

Fueling the Dragon's Flame:

How China's Energy Demands Affect its Relationships in the
Middle East

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-K. Douglas, M. Nelson, and K. Schwartz

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1. INTRODUCTION

As a major oil consumer, the People's Republic of China (PRC) has turned outward, cultivating bilateral relationships with states that can literally fuel China's rapidly growing economy. This paper deconstructs China's foreign policy towards supplier states in the Middle East—especially Iran and Saudi Arabia—in an effort to assess China's grand energy strategy. It rejects the view that China can successfully pursue a “neo-mercantilist” strategy of securing reserves. It will evaluate whether China's “no strings attached” commercial relationships with unsavory regimes threaten global security. Finally, it will consider the strategic challenge posed to the U.S. by the emergence of China in the Middle East. The paper concludes that a policy of active engagement and support for China's increasing diversity of energy sources can help prevent harm to U.S. economic interests. It can also constrain China's incentive to take bilateral relations with energy suppliers to the level of security guarantees, which would challenge U.S. military supremacy in the region.

China's disregard for the human rights abuses and other violations of international norms by oil supplying states such as Sudan and Iran, and its opposition to the imposition of sanctions by the UN on these states, has prompted some western powers to criticize the PRC for exploiting what has been termed the ‘morality gap’. The PRC's uncritical engagement of Syria, Iran, and Sudan has raised questions about Beijing's ability to be, in the words of Former U.S. Deputy Secretary of State Robert Zoellick, a “responsible stakeholder.”¹ Indeed, so long as Beijing pursues commercial interactions without regard to the odious behavior of its foreign partners, it will be perceived in some quarters as defying international moral standards and contributing to instability and lawlessness.

Nowhere is this issue now more apparent than in relations between China and Iran. China and Iran first became strategically aligned as a result of Chinese arms sales in the 1980s. The two countries share a similar narrative as historically great civilizations whose progress toward modernity was retarded by Western infringement, but the friendship is also built on commercial interests and a mutual commitment to a multi-polar world to blunt U.S. influence. Iran views its friendship with China as vital to its continued ability to resist pressure from the West and endure sanctions. It has worked to expand its relationship with China to include military assurances, for which China has shown little interest. China views Iran as an important partner in China's plans to develop overland routes to transport oil from the Middle East. Moreover, a strong partnership with Iran has enhanced China's capacity to become an important player in Middle Eastern affairs. Although China recognizes its relationship with Iran may cost it international prestige and threaten Sino-U.S. relations, it has thus far shown unusual willingness to support Tehran.

A new element in the Sino-Iranian relationship is the emergence of the Shanghai Cooperation Organization (SCO), to which China is a member and Iran is an official observer. The SCO is the most public forum where Iran and China have the opportunity to work toward common economic, political, and military goals. Understanding the SCO's rapid emergence is vital to

¹ Zoellick expanded on this point, saying “China should take more than oil from Sudan – it should take some responsibility for resolving Sudan's human crisis.” Robert B. Zoellick, Deputy Secretary of State, “Whither China: From Membership to Responsibility?: Remarks to National Committee on U.S.-China Relations,” New York City, September 21, 2005.

assessing Sino-Iranian relations. This partnership of states is working to build energy and military cooperation in Central Asia and has also emerged as a forum to express opposition to American influence. Although some experts have asserted that this group could evolve to be as militarily significant as NATO and as energy dominant as OPEC, there are a number of barriers that make such a result unlikely.

China's partnership with the House of Saud is far more recent, as Saudi Arabia was one of the last countries in the Middle East to establish diplomatic ties with China, in 1990. Relations between the two countries remained cool through most of the 1990s. Bilateral ties have been strengthened considerably since then, with China emerging as an important buyer of Saudi oil, a willing investor in joint production and refining projects, and a supplier of arms and ammunition. To the Saudis, China's growing demand for oil and lack of attendant political pressure is an attractive hedge against their traditional reliance on the U.S. market. China, in turn benefits from supply source diversification and the reliability of Saudi production. While strengthening relations between these two states may allow Saudi Arabia to distance itself somewhat from the U.S., it is less likely to have any lasting strategic impact on U.S. interests in the region. U.S. oil imports from Saudi, and more importantly U.S. naval supremacy in the region, will not be challenged by China. Moreover, the closer China is to Saudi Arabia, the more pressure Chinese leaders will be under to moderate their support of Iran.

China has shown no interest in exploiting the political leverage it might have to influence the policies of Iran, Syria, and Saudi Arabia. During his 2006 visit to the United States, President Hu Jintao reportedly defended his country's disinterest in pressuring its partners by explaining that the PRC is focused on its own internal reforms and construction and does not wish to distract itself by meddling in the affairs of other states.² The PRC is adamant about the inviolability of sovereignty. By standing for such a principle when other states are at issue, China calculates that those states will refrain from supporting interventionist policies if ever the PRC is the focus of international opprobrium. However, as the confrontations over human rights violations in Sudan and nuclear weapons in Iran continue, the PRC may find itself less able to avoid taking a stance on matters of international concern.

2. THE DEMAND FOR OIL IN CHINA

Driven by unprecedented growth of the Chinese industrial, petrochemical, and manufacturing sectors — all of which are oil-intensive, and the rapid expansion in the use of the personal automobile, the PRC passed Japan to become the world's second largest consumer of oil in 2004.³ The U.S. Department of Energy estimates that China will consume 7.4 million barrels per

² Joe Kahn, "In Private Candor From China, An Overture to Promote a Thaw," *The New York Times*, April 17, 2006.

³ As recently as 1990, the PRC had only one million cars on its roads. By 2005, the Chinese people drove 12 million cars, and the Chinese government predicts that 4 million new cars will be sold in 2006. In comparison, U.S. consumers purchase 12-18 million cars per year. Most replace existing cars and negligibly impact fuel consumption. Furthermore, with only 8 vehicles per 1,000 residents, the PRC has a highly underdeveloped transportation sector; transportation fuels consumption is forecast to quadruple between 1995 and 2015. Yves Engler and Bianca Mugenyi, "China's cars on road to ruin?" *People and the Planet*, June 7, 2005; Embassy of the People's Republic of China to the United States, "Auto sales expected to hit 4 mln units in '06," April 10, 2006. <http://www.china-embassy.org/eng/xw/t245422.htm>; E. Iain McCreary and Alan Y. Gu, "China's Energy: A

day in 2006, representing nearly a half million barrels per day increase from 2005.⁴ By 2025, China's consumption is forecast to increase to 14.2 million barrels per day.⁵

If the PRC could meet its rapid increase in oil demand by exploiting domestic reserves, oil would not be a major factor in Chinese foreign policy. Until 1992, China was a net exporter of oil, but domestic production potential has been largely exhausted and production has not increased with demand.⁶ The gap must be met by imports, which, at 3.6 million barrels per day, currently represent approximately 50 percent of consumption. By 2025, imports are forecast to more than triple to 10.9 million barrels a day, and will exceed 70 percent of total consumption.⁷ Furthermore, more than 50 percent of current imports travel through the Straits of Malacca, one of the least secure shipping lanes in the world, and the PRC lacks the naval power to defend these straits against an economic blockade.⁸ Thus, the PRC's oil demand has become a strategic liability.

Faced with the challenge of meeting a voracious appetite for oil, the PRC has worked to diversify its supply. It has tried to develop an Asia-based, regional capacity for oil production that makes it less dependent on international shipping, and its oil firms have become major players in African energy development.⁹ The fruit of this investment appears to have paid off, as Angola has reportedly surpassed Saudi Arabia as China's largest oil supplier in 2006.¹⁰

China's oil imports from Kazakhstan more than doubled in the first four months of 2006, compared with the same period in 2005. Crude imports from Russia climbed 36 percent during the same period, making the country China's fourth-biggest oil supplier.¹¹

Despite aggressive pursuit of supply diversity, as much as 70 to 80 percent of China's future oil imports will have to come from the Middle East and North Africa.¹² China's three major state

Forecast to 2015," Published by the Los Alamos National Laboratory for the U.S. Department of Energy (LA-UR-96-2972), September 1996. <http://www.lanl.gov/source/orgs/d/d4/energy/docs/china.summary.pdf>

⁴ "China Country Analysis Brief," Energy Information Administration, U.S. Dep. of Energy, August 2006.

⁵ Charles Esser, "China Country Analysis Brief," Energy Information Administration, U.S. Department of Energy, August 2, 2005.

⁶ *For instance, despite increasing demand, production in Daqing, the nation's most productive field, fell five percent in 2004.* Esser.

⁷ Esser; also "China Country Analysis Brief," August 2006.

⁸ Emma Chanlett-Avery, "Rising Energy Competition and Energy Security in Northeast Asia: Issues for U.S. Policy," Congressional Research Service, Washington, DC, January 20, 2006; also see "Mapping the Global Future: Report of the National Intelligence Council's 2020 Project," National Intelligence Council, December 2004. <http://www.foia.cia.gov/2020/2020.pdf>

⁹ *In the first 10 months of 2005, Chinese companies invested a total of \$175 million in African countries, primarily on oil exploration projects. In Sudan, China National Petroleum Company (CNPC) invested in a pipeline project and in 2005 bought 50 percent of Sudan's oil exports, which accounted for five percent of China's oil needs. In Angola, which exports 25 percent of its oil to the PRC, the Chinese have gained access to oil resources by offering a \$2 billion aid package that will fund Chinese construction of schools and infrastructure.* Tan Jin San, "Race for more oil fuels China's power game; Search on for more energy sources as far away as Africa as economy burgeons," *The Business Times Singapore*, April 11, 2006.

