

“Guidelines for Practices of Intellectual Asset-Based Management for Small and Medium Enterprises”

(Summary)

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Organization for Small & Medium Enterprises and Regional Innovation, Japan

The Organization for Small & Medium Enterprises and Regional Innovation, Japan (SMRJ) established “the SME Intellectual Asset-Based Management Forum” in 2006, and thereby has supported the efforts of intellectual asset-based management by small and medium enterprises (SMEs). Last year, SMRJ compiled the “Intellectual Asset-Based Management Manual for Small and Medium Enterprises” so that SMEs can put intellectual asset-based management into practice, and have encouraged its broad use.

The manual indicates that what proprietors of SMEs engaged in intellectual asset-based management are concerned with is a proper evaluation from people engaged in finance; meanwhile, financial institutions are keeping a close eye on the “improvement of ability to identify qualities” or improvement of evaluation ability of intellectual assets as an urgent issue in relationship banking as specified in the “Comprehensive Guidelines for Supervision of Small and Regional Financial Institutions” released in 2007 by the Financial Services Agency.

In consideration of this situation, from a point of verifying the effectiveness of the disclosure to stakeholders, SMRJ clarifies the actual status by conducting research and study including evaluation of intellectual assets and use of non-financial information on credit decisions, etc. in financial institutions which are among those that receive the disclosure information from an enterprise. In addition, SMRJ conducts research and study on support for preparing an Intellectual Asset-Based Management Report with the main objective of utilizing the Intellectual Asset-Based Management Manual for Small and Medium Enterprises in actual business situations.

In order to proceed with the research and study at this time, SMRJ has set up the “Finance Working Group of Intellectual Asset-Based Management by SMEs” under the SME Intellectual Asset-Based Management Forum, whereby analyses, examinations, and summarizations with reference to these Guidelines are implemented.

Also, note that these Guidelines comprise two separate parts: “Research/Study Version of Support to Compile an Intellectual Asset-Based Management Report” and “Research/Study Version of Intellectual Asset-Based Finance.”

“Research/Study Version of Support to Compile an Intellectual Asset-Based Management Report”
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Chapter 1 Compilation support of an Intellectual Asset-Based Management Report (Introduction of model enterprise cases)

SMRJ provided support for the compilation of an Intellectual Asset-Based Management Report to 10 companies which had been working on intellectual asset-based management in accordance with the Intellectual Asset-Based Management Manual for Small and Medium

Enterprises compiled last year.

Companies that SMRJ supported in compiling such reports are as follows:

- (1) Kimura Alumi-Haku Co., Ltd.
 - manufactures silver foil, aluminum containers, and film canisters.
 - engaged in production of molded cups and aluminum containers, and cutting and processing of silver foil to flat seals.
- (2) Kur and Hotel Ltd.
 - originally started business for the purpose of managing business hotels, but expanded its operation by having newly established its health land division.
 - maintains a highly profitable structure primarily based on this new division.
- (3) SEIRIN CORPORATION
 - specialized producer of needles for acupuncture with its business structure exclusively focusing on manufacturing disposable needles for acupuncture.
 - already grown to become the leading domestic manufacturer in this field.
- (4) DENSOKU TECHNO Co., Ltd.
 - mainly engages in production, repair, and calibration of electric measuring instruments and manufacturing and sales of watt-hour meter test sets and watt-hour meter test boards.
- (5) Nimbari Kousakusyo Co., Ltd.
 - although engaged in the sheet-metal processing industry, has high technology and a manufacturing structure enabling integrated production, and is differentiating itself as a complete manufacturer which can make completed products from other companies.
- (6) Hashinaga Kinzoku Co., Ltd.
 - is a specialized trading firm selling non-ferrous metal materials and processed parts used as functional materials of autos and digital home appliances.
- (7) Fuji Kousakusho Co., Ltd.
 - engages in can production, sheet-metal production, press machining, laser processing, etc.
 - manufactures various industrial equipment parts such as water turbines for power generation, boiler parts, and boring equipment.
- (8) Meiji Sangyou Co., Ltd.

- business includes retail and wholesale operations of incidental equipment to household equipment with equipment that runs on liquefied petroleum gas as its core.

(9) Yamasan Co., Ltd.

