Corporate Brand Valuation – A Global Perspective

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INTRODUCTION

Brands are emerging as important strategic assets of the firms. Brand valuation can better explain the vast difference between the market value and the book value. Failure to value brands can affect the firm's rate of return and can create the lop-sided balance sheet.Moreover; there is an increasing realization among the CEOs that brands are the assets created by marketing people and one best way of recognizing marketing department performance is through brand valuation. Brand valuation helps a firm to evaluate its existing brands and initiate suitable strategic moves like weeding out non-performing brands, strengthening performing brands, brand acquisition, brand repositioning, etc.

Corporate India, too, on account of competitive pressures, threats of takeovers, desire to reveal true profits and position, etc. is recognizing the need of brand valuation. Some of the highly performing brands like Infosys, Wipro, Tata, etc., are getting their brands valued either internally or with the help of external brand experts.

OBJECTIVES OF THE STUDY

The present paper is an attempt to understand the whole process of brand valuation, need, objectives and methods of valuations as used by Indian companies and international agencies like UK's Interbrand.

FINANCIAL EVALUATION AND ACCOUNTING FOR BRANDS

Financial evaluation and accounting procedures for brands have become subjects of considerable interest. This intense interest in the subject has several technical, economic and fiscal aspects which especially reflect the discovery of the importance of intangible investments in modern companies and of the growth that a brand can generate. This aspect is gaining importance at the international level as these are concerned with the financial information of large multinational corporations holding brands that are strong. However, there exist differences in the accounting procedures for brands and their position in the balance sheet from one country to another, which greatly affects the interpretation of the financial health of the companies. Besides this, within the same country, the accounting procedures and regulations may be contradictory, thus creating certain possibilities which may be seized by certain innovating companies.

The reason for the interest in this subject is the large increase in the number of mergers and acquisitions of companies worldwide. When one company is acquired by another; there exists a huge difference between the actual price paid and book value of net assets of the company. This difference is significantly more in case of companies which have strong brands and positive forecasts for growth. This difference is commonly known as goodwill, which is a measure of the financial markets positive attitude to the future of the company. For accounting purposes, the payment made by the acquiring company which is excess of the assets must lead to the inclusion in its balance sheet, so as to get a perfect match between these elements and the price paid. In the modern accounting system and norms, goodwill must be allocated to the specific items that have created it. Brands, patents, know-how and databases are from this category. The difference between the price paid and book value of net assets of the company can be influenced by the various intangible and tangible assets.All these influencing assets have been depicted in the following figure:

Price Paid

Sources of the Gap: Intangible and Tangible Assets		Goodwill (Large meaning)
	Existing Goodwill	
	Brands	
	Patents	
	Technical Know-how	
	Data base	
	Equipment (economic value)	
	Buildings (economic value)	

Net assets (Book value)

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BENEFITS OF BRAND VALUATION

The following are different types of tangible and intangible benefits of Brand Valuation:

TANGIBLE BENEFITS

a) **Merger & Acquisition:** It is of critical importance for an acquirer, as well as for the vender to understand and evaluate their real worth for negotiating the correct purchase consideration.

b) **Disposal:** The current focus on brands has led many companies to recognize that they cannot support properly all their brands or certain brands could be worth more to a third party than to their current owner. Brand evaluation technique can be used to judge which brand to dispose of and their possible economic worth to a third party.

c) **Licensing:** Brand licensing, either to third-parties or internally to its own subsidiary, is an increasingly common practice. Brand valuation assists in formulating this strategy.

d) **Fund Raising:** Brand valuation is playing an increasing prominent role in the area of fund raising, particularly from the public as a brand represents robust asset against which to seek funds is much easier.

e) **Discount Rate:** Brand valuation reveals the robust strength and also assists in acquiring large funds at a lower cost.

INTANGIBLE BENEFITS

(a) **Enhances confidence:** Brand credibility shows the faith and confidence of public at large in the product; Valuation if reflected in the books of accounts further enhances the public loyalty to the product and hence becomes a force multiplier.

(b) **Indicator of effective utilization:** The investment in the brand building creates value in the reverse direction when compared to the capital expenditure. When the firm invests in capital expenditure, it utilizes the proportionate cost every year, which the firm can write off in the form of depreciation or amortization, where as, the expenditure in brand building is incurred day to day and this expenditure is converted into a valuable asset over a period of time. The expenditure is considered as revenue expense due to accounting and taxation provision which really is not so. Hence, valuation gives the real affective worth, which has been created over the years through brand building.

