

**CHINA'S PROPAGANDA AND INFLUENCE
OPERATIONS, ITS INTELLIGENCE ACTIVITIES THAT
TARGET THE UNITED STATES, AND THE RESULTING
IMPACTS ON U.S. NATIONAL SECURITY**

HEARING

BEFORE THE

U.S.-CHINA ECONOMIC AND SECURITY
REVIEW COMMISSION

ONE HUNDRED ELEVENTH CONGRESS

FIRST SESSION

APRIL 30, 2009

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WASHINGTON : JUNE 2009

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The Commission's full charter is available at www.uscc.gov.

May 26, 2009

The Honorable ROBERT C. BYRD

President Pro Tempore of the Senate, Washington, D.C. 20510

The Honorable NANCY PELOSI

Speaker of the House of Representatives, Washington, D.C. 20515

DEAR SENATOR BYRD AND SPEAKER PELOSI:

We are pleased to transmit the record of our April 30, 2009 public hearing on “*China’s Propaganda and Influence Operations, Its Intelligence Activities that Target the United States, and the Resulting Impacts on U.S. National Security.*” The Floyd D. Spence National Defense Authorization Act (amended by Pub. L. No. 109-108, section 635(a)) provides the basis for this hearing, stating that the Commission shall examine “...the triangular economic and security relationship among the United States, Taipei and the People’s Republic of China,” as well as “...the implications of restrictions on speech and access to information in the People’s Republic of China for its relations with the United States in the areas of economic and security policy.”

The first panel of the day examined the Chinese government’s propaganda directed to foreign audiences, and the extent to which this might affect U.S.-China relations. Dr. Nicholas J. Cull, professor of public diplomacy at the University of Southern California, opened the panel with a discussion of China’s public diplomacy, which he defined as “the process by which an international actor conducts foreign policy by engaging a foreign public.” He identified five components in this process: listening, advocacy, cultural diplomacy, exchange diplomacy, and international broadcasting, and maintained that the People’s Republic of China (PRC) engages actively in all of them. He also described an effort by the PRC to “buy friends” by cultivating influential figures in developing countries, and advised that such efforts could be successful in displacing western influence and values throughout much of the world. In response, he advocated renewed efforts for U.S. public diplomacy, particularly through the expansion or revival of U.S.-supported news broadcasting. Next, Dr. Judy Polumbaum, professor of journalism and mass communications at the University of Iowa, focused on the role of journalists within China’s state-controlled media system. She emphasized that China’s media system is not monolithic, and that different institutional actors may have differing outlooks and interests. She also stated that China’s reported plan to expand English-language media outlets does not necessarily represent a systematic effort to enhance the PRC’s foreign propaganda, but might be explained at least in part as bureaucratic “empire building” by actors such as the Xinhua state news agency. Finally, Dr. Anne-Marie Brady, associate professor of political science at the University of Canterbury, New Zealand, discussed the Chinese Communist Party (CCP)’s efforts to take a less visible hand in direction of the state media—to employ “management” rather than “control”—and to make its propaganda more convincing and effective through the adoption of western practices. Despite this seemingly softer touch, Dr. Brady emphasized the continuing critical importance of propaganda as the “life blood of the Party” and its effort

to maintain itself in power.

Witnesses in the second panel examined ways in which the Chinese government has allegedly sought to levy influence over U.S. institutions. Dr. Ross Terrill, associate in research with the John K. Fairbank Center for Chinese Studies at Harvard University, testified about PRC efforts to influence the writings of U.S. opinion-makers such as academics and think tank researchers. He described both coercive steps, such as the denial of visas to writers who angered the Chinese government, as well as more subtle efforts to co-opt scholars and institutions through financial donations made by parties friendly to Beijing's views. In response, he recommended that the United States resist such efforts to "pick winners and losers" among academics who study China. Following these remarks, Dr. Eric Anderson, analyst with Science Applications International Corporation, described in his testimony alleged efforts by the PRC to gain leverage over U.S. policy through state-backed investments in the U.S. financial sector. Dr. Anderson concluded that no signs of such efforts could be found, and that Chinese investments were benign actions undertaken in the expectation of profitable returns. The last speaker of the panel, Dr. Jacqueline Newmyer, President and CEO of the Long-Term Strategy Project, analyzed alleged PRC efforts to influence U.S. institutions within the broader context of PRC foreign policy strategy. In her testimony, she described an active and coordinated effort by the PRC authorities to manipulate foreign perceptions of China's rise and future course, supporting this assertion with quotations from internal, restricted-distribution CCP publications. As cited by Dr. Newmyer, these documents called for the use of "public relations weapons"—such as the cultivation of prominent people and media outlets in other countries—to create a benign and reassuring image of China.

The third panel discussed the extent of Chinese espionage directed against the United States. Drawing upon 25 years of service with the FBI, Mr. I.C. Smith, a former special agent with the Federal Bureau of Investigation, observed that the PRC views the United States as its "number one adversary," and he also directly stated his opinion that the PRC represented the "number one threat to the United States." He described the Chinese model of espionage as relying heavily on seeking to recruit or intimidate Americans of Chinese heritage into performing tasks on behalf of the Chinese government. He also noted the decentralized and frequently amateur nature of Chinese intelligence gathering, particularly as it pertains to the acquisition of technology. Mr. Smith warned that the large numbers of Chinese students entering the United States would include many students either encouraged or intimidated by the government into seeking out technological acquisitions on behalf of the PRC. He advised "stricter reciprocity in dealing with the PRC," to include possibly cutting the number of visas granted to Chinese students. Dr. James Mulvenon, director of the Center for Intelligence Research and Analysis, Defense Group, Incorporated, focused his remarks on economic espionage carried out by "espionage entrepreneurs" who did not possess any formal intelligence training. He identified the PRC as the largest perpetrator of economic espionage against the United States, and described extensive "mom and pop" operations directed at acquiring technology through "secondary market distributors," as well as via exports that involved the obfuscation of end users. By way of response, he advised that the United States apply a means-ends test in order to best focus on items that the Chinese

seek to acquire in order to fill gaps in their military capabilities, and to work more closely with the Hong Kong authorities to block transshipments of dual-use technology.

The hearing's final panel examined Chinese cyber espionage directed against the United States. In his testimony, Mr. Kevin Coleman, senior fellow with the Technolytics Institute, assessed that "we are in the early stages of a cyber arms race," and presented a stern warning that the United States is not adequately prepared for the level of cyber threat that it currently faces. He opined that China, in particular, was the source of four times as many cyber attacks against U.S. targets as any other country. Next, Mr. Rafal Rohozinski, principal with the SecDev Group of Ottawa, Canada, described his recent research analyzing a cyber-espionage network called "Ghost Net" that had infected over 1,200 computers of government and other political entities in 103 different countries. His organization traced the control servers for this network back to China; and while he could not conclusively prove PRC government involvement, he opined that aspects of Ghost Net's activities showed signs of consciously directed intelligence collection whose effective exploitation would require resources beyond that of a private actor. However, Mr. Rohozinski counseled against implementing overly restrictive internet security that would "throw the baby" of the internet's benefits "out with the bathwater," and recommended instead improving awareness of, and training in, existing internet security practices.

The prepared statements of the hearing witnesses can be found on the Commission's website at www.uscc.gov, and the complete hearing transcript also will be made available on the website. Members of the Commission are available to provide more detailed briefings. We hope the information from this hearing will be helpful as the Congress continues its assessment of U.S.-China relations. The Commission will examine these issues in greater depth, together with the other issues enumerated in its statutory mandate, in its 2009 Annual Report that will be submitted to Congress in November 2009.

Sincerely yours,



Carolyn Bartholomew
Chairman



Larry M. Wortzel, Ph.D.
Vice Chairman

cc: Members of Congress and Congressional Staff

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**CHINA'S PROPAGANDA AND INFLUENCE
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RESULTING IMPACTS ON U.S. NATIONAL
SECURITY**

THURSDAY, APRIL 30, 2009

U.S.-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION

Washington, D.C.

The Commission met in Room 485, Russell Senate Office Building at 9:00 a.m.

**OPENING STATEMENT OF COMMISSIONER WILLIAM A.
REINSCH, HEARING COCHAIR**

HEARING COCHAIR REINSCH: Good morning, everyone. On behalf of our Chair, Carolyn Bartholomew, who will be joining us later, and our Vice Chair, Larry Wortzel, who will also be joining us later, and the other members of the U.S.-China Economic and Security Review Commission, I'd like to welcome all of you to this hearing, the fourth this year to examine issues related to our statutory mandate from Congress.

Today, we will examine issues related to the Chinese government's propaganda directed at foreign audiences, its alleged efforts to exert influence over U.S. institutions and U.S. public opinion, and its espionage and cyber espionage activities directed against the United States.

We're going to be talking about things that all governments do in

one form or another. Governments seek to influence public opinion: that of their own people and that of others. Governments apparently like to be loved as much as people like to be loved. What we are trying to understand today is how the Chinese do it, what tactics they employ, and to some extent what the results are?

Many issues related to these topics have been significant points of controversy in recent years. For example, are the reported plans of the Chinese government to substantially increase its news coverage and publicity efforts directed at foreign audiences a cause for any concern in the United States, or do these efforts represent benign public diplomacy efforts of the type used by nearly all governments?

Does the Chinese government seek undue influence over academics and other shapers of opinion in the United States by exerting personal pressure on them?

What is the extent to which Chinese intelligence operations target control technologies and restricted information, and to what extent do such efforts affect U.S. national security and our future economic competitiveness?

It's our hope that this hearing will help to shed more light on some of these debates and help to better inform the Commission as we prepare our annual report to Congress later this year.

We're joined today by a number of truly exceptional witnesses, experts in these fields, who will help us further explore these issues.

They include academic authorities on Chinese politics and propaganda, national security experts from the defense consulting community, a retired agent of the FBI, and expert researchers in the field of cyber security. We welcome their presence with us today, and we look forward to hearing their views on these issues.

With that, let me turn the floor over to my colleague and the cochair for this hearing, Commissioner Peter Brookes.

OPENING STATEMENT OF COMMISSIONER PETER T.R. BROOKES, HEARING COCHAIR

HEARING COCHAIR BROOKES: Thank you, Bill, and thank you for that introduction. Good morning, everyone, and welcome. I'll make a short statement here for the record, and then we'll get started with this morning's hearing.

The topics of today's hearings have been made all the more relevant and timely by a series of recent media revelations related to the Chinese government's employment of propaganda, intelligence operations and cyber espionage in its relations with the United States.

Early this year, media reports emerged that the Chinese government plans to spend an estimated 45 billion renminbi, or

approximately 6.6 billion U.S. dollars, to update its foreign language news service, to include plans for a 24-hour English-language news network that would represent world affairs from the viewpoint of Beijing.

While it is the right of every government to seek to peacefully promote its views to international audiences, it is also prudent to examine the effects that such propaganda effects could have on U.S.-China relations.

Even more striking, however, and of greater concern, have been recent revelations of alleged Chinese espionage against the United States. In just one such example, among many others, earlier this month, the owner of a firm in Newport News, Virginia was sentenced for illegally exporting Chinese technical data related to systems components for space launch vehicles.

This has been followed by alleged hacker penetrations into defense contractor computer systems related to the development of our most advanced fighter, the F-35, as well as alleged mapping of the computer networks that control electrical grids within the United States.

While public identification of the hackers in these instances has not been conclusive, the electronic trails in both instances have reportedly led back to China.

Whether coming in human or electronic form, such espionage is of serious concern to both the national security and future economic security of the United States. We at the Commission hope that our efforts this year will help to further clarify these complex issues for both the Congress and the broader public.

With that, I'll turn it over to Commissioner Reinsch who will commence the first panel today.

HEARING COCHAIR REINSCH: Thank you.

Before I introduce the panelists, let me simply say procedurally your entire statements will be put in the Commission's record so we're hoping that you'll summarize them, and we've allocated seven minutes to each of you to do that.

There's no timer I'm told, but just watch the lights. Unlike during the Cultural Revolution, red means stop, not go. So the red light will go on at seven, and since there are just three of you, you don't need to stop in mid-sentence but take that as a clue, and as I said, your full statements will be in the record.

We'll proceed with all three of you in the order in which I'm about to introduce you, and then we'll open all three of you up to questions when you have concluded your panel.

The first panel consists of Dr. Nicholas Cull, who is Professor of Public Diplomacy and Director of the Masters Program in Public

Diplomacy at the University of Southern California. He is also President of the International Association for Media and History, a member of the Public Diplomacy Council, and has worked closely with the British Council's Counterpoint Think Tank.

Much of his work has focused on the role of culture, information, news and propaganda in foreign policy. He contributed the chapter "The Public Diplomacy of the Modern Olympic Games and China's Soft Power Strategy" to *Owning the Olympics: Narratives of the New China*.

He is also the author of *The Cold War and the United States Information Agency: American Propaganda and Public Diplomacy*.

Dr. Judy Polumbaum is a Professor of Journalism and Mass Communications at the University of Iowa where she has taught since 1989. Her research focuses on journalism and media in mainland China. She has worked as a newspaper reporter in Vermont, California and Oregon. She taught journalism at the Chinese Academy of Social Sciences postgraduate school from 1979 to 1980 and worked as a writer and editor for the national English-language publication China Daily during its first year of publication.

She has a bachelor's degree in East Asian Studies from McGill University, a master's from Columbia Graduate School of Journalism, and a doctorate in Communication from Stanford.

Her most recent book is *China Ink: The Changing Face of Chinese Journalism*. Great pun.

Winning the award for the farthest traveler not only for this panel, but I think for all time in the Commission's history, is Dr. Anne-Marie Brady, who is an Associate-Professor of Political Science at the University of Canterbury, New Zealand, who specializes in researching Chinese domestic and foreign politics.

Dr. Brady has written several books and numerous scholarly articles on Chinese politics. She graduated from the University of Auckland with both a B.A. and an M.A. in Chinese and Politics. She received her Ph.D. in East Asian Studies: International Relations from the Australian National University.

In 2005, Dr. Brady was awarded a three-year research grant by the Marsden Fund of the Royal Society of New Zealand to set up an international research team on the topic of China's propaganda system.

In 2008, she researched and produced a BBC radio documentary: "The Message from China," which discusses the modernization of the Chinese domestic and foreign propaganda system.

So with that, why don't we proceed with Dr. Cull and Dr. Polumbaum and Dr. Brady in that order.

Thank you.

**STATEMENT OF DR. NICHOLAS J. CULL
PROFESSOR OF PUBLIC DIPLOMACY, UNIVERSITY OF
SOUTHERN CALIFORNIA, LOS ANGELES, CALIFORNIA**

DR. CULL: Thank you.

I'd like to thank the Commission for the invitation to be here today and to speak about this subject because I think it's a crucial subject for the interests of the United States and of the West more generally, and as you'll detect, I'm not an American. But I feel this is of concern to your allies as well as yourselves, and the subject of China, China on the move, especially in this field of media and public diplomacy.

As I see public diplomacy, it's divided into five elements through which an international actor conducts foreign policy by engaging a foreign public. Those elements are: listening; advocacy; cultural diplomacy; exchange diplomacy; and international broadcasting. And China is moving in all five of these fields.

In its listening, it is collating data, conducting opinion polls, analyzing this, and changing policies, changing its rhetoric, and feeding this into its foreign policy, developing a network of embassies around the world, of posts, expanding its diplomatic posts around the world.

In terms of advocacy, it's making sure that it's getting its message out, further expanding the network of news agency posts.

In terms of its cultural diplomacy, we see the amazing investment in Confucius Institutes. It looks as if we'll be at the total of 200 worldwide by early next year. We see large-scale international student recruitment. We see the expansion in international broadcasting of the plan to launch the 24-hour news network, and the new English language newspaper that they're talking about developing.

We also see this initiative around the world to promote China really by buying friends, through lavish aid programs, and open-handedness to developing nations at a time when the United States and Western allies are increasingly asking for political reform as a price for aid, and I think this is a challenge.

It's interesting to see when you're analyzing Chinese rhetoric and the debate around foreign policy within China, how China has latched onto the idea of soft power and is looking to leverage soft power, and of course this was really obvious in the Olympics. It will be obvious again in the Shanghai Exposition.

I feel that China is doing nothing intrinsically wrong in having a public diplomacy drive to engage the opinion of the world; it's a wise policy from China's point of view. What would be wrong would be for us to ignore it, and the appropriate response of the West should be to

meet the overtures for exchange in the spirit in which they're intended and to accept opportunities to know China better and facilitate China's knowing more of the West.

But equally where China is challenging the Western presence, where China is displacing Western voices, and especially in its displacement of things like Western media partners in Africa, which we are now seeing, I think that the United States specifically needs to raise its game in its own public diplomacy.

I don't think that the United States needs to expand its public diplomacy solely to keep pace with China anymore than it should do so solely to prevail over radical Islam, but I do believe that the United States needs to expand its public diplomacy because this is an essential element of foreign policy in the 21st century, and in an age when power increasingly rests on public opinion, success requires effectively engaging with the people, and anything that this Commission can do to encourage the rebuilding of America's public diplomacy I think would be a wise investment in the future of this country and the ideals on which it's built.

Thank you, again, for inviting me here today.
[The statement follows:]

*Testimony before the US-China Economic and Security Review
Commission hearing:*

**China's Propaganda and Influence Operations, its
Intelligence Activities that Target the United States and
its Resulting Impacts on US National Security,
30 April 2009**

Dr. Nicholas J. Cull,
Professor of Public Diplomacy, University of Southern California.

The Frame: Public Diplomacy and Soft Power

The phrase 'Public Diplomacy' means simply the process by which an international actor conducts foreign policy by engaging a foreign public. Though the term in its present use dates only from 1965, the five core elements of Public Diplomacy each have much greater antiquity. The foundational element of Public Diplomacy is Listening: engaging a foreign public by collecting and analyzing its opinions and feeding that into both the formation and explanation of policy. The second is Advocacy: the direct presentation of policy and information. The third is Cultural Diplomacy: the facilitated export of or participation in culture, including sports. The fourth is Exchange Diplomacy, mutual exchange of personnel, especially students, with a foreign partner.

The fifth is International Broadcasting: engaging foreign publics through direct broadcasting of news particularly. While these forms overlap the basic elements of Public Diplomacy cohere around distinct infrastructures, time-frames of operation, sources of credibility and even working practices. The entire structure of Public Diplomacy works with the policies, culture and values of the society conducting it – the factors which Joseph Nye has famously labeled the Soft Power of an actor. These Soft Power factors must also be considered in any assessment of an actor's Public Diplomacy: the best Public Diplomacy structures in the world can not sell a bad policy, but an effective Public Diplomacy structure not only can make good policies known, it can feed international opinion back into the policy process and make good policies even better.¹

The Origins of Contemporary Chinese Public Diplomacy

There are three basic points of origin for contemporary Chinese Public Diplomacy. First, is a traditional Chinese concern with issues of image in all relationships. Second, is the history of external propaganda practiced by the Communist regime. Third, is the recent realization of the central role that Public Diplomacy and communication must take in the new world. This last point is the immediate cause of the policies that writer Joshua Kurlantzick has dubbed China's Charm Offensive.²

Chinese culture places great value on personal image, through the concepts which the west translates as 'face' (*Lian*, a concept of personal honor and moral worth, and *Mianzi*, a concept of social prestige).³ Public Diplomacy reflects an extension of these concerns to the international sphere. Centuries before Joseph Nye, Confucius himself spoke of 'attracting by virtue' (*yide laizhi*) and argued that an image of virtue and morality was the foundation of a stable state.⁴ Successive Chinese governments, as well as Taiwan and Singapore, have deployed foreign policies to the same ends.

The revolutionary government of Mao – tutored in the international propaganda of the Soviet Union – was swift to extend its own use of propaganda abroad. The traditional term for such work is '*dui wai xuan chuan*' or '*wai xuan*' meaning 'external

¹ For further discussion see Nicholas J. Cull, 'Public Diplomacy: Taxonomies and Histories' *ANNALS of the American Academy of Political and Social Science*, Vol. 616, March 2008, (special issue 'Public Diplomacy in a changing world,') pp. 31-54 and Joseph Nye, *Soft Power: The Means to Success in World Politics*, PublicAffairs: New York, 2004.

² Joshua Kurlantzick, *Charm Offensive: How China's Soft Power is Transforming the World*. Yale: New Haven, 2007.

³ For a classic exploration of the concepts see David Yau-Fai Ho, 'On the Concept of Face,' *American Journal of Sociology*, Vol. 81 (4), 1976, pp. 867-84.

⁴ Qing Cao, 'Selling Culture: ancient Chinese conceptions of the other in legends,' in Stephen Chan, Peter Mandaville, and Rolan Bleiker (eds), *The Zen of International Relations: IR theories from East to West*. Palgrave: New York, 2001, pp. 178-202.

propaganda.’⁵ Mao’s ‘*xuan chuan*’ was based on a tightly controlled message. The regime carefully selected those aspects of China that would be seen abroad, and censored much of the rest. Favored journalists were allowed glimpses of the nation, while state journals like *Beijing Review* showcased achievements. Radio Beijing harangued the world about the Chairman’s monopoly on virtue. The regime sought to export its revolution by sponsoring Communist Parties in East Asia and later in Africa and Latin America.⁶

The post-Mao reforms launched in 1978 by Deng Xiao Ping included the opening of China to international exchange and tourism. In 1983 the Ministry of Foreign Affairs opened an Information Department. Then, in 1989 the house of cards that was China’s international reputation came crashing down as the world witnessed images of the repression of the protests in Tiananmen Square. In the aftermath of the crisis Beijing engaged the international public relations firm Hill and Knowlton to begin the process of rebuilding China’s image abroad. The parallel process of consolidation followed included the reconfiguration of domestic and international information work under a single State Council Information Office (SCIO), founded in 1991. Its declared purpose was to ‘promote China as a stable country in the process of reform, a China that takes good care of its population, including minorities, and works hard to reduce poverty.’ It was a foundation for future work.⁷

As the 1990s progressed, Beijing placed renewed emphasis on its international image. SCIO flourished under the dynamic leadership of the former vice mayor of Shanghai, Minister Zhao Qizheng, who led the office from 1998 to 2005.⁸ Wary of the negative spin that the west gave to ‘propaganda,’ his innovations including dropping the term ‘*xuan chuan*’ in favour of the more benign ‘*shuo ming*’ or ‘explaining’.⁹ He had an

⁵ For discussion and survey of contemporary work see Wang Yiwei, ‘Public Diplomacy and the Rise of Chinese Soft Power,’ *ANNALS of the American Academy of Political and Social Science*, Vol. 616, March 2008, (special issue ‘Public Diplomacy in a changing world,’) pp. 257-290.

⁶ For a survey of the evolution of Chinese PD see Hongying Wang, ‘National Image-Building and Chinese foreign policy,’ *China: An International Journal*, vol. 1, no. 1, March 2003, pp. 46-72.

⁷ Ingrid d’Hooghe, ‘Public Diplomacy in the People’s Republic of China,’ in Jan Melissen (ed.) *The New Public Diplomacy: Soft Power in International Relations*, Palgrave, London, 2005, pp. 92, 98-99.

⁸ Erik Eckholm, ‘China admits ecological sins played role in flood disaster,’ *New York Times*, 26 August 1998, p. A1.

⁹ Todd Crowell and David Hsieh, ‘Beijing’s spin doctor,’ *Asia Week*, 22 September 2000. In 2005 an anthology of Zhao Qizheng’s speeches appeared with the title *Xiang Shijie Shuoming Zhongguo* (Explain China to the World). See also ‘Hong Kong daily analyses official’s role in improving China’s public image,’ *BBC Monitoring International Reports*, 7 June 2005.

uncharacteristic charisma and was prepared to take risks including conceding error and sharing the stage with potential critics, as when in 2005 he engaged in a sustained dialogue on religion with the American evangelist Luis Palau.¹⁰ Zhao's determination to present China to the world was supported at the highest level and in February 1999 President Jiang Zemin called for China to 'establish a publicity capacity to exert an influence on world opinion that is as strong as China's international standing.'¹¹ This led directly to a number of parallel policies, coordinated through the dual structure of the Communist Party and SCIO. Zhao was double-hatted as both director of SCIO and of the International Communication Office of the Central Committee of the Communist Party.¹²

In 2005 Zhao Qizheng moved to his present role as dean of the Communication School at Remin University and a member of the National Committee of the Chinese People's Political Consultative Conference (CPPCC), where he is vice chair of its foreign affairs committee. Since his departure, the most prominent figure in Chinese Public Diplomacy has been the director of the Publicity Department of the Central Committee, Lui Yushan. Director of the Publicity Department since 2002 and a member of the Politburo since 2007, Lui is a regular source of edicts on matters of propaganda and international image at home and abroad and has personally taken part in China's charm offensive by conducting international visits such as a trip to Egypt in November 2008.¹³ The present director of SCIO is Wang Cheng, who is integrated into the party system through his dual role as deputy to Lui Yushan in the Party Publicity Department.

During the course of 2007 the Chinese government began to focus explicitly on Soft Power as a dimension of foreign policy. In February 2007 Soft Power was the subject of the annual conferences of both the National People's Congress (China's parliament) and the Chinese People's Political Consultative Conference. Participants acknowledged the scale of the challenge that lay ahead.¹⁴ The year culminated in October with a formal call by President Hu Jintao at the 17th National Congress of the Communist Party to enhance the 'Soft Power' of Chinese culture through methods including management of the internet and investment in cultural institutions at home. 'The great rejuvenation of the Chinese nation' he argued 'will definitely be accomplished by the thriving of Chinese culture.'¹⁵ The theme has been widely underlined. Typical

¹⁰ Luis Palau and Zhao Qizheng, *A Friendly Dialogue Between an Atheist and a Christian*, Zondervan: Grand Rapids, Michigan, 2008.

¹¹ 'President calls for further propaganda work to enhance China's image abroad,' *Xinhua*, 28 February 1999 as cited in Kurlantzick, *Charm Offensive*, p. 39.

¹² The structure may be readily constructed from biographical entries on the Chinavita website.

¹³ For a brief vita see http://www.chinavita.org/biography/Liu_Yunshan%7C32

¹⁴ Li Baojie, Cheng Yifeng and Wang Mian, 'Soft Power a new focus at China's Two Sessions,' *Xinhua*, 14 March 2007.

¹⁵ 'Hu Jintao stressed enhancing Soft Power of Chinese culture,' *Xinhua*, 15 October 2007,

explications include an un-attributed article on the *Xinhua* site of 28 December 2007 with the title 'Raise National Culture's Soft Strength.' The piece echoed Hu Jintao with a call for 'raising our cultural propaganda abilities and continuously expanding China's cultural influence,' continuing:

The influence of a country's culture depends on whether it possesses unique charm but also depends on whether it possesses advanced propaganda methods and strong propaganda capabilities. Especially in today's informatized society every country that has advanced propaganda methods and strong propaganda capabilities can widely spread its cultural ideals and value concepts, and it can grasp the speaking power to influence the world and popular feeling. Cultural propaganda capabilities have already become a decisive factor for a national culture's soft strength.¹⁶

The Message

The central message of Chinese Public Diplomacy is that China is back as a world power after a two hundred year hiatus; that Chinese culture is admirable and that China's intentions are benign. This last is variously expressed as a 'peaceful rise'¹⁷ and, from 2007, an intent to 'build a harmonious world.'¹⁸ The message comes directly from Premiere Hu Jintao and flows outwards from the party ideological apparatus.

The Audience

The audience for China's Public Diplomacy is two fold. The primary audience is global and seems to include both masses and elites. School children are increasingly targeted. While all nations are approached, the campaign plainly has special resonance with the Chinese Diaspora. This said, Chinese Public Diplomacy is also conducted with a domestic audience in mind. The Chinese government wishes above all to give the Chinese people the gift of the admiration of the world, to buttress their own legitimacy and counter any doubt that the CCP might not be the best stewards of China's destiny. Such sentiments may readily be detected in set-piece speeches by Lui Yushan, with their emphasis on western admiration for Chinese achievement in both its economic success and management of adversity.¹⁹

¹⁶ 'Raise National Culture's Soft Strength,' *Xinhua*, 28 December 2007 as translated by *BBC Monitoring Asia Pacific* as 'China urges 'cultural soft strength' ethnic unity in light of party congress, 6 January 2008, p. 1.

¹⁷ Joshua Cooper Ramo, *Brand China*, Foreign Policy Center, London 2007 p. 8-9, online at <http://fpc.org.uk/fsblob/827.pdf> see also Zheng Bijian, *Peaceful Rise: Speeches of Zheng Bijian, 1997-2005*, Brookings Institution Press, Washington DC, 2005.

¹⁸ Li Baojie, Cheng Yifeng and Wang Mian, 'Soft Power a new focus at China's Two Sessions.' *Xinhua*, 14 March 2007.

¹⁹ For a sample text see Liu Yunshan, 'Lessons, thoughts...' a speech of 31 July 2008,

The Mechanisms of Public Diplomacy

i. Listening.

China is certainly listening to the world. We know from official statements that China is tracking both the course of anti-Chinese sentiment around the world, and international opinion about China. Negative opinion was a major driver of the rebuilding of Chinese Public Diplomacy. Positive foreign statements about China are fed back to the Chinese people as evidence that foreigners admire the accomplishments of 'Socialism with Chinese Characteristics' and accept China as a world power of the first rank.

China uses opinion polls to track its relationships. Recent innovations include a poll from 2005 jointly designed and administered with Japanese counterparts to survey the state of mutual opinion.²⁰ Other examples of Chinese listening include the flurry of activity in 2007 to ensure that celebrations of the Year of the Pig did not offend Islamic nations. More significantly, in the spring of 2007 international anger over China's support for the regime in Khartoum in the face of the Darfur genocide brought a reversal of Chinese foreign policy in East Africa.²¹

The chief mechanism for listening is the growing network of embassies and consulates across the world. China is investing heavily in developing regional expertise within its diplomatic corps, sending thousands of its best students overseas to study their target state and society first hand.²² Unlike the western penchant for the generalist, the Chinese Foreign Service encourages officers to work entire careers in their specialist geographical area. The rising generation of diplomats will be well placed to learn from their experience and to inject local knowledge into the making of Chinese foreign policy for years to come.

ii. Advocacy.

China's international advocacy includes both the traditional CCP techniques of leader speeches and articles in the state Xinhua news agency and increasingly western-style press conferences. Zhao Qizeng's institutional reforms included an upgrading of China's ability to address the foreign media. The wake-up call seems to have been the SARS outbreak of 2002. As Anne-Marie Brady has noted, in the wake of the clumsy SARS cover-up China began studying spin as practiced in the west, taking the Blair

published on the *Qiushi* website in October and translated by *BBC Monitoring Asia-Pacific*, 23 October 2008 as 'Chinese propaganda chief views problems, achievements in 2008.'

²⁰ 'Chinese, Japanese NGOs release poll on bilateral relations,' *Xinhua*, 24 August 2005.

²¹ 'Shaming China on Darfur,' *Boston Globe*, 31 May 2007.

²² Kurlantzick, *Charm Offensive*, p. 65-66.

government in Britain as one model of how to do it.²³ Moves towards openness and interactivity were part of this process and hence, in December 2004, Zhao astonished a gathering of journalists at Beijing's Kunlun hotel by presenting them with the names and phone numbers of the seventy-five spokespersons of every ministry and commission under the State Council. This, he promised, would be an annual event.²⁴ Other advocacy initiatives included the launch of an overseas edition of the *People's Daily* and a number of English language websites.²⁵ The domestic and international handling of the news of the Sichuan earthquake in the spring of 2008 revealed much greater skill.²⁶

iii. Cultural Diplomacy.

Beginning with the tenure of Zhao Qizheng at SCIO, China has devoted increasing energy to the field of cultural diplomacy. The CCP leadership seems particularly concerned to see that Chinese culture receives the admiration that it deserves around the world. Both the Beijing Olympics of 2008 and forthcoming Shanghai Expo reflect this. Other initiatives include major exhibitions such as the visit of the Terracotta Army to London, 'China Weeks,' and tours for artists.

The central project of Chinese cultural diplomacy is the rapidly growing network of Confucius Institutes around the world. Their title reassuringly emphasizes the glories of the classical Chinese past rather than the vibrant present (or controversial Communist history) but the Institutes activities typically emphasize opportunities to get to know contemporary China rather than its historical abstract. These institutes are (officially) enterprises shared between the Chinese government's language teaching agency, known as *Hanban*, and local institutional hosts (usually universities). The hosts receive a start-up subsidy from Hanban and provide a home to language teachers supplied by that agency. In 2006 the government set a goal of establishing more than one hundred institutes within five years. This target has already been realized and the number seems likely to break 200 by the end of 2010.²⁷

²³ Brady as quoted in Tania Branigan, 'China looks to Labour to learn secrets of spin,' *The Guardian* (London), 21 March 2009, p. 23.

²⁴ 'China makes public names of government spokespersons for the first time,' *Xinhua*, 28 December 2004, also 'Hong Kong daily analyses official's role in improving China's public image,' *BBC Monitoring International Reports*, 7 June 2005.

²⁵ 'English web platform opens,' *China Daily*, 17 September 2004 on the English site at <http://english.sohu.com> – a state-private partnership of the *China Daily* and the private search engine company Sohu.com.

²⁶ For Liu Yunshan and coverage of the media response to the earthquake see 'Senior leader hails media worker covering quake,' *Xinhua*, 17 May 2008.

²⁷ 'Confucius Institute: promoting language, culture and friendliness,' *Xinhua*, 2 October 2006. In some poorer countries Chinese aid ensures that it is cheaper to be educated at a Chinese-funded school than within the national system. Kurlantzick, *Charm Offensive*, pp. 67-69.

iv. Exchange Diplomacy.

Some nations – Japan most prominently – couch their Public Diplomacy in terms of exchange, seeking to build reciprocity into as many activities as possible. China is not limited by such a priority. China certainly participates in mutual educational exchanges, though one might suspect that the mutuality is seen as a price of access to foreign institutions and audiences. Recent years have seen a flurry of new bilateral agreements with partners around the world from Austria to Zimbabwe. Institutions which manage people-to-people exchanges, such as the Chinese People's Association for Friendship with Foreign Countries, have flourished. China also expanded its recruitment of international students, bringing twenty percent more with every passing year. The Ministry of Education expected rolls to top 120,000 by 2008.²⁸

Exchanges have been used to promote international study of the Chinese language, lately targeting younger groups of students, providing a stream of foreign language teachers for overseas service and wooing foreign school principals through trips to China, as priorities shift from the university to secondary and even primary school sector. In June 2007 the Office of the Chinese Language Council declared that 30 million people around the world were now learning Chinese and predicted that this figure would hit 100 million by 2010.²⁹ In February 2007 the Premiere of the State Council, Wen Jiabao paid tribute to the value of exchanges in presenting China's best face to the world, noting that they have: 'fostered an image of China as a country that is committed to reform and opening-up, a country of unity and dynamism, a country that upholds equality and values friendship, and a country that is sincere and responsible.'³⁰

One example of exchange is the agreement between China and Russia to designate 2009 Russian year in China and 2010 China year in Russia, with corresponding language teaching initiatives. The occasion for the celebration is the sixtieth anniversary of the Soviet recognition of and friendship treaty with the People's Republic.³¹

v. International Broadcasting.

²⁸ 'Number of foreign students in China rises 20 percent annually,' *Xinhua*, 19 January 2006 as cited in Kurlantzick, *Charm Offensive*, p. 118.

²⁹ 'Overseas craze for Chinese spreads from universities to schools,' *Xinhua*, 26 June 2007 see also 'Foreign headmasters follow Chinese language teaching trail,' *Xinhua*, 20 June 2007 and '110 British headmasters visit China for language teaching co-op.' *Xinhua*, 27 May 2007.

³⁰ Wen Jiabao, 'Our Historical Tasks at the Primary Stage of Socialism and Several Issues Concerning China's Foreign Policy.' *People's Daily*, 27 February 2007 (translation *Xinhua*, 5 March 2007).

³¹ For coverage see <http://www.cctv.com/english/20090321/101135.shtml>

China has a long history of international broadcasting through Radio Beijing. Its lead agency in the 21st century is Chinese Central Television, whose channel 9 – launched in September 2000 – broadcasts in English and is intended for foreign audiences.³² The channel is carried internationally on a variety of platforms: Rupert Murdoch's Sky satellite to the UK and Fox services in the USA, and Vanuatu in the mid-Pacific.³³ China has paid particular attention to distribution, seeking out contracts for local rebroadcast of their media feeds. CCTV 9 has displaced CNN as the prime foreign feed in several African markets, including Kenya, and Radio Beijing is rapidly accumulating local affiliates to rebroadcast Radio Beijing on the FM wave band as Africa moves finally away from shortwave.³⁴

CCTV has diversified into other languages. 2004 saw the launch of CCTV E&F, a bilingual French/Spanish feed which split into single language services in Spanish (CCTV E) and French (CCTV F) in 2007. CCTV is presently hiring staff to launch both Arabic and Russian language channels towards the end of 2009.³⁵ While these channels are fairly easy to view – CCTV 9 and CCTV E are both on the Dish satellite within the United States – audiences are reportedly small. CCTV 9 has 90% of its viewers in China, of which 80% are Chinese wishing to improve their English. The channels, however, operate as badges of prestige as much as an actual ideological delivery apparatus, and are not subject to the same market pressures as commercial channels.³⁶

The content of CCTV 9 has reflected a need to present something close to real journalism rather than just the litany of achievements and cultural events that once typified broadcasts. Since 2003 a new openness has been detectable, with CCTV 9 presenting stories about China's pollution problems and its energy crisis which would have previously been swept under the carpet. In the spring of 2004 CCTV 9 announced a major re-launch to include the employment of foreign anchors and a consultant from the Murdoch stable, John Terenzio. With disarming honesty the station's controller Jiang

³² 'China to launch all-English channel tomorrow,' *Xinhua*, 24 September 2000.

³³ On the Murdoch deals see 'Danny Gittings and Julian Borger, 'Homer and Bart realize Murdoch's dream of China coup,' *The Guardian*, 6 September 2001, p. 3 and 'Murdoch gets approval for Chinese TV service,' *The Australian Financial Review*, 7 March 2003, p. 63; 'China's English international channel to air in Vanuatu,' *Xinhua*, 10 August 2005.

³⁴ On China in Africa see Adam Clayton Powell III, 'Chinese TV extends its reach into Africa,' 19 December 2005, USC Center on Public Diplomacy web site at http://uscpublicdiplomacy.com/index.php/newsroom/journal_detail/051219_chinese_tv_extends_its_reach_into_africa/

³⁵ For the recruitment process see <http://www.cctv.com/english/20090119/105739.shtml>

³⁶ For discussion of audience see Gary D. Rawnsley, 'China talks back: Public Diplomacy and Soft Power for the Chinese Century,' in Nancy Snow and Philip M. Taylor (ed's), *Routledge Handbook of Public Diplomacy*, Routledge: London, 2008, p. 286.

Heping told the *South China Morning Post* that: 'We are taking great efforts to minimize the tone of propaganda, to balance our reports and to be objective. But we definitely won't be reporting as much negative domestic news as the Western media.'³⁷

Chinese Public Diplomacy hence seems poised to face the same issues of the boundary between news and advocacy that have loomed so large in the history of western international broadcasting, similarly, it now must consider how domestic negatives should be treated in Public Diplomacy. In February 2007 an article in *The People's Daily* under the byline of Wen Jiabao, declared: 'We should conduct Public Diplomacy in a more effective way. We should inform the outside world of the achievements we have made in reform, opening-up and modernization in a comprehensive, accurate and timely manner. At the same time, we should be frank about the problems we have.'³⁸

vi. Diplomacy of Deeds

In parallel with the informational engagement with international audiences, China pays close attention to the diplomacy of deeds, seeking to win friends around the world by programs of aid and 'good works': these activities range from aid and development work to targeted investment. China makes a particular point of not requiring any political concessions of the sort expected by western donor nations, famously going so far as to court pariahs like the regime in Sudan or Zimbabwe.³⁹ Chinese aid sometimes includes assistance with media development. In Venezuela China has assisted the development of Hugo Chavez's satellite TV channel Telesur. In Zimbabwe China provided the equipment to enable radio jamming by the Mugabe regime.⁴⁰

A sub-field of China's diplomacy of the deed is the entry of Chinese public figures into the realm of Celebrity diplomacy. Venturing where westerners including Princess Diana and Angelina Jolie have gone before, Chinese celebrities are now identifying themselves and China with international aid work around the world. The pianist Lang Lang is now a UNICEF goodwill ambassador and basketball-player Yao Ming and actress Zhang Ziyi are both goodwill ambassadors for the Special Olympics.⁴¹

³⁷ 'CCTV international to re-launch, add new languages,' *BBC Monitoring International Reports*, 6 April 2005, and author's own viewing.

³⁸ Wen Jiabao, 'Our Historical Tasks at the Primary Stage of Socialism and Several Issues Concerning China's Foreign Policy,' *People's Daily*, 27 February 2007 (translation *Xinhua*, 5 March 2007).

³⁹ Kurlantzick, *Charm Offensive*, p. 44.

⁴⁰ 'Zimbabwe uses "Chinese Technology" to disrupt VOA radio signal,' *BBC Monitoring*, 5 July 2006.

⁴¹ David Patrick Stearns, 'Chinese pianist Lang Lang strikes the right keys,' *Philadelphia Enquirer*, 18 April 2006; 'Chinese Sensation Ziyi Zhang Joins Special Olympics as Newest Global Ambassador,' *PR Newswire*, 16 November 2006; 'Yao Ming appears as Ambassador to the Special Olympics,' *Xinhua*, 22 July 2006.

The Professionals.

The history of Public Diplomacy bureaucracies around the world is typically the history of turf wars and clashing approaches to the business of communication. This was the case in the old Soviet Union and it has been true in the United States also. While there are differences in approach between the various elements of Chinese Public Diplomacy – the most obvious being the element of self criticism allowed on occasion at CCTV 9 – no turf war has yet broken into the open, instead, China's Public Diplomacy displays remarkable cohesiveness. One of the more interesting features of Chinese Public Diplomacy is its ability to rally support among the ordinary citizens and the international Diaspora, as seen during set-piece confrontations like international criticism attending the route of the Olympic torch in the spring of 2009. While a certain uniformity of placards and pro-China rallies suggested official coordination, the scale of participation among overseas Chinese revealed a popular embracing of the cause. China's presence on the World Wide Web seems to be based on enthusiastic individuals rather than a state cyber-corps, though the effect is the same.

The Domestic Audience

The indirect domestic audience remains a prime driver of Chinese Public Diplomacy. This is not surprising. Winning opinion in Kansas will help the Chinese economy in a round about way, no doubt, but it is the fear of losing opinion at home that keeps members of the Politburo awake at night. China is not unique in this. The Soviet Union ran much of its foreign propaganda to convince the home audience that their nation was the envy of the world, and U.S. Public Diplomacy also often has its eye on the domestic market and four year electoral cycle.

The Next Phase

China's declared objective is to further expand its cultural and media presence overseas. Speeches by leaders reveal a belief both that an international media is a badge of prestige and that further influence flows from the possession of such organs. As propaganda minister Liu Yushan put it in an essay published in January 2009:

It has become an urgent strategic task for us to make our communication capability match our international status. In this modern era, who gains the advanced communication skills, the powerful communication capability and whose culture and value is more widely spread is able to more effectively influence the world.⁴²

⁴² Quoted in David Barboza, 'China aims to create a global news empire,' *International Herald Tribune*, 15 January 2009, p. 1.

China's expansion of the Xinhua agency – adding bureaus – and its plans for a 24 hour news channel and the projected launch of a global English language newspaper are significant.⁴³ It is unlikely that the paper will win a wide print readership in the USA, but an increased flow of Xinhua stories circulating on the world wide web is inevitable and, with the crisis in western international newsgathering, stories from a Chinese perspective could easily move to plug gaps, especially in spaces like Latin America and Africa where not being made in the USA is a palpable asset.

