STANDING UNITED AGAINST THE PEOPLE'S REPUBLIC OF CHINA'S ECONOMIC AGGRESSION AND PREDATORY PRACTICES

HEARING

BEFORE THE

SUBCOMMITTEE INDO-PACIFIC

OF THE

COMMITTEE ON FOREIGN AFFAIRS
HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTEENTH CONGRESS

FIRST SESSION

MAY 18, 2023

Serial No. 118–25

Printed for the use of the Committee on Foreign Affairs

Available: http://www.foreignaffairs.house.gov/, http://docs.house.gov,
or http://www.govinfo.gov

U.S. GOVERNMENT PUBLISHING OFFICE

53–222PDF WASHINGTON : 2023

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STANDING UNITED AGAINST THE PEOPLE'S REPUBLIC OF CHINA'S ECONOMIC AGGRESSION AND PREDATORY PRACTICES

Thursday, May 18, 2023

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON THE INDO-PACIFIC,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:01 a.m., in room 210, House Visitor Center, Hon. Young Kim (chair of the subcommittee) presiding.

Mrs. KIM OF CALIFORNIA. Good morning, everyone.

The Subcommittee of the Indo-Pacific on the Foreign Affairs Committee will come to order.

The purpose of this hearing is to spotlight different dimensions of the People's Republic of China's economic coercion, economic coercion tactics, and discuss how we can coordinate an allied response.

I now recognize myself for an opening statement.

Welcome. This is our Indo-Pacific Subcommittee's hearing examining the People's Republic of China's economic aggression and predatory practices. Today we will hear from experts on the PRC's economic coercion, and my goal for this hearing is to give the witnesses an opportunity to sound the alarm on the PRC's predatory practices against our partners, allies, and even everyday Americans.

One of our witnesses is a firsthand victim of PRC's economic coercion and predatory practices. The PRC often successfully intimidates individuals and entities not to speak openly. So we thank you, Mr. Alon, for having the courage to tell your story publicly.

I recall in October 2021 my colleague, Mr. Brad Sherman, said during the House Financial Services Subcommittee hearing on China that several financial industry representatives had withdrawn their original commitment to testify because of fear of backlash from China. It is unacceptable for the CCP to limit Americans' free speech and even more unacceptable that the CCP can do it without consequences.

Last month, U.S. Chamber of Commerce warned that China's mounting scrutiny of American companies have dramatically raised the risks of doing business in the country.

I would like to submit for the record a Reuters article titled "China Detains Staff, Raids Office of U.S. Due Diligence Firm Mintz Group," as well as a Wall Street Journal article titled "Bain's

Staff in Shanghai Questioned as China Targets Foreign Businesses."

[The information referred to follows:]

REUTERS

My View Following Saved

World

China detains staff, raids office of US due diligence firm Mintz Group

By Michael Martina and Yew Lun Tian

March 24, 2023 7:14 AM EDT · Updated 8 months ago

Aa

A general view shows traffic during evening rush hour at the central business district (CBD) in Beijing, China, January 15, 2021. Picture taken January 15, 2021. REUTERS/Tingshu Wang *Acquire Licensing Rights*

WASHINGTON/BEIJING, March 24 (Reuters) - Chinese authorities raided the office of U.S. corporate due diligence firm Mintz Group in Beijing and detained five local staff, the company said, putting foreign companies in China on alert just as the country hosts an international economic forum.

News of the raid and detentions comes as Sino-U.S. relations have spiraled downwards following months of diplomatic tensions, including over the U.S. military downing in February of a suspected Chinese spy balloon and a planned U.S. transit next week by the president of Taiwan, the self-governed island China claims as its territory.

"We can confirm that Chinese authorities have detained the five staff in Mintz Group's Beijing office, all of them Chinese nationals, and have closed our operations there," the company said in an emailed statement to Reuters late on Thursday.

It said it was ready to work with the Chinese authorities to "resolve any misunderstanding that may have led to these events", and that its top concern was the safety and wellbeing of colleagues in China.

"Mintz Group has not received any official legal notice regarding a case against the company and has requested that the authorities release its employees," the company said.

Chinese foreign ministry spokeswoman Mao Ning said on Friday she was not aware of this case. The Beijing public security bureau did not respond to a request for comment.

A source at the New York-headquartered firm earlier told Reuters on condition of anonymity that the company's local legal counsel said the raid occurred on the afternoon of March 20, and that the employees were being held incommunicado somewhere outside of Beijing.

'RED ALERTS'

As per Mintz Group's website, the Beijing office is its only one in mainland China. The website says the company specialises in background checking, fact gathering and internal investigations. Its wide-ranging clients include the National Football League, New York City and The Beatles, according to media reports.

Mintz has 18 offices around the world and hundreds of employees. Randal Phillips, a partner at the firm who heads its Asia operations but is based outside of China, is listed on its website as the Central Intelligence Agency's former chief representative in China.

Phillips worked in Beijing for years after leaving the CIA. There was no indication the incident was related to him, and Reuters was unable to reach him for comment.

The news of the raid and detentions comes as Beijing is gearing up to hold the three-day China Development Forum from Saturday, where executives from multinationals and representatives from international organisations will be among the more than 100 overseas delegates present.

One U.S. business community person told Reuters the Mintz Group incident sent a "remarkable signal" that Beijing wants foreign money and technology but that it won't accept credible U.S. firms conducting due diligence on Chinese partners or the business environment.

"Red alerts should be going off in all boardrooms right now about risks in China," the source, who did not wish to be identified due to the sensitive nature of the matter, said.

China has said it welcomes foreign trade and investment but stressed that security comes before development.

U.S. businesses operating in China are increasingly pessimistic about their prospects in the world's second-largest economy, according to a survey released this month by the American Chamber of Commerce in China.

Two-thirds of the respondents cited rising U.S.-China tensions as the top business challenge.

Western due diligence companies have got into trouble with Chinese authorities before. British corporate investigator Peter Humphrey and his American wife Yu Yingzeng, who ran risk consultancy ChinaWhys, were detained in 2013 following work they did for British pharmaceuticals group GSK.

Humphrey, who spent two years in jail for allegedly acquiring personal information by illegal means, which he denied, told Reuters that providing due diligence in China was even harder now because of a "massive tightening in access to information."

"The foreign business community needs due diligence in order to conduct safe business, to pick the right partners and the right hires, to invest in the right companies without losing their shirt ... But Beijing has made it impossible to do this," he said in an email.

"This is at a time when Western companies need transparency more than ever," he added.

Reporting by Michael Martina in Washinton and Yew Lun Tian, Laurie Chen and Joe Cash in Beijing; Editing by Raju Gopalakrishnan, Muralikumar Anantharaman and Jane Merriman

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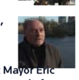

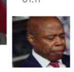

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Polish president to swear in government; opposition condemns 'farce'

Europe · November 27, 2023 · 3:53 AM EST

Poland's president will on Monday swear in members of a government that will likely only last until December, in what opposition parties say is a "farce" intended to delay them from taking power after they won a majority in an October election.

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BUSINESS | ASIA

Bain's Staff in Shanghai Questioned as China Targets Foreign Businesses

American businesses face increasingly risky environment in China

By *Dan Strumpf*

Updated April 27, 2023 11:19 am ET

Bain & Co.'s presence in China includes offices in Shanghai, as well as Beijing and Hong Kong. PHOTO: HECTOR RETAMAL/AGENCE FRANCE-PRESSE/GETTY IMAGES

HONG KONG—Chinese authorities questioned Shanghai workers at consulting firm Bain & Co., underlining the mounting uncertainties facing foreign executives and businesses operating in China after a series of detentions and investigations.

The Boston-based company said Wednesday U.S. time that it was cooperating with authorities and declined to comment further. Shanghai police didn't immediately respond to a request for comment on the reason for the visit, earlier reported by the Financial Times, which also said police took away computers and phones.

The episode underscores the increasingly risky environment for businesses operating in the world's second-largest economy amid worsening ties between

Beijing and Washington. It also comes as China brings a potentially wider array of business activities under an expanded anti-espionage law that was updated this week.

Sino-U.S. tensions are the biggest challenge for American businesses this year, according to a survey of foreign executives released Wednesday by the American Chamber of Commerce in China, with almost two-thirds of the more than 100 respondents ranking it their top concern. Almost nine out of 10 said they were pessimistic or slightly pessimistic about U.S.-China relations, the survey showed.

Michael Hart, president of the Beijing-based chamber, said Wednesday before reports of authorities' visit to Bain that the risk of detention was a worry that had come up in conversations with foreign business leaders in China. "They have raised this question," he said, adding that while it isn't seen as likely, "it is a major concern."

In its latest travel advisory published March 10, the U.S. State Department said Americans should reconsider travel to China, citing risk of wrongful detentions, what are known as exit bans and other legal risks.

In an opinion piece published Thursday, China's official Xinhua News Agency said the U.S. has been sending mixed messages to China, expecting cooperation while seeking to contain the country's rise. "It is like stretching out one hand for a handshake and saying, 'Let's work together,' and then slapping the person in the face with the other," it said.

On Wednesday, China passed an expanded version of its espionage law that placed tighter state control over a wider swath of data and digital activities. Foreign executives said they worry the new law, and its extended definition of what could constitute espionage, could effectively criminalize an array of normal business activities such as gathering intelligence on local markets and business partners.

Last month, authorities raided the Beijing offices of the due-diligence firm Mintz Group, detaining all five of the American company's staff members in mainland China. Mintz said its Beijing office was closed following the raid. The company said it is licensed to do business in China and operates transparently and within the law.

Also in March, China said they detained an employee of Japanese drugmaker Astellas Pharma Inc. on suspicion of engaging in espionage activities. The detained man is a Japanese national in his 50s, Japan's chief spokesman said at the time.

Mintz didn't immediately respond to a query seeking an update on the employees who were detained. An Astellas spokesman said the company is communicating with the Japanese government and will take appropriate measures.

Mintz and Bain both operate businesses involving collection of information, an area that some executives worry are coming under increasing scrutiny from Chinese authorities. As a due-diligence firm, Mintz offers services such as background checks and investigations on potential business partners, rivals and new hires.

Bain—whose presence in China includes offices in Beijing, Shanghai and Hong Kong—specializes in providing counsel to businesses and conducts and publishes research on local markets.

The detentions come as China is seeking to lure foreign investment back to the country following years of a zero-tolerance policy to Covid-19 that squashed growth and shut the country off to much of the world.

At least dozens of chief executives and other senior executives from the U.S. and other countries have made their way to China in the months since the country dropped its pandemic restrictions. Many have paid visits to local staff and offices and attended the handful of high-level conferences that the government has held to show that China is open for business again.

However, many foreign executives remain uneasy about China, especially as relations have deteriorated between the U.S. and China. The U.S., for its part, has stepped up its actions against Chinese firms, slapping new sanctions on a number of companies and putting added scrutiny on companies such as ByteDance Ltd.'s TikTok.

Write to Dan Strumpf at Dan.Strumpf@wsj.com

Appeared in the April 28, 2023, print edition as 'Bain Employees in Shanghai Questioned'.

Mrs. KIM OF CALIFORNIA. These headlines are unfortunately the new normal for American businesses. And as you will hear from our witnesses, we are not doing enough to make these predatory practices consequential to the CCP. The CCP must know that every act of coercion will result in a countermeasure from the United States and its allies, and that the PRC must abide by the same international rules and norms that everyone else in the international community is bound by.

We must also recognize the immense economic pressure that the PRC puts on our allies, partners, and friends around the world. The CCP uses debt-trap diplomacy through the Belt and Road Initiative to achieve its political goals abroad, so much so that it is willing to crash economies and generate instability as it did in Sri Lanka.

This pressure is especially overt in the Indo-Pacific Islands, Pacific Islands, where PRC diplomats host politicians for dinner, and those politicians leave with envelopes full of cash and promises of major infrastructure projects.

It is an unfair fight, and we need to show up. We must equip our diplomats in these countries to respond to economic coercion, and our diplomats need a clear sense of the direction we are going.

To respond to economic coercion, the United States should take several steps. As a first step, American money and technology that fuels CCP coercion and predation cannot keep going to the PRC. It makes no sense to increase the PRC's ability to coerce the United States and help it gain more leverage over us.

Second, if the PRC is unwilling to change coercive elements of its economy, the United States must make it more costly for the PRC to maintain that system. That means action on tech transfers and subsidies.

Third, the United States needs to build a coalition of countries, in particular in the Indo-Pacific, that adopt the same actions. And I cannot stress enough the importance of coordinating our responses to economic coercion with our allies and partners in the Indo-Pacific. When even a few countries act in concert, we can undermine core CCP strategies and objectives. We must stand together to make sure each CCP coercive act against an aligned country fails.

So I look forward to hearing from our panel on how to put these objectives into practice.

The chair now recognizes the ranking member, the gentleman from California, Mr. Bera, for his opening statements.

Mr. BERA. Thank you, Madam Chairwoman, and thank you for holding this hearing. This is a topic that I have spent a lot of time thinking about, we have introduced legislation on, and is incredibly important.

Let me start by saying, you know, the PRC will, you know, try to put out a dialog saying, you know, that the United States is trying to, you know, isolate the Chinese economically. The truth is, we would like to maintain the status quo, which has lifted all the countries in that region through a rules-based order. But we have to respond to Chinese aggression and Chinese economic coercion, and the countries in the Indo-Pacific know firsthand.

You can look at Chinese economic coercion against the Republic of Korea when we deployed THAAD batteries for the protection and the defense of Korea. You know, the Japanese have faced economic coercion and blowback. The Australians have faced economic coercion and blowback.

You see Chinese aggression in the South China Sea. You see them encroaching on Vietnam's exclusive economic zone, the Filipinos' exclusive economic zone, and it is incredibly important for us to understand how they are using economic coercion and how we can counter this.

Even more so worrisome is what they are doing in recent weeks and months. You know, we have seen direct targeting of American companies in terms of targeting of Micron. Now we are seeing them go after consulting companies like Bain Capital and others. And I would argue this is not in China's interest, because as they start to target specific companies, it will make it much harder for us to continue to think about how we do business in China, how investment flows into China, but, again, Xi Jinping has kind of signaled where he is headed.

In the last Congress, we were able to introduce a bill and pass a bill, the Countering China Economic Coercion Act. This bill authorized the Administration to establish an interagency task force to respond to the PRC government's acts of economic coercion and required the evaluation of the impacts on U.S. business and economic performance.

This Congress, in bipartisan support for robust response to the PRC economic coercion, we have introduced H.R. 1135, the Countering Economic Coercion Act of 2023, led by myself, Ranking Member Meeks, Chairwoman Kim, and Chairman of the House Rules Committee, Tom Cole. There is also a Senate equivalent.

This bill would give the President new tools to provide rapid economic support to partners and allies facing economic coercion from the PRC and hold the PRC accountable for its actions. This is the type of legislation that we should be doing to make sure we can both support our allies but also react fairly quickly.

It is also my hope that as the G7 meets in Hiroshima that they will also discuss economic coercion, and hopefully we will see, you know, some statements of support for rules-based order and how the G7 can work together to support one another, but also to support some of those smaller economies and smaller countries, should they face Chinese economic coercion.

So, again, Madam Chairwoman, I appreciate your holding this hearing. I think this is an incredibly important topic, and this is a bipartisan, bicameral topic.

So with that, let me yield back. And, again, thank you.

Mrs. KIM OF CALIFORNIA. Thank you, Ranking Member.

And other members of the committee are reminded that opening statements may be submitted for the record.

And we are pleased to have a distinguished panel of witnesses before us today on this very important topic. Mr. Alon Raphael is the president and CEO of FemtoMetrix, Dr. Derek Scissors is a senior fellow at the American Enterprise Institute, Mr. Matthew Reynolds is a fellow in the economics program at the Center for Strategic and International Studies, and Mr. David Feith is an adjunct senior fellow at the Center for New American Security and was previously the U.S. Deputy Assistant Secretary of State for East Asian and Pacific Affairs.

Thank you all for being here today. Your full statements will be made part of the record, and I will ask each of you to keep your spoken remarks to 5 minutes in order to allow time for members' questions.

I now recognize Mr. Alon for your opening statement. You have 5 minutes.

STATEMENT OF ALON RAPHAEL, CEO, FEMTOMETRIX

Mr. RAPHAEL. Chairwoman Kim, Ranking Member Bera, and distinguished members of the subcommittee, thank you for the opportunity to testify at today's hearing. It is an honor to be here and share my story.

Today I will testify about my company's recent experience with trade secrets and intellectual property theft and how that theft highlights industry-wide vulnerabilities in developing advanced semiconductor production in the United States.

I am the chief executive officer of FemtoMetrix, Incorporated, a small California-based company innovating in-line process control tools for advanced semiconductor production. We produce a complex tool system that is both wholly unique and utterly vital to progress in advanced microchip manufacturing. Our tool system, the Harmonic F-Series, uses unique non-destructive techniques to detect advanced microchip manufacturing blind spots created by the introduction of new materials, new processes, and new 3D architectures.

FemtoMetrix was founded in 2011 building on decades of Department of Defense-funded research at various institutions, including Boeing, NASA, JPL, and the Institute for Space Defense Electronics. FemtoMetrix technology is essential to any country wanting to lead in cutting edge, integrated circuit manufacturing capability. It provides vital data to advanced chipmakers, increasing yields and decreasing the field failure rate of chips sold.

Also, it is the only metrology tool in existence that functions in line for critical applications with the newly emerging chip structures and designs like Gate All Around, also known as Intel RibbonFET and Samsung MBCFET.

In September 2020, FemtoMetrix's Vice President of System and Field, a Chinese national, resigned. Shortly after, another Chinese national hired at first's recommendation, also left the company, followed by a third. During their duties, the three Chinese nationals were trusted team members privy to the inner workings of FemtoMetrix's technology.

The three had significant experience building, calibrating, and using the Harmonic F-Series systems, although they worked in different areas. One even invested in the company while employed there. As we later learned, the three individuals were able to piece together the trade secrets they were separately privy to and create a competing copycat business in China called Weichong Semiconductor.

They made a business plan presentation that contained highly sensitive and proprietary information, which they used to solicit FemtoMetrix's customers, all while still employed there. In the business plan, they did not even remove FemtoMetrix's name from product images.

FemtoMetrix also discovered that they covertly absconded with thousands of files and years' worth of proprietary information upon leaving the company and snuck those files to Weichong in China. In addition, because one was also an investor in the company, he had access to and seems to have taken additional materials.

Weichong has also filed Chinese patents using FemtoMetrix's technology to publicize trade secrets and thwart legal challenges to enforce American trade secret laws. In 2022, FemtoMetrix sued the three Chinese nationals in Federal Court. Weichong has retained a multinational law firm to defend the lawsuit.

Counsel for Weichong has Stated their intention to wage a legal war of attrition. Nonetheless, FemtoMetrix is committed to fighting and defending what is right, because the United States cannot afford to lose FemtoMetrix as that would critically undermine U.S. semiconductor capabilities and leadership.

Assuming FemtoMetrix obtains a judgment, as a practical matter, it will not be enforceable in China. A permanent injunction would likely limit Weichong's prospects for expansion beyond China, but not within. The American legal system is not designed to address deliberate international thefts of this kind and is not adequate for the task.

Foreign companies like Weichong have become accustomed to exploiting the court system's slow-paced and high cost. Alternative means of addressing such international theft are needed. Weichong is not an outlier but an exemplar for the theft of American intellectual property.

It begins in China when someone like a venture capitalist knows someone else like a technologist. The technologist works to create rapport with the target company. Once the technologist has the required access and data, the venture capitalist funds a Chinese company supported by the stolen technology.

