Does human resource management matter in a transitional economy? – China as an example

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Abstract

This paper investigates the significance of how firms manage their human resources (HR) within the confines of powerful social institutions in a transitional economy, the People's Republic of China (China). We propose that two dimensions, the role of human resource management (RHR) and followers' perception of the leader (TOP), are important contributors to firm performance as are the influences of the regional economy and firm ownership. We tested our hypotheses with a survey of 180 firms from nine cities in China. We found that both role of HRM (RHR) and follower's perception of top-level management (TOP) are important to firm performance. The study confirms that while social institutions remain powerful in a transitional economy, effective HRM is important to firm performance.

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– China as an example

How foreign and local businesses manage their operations effectively in a transitional economy like the People's Republic of China (China) depends on how they manage within the confines of the country's powerful institutions. These institutions include formal organizations, such as social, economic and political bodies, and the social norms and rules such bodies articulate (North 1990; Scott 1995). Taken together, they represent China's established institutions and ideological frameworks that govern how individuals and firms behave.

The first of the institutions is China's mixed economic system. While the country is undergoing a rapid transition to a market economy, researchers have noted that the old political systems still exercise major influences on the country's economic activities (Child & Tse, 2001). Many industries are still influenced by the entrenched and centrally planned economic system (Boisot & Child, 1996; Nee, 1992; Peng & Heath, 1996). Concealed government subsidies including soft-budget constraints (Kornai, 1992) and market barriers imposed by inter-locking firm relationships are known to twist China's market. Within this hybrid system of the old and the new as well as the conservative and the liberal, many foreign firms choose to operate in places with explicit laws and policies to ensure that their operations are not hampered by China's conflicting political agendas (Lin, 1998).

The second institution is China's system of local governments (Walder, 1995). Since 1978, China's national (i.e., central) government has continuously delegated its authority to local governments to implement and, at times, to interpret nation-wide policies. Local governments can exercise discretion in setting taxes, specifying entry barriers and creating administrative red tape for businesses operating in their jurisdictions (Lin, Cai & Li, 1996).

Some local governments function as “economic warlords” and protect firms that they own from those they do not own. Firms need to maintain good relationships with local governments in order to operate successfully.

Past studies have confirmed the salience of these two institutions as foreign firms enter into China. Tse, Pan and Au (1997) found that MNCs chose specific location and entry modes as strategies to work with China’s powerful institutions. In the sino-joint venture literature, Beamish (1993) found that a good firm-government relationship is essential.

Does this evidence imply that firms need only to pay attention to China’s economic and governmental institutions when they operate in China? With China’s entry into the WTO, many market barriers will be removed voluntarily by the Chinese government as part of their state-owned enterprise (SOE) reform and involuntarily by country-to-country negotiations. As China’s institution begins to change, the contribution of quality firm management to firm performance is a timely research issue.

This paper is an attempt to look at the impact of two variables, namely the role of the human resources management and employees’ perception of top-level management, on firm performance within China’s institutional forces. We argue that these variables work under firms with different ownership types that operate at different location in China. The paper has three objectives. First, it aims to substantiate the relationship between HRM and firm performance in China. Second, the paper assesses the effectiveness of two key dimensions of HRM on firm performance. The dimensions are the strategic role of HRM and employee’s attitude towards their firm leader. Third, the paper examines the effects of each HRM dimension on firm performance. In a country that is characterized by changing and complicated institutions, the study seeks to answer the question, “does good HRM matter?”

Firm Performance in Transitional Economies

As former centrally planned economies move towards open markets, institutions woven into the cultural and ideological fabric of the country do not suddenly disappear. Rather, these intricate economic, social and political systems with long-established goals and rules continue to shape the distinctive institutional milieu within which firms need to work (Peng, 2000). China is an exemplar of the transitional economies. When China opened to the world in 1978, studies have confirmed that how firms perform depend on how they manage within the country's powerful institutions.

Studies have found that a critical success factor in sino-joint ventures lies in the choice of local partners (e.g., Beamish, 1993) because local firms and local governments can form systems of "network capitalists" with intricate firm-to-government and firm-to-firm relationships through reciprocity treatments (Boisot & Child, 1988) that benefit one another. To succeed, a firm needs to find powerful partners that are part of these networks. In his seminal work, Walder (1995) demonstrated that China's local governments might operate as powerful "warlords" within their jurisdictions.