Conclusion:

China is doing nothing wrong in its Public Diplomacy drive. It is wise policy from China's point of view. What would be wrong would be for the west to ignore it. The appropriate response of the west should be to meet the overtures for exchange in the spirit in which they are intended and to accept opportunities to know China better and facilitate China's knowing more of the west. Equally, where China is challenging the western presence, and displacing western voices, as in its drive to accumulate FM radio affiliates in Africa, the west, and the United States specifically, needs to raise its game. I will not argue that the United States needs to expand its Public Diplomacy solely to keep pace with China, any more than it should do so solely to prevail over radical Islam. I believe that the United States needs to expand its Public Diplomacy because it has become an essential element of foreign policy in the twenty first century. In an age when power increasingly rests on public opinion, success requires effectively engaging with the people. Anything that this committee can do to encourage the rebuilding of American Public Diplomacy would be a wise investment in the future of this country and the ideals on which it is built .

HEARING COCHAIR REINSCH: Thank you.
Dr. Polumbaum.

STATEMENT OF DR. JUDY POLUMBAUM, PROFESSOR OF JOURNALISM AND MASS COMMUNICATIONS, UNIVERSITY OF IOWA, IOWA CITY, IOWA

⁴³ For coverage of these plans see Vivian Wu and Adam Chen, 'Beijing in 45 b Yuan global media drive,' *South China Morning Post*, 13 January 2009, web edition; Peter Ford, 'Beijing launching a Chinese CNN to burnish image abroad,' *Christian Science Monitor*, 5 February 2009, p. 1.

DR. POLUMBAUM: I also would like to thank the Commission and the Commission staff for inviting us and organizing this very important program.

My interest is in journalism and the practice of news gathering, selection, presentation. I'm particularly interested in the role that individual actors, journalists themselves, have within a structure that certainly from the outside looks extremely authoritarian.

One of your questions for this panel is whether different institutional actors involved in external propaganda in China have different outlooks and interests. And the answer is decidedly yes. And I think this is a key, a key understanding.

One important manifestation of these differences is divergence between central and local interests. China is a country that traditionally has centrifugal tendencies, and this means, for example, that local authorities may override central policies or preferences when it comes to handling news media in different locales.

I think this partly, although not entirely, explains the contrast in access granted to both domestic journalists and international correspondents. Last year, after the riots in Tibet and after the earthquake in Sichuan, Tibetan authorities, who of course include ethnic Tibetan officials appointed by, and thus benefiting from their association with, the central government were adamantly opposed to journalistic access despite some views to the contrary in Beijing, while Sichuan provincial authorities allowed broad access, which, of course, proved beneficial for eliciting worldwide sympathy and relief.

One also finds differences across agencies. At any given level and within institutions, individual actors, some of whom regularly or occasionally may be in pivotal positions, also possess different outlooks and interests.

Thirty years of studying the media in China has impressed upon me that individual agency is of no small importance in China. This includes individual efforts to circumvent rules and, in fact, contrary to what one might expect in a nation so authoritarian in structure, the country is full of scofflaws, and there are good reasons that the irrepressibly mischievous character of the "Monkey King" is such a beloved folk icon in China.

Media industries and organizations, of course, constitute a very important set of institutional actors that may differ with propaganda dictates coming from Party and government authorities.

China's media outlets are often described as state-controlled or official, but even the most obvious standard bearers for the Party and government are also self-interested entities in their own right. So, for instance, claims or appearances that Chinese media are necessarily

maidservants of a coherent national strategy can be misleading. They may be, first and foremost, working in their own organizational interests.

And when the South China Morning Post recently reported on this tremendous investment in Chinese external propaganda efforts that included a big chunk of investment for expansion of Xinhua News Agency both in terms of expansion of foreign bureaus and development of a rather amorphously described television network, perhaps based in Asia, that could be likened to China's CNN or China's Al-Jazeera, whereas, some observers looked at this as a coherent plan of the central government and the Communist Party, I immediately thought this is Xinhua's empire building.

Xinhua as an organization has been empire building since the beginning of reforms, and so there are many confluences and cross-currents of interest I believe going on in these new plans.

Another new development that's gotten a great deal of attention is the launching of a new English-language edition of Global Times, which is an offshoot of the People's Daily, the flagship newspaper of the Central Committee, and I think that also is a little bit of empire building on the part of People's Daily.

In sum, my view is that the most important ramifications of expanded external communication efforts by China may not be intentional objectives at all, whether they be malevolent or benign, although personally I tend to favor benign interpretations.

Rather in my view, the more individuals, organizations and institutions in China are brought into the mere effort of trying to do better at communicating, which includes centrally the enhancement of abilities to deal directly in foreign languages with foreign peoples and cultures, the more potential there is for enhanced knowledge, sophistication and understanding of the rest of the world among Chinese involved in this project.

In other ways, the endeavor to develop media that in both format and content are not merely palatable but compelling to foreign audiences can have positive results for China internally.

In reference to journalism specifically, I would argue that external propaganda efforts in exposing Chinese media workers to international knowledge, ideas and examples create dynamics that further encourage professional trends in China's journalism core.

[The statement follows:]

**Prepared Statement of Dr. Judy Polumbaum, Professor of
Journalism and Mass Communications, University of Iowa, Iowa
City, Iowa**

April 30, 2009

Judy Polumbaum, The University of Iowa

Testimony before the U.S.-China Economic & Security Review Commission, hearing on
“China’s Propaganda and Influence Operations”

First, let me thank the Commissioners for inviting me here today, and the Commission staff for putting together this illuminating program. All of you already are experts on China, but I hope I can contribute a useful perspective for understanding the production, content and plans for what China calls “external propaganda.”

The word propaganda, of course, is anathema to us in the land of the First Amendment—even if all governments, not to mention businesses, religious and educational institutions, yea, everything from the Pentagon to the American Heart Association, practice it. For good reason, the Chinese are beginning to translate the term as “publicity” or “information.” But even in Chinese, the term is falling out of favor. The most intrepid investigative reporters in China see propaganda authorities as adversaries, and try to outrun them!

Political scientist Harold D. Lasswell, a propaganda expert who some consider a “founding father” of U.S. communication research, famously summed up the communication process as “Who says what to whom in what channel with what effect” (“The structure and function of communication in society,” in *The Communication of Ideas*, ed. by L. Bryson; Harper, 1948). This formula, and the behavioral science orientation from which it arose, presumed a stimulus-response model that emphasized the power of media institutions to reinforce or change social behavior through messages directed at a mass of isolated, anonymous recipients. This approach obviously is outdated in today’s world of media convergence, Twittering, citizen journalists and the active audience. Lasswell indeed was a prolific scholar who made important and wide-ranging contributions to the study of politics, personality and culture, but his “Who says what to whom in what channel with what effect” formulation is now more of a historical footnote than the mantra for research it once represented.

Nevertheless, in searching for a convenient way to present my thoughts on China’s external propaganda efforts, Lasswell’s string of communication components came to mind as a useful outline—supplemented by Daniel Lerner’s addition (“Communication and the Nation State,” *Public Opinion Quarterly*, v. 37 n. 4, Winter 1973-74) of “why (referring to policy) ... how (technique)... and who talks back (feedback)” to the list. Just bear in mind that I’m using an artificial and admittedly simplistic device to parcel out information and ideas that are interrelated with each other and embedded in the much larger matrices of both Chinese and global society.

Thus, question one: WHO are the planners and purveyors—the masterminds, if you will, as well as the implementers—of China’s external propaganda?

For starters, the Chinese Communist Party and government apparatus. Main guidelines for media and propaganda ostensibly emanate from the heart of the Party, the Central Propaganda Department—with policies managed and administered through an array of other agencies, including the State Press and Publication Administration and the State

Administration of Radio, TV and Film, as well as units and functionaries assigned to propaganda and managerial tasks at provincial, municipal, local and workplace levels.

However, much as “China” is not a monolith, neither are the Party or government or its agencies seamless unitary entities. Rather, both Party and government feature competing agencies and interests at national, regional and local levels, and within agencies and units are varied, and sometimes vying views.

Atlantic correspondent James Fallows has observed from Beijing: “Most Americans think this is an all-powerful central government; most of the time, it looks like a relatively weak, remote titular leadership trying to tell the equivalent of warlords (provincial governors) what they should do.” I would extend this analogy down through the hierarchy.

China’s centrifugal tendencies mean, for example, that local authorities may override central policies or preferences when it comes to handling news media in different locales. In part (although not entirely), this is behind the striking contrast in the stifling versus enabling of media coverage—both domestic and foreign—during two major events occurring in succession last year: the riots in Tibet in March 2008, and the Sichuan earthquake in June. Tibetan authorities—who include of course ethnic Tibetan officials appointed by (and thus benefiting from their association with) the central government, were adamantly opposed to journalistic access, despite some views to the contrary in Beijing; while Sichuan provincial authorities allowed broad access, which of course proved beneficial for eliciting worldwide sympathy and relief.

One of your questions for this panel is whether different institutional actors involved in external propaganda have different outlooks and interests—and the answer is decidedly yes. Central-local divergence is just one manifestation. One also finds differences across agencies on any given level; for instance, the State Council and Foreign Ministry often harbor what we might consider more enlightened opinions about license for expression and even dissidence when compared to, say, Public Security and the military. (Sound familiar when it comes to the U.S. State Department and the Department of Defense? Or the local city council and police department!)

I would add that within institutions, individual actors, some of whom regularly or occasionally may be in pivotal positions, also possess different outlooks and interests. And while structural and organizational forces often exert prevailing influence, individual agency is of no small importance in China. This includes individual efforts to circumvent rules—and in fact, contrary to what might expect in a nation so authoritarian in structure, the country is full of scofflaws. There are good reasons the irrepressibly mischievous character of the Monkey King is such a beloved folk icon in China.

Another relevant point is that, while China’s Communist Party and government do have widespread and pervasive monitoring capacities to conduct surveillance on all manner of media, the country does not have a systematic pre-publication censorship apparatus (as did the Soviet Union and most Eastern European countries). This is partly from tradition, and

partly because such a system would be simply impossible to implement in such a vast and variegated country. Conformity to policy largely hinges on anticipation of consequences.

Media industries and organizations constitute another set of institutional actors that may differ with propaganda dictates as well as housing differences within. China's media outlets are often described as "state-controlled" or "official," but even the most obvious standard-bearers for Party and government are also self-interested entities in their own right. So, for instance, claims or even appearances that Chinese media are maidservants of coherent national strategy can be misleading—they may be first and foremost working in their own organizational interests.

As with individuals in bureaucratic agencies, individual mass communicators also have varied ideas and approaches to their work that may put them at odds, directly or indirectly, with official dictates. In the foreword to my recent book *China Ink*, Aryeh Neier, president of the Open Society Institute, identifies "professionalism" as the most important trend today in Chinese journalism (and numerous other fields such as medicine and law). He writes that, "the professionalism of Chinese journalists is gradually expanding the space in which they are able to operate... [and] expanding freedom in China."

The sort of journalists we would consider most professional are those who resist orthodoxy in savvy ways, using unassailable tools of assiduous fact-finding, solid verification and moderation in language. Such journalists, furthermore, cultivate networks of protection that buffer consequences of transgression (editors protect reporters in their purview, reporters look for editors who will go to bat for them, reporters who "make mistakes" get shifted to the library, not to a labor camp).

WHAT messages do these actors hope to, and what do they actually, convey?

The content of Chinese media aimed at foreigners long suffered from direct translation of domestic propaganda—so it not only was often replete with misrepresentations, exaggerations, jargon-laden screeds, and all the other ills of domestic media, but it took no account of what foreign audiences might find relevant, interesting or even coherent. The first challenges for external propagandists once China began its reforms and opening up were to redress these obvious problems—with new training, education and recruitment of journalists who could write directly in foreign languages. Xinhua's *duiwaibu*, external news department, shifted from translation to greater volumes of original reporting and writing in other languages; and the *China Daily* was founded with this mode in mind.

When it comes to sensitive issues—Tibet, Taiwan, foreign policy, dissidence or human rights violations—I don't have to tell you that simplistic bombast with intransigent positions still dominates content, in both domestically and foreign-directed media. My Chinese colleagues and friends (a goodly number formed over the past 30 years)—mostly intellectuals, including many journalists—are mortified by this practice. Not only for pragmatic reasons (it's stupid and ineffective) but because they, too, long for intelligent coverage and discussion of these issues.

The Chinese government is often seen as being complicit in nationalistically-tinged reporting, rants aimed at the West, protests about Western media and financial conspiracies and so forth—and clearly there is a vocal constituency for these ideas in China. Again, though, my colleagues and friends think this stream of communication, which gets lots of attention both in China and abroad, is childish and counterproductive—and while loud, not broadly representative of either Chinese elite or mass thinking.

Popular themes, again for domestically as well as international consumption, include appreciation of China's ancient culture along with modernization and dynamism, global engagement and international citizenship. The 2008 Beijing Olympics, of course, provided a good vehicle for messages of glorious tradition and vigorous modernization. And just serendipitously, the fact that the international media recently had given a great deal of attention to “bad news” stories of Tibet and Sichuan probably cleared the air for more positive coverage during the Games (in fact, I heard one U.S. China correspondent say as much).

A good deal of what goes out to the world pertains to topics, events, issues and also controversies and problems that journalists want to cover: Real life at the grass roots, human interest stories, enterprise and investigation. The nature and scope of such stories hinge largely on content in the domestic media, whose range and diversity undeniably have grown greatly over the past three decades. Nowadays China's domestic media provide the main leads for most of the important stories that foreign correspondents then pursue. The days when China-watchers sat in Hong Kong and read tea leaves are long over. The days when foreign correspondents get scoops have not arrived, however; they are more likely to build on scoops of domestic reporters.

To WHOM is the communication directed, i.e., who are the purported and actual audiences?

Intended audiences include, most directly, foreigners in China—tourists, teachers, students, diplomats, business people; and, interestingly, foreign-language learners (mainly English) in China. This domestic constituency actually constitutes the largest proportion of *China Daily's* circulation, although actual numbers are closely held; and is the main target of a lucrative stable of English-language weeklies put out by that paper, *21st Century*, in editions for elementary, middle school, high school and college students as well as a teachers edition.

Less directly, intended audiences include international correspondents, who pick up leads and stories from foreign-language as well as Chinese-language media; and ultimately citizens abroad, including international elites and policymakers. Although Xinhua News Agency fancies itself an equivalent of Associated Press, Reuters or AFP, U.S. news organizations certainly do not use its dispatches verbatim, but many news outlets elsewhere around the world certainly do, and overseas Chinese media make ample use of the China News Service. The implications of this will depend on your thoughts about audience credulity, and different people will judge content and sources in different ways; but we have no reason to believe foreign audiences have any particular susceptibility to Chinese content going directly into overseas use as opposed to content from any other sources.

Some Chinese propaganda functionaries and media managers do seem to have an illusion, however, that people abroad have an unmet appetite for media content directly from Chinese sources. This ostensibly is the rationale for the start a couple of months ago of a “North American edition” of *China Daily*—which strictly speaking is a weekly Monday supplement folded into papers printed in New York and San Francisco. Frankly, I am baffled at this development and don’t see a market—those who wish already can read *China Daily* on the web, and are not about to use even a daily edition as a substitute for *The New York Times* or whatever their regular daily news fare might be. So the best explanation I’ve heard is the current editor wants this—and I suspect it’s a way of fostering confidence and even garnering prestige, in response to beliefs (or more properly, delusions) at higher levels that there actually is a demand for *China Daily* on Main Street America.

WHY is the communication generated? What policy objectives and other intentions propel external propaganda efforts?

In terms of broad objectives, some agencies and actors producing media content aimed at foreigners genuinely hope to explain China’s policies and programs to “outsiders” and engage in conversation with them. I would say this is the primary motivation of middle-aged and veteran reporters, writers and editors at *China Daily*.

Regarding the new investments and ambitions for China’s external propaganda, the desire to interject China’s “voice” and perspectives into the international arena seems to be a genuine motivation. Perhaps some think expanding external propaganda truly can influence or even manipulate international opinion—and perhaps propaganda authorities have such hopes, but I don’t think most serious journalists actually involved in the external communication sector believe this.

I have no doubt that propaganda authorities are trying to develop more sophisticated approaches to international image building, including through external propaganda; but I think this motivation is less prevalent among the journalists actually generating the news for foreign audiences. Rather, they are more likely to have an occupational perspective, wishing to pursue careers that provide them with both intrinsic and extrinsic rewards—ideally, both.

I am not of the school that contends that externally directed media, and those working in this sector, are primarily driven by ulterior motives, e.g., that such media are major conduits for disinformation, distraction, smokescreens. More realistically, I think, this sector is likely to be valued for its capacity to generate both tangible and intangible goods for those involved in it—such as reputation, influential connections and commercial rewards.

Those actually producing content for foreign audiences, e.g., working as editors, producers, writers, reporters and even in technical roles, are best positioned to recognize perhaps unplanned or unintended byproducts of the sector—such as its contributions to increasing professionalism among media workers, and its role in fostering foreign (English) language learning and, more generally, cosmopolitanism, within China.

WHAT CHANNELS carry the communication? More broadly, HOW is the communication created and disseminated?

The behemoth is Xinhua News Agency's *duiwaibu*. Xinhua is hoping to both expand its international correspondent network and build broadcasting capabilities—it already is providing video footage for TV. The agency is now looking for native speakers of other languages to both work in Beijing and serve as correspondents abroad, and the latter is new.

When the *South China Morning Post*, citing anonymous high-level sources, reported China's plans to invest some \$10 billion in expanding external propaganda efforts, including a major initiative by Xinhua News Agency, I immediately thought: Xinhua empire-building! Xinhua patently has been building up its empire, in its own interests as much as if not more than in the national interest, since the reform period began in the late 1970s. Reports say Xinhua hopes to start its own Asia-based channel, presumably Chinese-language, that some dub the Chinese Al-Jazeera. The State Administration of Radio, TV and Film reportedly is not pleased at Xinhua's TV plans.

Broadcasting includes China Radio International (the former Radio Beijing), the international central television channel CCTV 9, and lots of intermittent attempts, not systematically tracked, at English-language regional/local programming for both radio and TV—often enlisting “polishing” or editing help from foreigners who happen to be teaching English in the vicinity. China Central TV also set up French and Spanish-language channels before the Olympics last year, and is said to be planning Russian and Arabic services.

China Daily marked its 25th year of publication in 2006. Its experience makes it the lead candidate for high-profile projects, frustrating the ambitions of the *Beijing Youth News*, which had been publishing an English weekly, in a contest for the contract to publish an English-language daily for the Beijing Olympics. *China Daily* similarly put out a daily special when the Asian Games were held in Beijing. Along with the 21st Century group, *China Daily* also publishes the weekly *Shanghai Star*; as overt competition to the latter, a former *China Daily* journalist started the *Shanghai Daily*, under the municipal government; the *Shenzhen Daily*, started in 1997, is aimed at readers among the concentration of foreign residents in southern China.

The new English edition of *Global Times*, which began publishing weekdays on Monday, April 20, is an offshoot of the Chinese *Global Times*, or *Huanqiu Shibao*, a successful (i.e., popular and money-making) subsidiary of *People's Daily*, or *Renmin Ribao*, flagship paper of the Central Committee. Editors of the English *Global Times*, acknowledge they are going after the same audiences as *China Daily*. They also purport, however, to be different from *China Daily* in offering a more “independent” stance. The Chinese *Huanqiu Shibao* styles itself independent; Western observers often label it “nationalistic,” and it is replete with what we probably would call “news analyses,” although they are not labeled as such. *Global Times* claims a worldwide staff of correspondents—neither Chinese nor English editions bothering to clarify that they are the *People's Daily's* correspondents, moonlighting for piece rates! *Global Times* editors have told interviewers that no government money went into launching the English edition. That's because the Chinese original can afford the investment.

The roster of magazines that used to be published in many foreign languages has been cut down substantially—*Beijing Review* remaining as a distillation of documents and major news—even as the domestic magazine marketplace has burgeoned. Technically, foreign investment is not allowed in media content—but in actuality, publications produced by and aimed at expats, emphasizing arts and entertainment coverage, have strong followings in Chinese cities.

The adoption and encouraged expansion of a government “spokesperson” system, the increasing practice of press conferences, including live televised sessions, at the national level, and production of central government white papers and plans on controversial issues—most recently, a human rights plan—are all part of developing a more sophisticated public relations apparatus for dealing with both the domestic and the foreign press.

The loosening of restrictions on international correspondents prior to the 2008 Beijing Olympics—and then an extension of the program after the Games—is sometimes interpreted as a PR move; but I think it actually is a sign that arguments within central units such as the Foreign Ministry and the State Council about the ultimate long-term benefits of greater openness and transparency have made headway.

Media outlets and government agencies have Internet operations of growing scope and importance. The Internet obviously poses special quandaries for Chinese authorities seeking to restrict and manage the terrain even as it necessarily expands.

WHAT FEEDBACK is generated, with what results on the communication process?

From the inception of the People’s Republic, Chinese media organizations have enlisted “foreign experts” to polish foreign-language content; and since the beginning of reforms, have invited foreigners to comment and critique—albeit with varying degrees of responsiveness. Some foreigners who have worked at *China Daily* will swear that all their advice fell on deaf ears. My experience—I worked at the paper its very first year of publication, 1981-82, have spent shorter periods there since and have kept up with doings there—has been quite different.

In general, though, responsiveness to the ostensible target audiences is not a strong suit!

WHAT EFFECTS does the communication produce? What are the implications or results of China’s external propaganda efforts, e.g., regarding knowledge, values, attitudes and behavior of individuals, groups, institutions and/or societies reached directly or indirectly; impact on media producers, organizations and institutions; influence on international activities, attitudes and policies, etc.

Here’s the real unknown. Should we make a presumption that China’s external propaganda amounts to psychological warfare, aimed at political influence, if not diabolical manipulation? Or shall we believe the assertions that motivations are benign, aimed at

sharing viewpoints and information and fostering mutual understanding and cultural exchange? And in either case, are the efforts successful?

Ultimately, potential influence relies on credibility—and the prerequisite for that of course is greater media independence. My own research suggests reason to be hopeful, but others have a bleaker view.

In my view, the most important ramifications of expanded external communication efforts may not be intentional objectives at all, whether malevolent or benign (although I tend to favor the benign interpretation). Rather, in my view, the more individuals, organizations and institutions are brought into the mere effort of trying to do better at communicating—which includes, centrally, the enhancement of abilities to deal directly in foreign languages with foreign people and cultures—the more potential there is for enhanced knowledge, sophistication and understanding of the rest of the world among Chinese involved in this project.

In other ways, the endeavor to develop media that in both format and content are not merely palatable but compelling to foreign audiences can have positive results for China internally. Specifically in reference to journalism, I would argue that external propaganda efforts, in exposing Chinese media workers to international knowledge, ideas and examples, create dynamics that further encourage professional trends in China's journalism corps.

HEARING COCHAIR REINSCH: Thank you.

Dr. Brady.

**STATEMENT OF DR. ANNE-MARIE BRADY, SCHOOL OF
POLITICAL AND SOCIAL SCIENCES, UNIVERSITY OF
CANTERBURY, CHRISTCHURCH, NEW ZEALAND**

DR. BRADY: Good morning. It's a great honor and privilege to be able to speak to you today on my research on China's propaganda system.

When I look at propaganda, the term "propaganda" in Chinese is not a negative term, and my focus is somewhat different from Dr. Polumbaum in that I'm looking at control, the objectives of the Party in managing the public sphere, and that's somewhat different from what the journalists are doing and thinking.

The Party places great importance on what they call propaganda and thought work. In fact, in the contemporary period, it's actually described as the lifeblood of the Party. People often talk about the Party's legitimacy in the current era being based on its economic performance. Well, the Party itself sees that it's not; it's based both on economic development and an incredibly strong awareness of the importance of managing the public sphere.

But what has to be noted about China's propaganda work in the current period is although the importance of propaganda work hasn't changed from the Mao era, the tactics have changed and the content has changed, and what's been very interesting in researching this topic is discovering how much China has been learning from the West in modernizing its propaganda system.

So they've been picking up techniques of political public opinion, which originated in the West, and those aspects of mass communication which support the propaganda state, don't undermine it, and so on.

China divides propaganda between foreign and domestic propaganda. However, nowadays, it's recognized that there are enough foreigners in the world who understand Chinese that even domestic propaganda has to be mindful of foreign audiences.

I would disagree somewhat with what Professor Polumbaum was saying about agency when it comes to foreign propaganda because there's a saying in Chinese, "waishi wu xiaoshi," and what that means is that foreign affairs is not a small matter. So domestic journalists have a lot more agency than those who work for China Daily and Xinhua News Service, People's Daily online in foreign languages.

And it's not to say the journalists wouldn't want that agency.

There's a station, CCTV-9, which was supposed to be China's CNN, and I visited and did interviews at that station a couple of years ago, and they were a very frustrated bunch of journalists and editors.

They desperately wanted to make their station China's CNN, but the authorities above would not let them. And that is a problem for China's international influence and its foreign propaganda. If the Chinese Communist Party would give its journalists involved in foreign propaganda media outlets the same amount of freedom that they have in the domestic media, it could well be a much more persuasive message.

That's what's interesting about this new station that's been talked of, that's going to be set up in either Thailand or Singapore, the station that both my previous panelists mentioned, because if that station was allowed to be like Phoenix Television, which is regarded as independent and yet more loyal than CCTV, that could be a very persuasive TV station, and not necessarily to viewers like myself or yourself, but to one of the main intended audiences of China's foreign propaganda, and that's the overseas Chinese.

China has been working very, very hard, since 1989, to build the support of the overseas Chinese because the Party leadership realized in 1989 that not only did they not have the support of many Chinese outside China, but that overseas Chinese were actually supporting the democracy movement in China, actively involved in undermining the Party-State.

So the Chinese government has made a major investment in what they call overseas Chinese work, "qiaowu gongzuo." And this is one of the main targets, as I said, of foreign propaganda work.

So if the Party can develop or support the development of a station that is more like the Chinese domestic media, which is now doing very, very well, it is very popular outside the Party papers, the Chinese mainstream media has a lot of support from the readers.

People make a distinction; that the journalists are mediators between news and propaganda, and it's kind of an arbitrary divide in some ways. But the readers think they're reading news and they're not reading propaganda.

Just briefly, because I know I have very little time, the propaganda system in China is huge and comprehensive, and propaganda, the idea of what consists of propaganda, is much, much broader than we might normally think of it, and foreign propaganda is similarly more than just news outlets.

So it also is about contacts between people, PR associations and media campaigns on topics like AIDS. So China's expansion of its foreign propaganda is going to be much broader than things we're accustomed to looking for like TV stations and newspapers.

Thank you.
[The statement follows:]

**Prepared Statement of Professor Anne-Marie Brady, School of
Political and Social Sciences, University of Canterbury,
Christchurch, New Zealand**

Overview of China's Foreign Propaganda

The Chinese government puts a high value on propaganda work, describing it as the life blood (*shengmingxian*) of the Party-State in the current era. The Chinese Communist Party (CCP) has historically divided propaganda work into two categories: internal (*duinei*) and external (*duiwai*), meaning that which is directed toward Chinese people and that which is directed toward foreigners in China, Overseas Chinese, and the outside world in general. CCP propaganda specialists also divide propaganda into four types: political, economic, cultural, and social. Relevant offices within the Chinese Party-State administration take over responsibility for propaganda work related to their area of expertise.

China's foreign propaganda experts are extremely critical of what they call the "Western media's ideological assault on the rest of the world." It is a matter of pride that in the current era, unlike the Mao years, China does not push its political ideology onto others. Unlike the Mao era, China's post-1989 foreign propaganda tends to be defensive, reacting to external criticisms and aimed at upholding China's political *status quo*. However foreign propaganda targeted at Overseas Chinese and the Taiwanese is essentially offensive in nature, with strategic goals in mind such as neutralizing support for anti-CCP forces and promoting Chinese reunification.

The audience for China's foreign propaganda is not one and the same, so different messages are promoted at different groups. The main divide in China's foreign propaganda is between Overseas Chinese and non-Overseas Chinese. The Taiwanese are targeted as a sub-category of China foreign propaganda targeted at Overseas Chinese. In the following sections I will discuss the themes, audiences, means of transmission, and institutional actors involved in China's contemporary foreign propaganda, as well as China's plans to expand foreign propaganda activities in the future.

Central Level Institutional Actors Involved in Foreign Propaganda

The Central Propaganda Department is in charge of all internal propaganda, while its brother organization, the Office of Foreign Propaganda, which is more commonly known by its other nameplate, the State Council Information Office, oversees matters relating to external propaganda. The two bureaucracies are closely linked and coordinated. In recent years, with the advent of the Internet and China's increasing globalization and internationalization, the boundaries between the two categories of propaganda have been growing less and less obvious. For example the Office of Foreign Propaganda has been put in charge of monitoring the Internet both inside and outside China, while the News Department of the Central Propaganda Department also takes a close interest in developments in the same area, providing guidelines on the topic in its regular bulletins to propaganda workers around the country. In 2003, due to the increasing numbers of Chinese-speaking foreigners (either living in China or reading Chinese newspapers online outside China) and Chinese citizens who speak foreign languages and have access to foreign media sources, the Central Propaganda Department actually argued that internal propaganda should now be regarded as the same as external propaganda. This means that Chinese journalists must be mindful that they now have a foreign audience alongside their domestic audience.

The CCP Central Committee Foreign Propaganda Group which is a top level committee consisting of the heads of leading foreign propaganda outlets, has a central guiding role in setting foreign propaganda policies. These are implemented by the OFP/SCIO at the national level and by provincial level foreign

propaganda offices at the local level. The OFP/SCIO and its local equivalents direct officials in various government departments and work units whose interests touch on foreign propaganda, such as foreign affairs; foreign trade; tourism; Overseas Chinese Affairs; radio and television; the print media; publishing; cultural, educational, and sporting institutions; as well as State planning, finance, State security, public security, customs, Taiwan affairs, and banking.

The Office for Foreign Propaganda/State Council Information Office (OFP/SCIO) is tasked with managing any sensitive news stories on the following topics: foreign embassies, diplomats in China, Overseas Chinese business people, foreign students, foreign travellers, Hong Kong, Macau, and Taiwanese residents, especially when they involve loss of life. They also guide the Chinese media during any major events regarding Tibet, Xinjiang, ethnic minorities, religion, human rights, democracy movements, internal and external terrorist activities, and Falungong. For extremely serious incidents, only Xinhua News Agency is allowed to report on them and all other Chinese media must use the Xinhua report word for word.

The OFP/SCIO is also in charge of “clarifying and refuting” any stories which, while forbidden from being reported in China, have been reported on in the foreign media. Articles on foreigners are to be sent to the Ministry of Foreign Affairs for verification. Similarly, stories on Hong Kong, Macau, and Taiwanese residents are to be sent to the Offices of Hong Kong and Macau, or Taiwan Affairs, while stories on Overseas Chinese businesspeople should be sent to the Ministry of Commerce. The Ministry of Culture is in charge of China’s foreign cultural propaganda, under the leadership of the CCP Foreign Propaganda Group. Cultural exchanges are regarded as useful way to break through prejudice and establish warm feelings.

Overseas Chinese

Gaining influence over Overseas Chinese groups outside China in order to “turn them into propaganda bases for China” is a key task in foreign propaganda work. The student protests of 1989, which received strong support from the Overseas Chinese community, alerted the Chinese Communist Party (CCP) to the fact that many within the Overseas Chinese community were inclined to support democracy activities within China. Historically China’s revolutionary movements have always received considerable funding from the Chinese *diaspora* and many Chinese revolutionaries found safe haven in Overseas Chinese communities when the political situation in China became to tense. At the same time, as China’s economic reform process continued to expand after 1989, and especially from 1992, China sought to tap in to the considerable economic resources of the Overseas Chinese as a source of investment and technological transfer.

After 1989 China’s propaganda targeted at the Chinese living outside China—whether they were PRC passport-holders or ethnic Chinese who had been residing abroad for generations—aimed to build patriotic sentiment towards the Chinese Motherland (*zuguo*), and support for the political *status quo*. The goal was to neutralize antagonism towards the CCP government, enhance antagonism towards anti-CCP forces within China and their adherents in exile, and at the same time, encourage a constructive attitude towards Overseas Chinese helping to make China “rich and strong” (*fu qiang*). These efforts have been remarkably successful.

The means by which China promotes its foreign propaganda towards the Overseas Chinese community include: the numerous local Chinese language newspapers, radio and television stations; the Internet, China’s own China Central Television channel aimed at Overseas Chinese CCTV 4; as well as through cultural activities; support for the teaching of Chinese language internationally which includes the rapid spread of Confucius Institutes; and special activities organized for the Overseas Chinese community such as conferences and “root-seeking” (*xun gen*) cultural tours.

China’s Xinhua News Service currently provides free content to the Chinese language news media outside

China. Formerly Hong Kong and Taiwan-based news groups were the main source of news for Overseas Chinese, but in the last ten years they have basically been driven out of the market by a plethora of free Chinese newspapers which derive virtually all their content from the Mainland media. Few Chinese language newspapers outside China have the financial resources (outside of Taiwan, Singapore or pro-Falungong papers) to resist the offer of free content. The same goes for Chinese language radio and television stations abroad, they too now relay Mainland media programmes and exclude other Chinese language sources. Chinese embassy officials work closely with the Overseas Chinese media in order to ensure their continued compliance. It should be noted that in the current era, Xinhua reports are virtually indistinguishable from stories off the wire that might be available from say Reuters, with the exception that they represent a pro-PRC, pro-CCP viewpoint and match current propaganda guidelines on avoiding taboo topics. The PRC long ago stopped promoting revolution or its state ideology.

The Internet has become an extremely important means for China to build support with Overseas Chinese in the last ten years. PRC-based Internet sites are now the leading source of Chinese language and China-related news for Overseas Chinese. The Internet is also proving to be an extremely effective tool for guiding and organizing Overseas Chinese public opinion. An example of this was the role of the Internet in organizing popular protests by Overseas Chinese in 2008 against the perceived bias of the Western media in its coverage of unrest in Tibetan areas in March 2008 and, a month later, in organizing a series of worldwide demonstrations in support of China during the Olympic torch relay. These protests and the later demonstrations were genuine and popular, which shows the effectiveness of China's efforts to rebuild positive public opinion within the Chinese *diaspora*, but it should be noted that they received official support, both symbolic and practical. This development matches the rise of popular nationalism within China since 1989, which has been fostered from the top down, but has a genuine resonance with the Chinese population.

Despite being genuine popular movements, the protests and demonstrations adopted the slogans of CCP foreign propaganda directed at Overseas Chinese such as "Ai wo Zhonghua" or "Love China". Thanks to the Internet, even those who could not attend demonstrations could show their support for China by attaching a red heart moniker next to the word China to their avatars. This initiative was launched by MSN China and spread rapidly throughout the Chinese Internet in 2008. MSN's involvement not only demonstrates how many Chinese companies respond to the CCP propaganda message on patriotism, but it is also an indication of how these days the propaganda message is not just promoted directly from propaganda authorities; rather it is frequently relayed through intermediaries on to a wider audience.

During torch relay demonstrations in cities such as Canberra, San Francisco or Seoul in 2008, Overseas Chinese were not compelled to turn up and there were no consequences for not taking an interest, but those who did come were given free matching t-shirts, souvenirs, transport, and in some cases accommodation, all courtesy of local embassy officials and China-based donors. These demonstrations successfully drowned out the protests of anti-CCP groups such as Falungong, Tibetan activists and human rights groups who had hoped to use the Beijing Olympics as a vehicle to promote their criticism of the Chinese government.

Taiwanese

A sub-group of China's foreign propaganda directed at Overseas Chinese is that directed towards the Taiwanese. The message aimed towards them also aspires to build feelings of patriotism towards the Chinese Motherland and support for the political *status quo*, but it is also designed to garner support for the reunification of Taiwan with the Chinese Mainland. These efforts have also been relatively successful in recent years.

Some of the means which China employs to promote its views to Taiwanese audiences include: special television programmes directed at Taiwanese audiences on CCTV 4; the setting up in 2005 of Strait Star

TV a Fujian Province-based satellite station which beams towards Taiwan; study tours for the Taiwanese elite; joint conferences held on themes which help to build common interest such as Chinese heritage and Confucianism; and the hosting of large-scale events which promote notions of ethnic unity across the Taiwan Strait such as commemorations for the birth of Confucius, celebrations for the cult of Mazu (which is prominent in Taiwan and Fujian) and ceremonies in honour of the Yellow Emperor, the symbolic ancestor of all Han Chinese.

Foreign Propaganda Targeted at Non-Chinese

China's foreign propaganda directed at non-Chinese audiences has undergone major reform in the last decade. These reforms are indicated by the Chinese media's avoidance of the term "propaganda" in foreign language publications to discuss CCP media management, though the term "xuanchuan" (propaganda) continues to be used in Chinese. So for example, the CCP Central Propaganda Department (*Zhongxuanbu*) is now translated as Central Publicity Department by *China Daily* and Xinhua and they use terms such as "publicity", "information", "public relations", "cross cultural communication" and "public diplomacy" to discuss activities which are still classified as *waixuan* (Foreign Propaganda) in Chinese language publications. As in its domestic propaganda, China now adapts many of the methods of public opinion management which originated in modern industrialized societies such as the United States.

China's international image was considerably damaged in the eyes of non-Chinese foreign audiences after 1989. Since that date China has worked hard to build constructive international public opinion. The overall themes of China's foreign propaganda work since 1989 and up to the present have been to promote the image of China's social, economic, and political stability; as well as the continuance of China's reform and opening up policies and CCP leadership over the political system. But in particular, promoting the Chinese economy and encouraging further foreign investment and trade has become the primary task of foreign propaganda work, particularly after 1992. Throughout the 1990s China was certainly successful in promoting awareness of its economic growth and enthusiasm for the opportunities which the Chinese market offered international investors, but perceptions towards the politics of China proved much harder to shift, at least among Western audiences. It should be noted that beginning in the 1990s and continuing up to the present day, China's prestige began to grow in the developing world.

Promoting a new national image (*guojia xingxiang*) internationally was one of the key strategic goals of China's 2008 Olympic bid. The new image aimed to allay international fears about China's increasing political, economic and military power, at the same time as projecting awareness of China's renewed strength and prosperity. The two weeks of the August 2008 Olympics were indeed a sporting and PR triumph for Beijing. Despite the controversies surrounding hosting the Olympics in Beijing—human rights, the environment, food safety and other issues—the Chinese government actually managed to increase its public approval in China and succeeded in re-shaping its image on the international scene.

There are multiple means adopted for the transmission of China's foreign propaganda targeted at non-Chinese foreigners. These include PRC-based foreign propaganda outlets such as *China Daily*, CCTV-9, China Radio International, *People's Daily* online published in translation in a number of languages, and china.org the main portal for China's foreign propaganda, as well as publishers such as the Foreign Languages Press; but they also include the foreign media and foreign VIPs who China targets to promote certain views. In the following section I will discuss some of these channels for transmission in more detail.

CCTV-9 was launched as a 24-hour channel in 2002, and from 2004, it began broadcasting in Spanish and French. In September 2005, the station was re-launched with much fanfare, though with little noticeable change to content or style of programming. The goal was to make CCTV-9 China's equivalent to CNN, a global media presence with 24-hour news coverage. However, unlike CNN, which is not (formally at least) the mouthpiece of any particular government, CCTV-9 is most definitely the mouthpiece for the Chinese

government's perspectives on international affairs and the Party-line perspectives on China's own affairs. The station has been granted substantial resources in terms of equipment; but has no editorial independence. CCTV-9 journalists are under constant pressure to present a positive account of China. In August 2005, a series of items reported factually on coal mining disasters in China; soon after the channel's leaders received a warning from the Ministry of Foreign Affairs that its reports were harming China's international image. Following this incident, senior editorial staff and journalists were all forced to write self-criticisms. This is a classic example of the current relative lack of agency of Chinese journalists involved in China's foreign propaganda activities aimed at non-Chinese foreigners. In many ways they are more constrained than journalists who write for Chinese audiences.

A further channel for China's foreign propaganda is the Chinese PR Association, set up in the early 1990s, which works closely with the Central Propaganda Department towards the goal of "optimizing a pro-China international environment," "establishing a positive image of China internationally," and "packaging China." One of the organization's tasks is to act as an intermediary between foreign embassies and organizations in China with Chinese government departments. The association also takes a behind-the-scenes role in PR campaigns (targeted at the concerns of Western governments and NGOs) such as the high-profile anti-AIDS campaign of November-December 2002.

The CCP has a longstanding policy of utilising foreigners in its foreign propaganda work, this is called "using foreign strength to promote China" (*liyong waili wei wo xuanchuan*). Historically, pro-CCP foreigners have been extremely useful in producing a wide range of propaganda materials, ranging from books, films and poetry, to public and private lobbying. Soon after June 4, Jiang Zemin instructed foreign affairs personnel to step up their activities to garner the support of prominent foreigners "friendly to China," to influence Western governments and get them to drop their sanctions against China. Henry Kissinger and George Bush Senior are commonly cited as being particularly helpful (behind the scenes) to blunt the effects of sanctions in this period. The foreign friends the CCP has come to value most in the post-1989 period are prominent foreign figures that can bring commercial and political advantages to China and the Chinese oligarchy. Public agreement on China's political positions is not required, though it might help business along a little.

In the years since 1989, Beijing has worked hard to get foreigners to promote China. Foreigners based in China and Western China specialists are often approached by foreign affairs cadres to write articles on China for the Chinese media. Naturally, only viewpoints which are in accord with the current propaganda line can be published. *China Daily* specializes in featuring this type of material, although similar stories also periodically appear in the Chinese language media. Another tried and true practice in China's foreign propaganda work is to bring in "prominent person" foreign delegations on all-expenses-paid tours of China, in the hope that they will go home promoting China's point of view. Local propaganda officials are instructed to host foreign journalists and researchers; do thought work on foreign experts, students, tourists, Taiwanese, and Overseas Chinese; and increase sister-city exchanges; all in order to create an "international army of friendly propagandists" for China.

In 1992, a meeting of foreign propaganda officials was held to discuss techniques for getting China's propaganda materials published in the Western media. Since that meeting there has been a dramatic increase in materials published abroad. Between 1992 and 2000 over two thousand articles were published in Taiwan alone. China's propagandists try to get foreign newspapers to do China's propaganda work; this is called "borrowing foreign newspapers" (*jieyong haiwai baokan*). In order to achieve this, China's local level foreign propaganda officials host approved foreign journalists, take them around approved sites and give them materials for their reports. Non-approved visits to sensitive sites (if found out) can have foreign journalists thrown out of China.

In early 2009 Beijing announced that it would invest a further phenomenal 45

billion yuan into its main media outlets to strengthen their international news coverage and global presence. As part of this, Xinhua News Service will increase their overseas bureaus from 100 to 186, almost enough to have one in every country in the world. The *Global Times*, an extremely popular *People's Daily*-owned tabloid with a strong international focus, will soon set up an English language edition. And CCTV-9 will set up Arabic and Russian language services.

There are also concrete plans in the next two year to establish an Asia-based television station (Singapore or Thailand are the likely locations) that would beam global news to the world as told from a pro-PRC perspective. This new channel would take as its model Phoenix Television, which is beamed via restricted satellite to the Chinese elite within China and on paid satellite tv outside China. Phoenix is nominally privately-owned; however its current main investor is the State-owned enterprise China Mobile.

