

## Chapter 6

# Managing SOEs for Improved Performance

by Irv Beiman

### STRATEGY MANAGEMENT SURVEY

In 2006, eGate Consulting conducted a survey of organizations in the People's Republic of China (PRC). Survey respondents were queried on the most important business challenge facing companies in the PRC. Chinese managers cited “strategic management” as the most significant business challenge. Strategic management includes all phases of strategic planning, execution, and evaluation. Based on the survey results, eGate identified three important lessons:

- Strategy management is the biggest challenge for all types of organizations in the PRC, both state-owned enterprises (SOEs) and private companies;
- Establishing a clear, repeated, and ongoing strategy management process more than doubles the chances of becoming a winner in the PRC; and
- Implementing a balanced scorecard (BSC) helps companies establish clear strategies that, when used effectively, serve as a foundation for an effective strategy management process.

During August of 2006, all types of companies in the PRC were surveyed on 10 different areas of business challenges. Of the 105 usable responses received, slightly less than half of the organizations were state-owned or private enterprises; the other half of respondents were joint ventures or wholly foreign-owned. Of the 10 different challenges evaluated on a 5-point rating scale, only one (strategy management) was rated above 4.5 in importance. Strategy

management was rated as the most important challenge (4.57 on a 5-point scale) facing all types of organizations, including SOEs. This was an important first conclusion from the survey.

The survey revealed that more than half of organizational respondents reported not having any process in place for managing strategy. One half of this group indicated they had no strategy execution or formulation process in place, while the other half reported they were using a process for *formulating* strategy, but did not have a process for execution.

The second conclusion arising from the survey was based on the following results. Only 17% of respondents indicated they had an effective, clear, repeated, and ongoing strategy management process. For this group of companies, more than 80% of them reported being “winners”— they were performing either better than competitors or had achieved breakthrough results. Of the remaining 83% of respondents who indicated they did not have a clear, repeated, and ongoing strategy management process in place, only 42% reported they were “winners”. Thus, putting in a clear, repeated, and ongoing strategy management process doubles a company’s chances for becoming a winner in the PRC. This is true whether the company is an SOE, privately-owned, or a wholly owned joint venture enterprise.

A comprehensive implementation of the BSC Methodology enables three important pieces of strategy management: description of the strategy, execution of the strategy (or strategic plan) and evaluation of strategic results.

The third conclusion from the survey was based on the following results. Slightly less than one third (31%) of companies reported they had implemented any sort of BSC. One third of those that had implemented a BSC reported having a clear and ongoing strategy management process in place. Another third reported they had formulation and execution in place, plus some sort of evaluation, but were not evaluating strategic results regularly. The final third lacked either execution or evaluation, or both. eGate interpreted this to mean the following: BSC can help improve results but it must be deployed in a manner that establishes a clear, repeatable, and ongoing strategy management process.

A comprehensive implementation of the balanced scorecard methodology enables three important pieces of strategy management: description of the strategy, execution of the strategy (or strategic plan), and evaluation of strategic results

It is noteworthy that one of the key Process Objectives in the SASAC Strategy Map reported in Chapter 4 of this book is Establishing a Strategy Management Process. This objective is consistent with the survey on how to become a “winner” in the PRC.

The strategy management survey reports, in combination with the SASAC strategy map, highlight a key issue for SOE awareness and action: “business as usual” is not sufficient. An important first step toward establishing a strategic management process is to adopt the BSC framework and approach to management. Once the BSC is adopted, the strategic management process can be expanded into a repeatable, clear, and ongoing process that includes updating the BSC periodically to adjust to changing business and competitive conditions.

### STRATEGY MANAGEMENT PROCESS: DESCRIBE, MEASURE, ALIGN, AND MANAGE

What can SOEs do to improve their performance and better achieve their strategic objectives? Research has been conducted over the last 15 years to identify the principles, tools, and best practices for executing strategy. These have been derived from more than 80 organizations that have been awarded the Balanced Scorecard *Hall of Fame for Executing Strategy*<sup>TM,52</sup>. This award recognizes organizations that have achieved breakthrough results using the BSC Methodology. The best practices by Hall of Fame companies have been adapted for the PRC and are being applied now by such Chinese organizations as Bao Steel (and Bao HQ), China Union Pay, China Resources, Qingdao Beer, and CATIC (China Aero-Technology Import & Export Corporation).

