

# China's Energy Cooperation with Middle East Oil-producing Countries

QIAN Xuewen<sup>①</sup>

(Middle East Studies Institute, Shanghai International Studies University)

***Abstract:** China is rich in coal, but insufficient in petroleum and gas. The energy shortage is not a general shortage but a structural imbalance. In recent years, China's dependence on foreign oil supplies keeps increasing to meet the needs of China's rapid economic growth. China's top leadership, for this goal, has committed itself to energy diplomacy and vigorously promoted China's energy cooperation with Middle East oil-producing countries. In the current conditions, carrying out energy cooperation with the Middle East oil-producing countries is inevitable and beneficial to China's security. China and the Middle East oil-producing countries have maintained friendly and cooperative relations: mutual political, economic complementarities and cultural fusion, which create a favorable environment for cooperation for extracting and removing the Middle East oil. As for the problems and difficulties exposed in carrying out energy cooperation in the Middle East, China should bravely face them and seriously resolve them.*

***Key Words:** China; Energy Cooperation Diplomacy; Middle East Energy*

## I. China's Oil Supply Security and the Middle East Oil

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<sup>①</sup> QIAN Xuewen, Professor of Middle East Studies Institute, Shanghai International Studies University. This research is the product of Chinese Educational Ministry program "China's National Interest in the Middle East (Western Asia and Northern Africa)" (2009JJJD810010).

Promoting diversified development and strengthening mutually beneficial cooperation in international energy is one of China's energy development strategies. In the process of China's energy development, being different from development and utilization of other energy, the oil industry has its own particularity. In China's energy consumption structure, the proportion of coal is, for a long-term, high. In 2005, the consumption of coal accounted for 68.7%, oil and natural gas 24%, hydropower and nuclear power 7.3% (Qiu, 2007: January); In 2009, the consumption of coal represented 70.3%, oil 18.0%, natural gas 3.9 %, hydropower, nuclear power and wind power 7.8% (National Bureau of Statistics, 2010: May).

The situation remains the same. The ratio of oil and coal is close to 1:3, but their contribution rate to China's economic development is self-evident. The consumption structure of coal-based shows that China is still in the low efficient and poor benefit Coal Age, which remains outside the main trend of world development energy. It produces an adverse effect on China's economy, utilization of energy, the ecological environment and the quality of people's life. China's energy shortage is not a general shortage, but a structural shortage. From the structure of energy storage, China is rich in coal, but insufficient in petroleum and gas. The petroleum shortage can not be replaced by coal or other energy in the short term. To protect its economic security, China must give priority to protecting the security of its oil supply. In addition, due to the limit of resource conditions and producing capacity, China's domestic oil producing capacity has reached the maximum 200 million tons. The consumption of oil will grow rapidly owing to economic development. When domestic producing capacity remains the same or increases slightly, the growing consumption of oil in future will increase the China's oil consumption gap and the dependence on import of oil.

According to the National Development and Reform Commission statistics data, China's crude oil production was about 189.4 million

tons in 2009, which can only meet half of domestic demand. The Ministry of Land and Resources announced that China has become the 4th largest oil-producing country in 2009, next to Russia, Saudi Arabia and the United States, accounting for 5.4% of world crude oil production. According to information released by China's General Administration of Customs, China imported a total 204 million tons of crude oil in 2009, the ratio of dependence on oil reached 52%, the highest in history, up 13.9% on 2008 (the same below). The imports of crude oil worth 89.26 billion US dollars, down 31%; import average price was 438 US Dollars per ton, down 39.4%. The top three sources of imports were Saudi Arabia, Angola and Iran. Among them, China imported crude oil of 41.86 million tons from Saudi Arabia, up 15.1%; Angola 32.17 million tons, up 7.6%; Iran 23.15 million tons, up 8.6%.

