THE EFFECT OF BRAND EQUITY ON CASH FLOW, FINANCIAL PERFORMANCE AND COMPANY VALUE IN INDONESIA

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ABSTRACT

This study aims to analyze the effect of brand equity on cash flow, financial performance and firm value. The type of research used is quantitative research, the samples taken in this study are sub-sector consumption companies listed on the Indonesia Stock Exchange in 2015-2019 and meet the requirements for calculating the brand value of the Hirose method. PLS analysis in this study was carried out using warpPLS. That high brand equity is able to convince consumers of the quality of the products they buy, can maintain sales stability and ultimately improve financial performance. In conclusion, brand equity has a significant effect on cash flow, but not significant on firm value and financial performance has an effect on firm value. Future research must understand the relationship between brand equity and financial policies such as capital structure and company growth.

Keywords : Brand Equity, Cash Flow, Financial Performance, Corporate Value, Business

INTRODUCTION

Brands equity have important product market implications because they identify and distinguish firms' products and services from those of competitors. Brand equity has been shown to significantly contribute to firm value [1, 2, 3] and to be associated with higher firm performance, higher credit ratings and lower firm risk [4]. Brand equity, nowadays, is an important concept in business practice. In the 1980s, the discussion of company brand equity attracted attention and became an in-depth study in the business community [5]. Brand equity is recognized as a strategic business asset of companies in marketing theory and practice. Brand equity is recognized as a strategic business asset of the company in contemporary marketing theory and practice [6].

A brand is an intangible asset that increases cash flow rates and reduces cash flow vulnerability. The higher the cash flow in the company, the better the company's performance [7]. Research studying the effect of brand equity on a company's financial condition is still rare, especially in Indonesia.

Some research says, the relations between our brand equity measure and firm risk and performance. Consistent with the literature, we find that brand equity is negatively related to measures of risk and positively related to measures of profitability. [8] Thus, our trademark-based brand equity measures capture the same cash flow and volatility characteristics of brand equity documented in the literature. Given these characteristics, and all else being the same, a balancing theory of optimal capital structure would predict that firms with considerable brand equity should be more highly levered [8,9].

This research studying brand equity was conducted on the consumer non-cyclicals sub-sector which was listed on the Indonesia Stock Exchange for the period 2015 - 2019. This research was analyzed using WarpPLS regression analysis. Therefore, this study aims to determine the effect of brand equity as measured by cash flow, financial performance and firm value.

LITERATURE REVIEW

A brand is a symbol including name, logo, sign, symbol, package design, etc., which are used by companies to identify and differentiate their products and services from competitors [10]. Brand equity is the added value that a product achieves as a result of past investment in marketing activities for that brand [11]. Brand is the identity of a product that is used to differentiate products and services from competitors [12]. Brand is the essence or promise of a product delivered or experienced by customers. Brand is a marketing asset that stimulates present and future profits for the company [13].

The concept of Brand Equity can be understood from the perspective of four main players, namely investors (brand owners, producers, retailers, and consumers or customers [14]. Where brands add product value to each of the four main players. Investors are motivated by financial issues to extract brand value from other company assets [11]. On the other hand, consumers and retailers are more motivated by the strategic implications of Brand Equity. Developing and managing brands has become a priority for companies to maximize the value of these assets significantly [15]. Companies with good branding have a competitive advantage in the market, because good branding is built from good product quality or good supporting aspects such as brand image and distinct personality [15,11].

Proposed that market-based assets such as brands can increase shareholder value through (a) accelerating cash flows, (b) increasing cash flow rates, (c) reducing cash flow volatility and vulnerability, and (d) increase in the residual cash flow value [16]. Signals can be defined as "attributes or activities that can be manipulated that convey information". Signaling theory, states that the company's growth factors can provide a positive signal about the company's condition that is captured by shareholders and other stakeholders. Signaling theory, states that market equilibrium results in excess investment of signaling effects which are personal benefits to investors [17].

Brand signals consist of past and present marketing mix strategies and activities related to brands, so that in the presence of asymmetric and imperfect information, brands can function as credible market signals [18]. Signaling Theory shows that signal credibility determines whether market signals convey information effectively [19]. States that every brand equity asset generates value for customers as well as for the company. Managing brand equity, it is important to be sensitive to the value that can be created in order to manage brand equity effectively and to make informed decisions about brand building activities and the ability of brands to generate marginal cash flows to the market. The theory of cash flow signaling hypothesis [12]. Suggests that changes in dividend payments to shareholders will provide information about cash flow or current cash flow and the company's cash flow in the future [11].

Signaling theory (Ross, 1977) suggests that the thinking of company managers has better information about company profitability than investors regarding company prospects [4,8]. Signaling theory Spence (1973) investment spending is a positive signal for company growth in the future, thereby increasing stock prices as an indicator of firm value. Signaling theory Spence (2002) net benefits from signal issuance are positively correlated with invisible attributes/brand equity that contribute positively to productivity [8].

