

Abstract

Chinese economic policy makers over the last twenty years have deliberately used the attraction of Foreign Direct Investment (FDI) into concentrated geographical locations, now known as Economic and Technological Development Zones (ETDZs), as a major element in economic development. This paper examines two industrial parks around Suzhou, near Shanghai, particularly in terms of the role of the ETDZs in assisting FDI, as well as how FDI is affecting economic development.

Keywords: China, Economic Development, Industrial Parks, FDI, core-periphery

Introduction

China now accounts for 1/3rd of all FDI in emerging markets and nearly 80% of that going to South-East Asia outside Japan. Tse et al, 1997, showed that by 1994 China was the location for around half of all FDI. Further, this FDI is estimated to account for 1/3rd of China's industrial output, 10% of its urban employment, 25% of its GDP growth and half of its exports (Walsh, 2002).

Figure 1 China



Generally FDI in China has been concentrated along the Eastern seaboard (Broadman and Sun, 1997; Wei et al, 1999) around Hong Kong, Shanghai, and Beijing. Zhao and Tong (2000) argued that the initial focus of development of coastal China (in which FDI attraction played a major part) was based on theories where concentrated effects would eventually spread out to the whole economy. They argue, however, that this has not occurred, necessitating a rethink of the policy, and increasing focus on spreading economic development to the rest of China. There are, indeed, now increasing moves by the Chinese government to utilise FDI in pushing

economic development inland, to the West (Lafitte, 2001; Towson et al, 2002). However, there continues to be a focus on utilising spatially concentrated areas in which to locate the FDI itself. Chinese policy makers in Deng Xiaoping's post-revolutionary era initially identified Special Economic Zones (SEZ) (4) and Open Cities (14) as the preferred destinations to which Foreign Direct Investment (FDI) in the Peoples's Republic of China (PRC) was to be directed. This policy was intended to attract foreign firms to China, generating foreign currency earnings, regional employment and infrastructure development and economic growth (Sun and Parikh, 2001). Now the SEZ has been replaced by the industrial park or Economic and Technological Development Zone (ETDZ) and has sought foreign help in establishing such locations (see Perry and Yeoh, 2000).

However described, these locations for FDI are viewed as a powerful tool of social and regional, as well as economic, development, and the large foreign firms which occupy them are increasingly being utilised to accelerate the effective implementation of these policies. FDI, and its beneficial effects, are therefore being targeted as an engine to drive regional (as well as national) economic competitiveness, growth and development.

A number of issues are, therefore, explored in this paper. The theoretical role of FDI in promoting economic development and competitiveness is outlined, as are the ideas behind concentrating economic development policy. China's history with respect to economic development is then briefly analysed. The examples, Suzhou Industrial Park and Suzhou New District, (located around Suzhou, near Shanghai, in Jiangsu Province in the Lower Yangtze Delta) are then examined to explore the issues. Ramifications from these case studies on general policy are discussed and a research agenda is established.

The Theoretical Role Of FDI In Economic Development

FDI is targeted as part of economic development policy (particularly in high unemployment regions) because of the potential benefits, both direct and indirect, that these firms can bring to the economy, in terms of many of the factors mentioned above. Whether such FDI actually generates overall negative or positive effects on the host economy, however, depends on the strategy of the particular company undertaking the investment, as well as the development state of the country it is locating within, the strategy of its government with respect to FDI and indigenous firm development, and the power-relations between company and government. Hood and Young, 1984, summarised the potential effects under the headings of employment, competition, R&D dependence and truncation, trade, and resource transfer (concerning the transfer of capital, technology, management and production techniques from incoming multinationals into the wider host economy).

