# Cost-to-Duplicate Approach

As the name implies, this approach involves calculating how much it would cost to build another company just like it from scratch. The idea is that a smart investor wouldn't pay more than it would cost to duplicate. This approach will often look at the physical assets to determine their fair market value.

The cost to duplicate a software business, for instance, might be figured as the total cost of programming time that has gone into designing its software. For a high-technology startup, it could be the costs to date of research and development, patent protection, and prototype development. The cost-to-duplicate approach is often seen as a starting point for valuing startups since it is fairly objective. After all, it is based on verifiable, historic expense records.

The big problem with this approach—and company founders will certainly agree here—is that it doesn't reflect the company's future *potential* for generating sales, profits, and return on investment. What's more, the cost-to-duplicate approach doesn't capture intangible assets, like brand value, that the venture might possess even at an early stage of development. Because it generally underestimates the venture's worth, it's often used as a "lowball" estimate of company value. The company's physical infrastructure and equipment may only be a small component of the actual net worth when relationships and intellectual capital form the basis of the firm.