Testimony of Eric C. Anderson
Senior Policy Analyst
Fellow, New Ideas Fund
before the
U.S. China Economic and Security Review Commission
Hearings on China's Propaganda and Influence Operations, It's Intelligence Activities that Target the United States,
and the Resulting Impacts on U.S. National Security
30 April 2009

Good morning Chairwoman Bartholomew, Vice-Chairman Wortzel and Members of the Commission. As a long-time China watcher from within the U.S. Intelligence Community and then as a national security consultant, I thank you for the opportunity to share my views on China's efforts to exercise influence over U.S. financial institutions.

As you are aware, China currently maintains an approximately $2 trillion foreign currency exchange reserve. Roughly half of those reserves are invested in U.S. Treasury notes or other U.S. government bonds. Another $200 billion has been made available to the directors of the China Investment Corporation. At first blush, these large sums bespeak an obvious capability to influence decision makers in Washington and on Wall Street. In fact, however, to date China has been very cautious in attempting to exercise this potential influence.

I come to this conclusion for a number of reasons, but please allow me to open with the most famous case, China's ability to exercise financial "nuclear option." Let me say at the outset, there is no, repeat no, indication Beijing is currently engaged in an effort to sell-off a significant portion of her U.S. Treasury note holdings. While the Chinese leadership has recently expressed concerns about Beijing's U.S. Treasury holdings and wants assurances Beijing's investments are safe,[1] there is no reason to believe China is preparing to wholesale move those funds elsewhere in the immediate future.

Chinese officials, in fact, have gone to great lengths to downplay any discussion of the financial "nuclear option." For instance, in August 2007 the People's Bank of China tried to refute rumors of such a plan by releasing a statement declaring Beijing is "a responsible investor in international financial markets" and that "U.S. dollar assets, including American government bonds, are an important component of China's foreign exchange reserves."[2] Furthermore, Chinese leaders have been quick to call for Beijing and Washington to cooperate in efforts to address the current international financial crisis. As Chinese Premier Wen Jiabao told reports in February 2009, the U.S. and China must "fight the financial crisis and promote constructive and cooperative bilateral

[1] Wen Jiabao, 13 March 2009, "We have lent a huge amount of money to the United States. I request the U.S. to maintain its good credit, to honor its promises and to guarantee the safety of China's assets."
[2] Sim Chi Yin and Bhagyashree Garekar, 13 August 2007, "China Says it will Not Dump U.S. Dollar Assets—Central Bank Official Says they are Important Component of Nation's Forex Reserves," *The Straits Times*, Singapore.

relations."[3] Speaking with reporters from the *Financial Times* on 2 February 2009, Wen declared, "we believe that to maintain cooperation between China and the United States serves world peace, stability, and prosperity."[4]

That said, China is clearly seeking a fix to the current financial crisis that may serve to diminish Washington's dominate role on that front. In late March 2009, Zhou Xiaochuan, the governor of the People's Bank of China, released a paper calling for the establishment of a new "super-sovereign reserve currency" to replace the dollar. In his paper, Zhou said the new currency reserve system should be controlled by the International Monetary Fund (IMF) as a means of avoiding the "inherent vulnerabilities and systemic risks in the existing international monetary system."[5] Despite the fact China currently holds the world's largest foreign exchange reserve, this proposed "super-sovereign reserve currency" is to be supra-national. According to Zhou, the global dominance of a few currencies—the dollar, euro and yen—leaves the international financial system more volatile and vulnerable.

Zhou's solution—expand the use of "special drawing rights." Special drawing rights were an IMF creation in the 1960s. Under this system, the supra-national currency has a value determined by a basket of major currencies. Nations would gain access to these special drawing rights through increased contributions to the International Monetary Fund. As the *Wall Street Journal* observed, this would increase the role and powers of the IMF—indicating "that China and other international developing nations aren't hostile to international financial systems—they just want to have more say in running them."[6]