Brand equity has been shown to have a significant effect on cash flow, [20,21,22,23]. Research shows that investors perceive additional information about branding activities as a contribution to expectations of future cash flows [24]. The effect of cash flow on financial performance has been empirically proven significant [20].

Based on these reviews, the study studied the effect of brand equity on cash flow, financial performance and firm value in the non-cyclical consumer subsector in Indonesia. The performance of a firm is intuitively expected to be improved as a result of a stronger brand and higher brand equity. However 'brand equity' is defined in many different ways and there is no generally accepted standard way of measuring it. In this study a consumer based perspective is adopted in examining the brand equity concept.

METHODOLOGY

Brand equity in this study is treated as an exogenous variable in which brand equity in this study is measured by brand value. Brand value serves as a proxy for a company's reputation and goodwill [25]. Brand value, as in Hirose's theory, is the concept of competitive advantage through branding to increase current and future profits by leveraging competitive prices, high customer loyalty and the power of brand extension. The following is a description of the brand equity assessment using the Hirose [26]. Research conducted by Wang, also uses the Hirose et.al method [27]. This assumes brand value as a function of three main factors;

$$BV = f(PD, LD, ED, r) = \frac{PD}{r} * LD * ED$$

Hirose, *et.al.* (2002)

Where: BV = Brand Value, PD = Prestige Driver, LD = Loyalty Driver, ED = Extention Driver, R = Risk-free interest (discount) rate. Prestige Driver (PD) = Cash flow arising from a price advantage or excess value from a brand. PD calculations are measured in more detail using the following formula:

$$PD = \frac{1}{5} \sum_{t-5}^{0} \left\{ \left[\frac{Si}{Ci} - \frac{S_i^*}{C_i^*} \right] * \frac{AD_i}{O_i} \right\} * C_0$$

Hirose, *et.al.* (2002)

Where: PD = Prestige Driver; Si = Sales of Firm; Ci = cost of sales of firms; AD = advertising expenses and promotion costs; OE = total operation expenses. Loyalty Driver (LD) refers to the ability of a brand to maintain stable sales for the long term thanks to customer loyalty in repeating purchases of the same brand. Prestige Driver, measured using the following formula:

$$LD = \frac{\mu_c - \sigma_c}{\mu_c}$$

Hirose, *et.al.* (2002)

Where: μ_c = five -year average of firms' cost sales; σ_c = five -year standard deviation of firms' cost of sales.

Extension Driver (ED) brand expansion capability, the intention is to reflect the ability of a well-known brand to expand its business network to all industrial sub-sectors that differ from other geographical areas. The formula used to quantify ED in this study is as follows:

$$ED = \frac{1}{2}\sum >_{i=-1}^{0} \left| \frac{SX_i - SX_{i-1}}{SX_{i-1}} + 1 \right|$$

Hirose, *et.al.* (2002)

Where: ED = driver extension; SX = sales from non-core and overseas businesses. The cash flow ratio used is as follows:

a. Net Cash Flow from Operating Activities Total Assets (NCFOTA)

NCFOTA is net cash flow from operating activities divided by total assets. This study uses a formula [28].

$$NCFOTA = \frac{NCFOTA}{TotalAsset}$$

b. Net Cash Flow Total Sales (NCFOSA) is net cash flow from operating activities divided by total sales. This study uses the formula from [29].

$$NCFOSA = \frac{NCFOSA}{TotalSales}$$

c. Total Asset Investment (ITA) is investment activity divided by total assets excluding current assets. This study uses the formula:

$$\mathrm{I}TA = \frac{Investasi}{(TA - CA)}$$

d. Financial Long Term Debt (FLD) represents cash inflows from financing of total long-term debt and equity. This study uses the formula:

$$\mathrm{FLD} = \frac{Financing}{Long\ term\ Debt + \ Equities}$$

The endogenous variables in this study are cash flow, financial performance and firm value. Cash Flow is measured by NCFOTA, NCFOSA, ITA, and FDL. Financial performance is measured by return on equity (ROE). return on investment (ROI), NPM and EPS and company value is measured by MBR, Tobin Q and Market Capitalization (MC).

RESEARCH AND RESULTS

This study investigates the effect of brand equity on cash flow, financial performance and firm value in the Consumer non-cyclicals subsector in Indonesia. The sample for this research is consumer non-cyclicals sub-sector companies in Indonesia that meet certain requirements such as publishing their financial statements frequently during the period 2015 to 2019 and their brand value can be calculated using the Hirose method. Based on these criteria, 21 companies were selected as the research sample. There are a total of 105 units of analysis (21 companies in 5 years). Regression analysis in this study was carried out using WarpPLS software.

Table 1 The coefficient of determination (R^2) for the endogenous variables Cash Flow, Financial Performance and Firm Value are, respectively, 0.248, 0.523, and 0.675. Based on the R^2 value, the predictive relevance of Q2 can be calculated as follows:

$$Q^2 = (1 – (1 - 0{,}248)(1 - 0{,}523)(1 - 0{,}675) = 0{,}8834 = 88{,}34\%.$$

Therefore it can be said that the model is good, that is, it can explain the phenomenon or system being studied at 88.34%. The remaining 11.66% is influenced by other variables that have not been included in the model and errors.

