

## **Probe into Modes of International Human Resource Management in Chinese Small and Medium Enterprises**

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*As a result of the opening and reform of China, Chinese small and medium enterprises (SME's) have become an important force in China's national economy. When Chinese SME's seek international business operations, human resources management (HRM) has a direct impact on international competitiveness of these enterprises. This paper, based on theories of international HRM, considers the status quo of HRM of Chinese SME's and explores modes of International HRM in Chinese SME's-- aimed to upgrade the level of HRM, enhance strength, and achieve better and rapid development of these enterprises.*

**Field of Research:** Chinese SME's; International HRM

### **1. Introduction**

As a result of the opening and reform of China, Chinese SME's have experienced rapid development and become an important force in China's national economic development. At the end of 2006, Chinese SME's accounted for 99.8% of the number of China's enterprises, 58% of China's GDP, 74.4% of industrial added value, 58.9% of social sales, 46.2% of tax revenue. Meanwhile, 75% of jobs are also provided by Chinese SME's (China SME Club, 2007). Nowadays with economic globalization, international business operations in Chinese enterprises are becoming increasingly important, and Chinese SME's are facing a strategic choice of international business operations in order to develop further.

HRM is closely related to steady development of business internationalization. One important challenge Chinese SME's face is development of international HRM congruent with international business strategies required to compete in a global environment. However, there are some problems in HRM of Chinese SME's, which have become barriers of Chinese SME's internationalization. This paper, based on theories of international HRM, considers the status quo of HRM of Chinese SME's and explores modes of International HRM in Chinese SME's-- aimed to upgrade the level of HRM, enhance strength, and achieve better and rapid development of these enterprises.

### **2. Role of International HRM**

Human factors are increasingly recognized as critical to organizational success. As Bohlander and Snell (2007, p.4) commented, "In the past, observers feared that

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machines might one day eliminate the need for people at work. In reality, just the opposite has been occurring. People are more important than ever before. In many fast-growing economies, it may be easier to access money and technology than good people. Competitive advantage belongs to companies that know how to attract, select, deploy, and develop talent”.

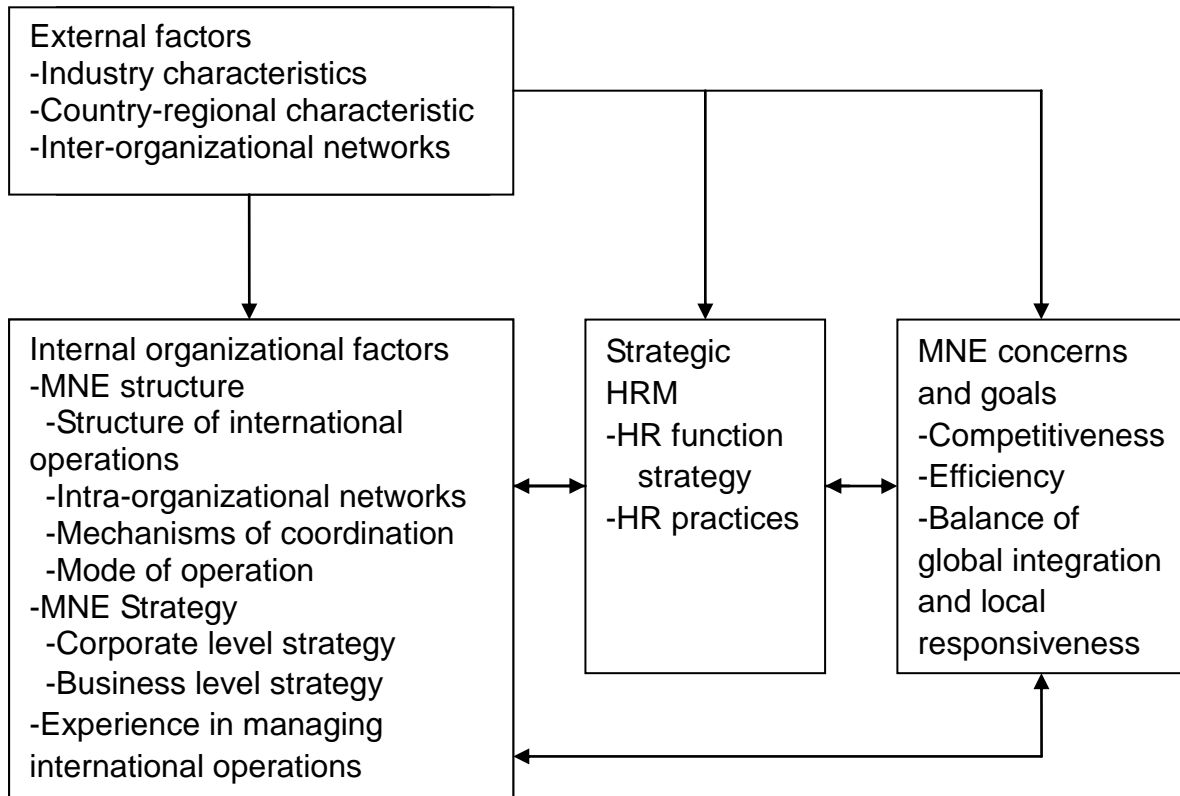
The human factor is particularly important when international activities are involved. Although basic activities of HRM (e.g., human resource planning, staffing, training and development, performance management and compensation) do not change substantially between domestic and international environments, international HRM does involve a more diverse set of activities, with a more diverse population: host-country nationals (HCN's), parent-country nationals (PCN's), as well as third-country nationals (TCN's), in a more complex external environment. Factors which differentiate domestic and international HRM are