As it turns out, the *Wall Street Journal* was right on the mark. During the last week of March 2009 Beijing made it would be willing to make more money available to the IMF so as to increase the institution's ability to assist nations ailing as a result of the current financial crisis, but only for greater IMF voting rights. As an economist for Deutsche Bank told the *Journal*, "China sees this as a good opportunity to increase [Beijing's] influence."[7] International financial analysts watching Beijing's apparent power play agreed the request seemed reasonable, but also warned a larger role for China could result in greater scrutiny of banking practices in Europe and the United States. They specifically pointed to a statement People's Bank of China deputy governor Hu Xiaolian made in late March 2009 as evidence of their claim. According to Hu, "under the current situation, [China feels] the IMF particularly needs to strengthen its surveillance of the economic and financial policies of the major reserve-currency-issuing nations."[8]

---

[3] ____, 2 February 2009, "Wen: China, U.S. Should Work Together to Fight Financial Crisis," Xinhua, Beijing.
[4] ____, 2 February 2009, "Wen: China, U.S. Should Work Together to Fight Financial Crisis."
[5] David Barboza, 24 March 2009, "China Urges New Money Reserve to Replace Dollar," *New York Times*, New York.
[6] Andrew Batson, 24 March 2009, "China Takes Aim at Dollar," *Wall Street Journal*, New york, p. A1.
[7] Andrew Batson, 31 March 2009, "China Seeks More Involvement—and More Clout," *Wall Street Journal*, New York, p. A10.
[8] Andrew Batson, 31 March 2009,

So what does China want? This bid for a greater voice in governing the international financial system is indicative of China's broader efforts to level the playing field. Beijing is not seeking to dictate or dominate the conversation, she is simply attempting to ensure non-Western voices have a say at the table. While the proposal to move away from the dollar to an IMF-governed special drawing rights system would diminish Washington's role, China is not attempting to replace the United States. Instead, it really does appear China is seeking to realize a rebalancing of the entire international system—such that, she is able to secure an "ambiguous world order"—one absent U.S. hegemony or regional efforts contrary to China's interests.

China's Sovereign Wealth Fund

Let's return again to China's potential financial "nuclear option." In this case, I would like to specifically focus on China's alternative investment options should Beijing decide to walk away from U.S. Treasury notes. In this case, I will focus on the factors that caused China to establish a sovereign wealth fund. While direct evidence of an internal political debate concerning Beijing's disappointment with the returns offered by U.S. Treasury notes is unlikely to be found, there is circumstantial reporting suggesting just such a discussion is underway in China. For instance, in May 2007 Gao Xiping, Vice Chairman of the National Council for the Social Security Fund, took $3 billion from his agency's coffers to acquire a 9.9% share in the Blackstone Group—a move now considered China's first sovereign wealth fund investment.

In July 2007, an academic from Shanghai's Fudan University published a newspaper article arguing "from a rate of return standpoint…buying U.S. Treasury bonds is not very profitable." As such, the scholar continued, China should take its money elsewhere in an effort to "accelerate" the country's rise.[9] In short, there is little doubt Beijing was aware of the sovereign wealth funds being run from Abu Dhabi, Kuwait, or Singapore. Furthermore, we have little reason to doubt Chinese leaders were aware of the fact they could earn a better return on their investment than that offered by U.S. Treasury notes. (Even if the top leadership was not aware of this situation, one can assume their economic advisors were suitably informed.) All of which suggests high-level discussions driving formation of a Chinese sovereign wealth fund were underway long before Western press sources became aware of the debate.

The second internal political dynamic behind Beijing's establishment of a sovereign wealth fund is to be found with the nation's citizens. Western scholars are increasingly aware of the fact Chinese politicians are susceptible to the winds of change generated by popular opinion. Absent a strong ideological underpinning, and increasingly cognizant of the argument its legitimacy hinges on meeting economic expectations, the Chinese Communist Party seeks to address citizen concerns passed through a growing number of

---

[9] Song Guoyo, 12 July 2007, "Sovereign Wealth Funds Gaining Popularity," *Shanghai Dongfang Zabao,* Shanghai, China.

intermediaries—including the press and Internet.[10] These citizen concerns appear to have been one of the elements that led to formation of the Chinese sovereign wealth fund.

