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The International Brand Valuation Manual

A complete overview and analysis
of brand valuation techniques,
methodologies and applications



3

Brand Valuation Method and Process

AS WE SAW IN CHAPTER 2, THERE IS STILL A CERTAIN degree of generalized ignorance or skepticism surrounding valuation tools, at least among investors and corporate financial managers. In this chapter, we will discuss the possible uses of brand valuation, and examine the questions that should be answered before launching a brand valuation project.

3.1 Brand valuation process

Nearly 20 years after the debate generated by the RHM incident, there are still many brand valuation detractors. Patrick Barwise, Professor of management and marketing at London Business School, holds that brand value cannot be separated from business value and is reluctant to accept what he calls “theoretical brand valuations” (those that take place when a business is not being bought nor sold), preferring what he calls “brand evaluations” that use metrics as management tools (as

cited in McAuley, 2003). The problem is that over the last 20 years, brand valuation has often been misunderstood, and as a result, many industry players are skeptical about the use of valuation models. In this section, we will assess the current state of the debate on brand valuation, primarily from the user's standpoint, and examine the questions that ought to be answered before launching a project of this nature.

3.1.1 What is brand valuation?

Asset valuations are expert opinions on the asset's monetary value based on data analysis and assumptions rooted in a particular moment in time; this is so in the valuation of any kind of asset, work of art, wine or brand. Therefore, brand valuation may be defined as the process through which a qualified expert forms an opinion on the value of a brand, based on a set of premises or hypotheses, and taking into account the objectives, and audiences for which his or her expert opinion has been solicited.

3.1.2 The current debate: Why bother with brand valuation?

As we saw in Chapters 1 and 2, most top executives recognize that intangible assets, and brands in particular, play an important role in long-term financial success. This understanding has led to a growing interest in the appropriate tools for measuring their value, evidenced partly by the great number of articles and brand value tables recently published by business and marketing magazines such as *Business Week*, *Forbes* and the *Financial Times*. Figure 3.1 shows the vast increase in the number of brand value league tables seen in the last seven years.

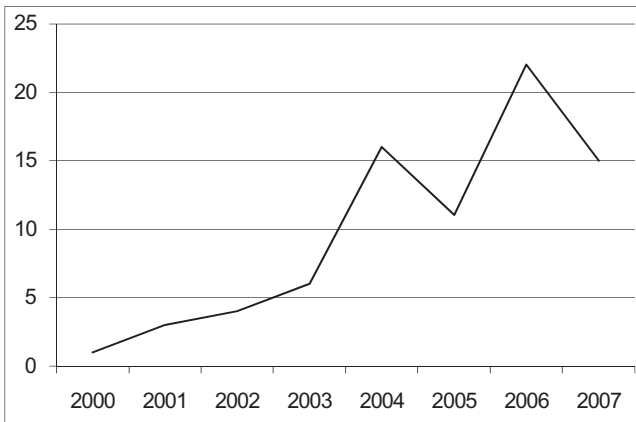


Figure 3.1 Evolution of the number of brand league tables published since 2000.

Source: Developed by author

But amidst the proliferation of new brand league tables, we face deeper questions: Is brand valuation necessary? In which circumstances? To satisfy which objectives?

As David Haigh and Jonathan Knowles suggested in a brilliant article entitled “Don’t Waste Your Time with Brand Valuation” in 2004:

Most companies do not need an answer to the question, *What is the value of my brand?* except for the specific purpose of accounting for goodwill after an acquisition. Rather, they need an answer to the question, *How – and for how much – can my brand contribute to the total success of my business?* It is this insight into the sources of customer value and the economic cost of delivering that value that will enable them to run more successful businesses (Haigh and Knowles, 2004b: 1).

These authors are part of a growing school of thought; one which holds that brand value on its own grants no more than

a chance to toot your own horn at a corporate cocktail party (Ehrbar and Bergesen, 2002; Haigh and Knowles, 2004b).

This is why clarifying the objective of a brand valuation is essential before embarking on these types of projects. We must answer the question: *What is the purpose of the valuation?* And we must distinguish between technical valuations (for accounting and transactional purposes) and brand management valuations.

