

Abstract

This paper explores the connection between the external opening of China and differences in innovation across Chinese regions. Controlling for locational advantages and fixed regional characteristics, for the period 1995-2010 overall we find that regions that have increased most the connections to the world market have become more innovative when compared to other regions. By interacting regional characteristics with openness, we find a U-shaped relation between regional income levels and innovation, where both the lower middle-income and the most advanced regions gain from globalization in terms of increased innovation and productivity. In relative terms, the higher middle-income regions gain less from globalization than the other regions. By examining the nature of international activities across regions, we conjecture that differences in the ownership structures of foreign investments and the nature of linkages between foreign and domestic firms are at the heart of this finding, as the higher middle-income regions have higher outsourcing levels and thus benefit less from foreign technology transfers.