High Performance Business in China 2007

In Pursuit of Profitable Growth

accenture

High performance. Delivered.

• Consulting • Technology • Outsourcing

William D. Green,
Chairman & CEO, Accenture

The dramatic rise of China as a global economic force has been nothing short of extraordinary, and the growth and change that continue to shape the nation is truly something to behold.

The resulting message to business leaders around the world is clear: Companies that aspire to compete on the global stage must have a growth strategy for China. At Accenture, this is my responsibility as the executive sponsor of our business and growth agenda for China. I spend a lot of time in China to help Accenture build a dominant market presence, as well as deep, differentiated skills to help our clients achieve and sustain high performance in that special market.

China is vitally important to Accenture's future. We set up our offices in Greater China more than 20 years ago. We now have close to 3,000 people serving a diverse group of clients. For Accenture, China represents a great reservoir of capability – talent, knowledge, know-how – to serve local enterprises as well as global clients. We are focused on helping our clients realize the potential of high performance in China, and we are equally committed to being part of the fabric of the local business community.

In observing Chinese businesses soar at home and abroad, we were eager to learn how they compare to the high performers we have identified through our ongoing study of the characteristics that drive superior results over time. Clearly, Chinese success stories such as Lenovo and China Mobile have been doing something right.

With Accenture's long-time experience working with Chinese companies–and with a proven and unique system for measuring high performance – we set out to answer our own question, and the questions we have heard from many Chinese executives about what it takes to achieve sustainable and profitable growth.

As background, Accenture has been studying high performance for many years. In 2003, we stepped up our research in designing and refining proprietary methods to evaluate performance. We have since looked at more than 6,000 companies and identified 500 high performers. These high performers successfully balance current needs with future opportunities, and consistently outperform their peers in revenue growth, profitability and total returns to shareholders. High performers sustain their superiority across time, business cycles, industry disruptions and changes in leadership.

As you will read in this report, we have now applied our research methodology to China, augmenting our five-point financial analysis with rich surveys of more than 75 board-level executives in China, as well as with in-depth case studies and interviews.

Our key findings explore which traits help Chinese companies succeed in this fascinating market, and which Chinese characteristics are advantageous and in what circumstances. The report also identifies places where Chinese companies are lagging behind global high performers, and it focuses on actions and outcomes to help them achieve high performance.

We hope you find this research insightful. It is the first in a regular series of reports on the secrets to long-term business success in China.

I am personally inspired by the promise and opportunity that China represents and the competitive dimension it brings to the global marketplace. The change taking place in China is tremendous – the determination, the ambition, the view of the future. One can't help but get excited about it and want to be part of it.

William D. Green,
Chairman & CEO, Accenture

Gong Li

Chairman, Accenture Greater China

When we began this research project last year, we believed that the best Chinese companies are those that harness the power of the nation's growth while retaining a sense of perspective about what is achievable in both the short and long term.

The research has proved our beliefs correct. There exists a strong line-up of companies that successfully and consistently balance the need to manage for today and for tomorrow. These are the high-performance businesses in the vanguard of the Chinese companies that dominate the domestic market. They are the front runners with the potential to alter the competitive landscape of overseas markets when they expand beyond China's borders. In fact, many of them are already doing just that.

My colleagues and I at Accenture are delighted to share this insightful report with you. It is the culmination not only of a richly detailed and unprecedented research program but also of more than two decades of hands-on experience in helping Chinese businesses push for ever higher levels of performance. But this report is by no means an end point. We are committed to extending and deepening our studies of what constitutes high-performance business in China, and we are just as committed to expanding our services to China's fast-growing organizations regardless of where they place on the performance spectrum.

I firmly believe that no other organization is better suited than Accenture to assist Chinese enterprises as they strive to achieve and sustain high performance. We have helped hundreds of clients around the world to do the same. We are equipped with a well-disciplined and well-proven methodology. And now we have real data from China – and about China.

We know you will find this report engaging, enlightening and applicable. We hope that it prompts you to talk with us about some of its findings.

Gong Li
Chairman, Accenture Greater China

Contents

Executive summary

The astonishing growth rates of so many Chinese companies have become a matter of great pride for the nation's business leaders – and a matter of concern for competitors around the world.

But can China boast of companies that significantly outperform their local peers in terms of revenue growth, profitability and total returns to shareholders? Do those businesses have the potential to be truly competitive on the world stage? And is their performance sustainable?

The short answer to the first question is a resounding "yes." Accenture's new study, featuring detailed analysis of nearly 200 publicly listed Chinese companies, has examined the characteristics of more than 25 Chinese high performers – in business-to-business sectors as well as in industries that serve consumers directly. These companies share a dozen methods and approaches with longtime global high performers such as Toyota, Microsoft and Wal-Mart. Yet they have their own secrets to success – Chinese characteristics that are unique to them.

The answers to the second and third questions are less straightforward. The high-performance businesses in China are not on a par with the world's foremost high-performance businesses – not yet. While their revenue growth soars on the back of China's continued economic growth, their ability to create value (by returning profit greater than their cost of capital) remains only half that of their global peers. It remains to be seen whether China's best players have built the management practices and supporting business operating models that will allow them to generate profitable growth in more mature markets over the long term. (For a detailed breakdown of these figures, please see Section 4 of the report)

Why is this important? It is one thing to succeed in a booming economy where tens of thousands of people join the ranks of the nation's shoppers every day, and where the sun shines brightly on the stock market. It is quite another thing to weather repeated economic doldrums or go head-to-head with hardened European, American or Japanese rivals in slow or no-growth markets where every sale is a battle and survival depends on good business models.

Yet there is no denying the global market presence of the Chinese companies that just a decade ago were virtually unknown outside China. Walk through the electronics section in most department stores between Beijing and Boston and it is quite obvious that Lenovo is firmly established as a premier player in electronic goods worldwide. Glance through the business section of any newspaper and it's easy to see that companies like China Mobile, Huawei and Haier now receive as much attention from journalists and executives as their global industry counterparts.

However, anecdotal evidence about the performance of China's best-known brand names, no matter how abundant, is not sufficient to guide the decision-making of the nation's business leaders. Nor is it enough to extrapolate based on long-term studies of best practices in other nations; China's business climate is too dynamic for that. When we set

out to study High Performance Business in China, we were not interested in generating yet another attention-grabbing "Top 100" list based simply on the companies with the highest revenues or profits. We wanted to get definitive answers to deeper questions. How do China's high performers go about building value for shareholders? Are they focused on revenue growth, profits or market share? Are they focusing on product development and R&D or concentrating on building customer loyalty and retention? Are they collaborating with multinational companies or preferring to go it alone? To what extent are they helped or hindered by government controls? How do they really compare to their global counterparts when gauged by widely used performance indicators? And how well prepared are they to compete in global markets? Above all, we wanted to know how China's best of the best match up to the rigorous definitions of high performance that Accenture has developed.

Our research yielded answers to those questions and more. It also exploded three persistent myths that hold back many Chinese business leaders' pursuit of high performance.

The first myth is evident in the overwhelming consensus among Chinese executives that their companies' ability to achieve high performance hinges on specific industry factors or on a company's current industry ranking. Our China research reveals that high performers exist in all but a tiny percentage of the industries studied – even in those that some would term unattractive due to their highly fragmented markets, intense competition and relatively anemic shareholder returns.

Second, there is a belief that there is only room for one or at most two successful players in each industry. That sense is especially strong as consolidation accelerates in China, but it is not backed by fact. We found that while roughly two-thirds of the industries we studied have at least two high-performance businesses, almost a third have at least three such businesses, and two industries have four apiece.

The final myth upset by Accenture's research is that well established incumbents have an edge on high performance. Many companies in China are giving up on high performance because a dominant player looks immovable. But our research found that neither relatively new entrants nor older companies have an edge when it comes to achieving high performance.

The moral: Average performers must never quit trying to improve their performance. The payoffs are too great. Moreover, companies can achieve high performance even in unattractive industries. They can do so when the markets demand growth and profits, when a dominant player seems to enjoy unfair advantages and when long-term bets are years away from paying off. For true high performers, then, "wait until next year" is never an option.

China's top performers stand apart in each of the three areas that Accenture has identified as the building blocks of

high performance, as explained on page 13 of this report. Here is a glimpse of where they excel:

Market focus and position

The Chinese companies that outpace their local competitors are akin to global high performers in that they recognize the value of making good decisions regarding where and when to compete. They capture best markets at home and abroad, they are good parents to the businesses they own, they focus on shareholder value creation, and they manage multiple horizons simultaneously. The key difference? As a rule, Chinese companies approach their markets from more of a "network" perspective.

Accenture's research shows that these companies have learned how to succeed in China's less developed markets where they often have lacked multiple distribution channels and choices in after-sales support, financing support and more. Whereas multinational top performers tend to decide whether to enter a new market based purely on the market's attractiveness, China's high performers don't make such decisions independently and don't tend to consider themselves "go it alone" players. Companies like China Mobile, Midea and Yantai Changyu Pioneer Wine Company line up their partners well ahead of time, relying on them to go to market and to support their efforts over the long term. At the same time, however – and this is important – they do not allow themselves to become distracted from their core businesses.

Distinctive capabilities

China's top performers, like their global counterparts, fundamentally recognize the need for distinctiveness. These companies define customer-centric business formulas and then deploy their capital accordingly. They constantly focus their integration efforts on their core processes and they balance evolutionary and revolutionary change in their business models. Additionally, China's top players have an especially positive attribute: a deep understanding of how fleeting such distinctiveness is.

In effect, high-performance businesses in China know they need to be serially distinctive – a subtle shift away from other Chinese businesses that more often focus on tactical initiatives that don't necessarily lead to long-term sustainable distinctiveness. In practice, serial distinctiveness translates into flexibility – an ability to change business models quickly to suit new markets, new opportunities, and new constraints. Look at how Lenovo, for instance, has continually adapted its business model since beginning life in the 1980s; or how Shuanghui, one of China's top meat producers, continues to impress investors with its ability to match its offerings and distribution channels to the evolving needs of consumer markets.

Performance anatomy

In China, high performers recognize, as their global peers do, that they need to develop key cultural mindsets that underpin their strategies and lead to improved business performance. They embrace the need to maintain a balance between market-making and execution, to obsessively identify and multiply talent, to use technology as a strategic asset, and to develop and grow their intangible assets such as the equity in their brands. Yet they distinguish themselves from their global counterparts in their ability to successfully blend Chinese and international approaches to management and risk.

Chinese high performers have recognized the need to adopt international best practices in a number of areas and are carefully combining them with best practices from Chinese business, not least its longer-term perspective and its ability to adapt to turbulence and volatility. One can see this most clearly in how the top performers address their employees' tolerance and understanding of risk and in how they gauge the expected returns for absorbing it.

Accenture's researchers are as excited as anyone to see how fast China's top performers will close the performance gaps with the world's best. These top performers are already stars compared to average Chinese companies, averaging total returns to shareholders (TRS) of seven percent between 2001 and 2005 while the average for all Chinese companies was negative 13 percent. Yet during the same period, the high performers lagged far behind their peers in our global analysis set. Top global players showed a TRS of 22 percent, and the average global company, with a TRS of nine percent, still outpaced China's best performers.

Even though profitability and TRS have improved significantly since the 2001-2005 measurements were made, it is highly unlikely that Chinese companies' fundamentals have picked up at the same pace as the growth of the market suggests. Business leaders concede that much of this growth has been driven by market reforms and excess liquidity.

The upshot, which we explore fully later in this report: no matter how far ahead of their local competitors Chinese companies might be, many still need to reemphasize the quality of growth in revenues and profits before they can go head-to-head over the long term with the world's best companies.

We are sure our new research findings will prove valuable to the many Chinese companies that are in pursuit of high performance. We also expect these findings to be very useful to the elite group who have achieved high performance. After all, it is far easier to become a high performer than it is to remain one.

So we urge senior managers to look closely at the similarities and differences between China's top performers and the global top performers – to apply the kind of scrutiny that China Mobile is now using to gauge itself against Vodafone, Verizon and others – and we recommend examining those nuances when grouped by Accenture's three building blocks of high performance.

1. What is a high-performance business?

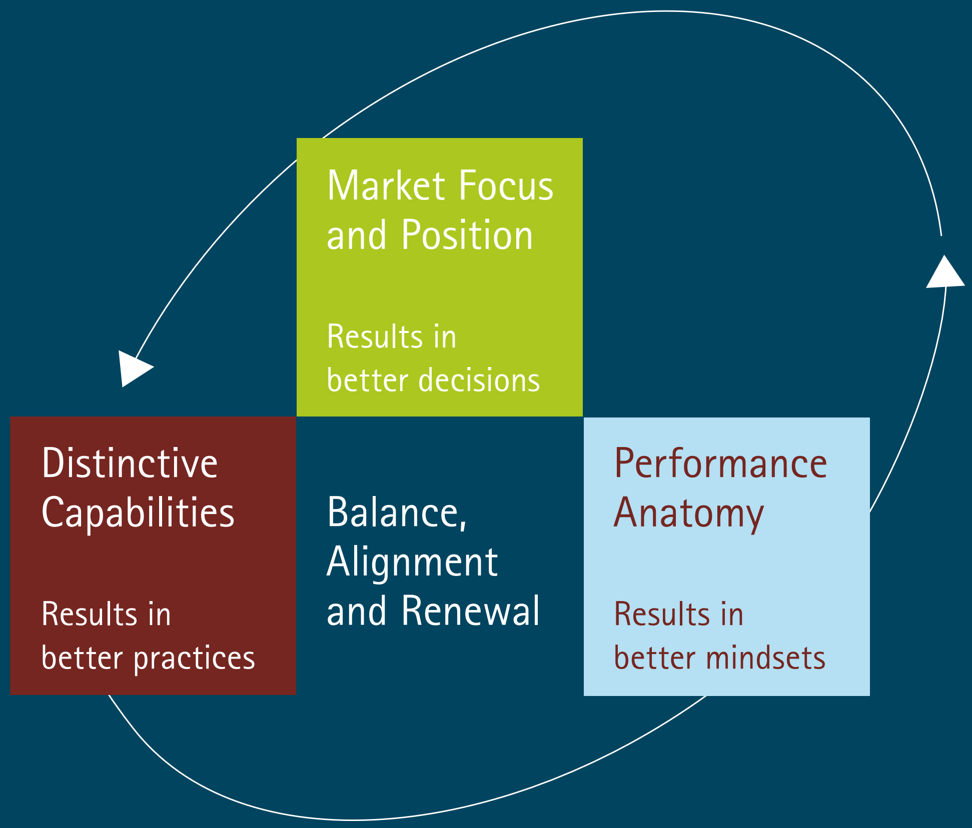
Accenture defines a "high-performance business" as one that consistently outperforms its peers across business and economic cycles as measured by widely accepted financial metrics. To be a true high performer, a company must survive and thrive through repeated economic and market disruptions – often across generations of leadership.

In our experience, fewer than 10 percent of public companies meet the mark.

Now in its fifth year, our global program of original research into high performance has been recognized by Harvard Business Review as one of the 10 most notable initiatives in the field during the past quarter century.[1] We find that the attributes of excellence that transcend industries and companies can be grouped into three categories – what we call the building blocks of high performance. A high performer has to get them right and constantly balance and realign them. They involve:

- A focus on market and position – knowing where and when to compete.
- A focus on distinctive capabilities – a company's differentiated approach to the way it builds and leverages its capabilities.
- A focus on performance anatomy - the underlying cultural characteristics and mindsets that enable a company to out-execute its competitors whatever strategies they choose.

Figure 1. Three elements of competitive essence



About Accenture's High Performance Business research

Accenture's High Performance Business research initiative is a global program that spans thousands of companies in a wide range of industries.

