

CONNECT

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Focus Topic :
BUSINESS INNOVATION
(PART ONE)



CUHK Business School
The Chinese University of Hong Kong



Dean's Message

I would like to welcome our readers to this edition of the CUHK Business School's magazine CONNECT. Situated at the world's doorway to China, with a well-developed foundation in business education and research, CUHK Business School at The Chinese University of Hong Kong has a unique role in nurturing business leaders for tomorrow. CONNECT magazine provides a platform through short articles in which to educate and inform on selected business topics by staff at CUHK Business School and guest writers. This edition of CONNECT magazine focuses on business innovation, and we hope that you will find the articles both interesting and stimulating.

Professor Vernon Hsu

Profile: The Chinese University of Hong Kong

- The Chinese University of Hong Kong (CUHK) was established in 1963 after the amalgamation of existing colleges which date back to 1949
- The Vice Chancellor & President is Professor Joseph J.Y. Sung
- CUHK has eight faculties (Arts, Business Administration, Education, Engineering, Law, Medicine, Science, Social Science) and 62 academic departments
- CUHK is ranked 39th in the QS World University Rankings 2013 and four of its academic staff have been awarded Nobel Laureates
- CUHK is based on a collegiate system of nine colleges
- CUHK has 23,000 students; 3,000 of whom are from outside Hong Kong

Profile: CUHK Business School (The Faculty of Business Administration)

- The Dean is Professor Vernon Hsu
- The Business School is comprised of two schools (Accountancy, Hotel & Tourism Management) and four departments (Finance, Decision Sciences & Managerial Economics, Management, Marketing)
- It has over 4,000 students (full-time/part-time)
- Over 500 undergraduate and postgraduate business students embark on an international exchange during regular term time annually
- CUHK Business School is the first business school in Hong Kong to offer MBA and Executive MBA programs
- The MBA program was ranked 27th in the world in 2013, and the EMBA programs was ranked 13th in the world in 2013, by the Financial Times
- The School runs dual MBA degree programs with HEC in France; Rotterdam School of Management in the Netherlands; and the University of Texas at Austin in the United States. It also runs a joint program with Cambridge Judge Business School in the United Kingdom and MIT Sloan School of Management in the United States; as well as masters teaching partnerships with Tsinghua University and Shanghai National Accounting Institute in China

Introduction:

IN 2014 and beyond, the next big frontier of business innovation is open for exploration. What are the leading trends? In a two-part series, **CONNECT** takes a look at different business management areas and how CUHK Business School takes on the role of a trailblazer to push for the next big leap.

The Next Big Frontier

Prof. T.J. Wong, former Dean, Director of Center for Institutions and Governance, CUHK Business School

WHEN the word “innovation” is mentioned, very often images of iconoclastic technologies pop up, and the faces behind them—from Polaroid founder Edwin Land to Apple founder Steve Jobs to founder of SpaceX, PayPal and Tesla Motors Elon Musk—give a mystical overtone to what innovation is about. Often though, behind the flashy products and services, hums the silent whispers of data. When data are analyzed in smart ways, they could galvanize into a brilliant product idea, a highly customized solution, a service that fits like a glove, a brand new business model or even a disruptive invention.



// whether it's finance, accounting, management or marketing, we need a huge amount of data to be able to understand consumer behavior and make strategic decisions ... //

The Year of Big Data

The sheer amount of data being accumulated and stored by organizations all over the world has led to a phenomenon known as “big data,” and it is quickly reshaping the business world.

Big data has made a lot of noise over the past year. This is the year that businesses do something about it. “Business must be combined with technology to make use of the big chunks of data gathered—especially in China, where the market is not very developed and the room for development is huge,” says Prof. T.J. Wong, the former Dean of the Chinese University of Hong Kong Business School. “As we look ahead, whether it’s finance, accounting, management or marketing, we need a huge amount of data to be able to understand consumer behavior and make strategic decisions,” he continues.

It’s Time to Crunch

To help companies better understand how they can make use of big data in their operations and management, CUHK Business School offers courses on both the undergraduate and graduate levels that not only provide state-of-the-art research facilities and platform, but also lots of hands-on application opportunities.

