Need, Approaches and Methodology of Valuation of Brands

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Abstract

The wave of brand acquisitions in the late 1980s exposed the hidden value in highly branded companies and brought brand valuation to the fore. The values associated with a product or services are communicated to the consumer through the brand. Consumers no longer want just a product or service, they want a relationship based on trust and familiarity.

The task of measuring brand value is a complex one. Several models are available for accomplishing this. The most widely used is the brand-earnings- multiple model. There are several variants of this model. The market realities of the brand can also be captured through a SWOT Analysis of the brand, with respect to its marketplace.

***Key words**: Brand Performance Valuation, Capital Asset, Competitive Benchmarking, Economic Use Approach, Valuation of Brands.*

Brand- The Most Pivotal Capital Asset

The fact that the brand is an organization's capital asset scarcely needs emphasizing. In certain sectors, in fact, it forms the very lifeblood of the organization. Though factories and manpower may disappear, organisations still retain a name whose public reputation is one of enduring asset value. Think of powerful brands in India such as Sunlight of Hindustan Unilever's washing soap (no longer in existence, but still being remembered by consumers), Horlicks, Dettol, Lifebuoy, and so on.

"If this business were split up, I would give you the land and bricks and mortar, and I would take the brands and trademarks, and I would fare better than you." John Stuart, Chairman of Quaker (ca. 1900).

The above quoted statement clearly depicts the value of Brand. If all other capital assets are taken on one side and the Brand at the other, the latter side will be weighing more.The brand is a special intangible that in many businesses is the most important asset. This is because of the economic impact that brands have.

Ultimately, Brands are all about trust..

… the reason consumers flock to some brands and ignore other is that behind the brand stands an unspoken promise of value. That is way brands are becoming even more important drivers of growth. That is also why Hindustan Unilever wants Surf, Lux, Brooke Bond, Sunsilk, Knorr, … on its plate.

A brand is an experience: "A brand is essentially a container for a customer's complete experience with the offer and the company" –Sergio Zyman.

Value of Brands is due to

- Its ability to influence customers, employees, investors and all stakeholders
- Its Important even for non-profit organizations to attract sponsors, donations, etc.
- Brands contribute significantly to market capitalization.
- Companies with strong brands outperform the market in respect of several indices.

Need for Valuation of Brands

Brand valuation is needed under the following circumstances:

I. For Accounting Purposes

FAS 141 and IFRS 3 now require that the 'goodwill' in an acquisition be allocated to the intangible assets that the company is acquiring. This means that brand valuations are now a part of the commercial due diligence performed before an acquisition.

II. For Transactional Purpose

Transactions are generally of four types -licensing, acquisitions, securitization, ax-planning, Brand licensing requires an understanding of the economic benefit provided by the brand in order to establish an appropriate royalty rate. A similar logic applies to the acquisitions of branded companies when the brand represents a major asset in the transaction. Securitization involves raising funds against the security of future revenues. However, brands have rarely been used as the collateral for asset-backed securities. Brand-based tax planning is a relatively common practice in several countries. It involves transferring the ownership of the trademark and, usually, other forms of intellectual property to a central holding company that then charges a royalty for the use of these assets to the operating companies.

III. For Brand Management Decisions and Value-based Management

Approaches to Brand Valuation

There are two broad approaches to Brand Valuation viz.

I. Research-based Brand Equity Valuations and
II. Financially-driven Approaches.

Research-based Brand Equity Valuations

The distinct features of Research-based Brand Equity Valuations are:

- Consumer research to assess the relative performance of brands.
- These do not put a financial value on brands. They measure consumer behavior and attitudes that have an impact on the economic performance of brands.
- They try to explain, interpret and measure consumers' perceptions that influence purchase behavior.
- They include a wide range of perceptive measures such as different levels of awareness (unaided, aided, top of mind), knowledge, familiarity, relevance, specific image attributes, purchase consideration, preference, satisfaction and recommendation.
- Some models add behavioural measures such as market share and relative price.
- These approaches do not differentiate between the effects of other influential factors such as R&D and design and the brand.

Financially-driven Approaches

Financially driven approaches fall under four categories:

1. **Cost-based Approach**

This approach defines the value of a brand as the aggregation of all historic costs incurred or replacement costs required in bringing the brand to its current state. This approach fails because there is no direct correlation between the financial investment made and the value added by a brand.

2. **Comparables**

We need to arrive at a value for a brand on the basis of f something comparable. It is difficult - as by definition brands should be differentiated. The value creation of brands in the same category can be very different, even if most other aspects such as target groups, advertising spend, price promotions and distribution channel are similar or identical. Comparable can provide an interesting cross-check. It should never be relied on solely for valuing brands.

3. Premium Price

The value is calculated as the net present value of future price premiums that a branded product would command over an unbranded or generic equivalent. 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 approach is flawed, as there are rarely generic equivalents to which the premium price of a branded product can be compared. The price difference between a brand and competing products can be an indicator of its strength, but it does not represent the only and most important value contribution a brand makes to the underlying business.

4. Economic Use Approach

Approaches that are driven exclusively by brand equity measures or financial measures lack either the financial or the marketing component to provide a complete and robust assessment of the economic value of brands. The economic use approach was developed in 1988. It combines brand equity and financial measures. It has become the most widely recognized and accepted methodology for brand valuation. It has been used in more than 4,000 brand valuations worldwide.