We have conducted in-depth analysis of more than 6,000 companies and identified over 500 "high performers" – companies such as General Electric, Toyota and Procter & Gamble.

Unlike other approaches which simplistically equate high performance with raw financial metrics such as operating income, Accenture's research grades on a curve across five discrete metrics.

A company is deemed to be a high-performance business if and only if its performance is substantially and statistically better than that of its peers across a range of aggregated measures – over several years.

By examining so many metrics among peers in an industry set, we are able to gain a highly informative "apples to apples" picture of differential performance by industry.

(For more detail on our unique research approach, please turn to Research Methodology on page 50)

2.
Pursuing high performance on the global stage

Accenture's research on the global economy reveals a new world in which leading Chinese companies are becoming forceful competitors – and where legions of fast-growing Chinese contenders are eager to learn what it takes to compete at the highest levels.

Globalization is entering a new and more complex phase. The collective economic dominance of the US, Europe and Japan is giving way to a world order characterized by multiple poles of economic power and business activity. The new economic hubs are not limited to China, India, Brazil and Russia; fast-growth economies such as Mexico, Turkey and Poland are starting to exert their own gravitational pulls.

The implications for Chinese enterprises are profound. In this multi-polar world, competition for talent, capital, consumers, resources and new ideas is no longer contained within national boundaries (see Sidebar A, page 17). Yet the evolution of globally interdependent markets is just one of several factors driving the need for enterprise transformation in China. Accenture's research has uncovered three additional critical issues forcing Chinese businesses to re-examine their understanding and pursuit of high performance:

1. Hyper-competitive domestic markets

The reality of operating in the new multi-polar world is as daunting for Chinese companies as it is exciting. Realizing it cannot hold back market forces, the Chinese government is determined to meet the challenge head-on. It is raising the level of business performance in China by pushing thousands of State-Owned Enterprises (SOEs) to transform their operations – and to consolidate. Under the guidance of the State-owned Assets Supervision and Administration Commission (SASAC), roughly 5,000 of the nation's total of 130,000 SOEs are being privatized each year.[2] The initiative is a dramatic one: Many former SOEs are now wrestling with the challenge of developing a high-performance business culture for the first time.

Simultaneously, a cohort of leaner, more agile Chinese companies is emerging, eager and ready to challenge the older state-owned businesses. A booming private sector, inspired by the success of trailblazing companies such as Baidu, Sohu, Huawei, Home Inn, Mengniu and Suning, is further demonstrating that success in China is not just the preserve of companies that began life as part of a government entity. Unencumbered by the typical SOE's legacy of bureaucracy and inflexibility, these companies are setting new standards for enterprising business practice in China.

2. Diminishing local advantages

While Chinese companies continue to grow and evolve, a number of the advantages that have served them well are steadily diminishing. Recent data released by the China Association for Labor Studies[3] suggest that wages in China have nearly doubled over the past four years, outpacing the rate of growth of the nation's economy. While there is still an abundance of unskilled workers in the interior, coastal manufacturing regions are beginning to experience a shortage of labor, which is expected to put further pressure on wages. In regions with concentrations of businesses requiring highly skilled workers, wage inflation is rife as demand outstrips supply.

Concurrently, the barriers to competition are being dismantled in sector after sector. As foreign companies spend more time operating in China, they are picking up local knowledge, relationships and understanding. In some cases, international companies now have Chinese subsidiaries staffed entirely by locals, meaning that the comparative advantage that Chinese companies had in terms of local understanding is being eroded. As the playing field flattens out, the best Chinese enterprises no longer rely exclusively on specific Chinese factors for their success even though some of those factors are undoubtedly still useful. Instead, those organizations are intent on transforming their operations to bring them in line with their international peers on all fronts.

3. Shareholders are seeking results

The last 18 months have witnessed a remarkable stock market boom in China. By July 2007, the Shanghai A-share market had risen by more than 50 percent since the start of the year, and by 144 percent over the preceding 12 months. The average price/earnings ratio was approaching 50. Three factors have fuelled the equity boom: There has been a flood of IPOs since restrictions were lifted last year; there is excess liquidity in the market; and individual investors get only meager returns on financial alternatives such as banks' savings deposits.

Such a phenomenal increase in valuations is a double-edged sword for Chinese companies, and the high performers know it. Although there may now be broader access to more capital, businesses' stock prices are trading at levels that reflect investors' expectations of their future performance. If China's listed companies are to "grow" into their stock prices, they have to be able to demonstrate the consistent creation of profitable growth over the long term.

On top of that comes the complication that all shares in Chinese companies are set to become fully tradable over the next five years. This will give local businesses further opportunity to try to attract strategic foreign investors with desirable capabilities. Such investors will no doubt be looking for companies whose management teams are focused on profitable growth and not just growth in revenue.

Competing on a higher plane

The confluence of these factors represents a turning point for Chinese businesses – a point at which their ability to blend global best practices with proven home-grown methods is crucial, and where they must start looking far over the horizon in search of opportunities for sales, funding, investments, sourcing, talent and alliances.

China's future high performers are replacing serendipity for proactivity, taking firm control of their destinies. Although many local companies have been able to ride the wave of China's economic expansion – growing revenues on average 17 percent faster annually than their global counterparts between 2001 and 2005[4] - the best performers know they cannot expect national economic uplift to keep revenues soaring indefinitely. They also understand that top-line increase alone is not enough – growth must be profitable, and profitable growth must be sustainable. Anything less means they will strain to become world-class high performers.

The convergence of those factors has real significance on macroeconomic and social levels too. It calls for a reassessment of relationships between private and public sectors. In our multi-polar world, China's businesses, long intertwined with government, are finding they are the pivot points of new national policies. But today's interactions involve collaboration instead of control, and state officials and captains of industry alike are learning what it means to be interdependent.

Political leaders in Beijing – and in China's provinces – understand that by fostering globally competitive high-performance businesses that can build new markets and powerful global brands, China can reduce its dependence on foreign investment, technology and demand and make the nation a global focal point for highly productive economic activity and innovation.

Business leaders understand that their pursuit of high performance mirrors the government's shift in focus from the quantity to quality of China's economic growth. Far-sighted executives are well aware of the pivotal role their companies will play in continuing the creation of a harmonious society and in ensuring the more equitable and geographically even distribution of the benefits of economic expansion.

Sidebar A

China in a multi-polar world

Five themes highlight the new competitive landscape for China's companies – a worldwide landscape that offers unprecedented opportunity as well as challenge:

Talent

Talent has become a universal commodity, fought over by competitors from all over the world. China's labor force, while massive, does not include an endless supply of highly skilled workers, and competition for such employees is intensifying as more global businesses look to shift more knowledge-intensive activities such as product design to China. At a tactical level, local companies must now match or improve on-the-job offers being made by the competition. At a strategic level, such companies have to implement innovative talent management approaches that look at the workforce as an asset to be cultivated and optimized, not as a cost to be managed tightly.

Multidirectional capital flows

As the movement of labor between companies and nations has increased, so too has the flow of capital. Under the terms of its WTO membership, China has been liberalizing its rules on foreign direct investment, easing many of the restrictions that have prevented foreign companies from operating independently. In several industries including textiles and consumer electronics, Wholly Owned Foreign Enterprises (WOFEs) have been set up, often with great success. M&A restrictions have also been relaxed, and while many in China remain wary of allowing foreign companies to "buy their way to supremacy" in key sectors of the nation's economy, the government is eager to let market forces drive improvement in local companies' competitiveness.

Such investment flows are by no means all one way. Chinese outward investment is booming, albeit from a lower base: The value of overseas acquisitions completed by Chinese companies tripled in 2005 and almost doubled again in 2006[5]. Many Chinese companies have begun to go global, well aware that they need to expand beyond the fiercely competitive domestic market if they are to maintain their growth and to master new "soft" skills in areas such as marketing and branding, advanced technological innovation and management. The Chinese government is actively supporting many such expansion efforts in the hope of creating several national champions by 2010.

The liberalization of capital flows has also extended to the proliferation of Chinese IPOs on both local and foreign exchanges. Excited by Chinese companies' long-term prospects, investors have fueled record listings such as Industrial and Commercial Bank of China, with its market capitalization of US$21.9 billion[6] and Bank of China, at US$11.2 billion.[7] The new multidirectional nature of capital flow is well reflected in the fact that in 2006 the mainland Chinese and Hong Kong exchanges attracted more IPO funds than did either the London Stock Exchange or the combined total of the NYSE, NASDAQ and ASE exchanges, becoming the world's largest fund-raising market[8]. That is a remarkable development given that it was only in July 2006 that restrictions on IPOs in local stock exchanges were lifted after a year-long hiatus.

Consumers

The battle for China's new consumers rages more fiercely than ever. Average urban disposable income is rising at more than 10 percent a year[9] and a new home-owning middle class is forming, driving huge demand for products such as cars and household appliances that until recently were beyond the reach of most Chinese families. Given such growth in spending power, it is not surprising that Chinese consumers are becoming more discriminating about product features and quality – and more insistent on better customer service. International companies have set the standard for service, bringing to China the sophisticated techniques and capabilities they have developed and refined in their other markets. In most sectors, local companies are playing catch-up to match the multinationals' levels of performance in acquiring and retaining customers.

Resources

China's burgeoning consumer markets are a primary reason for the nation's unparalleled appetite for energy and raw materials. Chinese oil companies are among the most active on the African continent. China's imports of materials such as copper concentrate and iron ore are so enormous that even the slightest shifts in its demand patterns now trigger big changes in world prices for the materials. For many Chinese companies, global sourcing is now a reality. They face a future of increasing dependence on worldwide supply sources – with all that that means for vulnerability to external supply-chain shocks.

New Ideas

The developed world is also losing its monopoly on innovation. Clusters of innovation are springing up across the emerging world, with China becoming a key generator of new product concepts. The Chinese government aims to increase the country's research and development (R&D) spending as a percentage of GDP from 1.3 percent in 2005 to two percent by 2010.[10] While many local companies still lag their international counterparts in R&D investment, China's best companies are catching up rapidly. They are setting up their own R&D centers, encouraging and expanding knowledge transfer and collaboration with multinational partners, tapping into exciting new product ideas generated by customer feedback, and implementing innovative ideas into their management processes.

3.
The characteristics of Chinese high performers

About the High Performance Business China research

Accenture's High Performance Business study in China is based on two phases of research: quantitative, then qualitative.

First, we applied our proprietary method of performance evaluation. To meet our criteria, a company's annual revenues had to exceed RMB 1 billion, based on publicly available data from listed Chinese companies incorporated in mainland China. The company had to be listed (on either local or overseas stock exchanges), with at least 50 percent of its sales generated in China.

To pass the second stage of screening, the company had to be listed on the capital market for more than five years.[11]

The third screening level involved selection by industry. Since China's capital markets are far from mature, many Chinese companies, particularly the State-Owned Enterprises, are not listed. For an industry group to be included in the research, the sum of the market capitalization of the companies that had passed through the first two stages of screening had to make up at least 50 percent of the total market cap of the industry.

A final consideration in selecting the industry groups was whether Accenture had examined an equivalent global peer set that would enable direct comparisons to be made between the two.[12] By examining so many metrics among peers in an industry set, we were able to gain a highly informative "apples to apples" picture of differential performance by industry.

With 183 companies screened, we began the statistical analysis of their financials. Our High Performance Business methodology involves assessing a company's five core areas of performance by analyzing 11 financial metrics from publicly available sources. Each metric is then gauged for statistically significant outperformance of its industry peers.

Each company's performance was then compared to that of its peers on each measure and rated based on the degree to which it over- or underperformed its peers. The ratings for each measure were consolidated, creating one score for each company.

The research next moved to the qualitative phase. A detailed 63-question survey was carried out with 75 Chinese executives to help us understand how the most successful Chinese enterprises are achieving uncommon business success.

The resulting data provides meaningful insight into how China's true high performers succeed.

Market Focus & Position

High-performance businesses have remarkable clarity when it comes to setting strategic direction, especially regarding big decisions. They always seem to be in the right place at the right time. When one market matures, high performers are ready with the next big thing; when buying trends send customers in a different direction, these businesses are waiting at the end of the path; when they acquire new businesses, they do so wisely and tend to the acquisitions well. Add up these factors and the result is that high performers excel when it comes to their market focus and position - the "where and when to compete" aspects of business strategy.

In short, through their market focus and position, high performers achieve a kind of strategic decision-making capability that enables them to compete in the best markets and maximize growth opportunities, without reaching or scaling beyond their limits, and to select and manage the optimal portfolio of businesses.

Global best practices applied by Chinese high performers

1. Chinese high-performance businesses capture best markets at home and abroad

Accenture's global research reveals that high performers are masters of aligning the markets they go after with the capabilities that they have. Consider, for example, the way in which Toyota has enjoyed such success with its Lexus brand. Although the company was originally known for its price-competitive compact sedans, it leveraged its streamlined manufacturing capabilities to produce a high-end vehicle at a relatively low price compared to its competitors. As a result, it enjoyed dual success: Not only was the Lexus the best-selling car in the United States from 1999 to 2005, but it was also voted the most reliable every year between 1995 and 2004.[13]

As the Chinese economy matures, there continue to be great opportunities to capture growth in the domestic market. Geographically, the major metropolitan hubs, primarily found along the east coast, have long been the focus of attention. Now, however, the government's massive ongoing infrastructure investments are gradually extending and opening the arteries of China's transport system, improving the flow of labor and investment beyond the coastal provinces and creating exciting opportunities for companies to tap into previously inaccessible consumer demand in China's hinterland.

All companies operating in China are well aware of these developments. While many have been lured into pursuing each and every potential growth opportunity, high performers have used their local knowledge to identify the right markets in which to compete, based on careful alignment with their capabilities and with their ability to manage the fragmented distribution networks that persist. This approach considers the attractiveness of new markets alongside what these organizations can actually bring to the market. At the same time, these companies do not lose their focus on maximizing the returns they get from their investments in the more developed cities that are primarily found along the eastern seaboard.

For example, Midea, in household appliances, is exploiting new opportunities in less-developed regions of China. The company recognized that, given its local knowledge, it could create effective distribution channels as well as specific products tailored to the intermittent nature of the power supply in these regions. Therefore, in 2005, it invested more than US$13 million to establish a distribution network of 10,000 retailers in thousands of counties and towns. These outlets were used to launch a new type of air conditioner called "Lengjingxing," which can be used with the low-voltage power supply common in less-developed areas, but which also meets the requirements of the national standard for energy-saving air conditioners.[14]

Likewise, China Mobile recognized the attractiveness of the rural market and made a determined push to develop its offerings there in 2006 as part of a national initiative promoted by the central government. The company acknowledged that the potential uses of telecommunications in rural areas are very different to those in China's cities, and it tailored its offerings accordingly. Cell phone plans have been introduced that include information such as crop prices and tips on duck breeding delivered via text message, the Internet, and a call-in phone service.[15] Such targeted services helped boost China Mobile's subscriber numbers by 22 percent to 301 million by the end of 2006.[16]

Examples of Chinese companies capturing "best" markets are not confined to the local market. Several high performers are applying their knowledge to win in other economies - both emerging and developed. In emerging markets, Chinese companies can leverage their successful experiences dealing in similar levels of volatility and unpredictability at home. For example, in industrial equipment, Hangzhou Steam Turbine Co., Ltd., has focused on growing its market share in India as demand in China has slowed due to government-driven monetary tightening. As a result, Hangzhou Steam Turbine Co., Ltd has been able to maintain profitable growth. By the end of 2005, 20 percent of its output was destined for overseas markets. While India remains the key focus, new opportunities are being developed in places such as Indonesia, Malaysia, Turkey and Sudan.[17]

High-performance businesses are almost twice as likely as other companies to try to replicate their business models in overseas markets where it is applicable.

