School of Economics and Management
Lund University

Master Thesis
February 2003

Intellectual Capital in the evaluation process

A study made in the bank sector

Authors:
Karin Bengtsson
Katarina Paulin
Maria Svensson

Tutor:
Leif Edvinsson

FOREWORD

This paper is our master thesis in Strategic Management at School of Economics and Management, Lund University. By making this paper, we have obtained knowledge in the concept of Intellectual Capital and interesting insights in the evaluation process made in the bank sector.

To begin with, we would like to express our gratitude to our tutor Professor Leif Edvinsson, for inspiring us with enthusiasm during the working process. He also made it possible for us to attend the two "milestone" conferences in Oslo and Copenhagen and also encouraged us through conversations.

We want to thank all our respondents for giving us helpful information and for sharing their thoughts with us: Danske Bank Credit Department in Copenhagen, Niels Takklo, Lise Gronø and Thomas Justinussen; Skånes Provinsbank in Malmö, Magnus Paulsson and Cecilia Arkestad; Danske Invest Administration A/S, Carsten Koch. We also want to thank Krister Bengtsson at Smålandsbanken in Växjö for helping us with our first contacts as well as Tomas Paulin and Mattias Bengtsson for good advice and ideas.

Lund, February 2003

Karin Bengtsson *Katarina Paulin* *Maria Svensson*

SUMMARY

Title:	Intellectual Capital in the evaluation process. A study made in the bank sector
Subject:	Master Thesis, FEK 591 Strategic Management, February 2003
Authors:	Karin Bengtsson, Katarina Paulin, Maria Svensson
Tutor:	Leif Edvinsson
Problem formulation:	Traditional accounting and financial reports do not provide sufficient information today. New reports like the Intellectual Capital Statements are one answer to this problem. They systematically report on Intangible Assets that create value in the company. We found that external stakeholders do not use Intellectual Capital Statements in their evaluation processes. This made us wonder; *Why external stakeholders, in this case banks, do not consider non-financial information, like the Intellectual Capital statement, in a systematically manner when evaluating companies.*
Purpose:	The purpose of our thesis is to find out why banks do not consider non-financial information systematically, when evaluating companies. We hope that our thesis will start a learning dialogue within banks on how they will handle non-financial information, in order to improve their evaluation processes.
Method:	Our thesis is created through an interaction between the *deductive* and the *inductive* way. The investigation is made according to the *hermeneutic spiral*, which combines theory with the empirical work. Primary and secondary data has been gathered through a qualitative approach. By attending two milestone conferences with world renowned thought leaders in the field, we have collected as updated information as possible about newly proposed approaches. Interviews have been made at different departments in the Danske Bank group.
Conclusion:	Many reasons were given, but it appears as the major answers to our purpose are: there is a *lack of a standard* for the Intellectual Capital Statements and no commonly accepted terminology. This makes it almost impossible to make comparisons between different years and companies. They are *not functional* in their present shape and there is a lack of stringency. Another reason is that *too few companies are reporting* Intellectual Capital Statements. The financial statements are the ones that still are the most important information sources in the decision-making process.

Keywords: Intellectual Capital, Intangible Assets, non-financial information, evaluation, external stakeholders, banks

TABLE OF CONTENTS

1

PREFACE

"*The most important factor of production is small, grey and weigh on an average 1,3 kg. It's the human brain*."
(Nordström & Ridderstråle, 2000, page17)

1.1 INTRODUCTION

Our society is changing on many levels and at an increasing speed. We talk about the *New Economy* or the *Knowledge Economy*, which is characterised by several factors that are dissimilar from the ones characterising the traditional economy. Examples of these characteristics are: increased digitalisation, technological change, increased uncertainty, globalisation and application of knowledge. These different characteristics affect the way we look at things today. For example, we used to consider tangible assets like natural resources, machinery and products, as the basis for value creation. Instead we find that the Intangible Assets are becoming increasingly important (www.videnskabsministeriet.dk).

According to Malm (Lecture, 020905), today Intellectual Capital is a company's most important factor. The quality and uniqueness of the knowledge component, has become the most important source of competitive advantage. The New Economy is developing into a global network society, were ICT (Information and Communication Technology) are reshaping the communication both inside and between organisations. ICT is also creating leverage on the knowledge base and accelerates the knowledge development. The New Economy with rapid development of ICT creates an explosion of new business opportunities and erodes the business concept of traditional firms.

This development is also reflected by the increasing amount of the so-called *knowledge intensive companies*. According to Sveiby (1990) a knowledge intensive company is a company that exists by selling its know-how. Their production processes is often non-standardised, creative and highly dependent on the individual's ability to solve complex problems. This means that the knowledge company is, to a much higher degree dependent on the employees' individual skills and competence. Stewart (1999) means that due to the emergence of the New Economy, knowledge has become the most important factor of production and value creator. Consequently, it is becoming increasingly important for companies to visualise its knowledge assets in a more complete manner than before.

The general opinion is that the old accounting and reporting models cannot reflect reality in a sufficient manner. As a result, the pressure has increased on creating new, improved instruments that can give a more complete holistic picture of the company. (Lev, May 2000)

"*The development of standardized measurement and reporting modes for key elements of the new information structure will be an important contribution to improved accounting and reporting*" (Lev, January 2000).

One obstacle though, is the lack of a globally accepted definition and classification of relevant terms to be able to describe the knowledge assets. *Intangible Assets* are one example of terms that are currently being used. It appears to be an umbrella concept for several key production factors other than capital and labour. (www.ll-a.fr/intangibles/overview.htm)

OECD defines the term as:

"*non-material factors that contribute to the growth and performance of firms or nations without being included in the traditional category of fixed assets*" (Ibid.)
An alternative definition is:

"*sources of future potential benefits which do not have a physical embodiment*" (Lev, January 2000).

These definitions are not making the concepts any easier to grasp. Some examples of what Lev (Conference, 2002) includes in the concept of Intangible Assets that might help to clarify the phenomenon are: patents, know-how, brands, franchises and other customer-related assets. Other terms that are being used are *Intellectual Capital* (Edvinsson & Malone, 1997; Gu & Lev, 2001; Olve, Roy & Wetter, 1999; Stewart, 1999; Sullivan, 1998) and *Intangible Assets* (Grant, 2001;Gu & Lev, 2001; Sveiby, 1990). According to Evinsson & Malone, the term Intellectual Capital is somewhat broader and the distinction is that the concept includes future earnings capabilities besides financial assets. Some will find differences between these terms, others will claim that they have the same meaning and describe the same reality.

2

PROBLEM DISCUSSION

"To increase the usefulness from the traditional statements, like the annual report, we need to improve them, so that they also consider the value of the intangible assets" (Lev, 2000)

2.1 BACKGROUND

According to Stewart (1998) established accounting principles are based on 500 years of history. They have been refined, but not entirely changed during the years. The author thinks that the old principles are suitable for industrial companies, not for the knowledge intensive organisations in today's New Economy. In the Industrial Economy an idea was not worth anything until it could be transformed into a physical asset where the economic value easily could be estimated. In the New Economy, the values of the Intangible Assets are becoming more recognised since they are important value creators.

There are two main purposes with visualising an organisation's Intellectual Capital, *internal management* and *external reporting* (www.sveiby.com). The internal management purpose deals with the monitoring and assessing of the development of the knowledge assets. This is done in order to be able to make correct decisions and adjustments of the knowledge management. The external reporting purpose handles the information need from external parties like customers, creditors and stockholders.

When it comes to the external reporting, traditional accounting recognises and deals primarily with tangible assets and is not designed to deal with the conditions that exist in the New Economy. This makes it hard to value a knowledge intensive company and compare it to others. According to Lev (May, 2000), the knowledge capital is not reported in financial statements and because of this, users are not informed about 60-80 percent of the company's value. Investors have to "guess" what the true market value of the company is. Therefore they request more non-financial information opposed to financial information, since the traditional accounting no longer serves the needs of most external stakeholders. (Lev, May 2000)

Disadvantages with the traditional accounting methods that we have to come to terms with when forming new improved reports are that they do not communicate the value creating innovation process. This process has three fundamental phases: discovery/learning, where new products processes and services are developed; implementation, of the new

processes/services; and commercialisation, by bringing them quickly to the market. A problem with the current financial statements is that they look backward instead of forward. They deal asymmetrically with uncertainty by recognising expected losses but ignoring expected gains. Finally they also exclude all information on employee training, brand enhancement, R&D et cetera. (Ibid.)

These disadvantages can result in the following negative consequences at three levels (www.ll-a.fr/intangibles/overview.htm):

- *Business-internal level*: failure to visualise an organisation's knowledge assets makes it more difficult for management to make correct strategic decisions. This may prevent Intellectual Assets from being optimally used and renewed within the organisation.

- *Business-external level*: the lack of adequate external information concerning Intangible Assets could be making it harder for knowledge intensive companies to attract external financing and be correctly evaluated by external stakeholders.

- *Macro level*: the government's own accounts are heavily based on tangible investments. The lack of reliable statistical information and data on intangible investments makes it difficult to verify or to monitor its progress. It also makes it more difficult to assess the importance for competitiveness and growth of industries and national economies. This could actually result in a slow down in the growth potential of the knowledge economy.

Today's decision-making and decision support involves more and more information. Customer leveraging in co-operative environments, like cluster models, and value is no longer added through the traditional value chain perspective. According to Edvinsson, Kitts & Beding (2000), the traditional concepts of command and control seems out-of-date. Instead, new levels of knowledge navigation and monitoring of information is required, where one reason is the increased customer leveraging.

In Sweden, a group called *Konradgruppen*, started during the 1980's to investigate how to make annual reports more informative. Their work was primary concentrated on finding new key figures for accounting, control and valuation of different knowledge intensive companies (Konradgruppen, 1989). Several companies have also tried to come up with their own methods on how to visualise their Intangible Assets. The insurance and finance company Skandia was the first one to publish an annual report with an additional separate report on their Intellectual Capital, 1995. Skandia also developed the Navigator, which is the model that they use to visualise their Intellectual Capital (Edvinsson & Malone, 1997).

Denmark is now one of the first countries to develop a guideline for Intellectual Capital Statements for external purposes. The over all reason for creating the guidelines was to improve the framework of conditions for companies operating in the New Economy, but also because of the increased interest in Intellectual Capital Statements. The new improved and more practical extended version of the guidelines was released in December 2002. (www.videnskabsministeriet.dk) Another attempt to create some form of guidance on how to visualise Intellectual Capital externally comes from Norway and an organisation called the NFF, The Norwegian Society of Financial Analysts. They have tried to create a guideline from a Norwegian perspective with the aim to contribute to a more accurate valuation of

companies. This is done by providing information that is relevant for understanding the value creation processes in a specific company. (NFF conference, 021128)

In the European Union a proposition is made that states that all companies quoted on the stock exchange, should present their annual reports according to the IAS-standards no later than 2005. The IAS-38 for example is a standard for the accounting principles on Intangible Assets published by the International Accounting Standards Committees (IASC). The standard requires an enterprise to recognise an Intangible Asset if certain criteria's are met. It specifies how to measure the carrying amount of Intangible Assets and requires certain disclosures regarding them (www.iasplus.com). Another project that is related to Intangible Assets is MERITUM, which is about measuring intangibles to understand and improve innovation management. This is a research project financed by the European Union that has resulted in a proposal for consensus on a guideline, how to control and report on Intellectual Capital for internal purposes. (NFF, 2002)

2.2 PROBLEM FORMULATION

We became interested in the implications that are related to one of the three levels; the business-external level. Our definitions of external stakeholders are for example venture capitalists, investors, banks, the government, trade unions, accountants et cetera. We wanted to investigate from external stakeholders' point of view, the need of non-financial information when evaluating companies. We continued our study by looking at the bank sector as a representative for one of the external stakeholders and how they work with Intellectual Capital Statements in their decision-making process. The reason for choosing the banks are that they are considered to be traditional organisations that work daily with evaluating companies. It is therefore interesting to look at their working norms and policies.

In our primary investigation, we found out that depending on what level and what department we looked at, we sometimes got dissimilar answers. Some looked at as much information as possible, while others investigated a certain amount that they knew was needed. This made us wonder why banks as external stakeholders do not consider non-financial information, like the Intellectual Capital Statement, in a systematically manner when evaluating companies. After all, there seems to be many useful models like the different guidelines that can be more systematically applied in their evaluation process.

2.2.1 Purpose

The purpose of this thesis is to find out why banks as external stakeholders do not consider non-financial information systematically, when evaluating companies.

On our primary investigation we came across three aspects that we want to consider:

- When it comes to evaluating a company, is the financial statement the most important source of information?

- Is it true that banks as external stakeholders are reluctant to assimilate new methods and information sources like Intellectual Capital Statements in their evaluation processes?

- Could a possible explanation to the questions above be a lack of knowledge on an individual and/or organisational level?

2.2.2 Our focus

Different external stakeholders value different kinds of information in different ways depending on what their purposes are. We decided to limit our empirical investigation to a study of Danske Bank in Copenhagen, Denmark, Danske Invest in Copenhagen, Denmark and Skånes Provinsbank in Malmö, Sweden. The reason for choosing the bank sector was that we wanted to investigate an external stakeholder since we were interested in the *external* use of Intellectual Capital Statements. Two banks are interesting to investigate since they are part of the same organisation but operate in different countries. Danske Invest is a unit trust group with close relationship to Danske Bank and a part of Danske Bank Group. In this way we wanted to investigate departments that evaluate companies for different purposes within the bank. The reason for this is that we decided to limit our study to one bank, in which we wanted to go deeper into.

2.2.3 Target Audience

The target audience for this thesis is different banks, investment corporations and companies, especially knowledge intensive organisations. Another category is students and faculty members of School of Economics and Management, Lund University that might find our thesis interesting.

We hope that our thesis will start a learning dialogue within banks on how they will handle non-financial information that they are in need of. This should be done in order to improve their work and evaluation processes. We also hope that there are companies that might feel inspired to explore how to visualise their own Intellectual Capital. Arguments for this are the benefits with additional statements discussed in our thesis as well as the fact that companies will be required to report on this information in the future.

2.2.4 Disposition

Our thesis will investigate why an external stakeholder, like a bank group, does not systematically consider non-financial information in their evaluation process. One aspect in our purpose was to consider if there is a lack of knowledge concerning how to interpret Intellectual Capital Statements. Therefore this thesis includes a chapter with theories about learning organisations and knowledge management. The theoretical framework furthermore describes the concept of Intangible Assets and Intellectual Capital and gives examples of how to report on them. Existing banking approaches and theory about the evaluation process is explained as well as new reporting approaches for Intellectual Capital.

The material was collected from two milestone conferences, Interviews in Danske Bank, Skånes Provinsbank and Danske Invest as well as from literature made by professors, analysts, bankers and investors point of view. Finally, an analysis is made and conclusions are drawn from the theoretical and empirical studies, to answer our purpose.

3

METHOD

In this chapter we are going to explain how we decided to write a thesis on this subject, our course of action concerning the information gathering and choice of research object. The purpose of this chapter is to give the reader an understanding for the choices that we have made during our work, and how this affects the results presented later on.

3.1 HOW WE DECIDED ON THE SUBJECT OF OUR THESIS

We first came in contact with the term Intellectual Capital through the master course Strategic Management (FEK553) at Lund University. Professor Leif Edvinsson had a couple of lectures on the subject that caught our interest. We quickly learned that there is a great demand and a need to visualise the Intellectual Capital in companies around the world. We were among other things introduced to the Navigator, a model on how the insurance company Skandia chooses to visualise this form of capital to consist both internal and external stakeholders.

After having a discussion with Professor Edvinsson on possible approaches to the subject of the external reporting on Intellectual Capital, we decided to make a primary investigation. The reason for doing this was to gather more information on the subject in order to be able to formulate the question that our thesis was going to discuss. During this investigation many questions arose, but we finally decided to focus on why banks as external stakeholders do not consider non-financial information, like the Intellectual Capital Statement, in a systematically manner when evaluating companies.

The reason for investigating this particular question was that we found it interesting to understand the motives that banks have for not working systematically with non-financial information. This, since they seem to have well-established rules and guidelines on how to work with other kinds of information like financial information.

3.1.1 Perspective & Reference frame

The perspective works as a lens through which the investigator sees reality and chooses different aspects that are considered as relevant. It is also through the perspective that he/she interprets reality. (Lundahl & Skärvad, 1999)

Our perspective is the banks' point of view. We wanted to investigate what motives these stakeholders have for not systematically look at non-financial information when evaluating

companies. Therefore, we have not discussed the internal uses and benefits of Intellectual Capital Statements thoroughly.

A reference frame can be analogous with a pair of glasses through which one study reality. It is created from all the knowledge and information that has been collected and studied as well as from previous knowledge. We are aware that our education as well as our experiences will affect the way we interpret the information that we have collected. We are also aware of that the conclusions we make during the process of writing this thesis will add to our reference frame, as our knowledge about the matter increases.

3.1.2 Choice of research object

Our reasons for choosing to investigate Danske Bank and Skånes Provinsbank are: the banking sector interested us from previous experiences since one of us had been working in a bank during the summer and another has a parent working in a bank. The bank sector is also interesting to study since they often have policies as standards for almost everything and work daily with evaluating companies. The reasons for choosing the specific bank group are the close relationship between the banks – they belong to the same concern and are operating in two different countries with diverse accounting laws.

We used our contacts within the bank group in Sweden, in order to find some one who could help us with the information needed both in Denmark and Sweden. The first person in Danske Bank that we came to talk with was Niels Taklo, Managing Director at the Credit Department in Copenhagen. He then forwarded our questions to others within his department and the Swedish equivalent that might be valuable for us to talk with.

At the conference about new guidelines for Intellectual Capital Statement in Copenhagen (December, 2002), one of the lecturers was Carsten Koch, Managing Director at Danske Invest. In this way, we contacted Denmark's largest unit trust group, operating in the same Danske Bank group.

3.2 OUR COURSE OF ACTION

We followed an interpretation model that is sometimes called the *hermeneutic spiral*.

