China’s Strategy for Energy Acquisition in the Middle East: Potential for Conflict and Cooperation With the United States

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In this article, the authors examine China’s evolving energy strategy in the Middle East, particularly in the three countries that have the largest energy reserves and form the epicenter of the U.S.-China rivalry: Saudi Arabia, Iran, and Iraq. With $3 trillion in foreign currency reserves, Beijing is increasingly using its cash to secure future long-term access to energy in the region. Through energy-backed loans, as well as upstream and downstream joint ventures, China’s policy banks and its national oil companies are pumping up the volume of oil and gas that will flow from the Middle East to the mainland in the 21st century. At the same time, Beijing is embedding itself deeply in the economies of these major oil-producing states through expanded bilateral trade involving multiple sectors of the Chinese economy. Beijing’s monetary strength, coupled with its lack of military involvement and political baggage in the region, has China poised to benefit from its expansive access to the region’s energy resources. This article critically examines the political implications of China’s energy acquisition strategy, the potential for conflict as well as cooperation with the United States, and the possibility of the realignment of great powers in the Middle East.

Key words: China, energy, Middle East, oil, United States

Introduction

Throughout its “peaceful rise” strategy, “offend no one” diplomacy, and unprecedented economic growth, China has established itself as a major player in the global energy market. Now, with $3 trillion in foreign exchange reserves, China is employing a more sophisticated energy acquisition strategy that increasingly features investment in foreign energy companies, downstream joint ventures, expanded bilateral trade involving multiple sectors of the Chinese economy, and energy-backed loans to (EBLs) oil-producing states as preferred methods of securing access to greater energy resources (Stein & Oster, 2011).

Because the United States is the largest consumer of oil and the second largest consumer of energy in the world, any discussion of China’s energy strategy...
would be incomplete if it failed to detail the role of its primary rival for energy, the United States. In addition, the significant military footprint of the United States in the region and, more specifically, the critical role of its navy in safeguarding the oil shipping lanes, give the United States a looming presence in the region that shapes China’s strategy: to balance the pursuit of its energy interests with the major regional producers on the one hand and the United States on the other. If we consider the significant bilateral U.S.-China relations, the delicacy of this balancing act involving both rivalry and competition as well as cooperation becomes even more paramount.

Beijing’s energy imports, as well as its economic and diplomatic ties to the Middle East, have expanded dramatically in the decade since the terrorist attacks of 9/11, whereas U.S. oil imports from major Persian Gulf producers and Washington’s influence in the region have diminished. These changing dynamics in the Middle East are the product of China’s rapid economic growth and Beijing’s opportunistic energy acquisition strategy, which exploits tensions between the United States and key energy producers such as Saudi Arabia, Iran, and Iraq.

According to the International Energy Agency (IEA), the global demand for oil is projected to increase from approximately 74 million barrels per day in 2009 to 99 million barrels per day in 2035. China will account for approximately half of this increased consumption, whereas Organization of Petroleum Exporting Countries (OPEC) members will supply the vast majority of the additional 25 million barrels per day required by the global market. Specifically, the IEA projects that Saudi Arabia will increase its production from 9.6 million barrels per day in 2009 to 14.6 million barrels per day in 2035, with Iraq projected to increase from 2 million barrels per day in 2009 to 7 million barrels per day in 2035. During this period, Iraq and Saudi Arabia will account for approximately 12 million additional barrels per day, while some non-OPEC members will begin to see their output decline. These estimates, which are based on proven oil reserves, confirm that the Middle East will remain a critical region for China—the world’s largest consumer of energy and its second largest consumer of oil (IEA, 2011, pp. 5–6).

This article examines China’s recent policies in Saudi Arabia, Iran, and Iraq in order to understand Beijing’s evolving strategy for accessing energy resources from the region. As global demand for energy, particularly from China, continues to increase exponentially, the stage is set for intense competition over the remaining oil and gas in the Middle East. Going forward, some major questions merit our attention: Can both the United States and China obtain adequate energy resources from the Middle East peacefully? Or would the fruitful management of the rivalry necessitate further cooperation? In which Middle Eastern countries is the competition for energy likely to intensify, and what potential threats could derail China’s energy acquisition strategy? These are important questions that must be answered in order to understand the great power realignment that is currently under way in the Middle East.

The body of work on China’s energy relations with the Middle East is sparse and scattered, and it is a topic that until recently was ignored. However, in recent years, some good scholarship on the subject has emerged. Some notable works include John Calabrese’s *China’s Changing Relations With the Middle East* (1991);
P. R. Kumaraswamy’s *China and the Middle East: Quest for Influence* (1999); Barry Rubin’s “China’s Middle East Strategy” (1999); Mohamed Bin Huwaidin’s *China’s Relations With Arabia and the Gulf, 1949–1999* (2002); Erica Strecker Down’s *China’s Quest for Energy Security* (2000); Liangxiang Jin’s “Energy First: China and the Middle East” (2005); John Garver’s *China and Iran: Ancient Partners in a Post-Imperial World* (2006); Flynt Leverett and Jeffrey Bader’s “Managing China-U.S. Energy Competition in the Middle East” (2006); Harsh V. Pant’s “Saudi Arabia Woos China and India” (2006); Yufeng Mao’s “China’s Interest and Strategy in the Middle East and the Arab World,” which appeared in *China and the Developing World: Beijing’s Strategy for the Twenty-First Century* (2007); and Erica Downs and Suzanne Moloney’s “Getting China to Sanction Iran” (2011).

Our contribution, in contrast, is comparative in its scope, focusing on China’s relations with three key regional energy producers and political players, namely, Saudi Arabia, Iran, and Iraq. By incorporating an analysis of most recent political developments, our article also puts China’s role in the larger context of U.S.-China competition and cooperation for energy resources in the region and speculates on how this would impact the realignment of great powers in the Middle East, shedding light on an emerging new political map with global implications.