Market entry studies have shown that firms adopt specific entry strategies to reduce their exposures to risks imposed by China's powerful institutions. Tse, Pan and Au (1997) found that American firms preferred to enter Special Economic Zones and coastal cities where laws and policies were explicitly specified. Studies have also showed that the firm-government relationship is a significant determinant on firm equity investment decisions (Pan and Tse, 2000) and firm performance (Pan, Li and Tse 1999).

Luo and Peng (1999) reported that ownership type, a proxy for firm-government relations, is a significant performance contributor. As Peng (2000) postulated, China's social institutions remain a core component in understanding how firms operate and perform in the country.

From External Institutions to Firm Effort

Does the significance of institutions on firm performance imply that good human resources management practices are unimportant in China? Could firms succeed simply by crafting good relationships with the local governments and locating their businesses in markets with good potential? In economies that are severely twisted by past regulations and government subsidies, this may indeed be the case. Yet, China's situation is quickly changing.

Since 1990, China's national government has found it increasingly difficult to cover the massive losses incurred by its ailing SOEs (Tse and Lau, 1999). By 1997, the debt created by China's SOEs accounted for 66% of its national debt and, if allowed to grow, these debts will crush China's weak and protected financial systems. The failure of the country's SOEs will consequently erode China's remarkable economic accomplishments over the past twenty-five years. Thus Chinese leaders are committed to reforming failing SOEs, allowing them to reorganize, close down or be acquired by non-government businesses. The reform has de facto begun to remove a long-standing barrier to free market operations.

Another major change is China's entry into the WTO. Bilateral negotiations have removed barriers to competition and turned most of the country's industries into free markets. Even in restrictive sectors such as banking, telecommunications, and retailing, China agreed to gradually open these industries to allow competition and force a decline in its powerful institutions (Child and Tse, 2001). The current study is cast in this context. We postulate that, in China, a firm's internal management will affect its performance, even though influences from China's institutions remain significant. We choose to assess the impact of good HRM, a core component of a firm's strategy. Human resources management is an important management function in China because the HRM department is the one that set the organizational norms and culture of a firm. With effective HRM, a firm would be able to build up strong organizational values, high employee commitments and team cultures, which are critical to firm performance (see, e.g., Tjosvold, Law and Sun, in press; Wong, Wong, Hui & Law, 2001; Law, Wong, Wang & Wang, 2000).

HRM as a Sustained Competitive Advantage

According to the resource-based model of the firm (Barney, 1991; Wright & McMahan, 1992), when a firm's human resources are strategically aligned to fulfill the firm's goals, good HR practices will help improve firm performance (Becker & Huselid, 1998). Twomey and Harris (2000) found that firms with appropriate HR systems would encourage continuous improvement and breakthrough innovations. Huselid (1995) provided substantial evidence that HR practices used in a strategic sense would improve productivity and firm performance and reduce employee turnover. Taylor, Beechler and Napier (1996) postulated that HR systems contributed to a firm's competitive advantage because they helped develop specific human capital and generated tacit organizational knowledge.

Taylor, Beechler, and Napier (1996) classified HR practices into tangible competences and intangible competences. Huselid, Jackson and Schuler (1997) extended it to two HRM outcomes within a firm, namely strategic and technical HRM effectiveness. Strategic outcome describes "how well the HRM function developed a firm's employees to support its business needs" whereas technical outcome describes "how well the HRM function performed activities traditionally associated with personnel management" (p.175).

Recent studies have confirmed that sound HR practices enhance organizational performance (Delaney & Huselid, 1996), productivity, sales turnover (Huselid, 1995) and the firm's financial performance (Huselid, Jackson & Schuler, 1997). We adopt Huselid, Jackson and Schuler's (1997) proposal on the types of outcomes from HRM and the findings of Burton, Lan and Lu (2000) in China to delineate two HRM contributors to firm performance in China: the strategic *role* of HRM and the employees' attitude towards top management.