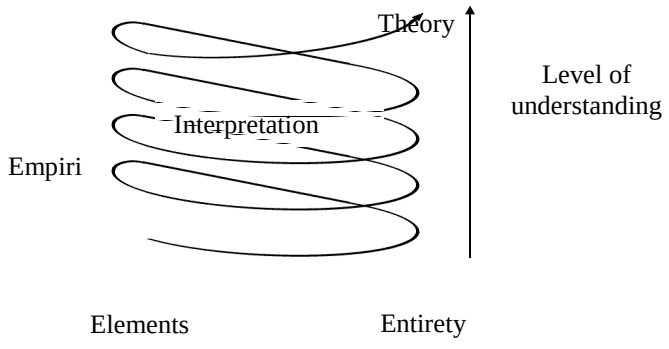

Figure 1. The hermeneutic spiral. Source: Made by us, inspired of *Att utreda, forska och rapportera* Wiedersheim-Paul, F & Eriksson, L-T (1991 4:th edition)

The starting point is the individual's previous knowledge. It is through this knowledge that one formulates questions, hypothesis and ideas about something that one wants to investigate. The next step is to start a dialog with the material that is being investigated. The reason for using the term dialog is that it deals with a form of two-way communication. The researcher asks questions and reacts to the answers and interprets them. This results in a deeper understanding for the problem, which leads to new questions and so on. (Wiedersheim-Paul & Eriksson, 1991)

Our thesis is created through an interaction between both the *deductive* and the *inductive* way to draw conclusions. When you start with the empirical material and use the experiences to create a common theory, then your conclusion is inductive. If the starting point on the other hand is theory and your conclusions are made from general principles, your conclusion is deductive. (Andersen, 1998)

The qualitative method's objective is to create a deeper understanding of the problem that is being investigated (Andersen, 1998). Since the purpose of our thesis is to create a deeper understanding for the motives to why non-financial information is not systematically investigated, we choose to use a qualitative approach. This type of study draws its conclusions from factors like attitudes, values and conceptions etc (Lundahl & Skärvad, 1999).

3.2.1 Information gathering

Primary data is material that the authors collect themselves, while *secondary data* is material that others have collected earlier (Lundahl & Skärvad, 1999). We have used both primary and secondary data in our thesis. Secondary data was collected via the Internet, literature, articles and annual reports etceteras. It provides valuable information on the current theories, others' experiences, investigations and thoughts. A thorough and systematic examination is important in order to accomplish a good result. (Andersen, 1998)

We started out by searching the Internet for information on the subject by looking at different sites that had been brought to our attention. They lead us further to other sites of relevance. We also used different navigators like www.altavista.com and www.google.com to search for information on keywords such as: Intellectual Capital, Knowledge Management, Intangible Assets and names of relevant persons, such as authors and professors related to the concept. The findings lead us to different book titles. Some of which were published on the Internet and others, which were available in libraries. There is not yet very much written about the specific problem that we wanted to investigate. Most of the books deal with the problem to visualise the Intellectual Capital and gave examples of how this can be done in a productive way. We quickly realised that we had to talk to experts in the area, in order to get all the material we needed for our thesis.

The primary data was gathered during different interviews and conferences. It has mainly been used in order to increase the understanding of the questions that has come up during our work. In order to capture attitudes and thoughts on the subject, we needed to make interviews. These were made with six employees, three at Danske Bank, two at Skånes Provinsbank and one at Danske Invest. We believe that banks are traditional and homogeneous organisations. With six persons made in three different departments within one bank, we think those different employees' thoughts about the evaluation process are represented. Therefore the operating and evaluation processes are similar in the bank sector, and general conclusions can be made.

In order to use as updated information as possible on the concept, Professor Edvinsson arranged for us to attend two milestone conferences about Intellectual Capital Statements, one in Oslo, Norway and one in Copenhagen, Denmark.

The conference in Norway (November, 2002) was organised by the Norwegian Society of Financial Analysts. The theme was to *"Turn the company's inside out"*. By this they meant that with the help of additional information on the company's value creation show external stakeholders the inside of the company. The lecturers that attended the conference were: *Baruch Lev*, Professor at NYU Stern School of Business, who discussed how to turn investors' mistakes into profitable investment opportunities. Lev is regarded as one of the key accounting researches in the field and also key contributor to the development of US guidelines by SEC and FASB. SEC (U.S Securities and Exchange Commission) works to protect investors and maintain the integrity of the securities markets (www.sec.gov) while FASB (Financial Accounting Standards Board) establish and improve standards of financial accounting, reporting and guidance to users of financial information. (www.fasb.org)

The following discussion was held by *Glen Rödland*, board member in NFF, concerning the Norwegian guidelines and how to report on additional information on the value creation. *Jon Fredrik Baksaas*, CEO at Telenor, told us about their experiences of management based on non-financial factors. Finally *Harald Espedal*, administrative director at Skagen Fondene, discussed the external stakeholders' perspective. His lecture was about Shareholder value: will reporting on additional information on value creation contribute to a more correct valuation of stocks/companies? Approximately eighty persons attended that mainly represented the Norwegian business life.

The conference in Copenhagen (December, 2002), *Videnregnskaber, Ny guideline-nye muligheder*, presented Denmark's new guideline on Intellectual Capital Statements and about 350 persons were attending. The new guideline and conference is the result from the collaboration of companies, consultants, government officials, professors and researchers, co-ordinated by The Ministry of Science, Technology and Innovation. The participants in the conference were among others; *Helge Sander*, Minister of Science, Technology and Innovation and *Jan Mouritsen*, Professor at Copenhagen Business School. Mouritsen is regarded as the key European accounting researcher on the subject with strong influence on the Danish guidelines. Participants were also *Carsten Koch*, Managing Director at Danske Invest, *Søren B Henriksen*, Manager Director at Dansk Handel & Service and *Georg von Krogh*, Professor at University of St. Gallen in Schweiz. Their lectures were about the Intellectual Capital Statement, how to use it and why it is demanding et cetera. We later attended different workshops with lectures in specific subjects, for example how to understand and interpret Intellectual Capital Statements.

3.2.2 The questionnaires

We formulated a couple of *open questions* that we used as guidance at the different interviews. By open questions we mean that they were formulated to initiate a discussion where the interviewed person spoke freely and without much assistance from us. The questionnaire was used to make sure that we got the information needed. We hoped that this approach would lead the respondents to express their own opinions on the subject. We did not have any special order in which the questions should be asked, even though there was an underlying structure in the questionnaire. This type of questionnaires is so called *semi-structured*. The questions were adjusted depending on the person that we interviewed and

their area of expertise. Some of the questions were the same though. *Advantages* with interviews are that you can ask the respondent to elaborate and/or clarify his/her answer. *Disadvantages* are that interviews take time, which can be stressful for the person being interviewed and they might not have time to give you complete answers. In our interviews, the respondents took time to explain and describe their answers and we did not notice any lack of time. (Lundahl & Skärvad, 1999)

In order to use the time efficiently we e-mailed the questions to our contact in advance, who then passed them on to persons that he/she felt were best suited to answer our questions. This was positive since the respondents had some time to prepare their answers to our open and rather extensive questions. If they had not had the time to prepare, they might not be able to give us any answer at all. On the other hand this approach might have given them too much time to prepare themselves so that all form of spontaneity was lost. (Repstad, 1999)

We felt that since we interviewed six persons, with four of them from Denmark, a tape recorder might help us when processing the material from the interviews. It is always hard to manage to take notes and listen at the same time. And if the respondents speak another language it does not get any easier. The tape recorder made it possible for us to listen and concentrate on the interview and made it easier when we were going to process the material. One disadvantage with the tape recorder is that it might create a certain distance between the respondent and the interviewer. (Hansén & Thor, 1997) We noticed that the respondents reacted when they saw the tape recorder. We asked if they had any objections against us using it, neither did. After a few minutes they acted as if it was totally forgotten.

The atmosphere during the interviews could be described as friendly and open. Our impression was that the persons that we spoke with were very open, optimistic and helpful. The environment that the interviews were conducted in was either separated from the personal office spaces or in one of the person's own office. This contributed to make the respondents feel comfortable and other employees at the office did not interrupt us. The results are presented in our empirical work through storytelling.

3.3 CRITICISM OF THE SOURCES

According to Patel & Davidson (1994) it is important that you do not choose material because it supports your own ideas. This selective behaviour creates a skewed picture that does not represent the reality.

Most of the information that we have used has been collected through six interviews and the two conferences that we attended in Denmark and Norway. This means that the material is fresh and updated, but it also means that it is hard to reproduce since the information is tied to individuals at a specific moment.

The problem with interviews is that different persons interpret the answers from the respondents differently. This is depending on how the persons apprehend the situation and on their previous experiences. Because of this, it is possible that persons understand the same situation in a biased way. We hope that the fact that all three of us have been present gives us a holistic view and helps to minimise this problem. Another possible explanation to why our material might be biased is, that there is always a risk for the person conducting the interview to affect the respondent to answer in a certain way. This phenomenon is called the *interviewer*

effect. (Patel & Davidson, 1994) Other difficulties with the interviews as a method for collecting information is that the respondent's personality, commitment and ability to be present at the interview affects the result as well as the surroundings/environment in which the interview is conducted (Holme & Solvang, 1996).

It is always important that one analyses and thinks about the reasons different authors have for writing their books. One should systematically use three different approaches when studying material that is already available: *ask others*, *read articles* and *search the literature with the help of navigators* (Andersen, 1998). Since the area we are investigating is rather new and unexplored, not very much is written about it. The authors tend to influence each other and they often develop new methods or models that they want us to use. Therefore it might be more similarities than differences between the different models. We have tried to gather information from several authors in order to minimise the individual author's relative influence on our thesis.

3.4 SUMMARY OF THE CHAPTER

This chapter started with an explanation on how we decided to write a thesis on this subject and choice of research object. Our course of action was then described and we presented terms like the hermeneutic spiral and the qualitative approach that we have used. Moreover we described our information gathering via interviews, conferences and secondary data. The purpose of this chapter was to give the reader an understanding for the choices that we have made during our work.

4

THEORETICAL FRAMEWORK

The theoretical framework provides a concept discussion of terms that are fundamental in our thesis. We have chosen some authors we think will give the readers a comprehensive view of Intangible Assets and Intellectual Capital. Theories concerning learning organisations, tacit and explicit knowledge and knowledge management are discussed. The content of this chapter will be used when the collected information will be interpreted and analysed.

4.1 THE INTANGIBLE ASSETS MONITOR

Sveiby (1990) describe that all companies have a combination of three types of capital, *financial, structural and individual*. Individual capital consists of the individual's former education, acquired experiences and skills, social competence, explicitly her ability to solve the customers' problems. The purpose of the structural capitals is to create systems, routines, networks and image to make it possible for the company to handle larger volume of business in a structured manner. It is also supposed to make the company less vulnerable to losses of staff and customers. For extern participants and investors, information about its structural capital is an important factor in the valuation process of the company. These thought are related to the reporting model called the Intangible Assets Monitor. According to Sveiby (1997) the invisible part of the balance sheet with the Intangible Assets can be classified as follows:

	Market Value			
	Tangible Assets	**Intangible Assets**		
		External Structure	Internal Structure	Competence
Growth				
Innovation				
Efficiency				
Stability				

Figure 2: The Intangible Assets Monitor. Source: Sveiby (1997)

- *External structure*

  External structure consists of relationships with customers and suppliers, brand names, trademarks and reputation or image. The value of the asset is primarily influenced by how well the company solves its customers' problems. The reputations and relationships can be good or bad and often change over time and this affects the perceived value. Sveiby state that the economic value of for example a customer relation is no more "invisible" than the market value of a house. The reason why the value of a relation seems invisible today is because it does not have a generally accepted definition and that it is not measured according to any recognised standard. These negative aspects do not mean that it is impossible or unnecessary to measure the value of the relation, only that comparison between companies and over time are difficult to make.

- *Internal structure*

  Internal structure consists of a wide range of patents, concepts, models, computers and administrative systems that are created by the employees. The fact that these assets are internally created means that they generally are "owned" by the organisation and adhere to it. These assets can sometimes be acquired from elsewhere. Decisions to develop or invest in them can be made with some degree of confidence, since the work is done in-house or bought externally. Other examples of what the internal structure consists of are: the informal organisation, the internal networks, the culture or the "company spirit". The internal structure and the people together constitute what we generally call the organisation.

- *Individual competence*

  Individual competence can be described as people's capacity to act in various situations. It includes skill, education, experience, values and social skills. People are the only true agents in business; all assets and structures, whether tangible physical products or intangible relations, are the results of human action and depend ultimately on people for their continued existence. Competence cannot be owned by anyone or anything but the person who possesses it, because when all is said and done employees are voluntary members of the organisation. Arguments can however be made for including competence in the balance sheet, because it is impossible to conceive an organisation without people.

4.2 INTELLECTUAL CAPITAL

According to Stewart (1999), companies of today are operating in a so-called New Economy based on knowledge. The old industrial economy, which was dependent on machines and muscle power, has been replaced by an economy driven by something called Intellectual Capital. According to Stewart, Intellectual Capital is described as the sum of an organisation's product methods, technology, patent, competence of the employees, supplier and customer information and traditional experience. It can therefore be described as *packed useful knowledge*. This expression is recognised and widespread in use by different authors according to Olve, Roy & Wetter (1999).

Knowledge is the key success factor for comparative advantages and the main function of the organisation is to manage and stimulate the Intellectual Capital in order to create economic profit. The existence of the Intellectual Capital may be one explanation to why a company's market value is higher than what the annual report reveal.

Edvinsson & Malone (1997) defines Intellectual Capital as a more dynamic value for future earnings capabilities, based on the amount of *human and structural capital*. Edvinsson (2002) describe the human capital as the combination of knowledge, skills, innovation ability and the employees' ability to perform and to create future earnings possible.

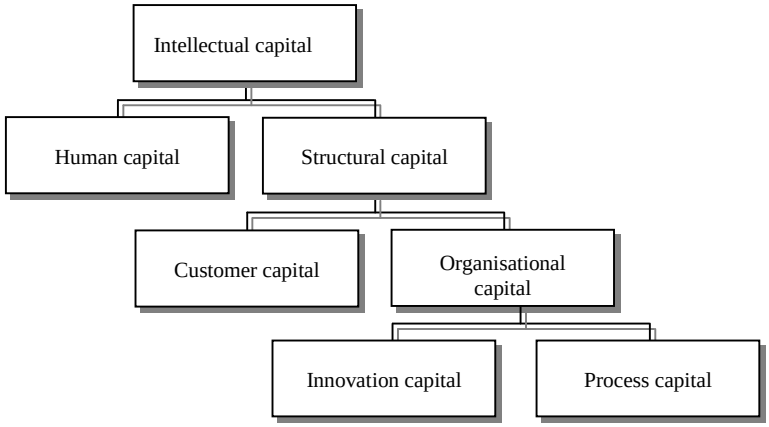

Figure 3: Intellectual Capital model. Source: *Intellectual Capital*, Edvinsson, L & Malone, M (1997)

The structural capital is defined as hardware, software, databases, patents organisational structure, brands and all other organisational factors that support and strengthen the employees in their work. The structural capital can also be explained as: everything that's left when the employees leave the office in the evening. Stewart's (1999) explanation to this definition is that the structural capital is owned by the stockholders and can be reproduced and shared with everyone in the organisation. The human capital on the other hand is not possible for the company to own. (Edvinsson & Malone, 1997)

According to Olve, Roy & Wetter (1999) Intellectual Capital in organisations can be cultivated through the increase of the human capital. This can be made by either employing the right persons or by expanding existing skills. External factors have influence on the structural capital and are for example dependent on the customers' attitude and image of the company. The important thing is to create databases of information about the customers and their interaction with the corporation. This will transform the human capital to structural capital and increase the value of the company. The influence of internal factors is about competence and knowledge. Investment in education and IT- solutions ends up as expenses in the balance sheet. When making the investment a part of structural capital, the company's market value would be higher.

4.2.1 The Navigator

Leif Edvinsson created The Navigator for Skandia (Edvinsson & Malone, 1997). The innovator named the holistic and dynamic report model, the Navigator to emphasise its

dynamic and evolutionary role. The Navigator is a business planning model that weights financial as well as non-financial values. It is also a tool for activity-based business planning and follow-up. This model helps management to translate targets into activities and is also used to implement strategies in the organisation.

The Navigator is consists of five focus areas: *financial, customer, process, human and renewal and development focus*. The Navigator can be visualised as a house:

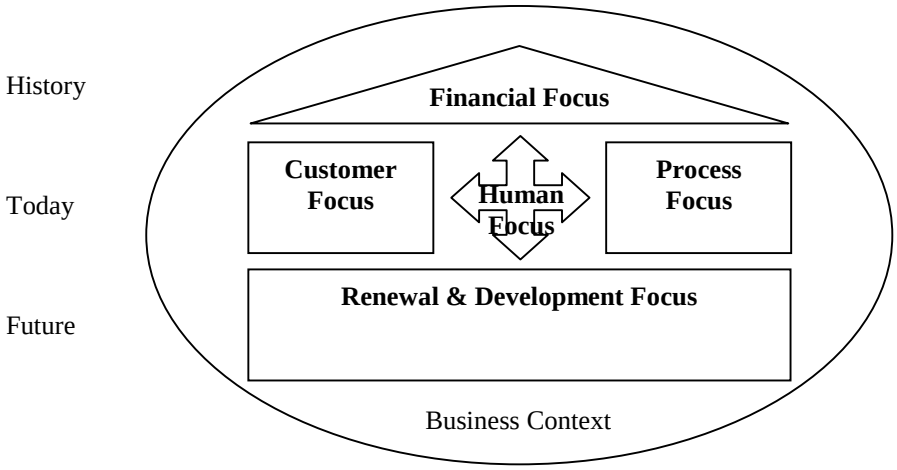

Figure 4: Skandia's Navigator. Source: *Intellectual Capital*, Edvinsson, L & Malone, M (1997)

- *Financial focus* represents the roof of the house. This focus includes traditional annual reports and concentrates on the company's history. This focus gives an exact measure of were the company was at a particular moment. When we move downwards in the figure, through the financial focus, we enter the customer and process focus, which represents the walls of house. At these stages we "enter the present" and most of the companies activities focus on today.

- *Customer focus:* most corporations of today are striving to fulfil the ambition of a total customer service. In the process of trying to reach these goals companies are applying considerable quantities of corporate resources as well as a wide range of new technological tools. To reach total customer satisfaction there are five different areas that must be considered: customer type, customer duration, customer role, customer support, and customer success.

- *Human focus* is often described as the Navigators heart and intelligence. This focus is the most dynamic and central part of the Navigator. It consists of the employee's competence and capabilities as well as the company's commitment to provide employees education frequently. To measure the human focus is probably the most difficult part of the entire model. According to Edvinsson it is more difficult to assign motivation or behaviour a value than account total revenue.

- *Process focus* deals with the role of technology as a tool for supporting the overall enterprise value creation. Applying a new technology is often hazardous. If an invention is adopted early, this may result in a decisive advantage over your competitors. But if the technology does not manage to become the standard or simply

does not work, you may find yourself behind the more conservative competitors trying to catch up.

- *Renewal and development* focus we move out of the present and try to capture the opportunities that will define the companies' future. It is on the opposite side of the financial focus.