**China’s Energy Relations With the Middle East**

China’s energy-driven engagement with the Middle East is a relatively new phenomenon. Prior to the 1990s, Beijing attempted to build alliances and gain credibility in the region by supporting “national liberation movements” and through weapons sales to countries such as Iran, Iraq, Saudi Arabia, and even Israel. When, as early as 1993, it became clear that China’s domestic oil production would not satisfy its growing demand, Beijing’s focus on the Middle East shifted dramatically to energy acquisition. Through its “going out” strategy, the Chinese government encouraged its three major energy companies—the China National Petroleum Corporation (CNPC), the China Petrochemical Corporation (Sinopec Group), and the China National Offshore Oil Corporation (CNOOC)—to go abroad and secure supplies of oil and gas through investment, exploration, drilling, and the construction of refineries and pipelines (Leverett & Bader, 2006, pp. 187–193).

The backlash against U.S. military interventions in the Middle East, especially in the last two decades, opened the door for China in the region—and allowed Beijing to present itself to states such as Iran, Syria, and a post-2001 Saudi Arabia—as a reasonable economic and political alternative to the United States (Leverett & Noel, 2006, p. 67). China’s entry into the energy markets of the Middle East was further facilitated by the fact that it did not have a colonial history in the region and in recent years, Beijing has not demonstrated a proclivity for expansionism or the violation of state sovereignty (Currier & Dorraj, 2009, p. 61).

In the first decade of the 21st century, as the United States waged wars in Afghanistan and Iraq and attempted to isolate Iran through U.N. sanctions, China continued “going out” to the Middle East with greater success. China’s oil imports from the Middle East, which rose from 8.42 million barrels per year in
1990 to 276.67 million barrels per year in 2000 (Jin, 2005, pp. 4–5), continued to increase dramatically, and by 2009 China was importing 2 million barrels per day from the Middle East (U.S. Energy Information Administration, 2011a).

While the United States expended considerable political capital attempting to rally the global community against countries such as Iran, Venezuela, and Sudan, China stepped in to gain access to their energy resources and to counterbalance U.S. influence, not only in these countries but also in the larger developing world. China contends that its energy relations, arms sales, and bilateral trade with states hostile to the United States facilitates the emergence of a multipolar world, one that is more peaceful and capable of supporting an expanding globalized economy. In this respect, China sees its dealings in the region as a way to balance U.S. hegemony, and not simply as a mechanism for gaining access to energy reserves (Currier & Dorraj, 2011, pp. 3–11).

Beijing’s Statist Approach to Energy

At the core of China’s energy strategy is Beijing’s skillful diplomacy, which is facilitated by the aggressive practices of China’s national oil companies (NOCs) and its policy banks, particularly China Development Bank (CDB) and China Export-Import Bank (Eximbank [EXIM]). There is a growing trend for China’s banks to offer EBLs to oil-producing states, including those in the Middle East, Africa, Latin America, and Central Asia, and for China’s NOCs and policy banks to invest heavily in downstream joint ventures with the major energy-producing states. These EBLs and joint ventures strengthen the supplier-buyer relationship and further solidify China’s future access to oil and gas.

In each of these areas—diplomacy, NOCs, and banking—there is one common goal: to ensure an adequate supply of energy capable of sustaining China’s unprecedented economic growth, which in turn will fund development in the world’s most populous nation. In order to achieve its goal of energy security, China must explore partnering with as many oil-producing states as possible. In some cases, this involves working with states ideologically opposed to one another and to China, such as Iran and Saudi Arabia, and working with states that are unfriendly toward the United States, such as Iran and Syria. This variety of suppliers is critical for Beijing as it attempts to diversify China’s sources of energy and thus safeguard its national interests. Hence, if China’s relationship with one energy producer threatens its balancing act with the United States, then Beijing can turn to a multitude of other suppliers to meet its expanding energy needs while preserving its important bilateral relations with Washington.

Energy Diplomacy

Beijing’s “offend no one” policy and its “peaceful rise” strategy stand in stark contrast to U.S. hegemonic policies in the Middle East. China employs virtually no military force in the region and has instead sought to expand its trade and economic ties with various oil-producing states. As Jon Alterman (2009) has observed, “China has pursued a patient and quiet strategy of building a wide array of commercial interests in the region, supplemented by diplomatic gestures and cultural ties” (p. 63).
For the resource-rich states of the Middle East, China’s potential for continued economic growth represents an appealing long-term market for their products. But equally important, by shifting a significant portion of their energy export to China, Middle Eastern states, especially those with adversarial relations with the United States, also have an opportunity to diminish U.S. power and influence in the region. In this respect, there is no duplicity in China’s energy relations with the Middle East. Beijing has openly stated its desire to cooperate with key energy producers in a manner that is mutually beneficial, and it has gone about its business without the use of force and without imposing its ideology on the region. At the same time, most Middle Eastern states value China’s array of low-cost goods and services and the less problematic nature of working with Beijing, a relationship that comes with significantly less political baggage than dealing with the United States and the European Union (EU).

Currently, 50% of China’s oil imports come from the Middle East and more than 25% come from Africa. Since all of its oil imports from the Middle East and Africa must pass through the vulnerable Straits of Malacca, China is devoting significant diplomatic efforts to securing multiple routes for transporting oil and gas from its source to mainland China. A good example of Beijing’s energy-driven diplomacy is its “string of pearls” strategy, which involves building closer diplomatic relationships with Pakistan, Bangladesh, Myanmar, Thailand, and Cambodia—countries located along the shipping lanes from the Middle East to the South China Sea (Lai, 2007, pp. 528–529).

