



Brand Valuation: the methodologies

Brand valuation has come a long way from its beginnings as a niche practice says **Sophie Roberts**

Valuation is something we intuitively do on a daily basis. It is easier to take the opinion that 'seeing is believing' when valuing something, but when it comes down to valuing a business, it's what you're not physically seeing that is truly valuable," said Julian Dailly, director of valuation at global brand consultancy, Interbrand.

Brands have come a long way from the time when it was first thought that the word 'brand' was just another word for logo. Brands are now recognised as a company's identity and encompasses names, terms, signs, symbols and designs, or indeed, a combination of these. "They identify goods, services or entities that create distinctive images and associations in the minds of stakeholders, and may ultimately generate economic value and benefit," said Roy D'Souza, managing director of Ocean Tomo's valuation practice and Brad Sarna, associate at Ocean Tomo.

It is now widely appreciated that a brand is one of the most important assets an organisation owns. An asset such as this cannot just sit on the bench which is why brand valuation and the methods in which to carry one out, has become an increasingly important tool.

"Brand valuation is important because intangible assets are increasingly being

recognised as highly valued properties. Brands can be one of the most valuable assets a company owns, but also tend to be the least understood," commented D'Souza and Sarna.

Originated in the 1980s, brand valuation has come a long way. The first major brand valuation was carried out in 1988 when Rank Hovis McDougall (RHM) believed that its brands were being undervalued when Goodman Fielder Wattie (GFW) offered £600 million for the company. Therefore, in RHM's 1988 financial accounts, the value of both internally generated and acquired brands under intangible assets was included. This value for the 'brands' alone, was calculated as being worth £680 million.¹

Since the first brand valuation was performed, universally recognised methods used to carry them out have been devised, tweaked and rated to assist not only brand valuers, but accountants, lawyers and marketers who are also involved in the process – the accountants being the toughest crowd to get on board.

Why value a brand?

A brand can be valued at any time and for a number of different reasons, including: brand strategy, financial reporting, mergers and acquisitions (M&A) and litigation. There is usually always a direct purpose for a brand valuation and they are not usually carried out

just for the sake of it as it can be an expensive and time consuming process. The following are just some scenarios that might require a brand valuation.

• Transactional:

- M & A
- Joint Ventures
- Licensing Negotiation
- Regulatory and Accounting compliance
- IP portfolio management

• Litigation:

- Damage/loss calculations
- IP infringement
- Licensing and royalty rate issues

• Marketing/Internal:

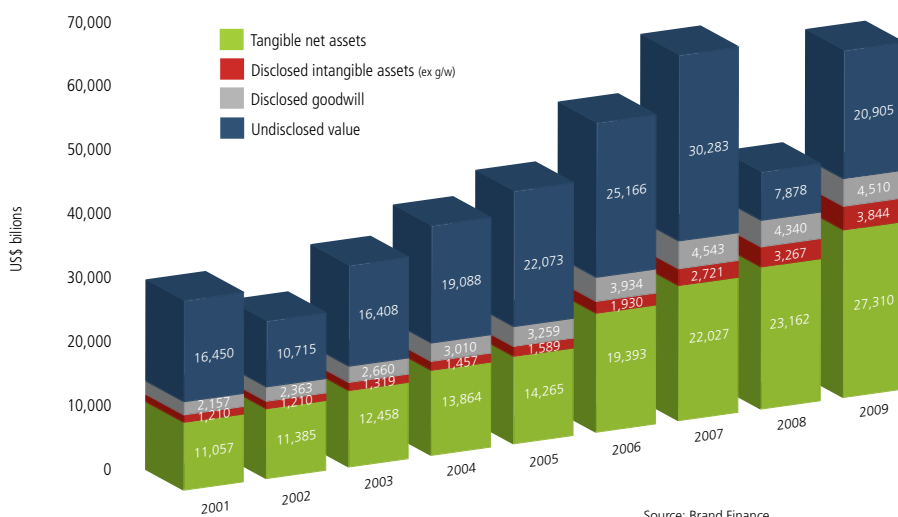
- Brand management strategy
- ROI/marketing investment allocation.²

Like most business-related valuations, brand valuation requires a lot of additional information in order to be successful and for this reason, it is usually considered as a specialisation within the valuation industry. "A brand valuation is similar to any other valuation, but has additional steps that extend the time-frame and amount of work to be completed," said D'Souza and Sarna. They continued, "it involves the application of generally accepted valuation techniques and theory coupled with an understanding of the qualitative factors that go into the key elements of a brand. The process of combining market research with financial results to understand what drives a brand's value is complex and specialised."

