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MOTIVATING PEOPLE

What China's Shift to a Service Economy Means for Its Managers

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There is no doubt that China has been one of the main engines of global growth in the last three decades. Essential to this economic success story has been China's role as "the factory of the world." Their reliance on export-dependent manufacturing is, however, coming to an end. As China moves away from a manufacturing-driven economy to a more consumption and service-driven model, Chinese companies will have to find new ways of managing and motivating their employees.

A manufacturing-driven economy has different requirements than a service-driven one and thus brings forward the question whether the incentive systems used to motivate employees in the former model will still work in the latter model.

A manufacturing model motivates employees through tangible financial means, often a one-to-one relationship: the more you get paid, the better you will perform and thus produce. This approach often prioritizes quantity over quality. In the past, this belief was very much reflected in China's customers' preference for lower-quality but cheap products. Moreover, this type of incentive system to motivate employees also aligned well with the more traditional management structures in Chinese companies where decision-making is centralized and leadership is equated to a large extent with adhering to quotas and other pre-established criteria.

A service-driven economy, however, faces different demands and requires a different approach to incentive systems. In a service-driven economy, customers cannot be lured in with cheap, low-quality offerings. Now, customers will demand high-quality products, and for that they are willing to pay more. To differentiate your company, it thus becomes necessary to communicate to customers why you are in the business of selling this particular product and what value it brings to the customer. This shift changes the kind of incentives required.

Simply motivating employees by paying them more when they perform better only installs a calculative type of thinking. Research has demonstrated that a consequence of such a mindset is that employees will pursue more their own self-interest, rather than the interests of other stakeholders including the customer's interests. Workers simply try to sell as many units of the most profitable products as they can. This is a problem, because for obvious reasons, in a service-oriented economy, companies need employees motivated to create not only short-term financial gains, but also long-term non-tangible outcomes for both the company and customers. It is exactly this dilemma between using tangible versus non-tangible incentives that Chinese companies are facing today.

To illustrate this problem, consider the following example. A milk company in Zhejiang province is developing strategies to attract customers based on their value of promoting healthy lifestyle. They've invest considerable financial resources in R&D to develop more innovative and healthier products. The aim of these investments is to achieve sustainable growth by being able to serve customers better by providing them access to higher-quality products. In turn, such service-oriented focus should result in long-term profits. The incentive system used in this company is to motivate sales managers by allowing them to earn a certain percentage of the monthly profit made. Based on interviews we conducted, it became clear that this kind of merit pay system, with a sole focus on the use of short-term tangible incentives, rather created a motivation to sell only the products that proved most successful in the past as those would create most financial value for themselves. The downside of this system revealed itself, however, in the way that managers were not motivated to provide better service by introducing their customers to the new and healthier products. The incentive system thus clearly created a calculative culture that undermined entirely the company's long-term efforts. As a result, the use of this financial incentive system led to significant losses for the company on the investment side, and as a result did not allow them to grow in becoming a company that serves the customer in better and more innovative ways.

In fact, the effects were particularly negative when it came to creating loyalty with the customers. An excessive focus on profit margins for their own pockets made the managers working in each of the shops less customer-oriented. No real interaction between sales people and customers existed, no information about the products of the company and the value it could create to the customer was communicated (remember, health is an important value of the company), and eventually customers did not feel treated well. As a result, customers did not develop a loyal attitude to the company that would promote a long-term relationship. Only when discounts were offered by the company did sales go up again. The calculative mindset of the managers, as induced by using only tangible incentives, created a similar attitude among customers. This clearly hurt profit margins.

Companies competing in a service-driven economy need employees who are flexible, pro-active, and creative in delivering the value a company's products stand for to the customer. These are requirements that cannot be qualified in immediate tangible consequences — therefore, the use of only tangible incentive systems is likely to fail. Rather, more non-tangible incentives will have to be used to motivate employees to be more effective and creative in promoting customer loyalty.

Research by Dan Ariely (Duke University) is particularly insightful in this respect. His studies, first of all, showed that using financial incentives worked to promote performance of employees on routine tasks that are highly repetitive. The more they were paid, the better they performed; a logic that fits well with the demands of a manufacturing economy. More interesting, however, is that his research also revealed that when employees had to engage in creative tasks, using only financial incentives did not improve performance. In fact, performance on creative tasks sometimes worsened when money was the primary incentive. This underscores the idea that tangible financial incentives do not create more value in tasks (and by extension economies) where non-tangible outcomes need to be achieved. This underscores the idea that tangible financial incentives do not always create more value in tasks. The problem is that incentive systems are often designed incorrectly and reward outcomes that are contrary to what the company desires. Put differently: The problem is usually with the design, not the incentive. This emphasizes that financial incentives should be used wisely and in conjunction with other practices and rewards when non-tangible outcomes need to be achieved.

So, what are Chinese companies - or any companies in an economy making the shift from manufacturing to services — to do?

A first important task is to train employees in ways that they understand (a) the value the company wants to create for their customers (e.g. selling milk products because the value of a healthy life style is the reason for your business), (b) how they should treat and interact with customers (e.g. employees should learn to know how and when to apologize, to listen, and to help beyond their contractual requirements), and (c) the importance of a pro-active attitude in helping the company to innovate and achieve sustainable growth over time (e.g. helping to promote the newest products and not only sticking to selling what is known to sell well).

A second task is to develop incentive systems that include both tangible and non-tangible elements. It is important for companies to realize that if money is the only thing you have left to manage, then you will without a doubt encounter serious problems on the long-term. Put differently, if employees are used to do something extra only when they are paid for it, then no culture will be created where employees will voluntarily show citizenship behaviour. Research indeed shows that if people are motivated only in financial ways then any kind of intrinsic motivation will be eliminated and they will only be extrinsically motivated to do their job. Thus, the presence of tangible incentives easily cancels out the value people assign to non-tangible rewards. For this reason, it is necessary in service-driven economies that employees are first and foremost motivated on intrinsic and thus not-tangible grounds and only if this is achieved financial incentives can be added to the package.

A third task involves a change in how leadership is practiced. For centuries, the Chinese traditional view on leadership relied on hierarchy and the use of employees' sense of duty to get the work done rather than making use of self-developmental styles in which tasks are delegated to employees so they can develop their own sense of ownership when it comes down to serving customers. The reason for this is that the more traditional way of looking at leadership includes the principles of centralized decision-making and tight control of execution and as such aligns well with the Confucian values of respecting hierarchy and the resulting focus on maintaining harmony to control and structure interpersonal relationships. As the economic situation is entering new territory, Chinese organizational leaders may also have to explore different leadership styles that are focused more towards creating a sense of inclusion for all of their employees while at the same time promoting their sense of ownership. Such a leadership approach carries with it the promise to build fertile ground for all employees to embrace the values the company stands for.

China's massive transformation towards a service-driven economy ultimately rests on its workforce. A manufacturing economy has different requirements than a service economy. To deal with this challenge, one important focus for Chinese companies will be to train, educate, and incentivize their work force in ways that develop a pro-active attitude motivated by an intrinsic desire to create long-term customer value.

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