

**Demetri Kofinas:** 00:00 Today's episode of Hidden Forces is made possible by listeners like you. For more information about this week's episode, or for easy access to related programming, visit our website at [hiddenforces.io](http://hiddenforces.io), and subscribe to our free email list. If you listen to the show on your Apple Podcast app. Remember you can give us a review. Each review helps more people find the show, and join our amazing community. And with that, please enjoy this week's episode.

**Demetri Kofinas:** 00:47 What's up everybody? My guest today is Kyle Bass. Kyle is the founder and Chief Investment Officer of Hayman Capital Management, which is an investment manager of private funds, focused on global, event-driven opportunities. Many of you will already know Kyle, either from his appearance in Michael Lewis', "The Big Short," or from countless media appearances and talks that he's given over the years.

**Demetri Kofinas:** 01:18 What's perhaps less widely known is that he is also a founding member of "the Committee On The Present Danger: China," which is a nonpartisan group who's stated mission is to help defend America through public education and advocacy, against the dangers posed by the People's Republic of China under the rule of the Chinese Communist Party, which it views as an existential and ideological threat to the United States and to Western, liberal democracies and values.

**Demetri Kofinas:** 01:51 Regular listeners to this show will know that I have devoted a number of episodes to China. To understanding its banking system, to understanding the complex web of relationships between the Chinese Communist Party and its corporate state champions, as well as to the vast Chinese bureaucracy that governs over 1.4 billion people.

**Demetri Kofinas:** 02:15 And I think the reason why I felt it's important to try and understand China, is because there's been this narrative that we've been given and which has proliferated over the last decade or so, which essentially says that "we are living in the Chinese century - that the future is China - and that America is a receding power, and that we need to accommodate China's rise into the international order, so that we can peacefully transition into a world of continued prosperity."

**Demetri Kofinas:** 02:50 And I think this narrative was acceptable to people like me, because it also came with the assurance that a Chinese century was not incompatible with a liberal, international order, and that China would either fold itself into that order or that it would lead it. Certainly, it was never suggested that China would overthrow that system, or that it would build an entirely new one along more authoritarian, or dystopian lines.

**Demetri Kofinas:** 03:20 But I think the facts seem to undermine that narrative, and I think that's why the crackdown in Hong Kong is so disturbing. It's why the Orwellian social credit system seems so bewildering to those of us living in

Western, open societies. And it's why I think we all have a really hard time processing these reports published in major Western outlets, like the New York Times and the Wall Street Journal, about re-education camps and crematoriums being operated in Northwestern China, that are reportedly housing somewhere around 3 million people who are not only being held against their will as so-called prisoners of conscience, but whose organs are, in some cases, being forcefully harvested and sold to people flying in on appointment for the express purpose of having a transplant.

- Demetri Kofinas:** 04:22 I just don't understand how that works. And honestly, I'm not sure I want to. I think Americans and Europeans are starting to ask themselves, "What exactly is a Chinese century supposed to look like?" because it's one thing to hand the baton over to someone who more or less shares your governing principles. But I'm not sure that this is really what's on offer here. And I'm not sure that many Westerners would be on board with living in a world shaped along more authoritarian lines, irrespective of whether those lines are Chinese, American, Russian, or anything else for that matter.
- Demetri Kofinas:** 05:08 I think most of us can agree that adopting China's model, would be a step in the wrong direction. But we need to decide what is most important to us, both economically and morally. Because the tools of 21st century totalitarianism, or "instrumentarianism," as Shoshana Zuboff has so aptly put it, bear little resemblance to their 20th century analogs. They are insidious, they are omnipotent, and they are largely invisible. And I'm afraid that their adoption would bring about a world that none of us would ever want to live in.
- Demetri Kofinas:** 05:49 And with that, I bring you yet another timely, and important conversation this week with my guest, Kyle Bass.
- Demetri Kofinas:** 06:04 Kyle, welcome to Hidden Forces.
- Kyle Bass:** 06:06 Great to be here. Thanks for having me.
- Demetri Kofinas:** 06:08 It's really exciting having you. Here you are. You're not unexpectedly chill. You're kind of...that's what I would've expected. I usually have a certain... I have expectations about what the guests are like, but I know that they can deviate. And usually I'm on target like 80% of the time. But there are times where I'm really off. It's always interesting. I try to hone that in. So, I was telling you that when I started preparing for our conversation, of course, I focused at the top on the Hong Kong dollar peg, and China overall. And of course, global macro, global economy, et cetera, financial markets.

- Demetri Kofinas:** 06:45 But as I started digging in and preparing more and more, I came to actually see that the more interesting overarching theme is that you and a number of other people are part of this growing collective of individuals, who feel that the framing of U.S., China relations is fundamentally wrong, and that the only thing that is effectively missing is something along the lines of a George Kennan, Long Telegram moment. Where not only the diplomatic core of American foreign policy, but also the population at large can reorient to understand that we are in fact in a new cold war with China. Is that accurate?
- Kyle Bass:** 07:33 I think it is accurate. I think when you look at the Ascension of China into the WTO in 2001, it changed everything. And we allowed China to ascend, prior to its ability really to ascend under this agreement that we have with them, and the WTO has with them, and the promises that they made as a part and parcel for their ascension. And to this day they haven't lived up to those promises. They don't live up to any promises they ever write down.
- Kyle Bass:** 08:02 But what's important, I think when you think about how we engage with China, the first question one must has to ask themselves today is, "Why do we engage with them?" And it's literal, meaning you have a country that has somewhere between one and 3 million ethnic Uyghur's in concentration camps, that they call them re-education camps. We in our intelligence edifice knew that something was going bad there when we noticed crematoria being built at each of these centers. They're not electing a new pope every time white smoke comes out of these things.
- Kyle Bass:** 08:36 And so it's important for me to think about how I frame my view of a regime like China's, today. Why do we interface with someone that takes more than a million people against their will, because of their ethnic or religious preference, and puts them in camps? And yet we can't wait to do another day's worth of business with China. We can't wait to chase the 1.4 billion people, the allure of future profits, and economic greatness, irrespective of their gross human rights violations, their lack of respect for the rule of law. They don't have one. They rule by law, not of law. And truthfully, if people take the time to read the facts that are out there, and try to understand what China does on a daily basis to subvert, take advantage of, steal, lie, cheat their way through their relationship with us. What come away from the conclusion, I think logically and think that we actually shouldn't be engaging with them. We should send them on their way.
- Demetri Kofinas:** 09:40 So I do want to talk about some of the financial parts of that. You and Roger W. Robinson, and others have done a lot of good work in fleshing that out. For those who aren't familiar with what's happening in Xinjiang, what are you talking about?

