

Three-dimensional framework
for SOE compensation reform
during the 15th Five-Year Plan
period

10 June 2026



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Introduction

2026 marks the rollout of China's 15th Five-Year Plan, ushering in a pivotal phase for the country to consolidate its foundational strengths and forge ahead toward the long-term objective of socialist modernization. The global landscape is experiencing profound shifts. The IMF forecasts global economic growth will remain stable at 3.3% in 2026 (see Chart 1), while the World Bank has downgraded its forecast to 2.6%, followed by a mild recovery to 2.7% in 2027 (see Chart 2). Rising geopolitical frictions, accelerating technological decoupling and industrial supply chain reconfiguration continue to drag on the world economy. On the domestic front, consumer demand remains subdued. Traditional industries struggle with overcapacity, whereas emerging industries encounter lasting obstacles to commercialization. China's transition from old to new growth drivers is gaining traction.

In this context, state-owned enterprises (SOEs) are confronted with three major headwinds: decelerating revenue growth, squeezed profit margins and growing risks of talent outflow (particularly in the digitalization, green and intelligent transformation areas). Talent shortage has turned from a latent risk into a constraint on high-quality development. Even as graduate numbers reach record levels, a disconnect persists between university education and industry needs. High-value talent – including senior executives and technical specialists with strategic foresight, cross-functional expertise and innovative mindsets – is in short supply across all sectors.

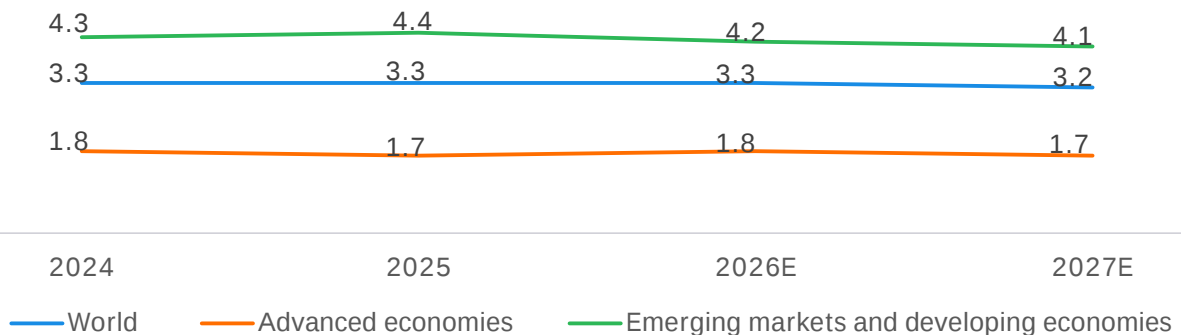


Chart 1: IMF, global economic growth projections (%)
Source: IMF, World Economic Outlook, January 2026

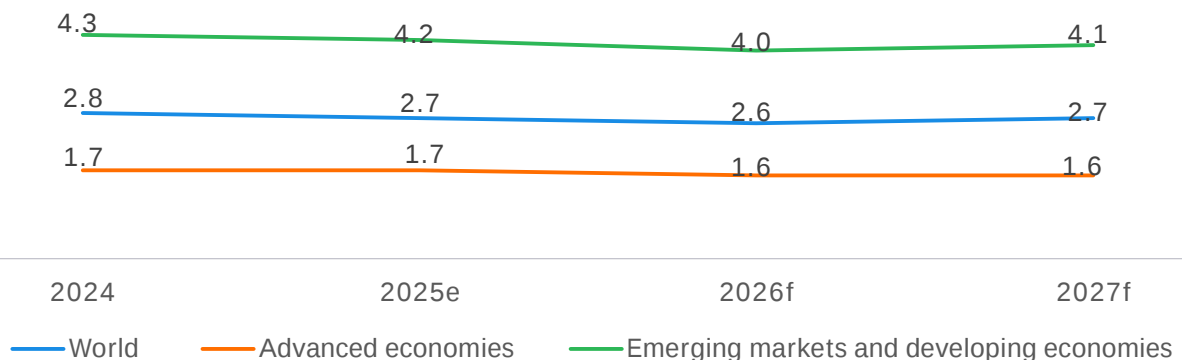


Chart 2: World Bank, global economic growth projections (%)
Source: World Bank, Global Economic Prospects, January 2026

Compensation is no longer a human capital expense. Instead, it serves as a core strategic lever across three dimensions:

- Attracting and retaining high-value talent in new industrialization, the green and low-carbon transition and Digital China initiatives.
- Boosting organizational vitality by translating top-tier strategic objectives into measurable, incentivized and actionable individual KPIs.
- Delivering higher quality, greater efficiency and lower costs through institutional innovation, even under rigid budget constraints.

