

# **THE CONTRIBUTION OF SKANDIA NAVIGATOR IN INTANGIBLES MEASUREMENTS AN ALBANIAN CASE APPROACH**

**Sulanjaku, Marsel**

“A.Xhuvani” University, Faculty of Economic, Elbasan, Albania

[msulanjaku@gmail.com](mailto:msulanjaku@gmail.com)

## **Abstract**

*The differences between the market and book value, the inadequacy of traditional accounting reporting in performance measurement and management, indicates a not recognized and not reported asset in the balance sheet, the intangible assets. As still there is not a commonly agreed consensus regarding the measurement and reporting of intangible assets by the accounting standards, on the other side the management accounting has made much progress in intangibles measurement for internal reporting by implementing various models for performance measurement using strategic analysis techniques. One of these models, which attempt to measure company performance and intangible asset value, is Skandia Navigator. The purpose of this research paper is to analyze the Skandia Navigator ability in measuring intangible assets and company performance and its implementation and adoption possibilities by Albanian companies. The key findings of the research paper is that the intangible assets models have began to be adopted partially by the Albanian decision makers and by additional training and research in the intangible measurement full implementation of similar models can be successfully adopted. The methodology used in the preparation of this paper will be that of the utilizing the foreign and national literature, and the utilization of interviews with selected business management in Albania interested in intangible asset management and other related parties to fulfill the questions raised by this research.*

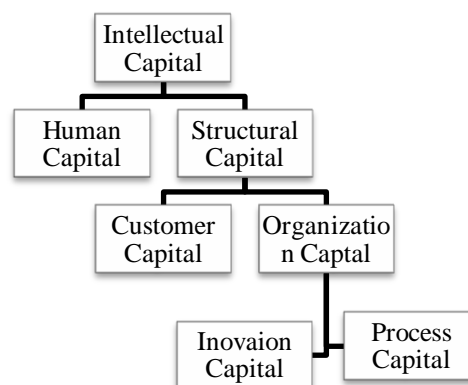
*Keywords: Skandia Navigator, intangible assets, intellectual property, intangibles measurement, performance indicators.*

## INTRODUCTION

Skandia navigator is classified as a non monetary model and was first developed by the author Leif Edvinsson in 1998, while he was corporate director of intellectual capital in a Swedish financial services company called Skandia. He was the first corporate director of intellectual capital in the world, and from then he has become a leading proponent of intellectual capital measurement (D. Andreissen, 2004). During his time he released several supplements in attempt to quantify the company's intellectual property by a model called Navigator. In later released publishing's with the co-author Michael Malone, the authors explains the need to measure the intellectual capital and the how it can be achieved using the Skandia Navigator model. It should be mentioned that in 1998 the author won the award "brain of the year" for the Skandia Navigator model.

Through several components and measurement systems, Skandia Navigator can be used by management as a model that realizes the performance management and the value of the intangibles. The authors argue that traditional accounting does not always respond to the market value and that is because of the value of intangible assets or intellectual capital. The model analysis the intangible assets and its components by dividing it in various components, establishing different measurement systems for each of them. Through the model, management is able to make a connection between company's strategic vision with its objectives serving as a communication and information tool (Roy, S. 1999). Concretely the model divides the intellectual capital into two main components: Human Capital and Structural Capital. Structural Capital is composed of customer capital and innovation and process capital.

Figure 1: IC components



Source: Edvinsson and Malone (1997)

*Human capital*: is the combination of knowledge, knowledge and the employee's skills to adapt to the different requested tasks in the company. *Structural Capital*: is composed of any other intangibles except human capital such as patents, trademarks, copyrights, database, computer software etc.

According to the author the main generator of intangibles is the human capital, which by combining their knowledge, experience, talents and skills is in a continuous transformation of human knowledge into structural capital. Structural capital is more "tangible" compared with human capital and can be used from the company as assets or as tools to generate future incomes. In other words structural capital can be described as everything that remains to the company after the employees goes home (J. Marti, 2012).