4.3 NEW REPORTING

The book value measures the historical performance, what everybody already knows. One reason to report additionally on the Intellectual Capital in a company is that it provides new information about future implications to both external and internal interested parties. (Gu & Lev, 2001)

Sullivan (1998) makes a distinction between sophisticated and less sophisticated companies since they have different thoughts about Intellectual Capital. The sophisticated companies are aware of the importance of the Intellectual Capital and are debating about how to use reports on these assets as a means to get a competitive advantage on its competitors. Mangers that are resistant to Intellectual Capital information are more frequently found among the less sophisticated companies. They fear that this kind of information reveals sensitive and secret information to competitors. Sullivan means that their fear is unjustified since this secret information already is reported through other media. The only difference is that in an Intellectual Capital Statement packages the information into one report. Another argument for not reporting is that it is considered as a waste of money that does not guarantee any results. Sullivan's response is that to achieve improved results, one must try to present improved reports with enhanced information content.

Sullivan (1998) discusses three reasons for reporting externally on Intellectual Capital:

- *Stock price*: by releasing an Intellectual Capital supplement to the annual financial report, the capital market obtains more information and can improve their evaluation of the company.

- *Strategic positioning*: it can be easier to change the strategic direction by reporting that their Intellectual Capital and knowledge is consisted with the new strategic position.

- *Effect on the cost of capital*: by making a report for external stakeholders, knowledge intensive firms demonstrate their intellectual capabilities and reduce the uncertainty. By reducing the perceived risk, the cost of capital is reduced.

According to the author, there are three different groups that are interested in a firm's Intellectual Capital. The first is the *company* themselves where the internal focus is about measuring effectiveness of activities and outcomes of the Intellectual Capital. Internally the firm is concerned with the management and utilisation of these assets. The second group is the *participants in the capital market* like regulators, investors, accountants and legal scholars. These participants are interested in making measures of Intellectual Capital match the conventional financial information. The third interested group are *academic macro-economists and policy analysts* that are concerned with the impact that the firm's Intellectual Capital has on society.

Sullivan (1998) refers to three groups of external stakeholders that are affected by Intellectual Capital reporting. The external parties have almost solely looked at financial indicators and are used to work within an accounting framework. Therefor they might find it difficult to consider information that is not stated in financial terms.

- *Capital markets* and their investors have a long history of analysis of financial reports. They argue that all important information can be reduced into financial information and other information can be covered in brief narrative statements. The investors require methods and procedures that convert Intellectual Capital Statements into measurable indicators. According to the author, several organisations are developing methods for measuring Intangible Assets.

- *Shareholders* are expecting to have access to all relevant information about the company since they are the owners of the company. The information is the same as the actors on the capital market receive, but the Intellectual Capital information should be focused on qualitative information and how the Intangible Assets contributes to the value creation in the company's future.

- *Other stakeholders* like suppliers, vendors and collateral businesses require information about the company's long-term business and explanatory frameworks. The stakeholders' own businesses may depend on the Intellectual Capital of the company.

The external participants in the capital market continue to use traditional physical-assets models to value companies. This is independent of whether the company is knowledge intensive with less physical and fiscal assets than a manufacturing company normally has. This indicates the need for so-called reporting rules for measuring the Intellectual Capital. Analysts have relied on developing measurement tools, indicators and standards but not related to the Intangible Assets.

Sullivan states that we are years away from standardised reports on Intellectual Capital. Today's managers are trained to use the old physical-assets model also in the New Economy. Even if many companies today make serious attempts to value non-financial figures/indicators in its annual reports, the reader often cannot put the information into a context, and consequently does not yet understand them fully. The analysis is further complicated by the fact that there are no comparative figures, no sector averages and no history to look at. The author believes that it will take time before investors have learnt to use the new figures. It will also take time before companies have learnt how to work construct and present their statements properly.

Gu & Lev (2001) says that, corporate executives and managers think they take to high risks if they reveal the Intangible Assets and Intellectual Capital in their financial reports. Unlike the tangible assets, intangibles cannot be traded in organised markets and the property rights are not secured within the company. This partially explains the attitude and makes it understandable, but at the same time it makes it even more difficult to estimate the assets value properly. To convince managers and corporate executive one need to practically prove that the analytical models can be useful and not only argue for that they are needed.

4.4 MEASUREMENTS

According to Gu & Lev (2001), the traditional way to evaluate a company's performance and profitability is to use one of the measurements like ROI (return on investment), ROE (return on equity) or price-to-book ratio. One problem that arises when these measurements are applied is that Intangible Assets will not be included in the calculations. This makes it ambiguous especially in situations when making acquisitions and mergers, where the Intellectual Capital and Intangible Assets is important to evaluate.

In some European companies intellectual property rights like patents, brands or trademark are considered as Intangible Assets. They are sometimes included in the balance sheet as goodwill when it is a matter of acquisition. (Grant, 2001) IAS 38 will however now require enterprises to be explicit also on internally generated goodwill. (www.iasplus.com) One of the most important Intangible Assets is technology. The ownership plays a critical roll if the technology is company-owned or employee-owned. The distinction is very vague and the more know-how dependent the asset is, the harder it is to make an assessment (Grant, 2001).

Stewart (1999) explains that to increase growth and profit, companies must identify measure and manage Intellectual Capital. Stewart has come across some measurements that he thinks can be useful for managers. The author feels that it might be a mistake to mix measurement on Intellectual Capital with other financial information in the traditional statements. To not include them at all would be a bigger mistake and the solution would consequently be to report on the Intellectual Capital in separate reports. The measurements on the reports concerning Intangible Assets are obligated to fulfil the demand of being equivalent to financial reports. According to the author, the management must be able to estimate the results and compare them year-by-year, to appraise the development compared with the goals. Another criterion that the numbers in the reports must fulfil is that it must be possible to make comparisons between different companies.

4.4.1 Tobin's q and the Market-to-book value

The other ratio of measuring the Intellectual Capital is to use the theoretical model of James Tobin, which is called Tobin´s Q. With this model, James Tobin developed a way to predict investment decisions made of companies, without considering macroeconomic factors such as interest rates. Tobin´s Q compares the market value of an asset with how much it would cost to replace it with a new one. In the model it is described that when q is less than one, it means that an asset is worth less than the cost of replacing it. The conclusion to make is that the company will not invest any further in this asset. When q is more than one and the asset is worth more than the replacement cost, the company will continue to invest.

Stewart (1999) applies this theoretical model on his own theory of Intellectual Capital. He calls his ratio market-to-book value. According to him the Intellectual Capital is described as the difference between the market value and the book equity. The ratio gives an easy, quick and reasonable suggestion on how to value the Intellectual Capital but is most useful when it comes to benchmarking. Investors can use the market-to-book value when comparing the possible future between competitive companies.

Gu & Lev (2001) disagree and argues that this model still does not give the right estimate. The problem is that market- minus book- value is dependent on the assumption that the capital market is rational and always sets the right price. According to Grant (2001), the problem

with underestimating companies happens when Intangible Assets are not included in the valuation of the companies. This is also the reason why it exists an increasing different between the book value and the stock market value of the firm. Stewart's states that the capital market's value of a company use to be higher than the book value and the conclusion is, because the Intangible Assets are more driving and enabling values, than the tangibles that are showed in the balance sheet.

4.4.2 IC Rating

Intellectual Capital represents the value creating factors not shown in the traditional balance sheet even though it is of importance to a company's long-term profitability. IC Rating is a measurement tool that uses a broader perspective and a new approach to measure an organisation's value creating abilities. An independent rating company, Intellectual Capital Sweden AB, makes the measurements, which is based on quantifiable information from both internal and external stakeholders. The result of an IC Rating is measurements of the resources that are of critical importance for the company's long-term earning capabilities. The result can be used as groundwork for change and also as a tool in the daily activities. (www.intellectualcapital.se)

The results of an IC Rating are presented from three different perspectives:

- An evaluation of the present *efficiency* of the Intellectual Capital
- An evaluation of the company's efforts to *renew and develop* its Intellectual Capital
- An evaluation of the *risk* that the present efficiency will decrease
  (Ibid.)

The IC Rating can be used in three different ways. First, it can operate as a foundation of a modern *business control system* with measurable goals for maximising future profitability. The analysis can be repeated in order to measure and secure the goal achievement. Secondly the tool can operate as a *basis for improvement and change* in activities both on a management and an operational level. The changes that can be made identify the areas of improvement. Finally IC rating can work as a *structured image* of value creating assets for example in the market communication or within the organisation. In the organisation the instrument can create a new basis and a new language for internal aspects important to the business activities. (Ibid.)

4.5 THE BALANCED SCORECARD

Balanced Scorecard is about creating a so-called learning organisation, which make changes and expand to become successful in the future. The theory of The Balanced Scorecard was for the first time introduced by Robert S. Kaplan and David P. Norton, in an article written for the Harvard Business Reviews 1992. The purpose of the Balanced Scorecard is to measure the non-financial factors that play a significant roll in the organisation. When putting together different ways of management, according to the authors' it is possible to obtain balance in the organisation. (Olve, Roy & Wetter, 1999)

According to Kaplan & Norton the traditional financial statement only illustrates the company from a historical point of view. In the new information age, future values are created through investments in innovation, customers, suppliers, processes, technology and employees. The Balanced Scorecard provides new, more useful measurements than the traditional ones, where

analysis can be made from different perspectives and time dimensions. The authors argue that both financial and non-financial measures must be available for employees at all levels in the organisation, and should be a part of the information system. The reason for the Balanced Scorecard is that the company's mission and strategy should be translated into tangible objectives and measures. (Kaplan & Norton, 1996)

The development of the Balanced Scorecard is based on several companies need for more complete annual reports. According to Olve, Roy and Wetter, the traditional annual report is based on a short time description of the company, which always has been the dominant way to describe Swedish companies. The purpose of the Balanced Scorecard should be to use it as a complementary tool to the organisation's financial control system. In this way, the risk of only considering short time reports will be reduced. At the same time it creates an awareness of where the company is going to be in the future and how to get there.

Kaplan & Norton (1996) have developed four perspectives that are critical to consider in the Balanced Scorecard. Depending on the situation that the organisations are in and who is using the scorecard the perspective changes. To each of the four perspectives there is a question to answer.

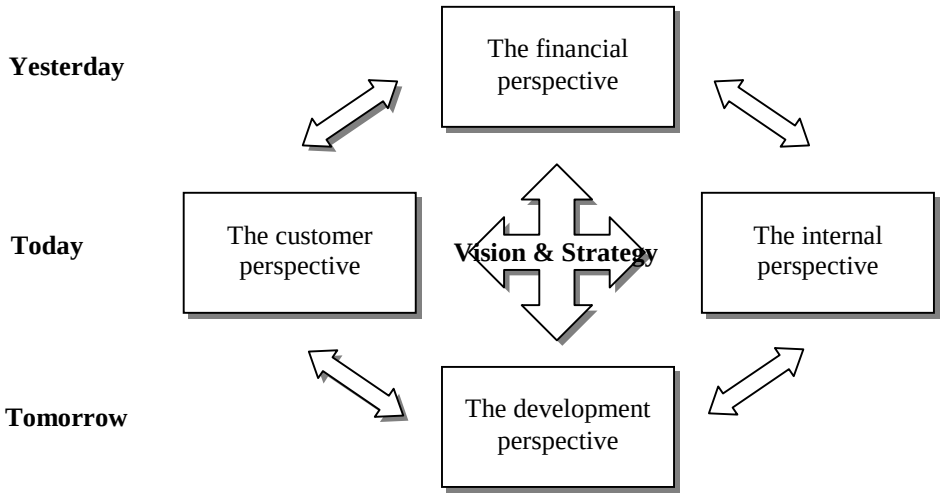

Figure 5: The Balance Scorecard. Source: *The Balanced Scorecard* Olve, Roy & Wetter (1999)

- *The financial perspective* is compared to the traditional financial statement. The measurements to use are EVA, cash flow, ROI, operating results etceteras. These measurements only indicate what have happened in the past and says noting about the present and the future. The question to answer is "how do our shareholders perceive us?"

- *The customer perspective* illustrates the interaction between the company and its customers. The measurements here include for example the rate of on-time delivery, customers' opinions and defect and failure levels. The time dimension is focused on the present situation, which can result in financial growth in the future if managed properly. The question in this perspective is "how do customers see us?"

- *The internal perspective* illustrates aspects of the present. Employee skills, quality and cost measures, productivity in processes and cycle time are examples of figures that can be enlightened. "What must we excel at?" is the critical question related to this perspective.

- *The development perspective* tries to describe the organisations' future innovations and learning possibilities. The focus is on long-term aspects and to decrease the risk of making only short-term investments. Factors to introduce are new product development cycle times, rates of improvement and competence of the employees. The question "how can we continue to improve and create value?" is the one to answer.

Olve, Roy & Wetter (1999) argue that external use of the Balanced Scorecard has several positive and negative effects for the company that is widely discussed. The main idea was to give better information to the external actors like shareholders, capital market actors and other interested parties. Equipped with this improved information the external actors should be able to make better valuations of the company and their future profit and growth possibilities. The question is how much information external interested parties can handle and understand. Another problem with the increased amount of reported information is that the company at the same time reveals information to its competitors about future competitive advantages and strategies.

One reason for not including the Balanced Scorecard in the traditional financial reports is that capital investors and shareholders own the companies. Until now, accountants only consider formal financial economic numbers and therefore the Balanced Scorecard can have problem of being considered reliable. Customer relations and employers are not included in the capital that legally needs to be controlled. This is further enhanced by the lack of any standard concerning the reporting to external parties on the scorecards. To make them understandable, the information it gives must be relatively compact and the used measurements must be, logical and possible to verify. To make them verifiable, independent inspectors with knowledge beyond the accountants of today is needed. (Olve, Roy & Wetter, 1999)

A major problem that is widely discussed is that comparisons between non-financial statements are difficult to make. There is a risk of making the companies more profitable than they really are and distortion is possible to make. (Ibid.)

The traditional way of evaluating companies by only using the financial statements like the balance sheet, does not give a complete picture of the individual company. Even if the Balanced Scorecard in some ways is inadequate, the need for a multidimensional scorecard is necessary and it is the only way to make the accounting more correct. The principal advantage of using scorecards is to change the attitudes towards the importance of "soft" values. Olve, Roy & Wetter (1999) believe that this new attitude attracts more investors; especially medium-sized investors. Small private investors may not have the time or interest in scorecard information since they only invest a smaller amount in a larger portfolios. The larger the investor is, like venture capitalist organisations, the more useful can the information proves to be.

4.6 A COMPARISON BETWEEN THE IC NAVIGATOR AND BALANCED SCORECARD

It has been suggested that the Balance Scorecard and the IC Navigator are almost the same thing. By looking at the two models it is easy to find the similarities between the statements. They both organise financial and non-financial indicators that are connected to the company's overall strategy. They go beyond the traditional financial accounting and the similar perspectives like the customer focus/customer perspective, the process focus/internal perspective etceteras.

When examining written material on the two models some differences that are not visible to the naked eye appear. The differences that exist are related to the following headlines according to Mouritsen, Torsgaard, Larsen & Bukh (2002),

- The perspective on the company
- The strategic perspective
- The organisational perspective
- The purpose of indicators

One of the most fundamental differences are that the Balance Scorecard focuses on describing the firm as a value-chain, while the IC Navigator sees the company as a extended value net that consists of heterogeneous knowledge resources and competencies. Another important difference is the divergence is the relation to the strategy. (Ibid.)

The Balance Scorecard builds on a competitive strategy since it is about choosing market position and organising the internal processes to reach this position. The market is considered to be more important than the production, which is constantly affected by the changing market conditions. The competitive advantage is based on the continuous repositioning to adjust to the customers' needs. Intellectual Capital on the other hand is more closely related to a competence-based strategy, which uses knowledge, skills and know-how to create value. Here the production potential is focused and competitiveness is based on building capabilities and competencies. The reason for the IC Navigator model to chose a competence-based strategy is that the spokesmen suggests that the competence of the company forms another basis for formulating the overall strategy than the needs of customers. (Ibid.)

When it comes to the organisational perspective both differences and similarities appear. The IC Navigator is more explicit on human capital. It is based on how to leverage that talent for future earnings capabilities, given the context of structural capital as well as external relationships. Another example is that both models centre top management but they highlight it differently. The Balance Scorecard aims at integrating the corporate strategy into every employer's work. Creating individual scorecards with indicators that are connected to the corporate strategy mainly does this. A result is that the organisation can be hierarchically co-ordinated as opposed to the laterally co-ordinated organisation, which is common for organisations using the IC Navigator. These different ways to co-ordinate the organisation also affects the role of the top managers. The Balance Scorecard managers' role can best be described as directive, and the managers with the Intellectual Capital perspective have a more cultivating role. (Ibid.)

Both models visualise and report on non-financial indicators as supplements to the traditional reporting information. The different categories in the two models are similar but not the same

and they are not assigned similar roles. They are casually related in the Balance Scorecard, while they are bundled and complementary in the IC Navigator. (Ibid.)

4.7 LEARNING ORGANISATIONS

Senge is the originator of the concept of learning organisation, 1990. The author claims that in a dynamic world with increasing independence and unpredictability an organisation must integrate thinking and acting at all levels. The first step to move into a learning organisation is called *adaptive learning*, which is about coping. But, for the organisation to become successful, it needs to apply something called *generative learning.* This is a learning process concentrated on creating with emphasis on continuous feedback and experimentation. (Senge, 2001)

The author has theories about different forms of leadership when it comes to learning organisations. The leaders are no longer charismatic decision-makers like in the traditional organisation. Instead, they are responsible for the organisation's learning abilities and they should be able to *build shared visions, bring to surface and challenge mental models* and encourage *systematic patterns of thinking*. By putting together each individual's unique vision, like pieces of a hologram, images become more lifelike and something that every employer can achieve. Initiatives and new thinking often conflict with established mental models and this is one reason why many ideas never are being used in practice. It is also important to use *system thinking* and see the holistic view. The focus should be on factors of change, patterns and trends. (Ibid.)

Olve, Roy & Wetter (1999) says that a learning organisation improves its' capabilities to react, adjust and explore internal and external changes. Hatch (2000) Theories about how organisations learn and change are a response to the post-industrial society. Economical, technological, social and cultural changes are going to reconstruct the concept of organisation structures. The New Economy is demanding flexible organisations, built on dynamic models that are easy to change and adjust depending on the situation. The theory of *the learning organisation* is a metaphor about how organisations creates internal dynamic in the learning processes, instead of adjusting according to external factors.