Pakistan now has a deepwater port in the city of Gwadar, near the entrance to the Persian Gulf. The port was heavily financed and constructed by the Chinese, who plan to ship oil from Gwadar to the Xinjiang region of China by road, rail, and possibly pipeline—a move intended to lower transportation costs and keep much of China’s Middle Eastern oil out of the Strait of Malacca. When tensions increased between the United States and Pakistan following the assassination of Osama bin Laden in Pakistan by U.S. Special Forces, Beijing praised Islamabad’s efforts at fighting terror and announced it was providing 50 additional fighter jets to the Pakistani air force (Bodeen, 2011). China’s position was the opposite of the U.S. response, which included heavy criticism of Islamabad and the threat of reducing or eliminating U.S. aid to Pakistan. As part of its energy strategy, Beijing seeks opportunities like this to exploit frayed U.S. relations in the region and present itself as a reasonable alternative to Washington. One of the consequences of this is that China has provided the regional powers with greater leverage against the United States.

**National Oil Companies**

NOCs are tools of governments like Iran, Saudi Arabia, and China that take a statist approach to energy. Beijing believes energy is too critical to its national interest and economic security to entrust it to the free market; therefore, it has placed its energy companies under state control. Of China’s three primary NOCs, the CNPC is the largest and is diversified in all levels of the industry. Sinopec Group is more heavily involved in downstream activities, particularly refining and distribution, while the CNOOC is extensively involved in upstream exploration and production. CNPC and its publicly traded division, PetroChina, have
oil and gas assets in 30 different countries and account for 54% of China’s oil output and 82% of its gas production (CNPC, 2011a). CNPC’s strategy has three elements: increasing and diversifying resources, expanding upstream and downstream operations to establish a dominant position in the market, and seeking a greater international role in a way that is mutually beneficial to CNPC and its partners (CNPC, 2011b).

Unlike U.S. energy companies, China’s NOCs have the backing of their government, which ensures these NOCs have adequate funding to aggressively grow their businesses. As Leverett and Noel (2006) have observed, “Beijing often follows up its network of energy deals by increasing exports of manufactured goods and capital to countries where its NOCs are operating. In some cases, the Chinese appear willing to put expensive packages of side investments on the table in order to secure energy deals” (p. 66). One point of contention in the U.S.-China energy rivalry is that NOCs do not compete on a level playing field with publicly held energy companies, which would like to see Beijing’s NOCs participate more fully in international energy markets.

In its 2009 annual report, CNPC credits its use of long-term contracts, hedging, processing, warehousing, and financing for strengthening its control of resources and for increasing its annual international trade in crude and petroleum products by 19.7% in one year (CNPC, 2010, p. 56). According to the U.S. Energy Information Administration (2011a), from October 2008 to December 2009, China’s NOCs invested approximately $17 billion in oil and gas acquisitions from other companies and secured $70 billion in loan-for-oil agreements with several oil-producing countries. As CNPC, Sinopec Group, and CNOOC continue to grow in tandem with the country’s energy consumption and its wealth, the United States, the EU, and Japan will likely hold China to a higher standard—no longer giving it a “free pass” as a developing country. As one of the wealthiest countries in the world, China will have a difficult time making the case that it should operate from a different set of trade and banking regulations than those that govern developed countries.

China’s Policy Banks and Extensive Cash Reserves

China’s policy banks, particularly CDB and EXIM, are playing an increasingly active role in its energy acquisition strategy. Specifically, CDB and EXIM are providing financing to China’s NOCs for energy investments abroad, financing the development of infrastructure to deliver oil and gas to China, and providing credit to foreign energy companies in return for long-term energy contracts. For example, in 2009 and 2010, CDB extended $65 billion in EBLs to Russia, Brazil, Turkmenistan, Ecuador, and Venezuela. These EBLs have several notable features that render them alluring to the developing nations, including their large size (up to $20 billion), their long-term commitment (up to 20 years), and their availability at a time following the global financial crisis when very few institutions are willing to lend large amounts of money for extended periods of time (Downs, 2011, pp. 1–2).

Policy banks serve as a “link between the strategic ambitions of the Chinese government and the commercial interests of Chinese firms” and ensure credit is not an impediment to China’s NOCs as they pursue energy resources abroad
CDB takes its role a step further by sending out “work teams” to more than 100 different countries to gather information, build relationships with business and political leaders, and identify investment opportunities for Chinese energy companies (Downs, 2011, p. 29).

CDB and EXIM, which are owned by the Chinese government and supervised by the State Council, were created in the 1990s to facilitate China’s “going out” strategy. EXIM’s Web site indicates its mission is to “strengthen China’s relations with foreign countries and enhance the international economic and trade cooperation” (China Eximbank, 2011). Policy banks like CDB and EXIM are not subject to China’s Commercial Banking Law, which blocks commercial banks from participating in both commercial and investment banking. CDB has taken advantage of its status to prosper further from underwriting the corporate bonds of major state-owned enterprises, which has substantially increased the bank’s size and allowed it to increase its foreign currency loans (Downs, 2011, p. 19). According to CDB’s 2009 annual report, the bank’s outstanding foreign currency loans increased from $16.5 billion in 2005 to $97.4 billion in 2009 (CDB, 2010, pp. 6, 57).

Because China does not belong to the Organization for Economic Cooperation and Development, its banks are able to operate outside the normal export credit rules. This provides states in the Middle East and Africa with a viable alternative for financing separate from the United States, whose offers of money generally require the support of certain U.S. policies and the advancement of human rights (Moss & Rose, 2006).

China also does not adhere to transparency initiatives such as the Extractive Industries Transparency Initiative. Therefore, the money its NOCs and banks are paying to oil-producing countries is not always reported publicly. This lack of transparency likely contributes to corruption, which ultimately threatens the stability of global energy markets. China’s aggressive banking practices are also promoting oil-based development. When the internal development of oil-producing states is driven by China’s energy needs and not necessarily the needs of that country, then the resource can become a curse, producing long-term, negative consequences for oil exporters as they struggle with a lack of economic diversity, inflation of currency, corruption, and conflict (Karl, 2005, pp. 21–26).

