



# THE PUZZLE OF INNOVATION IN CHINA - ADDING THE MISSING PARTS

- + **Innovation:** the key to continuing growth in China
- + **A plan for the future:** setting an innovation road map for MNCs
- + **Overcoming barriers:** taking the lead with proactive measures
- + **Looking inward:** a way to identify innovation capabilities

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# 01 EXECUTIVE SUMMARY

## ❖ *Innovation is vital for future growth in China*

The times when China could prosper by simply drawing on excess low-cost labor are over. Today the country is transforming into an innovation powerhouse and Multinational Corporations (MNCs) must keep pace to catch up with local competition. This report aims at providing companies with a framework for shaping their individual road maps toward innovative product, service and business models.

## ❖ *MNCs are realizing the significance of innovation but lack operational development*

Innovation in China is among the top priorities of MNCs, who have started to recognize the importance of innovation for customer-specific products. Yet the majority have no well-defined innovation road maps in place.

## ❖ *A concrete plan is required to systematically translate innovation into action*

A well-structured innovation road map is a prerequisite for driving innovation further and helps MNCs add the missing parts to their puzzle of innovation. This includes not only China-oriented product management, but also close cooperation with the international headquarters regarding product engineering and the overall product pipeline. By pursuing a clear innovation strategy, MNCs can evolve from import oriented companies into global innovation motors.

## ❖ *Barriers to innovation can be overcome*

Barriers to innovation reduce the overall speed of progress and might stem from a lack of innovation skills, intellectual property concerns and restrictive headquarters. However, barriers are not set in stone and proactive measures can help to move beyond them.

## ❖ *Self-assessing capabilities help to identify the missing part for driving innovation*

Identifying and benchmarking one's own innovation capabilities raises awareness of strengths and weaknesses regarding innovation performance. By using goetzpartners' Innovation Benchmarking Tool, concrete areas for improvement can be derived and the remaining parts of the overall innovation strategy added.



## Methodology

The opinions and data presented in this report are based on goetzpartners' work experience with multinational corporations in China. In addition, a comprehensive innovation survey was jointly undertaken with our partners from renowned Chinese institutions. In cooperation with Professor Zheng Han, Chair of Innovation and Entrepreneurship at Tongji University, and the German Chamber of Commerce in Shanghai, we interviewed more than 100 German corporations operating subsidiaries in the Chinese market, with two thirds of them being present in China for more than ten years. Although the survey focused primarily on the automotive and industrial sectors, many of the lessons can be applied to other industry segments as well. In addition, the results of the survey made a valuable contribution to the development of the goetzpartners' Innovation Benchmarking Tool.



## 02 NEW CHALLENGES AHEAD FOR MNCs

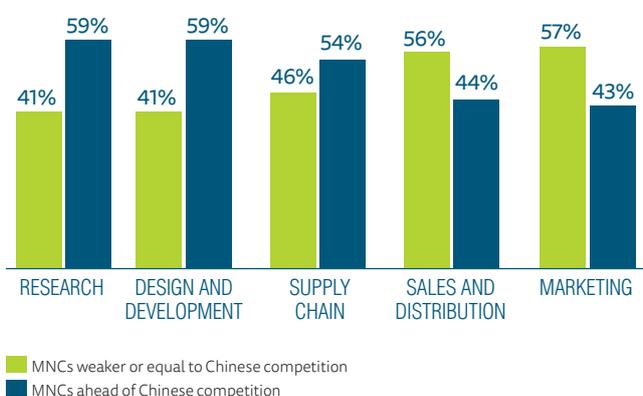
Once again, China has arrived at a turning point. Since the opening of China's economy in the late 1970s, the country has experienced double-digit growth rates averaging 10% during the last thirty years. Never before has an economy succeeded in lifting hundreds of millions of people out of poverty and become so powerful globally in such a short time span. Among other countries, China has achieved its unprecedented growth story by drawing on its vast resources of "excess low-cost labor" in rural areas. By reproducing basic manufacturing goods in huge quantities at a minimum-wage level, the country's manufacturing industry could leverage economies of scale and thereby achieve enormous profitability rates over the coming decades.

But that was the China of the past. Today, the low-hanging fruits have been picked and the "easy" gains in short-term technological improvements have been made. The supply of a rural workforce is gradually becoming scarcer as it moves to the cities, and simply purchasing advanced equipment and copying best-practices from Western companies will not be

sufficient to sustain China's startling pace of change forever. In addition, customer requirements regarding products and services have significantly increased. Inevitably, China has reached another milestone in its growth path: the challenge of how to achieve future growth from technological evolution instead of through factor accumulation. In fact, China is experiencing a slow but steady transition from a low-cost and labor-intensive economy to a knowledge-based one. To manage this transition, China is significantly enhancing its industrial mainland capabilities and upgrading to higher-value industries. "Innovating in and for China" has become an aspect of the strategies of Chinese companies, particularly in light of the "Made in China 2025" initiative. This five-year scientific and technological innovation plan by China's government aims to build China into an innovation powerhouse and lift the country's innovation competencies into the world's top 15 by 2020. By nurturing innovation at home, and acquiring R&D capabilities from abroad, China is now well underway in establishing its very own domestic culture of innovation.

*Stuck in the middle: while MNCs cannot keep up with the competitive cost structure of local players, they are facing significant headwinds from China's strengthening innovation process.*

FIG. 01 | CHINESE COMPETITORS GAINING GROUND



Although most MNCs are still confident they can lead the field, today China is perceived as a highly competitive market. In our survey, a considerable number of companies already admit that their competitive edge in designing, developing, selling and marketing new products is endangered. Their corresponding Chinese competitors have caught up or are even already performing better.

This transition has implications not only for local companies but also for foreign-owned businesses operating in China. MNCs begin to face a new set of challenges: In the very beginning, MNCs pursued a pure import-driven strategy. Fueled by the goal to quickly gain market shares, MNCs often introduced the internationally applicable best practices of their home-market product portfolios. This strategy could guarantee a successful entry into the Chinese high-end market, as innovation capabilities were much scarcer in China than abroad. Having already achieved world-class status at home, established foreign players' product solutions used to be technically advanced, allowing them to leverage their existing knowledge and R&D capabilities to out-innovate local companies.

**THE CHINESE BUSINESS ENVIRONMENT IS BECOMING A LOT MORE DEMANDING**

Yet in light of the shifting Chinese market landscape, local competition is increasing. Local companies have decisive advantages since they are better positioned to understand Chinese customers' demands. Accordingly, adapting to specific local customer preferences is a key factor for success.