- More HR activities (e.g., international taxation, international relocation and orientation, administrative services for expatriates, host-government relations, and language translation services).
- need for a broader perspective
- More involvement in employees' personal lives
- Changes in emphasis as workforce mix of PCN's and HCN's varies
- Risk exposure
- Broader external influences (Dowling & Festing, 2008).

Some similarities between domestic and international HRM activities are potentially transferable cross-nationally--the extent of transferability being defined by the host country context. However, failure to recognize differences in managing HR in foreign environments frequently results in considerable difficulties in international operations. As Desatnick and Bennett (1978) concluded, the primary causes of failure in multinational ventures stem from a lack of understanding of essential differences in managing human resources at all levels in foreign environment. Certain management philosophies and techniques have proved successful in domestic environment: their application in a foreign environment too often leads to frustration, failure and underachievement. These “human” considerations are as important as financial and marketing criteria upon which so many decisions to undertake multinational ventures depend. Therefore, when a firm internationalizes, the “human” factor should be an important variable in the decision-making process.

A broader or more strategic view of international HRM is required to better explain the complexity and challenges of managing international HRM issues. An example of a theoretical framework derived from a strategic approach and using a multiple methodological approach is that of DeCieri and Dowling (1999). Their framework, which is depicted in Figure 1, assumes that multinational firms operate in the context of worldwide conditions, including external contexts of industry, nation, region, and inter-organizational networks and alliances. Figure 1 shows that international firms compete in an increasingly complex environment where the level of challenge of doing business can be highly variable. Internationalizing firms rely on having the right people to manage and operate their businesses and good international HRM practices that are appropriate to the context in which they occur. The combination of appropriate people and HR practices has been a constant critical success factor in international business ventures.

Figure 1 A model of strategic HRM in multinational enterprises



Source: Adapted from DeCieri and Dowling, 1999.

### 3. Status Quo of HRM of Chinese SME's

China is one of the fastest growing economies. China's economic development has brought excellent developmental opportunities for Chinese enterprises. In markets where China's large enterprises dominate, Chinese SME's (with their comparative advantages such as flexible marketing strategies, especially applicable technology, small-scale and low-cost products) have also experienced rapid development. Tables 1 and 2 present the development of Chinese individual industrial and commercial households and private sector during 2000-2006. Chinese SME's not only help to expand the scale of the market economy, but also contribute to creation of the system of socialist market economics as a whole. Most management systems in China, for instance, began first in SME's and then became widespread (Fan, 2003). Development of Chinese SME's is critical for sustained growth of the economy.

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**Table1 China's Individual Industrial and Commercial Households Development in 2000-2006**

Year	Number of Registered Enterprises (thousand)	Rate of Growth (%)	Amount of Registered Fund (RMB billion)	Rate of Growth (%)	Amount of Average Registered Fund (RMB thousand)	Rate of Growth (%)
2000	25710	—	331.5	—	12.9	—
2001	24330	-5.7	343.6	3.7	14.1	9.3
2002	23780	-2.3	378.2	10.1	15.9	12.8
2003	23530	-1.0	418.7	10.7	17.8	11.9
2004	23510	-0.1	505.8	20.8	21.5	20.8
2005	24640	4.8	581.0	14.4	24.0	11.6
2006	25960	5.4	646.9	11.3	24.9	3.8

