



HOW TO IMPLEMENT THE KNOWLEDGE ECONOMY PRINCIPLES ~Japanese perspective~

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May, 2008**

**World Conference on Intellectual Capital for Communities
- Fourth Edition -**

-Background

- What's missing in financial information?
- Elements of Intellectual Assets based Management
- Experiences in Japan
- Efforts in the World
- Next Step & WICI

Era of Differentiation & Intellectual Assets (IAs)

Aging economy with
less population
→ Smaller domestic
market

Global competition
→ Emerging economies
are more cost-competitive

Knowledge
Economy
→ Intangible
assets became
more valuable

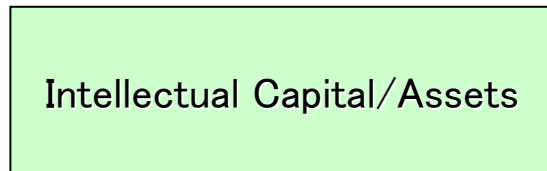
**Creating values/profits by making products or services
different from others is essential for business.**

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

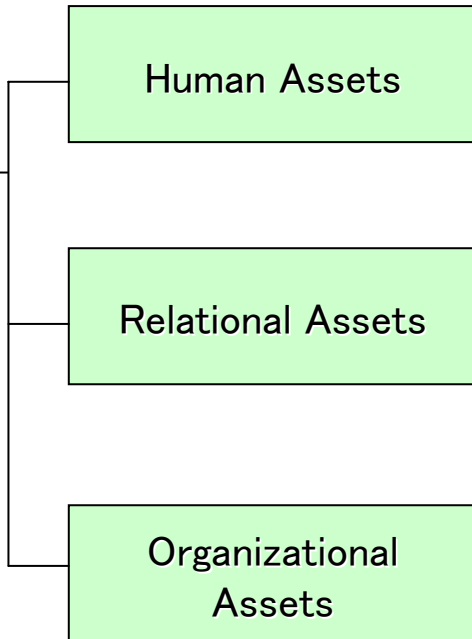
note: IAs include human resources, organizational capabilities, technology, and relational capital.