The geographical location and concentration of such FDI, and its activities relative to those of the local and surrounding area are also important. Hughes and Holland, 1994, argue that many of the questions regarding economic development should be viewed within a core-periphery framework. (see

Christaller's, 1966, central place theory, Williamson's, 1965, inverted U hypothesis, Myrdal's, 1957, cumulative causation theory; Hirschmann's, 1958, trickle-down theory; and Friedmann's, 1966, core-periphery ideas). Zhao and Tong, 2000, believe that Chinese policy makers appear to have been strongly influenced by these theoretical ideas that promote initial spatial concentration of economic development policy, assuming that in the long-term the benefits will eventually spread out from these "cores" to the peripheries around them, evening up economic and social development. Zhao and Tong, 2000, argue, however, that this is flawed for a number of reasons :-

- Empirically this is not an automatic outcome, being seen in the cases of the USA, Japan and Korea, but not in the UK, northern Europe, Indonesia or South America
- The centre-down paradigm assumes resource allocation and enterprise location will move from the centre-down when this does not happen in practice
- The paradigm assumes disparities in income will be removed by the market, when this is not necessarily the case in reality
- Regional economic development theory in the West has therefore moved beyond such theory

Zhao and Tong, 2000, support this with empirical evidence that shows widening disparities between urban and rural households and between provinces and regions in China over the period 1985-1995. There are, however, also a number of reasons to treat this with some caution. First, the evidence does not preclude long-run outcomes of the type desired by China (Japan and Korea in particular providing comfort). Second, China's government is in a different position to many in the West. Very different government – business power relationships are likely to exist, with China having much greater power relative to Western governments when dealing with foreign multinationals. This is due to their desperation to locate in China to take advantage of the low cost production and access to a huge market. The Chinese system also gives the government much greater control over indigenous firms, to direct where they establish, what they produce and the prices they set. Potentially, this gives China a greater ability to generate the type of centre-down effects it is seeking. Linked to this, business in China may be undertaken in ways different to the West. Perry and Yeoh (2000) highlight the Asian political management style of interpersonal relationships, networks and consensus, which is very different to Western management styles and thus may generate very different results. For these reasons we need to explore further the efficacy of China's policy within the Chinese context, and thus we need first to outline the recent history of economic development policy in China.

Recent History Of Economic Development In China

Central to the Chinese trading system is the concept of China being naturally divided into nine physiographic macro-regions, each with a major metropolitan core, and separated from the others by natural geographic boundaries.

SKINNER, 1997, argues that these macro-regions can be thought of as 'natural' vessels for territorially based socio-economic systems. At the end of the imperial era each of these nine physiographic regions supported a socio-economic system whose spatial structure was articulated by an interrelated cluster of Chinese-style cities (Skinner, 1977).

This physiographic regional structure was then overlaid with the 'open door' policy which affected the Chinese economy during the 1980s and 1990s. In 1978 Deng Xiaoping announced that China was opening to the world and that foreign investment was welcome. However, the Chinese saw a need to ensure that they controlled both the location and type of the initial inflows. Four Special Economic Zones (SEZs) were created along China's eastern seaboard, with Shenzhen, just north of Hong Kong, in the Pearl River delta being the highest profile. It absorbed nearly 60% of all foreign investment, created 5 million new jobs, accounted for one-sixth of China's exports and experienced growth rates that exceed the best years in Taiwan and South Korea (De Keijer, 1992). Fourteen coastal cities were also authorised as foreign investment destinations. Nearly all inputs, apart from land and labour were sourced from outside China, the main benefits to China being the amount of foreign capital generated, the upsurge in non-rural employment and the construction of infrastructure such as roads, ports and airports. These early SEZs were literally fenced off from the broader Chinese environment and economy. They were controlled by the Central Government, who, initially having no organisation to control these zones, rehabilitated a group of former capitalists as the China International Trust and Investment Corporation (CITIC). Any foreign enterprise wishing to invest in China had to deal with this organisation.

The original SEZ model has now been developed to ETDZs (the 'parks' in our case study being examples) to attract more sophisticated industries to China as it has sought to continue its rapid modernisation.

Table 1 : China's FDI and Trade since 1979

Year	Direct Foreign Investment in \$US 100 Million	Total Value of Imports and Exports by \$US 100 Million		Exports as % of GDP	Exports as % of World Exports	Foreign-Enterprises \$US 100	Funded ses million
		Exports	Imports				
1979		136.6	156.7				
1980		181.2	200.2	6.0	0.9	0.08	0.34
1981		220.1	220.2	7.6	1.1	0.32	1.11
1982		223.2	192.9	7.8	1.2	0.53	2.76
1983	11.66	222.3	213.9	7.4	1.2	3.30	2.88
1984	6.36	261.4	274.1	8.1	1.4	0.69	3.99
1985	12.58	273.5	422.5	9.0	1.4	2.97	20.64
1986	16.61	309.4	429.1	10.6	1.5	5.82	24.30
1987	18.74	394.4	432.1	12.3	1.6	12.08	31.22
1988	23.14	475.2	552.7	11.8	1.7	24.56	57.47
1989	31.94	525.4	591.4	11.6	1.7	49.13	87.9617
1990	33.92	620.9	533.5	16.1	1.8	78.1379	123.06
1991	34.87	718.4	637.9	17.7	2	120.47	169.07

