Non-state Shareholders Board Power, Board Deep-level Faultlines and Acquisition Decisions by State-owned Enterprises in China

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Abstract

In the context of mixed-ownership reform being further deepened in Chinese state-owned enterprises, based on principal-agent theory and resource-based theory, the study uses Chinese A-share listed state-owned enterprises from 2008-2019 as the research sample, and analysed the impact of non-state shareholders board power on acquisition decisions, in addition to exploring the moderating role of board deep-level faultlines. It was found that empowering non-state shareholders board power increased the likelihood of state-owned enterprises making acquisition decisions; However, if there were deep-level faultlines in the board, the ability of non-state shareholders board power to motivate state-owned enterprises to make acquisition decisions was diminished. The findings of this study suggest that giving non-state shareholders board power may bring benefits to state-owned enterprises in terms of business investment, but with a focus on a reasonable allocation of board members.

Keywords: state-owned enterprises, acquisition decisions, non-state shareholders board power, board deep-level faultlines

1. Introduction

Acquisitions deem to be an extremely complex and demanding investment activity by almost all enterprises, but implementing acquisitions enables enterprises to capture new markets and increases their competitiveness during economic structure optimising (Iskandar-Datta & Shekhar, 2020). The acquisition is of great significance to state-owned enterprises due to the following reasons. Firstly, acquisitions allow state-owned enterprises to diversify their operations at the lowest cost, enhance market dynamics and improve economic efficiency (Lee & Wang, 2017). Secondly, acquisitions can also achieve economies of scale, reduce competitors and further maintain the status of state-owned enterprises (Li & Xia, 2016). Finally, acquisitions can optimise the economic layout and structure of state-owned enterprises, accelerate economic transformation to achieve bigger, stronger and better enterprises (Guan, Gao, Tan, Sun, & Shi, 2021). China has been encouraging mergering and restructuring of state-owned enterprises since the promulgation of Guiding Opinions on Promoting the Restructuring of State-owned Capital and State-owned Enterprises, but data released at the 2019 China acquisitions Annual Conference showed that the number and quality of acquisitions deals by state-owned enterprises are trending towards being overtaken by private enterprises. Most studies pointed out that the situation was mainly caused by the lack of acquisition market capacity of state-owned enterprises and the self-interest motivation of executives (Dong, Dan, & Dan, 2019; Guilong, Jianhua, & Xinxiao, 2018). In addition to the already proposed countermeasures of enhancing experiential learning (Field & Mkrtchyan, 2016), controlling executive power (Njah & Jarboui, 2013) and incentivising executives with options (Datta, Iskandar-Datta, & Raman, 2001), few scholars have sought solutions from mixed-ownership reform currently underway in Chinese state-owned enterprises. Therefore, this study attempts to investigate the impact on acquisition decisions of non-state capital that has been "blended" into state-owned enterprises from the shareholding and has gained board power.

According to Thatcher & Patel (2012), in the decision-making of the board of directors, the role of non-state shareholders board power cannot be practiced without communication and exchange among the board members. Since then, this paper introduced the concept of board deep-level faultlines (Shaw, 2004), and investigated whether the interaction between board members of state-owned enterprises affects the influence exerted by

non-state shareholder board power on acquisition decisions.

This study made several important contributions: First, it enriches the research related to acquisitions of state-owned enterprises. Few previous studies have addressed the unique attributes of state-owned enterprises in the acquisition activity. Second, it points the way for the in-depth promotion of the mixed ownership reform of Chinese state-owned enterprises. Empowering board power of non-state shareholders is an effective way to solve the problems of state-owned enterprises. Thirdly, the study further extends the research related to board governance. The introduction of the board deep-level faultlines not only allows for the analysis of heterogeneity among board members, but more importantly allows for a dynamic and multidimensional measurement of the effects of interactions between board members, which is closer to the real scenario in corporate practice.

2. Literature Review

2.1 Non-state Shareholders Board Power and Acquisition Decisions by State-owned Enterprises

In China, mixed-ownership reform in state-owned enterprises has become a major concern for all sectors. Although the Chinese government has expanded the operational autonomy of state-owned enterprises and established a modern enterprise system after the reform and opening up (Qunhui & Jing, 2013), state-owned enterprises still face the problems of "Lack of Owners" and "One Share Dominates Exclusively." They are lacking of incentives and supervision mechanisms, so efficient governance must be improved (Genin, Tan, & Song, 2020). Non-state capital is seen positively in monitoring and auditing the executives of state-owned enterprises and it provides market-based resources (Jianbiao, Gaoyang, Shuaiqi, & Xile, 2016). Therefore, the Decision on Several Major Issues of Comprehensively Deepening Reform was released at the Third Plenary Session of the 18th CPC Central Committee in 2013, which provides further impetus to the progress of establishing a mixed-ownership economy. Since then, mixed-ownership reform of state-owned enterprises has been deepening and developing until now. The main realization form of mixed-ownership reform introduces non-state capital into state-owned enterprises (Dong et al., 2019).

