Carolyn Bartholomew
Vice Chairman, U.S. China Commission
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Good evening and thank you for inviting me to speak today. Thank you, particularly, to Cynthia Miyashita, Chairman of the Asia-Pacific Affairs Forum, for including the U.S.-China Commission in your China series. I would also like to acknowledge the leadership of your Congresswoman and my former boss, House Democratic Leader Nancy Pelosi, who appointed me to the Commission.

Thank you to the members of the audience for your interest in our work. The Commission was established in 2000 to monitor aspects of China's behavior after Congress voted to admit it to the World Trade Organization (the WTO).

We were created to track and advise Congress on the national security implications of the bilateral trade and economic relationship between the United States and China. Each year, Congress tasks us to focus on a series of issues. This year, our work addresses eight areas: proliferation practices, economic transfers, energy, U.S. capital markets, regional economic and security impacts, U.S.-China bilateral programs, WTO compliance, and the implications of restrictions on speech and access to information in China.

We hold 8 – 10 hearings a year, mostly in Washington, but have found it useful in the past few years to hold field hearings in different locations around the country, learning first-hand about the impacts, positive and negative, on American communities of U.S.-China trade. We have held hearings in Dearborn Michigan, Akron Ohio, Columbia South Carolina, Seattle, and San Diego, and this year, we also went to the U.S. Strategic Command in Omaha for a day of classified briefings on military issues.

I am one of 12 Commissioners, three each appointed by the House and Senate Democratic and Republican leaders. We run the gamut from a former career military intelligence officer to the former president of the International Steelworkers Union. We are one of the only remaining bipartisan institutions in a town of increasingly bitter partisanship, alternating our leadership between parties each year. We are proud of our annual report, which last year passed 11 – 1 and the year before was unanimous, and the policy recommendations we make to Congress, a number of which have been implemented. Of course, we are particularly pleased when our ultimate customers and clients, American citizens and taxpayers, are interested in our work as well.

As you have heard and as some of you know first-hand, I live in Washington, DC, a quarter mile or so and one neighborhood removed from the embassy of the People's Republic of China. The embassy is on Connecticut Avenue on the edge of a group of splendid chanceries and official ambassador's residences in a very posh neighborhood called Kalorama, Greek for "beautiful view." Just around the corner from the Chinese embassy is the residence of the French ambassador, a truly opulent mansion with a grand dining hall and room for a hundred guests. It's a bipartisan neighborhood as well. Senator Ted Kennedy lives there, reportedly quite peacefully with Defense Secretary Donald Rumsfeld.

But the Chinese embassy is an anomaly in Kalorama, just as China is an anomaly in the community of nations. And just as China itself has been undergoing great changes, so has China's presence in Washington. The question of who is gaining and who is losing from these changes is something I will talk about tonight. Some of the answers may surprise you.

The Chinese embassy sits in two very plain adjacent brick buildings. One used to be an inexpensive hotel for tourist families visiting the Nation's Capital. The other was an apartment building. Neither is mentioned in the list of historical buildings in Kalorama's historical district designation. There is a small parking lot in the back where some of the embassy staff practices Tai Chi in the mornings. And across the street is a tiny park where members of the Falun Gong or Tibetan sympathizers or environmentalists protesting the Three Gorges Dam often hold up protest banners. Without the protestors advertising the fact, you wouldn't know this plain brick building, with its tiny windows, is the embassy of the most populous nation on earth.

But a couple of miles up Connecticut Avenue, Chinese laborers have broken ground on a massive new embassy and chancery befitting a growing economic and military power. The new building, to be completed in 2008, is intended to make quite a different statement than the one transmitted by the humble brick building to the south.

The fact is, just like the Chinese embassy, both old and new, the People's Republic now has one foot firmly planted in the 21st century and one still firmly planted in the year 1978. That's the date, of course, when the Communist party leadership in China realized that three decades of Marxist-Leninism and the Great Leap Forward, followed by the Cultural Revolution, were moving the nation rapidly backwards.

