

## Wenzhou and the Third Italy: Entrepreneurial Model Regions

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Walcott, S. (2007) "Wenzhou and the Third Italy: Entrepreneurial Model Regions. *Journal of Asia-Pacific Business* 8(3):23-35.

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### **Abstract:**

Physically semi-isolated between the two economically booming deltas of Shanghai and Guangzhou, Wenzhou provides the premier example of successfully autonomous, bottom-up entrepreneurial development in contemporary China. Along with a prosperous urban area, rural farm cooperatives are developing a new model of financing that integrates the three previous periods of economic experimentation. This research outlines the Wenzhou Model, discusses similarities with the Third Italy Model, and notes development possibilities for other Chinese metropolitan regions. Keys to success lie in local trust-based social networks, a focus on niche sectors, market sensitive export orientation, and investments utilizing endogenous capital.

**Keywords:** China, development model, Third Italy, entrepreneurial

### **Article:**

#### ***ENTREPRENEURIAL REGIONS***

Long neglected for development attention by China's central government owing to its perceived hazardous location across the straits from Taiwan, Wenzhou municipality in central Zhejiang Province nevertheless thrived on its own and now serves as one of the principal success models held up for emulation. Coastal areas such as Wenzhou distinguished themselves from interior areas within the same province due to their dynamic capitalization of inherent organizational advantages (Ye and Wei 2005). Operating under the radar of the rigid central command economy, Wenzhou achieved recognition for its prosperity linked to a close-knit familial and village-based local network. Profitable real estate developments springing up in major towns throughout post-reform China testify to the pent-up investment capital and savvy of the "Wenzhou people," whose previous renown as far-flung salesmen hawking household products familiarized them with the national market. This research explores the roots of Wenzhou's success, considers whether it provides a replicable model in the economically freer atmosphere of contemporary China, and compares the strategies at work with some striking similarities apparent in the better-known "Third Italy" region of Emilia-Romagna.

Several different Chinese development models in east coast leading regions show variations on successful transition to what is currently termed "market socialism." The Sunan Model, centered in southern Jiangsu Province, stemmed from collectively owned and managed township and village enterprises. The Gengche Model from northern Jiangsu exemplified a village-based cooperative network. Beijing's Zhongguan' cun Model utilized knowledge spillovers from top national universities to form a cluster of high technology companies in the northwestern part of that city. The Pearl River Delta Model from Guangdong Province led to many small and medium-sized enterprises profiting from capital sent by overseas Chinese with native roots, as well as infusions from investors in nearby Hong Kong. In the Yangtze River Delta Model (Shanghai, Suzhou, and Hangzhou) large firms flourished from foreign direct investment and government connections. The Wenzhou Model's basis lies in small and medium size enterprises utilizing local household finance and efforts to support a locale-based group effort based on specialized family enterprises which strategically formed an integrated production unit (Rong 2004). The Wenzhou Model's basis lies in small and medium-sized enterprises utilizing local household finance and efforts to support a locale-based group effort. In one example, local ties and commitment remained so strong that upon their return successful emigrants taught other villagers what they

learned about businesses while absent. This process boosted economic multiples in a learning network leading to new types of industries and techniques. With the exception of the export-directed Deltas, the other model economies cater primarily to the Chinese market. Wenzhou's distinctiveness lies in how it achieved its current status despite—or perhaps owing to benign neglect by—official policy prior to the 1990s. As presented in Table 1, Wenzhou's concentration in manufacturing is higher than either the province or Ningbo, a similar sized successful neighbor. Wenzhou's GDP increase is comparable with provincial levels, but less than latecomer Ningbo's which is currently in a takeoff stage. Wenzhou's organization remains the most interesting element in its early success.

TABLE 1. Statistical Comparison, 2004

Unit	Population (10,000)	% Primary	% Secondary	% Tertiary	%'03-'04 GDP increase
Zhejiang	1,428	0.54	51.78	47.7	NA
Ningbo	210.45	0.14	52.86	47.0	17.50
Wenzhou	137.14	0.03	62.77	37.2	14.10

\*Year 2000

Source: All China Data Center, China City Statistics, China Marketing Research Co.

