

# Securing and Fuelling China's Ascent to Power

## The Geopolitics of the Chinese-Kazakh Oil Pipeline

Susann Handke

Clingendael International Energy Programme



Nederlands Instituut voor Internationale Betrekkingen  
Netherlands Institute of International Relations  
Clingendael

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**August 2006**

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Chinese-Kazakh oil pipeline is operational as of 25 May

Length: 962.2 km	Start construction: September 2004
Completion: November 2005	Costs of the project: US\$ 700 million
Annual amount of oil: 20 million tonnes	

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P.O. Box 93080, 2509 AB The Hague, The Netherlands  
Telephone: +31 70 374 66 16  
Telefax: +31 70 374 66 88  
E-mail: [ciep@clingendael.nl](mailto:ciep@clingendael.nl)

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## Abbreviations

ASEAN	–	Association of South East Asian Nations
b/d	–	barrels per day
BP	–	British Petroleum
BTC pipeline	–	Baku-Tbilisi-Çeyhan pipeline
CCP	–	Chinese Communist Party
CNOOC	–	China National Offshore Oil Corporation
CNPC	–	China National Petroleum Corporation
EIA	–	Energy Information Administration of the US Department of Energy
EU	–	European Union
GDP	–	gross domestic product
IEA	–	International Energy Agency
NATO	–	North Atlantic Treaty Organisation
OECD	–	Organisation for Economic Cooperation and Development
OPEC	–	Organisation of Petroleum Exporting Countries
PLA	–	People’s Liberation Army
PPP	–	purchasing power parity
SCO	–	Shanghai Cooperation Organisation
Sinopec	–	China National Petrochemical Corporation
UN	–	United Nations
US	–	United States of America
Xinjiang	–	Xinjiang Uygur Autonomous Region



# 1

## Introduction

In December 2005, Kazakh President Nursultan Nazarbayev celebrated his country's day of independence by opening the first stretch of the Chinese-Kazakh oil pipeline. Despite the importance of the pipeline for China's oil security, the Chinese side had "only" sent the Vice-chairman of the National Development and Reform Commission, Zhang Guobao, to co-preside over the opening ceremony. The pipeline has been high on China's economic and political agenda in recent years, and Chinese officials have made great efforts to realise this project. Even so, the Chinese government chose to keep a low profile during this opening ceremony in order to avoid offending Russian sensibilities. Obviously, the economic aspects of this pipeline project are only part of the story.

The Chinese-Kazakh pipeline is an important part of China's plan to diversify its oil supplies and its supply routes. Currently, China imports about 44% of its total annual consumption of oil, whereof about 60% originates from the Middle East.<sup>1</sup> Owing to the increased US dominance in the Persian Gulf region – especially after the outbreak of the 2003 Iraq war – and along the Southeast Asian searoutes, Chinese policymakers consider the country's growing dependence on Middle Eastern oil to be a strategic vulnerability.<sup>2</sup> As a result of its concern for the country's security of oil supply, the government decided to build a pipeline from an oil-producing region to China. In fact, the problem of securing reliable oil supplies has become a pressing issue since the country's oil demand began exceeding its own production in 1993 and, especially, since China's booming economy has caused huge increases in the demand for oil in recent years.

Central Asia<sup>3</sup> and Russia seemed the most likely to play an important role in China's strategy to reduce its dependence on oil supplies from the Persian Gulf region. In 2003 President Hu Jintao presided over the signing of both the Chinese-Kazakh and the Chinese-Russian agreements on the construction of trans-border oil pipelines. While the construction of the Russian pipeline has been severely delayed by unanticipated developments in Russia's energy sector and Japanese interference, China was able to accomplish the Kazakh pipeline project.

The first agreement between Kazakhstan and China was signed in September 1997. Subsequently, CNPC – the biggest of China's national oil companies – emerged as an important player in the competition for oil concessions in Central Asia and proposed spectacular pipeline projects for transporting oil to East China. Interestingly, both sides came together only one month after US President Bill Clinton had manifested his country's geopolitical interest in Central Asia.<sup>4</sup> Thus, despite the fact that Central Asia – with its quite substantial oil reserves – appeared to be China's most natural choice as an energy supplier,<sup>5</sup> the government's increased interest in cooperating with its western neighbours was also driven by strategic considerations regarding the geopolitical developments in that region after the demise of the Soviet Union and Russia's obvious loss of control.

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The author would like to thank Coby van der Linde and Kurt Radtke for their valuable suggestions and comments on a previous version of this paper.

<sup>1</sup> Chen Qiyu, "Fagaiwei mouhua yuanyou jinkou si da tongdao" (The National Development and Reform Commission focuses on four routes for China's oil imports), *Gongren ribao*, 14 February 2006. [http://www.grb.com.cn/news/news\\_detail.asp?news\\_id=249563&type\\_id=13](http://www.grb.com.cn/news/news_detail.asp?news_id=249563&type_id=13); Feng Yuewei, *Shiyou boyi* (The oil game), Beijing: Qiye guanli chubanshe, 2003, 308, p. 358.

<sup>2</sup> "Wo guo nengyuan anquan mianlin fuza xingshi" (The complexity of China's energy security), *Zhongguo nengyuan wang*, 30 December 2005. <http://www.china5e.com/news/zonghe/200512/200512300174.html>.

<sup>3</sup> "Central Asia" refers to Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan.

<sup>4</sup> Klare, Michael, *Blood and Oil: How America's Thirst for Petrol is Killing Us*. London: Hamish Hamilton, 2004, p. 133.

<sup>5</sup> Downs, Erica S., *China's Quest for Energy Security*. Santa Monica, CA: RAND, 2000, p. 43.

Geopolitical imagination frames world politics in a geographical context in which states vie for power outside their boundaries in order to gain control over other regions or overtake other states in their worldwide pursuit of global primacy. Subsequently, state leaders use maps in thinking about international power positions and alignments. Location constitutes the most important consideration in such power projections and entails even more specific geographical assumptions when state leaders decide where best to act and why their actions make sense.<sup>6</sup> Hence, the study of geopolitics focuses on the relationship between territory and power and investigates how states can increase their power by using geography to enhance their capabilities – for example, by securing allies and military bases close to rival powers or by controlling key natural resources.<sup>7</sup>

Central Asia has experienced numerous such activities of power projection since the end of the Cold War. In the mid-1990s, US energy companies concluded major oil deals with the governments of Azerbaijan and Kazakhstan. At the same time, the US Department of Defense established military ties with the post-Soviet states in the Caspian region. Furthermore, President Bill Clinton's designation of the region's energy resources as a matter of national security invited comparison with the 1980 Carter Doctrine. This doctrine regarded the secure flow of Persian Gulf oil as a vital interest of the US and, subsequently, demanded that access to the region's oil had to be protected by "any means necessary, including military force."<sup>8</sup> Consequently, in October 1999 the US Central Command in Tampa, Florida – originally created to implement the Carter Doctrine in the Persian Gulf – was given command authority over the Central Asian states of the Caspian Sea basin. Hence, any challenge to US interests in Central Asia would be countered with the full weight of US military power.<sup>9</sup>

The continued deployment of large contingents of US troops in the broader Central Asian region as part of the war on terrorism in Afghanistan illustrates the region's strategic importance to the United States. Officially, the US-led war was fought to destroy terrorist groups. Yet the US claimed victory when it had accomplished two other, very different, policy objectives, without having justified the original goal of the war with either of them. First, its broader power-projection strategy was realised by establishing US military bases close to potential rivals – i.e., China, Russia, and Iran. Second, the US became a major player in Central Asian affairs, enabling the US government to help secure US-based companies' access to the energy riches of the Caspian Sea region. Indeed, with the lingering political and economic uncertainty in Iraq, the US will badly need Caspian oil, in particular supplies from Kazakhstan, in the coming years.<sup>10</sup>

China, too, has made a great effort to increase its economic and political influence in Central Asia in recent years, mainly because of the leadership's concerns about the stability in and along the borders of the strategically important Xinjiang Uygur Autonomous Region (Xinjiang). Generally, many people are discontented due to the social inequality caused by China's rapid economic transformation and the tremendous gap between the booming eastern provinces and the poor landlocked western regions. Additionally, dissatisfaction with Beijing's policies often triggers ethnic tensions in China's minority regions. The government fears that large-scale social unrest could easily spread across the country and endanger China's development. Due to Xinjiang's strategic location and the latent discontent of its multi-ethnic populace, the economic development of Xinjiang has become one of the key issues of China's overall economic modernisation. In fact, Beijing hopes that Xinjiang's increased economic integration with its Central Asian neighbours, including major investments in energy-related projects, can boost Xinjiang's economy and ease social inequality.

Many studies have focussed on Central Asia's recent geopolitical developments. However, little attention has been paid to Chinese interests and activities in the region. Due to its close geographical proximity to Xinjiang, stability and economic prosperity in Central Asia are vital to China's internal

<sup>6</sup> Agnew, John, *Geopolitics: Re-visioning World Politics*. London: Routledge, 1998, p. 1.

<sup>7</sup> Goldstein, Joshua S., *International Relations*. New York: Longman, 2003, pp.77-81; Dekmejian, R. Hrair, and Hovann H. Simonian, *Troubled Waters: The Geopolitics of the Caspian Region*. London: I. B. Tauris, 2003, p. 5.

<sup>8</sup> Klare, Michael, 2004, 133; US President Jimmy Carter in his State of the Union address on 23 January 1980, quoted in Klare, Michael, 2004, p. 45.

<sup>9</sup> *Ibid.*, pp. 132 and 152.

<sup>10</sup> Yermukanov, Marat, "Astana's Oil Strategy Reveals Preference for United States," *Eurasia Daily Monitor*, 28 September 2005. [http://jamestown.org/edm/article.php?article\\_id=2370277](http://jamestown.org/edm/article.php?article_id=2370277).

economic transformation, which is considered the basis for the country's ascent to the ranks of great powers. Increasingly strong Chinese-Kazakh ties can be seen as an example of China's strategy to ward off the consequences of growing US influence in its periphery in order to avert developments that could endanger its economic progress and, subsequently, head off its rise to power. It is therefore important to look at China's involvement in the region from an economic as well as a geopolitical perspective.

Consequently, the main purpose of this paper is to use the Chinese-Kazakh oil pipeline as a case study and discuss the progress of this project, together with China's policy towards its periphery, as part of its grand strategy to ascend to ranks of great powers. Accordingly, the paper not only assesses the geopolitics of Central Asia, but also China's oil strategy and the Western Development Programme as the central government's effort to stabilise the country's economic development. The paper argues that China's involvement in Central Asia is a result of both China's energy needs and the threats to its oil security as well as the government's concern over the territorial integrity and social stability of the country. Hence, Chinese efforts to establish closer ties with its Central Asian neighbours should not be seen as part of a broader strategy to challenge global US power.

Previous studies have perceptively held that the current developments in Central Asia are the result of the activities of states as well as non-state actors.<sup>11</sup> Indeed, the multiplicity of forces operating in the broader Central Asian region requires that the framework of analysis include theories of geopolitics, balance of power, neorealism, interdependence, and culture conflict.<sup>12</sup> This study adopts the geopolitical approach and draws from the theories of balance of power as well as realism that are implicit in geopolitical thought. The realist school views international relations in terms of power. States whose behaviour is based on the rational pursuit of self-interest are the most important actors in realist thinking.<sup>13</sup> As will be discussed below, energy-related issues are not the only reason for China to seek more cooperation with its western neighbours. Therefore, the geopolitical approach is most suitable to analyse China's policy towards Central Asia.

The structure of this study is as follows. The second chapter provides an overview of China's grand strategy and the country's policy towards its periphery. The third chapter summarises the main points of China's strategy for securing its oil supply. Chapter four describes the progress of China's large undertaking to build an oil pipeline from western Kazakhstan to Xinjiang, while Chapter five discusses the importance of the pipeline both for the development of China's western regions and for China's relations with Kazakhstan. The sixth chapter shows how China is fostering its interests in Central Asia, focusing on the Sino-Russian strategic cooperative partnership, China's contribution to the establishment and institutionalisation of the Shanghai Cooperation Organisation, and China's military posture in the region. Chapter seven provides an evaluation of China's economic role in the broader Central Asian region in the near future. The last subsection of that chapter discusses three scenarios that could strongly impact the geopolitics of Central Asia and China's interests in the region. Conclusions are formulated in Chapter eight.

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<sup>11</sup> See Amineh, Mehdi Parvizi, *Globalisation, Geopolitics and Energy Security in Central Eurasia and the Caspian Region*. The Hague: Clingendael Energy Publication, 2003; and Dekmejian, R. Hrair, and Hovann H. Simonian, *Troubled Waters: The Geopolitics of the Caspian Region*. London: I. B. Tauris, 2003.

<sup>12</sup> Dekmejian, R. Hrair, and Hovann H. Simonian, 2003, p. 4.

<sup>13</sup> Goldstein, Joshua S., 2003, p. 73.



# 2

## The Rise of China and Its Security Environment

This chapter summarises China's grand strategy and provides an overview of the country's strategic adjustment to the post-Cold War unipolar world. The final section describes China's position in Asia and its regional policy.

### 2.1. China's Grand Strategy

#### *A Great Power in the Making?*

Chinese analysts are convinced that the first two decades of the 21st century will constitute a critical juncture for the Chinese people in accomplishing their country's internal revival and creating lasting prosperity, while simultaneously pursuing China's rise on the international stage.<sup>14</sup> Consequently, the country's leaders have deemed the next 20 years as a period of strategic opportunity for China to ascend to the ranks of great powers. Already in 1975, Deng Xiaoping (1904-97) declared that China must not remain at the stage of a third-world country, because it had the potential to become equal to the US within a few decades. Deng's decision to open up China's economy laid the foundation for China's economic and political rise. Yet his legacy also includes the insistence of China's independent development, the rejection of participating in alliances with other countries, and the focus on internal stability and rapid economic growth.<sup>15</sup>

Until now, China's grand strategy for ascending to the ranks of global great powers has never explicitly been presented by its leaders in any comprehensive manner. Still, from various public statements it can be concluded that China's grand strategy is geared toward the attainment of three interrelated objectives – i.e., the preservation of domestic order and well-being in the face of different forms of social strife, the defence against persistent external threats to national sovereignty and territory, and the attainment and maintenance of geopolitical influence as a major state.<sup>16</sup>

Ye Zicheng describes the term “grand strategy” as an all-embracing strategy of the state – a large strategic system that comprises the long-term goals of a state along with the various strategies for achieving it. A state's grand strategy thus consists of strategies that concern the country's foreign policy, diplomacy and military, as well as its geopolitical strategy and the strategies for the country's internal development – i.e., its political, economic, environmental, and cultural development strategies. As such, a grand strategy is the basis for all state policies.<sup>17</sup> Goldstein states that a grand strategy refers to “the central logic that informs and links various foreign policies, the regime's vision about how it can most sensibly serve the nation's interests (goals) in light of the country's capabilities (means) and the international constraints it faces (the context of interdependent choice).”<sup>18</sup>

According to Zhang Yunling and Tang Shiping, China's grand strategy must serve the central purpose of the country's development. Thus, this strategy aims at shaping and maintaining the security,

<sup>14</sup> Xu Jian, *Guoji huanjing yu Zhongguo de zhanlüe jiyuqi* (The international system and the period of China's strategic opportunity), Beijing: Renmin chubanshe, 2004, p. 364.

<sup>15</sup> Ye Zicheng, *Zhongguo da zhanlüe: Zhongguo chengwei shijie daguo de zhuyao wenti ji zhanlüe xuanze* (China's grand strategy: China's most important problems and strategic choices as a great nation). Beijing: Zhongguo shehui kexue chubanshe, 2003, pp. 34-5.

<sup>16</sup> Swaine, Micheal D., and Tellis, Ashley J., *Interpreting China's Grand Strategy: Past, Present, and Future*. Santa Monica, CA: 2000, pp. ix-x.

<sup>17</sup> Ye Zicheng, 2003, p. 1-2.

<sup>18</sup> Goldstein, Avery, *Rising to the Challenge: China's Grand Strategy and International Security*. Stanford, CA: Stanford University Press, 2005, p. 19.

economic and political environments conducive to China's focus on its economic, social, and political development. Four core concepts underpin China's current grand strategy. First, Sun Yat-sen (1866-1925) and the Chinese leaders that succeeded him have always believed that China should belong to the "club of great powers." Even though the country's position declined in the 19th and 20th centuries, their goal has been to make China a great power again. Second, Deng Xiaoping stated that China needs a stable and peaceful international environment for its modernisation. Moreover, he realised that the PRC's security conundrum in the 1960s and 1970s had not been the result of external forces alone, but rather the product of China's behaviour and interaction with the outside world. Deng's acknowledgement of the existence and origins of this security dilemma was a momentous shift and has exerted a profound influence on China's strategic thinking and behaviour ever since. Third, Deng Xiaoping consistently stressed the importance of self-restraint and warned his successors against actively seeking leadership in global or regional affairs and taking on responsibilities that China cannot bear. Finally, particularly since the 1997 Asian financial crisis, Chinese leaders have been aware of the fact that the country's economic welfare and its security depend heavily upon its interaction with other countries. Consequently, China must participate in world affairs more actively, which requires that China shoulder certain burdens and responsibilities. Hence, the PRC needs to act as a responsible great power on the international stage.<sup>19</sup>

A global great power is defined as "a state that easily ranks among the top five in the primary global structures – economic, military, educational, and normative – and that enjoys relatively low sensitivity, vulnerability, and security interdependence because of massive resource and skill differentials and relative economic self-sufficiency."<sup>20</sup> In general, great powers have the world's most capable military forces and the strongest economies, which rest on some combination of large populations, plentiful natural resources, advanced technology and educated labour forces.<sup>21</sup> Thus, a great power is "a strong state with the ability to mobilise the country's human and material resources in the service of its worldview and policy objectives."<sup>22</sup>

Applying these criteria and judging from the country's behaviour on the international stage, China must be regarded as a regional power that pursues a rather cautious approach to its global interests. Yet, China can be considered a rising great power by conventional measurements of the rise and fall of great powers in terms of shifts in the international military and economic power balances.<sup>23</sup> Actually, Chinese analysts are convinced that China's rise has already become inevitable – a development with which policymakers must now reckon.<sup>24</sup>

The most important aspect of China's rise, however, is the question of how its ascent to power will unfold. Although the rise of China as the predominant phenomenon of the 21st century is also widely acknowledged in international foreign policymaking and analyst circles, there is hardly any agreement as to how China will rise to the ranks of great powers and how China might be accommodated.<sup>25</sup> Nevertheless, Chinese elites believe that only an "intrasystem rise" can be a peaceful one.<sup>26</sup> Undoubtedly, the current leadership adheres to Deng Xiaoping's doctrine of "peaceful development" and has even substituted this slogan for the much-discussed term "peaceful rise."<sup>27</sup> The ultimate direction of China's further transition will be determined by both internal developments and several external factors, such as the government's ability to ensure stable economic growth, and the maintenance of a peaceful international environment.

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<sup>19</sup> Zhang Yunling, and Tang Shiping, "China's Regional Strategy," in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, pp. 48-9.

<sup>20</sup> Kim, Samuel S., "China as A Great Power," in *The China Reader: The Reform Era*, ed. Orville Schell and David Shambaugh, New York: Vintage, 1999, p. 448.

<sup>21</sup> Goldstein, Joshua S., 2003, p. 95.

<sup>22</sup> Kim, Samuel S., 1999, p. 448.

<sup>23</sup> *Ibid.*, p. 457.

<sup>24</sup> Xu Jian, 2004, p. 364.

<sup>25</sup> Xiang Lanxin, "China's Eurasian Experiment," *Survival* 46, no. 2 (2004): 114; Xu Jian, 2004, p. 364.

<sup>26</sup> Zhang Yunliang, and Tang Shiping, 2005, p. 53.

<sup>27</sup> "“Zhongguo de heping fazhan daolu’ baipi shu (quanwen)”(White book on China's way of the peaceful development (full text)), *Renmin wang*, 22 December 2006, <http://politics.people.com.cn/GB/1026/3965180.html>.

*Adjusting to a Unipolar World*

In the first decades of the 21st century, China's relations with the US as the only remaining superpower may hold the key to maintaining peace. In general, Chinese analysts still expect that the current international system, particularly the relations between the great powers, will prevail for the time being. Thus, the present international environment opens the door for China to become a global great power.<sup>28</sup> Tang Shiping identifies two preconditions crucial to the achievement of this great ambition: China's maintenance of an effective strategic nuclear threat and the striving for a multipolar international system.<sup>29</sup> The most critical external threats to China's rise, however, are the unsolved Taiwan issue and China's dependence on foreign energy supplies.<sup>30</sup> The country's dependence on oil imports could indeed endanger further steady economic development which, of course, is the most important precondition for China's ascent.<sup>31</sup> Yet both external threats are also directly linked to the dynamics of the Sino-American relationship.

After the end of the Cold War, optimism about an emerging "new world order" prevailed, and the experience of almost two decades of basically friendly ties between the US and China seemed to bode well for the immediate future. Yet the solid military-strategic foundation of self-interest that had encouraged Sino-American cooperation crumbled after the collapse of the Soviet Union in the early 1990s. The remaining incentives for cooperation were mutual economic interests and shared perspectives on a few regional and international security concerns. However, these issues were not in themselves sufficiently compelling to either offset old differences or counterbalance the new conflicts that emerged during the 1990s as a result of both China's growing capabilities and the transformed international system.<sup>32</sup> Additionally, the demise of the Soviet Union and the developments in its former satellite states induced new fears among the leaders in Beijing. Especially after the US supported sanctions against China in the wake of the 1989 Tiananmen incident, the Chinese government no longer saw the US as a valuable military counterweight to a powerful and threatening superpower neighbour, but once again as the leading advocate of ending communist rule in China in the same way as it had been ended elsewhere.<sup>33</sup>

Consequently, lingering disagreements about political ideology and the unresolved Taiwan issue were important triggers for the deterioration of Sino-American relations after the Cold War. In fact, attempts by US officials to pressure China to make domestic political changes were perceived as threats, because China's leadership saw them as a challenge to the internal stability necessary for the pursuit of the country's policies of economic reform and modernisation. Moreover, increasing US involvement with the Taiwan issue was viewed as part of a US-led effort to endanger China's ability to protect its vital national interest. Accordingly, the emerging dynamic in the Sino-American relationship began to reflect the logic of what international relations scholars refer to as "the security dilemma."<sup>34</sup> While US policymakers began to worry that a rising China might challenge the existing security order in Asia Pacific that rested on US preponderance and leadership, China's leaders feared that the US was determined to prevent China from legitimately exercising international influence commensurate with its growing economic power.<sup>35</sup>

In early 2001, the George W. Bush Administration initiated a sweeping strategic review. This review included a shift of strategic-military attention from Europe toward Asia – the most extensive realignment of US power in half a century.<sup>36</sup> Although this reorientation was not narrowly focused on China, it had a direct bearing on the Administration's China policy. Actually, at the outset of the 21st century, the US and China seemed on the brink of a new Cold War. After 11 September 2001,

<sup>28</sup> Xu Jian, 2004, pp. 364-5.

<sup>29</sup> Tang Shiping, "Lixiang anquan huanjing yu xin shiji Zhongguo da zhanlüe" (The ideal environment and China's grand strategy for the new century), *Zhanlüe yu guanli*, no. 6 (2000), 30 June 2000. <http://www.future-china.org/fcn/ideas/fcs20000630.htm>.

<sup>30</sup> Xu Jian, 2004, p. 209.

<sup>31</sup> *Ibid.*, 222; Tang Shiping, "Lixiang anquan huanjing yu xin shiji Zhongguo da zhanlüe," 2000.

<sup>32</sup> Goldstein, Avery, 2005, p. 2.

<sup>33</sup> *Ibid.*, p. 3.

<sup>34</sup> *Ibid.*, p. 14.

<sup>35</sup> *Ibid.*, p. 8.

<sup>36</sup> Hoge, James F., "A Global Power Shift in the Making: Is the United States Ready?," *Foreign Affairs* 83, no. 4 (2004), p. 5.

however, the rhetoric of cooperation replaced that of conflict. Still, both sides clearly remain vigilant. Potentially dangerous disagreements are still unresolved, while mutual suspicions about future capabilities and intentions endure.<sup>37</sup>

At the moment, China is neither capable nor willing to enter into conflict with the US on issues that could fundamentally worsen Sino-US relations. As a result, the grand strategy that guides China's international behaviour aims to engineer the country's rise to great-power status within the constraints of a unipolar international system that is dominated by the United States. Thus, China's leaders are trying "to increase the country's international clout without triggering a counterbalancing reaction."<sup>38</sup>

## 2.2. Strategic Choices after the End of the Cold War

### *China's Foreign Policy as an Ascending Great Power*

Realist international relation scholars, especially those aligned with neoconservatives in the US, have warned of China being an assertive and expansionist great power that will be able to challenge US predominance in the post-Cold War world and will further its interests by launching aggressive warfare against its neighbours. In contrast, the liberal argument assumes that China is a conservative power that will maintain the status quo in the foreseeable future and will become more open and democratic as economic reform proceeds. Zhao Suisheng, however, stresses that neither of these international relation theories alone can provide a full insight into how China's changing status in the international system will influence international stability and peace. So far, China's leaders have developed a pragmatic strategy resulting in "a firmly goal-fulfilling and national-interest-driven strategic behaviour conditioned substantially by China's historical experiences and geostrategic environment."<sup>39</sup>

During the first decade of economic reform, China's leaders continued the pragmatic foreign policy approach that had been developed by Mao Zedong (1893-1976) in the early 1970s and tried to manoeuvre between the two superpowers, eagerly promoting a world of multipolarity<sup>40</sup> consisting of sovereign nations that mutually respect the principle of non-interference.<sup>41</sup> In 1996, after several years of ad hoc attempts to deal with the fact that the US was the only remaining superpower and other post-Cold War challenges, China's leadership formulated a new foreign policy line. This new policy was designed to engineer China's rise to the status of a genuine great power that would be able to shape – rather than simply respond to – the international environment.<sup>42</sup>

During the celebration of the 80th anniversary of the Chinese Communist Party (CCP) in July 2001, President Jiang Zemin provided an ideological backing for the new foreign policy approach by endorsing the view that China should abandon its victim mentality<sup>43</sup> that emphasised the 150 years of shame and humiliation the Chinese people had been experiencing, and instead adopt a great-power mentality.<sup>44</sup>

<sup>37</sup> Goldstein, Avery, 2005, pp. 1, 8 and 9.

<sup>38</sup> *Ibid.*, p. 12.

<sup>39</sup> Zhao Suisheng, "Chinese Foreign Policy: Pragmatism and Strategic Behavior," in *Chinese Foreign Policy: Pragmatism and Strategic Behavior*, ed. Zhao Suisheng, Armonk, NY: M. E. Sharpe, 2004, p. 4.

<sup>40</sup> Chinese analysts often use the term "multipolarity" in order to describe the overall trend in international relations as a movement away from the bipolarity of the Cold War era. Yet, this academic discourse plays an ambiguous role in China's foreign policy process and should not be misunderstood as an indicator of China's leaders' revisionist intentions. Moreover, despite all its support for multipolarity, China's government is not doing a great deal to encourage its practical emergence. See Johnston, Alastair Iain, "Is China a Status Quo Power?," *International Security* 27, no. 4 (Spring 2003), pp. 30-8.

<sup>41</sup> Zhao Suisheng, 2004, p. 5.

<sup>42</sup> Goldstein, Avery, "The Diplomatic Face of China's Grand Strategy: A Rising Power's Emerging Choice," *The China Quarterly*, no. 168 (December 2001): pp. 835-6.

<sup>43</sup> A deep-seated victim mentality among both the elite and the populace first emerged in the imperial period as a result of earlier periods of conquest by nomadic invaders such as the Mongols (Yuan dynasty, 1271-1368) and the Manchus (Qing dynasty, 1644-1911). The victim mentality came to full prominence in the modern era due to China's humiliation and subjugation by foreign imperialist states after the Opium War (1839-42). Swaine, Michael D., and Ashley J. Tellis, 2000, p. 73.

<sup>44</sup> Medeiros, Evan S., and M. Taylor Fravel, "China's New Diplomacy," *Foreign Affairs* 82, no. 6 (2003): p. 32.

In general, the recent priority for China's foreign policy strategists has been to establish peaceful working relationships with as many countries as possible, enabling the Chinese leadership to direct its efforts to the country's economic development.<sup>45</sup> Indeed, in regions where geopolitical or security concerns are of primary importance, the Chinese use trade and investment as instruments for fostering new relationships.<sup>46</sup> Further, China has been posting many of its most seasoned diplomats to ambassadorships in key regional capitals, where they become actively involved in local communities, while lower-ranking diplomats attend academic and policy-related seminars, forge business ties, cultivate good relationships with local overseas Chinese communities and try to create good will.<sup>47</sup>

China's foreign policy aims at maintaining the international conditions that will make it feasible for the leadership to focus on domestic issues. The government needs this breathing space to be able to increase the country's economic and military capabilities. Consequently, since 1996, China has been making efforts to reassure potential adversaries, which had grown ever more worried about the country's rise, to reduce the likelihood that the US, or others with its backing, would exploit their current material advantage to thwart China's ascent and frustrate its international aspirations. Moreover, in recent years, China has placed more emphasis on great-power relations with Russia, the EU, and the US – now a top foreign policy priority – while trying to encourage those major powers to view China as an indispensable, or at least attractive, partner.<sup>48</sup>

Chinese leaders have avoided confrontations with the US and tried to defuse tensions with bordering countries. Zhao Suisheng concludes that China's resulting pragmatic strategic behaviour is "flexible in tactics, subtle in strategy, and avoids appearing confrontational," but China is uncompromising with foreign demands that concern its vital interests or involve historical sensitivities.<sup>49</sup>

### *The New Security Concept*

In general, the new security concept mainly draws from principles that have been pillars of China's foreign policy since the 1950s, in particular the so-called 'Five Principles of Peaceful Coexistence.' These principles entail mutual respect for the sovereignty and territorial integrity of other countries, non-interference in the internal affairs of other countries, non-aggression, bilateral relations based on equality and mutual benefits, and peaceful coexistence. The core of the new security concept is mutual trust, mutual benefit, equality and cooperation. These values are viewed as the basis for a fair and reasonable new international order. The vigorous promotion of these principles does not reflect China's strength to establish such a new international order, but is rather an indication of its self-perceived weakness and its frustration with an increasingly troubled global and regional security environment.<sup>50</sup>

After the end of the Cold War, the threat of a major war between two or more great powers was reduced considerably. As a result, during the 1990s, Chinese leaders regarded the country's security environment as the most favourable since the establishment of the PRC. Chinese analysts still consider China's security environment to be better than during the Cold War. However, Yan Xuetong argues that nowadays the likelihood to be drawn into a war is greater than during the 1990s.<sup>51</sup> Recent Chinese defence White Papers conclude that tendencies of hegemonism and unilateralism have gained new ground, as struggles for strategic points, resources and dominance crop up from time to time.

<sup>45</sup> Andrews-Speed, Philip, and Sergei Vinogradov, "China's Involvement in Central Asian Petroleum: Convergent or Divergent Interest?," *Asian Survey* 40, no. 2 (2000), p. 378.

<sup>46</sup> *Ibid.*, p. 379.

<sup>47</sup> Shambaugh, David, "China Engage Asia: Reshaping the Regional Order." *International Security* 29, no. 3 (Winter 2004/5), p. 78.

<sup>48</sup> Goldstein, Avery, 2001, 836; Medeiros, Evan S., and Taylor M. Fravel, 2003, p. 32.

<sup>49</sup> Zhao Suisheng, 2004, p. 5.

<sup>50</sup> Gill, Bates, "China's Evolving Regional Security Strategy," in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, pp. 248-9.

<sup>51</sup> The cross-Taiwan Strait relations became more strained after Taiwan's President Li Teng-hui had brought forward his "two countries" concept in 1999, and the pro-independence candidate Chen Shui-bian won the presidential elections in 2000. Yan Xuetong, "Quanjia hua yu Zhongguo de anquan huanjing" (The globalisation and China's security environment), 12 December 2004. <http://rwxy.tsinghua.edu.cn/xi-suo/institute/ky/yxt/wz/4.htm>.

Subsequently, the role of military power in safeguarding national security is assuming greater prominence.<sup>52</sup>

By the late 1990s, the government had reached agreements or was engaged in talks about the delimitation of China's borders with its western and southern neighbours as well as with Russia. This improved security along these borders. However, since 1989, China and the US have increasingly become military opponents. Moreover, China's security is also endangered by so-called non-traditional security threats, such as drug trafficking, terrorism, risks linked to the increasing dependence on information technologies, and China's growing economic interaction with other countries. Hence, China faces the risk of both a regional war and the danger of non-traditional security threats that could cause damage comparable to a conventional war. Finally, the growth of China's military capabilities lags behind the country's economic development. As a result, China's navy – the weakest part of the country's military – is not able to secure vital sea-lanes, a reality that could severely endanger its economic development.<sup>53</sup>

In the 1980s and 1990s, the military modernisation slowed down to focus on economic development. At that time, the Chinese leadership pursued a policy of “economic strength and military weakness.” Yet Yan Xuetong stresses that a country must be able to rely on different capabilities in order to deal with the various problems it might face.<sup>54</sup> At the moment, China's military capabilities do not allow the PLA to engage in a military conflict with the US, which is the only regional power that could exert any considerable pressure on the country. This vulnerability can only be overcome by accelerating the ongoing military modernisation.<sup>55</sup>

The US is expected to remain at the centre of China's strategic calculations. The future of China's regional strategy will be influenced by US long-term strategic intentions toward China and how the US views the PRC's interaction with regional countries.<sup>56</sup> For the short term, China views its neighbours as a shield from pressure exerted by external great powers. Therefore, maintaining a cordial relationship with regional states is the key to averting the emergence of a containment coalition led by any combination of external powers.<sup>57</sup> Hence, to cope with both traditional as well as non-traditional threats to its security, China's new security concept embraces security-cooperation instruments such as consultations and confidence-building measures rather than multilateral security institutions.<sup>58</sup>

### 2.3. Engaging with the Periphery

#### *Asia and the Rising China*

In the first three decades after its foundation in 1949, the PRC behaved differently on the regional stage. Sometimes it was forced to pursue policies of autarchy, or alignments with external powers – the US and the Soviet Union – were necessary to augment its security. At other times, it exerted a negative influence in the region as a result of its own domestic dislocations or attempts to subvert neighbouring non-communist governments.<sup>59</sup> In fact, when the PRC behaved in these ways – as a non-status quo power – it only became more marginalised from the principal actors and central dynamics of the region. Deng Xiaoping clearly recognised this and made it one of his highest priorities to try and

<sup>52</sup> Gill, Bates, 2005, p. 252.

<sup>53</sup> Yan Xuetong, “You heping bu yiding you anquan” (Peace does not necessarily mean security), *Huanqiu shibao*, 13 January 2006. <http://rwxy.tsinghua.edu.cn/xi-suo/institute/ky/yxt/wz/43.htm>.

<sup>54</sup> Yan Xuetong, “Qiangda junshi li cai neng baozheng heping jueqi” (Strengthening military capabilities is a precondition for a peaceful rise), *Huanqiu*, 1 September 2005. <http://rwxy.tsinghua.edu.cn/xi-suo/institute/ky/yxt/wz/02.htm>.

<sup>55</sup> Yan Xuetong, “Quanqiu hua yu Zhongguo de anquan huanjing,” 2004.

<sup>56</sup> Zhang Yunling, and Tang Shiping, 2005, p. 56.

<sup>57</sup> *Ibid.*, p. 51.

