

Discover hidden intellectual property to increase revenue and value

Part Two

IP increases the value multiplier

Once you've defined your IP and commercialised it, the IP increases the equity value of your business because IP is a value multiplier. The revenue stream on the IP has a higher multiplier than the product alone. The margins on IP are higher than on your product because the IP production costs are much lower than those for your first product.

It's like selling the second product to the same client. Because you don't need to find this client again, you'll make a higher margin on the second product. Think of it in those terms, but multiply it by a factor of four. The IP MacDonald's uses to build hamburger restaurants is already in the business. The production cost for franchising is zero because they used it to build the hamburgers business anyway. As soon as they commercialise the IP, it's all profit.

When Virgin created their brand strategy, they'd already done it to sell their product. In creating this company IP, they had a brand management strategy template.

In then commercialising the IP, they could sell something that didn't cost them anything to build – because they were doing it anyway. Their cost of IP was zero and their brand strategy profit went straight to their bottom line. The multiplier effect on company IP is huge and therefore changes the multiple for business valuation.

Beyond trading multiples

Say you're currently only operating on trading multiples, which is "revenue in" minus "costs" to provide "profit", times a "multiple". You can increase the margins substantially by now commercialising your IP because in this way you'll have substantially increased the "multiple".

Businesses that have gone the company IP route are valued higher on stock exchanges. They get a premium on their multiples and share prices. Other executives ask, "Why can't I do that?", but don't appreciate the IP multiplier effect.

It doesn't matter whether you're a small business of 15 staff or a big business of 150,000 staff, the same concept applies.

If you want to generate higher profits you must define, build and commercialise your IP.

IP's role in business valuation

IP is a “business asset”. Let’s see how this fits with other aspects of business valuation.

Most management teams are brought up on profit and loss and think in terms of “trading”. They know that to improve the business they can increase their profit (earnings), which will naturally increase valuation because “profit” times the “multiplier” brings a higher valuation.

To further increase the business’s value, you must go beyond the P&L and find value on the balance sheet. On the balance sheet, an accountant records “real assets” but generally not IP, which is a “business asset”. A real asset is property, trade debtors, money loaned and so on. If you sell a licence you can add it to the balance sheet because people have paid money for it. These balance sheet “real assets” are used in valuation because they fit accounting formulae and standards.

Uncovering business assets

Today, several businesses have begun to add the company brand to their balance sheet and a major company might value their brand at \$10bn. But brand is the only extent they’ll go in putting a “business asset” on the balance sheet. Like IP, “brand” isn’t a tangible, real asset like a licence or property.

Business assets rarely make it to the balance sheet. If they’re not on the P&L or Balance Sheet they’re hidden from the management team and the management team isn’t thinking about them on a day-to-day basis.

The team isn’t aware of these assets or how to commercialise them so they lie dormant and don’t generate extra value.

Imagine if Southwest Airlines had “culture” as a line item and valued it at \$Xm. Even McDonald’s might not fully value their franchising IP, but only itemise the value in terms of actual franchise revenue.

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Using IP for value generation

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We regularly work with businesses when they come to sell, our job is to find business assets that don’t show up on those two documents and work out how to make those hidden assets visible to the business and potential buyers. When we trade them we get much higher valuation payouts than if people only use the classic accounting formula.

One example of how this works is the sale of a conference company. Two partners were running the company, but wanted to retire and my accountant friend asked me to help. Jan and Gail said their business was generating \$11m gross revenues with a margin of 3%. “We make about \$330k a year in profit and we’ve had an offer of 750k,” they said.

My accountant friend thought they should get at least \$900k and were being short-changed by \$150k. He asked me to take a look at the business so I went through their books using my business assets checklist. “Do you have any IP?” I asked Jan and Gail. Blank looks. I re-phrased the question. “What are you really good at?”

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It turned out that their company IP was a hidden asset. Because they ran conferences for large corporates, they took away on three- to five-day conferences the top 10 to 600 executives in each company. In selling their conference “product”, they knew each executive’s date of birth, dietary requirements, next of kin all the way through to what pillows they liked to sleep on. They had more information on the top 100 companies’ executive teams than anyone else in that market.

This is IP!

I said, “Ladies, this is called company IP.”

I asked them to let me market their company over the next 12 to 18 months. “I believe I can get you a lot more than \$900k for it.” 15 months later I sold their business for \$11m. The difference between the final \$11m and original \$750k offer is their company IP. The original \$750k offer is simply “Trading Valuation numbers”, whereas our number is an “Asset Based number”.

And it works in the large end of the city as well; a company listing on the FTSE this year is ‘Ocado’ – let’s look at their business numbers:

- An eight (8) year old company
- Has one major client (considered very risky by most people)

Look beyond your real assets to discover your business assets and unlock significant hidden company value.

- Gross revenues £400m
- Has never made a profit in its 8 year history

And what is its listing valuation - £1bn.

How does a business that doesn’t make a profit get valued at two and half times gross revenues – answer: Asset Based Pricing that comes from Company IP.

In summary, your company will already have revenue-generating products, but you need to identify the IP – your company know-how – that they’re based on.

- The cost of your IP is virtually zero.
- Once you can define your company IP, you can begin to commercialise it.
- The multiplier effect on your margins is huge because your company IP already exists.

The revenue streams off the back of your company IP can significantly increase business valuation because this asset isn’t currently showing on your balance sheet. Look beyond your real assets to discover your business assets and unlock significant hidden company value. Do this coming out of the recession and your business will boom across the boom!!