Source: Adapted from Li, Zibin, China's small and medium-sized Blue Book: Current Situation and Policies (2007-2008) China's small and medium-sized SME associations Research Center of Nankai University

**Table2 China's Private sector development in 2000-2006**

Year	Number of Registered Enterprises (thousand)	Rate of Growth (%)	Amount of Registered Fund (RMB billion)	Rate of Growth (%)	Amount of Average Registered Fund (RMB thousand)	Rate of Growth (%)
2000	1760	—	1330.8	—	755	—
2001	2030	15.1	1821.2	36.9	898	18.9
2002	2440	20.1	2475.6	35.9	1017	13.3
2003	3010	23.4	3530.5	42.6	1173	15.4
2004	3650	23.3	4793.6	35.8	1313	11.9
2005	4300	17.8	6133.1	27.9	1426	8.6
2006	4980	15.8	7602.9	24.0	1527	7.1

Source: Adapted from Li, Zibin, China's small and medium-sized Blue Book: Current Situation and Policies (2007-2008) China's small and medium-sized SME associations Research Center of Nankai University

However, Chinese SME's also face many problems as China becomes more integrated into the world economy. These problems include: (a) a focus too much on domestic development while ignoring international development (b) inability to introduce timely advanced foreign technology; (c) difficulties in achieving technological breakthroughs; (d) paying attention to domestic capital while ignoring international capital. Most Chinese enterprises are managed by families and lack high-quality management talents. As a result, they are unable to introduce advanced foreign management methods. In addition, in Chinese SME's, enthusiasm of

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employees is not high--often resulting in high turnover (Sun, 2006).

Chinese SME's with good operational conditions have good HRM practices; while ones with bad operational conditions have poor HRM practices. From current development, the operational condition of Chinese SME's determines the development of HRM of SME's (Wu, 2005). Compared with large enterprises, HRM of Chinese SME's have both strengths and weaknesses, which influence international development process of Chinese SME's. See Table 3 (Zhao, 2007; Zhao, 2009; Chen, 2006; Huang, 2006; Cooke, 2004).

As data in Table 3 indicate, Chinese SME's still face many unfavorable factors in HRM. They especially suffer from skill shortage and scarcity of qualified international managers. These factors will become barriers to internationalization in Chinese SME's. According to a survey of 112 international business enterprises at Wenzhou city of Zhejiang province in China (including 109 SME's), respondents ranked the following items first: "the issues needed to solve to promote international business operation", "to attract and nurture international operations talents". While for the surveyed item "evaluation of the importance for resources and management resources of multinational enterprise", "human resources" is ranked first (Li & Lu, 2007). Therefore, it is important for Chinese SME's to use their strengths while avoiding HRM weaknesses by providing support for talent and international development.

### **4. Impact of International Development Patterns of SME's on HRM**

#### *4a.) International Development Patterns of SME's*

With regard to paths of internationalization of enterprises, there are generally two patterns: gradual development and "leaping" development, which represent two different development patterns and also provide a basis for international development of SME's (Wang & Zhang, 2005).

#### *4a1.) Gradual Development Pattern*

Gradual development pattern assumes that multinationals are not born overnight. evolution from a domestic to a truly global organization may involve a long and somewhat tortuous process with many and diverse steps. A common process of internationalization is: from domestic operations→indirect exporting through middlemen → direct exporting →sales subsidiary→foreign production → network of subsidiaries. But some firms may use other operation modes such as licensing and subcontracting instead of, or as well as, establishing their own foreign production or service facilities.

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**Table 3      Status Quo of HRM in Chinese SME's**