Phoenix has long been regarded by Party propaganda insiders as “more loyal than CCTV”. The proposed new channel would similarly be “privately-owned” and closely tied in to the CCP foreign propaganda agenda. If it were to follow the Phoenix Television model, which is that of a “loyal opposition”, this channel could well be more effective than CCTV-4 or CCTV-9 in building positive international public opinion for China. It certainly is likely to appeal to Overseas Chinese audiences as will focus on stories which are close to their interests and not covered elsewhere in such detail, while retaining the crucial impression of “objectivity” which CCTV-4 and CCTV-9 often lack. The new channel could also prove to be appealing to many viewers in the non-Western world such as Africa, the Middle East, South America and the South Pacific who are attracted to China’s alternative perspective of global affairs. As such this new initiative could well have a significant impact in strengthening China’s soft power internationally.

Panel I: Discussion, Questions and Answers

HEARING COCHAIR REINSCH: Thank you very much.

We'll continue now with questions. Commissioner Fiedler.

COMMISSIONER FIEDLER: Thank you.

I have two questions, one of which is a factual question. Could one of you, and perhaps it's Dr. Brady, discuss the difference between domestic control and external controls? In other words, who are the institutional participants on the external side that are different from the domestic, and including within that the role of the Foreign Ministry, which has often struck me as subordinate to other players?

DR. BRADY: First of all, in contemporary China discussion on these issues, they don't use the word "control" anymore. They use the word "management," "guanli."

That's an important distinction. It's not just an artificial change of wording. What it implies is that they are allowing the media a lot more freedom, and there's this talk of the media as a tool, and in the past, the media had to be the tongue and throat of the Party.

So the media as a tool is a media that is more like the media in this country where it's independently funded and separate from the state, and yet the government and different agencies can have a lot of influence in the media. At least that's how China sees it. The theories of Norm Chomsky are very popular in China. They're sort of saying

that works; we want that.

So in terms of the different agencies involved, there's a Central Propaganda Department which is kind of like the Vatican of China's propaganda and thought work. It's a small organization, about 300 or so people, and they're a processing station for a whole lot of other agencies that do policy work and also other groups.

The state organization is involved in the propaganda system which administers the policies so there's a separation between the ideas and the policies and the administration. And the Central Propaganda Department has a brother organization, the Office of Foreign Propaganda, which has another nameplate. Typical in the Chinese bureaucracy, you'll have one office, two nameplates. Its other nameplate is the State Council Information Office.

Both the Central Propaganda Department and the Office of Foreign Propaganda, they have some overlapping duties related to foreign propaganda activities, which I've explained in my statement. It's quite complicated. The Foreign Ministry has a role, too, and they sometimes come in on certain issues. I mentioned CCTV-9 and the journalists attempt to have some independent views.

An example [of what happens when the journalists tried to be independent] was in August 2005. There had been a series of coal mining disasters in China, and it caused a lot of attention not just outside China but within China, CCTV-9 actually reported in some detail and factually on coal mining disasters, then they got a slap on the hand from the Foreign Ministry saying you are making China lose face. And so the Foreign Ministry is a part of what they call the "xitong," the supra-bureaucracy involved in foreign propaganda.

There are these spider web-like bureaucracies over the top-down state bureaucracies in China on different topics. There's one on propaganda as a whole. There's another on foreign affairs. Defense is another one. Imagine these spider webs linking a whole lot of agencies. So Foreign Ministry is part of foreign propaganda bureaucracy, but it's not a leader. But they can step on an issue like that.

COMMISSIONER FIEDLER: Thank you.

One additional question. What role do any U.S. companies play in assisting Chinese agencies? For instance, I have knowledge of some Western PR firms doing crisis management advice. What role do they play?

DR. CULL: Following Tiananmen, it was Hill & Knowlton who rebuilt China's international reputation or worked to do that.

DR. BRADY: Yes. I'm sure it's a topic that the companies probably want to keep fairly secret, but Hill & Knowlton is one of the companies that we know of involved in China's PR bidding to help

China with its PR.

Saatchi and Saatchi is another big one. The names go on because they see China as a market for them. They've got a product. They want to sell it. So it's just another opportunity from the point of PR companies, and there have been a series of conferences where PR companies are trying to pitch to China this is what we can do for you.

COMMISSIONER FIEDLER: Are they effective, in your judgment? Is their advice being taken?

DR. BRADY: It's very interesting actually. In a paper I just wrote on the Beijing Olympics as a "campaign of mass distraction," I cited the speech of the CEO of Saatchi & Saatchi in 1998, and he was telling China that they needed to rebrand, and he mentioned the China brand, and [the concept he was espousing] kind of sounded like Falungong.

It was these New Age concepts of this ancient culture and so on and values that he couldn't find elsewhere. But elements of that were indeed present in the images that China was presenting in the 2008 [Olympics] Opening and Closing Ceremonies, its ancient culture, and a very selective vision of Chinese history, and so on.

That's something that we have to note as well about the foreign propaganda today is that China doesn't promote its ideology globally although the China model is to an extent promoted to countries like Cuba and North Korea and possibly parts of Africa and the South Pacific.

The main focus of China's foreign propaganda is economic. The [message promoted is that the] Chinese economy is doing well you should invest in the China market, and so on. That may not be true. As we know, Chinese statistics are not always reliable.

The other aspect is Chinese culture and China's perspectives on the world. So China has to get that out. Whether it is effective or not is another story.

COMMISSIONER FIEDLER: Thank you.

HEARING COCHAIR REINSCH: Commissioner Wessel.

COMMISSIONER WESSEL: Thank you all for being here and for winning the award for the longest travels to get here. So we appreciate your being here today.

I'd like to follow up on Commissioner Fiedler's question just for a moment in terms of institutions or companies that assist. It had been my understanding, and Dr. Cull, you talked about the listening mode, the polling, that some years ago, and I haven't updated this information, that foreign entities that wished to poll the Chinese people had to have their questions and their activities, in fact, approved by the central government.

But I guess whether it's Hill & Knowlton or others, they get to

listen here. Is that still the case?

DR. CULL: That's not my area.

COMMISSIONER WESSEL: Okay.

DR. CULL: I'm interested in what the Chinese government is doing overseas.

COMMISSIONER WESSEL: Okay.

DR. CULL: We know that they're listening very carefully to what is said in the Western media. Going through speeches by senior Politburo figures, we can see that they pepper them with quotes from what Western journalists have said what the Western media are saying, and what the world's media thinks of China.

COMMISSIONER WESSEL: But are they doing more active enterprise, not just doing open source review, but looking at commissioning polls--

DR. CULL: Sure, yes

The most famous one being the jointly commissioned poll on Chinese/Japanese mutual public opinion, which produced really quite alarming results of evidence of the split between those two countries. That was one where they actually worked with the Japanese government to conduct a poll.

COMMISSIONER WESSEL: Do either of the other witnesses have a comment on that?

DR. BRADY: Yes. This is something that I've looked at a little bit in my research, and public opinion polling is a very, very important part of propaganda work these days, particularly in domestic propaganda, where it's sort of like the government wants to identify what are the problems going on in society and then put some Band-Aids on them in advance of them becoming a bigger problem.

It is technically true that foreign companies who want to engage in social science surveys in China do need official approval, but rules and regulations are one thing in China. What happens on the ground can be quite different. But if a foreign company is working with a Chinese partner, all these things are much simpler.

COMMISSIONER WESSEL: Okay. A separate question is, as we look at the current economic crisis worldwide and China having its financial coffers fairly well stocked and now expanding its go-out strategy, are you seeing that they are able to benefit from the economic crisis in terms of expanding their reach overseas? What implications is that having? Each of the witnesses, if possible.

DR. POLUMBAUM: One thing I can say is I recently made a very brief visit to Beijing and kind of checked in on a couple of organizations including China Daily and the new Global Times right before the English edition was launched. And one impression I have is that large amounts of money are available, not necessarily from the

government, but from, generated within organizations for expansion, and there's a great frenzy to spend it on something to do with expansion without a great deal of thought.

For instance, China Daily earlier this year launched what it calls a North American edition, which isn't really a North American edition.

It's at this point a supplement, a weekly Monday edition to the regular paper, but is being printed and sold, apparently--although nobody I know has seen it--in San Francisco and New York. I think 20,000 in each place.

There's an evident assumption on the part of editorial management who launched this that there is a demand for this in San Francisco and New York, whereas, any of the editors, sort of working editors you talk with about this, think it's just, well, nuts, but they welcome the expenditure of the money because it's helping them train young reporters to do better, and they've been able to hire some additional foreign editors to help train these reporters and they see it as a kind of a building of expertise within China Daily.

Similarly, the audience for the English edition of Global Times and the purpose of that is kind of amorphous and diffuse, but the Chinese edition, Huanqiu Shibao, is very popular, very successful, and a money-making operation, so there is money to spend, but not very well thought out as far as I can tell.

COMMISSIONER WESSEL: Okay. My time is up.

HEARING COCHAIR REINSCH: Do you want the others, too, to comment as well or not?

COMMISSIONER WESSEL: If possible, yes.

HEARING COCHAIR REINSCH: I think we can take a minute since we don't have too many questions. Do either of the other two witnesses want to comment or respond to the question?

DR. BRADY: Just briefly. I'd agree with Dr. Polumbaum. There's a lot of money available, not always a lot of planning about how to spend it, and there's been a real problem for these agencies, traditional agencies involved in China's foreign propaganda activities like China Radio International, China Daily, and CCTV-9, in having trained staff or trained journalists and with good foreign language skills, and often they'll get them, they'll train them, and then they'll go off to a better paid job elsewhere.

So some of the money, we can assume, is topping up salaries and then dealing with the whole issue of benefits which are associated with jobs in China. So it's not necessarily--it's like spending on the Chinese defense forces as well. They've got a long way to go.

DR. CULL: I'm interested to see this diversification with the launch of the Russian version of CCTV and the Arabic version of CCTV this year. They're advertising in the trade papers looking for

people to serve on these TV channels.

I hope we'll get into--at some point--what we think the objective is here because I think some of Dr. Polumbaum's points are very suggestive of what the real priority is behind this. I think that what emerges when you start looking at these elements of Chinese propaganda overseas is that a lot of what is important is that something be seen to be done.

And that this is focusing on the ability to say to a domestic audience Chinese news is available on the streets of American cities, to be able to say there are 100,000 people worldwide now learning the Chinese language in Chinese government institutions, to be able to say we have 200 cultural centers around the world, and that these are not just paid by the Chinese government, but these are partnerships with people who are desperate to learn about China and to honor the glories of the Chinese culture. What I'm talking about here is conducting domestic propaganda by conducting foreign propaganda, and once you put that frame around what is going on, it makes much sense.

It's much more likely that people domestically would be impressed by 2008 drummers drumming in unison at the Opening Ceremony of the Olympic Games than the people in the world would actually find that an attractive thing to look at. It's about being seen to be able to display and about the kudos that come to the Communist Party by saying, "Look, behold, we give you the gift of the admiration of the world."

That is a big thing to lay before your own people, and once that frame is put around Chinese public diplomacy and propaganda activities, I think a lot of these odd little corners become clearer and it explains to me why some of these things are happening in the way that they're happening.

DR. POLUMBAUM: I would add just a little side note here. The University of Iowa where I teach has a Confucius Institute. It was one of the first that was established in the United States.

The only awareness we have of any Chinese official presence is when the institute was officially started, the consul from Chicago, Chinese Consul, came to put up a plaque and then couldn't even stay for a day. He had to go back for business.

This institute is basically run by a linguist, language expert, originally Chinese, now an American citizen, who is a phenomenal organizer of language programs and has used it to bring doctoral students in Chinese language teaching from China. So there's a whole infusion of young language teachers that turns over every year, and there are community classes and classes, extra classes in the university, and it's seen as a real contribution to our academic programs.

It also has matching funding from the university so in no way is it regarded as, and it actually doesn't operate as, an arm of Chinese public diplomacy, but from the Chinese point of view, it is.

COMMISSIONER WESSEL: Thank you.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Brookes.

HEARING COCHAIR BROOKES: Thank you.

Just to quickly follow on that and then I have another question. So you don't believe that the Chinese government is deluded into thinking that there's this tremendous interest in Chinese news overseas?

American newspapers are having enough trouble themselves getting people to buy their newspapers, but you think it's more of a be able to return--it's basically focused on the domestic audience as opposed to a foreign audience?

DR. POLUMBAUM: I think there is some of that delusion.

HEARING COCHAIR BROOKES: Oh, you think they're deluded?

DR. POLUMBAUM: I really do.

HEARING COCHAIR BROOKES: The way Dr. Cull said it is that they know what they're doing. There's a method to the madness. He understands that and he realizes it's reflected on the--

DR. POLUMBAUM: I absolutely agree with him.

However, I do think that at higher levels of the propaganda apparatus, that there is some overblown expectation that foreign audiences have an appetite for direct news from China.

In fact, we know that audiences are obstinate; they're resistant. They interpret. Chinese audiences are obstinate, read between the lines. We certainly are. So the issue of credibility is vital, and people who get unfiltered news interpret it in terms of its source. So I would say yes, there's some of this delusion, but it doesn't explain what's happening.

DR. CULL: I would agree with what Dr. Polumbaum is saying. I think that as with the former Soviet Union, there are people who believe their own propaganda, and in the end in the case of the former Soviet Union, the last people who believed that the Soviet Union was a great gift to the world and that everyone loved it were the people who were actually paying demonstrators to demonstrate in support of their system on the streets of third-world cities.

So, it's a really peculiar--the human capacity for self-delusion is certainly present here, but then China isn't the only place where people delude themselves that the world is fascinated by their way of life and is desperate to be just like them.

HEARING COCHAIR BROOKES: Okay. Dr. Brady, I have

another question, but I just wanted to keep pulling on this string for a moment.

DR. BRADY: I'd just like to add, though, that I do think that this big investment has come about because that's come, China very much feels that, and the Chinese population feels so the government feels, and those involved in propaganda work feel, and the population are in great sympathy with this idea that the West is continually distorting news about China, and that is an issue of great concern and so China wants to do something about it.

They've been trying to do something about it for a long time, and part of their foreign propaganda work is about hosting foreign journalists in China, preferably ones who don't speak Chinese and don't have their own contacts there, and making them very welcome in every possible way, and the Olympics, the hosting of the foreign journalists, this was the plan. It didn't always work that way because the journalists ended up feeling smothered according to my research.

But China has a number of ways in which it tries to get its voice out to the world. So it's not all about China Daily, which if any of you read it, it's not the kind of thing you'd want to pay a lot of money for on a regular basis. It's not the New York Times, but if Global Times comes out with an English language version, I'm going to want to read that because Global Times is a very interesting paper in Chinese.

So that's an interesting development and I think that's related to what I was saying about the media as a tool. So moving from the media as the tongue and throat of the Party and giving the media some independence, assuming it's not going to always do what you want it to do, but that people think it's going to be--think it's independent, and so they want to read it more, and so China, as I said, China really wants to get its own voice out to the world.

It feels very hard done by the Western media and Western media companies. So they think it's worth putting a lot of money in on all sorts of levels so that people will hear what they have to say and their perspective on world events.

HEARING COCHAIR BROOKES: I have a few moments left. Dr. Cull, if I understood you correctly, at the end of your testimony you said that, and I agree with this assertion that the United States needs to pick up the pace in terms of its public diplomacy.

DR. CULL: Absolutely.

HEARING COCHAIR BROOKES: What are the costs of not picking up the pace or being more effective for the United States vis-a-vis the Chinese efforts?

DR. CULL: Well, I think waking up and finding that people's attentions are elsewhere. Relationships are moving away from the United States, that influence is declining, and the world has moved on,

and while the United States is busy focusing on its own economy and on the Middle East, Latin America, Africa, East Asia have found other things to think about and other people to work with, and the relationships that have flowed naturally from America's presence in those places have declined, and opportunities no longer exist for this country, and influence no longer exists for this country.

HEARING COCHAIR BROOKES: Okay.

DR. CULL: We're talking about relative decline. We're talking about being left behind, and so I see it as a really severe problem. It's about maintaining your relationships, and you don't only talk to people when you want something from them.

HEARING COCHAIR BROOKES: Thank you.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Shea.

COMMISSIONER SHEA: Thanks very much for being here. Can you see me?

DR. CULL: Yes.

COMMISSIONER SHEA: I got scolded yesterday by a member of the Commission staff for failing to return this book by Professor Brady. It's in the Commission library so it's duly returned, John.

I have two questions actually. Professor Brady, you mentioned that the Chinese leadership is concerned about the impact of economic growth on political stability. They're also concerned about public opinion. I was wondering how do you assess their efforts marketing the economic stimulus plan, marketing what the government is doing in response to the global financial crisis? How are they providing what they view as "the correct guidance of public opinion," and are they being successful?

DR. BRADY: This kind of activity in China is always done with an optimistic point of view assuming they're just going to do the best they can, and how it's received is another story. It's not necessarily the focus of the materials that I look at. It's this is what we've got to do and we've got to do it well.

The promotion of the economic stimulus package I think has been received quite well internationally, probably because Western self-esteem is rather battered at the moment as a result of the problems in all our respective countries.

So, China, for my country, the Chinese economy is very, very important so there's a great sigh of relief if it looks like China is going to muddle through because if they're going to muddle through, then they're going to continue to want to buy our products.

In fact, there's been a ten percent increase in sales of dairy products from New Zealand, and our dairy industry is 30 percent of the New Zealand economy. So I think my impressions are that that kind of

information about that program have gone well.

But one thing we all know, those of us who look at Chinese politics, is that the plan is one thing; what happens on the ground can be completely different. And that's what is so interesting about China's foreign propaganda on the economy. We need some economists with Chinese language skills to come and break it down for us and do some research on what actually happens on the ground and if it really works, if local governments are pocketing the money or actually putting the money into the economy.

When it comes to the domestic market and the domestic consumers and how they're responding to the economic message from the government, the government has to sell it well because this is such a tricky year for China. There are too many anniversaries plus an economic crisis. They've got to get through this year.

COMMISSIONER SHEA: So an internal propaganda effort I assume is in overdrive to promote the positive benefits for the economy?

DR. BRADY: Yes, that's right. Everything is supposed to be good in the economy, and even when you lose your job, it all works out in the long run because you start out with this whole new career that you never would have done.

So that's what's going on in the TV channels at the moment, and there's quite a difference between the different kind of mediums in China.

The newspaper is one kind of audience. TV is the most mainstream; it's the main propaganda tool for the masses who don't necessarily read Chinese. There's still a lot of illiteracy in China.

Radio is another audience. Internet is completely different. The kind of debates you find on the Internet are much more complex and can be quite critical of government policy.

COMMISSIONER SHEA: Dr. Polumbaum or Dr. Cull?

DR. POLUMBAUM: I think an important discussion that's starting both in China and all over the world about the Chinese economy, and I'm not an economist so my take on this is very superficial, is what the world economic crisis means for China's longer-term economic strategy, and I think China suddenly appears to be quite vulnerable in terms of its tremendous dependence on an export-driven economy combined with its growing dependence on energy imports.

So I suspect that there's going to be a conversation about, even as China becomes increasingly entangled with the global economy, how to decrease these sorts of dependencies, and how they do it, of course, has tremendous implications for our own economy.

DR. CULL: All I would add is that it's interesting to see how

the Chinese political discourse is pointing to a Western admiration for socialism with Chinese characteristics, and they're saying the West now acknowledges that only socialism with Chinese characteristics can do this.

COMMISSIONER SHEA: Right.

DR. CULL: Like the old ad for Heineken beer, "only Heineken can do this because it refreshes the parts other beers cannot reach." Only socialism with Chinese characteristics can do this because it develops a country like no other system ever could. It's in the Chinese political discourse "Westerners are now acknowledging this"--and I'm seeing that crop up in speeches.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Mulloy.

COMMISSIONER MULLOY: Thank you, Mr. Chairman.

The question I have is related to something Dr. Polumbaum just said. She pointed out in passing that China does have a longer-term economic strategy. That's her term. Do you both agree with that, that China has a longer term economic strategy, Dr. Brady and Dr. Cull?

DR. BRADY: Of course. The plan is to make China rich and strong. Officially, that's the goal, rich and strong.

COMMISSIONER MULLOY: Do you see that the United States has a longer-term economic strategy just in passing, thinking about it?

DR. BRADY: That the U.S. has a longer plan than China? Well, China has got such a--

COMMISSIONER MULLOY: If someone said to you does the United States have an economic strategy, what would you say?

DR. BRADY: Maintaining the standard of living of the people in the United States.

COMMISSIONER MULLOY: What about you, Dr. Polumbaum?

DR. POLUMBAUM: Again, I'm not an economist, but nothing comes to mind.

COMMISSIONER MULLOY: What about you, Dr. Cull?

DR. CULL: This is a great question. In a former life I was a Professor of American Studies, and I've also taught Chinese history. One of the things that really comes home is the Chinese perspective is so long-term and they're planning 100 years or they claim to be planning 100 years, 200 years out, and whereas, in the United States, it's so frustrating to get people to think outside of the electoral cycle, and in corporations, so often they're just talking about the quarter and what are we going to do to hit our numbers this quarter?

That isn't something that you see in quite the same way when you're talking to people involved in business in East Asia, in general, and when you're talking to people who have a sense of China and Chinese politics. They're talking--they are now stepping back and

saying the point of a lot of this Chinese engagement with world opinion is to say China is back.

COMMISSIONER MULLOY: Yes, for purposes of this further discussion, they have one and we don't. At least that's kind of the understanding that we've got now. Dr. Ross Terrill is going to be on one of the later panels. He's a professor up at the Fairbank School at Harvard.

He talks about there's some money being given to U.S. think tanks, and sometimes by people who have made money in China, and he says that sometimes the price of getting that money is an ideological content into the think tank's thinking.

These Confucian Institutes, I don't know a lot about them, but the Chinese government is funding these, and they have a long-term vision as we've all established, and they're putting money into these. What do you think they think they're going to get for putting money into these Confucian Institutes?

Is there some kind of government strategy involved in putting money into these Confucian Institutes? Dr. Brady?

DR. BRADY: This is one of my research areas, and Dr. Polumbaum mentioned a minute ago that the government's idea and then what happens on the ground, in the universities, what they're thinking is going on is different, and I would concur with that.

The Confucius Institutes are formally part of China's foreign affairs system, and we can trace the trail back there if anyone had any doubts about it, but the partners of the Confucius Institutes, in some ways they don't want to acknowledge that reality.

COMMISSIONER MULLOY: Our partners here, you mean? Or?

DR. BRADY: Well, all around the world in the various countries.

And they do have the freedom to pretty much make it their own as long as they don't invite Wei Jingsheng to give a talk or anyone from Falungong or any of the known enemies of China, in their words in the government's eyes.

But as long as you're just teaching Chinese language, that's okay.

But some Confucius Institutes are involved in academic study and will have visiting speakers and so on. So obviously that's an inhibiting factor, and that's why some universities in New Zealand have made a point of saying that we don't want a Confucius Institute because we don't want to have any kind of constraints, but that's kind of an idealized world actually because then the businesses have a say. They've got a particular view of China they want too.

So I don't think there is any purist world where there isn't somebody's point of view influencing academic research and money coming without any strings attached. That's just the way the world is.

DR. CULL: What I wanted to add to that is, to confirm what my colleagues have said, to say that it seems that it's quite difficult to learn Chinese at a Confucius Institute, that they're not necessarily particularly efficient, but where they do seem to be effective is providing a focal point for the Chinese Diaspora, and as a way of energizing that Diaspora community, they seem to be being very effective.

In an odd way, the Confucius Institute is like some sort of lunch date where both parties are kind of hoping that the other person is going to pick up the tab at the end of the meal, and they're ordering more and more stuff, and saying how much they're enjoying it, and waiting to see where the check is going to come. I think that a lot of the universities that have agreed to have a Confucius Institute just assume that the three-year contract will keep rolling and that the Chinese government will be paying for this thing to happen on their campus.

Because one of the things that happened in the UK, for example, is that we've started closing Chinese language programs within universities because the argument is universities can't afford such a relatively small kind of enterprise, whereas, the Chinese, there's now four Confucius Institutes in London alone, one at the LSE, one at the School of Oriental African Studies, which is less than half a mile away from the LSE.

The hope is the Chinese government will pay what British academia can't, and it's the same in other places around the world, but my suspicion is the Chinese are also hoping that the Western governments and Western educational institutions will pay for Chinese cultural propaganda.

And so we have yet to see what happens to Confucius Institutes when the first round of major contracts expire. And the person, the little guy with the check comes and puts it in the middle of the table, who's going to reach when we come to the second round of contracts?

COMMISSIONER MULLOY: Thank you.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Cleveland.

COMMISSIONER CLEVELAND: You all have talked about the target audience being the Diaspora Chinese community and the domestic community. I'm interested in whether or not there is a regional flavor to propaganda, whether or not there are longer-term target audiences in Africa, Latin America, and if there is that long-term Chinese interest in propaganda on a regional basis, what are its characteristics? How would you describe their approaches on a geographical regional basis outside the two constituencies that you talked about they're trying to influence?

DR. CULL: Well, I think it's really important to look at what's happening both in Africa and in Latin America in terms of the way in which China is insinuating itself into the communications infrastructure.

If you look at Hugo Chavez' Channel TeleSUR, you find that there's Chinese advisors, there's Chinese material getting on there, and an awful lot of Chinese penetration into the media structures in Latin America.

In Africa, it's even more obvious because the Chinese are buying up the FM contracts so that, whereas, VOA has been coming to Africa over the shortwave, now Africa is turning to the long wave, and it's the Chinese who are getting the contracts.

Now, because China buying contacts for FM rebroadcast in Africa, it means that the United States is having to pay more and is getting shut out, and the Broadcasting Board of Governors I know is very concerned about this and needs to focus on getting the right sort of contracts, the right sort of rebroadcasting for the United States.

So this is a very practical way, in answer to Commissioner Brookes' point, where you can see that America is getting shut out. American news cannot be heard if it's Chinese news that's on that radio station, the crowding into America's, what has hitherto been Western media space.

DR. POLUMBAUM: The only thing I'd add is that it's my sense that while there is a very concerted effort to make inroads into certain regions and countries and take advantage of opportunities, that there is not a really refined effort in terms of adjusting content to different regional audiences.

COMMISSIONER CLEVELAND: You agree that the means are there, but the tailoring of the message has not been developed?

DR. POLUMBAUM: Right. There is, of course, there are some distinctions. For instance, Xinhua for a long time has had its French and Spanish and Arabic and Russian, and there are some expertise about those different audiences, but it's really not that different what's generated.

DR. BRADY: And I would concur with that, and it's part of the attitude in many ways within the Party system and the propaganda that's promoted towards the Chinese people about the foreign other as if it was all one thing, and so, I've done a little bit of research on China in the South Pacific and I have yet to come across a China South Pacific politics specialist. There may well be one nowadays, but I've been working a long time trying to find one, let alone a New Zealand politics specialist. There's a few Australian politics specialists now.

So China's main interest in foreign affairs is frequently really all about the U.S. and the Western world in general. But it is certainly

engaging very much with the developed world but not necessarily tailoring a particular message to them. It's still the same kind of bland content if you're looking at TV programs and CCTV-9. It's just available in Russian or whatever the language, Spanish or French instead of English.

But a more effective way of making the content local, as Professor Cull mentioned, of becoming involved in the local media process, and that's part of what's called "borrowing a boat to go out and onto the sea," is getting foreign journalists to promote China as much as possible because it is well understood that that's much more effective than getting a Chinese journalist from Xinhua to promote the Party message.

DR. POLUMBAUM: Actually a new development with the very latest recruitment calls from Xinhua News Agency involves trying to recruit native English-speakers or native speakers of other languages abroad as opposed to relying on Chinese correspondents, and this is totally new, and who knows whether this recruitment will be successful, but the notion of having people reporting from different places around the world who actually know those cultures and are part of those cultures could lend a different cast to the content.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Bartholomew.

COMMISSIONER BARTHOLOMEW: Thank you.

First, I wanted to thank our witnesses.

This is a very interesting topic, and I am trying to pull together some of the different strands because some of what I heard you say, Dr. Cull, when you were talking about the framing, about impressing the Chinese domestic audience, carries a very different kind of connotation than some of what I hear further in this discussion which sounds a whole lot less benign to me when I hear things about, first, concern about how China is being reported in the West, and then when I hear about that it's more effective for foreign reporters to be carrying the Party's message than it is for Chinese reporters to be carrying the Party's message.

And finally, Dr. Cull, what you were mentioning about Chinese media presence, and in some places control in Latin America and Africa, in particular, and given China's interest in wanting to take its rightful place on the global stage, I wondered if you could sort of play out for me just a recent example of how this could sort of unfold?

I'm thinking in the context of the global financial crisis, you're talking to the Chinese saying that pointing to Western admiration for socialism with Chinese characteristics. I'm not exactly sure where they're getting that from unless they're getting it because they are out there convincing other people that socialism with Chinese

characteristics is an effective way to do it. So we know that they are providing assistance in some places, financial assistance. How does that all fit together?

DR. CULL: Particularly, one of the things that was a source of positive reporting was Western reporting of the earthquake. The idea that the West admired China's response to the earthquake was very, very widespread and appeared in a lot of media reviews of the year and looking back over 2008. They obviously didn't repeat Western concern about people taking bribes to build schools with insufficient retrofitting.

COMMISSIONER BARTHOLOMEW: Right.

DR. CULL: We're talking about very selective readings of Western reporting, but what's important, I think that in a way the deep Chinese concern with what the West is saying about them reveals a vulnerability.

COMMISSIONER BARTHOLOMEW: Certainly that's one interpretation. I mean another interpretation would be that in order for China to take what it perceives as its rightful stage on the world, it needs to change the way that people in the West are thinking about it, which to me gets to the basis of all of the propaganda.

So the example that I'm thinking of right now that I think we're going to see unfolding is this whole issue of currency frankly, not currency valuation, Commissioner Mulloy, but the issue of the comments that have come out by some senior Chinese leaders about whether the dollar is or should be--

DR. CULL: The universal currency, yes.

COMMISSIONER BARTHOLOMEW: --the global currency. I wonder how if you see the lending that the Chinese government is doing to some countries in Latin America, if you see an increased presence of Chinese media messages in those countries, how this is going to unfold? Are we seeing potentially the beginning of a campaign where the Chinese government is interested in displacing the dollar as currency, and that there's different levels of propaganda that could be going on during the course of the economic crisis?

DR. CULL: That hadn't occurred to me.

DR. POLUMBAUM: I think that those statements were kind of a trial balloon. They weren't meant as any sort of programmatic intent. They also were a way of conveying a Chinese viewpoint that was different, part of this whole emphasis on expanding external propaganda.

Other than those who have delusions that you can shape and manipulate audiences so easily is to simply have a voice, to simply say China has this perspective, China has these ideas, and the fact that Chinese high level leaders, the head of the People's Bank, high

government officials, have had opinion pieces in the Financial Times and The Wall Street Journal, I mean this is new and this is a statement, "we have things to say, we're going to say them." It doesn't necessarily mean that there's a design there. It's something to think about.

Actually, there was a lot of backtracking on that statement and assurances that, no, China was not planning to propose a new basis for currency and so forth.

COMMISSIONER BARTHOLOMEW: Dr. Brady.

DR. BRADY: Just to follow up on Professor Cull's talk about the positive accounts of the Western media coverage of China's handling of the earthquake, that is a long-standing practice. I mean a typical example was after 1989, there were books published on how foreign leaders said China did the right thing on cracking down on the protest movement in China, and they had statements from Kissinger, if I recall rightly.

COMMISSIONER BARTHOLOMEW: Right.

DR. BRADY: So they do that. It's a very selective coverage of events often. But all the negative coverage that China got about how many people died because of buildings that were not built according to China's own earthquake standards.

The Chinese translation of Western media reporting on China can be surprisingly critical. I was shocked a couple of weeks ago when the Chinese media translated an interview that I did with Guardian Weekly on how China is copying from the Blair government spin doctoring approach to handle the media; and was in Cankao Xiaoxi, which is like a top classified newspaper for the elite, and I had people e-mailing me in China saying tell us more.

COMMISSIONER BARTHOLOMEW: Tell us more of how to do it?

DR. BRADY: No, it's an example of the critical voices in China that there are within the media and within mass communication departments and journalism departments who don't have the freedom that I have as a foreign academic to do this kind of research, and they know bits of the story, and it's been the advantage for me as an academic, foreign academic. I can go in and talk to lots of people and stick it all together; they can only put out little bits and pieces.

Their resistance to the management, as the government calls it, has to be in pockets, and so, yes, there's diversity. There is a lot of diversity in what China is getting. And so part of this investment in opening the Xinhua bureaus is to help China be more informed so that they don't just believe their own propaganda, like Gorbachev famously read Pravda every day, and it told him everything was fine.

So I do think it's in some ways another element we have to

understand is that China is making a good choice here to understand better the way the world perceives it.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Shea.

COMMISSIONER SHEA: This is a really a follow-up question to Chairman Bartholomew's question and Commissioner Brookes' question.

We've heard a number of reasons why China has decided to make substantial increases in investment in its foreign propaganda efforts. We've heard simple empire building by some Chinese institutions; domestic consumption, it's really more about domestic consumption; we've heard about foreign audiences having a huge appetite for news about China, and there might be a sense that we're going to provide that, fulfill that appetite; also fighting back against what is perceived as distortion by foreign journalism.

I was just wondering, do the Chinese cite specific examples of success stories, specific examples of success stories of how foreign propaganda efforts have helped support specific policy goals in certain countries, and I would be curious, are there case studies that they cite as particularly illustrative of how you can be effective in foreign propaganda?

DR. BRADY: The examples that were given to me in research that I did in China was all about how China patched things up with the U.S. after 1989, and that was through its relationships with senior figures like Kissinger, and so foreign propaganda, as I see it, it's not just about the newspapers and the TV stations and the radio stations.

It's also about foreign propaganda in the Chinese Communist tradition which has, incorporated all forms of mass communication including the conversation. Oral propaganda has always been an important task of a propaganda cadre.

So being able to win over and persuade a "foreign friend," as the Chinese call those who they get to agree with them on some, but not necessarily all points. You don't have to follow the whole package these days, but if you have something that you can agree with in China, and you're a prominent person, then you'll be a "friend of China." So this was the example that's been repeated to me a number of times in China and how this kind of foreign propaganda activity really worked for China and helped rebuild their relationship with the United States.

DR. CULL: But this is also what the United States has lost since its public diplomacy capacity has been so diminished since the end of USIA. USIA had people who were going out doing this person: face-to-face conversations with influential people, and that has been put on to the back foot in recent years. That should be of concern to every

American.

DR. POLUMBAUM: I think that your question is very interesting, and I couldn't think of specific things that have been presented to me as success stories in foreign propaganda, but I think definitions of what success might be really vary, and the both domestic and foreign coverage of the Sichuan earthquake presents a very interesting case study because for one thing it reinforces interest in favor of greater openness because it was in large part that greater openness that brought sympathy and support and relief and so forth.

But it also illustrates how much some of the best foreign reporting hinges on the best domestic Chinese reporting. Because all those stories about school collapses and corruption, that all was generated from the Chinese press first, and the days when China watchers sit in Hong Kong and read tea leaves are long over.

International correspondents read the Chinese press and get most of their most important leads from the domestic press.

DR. BRADY: I'd just like to add to that that that's really important because that's part of China framing the debates. That's how they help to frame the debates so that news is no longer seen as propaganda.

COMMISSIONER SHEA: May I ask another question?

HEARING COCHAIR REINSCH: Sure if it's short.

COMMISSIONER SHEA: Short, yes.

Could you just give us a little better flavor of what the state, the provincial propaganda offices are all about? Are they just sort of PR offices for economic development? What do they do and how do they coordinate with the national office?

DR. BRADY: They're a junior version of the central level organization so they gate keep if there's a problem in their local area and try to stop any bad news coming out, and there was a practice of the local journalists couldn't talk about a problem, but somebody from another province could come and report on it, and now there's been a special bill passed that that's now illegal.

But any local government wants to make sure that they don't get in trouble with the central government so they're always trying to keep out the bad news stories and promote positive stories about their province, and from a foreign propaganda point of view as a location for foreign investment and foreign tourism and contact and other forms of contact with foreign countries.

So they have a wide range of activities. They might be deputized to take over hosting some important personage who's been sent to their province, and as I said, it's just a junior version of the central activities.

HEARING COCHAIR REINSCH: Thank you.

COMMISSIONER SHEA: Thank you.

HEARING COCHAIR REINSCH: Commissioner Wessel.

COMMISSIONER WESSEL: Thank you.

Let me ask a question about the limits of what can be done, and we've seen here over the years U.S. companies wary of criticizing China for fear of retribution. We see U.S. news organizations, I think it was referred to earlier, are increasingly getting press because of the Internet, et cetera, so as a business model, they are having many problems.

We have heard from academics in the past that visa opportunities may be limited depending on their criticism of the Chinese, and before I think it was Dr. Cull who indicated that there's a ceiling or--I apologize--I don't remember which witness--that foreign journalists are getting much of their critical information from Chinese journalists or what appears, meaning that Chinese propaganda efforts, what they are willing to, the ceiling they're putting on reporting may be the ceiling on what U.S. journalists may be able to get for fear of retribution.

Has there been any kind of mutation of journalistic--I don't want to say integrity--but standards as it relates to reporting on China because of the way China treats all of this?

DR. CULL: I do have a comment that relates to that. And do you remember when Chris Patten, the last Governor of Hong Kong, was trying to publish his memoir, I think HarperCollins dropped the deal because it was too critical of the Chinese and it was part of their business. They didn't want to lose business opportunities in China.

COMMISSIONER WESSEL: Sky News and all the other.

DR. CULL: Right. But my response to this is to say, well, of course, these are business. We have got to wake up and see this business interest in the news, and American news has a commercial context. I think that there's a need for more news and more news from various sources.

This is the virtue of a state sponsorship of international news. It's why it helps to have a Voice of America out there that is talking to the world without having to worry about what Rupert Murdoch thinks, and it's the advantage of having a BBC World Service there talking to the world without having to worry about what Rupert Murdoch thinks.

Now, those journalists doubtless have their own concerns, but they're different concerns, and if we have multiple voices out there, each with slightly different concerns, slightly different cultures, then the audience isn't stupid, and they're able to piece together reality. But what worries me is a restriction on voices, and of other voices coming in to fill the gaps in that space, and when we look at the--I don't think a lot of people are going to sit and read Global Times if it

comes out in English.

I don't think you're going to see people on the Metro in Washington sitting reading the Global Times instead of the Washington Times. What I do think is that these stories from a Chinese perspective, from Global Times, from Xinhua, will be on the Internet and will be picked up by automatic news aggregation sites and will be dropped into people's home pages.

When you open up, your Google News will be sending you your news from a Chinese source because that's the news on this subject, and the volume of it will mean, just the sheer volume of the stuff will mean that it will be disproportionately cropping up more and more and playing more of a role in ordinary people's lives.

So I think this is significant and will be more a part because of the way in which we're now networked and stories are being passed around. Just the volume of material coming on to the network will make a difference.

Xinhua is increasing its number of bureaus. What are the Western news organizations doing right now? It is getting harder and harder to find good international news in this country. This is a big worry.

COMMISSIONER WESSEL: I agree with that--but as it relates to, let's say, the New York Times or other larger newspapers here that have bureaus there, are they being limited by that ceiling issue of their ability to access as well as the standards issue of concern about retribution in any way?

DR. CULL: I would see that as a research question, but Judy--

DR. POLUMBAUM: I don't think--certainly the international correspondents from this country for reputable news organizations do not compromise their standards. I think one change that has occurred mindful of consequences for Chinese citizens who may overstep bounds is that Western journalists are much more cautious about dealing with sources and putting sources in danger, which is a good thing.

But, I have the highest regard for most of the U.S. correspondents in China, and I think that your question illustrates the importance of maintaining a vibrant independent news media of great integrity and, of course, our newspapers, which is the sort of basis core of it all, are in crisis now. But it does highlight this problem.

COMMISSIONER WESSEL: Thank you.

HEARING COCHAIR REINSCH: Commissioner Fiedler.

COMMISSIONER FIEDLER: Let me ask another technical or factual case study type question. You've talked about the Sichuan earthquake. Does anybody know anything about the Chinese external response--this is the sort of nexus between domestic and external--

when the Chinese government cracked down on the mothers and fathers of the children who died?

It was fairly evident in the international press. I wasn't following it carefully enough to see what the official activity was coincident with that crackdown. Was there any upsurge in external propaganda? Did they just let it go and take it in the head?

DR. BRADY: The response was no coverage, and that's how they handle those kind of issues. And same with the milk powder crisis. There have been people protesting and trying to speak to foreign journalists because they can't get their voice out in the Chinese media, and some have been detained. That's not covered in the Chinese press.

So these kind of sensitive issues, they will be limited coverage--it's not like the old days where there would be absolutely no coverage whatsoever; it wouldn't even be mentioned. China knows that Chinese citizens can go online and get access to information alternative to the official accounts.

So they do, for that reason, there will be an official account of all crises that become publicly known, but the Party wants to dampen down the fires so after the coverage of the earthquake--the Party regards the coverage of the earthquake as a great success overall because this was where they had been preparing for awhile this concept, as I said, as the media as a tool and not the tongue and throat.

And so the media, according to the regulations, only Xinhua should have been covering the Sichuan earthquake because it's a major crisis, and they should give out the official report, but actually all these journalists from all over the place trekked into the region, and the central propaganda authority's response was, okay, because the reports were loyal reporting and very much focused on people, and that sells in China just like it sells in your country and mine, very emotional stories about people.

So the Party came out of it looking pretty good. And where there were problems, they dampened down the news and that just didn't get covered, and the editors responded to that requirement, do not report on--no more reporting on the shoddy buildings and don't collect the statistics of how many people died in these kind of circumstances.

COMMISSIONER FIEDLER: I understand that was the domestic response.

DR. BRADY: That's right.

COMMISSIONER FIEDLER: Are you saying that the external response--

DR. BRADY: The external response is Xinhua doesn't report on it.

COMMISSIONER FIEDLER: Just to ignore it, let it go. So it wasn't an affirmative. They took no action. So it was just a default

position, not a particular--

DR. BRADY: Another example of this is the recent clash between U.S. boats and Chinese boats, and let's not go into detail about what kind of boats they were, but there was no coverage in the Chinese media on this for days, but then the Western coverage became such a "kerfuffle" that finally Xinhua released a statement on it, and that's a classic example of the role of the State Council Information Office. If an issue related to China becomes a major international event, something which normally they would never have talked about in domestic propaganda, then there will be a statement on this because they understand they can't get away with saying nothing.

COMMISSIONER FIEDLER: Thank you.

HEARING COCHAIR REINSCH: Commissioner Mulloy.

COMMISSIONER MULLOY: Again, I want to thank the panel for coming to the hearing. It's been very helpful to us.

Dr. Brady, on page nine of your prepared testimony, and this comes off, we've talked about BBC and Voice of America, and I'm trying to, in my own head, make a distinction if there is one. Is there a reason why we should be concerned about these, the Chinese government, government controlled media?

You say there are concrete plans in the next two years to establish this Asia-based television station in Singapore or Thailand. And then you further talk about Phoenix Television, which is supposedly privately owned, but what you say is that Phoenix Television, its main investor is the state-owned enterprise China Mobile. So China Mobile is an investor in this privately owned--who owns Phoenix? Is that Mr. Murdoch who owns--

DR. BRADY: Actually China Mobile is 20 percent shareholder. So they're the next major shareholder. That's a slight typo there. But the ownership of Phoenix or the Phoenix model has been the subject of a lot of debate in mass communication circles in China and people interested in the Chinese media outside because the Chinese partner--the founder of Phoenix is a very interesting individual who has very, very close connections to the Chinese propaganda system himself, and then Phoenix employs ex-CCTV personnel.