<sup>58</sup> *Ibid.*

<sup>59</sup> Shambaugh, David, “Introduction: The Rise of China and Asia's New Dynamics,” in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, p. 1.

reintegrate China into the Asian region. After the first steps to ameliorate long-standing tensions and build new ties under Deng Xiaoping, even more substantial progress was made during the 1990s.<sup>60</sup>

Undoubtedly, China is again part of the mainstream and has been repositioning itself both as a central actor in the region and as a responsible power seeking to enhance the stability and security of the area. Actually, until the late 1990s, China's regional posture had remained somewhat aloof and less than fully engaged. However, since 1997-8 the PRC has demonstrated a new confidence in its external posture, and its ties with neighbours and regional organisations have exhibited a number of new features.<sup>61</sup> Additionally, due to China's increasing importance to the region, countries all around its periphery are adjusting their relations with Beijing, as well as with each other. Consequently, a new regional order is taking shape, creating an extensive web of mutual interdependence among states and non-state actors. Although China increasingly finds itself at the centre of the web, it shares the regional stage with the US, Japan, ASEAN, and India.<sup>62</sup>

Economically, however, China – not Japan or the United States – is already at the hub. Although China is the most obvious power on the rise, India and other Asian states also boast growth rates that could outstrip those of major Western countries for decades to come. Still, China has become the engine driving the recovery of other Asian economies from the setbacks of the 1990s. The country's economic influence among the member of ASEAN is growing steadily, and thanks to China, Japan is finally emerging from a decade of economic malaise. Indeed, China is now such a large player in the regional as well as the global economy that its health is inextricably linked to that of the system at large.<sup>63</sup> Furthermore, as a result of this growing interdependence, China is likely to become increasingly effective in pursuing its national goals and strategies both in Asia and among larger external powers with interests in the region, such as the United States.<sup>64</sup>

#### *China's Policy Toward Its Periphery*

After the foundation of the People's Republic of China in 1949, the Chinese leadership did not pursue a consistent regional policy. Moreover, tensions with many of its neighbouring countries became an important source of threat to the country's national security. Subsequently, China constantly had to be alert to the possibility of invasions by hostile powers via its neighbouring countries. China even fought several wars with neighbours or with external powers in neighbouring countries in order to diffuse the threat.<sup>65</sup>

As an immediate threat of invasion had disappeared and dynamic economies emerged along its eastern coast in the 1980s, China's security policy shifted from simply ensuring survival in a hostile world toward preventing instabilities along its borders that could possibly undermine the country's prospects for continued economic development.<sup>66</sup>

In the 1990s, the Chinese leadership began to develop a new periphery policy that would help China to achieve the goal of creating a regional environment conducive to its economic modernisation and national security.<sup>67</sup> Consequently, China has pursued a fairly consistent and coherent policy towards its periphery in the past decade, which focuses on two interrelated efforts. Neighbouring countries must be reassured that China will act as a responsible and cooperative player. At the same time, the Chinese leadership cultivates partnerships with the world's major powers in order to reduce the risk that other countries will unite to prevent China's rise to the ranks of great powers.<sup>68</sup> Hence, China's regional strategy can be viewed as the core of its grand strategy. Both the ideas and practices of its

<sup>60</sup> Ibid., p. 1.

<sup>61</sup> Ibid., p. 2.

<sup>62</sup> Shambaugh, David, "Return to the Middle Kingdom?: China and Asia in the Early Twenty-First Century," in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, p. 23.

<sup>63</sup> Hoge, James F., 2004, pp. 2-3.

<sup>64</sup> Gill, Bates, 2005, p. 262.

<sup>65</sup> Zhao Suisheng, "The Making of China's Periphery Policy," in *Chinese Foreign Policy: Pragmatism and Strategic Behavior*, ed. Zhao Suisheng, Armonk, NY: M. E. Sharpe, 2004, p. 256.

<sup>66</sup> Burles, Mark, *Chinese Policy toward Russia and the Central Asian Republics*. Santa Monica, CA: RAND, 1999, p. 8.

<sup>67</sup> Zhao Suisheng, "The Making of China's Periphery Policy," 2004, p. 257.

<sup>68</sup> Goldstein, Avery, 2001, pp. 840-2.

regional behaviour reflect the imperatives of its grand strategy, for Asia is the only region in which all aspects of China's national interest – security, economic and political cooperation – are present.<sup>69</sup>

In view of that, China's policy toward its neighbours has two security goals. First, China seeks to secure its boundaries by settling border disputes through consultations and negotiations. Second, the Chinese leadership tries to prevent alliances of its neighbours with outside powers that are hostile to China. This goal has involved the development of good relations with Asian countries and the search for common ground with its neighbours in resisting pressures from Western powers on issues such as market penetration and human rights issues.<sup>70</sup>

The Chinese government realises that its neighbours already see the country as a regional economic power and expect that its weight will continue to grow. Thus, the challenge now confronting China is how to make China's economic growth an opportunity for the region rather than a threat. By making China a locomotive for regional growth, states should be prevented from coalescing to thwart China's economic growth.<sup>71</sup>

David Shambaugh identifies four overarching characteristics of China's recent interaction with its periphery. First, China makes a concerted effort to build strategic partnerships and work with regional organisations. Second, the government tries hard to deepen bilateral political and economic interaction. Third, Chinese policymakers go to great lengths to expand economic ties. Finally, in recent years China has become engaged in various forms of bilateral and multilateral cooperation in order to remove distrust and anxiety in the security sphere.<sup>72</sup>

China's emerging regional security posture can be divided into three categories: unilateral, bilateral, and multilateral activities. China's military modernisation programme is undertaken unilaterally. The programme is mainly driven by two concerns. First, China wants to build and deploy a comprehensively modern military commensurate with the country's status as a major power. Second, the modernisation focuses on various Taiwan military scenarios. On the one hand, the People's Liberation Army (PLA) has not yet developed – or even placed a priority on developing – a power-projection capability. On the other hand, China possesses a navy and air force that numerically exceeds that of any other country in the region, and its entire force structure is becoming more modern and professional by the day.<sup>73</sup>

In general, China has been able to offset the impact of these unilateral moves with a series of bilateral and multilateral confidence-building measures. Indeed, with more than 15 countries bordering China, an aggressive posture is simply not in the government's interest, no matter how powerful China becomes. Aggressive behaviour would simply lead to a counterbalancing alliance of China's neighbours and a distant power, most likely the United States.<sup>74</sup> Accordingly, the Chinese government has established bilateral security dialogues with some neighbouring countries and has stepped up official military-to-military exchanges, which include bilateral military exercises with other nations, such as Kazakhstan, Pakistan, India and Russia.<sup>75</sup> Moreover, in 2003, China formally acceded to ASEAN's Treaty of Amity and Cooperation, committing China to the core elements of ASEAN's 1967 Charter. By signing the Declaration of Conduct on the South China Sea, China has accepted to adhere to non-aggression, non-interference, and a variety of other conflict resolution mechanisms and is also increasingly willing to participate in the ASEAN Regional Forum, which can be viewed as a potential basis for establishing a regional cooperative security community.<sup>76</sup>

Beijing has committed itself to some fundamental compromises that enmesh China in multilateral frameworks and regional interdependencies, such as the Shanghai Cooperation Organisation and

<sup>69</sup> Zhang, Yunling, and Tang Shiping, 2005, p. 51.

<sup>70</sup> Zhao Suisheng, "The Making of China's Periphery Policy," 2004, pp. 258-9.

<sup>71</sup> Zhang Yunling, and Tang Shiping, 2005, p. 51.

<sup>72</sup> Shambaugh, David, "Return to the Middle Kingdom?: China and Asia in the Early Twenty-First Century," 2005, p. 29.

<sup>73</sup> *Ibid.*, pp. 38-9.

<sup>74</sup> Zhang Yunliang, and Tang Shiping, 2005, p. 49.

<sup>75</sup> Shambaugh, David, "Return to the Middle Kingdom?," 2005, p. 40.

<sup>76</sup> *Ibid.*

closer ties with ASEAN. Yet the Southeast Asian and Central Asian states, for their part, have not entered into these arrangements with their eyes closed. As they have a long historical experience of dealing with a more powerful imperial China, these countries are well equipped for the emergence of China as a superpower in the 21st century.<sup>77</sup>

China has already largely completed its painful search for a national identity. Nowadays it no longer sees itself as a country that faces imminent external danger or is on the verge of internal implosion, but as one that has resources for managing its economic transformation and a growing ability to shape its environment. Thus, the PRC is becoming more confident of its relationships and its position in the region. As long as China's optimistic assessment of its external environment and its self-identity as a responsible great power continue to hold, the government will be able to pursue its current regional policy.<sup>78</sup>

In sum, a peaceful international environment is a precondition for China's ascent to the ranks of global great powers. After the end of the Cold War, Chinese leaders had to adjust their policies to an emerging unipolar international order and redefine their country's relations with the US. In the mid-1990s, the leadership developed a new foreign policy approach. China's main efforts to shape an environment conducive to its economic development are focussed on its periphery. As a result of China's economic rise and its successful regional policy, Asian countries are increasingly willing to take China's interests into account.

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<sup>77</sup> Vatikiotis, Michael R. J., "Catching the the Dragon's Tail: China and Southeast Asia in the 21st Century," *Contemporary Southeast Asia* 25, no. 1 (2003), p. 77.

<sup>78</sup> Zhang Yunliang, and Tang Shiping, 2005, p. 59.



# 3

## China's Oil Security

This chapter gives an overview of the development of China's oil consumption in recent years, China's strategy to secure sufficient oil supplies, and the country's policy towards its key oil suppliers. The final part of this chapter discusses the main threats to China's oil security – Japan as its most important regional competitor for oil supplies and US interference in oil-producing regions, as well as US activities along crucial transport routes.

### 3.1 The Development of China's Oil Demand

#### *China's Energy Consumption*

China has a quite distinctive energy consumption pattern among the major economies. Generally, these countries have opted to rely heavily on cheap oil and gas, while no more than 30% of their energy supply comes from coal. For the past 50 years, however, coal has been China's most significant source of energy, making up 67.1% of the country's current primary energy consumption.<sup>79</sup> At the beginning of Communist rule in the 1950s, less capital-intensive coal extraction was a natural choice. In fact, China's continued reliance on coal is a result of the country's scarce endowment of oil resources, a lack of environmental concern, and the higher technology barrier to exploring and extracting oil and natural gas.<sup>80</sup> Analysts expect that the consumption of other energy sources will grow, but coal will remain China's main energy source for the foreseeable future.<sup>81</sup>

Currently, oil is China's second most important energy resource, accounting for 20% of the country's energy consumption.<sup>82</sup> China has proven oil reserves of about 17.1 billion barrels, which is 1.4% of the world's total. In 2004, China produced 3.4 million barrels a day (b/d). Yet since 1993, China's demand for oil has been exceeding its domestic oil production.<sup>83</sup> The country's growing demand is further exacerbated by the fact that the major oil fields in Northeast China, where nearly 90% of the country's total crude is produced, have already peaked and are in decline. This is particularly true for China's largest oil fields, Daqing and Shengli in the provinces of Heilongjiang and Shandong, which are both considered to be over-drilled. Unfortunately, efforts to develop deposits located in the Tarim Basin in Xinjiang were for the most part in vain, as both Chinese and foreign companies failed to make the kind of discovery that would confirm the basin as a major oil source. Moreover, exploration in the Tarim Basin is rather unprofitable.<sup>84</sup> Despite recent offshore discoveries in the Bohai Bay, the

<sup>79</sup> "2005 nian Zhongguo meitan hangye fenxi" (2005 analysis of China's coal sector), *Meitan wang*, 18 January 2006. [http://www.coal.com.cn/CoalNews/ArticleDisplay\\_116698.html](http://www.coal.com.cn/CoalNews/ArticleDisplay_116698.html).

<sup>80</sup> Su Fubing, "The Political Economy of Industrial Restructuring in China's Coal Industry, 1992-1999," in *Holding China Together: Diversity and National Integration in the Post-Deng Era*, ed. Barry J. Naughton and Dali L. Yang, Cambridge: Cambridge University Press, 2004, p. 230.

<sup>81</sup> "2005 nian Zhongguo meitan hangye fenxi" (2005 analysis of China's coal sector), *Meitan wang*, 2006; Downs, Erica S., "The Chinese Energy Security Debate," *The China Quarterly*, no. 177 (March 2004), p. 22.

<sup>82</sup> Feng Yuewei, *Shiyou boyi* (The oil game). Beijing: Qiye guanli chubanshe, 2003, p. 371.

<sup>83</sup> British Petroleum (BP), "Putting Energy in the Spotlight: BP Statistical Review of World Energy," June 2005.

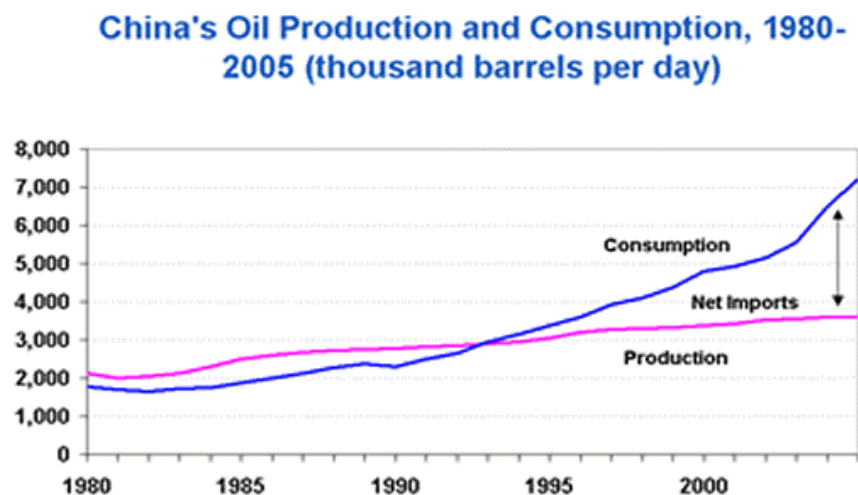
[http://www.bp.com/liveassets/bp\\_internet/globalbp/globalbp\\_uk\\_english/publications/energy\\_reviews\\_2005/STAGING/local\\_assets/downloads/pdf/statistical\\_review\\_of\\_world\\_energy\\_full\\_report\\_2005.pdf](http://www.bp.com/liveassets/bp_internet/globalbp/globalbp_uk_english/publications/energy_reviews_2005/STAGING/local_assets/downloads/pdf/statistical_review_of_world_energy_full_report_2005.pdf); Su Fubing, 2004, p. 229.

<sup>84</sup> Downs, Erica S., 2000, 7; Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence: The Costs and Policy Implications of Supply Alternatives," prepared for the James A. Baker III Institute for Public Policy of Rice University, Houston, TX, April 1999,

[http://www.rice.edu/energy/publications/docs/AsianEnergySecurity\\_ChinaGrowingEnergyDependence.pdf](http://www.rice.edu/energy/publications/docs/AsianEnergySecurity_ChinaGrowingEnergyDependence.pdf).

Pearl River Delta, and the Beibu Gulf (Gulf of Tonkin), China's domestic oil production is not expected to increase substantially in the coming years.<sup>85</sup>

**Figure 3.1: China's oil production and consumption, 1980-2005**



Source: Energy Information Administration of the US Department of Energy (EIA). "China." 2 August 2005, <http://www.eia.doe.gov/emeu/cabs/china.html>.

As a result of the country's rapid economic development and the decline in domestic supply, China has become ever more dependent on foreign oil in recent years.<sup>86</sup> Analysts expect that China's reliance on foreign oil supplies will continue to grow over the next two decades because of the widening gap between domestic production and demand. Currently, imports account for 40% of Chinese oil demand, and calculations suggest that China's oil import dependence will reach 50% by 2010 and at least 60% by 2020.<sup>87</sup>

#### *Economic Development and Energy Demand*

The aggregate energy demand of an economy is determined by the relative size of the agricultural, industrial, and service sectors. Economic development causes structural changes that are reflected in shifts in the output contributions of the agricultural, industrial and service sectors. These changes subsequently influence the growth of energy consumption. In the initial stages of economic growth, the share of agriculture in total output falls, while the share of industry rises. In latter stages of development the services share increases, which eventually will dominate total output. The industrialisation process is typified by enormous increases in energy consumption, because industry is more energy-intensive than agriculture. Additionally, energy demand for transportation and for residential and commercial uses also increases with economic progress.<sup>88</sup> However, currently wealthy economies

<sup>85</sup> Myers Jaffe, Amy and Steven W. Lewis, "Beijing's Oil Diplomacy," *Survival* 44, no. 1 (2002), p.120.

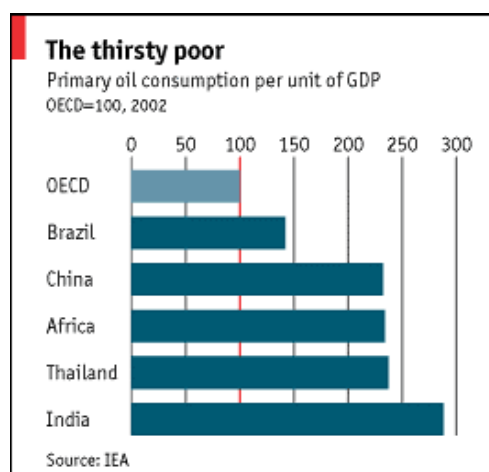
<sup>86</sup> Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," Testimony during the hearing on EIA's Annual Energy Outlook for 2005 by the Committee on Energy and Natural Resources of the US Senate, 3 February 2005, [www.iea.org/textbase/speech/2005/jl\\_china.pdf](http://www.iea.org/textbase/speech/2005/jl_china.pdf).

<sup>87</sup> Shi Dan, "Yizhan dui shijie shiyou geju de yingxiang ji woguo de duice" (The influence of the Iraq war on the structure of the global oil business and China's countermeasures), in *Yilake zhanzheng yu Zhongguo jingji* (The Iraq war and China's economy), ed. Shi Guangsheng, Beijing: Zhonghua gongshang lianhe chubanshe, 2003, p. 196; Downs, Erica S., 2000, p. 9.

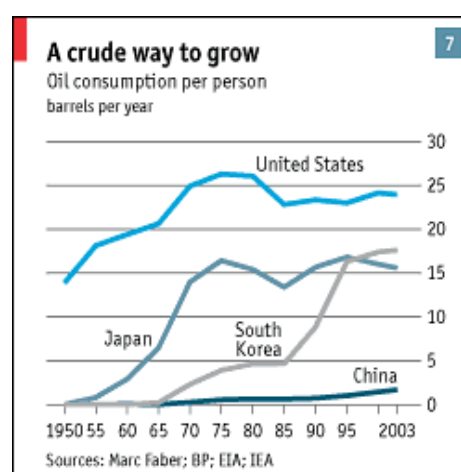
<sup>88</sup> Medlock III, Kenneth B., and Ronald Soligo, "The Composition and Growth of Energy Demand in China," prepared for the James A. Baker III Institute for Public Policy of Rice University, Houston, TX, April 1999, [http://www.rice.edu/energy/publications/docs/AsianEnergySecurity\\_CompositionGrowthEnergyDemandChina.pdf](http://www.rice.edu/energy/publications/docs/AsianEnergySecurity_CompositionGrowthEnergyDemandChina.pdf).

are less energy-intensive, in that they use energy more efficiently than do developing and industrialising countries.<sup>89</sup>

**Figure 3.2: Oil consumption per unit of GDP, Figure 3.3: Oil consumption per person 2002**



Source: "Oil: Pain at the Pump." *The Economist*, 20 May 2004, [http://www.economist.com/displaystory.cfm?story\\_id=2693292](http://www.economist.com/displaystory.cfm?story_id=2693292).



Source: "Survey –The World Economy: A Hungry Dragon." *The Economist*, 30 September 2004, [http://www.economist.com/displaystory.cfm?story\\_id=559446](http://www.economist.com/displaystory.cfm?story_id=559446).

Still, since growing demand for energy is a result of and a necessity for economic development, governments must either develop domestic resources or increase national dependence on international sources as part of their overall strategy for economic transformation.<sup>90</sup>

As a whole, China is still at the lower end of the development spectrum when per capita GDP is used as a benchmark for comparison with other economies. Thus, the bulk of China's total energy demand will continue to come from its ongoing industrialisation for the foreseeable future. Moreover, the analysis of the development of real GDP for various countries reveals a trend of increasing energy consumption with income growth. Medlock and Soligo therefore conclude that even under modest growth scenarios, energy demand in China will increase significantly for years to come.<sup>91</sup>

**Table 3.1: Comparative economic indicators, 2002**

Country	US	Japan	Germany	China	India
GDP (US\$ billion)	10,4446	3,973	1,994	1,266	502
GDP per capita (US\$)	36,406	31,270	24,211	974	480
GDP per capita (US\$ at PPP*)	36,406	26,739	26,663	4,720	2,620

\* purchasing power parity

Source: "Country Profile: China – Economic Structure." *The Economist*, 9 February 2004, <http://www.economist.com/countries/China/profile.cfm?folder=Profile%2DEconomic%20Structure>.

<sup>89</sup> "Oil: Pain at the Pump," *The Economist*, 22 May 2004, p. 79.

<sup>90</sup> Medlock III, Kenneth B., and Ronald Soligo, "The Composition and Growth of Energy Demand in China," 1999.

<sup>91</sup> Ibid.

**Table 3.2: China – Economic indicators, 2004**

<b>Population</b> (million)	1,299.8
<b>GDP</b> (US\$ billion; market exchange rate)	1,681.3
<b>GDP</b> (US\$ billion; PPP)	7,553.2
<b>GDP per capita</b> (US\$; market exchange rate)	1,293.0
<b>GDP per capita</b> (US\$; PPP)	5,811.0

Source: "Country Profile: China – Factsheet." *The Economist*, 13 July 2005, <http://www.economist.com/countries/China/profile.cfm?folder=Profile-FactSheet>.

**Table 3.3: China – Structure of the Economy**

% of GDP	1984	1994	2003	2004
<b>Agriculture</b>	32.0	20.2	14.6	15.2
<b>Industry</b>	43.3	47.8	52.2	52.9
<b>Manufacturing</b>	35.5	34.4	36.7	37.3
<b>Services</b>	24.7	31.9	33.2	31.9

Source: The World Bank Group. "China at a Glance." 9 July 2005, [www.worldbank.org/cgi-bin/sendoff.cgi?page=/data/countrydata/aag/chn\\_aag.pdf](http://www.worldbank.org/cgi-bin/sendoff.cgi?page=/data/countrydata/aag/chn_aag.pdf).

In 2004, China's oil consumption reached 6,684,000 b/d and its demand rose by nearly 900,000 b/d – or more than 15% – compared to the previous year.<sup>92</sup> In both 2003 and 2004, imports of crude oil grew alarmingly – from 1.4 million b/d in 2002 to 2.5 million b/d in 2004.<sup>93</sup> Consumption will not continue to grow at such a phenomenal rate, however, because the increased demand for oil was mainly the result of China's investment boom, a doubling of car sales, and shortages of cheap coal.<sup>94</sup> Expensive oil and diesel were temporarily used for electricity generation. Yet as soon as China has closed the generation shortage by installing new coal, natural gas, hydro, and nuclear power plants, the use of oil for electricity generation will decline. Finally, there will not be enough cars in all of China in the near future to sustain such rises in demand for oil.<sup>95</sup> Already in January and February 2005, China's oil demand rose by 5.4%; less than a quarter of the rate as the same period in 2004.<sup>96</sup>

Undoubtedly, China's demand for oil will continue to rise, though at more moderate rates, in the years to come. China's real GDP is still growing at an annual rate of around 9.5%,<sup>97</sup> while industrial production was up by 16.4% in the first half of 2005.<sup>98</sup> Continuing industrialisation and urbanisation will contribute to a steady increase in China's oil demand for many years.<sup>99</sup> The scarcity of its domestic oil resources forces China to rely on foreign oil supplies in order to guarantee a sufficient

<sup>92</sup> BP, "Putting Energy in the Spotlight," 2005.

<sup>93</sup> Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," 2005.

<sup>94</sup> "A Survey of the World Economy – The Dragon and the Eagle: A Hungry Dragon," *The Economist*, 2 October 2004, p. 12.

<sup>95</sup> "A Survey of Oil: Oil in Troubled Waters," *The Economist*, 30 April 2005, p. 6; Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," 2005.

<sup>96</sup> "A Survey of Oil: Oil in Troubled Waters," 2005, p. 6.

<sup>97</sup> Economic growth has averaged 9.5% over the past two decades and is likely to continue at that pace for some time. See Organisation for Economic Co-operation and Development (OECD), "Economic Survey of China 2005," 16 September 2005, [http://www.oecd.org/document/7/0,2340,en\\_2649\\_201185\\_35343687\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/7/0,2340,en_2649_201185_35343687_1_1_1_1,00.html).

<sup>98</sup> "The Economist Poll of Forecasters," *The Economist*, 27 May 2005, p. 114; "Emerging-markets Indicators," *The Economist*, 27 May 2005, p. 114; "Chinese Growth 'to Remain Strong,'" *BBC News*, 10 May 2006., <http://news.bbc.co.uk/1/hi/business/4756761.stm>.

<sup>99</sup> "A Survey of the World Economy – The Dragon and the Eagle: A Hungry Dragon," 2004, p. 15.

supply of energy resources for its economic development. This energy dependence will leave China with tough political choices.<sup>100</sup>

**Table 3.4: China – Economic indicators, 2000-4**

Year	2000	2001	2002	2003	2004
<b>GDP per capita</b> (US\$ at PPP)	3,980	4,340	4,720	5,180	5,811
<b>GDP</b> (% real change per anno)	+8.00	+7.50	+8.00	+9.30	+9.50
<b>Industrial production</b> (% change on year ago)	+9.8	+8.7	+10.0	+12.8	+16.4

Source: "China: No Sign of a Landing." *The Economist*, 29 January 2005, pp. 49-50; "Country Profile: China – Economic Data." *The Economist*, 13 May 2004, <http://www.economist.com/countries/China/profile.cfm?folder=Profile%2DEconomic%20Data>; The World Bank Group. "China: Economic Indicators – Cumulative." 21 September 2005, [siteresources.worldbank.org/CHINAEXTN/Resources/318949\\_1121421890573/chinaei.pdf](http://siteresources.worldbank.org/CHINAEXTN/Resources/318949_1121421890573/chinaei.pdf).

### 3.2. China's Strategy and Means for Ensuring Its Oil Supply

#### *China's Oil Strategy*

China has no energy ministry<sup>101</sup> or special commission to coordinate all energy-security activities carried out by actors throughout the Chinese bureaucracy and, subsequently, orchestrate an overall energy strategy.<sup>102</sup> China's "strategy" to secure its oil supply is, rather, a result of numerous debates and campaigns conducted by a number of stakeholders. The most important participants in this debate are China's major state-owned oil companies, the National Development and Reform Commission,<sup>103</sup> the Ministry of Foreign Affairs, the People's Liberation Army (PLA), and analysts affiliated with various think tanks and universities.<sup>104</sup> The participation of such a multitude of actors in the debate results from China's increased involvement with the outside world, which requires specialised knowledge and creates more room for apolitical expert input into the policy-making process.<sup>105</sup>

So far, the major oil companies and their partially privatised subsidiaries wield considerable influence in the debate because of their expertise and their political clout.<sup>106</sup> The ministry-level National Development and Reform Commission is responsible for drafting the five-year energy plans; it also sets energy prices and agrees upon projects larger than US\$30 million. In this regard, it plays an important role in coordinating energy policy aims. Its 2002 oil security plan, for instance, called for a number of measures aimed at increasing China's control over its supplies, including investments in overseas oil fields, the construction of a strategic oil reserve, and the development of Chinese naval and air forces to protect China's energy supplies. The Ministry of Foreign Affairs advocates the cultivation of close relationships with oil-producing states. Chinese diplomats are also involved in

<sup>100</sup> Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence," April 1999.

<sup>101</sup> The Ministry of Energy was set up in 1988. It was dismissed five years later because its administrative function overlapped with other departments such as the then State Development Planning Commission.

<sup>102</sup> Downs, Erica S., "The Chinese Energy Security Debate," *The China Quarterly*, no. 177 (March 2004), 30.

<sup>103</sup> This commission at ministry level is part of the State Council, China's government, and coordinates the central government's economic policy.

<sup>104</sup> Downs, Erica S., 2004, pp. 25-7.

<sup>105</sup> *Ibid.*, p. 39.

<sup>106</sup> Due to the importance of the companies for the government's oil strategy and the fact that top positions of CNPC, Sinopec, and CNOOC are appointed by the Central Committee of the Chinese Communist Party (CCP), executives of China's oil companies have direct access to the Chinese leadership. See Downs, Erica S., 2000, p. 46; Downs, Erica S., 2004, p. 25.

helping the Chinese oil companies plan their overseas investments. Hence, Chinese foreign policy towards oil-rich countries is increasingly determined by energy issues.<sup>107</sup> The PLA deals with the energy sector at two levels. First, it is frequently asked to participate in the modernisation and expansion of China's energy infrastructure. Second, it assesses possible threats to domestic energy sources and supplies from abroad.<sup>108</sup> PLA analysts fear that a possible conflict with the US over Taiwan could interrupt China's seaborne oil import. Therefore, the PLA is pushing for the development of naval and air forces to protect China's oil supply lines and has suggested decreasing the country's reliance on oil imports from the Middle East and establishing strategic petroleum reserves.<sup>109</sup>

The principal organ responsible for China's energy policy should be the Energy Bureau, a body under the ministry-level National Development and Reform Commission. However, as inherited from the country's planned economy, large oil, power and coal companies are administered by several ministries. Therefore, the Energy Bureau, with its staff of about 20 people, frequently fails to coordinate relations between the different energy sectors, obviously lacking the capacity and influence needed to handle China's energy industry that has total assets of more than US\$1.2 trillion. As a consequence, China's energy policy has often been inconsistent, sometimes even contradictory.<sup>110</sup> Moreover, the Energy Bureau's position within the governmental administration is too minor to allow it to cooperate efficiently with other countries. Yet in December 2004, the central government ruled out the possibility of re-establishing the Ministry of Energy for at least three years. Instead, the central government is considering the possibility of establishing a special office for the management of the energy industry directly under the State Council. Senior officials, including one vice-premier, would head that office.<sup>111</sup> However, even with the establishment of such an office it can be expected that the above-mentioned major stakeholders will continue to shape China's oil security strategy.

China's oil security debate is exemplary of the trend of "corporate pluralisation" in the country's policy-making process, in which the participants of the debate seek to influence the top 25 to 35 senior leaders who make national policy. In order to find their way through the bureaucracy, proposals for major projects need the passionate support of at least one senior leader to be approved by China's consensus-based leadership.<sup>112</sup> Thus, by evaluating and deciding upon proposals that emanate from below, China's top leadership is directly involved in energy-related decision making, including all major initiatives that China pursues to enhance its energy security.<sup>113</sup> Leaders such as the former Prime Ministers Li Peng and Zhu Rongji as well as former President Jiang Zemin have decided upon proposals for the development of overseas oil fields, the allocation of overseas investments, the routing of transnational pipelines, and issues of the country's oil diplomacy.<sup>114</sup>

The Chinese government's unease about the country's status as a net oil importer is the result of the dreadful experience of the late 1950s and 1960s. The withdrawal of all Soviet advisers and the chaotic management of the economy during the Great Leap Forward (1958-61) led to considerable energy shortages that caused China's leaders to call for an accelerated effort to become self-sufficient in oil and cemented the government's ultimate control over the domestic energy sector.<sup>115</sup>

Until the mid-1990s, China's energy strategy appeared disjointed and was often influenced by multiple, sometimes mutually exclusive objectives which were frequently designed to meet political

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<sup>107</sup> Downs, Erica S., 2004, pp. 25-6.

<sup>108</sup> Cole, Bernard D., *"Oil for the Lamps of China": Beijing's 21st-Century Search for Energy*. Washington, DC: National Defense University Press, 2003, p. 57.

<sup>109</sup> Downs, Erica S., 2004, p. 26.

<sup>110</sup> Xie Ye, "Government Rules out Forming New Energy Ministry," *China Daily*, 2 December 2004, [http://www.chinadaily.com.cn/english/doc/2004-12/02/content\\_396820.htm](http://www.chinadaily.com.cn/english/doc/2004-12/02/content_396820.htm).

<sup>111</sup> *Ibid.*

<sup>112</sup> This group of leaders mainly consists of the members of the Politburo of the CCP, but it also includes members of the Secretariat of the CCP, the Standing Committee of the State Council, senior military commanders, and provincial leaders. See Downs, Erica S., 2004, p. 30.

<sup>113</sup> *Ibid.*

<sup>114</sup> Downs, Erica S., 2004, p. 40; Klare, Michael, 2004, p. 168.

<sup>115</sup> Downs, Erica S., 2004, p. 11.

ends and disregarded economic considerations.<sup>116</sup> The current leadership is highly aware of the importance of undisrupted oil supplies to the country's economic development and political stability.<sup>117</sup> In 2002, Chinese analysts concluded that oil supplies from other regions should partially replace imports from the Persian Gulf.<sup>118</sup> Thus, growing instability in the Middle East and China's rising dependence on imported oil caused China's policymakers to reconsider the country's oil strategy. Accordingly, the leadership called for a diversification of the country's oil supplies, both in terms of the development of alternative energy resources and the establishment of new oil supply markets. In addition, this adjusted energy strategy was more based upon market principles than previous approaches had been.<sup>119</sup>

The Chinese government pursues a multilayered strategy by establishing strategic oil reserves, promoting overseas oil investments, and conducting its oil diplomacy pragmatically in order to diversify China's oil supply. China hopes to gain greater control over its foreign oil supply by acquiring oil concessions abroad. Overseas investments are made so as to insulate China's economy from price hikes on the international market and to stabilise the economy during a potential oil shock by ensuring that the Chinese market will always receive a certain amount of oil. This stability is achieved by investing in exploration and development in countries that have oil fields but lack the capital or technology to exploit them. Once the Chinese oil companies have a stake in the oil produced at a site, they will have secured long-term supplies independent of the world market prices.<sup>120</sup> Yet despite all attempts to diversify China's oil supplies, it seems impossible to substantially decrease China's reliance on Middle Eastern oil for the time being.<sup>121</sup>

### *The Function of the Three Major State-owned Oil Companies*

China's oil sector is controlled by three large state-owned oil companies. Since a major reorganisation in 1998, CNPC (China National Petroleum Corporation) and Sinopec (China National Petrochemical Corporation) have been involved in both upstream and downstream activities. Both CNPC and Sinopec have become vertically integrated companies of international stature, at least in size and range of activities.<sup>122</sup>

CNPC is the largest of China's state-owned oil producers and retains more than two-third of China's crude oil production capacity. It conducts exploration and production onshore and in shallow offshore areas. Sinopec's main business involves activities such as the marketing, refining, and processing of petrochemicals. Yet in recent years, Sinopec has also begun to produce oil and gas. CNOOC (Chinese National Offshore Oil Corporation) is primarily engaged in offshore oil exploration.<sup>123</sup>

<sup>116</sup> Tanner, Travis, "The Oil That Troubles US-China Waters," *Asia Times Online*, 18 June 2004, <http://www.atimes.com/atimes/China/FF18Ad04.html>.

<sup>117</sup> "Hu Jintao: quanmian zuohao nengyuan ziyuan gongzuo – youxian zhuahao jieyue nengyuan" (Hu Jintao: we have to comprehensively take on the task of [ensuring supply with] energy resources – energy conservation has to be given priority), *Renmin wang*, 28 June 2005, <http://politics.people.com.cn/GB/1024/3503686.html>.

<sup>118</sup> Xu Shengru, "Guoji zhanlue pinglun: Zhong E guanxi de 'toudeng da shi'" (A comment on international strategies: the 'matter of cardinal importance' of Sino-Russian relations), *Renmin wang*, 17 December 2002, <http://www.people.com.cn/GB/junshi/62/20021217/889469.html>.

<sup>119</sup> Tanner, Travis, "The Oil That Troubles US-China Waters," 2004.

