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Debunking the Myth That Business Appraisers Lowball Brand Values

By Christof Binder, Ph.D., MBA

How does something as emotional and intangible as brands and someone as fact-based and conservative as an accountant fit together? Not particularly well, according to marketers and brand valuation specialists. When they say "accountant," they're talking about valuation professionals outside the world of marketing.

"Most accountants are very conservative and habitually underestimate the level of income attributable to brands they value. They also tend to assume very short useful economic lives, low growth rates and high discount rates. It is therefore no surprise that an analysis of brand values calculated for balance sheet purposes tends to undervalue brands,"[1] says David Haigh, CEO of Brand Finance plc, a world-leading independent brand valuation and strategy consultancy.

Reasons for the mistrust. There are three major reasons for marketers mistrusting and disqualifying business valuation professionals in relation to valuing brands. First, CMOs and marketers want to stay in control of measuring and valuing their most important assets, instead of leaving it to the finance and accounting folks. Second, specialized brand advisory and valuation firms want to sell their own services and grow their business. And, third, the mistrust is a long and profound belief based on flawed facts.

Fifteen years ago, the major intention of the implementation of FAS 141 and IFRS 3 was to reduce the portion of goodwill reported in acquisitions. Some commentators—as well as marketers—were surprised to see that 45% of the enterprise value of acquired businesses on average remained allocated to goodwill. They had expected to see larger amounts being allocated to identifiable intangible assets, including brands, and amounts allocated to goodwill to disappear. Realistically, 45% of enterprise value on goodwill is certainly not too much, considering the synergies expected from a business combination, the value of the assembled workforce, and all of the future value from human and organizational assets, including the ability to improve, innovate, adapt, and change over the long term. Even with a sympathetic understanding for the role of marketing, brands have nothing to do with these components of goodwill.

Follow the money. From the countless brand value rankings they produced, brand valuation specialists concluded that the adequate average portion of brand value is 18% of enterprise value. Various studies on the results of purchase price allocations (PPAs) from Houlihan Lokey, PwC, EY, and others, show an average portion of brand of only around 10%, thus far less than the brand valuation specialists. The myth of the conservative accountant was born. But which party is right? Actually both, provided that we do not compare apples and oranges.

In all PPA studies, 40% of the cases observed do not report a brand value for three reasons. The brand is unimportant and will be replaced after the acquisition or because the acquisition was an asset deal that did not include a brand or trade name. In

1 brandfinance.com/news/press-releases/why-variation-supports-the-need-for-brand-valuation/.

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contrast, all cases sitting on brand rankings show a brand value. Furthermore, enterprise value in PPAs is different from nontransactional enterprise value for the control premium paid. This premium accounts for an average 35% on top of the share price prior to the announcement of the transaction. And, thirdly, there is an effect of sample composition. Adjusting for these effects, brand values found by "accountants" are in fact not lower but most comparable to those found by brand valuation specialists.

But that is not all. According to MARKABLES, the 100 most expensive brands acquired in business combinations since 2010 account for an average 34% of enterprise value.[2] Adjusting for the purchase premium, this percentage would amount to 46% to be fully comparable with the brand value rankings. Moreover, a comparative study[3] of 162 brand valuations reveals that accountants reported even higher brand values than brand valuation specialists in one-third of the cases.

As a matter of fact, accountants and business valuation professionals are neither more nor less conservative to value brands than brand consultants or marketers. There is no reason at all for accountants and business appraisers to stand in the shadow of specialized brand valuation firms. And marketers should finally begin to accept business appraisers, corporate finance advisors, and accountants as unbiased and experienced partners to value their most important assets: brands and customer relations. They have one important advantage over specialist brand valuators: They understand the value of all different assets of an enterprise and not only that of brands. ◆

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2 www.markables.net/files/Top-2014-Brand-Ranking.pdf.

3 www.markables.net/brand_value_rankings_are_they_blessing_or_curse.