The venture capitalist funds litigation through the copycat company and attacks American intellectual property and discloses trade secrets through published papers and patent applications. Then, predatory venture funds likely owned or controlled by foreign entities approach the undermined American company to invest, despite the foreign challenges.

They seek proprietary information technology, customer status, and market position under the guise of due diligence. Their primary goal is to utilize leverage created by the first venture capitalist to eviscerate the American target company further. Developing a novel in-line process control technology costs between 20 and $100 million or more and takes approximately 8 to 10 years of development.

During that extended pre-revenue period, new companies are vulnerable without significant support from large organizations. Small companies like FemtoMetrix are innovating against all odds domestically but cannot protect these innovations from foreign agents.

Due to the theft of FemtoMetrix technology, Weichong is now a company making a vital tool for advanced semiconductor production. While novel hardware is fundamental to technological advances, in-line process control tools rely on algorithms to function and improve. When a tool is integrated into the production line of a microchip fab, its efficacy grows. This is because the algorithms learn from access to a more extensive data set.

This means that if the Weichong tool is installed at leading-edge microchip makers' fabs instead of the FemtoMetrix tool, the FemtoMetrix tool will swiftly become obsolete. Moreover, the tool would be a Trojan horse, allowing Weichong to use the improved and improving algorithms in other areas, further accelerating foreign technological advancement.

Last, a Chinese firm would be the sole supplier of the strategic global resource. There would be no competitive American source of this vital tool.

Thank you.

[The prepared statement of Mr. Raphael follows:]

May 18, 2023

Statement of Alon Raphael

Chief Executive Officer, FemtoMetrix, Inc.

Testimony Before the House Foreign Affairs Committee,
Indo-Pacific Subcommittee

Standing United Against the People's Republic of China's Economic Aggression and Predatory Practices

Chairwoman Kim, Ranking Member Bera, and distinguished Members of the Subcommittee thank you for the opportunity to testify at today's hearing entitled "Standing United Against the People's Republic of China's Economic Aggression and Predatory Practices." It is an honor to be here and share my story.

I am the Chief Executive Officer of FemtoMetrix, Inc., a small California-based company innovating in-line process control tools for advanced semiconductor production. We produce a tool that is both wholly unique and utterly vital to progress in advanced microchip manufacturing. Today, I will testify about my company's recent experience with trade secrets and intellectual property theft and how that theft highlights industry-wide vulnerabilities in developing advanced semiconductor production in the United States.

Introduction

FemtoMetrix is a world leader in in-line optical Non-Visual Defect metrology tools for surface and buried defect detection in advanced semiconductor production. Its metrology system – the Harmonic F-Series – uses unique non-destructive Second Harmonic Generation techniques to detect advanced microchip manufacturing blind spots created by the introduction of new materials, new processes, and new 3D architectures.

FemtoMetrix technology is essential to any country wanting to lead in cutting-edge integrated circuit manufacturing capability. Our technology is crucial to the next iteration of microchip manufacturing. It is the only way to characterize many critical aspects of advanced microchips on the production line. It is also the only metrology tool in existence that functions in line for critical applications within newly emerging chip structures and designs like Gate All Around (also known as RibbonFET and MBCFET). Staying on the cutting edge of microchip manufacturing capability will require FemtoMetrix's technology.

FemtoMetrix's unique technology for process control provides vital data to advanced chip makers, increasing yields and decreasing the field failure rate of chips sold. Advanced microchip manufacturers must be able to characterize what they are making because atomic level deviations in the manufacturing process can cause chip failure if not addressed.

FemtoMetrix was founded in 2011 as a spin-out of the University of California, Santa Barbara, building on decades of Department of Defense-funded research at various institutions, including Boeing, NASA JPL, and the Institute for Space Defense Electronics. FemtoMetrix was founded on the premise that shifts in semiconductor production techniques and materials were needed to continue leveraging the benefits of Moore's Law. Since then, the company has grown from a prototypical startup out of a dorm room, to a small laboratory, to a Samsung Ventures and SK hynix portfolio firm with market-leading technical results and full manufacturing capabilities. FemtoMetrix's progress has been advanced with its Chief Technologist David Adler, former Chief Technologist at KLA Tencor.

Theft of FemtoMetrix's Trade Secrets and Intellectual Property by Chinese Nationals

The Harmonic F-Series is a highly complex measurement tool, the building, calibration, and use of which all involve highly confidential and specialized trade secret information. FemtoMetrix goes to great lengths to protect these trade secrets. FemtoMetrix employees are subject to contractual agreements to keep company information confidential, among other security measures, inside its walls. Outside of the company, FemtoMetrix shares the above information only with select customers and only under strict non-disclosure agreements. In all circumstances, FemtoMetrix limits such disclosures to what is absolutely necessary.

In September 2020, FemtoMetrix's Vice President of System and Field Chongji Huang, a Chinese national, announced his resignation, citing issues with his wife's visa as the impetus to move back to China. Shortly after, Huang's colleague Wei Wei Zhao – a Chinese national hired at Huang's recommendation – also left the company, followed by Puxi Zhou, a third Chinese national.

During their duties, the three Chinese nationals were trusted team members privy to the inner workings of FemtoMetrix's technology. The three had significant experience building, calibrating, and using the Harmonic F-Series systems. In addition, Huang, Zhou, and Zhao worked collaboratively at FemtoMetrix in different areas. FemtoMetrix believed it had a good relationship with all three men and parted on seemingly good terms. Huang even invested in the company while employed there.

As FemtoMetrix later learned, the three individuals were able to piece together the trade secrets they were separately privy to and create a competing copycat business in China called Weichong Semiconductor ("Weichong") that uses entire aspects of FemtoMetrix's trade secrets and proprietary technology. They made a business plan presentation that contained highly sensitive and proprietary FemtoMetrix information, which they used to solicit FemtoMetrix's customers – all while still employed there. This presentation included graphics and photographs created by FemtoMetrix and depicting FemtoMetrix's trade secret product information; reports purchased under the Non-Disclosure Agreement by FemtoMetrix for FemtoMetrix's sole use; and lists of FemtoMetrix past and current employees misrepresented as Huang's employees, among other confidential information. In the business plan, Huang did not remove FemtoMetrix's name from product images.

FemtoMetrix also discovered that, despite security measures, Huang and Zhou covertly absconded with thousands of files and years' worth of proprietary information upon leaving the company and snuck those files to Weichong in China. In addition, because Huang was also an investor in the company, he had access to – and seems to have taken – additional materials. Huang currently still owns stock in FemtoMetrix.

Weichong has also filed Chinese patents using FemtoMetrix's technology to publicize trade secrets and thwart legal challenges to enforce American law regarding trade secret protection. The full extent of Huang, Zhao, and Zhou's theft continues to unfold as information regarding Weichong trickles out of China.

Inadequacy of Litigation Against Weichong

In 2022, FemtoMetrix sued Huang, Zhou, Zhao, and Weichong in federal court in California per the employment agreements signed by all three former employees. Although litigation is still in the early stages due to service issues and motion-related delays, on March 10, 2023, the Court ordered an expedited jury trial in the Central District of California to begin on October 3, 2023. Weichong has retained the United Kingdom-based multi-national law firm Orrick Herrington & Sutcliffe to defend the lawsuit. Counsel for Weichong has explicitly indicated their intended strategy of waging a legal war of attrition. Thus far, Defendants have collectively filed two motions to dismiss and appear to be preparing for a third dispositive motion to drive up FemtoMetrix's legal fees. It is unclear how a new company like Weichong can afford one of the most expensive law firms in the world.

Nonetheless, FemtoMetrix is committed to fighting and defending what is right because the U.S. cannot afford to lose FemtoMetrix, as that would critically undermine U.S. semiconductor capabilities and leadership.

Assuming FemtoMetrix successfully obtains the injunction it seeks, as a practical matter, such an injunction is not enforceable in China. A permanent injunction likely would limit Weichong's prospects for expansion beyond China, but not within. Similarly, a judgment for monetary damages against Weichong and its founders is uncollectible in China. Consequently, litigation in a U.S. court has not slowed Weichong's growth, solicitation of investment, or solicitation of FemtoMetrix's customers. The American legal system is not designed to address deliberate, international thefts of this kind and is not adequate for the task. Foreign companies like Weichong have become more accustomed to exploiting the court system's slow pace and unwieldy cost. Alternative means of addressing such international theft are needed. Absent more substantial repercussions, Weichong will continue to develop FemtoMetrix's technology in China while hampering FemtoMetrix's development.

Systematic Theft of American Semiconductor Innovations by Chinese Entities Utilizing Chinese Nationals.

Weichong is not an outlier but an exemplar of the first half of a playbook for the theft of American intellectual property. It begins in China when someone, like a venture capitalist, knows someone else, like a technologist, from a university or other connections. Once the technologist is placed at an American company of interest, he may recruit other Chinese colleagues to the company or else conspire with other current Chinese employees. Sometimes the technologist is selected by paid Western agents employed by the venture capitalist to target technologies of interest by a foreign entity. The technologist (or group of technologists) works to create rapport with the target company. Sometimes the venture capitalist will even provide funds for the technologist to invest in the American target company to build trust and access to otherwise restricted materials. Once the technologist has the required access and data, the venture capitalist funds a Chinese company supported by the stolen technology. The venture capitalist funds litigation through the copycat company attacks American intellectual property, and discloses trade secrets through published papers and patent applications. Summitview Capital and Yunqi Partners are two such venture capital firms that invested in Weichong.

In the second half, predatory venture funds likely owned or controlled by foreign entities, such as OmniPE, approach the undermined American company to invest, despite the foreign challenges. They seek proprietary information on technology, customer status, and market position under the guise of due diligence. Their primary goal is to utilize leverage created by the first venture capitalist to eviscerate the American target company further. Foreign entities employ this deliberate and systematic playbook to steal strategic technologies and address current challenges with advanced semiconductor production.

Systemic Vulnerabilities in Domestic Development of Novel Semiconductor In-Line Process Control Technologies.

Developing a novel in-line process control technology costs between $20,000,000 to $100,000,000 or more. It takes approximately eight to ten years of development before microchip manufacturers consider adopting it and provide meaningful revenues. During that extended pre-revenue period, new companies are vulnerable without significant support from large organizations. Small companies like FemtoMetrix are innovating against all odds domestically but cannot protect these innovations from foreign agents. Small companies do not have the tools or capacity to fight a pattern of systemic theft by foreign entities. Litigation in American courts is inadequate to address incursion, and little support is available.

Larger, established companies are subject to the same tactics but are better equipped to protect innovations. However, they are also hesitant to accept the risks inherent in expensive, speculative, long-term, research-based projects such as novel techniques for in-line process control. And they are reluctant to report foreign theft problems due to economic concerns, such as share prices and marketing image, in addition to other concerns. This leaves small companies such as FemtoMetrix filling a critical gap in the industry without the necessary resources and protections.

While the CHIPS Act seemingly provides additional resources, absent cost-share waivers, smaller companies cannot participate in the program. Instead, larger companies will receive the lion's share and grow without the incentive to innovate as smaller companies like FemtoMetrix do. Suppose the U.S. wants to lead the world in advanced microchip manufacturing. In that case, it must nurture smaller, more agile companies and eliminate the fear that foreign entities will ultimately reap the benefit.

In addition, CHIPS Act funding has yet to reach equipment manufacturers. Groups like MITRE will be critical to advancing innovation from lab to fab, but the effect has yet to be felt.

Consequences of Weichong's Theft on U.S. Advanced Semiconductor Manufacturing

The two leading South Korean microchip makers first invested with FemtoMetrix in 2016 and 2018 to enable yields in advanced node production and expedite next-generation memory product introduction. Yet due to the theft of FemtoMetrix's technology, Weichong is now a Chinese company making a vital tool for advanced semiconductor production. Suppose Weichong continues to develop and sell FemtoMetrix's technology internationally unchecked, with an unfair competitive advantage. In that case, FemtoMetrix cannot compete, and there will be no American source of this vital tool.

While novel hardware is fundamental to technological advances, in-line control process tools rely on algorithms to function and improve. When a tool is integrated into the production line of a microchip fab, its efficacy grows. This is because the algorithms learn from access to a more extensive data set. The more use, the more data, the more it improves.

This means that if the Weichong tool is installed at leading-edge microchip makers' fabs instead of the FemtoMetrix tool, the FemtoMetrix tool will swiftly become obsolete. Moreover, the tool would be a Trojan horse allowing Weichong to use the improved (and improving) algorithms in other areas, further accelerating foreign technological advancement.

Lastly, a Chinese firm would be the sole supplier of this strategic global resource; there would be no competitive American source of this vital tool.

Mrs. KIM OF CALIFORNIA. Thank you, Mr. Alon.

I now recognize Dr. Scissors for your 5-minute opening statement.

STATEMENT OF DEREK SCISSORS, SENIOR FELLOW, AMERICAN ENTERPRISE INSTITUTE

Mr. SCISSORS. Thank you. The chair stole my thunder, so I am—but I will go into more detail. That is to say, if you want to respond to Chinese predation, the minimum step is to stop helping China become a better predator. We have been doing that continuously at times when China was less of a predator than it is now. There is no longer any excuse. American money and technology should not be allowed to help the PRC become better at coercing our allies and us and harming our interests.

And to give an example, in the case that my colleague on the panel is talking about, can American money still flow freely to this Chinese firm while it is in U.S. court? Is there any warning provided to investors that you might be supporting a company that has been accused with merit of taking U.S. IP? Nope. Nope. No restrictions. We can pour money into that company.

And, in fact, on the Chinese side, if you are successful in stealing IP, you become subsidized and more attractive to American investors. So let me flesh out the point—the main point.

Let's start with the fact that we choose not to respond to Chinese coercion. We have the capability to do so. The measure showing this—I will just be brief. We have a little less debt than China, a little less of a debt burden. Hard to believe, because our debt burden is very high, but theirs is even worse. We are a little bit younger. Both trends of those are in our favor.

The wealth gap as measured by Credit Suisse is widening between the U.S. and China. It is not a question of China is catching up quickly, catching up slowly. The wealth gap is widening.

The annual GDP gap is about the same as it was 10 years ago. So the idea that we cannot stand up to the Chinese, that they are the rising power, we are the declining power, on the economic side does not make sense. Our allies of course are much richer and more prosperous than China's allies. They do not call them allies, but close enough, and that would widen the gap if we weren't able to work together with our allies.

Let me say one more point about this. There is a lot of talk about the dollar losing its status to the yuan. There is no sign of that whatsoever. For that to occur, the Chinese would have to be willing to allow money to flow freely out of China, and they are afraid to do that. They are afraid to do that because they have mismanaged their economy.

So until you see stories about money flowing freely out of China, worry about our support for the dollar, our policies, but do not worry about the yuan challenging us.

With regard to China's industrial policy, the goals I think have shifted under Xi Jinping. That is a matter of debate. I do not think they have been trying to maximize growth, at least for the last 5 years. What they are doing instead looks more like gaining economic leverage, taking an indispensable position in key supply chains, so that they can threaten you and it is harder to threaten China.

The tools have not changed that much. We have heard about one, which is coercive IP transfer. Another one is skewing competition in their favor through regulation and subsidies. Large swaths of the Chinese economy are guaranteed monopolies. State-owned enterprises have a national monopoly or a regional monopoly.

There is a lot of revenue involved that makes them a difficult competitor on the revenue side. There are also subsidies for expansion globally, far in excess of what we considered in the United States.

On the tech side, the original problem was requiring tech transfer to operate in China. Now they have become, as we have just heard, more predatory. You do not have to go to China anymore to have China steal your IP. They will come to you and steal it.

The U.S. responses, in the last minute and a half, we have done very little. The tariffs that were imposed during the Trump Administration had little effect on trade. And during that—and I use this expressed very sarcastically—during the trade war, U.S. investment—so 2017 to 2020—U.S. investment in Chinese stocks and bonds rose $780 billion. I really would like someone to declare a trade war on me, and I will issue a bond and money will pour in. That is not standing up to China.

The Biden Administration has been extremely hesitant in its responses in my view. Congress tightened export controls in 2018. The Bureau of Industry and Security, first under the Trump Administration, and then the Biden Administration, ignored part of that tightening with regard to foundational technology, and then set it aside.

We had chip export controls promulgated by the Department of Commerce in October of last year, but we have not gotten the final version and we are still negotiating with South Korea. South Korea is currently exempt from those chip controls, which undermines their purpose.

On the stop helping side, we need to pass binding legislation, not an executive order—executive orders are always inferior to congressional action—that reviews investment, and there is a simple principle. If we do not let the Chinese buy it here because we are protecting the technology, we should not allow American funding to develop it in China. That is not a sensible action on our part, a set of policies where you cannot buy the technology, but we will help you fund it.

Last, I would say there are others, but punishing a few high-profile beneficiaries of IP coercion, we are not going to be able to do this comprehensively. The cat is out of the bag. But we would send a signal to the Chinese that there could be consequences if you steal American IP.

[The prepared statement of Mr. Scissors follows:]

Statement before the House Committee on Foreign Affairs, Subcommittee on Indo-Pacific

On “Standing United Against the People’s Republic of China’s Economic Aggression and Predatory Practices”

Title

Derek Scissors
Senior fellow American Enterprise Institute and Chief economist China Beige Book

May 18, 2023

While the international dimensions can matter a great deal, better American responses to Chinese coercion of American companies and entities are indispensable to successfully confronting Beijing's broader economic aggression. If the US does not consistently stand up to China, even when it's costly to do so, no one else will. The obvious reason is only the US has the economic capabilities to more than match the PRC, if the political will is there.

China's predation stems in large part from its industrial policy tactics. While the ends evolve over time, the means are the same: variations on warping competition through laws and subsidies and coercing intellectual property transfer. Recently, new tactics involving data have emerged. The first step in crafting a global response to these practices is painfully obvious, yet remains untaken: the US stops helping the PRC improve as a predator. American money and technology headed to China must be curbed, or fighting Chinese predation is just fighting ourselves.

American Economic Superiority

The PRC has multiple points of leverage in coercion. It has the second-largest stock of wealth in the world. It has the second-largest domestic market. For this reason, it is the second-largest national importer and, typically, the second-largest annual recipient of foreign direct investment. It has other advantages, such as important roles in a wide variety of global supply chains. But the other advantages also usually appear with the word "second" attached.

Most countries struggle with Chinese predation because, individually, their best choice is often to submit. Urged by domestic constituencies and international partners not to make waves, the US also frequently acts as if we have little choice but to accept the PRC's behavior. This is false. While knee-jerk reactions would be unwise, America very plainly has the capacity to deter or, if necessary, overmatch economic aggression undertaken by China, or anyone else.

National wealth is a measurement of the economic resources available for any task, including combating predation. Credit Suisse has maintained a database of national wealth for more than 100 countries for more than 20 years. At the end of 2021, it put US wealth at $146 trillion (confirmed by the Federal Reserve) and PRC wealth at $85 trillion.[1] In absolute terms, this is the largest gap on record between the two. Personal income is the single best measurement of prosperity. Comparable American and Chinese figures in 2022 were and $65,376 and $5,480, respectively.[2] Finally, the most commonly cited indicator is gross domestic product (GDP). The GDP gap between the US and PRC was well over $7 trillion in 2022, versus $8 trillion in 2012.[3]

The use of dollars in comparison incorporates exchange rate volatility. One response is to adjust for "purchasing power parity" (PPP). PPP-adjusted GDP shows China ahead of America, if by

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[1] Credit Suisse, "Global Wealth Report," https://www.credit-suisse.com/about-us/en/reports-research/global-wealth-report.html.

[2] Federal Reserve Bank of St. Louis, Personal Income per Capita, https://fred.stlouisfed.org/series/A792RC0A052NBEA and PRC National Bureau of Statistics, "National Economy Withstood Pressure and Reached a New Level in 2022," January 17, 2023, http://www.stats.gov.cn/english/PressRelease/202301/t20230117_1892094.html.

