Intellectual Capitalist: An Interview with Thomas Stewart

Capital used to be viewed in physical, tangible terms – factories, machinery and money. Now the quest is on for greater understanding of the most intangible, elusive, mobile and important asset of all: intellectual capital. Interview by Stuart Crainer.

Intellectual capital can be crudely described as the collective brainpower of an organisation. The switch from physical assets to intellectual assets – brawn to brain – as the source of wealth creation has been underway in the developed economies for some time. As an advertisement for Deutsche Bank put it: “Ideas are capital. The rest is just money”. Among the most influential chroniclers of this shift is the Fortune columnist Thomas A Stewart, author of The Wealth of Knowledge and Intellectual Capital: the New Wealth of Organizations.

Stewart claims that the changes taking place are as significant as the Industrial Revolution. “Knowledge has become the most important factor in economic life. It is the chief ingredient of what we buy and sell, the raw material with which we work. Intellectual capital – not natural resources, machinery or even financial capital – has become the one indispensable asset of corporations,” he says.

Intellectual capital is irrevocably bound up with the notion of the knowledge worker and knowledge management. Peter Drucker’s 1969 book The Age of Discontinuity introduced the term knowledge worker to describe the highly trained, intelligent managerial professional who realises his or her own worth and contribution to the organisation. The knowledge worker was the antidote to the previous model – corporate man and woman.

Drucker recognised this new breed but key to his contribution was the realisation that knowledge is both power and ownership. Intellectual capital is power. If knowledge, rather than labour, is the new measure of economic society then the fabric of capitalist society must change.

Converting knowledge into intellectual capital is a new and elusive form of corporate alchemy.

“Intelligence becomes an asset when some useful order is created out of free-floating brainpower,” notes Stewart. “Organisational intellect becomes intellectual capital only when it can be deployed to do something that could not be done if it remained scattered around like so many coins in a gutter.

“Intellectual capital is useful knowledge that is packaged for others. In this way, a mailing list, a database or a process can be turned into intellectual capital if someone inside the organisation decides to...
describe, share and exploit what’s unique and powerful about the way the company operates.”

Intellectual capital is often divided into human capital, customer capital and structural capital. Human capital is implicit knowledge – what’s inside employees’ heads. Customer capital involves recognising the value of relationships that exist between the company and its customers. Structural capital is knowledge that is retained within the organisation and can be passed on to new employees. According to Stewart: “Structural capital is knowledge that doesn’t go home at night”.

Stewart also argues that the knowledge economy augurs the end of management as we know it. Today’s knowledge workers carry the tools of their trade with them between their ears. It is they and not their managers who are the experts and must decide how to best deploy their know-how. As a result, what they do has more in common with work carried out by people in the professions and must be assessed not by the tasks performed but by the results achieved.

From this, he says, it follows that the professional model of organisational design should supersede the bureaucratic. So where does this leave managers? The answer, Stewart suggests, is that the only legitimate role for managers is around the task of leadership – although they don’t yet have a proper understanding of what’s involved.

He says: “If values and vision and empowerment and teamwork and facilitating and coaching sometimes sound like so much mush-mouthed mish-mash – which they sometimes are – that’s a reflection of the fact that managers are groping towards a language and a means for managing knowledge, knowledge work and knowledge-intensive companies”.

Stewart talked about knowledge management and the evolution of intellectual capital during a recent visit to London.

**Your book cites Enron as an example of best practice. You were not alone in lauding the company’s management practices. What do you now say?**

Enron is an interesting story in a number of ways. This sort of misbehaviour comes about because people think they can get away with it and people are prepared to believe it. But frauds and bubbles do not occur independently of real opportunities. People sell patent medicines because there are real medicines. People invest in tulips because there is a world of opportunity.

Enron was, therefore, a perverse manifestation of real opportunities as well as being a cautionary tale. Enron reported business that wasn’t there. Enron was a fiction but that doesn’t mean that everything intangible is a fiction. One of the other things that Enron tried to do was to create markets in things that hadn’t existed before. That is already happening elsewhere – in electricity, for example. The fact that Enron inaccurately and deliberately mis-stated results from those markets doesn’t change those underlying facts.

Enron should serve as a challenge. It shows that we really need to fix accounting. The inadequacies of traditional accounting allow people to get away with such things. Accounting needs reinvention as well as
reform. Unfortunately, Enron may move things the other way.

There is a sense looking through your book and others on intellectual capital that only a small number of companies are making it work. The same names keep cropping up.

You’d always like to find brand-new companies doing exceptionally interesting things. But over the years it tends to be a small number of companies, I suppose you could call them the usual suspects.

Intellectual capital is being implemented effectively by some companies. The Scandinavian countries, led by Denmark, are leading the way in terms of reporting intellectual capital. But knowledge management is being implemented inefficiently in a larger number of companies. To some extent the intellectual capital agenda has been captured by knowledge management to the detriment of both.

The difference between knowledge management and intellectual capital is basically the same as the difference between management and capital. Management is something you do to get more out of capital. Knowledge management has become the domain of the technologists, which is useful but not the be all and end all.