**Kyle Bass:** 09:54 So you know, it's been widely reported and many of the journalists have tried to get in to Xinjiang. Xinjiang, they used to call it East Turkestan, right? And basically, it's the Northwest corner of China where they ethnic population is primarily Muslim, and they're roughly 10 million ethnic Uyghur's there.

**Demetri Kofinas:** 10:17 China took that land over in 1949, correct?

**Kyle Bass:** 10:19 That's exactly right. When they drew that dotted line in The South China Sea and took over.

**Demetri Kofinas:** 10:23 I think it actually means, "The new territory", in Chinese, is that right? In Mandarin?

**Kyle Bass:** 10:25 You're exactly right. So, Xinjiang is a province of people that don't really look ethnic Chinese, they look more like Tibetans, or Muslims. And I think that what's happening is a full cultural genocide there. Meaning they're taking parents away from their kids, they're putting their kids in remedial grade schools. They're bulldozing graveyards to remove any kind of cultural attachment, or religious attachment to the land. And the rest of the world does nothing about it.

**Kyle Bass:** 10:58 And the reason the rest of the world does nothing about it is because they can't wait to invest another dollar in China, in the hopes of making a positive return. So, what's happening in Xinjiang is something that is reminiscent of what Hitler did in Germany. And I don't say that lightly. When Hitler was asked what he's doing with the Jews, he said, "Don't worry about it. They're less than 1% of our population." When China was asked about what they're doing within ethnic Uyghur's, in Xinjiang, they said, "They're less than 1% of our population. Nothing to see here." They said exactly what Hitler said.

**Demetri Kofinas:** 11:30 Well. Also, another thing that they're doing that we haven't talked about is the organ harvesting. Which is so horrific, that I think that's a parallel with the Holocaust in that it's difficult to imagine it. In other words, during the Holocaust, there were Jews that were coming over from Europe that were telling Americans what was happening in Nazi Germany, and it wasn't that people didn't believe them, they just couldn't imagine. It seems like something similar is happening.

**Kyle Bass:** 11:57 You're exactly right. One of the horrors that is happening in Xinjiang today, is in organ harvesting. If you go onto the internet and just type in Chinatribunal.com, the UK just concluded a tribunal run by one of the top lawyers in the UK, the QC. And he was the person who oversaw Slobodan Milosevic's war crimes trial in the Hague. So, this is a bonafide, deep dive into investigating the organ harvesting phenomenon in Xinjiang, and in China.

**Kyle Bass:** 12:31 And basically the conclusion of this tribunal, if you read the summary, I think it's roughly 25 pages. They talk to doctors that left because of what the horrors they saw. They talked to people that have escaped. They've talked to service providers. And it was 200 plus people they interviewed for this tribunal. And what the tribunal concluded is they actually tissue type and blood type everyone that they bring in. They call them prisoners of conscious. But we can just say the people that are taken against their will and putting in concentration camps.

**Kyle Bass:** 13:02 And they are actually paralyzing them. While they're awake, they're ripping their breastplate open and taking whatever organs they need to take, while they're awake. It's got to be the most horrific way to die you can ever imagine. If you could choose to die, I would choose to be in the gas chamber before I'd let you rip my kidneys out of me while I was awake. So, this is happening. The waiting list for an organ in China is three days. The waiting list for an organ in the U.S. is a year and a half. And to your point, it's so hard to imagine because we don't have pictures, we don't have videos.

**Demetri Kofinas:** 13:33 So I think what you just said actually was what drove it home for me. Was that in an interview that you did with General Spalding, that he said he had a contact in Israel, a doctor-

**Kyle Bass:** 13:42 Yes.

**Demetri Kofinas:** 13:42 ... whose patient came to him and told him that he was flying to China for a scheduled organ donation-

**Kyle Bass:** 13:49 In a month.

**Demetri Kofinas:** 13:50 ... in a month. And the doctor was stunned because he said, "How's that possible? You can't schedule an organ donation." [crosstalk 00:13:56]

**Kyle Bass:** 13:56 You can't schedule a heart transplant, right?

**Demetri Kofinas:** 13:59 ... a heart transplant. That's what brings it home. The fact that you can schedule that, it means that there are people that are being harvested.

**Kyle Bass:** 14:05 It's why the Israelis immediately banned organ tourism to China.

**Demetri Kofinas:** 14:10 Hmm. All right, so we're going to circle back to this. I just wanted to give some context at the start, but let's actually kind of circle back to Hong Kong, because that's also the most timely crisis. And I think also what's interesting about Hong Kong, is that it puts into focus what a world in which China's authoritarian model pushed upon open societies would look like.

**Demetri Kofinas:** 14:37 Hong Kong is not a democracy, but it is a liberal, Western society in its orientation. A lot of that has to do with its relationship to Great Britain, but also the crisis continues to escalate. We've covered it on this program, on a number of episodes. We also had Joshua Wong on the program. And I think Sunday there was someone who was shot, I don't know if he was killed, in the streets of Hong Kong. I saw a video today of a woman, pregnant woman being pepper sprayed.

**Demetri Kofinas:** 15:03 There is nuance, obviously. I'm sure it's difficult for the police as well in this situation, but what are you following? What are you seeing, and what is the situation now in Hong Kong?