[3] Federal Reserve Bank of St. Louis, Gross Domestic Product, https://fred.stlouisfed.org/series/GDP and PRC National Bureau of Statistics, "China Statistical Yearbook 2022," http://www.stats.gov.cn/sj/ndsj/2022/indexeh.htm.

differing amounts.[4] However, the application of PPP is fraudulent. It fails when tested.[5] This is possibly because it relies on open markets, which often do not hold (e.g. China's capital market). Creating a single price for all of the US to compare to a single price for all other countries is nightmarish.[6] PPP has become an exercise in telling poor countries they're richer than they are.

America's advantages are likely to be maintained. The US is less indebted, because the PRC's performance has been even worse. The Bank for International Settlements[7] shows non-financial outstanding credit as a share of American GDP at 252 percent at the end of 2011 and 278 percent in 2021 (falling partway through 2022). The equivalent Chinese figures are 178 and 285 percent (rising partway through 2022). What's happened recently on debt is what will happen soon on demography. According to the UN Population Division,[8] American and Chinese median age was almost the same in 2020. Yet in 2040, China is expected to be 6 years older - 48 versus 42. Projected Chinese aging 2020-2040 is even faster than for any 20-year period in Japan.

Dependence on foreign oil harmed American prosperity and security for decades. The PRC is now the world's top oil importer. And the top agriculture importer. And the top metals importer.[9] Its supplier dependence ranges from Russia and Saudi Arabia to the US and Australia. The dependence stems in part from state ownership of rural land, causing poor land management. China is still advancing with regard to innovation. However, it not only remains behind the US in annual R&D spending, there is a massive historical gap to overcome, due to being (far) behind

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[4] World Bank, "GDP, PPP," https://data.worldbank.org/indicator/NY.GDP.MKTP.PP.CD versus US Central Intelligence Agency, "The World Factbook: Country Comparison – Real GDP (Purchasing Power Parity)," https://www.cia.gov/the-world-factbook/field/real-gdp-purchasing-power-parity/country-comparison.

[5] Examples: Kai-Hua Wang et al., "Does the Purchasing Power Parity Fit for China?" *Economic Research-Ekonomska Istraživanja* 32, no. 1(2019): 2028–2043, https://www.tandfonline.com/doi/full/10.1080/1331677X.2019.1637763 and Steven Yee and Miguel D. Ramirez, "Purchasing Power Parity: A Time Series Analysis of the U.S. and Mexico, 1995–2007," *International Advances in Economic Research* 22, no. 4(2016): 409-419, https://link.springer.com/article/10.1007/s11294-016-9598-4.

[6] World Bank, International Comparison Program, "Using Capital City Average Prices in the Validation Of Inter-Regional Linking Factors," September 24, 2018, https://thedocs.worldbank.org/en/doc/355521539795895513-0050022018/original/ICPIACG06DocS13CapitalCityAveragePrices.pdf.

[7] Bank for International Settlements, "Credit to the Non-financial Sector," February 27, 2023, https://www.bis.org/statistics/totcredit.htm?m=2669.

[8] United Nations, Department of Economic and Social Affairs, Population Division, "Median Age of Population," 2022, https://population.un.org/dataportal/data/indicators/67/locations/156,392,840/start/1990/end/2050/table/pivotbylocation.

[9] US Department of Agriculture, Foreign Agriculture Service, "China: Evolving Demand in the World's Largest Agricultural Import Market," September 29, 2020, https://www.fas.usda.gov/data/china-evolving-demand-world-s-largest-agricultural-import-market#:~:text=China%20is%20now%20the%20world's,imports%20is%20also%20rapidly%20changing;
Daniel Workman, "Iron Ore Imports by Country Plus Average Prices," World's Top Exports, https://www.worldstopexports.com/iron-ore-imports-by-country/;
Rupankar Majumder, "Top Ten Countries with the Highest Bauxite Production in 2021," AlCircle News, https://www.alcircle.com/news/top-ten-countries-with-the-highest-bauxite-production-in-2021-79380#:~:text=China%20records%20as%20both%20the,the%20leading%20importer%20of%20bauxite. and
World Bank, "Copper Ores and Concentrates Imports by Country in 2021," https://wits.worldbank.org/trade/comtrade/en/country/ALL/year/2021/tradeflow/Ixports/partner/WLD/product/260300#:~:text=In%202021%2C%20Top%20importers%20of,Kg)%2C%20Korea%2C%20Rep.

the US in spending for literally every year of the PRC's existence to this point.[10]

A crucial expression of American advantage is the two country's currencies. At the end of 2022, the dollar's share of foreign reserves was more than 20 times the yuan's. At the end of March 2023, its share of global payments was more than 15 times the yuan's.[11] The yuan is not a genuinely independent currency. Its value is artificially maintained by enforcing a narrow trading range against the dollar and by controlling capital exit from the PRC.[12] The chief threat to the dollar's status is not China, it's us. In the background of defeating Chinese economic predation is more responsible American fiscal policy, to maintain the dollar as the world's premier currency.

All of this understates the resources the US could bring to bear, because we also have richer allies than the PRC. The EU is too slow and unwieldy to rely on as a group. Even excluding all EU members, Australia, Canada, Japan, and the UK are still overwhelmingly preferable compared to, say, Cambodia, Iran, Laos, Pakistan, and Russia (data on North Korea are unusable, but its economy is small). In wealth, the first group brings another $65 trillion to the table while the second offers $7 trillion. The 2021 GDP numbers alone are $11.5 trillion versus $2.5 trillion. America outmatches China, and our friends badly outmatch China's friends.

US v. China, from 30,000 feet

	US	China
2021 GDP	$24.4 trillion	$17.6 trillion
2021 wealth	$146 trillion	$85 trillion
2021 personal Income	$64,073	$5446
2021 debt	278% of GDP	285% of GDP
2021 share of foreign reserves	58.8%	2.8%

China's Predatory Policies

The PRC's laws and regulations are like the visible parts of icebergs. They matter and can be a bit daunting, but what's below the surface will sink your ship. The anti-monopoly law coexists with encouragement of enormous state monopolists.[13] When a large or technologically advanced

[10] World Bank, "Research And Development Expenditure (% of GDP) - China, United States,"https://data.worldbank.org/indicator/GB.XPD.RSDV.GD.ZS?locations=CN-US.

[11] International Monetary Fund, "Currency Composition of Official Foreign Exchange Reserves," March 31, 2023, https://data.imf.org/?sk=E6A5F467-C14B-4AA8-9F6D-5A09EC4E62A4 and Society for Worldwide Interbank Financial Telecommunication, "RMB Tracker," https://www.swift.com/our-solutions/compliance-and-shared-services/business-intelligence/renminbi/rmb-tracker/rmb-tracker-document-centre.

[12] Jean-Paul Rodrigue, *The Geography of Transport Systems* (New York: Routledge, 2020), chapter 7: Yuan Exchange Rate, 1981-2022, https://transportgeography.org/contents/chapter7/globalization-international-trade/yuan-usd-exchange-rate/ and Canadian Trade Commissioner Service, "Foreign Exchange Controls in China," November 2, 2021, https://www.tradecommissioner.gc.ca/china-chine/control-controle.aspx?lang=eng.

[13] Within a few weeks of each other, Brenda Goh, "China Fines Seven Shipping Firms $63 Million for Price Fixing," Reuters, December 28, 2015, https://www.reuters.com/article/uk-china-shipping-fines/china-fines-seven-

multinational is involved, the laws on the books pertaining to intellectual property have no connection to what happens in practice. Laws and regulations are meant to formalize policies already in existence or, worse, hide the extent of predation found in the true policies.

From 1993 to 2012, Beijing's dominant industrial policy objective was clear: create jobs inside China and transfer outside jobs to China. There was a generation-long surge of new workers entering the urban labor force[14] that needed to be employed, or "social stability" would be threatened. At home, the private sector was supported – more firms meant more hiring. Environmental destruction was permitted. Large-scale borrowing was as well, when needed for employment. Overseas, all actions were aimed at bringing foreign jobs to the PRC. Promises were made, some kept, to secure WTO accession. The RMB was always cheap. A combination of high competitiveness and distortions, such as subsidies, were used to induce firms to hire in China. Rapid GDP gains were mostly a means to this end, rather than an end in itself.

The labor force began shrinking by 2015,[15] reducing the need for fast economic growth. In light of this, General Secretary Xi Jinping has consistently de-emphasized growth since first taking power in late 2012.[16] It's unclear if there is a new industrial policy top priority or more of an amorphous blob to be molded as suits Xi. One possibility is controlling or co-controlling key global supply chains, such as chemical precursors, materials and packaging for semiconductors, and materials and components for electric vehicles.[17] As the Department of Defense documented in 2022, some chains have clear military significance.[18] Among other things, a grip on supply chains would enhance China's ability to coerce others and limit our ability to respond.

The new priority or priorities may not matter much, since tactics and impacts look to remain largely the same. *The keys are suppressing competition plus coercive acquisition of intellectual property (IP).* The nature of these shifts over time. Initially, the chief means to warp competition was subsidies (mostly uncounted) – very low-cost finance, access to cheap, reliable power, free land, and so on. As the Chinese market expanded, the biggest subsidy became assured revenue from that market via regulatory protection. Of the Fortune Global 500's 45 top firms, 14 are Chinese state-owned enterprises with a guaranteed monopoly in all or some provinces.

IP coercion has also changed. It started simple – if you wanted market access, you had to work with a Chinese entity, to include sharing trade secrets. While a violation of WTO principles,

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shipping-firms-63-million-for-price-fixing-idUKKBN0UB0CE20151228 and Joanne Chiu and Costas Paris, "China Approves Merger of Cosco, China Shipping," *The Wall Street Journal*, December 11, 2015, https://www.wsj.com/articles/china-approves-merger-of-cosco-china-shipping-1449834748.

[14] World Bank, "Labor Force, Total – China," https://data.worldbank.org/indicator/SL.TLF.TOTL.IN?locations=CN

[15] PRC National Bureau of Statistics, "China Statistical Yearbook 2019,"http://www.stats.gov.cn/sj/ndsj/2019/indexeh.htm and PRC National Bureau of Statistics, "China Statistical Yearbook 2022," http://www.stats.gov.cn/sj/ndsj/2022/indexeh.htm.

[16] For some history, see Andrew Batson, "Mobilization and Modules: What's Changing in China," October 13, 2021, https://andrewbatson.com/2021/10/13/mobilization-and-modules-whats-changing-in-china/

[17] Dan Blumenthal and Derek Scissors, "Breaking China's Hold," *The Atlantic*, December 23, 2022, https://www.theatlantic.com/international/archive/2022/12/china-economic-coercion-united-states/672524/.

[18] US Department of Defense, *Securing Defense-Critical Supply Chains: An action plan developed in response to President Biden's Executive Order 14017*, February 2022, https://media.defense.gov/2022/Feb/24/2002944158/-1/-1/1/DOD-EO-14017-REPORT-SECURING-DEFENSE-CRITICAL-SUPPLY-CHAINS.PDF.

Beijing and its supporters defended this as a choice by multinationals.[19] Those years turned out to be tame. Now, through cyber means, the PRC can steal IP regardless of whether the foreign holder has interest in its market and regardless of where the IP is located.[20] China now targets more advanced technology, sometimes for immediate gain and sometimes more to harm leading foreign firms and help less innovative Chinese enterprises become global leaders.

Not as central as but still early in its development is the PRC's emerging data mercantilism. Data extraction from the US and others previously occurred using telecom equipment and service.[21] It now features mobile software, including TikTok but also Temu, WeChat, and apps that store financial information like AliExpress. No matter what they claim, Chinese firms can never refuse the PRC's security ministries,[22] leaving the sole question as whether the data they gather should be safeguarded.

Threats against those moving data out of the PRC intensified in spring 2023. Foreign firms such as Bain have been harassed while domestic firms such as Wind have withheld basic information, fearing that providing it suddenly constitutes espionage.[23] Restrictions will likely apply to American companies reporting to the American government the very regulations and policies that govern their China operations. While insisting foreigners do not understand China, Beijing is trying to ensure fewer people know what's happening there. This makes US policy-making harder and US companies more dependent on the PRC. Data mercantilism fits the PRC's auto mercantilism, for example, but data effects cross industries.

China no longer limits itself to coercing foreign manufactures or even to its own borders, but that's still fair game. A few examples: the PRC's auto sector is passing Japan's as the world's leading exporter. American auto sensor-maker Mallentech has had IP stolen in China and legal

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[19] Edward C. Prescott, Ellen R. McGrattan, and
Thomas J. Holmes, "Quid Pro Quo: Technology Capital Transfers for Market Access in China," Federal Reserve Bank of Minneapolis, December 12, 2013, https://www.minneapolisfed.org/article/2013/quid-pro-quo-technology-capital-transfers-for-market-access-in china#:~:text=Quid%20pro%20quo%20is%20a,countries%20doing%20FDI%20in%20China.

[20] US Department of Justice, Office of Public Affairs, "Four Chinese Nationals Working with the Ministry of State Security Charged with Global Computer Intrusion Campaign Targeting Intellectual Property and Confidential Business Information, Including Infectious Disease Research," July 19, 2021, https://www.justice.gov/opa/pr/four-chinese-nationals-working-ministry-state-security-charged-global-computer-intrusion; and Nicole Sganga, "Chinese Hackers Took Trillions in Intellectual Property from about 30 Multinational Companies," CBS News, https://www.cbsnews.com/news/chinese-hackers-took-trillions-in-intellectual-property-from-about-30-multinational-companies/.

[21] Jesus Diaz, "China's Internet Hijacking Uncovered," Gizmodo, November 17, 2010, https://gizmodo.com/chinas-internet-hijacking-uncovered-5692217; Nick McKenzie, Angus Grigg and Chris Uhlmann, "How China Diverts, Then Spies on Australia's Internet Traffic," November 20, 2018, https://www.smh.com.au/technology/how-china-diverts-then-spies-on-australia-s-internet-traffic-20181120-p50h80.html; and Doug Madory, "Large European Routing Leak Sends Traffic Through China Telecom," Mutually Agreed Norms for Routing Security, June 11, 2019, https://www.manrs.org/2019/06/large-european-routing-leak-sends-traffic-through-china-telecom/.

[22] China Law Translate, "PRC National Intelligence Law (as amended in 2018)," June 27, 2017, https://www.chinalawtranslate.com/en/national-intelligence-law-of-the-p-r-c-2017/.

[23] China Law Translate, "Counter-espionage Law of the P.R.C. (2023 ed.)," June 17, 2021, https://www.chinalawtranslate.com/en/counter-espionage-law-2023/, and Bloomberg, "Police Raid Consulting Firm as China Starts Anti-Spy Campaign," May 8, 2023, https://www.bloomberg.com/news/articles/2023-05-08/china-starts-anti-spy-campaign-says-capvision-leaked-secrets?sref=bWSPFsy2.

protection denied - what now? Hollywood has long toed political lines overseas in order for movies to be released in the PRC, more recently the NBA has. Beijing has threatened Swedish telecom Ericsson both because Ericsson tried to protect itself in a non-Chinese court and due to Sweden's treatment of Huawei. [24] Xi Jinping has repeatedly attacked his own private sector; expecting less coercion of American and other companies is beyond naïve.

What the US Should Do

Multilateral cooperation can play a key role in countering Beijing's economic aggression. It makes more resources available and can close technological leaks. But the argument made by the strongest advocates of multilateralism, that the PRC's size and reach are too extensive to be countered by America alone, are incomplete or flawed. It's exactly because countries have a sizable economic stake in relations with China that they will not act until the US act first in some way, providing economic and political cover. While multilateral cooperation is preferable, American leadership is necessary. And the US is quite capable by itself of countering the PRC.

There is a simple policy principle for countering Chinese predation that is easy to implement and the floor for any serious response: *stop helping China gain more leverage*. Stop giving the PRC money and technology that increases its ability to coerce and reduces the effectiveness of our response. Part and parcel of this is to stop pretending that continuing to provide money and technology is the only way the US can have an acceptably safe relationship with China, that a dangerous "spiral" can only be checked if Washington does what Beijing wants. Curbing economic exchange is not a sanction. Indeed, less economic exchange can limit Chinese capabilities and thus prevent some Chinese sanctions and the ensuing American retaliation.

Start with American money sent to the PRC. The cumulative stock of all US investment in China and Hong Kong was $1.38 trillion at the end of 2021.[25] The bulk is holdings of mainland stocks and bonds. Those holdings soared nearly $800 billion from 2017 to 2020, after candidate Donald Trump vowed to stand up to China and during the supposed "trade war." This clashes sharply with PRC (including Hong Kong) holdings of American securities, which hit a 13-year low in mid-2022. Further, due to large trade surpluses and a closed capital account, Beijing must hold foreign assets. In contrast, American investors chose to send the hundreds of billions, while the PRC engaged in a military build-up, intense cyber activity, repression in Hong Kong, and so on.

The US has muttered uselessly about this. Parts of the Biden administration seem to believe an executive order (EO) on outbound investment should primarily reassure everyone America is not disruptive. The pending EO will likely affect very little investment, while being implemented possibly for only 15 months. Regardless of who's in the White House, Congressional action is superior to an EO. At the least, the US should not permit investment in technologies that China

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[24] Stu Woo and Daniel Michaels, "China's Newest Weapon to Nab Western Technology—Its Courts," *The Wall Street Journal*, February 20, 2023, https://www.wsj.com/articles/u-s-china-technology-disputes-intellectual-property-europe-e749a72e and Richard Milne, "Ericsson Warns of China Retaliation Following Sweden's Huawei Ban," *Financial Times*, July 16, 2021, https://www.ft.com/content/2a596954-1206-4ce2-9dca-9c128d326768.

[25] Derek Scissors, "What to Do About American Investment in China," May 10, 2023, American Enterprise Institute, https://www.aei.org/wp-content/uploads/2023/05/What-to-Do-About-American-Investment-in-China.pdf?x91208.

would not be allowed to acquire by investing here. Beyond that, a narrowed, bipartisan version of the National Critical Capabilities Defense Act[26] was offered in May and could enable a true competition with the PRC, where the US does not help finance Beijing's economic aggression.

The investment can advance Chinese technology. So can direct technology transfer to the PRC. Congress tried to weaken China's hand, with the 2018 Export Control Reform Act. The Bureau of Industry and Security (BIS) first ignored then set aside restrictions on transfer of foundational technology,[27] essentially arguing US corporate profit is worth making Beijing's life easier. In October 2022 BIS published interim rules tightening controls on semiconductor and related exports but, seven months later, final rules have not appeared. The delay is partly due to South Korean firms, which received a one-year exemption and are asking for more.[28]

Multilateralism cannot mean watering down, for the sake of friendly companies, policies already deemed necessary for American security. By their own actions, these companies place themselves at greater long-term risk of successful Chinese aggression. Coercion is tightly interwoven with technology transfer: Beijing coerces firms for the sake of transfer and the acquired technology makes the PRC a better predator. The US should fully implement chips controls, then move on to the next set of technologies, possibly in genetics or biologics.

IP infringement is closely related to technology transfer through exports, and here the American response is non-existent. The Section 301 investigation launched by the Trump administration started with IP, but ensuing tariffs did not consider it at all. It made no difference in application of tariffs if Chinese enterprises benefited from IP coercion or theft, leaving no incentive to change. With violation of IP rights long at or near the top of Beijing's aggressive economic acts, the US should stop pretending that incessant complaints about the PRC's behavior will change it and start to retaliate in some fashion. Retaliation cannot be comprehensive, but high-profile steps against several large, centrally-controlled SOEs will slow attacks on American IP.