This is especially true for China's current economic climate, in which demand varies greatly across industries and regions: There is a geographical shift occurring as the consumer population grows from coastal areas into newly emerging inland markets. This growing domestic wealth is bringing

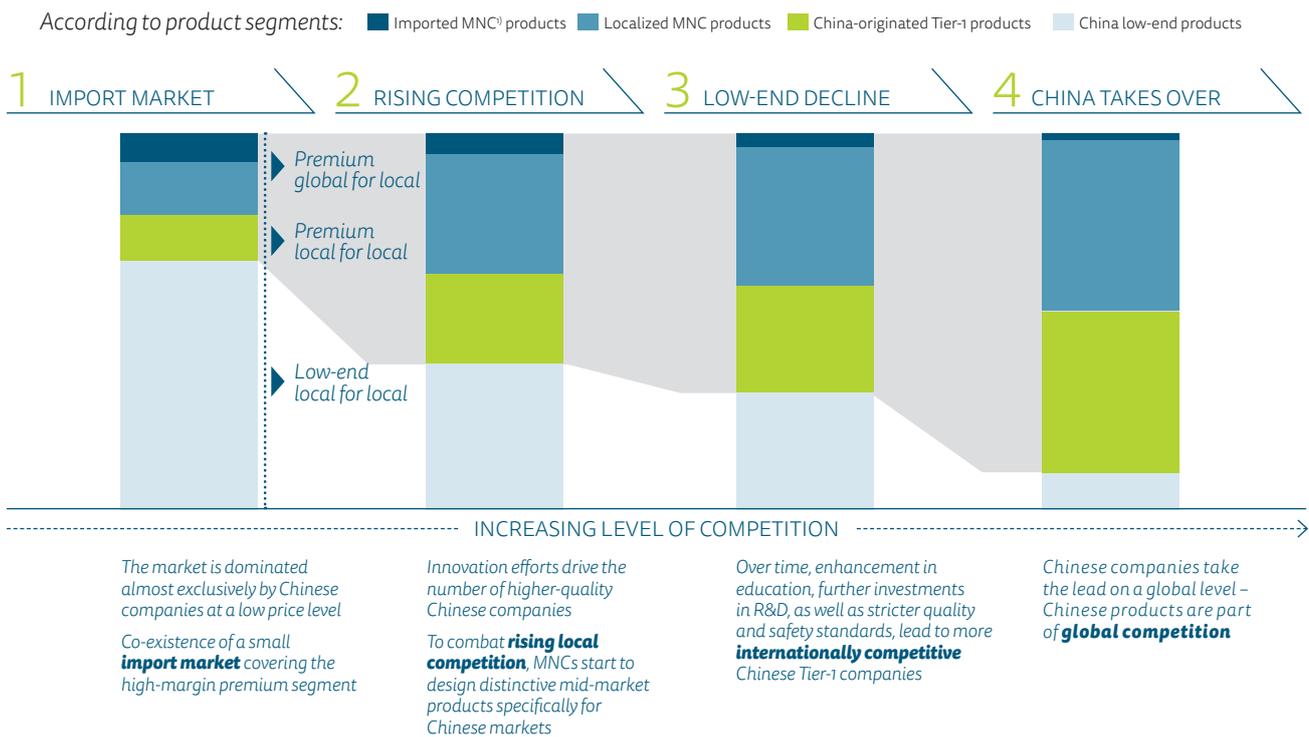
an increasing degree of heterogeneity across Chinese end-markets. Moreover, local companies often react with more flexibility and agility to changing market demands. By contrast, MNCs' usually complex organizational governances and standards entail slow decision making processes, leading to a lack of flexibility and speed-to-market.

**THE CONSEQUENCES ARE EVIDENT**

On the one hand, MNCs will feel significantly under pressure in the mid to high-end segments because of local companies introducing customer-specific products at a decent quality level. On the other hand, MNCs are often also not able to compete in the low-end segments, as their ability to grant price decreases to their home-made product portfolio is limited.

No matter how one looks at it, there is no getting around the fact that MNCs' product portfolios need to undergo a fundamental transformation in order to withstand intensifying competition and increasingly diversified market demands. Not only must existing products be significantly adapted or re-designed, but also novel business models and processes may be required. The times when MNCs could count on harvesting profits just from bringing their home-market products to China are over. Local competitors are clearly on the rise – for now mainly in China, but soon very likely also in the rest of the world. The figure shown below summarizes the transformation of China's market landscape along four major stages. ||

**FIG. 02 | TRANSFORMATION OF CHINA'S MARKET LANDSCAPE ALONG FOUR MAJOR STAGES**



1) MNCs refer to business organizations that have business activities located in more than two countries; in the context of this report and the conducted survey, MNCs have an international headquarters and established branches or subsidiaries in China

## 03 INNOVATION AS COMPETITIVE EDGE

Fortunately, MNCs have already begun to appreciate the impact and pace of China's innovation catch-up process and are starting to react. Nearly 70% of all interviewed MNCs stated that driving innovation in China is one of their Top 3 business priorities within the next three years (see fig. 03). Interestingly, 25% of interviewees have identified innovation as the Number 1 priority on their agenda.

FIG. 03 | INNOVATION HAS HIGHEST PRIORITY

*What is the degree of priority for innovation in your Chinese entity in the next three years?*



AMONG TOP 3 PRIORITY:

67%

TOP 1 PRIORITY:

25%

# 59%

*of survey participants  
have no well-defined  
innovation road map*

In addition, multinationals have begun to realize the central role that innovation plays in developing customer-specific products: 80% of interviewed companies consider innovation to be a vital instrument for meeting local customer needs (see fig. 04). Furthermore, innovation is seen as an efficient means to differentiate from competition (77% of interviewed companies) and attract new customers (70% of interviewed companies).

FIG. 04 | DRIVERS OF INNOVATION



Yet, despite the high priority assigned to innovation, MNCs need to significantly increase their efforts when it comes to developing an innovation agenda: Nearly 60% of surveyed companies have no well-defined innovation road map in place! ||

# 04 ACTIONABLE INNOVATION ROAD MAP

Many companies' headquarters emphasize the importance of innovation, yet business as usual dominates when the next steps for the Chinese market are determined. Simply articulating an auspicious vision for China is far from sufficient. It takes a structured step-by-step road map targeting specific milestones for each business unit and ultimately the product groups.

