

## VALUATION OF INTANGIBLE ASSETS AND CAPITAL MARKETS: AN INDIAN PERSPECTIVE

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### ABSTRACT

*Intangible assets form a significant part of the assets many enterprises. The valuation of intangible assets acquires importance since it affects the enterprise value. Accounting standards prescribe methods which are conservative. Also, they do not allow capitalization of internally generated intangible assets. In such a scenario, the true value of an enterprise may not be reflected in the financial statements reported. This article explores how capital markets are more indicative of the true value than the financial statements prepared as per accounting standards.*

**KEYWORDS:** *Intangible Assets, Enterprise Value, Accounting Standards, Capitalization, Capital Markets.*

### Introduction

Intangible assets are one of the emerging assets which got lot of significance and attracted attention from research point of view as they have a major role for various segments of industry. Tangible assets are normally valued on cost basis or market value basis. The valuation of tangible assets is fairly easy and straight forward since comparable assets or market value are available. In case of intangible assets, the value of assets changes based on time, origin, usage and on the business transaction. Because of their complex nature, unique and not frequently traded in the market freely. This makes the valuation of intangible assets difficult. Intangible assets such as brands, trademarks and copyrights are unique in their nature and are much more valuable than their cost value. Hence, the valuation method for an intangible asset depends on its origin, its usage and its impact on the market for a product or service. The value of an entity may be differently valued due to the intangible assets owned by it. Even the stock price of an entity has been found to be valued differently based on its intangible assets such as brand value or technical knowhow. This article analyses how the capital markets value an enterprise because of its intangible assets, though its book value does not reflect the fair value of intangible assets.

### Intangible Assets

Indian Accounting Standards AS 26 or the convergence standard Ind AS 38 are applicable for measurement and recognition of intangible assets. Ind AS 38 is applicable for companies which are required to adopt international accounting standards IFRS. Others are governed by AS 26. Intangible assets have been defined in the Indian Accounting Standards Ind AS 38 as an "identifiable monetary asset without any physical substance". It can be better understood by examples of intangible assets. Examples of intangible assets are brands, technical know-how, copyrights, patents, trademarks, computer software, titles, formulae, models, designs and goodwill. According to Indian Accounting Standard AS26 – Intangible asset is initially measured at cost. Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognized as intangible assets. Expenditure during Research phase not recognized as intangible asset. Similarly, start-up costs, expenditure on advertising and promotional activities should not be recognized as intangible assets. If separately acquired, value of

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intangible asset will be purchase consideration or acquisition cost. If part of amalgamation, value of intangible asset will be fair value on date of amalgamation. A definite life of maximum 10 years is prescribed in AS 26. According to IND AS38-Intangible asset is initially measured at cost. Subsequently, intangible assets will be recognized at revalued amount. The appropriate method of disclosure for intangible assets in a company varies based on its corporate actions, based on the industry to which it belongs and external factors. Who do enterprises acquire or generate intangible assets? Business enterprises acquire intangible assets by one or more of these activities (i) by internal generation (ii) through Research & Development (iii) by purchase (iii) through merger with another entity (iv) through licence or franchise (v) by way of goodwill. For example, the following companies spend huge amounts for promoting their brands which are not capitalized but expensed even though the benefits may be derived over many future years.

Name of Company	No. of Brands Owned	Amt Spent on Advertisement Rs. Cr.
Hindustan Unilever	35	4526
ITC	60	894
Dabur	35	712

Name of Company	Intangible Asset	Amount Rs. Cr.
Infosys	Brand Development	629.00
ITC	Design & Product Development	169.28
Dr. Reddy's Laboratories	R&D	6174.1

Source: Annual Reports of the companies www.bseindia.com

### Capital Market

Capital Market is a market for financial securities such as equity shares, debentures, bonds. There are buyers and sellers who trade in financial securities. There is the Primary Market which deals with issue of new securities. The Secondary Market deals with exchange of existing or previously issued securities. In India, the National Stock Exchange of India and Bombay Stock Exchange are the two biggest stock exchanges. Capital markets help channelize surplus funds from savers to institutions which then invest them into productive use. The issue taken up in this article is, do financial statements reflect the true value of intangible assets and hence the true value of an enterprise? It is seen that accounting standards do not allow capitalisation of internally generated brands, goodwill etc., R & D costs cannot be capitalized. Also external factors such as economic factor, market factor, Government policies and decisions and time factor, are not taken into account for valuation purpose. For the above reasons financial statements do not reflect the true value of enterprises. This is one of the reasons for the market value of an enterprise with intangible assets to be higher than its book value. The following analysis further brings out this fact from data of top 50 Indian companies which are listed on the National Stock Exchange (NIFTY 50).

### Analysis of Nifty 50 Companies

In this, secondary data from annual reports of companies listed on the stock exchange were collected and analyzed. NIFTY 50 index is a National Stock Exchange Index of Fifty (NIFTY) companies with large market capitalization and actively traded. The NIFTY 50 index was launched in 1996 by National Stock Exchange of India (NSE). The index is managed by NSE. The index includes 13 sectors of the Indian economy. The index is a free float market capitalization weighted index. The analysis was done for a six year period from financial year 2010-11 to 2015-16. Study was also done on the disclosures of intangible assets made by these companies in their annual reports. The results of the analyses are presented below.