The other key weapon in Chinese predation is access to its home market, which is limited by regulations, subsidies, fines, and informal boycotts. The US has rejected reciprocity as a response, since mirroring the PRC means much higher consumer costs. An alternative involving market access and anticipating what will certainly be future aggression is to forbid Chinese participation in the most important supply chains serving the US, for example pharmaceuticals. The first, indispensable step is the hardest: the US must completely shut China out of just one chain, in law and in practice. Congress has as yet failed to identify what it sees as most

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[26] US House Representative Rosa DeLauro, "DeLauro, Fitzpatrick, Pascrell Reintroduce Bipartisan National Critical Capabilities Defense Act," press release, May 9, 2023, https://delauro.house.gov/media-center/press-releases/delauro-fitzpatrick-pascrell-reintroduce-bipartisan-national-critical#:~:text=%E2%80%9CThe%20bipartisan%20National%20Critical%20Capabilities,chain%20manufacturing%20here%20at%20home.

[27] US Department of Commerce, Bureau of Industry and Security, "Commerce Control List: Controls on Certain Marine Toxins," Federal Register 87, no. 99 (May 23, 2022): 28332–43, https://www.federalregister.gov/documents/2022/05/23/2022-10907/commerce-control-list-controls-on-certain-marine-toxins.

[28] Han-Shin Park, Sul-Gi Lee and Jeong-Soo Hwang, "Us Eyes New Rules for Samsung, SK to Bring Chip Machines to China," The Korea Economic Daily, May 10, 2023, https://www.kedglobal.com/business-politics/newsView/ked202305100019.

important, while the administration identified too much in early 2022 and has done little since.[29]

If and when supply chain policy is actually implemented, the next set of actions will concern data. In addition to our own domestic considerations, the PRC's own data regime is still being fleshed out and the challenges to American companies and decision-makers are still taking shape. But data coercion is already happening and will be an issue for the indefinite future.

In sum,

1) Do not permit US investment in China in technologies China cannot acquire here.
2) Set aside profit-seeking and implement export controls, for the sake of national security.
3) Sanction the centrally-controlled SOEs that have benefited most from IP coercion.
4) Shut China out of a vital supply chain, such as pharmaceuticals.
5) Prepare for sustained Chinese data mercantilism.

[29] Many agency recommendations, little follow up: White House, "The Biden-Harris Plan to Revitalize American Manufacturing and Secure Critical Supply Chains in 2022," February 24, 2022, https://www.whitehouse.gov/briefing-room/statements-releases/2022/02/24/the-biden-harris-plan-to-revitalize-american-manufacturing-and-secure-critical-supply-chains-in-2022/.

Mrs. KIM OF CALIFORNIA. Thank you, Dr. Scissors.

I now recognize Mr. Reynolds for your 5-minute opening statement.

STATEMENT OF MATTHEW REYNOLDS, FELLOW, ECONOMICS PROGRAM, CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES

Mr. REYNOLDS. Thank you, Chairwoman Kim, Ranking Member Bera, and distinguished members of the subcommittee. It is an honor to be here today, and I look forward to discussing this important topic with you all.

I have been asked to talk today about our recent CSIS economics program report entitled Deny, Deflect, Deter: Countering China's Economic Coercion. China's economic coercion carries real costs for the firms and sectors that find themselves down range of Beijing's bullying tactics. The threat of coercion can deter allies and partners from pushing back against Beijing's malign behavior in other domains, whether that be human rights violations in Xinjiang or the suppression of democracy movements in Hong Kong.

That said, China's use of economic coercion carries costs for Beijing, too. Therefore, a well-informed counterstrategy presents an opportunity for the United States to exploit Beijing's missteps and assert leadership on the global stage while also enhancing our soft power.

In our report, we looked at eight prominent cases of Chinese economic coercion that spanned approximately the past 13 years. Although each instance of Chinese economic coercion is unique, common patterns and characteristics emerged across the cases examined. We detail several of those characteristics in our report, but I will briefly go over three of the most salient here.

First, China displays a preference for implementing its course of measures through informal means. This provides Beijing some plausible deniability.

Second, Beijing prefers to target items in which it enjoys an asymmetric advantage in the structure of trade.

And, third, China displays a cost and risk aversion. This complicates its ability to inflict a significant economy-wide cost on the countries it targets.

Our most surprising finding, however, was just how ineffective China's economic coercion was. Across the cases, Beijing had only mixed results at achieving its short-term goals, and in fact Beijing's bullying often carried long-term strategic costs for China as well.

Take Australia's experience, for example. Despite restrictions on its wine, coal, and some agriculture products, Canberra has refused to back down in its efforts to counter Chinese interference in its domestic politics and in its calls for an investigation into the origins of COVID–19.

In fact, Canberra has only been pushed into greater strategic alignment with the United States since China's bullying began, signing onto the AUKUS security agreement in 2021.

Australia's case also highlights another interesting finding from our report. That is that China's economic coercion intersects with U.S. interests in a more counterintuitive way than one might at first expect. China's economic coercion certainly works against U.S.

interests in the obvious ways, in that it challenges the rules-based international economic order, divides allies and partners, and makes it more difficult for the United States to build coalitions to push back against China's malign behavior in other domains.

However, at the same time, China's economic coercion can actually work with U.S. interests by driving trade diversification, harming China's global image, and pushing targets closer to the United States, again, as we saw in the case of Australia.

That is not to say that China's economic coercion should be tolerated. A world free from China's economic coercion is preferable to one where the thread of coercion looms over the decisionmaking of sovereign nations. Therefore, based on these key insights from our report, we recommend a counterstrategy which aims to deter China's economic coercion by building resilience and providing relief to targeted allies and partners.

The United States can help countries build resilience in two primary ways, the first being through the negotiation of free trade agreements that offer signatories real market access, and the second by preemptively helping to identify the mitigate countries' vulnerabilities to China's economic coercion. The ongoing supply chain resiliency initiatives that have emerged in the wake of COVID–10 offer logical platforms in which to embed these efforts.

When China does coerce, the United States should be ready to quickly provide relief to targeted countries. The United States has several existing tools it could use to do so, such as export financing, temporary tariff relief, and sovereign loan guarantees, to name a few. We also recommend augmenting this toolkit with the creation of a new coercion relief fund.

The counterstrategy should also be embedded in a larger diplomatic messaging campaign, which draws attention to U.S. efforts to build resilience and provide relief to targets while also shaming China for its bullying behavior. The United States should also seek to multilateralize its response by encouraging allied countries to adopt similar strategies.

It is, therefore, encouraging to see reports this week that the G7 is discussing how to jointly counter China's coercion. In this way, the United States can mitigate the cost of coercion for allies and partners, further reduce the effectiveness of China's bullying, and over time demonstrate to China the futility of its actions.

Thank you, and I look forward to your questions.

[The prepared statement of Mr. Reynolds follows:]

CSIS | CENTER FOR STRATEGIC & INTERNATIONAL STUDIES

Statement before the House Foreign Affairs Subcommittee on the Indo-Pacific

"Standing United Against the People's Republic of China's Economic Aggression and Predatory Practices"

A Testimony by:

Matthew Reynolds
Fellow, Economics Program,
Center for Strategic and International Studies (CSIS)

May 18, 2023
U.S. Capitol, HVC-210

Chairwoman Kim, Ranking Member Bera, distinguished Members of the Subcommittee, thank you for inviting me to testify at today's hearing entitled "Standing United Against the People's Republic of China's Economic Aggression and Predatory Practices." It is an honor to be here, and I look forward to sharing my thoughts on this important topic.

My testimony today will focus on summarizing and highlighting key findings and insights from a recent CSIS Economics Program report on China's economic coercion. I will conclude with some thoughts on how the United States can use our findings to inform a U.S.-led counterstrategy that advances U.S. interests, mitigates the costs of China's economic coercion to U.S. allies and partners, and deters China's economic bullying. My comments today are my own and should not be attributed to the Center for Strategic and International Studies.

Introduction

Since reform and opening, and especially after its entry into the World Trade Organization (WTO), China has experienced rapid economic growth, going from one of the world's poorest nations to the world's second-largest economy in approximately four decades. While lifting hundreds of millions of Chinese citizens out of poverty, China's rapid development and integration into the world economy has also provided Beijing the opportunity to weaponize its vast market to advance its geopolitical interests. Indeed, Beijing's use of economic coercion[1] is fast becoming a favorite foreign policy tool of the Chinese Communist Party.[2]

China's use of economic coercion challenges U.S. interests. Not only is it costly for targeted firms and sectors, it also undermines the norms and rules of the international economic system that have enabled decades of global economic growth, and which, paradoxically, have also contributed positively to China's own remarkable growth. In addition, China's economic coercion divides U.S. allies and partners as firms and producers in other allied countries at times awkwardly stand to benefit from the targeted ally's pain. Likewise, the threat of economic coercion arguably makes it more difficult for the United States to build coalitions to push back against Beijing's malign behavior in other domains as ally and partner governments may fear Beijing's economic retribution.

That said, it is important that China's economic coercion also be viewed with a sense of perspective. Although problematic, China's economic coercion has a decidedly mixed record at achieving its short-term goals, and more often than not, carries long-term, strategic costs for Beijing. Counter-intuitively, China's bullying behavior can actually also work in favor of U.S. interests by driving trade diversification, harming China's image around the world, and pushing targeted countries into greater policy alignment with the United States. A counterstrategy informed by a nuanced understanding of China's use of economic coercion therefore presents an opportunity for the United States to not only counter but also exploit China's bullying to our own advantage.

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[1] Daniel Drezner defines economic coercion as a "threat or act by a sender government or governments to disrupt economic exchange with the target state, unless the target acquiesces to an articulated demand." https://www.jstor.org/stable/3594840

[2] https://www.axios.com/2023/02/21/economic-coercion-chinas-foreign-policy-tool

Economic Coercion with Chinese Characteristics

In March 2023, the CSIS Economics Program published a research report on China's economic coercion entitled, *Deny, Deflect, Deter: Countering China's Economic Coercion*.[3] In the report, the program examined eight cases of Chinese economic coercion, spanning approximately the last 13 years. Those cases—Japan (2010), Norway (2010), the Philippines (2012), South Korea (2016), Mongolia (2016), Australia (2017/2020), Canada (2018), and Lithuania (2021)—reveal certain patterns and characteristics of China's distinct brand of economic coercion.

China's use of economic coercion appears to be triggered by a challenge to one or more of five People's Republic of China's (PRC) interests: threats to territorial integrity, domestic political legitimacy, national security, economic security, and/or PRC citizens. Although not every infraction triggers a response from Beijing, when Beijing does decide to deploy coercive economic measures, it prefers to do so in an informal manner. This informality, on the one hand, may be in part due to China's lack of more formal tools, but on the other hand, it also importantly provides Beijing with a degree of plausible deniability in its actions. The case of China's import restrictions on Philippine banana's imports is illustrative.

During the 2012 dispute with Manila over the Scarborough Shoal, China masked its restriction of Philippine banana imports behind phytosanitary and sanitary concerns asserting that Philippine bananas were contaminated with mealybugs. The targeting of Philippine bananas also reveals another distinctive characteristic of China's economic coercion: China attempts to target items not just for their economic impact but also for their political and symbolic importance. Much of the Philippine banana production takes place on the island of Mindanao, an important region politically and home to former Philippine president, Rodrigo Duterte.[4]

Across the studied cases, Beijing simultaneously deployed other coercive tools alongside its coercive economic measures, including nonviolent military and paramilitary coercion, hostage diplomacy, diplomatic sanctions, and cyber-attacks. Again, against the Philippines, China deployed coast guard vessels to the Scarborough Shoal, cut off formal contact with the Philippine foreign ministry for two years, and targeted the University of the Philippines, the Department of the Budget and Management, and the Philippines News Agency with cyber-attacks. Although China did not engage in hostage diplomacy during the Scarborough Shoal dispute, Australia, Canada, and Japan all saw citizens arbitrarily detained after drawing the ire of Beijing.

China also demonstrates a preference for targeting items in which it enjoys an asymmetric advantage in the trading relationship. For example, when China blocked imports of Australian coal in 2020, Australia was sending approximately 20 percent[5] of its coal exports by value to China, whereas China not only had access to other coal suppliers but also only had an import dependency of around 10 percent for coal.[6] Likewise, when China cut off rare earth exports to Japan in 2010, Japan depended on China for nearly 90 percent of its rare earth imports. And when China curtailed

[3] https://www.csis.org/analysis/deny-deflect-deter-countering-chinas-economic-coercion
[4] https://www.ft.com/content/3f6df338-056b-11e7-ace0-1ce02ef0def9
[5] https://oec.world/en/profile/country/aus?depthSelector1=HS6Depth&yearSelector1=2018
[6] https://www.iea.org/data-and-statistics/charts/oil-gas-and-coal-import-dependency-in-china-2007-2019

tourism outflows to South Korea in 2017, Chinese tourists accounted for roughly half of South Korea's overseas tourist arrivals.[7]

China's preference for asymmetry reflects its absolute economic size and is accompanied by an aversion to incurring domestic costs. After African Swine Fever decimated China's domestic hog herds, Beijing dropped restrictions on Canadian pork imports which had been put in place after Canada detained Huawei CFO, Meng Wanzhou. Likewise, Beijing avoided restricting Australian iron ore imports, which would have had deleterious downstream impacts on its own economy in its dispute with Canberra over the origins of Covid-19. Perhaps unsurprisingly then, China also opted not to interfere with a $7 billion investment by Samsung in its Xi'an facilities, nor did it target Lotte's petrochemical operations[8] during the dispute with Seoul over the installment of the Terminal High Altitude Area Defense (THAAD) system despite shutting down almost all of the Korean firm's supermarket stores in China – for which, conveniently, domestic competitors existed.

An aversion to incurring costs domestically is mirrored by an unwillingness, or perhaps inability, to impose significant costs on the targeted countries at the macroeconomic level. This is despite the significant size advantage China typically enjoys over its targets. Indeed, with the exception of Japan,[9] China displayed a preference across cases for targeting much smaller economies—Mongolia and Lithuania together do not even equal one percent of China's GDP. Although China's coercive measures can be expensive for the specific firms and sectors targeted—it is estimated that Lotte lost $1.78 billion due to China's restrictions—in many cases initial losses are offset with gains in third markets. For example, although Australia saw a reduction of $4 billion in trade with China, this was accompanied by a $3.3 billion increase in exports to new markets. The resulting net loss of $700 million represented just 0.25 percent of the value of Australia's total exports.

While potentially painful at the firm level, without the ability or willingness to inflict significant economy-wide costs, China's economic coercion has proven to be quite ineffective. In perhaps the most surprising finding from the study, China has only had mixed success at achieving its short-term, tactical goals, and even when it does achieve its short-term goals, its use of economic coercion often carries long-term, strategic costs for Beijing. In the case of Australia, for example, China's restrictions on Australian wine, coal, and agriculture exports did not result in any significant policy changes in Canberra and have only pushed Australia into closer strategic alignment with the United States. The inking of the AUKUS security agreement in 2021 is emblematic of this stronger alignment.

The ineffectiveness of China's economic coercion can be linked to many of its aforementioned intrinsic characteristics. Informality is a double-edged sword. It can provide plausible deniability, complicating the targeted state's response. However, it also makes it more difficult for China to enforce its economic sanctions. This means targeted items often still find their way into China, mitigating costs for the targeted country. At the same time, without a network of allies, China lacks

[7] https://www.forbes.com/sites/ralphjennings/2018/03/04/china-keeps-punishing-south-korea-with-tourism-cuts-for-now/?sh=67a5dd4366c4
[8] https://www.tandfonline.com/doi/pdf/10.1080/09692290.2021.1918746
[9] Japan is also unique as it is the only case surveyed where China relied on export restrictions, rather than import restrictions, as the primary coercive economic tool.

the ability, or at least the willingness, to multilateralize its coercive measures to prevent trade adjustment from offsetting costs for the target. Its preference for targeting commodities that are substitutable makes stopping this even more difficult. Likewise, advanced market economies are generally more robust to external shocks than poorer, non-market economies, while China's failure to credibly couple inducements alongside its coercive measures undermines incentives for targets to acquiesce to Beijing's demands.

Norway's experience with Chinese economic coercion highlights many of these weaknesses. Beijing blocked imports of Norwegian salmon on sanitary and phytosanitary grounds following the Oslo-based Nobel Peace Prize Committee's decision to award Chinese dissident Liu Xiaobo the Nobel Peace Prize in 2010. However, Norwegian salmon still found its way into China via Vietnam, with exports to that Southeast Asian nation increasing 17-fold. As a result, the economic impact of the restrictions on Norway was found to be "negligible."[10] Instead, it seems that Norway's moves to normalize relations were more motivated by the opportunity to restart negotiations on a Norway-China Free Trade Agreement. However, these negotiations again broke down in 2022.

Why Does China use Economic Coercion?

If China's economic coercion is so ineffective, why does China continue to do it? There are a couple possible explanations. First and foremost, there is likely a deterrent effect that China perceives it gains from punishing countries that violate certain interests. In making an example of violators, China is sending a message to other countries that crossing Beijing on certain issues is not cost free. While acknowledging this deterrent effect is likely to exist, it is difficult to quantify how substantial it is. At the same time, there exists examples where the threat of economic coercion has not deterred states from taking positions that cross traditional triggers of China's economic coercion, such as the European Union's increasing diplomatic activity with Taiwan.[11]

Another consideration driving Beijing's use of economic coercion may be propriety. That is, China as a great power, and a nation that views itself historically as the preeminent power in Asia, if not the world, cannot be seen to suffer slights from adversaries. A response is necessary, even if it carries costs for China, too. Relatedly, evidence has been put forward showing that China may see economic coercion as less escalatory than other coercive tools in the military domain. Taken together, this would help explain China's preference for targeting smaller countries with its economic coercion. A slight from a smaller country is both a greater insult, and all else equal, meting out economic punishment against a smaller country is less likely to result in escalation. In that way, China can be conceptualized as a "cautious bully."[12]

Looking ahead, Beijing's use of economic coercion is likely to continue. Through its Dual Circulation Strategy, Beijing hopes to enhance its position in the global economy, deepen its resilience to external shocks, and gain economic leverage over its trading partners by diversifying its supply chains and boosting domestic consumption. At the same time, China has grown more

[10] https://qz.com/1000541/norway-wants-china-to-forget-about-the-human-rights-thing-and-eat-salmon-instead
[11] https://ceias.eu/beyond-the-dumpling-alliance/
[12] https://direct.mit.edu/isec/article-abstract/44/1/117/12241/Cautious-Bully-Reputation-Resolve-and-Beijing-s?redirectedFrom=fulltext

nationalistic. The Party's sensitivity to challenges to its "core interests"—especially its One-China Principle—will likely increase. Assuming China's power increases, Beijing will become even less tolerant of slights from other states. Assuming geopolitical tensions between both the United States and China continue, a risk-averse Beijing will continue to prefer economic, rather than more escalatory military tools, in its efforts to coerce other states.

China's coercive tactics are likely to evolve along with its economic power. First, Beijing is likely to expand its economic toolkit to include a greater suite of formal coercion measures such as the Unreliable Entity List, the Export Control Law, and Anti-Foreign Sanctions Law. While it is possible this formalization could undermine China's plausible deniability, it could also enhance enforcement and provide firms operating in Beijing more clarity. Second, Beijing also seems likely to continue to use economic coercion in conjunction with non-economic coercive tools, including shows of force by the People's Liberation Army (PLA). Third, China might become more comfortable in challenging the policies of larger countries, including the United States, which it has previously been reluctant to challenge.

