



U.S.-CHINA ECONOMIC AND SECURITY  
REVIEW COMMISSION

***Hearing on “China’s High Technology Development”***

**Opening Statement of  
Patrick A. Mulloy  
Commissioner & Hearing Co-Chair**

**April 21, 2005  
Stanford, CA**

I would like to join the Chairman and Vice Chairman in expressing the Commission’s appreciation to Stanford, our former colleague Ambassador Ellsworth, and all the others that have made this event possible. The issues we are discussing today are vital to the long-term economic interests of the United States, and it is important that we discuss them in Silicon Valley, the nation’s hub of technology development and innovation.

The realities of China’s rapid economic advancement are well known. What is perhaps less well understood, however, is the broad spectrum of industries, including advanced technology sectors, for which China poses competitive challenges to the U.S. economy. A recent report prepared for the Commission by the Economic Policy Institute concluded that “China’s exports to the United States of electronics, computers, and communications equipment, along with other products that use more highly skilled labor and advanced technologies, are growing much faster than its exports of low-value, labor-intensive items such as apparel, shoes, and plastic products.” The report further found, remarkably, that the United States is now running a \$32 billion trade deficit with China in goods classified by the U.S. Department of Commerce as Advanced Technology Products.

The U.S. technology industry is clearly taking note of these dynamics. In its 2005 report, entitled *Losing the Competitive Advantage*, the American Electronics Association, whose president, Bill Archey will be testifying later this afternoon, made several key findings: First, “America needs to recognize that future innovation is not predetermined to occur in the United States” and that “even if we were doing everything right, we still face unprecedented competition from abroad.” Second, that “China is already the world’s manufacturing hub and now is moving up the production line to promote higher end technology firms, creating sobering competition for companies and workers around the world.”

Policy-makers in Washington need to understand what is driving the rapid advancement of China’s technology sectors. While some observers see this as the inevitable result of global market forces, there appears to be more to it than that. As the Commission’s past work has documented, the Chinese government is following a coordinated and comprehensive strategy, coupled with policy incentives, to build up its technology capabilities and foster the emergence of globally competitive companies.

As highlighted in the Commission's 2004 Report to Congress, the two key components of China's technology strategy are (i) to encourage foreign investment in areas where domestic capabilities are lacking and (ii) to limit foreign access to markets where domestic industries are gaining economies of scale. One such policy is the requirement that only domestic software or "qualifying foreign software" may be purchased by government entities. The criteria for qualifying foreign software have yet to be defined. The absence of such criteria has inhibited U.S. manufacturers from entering into government business and appears intended to shut foreign firms out of this lucrative market.

A second example is China's development of unique technology standards. By creating such standards, China has attempted to use its market leverage to promote standards that it controls, such as for wireless communication and digital music, rather than internationally recognized standards that are already in wide use. We will hear extensive testimony on this practice during the hearing.

I do not fault China for having a well thought-through, well-coordinated strategy to build up its technology competitiveness. Instead, I am concerned about the U.S. response. Technology competitiveness and innovation is a signature of our economic well-being and we cannot allow our competitiveness to wane. As we recommended in our 2004 Report to Congress, "the U.S. government must develop a coordinated, comprehensive national policy and strategy designed to meet China's challenge to the maintenance of our scientific and technological leadership," along the lines of the national security strategy that is currently developed to address our global military and political challenges.

This afternoon we continue our discussion with a panel of renowned observers of the U.S.-China high-tech trade and investment relationship: Henry Rowen, from right here at the Hoover Institution, Ernest Preeg of the Manufacturers Alliance, Eamonn Fingleton, author of *"Unsustainable: How Economic Dogma is Destroying American Prosperity,"* and Professor John Zysman of UC Berkeley who authored, among other books, *"Manufacturing Matters: The Myth of the Post-Industrial Economy."*

They will be followed by a panel examining the challenges China poses over the long-term to U.S. technology leadership. We are pleased to have with us Bill Archey, President of the American Electronics Association, Rhett Dawson, President and CEO of the Information Technology Industry Council, and John Ciacchella, Vice President at AT Kearney. Mr Ciacchella conducted two studies this past year; one exploring the economic impact of offshore outsourcing on the Bay Area, and another (due out soon) consisting of interviews with 300 high-tech leaders assessing their competitiveness in today's market.

Thank you all for being here today, I look forward to this afternoon's panels and tomorrow's session.