Elements of IA

Corporate Assets



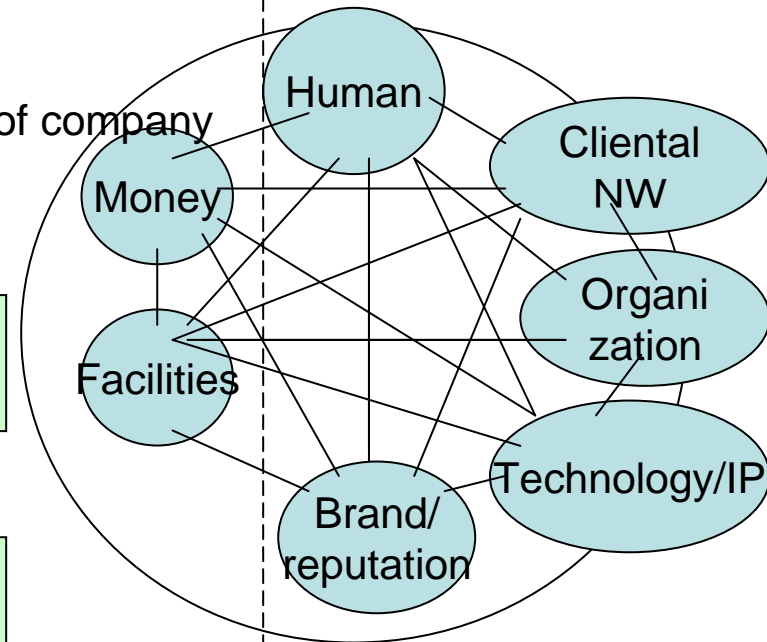
Classification of Intellectual Assets



Financial Assets

Intellectual Assets

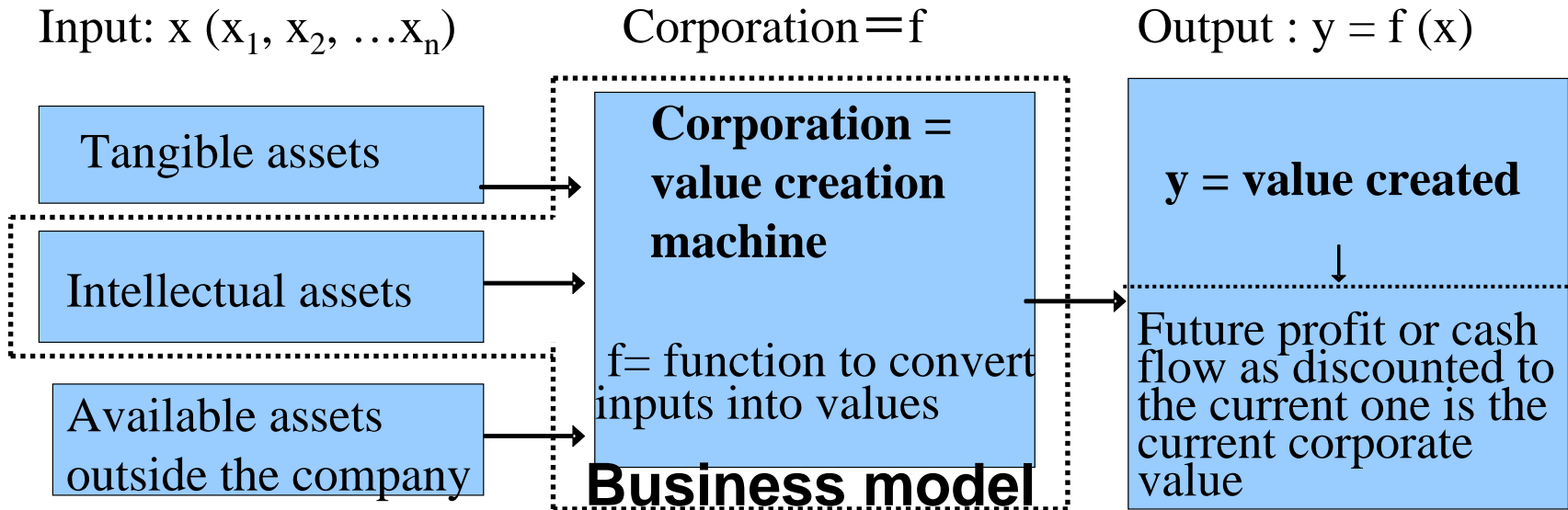
Boundary of company



Creation for Value / Profit

Real Corporate Value

Company is a value creation mechanism, which can be expressed in a metaphor of the mathematical function. The part surrounded by dotted line is usually invisible.



Not only IA itself (x), but also the conversion mechanism (f) to create values are substantial, since f is the very management.

IA and f last longer than tangible financial assets, therefore they are more reliable grounds for future achievement.

Limitation of Financial Information

Financial report does not reflect the real strength of a company based on intellectual assets.

Can we see the

- origin of the competitiveness
- value chain as a combination of peculiar IAs
- sustainability of the strength, and
- long term value

of a company from financial information?

Does the stock market evaluate properly these elements of a company?

Therefore, we need put more on

- non-financial information rather than financial information

- various intellectual assets without concentrating only on intellectual property among non-financial information

