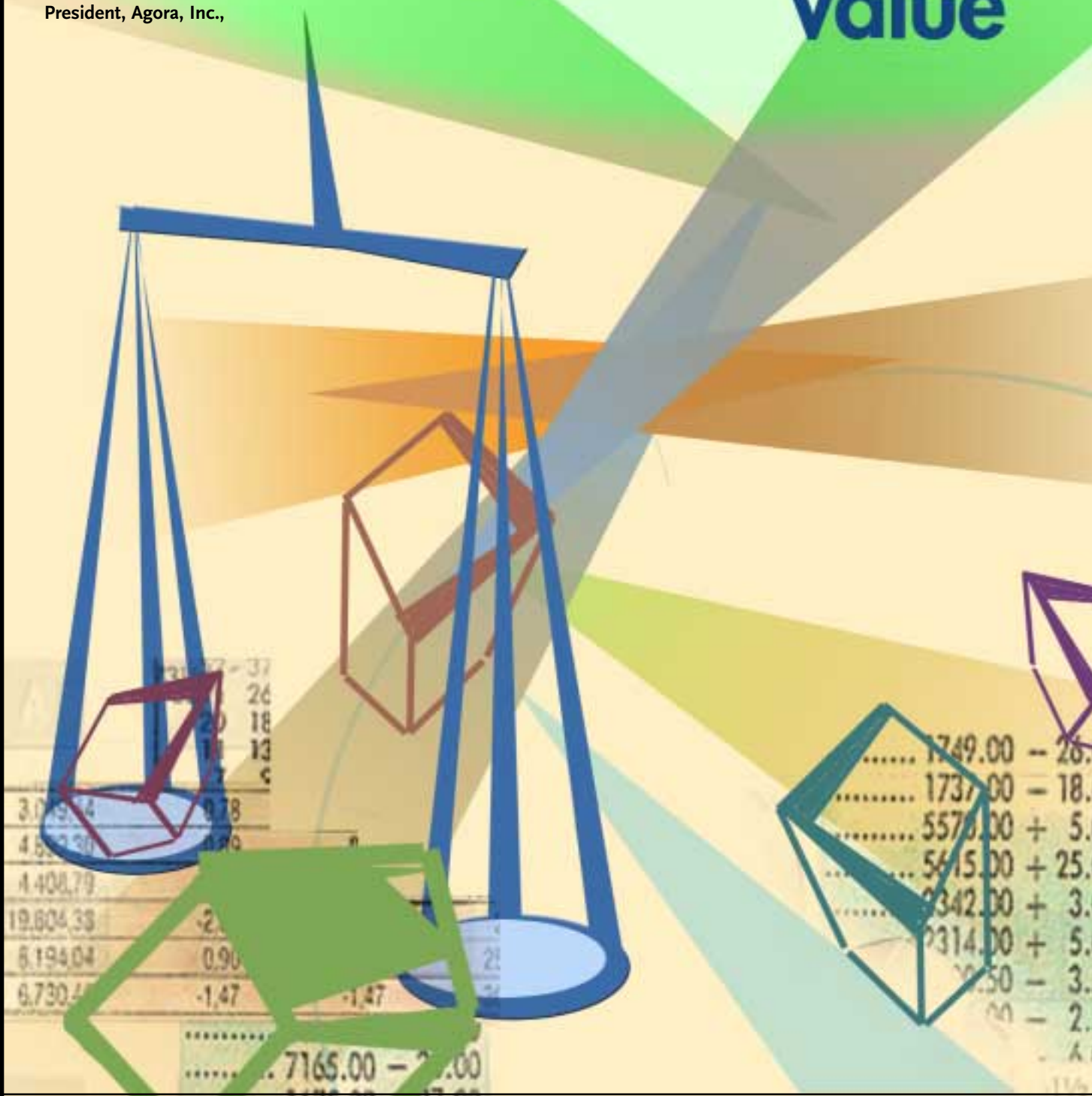


Measuring & Managing Brand Value

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Every marketer instinctively knows his or her brand is valuable. But, how much? Financially? When confronted by three basic senior management brand investment questions:

1. How much should we invest in our brand?
2. What will we get back?
3. Over what period of time?

marketers are hard put to provide answers.

In truth, few organizations know the financial value of their brand(s). Those who do generally have learned through a purchase price paid or asked in some sort of merger or acquisition activity. So, the only time brand value is known is during ownership transfer. Even then, the buying or selling price may not be an accurate indication of actual brand value for an on-going business, as some value may be carried through that most nebulous financial term, “goodwill.”