<sup>120</sup> Downs, Erica S., 2000, p. 18; "Shiyou dazhan hou kan Zhongguo shiyou lian – Zhongguo guoji gongcheng zixun gongsi shihua zhuanjia Yang Shangming zhuanfang" (China's oil sector after the big oil war – Interview with oil expert Yang Shangming, China international construction consultancy), *Zhongguo shiyouwang*, 1 February 2005, <http://www.oilnews.com.cn/oilnews/>; Forney, Matthew, "China's Quest for Oil," *Time Asia Magazine*, 18 October 2004, <http://www.time.com/time/asia/magazine/article/0,13673,501041025-725174,00.html>.

<sup>121</sup> Shi Dan, 2003, p. 189.

<sup>122</sup> Andrews-Speed, Philip, and Sergei Vinogradov, "China's Involvement in Central Asian Petroleum: Convergent or Divergent Interest?," *Asian Survey* 40, no. 2 (2000), p. 392.

<sup>123</sup> Downs, Erica S., 2000, p. 13; Cole, Bernard D., 2003, p. 2; Zhongguo shiyou huagong gufen youxian gongsi (China petroleum and chemical corporation (Sinopec)), "Er ling ling si nian shi'er yue sanshiyi ri zhi de yeji gonggao" (31 December 2004 business report), 31 December 2004, <http://www.sinopec.com/newsevent/announcement/download/ann050329a.pdf>.

The reorganisation of China's oil sector has not yet been completed. Thus far, some market mechanisms have been introduced to allow the participation of private domestic oil companies. Yet at least nominally, the state-owned enterprises remain at the commanding heights of the energy sector.<sup>124</sup>

**Table 3.5: China's state-owned energy companies**

2002, US\$ billion	Revenue	Net income	Market capitalisation (February 2004)
<b>CNPC</b>	29.5	5.7	90.7
<b>Sinopec</b>	39.2	1.9	51.9
<b>CNOOC</b>	3.2	1.1	16.8

Source: "We Are the Champions." *The Economist*, 18 March 2004, [http://www.economist.com/displaystory.cfm?story\\_id=2495172](http://www.economist.com/displaystory.cfm?story_id=2495172).

During the 1980s, due to internal competition between the companies for state funding and the government's fixing of prices for crude oil, refined products and petrochemicals, CNPC lacked sufficient funds to enhance domestic exploration activities. Subsequently, domestic production stagnated, while imports began to soar in the late 1980s and early 1990s.<sup>125</sup>

In 1993, after the Chinese government had gradually relaxed oil price controls, CNPC was able to raise sufficient capital for oil-field development. The enormous profits that CNPC gained between 1993 and 1997 enabled the company to acquire interests in petroleum exploration and production abroad. Another factor that prompted CNPC officials to invest overseas was the fear that the central government might confiscate these profits if CNPC did not invest the money quickly, as well as a combination of uncertainty about prospects for domestic development and the ready availability of oil abroad.<sup>126</sup> So far, most of China's onshore exploration activities abroad have been conducted by CNPC's holding company, PetroChina.<sup>127</sup>

In their pursuit of oil supplies, CNPC and the two other companies have transformed themselves into multinational, integrated oil companies by establishing subsidiaries and acquiring overseas assets along with refineries.<sup>128</sup> Although each of the three companies has attracted billions of dollars of capital by listing between 10% and 30% of the shares of their subsidiaries on stock exchanges in Hong Kong, New York, and Shanghai, the Chinese government still holds a majority interest in the companies.<sup>129</sup> Nevertheless, the companies' officials mainly base their decisions on profitability, and they increasingly decide in favour of the company's commercial interests, rather than solely following China's national energy strategy. Actually, they are no longer willing to engage in politically motivated but commercially dubious pipelines projects without financial support from the government.<sup>130</sup>

The three state-owned oil companies invest in overseas oil exploration and development projects for several reasons. First, China's rising oil demand has to be met. Second, domestic production has been declining for a couple of years while the companies have failed to make any major new domestic discoveries.<sup>131</sup> Moreover, they take advantage of the lower costs in their domestic market and rely on

<sup>124</sup> Cole, Bernard D., 2003, p. 1.

<sup>125</sup> Downs, Erica S., 2000, p. 14.

<sup>126</sup> Ibid.

<sup>127</sup> Cole, Bernard D., 2003, pp. 3-9.

<sup>128</sup> Ibid.

<sup>129</sup> "China: Investors Are Hungry for 'Big Macs'," *BusinessWeek*, 30 July 2001, p. 23; "China's Oil Companies: Drilling for the Party," *The Economist*, 24 May 2003, p. 66.

<sup>130</sup> Downs, Erica S., 2004, 30, 37; Cole, Bernard D., 2003, pp. 2-3.

<sup>131</sup> Downs, Erica S., 2000, pp. 13-4.

favourable credit conditions provided by the government and China's financial institutions to compete with rivals from the US and other countries. As a result, they spend wildly and their bids are often uneconomic, pursuing market and strategic objectives rather than commercial ones.<sup>132</sup>

The Chinese leadership's unease about the dominance of the world oil market by companies from the US, Japan and Western Europe stems from the fear that they could potentially seek to limit China's access to oil. Accordingly, the government views the internationalisation of the companies as a way for China to gain a foothold in the world oil market.<sup>133</sup> In fact, the Chinese government hopes that the three state-owned companies can fulfil two duties. First, that they gain experience in order to become competitive with the world's top energy companies. Second, that they contribute to the enhancement of China's national energy security.<sup>134</sup>

Chinese strategists acknowledge that the Chinese oil companies, which developed under the premise of oil self-sufficiency within a planned economy, are hardly able to compete with multinational corporations with more than 100 years of experience. Chinese companies must obtain the necessary know-how through cooperation with other companies. Overseas investments are deemed crucial for the companies to become world-class corporations.<sup>135</sup>

As the government's influence has been diminishing since the oil companies' initial public offerings abroad, the oil companies are becoming the key drivers of investments in overseas oil exploration and development projects.<sup>136</sup> Since they view themselves as global players, China's oil companies are eager to develop their overseas projects, not only by fulfilling their role in the government's strategy, but also as profit-minded corporations.<sup>137</sup> However, the lack of transparency over investment amounts, contract details, and proven oil reserves creates a more successful image of China's oil companies than is actually the case.<sup>138</sup> Moreover, despite the companies' ambitions, the Chinese government still has the final say over investments and acquisitions abroad. In addition, the unpredictability of the ongoing reform of China's energy sector and the resulting competition among CNPC, Sinopec, and CNOOC have a growing impact on their international activities.<sup>139</sup>

The Chinese government aims to spend several hundred billions of US dollars in the first decade of the 21st century to build pipelines, intensify oil and gas exploration at home and abroad, and make China's energy generation more efficient.<sup>140</sup> Therefore, the oil companies continue to receive substantial financial support and have been encouraged by senior leaders to obtain deals all across the Middle East, Southeast Asia, Russia, Central Asia, Africa, Australia, and the Americas.<sup>141</sup>

The spearhead of China's overseas oil and gas expansion is CNPC, which had already signed 48 contracts with 20 countries by the end of 2004.<sup>142</sup> Over the past few years, China's oil companies have acquired development rights to, or partial ownership of, major oil fields in many oil-producing countries by outbidding Western firms in almost every case, often by substantial amounts. Still, though many of these arrangements make sense in purely economic terms, at least as part of a strategy to diversify supply, they also reflect the geostrategic orientation of China's energy policy.<sup>143</sup> Consequently, all three state-owned will continue to pursue this approach for the time being. In 2006 they plan to acquire more concessions and firms in developing countries in Africa, the Middle East, Latin America, and Southeast Asia. Moreover, they want to cooperate more effectively. Finally,

<sup>132</sup> Forero, Juan, "China Woos Latins in Oil Hunt," *International Herald Tribune*, 2 March 2005, <http://www.iht.com/articles/2005/03/01/business/oil.html>.

<sup>133</sup> Downs, Erica S., 2000, p. 46.

<sup>134</sup> *Ibid.*, p. 51; Downs, Erica S., 2004, p. 25.

<sup>135</sup> Feng Yuewei, 2003, p. 332.

<sup>136</sup> "China: Growing up Fast," *BusinessWeek*, 31 March 2003, p. 21; "China's Oil: Taken Hostage," *The Economist*, 12 June 2001, [http://www.economist.com/displaystory.cfm?story\\_id=695683](http://www.economist.com/displaystory.cfm?story_id=695683).

<sup>137</sup> Shi Dan, 2003, pp. 194-5.

<sup>138</sup> Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," 2005.

<sup>139</sup> "China Bashing: Giving China a Bloody Nose," *The Economist*, 6 August 2005, p. 49.

<sup>140</sup> "China: Hungry for Energy," *BusinessWeek*, 24 December 2001, p. 20.

<sup>141</sup> Downs, Erica S., 2004, p. 34.

<sup>142</sup> "Feeding the Dragon," *Petroleum Economist* 72, no. 12 (2005), p. 10.

<sup>143</sup> Klare, Micheal, 2004, 171, p. 169.

Chinese firms are keen to make more joint bids with India's ONGC in some regions in order to reduce the bills for their foreign projects.<sup>144</sup>

### *China's Oil Diplomacy*

The Chinese government relinquished the goal of oil self-sufficiency in 1986.<sup>145</sup> Until that time, China enjoyed the luxury of neutrality toward events in oil geopolitics. As internal supplies fairly evenly matched domestic requirements, China's economy was sheltered from the volatile international oil business. Hence, conflicts in the Middle East were a matter of indifference to the Chinese leadership.<sup>146</sup> Undoubtedly, China's shift to an oil importer has had significant geopolitical implications. Since the mid-1990s, China has been forced to participate in the international energy trade, form energy supply and transportation alliances, and make security as well as environmental choices about fulfilling its future energy needs.<sup>147</sup>

Initially, Chinese analysts were split as to what a greater reliance on foreign oil would imply for China's overall security. However, oil security became a matter of great urgency in 2000, when crude oil imports doubled and the import bill tripled. The question as to how China can meet its growing demand for foreign oil without undermining its national security has been hotly debated ever since. In fact, for the government, securing China's energy needs has risen to the highest level of priority in terms of statecraft and commercial activity.<sup>148</sup>

Because Saudi Arabia has emerged as China's biggest oil supplier in recent years, China is making concerted efforts to ensure long-term supplies from this country by pursuing "cross investment" arrangements. Under these arrangements, Saudi Arabian companies make refinery investments in China, while Chinese oil companies conduct upstream oil-field activities in Saudi Arabia.<sup>149</sup> Currently, Saudi Arabian and Chinese companies jointly construct oil refineries in China. The first two refineries are being built in Qingdao in the eastern province of Shandong and in Quanzhou in the southeastern province of Fujian.<sup>150</sup> Saudi Arabia's Aramco received a 25% stake in each of these refineries and will supply the majority of the crude that will be refined there. Such arrangements will help guarantee that Saudi Arabia will earmark part of its oil production for the Chinese market.<sup>151</sup> Since the early 1990s, Saudi Aramco has been lobbying for these projects, which help Saudi Arabia to diversify its exports markets. Moreover, Saudi officials are eager to expand their sales of refined products and to gain access to the Chinese retail gas market.<sup>152</sup>

As Saudi Arabia will play a key role in China's strategy for the Persian Gulf, Chinese officials have been keen to improve relations between the two countries. Recent state visits by King Abdullah and Hu Jintao could further improve bilateral ties.<sup>153</sup> In fact, Saudi Arabia's closer energy cooperation with

<sup>144</sup> "Zhongguo shiyou qiye 2006 nian haiwai bingguo zhanwang: duoyuan bingguo quanmian jiemeng dao you shiyou de difang qu" (2006 M&A outlook for Chinese oil companies: united approach to oil-producing regions), *Di yi caijing ribao*, 27 January 2006. <http://dycj.yinet.com/article.jsp?oid=7519951>.

<sup>145</sup> China had been a net oil importer in the 1950s and early 1960s. At that time, it received most of its oil imports from the Soviet Union. After the Sino-Soviet split in 1961, Mao Zedong introduced the doctrine of self-reliance as the guiding principle for economic development. See Downs, Erica S., 2000, pp. 11-12.

<sup>146</sup> Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence," April 1999.

<sup>147</sup> Ibid.

<sup>148</sup> Downs, Erica S., 2004, p. 22; Calabrese, John, "Saudi Arabia and China Extend Ties Beyond Oil," *China Brief*, 27 September 2005.

[http://www.jamestown.org/publications\\_details.php?volume\\_id=408&issue\\_id=3474&article\\_id=2370272](http://www.jamestown.org/publications_details.php?volume_id=408&issue_id=3474&article_id=2370272)>> (28 September 2005).

<sup>149</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 123.

<sup>150</sup> Pottinger, Matt, "Aramco to Invest in China Again," *The Wall Street Journal Europe*, 12 July 2005, p. A4.

<sup>151</sup> Ibid.

<sup>152</sup> "Shiyou dazhan hou kan Zhongguo shiyou lian – Zhongguo guoji gongcheng zixun gongsi shihua zhuanjia Yang Shangming zhuanfang" (China's oil sector after the big oil war – Interview with oil expert Yang Shangming, China international construction consultancy), *Zhongguo shiyouwang*, 1 February 2005, <http://www.oilnews.com.cn/oilnews/>; Calabrese, John, "Saudi Arabia and China Extend Ties Beyond Oil," 2005.

<sup>153</sup> Saudi Arabia agreed to increase its oil and gas exports to China by 39% and promised to ship oil to China "what ever might happen." See "Shate yu Zhongguo shiyou hezuo erzhongjie: dui Zhongdong shiyou yilai jiashen" (Saudi-Chinese duet: dependence on Middle Eastern oil increases), *NetEase*, 23 January 2006, <http://biz.163.com/06/0123/05/284K6UQ900020QFA.html>; see also "Shate guowang xiang Hua song da dan: shiyou tianran

China can not only lessen domestic discontent at the government's previous too pro-American stance, but also help deflect US pressure to introduce political reforms. Furthermore, strong Sino-Saudi relations can increase Saudi Arabia's diplomatic capability to manoeuvre and realise its own diversified security strategies.<sup>154</sup>

For the Chinese side, the payoff is also worth the effort. When in March 2004 Saudi Arabia issued concessions for deposits in Saudi Arabia for the first time since 1973, Sinopec won the bid for a natural gas project in the Rub al-Khali gas fields, while US companies bid in vain.<sup>155</sup> Moreover, China takes advantage of discriminatory US policies towards the countries in the Persian Gulf, for instance regarding visa applications. As a result, Chinese universities are becoming attractive destinations for young Saudi Arabians, which helps create future Chinese-speaking business elites.<sup>156</sup> Additionally, the number of personal and professional contacts and exchanges between Saudi Arabia and China has risen in recent years, which makes it easier to overcome the linguistic-cultural divide.<sup>157</sup>

In fact, China has been able to establish mutually beneficial economic relations with most of the countries in the Middle East. Owing to these fruitful relations, none of the Persian Gulf countries imposed sanctions against China after the Tiananmen incident in 1989. In recent years, these countries have also become important customers for Chinese manufactured goods, and some of them continue to buy Chinese weapons. Moreover, due to the outrage that US activities in Iraq have caused in the region, China's political influence in the Middle East has been increasing since 2003.<sup>158</sup> As a result of its growing oil imports and its ever closer relations with oil-producing countries in the Persian Gulf region, China may possibly fulfil the economic function of the US in this region in a few years.<sup>159</sup>

Indeed, China's activities have developed into a decisive factor in the world's oil business. Undeniably, international energy relations are increasingly becoming politicised as a result of China's recent unscrupulous approach to energy-related agreements with oil and gas suppliers.<sup>160</sup>

As a result of China's deepening integration into the world economy, no foreign policy issue falls easily into a discrete functional, institutional or regional category. Foreign policy is therefore of interest to almost every actor in the Chinese policy-making system, especially to those who deal with China's energy security. Accordingly, diplomats are increasingly involved in activities that concern China's oil supply security, for instance in planning important investments of Chinese oil companies, as seen in CNPC's successful bids for oil projects in Venezuela, Sudan and Kazakhstan. Moreover, former ambassadors to oil-producing countries are the main proponents of an active oil diplomacy.<sup>161</sup>

The focus of China's diplomacy is to facilitate the country's economic development. Needless to say, this is especially true with regard to China's relations with oil-exporting states. Chinese energy strategists initially focussed on some 16 countries where new initiatives were considered, and also aimed at establishing relations with countries under US unilateral oil sanctions. Consequently, concerns about oil security are increasingly influencing China's diplomatic and strategic calculations.<sup>162</sup> As old doctrines of self-sufficiency have been replaced by assertive Chinese involvement across the globe, China's activities are nowhere as intense as in the area of energy supplies and energy security.<sup>163</sup> China competes with the US and other developed countries for oil

qi gongying nian zeng jin si cheng" (Saudi king gives a big present to China: the annual amount of oil and gas exports will increase by 40%), *Renmin wang*, 26 January 2006, <http://finance.people.com.cn/GB/42773/4065459.html>.

<sup>154</sup> Downs, Erica S., 2004, p. 38.

<sup>155</sup> Hirn, Wolfgang, *Herausforderung China: Wie der chinesische Aufstieg unser Leben verändert* (The China challenge: How China's rise is changing our way of life). Frankfurt am Main: S. Fischer 2005, p. 166; "Shiyou dazhan hou kan Zhongguo shiyou lian," 2005; Calabrese, John, "Saudi Arabia and China Extend Ties Beyond Oil," 2005.

<sup>156</sup> Hirn, Wolfgang, 2005, p. 166.

<sup>157</sup> Calabrese, John, "Saudi Arabia and China Extend Ties Beyond Oil," 2005.

<sup>158</sup> Möller, Kay, *Die Außenpolitik der Volksrepublik China 1949-2004: Eine Einführung* (The foreign policy of the People's Republic of China 1949-2004: An introduction). Wiesbaden: VS Verlag für Sozialwissenschaften, 2005, pp. 212-8.

<sup>159</sup> Shi Dan, 2003, p. 189.

<sup>160</sup> Van der Linde, Coby, "Het China Syndroom" (The China syndrome), *Energie Nederland* 8, no. 4 (2005), p. 8.

<sup>161</sup> Downs, Erica S., 2004, 26, p. 39.

<sup>162</sup> Myers Jaffe, Amy and Steven W. Lewis, Steven W., 2002, 127; Downs, Erica S., 2004, p. 115.

<sup>163</sup> Howell, David, "China's Global Impact Grows," *Alexander's Oil & Gas Connections*, 29 January 2005, <http://www.gasandoil.com/goc/news/nts50883.htm>.

imports as well as for explorations rights all over the world and, as the gap between China's oil demand and its domestic supply is increasing, this competition is becoming fiercer.<sup>164</sup>

China is pursuing a decidedly bilateral approach to energy security.<sup>165</sup> Chinese analysts consider close relationships with major oil-producing states as a means to enhance energy security. The Chinese government hopes that strong ties with oil producers will ensure that these countries continue to sell oil to China during a possible international crisis.<sup>166</sup> As a result, China is eager to further its relations with current and potential suppliers, who often favour Chinese investors above European or US companies because the Chinese enter without political expectations and demands.<sup>167</sup>

China also fosters its ties with its oil suppliers by providing them with arms and weapons technology along with other forms of military assistance. Further, China offers oil-producing countries political and economic benefits in exchange for access to oil.<sup>168</sup> Finally, as the Darfur crisis in Sudan has shown, China willingly uses its rising bargaining power and its permanent seat in the UN Security Council to protect the interests of oil-producing states.<sup>169</sup> Consequently, Persian Gulf oil producers are also increasingly turning toward China for their strategic relationships.<sup>170</sup>

On the one hand, recent history indicates that oil diplomacy may not enhance a country's oil security, at least in terms of protection from oil price hikes. Bilateral approaches to oil security might even cause too much dependency on certain exporting countries.<sup>171</sup> On the other hand, China's activities reflect the concern that US interference is viewed as the primary threat to China's oil security. Accordingly, China's oil-security measures are mainly defensive and designed to minimise the vulnerability of China's oil supply to such interventions.<sup>172</sup> Moreover, judging from their reaction to the sanctions against China in 1989, it is rather unlikely that oil-producing countries will team up with the US and decrease their exports to China as part of a US-led campaign to contain China.

In 1993, China's main suppliers were Indonesia, Oman and Yemen.<sup>173</sup> Initially, China chose Yemen and Oman as suppliers because it was not able to refine large amounts of the lower quality oil supplies that are produced in Iraq, Iran, Saudi Arabia and Kuwait.<sup>174</sup> In recent years, however, Saudi Arabia has become China's main oil supplier, accounting for 14% of China's imports in 2004. Oman, Angola, Iran, Russia, Vietnam and Yemen together supply another 60%, while the remainder comes from a long list of other suppliers.<sup>175</sup>

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<sup>164</sup> Shi Dan, 2003, p. 189.

<sup>165</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 115.

<sup>166</sup> Downs, Erica S., 2004, p. 38.

<sup>167</sup> Forero, Juan, "China Woos Latins in Oil Hunt," 2005.

<sup>168</sup> Chinese arms exports are generally much lower than those of the West and Russia, and its military sales focus on small, conventional-arms transfers. Myer Jaffe, Amy, and Steven W. Lewis, 2002, 128; Klare, Michael, 2004, p. 172.

<sup>169</sup> Hoyos, Carola, "Sudan: China and India Fill Void Left by Rights Campaigners," *Financial Times*, 1 March 2006, p. 3; Forney, Matthew, "China's Quest for Oil," 2004.

<sup>170</sup> Howell, David, "China's Global Impact Grows," 2005.

<sup>171</sup> Downs, Erica S., 2004, p. 39.

<sup>172</sup> Downs, Erica S., 2000, p. 53.

<sup>173</sup> Shi Dan, 2003, p. 187.

<sup>174</sup> China's aged and unsophisticated oil refineries can only handle domestic high-quality waxy crude oil, but not the low-quality heavy oil imported from the Middle East. In order to benefit from large-scale imports from the Middle East, China has to make massive investments in its refining sector; Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence," April 1999.

<sup>175</sup> Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," 2005.

**Table 3.6: China's crude oil suppliers by region as percentage of total supply, 2003-4**

<b>Region top three suppliers</b>	<b>2003</b>	<b>2004</b>
<b>Middle East</b>	<b>50.9</b>	<b>45.4</b>
Saudi Arabia	16.7	14.0
Oman	10.2	13.3
Iran	13.6	10.8
<b>Africa</b>	<b>24.3</b>	<b>28.7</b>
Angola	11.1	13.2
Sudan	6.9	4.7
Congo	3.7	3.9
<b>Europe and Western Hemisphere</b>	<b>9.6</b>	<b>14.3</b>
Russia	5.8	8.8
Norway	1.0	1.6
Brazil	0.1	1.3
<b>Asia Pacific</b>	<b>15.2</b>	<b>11.5</b>
Vietnam	3.8	4.4
Indonesia	3.7	2.8
Malaysia	2.2	1.4

Source: Zweig, David, and Bi Jianhai. "China's Global Hunt for Energy." *Foreign Affairs* 84, no. 5 (2005): 28.

Actually, the lack of adequate refining capacity suitable for heavier Persian Gulf crude oil has become a major issue in China's oil security strategy because it hampers an immediate increase of imports from the Persian Gulf region.<sup>176</sup> In 2000, the amount of Saudi Arabian oil exports to China had already grown 17-fold compared to that in 1995. During the same period, exports from Iran had increased 7.5-fold, and those from Oman 4.3-fold.<sup>177</sup> In 2001, about 60% of China's oil imports originated from the Middle East, compared to 45.4% in 1995.<sup>178</sup>

### 3.3. Threats to China's Oil Supply

#### *The Fear of Dependence*

The difficulties that the Chinese energy sector experienced in the wake of the Sino-Soviet split during the 1960s contributed to the conviction – still prevalent among some Chinese officials – that reliance on oil imports and foreign involvement in China's oil sector are dangerous.<sup>179</sup> China's recent shift from an oil exporter to importer has reinforced such concerns, highlighting the fact that dependence on foreign oil has already become a source of vulnerability that could subject China to unwanted foreign pressures.<sup>180</sup>

From an economic perspective, China faces a greater exposure to oil supply disruptions and price hikes as a result of its growing demand for oil. The consequences of this development became especially obvious during the 2003 Iraq war. The war had a major impact on China's security of oil

<sup>176</sup> EIA, "China," 1 July 2004. <http://www.eia.doe.gov/emeu/cabs/china.html>.

<sup>177</sup> Shi Dan, 2003, p. 187.

<sup>178</sup> Feng Yuewei, 2003, p. 308; Shi Dan, 2003, p. 187.

<sup>179</sup> Downs, Erica S., 2000, p. 11.

<sup>180</sup> *Ibid.*, 12.

supply. It revealed not only the weaknesses of China's energy policy, but also exacerbated already existing problems that are caused by external threats to China's oil supply.<sup>181</sup>

These external threats to China's oil supply are mainly the result of oil-related manoeuvres by the US, Russia, and Japan which have severely hampered China's attempts to improve its access to foreign oil resources and secure undisrupted oil supplies to China.<sup>182</sup> In addition, China's oil supplies from the Middle East are ever more under threat due to the US-led war in Iraq and its growing presence in the region. US involvement in the Middle East is aimed at gaining more and more control of the region's oil resources, which has considerable consequences for China's oil supply.<sup>183</sup> Furthermore, Chinese analysts are convinced that the increased antiterrorism intelligence cooperation between the US and Singapore broadens American control of the Malacca Straits and facilitates the containment of China.<sup>184</sup> As China's oil shipments from the Middle East must pass this sea-lane on their way to South and East China, an increased US presence is enough to unsettle Chinese strategists.<sup>185</sup> Finally, Japan is constantly trying to interfere with Sino-Russian negotiations on energy cooperation.<sup>186</sup>

### *US Interference*

As of the late 1990s, analysts expected that the concern over China's seaborne oil imports would produce an excellent opportunity to improve its relations with the US, and that implicit US strategic guarantees to maintain open access to Asian sea routes for energy trade could give real meaning to China's "strategic partnership" with the US.<sup>187</sup> Efforts to establish such a partnership were made when President Jiang Zemin paid a state visit to the US in late 1997 and President Bill Clinton reciprocated in summer 1998.<sup>188</sup> However, after George W. Bush – who had dubbed China a "strategic competitor" during his election campaign – became US president, it was futile to continue negotiations on any form of partnership. Despite initial Sino-US cooperation in the war on terror, Bush's earlier statements had already set the basic tune for his administration's approach to China.

Since China does not possess the military capabilities to secure the major sea-lanes through which the majority of its oil imports travel, it is in the uncomfortable position of being dependent on the US for the security of its imported oil. Therefore, Chinese analysts view China's growing reliance on imported oil as a vulnerability that could be exploited by the US during a potential economic or political Sino-American conflict.<sup>189</sup>

### *Japan as a Major Regional Competitor*

In an attempt to become less dependent on seaborne oil imports, China has been negotiating over its participation in the development of Russian energy resources, which the Chinese regard as an important source of future energy supplies.<sup>190</sup> However, China faces Japan as its most important regional competitor for Russian oil. In recent years, the competition between Asia's economic giants for oil supplies and access to new resources has become very fierce. As Japan imports about 88% of its oil from the Middle East, finding alternatives to the region has become a top government priority.

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<sup>181</sup> Fan Jianping, and Niu Li, "Yizhan dui shijie ji Zhongguo jingji de yingxiang" (The influence of the Iraq war on the world economy and China's economy) in *Yilake zhanzheng yu Zhongguo jingji* (The Iraq war and China's economy), ed. Shi Guangsheng, Beijing: Zhonghua gongshang lianhe chubanshe, 2003, p. 63.

<sup>182</sup> *Ibid.*

<sup>183</sup> Li Guanghuai, "Yi zhan dui Zhongguo jingji fazhan de yingxiang ji duice jianyi" (The impact of the Iraq war on China's economy and proposals for countermeasures), in *Yilake zhanzheng yu Zhongguo jingji* (The Iraq war and China's economy), ed. Shi Guangsheng, Beijing: Zhonghua gongshang lianhe chubanshe, 2003, p. 111.

<sup>184</sup> *Ibid.*, p. 110.

<sup>185</sup> Fan Jianping, and Niu Li, 2003, p. 63.

<sup>186</sup> *Ibid.*

<sup>187</sup> Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence," 1999.

<sup>188</sup> Shambaugh, David, "Sino-American Strategic Relations: From Partners to Competitors," *Survival* 42, no. 1 (2000), p. 98.

<sup>189</sup> Downs, Erica S., 2004, p. 32.

<sup>190</sup> *Ibid.*, p. 36.

The depth of Japan's energy insecurity was reflected in its aggressive diplomatic offensive to win the East Siberian pipeline deal, despite China's head start.<sup>191</sup>

In early 2003, the Chinese struck a deal with Russia to build an oil pipeline from Angarsk near Lake Baikal to the existing Chinese pipeline network at Daqing, Heilongjiang province, which would have supplied as much as 15% of China's imports.<sup>192</sup> At the same time, however, Japan – offering twice as much as China – also lobbied for a pipeline, which would bypass China and terminate in Perevoznaya near Nakhodka, the nearest Russian port to Japan.<sup>193</sup>

Unfortunately, the Chinese had made the agreement with YUKOS, whose CEO, Mikhail Khodorkovsky, had planned to use the pipeline to China to break the Russian state's pipeline monopoly.<sup>194</sup> China was hit hard by the legal assault on YUKOS, as oil shipments by train were cancelled – until late 2004 YUKOS was the only Russian oil supplier to China – and the YUKOS-led plan to build the Angarsk–Daqing pipeline was stalled because the Russian government deemed the Japan-oriented Taishet–Nakhodka pipeline financially more attractive.<sup>195</sup> Moreover, Russian analysts considered the Angarsk–Daqing pipeline as “extremely unfavourable” for the Russian side because it would deliver oil only to one single market, as the Chinese had refused to extend the pipeline to one of their eastern ports.<sup>196</sup>

### Map 3.1: Proposed pipelines from Siberia to Northeast China and the Pacific



Source: “Russian Oil: King Solomon’s Pipes.” *The Economist*, 5 May 2005, [http://www.economist.com/displaystory.cfm?story\\_id=3943415](http://www.economist.com/displaystory.cfm?story_id=3943415).

Nevertheless, CNPC helped finance the nationalisation of parts of the YUKOS empire and expected to secure long-term oil supplies and realise its former pipeline deal.<sup>197</sup> Subsequently, LUKOIL and ROSNEFT started supplying oil to China.<sup>198</sup> Still, China lost the pipeline deal to Japan when in late

<sup>191</sup> Fackler, Martin, “Japan’s Energy Dilemma,” *Far Eastern Economic Review*, 17 July 2003, p. 11.

<sup>192</sup> Forney, Matthew, “China’s Quest for Oil,” 2004.

<sup>193</sup> “East Asia’s Oil: Your Pipe or Mine?,” *The Economist*, 25 September 2003., [http://www.economist.com/displaystory.cfm?story\\_id=2088846](http://www.economist.com/displaystory.cfm?story_id=2088846).

<sup>194</sup> “Russian Oil: King Solomon’s Pipes,” *The Economist*, 5 May 2005, [http://www.economist.com/displaystory.cfm?story\\_id=3943415](http://www.economist.com/displaystory.cfm?story_id=3943415).

<sup>195</sup> Blagov, Sergei, “China’s Russian Pipe Dream,” *Asia Times Online*, 28 September 2004., [http://www.atimes.com/atimes/Central\\_Asia/FI28Ag01.html](http://www.atimes.com/atimes/Central_Asia/FI28Ag01.html).

<sup>196</sup> Центр стратегических разработок (Centre for strategic studies), “Аналитический доклад о возможных направлениях развития инфраструктуры по транспортировке российской нефти” (Analytical report on the possible directions of the development of the infrastructure for the transport of Russian oil), Moscow, 19 October 2004. [http://www.energypolicy.ru/files/IR-report\[19102004\].pdf](http://www.energypolicy.ru/files/IR-report[19102004].pdf).

<sup>197</sup> “China Had Role in YUKOS Split-up,” *BBC News*, 2 February 2005, <http://news.bbc.co.uk/1/hi/business/4226407.stm>.

<sup>198</sup> “YUKOS to Deliver 250,000 tons of oil to China,” *The Russia Journal*, 28 February 2005, <http://www.russiajournal.com/news/cnews-article.shtml?nd=47543>.

2004 Russia signed an agreement to build a pipeline from Taishet to the Pacific. This loss was a bitter disappointment for Chinese policymakers and diplomats who had been lobbying for the pipeline for 10 years. However, Chinese analysts are confident that the climate for Sino-Russian energy cooperation will become more favourable in the wake of repeated political setbacks in Russia's relations with the West. Already, President Vladimir Putin has assured President Hu Jintao that a stretch of pipeline to China will be built before the pipeline to the Pacific is finished. The construction of the stretch of pipeline from Taishet to Skovorodino near the Chinese border began in April 2006. After the completion of this part of the pipeline in 2008, China will receive two-thirds of the pipeline's annual throughput 30 million tons of oil.<sup>199</sup> Moreover, for the time being, the amount of oil that Rosneft is shipping by train to China is increasing continuously. In 2005, Rosneft already delivered 4.4 million tons of oil and will almost double that amount to about 7.5 million tons in 2006.<sup>200</sup>

Despite the fact that Japan is China's foremost regional competitor for oil supplies, it is not in the position to severely threaten China's oil supply. As a result of China's economic transformation and substantial investments by Japanese corporations in China, the two economies have become very interdependent. Since 2004, Japan's exports to China have surpassed those to the US. Furthermore, Japan relies heavily on coal imports from China.<sup>201</sup> It is also rather unlikely that other countries in the region will team up with Japan against China, because Japan has no political clout in Asia as it is politically irrelevant to the Asian mainland.<sup>202</sup> Moreover, the economic difficulties Japan experienced in the 1990s have boosted China's position relative to other economies in the region.<sup>203</sup> China's regional rise and the changing perceptions that its neighbours have of China have prompted countries along China's periphery to readjust their relations with Beijing. Therefore, many of these countries are already looking to China for regional leadership or, at a minimum, are increasingly taking China's interests and concerns into account in their decision making.<sup>204</sup>

The competition with Japan for oil resources poses an economic threat to China's oil supply that may eventually be mitigated by China's growing economic clout and political means within the Asian context. Furthermore, it is unlikely that Japan will try to interfere with China's oil supplies because of political considerations. Traditionally, East Asian governments have kept political differences and economic cooperation strictly separated. Potential US interference, however, is a political threat which China has to counterbalance with geopolitical manoeuvres.

In short, China's demand for foreign oil supplies will continue to rise in the foreseeable future. The country's assertive oil diplomacy has profound political consequences worldwide. China's oil strategy is the result of a continuing debate conducted by several stakeholders at various levels within the administration. Important oil-related decisions are made at the highest political level. China's state-owned oil companies play a major role in realising the country's oil strategy and have become active players in all major oil-producing regions. Even Saudi Arabia and Russia are keen to supply China with oil. As Japan's economic clout in Asia is declining, potential US interference constitutes the only genuine threat to China's oil security.

<sup>199</sup> "Shiyou dazhan hou kan Zhongguo shiyou lian," 2005; "'Tai Na xian' zhengshi kaigong E jia nengyuan youshi shiya Oumeng" (Taishet-Nakhodka pipeline officially opened: Russia uses energy to pressure the EU), *Zhongguo jingji wang*, 28 April 2006, [http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428\\_6849612.shtml](http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428_6849612.shtml).

