PNTR: OPENING THE WORLD'S BIGGEST POTENTIAL MARKET TO AMERICAN FINANCIAL SERVICES COMPETITION

HEARING

BEFORE THE

SUBCOMMITTEE ON
FINANCE AND HAZARDOUS MATERIALS

OF THE

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PNTR: OPENING THE WORLD'S BIGGEST POTENTIAL MARKET TO AMERICAN FINANCIAL SERVICES COMPETITION

TUESDAY, MAY 23, 2000

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON FINANCE AND HAZARDOUS MATERIALS,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:40 p.m., in room 2123, Rayburn House Office Building, Hon. Michael G. Oxley (chairman) presiding.

Members present: Representatives Oxley, Shimkus, Towns, Barrett, Luther, and Rush.

Staff present: Robert Gordon, majority counsel; Linda Dallas Rich, majority counsel; Robert Simison, legislative clerk; Shannon Vildostequi, professional staff; Brian McCullough, professional staff; Consuela Washington, minority counsel; and Bruce Gwinn, minority professional staff.

Mr. OXLEY. The subcommittee will come to order. This week we will be called upon to vote on a pivotal issue. Many have called the vote on granting permanent normal trade relations with China the most significant vote before Congress in decades. In casting this vote, we will be choosing whether economic integration or economic isolation is most likely to foster democracy and capitalism in China. There is much to be desired of China's Democratic and economic record. The momentous legacy still permeates the country through State controls and social and economic life. Nevertheless, the last 20 years show a pattern of China moving toward a market economy.

Progress has been slow, and at times, frustrating. But the fact remains that China has become significantly more Democratic and capitalistic than it was in 1978, thanks mostly to the reforms of Deng Xiaoping. As a single remaining superpower, the United States, in its support of China's WTO accession, is critical to integrating China into our global free markets and rule of law.

While a negative vote for PNTR will not prevent China's accession to the WTO, it will put the United States businesses and workers at an overwhelmingly competitive disadvantage versus our competitors in Asia, Latin America and Europe. A negative vote means that only the United States will be denied the benefits, and protections of China's accession to the WTO will confer on all other WTO member countries.

China's accession to the WTO will facilitate the shift of economic power from state-owned enterprises to private sector market participants. An economic prosperity increases pressure for greater democracy. As Federal Reserve Board chairman Alan Greenspan recently observed, history has demonstrated that implicit in any removal of power from central planners and broadening of market mechanisms, as would occur under WTO, is a more general spread of rights to individuals. In fact, we have just witnessed this unfolding of democracy in South Korea and Taiwan over the last two decades, as they have integrated with international free markets. WTO accession will not only benefit China, essentially it will translate into greater global harmony.

Free trade is more likely to foster cooperation than hostility. As China's global interdependency grows, so will its compliance with international protocols. This is precisely why Taiwan supports China's accession into the WTO. For WTO members, including the United States, China's WTO accession means increase access to the world's largest potential market. That translates to new opportunities and new jobs for American businesses and workers. With an aging population of 1.3 billion people, the potential opportunities for American financial services and providers are quite dramatic.

It has been estimated that under the full benefits of China's WTO related market opening, our annual exports to that country would grow between $8 and $10 billion by the year 2005. In fact, the financial services agreement to which China agreed in the WTO negotiations represents the largest single trade agreement in history. It covers $60 trillion in banking, insurance and securities transactions each year. Furthermore, this trade agreement represents unilateral gain by American workers and businesses. China has offered major concessions in return for WTO membership, while the United States has agreed only to preserve its existing market access without any new concessions.

For example, China has unilaterally provided for greater U.S. market access in telecommunications and financial services and has agreed to phaseout numerous import quotas, licensing and ownership requirements and geographic restrictions, and just last week, the European Union reached agreement with China as WTO negotiations gained further concessions. Those benefits will accrue to all WTO members, including the United States, if and only if we approve PNTR tomorrow.

In addition to the opportunities a successful PNTR vote offers American companies and workers, a successful PNTR vote provides our companies and workers with protection in the form of the WTO dispute resolution system. The U.S. will be able to use that dispute resolution system to protect its rights with the support and pressure from 114 other WTO member countries who have similar interests in forcing open China's markets.

We must remember that China's WTO accession does not hinge upon this week's PNTR vote. WTO members will reap the benefits of China's accession, regardless of the congressional vote on PNTR. If the Congress votes for PNTR, we will share in those benefits; if we vote against it, we will not. This is a chance we should not pass up. Extending PNTR to China is not only good economic policy, it is a good way to influence political reform. It will be much easier to influence Chinese reform as a trading partner than as the only WTO member that refuses to extend PNTR to China.

Today we will hear from representatives of the finance, insurance and high-tech industries. They offer a vital perspective on how PNTR will impact our Nation's economy, our businesses, and our workers. I thank them all for their testimony. I look forward to hearing what each of you has to say.

That ends the opening statement by the chair. I am pleased now to recognize the gentleman from New York, the ranking member, Mr. Towns.

Mr. TOWNS. Thank you very much, Mr. Chairman. The subcommittee will consider the facts regarding the PNTR for China. This hearing is very important to the American public, particularly as it relates to the future of millions of American jobs. Some say it will improve our financial services industry, which is very important to my home State of New York, and I know that Ms. Cynthia Valko will testify in support of this viewpoint later on behalf of New York Life.

I would still say if we believe that the export of financial services will be enhanced when we are still waiting for the government of China to honor its agreements with New York Life, Chubb Insurance, and Metropolitan Life, which are all New York companies. We also must question China's unfair labor practices, disrespect for fundamental human rights, and their tax and threats against Taiwan.

Mr. Chairman, I am concerned about who will enforce the agreement between our two countries. I am also concerned about which enforcement method will be used to ensure that our agreement hold when our companies are not treated fairly by China. The most important question, though, I have, Mr. Chairman, is who will stop our jobs from going overseas to China?

For all of the above reasons, Mr. Chairman, I am opposed to PNTR for China. However, I will be pleased to hear the different views of our witnesses this afternoon. Thank you very much for holding the hearing.

Mr. OXLEY. I thank the gentleman. His time has expired.

[Additional statement submitted for the record follows:]

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

On the heels of the comprehensive market access agreement reached with China last fall, Congress will be considering legislation this week to provide permanent status to normal trade relations with China.

The agreement that the EU just reached with China last week makes China's accession to the WTO a virtual certainty. The question before us now is not whether China will join the WTO, but whether the United States will enjoy the benefits of the agreement we reached with China last fall. And whether the U.S. will have the same market access rights as our Japanese and European competitors.

The Chinese market agreements are sweeping in their scope, and present significant new opportunities for American businesses. That translates into more good jobs for American workers. The financial services agreement alone covers sixty trillion dollars in potential transactions each year. With a population of 1.2 billion people and very little available in the way of financial services, the Chinese market for insurance, banking, and securities is vast. But right now, without PNTR, American companies have virtually zero access to China's market.

The concessions to which China agreed in the high tech sector are also significant to U.S. companies—both high tech and financial companies. The convergence of finance and technology has changed the way our own financial markets work today. As the functions of finance become increasingly immersed in e-commerce and digital automation, the software and hardware that high-tech companies produce is becoming the backbone of the financial markets. These dramatic changes improve the lives of Americans, as well as consumers abroad.

There is much work to be done to improve the rights, and the lives, of Chinese citizens. I strongly believe that by opening markets between the United States and China, we will be better able to achieve those goals. I look forward to the testimony of our witnesses today.

Mr. OXLEY. Now we will turn to our distinguished panel. Let me introduce them beginning with Mr. Newhouse on my right. Mr. Stephan F. Newhouse managing director, member of the management committee, Morgan Stanley Dean Witter. Mr. James S. Whittaker, director of international public policy from Hewlett-Packard Company. Did I see you on C-SPAN this morning?

Mr. WHITTAKER. You did.

Mr. OXLEY. Very good. This will be a lot friendlier. Ms. Cynthia Y. Valko, executive vice president of New York Life. Mr. Jesse J. Watkins, managing director, Herbert L. Jamison & Company LLC, from West Orange, New Jersey, on behalf of the Council of Insurance Agents and Brokers. Mr. Edward L. Yingling, no stranger to this subcommittee, deputy executive vice president, executive director of government relations with American Bankers Association, and Mr. Greg Mastel, director, Global Economic Policy Project, New America Foundation here in Washington.

Gentlemen and lady, thank you all for being with us, and we will begin with Mr. Newhouse. Let me ask if you could all try to stay to the 5-minute rule. We can facilitate this. I know Mr. Newhouse has to return to New York. We would love to be able to get through the testimony and then have an opportunity for members to ask questions to all of you. With that, I recognize Mr. Newhouse.

STATEMENTS OF STEPHAN F. NEWHOUSE, MANAGING DIRECTOR, MEMBER OF THE MANAGEMENT COMMITTEE, MORGAN STANLEY DEAN WITTER; JAMES S. WHITTAKER, DIRECTOR, INTERNATIONAL PUBLIC POLICY, HEWLETT-PACKARD COMPANY; CYNTHIA Y. VALKO, EXECUTIVE VICE PRESIDENT, NEW YORK LIFE INTERNATIONAL, INC.; JESSE J. WATKINS, MANAGING DIRECTOR, HERBERT L. JAMISON & CO., LLC, ON BEHALF OF THE COUNCIL OF INSURANCE AGENTS AND BROKERS; EDWARD L. YINGLING, DEPUTY EXECUTIVE VICE PRESIDENT, EXECUTIVE DIRECTOR OF GOVERNMENT RELATIONS, AMERICAN BANKERS ASSOCIATION; AND GREG MASTEL, DIRECTOR, GLOBAL ECONOMIC POLICY PROJECT, NEW AMERICA FOUNDATION

Mr. NEWHOUSE. Thank you, Mr. Chairman. Good afternoon. Again, thank you, Mr. Chairman, and good afternoon to you and members of the subcommittee. My name is Steve Newhouse. I am managing director and vice chairman of the Institutional Securities and Investment Banking Group at Morgan Stanley Dean Witter and Company.

Morgan Stanley Dean Witter is one of the largest global financial services firms and maintains leading market positions in each of its three business segments, securities, asset management, and credit services. The company provides its products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions, and individuals.

We support with enthusiasm your decision to hold these hearings to consider the implications for America's financial services industry of granting permanent normal trading relations to China. We are honored to have been invited to testify and to share with you Morgan Stanley Dean Witter's views on this timely and critical public policy issue. Without a doubt, granting permanent normal trading relations or PNTR to China is the single most important international trade issue to be considered by the 106th Congress and by this administration.

Morgan Stanley Dean Witter has over 560 offices operating in 25 countries through the world. We have been active in China for almost two decades. We have offices in Beijing, Shanghai and Hong Kong. In 1995, Morgan Stanley Dean Witter became the first foreign investment bank to participate in a domestic joint venture investment bank in China. So we know firsthand that the continued opening of the foreign markets to U.S. goods and services has been and continues to be an essential driver of this country's economic growth and success.

China, the world's fifth largest market and the U.S.'s fourth largest trading partner, stands ready to join the biggest block of trading nations in the world, the World Trade Organization. In order to do so, it has agreed to open its markets wider than ever before, making unprecedented unilateral concessions that will dramatically increase U.S. exports of goods and services. Both President Jiang Zemin, and more particularly the Premier Zhu Rongji, have put their personal and political credibility on the line for WTO membership. They have done so in the belief that economic openness and reform are the only answers to the economic challenges faced by China over the next decade.

This commitment to gain WTO membership was underscored last Friday by additional concessions made by the Chinese to reach agreement with the European Union on the issue of China's entrance into the WTO. Parenthetically, that historic agreement with a group of trading partners, which is, in the aggregate, larger than the United States, makes an optimal bilateral trade relationship between China and that country even more imperative.

We believe the United States must not miss this historic opportunity to embrace the commitments China has made and to welcome it fully into the world trading system on a most favored nation basis. The historic agreement reached by U.S. and Chinese negotiators in November 1999 is, as you are aware, both deep and broad-based, covering both the goods and services sectors. For the securities industry, the commitments from China, including minority ownership in local securities firms and asset management firms, creates a strong platform for continued development of China's capital markets. The commitments also importantly include grandfathering all of our existing activities and investments in that market place.

The opportunities for financial services firms in China are enormous and will become even greater once China joins the WTO. For example, over the next decade, the financial resources required to be invested in improvements to China's communications and transportation infrastructure and energy-related capital equipment are estimated to be over $1 trillion. The intermediation of both the domestic and international capital flows required to fill these requirements is one of the major business objectives of the next decade for U.S. financial services firms as well as for our competitors around the globe.

Herein lies the challenge: For if Congress fails to grant PNTR to China, when China enters the WTO, American firms will be deprived of the benefits of China's commitments in all sectors, even while other countries reap those benefits. With PNTR, U.S. firms, including financial services firms, will be able to enter and expand in China on the same terms as our international competitors.

At its core, bringing China into the WTO increases China's ties with the international community. And when U.S. companies establish operations in China, they bring with them the best practices that they have observed around the world. Our own experience as a partner in China's first domestic joint venture investment bank, China International Capital Corporation, provides us with a unique perspective on China's development and with a unique opportunity to assist in the development of China's economy and its capital markets. We are engaged in a number of dialogs in China across a wide variety of businesses, energy, technology, telecommunications, and banking, to name a few. We have been profoundly impressed with the high level of progress China has made and by its consistent commitment to reforming its economy.

We believe economic stability in China during the Asian financial crisis significantly contributed to the turnaround in the regional economies and contributed to the global economic recovery. We believe China is deeply committed to developing its capital markets and to becoming an even greater participant in the global economy. We believe that the trade agreement reached by the U.S. and Chinese negotiators in November is a demonstration of that commitment. Finally, we believe the agreement will play a significant role in advancing the restructuring that is the linchpin of economic reform in China.

Let me close with a personal observation. In my 25 years in international finance, I have spent a great deal of time working with emerging economies and emerging democracies. I have become convinced that the economic and financial reform and political and social reform are inextricably tied together. They are two sides of the same coin. Once a country accepts as an imperative the need to join the global economy, it has to make an implicit decision about a number of non-economic issues. It must embrace the rule of law or its trading partners will decline to enter into long-term commercial agreements with it. It must open its lines of communication and make transparent its disclosures about itself or capital will not flow across its borders and it must educate its people with the breadth and depth not needed in a closed economy, if they are to compete in a global one.

We urge you to support permanent normal trade relationship status with China because we believe it is in the best interest of the United States, the global economies and the world trading system.

Thank you very much for this opportunity to testify.

[The prepared statement of Stephan F. Newhouse follows:]

PREPARED STATEMENT OF STEPHAN F. NEWHOUSE, MANAGING DIRECTOR & VICE CHAIRMAN, MORGAN STANLEY DEAN WITTER & CO.

Mr. Chairman and Members of the Committee. Good afternoon. I am Stephan Newhouse, Managing Director and Vice Chairman of Institutional Securities and Investment Banking Group of Morgan Stanley Dean Witter & Co.

Morgan Stanley Dean Witter & Co. (the "Company") is a global financial services firm that maintains leading market positions in each of its three business segments—Securities, Asset Management and Credit Services. The Company provides its products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals.

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The opportunities for financial services firms in China are enormous and will become even greater once China joins the WTO. For example, over the next decade, the financial resources required to be invested in improvements to China's communications and transportation infrastructure and energy-related capital equipment are estimated to be over $1 trillion. The intermediation of both the domestic and international capital flows required to fill these requirements is one of the major business objectives of the next decade for U.S. financial services firms as well for our competitors around the globe.

