Business

THE CHALLENGES OF SUCCESSION

HANDING OVER THE REINS OF POWER CAN BE TROUBLESOME

By KAREN YIP

Lenovo Group Ltd may not want to disclose its succession plans but at least it has one. There's a good reason for the secrecy: Revealing who is going to replace whom puts the group at a disadvantage because it will encourage competitors to recruit its best people.

If history is an indicator, power or ownership transition is always difficult and most of the time, it will hurt.

"Chairman Liu (Chuanzhi) and CEO Yang (Yuanqing) realized that Chinese companies struggle with succession planning. The cornerstone for us is creating the next generation of leaders. The board worries about it," Kenneth DiPietro, senior vice-president of human resources at Lenovo, says.

Lenovo's board of directors, Yang and DiPietro discuss key moves within the organization once every year.

"We even create scenarios of possibilities such as 'what if we move this person to another department, what will happen?' or 'if this person is put here, what sort of results can we expect to see?'. This helps us to build up the skills and capacity of certain people," he says.

The process, which was adopted four years ago, speaks volumes, especially when Lenovo is up against other Chinese mainland companies in terms of corporate governance.

Most Chinese chief executive officers and founders are young, the majority of them being in their 40s or 50s. Starting succession planning now doesn't carry as much importance as pursuing bigger profits and expanding into new markets.

The limitation of companies is not access to talent, DiPietro says. "The question is also not always about funding for mergers and acquisitions. As we move into new markets and new technology space, we ask ourselves: 'How are we going to execute with depth?'"

Three decades after China's economic reform, the country's private sector, especially companies that have become globally competitive, will soon face the question of how to hand over to the next generation.

Liu Chuanzhi, Lenovo's chairman, is 67 and so is Ren Zhengfei, founder and president of telecom solutions provider Huawei Group. Zhang Ruimin, founder, chairman and CEO of Haier Group, a consumer electronics producer, is 62. Zong Qinghou, founder, chairman and CEO of Hangzhou Wahaha Group, a leading beverage maker, is 66.

Referring to succession planning in corporate China, Liu Shengjun, a professor from China Europe International Business School, says: "Usually they don't have a plan or they don't think it's necessary to have a plan. If they have a plan, it's usually poorly hatched."

He says the challenges that corporate China will face or is already facing are that founders are getting old, companies are getting too big to manage and companies are going global.

"Professionals are needed. Leaders with global vision are needed. But Chinese CEOs prefer to work life-long like Hong Kong tycoon Li Ka-shing. What they need are assistants rather than successors," he says.

When the 82-year-old Li was suddenly hospitalized in 2006, shares in his listed companies immediately sank.

In a joint study conducted on 250 companies controlled by ethnic Chinese families in Hong Kong, Taiwan and Singapore, Joseph Fan, a professor at the Chinese University of Hong Kong found that successions tended to go along with major declines in the stock value of these listed companies.

"If you hold shares valued at 100 yuan ($15) five years before the succession, the value will drop to 40 yuan by the time the company announces a succession," he says.

"It's a very challenging task. Most Asian companies have not done well. Those that have done well took 15 years to plan a succession," Fan says.

More than planning, succession requires founders to look deep at their lives and families too. "How many times they return home to eat, how many mistresses and children out of wedlock they have… all these matter," he says.

Even if succession is well planned, the ferocity of the business environment in China poses extra challenges to companies, he says.

A change in local government officials, unforeseen recession or macroeconomic changes, or starting the succession in a hostile business environment can find companies unable to turn against the tide.

When Lou Zhongfu first built Dongyang-based Zhejiang Guangsha Co Ltd in the 1970s into the multi-industry group it is today, he had the foresight to show his two sons the ropes in the hope that they could take over from him when he retires.

However, the listed Zhejiang Guangsha Co Ltd performed poorly over the years, which were predominantly affected by uncontrollable events. When the Dongyang local government changed hands in 2001, 2005 and 2007, even the well-connected Lou had to rebuild connections several times over while watching the company's debt rise due to various outstanding infrastructure projects.

Since 1993, Guangsha Group has invested 400 million yuan in the construction of infrastructure such as Dongyang Children's Park, Xishan Park, Guangsha Baiyun Culture City and Tiandu City Huanle All Season Park.

The listed company performed poorly in the stock market over the years and reported losses of 177 million yuan in 2005 and 272 million yuan in 2006. In the same year, the company found itself embroiled in credit scandals over defaults involving large loans.

In 2010, the listed Zhejiang Guangsha started to install a new set of board members and is expecting to turn the corner, backed by an experienced team.

Fan expects fights for control of Chinese mainland companies to be more severe than their other Asian counterparts due to a vacuum in values in current Chinese society.

"We used to say family businesses tend to survive up to the third generation. With poor family governance, businesses in China can only last one generation," he says.

He predicts that most of the Chinese entrepreneurs may sell their businesses before retirement and transfer their capital out of the country.

"It's very unfortunate if this were to happen. You can sell assets but not brains. Intellect cannot be passed down to the next generation," he says.

In addition, the one child in most Chinese families mean that it will be tough going for entrepreneurs to pass on to family members.

It's understandable that most founders of businesses in Asia and Europe desire to keep them within their families.

It's not surprising that most founders of companies believe that blood runs thicker than water.

Huawei's President Ren Zhengfei had promoted Li Yinan, a bright young executive, to be his second in command and potential successor. However, Li left Huawei in 2000 to start a rival company, which was later bought by Huawei in 2006.

For the first time, Huawei began disclosing biographies of its board directors in the group's 2010 annual report in order to be more transparent and "adopt a market-oriented corporate governance structure as part of its growth strategy".

While companies can outlive their founders, founders cannot live for centuries.


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