¹⁰ "China Country Analysis Brief," Energy Information Administration, U.S. Dep. of Energy, August 2006.

¹¹ Gordon Fairclough, "Iran Lobbies China, Russia to Help Curb U.S.; At Summit in Shanghai, Tehran Plays Its Oil Card In Push to Forge Alliance," *Wall Street Journal*, June 16, 2006. pg. A.4

owned oil companies – CNPC (Petrochina), China Petrochemical Corp (Sinopec), and China National Offshore Oil Corp (CNOOC) – have invested significantly in the Middle East.¹³ For example, in 2004, Sinopec outbid most of the American oil majors for the right to develop a new oil field in Saudi Arabia.¹⁴ More recently, CNPC partnered with an Indian firm to buy a significant stake in one of Syria's few oil fields.¹⁵

Three years ago, the head of China's National Reform and Development Commission (NDRC) and Iranian oil minister Bijan Namdar Zanganeh signed a memorandum of understanding regarding bilateral energy cooperation which included Chinese development of Iranian oil fields.¹⁶ In 2006, Sinopec reportedly signed an agreement with Iran to jointly develop the Garmsar oil block, one of 16 oil blocks that Iran offered for international tender in 2003.¹⁷ Iran is China's third largest oil supplier according to Chinese figures. Iranian and Saudi exports together now represent almost two-thirds of China's Middle East oil imports, meaning that relations with these two countries are of crucial importance. Chinese imports from other countries have also expanded, but partnerships with Saudi Arabia and Iran have increased even faster. Whereas in 1994, Iran accounted for just one percent of China's total imports, a decade later, Beijing purchased 13 percent of its oil from Tehran.¹⁸

3. CHINA AND IRAN

China and Iran first established diplomatic relations in 1971. Though the two nations have both experienced revolutionary change in the intervening decades, their continued relationship demonstrates that both countries value political pragmatism, strategic imperatives, and economic trade above discrepancies in ideology and religion. China views Iran as a regional power, whose strategic location and economic importance will remain steadfast in the years to come. However, in the face of protracted international concern over Iran's nuclear program, how far will China go in protecting such strategic, political, and economic benefits? Is China willing to support Iran's nuclear ambitions at the potential risk of jeopardizing Sino-U.S. relations and international prestige as a "responsible" power?

In the 1970s, when China viewed Iran as an outpost of U.S. imperialism, the PRC sought to engage the Shah in an effort to stem the greater perceived threat of Soviet social-imperialism.

¹² Wu Lei, "China-Arab Energy Cooperation: The Strategic Importance of Institutionalization," *Middle East Economic Survey*, Volume XLIX, Number 3, 16 January 2006.

¹³ All three firms held initial public offerings between 2000 and 2002, and western oil giants ExxonMobil, Shell, and BP all purchased significant minority stakes. However, the PRC remains a majority stakeholder in all three, and the government still controls the retail fuel market. All three firms have significantly reduced their workforce, but CNPC runs much like a ministry of government.

¹⁴ Steven Mufson, "As China, U.S. Vie for More Oil, Diplomatic Friction May Follow," *The Washington Post*, April 15, 2006.

¹⁵ Mark O'Neill, "CNPC aims to double overseas crude output by 2010; China's growing dependence on imports heightens need for alternative sources," *South China Morning Post*, February 13, 2006. Pg. 2.

¹⁶ Jill McGivering, "Iran crisis a dilemma for China," *BBC News*, January 17, 2006.
http://news.bbc.co.uk/1/hi/world/middle_east/4621182.stm

¹⁷ "China's Sinopec Signs a Deal To Develop Oil Block in Iran: Report" *Hong Kong AFP*, Compiled and distributed by NTIS, US Dept. of Commerce.

¹⁸ Jin Liangxiang, "Energy first (China and the Middle East)" *Middle East Quarterly* 12.2 (Spring 2005): 3-11.

Unwilling to see Iran fall under the Soviet sphere of influence, China reasoned that assisting a U.S. proxy, something the PRC up to that point was loathe to do, far outweighed the cost of non-engagement. For Iran, a closer relationship with China also proved beneficial. First, the Shah, like China, viewed the Soviet Union as the primary threat to his power. Second, a closer relationship with China could eventually provide the Shah with another outlet for purchasing advanced technology and armaments in his quest to modernize Iran's industry and military. Third, if ever U.S.-Iran relations were to collapse beyond repair, a close relationship with China could prove to be a valuable hedge.¹⁹

With the establishment of the Islamic Republic of Iran, Sino-Iranian relations briefly soured; CCP Chairman Hua Guofeng had visited Iran and supported the Shah as late as August 1978. But by the early 1980s, in the midst of the Iran-Iraq War and increased international isolation, Iran had put aside any ill-will harbored toward China for supporting the Shah in order to secure Chinese weaponry. Iran would greatly value Chinese support during the Iran-Iraq War, a time when most all other countries in the Middle East (and in the West) supported Iraq.

An improved relationship with a regional power like Iran provided China with economic and political benefits. Arms sales to Iran allowed China to improve its domestic arms industry during the early stages of its economic liberalization process, and China soon began to sell arms to the wider Gulf region.²⁰ Politically, China gained leverage by assisting Iran during its most dire hour, when it had few others to turn to for advanced weaponry.

China also assisted Iran in the field of nuclear technology, which not only gained China increased prestige in Tehran, but also demonstrated to the world that China was now to be regarded as among the major players in Middle Eastern security. According to a 2003 CIA unclassified report, China committed to discontinue its nuclear cooperation with Iran in 1997 and pledged to end its ballistic missile assistance to all countries in 2000. Both actions resulted from U.S. pressure; however, cooperation between Iranian and Chinese entities in both areas may remain.²¹

The Chinese decision to maintain close relations with Iran throughout the 1980s was a consequence of the PRC's new reading of the international system. As Soviet projection of power began to wane, China recognized that the gravest threat to its security and stability in the Middle East would be the preeminence of a singular hegemon, the United States. According to John Calabrese the early 1980s marks "the gradual unraveling of the Sino-U.S. "strategic partnership" and not coincidentally also marks the point of divergence between China's Gulf policy and U.S. Gulf policy."²²

¹⁹J. Brandon Gentry, "The Dragon and the Magi: Burgeoning Sino-Iranian Relations in the 21st Century," *The China-Eurasian Forum Quarterly*, November 2005, 113.

²⁰ *During the last half of the 1980s, Chinese arms sales to Iran, Iraq, and Saudi Arabia (its three largest Gulf costumers) was approximately \$3.9 billion.* John Calabrese, "Peaceful or Dangerous Collaborators? China's Relations with Gulf Countries," *Pacific Affairs*, Vol. 65 No. 4 (Winter, 1992-1993), 473.

²¹Central Intelligence Agency, "Attachment A Unclassified Report to Congress on the Acquisition of Technology Relating to Weapons of Mass Destruction and Advanced Conventional Munitions: January-June 2003," https://www.cia.gov/cia/reports/721_reports/jan_jun2003.htm#17.

²²Calabrese 474.

In 1990, bilateral trade between China and Iran totaled approximately \$314 million, but by 2003 it had reached \$5.6 billion.²³ The Iranian press asserts that trade reached \$29 billion in 2005, and that Iran's imports from China increased by more than 360 percent from 2000 to 2005.²⁴ While arms remain an element of this trade, between 1993 and 2004 China's average share of the Iranian arms market was only 18 percent; Iran purchased most of its weaponry from Russia.²⁵ The rapidly growing trade relationship between Iran and China primarily results from China's expanding demand for Iranian oil.

The persistence and expansion of Sino-Iranian relations in the 1990s and the early 21st century should indicate that both countries share a desire for long-term partnership and value the other's importance as an economic, strategic, and political ally.²⁶ While the relationship is driven by the sale of Iranian oil and China's military and (at least until 1997) nuclear assistance to Iran, Sino-Iranian relations, at a more fundamental level, are grounded in a mutual worldview. As John Garver points out in *China and Iran*, both China and Iran recognize the other as a one-time global power with a rich history that contributed enormously to the progress of civilization.²⁷ They see Western imperialism or infringement in their internal affairs as having retarded their progress as nations.²⁸ Consequently, both have maintained a steadfast commitment against infringement in a country's internal affairs. Put simply, China and Iran have convinced one another of their commitment to a multi-polar world and anti-hegemonic struggle.

As a result, the two countries have developed a sense of trust, exemplified in this statement by former Iranian ambassador to China, Fereydoun Vardinejad, during the debate over Iran's nuclear program:

Iran showed that under these sensitive conditions it is not alone and has many friends. Iran's nuclear case is the symbolic manifestation of the common views of Iran and China in international and political relations. Tehran and Beijing both believe that unilateralism on the world level is not in the interest of countries and the world economy.²⁹

²³ *This level of trade does not put Iran in China's top ten trading partners.* Gentry, p. 114-115.

²⁴ "Iran press: Commentary says Tehran-Beijing in a 'mighty alliance,'" Text of commentary by Azadeh Eftekhari by Iranian newspaper Sharq website," August 19, 2006. Translated from Persian by BBC Worldwide Monitoring, August 22, 2006.