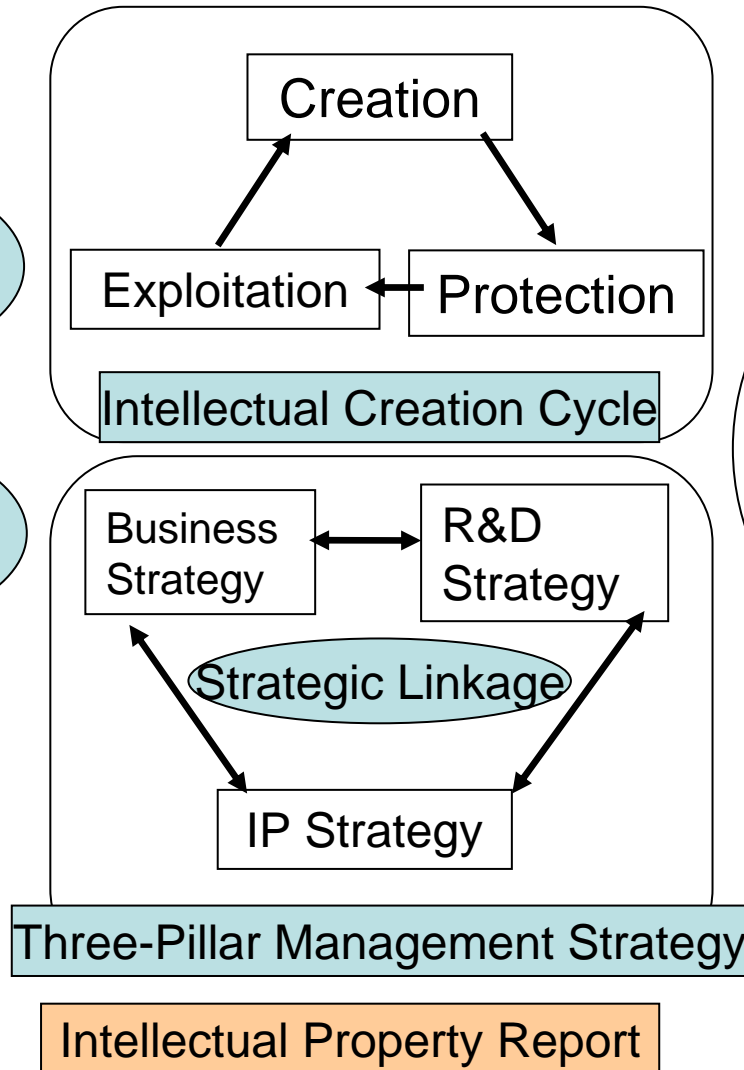
- management based on IAs rather than IAs themselves