The determination of the objective of the brand valuation exercise is closely related to the second key step in the process, given by answering the question: *What exactly are we valuing?* We must determine if we want to value the trademark or the entire branded business. The fuzzy definition of “brand” can often cause confusion here.

Once we have answered the previous two questions, we will be able to choose the methodology best suited to our objectives. This leads to a very important conclusion: that the selection of the brand valuation methodology will be contingent on the project’s objectives.

In the following sections, we will discuss the three key steps of a brand valuation exercise.

3.1.3 The purpose of brand valuation⁵

In the past 10 years, brand valuation techniques have become generally accepted tools with a wide range of applications. There are three major groups of applications:

⁵Based on Haigh and Knowles (2004b).

- valuations for brand management purposes
- valuations for accounting purposes
- valuations for transactional purposes.

Valuations for accounting or transactional purposes are done for balance sheet reporting, tax planning, litigation support, securitization, mergers and acquisitions, and investor relations. Thus, they focus on a value at a given point in time.

Valuations for brand management purposes are necessary for brand architecture, brand portfolio management, marketing strategy, marketing budget allocation and management scorecards. They are based on dynamic business models and on the role that the brand plays in the model's key variables.

3.1.3.1 Brand management

On certain occasions, brand valuation can be used as a management tool, and implemented to compare the levels of success of various brand strategies and the relative performance of different marketing teams. In this context, valuations have been used to defend marketing budgets, or to make decisions on brand extensions and architecture, as well as to measure the return on brand investment. But Ambler and Roberts (2006) point out several challenges to this usage (as cited in Salinas and Ambler, 2008). In general, when brand valuation is implemented for management purposes, the model will consider segmented values and sensitivity analysis, as the objective is to understand the impact that

different brand investment levels will have on the business performance.

3.1.3.2 Accounting purposes

New accounting standards require that all identifiable intangible assets of acquired businesses be recorded at their “fair value.” This breaks with the older practice of recording the purchase price in excess of the net acquired assets as a single figure under goodwill. Current regulations require that the value of acquired brands be included in the balance sheet. A recent example of this is South African Breweries’ acquisition of Miller Brewing Co. The Miller brand represents \$4500 million of the \$6500 million of intangible assets that appear in SABMiller’s 2003 balance sheet.

3.1.3.3 Internal or external transaction purposes

There are two types of transactions that may require a brand valuation: internal and external (see Figure 3.2).

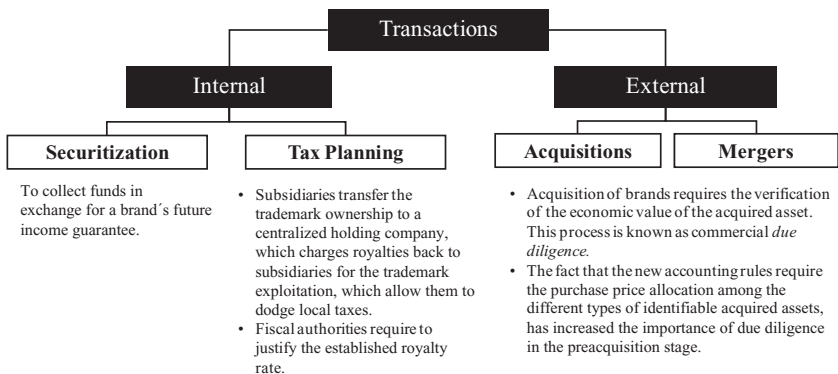


Figure 3.2 Transactional purposes: internal and external transactions.
Source: Based on Haigh and Knowles (2004b)

Internal transactions

The two most common types of *internal* transactions involving brands and trademarks are:

- Trademark-backed securitization and
- Tax planning.

In trademark securitization, funds are collected in exchange for collateral based on future revenues generated by licensing the trademark, i.e. trademark licensing royalties (Eisbruck, 2007). According to Hillery (2004), trademark-backed securitizations have not been as frequent as music or film; however, some high-profile examples of trademark-backed securitizations have recently been observed. According to this author, in 2003, Guess Inc. securitized royalty streams from 14 trademark license agreements for US\$ 75 million.

Brand valuation may also be used for *tax purposes*. Usually, subsidiaries transfer brand and other intellectual property assets to a centralized holding company, which charges operating companies royalties for the use of these assets, such that a portion of the operating companies' profits may evade local taxes. Of course, fiscal authorities require the justification of the brand value, to determine if it has been transferred to another fiscal jurisdiction by a fair value and to ensure that no fiscal obligations have been dodged.