So these people--who owns it? It's just like the Chinese newspapers today. They are nominally state owned, but in fact effectively privately owned these days, most Chinese papers apart from the Party papers because there's been a commercialization of the Chinese media.

The Party needs to maintain this nominal control so officially they're organs of the state, but, in fact, they're not going to subsidize papers anymore. They have to make money.

So the Phoenix model is related to that commercialization of the

so-called official Chinese media in that you have private business interests, but the personnel and the management are still very much locked into the propaganda traditions within China and very well aware of the norms and expectations, and they are more at risk than CCTV are because CCTV are like family so they can get away with being cheeky to Mum and Dad, but Phoenix TV can't because of their unusual status; they could be just told to go away.

So Phoenix could be very interesting as an international television, all the more loyal to Beijing.

COMMISSIONER MULLOY: This new international television station, English language, that they're talking about maybe in Singapore, is that going to be privately owned and what is the worry that we have? Why is that different from Voice of America, BBC or whatever?

DR. CULL: Could I answer that, Commissioner? The BBC and Voice of America both have charters that require balance, and they understand that if you don't give the bad news, you don't have any credibility, and if you're not honest and consistently, then you don't have credibility, and there are people within CCTV who understand this, and there are people within the Chinese media establishment who understand this and are pushing to be able to say more and to talk about China's problems.

And we can see, if you sample CCTV-9, you can see that at some points it's been getting better, and they've had, they've been able to get more of those sorts of stories like stories about the environment or stories about China's energy problems or internal displacement of people, the exodus from the countryside to the cities, and these stories have been on CCTV-9, and then they get pushed back in favor of just the more formulaic success story.

So I think that at the moment, this new Chinese channel will be very different from the BBC and from Voice of America because it won't be allowed to have true objectivity, as Chinese journalists also understand it, but were they to develop that kind of objectivity, then it would be a very interesting thing and, I think, a very welcome thing. The more voices we have out there, the better.

But state sponsorship does not mean state domination or state editorial control everywhere in the world, but in China, maybe it does. There is certainly more pressure applied to people to conform and operate under conditions of self-censorship of the message.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Bartholomew. Final question.

COMMISSIONER BARTHOLOMEW: Thanks. And thank you again to our witnesses for a very interesting discussion, very interesting testimony, and we appreciate your traveling here.

Dr. Polumbaum, you mentioned that one of the things that you see in Xinhua and China Daily is a desire on the part of more senior people to professionalize, to get some training or to professionalize the younger people that they have, and yet professionalism in journalism requires--is supposed to require objectivity and independence. And I wonder how much space do they actually have to promote that if freedom of expression and freedom of the press potentially contain some of the seeds of the destruction of one party control?

DR. POLUMBAUM: Well, I think that's the quandary, and I think there are sort of cross-currents of those who feel that the future lies in openness, transparency and professionalism and the sort of prevailing system tends to favor those who promote management and control of the press.

But I guess my simplest answer would be to refer you to my book, *China Ink*, but in the forward to that book, Aryeh Neier, who is the president of the Open Society Institute, identifies professionalism and professionalizing trends as the most important trend today in Chinese journalism and in other fields like medicine and law and writes that the professionalism of Chinese journalists is gradually expanding the space in which they are able to operate and expanding freedom in China.

I would say that the sort of journalists we would consider most professional in China, and they're not a majority, but they are a significant core, and I think a very important core, are those who resist orthodoxy in really savvy ways, using unassailable tools of assiduous fact-finding, solid verification, moderation in language, and such journalists furthermore cultivate networks of protection that buffer the consequences of transgression.

Editors protect reporters in their purview. Reporters look for editors who will go to bat for them. Reporters who make mistakes get shifted to the library as opposed to the labor camp, things like that. I think there is support for these trends at all levels, and in the very process of expanding external propaganda and needing to train an expanding core of journalists who understand and can negotiate the rest of the world, these professionalizing tendencies can only intensify.

So, in an odd way, you could say that external propaganda efforts contain the seeds of their own destruction maybe, that they become a valuable contribution to international news coverage and conversation and dialogue and so forth.

I tend to take a positive view of the world. Maybe it's a matter of self-protection or something, but, I hope that that's the direction in which things could go.

COMMISSIONER BARTHOLOMEW: Thank you.

HEARING COCHAIR REINSCH: Let me pursue that for just a second. You're projecting a glide path which has a happy ending or relatively happy ending. Agree or not. How long do you think it's going to take them to get there? Is this a 50-year glide path or--

DR. POLUMBAUM: Yes.

HEARING COCHAIR REINSCH: Or a five-year glide path?

DR. POLUMBAUM: China has kind of compressed the history of the Industrial Revolution and everything else so I think it's a long-term process. I think it's really unrealistic to believe for, for instance, those at Xinhua who want to plan an expanded network of foreign correspondents and correspondents who are natives of countries abroad and so forth, and an expanded broadcasting content, which Xinhua is already doing.

They already have broadcast crews all over the world. They don't have a station. They don't have their own channel, but they are actually starting to grow their broadcast activities, their video activities, that I think it's unrealistic and even ludicrous to think that this is going to turn into a respected operation very soon.

But in the long run, I mean the long run is for increasing interchange among cultures, and I also really separate this external propaganda thing from intelligence and spying and all that. I think it's interesting that you're having, that you're dealing with these topics on the same day, but I think they really are very different spheres.

HEARING COCHAIR REINSCH: Do either of the other panelists want to comment on the glide path question? We don't need to comment on the espionage question right now.

DR. BRADY: I would just say that I think professionalism in Chinese journalism is not a new thing at all. What's to be noted though is that the Party really has strong legitimacy these days, and so the journalists that I speak to, whether or not they're the investigative type journalists or the people who work for CCTV-1 or CCTV-9 or China Radio International, they're very patriotic. They love their country, and that means the People's Republic of China and the China that you have today, and that doesn't mean they don't want to see change. They just don't want to see radical change.

As journalists, they're very well aware of international perceptions of China and they don't like the Western, many of the Western accounts of China. I think that if we see this new channel or China Global Times coming out in English, as an example of the typical Chinese journalism that's very popular these days, we're going to see--we're going to see more of China's perspective on events, perspective that may not be to the tastes of all of us, but it does have an audience.

HEARING COCHAIR REINSCH: Thank you. And let me thank the panel. I agree with Chairman Bartholomew. I think you've been extraordinarily useful and very helpful to us. It's an extraordinary jury of expertise. We appreciate your travels and your coming here. We appreciate your sharing your time and your wisdom with us. There may be follow-up, but in any event, thank you very much.

We'll now take just a few minutes' recess while we change the nameplates and invite the next panel up.

[Whereupon, a short recess was taken.]

PANEL II: CHINA'S EFFORTS TO EXERT INFLUENCE ON U.S. INSTITUTIONS AND PUBLIC OPINION

HEARING COCHAIR REINSCH: We'll reconvene for the second panel that I would like to introduce, and then we'll follow the same procedure as with the first panel. I'll ask the witnesses to deliver their summaries hopefully within seven minutes each. Your full statements will be put in the record. I'll ask you to go in the order in which I'm going to introduce you, and then we'll turn to questions for all of you.

Our second panel today consists, first, of Dr. Ross Terrill, who is a historian and researcher with Harvard University's Fairbank Center for Asian Studies, a historian who specializes in modern China. As a regular visitor to China from the 1970s, his articles have been published in the *Atlantic Monthly*, *Foreign Affairs*, the *New Republic*, *National Geographic* and other national magazines.

He has appeared on CBS News, the Today Show and Nightline as a commentator on Chinese politics. Dr. Terrill has also taught modern Chinese history and foreign policy at the University of Texas-Austin.

He is the author of the *New Chinese Empire*, which won the Los Angeles Times Book Prize in 2004. He is also the author of *Mao: A Biography*, and *Madame Mao: The White Boned Demon*, among others.

He is a recipient of the National Magazine Award and the George Polk Award.

Dr. Eric Anderson is a national security consultant. As a long-standing member of the U.S. intelligence community, he has written over 600 articles for the National Intelligence Council, the International Security Advisory Board, and the Department of Defense.

In addition, he is a leading scholar on the rise of sovereign wealth funds. His book, *Take the Money and Run: Sovereign Wealth Funds and the Demise of American Prosperity*, was published in March 2009.

His focus on events in Asia is reflected in a forthcoming text, *The Middle Kingdom Redux: China Looks Forward to 2020*.

Dr. Jacqueline Newmyer is President and CEO of the Long Term

Strategy Group, a Cambridge, Massachusetts-based defense consultancy. For the last seven years, she's worked with offices in the U.S. government on future security issues to include research into the strategy behind China's military modernization; Iranian military concepts of operation; Chinese information management efforts; Chinese downside scenarios; China's capacity for technological innovation; and China's approach to energy security. She has also briefed members of five foreign defense establishments.

She is currently a Senior Fellow at the Foreign Policy Research Institute, has also held postdoctoral fellowships at the Belfer Center for Science and International Affairs at Harvard University's Kennedy School of Government, as well as at the John M. Olin Institute for Strategic Studies in Harvard's Department of Government.

Welcome to all three of you. We'll begin with Dr. Terrill.

**STATEMENT OF DR. ROSS TERRILL, ASSOCIATE IN
RESEARCH, JOHN K. FAIRBANK CENTER FOR CHINESE
STUDIES, HARVARD UNIVERSITY, CAMBRIDGE,
MASSACHUSETTS**

DR. TERRILL: Thank you, Commissioner.

I'm delighted to be sharing in this dialogue with you all on an important subject, constantly changing.

China's goals in trying to influence U.S. academics, journalists, think tanks and others are twofold. They want to promote the rosy side of China: that China is a responsible member of the international community; a model U.N. member that's never aggressed and never will; a country whose foreign policy has the twin aims of peace and development.

And then to conceal the less rosy side: that China lacks the rule of law; that the professions in China are not autonomous; that China is a semi-empire; and so on.

There's nothing wrong with seeking to influence public opinion. On the international plane, it's the most desirable mode of bending other nations to your purposes; the least desirable being warfare.

The Chinese people have as much right to influence international public opinion as the American people do. The tough issue comes when an authoritarian government tries this abroad for its modes differ from democracy's modes.

The Chinese party-state is used to maximize control at home, and internationally and within this country, and that spills over into heavy-handed methods.

Chinese public opinion is largely hidden. On some questions, a Chinese will give a pollster or reporter a candid answer—"Is life in

South China better than life in North China?" On other questions—"Is Hu Jintao doing a good job?"-there won't be a candid answer.

On all large political issues in China, domestic and international, publicly expressed Chinese public opinion reflects the party-state's policies.

It takes a Chinese student or official who lives in this country some time to realize that our government doesn't control what the newspapers print, that a demonstration in favor of the Dalai Lama is just as permissible here as a demonstration against him, that textbooks here may vary enormously from publisher to publisher and state to state.

In China, all published book manuscripts are approved by the party-state. The editorship of all publications is chosen or fired by the party state.

There are key terms which reveal this asymmetry between our two countries. If an American says something critical of China, it's said, and it's been said of me in China, I've hurt the feelings of the Chinese people. What this really means is that the opinion expressed has hurt the interests of the Chinese government.

The phrase "interference in China's internal affairs" is very common. But interference in China's internal affairs is broad enough to cover U.S. law allowing Falungong practitioners to protest outside Chinese consulates and the Chinese embassy in the United States.

American visitors to China read China Daily, which has been discussed this morning. Few are aware that it's a government newspaper, but it's a key link between the Chinese domestic political system and the views of American public opinion. American visitors to China in almost all cases can't read anything else in China because other newspapers are in the Chinese language.

So if Beijing and the China Daily can spin the truth about Tibet or North Korea or whatever, opinion in the West may be influenced and U.S. policy on these issues cast into doubt. By total contrast, Chinese visitors to the United States, whether they read English or whether they only read the many Chinese language newspapers in this country, can get a variety of opinions about American leaders and about American policies.

Sometimes the U.S. side, U.S. institutions, misjudges this non-equivalence. Last spring, prior to the Olympic Games in Beijing, the Nieman Foundation at Harvard went far down the path toward having a workshop not for Chinese journalists but for Chinese public security officials on how to handle the journalists who were descending on Beijing for the Olympic Games.

At the last moment Nieman alumni raised a few questions about this workshop, and it didn't occur.

Self-censorship is a daily necessity for journalists in China. It also can occur in diluted form here because people do worry about their next visa. They do worry in research terms, if they'll get to a sensitive spot like say the Muslim area of Xinjiang. They can be tempted to take the Beijing point of view because of largesse available -- of which we've heard a bit already this morning -- for a project, largesse coming from the Chinese side.

Enormous numbers of Chinese students are on our campuses--an excellent phenomenon. No other authoritarian state has ever had nearly as many of its citizens residing in this country as China does today.

The problem here is that it's difficult for the Beijing government sometimes to distinguish cultural nationalism from the political imperatives of the party-state. As the Olympic torch made its way around several nations, Chinese officials in embassies and consulates mobilized patriotic Chinese residents in those cities to fend off demonstrators.

So interference in China's internal affairs is one thing; interference in the internal affairs of France or South Korea or the U.S. is evidently another thing.

It's true there is sometimes an exaggeration in this country about the danger of China's manipulation. There is a vague race fear of huge China in some quarters and that worries Beijing. The prior example of Japan and the memory of older Americans is also a background factor. And Chinese civilization has a seductive power that can lead both to overestimation of China and to fear of China.

The good news is that in recent years, there's been an improvement in how China attempts to influence public opinion in this country due to more enlightened Chinese policies, vigilance on the part of Congress, of the American press, and commissions like yours, partly due to the many American and other Western returning Chinese students who are working in the Chinese bureaucracy, making Chinese socio-cultural activities abroad more sophisticated than they used to be.

Almost every Chinese I know well who has spent time in the U.S. on a campus, at an embassy or wherever has been substantially affected by American values of freedom and democracy.

On the whole, I'm optimistic about the future direction of U.S.-China socio-cultural interactions. China's increased prosperity plus globalization have on balance been good for liberalization of the mind among Chinese at home and abroad.

But American strength and vigilance is as crucial tomorrow as it has been in the past. We should not assume that economic boom has led China to the doorstep of democracy. We should resist China's

picking of winners and losers among Americans who are dealing in various spheres with China. We should continue to be a beacon of freedom in our own conduct and in speaking up for freedom around the world.

Thank you, Commissioner.
[The statement follows:]

**PREPARED STATEMENT OF DR. ROSS TERRILL, ASSOCIATE
IN RESEARCH, JOHN K. FAIRBANK CENTER FOR CHINESE
STUDIES, HARVARD UNIVERSITY, CAMBRIDGE,
MASSACHUSETTS**

China's efforts to influence U.S. academics, journalists, think tank personnel and other shapers of public opinion are part of its overall aims in the world. First, to fully recover from a period of reverses to China from the Opium War to the mid-20th century. Second, to gain time for economic development to make China an influential great power to match its greatness as a civilization. The soft power thrust has two proximate goals. First, to promote the rosy side of China's self-understanding: a responsible member of the international community; with a foreign policy of peace and development; a punctilious UN member that has never aggressed and never will. Second, to conceal the less rosy side: Chinese society lacks the rule of law; China is a semi-empire; the professions in China are not autonomous; and so on.

There is nothing wrong with seeking to influence public opinion. On the international plane, it is the most desirable mode of bending foreigners to your nation's purposes, the least desirable being war. The Chinese people have as much right to influence world public opinion as the American people do. But modes of influence are crucial. I have often lectured around the world for the USIA and similar agencies, which openly seek to have U.S. positions understood in foreign countries. The tough issue comes when an authoritarian government essays this abroad, for its modes differ from a democracy's modes.

When Britain, Japan, or France seek to influence U.S. shapers of public opinion, or the U.S. does the same in those countries, the activity is transparent. It is true that money affects the weight of the efforts. But essentially it is a case of individuals making arguments to persuade other individuals in an atmosphere of free exchange of information. That is not true with China. The Chinese party-state is used to maximum control at home and this spills over into high-handed attempts at control abroad.

Currently, China's ideological chief, Li Changchun, is touring various countries with an updated message. "Communication capacity determines influence," he said before leaving Beijing. "In the modern age, whatever nation's communication techniques are most advanced, it is that nation whose culture and core values will spread far and wide, who will have the most power to influence the world." The target of these arrows, he said, is "the international public opinion structure." To those with experience of the PRC, these are
arresting
remarks.

Chinese "public opinion" is largely hidden. On some questions a Chinese citizen will give a pollster or reporter a candid answer ("Is life easier in south China or north China?"). On others she will not ("Is Hu Jintao doing a good job?"). On large political issues, domestic and international, publicly expressed Chinese public opinion reflects Chinese party-state policies. We saw this at the time of the accidental bombing of the Chinese Embassy in Belgrade in May 1999, and the air collision near Hainan Island in 2001. Anti-American ferocity was evoked, then it was hosed down.

Chinese people can react only to what they are told. They do not know what they do not know. They can

readily detect, however, when they must amend their opinions.

It takes a Chinese student or official living in the U.S. some time to realize that the U.S. government does not control what newspapers print, that a demonstration in favor of the Dalai Lama is just as permissible as a demonstration against him, that textbooks vary widely in their content from state to state and publisher to publisher. In China, the appointment of chief editor to all media is made by the government. All book manuscripts must be signed off on by the government before publication.

Key terms reveal the asymmetry. A wrong opinion expressed by an American about China is said by Beijing to "hurt the feelings of the Chinese people." This really means the opinion hurts the interests of the Chinese government. The phrase, "Interference in China's internal affairs" is broad enough to cover U.S. law's allowing Falungong practitioners to protest outside a Chinese consulate in an American city.

The lack of equivalence between a democracy's dealings with "the other" and an authoritarian party-state's dealings with "the other" is illustrated by the Beijing newspaper "China Daily." American visitors to Chinese cities read "China Daily;" little else exists in English. Few are aware that this is a government newspaper (much improved over recent years). Here is a key link between China's domestic political system and its influence on American public opinion. If Beijing through "China Daily" can spin the truth about Xinjiang, Tibet, or North Korea, opinion in the West may be influenced and U.S. policy on these issues cast into doubt. By contrast, Chinese visitors to the USA, if they read English - even if they only read the many Chinese-language newspapers published from New York to California - get a variety of views on American leaders and American policies. "China Daily's" role in influencing English-speaking visitors to China achieves what years of clumsy projects within the U.S. failed to achieve in the 1970s and 1980s.

Sometimes U.S. institutions contribute to confusion by misjudging the U.S.-China non-equivalence. Prior to the 2008 Olympic Games, the Nieman Foundation for Journalism at Harvard went far down the path to offering a workshop for public security officials from Beijing on how to handle the foreign press descending on Beijing for the Olympics. Not a workshop for Chinese journalists, but one for police on how to handle journalists. The workshop was cancelled at the last moment after Nieman alumnae raised questions. Sometimes American intellectuals are more trustful of a foreign government that puts on a good show than of our own government that operates within a cacophony of debate.

I was once invited to attend a session at the Kennedy School of Government at Harvard where a visiting official from Qinghua University in Beijing proposed the idea of a journalism-school exchange between the Kennedy School's center on that subject and Qinghua. Qinghua had no background in journalism and the Chinese visitor pitched the project on different grounds. The Chinese government leadership is thick with Qinghua graduates, he said, and the Kennedy School would be plugged into some very influential people. Qinghua sought a foot in the door at Harvard's center for journalism and public policy. It had the money for the project. The Kennedy School to its credit took a pass.

Self-censorship, which is a daily necessity for journalists in China, also occurs in diluted form among American editors, academics, and others dealing with China. Folk worry about their next visa, their access to a sensitive area like Xinjiang for research, or take a Beijing point of view because of largesse available for their project from the Chinese side. One of the largest U.S. magazines a few years ago experienced Beijing's veto power over their choice of writer for a China story. The project was underway with myself as writer and a photographer lined up. But Beijing refused me a visa to visit the relevant sites. The magazine had to decide whether to cancel the story or pick another (more mellow) writer. They picked a fresh writer; he got his China visa. The article was published and its twenty million readers had no clue of Beijing's role in the selection of its author.

Do these efforts by Beijing influence U.S.-China relations? Far less than they used to. But they can keep alive an unsettling volatility in the traditional American view of China. One minute, China comes across as a victim (the Opium War, a poor Third World country that should be given special consideration in WTO...), and the American side feels sympathy. The next minute, the excited message on the lips of the American public is, "We Wuzz Robbed" (because the trade imbalance soars, China blames the U.S. for AIDS, a dangerous effort is made to hide the SARS epidemic...).

Chinese students in huge numbers are on U.S. campuses, an excellent phenomenon. The Soviet Union possessed no such human bridge into our society; no authoritarian country has ever had so many of its citizens living in the USA as China does today. The problem here is that recurrently it proves difficult for Beijing to distinguish cultural nationalism from the political imperatives of the party-state. The Chinese character "jia" is at once a term for family and part of the term for "state."

As the Olympic torch made its way through several nations, Chinese officials in embassies and consulates mobilized patriotic Chinese residents in those cities to fend off demonstrators. "Interference in China's internal affairs" is one thing. Interference in the internal affairs of France or South Korea or the U.S. is evidently another thing. The blind spot is a result of an interconnection, understandable historically, between Chinese cultural nationalism and the political imperatives of the party-state.

For a time, PRC manipulations within the U.S. were blunt because KMT manipulations were also blunt. Extremes tended to feed upon each other. The excesses of the McCarthy era inadvertently created a generation of pro-PRC academics offended by Senator McCarthy. The high-handedness of the Chiang Kai-shek "China Lobby" in the 1950s and 1960s gave an appealing underdog status to the Chinese Communists and fed Beijing's victim image long after Normalization in 1979.

Today, the more vigorously the pro-Dalai Lama forces agitate in the U.S., the stronger Beijing responds by promoting its view of "One China" and its assertion that "Tibet since ancient times has been part of China." The more blatantly an "anti-China" or "race card" message flashes from the U.S., the more strongly is PRC nationalism unleashed.

The American side sometimes exaggerates the danger from China's manipulation. A vague "race fear" of huge China (its population far exceeds that of the U.S., Russia, and all Europe combined) does linger in some quarters and this worries Beijing. The prior example of Japan in the memory of older Americans is also a background factor. Finally, Chinese civilization has a seductive power that can lead both to over-estimation and fear of China.

A paradox is that as China's influence rises, there is less need for manipulation by Beijing, but as China's muscle-power grows, more money is available for subtler forms of manipulation. The corruption of power has been familiar in all Communist systems. The corruption of money is new with China, as this extraordinary country moves away from Marxism to some unknown future.

A symbiosis occurs between Americans who benefit from business or other success with China and American institutions. Money may appear from a businessman with excellent connections in China and it is hard for a think tank, needing funds for its research on China, to decline it. But the money may bring with it major Chinese ideological input into the program of the U.S. think tank. Not all Americans realize that U.S. corporations operating internationally are far less tied to U.S. policies than Chinese corporations operating internationally are tied to Chinese government policies. In the last year or two, Chinese companies have started making healthy donations to think tanks in Western societies.

The good news is that Beijing's efforts to influence U.S. shapers of public opinion are less heavy-handed than they used to be. In the 1970s, a delegation of American scholars going to China could be canceled by

the Chinese side if merely one member of the group had written an essay unacceptable to Beijing. One time, a trip by mayors of U.S. cities was cancelled because the American delegation included the Mayor of San Juan, and Beijing viewed Puerto Rico, not as a legitimate part of the U.S, but as an oppressed colony. Often the American press and Congress have been more principled in this matter than American academia. The New York Times, to its credit, never gave in to Beijing over which ads it would accept in the 1970s.

In recent years a secular improvement has occurred, helped by more enlightened Chinese policies, vigilance on the part of Congress, parts of the American press, and commissions like this one. Partly due to the many American and other Western Ph.Ds in the Chinese bureaucracy, China's sociocultural activities abroad are more sophisticated than they used to be. Almost every Chinese I know well who has spent time in the U.S., on a campus, at the Chinese Embassy, or wherever, has been substantially affected by American values of freedom and democracy.

That U.S. resistance to China's attempted manipulations is important is proved by the fact that Chinese methods are cruder towards smaller powers than toward the USA. Beijing has learned they need to be fairly prudent in the U.S., and it is to their credit that recently they have been. By contrast, when Hu Jintao visited Australia in 2003, the Chinese embassy in Canberra wrote to Australian newspapers, urging them to accept no ads from Tibetan groups; and the Chinese ambassador asked the Australian foreign minister to require two members of the Australian Senate, who had recently heckled President Bush during a speech in their chamber, to be put behind sound-proof glass for Hu Jintao's speech to the Senate. It was like the bad old days in the U.S. during the 1970s. A smaller country cannot say No as readily as the U.S. can and should.

On the whole I am optimistic about the future direction of U.S.-China sociocultural interactions. China's increased prosperity plus globalization have on balance been good for liberalization of the mind among Chinese at home and abroad. But American strength and vigilance is crucial, tomorrow as it has been in the past. We should not assume that economic boom has led China to the doorstep of democracy. We should resist China's picking of winners and losers among Americans dealing with cultural and intellectual exchanges with the PRC. We should continue to be a beacon of freedom in our own conduct and in speaking up for freedom around the world.

HEARING COCHAIR REINSCH: Thank you.
Dr. Anderson.

**STATEMENT OF DR. ERIC C. ANDERSON
SENIOR POLICY ANALYST; FELLOW, NEW IDEAS FUND
MCLEAN, VIRGINIA**

DR. ANDERSON: Thank you. I want to thank the Commission members for this opportunity.

I'd like to talk today about my views on Beijing's efforts to exercise influence over the U.S. financial institutions.

As you're aware, China currently maintains an approximately \$2 trillion foreign 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 directors of the China Investment Corporation, China's sovereign wealth fund.

At first blush, these large funds 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 I'll open with the most famous case: China's ability to exercise her financial nuclear option.

Let me say at the outset that there is no--repeat--no indication that Beijing is currently engaged in an effort to sell off a significant portion of her U.S. Treasury notes. While the Chinese leadership has recently expressed concerns about Beijing's U.S. Treasury holdings and wants assurances that those investments are safe, there is no reason to believe that China is preparing to wholesale move those funds elsewhere at least in the immediate future.

In fact, China is clearly seeking a fix to the current financial crisis in a manner that may serve to diminish Washington's dominant role on that front. In late March 2009, the Governor of the People's Bank of China released a paper calling for the establishment of what he said was a super-sovereign reserve currency, a currency that would essentially replace the U.S. dollar.

In his paper, the banker said that the new currency, reserve currency, should be controlled by the International Monetary Fund as a means of avoiding what he said were the inherent vulnerabilities and systematic risks in the existing international monetary system.

Despite the fact that China currently holds the world's largest foreign exchange reserve, this proposed new super-reserve currency is to be supra-national. As the banker put it, the global dominance of a few currencies--the dollar, the euro and the yen--leaves the financial system more volatile and more vulnerable.

His solution, as The Wall Street Journal observed, would increase the role and powers of the IMF, indicating, as The Wall Street Journal put it, that China and other international developing nations aren't hostile to the international financial systems; they just want to have more say in them.

As it turns out, The Wall Street Journal was right. During the last week of March, Beijing made it clear China 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. International financial analysts watching Beijing's apparent power play agreed the request seemed reasonable, but also warned that a greater role for China would result in greater scrutiny of banking practices in Europe and the United States.

So what does China want? This is a bid for a greater voice in governing the international financial system. It's indicative of China's broader efforts to level the playing field. Beijing is not seeking to dictate or dominate the conversation. She's 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 does really appear that China is seeking to realize a rebalancing of the entire international system such that she might be able to secure an ambiguous world order, one absent of U.S. hegemony or regional efforts contrary to China's interests.

Similar observations can be made about the investment strategies that we've seen at the China Investment Corporation. The first two-thirds of the sovereign wealth fund's investment was used to assist Chinese firms, primarily banks, in their efforts to compete internationally. 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 then we have the other 70 billion.

As it turns out, China's offshore spending via the sovereign wealth fund has been a painful adventure. In May 2007, China purchased 9.3 percent of Blackstone Group for a reported \$3 billion. Unfortunately, for the Chinese, what seemed like a good deal soon went astray. By early February of this year, Blackstone prices had dropped to the point where the Chinese investors were looking at an 83 percent loss on their investment.

The CIC's next major overseas purchase came on 19 December 2007 when the Chinese acquired a 9.9 percent share of Morgan Stanley for a reported five billion. By 1 March, the 9.9 percent share of Morgan Stanley had declined to a value of 4.91 billion. Of note, this loss didn't go unnoticed in Beijing.

As the Commission has heard before, when asked to explain the CIC's investment in Morgan Stanley, the head of that corporation went before the World Bank and said, "If we see a big rabbit, we'll shoot at it," but then he also said, "Some people say we may have been shot by Morgan Stanley."

China's dalliance with Western financial institutions continued in February 2008 when word of a potential CIC deal to place four billion dollars in a private equity fund operated by JC Flowers was leaked to the press. Little-known U.S. based JC Flowers is run by a former Goldman Sachs banker, 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.

In conclusion, I can find little evidence suggesting Beijing is engaged in a widespread 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 system as an honest broker who realizes she has much to lose by engendering suspicion and/or abetting havoc.

My extensive study of the Chinese Investment Corporation's investment strategies indicates Beijing is using her sovereign wealth fund to generate profit for Chinese taxpayers, not to undermine Wall Street or the U.S. Treasury.

In short, I can find no evidence suggesting China is using her foreign exchange reserve to coerce the West. Beijing realizes employment of the financial nuclear option would have a devastating impact on China's own economic future. What is the peril that Chinese affluence presents to America? The peril for the moment appears largely confined to short-term reinvigoration of jingoistic statements and proposals to revisit protectionist legislation aimed at preserving American national security from an amorphous threat.

Over the longer-term, however, the CIC peril may be profound. It's not that the Chinese will purchase U.S. sovereignty--quite the contrary. The long-term peril is that China and many other profit-oriented customers will go shopping for investments offering a greater return than that provided by our U.S. Treasury notes.
[The statement follows:]

**PREPARED STATEMENT OF DR. ERIC C. ANDERSON
SENIOR POLICY ANALYST; FELLOW, NEW IDEAS FUND
MCLEAN, VIRGINIA**

**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 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

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.

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."

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

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—

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,

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 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*

⁹ Song Guoyo, 12 July 2007, “Sovereign Wealth Funds Gaining Popularity,” *Shanghai Dongfang Zhabao*, Shanghai, China.

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

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 foreign competition. Given the apparently sad state of affairs resident on the balance

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 Zhabao*, 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.

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

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-

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 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

stock and State-owned Banks," *China Brief*, Volume 5, Issue 18, The Jamestown Foundation, Virginia.

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

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 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

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,” Bloomberg.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).

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.)

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 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

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.

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 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

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.

³⁶ _____, 30 November 2007, "China Wealth Fund Seeks to be a Stabilizing Presence in Global Markets," *Xinhua*, Beijing.

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 more 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 a lower tendency to follow this pattern.⁴² The China Investment Corporation is following

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.

⁴² Shai Bernstein, Josh Lerner, and Antoinette Schoar, 2009, “The Investment Strategies of Sovereign Wealth Funds,”

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

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.

COMMISSIONER BARTHOLOMEW: Thank you.
Dr. Newmyer.

**STATEMENT OF DR. JACQUELINE NEWMYER
PRESIDENT AND CEO, LONG TERM STRATEGY GROUP,
CAMBRIDGE, MASSACHUSETTS**

DR. NEWMYER: Ms. Chairman, members of the Commission, thank you for the invitation to speak today on this timely subject.

My remarks will be centered on how Chinese influence operations figure into a broader strategy for China as it rises. The subject of a broader strategy came up this morning, and my remarks will be structured around what the Chinese are actually saying and writing in their internal reports.

Dr. Brady this morning mentioned Cankao Xiaoxi, the Reference News, which is a branch of Xinhua, the official news agency, but it's charged with reporting to high level cadres, Chinese Communist Party elites, on analysis and data that they must have so it's got limited circulation and it's distributed at the highest levels.

I'm going to talk about what they're actually writing in reports that appear in this outlet, and then I'll move to where I think this might come from, what the logic behind it is, and I'll offer a preliminary assessment of how I think the Chinese are doing.

But just to give you a preview, my answer is clearly yes, the Chinese are trying to influence or shape American perceptions of and policies toward China, mainly up till now in the direction of trying to reassure us -- to allay concerns about China's economic rise, military build-up and increasing political and diplomatic influence.

So let me begin by referring to an official Chinese publication addressing the need for and character of Chinese strategic information capabilities directed abroad.

Again, this is not a policy document, but I think it's representative of a certain mind-set, and it's reaching and it's commissioned by Party officials at the highest levels.

In February 2009 Reference News publication, the subject of national public relations weapons was addressed, and this is how it was defined, quote:

"By national public relations, meaning dialogues between nations or between a country and relevant stakeholders against the backdrop of competition over power and interest."

The article explicitly addresses the need to, quote, "set the agenda for foreign media," under a subhead of the article called, quote, "Media Diplomacy: Breaking the Siege of Public Opinion in the West."

The author writes, quote:

"It is obvious that the West still has the upper hand while the East remains weak. Whenever there's an agenda dispute, international public opinion will form a force that involves the West's besieging the East."

Then the article goes on to say, quote:

"Influencing and setting the foreign media agenda fully embodies a rule of the game in modern society--that is, whoever can influence the media agenda can influence the public agenda. The foreign media are not a taxi on the road that can be flagged when one needs it and shoved away when one does not need it. In other words, these people, these foreign media, always have to be cultivated. We have to have relationships so we can depend on them when we need them to report in certain ways.

How? Quote: "Foreign media outlets should be given special treatment so that they will not be forced to unite and form a confrontational alliance."

In other words, divide them or keep foreign media from uniting against China, keep them divided. More on how this can be achieved.

Quote: "Provide them"--these foreign media outlets--"with specialized information." Grant them privileges to encourage positive coverage of China.

And then still under the heading of, "Breaking the Siege of Public Opinion in the West," there are general precepts such as, quote:

"When a negative event occurs, the authorities should not order the media to shut up. Public opinion is like a big container. The more information you inject, the less space there is for other people's views and ability to return fire."

In other words, flood the zone. Even when there are crises within China that the Western media may have access to, we should not clam up. We should report on it so that we can shape the direction of foreign reporting.

More specifically, under the heading of "Lobbying," the author writes, quote:

"We need to influence the influential. In every country, there are famous commentators and writers, and they are the media and public focus. With the support of these foreign eloquent speakers and writers, the national public relations drive can yield twice the results with half the effort. In addition, it is necessary to fully mobilize overseas elites and overseas Chinese who are familiar with China. Because they understand the cultural environment abroad, they can be good assistants to China's public relations."

So where does all this come from, this talk of "siege of public opinion in the West" and "national public relations strategy," "public

relations weapons"? I think it flows from a tradition, a strategic tradition that stresses the role of information and perceptions in political and geopolitical interactions -- that is, both domestic politics and foreign relations.

I'd go so far as to say that the Chinese tradition puts managing perceptions at the heart of strategy. This is evident from Sun Tzu's injunction to know the enemy and know thyself, which after all is about knowledge and information and perceptions, to the CCP's extensive domestic propaganda and information management efforts, which have been analyzed and explored by scholars like Anne-Marie Brady, David Shambaugh, Daniel Lynch, and Ashley Esarey, among others.

Perhaps most obviously for our purposes, it's evident in Deng Xiaoping's famous line that China should bide its time and hide its capabilities, which can only be understood as a call to shape the data that reaches foreigners, in this case, to conceal certain data, keep certain information from reaching foreigners.

And then we have the famous line about China's "peaceful rise", which was introduced by a Party school official, or somebody who is often described as a Party school official, and he was, Zheng Bijian, in 2002. He later changed the statement to "peaceful development" because even the term "rise" was seen as potentially counterproductive to the mission of reassuring foreigners as it might raise anxiety about China.

So instead of talking about peaceful rise, because it includes the word "rise," we now hear about peaceful development. But before this change took hold, Zheng kind of slipped up in 2004, when he went on Shanghai TV, and instead of talking the way he talks to foreigners about China's peaceful rise, this is what he said, quote--and this is in a recent China Quarterly article by Dan Lynch--quote:

"Working in this way has its advantages," --and working in this way means talking about, in this case, China's peaceful rise--"in obtaining greater understanding, sympathy and support, in winning discourse power on the question of China's development path, in winning discourse power in the international sphere. It is all extremely advantageous, and there's absolutely no downside."

So this is a pretty stunning shift from talking about peaceful rise as an earnest description of what China's present and future trajectory is to talking about it as an instrumental term that's designed to reassure.

Zheng is affiliated--he's often talked about being a Party school official, and that's often described as being a think tank, but he's also been a propaganda official since the 1960s in China, and he's part of that vast propaganda apparatus with its spider web that connects

different bureaucracies that Dr. Brady talked about this morning.

So the Party school and Chinese think tanks in general are not like AEI or Brookings. Actually, the Chinese sources talk about this. In another recent article called, quote, "It Is Difficult for Chinese Think Tanks to Learn from the American Model," the author says, quote:

"U.S. private think tanks are in a thriving state. This is unique in the world, a byproduct of the U.S. dual-party election system, fundamentally different from the domestic conditions of China."

"Therefore," and then the author goes on to say, "it's a pity we can't learn that much from American think tanks except for maybe some internal organization tips because their whole structure and their place in society is so different."

In a different piece called, quote, "China Must Have Strong Nongovernmental Diplomatic Power," again published in a limited circulation publication that's meant to analyze foreign perceptions of China and keep track of them for Chinese elites, the author identified the fundamental differences between the U.S. and China in think tank realms and considered China to be at a disadvantage, quote:

"The diversified nongovernmental forces have provided U.S. diplomacy with multiple abilities to set up various agendas. In the meantime, China can do nothing but rely on its government's single-track diplomacy. This has placed China in a passive position in which it is hard to cope with the situation as if it is shooting mosquitoes with a cannon."

The article goes on to say that to avoid embarrassments like the crackdown on free Tibet protestors in the run-up to the Olympics, China must unleash overseas Chinese nationalists to counter Western public expressions of sympathy for Tibet.

The general analysis is the U.S. strategically benefits from having people who aren't connected with the government saying things that are favorable to the U.S. and critical of China, and China needs to counter this by deploying overseas Chinese and people in foreign countries.

Well, what is this about, this talk of national public relations strategy and discourse power? With regard to the United States from the lines "biding time and hiding capabilities" and "peaceful rise," we can be sure that there is an effort to keep America friendly, reactive, and reassured about China, but there's also an emerging realism in the Chinese writings about the feasibility of this, the continuing feasibility of this, as China passes through different stages of modernization and development and starts to assume roles associated with great powers.

From the document that I quoted on the outset, there's a

description, quote:

"China's public relations drive is not a competition that involves waging a quick battle, but what Chairman Mao described as a 'long running- battle.' According to Chairman Mao, a long-running battle involves three stages: defense, confrontation, and counterattack. From the strategic level of national public relations, the defense stage comprises passive defense and active defense. We divide the confrontation period into two parts: confrontation resulting from both sides being well matched in strength and dialogue brought about by a balance of power. The counterattack stage involves attacking and countering."

There's a lot of discussion about whether China can continue to bide its time and continue in this phase of, quote, "unrestrained modesty" that marks the passive defense stage or whether it needs to proceed to the next stage.

In terms of China in the world more globally, as some of the speakers mentioned this morning, there appears to be a perception in China that there's a competition in the world in the realm of international public opinion, and various scholars in China have tried to study where China ranks in this global competition, and they have suggested that they're behind the U.S. because the U.S. has, quote, "international mobilization capacity" because we have more friends in the world, but that China can erode that advantage in three to five years if it properly, quote, "positions" itself. It's a PR term.

This is the advice from Dr. Yan Xuetong, who is the Dean of Tsinghua, but he's writing in another one of these internal circulated high level cadre publications, quote:

"We may think of repositioning China's international identity and expanding the homogeneity between China and other countries in identity. Economically, China may position itself as a burgeoning modern country between a developed and an underdeveloped country. Politically, China may position itself as democratizing between a democratic country and an autocracy. Culturally, China may position itself as a Confucian country between a religious and a nonreligious country."

In other words, to maximize its appeal and its ability to win friends abroad, if they can spin themselves in the right way, they can overtake the U.S. in terms of the number of friends they have.

Just to conclude, how effective is this? It's tough to measure the effects because it requires addressing a counterfactual: would we as the U.S. be doing what we're doing in the absence of whatever China is attempting to persuade us of? It's difficult to know, but I can refer you to an article, a recent article by Carsten Holz, who is a scholar in Hong Kong, who wrote a piece called "Have China Scholars All Been

Bought," which begins "Academics who study China, including this author, habitually please the Chinese Communist Party, sometimes consciously and often unconsciously."

Or take the words of a senior American scholar of China, Orville Schell, quote:

"I try to say, 'Okay, here's what I think, what I understand, what I think I see, have learned and read.' Then, I try and think through what the Chinese government's reaction will be. And then I try to be as truthful as I can in a way that is respectful and unprovocative but that is not pandering. China has a tremendously highly evolved capacity to create panderers, both among its own people and foreigners who become involved with them."

So where is all this going if China succeeds in reassuring the U.S. and cultivating international mobilization capacity? I think that's in some ways a subject for another hearing, but I don't think we're doing China any favors over the long term if we continue to act like we can be flattered and persuaded into reactivity and a posture of passivity.

Thanks.

Prepared Statement of Dr. Jacqueline Newmyer, President and CEO, Long Term Strategy Group, Cambridge, Massachusetts

Mr/s Chairman, Members of the Commission, Thank you for the invitation to speak today on this timely subject.

My testimony will address how Chinese foreign-directed information operations figure into the People's Republic of China's (PRC's) broader strategy as it rises, and my remarks will be structured around what the Chinese themselves are saying and writing about foreign-directed information operations in their internal reports. After reviewing a representative sample of the Chinese reports, I'll move to the logic behind their approach, or where it comes from, and finally, what China's aims are, before offering a preliminary assessment of their success. To give you a preview, my answer is, clearly, yes, the Chinese Communist Party (CCP) leadership is trying to influence or shape American perceptions of, and policies toward, China. Mainly, up to now, these efforts have been in the direction of reassurance, to allay US concerns about China's economic rise, military build-up, and increasing political and diplomatic influence.

Let me begin by referring to a Chinese report addressing the need for, and character of, foreign-directed strategic information capabilities. This article, a kind of roadmap for foreign-directed information campaigns, appeared in a February 2009 *Reference News* (*Cankao Xiaoxi*) outlet, and it was translated by the American Open Source Center, along with the other articles that I am going to cite today. *Reference News* publications come out of a special branch of the official Chinese news agency Xinhua that is charged with preparing information and analysis for senior cadres. In theory, the circulation of these *Reference News* reports is limited to high-ranking Party members. To be sure, I am not about to quote a policy document but rather an analytical piece. It seems to be representative of a certain cast of mind, however, as we will see. The article from February refers to "national public relations weapons," which it defines: "By national public relations, we mean dialogues between nations or between a country and relevant stake holders against the backdrop of competition over power and interest."

The need to “set the agenda for foreign media” is explicitly stressed. Under a subhead of the article called “Media Diplomacy: Breaking the Siege of Public Opinion in the West,” the author writes:

It is obvious that the West still has the upper hand while the East remains weak... Whenever there is an agenda dispute, international public opinion will form a force that involves the West’s besieging the East.

And the article proceeds to explain:

Influencing and setting the foreign media agenda fully embodies a rule of the game in modern society – that is, whoever can influence the media agenda can influence the public agenda... The foreign media are not a taxi on the road that can be flagged when one needs it and shoved away when one does not need it.

