CORPORATE AND BRAND LICENSING

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Introduction

Products using licensed brands registered global sales of $149.77 billion last year. The top 100 companies generated more than $125 billion in sales of licensed products. More and more executive committees and boards of directors discuss licensing in their strategic planning meetings and more and more private investment firms consider licensing their portfolio companies' trademarks. Licensing is continuing to be elevated. From its humble beginnings, brand licensing is evolving into a big and a serious business.

Not long ago brand licensing was largely a sidekick function of promotional activity, hidden in the back rooms of marketing departments. Many licensed products were give-away freebies. How things have changed!

Today you can don licensed Caterpillar® work boots and cut your lawn with a licensed Scotts® lawn tractor. Reward yourself with a fresh cup of coffee from a Melitta® licensed coffeemaker, take your Jeep® branded bike to the store to pick up your new Kodak® eyeglasses. Survey your property anew and call over the licensed Sears® contractor to fix your roof. Negotiate with your son to clean-out your sink and toilet drains with licensed Roto-Rooter® drain cleaning chemicals and then take your Eddie Bauer® SUV over to Sotheby's Real Estate® and have them sell your house. Catch up on the news on your new Westinghouse® HDTV, fly licensed United Express Airlines® into the big city, have your hair cut at the Armani® hair stylist, and spend the night at Armani's licensed nightclub!

The truth is, consumers are increasingly surrounded by licensed brands without even knowing about it. The deals are better engineered, the licensed products and services have higher quality and function, and products have better affinity with the brands.

With the "flattening" of the world, more and more brand owners no longer own the factories which produce their products. Such out-sourcing is a big step As a result, to most consumers, license transactions remain nearly invisible.

We have witnessed licensing grow up and become a serious business. And, as with any serious business, the discussions about licensing have moved from being about trinkets to now involving strategic issues, keeping executive committees and boards of directors alert to new opportunities.

License! magazine's annual list of the top 100 licensors, continues to include more corporate trademark owners every year, with the trademark/brand licensing segment of the overall licensing industry representing almost $32 billion annually.

Why Licensing Became a Real Business

There are many reasons why licensing has grown so impressively and quickly. The traditional reasons have not changed very much:

(1) New competitors, high advertising costs and new media vehicles required companies to look for innovative ways to reach consumers;

(2) Mature markets and increasing competition forced companies to explore new growth avenues;

(3) Financial exposure in licensing is very limited and the upside can be quite substantial;

(4) Minimal risk makes licensing very appealing; and

(5) Better and better companies are becoming licensees…further reducing the risk and boosting the attractiveness.

But there are also some new reasons which are adding to licensing's growth in business.

***More and Better Licensees*.** Manufacturers are increasingly faced with just how fleeting their current technological advantage can be and are tiring of competing on price for the opportunity to be a source to branded companies. Product life cycles are being squeezed into shorter and shorter periods. A new technology introduced today can become obsolete in less than a year. Forward looking manufacturers realize that brands are one of the few sustainable advantages available and an increasing number of good companies want to use established third-party brands. Some licensees. like Akeena Solar, which licensed the Westinghouse® brand and now trades as Westinghouse Solar (NASDAQ: WEST), bring proprietary technology to the licensed brand and the classification of goods.

***Retail Consolidation*.** Retailers are becoming fewer and fewer, by virtue of mergers, acquisitions, or bankruptcies. Those that expect to succeed understand the need to differentiate themselves from the competition, and brands play a key role in the formula. Having a good brand is becoming a prerequisite to even talking about doing business with big retailers.

***Playing Catch Up*.** More top managements are seeing successful licensing programs conducted by their key competitors and they are demanding efforts to catch up. It is tough to argue with brand licensing if your arch competitor in your own industry is clearly benefiting from it. This “don't miss the boat” motivation is becoming increasingly pronounced.

***Event-Driven Industries*.** With the heightened awareness of terrorism, we have seen an emergence of new industries. Government grants and private sector financing has been pouring into the development of all sorts of security and surveillance-related devices that could protect us. On a similar front, in response to the West Nile Virus, there has been a surge in development of new insect repellants, devices, etc., and because so many are being introduced by relatively unknown players, there is strong interest in established brands available for licensing.