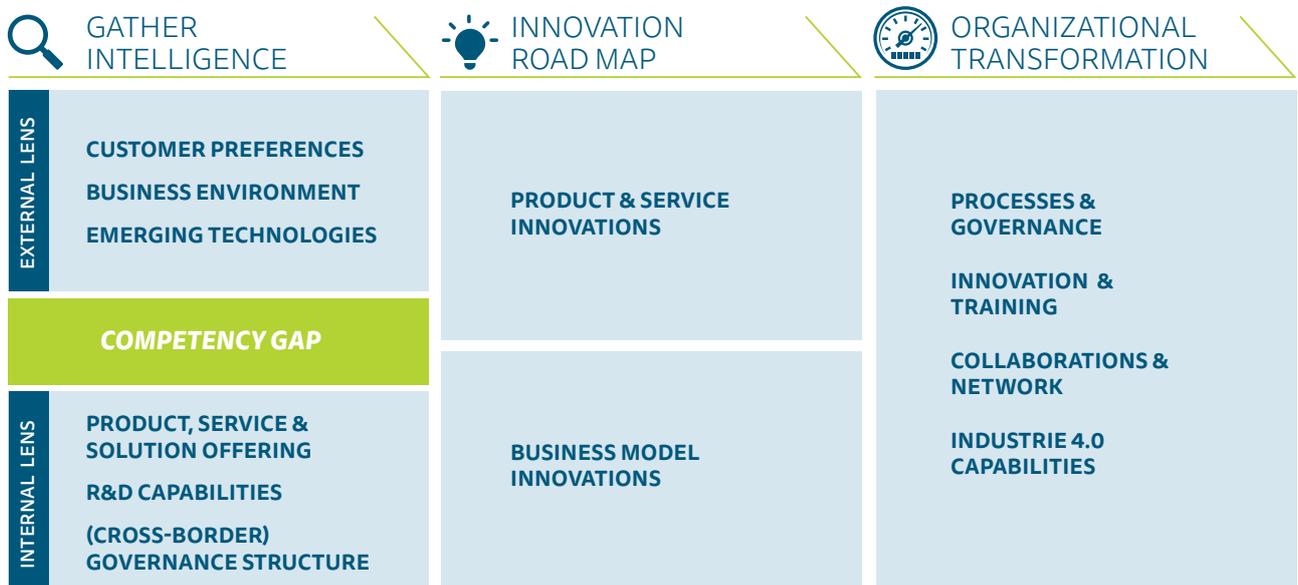
Before the introduction of innovations, a process must take place that needs to be actively shaped according to the specific circumstances of an individual company.

*Naturally, due to the peculiarities of each company, there is no single, standardized approach for establishing an innovation road map.*

This takes a clear understanding of the impact that the shifting Chinese market landscape has on an individual company. Aside from the external market, every aspect of the business – from product portfolio, pricing and point-of-purchase, to processes and governance structures – needs to be carefully reexamined, and its fit for the upcoming challenges evaluated. The outcome is an ultimate end-to-end target operating model that is broken down in all affected business functions. Capturing this defined target state in detail is the basis of a company's "innovation road map".

Therefore, this report aims to provide companies with a framework for shaping their individual road maps for innovative product, service and business models. Based on our experience, MNCs can face this challenge best by following three guiding steps: A profound understanding of the company's environment sets the scene and is the basis for reshaping the business model. Companies will only be as successful as their organizational structures and capabilities allow – therefore, a comprehensive organizational transformation must be pursued to support the defined strategy.

FIG. 05 | THREE STEPS TOWARDS INNOVATION



#### 4.1 GATHER INTELLIGENCE

Ideation or prototyping of any product starts with figuring out what problems actually need to be solved. To avoid wasted time and energy, the first step is to determine the exact nature of the innovation opportunity from the market’s perspective. Once armed with real-world market insights, the organization’s internal capabilities should be made transparent. Bringing the gathered insights together – market demands on the one side, internal competency profile on the other – gaps can be identified and problem statements derived. Subsequently, companies can focus their resources on the identified gaps to create valuable solutions.

#### EXTERNAL LENS: MARKET UNDERSTANDING

Customer preferences can vary significantly – regarding product categories, demographics and geographical terms. Understanding the differences is a prerequisite for designing tailored offerings – not only concerning products, but also solutions. For instance, manufacturing customers in China are often demanding comprehensive turnkey solutions rather than single engineering components. MNCs who provide highly sophisticated components, but rely on their customers to accomplish the integration by themselves, may have a hard time conquering the Chinese market.



Thus, as a first step toward gaining transparency, key purchasing criteria per product group need to be systematically identified. From there, the focus should be set on existing customers as well as potential new ones. In our survey, 60% of interviewed companies state that new customers tend to have needs that differ from their existing customers (Fig. 06). Accordingly, a solid understanding of purchasing behavior will not only help to keep existing customers, but also to expand the overall customer base.

Aside from customer preference examinations, market trends and competitive dynamics also need to be understood in their entirety. A thorough analysis should provide MNCs with the following information:

- Core competitors**
- Risk of new market entries**
- Competitors' product range, target markets and geographic regions**
- Competitors' USPs vs. own USPs**
- Competitors' go-to-market approach and pricing structure**
- Risk of substitutions, e.g. through emerging technological trends**
- Opportunities affecting current business model, e.g. Industrie 4.0**

The continuous recalibration of the findings helps maintain an understanding of the impact of different developments on the organization and a focus on the likelihood of sudden business-model disruptions.

## INTERNAL LENS: ORGANIZATIONAL MAPPING

To outline a strategy for the future, understanding the internal status quo is also vital. The process of mapping the overall organizational picture reveals pain points, inefficiencies as well as missing or overlapping roles and responsibilities. Organizations can identify their current competence profile by conducting site visits as well as structured interviews with key stakeholders:

- Identify and map relevant as-is processes, responsibilities and governance structures; be sure to uncover the actual status and not just the favored one.
- Identify official as well as hidden cross-border interfaces and interdependencies between the Chinese entity and the international headquarters.
- Uncover ongoing initiatives both in the Chinese division as well as in the headquarters to identify overlaps, synergy potentials and alignment needs.
- Identify key employees and knowledge pools across organizational units.
- Learn from the past – leverage use cases of historic market entry efforts of product and service innovations to evaluate success factors.

## PUTTING THE PARTS TOGETHER: THE LONG LIST OF INNOVATION OPPORTUNITIES

Matching the internal picture against the identified external market requirements helps to disclose competency gaps and to develop a long list of innovation opportunities. These opportunities may range from new product lines over customized integrated solutions, to the capability of delivering predictive after-sales services.

### 4.2 ELABORATE THE INNOVATION ROAD MAP

Identifying and investing in the right innovation projects is a challenging task, particularly in times of unpredictable market dynamics. Therefore, successful innovators in China have a systematic product and service portfolio management process in place and rigorously validate the identified opportunities according to expected value, timing and associated risks.

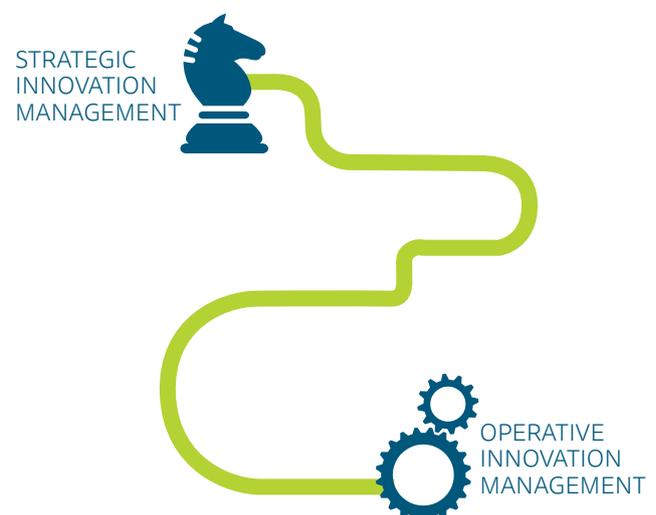
Subsequently, a prioritization, or short list, of opportunities is derived by trading off the potential financial and operational impacts on the one hand and the ease-of-implementation and

required investments on the other. From here on, “ease-of-implementation” should receive particular attention. It is determined by the degree to which an opportunity requires the redesign or adaptation of existing products and services to fit local market needs. Depending on the required extent of modifications, MNCs can pursue either a top-down or a bottom-up approach.