This research examines whether patterns in Wenzhou can be usefully compared with patterns of family firms prevalent in Third Italy, a region more frequently researched and observed in the West (Yanagisako, 2002). Contributions of this examination include an analysis of limits to locale-based trust networks that launch then limit economic expansion, the next stage of manufacturing globalization in Wenzhou, the ongoing third stage reform of rural finance and governance outside the Chinese city and the suggestion of increasing convergence as similar models seek to mediate their limitations. Wenzhou municipality in coastal Zhejiang Province serves as China's outstanding example of successful economic entrepreneurial practices financed by household level initiatives toward "marketization" since very early in the reform era. The prefecture-level city comprises 11,784 sqkm, with an urban population in 2005 of 1.37 million set in a metropolitan area of 7.46 million. Approximately one-sixth of Wenzhou's population is urban, and two-thirds of the urban population is nonagricultural—a fairly high number for contemporary Chinese metropolitan areas of this size (Information Office, 2005). The "Third Italy" region, also referred to as Emilia-Romagna, forms a northeastern group of counties that propelled themselves to a position of prosperity between the relatively wealthy northwestern triangle of Italy and the relatively impoverished Mezzogiorno region south of Rome. The following sections first examine the historical background, urban economic pattern, and rural examples from Wenzhou. The next section offers a comparative analysis with the Third Italy situation better known in the West. The conclusion summarizes these two models and future trends. An underlying aim of this article is to indicate the usefulness of a cross-cultural comparison noting strong similarities in development scenarios, divergences, and which are most important.

## WENZHOU

### *Historical Background*

Wenzhou traditionally served as the major port of southeastern Zhejiang Province. Topographically surrounded by highlands composed of a mixture of volcanic, sedimentary, and granite composition, the water bodies draining toward its port outlet provide the city with a marshy setting of many small islands. Due, in part, to this geographic isolation, the native dialect remains distinctive and the inhabitants possess a strong sense of their bonded uniqueness. Noting that the city's history stretches back to 1,700 BC, various scholars (Liu, 1992; Tsai, 2006) saw roots of Wenzhou's clannish distinctiveness in its past (an intriguing point dismissed by a local scholar as too distant: "Outsiders can never understand what insiders know"). A second century BC failed rebellion against the Han led to wholesale removal of the population to Anhui and importation of literati from the northeast. By the tenth century AD Wenzhou was a center of handicrafts and scholarship, known for its pottery, celadon porcelain, silk, tea, embroidery, and leather output. Its products and people circulated throughout China and overseas. A Wenzhou merchant's "hall" (*tang*) from the 1600s, an early form of Chamber of Commerce branches that served as meeting and temporary hospitality sites, still stands in modern Tianjin. Over 100 branch associations from Wenzhou currently operate throughout China.

A local rebellion led to self-liberation shortly before the arrival of outside communist forces in 1949, demonstrating the solidarity and self-reliance of this independent enclave. Some observers point out that native

and outside cadres intermingled, diluting the Wenzhou personality effect. These scholars argue that economic circumstances reinforced the earlier pattern of self-reliance in the face of lack of funds from the central government. Owing to Wenzhou's Zhejiang Province location close to the Taiwan Strait, central government investment skipped this locale deemed too militarily risky and went instead to "Third Line" sites such as inland Xi'an and Sichuan cities. Natives were thrown back on their own resources to invest in ventures that challenged their creativity outside of what became a cumbersome and restrictive state-owned enterprise system. Accumulation of capital, under the communist regime, stemmed from intermittent pre-Cultural Revolution agricultural policies permitting retention of some profits from household workshops (Whiting, 2001). Tight-knit social networks preserved local autonomy, as in the money-raising family networks known as *gao li dai* or the *meng*, composed of six or more men. Collateral for loans could consist of one's house. The weakness of the post-1949 industrial sector became the strength of the post-1979 household-based commodity sector model of "development from below."

