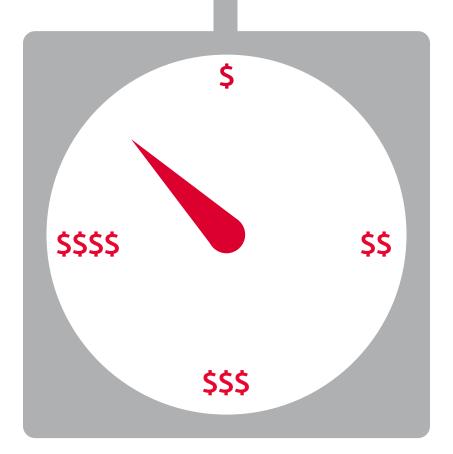
Financial applications for brand valuation

Delivering value beyond the number

Creating and managing brand value™

Interbrand



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Delivering value beyond the number

by Mike Rocha

Compared to when Interbrand first pioneered brand valuation in the 1980s, the global business community now widely accepts the importance and value of strong brands—and the significant contribution they make to business value.

This has resulted in an increasingly wide range of business applications for brand valuation, which can broadly be categorized into three areas:

- Brand management
- · Strategy/business case development
- Financial

From a brand management perspective, brand valuation is a strategic tool that brings together market, brand, competitor, and financial data into a single, value-based framework within which the performance of the brand can be assessed, areas for

improvement identified, and the financial contribution of the brand to business results quantified.

From a strategy and business case development perspective, the same data can be used to assess strategic options and create a business case for brand change. By combining strategy, analytics, and valuation to determine the expected impact of brand investment on the top and bottom line, while also quantifying the expected change in brand and business value, a case for investment can be made with language and data that is more likely to persuade the board and senior management.

Finally, a wide range of financial applications for brand valuation has grown over time, driven by a number of factors including (but not limited to):

- An ever-increasing emphasis on brands in *investor communication*s and annual reports
- Brands driving significant premiums in M&A
- The centralization of brand-related intellectual property governance and management, often in offshore locations for tax purposes, requiring both valuations and the setting of appropriate royalty rates
- Brand assets increasingly being considered as acceptable security for asset-backed financing
- Accounting standards requiring balance sheet valuation of brands and other intangible assets following an acquisition

	Brand Management	Strategy/Business Case Development	Financial
Applications	 Brand performance management Brand portfolio management Brand roadmap development Resource allocation Brand tracking/dashboards Return on investment analysis Sponsorship evaluations Senior management KPIs 	 Brand positioning Brand architecture Brand extension Brand launch Business case for brand investment 	 Investor relations Mergers & acquisitions Licensing/royalty rate setting Tax valuations/transfer pricing Balance sheet valuations Asset-backed financing
Typical Frequency	Recurring	One-off	One-off
Primary Objective	Ongoing brand management leading to insight and recommendations to grow brand value	Business case connecting brand change/investment to expected financial results	A robust value with supporting analysis

Figure 1. Brand valuation applications

Interbrand brand valuation methodology overview

Strong brands usually enhance business performance by influencing three key stakeholder groups, whether current or prospective: customers, employees, and investors. They influence customer choice and create loyalty; attract, retain, and motivate talent; and lower the cost of financing.

The influence of brands on current and prospective customers is a particularly significant driver of economic value. By expressing an authentic, relevant and differentiated value proposition consistently across all touchpoints, brands help shape attitudes and, therefore, purchase behavior, making products and services less substitutable and demand more sustainable (especially when faced with competitor pricing and promotions). By driving choice and enabling price premiums, brands enable their owners to enjoy higher returns. Strong brands also create continuity of demand, thus making expected returns more likely—or less risky. Brands, in short, create economic value by generating higher returns and growth, and by mitigating risk.

has been specifically designed to take all of these stakeholders and value-creation levers into account. **Role of Brand** analysis is critical to understanding purchase behavior, assessing the brand's influence on the factors that drive demand and choice. **Brand Strength** analysis measures the ability of the brand to create continuity of demand into the future and its potential to reduce risk. It takes both "internal" (management and employee) and "external" (customer) factors into account. Finally, these inputs are combined with an in-depth financial model of the business to measure the brand's current and future ability to create economic value for its owner.