Rumors of public pressure to more productively employ Beijing's growing foreign exchange reserves began to appear in early 2007. Writing for the *International Herald Tribune,* a reporter working from Hong Kong observed, "in postings on domestic Internet message boards and in conversations among educated urban Chinese, critics are suggesting the central bank should earn higher profits from its vast hoard."[11] One Chinese blogger is said to have rhetorically asked, "China has huge amounts of foreign reserves, why doesn't the government put more of it into education?"[12]

So where to invest? Western observers were aware of a debate over the China Investment Corporation's mandate before the institution even opened its doors for business. In an article published in September 2007 *The Wall Street Journal* reported the "fund's mandate has been the subject of contention among Chinese officials." According to the *Journal*, "many involved in the [CIC] planning favor passive investments, by turning money over to professional money managers, with the single goal of improving returns on China's…foreign exchange reserves….Other officials are viewing [the CIC] as a more strategic vehicle, such as to back Chinese state-owned companies as they invest overseas."[13] At the moment, the truth seems to lie somewhere between these two extremes.

CIC officials used the first tranche of $67 billion to acquire Central Huijin and thereby win control of the Chinese government's holdings in the largest three recapitalized, publicly-listed commercial banks—the Industrial and Commercial Bank of China, the Construction Bank of China, and the Bank of China. Financial analysts contend the price of publicly traded shares in these banks suggest CIC received a good deal. The second tranche was dedicated to recapitalizing two other state-owned banks, the China Development Bank and the Agricultural Bank of China. An estimated $20 billion was passed to the China Development Bank, with the ailing Agricultural Bank of China receiving the remaining $40-50 billion.[14]

Why proceed down this path? Commercial gain and the nagging issue of non-performing loans. In 2001, when China won accession to the World Trade Organization, one of the stipulations for Beijing's admittance was opening the country's financial industry to

---

[10] Susan Shirk, 2007, *China: Fragile Superpower—How China's Internal Politics Could Derail Its Peaceful Rise,* Oxford University Press, Oxford, pp. 79-104.

[11] Keith Bradsher, 5 March 2007, "China's Money Woe: Where to Park it All," *International Herald Tribune*, Hong Kong. Similar arguments appeared in Chinese press stories. For an example see: Song Guoyo, 12 July 2007, "Sovereign Wealth Funds Gaining Popularity," *Shanghai Dongfang Zabao,* Shanghai, China. The author goes so far as to argue, "from a rate of returns standpoint…buying U.S. Treasury bonds is not very profitable. The effective rate may even be negative. In fact, higher earnings has precisely been the most important reason why countries have created sovereign wealth funds one after another."

[12] Keith Bradsher, 5 March 2007.

[13] Rick Carew, 28 September 2007.

[14] Clifford Chance, 22 February 2008.

foreign competition. Given the apparently sad state of affairs resident on the balance sheets of China's banks, Beijing was granted a five-year grace period—stalling outside access to the nation's financial industry until 11 December 2006.[15] This delay can be primarily attributed to the fact China's banks had long served as a lifeline for struggling state-owned enterprises. Unwilling to allow these unprofitable businesses to fail, and thereby suffer the political consequences of massive unemployment, Chinese authorities had used the banking industry—more specifically, the population's unparalleled savings rate—to maintain liquidity within the unprofitable enterprises. The result was predictable, a staggering number of non-performing loans.

Beijing has been engaged in an extensive effort to address—and at least nominally resolve—the non-performing loan problem. The first step was to follow a procedure used during the 1997-89 Asian financial crisis and transfer some of the non-performing loans to asset management companies. The second step occurred in 2003, when the Chinese government established Central Huijin—an investment office within the State Administration of Foreign Exchange. In late 2003, Central Huijin "invested" $45 billion from China's foreign exchange reserves in 2 banks—The Bank of China and the China Construction Bank. (A week after announcing this move, the Finance Ministry quietly decided to write-off a $41 billion stake in the two banks in an additional effort to help alleviate their non-performing loan problem.[16])

This fiscal transfer resulted in Central Huijin owning 100% of the Bank of China and 85% of the shares issued by the China Construction Bank. As it turns out, this purchase gave Central Huijin almost exclusive claim to returns realized from the initial public offering of these banks in 2005—a tidy profit according to some Western analysts. In any case, Central Huijin's realized return on its investments at the end of 2004 was estimated to be almost $6 billion—not bad for a firm that had been open for little more than a year.[17]

The third step in Beijing's war on non-performing loans took place on the regulatory front. In 2003, Beijing sought to resolve the problem of poor business practices associated with the non-performing loans by standing up the China Banking Regulatory Commission to supervise and control the country's financial institutions. This move on the regulatory front appears to have fallen short of the mark. In 2004 Chinese authorities resumed their efforts to resolve the non-performing loan problem through further