Natives were generally too poor to invest in collective enterprises in the 1980s, so cadres encouraged investment that protected private property to pull capital into circulation (Whiting, 2001). During this same decade Wenzhou natives revived their historic pattern of selling products door-to-door across the country. Their work on widespread construction sites as part of a Wenzhou team of workers stood in good stead for capital accumulation and later investment in real estate nationwide, a readily recognized hallmark of Wenzhou economic activity. Crucial by-products of this widespread entrepreneurial activity included remittances to fuel growth in the hometown and, even more importantly, knowledge of national markets and supplier connections. The widespread extent of Wenzhou natives traveling outside their city, while maintaining economic and social links that fueled knowledge and capital transfer, demonstrated a cultural characteristic with financial payoffs (Shi 2004). Illegal links with the prosperous Taiwan market boomed in the 1980s via fishermen and an "electronics for antiques" swap across the Strait (Whiting, 2001). Currently 129 Wenzhou Chambers of Commerce can be found throughout China, demonstrating both the breadth of the market covered by traveling natives and their place-based (*diyuan*) nature. The former so-called Zhejiang Town, a cluster of largely Wenzhou natives in Beijing, was so close-knit as to pose what capitol city police saw as a threat to their control. The settlement was forcibly disrupted and dispersed.

Building on its history and making the most of its local financing base, the city became known for its "big market with small commodities" (Information Office, 2005). Products now range from auto parts to zippers, with a total in 2004 of US\$ 4 billion in industrial output and US\$1.4 billion in agriculture. Typical Wenzhou products include inexpensive consumer and household items such as plastic shoes, purses, kitchenware, and glasses, which it markets throughout the surrounding region. Wenzhou functions as the economic, cultural, and transportation center of southeast Zhejiang Province, strategically located between the coastal powerhouses of the Yangtze (Shanghai) and Zhujiang (Guangdong, Hong Kong) deltas. Future plans envision connecting Wenzhou more tightly to export markets for its manufactured goods by creating an industrial complex zone with enhanced transportation access for business and tourism, breaking the geographic bottleneck of surrounding mountains and previous development neglect.

Starting in 2005, the introduction of outside investment formed a top project of Wenzhou's government. The specialized market-sensitive town-based production defied a Weberian place separation between the stages of economic development from agriculture to commercial and industrial pursuits. Instead of industrialization pushing production out of the home to a distant factory, manufacturing and residency remained rooted in the same locality from which it drew defining characteristics. Town-based transition utilized a pro-growth coalition of business and political cadres. A Wenzhou contributor said that the degree of political-economic cooperation depended on who was the party secretary, which changed frequently. Local observers agreed that Wenzhou was influenced more by informal customs and traditions and followed a persuasive rather than coerced transformation.

Wenzhou remained a town with two-three story structures and many bicyclists until the turn of the twenty-first century. The new government center now dominates a large green plaza as a multiwindowed glass square. Skyscrapers and expensive residential buildings punctuate a new CBD skyline. Ambitious future plans for the

prosperous city include multiple port complexes, new bridges (and/or tunnels) and railroad facilities, an island entertainment complex, and a hospital complex in the swampy side of town by 2020. The very public nature of the urban exhibit indicates the transparency of planning in this progressive city. It contrasts with the secrecy of other municipalities' land use change plans, which increase the possibility of unhealthy influences on planning processes and outcomes. The government's "Sunshine Plan," detailed on a wall of newspaper reports, explains the policy of transparency in planning "so there will be no dark or corrupt areas in Wenzhou's future." A dedicated section invited public comments and suggestions, building on the participatory character binding the Wenzhou people.

