REVIEW
Government Subsidies and Enterprise Innovation: Moderation Effect of Absorbed Slack

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ABSTRACT
It is worth studying whether enterprises receiving government subsidies can transform them into innovative achievements under the constraints of enterprise resources. The data from the three industries of electronics, pharmaceuticals, and information technology during 2013-2016 were empirical tested to verify the moderating effect of the absorbed slack on the relationship between government subsidies and enterprise innovation. The results show that government subsidies can promote enterprise innovation; absorbed slack promotes enterprise innovation; the absorbed slack of enterprises plays a positive moderation role in the relationship between government subsidy and enterprise innovation. In other words, the enterprises with high absorbed slack can promote the innovation of enterprises by government subsidies. The conclusions provide theoretical guidance for government departments to select the most suitable enterprises which accept innovative subsidies.

1. Introduction
The report of the 19th National Congress pointed out that innovation is the primary driving force of development. Chinese development is in transitional period, and there is a gradual establishment and enhancement process for the main position of technological innovation of enterprises[1]. In this process, the market cannot provide sufficient innovation power for enterprises, so the government needs to intervene[2]. In order to effectively guide enterprises to change their business concepts and focus on independent innovation, governments at all levels are consciously striving to build innovative platforms and provide supporting innovative resources, such as providing corresponding government subsidies for specific industries and enterprises. From the figures, in 2005-2017, China’s fiscal expenditure on science and technology increased from 133.5 billion Yuan to 729.6 billion Yuan, which can also indirectly prove the fact that government subsidies are increasing.

On the one hand, Government subsidies provide incentives, and on the other hand, they alleviate the financing

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difficulties of enterprises and make up for the imperfections in the external financing market. However, whether government subsidies can certainly promote enterprise innovation remains to be further analyzed. After combing the existing research results, scholars mainly analyze from three perspectives. First, from the perspective of enterprises themselves, to analyze the role of government subsidies on enterprise innovation, that is, from the innovation conditions of enterprises; the second is to analyze the relationship between government subsidies and enterprise innovation from the perspective of the government itself, that is, from the perspective of quantity and strength of government subsidies; the third is to study government subsidies and enterprise innovation from the perspective of external environment, that is, in the whole social environment. There is an inconsistency in the conclusion. Some studies have found that the government promotes enterprise innovation, and government subsidies have an “Incentive Effect” on enterprise innovation. It will greatly encourage enterprises to increase R&D investment and drive innovation output; or government subsidies directly promote enterprise innovation; or government subsidies can attract more investment, and then promote enterprise innovation. Another part of the studies found that government subsidies inhibit enterprise innovation, and the government’s R&D subsidies have “crowding out effects” or “substitute effects”, which will crowd out the company’s own R&D investment, thereby reducing enterprise innovation resources; or when government officials have paying more attention to local GDP and employment, government subsidies are more likely to flow to less productive enterprises, it makes government subsidies to be less effective than expected. The inconsistency of the research conclusions shifts the attention of the research to other influencing factors, that is, considering the internal factors of the enterprise.

Redundant resources belong to the internal factors of enterprises. There are different levels of redundant resources in the enterprise, such as redundant cash, idle production equipment, etc. According to flexibility and mobility, they can be divided into absorbed slack and unabsorbed slack. For example, redundant cash is unabsorbed slack, while idle production equipment is absorbed slack. These redundant resources can play a buffer role to help enterprises adapt to internal and external pressures. Although unabsorbed slack has strong mobility and flexibility, it is not related to the key business of the enterprise, it cannot provide help when the enterprise is facing changes in an increasingly dynamic environment. Unabsorbed slack must be transformed into absorbed slack in order to play its role. Redundant resources can support enterprise innovation, reduce internal pressure, relieve external shocks, and ensure the stability of the enterprise. Therefore, in view of the instability of the relationship between government subsidy and enterprise innovation, this paper introduces absorbed slack as moderate variables to test the changes of the relationship between government subsidy and enterprise innovation, so as to clarify the research boundary of the model.