---

[15] There is considerable debate as to Beijing's willingness to comply with this requirement. Chinese banking regulations concerning outside participation in the country's financial system largely eliminate the possibility of foreign banks opening branches that could directly compete with domestic institutions. For instance, rather than establishing branches, foreign banks are required to incorporate each local operation in China as a Chinese-registered company and each of these entities must have $125 million in registered capital. Second, the minimum deposits for individuals in these companies is $125,000. Finally, any foreign bank not locally incorporated can only offer services to businesses in Yuan—services to individuals can only be done in foreign currency. (____, 5 September 2006, "China: Deferring a Banking Crisis," STRATFOR, Washington DC.)

[16] Keith Bradsher, 14 January 2004, "China to Give Up $41 Billion Stake in 2 Big Banks," *New York Times*, New York.

[17] Victor Shih, 16 August 2005, "Beijing's Bailout of Joint-stock and State-owned Banks," *China Brief*, Volume 5, Issue 18, The Jamestown Foundation, Virginia.

transfers to the asset management companies. Accordingly, these firms purchased another $34 billion in non-performing loans from the Bank of China and the Construction Bank of China—this time at 50% of book value.[18]

What did all this do for the non-performing loan problem? By 2006, the "big four" were reportedly confronted with a non-performing loan ratio of 9.3%.[19] Dollar figures associated with this statistic remain in dispute. Ernst and Young Global issued a revised report in May 2006 claiming the "big four" were then confronted with approximately $133 billion in remaining non-performing loans.[20] The China Banking Regulatory Commission stated overall non-performing loans had declined in value to a total of $160 billion. Western accounting firms immediately dismissed this figure by issuing reports stating the number was likely closer to $475 billion.[21]

Given this background on China's non-performing loan problem—and specifically how that issue was addressed within the "big four" financial institutions—we are now ready for a return to an evaluation of CIC's initial purchases. As stated above, the CIC executive board was apparently caught between those who argued the sovereign wealth fund be strictly used for profit motives, and those who felt the money should be used to assist Chinese firms as they venture into the global market. The Chinese Investment Corporation—as any good Chinese bureaucracy will do—sought a middle ground, thereby probably earning a unanimous vote from the board members.

The first evidence of this effort to find a middle ground came in the form of CIC's acquisition of Central Huijin for an estimated $67 billion.[22] A key participant in Beijing's efforts to prepare China's financial institutions for foreign competition, Central Huijin had become a clearing house for funds headed to the country's ailing banks. The task, while seemingly unproductive, had been lucrative for Central Huijin—as the central bank's investment arm was said to own controlling shares in at least three of the "big four"[23] and had engaged in deals that gave the firm significant interest in a number of smaller banks.[24] Thus a decision to use CIC funds to acquire Central Huijin would turn these profitable holdings over to the Chinese Investment Corporation—a potentially

---

[18] Min Xu, 1 April 2005, "Resolution of Non-Performing Loans in China," The Leonard Stern School of Business, Gluckmans Institute for Research in Securities Markets. The author reports the China Banking Regulatory Commission claims the asset management companies disposed of almost half of the loans acquired between 2000 and 2004 by 31 December 2004.
[19] Kent Matthews, Jianguang Guo, and Nina Zhang, November 2007.
[20] ____, 15 May 2006, "Ernst and Young Withdraws China Bank NPL Report After Acknowledging Errors," AFX News Limited, Forbes.com.
[21] ____, 23 August 2006, "China's Banks in Sound Shape: Bad Loans Drop," Chinadaily.com
[22] Jason Dean and Andrew Batson, 10 September 2007, "China Investment Fund May Tread Softly," *The Wall Street Journal*, New York.
[23] Belinda Cao, 29 September 2007, "China's $200 Billion Sovereign Fund begins Operations," Blomberg.com.
[24] Central Huijin is known to have purchased at least a 6% share in China's fifth largest bank, the Bank of Communications (Rose Yu, 25 March 2008, "China Central Huijin to Transfer 6.12% BoCom Stake to MoF," Dow Jones Newswires) and at least a 70% share in China Everbright Bank (____, 9 November 2007, "Central Huijin to Inject RMB 20 Billion in Everbright," marketinfo.tdctrade.com).

lucrative move—and further bolster the "big four's" move onto the commercial realm by providing monies that could be used to eliminate remaining non-performing loans.