²⁵ Rory Miller, "China has more reasons than ever to enter Middle East debate," *The Irish Times*, September 5, 2006.

²⁶ Former Chinese Ambassador to Iran (and current Middle East special envoy) Sun Bigan said, "Over the past 30 years, especially since the establishment of the Islamic Republic, Chinese-Iranian relations have developed substantially in all areas.... but neither [country] is satisfied with the status quo, we see the potential for even closer ties in many areas." World Service of Islamic Republic of Iran Broadcasting Website (*IRIB*), 2001 (interview with an unnamed Iranian reporter). <http://chinese.irib.ir/caifang/dashi.htm>. Translation by John Keefer Douglas.

²⁷ See, for example, Song Rong and Bai Jie. "(PRC-foreign exchange) special interview: Rebuild the Silk Road, erect bridge of peace, security for Asia—interview with Iranian ambassador to China Fereydun Verdinezhad," *Xinhua* (New China News Agency), 14 June 2005. From "Iranian Envoy to China Interviewed on Bilateral Ties," *Global News Wire- Asia Africa Intelligence Wire, BBC Monitoring/BBC*, June 15, 2005.

²⁸ John W. Garver. *China and Iran: Ancient Partners in a Post-Imperial World*. (Seattle and London: University of Washington Press, 2006). See Chapter 1, "The Spirit of Sino-Iranian Relations: Civilization and Power.

²⁹ Iran: Iran's Ambassador to China Says Iran, China to Have Long-Term Cooperation, *Tehran Sharq*, December 21, 2004 (FBIS).

Iran views China as a powerful ally among the world's leading nations-- a country that because of a shared interest in stemming the dominance of the United States will advocate on its behalf. Iran hopes that its relationship with a global economic powerhouse like China will attract business from other countries wary of Iran's pariah status. China, however, with its export-led economy that shipped \$762 billion worth of goods in 2005 and its deep integration into the global economy, is far more willing to live with the reality of U.S. dominance than Iran.³⁰

Furthermore, Iran has looked to China (as well as Russia) to counter the call in the United Nations Security Council, and elsewhere, for economic sanctions in response to Iran's nuclear program. According to Iran, what is good for the Islamic Republic is also in the best interest of the PRC. As an editorial in Iran's conservative leaning *Shoma* put it, "any cooperation China enters in security, political, economic sectors with the region's leading nations like Iran and Saudi Arabia that supply China's energy as well would represent a great victory for Chinese politicians over their Western counterparts."³¹

While such a position is by no means uniform, many Iranian editorials on the subject have echoed similar claims, going so far as to warn China and Russia that their economic and political livelihood in the Middle East depend on defying international pressure against Iran.³² The reformist daily *Aftab-e Yazd* plainly laid out the *quid pro quo*, stating that since "we have assured China that its energy and oil needs will be met, we should ask that country to complete its position and go beyond mere expressions of opposition to the referral of Iran's dossier to the Security Council."³³

But Iran is unwilling to question the strength of Sino-Iranian relations. Even in the face of current Security Council pressure, this Iranian belief stems from two main reasons. First, Iran recognizes that potential Security Council action has thus far been lukewarm in advocating for sanctions. If sanctions against Iran's oil exports ever did become a major issue, Iran strongly believes that, in the end, China would prevent their implementation. Indeed the same day that Iran was given a one-month deadline to end uranium enrichment or face possible sanctions, China's head of central planning, Ma Kai, was in Tehran trying to finalize plans for Sinopec to develop Iran's rich Yadavaran oil-field. Second, Iran recognizes that there is little value in criticizing Sino-Iranian relations. For better or worse, China is Iran's best supporter available.

The current Iranian government of Mahmoud Ahmadinejad, based on a re-reading of recent international developments, has placed Iran on a far more aggressive track than his predecessor Khatami. Believing that the U.S. is unwilling to undertake another war in the Middle East, Iran has concluded that conditions are set to force the issue of its 'inalienable nuclear rights.' No longer, Tehran has reasoned, is it necessary to court the European nations and prevent them from presenting a unified front with the United States in the Security Council. With the seeming lack of any real military threat from the United States and a Chinese (and possibly Russian) ally in the

³⁰ "US-China Trade Statistics and China's World Trade Statistics," *The US-China Business Council*, <http://www.uschina.org/statistics/tradetable.html>.

³¹Iran: Editorial Views PRC to Provide 'Stability' in Persian Gulf Region. Editorial by Behnam Sarkheyl from the "Note" column: "China's Link to Persian Gulf Security," *Shoma*, 25 Mar 2006. (FBIS)

³²Commentary Warns China, Russia Not to Follow US Lead in Iran Nuclear Case, Commentary by Ali Qasemi: "Iran-China Relations, Low-cost Path," *Resalat*, 1 March 2006. (FBIS)

³³"Daily Wants China to Stop Iran Dossier Going to UN Security Council," *Aftab-e Yazd*, 7 Nov 2004. (FBIS)

Security Council, Iran reasoned such conditions would be enough to safeguard against intense international sanction.

Iran, however, appears to be over-estimating China's ability and desire to safeguard Iranian interests by confronting the United States and the West. In moving toward sanctions over Iran's nuclear program, Iranian analyses at the government and civil-society level have been slow to pressure China, which has never vetoed a Security Resolution relating to the Middle East. (The PRC voted with the UN Security Council for Iran to end its nuclear program by August 31, 2006.) Indeed Iran has been unwilling to critique China's role in acceding to Security Council pressure, instead reaffirming the strength of Sino-Iranian relations and reserving its ire for the U.S. and Europe. At the end of the above cited *Aftab-e Yazd* editorial, for example, which strongly beseeched China to stop Iran's nuclear dossier from reaching the Security Council, the following statement appeared:

In the last working hours of the daily, we received the comments of the Chinese foreign minister, which indicate that we should not set many hopes in China in the Security Council. So the matter should be taken into account in our relations.

Already in 2004, when the editorial was published, China seemed to know it would be voting alongside the rest of the Security Council. The interim period (2004-2006), one can suspect, was simply a matter of extracting maximum concessions both from Iran, such as the above-cited Sinopec deal, and the United States. As John Garver points out in *China and Iran* concerning the intersection of Sino-Iranian and Sino-U.S. relations:

China's support for the anti-hegemony struggle had to be conducted in such way as not to undermine China's relation with the United States. China's overriding foreign policy interest was in ensuring that the United States continued benevolent, friendly policies toward China's post-1978 economic development drive. There was a contradiction between this objective and China's support for Iran's antihegemony struggle, and this contradiction had to be handled correctly. When absolutely necessary, the secondary goal of moving the world toward multipolarity by supporting Iran's antihegemony resistance would be subordinated to the primary goal of protecting the Sino-U.S. relationship.³⁴

While China had used its resistance over sanctions in the Security Council to provide Iran with the time needed to settle the nuclear crisis on its own terms, the cost of fully supporting a sovereign and indigenous Iranian nuclear program is simply too high. China has gone to great lengths in the Security Council, and elsewhere, to demonstrate to the Iranians the importance of Sino-Iranian relations. For example, in July 2006, after voting in favor of a one-month deadline for Iran to end its enrichment of uranium or face Security Council sanction, Ambassador Liu Zhemin of China stated that, "Whether now or in the future, the Council could not handle the issue single-handedly. Dialogue and negotiations were the only way out. IAEA should always

³⁴See Garver Chapter 7.

be the main mechanism for dealing with the issue. Any measures adopted by the Council should serve the purpose of diplomatic efforts.”³⁵

Such a statement, coupled with a Chinese vote against Iran in the Security Council, encapsulates the delicate balance of Sino-Iranian relations. China is certainly eager to continue its close relationship with a Middle Eastern regional power, but red-lines in Sino-Iranian relations do exist. China's hope is simply that the stored capital it has garnered from arms sales during the Iran-Iraq War, assistance in nuclear technology, economic partnership, and proven mutual trust is enough to maintain Iran's willingness to “look east,” especially in the energy arena.

For China, partnership with Iran is only one part of its energy diversification strategy. Chinese goodwill is by no means guaranteed, but very much desired. Under such an arrangement, Iran is best seen as only one strand among the complex web of energy relationships China is currently pursuing.

4. THE SHANGHAI COOPERATION ORGANIZATION

To understand how energy and security needs are influencing the relationship between China and Iran, it is important to assess their diplomatic relations. In the past year, no aspect of diplomacy has received more attention than the Shanghai Cooperation Organization (SCO). For in the words of former Iranian foreign minister Akbar Velayati,

In the framework of the Shanghai cooperation agreement, Russia, China, India and Iran, together with other Asian countries, are busy establishing a new political bloc in the world, which in addition to confronting any one-sided attempt at hegemony by NATO, are also trying to establish a secure and stable climate throughout Eurasia.”³⁶

Since 2005, the six member SCO – including Russia, China, Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan – has emerged from relative obscurity to be viewed in some circles as a serious counterweight to American power in Asia and even, in the words of Cambridge University's David Wall, “an OPEC with bombs.”³⁷ In reality, the SCO is a young organization with few current capabilities. Its operating budget is less than U.S.\$30 million, and it employs only a few dozen people.³⁸

Despite its limited effectiveness at the current time, the SCO is receiving extensive attention from western experts because of its potential. In 2005, the SCO added Mongolia, Pakistan, Iran and India as official observers. As Iranian President Mahmoud Ahmadinejad stressed in a speech at the SCO in June 2006, nearly half the world's population lives in member or observer

³⁵“Security Council Demands Iran Suspend Uranium Enrichment by 31 August, or Face Possible Economic, Diplomatic Sanctions,” *Security Council SC/8792*, Department of Public Information—News and Media Division, The United Nations, New York 31 July 2006. <http://www.un.org/News/Press/docs/2006/sc8792.doc.htm>.