Tough Times. Faced with a shrinking marketing budget and lower headcount, how do you intensify your marketing efforts and get more great product into the market? A licensing agency adds a team of licensing professionals to your company without adding to headcount, typically on a largely contingent compensation basis. The licensees add to your brand’s marketing and broaden your range of products and services in the market.

To License or Not to License? — That Is the Question

While some companies still struggle to answer this question, most have answered with a resounding, “Yes”. In 1987, one out of every ten Fortune 500 brands was involved in licensing. By 2009, that number had risen to eight out of ten.

Let's review some of the primary motivations to license.

Marketing Motivations

Raising a brand's top-of-mind awareness continues as one of the top motivations among licensors. In these times of shrinking marketing budgets, this becomes even more of a challenge than it was in the past. In addition to boosting awareness, they want to expand presence at retail, increase advertising levels (licensees spend their own money advertising and promoting the brand), establish their brand with future consumers (or other non-core target groups), as well as to contemporize and help differentiate the brand from its competition.

Here is a very compelling example from a well-known brand: Roto-Rooter Corporation, this service franchise which markets drain cleaning and plumbing services nationwide, is licensing its name into a line of drain-cleaning chemicals. Do they do this to put their franchisees out of business? No, they do it to stay “top-of-mind” with consumers who first dive under their kitchen sink when searching for a drain cleaning solution. Once there, they find the Roto-Rooter chemical and, if it doesn't solve their problem (chemicals don't help with root problems, for example), they reach for the phone and call the toll-free 800 number listed on the package (along with a discount coupon) for a Roto-Rooter technician. This helps to keep them from searching elsewhere for a plumber. So, in this case Roto-Rooter is offering a comprehensive product-and-service solution to consumers. By virtue of leveraging their great brand, they've worked to get ahead of any large local plumber/competitor who buys a bigger Yellow Pages ad than Roto-Rooter.

Financial Motivations

***Make Money*.** There is little doubt that companies decide to license their brands, in part, for monetary reasons. Profit growth is key to corporate life and brands are often among the least explored assets on the balance sheet. And licensing has a direct impact to the bottom line. One major company (who is a client) has been able to double their net profit by adding new revenue from licensing. They did this without making an investment, adding staff, or even attending a seminar on licensing.

***Grow the Business*.** Licensors look to licensing to help them expand into new business sectors. Often these new areas have stronger margins than their core business, but investing in them, or growing them organically, represents risky, costly, and time consuming affairs. Licensing represents a very attractive business model, one that generally meets even the most stringent internal return hurdles. In the enormous economic downturn of 2008-2010, licensing became even more important for corporations, as licensing provided the opportunity to significantly bolster bottom line profitability without increasing already stressed working capital needs and, if done with an agency, without adding to headcount.

***Help Financial Flexibility*.** Recently, some financial institutions have started to secure the cash flows generated from licensing programs. This newly structured intangible asset-backed vehicle, which works very much like a mortgage-backed security, offers the brand owner an immediate pay-out on the future of the licensing program, even if the program is still early in its maturity. This strategy is receiving good reviews from CFOs looking for alternative sources of capital.

***Boost Stock Price*.** Another unexpected financial benefit of licensing is that while it expands the brand's presence, it makes more connections with consumers, businesses, retailers, but also with…shareholders, newspapers, and Wall Street analysts. This increased exposure in these sensitive areas often translates to enhancing market valuation. When Salton, for example, announced launching of the White-Westinghouse license for its small kitchen appliances, the stock experienced a 17% increase on the day of the announcement.

Strategic Motivations

***Reduce Barriers to Entry*.** When moving into a new business, barriers to entry can be very substantial and companies always evaluate their financial commitments, degree of risk, and potential return before they undertake any new project. Because new areas can be difficult and costly to get into, companies welcome strategic alliances that can help them reduce both cost and risk. Licensing is a perfect form of a strategic alliance: a group of licensees with significant resources work under the umbrella of a single brand. The licensor sets the brand's direction and enforces the controls, including accepting appropriate categories, restricting territories, monitoring quality and timing.