#### • Analysis of Intangible Assets Vs. Market Capitalization

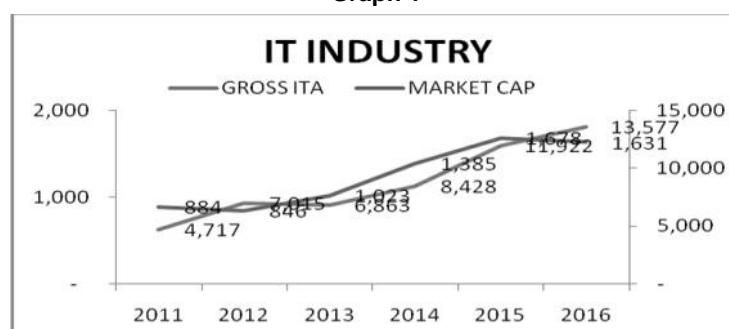
An Analysis was undertaken to study the correlation between value of intangible assets and the market capitalization of listed companies in National Stock Exchange of India under the index NIFTY 50. The NIFTY 50 companies selected for the analysis are as follows:

Name of the Company			
1	HCL Technologies Limited	26.	Indian Oil Corporation Limited
2	Infosys Limited	27.	ACCLimited
3	Tata Consultancy Services Limited	28.	Ambuja Cements Limited
4	Tech Mahindra Limited	29.	Grasim Industries Limited
5	Wipro Limited	30.	Ultra Tech Cement Limited
6	Cipla Limited	31.	Coal India Limited
7	Dr. Reddy Laboratories Limited	32.	Hindalco Industries Limited
8	Lupin Limited	33.	Tata Steel Limited
9	Sun Pharmaceuticals Limited	34.	Bajaj Auto Limited
10	Aurobindo Pharma Limited	35.	Bosch Limited
11	Bharti Airtel Limited	36.	Hero Moto Corporation Limited
12	Idea Cellular Limited	37.	Mahindra & Mahindra Limited

13	Bharti Infratel Limited	38.	Maruti Suzuki Limited
14	Zee Entertainment Limited	39.	Eicher Motors limited
15	Asian Paints Limited	40.	Tata Motors Limited
16	Hindustan Unilever Limited	41.	Bharat Heavy Electricals Limited
17	ITC Limited	42.	Axis Bank Limited
18	Bharat Petroleum Corporation Limited (BPCL)	43.	Bank of Baroda Limited
19	Gail(India)	44.	Housing Development Finance Corporation Limited
20	National Thermal Power Corporation	45.	HDFC Bank Limited
21	Oil Natural Gas Company Limited	46.	ICICI Bank Limited
22	Power Grid Corporation of India Limited	47.	Indusind Bank Limited
23	Reliance Industries Limited	48.	Kotak Mahindra Bank Limited
24	Tata Power Limited	49.	State Bank of India Limited
25	Larsen And Toubro Limited	50.	Yes Bank Limited

- **Industry Wise Analysis:** The companies selected for analysis were initially classified according to the group of Industry they belong. The value of Gross Intangible Assets (ITA) was taken from the Annual Reports of the companies available on the annual filings with National Stock Exchange. Market Capitalization is calculated by multiplying the number of shares outstanding with the market value per share.
- **IT Industry:** There are four (4) IT Companies listed in the NIFTY 50 Index which are Infosys Limited, Tata consultancy services limited, Wipro limited, and Tech Mahindra Limited. The following is the Analysis of Value of Intangible Assets (ITA) and Market Capitalization.

**Graph 1**

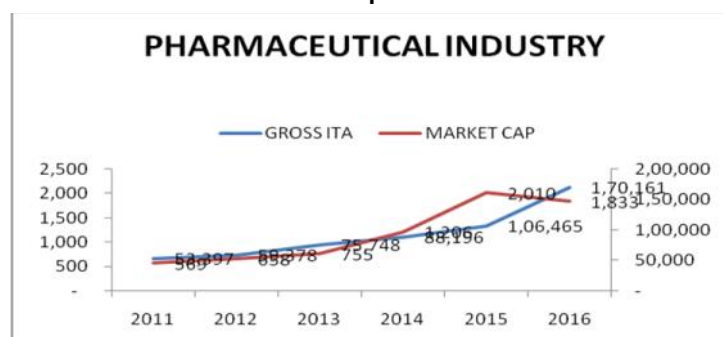


(Source: Compiled from Annual Reports of the companies available on website [www.bseindia.com](http://www.bseindia.com) and company website)

As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **Pharmaceutical Industry:** There are five Pharmaceutical Companies listed in the NIFTY 50 Index which are Lupin Limited, Cipla Limited, Reddy Labs Limited, Aurobindo Pharmacy Limited and Sun Pharmaceuticals Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

**Graph 2**

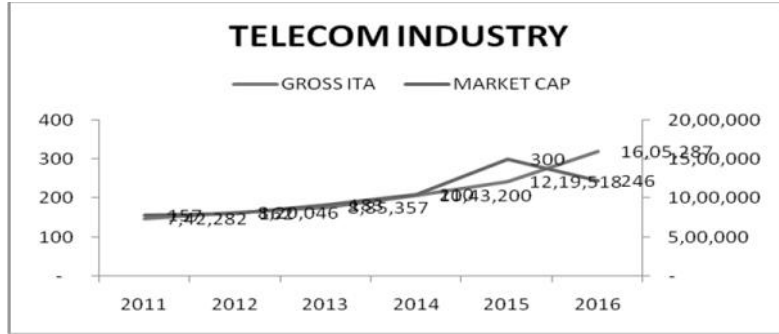


(Source: Compiled from Annual Reports of the companies available on website [www.bseindia.com](http://www.bseindia.com) and company website)