The Economic Use approach uses the marketing and financial principles.

The Marketing Principle relates to the commercial function that brands perform within businesses. It assumes that

- Brands help to generate customer demand. Customer demand translates into revenues through purchase volume, price and frequency.
- Brands secure customer demand for the long term through repurchase and loyalty.

The Financial Principle relates to the net present value of future expected earnings. According to this principle, the Brand's future earnings are identified and then discounted to a net present value using a discount rate that reflects the risk of those earnings being realized.

Steps in Valuation of a Brand

The steps in valuation of a Brand include

I. Market Segmentation

Split the brand's markets into non-overlapping and homogeneous groups of consumers according to applicable criteria: e.g. product or service, distribution channels, consumption patterns, purchase sophistication, geography, existing and new customers. The brand is valued in each segment and the sum of the segment valuations constitutes the total value of the brand.

II. Financial Analysis

Identify and forecast revenues and earnings from intangibles generated by the brand for each of the distinct segments determined in Step 1. Intangible earnings are defined as brand revenue less operating costs, applicable taxes and a charge for the capital employed. The concept is similar to the notion of economic profit.

III. Demand Analysis

Assess the role that the brand plays in driving demand for products and services in the markets in which it operates, and determine what proportion of intangible earnings is attributable to the brand measured by an indicator referred to as the "role of branding index." The process is completed in two stages viz.

(a) identifying the various drivers of demand for the branded business and
(b) Determining the degree to which each driver is directly influenced by the brand.

Branding index represents the percentage of intangible earnings that are generated by the brand. Brand earnings are calculated by multiplying the role of branding index by intangible earnings.

IV. Competitive Benchmarking

Determine the competitive strengths and weaknesses of the brand to derive the specific brand discount rate that reflects the risk profile of its expected future earnings (this is measured by an indicator referred to as the "brand strength score").

This comprises extensive competitive benchmarking and a structured evaluation of the brand's market, stability, leadership position, growth trend, support, geographic footprint and legal protectability.

V. Brand Value Calculation

Brand value is the net present value (NPV) of the forecast brand earnings, discounted by the brand discount rate. The NPV calculation comprises both the forecast period and the period beyond, reflecting the ability of brands to continue generating future earnings.

Brand Valuation is useful in the following instances

- ✓ predicting the effect of marketing and investment strategies;
- ✓ determining and assessing communication budgets;
- ✓ calculating the return on brand investment;
- ✓ assessing opportunities in new or underexploited markets, and
- ✓ Tracking brand value management.

Brand Performance Valuation

A number of indices and techniques are available to measure brand performance. Some of them are given here under:

a. Landor Power Index,
b. Inter brand Valuation model,
c. Y&R Brand asset Valuator
d. Intangible Value Valuator

The Landor Power Index

This index equated Power with strength. The two synthetic measures are awareness and esteem. Index is built on 'Share of Mind' idea (cf. Share of Market, Share of Voice, Share of Requirements, etc.). Most influencing factor is brand perceived quality.

Interbrand's Brand Strength Attributes

Leadership (25%) Market share Awareness Positioning Competitor Profile	Internationality (25%) Geographic spread International positioning Relative market share Prestige Ambition
Stability (15%) Longevity Coherence Consistency Brand Identity Risks	Trend (10%) Long-term market share performance Projected brand performance Sensibility of brand Plans Competitive actions
Market (10% What is the market? Nature of market (e.g. volatility) Size of market Market dynamics Barriers to entry	Support (10%) Consistency of message Consistency of spending Above vs. below line Brand franchise
	Protection (5%) Trademark registration and registrability Common law Litigations/ disputes

Young & Rubicam's Brands set Valuator Power Grid

Brand Strength (Differential & Relevance)	Niche/ Unrealized Potential D R E K	Leadership D R E K
	New/ Unfocussed D R E K	Eroding Potential D R E K
Brand Stature (Esteem & Knowledge)		

Differentiation Relevance Esteem Knowledge

Summing-up

All of us have affirmation with the fact that a balance sheet discloses the financial position of a company. At the same time, it is also accepted that the financial position of an enterprise is influenced by the economic resources it controls, its financial structure, liquidity and solvency, and its capacity to adapt to changes in the environment. However, it is becoming increasingly clear that intangible assets have a significant role in defining the growth of a company. The strength of the invisible can't be denied.

The wave of brand acquisitions in the late 1980s exposed the hidden value in highly branded companies and brought brand valuation to the fore. The values associated with a product or service are communicated to the consumer through the brand. Consumers no longer want just a product or service, they want a relationship based on trust and familiarity. A brand is much more than a trademark or a logo. It is a 'Trustmark' - a promise of quality and authenticity that clients can rely on. Brand equity is the value addition provided to a product or a company by its brand name. It is the financial premium that a buyer is willing to pay for the brand over a generic or less worthy brand. Brand equity is, (not created overnight. It is the result of relentless pursuit of quality in manufacturing, selling, service, advertising and marketing. It is integral to the quality of client experiences in dealing with the Company and its services over a period.

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