If taking the refined oil into account, China's dependence on foreign oil was even higher. China's rapid economic development constituted one cause of the increasing dependence on foreign oil. Besides, the resource condition of oil producing is a severely restraining factor. According to the estimation of Yan Luguang, an academician of CAS, China's oil consumption will exceed 800 million tons in 2050, while domestic oil production due to constraints of resource and capacity, will stabilize at about 200 million tons in annual production. The ratio of dependence on foreign oil will reach 75% (Liu, 2007: June). China's current crude oil production is nearly 200 million tons and has no space to increase. This means that in future years, China must continue to promote oil production cooperation with foreign countries thus effectively solving the growing shortage of oil supply.

The preferred way of obtaining foreign oil is cooperative exploitation, and the second choice is engaging in import trade. For the development and utilization of oil and gas resources in the Middle East, Chinese experts have persistently different views. The situation in the Middle East is complex and long-term instable; therefore quite a few experts have advocated the diversification in oil sources as soon

as possible, avoiding undue reliance on Middle East oil and gas. They also claim that China's dependence on foreign oil should be controlled within 1 / 3. Then, China imports its oil from Russia, Central Asia and the Middle East (Mei & Wang, 2005: 248-250). This program is actually a bit idealistic. From the current situation, Russia and Central Asia cannot achieve the immediate goal of the experts, let alone the achievement of long-term goals. At present, in the field of storage and production of the oil and gas, the Middle East oil-producing countries' main force status cannot be replaced. In terms of oil prices, transportation and geographic factors, the Middle East oil should be China's main source of oil. Although in recent years, oil production in Central Asia, Africa increased, the Middle East crude oil is still dominant in the world oil market. The resource conditions and production in central Asia, in any case, can not meet China's 1 / 3 of the external demand for oil (Qian, 2007: May). Thus, under current conditions, it is inevitable that China should carry out cooperation with Middle East oil-producing countries or list the Middle East oil as a source of China's

According to incomplete statistics, the following is the situation of China's crude oil import from major Middle East oil-producing countries:<sup>②</sup>

Origin	2008 (million tons)	2007 (million tons)	Up % on previous year	prospect ( million tons)
Saudi Arabia	36.37	26.33	38.1%	50
Iran	21.72	20.54	5.7%	
Oman	14.37	13.68	5.0%	
Sudan	10.21	10.31	-1.0%	
Yemen	3.96	3.24	22.2%	
Libya	3.48	2.91	19.6%	

<sup>②</sup> According to the information form Internet, for reference only.

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Algeria	0.70	1.61	-56.5%	
Kuwait	5.90	3.63	47.7%	25
Iraq	1.57	1.41	11.3%	
Total	98.28	83.66	17.5%	
Total imports of oil products	200.67	196.80		
proportion	48.98%	42.51%		

The table does not include the data of UAE and other countries. if coupled with imports from these countries, China's imports of crude oil from the Middle East were certainly more than 50% of total imports in 2008.

In 2009, Middle East oil-producing countries' proved oil reserves were 112.199 billion tons, accounting for 60.48% of total world reserves. The proved oil reserves of West Asia were 103.2 billion tons; the proved oil reserves of North Africa were 8.999 billion tons. Oil production of the two areas was 1.244 billion tons, accounting for 37.25% of world oil production, up -0.1% on previous year. The oil production of Western Asia, North Africa was 1.044 billion tons and 0.2 billion tons respectively (Liang, 2010: January).

Currently, China is actively pursuing the policy of diversification in energy sources. From the reality of energy supply, the Middle East has been the main source of China's overseas oil. The resources in other areas or countries are supplementary resources for diversification.

