



Hi, I'm Greg Autry, co-author (with Peter Navarro) of *Death by China: Confronting the Dragon, a Global Call to Action*. I teach macroeconomics at the University of California, Irvine where I am completing my PhD in management in the area of Public Policy and Economics. I have previously taught corporate strategy courses as well and speak regularly on China policy and China risk.

I'm greatly honored by this opportunity to speak at this China Forum co-sponsored by Scott Reid, M.P., the Chair and Vice-Chairs Irwin Cutler, M.P. and Wayne Marston, M.P. of the Human Rights Committee of the Canadian House of Commons.

This picture that I took at Coca Cola's China headquarters in Beijing two weeks ago, says a great deal about the dysfunctional relationship between the West and China's Communist regime.

The Reality Distortion Field

The reality distortion field was a confounding melange of a charismatic rhetorical style, indomitable will and eagerness to bend any fact to fit the purpose at hand.

- Andy Hertzfeld speaking of Steve Jobs



Walter Isaacson's recently released biography of Steve Jobs has given me a name for a phenomena I've been trying to define for sometime, "The Reality Distortion Field."

Apple employees and friends of Jobs describe it as Job's ability to look one directly in the eye and openly lie with impunity and to behave ways that were personally offensive and often ethically reprehensible with impunity. Jobs would still manage to keep everybody in line with his personal objectives.

Jobs would routinely say things that everyone in the room knew to be completely untrue and yet everyone would proceed in both discussion and action as if it were true. Confronting Jobs was simply not possible and joining him in lying to others was both easier and potentially more profitable. The more he got his way, the more powerful his Distortion Field became.

The Reality Distortion Field

After a while most of us gave up, accepting it as a force of nature.

- Andy Hertzfeld



I and many other analysts of China's brutal regime have been baffled at the inability of Westerners to see it for what it is. No matter how heinously the Chinese Communist Party behaves domestically, how aggressively it attacks cheats in trade, how blatantly it spies on our governments and business, and how very openly it prepares for war, we in the West remain paralyzed under its unwavering fake smile.

Reality remains what the Chinese Communist Party says it is and no amount of facts on the ground will move the discussion an iota. In the end, China, Inc. nearly always gets what it wants regardless of how bad that is for the people of China and the economies of the West. It is as though the leaders of the CCP possessed some special ability to suspend reality and project their own image of it directly into our group consciousness.

The Reality Distortion Field

Amazingly, the reality distortion field seemed to be effective, even if you were acutely aware of it.

- Andy Hertzfeld



The leaders of the Chinese Communist Party have grown up with a similar confidence in their own infallibility and power to define the truth as rulers of a vast totalitarian state. In China, with its massive censorship and propaganda machine, reality is defined by Hu Jintao and Wen Jaibao's pronouncements in the People's Daily.

If they assert that "China's currency is fairly valued", then IT IS FAIRLY VALUED!, regardless of the clearly stated trading ranges the government issues and massive sterilization mechanism they run to collect many billions of US dollars in their economy. If they say "China's rise is peaceful", President Obama welcomes "China's peaceful rise" despite the obvious evidence to the contrary in the largest military build-up of a dictatorship since the 1930s.

After 30 Years of “Engagement” and “Free Trade”:

- China’s domestic market is anything but free
- China’s trade policy remains mercantilist
- China’s environmental destruction has accelerated
- China’s human rights record remains abysmal
- China’s military grows faster than GDP
- China’s espionage and cyber attacks grow bolder

20 of the top 20 firms in China are still state-owned. This includes virtually all energy, resource, banking, telecom and advanced technology. Even the largest retailer is an SOE. The state sector is accumulating profits and capital faster than the private sector in a process the Chinese refer to as "国进民退" (The State Advances and the People Recede). Successful foreign firms are finding themselves rapidly displaced and even subject to various forms of unfair treatment at the hands of China's regulators.

China’s trade strategy remains based on currency manipulation, export subsidies, bold market protectionism, intellectual property theft and mostly: dump, destroy foreign industry, and claim monopoly rents. Foreign nations have NOT found the Ricardian benefits promised by "Free Trade" with this most unfree partner. US and Canadian trade deficits with China swell year after year and thousand of high value jobs are lost. China drives up trade deficits with our other trading partner by unfairly competing with our goods in those markets.