***Increase Barriers to Entry**.* Successful brand extension licensing increases the barriers to entry for one's competitors.

***Test Relationships*.** Licensing is an easy way to test the affinity between partners before getting involved in a deeper relationship that could be difficult to terminate. Licensing relationships are relatively hands-off and unburdened by the issues of funding and management. Neither party tells the other how to run their business. Well-matched licensing partnerships tend to evolve into more comprehensive relationships. For some, licensing provides an "analytical window" to take a look at other businesses, with licensee and licensor sharing important information about each other's business. For others, licensing paves the way for future alliances, opening up better sources of raw materials, sharing technologies, and other resources.

LG Fashion, one of the largest fashion companies in South Korea, has successfully built an outdoor apparel and footwear business through brand licensing with Lafuma, a French company that specializes in outdoor apparel, equipment, and footwear. The licensing program worked well for both parties and Lafuma assigned its trademark rights in South Korea to its licensee, LG Fashion in July 2009. Such License-to-Own (LTO) licensing deals are not common in the U.S. or in Europe, but the LTO strategy provides strong incentives to Asian licensees to invest heavily upfront in the brand, and to treat the brand with the level of dedication and care as if it were their own.

***Manage Resources and Stay Focused*.** Many top managers develop licensing relationships as a means to expand their overall resource base. Others are motivated to license because it allows them to "stick to their knitting," to keep their attention focused on the core businesses that are in line with their corporate strategic directions and more profitable, particularly in tough economic and competitive times. For example, as the worldwide PC market shrank and profit margins plummeted in 2008, Philips took a decisive step to improve their profitability levels by selling its IT Displays business to Hong Kong-based TPV Technology Ltd, the largest manufacturer of PC monitors in the world. As part of the 5-year brand licensing agreement, TPV Technology will assume responsibility for manufacturing, distribution, marketing and sales of Philips branded PC monitors worldwide. TPV has the exclusive right to use the Philips brand for PC monitors worldwide, in exchange for Philips' receipt of revenue-based royalty payments. This created a win-win deal for both parties as each of them can allocate their resources in a more effective way. In Aug 2010, Philips granted an exclusive trademark license to AOC Holdings Limited, a subsidiary of TPV Technology Ltd, for a period of 5 years under which AOC may design, manufacture, source, sell, distribute and market Philips-branded televisions in Mainland China from Q4 2010. This is another major step that Philips has taken to reduce its reliance on the consumer electronics business, which is filled with fierce competition and turn to the other core businesses.

Licensing helps trademark owners develop manufacturing, marketing, and financial knowledge in areas totally outside their own. Winchester wants to diversify into new industries that extend beyond firearms and ammunition and provide strong opportunities for long-term growth. Licensing helps them avoid the mistakes associated with starting such new businesses. Their entry is more expedient, their risk is reduced, and their chances of success are improved.

***Expand into New Territories*.** Licensing can also be a means to expand the brand quickly into new markets and into markets in which there are legal barriers to foreign ownership Licensing has long been used by pharmaceutical and semiconductor companies who have products with worldwide appeal, but sales and distribution reach limited to particular geographic areas. Many companies use licensing agreements to expand their worldwide sales rapidly without the need to commit to growing internal organizations. The Frigidaire brand, for example, is licensed for appliances throughout Europe, the Middle East, and other regions of the world. Zenith televisions are manufactured and marketed via license in Southern Europe, and United Airlines licenses its name to six regional U.S. airlines to make up the United Express feeder line.

***Technological leadership*.** Identifying and engaging licensees with leading technologies can perpetuate a brand's reputation for leadership, further strengthening the brand, yet without increasing R & D spending.

***Legal**.* Extending a brand into new classifications of goods through licensing allows broader trademark registration of the brand and, therefore, stronger ownership of the brand. In situations where a brand is in danger of being declared generic, registration for other classifications of goods may help win that battle.

Several Important Trends Are Taking Place in Brand Licensing

Trend #1: Licensing Programs Are Becoming More Deliberate, More Strategic, and More Tailored

Licensing is becoming a more pro-active, strategy-driven business. While this seems like a logical approach, it has not always been so.