According to Jacobsen & Thorsvik (1998), learning is a change in behaviour. It includes both knowledge and factors of acting and is also a matter of experience. Learning on an organisational level differs a lot from learning on an individual level. The organisation is exposed to numerous triggers and involves several persons. Every person must adjust and analyse the triggers and change their behaviour all together. On the organisational level one has to consider that the process of learning is individual and differs from person to person. The model of the complete learning cycle shows that the learning is a continuous process composed of the four components visualised in the picture below. It is important that the cycle never must be broken or disrupted.

Learning can be limited or encouraged by the organisation's structure, which is the company's memory. This structure becomes the model of acting with rules, routines and procedures, which is the result of learning but is also limiting the learning. Therefore the learning must continuously develop the actions.

Learning can both be influence of and influence the organisation's culture and the chain of command structure. A strong culture within a group can limit the learning from acting.

Employees that are working as a group can develop a special way of thinking where they have the same way of considering values and norms. When exposed to triggers, there could be a negative reaction and resistance to learning. In the chain of command structure, the learning process can change the existing distribution of power and threaten individual actor's positions. Theses individuals can prevent information of triggers and limit the organisation's ability to learn.

4.7.1 Knowledge Management

According to Davenport & Prusak (2000), one of the reasons that we find knowledge valuable is that it is closer to action than data or information. Knowledge can and should be evaluated by the decisions or actions to which it leads. We can use it to make wiser decisions about competitors, customer, distribution channels, products and service lifecycles.

Knowledge is about information, thinking, understanding and experiencing etceteras. Managing knowledge concerns using knowledge in the operating processes. This will increase the company's over-all quality and growth and give them comparative advantages. (Ministeriet for Videnskab, Teknologi og Udvikling, 2002) According to Prusak & Davenport (2000), knowledge extends over time through experience, which includes what we absorb from books, experts, and mentors as well as from informal learning. Experience refers to what we have done and what has happened in the past. One of the primary benefits of experience is that it provides a historical perspective through one can view and understand new situations and events.

Unlike data and information, knowledge includes an amount of judgement. Knowledge cannot only evaluate new situations and information in light of what is already known. It compares and refines itself in response to new situations and information. Knowledge can be resembled as a living system that grows and changes as it interacts with the new environment. (Prusak & Davenport, 2000)

When discussing knowledge in an organisation, values and beliefs are two keywords. Nonaka and Takeuchi (1995) describe that knowledge unlike information is about beliefs and commitment. People assume that organisations are objective and neutral. Their purpose may be to create a product or provide a service to their customers. This ambition/goal may at first seem unrelated to the company's values. In fact values and beliefs have a powerful impact on organisational knowledge. Organisations are after all made up of people whose values and beliefs certainly influence their thoughts and actions. The organisations themselves have histories derived from people's actions and words; they also express corporate values and beliefs. Values and beliefs are essential to knowledge, determining in large what the individual sees, absorbs and concludes from an observation. People with different values see other things in the same situation and organise their knowledge by their values. (Prusak & Davenport, 2000)

4.8 TACIT AND EXPLICIT KNOWLEDGE

There are four patterns in the knowledge creating company that are interacting with each other and form a so-called *"spiral of knowledge"*, according to Nonaka & Takeuchi (1995).

He argues that knowledge is the only resource of competitive advantages in a company that will last. A company that is knowledge creative i.e. those that continuously are working with innovations and creating new knowledge are the ones that will be successful in the future.

The author describes a company as a living organism, not a machine. The employees are the most important assets in the company, and it is vital that they know the organisation's identity and mission. The employees have to understand what the company stands for, where it is going and what world it wants to live in and how to make it reality. According to Nonaka, to create new knowledge the company must able to change, including the employees. It is a never-ending process where everyone must be an entrepreneur and together make the knowledge-activity a way to live.

First, Nonaka talks about *socialisation*, which is when one person's tacit knowledge directly becomes tacit to another individual. In the socialisation pattern, the individual learns from others by observing, imitating and practising. The second pattern is to *externalise* the tacit knowledge into explicit knowledge. The knowledge can then be shared and expressed to others like team members. It is also important, in the knowledge creative process, to make existing explicit knowledge, explicit but in a different way. *Combining* information that has been collected from diverse parts of the organisation will do this. The exchange that then takes place, when the tacit and the collected explicit knowledge interact with each other, increases the company's knowledge base. The final pattern is to *internalise* explicit knowledge into tacit knowledge. This is made when the new explicit knowledge is known by the organisation as a whole, and individuals are using it to extend their own tacit knowledge. The explicit knowledge becomes tacit when it eventually is being a part of the individual know-how. This way the spiral starts all over again but according to the author, the knowledge in the company has been taken to a higher level.

Knowledge creating activities are taking place at all levels of the company and making knowledge available for others is a central issue. According to Takeuchi (1995) *explicit knowledge* can be expressed in words and numbers and shared in form of data, product specification, manuals or principles of the company. *Tacit knowledge* is highly personal and it is deeply rooted in an employee's actions and experience as well as in ideals, values or emotions. Tacit knowledge is hard to formalise and therefore it is difficult to communicate and share with others. There are two dimensions of tacit knowledge *technical* and *cognitive*. The technical dimension includes the kind of informal skills often captured in the term of *know-how*. The second dimension consists of beliefs, perceptions, ideas, values and mental models.

4.9 SUMMARY OF THE CHAPTER

We have introduced the reader to our subject by providing an overview discussion on the concepts of Intangible Assets and Intellectual Capital. The reason for starting with this was to give the reader a more nuance understanding of the concepts that are being used and the confusion that makes it difficult to discern a common language and standard.

The theoretical framework that will be used in our analysis mainly consists of theories concerning combinations of knowledge and its relation to organisations and learning.

5

EXISTING BANKING APPROACHES

The purpose of this chapter is to present how the work concerning credit approvals and investments are done in practice. We hope that this information will increase the readers understanding for the underlying motives banks have for doing their work the way they do. This material has also been important for the development of our understanding of the problem.

5.1 INTRODUCTION TO THE EVALUATION OF A COMPANY

> *"The shortcomings in the assessment processes should be considered as strong reasons for a nuanced knowledge development"* (Green, 1997, page 3).

Different external interested parties consider different things depending on what perspective and purpose they have for looking at a company. They usually have access only to public information that different authorities and the individual companies provide. Banks for example need relevant information like balance sheets, cash flow analysis and income statements to be able to evaluate and estimate the risk associated with approving a credit to a certain client. (Hansson, Arvidsson & Lindqvist, 2001)

The two purposes with the evaluation process are, according to Green (1997):

- to avoid credit losses
- to maximise the return on the banks consolidated capital

The employee's knowledge and experience as well as the participation and information sharing is of fundamental importance to a successful evaluation. His/her intuition, local awareness and presence in combination with personal chemistry, are important factors that affect the assessment process. (Svensson Kling 1999)

"A paradox is that while a close relationship creates conditions for understanding, it can also disturb the Bank Officer's ability to interpret negative information" (Svensson Kling 1999, Page 63)

5.2 RISK ASSESSMENT

Risk is a term with many definitions depending on who interprets the word. According to NUTEK (1992) *risks* are defined as; when multiple outcomes are possible and these outcomes can be identified before hand. Moreover, there should also be a possibility to estimate the probability for the different outcomes. NUTEK (1992) states that bank employees that took part in an investigation said that risk stands for a *possible loss in terms of money*. They also stated that it is easy to consider a loan as risk free if it is approved, the same goes for older engagements. *Uncertainty* on the other hand is defined as when multiple known or unknown outcomes are possible and that the probability for each outcome is unknown.

Three factors affect the decision maker's behaviour when it comes to risk according to NUTEK (1992).

- the decision maker's capacity
- the problem's properties
- the qualities of the evaluated organisation

Uncertainty can often be compensated by a premium. The competition and the assessors opinion on the potential client's situation decides weather it is possible or not to take such a premium. To overcome or limit some of the insecurity, aspects like the entrepreneur's personal qualities, motives and competence is considered, as well as the business concept, financial statements and the securities offered. (Hansson, Arvidsson & Lindqvist, 2001)
If the methods for assessing credits will get better, this will result in fewer possibilities to take premiums. The better methods, the more accurate will the judgements and the quality on the credits become. This will result in lower premiums on an average and lower transaction costs. (Green, 1997)

According to Sveiby (1990) extern participants do not take larger risks when they invest in knowledge intensive companies. The risk is different, but should not be greater. The problem, however is that the risk in these companies often appears to be higher than the risk involved in a manufacturing company with a high net worth in capital terms. The amount of Intangible Assets is invisible and their value is hard to quantify, as the relevant key indicators are not given. Even if they were, they are not yet fully understood by most readers.

5.3 INFORMATION

A fundamental problem when evaluating knowledge intensive companies is obtaining correct, current and relevant information. Knowledge about the client is one of the most important aspects in the evaluation process. The limited supply of information, which often characterises the process, means that bank employees are faced with a high degree of uncertainty. (Svensson Kling, 1999) The personal characteristics of the bank employee combined with his/her understanding of the available information also have effects on the decision-making. This is especially true if the level of uncertainty is perceived as high. (Green, 1997)

"The problem for non-experts is that information relevance is task dependent. What is relevant in one task may be irrelevant in another. Only a skilled expert can determine what is

relevant in a given situation. That is precisely why they are considered experts. Thus, the ability to evaluate the task is central to expertise". (Green, 1997, page 38)

The different forms of information can be categorised and visualised in the following manner page 54 (NUTEK, 1992)

	CONTEXTUAL INFORMATION	**COMPANY SPECIFIC INFORMATION**
SOCIAL INFORMATION	Information about trends in society	Information about persons in the company
COMMERCIAL INFORMATION	Information about business conditions in general	Information about business conditions in particular

Table 1. Information categorisation. Source: *Riskbedömning – bankers riskbedömning vid kreditgivning till nystartade företag*, NUTEK (1992)

Altman (Svensson Kling, 1999) has formulated the credit assessments' five C's that bank employees often focus their investigation around.

- Capacity – ability to pay back
- Character – willingness to pay back
- Capital – assets
- Collateral – securities
- Conditions – environmental situation

The analysis of the financial statements forms a base for different kinds of decisions and prognosis. It measures the company's strength and weaknesses regarding their ability to pay their loans, the profitability and the financial strength. Other examples of information that banks choose to investigate are: written information on prospects, management, customer stock, and product offerings. (Hansson, Arvidsson & Lindqvist, 2001)

The accessibility to certain types of information affects both the motivation to look for it and the accountability. There is a tendency that information that is easy to access is also considered to be reliable, even though this is not always the case. The choice of information sources is affected by what kind of information the bank employee hopes to find by looking at it. Bank employees find that it can be hard to find information about the current market situation, they therefore have to trust their clients and the information that they provide. Personal relations facilitate the search for information. It is not unusual that the bank employees create their own routines for how they work with the credit assessment process.

There are some difficulties related with qualitative information – a common language and guidelines for decision making is missing. Numbers are easier to communicate and distribute without distortion than verbal qualitative discussions. Qualitative information can be more

comprehensive compared to quantitative information, but it is also subjected to individual interpretation.

The latest development in the area is the use of quantitative methods supported by advanced computer-technologies like expert systems, scoring systems and neural networks (Svensson Kling, 1999).

5.4 THE CREDIT RISK ASSESSMENT PROCESS

The main question with all forms of credits is: Will the client be able to repay the credits full amount at the right time? Therefore banks investigate the potential a company has to be able to continue its payments. (Green, 1997) The credit risk assessment process in banks is more specifically related to the following questions:

- Will you grant a specific client a loan?
- What amount can you lend to the client?
- What will the terms be, what kind of safety is needed and how will the amortisation be executed? (Hansson, Arvidsson & Lindqvist, 2001)

The requirement on the bank employees' ability to interpret and gather information is increasing if a knowledge intensive company is to be evaluated. The amount of material collected, and the time spent on analysing and interpreting it is motivated by the size of the credit and an overarching risk assessment.

"Analytic thought is based on detailed defined relations between two elements at a time. Intuitive thought is based on an emotional state associated with all the elements in the field of knowledge (overall impressions)". (Bastic, Tony, 1982 Intuition- how we think and act, page 61)

The analytical thinking is characterised by the fact that you in detail can clarify your starting points, the processes that has been done and the results that followed. The possibility to give a statement on what happened makes it possible to communicate and discuss the factors that were taken under consideration with others, which results in a development of the thinking. Intuition is much harder to verbalise and is therefore also harder to communicate and develop. (Green, 1997)

Intuition is an important factor when it comes to the decision-making in the evaluation process. It contributes to a general understanding of the individual and the company's business concept etceteras. This general understanding may result in a concrete decision or a reference frame for the rest of the assessment process. It helps to decide what information to look for, where to look, how to process it and what decision that can be made from it. The following investigation can therefore be seen as a way to give legitimacy to the final decision that was originally based on intuition. When there is a lack of information or if it is inadequate or too complicated, intuition gains importance. The probability that a bank employee trust his/her intuition increases with the experience and the intimacy with the client. (Green, 1997)

5.4.1 The static and dynamic approach

According to Svensson Kling (1999) bank employees form a relatively homogenous group of individuals when it comes to agreeing on what the problematic areas of credit management are, as well as on which factors that is important to consider. The differences in credit management that existed in their investigation could be connected with the employee's way of looking at the environment. This led to the following categorisation into two extremes by the author: the *static approach* and the *dynamic approach*. (See table 2) These approaches influence the bank employee's management of information during the evaluation process.

The static approach implies that the bank employee considers the environment to be rather stable, which makes it possible to predict which firm is going to survive and which is not. Another characteristic of the employee is that he/she believes in oversimplified decision models, in which the different variables required for the assessment can be quantified and put into an overall judgement. The risk is assessed from the available information.

	STATIC APPROACH ◄——► ***DYNAMIC APPROACH***	
Starting-point	Assessment of risk	Reduction and assessment of ambiguity
Assumption regarding Business Activity	A successful business activity can be predicted since general factors exist that determine success	A successful business activity can not be predicted since general factors do not exist that determine success
Assessment Variables	General assessment variables which are valid for all firms and over time	Unique assessment variables which vary between firms and over time
Credit Management	Focusing on the initial decision and restricting the follow-up to the annual check-up	An active process where the firm is continuously followed up
Ambition	Improve the credit management through a scrupulous initial assessment	Improve the credit management through a continuous information management
Solution	Oversimplified decision models Standardized methodology Computer-based analysis of financial reports	Continuous information management Long-term credit relationships Strong networks

Table 2. The Static and dynamic approach**.** Source: *Credit intelligence in bank* Svensson Kling, (1999)

The dynamic approach on the other hand regards the environment to be highly complex and continuously changing. Because of this the initial assessment can lose its actuality quickly. Consequently, this approach leads to the conclusion that it is very difficult to make correct and reliable predictions about the firm's future. One way to handle this is to constantly have access to relevant information regarding the firm. (Svensson Kling, 1999)

The interviews and seminars that Svensson Kling (1999) based her book on pointed on the importance of business models and interaction between the bank employee and the specific firm. These observations resulted in the following integrated credit management concept. (Table 3) It is important to keep in mind that a dynamic approach implies that not only the interaction is focused up on, just like the static approach does not imply that only financial

aspects are observed. The difference between the approaches lies in that the analysis is made in different ways. (Svensson Kling, 1999)

	ORIENTATION	
APPROACH	**Financial Models**	**Interaction**
Static Approach	Stereotyped assessment of the balance sheet and the securities regarding the situation when the assessment is being made.	Striving of the optimal initial assessment of the firm manager's character. A personal guarantee creates co-operation.
Dynamic Approach	Firm-specific assessment of the income statement and the cash flow and their future development.	Striving after long-term credit relationships. A long-term relationship filled with sincerity and confidence creates co-operation.

Table 3. Integrated credit management concept. From the book: *Credit intelligence in bank*, Svensson Kling, (1999).

If the bank employee has a static approach and focuses on financial models, he/she strives to assess the risk at a bankruptcy situation. The balance sheet, the securities and their value are considered at the time of the assessment. The income statement is also considered but with the purpose of making an assessment of the progress over the last year. The consequences of this behaviour may lead to a credit management that is reactive instead of proactive. (Ibid.)

If the employee on the other hand has a dynamic approach and focuses on the financial models he/she will focus on the risk of bankruptcy. Looking at income statements and the changes in these variables in the future as well as cash flow analysis does this. Efforts are also made to assess the underlying causes that affect the income statement for example. (Ibid.)

When the static approach is combined with interaction, other factors emerge as important compared to the other approaches. This time the efforts are focused on making a correct initial assessment on the character of the manager. The underlying thought is that if the initial assessment is correct, losses will diminish. Compared to the dynamic approach in combination with interaction, the dynamic bank employee realises that a persons personality can change very fast when the environment changes. (Ibid.)

A conclusion from this can be that a bank employee that uses the dynamic approach to both the financial models and the interaction will have the opportunity to reduce information asymmetry and, as a result of this also reduce the incorrect allocations of loans. (Ibid.)

5.5 PROBLEM AREAS

The evaluation process is like all other human judging processes because they expose the individual for limits in their mind. These limitations may lead to interpretation problems and incorrect decisions. One example of these limitations is that you only search for confirming information that may result in ignorance of other important information. Too little time, the organisational culture and different compensation programs affects the search for relevant information towards a search for confirming information. Education and development of information systems can reduce the problems. (Green, 1997)

Another example of limitations is analogy thinking, which means that you use the experiences that you have from similar situations. The fact that you recognise the situation gives you a sense of security, but this may also limit your perception abilities.

The traditional organisation where internal recruitment and many years within the organisation are promoted may have been a contributing reason for the evaluation process being too one-sided and not adjusted after the current circumstances. (NUTEK, 1992)

5.6 SUMMARY OF THE CHAPTER

This chapter discussed the evaluation process of a company concerning credit and investment decisions. We hope that it has helped the reader to understand how the work is done in practice, which gives another dimension to the analysis of the guidelines for example. Topics that were discussed were risk assessment, information gathering and the static and dynamic approach.

6

NEWLY PROPOSED APPROACHES

To present as new information and theory as possible, we attended two conferences were world-leading speakers on the subject participated. One was in Oslo, Norway and the other one in Copenhagen, Denmark. This chapter is based on the material from the conferences and the newly proposed approaches of Intellectual Capital. We hope to give the reader a comprehensive view of the different guidelines and statements made. This theoretical chapter is essential for our thesis and will be interpreted in our analysis.

