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What the market foretells

Intellectual property-related concerns and issues will increasingly affect corporate decision-making over coming years

Chicago, Illinois September 8, 2003: Everybody talks about the weather knowing full well that there is very little we can do about the hurricanes and tornados that blow our way except to duck and take cover. The question for IP professionals is whether the growing intangibility of corporate value is a weather report or alternatively, a weather machine providing for an opportunity to change and manage our environment.

Our forecast is generally that corporate executives and directors seeking to maximise shareholder value must now fully understand and manage their intangible assets. More specifically, we offer the following 10 predictions:

Prediction One: The irreversible trend toward intangibles. The thermodynamics of knowledge favours the increase of information because it is entropy positive. Additional knowledge increases the number of available economic alternatives to which it can be applied. Yet because information transfer efficiencies have risen in proportion with computing technologies, highly effective economic states based on proprietary knowledge can be preferentially occupied through licensing while still meeting thermodynamic constraints. In other words, by their very nature intangibles lend themselves to efficient commercialisation as the asset can be replicated without cost and then sold to an endless stream of buyers.

Prediction Two: Corporate understanding and management of IP assets. Corporate executives and directors have an understandable focus on maximising shareholder value, ie share price. Given that a large percentage of what investors are now buying is intangible it is obvious that managers will begin to focus greater attention on this asset and indeed begin to communicate to the investing public an understanding of and appreciation for IP.

Prediction Three: Redeployment from tangibles to intangibles. Often the fate of a successful business is to become a brand or a bank or, preferably, both. General Electric water heaters have the largest market share at Home

Depot. Funny thing is, GE hasn't made water heaters in over 20 years. GM has sales of US\$190 billion and a market cap of US\$23 billion. Harley-Davidson has sales US\$4.6 billion and a market cap of nearly US\$15 billion. Thanks in part to its brand, GE now earns roughly 40% of its income from GE Capital which, is a finance company. That's the "preferably, both".

Prediction Four: Corporate metrics for success will be based on measurements of intangibles. In the politics of business, advancement depends on the clear fingerprint of success in past accomplishments. The problem with intangibles today is that they are often not accounted for so their successful use rarely points to particular actors. The politically savvy manager will quickly realise that without clear intangible metrics, someone else could get the corner office based on "trust me" versus "show me".

Prediction Five: Codifying intangible reporting practices. The world today has diminished trust in the advice of accountants and stockbrokers. With 90 million Americans dependent directly or indirectly on the stock market for a substantial piece of their retirement future, there is no tolerance left for faulty communication of business information. In this regard the AICPA, SEC and the AARP are fully co-aligned.

Prediction Six: Shareholders will hold management accountable for IP. This stems directly from Prediction Five because once the IP facts are clearly on the page, investors can and will ask the hard questions that ultimately shape corporate activity. It will not be long before an enterprising plaintiff's bar links an adverse IP judgment coloured by a willfulness finding with a drop in share price and an assertion of senior management responsibility.

Prediction Seven: Emergence of IP insurance and risk management. IP insurance products are in their infancy to be sure but their very existence is a bellwether for the future. The mission of insurance is to collect and pay money in relation to life's uncertain events. Insurance from an insurer's point of view works best when premiums paid exceed claims. The fact that insurers can articulate premiums for IP suggests there is the growing body of measurable evidence for the success and failure of these assets.

Prediction Eight: Financial services will invent new products and services that use IP as the collateral asset. Once IP accounts and related

risk can be measured, there are many choices for how it can be bundled and sold. Historically, royalty streams from IP have been sold off for assets ranging from rock'n'roll to pharmaceuticals. Now the IP assets themselves are looking like attractive opportunities for investment through sale and back-licence arrangements. Over US\$100 billion in royalties changing hands each year is compelling evidence of trillions in assets.

Prediction Nine: Registration of intangible property rights will proliferate. In the words of the late rock poet Warren Zevon: "Send lawyers, guns and money". Well at least send lawyers. The ability to finance intangibles directly leads to the question of who owns the IP? Fortunately the legal community has a well established array of methods to articulate ownership. And valuable IP will lead metaphorically to gunfights because the stakes are truly high. Maybe Warren was right all along.

Prediction Ten: Globalisation leads to IP standardisation. The cost to physically move knowledge from country to country is negligible. Knowledge workers in India, China and Russia are picking up assignments once performed by US scientists and engineers. Who will own this knowledge and who can use it will be among the most critical economic issues of the first half of the 21st century. Standardising IP legal rights is central to protect both developed economies willing to export knowledge work and developing economies that must demonstrate they can operate within the rule of law.

Bottom-line, we have transitioned from a manufacturing economy through a service society to an intellectual property based marketplace wherein only the proprietary benefits associated with intangibles provides satisfactory returns to capital and their investors. Whether business will view IP like the weather or a weather machine we will leave for you to forecast or design depending on your point-of-view. It's still good conversation either way.

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