1992	43.66	849.4	805.9	18.5	2.3	173.56	263.71
1993	110.07	917.4	1039.6	15.3	2.5	252.37	418.33
1994	275.15	1210.1	1156.1	22.3	2.9	347.13	529.34
1995	337.67	1487.8	1320.8	21.3	3	468.76	629.43
1996	375.21	1510.5	1388.3	18.5	2.9	615.06	756.04
1997	417.25	1827.9	1423.7	20.7	3.3	749.00	777.21
1998	452.57	1838.1	1402.4	19.5	3.4	809.62	767.17
1999	454.63						

Source: Derived from China Foreign Economic Statistical Yearbook 1999

Table 1 illustrates the rapid recent growth in FDI activity in China, as well as its importance to China's trade position. However, it is only very recently that FDI began making a positive contribution to China's trade balance (i.e. exports from FDI exceeding imports). Tse et al, 1997, point out that in 1994 China became the World's second largest recipient of FDI. Its initial experience lead it to focus on creating a stable investment environment for investors, including law and tax changes to accommodate investment needs. This growth, predominantly along the seaboard, had, however, developed to the stage where it was causing tensions in Central and Western China (income disparities, regional depopulation etc.). FDI and economic development were, therefore, now encouraged in Central and Western China, building on the success of the 3 major coastal regions around Hong Kong, Shanghai and Beijing. Lafitte, 2001, however sees this push westward as likely to produce "islands" of intensive development in the ETDZs linked to transport corridors back to central and coastal China.

Nevertheless, these new locations for FDI are viewed as a powerful tool of social and regional, as well as economic, development and the large foreign firms who occupy them are increasingly being utilised to accelerate the effective implementation of these policies. They can also be seen as developing not only from Western economic theory but also from China's own economic history, based on core-cities and peripheral regions.

China has thus put much faith in the power of FDI and the ETDZs as a tool for economic development. However, there are also potential dangers of policies that become over-reliant on spatially concentrated FDI. Further, such dangers may be compounded if the role of indigenous firm development and entrepreneurship is not also developed. The 'open door' policy encouraged many foreign companies to seek joint venture relationships with State Owned Enterprises that attracted interaction between foreign and local Chinese companies because of the potentially lucrative outcome of selling to a market of over 1 billion customers. As the government decentralised control it also sought to develop a new generation of internationally minded managers who could deal with the increase in foreign trade. This combination of more highly educated people and the opportunity of foreigners bringing business to China gave rise to an emerging entrepreneurial Chinese business sector, consisting of both in-enterprise and private business entrepreneurs.

Devolvement of business from State Owned Enterprise to privately owned and self employed business people has made provision for entrepreneurial activity to take place (Dacosta and Carroll, 2001; Fan et al, 1996). Although

entrepreneurial activity has increased, and its contribution to economic growth has been substantial, however, Zapalska and Edwards, 2001, also found substantial barriers to development and growth that needed to be dealt with, including labour markets, administration, low consumer demand, education and high cost factors.

It is therefore important to examine the policies of these Industrial parks and the FDI within them, and the links, or lack of them, with indigenous firm development (in some ways an examination of the FDI “core” with the indigenous periphery). This is undertaken through case studies of two ETDZs, undertaken during two visits to the Shanghai macro region of China during June-August 2003. A number of interviews with multinationals, local administrators and politicians were conducted and analysed to produce an initial view of the situation as it currently exists, and from which a longer term research agenda can be established.