The leadership in Beijing correctly decided that a free market system was preferable to central economic planning. It wasn't rocket science. Just economics 101. The party leaders had only to look at the situation on the Korean peninsula to see that collectivism and Stalinism were a poor match for economic growth and capitalism.

The resulting change to China and the world has been truly profound. China's economic growth has been so remarkable since 1978 that almost every statistic looks like a typographical error. And, centuries of global trade theory are being called into question. China's foreign trade flows, for example, climbed from $21 billion in 1978 to $1.1 trillion in 2004. That's a 52-fold increase. In terms of purchasing power parity, China's economy is now the second largest in the world, just behind the United States, according to Federal Reserve calculations. In very short order, China has become the world's factory floor, now ranked third in its share of world exports, nearly all of them manufactured goods.

Importantly, this economic reform has helped to lift an estimated 200 million people out of poverty. That's a number equal to two-thirds of the American population.

The visible evidence of all this prosperity shows in such cities as Beijing and Shanghai. So, too, does the environmental degradation accompanying it. China is preparing to host the 2008 Olympics and when the Commission visited China in June, we could already see some of the construction for the games. Drab cement apartment buildings in central Beijing are being torn down at an astounding rate to make way for new office buildings. Sports complexes and colorful, modern apartments are going up, many in suburban areas connected by new road construction. Skyscrapers, often complimented by enormous, futuristic-looking sculptures, march up and down the main boulevards. But in seven days spent in three different cities in China, we saw blue sky for a total of only about twenty minutes. The rest of the time, the brown-grey fog of industrial pollution prevailed.

On the roads, cars have taken over from bicycles. China is already the third largest producer of cars in the world, behind Japan and the United States, and the world's second largest vehicle sales market. In the first quarter of 2006, car sales in China rose 54 percent. By 2020, China will eclipse the United States to become the world's largest carmaker, according to Deutsche Bank. Not bad for a country that just a decade ago banned most private ownership of automobiles.

You could fill entire volumes with such wonderful statistics. Some, like New York Times columnist Tom Friedman, already have. To hear Friedman and other authors tell it, nearly three decades of 10 percent annual growth has turned China into a perpetual motion machine, distributing economic benefits throughout Asia. Meanwhile, 290 million American consumers are enjoying declining prices for laptops, big screen televisions and designer jeans while borrowing at low interest rates, thanks to the propensity of the Chinese to save their money and loan it back to us.

But can all this be true? Is this vast rising tide lifting all boats? Or, just the biggest yachts? Are the benefits of China's economic boom being reflected in the lives of the average Chinese? Are they leading to greater freedoms of speech and assembly and religion? Is China's court system affording the people protection of private ownership of land? And, is it delivering justice? Does the government encourage entrepreneurship and innovation?

And what of China's place among nations? We hear much about the role of China as a "responsible stakeholder" – a concept proposed by then-Deputy Secretary of State Bob Zoellick. What does this term even mean and how do we measure "responsible stake holding?"

Is China, for example, acting as a responsible member of the World Trade Organization? Of the United Nations Security Council? Is it, like other responsible nations, working to limit the proliferation of nuclear weapons and other weapons of mass destruction? To stop genocide? To promote open, transparent, and accountable governments and multilateral institutions? To halt pollution and to make wise and efficient use of energy?

Unfortunately, in all too many areas, we find that China's economic growth is not matched by its performance in the indices of responsible governance.

For all the shiny skyscrapers, a closer look at life outside the capital and the big coastal cities such as Shanghai reveals some worrisome trends. Income inequality there is increasing rapidly. In this dubious distinction, China has already surpassed the United States. One big reason is that the 45 percent of Chinese citizens who live in rural areas have not shared in the bounty enjoyed by their urban comrades. Those 200 million who have climbed out of poverty have largely done so by moving to the cities, many to accept low-wage jobs. China still has a long way to go.

The social tensions created by these disparities, exacerbated or facilitated by corruption, are increasingly evident. According to the Chinese government's own statistics, there were 87,000 "disturbances" in 2005 alone. Reporters, forbidden to cover these "events" have been racing to the scene to try to find out what is going on before they are officially barred from the sites. However, several months ago, the Chinese government implemented a new law with a $17,000 fine for reporting on public emergencies or "sudden events" without government approval. That fine will certainly serve as disincentive for honest and open reporting.