6.1 THE NORWEGIAN GUIDELINE ON INTELLECTUAL CAPITAL STATEMENTS

Accounting and reporting today often consists of more than what is required by law. This indicates that the traditional reporting methods are not information enough for different stakeholders. They need more information that the law requires, especially related to Intangible Assets that are not reflected in the balance sheet. NFF's ambition is to help companies (primarily those listed on the stock exchange) that want to expand their reporting with additional information to different stakeholders in a systematically and continuously manner. One objective was that by reporting on additional information increase the understanding of the importance of the Intangible Assets as value creators. (Conference, 021128)

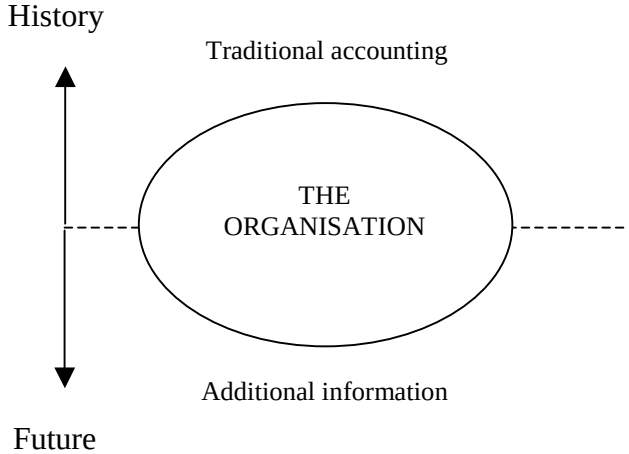

Figure 6: NFF model of the relationship between value creating indicators and traditional accounting
Source: NFF conference November 2002

The picture illustrates the relationship between traditional accounting and value creating indicators according to NFF. The traditional accounting tells the "true story", while the additional information on the value creating indicators tells us what developments to expect. (Ibid.)

The additional information may consist of both figures and text. NFF recommends that the text should be supported with numbers as much as possible. If it isn't possible to give any numbers on the different factors the text should still be there. (Ibid.)

The guidelines are a tool, a framework for how a company could choose to report and present additional information. It is voluntary to use but it should preferably be released at the same time as other reports from the company such as the annual report. The reason for this is that the usefulness increases if the reports are read together in a context.

Thoughts that have been guiding in the work with developing the guidelines are:

- It's voluntary to adopt the guidelines
- The information should be company specific and relevant
- Less is more – the additional information is no marketing campaign
- Consistency and continuity
- Possibility to make comparisons to other information and between previous years
- The true situation should be reflected objectively, both the good and the bad sides (Conference, 021128)

The focus of the process of developing the guidelines has been market oriented, and the aim was to satisfy the requests that the different stakeholders on the financial market might have. The discussion has not been focused at discussing what might be included in the different concepts like structural capital or relation capital. Instead issues like how to secure the relevance, consistency, continuity and the possibility to reach different targets have been focused. The additional information should report externally on the status and development for the target values that the company has defined as critical. (Ibid.)

6.2.1 The elements of the Intellectual Capital Statement

The work with the guidelines resulted in the following model that shows how the additional information could be visualised and reported on. The model was presented at the conference in Oslo (021128).

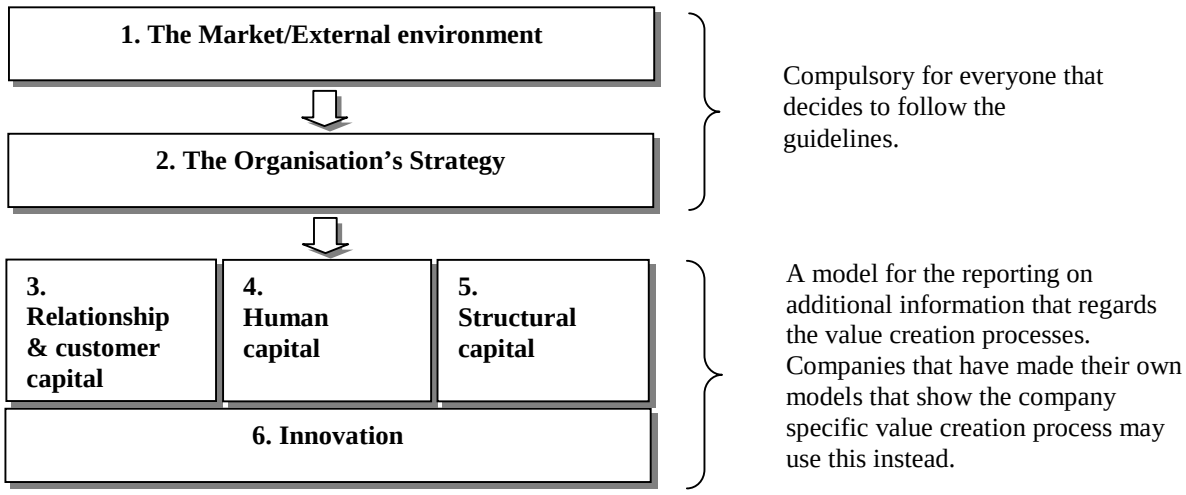

Figure 7: The Norwegian guidelines Source: *Vend selskapets innside ut* NFF (November 2002)

Examples of what can be included in the different boxes are:

1. *How does the company see its situation and the market on which it operates?* The macroeconomic situation, relevant laws and the competition is a minimum of what should be included.

2. *The company should describe how it has adjusted to its market situation and what kind of strategy they have for creating value*. Information concerning changes is very important in this section. The minimum of information required is;

    - Strategies and goals (both short and long term)
    - Organisation and management (composition and effects on the values)
    - Risk valuation (how the company sees the risk situation and how they are handling it)

3. *Relationship and customer capital is the value of all kinds of relations that the company might have*. The following subcategories should be included in the report;

    - Market position
    - Brand position
    - Relationship to its customers
    - Suppliers, distribution channels and partners
    - Image

4. *Human capital is the value of the knowledge that the employees possess*. It concerns the internal relations and relevant target parameters are;

    - Ability to absorb relevant knowledge
    - Competence transmission and improvement
    - Ability to retain important competencies
    - Management improvement
    - Incentive systems

5. *Structural capital is the value that remains in the company after five o'clock.* The value of the structural capital increases if the company has well functioning internal processes and control.

    - Status and change of the following factors should be included as well as;
    - Critical management processes/systems
    - Information from the working processes within the company
    - Intellectual property rights – IPR
    - Certifications

6. *Innovations are improvements and inventions that can be commercialised.* The following innovation categories should be addressed;

    - Product development
    - Technological innovation
    - Commercialised innovations

These six elements that represent the Norwegian model give the company a framework of how they can report on their information in an Intellectual Capital Statement.

6.2 THE DANISH GUIDELINE ON INTELLECTUAL CAPITAL STATEMENTS

The first guideline for Intellectual Capital Statements, where developed by the Danish minister of knowledge, technology and development in November 2000. The second edition was presented at a conference in Copenhagen 021202, and this new version will be published in February 2003.

The guideline in the 2000 edition was the first step from the Danish minister to develop a key to knowledge management. Denmark is one of the first countries in the world to have developed guidelines for companies, in purpose to prepare them for Intellectual Capital Statements. According to the Danish minister of knowledge, technology and development, there is an increasing interest in Intellectual Capital Statements as more companies realise the importance of knowledge management. In order to become competitive in a global market there is a need for developing knowledge resources further. An awareness of the need should communicate the knowledge and development in a comprehensible and credible manner. (www.videnskabsministeriet.dk)

Both the first and second versions are results from the collaboration of companies, consultants, government officials and researchers over several years, with the co-ordinations from the Minister for Knowledge, Technology and Development. The new guideline is a revised edition with an emphasis on a more practical approach. It is a more concrete tool compared to what was introduced in the first guidelines, with items that make the statement more precise, easy to follow and well founded. According to Helge Sander, the difference between the two versions is that trade associations together with 100 companies, both in the private and the public sector, has now tested the new guidelines. From 2000, a team of researches, led by Professor Jan Mouritsen at the Business School of Copenhagen, have put together and analysed the information of the experiences made by the different participating companies.

6.2.1 The elements of the Intellectual Capital Statement

The internal purpose of the statement is to develop a strategy for knowledge management. In the Danish model, there are four knowledge resource factors;

- *Employees*; this factor includes competence, experience, and the combination of different types of employees, motivation, commitments etcetera.

- *Customers*; relationships with customers and suppliers, their loyalties, needs, opinions of the company. The company's degree of collaboration with its customers and suppliers in product- and process development is also included.

- *Processes*; are knowledge that exists in companies' routines and procedures. Development processes, quality processes, management processes and mechanisms to handle information.

- *Technology*; this is about how the technology in the companies support other knowledge resources. Focus is on the IT-systems, -intensity, -competence, - usage and intranet.

The work with these resources shall create results in the four following elements: 1. *a knowledge narrative*, 2. *management challenges*, 3. *actions*, 4. *indicators*. It is the interaction between theses knowledge resources that creates the need of knowledge management.

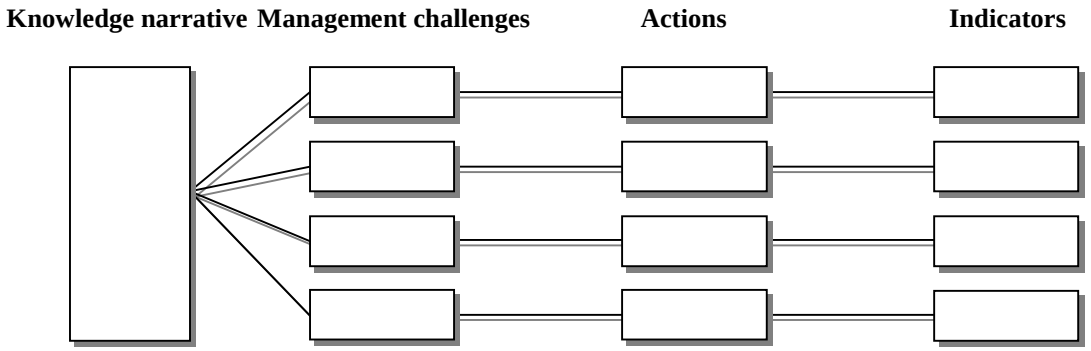

Figure 8: The Danish guidelines. Source: *Videnregnskaber Ny guidline-nye muligheder.* (Ministeriet for Videnskab, Teknologi og Udvikling ,2002)

The model shows the four elements that together analyse a company's knowledge management. The elements identify and map out the need of knowledge management. The model shows which actions that effect the knowledge management. It also provides a set of indicators that makes it possible to describe the actions precise, concrete and gives feedback. The four elements are useful when putting them together in a context.

1. *Knowledge narrative*; this element reflects the company's ambition to match their performance with the user needs. It describes how the knowledge resources are organised to achieve this goal and in what way the company's products and/or services help the user. In this way, the narrative becomes the link between the customer and the company's know-how.

2. *Management challenges*; is a set of challenges, which are identified and translated from the knowledge narrative. From the management challenges, the company should develop strategies to create user-value. The strategies should decide which knowledge resources that are profitable to develop internally in the company and which to obtain externally. The challenges are for example to strengthen the relationship with customers or identify which divisions those are in need of more expertise.

3. *Actions*; are identified to arrange the management challenges into concrete activities. They explain how to combine, acquire or develop knowledge resources. Actions are also about considering the knowledge resource's effects and extent. The purpose is to make a comparison of actions made year-by-year and therefore they are made in the short time perspective.

4. *Indicators*; are the fourth element in the model. The indicators make it possible to evaluate the actions and give feedback on their effects and results. They are separated

in *direct indicators*, like money invested in IT, and *indirect indicators*, like numbers of external consultants for developing the company.

6.3 THE INTELLECTUAL CAPITAL STATEMENT AND ITS DISPOSITION

A statement means a description of the company's chain of events. It also indicates if the organisation is operating in the right direction. This is the same regardless if it is a financial statement or an Intellectual Capital Statement. It sets numbers on activities and results and describes the collaboration between them. The Intellectual Capital Statement is focused on the development and the results that knowledge resources have contributed to. (Ministeriet for Videnskab, Teknologi og Udvikling (021202)

The Intellectual Capital Statement is both an instrument for knowledge management as explained above, and for communication. The statement describes to both internal and external interested parties how the company can create value for its customers, investors and business partners. It also indicates if the company is heading in the right direction and if it seems capable to manage and expand their knowledge resources.

For external interested parties, the Intellectual Capital Statement is making the company's Intangible Assets more visible and points out the importance of the human resources. This may result in an attraction of new employees, customers and investors. The statement can also be seen as an indicator of the company's ambition of being innovating and flexible.

The external Intellectual Capital Statement is recommended to be a separate document, but can in practice be integrated in the company's annual report. There are no formal rules or standards when it comes to creating it. One explanation is that it is considered positive to leave it up to the company to decide how to communicate its own identity and trademark. In the new guideline there are suggestions on a structure and what to include in the different chapters.

DISPOSITION OF EXTERNAL INTELLECTUAL CAPITAL STATEMENTS

A. Manage report
B. Business report
C. Knowledge narrative
D. The model of Intellectual Capital Statement
E. Management challenges incl. activities and indicators
F. Accounting policies

Figure 9: Table of contents of an Intellectual Capital Statement. Source: *Videnregnskaber, Ny guidline- nye muligheder*, Ministeriet for Videnskab, Teknologi og Udvikling (2002)

6.4 SUMMARY OF THE CHAPTER

We have given the reader the recently launched guidelines about Intellectual Capital. The materials were collected from two milestone conferences and are important information for our thesis. These guidelines from Norway and Denmark might be important contributions to the emerging standards.

7

EMPIRICAL RESULTS

The following chapter is a statement of the information that we have collected empirically during our work. Material from the different interviews will be accounted for, as well as material from the conferences that we attended in Oslo, Norway and Copenhagen, Denmark. The interviews will be structured as a narrative, since we think that this will facilitate the reading and clarify the context. The opposite alternative would be to account for each question individually, which we think easily can be very static.

7.1 DENMARK'S NEW GUIDELINES ABOUT INTELLECTUAL CAPITAL STATEMENTS

Jan Mouritsen, Professor at Copenhagen Business School presented the new guidelines of Intellectual Capital Statements at the conference in Copenhagen December the 2nd, 2002.

He began his presentation with clarifying that Intellectual Capital shall be observed as a company's knowledge management. The statement identifies the company's strategy for knowledge management, explicitly the firm's goals, result, and knowledge. Intellectual Capital shall be used to develop knowledge resources and communicate a strategy to the company and its world around.

Comparing to the old guideline, the new ones is compiled in a more practical manner. It also considers if the company is small, large, private or public and which branch it is establish in. Companies in the public sector have had the largest problems with reporting on the Intellectual Capital. The new guideline can help them with this.

Another difference between the old and new guidelines is that the renewed version focuses more on development, process development, customer satisfaction and technological improvement. The new guidelines main contribution is that it establishes a related thought about the corporation's knowledge management and can be used both internal as well as external.

Three arguments to why firms shall use Intellectual Capital Statements in their reporting are:

- To create a systematically management of the company's Intellectual Capital, which is a volatile resource.
- To present how the firm develops its knowledge resources.
- To attract customers, employees and other resources.

7.2 How to analyse a statement on Intellectual Capital

Professor Per Nikolaj Bukh from Aarhus Business School (Conference, 021202) explained that there are three important factors/indicators that external stakeholders have to consider when they evaluate a company's financial accounting. The three factors are:

- Solidity
- Investments
- Earning Capacity

According to him there is one disadvantage with the financial accounting though. It usually does not say much about the company's future, which every stakeholder is interested in knowing more about. The Intellectual Capital Statement on the other hand provides the evaluator with information and indicators about the future of the company in a systematic way. It is therefore important to consider statements like these in the evaluation process. There are a few important issues, presented below, that external stakeholders have to analyse on a deeper level to accomplish a correct evaluation.

- How are the company's knowledge resources related?
- What has the company accomplished to strengthen the collective knowledge?
- What are the effects of working with knowledge?

In addition to the answers to these three questions, external stakeholders have to consider three essential indicators when they evaluate the firm's Intellectual Capital (Bukh & Moritsen, Conference, 021202). The three indicators are: effect figures, activity figures and finally resource figures. *Effect figures* can for example explain if the productivity is high or low and what the quality is like in the corporation. These figures describe the collected effects and development of knowledge resources. *Activity figures* can incorporate information about the development of processes, meeting with customers and education. The purpose of the activity figures is to improve the company's overall quality. *Resource figures* can be described as a portfolio of the firm's knowledge resources. This portfolio includes the technological platform and the distribution of education. It is important that the company give a definition of what they mean with the different activity, resource and effect figures, and how they relate to the value creation in the company and to its customers and investors.

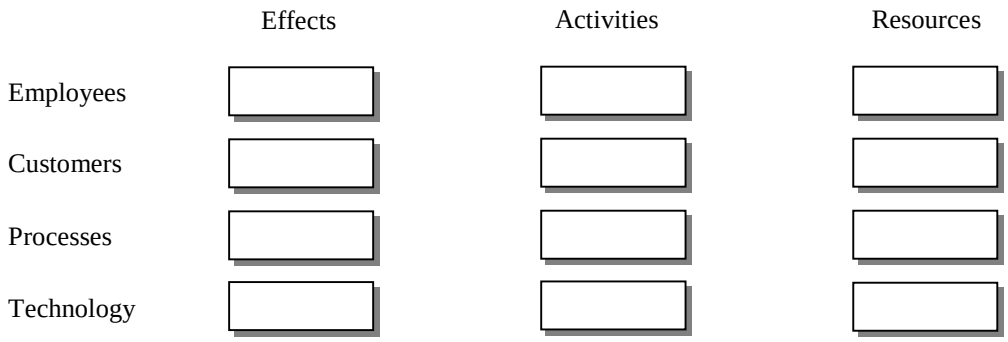

Figure 10: Analysis model of the Intellectual Capital Statement.
Source: Conference in Denmark (021202)

7.3 DANSKE INVEST

Danske Invest is Denmark's largest unit trust group and is owned by 175000 unit holders. They invest the unit holders' money in different portfolios that consists of stocks and bonds. The portfolios are differentiated in order to offer the unit holders investment alternatives depending on their willingness to take risks. Danske Invest Administration A/S is an administrative association that uses an Intellectual Capital Statement both internally and externally.

At the conference in Copenhagen Carsten Koch, Managing Director at Danske Invest described how they as investors were in need of information that describe future earning possibilities and information about risks related to the company. Consequently they were using Intellectual Capital Statements in their evaluation of companies of interest.

According to Koch, there are several reasons why there is a growing demand to report Intellectual Capital Statements. The trend is that more and more of the world's largest organisations report non-financial information to its stakeholders because of an increasing interest from both investors and the public to study this information. Another contributing factor is the new version of the Danish law concerning the content in annual reports. It is now stated that companies are obligated to describe their knowledge resources if they are important for future profits. Benefits with reporting on this information are also a motivating factor. Examples of what the statement signals are: openness, responsibility taking and integrity both in the organisation and the management.