China’s policy banks are clearly taking advantage of what is now the country’s greatest asset—its cash. CDB and EXIM are not only facilitating the growth of China’s NOCs and expanding the country’s energy infrastructure, but they are also securing long-term energy deals by offering high-dollar, long-term financing that energy-producing states are unlikely to find anywhere else in the world. These EBLs also help China diversify its foreign exchange reserves. As of January 2011, China held $1.15 trillion in U.S. Treasuries. Beijing’s strategy of investing heavily in U.S. Treasuries over the past decade was for the purpose of keeping the dollar and other currencies strong in relation to the yuan, a move intended to keep Chinese exports attractively priced for consumers abroad. Critics of China’s strategy argue that Beijing’s excessive reserves and undervalued currency are driving up inflation rates at home, which hinders domestic development. This situation is potentially explosive and could lead to civil unrest if many of China’s 1.3 billion citizens feel they are not benefiting from the country’s massive generation of wealth. According to Li Jie, a researcher at the Central University of
Finance and Economics, “It is too high a cost to pay to let the whole domestic economy suffer from high inflation just to protect exporters. China cannot afford to sacrifice its internal economy as it has a vast domestic market” ("The Problem,” 2011).

While China is now making increased efforts to globalize the yuan, which will ultimately increase the value of its currency, Beijing also understands the important role its low-cost exports have played in gaining access to energy markets throughout the world. As Chinese goods become more expensive, Beijing may lose a powerful energy acquisition tool; however, a stronger currency will also give China greater buying power abroad. As such, we may be witnessing a shift in Chinese energy acquisition strategy, where low-cost exports, which were once critical to gaining access to energy markets, assume a less significant role, and “money,” in the form of acquisitions, joint ventures, and EBLs, becomes Beijing’s primary tool for securing energy resources.

China’s Cash Goes Downstream

For wealthy Middle Eastern states that do not necessarily need China’s financing, Beijing’s energy acquisition strategy also includes the pursuit of mutually beneficial, downstream joint ventures for the construction and operation of oil refineries and pipelines. Many of these partnerships are with major energy suppliers from the Middle East. According to the Wall Street Journal, in March 2011, Aramco signed a memorandum of understanding to provide “up to 200,000 barrels a day of Arabian crude oil through long-term contracts to PetroChina’s 10-million-metric-ton-a-year refinery in Yunnan” in southern China (Said, 2011). The crude will be delivered through a pipeline, currently under construction, that will run from the west coast of Myanmar to southern China—a move intended to keep this oil out of the narrow and dangerous Strait of Malacca. While the Myanmar-China pipeline will reduce China’s dependence on U.S. naval security in the Strait of Malacca, it may also increase tension with the United States, which remains at odds with the military government in Myanmar (Said, 2011).

Sinopec Group and Saudi Basic Industries Corp. recently started production of petrochemicals at a facility in Tianjin (China), and Sinopec Group and Aramco signed a memorandum of understanding to “develop the 400,000-barrel-per-day Yanbu refinery on Saudi Arabia’s Red Sea coast” (Said, 2011). Of these deals, Aramco Chief Executive Khalid Al-Falih stated, “We don’t consider ourselves simply as sellers of oil to China, but rather strategic partners” (Said, 2011).

Downstream joint ventures solidify China’s relations with its key energy supplies while channeling additional energy resources to the mainland. These refineries and factories also represent profitable investment opportunities for China’s extensive cash reserves.

The U.S.-China Rivalry in the Middle East and Its Political Implications

There are three states surrounding the Persian Gulf that form the epicenter of the U.S.-China energy rivalry in the Middle East: Saudi Arabia, Iran, and Iraq. These three countries produce over 16 million barrels of oil per day and
figure prominently in the energy, trade, and overall geopolitical strategies of both the United States and China. Other countries in the region, such as the United Arab Emirates (UAE) and Kuwait, are important centers of energy and trade but are unlikely flashpoints in the U.S.-China rivalry for two reasons. First, the UAE and Kuwait have healthy energy and bilateral trade relations with both the United States and China. Second, the UAE and Kuwait support the role of the United States as protector, and China’s cash reserves or soft resources are unlikely to diminish that support. At the same time, though, the UAE and Kuwait equally support the role of China as a new energy and economic superpower, and political pressure from Washington is unlikely to diminish that support. Saudi Arabia, Iran, and Iraq, on the other hand, have complex relations with the United States and China that make them more likely flashpoints in the rivalry as the global competition for energy intensifies in the 21st century.

U.S. relations with the epicenter countries are a mixed bag. Saudi Arabia is an ally, but U.S.-Saudi relations have cooled considerably since 9/11. Washington and Tehran remain openly hostile over Iran’s nuclear program, which the United States insists is for the purpose of developing weapons of mass destruction. A post-Saddam Iraq is more accessible and somewhat cooperative, but remains frustrated with U.S. policies in the region. As the United States struggles with the civil war in Afghanistan, China quietly goes about its business, expanding trade and energy relations throughout the Middle East, including the three epicenter countries.

As the balance of power shifts in the Middle East, Canada and Mexico have become the top two sources of crude oil for the United States, while Saudi Arabia has slipped to number three and Iraq is sixth—a reflection of the post 9/11 order where Washington has closed its bases in Saudi Arabia and invaded Iraq (U.S. Energy Information Administration, 2011c). U.S. imports of crude oil and petroleum products from OPEC countries have decreased by more than 234 million barrels per year in the decade since the terrorist attacks of 9/11, and the Chinese have picked up the slack (U.S. Energy Information Administration, 2011d). In 2010, China imported 4.8 million barrels of oil per day, of which 47% was from the Middle East. By 2035, the U.S. Energy Information Administration projects China will import 72% of its crude (U.S. Energy Information Administration, 2011a).