As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **Telecom Industry:** There are three Telecom Companies listed in the NIFTY 50 Index which are Bharti Airtel Limited, Idea Cellular Limited and Bharti Infratel Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

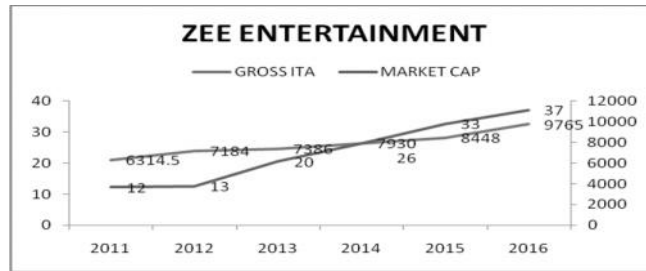
**Graph 3**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **Media and Entertainment Industry:** There is one Media and Entertainment Company listed in the NIFTY 50 Index which is Zee Entertainment Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

**Graph 4**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **FMCG Industry:** There are three FMCG Companies listed in the NIFTY 50 Index which are Asian Paints Limited, Hindustan Unilever Limited, and ITC Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

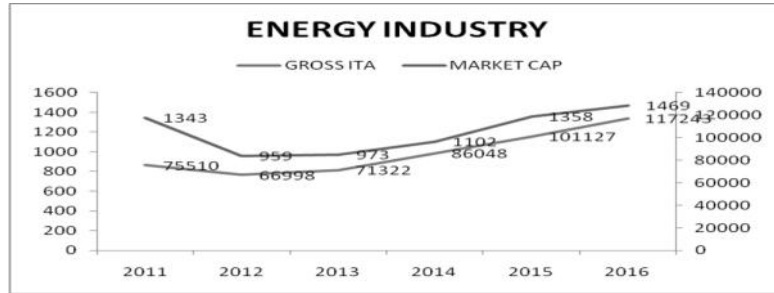
**Graph 5**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- Energy Industry:** There are seven Energy Companies listed in the NIFTY 50 Index which are GAIL (INDIA) Limited, Tata Power Limited, NTPC Limited, Reliance Industries Limited, BPCL Limited, ONGC Limited, and Power Grid Corporation Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

**Graph 6**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- Construction Industry:** There is only one Construction Company which is listed in the NIFTY 50 Index which is Larsen and Turbo Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

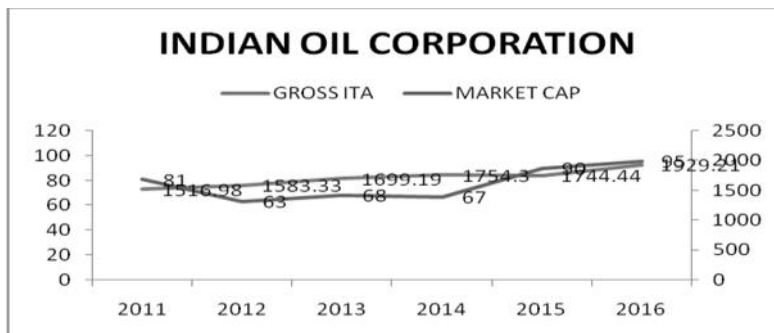
**Graph 7**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- Oil and Natural Gas Industry:** There is only one Oil and Natural Gas Company which is listed in the NIFTY 50 Index. It is Indian Oil Corporation. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

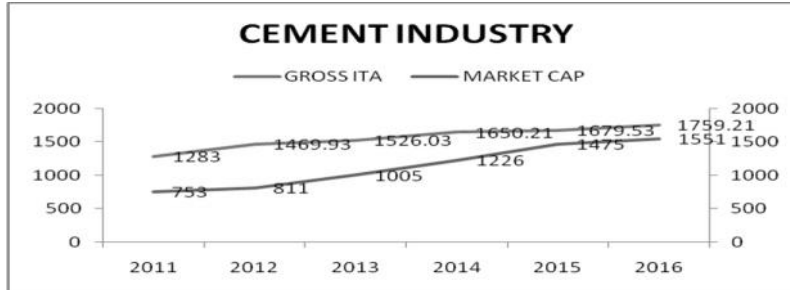
**Graph 8**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- Cement Industry:** There are four Cement Companies listed in the NIFTY 50 Index. They are ACC Cement Limited, Ambuja Cement Limited, Grasim Industries Limited, and Ultratech Cements Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

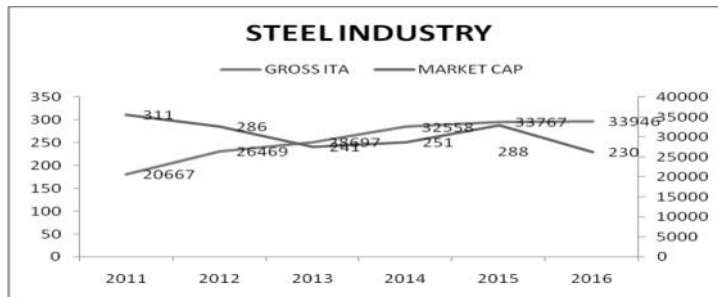
**Graph 9**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- Steel Industry:** There are three Steel Companies which are listed in the NIFTY 50 Index. They are Coal India Limited, Hindalco Industries Limited, and Tata Steel Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