³⁶Iran: Former Foreign Minister Comments on Oil, Gas Links with China. Unattributed report: “Ali Akbar Velayati: Iran-China cooperation will strengthen security in the region,” *E'temad-e Melli*, 25 Feb 2006 (FBIS).

³⁷ Michael Mainville, “A potential rival for NATO,” *The Toronto Star*, June 3, 2006.

³⁸ “China and Russia: New 'axis' in the making?” *The Straits Times* (Singapore), July 21, 2006.

countries.³⁹ If the SCO participating states emerged as a united force diplomatically, economically, or militarily, they would be a potent player in the international arena.⁴⁰

4.1 Differing Goals

Despite its potential, it remains unclear what the SCO can and will become. Even the member states themselves do not appear to be in agreement on how the SCO should evolve. Some participants see the SCO emerging as a potent counterweight to American power. Iranian President Ahmadinejad has called for increasing the role of the SCO to “prevent threats and interventions by bullying powers.”⁴¹ Russian Defense Minister Sergei Ivanov has said that member states “should, if needed, help neighboring states block and possibly destroy” invaders.⁴² This attitude held sway in 2005, when the SCO members passed a resolution calling on the United States and its coalition to “set a final timeline” for the “stay of their military contingents on the territories of the SCO member states.”⁴³ Soon after, the U.S. was asked to leave its base in Uzbekistan, and operations at Manas airbase in Kyrgyzstan were limited to flights that re-supply the U.S. mission in Afghanistan.⁴⁴ As an editorial in a conservative Iranian daily put it, “fighting against America's unilateralism and removing its bases in Central Asia and the Caucasus region can also be considered as one of the goals of the SCO.”⁴⁵ (For more on SCO military capabilities, see Appendix.)

Fears that the SCO is emerging as the diplomatic forum for disgruntled dictators sharing a common disgust for the United States were raised by the SCO's 2006 meeting. First, the SCO members welcomed Iranian President Ahmadinejad despite American attempts to isolate the Islamic Republic diplomatically for its nuclear program.⁴⁶ Next, many Central Asian leaders used the meeting to express strong opposition to America's pro-democratic foreign policy, which they believe is partially responsible for revolutions that toppled pro-Russian and pro-Chinese allies in Ukraine, Georgia, and Kyrgyzstan.⁴⁷

³⁹ Fars News Agency, “Ahmadinejad: Development of Shanghai Cooperation Impedes Intervention of Bullying Powers,” June 15, 2006. <http://english.farsnews.com/newstext.php?nn=8503250185>

⁴⁰ *In the words of Michael Berk, who is with the Canadian Institute of International Affairs, “Any entity whose purpose, like the SCO, is promoting stability, cooperation and economic development in a region consisting of such pivotal countries as India and China, as well as such resource-rich states as Russia and Kazakhstan, will be a powerhouse of economic activity and a major global force throughout this century.” “SCO will be economic powerhouse: Canadian scholar,” Xinhua General News Service, June 16, 2006.*

⁴¹ Fars News Agency, “Ahmadinejad: Development of Shanghai Cooperation Impedes Intervention of Bullying Powers,” June 15, 2006. <http://english.farsnews.com/newstext.php?nn=8503250185>

⁴² Michael Petrou, “Is this a Rival to NATO?” *Maclean's*, August 7, 2006.

⁴³ “Declaration of Heads of Member States of Shanghai Cooperation Organisation,” *Astana*, July 05, 2005. (Unofficial translation by the SCO Secretariat.)

⁴⁴ Ariel Cohen, “How the US can crash a cosy club,” *The Straits Times* (Singapore), June 15, 2006.

⁴⁵ “Viewpoint” column, by Sa'id Arjomandi: “On the Sidelines of the Shanghai Meeting,” *Resalat*, Tuesday, July 18, 2006. Compiled and distributed by NTIS, US Dept. of Commerce.

⁴⁶ *The U.S. Defense Secretary Donald Rumsfeld chided China for backing Tehran's participation in the summit, asserting it had invited the “leading terrorist nation in the world into an organization that says it's against terror.” SCO chief Zhang Deguang responded, “We cannot abide by other countries calling our observer nations sponsors of terror.”* Ali Akbar Dareini, “In Shanghai, Iran's president sounds out Russian, Chinese backing in nuclear standoff,” Associated Press Worldstream, June 14, 2006.

⁴⁷ Jehangir Pocha, “Summit Forges Military Ties in Central Asia,” *The Boston Globe*, June 18, 2006.

4.2 The Role of Energy in the SCO

Though it was initially formed to deal with border disputes, terrorism and separatist threats, energy cooperation has emerged as a primary focus for the SCO. In particular, Chinese analysts increasingly talk about using the SCO to turn the old Silk Road across Central Asia into an 'energy road.'⁴⁸ Like China, Russia views the SCO as a tool to promote energy development, as expressed in a 2005 op-ed by the Deputy Foreign Minister:

“Cooperation in fuel, energy, and transport may bring great benefits. Potentially, the SCO members can pool their efforts in geological prospecting, and jointly develop Central Asia's vast resources.” He argued that the SCO could facilitate energy projects, some of which would be “the projects of the century.”⁴⁹ Also, Pakistani President Pervez Musharraf used recent SCO meetings to propose that his country serve as an “energy corridor” between producers and consumers, a suggestion believed to be aimed at a possible oil pipeline from Iran to China or India through Pakistan.^{50 51}

Iran also views the SCO as a tool for expanding energy exports. In his speech at the SCO in June 2006, President Ahmadinejad said “the presence of both the energy consumer and producer states in the organization has prepared a proper ground for energy cooperation within the SCO.” He proposed a summit for energy ministers of the member states “to study avenues for better cooperation in various grounds such as exploration, extraction, transportation, transformation and improved and joint exploitation of energy.”⁵² Ahmadinejad also emphasized that Iran's large reserves of crude oil provide “conducive grounds” for these countries to cooperate with Tehran.⁵³ At the SCO meeting in June, Iran and Russia held bilateral talks in which they discussed an “energy club.” This term, which has eluded any definition, has raised fears that these oil producers are considering a new form of cartel.⁵⁴

It is clear that these relationships go beyond political rhetoric. Over the last year, China, India, Russia, and Iran have signed energy deals with each other valued at about \$500 billion.⁵⁵ In the immediate aftermath of the 2006 summit, Sinopec reportedly signed an agreement to develop Iranian oil fields.⁵⁶ China's oil imports from Kazakhstan more than doubled in the first four

⁴⁸ Gordon Fairclough, “Iran Lobbies China, Russia to Help Curb U.S.; At Summit in Shanghai, Tehran Plays Its Oil Card In Push to Forge Alliance,” *Wall Street Journal*, Jun 16, 2006, pg. A.4

⁴⁹ Alexander Yakovenko, “Seeking Multilateral Regional Cooperation,” *The Hindu*, August 12, 2005.

⁵⁰ Bill Savadove, “Tehran Seeks Allies Through Energy Co-operation Offer,” *South China Morning Post*, June 16, 2006.

⁵¹ Steven R. Weisman, “As the Price of Oil Soars, So Does Its Power to Shape Politics From Washington to Beijing,” *The New York Times*, July 25, 2006.

⁵² Fars News Agency, “Ahmadinejad: Development of Shanghai Cooperation Impedes Intervention of Bullying Powers,” June 15, 2006. <http://english.farsnews.com/newstext.php?nn=8503250185>

⁵³ Gordon Fairclough, “Iran Lobbies China, Russia to Help Curb U.S.; At Summit in Shanghai, Tehran Plays Its Oil Card In Push to Forge Alliance,” *Wall Street Journal*, June 16, 2006, pg. A.4

⁵⁴ John Cherian, “Shanghai spirit,” *Frontline* (from the publishers of *The Hindu*), Volume 23 - Issue 13: July 1-14, 2006.

⁵⁵ Jehangir Pocha, “Summit Forges Military Ties in Central Asia,” *The Boston Globe*, June 18, 2006.

⁵⁶ “China's Sinopec Signs a Deal To Develop Oil Block in Iran: Report” *Hong Kong AFP*, Compiled and distributed by NTIS, US Dept. of Commerce.

months of the year, compared with the same period in 2005. Crude imports from Russia climbed 36 percent during the same period.⁵⁷

Western analysts are increasingly alarmed that the economic endgame of the SCO is “to dilute Washington's hold over the Caspian Sea's energy reserves,” as Robert Karniol, Asia-Pacific editor for *Jane's Defense Weekly*, put it. China and India, the world's fastest-growing energy consumers, want to divert Central Asia's energy resources toward their own economies, and Iran and Russia, the region's largest energy suppliers, are keen to reduce their dependence on sales to the West, Karniol argues.⁵⁸

Despite this concern, the SCO is not a “mercantilist” tool for China to “lock up” the oil reserves of unseemly governments in central Asia.⁵⁹ In a global market, locking up oil is exceptionally difficult. Lt.-Gen. William Odom (retired), a professor at Yale and former director of the National Security Agency, explains, “I've never been of the view that you have to be highly influential in a region to get it to sell you oil.”⁶⁰

First of all, China's overseas activities are not on a scale that would warrant the level of international concern and condemnation it has received. The Energy Information Administration explains: “For all the attention given to Chinese firms' investments in overseas oil assets... their total current contribution to China's oil imports is well under 300,000 barrels per day as of mid-2005, a small amount compared to imports currently running at around 3.5 million barrels per day.”⁶¹

Second, major development projects between SCO states have not proceeded without difficulty. For instance, a 2004 Memorandum of Understanding between Iran and China to establish a 25 year agreement for LNG exports worth \$100 billion has so far only led to further negotiations, despite the big splash when signed.⁶² ⁶³ Similarly, a plan to build a pipeline from Russia to China was announced in 2003, yet the two governments continue to negotiate the terms of this agreement.