Indeed, recent reports of China's scrutiny of U.S. consultancies, Bain[13] and Mintz,[14] as well as the U.S. semiconductor firm, Micron,[15] has led some to question whether these moves are Beijing's retaliation against the United States for the October 7, 2022 export controls placed on high-end semiconductors and the manufacturing equipment needed to produce them by the Biden administration.[16] However, the harassment of these firms may also emanate from China's increasing suspicion of the United States and its drive for self-reliance more generally. Either way, these moves are also likely to carry costs for China, especially as it sends signals to foreign firms contradicting Beijing's claims that China welcomes foreign investment.

Toward a U.S. Counterstrategy

Based on the case study findings, we put forward a counterstrategy based on the logic of deterrence by denial.[17] The counterstrategy consists of two mutually reinforcing components: a proactive "resilience" component and a reactive "relief" component. Together these components will enable the United States to mitigate the costs of China's economic coercion for targeted allies and partners, speed market adjustments away from China, and increase the costs of exercising economic coercion for Beijing, while at the same time further undermining the tactic's effectiveness. Over time, the counterstrategy aims to demonstrate to Beijing the futility of its actions, forcing a reassessment of the utility of targeting U.S. allies and partners with coercive economic measures.

The United States can help allies and partners proactively build resilience to China's economic coercion in two primary ways. First, the United States can work to assist allies and partners in identifying potential vulnerabilities to China's economic coercion. The ongoing supply chain

[13] https://www.nytimes.com/2023/04/27/business/bain-china.html
[14] https://www.reuters.com/world/us-due-diligence-firm-mintz-groups-beijing-office-raided-five-staff-detained-2023-03-24/
[15] https://www.nytimes.com/2023/04/04/business/micron-china-investigation.html
[16] https://www.reuters.com/world/eu-ambassador-china-says-chinas-anti-espionage-law-not-good-news-2023-05-09/
[17] Deterrence by denial seeks to deter an adversary not so much from instilling in them a fear of punishment but rather a fear of failure and its associated costs.

resiliency initiatives which have emerged in the wake of the Covid-19 pandemic offer logical platforms in which to embed these assessments and coordinate efforts to mitigate vulnerabilities. Second, resiliency can be enhanced through the negotiation of free trade agreements that offer real market access to signatories. China has been expanding its presence in multilateral free trade agreements, with Beijing applying for membership in the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) in 2021 and the Regional Comprehensive Economic Partnership (RCEP) going into effect last year. Engaging in free trade agreements will not only help to offset China's growing global trade influence, but also make it easier for markets to adjust in response to China's economic coercion.

When coercion does take place, the United States should be ready to offer quick relief[18] to targeted allies and partners to mitigate economic costs and reduce political pressure affected firms and sectors may be placing on the targeted government. The United States has a number of existing tools that it could deploy to aid a targeted government in such a scenario. These include, but are not limited to, export financing, sovereign loan guarantees, and temporary tariff reductions. In addition, the United States should also consider creating a coercion compensation fund, which could be used to transfer funds to the targeted country to help offset costs, especially those associated with finding new markets or suppliers. These tools should be bundled together on a case-by-case basis depending on the specific characteristics of an instance of China's economic coercion. For example, it likely would not make sense to provide export financing to speed U.S. exports to a targeted country if that country is facing restrictions on its exports to China. In such a case, reducing U.S. tariffs on the targeted item would be more appropriate.

It is unlikely that these relief tools would have to be very expensive for the United States. As the case studies show, China has largely been reluctant or unable to inflict significant costs on the targeted countries. In addition, the goal of U.S. relief should not be to completely offset the entire cost incurred by targets, as that could create a moral hazard where firms are not accurately pricing in the risks of doing business in China. Instead, relief should be focused on speeding the market adjustments that are already taking place naturally in the face of China's economic coercion. For example, Canada provided just C$19 million in relief to its agriculture producers in the wake of China's import restrictions. This amount, combined with increased exports to new markets, proved sufficient, as Ottawa never caved to Chinese pressure. It also suggests that U.S. relief would be augmenting relief provided by targeted governments to their own domestic industry. Indeed, the United States should be encouraging its allies and partners to adopt similar counter coercion authorities. The G7 is a logical place to start and can serve as a platform for coordinating multilateral relief, enhancing the quality and amount of relief flowing to a targeted country.

Both the resilience and relief components of the counterstrategy should also be embedded in a larger diplomatic messaging campaign. First, the United States can draw attention to China's bullying tactics, the U.S.-led efforts to build resiliency, and the ineffectiveness of China's past usage of economic coercion. In doing so, the United States can increase the reputational costs for China, while also eroding the deterrent effect of China's threats of economic coercion and altering Beijing's calculus around the future use of economic coercion. Second, if China begins to coerce an ally country, the United States should seek to signal that relief is coming, rally multilateral

[18] Speed of reaction is important because sanctions are likely to bite the most before market adjustments can take place.

support, and join WTO cases if possible. Together, this should help the targeted government stand up to Beijing until the relief arrives.

Conclusion

China's economic coercion carries real costs for the firms and sectors that find themselves downrange of China's coercive measures. Likewise, the threat of China's use of economic coercion likely has some level of deterrent effect, possibly preventing countries from standing up to Beijing's malign behavior in other domains, whether that be human rights violations in Xinjiang or the suppression of democracy movements in Hong Kong. However, a careful review of eight cases of Chinese economic coercion by the CSIS Economics Program reveals a tactic that carries real costs for Beijing as well. With a well-informed counterstrategy, China's economic coercion can therefore be mitigated, if not deterred. This can be done in a way that primarily makes use of market forces to speed trade adjustments and provide relief to targeted countries. Over time, as it comes to be seen that economies prove themselves more resilient to China's coercive measures, the deterrent effect that China had received from its threat of economic coercion will likewise be eroded. In addition, by focusing on building resiliency and providing relief to allies and partners, countering China's use of economic coercion provides the United States the opportunity to assert leadership on the global stage and enhance its soft power vis-à-vis China.

Mrs. KIM OF CALIFORNIA. Thank you, Mr. Reynolds.

I now recognize Mr. Feith for your 5-minute opening statement.

STATEMENT OF DAVID FEITH, ADJUNCT SENIOR FELLOW, CENTER FOR NEW AMERICAN SECURITY

Mr. FEITH. Thank you. Chairwoman Kim, Ranking Member Bera, and members of the subcommittee, it is a privilege to testify today.

My testimony has three purposes. First is to define the problems of China's economic coercion. This is an enormous challenge for U.S. foreign policy and national security. The harm we face is broader than the bullying of individual countries in a handful of cases.

Economic coercion is central to Chinese leader Xi Jinping's grand strategy. Collecting and exploiting leverage over foreign targets is how Xi approaches the outside world. It has helped him perpetrate genocide in Xinjiang with impunity. It is part of why he may feel confident enough to invade Taiwan and discount the risks of world war.

In the coming years, China wants to become a kind of super OPC, controlling key world economic supplies as leverage over all of us. These are the stakes.

My second purpose is to suggest how the United States and our allies should counter China's strategy of economic coercion. Much of the debate on this matter has focused on mitigating the harm done to victims of China's policies. We should also seek to deter China by imposing costs on its coercive behavior. To do this well, however, U.S. and allied policymakers need to know more about relative strengths and weaknesses in our economic relationships with China. We can improve our knowledge by launching a 301-style investigation in Washington, akin to the effective 301 investigation into Chinese unfair trade practices undertaken in 2017/2018.

The U.S. could also lead, perhaps via the G7 or AUKUS, in the creation of a standing multilateral body for studying these issues together with allies. Most of all, we should limit U.S. and allied exposure to Chinese coercion in the first place by limiting trade with China in strategic areas. It is important to ensure that the U.S. and allied balance of dependence with China, especially in key technologies, continues to favor us.

My third purpose is to warn that current U.S. policies are increasing America's exposure to economic predation by China. We have important environmental interests, for example, but increasing our reliance on Chinese solar panels and Chinese components for electric vehicles is dangerous. It creates national security perils similar to those that Germany inflicted on itself by becoming dependent on Russian energy in the years before the Ukraine war.

My written testimony has more details on all these matters. For now, I will note further that this challenge is unprecedented in our history. The United States has never faced a geostrategic rival with as much economic coercive power as Beijing wields today, let alone the economic coercive power that Beijing credibly seeks to wield in the future.

The Communist party's goal is to decrease China's dependence on high-tech imports from other countries while making other countries more dependent on imports from China, especially for critical technologies. The aim is to maximize global economic leverage for future coercive use. It bears repeating: the goal is for China to become a super OPEC of the 21st century, a single country that decisively controls crucial economic inputs for the world economy.

Policymakers should constrain these aspirations now, first, through coordinated deterrence; second, through strict limits on China's access to technology, capital, and data controlled by the United States and our allies. We should not wait until China has taken fateful steps, such as attacking Taiwan, that could lead to superpower conflict.

We and our allies require a strategy of constrainment to counter China's economic coercion. This strategy would take note of the realities of economic interdependence and aim to adjust them to serve Western security interests. Constrainment can provide deterrence, working to deflate the confidence of Chinese leaders that they can achieve their aims through aggression and war.

We do not want Chinese leaders to feel optimistic about their coercive economic leverage over us and our friends. The new U.S. and allied export controls on semiconductor technology are a step in the right direction. If enforced diligently, the rules could foil China's ambition to make itself a home for advanced chip manufacturing. They can ensure that China remains dependent on the United States and our allies for these critical supplies.

While we are at it, U.S. and allied policymakers should not ignore so-called mature semiconductor production. We do not want China to dominate the global production of chips needed for lower end electronics such as cars and critical infrastructure systems either.

Constrainment should strive to maintain a favorable balance of dependence in a wide range of areas. It should, for example, strengthen the dominance of the U.S. dollar as a global reserve and trading currency, extending Washington's ability to monitor and punish money laundering, weapons proliferation, bribery, and other dangerous actions by Beijing.

Constrainment should remind China of its dependence on foreign sources of food and energy while reversing our growing reliance on Chinese batteries, solar panels, and other green technology. The green technology point is especially crucial because trend lines appear to be moving fast in the wrong direction.

As Washington subsidizes solar energy, electric vehicles, and other renewable technologies, are we protecting against the risk of growing dependency on China? Failure to do so would be grave strategic neglect.

National Security Advisor Jake Sullivan recently gave a speech underscoring the importance of both greening U.S. energy supplies and limiting "dependencies that could be exploited for economic or geopolitical leverage." Yet there appears to be little in current policy or in the language of the Inflation Reduction Act, or other such bills, to ensure that we are protecting ourselves properly.

We should reduce risks that U.S. subsidies and green energy targets give greater coercive power to China. We should carefully review the downsides of Chinese renewables exports into the U.S. energy market.

Let's draw on the wisdom of the Hippocratic Oath. China already has enormous——

Mrs. KIM OF CALIFORNIA. Sir, your time is up.

Mr. FEITH. Thank you.

Mrs. KIM OF CALIFORNIA. And we will make note that your full written testimony is in the record.

[The prepared statement of Mr. Feith follows:]

David Feith
Adjunct Senior Fellow, Center for a New American Security
Former Deputy Assistant Secretary of State for East Asian and Pacific Affairs

Testimony before the U.S. House Committee on Foreign Affairs
Subcommittee on the Indo-Pacific
"Standing United Against China's Economic Aggression and Predatory Practices"

May 18, 2023

Chairwoman Kim, Ranking Member Bera, and members of the Subcommittee – thank you for the opportunity to testify today. My testimony has three purposes:

> 1. First is to outline China's strategy of economic coercion. This is a central element in Chinese leader Xi Jinping's grand strategy. Collecting and exploiting leverage over foreign targets is how Xi approaches the outside world. The challenge this poses for us is much broader than the case-by-case bullying of individual countries. It is a vital but insufficiently recognized motive for the economic ties that China cultivates around the globe. Xi continually stresses that no Chinese business connection is simply or merely commercial.
>
> 2. My second purpose is to suggest how the United States and our allies should counter China's strategy of economic coercion. Much of the debate on this matter has focused on mitigating the harm done to victims of China's policies. We should also seek to deter China from bullying by imposing costs on its coercive behavior. Most of all, we must limit U.S. and allied exposure to Chinese coercion in the first place by limiting trade with China in strategic areas.
>
> 3. My third purpose is to warn that current U.S. policies are increasing America's exposure to economic predation by China. The United States has important environmental interests, for example, but increasing our reliance on Chinese solar panels and Chinese components for electric vehicles is dangerous. It creates national security perils similar to those Germany inflicted on itself through becoming dependent on Russian energy. Our first principle should be to do no harm to ourselves.

—

1. Economic Coercion is Xi Jinping's Grand Strategy

How does China under Xi Jinping practice economic coercion, and why is it a problem?

Defined simply, economic coercion is a government's use of economic power to pressure another government to change behavior. It is common for governments do it, certainly including the United States. What China is doing, however, is unprecedented in our history. The United States has never faced a geostrategic rival with as much economic coercive power as Beijing wields today and credibly seeks to wield in the future.

There are some well-known examples of China's economic coercion over the last decade. China curbed exports of rare earth minerals to Japan to influence a territorial dispute. China let Philippine bananas rot at port to influence another territorial dispute. China blocked South Korean exports after Seoul deployed U.S. missile defenses. China has limited trade and diplomatic contact with countries that hosted the Dalai Lama. China banned imports of Australian goods after Canberra enacted laws to counter foreign interference and called for an investigation into the origin of Covid. China halted trade with Lithuania to punish its expanded ties with Taiwan.

These examples of Beijing's coercion are important, but they fail to convey the magnitude of this issue or its centrality to the future of peace and prosperity in the world. China's strategy of coercion is not just a challenge occasionally affecting countries and sectors randomly across the map. Nor does it simply reflect Beijing's "Wolf Warrior" diplomatic excesses of the moment.

Rather, economic coercion is a vital mechanism in Chinese strategy under Xi Jinping. It is fundamental and pervasive. China practices it every day and globally – including against the United States, and already with significant success.

Chinese leaders declare openly that they are using China's market and supply-chain power as leverage over trading partners and a means to impose their will in the world. In its Five-Year Plan published in 2021, the Chinese Communist Party laid out a geoeconomic strategy for exploiting what it called the "powerful gravitational field" of the Chinese economy.

This built on a pair of speeches in 2020 in which Xi called for economic "deterrence" power and "self-reliance". Xi said China "must sustain and enhance our superiority across the entire production chain." He also said China "must tighten international production chains' dependence on China, forming a powerful countermeasure and deterrent capability against foreigners who would artificially cut off supply."

Chinese officials call their policy "dual circulation," a clunky reference to prioritizing consumption of domestic goods (internal circulation) over dependence on foreign markets (external circulation). The goal could more plainly be called "offensive leverage." Beijing aims to decrease China's dependence on high-tech imports from other countries while making other countries more dependent on imports from China, especially for critical technologies. The purpose is to maximize global economic leverage for future coercive use.

None of this would be too unusual or problematic if not for China's size and the nature of its regime: deeply hostile to the United States and our allies, ambitious to subjugate Taiwan and rewrite global order by force if necessary, and demonstrably successful at accumulating economic coercive power through techno-industrial policy. The more central Beijing gets to international trade and global supply chains, the more economic coercive power it husbands, the more likely it is to confront us and our allies and risk world war over Taiwan.

Beijing's aspirations may be greater than what it can realistically accomplish. But Xi Jinping, like his friend Vladimir Putin, does not seem to believe that his reach exceeds his grasp. Policymakers around the world should take note.

It would be better to constrain and temper Xi's aspirations now – through coordinated deterrence and strict limits on China's access to technology, capital, and data controlled by the United States and its allies – rather than wait until he has taken fateful and irrevocable steps, such as attacking Taiwan, that could lead to superpower conflict. Understanding Beijing's economic coercion strategies, and beginning to counter them more effectively, is a necessary step.

2. A View from the State Department

When I served at the State Department, from 2017 to 2021, official discussions of Chinese economic coercion were still generally in their infancy.

U.S. policy in those years was productively exploring a wide range of economic-policy tools that Washington had long failed to apply effectively (if at all) toward China. These included tariffs, export controls, sanctions, inbound and outbound investment restrictions, cross-border data restrictions, and more. But when it came to countering Beijing's economic coercion, our efforts were mostly focused on identifying the problem, calling it out publicly, and establishing a foundation of common understanding on which U.S. and allied policy countermeasures could be built.

In July 2020, State Department Assistant Secretary Dave Stilwell used an address on the South China Sea to observe that Beijing's coercive activities had become a global scourge affecting governments, people and industries far beyond Southeast Asia:

> *A few years ago, many believed that Beijing's South China Sea abuses were mostly a local phenomenon, a kind of limited indulgence for a rising power finding its way in the world. Today we know that the Chinese Communist Party's neo-imperial ways aren't incidental to its character but are an essential feature of a nationalist and Marxist-Leninist mindset. Beijing wants to dominate its immediate neighborhood – and eventually impose its will and its rules on your neighborhood too, wherever you may be.*

> *You could be a university student in Australia, a book publisher in Europe, or the general manager of an NBA franchise in Houston. You might work for an international hotel chain, a German car company, or a U.S. airline. You could be a 5G customer in Britain – or anywhere else in the world. Wherever you are, Beijing increasingly wants to stake claims, coerce, and control. By its nature, it cannot accept a pluralistic world with fundamental freedoms of choice and conscience.*[1]

By late 2020, some U.S. and allied officials had begun informal discussions of the need to push back collectively on Beijing's economic coercion, possibly through an "Economic Article 5" mechanism on the NATO model. These discussions picked up especially after Beijing's coercion of Australia intensified in April 2020. But in those initial months they could only advance so far.

3. Institutionalizing Economic Deterrence

Today the U.S. and allied conversation has matured, as demonstrated by this hearing and a range of other initiatives. At the end of this week, President Biden and G-7 leaders meeting in Japan are expected to issue a special statement condemning economic coercion (though China may not be mentioned by name). Here in Congress, several relevant bills are under consideration, including the "Countering Economic Coercion Act" of Senators Coons and Young. In Brussels, the European Union has been working since 2021 on an "anti-coercion instrument" that recently won provisional political agreement from member states.[2]

To date, in dealing with Chinese economic coercion, U.S. and allied policymakers have mostly focused on ways to cushion the blow for victims, in hopes of making them less likely to bow to Beijing's will. Proposed measures to aid Beijing's victims have included export credit, sovereign loan guarantees, political risk insurance, reduced tariff barriers, and even direct funding to buy certain coercion-affected goods. Such allied-support measures are worth considering.

But it is important to recognize that Beijing will not likely be deterred unless it also faces the credible threat of costs for its economic aggression. U.S. and allied policymakers should consider how penalties can be readied so that China can be deterred.

To be sure, the Coons-Young bill includes authorities to "increase duties on imports from foreign adversaries committing economic coercion."[3] That's a start.

But do U.S. officials know with confidence which import duties would impose the most harm on Beijing while minimizing costs to us? The same question applies to export restrictions – and to restrictions on the flows of capital and technology. We aren't used to thinking in such mercantilist terms, neither unilaterally nor with allies. But we must have answers to these questions to counter China's economic coercion strategy.

Georgetown University's Victor Cha testified last week before the House Rules Committee, highlighting areas in which China depends heavily on imports from the United States, Japan, Australia and other countries that it has targeted for coercion:

> *The eighteen countries that are previous and current targets of Chinese economic coercion export over $46 billion worth of goods to China upon which the country is more than 70 percent dependent as a proportion of its total imports of those goods, and over $12 billion in goods upon which China is more than 90 percent dependent. These states can band together and practice economic deterrence by promising collective retaliation on these high-dependence goods should China act against any one member of the collective. . . .*
>
> *Collective resilience might sound too mercantilist for the ears of some liberals and globalists, but it's a necessary competitive strategy to protect the liberal international order.*

To be sure, all this is easier said than done (as Cha notes). There are complex considerations of law, policy, escalation risk, allied coordination and more. These complexities are why U.S. policymakers would benefit from more deliberate and robust mechanisms for studying these issues and readying appropriate policy tools.

