported by the Earthlink brand remaining the second worst in the Online consumer sector. The brand scores a negative momentum of -44% in this poll.
- On the upside, **ELNK** could benefit from the improvement of the Online sector’s ranking (up 38 places). However, we believe that such +ve sector momentum is created by other online brands and shouldn't relatively benefit **ELNK**”.

The following 3 month return (Mar-31 to Jun-30) on Earthlink (EA) was **-6.8%**.

Internal testing on passive and active portfolios from 2008 – 2009 revealed that 67% of the top 20 and bottom 20 names, ranked by the methodology (Growth Factor score), predicted a three month outperformance against the S&P500, two months after polling. In other words the data appears to be predictive 2-5 months out, approximately two thirds of the time.

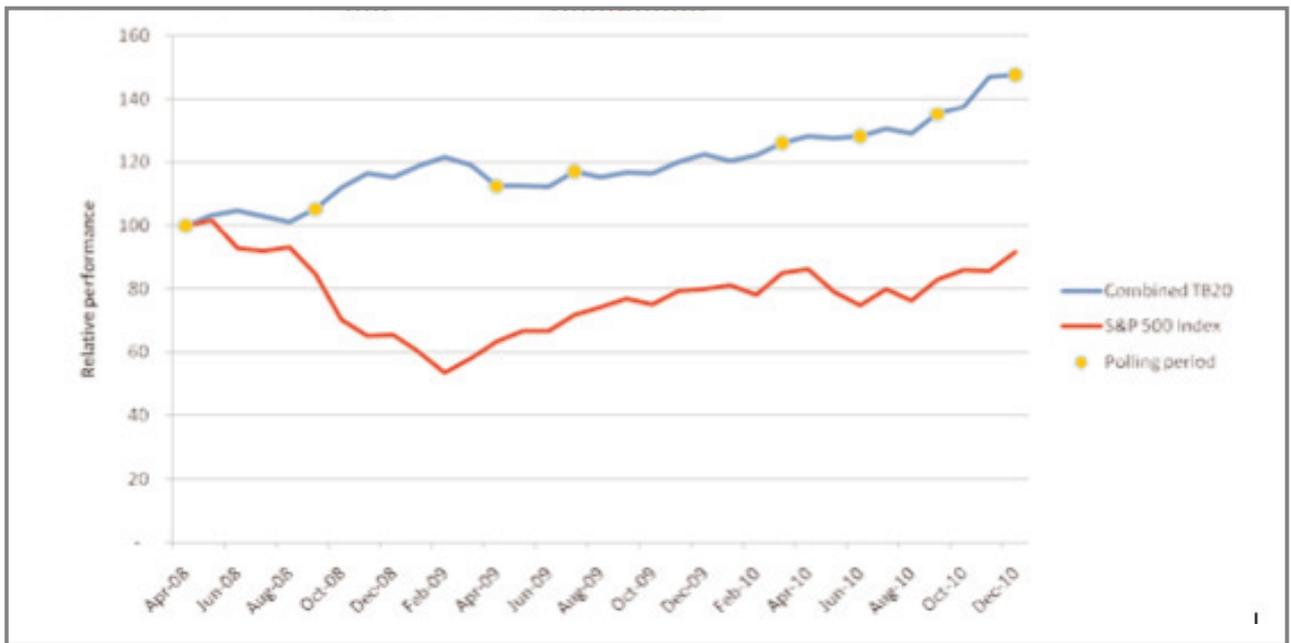
Polling is conducted quarterly in March, June, September and December timed to coincide with peak company earnings seasons. The data helps company management support sales and revenue forecasts and investment analysts with revenue estimates.

4. Portfolio performance

Halpern Associates, LLC a firm of Certified Public Accountants specialising in hedge fund administration tested the data from Apr-08-Dec-10. In their analysis the Lepere polling data is **the only basis on which names have been selected**; no other investment criteria or factor has been taken into consideration when selecting names. Additionally, no trading discipline has been deployed other than a 10% stop loss. The aim was to isolate the data as being the only variable.

In the 32 months (Apr-08 to Dec-10) the TB20 (top 20 and bottom 20 names) portfolio performance was up 46% against the S&P500.

