IMPACT OF BRAND ACCOUNTING ON CORPORATE PROFITABILITY

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ABSTRACT

The objective of this paper is to explore the impact of brand accounting on corporate profitability. The objectives includes: to examine how lack of uniformity in brand valuation technique affects corporate profitability, examine how brand accounting increases corporate profitability. Secondary sources were used in obtaining information, it was realized that brand accounting attracts better quality employees, pay less to retain these employees and require fewer incentives to motivate these employees, helping the corporate firms to increase their profit. It concludes that management will inevitably need to install more value based brand management and accounting system that can align the management of the brand assets and provide more reliable indicators on contribution of brand to the overall business performance.

Introduction

Brand Accounting was first pushed to limelight in 1988, when Ranks Hovis McDoughali (RHM) company employed the valuation services of interbrand Plc to value and incorporate the company's brand assets in the balance sheet in the attempt to fight a hostile takeover bid (Ramalyer, Kalyanasun drama and Bumani 2009). In accounting, a brand is defined as an intangible asset. It is often the most valuable asset on a corporate balance sheet. Brand owners manage their brands carefully to create shareholder value, and brand valuation is an important management technique that ascribes money value to a brand and allows marketing investment to be managed (e.g prioritized across a portfolio of brands) to maximize shareholders' value.

According to London Business School (LBS 2015), researches conducted on brand valuation accounting demonstrates that organizations with strong brand or intangible assets are able to attract better quality employees, pay less to retain these employees and require fewer incentives to motivate their employees. The incorporation of brand as an asset in the balance sheet gives rise to the concept of brand equity. This emerging view stems from the recognition of the strong role of brands in driving benefits to the organization bottom line (Ramalyer et al 2009). Aaker (1991) defines brand equity as "a set of brand assets and liabilities linked to a brand, its name and symbol, that adds to detract from the value provided by a product or services to a firm and/or to the firm's customers.

Accounting, on the other hand, is the information system that measures business activities, processes that information system into reports, and communicates the results to decision makers (Horngren 2002). Brand accounting is then "an information system that measures brand equity, process and incorporate it into financial reports and communicates these values to the users of accounting information (Ramalyer et al 2009). Accounting for brand has economic value in a company's shareholders value which is most viable when companies are being bought or sold.

Feldwick (1996) simplifies the variety approaches by providing a classification of the different meanings of brand equity as “the total value of a brand as a separable asset when it is sold or included on a balance sheet”, ‘‘a measure of the strength of consumers’ attachment to a brand”, a description of the association and beliefs the consumers has about the brand”. With the current trend in globalization and technological advances, it is believed that intangible assets like intellectual capital, knowledge systems, patent, registered designs, brand assets and trademark will enable more services to be provided to make more profit than required to the organizations and are going to be the key drivers to market capitalization in the twenty first century (Ramalyer 2009).

Due to the increased importance of brand as assets in business organization, there is a growing trend of business organization initiating the valuation of their brands for internal or external reporting purposes. The problem of brand accounting on corporate profitability is identified as lack of uniformity in the brand valuation techniques which causes inefficient valuation of brand assets and reduces the usefulness of brand accounting information. Inconsistent and insufficient accounting regulations guide and govern the full disclosure of quality information on brand assets in accounting report.

REVIEW OF RELATED LITERATURE

WHAT IS A BRAND?

There are yet no standard definitions of a brand for accounting purposes. It seems to be generally accepted that a brand is a recognized name, such that consumers perceive that the related product is preferable to other similar products (Campbell 2010). That perception provides a competitive advantage to the owner of the brand, allowing the owner to charge a premium price for the product.

However, a brand is often more than just a name of the product. A brand may also include the know-how that is needed to create the product. Brands are used in business, marketing and advertising. In accounting, a brand is defined as an intangible asset or is often the most valuable asset on a corporation’s balance sheet. Brand owners manage their brands carefully to create shareholders value and brand valuation is an important management technique that ascribes a money value to a brand, and allows marketing investment to be managed to maximize shareholder value. Although, only acquired brand appears on a company’s balance sheet, the notion of putting a value on brand forces marketing leaders to be focused on long term stewardship of the brand and managing for value (Wikipedia 2015).

The word “brand” is often used as metonym referring to the company that is strongly identified with a brand. Investopedia (2013), also asserts that brand is the personality that identifies a product services or company (name, term, sign, symbol, design or combination of term) and how it relates to key constituencies: customers, staff partners, investors etc.

WHY ACCOUNT FOR BRANDS?