Phase I

Protection of IP

Promotion of invention

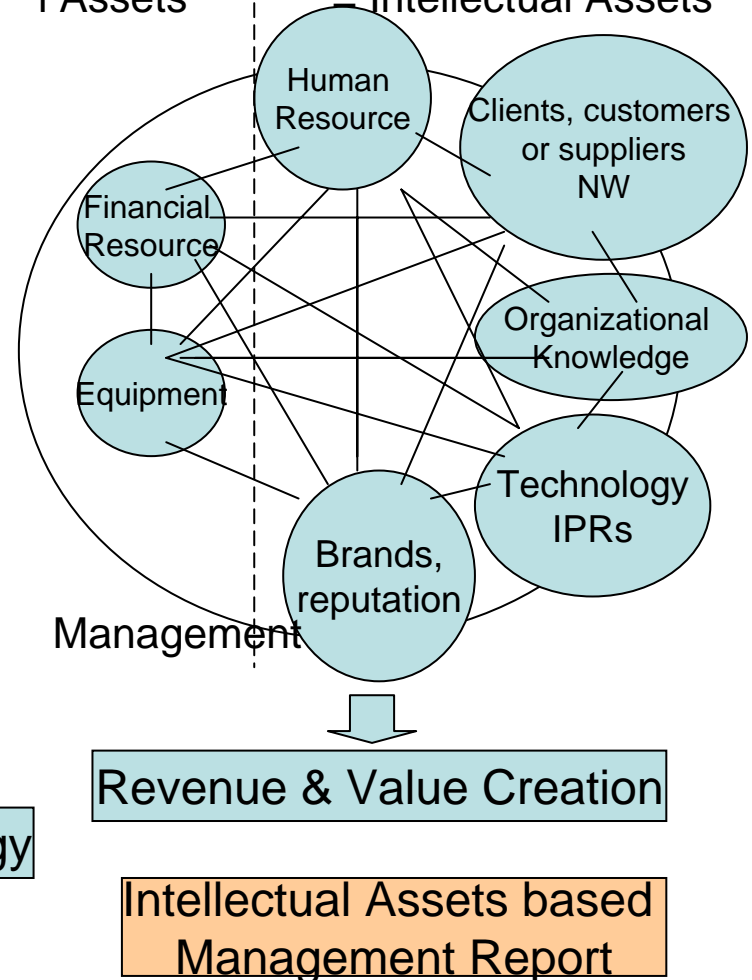
Phase II



Phase III

Financial Assets

Non-Financial Assets = Intellectual Assets



Benefits of IAbM for stakeholders

1) For top management

- realize and visualize the origin of competitiveness
- increase prospects for the **future value** of their business
- enables **optimal business resource distribution**
- Improve the understanding from outside

2) For shareholders

- Recognize the long-term value of the company

3) For financial institutions

- gain **credible ground for financing**

4) For clients and local communities

- **deepen understanding** and **more confidence in the company**

5) For employees

- **raise morale** by clarifying the basic philosophy of the company
- choose the most suitable company (for recruiting people)

Increase Corporate Value by utilizing IA

Difference between financial information and intellectual assets based management

IAs and IA based management

- No requirement to visualize
- Diversified
- Improvement in internal management first

Reporting in Accounting

- More mandatory disclosure
- Standardized in some way
- Mainly for interests outside the company

Elements and KPIs as proofs

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



Japanese Experience Progress since 2004

2004 Jun. White Paper on International Trade focusing the importance of IAs

2005 Oct. Guideline for Intellectual Assets based Management Disclosure_(METI)

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

Nov. 1st IA Week in Japan, Establishment of IA based management consortium (IAMaC)

2006 Mar. Interim Report on IAbM in SMEs (SMRJ)

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

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

Aug. Check list on IAbM for financial institutions (JICPA & Osaka Chamber of Commerce)

Dec. OECD IAbM Conference in Tokyo

2nd IABM week in Japan <http://www.meti.go.jp/information/data/c6073fj.html>

2007 Mar. Manual on IAbM for SMEs (SMRJ)

Apr. Report by WG under Financial Service Agency referring IAbM report

Apr. Amendment of innovation related laws to define the concept of IAbM

Sept. Germany- Japan IA/IC summit in Bodensee

Nov. 3rd IAbM week

International Conference on Intellectual Café

2008 Mar. Guide for recognizing and utilizing IAs (METI)

May/June- Project to promote collaboration of regional vitality using IAs (planned)

Nov. 4th IAbm week (planned)

Nov. WICI Forum

SMRJ: Organization for Small and Medium Enterprises and Regional Innovation in Japan

METI Guideline on IAbM Disclosure

History

Feb. 2005 Establishment of special sub-committee under Industrial Structure Council
 Aug. 2005 Mid-term report summarized by the sub-committee on IAbM
 Oct. 2005 METI published 'Guideline for disclosing IAbM'

Main Characteristics

- Encourages companies to express 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

- **Showing the overall picture from top manager's eye in a story**
- **Focusing on the future value creation that affects corporate value**
- **Evaluate future uncertainty (risks/chances) fairly and explaining how to deal with them**
- **Making a report easy to understand for important stakeholders**
- **Supplementing and being compatible with financial information**
- **Adding supporting KPIs to enhance credibility**
- **Providing historical comparability (e.g. KPI for the past two years)**
- **Making a report on a consolidated basis**

Element of the Story

- Nature of business and direction
- Corporate strategy, investment, accumulated IAs and unique value chain as of today
- Current business results
- Predicted uncertainties (risks and chances), accompanied by ways to deal with them, including investment
- Projected achievement in the future

Summarized IAbM Reports

-More than 30 companies have created and released reports based on the guidelines by METI.

Some companies have included their intellectual asset management reports in their annual reports.

-Through the R&D grant application process of NEDO, 240 companies in 2007 and 190 companies in 2008 summarized gist of IAbM reports, though they are not published.

