

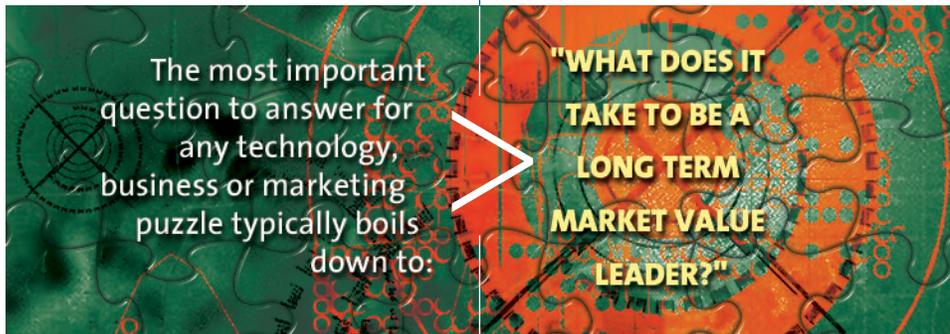
PUZZLE OF THE MONTH

Benchmarking

In the October issue of *Breakthroughs in Knowledge Management* we said: "Defining the puzzle to be solved and describing the Knowledge Blocks needed to solve the puzzle should always be the first thing to do."

The Puzzle

Fifteen years ago, a company entered a US market that both Federal and State authorities said was strategic to the long term interests of the United States. As an inducement,



economic incentives were offered to jump start new businesses.

This year, because these economic incentives would soon cease, the company decided to update its competitive intelligence, compare its manufacturing cost with leading competitors and determine best practice manufacturing cost. They believed that a cost reduction program would be required and wanted a best practices cost target.

Benchmarking should answer a number of questions, the most important of which is how to achieve optimum market value. Cost benchmarking alone cannot provide the complete answer.

The company needs to know how to make its business the market value leader even without external economic incentives. Even if this wasn't done when the company launched its business, the long term viability of a business should always be known. Market value includes properties and market influence as well as economic value.

Two Knowledge Blocks are required to solve this month's puzzle –

1. An Economic Value Knowledge Block that not only evaluates the best practices of all competitors but also details the optimum economic value that must be offered when the market matures.

2. A Market Value Knowledge Block that proves that the market value offering is sufficient to sustain market growth, even without economic incentives.

The most important question to answer

for any technology, business or marketing puzzle typically boils down to: "What does it take to be a long term market value leader?"

Since this puzzle concerns revitalizing an existing business, an Extend® Program is recommended.

The Solution: KVC's Extend® Program

KVC's Extend® Program provides step-by-step direction and training to enable business teams to create all of the knowledge blocks they need to increase the growth and profitability of their business.

The focus is always on what it takes to achieve and/or maintain long term market value leadership.

Extend Programs can be accomplished in phases. Once a knowledge block is created, it's never lost. Other knowledge blocks can be added at a pace that takes into consideration your company's ability to absorb change. ■

"When cost benchmarking is suggested, think about how economic value relates to market value."

The Economic Value Knowledge Block includes a simple ratio (ECORAT) of end-product cost -to- customer goal status, quantification of the market value chain's profit pool and calculations to determine the economic value contributed by each player in the market value chain. ECORAT is the economic variable used to calculate market value.

$$\text{ECORAT} = \text{ISUM Cost} \div \text{Goal Status}$$

The *numerator* is the customer's detailed cost picture, which shows the variable and fixed costs associated with the manufacture, sale and distribution of products and services.

The *denominator* deals with the customer's goals and objectives. The customer's aim is to achieve the best economic ratio for its own business. This is achieved either by improving the numerator (company's cost of products and services) or by improving the denominator (enabling the company to achieve its goals and objectives).

Economic ratios start off at a certain level, say 2.0 or higher and typically improve to < 1.0, as the market matures.

Cost benchmarking is only one piece of a market value analysis. It must be remembered that players in a market value chain frequently trade off properties and economic value to maximize their profitability, while also doing what is required to protect their market value position.

For an immediate analysis of a specific puzzle, email your request to info@kestingventures.com. ■

A Case Snippet: What can be learned from Economic Value and Market Value Knowledge Blocks?