Chinese high performers have also been quick to identify opportunities in other product markets within their sectors. For example, Lenovo, whose original success in the 1980s was based on its introduction of an add-on card that allowed Chinese applications to run on English-language operating systems, has shown considerable adroitness in moving into markets where it can use its capabilities in producing consumer electronics to match demand.

Lenovo has recently launched a series of low-cost notebooks and desktop PCs under its own brand, targeted at small and medium enterprises (SMEs). These computers come with a series of business maintenance and service features designed to assist small companies that lack a dedicated IT department. As a result, Lenovo's share of China's SME market jumped from 21 percent in 2005 to 39 percent in 2006.[18]

Lenovo also recently made an ambitious move into China's high-end phone market, unveiling a smart phone equipped with the first Chinese version of the Windows Mobile 6.0 operating system.[19] The company hopes to exploit the lack of attention previously paid to the high-end market: Until now, local handset manufacturers have targeted the low end, leaving consumers who can afford more sophisticated phones little choice but to purchase a phone made by a global player such as Nokia or Samsung.

Clearly, Chinese high performers understand what they can do well and stick to it. Whether directly related to the companies' available resources or connected to their core offerings to consumers, Chinese high performers concentrate on the markets where they possess unique strengths.

Nearly 90 percent of high performers focus on markets where they believe they have unique strengths. Less than two-thirds of low performers do so.

2. Chinese high-performance businesses are good parents to their owned businesses

At the global level, Accenture's research has shown how high performers have consistently driven value from their corporate centers to their other business units (both geographical and functional). A prime example is Johnson & Johnson, the multinational manufacturer of health care products, which is the parent of more than 200 operating companies. It has instilled a strong culture across all of them, fostering distinctive and hard-to-imitate advantages, while allowing the subsidiaries sufficient leeway to make decisions on how they operate.

The results of our analysis suggest that the best Chinese companies are adopting a similar approach. Zhejiang Hisun Pharmaceutical Company, for example, split its product lines into 10 separate business units in August 2006. Each unit is managed by a senior executive who controls everything from HR appointments, salary allocations and finance through to procurement and sales and product options. In this way, the company has implemented its so-called "Big Company, Small Operation" reform which aims to lower operating costs, improve efficiency and speed new products to market.[20]

Our survey results revealed that it is the larger companies (those with revenues over US$1 billion) who are more inclined to give more autonomy to their business units, geographic units and divisions. As Chinese companies scale up, they appreciate that not all control can be retained at the core and they are establishing the appropriate balance between delegation and direction from the corporate headquarters.

A number of Chinese companies that have expanded into international markets demonstrate this trend. For example, a major household appliance manufacturer has successfully established operations in the US by giving its management team there sufficient autonomy and decision-making rights since it entered the market in 1999. A US-based R&D center, a trading company and a production plant have all been established to cater to local consumers' tastes and channels. The trading company is led by an American with extensive industry experience who has responsibility for sales and marketing activities in the US market and is authorized to make decisions about the US operations. Meanwhile, the parent company retains control of strategy formulation. This strategy of decentralized decision-making processes has worked well: The company's US operations became profitable the second year after their establishment, and revenue has grown significantly in the years since.

Nevertheless, our research indicates that Chinese companies, on average, give their subsidiary businesses much less jurisdiction than their international counterparts do. Perhaps it is unsurprising for companies accustomed to a centrally planned economy. In addition, there may be another element at play: Culturally, Chinese people are somewhat less inclined to make decisions proactively without clearing them first with their superiors. Although this approach does reduce risk, it may prove a hindrance because rapidly changing environments mean that decisions need to be made quickly and appropriately to suit local conditions.

3. Chinese high-performance businesses focus on shareholder value creation

Listed companies' primary responsibility is to create returns for their shareholders. Consider how American energy company Constellation Energy successfully evolved from a US$3 billion regional regulated utility into a nearly US$13 billion national energy company between 2001 and 2005. Now North America's leading energy supplier, Constellation achieved success by instilling a commercial mindset across the company - a huge undertaking given the comfortable position the organization had enjoyed until the 1990s in a highly regulated industry. As deregulation flattened the playing field, this customer-driven and shareholder value-based perspective enabled the company to survive and prosper.

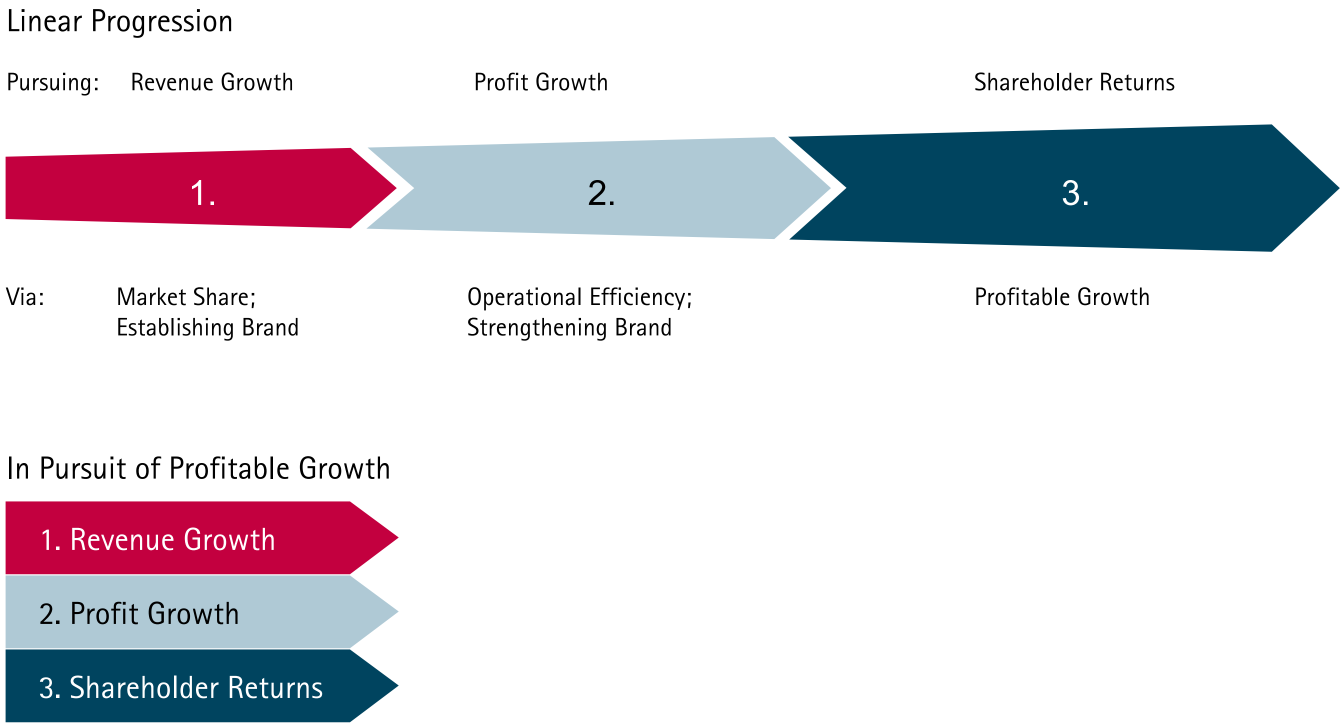
In China, the issue of shareholder value creation is complex. Many companies initially pursued listings to gain access to capital with relatively little consideration of how to maximize value for their investors. Transparency and corporate governance were not priorities. That situation is changing fast. The State-owned Assets Supervision and Administration Commission of the State Council of the People's Republic of China (SASAC) is demanding greater returns to shareholders. Local investors continue to become more sophisticated in examining companies' operations rather than speculating on the fluctuations of the market as a whole. Additionally, many Chinese companies hope to attract strategic investments from foreign investors and are eyeing listings overseas. These three factors are driving the adoption of international best practice in this area.

Our survey yielded revealing data on this point. The high performers identified shareholder returns as their top priority when forming strategy. Poor performers were far more likely to focus on revenue growth above anything else, while the average companies prioritized improving their businesses' performance and efficiency.

Almost half of the high performers ranked "creating shareholder returns" as their top priority when forming strategy. Less than one-fifth of the other companies surveyed did so.

Further in-depth analysis of the Chinese high performers indicated that their management teams are pursuing a different path to success compared to their competitors. Most Chinese companies are progressing along a

Figure 2. The evolution of a Chinese company



linear path that first involves rapid growth to establish market share and brand, then allows time for operational improvements and an increase in margins and profits, and finally focuses on shareholder value creation. However, high performers have a much more holistic strategy that balances all three of these needs at the same time (see Figure 2). The lesson is clear: Every company in China needs to keep growing, but growth should not come at the expense of operational efficiency or shareholder returns. (For an in-depth look at the issue of scale and business performance in China, see Sidebar B.)

But it is not enough for companies to prioritize creating returns for their shareholders via profitable growth. It is equally important to clearly communicate this priority to investors who are anxious to understand how management teams intend to navigate the reality of operating in the new "multi-polar world" with its interdependent global markets for talent, capital, resources, consumer markets and innovation. Our survey results lead us to believe that Chinese companies have some way to go in this area: When asked which intangible assets they currently measure, only two companies mentioned their media or investor relations. Both companies are high performers.

Recent research by Accenture's Finance and Performance Management team corroborates these findings. The team discovered that the information that Chinese CFOs cover most extensively in their company annual report tends to be financially based and internally focused, especially among the SOEs. These organizations could improve their relationships with investors by expanding and refocusing the data provided, especially concerning what the company will do in the future. The good news is that two-thirds of survey respondents plan to increase the amount of information they release to investors about company performance in the next two years. In addition, nearly half say they will add more analysis and reporting of performance against key drivers of growth and strategy. And 40 percent will add more discussion of their management outlook.

For the best Chinese companies, the ability to expand their views beyond traditional balance sheets and income statements and look at other metrics will become even more important as they look to expand beyond China's borders. With such a large portion of their share prices based on expectations of future performance, companies whose CFOs extend the scope of enterprise performance management to include external perspectives on value creation will be much more likely to achieve and sustain high performance. The same is true for those tracking both tangibles and intangibles in this context.

4. Chinese high-performance businesses simultaneously manage multiple horizons

For high performers, good choices are rooted not only in the companies' present capabilities but also in those they can readily develop. The ability to make the right decisions in this dimension is also based on a company's skill at managing across near, medium and long-term time horizons, often simultaneously. For example, Microsoft

Sidebar B

Industry-leading scale is not a precondition of high performance

Many successful Chinese business leaders believe it is important to gain the advantages of scale as quickly as possible. (See "The evolution of a Chinese company" page 23) However, Accenture's rigorous analyses found little correlation between size – measured as each company's percentage of the industry leader's revenue – and business performance.

Although most of the companies that Accenture has identified as high performers show some measure of scale within a particular business segment, in only a few cases are they the absolute revenue leaders in their industries. In fact, the largest companies were the best performers in only five of the 13 industries examined. And of those five, two are State-Owned Enterprises that have been able to take advantage of a lack of competition in their sectors or of a dominant position inherited as the result of government-driven industry consolidation (See Figure 3).

Many Chinese business leaders are convinced that company size is crucial in part because government policy actively supports the development of large "national champions" that will create more jobs and tax revenue. Chinese companies also face growing competition from foreign competitors that often dwarf them in size, and many local executives feel that they can only fight off the challenge by achieving scale.

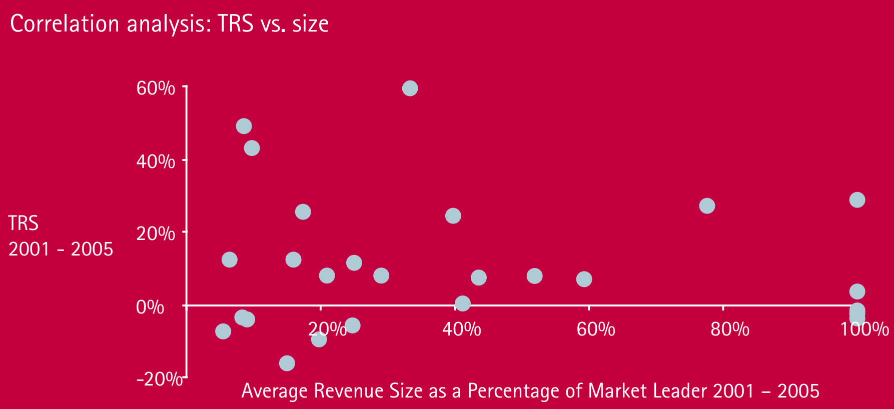
In practice, a measured approach to scale is needed. It is true that, in the right context, scale can undoubtedly deliver well-documented competitive advantages: increased production efficiencies and purchasing power, and especially for a market as fragmented and spread out as China, greater brand prominence and larger market share. But the fact that many Chinese high performers compete successfully at a fraction of the size of revenue leaders suggests that, once sufficient scale has been achieved to survive and ward off hostile takeovers, greater size is not necessarily needed for high performance.

For example, analysis into sectors such as pharmaceuticals and textiles has shown that there are many smaller companies that are outperforming their largest peers in terms of value generation over three and five-year timeframes between 2001 and 2005.

Tellingly, it is in those industries that have opened up to foreign participation that the performance of the largest companies has suffered most. In sectors such as household appliances, alcohol and beverages, and food products, the best performers in terms of achieving profitable and consistent growth have been the relatively small, more nimble companies. As a result of their size, these companies have been flexible and adaptive enough to navigate competitive landscapes where industry structural conditions, key success factors and business models are all in flux. The largest companies in these sectors have been hindered by their size – what economists call "diseconomies" of scale. These complexities create vulnerabilities that can hamper a company's responsiveness to potentially disruptive events like new technology, competitors and the constantly evolving demands and needs of customers.

The upshot: Chinese companies in industries that are now opening up to overseas participants should prepare themselves accordingly and discourage the obsessive pursuit of scale.

Figure 3. Five-year TRS performance vs. relative size of the high-performance businesses



has maintained dominance in the PC operating system and applications arena, while using the cash flow from that core business to build a leadership position in desktop applications (such as Office and Internet Explorer), and related ventures (such as its Xbox). Microsoft is managing its businesses with an eye toward success both today and tomorrow.

This forward-looking characteristic is also evident in the best Chinese companies. Taking a long-term view comes naturally to Chinese executives – China's Confucian culture and practice of decision-making is like no other, rooted in a history of long-termism. But winning Chinese companies have leaders who can temper this instinct with the realization that success requires them to manage the near-term horizon just as carefully.

Only two out of 75 companies surveyed focus on just the short term (less than two years) when carrying out their strategic planning. Nearly three-quarters focus on both short term and long term (between two and five years).

Chinese enterprises often employ "five-year plans" in the same way that the Chinese government manages the economy (China is currently in the middle of the 11th Five-Year Plan, which runs from 2006 to 2010). And what did Accenture find to be the key difference between the best and the rest? The high performers do not maintain a static plan that must be adhered to at all costs. Instead, they distinguish themselves by having constantly evolving plans that aim at where the money is going to be. They anticipate market moves and demographic trends. They create what customers will want in the future, not just what customers want now.

This approach is exemplified by a company in the Chinese pharmaceutical sector, Yunnan Baiyao. In 2005, the company established its "Steady the center and emphasize two wings" strategy. Steadying the center involves maintaining sales growth at 10 percent a year by building the strength of its four core products as the major source of its competitiveness: Baiyao Capsule, Baiyao Powder, Baiyao Spray, and medicine for usage during childbirth. At the same time, the company has been emphasizing the development of its "two wings" – two new departments that focus on creating products to introduce alongside the major ones. These are skin care products, such as Baiyao plaster, and health care products, such as Baiyao toothpaste.[21]

This ability to manage for both today and tomorrow is vital because it is far easier to become a high-performance business than to stay one. Many of our Chinese high performers have been focusing on achieving a dominant market position during the recent period of rapid growth. Now that they have achieved it, they must not get complacent and wait too long to attempt further adaptations to their businesses. After all, the best way to transform is from a position of strength.