Previously, prospective licensees would knock on a brand owner's door, requesting permission to license the brand and it would be considered or not. This was primarily opportunistic licensing and categories like apparel and toys were particularly evident.

For a program to be successful in the long-term, however, targeted categories must make unique sense for the brand. This is why we see successful licenses such as Kodak® eyeglass lenses, Arm & Hammer® air filters, Melitta® coffee makers, Winchester® home safes, Roto-Rooter® drain openers, Mensa® learning products, Weight Watchers® frozen dinners, Frigidaire® central air conditioning equipment, Mott's® apple muffin mix, Gatorade® chewing gum, Mack Truck® lawn tractors, Armani ®nightclubs, and *Brandweek*® executive education. These licenses provide a long-term income stream to licensors and virtually create new businesses for licensees.

Trend #2: Royalty Spreads Grow, Driven by Conflicting Forces

Royalties used to be easy to determine. Interested parties looked at some established category-oriented rate guidelines; they selected one that was applicable to them; and they filled the blank in the contract. But, as the concept of leasing a brand is becoming increasingly accepted and more companies are adopting it, the increased demand for brands drives up the royalty rates. Although the current economic situation has moderated rates, the better brands and properties still command the highest rates and guarantees. But other forces are at play, too. Licensees are working harder than ever to deliver brand-appropriate, superior products that provide unique performances and they use brands as catalysts. The current economic situation has fostered a bit more flexibility in rates guarantees and terms to insure that both Licensor and Licensee have made deals which make good business sense in today's times. Consider the opposite examples of the Spider-Man® wristwatch and the Arm & Hammer® air filter.

The special thing about this watch is that it has Spider-Man on it. The watch itself is a commodity. In this case the image of the superhero, and probably the fact that it was a hit motion picture, determines the unique "value" proposition to this license. And so, if the point of difference in a licensed product is the brand itself, then rate will reflect it. The money in this example goes to Spider-Man.

On the flip side, the Arm & Hammer filters are loaded with superior technology. The same is true of the award-winning Westinghouse cordless vacuums and smart appliances. These licenses combine famous brands with special product performance and technologies developed by the licensees.

Second tier brands and ordinary products have plumbed considerably lower rates, guarantees and appealing terms.

In summary, the royalty rate, minimum guarantees and other terms need to express the contribution of “value”; it's a determination of who brings what to the deal. And we are observing a greater discrepancy between the lowest and the highest rates, depending on relative contributions delivered by the respective parties.

Trend #3: Professional Development

In the past, licensing has had more than its share of fast talkers. As the business moves into the mainstream of corporate life and receives attention from higher levels of management, true professionals are starting to take charge and they are being positioned in top management ranks. In fact, we are seeing the emergence of a new chief licensing officer position in major corporations, which often directs licensing activities in all areas of intellectual property.

The chief licensing officer brings together a spectrum of different capabilities: new products, sales, legal, financial planning, marketing, strategy and deal making. This is a cross-functional type of a professional.

In a parallel vein, more educational programs are being made available in the field. LIMA, the industry association, for example, has created a broad training program geared to working practitioners, and a certification program assuring certain levels of education. On other fronts, college courses are being developed for business students and executive search firms are beginning to develop licensing practices.

Trend #4: Retail Partnerships

In face of retail consolidation, where there are fewer buyers, engineering a real constructive partnership between licensor, licensee, and retailer/distributor will become increasingly essential as competition among licensed brands intensifies. A real opportunity exists for smart manufacturers who present their distribution partners dedicated programs that uniquely address the needs of their customers. Often this will even take the form of unique product designed to especially and exclusively for a specific retailer.

Trend #5: Ingredient Co-Branding

Brands are starting to realize they have things they can offer in addition to their brand. In fact, unless they pair-up the name with its necessary ingredient or brand attribute that makes the brand unique, a pure brand license deal will be less powerful. So, where possible, brand owners try to do that. And you see this in the automotive industry, where Ford Explorer led the way with its Eddie Bauer limited version (the deal included specially designed rugged luggage from Eddie Bauer). Others have attempted to replicate this model, with LL Bean hooking up with Subaru and Coach appearing with Lexus.