A Division President commissioned a benchmarking study for a business like the one described in this month's puzzle. Cost benchmarking compares top players with best practices. The chart below is part of an Economic Value Knowledge Block. Note that it also shows 'optimum cost', which is the key difference of KVC's ISUM Competitive Intelligence System. Optimum cost takes into



consideration the theoretical limits of process technology. KVC's ISUM Competitive Intelligence Systems facilitates the comparison of different technologies.

Cost Comparison

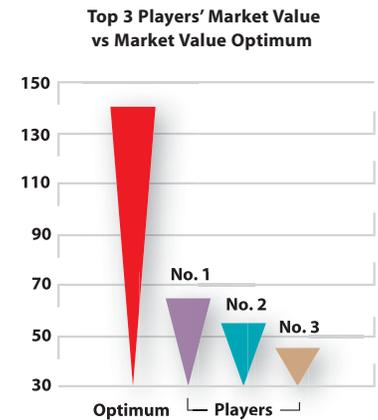
This cost chart (left) shows that best practices are NOT a meaningful cost standard. In fact, the company would probably have exited this business if best current practices were all that could be achieved.

Market Value Comparison

The chart at right compares the market value offering of the top three players with the market value optimum that is really wanted by the market. The market value metric is produced by a three dimensional model linking properties together with economic value and marketing influence. It is clear the top players' offerings are nowhere near optimum value.

A detailed discussion of market value is beyond the scope of a newsletter. However, these simple market value charts reveal a few salient points that prove the importance of market value knowledge –

1) KVC's work in numerous markets during the past twenty years leads us to expect that the leading players in this type of specialized market example ought to offer a market value



of 90 to 95 versus a market value optimum of about 110. The fact that the leading players in this market only offer a market value of 45 to 65 versus a market value optimum of 140 is unexpected.

2) It is apparent that a breakthrough is called for and that none of the current players have identified the breakthrough.

3) Clearly, a cost reduction program to reach best practices cost will not be enough to help this company. **However, a KVC Extend® Program could reveal how to attain optimum market value – and potentially explode this market. ■**

breakthroughs
in knowledge management

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About Kesting Ventures

Since 1984, the mission of Kesting Ventures Corp. has been to develop, improve, record and facilitate the problem-solving methodology required by R&D, marketing and commercial development specialists.

The powerful problem-solving methodology of Experiential Modeling embodied in KVC's Extend® and Start® Programs enable your organization to form specific operational plans for entire businesses, envision and then invent new products and technologies – even renew the growth of existing businesses.

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On Stephen Wolfram's "A New Kind of Science"

DR. WOLFRAM'S best-selling book "A New Kind of Science" validates the methodologies behind KVC's Market Value System.

His basic theorem is that all of the complexity in nature is the result of systems that started from simple initial conditions; however, over time the interactions of these simple conditions become highly complex.

He believes that to understand what is going on in markets one needs a basic model for the operation and interaction of a large number of entities. He shows that it is possible to generate complex behavior by starting from simple initial conditions and then following simple sets of rules.

However, if one starts from some particular piece of behavior, such as current market dynamics, there are no such simple rules that allow one to go backwards and find out how this behavior evolved. He says to effectively study a market, one should begin with a simple market model that is capable of

surfacing a complex picture.

Dr. Wolfram observes that it is a good sign if the model is simple, yet still manages to reproduce a large number of features of a particular system. And it is an even better sign if a fair fraction of these features are ones that were not known, or at least not explicitly considered, when the model was first constructed.

This month's case snippet shows that a simple three-dimensional market value model surfaced an unexpected complete picture that pointed the way to long term success.

Please visit the Literature section of our website, www.kestingventures.com and download a PowerPoint presentation about KVC's "ISUM Competitive Intelligence System." ■

Dr. Stephen Wolfram was educated at Eton, Oxford, and Caltech. He received a Ph.D. in theoretical physics in 1979 at the age of 20. He was R&D Magazine's 2002 Research Scientist of the Year, and is the developer of the Mathematica Series of computer programs in use by over two million people worldwide.