



A New Wave of Intellectual Assets based Management from Japan

Presentation in IC for Communities

Takayuki Sumita

METI, Japan

June, 2006

Recent Activities related to IAs (2005–2006)

2005

Aug. Interim Report about “Disclosure of Intellectual Assets Management” (Industrial Structure Council)

Oct. Guideline for Intellectual Assets based Management Disclosure (METI)

http://www.meti.go.jp/policy/intellectual_assets/index.htm

Oct. OECD Conference in Ferrara (more than 20 Japanese attended)

Nov. 1st IA Week in Japan (seminars and symposiums)

Establishment of IA based management consortium (IAMaC) with more than 100 members

2006

Mar. Interim Report on IA based management report in SMEs

(SMRJ: Organization for Small and Medium Enterprises and Regional Innovation Japan)

<http://www.meti.go.jp/press/20060324002/20060324002.html>

Apr. 5 Comments to IASB Discussion Paper on Management Commentary from Japan

May Japan proposed a new project on IA in OECD ministerial meeting

Jun. New Economic Growth Strategy including the element of IA based management (METI)

<http://www.meti.go.jp/press/20060329003/20060329003.html>

New system to put much on the element of IA based management in R&D subsidies

5 companies have already published the IA based management reports as of May 31st.

History of Study on IA based management

20th Century

- Itami, H., & Roehl, T. W., *Mobilizing invisible assets*, Harvard University Press(1987).
 - Describing intangible assets as source of competitive advantage.
- Nonaka, I., & Takeuchi, H., *The knowledge-creating company*. Oxford University Press(1995).
 - A SECI Spiral, interactive transformation between subconscious knowledge and recognized knowledge, as a model of the organizational process of knowledge creation.
- Japan Quality Award (1995) --- Modified version of Malcom Baldrige Award
- Committee on Corporate Management Capabilities (1974-2000, METI)

21st Century

- 2002 Final Report on Intellectual Capital Study Group
- 2003 Study Report on *NEW MANAGEMENT INDICATOR 'Intellectual Capital'*
- 2004 Reference Guideline for Intellectual Property Information Disclosure
 - About 30 corporations disclosed the information of Intellectual PropertyWhite Paper on International Trade (METI) –focusing the importance of IAs
- 2005 Sub Committee on Management and IA established under Industrial Structure Council
Intellectual Property Strategic Program 2005 (Intellectual Property Policy Headquarters)
 - emphasizing the importance of IA based managementBasic Policies for Economic and Fiscal Management and Structural Reform 2005 (Council on Economic and Fiscal Policy) --requiring to compile guideline for IA based management report

Why is IA based management the matter now?

Aging economy
with less population
→ Smaller domestic
market

Global competition
→ Emerging economies
are more cost-
competitive

Knowledge
Economy
→ Intangible
assets became
more valuable

**Creating values/profits by making products or services
different from others is essential for business.**

IA based management which realizes the differentiation
through utilizing company's unique IAs for sustainable profits
has become more critical.

note: IAs include human resources, organizational capabilities, technology, and relational capital.

IA based management as a solution for global challenge

Common Concern on Global competition

'Winner takes all' situation in the global market

- have nots issue=social unrest
- majority(=losers) claims for protectionist measures

Concentration of production of goods in cheap labor countries

- regional employment lost
- destruction of local economy while raising the protectionism

IA based management in companies

Value Creation based on each company's unique characteristics

- each characteristic may create a winner
- winner abundant society
- smaller risk on economic/social unrest

IA based management in Communities

Diversified regional management utilizing the characteristics of the region

- PR globally its own characteristics to attract more people and capital
- Creation of vitalized regional economy
- Compatibility of globalization with regional employment achieved

IA based management as a solution

Outline of METI Guideline on IA based management

Main Characteristics

- Encourages companies to Indicate corporate story of management in a narrative way, by showing the outline of the story
- Proposes the way of incorporating supporting KPIs for enhancing the credibility of the story
- Exemplifies 35 KPIs related to IAs
- Presents a guideline for analysts/stakeholders to evaluate the report

Basic Principles for Disclosing the IA based Management

- Showing the overall picture of corporate management from top manager's eye in a story
- Focusing on the future value creation that affects corporate value
- As a prerequisite for the future value creation, evaluating future uncertainty (risks/chances) fairly and explaining how to deal with them
- Making a report easy to understand for important stakeholders (stockholders, employees, clients, creditors, communities, etc.)
- Supplementing and being compatible with financial information
- Adding supporting key performance indicators (KPI) to the points of the story to enhance credibility. (Explanation on status of internal control is also desirable)
- Providing historical comparability (e.g. KPI for the past two years)
- Giving explanations reflecting the current business activities on a consolidated basis