There have been many unmet promises in this relationship. Clearly, the supporters in the United States who lobbied Congress so hard for approval of China's admission to the WTO oversold, at best, and mischaracterized, at worst, their case. Here I am talking about the business groups that wield such enormous influence in Washington's corrupted legislative process: the Business Roundtable, the U.S. Chamber of Commerce, the National Association of Manufacturers, and the U.S.-China Business Council, among others. Some of those unmet promises hit very close to home here in the nation's cradle of technological innovation.

Let's take the promises made by the proponents of admitting China to the 149-member World Trade Organization. You may remember the debate over this, in the late 1990's. Proponents of this move brushed aside the fact that China was an authoritarian state, run by central planners according to a succession of five year, industrial policy plans, with little commitment to following market principles. Political reform, we were assured, would surely follow economic reform, just as the day follows the night. And so today, five years after it was admitted to WTO membership, sixteen years after the beginning of the post Tiananmen Square debate on China's Most Favored Nation status, China is an authoritarian state run by central planners according to a new five year plan—the 11th, adopted only this year—still with little commitment to following market principles.

And political freedoms? Freedom of assembly? Freedom of religion? Freedom of speech? Not in China where you can be imprisoned for merely criticizing the government.

Certainly, China's economic growth has resulted in much greater access by the Chinese people to telecommunications and to the World Wide Web. But that access is tightly controlled and belies the promise of the Internet – open access to the free flow of information for all. The Chinese government, fearing the use of modern communications to organize against it, to date has parried technological advances, in most cases with startling effectiveness. It deploys advanced technology to censor telephone and Internet communication, track cyber-dissidents, and disseminate propaganda. Last year, the Commission heard testimony that China employs 30,000 people to censor the Internet. On our recent trip, we were told that estimate is now considered low.

The Chinese government uses routers that disrupt user attempts to access particular websites, software that detects sensitive key words and prevents user connections to sources where those words appear, and programs that block Internet discussion boards and chat rooms. It also uses burdensome licensing requirements for Internet cafes and harsh but selective enforcement that encourages self-censorship.

As a condition of their operation in China, Internet Service Providers are required to keep personal data on subscribers, which requires hiring site moderators to ensure posted content complies with government requirements. Words such as "dictatorship, truth, and riot police," are automatically banned in online forums.

Chinese government control of information has consequences for the United States, too. The Chinese government uses the Internet to encourage nationalist sentiment, rarely censoring anti-U.S., anti-Japanese, and anti-democratic views. Demonstrations against the U.S. Embassy in Beijing are often coordinated through text messaging. These practices risk creating an environment prone to misunderstanding and miscalculation in the bilateral relationship, particularly during times of crisis, such as the seizure of the U.S. spy plane in April, 2001.

In addition to our serious concerns about what is occurring in China, we are also concerned about the contributions that U.S. technology companies are making to China's capability to control and repress information, and to identify and penalize those who express views contrary to the government's.

Google, Yahoo, and Microsoft have all made Faustian bargains in order to do business in China. They provide censorship mechanisms and, in the case of Yahoo, have even identified the authors of Internet content that the government found objectionable. At least one such cyberdissident was imprisoned as a result. Meanwhile, Google places limits on its Internet searches to avoid offending the government.

What is the conclusion here? Far from capitalism changing the Chinese government, it is the Chinese government changing capitalists. Rather than a new birth of freedom with telecommunications and the Internet serving as the handmaiden of democracy, we have the Internet entrepreneurs selling rope to the hangmen.

So then what of China's behavior, in particular its promises to adhere to WTO rules on trade? Here, too, we find that the promises don't match the reality. There are many examples including lack of compliance with market access agreements and the imposition of non-tariff barriers. Today, I will just discuss three issues—the rampant piracy of America's intellectual property, China's mercantilist export policy, and the calculated manipulation by Beijing of the value of its currency.