Brand valuation standards

The International Organization for Standardization (ISO), one of the world's largest developers and publishers of international standards, published a standard last year entitled *BSI ISO: 10668 Brand Valuation: Requirements for monetary brand valuation*; a document which has grabbed the attention of brand valuers. The standard covers requirements for procedures and methods of monetary brand measurement and provides a framework for the processes to be followed when undertaking a valuation of this kind. These include objectives, bases of valuation, approaches to valuation and methods of valuation.

Global Enterprise value 2001-2009



The standard was put together and developed for the purpose of addressing a number of issues which have been cropping up regarding brand valuation – namely, the methods and how they were implemented. “But what is most significant about this, is that the ISO considers brand valuation to be important enough to publish a standard on it,” commented David Haigh, chief executive of Brand Finance and member of the international committee that put together BSI ISO: 10668. “This is a huge step in the right direction.”

The three most common approaches for valuing a brand are: market approach, cost approach and income approach. The BSI ISO: 10668 categories these approaches under financial analysis. They tend to work in conjunction with each other and are universally agreed to be the most reliable and effective in valuation: the income approach being the most preferred. The BSI ISO: 10668 also stipulates that before performing the financial analysis, it is important to carry out a legal analysis and behavioural analysis to ensure that all the necessary information is on the table.

Legal analysis

According to the BSI ISO: 10668 standard, the legal analysis should be the first area of analysis. It can be something which is often over looked during the process according to Haigh. “There is a general consensus that valuers simply don’t want to take on the responsibility of carrying out a legal analysis,” said Haigh. Within the team that contributed to the ISO standard, there were several IP lawyers involved who shared their opinion. “The IP lawyers, especially the German lawyers, were vehement in the opinion that ‘if you don’t do a proper due diligence country by country, how can you perform an accurate financial analysis?’”.

Assessment of legal protection as noted in the BSI ISO: 10668 standard:

- “The appraiser shall assess the legal protection afforded to the brand by identifying:
- each of the legal rights that protect the brand;
 - the legal owner of each of those legal rights;
 - the legal parameters influencing negatively or positively the value of the brand.

Note 1: An important component of brand valuation is assessing the legal protection afforded to the brand in each relevant jurisdiction. Legal protection is one factor that informs brand value because it permits the brand owner to utilise formal legal systems to exclude third parties

from using the same brand, thereby providing a degree of exclusivity.”

Behavioural analysis

To perform a successful brand valuation, it is necessary to determine a brand’s strength which is then subsequently used to create a framework for the valuation model. “This entails examining available market research and benchmarking the brand against its competitors to assess the brand’s strengths and weaknesses,” said D’Souza and Sarna. “Once this information has been gathered and analysed, it is possible to build a financial model to assign numbers to the brand.”

Behavioural analysis, in relation to the financial aspects is defined in the BSI ISO: 10668 standard as:

“In order to assess the value of the brand, the financial analysis shall incorporate an analysis of the behavioural aspects of the brand related to the stakeholders. When applying the income approach, an analysis of the behavioural aspects of the brand is necessary in order to determine the monetary proportion attributable to the brand and to assess the risk connected to the brand when determining the discount rate.”

However, like with any aspect of a valuation, challenges can arise, such as the availability of information. If this information is lacking or not relevant, it can present difficulties. Dailly enforces this further, referring to the significance of the quality of behavioural information. “Often you are looking at an asset owned by a company in way that the company hasn’t looked at it before – although it may have some of the necessary information for that purpose, the quality can be hit or miss.”

Both legal and behavioural analysis enhance the transparency of the information required for a brand valuation, making it easier to perform.

This also refers to the financial data which is ultimately drawn out of the financial analysis.

The market approach

The market approach focuses mainly on comparables. It is defined under BSI ISO: 10668 as:

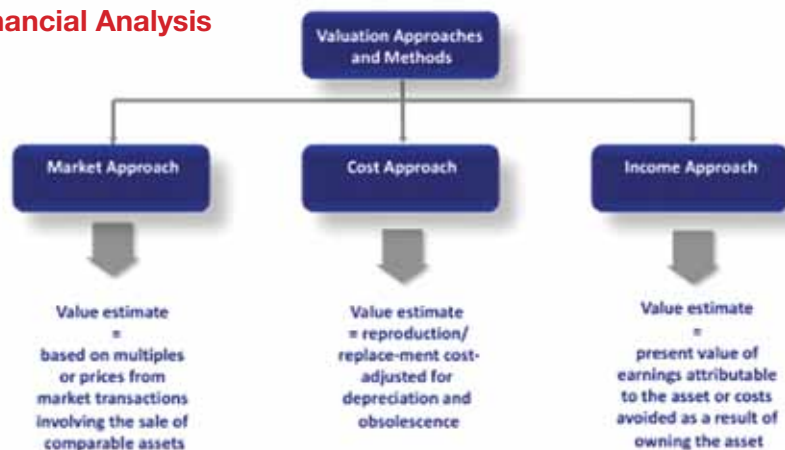
“The market approach measures value based on what other purchasers in the market have paid for assets that can be considered reasonably similar to those being valued. The application of the market approach shall result in an estimate of the price reasonably expected to be realised if the brand was to be sold. Data on the price paid for reasonably comparable brands shall be collected and adjustments shall be made to compensate for differences between those assets and the brand under analysis. For selected comparables, multiples shall be computed on the basis of their acquisition price. Those multiples shall then be applied to the aggregates of the subject brand.”