Campbell (2010), posits that the key reasons why companies might choose to account for brands are summarized below.

i. Several companies have included brand valuation in their balance sheet in apparent responses to the threat of a hostile takeover bid. Accounting for brands is perceived as strengthening a company's balance sheet, thus making it more able to bend off unwanted sectors. In an active corporate scene, acquisitive companies and their advises are constantly seeking "undervalued" element in the target company, either by achieving a relatively high annual return on capital employed or by selling off component parts of the business. In these circumstances, management of a potential target company may consider that it's share price is too low because it does not fully reflect the value of the company's brands. Consequently, management has an incentive to account for brands in an attempt to increase the share price and therefore deter would be predators. This approach relies on the implicit assumptions that the market does not attribute and appropriate value to a company's brand unless these brands incorporated into its balance sheet (Aaker 2009).

ii. An acquisitive company may have a similar incentive to account for its own brands in an attempt to increase its share price. The company can then use it's more highly – related shares to finance a paper-for-paper acquisition, rather than using hard cash to finance the deal.

iii. Another reason for accounting for brands is to increase a company's borrowing powers, within any existing constraints imposed by its articles of association or by it's providers of loan capital. A company borrowing power may be restricted by reference to its level of debt in relation to its share capital and reserves. Accounting for brands may increase reserves and so many allow a company to increase its borrowing (Campbell, 2010).

iv. By accounting for brands a listed company may not need to seek shareholders' approval for certain transactions. The stock exchange requirement for shareholders' approval and for circulars to be sent to shareholders is based on certain size tests, one of which concerns the company's assets. If a company capitalizes its brands and hence increase its asset, then it may be able to execute significantly large transaction such as acquisition without the need for shareholders' approval or circulars (Keller, 2003).

v. Accounting for brands may be attractive to groups that seek to avoid high goodwill figures. By attributing fair values to brands that is acquires on the purchase of a business, a group will reduce the calculated figure of goodwill on consolidation brands can then be revalued in the balance sheet in subsequent years, whereas goodwill cannot be revalued. Consequently by accounting for brands a group retains greater flexibility in its accounting options. However, this flexibility may only be attractive, if brands are depreciated, then the effect on the profit and loss account is the same as if goodwill had been capitalized and then amortized (assuming the useful life of the brands and the goodwill are the same). If brands are revalued and then depreciated, then the charge against profits will be greater than it goodwill had been capitalized and amortized. If brands are revalued but not depreciated, then the group can strengthen its balance sheet without adversely affecting its profit (Keller, 2003).

RECOGNITION OF BRAND AS AN ASSET

The characterization of intangible or brand as asset is a necessary preliminary step leading to the examination whether brand can be recognized in the balance sheet. Brand is intangible assets. They can only be recognized if they comply with the asset definition. For that reason we firstly study the definition applying to intangible assets before dealing with question relating to the inclusion of brands in that clarification. IAS 38(Para 7), defines an intangible asset as an "identifiable, non-monetary asset without physical substance held for use in the production or supply of goods or services, for rental to others or for administrative purposes". An asset "is a resource, a controlled by enterprises as a result of past event; and (b) from which future economic benefits are expected to flow to the enterprise. The standard indicates that "enterprises frequently expand resources or incur liabilities, on the acquisition, development, maintenance or enhancement of intangible resources such as trademarks (including brand names and publishing titles). Not all intangible items meet the characteristics of an intangible asset that is identifiability, control over the resource and existence of future economic benefits.

IAS 38 requires, in that respect, that an intangible asset is indentifiable to distinguish it clearly from goodwill, which is the case if the asset is separable. Separability is given if the specific future economic benefits arising from the asset can be by renting, selling, exchanging or distributing them without also disposing of future economic benefits of other assets used in the same revenue earning activity. But it may also be possible to proof the identifiability of an asset in some other way (IAS 38, Para 11, 12). IAS 38 defines "control over a resource" as the power to dispose of the future economic benefits of the resource and to exclude other from the exploitation of these benefits. Future economic benefits may result from the siles of product or services as well as from cost saving or other benefits resulting from and use of the asset by the enterprise (IAS 38, Para 17).

BRAND EQUITY

Brand equity has been defined as "outcomes that accrue to a product with its brand name compared with those that would accrue if the same product did not have the brand name". in (Ailawadi, Leliman and Neslin 2003), i.e, the benefits a product achieves through the power of its brand name. Keller and Lehman (2003) delimit three approaches for assessing brand equity: Customer Mindset, product market and financial market. These approaches have different strength and weaknesses (Ailawadi et al 2003). Financial market measures theoretically capture current and future brand potentials; they often rely on subjective judgments or volatile measure to estimate future value (Simon and Sullivan 1993). Product maker measures are more closely related to marketing activity but don't capture future potentials (Kamakura and Russel 1993). More importantly both approaches have limited diagnostic value. Customer mindset metrics, on the other hand identify brand strength and weakness (Keller 1993). While these provide insights for strengthening brand equity, they provide little information about brand performances in term of market share or profitability.