On our recent trip to China, we were astonished to hear one top official at the Chinese Ministry of Commerce insist that piracy is "negligible." Just walk down the street in Beijing and you will be offered pirated CDs. Entire shopping malls are devoted to knock-off goods.

From every measurement, other than those of some Chinese government officials, violations of intellectual property rights are rampant. The Business Software Alliance and the U.S. Trade Representative's office in Washington say that more than 90 percent of the business software in use in China is unlicensed. Just imagine what a subsidy for Chinese business that entails—free software! Nearly 100 percent of the DVDs available in China are pirated.

But the problem does not stop there. The Commission heard testimony this year about the diversification and increasing sophistication of Chinese counterfeiting. Chinese counterfeiters are, for example, fashioning auto parts, including brake pads made out of grass and wood, and selling those under American brand names, even exporting them to the United States. Counterfeit parts are being discovered in commercial airplanes and even in U.S. military vehicles and weapons.

There is growing evidence that pharmaceuticals sold on the Internet, purporting to be from Canada, are actually knock-offs coming from China, and their ingredients are sometimes bogus. The risk to the United States of rampant IPR violations is no longer just economic, serious as that is. They are now an increasing threat to the health and safety of American consumers.

Let's turn to the trade deficit. At the time of the Tiananmen Square massacre in 1989, the U.S. trade deficit with China was $3 billion. In 1995, the U.S. bilateral deficit with China was about $20 billion. Ten years later, last year, it was ten times that amount, $202 billion. That meant that China accounted for 28 percent—the largest portion of any nation--of America's 2005 trade deficit of $716.7 billion.

The problem is accelerating as the gap with China continues to grow dramatically. Last Thursday, the Commerce Department said the June trade deficit with China was $19.7 billion, up from $17.7 billion the month before. We sold $4.3 billion of stuff to China in June; China sold $24.1 billion of stuff to us.

Well, so what, some say. Why should this matter?

America's overall trade deficit requires that we get foreigners to finance the difference between our exports and imports. Foreigners do so either by loaning us the money or by investing in the U.S. Or we can also pay for our deficit by selling American-owned properties held overseas.

So far this big debt run-up has not been painful. That's because Beijing has decided to loan America the money and at pretty good rates, too.

Some time this year, in fact, China will have accumulated $1 trillion in foreign currency reserves—mainly dollar-denominated securities such as U.S. government and corporate bonds. China has accomplished this in part by buying up the dollars that enter the country to pay for China's exported goods. The Chinese central bank then uses those dollars to buy U.S. bonds.

This accomplishes an important goal for China, which wants to expand its economy through exports to the rest of the world. Buying up all those dollars with Chinese Renminbi helps to keep the value of the dollar from falling or conversely, the value of the RMB from rising. A falling currency is exactly what you would expect from a country that runs a huge trade deficit like America's. It is a way that the free market has of balancing trade among countries.

But China is cheating the market by manipulating its currency—artificially pegging it at about 8 RMB to the dollar. Economists generally estimate that this gives China a 15 percent to 40 percent price advantage. That means that U.S. exports to China are 15 percent to 40 percent more expensive than if the two currencies traded freely with each other. So here is your perpetual motion machine in a sense. America will go on buying from China so long as China loans it the money to do so at an artificially low rate of interest and exchange.

Who is the loser in this? Well, for one, the Chinese people. Their standard of living is artificially lowered because their economy is based on production for exports rather than production for internal consumption. Chinese government policies constrain their ability to make their own decisions on consumption levels and investment opportunities. They would like to be better fed and healthier, no doubt, but the government is directing investment away from such things as agriculture and hospitals and toward the production of goods for export. The choice is not theirs.

Another loser is America's small and medium-sized manufacturers. Unlike such large multinational corporations as General Motors, Caterpillar, Intel, General Electric, Microsoft, Boeing, and Motorola, smaller American manufacturers don't have the flexibility or the easy credit it takes to shift jobs and factories to China. Also, while the artificially low value of the RMB acts as an inducement for multinationals to buy cheap land, labor and components in China, it acts as a barrier to the exports of America's smaller manufacturers. Similarly, such large retailers as Wal-Mart and Target can sell the subsidized Asian imports at higher profit margins.