One such mechanism could be an official investigation under Section 301 of the 1974 Trade Act into China's use of unfair coercive practices against U.S. (and allied) targets. This would follow on the broad 301 investigation into Chinese unfair trade practices undertaken by the U.S. Trade Representative in 2017-2018, which examined the issues, held public hearings, received expert testimony, documented findings, and teed up countermeasures.

A new 301-style investigation could elevate this issue internationally, contributing to deterrence while it is underway. It could impose a price on China for its coercive activities, helping Western policymakers understand what kind of response is appropriate. The evidentiary, policy innovation, and deterrence value of the exercise would be greater, of course, to the extent that allies are involved or pursue coordinated efforts of their own, perhaps beginning with the G7 plus Australia.

Western policymakers need a better understanding of the tools they have available. They should devise multilaterally, if possible, the policy structures needed for collective economic resilience and deterrence. They should consider creating a standing consultative body to institutionalize allied response to China's strategy of economic coercion. That body could perform long-term study, develop a common threat assessment, consider policy options, host exercises, etc. It can do for this Chinese economic strategic challenge what NATO did, starting in the late 1940s, for the Soviet military challenge of the Cold War.

4. Is China's Coercion Self-Defeating?

It is worth noting that there is debate over how successful China's economic coercion really is. The record is not uniform. Sometimes Beijing succeeds in cowing targets and winning notable concessions. Sometimes Beijing fails, causing targets to harden their positions and refuse concessions.

A recent Center for Strategic and International Studies (CSIS) report analyzed eight cases since 2010 and found that "the most salient characteristic of China's economic coercion is that it simply is not very effective."[4] Beijing was judged to have scored "wins" only in coercing Mongolia (about the Dalai Lama) and the Philippines (on South China Sea), while it suffered "losses" in coercing Japan (on rare earths), South Korea (on missile defense), Australia (on various matters), Canada (on Huawei) and Lithuania (on Taiwan). CSIS assessed the outcome in Norway (regarding Liu Xiaobo's Nobel prize) as "mixed."

This scorecard highlights interesting complexities in the exercise of economic coercion. Beijing sometimes finds its cards are weaker than anticipated. Target countries sometimes prove surprisingly resilient politically and adapt commercially by finding new markets other than China for their goods. China has learned that accumulating leverage can be easier than using it. When it generates fear and loathing among foreign governments and businesses, it spurs diversification away from the China market. That can diminish China's leverage with those targets in the future.

And yet.

China's record of economic coercion extends far beyond those eight cases. In fact, China exercises economic coercion every day, and has considerable success in doing so.

Consider the way the world deals with the Xinjiang situation. This is perhaps the largest and clearest example of the success of China's strategy of economic coercion. Multiple countries have condemned the Chinese government for perpetrating genocide against its own Uyghur Muslim citizens. But China has faced almost no consequence at all, neither in the sphere of diplomacy nor business. Its impunity testifies to its coercive economic power.

The same goes for Beijing's depredations in Tibet, Hong Kong, the South China Sea and beyond. China engages in behavior every day that not only violates the basic human rights of its own people, but abuses its neighbors, sometimes violently; disregards the sovereignty and other rights of foreign states and individuals around the world; and threatens the peace and prosperity of its region and beyond.

Ask the fishing boat captains from the Philippines whom Chinese forces have attacked. Ask the citizens of Sweden, Australia and elsewhere who have been kidnapped abroad and imprisoned in China for criticizing Chinese policies. Ask the businesses worldwide that have had their intellectual property stolen by Chinese hackers, spies and "talent plan" recruits. What price has China paid for these actions? The answer is nothing substantial. Again, the weakness of the response demonstrates that China's strategy of economic coercion is potent and successful.

Then there is Taiwan, which Beijing harasses through economic coercion aimed directly at it and also at other countries. This is designed to keep the island diplomatically isolated, militarily ill-defended and therefore a softer target.

If Beijing follows through on its credible threats to invade Taiwan, it will be driven in part by a calculus that enough countries would rather allow Beijing's takeover than risk the economic consequences of opposing it. Countries also fear Beijing's military might, of course, but economic factors would be a key consideration for policymakers in many countries. When analysts note amid the economic disruptions of the Ukraine war that China has 10 times the economic power (and global interconnectedness) of Russia, that signifies that China's strategy of economic coercion is a powerful reality.

Such is China's multifaceted economic coercive power today. And this coercive power will only multiply if Beijing amasses more leverage over the global economy, one supply chain and critical technology at a time.

5. Preventing China from Becoming a 21st-Century Super-OPEC

Historical analogies help underscore what is at stake here. Consider OPEC, and consider Russia's natural gas policies.

China is working to become a super-OPEC of the 21st century, a single country that decisively controls crucial economic inputs for the world economy, especially semiconductors and materials needed for "green" energy. Its aim is not just commercial but strategic – to give itself leverage for coercion.

To safeguard our own security, the United States and our allies have to counter China's strategy. Allowing China to achieve OPEC-like power over advanced industries would give Xi Jinping the means to cripple the U.S. and allied economies, blunt our technological edge, and undermine our military strength.

If Xi gets his way, China's economic coercive power over Asia and the world would dwarf what Vladimir Putin created by tying Western Europe to Russia for gas supplies. Putin hoped that the dependency of Western Europe's states would ensure their acquiescence in Russia's conquest of Ukraine. He would likely have been correct if the Ukrainians had not mounted such a courageous and skillful resistance. By making itself so dependent on Russian energy, the Europeans effectively encouraged Russia to launch the war. It is a powerful cautionary tale for Europe and America.

The United States and our allies require a strategy of “constrainment” to counter China’s economic coercion. “Containment” is an unrealistic term regarding China. “Constrainment” takes note of the realities of economic interdependence and aims to adjust them to serve Western security interests. Constrainment can provide deterrence, working to deflate the confidence of Chinese officials that they can achieve their aims through aggression and war. We do not want Chinese officials to feel optimistic about their coercive economic leverage over us and our fellow democracies.

The new U.S. and allied export controls on semiconductor technology are an step in the right direction. If enforced diligently, the rules could foil Xi’s ambition to make China a home for advanced chip manufacturing. They can ensure that China remains dependent on the United States and its allies for these critical supplies. (While we are at it, U.S. officials should not ignore so-called “mature” semiconductor production. We do not want China to dominate the global production of chips needed for lower-end electronic goods crucial for critical infrastructure and autos.[5])

Constrainment should strive to maintain a favorable balance of dependence in a wide range of areas. It should, for example, strengthen the dominance of the U.S. dollar as a global reserve and trading currency, extending Washington’s ability to monitor and punish money laundering, weapons proliferation, bribery, and other dangerous actions by Beijing. Constrainment should remind China of its dependence on foreign sources of food and energy while reversing the United States’ growing reliance on Chinese batteries, solar panels, and other green technology.

The green technology point is especially crucial because trend lines appear to be moving fast in the wrong direction. As Washington subsidizes solar energy, electric vehicles, and other renewable technologies, is it protecting against the risk of growing dependency on China? Failure to do would be grave strategic neglect.

National Security Advisor Jake Sullivan recently gave a speech underscoring the importance of both greening U.S. energy supplies and limiting "dependencies that could be exploited for economic or geopolitical leverage."[6] Yet there appears to be nothing in the administration’s approach, or in the language of the Inflation Reduction Act or other such bills, to ensure that we are protecting ourselves properly. We should reduce risks that U.S. subsidies and green-energy targets give greater coercive power to China. We should carefully review the downsides of Chinese renewables exports to the U.S. energy market.

Let's draw on the wisdom of the Hippocratic Oath: China already has enormous coercive economic power in the world, even over the United States in some sectors. As policymakers manage America's energy transition, they should first do no (additional) harm to ourselves.

[1] https://asean.usmission.gov/the-south-china-sea-southeast-asias-patrimony-and-everybodys-own-backyard/
[2] https://www.consilium.europa.eu/en/press/press-releases/2023/03/28/trade-political-agreement-on-the-anti-coercion-instrument/
[3] https://www.young.senate.gov/newsroom/press-releases/young-coons-introduce-bill-to-counter-economic-coercion-of-allies-and-partners
[4] https://www.csis.org/analysis/deny-deflect-deter-countering-chinas-economic-coercion, https://www.aspi.org.au/report/chinese-communist-partys-coercive-diplomacy
[5] https://foreignpolicy.com/2023/04/03/chips-biden-xi-china-sanctions-semiconductors/
[6] https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/04/27/remarks-by-national-security-advisor-jake-sullivan-on-renewing-american-economic-leadership-at-the-brookings-institution/

Mrs. KIM OF CALIFORNIA. I also do want to make a quick announcement that our votes are called at 9:40. So we will go as long as we can with member questioning, but we may have to take a short break to go and vote and come back.

I want to thank all the witnesses for joining us and, you know, sharing your testimony.

Mr. Alon, I want to thank you again for coming and for the courage to tell your story publicly. And I just want to ask you to elaborate on your experience, so we can understand how we can stop what happened to you from happening to other American companies in the future.

Mr. RAPHAEL. May I ask which aspect I should elaborate on?

Mrs. KIM OF CALIFORNIA. The challenges, the coercion, what kind of experience you had where you are doing business with China.

Mr. RAPHAEL. I have not done business with China, but apparently China has done business with me.

[Laughter.]

Mrs. KIM OF CALIFORNIA. Is stealing the information you have.

Mr. RAPHAEL. Correct.

Mrs. KIM OF CALIFORNIA. So then can you talk about some of the laws or regulations that is—I know I was told that you were approached by China to try to sell your business to them, and you did not do that. So could you talk about that? You know, what stopped you from selling your company to a PRC venture capital?

Mr. RAPHAEL. I cannot confirm that they were a PRC venture capital, but I know they are Chinese. And what stopped me is because I am an American and I sell a critical technology that if I am the only source of that ends up in Beijing, and I am approaching you saying ni hao, then I have a very different way of looking at the world than that of an American.

Mrs. KIM OF CALIFORNIA. Thank you. Is there anything else that you can share with us about the challenges, so we can have the public, especially the American companies, trying to, you know, do business with China, or if they are facing with a similar economic coercion from China?

Mr. RAPHAEL. We are relying on policymakers to creatively utilize all the tools in the toolbox to help us. So what I can suggest is that, you know, my stick is the courts, and it is ineffective.

Mrs. KIM OF CALIFORNIA. Thank you.

Mr. Scissors, you know, I recently joined Congressman Ed Case to introduce legislation authorizing the President to implement a pilot program of economic defense response teams to provide emergency technical assistance to countries who are subjected to coercive economic measures. You are aware of that, though, right? Yes.

So what is missing in our response to countries under the threat or use coercive measures? And do you think the response teams referenced in that legislation can improve our response?

Mr. SCISSORS. I am sorry to say this, but I think what is missing is credibility on our side. You know, we—basically, when you are being—if China is coercing another country—Australia, Lithuania, South Korea, Taiwan—the No. 1 thing the U.S. would like to have is to tell people, “Hey, we have to work through our policies. We have to implement our legislation. But trust us, we are going to come help you.” And I do not know that we always have that. We do not have that in part, as you and I have both mentioned already, because we are helping China at the same time we say we are going to help whatever country is being targeted.

We also do not have it because the American policy attitude toward trade has changed in roughly the last 10 years, where if you say something like, "Oh, you know, to help out a fairly major exporter of a product, we are going to make it easier for them to sell to the United States because the Chinese are using their market size to coerce them," you are going to get opposition to that. You know, people are going to say, "No, no, no. The China coercion part is not as important as the trade part."

And so I think any steps Congress takes, they do not have to be large, if they are credible, if they are put into law—and this is not an attack on any Administration—EOs die off. If Congress takes steps that are put into law, that is going to help, because I think the first thing we need to do to reassure our allies is to say, "You can trust us. It might take us a while, but we are on your side, and we will take steps to show that."

Mrs. KIM OF CALIFORNIA. Thank you. You know, one of the things that we can do is to ensure that PRC does not have the tools to use the coercion in the allies, and especially in the Indo-Pacific war in developing countries that need help from us, which is why this Congress, we passed—the PRC is not a developing country.

They are using that as a—in a way to game the system, so they can use that special status to get the low interest rates or no interest rates from the international groups like the World Bank, IMF, and then they use that loan to backstop and reinvest in those developing countries that truly need help to set up the debt trap. That is one of the things that I think we are using, but I know there is a lot more that we can do.

Mr. Feith, I want to ask, how do we get allies to join the cause to push back on China?

Mr. FEITH. Well, there is a need for the sort of support and consultation that we have talked about, certainly for the sort of supply chain resilience. You know, there has been a lot of certainly post-COVID greater discussion about shifting supply chains, but I think this economic coercion issue raises the illustration of how really enormous that issue is.

It is fundamentally about macro trade relationships in the world and unwinding really decades of shifting of greater exposure of the U.S. market and of our allied markets to China. If that isn't reversed, China's ability to coerce will continue to grow.

Mrs. KIM OF CALIFORNIA. Thank you.

Let me now recognize Ranking Member Bera for your 5 minutes of questioning.

Mr. BERA. Thank you, Madam Chairwoman.

Yes. Sometimes we are slow to recognize the threat, and so forth, but I think everyone's eyes are wide open today. You know, a decade ago, two decades ago, the hope would have been, as, you know, China developed a middle class, an entrepreneurial class, they would adopt what a lot of the rest of the world has, free market opportunities, and so forth.

Clearly, we do not have to guess the direction that Xi Jinping's PRC is headed. You know, he has certainly signaled where he wants to go. And, again, maybe we are a little slow to recognize the risk, but I think the world and the United States certainly is doing what it can to have the tools and be ready to counter that.

You know, this Congress we have introduced the bipartisan Countering Economic Coercion Act of 2023, and, you know, some of the specific things in there are authorities that we would like to give to the President to, you know, if we see China targeting some of our trading partners, you know, the ability to reduce or eliminate duties, modify tariff rate quotas, requesting appropriations and authorization for foreign aid and financing, expediting export licensing decisions, and expediting regulatory processes.

Mr. Scissors—or, Dr. Scissors, I certainly agree that it is better for Congress to act and put into legislation. I would be curious about your thoughts—I am sure you are aware of that bill—your thoughts on that bill and strengths, but what is it missing?

Mr. SCISSORS. Well, I think the strength is exactly what you just said, sir, which is we have to be willing in a time of crisis to be nicer to our friends than we are otherwise. That does not mean our friends get to do whatever they want. I am personally not happy with the South Korean government and their companies right now with regard to export controls.

But in a time of crisis, we need to do more. We need to show that we will stand up with them. That is a way to reassure them and to deter China.

So those measures that you talked about of reducing barriers to the U.S. market in time of crisis I think are the right measures. And of course you have people who are very sensitive to that in the U.S. I am not suggesting that we rush to reduce barriers when there is a case of Argentina coercing Bolivia, but China is in a very different category.

So I think that is the strength of the legislation and, as you said, the fact that it is legislation that could be passed on a bipartisan basis would be ideal.

I think, again, you know, I do not mean to repeat myself, but the legislation is addressing a symptom, and the problem is, if we take these steps to help our friends, and it happens to be in that year—we have $200 billion in new money going to China—on net, we are still helping the Chinese become better at coercion.

So I think the legislation is a good idea. I support other sorts of legislation from the Congress addressing this issue, but I do think we need to look at, if we are helping the Chinese more than we are countering them, the net benefit is we are hurting our friends.

Mr. BERA. So I do not disagree. I mean, there is discussion on how you slow down outbound investment and outbound flows.

Maybe, Mr. Reynolds, let me ask you. On that perspective, how should we think about, you know, you still see a lot of U.S. company investment flowing into China. You know, I am not of the thought that says we should be telling companies what they can and cannot do, but I also do think there is increased risk. So how should we think about outbound investment and perhaps approach that?

Mr. REYNOLDS. Yes. Thank you, Mr. Congressman. You know, first, I may want to go to H.R. 1135. I really—what I really like about that bill is the timelines you all built in for a speedy response. I think that is really a key part of, you know, any sort of counterstrategy to counter China's economic coercion.

Something that you see in the sanctions literature is that, you know, sanctions tend to be most effective really basically when they are threatened, and then shortly after they are imposed. So in that window before markets can adjust, they kind of bite the most. So that is really, you know, to borrow a medical term, sort of the golden hour that we need to be responding and getting relief to the targeted countries, so that they do not back down in the face of China's economic coercion.

One other thing I would say that, you know, a big missing piece of the response so far, though, is also on this resiliency side. I think the U.S. needs to get back into business of negotiating free trade agreements. We have seen China continue to expand its presence in these trade agreements, you know, applying the joint CPTPP-RCEP became effective last year. You know, a greater and greater proportion of the world's countries now see China as their largest trading partner instead of the United States. So that is a big missing component.

Quickly, on outbound investment, I agree, I think there is a need to control this outbound investment, especially in these critical technologies where China could gain this chokepoint leverage over the United States. The Biden Administration I know is looking at technologies—semiconductors, biotech, green tech.

I would say one thing on that, though, we also need to make sure that we multilateralize those efforts. We see this with the export controls. When we do these things unilaterally, there can be loopholes. And so I think the same thing for outbound investment. We need to be looking to multilateralize that.

Mr. BERA. Great. Thank you.

I notice I am out of time.

Mrs. KIM OF CALIFORNIA. Thank you.

I now recognize Congressman Barr for your 5 minutes of questioning.

Mr. BARR. Thank you, Madam Chairwoman.

And I want to followup right where we left off with that good question from the ranking member about outbound investment. Dr. Scissors, my bill, the Chinese Military and Surveillance Company Sanctions Act, sanctions specific companies on four specific U.S. Government lists—the DOD 1260H Chinese military company list, Treasury's non-SDN Chinese military industrial complex companies list, and Commerce's entity list and military end user list.

And the bill harmonizes these lists and imposes OFAC sanctions on them to send a signal that not only are these companies off limits on U.S. exchanges, but over the counter on foreign exchanges and they presumably have a multilateral effect insofar as its OFAC sanctions, and so it signals to non-U.S. investors these are also off limits to them.

I would like your thoughts on this approach. Does it provide the American private sector—specifically, asset managers, index aggregators, investors—with sufficient clarity and certainty about what Chinese businesses are red light businesses and which Chinese entities are green light?

Mr. SCISSORS. I think that the bill would be an important step forward. I think the key word you used there is "clarity." Two things that it does. One, it tells us exactly what the rationale is for these restrictions; and, two, as I am sure you and your staff and everybody who has followed this are aware, harmonization of U.S. lists would be a great idea for the private sector. Sometimes you will meet private sector actors and you will tell them, "Well, did you check this list?" And they are like, "What? There is another list?"

And, you know, we have Commerce, Defense, State, we have different—Treasury. We have different agencies creating different groups of companies that they want to single out. Harmonizing that list for the sake of an action is a positive step. Explaining the rationale for your action, which is done in the bill, is also a positive step.

I think on the multilateral side, to get to both outbound investment in general, and your bill in particular, we are the leader on this. It is not an accident that countries began looking at inbound investment reform after we passed CFIUS reform.

We provide the technical information and the know-how to most of our partners. So I think there is an automatic multilateral benefit when you set out a U.S. policy. Clearly, that does not mean they are going to do exactly what we did. It means that they can learn from it and be encouraged by it.

