Hearing on "Risks, Rewards, and Results: U.S. Companies in China and Chinese Companies in the United States"

Thursday, February 28, 2019
Hart Senate Office Building, Room 216
Washington, DC 20002

Opening Statement of Vice Chair Cleveland

Thank you, Commissioner Wessel, and good morning everyone. I want to thank our witnesses for joining us today and for the thought and consideration they have given their testimonies.

When China joined the WTO, it was the sixth largest economy in terms of nominal GDP. American companies were attracted to the large and rapidly growing market in spite of concerns about restrictions on investment opportunities, a lack of regulatory transparency and inconsistent enforcement of rules and law. Today China is the world's second largest economy and the world's leading exporter yet perceptions of both risk and reward for the global private sector remain largely unchanged. The Australian Chamber of Commerce reported last year that more than two thirds of their companies find it difficult to do business in China yet remain committed because of the "rise of the middle class." Similarly, the American Chamber notes that 75% of their members feel unwelcome and believe foreign invested companies are not treated fairly yet their annual report notes revenues are up across sectors and it concludes that China's growth rate will continue to provide opportunities for expansion.

It is this dichotomy that our hearing today will address. On the one hand, Chinese consumers and the broader market represent obvious opportunity. On the other hand, evidence suggests the Chinese Communist Party has skillfully and consistently protected their interests, particularly in state-owned enterprises. Evidence of this protectionism is the exhaustive government lists which explicitly restrict or ban American investments in Chinese companies. I am interested in how this list has evolved over the years but it is not the exclusive means of protecting Chinese interests. The subtler version of this game seems to play out in the Party's approach to negotiations over market access for non-Chinese companies. While these innovative, competitive firms engage in endless negotiations over the terms of entry, Chinese companies and, indeed, entire industries are protected and given room to grow a customer base. By the time foreign companies finally are provided access, market loyalty and share have been locked up.

These constraints on direct foreign investment in China have contributed to the surge in reverse mergers and initial public offerings allowing Chinese companies to raise capital in the United States. As Commissioner Wessel noted, we have released a summary today reporting on the $1.2 trillion that American households and investors have committed to capitalize Chinese companies. American retirement accounts and mutual funds have invested in virtually every sector from transportation and biogenetics to energy and consumer goods. In reading the annual reports for many of these enterprises, I have been struck by the unvarnished praise heaped upon the Communist Party for commercial achievements.

In return for providing 41% of global market capitalization in 2017, U.S. exchanges and investors assume U.S. rules, standards and regulatory oversight protect their investments. Companies raising capital in U.S. markets are required by law to submit to the SEC financial statements prepared by registered auditing firms. In turn, those auditors agree to inspections by the PCAOB. Together the SEC and PCAOB identify and monitor risk, prevent fraud and protect investors. Access to timely information is essential to protecting investors.

China is a large, notable, and longstanding exception to this cooperation. In a recent statement, the Chairmen of the SEC and PCAOB described the limits imposed by the Chinese government on U.S. regulators' access to business books, records and audit work papers of U.S.-listed Chinese companies. PCAOB further faces restrictions on attempts to inspect audit work and accounting practices of PCAOB-registered firms. The data we are releasing today indicates how large a risk this is to financial markets and, thus, American households. $1.2 trillion in American capital market investments have been made into a black box.

I supported China's accession to the WTO, and for many years expected free market fundamentals to take root in China's economy. Regrettably, more recent evidence suggests that has not happened. While the CCP restricts ownership or operation of gas stations, China Petroleum and Chemical Corporation can raise $3.5 billion from U.S. households. MasterCard, PayPal and Amazon cannot gain access to Chinese consumers, yet Alibaba and its subsidiaries have raised $21 billion through a Cayman island holding company pumping up their market valuation to $433 billion.

I would like to believe these are sound investments for American households, but without credible financial statements and audit inspections, it is impossible to say. I look forward to hearing from our panelists today on their understanding of how level, accountable and fair the field is for both Chinese companies here and American companies in China.

As we begin, I would like to remind our audience that the testimonies and transcript from today's hearing will be posted on our website, www.uscc.gov. Finally, I will take the opportunity to advertise the Commission's upcoming hearing on March 21, "An Emerging China Russia Axis? Implications for the United States in an Era of Strategic Competition."