Herein lies the challenge. For if Congress fails to grant PNTR to China, when China enters the WTO, American firms will be deprived of the benefits of China's commitments in all sectors, even while other countries reap those benefits. With PNTR, U.S. firms, including financial services firms, will be able to enter—and expand—in China on the same terms as our international competitors.

At its core, bringing China into the WTO increases China's ties with the international community. And when U.S. companies establish operations in China they bring with them the best practices that they observe around the world.

Our own experience as a partner in China's first domestic joint venture investment bank, China International Capital Corporation Limited (CICC), provides us with a unique perspective on China's development and with a unique opportunity to assist in the development of China's economy and its capital markets. We are engaged in a number of dialogues in China across a wide variety of businesses—energy, technology, telecommunications and banking, to name a few. We have been profoundly impressed with the high level of progress made by China and by its consistent commitment to reforming its economy.

We believe economic stability in China during the Asian financial crisis significantly contributed to the turnaround in the regional economies and contributed to the global economic recovery. We believe China is deeply committed to developing its capital markets and to becoming an even greater participant in the global economy. We believe the trade agreement reached by US and Chinese negotiators in November is a demonstration of that commitment. Finally we believe the agreement will play a significant role in advancing the restructuring that is the linchpin of economic reform in China.

Let me close with a personal observation. In my 25 years in international finance, I have spent a great deal of time working with emerging economies and emerging democracies, I have become convinced that economic and financial reform and political and social reform are inextricably tied together. They are two-sides of the same coin. Once a country accepts as an imperative the need to join the global economy it has made an implicit decision about a number of noneconomic issues. It must embrace the rule of law or its trading partners will decline to enter into long term commercial agreements. It must open its lines of communication and make transparent its disclosures about itself or capital will not flow across its borders. And, it must educate its people with a breadth and depth not needed in a closed economy if they are to compete in an open global one.

We urge you to support Permanent Normal Trade Relations Status for China because we believe it is in the best interests of the United States, the global economy and the world trading system.

Thank you again for this opportunity to testify. I will be pleased to answer whatever questions you have or to provide additional information for the hearing record.

Mr. OXLEY. Thank you.

Mr. Whittaker?

STATEMENT OF JAMES S. WHITTAKER

Mr. WHITTAKER. Chairman Oxley, members of the subcommittee, good afternoon. My name is Jim Whittaker and I am director of international public policy with Hewlett Packard Company. I am testifying before you today as chairman of the U.S. High-Tech Industry Coalition on China. The Coalition is comprised of 13 high technology trade associations, which represents U.S. manufacturers of semiconductors, computers, electronics software, telecommunications equipment as well as U.S. service providers and Internet companies.

U.S. China bilateral WTO accession agreement that Ambassador Barshefsky negotiated is a solid win for the U.S. high-tech industry. Under that agreement, China is committed to eliminate tariff and non-tariff barriers to trade, remove regulatory hurdles and investment restrictions on foreign firms. As a result, U.S. high-tech industries are poised to expand sales and exports to this rapidly growing market to increase high wage American jobs, and to maintain our technological leadership and competitiveness in international markets.

However, in order for industry to reap these benefits, congressional approval of PNTR is necessary. For this reason, we believe that establishing permanent normal trade relations with China is the most important vote that Congress will make in support of American high-tech industry this year.

A few quick words about our industry. The high-tech sector is a strong and important contributor to the U.S. economy. It is the largest manufacturing sector in the U.S. employing 5 million Americans last year. It is our Nation's top manufacturing exporter with 25 percent of total exports, and its employees earn 82 percent higher than the average private sector worker.

Over the next few years, China is expected to become one of the largest high technology markets in the world. According to International Data Corporation figures, annual growth rates for many segments of the high-tech sector will be 20 to 40 percent annually. Indeed, China's semiconductor and cell phone markets are projected to be the world's second largest by 2003, with a PC market projected to be number two in the world next year. More than 20 million Chinese will be on-line next year, and we expect that to go as high as 35 million in the following year.

Given these opportunities and the strong terms of the bilateral agreement, China's WTO accession will provide significant opportunities and benefits to the high-tech industry, including increased exports and related jobs.

I would like to just take a few minutes to highlight a few of the changes that will help us the most. One, China has agreed to adopt the information technology agreement, which eliminates tariffs altogether on an array of IT and telecom products by the year 2005.

Two, China will, for the first time, permit American and other foreign companies to directly import and export products. It will also, for the first time, agree to permit us to distribute directly our products and provide after-sales service repair and maintenance.

Three, China will immediately become subject to the TRIPs agreement on intellectual property protection. We believe that the TRIPs agreement is the best vehicle available to us to combat piracy of intellectual property and to support improved IT by Chinese's governmental authorities.

Four, China has agreed to implement the TRIMS agreement upon accession. This means that it will not condition investment approvals, import licenses, or any other import approval on performance requirements of any kind, including local content requirements, technology transfer, or requirements to conduct R&D in China.

Five, China has agreed that it will ensure that state-owned and state-invested enterprises will make purchases and sales based solely on commercial considerations providing U.S. firms with the opportunity to compete on nondiscriminatory terms and conditions.

Six, China agreed, for the first time, to open its telecom market to foreign service providers. In the important area of value-added services, including Internet services, China has agreed to allow up to 50 percent foreign ownership 2 years after accession. In addition, China agreed to sign on to the WTO BTA agreement and committed to a set of regulatory principals contained in the so-called reference paper to the BTA.

And finally, in the area of antidumping, the bilateral agreement enables the U.S. to maintain strong protections against dumping for 15 years. Since China's economy is not fully market-oriented yet, it is critical that the United States maintain its ability to utilize its existing non-market economy and methodology in the application of antidumping laws.

In conclusion, the American high-tech industry has been the forefront of U.S. economic expansion and technological leadership. Ambassador Barshefsky was able to obtain an historic market opening package. We would hate to see these advantages to our foreign competition. Granting China PNTR coupled with significant market reforms in China embodied in its WTO commitments will ensure our industry is able to participate fully in this critical market.

Along with many of America's leaders across the political spectrum, we believe that engagement, not isolation, will lead to improved economic and social conditions in China. The terms for China's accession in the WTO will help China to continue on its path of economic reform, which we believe will lead to positive changes in many areas. Already, American high-tech businesses are having a positive impact on China by bringing our best practices in the areas of human resource, environmental and business management to China.

For these reasons, we support the establishment of PNTR with China and are urging Congress to pass H.R. 4444.

Thank you, Mr. Chairman.

[The prepared statement of James S. Whittaker follows:]

PREPARED STATEMENT OF JAMES S. WHITTAKER, DIRECTOR, IMTERNATIONAL PUBLIC POLICY, HEWLETT-PACKARD COMPANY, ON BEHALF OF U.S. HIGH-TECH INDUSTRY COALITION ON CHINA

Chairman Oxley, members of the Subcommittee, good afternoon. My name is Jim Whittaker, and I am Director of International Public Policy with Hewlett-Packard Company. I have the honor of testifying before you today as the Chairman of the U.S. High-Tech Industry Coalition on China.

The High-Tech Coalition on China is comprised of thirteen high-technology trade associations, which work together on our highest priority public policy issue this year—China's accession to the World Trade Organization (WTO). The coalition represents U.S. manufacturers of semiconductors and semiconductor equipment and materials, computers, electronics, software, and telecommunications equipment, as well as U.S. service providers and Internet companies. A list of coalition members is attached.

The U.S.-China bilateral WTO accession agreement reached on November 15, 1999 is a solid win for U.S. high-technology industries. In that agreement, China committed to comprehensive reform of its economy, and to eliminate tariff and non-tariff barriers to trade, regulatory requirements and investment restrictions. As a result of this historic step, U.S. high-tech industries are poised to expand exports to this rapidly growing market, increase high-wage American jobs, and continue our technological leadership and competitiveness in international markets.

For our industry to reap the benefits of these market opening concessions that China has made, however, Congressional approval of permanent normal trade relations (PNTR) with China is necessary.

IMPACT OF U.S. HIGH-TECHNOLOGY INDUSTRY ON THE U.S. ECONOMY

The high-tech sector is a strong and important contributor to the U.S. economy. According to the American Electronics Association data from *Cyberstates 4.0,* the high-tech industry is the largest manufacturing sector in the United States, employing 5 million Americans in 1999. This was twice as many as in auto manufacturing and services, and far exceeds the one million workers in the chemical manufacturing industry. The high-tech industry added over 1.2 million jobs to the U.S. economy between 1993 and 1999, a 32 percent increase.

In addition, the high-tech industry also provides its employees with salaries 82 percent higher than the average private sector wage. In 1998, the average high-tech wage was nearly $58,000 a year, while the average private sector wage was almost $32,000. While high-tech wages increased 29 percent, private sector wages grew only 8 percent between 1993 and 1998.

Federal Reserve Chairman, Alan Greenspan, recently reported that the high-tech sector has been responsible for nearly half of U.S. domestic GDP growth since 1994. Please see the attached chart.

In 1998, American high technology companies lead all other industries in private-sector expenditures on research and development (R&D). High-tech companies per-formed $55 billion in R&D—a 63 percent more than in 1993. Total industrial R&D amounted to $145 billion in 1998, a 53 percent increase since 1993.

The high-tech industry is our nation's the top manufacturing exporter. In 1999, the high-tech sector exported $181 billion. High-tech exports comprised 25 percent of total U.S. exports in 1999. Based on U.S. Commerce Department data, China represented the 14th largest high-tech export market in 1999, with high-tech exports exceeding $3.3 billion—a 121 percent increase since 1993.

OPPORTUNITIES IN THE CHINESE MARKET

In the next decade, China is expected to become one of the largest markets in the world. According to International Data Corporation figures, annual growth rates for many high-tech products are increasing 20 to 40 percent. The following provides an overview of the Chinese market for some of the key high-tech sectors.

Semiconductors and Semiconductor Equipment and Materials

The current semiconductor market in China is estimated to be up to $8 billion per year. Some analysts expect it to become the third largest semiconductor market by 2001 (ahead of Germany, but behind Japan and the United States) and the second largest by 2010. The current semiconductor equipment and materials market in China is estimated to be over $1 billion per year and is projected to reach almost $4 billion in 2003.

Computers

The market in China for computers is expanding rapidly, averaging 37 percent growth per year for the past three years. The Chinese market will continue to grow—International Data Corporation predicts that by 2001, China will be the second largest PC market after the US and Japan. More than 120 million Chinese citizens plan on buying a computer in the next two years.

Software

China's software market is growing at 28 percent a year. High growth rates will continue as Internet use in China continues to climb and piracy rates decrease. The Internet is projected to reach an estimated 20 million people in China by the end of 2000.

Telecommunications

China's market for cellular telecommunications is growing at a tremendous rate. By the end of 1999, China boasted approximately 40 million cellular subscribers, bringing it closer to its target of becoming the world's second largest cellular market with approximately 60 million subscribers. Only the cellular market of the United States is projected to be larger than China's by the end of this year. With the market potential for 3rd generation mobile communications also taken into consideration, China promises market opportunities for years to come.

Internet

More than 9 million Chinese are already on-line, and in the next few years China is expected to become one of the largest Internet markets in the world. This growing market offers tremendous commercial opportunities to U.S. firms. By participating in this market, U.S. Internet service and content providers can make sure that vital social services—such as education, communications and telemedicine—are delivered across the Internet. We can also lay the groundwork for e-commerce and the economic growth, productivity and jobs it will generate.

BENEFITS OF CHINA'S WTO ACCESSION

As the China accession negotiations began in earnest, the High-Tech Industry Coalition on China set forth its objectives for our U.S. negotiators. The package that they have come back with meets those objectives.

Under the terms of the November 1999 bilateral agreement, China's WTO accession would provide significant opportunities and benefits to U.S. high-tech industries. A summary of some of these key benefits follows.

• *Information Technology Agreement:* China has agreed to adopt the Information Technology Agreement (ITA), which eliminates tariffs on products such as computers, telecommunications equipment, semiconductors, semiconductor manufacturing equipment, computer equipment and other high technology products. China has agreed to eliminate nearly all of its IT tariffs (which currently average 13%) by 2003, and the remainder by 2005.

The benefits to U.S. high-tech industries are clear: duty-free entry of U.S. products should result in increased exports, sales and market share of U.S. products. In addition, American high-tech companies producing in China will have access to lower cost inputs. Finally, China's adoption of the ITA will help to combat smuggling, since the incentive for the creation a black market to circumvent tariff barriers will be removed.

• *Trading and Distribution Rights:* China will, for the first time, permit American and other foreign companies to directly import and export products—so-called trading rights. China has also, for the first time, agreed to permit American and other foreign companies to directly distribute their products, including wholesale and retail and after-sale service, repair, maintenance, and transport.

For American high-tech industries, the right to provide direct service is essential to control quality and ensure the authenticity of the spare parts being delivered. Indeed, in other important overseas markets, American firms increasingly are using quality service as a strategic weapon against foreign competitors to win customers and grow market share. The inability to deal directly with end-users is a particular problem in the semiconductor industry, where the design and development of application-specific chips requires extensive contact between semiconductor producers and the ultimate end-users of the chips.

Since China has agreed that all restrictions on trading and distribution rights will be eliminated three years after accession for most sectors, the benefit will be the ability for our industries to quickly excel in China's rapidly growing, competitive information technology market.

• *Investment Restrictions:* China has agreed to implement the WTO Trade-Related Investment Measures (TRIMS) Agreement upon accession. This means China will eliminate and cease enforcing trade and foreign exchange balancing requirements. China will also eliminate and cease enforcing local content requirements, and refuse to enforce contracts imposing these requirements. China will guarantee that laws or regulations to the transfer of technology or other know-how will be consistent with WTO obligations to protect intellectual property rights and trade-related investment measures.

China has also agreed that, upon accession, it will not condition investment approvals, import licenses, or any other import approval process on performance requirements of any kind, including: local content requirements, offsets, transfer of technology, or requirements to conduct research and development in China.

These provisions will help protect American firms against efforts by some Chinese officials to force the transfer of U.S. commercial technology to Chinese firms, which has been a significant issue for U.S. high-tech companies seeking market access or the right to invest in China.

• *State-Owned and State-Invested Enterprises:* China has agreed that it will ensure that state-owned and state-invested enterprises will make purchases and sales based solely on commercial considerations, providing U.S. firms with the opportunity to compete for sales and purchases on non-discriminatory terms and conditions. This is an important point for U.S. high-tech industries, since state-owned and state-invested enterprises currently control a significant share of domestic and international trade in commercial high-tech goods in China.

• *Telecommunications Services:* Included in China's concessions in the telecom sector, China agreed to open its telecom market to foreign service providers according to the following schedule:

- Phase-in of foreign participation in paging/value-added services in two years, allowing up to 50 percent ownership by foreign investors;
- Phase-in of foreign participation in mobile/cellular services over five years, allowing up to 49 percent ownership by foreign investors;
- Phase-in of foreign participation in fixed line/international long distance services over six years, allowing up to 49 percent ownership by foreign investors.

In addition, China agreed to sign onto the WTO Agreement on Basic Telecommunications Services (BTA). The BTA commits participating countries to open their telecom services markets. China has committed to a set of regulatory principles contained in the so-called Reference Paper to the BTA, and has therefore made specific commitments to open up its telecom services markets. These include providing access to the public telecom networks of incumbent suppliers under non-discriminatory terms and at cost-oriented rates. China also agreed to technology-neutral scheduling, meaning technology choices are made as commercial decisions, rather than government mandate.