The strategic role of HRM within a firm refers to the salience a firm gives to the HR department in its key strategies. In China, many MNCs that face the shortage of capable management talent (Ralston, Egri, Stewart, Terpstra & Yu, 1999) and highly price-competitive market, resort to develop their local staff through intensive training programs. A firm's HR strategy is now commonly accepted as a top management priority in China. Bae and Lawler (2000) confirmed that the salience of HR management in Korean firms, that is, how HR is valued within an organization, affects firm performance. We hypothesize that:

H_1: In China, firms that recognize and emphasize the strategic role of the human resource department would perform better than those that do not.

Employee's Attitude of Top Management

Effective leaders are essential to good HRM system. Effective leaders articulate the need for sound HR practices and skillfully sail through organizational processes for these practices to develop and sustain (Boal & Hooijberg, 2001). This is especially salient to firm management in transitional economies where uncertainties and risks would imply business failure and massive layoffs. In their in-depth studies of China's successful firms, Burton, Lan and Lu (2000) attributed firm success to the effectiveness of their leaders. In Haier and Kelon, China's emerging giant appliance firms, a common success factor has been how their top management won the acceptance of their employees to decisively capture their market opportunities.

Similar postulates can be found in the emerging strategic leadership theories (Boal & Hooijberg, 2000) in which how leaders' capacity to learn, change, and manage are core attributes. In China's collective (inter-personal) cultural orientation, leaders' ability to navigate through socially complex institutions is critical to their success. They have to articulate for change that the firm's past, present and future come together (Gioia & Thomas, 1996). This is often regarded as the social intelligence leaders need to possess so as to win the confidence of their followers.

Respect for corporate leaders is especially salient during China's continuous and overlapping reforms (Child & Tse 2001; Hui, Law & Chen, 1999). Since 1998, massive layoffs have happened to senior executives, mid-level managers and front-line workers alike. Planned HR deployments and activities designed to enable a firm to achieve its goals (Wright & McMahan, 1992) need the support of employees from all ranks. This cross-level acceptance is consistent with the proposition that HR management is a control system (Ouchi, 1977) that monitors the input, outputs and behaviors within the organization.

A firm may have senior managers who think and act strategically, yet without front-line workers to implement its strategies, the firm will not perform well (Shipper & Davy, 2002). Thus, we propose that for HR systems to contribute to firm performance, it is the acceptance of senior management leadership at the worker's level that will lead to better firm performance. We hypothesize that:

H_2: Higher levels of employee attitudes toward firm leadership will be associated with higher levels of firm performance.

As discussed, our study aims to assess the effectiveness of HRM in relation to China's two powerful social institutions: regional development (representing different degrees of openness in the economy) and firm type (representing the influence of local governments).

Regional Development and Firm Performance

Since 1978, China's state government has adopted market-oriented measures to stimulate firm performance. Tse, Pan & Au (1997) showed that firms in various regions in China perform at different levels because of three factors: the investment climate, government support and purchasing power.

As the cornerstone of its modernization strategy, China has created five Special Economic Zones (SEZs) and 45 open coastal cities sequentially. These regions extended preferential tax incentives to foreign and local firms and at the same time allow these firms to autonomously recruit, reward, and dismiss their workers. Studies based on manager surveys (Beamish, 1993) and large-scale databases (Tse, Pan & Au, 1997) have confirmed that these incentives and the degree of openness to the market economy have been effective in attracting investments and improving firm performance. Yet, in other parts of China, firms continue to struggle within the bureaucratic structures.

Different treatments that firms receive result in large variations in economic success across regions. Some areas, like Beijing, Guangdong or Shanghai outperformed the rest of the country economically. People in these regions and cities have enjoyed three times higher per capita income than the national average. This large regional income disparity implies that firms located in these prosperous regions have more opportunities to capture the region's purchasing power. Thus, we expect firms in more developed cities in China will perform better than firms in less developed cities.