<sup>200</sup> "Zhongguo shiyou waijiao 'da tuwei'" (China's oil diplomacy – a big break out of the encirclement), *Renmin wang*, 14 July 2005; Helmer, John, "China to Get First Crack at Russian Oil," *Asia Times Online*, 16 July 2005, <http://www.atimes.com/atimes/China/GG16Ad01.html>; "E shiyou gongsi jiang zengjia dui Hua chukou," *Jingji cankao bao*, 9 February 2006. <http://jjckb.xinhuanet.com/www/Article/200512313197-1.shtml>; "E Tai Na xian shuyouguan yiqi gongcheng san fenzhi er yuanyou shuwang Zhongguo" (During first fase of the Russian Siberian oil pipeline two-thirds of the oil will be shipped to China), *Zhongguo jingji wang – nengyuan*, 28 April 2006, [http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428\\_6848757.shtml](http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428_6848757.shtml).

<sup>201</sup> Cole, Bernard D., 2003, p. 50.

<sup>202</sup> Brzezinski, Zbigniew, "A Geostrategy for Eurasia," *Foreign Affairs* 76, no. 5 (1997), p. 62.

<sup>203</sup> Hale, David, and Lyric Hughes Hale, "China Takes off," *Foreign Affairs* 82, no. 6 (2003), p. 46; Ye Zicheng, 2003, p. 354.

<sup>204</sup> Shambaugh, David, "China Engages Asia: Reshaping the Regional Order," *International Security* 29, no. 3 (Winter 2004/5), p. 65.

# 4

## The Chinese-Kazakh Oil Pipeline

This chapter describes the competition for Central Asia's oil resources and China's energy-related interests in the region. The first section of this chapter introduces the issue of security of oil supply and the need to diversify supplies. In section two, the current state of Central Asia's energy sector is assessed. The last section deals with China's involvement in Kazakhstan's oil sector and assesses the progress of the Chinese-Kazakh pipeline project.

### 4.1. China's Reaction to the Changing Oil Market

#### *The Current Oil Market*

Access to oil is a precondition for economic growth and stability. Currently, net importing countries balance their oil imports with exports of other goods and services along with capital imports, to avoid balance of payments deficits and potential economic instability. Yet the ability of governments to shield their national economies from large oil price fluctuations, which are caused by disruptions in the supply of oil, depends on several factors – i.e., the willingness to invest in the energy sector, the possibility of foreign direct investments in oil-producing countries, the proper functioning of the international capital markets, and the effectiveness of the international oil market mechanism. Hence, international trade and investment policies become increasingly crucial to the development and functioning of the domestic energy markets of developing net oil importers.<sup>205</sup>

According to calculations of the International Energy Agency (IEA), Asian oil import dependency will increase to more than 75% in 2030. A considerable share of this increase will be the result of China's and India's economic transformation. Generally, satisfying the growing demand for oil requires investments in both oil-producing countries and transport infrastructure. While new oil demand must be met, the production capacity of mature oil fields also has to be replaced in order to maintain current supply levels. Given the distribution of current proven oil reserves, future increases in production will have to come from the OPEC countries. Thus far, however, growing demand for oil has not been followed by a steady increase in supply capacity in the OPEC countries. Consequently, the tight oil market of 2004 and 2005 has led to concerns about the ability of these oil-producing countries to match future demand.<sup>206</sup>

According to IEA calculations, only 35% of the current proven oil reserves are accessible to foreign private investors. Additionally, some countries that have opened up for foreign direct investment are unable to meet international investment standards. As a result, the import dependency of major oil-importing countries will not only increase, but will also be concentrated in a few supplying regions. Still, all major consuming countries prefer to diversify their trade dependence to as many oil suppliers as possible in order to retain sufficient access for energy investments.<sup>207</sup>

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<sup>205</sup> Van der Linde, Coby, and Lucia van Geuns, "Security of Supply," 2005.

<sup>206</sup> Ibid.

<sup>207</sup> Ibid.

### *China's Interests*

The 2003 Iraq war and the subsequent oil price increases had a considerable effect on China's economy.<sup>208</sup> In the first four months of 2003, China's oil imports grew by 42.9%, but its payments rose by 110.6% per year, resulting in extra costs of about US\$4 billion.<sup>209</sup> Furthermore, the war caused severe damage to the more than 100 projects with Chinese participation that were underway in the Middle Eastern region at that time, also affecting tens of thousands Chinese contract workers. Moreover, Iraq will not repay the loans China had granted the country in the past. Finally, CNPC will not be able to develop its three Iraqi oil concessions, at least in the near future.<sup>210</sup>

With the country's growing dependence on oil imports, Chinese analysts are afraid that high oil prices could substantially harm China's economic modernisation. First, high oil prices reduce China's export revenues, diminish its economic growth rate, accelerate the inflation rate, and increase China's foreign-currency payments because of its growing oil imports and the necessity to buy oil for its strategic reserves. Second, as an indirect result, production costs rise, hampering China's export-oriented light industry, which in the long run could inflict considerable harm on China's competitiveness. Third, economic decline in other parts of the world reduces demand for Chinese products.<sup>211</sup> Chinese analysts even suspect "the West" of using high oil prices to obstruct China's economic rise and state that the current price levels affect Western economies less severely than they do China's situation.<sup>212</sup>

Thus, as has already been discussed, China has several reasons to diversify its oil supplies, and its oil diplomacy focuses on a number of countermeasures. First, China is trying to reduce its dependency on oil supplies from the volatile and increasingly US-controlled Middle East. Second, the Chinese government is seeking to engage in energy cooperation with countries that are not considered US allies in order to diminish the risk of US interference with supplies from these countries. Third, China is trying to incorporate energy cooperation into its overall bilateral relations with oil producers in order to guarantee undisrupted supplies. Fourth, China is trying to obtain oil from Russia and Central Asia in an attempt to avoid US-controlled sea-lanes and establish a cross-border pipeline. Finally, due to its concerns about the economic consequences of major supply disruptions, the government urges Chinese companies to acquire as many concessions to foreign oil fields as possible in order to ship "Chinese-owned" oil to China.

Such considerations, as well as the economic impact of the Iraq war, led China's President Hu Jintao to preside over the signing of a pipeline deal with Russia's YUKOS and seek to revive its energy cooperation with Kazakhstan within less than a week in the first half of 2003.<sup>213</sup> However, due to the characteristics of the Caspian oil business and geopolitical manoeuvres by other powers in the region, China's energy projects in Central Asia have not been as fruitful as the Chinese had wished.

### *Closer Ties with Caspian Countries*

In an effort to secure energy supplies from the Caspian Sea region, China is extending its bilateral relations with all five riparian states – Russia, Kazakhstan, Turkmenistan, Azerbaijan and Iran. Besides engaging in energy cooperation with Kazakhstan, China has also become more active in other Caspian countries.

<sup>208</sup> According to China's National Statistical Bureau, every US\$10 price increase over the period of one year results in 0.5% less growth of China's GDP. See "Tebie zhenghua: guoji youjia yi lu jingsheng Zhongguo ruhe yingdui" (A special plan: international oil prices increase substantially and how China can respond), *Renmin wang*, 19 October 2004, <http://www.people.com.cn/GB/news/9719/9720/2927617.html>.

<sup>209</sup> Chu Shijia, "Yi zhan dui wo guo jingji maoyi de yingxiang" (The impact of the Iraq war on China's economy and trade), in *Yilake zhanzheng yu Zhongguo jingji* (The Iraq war and China's economy), ed. Shi Guangsheng, Beijing: Zhonghua gongshang lianhe chubanshe, 2003, p. 104.

<sup>210</sup> *Ibid.*, pp. 105-6.

<sup>211</sup> "Tebie zhenghua: guoji youjia yi lu jingsheng Zhongguo ruhe yingdui," 2004.

<sup>212</sup> *Ibid.*

<sup>213</sup> Murphy, David, "Asia's Pipeline Politics," *Far Eastern Economic Review*, 17 July 2003, p. 13.

When Turkmen President Saparmurat Niyazov visited China in April 2006, he offered not only to build a gas pipeline to China, but also invited Chinese energy companies to develop onshore oil fields in his country in exchange for helping to develop several industrial projects.<sup>214</sup> In 2004, China had provided Turkmenistan with a US\$1.8 million grant and US\$3.6 million worth of interest-free loans to purchase equipment for the country's gas industry. Between 1998 and 2000, Turkmenistan's state-owned energy companies received loans of US\$12 million, which were used to buy Chinese drilling rigs and lifting systems.<sup>215</sup> Although there are good prospects for Sino-Turkmen energy cooperation, the transport of the resources to China remains a challenge.

In Azerbaijan, Chinese energy companies are only involved in onshore fields. CNPC has invested US\$800 million in the Kursengi-Garabagly field and has signed further contracts to develop other sites worth an additional US\$120 million. Other agreements have been signed concerning the development of the Pirsaat oil field and the Karamay oil fields.<sup>216</sup> However, China's purchases in Azerbaijan hardly give it a commanding position in the country's energy holdings and do not overcome the difficulty of gaining reliable access to pipelines.<sup>217</sup>

Iran has become one of China's most important oil suppliers in the Middle East. Additionally, Iran constitutes an attractive transit country for Central Asia, especially for exports to East Asian markets. In recent years, economic relations between Iran and Turkmenistan as well as Kazakhstan have been very fruitful, which has opened up the possibility for Iran to export oil and gas, participate in oil swaps, receive transit revenues, and create employment in its oil and gas sector.<sup>218</sup> In the late 1990s, due to the fact that many multinationals that are active in Kazakhstan's western oil fields are barred from any cooperation with Iran by US legislation, the Kazakh government approached Chinese energy corporations with the request to open up this promising export route.<sup>219</sup> China has also been keen to enlist Iran as a partner in the transport of Caspian oil to China. At the moment, China follows the example of Turkmenistan and Kazakhstan in conducting oil swaps. Iran exports oil through the Persian Gulf from its southern fields in exchange for Kazakh or Turkmen oil.<sup>220</sup>

In order to counter US attempts to exclude it from Caspian energy deals, the Iranian government had announced a three-stage plan involving swaps and direct exports to a trans-Iranian route for Kazakh, Azeri, and Turkmen oil. A 392-km long pipeline would link Neka – the nearest Iranian Caspian port – with Tehran to supply the country's heavily populated northern provinces with oil. Oil could then also be transported to Isfahan and Arak through existing pipelines. Through flow reversals of existing pipelines and the construction of missing links, Caspian oil could also directly reach the Persian Gulf.<sup>221</sup>

In accordance with a series of agreements that China and Iran signed in 2002, CNPC delivers Kazakh oil to refineries in northern Iran and ships equal amounts of Iranian crude to China. Moreover, the two countries agreed that Sinopec would upgrade Chinese-built refineries in Iran in order to improve the refining process of the heavier crude coming in from Kazakhstan, and build an oil terminal port in the port of Neka.<sup>222</sup> Currently, Sinopec, Hong Kong-based Federal Asia and CNPC are participating in the construction of a pipeline from Iran's Caspian Sea port of Neka to a refinery near Tehran and other major population centres.<sup>223</sup> In 2004, China and Iran signed further agreements worth US\$100 billion

<sup>214</sup> “Tukumansidan zongtong jiang lai Hua fangwen zhunbei xiang Zhongguo gongying tianran qi” (The Turkmen president to visit China: willing to supply gas to China), *Zhongguo jingji wang*, 31 March 2006, [http://www.ce.cn/cysc/ny/trq/200603/31/t20060331\\_6554610.shtml](http://www.ce.cn/cysc/ny/trq/200603/31/t20060331_6554610.shtml).

<sup>215</sup> Daly, John C. K., “The Dragon's Drive for Caspian Oil,” *China Brief*, 13 May 2004, [http://www.jamestown.org/publications\\_details.php?volume\\_id=395&issue\\_id=2952&article\\_id=236701](http://www.jamestown.org/publications_details.php?volume_id=395&issue_id=2952&article_id=236701).

<sup>216</sup> Daly, John C. K., “The Dragon's Drive for Caspian Oil,” 2004.

<sup>217</sup> Blank, Stephen, “PetroKaz: China's Difficult Search for Central Asian Energy,” *China Brief*, 8 November 2005, [http://www.jamestown.org/publications\\_details.php?volume\\_id=408&issue\\_id=3519&article\\_id=2370441](http://www.jamestown.org/publications_details.php?volume_id=408&issue_id=3519&article_id=2370441).

<sup>218</sup> Amineh, Mehdi P., 2003, pp. 83-5.

<sup>219</sup> Nazar, Naz, Edige Magauin, and Bruce Pannier, “Kazakhstan, Turkmenistan Turn East for Oil Exports,” *Asia Times Online*, 20 April 1999, <http://www.atimes.com/c-asia/AD20Ag01.html>.

<sup>220</sup> Kalicki, Jan H., “Caspian Energy at the Crossroads,” *Foreign Affairs* 80, no. 5 (2001), p. 126.

<sup>221</sup> Dekmejian, R. Hrair; Simonian, Hovann H., 2003, pp. 35 and 38.

<sup>222</sup> Cole, Bernard D., 2003, p. 31.

<sup>223</sup> Klare, Michael, 2004, p. 171; Kalicki, Jan H., 2001, p. 125; Amineh, Mehdi P., 2003, p. 204.

of Chinese investment in Iran's oil and gas exploration, petrochemical and pipeline infrastructure in exchange for the delivery of liquefied natural gas.<sup>224</sup>

The Caspian region is no longer in the grip of the former Soviet-Iranian monopoly. Nowadays, a complex diplomatic and economic infighting surrounds the exploitation of Caspian energy reserves, with newcomers such as China and the US increasingly wrestling behind the scenes to acquire a dominant role.<sup>225</sup>

#### 4.2. The Focus of Interest – Caspian Energy Riches

##### *Access to the Energy Resources of the Caspian Basin*

The prospect of large energy resources found in the region was the primary factor that brought world attention to the Caspian Basin after the end of the Cold War.<sup>226</sup> According to recent calculations, the Caspian region has proven oil reserves of about 47.7 billion barrels or 6.5 billion tonnes.<sup>227</sup> Azerbaijan and Kazakhstan together account for almost half of the regional oil production, reaching 1,613 million b/d in 2004. Some smaller oil fields are also being developed in Turkmenistan and Uzbekistan.<sup>228</sup> Cautious estimates put the number of the Caspian region's annual production at about 3 million b/d by 2010.<sup>229</sup> In 2004, Azerbaijan, Kazakhstan, Uzbekistan and Turkmenistan together produced 1,967 million b/d.<sup>230</sup> Kazakhstan is Central Asia's main oil producer and has proven reserves of 39.6 billion barrels.<sup>231</sup> Its three major oil fields are all located in the west of the country.

Actually, the Caspian region's natural gas resources are even more significant than its oil deposits. The region holds proven reserves of 9.13 trillion cubic metres.<sup>232</sup> Yet governments and energy companies have put greater emphasis on the development of oil-related projects, partly due to the greater investments necessary to exploit gas deposits and the difficulties of getting it to world markets.<sup>233</sup> However, gas is slowly being recognised as the more promising fuel that could prove crucial to the region's long-term development.<sup>234</sup> All oil-producing countries of the Caspian Sea region possess significant reserves of natural gas, especially Kazakhstan with 3.0 trillion, Turkmenistan with 2.9 trillion, and Uzbekistan with 1.86 trillion cubic metres.<sup>235</sup> Thus, except for Kyrgyzstan and Tajikistan, all Central Asian countries have considerable energy resources that could contribute to the economic development of these countries if the necessary infrastructure can be established to transport those resources to international markets.

Currently, 13 separate pipeline projects aim to bring Caspian oil to Turkey, Russia, the Black Sea, Iran, Pakistan and China.<sup>236</sup> The Baku-Tbilisi-Çeyhan (BTC) pipeline, one of the largest projects and probably the most controversial, was completed in May 2005. Led by BP, 11 of the world's largest oil firms participated in the construction of the 1,762-km long pipeline, which will soon pump 1 million b/d of Caspian oil to the Turkish Mediterranean port of Çeyhan. From this port, the crude oil can be

<sup>224</sup> "China to Develop Iran Oil Field," *BBC News*, 1 November 2004, <http://news.bbc.co.uk/1/hi/business/3970855.stm>; Bajpae, Chietigj, "China Fuels Energy Cold War," *Asia Times Online*, 2 March 2005, <http://www.atimes.com/atimes/China/GC02Ad07.html>; Gundzik, Jephraim P., "The Ties that Bind China, Russia, and Iran," *Asia Times Online*, 4 June 2005, <http://www.atimes.com/atimes/China/GF04Ad07.html>.

<sup>225</sup> Daly, John C. K., "The Dragon's Drive for Caspian Oil," 2004.

<sup>226</sup> Dekmejian, R. Hrair; Simonian, Hovann H., 2003, p. 28.

<sup>227</sup> Metric tonnes. BP, "Putting Energy in the Spotlight," 2005.

<sup>228</sup> *Ibid.*; EIA, "The Caspian Sea Region," 10 December 2004, <http://www.eia.doe.gov/emeu/cabs/caspian.html>.

<sup>229</sup> "At-a-glance: Caspian Oil Riches," *BBC News*, 25 May 2005, [http://news.bbc.co.uk/1/shared/spl/hi/pop\\_ups/05/business\\_caspian\\_oil\\_riches/html/2.stm](http://news.bbc.co.uk/1/shared/spl/hi/pop_ups/05/business_caspian_oil_riches/html/2.stm).

<sup>230</sup> BP, "Putting Energy in the Spotlight," 2005 (excluding Russia and Iran).

<sup>231</sup> *Ibid.*

<sup>232</sup> *Ibid.*

<sup>233</sup> EIA, "The Caspian Sea Region," 2004.

<sup>234</sup> "At-a-glance: Caspian Oil Riches," 2005.

<sup>235</sup> Ministry of Energy and Mineral Resources of the Republic of Kazakhstan, "Energy Policy of Kazakhstan," presented at the Clingendael International Energy Programme Energy Roundtable, The Hague, 30 August 2005, [www.clingendael.nl/ciep/events/20050830/20050830\\_ciep\\_shkolnik.pdf](http://www.clingendael.nl/ciep/events/20050830/20050830_ciep_shkolnik.pdf); BP, "Putting Energy in the Spotlight," 2005.

<sup>236</sup> "At-a-glance: Caspian Oil Riches," 2005.

shipped to world markets.<sup>237</sup> From the outset, US officials have urged Kazakhstan to build an oil pipeline beneath the Caspian Sea to the BTC pipeline, so that Kazakh oil can also be transported to European markets.<sup>238</sup>

**Map 4.1: Existing and planned pipelines for transporting Caspian oil to its markets**



Source: EIA. "Azerbaijan Country Analysis Briefs." 24 August 2005, <http://www.eia.doe.gov/emeu/cabs/azerbjan.html>.

Oil companies always want to build the cheapest route to the best market. In the case of Caspian oil, the construction of a pipeline through Iran to the Persian Gulf would be preferable in commercial terms. Since this would significantly increase Iran's influence in the region, the US has favoured alternative routes.<sup>239</sup> Moreover, almost all Western oil-producing consortia in the Caspian region comprise at least one US-based oil company which are barred by US law from undertaking major investments in Iran.<sup>240</sup> The struggle for pipeline routes concerns as much commercial consideration as geopolitical influence.<sup>241</sup> Thus, decisions about where pipelines will run, who will finance them, and who will control them constitute key issues that will determine the political future of the region for decades to come.<sup>242</sup>

Until recently, Russia held an effective monopoly on Caspian oil transportation. Caspian leaders viewed this dependence on Russian pipelines with unease, because it gave Russia the possibility to unilaterally raise tariffs and constrain Caspian exports, or threaten with these actions in order to win political or economic concessions from its neighbours. Thus, the Caspian countries' political autonomy rests on their ability to secure independent access to international energy markets.<sup>243</sup>

The BTC pipeline is the first pipeline that completely bypasses Russian territory. As a result, its completion caused much emotional upset among Russian policymakers. Nevertheless, according to Russian energy analysts the pipeline constitutes no threat to Russia's energy policies from an economic perspective. At the moment, more Caspian oil is shipped through Russia than its pipeline network can handle, forcing Russia to provide for costly alternatives such as shipments by rail and boat. Moreover, Milov stresses that the BTC pipeline was not intended as an overtly anti-Russian

<sup>237</sup> "Caspian Oil Pipeline Set to Open," *BBC News*, 25 May 2005, <http://news.bbc.co.uk/1/hi/business/4577497.stm>.

<sup>238</sup> Klare, Michael, 2004, p. 159.

<sup>239</sup> "Survey on Central Asia – A Caspian Gamble: Pipeline Poker," *The Economist*, 5 February 1998.

[http://www.economist.com/surveys/displayStory.cfm?story\\_id=112340](http://www.economist.com/surveys/displayStory.cfm?story_id=112340); Berthelsen, John, "World Bank Backs Caspian Pipeline," *Asia Times Online*, 6 November 2003. [http://www.atimes.com/atimes/Central\\_Asia/EK06Ag01.html](http://www.atimes.com/atimes/Central_Asia/EK06Ag01.html).

<sup>240</sup> Myers Jaffe, Amy, and Robert A. Manning, "The Myth of the Caspian 'Great Game': The Real Geopolitics of Energy," *Survival* 40, no. 4 (1998/9), p. 116.

<sup>241</sup> "Pipeline Poker," 1998.

<sup>242</sup> Amineh, Mehdi P., 2003, p. 196.

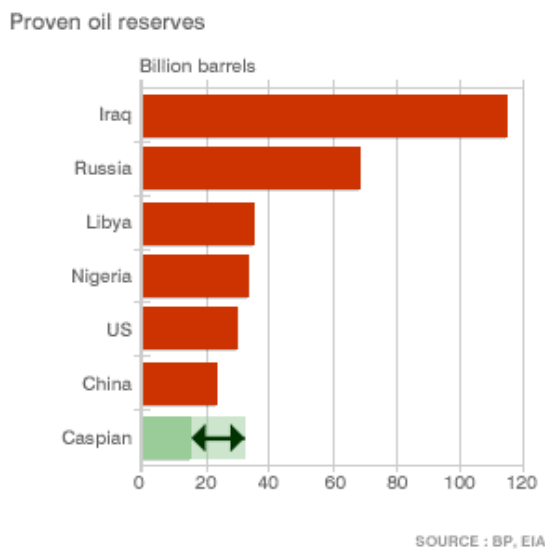
<sup>243</sup> Kalicki, Jan H., 2001, p. 123.

project – LUKOIL, which had been invited to join the consortium, was even pressured by the Russian government to reject any cooperation.<sup>244</sup> As will be discussed later, the BTC pipeline entails more geopolitical considerations than sound economic calculations, and its repercussions are felt in many capitals, even as far as in Beijing.

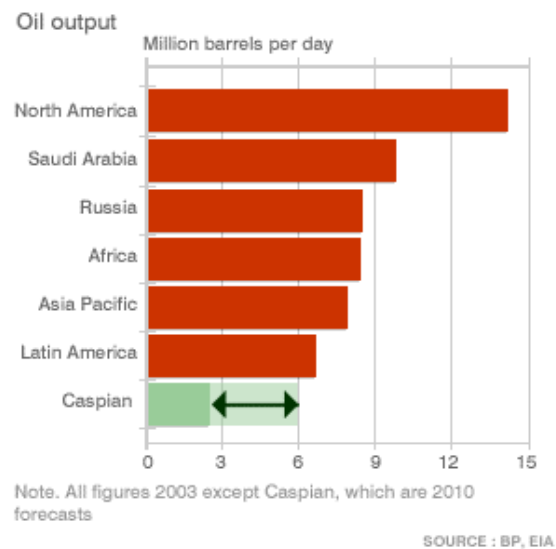
### *Exaggerated Expectations*

In the hyper-confident atmosphere of the early 1990s, the Caspian region was reckoned likely to rival the Middle East. While oil companies and investors relied on the rumoured promise of hidden wealth, no distinction was made between the Caspian region's potential reserves – i.e., resources that might be uncovered after two or three decades of exploitation – and the proven reserves of the Persian Gulf. Regional leaders had used the exaggerated Soviet estimates of the 1970s to attract investment and Western interest.<sup>245</sup> Fuelled by technical difficulties inherent in the process of estimating oil and gas deposits, as well as by the geopolitical and economic motivations of regional and international actors, the controversies over the amount of energy wealth in the Caspian region reached their zenith in 1997, when Caspian oil production was expected by some to reach 3 to 4% of world production by 2010.<sup>246</sup> In 1998, however, US analysts had already concluded that this amount would do little to reduce US dependence on oil supplies from the Persian Gulf region. Moreover, expectations that the Caspian region could become an alternative to Persian Gulf supplies could neither be supported by the region's known reserves nor by the realities of the global energy market.<sup>247</sup> Actually, the Caspian Basin's proven reserves are roughly on par with those of Nigeria, and the region looks likely to produce only about twice the amount of oil as Canada, at least for the present. Thus, producers such as Russia and Saudi Arabia will continue to dwarf it.<sup>248</sup>

**Figure 4.1: Proven oil reserves of the Caspian Basin**



**Figure 4.2: Oil output 2003 (Caspian numbers are estimates for 2010)**



<sup>244</sup> Milov, Vladimir, "Нефтепровод Баку-Джейхан: Лучше дружить" (Baku-Çeyhan pipeline: Better be friends), *Vedomosti*, 2 June 2005, <http://www.energypolicy.ru/news.php?id=1001865>.

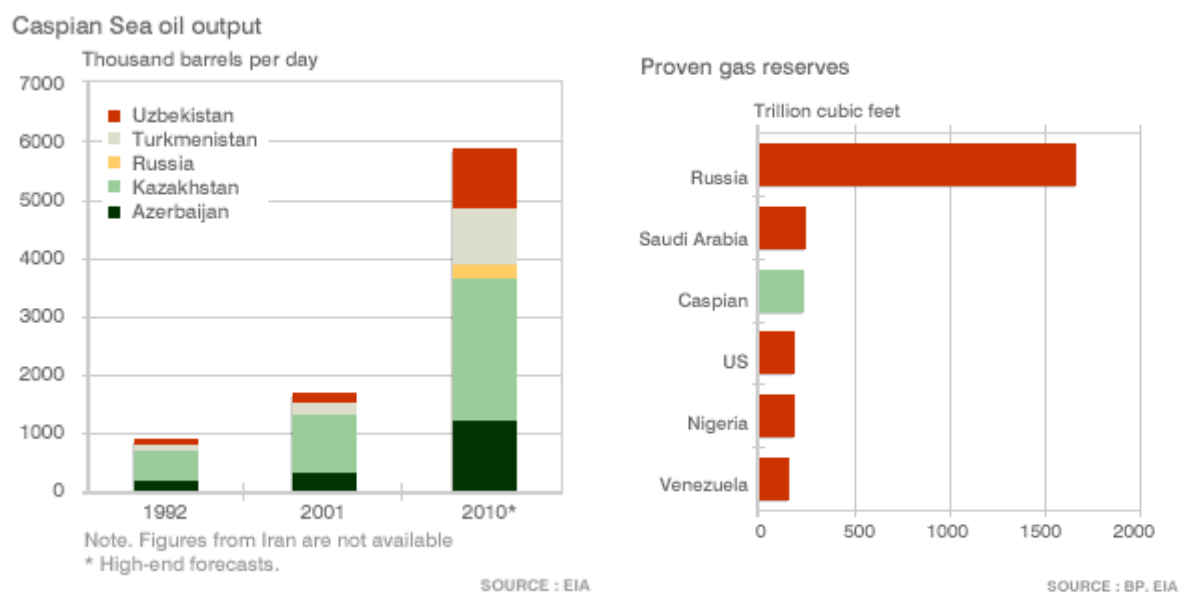
<sup>245</sup> The Kazakh government once claimed its oil potential to be only second to that of Saudi Arabia. See "Survey on Central Asia – A Caspian Gamble," *The Economist*, 5 February 1998, <http://www.economist.com/surveys/showsurvey.cfm?issue=19980207>.

<sup>246</sup> Dekmejian, R. Hrair, and Hovann H. Simonian, Hovann H., 2003, pp. 28-9; Myers Jaffe, Amy, Robert A. Manning, 1998/9, p. 114.

<sup>247</sup> Myers Jaffe, Amy and Robert A. Manning, 1998/9, pp. 114 and 118.

<sup>248</sup> "At-a-glance: Caspian Oil Riches," 2005.

**Figure 4.3: Caspian oil output, 1992 and 2001; Figure 4.4: Proven gas reserves forecasts for 2010**



Source for figure 4.1 to figure 4.4: "At-a-glance: Caspian Oil Riches." *BBC News*, 25 May 2005, <http://news.bbc.co.uk/1/hi/business/4577497.stm>.

Generally, the exploitation of Caspian oil is hampered by complex logistical, technical, economic, social, and geopolitical obstacles. The region's energy deposits lie far from the world's major energy-consuming countries.<sup>249</sup> Thus, the Central Asian countries have to rely on costly pipelines that traverse several neighbouring countries. Yet pipeline transportation entails some peculiar attributes – high investment costs, a high degree of inflexibility, and significant economies of scale.<sup>250</sup> Additionally, the oil drilled in the Caspian fields has a high sulphur content which increases the production, storage and transport costs considerably.<sup>251</sup> Moreover, new exploration is focussed on offshore fields, which requires sophisticated and expensive infrastructures.<sup>252</sup> However, exploitation has often been constrained by insufficient exploratory equipment. Finally, the realisation of pipeline projects is complicated by ethnic and religious conflicts along the proposed routes and political barriers.<sup>253</sup>

Kazakhstan's oil resources were not developed during the Soviet period, due to environmental considerations and complex geological conditions. The entire northern Caspian Sea had been a nature reserve since 1971. After Kazakhstan's independence, the big multinational companies persuaded the Kazakh government to suspend the protective status in order to develop the Kashagan field that is located offshore in the shallow Caspian Sea.<sup>254</sup> Fuelled by the Kazakh government's optimistic expectations that the Kashagan field would contain about 50 billion barrels of oil, the field was initially hailed as the largest oil find since oil was discovered in Alaska's Prudhoe Bay in 1971.<sup>255</sup> Nowadays, the field is considered to hold 12 billion barrels of recoverable crude oil.<sup>256</sup> According to an Agip representative whose company led the initial exploration of the Kashagan field, its exploitation is expected to be very expensive and difficult because of the field's location, being far out in the open sea which is frozen all winter. Moreover, a strong north wind usually decreases the depth of the shallow sea even more, and in winter icebreakers often hit the bottom of the sea. Further, sea

<sup>249</sup> Myers Jaffe, Amy, and Robert A. Manning, 1998/9, p. 114.

<sup>250</sup> Dekmejian, R. Hrair, and Hovann H. Simonian, 2003, p. 34.

<sup>251</sup> *Ibid.*, p. 31.

<sup>252</sup> *Ibid.*, p. 33.

<sup>253</sup> Myers Jaffe, Amy, and Robert A. Manning, 1998/9, pp. 115 and 118.

<sup>254</sup> Environmentalist quoted in Kleveman, Lutz, *The New Great Game*, London: Atlantic Books, 2004, p. 78.

<sup>255</sup> Kleveman, Lutz, 2004, p. 75.

<sup>256</sup> Ministry of Energy and Mineral Resources of the Republic of Kazakhstan, "Energy Policy of Kazakhstan," 2005.

levels periodically rise and fall by more than a meter.<sup>257</sup> The Tengiz field near the town of Atyrau (former Guryev) was discovered in 1979, but Soviet engineers never managed to cope with the oil field's enormous depth and its exceptional pressure. After a fatal blow-out in 1985, the well was ablaze for more than a year.<sup>258</sup> Adding to these geological problems, political disputes and competition for oil concessions create a very harsh business climate.

#### *The Competition for Sufficient Supplies*

At present, it is more than questionable whether the Caspian oil producers will be able to live up to the high expectations. The BTC pipeline is projected to reach 1 million b/d, which would be about 50 million tonnes a year.<sup>259</sup> However, Azerbaijan produced only 318.000 b/d, or 15.7 tonnes of oil, in 2004.<sup>260</sup> Thus, there is a gap of roughly 35 million tonnes a year – approximately 700.000 b/d – between the amount of oil needed to fill the pipeline and Azerbaijan's current production. Moreover, Azerbaijan's production has been stagnating for a couple of years.<sup>261</sup> A sudden increase in production is therefore unlikely.

Undoubtedly, the multi-billion US dollar project would turn into an economic disaster without Kazakhstan's participation. Yet Kazakhstan's current annual production amounts to about 61 million tonnes, or 1.3 million b/d. If Kazakhstan were to jump in and fill the gaps in Azeri oil production, it would have to ship more than half of its annual production across the Caspian Sea.<sup>262</sup> Kazakhstan's oil production is expected to reach 90 million tonnes per year (1.8 million b/d) by 2010.<sup>263</sup> Still, nearly one third of its annual production would have to be earmarked for the BTC pipeline. This could have serious consequences for other pipeline projects, for instance for China's plans that aim at transporting Kazakh oil to China. In fact, the oil pipeline that is being built from western Kazakhstan to Xinjiang will also need about 50 million tonnes per year.<sup>264</sup> Accordingly, Kazakhstan's closer energy cooperation with Azerbaijan leaves many Chinese analysts with a sense of unease.<sup>265</sup> Hence, the competition for Caspian oil resources will continue for a couple of years.

### 4.3. China's Involvement in Kazakhstan's Oil Industry

#### *Chinese Purchases and Pipeline Projects*

Kazakhstan possesses three major oil fields – Karachaganak, Kashagan and Tengiz – with proven reserves of about 2.4 billion barrels, 12 billion barrels, and 6 to 9 billion barrels respectively.<sup>266</sup> The Tengiz oil field could potentially produce 700,000 b/d, or almost 35 millions tonnes annually, by the end of the decade. At present it accounts for approximately 35% of Kazakhstan's production.<sup>267</sup>

Since Kazakhstan is the country with the most significant oil deposits in Central Asia, it has received the largest amount of Chinese investments so far. However, Chinese companies have frequently been foiled in their efforts to buy stakes in Kazakh oil fields. Thus far, they have not secured any major

<sup>257</sup> Kleveman, Lutz, 2004, pp. 76-8; EIA, "Kazakhstan," 4 November 2004, <http://www.eia.doe.gov/emeu/cabs/kazak.html#Kaz-china>.

<sup>258</sup> Kleveman, Lutz, 2004, p. 80.

<sup>259</sup> Centre for strategic studies, "Аналитический доклад о возможных направлениях развития инфраструктуры по транспортировке российской нефти," 2004.

<sup>260</sup> BP, "Putting Energy in the Spotlight," 2005.

<sup>261</sup> Ibid.

<sup>262</sup> Ibid.

<sup>263</sup> Ministry of Energy and Mineral Resources of the Republic of Kazakhstan, "Energy Policy of Kazakhstan," 2005.

<sup>264</sup> Centre for strategic studies, "Аналитический доклад о возможных направлениях развития инфраструктуры по транспортировке российской нефти," 2004.

<sup>265</sup> "Lihai guanxian yu 'Zhong Na guanxian' zheng youyuan yingxiang Zhongguo shiyou zhanlue" (The Baku-Ceyhan pipeline and the 'Chinese-Kazakh pipeline': Competition for oil supplies affects China's oil strategy), *Yahoo! China*, 2 June 2005, <http://cn.news.yahoo.com/050602/1350/2cf3z.html>.