But most importantly, it is vital to understand that the only way for China to lock up oil in today's market, even with its SCO partners, would be to sign long-term purchase agreements and

⁵⁷ Gordon Fairclough.

⁵⁸ Jehangir Pocha.

⁵⁹ *In September 2005, US Deputy Secretary of State Robert Zoellick said in a speech: “China is acting as if it can ‘lock up’ energy supplies around the world. Moreover, a mercantilist strategy leads to partnerships with regimes that hurt China's reputation.” In 2006, the U.S. National Security Strategy again accused the PRC of trying to “lock up” oil resources.*

⁶⁰ Michael Petrou, “Is this a Rival to NATO?” *Maclean's*, August 7, 2006

⁶¹ Esser.

⁶² “China's Sinopec Signs a Deal To Develop Oil Block in Iran: Report” *Hong Kong AFP*, Compiled and distributed by NTIS, US Dept. of Commerce. “China, Iran close to finalize energy contracts” (AFP), February 17, 2006, from *China Daily*.

⁶³ *China considered sending its top economic planner to Iran in February in hopes of finalizing energy contracts, but Chinese Minister of the State Development and Reformation Commission Ma Kai did not visit until late June. After the meeting, Ma Kai said “The economies of China and Iran are closely tied together,” and called for an increase in Tehran-Beijing transactions, but the visit did not produce a final deal. “Iran, China Underline Energy Cooperation Agreements,” BBC Monitoring International Reports, July 4, 2006.*

outbid the other firms in the race. Chinese state firms can consistently win bidding wars only if (a) they are willing to pay more for oil than private firms from the United States, India, and Europe believe the resource to be worth, or (b) oil rich SCO states are willing to accept reduced financial reward in order to sell their oil to China. If China wishes to burden its economy with fuel costs above market value, the United States, as an economic competitor, would have a comparative advantage over oil intensive industries in China.

China's attempt to secure long-term oil supply is better understood as a hedging technique. Chinese oil companies, and their private investors, are willing to pay higher prices because the demand for fuel in China is growing rapidly, and the firms believe that there will be a market for their product, even at prices above the world average.

4.3 Interests

A thorough assessment of the SCO reveals that the states participating in the SCO do not have matching interests regarding energy or military power.⁶⁴ As oil prices have risen from about \$27 a barrel at the start of the Iraq war to a high of \$78 during the conflict in Lebanon, Iran and Russia benefited while India and China suffered. According to Cambridge Energy Research Associates, each \$5 increase in oil prices translates into \$85 million a week for Iran's bank account.⁶⁵

Ariel Cohen correctly notes, "If not restrained and contained, Iran is likely to drive world oil prices even higher" as part of its agenda. He points out that Russia, as a high-cost oil producer, benefits from Middle Eastern instability that keeps oil prices high.⁶⁶

China and India, on the other hand, are economic powers dependent on cheap Middle East oil. Their interests are in working together with major consumers to keep prices reasonable. To this end, the two states have recently signed an agreement designed to end the "mindless rivalry" over oil. The agreement has established a formal procedure to exchange information about oil development bidding. The agreement may lack teeth, but it demonstrates that two of the world's major consumers have recognized that, as India's petroleum minister put it, "rivalry only benefits those who are selling assets, no matter which country wins."⁶⁷ There is evidence that China would be willing to pursue similar cooperation with the U.S. In a recent speech Zhang Guobao, Vice Minister of NDRC, stated, "Conditions are favorable for Chinese and U.S. oil firms to cooperate on the development of oil fields in third countries."⁶⁸

⁶⁴ See the Appendix to this report for analysis of the military dimension of the SCO.

⁶⁵ Weisman.

⁶⁶ Ariel Cohen, "How the US can crash a cosy club," *The Straits Times* (Singapore), June 15, 2006.

⁶⁷ Carola Hoyos, Jo Johnson and Richard McGregor, "China and India forge alliance on oil with aim of ending 'mindless rivalry'," *Financial Times* (London), January 13, 2006.

⁶⁸ "Cooperation between Chinese and US firms could be mutually beneficial," *Xinhua*, September 13, 2006.

Accessed at Sinopec News site on September 13, 2006: http://sinopecnews.com.cn/shnews/2006-09/13/content_407064.htm

5. CHINA AND SAUDI ARABIA

Sino-Saudi relations are a relatively new development, with China and Saudi Arabia having only established relations in 1990. This year has been a landmark year in Sino-Saudi relations, witnessing the visit of Chinese President Hu Jintao to Saudi Arabia and the visit of Saudi King Abdallah to China. King Abdallah's visit to China was his first trip outside of the Middle East since ascending the throne in August 2005.

According to Arabic sources, the exchange of visits between King Abdallah and President Hu point to the unquestionable seriousness of Sino-Saudi relations. First, Hu's trip to Saudi Arabia occurred only three months after Abdallah's trip to China.⁶⁹ Indeed, during his trip to Saudi Arabia, President Hu himself pointed out that head-of-state exchanges in such a short amount of time are extremely rare.⁷⁰ Second, Hu was only the second foreign president to address the Saudi Consultative Council, after Jacques Chirac.⁷¹ Third, the Hu visit ended with tangible results, not only in regards to energy, but also other fields, such as health and trade.⁷² Accordingly, Chinese Middle East envoy Sun Bigan pointed out, the visits "laid a solid foundation for the growth of bilateral ties in the years ahead."⁷³ A Saudi Arabia Information Resources report from April 2005 states:

...Abdullah Al-Mubti, head of the delegation and chairman of the Abha Chamber of Commerce and Industry, said the Arab-China Business Conference in Beijing was successful as it helped strengthen mutual confidence. He said the organizers have agreed to hold the second conference in an Arab country. More than 200 Arab businessmen took part in the conference.... He added Saudi-Chinese trade exchange grew from \$300 million in the beginning to \$10 billion (SR37.5 billion) last year.⁷⁴

The greatest challenge for China in expanding the scope of Sino-Saudi relations will be allaying Saudi Arabian fears over the nature of relations themselves as well as China's close relationship with the Iran. Indeed in his speech to the Consultative Council of the Kingdom of Saudi Arabia, Hu Jintao strove to allay Saudi fears over expanded ties with China in these two key regards.

First, President Hu stressed the importance of China's non-interference policy, not only in an effort to maintain peace and stability, but also in terms of a country's internal security. He explained that countries "should respect and maintain each country's right to independently choose its social system and its road of development."⁷⁵ By reiterating their long-standing commitment to non-interference in the context of Sino-Saudi relations, China wishes to

⁶⁹For example see, in Arabic: "The Kingdom and China are Signing Agreements for Security and Defense Cooperation and a Memorandum of Understanding for the Advancement of Trade," Al-Riyadh, 23 Apr 2006, Issue 13817. <http://www.alriyadh.com/2006/04/23/article148704.html>.

⁷⁰Ibid.

⁷¹For example see in Arabic: Aliyan Al-Saadon. "Chinese President Addresses Shura Council with Important Speech," Al Jazeera, 22 Apr 2006.

⁷²"The Saudi-Chinese Summit Culminates in Agreements Related to Security, Defense, Health and Trade," Al-Sharq Al-Awsat, 23 Apr 2006, Issue 10008. In Arabic at <http://www.asharqalawsat.com/details.asp?section=3&article=359563&issue=10008>

⁷³"Saudi crown prince meets Chinese Mideast envoy," *Xinhua*, August 15, 2006.

⁷⁴From the Saudi Arabia Information Resource website, April 17, 2005: <http://www.saudinf.com/MAIN/y8082.htm>.

⁷⁵"Promote peace in the Middle East and build a harmonious world," *Xinhua*, April 23, 2006.

distinguish Sino-Saudi relations from the current trend in U.S.-Saudi relations, namely the effort by the U.S. government to push for political liberalization in Saudi Arabia since September 11th. Indeed Saudi Arabian government officials have already expressed appreciation for China's commitment to a policy of non-interference, especially in times of unrest in the Middle East.⁷⁶ Put simply, Chinese companies are not constrained in their overseas activities by the political commitments of their home country in areas such as human rights and nuclear non-proliferation as are their American counterparts.⁷⁷

In seeking to diversify its cooperation with Asian companies in export markets, but also technical know-how, arms and ammunition, and education for the elite, Saudi Arabia welcomes new partnerships that do not advise it on how to run its internal affairs and do not contain any "strings" on how the Saudi Royal Family should rule.⁷⁸ As Prince Turki Al-Faisal, the Saudi Arabian ambassador to the United States, noted in a discussion with *USA Today*, China is "[n]ot necessarily a better friend [than the United States], but a less complicated friend."⁷⁹ While Turki went on to state that Saudi Arabia does not see China as a counter-weight to the United States, the above quoted comment should be read as a new realization by many in Saudi Arabia to the negative aspects of too close an association with the United States.