The employment of CIC's second $67 billion tranche also played to the political middle ground. The transfer of funds to the Agricultural Bank of China and China Development Bank helped ready these financial institutions for market listings, and provided the CIC with shares that would almost certainly increase in value after the two banks proceed with initial public offerings.[25] In short, the first two-thirds of the CIC's funding was used to meet its potentially competing missions: assist Chinese firms in their efforts to compete internationally, and generate capital over the long run using "excess" foreign exchange reserves. As such, an American observer could not be faulted for concluding the Chinese sovereign wealth fund's expenditure of almost $140 billion had generated little peril or potential for Washington. But what of the remaining $70 billion?

China's Sovereign Wealth Fund Looks West

The first foreign investment ascribed to the China Investment Corporation came almost six months before the organization was declared officially open for business. In May 2007, China purchased a 9.3% share of the Blackstone Group private equity firm for a reported $3 billion.[26] According to Chinese authorities, the Blackstone investment came with no voice in corporate affairs and was said to have been negotiated with a 4.5% discount on the $31-a-share price listed at the initial public offering on 22 June 2007.[27] Unfortunately for the CIC investors, what had seemed like a good deal soon went astray. By early February 2009, Blackstone share prices had declined to the point the Chinese investors were looking at an 83% loss.[28]

In November 2007, the China Investment Corporation announced its second international investment—$100 million in shares acquired during the China Railway Group's initial public offering. The announcement came as the China Railway Group, a state-owned construction company, prepared for a listing on the Hong Kong Stock exchange.[29]

---

[25] In January 2008, CIC officials announced they would be injecting another $20 billion into the China Development Bank. According to a CIC website posting, the cash infusion will "increase China Development Bank's capital-adequacy ratio, strengthen its ability to prevent risk, and help its bank move toward completely commercialized operations." (Rick Carew, 2 January 2008, "China Taps its Cash Hoard to Beef Up Another Bank," *The Wall Street Journal,* New York; see also, ____, 1 January 2008, "China to Shift $20 Billion as Capital for Policy Bank," *The New York Times,* New York.) Quite frankly, this focus was exactly what Lou Jiwei had promised at the CIC opening ceremony on 29 September 2007—"the new investment company will continue to boost the capital of state-owned financial institutions." (Belinda Cao, 29 September 2007, "China's $200 Billion Sovereign Wealth Fund Begins Operations," Bloomberg.com.)

[26] This investment was underwritten using monies provided by the National Social Security Fund. (Chris Oliver, 27 September 2007, "China Sovereign Wealth Fund Said Set For Launch," MarketWatch.com, New York.)

[27] Keith Bradsher and Joseph Kahn, 29 May 2007, "In China, A Stake in Blackstone Sirs Uncertainty," *New York Times,* New York.

[28] Daniel Kruger, 9 February 2009, "China's Blackstone Pain is Good News for Treasuries," Bloomberg.com.

[29] Rick Carew, 20 November 2007, "China's Sovereign Wealth Fund Forges Strategy, Hunts for Staff," *The Wall Street Journal*, New York.

Western analysts declared the purchase was a "cornerstone" investment that appeared to indicate the CIC was continuing with an acquisition strategy focused on Chinese firms preparing for competition in the global market place. It is too early to determine if similar off-shore acquisition of shares in Chinese firms will occur, but one suspects CIC's hand in the Hong Kong stock exchange—and further cornerstone investment in domestic firms preparing to list there—is going to increase over time.