5. Unique Chinese best practice:

Chinese high-performance businesses take a networked approach to market focus and position

Chinese high-performance businesses share several aspects of the market focus and position building block with their global counterparts. In one particular area, however, they are leveraging their local advantage - through their ability to rapidly create "ecosystems" that help them get to market nimbly.

Put simply, such ecosystems are the culmination of companies' local knowledge and connections with an array of organizations such as the government, industry associations, international companies, suppliers, companies in other industries and in some cases, even competitors. As a result, Chinese high performers are able to embed their businesses in the fabric of the local markets where they want to compete. They can also better navigate what is still, with the exception of a few large cities on the eastern seaboard, a fairly immature market with fragmented supplier and distribution networks and often inconsistent regulatory environments. Finally, such partnerships and relationships help Chinese high performers better accommodate the many differences among the country's diversified regional markets.

Only three companies surveyed believed that success in China can be achieved regardless of current relationships with external organizations.

Undoubtedly one part of this networked approach is the creation of win-win situations with government institutions, a factor confirmed by the results of our survey. But the Chinese high performers go far beyond that in creating a broad network of contact points – official and unofficial - that allows them to compete in the best markets and maximize growth opportunities. That's especially true of many SOEs. For example, the energy giants Sinopec, PetroChina and CNOOC regularly exchange information, share best practices and visit each others' sites – a degree of cooperation between enterprises in the same industry that is alien to most foreign companies.

Over 80% of the companies surveyed agreed that they were very good at creating win-win situations with local governments.

The development of these networks occurs hand in hand with growth. Witness the way in which, for example, dominant local players in the dairy industry have handled their expansion as demand for their products grows (milk production increased at a compound annual growth rate of 28 percent between 2000 and 2005[22]). These companies have been able to increase their national reach via intricate supply chain networks that require the establishment of solid relationships with local farmers and retailers. At the same time, these companies have recently struck a deal to work with China Railway Container Transport, a state-owned container transportation company, to help them get their products to market more effectively and efficiently.

Often, this networked approach has involved companies diversifying within their own industry's value chains. For example, Lu Tai Textile Co., Ltd., in the textile industry, has spent the last 10 years focusing on developing appropriate relationships to aid the growth of its core business. Unlike so many textile companies which attempted to diversify into other industries on the back of the rapid growth experienced after the market opening in 2001, Lu Tai's management team refused to be distracted. By maintaining a tight focus on textiles, the company has been able to enhance its capabilities throughout the entire textile value chain.[23]

For instance, in the upstream area, Lu Tai built its own cotton production base in Xinjiang. The cotton is then processed in one of the companies' 11 factories that specialize in spinning, discharge, weaving, disposal, and clothing production. By not diversifying away from its core competency, the company maintained a gross margin of more than 30 percent from 2002 to 2005, and its return on invested capital is more than four times the industry average (7.6 percent vs. 1.8 percent in 2005[24]).

Likewise, Midea, in the household appliance industry, penetrated the compressor manufacturing industry in 1999 by establishing a joint venture with Toshiba. This enabled Midea to secure supplies of compressors for its air conditioning business, thereby enhancing control over its own value chain as well as increasing company profitability: In 2005, the gross margin for the compressor industry was nearly 10 percent higher than for the air conditioner business.[25]

Partnerships with international

companies are common, but the hallmark of Chinese high performers' relations with such companies is that they have built long-term strategic relationships based on mutual trust and understanding. These relationships are targeted, founded on companies' medium- and long-term strategies rather than on possible quick wins.

China Mobile, for example, wants to increase its revenues from value-added services. With its massive subscriber base, it has had international companies knocking down its door in search of collaborations. China Mobile has signed agreements with Vodafone Group, News Corp., Viacom's MTV networks, and the US National Basketball Association. It now has a music download service in partnership with Sony BMG, Universal Music Group, EMI and Time Warner called M.music. In January 2007, the company announced that Google's search engine would be featured on its Monternet Internet portal.[26]

Other Chinese high performers have had to work harder to show potential partners what they can offer. In the alcohol and beverages industry, Yantai Changyu Pioneer Wine Co., wants to become one of the world's top 10 wine companies[27] and has spent considerable time and effort signing collaborative agreements with a number of companies that can provide global market access and expertise. These include one of New Zealand's top wine purveyors, a Cognac company and a Canadian ice wine heavyweight. With these deals in place, Yantai Changyu's management team has earmarked 30 percent of sales to come from overseas markets in the next three years. Eventually, they foresee overseas sales matching those made at home.[28]

This networked approach is certainly not unique to Chinese companies. Many multinationals have also invested time and effort in forging relations with external organizations in China. But the key difference is the time it takes these organizations to gain the trust and respect of their partners. Often, by the time such bonds have been established, the opportunity is lost. Local high performers are not only masters at identifying where their capabilities match opportunities; they are masters at getting there first.

Distinctive Capabilities

As China strives to move further up the value chain and reduce its reliance on foreign exports and technology, Chinese companies are being encouraged to compete based on capabilities rather than price alone. But this advice can take companies only so far. For capabilities to make a difference in business performance, ultimately, they must be distinctive. This means using innovation to build hard-to-replicate sets of processes that customers value and that create sustainable competitive advantages.

By studying Chinese high-performance businesses within their competitor sets and across industries, Accenture has learned what makes capabilities truly distinctive, and how companies develop such capabilities. We are also starting to see how Chinese high performers successfully create and manage the unique sets of business processes and resources that underpin their distinctive capabilities.

Global best practices applied by Chinese high performers

1. Chinese high-performance businesses define customer-centric business formulas

Chinese consumers are becoming increasingly demanding and sophisticated in their choice of products. According to the National Consumers' Association, in 2006 total customer complaints numbered 702,350, up from 8,041 in 1985. Chinese companies recognize that to retain customers, they have to serve these customers well.

But how can a company achieve that goal in a way that yields sustainable competitive advantage? Accenture's global research found that the best companies invest time and effort in gaining deep insight in two areas. First, they investigate what consumers truly value (or will value) in each category, and gain an understanding of the marketing capabilities – for example, building the branded experience – needed to create and sustain demand. Second, they identify the most profitable configuration of resources to deliver the promised value. The ability to do so can come only from deep knowledge and mastery of a range of capabilities, from finance to supply chain to human performance.

Our model of customer-centric formulas for value creation is by no means easy to achieve. It requires deep insights into customers' current and future needs, and it demands the creative use of resources to manage the costs of delivering exceptional value. Look at how Dell created its distinctive capability. By realizing that customers would trade delivery time for customization, Dell was able to create a business model where production was postponed till after payment was received, dramatically lowering its costs of goods sold.

Wuhan Iron and Steel Co Ltd. has used its market insights to achieve success in a unique way. Its rule on new product development is "We have what others don't have; what others do have, we excel at; we distinguish ourselves from what others are excelling in; and when others catch up with our distinctiveness, we find something new."[29] Based on its deep understanding of what the market needs, Wuhan Iron and Steel Co Ltd. focuses product development on what it calls "double high" products – high in added value and high in technology content. By focusing on its core strengths and what the customer wants, the company has developed a sterling reputation for providing specialized high-quality products.

Understanding what Chinese customers truly value has played a vital role in the success of several of our high performers; they have identified that Chinese consumers value their brands' Chinese heritage and associate it with Chinese culture and high quality. For example, one of China's major pharmaceutical companies, Beijing Tongrentang, has achieved great success at home and abroad by emphasizing the heritage and culture that it has built up over its 300-year history. This has manifested itself in a number of ways, most clearly in the 20 million RMB invested in the construction of the Tongrentang Museum that began in 2006. This museum is designed to provide background on the development of Chinese medicine and Tongrentang's own history and culture. The company also insists on retaining Chinese characteristics in all its stores, regardless of which country it is operating in, and it assigns senior staff to work abroad to ensure that this occurs.[30]

Likewise, Shanxi Xinghua Cun Fen Wine Company, in the alcohol and beverages industry, blends its traditional culture with its business strategy. It emphasizes the fact that it is still located in the village where it was founded 1,500 years ago and takes advantage of the location's attractiveness to tourists. It hosted a wine culture festival in 2004 that included a press conference, the publication of a book about the company and the refurbishment of the wine culture museum.[31]

Being distinctively Chinese has clear benefits, but the high performers also realize that in the future they cannot rely solely on this factor. In fact, according to MOFCOM , 70 percent of the 1,600 "Chinese heritage" brands are facing a very difficult situation; 20 percent are living off the margin; and only 10 percent are on the right development path. This outlook reflects the fact that young consumers are less inclined to make purchases based purely on brands' Chinese heritage. They're also more willing to try Western brands and products. (See Sidebar C for a more detailed look at this issue.)

2. Chinese high-performance businesses align their capital deployment with their customer-centric business formulas

The key to making a distinctive capability work is ensuring that capital deployment is disproportionately targeted to the underlying business formula. At a minimum, this strategy entails ensuring that each component process has the financial backing it needs to be successful. This kind of commitment can be substantial. One global retailer, for example, is estimated to have spent US$500 million in the early 1990s to create the infrastructure needed for its linchpin supply chain capability.

The top-performing Chinese companies are taking similar steps to make sure their competitive advantages work for them. For example, Wuhan Iron and Steel Co. Ltd. is investing several million RMB in building a sales network system with the customer at its center to ensure that its distinctive products reach the right markets and match customers' expectations. This has involved building strategic relationships with downstream customers and integrating IT systems with them, as well as building integrated supply chains.[35] In January of 2007, Wuhan also started its "customer service technical representative" system, which assigned customer service representatives to 50 important end customers for automotive, home appliance, and silicon steel products. A management and examination system has been implemented to supervise the representatives' work, and communication channels have been opened to make sure feedback from clients is obtained and acted upon in the shortest time possible.

Sidebar C

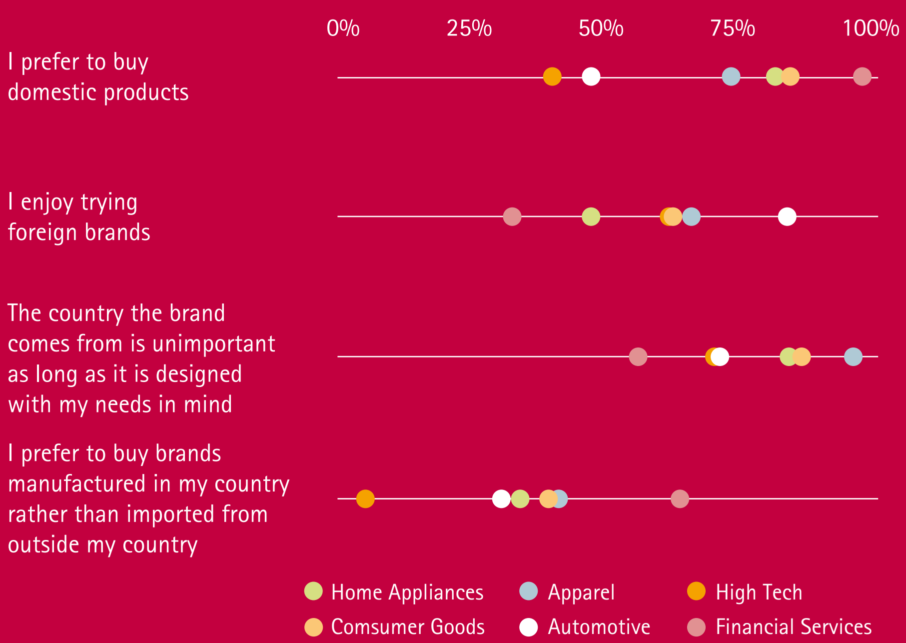
High performers know that Chinese heritage alone is not enough

Fully 95 percent of Chinese consumers who are aware of Chinese brands actively consider buying them, according to a recent Accenture study[33] into how international brands can succeed in China.

However, those same consumers are very open to overseas brands even though they are not infatuated with them.

Accenture's study found that many spenders say they enjoy trying foreign brands (see Figure 4). That finding is supported by The Gallup Organization's long-term studies, which point out "that a 'Made in China' label doesn't guarantee protection against newer, more exciting, and perhaps more relevant foreign competitors."[34]

Figure 4. China's new consumers aren't tied to Chinese brands



* Seven-point scale: 1=strongly disagree, 7=strongly agree. Data points show the percentage of respondents for each product category who gave a score of 6 or 7.

Over two-thirds of high performers target their major investments to improving customer satisfaction and loyalty. Only a third of the low performers do so.

Likewise, in the alcohol and beverages sector, Kweichow Moutai Co. Ltd., identified customer satisfaction as the key factor to beat its competition, especially since over 60 percent of company revenues come from institutional customers with little price sensitivity.[36] The company is one of the first domestic companies in its sector to set up a customer relationship management (CRM) database marketing system. This will help the company to collect, store, analyze and update customer information, as well as study the characteristics of customer behavior. Such large investments reflect the fact that Chinese companies know that they risk losing market share to multinationals that have previously invested substantially in sophisticated customer service capabilities at the global level, and are applying similar if not identical approaches to the Chinese market.[37]

Not all such investments are capital-intensive, though. In China, where labor is comparatively cheap, many companies are replacing large-scale capital investments with investments in labor to create distinctive levels of service. What all these investments have in common is that they are relatively large, one-off investments. High performers rarely attempt to incrementally invest their way to greatness.

3. Chinese high-performance businesses concentrate their integration efforts on core processes

High performers focus their integration efforts. They invest significantly in integrating only what truly matters to their business formulas; they don't try to connect everything to everything else. In the airline industry, for example, low-cost carriers such as Southwest Airlines have achieved great success by integrating cost savings in customer-facing processes with high asset utilization in operations. These carriers' processes, which make up their distinctive capability models, include approaches such as providing only one class of service, using a uniform fleet of aircraft and having employees serve in multiple roles.

In China, operational integration has been both an operations nirvana and a business buzzword for some time, but it is also an important part of what makes the capabilities of a Chinese high performer distinctive. Creating the right integration in the meat industry is a good example. One Chinese company's value formula is focused on freshness, so speed from its factories to store shelves is critical. To achieve this goal, the company has focused on dealing with customers' orders more efficiently. Previously, every order was processed by hand, meaning that it took three or four days for the customer to receive the product. In addition, the company had a number of management systems that were not integrated. For example, it had more than 70 separate statistics functions whose lack of integration was hurting efficiency.[38]

To address these challenges, since 2000 the meat producer has focused on the implementation of a new logistics system with online ordering, a unified database and a centralized information processing platform, which ensures accurate order information, enhances internal quality control mechanisms and automatically provides statistical analysis wherever and whenever people want it. Now, orders are all processed centrally, taking, on average, one employee one hour to send each order to the relevant factory. Such a dramatic improvement in the logistics system has sped up execution and contributed significantly to the company's revenues increasing by a multiple of five between 2000 and 2006.[39]

Likewise, a Chinese company in the industrial equipment sector carried out an exhaustive assessment of its core processes to improve performance in the late 1990s. The company's main products, utility boilers, are high-temperature, high-pressure units that require a high level of security. Quality control from equipment design through to manufacture is paramount. In addition, utility boilers were being made to order in small batches or even in single units. Production was complicated. Further, almost all boilers needed to be designed separately, meaning the designers were bogged down at their drawing boards. The company wanted the designers to pay more attention to new product development. Finally, raw material expenses accounted for 70 percent of the total manufacture cost. The inventory of steel was huge.

