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Statement Before the

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**Subcommittees on Asia and the Pacific
and Terrorism, Nonproliferation and Trade**

"China's Predatory Trade and Investment Strategy"

Testimony:

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Thank you for the opportunity to appear before you today. I want to begin by making clear the views I am presenting are my own and not those of either CSIS or Kelley, Drye & Warren. China's economic strategy is well-known. The Foreign Affairs Committee has discussed it in previous hearings, and the administration has documented it in its Section 301 report. Rather than repeat that material, I will spend my time discussing what the United States might do about it. I begin with a fundamental principle: if a country has an adversary and wants to stay ahead of him, there are only two ways: hold him back or run faster. Both strategies have their limitations, which is why the best approach is to pursue both. Let me take them one at a time.

Holding him back means denying him the means of gaining advantage, if possible, while trying to leverage better behavior. This has been the focus of the administration's efforts thus far, and it remains to be seen how successful it will be. We are attempting to deny China advantage through investment controls and export controls, both designed to impede the flow of critical technology beyond our borders. Congress has recognized that the current CFIUS process does not subject enough transactions to review and has moved to expand its reach. Both versions now in conference are thoughtful and carefully drafted. The administration has expressed its support for the legislation, and I agree that its enactment would be a positive step.

Similarly, your committee has reported and the House has passed legislation to reauthorize the Export Administration Act. That is long overdue, as you know, and its enactment would also be a useful step. I would, however, caution the committee against a too-broad expansion of controls. Maintaining control over the crown jewels of our economy is important. Attempting to re-control technologies that have already been released, are not critical, and are available from multiple sources would accomplish nothing and would do serious harm to our exporters.
In addition to investment review and export licensing, devoting more resources to compliance and enforcement is critical. The problem is not with large, established companies which know the rules and devote considerable resources to comply with them. Rather I worry about the small start up -- the proverbial two guys in a garage with a brilliant idea. When a savvy Chinese investor offers them $100 million for their company, they may not know -- or care -- that such a transaction would require CFIUS review or that any technology transfer pursuant to it could require an export license. The government does not currently do an adequate job of finding and monitoring those situations and making sure innovators know what their responsibilities are.

Leveraging better behavior is more complicated. As the president has said, the Chinese are doing what is good for them. Persuading them to do what is not good for them is a heavy lift. Nevertheless, there are some areas where agreement ought to be possible. The Chinese have in the past promised to end commercial IP theft, and there is no reason they couldn't do that again -- and actually mean it. It is a serious domestic problem in China -- most of the current IP litigation is between Chinese companies -- and very much in the government's interest to crack down on it if it wants to keep its own innovators from leaving. Similarly, discrimination against foreign companies in China based on corruption -- for example, the Chinese competing company gets favorable treatment because it is owned by the provincial Party secretary's nephew -- is something the government is already trying to stop.

The most difficult problem to address is *Made in China 2025.* Here we are asking China to restructure its economy into a market-based system and effectively abandon its technology competitiveness goals. Doing that would reduce the Party's control of the economy and the society, which is the last thing they will be willing to do. Many of the technologies at issue involve aspects of the digital economy. For China these are not trade issues; they are national security and public control issues, and they are not susceptible to resolution in a trade negotiation. The president is attempting to force changes through tariffs. That is not likely to succeed for the reason I have indicated -- we are demanding that the Chinese do something that will imperil the Party's control – and it will certainly produce a great deal of collateral damage in its wake.

A better approach is through building coalitions. We have learned over the years that the Chinese do not like to be outliers. They do not like to be singled out as rules violators. When we have been able to get other major nations -- the Europeans, Japanese, Koreans, Indians, Australians and so on all conveying the same message at the same time at a high level we have had some success. So far, the administration has not shown much interest in this approach.
I would also suggest that a more productive course would be to recognize that the long-term battleground is not in China but in the United States and in third countries where the playing field is level. We can deny them advantages here and in the process give a boost to our own manufacturers and innovators. In third countries we can not only compete with the Chinese on more equal terms, we can also develop networks of rules and standards that work to the advantage of Western economies. That is what TPP was really about, and it is what TTIP is about -- building trading structures based on Western rule of law principles and standards to which the Chinese will ultimately have to conform if they want to access the very large market structures and global supply chains we have created.

Beyond trade negotiations our government can also help Americans compete more effectively through more aggressive use of time-tested tactics: letting the Export-Import Bank function as intended, using trade missions to promote American products, and aggressively defending American commercial interests in third countries. The single data point I hope you will remember is that 95% of the world's consumers are outside the United States. Maintaining a competitive advantage over China inevitably means beating them in third countries. If we cannot do that, we ultimately marginalize ourselves and yield leadership to China.

Finally, let me say a few words about running faster. Although it is not my primary topic today, it is more important. The reality is that holding the other guy back doesn't work all that well. There are simply too many ways to get around the steps we take. Plus, there are inevitable limitations on what we can do to control someone else's economic policy. The one thing we can control is our own economic policy, and if we do it well, we can surmount the Chinese challenge. In today's globally integrated economy, that means more than pro-growth macroeconomic policies and more than job creation. In the past I have suggested a competitiveness tripod:

1) Train our workforce for the demands of the 21st century economy through more effective adjustment assistance programs and education policies that help future workers be more agile and acquire the skills necessary in a digital economy.

2) Give our companies incentives to stay here. In my fifteen years representing large companies at the National Foreign Trade Council I learned you can't bludgeon them into submission but you can incentivize them into better behavior.

3) Promote innovation. This is something we have always been good at. Beginning in the Lincoln Administration, the United States has a long history of successfully mobilizing public support and resources to meet national priorities. World-class agriculture, wireless communications, aerospace and the Internet are good examples. Over the years we have shown ourselves to be very good at targeting government resources on innovation in the sectors that will define global leadership in the future. This is what the Chinese intend to do, and we should remember that we thought of it first and can do it better -- not with the massive WTO-illegal subsidies they plan to use, but with expanded support for basic research, encouragement for our private innovators, and immigration policies that encourage smart people to study -- and stay -- here.

These can be debated, and I know my colleague Rob Atkinson has a more detailed plan, but the principle of running faster remains fundamental. A strategy based solely on trying to hold China back will not succeed.