The Case Study ETDZs

Suzhou is approximately one hour from Shanghai and now has a population of six million people. In this same region the logistical corridors linking Shanghai with Nanjing, Suzhou, Hangzhou and Ningbo have all undergone major development over the past 5 years and the region is now recognized as one of the major hubs of development for China during the next five years (2003 – 2007 incl.). Some of the 70 major projects commissioned in Suzhou at present include linking the two major economic districts (parks) of Suzhou New District (SND) and Suzhou Industrial Park (SIP) and eventually Shanghai and Suzhou by fast train, road works to link SND township enterprises and the SND, and development of the east region of SIP, to include an area of heritage and tourism as well as industrial development (e.g. water villages, theme parks and resorts).

The establishment of the industrial parks in Suzhou owes much to the Singapore experience (see Perry and Yeoh, 2000, for further details). A state level agreement was signed and the principal development agency of the Singaporean government, the Jurong Township Corporation (JTC), was appointed to manage the establishment process for what was initially called the Singapore Industrial Park (SIP). Located between Shanghai and Suzhou, to the northwest of Shanghai, it became a flagship project for the new generation of investment zones. The initial investment and control was 65% Singapore and 35% Chinese and the park was managed by a specially set-up authority. It had its own customs house and was notable for its superior infrastructure and strict environmental controls. However, much to the chagrin of the Singaporeans and the embarrassment of the Chinese, the local Suzhou municipality, seeing the success of the SIP, but having no share in the wealth being generated, instigated their own technological zone at the other end of the city in competition to the SIP. The Suzhou New District (SND) was thus built by the local municipality. The land was superior to that of the SIP and was located right beside the city centre of Suzhou, whereas the SIP was more remote. Despite fierce initial rivalry, both parks are now successfully

established and are attracting substantial FDI. Control of the SIP has now moved the Chinese to a 65%-35% split with Singapore.

Whilst, Jiangsu Province has a number of development zones, the Suzhou New District (SND) and the Suzhou Industrial Park (SIP) are the major economic development zones in this region. Geographically the two parks extend from the boundary of Shanghai to Wuxi (approximately a 100 kilometre radius), and thus have a wide ability to generate economic effects from FDI. These 'parks' have specific regulations that vary within each area. SND provides incentives for housing local SND workers and SIP has a waste management plan. Therefore, 'special' rules apply in this 'park'. These variations from the regulations are designed to allow easier entry to the China market and provide a competitive edge in attracting FDI from specific industries that will compliment the park. For example the Suzhou New District has a 'Technology Township' within the park that is designed to provide research and development and component manufacture that then supplies the larger assembly plants in the 'park'. Therefore a distinct logistical chain operates from Wuxi to Shanghai where the supply of components is manufactured in Wuxi, assembled in Suzhou and the sales and marketing offices are situated in Shanghai.

SND was first established in 1992, and considers itself a 'high-tech park' with a science and technology theme. This park also boasts a 'garden like' atmosphere where the surroundings are 'liveable'. The infrastructure in SND has been developed through establishing a banking sector and medium rise expatriate living area. The 'park' is home to companies such as Phillips, BenQ, Acer and Fujitsu. The growth of this 'park' over the past six months has been through the development of infrastructure services. SND has now established a theme park and is now investing in the development of recruitment, employment and training industries. SIP has the infrastructure of its own water plant, sewage and gas and ISDN telecommunications availability. The 'park' has a preferential tax policy that offers foreign investment companies with a term operation of 10 or more years the following:

- Enterprise Income Tax - 15%
- Tax Holidays - First two profit making years exempt 50%
- Export-oriented enterprises - 10% enterprise income tax after tax holidays
- Technologically advanced enterprises of a 10% enterprise income tax for an additional three years after the tax holiday.

Foreign invested enterprises in the SIP are also exempt from customs duty and import-related VAT for the equipment imported within its approved total investment and which is for the enterprises own use. The 'park' hosts multinational companies including; Lion Nathan, L'Oreal, Motorola, Nokia, Emerson and Copeland and Bosch. SIP has grown considerably over the past six months. The local schools (private and state owned) are operating at capacity and multi national joint venture companies in telecommunications

manufacturing have shown 100% growth in the past year. The price of housing in SIP has also doubled in the past three years.