**Graph 10**

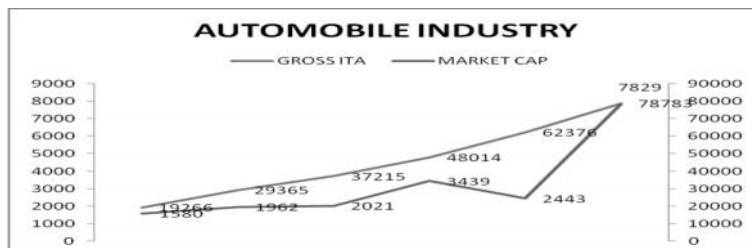


(Source: <https://www.financierworldwide.com/outlook-for-the-global-steel-market/#.Wa0wlvvmGPIU>)

The above analysis does not give a clear picture about the Steel Industry Gross Intangibles and Market Capitalizations. Though the graph does not show positive correlation between the market capitalization and the value of intangible assets, other market factors have affected the market capitalization. Global steel industry has been facing turbulent times. Global excess capacity and historically low prices have adversely affected the profitability of steel industry and hence, the market capitalization has been declining. Finally in the given case there is an impact of intangible assets in proportion with market capitalization. However, the same was dominated by other factors. Consequently, the impact was mitigated to that extent and the results are depicted as above.

- Automobile Industry:** There are six Automobile Companies which are listed in the NIFTY 50 Index which are Mahindra Limited, Hero Moto Corp Limited, Tata Motors Limited, Eicher Motors Limited, Maruthi Suzuki Limited, and Bajaj Auto Limited. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

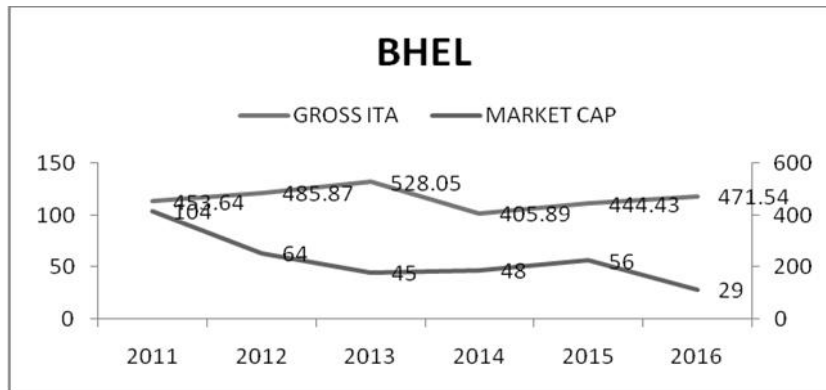
**Graph 11**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **Manufacturing Industry:** There is only one Manufacturing Company which is listed in the NIFTY 50 Index which is Bharat Heavy Electricals Limited (BHEL). The following is the Analysis of Value of Intangible Assets and Market Capitalization.

**Graph 12**

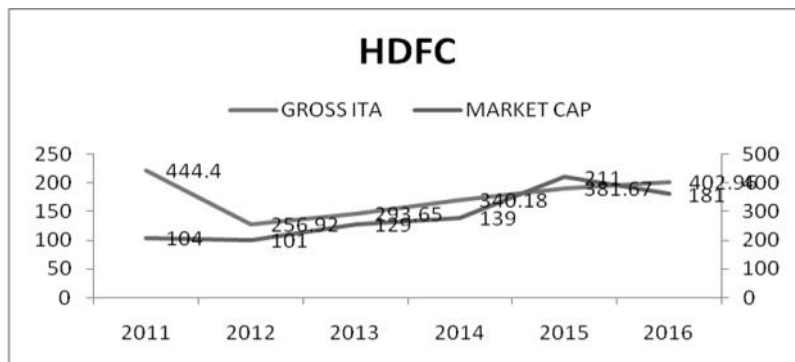


(Source: <http://economictimes.indiatimes.com/bharat-heavy-electricals-ltd/chairmanspeech/companyid-11831.cms>)

In the above case of BHEL, the graph does not show a positive correlation between the market capitalization and the value of intangible assets. However, there is no negative correlation too. Hence, the market capitalization has been affected by other factors. The Chairman of the Company in his speech in the Shareholders' meeting had explained that "the company is in the midst of the toughest times it has faced since its inception. The uncertain global economic order, caused by weak global recovery, slowing global trade and China's growth transition, is the "new normal". The desired pace of growth continues to elude the domestic industrial sector as it faces continued pressure from subdued capital expenditure and capacity underutilization. Power generation equipment industry, in particular, has been facing a tough time for the last few years, accentuated by the ongoing energy transition. In addition to this, geopolitical disturbances in the target export markets and fluctuating energy prices have dampened the international business. The overall subdued business environment due to these factors and the current business mix affected the financial performance of the company".

- **Financial Sector:** There is only one Financial Company which is listed in the NIFTY 50 Index which is HDFC. The following is the Analysis of Value of Intangible Assets and Market Capitalization.

