Importance of strategic readiness of intangible assets

In 2000, the market-to-book value, or in other words, the ratio of the stock-market value to accounting value of the largest 500 companies in the U. S, increased to 6. 3. In simple words this means that for every six dollars of market value, only one dollar appeared on the balance sheet as a physical or financial asset. The cause of this large difference has been attributed to the rise in value of intangible assets. (*Source: Getting a grip on Intangible Assets, Harvard Management Update)*

In the past decade, there has been an increasing academic and corporate focus on the subject of intangible assets offering clarity to business leaders on the ways to measure and manage these assets in context of a business's strategic goals. On regulatory front, European Union is soon to introduce standards for reporting on intangible assets.

Our report aims to analyse one such academic framework, developed by Robert S. Kaplan and David P. Norton, which highlights the importance of strategic readiness of intangible assets. The methodology of this conceptual framework is creation of a Strategy Map on which intangible assets have been mapped and measured.

Three key things that emerge from the analysis of this work named Measuring the Strategic Readiness of Intangible Assets and written for Harvard Business Review in 2004are:

1. Identification of the important intangible assets in a business organization.

2. Mapping these intangible assets to a business's strategy.

3. Understanding the factors that enable these intangible assets to contribute to the success of the business.

Introduction

It is increasingly clear from the example at the beginning, that, in 21 st century's knowledge-driven, services-dominated, economy, it is the intangible assets, and not so much the physical and financial assets, which are playing an increasingly important role in shaping a business's success. At the same time, it is realized by management, that there is a need to objectively evaluate the readiness of these intangible assets in enabling a business to achieve its strategy.

For the benefit of analysis, we start by defining intangible assets as any nonphysical assets that can produce economic benefits. These cover intellectual capital, knowledge assets, human capital and organizational capital as well as more specific attributes like quality of corporate governance and customer loyalty. (*Zadrozny, Wlodrek)* .

So what is required to map and manage these assets for the success of a business's strategy?

Analysis of Situation

According to Kaplan and Norton, while developing Balanced Scorecard (a concept for measuring a company's activities in terms of its vision and strategies, and helps to give managers a comprehensive view of the performance of a business), they identified three major categories of intangible assets:

No.	Intangible Assets	Encompassing Elements
1	Human Capital	Skills; Training; Knowledge
2	Information Capital	Systems; Databases; Networks
3	Organization Capital	Culture; Leadership; Alignment; Teamwork

Further, while understanding the critical success factors that transform a business organization into a performing and strategy focussed entity, the article discusses how these assets need to be mapped to the organization's strategy on a framework called strategy map. Finally it explains the route by way of which, quantitative values can be assigned which clearly help an organization to understand the readiness of these assets in enabling an organization achieve its strategy.

Discussions and Findings

As we discover, there are unique features of intangible assets that make their behaviour different from the physical and financial assets. These are:

1. Intangibles assets mostly cannot create value for an organization in a standalone form. They need to be combined with other assets. The implication of this is on a firm's ability to assign a value to these assets on a standalone basis.

2. These assets rarely affect financial performance directly, unlike physical or financial assets which immediately start paying off. Intangible assets contribute indirectly through a chain of cause and effect. For example, the

investment in training a team in total quality management may decrease defects and therefore may give rise to customer satisfaction and heighten positive brand perception.

3. While human capital and information capital are easier to map and manage, organizational capital is much more difficult.

4. Human capital may be measured by mapping the jobs and identifying the strategic job families before focusing on getting these jobs ready for strategy implementation. Information capital may be evolved by identifying and creating a portfolio of transactional, analytical and transformational computer applications and sturdy network infrastructure that give a positive edge to the manner in which business is conducted. One such example is the complete transformation in retail banking with deployment of information systems that empower a customer exponentially.

5. Organizational capital is the most challenging element to map and manage because of the complete behavioural change required in conducting business at all levels. Changing the base culture – that involves the employees' shared attitudes and beliefs, and the Climate – which comprises of the shared perception of the organization's policies, procedures and practices, require a grip on deep-rooted, socio-psychological dynamics at work within the organization. For example, changing National Health Services (NHS) culture from a budget oriented operations to a dynamic business plan oriented operations that focuses on health consumer, is more challenging than mapping the strategic jobs and putting state-of-the-art

information capital. For bringing organizational capital readiness, leadership plays a very important role, as do communication and knowledge-sharing.

6. Once these intangible assets are brought in state of strategic readiness, they start contributing in generating cash for the business. For example, if McDonalds sets a service response time of 30 seconds and trains its human capital to achieve this target, the customer turnover at the counter will increase and lead to higher revenues.

7. Finally, for these assets to come into a state of strategic readiness, they need to be aligned with the organization’s strategy. If they are not properly aligned, it can lead to chaos. For example, if McDonalds promises its customers a 30 seconds service but does not care to bring its human, information and organizational assets up to required standards, there will be widespread dissonance amongst its customer base and the risk of erosion in brand value will be very high.