This methodology has evolved continuously, such that it is now the accepted global and PRC standard for best practices in strategy execution. Five Principles and 27 global best practices have been adapted for accomplishing four primary strategic management

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<sup>52</sup> See [www.bscol.com](http://www.bscol.com) for information about the Balanced Scorecard Hall of Fame for Executing Strategy<sup>TM</sup>. See [www.egate-china.com](http://www.egate-china.com) for information about the PRC's Hall of Fame for Strategy Focused Organizations.

objectives in the PRC: describe, measure, align, and manage the strategy.

The better-designed balanced scorecards illustrate a good balance between financial and nonfinancial metrics, between short- and long-term objectives, and between leading and lagging indicators of strategic success

1. **Describe the Strategy** is accomplished via an innovative tool developed by Dr. Robert Kaplan and Dr. David Norton of Palladium and the Balanced Scorecard Collaborative—a *Strategy Map*. A typical Strategy Map is a one-page, graphic illustration of strategic objectives in four primary perspectives: financial, customer, process, and learning and growth. Strategy Maps are powerful tools for clearly communicating throughout an organization, as well as serving as a catalyst and reference point for a well-managed change process. Some strategy maps show cause-and-effect relationships between different objectives. This describes the business logic of the strategy for success.
2. **Measure the Strategy** is accomplished via a BSC with objectives, measures, targets, and initiatives (action plans) for achieving the desired results. Many managers may think they are using best practice just because they have performance objectives and measures or key performance indicators (KPIs) organized into the four typical perspectives identified above. KPI systems typically reinforce “silo focus” rather than the more holistic “enterprise strategy”. A well-designed BSC must be properly developed. The better-designed BSCs illustrate a good balance between financial and nonfinancial metrics, between short- and long-term objectives, and between leading and lagging indicators of strategic success. Consider the issue of safety. Safety is a common objective area in the process perspective for companies engaged in hazardous activities (mining industry) or dealing with hazardous materials (chemical industry). This might appear as a single objective, or as a broader theme to include meeting regulatory requirements for hazardous materials. The number of safety incidents is a common measure for this objective. Some companies measure not only the number, but also the severity of such incidents.
3. **Establish and Sustain Vertical and Horizontal Alignment** by cascading strategic objectives vertically throughout the organizational structure. During the vertical cascade process

for a holding company, conglomerate, or single enterprise, consideration of horizontal alignment issues is critical. Cross-functional needs of commercial and support organizations can be identified in a horizontal alignment needs survey.<sup>53</sup> The BSC Methodology can be used to track and resolve critical alignment issues for strategy execution success.<sup>54</sup> Improving organizational alignment is a highly important strategic management issue for organizations anywhere in the world. This is even more important in Asian cultures that are hierarchically oriented, as well as in national economies that are in transition from central planning to greater market sensitivity. Each of the four cases described later in this chapter paid specific attention to establishing vertical and horizontal alignment.

4. **Manage the Strategy** by linking it to critical systems and processes, such as budgeting, human resources, and IT. Management should conduct strategic review meetings that build the competency for strategy execution. Well-run strategic review meetings create *real-time learning and development*, by combining the best of different opinions into a shared, consolidated view of important challenges and how to cope with them.

Improving organizational alignment is a highly important strategic management issue for organizations anywhere in the world

### THREE PRC SOE CASES OF BALANCED SCORECARD DEPLOYMENT FOR STRATEGY MANAGEMENT

This section presents descriptions of three case projects delivered by eGate that describe how SOEs in the PRC are using BSC tools to put a strategy management process in place. Each of these cases is in a different industry. Each organization was facing different internal and external business conditions at the time that SOE executives chose to investigate and deploy the BSC as a tool for

<sup>53</sup> eGate has developed a horizontal needs survey appropriate for SOEs. Some form of this survey was used in each of the SOE cases described in this chapter.