In the interview (021218) with Koch at Danske Invest's office in Copenhagen, he stated that financial reports will always be the most important source of information to them. In the trust group it is important to make investments in companies that are telling something about future earning potentials and not only provides historical financial information. Unfortunately there are inadequate numbers of companies that are reporting on their Intellectual Capital. This is especially true among unlisted companies (Conference, 021202). Possible reasons for today's lack of interest in making Intellectual Capital Statements can probably be related to the fact that the concept of Intellectual Capital is rather new. Another contributing factor is that Denmark has several small companies that may not have the same need for knowledge management and Intellectual Capital Statements as larger corporations. Danske Invest does not directly require individual companies to develop statements of their own, but they support the ideas behind the new Danish guidelines. Koch believes that the utilisation will increase in the future because of the demand for more information on long-term strategic ideas about the development, knowledge management and activities in companies. Knowledge is of great importance in every organisation and the reporting on knowledge assets is therefore not likely to be just a trend. The evaluation models that are in use today are very general which consequently makes it harder to evaluate knowledge intensive companies. Koch thinks that reports on non-financial information can contribute to more fair assessments in the future. (Interview, 021218)

7.3.1 Danske Invest Administration A/S's Intellectual Capital Statement

Koch was introduced to the concept of Intellectual Capital through one of Danske Invest's employees. The employee had studied management at Copenhagen Business School and had written a paper about Intellectual Capital (Interview, 021218).

Koch found the concept of great interest for the work in Danske Invest. The Intellectual Capital Statement is now a part of the communication strategy and the report is to ensure that the unit holders' money is invested rationally (Conference, 021218). Danske Invest believe that they have an obligation to provide as much information as possible to their members, both financial and non-financial. They make investments on behalf of their unit holders and therefore their knowledge about the portfolio companies must continuously be updated, as well as their ability to interpret new information. The long-term investments that they make mean that information to the members about how well knowledge orientated the company is and explanations about plans for the future are essential to establish trust between them and their unit holders. (Interview, 021218)

Danske Invest Administration's Intellectual Capital is based on the Danish guidelines. The statement was created on an own initiative and is primarily made for an external use. All eight departments in Danske Invest were represented and participated in the development process. During their work they tried to see the statement through the eyes of the unit holders and their information need. This was done in order to make sure that only relevant information to the external stakeholders was included in the statement. We asked if they had used the Balanced Scorecard concept in the organisation since it shares similarities with the Intellectual Capital. Koch said that Balance Scorecard had not been used in Danske Invest, but he agrees that it exist several similarities between the two models concerning the information that they report on. (Interview, 021218)

The major problem when developing the statement was that a lot of resources was needed, both time and employees. Another problem with external reports is that not everyone's knowledge can be mentioned according to Koch. This could mean that employees in the accounting division for example are not as meaningful to report on externally as information focused on Danske Invest's investment policies. This does not mean that these employees are any less meaningful to the organisation and its value creation. It is just a reflection on the different information needs that different stakeholders might have. Positive effects of the Intellectual Capital Statement are that the company has to think about what they actually do to create value and how to present this information to their stakeholders. (Ibid.)

The content of the statement can vary between the years, but Koch means that there is a need for stringency though. One part of the statement should give information on areas of interest that stay the same like for example activities, employees and strategy. The other part could be more continuously changed. In this section different problems and goals can be addressed. One important thing is that it is possible to make comparisons between different years. Therefore descriptions of how the indicators were constructed are of great importance. (Ibid.)

According to the interview (021218), the analysis of an Intellectual Capital Statement will require new knowledge and competencies from both investors and other external stakeholders, maybe not today, but in the future when standards are developed. When Danske Invest was creating their own Intellectual Capital Statement, the investors were at the same time learning how to read and analyse others statements. This is an important advantage according to Koch.

Koch thinks that the Intellectual Capital Statement has a promising future, even if Danske Invest are in the first stages. In their development of a second statement they will focus on linking strategy, vision and values closer together. The next Intellectual Capital Statement for Danske Invest will probably take as much resources and time as the first one. The reason for

this is that every report needs to consider if new indications should be used or if the old ones are sufficient (Interview, 021218). Since the statement is used as a communication tool they will continue to focus on the unit holder's information need and try to make it more readable with the help of words instead of figures. This approach is called storytelling. (Conference, 021202)

Departments in Danske Bank have been notified about the existence of Intellectual Capital Statements and have been given comments about the one made by Danske Invest Administration A/S. Koch means that even though Danske Bank is a more traditional organisation, they all need the same non-financial information. (Interview, 021218)

7.3.2 Thoughts about Intellectual Capital Statement

The Intellectual Capital Statement has the purpose to provide a so-called holistic view of the company. Its purpose is to present useful non-financial information that the financial annual report does not focus on. Koch thinks that the Intellectual Capital Statement can prevent future financial scandals, because the information that the Intellectual Capital Statements provides makes it harder to fiddle. (Conference, 021202)

Koch says that the content in an Intellectual Capital Statement is a mixture between text and figures. It describes the problems that need to bee solved and how to do this. One should be able to compare indicators year by year and see the changes. For example, if the personnel turnover is five percent today and was three percent last year, the text must explain why the numbers have changed in this way. The organisations' management must also explain if this development is considered as positive or negative. It is important to clarify what the indicators stand for and how they are calculated, as well as to motivate actions taken. Today, many figures are ambiguous and in need of an explanation. Koch means that the statement informs, and creates a sense of the managers' competencies and skills to the external stakeholders. He also thinks that this information source may reduce the risk associated with the company's uncertain future. (Interview, 021218)

Koch points out both in the interview and at the conference, the importance of standards or norms for reporting non-financial information. It is impossible to make comparisons between companies for example in the same line of business without it. He says that the Intellectual Capital Statements today are mainly window dressing; they are too optimistic, too subjective and work as an advertisement. This makes them very hard to analyse and investors are not interested in considering them until the imperfections are minimised. Non-financial reports today are not specified and one does not know in advance what information that can be obtained from them. Standards are needed and the statements must be more practical and systematic to use (Conference, 021202).

Koch realise that difficulties will arise when creating a standard, because every organisation is unique and have different knowledge focus on their core competencies. He believes that some authority must develop a standard; otherwise the information will continue to be unregulated and anarchistic. International standards will take very long time to create, according to Koch, but attempts made by the Ministry of Knowledge, Technology and Development in Denmark and international groups are positive signs though. (Interview, 021218)

7.4 DANSKE BANK

In the Scandinavian financial markets, Danske Bank plays a leading roll as the largest bank in Denmark. The bank is operating in a global network and is a part of the Danske Bank Group. This group offers a wide range of financial services like mortgage finance, insurance, real estate, and asset management et cetera. Danske Bank group encompasses for example Danske Bank, BG Bank and Realkredit Danmark. (www.danskebank.dk)

Danske Bank has an old history with its origin back in 1871. Today's bank is a result from a merger in 1990, between Den Danske Bank af 1871, Københavns Handelsbank and Provinsbanken. Danske Bank Group serves a significant number of customers in the public, corporate and institutional sector and has almost three million retail customers in Denmark, Sweden and Norway. (Ibid.)

Danske Bank is operating under the name of Östgöta Enskilda Bank and its local banks in the Swedish provinces, while in Norway, the bank operates under the name of Fokus Bank. (Ibid.)

From the interviews made at Danske Bank's Credit Department we learned that they consider Danske Bank to be structured and organised as a typical centralised and hierarchical organisation. Despite the centralisation their customers see them as a bank with quick response rates and fast decision-making process.

7.4.1 Danske Bank's evaluation process (Interview, 021126)

The persons interviewed at the Credit Department explain that Danske Bank has been using a rating model since 1997. The classification systems use grades from one to ten. A company with the grade one is acknowledged as a strong and stabile company. The grade ten indicates that the corporation has very high debts. According to the persons interviewed it provides a good reference frame for the decision-making (Interview, 021126). The grades are based on an analysis of the company's creditworthiness. The rating model uses the same classifications on all companies, small as well as large. The purpose of the model is to identify and avoid customers with large financial problems. In general The Credit Department evaluates their customers at least once a year just to make sure that they still have a satisfying economy. If they find that their customers are beginning to have negative cash flows or negative profit, the companies must report on their balance sheet every month or every six months, depending on how negative the results are.

When evaluating a company it is also considered what line of business the company is established in. Facility companies are not evaluated in the same way as other companies though. It would be unjust since facility companies have higher liquidity and is characterised as stabile. The persons interviewed at the Credit Department state that Danske Bank is, and has always been a rather conservative bank. Consequently they did not invest as much as others in Dot.coms and therefore did not loose as much money as other banks when the IT sector started to decline.

The persons interviewed at the Credit Department also explains that the interest rate in part dependent on the company's grade in the rating process. A company that belongs to the category four will receive a loan with a higher interest rate, than a company belonging to class two. The interest rate is also depending on which type of loan the company demands. Short-

term loans with a payback period of five years are less expensive than long-term loans with a payback period of 20 years. The interest rate in Danske Bank is always related to the risk premium and is not affected by other bank's credit rating and interest offerings. In recessions Danske Bank is more conscious about approving loans than in a boom.

Skånes Provinsbank, which is a part of Östgöta Enskilda Bank, in Sweden and Fokus Bank in Norway, use the same rating model as Danske Bank in Denmark. Decision-making about credits concerning small and medium-sized companies, are permitted at the local offices within certain limits. Regarding large sized companies and larger loans, Danske Bank in Copenhagen makes the final decision.

When evaluating a company, initially the financial key factors are considered. According to the interview (021126), the persons interviewed at the Credit Department do not see any problem in their current evaluation processes of companies. They base their decisions on financial information, even if the figures represent historical facts. The financial information is at most three months old and financial values can describe the company's past as well as the future. By comparing the company's last three or four annual reports one can see a specific pattern. In an early stage in the process, the Credit Department can therefore come to a correct conclusion and avoid companies at the edge of bankruptcy.

This is not all information that is considered. Also non-financial information especially related to the customer and his/her company is considered. The reason for this is that it is always important that the decisions are based on trust. If the bank does not trust the customer it will not grant the credit, no matter how good the financial figures seems to be.

7.4.2 Non-financial information

Even if Danske Bank considers financial information as the most important one, they also consider non-financial information like the company's R&D, management, employees' knowledge and skills. This information is assembled during meetings at the clients company and from the Internet. Concerning R&D it is observed how many products the company is developing and the competitors and their products are investigated as well. They also try to estimate how the market could respond to new products.

7.4.3 Thoughts about Intellectual Capital Statements

The persons interviewed at the Credit Department classify the Intellectual Capital Statements as a management tool. It can help the company attract new employees and create awareness for the knowledge in the organisation. They believe that it will take time to develop a common standard for how to put a value on a non-financial asset.

They do not use any version of the guidelines and have only been reading about them. Their opinion on the first version of the guidelines was that it was written in a theoretical manner and that it was difficult to put into a context. They feel that the new guideline is more practical and well matched for the needs of the external stakeholders in for example the banking sector. This version will probably be used in the future. The reason behind this opinion is that the new law about annual reports that will take effect in the beginning of 2003 states that companies must report on knowledge resources that are important for the value creation in the company.

7.5 SKÅNES PROVINSBANK

Skånes Provinsbank in Malmö is a part of Danske Bank's organisation in Sweden. In 1994 Skånes Provinsbank was established as an approach to expand the market share in Sweden. Like the rest of Sweden, large banks had dominated the financial market of Skåne for a long time. Danske Bank's strategy on the Swedish market was based on the growing demand in independent and more local banks with closeness to its customers and local knowledge. (www.oeb.se)

With the resources from the largest bank in Denmark, Skånes Provinsbank has capabilities to be competitive on both smaller and larger customers. Danske Bank and Skånes Provinsbank are collaborating, but the Swedish bank can make independent decision on credits within certain limits. Only large credits need approval from other higher authority levels in the Swedish organisation or from Danske Bank in Copenhagen. (Interview, 021218)

According to the interview (021218) with Skånes Provinsbank, risks are something that investors and company owners have to take, but that the banks' credit department should avoid. When making credit assessments, the bank considers financial information and are analysing the company's overall situation. The non-financial information that is considered is for example related to the individual client, management and customers. Internet is an information source that complements other traditional reports. Visits at the company in its' own environment are also important to obtain a comprehensive view of the client. All information that can be gathered this way is important when trying to forecast the company's future.

In a traditional organisation with a hierarchical structure and several decision levels, close customer relations between the bank and the client are of great importance. The bank is "*living with the company"* and credit assessments are done continuously, depending on changes that affect the company's situation. These changes can both be internal, like investments, and external, like market changes. According to Skånes Provinsbank, the personal and close relationship is the best way to ensure an access to relevant and timely information. The employees' skills and knowledge is developed by attending several internal courses and through the practical work in the bank. The employees are always working in pairs and it is not unusual that a new employee works with a more experienced mentor. Knowledge is also available through the collaboration with Danske Bank.

Skånes Provinsbank never finances research and development companies. These companies have no profits and negative cash flow and are therefore in need of capital investors. R&D companies should instead be financed by venture capitalists and investors like for example Danske Invest. Knowledge companies like consultant- or IT companies are consistent with operating profits and are possible customers to the bank.

7.6 Intellectual Capital from an analyst's point of view

Jens Houe Thomsen who is a Senior Portfolio Manager at Bank Invest, described the analyst's attitudes regarding the Danish guidelines at the conference (021202).

From the beginning when the first guideline was established the analysts were critical. The reasons for this were that they did not know how to use it and how to understand and evaluate companies according to it. They also thought that it was to abstract and not user-friendly. Consequently they have demanded a standard or dominant design that would make the statements easier and more useful. According to Jens Houe Thomsen the financial sector have a positive attitude towards the new guidelines and they are ready to implement it in their evaluation processes.

When an analyst evaluates a company there is a paradox related to how they require information. They demand all the information they can get but at the same time not all information is relevant for their evaluation. Analysts emphasise that it is the holistic view that is important, where the amount of details is meaningful. Therefore they have to reduce information that is not important.

When they evaluate a company they consider if there is a continuity and consistency in the information that the company provides. Next, they observe the quality of the information. After that they examine if the information has an operational character and is reliable. Finally, they make sure that the company's information fulfils the requirements made by the law and government systems.

The purpose of the annual report is to give information about the company's financial position, profit and changes in the financial situation. These details are important for investors in their decision-making. Annual reports that are evaluated in the way as presented above, fulfil most investors' general needs. But the financial statement does not present all information that is important for the users in order to make accurate decisions. The reason for this is that annual reports primarily reflect the economic results of earlier events and does not necessarily reflect non-financial information that is aimed at describing the future.

7.7 Opinions from an external stakeholder – Skagen Fondene

Skagen Fondene is an option administrator on the Norwegian market. Their products are composed to cover both short and long-term savings needs. The company has a strong global orientation since the founders had experiences from the international stock exchanges. At the conference in Oslo (021128) Harald Espedal from Skagen Fondene expressed their opinions concerning reports like the Intellectual Capital Statement. According to him the reporting on additional information is a tool for increased understanding of Intangible Assets in a company. It gives the investor valuable insights in the company and its value creating processes. Investors are always interested in information that is relevant, complete, consistent and accurate. Today investors feel that the traditional accounting information is not enough and that the additional information that is provided lacks stringency and is in many cases more of a commercial brochure than an information tool.

Additional reporting does not change the fact that an investor primarily looks at the financial reports but they give investors valuable indications so that they more easily can get an opinion

about the future of the company. Other stakeholders might prioritise additional information more than financial reports. The new information is only interesting if it provides indications about the future. The historic information is interesting in the sense that it might help investors predict bankruptcies.

There are still some problems that have to be dealt with concerning the new accounting. There is no commonly accepted terminology for Intangible Assets, and it is difficult to decide what indicators to look at and what their values will be. They hope that in a couple of years an industry specific standard will be adopted, and that companies will establish a dialog with the investors so that the information asymmetries can be overcome.

7.8 SUMMARY OF THE CHAPTER

There is a growing demand to report on an organisation's Intellectual Capital. The trend is that there is an increasing interest from both investors and the public. More and more of the world's largest organisations are reporting non-financial information. The primary advantages to report on non-financial assets are that it gives signals about an openness, responsibility taking and integrity in the organisation and from the management. By presenting how the firm develops its knowledge resources they hope among other things to attract new customers, employees and other resources.

In this chapter we also learned that there are several reasons why bankers do not consider Intellectual Capital Statements when evaluating companies. These reasons will be focused on, explained and analysed in the next chapter.

8

ANALYSIS

This chapter presents our interpretation from the analysis of the material with the assistance from the theories presented in the theoretical framework. The material is presented according to the list of arguments that was constructed in the previous chapter. Each argument is discussed and analysed in two categories, banks and investors. Furthermore a comparison is made between the Norwegian and Danish guidelines.

8.1 Our analysis and interpretations

When we started our work with this thesis we assumed that banks, as external stakeholders, did not take much interest in non-financial information. We thought that except for the financial information, bank employees only looked at the client's characteristics and his/her previous engagement with the bank. During our preliminary investigation we soon learned that the bank employee considered more non-financial information than we first expected. According to our interviews they searched for as much information as possible, both financial and non-financial. Examples of non-financial factors that they considered were what kind of products the company produced, their market situation, management qualities, number of customers, and the company's dependence of them. There seemed to be an information need that the traditional reports did not cover and the employees therefore created their own evaluation processes. Hansson (2001) has discussed this as well as Green (1997) amongst others.

8.2 Reasons for not looking at Intellectual Capital Statements

It turned out that there could be numerous explanations to why external stakeholders did not look at non-financial information in a systematic way. Below is a table of the explanations that surfaced in our empirical study. The material is extended with a classification into two categories: banks and investors. In the bank category, interviews from Danske Bank and Skånes Provinsbank are included. In the investor category material from Danske Invest, Bank Invest and Skagen Fondene is represented.

REASONS FOR NOT LOOKING AT INTELLECTUAL CAPITAL STATEMENTS	**BANKS** (Danske Bank and Skånes Provinsbank)	**INVESTORS** (Danske Invest, Bank Invest and Skagen Fondene)
1. There is a lack of a standard and no commonly accepted terminology	X	X
2. It is almost impossible to make comparisons between different years and between different companies	X	
3. There is a sense of ignorance for new learning	X	X
4. There is a lack of knowledge on how to interpret the statements	X	
5. They are not functional in their present shape and there is a lack of stringency	X	X
6. They do not see the benefits with the statements	X	
7. Too few companies report Intellectual Capital Statements	X	X
8. The financial statements are the ones that are the most important for the decision-making	X	X
9. The organisation's learning	X	
10. It is too time and resource demanding	X	X

Table 4. The reasons our respondents had for not looking at Intellectual Capital Statements.