2. Literature and Hypothesis

Enterprise innovation refers to the change of products, production technology or management methods, which is the inevitable choice for enterprises to seek long-term development. Innovation is the driving force of sustained economic growth, while resources do not always flow smoothly to innovation, especially when the leading force of enterprises supports the normal business activities. Therefore, the effective solution to the problem of resource supply has become the primary issue of successful implementation of enterprise innovation. Government subsidy relieves the financing difficulties of enterprises to a great extent, but whether government subsidy promotes enterprise innovation remains to be further studied. This paper holds that although the way and intensity of government subsidies have a great impact on innovation, the key factors affecting innovation are the conditions of enterprises themselves and the external environment. On the one hand, redundant resources are inherent to every enterprise, which are the characteristics of the enterprise. Whether redundant enterprises can easily convert government subsidies into enterprise innovation resources is worth studying; On the other hand, the external environment of enterprises has changed dramatically. It is worth exploring whether the high uncertainty of the environment hinders enterprises from transforming government subsidy into innovation. Further analysis, for enterprises, it is worth to analyze and test whether the internal and external factors will overlap and act together on the transformation of government subsidies into innovation process.

2.1 The Relationship between Government Subsidies and Enterprise Innovation

The operation and investment activities of enterprises need corresponding resources as support. Resources are an important source for enterprises to build and maintain their competitive advantages. Especially for enterprise innovation, more resources are needed, such as sufficient funds, high-quality equipment, innovative decision makers, etc. Among them, financial support is the most basic driving force. Only when enterprises have sufficient funds,
can they invest in R&D and then innovate, in the case of maintaining normal operation. Enterprise investment is the main source of funds for R&D activities, but the actual R&D investment of enterprises is often lower than the optimal level. This is because the high risk of R&D investment exists, and the knowledge spillover in R&D investment enables other competitors to share knowledge, thus enhancing the innovation capability of enterprises without any additional costs [26]. In this case, government subsidies are needed to guide enterprises to invest in R&D. Government subsidies can effectively reduce the investment cost and risk of enterprises, stimulate R&D investment of enterprises, give full play to the positive externalities of R&D investment of enterprises, and promote the upgrading of innovation ability of the whole industrial chain [27]. From the perspective of factor endowment, the production function composed of different factor inputs has an important impact on enterprise’s profit and competition. Technological input and innovation have multiplier effect, but it is a high-risk and high-cost activity. In order to avoid risks and reduce costs, many enterprises often choose cheap and sufficient factors of production, which is not conducive to the considerable progress of enterprises. However, government subsidy can reduce the risk of technological investment of enterprises, which is conducive to technological investment and innovation, transformation of production mode and stimulation of multiplier effect of technological innovation [28]. From the perspective of information asymmetry, Keynesian economics believes that the market is not omnipotent, free market is prone to market failure. When enterprises need R&D investment, it is difficult to obtain external investment because of information asymmetry. At this time, government subsidies act as a visible hand in the market. Government subsidies disseminate a favorable signal [29-30], which means that the enterprise project is focused by the government and has huge market potential. At the same time, it also reveals that the enterprise has good reputation and makes it easier for enterprises to obtain bank loans and outside investment. While financing pressure decreases, enterprises obtain more funds for R&D investment and promote enterprise innovation.