TOP-DOWN refers to the adaption of an existing design to local requirements and is particularly suitable for customers with a moderate to low price sensitivity who value high-end products from international markets. While this approach can usually be readily implemented, it doesn't allow for product cost reductions of more than 20%.

BOTTOM-UP approaches gain in importance since they allow for substantial cost advantages even when local competitors are increasingly offering adequate quality at low price levels. By rebuilding product solutions from scratch, significantly higher cost advantages are realizable and thus allow for noteworthy price decreases. As a result, MNCs can keep up with local competition and at the same time cater more accurately to local market demands. While the bottom-up approach offers considerable leverage for improvement, it must be diligently orchestrated to avoid potential pitfalls. Its success depends mostly on the smooth cooperation of cross-border R&D teams, making the seamless and secure transfer of know-how a key challenge.

The short list of innovation opportunities is captured in a detailed innovation road map. This roadmap forms the bridge between strategic and operative innovation management, and outlines the timing and frequency of the introduction of product extensions, upgrades and new generations. Furthermore, it includes the assignment of staff with specific responsibilities as well as critical project milestones.



### 4.3 ORGANIZATIONAL TRANSFORMATION

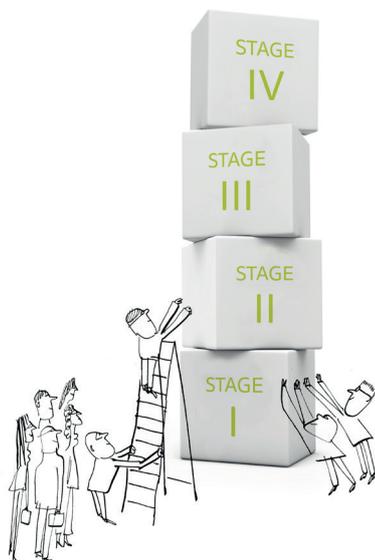
Translating a defined innovation road map into reality can turn into a major headache for many companies. Often, failure in executing the defined innovation road map is primarily due to a lack of the right organizational pillars supporting the endeavor. In addition, road maps are not realized in a short period of time, but rather step-by-step within a minimum

time horizon of 5 years. Chinese entities must be systematically entrusted with increased responsibilities to enable them to successively evolve their local innovation competencies along a commonly observed development path (see fig. 07).

Within this path, one distinguishes between four stages of development: Early explorers, local adaptors, local designers and global innovation motors.

FIG. 07 | FOUR STAGES OF INNOVATION

		STAGE I	STAGE II
		EARLY EXPLORERS	LOCAL ADAPTORS
SEVEN DIMENSIONS	1 INNOVATION MARKET PERFORMANCE	<ul style="list-style-type: none"> <li>No development of products and business models that are tailored to local markets</li> </ul>	<ul style="list-style-type: none"> <li>Adaption of existing products to local markets</li> <li>Increased revenues of local entity through adapted products (up to 10%)</li> </ul>
	2 INNOVATION ATTITUDE	<ul style="list-style-type: none"> <li>Market-specific innovation is of minor priority</li> <li>No innovation strategy in place</li> </ul>	<ul style="list-style-type: none"> <li>Innovation gaining in importance</li> <li>First draft of innovation strategy</li> </ul>
	3 INNOVATION ACTIVITY AND LOCALIZATION	<ul style="list-style-type: none"> <li>Products are designed for original domestic market only</li> <li>Products are imported without adaption</li> </ul>	<ul style="list-style-type: none"> <li>Adaption of finished products and applications to local market demands</li> </ul>
	4 INNOVATION ORGANIZATION AND CULTURE	<ul style="list-style-type: none"> <li>No own local R&amp;D</li> <li>Local management with only low autonomy granted by HQ</li> </ul>	<ul style="list-style-type: none"> <li>R&amp;D gradually transferred to China</li> <li>Local management with limited autonomy but first cross-border teams established</li> </ul>
	5 INNOVATION SKILLS	<ul style="list-style-type: none"> <li>Limited innovation capabilities and skills of staff</li> </ul>	<ul style="list-style-type: none"> <li>Staff shows first innovation skills but products are mainly adapted</li> </ul>
	6 INNOVATION IN INDUSTRIE 4.0	<ul style="list-style-type: none"> <li>No engagement in I4.0</li> <li>Profits gained from traditional products without digital interfaces</li> </ul>	<ul style="list-style-type: none"> <li>First I4.0 prototypes designed with enhanced functionalities, e.g. monitoring applications</li> </ul>
	7 INNOVATION COLLABORATION	<ul style="list-style-type: none"> <li>No collaboration for innovation yet</li> </ul>	<ul style="list-style-type: none"> <li>Collaboration with customers and suppliers to drive innovation</li> </ul>



STAGE III	STAGE IV
LOCAL DESIGNERS	GLOBAL INNOVATION MOTORS
<ul style="list-style-type: none"> <li>Local product development, contributing to ~ 20% of revenues</li> <li>Alignment of processes, enabling speed-to-market above industry avg.</li> </ul>	<ul style="list-style-type: none"> <li>Pioneer disposition in introducing local innovations</li> <li>Revenue share generated by localized innovations &gt;20%</li> </ul>
<ul style="list-style-type: none"> <li>Innovation as Top 3 priority</li> <li>Innovation strategy in place</li> </ul>	<ul style="list-style-type: none"> <li>Innovation as Top 1 priority</li> <li>Well-defined innovation strategy in place</li> </ul>
<ul style="list-style-type: none"> <li>Engineering of improved and new designs specifically for local markets</li> </ul>	<ul style="list-style-type: none"> <li>Engineering of improved and new designs for local but also global markets</li> </ul>
<ul style="list-style-type: none"> <li>Selected steps of value chain transferred to China</li> <li>Management acts autonomously and strongly supports innovation behavior</li> </ul>	<ul style="list-style-type: none"> <li>Globalization of value chain</li> <li>Local management with full authority for global product and services development</li> </ul>
<ul style="list-style-type: none"> <li>Staff has innovation skills that are further shaped and developed in trainings</li> </ul>	<ul style="list-style-type: none"> <li>Very innovative staff that proactively drives innovation</li> <li>Broad training offerings</li> </ul>
<ul style="list-style-type: none"> <li>Active engagement in I4.0 projects</li> <li>Collaboration with various partners, incl. universities and research institutes</li> </ul>	<ul style="list-style-type: none"> <li>Systematic engagement in I4.0 and development of technological fully integrated products</li> </ul>
<ul style="list-style-type: none"> <li>Strategic collaborations</li> <li>First acquisition of firms to drive innovation</li> </ul>	<ul style="list-style-type: none"> <li>Strategic collaborations</li> <li>Further acquisition to drive innovation</li> </ul>

### EARLY EXPLORERS:

Many international organizations start their businesses by opening a sales office and importing goods produced in their home country. These import-oriented organizations use China only as a consumer market without localizing any, or merely a few, functions of the value chain. About 26% of survey participants are currently in this development stage.