- seafood processor of shrimp rice crackers, squid rice crackers, etc., with a long-standing reputation over 50 years in the region, albeit small scale.

(10) Yuei Caster Co., Ltd.

- manufacturer of casters and related products, and always focuses on developing new products in addition to manufacturing a lot of current products as backed by its long business history.

Chapter 2 Actual situation of companies dealing with intellectual asset-based management

SMRJ conducted an inquiry survey concerning intellectual asset-based management, targeting companies which compile an Intellectual Asset-Based Management Report and supporters of the compilation of the report. The main points gained from the review based on its result are as follows:

- (1) Companies named financial institutions, customers, suppliers, employees, and formulation of their management vision as the purposes of compiling the report. The content includes both use by outside parties such as financial institutions and customers and internal use for employees; consequently, as it stands now, the report is compiled for diversified targets.
- (2) Among disclosure targets which respondents felt were the most effective, customers and users were at the top; this leads to an estimate that there are many opportunities to introduce their own companies in sales activities.
- (3) Those companies which compiled the report once are considering continuously preparing it in the future, and more than 70 percent are considering updating it once every one to two years.
- (4) Meanwhile, supporters of compiling the report are conscious of financial institutions as disclosure targets. They expect improvement of evaluation from financial institutions. For this purpose, they recognize that further diffusion and education are necessary.
- (5) Future issues include the difficulty of establishing substantiating indicators (e.g. establishment of KPI, etc.), the length of time required for the compilation and the improvement of recognition of intellectual asset-based management by introducing a lot of example compilations.

Chapter 3 Management Report Elevating Business Value (Intellectual Asset-Based Management Report)

SMRJ examined how to make a report in order to explain plainly and briefly to stake holders

for the purpose of further disseminating and utilizing intellectual asset-based management. Specifically, SMRJ compiled as “Management Report Elevating Business Value” an Intellectual Asset-Based Management Report whereby management of a company can be expressed in a single A3 sheet. SMRJ has developed a method even for a smaller-sized company to be able to compile an Intellectual Asset-Based Management Report based on Intellectual Asset-Based Management Manual for Small and Medium Enterprises which was compiled in 2007. The compilation method and two model companies will be introduced.

(Examples of “Management Report Elevating Business Value: model companies)

- (1) Nimbari Kousakusyo Co., Ltd.
- (2) Kur and Hotel Ltd.

“Research/Study Version of Intellectual Asset-Based Finance”

Chapter 1 Actual situation of use of non-financial information at financial institutions

In order to verify the present state of evaluation of “intellectual assets” and credit decision and the utilization situation of non-financial information at the time of decision of whether or not to provide finance in financial institutions, SMRJ conducted a hearing investigation to seven financial institutions and administered a questionnaire survey to 575 financial institutions across the country. The main points are as follows:

- (1) The survey has revealed the actual state of utilization of non-financial information and prioritized items during operation supports and at credit decision by financial institutions.

For example, in using non-financial information at the time of operation support, management plan, ability of management control, and existence of successor are ranked high, while the company’s borrowing potential, transaction status with other banks, and existence of successor were of higher priority in using non-financial information at the time of credit decision. Observing items ranked higher; financial institutions still appear to persistently put more emphasis on mortgage collateral or personnel guarantee rather than on ability to identify qualities of business value (see charts 2-1-3 and 2-1-4 of the attached sheets).

- (2) Also in responding to community-based finance in financial institutions (relationship banking), compliance system, management plan, and changes in business, etc. are ranked high as prioritized items after an action program of relationship banking is released. The importance and others of compliance seem to be primarily attributable to responses to risks by companies, mainly because of the faked production area or country and freshness date of foods and the scandal over buildings built based on fabricated earthquake resistance data (see chart 2-1-6 of the attached sheets).

- (3) The following situation has been found based on the survey result:
 - In utilization degree of intellectual assets (viewpoint of evaluation), related assets are ranked high in credit decision as viewed from the relation of human assets,

related assets and structural assets. In particular, items such as status of transactions with other banks and related companies are ranked high.

- Items emphasized in credit decisions are also emphasized for operation support as a whole. However, existence of successor, among others, is an item where a distinct difference is seen (see chart 3-2 in the attached table).
- Utilization ratio between non-financial information and financial information is approximately 3 to 7. Financial institutions using non-financial information more than 30 percent of the time account for over 50 percent of the whole.
- More than half of financial institutions make an evaluation using the prepared hearing sheet.
- Utilization rate of non-financial information per type of bank is the highest in regional banks.

