Variation in Brand Valuation: Indian IT Services Brands

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Owing to the CoronaVirus lockdown in India, Manas Das, the Founder and Chief Executive Officer (CEO), ValuEndow Consulting couldn't physically meet his team to discuss some exciting business opportunities. While scanning through public sources, he came across an interesting area and less understood topic called 'Brand Valuation'.

Manas set a video conferencing call at 10.00 IST on Sunday, 29th March 2020 to gather views on the "Brand Valuation" of IT companies in India. He opened a discussion on Brand Valuation and he said: "I am extremely disappointed to see limited Indian Brands figuring in the Global 500: 2020[i] - a brand valuation report of Brand Finance". However, "I am quite excited to locate Tata Consulting Services (TCS), Infosys, HCL, and Wipro in the top 10 most valued global 'IT services brands' in the report "IT Services 25: 2020" by Brand Finance[ii]".

After a strong and meaningful deliberation, Manas asked Sheikh Sanah, a young officer from the Business Development & Marketing group to look deeper into the brand valuation process, methodologies, and assigned brand value by Brand Finance. Further, Sanah was asked to carefully review the valuation approaches of Kantar Millward Brown (Kantar), a multinational market research firm, which was popular for ranking the top global brands. Sanah was asked to conduct a diligent study and find out the reasons for the differences between the brand valuation methods followed by Brand Finance and Kantar, and suggest how Indian IT firms can improve their brand value. Sanah agreed to present her report and findings in the next meeting scheduled on 5th May 2020.

Brand Valuation

To develop a better understanding of the subject matter, Sanah started reviewing ISO 10668[iii] - the standard set for monetary brand valuation, "*The term 'brand' is defined in the Standard as a marketing-related intangible assets that may include names, terms, and logos that are intended*

to identify goods and create distinctive images and associations in the minds of stakeholders, thereby creating economic benefits for the owner". Branding literature suggested multiple approaches including Income Approach, Market Approach, and Cost Approach for brand valuation[iv].

She scanned through published reports of Brand Finance and thoroughly looked at "The annual report on the most valuable and strongest IT services brands in 2020". Indian IT Services Brands like TCS, Infosys, HCL, and Wipro registered positive 'Brand Value' growth (*Exhibit-1*). In the 2020 rankings, IBM was leading the table with a brand value of $25.29 billion followed by Accenture ($21.18 billion), and TCS ($13.49 billion). The top ten companies in the list included four companies each from the USA and India.

As per Brand Finance, 'Artificial Intelligence' and 'Cloud Services' boosted the brand value of Accenture and TCS. IBM continued to lead by investing in brand asset acquisition, especially in cloud services. On July 9, 2019, IBM acquired Red Hat for $34.8 billion[v]. Red Hat's architecture allowed clients to build an application once and run it anywhere. This acquisition was expected to strengthen IBM's position in the $1.2 trillion hybrid-cloud market. IBM generated intangible asset value of $13.47 billion generated from the acquisition of Red Hat.

India-based HCL , which was ranked ninth on the list, acquired Strong Bridge Envision, a US-based digital and analytics consulting services firm for Rs. 3110 million[vi] (approx. $41 million). The acquisition was expected to strengthen HCL's brand through technology architecture, data and analytics[vii]. India-based Wipro, which was at the tenth position on the list acquired several companies like Designit, Appirio, Cooper, Infoserver, Syfte, and International TechneGroup. These acquisitions strengthened Wipro's position in design and business strategy consultancy, digital engineering and manufacturing solutions, and strengthened Wipro's position in digital solutions space.

TCS - another Indian company, which was at the third position on the list, acquired the London-based W12 Studios Limited for Rs.660 million[viii] (approx. $8.7 million). This was expected to strengthen its brand portfolio, brand reputation, and brand value. Infosys, which occupied the fifth place on the list invested in several brand acquisitions including WongDoody, HIPUS Co., and Outbox Systems Inc.

Infosys through its wholly-owned subsidiary Nova Holding acquired Outbox Systems Inc. (renamed Simplus), with expertise in Salesforce domain for US$ 250 million[ix].

In 2020 ratings, TCS retained its Brand Strength rating of AAA-, whereas both Accenture and IBM fell from AAA. According to David Haigh, CEO of Brand Finance, "TCS was well placed to leverage its existing brand strength in the strategic sector of the future economy". Despite IBM's Brand Value erosion, there was a huge gap of $11.8 billion between IBM and TCS. In the

2020 Ranking, Infosys, TCS, HCL, and Wipro registered brand value growth of 9 percent, 5.3 percent, 5.2 percent, and 8 percent respectively compared to 2019.

Sanah scanned through Kantar's Top 75 most valuable Indian Brands -2019 (BrandZ) and found that TCS, Infosys, HCL and Wipro occupied third ,11th, 41st , and 32nd places with the brand value of $18.16 billion, $5.17 billion, $1.6 billion, and $1.9 billion respectively (**Exhibit 2**). Sanah noted that Kantar valued TCS at $5.34 billion more than Brand Finance's value in 2019. On the contrary, Brand Finance valued Infosys at $1.3 billion higher than Kantar's valuation in 2019.