### LOCAL ADAPTORS:

When getting more acquainted with the Chinese market landscape, Chinese affiliates begin to modify individual features of existing products within a well-defined scope. While most activities are still conducted at home, R&D activities are gradually transferred to China. In addition, initial cross-border project teams and regular transfers of key personnel are established, yet Chinese affiliates are strongly dependent on the headquarters with only limited discretion rights. In our experience, which was confirmed by survey correspondents, a large number of MNCs can currently be ranked in this category – 39% of Chinese affiliates interviewed are focusing on the adaptation of already existing product lines.

### LOCAL DESIGNERS:

At this development stage, MNCs have successfully mastered the process of application development, i.e. the adaptation of their development processes and production technologies to the Chinese market. In addition, they have started the first efforts to innovate complete new product lines and business models in China and for China. Often, the localization of selected steps of MNCs' value chains, such as full-scale sourcing or assembly, goes along with this innovation process. 19% of interviewed companies have managed to reach the competency level of a "local designer."

### GLOBAL INNOVATION MOTORS:

Having reached the final development stage, Chinese affiliates provide more input to other affiliates and the global headquarters than they receive in turn. Research and development outcomes achieved in China are applied not only for the production of Chinese local products, but also outside China. Eventually, the Chinese affiliates will gradually evolve to operate in the center of Asian activities and moreover to be a net contributor to the global value chain. While currently only the minority of interviewed companies (17%) have been empowered by their headquarters with these far-reaching capabilities, this development stage is expected to gain in importance in the years to come.

The transition from one stage to the next is determined by a company's level of innovation capabilities that can be distinguished in seven dimensions (see fig. 08): Innovation Market Performance, Innovation Attitude, Innovation Activity and Localization, Innovation Organization and Culture, Innovation Skills, Innovation in Industrie 4.0, Innovation Collaboration. Depending on the expression of those seven dimensions, a company transitions faster or slower from one development stage to the other. ||

FIG. 08 | SEVEN DIMENSIONS OF INNOVATION CAPABILITIES





## EXPLANATION

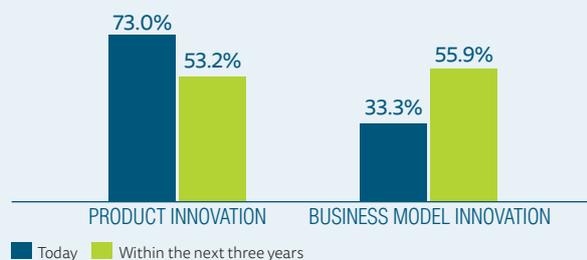
### Business Model Innovations & Implications of Industrie 4.0

A strong innovation portfolio is not just about products. Even though this category represents the most important innovation field for now, our survey results indicate the rising importance of business model innovations. In fact, business model innovations are expected to evolve into the most important innovation type in the years to come.

Up to now, business model innovation has often been regarded as a task primarily for start-ups. With the rise of Industrie 4.0 (I4.0), business model innovation is also becoming vital for well-established companies (see fig. 09).

**FIG. 09 | TYPES OF INNOVATION**

*Which types of innovation do/will you engage in?*

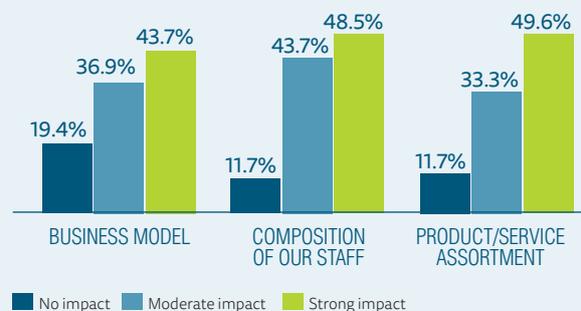


Cyber-physical networks are currently implemented across the entire value chain and products and processes are extensively digitalized. Naturally, this changing business environment paves the way for new products, product-related services and business models. Traditional production and product technologies can be taken as a starting point and merged with modern information technologies to form a next stage of value creation.

In the manufacturing industry, future business models will very likely lead to a shift away from physical up-front product sales and toward more usage-based revenues derived from services. Almost 50% of interviewed companies anticipate a strong transformation of their product/service portfolio mix in upcoming years (see fig. 10).

**FIG. 10 | IMPACT OF INDUSTRIE 4.0**

*What will be the impact of I4.0 in the following areas in your Chinese entity in 5 years?*



One new type of business model is represented by “as-a-service” offerings, i.e. instead of an initial fixed purchase price, customers pay on a usage-basis and thereby transform machinery from CAPEX to OPEX. For the machinery supplier, this model yields attractive opportunities as well, particularly regarding data that can be collected during the operation of the machine.

Collecting relevant machine data and capitalizing on these existing data sources opens up another business opportunity: machinery manufacturers can tap into the wide spectrum of monitoring services, ranging from the mere detection of failures and diagnosis, to opportunities for predictive maintenance and autonomous control, thereby unlocking new value potential.

However, many of the companies we have spoken with are not yet able to clearly see what I4.0 actually stands for, nor the specific benefits it provides. This fact is also reflected by our survey results: Over 60% of interviewed companies are not actively engaged in I4.0 topics yet.