“The trend of big data has been the driving force behind some of our latest courses and it continues to provide the direction of our new curriculum development,” says Prof. Wong.

An example is the new Master of Science degree program on business analytics, which has just been launched by the Department of Decision Sciences and Managerial Economics. The course is about data mining and aims to improve students’ understanding of the China market and its consumer behavior.

The Marketing Department continues to offer an undergraduate course in marketing engineering, which provides excellent opportunities for students to work within companies, using IBM’s sophisticated data-crunching software to help them make better marketing decisions.

In research, the Center for Institutions and Governance is currently using big data to map the social networks of Chinese companies’ top executives in order to find out how such networks help the companies with their investment decisions, how knowledge sharing takes place within the companies, how much resources they can obtain from the government and so on. One of the latest developments at the Business School is its collaboration with CITIC Bank to set up a joint center to research risk management, credit analytics and consumer preference using big data.

// CUHK Business School has evolved to become a trailblazer in the research of big data mining and application in the Greater China region ... //



Prof. T.J. Wong

Unique Positioning

Thanks to its unique positioning, CUHK Business School has evolved to become a trailblazer in the research of big data mining and application in the Greater China region.

CUHK will be opening a new campus in Shenzhen and the Business School will be the first faculty to offer its undergraduate course in 2014.

“Being the first university in Hong Kong to set up an undergraduate program on its own campus in Shenzhen, we are rapidly expanding our network with Chinese companies,” says Prof. Wong. “Our unique positioning comes from our ability to apply Western technology in the China market.”

He explains that CUHK’s Shenzhen campus provides a solid base for the Business School to research the China market. “Shenzhen is the most market-oriented city in China,” he points out. “It is very competitive and its companies demand rigorous scientific management.”

Prof. Wong says through the Shenzhen campus, the Business School aims to build solid relationships with the academia, government and enterprises there. “We hope that through our cooperation, we can help to expand the regional economy. For example, we’d like to conduct policy research for the government and education programs to help the local communities,” he says.



“...China is a new source of innovation for the world...”

Prof. Wong emphasizes that the Shenzhen campus not only benefits the local economy but also acts as a stepping stone for the School's students in Hong Kong. "Through our Shenzhen campus and connections, our students in Hong Kong will find it much easier to gain opportunities to participate in internships and academic exchanges in China," he explains. "This will help them get a head start in their career."

Galvanizing Innovative Ideas

China is a totally new market for the world in terms of the development of innovative companies and business models. "China is a new source of innovation for the world," says Prof. Wong. "There are more and more innovative companies that want to 'go out' and we want to be a part of this, helping them move beyond the domestic market."

The School's Center for Entrepreneurship and Center of Business Innovation and Globalization are two important catalysts that have been promoting innovation, not just in products but also business models and business processes. They will continue to play the role of catalysts for innovative practices in the region.

The latest effort at CUHK is the creation of a Creativity Lab at the Wu Yee Sun College. Prof. Wong, a founding fellow of the college, along with three other professors

from the Business School—Bernard Suen, Denis Wang and Wilton Chau—have been invited to promote innovation and encourage entrepreneurial spirit among the students in the college, who are studying a broad range of subjects. "Hopefully, this will bring out more innovative thinking and entrepreneurial impetus in fields other than business," says Prof. Wong.

Biggest Challenges Ahead

As we look ahead, what are the greatest obstacles for innovation? According to Prof. Wong, it is information overload. And the antidote to that? "Keen observation," he says. "Without the ability to distill all the data and wade through all the noise, you won't be able to come up with creative paradigms and make new products or services."

To increase the chances of those mystical "light-bulb moments," Prof. Wong says one must train to think laterally. "You may not need to create something from scratch but you need to be able to connect the dots. The more you train yourself to observe the pattern of things and to see the big picture, the more you will be able to come up with innovative ideas."

By Louisa Wah Hansen

How Smart can Smart Data be?