There are two ways to govern non-state capital entering state-owned enterprises, namely, equity governance and top-level governance (Xinxiao, Taijie, & Guojian, 2020). Initially, some studies suggested that the introduction of non-state capital at the equity level in state-owned enterprises would be beneficial to the improvement of governance mechanisms and the quality of decision-making (Lianfu, Lili, & Qi, 2015). However, most subsequent studies have demonstrated that mere ownership of state equity is not sufficient to give non-state shareholders substantial power to intervene in the governance process and strategic decisions of state-owned enterprises (Lin & Li, 2008). Compared to equity governance, top-level governance is more effective in improving corporate performance, monitoring, and incentivizing executives, etc. (Renzhi, 2019). High-level governance refers to non-state shareholders appointing representatives to the board of directors, supervisory board, and management of state-owned enterprises to participate in corporate governance and decision-making, where the board of directors is the core of corporate governance and the highest decision-making body (Guan et al., 2021). If non-state shareholders are given seats on the board, they can influence the strategic decisions and economic behavior of the state-owned enterprises while protecting their own rights and interests (Dong et al., 2019). Non-state shareholders board power refers to the decision-making power and supervisory rights of non-state capital, arising from the Board seats in state-owned enterprises based on the possession of state equity.

A number of studies based on principal-agent theory and resource-based theory have clarified that non-state shareholders board power has a positive effect on the economic behavior and strategic decisions of state-owned enterprises, such as investment, innovation, and taxation (X. Dong & Yumiao, 2020; Shu, Pengsui, & Wei, 2019). Acquisition is one of the most important economic behaviors of state-owned enterprises. The study predicts that non-state shareholders board power may also have a facilitating effect on the decision-making power of state-owned enterprises in relation to acquisitions.

2.2 The Effect of Board Deep-level Faultlines

Board of directors with directors having widely different characteristics can have an impact on governance efficiency. Lau (1998) introduced the concept of faultlines, which refers to the faultline as "a hypothetical line of demarcation that divides a team into multiple subgroups based on a characteristic." Unlike heterogeneity, which focuses on only one characteristic at a given time, faultlines have interactions from the multiple characteristics of team members simultaneously (Gratton, Voigt, & Erickson, 2011). In an in-depth study of faultlines, scholars have divided the fracture zones into two categories: deep-level and surface-level faultlines (Peteghem, Bruynseels, & Gaeremynck, 2017). Surface-level faultlines are formed based on some easily observable characteristics, such as gender and age. Deep-level faultlines are formed based on some not easily observable characteristics, such as experience, knowledge, and cognitive level. Considering that the effects

produced by surface-level faultlines are transient and they disappear with time, the effects produced by deep-level faultlines are strong and far-reaching. The study chooses to use deep-level faultlines to conduct research.

According to faultlines theory, deep-level faultlines induce the formation of several subgroups within the board, based on one or more similar features (Lau & Murnighan, 1998). Mutual agreement will be found among members within the same subgroup, while conflicts and discrimination between different subgroups will occur, thereby reducing board cohesion (Kuusela, Keil, & Maula, 2016). Ultimately, this makes it difficult to form a unified view within the Board and perpetuates irreconcilable conflicts, which seriously affects team performance, easily leading to important decisions being put on hold. Therefore, in exploring the relationship between non-state shareholders board power and acquisition decisions of state-owned enterprises, the role of board deep-level faultlines cannot be ignored.

3. Research Hypotheses

3.1 The Effect of Non-state Shareholders Board Power on Acquisition Decisions by State-owned Enterprises

Resource-based theory suggests that only having homogeneous resources can hinder the sustainable development of enterprises, so it is essential to introduce a wide and deep range of heterogeneous resources into the company. Empowering board power of non-state shareholders in state-owned enterprises will, on the one hand, transfer the market experience and relevant market resources of non-state shareholders to the management of state-owned enterprises, which will help state-owned enterprises to grasp the timing of acquisitions and respond flexibly to market risks, thus increasing the success rate of acquisitions (Dong et al., 2019). On the other hand, non-state shareholders have board power, which can stimulate the participation and in-depth understanding of the enthusiasm and sense of responsibility of state-owned enterprises' acquisitions, assist state-owned enterprises to quickly expand the channels for obtaining business informations, and try their best to find the crux of acquisitions, then solve the problems encountered in acquisitions (Renzhi, 2019).