The Ministry of Information Industry (MII) is preparing China for competition from foreign service providers after China's accession to the WTO. To meet this goal, China's second telecom carrier, China Unicom, is slated to buildout an additional national cellular network in 2000 based on Code Division Multiple Access (CDMA) technology. This development is very positive for U.S. telecom equipment manufacturers, as they are the world's leading suppliers of this technology. In addition, China introduced a new service provider into the market in 1999, China Netcom (CNC). This new company will focus on the provision of Internet Protocol (IP) telephony, allowing more efficient use of bandwidth on the Chinese networks.

• *Intellectual Property:* By joining the WTO, China will become subject to the Agreement on Trade Related Aspects of Intellectual Property (TRIPs). Moreover, China has agreed to be subject to all TRIPs obligations upon accession, without any transition period. The TRIPs agreement is the best vehicle available to high-tech industries to combat piracy of intellectual property and to create a healthy environment for the development of information technology in China.

Industry experts estimate that 95 percent of the business applications software used in China was pirated in 1998 (the last year for which data is available), depriving the software industry of nearly $1.2 billion in licensing revenue. If China were to bring its legal system into compliance with the standards in the TRIPs Agreement, the U.S. software industry should be much more able to enforce its rights in Chinese courts and administrative tribunals. However, the United States will be unable to ensure Chinese compliance with the TRIPs Agreement absent the grant of PNTR to China.

• *Antidumping:* The bilateral agreement enables the United States to maintain strong protections against dumping. Since China's economy is not fully market-oriented, it is critical that the United States maintains its ability to utilize its existing non-market economy methodology in the application of U.S. antidumping laws. The United States and China have agreed that the United States may maintain this current methodology for 15 years after the date of China's accession to the WTO.

PNTR IS NECESSARY FOR THE U.S. TO BENEFIT FROM CHINA'S WTO ACCESSION

The United States must approve permanent normal trade relations (PNTR) status for China in order for U.S. firms to receive the benefits of China's accession to the World Trade Organization (WTO). If China accedes to the WTO and the U.S. Congress does not pass legislation granting China PNTR, it is expected that the Administration would invoke its right of "non-application" under Article XIII of the WTO Agreement, as has been done with respect to other countries subject to the Jackson-Vanik Amendment. This would be done at the time China formally accedes to the WTO. Even though China would become a WTO member, the United States would not treat China as a WTO member. Moreover, China would not be required to treat the United States as a WTO member.

Without PNTR, an historic opportunity would be jeopardized for U.S. companies and their workers. The terms of the landmark U.S.-China bilateral agreement concluded in November and all other terms of China's WTO accession package would not apply to U.S.-China trade and investment, except to the extent that existing bilateral agreements make the WTO agreement terms binding between the two countries.

While the United States would receive some modest benefits, such as tariff cuts, under the terms of the 1980 bilateral agreement between the United States and China, many of the hard-fought concessions by the Chinese are not covered by this agreement. For example, China's agreement to eliminate forced technology transfer and investment requirements would not be extended to the United States. Nothing in the 1980 agreement requires the Chinese government to ensure that its state-owned and state-invested enterprises make their purchases solely on commercial terms, while China agreed to this commitment in the WTO accession agreement. Without PNTR, U.S. companies would not benefit from China's agreements to allow distribution rights for foreign companies and to allow investment in telecom and Internet services. Additionally, the United States would not have access to the WTO dispute settlement process to enforce intellectual property and other rights in the case of any noncompliance by China.

ANNUAL NTR EXTENSION IS NOT SUFFICIENT

Article I of the General Agreement on Tariffs and Trade (GATT) requires that WTO members provide "unconditional" MFN treatment to other WTO members. This principle is a cornerstone of the WTO and an open global trading system.

Some have argued that the United States can meet this unconditional MFN obligation, and thus be entitled to China's WTO concessions, as long as Congress renews NTR on a continual basis. But under the Jackson-Vanik Amendment to the Trade Act of 1974, China's MFN status is tied to annual Presidential findings or waivers regarding freedom of emigration, which can be overridden by Congress through a joint resolution of disapproval. Continued annual renewal of China's NTR status would violate WTO rules because it would be *conditional* (on freedom of emigration per the Jackson-Vanik Amendment) and *discriminatory* (requiring procedures for China that are not applied to other WTO members). Approval for *permanent* NTR is necessary to meet the WTO's unconditional MFN obligation.

CONCLUSION

The American high-tech industry has been at the forefront of U.S. economic expansion and technological leadership. Granting China PNTR, coupled with the significant market reforms in China embodied in its WTO commitments, will enable our industry to expand its market presence and business opportunities in this critical market.

Moreover, access to American commercial information technology enables people worldwide to improve business efficiency across all sectors, enhance educational and social opportunities, and connect with one another. Improved market access for U.S. commercial information technology in China will help to advance economic and social reform in China. A timely congressional vote granting PNTR to China is a critical and necessary step toward securing this goal.

U.S. HIGH-TECH INDUSTRY COALITION ON CHINA

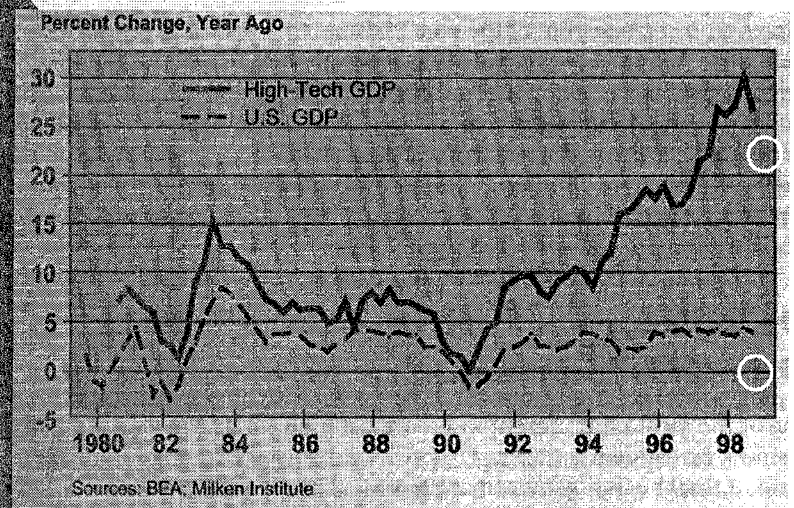
American Electronics Association; Business Software Alliance; Computer Systems Policy Project; Computing Technology Industry Association; Consumer Electronics Association; Electronic Industries Alliance; Information Technology Industry Council; National Venture Capital Association; Semiconductor Industry Association; Semiconductor Equipment & Materials International; Software & Information Industry Association; Telecommunications Industry Association; and United States Information Technology Office.

U.S. High-Tech Industry: America's Engine of Economic Growth

- Largest manufacturing sector -- by employment, by sales and by exports
- Responsible for 44% of domestic economic growth since 1994
- Highest sectoral wage payer
  - high-tech workers earn 77% more than average private sector wage
- Leading sector for investment overseas, stimulating substantial exports
- Leading sector in R&D expenditures

U.S. High-Tech Industry Coalition on China

Contribution of IT to Domestic GDP



U.S. High-Tech Industry Coalition on China

PNTR: Our #1 Priority

To stay in front of competitors

To ensure rules-based commercial policies, with meaningful enforcement

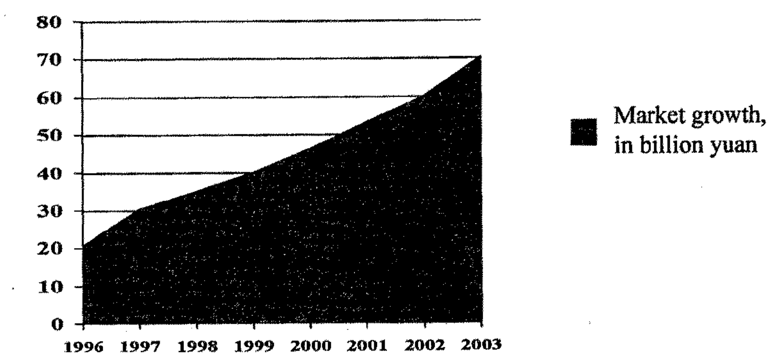
To benefit American workers, strengthen high-tech industry and contribute to U.S. economic growth

China is a Key Market

- China's rapidly expanding IT market offers major opportunities for U.S. high-tech exports & investment
  - High-tech exports to China grew nearly 500% between 1990 and 1998
- China is now the largest IT market in Asia, excluding Japan, with 20-40% annual growth
- IT is the linchpin of China's economic development

China's Semiconductor Market

China is expected to become the third largest semiconductor market in the world by 2001 and the second largest by 2010.

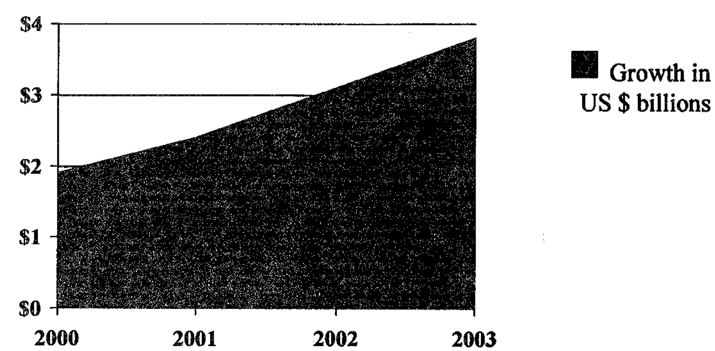


U.S. High-Tech Industry Coalition on China

China's Market for Semiconductor Equipment and Materials (SEM)

The current SEM market in China is over $1 billion.

This market is projected to be $4 billion in 3 years.



U.S. High-Tech Industry Coalition on China

China in the WTO Fixes Real Problems: SEMICONDUCTORS

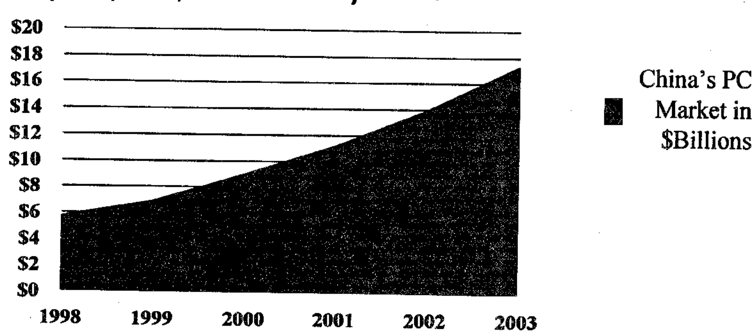
Current Situation	With this Agreement
Tariffs encourage smuggling	✓ Tariffs eliminated
Foreign investment conditioned on tech transfer/ performance requirements	✓ Tech transfer requirements and investment restrictions eliminated
Restrictions on trading/ distribution rights prevent direct contact with end-users	✓ Trading and distribution rights granted
IPR concerns	✓ Adherence to TRIPS, with enforcement
High level of state investment in electronics industry	✓ State-invested enterprises must purchase on commercial basis only
	✓ Non-market economy antidumping methodology preserved for fifteen years

U.S. High-Tech Industry Coalition on China

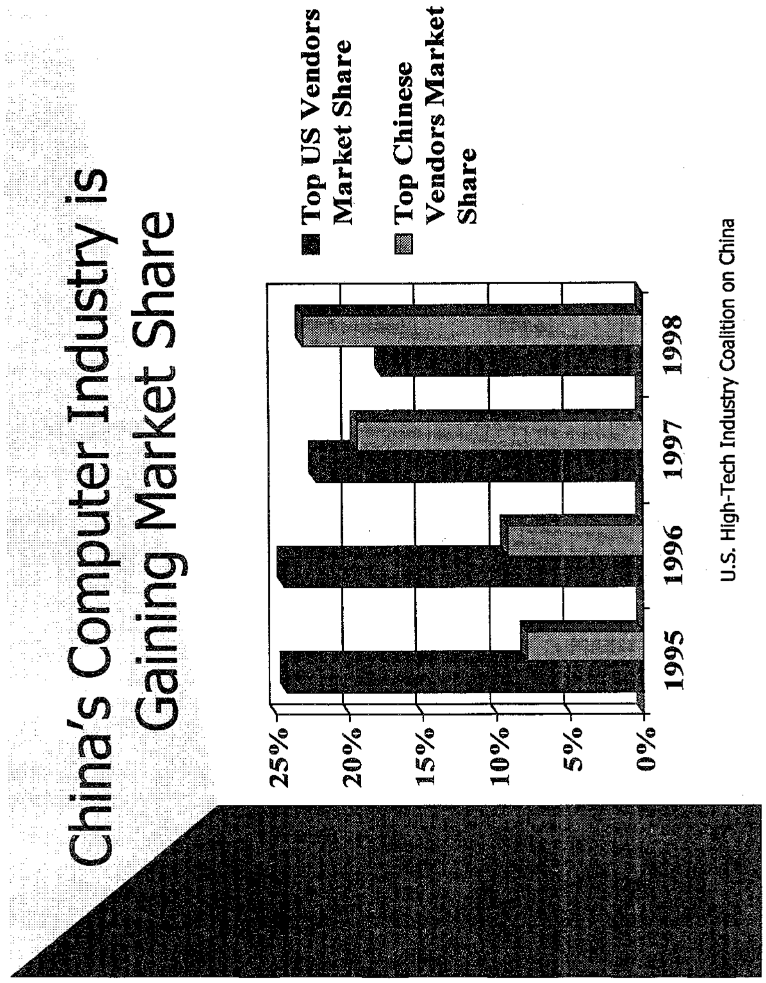
China's PC Market is Exploding

China was the world's 6th largest PC market in 1997 and will be the world's second largest in 2001.

China's PC market will grow from nearly $7 billion last year, to $17 billion by 2003.



U.S. High-Tech Industry Coalition on China


China's Computer Industry is Gaining Market Share
Top US Vendors Market Share
Top Chinese Vendors Market Share
25%
20%
15%
10%
5%
0%
1995
1996
1997
1998
U.S. High-Tech Industry Coalition on China

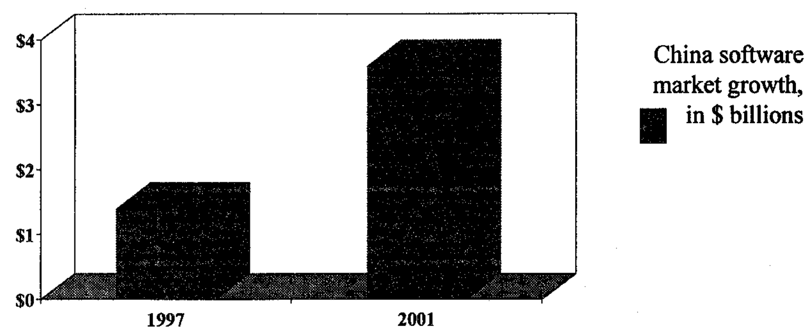
China in the WTO Fixes Real Problems: COMPUTERS

Current Situation	With this Agreement
Competitive disadvantage on price: 10% tariff wall	✓ Zero Tariffs by 2005
Must use costly "middleman" for after-sales service and support	✓ Full trading and distribution rights within 2 years
Investment sometimes conditioned on tech transfer, performance requirements	✓ Adoption of TRIMS upon accession

U.S. High-Tech Industry Coalition on China

China's Burgeoning Software Market

China's $3 billion software market is expected to grow nearly 30% per year for the next five years. 95% of software sold in China is pirated, costing US software companies $800 million/year (1998).