While both 'parks' boast about the access to Shanghai, the airport, the port and the highway, there are considerable difference in the operation of the two development zones. SND's committee has access to the old city of Suzhou infrastructure. The first difference, therefore, is the international versus local culture that prevails in SND versus SIP. SIP has a distinctly more international flavour with a 'Singapore Square', and a tax policy favouring foreign investment.

Secondly, while both 'parks' are willing to entertain entry from all countries, a majority of joint ventures companies in SND are from Taiwan or Japan. In the SIP, while enterprises from the same two countries dominate, many other international corporations from the UK, USA, Canada and Germany are also present. Evidence from interviews with enterprise principals indicates the administrative authorities and regulations in SIP are more favorable towards more western operations. Aligned with this is the distinct advantage of SIP to provide customs clearance and administration for immigration.

The rapid expansion in these 'parks' has also had its drawbacks. Infrastructure, in the service industry, like restaurants, medical services, employment services and logistics, are often not able to meet the needs of the employees and owners of the companies. For example, it is often a fifteen minute wait for a taxi from any of these enterprises. Therefore access to the companies for meetings is prohibitive if time constraints exist (although, as will be seen later, this has produced an opportunity for local entrepreneurs).

Interviews with managers of foreign enterprises indicated that the park management had facilitated their entry by making it easier for them to obtain the necessary permits and licences required for registration as a foreign enterprise in the PRC. The SIP and SND both promote their ability to act as a 'one stop shop' for foreign enterprises. When faced with the myriad requirements and bureaucratic delays of obtaining this registration, the facility offered by both parks acted as a strong inducement for foreign enterprises to locate within them.

In the case of the SIP this facilitation extends to provision of the park's own customs house. Several US companies indicated that being able to bypass lengthy delays at the busy entry points of the Shanghai International Airport and International Shipping port saved them at least three working days per shipment. The SND is unable to offer a similar facility but is now negotiating for its resident firms to be able to use the same facility.

The park administration also conducts major recruitment fairs on behalf of its occupants. Such is the attraction of the parks that the Spring Recruitment fair in February this year attracted over 88,000 graduates from all over China. As part of the process the HRM departments of the park administration check qualifications and references, provide additional training and promote the employment prospects of the various enterprises. Three managers admitted

that having the park administration carry out these functions on their behalf made the recruitment process far less time-consuming than if they had to do it themselves.

The most noticeable impact of the two parks on the Chinese firms within the region (and hence indigenous entrepreneurial activity) has been to quickly assimilate them into the multinationals' supply chains. Most international firms commenced operations in the parks using their own established supply chains. This was for various reasons including reliability of supply, quality assurance and long-term relationships. However, many of these enterprises are now changing their supply chains to include local producers. There has been a proactive approach by the various levels of government to localise the supply chains. They use the hegemonic power of the foreign firms to force their suppliers to locate either within the industrial parks or along the designated supply chain corridor (the Nanjing-Ningbo expressway). In some cases international suppliers have been unable or unwilling to relocate so their places have been taken by local firms.

These township enterprises have also quickly commenced producing the components required by these international firms. Because of the large geographic area of the industrial parks many small townships are located within them. These township enterprises are assisted by the park administration, county and Provincial authorities to access the initial start-up capital and to access intermediaries in the supply chain who have the necessary quality assurance credentials to satisfy the requirements of the foreign enterprises.

For example, BenQ, a large Taiwanese computer manufacturer, located in the SND, commenced production less than two years ago with a supply chain based entirely on supply from Taiwan. Now, apart from some proprietary technology, their supply chain is based around a series of suppliers in township industries within the SND. Glaxo Smith Kline Beecham has also changed their supply chain from its traditional suppliers to a localised one, again with the exception of proprietary technology. Interestingly, Glaxo is located in the SIP but most of their suppliers are township enterprises in the SND. A series of interviews with 12 enterprises located within the SIP indicated that about 60% of their supplies were now being provided by local suppliers. Of this 60%, about 80% was originally supplied from traditional supply chains outside of China. Eight firms within the SND were interviewed and the results were similar. Management at the SIP and SND were most insistent that this process would increase and accelerate as more firms achieved the necessary ISO accreditation. While the interviews were being conducted the park management was promoting the next round of ISO accreditation courses to the various suppliers and industries in the SND.