Principal-agent theory states that there are two types of agency problems caused by the separation of owners from operators and the over-concentration of a single shareholding. "The lack of ownership" and "the dominance of one share" are serious agency problems in state-owned enterprises that has not been properly addressed (Jianbiao et al., 2016). As the "gatekeeper" of the enterprise, the executives of state-owned enterprises are in an advantageous position in terms of information possession, which increases the possibility of rent-seeking due to the existence of agency problems (Hongbo et al., 2008). When faced with a highly complex and risky decision, such as acquisitions, executives of state-owned enterprises may put their own interests before those of the company and develop a managerial defensive motive, abandoning the acquisitions in order to preserve their current position and their own Interests. For non-state capital in state-owned enterprises, promoting acquisitions in state-owned enterprises can increase their access to regulated or monopolistic industries, thereby strengthening their market power and reaping excess profits (Guan et al., 2021). The economic benefits generated by state-owned enterprises acquisitions are in turn related to the returns generated by the capital invested by non-state shareholders (Sujian, 2014). Therefore, a strong economic incentive of non-state shareholders inhibits the emergence of self-interest motives such as management defence by state-owned enterprises executives to the detriment of corporate interests. Board power provide non-state shareholders with the opportunity to participate in decision-making and overall supervision of state-owned enterprises as well as being used as a counterweight to the executives of state-owned enterprises by non-state shareholders (Dong et al., 2019), which enable non-state shareholders to guide state-owned enterprises in making acquisition decisions with the goal of "maximizing returns". Thus, hypotheses 1 is obtained:

Hypothesis 1: Non-state shareholder board power can drive acquisition decisions by state-owned enterprises.

3.2 The Moderating Effect of Board Deep-level Faultlines

When non-state shareholders join the board of state-owned enterprises, they are likely to be drawn in or excluded by a pre-existing sub-group, each of which will reduce the incentive for non-state shareholders to participate in governance to some extent. Due to board deep-level faultlines, board members focus most of their energy on confrontation or conflicts (Richard, Wu, Markoczy, & Chung, 2019), and may ignore advice and supervision of acquisition actions by non-state shareholders, who, because of their status, are also unable to resolve the conflicts involved and may ultimately decide not to speak out. Board power held by non-state shareholders in state-owned enterprises does not play a role in enhancing the efficiency of governance and providing market-based resources, and decisions on acquisitions by state-owned enterprises are still dominated by the executives or actual controller of state-owned enterprises. Ultimately, board deep-level faultlines undermine the advantages that non-state shareholders with board power would otherwise bring to state-owned enterprises in acquisitions. Accordingly,

hypothesis 2 is formulated:

Hypothesis 2: Board deep-level faultlines weaken the contribution of non-state shareholder board power to state-owned enterprises acquisition decisions.

4. Research Design

4.1 Sample Selection and Data Sources

The study tests the research hypothesis by selecting a sample of A-share listed state-owned enterprises in China for the period of 2008 to 2019. The starting year for the study was chosen as 2008 because it was only after the completion of the shareholding reform in 2007 that non-state shareholders gained access to state-owned enterprises to participate in governance. The following exclusions and filters were applied to the sample data with reference to existing studies: (1) exclude samples from the financial sector; (2) exclude samples that have been delisted; (3) exclude samples from the ST and PT categories for the year; (4) exclude samples with failed acquisition transactions; (5) exclude samples with acquisition transactions of less than ¥500,000; (6) screen out samples where the subject of the acquisition is only equity; (7) if a company makes multiple acquisitions in a year, retain only the one with the larger acquisition transaction amount; (8) exclude samples with abnormal financial data (gearing ratio less than 0 or greater than 1) and those with serious deficiencies. A final sample of 6515 observations was obtained.