In other words, the foreign press has to be cultivated, so that when a crisis strikes, certain outlets can be counted upon to report favorably on China.

How can this be achieved? “Foreign media outlets should be given special treatment so that they will not be forced to unite and form a confrontational alliance.” In other words, divide them, or keep them divided. The article elaborates on this question, emphasizing the need to “provide them with specialized information...” That is, grant privileges to encourage positive coverage.

Under the same heading of “Breaking the Siege of Public Opinion in the West,” the article also offers general precepts such as,

When a negative event occurs, [the authorities] should not order the media to shut up. Public opinion is like a big container. The more information you inject... the less space there is for other people’s views and ability to return fire.

In other words, flood the zone.

More specifically, under the heading of “Lobbying,” the author writes:

We need to influence the influential. In every country, there are famous commentators and writers, and they are the media and public focus. With the support of these foreign ‘eloquent speakers’ and writers, the national public relations drive can yield twice the results with half the effort. In addition, it is necessary to fully mobilize overseas elites and [overseas] Chinese who are ‘familiar with China.’ ... [Because they] understand the cultural environment abroad, they can be good assistants in China’s public relations.

Where does all this come from? Whence this talk of a “siege of public opinion,” “national public relations weapons,” and the like? It flows from a tradition that stresses the role of information in political and geopolitical interactions – that is, in both domestic and foreign strategy. I’d go so far as to say that the Chinese tradition puts managing perceptions at the heart of strategy. This is evident from Sun Zi’s injunction to know the enemy and oneself to the CCP’s extensive domestic propaganda and information management efforts, which have been explored by scholars such as Anne-Marie Brady, David Shambaugh, Daniel Lynch and Ashley Esarey, among others. Perhaps most relevant for our purposes, the emphasis on information in China’s strategic culture is evident in Deng Xiaoping’s famous injunction that China should “bide its time and hide its capabilities,” which can only be understood as a call to shape the data that reaches foreigners, in this case to conceal certain data.

In this connection, consider the formulation designed to influence how foreigners understand China's increased power on the world stage, "peaceful rise." The line, promulgated by Zheng Bijian in 2002, was later changed to "peaceful development," lest the word "rise" provoke anxiety and undermine the intended effect of reassuring foreigners about China's trajectory. But before this change took hold, Zheng slipped up in a September 2004 Shanghai TV appearance, as quoted in a recent *China Quarterly* article by Daniel Lynch: "Working in this way [touting the "peaceful rise"] has its advantages – in obtaining greater understanding, sympathy and support, in winning discourse power on the question of China's development path, in winning discourse power in the international sphere... It is all extremely advantageous, and there is absolutely no downside." This is a pretty stunning shift from insisting that "peaceful rise" is an earnest description of China's present and future to describing the label as instrumental, a tool for "winning discourse power."

Now Zheng is affiliated with the Central Party School of the Chinese Communist Party, but he has been a senior member of the Party's propaganda apparatus, an extensive network of offices that exists behind the official bureaucracy, since the 1960s. Zheng is never identified this way in Chinese Western-language news outlets. Further, the Party School is often referred to as a Chinese think tank. Is this an institution just like our Brookings or AEI? No. In another recent article called "It Is Difficult for Chinese Think Tanks to Learn from the American Model," the author explicitly notes the differences: "US private think tanks are in ... a thriving state. This is unique in the entire world, ... a byproduct of ... the US dual-party election system... fundamentally different from the domestic conditions of China." Therefore, "one is afraid that what China think tanks can learn from US think tanks is more about micro-level management and operational models." In other words, because most Chinese think tanks are sponsored by the Party, while American think tanks are private, all Chinese think tanks can learn from their US counterparts is internal organizational details.

A different recent piece, "China Must Have Strong Nongovernmental Diplomatic Power," published in a Chinese *People's Daily* [*Renmin Ribao*] outlet that tracks foreign opinion on China for senior cadres, reviews the fundamental differences between the United States and China in the think tank realm, and assesses that China is at a disadvantage:

The diversified nongovernmental forces have provided US diplomacy with multiple abilities to set up various agendas. In the meantime, China can do nothing but rely on its government's single-track diplomacy. This has placed China in a passive position, in which it is hard to cope with the situation, as if it is shooting mosquitoes with a cannon.

The article goes on to say that to avoid embarrassments like the crackdown on free Tibet protestors in the run-up to the Olympics, China must unleash overseas Chinese to counter Western public expressions of sympathy for Tibet.

What is this talk of "discourse power in the international sphere" and "shooting mosquitoes" about? Well, with regard to the United States and the lines about "biding time, and hiding capabilities" and "peaceful rise," we can be sure that there is an effort to keep America friendly and complacent. But there is also increasing realism in the Chinese reports about the continuing feasibility of this approach as China passes through different stages of modernization and development and starts to assume roles associated with great powers.

From the "national public relations" document that I quoted at the outset, here is a description of a natural evolution for China's foreign-directed information campaigns:

China's public relations drive is not a...competition that involves waging a quick battle, but what Chairman Mao...described as a 'long-running battle.' According to Chairman Mao, a long-running

battle involved three stages: defense, confrontation, and counterattack. From the strategic level of national public relations, the defense stage comprises passive defense and active defense. We divide the confrontation period into two parts: confrontation resulting from both sides being well matched in strength, and [then] dialogue brought about by a balance of power. The counterattack stage involves attacking and conquering.

Within the PRC today, there seems to be significant discussion of whether China can continue to bide its time or whether China will be compelled to shift its foreign-directed information efforts. The roadmap article concludes, “While we should not demonstrate toughness characteristic of the confrontation stage and the counterattack stage, we cannot continue making the kind of unprincipled compromises or maintaining the unrestrained modesty that marks the passive defense stage.”

In addition to shifting the message directed at the United States, China may accelerate its wooing of other countries. Perhaps inspired by the idea of “soft power,” the Chinese seem to believe that a competition exists in the realm of “international public opinion.” A January 2008 analysis by the scholar Yan Xuetong, published in a journal of the Chinese Institute of Contemporary International Relations (CICIR), a “think tank” with ties to the Ministry of State Security, which oversees Chinese counterintelligence, argues that “if a country has relatively many strategically friendly countries, it is likely to win support from other countries.” According to Yan, the United States has an advantage in allies, or “international mobilization ability,” but this can be eroded in three to five years if China properly “positions” itself or manipulates impressions of China’s “identity”:

We may think of repositioning China’s international identity and expanding the homogeneity between China and other countries in identity. Economically, China may position itself as a burgeoning modern country, being between a developed and underdeveloped country. Politically, China may position itself as a democratizing country, ... between a democratic country and ... [an autocracy]. Culturally, China may position itself as a Confucian country, between a religious and a nonreligious country...

I have been talking about Chinese intentions up to now. To conclude, I would like to turn to an assessment of effects. But effects are difficult to measure, in part because any judgment requires addressing the counterfactual question, Would we have acted as we have in the absence of Chinese foreign-directed information campaigns? As a preliminary answer, let me adduce the article “Have China Scholars All Been Bought,” by the Hong Kong-based professor Carsten Holz. Holz begins, “Academics who study China, which includes the author, habitually please the Chinese Communist Party, sometimes consciously, and often unconsciously.” Consider, too, the words of one of the most senior American scholars of China, Orville Schell:

I try to say, ‘Okay, here is what I think, what I understand, what I think I see, have learned and read.’ Then, I try and think through what the Chinese government’s reaction will be... And then I try to be as truthful as I can in a way that is respectful and unprovocative but that is not pandering. China has a tremendously highly evolved capacity to create panderers both among its own people and foreigners who become involved with them.

Where is all of this going if China succeeds in reassuring the United States while increasing its “international mobilization ability”? That’s a subject for a different hearing, I think. Thank you again, and I look forward to your questions.

Panel II: Discussion, Questions and Answers

HEARING COCHAIR REINSCH: Thank you very much.

We'll begin with Commissioner Wessel.

COMMISSIONER WESSEL: Thank you all for being here, and a very interesting follow-on panel.

Dr. Anderson, I want to make sure that I don't misinterpret what you said and get comments also from the other panelists. You seem to indicate that China was not willing to use its vast reserves, that that would be shooting itself in the foot. But there are some who believe that the mere threat of going to baskets of currencies, that the going to special drawing rights, the enhanced power at the IMF, et cetera, signals a shift in the balance of economic power between major nations, China being one of them.

And that seems to have sent some shock waves through policy circles. We've seen a change, a dramatic change, I think, in the way that the U.S. is approaching the question of the valuation of China's currency. We are seeing a number of major U.S. entities--companies--continuing their efforts to engage in the China market and to diminish U.S. responses to certain trade actions by the Chinese, shall we say.

So how do we fit all this? Is China, in fact, using its reserves, its rising power, to change that balance? And also, Dr. Newmyer and others, what impact is that having on our institutions here, both our companies which are lobbying in some ways for the Chinese because of their interest there, the questions we had of the earlier panel about whether it's Hill & Knowlton or others, their access to our process and how they might affect it?

DR. ANDERSON: I'll try to give you the short answer to a very long question.

COMMISSIONER MULLOY: Short answer, yes. Thank you.

DR. ANDERSON: The Chinese have an interesting quandary, and they're not alone in this. Almost any major holder of large foreign currency reserve worked under the same assumption, that you invested in the safest place you could find, and you made sure that you were able to access that money quickly in the event you need it for a financial emergency.

That made us the favorite place to invest. It wasn't an effort to persuade Washington. It was an effort for central bankers to act prudently. What we're seeing the Chinese do is develop an option that is sufficient to provide the same level of security but not leave them as dependent on what they now perceive to be a very vulnerable American economy, and that proposal is very forthrightly being floated with this IMF special drawing rights issue.

If you've been watching over the last month, the Chinese and now the IMF, and I'm not surprised at the IMF delight with this, have suggested that they increase the reserve access within the IMF from 250 billion to a trillion dollars, essentially setting up over a longer

term the ability for these nations who have the larger foreign exchange reserves to invest someplace else and someplace that they believe is of greater stability because you have a multinational consortium sitting behind those funds.

So the Chinese have initially stated that they would be willing to move about \$40 billion into that fund, a relatively small change in the world we're talking about here, but it's a signal, and it comes at the end of now three months of signals from the Chinese saying that they are displeased with what they see as our financial management, displeased with what they see as probably the instability of the U.S. currency over a longer term.

I had one of my Chinese counterparts tell me, "what I see is the United States government printing money hand over fist to essentially create inflation that will render our debt worthless." It's not a Chinese suspicion held in sort of their own little world. That has been expressed elsewhere. The Europeans have offered equally profound statements about what they think we're up to here.

So when I look at what the Chinese are doing in that investment option and in the statements that are coming, particularly from Wen Jiabao, you see the warning signs being offered, but you don't see action that should cause us to be nervous at this point. Rather I would argue it's sort of a prudent decision on their behalf, and they're giving us a chance to do something about it.

I will tell you that if you look at the investment strategies that are being exercised within the CIC, the Chinese Investment Corporation, their sovereign wealth fund, they're far less subtle, but then they've been very blunt and told us that they need to earn \$40 million a day in essentially interest in order to pay for that fund. It was borrowed from the Chinese citizenry.

And as a result, they will not invest in the U.S. financial industry until they see some stability appear on that front. Instead, they are taking their investment into Europe where they believe there are more stable options. They're moving into the commodities market, and if you haven't started purchasing rights in copper, you should.

COMMISSIONER WESSEL: Let me just interrupt there for a moment. You say it's greater stability on the European market or is it greater receptivity to Chinese investments, and we still have a CFIUS overlay, shall we say, and the Europeans seem to be welcoming foreign capital with fewer concerns?

DR. ANDERSON: The Europeans were late to the game. The Germans, the French, and to some extent surprisingly even Great Britain was very reluctant to allow the sovereign wealth funds in, and the Chinese were very blunt. They said if you're unwilling to do that, there are another 150 nations where we might be able to spend our

money.

It wasn't until the financial crisis reached the status that it has that the Europeans suddenly decided maybe it would be a good idea to welcome with open arms this outside investment. I would note they're not alone. The Japanese are also now offering tax inducements intended to draw in these foreign wealth funds. So the manipulation, if you will, is not based simply on addressing a Chinese audience, but on an ability to draw any foreign investor that you can get in and offer the market that's available.

The Chinese have been paying attention; they offered a number of comments when we came up with the FINSA regulations. Their particular concerns focused on ownership and special treatment for foreign governments. I would note that they were not unique in their comments. The British response was very similar, and the Germans also offered fairly scathing remarks when they looked at that legislation.

I would note, however, I looked at the CFIUS investigations over a ten-year period, and when you do the calculation, the number of mergers and acquisitions by foreign governments or foreign entities within the United States versus the number of CFIUS investigations, over a ten-year time period, you have a greater likelihood of being struck by lightning than being subjected to a CFIUS investigation.

So the Chinese aren't terribly concerned about what's happening there. They shouldn't be.

HEARING COCHAIR REINSCH: Thank you.

Commissioner Fiedler.

COMMISSIONER FIEDLER: A couple of quick questions. Does anyone know how many academics have been denied visas still?

DR. TERRILL: During what period?

COMMISSIONER FIEDLER: Well, I know in the '80s and early '90s, there were many. The question is in the last five years.

DR. TERRILL: Yes, in the bad old days of the 1970s, when there were delegations typically going to China, the Chinese would sometimes say Miss X or Mr. Y is not acceptable, and then our side had to make the difficult decision whether to go without those two people or not to go at all, and sometimes the decision went one way and sometimes the decision went another.

In more recent years, it's just been individuals including myself who have been denied visas, but there would be dozens, either related to people working in sensitive areas like Tibet or Xinjiang or wanting to do so or people who have written something unacceptable to Beijing on a sensitive subject.

But the more common mode is not to deny the visa, but not to say yes or no, and the date say of the conference or whatever comes

and goes and, of course, the American person doesn't go to the appointment because his visa didn't come through.

COMMISSIONER FIEDLER: That's an effective denial.

DR. TERRILL: Well, it's a Chinese mode of denial.

COMMISSIONER FIEDLER: Did you have something?

DR. NEWMYER: Yes. Could I just say one other thing? Denying a visa or not answering is a pretty overt signal, and there are more subtle things that can be done, that are done, to cultivate friendly academics or desirable ones and exclude others, and this has to do with granting access to archives, research opportunities, interviews.

So there are some academics in the U.S. who have over the long term been given access to formerly secret documents or have seen archives that were closed, and this has been very good for them and their academic careers, and they're grateful, and who knows whether this compromises their integrity, but it's certainly a more clever or behind-the-scenes way of reaching out and extending influence to academics, and it's much more subtle obviously than the whole visa tool.

Just to answer your question, Commissioner Wessel, about the influence over U.S. companies. I think clearly, as many people have acknowledged, the Chinese are very different as an autocratic state from many former, other autocratic states that the U.S. has ever dealt with, and so the ways that they proceed to shape us and influence us are different from the ways that we are familiar with from the Soviet Union.

They're not heavy-handed, and in the case of a lot of commercial relationships, they're kind of pushing on an open door because business people are inclined to favor stability, continuity, and Pacific relations because it's good for business and commerce. So I think in this whole realm of finance and business, it's difficult to tell what they're doing that's driven by profits and what they're doing that's primarily driven for strategic reasons, but to the extent that they're making investments in U.S. firms, they're encouraging a tendency that's already latent, to say, well, we should just pursue engagement and have good relations and stability will be good for everybody because that's just sort of the economic or the business approach to foreign affairs generally.

COMMISSIONER FIEDLER: Thank you.

Let me ask another question. There have been a lot of rumors with no evidence going around over the last six months that the Chinese entities--some are making contributions to U.S. think tanks in amounts of money that have not been seen before. Let's just say that. Do we have any evidence for this?

DR. TERRILL: Sometimes it's done covertly, but if we take the

Western world in general, there's no doubt that we have cases. For instance, a few months ago, a Chinese company gave hundreds of thousands of dollars to the Lowy Institute in Sydney, Australia, and is now on board as a major contributor to the Lowy Institute.

DR. NEWMYER: Yes, there are centers, a lot of important think tanks, and even university institutions in the U.S. that are funded by Chinese donors, and they're not always official. They sometimes have behind the scene ties to officials, but to be fair, this is not something that is unique to China. The Saudis have done this for a long time. There's a book called *Ivory Towers on Sand* by Martin Kramer that describes it.

COMMISSIONER FIEDLER: Oh, yes, I'm not saying they're the only ones in the world. It's a new phenomena is all I'm saying.

DR. NEWMYER: For China.

COMMISSIONER FIEDLER: Yes.

DR. NEWMYER: Relatively new.

COMMISSIONER FIEDLER: Yes. There are those who argue that this was done largely through U.S. corporations before, but now it's not, and that the Chinese are getting into it themselves because they want more direct influence.

So if you can later send any list that you've got of examples of that, I'd appreciate it because I haven't seen any evidence of it.

HEARING COCHAIR REINSCH: Thank you.

DR. TERRILL: Might I add a footnote to that? The more common mode that I think we'll see is that American businessmen who have done well in business with China will come up with large donations for an American think tank designed on terms that will give full weight to the Chinese government point of view.

That's a very logical pattern for the American businessman and a very typical way in which the Chinese government would like to cooperate because they are not technically involved with the think tank themselves.

COMMISSIONER FIEDLER: Well, that buys somebody the characterization, one, either of friend, good friend or great friend; right?

HEARING COCHAIR REINSCH: Thank you.

Commissioner Wortzel.

VICE CHAIRMAN WORTZEL: I want to thank the three of you for being here and for your testimony.

Dr. Anderson, I'd be interested in any discussion or light you could shed on sovereign wealth funds and their relationship with other government-linked, whether it's Hong Kong or offshore banks and funds, and any coordination between these other entities that seem private and the sovereign wealth funds and their activities.

For Dr. Terrill, is the Chinese Embassy or the consulates active in staying in touch with students on campuses, and if any of you are aware of it, how are they using these new Confucius Institutes to influence what is going on?

Dr. Newmyer, or any others of you, Commissioner Fiedler talked about investments in think tanks and universities. We know, for instance, that the University of Georgia's Nonproliferation Institute's operations in China are fully funded by a Chinese government organization, but, for instance, the CSIS sponsors, has a strategic partnership with an entity that belongs to the Ministry of State Security, and they sponsor a resonant fellow from that institution.

Brookings has a strategic partnership with a Chinese intelligence community-controlled organization. Carnegie has a strategic partnership. To my knowledge, Heritage, AEI, and Cato may be the only think tanks in Washington that don't have those. But how do these strategic partnerships inhibit objective writing or do that?

DR. ANDERSON: I'll open with the sovereign wealth fund. In the trainee situation, you have kind of an interesting problem because there's clearly a bureaucratic battle taking place over who gets to manage a majority of the foreign exchange reserve.

The sovereign wealth fund, the CIC, was carved out of those reserves and then set up as a separate organization that took over for Central Huijin. Central Huijin was running essentially reorganization of the Chinese non-performing loan problem.

The sovereign wealth fund relationship between those two are such that the Chinese sovereign wealth fund now owns Central Huijin and owns the shares within the Chinese banks that have been publicly listed, a profitable venture, by the way. This was actually an astute business move on their behalf.

The problem that we have in breaking out between where the investments are taking place in a sovereign wealth fund, the declared sovereign wealth fund, and other institutions within China is the activity that we see resident within SAFE, the State Administration for Foreign Exchange.

They apparently have decided that they're not going to render up all of the ability to go invest outside of the country, and so they almost directly compete with the China Investment Corporation, and you can see, and it comes across occasionally in reporting, the debate that's taking place as to who gets to ultimately own all of this, and one gets the feeling that SAFE is going to eventually try to reach back down and put CIC back underneath their auspices. I suspect that that will eventually happen.

Your question concerning the relationships on offshore investment, this is a real problem area for Wall Street, in particular.

The Chinese Investment Corporation, for instance, in placing \$4 billion within JC Flowers put that money into essentially a hedge fund, if you will, a trust that goes and invests for them.

They have told Flowers and company that they have no interest in managing the corporation, and that they only expect a return, that they're not going to exercise influence.

I would tell you that there was a precedent that took place yesterday that every sovereign wealth fund manager is going to notice across the planet, and that was the decision by Calpers to vote against retention of the Bank of America directorate, all 18 members of the Bank of Directorate. Calpers, for any organization outside this country, is considered to be an American sovereign wealth fund, and their decision to directly input on the Board of Directors' vote will probably be exercised now by other organizations.

The Norwegians already proceeded down that path. I suspect the Chinese will follow suit eventually. They will tell you it's just good financial management. You're looking out for your investors' concerns so that's what they're going to do.

The bigger problem on tracking Chinese investment within this country is something called "dark pools." And that is the situation on Wall Street whereby trades are matched up via computer systems that are not publicly announced sometimes for 24 to 36 hours after they transpire.

Five years ago about five percent of the business on the street was done using dark pools. The most recent estimate I saw was somewhere around 40 percent, and there is an estimate that that will continue to increase because it's very efficient. It's an effective way to do business, and it matches up large swaps of money with large available stocks, if you will. We don't know--

HEARING COCHAIR REINSCH: Let me interrupt for a second. We're running out of time here, and I want to make sure that all commissioners have a chance to have their questions answered.

Can we, maybe you can have a sidebar on that? You asked a second question; did you not?

COMMISSIONER BARTHOLOMEW: I'm actually next on questioning, and I'm going to defer that chance and let the witnesses answer Larry's second set of questions under my time.

HEARING COCHAIR REINSCH: Can we go then to your second question and we'll come back to Dr. Anderson later?

VICE CHAIRMAN WORTZEL: All right. My second question was for Dr. Terrill on the Chinese Embassy and how it operates on campus?

And the third was for Dr. Newmyer principally on how strategic partnerships affect operations.

DR. TERRILL: Well, the Chinese Embassy--

COMMISSIONER BARTHOLOMEW: Excuse me, Dr. Terrill. I just want to add one other issue into that mix, and that is although I was thinking about it in the context of denial of visas, Dr. Newmyer, you were mentioning about access to research materials. How is that on campus? How is it being perceived on campus as people are either getting access to things or being denied access to things?

Is it indeed creating a competitive disadvantage for certain categories of graduate students as they move forward in their careers? I think it is all part of the same thing.

Dr. Terrill.

DR. TERRILL: It's more of a problem for the younger ones because they have their whole careers ahead. It's more of a cat and mouse game with the older ones because after awhile, the Chinese government would look very stupid, for instance, to make a fuss over me coming into the country; they would probably end up losing more than they could gain.

But their influence over what graduate students here will choose as their topics can be considerable on the archive question.

Yes, the Chinese Embassy and consulates do keep in very close touch with the students. A lot of it is benign, just like the French consulate in Boston keeps in touch with students from Paris. Where it becomes problematic is what happened with the Olympic Torch in San Francisco, that the Chinese students are mobilized by the consulate to interfere with the Americans who are saying things, in our normal kind of fashion, in the streets, about an issue and the Chinese grab the posters from them and stop them.

So it's as if in '99 with the accidental bombing of the Embassy in Belgrade or in '01 with the EP-3 incident, when the Chinese converged on the American Embassy in Beijing, it's as if the Beijing Embassy got the Americans from every province in China to come and combat the Chinese protest. You know, we don't do things like that.

They do do things that way. The Confucius Institutes are very much in evolution and money is going to be the key. Just very recently, the last couple weeks, in Britain, the Chinese decided they would pay the full salary of the co-director, not just the London Institute paying half and China the full. So this is going to be the typical challenge we have to face.

The extra money in Chinese pockets is good in that they don't have to do some of the PR work they used to do in a very clumsy way.

But the extra money also means that there will be new modes for their work.

HEARING COCHAIR REINSCH: We still have not gotten to Larry's question about the think tanks. Could we do that?

DR. NEWMYER: Could I just quickly tackle that? Yes. I think that the answer is the effect of these partnerships between think tanks like Carnegie and Brookings is huge in terms of the way it sets the research agenda for the think tanks and the things they talk about and don't talk about, and I think the fact that there is no relationship that I know of with AEI is not for lack of Chinese efforts.

And the same with the Harvard Kennedy School and, in fact, there are ties. But I think the interesting thing is we're only having, the Commission is only having this hearing on Chinese influence operations now and there are very few books about these words that come up all the time in Chinese writings, public relations strategy, war, informatization war, not in the military realm, but in the diplomacy realm.

The fact that Zheng Bijian, this guy who came up with the term "peaceful rise," there's a China Quarterly article about the term and its change to "peaceful development" that doesn't even mention that he's a propaganda official from the 1960s. He's been a propaganda official.

We never hear that a lot of the institutions in China that we talk about as think tanks are actually part of the Ministry of State Security, which is responsible for counterintelligence. It is the highest levels of the political military elite in China, and we talk about it like it's Brookings.

So I think that the impact is huge of these relationships and connections, and Americans are by nature trying to be democratic and conciliatory and engaging, and so there are just things that we don't talk about because it's not polite.

And then the other interesting thing I think about the Chinese students on campus is the way that it may be the case that instead of becoming more open by exposure to the U.S., their nationalism is being fueled. This has been my experience from anecdotally all the Chinese students that I've talked to at Harvard, around Harvard. If you hang out at Harvard these days, you hear that America is in decline, that maybe that's a good thing, that it's fine for there to be a different kind of multipolar world.

If you're a Chinese student at Harvard, you hear that, and you come from China and you're proud, and I think some of your nationalism gets reinforced. It's not that the experience makes you more open to the West and freedom. It makes you more proud of being Chinese and more convinced that China has a certain place in the world that it should occupy soon.

HEARING COCHAIR REINSCH: Does this mean we should be investigating Harvard? Is that what you're suggesting?

DR. NEWMYER: It's not just Harvard. I just happen to live in Cambridge, but I think this is a general academic phenomenon.

HEARING COCHAIR REINSCH: I see. I suspect some of my colleagues might want to do that, but anyway Commissioner Mulloy.

COMMISSIONER FIEDLER: It's a waste of time.

COMMISSIONER MULLOY: Thank you, Mr. Chairman.

I remember reading a book--I think it was by Jim Mann. Mr. Mann was our correspondent for Los Angeles Times in Shanghai for a number of years. He's written a number of interesting books, but this one, I think was called the *The China Paradox*.

DR. NEWMYER: *Fantasy*.

COMMISSIONER BARTHOLOMEW: *China Fantasy*.

COMMISSIONER MULLOY: *China Fantasy*. I remember reading that when I went to hear him speak, he described Washington think tanks as I think something like peculiar institutions that seem to reflect the views of those who pay them.

So when I was reading Dr. Terrill's testimony, and he was talking about wealthy Americans who made a lot of money in China putting money into a number of think tanks, and then he says further that two Chinese companies--I presume these Chinese companies are government-owned companies or government controlled--have started making healthy donations to think tanks in Western societies.

So the issues that we're talking about I think are pretty important because if these think tanks are helping shape public policy in the United States, we at least ought to know something about the connections and the type of views of whoever is paying them likes espoused.

Dr. Terrill, do you want to respond, and then Dr. Newmyer.

DR. TERRILL: I'll start with one point. The way to nip this in the bud is to have a look at the agenda for the seminars and conferences that come out of this think tank. Now, we may have--we have had conferences where you have someone from the NPC in China, the National People's Congress, and then someone from the Congress here.

Well, the NPC is not a legitimate parliament. No one has elected these people, but it looks as if you're having someone from the American side and someone from the equivalent function on the Chinese side. That's what's going to happen if the money is coming in one way or another from the Chinese side, and you have these murky people as sponsors and participants. Dr. Newmyer has given examples of people who, it's not known are they from the Chinese military or where are they from?

And in America at a conference, it's pretty transparent who are these people; they have their reputations. Something different is going to happen if the money comes into think tanks from the Chinese side.

COMMISSIONER MULLOY: Do you have anything you want to

say, Dr. Newmyer? There's just one follow-up. Then, I want to ask Dr. Anderson.

In your page ten of your testimony, you're talking about the Chinese investments in America and they've got all this money. As we've tracked through the years, of course, they've got a lot of this money by very mercantilist trade policies including under pricing their currency, which they then get the dollars that they get by running a huge trade surplus and reinvest it back in our Treasuries, which we did a hearing on in February, and there's some suggestion that that contributed to the current global financial crisis.

So what I was struck by, and I know many members of Congress, including President Obama when he was a member, cosponsored legislation to say that the underpriced Chinese currency is an export subsidy, and Chinese commentators all would say that's protectionist legislation.

So I was very interested that you talk about there's a worry about protectionist legislation, and I just wondered what are you talking about, and what would be protectionist in your mind? Would that kind of legislation be protectionist? Is there something else you have in mind?

DR. ANDERSON: From the Chinese perspective, the biggest concern is a restriction on their ability to invest within this country and specifically a restriction that limits a government entity investing within this country. They would call that protectionist legislation.

Your question on the currency valuation, I can tell you that the Chinese response is twofold. One, they go back to the Bretton Woods agreement, that they say if you look at the underlying principles in Bretton Woods, it was the idea that the core supported the periphery and development within the periphery, and that's what they continued with, as far as they're concerned, what they did with their development process.

And then they pick up their pieces, and this is something that's going to be thrown in our face repeatedly now, and they point to the decision that was made during the '97-98 Asian financial crisis where the Chinese chose not to devalue their currency and thereby finally put a stop to what was going to be runaway devaluation of all the Asian currencies.

And they took it in the shorts, quite frankly. They paid much higher prices for the imports that were required in order to run their factories, so that in the short-term they could, at our behest, by the way, help maintain the value of the Asian currencies and restabilize that marketplace.

They're now looking at us in bewilderment and saying here's what we have done, and, yes, we maintain the strict control over our

currency, but, one, it's to prevent inflation in our own country; two, we have allowed a float. They've allowed about a 20 percent float, if I remember, over the last year in the value of that currency. And they're going to maintain strict control on it because what they're telling us over and over again is that when required, we behave like a responsible international player, and now we're looking at you and we're looking at the way that you regulated your economy and telling you it didn't work there and so why should we follow in your model? And so we have a problem on our hands.

HEARING COCHAIR REINSCH: Commissioner Slane.

COMMISSIONER SLANE: Thank you.

Dr. Anderson, I just wanted to follow up on a question that Commissioner Wortzel asked you. It's hard for me to believe that when the interest bill comes due on the stimulus next year, that we're not going to see significant inflation in our country. It seems like the warning signs that you talked about indicate that the Chinese are going to start shifting some of their investment into the EU.

Can you talk about that and the effect that it will have on our economy?

DR. ANDERSON: I have, I think, what some people would call the misfortune of spending a lot of time talking to Nouriel Roubini, "Dr. Doom." And I also moonlight as an economist so you can throw bricks at me.

The basic problem we have in this country is that I think in some senses we've forgotten that money is a commodity and that there is only a certain amount of it available, and we have tremendous competition for access to that commodity. The largest competitor these days is the U.S. government, and the U.S. government is trying to stimulate consumer spending.

In order for the U.S. government to continue down that path without creating tremendous inflation, we have to get somebody to buy our Treasury notes. Okay. That somebody has been the Chinese and the Japanese primarily. We don't have the domestic savings to do that.

Should our Treasury notes be no longer of interest to outside consumers, to the Chinese, to anybody else sitting off our shores, the cost of borrowing in this country is going to increase. The conservative models will tell you that the cost of that increase will be somewhere around 50 basis points. So instead of six percent, you'll pay 6.5 percent for a loan.

The grimmer models that start to look at what's coming start at 150 basis points, and probably the most popular right now with the economics community are 300 basis points.

So if you're looking at a stimulus package that has to survive over time, you need one that does not cause the cost of borrowing in

this country to go from six percent for an auto loan to nine percent because now you're going to have the same problem we have today. Consumers will not spend when they start looking at that kind of cost.

That's the consequence of the Chinese pulling out of our economy if they believe that it is not a stable place to place their currency.

DR. NEWMYER: Can I just follow up because I think we're equally political science Ph.D.s and therefore equally "economists" on this panel?

I actually think that for the Chinese, as long as their reserves are as big as they are, their reserve holdings, there aren't that many options for them other than U.S. Treasuries. And they've tried to diversify a little and they've moved into commodities, and it's possible that as their exports go down, the size of their surplus will go down, although they've also cut back their imports. So they're still running big surpluses.

And they can't really shift to the EU. As long as they want to try to keep their currency low by buying something, by sterilizing their surpluses, they can't really shift to the EU because then they're kind of hostage to, for instance, the Italian government's current financial policies. I mean there's no equivalent of the dollar in the EU.

Policies are hostage to or determined by the individual member states. So the Chinese actually, I don't think we have to be so nervous. I think this is a little bit of a red herring, and I think we, maybe you're talking about it too much, this idea that there's a big threat-- the mutually financially assured destruction-- hanging over us.

If they move out of the U.S. Treasuries, they don't have any other options at this point.

DR. ANDERSON: I would have agreed with that statement right up until the point where we all agreed that the IMF needed to have a trillion dollar fund available for loaning out to other countries and suddenly you have direct competition to U.S. Treasury notes.

DR. TERRILL: My Chinese friends give another reason why they're not going to sell their Treasuries--because the dollar would go down and the value of their Chinese exporting to the United States, which is crucial to their economy, would collapse around them.

It's not without interest that in last October, which I spent in Shanghai, the heads of two of China's top four banks said words to the effect that American economic strength is good for China.

And there's a big gap between the students at Harvard or Berkeley, who are influenced by their American professors on American decline, and the views in the Chinese Communist Party. The Chinese Communist Party neither wants nor believes in American decline.

HEARING COCHAIR REINSCH: Commissioner Cleveland.

COMMISSIONER CLEVELAND: I think Professor Newmyer's comments were probably most consistent with mine in terms of believing that there are not a lot of other options, but I'd like, if possible, Mr. Anderson, if you would clarify or expand upon where you think the Chinese actually could go. And a trillion dollars at the IMF, as we all know, is not actually real money; it's callable capital. And so it doesn't directly compete with U.S. Treasuries in the short term.

It may affect the governance agenda at these institutions and some of the policies that the institutions pursue, but it's not direct competition for U.S. Treasuries. So if you'd like to add to your comments about what the alternatives are in terms of where the Chinese might invest and, Dr. Newmyer, and Dr. Anderson, if you could speak to that as well.

DR. ANDERSON: Sure. I'll respectfully disagree with you, ma'am. The problem that we're running into, and it's now started to receive coverage within the American financial press, is the fact that the IMF fund is going to pay an interest rate. It's a bond issuance in order to fund that. And because it's a bond issuance, there will be interest that's associated.

And as somebody told me, all you have to do is pay 50 basis points above what the U.S. Treasury notes are offering, and when you're looking at \$40 billion investments, people will be interested in moving their money elsewhere. So there is an option there.

The Chinese as--and sort of the indicator that I use for people on where the Chinese may be moving their money otherwise is to follow the sovereign wealth fund investments and where they actually have opportunities to go into foreign countries and invest.

The particular case in point that I like to look at is where the Norwegians have been welcomed, and the Norwegians have the most opaque or the most transparent fund sitting out there. The Norwegians now own--one of my friends will tell me--five percent of approximately every major corporation within Europe. So it's not a focused investment within a particular country; it's spreading your wealth out amongst a large number of other opportunities that are available.

COMMISSIONER CLEVELAND: But clarify what that means. Five percent of a lot of companies sounds like a significant issue. What does it actually mean in terms of dollars given the size of the reserves the Chinese are sitting on perhaps? It's misleading to suggest that five percent is--well, go ahead. Sorry.

DR. ANDERSON: Okay. No, no, no. I use two examples when I'm trying to explain this, and one of them is to look at where the

Singaporeans have invested their funds over the last five years now. There's a distinct investment trend there.

The Singaporeans are not buying Treasury notes, by the way, nor, by the way, are the Norwegians. They're going the opposite direction. They've taken their \$300 billion foreign, their \$300 billion sovereign wealth fund and used it to invest anywhere but U.S. Treasury notes essentially, and they could if they so choose. So could the Singaporeans.

To use the models that are available from Harvard and Yale in their endowment funds, it's a divestment, and you divest as far as you can, and so the concern becomes what other options are available at the time? So we're now looking at a Chinese interest in, for instance, real estate in this country, which has drawn significant interest when you can pay 40 cents on the dollar.

We're looking at significant Chinese interest in purchasing commodities of all varieties, not just copper. We're also looking at the acquisition of oil rights.

So there's an interest in spending that money elsewhere that is useful for China's long-term development, and as you take funds away from us, it's not going to happen overnight. It's not one of these things where I'm telling you that tomorrow morning, the interest rates are going to go through the ceiling.

What I'm telling you is that those interest rates are going to start going up over a longer time period as those funds move elsewhere.

COMMISSIONER CLEVELAND: But you just identified two sources where they're moving that are both U.S.--I mean for better or for worse--both U.S. opportunities in terms of U.S. real estate and --

DR. ANDERSON: What they're not doing is putting the money into our Treasury notes. That's the problem. By acquiring real estate, you're not putting that money back into the government's hands to make it available to avoid the increased cost of interest.

COMMISSIONER CLEVELAND: Some of us view capitalism as a positive thing, but--

DR. NEWMYER: Just quickly, yes, they have a lot of cash and they need to figure out how to keep it growing, but they also have a huge problem. Their stimulus package was a bigger share of their GDP than ours was, and it's likely to be less efficient and less successful because it was allocated to state-owned enterprises and road construction and infrastructure projects which provide temporary employment, but they're not a source of growth and investment going forward into the future.

What the economists prescribe for them is a much more robust domestic consumption economy, which they can't switch to overnight even if they wanted to. It's not clear to me that they want to because

it would mean a significant loss of control for the Party which has a lot of resources at its disposal in the center right now, and to have a robust domestic economy would involve a much more independent banking infrastructure, rule of law for contracts, etc.

Their growth so far has leveraged Western rule of law because it's been export led, but to have a robust domestic economy that would insulate them from this kind of downturn, they would need to change a lot, and it's not clear that they can or want to.

DR. ANDERSON: If I could for a minute. A comment on the Chinese stimulus package because--

HEARING COCHAIR REINSCH: A brief comment, please.

DR. ANDERSON: Yes, sir. We've seen a lot of popular media comment in this country on this. I'll give you the source I think is relatively reliable in the world of capitalism. The Wall Street Journal believes that the Chinese stimulus project was the most effective passed to date, and in that stimulus package, we have movement available that pushes them towards the consumer economy which is really what we want them to do, and it's in a number of places, not just infrastructure development, but also in the health care programs and retirement programs, and in the education investments.

HEARING COCHAIR REINSCH: Commissioner Bartholomew is going to have the last word.

COMMISSIONER BARTHOLOMEW: Just to say that it's a very interesting discussion, but to tie it directly back into the topic at hand that we have been dealing with, what strikes me is that there's a debate about the reality of the threat. In some ways, that's beside the point.

One of the questions to my mind is that the leverage that the Chinese government gets from the perception that they might indeed make financial decisions that could have an impact, that we are seeing cases where the United States government is not taking action on things that might be in the U.S. interest because they are concerned that the Chinese might decide that they no longer want to buy our debt.

So the perception of how they're using that and the leverage that they're getting out of that is, I think, a critically important piece of how we deal with this global financial crisis.

DR. TERRILL: That's true, Commissioner, but doesn't it also illustrate that we now are in a certain interdependence with the Chinese?

For instance, they could say, "What if Americans stopped going into Wal-Mart and buying those photo albums and those shoes?" You and I know that's not going to happen here because the price is good, the quality is reasonable, and Americans, short of some major crisis in the world with China, are not going to stop buying those things.

I think we're in this interdependence with the Treasuries on their

side, with their products in our stores on our side, and I take some heart from this because there are good sides to the interdependence, too.

COMMISSIONER BARTHOLOMEW: Dr. Terrill, I think you're absolutely right on that interdependence, and it's interesting that as Americans indeed did stop buying, although they have not completely stopped buying at places like Wal-Mart, that production in China has shut down in a number of places. I think it demonstrated something that some of us started talking about ten or 15 years ago, that as Americans were losing jobs because they were losing manufacturing jobs overseas, their ability to purchase was going to be diminished. So there is an interdependency in all of that.

HEARING COCHAIR REINSCH: Let me thank the panel for a very interesting and enlightening and occasionally heated conversation which has been very useful to us. We appreciate your time with us and thank you very much.

We're now going to recess until 1:15 when we'll begin with the final two panels for the day.

[Whereupon, at 12:20 p.m., the hearing recessed, to reconvene at 1:20 p.m., this same day.]

A F T E R N O O N S E S S I O N

PANEL III: CHINA'S ESPIONAGE AND INTELLIGENCE OPERATIONS DIRECTED AT THE UNITED STATES

HEARING COCHAIR BROOKES: Good afternoon. Welcome or welcome back. We're going to commence the third panel now as soon as I find the biographies.

Joining us for today's third panel on "China's Espionage and Intelligence Operations Directed at the United States" is Mr. I.C. Smith and Dr. James Mulvenon.

Mr. Smith joined the FBI in 1973 and served as a Special Agent until 1998. During this time, he saw assignments in St. Louis, Washington, D.C., Miami and Little Rock. He also served as Legal Attaché in Canberra, Australia with responsibility for independent nations of the South Pacific.

He was also posted to the State Department as Chief of Investigations, Counterintelligence Programs. During the course of his career, he was involved with a number of high profile espionage cases, including those of Larry Wu Tai Chin and Katrina Leung.

Also joining Mr. Smith on the panel is James Mulvenon, no stranger to our committee. He is the Vice President of Defense Group, Incorporated's Intelligence Division and Director of its Center for Intelligence Research and Analysis.

A specialist on Chinese national security issues, Dr. Mulvenon's research focuses on Chinese military development, defense research and development organizations and policies; strategic weapons programs; and the military and civilian implications of the information revolution in China.

Thank you both for joining us today. If you would, since we have your written statements, which will be submitted in full into the record, if you could keep your comments to seven to ten minutes, it will allow us the maximum time for questions and answers.

Mr. Smith, if you would like to proceed.

**STATEMENT OF MR. I.C. SMITH
SPECIAL AGENT (RETIRED), FEDERAL BUREAU OF
INVESTIGATION, WASHINGTON, DC**

MR. SMITH: Thank you, Commissioner.

Let me begin by stating the obvious. The People's Republic of China is neither the people's nor is it a republic. The PRC is an oppressive, totalitarian police state that's governed by the Communist Party that allows less than five percent of its population to become members. The Chinese Communist Party has, in effect, become the new royalty whose primary goal is to retain power.

As a growing awareness of the threat posed by China gains, well, hopefully, some momentum, I suspect that even this Commission is divided as to where the major emphasis of our attention should be.

There is, of course, the pervasive violation of human rights and civil liberties of its own people. There's the oppressive occupation of Tibet. There are the repeated violations of copyright and other trade and economic related matters. Then there is the daily deluge of cyber attacks targeting the infrastructure of our national security.

The Chinese make political mischief for our nation at every opportunity, and there is a massive attempt to obtain by any means this nation's technology. Regardless of one's emphasis, there is enough reason for worry that there should be concern for all of us. There is no doubt the Chinese view the United States as its number one adversary. The totality of the threat by the Chinese is the greatest

threat to our national security that we face today.

Now from the standpoint of this panel's portion of the hearings, we should note that never has this country faced such massive attacks on virtually all fronts from a single country as we see from China right now.

But from the standpoint of the human aspects of that effort, there's a clear distinction between past and present adversaries. That is the Chinese almost total dependence of those of a like ethnicity to accomplish their goals. Further, not all Chinese spies steal technology and not all restricted technology acquired by the PRC is stolen by intelligence officers.

Indeed, if one looked at those investigations that have been in the public eye, the two most prominent cases where there is little doubt there was a PRC intelligence service presence, and that would be the Larry Wu Tai Chin and Katrina Leung matters, neither of those cases involved the acquisition of technology.