FACTORS AFFECTING BRAND AND BRANDING

According to Brata and Home (2014), asserts that eh two main principles in branding are informing customers about the brand existence and reinforcement of brand image. One of the notions about reinforcement of brand image is the original brand personality. Brand personality is the features of brand formed by the customer. These features are; attributes benefits and situation.

Consumer and consumption images are two kinds from the four kinds of not product related feature. The other two kinds are knowledge about the price and packaging or superficial information. Consumer and consumption images allows the customer to generate reputation and features of brand personally and they are generated by direct experience or advertisement or marketing. These circumstances develop the reputation personality and the features of brand described by the customer. The main factor for choosing brand by the consumer is to understand the brand personality of the product or service considering the competitive environment. Therefore, the brands that are well established and have the desired personality have advantage in market place and draw the positive attention to customer (Batra and Home 2014). Aaker (2009), states other factor for choosing brand is reputation. Having reputable like a popular athlete makes the customers purchase the product or services. Confirming the reputation depends on the person and product. The endorser's fit is important such that a brand with a fixed personality may use it well for its interest or not. Therefore, the endorser's personality must have compliance and fit with brand.

The variable affecting the customers perception are; sponsorship, fit, brand personality, attitude towards brand, product involvement or contribution, purchase behavior, attitude towards sponsor etc.

APPROACHES TO BRAND VALUATION

For those concerned with accounting, management, mergers and acquisition brand valuation plays a key role in business today. Although financial values have to some extent always been attached to brands and to other intangible assets, it was only in the late 1980's that valuation approaches were established that help understand and assess the value of brands (Tatjana and Ladislau 2007). Unlike other assets such as stocks, bonds, commodities and real estate, there is no active market in brands that would provide comparable values. Therefore, a number of brand evaluation approaches have been developed over the last two decades. Basic approaches fall into three categories: Research-based, financially driven and economic.

(a) Research Based Approaches – it uses consumer research to assess the performance of brands. Although the sophistication and complexity of such models may vary, they all try to explain and measures consumer's perceptions that influence purchase behavior. They include a wide range of perceptive measures. Through different methods of statistical modeling, these measures are arranged either in hierarchic order, to show degrees of relationship towards the brand (from awareness to pretense and purchase). The disadvantages of the research –based techniques is that they do not differentiate between the effects of the brand on consumers and the effects of other factors such as research, developing and design. They therefore provide a clear link between the specific marketing indicators and the financial performance of the brand.

(b) Financially Driven Approach – This approach is based on financial performance of a certain brand. Hence Micheal (1994) opines that one of the most effective ways for accountant to provide information to management is by conducting periodic brands valuations. It includes:

i) Cost – Based approach – According to Oladimeji (2012), the value of a brand as the aggregation of all historic costs incurred while bringing the brand to its current state that is, the development costs, marketing costs, advertising and other communication costs, and so on. Cost-based approaches fail because there is no correlation between the financial investment made and the values added by a brand. Financial investment is an important component in building brand value, provided it is effectively targeted.

ii) Comparables – This approach is used to arrive at a value for a brand by observing and valuing comparables of different brands. According to Elliot (1993) through brand, organizations are able to quantify a value that can be compared across product lines and among other companies of the same size in the industry. Defining comparable is difficult as by definition they should be differentiated and thus not comparable. Comparables can provide and interesting cross –check; however, they should never be relied on solely for valuing brand.

iii) Premium Price- This is the price paid by a buyer for improved quality of the product guaranteed by the certificate and not for product appearance. In this method, the price (premium price) is calculated as the net present value of the future price premium that a branded product would command over and unbranded or generic equitant. However, the primary purpose of many brands is not necessarily to obtain a price premium but rather to secure the highest level of future demand. This method is flawed because there are rarely generic equitant to which the premium price of a branded product can be compared. Today, almost everything is branded and in some cases store brands can be as strong as producer brands charging the same or similar prices. The price difference between a brand and competing products can be and indicator of its strength, but it does not represent the only and most important value contribution a brand makes to the underlying business.

c) Economic Use Approach – This provides the multidimensionality to brand valuation as it combines brand equity with financial measures. Companies compile a list of most valuable brands each year which is based on economic principle and replies to the fundamental questions: how much more valuable is the business because its own certain brands. High (1997) stresses that brand valuation includes both a marketing measure that reflects the security and growth prospects of the brand and a financial measure that reflects the earnings potentials of the brand.

