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# trekking

a newsletter on practical strategic planning and action  
issue #12: is intellectual capital important to your business?

## editor's message

The term Intellectual Capital gets used a lot today—and with good reason. Success in today's world is often dependent on how we use knowledge. So what does that mean to you in your own business? You need to develop a way of understanding and actively managing Intellectual Capital. This month we will try to help you with that. In Strategic Planning, we give some background on the emerging management study of Intellectual Capital. In Strategic Action, we help you think about how to measure and manage it. Our Industry Snapshot looks at outsourcing and the Reading List reviews [Patriot Reign](#), a case study of excellent (and winning!) management.

## strategic planning

### *What is Intellectual Capital?*

My early career was spent in the finance industry. As a young bank officer, I spent many hours analyzing companies for credit presentations. We spent the lion's share of our time on the financial statements, and I spent plenty of time working on spreadsheets (at that time, you hit calc and went for coffee because it took so long...). We were also expected to write succinct evaluations of management, competitive position, and strategic outlook for the company. Unlike financial analysis, there was no set requirement, no consistent way of looking at the non-financial side of the business—we simply relied on our business education and experience.

When I started the predecessor firm to Trek, I faced the same challenge. I used the financial skills I had learned but had to work to find better ways of evaluating the non-financial side. There are countless management theories and practices that explain parts of the picture but no overriding system. However, this has changed over the past ten years, as this non-financial side has come to be addressed through the study of Intellectual Capital.

The most simplistic definition of Intellectual Capital is the difference between a company's book value and its market value; that is, everything that creates value for a company but cannot be captured by traditional accounting. Further, where accounting looks to the past, Intellectual Capital looks to the future earnings capacity of the company. This field is still evolving, but most people agree that a more complete definition of Intellectual Capital includes the following categories:

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- **Organizational Capital**—includes intellectual property as well as the processes and practices that help the company do its work
- **Human Capital**—includes both management and employees
- **Relationship Capital**—includes a company's brand, customer capital, and its network of vendors and other partners
- **Business Model**—includes strategy and competitive environment

This is a great framework for thinking about a company's non-financial side and a helpful scorecard for thinking about the future.

-Mary Adams ([adams@trekconsulting.com](mailto:adams@trekconsulting.com))

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## strategic action

### *How to Round Out Your Internal Information*

By many estimates, over half of the market value of public companies today is in Intellectual Capital. For some companies, Intellectual Capital can represent more than 90% of their value (think eBay, Google, Microsoft). Even if you have a traditional, more "hard" asset intensive business, what will be the key to future success—assets or Intellectual Capital? If Intellectual Capital is going to be important going forward, what are you going to do about it today?

We encourage people to start looking at Intellectual Capital from a strategic perspective. Sure, you have specific functions for human resources, IP, sales and procurement. But, are you looking at the trees and not the forest? Do you look regularly at your full capital picture, including both physical and Intellectual Capital? Can you say how you measure up, not only internally, but in comparison with your competition? What is the dynamic among all your factors of production, both tangible and intangible? These are helpful questions for companies to ask that want to think and act strategically.

But, how do you actually evaluate Intellectual Capital? At a macro level, we use a variety of approaches. Good old fashioned research can help with competitive analysis. But, the most powerful tool is to ask your stakeholders, including employees, customers and market partners. You need to have structure for this process so that you get comparable, usable information. The Intellectual Capital framework is a powerful way of organizing your research and analysis for the best strategic decisions and action. This is a powerful concept—so stay tuned to hear more from us in the future about Intellectual Capital.

- Michael Oleksak ([oleksak@trekconsulting.com](mailto:oleksak@trekconsulting.com))

## industry snapshot

### *The Contradictions of Outsourcing*

Outsourcing is a strategic option that cannot be ignored in today's world. The lower cost is compelling, but the trade-off is higher risk. To minimize that risk, put in place systems that will ensure high quality production. Here are some things to think about as you develop these systems:

- Prepare more thoroughly than you ever have within your own organization.
- Understand your own process first. What needs to be done—step by step?
- Communicate precisely. With distance, time, culture and language all working against you, you need to find a way to ensure that your message is understood.
- Create processes for communication and oversight.

However, putting this type of quality system in place has an interesting consequence that was recently pointed out by a client of ours, Dave Vogel of Intertech Engineering Associates, who is an expert on software quality. In an article on offshore software development, he and a colleague asserted that following strict quality practices, such as those described above, could actually enable an organization to achieve productivity improvements domestically that might exceed the cost benefit of going off shore. Their findings are an interesting reminder to all companies evaluating an outsourcing strategy. To learn more, read their entry in the Handbook of Business Strategy (<http://www.inea.com/Body/articles/Handbook%20of%20Business%20Strategy%202005%20-%20Offshoring%20-%202%20column.pdf>).

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## reading list

### *Patriot Reign* by Michael Holley

Michael Holley has written an excellent insider's account of the success of Bill Belichick, owner Robert Kraft, and the New England Patriots. My status as a long-time fan aside, this is a great story of strategic management at its best.

Patriot Reign shows how Kraft and Belichick built the teams that have now won three of the last four Super Bowl championships. Holley reports on Belichick's long-term relationships with the current management team (the Krafts, coaches and scouts), his search for and retention of intelligent personnel (players), the qualities he looks for when recruiting and hiring (the draft and free agency), his recent mastery of public relations (media), and lessons learned. Holley describes the cooperative approach among coaches and thorough communication with players for game planning. He reveals how Belichick and staff used intense research and their own

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needs analysis to prepare for its hugely successful 2003 college player draft. Holley explains how Belichick's team determines and assigns value, a system that led to the release of popular players such as Drew Bledsoe and Lawyer Milloy.

Football fans will enjoy the inside story that Belichick permitted Holley to report. Business people will see the development of a systematic process that has created success that is the envy of others. For more information, visit the Harper Collins Web site ([http://www.harpercollins.com/global\\_scripts/product\\_catalog/book\\_xml.asp?isbn=0060757949](http://www.harpercollins.com/global_scripts/product_catalog/book_xml.asp?isbn=0060757949)).

- *Michael Oleksak* ([oleksak@trekconsulting.com](mailto:oleksak@trekconsulting.com))

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## announcements

Trek was featured in the Family Business Magazine E-News with our piece entitled, "What Drives Shareholder Value in Family Firms?". Click here to read the full text of the article ([http://www.trekconsulting.com/Publications/Articles/FamilyBusiness-Magazine\\_03\\_21\\_05.pdf](http://www.trekconsulting.com/Publications/Articles/FamilyBusiness-Magazine_03_21_05.pdf)).

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This issue closes out the first full year of Trekking. So far, every issue has published at exactly the same time each month, thanks to discipline of our principals at Trek and the folks at Square Peg (<http://www.squarepeg.biz/?TrekNewsletterAnnouncements>), who thoughtfully edit and produce each issue. We thank you for your support and invite your feedback.

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Next month, we will talk about getting outside input.

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## about trek consulting

Since 1999, Trek Consulting has helped CEO's of early stage and middle market companies to face challenges of growth, change and succession. Our hallmarks are fresh information, disciplined analysis and practicality. We help you create specific action plans with metrics tied to revenues, costs or corporate value. Then we follow up to help you keep on track and/or adjust your plans as circumstances change.

Our clients report improved market focus, increased revenues, better margins and lowered costs. To learn more about Trek Consulting and how we can help you improve your company's results, visit us on the web at [www.trekconsulting.com](http://www.trekconsulting.com) or call us at 781-729-1008.