After identifying these issues, the company implemented its CIMS (Computer Integrated Manufacturing System) application project. First, it introduced two-dimensional CAD (computer-aided design) drawing, solving the problem of its long design cycle and improving its design capability Second, it introduced the MRP (Material Requirements Planning) system to its operations, with material management as its key point. After integrating its MRP systems with its accounting information systems, the company greatly reduced its inventory levels.[40]

4. Chinese high-performance businesses balance evolutionary and revolutionary change

A company's distinctive capabilities must be dynamic because they require rapid responses to ever-changing customer needs. They must also respond to the demands of environmental change and technology disruption. High performers are particularly good at both adjusting their formulas and redefining them when circumstances require them to do so. Their secret appears to be in achieving the right balance – knowing when a formula must evolve versus when change must be more revolutionary. Many companies have failed because they gave up on a formula too soon; just as many fail because they hold onto a formula too long.

Our global research discovered one company that has done this with particular success: packaged foods manufacturer Kellogg Company. The company recognized that today's consumers are buying food at convenience stores, fast-food outlets and other locations beyond supermarkets and grocery stores. It also has recognized the need to reduce its sales risks by having only a small number of key retail buyers. To increase the variety of its sales outlets, the company purchased Keebler, whose products are widely available in vending machines. Now Kellogg's Nutri-Grain bars, Pop-Tarts, and even single-serving cereal bowls are available at many more locations, increasing the consumer reach and market share of these products while avoiding over-reliance on key retailers.

Accenture has found that high performers maintain the right balance between evolutionary and revolutionary change by constantly moving quickly to take on the new capabilities they need to adapt to changing market conditions. Chinese meat producer Shuanghui has done this successfully. The company recognized that more and more Chinese consumers want to purchase meat products in "international standard" environments as opposed to the more traditional markets or small shops. In 2001, it opened its first fresh meat chain store, and by the end of 2006, had opened over 750 of them. The company saw that good customer service was integral to these stores' success and so focused on minimizing its turnover rate, increasing salaries and managing staff more proactively. The new stores now account for more than 10 percent of the companies' revenues, and further expansion plans are underway.[41]

Yantai Changyu Pioneer Wine Co. has also shown that it understands changing customer needs. As the wine market's growth rate picked up at the beginning of this century, the company moved quickly to reform its distribution network and increase its national coverage. It formed a three-tier sales system, broken into four regions, 26 distributors and 500 sales representatives' offices supported by a growing number of retail franchisees - more than 3,300 at the last count. Results have been impressive. For example, in 2005, Changyu's sales increased in Guangdong and Beijing by 34 and 50 percent respectively. The company's competitors, however, continue to use their regional sales representative models using only a few hundred franchisees. More recently, Changyu has set up direct sales outlets in Yantai and Weihai and halted relationships with 44 franchisees in these cities, demonstrating its willingness to adapt continuously to changing customer dynamics and preferences.[42]

5. Unique Chinese best practice:

Chinese high-performance businesses recognize the fleeting nature of distinctiveness

A Chinese company's distinctiveness is often very short-lived given the nature of the country's growth, the speed of innovation and technological advancement, the relatively low protection of intellectual property and, in most industries, the sheer numbers of companies vying for dominant market positions. Yet in contrast to the majority of Western multinationals, most of which have taken decades to become truly global, many leading Chinese enterprises have used several distinctive capabilities to manage their rise to prominence in a remarkably short space of time.

Consider how Lenovo developed so successfully since bursting onto the scene in 1987 thanks to its add-on card that allowed Chinese applications to run on English-language operating systems. The company's success in the PC business followed soon after, based on superior marketing and sales functions compared to those of their local competitors. As international companies entered the market, Lenovo made yet another step change, capturing the high-end user market by offering comparable products to those offered by multinationals such as HP, IBM and Compaq, but at significantly lower prices. As multinationals continue to ramp up their competition in China, Lenovo will need yet another shift in distinctive capability. Its recent announcement that it will outsource all its international marketing campaigns to India, working closely with advertising agency Ogilvy & Mather, may well be the first step toward achieving its next shift – this time at a global level.

The importance of Chinese businesses' ability to reshape their distinctive capabilities is reinforced when you consider the rate and unpredictability with which regulatory change occurs in China. Even in those industries deemed of "national strategic interest," which remain closed off to foreign participation, such change has dramatic effects. Consider, for example, how one of the high performers in the pharmaceutical sector had to react when the central government suddenly introduced legislation that levied price limitations on anti-tumor drugs. Well-prepared for such changes, the company was able to diversify its product line more quickly than the competition due to its investments in R&D.

As China's reintegration into the global economy continues, Chinese companies' ability to adapt quickly to external influences will stand them in good stead, especially as they enter other emerging markets with similar levels of volatility and regulatory opacity. Such adaptability requires significant investment, and this is where the findings of our survey suggest that the high performers are well ahead of the game. Three-quarters of the high performers we spoke to claimed that they invest enough to ensure that their businesses can adapt accordingly when interrupted by external factors. In contrast, only a third of the low performers made the same claim.

Three-quarters of Chinese high performers invest enough to ensure that their businesses can adapt accordingly when interrupted by external factors, versus only a third of the low performers.

One final point on distinctive capabilities: In the past, the Chinese market has been characterized by a high level of imitation. Very strong intellectual property protection laws exist, yet their enforcement has often been weak. That situation is changing. While challenges undoubtedly remain, our client interactions indicate that Chinese companies now take a more enlightened view of their own intellectually property. Local companies are beginning to pursue cases of imitation and copyright infringement with as much vigor as multinationals do. In such an environment, it becomes all the more important for the best performers to create and rely on their own distinctive capabilities.

Performance Anatomy

Competing companies can appear almost identical – at least for a while. They may share the same targeted markets, business model, revenue base, and employee compensation levels, for a start. But over time, their performances will start to vary, and soon it becomes obvious that they never really were the same. Where they differ is in something that Accenture calls performance anatomy. This is perhaps the most elusive characteristic of all great companies. But with its distinctive impact on the interaction between leadership and strategy, people development, IT enablement, performance measurement and innovation, this element is critical to defining a high-performance business.

Performance anatomy runs deep; it affects all of a company's employees and functions. It is neither hereditary nor accidental. It is the outcome of deliberate choices made by senior executives. Yet it is rarely if ever reducible to a statement of vision and values.

We believe, as do others, that culture matters when it comes to explaining how some organizations achieve and sustain high levels of performance. But frankly, most discussions of culture end up being less precise and less actionable than what we have in mind when we refer to performance anatomy. To be explicit, performance anatomy is different in three key ways:

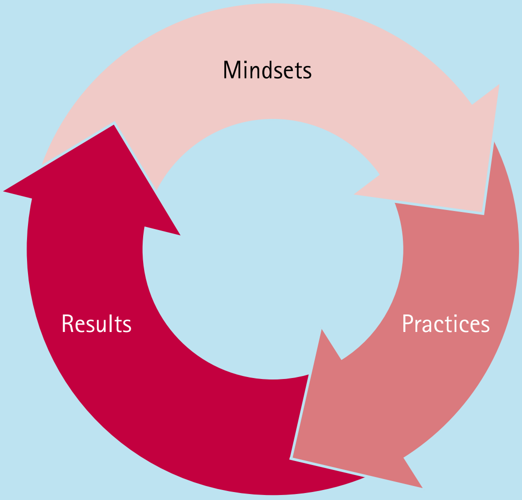
1. It represents a unique way of approaching how the core elements common to every business should be managed: leadership and strategy, people development, technology enablement, performance management, and innovation.
2. It shows how to actively manage the interaction and integration of those core elements; that is, how and why they relate to each other as they do.
3. It is not just about values and assumptions – it is a touchstone, guarded and stewarded by the CEO, that aligns the top management team.

Performance anatomy has an impact on decisions about organization design, business models, incentives and values, and top management team composition and succession planning. It affects the long-term effectiveness, quality and speed of decision-making as well as the mastery of change and innovation productivity. (For a visual representation of performance anatomy, please see Figure 5 on following page).

The challenge of creating a high-performance anatomy is considerable, because executives must commit to decisions and actions that may produce only subtle changes in the short term, even if these decisions will have enormous competitive impact years later. In too many businesses, the agenda gets swamped by today's pressing operational realities. In the sections that follow, we lay out our thinking on both the perspectives and the behaviors that characterize Chinese organizations with high-performance anatomies.

Figure 5. A virtuous circle

Think of performance anatomy as being divided into three components: mindsets, practices and results. When mindsets are aligned, they generate operational practices that lead to superior business results.



Global best practices applied by Chinese high performers

Mindset 1: Chinese high-performance businesses maintain the right balance between market-making and disciplined execution

Companies can sometimes get stuck in an "either-or" mode: Either we can manage for today and optimize returns with existing people and assets or we can invest in the hope that our next generation of products and services will be our salvation. Our global research shows that high-performance companies do both. They successfully manage the paradoxes of near- and long-term business focus, including the requirement to create both lasting stability and constant change, both management control and organizational flexibility.

Look at how Microsoft expertly manages the constant blocking and tackling of high performance. The company has established world-class distribution and customer service, for example. Yet it has also repeatedly moved into important new markets that play to its strengths, such as Internet services and video and online gaming. Other companies – Dell, Nokia, UnitedHealth, and Procter & Gamble, to name just a few – consistently demonstrate this sort of balance by weathering dramatic changes in their business environments, while remaining on top in every area in which they compete.

In China, a one-dimensional focus is fatal. It has never been a good idea for an organization to ignore the short term in favor of long-range planning, but today, in the face of increasingly demanding expectations for flawless execution, it's deadly. Leaders of Chinese high-performance businesses avoid the either-or trap by taking a "both-and" approach and surrounding themselves with talented individuals who excel in both managing the current reality and strategizing for the future. While insisting on outstanding returns from today's operations (as demanded by investors), these companies also invest heavily in what it will take to be a game-changing innovator in the future. Along the way, they catalyze new ways of thinking that open up spaces of uncontested opportunity on the one hand and build deep commitment to flawless execution on the other.

Consider how China Pharmaceutical is implementing its "two vertical strategies," which it describes as "going up to the top for technology and going down to the bottom of the market." Going up to the top for technology means pursuing leading-edge pharmaceutical technology in new product research and development as well as in new operational processes. By the end of 2006, the company had developed over 50 new medicines, including a number of patented products. Concurrently, the company is building an excellent network to supply qualified products and services to customers. Leveraging this network of over 80 sales and service entities and over 3,000 sales and marketing staff, the company now sells its products in over 30 provinces in China and in over 50 different countries.[43]

Obtaining such a balance between managing for today and for tomorrow is far from straightforward. In China, where innovation has become a national buzzword, and great emphasis is being placed on companies' ability to move up the value chain, the temptation may be to focus too much on introducing new products and services, to the detriment of current operations. Where the best companies differentiate themselves is in their ability to innovate while maintaining excellence in their current offerings. Of our more than 25 high performers, the vast majority are making significant investments in R&D and innovation. But these are not just investments for investments' sake that pay mere lip service to the government's innovation drive. They are focused on the parts of the business where the company can build on its distinctive capabilities, and they are designed to provide lasting advantages rather than quick wins.

63 percent of high performers are making significant investments in improving products and R&D.

Many of these investments occur in partnership with multinationals. Lenovo recently announced the launch of its first innovation center in India in partnership with global giants like Intel, Microsoft, IBM, and Cisco. Their shared goal is to develop new personal computer solutions for emerging markets. Baosteel teamed up with SKF AB in May 2007, the world's leading ball bearing maker, to establish a remanufacturing facility that will turn used parts into new products.[44] In 2006, Zhejiang Hisun Pharmaceutical Company, announced it had entered into a cooperative agreement with Eli Lilly. Under the terms of the agreement, Eli Lilly will provide capital support and transfer technology for producing certain drugs to its partner, free of charge. In addition, Zhejiang Hisun will select and appoint some technical and management staff to attend Good Manufacturing Practice (GMP) training conducted by Eli Lilly and Purdue University.[45] Chinese companies such as Lenovo and Zhejiang Hisun Pharmaceutical Company are building long-term strategic relationships designed around win-win outcomes for both parties.

Figuring out how to prioritize the innovation agenda is at the top of many Chinese executives' agendas. A recent study by Accenture and the Economist Intelligence Unit on growth and innovation[46] pointed out that, although executives are confident in their growth strategies, they are less confident in their companies' ability to execute those strategies. When it comes to getting innovation right, high-performing businesses are those that put in place the structures, processes and conditions that increase the likelihood that innovation will occur over the long run. Chinese companies would therefore be well-served to properly assess their core competencies, and to invest in focused research and development that closely matches those competencies and looks much further out than just a few years ahead.

Mindset 2: Chinese high-performance businesses obsessively identify and multiply talent

One of Accenture's key findings is that high-performance businesses prove more effective than their competitors at exploiting the collective intelligence and motivation of their workforces. They are far more likely to regularly measure the link between investments in people and business results. Moreover, their CEOs take a much more visible and direct role in people-development initiatives. In this way, high performers create a "talent multiplier" that becomes a hard-to-imitate competitive advantage. Those companies consider human capital development to be strategic. Rarely is this shift accomplished by simply elevating conventional human resources executives to the executive suite. Indeed, in more than one instance, we found that high-performance companies drew their HR executives from outside the HR community. And when solid advisors cannot be found within the company – as was the case at General Electric under chief executive Jack Welch – outside experts were brought in to advise the CEO.

In China, it is hard to overstate the importance of managing human resources appropriately. Despite an apparent plentiful supply of labor (nearly five million students will graduate from universities in 2007 alone), there is a shortage of experience and deep capability, especially of skilled managers and technical staff. China has committed to doubling spending on education from 2.8 percent of GDP in 2005 to four percent by 2010.[47] The government has also promised to better align the education system with what businesses need: more practical application of knowledge, practice in teamwork, leadership skills, and an increase in vocational training.

Despite such government investments, companies should not expect overnight changes in the quality or quantity of available talent. The best Chinese companies are making significant investments in the quality of the people they already have and leveraging their understanding of local employees' needs to make sure they hold onto them and tap their collective knowledge and skills. Our survey findings back this up: While the poorly performing companies believed that their workforce is a cost that has to be managed tightly, the high performers did not. More importantly, the best companies agreed that they obtain unique business advantages from the way they manage their human capital. The rest of the survey group was far less confident.

Over two-thirds of the high performers surveyed believed that they got unique business advantages from the way they managed human capital. Less than a quarter of the low performers believed so.

One Chinese high performer in the food industry illustrates how best to implement a talent-multiplier approach. Its strategy on talent explicitly states "take in, train, make good use, award and keep." With over 40 percent of its entire workforce made up of technical experts, the company's recruitment activities involve finding the best talent from over 50 colleges and scientific research institutions as well as attracting people with overseas study experience. Staff training is plentiful - more than half a million US dollars are invested each year in supporting promising technical employees while they study in universities in developed countries. Making good use of the company's workforce involves providing those employees who have creative ideas, capabilities, and development potential with challenging positions. To award and keep their best people, the organization uses a portion of sales revenue to reward those who contribute to technical innovation and new product development.[48]

Such an approach reflects the national imperative stated by the administration of President Hu Jintao and Premier Wen Jiabao. In the same way that they have promised to shift the focus of China's economic growth from quantity to quality and to "put people first,"[49] so must Chinese companies rethink what it takes to attract, motivate and retain their best talent. The signs are encouraging: Virtually all the companies we surveyed claimed to have a clear talent management strategy. Long gone are the days when companies provided workers with the same rewards regardless of individual effort. (For more details on how to manage talent in China, see Sidebar D).