Therefore, compensation reform is evolving into a core strategic priority that underpins modernized corporate governance and sustains a competitive edge during the 15th Five-Year Plan period. To fully tap growth potential and pursue high-quality development, enterprises should adopt holistic, forward-looking talent strategies balancing three trade-offs: centralized oversight vs. operational agility, internal pay equity vs. performance-based differentiation and short-term variable pay vs. long-term value alignment.

I. Prioritizing productivity gains: Leveraging the “one profit, five ratios” framework to embed labor productivity gains into the 15th Five-Year Plan execution

Background: The market paradigm is shifting from scale-centric expansion to quality-driven operations

Delivering high-quality development stands among the top priorities outlined in the 15th Five-Year Plan. SOEs are strengthening the “one profit, five ratios” assessment framework, which covers six core indicators: total profit, return on equity (ROE), asset-liability ratio, R&D intensity, total labor productivity and operating cash flow ratio. Notably, the operating cash flow ratio¹ – calculated as net operating cash inflows divided by revenue – has officially replaced the operating profit margin². The new metric captures the speed at which corporate revenue converts into real cash inflows, effectively mitigating the risk of inflated book profits under strained liquidity conditions. It provides a granular view of disposable cash flow generated within each assessment cycle, filters out accounting profits lacking cash backing and enables rigorous evaluation of top-line revenue quality. These regulatory refinements establish targeted, precise standards for operational management. SOE supervision has undergone a fundamental shift from output-oriented tracking to cash flow-based governance, and from scale expansion evaluation to sustainable growth monitoring. Moving forward, verifiable profitability, stable operating cash flow generation and sustained long-term growth capacity will serve as the cornerstones of SOEs’ high-quality development.

Meanwhile, human capital is evolving from a cost item into a productivity resource. Facing slowing revenue growth, squeezed gross margins and lengthening receivables cycles, SOEs can no longer rely only on capital expenditure or price adjustments to drive expansion. To unlock meaningful efficiency gains amid constrained resources, enterprises must elevate the economic value created per unit of labor. As the 15th Five-Year Plan launches amid fast technological disruption and fiercer cross-industry competition, corporate competitiveness hinges entirely on sound workforce and talent management systems. An organization’s ability to translate strategic priorities into executable frontline actions and convert workforce effort into measurable value creation determines its resilience to market fluctuations and long-term competitive position. Boosting labor productivity is far more than a HR task – it is a core strategic priority. SOEs need to adopt a holistic approach that integrates productivity optimization across corporate strategy, daily operations, incentive frameworks and culture development.

¹ Operating cash flow ratio = Net operating cash inflows/revenue × 100%, where “net operating cash inflows” refers to the actual cash received by the enterprise from the sale of goods and provision of services

² Operating profit margin = Net profit/revenue × 100%

■ Diagnosis: Three bottlenecks holding back labor productivity improvement

- Misaligned strategic deployment: Top-level corporate goals often fail to cascade into measurable, incentivized and actionable individual KPIs. This disconnect creates a rift between organizational priorities and staff behavior, wasting labor input and dragging down output efficiency.
- Oversimplified productivity diagnosis: Management frequently blames weak labor efficiency purely on overstaffing, resorting to blanket fixes including headcount cuts, hiring freezes and mandatory overtime. Such superficial solutions ignore deeper structural barriers: outdated workflows, immature digital systems and complex cross-team coordination. The outcome is heightened internal friction alongside sliding staff morale and retention.
- Flawed performance-incentive alignment: Pay and performance remain poorly integrated with no closed-loop mechanism linking productivity uplifts, incremental value creation and variable pay disbursements. Current incentive schemes overemphasize standalone profit metrics while discounting marginal efficiency gains from productivity upgrades. Companies thus drive profit growth via short-term cost trimming or one-off capital outlays, instead of enterprise-wide productivity transformation. This structural flaw prevents synchronized progress on ROE and overall labor productivity.