**Kyle Bass:** 15:13 Yeah, Hong Kong it's such a difficult thing, again, for people in the U.S. to understand. But imagine if you lived with a basic law, a Western rule of law, like Great Britain's for the last call it hundred plus years. And then all of a sudden, the Chinese Communist Party was going to remove those freedoms and was going to do it in one fell swoop, and basically tell you that they can extradite you to China, just based on an allegation by the government.

**Kyle Bass:** 15:45 There'd be no judicial oversight, no judicial review. Just a rubber stamp, a perfunctory stamp. These people have been living in Hong Kong for decades, and now all of a sudden out of the blue, they're having communism thrust upon them. And the fact that Carrie Lam has now recently invoked, the Emergency Ordinance Act, allows them to take property, to take your bank account, to incarcerate you, where you have no legal or judicial recourse. Basically, it's martial law. And I think the youth of Hong Kong are fighting for their lives, something they thought they'd be doing in 2047.

**Kyle Bass:** 16:22 So you probably know, back when Margaret Thatcher and Deng Xiaoping negotiated the handover of Hong Kong back to the Chinese. That negotiation happened in 1984, and that deal was signed with the UK in '84, and then in '92, the U.S. basically set forth our governing agreement, the Hong Kong Policy Act of '92. And so, we thought that China was going to leave Hong Kong alone, leave the British law in place, leave the rule of law in place, basically allow free and democratic elections in every position except for the chief executive who China gets to choose. And what we see happening, is not 2047, it happens to be 2019, and it's happening right now.

**Demetri Kofinas:** 17:06 For listeners who haven't heard our episodes with Ho-fung Hung, or David Webb, I suggest you listen to those. We go into some details about the history, particularly with Ho-fung Hung. How do you feel this narrative is currently being spun in mainland China? And how much control does the CCP have over the views and opinions of Mainlanders in your estimation?

**Kyle Bass:** 17:26 Look, the rhetoric coming out of the mainland China accounts on Weibo over the weekend was really sickening. That young man that was shot point blank in the chest, no weapon, nothing in hand, was walking towards a police officer that had someone else detained, and was just shot in cold blood in the middle of the street. And we see this on video, so we're not having to interpret something that I read. But the mainland Chinese said he deserved getting shot, and they should shoot all of the Hongkongers. That they have it too easy, and the mainland Chinese...

**Kyle Bass:** 18:03 You asked me how it's being spun. So, if you look at the rhetoric in Mandarin that's coming through CCTV, and the China Daily, and Global Times, you'll see that the narrative that's being spun on the mainland is the Hongkongers are causing all of the riots. And then many of the cases, they say the U.S. And our intelligence agencies are the root cause of all of these problems. And by the way, as we all know, communist government controls the narrative. They control the press, they control the police, they control the printing press, the money.

**Kyle Bass:** 18:34 And so the Chinese government is masterful at developing narratives. And by the way, they project those narratives all the way over here with their "news organizations", which are just propaganda outlets.

**Demetri Kofinas:** 18:46 Mm-hmm (affirmative). So how is this impacting Hong Kong's economy at the moment?

**Kyle Bass:** 18:51 Yeah, Hong Kong's economy is falling off a cliff. If you look at real estate sales, if you look at GDP. By the way, it's only going to get worse and worse, because of what we're seeing in, call it the last five days. If I told you a year ago, if I showed you a picture of what happened at the Chinese University in Hong Kong last night, and I said this is in Hong Kong one year from now, you would throw me out the window. You would say that will never happen. And here it is happening today. It looked like a war zone in Beirut back during the civil war, right? So, I think what's important to understand is you have a generally peaceful population of only seven and a half million people, and you have riots happening on a daily basis now, whose intensity continues to multiply and worsen, and you have the Chinese government and their Politburo Standing Committee member that's in control of the Hong Kong affairs tell you that it's about to get uglier.

**Demetri Kofinas:** 19:51 So I want to bring in your thesis on the Hong Kong dollar. When did you begin to develop this?

**Kyle Bass:** 19:57 So let's talk about Hong Kong in general. So, I won't talk about the positions or anything that we do for FCC rules. But I will talk about as far as our interest in Hong Kong began three years ago, and our investments in Hong Kong began two and a half years ago. So, one could say we had a little bit of foresight, it wasn't too hard to see that this was

going to come to a boiling point. Truthfully, it's happening sooner than we thought. But Hong Kong has a severe financial disadvantage that used to be an amazing advantage. And what I mean by that is you just back up 10 years, and first of all, back up 36 years, back when they pegged their currency to the US dollar, when you peg your currency to another currency, you're basically letting, I say, let Jesus take the wheel. You're really letting-

- Demetri Kofinas:** 20:43 I like that expression.
- Kyle Bass:** 20:44 ... the central banker of the country you're pegging to, you're basically seeding your monetary policy to him, or her. And so basically Hong Kong has essentially no control over its own policy, I.E., because if you don't move your interest rates exactly with the country that you're pegging to, that will create capital flows one way or the other and your peg will break. So, you have to basically keep your rates almost identical to avoid capital flows one way or the other. Either stronger or weaker. And so, when you're seeding your control of your monetary policy to another power, you must have synchronicity in your economy, I.E., if our economy is growing, and theirs is contracting, and we're raising rates and they have to raise rates while they're contracting, that is the worst possible thing that can happen to an economy.
- Demetri Kofinas:** 21:36 Especially if they have a very leveraged private sector and banking system.
- Kyle Bass:** 21:40 Exactly. And what's important to note specifically with Hong Kong is they just had the best 10 years they will ever have, I.E., 2008 the United States goes into a financial crisis. We drop rates 5% to zero. And Hong Kong goes along with us, and drops rates to zero, at the time in which their one trading partner, China went to the gas pedal and started growing double digits. So, what happens when you have free money, and your number one trading partner's growing GDP at double digits, you have money flying over the walls, you have real estate going up exponentially, which it did. It's gone up almost 800% in 10 years, I mean in mass. And so, when you have the best 10 years of your life, then you get to a point where you have the converse, and that's what's happening today. You have a banking system that's levered 900% of its GDP, I.E., if you remember when Ireland and Iceland and all of the European economies that fell like dominoes in the European financial crisis.
- Kyle Bass:** 22:42 I would say the number one common denominator was the amount of leverage in the banking system as a percentage of GDP. So, when bank loans start to go bad, they break the whole country. And so, Hong Kong is at a level that you saw Iceland and Ireland at, at 900% of GDP. The other side of the story there is to your point, is private sector leverage. So private sector credit to GDP is 300% in Hong Kong. To put that into



context, both the US and Japan, one would say the US and Japan are two of the most levered private sectors in the world, we're at 150. And so now you have an economy that's tanking, and the travel services deficit is exploding.