Combined TB20 vs S&P500 (Halpern)



Top 20 and Bottom 20 vs S&P 500 (Halpern)



Test parameters:

- New portfolio at each poll, constructed on first day of the month following each poll
- Long top 20 and short bottom 20, ranked by Growth Factor
- \$1M fund - \$500K long and \$500K short (left in cash to cover, not as leverage for longs)
- Each position equally weighted i.e. 2.5% of portfolio
- 10% stop loss and held as cash until next portfolio re-set
- At period end portfolio liquidated with P&L carried forward to new portfolio
- Combines Growth Factor 1.0 and 2.0
- Excludes friction costs (trading costs, foreign exchange, dividends, etc)

A new portfolio was created with the new data from each poll. The breakdown of each portfolio vs the S&P500 is below:

Lepere Analytics performance								Total
	30/4/08 30/9/08	30/9/08 30/4/09	30/4/09 31/3/10	31/7/09 31/3/10	31/3/10 30/6/10	30/6/10 30/9/10	30/9/10 31/12/10	30/4/08 31/12/10
Halpern Associates	5.2%	6.8%	4.1%	7.7%	1.7%	5.9%	N/A	35.1%
S&P 500	-15.8%	-25.2%	13.1%	18.4%	-11.9%	10.7%	10.2%	-9.2%

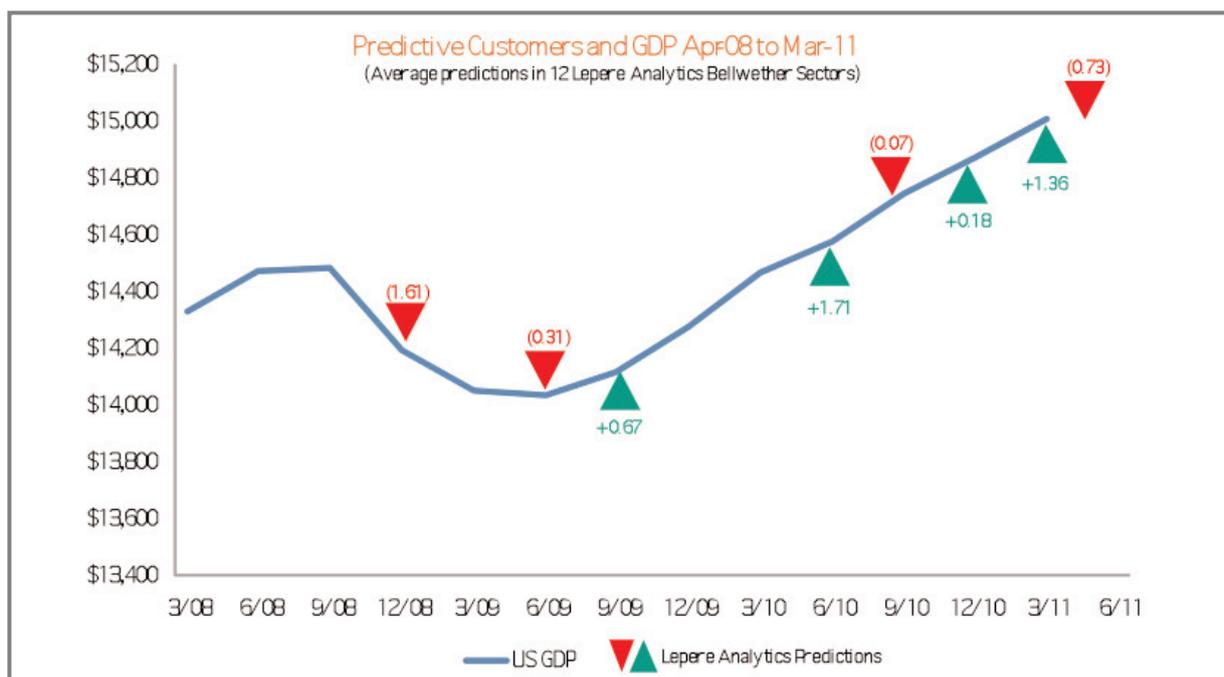
As noted above, this Halpern test combines two different methods of calculating the Growth Factor. It appears that version 1 performs better but both results are included because they point to the veracity of brand momentum as the underlying data behind the Growth Factor as a significant factor in selecting stocks.

5. GDP forecasts

Investors buy companies but consumers buy brands. Lepere Analytics bridges this gap by predicting brand momentum in consumer defined sectors and subsectors, rather than industry defined or GICS sectors. The aim is to create the real world trade-offs facing consumers in their buying decisions.

The Mar-11 study measured the momentum of 1066 brands in 95 consumer subsectors, covering 405 companies in total. Of the 95 consumer subsectors 12 have been identified as Bellwether predictors of the US economy as measured by GDP.

Sector momentum is the average of all brands in a sector. The change in sector momentum, from one study to the next, is then calculated. These sector results are then aggregated to create an overall prediction, which is remarkably accurate in predicting GDP.



Contributors

Columbia Business School – Dr Joseph Plummer, Adjunct Professor

Lepere Analytics Ltd – Marc Lepere, Chairman & CEO; Holly Stark, COO; Avantha Seresinghe CFA, Equity Analyst

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