Conversely, if one looks at a number of other high profile investigations such as Wen Ho Lee, Peter Lee, Min Guo Bao, which involved highly classified technologies, there is no apparent PRC intelligence service presence, and this even applies to Chi Mak, where the government and media assertions that he was a long-time intelligence officer are less than clear to me.

This simply serves to confuse the whole issue. One may ask something of an academic question: Is it truly an intelligence operation in the absence of an intelligence service? Well, oftentimes, it's practically impossible to determine if any activity is truly being run by the PRC's intelligence services or is this being run by an academic or even business interest?

The old saying that if it "walks like a duck and quacks like a duck and looks like a duck, then it's probably a duck" simply doesn't apply to Chinese operations.

Further, I'm still convinced that the Chinese collection effort remains highly decentralized, even with the implementation of its highly touted 863 Program, with little coordination between the military and civilian intelligence agencies, academic institutions, and increasingly business interests where there is as much tendency to compete as there is to cooperate.

But while in the past, I've opined that the Chinese have been much better at collecting information than putting it to use, I get the impression that they have improved considerably in their ability to implement their ill-gotten technology into weapons systems by making use of dual-use technology as it can have both civilian and military applications.

Now, the primary role of the Chinese intelligence and security

services is to ensure the Chinese Communist Party remains in power. That applies to both the civilian intelligence agencies, the MPS and the MSS, and that's one of the really enduring characteristics of Communism in general and certainly applies to the Chinese.

As a result, these services are given status and privilege far beyond their counterparts in the West. They're also given immense power and they are the single-most feared part of Chinese society. Unlike the PLA, where conscripts are an integral part of its ranks, the ranks of the MPS and MSS are much more select, and it is within their own self-interest to ensure that the Chinese Communist Party remains in power.

And it's these services and especially the MSS that are at the forefront of the espionage and intelligence operations within the U.S., and they're an arrogant, confident and freewheeling service which can have no doubt that they have the complete confidence of the Chinese Communist Party's leadership.

My experience is that there is oftentimes little specific targeting of information or technology by the Chinese, but instead they take the approach that just get the information to us and we'll sort it out later. But there's almost a total dependence on Chinese Americans to accomplish their technological acquisition effort. The Chinese don't just hope that Chinese Americans--and that's the overseas Chinese from their standpoint--will aid in their efforts. They don't just expect that this will occur; they simply assume that all ethnic Chinese will be of service to mother China.

The Chinese simply can't envision that an ethnic Chinese could have loyalties to any other country but their own. They are, after all, Chinese.

But their considerable successes have largely centered around first generation Chinese Americans who were born in China, made their way to the United States, but have retained a strong cultural identity and family ties to their homeland.

The Chinese have been largely unsuccessful in gaining the support of second generation and beyond Chinese Americans who many times even reject the Chinese language and culture and are more interested in becoming Americanized than having divided loyalties.

But we as a country make it relatively easy for the Chinese. We allow them to purchase our companies; to send literally thousands of students to study in this country in all disciplines. Delegations have almost a free rein in traveling about the country, and politically we haven't shown any political will to punish the Chinese for their frequent violations, activities such as the Hainan Island incident, the harassment of our ships in international waters, and such.

Our approach seems to be, even including Tiananmen Square,

was to get the incident out of the news as quickly as possible. I believe, in my view, that it's time for this country to practice a stricter reciprocity in dealing with the PRC, and while we, as a country, look at long-term goals as the next election cycle, the Chinese have no such obstacles in planning for the future.

They will simply stay the course, grind away, eventually expecting to wear you down until they obtain whatever goal they're seeking, and right before I left, I remembered a quote by Sun Tzu so I went back in--and that should be required reading, by the way, for everybody dealing with China and counterintelligence and what have you--but he made this comment written 2,500 years ago:

"For to win 100 victories and 100 battles is not the acme of skill; to subdue the enemy without fighting is the acme of skill."

I firmly believe the Chinese are still practicing that advice from Sun Tzu of over 2,500 years ago.

Thank you.

[The statement follows:]

**PREPARED STATEMENT OF MR. I.C. SMITH
SPECIAL AGENT (RETIRED), FEDERAL BUREAU OF
INVESTIGATION, WASHINGTON, DC**

Let me begin by stating the obvious. The People's Republic of China is neither the people's nor is it a republic. The PRC is an oppressive totalitarian police state that is governed by the Communist Party that allows less than five percent of the population to become members. The Chinese Communist Party has become, in effect, China's new royalty whose primary goal is to retain power.

As the growing awareness of the threat posed by China gains, hopefully, some momentum, I suspect, even this Commission is divided as to where the major emphasis of our attentions should be. There is the pervasive violation of human rights and civil liberties of its own people, there is the oppressive occupation of Tibet, there are the repeated violations of copyright and other trade and economic related matters and there is the daily deluge of cyber attacks targeting the infrastructure of our national security. The Chinese make political mischief for our nation at every opportunity and there is the massive attempt to obtain, by any means, this nation's technology. Regardless of one's emphasis, there is enough reason for worry that should be of concern for all of us. There is no doubt the Chinese view the United States as its number one adversary. The totality of the threat by the Chinese is the greatest threat to our national security that we face today.

From the standpoint of this panel's portion of these hearings, "China's Espionage and Intelligence Operations Directed at the United States," we should note that never has this country faced such massive attacks, on virtually all fronts, from a single country as China does right now. But, from the standpoint of the human aspects of that effort, there is a clear distinction from past and present adversaries, that is, the Chinese almost total dependence on those of a like ethnicity to accomplish their goals. Further, not all Chinese spies steal technology and not all restricted technology acquired by the PRC is stolen by intelligence officers. Indeed, if one looks those investigations that have been in the public eye, the two most prominent cases where there is little doubt there was a PRC intelligence service presence, Larry Wu Tai Chin and Katrina Leung, neither of those cases involved the acquisition of technology. Conversely, if one looks at a number of other high profile investigations such as Wen Ho Lee, Peter Lee, Min Guo Bao, etc., which involved highly classified technologies, there is no apparent PRC intelligence service presence. And this even applies to Chi Mak, where government and media assertions that he was a long-time

intelligence operative are less than clear to me.

This simply serves to confuse the whole issue. One may ask something of an academic question, “Is it truly an intelligence operation in the absence of the presence of an intelligence service?” Often times it is practically impossible to determine if an activity is truly being run by the PRC’s intelligence services, or is this being run by academic or even, business interests. The old saying that if it “...walks like a duck, quacks like a duck and looks like a duck, then its probably a duck,” doesn’t apply to Chinese operations. Further, I’m still convinced that the Chinese collection effort remains largely decentralized, even after the implementation of its highly touted “863 Program,” with little coordination between the military and civilian intelligence agencies, academic institutions and increasingly, business interests where there is as much a tendency to compete as there is to cooperate. But while in the past I’ve opined that the Chinese have been much better at collecting information than putting it to use, I get the impression that they have improved considerably in their ability to implement their ill-gotten technology into weapons systems by making use, for instance, of dual use technologies that can have both civilian and military applications.

The primary goal of the Chinese intelligence and security services is to ensure the Chinese Communist Party remains in power. That applies to both the civilian intelligence agencies, the Ministry of Public Security, the *Gonganbu* as well as the Ministry of State Security, the *Guojia Anquanbu*. This is one of the enduring characteristics of Communism in general and certainly applies to the Chinese. As a result, these services are given status and privileges, far beyond their counterparts in the West. They are also given immense power and they are the single most feared part of Chinese society. Unlike the People’s Liberation Army, where conscripts are an integral part of its ranks, the ranks of the MPS and the MSS are much more select and it is within their own self interest to ensure that the CCP remains in power. It is these services, and especially the MSS, that are at the forefront of the espionage and intelligence operations within the US, an arrogant, confident and freewheeling service which can have no doubt that they have the complete confidence of the CCP’s leadership.

My experience is that there is, often times, little specific targeting of information or technology by the Chinese, but instead, they take the approach that just get the information to us and we will sort it out later. But there is an almost total dependence on Chinese-Americans to accomplish their technological acquisition effort. The Chinese don’t just hope that Chinese-Americans, the “Overseas Chinese” from their standpoint, will aid in their effort, they don’t just expect that this will occur, they simply assume that all ethnic Chinese will be of service to mother China. The Chinese can’t envision that an ethnic Chinese could have loyalties to any other country but their own. They are, after all, Chinese!

Their considerable successes have largely centered about first generation Chinese-Americans who were born in China, made their way to the United States, but who have retained a strong cultural identity and family ties to their homeland. The Chinese have been largely un-successful in gaining the support of second generation, and beyond, Chinese-Americans, many of whom even reject their Chinese language and culture and are more interested in becoming fully Americanized without divided loyalties.

But we, as a country, make it relatively easy for the Chinese. We allow them to purchase our companies, to send literally thousands of their students to study in this country in all disciplines, delegations have almost a free rein in traveling about the country and politically, we haven’t shown any political will to punish the Chinese for their frequent violations and activities, i.e. the Hainan Island incident, undervaluation of their currency, the harassment of our ships in international waters, the sudden cancellation of ship visits to Hong Kong, etc. Our approach, even including Tiananmen Square, was to get the incident out of the news as quickly as possible. I believe it’s time for this country to practice a stricter reciprocity in dealing with the PRC. And while we, as a country, look at long term goals as the next election cycle, the Chinese have no such obstacles in planning for the future. They will simply stay the course and grind away, eventually expecting to wear you down until they obtain whatever goal they were seeking.

I look forward to our discussion.

HEARING COCHAIR BROOKES: Thank you, Mr. Smith.
Dr. Mulvenon.

**DR. JAMES MULVENON, DIRECTOR
CENTER FOR INTELLIGENCE RESEARCH AND ANALYSIS
DEFENSE GROUP, INC., WASHINGTON, DC**

DR. MULVENON: Thank you, Mr. Chairman. As a way of introduction and disclaimer, given my current responsibilities, I have clearly prepared my comments very carefully, and I will answer your questions carefully. I'll try not to parse too much. But I certainly don't want my comments in any way to reflect on any of my wise and generous sponsors in the U.S. government or any of the work that we do for them.

The good news is that there's plenty of material available on this subject in the public realm, and I believe that analytical judgments can be made based on that as well as other experience analyzing this type of material.

I have three points. I think, Mr. Chairman, that even open source material reveals that China is one, if not the largest, perpetrator of economic espionage against the United States right now. I personally maintain a spreadsheet of relevant economic espionage cases, not always easy to assemble. Often these articles are only in obscure state and county level newspapers across the United States.

There's no centralized repository of them, but I count at least 25 cases since 2004 that fit the rough pattern of what we would describe as Chinese economic and technological espionage against the United States.

I know of no other foreign power with a similar record. It may be symptomatic of a lack of professionalism on the Chinese side, or it simply may be reflective of what it is, which is the scale of the activity.

There are certain patterns in these cases that I find analytically interesting. I echo the comments of my colleague here on the panel although I would note the surprising presence of a large number of Taiwanese Americans as well as naturalized citizens of Taiwan background involved in these economic espionage cases that are clearly meant to benefit China, and so I think that we need to take a more expansive definition of the categories of people we're looking at because the Chinese system has shown a propensity, in my view, to tap into networks of overseas Chinese broadly defined.

Second, I would note that in many of these cases what we're describing are mom and pop operations, often being run out of individual's homes. They have set up companies clearly for the conduct of this behavior, but it is a company in name only. It's a mailbox; it's simply operating out of their apartment.

Thirdly, I would note that in terms of the technology acquisition that we find troubling, more often than not our defense contractors, our classified defense contractors, and other manufacturers of sensitive equipment are often not directly involved.

My experience has been that those companies have excellent security practices in terms of ITAR controls and the physical control of their technologies, but instead that we often see in these cases Chinese taking advantage of a secondary market of distributors. You can even on a daily basis find things on eBay frankly that while may not be state-of-the-art simply would benefit the Chinese system.

Often in these cases, we find them obfuscating the end user, and there are layers here that I think are important about how easy it is for them to obfuscate the end user, and that has a lot to do with our own weaknesses, particularly in the area of Chinese language issues, and I'll come to that at the end when I talk about some of the remediation that I think we could make.

But the strategic goals from the Chinese side for this economic espionage I think are fairly clear. Their state innovation planning documents specifically discuss the extent to which they need to acquire technology from abroad, both licitly and illicitly, in order to fund their innovation process.

China, in my view, is on the fulcrum point of a strategic transition in terms of its internal economy as well as its science and technology prowess. For 20 years, as you know, Mr. Chairman, China has been largely an export processing zone for other country and other multinational companies to then export technology and equipment and goods out of China. But the Chinese leadership has made it very clear for as long as you can go back that they resist this dependency at a strategic level; they believe that China is poised to become a strategic innovator in a wide variety of sectors.

But that innovation requires inputs of high-end and state-of-the-art technology and know-how that multinational companies I think to a large extent have wisely decided to not export to China, and so, we could talk about semiconductors and trends there of things that have been withheld and technologies that have been withheld and capabilities that have been withheld, but China clearly wants to push that with the ultimate goal of import substitution, of creating a class of national champion Chinese companies that can then supplant those multinational companies, both in the Chinese market as well as globally.

We can highlight companies like Huawei and others that have already successfully done that.

My second point would be that the open source evidence clearly suggests that most of these cases that the individuals involved are not

trained espionage agents as we would define them with tradecraft training and other professional training, but instead are what I would term espionage entrepreneurs.

In other words, these are people, these are individuals who by hook and crook have either through networks and connections come across access to various technologies or have developed relationships with Chinese government or non-government individuals that have expressed interest, and then for primarily financial reasons have gone out to try and acquire the very technologies that are desired.

And I make this point--I would tell one story. There was a case in the Stanford University area of a woman who had been a student, who had been, because she was a PRC national had been charged with helping escort PRC delegations when they visited Stanford. In the course of those duties, had escorted and hosted a delegation from NORINCO, the Chinese ordnance manufacturer, and then on her initiative or perhaps a little bit of coaxing, she and her husband then began attending defense industrial equipment auctions in the California area, were able to acquire 15,000 artillery blade fuse cutters, and then based on that acquisition then contacted some of the people that they had been hosting as students during those delegation trips to Stanford University.

That to me is a more accurate model for understanding what's going on with Chinese economic espionage than one in which we have established front companies, trained agents using professional tradecraft to try and acquire, the kind of model we may have seen previously with the Russians and others.

Now, on the one hand, we see multiple redundant tasking in this model, and so this is both good news and bad news, to be clear. The good news is that they are not professionals; the bad news is that I would argue that the nature of that type of economic espionage and those patterns are very, very difficult for our system to track, which is trained to observe patterns of more professional tradecraft, and that a lot of what's going on with the Chinese side, in fact, goes underneath that radar, and I'll talk about that in a minute.

One thing that I would like to debunk if you will based on my personal observation is a monolithic model in which we envision the Chinese system as sort of some faceless person stroking a white Persian cat in their lap in their floating volcano island headquarters.

In my view, we project that monolith onto the Chinese system to cognitively cover our own lack of data. Instead, when you really get under the hood of many of these cases, you see bitter rivalry, you see multiple redundant tasking, you see individuals and companies being tasked to compete with one another to acquire the same technology.

In other words, inefficiencies in the way they do that potentially

raise their operational security profile to the point where you might actually notice what's going on. So when you get under the hood, you even find Chinese institutes and Chinese government entities competing with one another to acquire the same technologies, and so I would submit for your review that we shouldn't project that monolith onto the Chinese system.

But that what I'm describing is actually a more difficult situation. It's easier to understand a monolith. It's easier to track a monolith. It's easier to ascribe internal rationality to a monolith than the situation I'm describing.

And so we see a pattern of small companies, mom and pop companies, overseas Chinese organizations, dedicated to science and technology cooperation. This is largely the milieu of the U.S. scientist invited to China to speak at a conference and then gets hit at multiple levels by interlocutors seeking the answers to specific questions.

And finally, because of our open society, a fairly intense open source intelligence gathering effort directed at the defense technology information system, the national technology information centers, and so on and so forth.

My final point would be that I would attribute the success of Chinese economic espionage to date therefore as attributable not to their prowess but to our own internal problems. The primary challenge that I often see, and as a Chinese linguist and as someone who runs a team of Chinese linguists, it's the challenges of the Chinese language as China's first line of national defense, its first layer of encryption, thwarting our ability as a system to even get in and understand a lot of the activity that's going on.

Second are the well-known weaknesses of our export control system. In particular, this pressure from the Chinese side blaming the trade deficit on our high tech export controls, but also the weaknesses in that export control system in terms of being agile and nimble enough to keep up with the pace of technological change and to really correctly identify what is the state of the art.

I would also submit to you that our export control system is overly focused on the state of the art and doesn't apply a means-ends test to why the Chinese are requiring a specific piece of technology. There are pieces of technology, I would argue in the record, that the Chinese are trying to acquire that are 20, 25 years old that are mainstays of existing U.S. defense systems, but come nowhere close to being considered state-of-the-art, and yet a means-ends test would correctly identify those as critical gaps in the Chinese system.

Our legal system unfortunately in this area gets bound up very much on issues of intent, which means if you have a single piece of paper, a single e-mail, a single phone call from a Chinese actor, in

which they say, hey, we can't do this, that's illegal, that's exculpatory and therefore undermines the intent and therefore reduces the incentive for the AUSA in the case to want to pursue it.

In addition, we have the problem with Hong Kong, which was established as a separate customs entity during the handover for the Chinese for very sort of noble and pure reasons, but has now become a very troubling transshipment point for Chinese economic espionage, and because of its nature as a separate customs entity is not governed by the restrictions that we have on exports to China.

And then finally, as Mr. Smith mentioned, the comprehensive national security challenges we face in terms of cyber espionage, and here I think the problems are very known, both cyber espionage as a vehicle for espionage in and of itself but also as a vehicle for obtaining sensitive technology. And let me stop there.

Thank you.

PANEL III: Discussion, Questions and Answers

HEARING COCHAIR BROOKES: Thank you very much.

Commissioner Wortzel has to leave a little early so I'm going to turn to him first.

VICE CHAIRMAN WORTZEL: I want to thank both of you for your testimony.

I think you're right. Both of you talked about economic espionage and really there have been few espionage prosecutions, but a lot more for economic espionage or acting as a foreign agent. So I'd like both of you, if you could, to discuss what Congress might do to make it easier to pursue Chinese espionage here.

I'd also like your thoughts on whether we can infer state involvement by intelligence services from the type of cyber or human penetration and the information extracted?

Mr. Smith, you talked about reciprocity. It's been a long time since a diplomat or a military attaché was expelled from either country, but if we really stick to reciprocity, then we're going to lose some pretty good operators out in China because they'll do the same, and I would welcome your thoughts on that.

MR. SMITH: Thank you.

Let me start with the reciprocity issue. At this given time, we don't know, the State Department doesn't know, Chinese don't know, how many students they got in this country.

Now one of the lessons that you learn is-- there's an investigation that kind of demonstrates this to some degree--the Wu Bin investigation involved the fellow who was getting the night goggles down in Norfolk area. But what they did with him is that he

was something of an academic in the liberal arts area, but because of his stance on Tiananmen Square, something like this, essentially the MSS leaned on him and said, okay, they said what we're going to do is you have a choice: you can either go to the United States and set up a front company or you can go to jail.

And by the way, we're going to let your girlfriend go with you, and so they sweetened the pot, and sure enough--he said, well, I don't know anything about technology. They said that's not important. Go there. All right. And so essentially this is what I see happening with a lot of these Chinese students. This is where I talk about the reciprocity.

I think a lot of these Chinese students, and it goes back to my time when I used to run that program for the FBI, is that they were willing to sell their soul to the devil just to come to study in this country. So what you have, these are not trained intelligence officers.

But they are--and what actually the Chinese do, they kind of flood the market. They know that every one of these Chinese students, and that's both J-1s and F-1s, because you got to remember the Chinese completely control the visa process coming out of the embassies and the consulates there.

You have a harried consular officer who the only role that really a foreign service officer plays in that process is he signs the okay after the Foreign Service National tells him where to sign.

These people are normally very junior, probably the first or second assignment overseas. They probably don't even speak the language so they become totally dependent on these Foreign Service Nationals, and these Foreign Service Nationals wouldn't be working for the American Embassy if they didn't have some sort of accommodation with the intelligence service.

So what you end up with, these students, they actually control who comes out of China, and I will guarantee you that they, a large percentage of these people have reached some sort of accommodation with the Ministry of State Security. Well, what happens is not all of them are going to end up providing information. The Chinese know that, but a substantial number of them will.

One of the things that we discovered when I was still with the FBI, when the Chinese students first started coming over here, is that the Xerox paper bills for academic institutions went up dramatically when the students started showing up. Well, you can kind of tie two and two together and that sort of thing.

This is the reciprocity, though, Larry, that I'm thinking about. What do we have? 5,000 students studying in China? Well, maybe we ought to have, say, okay, we ought to work out some arrangement here.

Well, if you have 100,000 over here and we have 5,000 over there,

and by the way, they just can't go anywhere and study anything in China, maybe we should take a stance that we would make it a little bit closer. Maybe instead of having 100,000, maybe they should only have 50,000 here, come up with some number or something of that sort.

Same thing with traveling delegations. If you travel to China as a delegation or something like that, you're tightly controlled. Here they wander around the country almost without any escort at all from the U.S. government.

Another good example is you can't even--a Chinese national can't even walk up to an American Embassy in Beijing or the consulates in Shanghai or Shenyang, any place like this, because they have Chinese guards there. So even access to the American Embassy or something like that is tightly controlled.

Now I realize this would be rather draconian, but think what would happen if we suddenly put up a fence around the Chinese Embassy here on Connecticut Avenue, and we started taking names of who would go in there. This is the sort of thing that I'm talking about from reciprocity in it as well.

But there were some other areas, too, that--

VICE CHAIRMAN WORTZEL: Whether there's any better tools or more effective tools that Congress could legislate that would help pursue economic or other forms of espionage?

MR. SMITH: Okay. The espionage issue is terribly difficult because of the way the Chinese operate. They aren't going to be doing the dead drops under the bridges as you saw in the Robert Hanssen case or something like that. Most of the information that goes out of there is actually delivered by some other means into China itself.

For example, even if you go back and look at the Larry Chin case, and this is public knowledge, is that his handler never met him in the United States. He traveled to Toronto, there was a brush pass, he passed off the film, and this sort of thing like that as well.

So it's terribly difficult to make an espionage case, and from a traditional standpoint because you just don't have that piece of evidence, that document or something like this. Even in the Larry Chin case, the government didn't have it. It depended on a very crucial interview, and probably had he kept his mouth shut for another ten minutes, he'd have been home free. When he finally made the confession, he was not convicted because of the tangible evidence. He was convicted because of his own statements, that sort of thing.

So I think in many respects, Larry, it's going to be terribly difficult to prosecute true espionage cases with the Chinese. So that's why I think prosecutors, and correctly so, are resorting to other things like Foreign Agents Registration Act, the economic espionage related

issues and stuff like this.

DR. MULVENON: Commissioner Wortzel, I would only offer a couple of points to your questions. One on the congressional side. I think that the FBI in its China campaign, its dramatic and aggressive recruiting of more special agents on the China counterintelligence mission is definitely a step in the right direction. I would encourage Congress in that respect to continue to support the FBI's efforts in that area. That's a tough recruit, particularly if you're looking for people who are both clearable and who potentially have Chinese language capability. I know that from personal experience.

But in parallel also, the somewhat maligned intel analyst program within the Bureau is actually the place where you're more likely to find people with Chinese language capabilities who are building up an element of institutional memory and expertise and are not subject to the vagaries of the promotion patterns of being a special agent in the FBI where you may not stay on that mission for your entire career, and so those two programs in parallel have, in my view, gotten off to a good stop but require continued congressional support.

On the cyber side, you've asked, of course, the most difficult question, which is inferring state involvement which, of course, gets back to this issue of the cyber attribution problem, which is incredibly difficult.

I would say that not only is the attribution problem historically and technically difficult, but is now made probably worse by the publicity surrounding China origin intrusions in the U.S. systems because now every other adversary that we face understands that it's probably in their interests to route their computer network exploitation activities through the legions of unsecured Chinese servers in order to pin the tail on the Chinese donkey.

And so at the end of the day, I usually apply a who benefits "cui bono" criteria, which is I like to look at the specific material itself that was purloined and then ask myself who would benefit from acquisition to that material, and then come to a rough conclusion because I think if we continue to try and find some sort of a silver bullet on the technical side that will improve attribution, we'll just be basically spinning our wheels forever.

VICE CHAIRMAN WORTZEL: Thank you very much.

HEARING COCHAIR BROOKES: Thank you.

I have a couple questions here. I guess I'll get some of them and then perhaps some in the next round as well. I open this up to the panel.

So a reasonable question to ask is how many Chinese assets are currently in the United States? I realize it's going to be difficult to come up with a very specific number, but it's a reasonable question for

a congressional panel or Congress to ask. What are we talking about here?

MR. SMITH: Well, there was a defector in Australia, and he made a public statement that the MSS and the other intelligence agencies for China had a thousand people there.

Well, I don't think he was talking about a thousand badge-carrying MSS or MID/PLA officers, something like this. I think he, what he was thinking about was probably a lot of these students who were compromised into cooperating and the front companies and things of that nature.

I wouldn't have a clue. I don't, probably of the badge-carrying types, the true MSS officers and stuff like that, I don't know. Probably no more than 50 or so, and that's just a guess, and I haven't seen any numbers in years.

But on the other hand, I would think that you're talking about hundreds of people who potentially came over here who had reached some sort of accommodation with the MSS, in particular, before they were allowed to come out of there.

Now, you got to remember something. A lot of these people, they aren't activated right away. They come here and they say we will call you when we need you, and they do call them, and some of the people are here literally for years before they get the call.

This was one of the secondary revelations of the Chin investigation. We were somewhat surprised, and the other thing is that their station in life was not always what we expected. You would expect that people coming here would be academic or they have military expertise or something like that. Not the case at all. They may be a taxi driver, but they will have reached that sort of accommodation with the Chinese. It would have to be thousands probably total at this point.

HEARING COCHAIR BROOKES: Originally you said hundreds; now you're saying thousands. I realize you don't have a specific number.

MR. SMITH: Well, in sum. When you talk about a hundred, you can say a thousand, but 2,000 would be thousands or something of this amount.

HEARING COCHAIR BROOKES: Okay.

MR. SMITH: I realize this is a play on words, but if you think about that, how many students we've had come over here, how many have remained here since normalization--what--30 years or so of normalization now--is that a lot of these never go back. So they are at least potentially, they will have reached some sort of agreement with this. So I think it probably is in the low thousands.

HEARING COCHAIR BROOKES: Okay. Dr. Mulvenon, do you

have any thoughts on that at all?

DR. MULVENON: I think, Commissioner, it's impossible to know. I remember during the context of the Cox Commission going around the mulberry bush about 3,000 front companies; 5,000 front companies.

As someone who is looking pretty carefully, as Commissioner Fiedler was, at this issue, my instincts told me that the numbers were actually much, much lower. It was a useful heuristic to think about the total number of Chinese registered companies in the United States and then look for patterns among those companies, and that's what we were doing, trying to find common officers of those companies with companies in Hong Kong that we knew were associated with bad behavior and things like that.

But I think, I think, in a sense, we're sort of on a wild goose chase by trying to nail down those numbers. I would be much more content to have a better process picture of how this activity is carried out, to know what those patterns look like, to be able to spot those patterns, to train people on a systematic basis to look for those patterns, because I think the kinds of numbers we'd be talking about, even with Chinese registered companies in the United States, would simply overwhelm our ability from a resource perspective to even go after it. I think there are more efficient ways to do it.

HEARING COCHAIR BROOKES: Well, the reason I ask because obviously it's trying to figure out what sort of resources we should put towards it.

DR. MULVENON: Right. I mean I think--

HEARING COCHAIR BROOKES: If we're dealing with very small, limited number of assets, then that would help you to scope the type of resources you should put after this, but if we don't really know, that's something we probably should be trying to find out.

DR. MULVENON: I think, for instance, if you took the numbers from my testimony and said find me another country where you have 25 prosecuted cases involving somewhere between 50 to 100 people, find me another country in the last five years where we have those kinds of levels, I think it's fairly easy to prioritize where the resources should go for the Bureau.

HEARING COCHAIR BROOKES: Or the size of the resource, of course: is that the tip of the iceberg or is that the iceberg?

DR. MULVENON: Right.

HEARING COCHAIR BROOKES: That's the big question.
Commissioner Fiedler.

COMMISSIONER FIEDLER: Thank you.

Dr. Mulvenon, since you raised it and since none of us actually want to go back to the errors of the Cox report, is there any source in

the government--this is for either of you--that has a list of Chinese companies operating in the United States?

DR. MULVENON: I don't know of one, but I would say that the basis of my data and probably the smart, market-based base of the data for the government would be simply to use Dun & Bradstreet or LexisNexis because that is a data field in those databases. I think it would be a waste of our taxpayer money to reproduce what Dun & Bradstreet and LexisNexis have already done for commercial purposes.

COMMISSIONER FIEDLER: I might take issue with you on the citation on that. So, from a counterintelligence point of view, we don't even know what the universe is within the government?

MR. SMITH: At one point, the FBI had rough statistics on those sorts of things, as does Customs. I'm assuming that someone still has a list of those companies. I'm assuming.

COMMISSIONER FIEDLER: You are assuming.

MR. SMITH: Because, like I say, I've been retired for a number of years.

COMMISSIONER FIEDLER: I haven't found it yet actually, and I've asked a lot of witnesses this, and I don't think it's a classified issue. I just don't think it exists.

Secondarily, if you were to make a judgment, either of you, what produces the largest take for the Chinese? Cyber intrusions or human intelligence gathering operations? The most important take, forget largest.

MR. SMITH: I, and I'm not as familiar with cyber activities as perhaps the good doctor is, but my impression is if you look at the technology, that's pretty clearly been tied to HUMINT operations, that those have been very, very successful for them.

If you look at things like the neutron issue involving the Tiger Trap case involving Min Guo Bao and things of this nature, that as well, I think that's been very, very good, good for them.

DR. MULVENON: Commissioner Fiedler, could I beg your indulgence and answer the question perhaps a slightly different way?

COMMISSIONER FIEDLER: Yes.

DR. MULVENON: Which is to say that without knowledge about the scale of either, although I would point out that the prosecuted cases usually involve a fairly finite number of chips or night vision goggles or cameras or things along those lines, I'm more troubled by the cyber intrusions because they are acquiring plans, know-how, other blueprints, other kinds of information that would allow them to then develop the production capacity to produce their own equipment.

I think in many ways what we see from the Chinese side, particularly in defense electronics, is the illicit acquisition of the high-end military-specific technologies and components that the

Chinese information revolution is not capable of producing.

If the Chinese military needs advanced switches and routers for their fiber optic networks, they buy it from Huawei. But if they need a traveling wave tube or an analog to digital converter with a high temperature range or something like that, there is no commercial analog for that componentry in the Chinese economic revolution, and in my view, that's why they've been driven to try and steal that.

But when you steal it, then it relies on your ability to do reverse engineering as to whether you have any long-term benefit from it. Now, you could drop that into an existing system, you might even build it into your production of those systems, but in the back of your mind, you're always going to know there's a dependency there.

But if there is cyber, you're stealing in fact the ability and the know-how to be able to produce similar types of equipment ad nauseam and to innovate. To me, that's the more troubling acquisition.

COMMISSIONER FIEDLER: One other question. Are our counterintelligence resources, generally speaking, up to the task that we face?

MR. SMITH: I'm troubled at times by this issue, and let me give you a very brief example. Two or three years ago, I was up in New York, and I was actually involved in a court case, and I talked to the Chinese squad supervisor in New York, and I said something about the Larry Chin case, and she wasn't familiar with it. That bothered me.

One of the other things that I've seen is that there doesn't seem to be the same emphasis on the training of things like the language or the culture, the history of China, and things of that nature that I saw, that happened to me when I was getting involved with the business and stuff like this.

We took every course that we could. We went to State Department. We went to the Smithsonian, DIA, anything, any course that we could come up with to help us know more about China. I don't see that same commitment by the agent personnel that has been--or even the emphasis by the FBI on that thing, and I think this is--you have to understand the other side before you can really successfully attack it.

DR. MULVENON: I would largely agree. The people I've dealt with in the China counterintelligence world in the U.S. government, they understand the threat. They're aggressively pursuing it as best they can. It's uniformly been a positive experience for me dealing with them.

But the structural weakness in the system, and I keep coming back to this, and admittedly this is my bias as a Chinese linguist, is the language because so much of the interpretation of what's going on in a given situation is linguistically based.

There's a lot of ambiguity, particularly in the tradecraft, about communications and things like that, that someone who has had two, three years of Chinese is simply not going to be able to pick up the nuances that go in there.

At the same time, I offer the following caution because I have been involved in some of the limited training that's gone on, and I refer to one of Mulvenon's iron laws, which is an experience I've had from the Department of Defense, which is the value of any briefing on China is inversely proportional to the number of Sun Tzu quotes in the briefing.

So while I admit that Sun Tzu is an important cultural backdrop for understanding the Chinese, there is an extent to which because of the gaps in our understanding, that instead we use these cultural exceptionalist sort of stand-in models for a lack of data about what's actually going on in actual tradecraft and behavior and patterns, and so we can get a little too wrapped around the Sun Tzu axle, if you will, but it was instructive for me to read it, and I would point out that every Chinese university I ever studied in, every military officer I've ever spoken with, those sources, the 36 Stratagems in Sun Tzu are the lingua franca of that community.

It's the base strategic sort of canon for that community, and so much of how they talk to one another and think about problems is built out of that canon. So it's important for us to understand. It's just it shouldn't be the only thing.

COMMISSIONER FIEDLER: Interesting answer, but you didn't answer my question. Are we up to it or are we not?

DR. MULVENON: I would say we could still do more.

HEARING COCHAIR BROOKES: Thank you.

Commissioner Wessel.

COMMISSIONER WESSEL: Thank you, gentlemen, for being here.

Dr. Mulvenon, it's good to see you again here, and I understand the impediments for our analysis from lack of Chinese language skills since I have none, but I'd also say that there is so much open source that the dots are not being connected.

I'll give you an example, that in a recent meeting, some of our cyber security specialists were unaware that Huawei and Symantec had a joint venture in Hong Kong where we were being able to share certain network security issues, which should never have been allowed to happen, and our experts should have known about that to be able to use that information to enhance our security.

Let me ask two somewhat distinct questions. First is we heard earlier today in panels about the benefits of Chinese students coming here in the sense of understanding a free press, understanding that

their access to information at home is not as robust as maybe they would like or we would like.

And, Mr. Smith, you pointed out the converse side of that, which is there are a large number of students here who may be acting adverse to our interests.

What's the proper balance? I understand you said that reciprocity, but are we better off with having the students here in terms of what they bring back home in terms of U.S. values, democracy, freedom of the press, et cetera, are we losing more vis-a-vis the espionage issues? That's number one.

Number two and separate is we've seen a lot of very senior U.S. officials who when they leave government go into the private sector and advise through various entities. What risks do you think there are for those that have gone on to the payroll of the Chinese directly or indirectly? What kind of leakage do you think there is in terms of the benefit of the knowledge they've gained and how that may assist? I don't say they're sharing specific documents, but their overall knowledge base certainly has tremendous value.

Both questions if possible.

MR. SMITH: On the first issue involving Chinese students, and I certainly appreciate the benefits, and this is one of the things we discussed very early on when Chinese students were allowed to come to the United States, perhaps it's the disciplines themselves that should be scrutinized more closely. As of now, most of the people that are involved, civil rights issues and stuff like that, these are the people in the liberal arts disciplines and stuff like this so you could say, yes, you could have all the students you want to come to the United States to study journalism you want to, but you aren't going to be able to study some hard science.

Perhaps that's something that they should look at and from that standpoint. I would actually cut the number of them frankly, and by the way, I don't, I think that, I don't think that China has got the highest number of Chinese students here anymore. I think it's India or one of the other countries now.

COMMISSIONER WESSEL: Yes.

MR. SMITH: And certainly there's a very large number of Taiwanese in the country as well.

COMMISSIONER WESSEL: Just as a related question, from your experience, how much ability is there for our officials to track these students? Many, as I understand, come here and then change disciplines. Because you said we should have a discipline-oriented approach potentially. Will that system work?

MR. SMITH: Practically impossible. You can't keep up with all of them. First of all, there's a lot of the academic institutions resist

any sort of a FBI presence or anything like that dealing with those students. They talk about academic freedoms and certainly those are legitimate in that regard. So it's extraordinarily difficult.

One time, and I think I can safely say this, the total Chinese program, the number of agents that were assigned, and this was before we started having a larger influx of analysts, the total Chinese program probably consisted less, no more than 50 or 60 people for the FBI.

And that's when you had several hundred, if you look at all of the officials that were here on diplomatic passports, you look at the consulates and the U.N. mission and U.N., and what have you, not counting the students, delegations, stuff like this, you were absolutely overwhelmed with them. So it's practically impossible. You can't have a--like even a 20-to-one ratio between an agent and 20 individuals to look at. It goes much, much higher than that.

COMMISSIONER WESSEL: And as to the question of leakage, both your views and Dr. Mulvenon, leakage in terms of former senior U.S. officials who have information that might be valuable?

MR. SMITH: Any time that you're talking to someone, if you ask a question, you're providing information, and any time that there is a relationship of that sort, particularly if it's a paid relationship, there is going to be leakage and it's going to depend on the individual.

Frankly, I'm troubled by it, and I--not only involved with China but the whole government in general. I think there should be a moratorium of several years before you are allowed to go back and work in the area that you worked for in the government or something like that, not only a couple a years, what it is now, that sort of thing.

But there is no doubt that there will be leakage, and frankly I find it troublesome that you had former government employees who, they live good lives and good pensions and stuff like this from the government, and all of a sudden they go back and they are on the payroll of someone if they're not something that has an adversarial relationship. I find that troublesome.

COMMISSIONER WESSEL: Dr. Mulvenon.

DR. MULVENON: On the Chinese student issue, again, I'm going to dodge and oblique away from you. It's a truism, and the National Academy of Sciences and other people have noted this, that if we were simply to unilaterally restrict the access of foreign students to our hard sciences programs, most of them in the United States would collapse, and frankly that says more about us than it does about them in the sense that I've always decried the lack of resources and innovation that was going on in terms of our national innovation system.

I mean we are entirely dependent at this point in the hard sciences on foreign graduate students, foreign-born graduate students,

and I don't know what we need to do at the education level to change that pattern, but that does not bode well for the future innovation of the American economy and our infrastructure.

That said, I do agree that we could have better controls on that front. I am reminded, though, of the outcry from the university sector when the Patriot Act restrictions came out on monitoring foreign students in universities, and this was, from a university perspective, at the least defensible time in U.S. history to throw up roadblocks, and yet they did.

I'm also reminded of the activities in the Federal Register a number of years ago about deemed exports, about trying to change the deemed export regulations to reflect that if an individual was working in a graduate lab on a piece of technology that would have required a deemed export license if it was shipped abroad, that the same rules should apply within a graduate lab in a university in the United States, and of course Commerce was deluged by hundreds of letters from university presidents describing how this would cripple their programs.

I understand their point of view, but my point would be that the programs would not have been crippled if we had had a similar influx of U.S. citizen graduate students in those hard science programs. The university presidents were writing primarily from a perspective of their dependency on foreign students, and I think that that's the core root of the problem rather than from an enforcement perspective.

On the leakage issue, I have no opinion.

COMMISSIONER WESSEL: Thank you.

HEARING COCHAIR BROOKES: Thank you.

Chairman Bartholomew.

COMMISSIONER BARTHOLOMEW: Thank you very much. Thank you, gentlemen, for your testimony, and both of you for the service that you have provided in your different capacities.

Following up just very briefly on Commissioner Fiedler's question about cyber, I was thinking about how cyber could be changing the very nature and extent of traditional espionage in terms of information gathering so we're having one level of discussion about what is going on on the ground at the same time that what's going on on the ground could very well often be made obsolete by the fact that you don't need people in a place in order to gather the information, but time will tell on that.

I wondered if you could, particularly Dr. Mulvenon, you mentioned how on economic espionage, it's not professionals doing the espionage. It's often mom and pop operations, both that and U.S. scientists who are invited to speak at conferences, as a way to get access to information.

Can you talk a little bit about the tasking? Who is it? Who is determining what these mom and pop operations should be looking for? How are those assignments being given out? This Stanford student that you mentioned, the Stanford area student that you mentioned, I mean I suspect that they did not know that going to these auctions and buying these blades was something that they would just think up on their own. So where are the marching orders coming from?

DR. MULVENON: Well, and here there's an interesting change in the Chinese system with regard to defense industrial production and research facilities. In 1998, the central government in China largely cut these institutes and factories loose from state subsidies, and they were told you need to go and develop spinoff commercial things to be able to cover more of your costs. It was part of a general reform movement in 1998.

As a result, many of the numbered defense industrial institutes and factories associated with the main defense industrial sectors in China began proliferating a set of commercial companies associated with those institutes. Now, these are not front companies. There are a separate class of companies that I would correctly label front companies. These are genuine commercial concerns that are derivative of these. They are collocated with them. Often the way we find them is because we translate their street address and then we all, lo and behold, we discover that they're in the same walled compound as their institute or factory sponsor.

But those commercial companies, which have anodyne sounding names, that don't say No. 23 ordnance factory, are often the venue for contacting these companies for RFQs or, you know, for request for quote or request for bid on various things.

And in the Bridey [ph] case, for instance, the Stanford case, it was interactions with a commercial company associated with NORINCO, and so while nobody--they would have been horribly naive to not understand that they were dealing with the ordnance ministry, but they were clearly being contacted by entities that were associated with the delegations they had hosted.

And so, but the actual commercial transactions themselves are often as mundane as simply receiving a fax saying here is the shopping list of things that we're interested in with no clear direction as to where they're going to find them, and then relying on the natural entrepreneurship and aggressiveness of the people that they've contacted.

What I would highlight, however, Commissioner, is that often they're not the only people within the network that are being given this similar tasking, and that this is a distributed network in which there is redundant multiple tasking, and often it's who in the words of

Stonewall Jackson--"get there firstest with the mostest."

And so that's very different than a model in which you have a directed front company in which you've expended significant assets setting up cover for and then bringing in people under false pretenses who have professional tradecraft to run that, to run that.

COMMISSIONER BARTHOLOMEW: Dr. Mulvenon, that fax originates somewhere, and what I'm trying to understand is who is it who has their eye on the picture of what it is that needs to be acquired? I mean are these individual companies in China that are able to direct assets? We'll use "assets," for want of a better word here. Or where is this initiated?

DR. MULVENON: I think it's both bottom up and top down. I mean we know from open sources that there is a level of high-level state coordination on S&T procurement that goes on at the Beijing level, whether it's in the Ministry of Science and Technology, whether it's in the former COSTIND, which is now called SASTIND, under the Ministry of Industry and Informatization, whether it is derivative of the 863 Program, which itself was the result of high-level state coordination to identify key future technology gaps that China needed to push.

There is that centralized system that is very focused on identifying those kinds of gaps and directing resources towards them including the illegal technology acquisition from abroad, and we've acquired sources over the years that have been translated that described this process in some detail.

At the same time, there is innovation going on at the bottom level where people are for their own materialist interests trying to acquire things that they know would be valuable and then going to find customers for it at higher level, at higher echelon, and so I think both of those processes working at the same time, but in a much more distributed, diffuse way in execution than we would probably ascribe if we were simply describing a Chinese monolith.

COMMISSIONER BARTHOLOMEW: Thank you.

HEARING COCHAIR BROOKES: Commissioner Videnieks.