*Prof. Lau Kin-nam,
Department of Marketing and Director of the Marketing Engineering Lab*

FOR quite some time, businesses have been eyeing big data for its huge potential to reinvent marketing, but successful applications are still rare. How can companies achieve greater heights through smart data applications?





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Big data is quickly becoming the go-to solution for any company that wants to have an edge over their competitors.

According to a McKinsey report, titled “Big data: The next frontier for innovation, competition, and productivity,” the use of big data will become a key to competition and growth going forward: “From the standpoint of competitiveness and the potential capture of value, all companies need to take big data seriously.”

At The Chinese University of Hong Kong Business School, professors and students of the marketing department are actively engaging themselves with the business sector to help them translate their big data into practical and strategic solutions.

In fact, they have been doing so since the late 1990s, but today, their effort is further crystalized through the official opening of a Marketing Engineering Lab last year with the sponsorship of IBM, who donated sophisticated data-crunching software. The lab now aims to play a pivotal role in pioneering big data applications.

Lau Kin-nam, marketing professor at CUHK Business School and director of the lab, says that his objective is to connect academia with industry by providing a free student service to different business sectors. The goal is to help companies set up the software infrastructure and business model so they can start using data in an intelligent way to support their marketing decisions.

Currently there are 80 students from the Master of Science in Marketing program, and another 15-20 undergraduates who have signed up for the big data program. “We will train them to help companies. At the same time, students can have real data and practical experience. It would help them get a job in the area,” says Prof. Lau.

He gives an example of how the retail sector could make use of its customer data to design better marketing strategies.

“Each point-of-sales (POS) transaction—may it be credit card number, Octopus card ID and so on—contains customer data. Most retailers just want to capture MIS data and stop at the sales statistics level. By contrast, we want to capture data at the customer level.

For example, we can count how many customers come to the store each month, how much money they have spent and what exactly they have bought,” he says. “By capturing these data, a retailer can then make more cost-effective decisions on its marketing efforts.”

Prof. Lau has assigned students in his class to serve companies in the retail industry during 2014. They will help the companies analyze the POS data and turn them into effective marketing decisions.

All About Relationships

Today, many industries still suffer from inefficient marketing efforts and spending. Prof. Lau cites the hotel industry as an example. "Hotel clubs or food-and-beverage eateries send many promotional materials," he says. "Often, I can get a dozen different promotional materials at the same time from the same club."

He says the problem with hotels is that they often lack in-house customer relationship management (CRM) teams and do not have the staff to manage their customer database.

While CRM has been used for about two decades, the proliferation of social media and the latest development of mobile applications mean marketers should pay acute attention to their customers' particular needs through these channels.

By gathering and analyzing customer data through social media and contacting them through mobile apps (mobile CRM), companies will stand a much greater chance in not just acquiring new customers but also in keeping them for the long haul, says Prof. Lau.

"Today, the third largest nation in the world is Facebook. As many as 90 percent of our students use the smartphone. On social media and mobile devices, friends tell their friends about products and services that they like, so this could really reduce advertising dollars spent in traditional areas," he says.

Prof. Lau explains that traditional media such as TV stations have already realized that traditional advertising won't tell them who is watching the ads and how many views actually lead to purchases. On the other hand, by monitoring the click rates on online media channels, companies will be able to design their marketing budgets more efficiently.

He explains that the older form of metrics, "cost per click" (CPC) has gradually been favored by "cost per unit of sale" (CPS), which can tell an advertiser how clicks on an online ad translates into actual purchases.





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As online advertising becomes increasingly prevalent through PC and mobile devices, Prof. Lau predicts even more of companies' advertising budgets will shift away from traditional media to mobile media over the next few years.

"By capturing and analyzing customer data, companies can manage customer relationships using mobile devices," he says, pointing out the latest development being real-time location marketing, driven by the mobile phone. The way it works is actually quite simple: Shops in a mall would send promotional messages to shoppers who have chosen to connect their mobile devices to the mall's Wi-Fi server. This not only helps stores reduce their advertising spending but also makes the effort much more targeted than traditional advertising.