Interbrand's brand valuation methodology

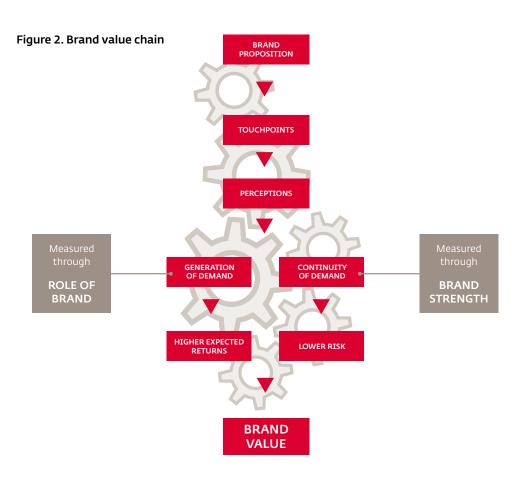
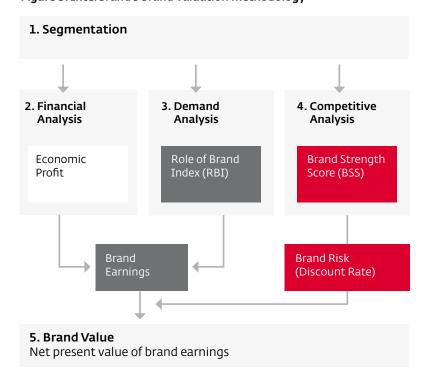


Figure 3. Interbrand's brand valuation methodology



Delivering value beyond the number

An important output of our valuations is a rigorously analyzed and defendable valuation number. What differentiates us from our competitors is our ability to also provide a rich and insightful brand analysis, delivering value to the business beyond the number alone.

Interbrand's brand valuation methodology builds a rich understanding of how a brand performs—and should perform—to create economic value. Our approach differs from others because our Brand Strength and Role of Brand analyses also act as diagnostic tools, allowing us to better understand the factors underlying a brand's strengths and weaknesses, both internally and externally.

Armed with these insights, and by leveraging our global expertise in creating and managing brands, we then deliver recommendations on how to increase brand value and, most importantly, the impact of the brand on business results. This means the valuation exercise delivers value to the business far in excess of the valuation number alone.

Case study 1: Securing the future for the employees of a UK insurance brand

Enabling trustees to assess a proposed pension fund deficit recovery plan that used the brand as security

Interbrand was retained by the trustees of a UK insurance provider's pension fund to assess a proposed Asset-Backed Funding (ABF) structure to eliminate the fund's deficit. The proposal involved the use of the brand asset as security to generate an income stream that would be used to fully offset the deficit over a 25-year period, with the fund granted security over the core brand assets.

Unclear whether this was in their members' best interests, the trustees came to us for an assessment of:

- The current value of the brand ("base case")
- The minimum realizable value of the brand in a "distressed sale" scenario

 An assessment of the likelihood of a brand value decline of a scale that would prevent the fund from recovering the value of its security through the sale of the brand

In addition to this, our valuation report included an in-depth assessment of the brand through the lens of Interbrand's Brand Strength framework. This resulted in a number of key insights and recommendations relating to the management of the brand. These findings were separately presented to the brand and marketing teams at the company.

"An important output of all of our valuations is a rigorously analyzed and defendable valuation number. What differentiates us from our competitors is our ability to also provide a rich and insightful brand analysis, delivering value to the business beyond the number alone."

Case study 2: Advising pre-IPO negotiations over ownership and control of a brand

Arming a CEO during a brand's IPO negotiations by quantifying the importance of the brand to business results

Prior to its IPO, a brand's CEO and management team came to us for help with a unique challenge—it shared control over its brand name and key visual brand assets with a third party who could technically revoke their usage. As the IPO approached, the company had entered into negotiations with the third party to clarify ownership of the brand and ensure complete security over its future use. Interbrand was asked to analyze five assertions at the heart of the negotiations:

- 1. Trust (among customers, general public, and employees) in the brand was high and the brand was highly distinctive of the business.
- The brand was a business asset with significant value, which made a sizable contribution to the company's business performance
- 3. Rebranding the business would be expensive (especially with time constraints)
- Rebranding could result in the loss of customer goodwill and loyalty (i.e. potential loss of business value)
- Uncertainty in the ownership of the brand would introduce risk, potentially undermining the value of the business on IPO

A particular challenge was the modeling of potential business value at risk should control over the brand be lost (i.e.

requiring a full rebrand). To adequately assess the level of risk, we devised three potential scenarios, leveraging rebranding case studies, an analysis of the strength of the brand and how it worked to influence customer purchase decisions, together with an understanding of the business model as well as industry and competitive trends. Working closely with the brand's finance team, Interbrand developed a range of scenarios for the potential business value at risk. Due to their sensitivity—and given the imminent IPO and the importance of the negotiations, the valuation analysis and findings were rigorously scrutinized by the brand's senior management.

Our analysis played a pivotal role in supporting the brand's claim to full ownership control, and the CEO used our report to help support the company's position during the negotiations. From a business perspective, the IPO was successful and one of the most heavily subscribed listings of the year.