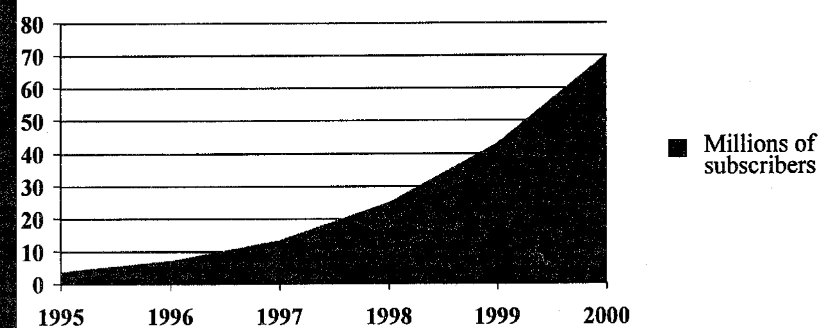
U.S. High-Tech Industry Coalition on China

China in the WTO Fixes Real Problems: SOFTWARE

Current Situation	With this Agreement
95% software sales are pirated products	✓ Adoption of TRIPS upon accession, with enforcement
Tariff wall	✓ Zero Tariffs by 2005

Explosive Growth in China's Cellular Phone Use

This year China will be the 2nd-largest market for cell phones in the world, second only to the U.S.



U.S. High-Tech Industry Coalition on China

China in the WTO Fixes Real Problems: TELECOMMUNICATIONS

Current Situation

- Foreign equity ownership in services banned
- Limited service by geography, type of technology
- Myriad of quotas, import licenses on equipment

With this Agreement

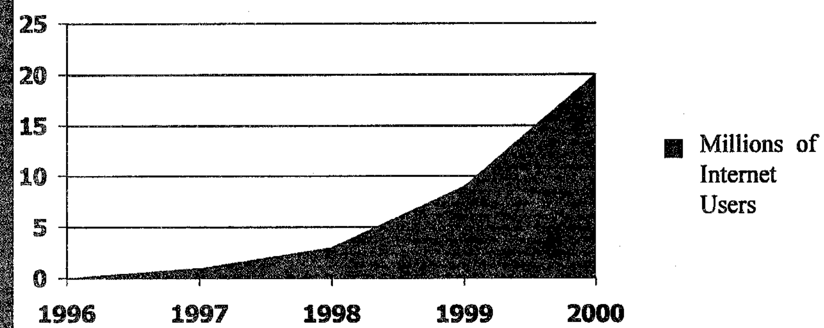
- ✓ 49% ownership in all services (cellular/mobile - 5 yrs./ fixed line/int'l - 6 yrs.), 50% in value-added, paging (2 yrs.)
- ✓ No geographic restrictions; technology-neutral scheduling; independent regulator
- ✓ Non-discriminatory licensing and elimination of quotas

U.S. High-Tech Industry Coalition on China

China's Internet Economy is Booming

20 million Internet users are expected by 2001.

Over 150 ISPs are currently operating in China.



U.S. High-Tech Industry Coalition on China

China in the WTO Fixes Real Problems: INTERNET

Current Situation	With this Agreement
China bans foreign ownership in service	✓ Allows 50% ownership within 2 years
Investment sometimes conditioned on tech transfer	✓ Adoption of TRIMS upon accession
China developing Internet/E-Commerce Framework	✓ Allows U.S. to work with China on international rules and practices

China's WTO Deal Achieves Every Objective of the U.S. High-Tech Industry

- Eliminates tariffs on IT products by 2005
- Ensures commercial rules for purchases by state-owned and -invested enterprises
- Expands trading and distribution rights
- Phases-out non-tariff measures
- Eliminates investment restrictions and tech-transfer requirements
- Ensures intellectual property protection
- Provides access for foreign telecom & Internet service providers

U.S. High-Tech Industry Coalition on China

Expanded Market Access in China Strengthens America's New Economy

- Expanded U.S. exports & investment for the U.S. high-tech industry
- All Americans benefit:
  - More higher-wage jobs in the high-tech sector
  - Productivity gains through adoption of IT
  - Innovation and entrepreneurship
  - Multiplier-effect across other industries and society
  - Sustained contribution to U.S. economic growth

Bottom Line

China's WTO Accession:
- Opens markets
- Promotes rule of law and transparency
- Enhances enforcement

China makes all the concessions -- U.S. guaranteed benefits by passing PNTR

A vote for PNTR with China is a vote for continued American technological leadership

Mr. OXLEY. Thank you.
Ms. Valko.

STATEMENT OF CYNTHIA Y. VALKO

Ms. VALKO. Thank you, Mr. Chairman. I am grateful for the opportunity to offer New York Life International's perspective on the implications of China's impending membership into the WTO. As chair of the International Life Insurance Committee of the American Council of Life Insurers, I work closely with the colleagues throughout our industry to promote a China agreement that addresses our most pressing commercial priorities in that market. We have much to be enthusiastic about in the agreement negotiated by U.S. Trade Representative Barshefsky's team.

At the outset, I would like to cite a few key examples of how the WTO agreement really offers a whole new basis for our industry's access in the China market. The provisions I am about to summarize represent the results of the WTO agreement negotiated between the U.S. and China, which we have studied in detail. The EU concluded its own agreement with China last week and while details are still emerging, we are hearing that that agreement may have achieved some additional enhancements for life insurance, particularly in terms of phase-in periods for a number of Chinese commitments.

Because China's final WTO package will be based on the best offers on the table, the benefits to the U.S. can only get better as a result of any enhancements achieved as part of the EU agreement. Today, the ability of our company and many others to obtain a license to sell life insurance in China is governed by a process that is unpredictable, non-transparent and frequently politicized. Under the WTO agreement, China has committed to granting licenses based on clear-cut factors without easily manipulated economic needs, tests or quantitative limits on licenses. Today, American life insurers face geographic restrictions determining which Chinese cities are open for business to their activities.

Under the WTO agreement, these restrictions will be eliminated fully within 3 years of China's accession, and a specified list of cities will be fully opened even sooner. Today, foreign life insurance firms operating in China are not allowed to offer the full range in financial products. Under the WTO agreement, companies like ours will be able to sell health products within 4 years of China's accession and pension group and annuity products within 5 years. Today, foreign insurers in China are limited in their form of ownership and restricted in their choice of joint venture partners.

Under the WTO agreement, we will be able to select a Chinese partner of our choice immediately upon China's WTO accession with a provision for 50 percent share in equity.

In short, these commitments represent a clear statement of the political will of China's leaders to open China's financial services markets to greater competition. In essence, China's political leaders are giving the country's regulators and bureaucrats some extremely significant marching orders and that, in the final analysis, is what really matters in this agreement. The significance of China's commitments is particularly striking in light of the tremendous potential of the Chinese market for life insurance. Although China has more than one fifth of the world's population, it currently accounts for less than .2 of a percent of the world's life insurance market. Clearly, there is an immense room to grow.

The agreement offers us the possibility to participate in that growth. China's market liberalization steps will accelerate a process of awareness about life insurance. As China's huge population ages, the sheer number of elderly is stretching the traditional system beyond the breaking point. Recognizing this, individual Chinese are increasingly moving to assure their long-term social security by investing in life insurance and pension products. The WTO agreement will accelerate that trend.

So the terms of the agreement are clearly good for U.S. providers of life insurance and related products, but the financial services dimensions of the agreement will also contribute to a process of positive societal change in China. We know from experience that competitive and transparently regulated financial services systems are at the very core of the entrepreneurship and economic freedom. New York Life very much looks forward to being a part of that process.

Mr. Chairman, China's participation in the World Trade Organization is truly a momentous development. By approving PNTR, Congress can send a strong signal that it recognizes those benefits, for the citizens of both China and the United States, of China's decision to play by global trade rules. Thank you very much for your attention and for inviting me here today.

[The prepared statement of Cynthia Y. Valko follows:]

PREPARED STATEMENT OF CYNTHIA Y. VALKO, EXECUTIVE VICE PRESIDENT, NEW YORK LIFE INTERNATIONAL, INC. AND CHAIRPERSON, INTERNATIONAL LIFE INSURANCE COMMITTEE, AMERICAN COUNCIL OF LIFE INSURERS

Mr. Chairman, members of the Committee, I'm grateful for the opportunity to offer New York Life International's perspective on China's impending membership in the WTO, and the implications for an American life insurance company like ours. As Chair of the International Life Insurance Committee of the American Council of Life Insurers (ACLI), I've worked closely with colleagues throughout our industry to promote a China agreement that addresses our most pressing commercial priorities in that market. I'm glad to report that we have much to be enthusiastic about in the far-reaching agreement negotiated by U.S. Trade Representative Charlene Barshefsky's team.

In the life insurance and pension products sector, the agreement truly shifts the basis for foreign companies' participation in the Chinese market. I'd like to cite a few key examples of how the agreement negotiated by the United States will improve our prospects in China.

I should note that last week's agreement between the European Union and China appears to encompass a number of elements which improve upon the deal negotiated by the U.S. team, particularly with respect to accelerated phase-ins of Chinese market-opening commitments. Details on the EU-China deal are still trickling out, so I will focus today on the provisions of the U.S. agreement, which we've had a chance to study. But I want to stress that our deal can only get better because of what the EU has negotiated. Because China's final WTO package will be based on the "best" offers on the table, American insurance companies will benefit from any enhancements that the European Union has in fact achieved.

Today, the ability of our company and many others to obtain a license to sell life insurance in China is governed by a regulatory process that is unpredictable, nontransparent, and frequently politicized. *Under the WTO agreement,* China has committed to granting licenses based on clear-cut qualification factors, and without easily-manipulated economic "needs tests" or quantitative limits on licenses.

Today, American life insurers face geographic restrictions determining which Chinese cities are "open for business" to their activities. *Under the WTO agreement,* these access restrictions will be eliminated fully within three years of China's accession, and a specified list of cities will be fully opened even before that period expires.

Today, foreign life insurance firms operating in China are not allowed to offer the full range of financial products. *Under the WTO agreement,* companies like ours will be able to sell health products within four years of China's accession, and pension, group, and annuities products within five years.

Today, foreign insurers in China are limited in their form of ownership and restricted in their choice of joint venture partner. *Under the WTO agreement,* we'll be able to select a Chinese partner of our choice immediately upon China's WTO accession, with a provision for a 50 percent share in equity.

China's commitments in the life insurance sector represent a clear statement of the political will of China's leaders to open China's financial services market to greater competition. In the process, these reforms will significantly enhance the ability of China's citizens to control their financial destinies. By sending this political signal, and by committing China to fundamental reforms through binding WTO obligations, China's leaders are giving the country's regulators and bureaucrats some extremely significant marching orders. And that, in the final analysis, is what really matters in this agreement.

The significance of these commitments is particularly striking when one considers the future of the Chinese market for life insurance, pension products and other personal financial services. Although China has more than one-fifth of the world's population, it currently accounts for less than two-tenths of a percent of the world's life insurance market. Even though the Chinese have one of the highest individual savings rates in Asia, China spends less on all forms of insurance than 28 U.S. states.

This disparity between China's size and its currently underdeveloped insurance market can be summed up in a single word: potential. The market-opening commitments contained in China's WTO agreement are likely to lead to volume increases that exceed 300 percent—more than $4.8 billion.

China's market liberalization steps will accelerate a process of awareness about life insurance and other personal financial management tools that is already underway in China, by virtue of changing attitudes about personal finance. As we have seen so clearly in the Eastern European region, doubts about the solvency of state-run pension systems are increasing the demand for privately-held pensions, annuities and life insurance.

In China, this dynamic is particularly relevant in connection with emerging strains on the traditional rural system of old age support. As China's huge population ages, the sheer number of elderly will stretch the traditional rural system beyond the breaking point. Recognizing this, individual Chinese are increasingly moving to assure their long-term social security by investing in life insurance, pension products, and other personal financial instruments. The WTO agreement will accelerate that trend, and will allow U.S. companies to participate more fully in it.

So the terms of the agreement are clearly very good for U.S. providers of life insurance and related financial products. But I think it is important to stress that the financial services dimensions of the agreement will also contribute to a process of positive societal change in China.

As members of the Committee are well aware, one of the key debating points regarding PNTR centers around the degree to which China's membership in the WTO, and its associated economic and trade liberalization commitments, will advance the development of a more stable and democratic China. We have to be careful in this argument. I think it is unwise to portray WTO membership as a sort of "silver bullet" that will rapidly transform Chinese society in a way that addresses many U.S. policy concerns. There are no quick fixes to these problems, and we should not pretend that the WTO will provide such a fix.

But I do believe that U.S. goals can be achieved most effectively and most quickly by granting China PNTR status, bringing it into the WTO and integrating its economy more deeply with that of the rest of the world. Moreover, I'm convinced that the financial services dimensions of China's WTO package speak eloquently to the power of WTO accession to foster positive economic and social change in China.

We have seen over and over in the "newly industrializing" countries that competitive, dynamic, and transparently-regulated financial services systems are at the very core of entrepreneurship and economic freedom. A mature and competitive financial services market creates stable pools for investment in infrastructure, housing, and other critical needs. Such a market also provides people with a larger set of options about managing their financial destinies and long-term well-being. I am convinced that the Chinese negotiators knew exactly what they were doing in offering such far-reaching "concessions" in the financial services area, because those very "concessions" are in fact critical to the development of strong social safety nets and individual prosperity in China.

The investments that millions of Chinese make in an expanding array of personal financial instruments will be translated into a stronger financial foundation for the country as a whole. And just as the insurance industry in the United States has enabled some of this country's most significant investments in infrastructure and productive enterprises, the expansion of China's financial services market will reinforce the entrepreneurial spirit that is already at work creating a "new China." New York Life very much looks forward to being part of that process.

The bottom line is that China's participation in the World Trade Organization is a truly momentous development in that country's evolution towards greater economic reform and political freedoms. Congress, by approving PNTR, can send a strong signal that it recognizes the benefits—for the citizens of both China and the United States—of China's decision to play by global trade rules.

Thank you for your attention, and for inviting me to appear today.

Mr. OXLEY. Thank you.

Mr. Watkins?

STATEMENT OF JESSE J. WATKINS

Mr. WATKINS. I am here as managing director of my company which is in New York, now that is New York and New Jersey. I am representing the Council of Insurance Agents and Brokers, which represent the Nation's largest commercial agents and brokers for property and casualty insurance. I am also a director of the U.S. China Foundation, which seeks to foster greater economic and cultural relationships with our neighbors in the east.

At the outset, I want to thank Chairman Oxley and Congressman Towns for the great support you have given to us in our quest to open Chinese markets to foreign brokers. As you know, insurance brokerage dropped off of the table during early negotiations with the United States. In the Oxley-Towns letter to the Chinese Ambassador in Washington back in March, you strongly urged the Chinese Government to include this sector in the final Chinese agreement, which was reached with the European Union.

I was in Hamburg, Germany last week at a meeting of the International Insurance Brokers Association, and I am delighted to report that the Chinese did concede to allow insurance brokers into their agreement. Now that the EU has obtained this new important concession from the Chinese, all brokers, including Americans, will be beneficiary. The leadership of this subcommittee has made an important difference in achieving this victory and we appreciate it. Even without this concession, though, our association strongly believes that China should be part of the WTO. In the past year, I personally have had an opportunity to travel to China to discuss the need for promoting access for international insurance brokerages to their market.

Unlike some of the other firms, my work has not been focused singly on building a presence of my firm in the Chinese marketplace. Instead, I have been working with the Chinese to bring professionals to the U.S. to train them here so that they can build an effective industry in China.

