

The Truth About Investment in China

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KEY TAKEAWAYS

Over the past decade, \$2 trillion–\$3 trillion or more of U.S. investment has flowed into China with virtually no transparency and oversight.

To meet national security threats, notifications and prohibitions should be required for investments involving dual-use technology with military applications.

Yet some politicians continue to rely on myths to argue that American investment in China’s military–industrial complex should remain unrestricted and opaque.

Over the past decade, as much as \$2 trillion–\$3 trillion or more of U.S. investment—much of it supporting China’s growing military capabilities—has flowed into China with virtually no transparency and oversight.¹ In August 2023, President Joe Biden issued an executive order that eventually will begin to address this threat,² but congressional action to strengthen the Biden Administration’s half-measures remains essential.

Nevertheless, some politicians continue to block bipartisan legislation that would scrutinize and ideally prohibit dangerous investments in China, relying on myths to argue that American investment in China’s military–industrial complex should remain unrestricted and opaque. This *Issue Brief* examines those myths and provides the truth about the effects of this investment on America’s economy and national security.

This paper, in its entirety, can be found at <https://report.heritage.org/ib5348>

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Myths and Truths About Investment in China

Myth: More U.S. investment in Chinese companies will improve the behavior of the Chinese Communist Party (CCP).

“We want Americans on the boards of Chinese companies spreading Western standards and complying with U.S. laws.... It is therefore unclear why the U.S. would want to prevent Americans from going abroad to pry open the world’s most opaque major economy.”³

Truth: Seeking to liberalize China through free trade and U.S. capital investments has been tried for decades and has failed miserably, degrading U.S. prosperity and national security in the process. China was supposed to grow freer as it grew richer; instead it has grown more repressive at home and aggressive abroad. The record is clear: Hundreds of billions of dollars of unrestricted American investment in China’s leading companies has neither convinced the CCP to adopt “Western standards” nor “pried open” China’s economy. In fact, under CCP General Secretary Xi Jinping’s increasingly dictatorial rule, that is even less likely to be true today than it was at the turn of the century.

Myth: Limiting investment in China’s military technologies would be “emulating Xi Jinping.”

“[T]o outcompete China we cannot become more like the Chinese Communist Party.”⁴

Truth: It is extremely disingenuous to suggest that America’s monitoring of U.S. capital flows into China—and not funding China’s military-technology programs—is akin to America’s becoming Communist. On the contrary, it is common-sense national security policy. Executive and legislative proposals to monitor and restrict U.S. investments in China are incremental and would leave the majority of U.S. capital flows to China untouched. Moreover, many of the affected types of investments in other foreign adversaries are already prohibited—Russia, Iran, and North Korea are all subject to total bans on U.S. investment—but investing in China, even in military technologies, is still allowed. Just as the U.S. would not have funded Soviet missile programs during the Cold War, there is nothing un-American about not funding the military-technology capabilities of your principal adversary.

Myth: U.S. investment doesn’t help China develop military technologies.

“[T]he premise of an ‘outbound CFIUS’ has lacked the basic facts necessary to warrant such a move. You hear of ‘loopholes’ and ‘gaps,’ but not a single real-world example.”⁵

Truth: The United States has the world’s largest capital markets, savviest investors, and most credible financial institutions. There are numerous examples of U.S. capital and expertise aiding the development of CCP military technology.⁶ In one of the most concerning examples, the Semiconductor Manufacturing International Corporation SMIC, the CCP’s semiconductor foundry champion, was supported with U.S. venture capital for years before being blacklisted by the Pentagon.⁷ An investigation by the House Select Committee on the Chinese Communist Party found that one American company, Blackrock, has invested more than \$429 million in companies that “act directly against the interest of the United States,” including military and technology companies.⁸

Myth: The Treasury Department doesn’t have data to support outbound investment restrictions on China.

*“I sent a letter to Secretary [Janet] Yellen asking for the data to justify outbound restrictions. Not one of my questions was answered. That’s because there is no data to begin with.”*⁹

Truth: The data are limited because U.S. national security agencies are not currently able to monitor investments in military technology development in China. That is precisely why new authorities are needed and why bipartisan legislative proposals have been advanced to generate such data by requiring notification of certain investments. The same politicians who claim that America lacks this information are trying to halt efforts to generate it, most recently by removing a bipartisan outbound investment review proposal from the National Defense Authorization Act for Fiscal Year 2024.¹⁰

Myth: American investors can outperform Chinese state-owned companies inside China.