¹ The royalty relief approach is based on an estimation of the royalties the brand owner would have to pay if it were the licensee of the brand rather than the owner. It involves estimating likely future sales, applying an appropriate royalty rate to them and then discounting the estimated future, post-tax royalties, to arrive at a net present value, which is considered to represent brand value. The royalty relief approach does not yield the brand management insights that Interbrand's proprietary methodology does, but we occasionally use it for financial valuations or as a secondary, supporting methodology.

Case study 3: Quantifying royalty rates for a global business-to-business conglomerate

Developing a framework to determine and support internal royalty rates to the tax authorities

An international B2B business asked Interbrand to recommend royalty rates to be charged to operating entities within the group for the use of its master brand. The task was complicated by the size and complexity of the enterprise, which operated across numerous sectors and countries. In addition, the business employed a variety of brand architectures, making greater or lesser use of the master brand alongside other brands in its portfolio.

We began by clustering different business units for analysis based on the extent of their connection to and use of the master brand, as well as how much of their business was in the brand's home market (where it was significantly stronger than elsewhere). For each of these clusters we identified the brand-related intangibles being used, and which part of the group was responsible for creating and developing these assets.

We then conducted an extensive search for comparable licensing agreements across several databases in order to identify a short list of agreements that were sufficiently comparable to be used as benchmarks.

Finally, we determined three levels of royalty rates and established criteria for determining which rate would be applicable based on:

- Brand architecture—level of use of the master brand
- Strength of the master brand in the market (taking geographic proximity to the home market into account)
- 3. Profitability of the business

Based on these royalty rates, we also conducted a valuation of the brand using the royalty relief methodology.¹ Our findings were presented to the head of tax and his team, and have been implemented to set royalty rates for the brand across the business.

Case study 4: Supporting the recapitalization of a major UK bank

Determining a brand's fair market value to inform recapitalization negotiations

A UK bank approached us in the aftermath of a significant acquisition that had gone sour and was threatening the very existence of the business and brand. A number of recapitalization options were being considered, one of which involved the bank's ultimate owner injecting approximately £1bn (approx. USD \$1.6 billion) into the bank. Part of this proposed deal involved transferring the bank's trademarks to its owner. The owner would then license the trademarks back to the bank in perpetuity on a royalty free basis. Interbrand was engaged to assess the fair market value of the trademarks.

We worked closely with senior management, within extremely tight timelines, to conduct the valuation. We also conducted an indicative valuation of the banking business operating under the brand and compared this value to the value of the trademarks as a "reasonableness" check. Due to the nature of the transaction, the trademarks were valued using the royalty relief methodology, which assumes the

trademarks will be licensed, as was to be the case in this situation. Assessing the competitive strength of the brand using Interbrand's Brand Strength framework helped to inform the royalty rate used for the valuation and highlighted areas of improvement for the brand.

In order to answer specific questions from the owner's legal team, we also valued the trademarks using a range of alternative scenarios, based on the likely value to different types of buyers and under a range of potential uses for the trademarks.

Our valuation report was delivered to senior stakeholders (including finance and marketing teams) at the bank, and our analysis and findings were accepted without adjustment. The valuation supported the recapitalization negotiations, which were successfully concluded with a total of £1.5bn (approx. USD \$2.4 billion) of Tier 1 capital ultimately being injected into the business.

Internal Factors

Clarity

Clarity internally about what the brand stands for and its values, positioning, and proposition. Clarity too about target audiences, customer insights, and drivers. Because so much hinges on this, it is vital that these are articulated and shared across the organization.

Commitment

Internal commitment to brand, and a belief internally in the importance of brand. The extent to which the brand receives support in terms of time, influence, and investment.

Protection

How secure the brand is across a number of dimensions: legal protection, proprietary ingredients or design, scale or geographical spread.

Responsiveness

The ability to respond to market changes, challenges, and opportunities. The brand should have a sense of leadership internally, and a desire and ability to constantly evolve and renew itself.

External Factors

Authenticity

The brand is soundly based on an internal truth and capability. It has a defined heritage and a well-grounded value set. It can deliver against the (high) expectations that customers have of it.

Relevance

The fit with customer/consumer needs, desires, and decision criteria across all relevant demographics and geographies.

Differentiation

The degree to which customers/consumers perceive the brand to have a differentiated positioning distinctive from the competition.

Consistency

The degree to which a brand is experienced without fail across all touchpoints or formats.

Presence

The degree to which a brand feels omnipresent and is talked about positively by consumers, customers, and opinion formers in both traditional and social media.

Understanding

The brand is not only recognized by customers, but there is also an in-depth knowledge and understanding of its distinctive qualities and characteristics. (Where relevant, this will extend to consumer understanding of the company that owns the brand.)

Figure 4. Interbrand's Brand Strength factors



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Mike leads Interbrand's brand valuation practice globally, providing overall strategy, thought leadership and consistency across its network.

He has over ten years of experience in understanding and measuring the value of brands, their impact on business performance and in uncovering insights from the valuation process to drive brand value growth.