On the Drawing Board

In 2014, the marketing department of CUHK Business School will be rolling out a smart marketing conference to bring together the academia and

different industry sectors—including companies from China, IBM's clients and some professional organizations. The event aims to introduce innovative ideas and developments in smart marketing and big data engineering.

Discussions are also underway with IBM China to co-organize the second teachers' workshop in smart marketing in China—the first one having taken place in Hong Kong last year.

"Our goal is to come up with a new CRM model for each of the industry we're going to work with—banking, retail, hotel, skincare and fashion—and help support them so that they can make smarter marketing decisions."

By Louisa Wah Hansen

A Shift in Service Paradigm

*Prof. Denis Wang,
Director of School of Hotel and Tourism Management*

THE hotel and tourism industry has for too long been relying on a fixed way of doing things—so fixed that customers need to compromise their level of comfort to fit to the hotel's own needs. CUHK Business School is resolved to lead the industry in making some drastic changes that put the customer's needs first and foremost.



As consumers' needs become more and more diverse, it is getting increasingly obvious that the hotel and tourism industry's traditional "one-model-fits-all" star-rating system is getting outdated. Creating niche and customized services for tourists is the key that will drive innovation in the industry in 2014 and beyond. According to Prof. Denis Wang, Director of the School, the traditional "star system" adopted by hotels around the world is based on tourists' social economic status. Increasingly, tourists care more about "functions" when they travel.

"Human needs are becoming more and more sophisticated and diverse, we need to come up with innovative and creative ways to satisfy those needs, which are not necessarily bound by social economic classes," he says. "When you travel, what do you actually look for? This is the question we need to ask."

To help practitioners in the hospitality and real estate industries in China and Hong Kong to become more competitive through innovation, the School of Hotel and Tourism Management at the CUHK Business School has been forging close collaborations with industries working on two big themes: function-based hotels which better serve 'Human' Needs and the "China Wallet" strategy.

Serving 'Human' Needs

Prof. Wang cites a project that his school and a hotel developer have recently collaborated on as an

example of a creative way to break the old star-based paradigm. The project aimed to renovate a three-star hotel near the Shanghai railway station to make it an attraction among the transient travelers passing through the area.

The key, he says, is to leverage on the strategic location of the hotel and the high traffic flow, and provide the most important features that train travelers crave for. After an open assessment of the customers' needs, the team decided to focus on only two things: an ultra "heavenly" bed for a good night's sleep and a spacious and well-equipped bathroom for cleaning up after a long train journey. As for other facilities, clean and simple furniture and vending machines would be sufficient to fulfill the guests' needs. There are many restaurants nearby so it would be a waste of resources to provide room service, he says.

"This concept clearly breaks away from the rigid star system," explains Prof. Wang. "Instead of having to install multiple features to satisfy the requirements of the star system, hotels can focus more on installing individual components that not only fulfill their guests' needs but exceed their expectations. In this case, the bathroom fixtures and the beds are even better than those you'd normally find in a five-star hotel."

Prof. Wang says that CUHK Business School hopes to further develop this function- or theme-based concept into a classification system to replace the arcane star

// the hotel and tourism industry's traditional "one-model-fits-all" star-rating system is getting outdated. //



system. "The old one-model-fits-all system classifies hotels based on very objective things like staff-to-customer ratio, interior decoration and facilities," he says, adding that some of these "must-have's" are superfluous. For example, personal butlers who follow guests around actually deprive them of their privacy. Many of the decorations and facilities just sit there as if "for display only."

"What would make it more cost-efficient and competitive for hotels is to profile customers' actual needs and invest in facilities to cater for their needs," he continues. "The basic, common features across the board, no matter what 'star' the hotel belongs to, should include cleanliness, security and courteous and friendly service. Based on these prerequisites, a hotel can then leverage on other unique advantages it has, such as its particular environment and location, to further develop its niche market."

Prof. Wang is leading an effort with his industry network to start a dialog with hotel and other travel-industry associations to replace the star-based system with a new accreditation system that assesses for quality, individual components, functions, logic and more.