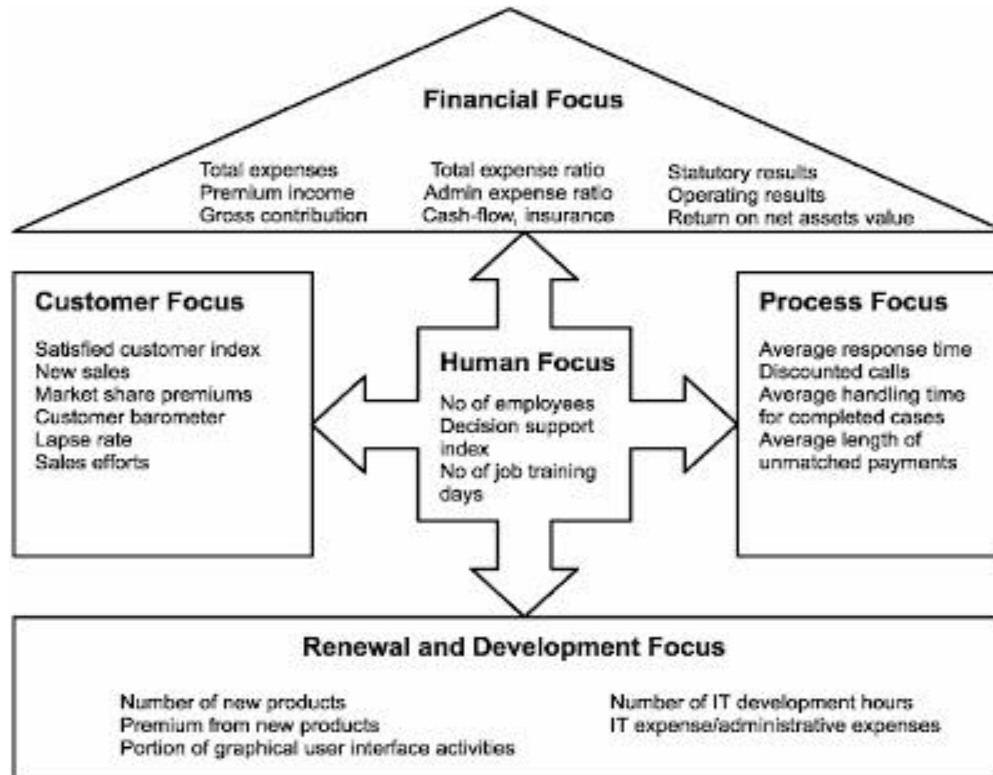
In his studies, L. Edvnisson thinks that the financial statements derived from actual accounting standards do not provide to the managers the needed information to predict or evaluate the company's future financial performance, and its value creating factors. Consequently the usage of financial statements which "hide" the intangibles can result to wrong decision making.

According to the model management should have a "navigator" which can lead them to the right decision making. The Skandia Navigator consider five different perspectives: financial focus, customer focus, process focus, human capital focus and innovation focus. For each perspective the authors L. Edvinsson and Malone, uses four different indicators to measure the performance of each above mentioned perspectives; cumulative (direct measures, generally expressed in monetary forms), competitive (it compares the actual ratios with the sectors ratios), comparative (compares different ratios with similar companies) and combined measures (it combined more than one perspective). The model integrates different measurements such as monetary basis, percentages, and different units by combining them into a general and meaningful framework.

## **COMPONENTS OF SKANDIA NAVIGATOR**

Skandia Navigator describes the elements that contribute in the company performance in five different perspectives or focuses. Intellectual capital resources are often referred to as performance drivers, which suggest causal relationships between these resources and organizational value creation. Intellectual capital resources such as employee skills and customer relationships often deliver customer satisfaction and loyalty, which in turn delivers shareholder value (Low, J., and P. Kalafut. 2002).

Figure 2: Skandia Navigator model



Source: Edvinsson and Malone (1997)

### 1- Financial Focus

It takes in consideration financial results of the company and it is based on all the company's efforts to create monetary value. In difference with other focuses, the financial focus is not future oriented, but pas oriented as it considers past economical transactions (Edvinsson, L. and Malone, M.S. 1997). In the financial focus variables and ratios like; total assets, total assets/employee no. ; Total revenues from the new business operations or new products, hours spend with clients/total labor hours, revenues from new clients/total revenues etc.

### 2- Customer focus

Authors specify that the customer relationship has a key element in a company's perspective and success. The customers should not be considered as a variable outside the company's infrastructure but as an integral part of the company that provides value added to the company. In this perspective the information gathered regarding the customers will be part of the internal reporting .In this focus different perspective are taken in consideration to evaluate the customer focus such as: customer characteristics, incomes, the contact and buying frequency of customers, customers feedback , after sale services etc.