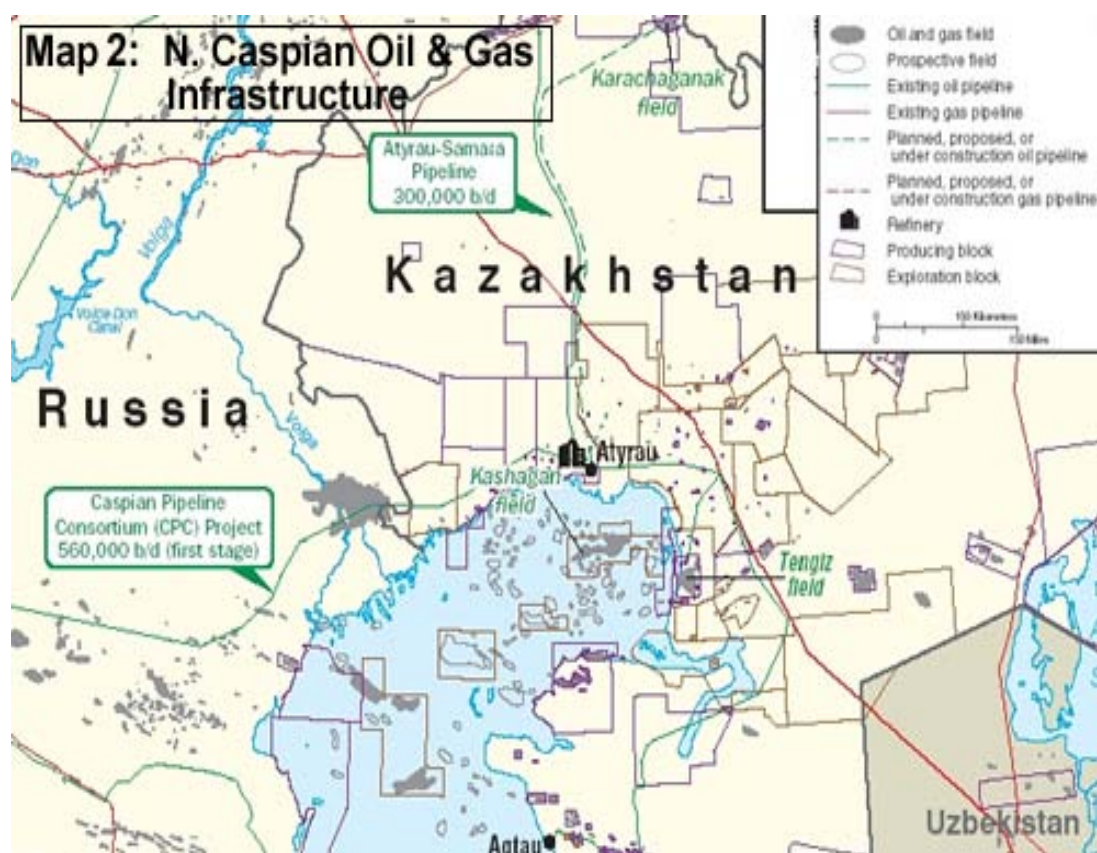
<sup>266</sup> EIA, "The Caspian Sea Region," 2004; Ministry of Energy and Mineral Resources of the Republic of Kazakhstan, "Energy Policy of Kazakhstan," 2005.

<sup>267</sup> EIA, "Kazakhstan," 2004.

drilling rights. Moreover, the fields for which Chinese companies have been able to acquire concessions are already mature, and the companies have even overpaid.<sup>268</sup>

In 1993, China already expressed its interest in Kazakhstan's oil and gas production and also initiated the idea of a pipeline that could transport oil from western Kazakhstan to Xinjiang.<sup>269</sup> Initially, it appeared that Kazakhstan simply used the talks with China as a bargaining chip in the negotiations with other parties. Yet due to the low oil prices in 1997, Kazakh petroleum resources became rather uncompetitive in the eyes of potential investors. Suddenly, the Kazakh government viewed China – the largest market for oil adjacent to Central Asia – as an attractive destination for oil exports. Consequently, Kazakhstan responded positively to China's approach to construct a pipeline to the east, because the Chinese side also appeared to have the funds for a large-scale project for which normal commercial criteria did not seem to apply.<sup>270</sup>

**Map 4.2: The main oil fields in western Kazakhstan**



Source: EIA. "Kazakhstan Country Analysis Brief." 12 August 2005, <http://www.eia.doe.gov/emeu/cabs/kazak.html#oil>.

Since the first energy-related consultations in 1997, China and Kazakhstan have agreed on several concrete projects in the production of oil and its export to China. The first agreement was concluded in June 1997 and provided for CNPC's acquisition of a 60% stake in the Kazakh firm AKTOBEMUNAIGAZ in order to gain access to deposits in the Aqtöbe<sup>271</sup> region. AKTOBEMUNAIGAZ controls three large oil fields in northwestern Kazakhstan – Zhanzhol, Kenkiyak One and Kenkiyak Two – with combined recoverable reserves of about 1 billion barrels.<sup>272</sup>

<sup>268</sup> Forney, Matthew, "China's Quest for Oil," 2004.

<sup>269</sup> Roberts, Sean R., "A 'Land of Borderlands': Implications of Xinjiang's Trans-border Interactions," in *Xinjiang: China's Muslim Boderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 221.

<sup>270</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, p. 396.

<sup>271</sup> Also "Aktobe," formerly known as Aktyubinsk.

<sup>272</sup> Downs, Erica S., 2000, p. 15.

CNPC agreed to service AKTOBEMUNAIGAZ'S debts of US\$71 million, invest US\$10 million in environmental protection measures, guarantee the pensions and housing of about 5,000 employees, and to pay royalties to the government of Kazakhstan. Moreover, CNPC pledged to invest US\$4.6 billion in the firm's development over the next two decades.<sup>273</sup> This was the most significant Chinese-Kazakh deal to date. In bidding for AKTOBEMUNAIGAZ, CNPC beat Texaco, Amoco and a Russian company, because CNPC's bid contained two offers the other companies could not match. First, CNPC agreed to pay up-front a US\$320 million bonus to the cash-strapped Kazakh government. Second, CNPC was willing to conduct a feasibility study on the construction of an oil pipeline from the fields in the Aqtöbe region to western China, which would provide Kazakhstan with a non-Russian export line.<sup>274</sup>

In September 1997, China and Kazakhstan signed a memorandum of understanding to build an eastward pipeline to China. This memorandum was part of a deal regarding CNPC's purchase of concessions in two Kazakh oil fields, Uzen and Tengiz.<sup>275</sup> CNPC was able to outbid Petronas, Amoco and Unocal by paying an up-front bonus of US\$52 million along with an immediate investment of US\$400 million. Yet the key to CNPC's success was its offer to build a pipeline from Uzen to the Aqtöbe fields and its plans to build another pipeline from Uzen to Iran via Turkmenistan.<sup>276</sup>

At that time, the costs of the pipeline that would link western Kazakhstan's oil fields with Xinjiang were estimated at US\$3.5 billion.<sup>277</sup> Few analysts considered the proposed pipeline from Kazakhstan to China to be commercially viable. Therefore, it was regarded as a strategic decision of the Chinese government to get involved in the Caspian oil business.<sup>278</sup> In the late 1990s the continued low level of oil prices brought a dose of realism to China's pipeline dreams. After international investors had begun to consider the Caspian region less attractive and the multinational oil companies had already eliminated all but the most profitable export options, China's State Council also became disinclined to accept the high premium costs connected with the Chinese-Kazakh pipeline project and pressured CNPC to shelve the construction plans.<sup>279</sup> CNPC focussed on the stretches of pipeline within Xinjiang in the late 1990s, while bilateral contracts led to very little construction in Kazakhstan.<sup>280</sup> When Kazakh President Nursultan Nazarbayev promised the US in March 2001 that Kazakhstan would reroute its oil to the BTC pipeline after its completion, the Chinese-Kazakh pipeline project was entirely put on hold, as the Kazakh government was unwilling to guarantee the Chinese side the annual minimum volume of 20 million tonnes of crude oil for the pipeline.<sup>281</sup>

In June 2003, however, President Hu Jintao chose Kazakhstan as the destination for his first bilateral talks abroad. After having attended the SCO summit in Moscow, Hu went to Kazakhstan where a blueprint for bilateral cooperation for the period from 2003 to 2008 was signed. During this visit, President Hu renewed China's commitment to building an oil pipeline from Kazakhstan to Xinjiang, while CNPC increased its stake in AKTOBEMUNAIGAZ to more than 80%.<sup>282</sup>

Up until now, the Chinese oil companies have shipped crude by railway to China. However, the capacity of railway transport is insufficient, mainly because of increasing trade relations and the fact that the railway station at Alashankou is the only border customs point between China and Kazakhstan

<sup>273</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 125; Wiemer, Calla, 2004, p. 185; Cole, Bernard D., 2003, p. 19; Downs, Erica S., 2000, p. 15.

<sup>274</sup> Downs, Erica S., 2000, p. 15.

<sup>275</sup> Klare, Michael, 2004, p. 170.

<sup>276</sup> Downs, Erica S., 2000, p. 16.

<sup>277</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 125.

<sup>278</sup> "Pipeline Poker," 1998.

<sup>279</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, 390; Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 125.

<sup>280</sup> Cole, Bernard D., 2003, 19; "\$2.3bn West China-Kazakhstan Pipeline on the Fast Track," 22 May 1999, <http://www.atimes.com/china/AE22Ad02.html>.

<sup>281</sup> Chung Chien-peng, "The Shanghai Co-operation Organization: China's Changing Influence in Central Asia," *The China Quarterly*, no. 180 (December 2004), p. 1002.

<sup>282</sup> Blagov, Sergei, "Hu Makes His Mark in Central Asia," *Asia Times Online*, 4 June 2003, [http://www.atimes.com/atimes/Central\\_Asia/EF04Ag01.html](http://www.atimes.com/atimes/Central_Asia/EF04Ag01.html); Murphy, David, 2003, p. 16.

for rail transshipment.<sup>283</sup> Therefore, the construction of the pipeline has become a pressing issue for the oil companies.

**Map 4.3: The Chinese-Kazakh pipeline from western Kazakhstan to Alashankou, Xinjiang**



Source: EIA. "Central Asia: Background." September 2005, <http://www.eia.doe.gov/emeu/cabs/Centasia/Background.html>.

In its first stage, the renewed pipeline deal provides for the construction of a 988-km pipeline from Atasu in Central Kazakhstan to Alashankou, a border town near the Alatau pass in the Tian Shan Mountains, which is not far from the town of Karamay (Kelamayi)<sup>284</sup> in the Junggar Basin – one of Xinjiang's oil-producing areas. Later, the pipeline will be extended to the Tengiz oil field in western Kazakhstan. An already existing stretch of pipeline connects this field with Aktau (former Shevchenko) that is located not far from the Kazakh-Turkmen border, which could facilitate a link-up with fields in Turkmenistan.<sup>285</sup>

#### *The Progress of the Projects*

From the outset there have been considerable cost disadvantages for Kazakhstan in delivering its oil to China, because Kazakhstan would earn higher revenues by exporting to the Mediterranean rather than to China by way of the Persian Gulf. The cost disadvantage of shipments via the proposed pipeline is even larger. Therefore, large Chinese investments were necessary to induce Kazakhstan to supply China with its oil over land rather than sell it via Iran or Russia to the Mediterranean market.<sup>286</sup>

Apparently, China's projects in Kazakhstan have also been affected by the same problems that have delayed pipeline construction by western consortiums in Central Asia – i.e., economic and logistical difficulties along with social instability and ethnic unrest.<sup>287</sup> The realisation of the pipeline project from western Kazakhstan to Xinjiang had also been hampered by CNPC's frictions with Kazakh authorities. CNPC representatives even expressed reservations about the possibility of successfully completing the project. Corruption on both sides of the Sino-Kazakh border, disputes within

<sup>283</sup> Daly, John C. K., "The Dragon's Drive for Caspian Oil," 2004.

<sup>284</sup> For place names in Xinjiang, the Uyghur/Turkic name – as it will be most familiar to the reader – is followed by the Chinese name in brackets.

<sup>285</sup> Bajpaee, Chietigj, "China Fuels Energy Cold War," 2005; MacWilliam, Ian, "Kazakhs Plan China Oil Pipeline," *BBC News*, 23 February 2004, <http://news.bbc.co.uk/1/hi/business/3514925.stm>.

<sup>286</sup> Soligo, Ronald, and Amy Jaffe, "China's Growing Energy Dependence," 1999.

<sup>287</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 126.

Kazakhstan's government, difficult natural conditions, and the slow development of Central Asian oil fields are also factors that have caused severe delays.<sup>288</sup>

CNPC's exploration of its oil fields has been a fiasco so far. Moreover, the fields CNPC had acquired cannot produce enough crude to justify the pipeline project's huge expenses.<sup>289</sup> Until the completion of Chinese-Kazakh pipeline, CNPC has to use rail transport to get the crude to China. However, due to the insufficient transport infrastructure, the Chinese were even forced to sell much of the crude at a loss to a Russian refinery.<sup>290</sup>

The first step in the construction of the Chinese-Kazakh pipeline was the completion of a pipeline from the Aqtöbe fields to the oil hub Atyrau in 2003. The first part of the pipeline from Atasu to the Alatau pass will be completed in December 2005.<sup>291</sup> The construction of the last and longest section of the pipeline – from Atasu to the Tengiz field – began in summer 2004.<sup>292</sup> The final stage of the project will entail the construction of a stretch of pipeline from the Kenkiyak fields to the southern fields of Kumkol. After its completion, the pipeline will initially deliver 20 million and later up to 50 million tonnes of oil annually.<sup>293</sup> The amount would represent 16% of China's current oil consumption, but less than 5% by the time the project reaches completion.<sup>294</sup>

However, it is not clear whether there will be enough Kazakh oil to fill the pipeline. Although the pipeline is financed by both Kazakhstan and China, CNPC will be responsible for filling the pipeline from its oilfields in Kazakhstan once it is finished.<sup>295</sup> From the outset, CNPC knew that its Aqtöbe reserves could only provide half of the minimum volume. An attempt by the Chinese to bid for a share held by British Gas in the giant Kashagan field was pre-empted by some of the field's other foreign owners, who also include US interests.<sup>296</sup> Currently, CNPC produces approximately 8 million tonnes annually in western Kazakhstan. LUKOIL and PETROKAZAKHSTAN together produce 10 to 12 million tonnes annually in Kumkol. In August 2005, CNPC acquired the Canadian-listed company PETROKAZAKHSTAN, agreeing to pay US\$4.18 billion, which is US\$55 per share – 21% more than the stock-market price at that time.<sup>297</sup> Thus, CNPC might still be forced to buy oil from Kazakhstan or Russia to fill its pipeline. Crude from Russia can be shipped to the Chinese-Kazakh pipeline via the neglected Omsk-Turkmenabat (former Chardzhou) pipeline. Yet with an initial volume of only 5 million tonnes annually, no large company will feel inclined to carry out the necessary repairs to make the pipeline operational.<sup>298</sup> As a consequence, China will continue to urge its oil companies to buy more concessions to develop Kazakh oil fields in order to secure enough oil to fill the pipeline.<sup>299</sup>

After the crude will finally have reached the border town of Alashankou, it will be shipped via already existing pipelines to Dushanzi in Xinjiang and further to refineries in Lanzhou, Gansu province, and Chengdu, Sichuan province.<sup>300</sup> A 1,200-km long pipeline has already been built from Lanzhou to Chengdu and Chongqing that can ship up to 10 million tonnes per year.<sup>301</sup> The southwestern province

<sup>288</sup> Cole, Bernard D., 2003, p. 20.

<sup>289</sup> "China: Growing up Fast," 2003, p. 21.

<sup>290</sup> Wiemer, Calla, "The Economy of Xinjiang," in *Xinjiang: China's Muslim Borderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 185; "Pipeline Poker," 1998.

<sup>291</sup> "Zhong Mei boyi lihai shiyou: Meiguo jieli zurao Zhong Ha shiyou guandao jianshe" (China and the US gamble for Caspian oil: The US does its utmost to obstruct the construction of the Chinese-Kazakh pipeline), *Yahoo! China*, 3 June 2005. <http://cn.news.yahoo.com/050603/346/2ceq.html>; EIA, "Kazakhstan," 2004.

<sup>292</sup> Bajpaee, Chietigj, "China Fuels Energy Cold War," 2005; MacWilliam, Ian, "Kazakhs Plan China Oil Pipeline," 2004.

<sup>293</sup> Centre for strategic studies, "Аналитический доклад о возможных направлениях развития инфраструктуры по транспортировке российской нефти," 2004.

<sup>294</sup> EIA, "Kazakhstan," 2004; ВР, "Putting Energy in the Spotlight," 2005.

<sup>295</sup> EIA, "Kazakhstan," 2004.

<sup>296</sup> Murphy, David, 2003, p. 13.

<sup>297</sup> "China and India: A Rage for Oil," *BusinessWeek*, 5 September 2005, p. 29; Socor, Vladimir, "Implications of China's Takeover of PetroKazakhstan," *Eurasia Daily Monitor*, 7 September 2005.

[http://www.jamestown.org/publications\\_details.php?volume\\_id=407&&issue\\_id=3449](http://www.jamestown.org/publications_details.php?volume_id=407&&issue_id=3449).

<sup>298</sup> Centre for strategic studies, "Аналитический доклад о возможных направлениях развития инфраструктуры по транспортировке российской нефти," 2004.

<sup>299</sup> CNPC's director general Zheng Chenghu, quoted in Kleveman, Lutz, 2003, p. 114.

<sup>300</sup> "Zhong Mei boyi lihai shiyou," 2005.

<sup>301</sup> "Lanzhou-Chongqing Oil Pipeline Project," *China Oil Web*, 31 October 2000.

[http://www.chinaoilweb.com/asp/content/OGP\\_Project/Project\\_content.asp?Type\\_id=10&Master\\_id=673&Catalog\\_id2=13](http://www.chinaoilweb.com/asp/content/OGP_Project/Project_content.asp?Type_id=10&Master_id=673&Catalog_id2=13).

of Sichuan is with 80 million inhabitants the most populous of China's provinces and hosts several large industrial centres. The contiguous booming municipality of Chongqing – with 31 million inhabitants China's biggest city – and its chemical industry are also a potential market for these oil supplies.

### *Coping with the BTC Threat*

The opening of the BTC pipeline in May 2005 alarmed Chinese policymakers, mainly because of its possible consequences for China's imports via the Chinese-Kazakh pipeline, which were widely reported in the Chinese media. In fact, in 2004 Azerbaijan was only able to export one fifth of the amount of oil needed to operate the pipeline at full capacity. Moreover, in the past few years no major find has been made in Azerbaijan that could fill the huge gap. Therefore, the US once again pressured Kazakhstan to build a pipeline from Aktau to Baku to supply oil to the BTC pipeline. Chinese analysts stated that if the Kazakh side would promise to supply specific amounts, the flow of oil to China could be threatened.<sup>302</sup> Kazakh officials, giving in to US pressure, have already declared that the Chinese must make certain that there is enough oil to ship to China.<sup>303</sup>

Since China has already invested heavily in the Chinese-Kazakh pipeline, insufficient oil supplies would leave the Chinese with considerable financial losses and a long-term effect on China's energy security. Accordingly, Chinese analysts urged the Chinese government to stand prepared to do what is necessary to guard against a defeat like the one China had suffered during the negotiations over the proposed Angarsk-Daqing pipeline a few months earlier.<sup>304</sup>

Despite the uncertainties, the fast progress of the Chinese-Kazakh project alarmed the Russian oil companies ROSNEFT and LUKOIL. They were afraid that there would not be enough demand for Russian oil in China after the completion of the pipeline. Yet these fears were unfounded, as CNPC will still need Russian oil to fill the pipeline. Additionally, until the completion of the Taishet-Nakhodka pipeline, Russia will be able to use the Chinese-Kazakh pipeline to export oil to Asia in order to diversify its export directions. In late 2005, Russia, Kazakhstan, and China agreed upon the delivery of Russian oil to Central Kazakhstan through the Omsk-Turkmenabat pipeline. The Russian oil will be shipped to Central Kazakhstan and then further through the Chinese-Kazakh pipeline to China. All three parties were more than content with this deal.<sup>305</sup>

To sum up, the Caspian Basin region is one of the few major oil-producing regions open to foreign direct investment. In order to lessen their dependency on the Middle East, the major oil-importing countries are keen to diversify their oil supplies. As a result, all major international energy companies have tried to acquire stakes in the Caspian region's energy riches, especially in Kazakhstan. China's decision to build a pipeline to Xinjiang was based on strategic considerations and the need to diversify its oil supplies. Despite various economic and political obstacles, the Chinese leadership is determined to go through with the project and will continue to assist the Chinese oil companies in acquiring oil concessions and investing in energy infrastructure in Central Asia in order to bring more oil to China.

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<sup>302</sup> “Lihai guanxian yu ‘Zhong Ha guanxian,’” 2005.

<sup>303</sup> “Zhong Mei boyi lihai shiyu,” 2005.

<sup>304</sup> Ibid.

<sup>305</sup> “Zhong E jiang ping fen Zhong Ha youguan yunneng Zhong Ha E ge de qi suo” (China and Russia share amount of oil shipped through the Chinese-Kazakh pipeline: China, Kazakhstan, and Russia are content), *Zhongguo nengyuan wang*, 3 December 2005, <http://www.china5e.com/news/oil/200512/200512030141.html>.



# 5

## The Regional Importance of the Pipeline

This chapter describes the political and economic rationale behind China's involvement with the developments in Central Asia. The first section deals with the main features of the Western Development Programme. The second section assesses Xinjiang's economic modernisation and the social consequences of its increasing interaction with both East China and Central Asia. Finally, China's strengthening ties with Kazakhstan will be discussed, together with a short assessment of the importance of the pipeline project for the bilateral relations.

### 5.1. The Western Development Programme

#### *The Fear of Internal Instability*

According to Ye Zicheng, the most crucial requirement for China's rise is the leadership's ability to maintain internal political stability and rapid economic growth. An important question is whether or not the Chinese leadership will make the same mistakes as previous rising powers did when they tried to address external challenges and internal problems. Indeed, internal problems are the most likely endangerment to China's rise. Despite the successes of more than 20 years of economic reform, China faces numerous urgent problems – unemployment in rural and former industrial areas, widespread corruption, social inequality, an insufficient educational level of large parts of the population, the speed of the economic transformation, unbalanced demographic development, environmental pollution, general social discontent, a shortage of energy resources and huge regional disparities in wealth.<sup>306</sup>

Whereas many countries have to deal with regional disparities in wealth, such social and regional inequalities are viewed as a political problem in China. Throughout Chinese history many dynasties have been overthrown by poor peasants because of the rulers' inability to relieve the burdens of the poor. Indeed, the distribution of wealth among China's regions is exceptionally uneven. On average, people living in Shanghai or Beijing earn 10 times more than those in the poorest regions of Central China.<sup>307</sup>

When China launched its economic reform in the late 1970s, the provinces of Guangdong, Fujian, Jiangsu, and Zhejiang were the first to gain from the new economic policy because the central government introduced various preferential policies for coastal provinces, recognising the need to open up to the world economy.<sup>308</sup> Due to easy access to ports and the proximity to Hong Kong, Macau, and Taiwan, export-oriented investors located their production facilities in these coastal areas, which have been enjoying tremendous economic growth rates ever since.

As early as 1979, Deng Xiaoping popularised the concept of a “well-off society,” which then translated into reaching a per capita GDP of US\$800 by the end of the 20th century. Due to China's rapid economic development and a population growth of only 1% a year, Deng and his successors have achieved this goal.<sup>309</sup> Additionally, to cope with the widening gap between the booming coastal areas and the underdeveloped interior provinces in the latter half of the 1980s, Deng formulated the strategy of “the two overall situations” – i.e., during the first stage of economic reform, coastal areas

<sup>306</sup> Ye Zicheng, 2003, pp. 355-6.

<sup>307</sup> Ibid., pp. 382-4.

<sup>308</sup> Naughton, Barry J., “The Western Development Program,” in *Holding China Together: Diversity and National Integration in the Post-Deng Era*, ed. Barry J. Naughton and Dali L. Yang, Cambridge: Cambridge University Press, 2004, p. 256.

<sup>309</sup> Hale, David, and Lyric Hughes Hale, 2003, p. 39.

were to be given support, but once they had reached a sufficient level of development the interior areas would be entitled to receive such support.<sup>310</sup>

**Map 5.1: China – GDP per capita by province, 2005, US\$**



Source: "Survey: China – Coming out." *The Economist*, 23 March 2006, [http://www.economist.com/opinion/displaystory.cfm?story\\_id=5623226](http://www.economist.com/opinion/displaystory.cfm?story_id=5623226).

Raising standards of living is still a goal of China's leadership – achieving a well-off society now means reaching a per capita GDP of US\$2,000 by 2020. Yet economic inequality between rural and urban areas, as well as between the different regions of the vast country, has become an even more urgent topic on the leadership's agenda.<sup>311</sup> Ye Zicheng observes that regional inequality poses a serious danger to China's further development. In the case of widespread social unrest, China's social and economic achievements of the last two decades would be destroyed. Moreover, increased economic disparity could aggravate ethnic divisions and, eventually, threaten China's territorial integrity.<sup>312</sup>

In early 1992, Deng Xiaoping reiterated his two-stage strategy of regional development and marked the turn of the century as the time when the prosperous areas should have achieved a moderately high standard of living, which would allow the leadership to gradually shift the focus of central preferential policies toward the development of the interior. Thus, the future development of the inland regions became an integral part of the CCP's strategy to foster a well-off society over the whole of China by the middle of the 21st century.<sup>313</sup>

<sup>310</sup> Holbig, Heike, "The Emergence of the Campaign to Open up the West: Ideological Formation, Central Decision-making and the Role of the Provinces," *The China Quarterly*, no. 178 (June 2004), p. 336.

<sup>311</sup> Hale, David, and Lyric Hughes Hale, 2003, p. 40.

<sup>312</sup> Ye Zicheng, 2003, pp. 385-6.

<sup>313</sup> Holbig, Heike, 2004, p. 337.

Chinese economists had hoped that at some time the economic situation of the western regions would improve in the wake of sustained growth in the eastern provinces.<sup>314</sup> Yet, the interior remained a supplier of primary goods to the rest of the country.<sup>315</sup> Moreover, regional disparity worsened rapidly during the first half of the 1990s. Chinese analysts found that the intensification of regional differences were even more alarming than in the disintegrating former Yugoslavia. Thus, in mid-1999 President Jiang Zemin, while living up to Deng's promise and acknowledging the seriousness of the situation, announced the Western Development Programme.<sup>316</sup>

### *The Purpose of the Western Development Programme*

The Western Development Programme comprises eleven western provinces and autonomous regions as well as one municipality—i.e. the municipality of Chongqing, the provinces of Yunnan, Guizhou, Sichuan, Shaanxi, Gansu, and Qinghai, as well as Guangxi Zhuang, Ningxia Hui, Xizang (Tibet), Inner Mongolia, and Xinjiang Uygur autonomous regions. The programme is considered the centrepiece of the leadership's effort to strengthen national unity and integration.<sup>317</sup>

The two main objectives of the programme were to dramatically improve the local infrastructure and the natural environment of the regions concerned, while problems surrounding four different policy fields should be incorporated—i.e. environment, energy, market reform, and minority nationalities. In late 1999, the Western Development Programme was declared official state policy, and a group of high-ranking officials led by Prime Minister Zhu Rongji took care of the coordination of the various projects.<sup>318</sup>

Actually, the fact that comparisons were drawn between West China and the former Yugoslavia is crucial to assessing the importance of the Western Development Programme. Confronted with the developments in Yugoslavia as well as in Central Asia after the disintegration of the Soviet Union, the Chinese leadership was deeply concerned about challenges to China's territorial integrity.<sup>319</sup> Additionally, Chinese analysts saw China's WTO membership as a painful challenge to various sectors of the domestic economy and predicted that the interior regions would suffer most because of their backward agriculture and loss-making heavy industries. The imminent threat of industrial breakdown and accelerated poverty of the rural populace led provincial leaders to urge the central government to come up with a viable counter-strategy.<sup>320</sup>

Admittedly, the current leadership is trying to use the Western Development Programme to buy support, ensure stability, and discourage challenges to their transition strategy. In fact, one third of the current members of the Politburo of the CCP – the party's highest policy-making organ – have a personal background in China's West, most prominently the former head of the National Development and Reform Commission and current Vice-Premier Zeng Peiyan, Prime Minister Wen Jiabao, and President Hu Jintao. They not only know the problems of the western regions from personal experiences during previous appointments but their political power is also based on the support of party officials from the interior.<sup>321</sup> Hence, stability and economic development in China's western provinces and regions constitutes a crucial part of the current leadership's approach to China's further modernisation.

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<sup>314</sup> Robert F. Ash correctly notes that it is misleading to cite an east-west divide within China as the exemplar of economic regionalisation. However, "even such a simple vertical division does highlight the disproportionate impact of reform on coastal provinces and suggest the faster pace of foreign trade-oriented growth and modernization in these areas." See Robert F. Ash, "China's Regional Economies and the Asian Region: Building Interdependent Linkages," in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, p. 97.

<sup>315</sup> Goodman, David S. G., "The Campaign to 'Open up the West': National, Provincial-level and Local Perspectives," *The China Quarterly*, no. 178 (June 2004), p. 319.

<sup>316</sup> Holbig, Heike, 2004, p. 341.

<sup>317</sup> Naughton, Barry J., 2004, pp. 253 and 255.

<sup>318</sup> *Ibid.*, pp. 262-3.

<sup>319</sup> Goodman, David, S. G., 2004, p. 329.

<sup>320</sup> Holbig, Heike, 2004, p. 342.

<sup>321</sup> *Ibid.*, pp. 352-4.

## 5.2. Xinjiang – A Strategically Important Region

### *China's "Oil Tank"*

China is the only regional power that has direct power over a part of the broader Central Asian cultural region. After the re-opening of the borders between China's westernmost region Xinjiang<sup>322</sup> and the Central Asian countries, everything that happens in Central Asia immediately affects China. Throughout history, Xinjiang has been a geographical nexus, containing vital land routes to Russia and Central Asia. These routes are crucial communications lines that China has historically tried to control as far from China proper as possible in order to avoid leaving an open flank.<sup>323</sup>

### Map 5.2: China – The Xinjiang Uygur Autonomous Region



Source: "China: The Great Leap West." *The Economist*, 26 August 2004, [http://www.economist.com/displaystory.cfm?story\\_id=3140706](http://www.economist.com/displaystory.cfm?story_id=3140706).

As Xinjiang's wealth of natural resources constitutes its primary economic significance, the sectoral composition of Xinjiang's economy differs markedly from that of China as a whole. Extraction plays the dominant role in the industrial sector, and in 2000 its share accounted for 61% of Xinjiang's production. Currently, Xinjiang produces more than one tenth of both China's crude oil and natural gas. These shares are projected to rise over the coming decade. Three oil basins lie within Xinjiang's boundaries: the Turpan (Tulufan), Tarim (Talimu), and the Junggar (Zhunge'er) Basins.<sup>324</sup> Moreover, its large mineral deposits and the infrastructure projects underway in the extractive industries ensure that this sector will remain the key to Xinjiang's economic future.<sup>325</sup> Despite recent disappointments in not finding new wells, the Chinese leadership still considers Xinjiang's oil resources vital to China's future energy security.<sup>326</sup> In 2005, Xinjiang produced about 24 million tonnes of oil. Accordingly, the region ranks first among all other Chinese regions and provinces.<sup>327</sup> Wealth from oil and gas production has already brought Xinjiang's major cities glittering prosperity.<sup>328</sup>

<sup>322</sup> Xinjiang borders eight countries – Mongolia, Russia, Kazakhstan, Kyrgyzstan, Tajikistan, Afghanistan, Pakistan, and India.

<sup>323</sup> Bedeski, Robert, "Western China: Human Security and National Security," in *China's West Region Development: Domestic Strategies and Global Implications*, ed. Lu Ding and William A. W. Neilson, Singapore: World Scientific, 2004, p. 47.

<sup>324</sup> The three basins are located near the oasis town of Turpan, in the Taklimakan (Takelamagan) Desert, and in an area that stretches south of the city of Altay (Aletai) and east of the city of Karamay.

<sup>325</sup> Wiemer, Calla, 2004, p. 173.

<sup>326</sup> Burles, Mark, 1999, p. 11.

<sup>327</sup> "Xinjiang zhu cheng Zhongguo nengyuan chubei jidi si nian hou zai zao yi ge Daqing" (Xinjiang becomes China's energy base: establishing another Daqing in four years), *Tianshan wang*, 28 December 2005, <http://www.tianshannet.com.cn/GB/channel3/16/200512/28/212879.html>.

<sup>328</sup> Starr, S. Frederick, "Introduction," in *Xinjiang: China's Muslim Borderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 4.

**Table 5.1: Xinjiang's energy production, 2004**

Product	Amount	Increase over 2003 (%)	% of China's production
Coal	22.20 million tonnes	15.0	2.2
Crude oil	22.23 million tonnes	5.1	12.7
Natural gas	5.71 billion cubic metres	14.6	14.0

Source: Zhonghua renmin gongheguo guojia tongjiju (National Bureau of Statistics of China). "Xinjiang Wu'er zizhiqu 2004 nian guomin jingji he shehui fazhan tongji gongbao" (2004 statistical report on the economic and social development of the Xinjiang Uygur Autonomous Region). 17 March 2005, [http://www.stats.gov.cn/tjgb/ndtjgb/dfndtjgb/t20050323\\_402237340.htm](http://www.stats.gov.cn/tjgb/ndtjgb/dfndtjgb/t20050323_402237340.htm); BP, "Putting Energy in the Spotlight," 2005.

Due to the strategic importance of its oil and gas industries and the substantial capital and technological requirements associated with tapping these resources, Xinjiang's economy remains among the most state-centred of all Chinese provinces and regions.<sup>329</sup> Additionally, Xinjiang's development during the reform era was less profound and sweeping than the transformation in East China, for the dominant energy sector was not as amenable to the entry of small businesses as manufacturing was elsewhere.<sup>330</sup> Moreover, Xinjiang's great distance from the coast militates against the large-scale infusion of foreign trade and investment.<sup>331</sup>

The integration objective of the Western Development Programme, which emphasises that modernisation and socio-economic progress will finally lead to the integration of the peripheral economies with East China, was decisive in bringing Xinjiang within the scope of the programme. Ranking 13th among China's 31 provinces in per capita GDP,<sup>332</sup> the region is not poorer than coastal provinces (see Map 4.1). However, violent attacks by separatist Uygurs in the late 1990s raised the concern for the region's stability and qualified it for massive investment in infrastructure projects and economic development in order to prevent uprisings by impoverished ethnic minorities.<sup>333</sup> During the period from 2002 to 2007, the programme provides for investments of US\$12 billion for Xinjiang alone. These investments are mainly directed towards the development of communications, transportation, large-scale industries, and the energy sector.<sup>334</sup> Chinese analysts are convinced that the recent investments in Xinjiang's energy business and transport infrastructure, and, in particular, the construction of the Chinese-Kazakh pipeline, will further transform Xinjiang into China's "oil tank."<sup>335</sup>

Policy initiatives such as the Western Development Programme have had a major impact on the expansion of China's cross-border trade. In recent years, the structure of border exports has shifted markedly from primary commodities towards industrial manufactures.<sup>336</sup> Table 4.2 highlights the importance of the region's western and northern neighbours to its overall foreign merchandise trade.

<sup>329</sup> Wiemer, Calla, 2004, p. 163.

<sup>330</sup> Ibid., p. 173.

<sup>331</sup> Ibid., p. 170.

<sup>332</sup> Xinjiang's GDP amounted to RMB220 billion (US\$27.2 billion) in 2004, 11.1% higher than the year before; its industrial production grew by 14.5%. See Zhonghua renmin gongheguo guojia tongjiju (National Bureau of Statistics of China), "Xinjiang Weiwu'er zizhi qu 2004 nian guomin jingji he shehui fazhan tongji gongbao" (2004 statistical report on the economic and social development of the Xinjiang Uygur Autonomous Region), 17 March 2005, [http://www.stats.gov.cn/tjgb/ndtjgb/dfndtjgb/t20050323\\_402237340.htm](http://www.stats.gov.cn/tjgb/ndtjgb/dfndtjgb/t20050323_402237340.htm).

