Enhancing profitability WITH INTELLECTUAL PROPERTY

By **Lindsay Moore,** PhD

Companies that possess proprietary formulations, trade secrets, unique manufacturing processes or patents may be leaving money on the table that could bolster their profitability or deliver enhanced earnings per share, while also strengthening their competitive advantages.

'Portfolio mining,' an intellectual-property strategy widely practiced in other industries, could be deployed by supplements and functional-foods manufacturers to deliver *free cash flow* to their bottom lines.

Intellectual property (IP) is usually obtained to deliver competitive advantage to its holder. While that is the primary purpose for obtaining IP, that same IP also can be used simultaneously to create new streams of high-margin revenue that can fall to the bottom line without being burdened by traditional P&L expenses.

The theory of portfolio mining is to accumulate intellectual property and then slice and dice it into elements that can be licensed, alone or in combination, to other enterprises in exchange for licensing fees and streams of royalty income. Deploying IP for more than one purpose at the same time increases asset leverage and enhances the return on the respective asset.

Portfolio mining was originally developed by IBM during the early 1990s when it realized that its vast patent holdings were underleveraged in being used just for IBM's technological purposes. Many of its patents also could be licensed in part or whole to other companies in return for royalties that would enhance its return on assets. Thus began a program that boosted patent-licensing royalties at IBM from $30 million a year in 1990 to more than $2 billion in 2005! To match that sort of net cash flow, IBM would have to sell $40 billion worth of additional or new products – a difficult feat for a $96 billion company.

Even companies with small IP portfolios can learn to leverage their holdings into the free cash flow of licensing income by parsing their IP holdings, and finding those enterprise partners who can benefit from their IP without undermining their own competitive advantage. The trick lies in shifting the mindset surrounding IP to recognize that even the individual pieces of intellectual property, such as specific patent claims or portions of trade secrets, can be of immense value to other companies in other markets and industries, and can be licensed even to competitors without harming either the licensors' competitive advantage or their financial performance.

Even companies with small IP portfolios can leverage their holdings into the free cash flow of licensing income by parsing their IP holdings

Companies with unique product formulations that sell their products in grocery, mass and drug, can license selected IP, with certain restrictions, to enterprises that play within other nonstrategic channels of trade such as institutional, military or government. Manufacturers with unique manufacturing processes or specialized techniques that prevent, for example, the loss of volatile oils or active ingredients in manufacturing processes can license their patent-protected processes to emerging market players in pharmaceuticals and medicine to create and profit from innovative products in entirely different industries.

Similarly, players can license even highly proprietary formulations to businesses located in foreign countries and far-flung markets where they would never distribute their products, and thus profit from previously unavailable market penetration opportunities. Imaginative businesses can create appropriately modified versions of their most successful proprietary holdings, and then license them directly to competitors to fill consumer niches that would otherwise undermine the licensor's brand position.

Years ago 'intellectual property' wasn't even in the strategic lexicon of CEOs and corporate executives. Indeed, to this day, most executives still think that IP is merely a legal matter that is unrelated to the truly strategic thinking of competitive advantage. However, for those who can think in a new way, strategies like patent mining can provide a 360-degree deployment of intangible corporate assets, and can change the fortunes of companies with low profit margins by enhancing their profitability with consolidated streams of royalty income, supplementing and fuelling the natural growth of their enterprise.

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