The Commission recently held a hearing in Michigan and heard from auto parts makers and tool-and-die manufacturers. We found them in desperate shape. They tend to be small manufacturers, many family-owned. They can't afford to move to China, and most don't want to, even though the Big Three automakers -- Ford, Chrysler and General Motors -- have already done so and are insisting on sourcing their parts in China. Industry analysts predict that of the 800 parts manufacturers in business in the U.S. in 2000, only 100 will remain by 2010. This has enormous implications for the United States. Three of every four jobs in the production of motor vehicles today are in the companies that make the parts, rather than in the Big Three that mostly just assemble the vehicles and then market them through dealerships.

Auto manufacturing is the crown jewels of our manufacturing base, providing not only significant employment, but also the high-technology processes, engineering, design work, and technological spin-offs that the space program once created. And, the auto sector and the steel working sector that supports it are a critical component of our defense industrial base. The decline of tool-and-die manufacturers and the high-skilled workers they employ is already having consequences for our ability to produce the equipment needed to support our military.

I should point out that we invited the Big Three to testify at our hearing. All of them, including their chief trade association, turned us down. The Chinese government rewards those who do what they want and punishes those who speak out against its practices. The Big Three, already heavily invested in China, fear the loss of special privileges—cheap land, tax breaks, loans from state-owned banks at favorable rates, loan forgiveness, a cavalier approach to workers rights—if they should openly criticize the government.

America's biggest corporations and business lobbies counsel the Bush Administration to take a go-slow approach in pushing China to revalue its currency, as they do with virtually any systematic response to Chinese unfair trade practices. As a result, the Bush Administration, like the Clinton Administration before it—at the urging of Big Business – does not use its leverage to force action by the Chinese government to halt unfair trade practices, but settles for talk, instead. The result has generally been a trail of broken promises, re-negotiated agreements, and lots of press releases.

So, we watch the contortions the Department of Treasury goes through to avoid designating China as a currency manipulator. Such a designation would require the Administration to act, not just talk. And without serious action, we face the possibility of passage of the Schumer/Graham bill, which would implement serious across-the-board tariff hikes on Chinese products.

As we are adding up the list of consequences of admitting China to the WTO and giving it normal trade relations with the United States, here's another one: U.S. multinationals have come to identify more with Beijing than with Washington. They are profiting from Chinese mercantilism and protectionism. The Chinese government does not need to spend a dime on direct lobbying in Washington, although it recently signed a modest-by-Washington standards lobbying contract for $20,000 a month with a major D.C. lobbying firm —Beijing already has America's biggest companies to represent its interests. They are the loudest voices in and the biggest beneficiaries of U.S.-China policy.

I am not among those who believe that China, by acting as our creditor and we, by acting as their debtor, have necessarily placed ourselves in a master and vassal relationship yet, although we are heading in that direction. Some who hold the view that Americans have become indentured servants insist that we cannot do anything to upset the Chinese government because if we do, they will stop financing our misguided fiscal policies. We must remember that China only holds an estimated 6.7% of our publicly held debt. If China's central bank started dumping that, they would reduce the value of their remaining holdings. And besides, China needs the United States, its prime customer, more than the United States needs China as a supplier.

Now, what about China's role as a responsible stakeholder in world affairs? China has received oceans of praise internationally for its willingness to sponsor the six party talks among Japan, Russia, the United States, and North and South Korea. They have been using that card with the U.S. for at least the past twelve years. And over that time, North Korean behavior hasn't changed much. It certainly hasn't improved. Witness North Korean President Kim Jong Il's missile diatribe this past July when he fired a series of missiles east into the Pacific. The Chinese government either has leverage with the North Koreans it isn't using – oil and food for example – or it doesn't have the leverage and we should stop pretending it does.