Isn’t intellectual capital in danger of becoming just another management fad?

Surviving fad-dom is not a trivial accomplishment. The definition of a fad is that people start doing something without having a reason for doing it. There was a study by Forrester Research that found that six out of seven companies undertaking knowledge management projects did not calculate return on investment. That’s a definition of a fad.

More money has been wasted than made in knowledge management so far. When things go wrong it’s usually because it has been introduced for faddish reasons. But increasingly I see companies looking first to discover their knowledge business, their knowledge value proposition – what they know that they can sell and how to sell it profitably – and then figuring out how to manage knowledge. That is an approach that works.

So, the faddishness is disappearing. You can see it in the diminishing advertising pages of knowledge management magazines. Going out and throwing technology at it is over. That’s good because it creates the real opportunity, the opportunity that I write about: let’s find the knowledge and build the organisation around it to run a profitable knowledge business. Too many companies have seen knowledge as an internal matter, making sure that everyone knows what everyone else knows. All this is good, but to what end?

If knowledge management is something of a distraction, what should managers be looking at?

The real question is what is the knowledge business? And then, tracking the knowledge business, building and acquiring the assets needed to make the business more profitable and effective. The wealth of knowledge is not found internally but in the markets.

We need to look at what customers are buying and ask questions. Why are they shopping in our store?

Why aren’t they buying from the competition? What do people purchase from us that is unique and valuable? What is a customer paying for when he or she buys from us? The answer is some set of attributes and price – quality, breadth of product line and so on. But what created that broad product line, technical expertise or quality? What allows companies to offer low prices? It’s then you uncover knowledge, the knowledge assets that produce value.

Aren’t knowledge management and intellectual capital fighting against human nature? People are simply not very good at sharing.

One of the big questions in an organisation is how you get promoted. A lot of organisations that talk about knowledge reward people for hoarding rather than sharing it. Until you build knowledge sharing into reward systems and culture it won’t change.

If you ask a question in a company – can you help me with this? – you need to know that it is alright to ask such questions, have a reasonable expectation that you will get an answer and be able to find the best person to approach. Before they answer, the person questioned also has a number of barriers. Who is the person asking the question? Will they try to take credit for the answer? Will I get into trouble if I answer?

There are a lot of sociological and psychological issues that organisations need to get at before knowledge
starts flowing around. You can do all you like with technology but issues like politics, permission and power are extraordinarily important.

So organisations need to change for intellectual capital to be valued and to create value?
Radical changes in the structure of organisations are required. The law and economic theory say that a company is a bundle of assets. Information Age fact says it is really a beehive of ideas. That change has profound implications for how companies are set up and run – and how they compete.

Companies exist to provide purpose, to be a magnet for intellectual capital, to host conversations and house tacit knowledge, to offer a warranty in terms of brand and reputation, and to perform financial and administrative services.

Are organisations changing?
The best companies in every industry have begun the process of identifying themselves with their ideas more than with their assets. Companies now share assets through outsourcing. Cisco owns less than a handful of factories that actually make products. Most of its products are not touched by Cisco people. There are more and more joint ventures and alliances, odd hybrid structures, professional service firms going public to gain access to capital markets. There are all kinds of fusing of what were once fairly clear boundaries between one company and the next.

Already intellectual capital is being measured at national level. Is this helpful?
We know that knowledge is created when smart people talk to each other. Clusters are intense places of interaction. Governments can encourage that by looking at taxation and immigration to see what they can do to attract the brightest people in the world. Human brains have always been randomly distributed.

There are a profusion of models and measures of intellectual capital. Will there be one dominant and accepted measure?
There is no sense that there will ever be one measure but every company needs to be measuring in some way what its knowledge assets are and how well it is investing in them and exploiting them.

There are some people who see knowledge as packaged goods. They want to know where to sign up to get some of that. They finish with cans of soup and no can openers. The right approach is not packaged goods but to start with an understanding of what is the knowledge that matters. You don’t have to have the same knowledge or knowledge assets as anyone else. If you do, you’re not unique.

How would you describe the process by which intellectual capital can be managed?
First, you need to identify and evaluate the role of knowledge in your business – as input, process and output. How knowledge intensive is the business? Who gets paid for what knowledge? Who pays? How much? Does whoever owns the knowledge also create the most value?

Second, match the revenues you’ve just found with the knowledge assets that produce them. What are the expertise, capabilities, brands, intellectual properties, processes and other intellectual capital that create value for you? What is the mixture of human capital, structural capital and customer capital assets?

Third, develop a strategy for investing in and exploiting your intellectual assets. What are your value proposition, source of control and profit model? What strategies exist to increase the knowledge intensity of your business? In what ways can you increase your ability to leverage your intellectual assets? Can you improve results by restructuring intellectual assets (for example, converting human capital into structural capital or vice versa)?

Finally, improve the efficiency of knowledge work and knowledge workers. Bearing in mind that knowledge work does not necessarily follow the linear path that physical labour often does, how can you increase knowledge workers’ productivity?

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