With this table we want to clarify the different arguments that the two categories have for not looking at Intellectual Capital Statements. We also wanted to see if some kind of pattern would emerge by categorising the answers. The following text will elaborate on the answers more thoroughly.

8.2.1 There is a lack of a standard and no commonly accepted terminology

The New Economy is said to affect the information needs of different stakeholders both external as well as internal. The information external stakeholders request is often related to non-financial information. This results in a need of standardised reporting and evaluation models as well as a common language. Different attempts have been made from both companies, like Skandia that created the *Navigator*, authors like, Sveiby who created the *Intangible Assets Monitor*, Kaplan and Norton's *Balance Scorecard* and Intellectual Capital's *IC Rating*. These models discuss and give suggestions on how to visualise and present the Intangible Assets in an organisation. The utilisation of these models has primarily been for internal uses. This may be because companies are afraid for so called transparency, which means to expose sensitive information to external stakeholders like their competitors, a thought that is supported by Sullivan (1998).

When we asked why the banks do not look at non-financial information in a systematic way, the answer often related to the fact that no accepted standard or analysis models exist. This is a valid point, but since the Danish Ministry of Knowledge, Technology and Development

published their statement this is no longer entirely true. They have developed guidelines for the reporting on Intellectual Capital in organisations, and 100 different companies have contributes to the evaluation of these guidelines. In the publication models are available as well as questions that can help when evaluating a statement. If this material is considered to be inadequate, it can be useful as a source of inspiration if the banks would like to develop their own models. However, this does not seem to be the case. Instead banks tend to wait for some organisation to develop or approve a standard that they can adopt and adjust.

Something that is important to point out is that when the banks talk about a standard they often relate to the indicators in the Intellectual Capital Statements. The information in writing is something that they often seem to neglect. A possible explanation to this behaviour is that bank employees are used to analyse figures, not text to the same extent.

8.2.2 It is almost impossible to make comparisons

According to Hansson, Arvidsson & Lindqvist (2001) different external stakeholders look at different things depending on what perspective and purpose they have for evaluating a company. We investigated the Credit Department at Danske Bank, the business department at Skånes Provinsbank and an investor representative from Danske Invest. We thought that they would look at similar information in their evaluation processes, an opinion that turned out to be shared by Koch at Danske Invest.

From the interviews we however learned that there seems to be differences in what kind of material the departments seem to focus on in their analysis. To investors it is very important that they are able to make comparisons between different companies and over the years. This is not very easy since there is a lack of standard and no common indicators. It is therefore very important that the companies explain how they have calculated their indicators. As a result the guidelines will only be an additional information source in the investors' evaluation process, until standards and measurements have been created. The creditors on the other hand concluded that the guidelines are of minimal use to them today since they are more interested in studying financial information to make sure that the bank will get its money back. If they need non-financial information they study their own registers and consider their relation to the client.

8.2.3 There is a sense of ignorance for new learning

Theories about learning organisations state that new thinking often is in conflict with established mental models. When exposed to triggers, a reluctance to learn can be the negative response from the employees. This might be one reason why some new ideas are never being used in practice, and why banks question the usefulness of the concept of the Intellectual Capital Statement.

During our interviews we learned that the employees consider the bank to be a traditional, hierarchical and centralised organisation but there is a tendency to give local offices more responsibility. Theories about learning organisations explain that the organisation's structure sometimes can have constraining effects on the learning process. According to different authors, the concept of the New Economy is demanding flexible organisations that easily can adjust to changes. Our opinion regarding organisations with a centralised and hierarchical structure is that they tend not to be very dynamic. Danske Bank for example is operating with the assistance from rules and policy statements, like their credit policy and rating model that

is used on small as well as large sized companies. These assisting tools regulate work routines, like the evaluation process, in the bank and results in a particular behaviour. We believe that this constrained behaviour is reinforced by the traditional and hierarchical organisational structure. This consequently leads to an organisation that is cautious when it comes to adopting new ideas that have not been properly tested. It may also be reluctant to develop new ways of thinking. The result, in our opinion, is an organisation that experience limited learning.

Banks often are organisations with a long history and tradition. This also affects their perception of the world. Knowledge management theories emphasise that peoples' values and believes influence thoughts and actions in organisations. Employees are easily affected by the traditions, culture and procedures that have been developed over the years in this type of organisation. This is also true for the evaluation processes and the decision-making within the organisation. An argument could be made that the historical luggage and the centralised organisation prevents developments in certain areas, like the evaluation process. (NUTEK, 1992) We believe that especially these kinds of organisations must be aware of the importance of new impulses, development and innovations, not to become more static, uniform and obsolete.

Svensson Kling (1999) discussed two different approaches from the bank employees in the evaluation process: *the static* and *the dynamic approach.* It is easy to place bank policy in the static approach, which stipulates that the starting point of the analysis is the risk assessment, followed by a thorough initial assessment. The environment is considered to be rather stable and it is possible to predict if the business activity will be successful. In this category a standardised methodology is the solution in combination with computer-based analysis of financial reports. Some of these characteristics are applicable on some of the employees' evaluation processes, but some are not. Instead we found out that the division into these two extremes does not seem as relevant since new approaches are being emphasised. One example of this is the importance of the relationship with the client. Long-term relations are promoted, which strengthen the bank's network and ties the clients closer to them. Another effect that is positive on the evaluation process is that close relationships facilitate a continuos information management. All these benefits are found in the category that Svensson Kling defines as the dynamic approach. One difference that we find important between the two approaches is related to the assessment variables. The static approach has general assessment variables, which are valid for all firms at all times. The dynamic approach on the other hand uses unique variables, which vary between firms and over time. So far our investigation indicates that the credit department falls under the static approach.

Altman (Svensson et al, 1999) has formulated the credit assessments' five C's that bank employees often focus their investigation around. The five C's are stated below.

- Capacity – ability to pay back
- Character – willingness to pay back
- Capital – assets
- Collateral – securities
- Conditions – environmental situation

The *capacity* describes the company's ability to pay back a loan. The information to decide on this is can usually be found in the traditional financial statements, and in the banks private files on the client. The C that stands for *capital*, however limited to financial capital and

traditional accounting that can be assessed through financial statements. *Collateral* or securities may be reported on in the financial statements, but it is not unusual that the bank employee visits the company to inspect and get an understanding on how to evaluate them. The *character* can be estimated from the prior engagements that the client has had with the bank in combination with the employee's intuition concerning the specific client. Information on the *conditions* can be obtained from different organisations, newspapers and a SWOT-analysis.

Not once was Intellectual Capital Statements mentioned in the previous section even though it could have been used on some of Altman's C's. We think that a statement could be used to report on intelligence about the conditions, capacity and character of the client and the company. But this is not yet recognised according to the persons interviewed.

8.2.4 There is a lack of knowledge on how to interpret the statements

It seems as the evaluation process concerning the Intellectual Capital varies between different employees. Each and everyone independent of who their clients are, and what level of experience they have, develop their own methods of dealing with their tasks. The common denominator is that they try to collect as much material as possible, in order to make well-founded decisions. This process is in our opinion not an expression of a creative process, but rather a passive one since only material that can be found is collected and no active choices are made. The fact that the evaluation process is becoming increasingly individual makes it difficult to transform into common knowledge in the organisation. Each and everyone have to develop their own methods and experiences, which takes time. The knowledge that is the result of this development is often tacit.

In our investigation we found that there seemed to be a connection between the amounts of material collected and the closeness between the bank, its employee and the customer. If the bank employee was situated at a smaller local office, the local awareness was usually deeper and more complex. This seemed to affect the decision making process in the following manner: the clients personal characteristic and prior bank engagement gained greater importance, and the bank employees intuition and experience made the decision easier to make. According to the banks', the financial statements and market situation was always considered and emphasised despite this. This has also been supported in investigations made by Green (1997).

If the client was new and nobody knew much about him/her or the company, more information was collected both financial and non-financial. This is also discussed by Svensson Kling (1999). The author states that just as well as the closeness to the client might facilitate the evaluation of a company, it might just as well disturb the employee's ability to maintain his/her objectivity. Hansson, Arvidsson & Lindqvist (2001) argues that the relationship between the client and the bank employee also affects the amount of material collected and the time spent on analysing and interpreting it. These thoughts were supported during all of our interviews.

The employee's individual characteristics affect both the decision-making and the evaluation process. In our theoretical framework we discussed intuition, which is partially dependent on the relationship between the client and the bank employee, as well as from previous experiences made in the line of duty. Green (1997) supports this and also states that intuition gains importance when the insecurity increases or if the information available is insufficient.

We do not agree with her on the last statement though. We found that when it comes to making decisions in a bank uncertainty and risks is something that should always be minimised as much as possible. This means that if a client's proposition is not supported by enough information the decision will be negative. Banks are not supposed to take chances and gamble with peoples' money.

Intuition contributes to a general understanding of the individual client and the company's business concept. During our interviews at Skånes Provinsbank they emphasised the relationship's importance in order to be good evaluators and partners to their customers. The bank also said that much of the work needs a certain amount of experience that helps to decide for example what kind of information is needed, how much information to collect et cetera. According to them experience is not anything that you can learn by reading a book, instead they promote to learn from more experienced colleagues.

Koch does not believe that the investors need to learn more about how to read non-financial information. Instead a standard is needed that makes it possible to look at the information in a systematic manner and make comparisons between different companies. Sullivan (1998) on the other hand states the opposite. He think that it will take time before investors have learned how to use the new figures, even if there is an existing standard that makes it possible to structure the analysis.

8.2.5 They are not functional

This statement is connected to the opinion that there is a need for a standard in order to make the Intellectual Capital Statements more functional. Because of the lack of a standard the statement tend to be just another commercial brochure and not the information and communication tool that it could be. Another negative aspect is that it is hard to make comparisons between the statements today since they focus on different things compared to if there had been an accepted standard.

The Danish and Norwegian guidelines are examples of attempts to create external reports. We think that the Danish model is the more useful one since it presents exactly how to develop a statement that turns to external stakeholders. It is a hands-on model that is easy to comprehend and utilise. The creators, the Ministry of Technology Knowledge and Development's ambition is that the guidelines will be an important tool for different companies in their process of creating a statement. If enough companies find it useful a step towards a common standard is taken. We think that there is a good chance that this will happen. Already 100 companies have evaluated the model and the debate seems more alive compared to the Swedish conditions. Koch (Interview, 021218) as well as Sullivan (1998) are more sceptic though. They say that we are years away from an accepted standard on Intellectual Capital.

8.2.6 They do not see the benefits with the statements

Companies have difficulties seeing the benefits they can have for creating Intellectual Capital Statements. They feel that it takes a lot of resources to develop the statement, both in time and money. Since there is a limited number of companies that actually report continuously on their Intellectual Capital, investors and creditors have difficulties knowing how to use these statements in their evaluations. When Danske Invest made their own Intellectual Capital Statement, the spill over effect was that their employees learned how to interpret others

companies statements and what information to look for. This is something that we believe is a very important implication. By being a part of the company's own development process when creating an Intellectual Capital Statement the knowledge is internalised in accordance with the knowledge spiral.

Banks and especially persons at the Credit Department were not as optimistic as the investors about possible fields of application in their line of work, but they would consider using them when they felt that it was relevant. Koch at Danske Invest explained that Intellectual Capital Statements give important indications on the management's intentions that he feels are valuable for their decision-making. He also means that despite the different department's area of expertise, he believes that they all have use for the same non-financial information, provided by Intellectual Capital Statements.

8.2.7 Too few companies report Intellectual Capital Statements

Some companies might be afraid to expose sensitive information to external stakeholders like their competitors, according to Koch (Interview, 021218) and Sullivan (1998). We do not agree with the opinion that secret information about the company is revealed if they publish an Intellectual Capital Statement. Consequently we do not consider this to be a valid explanation for not making statements. The reason for this is that the content of the statements can be varied depending on which stakeholder that should be reading it. In fact the Danish guidelines recommend that the target audience and the focus of the material as well as the medium should be carefully evaluated before the statement is created. This would minimise the possibility for competitors to take advantage of the information published in the statements. Instead, we think that the companies should use this opportunity to start a dialog with its stakeholders in order to get creative feedback.

8.2.8 Financial statements are still the most important ones for the decision-making

When banks make an evaluation of a company it might serve different purposes. We focused our research on the credit assessment process and the investment process. These processes differ somewhat mainly on the perception of the risk. Our perceptions from the interviews are that when a bank makes a credit assessment the first thing to consider is the financial statements, the proposition from the client and his/her previous history with the bank. The material is subjected to the banks official credit policy, rating models and recommendations on how to handle a specific case like the one that the employee is working on. The result from this analysis is usually presented before a committee that discuss the options and make decisions.

In our investigation we found out both from our interviews and from the literature that bank employees often search for more information than the financial. This is done to create a sense for the individual client and his/her intentions. We mean that there seemed to be a connection between the amounts of material collected and the closeness between the bank, its employee and the customer. If the bank employee was situated at a smaller local office, the local awareness was usually deeper and more complex. This seemed to affect the decision making process in the following manner: the clients personal characteristic and prior bank engagement gained greater importance, and the bank employees intuition and experience made the decision easier to make. According to the banks', the financial statements and market situation was always considered and emphasised despite this. This has also been supported in investigations made by Green (1997).

8.2.9 The organisation's learning

The first step of becoming a learning organisation according to the theory is to apply *adaptive learning*. We think that this is done with the trainee and mentor concept in Skånes Provinsbank where all new employees are working in a team with a more experienced mentor. One problem with this constellation is that the knowledge eventually cannot be separated from the mentor depending on his/her will and ability to teach. The positive effect is when the experienced mentor succeeds with passing on his/her tacit knowledge so that it can be turned into useful explicit knowledge through *socialisation.* Another problem related to the mentorship might be that the adept's skills and knowledge from his/her education that could provide new influences might be unused and neglected. One conclusion that we draw from this is that there is a risk for developing the same kind of knowledge over and over, without any new additions, in the organisation.

The second step in order to become a successful organisation in a dynamic world is that it must apply *generative learning*, with is about experimentation. We mean that the Credit Department of Danske Bank and Skånes Provinsbank cannot take uncalculated risks both since their purpose is to cover profits and margins and the fact that they administer people's money and therefore have obligations towards them. We therefore mean that generative learning in banks' credit departments should not be used if it jeopardises the quality of the decisions. Danske Invest, on the other hand, is able to make investments exposed to a higher degree of risk. However, this kind of generative learning in this organisation is also restricted by the responsibility to their trust holders.

Danske Bank's common rating model is an example of how they *externalise* the tacit knowledge into explicit through a model. With close relationship to other departments of Danske Bank, both in Sweden and in Denmark, the knowledge and culture is *combined* and extends the bank's knowledge base. The final stage in the spiral of knowledge is about new explicit knowledge. This kind of knowledge is known in the entire organisation and should be used to inspire the employees to increase their tacit knowledge, that later is converted to external knowledge as the spiral continuous.

8.2.10 It is too resource demanding

The respondents did not explicitly express this reason, but we sensed that this was one valid explanation that the interviewed persons expressed implicitly. We understood from our interviews that for example the employees at the Credit Department were under a lot of pressure, and that the lack of time was one of their main issues. Intellectual Capital Statements are not supposed to be difficult to understand or interpret, and according to Koch they are not. The employees at the Credit Department at Danske Bank are used to analyse traditional financial information. For them, the new format of the statements might consist a hold-up in the beginning. This could mean that it would take longer to analyse an Intellectual Capital Statement, than to use other information sources that the employee is used to exploit.

8.3 OUR COMPARISON BETWEEN THE NORWEGIAN AND DANISH GUIDELINES

According to the Danish Ministry of Science, Technology and Innovation knowledge is becoming increasingly important as a value creator in the New Economy. The aim is to increase and strengthen the utilisation of the knowledge assets that the company controls. The guideline is a tool that can help to make reports holistic and more systematic as well as achieving the goals above.

The Norwegian financial analyst's ambition is to assist companies (primarily those listed on the stock exchange) that want to expand their reporting with additional information to different stakeholders in a systematically and continuously manner. One objective they hoped to fulfil was that by reporting on additional information increase the understanding of the importance of the Intangible Assets as value creators.

8.3.1 Similarities and differences

The Danish guidelines from 2002 are the second edition that the Ministry of Science, Technology and Innovation has published so far. This edition is based on a revised version of the old guidelines from 2001 and a study performed with 100 participating companies. The information has been collected and analysed by Professor Jan Mouritsen, Copenhagen Business School. The guideline has been developed mainly by academics at the Copenhagen Business School and the Aarhus Business School.

The Norwegian guideline is based on the work of the Norwegian society of Financial Analysts (NFF). A team was assembled during the fall 2001 with the mission to develop suggestions on guidelines for future voluntary reporting on non-financial information in Norway. The team consisted of different representatives from the Norwegian trade and industry and the approach was mainly based on questionnaires.

The different approaches have resulted in different models. There are both similarities and differences between the two models, even though they never mention each other's work in the publications. It is possible that they do not know about their neighbours work, but we think that the background study must have revealed this.

We think that the differences between the two models are the important ones to investigate more thoroughly. This is why the following text will focus mainly on the differences as we see them, instead of accounting for the similarities and differences separately. The analysis will be concentrated to the following headlines:

1. the visualisation
2. the description of strategy and the external conditions
3. the indicators

Let us start at the top of the list.

1. Differences in the visualisation

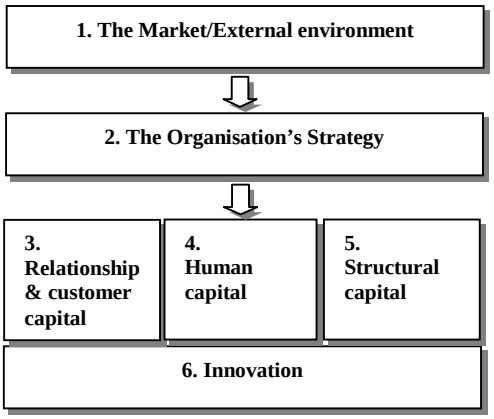

Figure.11: The Norwegian model

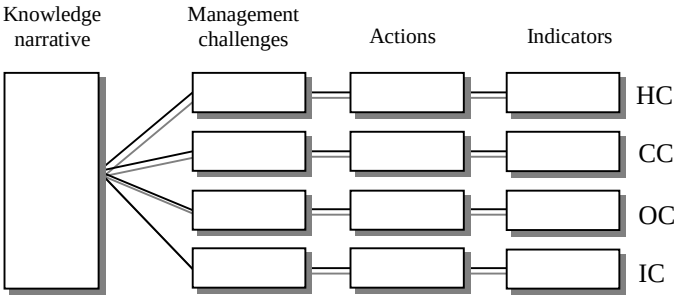

Figure 12: The Danish model

The two models are somewhat different in their visual appearance. The Norwegian model shares some characteristics with the Balance Scorecard and the Navigator, while the Danish model reminds us of a kind of Value Chain model. The layout also shares similarities with the thoughts on cause-and-effect relations as well as mean-aim hierarchies.