It is inevitable and safe that China promotes energy cooperation with Middle East oil-producing countries. The Arab countries are main oil producers in Middle East. In the past, Arab national cohesion and the specific cohesion of the Islamic Muslims, have been the underbelly of the over-concentration of energy sources. But now the geopolitics of Middle East countries has already changed. Under the Western power politics and the strong cultural impact and influence,

the original cohesion of Arab countries and traditional culture have disintegrated. More over, Iran had a long-term discordant relation with other Middle East oil-producing countries. Therefore, currently, China engages in cooperation with the Middle East oil-producing countries which should not be seen as a tight unit, but with the different independent countries upholding their own interest. Middle East oil-producing countries are now no longer monolithic. The case in which they carried out joint operations to deal with western countries in the 1970s was already history. In current conditions, carrying out energy cooperation with Middle East oil producing countries need not worry about the growing dependence on external oil, as China should further increase the diplomatic efforts in the Middle East energy. Obtaining the oil from the Middle East should be regarded as an effective measure for diversification of sources. No matter what point of view, it should be safe.

## **II. The Process of Energy Cooperation between China and Middle East**

After July 2004, China negotiated with the Arab Gulf Cooperation Council on the establishment of a free trade zone. By the end of December 2005, Kuwait's oil minister and OPEC delegation visited China; in January 2006, King Abdullah of Saudi Arabia came to China. In April 2006, President Hu Jintao with a delegation paid a return visit to Saudi Arabia and OPEC member Nigeria. Through the frequent contacts of state leaders of both sides, it is not difficult to conclude that China needs a continuous oil supply from the Middle East while the Middle East needs this huge oil consumption market.

China's energy diplomacy gained immediate results. In a project bidding of gas exploitation in Saudi Arabia's desert region, Sinopec beat American companies, becoming one of the four authorized mining companies in that region. In addition, when the project of China-Myanmar oil line had no result after long-term discussions,

Chinese oil companies decided to open a new path, through Gwadar Port of Pakistan, transporting the oil from Saudi Arabia, Iran to Xinjiang. Thus it strengthened the marine security of the Malacca Straits. In Fujian Province, China, a 3.5 billion US Dollars oil refinery, invested by Sinopec, Exxon - Mobil and Saudi Arabia, commenced construction. In addition, Saudi Arabia was also prepared to invest in some of the oil reserves and oil refining project in Hainan, Qingdao, and Dalian. These projects constitute the basic framework for energy cooperation between China and Saudi Arabia.

By the end of 2005, Kuwait and China signed a "Memorandum of Understanding", which intended to invest 5 billion dollars in building a joint venture oil refinery near Guangzhou. It was designed to process 30 million barrels of crude oil from Kuwait per day. Once the refinery project is passed, it will exceed the CSPC Nanhai petrochemical project in which 4.3 billion dollars were invested, and it will be China's largest joint venture project. On March 29, 2006, Kuwait Oil Company set up offices in Beijing and had close contact with Chinese oil companies. It was a win-win result. China's "going out" strategy not only promoted the cooperation with the oil-producing countries, but also attracted capital and technology of oil-producing countries in China's petrochemical project, which resulted in a symbiotic relation with oil-exporting countries.

Ignoring the will of the Americans, Kuwait invested in China and pursues the energy cooperation, which set a model for other Middle East oil-producing countries. All the other Middle East oil-exporting countries followed to contact with China that promoted the energy cooperation between China and the Middle East. On May 22, 2007, China Gas Holding and its shareholders, Oman national oil company signed a strategic joint venture agreement involving imports of energy products from the Middle East to help China Gas Holdings to obtain stable energy supply. The joint venture's authorized capital totaled 40 million US dollars, with each holding 50% equity in the joint venture (Tan, 2007: July). On May 23, world-class supplier of ethylene---Qatar

Petrochemical Co., Ltd. established its fifth office in Guangzhou, and in the following Beijing, Shanghai, Taiwan and Hong Kong. At present, in the South China market its main product of ethylene is in short supply (Li, 2007: May). On June 20, Iraqi President Jalal Tabarani visited China. During the visit, the Iraq oil ministers consulted with China on the investment in Iraq's oil fields. This consultation has not yet led to agreements, but the Iraqi ambassador made it clear that the coming of an "oil law" would open the Iraq oil fields to international companies, and China will become one of the beneficiary countries. A frozen oil contract between China and Iraq, signed in 1997, will soon be activated (Chen, 2007: June). The facts show that energy cooperation between China and the Middle East oil-producing countries have entered a new period with increasing and large-scale cooperation projects.