So I think I wouldn't say the bill is, in my view, a solution to all the problems because we do have critical technologies to consider. That is a difficult debate. I think your approach is excellent, because when we say we are—these are bad Chinese entities that we shouldn't do business with, we are not actually implementing that. The entity list, for example, is a licensing process. We do not way to say, "Oh, this company deserves to be on the entity list," later give them a license, and it turns out American investment is going to the company.

So I think, you know, I see your bill as there are other options as well, but it is an excellent first step, because the private sector should be able to handle it better than the current confusing U.S.——

Mr. BARR. And our bill not only requires coordination entity lists—Commerce, Treasury, and DOD—but it also does now—the amendment in the nature of a substitute we are working on also requires as these agencies update the lists that they look at—they look at special sectors of special concern. So these critical technology sectors.

And I would invite my colleagues—the ranking member, Mr. Kim, who is on the Select Committee with me on China. I have talked to Ranking Member Krishnamoorthi about my approach. This needs to be a bipartisan effort. I think it can and should be, Chairwoman Kim.

So I want to engage with my colleagues on both sides of the aisle to make this the right approach, and the approach that is consistent with our basic default value of cross-border capital flows, but identifying the specific entities of concern, of national security concern, Chinese military technology and surveillance companies, and excising them from U.S. investors' investments.

Let me just go to Mr. Raphael really quickly. I was interested in your testimony that you said the CHIPS Act, while generally positive, does not help smaller, more agile companies, and eliminate the fear that foreign entities will ultimately reap the benefit. Can you amplify that testimony? And, obviously, as a victim of Chinese commercial espionage, what do we need to do to protect smaller companies like yours in the semiconductor space?

Mr. RAPHAEL. Well, we are relying on policymakers, again, to creatively utilize all tools in the toolbox to help protect us. I make cool things. I do not know how to protect them per se, but what I can say is that the CHIPS Act is a double-edged sword, insofar as companies like mine that will innovate and grow a garden at the end may be harvested by foreign entities.

So we I think need to ensure that the resources to grow this garden are present, but also the resources to defend it.

Mr. BARR. Thank you. My time has expired.

Mrs. KIM OF CALIFORNIA. Now I recognize Representative Andy Kim your 5 minutes.

Mr. KIM OF NEW JERSEY. OK. Thank you. Thank you so much for all of you coming on out here.

Mr. Reynolds, I would like to start with you. You were talking earlier today about just kind of analysis of different countries and whether or not they have been subjected to economic coercion and how they fared, whether that was something that was positive or negative in terms of moving that direction.

That was really interesting to me, this kind of question of—that I am kind of thinking about right now is our best understanding of, you know, which countries are most vulnerable to this type of economic coercion? Do we see any types of patterns? Is it about, you know, geographic proximity to China? Is it about certain size markets or last—you know, a certain type of lack of diversification in their economy or other things? I am just kind of curious if you have been able to kind of elicit any insights on this?

Mr. REYNOLDS. Yes. Thanks for your—thanks for your question. I would, you know, say just directly the most vulnerable countries are going to be the smallest countries, and not—you know, small countries can still be resilient if they have advanced economies and advanced political system. So the most vulnerable countries are really going to be the countries that do not have market systems and do not have strong political systems.

So you kind of see when the—in the case studies that we have, probably the two where China had the most success of coercing and getting the policy outcomes that it wanted was against the Philippines and Mongolia. At the time, Mongolia was facing a recession and was very susceptible to, you know, Chinese threats of cutting off a concessional loan, so they quickly apologized for inviting the Dalai Lama and then, you know, promised not to invite the Dalai Lama back.

The Philippines is a little bit more complex because you had Duterte, you know, become elected or was elected and then kind of switched, you know, the Philippines' alignment. But I would say and those two cases had sort of the weakest political systems and weakest economies, and China had the most success.

Mr. KIM OF NEW JERSEY. Mr. Feith, I wanted to bring you in on this because I was looking through your testimony. It seems like you were kind of looking at this similar question, in fact some of the same data there. I would like kind of your reaction on that from—both in terms of what Mr. Reynolds just said, but also in your testimony you said, look, you know, there are some examples where they have been able to push back, but there are some broader overarching examples as well where it has been effective.

So over to you.

Mr. FEITH. Thanks for the question. Indeed, you know, the CSIS report is a really valuable study and allows us to work through these questions, which really are sort of interesting and nuanced in a detailed way. You know, as that report highlights, and as was just discussed, there have been these several cases that have gotten a lot of attention, and on those cases—you know, roughly 8 or 10 over a decade—China's record of apparent success in the particular sort of political aims of its coercion against these individual countries is very mixed. And there are interesting lessons in there about how challenging it is for China to achieve some of its objectives in some of these cases.

So, for example, you know, they generate fear and loathing in these foreign capitals. They sometimes make foreign public opinion and strategic opinion hardened against Beijing. Similar effects can happen when China goes after companies, right? China is not looking to make itself right now seem like an inhospitable place, say to foreign semiconductor companies.

So when it takes an action and goes after a micron, it can have some coercive bullying effect, but it also has an obvious downside of making companies and governments that are interested in those companies have less faith in these economic relationships with China.

The problem is the full scope of China's economic coercion, the full definition would appear to extend far, far beyond any 8 or 10 or 12 cases. China is using its economic coercion far more broadly. China has been able to continue to carry out its human rights abuses in Xinjiang largely because of its economic coercive power, the sense that other countries do not want to anger Beijing.

We have had a lot of discussion and interest in the Congress in the fact that in the United States, in our media, in Hollywood, across corporate America, major leaders with influential voices are very careful about what they say about China for fear of economic response.

Mr. KIM OF NEW JERSEY. One thing I would just kind of push back a little bit on this, I mean, look, we have struggled, you know, 20 years ago to address Sudan and the genocide in Darfur. You know, we have struggled in a lot of those cases, not necessarily because of just, you know, market issues. We have a lot of challenges in terms of how to actually address human rights abuses all over the world in both large markets and smaller countries as well.

I just want to say this for my colleagues. I think this is a really important issue about just, you know, where can we have precision? Where can we have the scalpel? Where can we use that? And where do we need the broad tools? And I think that that is something that we think about in terms of understanding all the tools in our toolbox and recognizing it. I think for us to have that kind of fidelity would make our policies and our strategies stronger.

And with that, I will yield back.

Mrs. KIM OF CALIFORNIA. Thank you, Representative Kim.

I now recognize Mrs. Radewagen for 5 minutes.

Mrs. RADEWAGEN. Talofa lava. Good morning. Thank you, Chairwoman Kim and Ranking Member Bera, for holding this hearing. And thank you all for appearing today.

Earlier this week we held a hearing in the Natural Resources Committee on countering China in the FAS and Pacific territories. One of the stories we have heard is how China has punished the Republic of Palau by hurting its tourism industry. Another example is how when Australia called for an independent investigation of COVID–19, China banned Australian goods. So this hearing is a good followup to that hearing from earlier this week.

Now, Mr. Feith and Dr. Scissors, my questions are directed at you. Given the PRC's extensive economic coercion in the Pacific Islands, what option does the United States have to work in tandem with Pacific Islands countries to ensure that the PRC's aggression is not successful?

Mr. FEITH. Thanks for the question. Certainly, we have seen this problem worsen in recent years, and we have seen U.S. diplomatic and strategic attention grow toward the Pacific Islands and the China-related challenges there, but not yet sufficiently. Some of that is actually playing out, you know, very much in real time this week, because President Biden was going to be the first U.S. President to visit Papua New Guinea. He was going to do this in a few days after going to Japan for the G7, and he would have attended in Papa New Guinea the Pacific Islands Forum. And this, you know, reflects sort of a stepping up of U.S. interest that goes back into the previous Administration and has in various ways continued since.

The President canceled that trip in light of the debt ceiling questions here back in Washington, which is earning a lot of predictable criticism and concern from the region, which wants more U.S. engagement. That U.S. engagement can take the form certainly of greater economic interest, which is often difficult given, you know, companies have a hard time operating in some of these environments.

The U.S., with the Congress, over the last several years has strengthened tools like our Export-Import Bank, our Development Finance Corporation, but bringing those tools to the speed and the magnitude of relevance, including in the Pacific Islands, has really been a challenge.

One obvious solution is working especially closely with our allies, including Australia of course in that region, but also Japan, when it comes to matters of export credit and development finance where the Japanese have been very successful over a very long time.

Mrs. RADEWAGEN. Dr. Scissors.

Mr. SCISSORS. Thank you for the question. I think I would start with the basics, which is that we should not be considering, in the Pacific Islands or anywhere else, that we get into a bidding war with the Chinese. We do not want to be in a situation where, oh, you offered $100 million worth of aid, we will offer 110 million, and around the world we do this everywhere, Latin America, sub-Saharan Africa.

I think the best strategy for the U.S. to keep it simple is to try to make the Pacific Islands States as strong and prosperous as possible. So our goal should not be to say, “Oh, China is going to build something for you. We will build something bigger.” It should be to say, “How can we make your societies more resilient, but really also more successful, make lives better for people?” and then there won’t be a thought that, oh, we should reach out to the Chinese and they have some magic wand they are going to wave.

So I think the basics are we should consider our Pacific ally—friends and allies, Pacific Islands friends and allies, we should consider their well-being. And as they do better, they are going to be less interested in Chinese quick fixes.

Mrs. RADEWAGEN. Thank you. And as a followup, other than re-signing the compacts of free association, what steps can the United States take to coordinate an allied response that safeguards Pacific Islands from Chinese predatory practices?

Mr. Feith? Dr. Scissors?

Mr. FEITH. I would just note one additional point, which relates partly to what Dr. Scissors has mentioned about resilience. Our efforts that would apply, not only in the Pacific but around the world, to have a better understanding and greater transparency around Beijing-backed corrupt practices, because one of the ways that the Chinese Communist Party takes advantage of countries that do not have strong resilience at home and generally works in ways that are disadvantageous to us, is they use corrupt practices, they use them politically and commercially, and these can be very effective, unfortunately, in capturing a lot of local political influence to the detriment of those countries and to the detriment of our interests.

Our ability in intelligence terms, in law enforcement support terms, in support for public prosecutors in journalism and transparency and sunlight in these cases, is really very important and another area for U.S. and allied coordination.

Mrs. KIM OF CALIFORNIA. The gentlewoman’s time has expired.

I now recognize Mr. Waltz for your 5 minutes.

Mr. WALTZ. Thank you, Madam Chair.

Mr. Feith, I just wanted to continue with you. I think, you know, as we talk about economic coercion, language matters. Language from our leadership matters, so I will ask you a question I have asked many in the Administration and thought leaders in this space. Is the Chinese Communist Party in a cold war with the United States? Using just the basic understanding of using non-military means to supplant, replace, defeat a foe?

Mr. FEITH. Yes. And Xi Jinping’s own words, especially spoken to his own leadership, say so. They believe they are in a systemic and existential challenge with us and that they will win.

Mr. WALTZ. So I think that language matters so much because if we are asking investors, researchers, academia, small businesses, we can go down the line to essentially walk away from a market, from profit for, you know, funding for research that they may care about, we need to think about it as a society in that light, right?

Mr. FEITH. I would agree.

Mr. WALTZ. Is there anyone that disagrees? Because I hear a lot, you know, "Oh, no, no. We are in a competition." Competition sounds like a couple of countries in the Olympics. I mean, this is a cold war, and they seek to win it, and they seek to win it without firing a shot.

Mr. FEITH. That is right. And part of the challenge is that, you know, we have habits and institutions that are for good, historical reasons driven to see especially U.S. Government action that is limited and restrained and surgical and careful. And that is generally a good thing, right? We want our government intervening, say, in markets in ways that are generally limited. It is just that China poses a scale of a threat——

Mr. WALTZ. Sure.

Mr. FEITH [continuing]. And a degree of economic connectedness to us that we have never faced before.

Mr. WALTZ. Let me just in the sense you are talking about agree. I want everyone to make money. No problem. But when it comes at the expense of our national security and key dependencies, along those lines, there has been—I mean, there is a plethora of information out there on the CCP's dominance of global critical mineral supply chains, particularly cobalt owns now nearly half of the world's mining, owns three-quarters of the refining, lithium, manganese. We can go down the list.

I think my question is, how does the Biden Administration's emphasis, billions that we are spending, that we passed out of this body on green energy, electric vehicles, including in our own military, to combat climate change, increase China's economic leverage over the United States, and in accordance with their own Made in China 2025, which is not just to in-source their own manufacturing, it is to create global dependencies, right? So how does that increase their leverage?

Mr. FEITH. It would seem unfortunately that a lot of our own recent policy decisions are pointing in the direction of significantly increasing Beijing's leverage over us and over our energy economy. And this was one of the factors after all that appears to have made Vladimir Putin confident that he can invade Ukraine and survive the consequences was because he understood that he had a strong degree of leverage over western European energy.

Mr. WALTZ. Have you seen as you study CCP writings very closely the actual translations? I mean, they have somewhat tried supply chain coercion with the Japanese and the Australians. Do you believe that is baked in, they are prepared to do that even at risk of damage to their own markets and economies with the United States?

Mr. FEITH. Oh, yes. And we have seen them not only do so, but especially since COVID, Xi Jinping has been increasingly explicit about this. He gave a series of speeches in 2020, and the speeches were then reflected in the 14th Five-Year Plan that was published by Beijing in March 2021 where he spoke explicitly about tying global supply chains and dependencies increasingly to China using what he calls the powerful gravitational field of China's domestic market in order to make other countries dependent on them while reducing the dependency of China on others.

Mr. WALTZ. Just in the few seconds I have remaining, shifting a bit, the board that oversees the Thrift Savings Plan, which is the military's 401(k), has made a series of moves to invest their international index into Beijing, amongst other, because of this—again, this notion of "We are just here for returns."

Our military's own retirement plan to be invested into our greatest adversary, do you believe that this board, and boards like it, have a moral, have a fiduciary responsibility, to disinvest?

Mr. FEITH. Yes. And there were efforts to bring that about in 2020, especially that I gather have been undone largely by some of the technical changes since then.

Mr. WALTZ. Thank you, Madam Chair.

Mrs. KIM OF CALIFORNIA. Thank you. Thank you, Representative Waltz.

I now recognize Representative Castro for 5 minutes.

Mr. CASTRO. All right. Well, thank you for being here today to speak about this important and timely topic. I know we are all watching closely as the G7 meets in Japan this week to discuss China and its economic practices.

And the United States serves as an important counterweight, as you all know, to China's aggressive economic tactics around the world and in the Indo-Pacific region. The United States must continue to be an economic partner, a first choice for nations around the world, and work to build trust and goodwill between any country looking for transparent, sustained, and quality investments. But, as you all know, there is more work to be done.

So, Mr. Reynolds, the United States has multiple tools to counter China's economic coercion, which is mostly targeted toward smaller nations. In your testimony, you indicated that some of these tools include export financing, sovereign loan guarantees, and temporary tariff reductions.

The United States also has many institutions that can support a country's development goals, such as with the Millennium Challenge Corporation. Though in recent years it has become obvious that more countries need access to MCC funding—and that is why I introduced the Millennium Challenge Corporation's Candidate Reform Act, which would modernize MCC's statutory criteria and redefine the MCC's candidate country pool—and these changes would offer more countries an alternative to China-backed financing.

Can you explain why it is important to ensure more countries, especially those vulnerable to Chinese coercion, have access to U.S. economic support?

Mr. REYNOLDS. Thank you, Mr. Congressman. As you mentioned, in our report one thing we did see was that China has a preference for targeting smaller countries. And one of our, you know, recommendations was that the United States should practically seek to build resilience. So, you know, not being an expert on MCC, what I would say, any policy that can, you know, practically help those countries build a resilience should in theory in the long run make them more resilient and able to stand up and withstand China's economic coercion.

One thing I will say is that there could be, you know, tradeoffs with expanding the pool of eligible countries. If you are raising the threshold to allow richer countries in, you also need to make sure that does not come at the expense of smaller countries that are the most vulnerable.

Mr. CASTRO. I will open it up for anyone else who would also like to comment. No? OK.

My second question is really about Chinese misinformation or disinformation and manipulation of certain industries, and this time I am going to focus on an industry we do not focus on too much around here, but we should focus on more, which is the media and entertainment industry in the United States.

Mr. Scissors, you spoke extensively about the advantages and disadvantages between the United States and China's economies. You also pointed out non-traditional means of economic coercion, such as bullying Hollywood, the 2021 NBA spat, and what you described as "data mercantilism."

I am interested in how China might use its market to influence aspects of American-made movies, for example, identities of certain characters have been changed, movie releases have been dropped, and whole scenes have been added to stay in good standing with the PRC. Why do these changes undermine the role of Hollywood as a source of soft power and cultural diplomacy for the United States? And what implications does it have for China's economic coercion toolkit?

Mr. SCISSORS. Thanks for the question. I could talk a long time about the new data mercantilism coming out of China and our need to respond, but I will focus on what happened with the entertainment industry. You have seen in the NBA—you have seen it in Hollywood for a long time, you have seen it in the NBA more recently, that gravitational pull of the Chinese market that David referred to, which is saying to companies, "Wouldn't it be easier if you changed this movie a little bit and you could make a lot more money? It is very seductive."

And what happens is this is part of what China considers to be information warfare. Stop letting people know what is actually happening in China. It matters at the level of an individual company operating in China where the Chinese say, "Stop sending data outside of the country," and it matters for U.S. entities here who wouldn't appear, like the NBA, to have any real direct connection to China.

Authoritarian governments like information control, and our advantage economically and as a society is to fight that off and to allow people to express their views freely without worrying about, is this going to cost me money?

Mr. CASTRO. It is interesting because China has created a very competitive situation within Hollywood and American media where they will only allow a certain number of movies—American movies—per year to be shown in China. And so that is what gives them oftentimes a leverage to say, you know, "We are not going to let you—we are not going to show your movie if you do not take this out," or you change this or that. And there seems to be no discernible end in sight necessarily to that continuing.

Mr. SCISSORS. I think it would get worse. One of the things I have noticed in our conversation is just to drive home the point that sometimes we are slow in responding because we still think

China is the same as it was 20 years ago. Xi Jinping's China is a different China, and we should expect more of that coercion, especially if we do not respond to it.

Mr. CASTRO. I yield back.

Mrs. KIM OF CALIFORNIA. The gentleman's time has expired.

Now I recognize Mr. Davidson for 5 minutes.

Mr. DAVIDSON. I thank the chairwoman. Thank you for our witnesses calling attention to, you know, really an incredibly important topic. I am glad we are having this hearing today. As a guy who was trying to make a manufacturing company work in the United States, it was really obvious we weren't just competing against other companies. We were competing against countries, and nowhere is that more true than China.

So, at this point, you know—well, let's go back to 2018. 2018, the Office of the U.S. Trade Representative, tasked with monitoring China's compliance with WTO commitments, found China to have "a poor compliance record" and is "violating, disregarding, and evading WTO rules." This committee has recognized that they are abusing the developing nation status or claims within the WTO.

So that was 5 years ago when those quotes were cited in the—so I guess the real question is, is the WTO still an effective, or was it ever an effective mechanism to deal with the PRC's predatory economic practices? And what should the United States do if the WTO structure is in fact failing? Mr. Scissors?

Mr. SCISSORS. Wow. Big question. Thank you. I do not think the WTO is effective any longer. I do not mean to say it was never effective. I do not mean to say it is a terrible idea. I think China has moved in a direction of violating WTO principles and gaming the WTO, and it is now of a size that it is intolerable.

When China broke WTO rules in 2003, it wasn't great, but it wasn't as much of a strain on the system. Now they are more aggressive in breaking the rules under Xi than they were under Jiang Zemin at the time, and they are much bigger. So I do not think the U.S. should just try to destroy the WTO, but I do think we should recognize the WTO cannot check Chinese behavior. And we are going to have to either act on our own or create another organization of some sort to do so.