### 3- *Process focus*

At the process focus is considered mainly the technological factors that support the value creation process derived mainly from the human capital, such as; IT systems, databases, working procedures etc. The management of these factors is of a vital importance for the company performance. The process focus has many variables and ratios to be measured such as: administrative expenses/total assets, contract closed without errors, computer no./ employee no., administrative expenses / employee no., no. of IT staff / total staff, expenses on IT / total expenses , % of IT expenses / total expenses etc.

### 4- *Innovation focus*

Innovation focus is the opposing component of financial focus, from time perspective as in difference from financial focus, it is future oriented. Through the innovation focus the management is able to identify the actions that could create new opportunities for an economical growth of the company. Skandia Navigator takes in consideration various elements regarding the innovation focus such as the attractive ability of company for new investors and customers, new products or services that it can develop, strategic partnership , improvement in infrastructure , recruiting of highly skill employees , no. of employees in R&D / total employees, no. of newly developed products, no. of intellectual property assets registered etc.

### 5- *Human capital focus*

According to the authors human capital focus is the most vital elements of intangibles and it is placed in the centre of the Skandia Navigator model, because it is consider as the key source for the other components on intangible assets. In the valuation and measurement of this component factors like leadership index (%),motivation index (%) , education, experience, age, salary , training cost / total cost, total salary / total revenue ratios etc.

According to Skandia Navigator the real capacity of intangibles to create added value is calculated as the production of intangibles coefficient and intangibles total value.

To find the intangible value the authors have selected 21 indicators from the different focuses of the strategy model as above human, financial , customer, process and innovation focus as the most suitable for the valuation. These indicators are such as: investments in new markets, investment in development of new products, revenues from new operations, investments in IT and customer relations, investment in human capital , investments in intellectual property assets etc.

In order to find the intangibles coefficient other indicators, expressed in percentage or ratios are selected from these different focuses to derive a single index.

By the combination of intangibles value and the coefficient of intangibles performances can be derived the “true” value of intangibles and the connection of intangibles with company performance.

From this formula the authors state that the value of intangibles is in function of the company’s performance and the investments in intangibles. Thus comparing two companies with same investments in intangibles the company with higher performance index of intangibles can have a greater value of intangibles. Through this formula the authors can predict the future value of the intangibles or the company performance.

In a first look, the Skandia Navigator has strong similarities with balanced scorecard (Ax, C. and Bjørnenak, T. 2005). In different from balanced scorecard the Skandia Navigator considers the human capital as the most important component of intangibles and in addition it comes with a formula that evaluates the value of intangibles based on their performance, using the performance indicators in form of percentages and ratios.

Skandia Navigator gives an important contribution in the measurement of intangibles and their performance in the overall company performance. The model is accurate for the large number of indicators that it takes in consideration in performing the intangibles value (Petty, R. and Guthrie, J. 2000).

One of the model disadvantages is that it was developed in “tailor suit” for one specific company the Skandia company, and in order to be used in different companies operating in different sectors it should be revised according to specific conditions (Marr, B., Schiuma, G. and Neely, A. 2004). Another main disadvantage of the model is the fact that the model tries to give a single value of intangibles by combining the investment in intangibles with their performance, that in fact is difficult to combine different ratios and percentages of very different sectors in one single coefficient (Daniel Endreissen, 2000).

## **THE CONTRIBUTION OF SKANDIA NAVIGATOR IN INTANGIBLES MEASUREMENT AND MANAGEMENT**

Skandia Navigator is a very important development in the literature of the intangibles’ measurement and management. The Navigation model supports managers in visualizing and developing measures that reflect intangible assets (Skyrme, D. J. 1998). Through the model the management is able to check the relation among different component of intangibles in a very clear way. By setting measures to the different company focuses the final perception is the valuation of the company’s or shareholders value added. The scorecard models for internal reporting; like Skandia Navigator is mostly used, as the accounting standards do not track the value of intangibles.

The main reason why management wants their intangibles to be measured is (1) to help company to create a long term business strategy (2) to develop different performance indicators rather than the financial measures that will contribute to value the management performance (3) to make a connection between the objectives achieved and the performance valuation of different employees working in different positions and (4) to communicate to the interested parties the value of intangibles that , the financial statements cannot represent in their financial statements.

In difference from other scorecard methods the Skandia Navigator has a great contribution in intangible measurement as it present to the users a large scale of measurement systems for intangibles from each perspective. Apart of financial focus, the model has developed very useful tools to derive the performance of intangibles in different focuses, by using a large numbers of ratios and percentages. Even these indicators may be for different specific sectors, the model integrates them into one single indicator. Although the usage of different percentages and indicators in a single coefficient is seen to the models weak point, they can be used even separately to measure intangibles.