Mindset 3: Chinese high-performance businesses recognize technology as a strategic asset

High-performance businesses regard IT as a source of both operational excellence and competitive advantage. They look beyond using IT as a tool for controlling costs and understand that IT is the key to capturing the business value of information. However, the strategic use of IT demands far more than just a strategy and a roomful of leading-edge systems. Top management must recognize that IT's true benefit is as an enabler of innovation and new value creation, and that this benefit will be realized only when employees use IT intensively and creatively. This extends to the use of IT in creating business insights, quality and innovation in both products and services.

For example, a global high performer in the utilities industry organizes IT implementations by business process, independent of the ultimate software application. This means that the IT organization insists that the business first figure out what it wants to accomplish in its key markets – for its customers and against its competitors – before any discussion of vendor or package is allowed. That way, management reinforces a strong connection between business strategy and technology. To measure whether the company has embraced this mindset, executives track subtle but telling signs: Is IT (as a function) involved in the creation of business innovation – that is, to what extent has it helped the company break out of its organizational silos? Do idea practitioners and corporate planners regularly attend technology and innovation conferences to keep abreast of emerging technologies? Is there an ongoing process to assess and adopt new technologies as they become economical and scalable?

Chinese high performers are becoming more aligned with global high performers when it comes to the use of IT as a source of both operational excellence and competitive advantage. Many of them are carefully examining the linkages between IT investments and business results. Such a mindset is

Sidebar D

Talent management in China

1. Make sure talent is empowered

Retention depends largely on empowering local talent. Chinese people place a premium on being recognized for their contribution and achievements. Nurturing a sense of ownership and stake in the company's performance helps generate greater levels of employee commitment and involvement. Companies need to invest in processes that adequately equip and reward their talent and engage with their staff on an emotional and intellectual level. While total compensation packages and benefits are important, the ability to provide relevant learning opportunities and clear, well-rounded opportunities for career development and advancement is seen as just as crucial, if not even more so, by Chinese staff.

2. Understand people dynamics in China

People in China tend to be more loyal to those they work with rather than to the company itself. So companies must continuously emphasize that they are committed to their employees' career enhancement, and that the organization as a whole can make far more difference than one person ever can. Executives should be objective when assessing Chinese employees' engagement levels: workers may be engaged but that doesn't necessarily prevent them from leaving. Establishing open and constant communication throughout the company will help foster greater understanding between the company and its workforce and ensure that employees' interests are being addressed and balanced.

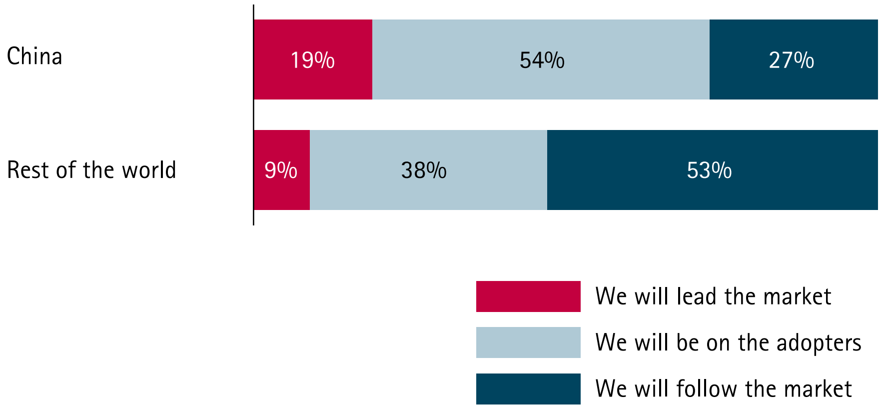
3. Develop a "learning organization"

It will take some time before businesses see the benefits of improvements to China's education system. Companies must create their own ways of nurturing and developing talent and addressing any skills shortfalls. This will involve integrating talent development into the company's core corporate strategy. By creating a learning organization, focusing on systems that cultivate the right skills needed and encouraging greater connection and interaction between new staff and the company, companies can expect to develop a strong base of talent more quickly. Not only will this reduce high turnover itself, but it will also reduce the cost of talent replacement.

Figure 6. Out ahead

In China, most CIOs believe they will either lead the market or be early adopters of innovative technologies.

How organizations will adopt innovative technologies



an integral part of high performance, especially in China, where enterprises are positioned to leapfrog several generations of IT hardware and applications, adding further momentum to their transformations. This contrasts sharply with the situation faced by CIOs in much of the rest of the world, where the complexities inherent in legacy IT mean that much more of the money in IT budgets is spent fixing and maintaining existing systems.

Accenture research[50] shows that China's CIOs differ from their counterparts elsewhere in another respect. While CIOs in other major markets tend to be technology followers, China's IT leaders and business leaders are keen to be early adopters of the most innovative IT tools. While 53 percent of their global peers were content to follow the market, a full 73 percent of CIOs surveyed in China said they wanted to lead the market (see Figure 6).

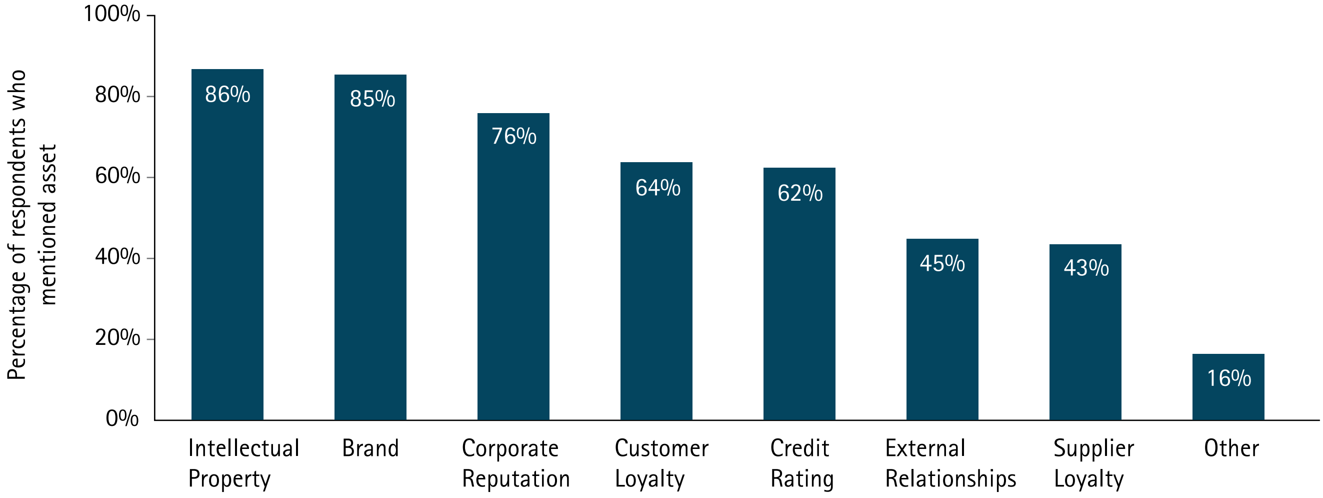
That is not to say that the Chinese high performers are implementing change for change's sake. According to another Accenture study[51], high-performance businesses often spend less on IT than their competitors do, but their investments always have strategic implications. These companies also push their technology leaders to think like business strategists and operators. As a result, an organizational mindset takes hold in which IT is seen as a strategic asset. In such circumstances, every employee and function has an understanding of the value of IT for innovation and competitiveness.

For example, a Chinese high performer in the alcohol and beverages sector has recently established an e-business platform that has boosted sales via increased customer understanding, improved brand loyalty and better quality control. In 2002, the company allocated computers to all its distributors across China and helped them to establish relationships with their customers using the e-business system. Two years later, the company provided 500 computers to franchised stores, and the stores' managers were encouraged to contact headquarters using their new tools. Finally, in 2005, the company realized online payment and settlement with the help of Industrial and Commercial Bank of China and encouraged distributors to use the B2B and B2C e-business platforms. Between 2002 and 2005, the company invested over US$16 million in this enterprise marketing and sales system.[52] As a result, by the end of 2005, the company's online sales already amounted to approximately US$13 million, and with the extension of this online sales system set to continue at a rapid clip, further positive impact on revenue generation is likely.[53]

Mindset 4: Chinese high-performance businesses understand the importance of intangible assets

Accenture's global research shows that high-performance businesses create value-centered cultures that permeate the entire organization. They recognize that future performance also depends on resources that don't appear on conventional balance sheets, and they actively manage intangible assets as a result.

Figure 7. Intangible assets measured by Chinese companies



In China, where price/earnings ratios continue to soar, it is becoming increasingly important for Chinese companies to track their intangibles. The results of our survey were encouraging in this regard, indicating that Chinese companies are establishing disciplined performance measurement for today's widely recognized intangible assets, with a particular focus on their intellectual property, brands and corporate reputations (see Figure 7). That's a good thing. Although a few leading companies such as Lenovo are already beginning to enjoy the benefits of their robust brand equity, many of their industry peers still have more to learn about everything that it takes to build and protect a corporate reputation. The ongoing concerns over the safety and quality of Chinese exports, whether justified or not, are a clear reminder of how perishable brand equity can be. They also serve to illustrate how one company's sullied reputation can hurt other companies within and beyond its industry.

Despite this progress, our discussions with Chinese clients tell us that Chinese companies do still lag behind their international counterparts in identifying those intangibles that are specific to their corporate values. For example, at Best Buy, employee engagement is a key measure for tracking business performance. Generated by survey, this measure indicates workers' commitment to the job and to the company. Best Buy, which has nearly 1,000 stores, then uses the scores to analyze how local management variations relate to each store's financial performance. In an internal study, analysts found that, in the store with the highest employee engagement score, 91 percent of the workers agreed with the statement, "I know what's expected of me at work." In the store with the lowest engagement score, only 27 percent agreed. Moreover, the store with the highest score ranked in the top 10 percent of Best Buy stores as measured by P&L budget variance; the store with the lowest score ranked in the bottom 10 percent. The company's leaders make sure that store managers are aware of the importance of these numbers to Best Buy's continuing high performance.

Such sophisticated approaches to performance measurement and improvement are integral to the successful implementation of high-performance initiatives. Chinese companies who wish to develop in a profitable and sustainable manner should take the necessary time to identify which intangible assets should be tracked on an ongoing basis and which of these assets have the largest impact on their revenues, profits and shareholder returns.

Unique Chinese best practice:

Mindset 5: Chinese high-performance businesses create a unique blend of Chinese and Western management styles

The final component of high-performance businesses in China concerns the way in which they blend complementary international and Chinese approaches to management and risk. These companies are well aware that they must continue to adopt international best practices, leveraging Chinese culture's remarkable ability to adapt and internalize new thinking. That's particularly true in the areas where Chinese organizations have traditionally been weak: corporate governance, the use of technology and risk management, to name a few. At the same time, they do not completely disregard their extensive local experience in what works best in China, nor do they abandon their Chinese heritage, traditions and culture when they expand overseas. Perhaps most importantly, these companies are determined to retain their well-documented perseverance and persistence toward success.[54]

A good example of such a 'combination' approach to management is found at Yantai Changyu Pioneer Wine Co. Ltd, in the alcohol and beverages sector. This business runs itself very much as a traditional Chinese organization: Its motto of "love the country, love the job, pursue high quality, and be the best" reflects its culture of putting the collective first. But it also has a long-term strategy that involves "combining the best from the East and West and being a trend setter". This has involved the active hiring of foreign wine experts and MBA graduates as well as sending outstanding employees to Europe and America to study international trends in the wine industry.

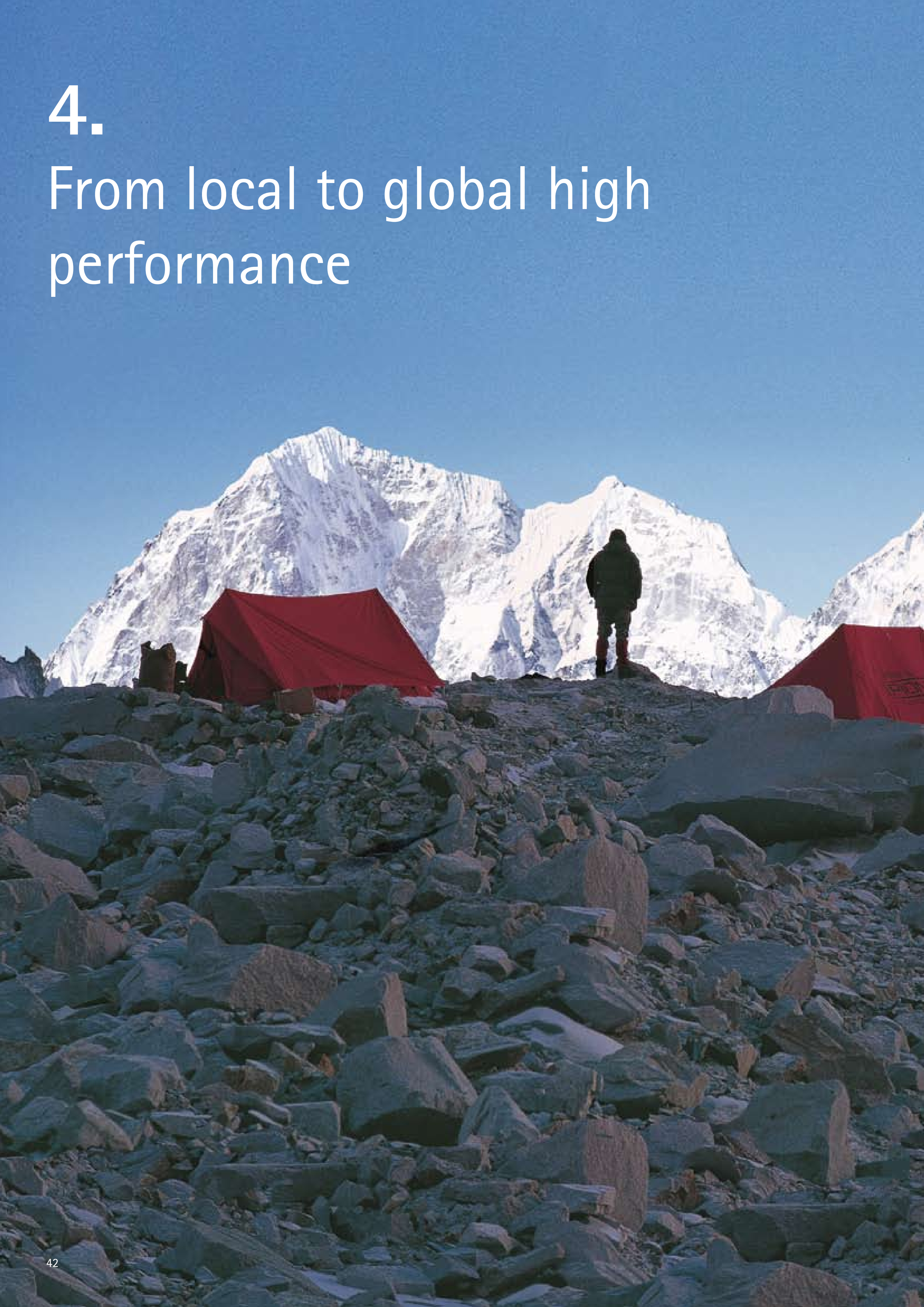
Likewise, a Chinese high performer in the oil and gas industry has benefited greatly from partnering with a number of major international oil companies to learn and then apply global best practice in the China context. The company has fostered a culture that focuses on shareholder value creation and has implemented an impressive program of investor and media relations activities, including overseas site visits. Its determination to proactively seek out and implement appropriate best practice, despite operating in one of China's protected industry sectors, will provide this company with long term advantages at both home and abroad.