This month, the School of Hotel and Tourism Management will launch an industry-based seminar to brainstorm and initiate new and emerging theories in hospitality and real estate. Professors, students and companies will be invited to collaborate with the aim of promoting innovations in the industry.

'China Wallet' Strategy

Another research and collaboration area that the School has been working on is the "China Wallet" strategy. As an ever-increasing number of Mainland Chinese are traveling around the world, the hotel and tourism industry must pay attention to their needs so as not to lose out to the competition, stresses Prof. Wang.

The School's collaboration with Dorsett Hospitality International, a Hong Kong-based hotel operator, has yielded a number of interesting observations and innovative strategies that the company has applied to its 19 hotels in Hong Kong, Mainland China and Southeast Asia.

For example, the team has observed that Mainland tourists generally keep their purse strings tight except for purchases that would enhance their mianzi (face). So they would not pay for late check-out charges, even if they insist on checking out late. This has made it difficult for hotel staff to check in new guests. To solve this problem, it came up with a new concept: a spa with free facilities, massage services and beverages for guests who need to leave the hotel later than the usual check-out time. The spa provides them with a place to hang out free-of-charge, while the hotel staff prepares the vacated rooms for the new guests.

"This strategy makes use of Mainland tourists' psychology and has proven to be very popular," says Prof. Wang.





Another new way of catering for Mainland customers' needs is to take them on shopping tours by providing not only bus tours to popular shopping areas and stores, but also having the drivers take their shopping bags and depositing them in their rooms so they can continue on other tourist destinations without having to lug the bags around. "This is very function-based and matches Mainland tourists' traveling style perfectly," says Prof. Wang.

Another detail that the hotel group has implemented is to skip the bed-sheet turndown service. This is because Mainland tourists like to spread the goods they have shopped on the bed in the evening. A turndown service would be inconvenient for them. On the other hand, hot water is provided in the room for free as Mainlanders have the habit of drinking hot or warm water and believe that one should not have to pay for it. In addition, extra insulation is installed in the walls because Mainland guests have the habit of talking very loudly.

"In the past, five-star hotels required customers to fit their habits to the hotel facilities," Prof. Wang points out. "But today, it should be the other way round. People's lifestyle has changed. They prefer having more choices. So hotels need to come up with innovative and creative ways to satisfy their guests' needs based on their profiles."

From Academia to Industry

To promote collaboration between the School and the industry, the curriculum is designed in such a way that theory and practice are seamlessly integrated. For example, in the "Hospitality Facilities Planning and Design" course—required by the School's final-year hotel students, some students have chosen to do in-depth research on the changing lifestyle and behavioral preferences of Mainland tourists and shoppers for their group projects. The goal is to come up with facilities design and managerial implications for hotels in Hong Kong that aim to adopt the "China Wallet" strategy.

"The findings and outcome of these group projects will have practical and useful implications for the hotel industry," says Prof. Wang.

Hotel owners and operators interested in leveraging the 'China Wallet' strategy will be invited to attend the student presentations and learn from their research and analysis, and from the professors, who will be giving detailed guidance, comments and critique for the improvement of the projects.

By Louisa Wah Hansen

Instead of Counting Beans

*Prof. Zhaoyang Gu,
Director of School of Accountancy*

BY nature, the accounting profession is conservative and as a result, financial statements often don't reflect the innovative potential of a company. How can investors get better guidance if they want to invest in innovative companies? And how can accounting procedures encourage more innovation within companies?



// there are ways in which financial figures can be interpreted so that investors can make sounder predictions on a company's future performance ... //

Innovation is such an intangible aspect in a company's activity that it is often hard to reflect it in any financial statements.

Prof. Zhaoyang Gu, Director of School of Accountancy at The Chinese University of Hong Kong Business School, admits that the accounting profession is backward-looking and inherently conservative and thus often inadequate in reflecting innovative activities that carry profit-making potential. However, he stresses there are ways in which financial figures can be interpreted so that investors can make sounder predictions on a company's future performance as a result of its investments in innovation.