*“If you oppose Beijing’s state-owned enterprises, you want more Western investment in China—not less.”*¹¹

Truth: China’s market is rigged in favor of the CCP’s favored companies, especially its state-owned companies, which are only growing more powerful in China’s economy.¹² American companies have been methodically forced out of China’s market and face rampant and relentless threats of intellectual property theft.

Myth: The CCP will let American investors “control” China’s tech companies.

*“If you are concerned about Chinese technology companies, you want more Americans in control of them—not fewer.”*¹³

*“No one in the CCP is proposing an outbound investment regime that would block Chinese nationals from taking over America’s technology innovators.”*¹⁴

Truth: The CCP will *never* allow Americans—or any other foreigner—to exercise meaningful control of China’s domestic technology firms. The CCP is currently detaining foreign executives, cutting off basic information about China’s economy, and inserting party cells into the governance structures of a growing number of private companies.

Myth: The CCP doesn’t want Western investment.

“Xi Jinping has been attacking Western influence in Chinese companies.”¹⁵

“Under the Xi dictatorship, China has attacked Western investment as a threat to the CCP’s hold.”¹⁶

Truth: The CCP wants access to American capital, know-how, and technology. Xi is simultaneously extending the CCP’s control of all economic activity in China while also seeking to draw in more foreign investment—in sectors the CCP chooses and on China’s terms.¹⁷

Myths and Truths About How to Stop Funding CCP Military Technology

Politicians close to Wall Street continue to oppose bipartisan legislation and a White House executive order that would require transparency for some U.S. investments in China. These advocates are instead supporting only the use of existing authorities to sanction individual Chinese companies without establishing new tools. Their attempts are misguided.

Myth: Sanctions alone can stop outbound investments that threaten national security.

“It is...unclear why the Administration believes that prohibiting...investments would be more effective than comprehensively using...sanctions.”¹⁸

Truth: Sanctions are inherently backward-looking. A genuine solution would prevent American investment from helping CCP companies to develop military technology in the first place instead of attempting to sanction them after they have already succeeded. U.S. sanctions policy toward China is riddled with a long list of failures and constantly behind the curve. Playing “whack a mole” by attempting to sanction individual Chinese companies and subsidiaries that are part of complex networks and well-versed in evading sanctions will not address the problem and will not work.

Myth: Sanctions are a “proven” solution.

“Sanctions and entity-based approaches...are more effective, immediate, multilateral, and stronger than bureaucratic and slow sector-based approaches at cutting off western financing for the CCP’s military-industrial complex.”¹⁹

Truth: Time and again, sanctions have proven inadequate to stop outbound investments that empower China’s military technology. The Chinese Military and Surveillance Company Sanctions Act²⁰ would allow the Administration to use only the powers it already has but refuses to use, even against known CCP military companies like Hikvision.

Myth: Congress must choose either sanctions or outbound investment prohibitions.

“We must use time-tested tools to get tough on China—Not novel concepts”²¹

Truth: While individual sanctions on specific entities are not a complete solution for risks stemming from outbound investment, they remain a useful tool with which to address known threats. Sanctions can and should be implemented more effectively and can be strengthened along with outbound investment prohibitions. These tools are not mutually exclusive.

A Real Solution

A genuine solution to national security threats stemming from U.S. outbound investments in China would include two essential elements:

Notification. U.S. companies seeking to sell controlled technology to a Chinese company are required to notify the Department of Commerce and receive a license. There is no such requirement for a U.S. investor who helps that Chinese company to develop the controlled technology inside China—and beyond the reach of U.S. national security agencies. Outbound investment reform must therefore begin with a notification requirement for investments in China that present national security risks.

Sectoral Prohibition. Outbound investment in China should be prohibited in sectors that produce dual-use technology with military applications. Covered sectors should include semiconductors, high-performance computing, data storage, artificial intelligence, quantum technology, biotechnology and pharmaceuticals, robotics, remote sensing, advanced communications, advanced materials, and space technology.

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Endnotes

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