COMMISSIONER VIDENIEKS: My question was basically asked by Chairman Bartholomew. It was an identity question. Frequently, the government puts out a request for information, and then the results are used to put together the solicitations or other documents.

The question basically is who, which organizational component in PRC, accumulates this scattered or grain-of-sand type of technological information? Is there a specific centralized outfit?

DR. MULVENON: If you're talking about unclassified U.S. defense information, there are a number of organizations that are

easily identifiable, some of whom have offices here in the national capital region. Such, for instance, is the China Defense Science and Technology Information Center, which is subordinate to COSTIND and also to the General Armaments Department in various ways.

This is an organization whose sole organizational purview is the vacuuming up of large volumes of foreign unclassified defense information, and for an open society like ours with large numbers of technical publications and things like that, all you need to do is look frankly at the customer information of who is requesting microfiche from DTIC and NTIS and other organizations in the U.S. government that are charged with disseminating large volumes of microfiche of unclassified information to see those patterns, to see those flows.

Each of the defense industrial sectors in China, ordnance, aviation, aerospace, shipbuilding--I'm going to forget one--each of those have institutes and centers devoted towards the same kind of science and technology information centers, is what they're often called, and their role is to systematically subscribe to and collect the technical R&D journals in English that are associated with this, and we know this from a variety of sources, not the least of which is that when you look at Chinese language technical R&D journals in the defense area, very robust footnotes of U.S. technical R&D journals.

Now, I would submit to you that individual Chinese scientists who don't speak English are not themselves independently acquiring subscriptions to all these journals. That may be true, but much like our own system, it's much more efficient to have clearinghouses of these kinds of journals, and then there are journals that we have seen in the Chinese language journals in the footnotes that are clearly summaries of foreign technical R&D journals. In other words--

COMMISSIONER VIDENIEKS: May I? Your answer then is that there are several of these clearinghouses?

DR. MULVENON: Right.

COMMISSIONER VIDENIEKS: And they act more or less in a coordinated fashion or independently? That would be a quick question.

The other question to Mr. Smith is what should we recommend to Congress that we do in a free society?

MR. SMITH: I'm not as confident that there is that great a coordination back there. I just can't imagine that a professor from the Harbin Institute of Technology is coordinating at the same level as NORINCO or some business in Guangzhou. I think it's pretty fragmented.

Now they have a mechanism set up to coordinate this, but let me tell a quick story, and then let me get the answer to that as well, and it involves the front companies. I spent several days, two or three years ago, with an MSS officer who--this is after I retired--who is charged

with setting up a front company.

It was interesting about what one of the interesting characteristics of the front company is. The Chinese expect them to be self-sustaining. They pay their own way. It's unlike those that maybe the FBI, the CIA sets up where we just keep funneling money to them, and it's great difficulty at times sometimes showing that these are actually legitimate companies when they aren't really making any money.

The Chinese front companies have to pay their own way, and what's interesting about that, is that the Chinese really don't care how much money the individuals running that front company make themselves. This is one of the things that, for example, that happened in the Wu Bin case, and it happened with this MSS officer that I was spending this time with.

They don't really care how much money they make individually as long as they start funneling this information back to China. The other thing was that I found somewhat striking is the fact that they didn't really have specific targeting.

Now go back again to the Wu Bin case, he was given a list of technologies that they wanted. They told him to memorize them, and then they took the list back away from him. Well, it had 30 pieces of technology on the list, and the only thing he remembered is something like buy radar or something else, and he ended up getting in trouble for night vision goggles, that as well.

Same thing happened with my friend, the MSS officer. I said, "What did they tell you specifically?" He says, "Anything to do with the U.S. military." "What did you do?" He said, "I went to junkyards. I bought anything to do with U.S. military on it. I bundled it up and shipped it back there." I said, "Well, what happened back there?" He says, "Well," he says--and you got to remember the system in China is absolutely corrupt. So it goes back there, he gets this shipment of junk, and they say--I'll use this name—"Wang, is doing good." Well, see, Wang made his boss look good.

So he then reports it up to a higher level, and they say Wang's boss is looking good because Wang is really producing this thing, and it goes all the way up through the system. Everybody--and it's corrupt. It's junk, all they're getting, but the point was that they are sending this stuff back there to them. So that as well.

So this is, I think, how a lot of these front companies actually operate, and the Chinese, there again, they flood the market and eventually somebody is going to come up with that good piece of information, that good piece of technology.

COMMISSIONER VIDENIEKS: So at which point is it espionage? At which point is this information gathering for marketing

purposes? Would that depend on the organization which receives it, the information?

MR. SMITH: Is it espionage at that point? No.

COMMISSIONER VIDENIEKS: Whether it is or is not espionage?

MR. SMITH: It's probably not, almost certainly not, especially if they're getting it from junkyards. One of the interesting things about China in the language standpoint is the old business--and the doctor can speak to this much better than I--but there's no real phrase in Chinese involving intelligence gathering. The word "qing bao sou", kind of like information gathering, something like this, that is really what you see them doing more so than actually intelligence information. It's information gathering.

DR. MULVENON: In fact, Commissioner, when I'm in China, I often translate the title of my organization as the Center for Information Research and Analysis.

COMMISSIONER VIDENIEKS: Thank you.

HEARING COCHAIR BROOKES: Thank you.

Cochairman Reinsch.

HEARING COCHAIR REINSCH: Thank you.

I can't resist a comment or two, which will not surprise Dr. Mulvenon. I think your point on the students is well-taken. I just would comment that looking at the state of our current education system, which is something you alluded to, we cannot simultaneously be a world innovation leader and think that we're going to do it solely on the basis of American students.

Looking at it historically, the great strength of this country for 200 years has been immigration. It's been built on immigrants, certainly in my family, and I think that of most everybody here. I think that's where our future lies too.

I think people will tell you, most people will say, that if you look particularly at the students that are coming here to get advanced degrees or even undergraduate degrees, the benefits we accrue from them whether they stay here or they go back vastly outweigh the costs, which is not to say the costs are zero, which Mr. Smith alluded to, but I don't think there's anywhere near a balance here.

On the deemed export issue, Dr. Mulvenon, I remember and have heard very well the comments of the academics on that subject. What you haven't really noted I think from the other standpoint is the real problem with that has always been the cost/benefit ratio. The government was pouring a large amount of time and energy and resources into a process that rejected maybe one or two people a year, because they didn't have information really that was much more extensive than the information that was available when the visa was

granted in the first place, and these were mostly people who had visas and were trying to convert because they were leaving academia and getting a job.

There are better ways to deal with this problem and certainly more cost effective ones than to create this enormous process that ends up identifying maybe one person in a year.

So one of the things that I think has been lacking in this discourse in the past, and is still lacking, is any sense that this is a risk management problem. Most people approach this as a zero risk problem, and if you approach it as a zero risk problem, you can't possibly win.

If you approach it as a risk management problem, then you're going to put your resources where they'll do the most good, and you'll be able to accomplish something. This has been frankly one of my complaints about the FBI over the years. They never understood that.

Now let me ask a question having finished with the rant. For Dr. Mulvenon, you said an interesting thing way back. You alluded to Hong Kong, and I'd like to pursue that with you for just a moment. I certainly would agree that there is a theoretical risk with respect to Hong Kong. It's obvious, and you stated it.

I'm not aware of a lot of practical problems, and I'm well aware of the extent to which the Hong Kong government has gone to try to make sure that there aren't any problems. Has something happened in the last year that I don't know about?

DR. MULVENON: Sir, I would submit that it is a significant problem, and that it may not be reflected in the data you're seeing, but when the equipment is transferred to Hong Kong, there are therefore no restrictions on its transshipment to the mainland, and that a large percentage of the export control cases that I have seen have involved Hong Kong transshipment.

HEARING COCHAIR REINSCH: Okay. That's useful. I think I'd like to get more information about that. We'll do it offline.

DR. MULVENON: Maybe we could talk about that offline.

HEARING COCHAIR REINSCH: We'll do it. Yes, we'll do it as a sidebar.

Thank you.

HEARING COCHAIR BROOKES: Thank you.

Commissioner Shea.

COMMISSIONER SHEA: Thank you both.

I just want to follow up on a question that Chairman Bartholomew asked, and I think you, Dr. Mulvenon, responded to what I was thinking of asking you.

In a small way, I'd like you to sort of amplify, both of you, on it, this notion of entrepreneurial espionage. It seems like the notion of

people in the United States trying to get access to information that they think some sponsor in China might be interested in, it seems very similar to the patriotic hacker associations within China that just hack into U.S. sites, perhaps not state-sponsored in any way, but thinking that the information that they might gather would be useful to somebody.

Could you quantify this entrepreneurial espionage? Is it half of what's going on or to what degree are we talking here?

DR. MULVENON: I would just say, for instance, since 2004, as an example, we have a handful of what I would describe as pure espionage, directed at U.S. secrets with tradecraft and everything else, but 25 cases of this entrepreneurial espionage. And so there's basically a seven or eight to one ratio.

So I think it's the dominant form with the following caveat, which is we don't know what we don't know, in a "Rumsfeldian" sort of way, which is that I fear that most of the people that we have ensnared in these investigations are ones who are just too damn stupid to begin with, and my question is what have the smart people gotten away with that we don't know about? Because given the language barriers and everything else, it would be fairly easy to fly under the radar.

COMMISSIONER SHEA: Mr. Smith, do you have anything to add?

MR. SMITH: One of the things that 60 years of communism hasn't done for the Chinese people and that's dampened their entrepreneurial spirit. They're still interested in making money just like they're still interested in gambling. Some of these things that the communists say they're going to get rid of, well, they haven't.

From the standpoint of prosecution, this is where I think that--and perhaps it's not so much it's a legislative issue--is that from the standpoint that there should be a great deal of discussion on how they should approach these. I don't think it's necessary for the government to try to prove, for example, as they did in the Chi Mak case, that he was an intelligence operative.

The point was that he had stuff that shouldn't be leaving the country and he was leaving the country with it. Leave it at that. And I think there should be a greater emphasis, not only from the standpoint of prosecution, but also from the standpoint of the investigations themselves, to--particularly dealing with the Chinese, that espionage is a terribly difficult statute to prosecute, and it's a terribly difficult statute to investigate--take a step back and go with what you got.

And that's what I think you see is happening to a large degree with these 25 or so investigations. They would prefer to have espionage cases, but they just aren't there. And I'm not even sure that

they are there, much less the fact that it's a matter they just can't prove them.

COMMISSIONER SHEA: Okay. Thank you.

HEARING COCHAIR BROOKES: Commissioner Mulloy.

COMMISSIONER MULLOY: Thank you, Mr. Chairman. I want to thank the witnesses, both of you, for being here. Mr. Smith, I want to say special thanks to you for your service to our country in the FBI for many years.

MR. SMITH: Thank you.

COMMISSIONER MULLOY: I see we've talked about espionage here, and that they targeted technology. The Chinese have targeted technology as part of the espionage. That's what we've been talking about. But I see two ways in which the technology is moving out of this country without espionage at a very rapid pace.

Our ability, so much of our R&D is tied to the manufacturing sector of our economy. And the manufacturing sector of our economy is being outsourced due to, I think, some pretty sophisticated trade strategies being used, and when the manufacturing leaves, now the R&D is moving.

I went to a big research park right outside of Beijing and saw the seriousness of purpose with which the Chinese are trying to move up the technology ladder, and I think, Dr. Mulvenon, you talked about that, that they want to be an innovation society. They clearly talk about it.

So I see the trade strategy as being part of moving technology as an issue, and then the other thing I see is years ago, many of these Chinese students that came here stayed here. More and more they offer incentives to bring those students back, and because the Chinese economy is growing so rapidly, and ours is not, they're more inclined to do that.

I don't think Americans are stupid, and I think they can do science and technology. We used to do it back in the '50s. I remember when Sputnik went up, we were all going to school on Saturdays to learn math and science. Many of my friends went on to great careers in math and science.

They weren't ethnic people; they were American born, and they did all right. But I think so much has gone on in our state universities that it's easier to bring these foreign students in for some reason. Maybe they have people from the foreign country in charge of the research and then they bring in their own people. I don't know.

But I think there is something going on with regard to that, and just would you both comment on those two aspects of moving technology out of the country because our whole standard of living and our ability to have superior military is based on the fact that we're

more advanced in technology and science than other people?

Anyway, Mr. Smith and then Mr. Mulvenon.

MR. SMITH: One of the great difficulties in doing a damage assessment in an espionage investigation is what I like to talk about, the indirect access. Now, for example, in the Katrina Leung case, we can come up with a pretty good idea of what type of information she had access to by identifying that information that the agent handler had. It's initials on documents, case assignments, this sort of thing.

But what's extraordinarily difficult to come up with is the indirect access, the casual conversation he had with a colleague at a meeting, a file that he looked at on someone's desk that he wasn't supposed to, that wasn't really assigned to him, this sort of thing.

Same thing happens in the businesses. You know--what was it--three or four years ago--that the Chinese were allowed to purchase the telecommunications firm down in Carolina. Well, if they get access to that firm, they get access to not only the technologies there then but also the minds and the thoughts of the engineers and stuff like this. So there, again, it's hard to come up with exactly what they're coming up with.

I can tell you that if there's a factory built in China, regardless of the safeguards that you think are there, if you're going to have Chinese nationals in that factory, you're going to lose something. Without any hesitation, you're going to lose something, and that's just the price of doing business, I guess, and I think most U.S. businesses at this point have made the decision, well, it may be worth it. I'm not as convinced now as I was perhaps a few years ago that this is correct.

DR. MULVENON: Mr. Commissioner, I'm struggling to remember the exact citation, but someone sent me a study that was recently published that shows that 75 percent of the Chinese students that come to the U.S. are still staying here, and if I find it, I can send it to you.

COMMISSIONER MULLOY: Thank you. That would be helpful.

DR. MULVENON: I think the troubling dynamic that I've noticed in the trade relationship is that because of the demands of market access, because of the desire of so many multinationals from so many different countries to get into China, that that gives the Chinese government incredible amount of leverage. That many of the ministries that are now the regulators of individual sectors had spawned previously commercial companies which are now competitors and JV partners for those multinational companies coming in.

But what's been clear over the last five years is the coin of the realm to get into China, to get that market access, to get that JV relationship, has been to establish an R&D lab within China, and the

numbers vary, somewhere between 750 and 1,500 of these R&D labs.

In my experience talking to people who run these R&D labs, again as Agent Smith said, a cost of doing business, is that in almost all cases the students are routed through these labs and through these training courses, and that a very, very small percentage, if any, of those individuals actually are retained by the company that set up the R&D lab.

And so they're basically training areas for people to usually then go back to indigenous Chinese companies, and there is some frustration among multinational executives who have to deal with this situation because they know they're training people for their competition, but they also know that the establishment of that lab was a quid pro quo to get into the market, and that is all part of this, in my view, national innovation strategy on the Chinese side which says that there has to be this period where they aggressively and systematically try and acquire that kind of technology.

COMMISSIONER MULLOY: Thank you both. That was terrific to get that information on the record. Thank you.

HEARING COCHAIR BROOKES: Okay. Thank you.

I have another question. We'll be finishing up here in the next five minutes or so, but Mr. Smith, are potential assets developed in the United States?

MR. SMITH: Oh, of course.

HEARING COCHAIR BROOKES: Okay.

MR. SMITH: When you had a large influx of Chinese students, for example, I viewed them as a counterintelligence possibility and not so much as a counterintelligence problem.

HEARING COCHAIR BROOKES: So not all of them are recruited before being sent overseas?

MR. SMITH: Oh, yes, but what you do is you try to recruit those that have been reached through some sort of accommodation. That's really the idea behind--

HEARING COCHAIR BROOKES: But are there other assets that are recruited here in the United States for Chinese intelligence?

Who was doing that and how, what methods are they using to recruit people?

MR. SMITH: You mean from the U.S. side or from the other side?

HEARING COCHAIR BROOKES: Oh, whoever. Even if they were Chinese nationals or Americans, who is recruiting them and how are they recruiting them?

MR. SMITH: I'm a little bit unclear. Are you talking about--

HEARING COCHAIR BROOKES: I'm talking about the Chinese government.

MR. SMITH: The Chinese government. It seems to me that most of the cases where there were non-ethnic Chinese involved--the Ronald Montaperto case, for example, he was a volunteer. He became so enamored with them or something like this that he began to provide information and something of that sort as well.

But what I think they do, and what I know they do, is that they will find those people that have for whatever reason a strong cultural identity, the family ties back there or something like this, and you got to remember, this is not a hard pitch recruitment type thing. These people are never given the tradecraft and things like that. The only thing they want for them is to just establish a relationship.

It goes back to this business I talked about very early in this hearing, is that they don't look at it as a four-year cycle and this sort of thing. They lay the groundwork for years and years in advance for some sort of cooperation. At some point, they will expedite a visa, they will do something, they will do these favors. They'll invite them to the consulate, Chinese New Year party, but at some point, they may ask a favor.

They escalate that favor, this sort of thing, and that's how that process takes place. Really speaking, people don't even realize they're being recruited.

HEARING COCHAIR BROOKES: Thank you.

Chairman Bartholomew.

COMMISSIONER BARTHOLOMEW: Thank you.

I want to go back again, Dr. Mulvenon, in particular, the issue of economic espionage, and my question might not be as clear as it should be because my brain is not as clear as it should be on these things, but there has been a debate on and off or some discussion on and off within our own intelligence community about--we don't use our intelligence assets for economic espionage, in part, of course, because who would decide which companies would be the beneficiaries of whatever information was gathered and how would that determination happen.

You mentioned state-owned companies and spinoffs of state-owned companies, some of whom are competitors with each other. Who is it who is determining who gets access or what the economic espionage activities are, these clearinghouses, for example? If massive amounts of information is being sucked up, is the information in those clearinghouses available to anybody in the Chinese business world who is interested in getting access to what's been gathered?

DR. MULVENON: Well, Commissioner, I would say it depends on the source, but, for instance, just to give you a specific example, an organization like the Chinese Defense Science and Technology Information Center, which publishes a large amount of material in

Chinese that is derivative of the material that they collect from abroad, some of those journals that they publish are openly available. You can go to a military bookstore in Beijing and walk in and buy their journal or things along those lines.

But they also then for a variety of reasons, sometimes not pushed by espionage, but also by a desire to obfuscate the fact that they've committed some sort of intellectual property rights violation, the category, for instance, of *neibu* publications in China. A significant number of publications that are *neibu*, in other words, internal distribution only, to Chinese citizens, are disguising the fact that they are, in fact, illegal copies of copyrighted Western and U.S. material, and so, for instance, you can walk into a Chinese military bookstore and see the translation series of all of our joint doctrine publications.

All of those were illegally copied. All of those were translated in ways where they should have gotten royalties or books that are published by people at NDU and other places, where they're just simply violating the intellectual property.

So there's a certain classification that those things are distributed through, but those kinds of organizations are the ones that acquire and translate them, and it's quite obvious to me from harvesting a lot of this material that the numbers of translators that they have working on doing this compared with the numbers of books that our own system translates every year is just orders of magnitude different.

It just gives you a sense of the scale of the operation. So there is generalized access, I think, to a lot of this material, particularly the open source based material, and if you go to specialized bookstores, S&T bookstores, other things, you'll find an awful lot of this material that's openly available for distribution, and there's a whole gray economy, if you will, very similar to the DVD pirating and the CD pirating and everything else, but in this case it's S&T pirating, if you will, of this kind of material.

COMMISSIONER BARTHOLOMEW: Could a company like Huawei, just hypothetical, decide that it wants access to a certain kind of research that it believes is being done by an American competitor, an American company, could somebody at Huawei go somewhere within the Chinese government to request assistance in getting access to certain kinds of information?

DR. MULVENON: A company like Huawei, which I've spent a lot of years studying, is a very special organism, but they work very closely, for instance, in collaborative research, and there is open source evidence of collaborated co-written articles between Huawei researchers and researchers from numbered defense industry research institutes, for instance.

So they're clearly operating in that world in which they would be able to tap into the kind of open source derived intelligence of U.S. and other S&T research as part of being in that world.

COMMISSIONER BARTHOLOMEW: I'm asking you to go beyond the open source derived information and go other sources.

DR. MULVENON: Huawei may not be the best example for that then because most of, if not all of, what they produce is commercially analogous routers and switches. Huawei does not produce equipment that we would regard as governed under munitions lists or export regulations, and so there would be no reason for Huawei researchers in that context to want to acquire that kind of information.

Now, you could instead look at an organization that is involved in missile production or things along those lines where they would want to have information about specific seekers or something like that.

Because they are in the defense industrial system; therefore, they have all the purview in the world, particularly if they're working on a program that is designated by the General Armaments Department or someone else as part of those programs.

We know from their RDT&E process that foreign intelligence collection of defense S&T information is a key component of that process, and so it's integrated in that sense, much better integrated than, I would argue, than even in our own system, where my personal experience has been U.S. defense industrial companies not having a terribly good understanding of even what our own intelligence record is about foreign S&T developments.

COMMISSIONER BARTHOLOMEW: Okay. Thank you.

HEARING COCHAIR BROOKES: Thank you. Thank you, Mr. Smith, Dr. Mulvenon.

I'll conclude this panel. We'll begin again at 3:00 p.m.

[Whereupon, a short recess was taken.]

PANEL IV: CHINA'S CYBER ESPIONAGE DIRECTED AGAINST THE UNITED STATES

HEARING COCHAIR BROOKES: Good afternoon. Welcome. Welcome back. We're going to convene Panel IV today, which is "China's Cyber Espionage Directed Against the United States."

We're pleased to be joined by two panelists: Mr. Coleman; M. Rohozinski. Mr. Coleman is a long-time security technology executive with an extensive background in business operation technology. He has frequently been interviewed and quoted in diverse publications such as Business Week, Washington Technology Review, USA Today.

He also maintains a blog at the Web site DefenseTech.org that focuses on covering incidents and developments related to cyber

warfare.

Mr. Rohozinski is a Principal with the SecDev Group and the former Director of the Advanced Network Research Group, Cambridge Security Programme.

He is also a founder and Principal Investigator of the OpenNet Initiative where he directs the works of ONI researchers in the Middle East and former Soviet Union. He's also co-editor of ONI's global comparative study of network surveillance and censorship in 45 countries.

In cooperation with the researchers from ONI and the University of Toronto Citizens Lab, Mr. Rohozinski was the author of the March 2009 report "Tracking GhostNet: Investigating a Cyber Espionage Network." This report details a vast electronic spying operation that has infiltrated hundreds of government and private offices around the world including those of the Dalai Lama.

Mr. Coleman, if you'd start. If you'd keep your testimony to seven to ten minutes, that will allow a maximum time for questions and answers.

Please proceed.

STATEMENT OF KEVIN G. COLEMAN, SENIOR FELLOW TECHNOLYTICS, MCMURRAY, PENNSYLVANIA

MR. COLEMAN: Thank you.

First of all, I really appreciate the opportunity to address the Commission on such a critical issue to our national economy and our national security.

Every computer that is out there is a potential cyber weapon, waiting to be loaded and used by criminals, by terrorists or by rogue nation states, and until we accept that preface, we will not have the security necessary to defend our nation or our businesses.

In our report, we talked about a study that was just done. In preparation for this, I asked Solutionary, an organization that we deal with for a number of years to pull some numbers for us, and while cyber attacks is probably the most ill-defined term you're going to find, we opened it up and said just tell us about acts of cyber aggression, somebody doing something to the system they shouldn't be doing, such as reconnaissance.

They were able to go back for the entire first quarter and pull the numbers for us, and in the month of March, their customer base, which is nonmilitary, non-major government entities that they work with on

security and monitor their firewalls and such, experienced 128 acts of cyber aggression per minute from China. That's 4.6 times higher than the next closest nation.

Those attacks all came from IP addresses in China. Now who's behind that? We don't know. And we will be very lucky to ever get to a point where we can actually do that investigation because, quite frankly, it requires international cooperation and some type of legislation or regulations that mandate transparency and openness to conduct these investigations, to find out who the parties are behind these.

It could be a rogue nation state. It could be a terrorist group. What's interesting is--we actually covered this on the Cyber Warfare blog at DefenseTech.org--Hezbollah issued a press release about the formation of their cyber unit. Now, I'm not in the intelligence and defense community, but I missed the whole transition when terrorist groups start doing press releases about expansions.

This is just unprecedented, the amount of organizations that are flocking to cyber. Does anybody know what a B-1 Stealth bomber costs? It's about \$1.5 billion. Anybody know what a cyber weapon costs? You can get it on eBay for about \$30.

There was an interesting e-mail I got that said there will be an organizational DDOS, a distributed denial of service, attack against any web site you want for \$500.

This is a commercial enterprise, a criminal enterprise, that's working on this stuff as well as rogue nation states and militaries. You can't distinguish between them. There's a blur between the commercial side and the business side and the individual and the defense side. We can't separate that out.

In fact, there's a graphic that we use in our presentations and briefings that show all these culminating in what's called a cyber threat, and you can't analyze who's behind it and where the threat really lies until we get to that next level of cooperation and investigation.

In preparing for this, I tried to look at this and figure out how we could present eight to ten years of analysis that we've been working on since my days at Netscape without coming across as an alarmist, but the numbers speak for themselves.

How many of us would accept at our home, somebody walking around trying to open a window to our house? That keeps going on day after day after day and trying each door to make sure it's closed and it's locked. That's cyber reconnaissance. That's the scans and the probes.

How many organizations do you think that would accept day after day after day somebody walking into their offices, opening up a

file cabinet and taking hundreds of files and walking out the door? After about the second one, you probably have guards there and police and there would be some offensive action taken to stop that.

Why is it that we turn a blind eye when it's electronic but, boy, if it's a physical file that gets stolen, that's a whole different issue?

I think I'll end there and I look forward to your questions.

Thank you.

[The statement follows:]

**PREPARED STATEMENT OF MR. KEVIN G. COLEMAN, SENIOR
FELLOW, TECHNOLYTICS, MCMURRAY, PENNSYLVANIA**

2009

The U.S. – China Economic and Security Review Commission

Opening Statement

of

Kevin G. Coleman, Senior Fellow at Technolytics

April 30th, 2009

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The Technolytics Institute (TTI) has an international reputation for excellence in cyber security, cyber warfare and cyber terrorism that extends over the last decade. This program has included past and present thought leaders within the fields of computer hardware, computer software, networking and internet technology and supportive disciplines. TTI has sponsored and funded ground breaking research that has helped define the field of cyber aggression and continues to be at the forefront of investigation with our proprietary sources and methodologies.



U.S.-China Economic and Security Review Commission

- About:** The Commission was created on October 30, 2000 by the Floyd D. Spence National Defense Authorization Act for 2001 § 1238, Pub. L. No. 106-398, 114 STAT. 1654A-334 (2000) (codified at 22 U.S.C. § 7002 (2001), as amended by the Consolidated Appropriations Act, 2008 (regarding changing the annual report due date from June to December), the Treasury and General Government Appropriations Act for 2002 § 645 (regarding employment status of staff) & § 648 Pub.L. No. 107-67, 115 STAT. 514 (Nov. 12, 2001); as amended by Division P of the "Consolidated Appropriations Resolution, 2003," Pub L. No. 108-7 (Feb. 20, 2003) (regarding Commission name change, terms of Commissioners, and responsibilities of Commission); as amended by Pub.L. No. 109-108 (enacted Nov. 22, 2005) (regarding responsibilities of Commission and applicability of FACA).
- Purpose:** To monitor, investigate, and submit to Congress an annual report on the national security implications of the bilateral trade and economic relationship between the United States and the People's Republic of China, and to provide recommendations, where appropriate, to Congress for legislative and administrative action. Public Law 109-108 directs the Commission to focus its work and study on the following eight areas: proliferation practices, economic transfers, energy, U.S. capital markets, regional economic and security impacts, U.S.-China bilateral programs, WTO compliance, and the implications of restrictions on speech and access to information in the People's Republic of China.
- Hearing:** "China's Propaganda and Influence Operations, Its Intelligence Activities that Target the United States and the Resulting Impacts on U.S. National Security"
- Co-Chairs:** Commissioner William Reinsch and Commissioner Peter Brookes
- Date:** Thursday, April 30th, 2009
- Location:** Room 485, Russell Senate Office Building
Delaware and Constitution Avenues, NE
Washington, DC 20510
- Panel V:** China's Cyber Espionage Directed against the United States

This document provides a discussion of the employment of computer network exploitation by PRC state or state-affiliated entities to obtain information from the U.S. government, contractors, and industrial computer networks.

OPENING STATEMENT

It is both an honor and a privilege to be here today and address such a critical issue that is central to the national security interests of the United States. During the later stages of my tenure as Chief Strategist of Netscape, the company that pioneered the commercialization of the Internet, I became awakened to the darker side of what we were creating. From that point on I began my research and analysis efforts in the areas of cyber security, cyber espionage, cyber terrorism and cyber warfare which continues to this day. China's military strategists view our dependence on space assets and information technology as "soft ribs" and a strategic weakness. That begs the question –what are they basing their view on?

Less than a week ago I was to be face to face with my Chinese counterparts or cyber adversaries if you will, that I have researched and analyzed for years. The Chinese representatives included Mr. Hou Yinming, Delegation Leader and Former Director of the prestigious Zhang Ya Da Electronic Research Center, Major General Wang Baocun, PLA (ret), Professor Wang Xiangsui, Director of the Beijing University of Aeronautics & Astronautics Center for Strategic Studies and co-author of "Unrestricted Warfare" and finally Mr. Shen Weiguang, referred to as "the father of China's information warfare." At the last minute, only one Chinese panelist was allowed. The others were denied permission to attend by their government bosses. Clearly, they were concerned about the opposing panelists and there may have been other considerations as well. I might add timing was bad for them – given the disclosure of their scanning of the power grid and the discovery of a cyber spying network in 103 countries.

I'd like to start by discussing current observations before moving to ongoing initiatives. For far too long, cyber attacks, cyber terrorism and cyber warfare have been perceived as too complex an issue and a risk that could not be managed. Many others believe that until we experience the massive disruption that will surely follow a successful cyber attack, we do not possess the intestinal fortitude to take the actions necessary to help mitigate this risk. Another contingent believes reports of these threats are overblown and need not be addressed. It is my belief that this threat is real and we must take a proactive posture on acts of cyber aggression and espionage. For over two decades, China has been attempting to do what the Soviet Union never accomplished; covertly acquire western technology, then use it to move ahead of the west. I offer the following three observations that I feel are critical when discussing acts of cyber aggression and espionage.

1. Cyber espionage is a serious and evolving threat that demands immediate attention. In a report authored by Cambridge University it said that sophisticated computer attacks have been "devastatingly effective" and that "few organizations, outside the defense and intelligence sector, could withstand such an attack." We have all heard the comments and warnings from Dennis C. Blair - Director of National Intelligence, General Kevin Chilton - Commander of U.S. Strategic Command, MI5 – the Intelligence Service in the United Kingdom and many others throughout the world have even warned of successful cyber espionage activities against hardened systems that are said to have been traced to China. Perhaps the most troubling acknowledgement came when the

Wall Street Journal broke the story about the Chinese and Russians conducting cyber intelligence reconnaissance and mapping the nation's electrical power grid.

There are other reports of malicious code being found in the computer systems of oil and gas distributors, telecommunications companies, financial services industries and other pieces of our infrastructure. In February of this year I warned of acts of cyber terrorism against our water treatment and distribution systems in my presentation at the United Nations. Former CIA operative Robert Baer has publically stated that the "foreign intelligence service has been probing our computers, our defense computers, our defense contractors, our power grids, and the telephone system. ... I just came from a speech at the National Defense University and they were hit by the Chinese trying to get into their systems." What will it take before we realize the serious nature of these acts of espionage and again I must ask – What constitutes an act of cyber war? I asked that question a long time ago, former DHS Secretary Chertoff asked that question again in November of 2008 and we still do not have an answer!

2. At the 10th National People's Congress in 2003, the Chinese army announced the creation of "information warfare units." General Dai Qingmin said internet attacks would run in advance of any military operation to cripple enemies. Clearly cyber intelligence is a critical component of China's military arsenal. Cyber espionage officially arrived on Capitol Hill when two Republican congressmen, Rep. Frank Wolf of Virginia and Rep. Christopher Smith of New Jersey, went public with the news that in 2006 and 2007 their office computer networks had been breached by Chinese hackers. And also when Commerce Secretary Carlos Gutierrez, who was in China on a trip with a U.S. trade delegation last December, had his laptop slurped by Chinese cyber operatives. Not much happened after those two events. It was seen as just two of the many covert acts that take place in networks that connect the billions of computers and related devices globally. Perhaps the recent discovery of a vast Chinese cyber espionage network (code named GhostNet) that penetrated 103 countries, infected nearly 1,300 computers, and continued to infect at least a dozen new computers every week, will provide the wake-up call. I ask Solutionary, a security advisory client of ours and top ranked managed security services provider (MSSP) to pull some data about acts of cyber aggression that were tied to China. In March of this year, their security operations center (SOC) identified 128 acts of cyber aggression against their clients every minute that were tracked back to IP addresses in China. These acts should serve as a warning that clearly indicates just how far along China's cyber intelligence collection capabilities are.

3. Hardware is just as susceptible as software is to hackers through the inclusion of malicious logic; and the consequences of such an attack could be serious! One year ago this month, I wrote on a blog site (DefenseTech's Cyber-Warfare) about the growing number of concerns over backdoors and malicious code or circuitry hidden inside of counterfeit hardware and software -- all the way down to the BIOS and instruction set inside of integrated circuit chips. Last month we saw a flurry of articles about vulnerability in the BIOS of microprocessors that could be exploited to gain control over the computer. Hidden malicious circuits provide an attacker with a stealthy attack vector.

Commercial suppliers are increasingly moving the design, manufacturing, and testing stages of Integrated Circuit (IC) production to a diverse set of countries, which is making the securing of the IC supply chain infeasible. Together, commercial off-the-shelf (COTS) procurement and global production lead to an increasing risk of covert hardware/firmware based cyber attacks.

The extraordinary effort required to uncover such high-tech covert acts combined with the massive number of chips we would have to test and validate from a circuitry and microcode perspective, as well as the need to scan through tens of millions of lines of code and validate each software instance on billions of devices come together to make ensuring the integrity of our systems nearly impossible. Security must be designed and built in, not tested for after the fact. In support of that statement, researchers at the University of Illinois at Urbana-Champaign demonstrated how they altered a computer chip to grant attackers backdoor access to a computer. This is not the casual attacker! The level of effort would make this a tool for intelligence services of nation states.

If we are to ensure the integrity of our critical systems and information infrastructure, status quo is not good enough. Many organizations do not have the technical capabilities to evaluate the threat of cyber espionage or the budget to implement the advanced defensive measures needed to protect their information assets. You would think that the fact that IP and data theft cost businesses an estimated \$1 trillion in 2008 would be a call to action. However, at this point the call to action has been unanswered. Based on the sum of my experience, research and our analysis I would offer the following three suggestions to help mitigate the risks associated with acts of cyber aggression and espionage. Given this is a public hearing, I will leave my recommendations vague as not to risk any compromise to the security these measures could provide.

1. We need to examine in detail and further quantify the risk that the global supply of components, sub-assemblies, assemblies, sub-systems and systems pose to the integrity of our critical information infrastructure and our highly computerized military. It would be extremely difficult for the United States to create the computer and related equipment necessary to build and support our critical information infrastructure and our technologically advanced military. If we are not going to build everything we need here at home, then we need to advance the current testing and validation tools and techniques as well as our system covert compromise monitoring and detection capabilities. Refer to our report - Cyber Threat Analysis Report on the Global Supply Chain National Security Issues.
2. We need to take any and all actions necessary to ensure our military has access to a continuing supply of new offensive and defensive cyber capabilities that are required and will continue to be required to defend our nation. This is not a one-time investment. Continuous investment will be necessary to respond to the ever changing global supply of computer technology. Chinese authors believe the United States already is carrying out offensive cyber espionage and exploitation against China. China therefore must protect its own assets first in order to preserve the capability to go on the offensive. While this is a highly unpopular statement, WE ARE IN THE EARLY STAGES OF A CYBER ARMS RACE AND NEED TO RESPOND ACCORDINGLY!

This race was intensified when China created Kylin, their own hardened server operating system and began to convert their systems back in 2007. This action also made our offensive cyber capabilities ineffective against them given the cyber weapons were designed to be used against Linux, UNIX and Windows. Refer to our report - RED SOS.

3. Cloaking capabilities, pass-through servers, compromise web sites and remotely controlled zombie computers make tracking and identifying the source of attacks and those behind them an extremely difficult task. We need to develop and advance the concept of Digital DNA. This concept catalogs the characteristic signatures associated with the cyber attack artifacts (code). In addition to these technical capabilities, we need to establish a framework for international cooperation for the investigation of cyber attack.

In Conclusion

We top the global chart of military spending, with China and Russia ranking second and third. China's strategists believe the United States is dependent on information technology and that this dependency constitutes an exploitable weakness. There are reasons to believe that China and Russia's militaries are collaborating and cyber warfare is one area that not only lends itself to remote collaboration, but there is soft and medium intelligence that this has and is occurring. Last year Col. Gary McAlum, chief of staff of the command's Joint Task Force for Global Network Operations at U.S. Strategic Command, quoted approvingly from a new report Technolytics had produced saying, "China aims to achieve global electronic dominance by 2050." This conclusion was drawn prior to the massive decline in the U.S. economy. As the U.S. funding for research and development has slowed substantially, China's has increased. We are in the process of updating the report referenced by Col. McAlum and at this time it appears the new projected date for China's goal of electronic dominance is in the late 2020s or early 2030s. They will simply be able to outspend the United States and the rest of the world much as we outspent the Soviet Union in the cold war.

At this time, the United States is the most technologically sophisticated country in the world. It is that distinction that makes acts of cyber aggression so dangerous. It is critical to our nation's future to take any and all actions necessary to ensure the integrity of our critical information infrastructure and our sensitive systems. I struggled with the best way to summarize over a decade of learning and the best way to communicate how real the threat of cyber aggression is, as well as the severity of these types of threats without sounding like an alarmist. The nature of this threat is such that this is not a one-time fix. The continued advancements of cyber attack techniques coupled with the rapid evolution of cyber weaponry requires continuous vigilance and the real-time creation of innovative defensive mechanisms. China is laser-focused on dual-use technology that caters to military and public use at the same time. President Hu Jintao has promised to "blaze a path of development with Chinese characteristics featuring military and civilian integration." The USCC 2008 report stated that "The U.S. government has not established any effective policies or mechanisms at the federal level to retain research and development facilities within its borders." I believe what I have presented here is the result of that shortcoming. The issue that China is behind

acts of cyber aggression against the United States is not the most concerning. It is the fact that we currently do not know how extensive the problem of cyber espionage is today and where this will lead to tomorrow!

Thank you for the opportunity to provide my perspective on the many challenges facing our nation from acts of cyber aggression. In doing so, I tried to be mindful that this administration has only been in place for a few months and new or changing policies surrounding cyber security will likely arise in coming months. I look forward to answering your questions and working with you in the future.

Appendix A Question from USCC

Q. As best as can be determined from unclassified sources, what is the extent of computer hacking and computer network exploitation (CNE) that originates in China and is directed against the systems of the U.S. government and/or U.S. firms? Do you have personal experience of cyber espionage activity that you could discuss?

The accurate response to this question is WE DON'T REALLY KNOW! While there have been reports, some highly publicized, a vast quantity of these are not officially reported. A former US special agent with over 20 years of service stated he saw over 100,000 systems completely compromised and hundreds of thousands of files infiltrated." One study suggests that open acknowledgement of a breach results in between 1% and 5% decline in stock price for a corporation. That in and of itself is one reason why many of these events are not reported. One troubling attack was when hackers were able to glean the sensitive information of up to 12,000 visitors to the Oak Ridge National Laboratory. In a recent conversation about this and other cyber attacks with Gary Clayton, CEO of Privacy Compliance Group, he stated "Recent reports from Australia, Canada and the United States regarding the coordinated efforts of the Chinese to target key infrastructure, throw into sharp focus the necessity for better coordination among the government, industry and individuals to protect our infrastructure and our personally identifiable information. Today, the Chinese are targeting the Pentagon and the Dalai Lama. Tomorrow, the targets will be ordinary citizens, their personal data and the businesses upon which we rely. Unfortunately, most Americans are simply unprepared for the chaos and financial disaster that such attacks will cause." We need to address security awareness!

Q. Who/what are the entities in China involved in cyber espionage? What evidence, if any, exists to link such activity to Chinese state and/or state-sponsored entities? What are the major Chinese institutions involved in the development of Chinese cyber espionage capabilities?

The PLA has cyber warfare capabilities that in my opinion equal that of the United States and Russia. This is a three horse race (U.S. plus China plus Russia) and it is a dead heat. While at Netscape I became aware that China had a group that reviewed, monitored and filtered content based on guidelines set by the Chinese government. I have posted on my cyber warfare blog that this group has possibly been redeployed as a cyber militia. I also worked with U.S. Strategic Command's working group on cyber militias. In addition, the National University of China has Defense Technology advanced programs in place and is the strategic advisor to the PLA on Cyber Warfare. The Ministry of Science and Technology (MOST) is the lead organization in

defining science and technology plans and policies, drafting related laws, regulations and department rules, and guaranteeing the implementation for China. Part of their initiatives deal directly with cyber capabilities.

Q. What are the primary targets of such hacking and CNE activities? What government, infrastructure, economic, and scientific institutions and/or interests are being targeted by such activity? What are the implications for U.S. national security and economic competitiveness resulting from the loss of data and intellectual property in these areas?

I struggle to identify any computer that is not a target or potential target for cyber attack. Individuals are attacked for personal information and their computers become an unwilling participant in a botnet. A bot is a type of malicious software which allows an attacker to gain control over the affected computer. The affected computer is then referred to as a zombie because it is not under the complete control of the owner/user. A botnet is a collection of zombie computers under the control of the attacker. Corporate computers are attacked for Intellectual Property and customer lists. One study I saw suggests that around 80 percent of an organization's value now rests in its information. The Director of National Intelligence reported before Congress that Intellectual Property and data theft in 2008 totaled \$1 Trillion Dollars. It is all tied together.

The ability for foreign companies to advantageously compete against U.S. companies through cyber espionage impact our economy and our ability to support research and development and investment in defending our nation. Critical infrastructure control computers are compromised and mapped for possible attacks by terrorist groups or rogue nation states. A computer is a cyber weapon waiting to be loaded and used. Based on over a decade of work in their area without legislative standards for computer and systems security, our national security is at great risk and will remain so!

Q. Can you identify and explicate past case studies of PRC cyber espionage that would serve to illuminate Chinese intelligence operations within the United States?

Just look in the recent press and you will find plenty of examples. I was contacted by a security consulting company for advice when they uncovered a bot attached to an Oracle data base of a U.S. Company. Based on the information I was provided, the bot was said to have collected what I would categorize as competitive information and send it to an IP address in China. I ask Solutionary, a top ranked managed security services provider (MSSP) to pull some data about acts of cyber aggression against their clients that were tied to China. Their security operations center (SOC) on average, identified 128 acts of cyber aggression per minute that were traced back to IP addresses in China.

Q. Are you able to identify particular U.S. vulnerabilities (networks, infrastructure, etc.) that you believe need to be addressed? Are there any practices or policies that you could recommend to the U.S. Government to improve cyber security?

With the continuous discovery of vulnerabilities, the opportunity to compromise systems is always present. [April 14, 2009 \(Computerworld\) Microsoft today released eight security updates that patch 23 vulnerabilities in Windows, Internet Explorer, Excel and other software in the company's portfolio -- a collection of fixes one researcher called "insane."](#) You can prove a computer has been hacked and compromised. It is nearly impossible to prove a computer has not been compromised. We do not know how bad the problem is because many organizations do not disclose these security events. Mandatory reporting along with a classification of event type is required to properly track these malicious attacks and see if our preventative measures are working.