**FIG. 11 | INDUSTRIE 4.0**

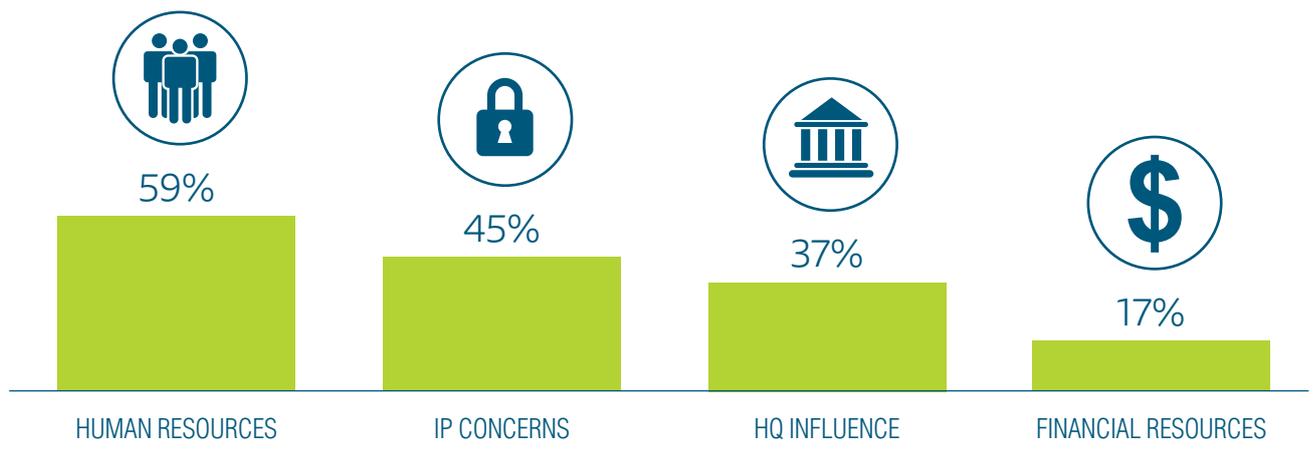
*To what degree have you already engaged in I4.0?*



This situation is opening up opportunities. Since primarily start-ups and innovative companies are moving into the I4.0 field at a fast pace, incumbent manufacturers need to react swiftly so as not to lose their competitive positions.

# 05 BARRIERS TO INNOVATION

FIG. 12 | BARRIERS TO INNOVATION



At a certain point in time, there are barriers that hinder companies from transitioning from one stage to the next, making it difficult to gain a sustainable foothold in China. Our survey indicates that especially human resource shortages, headquarters' influences and intellectual property concerns prevent a company from developing its full potential in the Chinese market. Interestingly, financial resources seem not to be a major problem (see fig. 12).

Human Resources can impose a significant barrier to innovation. Only around 25% of questioned firms are satisfied with the innovation capabilities of their local employees and see potential for improvement, especially with regard to creativity, critical thinking and complex problem solving capabilities. Consequently, innovation might fall by the wayside as employees are not sufficiently qualified to drive innovation forward. However, this hurdle can be overcome by consistently training the Chinese workforce, integrating employees with high innovation capabilities into the team and securing know-how transfers from the international headquarters to Chinese entities.

Yet, the transfer of knowledge can constitute a delicate topic itself, as companies fear the effective protection of their Intellectual Property (IP). This affects not only the sharing of internal know-how but also the establishment of their own local R&D competencies in China. As our survey indicates, a major reason for companies not to invest further in local R&D is IP concerns. Inevitably, high-value jobs

and research competencies are created everywhere else but China. As regulatory initiatives by the Chinese government remain largely ineffective, companies themselves must take the lead. Although there is yet no way to fully guarantee IP protection, certain measures can help to reduce the risk of IP violation – including using proprietary distribution channels, keeping business secrets among the closest employees and avoiding the use of the latest technology that, often, is also not required.

However, the protection of IP remains a topic that is of high importance for international headquarters and thus is one of the reasons why they strive to retain strict control regarding their Chinese entities. Also, other factors such as quality aspects and risk control contribute to the fact that headquarters keep hold of the reins. Not surprisingly, 42% of surveyed companies indicate that the decision making for their product supply is mainly conducted by their headquarters. As a side effect, Chinese entities are lagging behind regarding speed-to-market and overall innovation performance. Therefore, MNCs should think about easing up and loosening the reins to enable their entities to push innovation further. The clarification of decision rights and the introduction of strong governance structures can be first steps. In addition, governing the global-local balance will empower local organizations to capture cost, speed and market proximity advantages while at the same time ensuring global standardization and headquarters control over critical IP rights. ||

# 06 INNOVATION BENCHMARKING

*Survey results confirm: Innovation performance is positively related to sales growth*

### SELF-ASSESSING INNOVATION PROWESS

Despite everyone talking about innovation, it is often not easy to judge one's own innovation prowess. Therefore, we have developed the goetzpartners' Innovation Benchmarking Tool, which outlines a company's individual innovation capabilities and positions it against competitors. It sets a firm in the context of its competitive environment and thereby identifies not only potential areas for improvement but also derives the basis for the development of concrete strategic measures.

Our survey confirms that innovation performance is positively related to sales growth, i.e. companies that report higher innovation performance also indicate above-average sales growth rates.

With the Innovation Benchmarking Tool, a firm's innovation performance and sales growth rate can be compared against competitors and top innovators. It positions the firm within an innovation matrix (see fig. 13) according to its sales growth rate and its overall innovation prowess. Depending on its positioning, the firm can either be classified as lagging importer, prospering importer, slow innovator or innovative performer. In order to change positioning, it is necessary to take a deeper look at the seven dimensions of innovation that determine overall innovation prowess.

