BRANDTAXI | Insights

Brand Valuation – Leveraging Brand Value to Increase Revenue, Lower Cost, and Reduce Risk

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Brands have value, sometimes quite a bit. There are ways to measure and leverage this value to grow business. In the last two decades, there has been significant work in refining methodologies to both measure brand value, and then use it as a proactive business tool to benefit businesses. This paper will describe the methodologies and applications so that business leaders can determine if brand valuation has application to their organization.

What is Brand Value?

Brand value measures the economic asset value of a company or product brand. It details how much of the company's operating income and free cash flow is derived from the brand, the influence of the brand within each consumer purchase decision driver, and the associated brand risks.

By linking the brand to the economics of the business at a detailed level, brand value opens the door to a number of useful applications. Brand Valuation can answer questions and help business leaders move a franchise forward. Some typical questions include:

- How can I **prove that branding offers real value** to the CEO, CFO, and the Board?
- How can I **justify a proposed marketing budget**?
- How should we **optimize the marketing budget** across the brand portfolio? What else can brand value tell us that will make our marketing investment as efficient and effective as possible?
- How can we **align the commercial organization** around a metric that ties better to financial performance?
- How can we use brand value knowledge to **evaluate acquisition opportunities**? Is the acquisition brand gaining value or in decline?
- What is the **optimal royalty rate** for a licensing opportunity? For a co-branding opportunity? For an ingredient branding opportunity? For a non-profit co-marketing opportunity? How do we grow this revenue stream?
- In evaluating joint venture and partner relationships how can we **optimize the brand relationship** to capture the maximum value?
- In our selling process, how can we **best tell our brand story** with a better economic fact base to win more business?
- How can we use purchase driver insights from the Brand Valuation methodology to **focus investments**? Drive innovation initiatives?
- How can we use our brand heritage and value to **drive higher prices**?
- Given that brand drives earnings and therefore taxes, how can we **leverage brand value to lower taxes**?
- How can leverage brand value insight to retain the current employee base and **reduce turnover**?
- How do we **quantify the damage** to our brand in legal defense?

Brand valuation, as a methodology, has historically helped articulate the value of branding in many different types of business situations:

- Household brands like Apple and Coca-Cola are worth more than $50+ billion as an asset. Companies now understand that brands can contribute anywhere from 30-70% of a company's market capitalization.
- There are also over 200 brands that offer economic value exceeding $1 billion, including well-known companies like Google, McDonald's, Tiffany's, BMW, Coach, Harley-Davidson, Starbucks, Caterpillar, and Verizon. More than that, even a small $5 million business may have $1 million in brand value that can be leveraged.
- Academic work has shown a relationship between brand value and shareholder return. Companies experiencing the largest gains in brand equity saw their shareholder return average 30 percent; conversely those firms with the largest losses in brand equity experienced stock return average a negative 10 percent. Another study has shown that a portfolio of high brand value companies outperformed a total stock market index by a wide margin (23% per annum versus 16%) throughout most of the 1990's, and at a lower risk profile.

Calculating Brand Value

There are three types of calculations; Market-based, Cost-based, and Income-based.

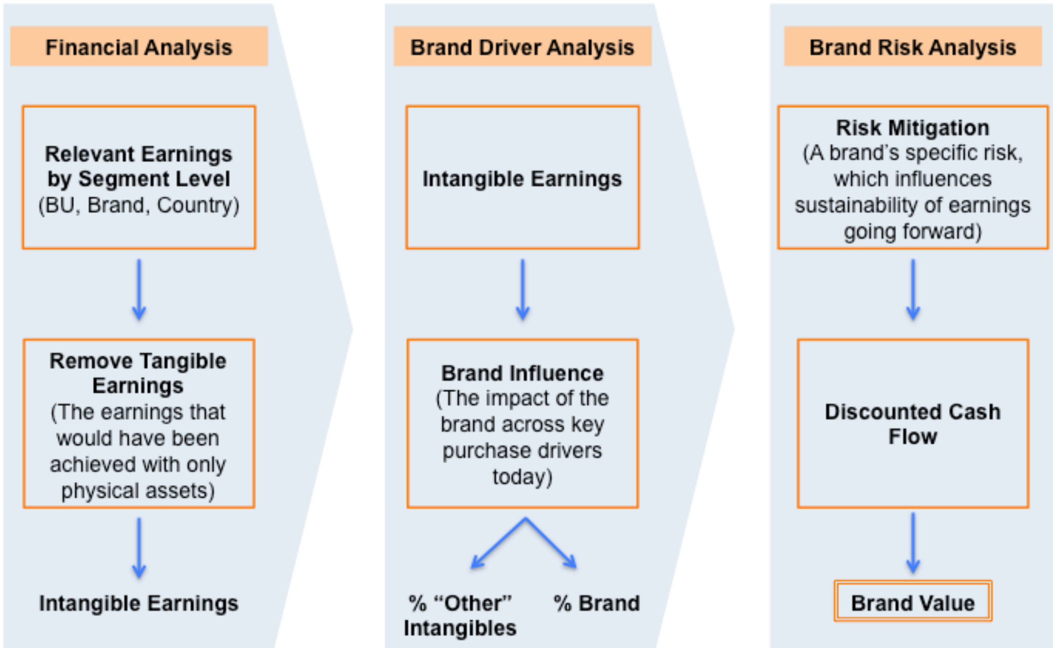
- **Market-based valuations** look at comparable market, company or stock transactions. If these transactions are readily available it might be possible to estimate one brand's value by comparison with the value of another comparable brand – a rare situation.
- **Cost-based valuations** assume it is possible to value a brand on the basis of what it costs to build or what it might cost to re-create. Unfortunately, past "cost to build" is not a guide to current value. And, by definition, unique brands are not re-created easily.
- **Income-based valuations** come in two common forms; royalty-relief method and discounted cash flows (DCF).
    - The **Royalty-relief** method assumes that a business does not own the brand and therefore needs to license from someone else. If a brand has to be licensed from a third-party, a royalty rate will be charged for the privilege of using the brand. In contrast, ownership of the brand relieves the business from paying a royalty rate. While occasionally seen in legal cases, the royalty-relief method can prove difficult because it is dependent on finding comparable royalty rates and the details behind their calculations.
    - **Discounted cash flow**. This method looks at free cash flow generated by the business under solid assumptions and then applies an appropriate discount rate to determine the business's present value. This is the most common form of brand valuation used today.