The data used for constructing the variable of non-state shareholders' board power were collected manually. First, the data was collected on the state-owned enterprises' directors who served in shareholders' enterprises (excluding those who served in the financial enterprises) from the CSMAR database. Moreover, the directors' nature was determined by nature of shareholders' enterprises in which they serve, and the nature of shareholders' enterprises is obtained from "sky-eye search" and other related websites. If a director serves in a non-state shareholder, the study considers that the director is appointed by non-state shareholder. This means that non-state shareholders have board powers. In addition, the director characteristics and other financial data used are obtained from CSMAR database.

4.2 Variable Measurement

4.2.1 Dependent Variable

Acquisition decisions (M&A). In the research, following Li (2018) and others, acquisition decision was defined as whether state-owned enterprises initiated acquisitions in the year. If the company initiated acquisitions in the year, it was recorded as 1; otherwise, it was recorded as 0.

4.2.2 Independent Variable

Non-state shareholder board power (Power). The research referred to the metric of Ludong (2019) et al. and uses two indicators namely whether non-state shareholders have board power (If_power) and the weight of board power (R_power), to represent non-state shareholders board power. The first was measured by whether the non-state shareholder appoints directors to the board of state-owned enterprises, with a value of 1 if it does and 0 otherwise, while the second was measured by the ratio of the number of directors appointed by non-state shareholders to the board of directors of state-owned enterprises to the total number of directors on the board.

4.2.3 Adjustment Variable

Board deep-level faultlines (FSL). The calculation of board deep-level faultlines usually contains two methods: one is the Fau algorithm of Thatcher (2003) et al. and the other is the FLS algorithm of Shaw (2004) et al. The Fau algorithm is generally applicable to groups consisting of four to six members, while the number of Chinese board members is generally between five and 19. Therefore, rather than Fau algorithm, the FSL algorithm was adopted to calculate board deep-level faultlines strength in this study.

Educational attainment represents the deeper characteristics, which is therefore used in this study as the focal feature for calculating board deep-level faultlines, in addition to which tenure and age are selected as other supporting features for calculating board deep-level faultlines. First, the features were classified and assigned values following Kuusela (2016), Zhu (2013) and others. Educational attainment was classified according to academic qualifications as secondary school and below, college, bachelor's degree, master's degree and doctorate, with values of 1, 2, 3, 4 and 5 assigned, respectively; the term of office was divided into less than 3 years, 3 to 6 years and more than 6 years according to the number of years as a director, with a value of 1, 2 and 3, respectively; age was divided into four categories for members born between 1928 and 1945, 1946 and 1960, 1961 and 1979, and 1980 and 1995, with values 1, 2, 3 and 4. Second, the internal consistency (IA) of the subgroups, a value that reflects the degree of similarity of the ancillary characteristics of members within the

subgroups other than the focal characteristic, was calculated. Again, the consistency between subgroups (CGAI) was calculated, which reflects the degree of similarity between subgroups for ancillary characteristics other than the focal feature. Finally, the strength of board deep-level faultlines formed based on the deep focal feature was calculated as FSL = IA*(1-CGAI), a value between 0 and 1, with closer to 1 indicating a stronger board deep-level faultlines.

4.2.4 Control Variable

The research synthesizes existing research and controls for a number of factors that may influence state-owned enterprises' acquisition decisions, including: Occupancy rate (Occupy), measured with other receivables/total assets; return on net assets (Roe), measured as net profit/owner's equity; board size (Board), measured as the total number of board members; listage, measured as ln(current year-year listed+1); and operating income growth (Growth), measured with (current year's operating revenue / previous year's operating revenue)-1. In addition, the Year and Industry dummy variables are also controlled.

4.3 Model Design

To test the research hypotheses, the following regression models (1) and (2) are constructed respectively:

$$M\&A_{i,t}=\beta_{1/2}*[If\_Power_{i,t}/R\_Power_{i,t}]+\sum\beta_x*Cons_{i,t}+\sum Year+\sum Industry+\varepsilon_{i,t} \quad (1)$$

$$M\&A_{i,t}=\beta_{1/2}*[If\_Power_{i,t}/R\_Power_{i,t}]+\beta_3*[If\_Power_{i,t}/R\_Power_{i,t}]*FSL_{i,t}+\beta_4*FSL_{i,t}+\sum\beta_x*Cons_{i,t}+\sum Year+\sum Industry+\varepsilon_{i,t} \quad (2)$$

Models (1) and (2) are both fixed-effects models, and model (2) adds a cross-multiplication term between the moderating variables and the independent variables to model (1) to test the moderating effect of board deep-level faultlines, where Cons represents all control variables, t denotes year, β is a constant term and ε denotes a random disturbance term.

