PERSPECTIVE

Value creation through brands

Over the years, there's been a tectonic shift in the source of value creation in enterprises. Today, brands have become a key component of corporate sustainability, says **Unni Krishnan**

Across a wide range of industry sectors, it is companies that are adept at developing and managing brand and intangible asset value that reap sustainable and superior rewards. Contrary to conventional orthodoxies, these potent business assets exert their economic influence not only in traditional packaged goods companies but also in the case of IT, consumer durables, cement and steel, luxury hotels and banking sectors.

Over the years, there has been a dramatic shift in the source of value creation — from tangible assets (such as property, plant, equipment and inventory) to intangible assets (such as brands, stakeholder relationships, IP, skilled employees, corporate culture, etc) that don't show up on the balance sheets.

Consequently, brands and related intangible assets make up a large part of the value of many successful companies. Yet, barring a few honourable exceptions, managing these precious assets remains more a dark art based on guesswork and hunches, deficient of a disciplined framework which the board or senior management can access and debate in an objective way. Most senior executive team members realise this, although many still do not appreciate the financial significance of getting it right. It is hardly surprising that many senior leaders grappling with brand and customer value issues have found the experience frustrating.

Yet, in today's economic scenario, brand and intangible values cannot be left unaccounted for as they profoundly bear upon the very destiny and survival of a firm.

Why do brands count?

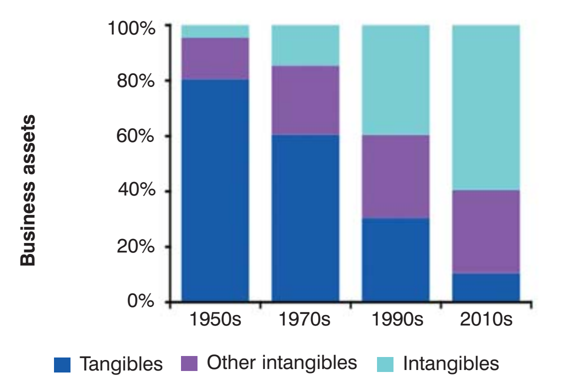
Words such as 'marketing' and 'brand' have been misused and misunderstood, sometimes conjuring up non-positive associations such as image, perception, or worse, pulling a fast one on the customer.

But the reality is that brands stand for a much bigger and sophisticated world of dynamic applications. Brand value in economic terms represents real capital because it enables firms to maintain long-term relationships with customers and various stakeholders. The concept of added value is the very basis of the capitalist system, and in the developed world it forms the bulwark of wealth creation capability.

Brand Finance's Global Intangible Finance Tracker (GIFT™) (tracking across 53 national stock markets and covering more than 37,000 companies) shows that brands add to a third of the world's wealth (see Figure 1).

Like it or not, brands have become a principal economic lever of companies across sectors. In this more holistic and intelligent sense, brands act as a shorthand of business strategy and as the glue which holds all functions together to deliver customer value and secure future earnings (see Figure 2).

Figure 1: Value you can't see



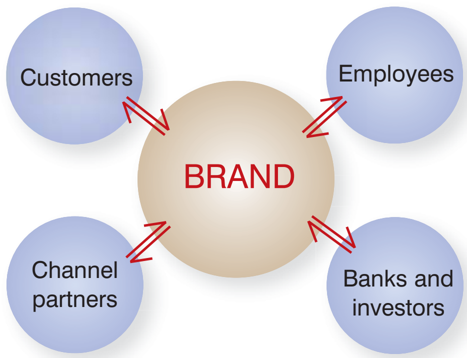
Based on Brand Finance Global Intangible Tracker Research

The brand is the single unbroken red thread which runs through all functions and stakeholders. There is an economic reward / penalty that every firm enjoys or pays by objectively managing it. Unfortunately, due to the narrow definition of marketing / brand today, there is no formal mechanism to connect the pieces of the jigsaw, check for internal alignment to the brand and stress test its full value creation potential.

The challenge of managing brands for value

Most managers 'feel' that they need to act on brands and intangible assets, and many have an intuitive sense of 'what' companies need to do to leverage value

Figure 2: Pivot of dynamic value exchange



from these potent assets. However, few appreciate the huge organisational barriers that prevent them from purposeful action and nimbleness to do so.

Behind each brand valuation we conducted over the last 14 years, we found that the shared hinge assumptions of the senior executive team about the future economic impact of brand and customer assets are dangerously incorrect. They are often unaware of the scale of economic consequences and drifting into an 'inflection point' — a moment of great opportunity as well as high risk to corporate sustainability.

The challenge to the senior executive teams is to demonstrate that brands are business assets capable of generating superior economic returns for their owners and worthy of multi-year investment commitments in new product development, R&D and people.

One major reason why even senior managers do not, as a rule, understand this fact is their mistaken identification of conventional accounting data and financial analysis with brand and intangible value economics and business impact analysis.

Brand Finance's global experience shows that a large majority of the 3,000 branded businesses studied in depth in India and across the world are overbalanced towards short-term firefighting priorities because they have little or no visibility into directing costs or investments into future value-producing activities driven by brands and intangible assets. Instead they tend to drift into 'nothing producing' activities and fail to realise it until it is often too late.