**Hypothesis 1: government subsidies can promote enterprise innovation.**

### 2.2 The Relationship between Absorbed Slack and Enterprise Innovation

Cyert and Arch (1963) first put forward the concept of redundant resources, that is, resources beyond the actual needs of the organization are redundant resources [31]; that is to say, an excessive but freely available resource is a redundant resource [19]. Redundant resources are the inevitable result of the production and operation of enterprises, which can help enterprises resist foreign risks and accidents, and ensure the normal operation and development of enterprises. The existence of redundant resources gives managers more choices when facing innovative projects [32]. When facing financing constraints, the role of redundant resources is unprecedentedly important [33]. If enterprises can make rational use of redundant resources, on the one hand, it eases the financing pressure of enterprises, enterprises can try more innovative projects, which is conducive to the innovation and development of enterprises; on the other hand, the rational utilization of redundant resources enhances the ability and confidence of enterprises to resist innovation risks, while other enterprises will not easily try the high cost and risk innovation. Redundant resources can reduce enterprises’ fear of innovation failure, and help to form an innovative culture and create an innovative atmosphere.

Further subdividing the redundant resources, unabsorbed slack has strong flexibility, such as cash or cash equivalents, but it is not oriented to the specific situation of enterprises, and the process of transforming into innovative resources is long. Therefore, unabsorbed slack is difficult to help enterprises form special advantages in the field of innovation. Comparatively speaking, absorbed slack is more closely related to enterprises. Absorbed slack includes machinery, equipment, human resources, and knowledge reserve, which are embedded in a specific situation and cannot be used arbitrarily. Research and development on the basis of these proprietary resources (patented technology, skilled experts) can greatly save the time of equipment acquisition and personnel selection and improve the efficiency of innovation. Once the enterprise’s surplus management ability is in line with the reality, it will provide a more relaxed and powerful R&D environment for enterprise innovation. Absorbed slack exists as a key innovation factor to directly support product innovation [31]. Specific redundancy also promotes enterprise progressive innovation [33]. There are some risks in enterprise innovation, the effect will be discounted if there is not enough resources to support enterprise innovation [31], redundant resources enhance the ability of enterprises to resist risks, so enterprises dare to carry out various innovation experiments [34].

**Hypothesis 2: Absorbed slack promotes enterprise innovation.**

### 2.3 The Impact of Absorbed Slack on the Relationship between Government Subsidies and Enterprise Innovation
Enterprises seek innovative developments, which need not only sufficient funds, but also other resources, such as idle machinery and equipment, skilled workers and so on. If enterprises have these absorbed slack resources, enterprises will be more likely to use government subsidies for R&D investment faster and more effectively, when enterprises get government subsidies. Because the idle machinery and equipment, skilled workers and other factors of production can be put into production quickly to shorten the innovation time, on the other hand, reduce the expenditure of re-purchasing machinery and equipment and training skilled workers, and the management costs and staff salaries owned by enterprises themselves can also reduce the extra expenditure of enterprises, so that government subsidies can be spent on innovation as fast as possible. Resources do not always flow smoothly to innovation and the process of innovation needs to consume resources, so redundant resources are very important. Redundant resources help enterprises to explore innovative projects, especially for those enterprises facing financing constraints. Redundant resources can provide strong support for enterprises to develop new products or enter new markets. Redundancy provides some resources for enterprises to innovate and change, so it improves the ability of enterprises to cope with environmental changes. When there is less redundancy in an enterprise, management is not inclined to take strategic measures to improve performance, but rather to improve the internal environment, reduce costs and improve performance. That is to say, when a company has scarce absorbed slack, government subsidies cannot greatly promote the R&D investment of enterprises, because such enterprises have a greater risk of R&D investment, which requires a lot of R&D preparation, including the purchase of machinery and equipment, factory buildings, hiring skilled workers and so on, all of which need to spend a certain amount of money, to a large extent, it will weaken the financing space brought about by government subsidies.

**Hypothesis 3:** The absorbed slack moderate the relationship between government subsidies and enterprise innovation. When enterprises have more absorbed slacks, government subsidies play a stronger role in promoting enterprise innovation.

### 3. Research Design

#### 3.1 Data Sources

The empirical analysis is based on China’s High-tech industries. Data from enterprises listed in China in three industries of electronics, pharmaceuticals and information technology from 2013 to 2016 are collected. In order to investigate the sustainability of the effect of government subsidies, t+1 year innovation data (2014-2017) are used to test t year innovation. These three industries belong to the field of high-tech, focusing on R&D and innovation. After data processing, 199 enterprises can be studied and 796 observation values are obtained. Relevant data are from CSMAR database and enterprise annual reports.