<sup>54</sup> Kaplan, R., and David Norton. 2006. *Alignment: Using the Balanced Scorecard to Create Corporate Synergies*. Boston: Harvard Business School Press. Go to [www.egate-china.com](http://www.egate-china.com) to learn where to purchase the Chinese language translation of this excellent book.

strategy management. These cases illustrate how the fundamental principles, practices, and tools of the BSC Methodology can be deployed in all types of SOEs.

### **PRC Balanced Scorecard Deployment Case 1: An Internationally Recognized Beverage Company**

The PRC is the largest beverage market in the world, with an average predicted annual increase of ~6% over the next few years. There is significant potential for market growth. Many international brands have sought to gain a piece of this market, with a number of them failing and pulling out of PRC operations. The beverage market in the PRC is intensely competitive.

ChinaBev is a well-recognized Chinese SOE beverage company in many locations around the world. GlobalBev, a major international player in the beverage industry, had taken a minority share in the Chinese organization. ChinaBev had a base of more than 20,000 employees, with revenue in excess of \$1 billion.

ChinaBev was facing challenges from both external competition and the need to improve internal management and utilization of productive capacity. Key executives recognized the company needed to improve clarity and focus on executing a winning competitive strategy. The CEO of ChinaBev decided to implement an initial BSC project involving corporate headquarters, one strategic business unit (SBU), plus several plants, sales organizations, and functional departments. The company spent about a half year designing and implementing the BSC Methodology in these units with consulting support and training.

An initial demand analysis identified key business needs and horizontal alignment issues. This information and analysis was incorporated into subsequent workshops that developed corporate and unit Strategy Maps and BSCs. A simple BSC tracking and reporting system was used to report on strategic performance at different organizational levels.

The BSC core team members were developed into serving as internal consultants for BSC implementation. They expanded the implementation process to include significantly more sales

organizations and production plants. The corporate and SBU Strategy Maps and BSCs were cascaded down to functional departments in multiple business units. The core team estimated that in the year following the BSC implementation, profit improved by approximately 20% on a revenue increase of approximately 2%.

Consider the words of ChinaBev's CEO:

*“Beginning our balanced scorecard project took a big stone away from my heart because when we formulated our strategy clearly, we learned how to turn it into action. We learned how to have everyone in our company understand our strategy and to execute our strategy. Importantly, we learned what actions needed to be taken to accomplish our strategy and how to probably use and implement our strategic measures and objectives. As a result, our organizational structure and process optimization are based on our newly clarified corporate strategy. And, we are not done. Every working day our employees are busy implementing our company strategy and employee moral and satisfaction has improved because workers feel more involved, valuable, and important.*

*Using the balanced scorecard methodology for communication enables us to make strategic thinking more real, visual, and practical. We had some strategic thinkers before, but now our employees understand how to execute strategy. Now our top management team knows how to manage the strategy, and how to execute company strategy through our management system.”*

*“Using the balanced scorecard methodology for communication enables us to make strategic thinking more real, visual, and practical”*

### **PRC Balanced Scorecard Deployment Case 2: An Internationally Competitive Industrial Company**

IndustryCo was a public company with more than 15,000 employees at the time of its BSC project. It was a member of the Global Fortune 500 and ranked as the third most competitive company globally in its industry. IndustryCo exports its products to more than 30 countries around the world.

During the past several years, IndustryCo had successfully implemented a series of manufacturing and quality projects,

including enterprise resource planning (ERP), process reengineering, and Six Sigma. Company leaders recognized the need for an effective strategy management methodology to exploit these operational improvements and improve their strategic success. A key functional department focusing on innovation was assigned the mission of exploring the BSC as a useful approach to meeting their strategy execution needs and to evaluate possible suppliers for a project.

After an extensive supplier evaluation process, eGate Consulting was selected to support IndustryCo in deploying the BSC Methodology.

The initial project scope included more than 30 functional, manufacturing, and business units, with the charter to develop a Strategy Map and the BSC for each of these units. Considerable effort was devoted not only to establishing vertical alignment from the enterprise map to each of the second-level unit maps, but also to establishing horizontal alignment across these second-level units. Multiple sessions with unit representatives were conducted to identify shared and contributory objectives for each unit.