Ultimately, we hope to build the same kind of cooperative environment with the Chinese that we have built with Europe. We stand to benefit to the extent that the Chinese ultimately will have needs for property casualty insurance products that need to be serviced both here in the United States and those products which our clients need to be serviced locally in China. I am pleased to join the delegation from the U.S. China Foundation to begin this effort to extend economic and cultural ties to China. The extent of my activities have been largely educational, and I believe strongly we must encourage trade with China.

It is a simple issue. The Chinese are isolated, they can't be educated. Active engagement in China in the trade's sphere is an essential link to bringing economic prosperity and economic freedom to China. Along the way, the prospects are limitless for American firms to engage in these exciting opportunities. It is difficult to argue that China's entry into the mainstream of the world trading system would not result in many positive benefits for the Chinese people. Distribution of the economic rewards throughout a society lead to greater political stability and ultimately a more Democratic process. History has shown that a country is more likely to move toward democracy when it has its own self-interest.

Membership in the WTO is clearly in China's interest today. We are suggesting that China's inclusion can lead to greater cooperation, and as a result, our ability to influence human rights and other crucial issues will increase significantly. This I know from personal contact.

We cannot ignore the benefits to American business. China is one fifth of the world's population, and an on-tap potential for U.S. businesses, many of which have already established offices in China. The financial service industry is the crest of the Chinese expansion. The three pillars of banking, insurance and securities are essential if that expansion is to continue, but those sectors must have access to the market and be able to operate in a competitive environment with clear rules and regulations.

The proposed structure would provide this to U.S. businesses. We are joining in the view of the World Federation of Insurance Intermediaries who are meeting today in Lisbon, in which the Council is also participating. If your vote this week fails, our efforts to change China in a positive way will cease. Again, Mr. Chairman, thank you for your work in advance of the cause and we appreciate the opportunity to testify today.

[The prepared statement of Jesse J. Watkins follows:]

PREPARED STATEMENT OF JESSE J. WATKINS, MANAGING DIRECTOR, HERBERT L. JAMISON & CO. LLC

This statement is submitted on behalf of the members of The Council of Insurance Agents & Brokers ("The Council"). The Council is a national trade association founded in 1913 as the National Association of Casualty and Surety Agents. Since 1913, The Council of Insurance Agents & Brokers has provided industry leadership while representing the largest, most productive and most profitable commercial insurance agencies and brokerage firms in the U.S., and around the globe. Council members operate in over 3,000 locations and place nearly 80%—well over $100 billion—of the U.S. commercial property/casualty premiums. In addition, Council members specialize in a wide range of insurance products and risk management services for business, industry, government and the public. Council members, who operate nationally and internationally, also administer billions of dollars in employee benefits.

Good afternoon, Mr. Chairman and members of the committee. I am Jesse Watkins, managing director of Herbert L. Jamison & Co. LLC, headquartered in West Orange, NJ, with offices in New York. I have been an insurance broker at Jamison since 1968, and I have been engaged in all aspects of our firm's business, which includes a full array of property/casualty products and employee benefits, with a focus on professional liability. Like many other insurance agencies and brokerage firms, our business is conducted on a national scale; additionally, we place business in international markets, and likewise receive the business of many companies that are headquartered offshore. I also serve as a member of the Board of Directors of the Council of Insurance Agents and Brokers.

At the outset, the Council would like to thank Chairman Oxley and Congressman Towns for the great support that they have given to us in our quest to open Chinese markets to foreign brokers. In their March 28 letter to the Chinese Ambassador Li Zhaoxing, Chairman Oxley and Congressman Towns expressed the importance of intermediaries. "We believe it is critically important that intermediaries be included along China's commitments for entry to the World Trade Organization," they said. The letter went on to urge the Chinese government to include this sector in the final EU/China agreement.

The Council is very appreciative of these efforts and has made access to the Chinese insurance markets one of its highest priorities. Indeed, in the past year, I personally have had an opportunity to travel to China on two occasions to discuss the need for promoting access for international insurance brokerages to their markets. Unlike some other firms, my work has not been focused singularly on building a presence for my firm in the Chinese marketplace. Instead, I'm working to bring Chinese professionals to the U.S. and to help train them to work effectively in this industry. Ultimately, we hope to build the same kind of cooperative environment with the Chinese that we have already built with European firms. We stand to benefit to the extent that the Chinese ultimately will have needs for property/casualty insurance products that need to be serviced in the United States.

I've been pleased to join with delegations from the U.S.-China Foundation to begin this effort to extend economic and cultural ties to China. To the extent that my activities have been largely educational to date, I have strong views in support of China's entry into the World Trade Organization. It is a simple issue. If the Chinese are isolated, they can't be educated. Active engagement of China in the trade sphere is an essential link in bringing economic prosperity and economic freedom to the Chinese. Along the way, the prospects are limitless for American firms to engage in these exciting opportunities.

Last week, I attended meetings of international insurance brokers in Europe, and I'm very excited to bring the news that the European Union successfully has persuaded the Chinese to include insurance brokerage as a part of their negotiated agreement on WTO entry. As you know, insurance brokerage "dropped off the table" during earlier negotiations with the United States. Now that the EU has obtained this new and important concession from the Chinese, all brokers—including American-based firms—will be the beneficiaries.

As noted at the outset, the crucial assistance of Chairman Oxley and Congressman Towns helped to make this Chinese concession a reality. Both of these leaders wrote to the Chinese ambassador in Washington, strongly urging the Chinese government to include intermediaries in the agreement with the EU. This pressure was also brought to the attention of our European counterparts, and helped create the environment in which insurance brokerage remained a priority of negotiators. We are extremely grateful for this important assistance, which came at a perfect time in the negotiations.

Even had this development not occurred, however, it is important to note that we would have strongly supported China's entry into the WTO. It has long been recognized that liberalization of trade is critical to economic growth and stability. When markets are opened and allowed to operate freely, society benefits from the prosperity created by a vigorous economy. Businesses flourish, jobs are created and living standards rise.

It is difficult to argue that China's entry into the mainstream of the world trading system would not result in many of these positive benefits for the Chinese people. Furthermore, distribution of the economic rewards throughout a society can lead to greater political stability and ultimately a more democratic process. Most Americans, I think, agree that such stability can be most readily accomplished through an open and competitive marketplace.

We are not suggesting that we should ignore China's many problems—the most visible of which are human rights issues. And we are not suggesting that by mainstreaming China that it would transform itself into a thriving democratic society overnight. Rather, history has shown that a country is more likely to move towards democracy when it is in its interest to do so. And membership in the WTO is clearly in China's interest today. We are suggesting that China's inclusion in the WTO can lead to greater cooperation and as a result our ability to influence human rights and other critical issues will increase significantly.

Nor can we ignore the economic benefits to American businesses. China has one-fifth of the world's population and the untapped potential of that market is vast. U.S. businesses are expanding at a rapid pace and many are establishing offices in China, offering services and products to the Chinese people and local businesses that are beginning to flourish in many areas of the country.

The financial services industry is on the crest of the Chinese expansion. The three pillars of a competitive market—banking, insurance and securities—are essential if that expansion is to continue. But those sectors must have access to the market and be able to operate in a competitive environment with clear rules and regulations that are not subject to the arbitrary whims of the government. The WTO structure provides stability for US businesses operating abroad.

With the financial sector, a liberalized insurance market can play a key role in enhancing such growth. The lowering of trade barriers to enhance the operation of foreign-based insurance agents and brokers is integral to this process.

When barriers to foreign professional insurance intermediaries are lowered, benefits flow to all parts of the economy. One of the primary beneficiaries is the insurance consumer. A healthy insurance distribution system provides consumers with a greater array of choice in insurance products and services. This in turn, allows commerce to flourish and the economy to grow.

In the 1950s, the manufacturing and service industries of the Western industrialized economies began to globalize and their insurance service providers began to globalize alongside their customers. Initially, the geographic expansion of insurance carriers and intermediaries was undertaken to ensure that the new risks associated with their clients' geographic expansion were identified and managed effectively. This first stage of globalization not only improved the lot of those engaged in cross-border endeavors, but it also provided the host countries with the economic benefits of goods and services, now manufactured locally, along with opportunities for local vendors to form partnerships with foreign-based concerns and the creation of new jobs to staff a modernizing economy.

The second stage in this process, from which much of the world today is deriving benefits, involves providing insurance and risk management services to indigenous or local businesses, especially those enterprises poised for growth and expansion beyond the borders of their home countries.

The process in which international intermediaries cultivate the business of home-grown companies is a crucial one for the China market. If unimpeded, this process transforms the relationship between developed and developing countries from one of producer-to-market to the more egalitarian one of competing producers. As the developing economies take shape, openness to foreign insurance intermediaries can make the difference between a country being included or excluded from the world economy. The benefits of global trading are not possible without liberalized trade in both insurance underwriting and distribution.

The need for insurance is clear and becomes more so with the increasing complexity of modern life. Without protection against the risk of expanding into unfamiliar territory, there would be few risk-takers and correspondingly little economic growth. Insurance earns its place in the business world by its ability to make certain risks worth taking, i.e. by transferring some of it to a third party formed expressly to assume a portion of a company's overall risk burden.

The contribution of insurance intermediaries may be less widely recognized, but is no less significant. The indispensable function of agents and brokers is to guide companies in this search for the most cost-effective way of managing risk. Agents and brokers help companies find as much protection as they need, at the lowest price possible and the best terms available.

Their contribution includes not just transferring risk to insurers, but evaluating and implementing other means of funding for potential losses (such as captive insurance companies and other forms of self-insurance), providing services aimed at preventing losses in the first place (safety and other loss control programs), and providing services to minimize the cost of losses that do occur.

International intermediaries do not simply procure products and services; linking their insurance and financial expertise with their expertise in client industries, they are true market innovators. Because of their close relationship with clients, they can often identify the need for a new product and may even create a suitable product before the underwriters themselves can do so.

The natural development from pure insurance intermediaries to partners with clients in "enterprise risk-management" has been evolving. The process in countries with newly-privatized economies or newly-liberalized financial sectors is bound to be much faster as lessons learned over the years can be applied as needed.

The foreign offices of international intermediaries are largely staffed and often headed by local inhabitants, whose knowledge of the local legal and economic conditions, as well as social and cultural mores, is indispensable. If you look at the overall geographic spread of intermediary networks, along with the make-up of their professional service teams, its clear that intermediation as a service, beyond simple placement of insurance, has become a worldwide commodity—a staple of modern economic development serving the interests of all involved.

What is of benefit to the client is the combination of local service and international access offered. Through an international network, intermediaries can get the best possible deal for clients because of their ability to tap into the worldwide insurance marketplace. The more markets intermediaries can access for risk capital, the better it is for the buyer. Intermediaries can "shop around" to get clients the most protection for the least cost.

Intermediaries also bring to bear considerable experience and expertise that helps clients in selecting markets that are both financially strong and well capitalized. Since the goal is not just growth, but safe growth for clients, the ability to draw on information about markets around the globe is key. Partnerships between local and foreign insurers, or local and foreign intermediaries, can instantly give the domestic insurance community critical international links.

When intermediary operations are sufficiently liberalized, those producing goods and services can take advantage of the more competitive financial atmosphere, making the most of their risk management budgets. The effect of such a combination is to further propel economic growth in all quarters.

Finally, liberalization of insurance intermediaries is a necessary complement to similar action in the insurance and reinsurance arenas. We recognize the importance of the US-China agreement reached last November to American interests and the financial services industry. It provides broad access to the Chinese market for banks, insurers and reinsurers. The initial failure of the US-China agreement to include insurance intermediaries was disappointing, because an offer made by the Chinese last April would have eliminated many of the geographic and other restrictions on foreign insurance intermediaries. Under current rules, intermediaries can only obtain a general business license in China, which places stringent restrictions on what they can do and where they can operate. Furthermore, they can be subjected to the whims of the government at any time. What is given can be taken away. It is therefore important that intermediaries have the same rights and protections that others in the financial services sector will receive once China accedes to the WTO. Had the Chinese not made the concession last week to allow intermediaries access to their markets, China would have denied insurance consumers the full benefits of a liberalized insurance marketplace.

We are very pleased that the Chinese are now demonstrating their commitment to full market liberalization by providing intermediaries with the same level of access granted to insurance companies. Insurance companies and intermediaries work closely together and it is difficult to imagine a viable system that allows insurers broad access to consumers, but denies their agents and brokers the ability to distribute those products.

We are joined in this view by the World Federation of Insurance Intermediaries, an organization representing over 500,000 professional insurance agents and brokers around the world, which is meeting this week in Lisbon with representatives from our organization. If the vote in the House of Representatives fails this week, it will be a severe blow to all of the participants in this international organization.

We understand the economic interests at hand in this debate and the value of bringing China into the fold of the trading fraternity. China's market provides enormous economic opportunities for US businesses and opens China to the benefits of goods and services that can only lead to a higher standard of living, greater internal stability and cooperation. The Council is on record for supporting market liberalization of economies around the world and will continue to do so. Again, Chairman Oxley, we appreciate your and Congressman Towns' continued support.

We appreciate the opportunity to express our comments today.

Mr. OXLEY. Thank you.

Mr. Yingling.

STATEMENT OF EDWARD L. YINGLING

Mr. YINGLING. I want to thank you, Mr. Chairman, for holding this very important hearing. Our economy and our financial institutions are the envy of the world, but to sustain our growth, we must continue to look for opportunities to open markets to U.S. firms. Providing China with PNTR status is just such an opportunity. It will help to assure that China will adhere to international economic rules, treat businesses operating in the country fairly, and provide American businesses, particularly small and medium-size firms, greater access to the world's largest emerging market.

I would like to emphasize three points. First, granting PNTR status to China will promote stronger economic growth. Chinese firms already have open access to U.S. markets, but up until now, U.S. firms have found it difficult to reach Chinese consumers. With 1.2 billion people in China and GDP growth exceeding 10 percent per year over the last decade, the potential export market for U.S. companies is extraordinary. Reducing barriers to trade and opening markets will increase U.S. exports, create new jobs to support this increase, and help sustain our current economic expansion.

Mr. Chairman, your State of Ohio is a good example. As you know, Ohio is already a significant exporter of goods and services to China. According to one recent study, Ohio exports to China in 1998 exceeded $500 million. The possibility for further exports from Ohio and all other States, particularly given the infrastructure needs that China faces, are substantial.

A second point granting PNTR will create new opportunities for banks and financial service providers. The financial services industry is one area in which the U.S. leads the world. U.S. banking, securities and insurance firms are the most innovative and strongest in the world. Opening foreign markets to financial services enables us to leverage these advantages leading to more U.S. jobs.

In addition, and this is an important point, a local presence in China by U.S. financial firms will help other U.S. firms take advantage of new opportunities. PNTR will mean a major presence by U.S. financial institutions on the ground in China and U.S. financial institutions, say, for a small business in Ohio, can help pave the way. They can provide the advice on how you get into that new market, how you get the financing, how you get through the export controls and the import controls, and that type of thing. If we give that up to financial institutions from other countries, their first priority is going to be to help small and medium-size firms in their country, not U.S. firms.

So having U.S. financial firms on the ground in China is a big advantage to all U.S. firms. A special word is in order about agriculture. The ABA has many members which are small community banks in agricultural areas. We have studied, in depth, the challenges that small rural communities face. To ensure the survival of these communities, we must solidify increased agricultural exports. We saw the other side of that coin a couple of years ago when Asia had its economic problems and the agriculture sector went right into the tank. Passage of PNTR for China will help small rural communities and their community banks.