- Kyle Bass:** 23:26 And everything in Hong Kong is coming to a standstill, and you're doing that in the most levered, most expensive economy in the world. One of the reasons also, you're seeing the youth, I think act in the manner in which they're acting, and this is happening all over the world, with interest rates at zero globally, asset prices become very high. So, an unintended consequence of central bank money printing is the rich get much richer. The middle-class has to rent those assets, and pay such high rent levels that they can't afford it anymore. And there's no upward mobility, because things cost too much. And so, what you're seeing in Hong Kong is median home price to median income is 21 times. In the US at the peak of our subprime greatness, we got to six and a half. So, there's really only one way to go in Hong Kong, and it's fundamental restructuring of their economy.
- Demetri Kofinas:** 24:18 So let's connect the dots here, because this is an important element. Let's connect the dots to the peg. Now the Hong Kong Monetary Authority says it has roughly 400, the last number I saw was 436 billion US dollars of foreign exchange reserves to protect the peg. Your calculation puts that actually at 57 billion of what can actually be used to viably defended it. I want to also connect the dots to why it's important that there's so much leverage in the banking system in the private sector, and what the implications are for that if Hong Kong had to raise interest rates in order to defend the peg, if they ran out of foreign exchange reserves. And maybe where you can also compare this to some other instances of currency pegs breaking like in Thailand or in Argentina for our listeners.
- Kyle Bass:** 25:04 So, how long is this show?
- Demetri Kofinas:** 25:07 Well we've covered them a little, we've covered them a bit in some prior episodes. We did one for listeners with Barry Eichengreen that you should listen to where we covered some of these peg breaks. We also did one with Robert Johnson when he and Stanley Druckenmiller and Soros shorted the Bank of England. So those are some examples to listen to, but just sort of give us your best analysis of it.
- Kyle Bass:** 25:27 Sure. So, for those of you that have a deep acumen in financial markets, we've recently seen fed funds, and a problem in the US funding markets where we saw the Federal Reserve sets the rate range for fed funds, and then we saw fed funds spiking hundreds of basis points in the US, and for the United States economy, that actually scared a lot of people as to what was going on.

**Demetri Kofinas:** 25:51 The repo market.

**Kyle Bass:** 25:51 The repo market. So again, this is a little bit of an Archaean concept, but it's going to answer your question in another way. In the US, we had 4.6 trillion on the Fed's balance sheet at the peak, their desire, their publicly stated desire was to get it down to somewhere around two and a half trillion. We wrote a piece in May of this year that basically stipulated that there's this thing called the Basel III liquidity capital ratio, and this basically maintains that banks need to have a certain amount of liquidity on their balance sheet in case we enter a recession, or there was a run on the banks.

**Demetri Kofinas:** 26:26 They raised those liquidity coverage ratios.

**Kyle Bass:** 26:28 So Basel III, Dodd-Frank has these liquidity coverage ratios that are required of all banks, and the only way to satisfy that is basically one of two ways. You either have government bonds, or you have the cash that you have on deposit at the Federal Reserve, both of those can be used as that allowable collateral for the LCR. What we said in May was that the Fed can't get its balance sheet much below three and a half trillion, because then the available collateral in the system, given the leverage of our system and the size of M2 will actually disappear. And the Fed would have to go into action. And people said we were crazy in May. And now, people understand that that's true. That comes back to Hong Kong. They said they had around 435 billion, they had 20 billion run in one month in August. And that was the biggest draw down since the pegs beginning 36 years ago in Hong Kong, since the imposition of their currency board.

**Kyle Bass:** 27:28 So what's important to note about that, again, what we look at is there's a certain amount of reserves out there, but there's a finite amount of usable reserves. You can't use cash that's on deposit at your central bank from other central banks. You can't use private equity and ports and things that you count in your assets as a government, but you can't defend your peg with liquid assets. And so, we make a number of adjustments and came to the conclusion prior to that number in August, is they had about 57 billion, we think that number is about 35 billion now. By the way, we don't know what happened last month, and we don't know what's happening this month. But I can tell you it's probably not inflows, right? So, what's happening is their system that's highly levered is shrinking. And that's just like quantitative tightening, right?

**Kyle Bass:** 28:15 When reserves leave, it's quantitative tightening. And that's what the majority of the participants don't quite understand. But if you have a quantitative tightening anymore, you're going to have rates move in a big way. So today, the Hong Kong interbank market on the one-month side is much higher than the US market. And on the one-year side it's also higher. And in overnight it's actually materially higher today. It's 40,

50 basis points higher. And that would tell all of us that things should be okay, over there, I.E., in the capital flows because their rates are higher than ours, they're earning a little better of return. So therefore, money shouldn't convert to dollars. The problem is money is converting to dollars, and money's leaving, and so you're having a quantitative tightening in the most levered developed country in the world. Oh, and by the way, there is no doubt that they'll have a banking crisis going forward, because you have a highly levered economy entering a recession. We all know what happens then.