Trend #6: Precursor to Mergers and Acquisitions

Historically, many acquisitions have not been successful long-term because the deals have not taken into the account the human factors, personalities, cultural, and other non-accounting/non-financial issues.

Although this is still a relatively new concept, a growing number of merger and acquisition executives view licensing as a means of testing the chemistry between two companies to avoid some of the more common dangers. Further, this allows the parties to fully realize the true attributes and commercial value of related trademarks and competitive forces.

Trend #7: Licensing as a Competitive Weapon

Brand licensing is a great business tool and as higher levels of senior management embrace it, new applications will continue to appear. As we look to the future, one application will be especially pervasive. Licensing will be used as a competitive weapon…in a range of different forms. One is oriented to preempting competition by getting into attractive new businesses before others can. The Roto-Rooter case discussed earlier is a good example. Another is to battle competition for retail space. One example is GE. They grant retailer exclusive licenses for limited product lines in return for guaranteed shelf space in their core product lines. Still other applications focus on product differentiation/superiority and on building ad spending budgets and consumer impressions

Trend #8: Licensing in Emerging Markets

Traditionally, the top global licensing markets are the U.S., Europe and Japan. However, in recent years, brand licensing has already taken off in many emerging markets, with a number of Western brands realizing remarkable success. Among the emerging markets,, two particular countries have gained prominence, namely, India and China. For example, China is the world's fastest-growing market for licensed goods, having expanded from $600 million in 2001 to more than $1.3 billion in 2008. Even at this level, the retail spending on licensed products per capita in China is merely $0.98 vs. $360 in the U.S. To many brand owners, China is the key market for brand licensing, not only because China enjoys a steadily growing economy, but also brand-conscious middle class Chinese consumers usually have a preference for Western brands; they are more willing to pay large brand premiums compared to consumers in the West. Some American iconic brands, such as Westinghouse, have already moved ahead in these emerging markets by licensing its brand to a number of Asia-based manufacturers. Currently, Westinghouse licensed small kitchen appliances, air purifiers and many other household products are being marketed in China, Russia, Middle East and South America. Furthermore, brand owners are encouraged by the emergence of some high caliber manufacturer licensees from emerging markets who have the capability of manufacturing licensed products in-house and marketing these products successfully in the U.S. too. For example, Hong Kong-based Techtronic Industries Ltd has licensed the Ryobi and RIDGID brand for power tools, and they've successfully brought the licensed products directly into large US retailers, thus eliminating the role of the traditional U.S. licensee, leaving better margins for retailers, the licensees and the brand owners. With low-cost manufacturing capabilities, well established retailer relationships, and highly respected consumer brands, powerful licensing relationships can be created for brand owners and licensees alike in emerging markets.

Some companies have looked at attractive foreign markets and seen issues with distance, language, culture, tariffs and other legal matters; hence, they have delayed investment in these markets. Many of these companies have great brands, product lines, sourcing infrastructures and full complements of sales and marketing know how, which are quite valuable in developing markets. Some of those well equipped companies --- even those without brand awareness in the foreign market --- have used licensing to leverage their trademark rights to derive significant royalty revenue on foreign sales, while allowing their foreign licensees to finance and run the businesses and manage their domestic legal issues.

Trend #9: More Emphasis on Product Quality

Recent cases of Mattel recalling 9.5 million toys in the U.S. in 2007 serve as fresh reminders of the importance of quality control on licensed products. More brand owners and their licensing agents are now conducting factory audits on licensees' manufacturing facilities with specific actions required prior to granting the license and periodic audits conducted randomly throughout the licensing term. New clauses have been included in licensing agreements, such as adding licensees' obligations to inform brand owners of changes in major subcontractors as well as the inclusion of local applicable quality and safety standards.

Summary

By virtue of its size and its presence in today's consumer marketplace, licensing is now considered a real industry. It is a business that combines the areas of marketing, new products, and corporate development. As a business tool, licensing is used in a wide range of different ways to accomplish a host of important goals. Licensing evolved from being a fringe supporting activity to a mainstream business. With proper expertise and intelligent strategy it has worked for more and larger serious companies. It can work for you.