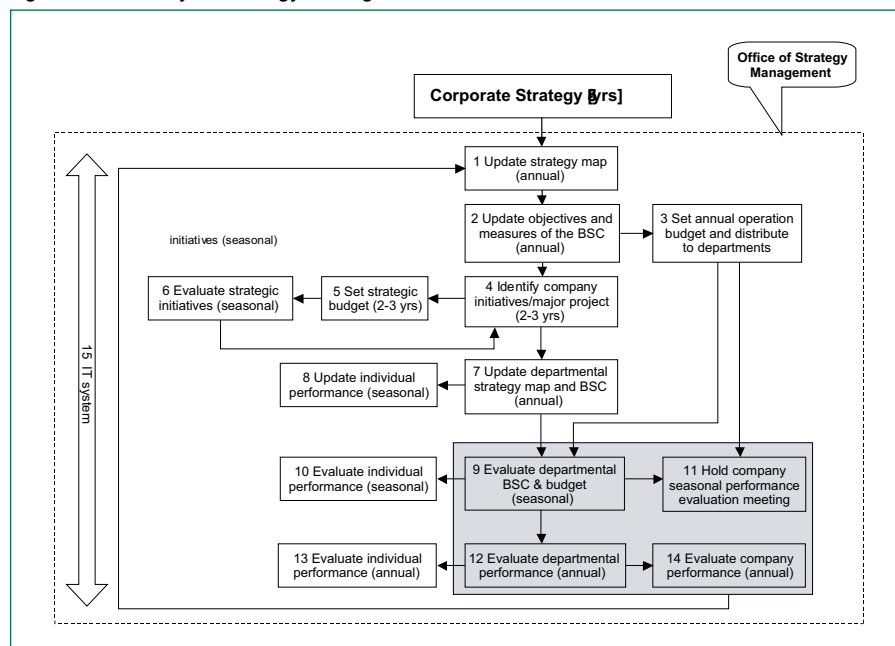
Before the BSC design and implementation, each of these units had established its own annual objectives and measures, with no holistic view of the enterprise strategy for success. The BSC Methodology surfaced critical alignment issues in both vertical and horizontal arenas. The previous performance evaluation system was replaced with one based on unit BSCs. The project team recommended establishing a linkage between the BSCs and other management processes (strategic planning and individual performance management), plus using the BSCs to identify critical Six Sigma projects.

As the project neared completion, company executives decided to implement a major change in organizational structure. The project's executive sponsor was promoted to a higher position in the reorganized conglomerate holding company. He recommended more extensive participation by executive leaders, as well as expansion of the methodology to associated subsidiary enterprises owned by the reorganized conglomerate.

At the time of this writing, IndustryCo had elected to expand the BSC Methodology to its reorganized headquarters and to several

associated subsidiary enterprises, each with more than 15,000 employees. IndustryCo also chose to provide initial BSC training to the management teams of recently acquired multiple enterprises. IndustryCo headquarters and subsidiary enterprises are beginning to use a consistent strategy management process based on tools, such as strategy maps and BSCs. See Figure 14 for an illustration of the draft strategy management process at IndustryCo.

Figure 14: IndustryCo Strategy Management Process



Source: eGate

### PRC Balanced Scorecard Deployment Case 3: A Dominant Financial Services SOE Facing International Competition

FinancialCo provides a wide variety of financial services in the PRC. During the previous 3 years, FinancialCo had experienced rapid growth and had defined its vision of becoming a recognized major global provider of financial services by 2010. The company

had formulated a clear, long-term strategy that included shifting focus from technical service delivery to increased and improved customer service. FinancialCo executives recognized they needed to develop an internal competency for managing this change and executing their new strategy.

By the end of 2006, financial services in the PRC were scheduled by WTO to begin opening up for foreign players. This schedule of market opening included several major competitors of FinancialCo. FinancialCo executives recognized they needed to prepare to compete with mature international organizations on product and service, as well as internal management and human capital. In this strategic context, FinancialCo executives reported a strong sense of urgency for improving internal management capability, including the related areas of organizational structure, business process, performance management and, most importantly, strategy execution.