■ Three-step implementation approach

- Diagnostic assessment: Conducting comprehensive operational and maturity evaluations to verify whether existing organizational capacity can achieve the strategic goals set under the 15th Five-Year Plan. This stage identifies core operational pain points, business bottlenecks and decision-making inefficiencies across the organization.
- Tiered rollout of strategic targets: Systematically decomposing corporate strategies and cascading enterprise-wide operational and productivity KPIs across all levels. Tailored metrics are defined for each business unit, covering core outcome indicators, process milestones and productivity quality benchmarks, such as high-margin and emerging business revenue share, customer satisfaction, automation penetration and core operating profit contribution ratio.
- Dynamic adjustment: Building a cycle of “strategy + productivity optimization + execution” and fully embedding it into the formal performance management and compensation administration processes. This framework eliminates formalistic compliance and one-size-fits-all performance rating practices, enables differentiated performance evaluation and ensures timely disbursement of performance-linked compensation.

II. Balance as a complementary lever: Fairness and precision to address diverse business and governance challenges during the 15th Five-Year Plan period

■ Background: Growing governance complexity

As SOE reform deepens through the 15th Five-Year Plan period, conglomerates face two challenges:

- Diversified business portfolios: Traditional industrial upgrading, incubation of emerging sectors and forward-looking deployment of future industries follow distinct development cycles, each requiring tailored management and compensation incentive frameworks. As SOEs focus on core operations while advancing layout arrangements for strategic emerging industries, establishing consistent group-wide incentive mechanisms across varied business lines becomes a key pain point.
- Multi-layered hierarchies: The three-tier governance model – group headquarters, secondary platforms and project entities – has been fully implemented. Flattened management layers streamline decision-making workflows yet expand oversight responsibilities at every management level, raising governance risks stemming from limited supervisory bandwidth and overstretched management capacity.

■ Diagnosis: Imbalance in compensation incentive

- Egalitarian pay weakens performance differentiation: Constrained by rigid payroll budgets, some companies adopt egalitarian compensation practices that decouple pay raise from tangible value output. High-performing teams only receive marginal pay uplifts slightly above the company average, while underperforming entities maintain elevated base salaries inherited from legacy frameworks. This egalitarian approach weakens incentive effectiveness and contradicts the performance-oriented principle of high-quality development.
- Insufficient performance evaluation and compensation management: Performance assessments often become box-ticking exercises driven largely by subjective managerial judgment, without standardized quantitative benchmarks, tiered rating scales, or objective indicators to measure individual capability and deliverables. Since formal appraisal results are poorly aligned with actual pay outcomes, the performance management system loses credibility. This fosters a widespread perception that high and low performers are rewarded equally.
- Perceived pay inequity: Ambiguous evaluation criteria and opaque incentive allocation rules raise employee doubts regarding pay fairness. Within diversified conglomerates, inconsistent measurement standards across business units lead to imbalanced and unfair evaluation outcomes. Such perceived inequity is not merely a subjective sentiment, it undermines cross-team collaboration and weakens employees' willingness to execute corporate strategic priorities.

■ Four-dimensional implementation strategy

- Enforcing group-wide governance guardrails: Rolling out unified corporate standards – consistent compensation oversight protocols, standardized pay-performance linkage models, aligned compensation frameworks and harmonized internal talent mobility rules. These measures mitigate decentralization risks from unrestricted discretionary adjustments by subsidiaries while retaining reasonable room for localized fine-tuning.
- Adopting process-driven labor productivity tracking: Breaking down annual productivity targets into quarterly milestones and establishing dedicated incentive pools linked to interim performance. This shifts evaluation from retrospective year-end reviews to ongoing, actionable guidance. It addresses the tendency to overemphasize end results at the expense of sustained progress, helping maintain momentum toward achieving strategic objectives.
- Improving internal fairness: Perceived unfair pay mainly arises from inconsistent evaluation benchmarks and insufficient internal talent mobility. A two-pronged governance mechanism addresses these gaps: unified benchmarking and structured career ladders. A group-wide job evaluation library should be established to standardize job grading, providing the baseline for performance reviews and compensation calibration. This ensures uniform value assessment to facilitate talent rotation across subsidiaries. Building a central strategic talent pool to boost cross-subsidiary mobility, with formal provisions linking pay revisions to job transfers, guaranteeing consistent recognition of staff contributions group-wide.
- Deploying targeted, differentiated incentive schemes: Abandoning generic one-size-fits-all incentive frameworks to eliminate egalitarian pay and fully unlock contribution-oriented reward mechanisms. Incentive weights are customized across three dimensions: entity nature (perfectly competitive vs. public welfare divisions), business segment (traditional industries vs. strategic emerging sectors) and business lifecycle stage (incubation, growth, maturity).