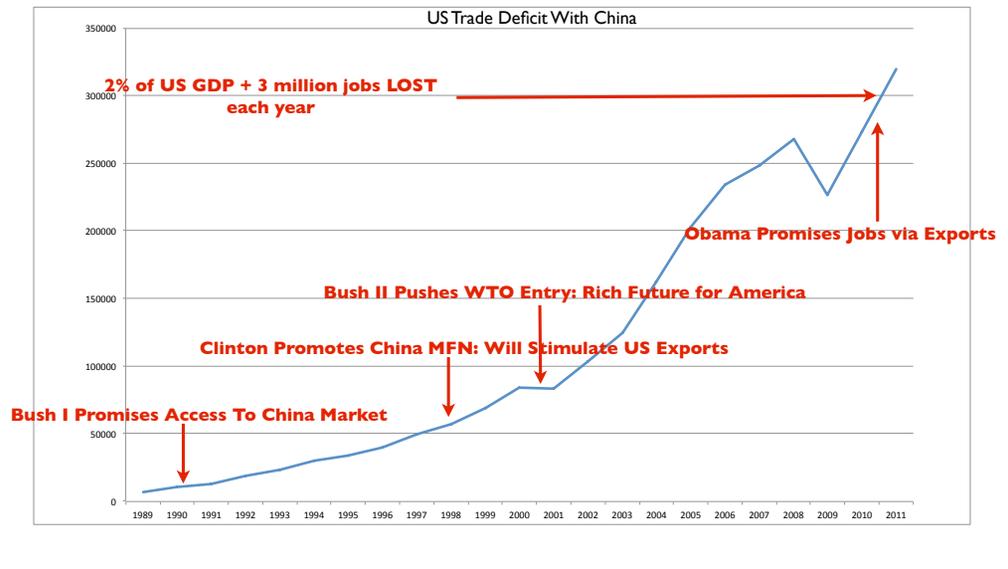
Despite a completely fabricated show of liberalism for the 2008 Olympics, the level of repression and spending on social control mechanisms has accelerated.

Despite a great deal of “green washing” and talk of alternative energy in its 12th 5 year plan the reality of China is coal, coal, coal and more coal. Levels of enforcement are so pathetic that the actual laws are totally irrelevant. Environmental protestors and lawyers continue to be repressed and often disappeared.

Despite facing no apparent external threat, China pursues one of history's most aggressive military build ups. Its weapons systems, both regional and strategic look increasingly expeditionary. China has provoked territorial conflicts with almost everyone of its neighbors: Taiwan, Vietnam, Japan, India, and the Philippines. These disputes could be resolved through negotiation with a democratic China, but the communist leadership in Beijing clearly views regional Hegemony as its prerogative and has no experience with the concept of compromise.

Chinese agents - many of them in an informal network of amateur spies controlled through their consulates - are constantly found snooping in Western governments and corporations. Revelations of significant cyber espionage and vandalism are a regular occurrence. There are dozens of documented instances of multimillion dollar thefts of intellectual property or spying that enables Chinese firms to cheat Western firms, including Canadian ones, on contracts and trade deals.

Someday Never Comes



And yet . .

- Canada, the U.S., and Europe stand idly by
- Realistic responses to China are met with a disconcerting silence or fearful warnings of “Chinese retaliation”
- Politicians, pundits, and business leaders rush to defend the Boys from Beijing

A Two-Pronged Attack

- Divide and Conquer
- Perception Management

China uses two primary techniques, both tried and true tools of previous authoritarian states, to get its way in the outside world despite its most unsavory nature. These are “Divide and Conquer” and “Perception Management.”

The second technique, Perception Management, is a process of co-ordinated media censorship both domestically and abroad along with the generation of a constant stream of carefully tailored propaganda aimed at Western populations, politicians, and business leaders.

Divide and Conquer

- Investors
- Corporations
- Industries
- Nations

China's divide and conquer strategy is hinged on its self-proclaimed status as "Belle of the Globalization Ball." Using the continuing mantra of "world's largest market" it lures investors, corporations, and nations into quickly striking very lopsided deals in hopes of establishing "first mover advantage" in China supposedly huge market and thereby gaining a competitive advantage over their peers.