	<b>Strengths</b>	<b>Weaknesses</b>
<b>Department of HRM</b>	<ul style="list-style-type: none"> <li>-Lean organizational structure integrated into other corporate functional department;</li> <li>-Flexible decision-making mechanism and strong ability to adapt to environment ;</li> <li>-Managers having versatile skills and responsibility for many functions;</li> <li>-Strong comprehensive staffing, which contributes to coordination between HRM and other functions and improvement of overall efficiency</li> </ul>	<ul style="list-style-type: none"> <li>-Less or no independent human resources department, dysfunction of management, smaller connotation of management, rough division of labor, focus on wages, files and labor protection and other issues;</li> <li>-Lack scientific HRM system, and relatively poor management system;</li> <li>-Managers often pay less attention to HR and lack necessary HRM skills</li> </ul>
<b>Practice of HRM</b>	<ul style="list-style-type: none"> <li>-Pay more attention to introducing talents;</li> <li>-Flexible employment mechanism;</li> <li>-Flexible salary system based on employee's contributions and effective incentives;</li> <li>-More relaxed working environment and flexible working time;</li> <li>-Fewer levels of management, low cost, high efficiency;</li> <li>-Larger individual growth space and more promotion opportunities;</li> <li>-Contribute to employee's all-round development ;</li> <li>Focus on employees communication and interpersonal emotion</li> </ul>	<ul style="list-style-type: none"> <li>-Lack concept of HR; no systematic approach for linking HRM with business strategies;</li> <li>- Lack management standard and advanced management tools;</li> <li>-face recruiting and retention problems;</li> <li>- lack coherence and continuity of enterprise training and suffer from skills shortages;</li> <li>-No systematic link between performance management, reward, and long-term motivation;</li> <li>-nepotism;</li> <li>- Low attraction of talents and high talents turnover rate;</li> <li>-Ignore construction of corporate values and culture, and lacking employee commitment</li> </ul>

Gradual development pattern is commonly found in the development of multinationals, but it also has positive significance for growing SME's. For those enterprises which have relatively stable products and technologies, as well as with a specific business advantage, this pattern is relatively safe and can help expand market space, effectively avoid business risks, and seek continuous development under the premise of playing their own expertise.

#### 4a2.) "Leaping" Development Pattern

A "leaping" development pattern assumes that firms do not have to strictly follow gradual development path in international development process and can leap over

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one or more links. For example, when choosing target markets, firms can aim at international markets initially and enter direct exporting to sales subsidiary and others. Also, some firms are able to accelerate the process through acquisitions, thus moving directly into foreign production.

Many successful Chinese SME's developed successfully through the leaping development pattern. This pattern is applicable for those SME's which have a smaller scale, less capital requirements, low-volume goods, more product species, flexible operational mechanism, at the start-up stage or growth stage.

Different development pattern requires Chinese SME's to be based on their own characteristics, make full use of their core strengths, to find proper internationalized ways in order to grow and prosper in a global environment.

### *4b.) Impact of International Development Patterns on SME's' HRM*

The international development pattern SME's choose will not only influence enterprise's operational pattern, but also raise different requirements for HRM.

Gradual development pattern requires that SME's develop their management patterns from domestic to foreign countries, through a gradually improving, from domestic to international management mechanisms to support enterprise development and expand and achieve continuous evolution and development. HRM, in relation to overall business management, has also gone through the development process from simple to complex, from relatively independent to coordinate with other functions. The pattern highlights the process of expansion from inside to outside, emphasizes its own business management functional integration, focuses on integrity and standardization, and realizes transformation from domestic to international management.

In a "leaping" development pattern, SME's enter international markets to compete by way of investment, and enterprises directly participate in international business operations. While enterprise's HRM should be based on the status of parent and host countries to choose suitable international management model, more rely on external efforts to expand HRM functions, including core talents absorption, HRM outsourcing, management consulting services and other means to upgrade the level of management, enhance HRM, and promote enterprises to develop by leaps and bounds. The pattern requires that management focuses on human resources, makes full use of external resources, meanwhile combines their own characteristics to form an effective international HRM, pay attention to management efficiency and functions at play so as to better support enterprises to achieve development by leaps and bounds.

Therefore, in the developmental process of Chinese SME's' internationalization, Chinese SME's should not only pay attention to business strategy, capital, technology and market, but also choose proper HRM Strategies to form their core competitive advantage and help business growth and development.

## **5. Strategic Choice of International HRM Modes in Chinese SME's**

According to the theory of strategic HRM as well as the above analysis, HRM needs to be closely related to business strategies. Therefore different international operation development patterns need different modes of HRM in support of enterprises' international development. Table 4 compares different characteristics of operation management between two different international operation development patterns, and based on the above differences, explores different modes of international HRM in Chinese SME's from management concept, management focus, high-level managers, HR department and first-line managers' focus aimed to help enterprises better adapt to practical needs of international business management, and to provide talent guarantees and intellectual support, and promote long-term development of enterprises.

## **6. Conclusion**

In the process of Chinese SME's internationalization, HRM determines to a large extent the effects of international business operations, and contributes to formation of core competitiveness of enterprises, while strategic choice of international HRM modes is key to determining effectiveness of management. An enterprise must make a strategic choice based on different international operation development patterns and specific environmental conditions, and gradually improve and develop international HRM mode best suited to the international development needs of enterprise.