Historically, attempts to measure brand value have focused on communication delivery and attitudinal changes among consumers—brand awareness, brand recognition, perceived product or service differentiation, intent to purchase—none of them financial. So, when asked to justify a proposed brand marketing or communication expenditure, marketing managers have had difficulty building any defensible financial case for investment or returns.

Why Financial Brand Value Is Important

Knowing the financial value of a brand is one of the most important things an organization should know. Brands are corporate assets just like other tangible items the organization owns. And brands have an actual marketplace financial value—that is, their value can increase or decrease. They can be leveraged to build shareholder value. They build and maintain future corporate income flows. In short, the brand, while not tangible material, is a corporate asset just as is a plant, factory, finished inventory or raw materials. Brands should be managed in the same way.

When the financial value of the brand is determined through accepted financial approaches, senior managers are often surprised to learn they are one of the most important and valuable assets the organization controls. They often outrank many of the more tangible, traditional assets carried on the balance sheet.

Viewing the brand as a corporate asset changes the organization’s understanding of brand value. But to treat the brand as an asset, some type of financial valuation is necessary. If the brand value is unknown or simply nebulous, managers can’t possibly determine whether a brand investment is a rational use of finite corporate resources. Unless the manager can determine whether invested resources are increasing brand value or not, any corporate investment in the brand is hazardous at best. Yet organizations around the world continue to invest millions of dollars chasing that elusive goal of increasing brand equity or shareholder value. In today’s economic climate, investments made without some estimate of return are managerial suicide.

Why Measuring Brand Value Has Been Difficult

If the brand has financial value, why hasn’t that value been measured or estimated in the past? The blame can be laid at the feet of the marketing communication community. In the early 1960s, the advertising industry, increasingly being challenged to prove the financial value of their activities, took the easy way out. Rather than attempting to connect financial investments being made to financial returns, they simply avoided the subject. Instead, they proposed the measurement of “communication effects,” that is, consumer attitudinal changes measured as a result of planned communication programs. Using a “Hierarchy of Effects” theoretical model that relates consumer attitudinal change (i.e., movements up a ladder of awareness to knowledge to preference and so on), leading up to, but not including, the consumer’s actual purchase behavior, communication managers successfully deflected connecting financial investments to financial returns. They convinced the industry to accept changes in consumer attitudes as the key advertising measure, arguing consumer attitude change would eventually lead to consumer behavioral change, i.e., product purchase. The problem: no direct link has ever been provided.

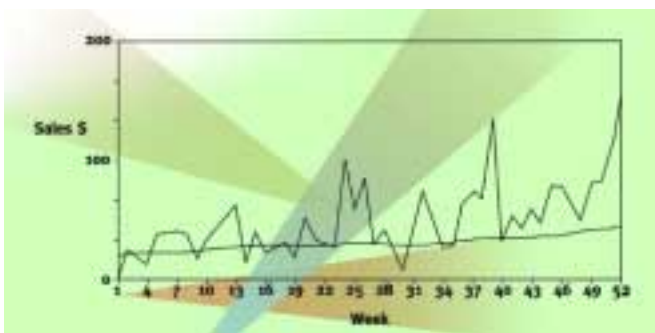
Cover Story

Brand valuation, taking its cue from the advertising industry, accepted the same premise: attitudinal measures equal brand value. Thus, today, primary measures of brand value continue to be attitudinal, such as consumer brand awareness, brand differentiation, brand bonding and the like. While interesting and helpful to communication managers attempting to create advertising or promotion campaigns, they are of limited value to the financial manager whose interest is the simple equation: dollars out on brand investments, dollars back in as a result.

A Financial Answer to the Brand Value Question

Two factors make financial brand valuation possible today. One is the development of more sophisticated financial concepts such as Activity Based Costing (ABC), Discounted Cash Flows (DCF) and EVA (Economic Value Added). The other is the increasing availability of point-of-sale or marketer-captured consumer data showing actual household marketplace purchases over time. When consumer behavior data is coupled with channel variables such as pricing, distribution, promotion and the like, financial brand value can emerge. By statistically decomposing consumer sales data, the returns on various marketing investments can be determined over time. One such analysis is illustrated below.