### *Manufacturing Model*

Ruili Auto Parts Factory, recently listed on the NASDAQ stock exchange, anticipates its debut with an IPO (initial public stock offering) in August or September of 2006. The SORL Auto Parts Factory, makers of auto air brake components and part of the Ruili Group industrial conglomerate, constitute the second largest company in Rui'an. Typical of Wenzhou, the two top officers are brothers from a farming family who founded their NASDAQ listed company in 1987. This type of industry was one of the "3 Pillars" of Deng Xiaoping's Opening and Reform movement in the early 1980s. However, since auto parts were not covered in the central planning system, this provided a niche opening for entrepreneurs. The United States is now the largest export market. Rui'an supported machinery production since 1916, forming the basis for an automotive industry that now sports 1,300 factories in the area.

The local village of Tangjiang is entirely dedicated to producing various products used in the auto production chain—a typically localized and differentiated Wenzhou characteristic. Another example of grassroots cluster development came from two people in one village who started to make eyeglasses, and now the whole village is involved in the factory with each family specializing in one part of the production. A third example came from one person who invented a cotton-processing machine. Others learned from him and set up factories to utilize this invention. The beginnings of Rui'an's auto cluster reportedly came from either a retired autoworker who returned to Rui'an and started a business, or a sent-down youth (during the Cultural Revolution time) who began the first parts shop. The important factor in learning transfer leading to cluster development lies in a local culture supporting people who come willing to teach others, who are eager to learn. These knowledge bearers are emulated rather than envied, decreasing information and transaction cost and creating a multiplier effect rather than seeing wealth more typically as a zero-sum game. Females make up 55% of the workforce, working 6 days a week (management works five). A company newsletter promotes openness and morale. Workers come from various provinces (purportedly 2,000 Wenzhou natives leave annually, while 3,000 workers enter from outside) and cluster into native place associations (Anhui, Jiangsu, etc.) along with a trade union and women's association.

Government's role lies in "endorsing and aiding the peasants' efforts," taking pressure off from any attempt at picking winners, according to officials who felt that government should encourage the grafting of local and foreign businesses. This step was predicted to attract technology and capital, encourage innovation, promote locally famous brands, advanced management learning, create an "alliance of local entrepreneurs," and raise enterprises to the next highest level by the "emancipation of productivity." Because land is at a premium, municipal government currently gives priority to enterprises with high technology and tries to push polluters out or at least constrain their operation—though smoke belches across the skyline well into the countryside where farmers seek to craft an innovation in rural financing.

### *Building the "New Socialist Countryside"*

The vice mayor of Rui'an City, Chen Lin, graduated from Beijing's prestigious Tsinghua University with a specialization in rural finance reform. He demonstrated an energetic, innovative, and inclusive approach to trying to implement new ideas for reforming both urban and particularly rural financial structures, which were featured previously in the local press. Major figures in the Meiyu Vegetable Association represent a timeline of rural financial schemes: the vice president, a board member, and the secretary-general of the rural cooperative association, a representative of the ag-tech extension, the legal counsel, and Rui'an's vice mayor. Articles in the

local press previously detailed the innovative rural financing contributions initiated by Vice Mayor Chen Lin in the Wenzhou spirit of community knowledge-based cooperation. The “Three Styles in One” include a credit cooperation system (a type of microcredit/finance system for farmers), coordination between supply and demand (matching seeds to market), and cooperation among farmers who are investor-owners of the credit union and thus in a position to share information and resources with members.

The 59 rural cooperatives in Rui’an represent 452 members of the 2,277 households in the city. Tomatoes comprise the base product. Salespeople travel around Zhejiang and Shandong provinces to investigate the market, and 44 sales brokers cover 13 cities in various provinces. Half a million RMB (*renminbi*) profit comes from 7 million RMB in sales annually. Local university R&D seeks to produce better quality vegetables, following an Israeli model. Examples of locally adapted innovation include a new kind of automatic greenhouse and a pesticide alert program.

Local needs are for more top-down institutionalized information flow and greater bottom-up university and Best Practice Models based on local experts. Better seed research for value added, better market place connection, and fewer pesticides for a “greener” countryside were other goals. The Rural Cooperative Association (RCA) has identified “5 Needs” as goals of rural modernization. The first is to deepen reform of quasi-governmental associations leading to rural cooperatives. These constitute the largest economic organizations in the country, but cannot provide direct service to farmers. In 2003 rural ownership reform led to cooperative economic alliances that provide a limited amount of information, technical support, rural credit, and market access.

