

investment by domestic Chinese firms.²⁷ This "round-tripping" is the result of efforts by Chinese firms to access the preferential treatment provided to foreign investors, as well as endeavours to stash assets off-shore. Chinese investors channel their investments through foreign intermediaries, generally located in Hong Kong. As the 1997 date for the return of Hong Kong approaches, however, the mainland investors may move their investment platforms farther afield. The exact size of this flow is unknown.

The main sources of foreign investment have been Hong Kong (including the somewhat misleading "round-tripping" component mentioned above), Taiwan, Germany, Japan and the U.S.. Foreign investment from Hong Kong and Taiwan has been concentrated in the southern and coastal provinces of Guangdong, Fujian and Jiangsu, although investors from Hong Kong are also leading the charge into the interior. Japanese investment has been concentrated in East and Northeast China, as has investment from Korea. Although the Japanese and Korean stakes have been largely in the light industrial sector, investment in larger-scale projects is beginning.

2.6 Russia/FSU

Russia inherited the remnants of the former Soviet Union's (FSU) centrally-planned economic system. While production and allocation decision-making authority notionally flowed down from the State Planning Committee through ministries at the industry and sector level to the various enterprises, economic decision-making was heavily influenced, if not actually controlled, by the Communist Party. All means of production and assets were owned by the state. The system stifled incentives and individual initiative, and eventually led to macroeconomic imbalances and suboptimal, if not perverse, microeconomic equilibria. The system was inefficient and unprofitable. The abundance of resources available in Russia may have masked these problems in the early years of the regime, but as the economy grew and developed, and growth became more dependent on the intensive rather than the extensive use of resources, the system could not cope.

Nikita Khrushchev first attempted to introduce reforms into the system in the early 1960s. He allowed some decision-making authority to devolve to the various regions, however, rather than to enterprise managers. The Kosygin reforms which followed in the late 1960s were reversed when it became apparent that partial change

²⁷ See C. Fred Bergsten and Edward M. Graham, Towards an Asia Pacific Investment Code: Issues and Options, Institute for International Economics, Washington, 1994, p.3. For an expanded discussion of this issue, see Nicholas Lardy, China in the World Economy, Institute for International Economics, Washington, 1994.