China implies to each party that if it can just hold its nose and dive into bed with the Communist Party first it will find fabulous wealth. Of course, in reality the wealth and power flow in one direction - to China. However, while not actually finding much wealth, the victim does become so invested in China. Facing down Beijing - or allowing anybody else to do it is totally off the table. It's a process very much like what the American Mafia uses to gain control of industries (gambling, waste collection, drugs) in the U.S.

As each corporation becomes dependent on China's low labor standards and each investment bank becomes further embroiled in China's growing asset bubble they find their interests align more with sustaining China's success than with the long-term needs of their "home country." For more and more U.S. and Canadian multinational firms, North America is nothing more than a market for their Chinese made products. When that dries up the plan is to sell Chinese products to emerging economies in Latin America and Africa. As these puppet firms reduce their manufacturing costs through China's web of subsidies and trade cheats, their remaining Western competitors are forced to move production and investment to China.

As entire industries move to China their industry associations and lobbies line-up to defend China from demands that it play fair with its remaining victims. The elected representatives supported by these multinationals and influenced by the think tanks they support follow along with what they believe is the economic interest of their constituents, resulting in the sad spectacle of those who picture themselves as the World's champions of liberty and free markets defending a brutal regime with a centrally planned economy on the grounds of supporting "free trade."

China's separates developing nations from the developed world by supporting atrocious regimes with cash and via the prostitution of its UN veto power. Its attempts to sever Europe from America have been obvious. In the case of North America China is eager to see Canada follow the lead of the U.S. in dropping talk of human rights issues for supposed trade advantages. For Americans, Canada has often represented our better nature and while it is hard to complain when your neighbor commits your favorite sin, seeing that happen is certainly sad.

Perception Management

- In China the truth has always been what the Chinese Communist Party says it is
- China has confidently projected this “Reality Distortion Field” abroad
- By looking a timid West directly in the eyes and blatantly lying, Beijing avoids the harsh judgements that an objective global evaluation would demand



Perception Management / Propaganda – Basically, China must "normalize" its appearance to the world in order to do business . The Communist Party therefore runs a constant 7x24x365 campaign in the media, in political circles, in business forums, and at the firm and individual level to make us all believe that there is something pleasantly benign about the world's biggest totalitarian police state rapidly building the world's largest military into a high-tech expeditionary force. It's working remarkably well so far. The carefully managed Panda Bears; the well controlled tourist experience in China; the "entertainment", payoffs, and extortion of business people; the Confucius Institutes in our schools, the aggressive positioning of "The China Daily" as a serious news source; and the operations of hundreds of thousands of Chinese students and nationalist immigrants on the behalf of the CCP have given many Westerners very positive views of a place they would be horrified of if they truly understood it.

China's Rulers don't trust their own data

Chinese GDP figures are 'man-made' and therefore unreliable.

- Le Keqiang , China's next PM



According to a cable released via wikileaks in a 2007 conversation with U.S. Ambassador Clark Randt. Le Keqiang, the anointed next Prime Minister of China called China's GDP numbers "man-made" and "unreliable." Since he himself can't trust them he uses electricity consumption and railroad cargo figures to estimate how things are going.

GDP figures are "man-made" and therefore unreliable, Li said.

When evaluating Liaoning's economy, he focuses on three figures:

- 1) electricity consumption, which was up 10 percent in Liaoning last year;
- 2) volume of rail cargo, which is fairly accurate because fees are charged for each unit of weight; and
- 3) amount of loans disbursed, which also tends to be accurate given the interest fees charged. By looking at these three figures, Li said he can measure with relative accuracy the speed of economic growth. All other figures, especially GDP statistics, are "for reference only," he said smiling.

The reality distortion field masks significant risks:

- Economic
- Geopolitical and military
- Corporate
- Sovereignty
- Social Bifurcation

The reality distortion field hides several significant risks from Westerners

Geopolitical Risk

Sovereignty Risk

Economic Risk

Corporate Risk

Social Bifurcation Risk

The New Great Game



China is making provocative and outrageous territorial claims in the South China Sea as well as engaging in disputes with Japan, India and potentially Korea.

