

BUSINESS VALUE FROM KNOWLEDGE MANAGEMENT

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This presentation addresses the question of how KM delivers business value. It also considers the often difficult aspects of justifying an investment in knowledge management, and perhaps more importantly, how you can demonstrate that value.

1. What Is Value?

Today, much of an organization's value is in intangibles – the value of customer relationships, the value of the skills and knowledge of its people, value of information in databases that has resale potential and value from intellectual property, such as patents. The intrinsic value of such intellectual capital is difficult to assess. This is one reason why the accountancy profession who like precision, continue to prepare balance sheets that do little to reflect the true worth of a firm. The realizable value depends on what others will pay. What is the value to you of a glass of water when you are in your home vs. where you are struggling to survive in desert? It also has a time dependency and depends on the perception of the valuer. At one time eToys was valued at more than Toys 'R Us, when its revenues were the equivalent of two stores (Toys 'R Us has over 1,500!). Today eToys is not on the radar screen. Similarly, rights to show football league matches on digital TV had a value of over £150 million in 2000. Today that seems somewhat high. Value is so context dependent.

Unless your primary business is in knowledge products and services, such as media, digital content, consultancy, the main value of knowledge is how it contributes to your business performance and other organizational objectives. Surveys of KM benefits show that increasing revenues, saving costs and improving the customer experience are the main contribution of better knowledge management. Understanding the link between knowledge flows and such business outcomes is therefore at the heart of demonstrating the value of knowledge and of knowledge management.

2. The Business Case for Knowledge Management

Knowledge management can be an expensive business. Investing five per cent of operating costs is not an unusual figure for many knowledge-based businesses. How can investments in particular KM projects that frequently cost £5 million, £10 million or much more, be justified? There are three main perspectives, one or more of which may be appropriate in a given situation:

- Asset perspective: what is the intrinsic value of this information or knowledge?
- Benefits perspective: what benefits accrue from effective utilization of knowledge?
- Cost-effectiveness: what cost saving accrue from better reuse of knowledge?
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Taking the first perspective, there is a whole new field of intellectual capital measurement that is currently evolving. This takes the various component, such as customer capital, human capital and structural capital (that in organizational processes, databases etc.) and intellectual property. What financial figure you put on it depends on your purpose. You may assign a replacement cost value or a perceived market value. There is also a risk value – how much damage would occur to your business if this information got into the hands of your competitors? IC accounting is not straightforward. For example one plus one rarely equals two. There is often more value in a well-honed team than the value attributed to each

individual. Therefore most IC methods use a range of indicators of value and track these year on year, rather than trying to determine an absolute financial number. Skandia insurance company is the pioneer of such methods, but it is slowly catching on as a corporate tool in other organizations as a focus for management attention.

The benefits perspective takes into account the benefits accrue from having the right knowledge in the right place at the right time. Sometimes such benefits, as finding relevant information quickly, are easily quantifiable. More often than not, knowledge workers will say that the time saved was not simply translated into a cost saving but used to better effect, e.g. to develop a sales proposal that had a higher chance of success, or of improving a product design. Ideally, a tool such as a benefits tree is needed to track the cause and effect relationships. However, in most situations this is idealistic rather than realistic.

The third perspective – and these perspectives are closely inter-related – is that of cost effectiveness. Reusing existing knowledge means that “the wheel” does not need to be “reinvented” elsewhere in the business and thus costs can be saved. One example includes Chevron’s savings of over \$100 million in its energy costs through its sharing of best practices. Another is a management consultancy that conservatively estimates that for every productivity boost of 1% their consultants bring in more than £ 50 million in fees. And a knowledge management programme that delivers them the information that they need quickly while working on a client assignment delivers quite a few percentage points in productivity.

Taking these three viewpoints together, it is not too difficult to identify many ways in which better knowledge management delivers value to the business. What proportion of any measurable improvement in business performance can be attributed exclusively to knowledge management, as opposed to the many other initiatives that also probably claiming such improvements, is a moot point.

3. Some Difficulties

Some of the problems of valuing the contribution of knowledge management have already been alluded to: How is the contribution valued? Do different people see the value as different? Which is cause, which is effect? On investigating most organizations more closely, however, it is found that many other investments, particular those that involve infrastructure or are widely diffused, face similar difficulties.