※Some of these reports can be viewed from the web site of http://www.meti.go.jp/policy/intellectual_assets/index.htm

Private Initiative

- JASDAQ

Provided its companies IAbM self-evaluation tools

Established a new market (NEO) with severer requirement on IR (2006)

- JICPA

Reports on auditing IAbM reports (2006)

- JICPA Osaka Branch & Osaka Chamber of Commerce Checklist for IAbM (2006)

- IAMaC (Consortium on Intellectual Asset based Management) (2005-) with more than 100 professionals

Private Initiative (continued)

- **Association of department stores**
kicked off a study group for IAbM (2006)
- **Material Industries Association & METI**
issued a vision which encouraged IAbM as one of the main policies
- **Kyoto Institute of Technology (College)**
set up a curriculum in a seminar where students dispatched to a company built up IAbM report on it based on interview and disclosed information.
- **Waseda University**
established Waseda Intellectual Capital Research Society and has continued to make fundamental research on IAbM and to develop new scheme for IAbM reporting.

Global Initiatives

- **OECD projects (Japan is one of major promoters)**
 - **Intellectual Assets and Value Creation (IA-VC) project (2004-06)**
 - **IA-VC follow-up project (2006-08) with wider scope on regions and nations as well**
 - **OECD Innovation strategy project (2007-10)**
 - **IA or IAbM is recognized as one of important tools for innovation in companies including high growth SME**
- **EU projects: MERITUM(2002), PRISM(2003), RICARDIS(2006)**
- **World Bank: Conference on IC for Communities (2005-)**
- **New Club of Paris (2006-)**

Movement on Taxonomy Setting

- **Joint work between Germany and Japan**
 - Especially on taxonomy for Intellectual Assets/Capital Reporting, including supporting software for SMEs
 - Based on common experience of already published reports (almost 100 in Germany, more than 20 in Japan)
- **XBRL (eXtensible Business Reporting Language)**
 - SEC (US) announced to adopt XBRL in financial report in Sept. 2006 (effective this summer)
 - Japan has already introduced XBRL in EDINET system with regard to financial statements
 - XBRL International has been working hard
 - Application of XBRL to non-financial information will be the next hot issue, as EBRC (Enhanced Business Reporting Consortium) strongly recommends
 - WICI (World Intellectual Capital/Assets Initiative) was established in Nov. 2007



World network on XBRL & IAbM

OECD



Australia

Society for Knowledge Economics



Europe

Japan

US

EFFAS

(Financial Analysts Association)

Waseda Univ.

METI

EBRC

Founding member:
AICPA, GT, PwC, Microsoft

XBRL US

AEI

Univ. of Ferrara
(Italy)