Due to the fact that a company’s IP is not generally disclosed publicly, it is therefore difficult to find comparables when utilising the market approach. “The market approach can be a difficult methodology to primarily depend on in a brand valuation,” said D’Souza and Sarna. “It is generally used in a supporting role or as a sense check to the income approach. Comparables can be difficult to find depending on the industry that the brand originates from. Some industries have publicly available transactions and many licensing agreements to use as comparables, while others may have very few or none at all.”

The cost approach:

The cost approach determines the value of a brand through deciphering what the overall

Financial Analysis



Source: Brand Finance

cost of building the brand is. It is defined under BSI ISO: 10668 as:

"The cost approach measures the value of a brand based on the cost invested in building the brand, or its replacement or reproduction cost... Note It is based on the premise that a prudent investor would not pay more for a brand than the cost to replace or reproduce the brand. The actual cost invested in the brand shall encompass all costs spent on building the brand up to the value date."

The cost approach is not typically relied on when determining a brand's value, but like the market approach, it is used in conjunction with and to help validate the income approach. To say it's an 'unjustifiable approach' is not quite right, "it's just less accurate and generally falls at the bottom," commented D'Souza and Sarna. The development and growth of a brand is difficult to replicate. It is therefore hard to establish a true replacement cost. "The volatility of the value of a brand is quite low because it is a unique asset which can't be copied," said Dailly when regarding the cost approach.

The income approach

The financial analysis of a brand valuation, or any valuation as a matter of fact, is the most popular. But it is the income method and the various methods recommended under the income approach which appear to be the most reliable; or perhaps to phrase it in a more neutral manner, consistent.

The income approach is defined under BSI ISO: 10668 as:

"The income approach measures the value of the brand by reference to the present value of the economic benefits expected to be received over the remaining useful economic life of the brand. The steps followed in applying the income approach shall include estimating the expected after-tax cash flow streams attributable to the asset over its remaining useful economic life, and converting these after-tax cash flow streams to present value through discounting with an appropriate discount rate. The cash flows (or an alternative measure of brand earnings) used in a brand valuation shall be those cash flows reasonably attributable to the brand. Various

methods are available to determine the cash flows."

Many contributors agree that this is the best approach and practice, but a subset of this approach – the royalty relief method – is considered to be the most effective. "The relief from royalty methodology has become the most mainstream method for valuing intellectual property in practice," commented D'Souza and Sarna. This method approximates the future royalties that the owner is relieved from paying by virtue of owning the brand, rather than having to licence it.

The royalty relief method is defined under BSI ISO: 10668 as:

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"...The value calculated through the royalty relief method, thus constitutes the present value of the royalty payments saved through the ownership of the brand. The royalty rate applied in the valuation shall be determined after an in-depth analysis of available data from licensing arrangements for comparable brands, an appropriate split of brand earnings between licensor and licensee, and shall be as close as possible to brands with the same characteristics and size as the brand being the subject for valuation."

This method is considered as being the most transparent of them all, an aspect which is key in any valuation. It is less volatile and tends to give a more consistent answer from year to year. Conveniently, it also provides some useful comparables for future valuations. But is it the most reliable? "I hesitate because all of the

methodologies have got things that can be criticised, depending on the circumstance," said Haigh. "There are a number of moving parts that form a view on what the correct royalty should be, but it can be easier, from an auditor's perspective, to audit the numbers that come out of the royalty relief method."

Summary

Brand valuation is not considered as a mainstream practice, but instead, a niche. In part, what the BSI ISO: 10668 standard has done is make it more conventional, which is a critical step. As many companies do not completely understand the value and strength of their brands, a main aim for valuers is "to transform organisations from being ones that see their main source of value as coming from tangible assets to being ones that see their value coming from intangible," said Dailly. However, this does require companies to buy into a different way of seeing and managing their business, which can be a tough nut to crack. But perhaps the BSI ISO: 10668 standard will solve this. It is also out there to bridge a gap between all parties where a brand valuation is relative and by that I mean, marketers, accountants, lawyers, market researchers and more senior company positions. The standard has also set out the important ways of valuing a brand, leaving plenty of leeway to use more technical analysis, making it an approachable and valuable resource.

Footnotes

1. Interbrand, *Brand valuation*, April 2004 pg 3
2. Provided by Ocean Tomo

Author



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