About Technolytics

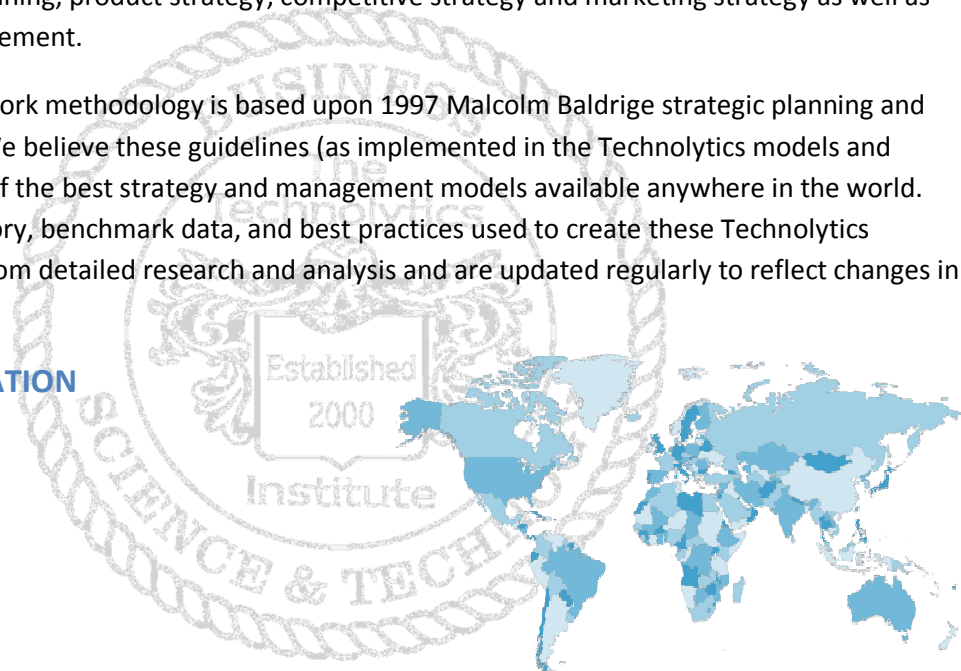
The Technolytics Institute (TTI) was established in 2000 as an independent executive think tank. Our primary purpose is to undertake original research and develop substantive points of view on strategic issues facing executives in businesses and industries around the world. Our strategic goals focus on improving business performance, creating sustainable competitive advantage, delivering innovation and technology, and managing security and risk.

Technolytics helps guide business executives, industry leaders and government policy makers in shaping the economic, regulatory and risk environment of tomorrow. One of the hallmarks of our service offering is our security and risk scenario planning. Our approach is called Trans-disciplinary Intelligence Engineering (TIE). This approach has been used to develop scenarios for Homeland Security, Corporate Event Planning, Corporate Espionage and Security and for other entities. This technique has been applied to strategic planning, product strategy, competitive strategy and marketing strategy as well as security and risk management.

Our technology framework methodology is based upon 1997 Malcolm Baldrige strategic planning and reporting guidelines. We believe these guidelines (as implemented in the Technolytics models and tools) represent some of the best strategy and management models available anywhere in the world. The knowledge repository, benchmark data, and best practices used to create these Technolytics models have evolved from detailed research and analysis and are updated regularly to reflect changes in the global market.

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The following is a list of research that will be published in the near future.

1. *International Policy on Cyber Aggression*
2. *Advanced Cyber Counter Intelligence*
3. *Advanced Cyber Counter Measures*
4. *Cyber Intelligence Acquisition Infrastructure*
5. *Cyber Threat Assessment 2009*



HEARING COCHAIR BROOKES: Thank you.

Please proceed.

**STATEMENT OF MR. RAFAL A. ROHOZINSKI, PRINCIPAL AND
CEO, THE SECDEV GROUP AND ADVISORY BOARD MEMBER
AT THE CITIZEN LAB, MUNK CENTER FOR INTERNATIONAL
STUDIES, UNIVERSITY OF TORONTO, ONTARIO, CANADA**

MR. ROHOZINSKI: First of all, thank you very much for the honor of appearing before your committee.

This is the first time that I'm appearing, but not the first time that my partners and I from the OpenNet Initiative or from the Information Warfare Monitor have had the pleasure to come before you to talk about Chinese practices in cyberspace.

Most recently last year we talked about Chinese practices of surveillance against the TOM- Skype platform as well as censorship and complicity of U.S. companies in censorship in China itself.

We are an evidence-based organization, and I will try to keep my remarks down to the facts derived from the recent GhostNet study itself.

The GhostNet study for most of you, for those of you who have not followed the news or seen the report, was a culmination of a ten-month investigation which uncovered a computer network of 1,200 computers around the world, 103 countries, all of which belonged to ministries of foreign affairs, embassies, international organizations and media organizations.

The network itself was specific and targeted, focusing on these targets in particular. The main command and control servers for the network were located in mainland China and the control interface to the network itself was in Chinese. Note, I did not say that this was a Chinese run network; however, all the circumstantial evidence does point to a network which, in effect, is Chinese operated.

Why we undertook this investigation--and I think this is important to understand--we looked at persistent allegations of Chinese cyber espionage against non-governmental groups. However, many of these allegations, at least in the information that's available in open sources, do not construct a proper attribution or evidentiary chain. They are allegations without evidence which in my mind is conspiracy.

So we set out with this investigation to try to create that evidence chain and that kind of attribution. We had a hypothesis in our action which is somewhat peripheral to this Commission but important to understand. The hypothesis was this: that the

sophistication of cyber attacks against targets which had a lower ability to defend themselves would themselves be less sophisticated and therefore better and easier for us to be able to discover.

In other words, we did not focus on cyber attacks against U.S. interests or Canadian interests, but rather we looked at attacks against third parties, in this case, the Tibetan community and India itself.

We were also afforded a high level of access to the Tibetan community which led us to run a very careful forensic investigation. That forensic investigation included both being able to understand how the Tibetans were handling their documents, in other words to exclude the possibility that the documents that were leaking in a manner other than through cyber, and also to be able to capture in real time technical data that would verify whether or not documents were moving.

We were able through our investigation on the field, in the field, in the Tibetan communities, in India, not only to verify the fact that their computers had been maliciously infected by a variety of vectors, but we were also able to observe documents being moved off those computers of a sensitive nature.

Now, when I say that, I would say that with a very strong qualification, and that qualification is that those documents that were being moved were not random documents that were simply stripped out of those computers because a virus happened to be downloading anything.

They were targeted documents, and in the case of one particular document that we're able to identify, it contained a confidential negotiating position that the Dalai Lama was preparing for with negotiations with China itself.

I would say just very briefly that the investigation had three phases. One was the field collection core component which I've already mentioned. There was another component where we actually analyzed the technical data from the field in our laboratories.

From that, we were able to discover this much broader network which encompassed not just the Tibetan community but 1,200 other entities. Some of those entities were located in the United States. They mainly focused on Solidarity networks that worked with the Tibetan community but did also include some commercial entities with government ties.

Our investigation of those particular cases seems to indicate that those were drive-by exploits rather than intended exploits. Other targets in the U.S. included foreign missions. The embassies of India, for example, the Pakistani mission to the U.N., were all targeted successfully and penetrated. However, whether we consider those to be U.S. interests or interests located on U.S. soil I think is a question

that we have to look at.

What are the findings of our investigation? And I'm willing to talk about these in greater detail during open session. Number one, the network that we discovered does not fit the profile of a cyber crime network, but rather seems to be targeted to the gathering of sensitive political intelligence.

In other words, there was not enough information which would have been readily exploitable by cyber criminals to make it worthwhile to go through the trouble of both infecting these machines and then reducing the target set down to a target set that actually could yield what usually cyber criminals look for, which is personal data or blackmail data.

Secondly, the systems that were penetrated were of a sensitive but unclassified nature. We have no indication that classified networks within these institutions were penetrated. However, the machines that were penetrated contained, for example, visa applicants to one of the countries in question; the main financial database of a particular embassy; the computer belonging to the military attache, the senior consular official.

So this was data which could be combined or penetrations which could be combined and used for other intelligence purposes.

The primary vector of infection was a socially-engineered e-mail, which is extremely difficult to defend against in technical terms.

Now, I'll deviate for one quick second here. Because attackers were able to take full control of an affected computer, rather than having to fake an e-mail message with which to infect someone, they could actually resend a legitimate e-mail message between two trusted parties using a secure connection, and that's why this particular network operated so well, is that it essentially used an existing system of trust to propagate itself in a rather low-tech method.

The network was located in China and on a variety of servers in China, none of which were password protected. Now some people have criticized this and saying, well, why was it hiding in plain sight; why was it not more covert? The simple answer is this: this was a disposable, built-to-purpose collection network, one of perhaps hundreds that exist.

In other words, the resources to build it weren't invested in the technology; they were invested in the exploitation side of it.

This last conclusion leads us to believe that the system was actually purpose-built to target a certain profile of actors, that is those possessing a low level of forensic ability and mediocre practices in information security.

This was hillbilly SIGINT, but it was targeted against a community that really couldn't defend itself against it very well.

We also have a high degree of confidence that the attackers were located in Hainan Island in China. This is because as part of our investigation, we actually infected ourselves. We set up something known as a honeypot computer and were therefore able to observe the behavior of the attacker for an extended period of time.

Of the sample set of what's known as entry IP addresses, 100 percent of them corresponded to Hainan Island, China. Moreover, the possibility, because if an attacker was using something called a proxy, the victim would have to be online, the intermediary victim would be online, and the attacker would have to be online. Coordinating all three activities at the same time is very, very difficult, and in our estimation highly improbable.

Our investigation was unable to conclusively prove whether or not the government interests or criminal interests were behind the network. However, our suspicion is that this was a operation which was essentially outsourced to third parties, essentially third-party actors possessing the equivalent of a letter of mark, legal pirates of the state, which had either some contractual arrangements or had some assurance of financial remuneration or reward in return for maintaining a specific kind of network such as this.

A caveat: is there an alternative explanation for this particular network, one perhaps that doesn't fall so conveniently into a cyber espionage theory? Yes, there is. It is possible that a particularly cleverly constructed vector moved among the diplomatic community because the diplomatic community does talk to themselves. They do use e-mail.

Topics of common interest such as the situation of Tibet or the Beijing Olympics would be probable cause for a message to move that way. However, the pattern of infections is over a period of two years.

The target set that was harvested at the beginning of the network is not what the network looks at its conclusion. The attacker essentially pared down and selected his targets into specific baskets. That conscious process of doing it argues against a coincidental infection.

Some tentative conclusions, and on this I'll end. This investigation leads us to the conclusion that do-it-yourself signals intelligence is now very much a reality. It does not cost a lot of money; you can essentially launch an attack of the ants and get an awful lot of return for a very low cost.

The fact that the attackers were able to use this low-tech technology means that this network exploitation technique is available to anyone. However, it's important to say that while the collection network was low tech, was uncomplex, the requirements that would be needed to be put in place to exploit the information gathered through that do require a scale larger than a small NGO.

Why? Linguistically, 103 different targets, including the Prime Minister's Office of Laos, the Israeli Consulate in Hong Kong, the Russian Embassy in Beijing, the Iranian Foreign Ministry, requires both linguistic skills as well as domain expertise in terms of being able to know what to look for and what to make out of it.

And on that, I will end my remarks.

Thank you.

Panel IV: Discussion, Questions and Answers

HEARING COCHAIR BROOKES: Thank you very much.

Commissioner Wessel. Chairman, Commissioner.

COMMISSIONER WESSEL: Thank you, gentlemen, for being her today, and unfortunately I guess we're not going to be able to get into all the depth of information that both of you possess because this is a fascinating and timely subject.

I want to understand from both of you, if I can, you referred to it somewhat as hillbilly techniques, but indicated that the techniques are matching the target, meaning that it--correct me if I'm wrong--that for more secure installations that there's clearly the opportunity to have more aggressive and technologically proficient techniques.

Do you believe that any, that all of our commercial interests, since we've now seen defense contractors, the electric grid, et cetera, do you believe that everything here is at risk?

MR. COLEMAN: Absolutely. The percentage of dollars that are spent on information security is minuscule compared to the overall IT budget and risk management budget in most organizations.

We looked at this awhile back, and we have what's called "stupid metrics," and we came up with one. The physical alarm industry was six times the size of the information security industry. So once again we're more interested in protecting our physical assets, not thinking about the digital assets.

MR. ROHOZINSKI: I think there's a question of possibility and probability. If you're asking me about the possibility of exploitation and more sophisticated fashions, absolutely. Take a look at how much of our hardware is presently prepared abroad. Take a look at the sales patterns of companies like Huawei that we talked about in the last session and the opportunity to imbed malicious code at the sort of hardware level into critical infrastructure certainly exists.

The question is how probable is that? And I think that's something that we don't have a very good data on at the moment.

COMMISSIONER WESSEL: How do we get at that question since, again, you know, the public has become alarmed, as policymakers have, with all their recent revelations, which

unfortunately are somewhat old and a little dated in terms of getting into the public domain?

We seem to have a problem between DHS, FBI, NSA and others jurisdictionally in terms of determining what's the best way of addressing this problem. Understanding that China is a location for a lot of this, it's a larger problem of course. What do you see the challenge? Do you see that there's--what's the best approach for resolution if there is one?

MR. ROHOZINSKI: Well, I think there are two things that need to be addressed quite independently. One is standards within the industry for actually being able to vet whether or not imbedded code exists on equipment that's brought in from abroad. At the moment, it's done rather ad hoc and on an institutional basis or institution by institution basis.

Some are better at it; some are worse at it. And I don't think there's an across-the-board set of standards that can be followed.

Secondly, I think there's the whole issue of simply opening up information security, in effect, declassifying a lot of the silos that currently exist around it. Had we not published the GhostNet report, it would be highly unlikely that it would ever see the light of day if it was passed through one of the formal institutions, simply because there's a great deal of concern and sensitivity around the sort of ways, means, techniques that it may reveal, and I think that's a big problem as you consider as legislators this issue.

COMMISSIONER WESSEL: Mr. Coleman.

MR. COLEMAN: Actually I've written about this particular topic. It's my opinion that DHS owns national security inside the United States in cyber, not the military. In fact, there's a piece of constitutional law called the Posse Comitatus Act that forbids military, uniformed military, being used against our own citizens, and that could be actually applied to the computer assets of businesses and individuals.

So it's going to be a combined effort, and that's why I was very interested in reading Senator Rockefeller's proposal that he put out as to the organizational structure and what they were going to be chartered with.

COMMISSIONER WESSEL: But are we at a point now where you think we're up to the task of addressing this or are we way behind the curve?

MR. COLEMAN: We are way behind the curve.

COMMISSIONER WESSEL: Thank you.

HEARING COCHAIR BROOKES: Commissioner Shea.

COMMISSIONER SHEA: Thank you, both, for your testimony.

I just have a question directed to Mr. Coleman. Reading your

written testimony before the hearing, you write that there are reasons to believe that the Chinese and Russian militaries are collaborating and cyber warfare is one area that not only lends itself to remote collaboration, but you suspect that this is and has occurred, and I was just wondering if you could amplify that a bit in a public forum?

MR. COLEMAN: Sure. There is no secret that China and Russia have been playing kind of like war games going back and forth. This is just another aspect of military operations for Russia and also for China.

The more concerning point about the Russian and China collaboration is there's an organization called RBN, the Russian Business Network. Basically it's organized crime. There was a time, and we received several communications from people who were looking at this, that indicated that a contingent of RBN, which is supposedly controlling the largest botnet in the world right now, moved some of its operations over to China.

Now that could be construed as saying, okay, maybe they're learning from RBN on how to manage and create these botnets.

There was another piece of concerning information that came out along the same lines, and that's 70 percent of the computers in China have already been compromised, and if you just run the numbers of what they're expecting the number of computers to be, at the end of this year, they will now have the possibility of having over 200 million computers compromised within their country that could be used in time of conflict against an adversary.

So I think with the organized crime component plus the joint military exercises that are going on, it's a reasonable conclusion that they're at least talking.

MR. ROHOZINSKI: I'd like to add to that, and just full disclosure, for the last five years, I've been running a NATO-Russia contact activity with the Russian National Security Council around the issue of information security and actually working with those parts of the Russian government that are involved in both the doctrinal development of cyber war as well as the doctrine of information security, the Russian Federation itself.

I'll make a couple of observations that may be salient to your particular question. First of all, yes, there is Russia-China collaboration, but it happens in fairly strict and fairly well-defined alleys, especially on the state to state level.

There is a Russia-China cryptographic treaty that has basically allowed both of them to develop interoperable standards in cryptography as well as to develop cryptography as a science and as an art for national security purposes, which is separate than that which occurs elsewhere. That has both commercial implications as well as

national security implications.

Yes, there is a lot of collaboration on information security through the Shanghai Cooperation Organization, certainly in terms of harmonization. At the same time, there's a great deal of competition. Let's not forget that Russia is contiguous territorially with China. There's an awful lot of worry about Chinese encroachment, particularly in the Far East.

There is also intense competition over the energy markets of Kazakhstan, the water resources of Tajikistan, and in a sense of strategic competition over Afghanistan and other critical areas within that.

So the Russians, my feeling, and having met with them just last week at a retreat where we were talking about exactly this particular issue, is that they feel that they're being pushed towards China because they cannot get a dialogue around issues which they see as being critical in the cybersphere with the U.S.

There's a great deal of concern about the U.S., about the U.S.-centricity of the Internet, and a great deal of fear that the whole question of ICANN, right now as it's being discussed, will somehow bring the whole Internet much closer into the U.S. orbit than it already is right now.

Their major diplomatic push, which you'll probably see in the next few months, will be to internationalize governance of the Internet, basically to try to push it towards the ITU and other such mechanisms where they feel they have a much more equitable voice on that.

That's what's happening on the state level. On the sub-state level, in terms of collaboration of criminal gangs, you know, the Internet is--and the Internet or cyberspace--is a domain which is open to colonization, and very often cyber criminals will move to a jurisdiction where they have the most protection through the absence of existing laws or the ability to prosecute crimes.

So what my esteemed colleague was mentioning to me is less an active cooperation of China and Russia, writ large, capital letters with an exclamation mark, than it is the fact that Russian criminals have found it convenient to operate from Chinese domain space simply because of the fact that they are much less subject to detection and prosecution than they are in Russia at the present.

COMMISSIONER SHEA: Okay. Thank you very much.

HEARING COCHAIR BROOKES: I open this up to the panel. Obviously, our interest is China as the U.S.-China Commission, but is China our largest cyber problem? Or is there another country that's--

MR. COLEMAN: The data that we had, 4.6 times the number of attacks more than the next closest country, clearly indicates that China

is a problem. But I would submit that we better be looking much broader than that and looking at the whole issue around the governance of cyber security and the investigation.

It's a three-headed, I guess, who's number one is anybody's guess at any point in time. The U.S., China and Russia are in the top three spots in the cyber arms race is the way we assess them.

HEARING COCHAIR BROOKES: We often hear that it's very difficult to track these attacks or aggression back to their origins, and that many of them seem to end in China. Do we have any sense of how many, what percentage of this sort of aggression may go beyond China that do not originate in China in terms of--

MR. ROHOZINSKI: Well, I can give you a statistic.

HEARING COCHAIR BROOKES: Okay.

MR. ROHOZINSKI: Because at present, 51 percent of all malware is actually originating from China, which means that 49 percent is not, but you have to put that into perspective. The perspective is this: China is becoming the most populous Internet nation in the world. 17 percent of the current Internet is Chinese. The vast majority of that is young. The vast majority of that falls within the 20 million man army which is fast becoming unemployed because of the global recession.

They are digitally promiscuous. They are experimenting. So much of what they do isn't so much criminal in intent as it is simply a kind of scattering around to see what they can do on the Internet which is not described by law.

HEARING COCHAIR BROOKES: How would this sort of troubling Chinese cyber activity, how would we break that down in terms of percentages? I don't know if anybody has looked at this in terms of criminal, other sort of--I don't know how you would characterize the sort of thing, the mischief that people are involved in, espionage, military related? I mean has anybody looked at this in terms of how all this cyber activity breaks down categorically?

MR. COLEMAN: Absolutely not. Until we get to that next level of investigation beyond the simple IP address that could be one of a compromised server, we won't know that. So once again, that's why I'm saying that we have to treat this, whether it's organized crime, whether it's state sponsored, whether terrorist sponsored, we have to treat it all under one governing set of rules and regulations and cooperation to find those numbers out.

MR. ROHOZINSKI: Yes. Commissioner, you put your finger on I think the holy grail that exists right now, and that's called how do we attain situational awareness in cyberspace so that we can actually know what's going on in order to take intelligent decisions, and I don't think we're there yet by any means.

HEARING COCHAIR BROOKES: Is anybody even outside of North America looking at these sort of issues because others have problems as well clearly?

MR. COLEMAN: I do know Germany is looking at it. I've received some indication Britain is as well.

HEARING COCHAIR BROOKES: Anybody looking at it aggressively or trying to get their arms around this in terms of these metrics and situational awareness?

MR. COLEMAN: In my opinion, the most aggressive is U.S. Strategic Command. They're looking at it. I have the utmost respect for the work that they're doing. I was just out there in January and I'll be there again later next month. They're working on this diligently.

MR. ROHOZINSKI: I would say that most advanced economies are taking this on very aggressively. Again, I can't speak to China directly, but I can speak to Russia, and I know that this has become priority item number one, and there's a great deal of interagency coordination around it.

HEARING COCHAIR BROOKES: I read your report, and I applaud you for it, not being a person of completely understanding cyber world, but to me it made quite a bit of sense.

Are there any other networks or other sort of schemes along these lines that you've come across besides this one you've published about?

MR. ROHOZINSKI: We continuously do investigations of this sort so I can say there are at least half a dozen that we've looked at personally. One thing that I would say that emanates from this report itself is the GhostNet Network that we wrote up was only one of seven malignant infections that we discovered. It just so happened that this is the investigation trail that we could report on as opposed to the others which were dead ends.

That's why in my remarks, I said this is the attack of the ants. These are essentially disposable networks that can be rapidly constructed, and I think that's the trend that we have to be aware of.

HEARING COCHAIR BROOKES: Could you describe to a certain extent the other networks, other malicious code that you came across besides GhostNet? Were they all related to Tibet or were there other issues here as well? Were they all Chinese or circumstantially Chinese?

MR. ROHOZINSKI: In this case, we were looking at Chinese ones and they had a very similar modus operandi. It's just that we could not follow the attribution chain. But there is a completely separate activity, which also I think baffles us at times, but which is very prevalent outside of North America where both Chinese and Russian interests are involved, and that is in the use of denial of

service attacks as a way of silencing operation and/or other politically active groups.

We have seen this repeatedly occur in Central Asia and other countries, and when we have looked at track back investigations in terms of who was involved, generally speaking, there was one common point of interest, and that is the individuals that were behind it all had some experience or some education in Russia, picking up essentially techniques from a community that's there.

But what's interesting about it with relation to China is that we've seen those techniques essentially being taken up now by Chinese hacking gangs, a Burmese, Vietnamese and others. So there is a propagation of technique.

HEARING COCHAIR BROOKES: Chairman Bartholomew.

COMMISSIONER BARTHOLOMEW: Thank you. Thank you to both of our witnesses, and Mr. Rohozinski, we always appreciate hearing from the OpenNet Initiative and what you guys are doing.

I think I agree with Peter on the question of attribution. I think that we're frequently told that one of the concerns in the event of a cyber attack is that it's not going to be easy to figure out who it is, who's launched the attack, and that it's possible that the place that launched the attack launched it through somebody else, and how we deal with that in the context of a world where cyber warfare is increasingly likely to be a real challenge.

But I want to get to two things. Can you talk a little bit more about what you're talking about on denial of service attacks that people or nation states are somehow, they're learning how it works in order to be able to use it to silence their own opposition? Where is that kind of knowledge coming from? Is it people online watching it take place and figuring out how to do the same thing? Is there some sort of active sharing of expertise?

MR. ROHOZINSKI: It's an underground economy. You could go online, and you could in a sense order crimeware that allows you to, first of all, set up your own botnet and then also target it and sell it to others, and that economy exists because of the fact that there's a market for it.

You know we in North America are used to a culture where you try to out-communicate your opponent. In many other parts of the world it's all about silencing your opponent. So there's a market for that kind of technology, and it's not just in politics; it's also in media.

If you want to be the most popular online source, well, you can either have the best content or you can make sure your competitor doesn't get it out. Up to a few years ago, in several countries where we studied, you actually saw newspaper articles or newspaper advertisements saying buy yourself a botnet. \$20 will get you this

kind of attack; \$500 will get you that kind of attack.

COMMISSIONER BARTHOLOMEW: Then I want to take that into this comment that had been made about Russian organized crime operating in Chinese domain space. I think the perception of a number of us has been that the Chinese have tighter control over their computer networks over there, over their content certainly, that's taking place, and we know that they have the ability to shut down when Chinese citizens are communicating things that they don't want communicated from person to person over the computer.

Is it really possible that Russian organized crime could be acting through Chinese space without the Chinese government being aware of it and/or allowing it to happen?

MR. ROHOZINSKI: I think you identified a very important characteristic of the Chinese concern. They are very concerned about the content space. They're not so concerned about monitoring the behavior on their networks from a cyber crime point of view.

My impression from having spoken to my Russian interlocutors is that they've spent an awful lot of time developing capacity for being able to surveil their internal network, specifically for activities, not the content level. It's not what they care about. There's no great firewall of Russia.

Whereas, the Chinese have invested an enormous amount of expertise, time and effort into monitoring what is actually exchanged on the Internet in terms of the content level while they have not really exploited what is actually done on the Internet at the protocol level. So I think that's the difference.

COMMISSIONER BARTHOLOMEW: So the exploitation by Russian organized crime or the use that they're doing is of--

MR. ROHOZINSKI: Of the actual hardware and servers themselves.

COMMISSIONER BARTHOLOMEW: Of the hardware, okay.

MR. ROHOZINSKI: So, for example, you know, one of the command and control servers for the GhostNet was located on a gov.cn server. When we looked at that server and we used a technique called "technical scouting," which means we didn't hack it, we simply took a look what's on it, we also found it serving all sorts of other malware that I'm sure the system administrator was never aware of.

You don't really see that kind of thing in Russia. I think if the Russian Mafia decided to blog in China, they would probably be picked up quicker than if they used an intermediary node to attack the United States.

COMMISSIONER BARTHOLOMEW: Very interesting.

Thank you very much.

HEARING COCHAIR BROOKES: Commissioner Videnieks.

COMMISSIONER VIDENIEKS: Good afternoon. I'm not a computer-type guy so my questions may be a little bit off the wall. What would the overhead costs be? I realize there's a problem, a security problem. In order to fix it software-wise, what would roughly the overhead factor be to a small office versus a big office?

MR. COLEMAN: I don't think they can fix it. And let me tell you why. I would actually look at what China has done so that they are not susceptible to attacks from the United States or any other adversary.

They've done two things that are very strategic, and when you look at them, it's also an economic issue for us. The first is the Chinese Government developed their own security hardened server operating system (Kylin) under very strict controls to eliminate the threat of preprogrammed back doors. Second, they developed their own microprocessor for the same assurances. That would be very difficult to do in the U.S.

COMMISSIONER VIDENIEKS: I think it would be a huge economic issue the way it sounds. If you've got a big problem, it's got to be fixed, the initial entry level for the criminal is minor, or the spy, whoever, you know.

MR. COLEMAN: Sure. China created their own operating system, and it's called Kylin, K-Y-L-I-N. It was a long-term initiative, started back in I believe 2000 or 2001. They've announced that they're going to start migrating their business and critical infrastructure in government systems over to that operating system.

It was 100 percent developed in China under very strict controls and it's hardened. We don't have that.

The second thing they did was to eliminate the hardware possibility of a compromise. They're developing their own national microprocessor chip that Kylin will actually run on top of. So they will have hardened hardware and hardened software so that they would be able to address it.

Now, if you take a look at the open source like Linux environment, it's very difficult to police millions upon millions of lines of code. We don't have what I would call a known, solid, good base to go from.

We already know that there's been massive compromises in terms of I think the total number was 700,000 counterfeit processors came into the United States and were seized by U.S. and Customs last year.

We know that \$76 million worth of confiscated counterfeit Cisco networking hardware was coming into the United States and actually was distributed, and some of that made it into the Defense Department and Washington, D.C. organizations because they were set up as a small business in the United States and they resold that.

We also know that we've got counterfeit chips in space. So we don't have that solid footing that we can build from. We would have to start over.

COMMISSIONER VIDENIEKS: We don't have a centralized security safeguard system?

MR. COLEMAN: Yes. We do not have a centralized security safeguard system.

COMMISSIONER VIDENIEKS: Sir, you want to comment, please?

MR. ROHOZINSKI: Yes, I'd just like to comment, with several observations perhaps.

COMMISSIONER VIDENIEKS: Yes.

MR. ROHOZINSKI: First of all, we cannot see security as a solution. You have to see it as a process, as a way of thinking. So there is no technology fix that can be applied across the board in order to solve the problem that we have here.

However, that being said, I think the field of information security right now is far too focused on engineers and far too focused in the hands of engineers. We are a technophiliac society.

COMMISSIONER VIDENIEKS: Are we playing their game? My question would be: is creative destruction the answer?

MR. ROHOZINSKI: I think so. The answer I would give to your question, which is somewhat indirect, is to say that we have to see network security as separate from cyber security, and cyber security really needs to be broadened to include not just the technology aspects, but also an appreciation that the most successful exploits that we've seen are ones that employ social means, not purely technological means, and until we get a good sense of that, and that may take a DARPA-like initiative, if you like, to build a new field of cybersecurity, we're going to be missing the boat and basically wasting billions of dollars looking for the next best widget that will solve our problem.

COMMISSIONER VIDENIEKS: Thank you, sir.

MR. COLEMAN: If I could add something?

COMMISSIONER VIDENIEKS: Yes.

MR. COLEMAN: You brought up the social engineering aspect of this. The number one topic right now is H1N1, the swine flu. We've already started to see phishing and malicious e-mails and Web sites to infect people using that type of content draw them in. That's the social engineering that is so difficult to guard against.

COMMISSIONER VIDENIEKS: If we were an autocratic country and we were to say, okay, we increase the penalties by ten and we make everyone buy new hardware and do something with the software, okay, would that kind of a process, is it feasible to some countries,

maybe not here but someplace else?

MR. COLEMAN: I don't think it's feasible here. It might be feasible in a very small country, but the infrastructure requirements to build the manufacturing of microprocessors and also the infrastructure around networks as well as just the technical capabilities of writing all the software would go beyond the means of most countries.

MR. ROHOZINSKI: I would only add to that that I think that cyberspace is a single-most valuable asset that the U.S. has as part of its public diplomacy and global engagement, and you certainly don't want to throw the baby out with the bath water by creating an isolated, super-secure network that doesn't serve that purpose.

COMMISSIONER VIDENIEKS: So we're struck with trying to create a counter process, a security process, to try to protect what we have?

MR. COLEMAN: Yes.

MR. ROHOZINSKI: Correct.

COMMISSIONER VIDENIEKS: Thank you, sir. Thank you.

HEARING COCHAIR BROOKES: Commissioner Mulloy.

COMMISSIONER MULLOY: Thank you, both, for being here.

Mr. Coleman, in your testimony on page seven, you talk about we need to, you say, you know, about digital DNA and some technical fixes to this problem, but then you say in addition to these technical capabilities, we need to establish a framework for international cooperation for the investigation of cyber attack.

Would it make sense--and I remember we raised this in another hearing--would it make sense to try and get a convention? I mean in my youth I was in the Foreign Service, and I remember working on the first U.N. Conference on the Human Environment in Stockholm. And so you realized there was a problem, so you set a meeting, and then you get everybody thinking for a couple years what do you want to get out of that meeting, and sometimes then you force people to identify the issues and then maybe even develop an outcome, a convention, that could try to head off the problem?

Is there any thinking about that out there as far as you know, or does that sound like a sound idea or a foolish idea or something that maybe we could even think of recommending to the Congress?

MR. COLEMAN: Actually, I think that's an excellent idea, and to the point, last month when I presented before the United Nations on cyber terrorism, I called on the United Nations to take this on because we're going to need all the countries that are currently attached to the Internet to really understand this and create this global repository of known threats as well as regulations that we can apply and cooperation so we can do the investigation so I can answer your question, what percentage was organized crime; what percentage was military

function?

MR. ROHOZINSKI: This isn't a new question. In fact, over the past ten years, there have been several attempts to try to create a global normative regime around cyber crime, cyber terror and the governance of cyberspace.

The European Convention on Cyber Crime was one such initiative by European countries. There have been several such initiatives that have been started by the U.N., including the Technical Working Group. The ITU has also taken it on.

In fact, the absence of being able to come to a consensus has meant that some of these international organizations have taken it onto themselves to create appropriate mechanisms for harmonization.

ITU created, for example, something ITU called Impact Alliance, which is a federated intelligence sharing network for cyber crime. The problem is that the convention itself has been stymied for the last seven years by a lack of engagement by the U.S. in issues which many countries have seen as being critical to discuss.

So, whereas, for example, some lower level issues of cyber crime have been discussed, when these countries have wanted to talk about broader issues of Internet governance or national security in cyberspace, the answer has been we don't discuss those issues because we don't have any capacity in cyberspace which, of course, you know is not the case.

The other problem that exists here is that it's not just the convention that needs to happen, but there has to be a harmonization of local national laws that actually describe what a cyber crime is.

In Russia, for example, there's a law on IT crime, not cyber crime, which encompasses copyright, which includes trademark, et cetera, but which excludes some of the things that the U.S. codecs concerns as being crime, which means they run into a problem, that even if the FBI passes a request through a third-party saying, hey, we suspect that a cyber crime was committed jurisdictionally in your territory, very often the country comes back and says, well, I'm sorry, this is not considered to be a crime or we haven't described it yet in legal terms; therefore, we cannot cooperate with you.

Multiply that problem 140 times and you see the scale that we're dealing with. We're in very early days.

COMMISSIONER MULLOY: Thank you, both.

HEARING COCHAIR BROOKES: Commissioner Wessel.

COMMISSIONER WESSEL: Thank you.

Let me follow up on that question, if I can, and go back a bit to the chip and Kylin software, et cetera, hardened software, which quite frankly I hadn't heard about before. What you were just talking, though, about is really a voluntary framework. If the question is about

government-sponsored espionage, about asymmetric warfare, et cetera, no convention is going to really stop that.

The question is we have a globalized supply chain now. Whether it's the Chinese chip and Kylin software or whether it's the fact that I don't think we make many, if any, hard drives or anything else here, the fact is that with a globalized supply chain, it can be either done through hardware or software, and we have a fairly porous system.

So while we may be able to get to the attribution issues or the prosecution issues on a level as it relates to commercial crimes, et cetera, if we're talking about governmental espionage or asymmetric warfare, is there an answer? You know what I hear is there's no answer. There is, you know, if we try and do what TI and others have done with hardened chips, you know, et cetera, et cetera, we're going to be several generations behind what is, in fact, the leading-edge technology.

So we can do something that's very myopic around our defense needs, but as we look at the commercial sector, whether it's banks, electricity grid, or et cetera, what I'm hearing today is there's no way to protect ourselves. Am I right or am I wrong?

MR. COLEMAN: First of all, the threat that we're seeing evolves and changes I would say daily. You know what was interesting a few years back is, oh, we've seen that, done that, moved on to something else. The way the Internet works, and the whole preface around the Internet, was this open sharing of information.

I don't think anybody who was at the original ARPANET design meetings ever thought we'd be doing financial transactions going over this. Therefore, the protocols and everything else that we're basing this on were not developed with security in mind.

Security has to be built in, not bolted on at the end, and that's where we are today. We keep trying to bolt this thing on at the end, and, you know, like I said, in about 2002 to 2004, we saw such a significant change in the level of sophistication and professionalism around these attacks, we actually saw QE comments in some of the code fragments that were left behind from one attack, and an interesting note, we were able to identify the hacker because he had a common misspelling in his notes, and we actually Googled the misspelled word, and we found him on a blog. So--hey, whatever gets you there at this point in time. But the bottom line here is I think until we recognize that all the investment in the Internet has been a great learning experience, and we've all benefited from it, we need to take the next step and come up with a protocol that replaces the one that's in place so we have security built in.

MR. ROHOZINSKI: I'll take a slightly different tact on this one. I'm a great fan of General Mattis, who I heard speak a couple weeks

ago, and his contention is there's no such thing as asymmetric warfare. Warfare is the history of adaptation. When Hannibal marched his elephants across the Alps, when the British deployed the machine gun against the Zulus, or when the first tanks rolled across the trenches, these were asymmetric because they changed the nature of the two actors that were engaged in a contest over political means and other things.

So I think we need to do away with that. The fact is that cyberspace is an asymmetric advantage because it levels the playing field for actors that otherwise would be faced with a great deal of economic, political and military dominance from a particular actor, which in this case is the United States. They've correctly identified; they correctly targeted. We should not be surprised.

I think the problem that we have is how do we separate within this new environment that's emerged signal from noise. What should we concentrate on which is a critical security issue? What should we just let go because it's part of the background, part of the friction that we experience in real life and which should be part of cyberspace to begin with?

That signal to noise filter is dependent upon situational awareness. That's where we don't have a capacity and that's where we do need a DARPA-like initiative to help build that capacity across the technical sciences, across the regulatory frameworks, across the technical means that we need to have.

What I would caution against is this focus on secure first, build the wall, really starts to push us towards throwing out the baby with the bath water, and I think we have to really be very careful about that.

COMMISSIONER WESSEL: Yes, I understand. But do you think STRATCOM is looking at it that way in terms of the signal to noise ratio, how they address the informationalized warfare issues that they're concerned with, but not throw the baby out with the bath water for the non--for the externals, if you will?

MR. ROHOZINSKI: I think General Cartwright and his colleagues do an awful lot of thinking about these things, and I think they work within the same kind of constraints, technical and otherwise, as we all do. But they are, yes. I wouldn't presume to speak on their behalf, but I do know that these are issues that are foremost in the minds of people who are on the sharp end of the stick with this.

COMMISSIONER WESSEL: Thank you.

HEARING COCHAIR BROOKES: Chairman Bartholomew.

COMMISSIONER BARTHOLOMEW: Thanks.

You mentioned what we need is a DARPA-like initiative on these issues. Is the Chinese government running their own version of a

DARPA-like initiative? I mean there can be an asymmetry, not necessarily in how things are playing out, but there can certainly be an asymmetry in terms of how aggressive a government is being in developing its own capabilities to undertake certain activities.

MR. ROHOZINSKI: I would make two observations on that. One, in terms of the amount of R&D dollar and attention that has been played by all levels of Chinese government, industry, military and others on what they call the "informatization space" has been considerable.

That will not necessarily take the form of a DARPA simply because the institutions are different, but certainly they have correctly identified this domain as the domain in which China must master to become a world power in the 21st century.

My other observation, however, is as follows: having been a student of authoritarian bureaucratic systems, they are generally much less flexible, much less adaptable, in terms of taking an advantage of resources that they put into a particular area.

I think there is where a U.S.-type approach, or our approach, which is much more flexible, maybe more chaotic, really does have an advantage.

COMMISSIONER BARTHOLOMEW: But how do we deal with the fact that what you identified with GhostNet was quite a low-tech initiative you've said? In other words, it didn't need to have a lot of money thrown at it. It perhaps needed some sort of focused attention on how to create it or a smart clever group of people who were tasked with doing something.

I guess I'm trying to understand that or to hypothesize it's not necessarily about throwing resources at something, but it is how to think creatively about how to do this, and it's interesting to me that it is an authoritarian government that seems to have been more successful at thinking creatively about this low-tech way to try to get away with something.

MR. ROHOZINSKI: I'll give you a two-part answer on that. The first one is maybe the high-level academic answer, and that the Chinese at least on their strategic level are all children of Confucius and Sun Tzu. They think in terms of stratagems and strategies. If you look at military doctrine and state doctrine, it's very much framed in that particular context.

That is very much about taking and looking three steps ahead. I think we have a tendency of focusing on tactics, techniques and means, and not really thinking strategically beyond the four-year cycle, no matter what that four-year cycle may be.

The more practical level answer is that look who is doing this kind of stuff in China. It's the 25-year-olds. Those 25-year-olds or

17-year-olds have 40-year-old fathers who happen to be working within institutions. Very often the opportunistic exploitation of a particular low-tech approach is derived through that chain, completely informally, rather than through somebody sitting in committee and deciding let's build 500 botnets that we're going to use to attack the Tibetan community.

COMMISSIONER BARTHOLOMEW: But if you can attribute back to, say, Hainan Island but not necessarily attribute back to who it is who might have been working on Hainan Island and doing this, it's difficult to know where the training was, who was trained and where they got their training, those 25-year-olds even.

MR. ROHOZINSKI: What I was very careful in my oral remarks to distinguish between was the collection network and the exploitation network. The collection network could have been outsourced. In other words, the person providing what I called "hillbilly" SIGINT may be completely unaware the purposes to which that network is being put.

The exploitation part of it, in other words, knowing what documents to request, how to exploit those documents further, how to grow the network out, that, in my estimation, requires an awful lot more thinking, resources and deliberative action.

COMMISSIONER BARTHOLOMEW: Okay. Thank you.

MR. COLEMAN: To answer your question about the DARPA program in China, it's referred to as Program 973, and we've given Mr. Dotson a copy of the Kylin report that we did, and we list several areas of technology that we're concerned about that they're developing advances too. So you may want to get that and take a look at that.

COMMISSIONER BARTHOLOMEW: Thank you.

HEARING COCHAIR BROOKES: This has been very informative, but one of the purposes of this panel is cyber espionage out of China. So to what extent do you think that we have a problem with this and to what extent do you think that private businesses are addressing it based on the Chinese threat?

MR. COLEMAN: I think we have a serious problem with the amount of what we call data exfiltration. We've heard that some estimates between 20 and 27 terabytes of data went out of the Pentagon back in 2007. That's not the recent attacks that we've heard about. We know that the Ministry of Defense over in the UK had a massive attack with a lot of data loss. In fact, the stats I saw a report that showed 75 percent of the Royal Navy was compromised. So a lot of intelligence about their systems and everything else went out.

DISA, the Defense Information Services Agency, I believe it is, published a report that talked about solicitation techniques, and they actually identify in order what the primary and secondary and third and fourth and fifth targets are in terms of technologies that these

organizations are going after.

If you look at it, and my colleague here pointed it out, we do stupid things. We've got people that really just don't understand the fundamentals of information security and because of that they click on the wrong links and compromise their systems.

Until we fix the people problem, which is a much harder and bigger problem, the espionage against our corporations is going to continue and it's going to get worse.

MR. ROHOZINSKI: I'll speak only to the evidence to which I have direct access rather than trying to speculate what the NSA may or may not know.

In the GhostNet investigation, the average length of infection for any of the systems that we saw was between 140 and 600 days, and these were not undefended networks, which means that even with considerable resources being put against defending these kinds of attacks, nevertheless, the attacker was able to maintain control over these computers for a significant amount of time.

We also noted that in the computers or in the systems that we had access to, there were multiple infections, which means that it wasn't just one GhostNet, it was a multiple of GhostNets. So I'd leave you to that as a way of extrapolating the possible scale of the problem.

HEARING COCHAIR BROOKES: Thank you.

Anyone else? All right. With that, I will close the panel and thank our panelists today for joining us.

MR. COLEMAN: Thank you.

HEARING COCHAIR BROOKES: With that, the Commission is adjourned.

[Whereupon, at 4:00 p.m., the hearing was adjourned.]