Ownership Type and Firm Performance

One significant change in China's economic transformation has been its changing industrial structure. In 1978, there were only SOEs (83,700 of them producing 80.8% of the country's GNP) and collectives (264,700 of them producing 19.2% of the GNP). By 1995, four types of firms contributed to the country's economy: SOEs (118,000 SOEs producing 33.9% of China's GNP), Town and Village Enterprises (TVEs; 1,475,000 TVEs producing 36.6% of the GNP), privately owned firms (5,688,200 firms producing 12.9% of the GNP) and other forms (60,300 Joint Ventures and shared enterprises, producing 16.6% of the GNP) (State Statistical Bureau, 1992-96). This dramatic shift of economic power has been the focus of many studies that have investigated firm evolution (Peng & Heath, 1996), management practices (Yan & Gray, 1994), organizational structure (Boisot & Child, 1988), readiness to change (Lau, 1997; Lau, Tse and Zhou 2002) in the new Chinese economy.

SOEs are former industrial giants owned and operated by the State government. In recent years some of them have been hampered by out-dated technologies, insufficient financial resources, corruption, and inefficient management systems. Sino joint ventures have up-to-date technologies, modern management systems. They are able to attract foreign capital for growth. Recently, another category of firms, the shared (or joint) stock companies, in which equity shares belong to workers, the state and/or private investors, has emerged.

Among the firms, the most surprising successes are the collectives. While most of them are regional, low-tech, labor-intensive and cottage-industry firms, their sudden rise reflects the power China's local governments (Walder, 1995). Local governments are allowed to set up and implement policies as long as they are not in conflict with national guidelines. As a result, many local governments are actively involved in forming and operating firms with local investors to improve their financial resources. Motivated by selfinterest, local governments are known to use unequal fees, soft budget subsidies, entry barriers, differential profit taxes, and regional policies to ensure that the collectives they own survive and continue to grow (Tse and Lau, 1999).

Past studies found that among the different types of firms, collectives perform the best, followed by joint ventures (JVs) and then the SOEs (e.g., Li, 1998). Following these general research results, we propose that other things being equal, collectives outperform JVs, which will outperform SOEs in China.

It should be noted that regional development and firm ownership are not control variables in the conventional sense because they have been and continues to be part of China's strong institutions. By nature, they encompass the influences of variables external to (such as firm-and-government relationship, inter-firm reciprocity) and internal to the firm (such as core competence, incentive systems). Being institutions, they represent complex and interacting systems of factors that are salient to how various management practices operate. Our study focuses on the effects of strategic role of HRM and perceived top management leadership. This is because strategic role of HRM and top management perception are intellectually rich and managerially relevant constructs that provide direct insights to managers and management researchers on how to improve firm performance.

METHOD

Sample

The sample in this study consisted of 3,964 respondents from 180 firms in nine cities in China recruited through a multi-stage sampling procedure. We first group all Chinese provincial capital cities into three stages of economic development based on their average "worker and staff member income" in 1995, which were the most recent figures available from the State Statistical Bureau (SSB). From each group, three representative cities were selected. The cities selected were: High growth - Beijing, Shanghai, Guangzhou; Medium growth - Nanjing, Wuhan, Chengdu; and Low growth – Xian, Changchuan, Guiyang.

We then randomly selected 20 firms from the manufacturing sector in each city according to the national industrial statistical data bank supplied by the SSB. These 20 firms had a balanced representation of ownership structures because we deliberately sampled an equal number of SOEs, JVs, town and village collectives (called collectives thereafter), and shared stock enterprises. Many collectives are owned by cities, towns, villages, or municipal governments. Shared stock enterprises, are formed by SOEs or collectives, many of which were originally owned by the State or municipal governments. The owners of shared stock firms distribute ownership shares among themselves.

We sampled only the manufacturing sector because in other sectors there were fewer types of ownership structures. Only firms with 100 or more employees were included in the sample. On average, 15.6 firms were included in each type of firm in each city in the sample. We deleted an average of 4.4 firms in each group in our final sample because some chosen ones had declared bankruptcy and some refused to participate in the study.

In the final stage, we obtained the employee list supplied by the personnel department of each firm. We eliminated the employees who were not involved in the core businesses of the firm such as firm-run kindergartens or hotels. We then selected 22 employees as potential respondents. They included a senior personnel manager, a senior marketing manager, 10 randomly selected middle-level managers and 10 randomly selected low-level employees. A new name was added whenever a potential respondent declined to participate in the survey. On average, the response rate was 60 percent. The data were collected in a six-week time period starting in November 1997.