The CIC's next major overseas purchase came on 19 December 2007, when the Chinese acquired a 9.9% share of Morgan Stanley for a reported $5 billion. Coming on the heels of Morgan Stanley's first-ever reported quarterly loss, the CIC purchase was heralded as a much-needed cash infusion for the U.S. firm and a welcome indication of China's intention to participate in global markets as a stabilizing force. Morgan Stanley officials buttressed this assessment by telling the press CIC had agreed to serve as a passive investor—albeit one they were going to have to pay a fixed annual rate of 9% on a quarterly basis for the next 3 years.[30] Chinese Investment Corporation officials refused to publicly comment on the deal. The silence, perhaps prompted by CIC's Blackstone experience, appears to have been wise. By 1 March 2008, the 9.9% share in Morgan Stanley had declined in value to $4.91 billion.[31] Of note, this loss did not go unnoticed in Beijing. When asked to explain CIC's investment in Morgan Stanley, Lou Jiwei told a World Bank audience, "if we see a big rabbit, we will shoot at it." But, he continued, "some people may say we were shot by Morgan Stanley."[32]

China's dalliance with Western financial institutions continued in February 2008, when word of a potential CIC deal to place $4 billion in a private equity fund operated by the JC Flowers was leaked to the press.[33] The little-known, U.S.-based JC Flowers is run by former Goldman Sachs banker Chris Flowers, and is said to focus on investments in distressed financial institutions—a skill CIC may find handy given its shares in the American and Chinese banking industry. According to news reports, JC Flowers would be responsible for operation of the fund, CIC's would not be involved in day-to-day management issues.[34]

Wary of Western Political Concerns

Given Chinese political sensitivities—and Beijing's concerns about how the world will treat the China Investment Corporation—it only seems fair to ask, what is the CIC investment strategy? For Lou Jiwei, China Investment Corporation's executive board chairman, the public response is academic and obvious: "the purpose is to realize a maximization of long-term investment returns within an acceptable risk range."[35] I

[30] Michael de la Merced and Keith Bradsher, 19 December 2007, "Morgan Stanley to Sell Stake to China Amid Loss," *New York Times,* New York.
[31] William Mellor and Le-Min Lim, 27 February 2008.
[32] Bob Davis, 1 February 2008, "China Investment-Fund Head Says Focus is on 'Portfolios'," *The Wall Street Journal,* New York.
[33] ____, 8 February 2008, "China's Wealth Fund to Invest in JC Flowers Fund," Indiainfoline.com. See also: Paul Maidment, 8 February 2008, "Wealth of Bad Thinking on Sovereign Funds," Forbes.com.
[34] ____, 4 April 2008, "China's CIC Eyes Noncontrolling Company Stakes," REUTERS, New York.
[35] Jason Dean, 1 October 2007, "Can China Fund Meet Tricky Task?" *The Wall Street Journal,* New York.

would note Lou's comments are in line with his contention CIC will have to earn a minimum of $40 million a day to meet the interest on bonds used to finance the fund. This requirement translates into at least $14.6 billion a year in profits—or a return of at least 7.3% on the $200 billion used to establish CIC.[36] Other Western analysts contend a more complicated answer is in order. More than one observer has argued, "now comes the hard part: deploying $200 billion in a way that earns robust returns, satisfies domestic political leaders, and avoids exacerbating anxiety abroad about the [fund's] intentions."[37]

So what will the China Investment Corporation purchase? Early investigations of CIC's purchases—condemned as "politically motivated" by some Western critics of Beijing's sovereign wealth fund—found an executive board apparently operating with little strategic direction. In an interview with a *Financial Times* reporter, a source said to have direct access to Chinese government officials participating in the CIC acquisition decisions declared the fund lacked a clear strategy, but would soon focus on the natural resources sector. The source went on to state the CIC would diversify away from the ailing U.S. financial sector and was seeking approval for this new approach from the central government. Why natural resources? According to the unnamed source, China's large U.S. dollar holdings were rapidly depreciating and Beijing was seeking to address this loss by sinking money in the rapidly appreciating commodity markets.[38]

This push for diversification appears to have won Beijing's approval—and was expanded to include more than simply natural resources. As noted previously, Chinese officials have repeatedly promised much of CIC's offshore activity would be limited to the purchase of indexed funds and a portfolio approach—making many small purchases of equities, bonds, and other investment options.[39] By February 2008, Lou Jiwei had, on more than one occasion, told Western audiences, the Chinese Investment Corporation will focus on "portfolios" rather than target individual firms.[40] In March 2008, Jesse Wang made essentially the same promise, by declaring the CIC would pursue, "highly diversified assets allocation…[this] will help spread the risk as much as possible and increase returns."[41]