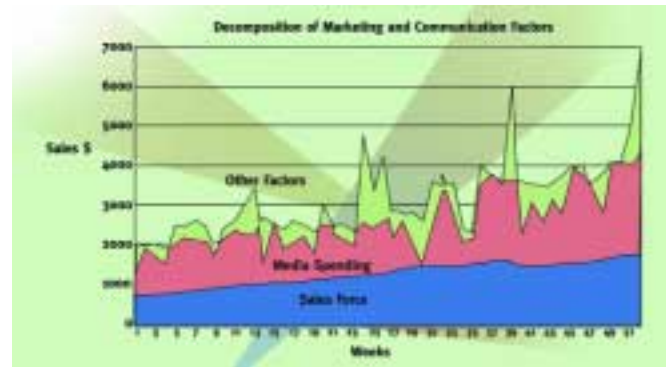
Chart 1
Units by Week
Actual versus Smoothed Data



Using historical sales data, a smoothed long-term brand sales trend line can be created [See Chart 1]. From that, incremental sales—sales over and above that expected—can be determined. Those incremental sales are generally the result of identifiable brand marketing or promotional activities. Incremental sales can account for a large or small proportion of total brand sales depending on the category, the competition, marketing activities and other factors.

Chart 2 shows incremental sales that have been parsed out into the causal promotional elements. Here, the effects of the sales force, media and other marketing factors can be seen.

Chart 2
Decomposition



This type of short-term, financial analysis of marketing activity results is now fairly common among sophisticated consumer product firms. While helpful in understanding ROI of various brand marketing initiatives, it does little to explain the financial value of the brand. Recall, the above analysis determines the return on discretionary marketing dollars spent in the short term. It says nothing about the on-going value of the brand such as returns that come from customer loyalty. A somewhat different approach is needed.

Getting to the Heart of Brand Value

In most boardrooms, only two things count: cash flow and shareholder value. Both are commonly discounted to net present value. Therefore, if managers can't relate their investments to one of these yardsticks, they have little claim to the use of finite corporate resources. Yet if the brand is an asset, and that asset can demonstrate growth potential over time, the current and on-going brand financial value becomes a critical ingredient in profitably managing the firm.

To determine brand value, a similar approach to the previous examples is used, by creating a smoothed long-term sales trend line. But instead of analyzing incremental sales, the challenge is to get at ongoing volume—what we call “organizational momentum volume” [See Chart 3].

Chart 3
Identifying Brand Equity



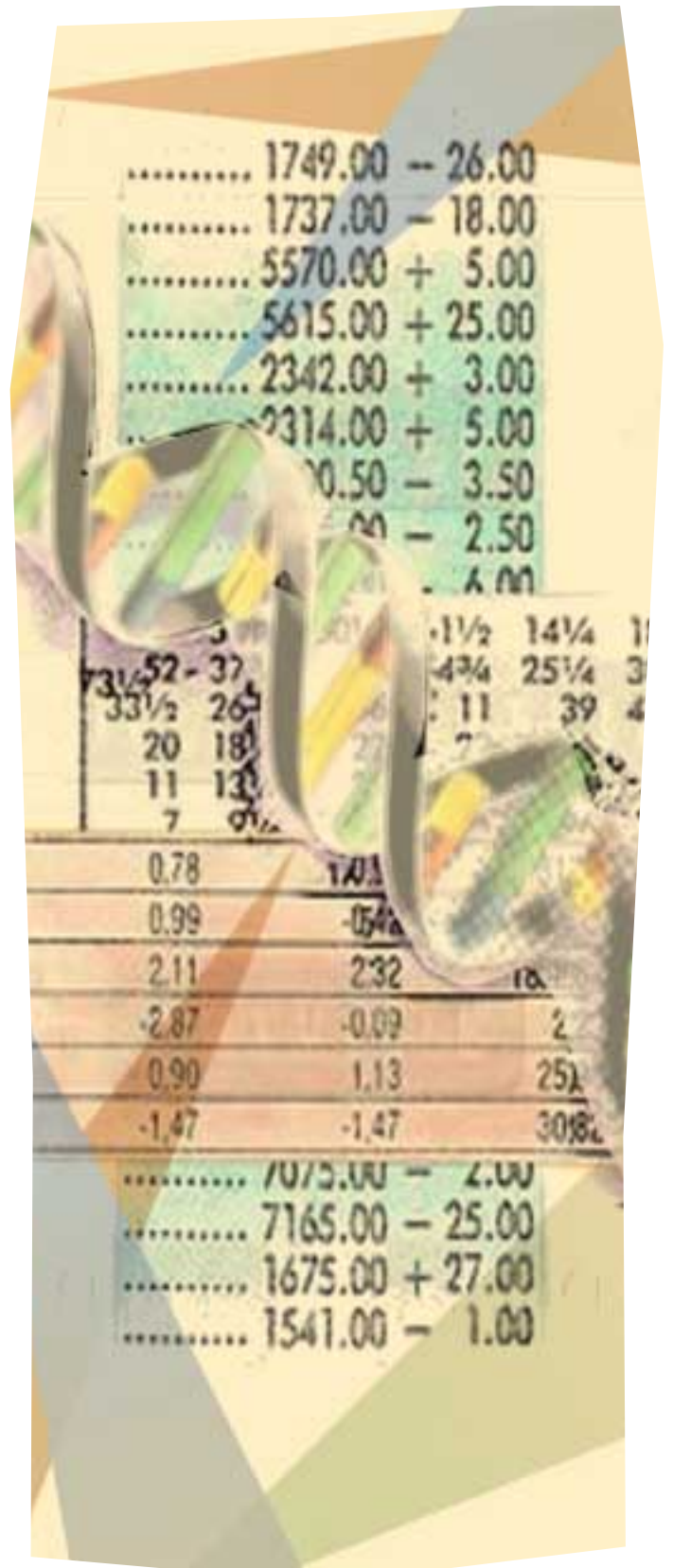
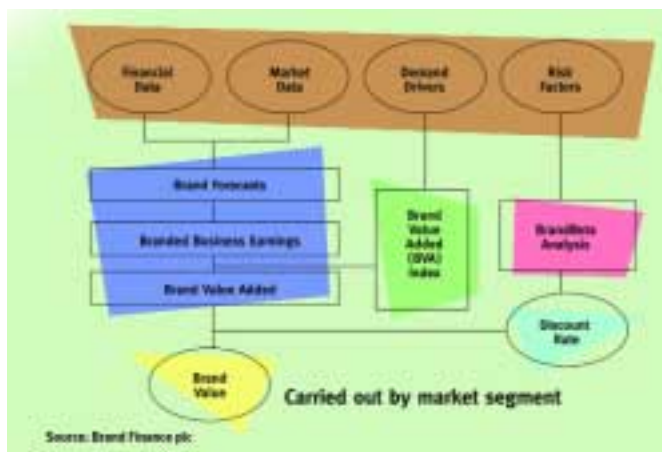
The ongoing, or “momentum volume” for many consumer product brands accounts for sixty to seventy percent or more of total brand sales. In other words, incremental sales are a minority.