- Demetri Kofinas:** 29:12 And aren't you seeing some indication of that in either Chinese banks that are based in Hong Kong, or Hong Kong banks that are raising deposit rates?
- Kyle Bass:** 29:19 Yeah. You have done your work here.
- Demetri Kofinas:** 29:20 Oh, I always do.
- Kyle Bass:** 29:21 You have done your work. So yeah, it's fascinating because it's only for new money. So, it's a very interesting way for the Chinese banks and even the banks in Hong Kong to try to attract foreign exchange reserves in, without having to raise the rate on all of their existing money. Because again, that would break them almost immediately. And the mortgages in Hong Kong, all the real estate loans, all the mortgages are indexed to one month overnight, the high bar rate, and they reset every month. So, imagine if you didn't know what your mortgage payment was going to be every month, especially if rates are really-
- Demetri Kofinas:** 29:56 They have to keep rolling that over, and they are perpetually short dollars.
- Kyle Bass:** 29:59 That's correct. And so, the real issue here is for instance, one week ago, the Hong Kong banks were trying to attract Australian dollars. Again, anything that they can spend, they can't spend Chinese money, so they can spend any other FX. So, they were willing to pay 11% for seven-day money, on new money. And so that goes also to show you that there's a pretty big panic going on already. It's a precursor to a banking crisis.
- Demetri Kofinas:** 30:27 So I also love that you mentioned the repo market. I do want to try and touch on that towards the end if we can, or in the overtime. I think the monetary base got something close to \$250 billion shy of your target of 3.5 before we started seeing hiccups in the repo market, because I think that is a really interesting story, but what does all this mean for China? Because Hong Kong is so important to mainland Chinese, particularly the elites who have used it as a way to get their money out, but also for Chinese corporations that are based in Hong Kong.

**Demetri Kofinas:** 31:02 They've also used Hong Kong as a way of raising external capital, which is something I really want to get into, because those numbers are remarkable. And honestly, like I told you, I have to prepare for an episode in order to cover a subject, and I really was kind of blown away by the number of companies that operate either on exchanges in the United States or OTC. And Robinson's done a lot of really useful work in that regard that I looked off of, but sir, that's my kind of general question.

**Kyle Bass:** 31:31 Yeah. Look, I think that Hong Kong is China's golden goose. It's where they raise the majority of their US dollars globally. And again, China is desperately short dollars. They're short energy, they're short basic materials, they're short base metals. They are short food. They have to import all these things, and they have to pay, they can't pay RMB for it because no one takes monopoly money.

**Demetri Kofinas:** 31:54 They have a closed capital account.

**Kyle Bass:** 31:55 Yeah, they have a closed capital account. So, they need to attract dollars one way or the other. They can either borrow them, they can get people to invest in their companies, and list them on the Hong Kong exchange for dollars, where they can steal things. But the bottom line is, Hong Kong is the conduit for the Chinese to raise money, but what's more important to the Chinese right now is maintaining power. And maintaining power supersedes any of these other things for China. And so that's why we think that you're going to see a banking crisis. It's already set to happen. Like there is no saving Hong Kong's economy. Their banks are going to blow up. And when you have something that's this tightly wound, and you have a business decline, as rapid as we're seeing there, there is no putting Humpty back on the wall. The question is, will that affect the currency? Will that affect the exchange rate between Hong Kong and the rest of the world? And that's an open question today.

**Demetri Kofinas:** 32:51 So then there's another question also that I think is operative, which is what happens politically in such a situation, right?

**Kyle Bass:** 32:58 Politically in which country?

**Demetri Kofinas:** 32:59 In Hong Kong. Well obviously,, this is a difficult subject to cover, right? Because it's one country, two systems, or supposedly two systems and all of this is in flux. What does a banking crisis in Hong Kong mean for the current political crisis between Hong Kong and the mainland?

**Kyle Bass:** 33:16 It just makes it more difficult. Look, it's our view that you're going to see Carrie Lam replaced. I mean, it's interesting. She's lost the respect of her people. She's lost the respect of Beijing. I mean she's finished.

**Demetri Kofinas:** 33:25 She's in a bad situation.

**Kyle Bass:** 33:27 She is finished. So, the question is, who do they replace her with? And it'll likely be a Beijing hardliner. They're already talking about implementing Article 23, which is as you know, the sedition rendition, a national security law that is way worse than the extradition bill. It's kind of the comprehensive martial law bill that basically puts China in charge. But you say what'll happen politically, in the end, Hong Kong will just be another city in China.

**Demetri Kofinas:** 33:54 You think that's inevitable?

**Kyle Bass:** 33:56 Well, we know it's inevitable in 2047, the question is it inevitable in 2020? And I say given the escalation of what we're seeing now, the fact that the emergency ordinance resolution's been enacted, I think it's inevitable that is in 2020, it will be Hong Kong, China.

**Demetri Kofinas:** 34:12 And I think we got a window into the mindset of the CCP and their commitment with the NBA situation. I think that the level of sensitivity to the speech of NBA coaches and players, I mean if they're that sensitive in that situation, it's hard to imagine how they would ever allow the situation in Hong Kong to continue, which again, that's disturbing for the rest of us. On the one hand, the question is also to what extent should and is American foreign policy trying to support the people in Hong Kong? I know there are some legislative initiatives being put forward by people like Marco Rubio and others are being pushed. Maybe the 1992 status will be revisited, but I think it's disturbing, and this brings us into kind of the larger conversation, which is this reframing of the US/Chinese relations. And one of the things that I touched on, and maybe this'll be an entry point, is really the extent of which the CCP has been using US capital markets to fund its foreign exchange reserves, its current account. Can you kind of flesh that out for our listeners?

**Kyle Bass:** 35:28 You ask some really tough, long-winded questions that have very long winded answers, but the bottom line is China used to run a very big trade surplus with the rest of the world. That's how they built up their, call it 4.6 trillion dollars' worth of reserves on their balance sheet. And now they say it's three, we think it's closer to two, and that's a working capital number that they need to operate with. So, what they're doing around the globe is everything they can to borrow or issue equity in their companies, because money's fungible. So, if a, let's say Tencent issues a bond and in the US, or a gas exemption, or they issue a bond in Hong Kong, that money, those dollars actually go to China, INC. They don't really go to Tencent.