Our third and final point is granting PNTR will keep the U.S. on a level competitive playing field with our European and Asian competitors. Today, there are over 54 foreign banks with a presence in China. Delaying adoption of PNTR will harm U.S. banks as European and Japanese banks seize the opportunity to gain market share at U.S. banks' expense. Such a situation will not only hurt U.S. financial firms in China, it will give our financial services competitors a stronger, broader base from which to compete throughout the world.

It doesn't just hurt us in China. It will hurt us throughout the world. In other words, failure to pass PNTR for China will hurt our competitive position, not just in China, but everywhere, because our competitors will have a stronger worldwide base than we will.

Thank you for the opportunity to present the views of the ABA.

[The prepared statement of Edward L. Yingling follows:]

PREPARED STATEMENT OF EDWARD L. YINGLING ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. Chairman, I am Edward Yingling, Deputy Executive Vice President and Executive Director of Government Relations for the American Bankers Association (ABA). ABA brings together all elements of the banking community to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional, and money center banks and holding companies, as well as savings institutions, trust companies, and savings banks—makes ABA the largest banking trade association in the country.

I want to thank you, Mr. Chairman, for holding this very important hearing. The financial services industry in the United States has been central to the economic expansion that we have enjoyed over the last decade. Our economy and our financial institutions are the envy of the world. To sustain our preeminence, we must continue to look for opportunities to open markets to U.S. firms. Providing China with permanent normal trade relation (PNTR) status is just such an opportunity. It will help to assure that China will adhere to the international economic rules, will treat businesses operating in the country fairly, and will provide American businesses—particularly small- and medium-sized firms—greater access to the world's largest emerging market. Not only will it stimulate economic growth in the U.S., but it will certainly boost economic growth in China and create a base for economic and social reform.

In my statement today, I would like to emphasize three points:

- Granting PNTR will promote stronger economic growth in both countries;
- Granting PNTR will create new opportunities for banks and financial service providers; and
- Granting PNTR will keep the U.S. on a level competitive playing field with our European and Asian competitors.

I would like to touch briefly on each of these points in my statement today.

GRANTING PNTR WILL PROMOTE STRONGER ECONOMIC GROWTH IN THE U.S. AND CHINA

Granting PNTR is in the best interests of both the U.S. and China. Chinese firms already have open access to US markets, but up until now U.S. firms have found it very difficult, in some cases impossible, to reach Chinese consumers. The historic trade agreement reached in November of last year, which paved the way to China's entry in to the World Trade Organization (WTO), was an important step in opening Chinese markets to U.S. goods and services.

The potential economic benefits are striking. With 1.2 billion people and GDP growth exceeding 10 percent per year over the past decade, the potential export market for U.S. companies is extraordinary (see Figure 1). In spite of current restrictions, China has become America's fourth largest trading partner, with total trade exceeding $95 billion in 1999 (see Figure 2). The Congressional Research Service projects that U.S. exports to China will grow as much as $13 billion annually over the next 5 years, supporting as many as 200,000 jobs in the U.S.

The reduction in tariffs will help both large and small firms. For example, Chinese tariffs on industrial and agricultural goods will fall by 50 percent or more over five years. This will substantially boost the potential market for U.S. exports. In fact, the United States Department of Agriculture estimates that improved access to China will increase agricultural exports by $2 billion per year by 2005 and will account for over one-third of US agricultural exports over the next decade. Moreover, China has committed to eliminating agricultural export and domestic subsidies, which have displaced U.S. exports in other foreign markets.

Figure 1

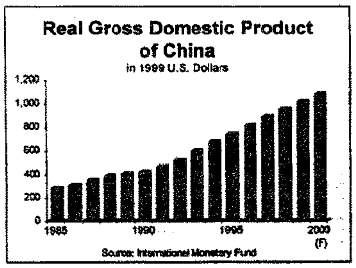
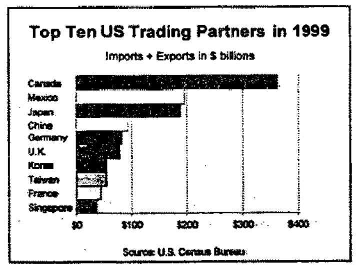


Figure 2



The elimination of tariffs by 2005 on computers, semi-conductors and other high-tech products will also significantly boost the potential exports for the U.S. high-tech sector. There is no doubt that this sector has been a driving force behind the economic performance in the U.S. over the last five years. Exports to China from this sector have already grown rapidly over this period. The opening of new markets, under fair competitive rules, will help sustain this competitive advantage of U.S. firms.

Mr. Chairman, your state of Ohio is already a significant exporter of goods and services to China and can serve as an example of what is at stake. According to the Massachusetts Institute of Social and Economic Research, Ohio exports to China in 1998 exceeded $260 million. Including goods from the U.S. going through Hong Kong to China, as well as exports from other states that pass to China through Ohio ports, adds another $256 million to the Ohio export total, according to K.C. Fung and Lawrence Lau.[1] The possibilities for further exports from key Ohio industries such as industrial machinery, computers, instruments, fabricated metal products, electronic and electric equipment, and chemicals are substantial—particularly given the new infrastructure requirements that will face China over the next decade.

Importantly, China is also reducing non-tariff barriers. For example, U.S. exporters will be able to reach Chinese consumers directly, and provide services in ways that could not have been done before. By increasing competition and eliminating the required use of middlemen, Chinese consumers will enjoy lower-priced and higher-quality goods and services.

The net effect of reducing barriers to trade and opening markets is that exports from the U.S. and elsewhere will increase substantially. China's trade now accounts for 3 percent of world trade. Given the potential size of the market, there is plenty of opportunity for companies around the world to market and sell products to Chinese consumers. The result will be increased economic growth in China, as well as economic growth and new jobs in the exporting countries.

GRANTING PNTR WILL CREATE NEW OPPORTUNITIES FOR BANKS AND FINANCIAL SERVICE PROVIDERS

The financial services sector is a key component of U.S. economic growth and development (see Figure 3). The opening of China's markets to financial firms presents tremendous opportunities for U.S. banks and financial firms and will add to U.S. economic growth.

In this context, it is important to stress that the arena of financial services is one in which the United State clearly leads the world. In banking, securities, insurance, and other aspects of financial services, U.S. firms are generally regarded as the most innovative and the strongest. Opening foreign markets to our financial services firms enables us to expand these advantages, which of course lead, to more jobs in the U.S. In addition, to the degree U.S. financial institutions can set up local offices and come to know local economies, other U.S. firms will benefit, as the financial firms can provide advice on how to compete in those local economies. In other words, as China opens up, competitive strength of U.S. financial service companies will help promote not only financial service jobs in the U.S., but jobs in other sectors as well.

[1] Fung, K.C. and Lau, Lawrence, "New Estimates of the United States-China Bilateral Trade Balances," March 1999, pg 9. It is estimated that over 40 percent of U.S. goods exported to Hong Kong are then shipped to China.

Due to market restrictions, investment and lending in China has been limited. For example, direct investment in China lags far behind other countries (see Figure 4). According to Goldman Sachs, China's domestic banking market is $1.1 trillion in deposits and $1 trillion in loans. As of June 1999, deposits and loans had grown 20 percent and 16 percent, respectively.

Figure 3

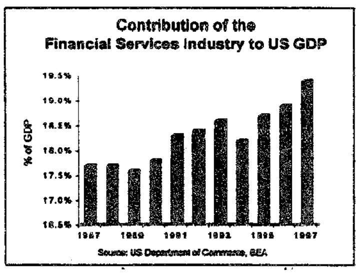
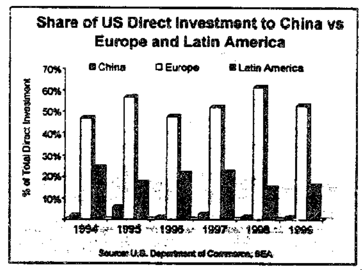


Figure 4



U.S. banks will have full market access by 2005 after China's accession into the WTO. This means that U.S. banks will be allowed to engage in all transactions that Chinese banks conduct today, including engaging in local-currency transactions with Chinese companies (within two years) and retail banking transactions with Chinese consumers (within five years). Moreover, all limits on geographic expansion within China will be lifted within five years. China will allow foreign institutions to establish direct branches or be allowed 100 percent ownership in subsidiaries without any numerical or geographic limitations. This is on par with what OECD countries have agreed to and is superior to commitments by most other developing countries. Foreign financial firms will also be allowed to acquire equity stakes (with limitations) in Chinese fund management companies and underwrite domestic securities.

Products that U.S. banks would likely offer include foreign exchange, hedging, local-currency-based project finance and interbank transactions, syndicated lending, and cash management for large corporations. Chinese financial consumers will also benefit as consumer credit markets become more efficient and more readily available. One of the largest financing needs will be for infrastructure and telecommunication improvements, estimated to be $1 trillion. China's private and public sectors cannot finance this alone; foreign sources of funding will be required.

Equally important is that the best practices of U.S. banking institutions will be exported to China. This will lead to more effective risk management, transparency of financial balance sheets and appropriate allocation and utilization of capital and credit.

Changes will also occur in insurance and securities markets as others on this panel will testify. Relative to the size of the economy, capital markets are small. This fact does suggest substantial growth potential. However, major steps will be required to complete a modern regulatory and legal framework.

Not only are there direct benefits from providing financial products and services in China, but there are many indirect benefits from U.S. banks as well. For example, U.S. banks provide export credits, trade finance and foreign exchange products to U.S. companies. They also lend to exporting companies such as the agricultural sector. In fact, it has been estimated that 80 percent of all exports to those with in China are produced by small to mid-sized firms. These companies, of course, rely on local bank financing for production and inventory control.

A special word is in order about agriculture. The ABA has many members which are small community banks in agricultural areas. We have studied in depth the challenges small rural communities face. Many believe the most important thing that could be done to ensure the survival of such communities is to solidify and increase agricultural exports. Clearly we saw the impact of the Asian economic crisis a few years ago on these communities. China is obviously a huge market for U.S. agriculture. As is the case with financial services, agriculture is an arena in which U.S. producers shine. Passage of PNTR for China will help small rural communities and their community banks.

There are of course many challenges ahead, and the difficulties they present should not be underestimated. These include the promotion of private sector firms, the need to clean up bad loans and enhance competition among banks, and the need to develop well-functioning financial markets. As China's economic wealth increases, however, these changes should occur, as will the demand for more financial services.

GRANTING PNTR WILL KEEP THE U.S. ON A LEVEL COMPETITIVE PLAYING FIELD WITH OUR EUROPEAN AND ASIAN COMPETITORS

It is important to keep in mind that China will receive the benefits of greater trade regardless of whether the U.S. takes this important step. China's accession to the WTO is near certain. The critical question, therefore, is whether U.S. banking and financial services firms (as well as firms in other sectors) will be allowed to benefit from the opening of China's markets.

As indicated above, China will face major infrastructure, telecommunications and energy needs requiring significant foreign capital and financing. Modernizing its economy requires a significant capital investment. With the PNTR, U.S. banking institutions will be able to provide new products and services. But the competition for these markets will be intense. Today there are over 50 foreign banks with a presence in China. Delaying adoption of PNTR will harm U.S. banks as European and Japanese banks seize the opportunity to gain market share at U.S. banks expense. Such a situation would not only hurt U.S. firms in China, it would give our competitors a stronger, broader base from which to compete throughout the world. U.S. financial services companies must be allowed to maintain our preeminent status by opening markets for our products and services.

Mr. OXLEY. Thank you.

And our final witness, Mr. Mastel.

STATEMENT OF GREG MASTEL

Mr. MASTEL. Thank you, Mr. Chairman. My name is Greg Mastel. I am the director of the Global Economic Policy Project of the New America Foundation. I am happy to be here today before the subcommittee. I want to testify today regarding the granting of PNTR status to China and China's membership in the World Trade Organization. I plan to focus my remarks on the WTO accession agreement with China and its record of keeping trade commitments and the ability of the WTO to cope with China.

On paper, many have mentioned the WTO accession agreement negotiated between the United States and China has many positive features. The recent bilateral WTO accession agreement between the EU and China in which all WTO members will benefit appears to further strengthen the ultimate WTO accession terms with China. However, the key question remains: Will China make good on its promises? Ultimately, the WTO is a trade agreement. It has a detailed process for enforcing compliance, but as the ongoing conflict between the United States and Europe on several agricultural issues demonstrates, that process has a number of flaws and implementation of promises and dispute settlement panel decisions is far from automatic.

The best indicator of China's willingness and ability to implement the promises it has made in the WTO context is its record in implementing other trade agreements. In the last decade, the United States and China have concluded a number of major trade agreements covering topics from protection of intellectual property to textile imports.

A detailed record of China's compliance with these agreements is included in a recent article I wrote for the Weekly Standard, which I asked to be included in the record of the hearing. The conclusion that can easily be drawn from the Chinese trade history is that China has a poor record of keeping its trade promises that is has made to the United States. Every major trade agreement the United States and China have struck has been dogged by repeated instances of Chinese noncompliance, and at times, open violation of the terms of the agreement.

China's supporters often point to several understandings struck on intellectual property as evidence of China's willingness to keep its trade commitments. Without question, the United States has invested a much greater effort in enforcing agreements on this topic than any other. In most areas, the United States has not seriously challenged China's agreement violations. With regard to intellectual property piracy, however, the United States has formally threatened to impose trade sanctions on China on at least three occasions to force China to live up to its bilateral agreements on the topic.

As a result of this pressure, there is evidence that China has made an effort to curb piracy. As any informed observer would concede, however, piracy of intellectual property, often directly involving Chinese Government ministries, the People's Liberation Army, or the relatives of China's leaders, remains a widespread problem in China. In fact, industry estimates of the piracy problem in China are that piracy rates are over 90 percent in most categories, and that total losses are actually higher than they were in 1995 when the Clinton administration began intense efforts to enforce the agreement. Moreover, the progress that has been made is the direct result of repeated threats of sanctions by the United States. Without these threats, China is likely to have made little progress in fulfilling its negotiated promises.

Often observers seem to assume that the WTO will automatically be able to improve China's compliance with its trade agreements. There is simply no basis for this assumption. The WTO has the potential strengths over bilateral understandings of obligating China to meet a wider array of commitments and bringing some multilateral pressure to bear on China to reform its trade policies.

Unquestionably, these are positive features, but the WTO is not well suited to policing China. The WTO is the ultimate rules-based, market-oriented organization. The fundamental problem is that China is neither a rules-based country nor a fully market-oriented economy, the ultimate square peg in a round hole.

Given the arbitrary and non-transparent manner in which Chinese ministries often make trade policy, it is difficult to even determine exactly what Chinese trade policy is in some areas, let alone actually win a WTO dispute settlement panel finding against China. As a result, the WTO is likely to suffer from exactly the same type of compliance problems in China that have plagued bilateral trade agreements, and the United States will have given up its option to impose bilateral trade sanctions on China to enforce the agreements. At some point China, should become a WTO member.

In a perfect world, it may be wise to keep China outside the WTO for a few years to allow its legal system to mature and the economic reform process to advance further. But policy is not made in a perfect world. I am cautiously willing to support China's WTO's membership, provided the United States invest time and effort to enforce the agreement. Congress could play an important role in ensuring the necessary time and energy is devoted to enforcement.

In general, the Congress has taken more interest in enforcing trade governments than various administrations. In the case of the

Clinton administration, much critical work is taking place in the last days of the administration at a time when many administration officials seem eager, perhaps too eager to complete China's WTO accession and convince Congress to vote for PNTR.

