

How Bill Clinton and American Financiers Armed China

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Hi,

Welcome to BIG, a newsletter about the politics of monopoly. If you'd like to sign up, you can do so [here](#). Or just read on...

It's the 70th anniversary of the People's Republic of China, which Xi Jinping is celebrating with aggressive rhetoric and a militaristic display of his ICBMs that can strike at the U.S. in 30 minutes. So today I'm going to write about how American aerospace monopolists, dumb Pentagon procurement choices, and the Bill Clinton administration helped create the Chinese missile threat we are now confronting.

But first, two house-keeping notes. First, I asked for stories about management consulting stupidity, and you responded. I'll be publishing some of your thoughts, from both the employee side and the consulting side ("confession of the Bob's"). Feel free to send me your story if you haven't yet. I'm going to be delving more into what seems to be a crisis of management in corporations and governing institutions across the West.

Second, the piece I wrote [WeWork post](#) went viral. It was reposted on Business Insider and the Stigler Center's ProMarket blog, and someone sent me an email with this wonderful line: "By the way, I knew Adam Neumann before he launched WeWork and everything you said about him is 100% accurate." I wrote that piece partially because I know there are 10,000 people who had to work for Neumann and deal with his behavior, and someone needed to point out that cruel behavior from bosses is not ok.

And now...



How America Equipped China with Missile Technology

In August of 1994, Bill Clinton's Secretary of Commerce, Ron Brown, flew to China to try and seal two deals for American corporations. The first was to enable Chrysler the ability to build minivans in China, and the second was to get the Chinese to buy 40 MD-90 aircraft 'Trunkliners' from McDonnell Douglas.

The McConnell Douglas deal was particularly important to the Clinton administration for a number of reasons. The company was dying; it was badly run by financiers who lacked an appreciation for quality production. More importantly, it had lost a key military contract for the F-22 in 1986, so the government felt an obligation to find customers to prop it up. There was also politics, with Bill Clinton trying to honor his unofficial 1992 campaign slogan, "it's the economy, stupid." Clinton would indeed hail the deal on the eve of the 1994 midterm election.

The Chinese agreed to buy the planes, but with [one caveat](#). They wanted a side deal; McDonnell Douglas should sell a mysterious company called the China National Aero Technology Import and Export Corporation (CATIC) a set of specialist machine tools that shape and bend aircraft parts stashed in a factory in Columbus, Ohio.

When Chinese representatives went to Columbus, Ohio, workers wouldn't let them see the tools, because workers realized that they would lose their jobs if the tools were sold to the Chinese. The Chinese then sent a letter to the corporation saying that the deal for the Trunkliners was at a stalemate, but if the machine tools were sold to a mysterious Chinese company, well, that would have a "big influence" on whether McDonnell Douglas could close the deal on the planes.

It wasn't just the workers who caused problems. The government could have been a hurdle for McDonnell Douglas as well, because these weren't just any old machine tools. "According to military experts," reported the New York Times, "the machines would enable the Chinese military to improve significantly the performance abilities -- speed, range and maneuverability -- of their aircraft. And if diverted, they could do the same for missiles and bombers." Selling the tools wasn't just a commercial deal, the machining equipment was subject to export controls for sensitive national security technology.

It was an insane idea, selling the Chinese government this important machining capacity. The Pentagon protested vehemently, as did Republican Congressman Tillie Fowler, who was on the Armed Services Committee. Fowler said allowing the transfer reflects an "emphasis on short-term gain at the expense of national security and long-term economic gain." And yet that's what McDonnell Douglas sought, and what the Clinton administration pushed through. The Commerce Department cleared the deal, in return for a pledge (or behavioral remedy) that China would not use the tools to build missiles, but would dedicate them to a civilian aircraft machine tool center in Beijing.