FinancialCo executives kicked off the strategy management project with consulting support throughout 2006. Project scope included a corporate Strategy Map and BSC, plus the same for 23 departmental units (including one branch company), and 60 individual scorecards for pilot evaluation and learning.

The top executive team demonstrated strong, visible support for this strategy execution project. They were in frequent communication with the project team, who brought implementation issues to them. This open and transparent communication process served to identify hurdles and develop ideas for solutions, as well as stimulate decision making for overcoming the challenges identified.

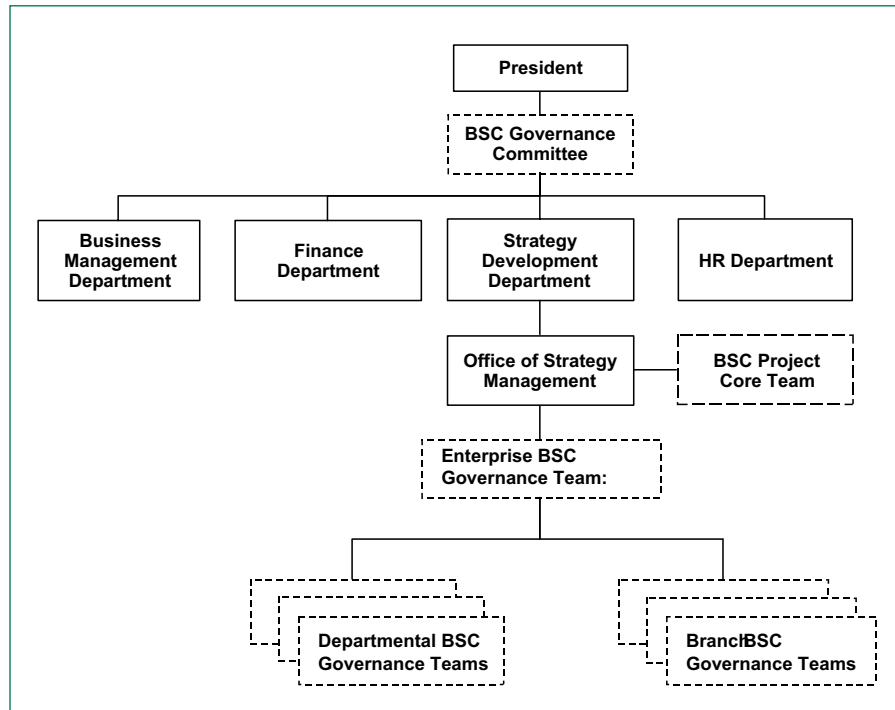
The BSC project was run in parallel with related high-level initiatives for restructuring and reengineering. Both of these latter projects were initiated with the explicit charter to support FinancialCo's long-term strategy, with the definition of that strategy described by the FinancialCo corporate strategy map. The process reengineering project included the objective of better defining cross-functional processes and responsibilities. Some team members participated in both the BSC and the reengineering projects. Both teams appeared to work well together, in part, because of the visible support and interest by top executives.

FinancialCo decided to form an initial BSC governance structure making use of an Office of Strategy Management (OSM). The OSM is the latest innovation emerging from the case research and innovative practices of Palladium and the BSC Collaborative. The OSM has been adapted for use in the PRC. This innovation is particularly useful in Asian countries that are hierarchically oriented, such as the PRC. It is common for Chinese organizations to use structural change as a lever for attempting to create organizational improvement. Reorganizing complex organizations is not sufficient by itself to create sustainable organizational improvement.

The OSM, however, is an innovative revision of what might be called the restructuring hypothesis, which includes the notion that changing the organizational structure will change some (or many) of the problems interfering with success. Rather than focus on structure per se, the OSM provides a visible and powerful means to create a revision in the organizational structure to clarify roles and responsibilities for strategy management. The OSM creates a focus on the strategy management process. The ongoing process of continuous improvement in strategy management has the potential to create sustainable organizational improvement and improved business results.

As the FinancialCo BSC project neared completion, executives reported their recognition of the need to establish an enduring unit to manage the strategy execution function relying on the BSC as a primary tool. Executives planned for the FinancialCo Office of Strategy Management to be formed under the existing department for Strategy Development. The OSM was chartered with the mission of driving future strategy execution at FinancialCo. Figure 15 illustrates FinancialCo's organizational structure for enterprise governance using the BSC.

