Opening Remarks

Give Me Your Yuan

By Peter Coy

"President Obama and I, we welcome, encourage, and see nothing but positive benefit from direct investment in the United States from Chinese businesses and Chinese entities. It means jobs." —Vice President Joe Biden, Aug. 19, 2011, Beijing

Could it really be that simple? American government officials at all levels are flocking to Beijing and Shanghai in hopes of recruiting Chinese investors who are eager to expand their businesses, or in some cases safeguard their wealth. While China owns more than $1.2 trillion in U.S. Treasury securities, it has only $28 billion in direct investments in American companies and real estate, according to estimates by the Rhodium Group, a private research company. By the end of 2020 that sum could balloon to between $100 billion and $400 billion, Rhodium says.

The Obama administration is working hard to smooth the way for China's dollars. In July, Chinese and U.S. leaders meeting in Washington agreed to restart negotiations toward a bilateral investment treaty that would accelerate the flow of investment from China to the U.S. in exchange for increased American access to China. U.S. Secretary of the Treasury Jacob Lew said the agreement "stands to be a significant breakthrough."

China, however, isn't just another Brazil or Denmark with money to spend. It's an economic juggernaut with historical resentments against the West and an increasingly assertive military. U.S. defense and intelligence authorities worry about China's methodical effort to attain the world's most advanced civilian and military technology. The Chinese, for their part, dislike what they perceive as America's effort to stymie them by declaring some sectors of the U.S. economy off limits–calling it, in one memorable phrase, "stepmotherly."

Chinese purchases of U.S. factories, research and development labs, farmland, and oil fields are likely to vex both countries for years to come. The most recent hambone of contention is whether America's food supply is threatened by Shuanghui International Holdings' attempt to acquire Smithfield Foods. On July 24, Smithfield said the Committee on Foreign Investment in the U.S. (CFIUS) needed an extra 45 days to review the deal, which critics allege could somehow make it easier for contaminated Chinese food to enter the U.S.

During the 1980s, Japanese investors' purchases of landmarks such as Rockefeller Center and the Pebble Beach golf resort stoked anxiety about Japan's growing influence over the U.S. economy. Those fears turned out to be misplaced, the product of xenophobia and an exaggerated assessment of Japan's economic strength. Now, before the floodgates of Chinese money really open wide, would be a good time for a sober conversation. Should the U.S. welcome Chinese investment with a smile or a gimlet eye? What sectors should be off limits on national security grounds? Should China be treated like any other country when it comes to investment, or does it require special scrutiny? For the sake of both nations, says Ian Bremmer, president of Eurasia Group, a consulting agency, "It's very important that the U.S. develop clear rules of the road."

The U.S. status quo is openness. Unlike countries such as Canada that evaluate the overall benefit of a foreign investment before saying yes or no, the U.S. sets the default at yes. A deal is rejected only if it violates antitrust rules or if CFIUS, an interagency committee, concludes it "threatens to impair the national security of the United States." During the presidential campaign last September, Obama cited national security to prevent a Chinese company from buying four wind farms near a Navy test range in Oregon. Other potential buyers have backed down from sensitive purchases before the White House ruled, including Huawei Technologies, which was founded by a former People's Liberation Army technician but denies links to Chinese intelligence.

To date, America's general openness has benefited both countries. China's Lenovo kept R&D in North Carolina after buying and expanding IBM's ThinkPad business. Chinese investors have also helped the U.S. increase its energy supply; in February, China Petrochemical signed a $1 billion deal to buy half of a shale oil field in Oklahoma owned by Chesapeake Energy. Wanxiang America in Elgin, Ill., has rescued a string of failing or failed auto-parts companies. It also bought lithium ion battery maker A123 Systems out of bankruptcy last year, playfully renaming it B456 Systems. Contrary to fears that China would suck American companies dry, Wanxiang has increased employment. "Our slogan is, 'Every penny we make, we're going to reinvest,'" says company president Pin Ni. "We haven't sent any dividend, not even a penny, to China since day one."

"It is emphatically in the U.S. national interest to gain a larger share of these new investment flows" from China, Asia Society scholars wrote in the preface to a research paper last year. American companies that get bought find they can sell more in China, says Thilo Hanemann, research director at Rhodium Group. "The Chinese are not going to start making socks and underwear in the U.S.," he says, "but some things that they should be making in the U.S. could come back."

Chinese investors are eager to acquire more assets in America. Why that could benefit both countries—up to a point

PHOTO ILLUSTRATION BY 731; PHOTOGRAPHS: ALAMY(2)

National security hawks, however, warn that the U.S. risks selling China the very goods the Chinese need to undermine American interests. "There is this stupid idea that there is this magical pile of technologies that are purely military, and all these others that are purely commercial that we don't need to worry about," says Michael Sekora, who started Project Socrates in the Reagan administration to monitor and rebuild U.S. competitiveness. Sekora, a physicist, says he attended a recent meeting in Texas in which a congressional staffer asked him about "dual-use" technologies that have both civilian and military applications. "I said, 'Sir, that's sort of a dumb question. Give me a technology that's *not* dual-use.'"

Usha Haley, a West Virginia University professor who testified against the acquisition of Smithfield, says even Chinese acquirers that aren't state-owned are serving the government's interests; otherwise they wouldn't get permission to do the deals. "They will start controlling our agriculture," Haley says. "Their motives are entirely benevolent at this point, but how do we know that will continue?"

China isn't another Brazil or Denmark—it's an economic juggernaut with an increasingly assertive military

This kind of talk drives the Chinese to distraction. China Investment President Gao Xiqing complained in April that the sovereign wealth fund is "singled out" by U.S. regulators. "We thought we were friends," he said after a meeting with officials in Washington. "All of a sudden, you've got people slapping you in the face and telling you, 'OK, we don't like you.'"

It's not healthy for anyone when the talk gets this heated. The point of the negotiations is to regularize the dealmaking and reduce friction. A bilateral investment treaty "would set a positive tone," former Treasury Secretary Henry Paulson said in a statement. David Marchick, a managing director at Carlyle Group and co-author of *U.S. National Security and Foreign Direct Investment*, says he hopes and expects that U.S. resistance to Chinese acquisitions will diminish over time. "It will be less interesting and less newsworthy because it will be part of what people will expect," he says.

But the opposite is also possible—that Americans' concerns will grow as the trickle of Chinese money becomes a torrent. Hoovering up Treasuries is one thing; large-scale acquisition of factories, labs, mines, and farms is quite another. Bremmer, an expert on China's state capitalism, says the upside is that China "will have a stake in our economy doing well." The downside, he says: "With every company they purchase, every piece of technology they get, the Chinese will be able to tip the playing field in a way that will really hurt the operations of American multinational corporations."

On both sides, certain sectors will remain closed to investment. Let's be clear, too, that a big source of this problem is the merchandise trade imbalance, which reached a record $315 billion last year. The U.S. should keep pushing China to buy American products instead of saving up to buy the companies that make them. But nothing can change the reality that China and the U.S. are rivals. The Obama administration is right to encourage more Chinese investment in the U.S.—but it would do well to be careful what it wishes for. B