The next issue concerned rural banks based on a credit union form, consolidating the number of shareholders. Lack of brokerage made it difficult to regulate small shareholders, but a telling example of the Wenzhou way of doing business lay in the system of credit rating provided by local residents. They felt that they knew both the prospective lenders and their assets (e.g., house) best, so could internally evaluate creditworthiness. Fifty-nine rural cooperatives focus on different products for commercialization, but cooperatives do not share information and no direct access to information for scale economies. A Household Responsibility System plus village cooperative association provide farmer services since the early 1990s, but most are empty shells with no role. Finally, better connection is needed between government and farmers. In the past, government provided subsidies to direct the command economy. Now a lack of central agency is felt for helping to raise farmers’ income. Farmers express a desire for a “democratic system of equal and concentrated management.” A Board of Trustees, Inspectors, and Executive Committee provide checks and balances “like the U.S. Constitution” to fight over departmentalization, leading to a “comprehensive, multi-dimensional new socialist countryside.” The Bureau of Technical Service and Extension distributes information, while Legal Aid system provides defense, and educational institutions provide training and create a Web site. A supply and sales rural network features research projects and technicians work in villages.

Collective bargaining comes from the rural cooperatives and peasant associations, while individual peasants make the basic decisions of what to grow since high risk is involved. Credit union directors are all volunteers, but control a great deal of money. The vice mayor’s idea is to combine the credit union, and the cooperative service organizations to create a new organization that can deliver services across scales in a more unified and comprehensive way. The idea is that a workable market is like democracy: It needs informed participants. The following example from a vibrantly democratic European country underlines elements of locally generated economic success in a very different political setting, but based on a strikingly similar social assemblage.

### **THIRD ITALY MODEL COMPARISON**

Wedged between the prosperous industrial area around Milan and Genoa in the northwest and the lagging Mezzogiorno provinces south of Rome, Italy’s northeast-central region of Emilia-Romagna provides a widely studied regional prototype popularly referred to as the “Third Italy” (Cooke, 1996; Amin, 1999; Agnew et al., 2003). Similarities to the Wenzhou development model are summarized in Table 2. As in Wenzhou, local social ties created dynamic networks supporting collective learning. Family-based small and medium-sized enterprises spatially concentrate in specialized industrial districts. Trust-based relations reflecting social network ties

reduce transaction costs, increase knowledge transmission, and encourage political-economic cooperation for growth. Characterized as the “Second Industrial Divide” (Piore and Sabel, 1984), operating procedures in this area contrasted starkly with the mass manufacturing automobile industry production system familiar since Henry Ford that is at work in neighboring provinces.

TABLE 2. Comparison of Wenzhou and Third Italy Model

	Location	Network	Structure	Mobility	Market	Products	Innovate	Future
Third Italy	Isolated, lagging region	Extended family	Vertical, place specialized	Global	Global	Custom niche	Trust, multiply transfer	University tech transfer
Wenzhou	Same	Same	Same	National	National	Same	Same	Kean University branch

Localized production centers utilize export-oriented niche specializations to create place-based economies supporting local firms. Related residents supply both low labor costs and endogenously accumulated capital. Light industrial products include foods, clothing, shoes, furniture, and metal work for a craft-based market. Building on a textiles and leather goods specialization, that demands rapid responses to a notoriously fickle fashion market, familial and other locally forged trust-based ties enabled local star “Benetton” to become an international fashion retail chain. Knowledge of the local market was so finely tuned that offerings were famously differentiated even within the same city. Exports catering to wide markets—as in Wenzhou’s motto “small goods, big market”—provided the volume sustaining small batch runs. External economies of place propelled tightly organized local regions to maximize returns based on clearly defined sectoral specialization. In one example clearly defying physical topography, Silicon Valley imitators sprang up around the globe as hopeful high technology havens. A real estate set-aside does not an industrial district make, however. The distinction of both the Third Italy and Wenzhou lies in its entrepreneurial supportive social network, whether involved in craft, industrial, or agricultural products.