Figure 15: FinancialCo Balanced Scorecard Governance Structure



Source: eGate

### AWARD-WINNING CASE: PRC RESOURCES MICROELECTRONICS – FIRST CHINA WINNER OF THE BSC HALL OF FAME

China Resources (CRC) is one of the leading conglomerates in Hong Kong and the Chinese mainland, with assets of approximately \$13 billion (~ HK\$100 billion). The conglomerate is often heralded in the PRC as an example of modern management. CRC's core businesses include three primary areas: manufacturing and distribution of consumer goods, property, and infrastructure and utilities. These core businesses are divided into 24 profit centers.

The corporate Chief Financial Officer sought to combine an improved use of the BSC with CRC's internal 6S management system (6 systems that were not in alignment) in a project with one of their subsidiary holding companies—China Resources

Microelectronics (CR-M). CR-M is also a holding company with multiple subsidiaries (SBUs) under its strategic umbrella. CR-M has an integrated supply chain within the organizational structure of its holding company (see Figure 16).

In 2005, CR-M had approximately \$487 million (~ CNY4 billion) in total assets and sales of more than \$244 million (~ CNY2 billion). With a focus on consumer electronics, CR-M engages in design, wafer manufacturing/processing, testing, and assembly of semiconductor products, with a focus on integrated circuits and discrete devices. CR-M seeks to deliver the best price and best quality to the PRC market in key product categories. Company strategy aimed to put chips into every Chinese household, with aggressive growth over the next 3 years.

The CR-M BSC project was supported by eGate and involved three levels: one profit center, six SBUs with six associated functional support units, plus a total of 22 departments from two of the SBUs, for a total of 35 organizational units. Each unit at each level worked with a project team and consultants from eGate to develop a strategy map and BSC.

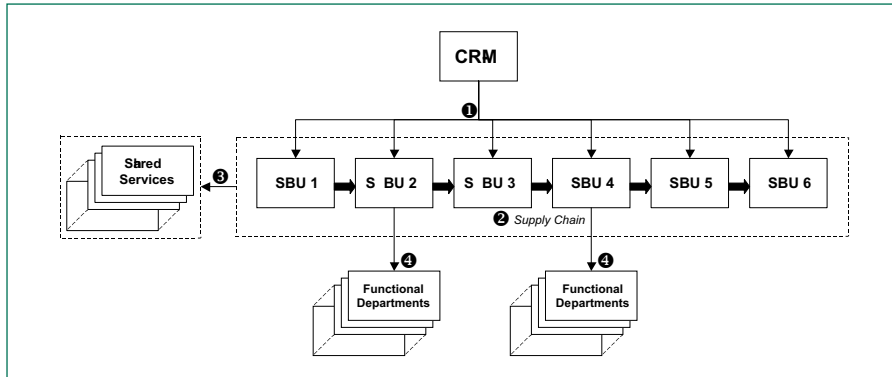
The six SBUs were connected in direct internal supply or support for an integrated supply chain under the microelectronics holding company umbrella. Interviews, discussions, and workshops were held to identify key vertical and horizontal alignment objectives that were consistent with the CR-M business strategy. Strategy maps and BSCs evolved through multiple iterations to reflect the thinking and input from executives at both the CR-M enterprise and SBU level. Two of the key focuses of discussion were the internal supply chain and allocation of resources for new product development.

The corporate CFO and CEO of CR-M planned to establish an Office of Strategy Management to oversee the entire process and assure sustainable linkage with CRC's 6S management system. See Figure 16 for a simplified illustration of the BSC structure and key alignment linkages at three different levels.

In September 2006, CR-M became the first Chinese organization to win the Balanced Scorecard Hall of Fame for Executing Strategy™. Dr. Robert Kaplan gave two leaders of the BSC project team the award in a ceremony during the Asia Summit

Strategy Maps and Balanced Scorecards evolved through multiple iterations to reflect the thinking and input from executives at both the CR-M enterprise and SBU level

Figure 16: China Resources Microelectronics Balanced Scorecard Structure and Alignment



Source: eGate

for Strategy Execution. The application process required extensive documentation of how CR-M applied the principles and best practices of Strategy Focused Organizations to achieve breakthrough results.