The second key point in the Chinese president's address concerned regional rivalry among states in the Middle East. "Different civilizations of the region should take a peaceful and magnanimous attitude toward each other's differences," Hu said. He continued by stating that "[d]ifferences should not become the root cause to regional conflicts and contradictions, but should become each other's reference and a force for integration of the region."⁸⁰ By speaking specifically about the civilizational differences as a source of contention in the Middle East, namely among Persians and Arabs, Hu not so subtly hinted that Sino-Saudi relations will not be subservient to China's close relationship with Iran, a country Saudi Arabia views with extreme concern and skepticism.

For China, with its sensitivity to volatility in oil price and supply, the stability of Saudi oil supply is enticing, as is the level of influence the Saudis are seen as having over both OPEC and non-OPEC oil producers. Chen Mo, a researcher at the Chinese Academy of Social Sciences, went so far as to say that, "In the future... .Saudi Arabia will be China's largest source of oil."⁸¹ Though 2006 saw the prospect of high-profile expansion of Sino-Saudi relations, it is important to place the China-Saudi Arabia relationship in its proper global context. China's commitment to increasing its relationship with Saudi Arabia is not simply a matter of locking up vast oil reserves. Nor, from the Saudi perspective, is it simply a matter of replacing an American export market with a Chinese one.

⁷⁶"Saudi crown prince meets Chinese Mideast envoy," *Xinhua*, August 15, 2006.

⁷⁷Anthony Bubalo. "Asia's alliance with the Middle East threatens America," *The Financial Times*, October 6, 2005.

⁷⁸Aziz-ud-Din Ahmad. "Saudi Arabia's Quest for New Allies," *The Nation*, February 1, 2006.

⁷⁹Prince Turki discussion with *USA Today* editors and reporters appeared in the May 10, 2006 edition of the paper.

⁸⁰Ibid

⁸¹ *Today*, *Angola is China's largest supplier*. Chen Mo, "The Duet Between Saudi Arabia and China on Oil Cooperation: Deepening the Reliance on Middle Eastern Oil," *Dazhong Web Reporting Service*, August 29, 2006. Accessed September, 2006 at http://www.dzwww.com/caijing/cybd/200601/t20060123_1336444.htm.

For Saudi Arabia, the increase in cooperation with China may signal an attempt to end the kingdom's overwhelming reliance on "one big friend" and "one big product," i.e., the United States and oil.⁸² Saudi Arabia has recognized that increased diversity of its oil exports and movement away from its heavy reliance on the American market has both economic and political benefits. Saudi Arabia cannot ignore the increased energy needs among Asian countries, such as China and India. The prospect for revenue is simply too large. As advisor to the Saudi minister of commerce and industry, Fawaz al-Alami, pointed out, "[t]he growth in our oil exports and petrochemicals will be China and India. Five years ago our trade with China was only \$200 million. Now it's \$14 billion, and in five years we expect it to be \$45 billion."⁸³

Furthermore, by distancing itself from a disproportionate reliance on the U.S. energy market, Saudi Arabia will be able to better extricate itself from the political costs of a close relationship with the United States. While Saudi Arabia has indicated its willingness to increase democratic participation in the country, the likelihood that Saudi measures will fully satisfy U.S. concerns in this regard is slim. The Saudi royal family's primary concern is to maintain its position of preeminence. In short, advancing democratic reforms too swiftly, if at all, may jeopardize the House of Saud's stability in the country. Second, Saudi Arabia's close relationship with the United States continues to play to the detriment of the country's image both at home and abroad. As recent instability in Iraq, Israel/Palestine, and Lebanon has demonstrated, the self-styled leading country of the Islamic world is beginning to come under fierce criticism for its unwillingness to jeopardize Saudi-American relations for the purpose of Islamic solidarity. The most recent example of such criticism can be found in the initial Saudi Arabian government condemnation of Hezbollah in its recent war with Israel, against the views of elements in Saudi Arabian society at large.⁸⁴ Such image problems at home present an additional reason to slow democratic reform, as an increase in voter and candidate participation could give rise to a series of populist contenders. Finally, the rising calls in the U.S. for more vigilance (and protectionism) in business dealings with Arab countries, as evidenced by the Dubai port ownership incident, could also increase Saudi wariness of the future of Saudi-U.S. relations.

Based on preliminary assurances by China on the direction of Sino-Saudi relations and the possible cooling of Saudi-U.S. relations, expanded ties between China and Saudi Arabia appear primed to move forward. However, Sino-Saudi relations are still in their infancy and it is uncertain the precise direction they will take. It is unlikely, for example, that now or in the immediate future Saudi Arabia would seek to use China as a viable strategic and military alternative to the United States. As the recent War in Lebanon indicates, Saudi Arabia remains fearful of the ability of Iran and Hezbollah to destabilize the Saudi regime. Security and stability of the Saudi regime remains of the utmost importance and, in that regard, U.S. military might in the Gulf is the House of Saud's final guarantor.

⁸²"Saudi Partnership with Asian Giants a Trailer," *Financial Times*, Global News- Asia Africa Intelligence Wire, January 31, 2006.

⁸³Roula Khalaf. "Saudis look east for new friendships in 'rebalancing' of foreign relations," *The Financial Times*, March 1, 2006.

⁸⁴Faiza Saleh Ambah. "Arab Leaders, Unlike Much of Public, Uneasy about Hezbollah," *The Washington Post*, July 24, 2006, A12.

China's aim in expanding Sino-Saudi relations is very similar to the Saudi rationale for expanded relations—diversification. In Saudi Arabia, China sees a way in which it can diversify its Middle Eastern oil suppliers and depend less on Iran for Middle Eastern oil. Additionally, a closer economic relationship with Saudi Arabia should be absent of the possible political consequences and image concerns that occur in Sino-Iranian relations. The PRC sees a great economic opportunity in expanded relations with Saudi Arabia, but not a replacement for their political and strategic partnership with Iran. Thus, the expansion of Sino-Saudi relations provides each country with the same need: the mitigation of reliance on one main oil supplier/consumer, rife with political and image concerns, with a less complicated and dramatic economic partnership.

6. XINJIANG: A POTENTIAL FLASHPOINT?

Religious and cultural differences between China and its Middle Eastern partners have had little effect on the trajectory of their relations to date. However, one possible flashpoint for the future of Sino-Saudi and Sino-Iranian relations may involve the treatment of Uighur Muslims in China's western Xinjiang province.

Saudi Arabia and Iran have shown little concern for the plight of Uighur Muslims, who are subject to Chinese human rights abuses in Xinjiang. Indeed, the Uighurs remain a repressed Muslim community that receives scant treatment in the international media (including in the Islamic world). The lack of media attention regarding the Uighurs has thus far allowed both Saudi Arabia and Iran to avoid the issue. Were the rights of Xinjiang's Muslims to become of greater concern in the Islamic world, both Saudi Arabia, as the guardian to the two Holy Cities of Islam and self-styled leader of the Islamic world, and Iran, whose championing of the dispossessed has been a staple since its revolution, could condemn Chinese policy.

The likelihood that the Uighurs' plight will somehow trigger world-wide attention in the near future, particularly in the Islamic World, is unknown. Anecdotal evidence provided by Bradley Jensen Murg, a PhD candidate at the University of Washington, currently researching Uighur issues in Urumqi, Xinjiang, suggests that Chinese authorities in Xinjiang have a firm political and military grip, with no evidence of any anti-regime political organization or armed resistance.⁸⁵

However, there are two factors that might bring greater world-wide attention to Xinjiang's Muslims. First, in the past five years (2001-2006), China has aggressively increased its policies of repression against Uighurs. After September 11th, 2001, for example, China has used the United States "war on terror" to pursue its own aggressive campaign against Uighurs Muslims in Xinjiang. A 2004 Amnesty International Report on Chinese abuses in Xinjiang states that China "continues to use 'anti-terrorism' as a pretext to suppress all forms of political or religious dissent in the region."⁸⁶ According to Zhao Yongchen, one of China's top anti-terrorism officials, Muslim separatists in western China have carried out 260 attacks and killed 160 people over the

⁸⁵ Interview with Bradley Jensen Murg, August 25, 2006, by John Keefer Douglas.

⁸⁶"People's Republic of China: Uighurs fleeing persecution as China wages its 'war on terror'," Amnesty International, 7 July 2004. <http://web.amnesty.org/library/index/engasa170212004>.

past ten years.⁸⁷ In official literature, the Chinese government also blames “outside forces,” such as al-Qaida, for sowing unrest in the province.⁸⁸ The World Uighur Congress, however, has stated that the “policies of political oppression, cultural assimilation, economic exploitation, ecological destruction, racial discrimination have gradually turned East Turkestan into a time bomb.”⁸⁹

Second, in the coming years China will more aggressively exploit Xinjiang's rich natural resources and proximity to Central Asia. If regional projects such as the SCO and the Silk Road Initiative are successful, Xinjiang could serve as the lynchpin of overland trade between China and Central Asia. If the plight of Uighur Muslims does become a sustained news story in the Islamic World, the reactions of Saudi Arabia and Iran will be a telling signal of the value they place on their relations with China.