The key question is where will China find this oil? While Africa holds significant potential for augmenting China’s energy needs, it is also arguably the one region in the world that is more volatile and unstable than the Middle East. South America holds some promise, once China has sufficient refineries capable of processing the heavier oil from Venezuela and Brazil. Also, the geographic distance and larger transportation costs from Latin America are significant challenges that must be considered. Russia has tremendous energy resources, but Moscow and Beijing have a checkered past, including a Sino-Soviet conflict in 1969. The most likely source for China’s additional energy needs remains the Middle East.

The United States has well-documented concerns with Chinese policies in the Middle East, including China’s weapons sales to countries accused of harboring terrorists, China’s expanding relations with countries openly hostile to the United States, and China’s lack of cooperation on nonproliferation and human
rights issues (Chen, 2010, pp. 39–54). China also has concerns, including what it considers to be U.S. hegemonic and unilateral policies in the Middle East, and Washington’s attempts to arm Taiwan. However, because China’s economic interests in the Middle East ultimately require stability and security, which China’s military is not presently capable of providing, it must rely on the U.S. military to protect shipping lanes and promote political stability in the region. According to Mao (2007), “Conflict with the United States would not only undermine Chinese diplomatic efforts and economic interests in the region, but also hinder China’s global political and economic goals” (p. 122). Beijing’s dependence on U.S. security puts it in an awkward position that begs the question, what sort of superpower is unable to defend its economic interests abroad? China’s increased military spending suggests that key decision makers in Beijing may be asking the same question.

In 2004, China’s military spending was $55.2 billion, approximately one-tenth the amount spent by the United States. By 2009, China’s military spending doubled to $110.1 billion and represented one-sixth of the U.S. amount (Stockholm International Peace Research Institute, 2011). While Chinese officials and some scholars insist that the rise of China is going to be peaceful and China’s intention is to create a harmonious world (Yongming, 2006, pp. 14–15), others contend that as China expands its military capabilities, the temptation will be to use those resources to resolve conflicts in its favor, thus potentially making China a new hegemonic power (Ikenberry, 2008, pp. 23–57). A more militarized China also increases the likelihood of conflict between the emerging superpower and its rivals, including the United States (Mearsheimer, 2006, pp. 160–162).

In addition to maintaining a strong military presence in the region through troop deployments, naval patrolling of shipping lanes, and military exercises, the United States sells billions of dollars’ worth of weapon systems to Saudi Arabia, Iraq, and the UAE, primarily to counter the perceived threat from Iran and insurgent groups like Al-Qaeda and to protect its economic interests. In October 2010, “the U.S. unveiled a record 10-year, $60 billion deal to sell advanced F-15 fighters, helicopters and other arms to Saudi Arabia” (Entous, 2011). The problem with using arms sales as a means of building better relations with Middle Eastern governments and gaining access to their oil is the dilemma that increased militarization of the region would not necessarily contribute to its political stability and the security of energy supplies. There is no guarantee that a regime receiving weapons today will still be in power tomorrow or that subsequent regimes would be more accommodating. The current uprisings sweeping through the Middle East highlight this risk. States such as Egypt, Tunisia, Bahrain, Libya, Yemen, and Syria have entered a period of great uncertainty, and many of these countries are heavily armed after years of purchasing weapons from Russia, China, and the United States.

**Saudi Arabia: The Prize**

With oil production of 10.2 million barrels per day and proven reserves of more than 260 billion barrels, Saudi Arabia figures prominently in both the United States’ and China’s energy strategies (U.S. Energy Information Administration, 2011b). The kingdom has approximately one-fifth of the world’s proven oil
reserves, which makes it the global market’s key swing producer, one capable of influencing market prices and averting economic crisis. The fact that oil export revenues have accounted for 90% of total Saudi export revenues and 75% of government revenues highlights the importance of oil to the Saudi economy and the royal family’s grip on power, and it explains why Riyadh has no choice but to maintain relations with the world’s top two energy consumers (U.S. State Department, 2012). However, diversifying its exports in a manner that gives Beijing a more prominent role in the region makes good political sense for the kingdom, which must deal with anti-U.S. sentiment from a sector of its population. According to Prince Turki al-Faisal, a former Saudi ambassador to the United States, when working with China, “there is less baggage, (and) there are easier routes to mutual benefit” (Meyer, 2010).

China established formal diplomatic ties with Saudi Arabia in 1990, and trade between the two countries subsequently increased from $290 million in 1990 to $40 billion in 2008 (Meyer, 2010). When U.S.-Saudi relations were strained following the terrorist attacks of September 11, 2001, Saudi oil shipments to the United States declined and Beijing ratcheted up its diplomatic effort to deepen relations with the kingdom. In 2004, China and the Gulf Cooperation Council, which is led by Saudi Arabia, proposed a Free Trade Area Agreement, which represents “an important advance on economic, trade, investment and technological cooperation” and is intended to facilitate “economic integration” between China and the Gulf states (Yetiv & Lu, 2007, pp. 206–207). While this initiative as of yet has not materialized, it reflects a willingness on both sides to expand ties. For example, when Saudi King Abdullah bin Abdul-Aziz al-Saud made his first trip outside the Middle East in January 2006, he traveled to both China and India—a clear shift in Saudi foreign policy intended to give the kingdom a political and economic alternative to the United States (Pant, 2006, p. 45). Since 2006, China’s President Hu Jintao has made two trips to Saudi Arabia. Not surprisingly, Saudi oil exports to China have been on the rise, from 455,000 barrels per day in 2005 to approximately one million barrels per day in 2010 (Meyer, 2010).