KPMG Azsa

AICPA

Harvard Business School

PWC London

FSA

FASB

EU Commission

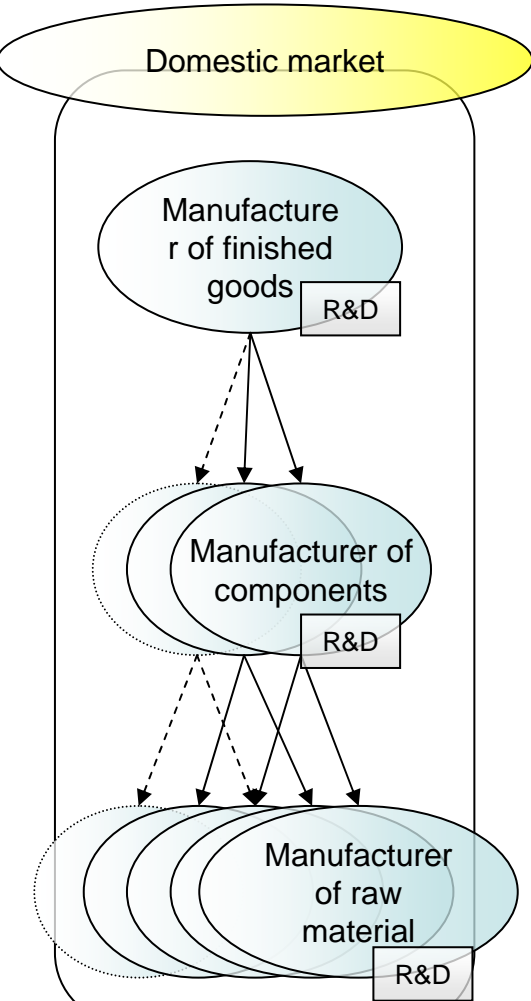
SEC



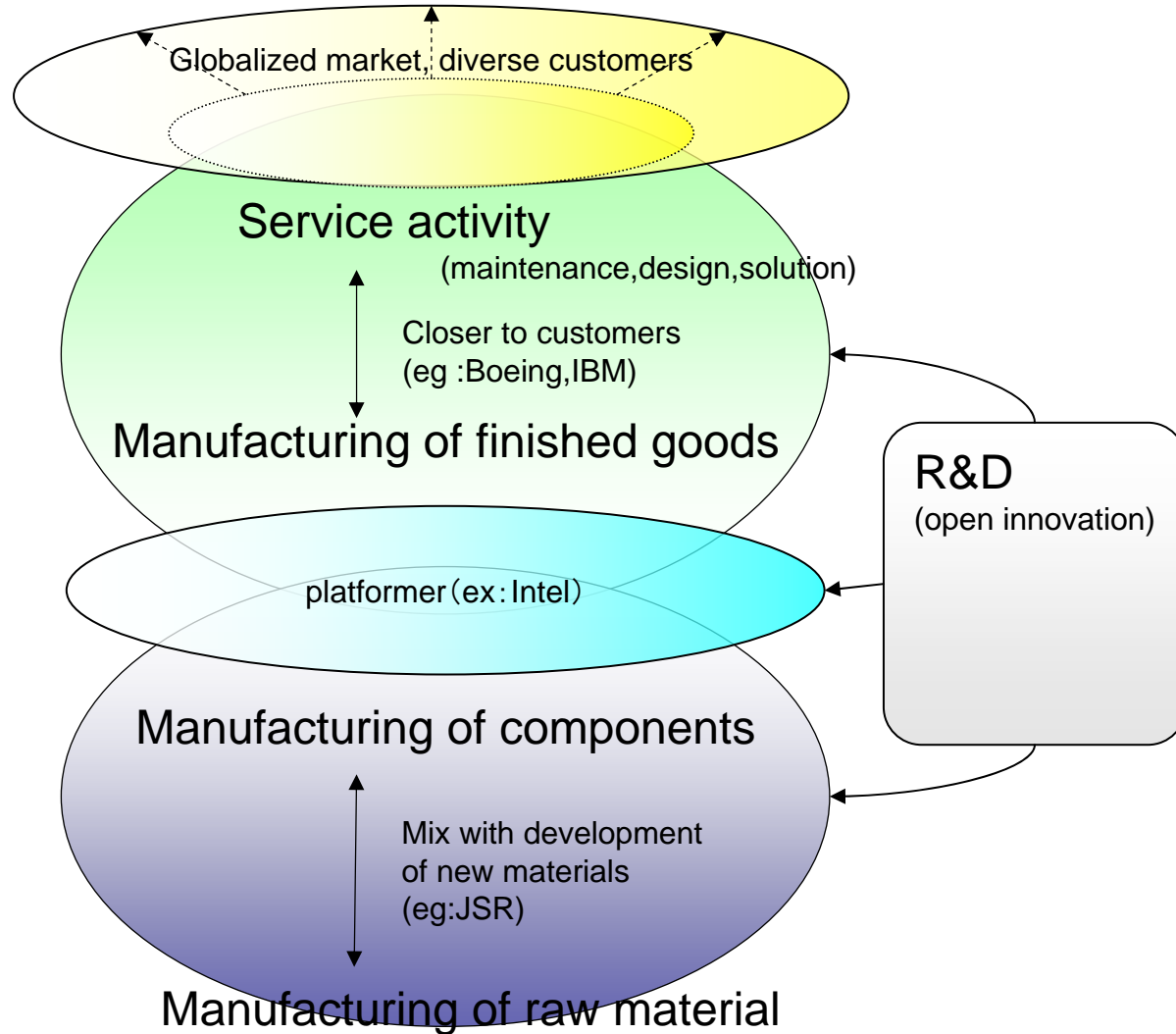