**Demetri Kofinas:** 36:16 Because these are state champions.

**Kyle Bass:** 36:17 Yeah. Well also because it comes into the Chinese central bank, they can show it on Tencent's balance sheet, but they can go use those dollars somewhere else. I.E., the government can. And so, I think it's important to note that the Chinese companies have borrowed 1.1 trillion dollars-

**Demetri Kofinas:** 36:33 Is that a BIS number?

**Kyle Bass:** 36:34 The BIS number over the last just five years. It's gone up exponentially. And now you're seeing an intense desire for Chinese companies to list in Hong Kong. And then I don't know how many people you know that own companies like Alibaba, or Tencent listed on the US exchange, but you don't own anything. You own a share in a variable interest entity in the Cayman Islands. That is a tracking entity for that in China. So, if things went poorly, and you thought you owned a share of a company that had some sort of value, you actually own nothing, and people need to understand that.

**Demetri Kofinas:** 37:12 Can you flush that out a little bit more? What do you mean when you say that?

**Kyle Bass:** 37:16 If you buy a share of Alibaba today, if you pull up your IRA or your trading account or whatever you do for your savings, and you tell E-Trade or you're a broker at Merrill Lynch or whatever, Goldman Sachs, you say, buy me some shares of Alibaba, the one listed on the US exchanges, right? B-A-B-A, right? You're buying an ownership interest in a Cayman Island entity. It's called a variable interest entity, a VIE, and that has no claim to the assets in China. You're basically just saying, I'll buy this thing because other people are buying it. And Alibaba does all of these things around the world and has a big record sales day over the weekend. But if in the event of a financial, let's say a financial problem, and let's say they have a bankruptcy, you, the American shareholder have a bankruptcy, you, the American shareholder of Alibaba don't own a thing.

**Demetri Kofinas:** 38:06 How do regulations not protect investors from this?

**Kyle Bass:** 38:09 So, that's the best question you've asked all day because the importance of how China manipulates our markets, we entered into an agreement, the PCAOB, which is the Public Company Accounting Oversight Board here in the U.S., entered into an agreement 2013 with the CSRC, which is China Securities Regulator, and we agreed to not force the Chinese companies to submit themselves to covered audits. So, today, those companies like Alibaba and Tencent and many others don't ever submit themselves to an audit like U.S. companies do. U.S. auditors aren't allowed to review this.

**Demetri Kofinas:** 38:47 Which is crazy when you hear it for the first time.

**Kyle Bass:** 38:48 It's like, can you believe this? So i.e., Chinese companies are raising money in the U.S. from unsuspecting U.S. investors without a basic covered audit and without being Dodd-Frank compliant like all the U.S. companies have to do.

**Demetri Kofinas:** 39:03 Well, some of this was covered in the documentary, The China Hustle, which I saw, which was remarkable that they were actually bringing investors in to some of these factories. They were making them run while the investors were there, and then, when they were leaving, they just-

**Kyle Bass:** 39:15 Turn them off.

**Demetri Kofinas:** 39:16 ... turn them off, which is absolutely remarkable.

**Kyle Bass:** 39:18 Yeah. I mean, look, they did it in Sino-Forest. A lot of people lost a lot of money. Imagine how much fraud is really there if you were to audit these things, and so, it's our view that the United States should implement Rubio's Equitable Act. An Equitable Act should just stipulate ... Again, this isn't anti-China. This isn't saying we're going to cut off capital flows to China. We will say China, Ecuador, you name places, Venezuela, if you want to list companies here, we might even overlook your political dysfunction and your gross human rights violations, but if you want to list a company here, you're going to have to bring it up to U.S. securities law compliance. God forbid that we level the playing field here in the U.S. to foreign companies. I mean, that should be a given.

**Kyle Bass:** 40:03 One thing that many investors also don't know is when foreign nationals, let's say Chinese people, invest in the U.S., let's say they invest in Uber and they make half a billion dollars or they invest in Intel and they make several million dollars, when they sell it and take their money back, they don't pay any tax. So, what's also very interesting is they use our legal system to adjudicate grievances, and they pay nothing into our judges or our system. There are some inequities out there that must be rectified.

**Demetri Kofinas:** 40:34 So, here's the question. How did we get this? How did this happen? How did we get to a place where the regulations have been written in this way or being gamed in this way and that Chinese companies and the CCP have had their way with America for so many years?

**Kyle Bass:** 40:51 Look, we allowed them in the WTO in 2001. We assumed our state department, our president, our presidential edifice, we all believed that if we allowed them to taste Western capitalism, that they would liberalize their capital account, they would liberalize their economy, they would become more Western. Even George Soros has recently said that we gave them the benefit of the doubt, and they blew it.

**Demetri Kofinas:** 41:18 Davos speech 2018.

**Kyle Bass:** 41:20 Two weeks ago, he actually was more punitive. I don't know if you saw it.

**Demetri Kofinas:** 41:23 No.

**Kyle Bass:** 41:24 He said we gave them the benefit of the doubt, and we were wrong. They went the other way, and he said, " China is our mortal enemy. As soon as we realize this, we'll be able to set policy going forward." So, this is a guy that has spent his entire life investing in the Open Societies Foundation, he is a massive proponent of globalization and free trade, and here is the poster child for globalization telling you that China is our mortal enemy, and we must act.

**Demetri Kofinas:** 41:56 That speaks volumes. The Chinese ... I say the Chinese, it's sort of a stand in for the Chinese elite, the governing council, what I think you or Bannon call the cadre.

**Kyle Bass:** 42:06 Yes.

**Demetri Kofinas:** 42:08 They have used money and Americans' greed as a lever to manipulate U.S. foreign policy in their direction. When we're talking about companies, I also want to note that I think a figure I saw was something around 700 companies are listed either on U.S. exchanges like the NYSE, NASDAQ, and over the counter markets. A lot of these companies are companies that I think most Americans would not want to invest in if they knew what they did, companies like Hikvision, which make the surveillance technology that's actually used in some of these concentration camps that we just talked about.