Individual-Level Data. Individual data were collected through face-to-face interviews with each respondent. Since non-Mainland researchers were not permitted to make direct contact with Mainland residents, a major market research company in Beijing with branches in all nine cities was commissioned to conduct the interviews. All respondents were informed of the confidentiality of their responses. Most interviews were conducted at the respondents' homes. Others were interviewed in the research firm. Each respondent was given a cash gift of 20 yuan (about 2 US dollars, more than three hours of an average daily pay). We hired one experienced research assistant independently who traveled to seven of the nine cities to monitor the fieldwork. The assistant contacted 1,150 (out of 3,960) participants to confirm that the research company had conducted the face-to-face interviews. No cheating was found.

Firm-Level Data. Firm-level data on profitability and productivity were first obtained from the SSB. These data were confirmed in a questionnaire completed by the senior personnel manager. After deleting data points for which firm performance data were not available and a few cases of extreme outliers, the number of firms in the final sample for this study was 122.

In forming the final merged sample at the firm level, we used the ratings by the senior personnel manager on the strategic role of the HR department in the firm (RHR) because he or she would be more knowledgeable than the marketing manager about the roles played by the HR department in the firm. The correlations among the two manager scores are high at around 0.7.

With respect to the perceptions of leadership of top-level managers (TOP), we use the ratings of front-line workers because they are those who implement firm plans and strategies. The final sample of 122 firms, therefore, consisted of ratings of top level management practices by front line workers; a rating of the role of the HR department in the firm by the senior personnel manager; and categorical variables showing the geographic location of the firms and firm ownership structures.

Size is an indicator of a firm's financial strength, which affects a firm's willingness to adopt modern management ideas or technologies. In a socialist economy, size can mean bigger financial budget and more bureaucratic power, so the influence due to size may not be as straightforward as that in a market economy. We used the number of employees (NUM) as an indicator of firm size and included it as a control variable.

Dependent variables. We used two business performance measures including: (1) the ratio of the firm's profitability in 1996 to its equity (ROE) and (2) the firm's productivity or the logarithm of the ratio of the firm's income in 1996 to the number of employees (PRODTY). Since the second performance measure included the number of employees, NUM was not used as a control variable when we analyzed this dependent measure.

Location. The cities included in the survey were grouped into three tiers according to their stage of economic development. Beijing, Shanghai and Guangzhou were considered to be highly developed cities (coded as Loc1=1; Loc2=0); Nanjing, Wuhan and Chengdu were considered to be developing cities (coded as Loc1=0; Loc2=1) and Xian, Changchuan and Guiyang were considered to be under-developed cities (coded as Loc1=0; Loc2=0).

Ownership. In each city, the SOEs were coded with an ownership dummy variable as Own1=1. Similarly, the JVs were coded with a second dummy as Own2=1. The collectives were then coded with a third dummy variable as Own3=1. The last ownership type, shared stock enterprises, was indicated by a zero code in all three ownership dummies (Own1=0; Own2=0; Own3=0).

Role of the Human Resource department (RHR). The strategic role of the HR department was determined from a 5-item measure. It was rated by the senior personnel managers using

6-point scales (as shown in Table 1). Two sample items were “The head of our HR department participates in the strategy formulation and development of our firm” and “Top managers in our firm frequently consult with the HR department for advice.” The coefficient alpha of the five items was .84.

Employee Attitude towards Top Management (TOP). We asked front-line employees to rate their attitude towards top management of their firm along four 6-point items. Two sample items were “Top managers in our firm are very united and cohesive” and “Top managers in our firm are brave enough to be creative and risk taking”. The coefficient alpha was .86.

Analyses

We test our hypotheses by block-wise multiple regression analysis. The firm performance measures were used as dependent measures and the role of the HR department as rated by the senior personnel manager (RHR) were first entered in the regression after the control variable size. This step was then followed by top management leadership as rated by front-line workers (TOP). The location and firm ownership variables were then added at the end of the regression run to test their incremental effects on the dependent variables. The significance of the change in the model’s R-square and F-value when a block of variables was added to the model was used as an indicator of how well the added predictors perform.