### 3.2 Measurement

The dependent variables are enterprise innovation (Inno). The common variables to measure enterprise innovation are: R&D cost, number of inventions and patents, and number of new products. The number of inventions, patents and new products is usually used to measure the innovation output of enterprises, but not all invention patents can be converted into products and put into the market to play their value. In addition, the awareness of patent protection of enterprises in China is not strong, and there are some limitations in using the number of patents to measure enterprise innovation. Therefore, this paper chooses the ratio of R&D investment to total assets to measure enterprise innovation.

The independent variable is government subsidies (Sub). The government subsidy index are measured as the part of government funds of all funding for scientific and technological activities of enterprise.

The moderating variable is absorbed slack (As). According to the previous literatures, the ratio of management cost to sales revenue is used to measure the absorbed slack of enterprises.

Control variables. Enterprise size (Size), debt pressure (Debt), development ability (Dep), profitability(Profit) and cash flow (CF) may have an impact on enterprise innovation. Therefore, these variables are put into the model as control variables. The logarithm of the number of employees is used to measure the scale of the enterprise, the asset-liability ratio of the enterprise is used to measure the debt pressure of the enterprise, the ratio of the total operating income of the current year minus the total operating income of the previous year to the total operating income of the previous year is used to measure development ability, the ratio of net profit to the shareholder equity balance is used to measure the enterprise’s profitability, The ratio of cash flow to business income at the end of each year is used to measure the enterprise’s cash flow.

### 3.3 Method Selection

From the data we can see, it has both cross-sectional dimension and time dimension, which is a panel data. The time dimension of the data is 4, the cross-sectional dimen-
sion is 199, and the time dimension is obviously smaller than the cross-sectional dimension, so this is a short panel data. In order to ensure the rigor of the study, Hausman test was used to determine whether to use short panel fixed effect regression or random effect regression. The test results showed that the P value was 0.2492, which accepted the original hypothesis, so the random effect model was adopted.

3.4 Hypothesis Model

According to the variable selection and research content of this paper, the following models are set to test the hypothesis:

\[ \ln(m+1) = \beta_0 + \beta_1 \ln(t) + \alpha_1 \ln(z) + \alpha_2 \ln(x) + \alpha_3 \ln(y) + \alpha_4 \ln(f) + \varepsilon \]

The results in Table 2. There is only control variables and dependent variables in Model 1; then government subsidies is added on the basis of Model 1 to build Model 2; absorbed slack is added on the basis of Model 1 to build Model 3; Model 4 is a complete model, which includes control variables, government subsidies, absorbed slack and their interactions.

4. Results and Analysis

4.1 Descriptive Statistics and Correlation Analysis

From Table 1, there are descriptive statistics of main variables and correlation analysis among variables, including mean, standard deviation and correlation coefficient of variables. The correlation coefficient between government subsidy and enterprise innovation is 0.231 (p < 0.001), which indicates that there is a positive correlation between government subsidy and enterprise innovation. The more subsidies the government provides the more innovations the enterprise will have in the future. Overall, the correlation coefficient between independent variables is not very high. Furthermore, the VIF value shows that the maximum VIF value is 1.76, it means all of them are less than 2. It can be seen that multiple collinearity does not exist in this paper.

4.2 Empirical Results

In this paper, stratified regression method is used to test the main effect and moderation effect. In order to reduce the multi-collinearity, the government subsidies, absorbed slack should be centralized. The results are shown in Table 2. There is only control variables and dependent variables in Model 1; then government subsidies is added on the basis of Model 1 to build Model 2; absorbed slack is added on the basis of Model 1 to build Model 3; Model 4 is a complete model, which includes control variables, government subsidies, absorbed slack and their interactions.