**Kyle Bass:** 42:44 That's right.

**Demetri Kofinas:** 42:45 Or China Shipbuilding, which actually builds military submarines and other-

**Kyle Bass:** 42:50 Aircraft carriers.

**Demetri Kofinas:** 42:50 Aircraft carriers.

**Kyle Bass:** 42:51 Yeah.

**Demetri Kofinas:** 42:52 AVIC, same thing with aerospace equipment. These are military companies.

**Kyle Bass:** 42:56 That's right.



**Demetri Kofinas:** 42:57 They're using American markets to fund the development of the Chinese defense system.

**Kyle Bass:** 43:02 It's truly shocking, but you know, even amongst my friends that are professional investors, when I bring a prospectus or I show them what the offering was ... I mean Xinjiang, as a province, came to the U.S. and sold \$200 million worth of bonds.

**Demetri Kofinas:** 43:19 I read that.

**Kyle Bass:** 43:19 It is unconscionable.

**Demetri Kofinas:** 43:21 They used that money to build the camps.

**Kyle Bass:** 43:22 They used that money to build ... Well, not only that, the World Bank who the U.S. taxpayer creates their AAA credit rating, the World Bank lent Xinjiang 150 million for education purposes, and I don't know if you saw recently in Foreign Policy magazine, they called them out.

**Demetri Kofinas:** 43:40 So, I did not see that, but I want to kind of find a way to reiterate something and circle back on this point that I made at the very beginning, which had to do with the long telegram and the sources of Soviet conduct. As I engage with this material more and as I speak with you, I again come back to this point that I think perhaps the fundamental problem for the public is the existing framing that they have in their head about what this relationship is because no one wants to actually shift. It's a big, big shift to go to a place from thinking, this is a relationship that we can make work, we can bring them into the liberal international order to one where this, the core parts of the PLA and other parts of the CCP have never been and are not interested in peaceful coexistence with the United States.

**Demetri Kofinas:** 44:32 I think Spalding said that, "They want to dominate us." I mean, there's a lot of great stuff in the interview that you did with him. I think it's available on Real Vision-

**Kyle Bass:** 44:39 It is.

**Demetri Kofinas:** 44:40 ... where he talks about private conversations that he's had with members of the Chinese People's Liberation Army.

**Kyle Bass:** 44:46 I'll step in here and say you're talking about the schism that exists, right? There is a schism and it's between ... If you would just put it on two sheets of paper, what you see is there are two schools of thought in the U.S. today, and if you look at the Intelligence Authorization Act of 2019, which was the appropriations bill that had to be passed to fund our intelligence universe here, in the Intelligence Authorization Act of

2019, they list what they call hard target countries that we as a country are desperate to guard ourselves against and to work against, China being one of them.

- Kyle Bass:** 45:25 So, our intelligence apparatus tells you China is one of the four countries in the world that we think is an enemy of the United States. Our military says China is the number one risk to our military over the next 20 years, bar none. Nothing's even close. Our Security Council, National Security Council thinks China is our number one enemy, and we work day and night against it, and yet the other side, let's say the other faction in the United States is Wall Street, and Wall Street and its many ways ... and I mean that corporate America and Wall Street are the two biggest lobbying firms for China, right?
- Kyle Bass:** 46:06 You have the billionaire CEOs that do business in China. You have the Wall Street firms that can't wait to issue another IPO for a Chinese company. They see fees, and they see paychecks. The U.S. population has been lulled to believe that cheap t-shirts and electronics from China are a good thing and that if you want cheaper Nikes, you're going to have to have them made in China, and Nike for all stretch, all intents and purposes would love to keep making cheap stuff in China.
- Kyle Bass:** 46:37 The problem is, is that fundamental schism between what are China's intentions, how do they operate, how they interface with us, and then to your point, you said they use our greed against us, they use capitalism against us, they bribe the few, and they're really good at it. What I mean by that is they'll take some billionaires, and they'll give them special access. They'll say, "You get a casino license. You can sell cosmetics here." Now, it's not a direct bribe, but they get access, they make billions of dollars, and they become the biggest cheerleaders of China.
- Demetri Kofinas:** 47:09 They're also becoming educated.
- Kyle Bass:** 47:11 Yeah.
- Demetri Kofinas:** 47:11 On the party line.
- Kyle Bass:** 47:13 They're also then lobbying the president of United States and Congress on China's behalf, and they do it all the time, and so, that's the schism that exists. Those are the groups of people.
- Demetri Kofinas:** 47:25 So, I actually want to drill in deeper here on this point. So, one of the things that came to mind when I was preparing for this was the relationship between the schism that existed also in the United States in the interwar years leading up to and then through World War II between some of the industrialists and financiers in the country and

American foreign policy and military policy. Something similar perhaps is beginning to happen here, and then also, there's something else, which is that the battle lines, the way that we think about war in the 21st century is very different. Now, there's always been information war. Cyber war is something new, altogether new and very scary. For listeners, we've covered that in great detail, particularly during our episode with Bruce Schneier, but there's also economic warfare. That's something that, again, to bring back Robinson, he's talked about his experience in the Reagan administration and the use of economic warfare against the Soviets, and his contention is that this is exactly what the Chinese Communist Party is doing to the United States.