"The key to innovation is being forward-looking. Outcomes are highly uncertain," says Prof. Gu. "But for accountants, investments in innovative activities are often recognized as a 'cost.' In reality, the potential benefits are expected to be higher than the cost. Unfortunately, this is not reported until benefits are realized. If we read the financial statements in the early

stage of investments, we often see a bunch of seemingly bad projects—loss after loss or cash being burnt. So if you just want to use financial statements to guide your investments or for investors to get useful information regarding whether they should provide further funding, it would not be sufficient."

In light of this, he recommends investors to focus on different aspects of financial statements at different stages of a company's life cycle. For example, for a start-up company or for a company that has made some initial large investments, the bottom-line earnings are not the best performance measure that one should look for.

"Rather than the bottom line, you might focus on the top line, i.e., the revenue," Prof. Gu says, citing Internet-related companies as examples. "It's more useful to look at figures such as the number of clicks and revenue growth, rather than the huge cost and negative earnings, which may

suggest value destruction on the surface, which is not true," he says. "Sometimes you might also want to focus on the cash flow statement rather than the income statement."

Besides looking at different aspects of financial statements, Prof. Gu suggests investors to look beyond the formal types of financial statements. "Accounting essentially is an information system. Firms may find alternative communication channels, such as press releases, conference calls, analysts' corporate visits and so on to communicate those intangible aspects to investors, so that they are willing to invest in them."



CSR Reporting and Compensation Strategy

One form of informal reporting system that has been gaining a lot of traction is Corporate Social Responsibility (CSR) reporting, which usually appears as a supplementary section in a company's annual report. According to Prof. Gu's observation, CSR has been popular in management circles for decades but not until recently has the accounting profession started to pay more attention to it.

Prof. Gu cites two publications¹ by George Yang and Albert Tsang, two accounting professors at the CUHK Business School. One of them found that firms that publish CSR reporting and have good CSR performance enjoy a lower cost of equity financing, and that there is a strong association between CSR performance and improvements in financial performance. The other finding is that investors consider such firms more transparent, and as such, financial analysts are better able to predict the firms' future profitability. "These would help innovation in an indirect way—making innovative activities easier," concludes Prof. Gu.

There is also a creative way to encourage investments in R&D and innovation through adjustments in the compensation structure and accounting figures.

Prof. Gu explains: "If a company ties a manager's salary or bonus to accounting numbers, e.g. return on assets (ROA), this would discourage innovation because initial innovation investments reduce earnings so the salary or bonus would be lower as a result. But in compensation contracts, one can adjust away innovation expenses in calculating the ROA, so that any innovation investments would not lead to punishments on the personal level."

One scenario is when a CEO is close to retirement and is faced with the dilemma of whether to further invest in R&D or not. What typically goes on in such a CEO's mind is: "All the benefits will show up in five years but right now I will bear all the costs." So it would not make sense for the CEO to make any long-term investments. One study² shows that when the compensation committee removed the cost of R&D from the income figure, the above-mentioned short-termism, or myopia, was removed. "By using an adjusted number, the CEO is motivated to continue investments in R&D. This is a clever, alternative way of using accounting numbers," says Prof. Gu.

// ... There are alternative ways of adjusting numbers. Numbers are numbers; it all depends on how you use them ... //



Another way is to combine accounting numbers with stock returns. Stock prices are forward-looking, reflecting all the future benefits and costs. So if an innovation activity is value-enhancing to a firm, stock prices would be ahead of accounting numbers in reflecting the net benefits. "By shifting compensation weight from accounting numbers to stock returns, managers would be encouraged to invest more on innovation projects," says Prof. Gu. "There are alternative ways of adjusting numbers. Numbers are numbers; it all depends on how you use them. Each should adapt the numbers to his or her purpose," concludes Prof. Gu.

In conclusion, innovation in the accounting field is much more intuitive, and some tweaks in the way accounting figures are interpreted and in how executive compensation is tied to financial figures could actually encourage innovation within companies.

By Louisa Wah Hansen

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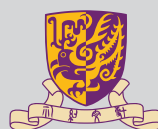
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