Current challenges for the Third Italy to sustain its predominance include raising the technology level of products and maintaining their distinctive local roots in the face of mergers and acquisitions, transformation from production to design as labor cost advantages diminish, or succumb to supra-local management (Cooke, 1996). The strength of this tightly bonded social network lies in its initial boost and self-sustaining cooperative nature. Limits flow from the same source. Rigid confinement to natives cuts off or alienates outside sources of talent and investment. Learning is hobbled if it must be “by, about and for us,” a realization leading some local leaders to look to outside sources of information such as research universities to fuel the next stage of regional growth.

## CONCLUSION

Varieties of capitalism occur and are shaped by preexisting practices in particular places. People produce economic activities and family relationships within historically evolved cultural frameworks that dynamically adjust through time. Innovation becomes possible with a willingness to attempt risky changes, and in both areas small firms took advantage of niche markets not occupied by large outside competitors, which in Wenzhou’s case meant pent-up demand not filled by cumbersome huge state-owned enterprises. The national-scale political economy and local family-community traditions combined with actions of leading individuals to shape practices at the family-firm-municipality-regional levels. Such post-Fordist practices of local trust-based networks enabling locally specialized production niches do not rule out but rather enhance the operation of mass manufacturing assemblages, epitomized in the Rui’ an Automotive Parts Factory operated by two brothers that successfully broke into the NASDAQ market listing.

The much-researched and discussed Wenzhou Model provides the earliest example of privately funded entrepreneurial economic activity “with Chinese characteristics,” and a continuing locale-identified economic success that is much remarked on by other Chinese. It is less unique in its parts as it is in its coherence. Isolation and self-reliance provided early strength and impetus for locally networked strategies, but may ultimately limit development by cutting off lessons offered by broader outside experiences. The type of space provided by higher authorities for local innovation, and the energetic outreach by businessmen to global markets while encompassing participation by local peasants and workers holds intriguing promise for a “bottom-up” general

model of increasingly self-directed freedom. Although Emilia-Romagna's exports cater to a global clientele while Wenzhou's national-scale market is more spatially constrained due to the time of its development, both famously look outward to sell products utilizing the inward foundation of a local industrial district.

Why model-defying breakthroughs occurred in these two regions, in the face of lagging circumstances in other areas, is probably a combination of timing, leadership, and proximity to successful elements such as migrants remitting capital and concepts. Isolation often makes identity bonds stronger, reinforcing the coherence of local policy—in these two cases to an unusual but ultimately successful extent. Major remaining challenges in both regions lie in improving product and worker quality, education, and infrastructure. The acknowledged need to increase quality and education was anticipated to be addressed by a US\$68 million campus of Kean University (NJ) being built in Wenzhou (McCormack, 2006), which would provide less expensive training than the current practice of sending administrators abroad. Several groups had gone to England as well as the United States for advanced coursework in management. One high-ranking political official remarked on her discomfort at being the only female in the group, which stayed a full 9 months in the UK. Overall, Wenzhou was moving with a deliberate strategy to build on earlier strengths while repositioning for the future.

In general, both Wenzhou and Emilia-Romagna constitute dynamic examples of economic democracy evolving as national heroes in an international spotlight. Ironically, the edge of expansion for global learning and local knowledge transfer finally meet in Manhattan, at the converging boundary of Chinatown and Little Italy. Natives of each region vie for real estate in lower New York City, the ultimate American economic and communal meeting place. Getting a company listed on the NYSE or NASDAQ remains the goal for business distinction; if you can make it in New York, you have made it. These regions clearly produced economically successful ventures. Whether the ties that bound them in tight social networks can be duplicated elsewhere remains more problematic, as their roots in social institutions reflect place particularities beyond economic strategies. That similarities occur across national boundaries and with strikingly different political histories underlines the essentially human nature of reinforcing entrepreneurial networks.

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