Intellectual Capital for Communities

“stove-pipe” model

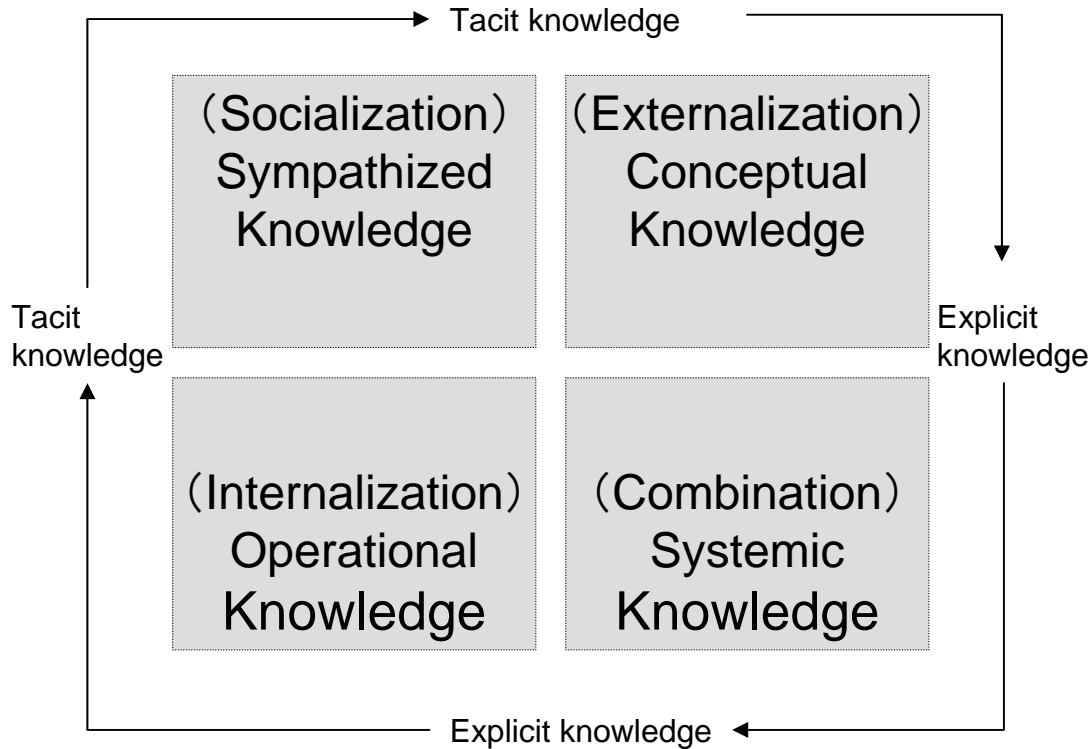
Transformation of industrial architecture