Based on two different international development patterns (gradual development pattern and leaping development pattern), there are two responding international HRM modes for Chinese SME's to choose. The former mode highlights that HRM in Chinese SME's should focus on integration and standardization of HRM functions, and achieve transformation from domestic management to international management. The latter mode requires that HRM in Chinese SME's should make full use of external resources while combining their own characteristics to form an effective HRM system, and paying attention to management efficiency and HRM functions played so as to better achieve enterprises' leaping development.

International development also requires Chinese SME's to make changes in HRM functions. The changes of HRM functions in Chinese SME's reflect the following aspects: from traditionally ignoring HRM to linking HRM with business strategies; from focusing on management by internal personnel to turning to management by external professionals; from focusing on introducing and utilizing talents to combining internal employees development with external talents introduction; from simple short-term material incentives to long-term comprehensive incentives to mobilize enthusiasm of employees and enhance attractiveness of organization and team cohesion; from focusing on internal management to combining internal management with outsourcing of HRM to upgrade management level and work efficiency; pay more attention to effects of cross-cultural management on human resources management, and strengthen construction of enterprise culture. While all these changes in HRM functions must be based on international operations context,



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enterprises must implement constant changes and seek more effective ways to achieve international business operations strategy.

**Table 4: Modes of International HRM under International Operation Development Patterns**

<b>International Development Pattern</b>		<b>Gradual Development Pattern</b>	<b>Leaping Development Pattern</b>
<b>Characteristics of Business Management</b>		<ul style="list-style-type: none"> <li>-Market-oriented and long-term focus ;</li> <li>- orderly organization expansion</li> <li>-Gradually expand market scope</li> <li>-Management emphasis on standardization;</li> <li>-Gradually establish and improve rules and regulations;</li> <li>-Corporate culture is combined with characteristics of other cultures</li> </ul>	<ul style="list-style-type: none"> <li>Customer-oriented and focus on efficiency;</li> <li>-Enterprise development features innovation and creates value through unique technology and product design;</li> <li>- Enterprise development through market breakthrough;</li> <li>-Operation management is oriented to customers and highlights characteristics;</li> <li>-Results-oriented rules and regulations;</li> <li>-Characteristics of cross-cultural management</li> </ul>
<b>Modes of international HRM</b>	<b>Management Concept</b>	Establish modern concept of HR; change from domestic HRM to international HRM	Establish concept of international talents and international HRM
	<b>Management Focus</b>	Focus on reasonable division of labor among corporate executives, HR manager, and first-line manager	Introduce talents to achieve optimization of HRM by outsourcing
	<b>Top Managers' Focus</b>	<ul style="list-style-type: none"> <li>-Change from business management to strategic management;</li> <li>-Emphasis on HR planning;</li> <li>-coordination and harmonization of management policy between Chinese and foreign employees</li> </ul>	<ul style="list-style-type: none"> <li>-Concern about influence of organizational leaping development pattern on demand for HR;</li> <li>-Pay attention to HR planning and emphasis on HRM</li> </ul>
	<b>HR Department's Focus</b>	-Establish a sound management system, perfect management mechanism, and implement	construction of department is based on flexible needs; managers are recruited from outside;

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		<p>standard management;</p> <ul style="list-style-type: none"> <li>-Specialize management and strengthen cross-cultural construction;</li> <li>-Pay attention to selection of expatriates;</li> <li>-Implement localization of talents</li> <li>-International staff training</li> </ul>	<p>implement outsourcing strategies of management to minimize working burden;</p> <ul style="list-style-type: none"> <li>-Improve management of expatriate managers;</li> <li>- Management consulting plays important role to enhance management level</li> </ul>
	<p><b>First-line Managers' Focus</b></p>	<ul style="list-style-type: none"> <li>-Organic combination of own and external talents;</li> <li>-Differentiated incentives;</li> <li>-Coordination of labor relations;</li> <li>-Staff team building;</li> <li>-Cross-cultural practice</li> </ul>	<p>Focus on introduction of large number of talents to form international talents team;</p> <ul style="list-style-type: none"> <li>-Implement flexible and effective incentive measures to mobilize enthusiasm of talents;</li> <li>-Concerned about versatile staff management;</li> <li>-Strengthen cross-cultural construction;</li> <li>-Coordination of labor relations</li> </ul>

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