The South China Sea claim extends some five hundred miles from Chinese territory and deprives Vietnam, the Philippines, Brunei, and Malaysia of the majority of their coast lines. In reality, it is, of course, another Chinese resource grab and China's maritime fleet and navy have already begun a campaign of harassment against ships from these other nations.

Tools for Force Projection



China J-20



NATO F-35

The J-20, stealth fighter is a HUGE aircraft, with a very high ground clearance. These aren't the most desirable traits in a defensive, air-superiority plane, where maneuverability and a small profile are key. However this design combined with its stealth capability make it well suited for delivering heavy ordinance to distant ground targets and evading radar defenses in Vietnam, Taiwan, Korea and Japan.

Tools for Force Projection



Shi Lang
(first Chinese Carrier)



东风 -21D
(long range anti ship missile)

The Shi Lang is China's first aircraft carrier. While of little value in protecting China's already heavily armed coastline and not at all worthy of opposing America's carrier fleet, the Shi Lang none the less represents a significant shift in the regional balance of power for nations not directly protected by the US Seventh Fleet.

Vietnam and its claims in the Spratly's and Parcel Islands would be easy prey for the Shi Lang and an appropriate retinue of escort vessels. That small communist nation has been the victim of repeated Chinese aggression, most notably a 1979 invasion that resulted in hundreds of thousands of casualties. Vietnam's reaction to Shi Lang has been to order a fleet of attack submarines and other armaments from the Russians.

The Dong Feng 21D, however is an asymmetric weapon specifically designed to sink the American flattops at sea and drive the U.S. out of the Western Pacific. These two stage, solid fueled missiles are road mobile making them hard to detect on-launch and feature a mach 10 reentry and a nearly vertical angle of attack that could render the current Aegis - Phalanx defense systems useless.

This is NOT how a “Peaceful Rise” looks



海南“Hainan” Island Sub-base
(underground lair)

China is not only expanding its offensive nuclear capability against its “trading partners” but has also constructed a secret underground sub base worthy of a James Bond villain. The facility is designed to hide perhaps 20 missile boats, each with a dozen head rockets containing one or more nuclear warhead from Western satellite view.

This is not how any rational nation with obvious external threats responds to being handed great wealth. And yet there is absolutely no apparent connection to this and the trade that supports it.

China's Colonial Model

- China economically invades resource-rich nations with promise of trade wealth
- China demands access to domestic markets & destroys value-added manufacturing industries, while protecting its own market
- The victim nation becomes indebted to China and its impoverished consumers become dependent on low-priced Chinese products
- China corrupts and co-opts the political establishment
- Chinese SOEs buy up the natural resources and *exports them to China not the open market*

China's new colonial system threatens the sovereignty of resource-rich nations across the globe and represents a model Canada should be particularly concerned about. Time-after-time, China has gone into nations in Africa and demanded access to the domestic markets in exchange for large purchases of raw materials and infrastructure build-out projects to support their extraction. These nations expect a boom in exports and jobs associated with the development projects and are bitterly disappointed to find that China brings in Chinese engineers and workers by the thousands, treats the locals like second-class citizens, and destroys the local manufacturing and even agricultural businesses with its low cost imports. China has even moved in hundreds of thousands of farmers to grow "Chinese" food while also undercutting the local suppliers in poultry and other food stuffs. The resource rich nation finds itself running a large trade deficit with China and becoming ever more dependent on China for products like clothing it previously manufactured locally.

The Chinese business and political leaders –often the same people – buy off, threaten, or blackmail the national and local political leaders into compliance. Working conditions actually deteriorate. According to the Economist workers at Chinese copper mines in Zambia are granted hard hats only after two years of work. Chinese mining managers have become infamous for incidents of shooting at their workers when they complain about conditions.

Spies 'R' Us

- 2008 - US Election Email - Obama campaign, McCain Campaign, White House
- 2009 - GhostRAT - Dali Lama + 30 embassies
- 2010 - Operation Aurora - Google +200 "big firms"
- 2011 - ShadyRAT - UN, Olympic Committees, IMF, Businesses, Canadian government

The list of China's blatant cyber attacks on Western targets could fill a book. The government of China actively co-ordinates a three tier system of professionals, semi-amateurs, and student hackers that are given free reign and the tacit protection of the Chinese government as long as they do their spying and damage off shore.