5. Research Result

5.1 Descriptive Statistical Analysis and Correlation Analysis of Main Variables

Table 1 below shows the results of the descriptive statistical analysis and correlation analysis of the main variables. The mean value of acquisition decisions (M&A) is 0.307, as can be seen from the results of the descriptive statistics, indicating that approximately 31% of the firms initiated mergers and acquisitions during the sample period. For the two indicators of non-state shareholders board power, the mean value of the presence or absence of board power (If_power) is 0.240, while the mean value of the proportion of board power (R_power) is 0.046, reflecting the fact that non-state shareholders were able to gain board power in state-owned enterprises after 2007, but with less power. The mean value of board deep-level faultlines (FSL) is 0.203, indicating that there are no strong deep fracture zones in state-owned enterprises boards, and the standard deviation is 0.111, indicating that the strength of board deep-level faultlines varies between enterprises. The results of the correlation analysis tentatively verify that non-state shareholders board power can motivate state-owned enterprises to make acquisition decisions.

Table 1. Results of Descriptive Statistical Analysis and Correlation Analysis of Variables

Variables	Mean	S.D.	Min	Max	M&A	If_power	R_power	FSL
M&A	0.307	0.461	0	1	1			
If_power	0.240	0.427	0	1	0.138***	1		
R_power	0.046	0.098	0	0.444	0.143***	0.842***	1	
FSL	0.203	0.111	0	0.553	-0.017	0.042***	0.043***	1

Note. *, ** and *** are represent the significance level of 10%、5%、1% respectively.

5.2 Regression Analysis

Table 2 presents the regression test results of the influence of non-state shareholders board power on acquisition decisions by state-owned enterprises, and the moderating role of deep-level faultlines. Column one includes only the coefficients related to the control variables. The second and third column provide a test of hypotheses 1 by including two indicators of non-state shareholders board power in the equation along with the control variables, respectively. The variable non-state shareholders board power (If_power and R_power) coefficients are both positive and significant (β = 0.044, p < 0.1; β= 0.333, p < 0.01). The results show that a positive correlation exists between non-state shareholders board power and acquisition decisions. Therefore, hypothesis 1 is supported. The fourth and fifth columns add adjustment variables to test the moderating role of board deep-level faultlines in the main effect. The variable non-state shareholders board power (If_power and R_power) remains a positive and significant correlation with the likelihood of acquisitions (β = 0.044, p < 0.1; β= 0.344, p < 0.01),

and the interaction term between the variable non-state shareholders board power (If_power and R_power) and board deep-level faultlines (FSL) is negative ($p<0.05$ or $p<0.01$), which shows that board deep-level faultlines inhibit the positive promotion of non-state shareholders board power on acquisition decisions. Therefore, the results support hypothesis 2.

Table 2. Regression Analysis Results

Variables/Model	(1) M&A	(2) M&A	(3) M&A	(4) M&A	(5) M&A
If_power		0.044*		0.044*	
		(0.023)		(0.023)	
R_power			0.333***		0.344***
			(0.109)		(0.109)
If_power*FSL				-0.318**	
				(0.133)	
R_power*FSL					-1.774***
					(0.598)
FSL				0.051	-0.028
				(0.067)	(0.059)
Occupy	0.666***	0.677**	0.686**	0.67**	0.678**
	(0.248)	(0.284)	(0.284)	(0.284)	(0.284)
Roe	0.158**	0.158**	0.158**	0.155**	0.155**
	(0.067)	(0.067)	(0.067)	(0.067)	(0.067)
Board	-0.014	-0.02	-0.015	-0.016	-0.012
	(0.06)	(0.06)	(0.06)	(0.06)	(0.06)
Listage	0.115***	0.121***	0.129***	0.118***	0.123***
	(0.023)	(0.023)	(0.023)	(0.023)	(0.024)
Growth	0.04**	0.04**	0.04**	0.04**	0.039**
	(0.017)	(0.017)	(0.017)	(0.017)	(0.017)
Year	Yes	Yes	Yes	Yes	Yes
Industry	Yes	Yes	Yes	Yes	Yes
_cons	-0.122	-0.144	-0.174	-0.153	-0.161
	(0.226)	(0.226)	(0.227)	(0.226)	(0.226)
Observations	6515	6515	6515	6515	6515
R-squared	0.332	0.332	0.333	0.333	0.334

Note. *, ** and *** are represent the significance level of 10%、5%、1% respectively.