PNTR is the Congress' major point of leverage vis-a-vis the administration in China. It will be wise, in my opinion, for the Congress to withhold its final vote on PNTR until the WTO accession process is complete. Failing that, Congress should at least insist that the final WTO accession protocol pay particular attention to enforcement issues and pass legislation to ensure regular U.S. efforts focused on enforcement.

Thank you, Mr. Chairman.

[The prepared statement of Greg Mastel follows:]

PREPARED STATEMENT OF GREG MASTEL, DIRECTOR, GLOBAL ECONOMIC POLICY PROJECT, NEW AMERICA FOUNDATION

Mr. Chairman and Members of the Subcommittee, my name is Greg Mastel and I am Director of the Global Economic Policy Project at the New America Foundation.

I appreciate the opportunity to testify today before the Committee regarding the prospect of granting Permanent Normal Trade Relations status to China and China's membership in the World Trade Organization (WTO).

I plan to focus my remarks on the WTO accession agreement with China, China's record of keeping trade commitments, and the ability of the WTO to cope with China.

THE WTO ACCESSION AGREEMENT

On paper, the WTO accession agreement negotiated between the United States and China has many positive features. The recent bilateral WTO accession agreement between the EU and China—from which all WTO members will benefit—appears to further strengthen the ultimate WTO accession agreement with China.

However, the key question will remain: "Will China make good on its promises?"

Ultimately, the WTO is a trade agreement. It has a detailed process for enforcing compliance, but as the ongoing conflict between the United States and Europe on several agricultural issues demonstrates, that process has a number of flaws and implementation of promises and dispute settlement panel findings is far from automatic.

The best indicator of China's willingness and ability to implement the promises it has made in the WTO context is its record in implementing other trade agreements.

In the last decade, the United States and China have concluded a number of major trade agreements covering topics from protection of intellectual property to textile imports. A detailed record of China's compliance with these agreements is included in a recent article I wrote for the Weekly Standard, which is attached.

The conclusion that can immediately be drawn from the record is that China has a poor record of keeping the trade promises it has made to the United States. Every major trade agreement the United States and China have struck has been dogged by repeated instances of Chinese non-compliance and, at times, open violation of the terms of the agreement.

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As a result of this pressure, there is evidence that China has made an effort to curb piracy. As any informed observer would concede, however, piracy of intellectual property—often directly involving Chinese government ministries, the People's Liberation Army, or the relatives of China's leaders—remains a widespread problem in China.

In fact, industry estimates of the piracy problem in China are that piracy rates continue at over 90 percent in most categories and that total losses are actually higher than they were in 1995 when the Clinton administration began intense efforts to enforce the agreement.

Moreover, the progress that has been made is the direct result of repeated threats of sanctions by the United States. Without these threats, China is likely to have made little progress in fulfilling its negotiated promises.

THE WTO AND CHINA

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As a result, the WTO is likely to suffer from exactly the same type of compliance problems in China that have plagued bilateral trade agreements with China. And the United States will have given up its option to impose bilateral trade sanctions on China to enforce the agreements.

CONGRESS'S ROLE

At some point, China should become a WTO member. In a perfect world, it may be wise to keep China outside the WTO for a few years to allow its legal system to mature and its economic reform process to advance further.

But policy is not made in a perfect world.

I am cautiously willing to support China's WTO membership provided the United States invests time and effort to enforce the agreement.

Congress could play an important role in assuring that necessary time and energy is devoted to enforcement. In general, the Congress has taken more interest in enforcing trade agreements than various administrations.

In the case of the Clinton administration, much critical work is taking place in the last days of the administration, at a time when many administration officials seem eager—perhaps too eager—to complete China's WTO accession and convince Congress to vote for PNTR.

PNTR is the Congress' major point of leverage vis-a-vis the administration and China. It would be wise for the Congress to withhold its final vote on PNTR until the WTO accession process is complete.

Failing that, Congress should insist that the final WTO accession protocol pay particular attention to the enforcement issue and pass legislation to ensure regular U.S. efforts focused on enforcement.

Thank you, Mr. Chairman.

The China Trade

Membership in the World Trade Organization won't liberalize Beijing unless America insists on compliance with the rules.

BY GREG MASTEL

The fight over the permanent extension of most-favored-nation trading status to China is likely to be one of the hardest-fought congressional battles of 2000. Last week, the administration launched a high-profile campaign in favor of MFN for China; labor is vigorously countering. But for all the lofty rhetoric, at its core, the issue is the prosaic one of the merits of the agreement negotiated between Washington and Beijing last November, setting out the terms for China's accession to the World Trade Organization.

If this agreement is sound and enforceable, it is likely to encourage reform in China and vindicate a policy of engagement. If it is faulty or simply unenforceable, it is unlikely to spur positive change. Thus, before election-year bombast swamps the discussion, it is important to reach a sober evaluation of the proposed agreement and of China's record of compliance with recent trade deals.

¶ *The WTO Accession Agreement.* Trade agreements are by nature compromises, and this one is no exception. Unquestionably, some provisions could be improved. Chinese tariffs could be lowered beyond the 17 percent Beijing has agreed to. Foreign telecommunications firms and banks could be granted more leeway to operate in China. Subsequent negotiations between China and other WTO members may improve the terms on these and other issues.

On paper, however, the November deal has quite a lot to recommend it. China does agree to significant tariff cuts. It promises substantial new market access for agricultural products. And it assures U.S. banks and insurance firms considerably increased access to Chinese consumers.

Already, however, Chinese press reports indicate that Beijing may not plan to fulfill the agricultural provisions of the agreement. It is a familiar song. An examination of the four recent major trade deals the United States has struck with China shows that compliance is a chronic problem.

¶ *Intellectual Property, 1992.* One of the best-known agreements between the United States and China aims to protect patented, copyrighted, and trademarked material. The United States has sought improvement in this area from China for many years. After threatening sanctions, the Bush administration convinced China to undertake a sweeping update of its laws, which brought China's intellectual property protection regime largely into conformity with Western norms.

But these legal changes had little discernible effect. Chinese piracy of music recordings, computer programs, and films grew at an alarming rate at least through the mid-1990s. Movies and computer programs made by Chinese pirates turned up as far away as Canada and Eastern Europe.

After trying to address matters through quiet consultations, the Clinton administration threatened to impose trade sanctions in 1995. As the deadline approached, China agreed to step up enforcement. A year later, however, little had improved. Once again, the Clinton administration threatened sanctions. After much complaint, the Chinese agreed to a far more specific enforcement regime.

Under consistent pressure from the United States, China has regularly produced records of pirate operations it has shut down and invited the press to watch steamrollers crush pirated CDs. Although these actions show some effort to attack piracy, they also prove that it continues. Despite the limited success of American efforts, the affected U.S. industries estimate that their losses to piracy today are greater than they were when the subject of enforcement was raised in 1995.

Two points relating to enforcement warrant further attention.

It is perfectly clear that the families of leading Chinese officials, provincial leaders, and even the Chinese military have been involved in the piracy of intellectual property. Pirates reportedly set up facilities to make illegal CDs, for example, on People's Liberation Army bases, as a means of evading internal security police charged with shutting down pirate operations. The theft of intellectual

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property, in other words, has not been solely the province of street level criminals. Elements of the Chinese government have participated.

Second, according to firsthand reports, government ministries routinely illegally copy computer software for their use. Chinese officials promised to address this matter in 1995, 1996, and March 1999. The persistence of illegal copying by government ministries calls into question the sincerity of China's commitment to protect intellectual property.

Both the private sector and the Clinton administration have made enforcement of this agreement a priority for the better part of a decade. Yet glaring violations remain. Were it not for the high-level American enforcement effort, there is no reason to believe that China would have made much effort to keep the promises it made in 1992.

¶ *Market Access, 1992.* Unfortunately, other trade agreements have not benefited from the same high-level commitment to enforcement. The sweeping agreement on market access struck with China in 1992 is a case in point.

Through the early 1990s, China followed an unabashedly protectionist policy, excluding many foreign products with trade barriers. Threatening sanctions similar to those used later on intellectual property, the Bush administration successfully negotiated improved market access for U.S. exports.

In its latest reports on the subject, the Clinton administration states that China has "generally" fulfilled its commitments. On some of the easily verifiable points, like elimination of formal barriers and lowering of tariffs, China does seem to have implemented the agreement. In other areas, however, there have been obvious problems. Only three will be discussed here.

First, China agreed in 1992 to eliminate import-substitution policies. In the past, economic planners had developed strategies for replacing particular imports used in the manufacture of automobiles, pharmaceuticals, power-generating equipment, electronics, and so forth, with domestic products. Time and time again, the Chinese government has ignored this commitment.

China also agreed to phase out import licenses and not to raise new barriers. Shortly after phasing out import licenses, however, China announced new import *registration* requirements for many of the products previously covered by licenses. And a number of other new barriers on products ranging from electricity-generating equipment to pharmaceuticals have sprung up.

Finally, China agreed to make public all its laws and regulations relevant to foreign trade—a major change. As a result, many trade directives are now publicly available. Yet, this elementary provision has not been implemented in a number of areas, including government procurement regulations.

These are unambiguous violations of the 1992 market-access agreement. It is difficult to estimate their economic importance. Washington has officially noted them over a number of years, and Beijing has offered neither denial nor explanation.

One obstacle to pursuing these matters, Clinton administration trade officials argue, is that other U.S. government agencies have other priorities, and many private companies oppose trade sanctions that could compromise their business in China. If, however, agency indifference and private sector grumbling are sufficient to halt enforcement, it is doubtful that *any* trade agreement, particularly with a country willing to intimidate U.S. companies, will ever be enforced.

¶ *Textile Transshipment.* For decades, trade in textiles and apparel has been governed by the Multi-Fiber Agreement. Under the MFA, importers and exporters of textiles negotiate what amount to quotas on textile imports on a bilateral basis. As the world's largest textile exporter and the world's largest textile importer, respectively, China and the United States concluded a number of bilateral MFA agreements.

For some years, there have been reports of "transshipment" of textiles and apparel by Chinese entities: Chinese companies label textiles made in China as having originated elsewhere, usually Hong Kong or Macao, to avoid MFA limits. Because transshipment is illegal, accurate figures are not available, but a past U.S. Customs commissioner estimated that transshipment from China into the U.S. market amounted to about $2 billion annually. A more recent U.S. Customs study noted that Chinese textile exports worth as much as $10 billion were not officially accounted for, and much of this undoubtedly found its way into the U.S. market.

The Customs Service has undertaken a number of enforcement efforts, including reducing China's official MFA quotas as a penalty for transshipment. In 1997, China and the United States reached a four-year textile trade agreement that, among other things, strengthened penalties and reduced quotas in 14 apparel and fabric categories where there had been repeated instances of transshipment. Nevertheless, in May 1998, the U.S. trade representative and U.S. Customs brought an action against China under the agreement, imposing $5 million in charges on textiles illegally transshipped.

Each year, a list of companies involved in transshipment is released. On the most recent list, 23 of the 26 companies assessed penalties for illegal transshipment were from China, Hong Kong, or Macao. Despite such enforcement efforts, China continues to ignore the MFA.

¶ *Prison Labor.* China has an extensive system of prison work camps that produce products ranging from apparel to tools and machinery. Often, prison work forces are leased to private firms to assemble or manufacture various products. Under a 1930s U.S. law, it is illegal to import into the United States anything made with prison or forced labor.

Over the years, it has been alleged that a number of imports from China violated this law. In 1992, the Bush administration concluded a bilateral agreement to halt the export of goods made with forced labor and to hold periodic consultations between customs officials from both countries.

Despite the agreement, advocacy groups have produced evidence that various Chinese companies exporting to the United States are involved in prison labor commerce, products made with prison labor have been imported into the United States, and Chinese companies are prepared to export such products to the United States.

Because it is hard to distinguish goods made by prison labor from others, it is impossible to credibly estimate the size of the problem. However, the State Department's most recent "Report on Human Rights for China" found that Chinese cooperation under the 1992 agreement had been "inadequate" and that when complaints were brought by the United States, "the Ministry of Justice refused the request, ignored it, or simply denied the allegations made without further elaboration." The report also notes that Chinese officials have attempted unilaterally to define Chinese work camps as not covered by the 1992 agreement—an interpretation that renders the agreement virtually meaningless.

This review of the evidence shows that there have been serious enforcement problems with every recent trade agreement with China. In some cases, the agreements produced improvements in Chinese trade practices, but Beijing's implementation still fell far short of the letter and spirit of these pacts. Without the extensive U.S. enforcement effort on intellectual property, little of the progress that has been made would have come about.

China's defenders often claim that its record is no worse than that of other countries. Certainly, a number of U.S. trading partners appear to have cheated on trade agreements over the years. Japan is most often cited.

It is difficult, however, to find another trading partner whose compliance with every significant trade agreement has been so deficient. Furthermore, difficulties go beyond China's mere ignoring of provisions offensive to important domestic constituencies. As Chinese leaders themselves concede, China lacks the rule of law. In the trade arena, this means that it is difficult or impossible for Beijing to direct policy changes that actually bind China's diverse ministries, state-owned enterprises, and provincial governments.

Unfortunately, the World Trade Organization is no magical solution. Indeed, the WTO itself is a law-based institution. It is unclear that it will be able to police a country that operates without a stable, reliable legal system. Trade policies in China are often made in secret, leaving no paper trail. It may be impossible even to document the existence of objectionable Chinese trade practices, much less win WTO rulings against them.

To some, enforcement may seem a side issue. But none of the benefits ascribed to China's accession to the WTO will be achieved without it. If China simply ignores the terms of the WTO, as it has other agreements, not only will the benefits vanish, but lasting damage will be done to the credibility of the WTO.

Furthermore, no one knows how long China will be governed by relatively reform-minded leaders. Given the uncertainties of Chinese politics, a regime led by the military or hardline elements could easily emerge. Such a regime would pose enormous challenges for WTO enforcement, as well as on many other fronts.

In fact, China's membership in the WTO will help reformers like Zhu Rongji only if it entails compliance. Thus, an energetic effort to enforce the WTO in China is the best contribution the United States could make to the cause of reform. But American performance in this area inspires no confidence.

In light of Washington's weak and unpredictable pattern of enforcement and China's poor record of compliance, Congress should construct a vigorous enforcement procedure. This could take the form of annual reviews with a direct role for Congress, backed up by the promise of trade sanctions. Such a mechanism should be made a quid pro quo for permanent most-favored-nation trading status for China. Without it, there are good grounds to doubt that enforcement of the WTO will be a priority for the United States.

In the coming months, this issue will be discussed in a highly politicized atmosphere. But our relationship with China will last beyond next fall's election. Even if, as seems likely, China joins the WTO this year, bringing it into compliance with the WTO's provisions will take decades. Success will require the vigilance of Congresses and administrations for many years to come. If *this* Congress and *this* administration can build a sturdy framework for attending to these important issues, they will perform a great service to future Congresses, future presidents, the cause of reform in China, and America as a whole. ♦

Mr. OXLEY. Thank you. Thanks to all of our panel. Let me begin with my questions before yielding to my friend from New York. Let me ask Mr. Newhouse, you mentioned that Morgan Stanley has been in China for over two decades. Are there other comparable American companies, securities firms that are broker dealers and investment houses that are in China as well?