Sanah was surprised to see the wide variations in the brand value of TCS and Infosys. She was wondering what could be the reasons behind such variations in brand values. Could it be ascribed to different valuation methodologies adopted by the prominent brand valuation firms?

She reviewed the financial performance of the concerned companies and observed that the brand values of TCS, Infosys, HCL, and Wipro were lower than the revenues (**Exhibit 2 and 3**) generated by these companies.

Brand Valuation Methodology

Brand Finance

Brand Finance used the 'Royalty Relief' approach to derive brand value based on which the brand league table was prepared. The approach involved projecting the future sales attributable to a brand. Further, the concept assumed a royalty rate, if it had licensed from an unrelated party. See Exhibit 4 for the formula for calculating brand value.

The forecast royalties were discounted post-tax to a net present value, which represented the current value of the future income attributable to the brand asset.

Kantar Millward Brown

BrandZ™- was a proprietary product that uniquely measured brand appeal to existing and potential customers and validated it against actual sales performance. Brands that were successful in building strong tractions primarily remained:

Meaningful

Meaningfulness is a combination of emotional and rational affinity. In any specific category, a brand must appeal more, create excitement, and generate greater "love", and meet or exceed the individual's needs and expectations on a sustainable basis.

Different

A brand needed to remain relevant and unique -- in a positive way "set the trends," and offer considerable and visible benefits to consumers to stay ahead of the curve.

Salient

A brand must do sufficient groundwork to strike the mind of the consumer spontaneously.

The Valuation Process[x]

Financial Value Calculation

Kantar calculated corporate earnings, attribution rate, and branded earnings. Further, Brand Multiples were calculated using the Bloomberg data. Branded Earnings multiplied by 'Brand Multiple' produced 'Financial Value'.

To strengthen the valuation process and bring appropriate results, BrandZ considered customers' viewpoints toward the sales and any additional premium delivered by positive brand associations. BrandZ calculated 'Brand Contribution', which was expressed as a percentage of 'Financial Value'.

Brand Value: To derive 'Brand Value', 'Financial Value' was multiplied by 'Brand Contribution'. Brand Value was the dollar amount a brand contributed to the overall value of a corporation, which reflected the contribution of intangible assets toward shareholder value.

Interbrand Brand Valuation

Sanah came across Interbrand's brand valuation[xi] but the concerned Indian IT brands didn't feature in the Interbrand's Brand raking report. However, she felt including the brand valuation method of Interbrand in her report for deeper study.

The brand valuation method[xii] by the Interbrand (Exhibit 5) is presented below:

Operating Profit –Taxes = NOPAT
NOPAT - Weighted Average Capital Cost = Economic Profit
Economic Profit x Role of Brand = Branded Earnings
Branded Earnings x Brand Strength x Discount Rate = Brand Value

Sanah gathered financial details for HCL (***Exhibit-6***) to calculate the brand value for 2020 and 2021. Through her sources, she found that brand strength for the IT industry in India was in the range of 70-80. Further, the role of brand and discount rate were in the range of 65-80 percent and 2-3 percent, respectively.

Pressing Issues

Sanah thought she had put in all the hard work to crack the brand valuation puzzle. She learned from literature that the "marketing investment in a brand, price, revenues, and perceived quality – have statistically significant effects on brand value"[xiii]. Sanah was almost ready for her presentation, but the following questions were still bothering her:

What is the role of revenue in the brand valuation in general and Indian IT companies in specific? How should she calculate the brand value of HCL for 2020 and 2021?

The more Sanah explored the brand valuation practices; she felt that the area was less explored. After putting serious efforts, she was still unsure of the right brand valuation method. She rang up Manas a week before the scheduled meeting and said: "I am ready for D-day, but I am still searching for answers to a few questions". Manas assured her that her work would impress the team. Sanah said: "I am feeling jittery and am keeping fingers crossed"!

Exhibit 1: Top 10 Global IT Services Brands as per Brand Finance

2020 Rank	2019 Rank	Brand	Country of Origin	2020 Brand Value ($ million)	2019 Brand Value ($ million)	Brand Value Change	2020 Brand Rating	2019 Brand Rating
1	1	Accenture	United States	25,294	26,292	-3.8%	AAA-	AAA
2	2	IBM (IT Services)	United States	21,188	20,367	4.0%	AAA-	AAA
3	3	TCS	India	13,499	12,815	5.3%	AAA-	AAA-
4	4	Cognizant	United States	8,573	8,704	-1.5%	AA+	AA+
5	5	Infosys	India	7,087	6,501	9.0%	AA+	AA+
6	6	Capgemini	France	6,630	5,922	12.0%	AA+	AA
7	7	DXC Technology	United States	5,830	5,525	5.5%	AA-	A+
8	9	NTT Data	Japan	5,058	4,266	18.6%	AA-	AA-
9	8	HCL	India	4,889	4,648	5.2%	AA+	AA
10	10	Wipro	India	4,324	4,002	8.0%	AA+	AA+