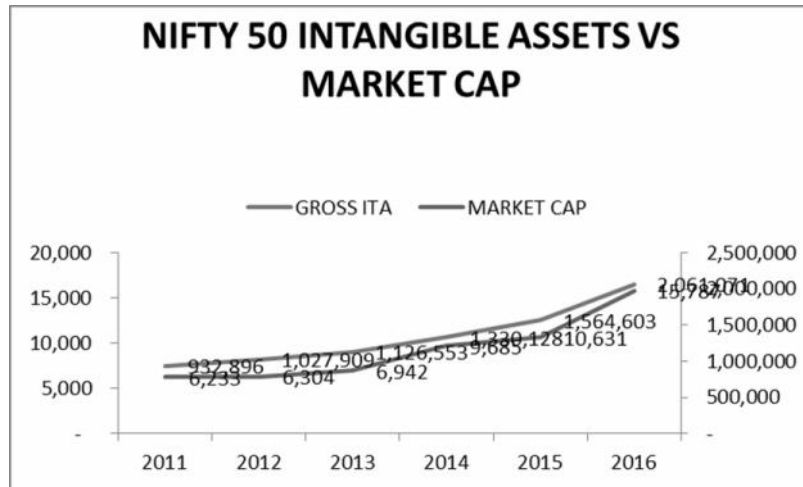
**Graph 13**



As can be seen from the above, a positive correlation exists between the market capitalization and the value of intangible assets.

- **Nifty 50:** There are 50 NIFTY Companies as mentioned above. Out of them 10 Companies do not have any Intangible Assets. The following is the Aggregate picture of trend Analysis of Value of Intangible Assets and Market Capitalization for the 40 Companies for 6 years chosen.

Graph 14



**Findings:** A positive correlation exists between the market capitalization and the value of intangible assets in most of the Companies over the 6-year period chosen. The aggregate picture also coincides with the Industry wise analysis. Even there, almost similar trend was observed except in BHEL case and Steel Industry case.

**Conclusion:** For Listed companies, Intangible Assets play a significant role in Market Capitalization during the period chosen subject the inflationary tendencies. An attempt is further made to check the relationship between these two variables through Coefficient of Correlation

- **NIFTY 50 CORRELATION – Correlation coefficient** - There are 50 NIFTY Companies as mentioned above. Out of them, 10 Companies do not have any Intangible Assets. Hence, the Correlation coefficient is calculated for the remaining 40 companies. The following formula was used to calculate correlation coefficient is:

$$\text{Correl}(X,Y) = \frac{\sum(x-\bar{x})(y-\bar{y})}{\sqrt{\sum(x-\bar{x})^2 \sum(y-\bar{y})^2}}$$

Where  $\bar{x}$  and  $\bar{y}$  are the sample means of variable 1 (Value of intangible assets) and variable 2 (Market capitalization)

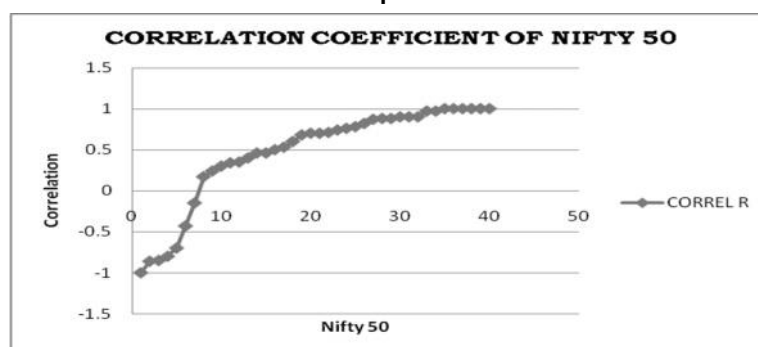
Table 15 Correlation 'R' for the 40 Companies

NIFTY 50	CORRELATION COEFFICIENT- R
GAIL	-1
TATA POWER	-0.86
TATA STEEL	-0.85
NTPC	-0.8
HINDALCO	-0.7
MAHINDRA MAHINDRA	-0.43
BHEL	-0.15
IDEA CELLULAR	0.17
COAL INDIA	0.24
WIPRO	0.3
HDFC	0.34
TECH MAHINDRA	0.35
LUPIN	0.4
BHARTI AIRTEL	0.46
LARSEN AND TUBRO	0.46
RELIANCE INDUSTRIES	0.5



INDIAN OIL	0.53
ACC CEMENT	0.6
HERO MOTO CORP	0.68
BPCL	0.7
ONGC	0.7
CIPLA	0.71
REDDY LABS	0.74
AMBUJA CEMENT	0.76
TATA MOTORS	0.78
AUROBINDO PHARMA	0.82
SUN PHARMA	0.87
GRASIM CEMENT	0.88
EICHER	0.88
INFOSYS	0.9
ZEE ENTERTAINMENT	0.9
MARUTI SUZUKI	0.9
BHARTI INFRATEL	0.97
ULTRA TECH	0.97
TCS	1
ASIAN PAINTS	1
HINDUSTAN UNILEVER	1
ITC	1
POWER GRID	1
BAJAJ AUTO	1

Graph 15



**Findings:** 1. Out of the 40 Companies, 7 Companies have Negative Correlation and 33 Companies have a positive correlation. 2. Within those 33 companies, 6 companies were having a perfect correlation with value of  $r$  as 1.