This concentration of economic development within the park has also clearly had impacts on entrepreneurial activity within the region. Some of this is at a relatively low level, particularly for the Small Township Enterprises located within the parks, and does not seem connected specifically with the presence of FDI. However, as outlined previously, there are larger, medium town

enterprises that are more directly linked with the FDI occurring within the parks through the developing supply chains.

Generally, the interaction between foreign owned and local enterprises follows a pattern in developing entrepreneurial activities within these parks. The foreign owned enterprise requires a locally supplied service. It either has to vertically integrate or find another independent local supplier. The traditional way was to contract either an international or state-owned enterprise to provide the necessary service. This posed a dilemma as the State owned enterprises tended to be cumbersome and inefficient while international service providers, while efficient, were costly. Locally-based expatriates have identified the service sector as providing opportunities and currently dominate most sectors, particularly training and logistics. However, fast moving local entrepreneurs are also getting involved. Some level of training is required, but the Chinese tradition of copying the 'shifu' (master) provide training by default, as local entrepreneurs learn from, and copy, the activities of logistics companies such as DHL and FedEx, even to the extent of duplicating their livery and assuming deceptively similar names. However, so fast is the local learning curve that local service providers are able to quickly displace international providers based not only on price, but also on efficiency and knowledge.

An example of this is the logistics system successfully employed by Lion Nathan to distribute beer to the local bars and retail outlets in Suzhou and surrounding townships. The beer is transported by locally owned truck to a local holding warehouse from where it is delivered to the local bars and outlets by bicycle. As most of these premises have little room for product storage, deliveries may be required in small amounts, several times in the same day or evening. This process is managed by a local entrepreneur who oversees the warehouse and draws on a fleet of local bicycles to carry out the deliveries. As a result of this innovative approach all network participants get a share of the revenue from Lion Nathan and Lion Nathan is able to satisfy its clientele. For Lion Nathan to adopt such a basic, but effective, supply chain management approach has required a major paradigm shift but the adoption of this approach has contributed to the turn around in Lion Nathan's fortunes in China. In contrast, Fosters persisted with the traditional beer delivery methods utilized in more developed markets and now have taken themselves out of the market.

Conclusions

The two industrial parks forming this case study seem to be having a significant impact on the economic activity of the region and this seems to be a deliberate policy to focus supply chains within the large ETDZs that these parks represent. In many ways, however, they may still be seen as 'islands' of international enterprises and activity, within a 'stream' of communism, especially as one of their features is the almost total absence of local Chinese firms at the top of the supply chains within the parks. The sheer magnitude of these parks, however, in terms of enterprise population, number of employees and residents, means that they are major growth engines for the region as a whole. The attraction of the foreign firms as consumers of locally produced componentry is driving the local firms, administrators, and politicians, to seek better quality control credentials, and as they achieve these, they in turn are able to move further up the supply chain. In addition, indirect service industries are springing up to service the needs of the foreign firms and their employees, promoting large local expenditure multipliers and providing conduits for information transfer that may be assisting in the promotion of local entrepreneurship.

The political power and control that is possible for government and the authorities within these parks is obviously very important to their development and to the behaviour of FDI in developing local supply chains, in ways that may not be possible in other parts of the world. This superficial analysis does seem to suggest that these zones are indeed being utilised to increase the benefits to be derived from inward investment.

More detailed research, however, is clearly required in order to determine the long-term effects of these strategies. For example, in-depth case studies of individual inward investors, their strategies and the processes underlying them may reveal a wider range of factors of importance to the international businesses located within these parks. This may also aid in a more precise mapping of the supply chains for foreign firms (via case studies or survey) which would allow a more in-depth insight into the true nature of the supply chain relationships and the extent to which FDI is truly embedded in the region. Such surveys, if accompanied by data concerning the spending decisions of these firms on the other factors of production (e.g. wages), and destination of output (Chinese and export markets) would also allow some quantification of effects (such as through input-output analysis) and the direct and indirect multipliers to be calculated.

Evaluation of the comparative success of the two parks in promoting economic development, given their different foci and policies is also important in determining future policy directions for these types of parks within China. Finally, further analysis of how the industrial park model fits within the overall economic strategy of pushing economic development westward is also required, not least to explore the potential future pressures on FDI and its production and location strategies from Chinese policymakers.

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