Source: Brand Finance

Exhibit 2: India's Most Valued IT Services Brands by Kantar Millward Brown

2019 Rank	Brand	Country of Origin	2019 Brand Value ($ million)	2018 Brand Value ($ million)	Brand Value Change
3	TCS	India	18,161	14,995	21.11%
11	Infosys	India	5,170	3,994	29.44%
41	HCL	India	1,618	1,446	11.89%
32	Wipro	India	1,907	1,665	14.53%

Source: Kantar Millward Brown

Exhibit 3: Revenue of TCS, Infosys, Wipro, and HCL

(Value in USD million)	TCS		Infosys		Wipro		HCL	
	2019	2018	2019	2018	2019	2018	2019	2018
Revenue	20,913	19,089	11,799	10,939	8,457	8,354	8,632	7,838
Cost of revenue	12,160	11,054	7,687	7,001	5,962	5,912	5,478	5,128
Gross Profit	8,753	8,035	4,112	3,938	2,495	2,442	3,154	2,709
SG & A expenses	3,406	3,305	1,416	1,279	1,098	1,173	1,028	913
Operating income#	5,347	4,730	2,696	2,659	1,397	1,269	2,127	1,797

#excluding other income

Source: Compiled from annual reports of TCS, Infosys, Wipro, and HCL

Exhibit 4: Calculating Brand Value

$$Brand\ Value = Brand\ Strength\ Index\ X\ Brand\ Royalty\ Rate\ X\ Brand\ Revenue$$

Steps Involved

a. ***Calculating Brand Strength Index (BSI):*** To calculate BSI (0 to 100), Brand Finance used a balanced scorecard based on key indicators such as brand investment, brand equity, and brand performance.

b. ***Determine Brand Royalty Rate:*** Revenue split analysis and comparable market transactions such as existing licensing agreements at the firm or industry level were used to determine the royalty rate. The royalty rate could be calculated by multiplying brand strength scores with the royalty rate range for a brand.

c. ***Determination of Brand Revenue:*** Brand-specific revenues are a proportion of the parent company's total revenue generated by the brand.

Further, based on historical brand-specific revenue along with forecasts of equity analysts and economic growth rate, the future flow of revenue was forecasted.

Brand Finance applied the royalty rate to the forecast revenues to derive the implied royalty charge for the use of the brand.

Exhibit 5: Brand Valuation Method by Interbrand

From NOPAT, a capital charge is subtracted to account for the capital used to generate the brand's revenues; this provides the economic profit for each analyzed year.

For the purposes of the rankings, the capital charge rate is set by the industry weighted average cost of capital (WACC).

Role of brand determination derived depending on the brand, from one of three methods: primary research, a review of historical roles of the brand for companies in that industry, or expert-panel assessment. The percentage of the role of brand is multiplied by the 'economic profit of the branded products or services to determine the amount of 'branded earnings' that contribute to the valuation total.

Brand strength is reported on a 0 to 100 scale, where a score of 100 is perfect, based on an evaluation across 10 dimensions of brand activation, which include clarity, commitment, governance, responsiveness, authenticity, relevance, differentiation, consistency, presence, and engagement.

Exhibit 6: Financial details for HCL

Particulars (value in millions of USD)	31-Mar-20	31-Mar-19
Total Revenue	9,936	8,632
Revenue	9,936	8,632
Cost of Revenue, Total	6,188	5,478
Gross Profit	3,748	3,154
Total Operating Expenses	7,965	6,834
Selling/General/Admin. Expenses, Total	1,222	1,028
Research & Development	181	132
Depreciation / Amortization	399	307
Interest Expense (Income) - Net Operating	-97	-124
Unusual Expense (Income)	4	0
Other Operating Expenses, Total	68	15
Gain (Loss) on Sale of Assets	30	10
Other, Net	0	-80
Net Income Before Taxes	1,971	1,798
Provision for Income Taxes	413	354
WACC	0.19%	12.43%

Total Equity & Debt	7446	5927

Source: Annual Reports of HCL

[i] Brand Finance. 2020. Global 500: The annual report on the world's most valuable and strongest brands.

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[v] Annual Report. IBM. 2019.

[vi] Annual report, HCL, 2018-19. P.292

[vii] HCL Technologies. 2019. HCL Technologies to acquire strong-bridge envision to enhance digital transformation consulting capabilities in HCL portfolio. Available <https://www.hcltech.com/press-releases/hcl-technologies-acquire-strong-bridge-envision-enhance-digital-transformation> Accessed on 12 April 2020.

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[x]Millward Brown. 2015. Brand Valuation Methodologies. Available at <http://www.millwardbrown.com/brandz/rankings-and-reports/top-global-brands/2015/methodology> accessed on 12 April 2020.

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