### **III. The Challenges and Problems in Energy Cooperation between China and Middle East Countries**

The situation in the Middle East has always been volatile, and the conflicts have been very complex. The world's great powers and the world's major oil companies competed for their profits in the Middle East. The competition was increasingly fierce in the background of the deepening globalization. Therefore, in the process of cooperating with Middle East countries, China encountered various complex constraining factors.

1. The great powers intervened in the Middle East to constrain China's energy cooperation. Presently, the turmoil of Iraq, the closed Israeli-Palestinian peace talks and the turbulent Lebanese politics lead to an uncertain situation in the Middle East. Under this background, the great powers, driven by political, economic, security factors, intervened in the Middle East affairs, increased their competing efforts, considered the Middle East as the key part of its global strategy. US focus on establishing a new world order dominated by him. The



overall goal is "relying on America", "dominating Asia" and "controlling the Middle East". Through the "road map", "two war fields", "three diplomatic supports", the US exerted pressures on the Middle East step by step. Taking energy cooperation as the starting point, the EU actively involved in Middle East affairs. They viewed the Middle East as a tool for seeking an important position in the world. For more than a year, the diplomatic actions of the EU in the Middle East were extremely active. On the Iranian nuclear issue, Israeli-Palestinian conflict and other Middle Eastern affairs, the EU kept an appropriate distance from the United States, highlighting its political independence, and trying to break the dominance of the US, the EU expanded its sphere of influence on the Middle East. The Middle East area is the strategic relationship to Russia. These areas also ease and balance the US strategy of squeezing the Russian strategic space in Central Asia. Properly dealing with the Middle East affairs is expected to improve their own geo-strategic situation and to constrain NATO and the EU. Taking the Iranian nuclear issue and the Palestinian-Israeli issues as starting points, Russia implemented a pragmatic diplomatic policy on the Middle East. In some issues, Russia stood in the opposing positions of the United States to resist the infiltration, control and pressure of the Western countries (Huang, 2006: December).

The Middle East oil is a crucial strategic material of big countries for economic development and their national power. So the United States, the European Union, Russia and Japan, spared no effort to strive for their own strategic interests in the Middle East energy, and their political, economic and military effects on the Middle East have been deep-rooted. Being wary of China's and other countries' energy cooperation in their orbit, the four countries strived to prevent their own orbit from meddling by outcomers; especially the United States' actions are the most prominent. The United States has always regarded China's energy cooperation with Middle East oil producing countries as a threat to its energy and global strategy. Therefore, the

U.S has always taken the attitude of containment and exclusion to China's energy cooperation in the Middle East region. In addition, Western countries, including Japan with its Western orientation, sought and maximized their own benefits according to their strategy. They created obstacles for China's energy cooperation with the Middle East. After the Iraq war, the United States greatly enhanced its control of the energy in the Middle East, which was more detrimental to China. It helped the US to constrain China's normal energy cooperation in the Middle East.

2. The complex and uncertain regional situation increases the risk of China's energy cooperation with Middle East countries. The Middle East is an "energy bank", a "powder keg", a conflicting vortex over half a century, a region where ethnic, religious and political disputes tangled. China should have adequate mental preparation and response measures to the profound and complex evolution of regional patterns, increasing uncertainties and safety problems.

3. The threat of foreign ethnic separatist forces has caused some Middle East countries turned a blind eye to the "East Turkistan" separatist forces so long as they do not endanger the local regime. This attitude contributed to the ethnic separatist forces' arrogance and power and brought the potential negative effects onto China's domestic security and stability. In addition, wars and turmoil in the Middle East, also caused the damaging effects on China's investment in the region as well as service and commodity exports.