From Table 2, we can see that the regression coefficient of government subsidy in model 2 is positive and significant at the level of P < 0.001. That is, the more subsidies the government provides, the more innovations the enterprise makes, so Hypothesis 1 is verified. The results of model 3 show that the regression coefficient of absorbed slack is positive and significant at the level of P < 0.001. It can be seen that the more absorbed slack the enterprise owns, the better innovation enterprise makes. Hypothesis 2 is verified. From model 4, we can see that the coefficient of interaction between government subsidy and absorbed slack is positive and significant at the level of P < 0.01. Hypothesis 3 is verified, the moderating effect exists, that is, absorbed slack has a positive moderating effect on the relationship between government subsidy and enterprise innovation. Among the control variables, corporate debt is

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>SD</th>
<th>Inno</th>
<th>Sub</th>
<th>As</th>
<th>Ch</th>
<th>Lnsize</th>
<th>Debt</th>
<th>Dep</th>
<th>Profit</th>
<th>Cf</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inno</td>
<td>0.035</td>
<td>0.046</td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sub</td>
<td>15.888</td>
<td>1.248</td>
<td>0.231***</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As</td>
<td>0.156</td>
<td>0.108</td>
<td>0.222***</td>
<td>0.177***</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ch</td>
<td>0.024</td>
<td>0.116</td>
<td>0.124***</td>
<td>-0.049</td>
<td>0.406***</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Lnsize</td>
<td>7.311</td>
<td>0.963</td>
<td>0.062</td>
<td>0.281***</td>
<td>-0.251***</td>
<td>-0.156***</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Debt</td>
<td>0.288</td>
<td>0.386</td>
<td>-0.041</td>
<td>0.174***</td>
<td>-0.226***</td>
<td>-0.066***</td>
<td>0.255***</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Dep</td>
<td>0.276</td>
<td>0.542</td>
<td>-0.011</td>
<td>-0.023</td>
<td>-0.180***</td>
<td>-0.068</td>
<td>0.149***</td>
<td>0.109***</td>
<td>1.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit</td>
<td>0.070</td>
<td>0.321</td>
<td>0.006</td>
<td>-0.095***</td>
<td>-0.066</td>
<td>-0.065</td>
<td>0.067</td>
<td>0.087</td>
<td>0.253***</td>
<td>1.000</td>
<td></td>
</tr>
<tr>
<td>Cf</td>
<td>0.700</td>
<td>0.972</td>
<td>0.001</td>
<td>-0.025</td>
<td>0.554***</td>
<td>0.307***</td>
<td>-0.315***</td>
<td>-0.398***</td>
<td>-0.156***</td>
<td>-0.032</td>
<td>1.000</td>
</tr>
</tbody>
</table>

Notes: *** (**) (*) indicate a significance level of 1% (5%, 10%)
negatively correlated with innovation capability.

