

## Product Innovations in Emerging Economies: The Role of Foreign Knowledge Access Channels and Internal Efforts in Chinese Firms

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**ABSTRACT** In this paper, we theoretically and empirically investigate factors that contribute to product innovation by firms in emerging markets. Combining the innovation literature with the latecomer literature on ‘catch-up’ strategies of firms in newly industrialized economies, we posit that access to foreign knowledge is essential for fostering product innovation. In particular, we investigate how innovation clusters formed by inward foreign direct investments in an emerging market and export activities of a firm are effective channels for acquiring foreign knowledge. We also suggest firms that invest in research and development and marketing activities benefit further from access to foreign knowledge due to increased absorptive capacity. Empirically, we employ information on over 160,000 indigenous manufacturing firms in China in 2005–2006. We find strong empirical support for our theoretical framework and conclude by discussing the implications for both theory and managerial practice.

**KEYWORDS** China, clusters, learning by exporting, marketing, product innovation, research and development (R&D)

### INTRODUCTION

Innovative activity is a critical determinant of competitive advantage (Porter, 1990). Since most innovative activity occurs or has occurred in developed countries, it is not surprising that most of our understanding of the determinants and effects of innovative activity comes from studies of firms in those markets (e.g., Cohen & Levinthal, 1990; Dosi, 1988). Although firms in emerging economies are commonly regarded as laggards in innovation, especially in cutting-edge innovations (Altenburg, Schmitz, & Stamm, 2008), recent evidence, derived mainly from case studies, suggests that firms in emerging markets do in fact innovate (Lu, 2000). Computing companies in China and pharmaceutical companies in India are able to develop new products either by adding significant value to imported foreign products or technologies or by developing new products to satisfy specific domestic