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# Brand Valuation: Accounting Perspective

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### Abstract

Brands are one the most valuable assets for any business firm without any doubt. But this value is subjective in nature and it is very difficult to arrive at an absolute, quantified value for the treatment in financial statements. Last 3 decades witnessed the lots of debate in this area of discipline. This paper explores the evolution in the accounting for the brands in recent past and trouble with the valuation of brands. It also discusses briefly different approaches of brand valuation.

**Keywords:** Myntra, Brand, Wallet, Acquisition, Value

## 1. Introduction

Flipkart has bought a major stake in Myntra in a cash and stock deal that could value the company between $300-330 million (Firstpost.com, 21 May 2014).

Snapdeal buys Freecharge for $400m (Times of India, 9Apr 2015)

What makes above news interesting? By looking at these deals, one can wonder what makes these companies that much of worth? The net tangible assets possessed by these firms cannot justify these valuations. So, there must me something more than the tangible assets which enhanced the value of these companies. These can be termed as intangible assets which may include goodwill, customer base, patents, copyrights, staff capabilities, and above all the power of brands. As John Stuart, President Quaker Oats in 1922 said "If this business were to be split up, I would be glad to take the brands, trademarks and goodwill, and you could have all the bricks and mortar -and I would fare better than you." (Marquette, 1967). This paper will explore the Brand value aspect of this intangible asset. Before going into the details in the realm of brand value, it is imperative to understand the meaning of the brand.

## 2. Definition of Brand

Word brand has its root in German origin which means 'Burning'. Initially, this word was used for the identity marks made by burning iron on livestock or criminals for their easy identification. From there it is adopted in marketing.

Kotler defined brand from the marketing perspective which says "name, term, sign symbol (or a combination of these) that identifies the maker or seller of the product".

Seetharaman et al. in his article titled "A conceptual study on Brand Valuation" defined brand from the accounting perspective. They said "A brand can be defined as an asset that does not have physical existence and the value of which cannot be determined exactly unless it becomes the subject of a specific business transaction of a sale and acquisition." (Seetharaman, Nadzir, & Gunalan, 2001)

In simple words, brand can be defined as the name or symbol that is intended to identify goods or services of one seller from the other sellers.

## 3. Brand Value

Often a company's brand value exceeds its net tangible assets. There are many examples of such valuation in business history. Such as acquired acquisition of Kraft Foods by Philip Morris Co. at whopping $12.9 billion which included an estimated $ 11.6 billion for intangibles. The

Following table represents the value of some top brands:

Source : World Intellectual Property Report, Brands – Reputation and Image in the Global

Marketplace, WIPO Economics & Statistics Series, 2013

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**Table 1.** Brands account for a considerable share of companies' market capitalization(World Intellectual Property Organisation, 2013)

| Interbrand | | | BrandZ | | |
|---|---|---|---|---|---|
| Company | Brand Value 2103( In billion USD) | Brand value as a percentage of market capitalization | Company | Brand Value 2103( In billion USD) | Brand value as a percentage of market capitalization |
| Apple | 98.3 | 58.0% | Apple | 185.1 | 41% |
| Google | 93.3 | 20.7% | Google | 113.7 | 39% |
| Coca-cola | 79.2 | 39.3% | Coca-cola | 78.4 | 46% |
| IBM | 78.8 | 26.9% | IBM | 112.5 | 56% |
| Microsoft | 59.6 | 22.9% | Microsoft | 69.8 | 27% |
| McDonald's | 42 | 43.9% | McDonald's | 90.3 | 94% |

## 4. Historical Background of Accounting for Brand Valuation

Accounting for brand valuation is not a very old paradigm. In fact, a serious debate on this aspect started during the 1980s when many British companies started taking over other rival firms. Since the transaction amount involved in these acquisitions was often more than the book value of the target firm, it forced the practitioners to give an account to the difference in the book value and acquisition value. This difference was associated with the goodwill and required to be written off which gave birth to the controversy as under these accounting rules the money paid over and above the fair value of identifiable assets is money lost without a compensating asset being acquired. This often turned into huge losses during the year of acquisitions.(Farquhar, Han, & Ijiri, 1992).