**Conclusion:** There is a Correlation between the value of Intangible Assets and Market Capitalization for Listed companies. Most of them are having positive correlation.

- **Disclosures Analysis by Indian Companies**

Analysis of disclosures by selected Indian companies in respect of the classes of intangible assets, value of intangible assets, methodology of valuation used and value of intangible assets as percentage of total assets and total revenue is made in the following paragraphs.

- **Analysis of Financial Statements of Companies that adopted IFRS Voluntarily**

In the table, the details of Indian companies and their disclosure about the intangible assets in their annual financial statements are given. The following companies issue financial statements as per IFRS in addition to financial statements as per Indian accounting standards: Infosys Ltd., Dr. Reddy's Laboratories Ltd., Wipro Ltd, TCS Ltd, HDFC Bank Ltd., Tata Motors Ltd., ICICI Bank Ltd, Bharti Airtel Ltd. and Glenmark Pharmaceuticals Ltd.

Table 16 shows method of valuation adopted, amortization method used and details of intangible assets disclosed in their financial statements as per Indian Accounting Standards.

**Table 16: Disclosures by IFRS adopted Indian Companies**

S. No.	Company Name	Disclosures	Amortization Method	Classes of Intangible Assets
1	Infosys Ltd.	Intangible assets are recorded at acquisition cost. Goodwill arising on consolidation or acquisition is not amortized but tested for impairment. Research costs are expensed. Software development costs are expensed unless their future economic benefits are probable, in which case they are capitalized.	Straight line method	Goodwill IPR Land-use rights
2	Dr. Reddy's Laboratories	Valuation at acquisition cost.	Straight line method	Goodwill, Customer Contracts, Technical Know-how, Product related intangibles Copy rights & Patents
3	Wipro	Valuation at acquisition cost.	Straight line method	Goodwill, Technical Know-how, Patents, Trademarks
4	TCS	Valuation at acquisition cost.	Straight line method	Goodwill, Acquired Contract Rights, IPR, Distribution Rights, Rights under licensing agreement and software licenses.
5	HDFC Bank	Valuation at acquisition cost.	Straight line method	Computer Software Licenses, Electronic Trading Platform (Website), Bombay Stock Exchange Card.
6	Tata motors	Valuation at acquisition cost.	Straight line method	Technical knowhow, Computer software, Product Development Cost
7	ICICI	No disclosure	No disclosure	Goodwill
8	Bharti Airtel	Valuation at acquisition cost.	Straight line method, Bandwidth amortized over period of agreement	Software, Bandwidth, Licenses (Including Spectrum)
9	Glenmark Pharma	R & D revenue expenditure is expensed. Development expenditure is capitalized if future economic benefits are probable. Intangible assets are de-recognized on disposal or when no future economic benefits are expected. Goodwill and intangible assets that have indefinite lives or that are not yet available for use are tested for impairment annually; their recoverable amount is estimated annually at the reporting date.	Straight line method, Impairment Testing	Computer Software, Brands, Product Marketing Rights, Product know-how

(Source: Compiled from Annual Reports of the companies available on website [www.bseindia.com](http://www.bseindia.com) and company websites)

**Findings:** 1. By observing Table 4.16, it can be inferred that Indian companies are using only cost method for initial recognition. 2. Subsequently, some companies are testing for impairment. 3. Banking companies make very little disclosure about intangible assets. 4. All the companies follow methods as prescribed by AS26. They also strictly follow the standards for capitalizing the expenditure related to intangible assets.

**Findings:** 1. The valuation methods are different under IFRS and under Indian AS26. Because of this, the value of intangible asset itself can be different for e.g., Infosys. 2. Impairment testing methods are different as per IFRS and Indian accounting standard AS26 for e.g., Dr. Reddy's Laboratories. 3. HDFC Bank has not made any disclosure under AS26 on the valuation method used. 4. Due to different

methods adopted between Indian Accounting Standards and IFRS standards, there is huge difference in the value of intangible assets which is summarised below:

**Table 17: Difference between Indian AS and IFRS Valuation**

S. No.	Company Name	Value as per Indian AS Rs. Cr (A)	Value as per IFRS Rs. Cr (B)	Difference in Rs. Cr. (A)-(B)
1	Infosys Ltd.	4580	1439	3141
2	Dr. Reddy's Lab	6879	5416	1463
3	Wipro	10791.3	11783.2	-991.9
4	TCS	711.01	3951.28	-3240.27
5	HDFC Bank	187.16	7494.2	-7307.04
6	Tata Motors	62456.0	60791.27	1664.73
7	ICICI Bank	125.7	3555.1	-3429.4
8	Airtel	112016.6	129276.9	-17260.3
9	Glenmark Pharma	3485	3485.1	Nil

Source (<http://www.pwc.in/assets/pdfs/publications/2015/pwc-reporting-perspectives-march-2015.pdf>)

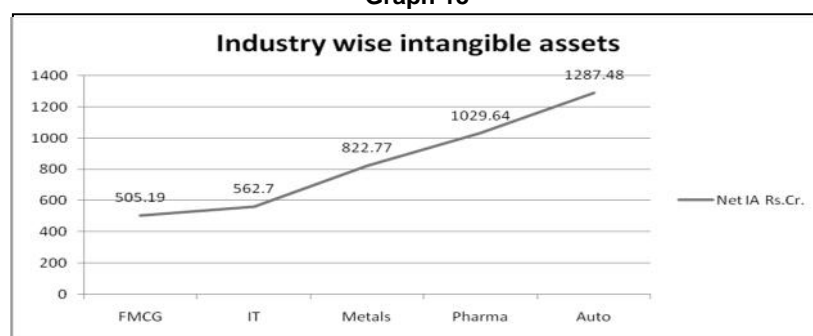
The table shows the summary of industry wise net intangible assets as on 31-3-2016 and the trend graph.