Table 2. The regression results of enterprise innovation

<table>
<thead>
<tr>
<th></th>
<th>M1</th>
<th>M2</th>
<th>M3</th>
<th>M4</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>0.036*</td>
<td>-0.052*</td>
<td>0.017</td>
<td>-0.061**</td>
</tr>
<tr>
<td></td>
<td>(1.71)</td>
<td>(-1.73)</td>
<td>(0.79)</td>
<td>(-1.98)</td>
</tr>
<tr>
<td>Sub</td>
<td></td>
<td>0.006***</td>
<td></td>
<td>0.006***</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(2.94)</td>
<td></td>
<td>(2.68)</td>
</tr>
<tr>
<td>As</td>
<td></td>
<td>0.106***</td>
<td></td>
<td>0.086***</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(3.69)</td>
<td></td>
<td>(4.12)</td>
</tr>
<tr>
<td>Sub*As</td>
<td></td>
<td></td>
<td>0.034**</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(2.06)</td>
<td></td>
</tr>
<tr>
<td>Size</td>
<td>0.001</td>
<td>-0.0003</td>
<td>0.001</td>
<td>0.001</td>
</tr>
<tr>
<td></td>
<td>(0.23)</td>
<td>(-0.10)</td>
<td>(0.55)</td>
<td>(0.21)</td>
</tr>
<tr>
<td>Debt</td>
<td>-0.012**</td>
<td>-0.015**</td>
<td>-0.015**</td>
<td>-0.024***</td>
</tr>
<tr>
<td></td>
<td>(-2.55)</td>
<td>(-2.41)</td>
<td>(-2.41)</td>
<td>(-3.13)</td>
</tr>
<tr>
<td>Dep</td>
<td>-0.003</td>
<td>-0.001</td>
<td>-0.001</td>
<td>-0.001</td>
</tr>
<tr>
<td></td>
<td>(-1.37)</td>
<td>(-0.44)</td>
<td>(-0.44)</td>
<td>(-0.47)</td>
</tr>
<tr>
<td>Profit</td>
<td>0.001</td>
<td>-0.002</td>
<td>0.002</td>
<td>0.001</td>
</tr>
<tr>
<td></td>
<td>(0.59)</td>
<td>(-0.93)</td>
<td>(0.93)</td>
<td>(0.62)</td>
</tr>
<tr>
<td>Cf</td>
<td>-0.002</td>
<td>-0.006**</td>
<td>-0.006**</td>
<td>-0.061**</td>
</tr>
<tr>
<td></td>
<td>(-1.31)</td>
<td>(-2.32)</td>
<td>(-2.32)</td>
<td>(-3.40)</td>
</tr>
</tbody>
</table>

Notes: *** (**, *) indicate a significance level of 1% (5%, 10%)

In order to further verify moderation effect of absorbed slack, the figure is drawn. As shown in Figure 1, the horizontal axis is government subsidies; the vertical axis is enterprise innovation. Solid lines indicate low absorbed slack and dotted lines indicate high absorbed slack. It can be found that in the case of absorbed slack (high or low absorbed slack), enterprise innovation increases with the increase of government subsidies. And in the case of low absorbed slack, the increase of enterprise innovation with the increase of government subsidies is smaller. While absorbed slack is higher, the increase of enterprise innovation with government subsidies is larger. It can be seen that absorbed slack has a positive moderation effect on the relationship between government subsidies and enterprise innovation, that is, the more absorbed slack enterprises have, the more obvious the role of government subsidies in promoting enterprise innovation.

5. Conclusion

This paper estimates the relationship between government subsidies and enterprise innovation under the constraints of enterprise resources. The results show that government subsidies can promote enterprise innovation; absorbed slack promotes enterprise innovation; the absorbed slack of enterprises plays a positive moderation role in the relationship between government subsidy and enterprise innovation. In other words, the enterprises with high absorbed slack can promote the innovation of enterprises by government subsidies. Comparing the research results of this paper with the old studies, we can find the market for acquiring external resources owned by Chinese companies is relatively imperfect; in some extent, government subsidies can alleviate the current lack of resources. This is also consistent with one of the conclusions drawn in this paper. Government subsidies can promote enterprise innovation. However, government subsidies cannot be completely innovated, which has a certain relationship with the company’s own redundant resources. Previous studies, especially domestic researches, have neglected the impact of redundant resources on enterprise innovation. This paper proves that the absorbed slacks play a positive role in regulating the relationship between government subsidies and enterprise innovation through empirical research.

When the company’s absorbed slacks are abundant, the innovation cost of enterprises is relatively low, and government subsidies can flow to innovation more easily. On the contrary, the effect of government subsidies on enterprise innovation will be weakened to some extent.

The conclusions can help the government to throw in innovation subsidies effectively. In the case of selecting enterprises, government prefers those enterprises with redundant absorbed slack, which can convert government subsidies into innovative and effective resources faster and better. The conclusion provides theoretical guidance for government departments to select and subsidize innovative subsidized enterprises in different situations.

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