Many British companies started protesting to these accounting rules. They argued that this was not goodwill alone but identifiable assets. They started reporting acquired brands in the financial reports. One of the instances can be traced back to 1985 when Reckitt & Colman accounted the value of Airwick trademark acquired from Ciba-Geigy on its balance sheet. In August 1988, likewise in 1988 Grand Metropolitan reported the value of several brands bought from Heublein at worth £588 million on its balance sheet.

Some British companies even capitalized their home-grown brands. RHM( Ranks Hovis McDougall's) with the consultation of Interbrand succeeded in placing value of all its brands, both acquired and home-grown worth £678 million on its balance sheet.

## 5. Accounting Treatment for Brand Value

Much of the controversy regarding the valuation of the brand is related to its recognition as an asset in balance sheet. Brands can be reported in balance sheet only after it is qualified under assets definition.

International Accounting Standards 38 deals with the treatment of the intangible assets. IAS 38 prescribes that recognition of an item as an intangible asset requires an entity to demonstrate that the item meets: (Ifrs, 2012)

(a) the definition of an intangible asset; and (b) the recognition criteria.

This requirement applies to costs incurred initially to acquire or internally generate an intangible asset and those incurred subsequently to add to, replace part of, or service it.

An asset is identifiable if it either: (Ifrs, 2012)

is separable, i.e. is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or

(b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

A brand meets both the above criteria of being treated as an asset. But IAS further recommends that an intangible asset shall be recognised if, and only if: (Ifrs, 2012)

(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and

(b) the cost of the asset can be measured reliably.(in case of internally generated intangibles The cost includes all the expenditures that can be attributed or allocated directly to creating, producing and preparing the asset from the date when the it was recognized as asset.

(Shodhganga))

Brand satisfies the first criteria, but it is very difficult to arrive at a reliable measurement criterion for the brand especially for home grown brands. For example, Coca-cola was established in the 1890s and since then it is has been continuously building its brand year after year. It is almost impossible to account all the cost incurred in the process of brand building with exact and reliable measures.

Apart from the measurement problems IFRS further dictates that "Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance shall not be recognised as intangible assets."(Ifrs, 2012)

In case of acquisition, the intangible assets shall be measured initially at cost. As per IAS 38 the cost of a separately acquired intangible asset comprises: (Ifrs, 2012)

(a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and

(b) any directly attributable cost of preparing the asset for its intended use.

## 6. Approaches to Brand Value Measurement:

There are numerous ways to measure brand value. Some of the prominent are following:

- Valuation based on Cost

Under this method the brands can be valued at either the actual cost incurred in the acquisition, building or maintenance of the brand or at the cost which would be incurred in case of recreating the brand in present business and economic conditions. The drawback of this method is that if we measure on the basis of actual cost it is not of much relevance with the passage of time and in case of replacement basis it is very complex to arrive at exact cost of recreating a brand under current situation.

- Valuation Based on the Premium Pricing

Under this method, it is assumed that brands hold a premium over the unbranded items.

The difference between the branded and unbranded products gives the base for valuation.

The major drawback of this method is that many brands do not have any unbranded rival.

Such as Boeing don't have any unbranded counterpart.

- Valuation Based on Market Value:

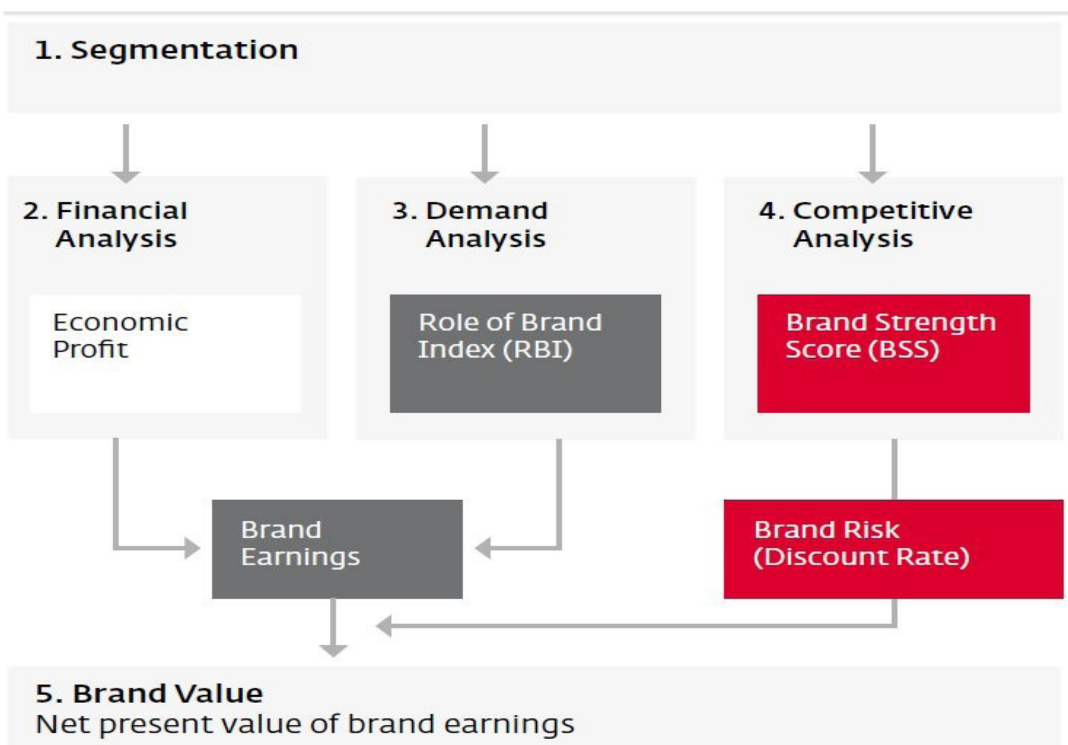


Figure 1.

This method is based on objective market value. It is one of the most logical methods since it provides the opportunity to compare across the companies and over a period of time.

- Valuation Based on Consumer Factor:

Consumer's perception and feelings towards the brand can also be used to measure the brand value. The biggest drawback of this method is that it is subjective in nature.

- Valuation Based on Future Earning Capacity:

It is one of the most appropriate method brand valuation and followed by practitioners widely. However, the biggest problem with this method is the assumption which it makes

i.e. the past trend is going to continue in future also without any change.

## 7. Interbrand's Approach to Brand Valuation

Interbarnd uses three components in their valuations of brands. These are : financial performance analysis, the role of brand in purchase decisions, the competitive strength of brands. These components are measured with respect to segments. ("interbrand brand valuation methodology," n.d.)

- Segmentation

It is defined in terms of customer group, geography, SBU, product or service category. Each segment analysed on every component i.e. financial performance, the role of brand and brand strengths.

Following figure represents the scheme of brand valuation by Interbrand:

Source: **Brand Valuation,** A versatile strategic tool for business, Interbrand(2014)

- Financial Analysis

It measures the overall economic profit.

- Role of Brand in Purchase Decisions

It measures the part of purchase decisions which can be attributable to the brand in comparison to other factors such as price, product features and convenience.

- Brand Strength:

Interbrand lists set of ten factors under categorized in internal and external factors:

- **Internal Factors:** ○ **Clarity** ○ **Commitment** ○ **Protection** ○ **Responsiveness**
- **External Factors** ○ **Authenticity** ○ **Relevance** ○ **Differentiation** ○ **Consistency** ○ **Presence** ○ **Understanding**

## 8. Benefits of Brand Valuation

The major benefits of brand valuations are :(Wood, 1995)

- It provides a realistic view of shareholder's funds
- Brand valuation gives a logical base to compare the firms operating in similar markets.
- Gives opportunity to raise capital easily by reducing gearing ratios
- Gives platform to compare brands across the portfolio · Help in future planning for brand management.
- Help in allocating the marketing resources accordingly
- It is useful in making the decision regarding the merger and acquisitions.
- It helps in raising funds by showing the worth of brand more clearly

## 9. Conclusion

In current business scenario brands are one of the most valuable assets for a company. A strong brand gives a sustainable competitive advantage. For marketers, the brands were always of valuable but the accounting treatment of the brand is still not considered as it should be. The problem with the accounting of brand lies in the very nature of brand itself. Since it is more of subjective in nature, it becomes very difficult to arrive at a universally acceptable quantified value of any brand. In case of acquired brand, it is a bit easy to determine the value of brand but for home grown brands it not as straight forward. Various institutions are working in the direction of finding a suitable and universally accepted method for treatment of brand value in financial statements.

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