**Table 18: Net Intangible Assets Industry wise**

Industry	Net IA
FMCG	505.19
IT	562.7
Metals	822.77
Pharma	1029.64
Auto	1287.48

(Source: [http://brandirectory.com/league\\_tables/table/india-100-2016](http://brandirectory.com/league_tables/table/india-100-2016)) which is not reflected in the financial statements

**Graph 18**



(Source: [http://brandirectory.com/league\\_tables/table/india-100-2016](http://brandirectory.com/league_tables/table/india-100-2016))

FMCG industry has the lowest value of intangible assets whereas Auto industry has the highest. This is actually contrary to the real fact. FMCG industry holds highest number of brands, but whose value is not at all reflected in the balance sheet of the entities.

**Overview of Observations**

Generally, the disclosures by Indian companies includes the following under IFRS disclosures: Method of valuation, Method of measurement of discount rate in determining present value, Method of amortization, Period of amortization, Method of impairment testing, Types/classes of intangible assets, Measurement of goodwill, Treatment R&D expenditure, Treatment of software costs, Treatment of intangible assets with indefinite life, Segment wise allocation of goodwill, Minimum value above which the intangible assets will be recognized, Foreign exchange differences, How the gain or loss on disposal is treated in the accounts, Fair value adjustments. Under Indian AS26, the disclosures were comparatively less and generally include the following: Method of valuation, amortization period, Treatment of R&D expenditure, How the gain or loss on disposal is treated in the accounts, Intangible assets under development, When an intangible asset is derecognized. It can be observed from the

above that Indian Companies disclosure on intangible assets as per IFRS is much more detailed than Indian Accounting Standards. For example, TCS discloses intangible assets geographical wise too. In cash flow statement, purchase of intangible assets is shown as a separate line item. Infosys allocates goodwill to its segments of operations as already mentioned above. Infosys also gives a detailed table on changes in carrying value of intangible assets. Under IFRS, the bargain purchase gain or negative goodwill arising on business combinations is recognized in profit or loss. Under Ind AS, the bargain purchase gain can be recognized either in other comprehensive income or capital reserve but not in profit or loss. Similar to business combination, bargain purchase gain on the acquisition of an associate is also not recognized in profit or loss. Brand value, which is normally a huge value, is never reflected in the intangible assets. Neither IFRS nor Indian Accounting Standards specify a method for valuation of brands and incorporation of the same financial statements. For example, "Tata" the number one brand in India has a value of USD 13,713 million (INR 91,857 Cr), Similarly Infosys has a brand value of USD 4794 million ( INR32,120 Cr.) which is nowhere reflected in the financial statements. It was observed that the value of intangible assets as per the disclosures is not correlated to the market capitalization of the entity.

Intangible Assets Vs. Market capitalization

Intangible assets VS Market Cap		
	Gross Intangible assets Rs. Cr.	Market Cap as on 11-/6/2016 Rs. Cr
H U L	3 1 3	1 8 3 4 0 0
B a j a j A u t o	8 9 . 2 9	8 1 4 0 9
I d e a	4 8 4 2 0	2 5 9 4 6
B H E L	4 6 9	3 3 0 1 8
A s i a n P a i n t s	2 7 6	1 0 0 0 1 0
B o s c h	6 . 7	6 7 5 3 7
I T C	8 9 8	3 0 1 7 8 6
D r R e d d y ' s	6 8 7 9	5 0 9 7 1
A d a n i p o r t s	2 2 3	5 9 7 5 7
A m b u j a c e m e n t s	1 1 4	4 7 8 2 4
I n f o s y s	4 5 8 0	2 2 2 9 8 7
T a t a M o t o r s	6 2 4 5 6	1 4 7 2 0 5
D a b u r	6 8 2	5 2 3 4 3
S u n P h a r m a	6 0 5 7	1 5 7 0 9 6

(Source: www.bseindia.com)

### Valuation Methodologies

As per Indian Accounting Standards, acquisition cost method or cost method is used for initial recognition and later only fair value method is used. Goodwill is tested for impairment periodically as per IFRS and the loss, if any, is recognized as expenditure. However, as per Indian accounting standards, goodwill is not amortised but to be tested for impairment. But this is rarely done as there is no definite way of testing the impairment of goodwill. For the purpose of impairment testing, goodwill acquired in a business combination is allocated to the cash generated units (CGU) or groups of CGU's, which benefit from the synergies of the acquisition. The chief operating decision maker reviews the goodwill for any impairment at the operating segment level, which is represented through groups of CGU's.

#### BHEL

Bharat Heavy Electricals Ltd. has stated that if the intangible asset value is more than Rs. 10000, then only it will be capitalized. Expenditure on Research is charged to P&L account. Expenditure incurred on Development during development phase of R & D is capitalized if it meets the relevant criteria. (Source: BHEL Ltd. Page 169 of Annual Report 2015-16).