Its usage of non-financial data gives the management the perspective to predict company's performance and to be prepared for the challenges that can come from different departments and factors rather than those inside the company. Through the Sandia Navigator the management accountants are becoming more involved in the decision making process, advancing more than the tradition accounting in relation to company's performance management and intangibles valuation.

## **USING SKANDIA NAVIGATOR AS A TOOL FOR INTANGIBLES MEASUREMENT IN ALBANIAN COMPANIES**

Albania is characterized of a vital economy that is following the dynamics and perspectives of new developments in economies of developed countries. Among these developments is the intangible assets valuation and management techniques. A disadvantage of the Albanian economy is its informal economy that still has not significant reduction despite the measures taken from the related institutions, which have a negative impact in the objectivity of the financial statements for external reporting.

The great interest in intangibles is well observed in the continuously increase of registered intellectual property in the related offices as well as the great interest of management in investing in intangibles such as brand names, copyrights, human resources , IT etc.

In the frontier of investments in intangibles of course there are sectors that have made more advances compared to the other sectors. From our interviews with different managers, CPA and other interested parties we observed that sectors like banking, media & entertainment and medical care are in the front line in measuring and manage intangibles. The sectors with high intensity of intangibles are the financial and service sector, and other sectors like bio technology, and hi tech sector are still not developed.

In financial and service oriented companies, the traditional accounting standards does not allow the accountants to fairly report the intangibles (Thomas Stewart, 2001). For this reason the management's attention is shifted towards internal reporting with new models that are based on company's performance management and towards models that are more effective in intangibles measurement. Skandia Navigator is a well known model for the managers and management accountants working in these sectors.

Although well known, the implementation of Skandia Navigator is not an easy task , as it need several steps to be successfully settled such as : creating a strategy for the company to follow, identify the core actions/focuses to be taken in order to realize the settled strategy , for each action/focus a set of measurement indicators should be selected in accordance to the company specifications and at lat but not an easy task is the combination of all these measurement units into a single monetary value for intangibles and a single ratio for the intellectual coefficient. Skandia Navigator is not fully implemented by Albanian companies, but it's ratios and measurement methods are wide used in the internal reporting.

Especially in banks and medical care where human capital and investment in processes like database protection and different investments made in IT we observe that managers despite the financial statements are using reports derived from managements accountants. In this reports different ratios related to customer, human and process focuses are becoming more evident and requested by the managers.

Special interest were observed regarding the analysis of employee training, where the expenses in training are considered in special reports from different perspectives in ratios such as: expenses on training / total expenses, expenses on training / net earnings , total expenses / no. employees.

From IT focus the most preferable measurement and ratios used were: expenses on IT / total expenses, current investments on IT / total investment on IT, expenses on IT / total earnings, expenses on IT / no. of it staff, IT capacities or properties etc.

From the innovation and customer focus a more detailed reports were developed in association with marketing department where reports like market share, no. of customers, customers satisfaction index, days spent visiting customers, no. of customers complain / total



products sold, average time of customers with company, no. of new customer / total customers, revenues from new customers / total revenues, revenues from new products / tot. Revenues, no. of customers / no. of employees in customer services etc.

## CONCLUSIONS AND RECOMMENDATIONS

The investigation of the added value for a company is a critical and very important task that cannot be performed using only financial metrics. Financial metrics is only a part of the elements that contribute to value added for a company, where the other elements are more intangible in their nature, but the effects of them in the company performance are obviously important.

Skandia Navigator is a powerful tool in function of intangibles measurement, as it provides to the managers a wide range of indicators and measurement perspective. The implementation of Skandia Navigator involves 164 metric measures (91 intellectually based such as ratios, percentages etc and 73 traditional measures) expanded in five different focuses (Suliman Al-Hawamdeh, 2003). The wide range of metric measures that the model introduces makes this model very popular and helpful for the Albanian managers and accountants who are interested in intangible measurement as well as in the performance management.

Albanian management is becoming more aware of the intangibles management and measurement. Although for above cited limitations that the Albanian economy is characterized, full model implementation regarding the intangibles still is not present. On the other hand partial implementation or usage of the scorecard methods is very popular and common for the management and management accountants. The scorecard models like Skandia Navigator are contributing significantly to help Albanian management measure the intangible assets and the company performance.

We are of thought that further training regarding the intangible measurement and company performance management should be conducted to increase the intangible's reporting awareness among the Albanian accountant.

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