Outline of IA based Management Report

(General) Basic management philosophy
Outline of business characteristics

(From Past to Present)

- A: Management policy in the past
- B: Investment (based on A) (performance figures included)
- C: Unique intellectual assets accumulated in the company, strengths based on them, and value creation method (based on A and B) (supporting intellectual assets indicators included)
- D: Actual performance in the past, such as profits (as a result of value creation C) (figures included)

(From Present to Future)

- E: (Based on C and the assessment of the past to the present) Intellectual assets that rooted in the company and will be effective in the future, and future value creation method based on them (supporting intellectual assets indicators included)
- F: Identification of future uncertainty/risks, how to deal with them, and the future management policy including those elements
- G: New/Additional investment for maintenance and development of intellectual assets needed (in line with the management policy F) (figures included)
- H: Expected future profits, etc. (based on E to G) (numerical targets included)

Elements and Indicators of IA based management

Key Elements of Corporate Value

(1) Management stance/
Leadership

(2) Selection and Concentration

(3) External negotiation power/
relationships

(4) Knowledge Creation/
Innovation/ Speed

(5) Teamwork/ Organizational
knowledge

(6) Risk Management/
Governance

(7) Coexistence in society

Examples of Indicators

- Degree of internal penetration of management principles
- External transmission of information by top manager
- Development of future leaders (average age of subsidiary presidents)

- Competitiveness of major business
- Weighted average of the numbers of companies providing the same products/services
- Employee assessment
- Review performance of unprofitable department
- Degree of R&D concentration
- Differentiation of market

- Weighted average of market share of main products/ services of the main business
- Degree of customer satisfaction
- New customer sales ratio or growth rate of new customers or members compared to those in the previous year
- Price pass-through capability
- Negotiation power
- Financing capacity

- R&D costs vs. sales
- Outsourced R&D cost ratio
- Number of IP owned, economically meaningful term
- Employees' average age and increase/decrease from the previous year
- New products rate

- In-house improvement proposal for quality control system
- Number of lateral projects
- Job leaving ratio
- Degree of employees' satisfaction
- Incentive system

- Compliance system
- Diversification of risks
- Number of public announcements regarding risk information and speed of public announcement of problems
- Risk of being an acquisition target
- Compensation claims in pending lawsuits
- Risk of information leakage

- Amount of environment-related investment
- Number of SRI funds which adopted the corporation
- Corporate image survey and ranking results

Disclosed Information (Examples)

- **Nissan Motor Company** clearly mentioned goals as CEO's message in its Annual Report with more detailed information on R&D, including past achievement and future targets.
- **Hitachi Chemical Corp.** described the core competence since establishment, the current business developed from it and the direction of future potential in its IPR report 2004.
- **Allabout, Inc.** published, just after listed on JASDAQ securities market, the IA based management report in Oct. 2005 which explains the strength and business focus while advertising the company.
- **Mnemonic Security, Inc.** explained the substance of its IT security-related business in IA based management report (Mar.06), which was highly evaluated by a regional bank in loan building.
- **Neochemir, Inc.** summarized the bio-tech related business with the direction from now on in its IA based management report (Jan.06), which raised substantially the reputation of the company.
- **Development Bank of Japan** wrote down its own IAs, synergy between them and reflection to financial services in the society, environment and IA report (Oct.05).
- **Dataplace, Inc.** presented the business report subject to the commercial law under a sub-title of 'IA based management report'. (Mar. 06)

List of companies making reports

Intellectual Assets based Management Report

Allabout Corp.	http://corp.allabout.co.jp/ir/ir_release/2005_03/051011_1.pdf (listed on JASDAQ)
Development Bank of Japan	http://www.dbj.go.jp/japanese/environment/pdf/2005_all.pdf
Neochemir Corp.	http://www.neochemir.co.jp/chizai/chizaihoukokusyoH17.pdf
Neemonick Securities Corp.	http://www.mneme.co.jp/#
Dataplace Corp.	http://www.dataplace.co.jp (listed on regional start-up market)

Intellectual Property Information

<Intellectual Property Report>

Olympus
Kabu. com
HITACHI
Asahi KASEI
Hitachi Chemical
Bridgestone
KONICA MINOLTA
AJINOMOTO
ISEKI
TOKYO ELECTRON
MITSUI ENGINEERING & SHIPBUILDING
Anges MG, Mitsubishi Heavy Industry