Although oil is at the core of the Sino-Saudi relationship, the two countries are rapidly developing deeper economic ties. According to a recent assessment, “90 Chinese companies (now) do business in Saudi Arabia, including 70 construction firms employing 20,000 Chinese people” (Meyer, 2010). China’s more expansive relations with Saudi Arabia also portend that it would be exceedingly difficult for the kingdom to dismiss this crucial partnership.

Iran: A Difficult but Beneficial Partnership

With significant coastline on both the Persian Gulf and Caspian Sea, Iran is an energy powerhouse and a strategically significant regional player. The country produces 3.7 million barrels of oil per day and has the world’s third largest proven reserves of 137 billion barrels. Iran also produces approximately 5.2 trillion cubic feet of natural gas per year and has the world’s second largest proven reserves of 1,046 trillion cubic feet, second only to Russia (U.S. Energy Information Administration, 2012).

In 2002, China’s President Jiang Zemin visited Iran to sign an oil and gas cooperation agreement. Two years later, Sinopec Group signed a memorandum
of understanding with Iran to purchase 250 million tons of liquefied natural gas and to develop the Yadavaran field, which will send 150,000 barrels of crude oil to China each day for 25 years. By 2003, Iran was already China’s number two supplier of oil, second only to Saudi Arabia (Lai, 2007, pp. 523–525).

Because U.N. sanctions and U.S. law make it illegal for U.S. companies to work with Tehran, it is not surprising that Iran figures prominently in China’s energy strategy. With no U.S. competition for Iran’s energy resources, China has deeply embedded itself in the Iranian economy as “Iran’s biggest single trading partner and largest investor in the oil and gas sector” (Slavin, 2011, p. 1).

But China’s relations with Iran are much more complex and ultimately beneficial to Beijing than simply satisfying a significant portion of its energy requirement. Beijing has masterfully used its relationship with Tehran as a bargaining chip in its relationship with the United States. The shrewdness of this particular geopolitical game is that Beijing frequently comes out the winner. With the United States and most of the EU countries out, and the diminished presence of Japan and the troubled nature of Russian-Iranian relations, China has had limited competition for Iran’s vast quantities of oil and gas. China’s behavior in regard to U.S.-EU-U.N.-led four sets of sanctions on Iran follows a pattern that reveals its adept foreign policy. When pressure from the United States on Iran’s nuclear issue becomes too great, Beijing relents in its opposition to the imposition of sanctions. Beijing realizes its support, or lack of support, of Tehran has great value to the United States, which has made the derailment of Iran’s nuclear program a top priority of U.S. foreign policy. On all four rounds of U.N. sanctions against Iran, Beijing deliberately dragged its feet, not just because it was reluctant to act against a key energy partner, but also because it was engaged in a chess match with the United States. In each case, China eventually supported sanctions, but not before gaining political concessions from Washington that ensures the continued protection of Chinese interests in Iran as its leading partner in trade. The key issue for China is how to maintain ties with Iran without ruining its own political capital as a responsible stakeholder in the international system (Dorraj & Currier, 2011, pp. 65–82).

That is not to say that China’s support of sanctions has no cost or consequences for either player (Iran or China) in this political chess game. If the cost of doing business with Tehran outweighs its benefits and seriously damages U.S.-China bilateral relations, that, in Beijing’s political calculus, looms much larger than its relations with a Third World country like Iran; China would not hesitate to pull back on the scale of its partnership with the Islamic Republic. In 2010, for example, “Chinese crude oil imports from Iran dropped by 35 percent” (Downs & Moloney, 2011, p. 18). In response, “Iranian parliament’s National Security Committee pledged to launch an inquiry into Chinese-Iranian relations,” and the Iranian media is building a case that “China is price gouging, that its materials are inferior, and that cheap Chinese imports are driving Iran’s small industries out of business” (Downs & Moloney, 2011, p. 19). These measures are likely a backlash against Beijing for supporting sanctions. Although Tehran recognizes it is being used by China, it has little alternative. Iran is dependent on its resource revenues, and China represents the lesser of two evils to a regime that sees its energy sales to Beijing as a steady source of income that fosters its economic and security interests.
Washington believes Beijing’s ongoing energy relations with Tehran are limiting the effectiveness of U.N. sanctions against Iran. President Barack Obama dispatched Robert J. Einhorn, a special advisor to the U.S. State Department, to Beijing in September 2010. During that visit, Einhorn presented the Chinese government with a list of Chinese companies the United States suspects of violating U.N. sanctions related to the development of Iran’s missile technology and nuclear capabilities. Einhorn’s delegation also pressured the CNPC and the China Petroleum and Chemical Corporation to cease or significantly reduce their investments in Iran. However, the delegation did not ask China to stop purchasing oil from Iran (Pomfret, 2010). In May 2011, approximately eight months after Einhorn’s visit to China, the United States sanctioned seven foreign companies for selling gasoline to Iran under the 2010 Comprehensive Iran Sanctions, Accountability and Divestment Act. Not a single Chinese company was sanctioned “despite the fact that China supplies about a third of Iran’s imported gasoline” (Slavin, 2011). Despite the rhetoric, the United States understands that it may no longer be powerful enough to force China to act against its national interests. Also, if China stops buying oil and gas from Iran, then the U.S.-China rivalry for energy resources would likely intensify in other states of the Middle East and beyond.

Iraq: United States Pays the Bill for China’s New Energy Market

While Saudi Arabia is the oil market’s swing producer, Iraq, which has the world’s fourth largest proven reserves with 115 billion barrels, is the wild card. Although Iraq’s oil infrastructure is desperately in need of repair and upgrade, contracts to private companies are now in place that could theoretically take the country’s oil production from a current level of approximately 2.5 million barrels per day to over 12 million barrels per day by 2017 (Hafidh, 2010). As such, Iraq is the country where the U.S.-China energy rivalry has the greatest potential to intensify. While the United States has paid dearly in blood and treasure for the war that toppled Saddam Hussein, China is quietly positioning itself to reap the energy benefits of that war.