Chapter 2 Ideal effective utilization of non-financial information in future

In response to the actual status of utilization of non-financial information in financial institutions described in Chapter 1, the chapter evaluates and verifies intellectual asset-based management of SMEs as seen from financial institutions, and summarizes ideal effective use of non-financial information toward the promotion of intellectual asset-based finance. The main points are as follows:

- (1) With reference with the efforts by financial institutions, particularly important factors are changes in consciousness of use of non-financial information and qualitative information of financial institutions, improvement of analysis and evaluation methods of intellectual assets, and human resource development and establishment of finance structure to promote intellectual asset-based finance.
- (2) Meanwhile, in order to expand the compilation and disclosure of Intellectual Asset-based Management Report from SMEs, it is important, like the case of financial institutions, to enhance recognition of proprietors of SMEs as well as accumulate internal know-how to improve the quality of “communications” through an Intellectual Asset-based Management Report as a means of communication and, at the same time, work on tools to improve human development programs to support it. In addition, utilization of qualified professionals with special knowledge, etc. is effective.
- (3) With regard to the approaches by policy makers, the most important role is expected to be diffusion of the Intellectual Asset-based Management Report and effective use of non-financial information. Specific measures where policy makers can take initiative include promoting recognition of the Intellectual Asset-based Management Report among SMEs, supporting improvement of the report by SMEs, disseminating utilization of the report by SMEs, and facilitating the unification of intellectual asset-based information disclosure.

Chart 2-1-3
Top 26 items of non-financial information during operation support (Averaging 3.48 points or over)

No.	Item	Average	SD
1	52. Management plan	3.97	0.680
2	14. Management control ability	3.93	0.642
3	31. Superiority of techniques	3.92	0.649
4	22. Existence of successor	3.91	0.626
5	30. Changes in business content	3.85	0.674
6	44. Borrowing potential	3.83	0.680
7	35. Superiority of main business	3.82	0.650
8	34. Profitability of products, goods, and services	3.81	0.674
9	17. Personality	3.79	0.678
10	43. Status of transactions with other banks	3.79	0.662
11	33. Superiority and brand of products, goods, and services	3.74	0.633
12	42. Existence of main bank	3.71	0.673
13	24. Individual assets of proprietor	3.69	0.672
14	64. Related companies	3.69	0.661
15	28. Economic climate, sensitivity to economy	3.69	0.626
16	29. Situation of competitors	3.66	0.634
17	51. Management principles	3.62	0.654
18	16. Leadership	3.62	0.664
19	67. Compliance structure	3.61	0.731
20	36. Clients and their situations	3.58	0.645
21	32. Intellectual property (rights)	3.56	0.696
22	15. Planning ability, ability to create ideas	3.53	0.635
23	23. Health condition	3.52	0.598
24	63. Supporting system of parent company	3.52	0.643
25	54. Business model	3.52	0.661
26	66. Response to legal risk	3.51	0.683

Chart 2-1-4
Top 21 items of non-financial information in making a judgment of finance (Averaging 3.57 points or over)

No.	Item	Average	SD
1	44. Borrowing potential	4.01	0.623
2	24. Individual assets of proprietor	3.99	0.592
3	43. Status of transactions with other banks	3.96	0.603
4	22. Existence of successor	3.95	0.567
5	52. Management plan	3.95	0.606
6	14. Management control ability	3.93	0.586
7	64. Related companies	3.88	0.641
8	42. Existence of main bank	3.86	0.626
9	30. Changes in business content	3.85	0.592
10	31. Superiority of techniques	3.85	0.596
11	35. Superiority of main business	3.84	0.620
12	34. Profitability of products, goods, and services	3.81	0.625
13	28. Economic climate, sensitivity to economy	3.80	0.622
14	17. Personality	3.78	0.656
15	29. Situation of competitors	3.73	0.597
16	33. Superiority and brand of products, goods, and services	3.68	0.585
17	63. Supporting system of parent company	3.66	0.629
18	67. Compliance structure	3.64	0.759
19	36. Clients and their situation	3.63	0.626
20	23. Health condition	3.61	0.602
21	66. Response to legal risk	3.60	0.705