7. ASSESSMENT OF CHINESE STRATEGY AND POLICY

After the end of the Cold War, most analysts in China expected to see the rise of a multipolar world, in which coalitions of weaker states formed to counter the power and interests of the U.S., constraining its ability to act as hegemon.⁹⁰ By the early 1990s, such a situation had not materialized and the application of U.S. military and economic power worldwide was left seemingly unchecked. Thereafter, the Chinese leadership concluded that in the area of energy, the best way to deal with a unipolar world was to try to compete with the U.S. at its own economic game, sending out Chinese companies to secure supplies both regionally and around the world in the same way that U.S.-based multinationals routinely do.⁹¹ This can be seen as a strategy of competing with the U.S. and its allies in a way that tries to avoid direct confrontation, by playing by the rules of international capitalism.⁹²

One consequence of this policy for China has been a strong public de-emphasis of military capabilities (except as they relate to Taiwan), and an unwillingness to provoke the U.S. through attempts to form strong military alliances.⁹³ China would much rather hide its strength and build commercial relationships, believing that such a strategy can be just as effective in thwarting U.S. dominance in key regions such as the Middle East. As countries in the region stand up on their own to U.S. pressure, they feel secure in the knowledge of continued access to Chinese markets

⁸⁷“China blames Muslim independence groups for 260,” Saudi Press Agency, 6 Sept 2005.

⁸⁸Benjamin Robertson. “China's ‘war on terror, under scrutiny,” Al Jazeera, 21 July 2004.

⁸⁹“China given warning on Xinjiang,” BBC World News, 30 Sept 2005. <http://news.bbc.co.uk/2/hi/asia-pacific/4297070.stm>.

⁹⁰ Lecture by Alan M. Wachman on “The Putative ‘Rise of China,’” April 3, 2006, The Fletcher School.

⁹¹ Zhang Weiping, “Overseas energy strategy needed,” *China Daily*, November 7, 2005. Author is an associate chief economist at CNOOC.

⁹² Use of terms unipolarity and multipolarity follows Avery Goldstein, *Rising to the Challenge: China's Grand Strategy and International Security* (Stanford: Stanford University Press, 2005) 81-94.

⁹³ *Even recent Chinese commentary holds to the line that China cannot hope to compete militarily with the US, nor will it be able to for decades to come.* See especially Sun Xuefeng, “The Effectiveness of China's Policy Towards the United States,” *Chinese Journal of International Politics*, (2006) 1, 1: 57-81.

should relations with the U.S. sour.⁹⁴ Especially in the Middle East, continued erosion of U.S. influence is understood by Chinese leaders as facilitating its ability to pursue energy supply wherever it can. With the belief that U.S. criticism of China for doing business in places like Iran, Syria and Sudan is increasingly falling on deaf ears in the international community,⁹⁵ China feels emboldened to ignore U.S. pressure, as it becomes harder for America to garner support for sanctions or other means to punish or isolate China and its energy suppliers. There appear to be limits, however, on how far China is willing to go down this road, as evidenced by their reported hedging on investments in Iran.⁹⁶ China values its U.S. ties, and can be persuaded in certain circumstances to constrain its political support for states like Iran.

A major source of U.S. weakness, in the eyes of Chinese analysts, is that the top priority of U.S. international strategy is maintenance of hegemony (military, economic, and political). All other strategic and diplomatic priorities, including counter-terrorism, democratization, free trade, and energy supply are understood to be subsumed within this conceptual framework.⁹⁷ The stated U.S. goal of fighting terrorism and promoting democracy in the Middle East is seen far more cynically by Chinese analysts as a thin cover for U.S. political, economic, cultural and military dominance. A very typical expression of this view can be found in the following quotation: "In reality, eliminating the terrorist threat is only one strategic objective of the U.S. 'Greater Middle East Democratization Plan.' An even larger objective is to install pro-U.S. political systems through the spread of U.S.-style 'democracy' and 'freedom,' strengthening their exclusive domination over the entire Middle East."⁹⁸ Current Chinese strategic thinking is characterized by the view that, as China engages and does business with any and all countries in the world, it is building a store of goodwill that may weaken U.S. dominance.⁹⁹ So long as they continue to acknowledge U.S. military hegemony and keep the public face of Chinese military modernization focused squarely and solely on the Taiwan Straits, China sees no need to pursue policies that could lead to direct confrontation.

7.1 Chinese Energy Policy

In its 2005 white paper titled *China's Peaceful Development Road*, the PRC explained its official energy policy as follows: "Through dialogue and cooperation regarding energy, China is working with other countries to safeguard energy safety and stability. China considers energy

⁹⁴ Such "foreign policy by proxy" is a strategy with deep roots in Chinese history and culture. To be able to achieve foreign policy objectives without direct, public action is the highest form of statecraft. For a more thorough treatment of Chinese Security and Defense Policy, see the Appendix to this report.

⁹⁵ Yin Jiwu and Li Jiangning, "The Limits on US Strengthening of Public Diplomacy in the Muslim World," *Research on International Issues (Guoji wenti yanjiu)*, 2006, no. 2. Translation by John Keefer Douglas.

⁹⁶ Andreas Landwehr, "China has much to lose from Iran nuclear crisis," *Deutsche Presse-Agentur*, August 28, 2006. DBA reports that China has instructed Sinopec to hold off on implementation of the agreement signed to develop Iran's Yadavaran oil field due to fears that Iran may be subject to a military strike. The push to develop Saudi relations can also be viewed in this light.

⁹⁷ Ren Weidong: "United States Aims at Maintaining Its Exclusive Hegemony by Hying the 'Long War' -- The 'Long War' May Become the Indicator of the New Historical Period After the Short 'Post-Cold War' Period," *Liaowang*, July 19, 2006. Translation by FBIS.

⁹⁸ Yin and Li.

⁹⁹ Yang Yi, "A Period of Strategic Opportunities for Chinese National Security," *Education and Research (Jiaoxue yu yanjiu)* 2006, no. 4. Translation by John Keefer Douglas.

saving one of its basic state policies.”¹⁰⁰ The origins of this policy rest in China's clear need for oil, combined with its desire to continue its non-interventionist philosophy of foreign affairs, and its more recent awareness that a “rising” China could be perceived as a threat. Recognizing the need for imports from overseas, Deng Zhenghong, Enterprise Manager for Sinopec, stated that China's overseas oil investments will be characterized by the following ‘sixteen character guideline’: “Consolidate the Middle East, develop the surrounding regions [i.e. border states], expand in Africa, and explore the Americas.”¹⁰¹ China is thinking globally, but it is not by accident that the Middle East is first on this list.

As oil imports have grown, China has been forced to formulate an energy security policy, especially concerning the Middle East. In practical terms, this has manifested itself in a major restructuring of the Chinese oil industry in 1998. The government aimed to refocus the major oil firms, end the division of labor between them, and push them to emulate the major multi-nationals, seeking upstream production rights overseas to complement domestic activities.¹⁰²

Despite an all-out diplomatic push to secure overland supply from Russia and Central Asia, and recent deals signed with Venezuela,¹⁰³ China realizes most of its future imports will have to come from the Gulf and North Africa:

Taking into consideration global oil distribution, producing capacity, supply potential, import costs and other factors, most of China's future oil imports, accounting for 70-80% of the total, will have to come from the Middle East and North Africa, particularly from the Gulf nations. As today's international oil security is rooted in the uneven distribution of oil resources, China has to be able to cope with it and get out of it as much as possible. Although oil imported from Russia, Central Asia and other parts of the world would help China improve its oil security, there is no denying that Middle East and North African oil has been and will continue to be a big element in China's oil security formula.¹⁰⁴

This means continued reliance on shipping lanes, in particular the Straits of Malacca. As in all such points of geopolitical friction in the world, official Chinese policy maintains a strict stance of non-interference. China has gone so far as to say that they will “never consider a military solution [to problems in the straits],” preferring instead to make guarded references to U.S. naval activity in the region and the need to respect the sovereignty of bordering nations.¹⁰⁵ Although improved relations with Russia and Central Asia, especially in the context of the SCO, are

¹⁰⁰ “Full Text: China's Peaceful Development Road,” *People's Daily Online*, December 22, 2005.

<http://english.peopledaily.com.cn>

¹⁰¹ Deng Zhenghong, Enterprise Manager, Sinopec, blog entry May 11, 2006. Accessed September, 2006 at <http://www.boraid.com/darticle3/list.asp?id=55007>.

¹⁰² *The United States and Japan are Saudi Arabia and Iran's largest oil customers, respectively*. United States Congress Joint Economic Committee, “Iran's Oil and Gas Wealth,” Research Report #109-31, March 2006. Obtained from www.house.gov/jec.

¹⁰³ NPR “Marketplace,” August 28, 2006.

¹⁰⁴ Wu Lei, “China-Arab Energy Cooperation: The Strategic Importance Of Institutionalization,” paper delivered to the China-Arab Cooperation Forum, sponsored by China's Ministry of Foreign Affairs, in Beijing on 12-13 December 2005. <http://www.mees.com/postedarticles/oped/v49n03-5OD01.htm>.