Take one point in particular. Often the human capital of an organization is its most valuable asset. But how well is the value of people measured? What is the business loss if highly knowledgeable workers leave? There are many organizations, especially those in the public sector, who do not accurately account for people’s time against key business activities, projects or customers. Faced with such imprecise baseline how can we possibly measure the impact of a KM programme?

4. Creating Value Through Knowledge Management

There are now many knowledge management case studies that demonstrate the changes and improvements that have been brought about. For many organizations, such activities are relatively straightforward to emulate. However, a more solid foundation for action starts by following this ABC:

- Assessing your baseline – knowing where you are
- Business drivers – understanding the key drivers of business value

- Choosing a focus – analysing where KM activities have the highest payback

There are now several knowledge management assessment tools. People in the organization complete a questionnaire that explores many factors, such as the handling of information, the capturing of tacit knowledge and the readiness of the organizational culture to promote knowledge sharing. Doing such an assessment is one way of checking progress in knowledge management capabilities.

Perhaps more important assessment, is that of the information or knowledge audit. Here the main business processes are analyzed and key knowledge workers interviewed to identify knowledge needs and how well they are being met. Such an audit – that need not be comprehensive but simply representative or focussing on key tasks – typically reveals tremendous duplication of databases and processes to collect information as well as some critical gaps.

Business drivers varies from situation to situation, but some common ones are increased competition, the need to save costs, a growing customer focus, providing a more seamless service to customers, product innovation, and in the UK public sector - eGovernment. Only if a knowledge initiative can show how it responds to these drivers does it deserve to get funding. Understanding these drivers will help you choose which of the knowledge levers will have the most impact.

An analysis of some 100 KM cases, showed that there are a number of recurring levers that are the focus of KM activities. Briefly the seven levers are:

- Customer knowledge – repeatedly cited in surveys as the most important knowledge an organization needs to capture and exploit
- Knowledge-enhanced products and services – adding value by surrounding the product with additional information, such as personal preferences when booking travel
- Knowledge in people – a people-focussed programme that aims to continually increase workforce skills through personal and team development; today e-learning as a delivery vehicle is in vogue
- Organizational memory – knowing what an organization knows, over space and time e.g. sharing best practice from one part of the world to another; recording lessons learned that should be taken account of in similar future situations
- Knowledge in processes – capturing the knowledge of your best professionals and embedding their good practices into the recommended procedures
- Knowledge in relationships – creating forums and other mechanisms to have closer sharing of knowledge with suppliers, customer s and partners
- Knowledge assets – the intellectual capital focus mentioned earlier.

5. Delivering Value

The ability to realize benefits depends crucially on implementation. This is where KM practitioners can learn extensively from each other. Perhaps, the overriding message that comes through again and again is that KM is not simply a technological solution. It is about people, processes and leadership.

To reiterate this point, many of the KM pioneers who have seen their organizations achieve significant benefits, did not have to justify ROI in financial terms. Even today a recent survey showed that around half of KM initiatives were not justified on ROI. The leaders had a clear vision and understood intuitively the contribution of better knowledge management to the

business. As one Chief Knowledge Officer told me “a good anecdotal story goes a lot further in convincing people of the merits of KM than a financial spread sheet”!

Further Reading

Measuring the Value of knowledge, David J Skyrme, Business Intelligence (1998).

Harvesting Experience: Reaping the Benefits of Knowledge, Jan Duffy, ARMA International (1999).

‘New Metrics: Does It All Add Up?’, David Skyrme, chapter 15 in *Knowledge Horizons*, Charles Despres and Daniele Chauvel, Butterworth-Heinemann (2001).

Learning To Fly: Practical Lessons from one of the World’s Leading Knowledge Companies, Chris Collison & Geoff Parcell, Capstone Press (2001).

About The Author

David is a leading international authority on knowledge management on which he speaks and writes regularly. Among his many publications are *Commercializing Knowledge: From e-business to k-business* and *Knowledge Networking: Creating the Collaborative Enterprise* published by Butterworth-Heinemann. His consulting work includes developing corporate KM strategies, conducting KM audits and reviews and running workshops for KM practitioners and senior managers. His clients have included many of the leading knowledge organizations in both the private and public sectors, both in the UK and abroad.