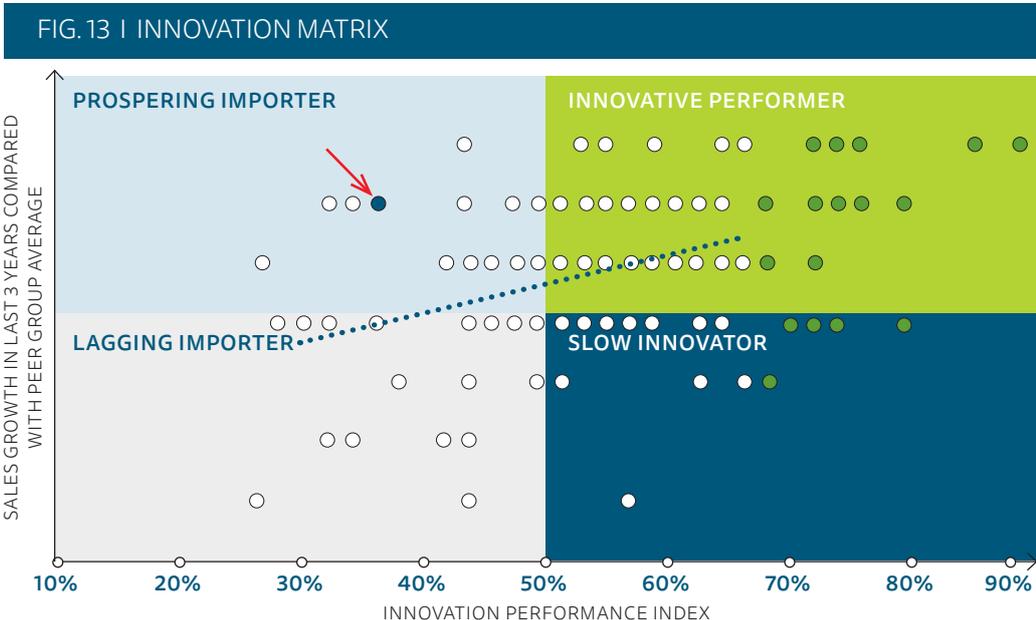
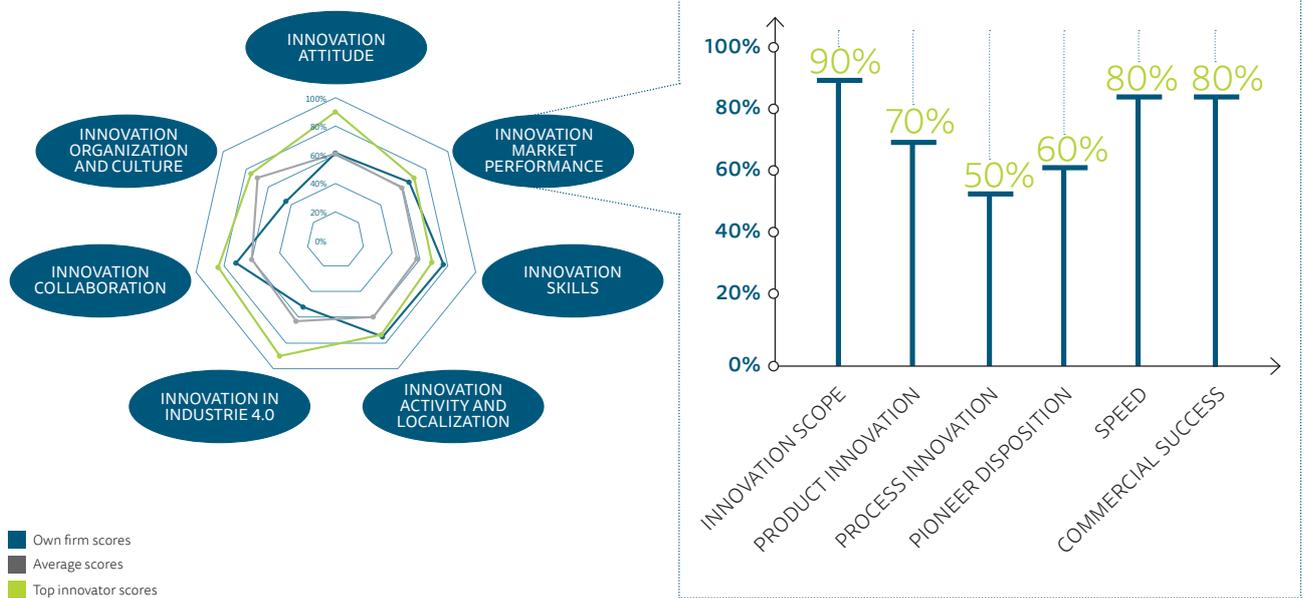


FIG. 14 | INNOVATION BENCHMARKING TOOL



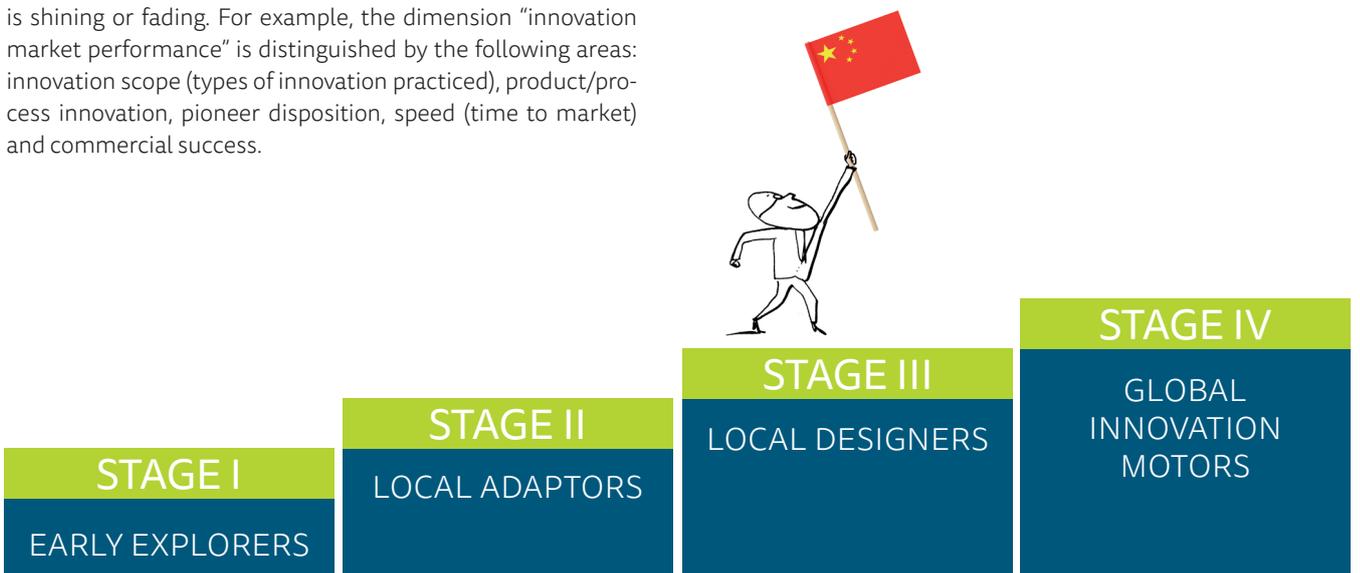
**FIRST STEP**

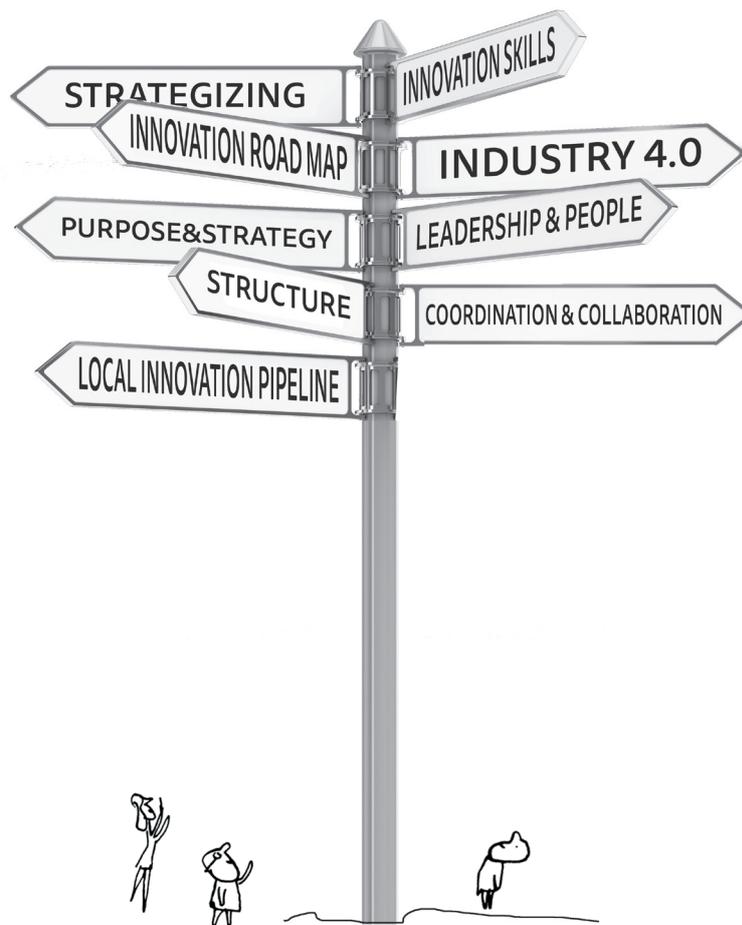
In the first step, the tool (see fig. 14) evaluates a company along the seven aforementioned dimensions to draw a comprehensive picture of its current innovation capabilities, attitudes and practices. The evaluation is based on a thorough self-assessment and a set of selected questions for each transformation dimension. Depending on the responses, each dimension receives a score between 0 and 100%. As a result, a detailed classification of the company's individual innovation prowess is derived.