(c) **Credibility to the real worth:** If the firm valuates its brand only at the time of disposal, it has a much lesser influence and will always leave a doubt of its real worth in the mind of both the buyer as well as the seller. Whereas, if the brand is continuously valued, it has a different impact and gives much more creditability to the real worth.

(d) **Strategy development:** Companies are applying brand evaluation techniques in order to understand and manage their brands better. Brand evaluation involves a detailed examination of a brand from the view point of marketing, financial and legal perspective. It also examines the brand performance, prospective, market opportunity, and competition. Thus, it provides an excellent tool for strategy development.

BRAND VALUATION METHODOLOGY

Recognisation of brands as assets has a long history. Perhaps, the interest in the financial evaluation of brands is a more recent phenomenon. The corporate world is in the wave of mergers and acquisitions which began in the 1980s and in which brands often played an important role. Economic valuation of brands are frequently done to serve the purposes such as setting royalty rates in licensing brands, evaluation of debt levels and risks, and estimating damages in trademark disputes, etc. Thus, several consulting firms have proposed and developed a variety of methodologies to meet this demand for brand valuation and performed various services regularly.

Financial World annually publishes the estimates of the value of more than two hundred brands that are based on a simplified version of the Interbrand methodology. According to this methodology, a brand's value is taken to be the product of two variables;

1. Its annual net after tax profits, adjusted to exclude the earnings expected for an equivalent unbranded product and averaged over time, and
2. A discount rate reflecting the brand's strength.

The assessment process of brand strength takes the following seven factors into account:

1. **Leadership**: ability to influence the market.
2. **Stability**: capability to maintain a consumer franchise.
3. **Market**: vulnerability of market demand to changes in tastes or technology.
4. **International scope**: cross-national/cultural potential.
5. **Trend**: long-term appeal to consumers.
6. **Support**: strength of communication.
7. **Protection**: security of the brand owner's legal or property rights.

Based on the above factors, the brand's strength is determined which in return determines the appropriate multiplier. The greater a brand's strength, the higher it's multiple. Multiples range from six to twenty.

METHODS OF BRAND VALUATION

The main purpose of valuing the brand is to determine the monetary benefit that accrues to the brand owner as a result of the brand. The valuation of a brand is more concerned about its economic use. For accounting purposes, there are different methods of brand valuation, which are concerned with the measure of historical value of a brand, as opposed to the value it will generate in future. The following two are the popular methods of brand valuation:

- Historical Cost Method.
- Replacement Cost Method.

Historical Cost Method: The historical cost accounting approach is an accounting technique that values an asset for balance sheet purposes at the price paid for the asset at the time of its acquisition. The historical cost accounting is the situation in which accountants record revenue, expenditure, asset acquisition and disposal at historical cost: that is, the actual amounts of money, or money's worth, received or paid to complete the transaction.

Replacement Cost Method: An accounting system that values assets and liabilities according to their replacement cost rather than their historical cost. Replacement cost accounting incorporates the effects of changing prices and the resultant changing values of the items that are listed in a firm's financial statements.

APPROACHES TO BRAND VALUATION

The Brand Valuation approaches can be identified into the following two types:

- Economic Use Approach
- Potential Earnings Approach

ECONOMIC USE APPROACH

This approach considers the economic value of a brand in current use to current owner. In other words, it considers the return that the owner actually achieves by owning the brand – now and in the future. Economic use valuations assume that brands provide their owners with security of demand. In the short run, a manufacturer without a brand might enjoy the same sales, the same economies of scale, even the same premium prices as the manufacturer with a brand. However, the non-branded manufacturer could not rely on the same security of knowing that the brand's customers this year are likely to be customers of the brand next year, and for many years after that. This approach also depends on the accuracy of future sales and earnings projections.

Within economic use there are two approaches for the valuation of brands. They are:

- The Relief from Royalty Approach.
- The Earnings Split Approach.

The Relief from Royalty Approach: Under this approach, the assumption is that a business does not own its trademarks but licenses them from another business at a market rate. Brand value under this method is the net present value of the royalty payments made for using the trademarks. This valuation methodology favors the fiscal authorities and the courts because they calculate brand value by reference to documented third-party transactions involving brands of equivalent strength in equivalent industries.