China's claims that it can't track down these perpetrators are ridiculous in a nation that has the world's most largest Internet censorship operation. They certainly had no problem intercepting my emails last year and arresting a trio of dissidents I was scheduled to meet in Shenzhen.

In 2008 Chinese hackers infiltrated the email servers of the Obama and McCain campaigns as well as the Bush White House.

In 2009 a Chinese attack dubbed "GhostRAT" got into the Tibetan government in exile as well as 30 foreign embassy and several targets in the U.S. government.

In 2010 Google revealed it had been attacked and its source code stolen and later added that 200 other big firms had been compromised.

This year McAfee revealed "ShadyRAT" a Chinese attack aimed at a number of Western firms that were negotiating business with China and the governments of nations China has a particular interest in (Korea, Vietnam, India). The records also showed that the hackers had infiltrated several UN agencies, the International Olympic Committee, the olympic committees of several nations, and the World Anti-Doping agency.

Business Fails to see the Risk

- A trade war or military conflict between China and the U.S. is very possible
- In such an event the value of firms dependent on China could = zero
- Financial institutions may collapse
- Canada will be impacted

As we've discussed the economic situation is tense and Chinese regional aspirations and military preparedness foreshadows conflict in a region where the U.S. is heavily invested.

Yet many Western firms, such as Apple and H-P find themselves essentially 100% dependent on Chinese manufacturing. It is hard to imagine that in the event of a disruption in trade flows that these firms would not experience catastrophic losses and corresponding drops in share prices. Canadian firms like RIM, which are better diversified, should resist the pressure to follow the Pied Piper to Shenzhen.

Exporting Social Bifurcation



China is leading a “race to the bottom” in labor and environmental standards. In China’s Orwellian Marxist economy capital rules all and class segregation is greater than anywhere else in the world. Hundreds of millions toil as serfs in an unseen medieval world while the children of privilege party in a splendor with naive foreigners.

Exporting Social Bifurcation



Any nation that opens its markets to competition from China's work force of indentured servants locked in gender segregated dorms, working 12-16 hours a day, 6-7 days a week, 51 weeks a year will find its own society beginning to mirror China's. China's repressive labor model reverses the modern trend of increasing returns to labor and decreasing returns to capital. The impact has already been dramatic in the U.S. where real wage growth has reversed since China entered the WTO, ending a hundred years of growth for America's standard of living. U.S. consumer goods giant, Proctor and Gamble has concluded that the American middle class is headed for extinction and is now bifurcating its product lines to match the new Rich/Poor society.

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The Emperor has No Clothes

China's Government:

- is illegitimate
- is guilty of heinous crimes on par with those of Iran, North Korea, and Libya - nations it supports
- cheats on a *scale beyond any comparison* in trade
- spies on our nations, firms, and citizens
- is preparing for war against our allies and ourselves

We have seen no net benefit after 30 years of trading with and financing this beast

In the end we must admit that the Reality Distortion Field has lured us into a lie and must cry out loud that “The emperor has no clothes!” This means clearly stating to all that will listen the following simple facts:

China's government is illegitimate.

It is guilty of heinous crimes on par with those of Iran, North Korea, and Libya.

It cheats on a scale beyond any comparison in trade.

It spies on our nations, firms, and citizens.

It is actively preparing for large scale war against our friends and ourselves.

We have seen no net benefit from trading with or financing this beast.

As Franklin said "We must all hang together or we shall surely hang apart." The first step is admitting that we have an enemy in the Chinese regime and our allegiance should be to our own citizens, our allies, and to the repressed people of China - in that order.

See the forest through the trees

If we can't deny these specifics, we must conclude:

There is at best a systemic ethical failure in China and at worst a conspiracy of evil.

Western pundits, even China's strongest apologists, have a very hard time defending that nation when faced with its litany of abuses including: espionage, censorship, trade cheating, currency manipulation, militarism, support for the most odious regimes, pollution, repression of fundamental human rights, ethnic cleansing. They will simply ignore most of them and attempt to white wash others with comparisons to Western actions in the past in a weak attempt at establishing moral equivalency that fails to consider the stunning scope and depth of China's scurrilous behavior.