Compare China's ineffective efforts to restrain North Korea with its eagerness to embrace other dangerous regimes around the world in order, among other goals, to secure access to oil, much of which it may actually be selling into the world market, rather than using at home. While Sudan and Iran are pariah states for their support of terrorism, China has forged close ties with them. This allows the Chinese government to position itself as a counterbalance to U.S. power and gives Chinese state-owned energy companies a competitive advantage over U.S. and other foreign companies excluded from those markets by altogether justified sanctions against their governments. Maintaining this competitive advantage means the Chinese government is not interested in solving the problems with these countries. The longer the problems continue, the more they solidify their place in those markets.

Sudan is a perfect and perfectly horrifying example of China's foreign policy strategy. In early August, the Commission held a hearing on China's role in the world. Among our witnesses was Dr. Eric Reeves, one of the driving forces behind the international campaign to stop the genocide in Sudan. Dr. Reeves started his testimony with the following statement,

"There is in all of Africa no more destructive bilateral relationship than that between China and Sudan, certainly when viewed from the perspective of U.S. interests and those of the people of Sudan. Beijing's relentless military, commercial, and diplomatic support of the National Islamic Front regime has done much to ensure that Sudan remains controlled by a vicious cabal of genocidaires."

The Chinese government uses military equipment, money, technical expertise, and its votes in the UN Security Council to protect its partner from international sanctions. Human Rights Watch, Amnesty International, and Doctors Without Borders have all documented the use of Chinese military equipment in attacks on the people of Darfur. Meanwhile, China has invested at least $4 billion in Sudan and controls a significant portion of the oil fields. In return, China opposes efforts by the international community, particularly through its vote on the U.N. Security Council, to stop the genocide in Darfur. And genocide it is.

Elsewhere in Africa, the Chinese government allies itself with other despots and human rights abusers, undermining international efforts to promote sustainable real development on that continent. As major donor countries are trying to re-tool their development assistance to promote transparency, accountability, an end to corruption, and good governance – and to make foreign aid more effective -- the Chinese government proudly goes in the opposite direction. In 2004, in fact, Chinese President Hu Jintao stated, "Providing African countries with aid without any political strings within our ability is an important part of China's policy toward Africa."

On July 2, 2005, hundreds of thousands of people around the world attended the Live 8 concerts designed to draw attention to African poverty. On that very same day, China Great Wall Industry Corporation was announcing a deal with Nigeria to cooperate on future satellite launches. The China Great Wall Industry Corporation was sanctioned by the United States in 1991 for selling missile technology to Pakistan. Its actions to secure a satellite technology pact with Nigeria are part of the Chinese government's strategy to ensure access to Nigerian oil and gas.

China's relationship with Zimbabwe is another example. Zimbabwean President Robert Mugabe looks to China for loans because the larger international community has shunned him due to his blatant human rights abuses. While Zimbabwe faces economic collapse and its people face starvation, Mugabe's government ordered 12 FC1 fighter jets from China in late 2004. (The FC1 is similar to Russia's MiG-33.) This was China's most advanced military aircraft order from an African nation, a move that angered South Africa, where many analysts fear it could begin an arms race in Sub-Saharan Africa. In Angola, a country with questionable human rights practices, China signed a $2 billion infrastructure loan program linked to oil deals. It also provided a gift to Angolan officials of housing surrounded by a security fence, presumably to keep out the shantytown dwellers that surround it. Angola is currently China's second largest supplier of oil.

This strategy and these practices are not limited to Africa. The Chinese government is actively supporting the government of Burma, interested in strengthening its relationship with Venezuela, and, as mentioned, working with the government of Iran.

What does all this mean for America? We know that terrorist cells seek out safe havens in failed and failing states. China's habit of propping up corrupt regimes hinders America's ability to stop rogue states, and to help to create stable, prosperous and open societies where governments respect the basic human rights of their citizens. When Western countries want to use the leverage of assistance or investment to encourage reform in African countries, the Chinese government is prepared to fill the investment hole without constraints. When we want to use multilateral institutions to censure appalling human rights practices, even genocide, the Chinese government stands in the way.