In addition, within each dimension, selected success criteria provide more insight into the specific areas where a company is shining or fading. For example, the dimension "innovation market performance" is distinguished by the following areas: innovation scope (types of innovation practiced), product/process innovation, pioneer disposition, speed (time to market) and commercial success.

**SECOND STEP**

To put the result into the right context and assess one's own capabilities and behaviors relative to others', the evaluation is benchmarked in a second step. Only through comparisons with competitors and best-in-class performers do the significance of the individual performance and the idea of how innovative a company really is become clearer. On this basis, individual strengths and weaknesses with regard to innovation can be derived and potential areas for improvement identified. In addition, it becomes possible to identify in which of the four innovation stages a company is currently positioned.





### MAKING INNOVATION WORK – TOGETHER

With the results from the Innovation Benchmarking Tool in hand, customized measures to increase one's overall innovation process can be developed. To derive a concrete action plan, a joint workshop is a suitable method for identifying the right focus areas and fields for future innovation action. We propose a three-step approach:

1

#### **BENCHMARKING ANALYSIS:**

company-specific reflection on the results of the innovation benchmark

2

#### **STRATEGIC THRUST:**

specification of focus areas and prioritization of success factors

3

#### **TAILORED MEASURES:**

design and operationalization of concrete measures to drive innovation

Companies have to  
dramatically

*change*

*their **organizational structure**  
and their culture to be designed  
around speed of innovation.*

JOHN CHAMBERS

## 07 CONCLUSION

*The question is not whether to innovate, but*

*how.*

The upwind in China is transforming the country from being low-cost and labor-intensive to knowledge- and technology-based, driving the motor of innovation. Local competition and MNCs have realized their chance to get on board and benefit from China's blossoming. While Chinese competitors can build on their knowledge of local market demands, MNCs have understood the urgency of innovating in order to keep up.

Yet, most MNCs are lacking a clear innovation strategy, hampering their way toward innovation success – only a well-structured innovation road map can provide a remedy. This requires the thorough research of customer preferences, market trends and competitive dynamics, as well as a detailed understanding of the organization and its structures, capabilities and potentials. On this basis, a long list of potential innovation endeavors can be derived that is further prioritized for concrete opportunities. Finally, by systematically enabling Chinese entities to evolve their local innovation competencies, the road map can be translated into action.

So far, as clear as it appears in theory, in practice most organizations lack an in-depth understanding of their own innovation capabilities and potentials. The goetzpartners' Innovation Benchmarking Tool can provide relief, helping MNCs to identify concrete areas of improvement in which to add the final piece to the puzzle and bring innovation out on the road. ||

# 08 THE AUTHORS

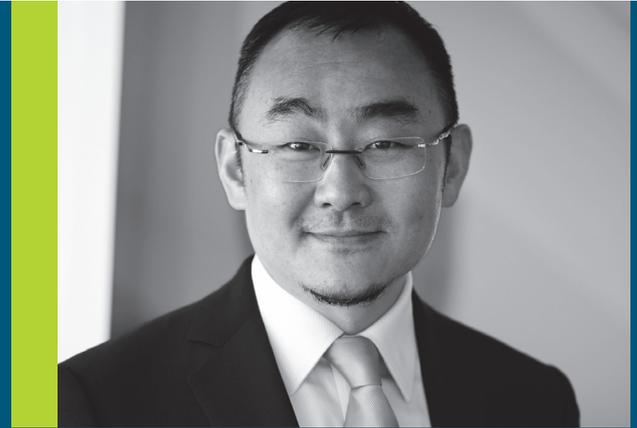


## GÖTZ V. STEYNITZ

Götz v. Steynitz, based in the Dusseldorf office and partner for Industrials, is responsible on the German side for driving the transfer of knowledge and intercultural exchange between the goetzpartners teams in China and Germany. Götz v. Steynitz has a proven track record leading major transformation projects for mid-sized and international corporations, and chiefly advises on China Market Expansion and Localization strategies, Operational Excellence as well as Sales Growth programs.

With nine years of industrial and seven years of consulting experience, he connects the dots between conceptual set-up and implementation. Having worked in China for several years, Götz v. Steynitz is able to leverage his hands-on experience at multinational companies operating in China and use this knowledge to systematically improve the business performance of client companies. He advises by first gaining a thorough understanding of the business-specific market dynamics and then deriving the value proposition it takes to succeed in the Chinese market. His focus area is the level of innovation for "China-to-China" and "China-to-Global" products, which goes hand-in-hand with the localization strategy.

Before working for goetzpartners, Götz v. Steynitz spent five years with DEUTZ AG in Germany, where he held several technical management positions, and three and a half years as Head of Industrial and International Sales for Deutz (Dalian) Joint Venture with FAW in China. He holds a degree in Industrial Engineering and is specialized in Mechanical Engineering.



## TAO LIN

Tao Lin is a partner from the goetzpartners' Shanghai office and is mainly focused on organizational innovation, China market growth and local transformation in China. He has helped with the strategic planning and implementation of many mid- to large-sized companies in China to successfully position, grow and transform them.

Tao Lin is accustomed to identifying, from the angle of China as well as that of an innovation expert, the pain points and areas of improvement for Western companies in China, especially in manufacturing. From his experience and objective third-party point of view, Tao Lin often helps his clients to first realize where their position within the market is and then where they should be in order to better survive and thrive in China's unique and dynamic environment. "Innovation" and the improvement of its use in China can be confusing to many who are within an organization of interest, yet Tao Lin can make them identifiable, measurable, tangible, organizable, actionable and implementable.

Before goetzpartners, Tao Lin spent 15 years in the strategy and management consulting industry in China, Europe and the USA with companies such as Value Partners, Accenture and Deloitte Consulting. He holds an MBA degree from INSEAD.

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