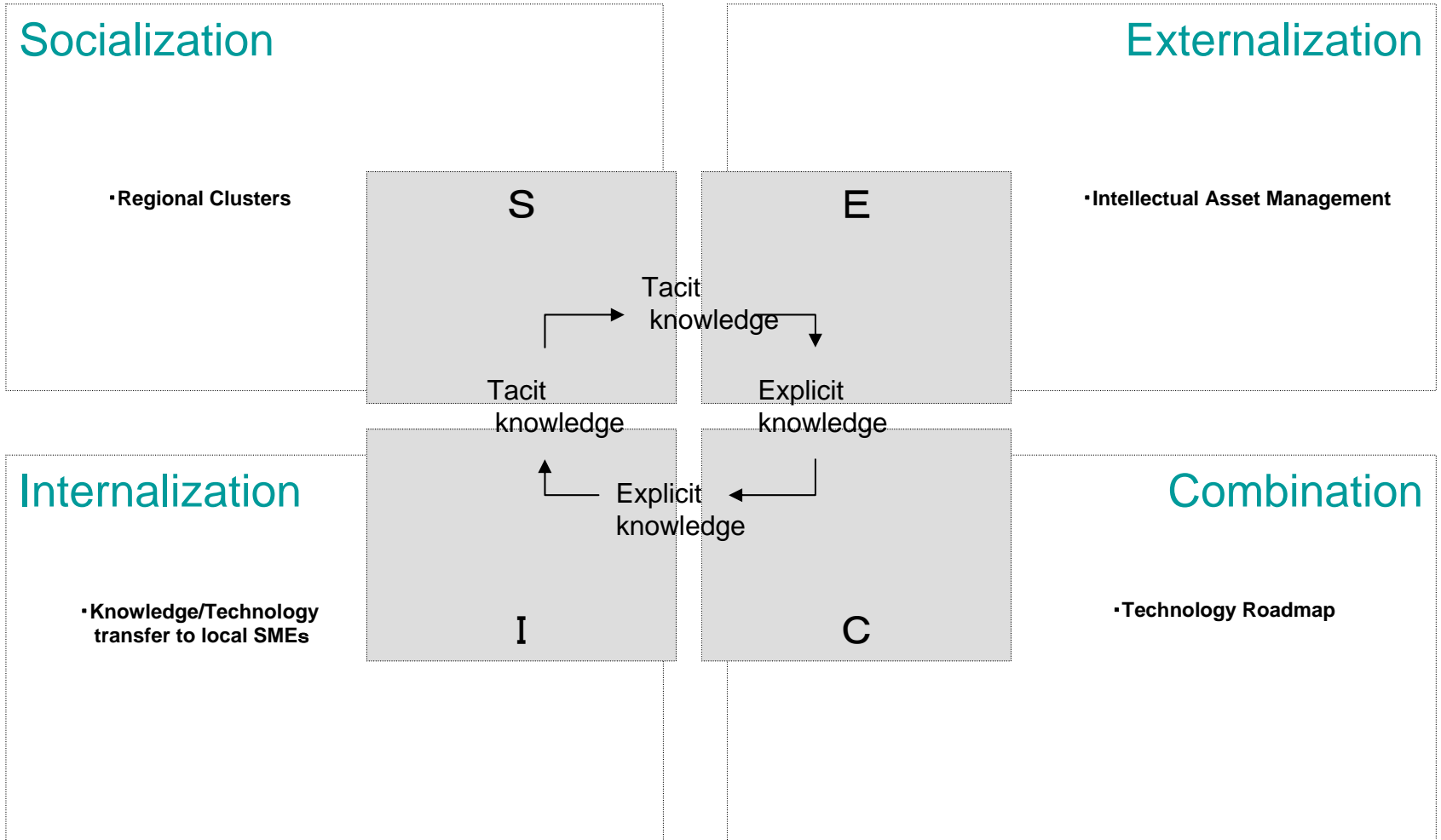
“hour-glass” model



The Knowledge-Creating Company-SECI model



SECI model (Source : Ikujiro Nonaka and Hirotaka Takeuchi .The Knowledge-Creating Company)



○ Technological Innovation

**Previous model : Innovation within particular sectors
Innovation within particular firms**

New model : Innovation across sectors / firms

→ **Open innovation → technology roadmap**

○ Mode Innovation

**Previous model : Innovation within particular categories
Innovation within particular brands**

New model : Innovation across categories / brands

→ **Colette : model (mixture of brands , arts , Street wears etc)**

○ Regional Clusters

Previous model : Networking within closed regional clusters

New model : Networking across regional clusters

→ **transformation of ‘ Italian growth model ’**

Fashion Map