<sup>333</sup> Goodman, David, S. G., 2004, p. 319.

<sup>334</sup> Starr, S. Frederick, 2004, p. 10.

<sup>335</sup> "Tebie zhenghua: guoji youjia yi lu jingsheng Zhongguo ruhe yingdui," 2004.

<sup>336</sup> Ash, Robert F., 2005, pp. 102 and 105.

**Table 5.2: Xinjiang's exports and imports, 1998-2004**

Year	1998	2000	2001	2002	2003	2004
<b>Export</b> (million) RMB	808	1,204	668	1,308	2,542	3,047
US\$	101	150	83	163	317	380
<b>Import</b> (million) RMB	724	1,060	1,103	1,383	2,230	2,589
US\$	90	132	138	173	279	323

Source: Xinjiang Weiwu'er zizhi qu renmin zhengfu (The government of Xinjiang Uygur autonomous region), "Xinjiang Weiwu'er zizhi qu 2004 nian guomin jingji he shehui fazhan tongji gongbao" (2004 statistical report on the economic and social development of the Xinjiang Uygur Autonomous Region). 17 March 2005, [http://www.xinjiang.gov.cn/1\\$001/1\\$001\\$003/27.jsp?articleid=2005-3-17-0028](http://www.xinjiang.gov.cn/1$001/1$001$003/27.jsp?articleid=2005-3-17-0028).

**Table 5.3: Value and direction/origin of Xinjiang's exports and imports, 2002**

Export/imports by region	Total exports <b>from Xinjiang</b> 1,308 Total imports <b>to Xinjiang</b> 1,383				
Five main export destinations	Kazakhstan	Kyrgyzstan	Azerbaijan	Italy	USA
Value (US\$ million)	442.0	99.5	86.3	79.7	76.0
Share of total exports from Xinjiang	33.8 %	7.6 %	6.6 %	6.1 %	5.8 %
Five main points of import origin	Kazakhstan	Russia	Kyrgyzstan	USA	Germany
Value (US\$ million)	923.6	168.2	54.4	49.8	35.6
Share of total imports to Xinjiang	66.8%	12.2%	3.9%	3.6%	2.6%

Source: Robert F. Ash, "China's Regional Economies and the Asian Region Building Interdependent Linkages," in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh (Berkeley, CA: University of California Press, 2005), pp. 115, 119.

From 1990 to 2002, Xinjiang's foreign trade grew by 18.3% annually. In 2004, Xinjiang's total exports amounted to RMB 3,047 million (US\$380 million) and total imports to RMB 2,589 million (US\$323 million), while cross-border trade made up roughly 73% of all exports (RMB 2,238 million) and 57% of all imports (RMB 1,471 million).<sup>337</sup> Further, it is noteworthy that the structure of border exports has begun to shift from primary goods to industrial manufactures.<sup>338</sup> In general, as the development of cross-border trade relations show, Central Asia is becoming more important for Xinjiang, while its neighbouring countries profit from the investment boom that was initiated by the Western Development Programme.

#### *Xinjiang's Socio-economic Characteristics*

Xinjiang has a population of 19.63 million, roughly 1.5 % of China's total population.<sup>339</sup> About 9 million Turkic people live there, with the Uygurs being the largest group, while approximately 9 million Han Chinese settle the region.<sup>340</sup> Since the 1759 conquest of the territory by the Manchu rulers

<sup>337</sup> Xinjiang Weiwu'er zizhi qu renmin zhengfu (The government of Xinjiang Uygur autonomous region), "Xinjiang Weiwu'er zizhi qu 2004 nian guomin jingji he shehui fazhan tongji gongbao" (2004 statistical report on the economic and social development of the Xinjiang Uygur Autonomous Region). 17 March 2005, [http://www.xinjiang.gov.cn/1\\$001/1\\$001\\$003/27.jsp?articleid=2005-3-17-0028](http://www.xinjiang.gov.cn/1$001/1$001$003/27.jsp?articleid=2005-3-17-0028).

<sup>338</sup> Ibid.

<sup>339</sup> Ibid.

<sup>340</sup> Sullivan, Stephen, "Uzbekistan: Implications for China, Xinjiang," *Asia Times Online*, 3 April 2004, <http://www.atimes.com/atimes/China/FD03Ad05.html>.

of the Qing dynasty that governed China from 1644 to 1911,<sup>341</sup> migration of Han Chinese to the region, which was mostly inhabited by Turkic Muslims, has been actively promoted by all successive governments until the 1970s. Nowadays, impoverished Han peasants from Central China set out for Xinjiang in search for a better life. Due to this continued migration, the Han Chinese population in Xinjiang is rising twice as quickly as the Uyghur population.<sup>342</sup> These movements, however, are not deliberately encouraged by the central government. Beijing is barely in control of the situation, as most migrants are lured to Xinjiang by Han Chinese contractors or go there to start their own businesses.<sup>343</sup>

Indeed, big cities like Kashgar (Kashi) – the major city in the area which the Uyghurs consider their heartland – and the region’s capital Ürümqi (Wulumuqi) increasingly resemble eastern Chinese boomtowns like Shanghai and Shenzhen. Han Chinese businesses are mushrooming, often aided by local officials when competing with Uyghur firms.<sup>344</sup> Consequently, Xinjiang’s modernisation bears a strong Chinese cast.<sup>345</sup> Unemployment in Xinjiang is more severe than elsewhere in China, and there exists a strong pattern of disparity related to ethnicity. In general, Han Chinese live in economically developed areas, while Turkic people dwell in poorer rural areas.<sup>346</sup> Hence, with the continued immigration of thousands of impoverished Han Chinese, tensions seem inevitable.<sup>347</sup> However, the intent of Beijing’s policies towards Xinjiang is not crudely repressive; the prime motive of the central government’s policies is the drive for social and economic transformation, and not the more narrow concerns that are specific to Xinjiang. Nevertheless, as in many other regions of the vast country, rapid modernisation brings about unexpected and unintended consequences.<sup>348</sup>

### Map 5.3: The Xinjiang Uyghur Autonomous Region – Major cities



Source: “China’s Rebellious Province.” *The Economist*, 21 August 1997, [http://www.economist.com/displaystory.cfm?story\\_id=154551](http://www.economist.com/displaystory.cfm?story_id=154551).

Most minority groups in Xinjiang remain relatively submissive to Beijing’s authority. Yet some elements within the Uyghur population have engaged in violent opposition to Chinese rule and have been waging a campaign of sporadic violence against Han Chinese since the 1980s. They mainly engage in activities such as planting bombs, killing police and soldiers, and robbing banks in order to purchase weapons. Since 1989, anti-Chinese riots have occurred in Ürümqi as well as in major trading centres such as Kashgar and Gulja (Yining), which left several people dead and were followed by a

<sup>341</sup> Until the 18th century no Chinese dynasty had continuously controlled for any length of time or governed in any thoroughgoing way the entire territory that is modern Xinjiang. The Qing rulers established a more permanent regime, ensuring the continued presence of China-based powers in the region. See Millward, James A., and Peter C. Perdue, “Political and Cultural History of the Xinjiang Region through the Late Nineteenth Century,” in *Xinjiang: China’s Muslim Borderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 48.

<sup>342</sup> Starr, S. Frederick, 2004, p. 17; “China: The Great Leap West,” *The Economist*, 28 August 2004, p. 50.

<sup>343</sup> Starr, S. Frederick, 2004, p. 19.

<sup>344</sup> “China: The Great Leap West,” *The Economist*, 28 August 2004, p. 50.

<sup>345</sup> Starr, S. Frederick, 2004, p. 11.

<sup>346</sup> Wiemer, Calla, 2004, p. 177.

<sup>347</sup> Starr, S. Frederick, 2004, p. 10 and 17.

<sup>348</sup> *Ibid.*, p. 19.

harsh crackdown by Chinese authorities and sporadic reprisals by Uygur militants. In fact, violent attacks in Xinjiang significantly increased after the signing of the five-partite treaty between the Central Asian countries and China in April 1996, which delimited their common borders and also included protocols that all parties to the treaty would neither harbour nor support separatist groups originating from other party states.<sup>349</sup> Undoubtedly, the most serious incident from the Chinese leadership's perspective was a bomb attack in Beijing in 1997 that injured about 30 people and which was claimed by a militant group based in the former Kazakh capital of Almaty.<sup>350</sup>

The most recent experiences of civil-war-like scenarios date back to the Cultural Revolution (1966-76). In 1969, struggles between different factions drowned Xinjiang in military chaos that even threatened the area around the Lake of Lop Nor (Luobu)<sup>351</sup> where at that time the first Chinese nuclear bomb was tested. There was a real danger of full-scale rebellion as well as direct interference by the Soviet Union.<sup>352</sup>

Dissatisfaction with current social and economic developments, alongside the revival of Islam in Central Asia, Turkic secularism, as well as the rise of Uygur identity as reaction to the influx of Han Chinese, has created a volatile mix. Small-scale clashes between militant Uygurs and police erupt in Xinjiang's western cities nearly every day.<sup>353</sup> Yet the tragedy of the extraordinary factionalism of the period 1911-49, when Xinjiang was governed by several warlords and plagued by ethnic riots that caused a large-scale loss of lives and the depletion of the region's resources, still lives in popular memory as a deep-seated fear of social disorder that helps to keep the region together.<sup>354</sup>

In 1996, provincial party leaders acknowledged the seriousness of the threat to stability in Xinjiang and called for more efforts to reduce the appeal of secessionism and religious extremism. They deemed greater economic development in Xinjiang as being vital to effectively addressing these problems. Improving the living standards of all nationalities was considered the most important basis for maintaining Xinjiang's stability.<sup>355</sup>

Since the launch of economic reform in 1979, Xinjiang has been experiencing rapid economic development. Until the opening of its western borders in 1987, however, Xinjiang's trade was largely oriented toward the eastern provinces. Nevertheless, the region was able to renew its traditional trade and exchange links with the rest of Central Asia during the 1990s.<sup>356</sup> In recent years, trade with Central Asia has been one of the main engines for economic growth in Xinjiang, which benefits greatly from serving as a transportation and distribution hub, especially for imports of oil and other raw materials. Therefore, the Chinese leadership is convinced that a prosperous and stable Central Asia would be the best thing possible for Xinjiang's economic development and stability.<sup>357</sup>

Since China's population includes about 20 million Muslims,<sup>358</sup> Beijing cannot afford to mishandle its domestic Muslim problems. China would run the serious risk of alienating states that directly control China's oil supply. Thus, unrest in Xinjiang could readily lead to a decline in outside oil supply.<sup>359</sup> Actually, in 1998 Sheikh Abdulaziz bin Baz, the former Grand Mufti of Saudi Arabia, proclaimed that Saudi Arabia had a moral obligation to help their "Chinese Muslim brothers," creating internal pressure on the Saudi government to support the Chinese Muslim populations financially and

<sup>349</sup> Brill Olcott, Martha, "Russian-Chinese Relations and Central Asia," in *Rapprochement or Rivalry?: Russia-China Relations in a Changing Asia*, ed. Sherman W. Garnett, Washington, DC: Carnegie Endowment for International Peace, 2000, p. 383; Gladney, Dru C., "The Chinese Program of Development and Control, 1978-2001," in *Xinjiang: China's Muslim Borderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 109.

<sup>350</sup> Chung Chien-peng, 2004, p. 999; Burles, Mark, 1999, pp. 9-10.

<sup>351</sup> Lop Nor, located in the eastern Tarim Basin, is China's sole nuclear and missile test range.

<sup>352</sup> Millward, James A., and Nabijan Tursun, "Political History and Strategies of Control, pp. 1884-1978," in *Xinjiang: China's Muslim Borderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 95.

<sup>353</sup> "China: The Great Leap West," 2004, p. 50.

<sup>354</sup> Gladney, Dru C., 2004, p. 104.

<sup>355</sup> Burles, Mark, 1999, p. 14.

<sup>356</sup> Wiemer, Calla, 2004, p. 170.

<sup>357</sup> Tang Shiping, "Economic Integration in Central Asia," *Asian Survey* 40, no. 2 (2000), p. 367.

<sup>358</sup> The majority of China's Muslims are ethnic Chinese (Hui). Hui communities can be found in all provinces, regions, and big cities.

<sup>359</sup> Gladney, Dru C., 2004, p. 115.

diplomatically. Yet the Saudi government has been cautious to support the Uygurs out of concern for its improving relations with China.<sup>360</sup> China on its part has sought to respond rapidly and decisively to any domestic ethnic unrest that has the potential to constrain its actions on the international scene, especially if important economic interests are concerned.<sup>361</sup> Hence, Xinjiang's well-being is closely linked with China's foreign policy in many areas as well as with China's economic survival, and it will continue to be so in the foreseeable future.<sup>362</sup>

### 5.3. The Sino-Kazakh Strategic Partnership

#### *Strengthening Bilateral Ties*

Since its independence, Kazakhstan has emerged as China's most important Central Asian neighbour. Kazakhstan's sheer size – stretching from the northern coastline of the Caspian Sea to the Tian Shan Mountains – along with the length of its border with China, the substantial number of Uygurs living in the country, and its considerable oil resources have provided China with a strong incentive to build an effective working relationship.<sup>363</sup>

The prospect of Kazakhstan supplying oil to the BTC pipeline was treated by the Chinese leadership as a matter of great urgency. During his state visit to Kazakhstan in July 2005, President Hu Jintao declared that Chinese-Kazakh relations had already reached a new stage and could be called a “strategic partnership.” Subsequently, Hu Jintao and Nursultan Nazarbayev signed a joint communiqué on the establishment of the strategic partnership between both countries “in order to foster the good-neighbourly, friendly and mutually beneficial cooperation and to take into consideration the profound changes of the regional and international situation.”<sup>364</sup>

Needless to say, the communiqué also called for increased cooperation in energy-related matters. Both parties agreed that they “will with all their strength provide for the necessary conditions to ensure that the Atasu-Alashankou pipeline will be operational on time.”<sup>365</sup> However, the agreed partnership will go far beyond energy cooperation, as it also entails issues such as trade, transport, science, culture and security. More favourable conditions should enable entrepreneurs to invest in the border regions. Further, China promised to support Kazakhstan's bid to join the WTO. The communiqué even mentioned plans to build a Kazakh cultural centre in Beijing.<sup>366</sup> Actually, this was a very symbolic gesture of goodwill towards a nation of 15 million people – just the same size as the Chinese capital's population.

Still, only a few months after this bold communiqué, Kazakhstan seemed ready to block CNPC's purchase of PETROKAZAKHSTAN, the biggest takeover deal ever made in the country, leaving “a bitter aftertaste of national humiliation and a new awareness of Kazakhstan's increasingly fragile position in dealing with its oil-thirsty great neighbour.”<sup>367</sup> Some Kazakh analysts warned that by giving priority to Russian and Chinese preferences for oil shipment routes, the country could become vulnerable to economic and political intervention by its two giant neighbours. Furthermore, they viewed Chinese purchases, such as that of PETROKAZAKHSTAN, to be part of China's attempt to gather the oil extracting, processing, and shipment infrastructure of southern Kazakhstan into a single hand. Accordingly, by granting approval to the deal the government would make way for Chinese

<sup>360</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 126.

<sup>361</sup> Gladney, Dru C., 2004, p. 117.

<sup>362</sup> *Ibid.*, p. 116.

<sup>363</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, p. 381.

<sup>364</sup> “Zhong Ha guanyu jianli he fazhan zhanlue huoban guanxi de lianhe shengming (quanwen)” (Joint Chinese-Kazakh communiqué on the establishment and development of a strategic partnership (full text)), *Renmin wang*, 4 July 2005, <http://politics.people.com.cn/GB/1026/3516412.html>.

<sup>365</sup> *Ibid.*

<sup>366</sup> *Ibid.*

<sup>367</sup> Yermukanov, Marat, “Astana May Sacrifice National Interests to Satisfy China Oil Deal,” *Eurasia Daily Monitor*, 7 September 2005, [http://www.jamestown.org/publications\\_details.php?volume\\_id=407&issue\\_id=3449&article\\_id=237018](http://www.jamestown.org/publications_details.php?volume_id=407&issue_id=3449&article_id=237018).

dominance in the region at a time when other oil-producing countries have refrained from selling their assets to Chinese companies.<sup>368</sup>

On the other hand, Kazakhs gain a lot from economic cooperation with China. Working conditions for local staff are better in Chinese corporations and many Kazakhs have made a fortune by dealing with the Chinese.<sup>369</sup> In fact, Kazakhstan simply cannot ignore its huge, booming neighbour. The country is, slowly but surely, being drawn into the Chinese economic and political orbit. Nonetheless, Rumer observes that “one must acknowledge that Beijing has thus far conducted itself – at least, to all external appearances – in a very peaceful manner, displaying much caution in relations with its Central Asian neighbours.”<sup>370</sup>

### *The Importance of the Chinese-Kazakh Pipeline*

From the outset, China’s involvement in Central Asia was driven by its geopolitical ambitions and its energy requirements. Nowadays, after substantial economic setbacks and major obstacles to the progress of the pipeline construction, it appears that the continuation of the project can only be justified by strategic considerations. However, as the pipeline will be China’s only cross-border pipeline, it is of strategic importance to the country’s oil security.

The completion of the Chinese-Kazakh pipeline will allow China to import 20 to 50 million tonnes of Kazakh oil annually. In 2004, China imported 308.6 tonnes of oil.<sup>371</sup> Thus, when the pipeline becomes operational, it will account for no more than 6 to 16% of China’s overall oil imports. This percentage will become even lower as Chinese oil imports continue to rise, and it is unlikely that CNPC will be able to produce and acquire enough Caspian oil to reach the maximum amount of 50 million tonnes annually to fill the pipeline.

In 2004, China imported 62.8 million tonnes of crude from the Middle East.<sup>372</sup> Due to its long-term commitments with Saudi Arabia and other oil-producing countries in the Persian Gulf region, it can be expected that imports from the Middle East will increase significantly when more refineries in China are able to process heavier crude. Hence, oil imports from Kazakhstan will not be able to replace imports from the Persian Gulf in any major way.

Initially, the decision to build a pipeline from Central Asia to China was partially based on the desire to secure some of China’s oil supplies in the face of possible US interference. Now, since the deployment of US troops in the region, China will not be able to capitalise on this strategic advantage of oil imports from Central Asia.

However, China has already invested billions of US dollars to develop its Kazakh oil fields and has constructed a vast network of pipelines both in Xinjiang and Kazakhstan, which should facilitate oil imports from CNPC’s western Kazakh oil fields. Therefore, the Chinese government has a vital interest in the completion of the project, in order to cover at least part of the cost by finally shipping oil to China. Consequently, the Chinese oil companies will try to acquire even more oil concessions and oil companies in Central Asia in the foreseeable future so as to ensure enough oil supplies for the Chinese-Kazakh pipeline and to avoid a major financial loss for CNPC and for the Chinese state as its major stakeholder.

From an economic perspective, CNPC could better ship its Kazakh oil to consumers in Europe via existing Russian pipelines and help satisfy China’s energy needs by buying cheaper crude from the Persian Gulf. Yet, the Chinese–Kazakh pipeline strengthens China’s bonds with Kazakhstan and could

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<sup>368</sup> Ibid.

<sup>369</sup> “Kazakhs Gain from China’s Oil Needs,” *BBC News*, 7 March 2005, <http://news.bbc.co.uk/1/hi/world/asia-pacific/4316615.stm>.

<sup>370</sup> Rumer, Boris, “The Search for Stability in Central Asia,” in *Central Asia: A Gathering Storm?*, ed. Boris Rumer, Armonk, NY: M. E. Sharpe, 2002, p. 41.

<sup>371</sup> BP, “Putting Energy in the Spotlight,” 2005.

<sup>372</sup> Ibid.

free it, to some degree, from reliance on the Persian Gulf.<sup>373</sup> Thus, above all else the construction of the pipeline and the joint ventures with Kazakh oil companies serve China's long-term interests of intensive energy cooperation which this strategically important neighbour.

Indeed, Chinese analysts stress the importance of the Chinese-Kazakh pipeline. They are convinced that the fast progress has helped China in dealing with Russia. As Russia's energy companies are also very keen to deal with China, they have sped up the preparations for the Taishet-Nakhodka pipeline. The Chinese-Kazakh pipeline is the first pipeline from Central Asia to China. However, other projects are already being discussed at the moment, such as the Kazakh proposal to build a gas pipeline parallel to the oil pipeline and Turkmenistan's plan to construct a gas pipeline to China.<sup>374</sup> Hence, the success of Sino-Kazakh cooperation opens up the possibility for other Central Asian countries to export their energy resources to a promising new market.

In sum, despite a still favourable international environment, China's strategy to become a great power could be endangered by internal instability. Huge disparities in the distribution of wealth between East and West China, along with the latent discontent of ethnic minorities at the Chinese manner of modernisation could cause widespread unrest. In order to mitigate these internal troubles, the Western Development Programme was launched. Due to strong separatist feelings among its largest ethnic minority and its exposure to outside influences, the situation in Xinjiang is especially volatile. Xinjiang is of strategic importance to China. The central government intends to transform the region into a transportation and distribution hub for energy imports from Central Asia and exports from East China in order to boost Xinjiang's economy and safeguard its stability. The Chinese-Kazakh pipeline is an important part of this plan, but it is only the first of a number of large energy-infrastructure projects that Central Asian countries have proposed so as to profit from China's energy demand.

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<sup>373</sup> Klare, Michael, 2004, p. 170.

<sup>374</sup> "Ha shiyou zhoumo dida Zhongguo: kaiqi wo duoyuan anquan xin gong you shidai" (Kazakh oil to arrive in China this weekend: the beginning of the era of the security of diversified oil supply), *Zhongguo jingji wang*, 28 April 2006, [http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428\\_6856127.shtml](http://www.ce.cn/cysc/ny/shiyou/200604/28/t20060428_6856127.shtml).



# 6

## China's Instruments for Fostering Its Interests in Central Asia

This chapter describes how China influences Central Asia's current affairs in order to secure its oil-related interests and stabilise the region. The first section describes how China and Russia utilise their strategic partnership to stabilise the region. The next section focuses on China's contribution to the establishment and institutionalisation of the Shanghai Cooperation Organisation (SCO) and the importance of this organisation for China's interests in the region. Finally, China's military posture in the region will be examined.

### 6.1. The Strategic Partnership with Russia

#### *The Concept of a Strategic Partnership in China's Foreign Policy*

A strategic partnership in the context of Chinese foreign policy is a particular form of bilateral relations and shows China's special interest in intensive and long-term cooperation with the country concerned. As the current foreign policy approach strives to reassure others of China's peaceful rise and transform China's international standing, the principal strategic focus of China's foreign policy is great-power diplomacy.<sup>375</sup> Accordingly, since 1996 China has been broadening its efforts to establish partnerships with other great powers. In this context, China has been trying to foster stable bilateral relations – including extensive economic cooperation, military-to-military exchanges, and regular summit meetings between top leaders – with these great powers in order to enhance China's attractiveness to other great powers and retain China's flexibility by not decisively aligning with any particular power. These partnerships form an important part of China's attempt to cope with the constraints of US unilateralism in the post-Cold War era and to accelerate the transition to an international system in which the US would no longer be so dominant.<sup>376</sup>

The strategic partnership with Russia – the first and most stable of China's new partnerships – is based on shared international security concerns. In addition, China works to build partnerships with other great powers, such as the EU, that can serve the country's economic modernisation. In this regard, relations with the US are the most important. In 1997, China and the US decided to form a constructive strategic partnership. Despite an optimistic start, worsened bilateral relations and American sensibilities now preclude applying that label.<sup>377</sup>

#### *The Post-Cold War Sino-Russian Rapprochement*

The gradual process of rapprochement between China and the Soviet Union was initiated by Mikhail Gorbachev who, in his 1986 Vladivostok speech, indicated that the Soviet Union was willing to compromise on three of the obstacles to improved relations with the China: the involvement of Soviet troops in Afghanistan, the deployment of Soviet troops in Mongolia, and continued Soviet support for Vietnam. In May 1989, a month after Vietnam had announced that it would withdraw its forces from Cambodia, Mikhail Gorbachev paid a historic visit to Beijing, where he and Deng Xiaoping agreed upon the normalisation of the bilateral relations.<sup>378</sup> In May 1991, China and the Soviet Union had already reached an agreement on the delimitation of 98% of their common border. In October 2004, both countries finally signed the last of three treaties demarcating the more than 4,300-km long border

<sup>375</sup> Goldstein, Avery, 2001, pp. 844 and 846.

<sup>376</sup> Ibid., pp. 846-7.

<sup>377</sup> Ibid., pp. 848-52 and 855.

<sup>378</sup> Burles, Mark, 1999, pp. 5-6.

between Russia and China.<sup>379</sup> Effectively resolving remaining border disputes removed one of the largest potential sources of conflict from the Sino-Russian relationship and allowed China to divert resources to economic construction.<sup>380</sup>

During his visit to Moscow in May 1991, President Jiang Zemin proposed to Russia's leadership far-reaching economic, military, and political cooperation. As a result of the sanctions imposed on China after the 1989 Tiananmen incident, China had mainly relied on Russia for imports of weapons and military equipment. Yet due to Russia's economic downturn, relations with China merely consisted of those weapons exports throughout the 1990s. In order to broaden and institutionalise their relations, both countries agreed in 1996 upon the establishment of a strategic partnership.<sup>381</sup> For the past couple of years, Sino-Russian economic relations have profited from China's rising energy demand. In 2005, the bilateral trade accounted for US\$29.1 billion – an increase of 37.1% from the previous year. China mainly imports oil and electricity from Russia. These imports will continue to grow in years to come.<sup>382</sup> This will help both countries to “normalise” their strategic partnership, as their strategic ties remain incomplete without more interaction in some non-security and non-political areas.<sup>383</sup>

Another major step in further intensifying the bilateral relations was taken when joint military exercises were held in August 2005. This was the first time that the two countries had conducted such exercises since 1958. The agreement to hold military exercises has once again raised the level of the strategic cooperative partnership.<sup>384</sup>

According to Li Jingjie, the Sino-Russian partnership rests on six basic pillars. First, it is based on mutual respect and equality, as neither country has taken advantage of the weaknesses of the other. Second, both countries have joined forces to create a new security system, including peaceful borders and security cooperation. Third, both countries actively cooperate to support the other partner's vested interests and make common cause on the international stage. Fourth, both Russia and China are keen to establish a world of multilateralism that will lead to a new international political and economic order. Within the quickly changing international situation, regular bilateral talks have become a necessity. Accordingly, the institutionalisation of high-level meetings forms the fifth pillar. The smooth development of the relations during the last one and a half decades can be attributed to the consistent support of each administrative level and a channel for regular dialogue between both governments. Therefore, the basic relationship is not likely to change, even if changes should take place in domestic conditions or in the international environment. Finally, the sixth pillar concerns the nature of the partnership. In all official statements, the heads of state stress that it does not constitute an alliance and is not directed against a third country. The partnership has to be seen as “an act of mutual strengthening and self-protection, not an instrument for outside aggression or assertiveness.”<sup>385</sup>

In fact, Chinese analysts describe the Sino-Russian strategic cooperative partnership as a very special relationship among all of China's bilateral relations and regard it as the “most normal relationship” in the more than 300-year long history of contacts between both nations.<sup>386</sup> Still, as Wilson puts it, “[t]he

<sup>379</sup> “Zhong E liang guo bianjie wenti chedi jie jue: zeng jin shuang fang de zheng zhi huxin” (The problem of the borderline between China and Russia is completely solved enhancing mutual political trust), *Renmin wang*, 15 October 2004, <http://www.people.com.cn/GB/tupian/1097/2921433.html>; “Hu Jintao hui jian Eluosi guofang buzhang: Gaodu pingjia liang guo liang jun guanxi” (Hu Jintao meets Russia's ministers of defence: high appraisal of both the bilateral civil and military relations between the two countries), *Renmin wang*, 13 December 2004, <http://www.people.com.cn/GB/shizheng/1024/3051959.html>.

<sup>380</sup> Burles, Mark, 1999, pp. 6 and 8.

<sup>381</sup> Möller, Kay, 2005, pp. 115 and 124.

<sup>382</sup> “Zhuyao jinkou nengyuan 05 nian Zhong E maoyi 291 yi Meiyuan” (Energy is the most import import commodity: the Sino-Russian trade amounts to US\$29.1 billion), *Zhongguo nengyuan wang*, 16 January 2006, <http://www.china5e.com/news/zonghe/200601/200601160325.html>.

<sup>383</sup> Yu Bin, “China and Russia: Normalizing Their Strategic Partnership,” in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, p. 228.

<sup>384</sup> “Zhong E liang jun jiang yu mingnian juxing shouci lianhe jushi yanxi” (Next year the Chinese and Russian militaries will conduct joint military exercises for the first time), *Renmin wang*, 14 December 2004, <http://www.people.com.cn/GB/shizheng/1026/3051981.html>; “Hu Jintao hui jian Eluosi guofang buzhang,” 2004.

<sup>385</sup> Li Lingjie, “From Good Neighbors to Strategic Partners,” in *Rapprochement or Rivalry?: Russia-China Relations in a Changing Asia*, ed. Sherman W. Garnett, Washington, DC: Carnegie Endowment for International Peace, 2000, pp. 91-3.

<sup>386</sup> Ye Zicheng, 2003, p. 303.

impetus to the development of ties between Russia and China did not derive from a shared sense of values and norms, but from an awareness on both sides – sometimes reluctantly arrived at – that a cordial relationship conformed to their national interests.”<sup>387</sup>

### *Common Policies towards Central Asia*

While the collapse of the Soviet Union created the opportunity for China to re-examine its relations with Moscow, the Chinese leadership also had to consider the impact of its evolving ties with the newly independent Central Asian countries on Sino-Russian relations. China is unlikely to jeopardise the Sino-Russian strategic partnership by making too many bold moves to gain uncertain advantages in Central Asia, especially since the possibility of long-term Chinese benefits in the region is not compromised by allowing Russia short-term gains in what the Russians view as their “near abroad” or strategic backyard.<sup>388</sup>

While Russia's policymakers still cherish the dream of restoring Russia's status as a great power that can dominate its geopolitical neighbourhood, Russia's influence in the post-Soviet republics has been further eroding in the past few years due to increasing strains in Russian-Western ties. Moreover, Russia's appeal as an attractive socio-economic model is waning because in 2004 Russia's economic performance was not impressive, despite high revenues from oil exports. Therefore, the countries that emerged from the ruins of the former Soviet Union do not perceive the Russian model to be either particularly attractive or stable. Additionally, the post-Soviet political elites in the newly independent republics, especially in Central Asia, feel that the protection provided by Russia has ceased to be a serious guarantee of their power.<sup>389</sup> Consequently, Russia fears that US-sponsored “colourful revolutions” could further diminish its influence in Central Asia. Accordingly, political processes in the former Soviet republics form a “major foreign policy problem for the Kremlin.”<sup>390</sup> In addition to their strategic importance to Russia, the Central Asian countries owe Russia immense debts.<sup>391</sup> Yet Russia, rather than urging for repayment of debt, wants to preserve its political influence in the region, to avoid the break-up of the post-Soviet military-strategic space and to have an opportunity to use the installations of its infrastructure.<sup>392</sup>

The Chinese leadership is aware of Russia's sensitivity concerning Central Asia. China thus avoids challenging Russia's sphere of influence and respects its political and military role in the region. Actually, during his 1994 tour of Central Asia, Li Peng went to great lengths to deny that China was trying to fill the power vacuum left by Russia.<sup>393</sup> Indeed, as Central Asia is only one of many areas of concern in the context of the Sino-Russian partnership, the level of cooperation in the region will not have a decisive impact on their overall bilateral relationship. Nonetheless, Central Asian affairs can have a powerful influence on the health of the partnership if one or both partners should be forced to act improperly in the region.<sup>394</sup> As apparent from President Vladimir Putin's proposals before the SCO summit in 2005, Russia intends to play a stronger military role in the SCO member states that were previously part of the Soviet Union by establishing a “mechanism of mutual assistance” within the SCO framework. However, in his proposal Putin explicitly acknowledged that Russia would not act

<sup>387</sup> Wilson, Jeanne L. *Strategic Partners: Russian–Chinese Relations in the Post-Soviet Era*. Armonk, NY: M. E. Sharpe, 2004, p. 198.

<sup>388</sup> The Russian term ближнее зарубежье (near abroad) is used to point to the former Soviet republics and indicates a certain attachment to these regions that is still felt by many Russian policymakers, intellectuals, and military officers. Brill Olcott, Martha, 2000, p. 375; Tang Shiping, “Economic Integration in Central Asia,” 2000, pp. 368 and 376.

<sup>389</sup> Torbakov, Igor, “Russian Foreign Policy Experts Debate Strategy for 2005,” *Eurasia Daily Monitor*, 10 January 2005, [http://www.jamestown.org/publications\\_details.php?volume\\_id=407&issue\\_id=3190&article\\_id=2369071](http://www.jamestown.org/publications_details.php?volume_id=407&issue_id=3190&article_id=2369071).

<sup>390</sup> Russian commentators use the term цветная революция, which can be translated both as “colourful revolution” and “flower revolution,” incorporating the whole range of brand names that have been attributed to such developments so far – “purple” for Georgia's revolution, “orange” for Ukraine's, and “tulip” for Kyrgyzstan's. Torbakov, Igor, 2005.

<sup>391</sup> Kyrgyzstan = US\$182 million, Tadshikistan = US\$306 million, Uzbekistan = US\$654 million. See “Долги стран СНГ по кредитам правительства России” (The debts the CIS countries owe to the government of Russia), *Regnum IA*, 12 October 2005. <http://www.regnum.ru/news/526711.html>.

<sup>392</sup> Rumer, Boris, “The Powers in Central Asia,” *Survival* 44, no. 3 (2002), p. 60.

<sup>393</sup> Tang Shiping, “Economic Integration in Central Asia,” 2000, pp. 365 and 367; Möller, Kay, 2005, p. 191.

<sup>394</sup> Tang Shiping, “Economic Integration in Central Asia,” 2000, p. 376.

without China's approval.<sup>395</sup> In general, Chinese analysts regard Russia's role in Central Asia as positive, especially after Russia's reappearance as an important regional player in 2002. Accordingly, the statement President Putin made in October 2003 that the US would only stay in Central Asia temporarily but that Russia would remain there for ever, was given a cautious welcome by the Chinese side.<sup>396</sup>

Before 11 September 2001 there was a convergence between Chinese and Russian interests over common Central Asian threats – i.e., Islamic extremism, drug trafficking, arms smuggling and terrorism.<sup>397</sup> As the countries of Central Asia, Afghanistan and Pakistan constitute Russia's southern flank and form China's western border, the interests of both countries coincide here, above all in the containment of the threat posed by Islamic radicalism and instability as a result of economic decline.<sup>398</sup> Indeed, both Russia and China have a strong interest in the domestic and foreign policy orientation of the states in the region, and they strongly object to US attempts to establish a permanent presence in the region. Therefore, both Beijing and Moscow look favourably on the secular, post-communist states of Central Asia, and see them as more sympathetic to Chinese and Russian perspectives than either Western-linked or Islamic states would be. Hence, internal as well as external factors encourage Russia and China to formulate a coordinated foreign policy approach to Central Asian affairs.<sup>399</sup>

## 6.2. The Shanghai Cooperation Organisation

### *Development*

In October 1992, a joint delegation from Kazakhstan, Kyrgyzstan, Tajikistan and Russia travelled to Beijing to reassure the Chinese of their commitment to the principles on which agreement had been reached between China and the Soviet Union in 1991. This move set the stage for future negotiations. In 1996, a summit was held in Shanghai during which China, Russia, Kazakhstan, Kyrgyzstan and Tajikistan reached the Agreement on Confidence Building in the Military Field along the Border Areas which – according to Russian officials – constitutes nothing less than a quasi non-aggression treaty, and also set the first step toward establishing the SCO.<sup>400</sup>

Further agreements on the demilitarisation of the border regions and on the fight against transnational security threats were reached in Moscow (1997) and in Almaty (1998), mainly concerning issues such as ethnic separatism, religious fundamentalism, international terrorism, arms and drugs trafficking, and other cross-border crimes.<sup>401</sup> Since 1996, the state leaders and foreign ministers of the SCO member states have gathered for annual summits. Nevertheless, after some early successes, further integration and cooperation frequently stalled due to resource shortfalls, lack of common vision, diplomatic quarrels and interstate rivalries.<sup>402</sup> During the fifth summit at Tajikistan's capital of Dushanbe in 2000, President Jiang Zemin suggested transforming the Shanghai Five from a series of ad hoc meetings into a regular and institutionalised mechanism for multilateral cooperation. In June 2001, the Shanghai Five became the Shanghai Cooperation Organisation, and Uzbekistan was granted membership.<sup>403</sup>

<sup>395</sup> “Шанхайский приговор: Судьба цветных революций решится в Астане,” (Shanghai verdict: The fate of the colourful revolutions will be decided in Astana) *Kommersant*, 5 July 2005, <http://www.kommersant.ru/doc.html?DocID=588895&IssueId=23447>.