A key facet of this 'combination approach' to management found in top Chinese companies is their inculcation of greater levels of risk-taking in their companies – a trait that one would certainly describe as "Western." At the same time, though, these companies balance this perspective by leveraging the traditional long-term view held by most Chinese executives to rein in the recklessness that can occur in rapidly growing markets and organizations. The result: Risk is intelligently embraced and managed. In the unique Chinese economy, these high-performance businesses occupy the middle ground between the high-quality but faint-hearted companies that are absorbed by their more assertive competitors and the aggressive companies that become overextended and badly positioned as result of poorly calculated choices.

Two-thirds of the high performers said their culture supported experimentation and risk-taking, versus only 40 percent of low performers.

Chinese high performers mark themselves apart from the competition by displaying an openness to new ideas and approaches and a willingness to implement transformational change, leveraging the best concepts and methodologies available to them. At the same time, these companies retain their core Chinese strengths and culture at the very heart of the company, regardless of whether their operations are limited to a single province in China or spread across multiple regions and countries around the world.

4.
From local to global high performance



China's business leaders are on a wild ride. They are company-builders in the truest sense of the term, guiding organizations that in many cases are doubling in size and complexity every few years. Their challenges with mastering management best practices are greatly magnified by the stresses and strains of their explosive growth.

But what exactly is "explosive"? Currently, Chinese companies can and do grow much faster than their global peers in terms of revenue growth. During the five years that our analysis covered (2001-2005), the Chinese enterprises that we analyzed across thirteen different industries grew on average three times faster than their global counterparts. The Chinese high performers almost doubled the revenue growth achieved by their global comparison peer set. Even those categorized as low performers shone brightly. (See Figure 8.)

Figure 8. Four year revenue growth performance (2001 – 2005): Chinese Vs. global peer sets[55]

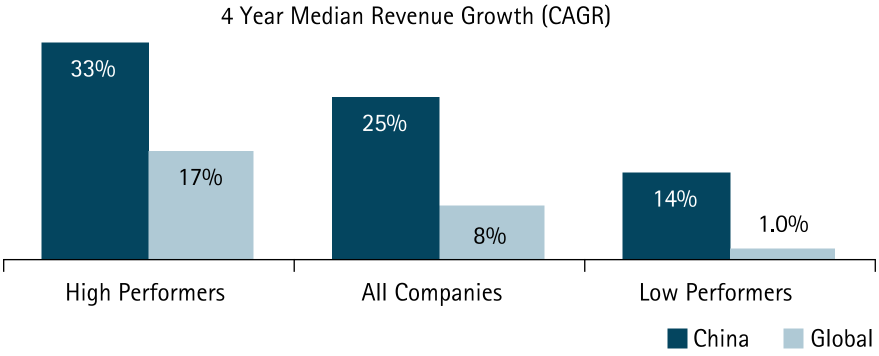


Figure 9. Five year average profitability comparison (2001-2005): Chinese Vs. global peer sets

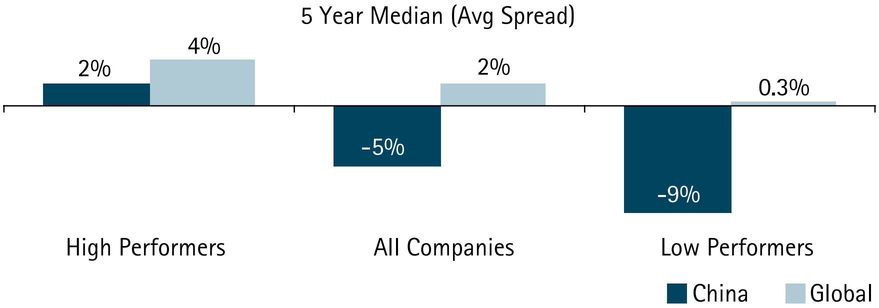
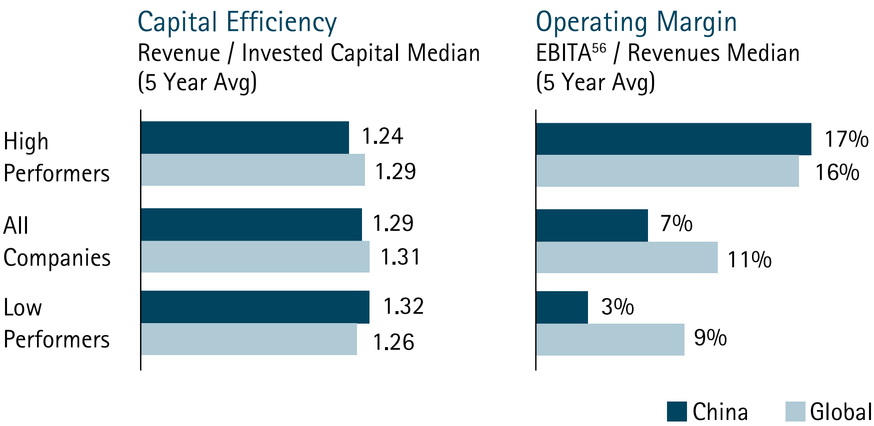


Figure 10. Five year capital efficiency and operating margin comparison (2001-2005): Chinese Vs. global peer sets



With regards to high performance in global terms, however, that is only part of the story. First, there is every expectation that Chinese companies' ability to maintain such growth in China will weaken as markets mature, consolidation continues and multinational players' participation in China's domestic markets deepens. A number of the top-performing Chinese companies have already adapted their strategies accordingly, capturing markets beyond China's borders, especially those where they have distinctive capabilities to match demand.

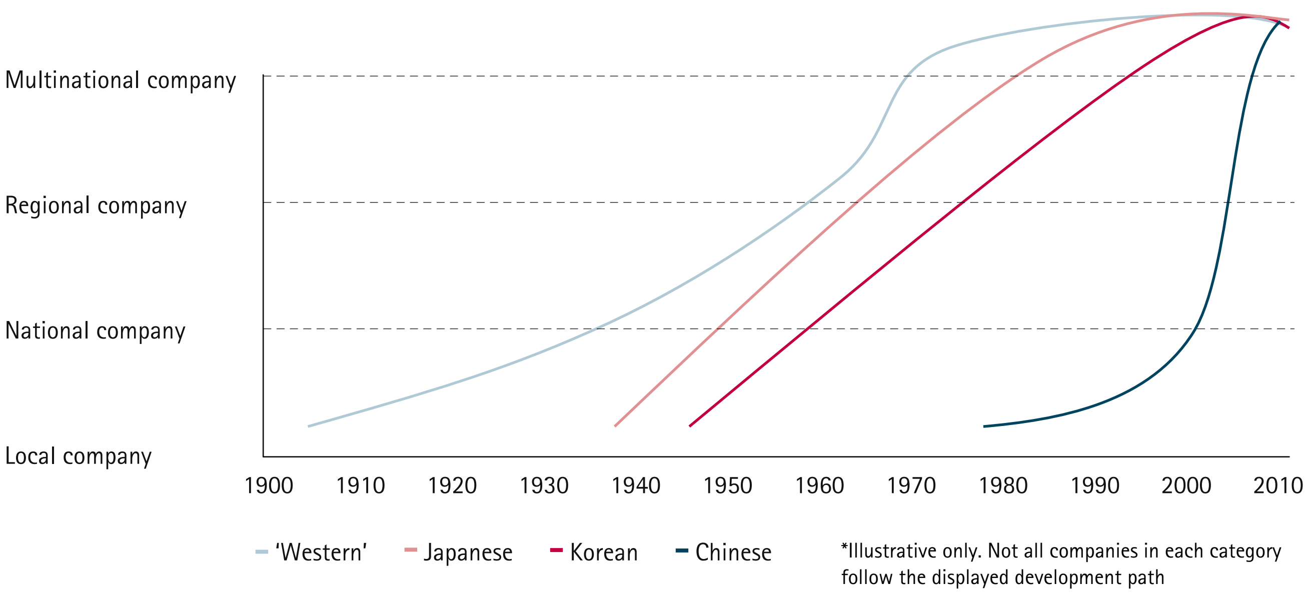
Another one of the insights from our investigation is more worrying. The tables are turned when it comes to our study of five-year profitability, as measured by examining companies' ability to return profit greater than their cost of capital. Our analysis reveals that in China, between 2001 and 2005, only the high performers managed to achieve this. And even that was only half of what the global high performers managed. The average score within our peer set of 183 Chinese companies was negative five percent while the poorest performers recorded a worrying negative nine percent (see Figure 9). Growing revenues while continuing to fall short on profitability is clearly not sustainable – either for the specific companies involved or for the Chinese economy as a whole.

By examining the underlying contributors to these profitability figures, we can identify specific actions Chinese companies can take to close the profitability gap with their global peers. Their ability to influence their cost of capital is constrained by a number of factors. These include the lack of a well developed corporate bond market and the lack of a market-driven interest rate mechanism that rewards companies' financial prudence.

Chinese companies can, however, have a major influence on their return on invested capital. The results of our cross industry analysis indicate that Chinese companies' capital efficiency already matches that of the global peer set. Their ability to create value is being hampered by their much lower operating margins. (See Figure 10).

This issue of operating margins is straight forward. It is widely understood and accepted that most Chinese companies are still operating towards the bottom of the value chain and as such are unable to command the price premiums of most of their global peers. The exceptions, of course, are the Chinese high performers. They have matched their moves toward the higher end of the value chain with their low cost structures to create operating margins that are superior to even those of the top global companies. Given the cross industry nature of our research, these findings suggest that Chinese companies should focus on moving further and faster up the value chain – regardless of the specific levels of maturity, foreign participation or regulatory pressures within their industries. By leveraging their lower cost structures, Chinese companies that focus on the creation of strong brands centered on high quality products and innovation will be able to create a long term sustainable competitive advantage in global markets.

Figure 11. The time compressed development of Chinese companies versus their global peers*



*Illustrative only. Not all companies in each category follow the displayed development path

Paradoxically, the ability of many Chinese companies to successfully go global may be enhanced by one of their unique challenges: the 'time compressed' nature of their development. If you track the historical development of multinationals, you can see that Chinese companies are trying to make the transition from being small local players to becoming true multinationals in less than 15 years – and some are succeeding. By contrast, most western companies have taken many decades – sometimes as much as a century – to reach true multinational status, and Japanese and South Korean corporations have taken 20 and 30 years to do the same. (See Figure 11.)

The challenge is producing positive results. It is equipping China's high performers with unique abilities and skills centered on speed and agility. These skills will serve them very well in the new, dynamic multi-polar world – especially as they push into other emerging markets. The consequences of dealing with such time compression are identified in this report as a superior ability to get to market quickly, using a tightly networked approach, and the ability to quickly adapt their distinctive capabilities according to internal and external drivers of change.

Of course, this does not imply that Chinese companies can expect global markets and competitors to fall before them. Far from it. Even the high performers have to be realistic about their relative lack of global business experience. Few can draw upon the business legacy that many of today's best-known multinationals share. And only a handful have anything approaching the experience of overseas engagement that is typical of most of their foreign rivals.

Accenture's key message then is this: When attempting to bridge the current gap between local and global performance, China's top performers should form a balanced pursuit of profitable growth that is based on all the components of the three building blocks of high performance. They cannot rely solely on their unique Chinese characteristics for their long-term success.

Then, and only then, will they be able to successfully make the jump from local to global influence with the potential to play leading roles in many global markets.

5.
Next steps - from understanding to action

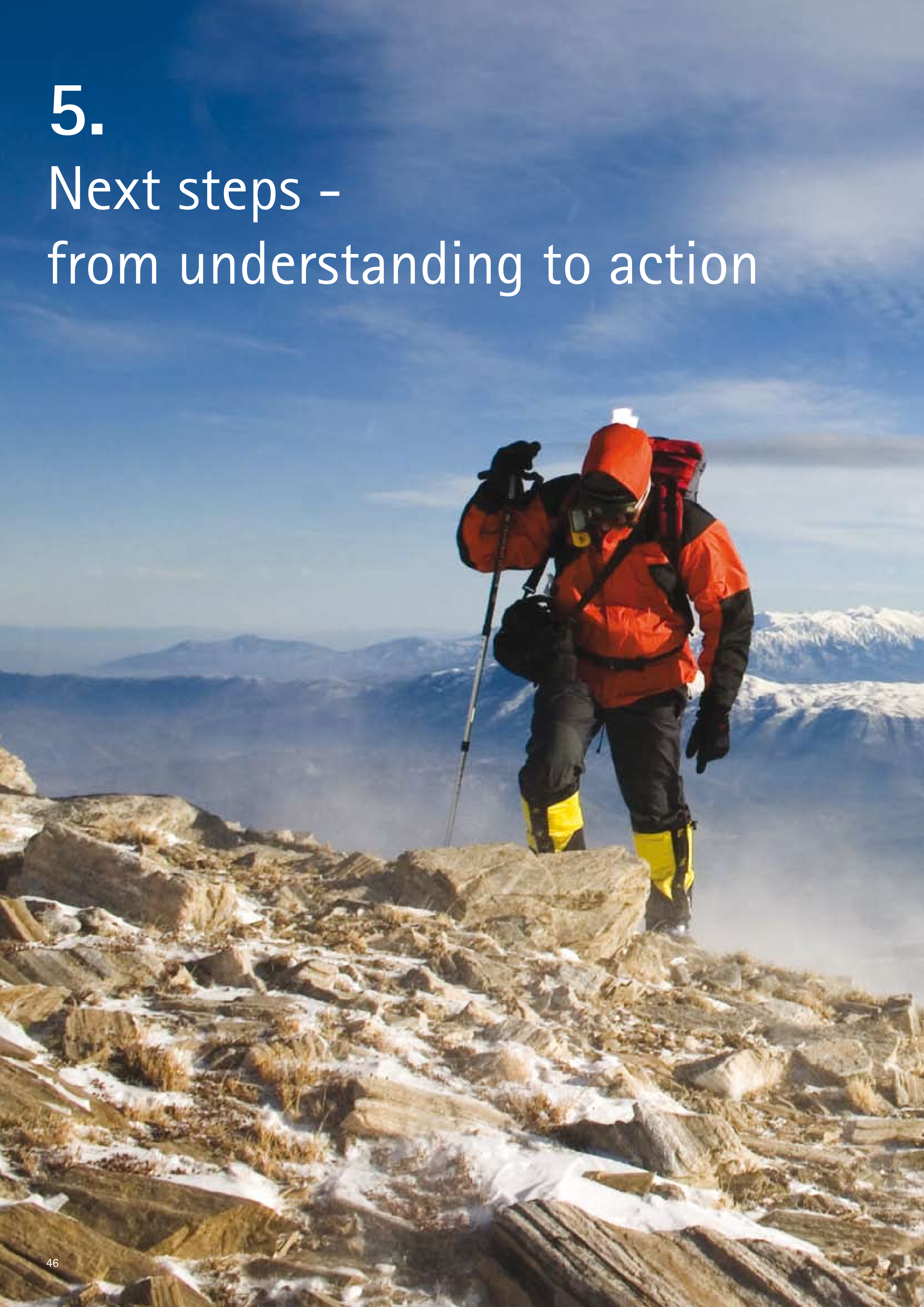
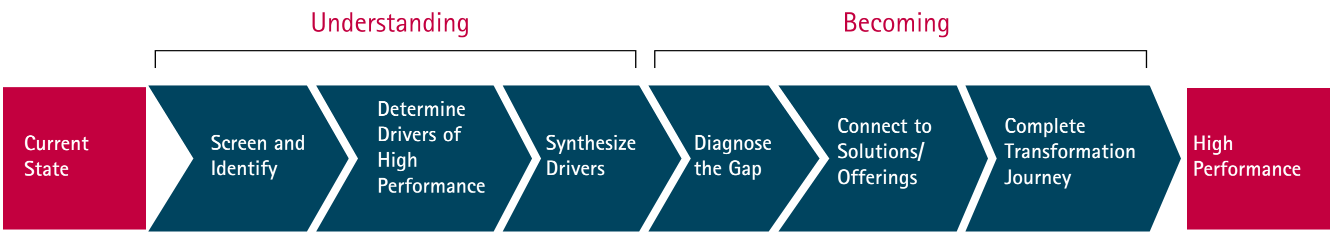


Figure 12. The journey to high performance



If Chinese business leaders absorb only one truth from this report, it should be that revenue size and revenue growth are no proxies for high performance.