Real information for wealth creation from brands

Enterprises are paid to create wealth from business assets, not simply control costs. But that obvious fact is not reflected in financial and MIS systems available.

Due to the legacy of past practices from the tangible-asset-heavy era, information required to make informed judgments about how brands, customers and employees add economic value remains hazy at best.

Our experience across a wide range of companies shows that transparency of information to gain visibility into brand and customer value economics can be significantly improved and requires three sets of diagnostic tools:

Foundational information: This is basic information pertaining to brands / products / stock keeping units (SKUs) / services / customer segments / key accounts to construct a true and comprehensive financial position of the economic value creating unit.

Productivity information: This is the business output information derived from foundational information across brands / products / SKUs / services / customer segments / key accounts.

Resource allocation sensitivity: This acts as a decision-making tool for allocation of precious resources, with better clarity as to where the future value is resident in brands / products / SKUs / services / customer segments / key accounts.

This kind of an in-depth granular analysis of brand and intangible asset economics, which conducts a pressure test on future earnings of the branded business, can be applied in any business across sectors from B2C to B2B. The following points will reveal more about them in an objective value-based manner:

- Visibility into which brands / products / SKUs / services / customer segments / key accounts are generating economic profit / loss and the reasons for this.
- Analysis of whether or not a particular brand / product / SKU / service / customer segment / key account is performing as per market opportunities on a defined set of parameters to assess return on investments.
- Generation of strategic scenarios to visualise whether brands / products / SKUs / services / customer segments / key accounts will deliver full potential value if resource allocation composition and magnitude are recalibrated.
- Determination of what will be the overall impact from releasing the full potential of brands / products / SKUs / services / customer segments / key accounts on the company's performance as a whole.
- Identifying the resource allocation framework that is most sensitive towards the hidden potential across brands / products / SKUs / services / customer segments / key accounts.

A framework for demonstrating the value of brands and intangible assets

Our analysis of why so many of today's iconic

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branded businesses have hit an inflection point and suddenly fractured in value provides the basis of the framework below. The most common factors are failure of the senior executive team's direction and sheer inertia of action. The reason: shared mental models of the senior executive team, which have hardened and not adapted to new market and strategic realities.

Step 1: Understand management's strategic assumptions — Branded Business Hinge Assumptions (BHA®):

The first step is therefore to unearth and stress test the strategic assumptions visualised by the senior executive team about the future of their branded business, customer segments, pricing, channel strategy, alignment of people and other key variables. Brand Finance conducts an internal expedition to identify the firm's most deeply held assumptions about itself, the markets it operates in and the customers it serves to generate long-term value for the branded business.

Step 2: Pressure test BHA™ and identify Brand Value Added (BVA®) drivers:

Brand Finance puts these strategic assumptions under a microscope and conducts a pressure test on each of them from a bottom-up and outside-in perspective, to check if the strategic assumptions of the senior executive team are in line with market opportunities, value chain sensitivity, customer experience expectations and competition dynamics. This is supported by factual analysis so that an objective set of cause-effect relationship factors can be arrived at.

Specific drivers would be identified, which can turn the firm's blind spots in the market, customer, product, pricing and service opportunity area into value-creating zones with attached risk and reward scenarios.

These drivers, called BVA drivers, act as credible, timely, challenge mechanisms that can make the senior executive team aware of economic risks / opportunities when their closely held assumptions are under duress.

Step 3: Estimation of sustainability of market performance in the form of Brand Beta® metrics:

The outside-in BVA review can be distilled into a focused set of market and customer metrics that will determine the strength of the branded business in the market place, which will show improvements when there is a discipline in execution behind each BVA driver. These are highly specific to a branded business and need to be urgently monitored for sustainable business performance.

Lack of improvement in these factors / metrics over two consecutive quarters should immediately raise a red flag at the board level. These Brand Beta factors are extremely useful to carry out dipstick assessments and to calibrate progress of BVA driver execution or its relapse into the orthodoxy of management hinge assumptions.

Step 4: Brand value governance:

Brand valuation is able to articulate these future scenarios and their drivers in a holistic and objective manner with economic rewards / penalties attached to them. Often, it is only when the full scale of economic opportunity at stake is completely understood and internalised that organisational functions galvanise around the customer and brand value axis.

Our view is that boards need to have a deep engagement with these brand valuation scenarios. Their deepest responsibility is to ensure that the company's most valuable assets are held together by a coherent, well-tested, outside-in strategy.

The next most important responsibility is to ensure that performance management systems and compensation for the senior executive team are aligned to the long-term sustainable value of the business, rather than just short-term financial results.

Boards are inescapably about risk management, and the risk to brand, customer and stakeholder value should surely rise to the top of their agenda. Locating the stewardship of these precious assets to secure corporate sustainability of India's finest companies cannot and should not be postponed.

Unni Krishnan is a management consultant focused on brand and customer-value-led business designs. He is the creator of brand value governance frameworks for corporate sustainability, an integrative discipline encouraging senior teams to find a point of balance between delivering today as well as creating tomorrow.