III. Diversification as the key: Building an all-round compensation framework under the 15th Five-Year Plan

Background: Talent competition shifts from cash-centric remuneration to shared value alignment

During the 15th Five-Year Plan period, Generation Z and millennials are becoming the backbone of the domestic workforce. Their evolving values and career expectations are reshaping corporate reward strategies in three ways:

- **Balanced expectations for tangible compensation:** While employees still expect steady growth in base salaries, they place greater priority on structured career advancement and roles with meaningful intrinsic purpose.
- **Diversified expectations on non-financial values:** Institutional recognition, social impact and work-life balance are viewed as equally important as cash remuneration.
- **Strong expectations on timely, continuous recognition:** Employees seek timely, visible rewards to acknowledge incremental high performance delivered at all stages of the performance cycle.

Concurrently, authorities are rolling out national initiatives to boost entrepreneurship and foster a culture that values labor, expertise, talent and innovation. These policies formally endorse cultural recognition and non-monetary incentive schemes. SOEs sticking to cash-only reward systems face two major risks: sustained cost pressures and lost opportunities to forge deep value alignment with next-generation talent.

Diagnosis: Diminishing returns of traditional incentive schemes

- **Stagnant base pay growth:** Sluggish growth momentum has imposed stringent constraints on annual payroll budget increments, with some enterprises even rolling back payrolls. Such fiscal limitations restrict companies' capacity to expand headcount and recruit high-potential talent, thereby creating a structural misalignment between compensation resource allocation and corporate growth objectives.
- **Overreliance on annual performance evaluation for incentive distribution:** Over 90% of total incentive budgets are disbursed as annual performance bonuses. Monthly and quarterly performance reviews remain heavily reliant on managerial subjectivity. Aside from a narrow range of quantifiable KPIs, annual performance assessments lack systematic design covering work processes, business scenarios and employee behavioral dimensions, leading to one-sided and incomplete performance measurements.
- **Underutilization of non-monetary incentive resources:** Enterprises have abundant intangible human capital resources, including corporate brand influence and systematic professional training systems. Nevertheless, these resources bring limited value to most employees. Innovative non-monetary incentive tools are deployed in isolation without cross-functional integration, failing to generate synergies with the total rewards system.

Innovative toolkit: Multi-tiered incentive framework

This tiered, multi-cycle incentive architecture sustains short-term operational momentum, stabilizes medium-term workforce expectations and aligns employees' long-term interests with corporate strategic value creation. The framework consists of four core pillars: cash remuneration (ad hoc performance bonuses, deferred compensation), long-term value alignment (virtual equity, project co-investment schemes), career development (dual-track promotion pathways, cross-business rotation mechanisms) and real-time organizational and peer recognition.

- **Encouraging career development with incentives**
 - **Career growth accounts:** Establishing development funds to support external professional training, industry certification examinations, industry summit participation and premium learning resources.
 - **Strategic talent rotation programs:** A centralized talent pool facilitates cross-functional rotations for core and high-potential employees, with the enterprise covering all travel and training expenses.

- Innovative long-term value alignment instruments
 - Profit-sharing schemes for traditional enterprises: A portion of annual excess profits and underutilized team operational budgets is allocated to employee collective incentive pools and distributed proportionally based on individual performance contributions.
 - Hybrid incentive pilots for emerging enterprises: A customized incentive model integrates role-based profit sharing, virtual equity and project co-investment mechanisms. This design closely ties core talent's financial interests to corporate and project operational performance.
- Scenario-based customized benefit portfolios
 - Young talent: Tailored benefits including rental subsidies, home purchase policy consultation and urban integration programs help early-career employees resolve settlement challenges.
 - Core leadership: Senior executives receive annual comprehensive health check-ups, supplementary medical insurance and exclusive professional mental health counselling services.
 - Female workforce: Flexible remote work arrangements, childcare subsidies and exclusive Mother's Day benefits are offered to enhance female employees' work-life balance.
- Real-time visualized recognition mechanisms
 - Instant performance recognitions: A "moments of excellence" module is embedded within corporate WeChat or DingTalk, allowing employees to submit outstanding cases of innovation, cross-team collaboration and client success. Qualified contributions generate recognition points to boost employee exposure and professional engagement.
 - Standardized recognition weighting: Peer recognition frequency, internal knowledge sharing and mentorship contributions are quantified and incorporated into annual performance assessment metrics.
 - Star contributor honors: Quarterly awards recognize high-performing teams and individuals who deliver key strategic milestones, with C-suite executives presenting official "strategic contribution medals" to outstanding recipients.

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