For the United States, the cost of its involvement in Iraq to date is staggering. By the end of fiscal year 2011, the Congressional Research Service projects the United States will have spent $801.9 billion on the war, while more than 4,400 of its military personnel have lost their lives and approximately 32,000 have been injured (“Iraq War,” 2010). When examining the total impact of the war, economist Joseph Stiglitz projects the final cost could be closer to $3 trillion (Bilmes & Stiglitz, 2008).

Yet when it came time to sign its first major post-Saddam oil deal, the Iraqi government chose the partnership of CNPC and British Petroleum to develop its 1.1 million barrel per day Rumaila field near Basra (Wan, 2009). CNPC also received a 22-year, $3 billion service contract to help with the development of the Ahdab oil field southeast of Baghdad—an award that was a renewed version of a 1997 agreement China had with the Saddam Hussein regime (Goode & Mohammed, 2008). A year later, in late 2009, a partnership involving CNPC, Malaysia’s Petronas, and France’s Total received a contract for the Halfaya oil field in southern Iraq, which has reserves of 4.1 billion barrels and a production potential of 535,000 barrels per day (“Iraq Oil,” 2009).
China’s initial success in Iraq also extends to the Kurdish Autonomous Region. Sinopec Group acquired the Swiss energy company Addax in August 2009 and gained access to two oil fields in northern Iraq. Addax has “a 30% interest in a Production Sharing Agreement (PSA) for the Taq field” and “a 26.67% working interest in the Sangaw North PSC” (Addax Petroleum, 2011).

According to Falah al-Amri, Director General of Iraq’s State Oil Marketing Organization, the country’s oil exports to Asian markets increased from 25% in 2006 to a current level of more than 60% (Lando, 2011). While the United States continues to pour billions of dollars into Iraq for results that are hardly tangible, China is investing in the country’s energy industry—a move that is likely to help Beijing secure access to greater energy resources while returning a profit for its NOCs. If China’s NOCs continue to outperform U.S. companies in Iraq’s expanding energy market, then tension between the two countries could escalate, particularly in light of the billions of dollars the United States spent on security and reconstruction in Iraq.

Some experts believe China’s involvement in Iraq’s oil industry represents a positive step that gives Beijing greater incentive to work for stability in the region. Mark Thirlwell, Program Director for International Economics at the Lowy Institute for International Policy, opines, “If you want China to be a responsible stakeholder in the world, you need to let China buy stakes in the world” (Bradsher, 2009). Even if U.S. companies do not directly benefit from Iraq’s expanding oil and gas production as much as they anticipated, the U.S. government has a vested interest in Iraqi energy production being back in the market at full strength to ensure adequate supplies that will buffer against price spikes, which could threaten U.S. and European attempts to recover from the economic recession of 2008.

Potential Threats to China’s Energy Acquisition in the Middle East

China’s strategy for energy acquisition in the Middle East faces several potential threats. First, as it goes further downstream and becomes more deeply embedded in the economies of the region, it will be harder to walk away from any supplier without causing itself severe energy and economic hardship. If a supplier from the region becomes a political liability and China has billions invested in its economy, then Beijing may have to abandon the “offend no one” policy in order to protect its investments and ensure adequate energy supplies. Ironically, the more successful China is at securing energy from the Middle East, the more dependent it will become on the region, which increases the likelihood that Beijing will soon encounter a geopolitical issue that challenges its current energy strategy.

Second, as the competition for global resources intensifies in the 21st century, China is almost certain to eclipse the United States as the largest consumer of oil and to further distance itself as the world’s largest consumer of energy. This new dynamic will present a host of possibilities in a world where the pursuit of energy security will likely become one of the driving forces mediating relations among countries (Klare, 2009). The expanding Chinese demand for imported energy sources renders it vulnerable to disruption of supplies overseas that could be triggered by chronic political instability in the Middle East.
Some scholars contend there is an emerging alliance of otherwise ideologically disparate nations in whose ranks are both consumers and producers of energy, namely energy consumers such as China and India and energy producers such as Russia, Brazil, Iran, and Saudi Arabia that constitute a new Second World, replacing the old communist bloc. The Second World is now challenging the Washington consensus and its hegemonic policies on a wide range of issues (Khanna, 2008). In this "post-American world," wealth and power is shifting away from the United States and dispersing in multiple centers where multipolarity and non-polarity co-exist (Zakaria, 2008, pp. 1–5, 77–86). China is an active and conscious participant in this process, using its assets and resources to bring to fruition this multipolar world that serves its interests and ideological predilections. This new paradigm may escalate tensions between the United States and China and spawn political confrontations. The current U.S. strategy to move some of its military assets and capabilities to the Asia-Pacific theater of operation in recognition of China’s continued economic and military rise indicates Washington’s assessment of the potential Chinese threat to its national interest in that part of the world.

Finally, Beijing’s energy security and continued economic growth could be threatened if a significant portion of the country’s 1.3 billion citizens becomes disillusioned with Beijing’s push for rapid development or feels excluded from China’s newfound wealth and global power. Over the past decade, Beijing’s foreign currency reserves have increased to $3 trillion. Most of that money is invested in U.S. Treasury bills and other foreign assets. At the same time, Beijing’s monetary policies have kept China’s currency undervalued, which has served the nation’s export industries and its energy acquisition strategy, but at the expense of domestic development. At some point, wages and standard of living must increase substantially in China, which still has a gross domestic product per capita of just $8,400, or Beijing faces the increasing likelihood of civil unrest at home.

All of these factors are contributing to an internal foreign policy debate in China regarding the country’s future direction as an economic superpower. Some advocate staying the course of the “peaceful rise” and “offend no one” strategies, while others argue that China now requires greater military strength to protect its significant economic interests throughout the world—a direction that could ultimately make it a new hegemonic power to rival the United States.