<sup>396</sup> Zhongguo xiandai guoji guanxi yanjiuyuan, 2004, p. 156.

<sup>397</sup> Tang Shiping, “Economic Integration in Central Asia,” 2000, p. 365.

<sup>398</sup> Rumer, Boris, “The Powers in Central Asia,” 2002, p. 62.

<sup>399</sup> Garver, John W., “China's Influence in Central and South Asia: Is It Increasing?” in *Power Shift: China and Asia's New Dynamics*, ed. David Shambaugh, Berkeley, CA: University of California Press, 2005, p. 211; Wilson, Jeanne L., 2004, p. 59.

<sup>400</sup> Burles, Mark, 1999, p. 6.

<sup>401</sup> Chung Chien-peng, 2004, p. 990.

<sup>402</sup> Oresman, Matthew, “Day of Reckoning for China–Central Asia Group,” *Asia Times Online*, 24 May 2003, [http://www.atimes.com/atimes/Central\\_Asia/EE24Ag02.html](http://www.atimes.com/atimes/Central_Asia/EE24Ag02.html).

<sup>403</sup> Chung Chien-peng, 2004, p. 991.

### *Institutionalisation*

The events following the attacks of 11 September 2001 paralysed the SCO for months. In fact, the US-led military operation in the region as part of the war on terror achieved more of the SCO's goals in five months than the organisation had until then. Actually, both the dramatic demonstration of the efficacy of US military power in Afghanistan and the willingness of the US to provide generously for military cooperation endangered the existence of the SCO.<sup>404</sup> Consequently, many Chinese and Russian analysts feared that the establishment of permanent US bases in Afghanistan, Kyrgyzstan, Tajikistan and Uzbekistan would undermine the need for the SCO and spoil both China's and Russia's political and financial investments.<sup>405</sup> Subsequently, at the summit in St Petersburg in 2002, attempts were made to re-energise the SCO.<sup>406</sup>

After the 2002 SCO summit, China and Russia began to solidify their commitment to Central Asia. The SCO has increasingly focussed on security issues such as cooperation against terrorism, separatism and extremism, while the ministers of defence of the SCO member states have come together on a regular basis. Moreover, the summit in St. Petersburg in 2002 was followed by tough negotiations until the Russians finally won their battle for more explicit and binding language and the Chinese gained the headquarters and the position of the secretary general.<sup>407</sup> At the summit in Moscow in May 2003, the SCO charter was adopted and China's ambassador to Russia, Zhang Deguang, was appointed executive secretary of the organisation. China and Russia agreed to each pay 30% of the organisation's cost, while the Central Asian countries each pay 10%. In 2003 the SCO secretariat was opened in Beijing.<sup>408</sup> During the Tashkent summit in June 2004, the SCO antiterrorism centre was opened.<sup>409</sup> Further, the member states agreed to give the SCO a legal character, which is an important prerequisite for the proper functioning of an international organisation.<sup>410</sup> The current areas of cooperation reach far beyond the initial concerns for security and stability in the region. The SCO nowadays promotes cooperation on commercial, economic, cultural, academic and energy-related issues, as well as transportation, tourism, environmental protection and education.<sup>411</sup>

Since 2005, India, Pakistan, Iran and Mongolia have been invited to participate in the annual meetings of the SCO as official observers. In April 2006 the secretary of the SCO Zhang Deguang even suggested that all observers could become full members of the organisation in the near future.<sup>412</sup>

Undeniably, the development and institutionalisation of the SCO has been a significant step toward improved international relations. The organisation has become an anchor for stability in the region.<sup>413</sup> In fact, for the first time in history, an overarching organisation groups Russia, China, and the Central Asian countries into a multilateral mechanism for regional security and economic cooperation that helps regulate the policy of the two regional powers towards the Central Asian countries.<sup>414</sup>

<sup>404</sup> Garver, John W., 2005, p. 212.

<sup>405</sup> Oresman, Matthew, "Day of Reckoning for China–Central Asia Group," *Asia Times Online*, 24 May 2003, [http://www.atimes.com/atimes/Central\\_Asia/EE24Ag02.html](http://www.atimes.com/atimes/Central_Asia/EE24Ag02.html).

<sup>406</sup> Chung Chien-peng, 2004, p. 994.

<sup>407</sup> Oresman, Matthew, "Day of Reckoning for China–Central Asia Group," 2003.

<sup>408</sup> Möller, Kay, 2005, p. 192; Oresman, Matthew, "Day of Reckoning for China–Central Asia Group," 2003.

<sup>409</sup> "ШОС открыла штаб-квартиру исполкома Региональной антитеррористической структуры Организации" (The SCO has opened the headquarters of the executive committee of the regional antiterrorism body of the organisation), *RIA-Novosti*, 17 June 2004, [http://rian.ru/defense\\_safety/20040617/613614.html](http://rian.ru/defense_safety/20040617/613614.html).

<sup>410</sup> "Саммит ШОС принял декларацию" (The summit of the SCO has adopted a declaration), *RIA-Novosti*, 17 June 2004, <http://rian.ru/politics/20040617/613813.html>; "Shanghai Cooperation Organization auf dem Weg zur wirtschaftlichen Integration" (Shanghai Cooperation Organisation on its way towards economic integration), *China aktuell* 23, no. 9 (2004): 964.

<sup>411</sup> "Shanghai hezuo zuzhi (xiao ziliao)" (The Shanghai cooperation organisation (short introduction)), *Renmin wang*, 1 July 2005, <http://politics.people.com.cn/GB/1026/3511202.html>.

<sup>412</sup> "На саммите ШОС может быть решен вопрос о новых членах Организации" (During the SCO summit decision on new members possible), *RIA-Novosti*, 19 April 2006, <http://www.rian.ru/world/20060413/45781934.html>.

<sup>413</sup> Zhang Yunling, and Tang Shiping, 2005, p. 55.

<sup>414</sup> Chung Chien-peng, 2004, p. 990.

*China's Interests and Its Role within the SCO*

From the beginning, China has been the driving force behind the establishment and further institutionalisation of the organisation. Unsurprisingly, the goals of the SCO resemble China's foreign policy goals in Central Asia. Various agreements guarantee China's sovereignty and territorial integrity, which means that all members recognise the "one-China-policy" and exclude the possibility of establishing diplomatic relations with Taiwan. Moreover, all Central Asian countries have pledged to support China's efforts against Uygur separatists. Recently, economic issues have been included in the scope of the organisation's activities as China aims to improve its trade links with Central Asia and establishing the region as a source of energy supply for China. Chinese experts also helped to set up the SCO antiterrorism centre in Tashkent which was opened in 2004.<sup>415</sup>

The SCO constitutes a manifestation of China's efforts to develop a stable regional environment for economic development in Xinjiang and underlines China's fears of various forces that might assail Xinjiang from beyond its western borders.<sup>416</sup> Further, China has been able to persuade the other member states to include energy relations in the scope of the SCO. Energy-related issues have already become regular topics during the meetings, and during the 2005 summit in Astana, SCO leaders reaffirmed their interest in strengthening energy-related cooperation.<sup>417</sup> China knows that if it intends to remain a prominent player in Central Asia, it has to do so through the broadening and deepening of its economic linkages with the region. Accordingly, in 2004 China offered nearly US\$1 billion for the development of mutual economic relations between the member states.<sup>418</sup> Moreover, China intends to establish a custom union and common market within the context of the SCO. In the coming two decades, the free movement of goods, capital, technology and services between the member states should be accomplished.<sup>419</sup>

China's security concept is based on the so-called five principles of peaceful coexistence: mutual respect for territorial integrity and sovereignty, mutual non-aggression, non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence. This concept can be regarded as a counterweight to the need for a presence of US military forces, US military alliances, and what China sees as US interventionism that manifests itself as anything from verbal criticism to military attack.<sup>420</sup> Accordingly, at the summit in July 2005, SCO secretary-general Zhang Deguang called for non-interference in the internal affairs of sovereign states. Obviously, the SCO intends to rid the region of the US military presence altogether. At the summit, the heads of state of the SCO members concluded that "the active stage of the anti-terror operations in Afghanistan" had already been accomplished and, subsequently, urged the US and NATO to set a deadline by which the coalition in Afghanistan would no longer use the military infrastructure in the SCO countries and remove its troops from the countries.<sup>421</sup>

Chinese analysts have coined China's policy of strategic, political, and economic opening toward Central Asia "new regionalism," which is a product of the post-Cold War era and is based on free trade or a cooperative forum to deal with security, economic development, and changes in the regional environment. This approach seeks to group together countries with different political systems and cultural and religious traditions, chiefly for the purpose of promoting trade and economic development in that region. Thus, "new regionalism" is an open, functional, interest-based cooperation among contiguous states. Moreover, with their emphasis on the intergovernmental character of the SCO,

<sup>415</sup> "The Shanghai Co-operation Organisation: Suppression, China, Oil," *The Economist*, 9 July 2005, p. 47; Oresman, Matthew, "Day of Reckoning for China-Central Asia Group," 2003.

<sup>416</sup> Starr, S. Frederick, 2004, p. 18.

<sup>417</sup> "The Shanghai Co-operation Organisation," 2005, p. 47.

<sup>418</sup> Chung Chien-peng, 2004, p. 1007; "Путин высоко оценивает шаг КНР, предложившей предоставить около \$1 миллиарда на развитие торговли между странами ШОС" (Putin highly appreciates China's step to offer almost US\$1 billion for the development of trade relations between the countries of the SCO), *RIA-Novosti*, 17 June 2004, <http://rian.ru/politics/20040617/613896.html>.

<sup>419</sup> "Shanghai Cooperation Organization auf dem Weg zur wirtschaftlichen Integration," 2004, p. 963.

<sup>420</sup> Pollpeter, Kevin, *U.S.-China Security Management: Assessing the Military-to-Military Relationship*, Santa Monica, CA: RAND Corporation, 2004, p. 39.

<sup>421</sup> "ШОС провозглашает свою цветную революцию," (The SCO announces its own colourful revolution) *RIA-Novosti*, 5 July 2005, <http://rian.ru/analytics/20050705/40847645.html>.

Chinese policymakers uphold the traditional undertaking by states to respect each other as principal actors in the international arena while having domestic sovereignty within their own borders. By doing so, China wants the other members to perceive it as both a defender of state sovereignty and a respected great power in the community of nations.<sup>422</sup>

### 6.3. Military Engagement

#### *PLA Modernisation and Military-to-Military Relations*

The current modernisation of the PLA has two main objectives. China intends to build and deploy a comprehensively modern military that is commensurate with its status as a major power. Furthermore, the PLA should develop a range of capabilities that the leadership deems useful in a possible conflict over Taiwan.<sup>423</sup> Indeed, China's new national defence strategy that was adopted in 2002 is target specific; the PLA prepares for an armed conflict with Taiwan, with possible US involvement, and to that end the PLA is pushing two transformations simultaneously – the mechanisation (enhancing hardware platforms) and informatisation (IT integration)<sup>424</sup> of its forces. Accordingly, China's December 2004 Defence White Paper states that the PLA must be prepared to fight and win local wars under the conditions of informatisation. This concept incorporates assessments of the implications of the revolution in military affairs, primarily the impact of information technology and knowledge-based warfare on the battlefield.<sup>425</sup> Yet the mechanisation of the PLA is far from complete. Therefore, mechanisation plus informatisation dictates a huge increase in military spending that could stretch China's economy to the limit. Moreover, if not managed well it may even cause the PLA to be more vulnerable in the short run. Much-needed mechanisation may be further delayed due to resources being diverted elsewhere. In the end, double construction may mean “falling between two stools.”<sup>426</sup>

The mere fact that China has established military-to-military relations with the Central Asian countries can be viewed as an indication of an overall rapprochement between China and the countries of that region. In general, Chinese foreign military relations with other countries have a larger political component. They usually reflect the state of the overall bilateral relations with those countries. Thus, military relations result from a mutual trust that has been created by reaching a common strategic understanding on issues important to China. These key issues are the modernisation of the Chinese state, which requires a peaceful and stable regional security environment, and the defence of national sovereignty, which touches upon unsolved problems such as Taiwan and the Senkaku/Diaoyu Islands. Additionally, since China views military relations from a political perspective, it engages in such relations to serve pre-emptive purposes rather than to create vehicles for inclusiveness or coalition-building against common non-military threats. Accordingly, China utilises its military relations to prevent armed conflicts with potential adversaries and to strengthen relationships with friends.<sup>427</sup> Hence, military cooperation with the Central Asian countries must be viewed in this context – as part of China's foreign policy as well as its security concept, and not as signs of alliance building or forward power projection.

<sup>422</sup> Chung Chien-peng, 2004, pp. 992-3.

<sup>423</sup> Shambaugh, David, 2004/5, p. 85.

<sup>424</sup> The term informatisation acknowledges the PLA's emphasis on information technology as a force multiplier and reflects the PLA's understanding of the implications of the revolution in military affairs on the modern battlefield. See United States of America Department of Defense, “Annual Report to Congress: The Military Power of the People's Republic of China 2005,” 19 July 2005, [www.globalsecurity.org/military/library/report/2005/d20050719china.pdf](http://www.globalsecurity.org/military/library/report/2005/d20050719china.pdf).

<sup>425</sup> US Department of Defense, “Annual Report to Congress,” 2005.

<sup>426</sup> You Ji, “China's Emerging National Defense Strategy,” Association for Asian Research, 12 January 2005, <http://www.asianresearch.org/articles/2428.html>.

<sup>427</sup> Pollpeter, Kevin, 2004, pp. 75-7.

### *The PLA in Xinjiang*

The number of PLA forces deployed in Xinjiang has often been exaggerated. Some observers even portray Xinjiang as “a great wall of steel,”<sup>428</sup> which should be of particular strategic importance and might, therefore, constitute one of China's frontline military commands.<sup>429</sup>

Xinjiang is part of the Lanzhou Military Region which, with over 3.4 million square kilometres, constitutes China's largest military region. It includes the provinces of Shaanxi and Gansu, the autonomous regions of Ningxia and Xinjiang, as well as the western part of the Xizang Autonomous Region (Tibet). Although this military region covers 35% of China's total territory, its “real” fighting forces comprise only some 220,000 PLA troops. The Xinjiang Military District, which includes western Tibet, covers 2 million square kilometres but has no more than 50,000 to 60,000 regular troops. Thus, in contrast to what is widely believed, PLA forces in Xinjiang are relatively few and spread very thinly.<sup>430</sup>

Other paramilitary forces stationed in Xinjiang comprise the Xinjiang Production and Construction Corps (about 2 million people) and the regional People's Armed Police Force (100,000 troops). However, their main duties relate to internal security and construction, and their direct role in an external military confrontation is bound to be marginal. In fact, these forces cannot be considered professional military organisations that could contribute significantly to Xinjiang's defence. Actually, neither Xinjiang's military nor the paramilitary units are strong enough to deal with serious internal problems, let alone external threats.<sup>431</sup>

The PLA's weakness became obvious in the wake of 11 September 2001. A week after the attacks on the US, a first-grade military alarm was proclaimed in Xinjiang while various forces rushed from Lanzhou to Xinjiang. Other divisions were moved from Kuqa (Kuche) and Kashgar to the Sino-Afghan border. A mountain field division was moved from the Sino-Indian border to Taxkorgan (Tashiku'ergan) near the Afghan border.<sup>432</sup> Moreover, combined live-ammunition battle exercises were suddenly held in the Tian Shan Mountains and in the Gobi Desert to prepare the production and construction corps and the regional People's Armed Police Force to deal with unforeseen exigencies of war. Only in mid-October 2001 did a signal intelligence unit, deployed to intercept Taiwan's telecommunications, be moved from Fujian province to Xinjiang.<sup>433</sup>

Due to the huge investments needed to modernise the PLA, there will not be any funds available for massive border fortification in the foreseeable future. Moreover, the PLA's doctrine of peripheral defence is not one of forward projection, and there is little evidence that the PLA will develop capabilities to project power beyond China's immediate periphery.<sup>434</sup> Consequently, for the time being the PLA will not be able to rapidly intervene in any neighbouring country, especially in the Central Asian region.

### *China's Security Cooperation with Central Asian Countries*

After the unifying power of the Soviet Union had disappeared, there were no mechanisms in Central Asia for dealing with regional and internal disputes. Regional conflict prevention is dependent upon relatively strong states that can act with coordination and strength. Yet due to their underdeveloped political structures and battered economies, Central Asian states are weak, both politically and financially. Thus far they have failed to engage in multilateral cooperation without any external

<sup>428</sup> Interestingly, this term originates from a statement made by Xinjiang's former party secretary Wang Enmao in 1992 who wanted to protect Xinjiang against hostile foreign elements. See Burles, Mark, 1999, p. 16.

<sup>429</sup> Shichor, Yitzhak, “The Great Wall of Steel: Military and Strategy in Xinjiang,” in *Xinjiang: China's Muslim Boderland*, ed. S. Frederick Starr, Armonk, NY: M. E. Sharpe, 2004, p. 121.

<sup>430</sup> *Ibid.*, p. 123.

<sup>431</sup> *Ibid.*, pp. 122 and 125-6.

<sup>432</sup> The military forces have been deployed along the border with Afghanistan, or adjacent Tajikistan and Pakistan-held Kashmir ever since.

<sup>433</sup> Shichor, Yitzhak, 2004, pp. 120-1.

<sup>434</sup> Shambaugh, David, 2004/5, p. 86.

powers such as Russia or China, which provides little prospect for collective conflict prevention.<sup>435</sup> Moreover, the fear of regional hegemony among Central Asian countries has made it necessary to include external members so as to create a functional regional organisation. The SCO has been successful in building confidence between its members and has explicitly made efforts to prevent conflicts. With the 1996 Agreement on Confidence Building in the Military Field along the Border Areas, China institutionalised its military cooperation with Central Asian countries. The agreement is aimed at averting border clashes and promoting military-to-military cooperation. However, more concrete mechanisms for multilateral military cooperation within in the SCO have not yet been developed,<sup>436</sup> mainly because of the lack of trust between the Central Asian countries, their distrust of both China and Russia, and recent interference by the US. Therefore, military cooperation in the region is mainly conducted on a bilateral basis.<sup>437</sup>

Thus far, owing to their geographic proximity, China's efforts in the security realm have focussed on bilateral military relations with Kazakhstan, Kyrgyzstan and Tajikistan.<sup>438</sup> In October 2002, Kyrgyzstan and China conducted joint military counterinsurgency exercises on Kyrgyzstan's side of their mutual border, which was the first such joint training exercise on foreign territory that Chinese forces are known to have engaged in after the Sino-Soviet split. In 2003, China and Kyrgyzstan again conducted joint anti-terrorism exercises. Moreover, all members of the SCO participated in joint military exercises in Kazakhstan and Xinjiang in August 2003.<sup>439</sup> Furthermore, in an effort to cooperate in the fight against "external and internal threats," all SCO members will participate in joint anti-terrorism exercises in Russia in 2007.<sup>440</sup>

At the SCO summit in 2001, it was discussed that China might in future be allowed to send troops to Central Asia to combat terrorist threats there, if requested by regional governments.<sup>441</sup> Actually, because of China's commitment to maintaining stability in Central Asia, some Western analysts even expected that Chinese troops might soon fight in internal conflicts in Central Asian countries, if requested.<sup>442</sup> Yet the Chinese government acted very cautiously when it received such a request from Kyrgyzstan's interim government in the spring of 2005.<sup>443</sup> After violent clashes between demonstrators and riot police in the Uzbek town of Andijan, several hundred people had fled to Kyrgyzstan's border town of Osh in the densely-populated Ferghana Valley, which is a stronghold of militant Islamists, and further destabilised the volatile situation in the city. In May 2005, the then Kyrgyz interim president, Kurmanbek Bakiyev, asked Russia and China to deploy troops to a newly built air base near Osh in order to fight militant Islamists there. Bakiyev further announced that he would officially request the SCO to deploy forces to his country in order to fight drug trafficking and terrorists. Chinese military analysts acknowledged that China, as a member of the SCO, would have a duty to assist other member states to maintain stability and security in the region, and that the time for multilateral measures might already have come.<sup>444</sup>

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<sup>435</sup> Swanström, Niklas, "The Prospects for Multilateral Conflict Prevention and Regional Cooperation in Central Asia," *Central Asian Survey* 23, no. 1 (2004), pp. 41-2.

<sup>436</sup> In 2002, an SCO defence minister meeting had been held in Moscow to arrive at concrete measures for military cooperation. Despite Chinese insistence, this attempt failed because Uzbekistan's minister – encouraged by the US – did not attend the meeting. See Chung Chien-peng, 2004, p. 999.

<sup>437</sup> Swanström, Niklas, 2004, p. 45.

<sup>438</sup> Burles, Mark, 1999, p. 7.

<sup>439</sup> Klare, Michael, 2004, p. 172; "Jiefangjun shifou bingfa Zhongya: Jifang gei Zhongguo chu yaoqing" (Is the PLA to send troops to Central Asia? Kyrgyzstan made a request to China), *Yahoo! China*, 2 June 2005, <http://cn.news.yahoo.com/050602/1350/2ceyi.html>; Möller, Kay, 2005, 192.

<sup>440</sup> "Китай по линии ВТС остается партнером РФ, заявил Иванов" (Ivanov: China becomes Russia's partner in military-technology cooperation), *RIA-Novosti*, 26 April 2006, [http://www.rian.ru/defense\\_safety/20060426/46923080.html](http://www.rian.ru/defense_safety/20060426/46923080.html); "Russia to Host Asian War Drill," *BBC News*, 26 April 2006, <http://news.bbc.co.uk/1/hi/world/asia-pacific/4946110.stm>.

<sup>441</sup> Chung Chien-peng, 2004, p. 994.

<sup>442</sup> Klare, Michael, 2004, p. 173.

<sup>443</sup> "Jiefangjun shifou bingfa Zhongya," 2005.

<sup>444</sup> *Ibid.*

**Map 6.1: Ferghana Valley**

Source : "Uzbekistan: The Blood-red Revolution." *The Economist*, 19 May 2005, [http://www.economist.com/displaystory.cfm?story\\_id=3992111](http://www.economist.com/displaystory.cfm?story_id=3992111).

Generally, the two basic tenets of Chinese foreign policy are upholding the principle of non-interference in domestic affairs of other states and strengthening the role and effectiveness of the United Nations and the UN Security Council.<sup>445</sup> Although China had already participated in more than ten UN peacekeeping missions, sending several thousand troops, it has not yet sent troops under other international agreements. Moreover, China had only sent troops on short-term missions, but the deployment of troops to Kyrgyzstan would be rather permanent.<sup>446</sup>

In this instance, China chose not to send troops, mainly because interference in this local conflict would not add to China's own security, while the presence of Chinese troops could even further stir up hatred among the locals.<sup>447</sup> Several considerations led China to decide not to grant Kyrgyzstan's request to station Chinese forces in the country. First, the deployment of Chinese troops beyond a UN mission would considerably alter the premises of current Chinese foreign policy. Second, Osh – an area of high unemployment – has been a trouble spot for years, plagued by high crime rates along with religious, ethnic and social violence. Thus, if Chinese and Russian troops would be stationed there, they would be meddling in internal Kyrgyz affairs. Third, China was afraid to interfere in Russia's "backyard," which could negatively affect Sino-Russian relations. Moreover, since the US and NATO member France had already deployed troops to the country, China was uncertain about the possible consequence for the relations with these countries. Finally, as the Chinese troops were to fight religious extremism in Osh, they would inevitably become a target of those militants. Therefore, it was uncertain how many soldiers would be enough to protect the Chinese base but not further aggravate the locals' anger. Hence, the PLA still has to come up with mechanisms to prepare for such missions.<sup>448</sup> Thus, it can be expected that China will continue to treat similar requests very cautiously and will only act when Xinjiang's security could be affected.

However, Kyrgyzstan's request has triggered a broader discussion in China, and some military analysts have concluded that the deployment of troops in Central Asia would benefit Chinese interests in the region. Since it is confronted with a strengthening US-Japanese alliance along its eastern coast, China needs a stable "backyard" to be able to solve problems that might occur in the East. The two main arguments in favour of Chinese military presence in Central Asia concern China's economic and security interests and the volatile situation in Iran. The developments in Central Asia since 1990 have shown how the EU and the US have approached the region and have begun to exert their political and economic influence in the region. Military presence could safeguard China's economic interests in the region, in particular its growing energy imports. Moreover, due to the strategic importance of Xinjiang's resources and trade communications, China cannot afford to deal with a possible military or terrorist attack on its own territory. Finally, by establishing military bases in its neighbouring

<sup>445</sup> Chung Chien-peng, 2004, p. 993.

<sup>446</sup> Ibid.

<sup>447</sup> At times, the fertile Ferghana Valley had been part of the Chinese Empire. Despite the recent delimitation of the borders between the Central Asian countries and China, the fear of Chinese territorial claims is still persistent in the region.

<sup>448</sup> "Jiefangjun shifou bingfa Zhongya," 2005.

countries, China might be able to prevent the US from using these countries in a potential war against Iran.<sup>449</sup>

To put it briefly, common national-security interests brought Russia and China together and now form the basis for an increasingly closer strategic partnership that also includes military cooperation. This partnership was crucial to China's successful attempt to establish an international organisation with the Central Asian countries in order to address its security concerns, which are mainly related to Xinjiang. China also succeeded in including energy-related issues within the scope of the SCO. Closer economic relations with the member states are vital for China to gain more influence in the region, because its own military is not capable of interfering in neighbouring countries or subsequently restoring stability in a possible regional crisis in Central Asia.

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<sup>449</sup> "Zhongguo xi jin Zhongya da zhanlüe" (China's great strategy to move westward to Central Asia), *Lie xun junqing wang*, 7 June 2005, <http://www.1n0.net/Article/zbjs/2141.html>.



# 7

## Evaluation and Perspective

This final chapter assesses the importance of China's involvement in Central Asian affairs and its role in the broader Central Asian region. The last part expands on three scenarios that could change the current balance of power in this region and considerably affect China's strategy for the region as well as its overall oil strategy.

### 7.1. China's Role in Central Asia

#### *Increasing Economic Influence*

The demise of the Soviet Union forced China to develop an entirely new policy towards Central Asia, aimed at constraining new threats and enabling China to take advantage of new opportunities.<sup>450</sup> In order to address concerns about the stability of China's borders with the newly independent states and the potential for unrest among the region's Muslim peoples, China promptly established diplomatic relations with all five Central Asian states, but it conducted its policy towards the new republics very cautiously. Actually, China did not fully grasp the strategic weight of the region until 1993. Prime Minister Li Peng's 1994 tour of the region was the beginning of a more coherent policy towards Central Asia. A large group of Chinese entrepreneurs was also part of Li's delegation, which highlighted the prominent role of economic relations in China's policy towards the region. Additionally, due to China's increasing oil needs and disappointing oil explorations in Xinjiang's Tarim Basin, many Chinese analysts began to see Central Asia as an ideal oil exporter to China.<sup>451</sup>

Over the past decade, trade between China and the five Central Asian countries has quadrupled. Yet, with US\$2 billion in 2002, it still accounted for only 0.4% of China's overall trade turnover of more than US\$500 billion.<sup>452</sup> Although this percentage is rather low, the prospect of more imports of raw materials from Central Asia is crucial to the Chinese side. Furthermore, the political need for China to promote economic development in Xinjiang renders these commercial relations especially important.<sup>453</sup> Since Xinjiang has not yet been able to fully profit from these trade relations, China's current Central Asian strategy calls for increased efforts to integrate Xinjiang into the slowly emerging Central Asian markets.<sup>454</sup> Actually, the first contacts between Chinese businesses and the Central Asian countries had been enabled through direct links between Xinjiang and the region. Chinese traders had rushed in to fill the supply vacuum that the disruption of the old Soviet internal trade framework had created. The resulting economic relations between China and its Central Asian neighbours were dominated by small-scale barter trade throughout the 1990s.<sup>455</sup>

China hopes that increased trade will enhance stability within the volatile countries, as mutually beneficial economic interactions could strengthen the secular-minded governments of the region against religious or ethnic-based militant groups.<sup>456</sup> Due to its experience with the Taliban regime (1996-2002) which trained members of extremist Uygur groups from Xinjiang in camps in Afghanistan and supported them with capital and weapons, China does not want to see the emergence

<sup>450</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, p. 380.

<sup>451</sup> Tang Shiping, "Economic Integration in Central Asia," 2000, p. 367.

<sup>452</sup> This is the same percentage as in 1997. See Burles, Mark, 1999, p. 19.; Chung Chien-peng, 2004, p. 1008.

<sup>453</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, p. 380.

<sup>454</sup> Myers Jaffe, Amy, and Steven W. Lewis, 2002, p. 126.

<sup>455</sup> Wiemer, Calla, 2004, p. 171; Tang Shiping, "Economic Integration in Central Asia," 2000, p. 370.

<sup>456</sup> Burles, Mark, 1999, pp. 12-4.

of militant Islamist regimes at its borders. Hence, the Chinese leadership tries hard to stabilise the secular Central Asian regimes.<sup>457</sup>

Trade has the potential to broaden China's relations with Central Asia beyond issues of security and to foster greater economic opportunity and cooperation between the countries involved, and all Central Asian countries can raise standards of living and stimulate economic development through trade with China. Therefore, Central Asian countries are keen to strengthen their links with the booming Chinese economy. Chinese enterprises in Central Asia already number in the hundreds involving some hundred million US dollars of investment capital, despite the obstacles for investment caused by incomplete reforms and corruption in these countries.<sup>458</sup>

Unfortunately, the economic benefits of trading with China seem to have so far accrued more favourably to (East) China than to the Central Asian countries because of the fact that China exports consumer durables, food, fertilisers, electric appliances and machines to Central Asia, while it imports minerals, agricultural and animal products from the region.<sup>459</sup> Moreover, the pursuit of convergent economic interests has often been hampered by Central Asian leaders' fears of unregulated Chinese immigration and the ever-growing number of Chinese business people in their economies.<sup>460</sup>

Sinophobic feelings are common, even among the Central Asian political elite. They are partly the result of Soviet-era propaganda that illustrated China as the prime enemy, because it claimed 1.5 million square kilometres of territory now belonging to Kazakhstan, Kyrgyzstan, and Tajikistan. Even with recently accomplished border agreements, fears of Chinese expansionism still persist.<sup>461</sup> These fears have been exacerbated by the flood of Han Chinese moving to the broader region, partly to Xinjiang in the wake of the increased economic activities in that part of China, but also beyond China's borders. In Kazakhstan alone, there are 300,000 Chinese – most of them traders and farmers.<sup>462</sup> Complaints that Han Chinese take the profits back home with them and that the traditional local way of life is being eroded have already been voiced among the Turkic peoples in several Central Asian countries.<sup>463</sup> Even countries that do not have common borders with China are worried about immigrants from China.<sup>464</sup> Yet despite the fact that anti-Chinese feelings are present in all Central Asian countries, they do not often lead to violent aggression, as happened when Chinese businesses were looted by demonstrators during the uprisings in Kyrgyzstan in 2005.<sup>465</sup> The Chinese leadership is aware of such fears among China's Central Asian neighbours and hopes that institutionalised international cooperation within the framework of the Shanghai Cooperation Organisation can change the perception that China will become a dangerous hegemonic regional power.<sup>466</sup>

### *Strategic Competition in a Rough Territory*

China opposes a permanent US presence in Central Asia. For several reasons which are related to the economic and geopolitical importance of Central Asia to China, the Chinese leadership wants to exclude or at least minimise American influence in the region.<sup>467</sup> However, Chinese analysts are convinced that the US army will not leave either Afghanistan or Central Asia any time soon. They believe that the US government has wanted to ensure US interests in the Caspian oil business from the outset of its recent involvement. In pursuit of these interests, the US has tried to strengthen its ties with

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<sup>457</sup> Möller, Kay, 2005, p. 192.

<sup>458</sup> Wiemer, Calla, 2004, p. 186.

<sup>459</sup> Chung Chien-peng, 2004, p. 1002.

<sup>460</sup> Möller, Kay, 2005, p. 191.

<sup>461</sup> "China and Central Asia: Fear of the Dragon," *The Economist*, 13 November 2004, pp. 62-3.

<sup>462</sup> Due to the rapid decline of its own arable acreage, China rent several thousand hectares for farming in Kazakhstan. Hirn, Wolfgang, 2005, p. 159.

<sup>463</sup> Gladney, Dru C., 2004, p. 119.

<sup>464</sup> "China and Central Asia: Fear of the Dragon," 2004, pp. 62-3.

<sup>465</sup> "Kirgizstan: Another Autocrat Falls," *The Economist*, 2 April 2005, p. 48.

<sup>466</sup> Hale, David, and Lyric Hughes Hale, 2003, p. 48.

<sup>467</sup> Chung Chien-peng, 2004, p. 998.

the Central Asian states since the mid-1990s, by making great efforts to replace Russia as the most important supplier of weapons and partner in military cooperation.<sup>468</sup>

With the decision to get involved in the Central Asian pipeline battle, China was able to considerably enhance its political presence and influence in the region, while it also secured new supplies of energy. Interestingly, the Chinese leadership made this decision only after Western influence in the region had become obvious and it was apparent that Russia was unable to maintain its previous standing there. Therefore, this decision reveals a strong convergence between China's foreign policy and its energy policy. However, before China could accomplish both policy goals, it had to make massive investments.<sup>469</sup>

According to a Chinese report on Central Asia, published in 1998, Chinese involvement in Central Asia's oil business would not endanger China's energy security. The report acknowledged that the US was a competitor for Central Asian energy resources, but its ability to threaten China's oil supply from this region was considered to be limited, as the location of the region, being far from the US, would hamper efforts by the US to use military force in the region.<sup>470</sup>

Actually, even before 2001, the US had already repeatedly used economic pressure to prevent Kazakhstan and Turkmenistan from cooperating with China on energy issues. Such interventions have considerably increased since the end of the war in Afghanistan. Undeniably, since the deployment of US troops to Central Asia in 2001, international competition for energy resources in the Caspian region has become even fiercer. Hence, Chinese analysts view the presence of US forces in Central Asia as a major constraint on the country's access to Central Asian oil.<sup>471</sup>

Although the countries of Central Asia cannot threaten China in a conventional military sense, they can affect conditions within China in a much more direct manner. This potential stems from the demographic similarities between the Central Asian states and Xinjiang, as considerable numbers of all ethnic groups of the region settle in every Central Asian country as well as in Xinjiang.<sup>472</sup> In the wake of the war in Afghanistan and due to continuing instability there, Chinese analysts are increasingly worried that civil war could re-emerge in Afghanistan and destabilise the Central Asian regimes, which would affect the security of China's western regions.<sup>473</sup> Chinese analysts point to the fact that the deployment of US forces, which are stationed only a few hundred kilometres from Xinjiang's border, adds even more to the traditional security problem of West China.<sup>474</sup>

The US has created a security network in Southeast Asia consisting of bilateral access agreements with Singapore, Thailand, Brunei, Indonesia, Malaysia and the Philippines, which allows the US access to their ports, airfields, repair facilities and military training grounds in return for aid, equipment, and training of military staff. In addition to the unsolved Taiwan issue, with 47,000 US troops in Japan and 37,000 in South Korea, and with the presence of US troops in Kyrgyzstan and Tajikistan, China fears that it has already become a target of US encirclement. Additionally, Chinese analysts suspect that, in particular, recent US attempts to intensify military cooperation with India are aimed at the soft containment of China. The establishment of permanent US bases in Central Asia threatens China from the rear, where it feels most vulnerable.<sup>475</sup>

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<sup>468</sup> Zhongguo xiandai guoji guanxi yanjiuyuan (China institute of contemporary international relations) *Guoji zhanlue yu anquan xingshi pinggu 2003/2004* (International strategic and security review 2003/2004), Beijing: Shishi chubanshe, 2004, p. 155.