Mr. DAVIDSON. Yes. And so do you believe there is a coalition—does anyone really believe there is—you know, I think not just at the military academy I attended, but probably all of them around the world, they would say you are more likely to win a war if you multiply your allies than you multiply your enemies.

The curious thing is, how hasn't China multiplied their enemies on trade? They have managed to do this to essentially every country around the world, yet how is it that we are not multiplying our allies to confront China on these abusive practices

Mr. SCISSORS. My quick answer to that is, again, going back to, how much credibility do we have? If the U.S. would take the lead on this, not all countries, not everyone, but some countries would join us? I think Japan, for example, would be very happy if the U.S. would take leadership on confronting Chinese predation. But it is hard to say you are taking the lead if you are still having money and technology flowing to China.

Other countries see that and they say, "Well, you are saying one thing. This committee may be saying one thing very clearly. But the U.S. as a whole is not acting in that same way." So allies aren't going to rally to us until we are willing to take the necessary actions ourselves.

Mr. DAVIDSON. Yes. So one of the things as I was coming to Congress in 2016, the Trans-Pacific Partnership was falling apart. And, you know, it was—the idea was we were going to solidify some folks in the Indo-Pacific region against what China was doing, but we were kind of doing it passively. We weren't really confronting China about their abuses.

We were just going to build some allies there. And I think that is a significant part of why TPP unraveled is because it did not actually confront China as sort of passive-aggressive, sort of this other way, and it failed from both sides. You know, both parties started campaigning against TPP in the 2016 election cycle.

Is there a path where we might be able to put something like that together? Or have we missed the moment? For anyone.

Mr. SCISSORS. Well, I did not—I will just say I did not like the substance of the Trans-Pacific Partnership. I liked the idea. I supported the idea. And then I saw the final agreement, did not like it. And the main reason I did not like it is exactly what you said. For example, in rules on State-owned enterprises, we are very weak for the sake of making Vietnam and Singapore happy, but it meant that we weren't doing anything to limit the behavior of Chinese State-owned enterprises.

I think we could, with the right partners, create an organization, but it would have to be an organization that is really focused on China. It is not a more general organization. As you bring in more countries, they have different interests with regard to China. So we would have to stand up and say, "Look, we would love a strong TPP. We did not get it. So, as a substitute for that, as an arrangement that is directed at Chinese economic predation, we are going to propose something else."

Mr. DAVIDSON. Yes. Thank you. And I wholly concur that is really where I landed. And, in 2017, I introduced the Global Trade Accountability Act, the counterpart to Senator Lee in the Senate. And I do not really think it is timely that Congress reclaim the Article I authority we have on trade. And, frankly, we represent the people, not just, you know, one person at the Administration, but really this body fully engaging on it, because I do believe it is one of the most important problems that we confront today that is shaping our foreign policy, our domestic policy, and our economic future.

So I hope we do that. I yield back.

Mrs. KIM OF CALIFORNIA. Thank you. I now recognize myself for 5 minutes, and I want to ask the question to Mr. Alon. You know, how would you counsel an entrepreneur looking for talent in a high-tech industry like yours?

Mr. RAPHAEL. Be very cautious who you hire. So fundamentally, you know, I can suggest that it is very challenging to find talent that is not sharing a risk profile in addition to the reward they can bring. So I would only say think hard.

Mrs. KIM OF CALIFORNIA. Are you having a hard time finding talent to work with you at your company?

Mr. RAPHAEL. Absolutely.

Mrs. KIM OF CALIFORNIA. OK. Is there anything that we can be of help to you in terms of policy initiatives?

Mr. RAPHAEL. Well, certainly. Right now I think there is a very clear and present danger that we are in front of insofar as our defense capabilities. One might recall in Desert Storm how the M1A1 Abrams tanks had a firing pin that cost 99 cents, and it did not work and what we ended up with was a block of metal in the desert.

I make machines that do process control. They help evaluate microchips that are going to go into some of these very glamorous, very large, and very critical systems, and I am struggling right now to find the resources necessary, and the protections necessary, to ensure that that firing pin or the equivalent microchip thereof in these large-scale projects does not cause another hunk of metal in the desert.

Mrs. KIM OF CALIFORNIA. Thank you. Well noted.

Mr. Feith, you mentioned—obviously, we all know a G7 meeting is happening right now. And I want to ask you, and then maybe the others can chime in, what do you hope to see come out of this G7 on economic coercion?

Mr. FEITH. Well, we have been told by the governments involved that they do plan to make this a focus and put it on the agenda and perhaps issue some sort of special statement about the economic coercion problem. It is not clear, though, if that statement will mention China, which is not the most important thing, but it is a proxy for how much, you know, diplomatic weight and, frankly, you know, effort and risk countries are willing to put behind these measures.

If the statement is just a statement and it is hollow and not backed by the willingness of the national governments, you know, back home to take real measures to push back—to incur push back from China, as a result statements at the G7 aren't going to matter for much, unfortunately.

And so it speaks partly of the question from a moment ago about which trade coalitions can really work. The G7 would be a great one, including if the European Union is willing to be involved, but that is 27 member States and that is complicated at best, beginning perhaps with AUKUS countries—that is, the U.S., Australia, and the U.K.—or with Japan as well. We have the Quad, of course, where Japan, Australia, and India fit. These might be smaller but more appropriate because more robust groupings for doing some of this overdue push back.

Mrs. KIM OF CALIFORNIA. Thank you. I yield back the balance of my time, and I would like to now recognize Mr. Sherman for your 5 minutes of questioning.

Mr. SHERMAN. Thank you. Our tax code has a capital gains allowance, much lower taxes on the money you make by selling stocks, bonds, other investments, designed to encourage you to invest in the U.S. economy, create jobs and economic progress.

Can any witness here—raise your hand if you think you can put forward an argument why we provide this capital gains allowance to those who invest in the equity securities of Chinese-based companies? Can any of you think of a reason why that is good U.S. policy? The record should indicate no one raised their hands.

Tariffs are really the only across-the-board way that we can disentangle our economy, and disentangling is so important because right now China does not need to hire a lobbying firm here in Washington, because the biggest American companies feel that their profits are dependent upon us kowtowing to China.

If we had a 1/4 percent tariff—just 1/4 percent tariff—on all Chinese goods, and we increased it by 1/4 percent every month, then companies that fail to disengage from China would find a—they would be at a 40 percent disadvantage by the end of the decade.

Finally, and I do not know if this is—I assume this has not been brought up at the hearings. China allows only 40, roughly, American movies to go into China every year. So if you are a studio, you hope it is yours. So they will never make another movie about Tibet. Richard Gere, sorry. Not just because they cannot have that movie displayed in China, but because if a studio makes a movie about Tibet, none of their movies are ever getting into China, and they know that. I am saying the quiet part out loud.

Does anyone on the panel have an idea of what we can do to make sure that China does not use that kind of economic coercion to affect what Americans see? Whether it is to exercise—you know, we have American basketball players and officials talking about human rights in China, we have movie studios that would like to make this or that movie but would be subject to retaliation. Does anybody have a plan just to make sure that the First Amendment isn't interfered with by China?

Mr. FEITH. Well, Congressman, one related thought would be to find an appropriate way to ban TikTok, because the kind of information power, the kind of—what the Chinese Communist Party calls global discourse power, and the kind of ability to propagandize to Americans and undermine our democracy, including undermining our, you know, First Amendment spirit of an open debate that is not coerced by foreign adversaries, is advanced increasingly by TikTok, which is a kind of foreign influence in our democracy no adversary has ever enjoyed.

Mr. SHERMAN. I would point out that there are a lot of Americans who really enjoy TikTok. They are worried that that enjoyment will be taken away from them. But I believe that America can be self-sufficient in cat video distribution systems. If we did not have TikTok, Americans would create TokTik and the kitties would still be there.

We have a huge trade deficit with China. Other—in fact, it is the most lopsided trading relationship in the history of mammalian life. Do any of our witnesses have a plan other than the tariff idea that I put forward to try to diminish that trade deficit? Yes.

Mr. SCISSORS. I mean, I have a partial solution, which is, you know, the 25 percent and sometimes 15 percent tariffs proposed by the Trump Administration did not actually shrink the trade——

Mr. SHERMAN. And I will point out, the average tariff on Chinese goods——

Mr. SCISSORS. Is still low.

Mr. SHERMAN [continuing]. Is under 5 percent.

Mr. SCISSORS. Exactly.

Mr. SHERMAN. That was a very selective system. Go on.

Mr. SCISSORS. Agreed. I think we can start in an area of I hope bipartisan agreement that it will not solve the trade deficit problem, but it will certainly reduce it, which is identify the goods that we do not want to depend on the Chinese for. So there is dollars in goods we may not care as much about. There is the debate over what those are. There is also dollars in goods we know we care about. We can address both the supply chain dependence——

Mr. SHERMAN. I understand that selectivity. I will say whatever the goods are you run—for every billion dollars of trade deficit, we are losing 10,000 jobs. And those who say that we have a labor shortage in this country I think are wrong until labor wages start going up.

I yield back.

Mrs. KIM OF CALIFORNIA. The gentleman's time has expired.

I know that votes have now been called, so I wanted to thank the witnesses for their valuable testimony, and the members for asking those questions.

Other members of the committee may have some additional questions for the witnesses. So we will ask you to respond to those in writing.

And I now recognize Mr. Bera for any closing remarks he may have.

Mr. BERA. Great. Thank you, Madam Chairwoman. Yes. I do not think Democrats and Republicans think about this issue in different ways. I actually think we are all taking this very seriously. And, you know, I think members on both sides of the aisle raised legitimate questions and, again, the witnesses, I thank them for, you know, raising the issues that we really do have to think about in an urgent way.

There aren't easy answers when we—you know, again, I tend to be a free market guy. I tend not to want to use the heavy hand of government to tell companies what they can and cannot do, where they can and cannot invest, but I also do think it is important for us—you know, Mr. Waltz raised, you know, our pension funds continue to go into China, continuing to disadvantage us.

I have talked to CEOs about that as well, and, you know, often they are just—you know, there is shareholder activism, there is just this intense focus on quarterly profits. Again, you know, Mr. Sherman raises some issues of how we might be able to use the tax code to help influence that.

I mean, this is worth a bipartisan conversation to think about, you know, how we, you know, protect our values, our freedoms, but also, you know, do not disadvantage, you know, what is, you know, the strategic competition.

I do not use the cold war language, but we do know we are, you know, headed toward a confrontation, and how do we head that confrontation off? And I think that is important.

So, again, thank you for holding this hearing. I would encourage all my colleagues to take a look at the legislation that we put forward. I think it is a good first step. It is not a last step, and there is a lot more for us to do.

So thank you, and I yield back.

Mrs. KIM OF CALIFORNIA. Thank you. And, again, thank you to all the witnesses. You know, as we prepare for this hearing, we wanted to make sure that we are addressing the economic coercion from PRC, and I think hearing from our witness, Mr. Alon, it was—it is more than ever important that we need to stress that American foreign policy must serve the interest of the ordinary Americans and businesses as well.

And then, also, the United States must also take on the PRC's predatory practices, which is why we had a very great discussion here. Thank you.

And, last, I think we need to emphasize that America must lead and then bring its allies and partners along, and that is very, very important. We need to show to our allies that they can trust us, that the United States will be the choice to do business with and to rely on us to protect their interests as well as showing through the combination of cooperation, that we are working with our allies and partners, that our adversaries should be able to fear us.

With that, I want to thank you so much for being with us.

And pursuant to committee rules, all members may have 5 days to submit statements, questions, and extraneous materials for the record, and subject to the length limitations.

So without objection, the committee stands adjourned.

[Whereupon, at 10:27 a.m., the subcommittee was adjourned.]

APPENDIX

FOREIGN AFFAIRS COMMITTEE
CHAIRMAN MCCAUL

COMMITTEE ON FOREIGN AFFAIRS
SUBCOMMITTEE HEARING NOTICE
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, DC 20515-6128

Subcommittee on the Indo-Pacific
Young Kim (R-CA), Chairwoman

May 11, 2023

TO: MEMBERS OF THE COMMITTEE ON FOREIGN AFFAIRS

You are respectfully requested to attend an OPEN hearing of the Committee on Foreign Affairs to be held at 9:00 a.m. in Room 210 of the House Visitor's Center. The hearing is available by live webcast on the Committee website at https://foreignaffairs.house.gov/.

DATE:	Thursday, May 18, 2023
TIME:	9:00 AM
LOCATION:	HVC-210
SUBJECT:	Standing United Against the People's Republic of China's Economic Aggression and Predatory Practices
WITNESSES:	Mr. Alon Raphael CEO FemtoMetrix
	Dr. Derek Scissors Senior Fellow American Enterprise Institute
	Mr. David Feith Adjunct Senior Fellow Center for New American Security
	Mr. Matthew Reynolds Fellow, Economics Program Center for Strategic and International Studies

To fill out this form online: Either use the tab key to travel through each field or mouse click each line or within blue box. Type in information.

COMMITTEE ON FOREIGN AFFAIRS

MINUTES OF FULL COMMITTEE HEARING

Note: Red boxes with red type will NOT print.

Day *18* **Date** *May* **Room** *HVC-210*

Starting Time *9:01 AM* **Ending Time** *10:28 AM*

Recesses ____ (____to ____) (____to ____) (____to ____) (____to ____) (____to ____) (____to ____)

Presiding Member(s)

Check all of the following that apply:

Open Session ☑
Executive (closed) Session ☐
Televised ☐

Electronically Recorded (taped) ☐
Stenographic Record ☐

To select a box, mouse click it, or tab to it and use the enter key to select. Another click on the same box will deselect it.

TITLE OF HEARING:
Standing United Against the People's Republic of China's Economic Agression and Predatory Practices

COMMITTEE MEMBERS PRESENT:
Chairwoman Kim, Ranking Member Bera, Rep. Sherman, Rep. Barr, Rep. Castro, Rep. Radewagen, Rep. A. Kim, Rep. Davidson, Rep. Waltz

NON-COMMITTEE MEMBERS PRESENT:

HEARING WITNESSES: Same as meeting notice attached? Yes ☑ **No** ☐
(If "no", please list below and include title, agency, department, or organization.)

STATEMENTS FOR THE RECORD: *(List any statements submitted for the record.)*
Rep. Connolly

TIME SCHEDULED TO RECONVENE ________
or
TIME ADJOURNED *10:28 AM*

Note: Please include accompanying witnesses with their titles, etc. (please note the fact that they are accompanying witnesses)

Clear Form

____
Full Committee Hearing Coordinator

Committee on Foreign Affairs Subcommittee on the Indo-Pacific

118th Congress

ATTENDANCE

Meeting on: PRC Economic Coercion

Date: May 18, 2023

Convened: 9:01 AM
Adjourned: 10:28 AM

Representative	Present	Absent	Representative	Present	Absent
Chairwoman Kim	X		Mr. Bera	X	
Mrs. Wagner		X	Mr. Sherman	X	
Mr. Buck		X	Mr. Connolly		X
Mr. Green		X	Mr. Keating		X
Mr. Barr	X		Mr. Castro	X	
Mrs. Radewagen	X		Mr. Kim	X	
Mr. Davidson	X				
Mr. Waltz	X				

STATEMENT FOR THE RECORD SUBMITTED FROM REPRESENTATIVE CONNOLLY

Standing United Against the People's Republic of China's
Economic Aggression and Predatory Practices
House Foreign Affairs Committee Hearing
9:00 AM, Thursday, May 18, 2023
HVC – 210
Rep. Gerald E. Connolly (D-VA)

Under the leadership of President Xi Jinping, China has undertaken a dramatic expansion of its global investment and influence. Over the past decade, the PRC has exerted its economic, political, cyber, and military or quasi-military force to shift the power dynamic in the Indo-Pacific in their favor.

The flagship of Beijing's tactics, especially within the economic sphere is the Belt and Road Initiative (BRI), a massive infrastructure project that China promises will attract more than $1 trillion of investment over the long-term. Characteristic of China's model of development, BRI projects often solicit unsustainable debt burdens for recipient countries, employ Chinese state-owned enterprises or labor, and lack transparency surrounding financing and contracting. We are already witnessing early signs of a backlash to China's predatory style of investment in the Indo-Pacific. In Sri Lanka, a Chinese state-owned company took control of the deep-sea port it had built in Hambantota after the Sri Lankan government was unable to service its loans. In Malaysia, the new prime minister Mahathir Mohamad soared to electoral victory by vowing to review a slate of "unequal treaties" signed by his predecessor with Chinese state-owned companies as part of BRI. Understanding whether these events are part of a growing trend will be critical to shape U.S. strategy.

China's nefarious tactics are one reason why I, as President of the NATO Parliamentary Assembly (NATO PA), urged NATO to put China on its agenda. In November 2020, I wrote a report for the NATO PA Political Committee entitled, "The Rise of China: Implications for Global and Euro-Atlantic Security" to encourage NATO to adapt to a new balance of power that reflects China as a world power. In this report, I urged my colleagues to include reference to China's actions in NATO's strategic documents, including the Strategic Concept which was unveiled in April 2022 and highlighted the stated ambitions and coercive policies that challenge the Trans-Atlantic Alliance's interests, security, and values. I welcome the newly adopted NATO Strategic Concept which does just that.

China has limited foreign competition in its domestic market and props up private enterprises with Chinese state funding and intelligence. For example, in order to bolster China's semiconductor industry, the Chinese government launched a $150 billion public-private fund to subsidize investment, acquisitions, and the purchase of new technology from 2015 to 2025. The Chinese government has also restricted U.S. cloud service providers from providing services in China. In the 117th Congress, Democratic majorities in both chambers passed the CHIPS and Science Act, legislation that made historic investments that will poise U.S. workers, communities, and businesses to win the race for the 21st century. Biased PRC policies flood global markets with cheap supply, undercut foreign competition, and create an environment where it is impossible for U.S. companies to compete.

The United States had an opportunity to set the rules for economic engagement in the Asia-Pacific with the Trans-Pacific Partnership (TPP), which accounted for 40 percent of global GDP and 20 percent of global trade. A high-quality TPP deal would have given the United States the tools it would have needed to combat China's gray zone tactics by strengthening ties to emerging partners and creating a rules-based order that set the rules for labor, environmental, human rights, and intellectual property standards. Conversely, the U.S. withdrawal from TPP created a vacuum that gave an unbelievable gift to the PRC. They continue to pop champagne in Beijing.

China is playing the long game. For the United States to compete strategically, we must counter China's actions in the economic sphere, especially to promote our goals for an open and prosperous Indo-Pacific. I look forward to hearing from our witnesses on how they believe the United States and similar governments must compete effectively with China in the economic sphere.

QUESTION SUBMITTED FOR THE RECORD

Question for the Record: David Feith

Question from Rep. Waltz

One of the biggest vulnerabilities to collectively confronting China's economic coercion has been the willingness of major European economies like France and Germany to decouple Chinese political behavior from economic behavior. In his trip to China in early April, President Macron behaved particularly egregiously, insisting on strategic autonomy for Europe, arguing against the dollar as reserve currency, and urging against becoming involved with issues like Taiwan. Just a week ago, German Chancellor Olaf Scholz overruled his own Vice Chancellor and security services to allow state-owned Chinese shipping company Cosco to by a quarter of Hamburg's Tollerort shipping terminal. How do France and Germany's actions impede the U.S. building a coalition to resist Chinese economic coercion? How do we ensure that our allies do not ignore China's political behavior because of their economic ties, or worse, actively seek to diminish our own efforts to hold China accountable?