Kikkoman, Haruna Corp
Japan Synthetic Rubber (JSR)
Taiheiyo Cement, TOSHIBA

<Annual Report etc.>

Asahi KASEI, Canon, JFE Steel
NEC, NTT Docomo, Matsushita Elec.
TOKYO ELECTRON, Omron
MITSUBISHI ELECTRIC, NTN
TAKEDA Pharmaceutical company
FUJITSU, Yokogawa, JR East
Osaka gas, Mitsubishi Chemical,
EPSON, Sumitomo Metal (May.2006)

Recent stage-up from Concept Building to Implementation

- New Strategy for Economic Growth (METI, June 2006) and
- Strategic Framework for Economic Growth (GOJ and ruling parties; will be published in July 2006)

(will) include following elements, which encourage IA based management in each segment.

- **Nation** - aiming at being the world innovation center
 - realizing a human resources based society
- **Region** - encouraging the regional management of its resources to vitalize economy
 - establishing a program to accelerate the business to utilize regional assets
- **Company** - enhancing the corporate value through IA based management
- **Human** - making plural paths for HRD

Growing Network of people concerned

Government

METI, Related Ministries

Local governments

Ruling Parties

Academics

Economics, Business Administration

Financial Engineering, IPRs

Market

Analysts, Stock Exchange, Institutional Investors

Financial Organizations

Development Bank, Regional Banks, Securities Firm

Related Business

CPAs, Tax Accountants, IR Business,

Consulting Firms, Auditing Companies

Rating Companies

**Organizations
to support
SMEs**

Business Enterprises

- Big Business
- SMEs
- Start-ups

Timetable

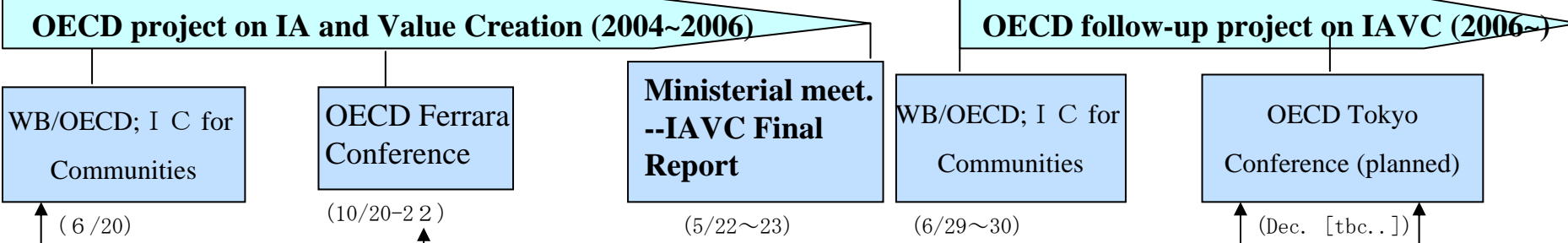
2005

2006

2007

Jun. Jul. Aug. Sep. Oct. Nov. Dec. Jan. Feb. Mar. Apr. May Jun. Jul. Aug. Sep. Oct. Nov. Dec. Jan. Feb. Mar.

International

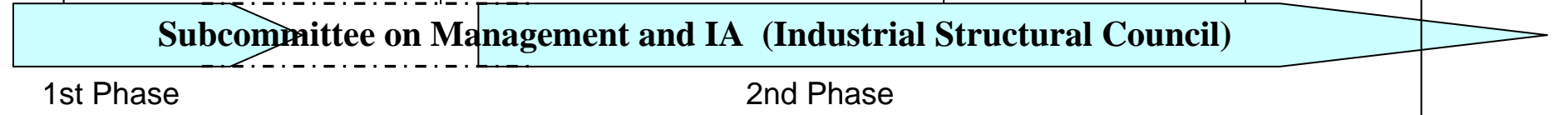


Domestic

- Interim Report (8/12)
- Guideline (10/14)

IASB·MC Working Paper (Public Comment) (05.10~06.4)

Comment to IASB Working Paper



Study Group on SMEs IA based Management (SMRJ)

IA Week 2005 (11/25-30)

IA Week 2006 (11/30-12/8 tbc.)

IA Week 2006 in Japan

Plans considered (subject to change)

Dates: From 30 Nov. (Thu.) through 8 Dec. (Fri.)

Planned Events

- Seminar for SEMs on IA based management (Osaka)
- Osaka Univ. Symposium on IA based management
- Workshop on IA based management (Waseda Univ.)
- IA Management Forum 2006 (Nikkei Shinbun)
- OECD Conference on IA (two days: tbc.)
- General Assembly of IA based Management Consortium