METHODOLOGY

In this study, ordinary least square method of analysis was adopted, this is because (OLS) is a widely used statistical technique to study trends and investigate relationship among variable and as such, it is used extensively in regression analysis and estimation. Ordinary least square method is specific by an equation with certain parameters to be referred to as observed data. Such data could be used for financial analysis, forecasting, price trend which will eliminate human bias. Therefore, the importance of its application is in data fitting. Furthermore, the best fit in least square, minimizes the sum of the squared residuals. Such residual is the difference between the observed value and the fitted value provided by the model. Since the model shall contain X parameters, there will also be Y gradient to Zero. The gradient equations apply to all least square problems. Therefore a regression model is linear when the model is comprised of linear combination of parameters.

Model Specification;

Coco Cola brand = F (Pepsi, Nescafe, Nestle).

Where:

Y = Cocoa Cola brand

X_2 = Pepsi

X_s = Nescafe

X_4 = Nestle

Mathematically;

$Y = X_1 + X_2 + X_3$

DATA PRESENTATION AND ANALYSIS

Table 1: Regression Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig
Model	B	Std Error	Beta		
I. (Constant	69.876	15.376		4.545	.004
PEPSI	1.345	.862	.531	1.560	.170
NESCAFE	-1.960	.845	.352	-2.318	.060
NESTLE	.930	1.260	1.260	.738	.488

A Dependent Variable: Brand

Source: SPSS output (Statistical package for social sciences)

The estimated relation for the model is:

$Y = X_1 + X_2 + X_3$

The results indicated that the slope coefficient (B) of Pepsi is higher than Nescafe is lower than that of Nestle. In other words, the slope coefficients of Nestle are greater than the coefficient of Nescafe and Nescafe lower than the Coefficient of Pepsi. This could be expressed as:

Pepsi >Nescafe <Nestle.

Furthermore, only the slope coefficient of Pepsi is statistically significant at 5% level. The implication of the above results is that the consumers in Nigeria place priority on Pepsi brand and in return Pepsi beverage made a significant profit.

Table 2: Present the Model Summary Regression Model Summary
Model Summary[b]

Model	R	R Square	Adjusted R Square	Std Error of the estimate	R Square Change	F Chang e	df1	df2	Sig F Chang e	Durbin Watson
1	983>>	.966	948	1.0866	.966	56.161	3	6	.000	1.944

a. Predicators: (Constant), Pepesi, Nescafe, Nestle
b. Dependent Variable: Cocoa Cola Brand.

Source: SPSS Output.

The regression equation Model shows a coefficient of determination (R^2) of 96%. This means that only 96%. This means that only 96.6% of the variation in the Beverage industry explained by the three explanatory variables – Pepesi, Nescafe, Nestle. The remaining 3.4% is accounted for by other omitted variables.

The analysis of variance result is present in table three.

Table 3: Analysis of variance[11] ANOVA[b]

Model	Sum of Squares	df	Mean Square	F	Sig
1. Regression	**198.929**	**3**	**66.310**	**56.161**	**.000[a]**
Residual	**7.084**	**6**	**1.181**		
Total	**206.013**	**9**			

a. Predicator: (Constant), Pepsi, Nescafe, Nestle
b. Dependent variable: Coca Cola Brand.

Source: SPSS Output

The Analysis of variance in table 3 shows that the model is significant at 0% level with f-statistic of 56.161. The Durbin Watson statistic of 1.944 indicates that there is no fiest order autocorrelation. The results of the estimate are therefore reliable for prediction and do not require transformation.

Decision Rule:

Since the f-statistics value 56.161 is greater than the Watson statistic of 1.944. We conclude that there is significant impact of brand accounting on corporate profitability.

CONCLUSION

Growing global competition and ever shorter periods of supremacy of products with inbuilt technology, the contribution of brand to its shareholders will keep on increasingly. Brand is one of the several factors that provide stable competitive advantage. As the importance of brand to company's increases, managers will inevitably need to install more value-based brand management system that can align the management of the brand asset with that of other corporate assets and provide more reliable indicator on contribution of brand to the overall business performance.

Management and the market, the first and most important step is the development of a unique economic use approach to brand accounting. Such system may well become the most important management tools in the future.

RECOMMENDATIONS

Based on the researches carried out the following recommendations were made;

1. Organizations that are involved in brand accounting should develop an appropriate technique to measure their brand.
2. Brand Accounting should be considered an important factor by organizations because it will help improve the financial reporting.
3. Brand Accounting should have a uniform technique or procedure in which brand can be accounted for by the organization.

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