- Demetri Kofinas:** 48:31 How do people wrap their minds around this problem because things are shifting so much? The way that we think about war is shifting, the way that we think about our liberal capitalist system in the context of, let's say a potential threat, all of this. I mean, how do you begin to wrap your mind around this, and how do you help the people that you speak to come to this reality?
- Kyle Bass:** 48:54 You put it succinctly and properly. I think there are four kinds of war today, and we're fighting three of them with China as we speak. So, you mentioned cyber war. As you know, they attack all day every day from PLA installations. So, cyber war, we're definitely fighting with China. The narrative war is actually a big one, influence pedaling, and they are able to project their narratives to the United States through people they provide special access to or through their "news media," which is propaganda. Here, they're delivering free China Dailies out in Berkeley. They just give it away and hope people read it. So, you have cyber war, you have narrative war. Then, you have, as you're saying, economic war. An economic war can be, something I've really never talked about publicly that we'll give you here on the show, is the one thing that they're so good at is putting U.S. industry out of business. As you probably know, the generic drug business is almost 100% in China now.
- Demetri Kofinas:** 49:56 Fentanyl
- Kyle Bass:** 49:56 There are drugs that are absolutely mission critical drugs here like heparin for dialysis patients, and that's 100% made in China. They could just stop sending it to us, and we'd be in a real problem very quickly, but even worse than that is the people that are sequencing genomes here in the United States, let's say you go to 23andMe or you go to ancestry.com or you just want to pay to get your genome sequenced, there's a Chinese company called BGI that does the overwhelming majority of all the sequencing of U.S. genes. There are other Chinese companies that are all the backbones of any of the U.S. genomic sequencing companies. China has the genomic sequence of every single person that's been gene typed in the U.S., and they're developing bio

weapons that only affect Caucasians, which is crazy. The way that they did that-

- Demetri Kofinas:** 50:48 Really?
- Kyle Bass:** 50:49 This is-
- Demetri Kofinas:** 50:49 I have not heard that before.
- Kyle Bass:** 50:51 Right, so what's important to note is, how did they get there? What they do is ... So, one of the genetic scientists in the world that is a friend of mine, his name is David Mittelman, he works at a company called Othram, but for 25 years, he's been sequencing genomes. He's known in the business as one of the best in the world, and David has brand new equipment. He's been doing this his entire life, and he tells me that there is absolutely zero chance that someone can sequence a genome for less than, call it 1,400 bucks or something like ... I don't know the exact number, but the Chinese company, BGI will sequence your genome for 1,200 bucks.
- Demetri Kofinas:** 51:34 They're subsidizing it?
- Kyle Bass:** 51:34 That's how they got all the business.
- Demetri Kofinas:** 51:37 Because they want that information.
- Kyle Bass:** 51:38 They can undercut every single company in the U.S. because it's state driven. This is how they put our aluminum business out of business. This is how they went after our steel business. This is how they go after our drugs, right?
- Demetri Kofinas:** 51:50 They're going after our genomic data.
- Kyle Bass:** 51:51 They already have it. No one knows this, and we're going to write about this but-
- Demetri Kofinas:** 51:55 Wow.
- Kyle Bass:** 51:56 Go look. Choose the sites if you go look to sequence your genome, and get into the websites of these companies, and look at your options, and you'll see who's actually sequencing your genome.
- Demetri Kofinas:** 52:07 Wow. Interjection for people that are interested in learning more about this, how can they do that besides going to some of these companies?
- Kyle Bass:** 52:14 Well, I mean, we haven't written it up yet.

**Demetri Kofinas:** 52:16 [crosstalk 00:52:16] Got it. Okay. All right. So, we'll look for that.

**Kyle Bass:** 52:18 I think, and that's just one example.

**Demetri Kofinas:** 52:18 We'll look for that.

**Kyle Bass:** 52:20 You asked, how did they do it?

**Demetri Kofinas:** 52:22 Sure.

**Kyle Bass:** 52:22 They subsidize businesses they want to take over, and they'll operate at an economic loss. We won't. We can't.

**Demetri Kofinas:** 52:29 Right.

**Kyle Bass:** 52:29 Right? So, we have to stop these things from happening.

**Demetri Kofinas:** 52:33 Okay. So, Kyle, I'm going to move us into the overtime where we're going to discuss this in more detail. I want to ask you more about what you know about what's happening behind the scenes in Congress with policy, what policy might be implemented to work around this. I also want to get your thoughts on the 2020 election if you think ... because it seems to me that it's become a bipartisan issue, right? I think the one thing that a lot of people can agree on across the aisle is that the Trump administration and Donald Trump's rhetoric might've been the only way to get to this point where we start to have a national conversation about this and shift the focus.

**Kyle Bass:** 53:09 I agree with that.

**Demetri Kofinas:** 53:10 So, I want to ask you about that. I also want to talk in more depth about technology and supply chains, 5G, Huawei. For listeners, we did an episode on Huawei with James Mulvenon. I think it was episode 71 where we went to this great deal of detail, and to the extent that we'll have the time, maybe discuss some of the larger macroeconomic issues. For regular listeners, you know the drill. If you're new to the program or if you haven't subscribed yet to our audio file, Autodidact or Super Nerd tiers, you can do so at [patreon.com/hiddenforces](https://patreon.com/hiddenforces), or go into the description of this week's episode. There's a link, which will take you to the Patreon page, and you can subscribe and get access to the overtime feed, which will be a continuation of my conversation with Kyle Bass as well as the transcript and rundown to this week's episode. Kyle, stick around.

**Kyle Bass:** 54:03 Okay.

**Demetri Kofinas:**

54:06

Today's episode of Hidden Forces was recorded at Creative Media Design Studio in New York City. For more information about this week's episode or if you want easy access to related programming, visit our website at [hiddenforces.io](http://hiddenforces.io), and subscribe to our free email list. If you want access to overtime segments, episode transcripts, and show rundowns full of links and detailed information related to each and every episode, check out our premium subscription available through the Hidden Forces website or through our Patreon page at [patreon.com/hiddenforces](https://patreon.com/hiddenforces). Today's episode was produced by me and edited by Stylianos Nicolaou. For more episodes, you can check out our website at [hiddenforces.io](http://hiddenforces.io). Join the conversation at Facebook, Twitter, and Instagram @hiddenforcespod, or send me an email at [dk@hiddenforces.io](mailto:dk@hiddenforces.io). As always, thanks for listening. We'll see you next week.