Mr. NEWHOUSE. I would have to say not comparable, in that there has been only one license granted for a joint venture investment bank, and that was the Morgan Stanley and CICC. It is currently contemplated there will be a number of additional, and this would have happened with or without a WTO quite frankly, a number of additional joint venture licenses granted within the next 12 to 18 months. Setting that aside, the opportunity exists currently for virtually all international financial intermediaries to intermediate, create between China and in the global financial markets. In other words, to operate as underwriters and distributors for external financings done by Chinese enterprises and by the government. So many of us compete in the global markets. Currently there is only one joint venture investment bank that is domestic.

Mr. OXLEY. What about European firms or other firms from, say, South Korea or Japan? Are they entrenched in China?

Mr. NEWHOUSE. Currently they are on the same status as the U.S. firms, but it is clear, as I said, with the momentum to import, if you will, transfer technology that with membership in WTO, China will be asking other international financial firms to embark in joint ventures for this technology transfer with Chinese firms. Obviously, this country's failure to grant normalized trade relationships would disqualify us from that. So I would say if this bill were not passed, you would see joint ventures that occur over the next 12 to 18 months. As I said, there will be several involving partners not from the United States, but solely from Europe and Japan.

Mr. OXLEY. Mr. Whittaker, you mentioned there are 20 million Chinese on-line currently; is that correct?

Mr. WHITTAKER. That should be by the end of this year, yes.

Mr. OXLEY. By the end of this year. How would that compare to the number of Americans on-line?

Mr. WHITTAKER. I don't know for sure, 22 million now.

Mr. OXLEY. So they are pretty close to us right now.

Mr. WHITTAKER. Growing very, very rapidly.

Mr. OXLEY. Frankly, I was struck by the phone calls that you got this morning. It pulled me away from Sportscenter. That is how fascinating it was. It was interesting because I was struck by the lack of information that most of the callers had, and frankly it was real scary. I thought you did a good job of handling it, but it was obvious that there were a lot of folks that didn't have a whole lot of information in that regard. They probably don't have a really firm grasp of what is really going on in China. Was that your impression?

Mr. WHITTAKER. That was my impression. It is obviously an emotional issue. There are any number of reasons why you might not like China or have the wrong impression of what is going on or have the wrong impression of this agreement, and that certainly came out this morning.

Mr. OXLEY. A lot of the critics of the PNTR say, well why should we reward China for, and then fill in the blank, whatever this particular transgression is, and the labor unions are talking about not giving China a blank check, whatever that means. But when I look at the agreement, all the concessions are on the side of the Chinese. We are not giving up anything, and they are basically making muck at opening concession in virtually every area. They are going from 100 percent on automobiles down to 25 percent immediately on the farm products, opening up markets for financial services that we are talking about today, and it boggles my mind to think that somehow we are doing them a favor by passing PNTR. Yet that is the kind of rhetoric we hear around these halls virtually every day lately. It is mind boggling.

Anyone else have any comment on that?

Mr. NEWHOUSE. I do. I would make this observation. The Chinese are also very aware of that fact. From their perspective, there is no economic reason why the United States would fail to pass this status for them because, in fact, all the benefits are to the United States.

Mr. OXLEY. Where is the largest opposition in China to this agreement?

Mr. NEWHOUSE. Basically, in those who want to keep the markets close, for example, the telecommunications industry, who wants to allow almost no investment. As you know, when Premier Zhu Rongji went home after his first attempt to negotiate an agreement here, the conservative powers over there made life very difficult for him. From the Chinese perspective, if there is no economic reason for us to oppose this agreement, the only reason for opposition must be some kind of basic hostility to China, and that is their attitude toward what this vote means. If there is no reason for us to do it for economics, we must be doing it for some other reason.

Mr. OXLEY. Anybody else?

Mr. MASTEL. If I could take issue with the statement a little bit. I support PNTR, as I said, in my testimony. But it simply is not true that the U.S. gives up nothing in the agreement. There are two major things the U.S. gives up. By making China a WTO member, we phaseout the textile restrictions faster than we otherwise would. That means China gets more access to the U.S. textile market than it otherwise would if it remained outside. Most importantly, the reason that China began this whole effort to enter the WTO was to get some assurance that it would be free from the threat of U.S. Unilateral sanctions as we threaten every year to withdraw them within, as we have threatened a number of times to impose sanctions on them.

Those are pretty good reasons. Those are pretty compelling reasons on China's behalf. I think it still makes sense to grant PNTR, but it is not true we don't give up anything in the debate.

Mr. OXLEY. Give me one example of how yearly votes on most favored nation has somehow changed attitudes or behavior on the part of the Chinese.

Mr. MASTEL. I didn't say it has changed attitudes or behavior on the part of the Chinese. I think, in fact, the annual threat ran out of credibility about 5 or 6 years ago, but the threat of sanctions has made a difference. In fact, the sanctions on intellectual property, as I explained in my testimony, is one of the important factors to push China toward better enforcement. The threats have some impact on China. That is, as I said, the whole reason that China began to go down the road for WTO membership was to get some assurance it would not be threatened by unilateral sanctions. They are not a bunch of rues. They have done a pretty good job of negotiating the agreement that achieves that goal for them. The U.S. Achieves many things, as you pointed out, but China gets some things, too.

Mr. OXLEY. It is obvious that China is going to join the WTO whether we vote tomorrow on PNTR or not; is that correct?

Mr. MASTEL. I think it is very likely, yes.

Mr. OXLEY. As a matter of fact, this administration has made it clear they would not oppose China entry into the WTO, and after the European deal last week, it is pretty clear that they will join the WTO. The real issue is whether we are going to take yes for an answer in regard to all of these concessions. That is basically the issue. I have run over time. Let me recognize my friend from New York, Mr. Towns.

Mr. TOWNS. Thank you very much, Mr. Chairman. Let me begin with you, Mr. Mastel. I am concerned about, it was your characterization of China in its failure to comply with commitments that it has made in the past. I note that you say China has failed even to make public its laws and regulations that pertain to foreign trade. What does this say about what our expectations should be that China will comply this time around, with its commitments to—would they actually file the agreement? What makes us think that this would happen? Is there any tiff here?

Mr. MASTEL. I think we should have some doubt. I was really struck today in testimony. I have done a number of these panels in the last couple of months that all the witnesses today cited the benefits of China's WTO accession. They seem not even to conflict the possibility that China would not fulfill its commitments. The reality is, every single agreement we struck with China in the last 10 years, I know intellectual property, on market access, on textiles, on prison labor, have all had serious compliance problems.

In fact, as we should expect, insurance would say we should suspect, if anything, China will not fulfill its commitments. WTO has a different enforcement scheme than bilateral agreements do, and it is a very well regulated process that relies upon the rule of law and transparent processes. None of those things really exist in China right now. There is no reliable rule of law. Many regulations are kind of made sub-rosa through administrative guidance. It is hard to know what the policy is in China.

I support, as I said, WTO membership for China, but let's be honest here. It is going to be a very long struggle to bring China into compliance, and it is a very difficult one. WTO is not a magical solution. It will take at least a decade, probably more, to really bring China in compliance. That should be the fundamental challenge the U.S. is facing now. That should be the real issue, I think, as opposed to talking about some of the side issues.

Mr. TOWNS. You agree with that, Mr. Watkins?

Mr. WATKINS. I would say there is no question that having gone and met with many of the governmental officials in China and the provinces that there will be compliance is not automatic. Compliance really, in most cases, is similar to our States here. It is difficult. The Providence runs their areas, and the central government makes policy. I do know from institutions I have had that the central government has been continually making efforts to impose compliance with a number of the policies that they have agreed to. There is no question it will take time.

My own personal feeling is in dealing with this, there will be more competition within China to gain investment in their local area, that that is their concern, local area, and to do those things that are necessary in the local area, to gain the investment. The more we can do that, the more they will deal with that, and they will, I know in dealing with local areas, they will do things to achieve investment that they feel is necessary for compliance.

It will not be overnight. There is no question in my mind, but there is a desire, one, for investment, and two, to do those things necessary to gain investment. If that means complying in many areas on a local basis, I think that can be achieved, but you have to educate them and have to work with them.

Mr. TOWNS. Why wouldn't the annual review get us there faster? Going year by year?

Mr. WATKINS. I really can't go into that totally, because it really would be speculative on my part. You have to understand China is 56 ethnic groups.

Mr. TOWNS. Sounds like my district.

Mr. WATKINS. Or Jersey City, right? I sell to those groups, too. It is a tough sale. But in those areas, the control of the central government is enforceable up to certain levels, but there is a lot of freedom on a local level in the provinces just to maintain that control. Now, I think it really is educational, and I do know from talking to local officials, there is more pressure for compliance from the central government. Whether it is achievable in all cases, I couldn't answer that.

Mr. TOWNS. Yes, Ms. Valko.

Ms. VALKO. Congressman, I would just like to reiterate a little bit of what Mr. Watkins said. I don't think China getting accession into WTO is going to be the silver bullet, as we say, to create compliance with everything all at once. If I can speak from the life insurance industry perspective from where New York Life comes from, today, right now, getting a license in that country is extremely unpredictable, is extremely non-transparent, and what the WTO agreement will do is start to give us some clear-cut factors as to how they identify and how companies can get licenses. And it will not be easily manipulated, politically done, as it has been in the past, and I think that is one step in the right direction, particularly from the life insurance side.

Mr. TOWNS. Thank you, Ms. Valko. Yes?

Mr. NEWHOUSE. Congressman, I am always more comfortable depending on enlightened self-interest than altruism for compliance with agreements. The facts are that China and China's leadership needs global openness for its economy if it is going to sustain the kind of growth rates, 8 to 9 percent, that are required for China to absorb its growing work force. So they are committed to the requirement to open their economic activity to globalization. That will not happen without the rule of law. Governments may enter into agreements where compliance is an issue, but businessmen don't.

So without the rule of law developing in China, the objectives that this global openness of economy that have been set forth by the government will not take place. Once this happens, I think you can be confident that the rule of law, the clarity of the regulations, will become a fact of life. Otherwise, the objectives won't be met.

Mr. TOWNS. Mr. Whittaker?

Mr. WHITTAKER. If I might, Congressman Towns, our view really is that the multilateral mechanism using 135 countries, with all its imperfections and difficulties and challenges, is far preferable to a unilateral sanction approach over the long run. I certainly agree that we all need to be vigilant, and actually our industry is gearing up programs to be able to work with Chinese Government officials, U.S. Government officials, and in the WTO, to address these kinds of issues which are a challenge, and we understand that and we are not naive in that sense.

But I think, as Mr. Newhouse said, ultimately what is really going to make things change is the commitment on the part of the Chinese Government to transform their economy. It is in their own best interest to make it work, their own economy, and it is also in their best interest to make sure that they behave and act responsibly in the WTO scheme.

Mr. TOWNS. Thank you very much. Thank you, Mr. Chairman.

Mr. OXLEY. The gentleman's time has expired. Let me just close with a couple of questions, if I may, and we will release this panel as I know the gentleman from New York has to go back. Let's assume for a moment that we don't do the right thing tomorrow and we don't pass PNTR. This is a very close vote, one of the closest votes I have been involved in since I have been in Congress, and it could literally could go either way. But let's say we, for some reason, we don't do that. Let me ask each one of you how you view that in terms of where you stand with your current and potential competitors in the Chinese market, where are they, who are they, and what effect would you have?

Mr. NEWHOUSE. As I suggested before, the short run, the competitive impact will be that clearly the Chinese response would be to grant concessions, and the joint venture licenses to non-U.S. firms. But I think more importantly, from our perspective, you can divide the world in a lot of different ways. Our firm chooses to divide it by latitude, if you will. Europe, the Americas, and Asia and the Pacific rim. In Europe, with the end of the cold war and with the reform of the Eastern European economies and the Soviet Union, that is on track. In North America and Latin America, Latin America particularly, with the progress Mexico is making that is on track, if you will, from our perspective as a global investment bank.

In Asia, China is the question mark. If China goes one way, that third leg, if you will, of our global investment banking and securities strategy, we will prosper. If it goes the other way, the opposite could be true. I think that, in my view, this vote and this stance taken by the United States will have a significant impact on the development of relationships between China and the west or in the U.S.

Mr. WHITTAKER. A couple of comments. One is I think rejection of PNTR would certainly hurt the prospects of the reformers in China, those entrepreneurs, those political groups that want to transform the Chinese economy. I think it would be a statement that the U.S. for some reason, is not part of this.

I do believe that we would, as an industry, face competition from Europe, Korea, Japan, Taiwan, any number of locations, very tough competition, and we would expect to be put at a disadvantage. Not only because we wouldn't get some of the advantages that would come from our being part of the WTO agreement with China, but also because I think our issues of reliability, questions that our Chinese customers would have about, are we a reliable supplier under these circumstances, and all of this would have a negative impact on us, and it would impact our ability to get the benefits to generate the exports and jobs here in the United States.

Ms. VALKO. We believe from the insurance industry, and certainly from New York Life, that without PNTR, and China remains closed to American insurers, it is very clear that the Europeans will end up getting licenses. In the past, what has happened is the Europeans have gotten doled out one license, and an American company has gotten one license in any given year. And it is very clear that if we do not end up voting for PNTR, that we are going to be at a clear disadvantage from the United States perspective of getting licenses in that country.

Our Europeans, the Japanese the Canadians, are going to be the ones that get the licenses granted, and quite frankly, we feel that we would ultimately be locked out from that marketplace to do life insurance.

Mr. WATKINS. European brokers service, European industry. Europe would have the edge on us, and so therefore, U.S. brokers would not be players at all.

Mr. YINGLING. I think it is important, if you look at this panel, to recognize you have high-tech and financial services here, and if you were picking two industries where the U.S. has a competitive leg up on the rest of the world, those would be the two high-tech and financial services. I think they would be more generally recognized in the high-tech area, but it is really true in financial services. We are the best.

So we would be shooting ourselves in the foot. Clearly, U.S. banks would be at a serious disadvantage, just as others have talked about the advantage of the Europeans and the Japanese in their sectors. That would be the case with banking. But it wouldn't be just in China again. It would hurt us throughout Asia. China is going to clearly be the economic base of Asia over time, and it would hurt us worldwide because if you are basically at a huge disadvantage and a huge country, it is going to hurt you worldwide when you are trying to compete.

Again, I put in a plug for community banks here. We have done a lot of work studying the future of rural communities, and the key in the next few years is agriculture exports. We are really at a crossroads in agriculture in this country, and if we don't open up those markets for our agricultural exports again in an area where we have a competitive advantage, our rural communities are going to suffer, and community banks in those rural communities are going to suffer.

Mr. MASTEL. Again, not to be a contrarian today. I agree with a lot of what was said. If we do imagine that the Congress turned down PNTR, which I guess I think is unlikely, but if we do imagine that, I think clearly reduction of—negative period of U.S.-China relations and the Chinese would try to find ways to have their ill feelings toward the U.S. known, but remember also, the U.S. has something like a $70 billion trade deficit with China. If the U.S. administration were willing to aggressively use its bilateral leverage to make sure that China didn't discriminate against U.S. companies, didn't grant licenses to European companies, I think that would be a powerful disincentive to China than embarking on a course of trade retaliation. But again, unquestionably, there would be a rough period in U.S.-China relations. I am not as certain as some of the other panelists are that that would mean the U.S. Would face direct retaliation. That is very difficult for the Chinese to pull off, especially in the face of the U.S. Having considerable resources on its own to counter those kind of threats.

Mr. OXLEY. Thank you. Mr. Rush, do you have any questions?

Well, that was good timing as we proceed to a floor vote. Thank you all very much for your excellent testimony and the subcommittee stands adjourned.

[Whereupon, at 3:50 p.m., the subcommittee was adjourned.]