Table 1. R-squared coefficients

Brand_Equity	*Cash_Flow*	Financial performance	The value of the company
	0.248	0.523	0.675

The results of table 2 show that brand equity has 3 indicators. From the estimated weight value of each indicator, the extention driver (PD) is the most appropriate indicator to describe brand equity. This is because the estimated ED Weight value is the largest of the 3, namely 0.994. Based on the critical point obtained, ED has a dominant and significant effect on brand equity because the critical point value obtained by Equity after exploration is only one indicator, namely ED. The weight of a single indicator is 1.

That of the 4 indicators that make up the Cash Flow variable, where NCFOSA is a stronger indicator has an estimated Weight value of 0.961. This indicates that for consumption sub-sector companies that went public on the Indonesia Stock Exchange (IDX) from 2015 to 2019, the NCFOSA indicator is the most important indicator.

That of the 4 indicators that most strongly form the Financial Performance variable is ROE which has an estimated Weight value of 0.517. This indicates that for consumer non-cyclicals sub-sector companies that went public on the Indonesia Stock Exchange (IDX) from 2015 to 2019, the ROE indicator is the most important indicator of the Financial Performance variable. This indicator has a positive direction, so that with an increase in ROE a higher company financial performance will be formed.

Table 2 shows that of the 3 indicators that make up the Firm Value variable, TobinQ is a stronger indicator with an estimated Weight value of 1.00. This indicates that for consumer non-cyclicals sub-sector companies that went public on the Indonesia Stock Exchange (IDX) from 2015 to 2019, the TobinQ indicator is the most important indicator of the company value variable.

Table 2. Measurement Models

No	Indicator	Weight	P value
Brand Equity			
1	PD	-0.062	0.261
2	LD	-0.04	0.341
3	**ED**	**0.994**	**<0.001**
Cash Flow			
1	NCFOTA	0.015	0.44
2	**NCFOSA**	**0.961**	**<0.001**
3	ITA	-0.05	0.304
4	FLD	-0.296	<0.001
Financial performance			
1	**ROE**	**0.517**	**<0.001**
2	ROI	0.354	<0.001
3	NPM	0.277	0.001
4	EPS	-0.023	0.406
The value of the company			
1	MBR	-0.037	0.35
2	**TobinQ**	**1.143**	**<0.001**
3	KP	-0.235	0.006

Brand Equity has an effect on Cash Flow obtained by a path coefficient of -0.498 and p-value < 0.001 (significant). Thus it can be said that the hypothesis of the effect of Brand Equity on Cash Flow is accepted. This research supports the research results which concludes brand equity has a significant effect on cash flow [20, 21,22,23]. Brand equity has an effect on firm value, obtained by a path coefficient of -0.121 and p-value = 0.102 (not significant). Thus it can be said that the effect of Brand Equity on Firm Value is rejected. This research is in accordance with research conducted by [5] which found that brand equity has no effect on firm value. The findings of this study do not support [27,30,31], which state that brand equity has an effect on firm value.

Financial Performance on Firm Value obtained a path coefficient of 0.701 and a p-value <0.001 (significant). Thus it can be said that financial performance affects the value of the company received. The findings of this study support the results of research conducted by [32, 33, 34, 35].

Table. Model Struktural

Hipotesis	**Path Coefficient**	***p-value***
Brand Equity effect on cash flow	-0,498	<0,001
Brand equity does not affect the value of the company	-0,121	0,102
Financial performance affects the value of the company	0,701	<0,001

Sig P-value < 0,05

Based on the research results, it is known that high brand equity is able to convince consumers of the quality of the products they buy. This can maintain sales stability and ultimately improve financial performance. However, average brand equity is not attractive enough for shareholders or investors who are more interested in high financial performance. High financial performance causes cash flow to flow to owners and the company's operating results will increase. Increasing cash flow will ultimately increase the value of the company.

CONCLUSION

Research linking brand equity with cash flow, financial performance and company value is still rare, especially in Indonesia. Therefore, this study aims to study the consistency of the effect of brand value on financial performance, and company value, especially in Indonesia.

The results of the study show that brand equity has a significant effect on cash flow. supports the Theory of cash flow signaling hypothesis (Lintner. 1956). Brand equity has no significant effect on firm value. This significant relationship between financial performance and firm value supports Signaling theory (Ross, 1977), Signaling theory Spence (1973), Signaling theory Spence (2002)

Future research must understand the relationship between brand equity and financial policies such as capital structure and company growth. It is also recommended to study the effect of capital structure and financial performance on brand equity, because there is a possibility that brand equity is also influenced by capital structure and financial performance. Lastly, similar research should be conducted in other industries to fully understand the implementation of brand equity in Indonesia.

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