[McDonnell Douglas](#) basically knew the behavioral remedies were fraudulent almost immediately; one of the most important pieces of equipment was shipped not to Beijing but directly to a Nanchang military plant. It wasn't just McDonnell Douglas who understood the con; Clinton officials [had the details of the deal](#), and let it go through anyway. Why? They used the same excuses we hear today - competitiveness and a fear of offending China. Here's the NYT explaining what happened.

"American officials want to avoid sending any signals that would fuel China's belief that the United States is trying to "contain" China's power, militarily or economically. And they know that if they deny a range of industrial technology to China, other competitors -- chiefly France and Germany -- are ready to leap in and fill the void."

China never honored the overall deal. By 1999, China had [acquired](#) only one of the 20 promised Trunkliner airplanes. And three years later, the Federal government [indicted](#) McDonnell Douglas for "conspiracy, false statements and misrepresentations in connection with a 1994 export license to sell 13 pieces of machining equipment to China." The government also went after the Chinese company.

Still, this was too little too late. The episode was by any metric catastrophic; the Chinese government got missile making machine tools in return for a promise they didn't honor, which should have been a massive scandal, borderline treason. But ultimately it wasn't a scandal, because Republicans, leading globalization thinkers, and Clinton Democrats decided that transferring missile technology to China didn't matter.

Remember, during this entire period, Bill Clinton pressed aggressively to open up the U.S. industrial base to Chinese offshoring. And towards the end of the Clinton administration, McDonnell Douglas, as we all now know, later [merged with Boeing](#), and that merger ended up destroying the capacity of Boeing - by then the sole American large civilian aircraft maker - to manufacture safe civilian planes.

How Bill Clinton Made the Worst Strategic Decisions in American History

Chinese power today is a result of a large number of incidents similar to this one, the wholesale transfer of knowhow, technology, and physical stuff from American communities to Chinese ones. And the confused politics of China is a result of the failure of the many policymaking elites who participated in such rancid episodes, and are embarrassed about it. As we peer at an ascendant and dangerous China, it makes sense to look back at how Clinton thought about the world, and why he would engage in such a foolish strategy.

Broadly speaking, there were two catastrophic decisions Clinton made in 1993 that ended up eroding the long-term American defense posture. The first was to radically break from the post-World War II trading system. This system was organized around free trade of goods and services among democratic nations, along with somewhat restricted financial capital flows. He did this by passing NAFTA, by bailing out Mexico and thus American banks, by creating the World Trade Organization, and by opening up the United States to China as deep commercial partners.

The Clinton framework gutted the ability of U.S. policymakers to protect industrial power, and empowered Wall Street and foreign officials to force the U.S. to export its industrial base abroad, in particular to China. The radicalism of the choice was in the intertwining of the U.S. industrial base with an autocratic strategic competitor. During the Cold War, we had never relied on the USSR for key inputs, and basically didn't trade with them. Now, we would deeply integrate our technology and manufacturing with an enemy (and yes, the Chinese leaders saw and currently still see us as enemies).

The second choice was to reorganize the American defense industrial base, ripping out [contracting rules and consolidating power](#) into the hands of a small group of defense giants. In the early 1990s, as part of the 'reinventing government' initiative, the Clinton team sought to radically empower private contractors in the government procurement process. This new philosophy was most significant when [it hit the military](#), a process led by William Perry.

In 1993, Defense Department official William Perry gathered CEOs of top defense contractors and told them that they would have to merge into larger entities because of reduced Cold War spending. "Consolidate or evaporate," he said at what became known as "The Last Supper" in military lore. Former secretary of the Navy John Lehman noted, "industry leaders took the warning to heart." They reduced the number of prime contractors from 16 to six; subcontractor mergers quadrupled from 1990 to 1998. They also loosened rules on sole source—i.e. monopoly—contracts, and slashed the Defense Logistics Agency, resulting in thousands of employees with deep knowledge of defense contracting leaving the public sector.