External transactions

External transactions tend to take the form of *acquisitions* of companies with brands. In these cases, commercial due diligence is required in order to verify the economic value of the

acquired asset, and to substantiate negotiations of the terms of the transaction.

3.1.4 Defining the scope of valuation and the concept of brand

In Chapter 1, Section 1.1.1.3, we reviewed three alternative definitions of *brand*. Each definition has distinct implications as to what other intangibles need to be considered in the valuation. For example, a “trademark valuation” (definition 1) would require the valuation of other associated intellectual property separately (like a formula for example). In a “brand valuation,” (definition 2), there would be no need to value those other intangible assets separately. For example, in the valuation of a beer brand, the trademark and the formula would be valued jointly. Sometimes the *brand* is confused with the *business unit* that operates under the brand (definition 3). “Branded business valuations” (definition 3) are really no more than business or company valuations, commonly used in strategic and financial decision-making.

Most CEOs are primarily interested in the impact that different brand strategies can have on the value of the branded business. On other occasions, such as in the case of a company that decides to transfer brands for fiscal reasons, brands are valued independently.

3.1.5 Choosing an appropriate methodology

The valuation model to employ will depend on the answers to the two questions we have posed in this chapter regarding the purpose of the valuation and the scope of the concept of brand. Salinas and Ambler (2008) classify the applications or

purposes of brand valuation in two general categories: technical purposes and “other brand management purposes.”

Brand valuations with technical applications are generally undertaken for business combinations, impairment tests, tax planning, securitization, etc. They are therefore focused on a value at a given point in time. They commonly refer to the valuation of the *trademark* or *brand*. *Brand valuations for management purposes* are used for restructuring brand portfolios, performance evaluation and budget allocation. These valuations are typically based on dynamic models of the *branded business* and aim to measure *the role that the brand plays in the model's key variables*.

Previous research has shown the correlation between the type of application and the methodology of choice. Salinas and Ambler (2008) analyze the methods employed by a sample of commercial providers previously classified as “providers positioned in technical practices” and “providers positioned in management practices.” They conclude that most of the providers oriented towards technical applications applied the “royalty relief” methodology, while those providers more geared towards management applications favored methodologies that focused on measuring the role the brand plays in generating demand (“Demand driver analysis,” cf. Section 4.3.3).

Salinas and Ambler's findings (2008)⁶ are consistent with the opinions of other scholars who have noted the royalty relief

⁶Their results and research are based on previous research by Salinas, G. (2008) “Valoración económica de marcas: ¿existe un método óptimo para valorar marcas?” in *La comunicación empresarial y la gestión de los intangibles en España y Latinoamérica*, Pearson Educación, Madrid.

methodology as the methodology of choice for valuations with accounting and reporting purposes (Mard, Hitchner, Hyden and Zyla 2002; Woodward 2003; Anson 2005). The “Big 4” accountancy firms tend to view royalty relief as the most reliable method, from a technical perspective (cf. Harms, 2008).⁷

3.2 Conclusions

Before embarking on any brand valuation project, we must define the purposes of the valuation as well as the scope of the definition of the asset to be valued. Different objectives and applications will lead to different definitions of “brand,” and will determine the appropriate methodology to use. Methods valid for internal management purposes will not necessarily satisfy accounting requirements or tax regulations.

“Royalty relief” is the methodology most commonly used for technical valuations, while “brand management-oriented valuations” are typically based on dynamic models of the *branded business* and aim to measure *the role that the brand plays in the model’s key variables*.

⁷http://www.ey.com/GLOBAL/content.nsf/UK/CF_-_Services_-_SFS_-_Library_-_Methodology_-_Valuing_IP; [http://www.ey.com/global/content.nsf/WebPrint/8b8e23cdd699f2b680256cc5004dafbb?OpenDocument&Click=](http://www.ey.com/global/content.nsf/WebPrint/8b8e23cdd699f2b680256cc5004dafbb?OpenDocument&Click=;); <http://www.deloitte.com/dtt/newsletter/0,2307,sid%253D3631%2526cid%253D58029,00.html>.

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