**Conclusion**

The present competition between China and the United States over oil and gas resources of the Middle East is pregnant with opportunities for great power cooperation as well as conflict. Thus far China’s government has successfully exploited tensions between the United States and major energy producers of the region, while using the country’s extensive cash reserves to secure access to resources and to create a network of energy infrastructure that will channel vast quantities of oil and gas to the mainland. At the same time, the United States, which has a recent history of military conflict in the region and a national debt of more than $14.7 trillion, is seeing its energy acquisitions and influence in the Middle East decline.
Scholar Hongyi Harry Lai argues that the U.S.-China rivalry for oil in the Middle East is not cause for concern since the United States now imports most of its oil from Canada and Mexico, and only about 15% from Arab OPEC nations (Lai, 2007, p. 531). However, as global demand for energy continues to increase and supplies become tighter, the United States may have no choice but to seek greater quantities from the Middle East. When that time comes, China’s position in the region may be even stronger, which will result in one of three scenarios: the United States will have to look elsewhere for energy, China and the United States could cooperate in the Middle East to deliver greater quantities of energy to the global market, or competition between the two petro-powers could intensify to the point of conflict.

As the U.S.-China energy rivalry intensifies, there is one critical point that cannot be discounted: the United States benefits from the output of China’s energy acquisitions. Countless products manufactured in China and exported to the United States are a mainstay of the U.S. lifestyle. Those products are only available and affordable because China has a lower labor cost than Western countries and is currently able to obtain adequate supplies of energy for its manufacturing facilities. In this respect, China’s energy acquisitions are often in the best interest of the United States. As such, a new era of cooperation makes sense for both countries. China’s abundance of capital, coupled with U.S. military strength and technical expertise, could form a powerful alliance, capable of delivering greater supplies of energy to the global market. As Charles Ziegler (2011) points out, “Diversifying supplies and bringing more oil onto the international market is in the interests of all major energy consumers, by contributing to stable flows and moderating prices. There is a strong incentive for major energy consumers to cooperate, if they can move beyond a mercantilist mindset that views the world energy markets in terms of relative gains” (p. 207).

Some signs of this more cooperative attitude on both sides are emerging. Whereas the United States adamantly opposed China’s attempted acquisition of Unocal in 2005, in November 2010, CNOOC invested $2.16 billion to acquire a 33.3% interest in 600,000 net acres in the Eagle Ford Shale of South Texas owned by Chesapeake Energy Corporation (Jiang & Sinton, 2011). Additionally, according to the most recent reports, China is scaling back on its investment and work in Iran’s energy sector, drawing anger from the Iranian government (Aizhu & Buckley, 2011). This seems to be a clear attempt to appease Washington, as were China’s votes in favor of four sets of U.S.-U.N.-imposed sanctions against Tehran. The key to a policy of cooperation is for the United States to change the current dynamic in the Middle East, where U.S. hegemony, coupled with its unwavering support of Israel and Washington’s tendency for unilateral action, present China as the more reasonable and desirable partner for major energy-producing states such as Saudi Arabia, Iran, and Iraq. Changing this dynamic will require the United States to limit its use of military force in the region, while making a genuine push for Palestinian statehood and abandoning unilateral action in favor of multilateral initiatives. Such a course of action would likely restore U.S. standing in the region and facilitate its future access to energy resources, while stemming China’s rapid rise in the region and rendering it more amenable to greater cooperation in the future.
A potentially fatal flaw with the current Chinese energy strategy of working with states not aligned with U.S. interests is that China could be creating long-term instability in key energy markets. By turning a blind eye to corruption and failing to hold energy-producing states accountable for human rights violations, China could be helping to sustain the next generation of energy autocrats in the mold of Saddam Hussein and Moammar Gadhafi.

The U.S. strategy of offering other countries arms and military protection as a primary incentive for political and economic cooperation has its limitations as well. The strategy only works if nations agree there is a clear threat to their sovereignty. Also, given the instability of the region, weapons sold to a regime friendly to the United States may end up in the hands of a future regime that is hostile toward Washington.

By the sheer volume of its energy acquisitions and the billions it is investing in the Middle East, China will inevitably become more deeply entangled in the geopolitics of the region. If China is simply purchasing oil and gas from countries like Iran and Sudan and the global pressure against it becomes too great, it can simply switch to other suppliers. However, as China increases its investments in refineries and pipelines and expands bilateral trade in nonenergy sectors, it will become much more difficult to walk away from any single producer. These partnerships will require China to defend or oppose its energy partners’ positions on sensitive geopolitical issues, such as Iran’s nuclear ambitions. At some point in the not too distant future, developed countries will no longer give China a free pass as a struggling, developing country. As China further establishes itself as an economic superpower, the world will hold Beijing to a higher standard. And if China chooses to support authoritarian states solely for the purpose of satiating its own thirst for energy, then Beijing will lose credibility in the global community and risk isolation.

Whether the U.S.-China energy rivalry is headed toward cooperation or conflict remains to be seen. What cannot be disputed is that a realignment of great powers in the Middle East is well under way. Through its impressive rate of economic growth, increasing energy acquisitions, and vast foreign currency reserves, China has emerged as a powerful player in the Middle East. Despite its rise, Beijing understands that the major energy-producing states in the Middle East, particularly Saudi Arabia, Iran, and Iraq, have successfully reclaimed ownership of their resources from Western energy companies, and these states will ultimately play a significant role in determining the outcome of the global competition for resources by choosing which NOCs or corporations have the privilege of purchasing their oil and gas and investing in their energy sectors. Lacking a history of colonial dominance and unhampered by the political cost of military involvement in the region, Beijing is attempting to build strategic relationships and mutually beneficial partnerships with major regional energy producers that would serve its long-term interests and sustain its impressive economic rise on the global stage.

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China’s Strategy for Energy Acquisition in the Middle East