This sequence of block-wise regression runs was conducted because we are interested in how HR practices affect firm performance. We added the effects of location and ownership because they are known to have powerful influences on firm performance.

RESULTS

<u>Scale measuring RHR and TOP</u>

We factor analyzed (with VARIMAX rotation) the 9 items used to measure the strategic role of the HR department (RHR) and employee attitude towards top management (TOP) using the master sample of 3,960 respondents. Results in Table 1 shows that two factors with Eigen-values greater than unity are identified. The first factor (explaining 35.6% of the variance) contains six items measuring top management respect (TOP). The second factor (explaining 34.1% of the variance) contains the remaining five items designed to capture the strategic role of the HR department and is labeled as RHR. This shows that the 9 items have discriminant validity and they measure two different dimensions of HRM well.

Effects of predictors on firm performance

Correlations among the variables in this study are shown in Table 2. Results of the regression analyses are shown in Table 3. Four observations deserve our attention. First, Front-line employee attitude towards top management registered significant effect on ROE ($F=4.07$, $p < .05$) but not on PRODTY ($F=.13$). So, H_2 is partially confirmed. Second, the strategic role of the HR department, as perceived by the senior personnel manager (RHR), has significant effects on ROE and significant effects on productivity ($F=5.13$, $p<.05$). Given that the relatively small sample size ($N=122$) does not have enough statistical power to generate highly significant results, Hypothesis 1 is considered to be supported.

Third, the stage of economic development of the cities where the firms were located (Loc), has significant effects on productivity ($F=6.48$, $p<.01$) but not on ROE. Fourth, firm ownership type (Own) has significant effects on both ROE and PRODTY. The changes in the F-value for the effects of ownership on ROE and PRODTY are 4.88 ($p<.01$) and 22.29 ($p<.01$) respectively.

It is not too surprising to obtain inconsistent results between return on equity and productivity. Use of capital-intensive equipment, which increases productivity, will require high financial commitments, which means the investment will lower the return on equity causing a discrepancy in these two variables.

We performed additional post-hoc analyses on top of the regression results. Since firm ownership type has a strong effect on firm performance, we compared the correlation patterns between the two HRM variables and firm performance by different firm types to check if the effect of HRM would differ across firm types. The results, shown in Table 4, confirmed that this was the case. The correlations between RHR and TOP and ROE in JVs and shared stock enterprises were .52 ($p<.01$), .36, .34 and .16, respectively, while those for SOEs and collectives were -.23, .17, .15 and .12, respectively. Similar correlation patterns between PRODTY and RHR and TOP were obtained. In shared stock enterprises, the correlations between PRODTY and RHR and TOP were .45 and .23, respectively, while those in SOEs and collectives were -.01, .13, .07 and -.10, respectively. These results imply that the HRM variables have strong to moderate effects on firm performance in JVs and shared stock enterprises while their effects in SOEs are negative and those in collectives are much smaller.

Table 5 shows the ANOVA results of ROE, PRODTY and the HRM variables by ownership type and the location of the firm. For PRODTY, significant main effects for ownership type and location were obtained. Collectives reported the highest productivity, followed by shared enterprises and JVs and SOEs. For ROE only the ownership types registered significant main effects. SOEs had lower returns as compared with JVs, collectives, and shared enterprises. The effects of regional development and firm ownership were confirmed.

DISCUSSION AND CONCLUSION

In this pioneering effort to assess the impact of different dimensions of HRM on firm performance in a transition emerging economy like China's, four results are worth noting. First and most important, the study establishes that HRM is important to firms' financial and operational performances. The relationship between strategic HRM and firm performance was only recently confirmed in the U.S. (Delaney & Huselid, 1996; Delery & Doty, 1996; Huselid, Jackson, & Schuler, 1997; Youndt, Dean, & Lepak, 1996). This is encouraging for international business managers because powerful socio-political forces are known to affect firm performance in transitional economies. In short, good HRM does matter to firm performance in a transitional economy.