So what are we to think about the state of the U.S.-China relationship? For the seventeen years in which I have been following U.S.-China policy, experts have wrestled with the nature of the relationship. Are we competitors? Friends? Antagonists? Strategic Partners? Potential enemies? There is agreement only that China is a member of the United Nations Security Council and that it is a large and growing economy situated in Asia. There is also a huge gap between the perceptions of the American people and the policy elite about everything to do with this relationship.

And, while the United States approaches its dealings with China on an ad hoc basis, the Chinese government has a strategic vision for what it wants to accomplish. We lack any coherent policy architecture, have yet to determine what U.S. priorities should be in the relationship and whose interests should be served, and end up lurching from issue to issue as they arise.

The new term of art, of course, is responsible stakeholder. By that, Deputy Secretary Zoellick apparently meant that China, with its vast resources and potential, should shoulder a level of responsibility commensurate with its economic and military power and its seat on the U.N. Security Council. The Chinese were initially bewildered by this notion since there is no equivalent word in Mandarin.

The Commission has just started the process of writing our 2006 Annual Report to Congress. A number of us are thinking about how to define what a responsible stakeholder is, as well as considering standards by which the Chinese government's actions should be measured.

I cannot resist the temptation to bring up one final controversy, the brief but intense fight over the attempt by the Chinese National Overseas Oil Company, or CNOOC, to purchase the El Segundo-based Unocal. The controversy ended when China withdrew its purchase offer, but the larger issues remain unresolved. Among them is the fact that the Chinese Communist party still controls many of the companies in China despite its pledge to move toward a market-driven economy. Also, there is the question of whether China ought to be trying to control natural resources in the ground—hording them, essentially—or whether China should be willing to engage in the global markets for such commodities as oil, rare earth minerals, and bauxite, as most market-oriented economies are willing to do.

Calling the transaction a free market activity, as the Chinese originally insisted, was absurd and a distortion of the notion of free markets. CNOOC is 70% owned by the Chinese government. It is one of three Chinese state-owned oil enterprises. The purchase of Unocal was approved by the State Council, China's cabinet, and the governor of the State Central Bank helped to assemble the financing package. The enterprise has direct and special access to the unlimited deep pockets of the Chinese government's reserves.
The loan package was heavily subsidized -- $7 billion from CNOOC's parent, China National Offshore Oil, which is 100 percent owned by the Chinese government.

Why should the Chinese government's control of CNOOC have mattered? Because the Chinese government would be taking ownership and control of a precious natural resource that is now freely available to America and its citizens. And because our allies, such as Japan and South Korea, also depend on the Liquefied Natural Gas now sold by Unocal. Unocal is also the owner of the last U.S. source of rare earth minerals, a critical component of magnets used in JDAMS, smart bomb technology, and other vitally important military applications, as well as being essential to the production of virtually all electronic devices including computers, mobile phones and plasma/LCD displays. The Chinese have been trying to corner the market on rare earth minerals. As globalization picks up speed and international business transactions become more complex, we need to know that the U.S. government has processes in place to weigh effectively the risks and benefits of such deals. Many of us do not yet have such confidence.

I mentioned at the beginning of this talk the old Chinese embassy in Kalorama and the construction of the new embassy, also on Connecticut Avenue to the north. Well, halfway between the two lies the National Zoo. The biggest visitor draw there is the new Panda cub, Tai Shan. He is the 62-pound offspring of Giant panda parents who are on a 10-year loan from the China Wildlife Conservation Association.

Tens of thousands of people who are unable to visit Tai Shan in person are accessing the two pandacams on the national zoo's website. Looking at the pandas, you can't help but be optimistic. It is indeed possible for the United States and China to have a mutually beneficial relationship. We hold many interests in common. But, in order for such a relationship to be sustained, our policymakers must determine, define, and defend U.S. interests – interests which address the economic security and national security of the American people, not just the major corporations. That is the challenge which the U.S.-China Commission was created to help meet. We look forward to continuing our work to this end.

Thank you for the opportunity to speak here today and for your attention. I look forward to your questions.

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