#### Hindustan Unilever Ltd.

In the notes, the company has disclosed the policy on intangible assets as "stated at acquisition cost net of accumulated amortization and impairment losses. Amortization is done on straight line basis. (Source: Hindustan Unilever Ltd. Page 155 of Annual Report 2015-16).

#### Idea Cellular Ltd.

Idea Cellular made following disclosure in its Annual Report for 2015-16. Copy Rights, Spectrum Licenses are amortized on commencement of operations over the validity period. Software, which is not

integral part of hardware is treated as intangible asset and amortized over its useful economic life as estimated by the Management between 3 to 5 years. Bandwidth/Fibre taken on indefeasible Right of Use is amortized over the agreement period. Assets costing up to Rs. 5000 are depreciated fully in the month of purchase. (Source: Idea Cellular Ltd. Page 155 of Annual Report 2015-16).

**Asian Paints**

Asian Paints values separately acquired intangible assets at acquisition cost initially. Intangible assets acquired on business combinations are valued at fair value. Trademarks are amortized over 5 years. Estimated life of each brand is assessed separately. Brand of bath fittings business is amortized over 2years. (Source: Asian Paints Ltd. Page 113 of Annual Report 2015-16).

Bharti Airtel made the following disclosure on valuation and accounting of intangible assets: Separately acquired intangible assets are recognized at cost. Software is valued at acquisition cost and amortized over the life of the license. Spectrum and licenses are initially recognized at cost and amortized on straight line basis over the validity period. Bandwidth is recognized at cost and amortized over a period of agreement which may not exceed 15 years. Intangible assets under development includes the amount of spectrum allotted to the Company and related costs for which services are yet to be rolled out. (Source : Bharti Airtel Ltd. Page 136, 152 of Annual Report 2015-16).

**Fair Value Method and Cost Method**

IFRS based financial statements recognize intangible assets on a fair value based methods in the case of business combinations. The valuation is normally done by independent valuers. Indian Accounting Standards do not specify any method for business combinations. However, if the asset is acquired in an amalgamation, the consideration is allocated on the basis of fair values on the date of amalgamation. If an asset is acquired in exchange of shares or securities, then also it is taken at fair value. Otherwise, cost method is widely used for valuation of intangible assets.

**Conclusions & Suggestions**

The above study reveals many gaps in the valuation of intangible assets in the financial statements as reported by enterprises. However, capital markets go beyond the financial statements and value enterprises. This is evident from the higher than book value valuations for enterprises which have significant intangible assets, particularly popular brands. Accounting Standards give detailed guidance for recognition and measurement of intangible assets. Initial measurement is mostly cost based and subsequent measurement fair value based. They also give reference for valuation in various corporative actions such as acquisitions, business combinations, exchange of assets, by way of Government grant etc., However, the Accounting Standards fail to take into account macro economic conditions ,market conditions, government policies ,and time factor. Further some of the accounting These shortcomings can impact the enterprise value adversely and hence market value of the shares of the enterprisewill also be affected. The balance sheet of the enterprise may not reflect the true value and may not reflect global value of the enterprise.Hence the guidance and methods provided by Accounting Standards are inadequate. There is scope for improvement in the all standards right from national level to global level .

The Global Intangible Finance Tracker (2017), which reviews annually the intangible value of top 100 enterprises, reports that the average enterprise value consists of 60% of intangible assets and only 40% of net tangible assets. Out of the 60% of intangible assets only 10% are disclosed, balance 50% is not reported. The report further states that “there is huge black hole in conventional accounting and financial reporting. Changes in the nature of the world economy over the last 20 years, and the inexorable growth in the number of intangibles based enterprises, means that the need for better reporting is now stronger than ever.” Table below shows how the market capitalization of global enterprises is build upon intangible assets:

Name	Total Intangible Value/Enterprise Value (%)
Apple Inc.	62%
Microsoft Corporation	88%
Amazon.com Inc	95%
AT &T Inc	95%
Facebook Inc.	85%

(Source: Global Intangible Finance Tracker 2017)

Sir David Tweedie, Chairman, Board of Trustees, The International Valuation Standards Council (IVSC), opines that "if purchased intangible assets can be put on the balance sheet of an enterprise, there is no logic in banning internally generated brands being shown as assets". David Herbinet, Global Audit Leader, Mazars, member of the Praxity alliance, opines that "It is hard in the modern age of accounting to ignore the reporting for brands, and other intangibles simply because these issues fell into the 'too difficult' box." (Source:[http://brandfinance.com/images/upload/gift\\_report\\_2017\\_bf\\_version\\_high\\_res\\_version.pdf](http://brandfinance.com/images/upload/gift_report_2017_bf_version_high_res_version.pdf))

### **Suggestions**

Accounting Standards require a re-look in the light of the changing scenario. Financial statements and financial reporting should be tuned in a better way to the market and economic factors. Valuation methods specified by Accounting Standards need a revamp so that they are in tune with the market capitalization. In doing this, professionals Company Secretaries, Cost Accountants and Chartered Accountants should play an important role. From the government, Ministry of Corporate Affairs may invite opinions on the recognition and measurement methods of intangible assets. Entrepreneurs need to be aware of the impact of intangible assets on the enterprise value. Finally, the investors awareness should be more on the impact of intangible assets and their value to enable them make better investment decisions.

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