Perry was a former merger specialist who fetishized expensive technology in weapons systems. But what Perry was doing was part of an overall political deal. In the 1980s, the Reagan administration radically raised defense spending. Democrats went along with the spending boost, on condition that they get to write the contracting rules. So while the Reagan build-up was big and corrupt, it was not unusually corrupt. When Clinton came into office, his team asked defense contractor how to make them happy in an environment of stagnant or reduced defense spending. The answer was simple. Raise their margins. The merger wave and sole source contracting was the result.

The empowering of finance friendly giant contractors bent the bureaucracies towards only seeing global capital flows, not the flow of stuff or the ability to produce. This was already how most Clinton administration officials saw the world. They just assumed, wrongly, that stuff moves around the world without friction, and that American corporations operate in a magic fairy tale where practical problems are solved by finance and this thing called 'the free market.' In their Goldman, McKinsey and Boston Consulting Group-ified haze of elitist disdain for actually making and doing real things, they didn't notice or care that the Chinese Communist Party was centralizing production in China. They just assumed that Chinese production was 'the free market' at work, instead of a carefully state-sponsored effort by Chinese bureaucrats to build strategic military and economic power.

Part of this myopia was straightforward racism, an inability to imagine that a non-white country could topple Western power. Part of it was greed, as Chinese money poured into the coffers of Bush-era and Clinton-era officials, as well as private equity barons. This spigot of cash continued through the Bush and Obama administrations. For instance, during the Obama administration, Mack McLarty - President Bill Clinton's first chief of staff - [made \\$300 million in luxury auto dealers](#) in China after Secretary of State Hillary Clinton's chief of staff helped broker an introduction to key Chinese leaders.

But most of it was a general view that the role of American policy leaders is to sell American finance abroad. Here's how Larry Summers put it in a 1998 speech pompously titled ["The Challenges of Success."](#) I bolded a few parts.

The world looks very different than it did at the beginning of this decade, a time when America was said to be in decline. It is now clear that America will grow faster in this decade than Japan and Europe. Their four-decade-long story of convergence has ended and America is pulling further ahead. Why this success? A large share of the credit must go to the two forces that this conference brings together: **technology and finance.**

The twin forces of intonation technology and modern competitive finance are moving us toward a post-industrial age. And if you think about what this new economy means - **whether it is AIG in insurance, McDonald's in fast-food, Walmart in**

retailing, Microsoft in software, Harvard University in education, CNN in television news - the leading enterprises are American.

In fact, Summers was papering over problems in the American engineering world that had been slowly festering for some time. I got a remarkable email from an engineer who watched this happen first-hand, which I've pasted below my signature. Read it. He details the intertwined problems of failed governance and corporate leadership that started in the 1980s but really accelerated in the 1990s.

The Clinton, Bush, and Obama administrations didn't notice these problems, because they lacked the wisdom to listen to engineers and people who actually work for a living. They didn't understand that workers who blocked Chinese buyers looking at vital machine tools had savvy and integrity that they themselves lacked.

Today, because of that lack of wisdom, the dangerous and increasingly totalitarian Chinese leader Xi Jinping has the capacity to launch missiles at the U.S. that can hit American cities in 30 minutes, and feels no need to disguise his global ambitions. It didn't need to play out this way.

If we change our strategy, we can prevent the end of liberal democracy or civilization itself. That is on us, across the West, and among those who believe it is in the capacity of humanity to build a peaceful and prosperous world.

Thanks for reading. And if you liked this essay, you can sign up [here](#) for more issues of Big, a newsletter on how to restore fair commerce, innovation and democracy. If you want to really understand the secret history of monopoly power, buy my upcoming book, [Goliath: The 100-Year War Between Monopoly Power and Democracy](#).

cheers,

Matt Stoller

P.S. I got this remarkable email from an engineering who watched the collapse of American aerospace and military technology first-hand.

I worked for the U.S. Air Force at Wright-Patterson Air Force Base from 1970-1980. That is when the problems with the US Aerospace industry really began. Jacque

Gansler was really the instigator of what William Perry ultimately accomplished. Jack between his 2 stints with DoD Jacque got his PhD in Economics. But before this degree, his ideas were already frozen that the Defense Industry had to consolidate because of economies of scale. Those of us managing technology exchange between the competitors thought otherwise.