The Earnings Split Approach: In this approach, the earnings above a break-even economic return on the tangible assets of the business are attributed to the intangible assets.The brand proportion of these intangible earnings is then estimated, generating a stream of earnings attributable to the brand. This approach of brand valuation is commonly used for most marketing purposes.

The following are five major components to the Earnings Split Approach:

1. Market and Competitive Context: This identifies the overall dynamics of the market and the strength of competition.

2. Business Segmentation: Brand influence varies by line of business, customer and product type. Consequently, this step divides the business into segments, based on the role played by the brand.

3. Financial Forecasts: These are projections for the future earnings of each segment in the previous step.

4. Brand Value Added: This involves identifying the drivers of purchase decisions in each segment, and the impact exerted by the brand. The composite brand score across all drivers provides the proportion of total branded business earnings that can be attributed to the brand.

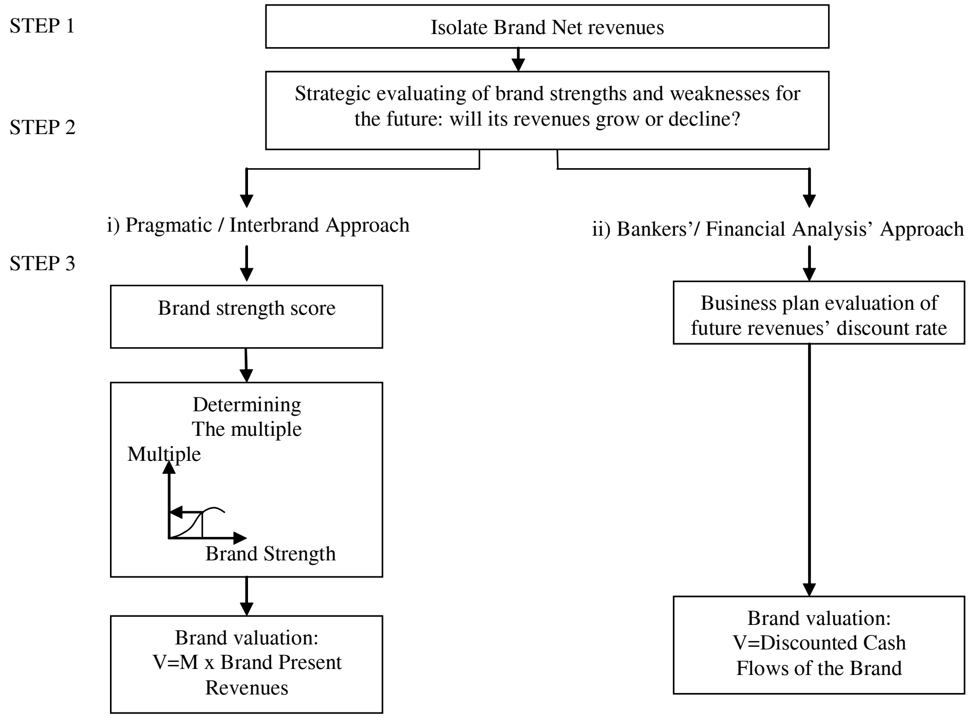
5. Risk Analysis: This assesses the strength of the brand's franchise with trade customers and end consumers to establish the security of future brand earnings. The result is a discount rate for the stream of earnings attributable to the brand.

In theory, both the forms of economic use should give rise to approximately similar valuations. But in practice, the Earnings Split Approach tends to produce higher values because it is generally based on a broader definition of a brand, and because it allows for growth into new segments.

POTENTIAL EARNINGS APPROACH

The need for the valuation of brands lies in the fact that they are considered as the most important assets of the organization.

In this regard, an asset is expected to generate revenues for the company. This approach to brand valuation is based on the expected profits of the brand. The process of valuing the expected profits of the brand can be divided into three independent stages which are exhibited in the figure below:



1. The first step involves separating and isolating the net income associated with the brand and not with the company.
2. The second step is to estimate the future cash flows. This requires a strategic analysis of the brand in its market or markets.
3. The third step involves choosing the suitable approach either by using multiple methods to determine precisely this multiple or a classic financial method of a discount rate and period.