5.3 Robustness Checks

5.3.1 Replacing the Regression Model

In the research, the dependent variable M&A is a dummy variable, therefore, the results of regressions (1), (2), (3) and (4) in Table 3, using the Logit model, show that the findings above are robust.

Table 3. Robustness Test Results

Variables/Model	(1) M&A	(2) M&A	(3) M&A	(4) M&A
If_power	0.229*		0.232*	
	(0.136)		(0.137)	
R_power		0.183***		1.878***
		(0.624)		(0.629)
If_power*FSL			-1.860**	
			(0.789)	
R_power*FSL				-9.778***
				(3.618)
FSL			0.406	-0.053
			(0.425)	(0.368)
Controls	Yes	Yes	Yes	Yes
Year	Yes	Yes	Yes	Yes
Industry	Yes	Yes	Yes	Yes
Observations	5275	5275	5275	5275
R-squared	0.108	0.109	0.109	0.111

Note. *, ** and *** are represent the significance level of 10%、5%、1% respectively.

5.3.2 Screen out Subsamples for Re-testing

Considering that there will be a long transition period from non-state shareholders being eligible to their actual entrance, it is possible that some of the non-state shareholder representatives introduced to the board of directors

of state-owned enterprises in 2008 were not actually in place. Therefore, this study again chose data between 2010-2019 as the sample to re-regress, and regressions (1), (2), (3) and (4) in Table 4 below are consistent with the results above.

Table 4. Robustness Test Results

Variables/Model	(1) M&A	(2) M&A	(3) M&A	(4) M&A
If_power	0.048* (0.027)		0.049* (0.027)	
R_power		0.344*** (0.125)		0.353*** (0.125)
If_power*FSL			-0.287* (0.148)	
R_power*FSL				-1.544** (0.647)
FSL			0.044 (0.076)	-0.025 (0.067)
Controls	Yes	Yes	Yes	Yes
Year	Yes	Yes	Yes	Yes
Industry	Yes	Yes	Yes	Yes
Observations	5535	5535	5535	5535
R-squared	0.348	0.349	0.349	0.350

Note. *, ** and *** are represent the significance level of 10%、5%、1% respectively.

6. Discussion

6.1 Research Findings

As Chinese mixed-ownership reform continues to develop further, the non-state capital is increasingly entering state-owned enterprises. Nevertheless, the way their influence on state-owned enterprises is exerted and the protection of their power and interests as shareholders remain to be studied. The research examines whether non-state shareholder board power affects acquisition decisions and fully considers the influence of faultlines.

All state-owned listed enterprises in A-shares in Shenzhen and Shanghai from to 2008–2019 were selected to explore the impact of non-state shareholders board power on acquisitions by state-owned enterprises. Moreover, the moderating role of deep-level faultlines in it was considered, and the following conclusions were drawn after empirical tests: (1) Non-state shareholders board power to facilitate acquisition decisions making in state-owned enterprises; (2) Board deep-level faultline will weaken the contribution of non-state shareholders board power to acquisition decisions.

6.2 Research Insights

Firstly, rather than a cosmetic project, mixed-ownership reform must seek ways to effectively safeguard the status and power of non-state capital in state-owned enterprises, and to "mix" in heterogeneous capital while paying more attention to "reform". Empowering non-state shareholders board power can genuinely expand the scope for non-state capital to practice decision-making and governance powers, then changing the "dictatorial rule" decision-making and governance format of the director in state-owned enterprises, reducing the chances of self-interest motivation and improving the efficiency of acquisition.

Secondly, state-owned enterprises need to implement a comprehensive approach to hybrid reform, not only by bringing in heterogeneous capital in multiple directions, but also taking the initiative to learn market-based operating mechanisms to complement their strengths and weaknesses. Non-state capital can provide state-owned enterprises with market-oriented information, technology and capabilities to assist them in implementing commercial investments such as acquisitions; non-state capital has a certain degree of flexibility in its governance style and can provide advice to improve the governance of state-owned enterprises and ease the rigidity of their governance mechanisms. If state-owned enterprises can fully learn from and absorb the advantages of non-state capital, they will become "stronger, better and bigger".

Thirdly, state-owned enterprises should focus on a reasonable mix of heterogeneous directors while improving the board structure to minimize the negativity of fracture zones in the boardroom. Although a board containing heterogeneous individuals cannot avoid faultline, appropriate allocation of board members and effective management of heterogeneous directors can reduce the negative effect of the faultline and prevent board misalignment, thus improve the efficiency of board governance and quality of decision-making.

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