After I left DoD, I continued to watch this consolidation folly as a consultant to Defense contractors, including Sunstrand. Harry Stonecipher was President and CEO of Sunstrand. After destroying Sundstrand, he moved to McDonnell Douglas, orchestrated the Boeing merger and then proceeded as the president and COO of Boeing to plant the seeds to destroy Boeing.

But, back to Jacque. Jacque not only hollowed out the Defense Industry, he did the same to the ability of DoD to manage the industry. My job at Wright-Patterson Air Force Base was in Manufacturing Technology. We actually had real engineers who did real work. There were our counterparts in each of the manufacturing plants. This included both civilian and military engineers. There were honest to God reviews and fights over what was to be done and how to do it. During the time period of 1970 to 1980's The DoD designed and produced the A10, F15, F16, F14, F-117, B1B the C5. Also, a fleet of Cruise Missiles, the HumVee and the M1 Abrams. It was a most exciting and honest time.

In my latest stint with DoD my job was not manufacturing. But old friends asked me to visit Boeing and look at the problems with the 787. In spite of my clearances and position, Boeing would not let me near the 787. I was allowed to look at 737 production. In the old DoD, a telephone call from the Pentagon to Boeing would have changed this. Now, it was clear that Boeing was in charge.

I was also asked to visit the F35 plant in Fort Worth. This was the former General Dynamics F16 plant. General Dynamics was a victim of consolidation. I was quite familiar with how the plant was back in the 70's and 80's. Gordon England, who later became DepSecDef was at GD Fort Worth at the time. But, that is yet another story.

Lockheed did let me have as much time in the F35 plant as I wanted. And, I had free reign to talk to anyone. I was totally appalled by what I saw. It was clear that the rate of production promised would not be accomplished with the plant as designed. Even

more disturbing was that there was complete lack of DoD oversight - none. There were no DoD engineers in the plant. Back in the Pentagon I asked to meet with the procurement people who were in charge of DoD industrial policy. There had been such a thing during the time when DoD did not take 35 years to produce an AC that still does not meet its design objectives and did not cause pilots to pass out – the F35. I was told that the lack of an industrial policy is an industrial policy. Around that time the administration changed from Bush to Obama and the situation only got worse. I let it go and continued my job while continuing to seethe inside.

The lack of an industrial policy is not only in the DoD. As a private pilot I follow closely General Aviation. Similar consolidation as occurred there. Troubling as that is, it is not as serious as the fact that the Chinese have taken over the US General Aviation industry. There are 2 piston AC engine companies. Continental and Lycoming. Continental was Teledyne. Now, it is owned by the People's Republic of China, as is Mooney.

The US General Aviation industry collapsed in the 1970's. In addition to product liability issues, there had not been a change to the design of GA AC for decades. Cirrus Aircraft started in 1984 and totally disrupted and nearly revitalized the industry with the design of plastic piston AC. This was followed by a personal jet. Today Cirrus builds more AC each year than all of the other piston AC manufacturers, and probably will do the same with their jet. They are owned by People's Republic of China since 2011. Piper AC has escaped the Chinese. They are owned by the Government of Brunei.

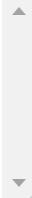
These Governments are not here because of the airplanes. They are here for the manufacturing technology - composites in the case of Cirrus. They are here because today's GA AC are platforms for the most advanced avionics and, in case of Cirrus, jet engines in the world. I doubt that a Chinese engineer could walk into the door of Garmin - the leader in AC systems. But, certainly a Cirrus engineer can. The Cirrus Glass Cockpit is equal to those of today's airliners. The Cirrus Jet engine is made by Williams International. Williams makes jet engines for our Cruise Missiles. The Chinese must really think Americans are naïve, if not totally stupid.

Matt, I know that my little soliloquy goes beyond your piece about Boeing. Doing forensics on the troubles with Boeing is only the tip of the iceberg.

Comments



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