EFFECTIVENESS OF BRAND VALUATION

Brand valuation assigns financial value to the name or image of a brand offering a comprehensive measure of equity for the organization. The brand's value, as a measure of success helps in estimating the effect of management decisions such as those generating short-term expenditures and long-term benefits. Brand valuation enables an organization in effectively discharging various functions such as:

- Brand valuation allows managers to appraise the efficiency of brand expenditures in terms of the increased value of the brand itself. The new role can be taken by accountants by helping marketing manager's measure performance in strongly branded companies.
- Brand valuation is another important accounting technique which may be more useful to marketing, which extends beyond a cost focus. Because of its comprehensiveness, it relates to outcomes and incorporates projections of future income and cash flows. This predictive information is important in assisting a firm with strategic brand management.
- Brand valuation provides the management with a measure that allows an appraisal of the brand relative to the other assets of the organization.
- Brand valuation facilitates a regular process whereby marketing professionals can help in alerting corporate strategists to the critical importance of the brand.
- Brand valuation techniques allow a company to deliver a consistent brand image. When the entire organization understands how brand value is ascertained, it will be easier to prevent actions that conflict with each other or interfere with the overall brand strategy.
- Brand valuation will also aid managers involved in budget allocation decision making. Marketing budget allocation can be done on the basis of relative value of the brand in the portfolio.
- Brand valuation allows the use of a comparable measure, which helps in comparing the performance of managers of different products or in different geographic segments.
- Brand valuations are an ideal measure for tackling short term issues and help in determining the performance and rewards.

- Coordination of strategies among separate product managers by considering the combined effect on brand value for management of the separate product segments is possible through brand valuation.
- The brand value helps in determining inter-company transfer price.

ANALYSIS OF THE WORLD'S MOST POWERFUL BRAND VALUE

Now, its proposed to examine the pattern and trend in the growth rate of brand value of world's most powerful brands, with a view to point out the progress of brand value. The relevant data is presented in the following table:

Value of World's Most Powerful Brands

No.	Brand Name	Country of Origin	Industry	Brand Value2004 (US $ m)	Brand Value2005 (US $ m)	Brand Value2006 (US $ m)	Brand Value2007 (US $ m)	Brand Value2008 (US $ m)
1	Coca-Cola	US	Beverages	67,394 (-4)	67,525 (0)	67,000 (-1)	65,324 (-3)	66,667 (2)
2	IBM	US	Computer Services	53,791 (4)	53,376 (-1)	56,201 (5)	58,709 (2)	59,031 (3)
3	Microsoft	US	Computer Software	61,372 (-6)	59,941 (-2)	56,926 (-5)	57,090 (3)	59,007 (1)
4	General Electric	US	Diversified	44,111 (4)	46,996 (7)	48,907 (4)	51,569 (5)	53,086 (3)
5	Nokia	Finland	Consumer Electronics	24,041 (-18)	26,452 (10)	30,131 (14)	33,696 (12)	35,942 (7)
6	Toyota	Japan	Automotive	22,673 (9)	24,837 (10)	27,941 (12)	32,070 (15)	34,050 (6)
7	Intel	US	Computer Hardware	33,499 (8)	35,588 (6)	32,319 (-9)	30,954 (-4)	31,261 (1)
8	McDonald's	US	Restaurants	25,001 (1)	26,014 (4)	27,501 (6)	29,398 (7)	31,049 (6)
9	Disney	US	Media	27,113 (-3)	26,441 (-2)	27,848 (5)	29,210 (5)	29,251 (0)
10	Google	US	Internet Services	—	8,461 (—)	12,376 (46)	17,837 (44)	25,590 (43)

Source: www.interbrand.com/league_chart.html

Note: Figures in brackets indicate annual percentage growth.

The analysis of data reveals that in the year 2008, Coca-Cola of US Beverages brand value was highest with US $ 66,667 Million followed by IBM, Microsoft, General Electric of US, Nokia of Finland, Toyota of Japan and Intel, McDonald's, Disney and Google of US brands during the period of review. As against these, Coca-Cola of US Beverages brand value in 2004 and 2005 was at US $ 67,394 Million and US $ 67,525 Million respectively. It was interesting to note that the Google brand of US Internet Services made a significant progress, though it entered into the market very recently in the year 2005. However, Toyota brand of Japan Automotive industry, Nokia brand of Finland Consumer Electronics, McDonald's brand of US Restaurants and General Electric brand of US Diversified have registered a regular and significant increase. Among the entire world's top most brands, US industries brands have been dominating the scene during the study period.

CONCLUSION

Now-a-days, brands are emerging as important strategic assets of the firms. Financial evaluation and accounting procedures for brands have become subjects of considerable interest. Brand valuation assigns financial value to the name or image of a brand offering a comprehensive measure of equity for the organization. Brand valuation also helps in determining inter-company transfer price.

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