A brand’s “momentum volume” consists of several things: product or service, quality, competitive set, pricing, service factors and, of course, brand value. The challenge is to parse out brand value to determine its financial worth compared to other factors.

The Brand Finance Process for Determining Brand Financial Value

Brand Finance, headquartered in London, with offices in the U.S., Australia, and Singapore, has developed a brand valuation methodology. An example of the methodology can be seen from the discounted cash flow statement below [See Chart 4].

Chart 4
Brand Finance Valuation Approach



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The process includes three basic elements:

1. A calculation to determine Branded Business Earnings. Separating earnings directly attributable to the brand.
2. Demand Drivers. Elements that contribute to the on-going purchase behavior of brand customers over time. Factors may include customer type, channel propensity, price involvement and others. This results in the Brand Value Added, or BVA, Index.
3. Risk Factors. Factors that determine how much confidence the brand valuator can place on historical data as being projectable into the future. Called the BrandBeta Analysis, it identifies the discount rate used to calculate net present value.

A Discounted Cash Flow chart for a hypothetical brand illustrates the process [See Chart 5].

Chart 5
Discounted Future Earnings Method

Simplified Example	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Net Sales	500	520	550	580	620	650
Operating Earnings	a 75.0	78.0	82.5	87.0	93.0	97.5
Tangible Capital employed	250	260	275	290	310	325
Charge for Capital @ 5%	b 12.5	13.0	13.8	14.5	15.5	16.3
Intangible Earnings	c 62.5	65.0	68.8	72.5	77.5	81.3
Brand Earnings @ 75%	d 46.9	48.8	51.6	54.4	58.1	60.9
Tax Rate	33%	33%	33%	33%	33%	33%
Tax	15.5	16.1	17.0	17.9	19.2	20.1
Post Tax Brand Earnings	e 31.4	32.7	34.5	36.4	38.9	40.8
Discount Rate	15%					
Discount Factor	f 1.0	1.15	1.32	1.52	1.75	2.01
Discounted Cash-flow	g 31.4	28.4	26.1	24.0	22.3	20.3
Value to Year 5	h 152.4					
Annuity	i 135.3					
Growth	0%					
Brand Value	287.8					

We start with Year 0 when Net Sales for the brand were \$500 million [Line a]. Sales are estimated to increase by four percent per year for the next five years.

Operating Earnings for the brand from internal records amounted to \$75 million [Line b].