The Discounted Cash Flow method separates analysis into three areas:

- **Financial Analysis** to isolate free cash flow
- **Brand Driver Analysis** to determine the influence of brands on that cash flow
- **Brand Risk Analysis** to discount the free cash flow based on calculated risk

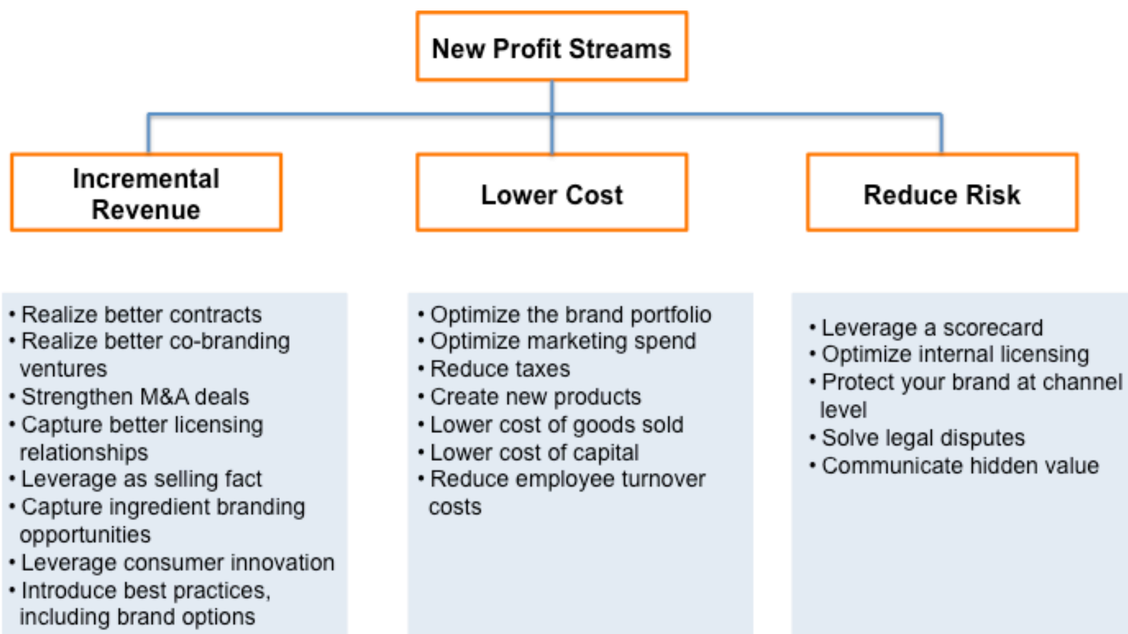
Below is a step-by-step process that results in a Brand Value that has many potential applications.

Discounted Cash Flow Brand Valuation Process



Using Brand Value Applications

There are at least twenty different proven brand valuation applications developed to date that fall into three general areas of business management decision-making; increasing revenue, lowering cost, or reducing risk. Depending on the business need, a strong brand valuation methodology can be fine-tuned to address specific challenges facing an enterprise. Most applications can be highly profitable with little or no capital investment.



Brand "Option Value" – Identifying Future Value Opportunities
Brand Valuation looks at current data to calculate value and determine optimal management tools to move a business ahead. But one real opportunity is to use valuation methodology to identify future opportunities. A brand with many avenues to future growth is undoubtedly more valuable than a brand with limited growth opportunities.

In classic finance terms, a business valuation can include "option value" in addition to the discounted cash flow valuation of the existing business. Option value relates to quantifying the value of future choices. For example, if a company has a plant in Asia that was built with regulatory approval, it may own barriers to entry versus its competitors. As a result, it may have access to additional product revenues with little competition. So focusing on Brand Option Value can identify ways to optimize and grow a business from the perspective of the brand. This becomes a powerful lens for growth.

Another example of this is Apple. Their continuing expansion has also fueled greater options for growth. When they initially moved from computers into music via iTunes and the iPod, this gave their brand greater stretch and consumer permission. This momentum continues to drive them into new territories of value. Along the way, they have locked in attractive raw material pricing, lower manufacturing costs, higher levels of customer service capabilities, etc., and often cornered the market in new technologies. Think about the iPhone, iPad, iCloud as new foundations. So Brand Option Value can be an organic tool for focusing growth. Today, Apple has many options beyond computers.

Brand Valuation, as a formal business tool, can help companies plan, optimize and navigate their future. By identifying incremental revenue opportunities, or ways to lower cost and reduce risk, companies can move forward with greater certainty and clearer direction.

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