Even China's critics in particular areas, such as trade and human rights, fail to place their own concerns into context with the other issues.

Taken as a whole the obvious conclusion must be that: There is at best a systemic ethical failure in China and at worst a conspiracy of evil.

If you don't believe me
take it from an expert

Policy Suggestions

- Trade rules should be reciprocal

All trade rules should be reciprocal. I.e. If a Canadian manufacturer cannot enter the Chinese market without being forced into a minority joint venture and being compelled to transfer its technology, then the Chinese firms must also enter a joint venture. If they don't have any unique technology to transfer to Canada then they must pay a fee for market access commiserate to the value of technology Western firms dole out to their Chinese partners.

Policy Suggestions

- Prevent the “siloiing” of issues

Canada (and the U.S.) must stop conceding to Chinese demands that human rights, trade, censorship, military and other matters all be negotiated separately. China’s strategy closely integrates all these issues. As when they use censorship as an excuse to block market access for Western Internet companies like Facebook or YouTube or when they use prisoners for labor or execution victims for their organ business.

In regards to sanctions connected to basic human rights or the weapons proliferation, the West should not apply one standard to Muslim nations - Iran, Syria, Libya, and another to China.

Policy Suggestions

- Canada should join the US in opposing Chinese currency manipulation

Canada must also oppose Chinese currency manipulation because it greatly distorts global markets and undermines the export of all other nations. It isn't just a U.S. problem. China's currency sterilization system creates a myriad of market inefficiencies that punish Canada, Europe and other countries as well as America.

In any case, Canadians should pay attention to what is going on in the US-Sino relationship because it will strongly impact them, like it or not.

There is a very strong feeling in the U.S. Congress that action will need to take place and the leading presidential candidate, Mitt Romney has promised dealing with China would be his “first order of business.” A recent poll showed 70% of Americans think China is an “economic threat” and 27% identify it as an “outright enemy.” This is a huge shift in just a few months. Many in the both the Tea Party and Occupy movements are now eyeing China as a prime suspect in America’s economic collapse.

Policy Suggestions

- Eject Chinese *state owned* media outlets until reciprocal and **UNCENSORED** access is permitted in China *and* credible efforts to protect Intellectual Property are seen

2.Canada (and the U.S.) should prevent entry of China Daily and ALL other Chinese media including TV, Radio, and websites into their markets until reciprocal and completely **UNCENSORED** access is permitted in China and credible efforts to protect Western intellectual property are truly implemented. At the very least this must apply to state owned media.

Policy Suggestions

- Treat Internet attacks for what they are - hostile acts of a foreign power

Ignoring blatant Chinese incursions into government agencies and into businesses for purposes of obtaining unfair advantages in trade or acquiring technology should be openly presented and appropriate counter measures taken What on Earth makes us think that continuing to "play nice" while this goes on will result in better behavior?

Policy Suggestions

- State Owned Enterprise of totalitarian states should be barred from purchasing any Canadian asset

No State Owned Enterprise should be allowed to purchase any assets in Canada including stock in public companies until there is a democratic government in Beijing. Selling Canada's precious assets directly to a regime that is hostile to the very principles for which it stands cannot be right.

China Management

- A body to coordinate a mutually beneficial response to China should be established by free nations lest they be subverted via China's divide and conquer

Canada, The U.S., South Korea, Taiwan, India, Japan, and Europe must understand that they are all in a similar position in regards to the negative economic and geopolitical consequences of China's unpeaceful rise. Formation of a coordinate response is the only way to confront China's one at a time, divide and conquer technique.

The Truth Matters



Words have meaning and in the end the truth matters.

If you allow yourself to become a victim of China's Reality Distortion Field and begin to parrot the Communist Party's empty slogans of "Peaceful Rise", "Friendship", and "Free Trade" you have traded the ideals our nations were founded on along with the futures of both the children of China and the West. They deserve to share a future of freedom and prosperity. They deserve to have jobs that can support a family with dignity and governments that respect that work and their rights. That is worth a lot more than the short term profits that can be gained by joining the Boys from Beijing's exploitation of its people and the world's resources.