From company records, it is determined that the Tangible Capital employed in making the product was \$250 million. A Charge for Capital from the Brand Earnings of 5 percent or \$12.5 million is deducted, leaving Intangible Earnings of \$62.5 million [Line c].

In Step Two, using the Demand Drivers from the Brand Value Added, or BVA, Index, brand earnings of 75 percent of the Intangible Earnings, or \$46.9 million, are determined [Line d].

The two charts below demonstrate how the BVA index works. Chart 6 shows an example of elements included in the BVA Index, while Chart 7 illustrates the results of a BVA analysis for a chocolate bar.

Chart 6
Hypothetical drivers of demand

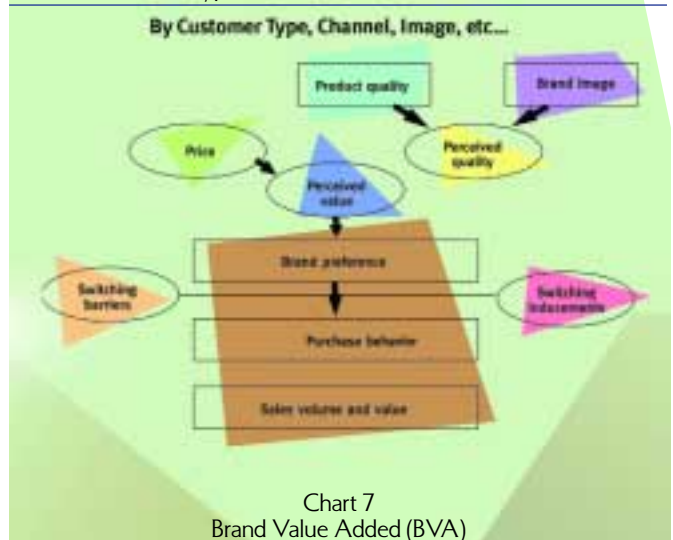
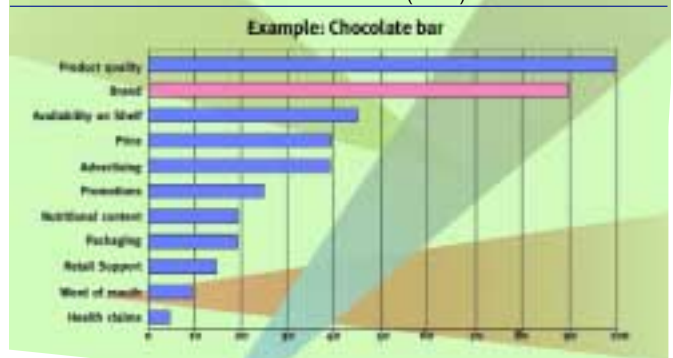


Chart 7
Brand Value Added (BVA)





Estimated Tax at the rate of 33 percent or Tax of \$15.5 million is deducted. This results in Post Tax Brand Earnings of \$31.4 million [Line e].

The Risk Factors facing future brand earnings are found through the Brand Beta Analysis. That provides the discount rate for future earnings of 15 percent in this example. The Discount Factor is applied to estimated future sales [Line f] to calculate the Discounted Cash-Flow [Line g] extensions.

By adding up the Discounted Cash-Flows for the next five years, the Brand Value to Year 5 is determined as \$152.4 million. The Annuity for the brand beyond the five year period is calculated as \$135.3 million [Line i]. Since we are using constant dollars, no Growth figure is included.

The final result is the total Brand Value of \$287.8 million.

The Real Value of Brand Valuation

To this point, many brand managers may find little value other than bragging rights. That is how brand valuation has historically been used. We take a different view.

Knowing the brand above has a value of nearly \$300 million provides the management with very critical information:

1. Investing in a \$287 million asset is much different than investing in a brand with 85 percent consumer awareness. It provides a managerial benchmark against which investments can be measured versus other uses of the organization's finite resources.

2. By determining the brand's value, a management benchmarking system can be developed, i.e., a "brand value dashboard" showing investments and returns. Thus, management can see whether brand investments meet the firm's required internal rates of return.
3. Brand managers have a better understanding of which brand activities work and which do not. By tracking investment levels and then relating those to the various initiatives, a closed-loop system of brand investment, measurement and re-investment can be developed and monitored.

A knowledge of brand value is worth the use managers make of the data. Being able to treat the brand as a corporate asset has great value to many firms since it allows managers to monitor their financial investments and returns. Today, the capability to measure current and on-going value of a brand is not only possible, it is practical as well. Given the attention senior management increasingly pays to corporate assets, it is only good business sense that the brand should be treated in the same way. **C**

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