Chart 2-1-6 Time-series comparison after the release of action programs of relation banking
– non-financial information

No.	Item	Time-series average	SD	Average during operation support	SD	Average of loan judgment	SD
1	67. Compliance structure	3.60	0.713	3.61	0.731	3.64	0.759
2	52. Management plan	3.58	0.641	3.97	0.680	3.95	0.606
3	30. Changes in business content	3.51	0.598	3.85	0.674	3.85	0.592
4	14. Management control ability	3.51	0.613	3.93	0.642	3.93	0.586
5	66. Response to legal risk	3.45	0.657	3.51	0.683	3.60	0.705
6	31. Superiority of techniques	3.43	0.590	3.92	0.649	3.85	0.596
7	22. Existence of successor	3.43	0.587	3.91	0.626	3.95	0.567
8	65. Response to leakage risk of operational confidentiality	3.40	0.628	3.39	0.683	3.34	0.706
9	64. Related companies	3.40	0.593	3.69	0.661	3.88	0.641
10	32. Intellectual property (rights)	3.39	0.576	3.56	0.696	3.44	0.668

Chart 3-2 List of average points of three categories in intellectual assets

	Average during supporting business	Average of finance judgment	Time-series average
Human assets (proprietors)	3.51	3.50	3.19
14. Management control ability	3.93	3.93	3.51
15. Planning ability, ability to create ideas	3.53	3.36	3.26
16. Leadership	3.62	3.49	3.21
17. Personality	3.79	3.78	3.25
18. Age of representative	3.45	3.47	3.17
19. Career in the industry	3.26	3.35	3.05
20. History in managerial positions	3.36	3.41	3.06
21. Human network	3.32	3.25	3.06
23. Health condition	3.52	3.61	3.18
25. Degree of devotion to business	3.36	3.37	3.10
Human assets (employees)	3.19	3.10	3.10
45. Number of employees	3.17	3.13	3.07
46. Average age of employees and rate change from the previous year	2.99	2.95	3.04
47. Turnover ratio	3.06	3.04	3.08
49. Know-how	3.35	3.23	3.16
50. Those holding qualifications and techniques	3.35	3.24	3.16
59. Degree of development of education	3.19	3.03	3.08
Related assets	3.48	3.51	3.19
26. External public relation activities	3.15	3.08	3.06
36. Clients and their situations	3.58	3.63	3.18
37. Suppliers and their situations	3.42	3.42	3.12
38. Relations with clients	3.42	3.41	3.14
39. Relations with suppliers	3.32	3.30	3.10
40. Customer satisfaction level	3.45	3.32	3.22
41. Promotion activities/advertising activities	3.23	3.12	3.09
42. Existence of main bank	3.71	3.86	3.27
43. Status of transactions with other banks	3.79	3.96	3.34
63. Supporting system of parent company	3.52	3.66	3.20
64. Related companies	3.69	3.88	3.40
Structure assets	3.43	3.40	3.29
22. Existence of successor	3.43	3.91	3.95
27. Share and position in the industry	3.48	3.53	3.18
30. Changes in business content	3.85	3.85	3.51
31. Superiority of techniques	3.92	3.85	3.43
32. Intellectual property (rights)	3.56	3.44	3.39
33. Superiority and brand of products, goods, and services	3.74	3.68	3.37
34. Profitability of products, goods, and services	3.81	3.81	3.37
35. Superiority of main business	3.82	3.84	3.35
48. Incentive system	2.83	2.77	3.00
51. Management principles	3.62	3.45	3.25
53. Company brand	3.38	3.32	3.15
54. Business model	3.52	3.43	3.27
55. Number of business offices	3.00	2.99	3.00
56. Smoothness of management-labor relations	3.14	3.09	3.05
57. Internal suggestions for improvement system and number of improvements implemented	3.02	2.87	3.04
58. Personnel evaluation system	2.94	2.81	3.01
60. Situation of introduction of IT system	3.14	3.06	3.18
61. Structure of the company	3.38	3.28	3.27
62. Commitment to research and development	3.36	3.26	3.17
65. Response to leakage risk of operational confidentiality	3.39	3.34	3.40
66. Response to legal risk	3.51	3.60	3.45
67. Compliance system	3.61	3.64	3.60