A study conducted at the Harvard Business School suggests China—and most sovereign wealth funds—are adhering to this strategy. According to Harvard, sovereign wealth funds are mote likely to invest at home when domestic equity prices are higher, and more likely to invest abroad when foreign prices are higher. (Good business practice.) In addition, Harvard found sovereign wealth funds governed by politicians tended to have a greater likelihood of investing at home, while those relying on external managers display

---

[36] ____, 30 November 2007, "China Wealth Fund Seeks to be a Stabilizing Presence in Global Markets," Xinhua, Beijing.
[37] Jason Dean, 1 October 2007.
[38] Tan Wei, 30 December 2007, "China's CIC likely to Diversify away from Further U.S. Banking Sector Investments, Source Says," *Financial Times*, London.
[39] Keith Bradsher, 29 November 2007, "$200 Billion to Invest, But in China," *The New York Times*, New York.
[40] Bob Davis, 1 February 2008.
[41] ____, 3 March 2008, "China Sovereign Wealth Fund to Target Range of Assets: Report," Agency France Press, Shanghai.

a lower tendency to follow this pattern.[42] The China Investment Corporation is following these patterns. In mid-February 2009, the Chinese sovereign wealth fund was found to be focusing on resources (minerals), property (globally) and fixed income assets (U.S. Treasury notes).[43] As Jesse Wang told reporters, “we are interested in basic necessities, resources, and manufacturing because we want to balance our investment portfolio.”[44] By mid-April 2009, China Investment Corporation officers were announcing plans to expand their investments even further. As Lou Jiwei put it, “Key countries in Europe are now welcoming us. So we’ll actively consider that, because we have also discovered some opportunities.”[45]

Conclusion

I can find little evidence suggesting Beijing is engaged in a wide-spread effort to influence U.S. financial institutions and thereby threaten our national security. Rather, I would argue China is seeking to participate in the international financial system as an honest broker who realizes she has much to lose by engendering suspicion and/or abetting havoc. My extensive study of the China Investment Corporation’s investment strategy indicates Beijing is using her sovereign wealth fund to generate a profit for Chinese taxpayers—not undermine Wall Street or the U.S. Treasury. As such, China is simply following in the footsteps of other nations—some of whom have been operating sovereign wealth funds for over 50 years.

In short, I can find no evidence suggesting the China is using her foreign exchange reserve to coerce the West—Beijing realizes employment of the fiscal “nuclear option” would have a devastating impact on China’s own economic future. What then is the peril the China Investment Corporation presents to America? The peril—for the moment—appears largely confined to short-term reinvigoration of jingoistic sentiments and proposals to revisit protectionist legislation aimed at preserving American national security from an amorphous “threat.” Over a longer course of time, however, the CIC peril may be profound. It is not that the Chinese will purchase U.S. sovereignty—quite the contrary. The long term peril is that CIC—and many other profit-oriented customers—will go shopping for investments offering a greater return than that provided by U.S. government securities

[42] Shai Bernstein, Josh Lerner, and Antoinette Schoar, 2009, “The Investment Strategies of Sovereign Wealth Funds,” Working Paper 09-112, Harvard Business School, Harvard University, pp. 3-4..
[43] George Chen, 19 February 2009, “CIC Shifting Focus,” REUTERS, Hong Kong.
[44] George Chen and Xie Heng, 4 March 2009, “China’s CIC Sees Opportunities in Natural Resources,” REUTERS, Beijing.
[45] Jason Dean, 18 April 2009, “China Wealth Fund to Boost Investments,” *Wall Street Journal,* New York.

Filename:	USCC_Eric Anderson_testimony 4-20-09
Directory:	C:\Documents and Settings\Jertman\Local Settings\Temporary Internet Files\OLK5E
Template:	C:\Documents and Settings\Jertman\Application Data\Microsoft\Templates\Normal.dot
Title:	Testimony of Eric C
Subject:	
Author:	ecander
Keywords:	
Comments:	
Creation Date:	4/20/2009 12:53:00 PM
Change Number:	2
Last Saved On:	4/20/2009 12:53:00 PM
Last Saved By:	Kathy
Total Editing Time:	5 Minutes
Last Printed On:	4/30/2009 8:16:00 AM

As of Last Complete Printing

Number of Pages: 10

Number of Words: 4,045 (approx.)

Number of Characters: 22,011 (approx.)