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Remarks to the U.S.-China Economic and Security Review Commission

Senator Jim Webb
February 7, 2008

I would like to thank Commissioners Pat Mulloy and Larry Wortzel for their invitation to speak today. I applaud the decision of the U.S.-China Economic and Security Review Commission to hold a hearing regarding China's sovereign wealth fund.

Let me take a few moments to make some general remarks regarding sovereign wealth funds. Then I would like to speak briefly about the political, national security, and economic implications of the growth of these funds. I will conclude by raising issues for follow-up by Congress and the U.S.-China Economic and Security Review Commission.

Although foreign governments have been investing in the United States through various investment vehicles, sovereign wealth funds have captured the attention of lawmakers as the funds increase their footprint in the U.S. economy. According to the International Monetary Fund, while currently valued at $2.2 trillion, sovereign wealth funds could be worth over $10 trillion within five years. With sufficient foreign exchange reserves to cushion against economic shocks, foreign governments are seeking investment alternatives to U.S. Treasury securities.

But what we're seeing is not merely private foreign investment—it is foreign government investment, which raises new policy questions for which we do not have all the answers.

Governments are motivated by a broader range of factors than commercial investors. While foreign governments may invest money in our country to make a profit, they may also do so in order to further their foreign policy ambitions, to acquire national security assets, or to purchase a stake in strategic industries. Gerard Lyons, the global head of treasury research at Standard Chartered Bank, coined the phrase "State Capitalism" to describe the phenomenon of sovereign wealth funds.

Some commentators are quick to levy warnings of "protectionism" in relation to any concerns that are expressed regarding the potential impact of sovereign wealth funds. Their critique falls wide of the mark. No one is advocating building a wall around our country. I welcome investment that promotes economic growth and generates good jobs for American workers. But such investment must do so in a manner consistent with protecting U.S. national security and the stability of U.S. markets.

Congress has an important role to play in making sure these concerns are addressed. We don't fully understand what these funds mean for our country and there are serious policy questions that need to be raised. Let me address a few of these concerns in turn.

The investments made by sovereign wealth funds are largely discussed as politically benign, but it would be naïve to assume other motivations will not enter into the picture. The Qatari Investment Authority's recent failed effort regarding J. Sainsbury in the United Kingdom included an aggressive effort to seek management control.

Norway, which is held up as the model for sovereign wealth funds, incurred the ire of Iceland when it sold short on bonds issued by its banks, a move perceived as undermining Iceland's economy. Iceland's prime minister at the time protested vehemently. What will we do when a fund takes such actions in relation to the United States?

As Felix Rohatyn has noted, the difference between sovereign wealth funds and other foreign investment is "the political element" and the desire of the funds to play a more prominent global role. Undoubtedly some funds are interested solely in their financial return and will invest like a commercial investor, but we should not presume that all funds will act in this manner.

All proposed foreign investments that have national security implications are potentially subject to review by the Committee on Foreign Investment in the United States. I have been particularly concerned regarding passive investments that may nonetheless provide foreign governments and state-owned corporations with control over sensitive national security information.

Holding a small minority of shares or not taking a board seat does not provide a guarantee that there will be no influence or control. For example, Saudi Prince Walid Bin Talal, who holds a 3.9 percent stake in Citibank, was closely consulted in the ouster of Chuck Prince from Citibank as its CEO. Prince Bin Talal does not sit on the board. You do not need a seat on the board, however, to have a seat at the table.

Prince Bin Talal has invested his money, not his government's, and he is held up as a responsible and conscientious investor. The Prince's role in another Prince's ouster, however, speaks volumes to those who suggest that you need to be on the board to exert influence.

In September, I, along with the Chairman Dodd and Ranking Member Shelby of the Banking Committee, and Chairman Bayh of the Subcommittee on Security and International Trade and Finance, sent a letter to Treasury Secretary Paulson. The letter requested that the Committee for Foreign Investment in the United States examine passive foreign ownership interests in assets in the United States, including through sovereign investment funds.

The letter urged the Treasury Department to draft regulations, which will be issued this month, which are broad enough to ensure that potential national security implications of such investments are appropriately assessed in the context of ongoing foreign investments in the U.S. economy. In December, I participated in a Banking Committee hearing regarding the implications of sovereign wealth funds.

Sovereign wealth funds are now large enough to shift markets. At the core of maintaining market stability is transparency and the free flow of information. Unfortunately, some sovereign wealth funds operate, in effect, in a black box. Decision-making is opaque and their investment strategies are known only to a few. While I applaud the efforts of the Treasury Department to work with the International Monetary Fund, the World Bank, and the Organization for Economic Cooperation and Development to promote transparency and best practices, there is a legitimate question to be asked regarding compliance with the standards that these institutions will establish: how will a mechanism that relies, in effect, on peer pressure ensure compliance among the least transparent sovereign wealth funds?

Lastly, the issue underlying this discussion is the transfer of our productive wealth away from the United States, a trend that imperils our economic well-being. Our need for the inflow of capital is unsustainable. As Jeffrey Garten at Yale noted regarding sovereign wealth funds, the "U.S. is going to be extremely vulnerable for a long period of time because we're so hooked on foreign capital."

Although the investment by sovereign wealth funds represents a small proportion of overall flows of foreign capital into the United States, it affords the opportunity to highlight the precarious financial position our country is in. We cannot keep selling off our country; we cannot continue our excesses of spending and borrowing; and above all, American Capitalism must be reminded to nurture the democracy that allowed it to thrive.

With a tight credit market, we can expect to see investment by sovereign wealth funds continue to grow. As such, we need to ensure that our policies protect our national security and our economy from the risks associated with these funds.

We must ensure that we are taking adequate stock of a foreign government's strategic priorities when we review the national security implications of particular transactions. We need to ensure that our laws and policies distinguish between politically motivated sovereign investment and commercially motivated sovereign investment. We need to closely scrutinize strategically motivated investments, and adequately define "control" of U.S. assets, which triggers review by the Committee on Foreign Investment in the United States. And we need to design strict controls regarding the type and extent of such investments by foreign governments. Congress also needs to maintain close oversight of the Committee on Foreign Investment in the United States.

Any efforts that the U.S.-China Economic and Security Review Commission can make to further these goals, by collecting relevant information and data, would be helpful to Congress.

I intend to stay engaged on these important issues. Thank you for your time and attention.