4. Oil producing countries including Saudi Arabia and Kuwait, have the desire to conduct energy cooperation with China, the realization of their potential oil export should overcome various problems. In the Middle East countries, China has conducted energy cooperation for many years. In recent years, various Chinese delegations visited the Middle East countries for negotiating oil and gas projects, but the outcome moves slowly and is so far unsatisfactory. Owing to a variety of reasons, it is hard to carry out the substantive cooperation in large-scale projects, except in some countries, such as

Sudan and Iran. Some of projects are even in the technical and economic feasibility stage. It is understood that Iran tends to take advantage of its energy, when dealing with its relations with China. Seldom can contracts or orders of substantive cooperation project be signed.

5. Chinese oil companies should further strengthen their coordination and communication with China's overseas diplomatic institutions. In the beginning of the twenty-first century, the former Chinese Foreign Minister Tang Jiaxuan said that China's diplomacy was going to be the oil diplomacy in the next period. Since then, when China's leaders visited around the Middle East, China's oil diplomacy has made impressive achievements. In 2006, China's energy diplomacy reached its climax. All the openings of four main diplomatic policies for oil were followed by a series of closely related diplomatic arrangements. China's oil diplomatic strategy advocates the healthy competition under a harmonious world. First, China should cooperate with OPEC, Russia and the United States and other powerful players in the energy field. Secondly, China also needs to work with Iran, Sudan, Angola and India and other disadvantaged players thus promoting the establishment of new rules (Xie, 2006: September). However, the cooperation between its oil companies and overseas institutions was short of understanding and communication. They complained to each other, which is a discordant note that should not appear in China's oil diplomacy and energy cooperation with the Middle East countries.

6. Underestimating the status and influence of Chinese companies' participation in international cooperation projects and lacking the guidance of diplomatic policies, the Chinese government has not produced a long-term energy developing strategy. Therefore, in the fiercely competitive and changeable market, Chinese oil companies often have committed some mistakes, such as a lack of experiences, betraying each other and responding slowly to problematic situations. All of that results in an inefficient cooperation.

Then, some Chinese companies lack the sufficient material and mental preparation for investigating the resource supply countries, easily believing in the information of western countries' agents, thus resulting in being cheated by the agents. Finally, some Chinese personnel involved in negotiations can not adapt themselves quickly to changing situations, and lack the experiences of foreign affairs. They just say something good and avoid discussing the problems or intend to ignore the problems. Sometimes they can not make a counterattack against the agents' unreasonable demands, which leads to an unsatisfactory result (Qian, 2007: 471).

#### **IV. The Historical Opportunities for Carrying Out Energy Cooperation with the Middle East Countries**

After the 9/11 tragedy, there were cracks in relations between the United States and Middle East countries. The Iraq war cast a shadow over relations between the United States and the Middle East oil producers, which gave the best opportunity for the Chinese oil companies for strengthening cooperation in energy development with the Middle East oil producing countries.

First, the Iraq war severely exacerbated the ethnic and religious sentiments in the Middle East. The Middle East countries worried about that the US Greater Middle East Initiative, a western-style democratic reform which could shake the foundation of their monarchical regimes. They also were concerned whether Iraq, manipulated by the United States, could restore the oil producing capacity of 500 million barrels of crude oil per day before the Gulf war. However, Iraq might surpass Saudi Arabia in its oil producing capacity, becoming the biggest oil producing country. Then, it would endanger OPEC's major source of income through dominating the oil pricing and market shares allocation which is controlled by OPEC. At this point, the United States' interests are different from Saudi Arabia's and other Middle East oil producing countries. So it is taken for

granted that these oil producing countries are keen on finding a new partner. Secondly, the Middle East needs to have a stable market. As a rapidly growing developing country, China demands vast amounts of energy and has a great potential market. Moreover, China has maintained long-term cooperative relations and friendship with the Middle East countries. At present, Saudi Arabia, Kuwait, Iran and other Middle East oil producing countries are gradually breaking the monopoly of the national power, and are carrying out their resource project by inviting public bidding (Chun, 2004: August). Therefore, the domestic energy experts believe that the time is ripe for China strengthening energy cooperation and with Middle East oil-producing countries. In addition to these conditions, energy cooperation with the Middle East is also supported by the following two conditions:

1. China pursues a balanced Middle East policy which is well received by the countries in the region. China, as a permanent member of the Security Council and the largest rapidly developing country, is playing an increasingly important role in the international arena and Middle East affairs. China is winning the appreciation and support of the majority of Arab countries. Until now, China has established official diplomatic relations with all the countries in the Middle East region, and has maintained friendly and cooperative relations with them. All of these developments have laid a solid political foundation for the launch of China's energy cooperation with Middle East countries and successfully created a good atmosphere and overall environment for China's oil imports from the Middle East.

2. The Middle East countries are envious of the fact that China's economy is growing rapidly and its overall national strength is increasing, and they are confident in cooperating with China. Hence they are happy to see the oil flowing to the Chinese market. Middle East oil producers generally have an optimistic expectation about China's huge demand for oil markets. After the 9/11 situation, the Arab oil-producing countries have had strong dissatisfaction with the Western countries represented by the US, trying to change the

situation of over-reliance on Western powers and passive economy. They are suggesting that the strategy of economic energy development cooperation should turn toward the oriental regions. The main consideration is to ensure the security of energy output. Through the expansion of cooperation with Asian countries represented by China in the oil fields, they can achieve the diversity of oil exploration, development, production, sales and market flows. Then they can take advantage of other parties' power including China's to contain the hegemony of the US, ease the pressure from the US and achieve their political goals.

## **V. Some Advice for Cooperation with the Middle East Countries**

1. In the various Middle East Oil-producing countries, the production capacity is different. In the current conditions, China should engage in energy cooperation without considering the amount of oil to be obtained for political purposes, some Middle East oil-producing countries have expressed a willing trend of strengthening cooperation, hoping that China can speak out from justice on the Middle East issues. China should maintain a clear understanding to this issue, making flexible and pragmatic responses. Under current conditions, it is difficult to immediately obtain the big projects in Saudi Arabia, Kuwait, UAE, Iraq and other Middle East oil-producing countries. Engaging in joint development also has existing obstacles. Therefore, China should stick to its position, maintaining the existing foundation, and then seeking development--- as in Sudan for example. In 2006, its new oil proved reserves increased by 788.10%, which is no doubt good news to Chinese oil companies.

2. The Chinese government should give diplomatic support and strengthen the macro guidance to Chinese oil companies' participation in exploiting the Middle East energy resources. In this regard, China

must establish a energy development strategy which coordinates the central and the local needs and face the world market as a relatively independent energy management sector as soon as possible. Aiming at problems exposed in the Chinese oil companies' working and operation, the Government should give regular supervision, inspection and guidance to these domestic companies and guarantee that they minimize the risk involved in the project in order to reduce the loss of national interests.

3. China's oil companies and overseas institutions should strengthen coordination and cooperation. In particular, they should introduce the appropriate, flexible, and the necessary incentive mechanisms. The diplomatic institutions should play a full role as a bridge between domestic and international markets. In this incentive mechanism, China's diplomatic service and foreign institutions should keep pace with top leadership, actively implementing energy diplomacy, and vigorously promoting energy cooperation the Middle East.

4. China should adhere to a "going global" and "bringing in" policy. When Chinese oil companies go out to carry out cooperation, China also needs to bring in the capital of the Middle East oil-producing countries in order to invest in domestic oil project, so that it will reduce the threat of changes in the world oil market to China.

5. The recent financial crisis gave a golden opportunity to China. It previously had been greeted with much bigotry and harassment. However, after the crisis, China was suddenly pushed to the front to the stage, and became responsible for international obligations. Its international status and roles greatly changed. In this situation, China should seize this favorable opportunity to improve its energy cooperation with the Middle East oil-producing countries, serving the country's economic development and assuring the economic security.

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