The Navigator could actually be applied to both models but in different directions. At the NFF model the direction *horizontal*. The boxes relationship and customer capital, human capital, structural capital and finally innovations are the equivalent to the Navigator's customer focus, human focus process and renewal focus and finally the development focus. In the Danish model the direction is *vertical,* since the categories in the Navigator can be applied at the management challenges, the actions and the indicators.

The Norwegian model is a straightforward model with arrows indicating in what direction the model is to be used. One objection against its layout is that the innovations are located at the bottom of the figure. This might be interpreted as if the other categories above are more important then the innovations. Our suggestion is that this category should be moved to the same levels as the ones above to avoid this misinterpretation. Another suggestion is to show the Intellectual Capital components related to the Danish model as shown in the picture above. Here the abbreviations stand for: HC- human capital, CC- customer capital, OC- organisational capital and finally IC- innovation capital.

The Danish model is not as straight forward as the Norwegian model. This model can in fact be read both from the right to the left or vice versa. In the publication from the Danish Ministry of Knowledge, Technology and Development six questions are formulated to connect the different parts. The question are formulated depending on what directions that is being used in the analysis.

From left to right the questions are related to "how to create value?":

- What values do we want to create?
- What actions to take?
- How shall we do it?

From right to left the questions are related to "what have we achieved?":

- What indicators?
- What actions?
- What achievements is there to tell?

2. The description of strategy and the external environment

Both models recognise the importance of strategy, especially strategy related to knowledge. We find the Norwegian model to emphasise the importance of organisational strategy more clearly than the Danish model does. Evidence of this is already found in the visualisations of the two models. In the Norwegian model the strategy has its own box, and the material from NFF about the model is states that it is important to relate the indicators to the overall strategy.

The Danish model do not emphasise strategy in the same way since it seems more statement driven. Instead the indicators and actions are related to the narrative questions like:

- What is our business idea?
- How do we create value?
- What are our knowledge resources?
- What achievements on the IC components?

When it comes to the description of the external environment the Norwegian model again seems more thorough than the Danish. This may be because it has its own box in the model. This information is primarily described in text compared to the other boxes like the relationship and customer capital box. In the Danish model the effects that the external environment might have is discussed in combination with the actions taken to reach the goals.

3. The indicators

In the Danish model the indicators is the last step in the chain of events. The indicators are in both models a way to be able to control if the goals are met and make comparisons between different years. Since there is no accepted standard difficulties exists when it comes to benchmarking different companies. As a consequence it becomes very important that the company explains their choices on indicators and clarifies what information that is needed in order to calculate them.

If the information is too hard to find reliable and functioning indicators to, the description could be made in writing, since it is no use in reporting numbers in itself.

8.3.2 Pros and cons

Both models have an underlying ambitious thought by trying to put a model for how the Intellectual Capital Statements can be designed into practice. The Danish model has some advantages compared to the Norwegian. First and foremost, the Danes have made their second edition and have studied and collected experiences from 100 companies that have evaluated the model. For the Norwegians it is their first version and they have not been able to test it yet, thereby missing out on valuable experiences.

The Danish model seems very complicated at first sight, but this is simply because the aim was to create a more practical guideline. It has proven to be very useful when constructing statements in different companies. When the work is done, the statements reports valuable information and give a holistic view of the company and its value creating processes. If this is valid for the Norwegian model is yet to be discovered. What this model gains in simplicity, it loses in usefulness. Consequently there is a chance that this model may be too shallow to be useful as a guideline when constructing a statement. On the other hand, some organisations may find this low level of detail liberating and positive since it puts pressure on them to be creative themselves.

A benefit that both models provide is that after a company has constructed a statement of their own, they know what to look for when analysing and comparing their statement to the statements of other companies. Especially the Danish guideline may be useful in this context because of its detailed descriptions of how the statements can be produced. Questions that could be asked in an analysis may be: what existing or potential resources is needed to create value, if the goals are ambitious and if some goals are more important to the company's success than others.

There are some negative aspects to observe. These aspects are primarily related to the companies' opinions of the statements. Examples of what managers say is that the development of this kind of statements take too much time and resources, there are no available standard, which makes it difficult to make comparisons to other companies. Another argument is that if they were to report this information, they would be very restrictive in their external use of it. The reason for this is that they fear that they would be giving away sensitive information and that this would hurt their competitiveness. These arguments indicate that they have problems seeing the benefits from reporting on non-financial information.

8.4 SUMMARY OF THE CHAPTER

In this chapter we have presented our interpretations that resulted from our analysis of the empirical material. The main ideas that were discussed were: the organisation's attitude towards knowledge, the lack of an accepted standard and finally the effects on the evaluation process. A comparison of the two guidelines was made in which we concluded that the Danish model contributes the most at this point. Our thoughts and opinions presented in this section will be used in the next chapter that accounts for our conclusions.

9

EMERGING INSIGHTS

9.1 CONCLUSIONS

In the previous chapter we discussed the reasons external stakeholders have for not looking at Intellectual Capital Statements. There were as much as ten arguments that we listed from our empirical research, some were perhaps more relevant or easier to understand than others. The lack of a systematic approach to identify and analyse the non-financial information makes in our opinion the Intellectual Capital evaluation process less efficient, slow and sprawling. The comprehended uncertainty is increased since everyone has to develop his/her own methods. Some form of guideline would perhaps be of some assistance in this case, and make the evaluation process more efficient and pro-active instead of reactive.

9.2 BANKS AND INVESTORS POSITIONS

The problems with the evaluation process as we see it, is that the current models provided by banks does not seem possible to be adjusted to the different companies' situation. By this we mean that factors like the company's size, its position in the lifecycle and what line of business they belong to does not affect the evaluation models. The creditors at the bank seem to be satisfied with the existing models, like the financial capital rating model and credit policy. They feel that the most important thing to consider is the company's ability to pay back its loans. The analysis of the financial information is therefore central in their evaluation process. If non-financial information is needed, the relationship between the client and the bank is used as well as other sources in the personal network.

Investors in general request more information than bankers, especially non-financial information in order to increase their understanding of the company and its actions. To them, an Intellectual Capital Statement or some other form of report on non-financial indicators is very interesting. It creates a deeper understanding for the company, the management and their way to handle things. The statements and their content might be a determining factor when investors decide on what company to invest in when creating portfolios to their customers.

9.3 THE MOST IMPORTANT STANDPOINTS ACCORDING TO US

There were five arguments that banks and investors overlapped on concerning why they do not look at Intellectual Capital:

- There is a lack of a standard and no commonly accepted terminology
- It is almost impossible to make comparisons between different years and between different companies
- They are not functional in their present shape and there is a lack of stringency
- Too few companies report Intellectual Capital Statements
- The financial statements are the ones that are the most important information source for the decision-making

We believe that these arguments are the most important ones to start working with in order to initiate a change in the negative attitudes and thoughts about the usefulness of Intellectual Capital Statements. If we look closer on the arguments we find that the first four are related to each other since they all can be associated to the lack of a standard.

We understand that both categories, banks and investors, search for additional information in their evaluation processes. But neither the information gathering nor the analysis is done in a systematic manner. We would classify the evaluation processes to be tacit, since every employee has their own methods for how they would like to work. This makes it hard to generalise the knowledge and experience and make it explicit. If banks were using Intellectual Capital Statements or some kind of standardised material in their evaluations, this would probably facilitate the transformation of this knowledge from tacit into explicit.

What gets measured gets done which means that if the value-creating factors are recognised and one starts to work with them they often improve. This indicates that a statement can result in explicit knowledge of what the company does to create value and what resources are needed to do this. A standard might help to overcome the obstacles that exist, like the argument that statements are very resource demanding. It might also help to shape the collective understanding of the company and its value creating processes.

We think that it is important to improve the knowledge about evaluation methods that exist today so that they might fulfil the needs of tomorrow. When standardised Intellectual Capital Statements are becoming more frequently published, it might be a good idea to educate investors and creditors in order to help them increase their understanding for how the statements are constructed and how to interpret them.

The guarded attitude from the creditors could be explained by the lack of a standard in combination with the fact that not many companies report on their Intellectual Assets today. This negative circle is one major problem if the development is to continue. In order to increase the possibilities that a standard will be accepted, we would like to recommend banks and investors to clarify that they are interested in this kind of information from its clients. They should also make their own statements to increase their understanding of the statements and to inspire companies to do the same. This increased inspiration would mean that the companies are motivated to report on their Intellectual Capital, and this in turn will increase the demand for a globally accepted standard.

We hope that the ambitious attempts to create some form of guidelines in Denmark, Norway and the European Union will be recognised and that companies will start to leverage their Intellectual Capital.

The fifth argument was that the most important source of information was, and probably will continue to be, the financial information. This does not have to be a problem at all. We only

want to point out that the financial information must be complemented by non-financial information. We think that Intellectual Capital Statements is one good example of how this information can be systematised and visualised. These statements might be useful information sources in the future when a standard is accepted and should be naturally included in every thorough evaluation process.

There is surely a lack of competence at the individual level when it comes to evaluating non-financial information in some cases. On the organisational level we think that the answer is more closely related to the will to change and adapt new ideas. If there in fact is insufficient staff knowledge when it comes to evaluating Intellectual Capital Statement cannot be fully determined until a standard exists or more companies report on this kind of assets.

9.4 Intellectual Capital Statements in the evaluation process

So why should the Intellectual Capital Statement be used in the evaluation process? Our answer to this question is that it: facilitates the work for the employees, it highlights the critical resources and reduces uncertainty. They complement the information sources that already are available and extend the information on the willingness to pay back and the environmental situation. It helps to indicate if there is positive or negative trend in the development of important Intellectual Capital factors that the financial statements do not regard. And finally it increases the understanding for the company's actions and helps to integrate the information into a holistic picture.

9.5 Future research

One suggestion is to investigate why close countries like Norway and Denmark, does not co-operate to create a common "Scandinavian" standard for guidelines on Intellectual Capital Statements. We believe that by working together the Scandinavian countries can save time and resources, by using their assembled knowledge. Perhaps this will come true when each country has developed their own guidelines that are specially suited for the specific country and its conditions. It is also possible that each country has to make own experiences first, in order to make a future co-operation more productive.

Another suggestion would be to study the Swedish situation. Are there any attempts to create a Swedish guideline? Is there any difference between the acceptance of the statements in a newly established firms versus companies quoted on the stock exchange?

We believe that a standard will increase knowledge on how to handle these statements in the credit evaluation process. A final suggestion for future research is therefor to study the effects on the evaluation processes at banks and investors, after a standard on Intellectual Capital Statements has been accepted and put into practice.

LIST OF REFERENCES

LITTERATURE

- Andersen, I (1998), *Den uppenbara verkligheten,* Studentlitteratur, Lund
- Bastic, Tony (1982), *Intuition- how we think and act*,
- Davenport, T & Prusak, L (2000), *Working Knowledge,* Harvard Business School Press, Boston, Massachusetts
- Edvinsson, L & Malone, M (1997), *Intellectual Capital*, HarperBusiness, New York
- Edvinsson, L (2002) *Corporate longitude navigating the knowledge economy,* Bookhouse, Stockholm
- Grant, Robert M (1991/2001), *Contemporary Strategy Analysis,* Blackwell Publishers Ltd, Malden, Massachusetts
- Green, E (1997), *Kreditbedömning och intuition*, Lund University Press, Lund
- Hansén, S & Thor, C (1997), *Intervjua, en grundbok för media*, Ordfront förlag
- Hansson, S, Arvidsson, P & Lindquist, H (2001), *Företags- och räkenskapsanalys*, Studentlitteratur, Lund
- Hatch, Mary Jo (2000), *Organisationsteori*, Studentlitteratur, Lund
- Holme, I M & Solvang, B (1996), *Forskningsmetodik*, Studentlitteratur, Lund
- Jacobsen, D I & Thorsvik, J (1998), *Hur moderna organisationer fungerar,* Studentlitteratur, Lund
- Kaplan, R S. &. Norton, D P (1996), *The Balanced Scorecard*, Harvard Business School Press, Boston, Massachusetts
- Lundahl, U & Skärvad, P-H (1999), *Utredningsmetodik för samhällsvetare och ekonomer*. Studentlitteratur, Lund
- Nonaka & Takeuchi (1995), *The knowledge creating company,* Oxford University press, New York
- Nordström, K A & Ridderstråle, J (2000), *Funky Business*, BookHouse Publishing, Stockholm
- NUTEK (1992), *Riskbedömning – bankers riskbedömning vid kreditgivning till nystartade Företag,* Stockholm

- Olve, N-G, Roy J & Wetter M (1999 edition 3:2), *Balanced Scorecard i svensk praktik*, Liber AB, Malmö
- Patel, R & Davidson, B (1994), *Forskningsmetodikens grunder, att planera genomföra och rapportera en undersökning,* Studentlitteratur, Lund
- Repstad, P (1999), *Närhet och distans, kvalitativa metoder i samhällsvetenskap,* Studentlitteratur, Lund
- Silver, L (2001), *Credit risk assessment in different contexts,* Universitetstryckeriet, Uppsala
- Sullivan, P H (1998), *Profiting from Intellectual Capital,* John Wiley & Sons Inc., Canada
- Starkey, Ken (1996/2001), *How organizations learn,* International Thomson Business Press, Senge, P M, *The leader's new work- building learning organizations*
- Stewart, T A. (1997/1999), *Intellektuellt kapital*, Nerenius & Santérus Förlag, Stockholm
- Sveiby, K E, Konradgruppen (1990), *Den osynliga balansräkningen,* Affärsvärldens förlag AB, Gotland
- Svensson Kling, K (1999), *Credit intelligence in bank,* Lund Business Press, Lund
- Wiedersheim-Paul, F & Eriksson, L-T (1991 4:th edition), *Att utreda, forska och rapportera*. Liber-Hermods, Malmö

ARTICLES

- Edvinsson, L, Kitts, B & Beding, T, *The next generation of IC measurement-the digital IC-landskape,* Journal of Intellectual Capital, vol 1 No 3, MCB University Press, 2000
- Gu, F & Lev, B (April 2001), *Intangible Assets, measurement, drivers, usefulness**
- Lev, B (January 2000), *Knowledge and Shareholder Value **
- Lev B (May 2000), *New Accounting for the New Economy**
- Mouritsen, J, Torsgaard, L & Bukh, P.N, *Dealing with the knowledge economy & Intellectual Capital versus Balance Scorecard,* Copenhagen Business School & Aarhus School of Business, February 2002
- Sandström, O (020720), *Risktagare tar inga risker längre,* Dagens Nyheter, part C page 3 (020902), *Special: Riskkapital – Snålheten tar över,* Veckans Affärer

* articles were found at www.baruch-lev.com

ELECTRONIC SOURCES

www.baruch-lev.com

www.danskebank.dk

www.danskeinvest.dk

www.fasb.org

www.iasplus.com

www.intellectualcapital.se

www.ll-a.fr/intangibles/overview.htm

www.oeb.se

www.sec.gov

www.sveiby.com/articles/Emergingstandard.html

www.videnskabsministeriet.dk

www.finansanalytiker.no

EMPIRICAL SOURCES

- KPMG (2001), *Den nye årsregnskabslov*.
- Ministeriet for Videnskab Teknologi od Udvikling conference (12th December 2002), *Videnregnskaber Ny guidline – nye muligheder*
- NFF conference (28th November 2002), Vend selskapets innside ut; - Tilleggsinformasjon om verdiskapning, Oslo

INTERVIEWS

Danske Bank, International credits, Copenhagen 02-11-26

Niels Taklo	Vice President	Large Customers-Credit office
Lise Gronø	First Vice President	Credits Department
Thomas Justinussen	Vice President	Credits Department

Skånes Provinsbank, Malmö 02-12-18

Magnus Paulsson	Managing Director
Cecilia Arkestad	Client Manager

Danske Invest, Copenhagen 02-12-18

Carsten Koch	Managing Director	Danske Invest Administration A/S

LIST OF FIGURES AND TABLES

FIGURES

TABLES

APPENDIX 1 – QUESTIONNAIRE

INTERVIEW WITH DANSKE BANK (021126) AND SKÅNES PROVINSBANK (021218)

Description of the organisation and the decision-making process

1. Danske Bank's credit policy, in Denmark and Sweden. What are the differences/ similarities? How are decisions made?
2. "Cultural" differences, effects from political decisions? Differences when it comes to Intellectual Capital?
3. Describe the internal rating model.

The work process

4. How is the evaluation of Intellectual Capital made practically?
5. How do you collect the material/information about the company? What kind of information do you request?
6. In what way do you consider Intellectual Capital? Which ones are important to consider compared to financial indicators?
7. Are you using the same rating model on all companies or are there any differences depending on the company's characteristics?
8. Do you feel that it is hard to evaluate knowledge intensive companies? How much of your portfolio is invested in this category of businesses?
9. Are there any knowledge intensive firms that report in their Intellectual Capital that you find relevant? If so, why?
10. Have you heard of "Guideline for videnregenskaber" from the Ministry of Knowledge, Technology and Development? Does it affect your work?
11. Is there an increased interest in evaluating Intellectual Capital?
12. Has the IT boom affected your credit assessments?
13. Voices are raised that the traditional accounting does not provide enough information and that the Intellectual Capital should be included. Are you of the same opinion?
14. Do you feel that you are lacking knowledge on how to interpret the Intellectual Capital Statements?

APPENDIX 2 – QUESTIONNAIRE

INTERVJU WITH DANSKE INVEST, CARSTEN KOCH (021218)

1. Describe your organisation and relation to Danske Bank
2. What differences are there between an investment department and a credit department?
3. How did you come in contact with the term Intellectual Capital? Why was it introduced in Danske Invest?
4. Why has Danske Invest made their own Intellectual Capital Statement and who are your target audience? Describe your statement.
5. Have you been using the Danish guidelines?
6. Do you feel that investors need new knowledge to understand Intellectual Capital Statements?
7. Have you used the Balanced Scorecard?
8. What do you think about the Danish guidelines?
9. Do different departments have use for statements on Intellectual Capital?
10. How do you evaluate Intellectual Capital Statements?
11. Why are standards important? Who will develop them in your opinion?
12. Do you request and inspire companies to create statements of their own? How?
13. What is your opinion on financial information?
14. Is there a need to account for non-financial information? Why?
15. What do you think about the future of the concept?