Second, the study contributes to the existing literature by investigating two dimensions of HRM: the strategic role of HRM in a firm and employee attitude towards top management within a firm. These dimensions prove to be instrumental in our understanding of firm performance in transitional economies like China's. The strategic role of HRM in a firm has been shown to affect a firm's productivity while employee attitude towards top management has been shown to affect firm profitability. Yet, such impacts are not universal across firms. The correlation analysis by ownership type (Table 4) confirms that while some SOEs may recognize the key role HRM plays, their inability to execute HRM policies limits them from capitalizing on the benefits of such practices. This is reflected by the positive and significant correlations between the strategic role of the human resource department and a firm's return on equity in JVs (.52) but not in SOEs (-.23). Many HR departments in SOEs are still run like the traditional personnel departments. Instead of being a component of a firm's strategy, their role is to ensure "that necessary paper work was correctly filled in, that all the T's were crossed and the I's dotted" (China Staff, May 2002, p.4). At present, many of China's SOEs are operated as government offices, most HR tasks in SOEs are to ensure that decisions are politically rather than economically correct. It is, therefore, understandable that the more powerful the HR departments in SOEs are, the more political the enterprises will become, and the lower the chance that the firms will have good economic performance.

The third notable finding is that, in transitional economies, the senior management team's ability to work together and lead, especially as perceived by the front-line workers, is critical. Put simply, this finding suggests that in firms in China in which most employees used to enjoy the benefits of a permanent but not permanently non-performance-based compensation system, called the "iron rice bowl", how effective HR practices are regarded by the front-line workers directly impacts a firm's performance.

As China continues to seek ways to manage its inefficient SOEs better, the findings of this study suggest that a new ownership structure is a viable alternative. Currently, the central government is encouraging SOEs and collectives to become privatized. Our findings lend some support to this initiative. The new firm type, shared stock enterprises, outperforms SOEs, JVs and collectives. This suggests that shared stock ownership is more effective in motivating firms to perform efficiently and effectively (Child and Tse, 2001) . As some firms have found, turning employees into owners encourages them to reduce costs, foster a strong team spirit and help each other to perform better. In a transitional economy where workers are used to sharing the "iron rice bowl", this new ownership form may encourage them to rethink their work ethics and enhance their output. Perhaps the free-rider effect and spending sprees of firm resources can be reduced.

One difficult challenge in reforming the country's economy is the reengineering of the SOEs. Most SOEs are known for their inefficiency and lack of concern for profitability. Under the old planned economy, SOEs survived and grew through managing their socio-political networks in a manipulated economic system (Peng, 2000). From being the "privileged few" China's SOEs are now fast slipping into the "defeated masses" (Li & Tan, 1997).

This study finds that although the introduction of modern management concepts such as applying good HRM have the potential to improve firm performance, this effect seems to be significant in shared stock enterprises and JVs but not in SOEs or collectives. Since 1978, many SOEs that tried to introduce new management insights into their operations have failed. This study seems to suggest that there may be a prima facie for HR change, that is, HR change needs to be accompanied by a change in ownership. Unless a firm's employees recognize that their performance is directly linked to their firm's futures as well as their future, many of our modern management innovations may prove futile.

There are three limitations in this study. First, the study does not measure how firms perform on the functional aspects of HR practices. This limits us to examine the effect of HRM on firm performance comprehensively. Second, the small sample size in the survey also limits the type of analyses one can perform. Third, other than the strategic role of HRM and perception of top management, there are variables attributable to organizational type and location that are of salience to firm performance. Their effects need to be addressed in future studies.

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Table 1. Factor loadings of the items on the two human resource factors in the exploratory factor analysis.

Items	TOP	RHR
Top managers in our firm are very united and cohesive.	**.89**	.30
Top managers in our firm are fair in their decisions.	**.90**	.22
Top managers in our firm are brave enough to be creative and risk taking.	**.84**	.25
Top managers in our firm are well united with all employees in this firm.	**.75**	.30
The head of our HR department participates in the strategy formulation & development of our firm.	.30	**.74**
Top managers in our firm frequently consult with the human resource department for advice.	.27	**.78**
Our human resource department has the right to challenge the HR decisions of other departments.	.12	**.73**
Top managers in our firm use human resources as a critical competitive advantage of our firm.	.32	**.73**
Top managers in our firm believe that human resources are critical to our success.	.23	**.76**
Percent variance accounted for by factor	35.6%	34.1%