<sup>469</sup> Tang Shiping, "Economic Integration in Central Asia," 2000, p. 368; Andrews-Speed, Philip, and Sergei Vinogradov, 2000, pp. 394-5; Logan, Jeffrey, "Energy Outlook for China: Focus on Oil and Gas," 2005.

<sup>470</sup> Downs, Erica S., 2000, p. 46.

<sup>471</sup> Fan Jianping, and Niu Li, 2003, p. 63; Chen Fengying, "Dui jianli woguo zhanlue shiyou chubei de jidian sikao," (Some considerations regarding the creation of China's strategic petroleum reserves) in *Yilake zhanzheng yu Zhongguo jingji* (The Iraq war and China's economy), ed. Shi Guangsheng, Beijing: Zhonghua gongshang lianhe chubanshe, 2003, p. 203.

<sup>472</sup> Burles, Mark, 1999, p. 8.

<sup>473</sup> Jiang Xiyuan, *Daguo zhanlue yu weilai Zhongguo* (Great nation strategy and future China), Beijing: Zhongguo shehui kexue chubanshe, 2003, p. 336.

<sup>474</sup> "Jiefangjun shifou bingfa Zhongya," 2005.

<sup>475</sup> Klare, Michael, 2004, pp. 162-3; Hoge, James F., 2004, p. 5; Garrido, Marco, "America's Military 'Imperial Perimeter,'" *Asia Times Online*, 17 May 2003, [http://www.atimes.com/atimes/Middle\\_East/EE17Ak01.html](http://www.atimes.com/atimes/Middle_East/EE17Ak01.html).

The US is obviously trying to influence minorities in Xinjiang. US Congress is financing Uyghur organisations, including the Uyghur government in exile.<sup>476</sup> Such groups could easily be used to trigger US-sponsored uprisings like those in Georgia, Ukraine and Kyrgyzstan, which were viewed with much unrest in Beijing. Thus, by maintaining a military presence on China's western flank, the US is placing itself in a very advantageous position for any future strategic bargaining with the Chinese leadership.<sup>477</sup>

However, US containment of China does not appeal to many Asian states. Moreover, despite its military involvement in Afghanistan, the scope of US power in Asia is considerably smaller than it was at its height 25 years ago, because East Asian and Southeast Asian countries have grown significantly stronger, richer, and generally more stable.<sup>478</sup> Kang observes that Asian countries increasingly orient their economic and political focus toward China. He concludes that if forced to choose between the US and China, these countries might not make the choice that US strategists assume they will make. Therefore, US attempts to form a balancing coalition against China may be counterproductive.<sup>479</sup>

Hierarchies can be separated into global and regional levels. For Asia's further development, it will be particularly crucial as to whether the US will allow China to resume its traditional place atop the Asian regional hierarchy.<sup>480</sup> However, as Asia will be the most important economic region for decades to come, the dominant power in this part of the world will also exert considerable global influence. Therefore, it cannot be expected that the US will resign itself to the Chinese dominance of Asia. In fact, judging from American activities in Asia, especially in Central Asia, it can be concluded that the US is prepared to head off China's rise.

As accelerating globalisation binds Asian societies and economies together in complex and interdependent ways, its traditional geographic subcomponents – i.e., Northeast Asia, Southeast Asia, South Asia, Central Asia, and contiguous Oceania – are no longer useful intellectual constructs for dividing or distinguishing the macro processes affecting the whole region.<sup>481</sup> As has been described, developments in East China affect Xinjiang and subsequently Central Asia and vice versa. Therefore, analysts need to be able to fully comprehend the impact of China's internal transformation upon regional stability. If China's domestic reforms stall or if there is significant social upheaval, the results would have major negative implications for the whole of Asia.

During the first two decades of the 21st century, China's leadership will be challenged to provide a range of public goods to the populace and improve the people's quality of life. China's governance challenges, however, will also increasingly become the responsibility of China's neighbours. If they collectively fail, widespread unrest within China will result and could possibly spill over China's borders, destabilising the regional order. Hence, while China increasingly engages in regional affairs, more than ever before, the rest of the region and even the world beyond have a major stake in the success of China's domestic development and reforms.<sup>482</sup>

After the gain of their independence, the perceived weakness of the Central Asian states made the region seem ripe for domination both by the more powerful states bordering the region and by interested external parties.<sup>483</sup> At present, Central Asia is still in a state of flux. Accordingly, Central Asia can be viewed as a region in need of a new equilibrium of power.<sup>484</sup> Andrews-Speed and Vinogradov correctly observed that even without the presence of substantial energy reserves, the former Central Asian Soviet republics would have developed into a battleground for competing

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<sup>476</sup> "China: The Great Leap West," 2004, p. 50.

<sup>477</sup> Chung Chien-peng, 2004, p. 1003.

<sup>478</sup> *Ibid.*, p. 71.

<sup>479</sup> *Ibid.*, p. 83.

<sup>480</sup> Kang, David C., "Getting Asia Wrong: The Need for New Analytical Frameworks." *International Security* 27, no. 4 (Spring 2003), p. 71.

<sup>481</sup> Shambaugh, David, 2004/5, p. 97.

<sup>482</sup> Shambaugh, David, 2004/5, p. 98.

<sup>483</sup> Brill Olcott, Martha, 2000, p. 371.

<sup>484</sup> Dekmejian, R. Hrair, and Hovann H. Simonian, 2003, p. 7.

outside interests seeking to establish their influence.<sup>485</sup> Thus, China would also have had a strong incentive to become involved in Central Asian affairs even without the prospect of oil supplies from this region – namely, because of China’s concerns about the stability of Xinjiang.

Undeniably, China’s growing economic engagement in Central Asia is accompanied by increasing political influence. Strategic considerations were already part of China’s goals when it decided to get involved in the region. Over the past few years, China has achieved certain objectives of its policy towards Central Asia. The question is whether China will be able to play its current role in the wake of fiercer competition for energy resources and continuing US interference in the political and economic affairs of the Central Asian countries. Still, China’s concern for internal and external stability will preclude war as a means of achieving its policy goals in Central Asia.

## 7.2. Towards Inter-Regional Economic Integration

### *Avoiding Sea-lanes – Cooperation with Myanmar and Pakistan*

Despite major efforts by the Chinese government to diversify its oil supplies, the Persian Gulf region will remain its most important oil supplier. Shipments from the Persian Gulf are, however, vulnerable to US interference, as the US Navy controls all major sea-lanes to China. Currently, the US Navy protects the narrow straits of Hormuz, Malacca and Taiwan. Due to financial constraints caused by its plans to modernise the PLA, it seems rather unlikely that China will be able to build a navy and air force capable of protecting Chinese oil tankers that use these sea-lanes.

Chinese analysts believe that China would face an energy crisis if its oil supply lines were disrupted, and that China’s main oil transport route could be blocked by whatever power controls the Indian Ocean and the Strait of Malacca.<sup>486</sup> This vulnerability has caused China to seek alternative safe supply routes for its energy shipments. Actually, Southwest and South Asia constitute a littoral that gives China’s southwestern and westernmost regions access to vital sea-lanes.<sup>487</sup> Consequently, China is establishing numerous ports along the sea-lanes from the Middle East to the South China Sea, including facilities in Pakistan, Bangladesh, Myanmar and Thailand, which US analysts call China’s “string of pearls” strategy.<sup>488</sup>

The ports of Gwadar (Pakistan) and Sittwe (Myanmar) will play especially important roles in China’s strategy to avoid critical sea-lanes for its oil shipments. In 2004, Chinese experts made the first proposal to build a pipeline from Sittwe to Southwest China. In July 2005, both governments signed a memorandum on the construction of the pipeline to Kunming in the province of Yunnan. This pipeline will allow Chinese oil shipments from the Middle East and Africa to avoid passing the Strait of Malacca. The pipeline will be built by CNPC and Sinopec. CNOOC is also interested in the completion of this project. All three companies have acquired concessions for onshore as well as offshore exploration in Myanmar in recent years. Moreover, the province of Yunnan is keen to build refineries and invest in the establishment of petrochemical facilities, so that it can provide neighbouring provinces with oil derivatives. By 2010 the five southwestern provinces will be short 22 million tonnes of gasoline and diesel annually. The pipeline, with its annual shipment of 40 to 60 million tonnes of crude oil, will not only ease this shortage but also enable the export of oil products beyond Southwest China’s to the populous provinces of Hunan and Hubei.<sup>489</sup>

The port of Gwadar, which was initially set up as part of China’s plans to transport Kazakh oil through Iran to China, will rank among the world’s largest deep-sea ports after its completion. Gwadar is

<sup>485</sup> Andrews-Speed, Philip, and Sergei Vinogradov, 2000, p. 397.

<sup>486</sup> Zweig, David, and Bi Jianhai, “China’s Global Hunt for Energy,” *Foreign Affairs* 84, no. 5 (2005), p. 29.

<sup>487</sup> Garver, John W., 2005, p. 209.

<sup>488</sup> Ramachandran, Sudha, “China’s Pearl in Pakistan’s Waters,” *Asia Times Online*, 4 March 2005,

[http://www.atimes.com/atimes/South\\_Asia/GC04Df06.html](http://www.atimes.com/atimes/South_Asia/GC04Df06.html); Niazi, Tarique, “Gwadar: China’s Naval Outpost on the Indian Ocean,” *China Brief*, 15 February 2005,

[http://www.jamestown.org/publications\\_details.php?volume\\_id=408&issue\\_id=3232&article\\_id=2369262](http://www.jamestown.org/publications_details.php?volume_id=408&issue_id=3232&article_id=2369262).

<sup>489</sup> “Zhong Mian shiyou guandao fang’an shouci baoguang: da zu’ai yinsu wei paichu” (The Chinese-Myanmar pipeline project revealed for the first time: big obstacles not yet removed), *NetEase*, 27 April 2006, <http://biz.163.com/06/0427/15/2FNPDRHH00020QFA.html>.

located in Pakistan's Balochistan province, just 72 km from the Iranian border and about 400 km from the Strait of Hormuz, and is bounded by the Persian Gulf in the west and the Gulf of Oman in the southwest.<sup>490</sup>

### Map 7.1: Gwadar deep-sea port



Source: Ramachandran, Sudha. "China's Pearl in Pakistan's Waters." *Asia Times Online*, 4 March 2005, [http://www.atimes.com/atimes/South\\_Asia/GC04Df06.html](http://www.atimes.com/atimes/South_Asia/GC04Df06.html).

The project had already been under study since May 2001, but China stepped up its involvement in the project in the wake of the US-led war in Afghanistan. From a strategic perspective, the project provides China with a foothold in the Arabian Sea and the Indian Ocean and also helps transform Pakistan's Navy into a force that can rival other regional navies.<sup>491</sup> Moreover, China is by far the country's most important weapons supplier. In 2004, China and Pakistan solidified their military relations by conducting their first-ever joint naval exercises in the East China Sea near Shanghai and joint anti-terrorism exercises near Taxkorgan in Xinjiang.<sup>492</sup> In order to help coordinate military cooperation and avoid suspicion by India, China's navy conducted military exercises with the navies of both Pakistan and India in the Indian Ocean in late 2005.<sup>493</sup>

China has sent 450 engineers and provided a substantial part of the total cost of US\$1.16 billion as well as technical expertise for the Gwadar project. Moreover, a road from Gwadar to the north of Pakistan is under construction, which will be the shortest connection between Central Asia and the Arabian Sea. Gwadar will provide China with a transit terminal for oil imports from Iran and Africa that will then be transported to Xinjiang.<sup>494</sup>

After the completion of the Gwadar project, China will have access to a network of rail and road links that will connect Pakistan with Afghanistan and Central Asia.<sup>495</sup> Moreover, President Pervez Musharraf has repeatedly stated that his country is prepared to become China's "energy corridor." He has stressed that he is willing to pursue this proposal and has invited Chinese private investors to participate in the construction of the necessary infrastructure. Musharraf has further declared that he is not afraid of pressure from external powers to halt the project.<sup>496</sup>

<sup>490</sup> Ramachandran, Sudha, "China's Pearl in Pakistan's Waters," 2005.

<sup>491</sup> Pakistan has designated the whole port area as "sensitive defence zone." Indeed, Gwadar also provides China with a listening post where US naval activity in the Gulf can be monitored from. China has already set up electronic eavesdropping posts at Gwadar that are monitoring maritime traffic through the Strait of Hormuz and the Arabian Sea. See Ramachandra, Sudha, "China's Pearl in Pakistan's Waters," 2005; Niazi, Tarique, "Gwadar," 2005.

<sup>492</sup> Niazi, Tarique, "Gwadar," 2005; "Allwetterfreundschaft wie gehabt zwischen China und Pakistan," (All-weather friendship as usual between China and Pakistan) *China aktuell* 23, no. 8 (2004), p. 835.

<sup>493</sup> "Zhong Yin junshi jiaoliu shengji: haijun lianhe yanbing Yindu linghai" (Chinese-Indian military exchanges improves: joint exercises in Indian territorial waters), *Renmin wang*, 30 November 2005, <http://military.people.com.cn/GB/1076/52965/3902747.html>.

<sup>494</sup> Ramachandran, Sudha, "China's Pearl in Pakistan's Waters," 2005.

<sup>495</sup> Ibid.

<sup>496</sup> "Mushalafu wuju wailai yali yu jian Zhong Ba nengyuan zoulang" (Musharraf not afraid of external pressure: he wants to build the Chinese-Pakistani energy corridor), *NetEase*, 29 April 2006, <http://news.163.com/06/0429/11/2FSEEKHP00011234.html>.

As the Gwadar project will facilitate China's energy imports and the export of Chinese manufactured goods, part of China's aim is to help Xinjiang regain its previous function as an important hub of communications between China, Central Asia and South Asia.<sup>497</sup> Thus, oil supplies to Xinjiang will not originate only from Central Asia. Hence, it can be expected that investments, which were made in the wake of the Western Development Programme to extend Xinjiang's network of pipelines and modernise its oil industry, will likely pay off in the foreseeable future.

### *Chinese Stakes in Iran*

China and Iran have been cooperating successfully in the energy business for decades. Since the end of 2004, China has been Iran's major oil export market.<sup>498</sup> Moreover, as already mentioned, the two countries conduct oil swaps as a way to get Caspian crude to China until the completion of the Chinese-Kazakh pipeline is realised. China has already become one of Iran's most important trade partners. In 2005, bilateral trade reached a volume of US\$10 billion, which is several times higher than a decade ago.<sup>499</sup> Besides China's extensive energy cooperation with Iran, other Chinese firms are also active in the country, constructing dams, cement plants, steel mills, and railways. In February 2003, the Chinese auto manufacturer Chery opened its first overseas production plant in Iran. The two countries have signed more than 100 contracts for major infrastructure projects.<sup>500</sup>

As can be imagined, Western governments – especially the Bush Administration – have been showing growing unease at China's stance on the conflict over Iran's nuclear energy programme. After concluding historic gas and oil deals with Iran in 2004, China made clear that the issue of Iran's nuclear facilities must be solved through dialogue and dismissed the proposal to refer the case to the UN Security Council. China's Foreign Minister, Li Zhaoxing, also stressed that China would not support any UN Security Council action against Iran's nuclear energy programme.<sup>501</sup> In general, as a result of the strengthening economic ties with Iran, possible sanctions imposed by the UN Security Council would harm China's national interest.<sup>502</sup>

Ever since Iraq, Iran, and North Korea were dubbed the “axis of evil” in US President George W. Bush's State of the Union Address in January 2002 and, subsequently, the first regime on the list had been overthrown by US forces, China has been keen to strengthen its ties with Russia and Iran, so as to prevent US military action against the remaining countries. Undoubtedly, closer cooperation between China, Russia, and Iran is challenging US interests in Central Asia. Needless to say, Iran – like Russia and China – opposes permanent US deployment in Central Asia and Afghanistan. Iran is of course seeking a way out of its increasing nuclear impasse with the United States. In 2004, Iran announced that it was interested in joining the SCO.<sup>503</sup> Recent statements by the secretary of the SCO suggest that the organisation is seriously considering the possibility of Iranian membership. However, Russia's minister of defence, Sergey Ivanov, also has made clear that the organisation would not defend Iran in case of a military attack.<sup>504</sup> Nevertheless, Russia and China will do their utmost to prevent sanctions against Iran.

<sup>497</sup> Niazi, Tarique, “Gwadar,” 2005.

<sup>498</sup> Gundzik, Jephraim P., “The Ties that Bind China, Russia, and Iran,” 2005.

<sup>499</sup> “Zhongguo jing cheng le zhuyao zhang'ai? Yilang hewei ji kaoyan Zhongguo waijiao” (Is China the most important obstacle?: the Iranian nuclear crisis tests China's diplomacy), *Zhongguo jingji wang*, 18 January 2006, [http://www.ce.cn/xwzx/gjss/gdxw/200601/18/t20060118\\_5866962.shtml](http://www.ce.cn/xwzx/gjss/gdxw/200601/18/t20060118_5866962.shtml).

<sup>500</sup> Shuja, Sharif, “Warming Sino-Iranian Relations: Will China Trade Nuclear Technology for Oil?,” *China Brief*, 23 July 2005, <http://www.asianresearch.org/articles/2653.html>; “Zhongguo jing cheng le zhuyao zhang'ai?,” 2005.

<sup>501</sup> Shuja, Sharif, “Warming Sino-Iranian Relations,” 2005; Gundzik, Jephraim P., “The Ties that Bind China, Russia and Iran,” 2005.

<sup>502</sup> “Zhongguo jing cheng le zhuyao zhang'ai?,” 2005.

<sup>503</sup> Gundzik, Jephraim P., “The US and that ‘Other’ Axis,” *Asia Times Online*, 9 June 2005, <http://www.atimes.com/atimes/China/GF09Ad08.html>.

<sup>504</sup> “Иванов: ШОС не будет защищать Иран в случае нападения” (Ivanov: SCO will not defend Iran in case of attack), *Nezavizimaya gazeta*, 25 April 2006, <http://news.ng.ru/2006/04/25/1145956406.html>.

### 7.3. The Geopolitical Outlook

#### *Is China Trying to Balance US Influence?*

At the end of the Cold War, US scholars saw Asia as being “ripe for rivalry,” expecting the fulfilment of the growing possibilities of Japanese rearmament, increased Chinese adventurism spurred by China’s rising power, and ostensibly revisionist intentions.<sup>505</sup> Undeniably, China’s rising power and increasing participation in international affairs have raised the question as to what extent China could be described as a ‘revisionist’ or ‘non-status quo’ state. Gilpin states that international relations involve certain “rules of the game” – i.e., the distribution of power and the hierarchy of prestige among states, as well as the rights and rules that govern, or at least influence, interaction among the states.<sup>506</sup> From the perspective of rising powers, the perceived costs of changing the international system constantly decline relative to the potential benefits of doing so.<sup>507</sup> Thus, revisionist states eventually seek to fundamentally alter the components of the international system. However, if a state pursues anything less,<sup>508</sup> it becomes problematic to call the state either revisionist or non-status quo.<sup>509</sup>

Indeed, there is no indication that China is attempting to be a balance to US military power or trying to undermine its alliances in Asia. Given the current stage of China’s economic transformation and its growing economic interdependence, the Chinese leadership appears to be unwilling to bear the economic and social costs of mobilising the economy and militarising society to seriously balance against US power and influence in the region.<sup>510</sup> Although the leadership wishes to increase China’s relative economic and military power, it does not appear to wish to risk much in terms of the country’s economic development or its relationship with the US. Therefore, China’s desire to be richer and more powerful has not translated into a concerted military effort to replace the US as the predominant state in Asia.<sup>511</sup> Moreover, China’s current regional policy does not rely upon pushing the US out of Asia. Not only does China lack the capacity to do so, but it does not deem this to be in its own best interest or that of the region. As long as the US does not threaten China’s core interests, China can live with this “hegemonic power.”<sup>512</sup> Hence, for the time being, China “is not seeking a place in the sun, but rather a protected place in the shade.”<sup>513</sup>

Undeniably, China “has played its diplomatic hand adroitly” and has been successful in exploiting the growing strains in the relations between Asian countries and the US.<sup>514</sup> Such manoeuvres, however, were conducted in international forums or bilateral consultations and cannot be characterised as coercive.<sup>515</sup> Moreover, as the establishment of the SCO as an international institutional framework has shown, much evidence can be found that China is likely to act within bounds acceptable to the other Asian nations.<sup>516</sup> China has proposed very few new rules in international institutions, and analysts have generally been positive of China’s conformity to extant rules when the country has become a member of international institutions.<sup>517</sup> Hence, China clearly acts within the “rules of the game” and is not positioning to become a balance to US power in Asia. Moreover, as China’s influence is mainly restricted to the Asian context, it cannot be considered a revisionist state.

Yet the ideology-based US foreign policy and its double standards hamper other members of the international community in finding peaceful solutions to international conflicts through making

<sup>505</sup> See, for instance, Friedberg, Aaron L., “Ripe for Rivalry: Prospects for Peace in a Multipolar Asia,” *International Security* 18, no. 3 (1993), pp. 5-33.

<sup>506</sup> Gilpin, Robert, *War and Change in World Politics*. Cambridge: Cambridge University Press, 1981, pp. 28-35.

<sup>507</sup> *Ibid.*, p. 187.

<sup>508</sup> According to Morgenthau, minor adjustments which leave intact the relative power positions of the nations concerned are fully compatible with a policy of the status quo. Morgenthau, Hans J., *Politics among Nations: The Struggle for Power and Peace*. New York: Alfred A. Knopf, 1978, p. 46, quoted in Johnston, Alastair Iain, 2003, p. 8.

<sup>509</sup> Johnston, Alastair Iain, 2003, p. 10.

<sup>510</sup> *Ibid.*, p. 47.

<sup>511</sup> *Ibid.*, p. 56.

<sup>512</sup> Zhang Yunliang, and Tang Shiping, 2005, pp. 53 and 57.

<sup>513</sup> Xiang Lanxin, 2004, p. 118.

<sup>514</sup> Shambaugh, David, 2004/5, p. 90.

<sup>515</sup> *Ibid.*, pp. 90-4.

<sup>516</sup> Kang, David C., 2003, p. 83; Zhang Yunling, and Tang Shiping, 2005, p. 59.

<sup>517</sup> Johnston, Alastair Iain, 2003, p. 23.

compromises. While the 20th century was dominated by the biblical dichotomy of “good” versus “evil,” the abrupt end of the Cold War made many Cold War strategists “missionaries for a cause that no longer existed.”<sup>518</sup> Hence, US think tanks, especially those dominated by Bush’s neoconservatives, have been targeting China as one of the main challenges ever since. Although the wars on terror and tyranny have diverted their attention toward other threats, the alleged “China treat” is still imminent.<sup>519</sup> Currently, US analysts view China’s actions in Central Asia as a response to its national-security concerns, and not as a fundamental threat to US interests. Nevertheless, neoconservative analysts who foresee China growing into a major military rival are alarmed by any sign of geopolitical initiative on China’s part.<sup>520</sup>

Moreover, the neoconservative hardliners whose assumptions shape the Bush administration’s perception of China are convinced that the country is “ruled by an aggressive and fundamentally anti-American dictatorship that seeks ultimately to dominate Asia” and that “represents a greater potential danger in the long term than any other nation in the world.”<sup>521</sup> Thus, China constitutes “a direct threat ... to America’s vital interest in a balance of power in Asia.”<sup>522</sup> Even liberal analysts state that “China and America are strategic competitors (albeit of vastly unequal power) locked in an ambiguous relationship with elements of conflict, coexistence and cooperation.”<sup>523</sup> Further, a close reading of the *Quadrennial Defense Review* of 2001 reveals that the US military’s long-term strategy is based on the expectation that the next threat to global US security interests will be China.<sup>524</sup>

Actually, US analysts and policymakers view the current post-Cold War period as a fluid time that offers a strategic opportunity to shape the world to come, during which the US should not “adhere to every international convention and agreement” that entail an epidemic of “illusory ‘norms’ of international behaviour.”<sup>525</sup> In order to defend the “national interest,” the US Army must be able “to meet decisively the emergence of any hostile military power in the Asian Pacific region, the Middle East, the Persian Gulf, and Europe.”<sup>526</sup> An overly broad definition of “America’s national interest,” however, would leave the US looking to the UN to sanction the use of US military power in the name of humanitarianism, which would imply that the US would do so even when its vital interests are involved, “which would also be a mistake.”<sup>527</sup> With the legally questionable justification and conduct of the 2003 Iraq war, it became clear that this foreign policy approach has already been put into practice. Therefore, it can be expected that the US will not refrain from using its military power and unilaterally interfere with the affairs of other countries where the “national interest” legitimises such actions.

Despite the benefits of economic interaction with China, US analysts still consider China to be a potential threat to stability in the Asia-Pacific region, mainly because of the unresolved Taiwan issue and its military cooperation with Pakistan and Iran. As China allegedly resents the role of the US in this region, it cannot be viewed as a status quo power, but “one that would like to alter Asia’s balance of power in its own favour,” which alone makes it a “strategic competitor.”<sup>528</sup> Accordingly, the necessity to cooperate with China notwithstanding, the US should never be afraid to confront Beijing when the interests of the two countries collide.<sup>529</sup>

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<sup>518</sup> Xiang Lanxin, 2004, p. 111.

<sup>519</sup> *Ibid.*, p. 115.

<sup>520</sup> Klare, Michael, 2004, p. 164.

<sup>521</sup> Munro, Ross H., “China: The Challenge of a Rising Power,” in *Present Dangers: Crisis and Opportunity in American Foreign and Defense Policy*, ed. Robert Kagan and William Kristol, San Francisco, CA: Encounter, 2000, pp. 47-8.

<sup>522</sup> Munro, Ross H., 2000, p. 68.

<sup>523</sup> Shambaugh, David, 2000, p. 97.

<sup>524</sup> Chung Chien-peng, 2004, p. 1003.

<sup>525</sup> Rice, Condoleezza, “Promoting the National Interest,” *Foreign Affairs* 79, no. 1 (2000), pp. 48-9.

<sup>526</sup> *Ibid.*, p. 52.

<sup>527</sup> *Ibid.*, p. 54.

<sup>528</sup> *Ibid.*, p. 56.

<sup>529</sup> *Ibid.*, p. 57.

### *Three Possible Scenarios*

Two situations could turn China's current international behaviour into that of a revisionist or non-status quo state – i.e., domestic social and political upheavals and worsening China-US relations. Actually, US policy would be able to do much more about an emerging China-US security dilemma than about the negative effects of the transition to a market economy.<sup>530</sup> At present, China pursues a rather defensive approach as regards to its domestic social and political challenges as well as regarding its relations with the US.

Undoubtedly, the war on terrorism, the developments in the world energy market and the goal of exporting democracy worldwide has brought the broader Central Asian region to the forefront of US national security priorities.<sup>531</sup> Therefore, US military presence in Afghanistan and Central Asia will have to be maintained for a considerable length of time.<sup>532</sup> Klare expects that the struggle for geopolitical advantage in Central Asia “will almost certainly intensify in the years ahead” and will become one of the main sources of friction and crisis in Sino-American relations, as “nowhere else on earth do the vital interests of the major powers collide in this fashion, and nowhere are there so many potential sources of friction and crisis.”<sup>533</sup> Thus, the temptation of the major players “to exploit these divisions in order to gain tactical advantage over one or the other may prove irresistible.”<sup>534</sup> In fact, the very fear of such developments caused China to become more involved in Central Asia. Thus, the current unpredictable situation in Central Asia could worsen as a result of US activities in the broader region or of direct attempts to destabilise China as part of a Sino-US conflict.

One scenario that could affect China's interests in the broader Central Asian region would be a US-led war against Iran. Indeed, a war against Iran would further destabilise the Middle Eastern region and could inflict even more damage on China's economy than the war against Iraq. Therefore, China will do its utmost to prevent such a scenario. Increased US pressure on Iran would strengthen Sino-Russian diplomatic and security ties and consolidate the current security arrangements within the SCO, as well as enhance both Russia's and China's bilateral cooperation with Iran. As a US-controlled Iran would substantially change the geopolitics of the Middle East and Central Asia, it can be expected that China, together with Russia, will do anything possible to prevent a US-led attack on Iran.

With Nursultan Nazarbayev's re-election in 2005, a “colourful revolution” in Kazakhstan was prevented, at least for the time being. A US-sponsored change of the Kazakh government would be another development that could upset China's Central Asian policy. This kind of remote-controlled regime change would considerably hamper China's energy-focussed strategic partnership with Kazakhstan and make it even more difficult for China to acquire sufficient oil to fill its oil pipeline. However, as China's reaction to the developments in Kyrgyzstan in the spring of 2005 has shown, it can be expected that the Chinese government will try to seek as much common ground as possible in order to further its interests. The institutionalisation of the SCO can be seen as a viable means to mitigate the effects of rather sudden internal disruptions within the member states. Therefore, it can be expected that, at least for some time, China will continue to use its economic clout to court the new Kazakh government and pursue its economic interests. Moreover, China is accustomed to keeping its economic relations separate from politics. Finally, China's state-owned companies – as part of the government's geopolitical manoeuvres – can invest larger amounts of money than the profit-driven American private enterprises. Hence, economic relations with China are increasingly important for the regimes in China's periphery, and even a US-sponsored new government of Kazakhstan would have to find a way to cooperate with its booming neighbour.

Finally, in the worst-case scenario, spillover effects of colourful revolutions in Central Asia or US interference could directly affect Xinjiang's stability. The Chinese are especially afraid of a Kosovo-like scenario, entailing US or NATO operations from bases in Central Asia on behalf of forces such as

<sup>530</sup> Johnston, Alastair Iain, 2003, p. 56.

<sup>531</sup> Oresman, Matthew, “Central Asia as the New Arena in Sino-U.S. Relations,” *China Brief*, 29 April 2004, [http://www.jamestown.org/publications\\_details.php?volume\\_id=395&issue\\_id=2939&article\\_id=236641](http://www.jamestown.org/publications_details.php?volume_id=395&issue_id=2939&article_id=236641).

<sup>532</sup> Menon, Rajan, “The New Great Game in Central Asia,” *Survival* 45, no. 2 (2003), pp. 189-91.

<sup>533</sup> Klare, Michael, 2004, p. 175.

<sup>534</sup> *Ibid.*, p. 178.

secessionist Uyghurs. Because of the widespread Uyghur diaspora, this could have repercussions in the whole region, affecting Central Asia, Pakistan and China proper. Tens of thousands of displaced Uyghurs have found refuge in Central Asia, as well as in Pakistan, where the majority of them live in the country's two most populous cities, Lahore and Karachi. As a result of a broader conflict in Xinjiang, violent attacks could endanger China's huge investments in Pakistan, amounting to about US\$4 billion.<sup>535</sup> Moreover, the inevitable countermeasures that would have to be taken by Beijing to restore order and stability in Xinjiang would certainly damage China's relations with its Muslim neighbours and Middle Eastern partners. Undeniably, a worsening of China's relations with the Middle East would cause severe economic problems in China that could eventually trigger further social-economic disruptions.

In sum, China is involved in a wide range of activities in the broader Central Asian region. As a result, it can be concluded that this region will play an important part in China's oil strategy and its overall strategy to modernise the country's economy, as well as its foreign policy and security strategy. China's economic rise is changing its periphery at a breathless pace, contributing to more and more inter-regional cooperation. Any attempt by external powers to interfere with developments in this region could disturb this cooperation and eventually trigger hedging measures by regional powers that would definitely increase the possibility of conflict in the region.

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<sup>535</sup> Niazi, Tarique, "Gwadar," 2005.



# 8

## Conclusion

This paper has aimed at assessing the geopolitical developments in Central Asia and China's policy towards the region. The construction of the Chinese-Kazakh oil pipeline, as an example of China's cooperation with its neighbours, has been discussed as part of China's oil strategy and the government's efforts to foster economic development in West China. The construction of this pipeline illustrates the far-reaching economic as well as geopolitical implications of China's economic transformation. China's leaders have to accomplish their country's ascent to the ranks of global great powers in a unipolar international order. They mainly focus on China's periphery to shape an environment conducive to the country's economic development. This approach has so far proved successful.

Since its neighbours increasingly profit from China's economic rise, they are increasingly willing to take China's interests into account. This is also true for China's energy cooperation with Central Asia, in particular with Kazakhstan. Now that China has become a net oil importer, the demand for ever-increasing oil imports, needed to maintain high economic growth rates, has dominated China's relations with oil-producing countries. As China's bargaining power within the Asian context has considerably increased in the last decade, only US interference constitutes a serious threat to China's seaborne oil supplies and its attempts to acquire new oil concessions abroad. At the moment, 60% of China's oil imports originate from the Middle East. Due to the substantial US influence in that region and growing instability, China has been trying to diversify the origins of its oil supplies.

The Chinese government had supported CNPC's and YUKOS's plans to build an oil pipeline from East Siberia to Northeast China. Yet the Russian government eventually opted for a financially more attractive pipeline project to supply Japan with oil. After this blow to China's oil security strategy, it seemed that Central Asia was the only alternative for the Chinese in building a cross-border pipeline. Therefore, investments in Kazakhstan to acquire sufficient oil concessions and to construct the pipeline have to be evaluated in view of these strategic considerations. The Chinese government provides Chinese oil companies with substantial financial and political support. Still, the government also expects the state-owned companies to fulfil the country's oil strategy, which entails the realisation of investments in regions that are often shunned by multinational energy companies. In fact, the construction of the Chinese-Kazakh pipeline is not only an important part of China's effort to diversify its oil supplies, but also facilitates the further upgrading of Xinjiang's oil sector. In order to boost the development of this region, China is assertively establishing economic ties with its periphery. This effort is facilitated by China's and Russia's converging interests in Central Asia and the establishment of the SCO, which has become an important counterweight to the increasing US influence in the region. Indeed, China's economic and political clout in the broader region has been growing for a couple of years.

However, the assertion that China is using its growing influence to balance against American power is a gross distortion of the facts. China possesses neither the economic resources nor the military capability to replace the US presence in Asia. Consequently, for the analysis of the geopolitical struggles that are unfolding in Central Asia, it is crucial to thoroughly understand the rationale behind China's actions. Basing the analysis merely on China's need for oil supplies or viewing China as a revisionist rising power that is keen to project its power onto a volatile region, might constitute a serious omission. Therefore, it is indispensable to analyse – as has been attempted in this paper – the complex interactions between China's internal economic and social development and its international behaviour in order to correctly assess the wider geopolitical implications of China's rise.

Asia is changing at breathless speed, and the most significant trend is more inter-regional economic cooperation than ever before. Without a doubt, the completion of the first stretch of pipeline from Kazakhstan to Xinjiang was not the last celebration of a major project that Chinese officials and their Central Asian counterparts will enjoy together.

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