However, executives who learn only one lesson from the report will be short-changing their companies. An understanding of and pursuit of all the elements of high performance has never been so vital for Chinese businesses large and small. That is why this report provides detailed and pragmatic guidance on what it takes to become – and to sustain – a high-performance business in China. It gives outcomes and actions, not theory.

Rooted in rigorous performance evaluation across many companies in many industries, the research behind our report highlights what the best Chinese businesses do differently and better than their local peers. But the report's greatest value, we believe, is in pinpointing key areas for improvement. When read thoughtfully, the study can help Chinese executives see where they can close the gaps between their companies' performance and that of their local and global competitors.

Accenture considers this report to be the first of a series of steps that many forward-thinking Chinese businesses will take as their companies journey toward high performance. Figure 12 illustrates how Accenture assists companies on this journey – first helping them understand the drivers of high performance in their industry and then working with them to complete the necessary transformations and changes to achieve it.

In China, our primary role will be to leverage the extensive experience we have gained locally and worldwide to date. Our extended role will be to help many of those businesses to capitalize on their unique capabilities – attributes that they can exploit to lasting advantage in overseas markets as well as at home.

The journey starts with a new and more nuanced understanding of what it takes to deliver sustained performance. (That understanding begins with tough introspective questions, as illustrated on page 48.) It continues with a focused and prescriptive program of change that may be uncomfortable for executives who are focused on the operational status quo. It is a journey that does not end. After all, it is far easier to become a high performer than it is to remain one – and not only in China's fast-moving domestic markets.

To those Chinese businesses on the cusp of change, we counsel their executives to accelerate their change initiatives and actively chart progress toward their high-performance goals. If they cannot now say with confidence where they are on the journey, they are a step behind where they need to be.

To those companies already at or close to the leading edge, we urge regular reviews of how well their leaders have succeeded in institutionalizing change and weaving new business processes into their companies' organizational fabric. If they cannot state with conviction that they have built high-performance cultures that employees and investors truly believe in, then their organizations may not be frontrunners for long.

Robust, sustained high performance is by no means an easy thing to master. But the exemplars show that it is absolutely possible. It is the duty of every Chinese business leader not only to manage the everyday but to master the possible.

So how will your management agenda be different tomorrow?

Ask, reflect, and discuss: 15 big questions every Chinese executive should ask:

1. How will our markets look different in the new multi-polar world?

2. Who will we be competing with five years from now, and how will those companies differ from our competitors today?

3. How is our brand perceived in our desired markets, how does it need to be perceived and what do we have to do to change it?

4. Are we managing our business in the short and long term at the same time?

5. Are we really focusing on markets where our company has unique strengths?

6. What skills will be needed for the markets we intend to compete in and where will the talent come from?

7. Are we focused on shareholder value creation and are we communicating this properly to our investors?

8. What unique characteristics will enable my company to become a high-performance business?

9. Do we truly understand what our customers value?

10. Are we using our capital in the best way to meet the demands of our customers?

11. Are we really using our IT strategically and as a source of competitive advantage?

12. Are we investing enough in our intangible assets such as our brand?

13. Are we creating the right blend of Chinese and Western management approaches?

14. Where are the biggest gaps between our performance and that of China's high-performance businesses? And that of the world's best high-performance businesses?

15. Can we candidly say we have a strategy and an operating plan to become a high-performance business? Has this been communicated throughout the business?

Research methodology

A sturdy research pedigree

Over the years, Accenture has amassed an unparalleled body of knowledge about what it takes to become a high-performance business. Our proprietary High Performance Business research initiative is a multi-million dollar program that spans thousands of companies across the globe. Prior to extending the program to China, we had already conducted in-depth analysis on more than 6,000 companies and identified over 500 "high performers" – companies such as General Electric, Toyota and Procter & Gamble, and many others.

Our initiative is obviously not the first effort to codify high performance. Nearly a quarter of a century ago, the famous book "In Search of Excellence" was published with that quest very much in mind. But Accenture's research is the first not only to conclusively identify the hallmarks of high performance but to develop useful insights that help aspiring companies accelerate their push to high performance – and help today's top performers stay that way.

Unlike other approaches which simplistically equate high performance with raw financial metrics – revenue size or operating income, for instance – Accenture's High Performance Business research grades on a curve. A company is deemed to be a high-performance business if and only if its performance is substantially and statistically better than its peers across a range of aggregated measures – over several years. By examining so many metrics among peers in an industry set, we are able to gain a highly informative "apples to apples" picture of differential performance by industry. Accenture's approach has been lauded for its rigor by the Harvard Business Review journal.

How we measured high performance in China

This High Performance Business in China report is based on two phases of research: quantitative, then qualitative. First, Accenture's proprietary method of performance evaluation was applied to the China market to identify the high performers. We began by screening companies using the following broad criteria:

- Annual revenues had to exceed RMB 1 billion, based on publicly available data from listed Chinese companies incorporated in mainland China.
- The companies had to be listed (on local or overseas stock exchanges), with at least 50 percent of the companies' sales generated in China.

That screen narrowed our list to 748 companies across 36 industries. To advance to the second stage of screening, companies had to be listed on the capital market for more than five years.

The third screening level involved selection by industry. Since China's capital markets are far from mature, many Chinese companies, particularly the State-Owned Enterprises, are not listed. For an industry group to be included in the research, the sum of the market capitalization of the companies we could analyze had to make up at least 50 percent of the total market cap of the industry. A final consideration in selecting the industry groups was whether the company had examined an equivalent global peer set that would enable direct comparisons to be made between the two. By this point, we had narrowed the scope of research to 183 companies in 13 different industry groups. (See: Industries examined.)

Finally, we commenced our statistical analysis of the financials of the 183 companies. Accenture's High Performance Business methodology involves assessing companies' five core areas of performance by analyzing 11 financial metrics from publicly available sources (see Figure 13 for details). Each metric is then gauged for statistically significant outperformance of its industry peers.

Each company's performance was then compared to that of its peers on each measure and rated based on the degree to which it over- or underperformed its peers. The specific ratings for each measure were consolidated, creating one grade score for each company. Hence the definition of the absolute performance required to achieve High Performance Business status will vary based on an industry's established performance norms.

When our quantitative analysis was complete, we had recognized a number of Chinese companies as having significantly differentiated and superior performance to the others within their industry peer groups. We also compared the performance of those exemplars with that of our body of global high performers.

The research then moved to the qualitative phase. A detailed 63-question survey was carried out with 75 senior executives from Chinese companies (including 16 of the high performers) in order to help us understand how the most successful Chinese enterprises are achieving uncommon business success. The survey was split into six sections: markets; strategy and organizational structure; investment and returns; regulatory environment; workforce management and culture; and operational management and performance management.

Industries examined

Alcohol & beverage
Food products
Household appliances
Consumer electronics
Steel
Pharmaceutical
Industrial equipment
Chemicals
Computers & peripherals
Textiles
Utilities
Telecoms
Oil & gas

Figure 13. Detailed breakdown of financial metrics

Industry Peer Set Screen	Component Metrics
Profitability measured by the spread between the return on invested capital and the cost of capital.	• 3 Yr. Avg. Spread • 5 Yr. Avg. Spread
Growth measured by revenue expansion.	• 3 Yr. Revenue Growth CAGR • 5 Yr. Revenue Growth CAGR
Positioning for the Future measured by the portion of share price that cannot be explained by current earnings (what we call future value) and by the portion of the industry total that each company's future value represents.	• 5 Yr. Change in Relative Future Value • 5 Yr. Level in Relative Future Value
Longevity measured by the duration of out performance in total returns to shareholders, a performance area important to our requirement of sustained value creation over time.	• 3 Yr. Total Return to Shareholders CAGR • 5 Yr. Total Return to Shareholders CAGR
Consistency measured by the percentage of time that a company's performance has been greater than median performance in terms of profitability, growth and positioning for the future.	• 5 Yr. Median Outperformance in Rev. Growth • 5 Yr. Median Outperformance in Spread • 5 Yr. Median Outperformance in Future Value

Definitions of Financial Terms

Spread = Return on Invested Capital (ROIC) less Weighted Average Cost of Capital (WACC). Measures a company's ability to generate returns on invested capital that are greater than the relevant cost of that capital.

Return on Invested Capital (ROIC) = Net operating profit less adjusted taxes (NOPLAT) / Invested capital (capital provided by debt and equity investors).

WACC or Cost of Capital (CoC) = Debt/EV*(Kd)*(1-Tr)+Equity/ EV*(Ke), where Kd is the cost of debt, Tr is the marginal tax rate (determined by country of operations), Ke is the cost of equity, and EV is the enterprise value of the company (debt+equity).

Future Value (FV) = a shareholder value-based measure of investors' expectations of the value of a company's cash flow growth. The metrics we use reflect two variables of FV (change and level) and are equally weighted:

Change in FV =
(Average FV A - Average FV B) / 2-yr. avg. invested capital

Level of FV =
5-yr. avg. FV / 5-yr. avg. invested capital

Consistency is measured as the percentage of years over a five-year period that the company has outperformed its peer set median in each of a set of measures.

Consistency is measured across the following output metrics:

- Year-over-year revenue growth
- Annual spread
- Annual FV/Invested capital

Total Returns to Shareholders (TRS) measured as share price appreciation including dividends:

$$\text{TRS CAGR} = \left[\left(\frac{\text{Ending stock price} + \text{Accumulated dividends}}{\text{Beginning stock price}}\right)^{\wedge(1/n)}\right] - 1$$

References

1 Toward a Theory of High Performance, Harvard Business Review, July 2005

2 Li Rongrong: Speed up SOE Reform, Cut Down the Number of SOEs by 4000-5000 Each Year, People's Daily, December 2005

3 Chinese Wage Increases Outpacing Economic Growth, Forbes, Feburary 2007

4 Accenture analysis of four-year revenue growth performance 2001-2005 across 12 industries

5 Thomson Financial and Dealogic figures

6 ICBC Debuts in Hong Kong Bourse, Xinhua Agency, October 2006

7 China's Biggest Bank Gets Approval for IPO, Xinhua Agency, July 2006

8 JP Morgan, PricewaterhouseCoopers and World Federation of Exchange figures

9 National Statistics Bureau figures

10 Outline of National Plan for Medium to Long-term Scientific and Technological Development (2006-2010)

11 Since China's capital markets are relatively immature and many Chinese companies have only been listed for a relatively short time, we shortened the timeline for the analysis used at the global level from 10 to five years (2001–2005). Given the proven resiliency of our research model, we also included a very small number of companies listed for three or four years only if we believed that their exclusion would render the analysis incomplete for that particular industry.

12 Out of the 13 industries finally included, textiles is the only one that does not have a corresponding global peer set.

13 JD Power & Associates reliability survey results

14 Midea Started the 'Revolution of AC Popularity in Towns and Villages', TOM Technology Channel, April 2005

15 China Mobile's Hot Signal, BusinessWeek, February 2007

16 Countryside Campaign Boosts China Mobile Returns, Forbes, March 2007

17 Hangzhou Steam Turbine Running towards International Market, Hangzhou Daily, October 2005

18 Lenovo's SME Market Share Jumps to 39 Percent, CCID, April 2007

19 First Chinese WM6.0 Mobile, Lenovo ET600, eNet, March 2007

20 Operation Management Reform Fully Implemented, Company Website, August 2006

21 Yunan Baiyao: Steady the Center and Emphasize Two Wings, Eastmoney.com, August 2006

22 China's Dairy Sector, Catching Up with Demand Growth?, Rabobank, October 2006

23 Work on Core Business and Carry on to be the Leader of the Coloured Woven Textile Industry, China Textile, Feburary 2007

24 Analysis based on company annual report figures and Accenture methodology

25 Midea Annual Report 2005

26 China Mobile's Hot Signal, BusinessWeek, 05 February 2007

27 China Business Post, March 2007

28 Changyu Internationalization's Bypass, China New Time, August 2006

29 PR is Necessary for the Company's Development, Company Website

30 To Keep Developing Chinese Medicine Culture, TRT Built up Museum in its Courtyard, Xinhua Agency, April 2007

31 Xinhuacun Brand Strategy Planning, Study365, 2004

32 Research Shows China Historical Famous Brand's Value are Hugely Diversified, Xinhua Net, August 2006

33 Why Winning the Wallets of China's Consumers is Harder than You Think, Outlook Journal, September 2006

34 Inside the Mind of the Chinese Consumer, Harvard Business Review, March 2006

35 Brand Strategy of the Competitors, Capital Steel Daily, May 2007

36 Broker Call - Kweichow Moutai a 'Buy' on Liquor Brand Value - Citigroup, Xinhua Financial News, April 2007

37 Moutai: Cutting Edge on E-business, ChinaByte, March 2006

38 On the Information Highway, CCID, October 2006

39 On the Information Highway, CCID, October 2006

40 Dongfang Boiler CIMS Projects Implemented, Quick-React Ability to Market Increased, ChinaBBC Network, September 2001

41 Shuanghui – First Brand of the Chain Store Model in China's Meat Industry, China Sales Communication Network, September 2003

42 Changyu's Brand Marketing and Direct Sales, New Fortune, June 2006

43 Two Vertical Strategies Kept Shijiazhuang Pharmaceutical ahead in Technology, Hebei Daily, March 2007

44 BaoSteel and SKF JV for a Bearing Restore Factory, SKF website, May 2007

45 China's Hisun Seeking Foreign Investor, Hires UBS, Reuters, April 2007

46 'Moving from Strategy to Execution to High Performance, Outlook Journal, Issue 2, October 2006

47 National Education 11th 5 Year Plan

48 Develop the Brand, Make the Enterprise Strong, Shuanghui Group, MofCom Website, August 2006

49 The CEQ on FT.com: Putting people first, 10 April 2007

50 Getting IT Right the First Time, Outlook Journal, May 2006

51 Breaking Away, Outlook Journal Special Edition, May 2004

52 Moutai: Cutting Edge on E-business. ChinaByte, March 2006

53 Moutai: Cutting Edge on E-business. ChinaByte, March 2006

54 Knowing the Business Environment: The Use of Non-Market Based Strategies in Chinese Local Firms, Ivey Business Journal, November 2005

55 Chinese peer set consists of 183 Chinese companies in 13 different industries. Global peer set consists of 277 companies from matching industries (excluding textiles which has not been examined at the global level).

56 Earnings before the deduction of interest, tax and amortization expenses

About Accenture

Accenture is a global management consulting, technology services and outsourcing company. Committed to delivering innovation, Accenture collaborates with its clients to help them become high-performance businesses and governments. With deep industry and business process expertise, broad global resources and a proven track record, Accenture can mobilise the right people, skills, and technologies to help clients improve their performance. With approximately 158,000 people in 49 countries, the company generated net revenues of US$16.65 billion for the fiscal year ended Aug. 31, 2006. Its home page is www.accenture.com.

For more information visit www.accenture.cn/research or contact andrew.sleigh@accenture.com and taylor.guo@accenture.com