Table 2. Correlations among the variables in this study [a, b, c]

	ROE	PRODTY	NUM	RHR	TOP	DEV1	DEV2	OWN1	OWN2	OWN3
ROE	1.0									
PRODTY	.41**	1.0								
NUM	.10	.13	1.0							
RHR	.21*	.21*	.16+	1.0						
TOP	.18+	.03	-.04	.25**	1.0					
DEV1	.05	.30**	.21*	.05	.09	1.0				
DEV2	.02	-.09	-.15	-.17+	-.23*	-.53**	1.0			
OWN1	-.36**	-.38**	.07	-.18+	-.07	-.04	-.07	1.0		
OWN2	.04	-.27**	-.28**	-.10	.06	-.02	.02	-.34**	1.0	
OWN3	.14	.50**	-.17+	.02	.01	.01	.01	-.35**	-.32**	1.0

[a] N=122
[b] **p<.01 *p<.05 +p <.1;
[c] Loc1=Developed provinces; Loc2=Developing provinces;
Own1=SOEs; Own2=JVs; Own3=collectives.

Table 3. Effects of Role of HR (RHR), Employee Attitude (TOP) and Ownership (Own), Location (Loc) on Return on Equity & Productivity [a, b, c, d]

Order of Entry	Return on Equity (ROE)			Productivity (PRODTY)		
	β	ΔF	ΔR^2	β	ΔF	ΔR^2
1. NUM	.11	1.15	.01	--	--	--
2. TOP	.15^{+}	4.07*	.03*	-.02	.13	.00
3 RHR	.11	3.07^{+}	.02^{+}	.12	5.57*	.05*
4. Loc1	.04	.94**	.10**	.31**	6.48**	.10**
Loc2	.09			.07		
5. Own1	-.33	4.81**	.10**	-.33**	22.28**	.32**
Own2	-.03			-.27**		
Own3	.03			.30**		
Adj Multiple R			.36**			.65**

[a] N=122
[b] **p<.01 *p<.05 $^{+}$p <.1;
[c] the β-weights are the regression weights of the final regression model.
[d] Loc1=Developed provinces; Loc2=Developing provinces;
Own1=SOEs; Own2=JVs; Own3=collectives.

Please note that in block-wise regression analysis, it is a standard practice to put in F-value and change in R-square for each ***set*** of variables. The significance of the betas in the final regression equation is not a good indicator of the usefulness of a group of variables in predicting the dependent variable for two reasons. First, it is difficult to interpret betas for more than one variable. Second, betas of the final regression equation can be affected by multicollinearity, if any. A better approach to assess the effect of different groups of independent variables on the dependent variable is to enter them one at a time as a block. Their significance, therefore, are assessed by the incremental R-square and F-value.

Table 4. Effects of HRM variables on firm performance by firm type.

	Return on Equity	Productivity
SOEs		
RHR	-.23	-.01
TOP	.19	.15
Collectives		
RHR	.15	.07
TOP	.14	-.11
Joint-ventures		
RHR	.52**	.09
TOP	.30	-.15
Shared Enterprise		
RHR	.34+	.45*
TOP	.13	.20

**p<.01 *p<.05 +p <.1.

Table 5. Firm performance and HRM variables by ownership-type and location [a,b]

	Main Effects		Interaction	Group means						
				Firm-type				Location		
	Firm-type	Location	Firm x Loc	SOEs	JVs	Share	Coll.	Under-developed	Developing	Developed
ROE	6.23^{**}	.05	1.79	-.03	.01	.03	.02	.00	.01	.01
				SOE < (JV = Share = Coll.)						
PRODTY	24.31^{**}	8.01^{**}	.84	1.52	1.58	1.90	2.16	1.65	1.73	1.95
				(SOE = JV) < Share < Coll.				(Dev'd = Developing) < Under-dev'd		
RHR	3.93^{*}	2.78^{+}	1.02	3.56	3.65	4.08	3.79	3.89	3.59	3.81

[a] the first three columns are F-values of the ANOVA analyses; the rest of the other columns are mean values
[b] $^{**}p<.01$ $^{*}p<.05$ $^{+}p<.1$