#### CR-M Financial Results (3-5 years)

- Total Assets: 10x increase
- Turnover: 7x increase, to HK\$1.45 billion, with compound annual growth of 72%
- Output per Employee: 97% increase, with compound annual productivity improvement of 18%
- Operating Profit: compound annual growth rate of 70% (since 2003)
- Inventory Turnover: improved from 1.62 in 2001 to 3.69 in 2005, with compound annual improvement of 23%

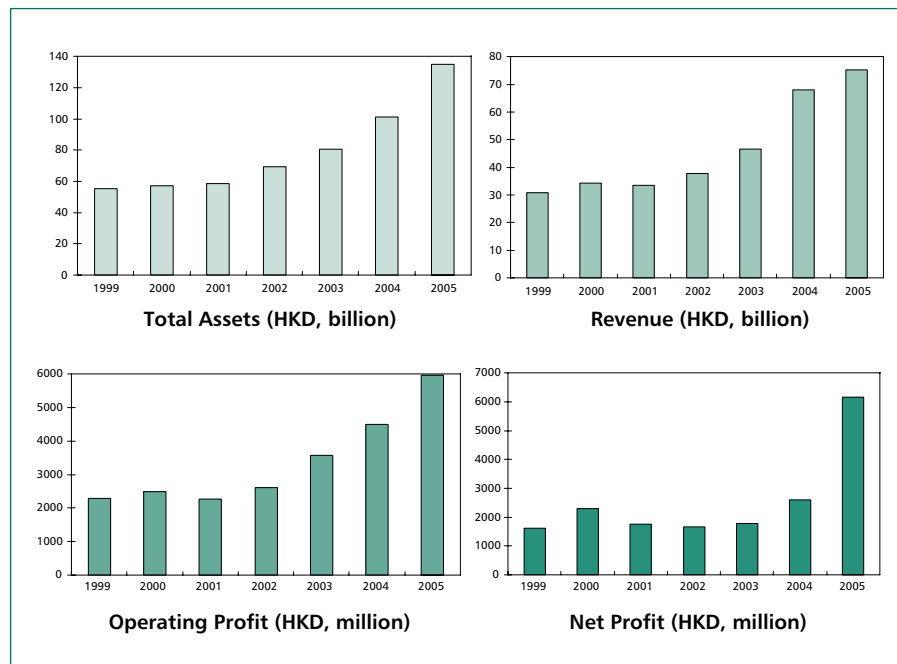
#### CR-M Nonfinancial Results (3 years)

- Customer Satisfaction rating improved from 72% to 81%
- Product Yield improved from 72% to 97%
- Effectively refocused on target customers, moving from lower-end domestic market to serving a group of customers that were more global, larger, and with better credit rating and more stable recurring orders

- Improved cooperation with more synergy and efficiency across CRC's other business units
- Achieved Top 100 Electronic Enterprise for Quality in the PRC (*Ministry of Information Industry* - June 2005/2006)
- CRHM,CRSM,CRMAT recognized CR-M as a Top 10 enterprise in their respective fields in 2004 (*China Semiconductor Industry Association*, March 2005)
- Wang Guoping, GM of CR-M, was awarded Industry Leader of Chinese Semiconductor Industry from 2003 to 2005 (*China Electronics News* Feb 2004/2006).

It is interesting to note that the China Resources (CRC) holding company parent of CR-M had been using the BSC in some form since 1999. CRC's results are quite impressive (see Figure 17).

Figure 17: China Resources Corporation Breakthrough Results



Source: eGate

The four case studies described in this chapter illustrate how different types of SOEs—operating under different business conditions—have applied strategy maps, BSCs, and cascading to manage strategy and improve alignment. SOEs can use these tools to create improved performance, increase shareholder value, and achieve profitable growth.

The CRC holding company performance data, as well as the CR-M case study, demonstrate that truly dramatic breakthrough results are possible when the BSC tools are effectively applied by SOEs in a logical, rational, and effective strategy management process.