¹⁰⁵ “China-US Energy Cooperation: Challenges and Opportunities.” Policy statement by Chinese Energy Bureau (Vice Ministry under NDRC charged with formulating energy policy). Accessed on August 3, 2006: http://nyj.ndrc.gov.cn/dcyj/t20051229_55139.htm. Translation by John Keefer Douglas

worthy of close attention, they do not yet demonstrate a policy shift for China. Chinese leaders remain acutely aware that a U.S. blockade of the Straits of Malacca could virtually paralyze their economy and that overland supplies will not replace ships in the foreseeable future.¹⁰⁶

To many analysts in the U.S., the rapid emergence of Chinese state-owned oil companies on the global stage is of major concern. They argue that the companies are enacting the foreign policy directives of the central government by pursuing exclusive, long-term oil supplies that need not be sold on open markets, but rather can be sold within a closed Chinese retail market.¹⁰⁷

However, China's leadership views its energy policy quite differently. As Zhang Guobao, deputy minister of the National Development Reform Commission (NDRC), explained, "Some people show they are biased against China's economic development by blaming China for boosting international oil prices. Why are other countries' oil imports justified, but it is called 'a threat' when it comes to China?"¹⁰⁸

To Chinese officials, their companies are only acting as any other major oil and gas firm by competing for supply contracts and expanding reserves. Zhang Weiping, an economist at CNOOC, explains:

Leading global powers are readjusting their energy strategies. The United States has managed to strengthen its strategic position in the Middle East in the wake of the Iraq War and increased threat deterrence along oil transportation passages through its military presence. At the same time, Washington has reinforced control over global strategic resources via giant multinationals' activities worldwide.¹⁰⁹

To Zhang and his Chinese colleagues, a Chinese oil and gas firm is no different from Exxon Mobil. In the event of a crisis, they believe American firms would prioritize the U.S. market, and would be protected in this action by the strength of the U.S. Navy, a protection Chinese companies do not enjoy. There is strong evidence that China realizes the impossibility of locking up resources; Zhang Guobao's recent comments on the willingness of Chinese oil firms to cooperate with U.S. firms in overseas upstream and downstream activities suggest that China is actively trying to allay U.S. fears of neo-mercantilist policy. Multinational oil firms may see no advantage in cooperative ventures with Chinese firms. Nonetheless, it may be in U.S. policy interests to promote such ventures as a way of highlighting U.S.-Chinese common interests as consumers, and mitigating the threat of bidding wars with China over oil fields.

8. IMPLICATIONS & RECOMMENDATIONS FOR THE UNITED STATES

The PRC's stated policy of peaceful development is intended to assure major oil producers and major consumers that a 'rising China' will be a non-threatening trading partner in troubled

¹⁰⁶ Wu Lei and Shen Qinyu, "Will China and the US go to War over Oil," *Far East Economic Forum (Yuan dong jingji pinglun)*, April 13, 2006. Translated by John Keefer Douglas.

¹⁰⁷ Larry M. Wortzel, "Introduction to U.S.-China Economic and Security Review Commission." The Fletcher School. Medford, April 12, 2006; and also Chanlett-Avery.

¹⁰⁸ Xie Ye, "Energy bogey," *China Daily*, June 6, 2005.

¹⁰⁹ Zhang Weiping.

regions of the world. However, some argue that China's energy policy poses a threat to U.S. interests. Based on the analysis presented in the previous sections of this document, we make the following recommendations for American policymakers.

Recommendation 1: View Chinese Oil Company Activities as Capitalist, not Mercantilist

The Bush Administration argues that China's neo-mercantilist strategies threaten American 'oil security' by 'locking up' resources, thereby threatening American access to this vital commodity. Other analysts point to the SCO as evidence of an emerging closed Asian 'energy club.' We view these analyses as flawed for both economic and security reasons. In today's economic system, China's oil companies could only lock up resources by consistently outbidding other international energy interests and paying above market rates. Such a policy, however, would strain China's already heavily subsidized retail fuels market, lead to unnecessarily high oil prices, and harm to China's overall economy. There are enough producers in the global oil market that China's efforts to "lock up" resources are unlikely to keep the U.S. from getting what it needs. In the near term, continued supply is not a major concern—energy experts assert that current high oil prices are caused mainly by lack of infrastructure investment and complete reliance on Saudi Arabia as the only producer with any buffer of excess capacity—and not because America is losing access to oil.¹¹⁰ To the contrary, we believe that China's aggressive upstream investment activity will increase international oil supplies to America's economic benefit.

China currently lacks either the means or the intention to intervene militarily in defense of its overseas interests. In practical terms, this means that any restriction in supply could produce serious consequences in China, especially since it has only just begun to create a strategic oil reserve. China admits it will not have capacity to project naval power to secure shipping lanes any time soon.¹¹¹ Overland routes mitigate this, but China's reticence to form strong military alliances, even in the context of the SCO, means that pipelines will be difficult to defend. Thus, China realizes its best hope in the current international climate is diplomacy, capitalist competition, and cooperative ventures to improve the quality and efficiency of the Chinese oil industry.¹¹²

Official Chinese statements on energy policy stress independence to the greatest extent possible, and where they must rely on imports, international cooperation to maintain secure supply—they take a "we're all in this together" view. This forms a key area for engagement by U.S., stressing our common interests as consumers to make a push for security and peace in the Middle East.¹¹³ China's recent agreement with India designed to reduce competition over oil supply, and China's willingness to cooperate with U.S. oil firms suggests this cooperation could be fruitful.

¹¹⁰ "Two Cheers for Expensive Oil (petroleum crisis)." Leonardo Maugeri. *Foreign Affairs* 85.2 (March-April 2006): p149.

¹¹¹ Chinese Ministry of Foreign Affairs press conference, December 2005. Translation by John Keefer Douglas.

¹¹² "China-US Energy Cooperation: Challenges and Opportunities" (Energy Bureau).

¹¹³ Ministry of Foreign Affairs for the PRC. "Transcript of Premier Wen Jiabao's Press Conference in Cairo." June 19, 2006. Obtained from <http://www.fmprc.gov.cn/eng/wjb/zjzg/xybfs/xwlb/t258665.htm>, August 2006. Ministry of Foreign Affairs for the PRC. "President Hu Jintao Attends G8 Outreach Session and Delivers Important Speech." July 18, 2006. Obtained from <http://www.fmprc.gov.cn/eng/zxxx/t264518.htm>, August 2006.

Recommendation 2: Promote Broad Chinese Investment

The second common indictment against China is that its appetite for oil has led to closer political relationships with oil rich regimes that Secretary of State Rice asserts is “warping” China’s foreign policy.¹¹⁴ The need for oil gives the PRC an economic incentive to use its international influence in support of oil producing states. Here, we believe that the PRC has the potential to be either an ally or a counterweight to America’s political goals in the Middle East. To advance the potential for Chinese support, we make the following recommendation.

We argue that allowing Chinese oil firms to participate in overseas upstream activities integrates them into the global economy in a way that serves to shape and constrain Chinese foreign policy. As China diversifies its oil supply network, it has less incentive to expend energy defending or securing any one of those suppliers. For instance, China must be cautious in its support of Iran for fear of disrupting its relationship with Saudi Arabia. Coaxing a rising China into ever-deeper economic commitments will lead to a complex web of economic involvement. The final result should be the emergence of a multiplicity of new viewpoints to be considered in their formulation of foreign policy, which will give them a greater stake in regional stability.

Recommendation 3: Work to Secure the Interests of all Oil Dependent Economies

China defines stability far differently than the United States. It is willing to provide economic and military assistance (in the form of arms sales) to brutal but stable regimes in this pursuit, but its willingness to get involved beyond this level (i.e. guarantees of Chinese military involvement) has thus far been limited. Should China put its military and diplomatic weight behind its oil suppliers, this would certainly pose a significant risk to U.S. interests and U.S. security.

With China’s state owned firms investing in the energy infrastructure of Middle Eastern states, the PRC’s ability to stand clear of the internal affairs of the places in which they invest will be increasingly difficult. Eventually, Chinese oil firms will be faced with internal policies in some states that harm Chinese investments, and China will have to decide whether the principle of sovereignty – a core principle of China’s foreign policy – should be sacrificed to protect economic investments.¹¹⁵ Our research indicates that little serious thought has yet been given to the security implications of the stated goal to transform Chinese state-owned oil firms into true global players. This presents a strategic opportunity for the US in that China continues to depend on U.S. naval protection of major shipping lanes.¹¹⁶

¹¹⁴ Mufson.

¹¹⁵ *China’s foreign policy reflects two primary principles. First, the PRC wants to be seen as a responsible great power, not a threat to be challenged. Second, the PRC believes it is essential to defend the integrity of state sovereignty. Both of these principles help China’s oil companies make major investments abroad without causing fear that Chinese interventionism will soon follow.*

¹¹⁶ *China’s increases in military spending may eventually produce a traditional security threat to U.S. interests in East and Pacific Asia. While it is difficult to guess the nature of secretive military spending in China, the power to project naval power in remote areas would require a much more visible build-up than is currently taking place. In this regard, military preparations probably still focus on the well-documented preparations for a possible war over Taiwan.* Thom Shanker, “US Questions China on Arms Buildup,” *The New York Times*, May 24, 2006.

American policymakers should recognize that while Chinese commercial interests will increasingly call for the projection of Chinese power in the Middle East to protect their interests, Chinese power does not necessarily have to follow. Japan, the third largest importer of Middle Eastern oil, serves as an example. Like Japan, China currently receives the benefits of America's naval presence, while the United States maintains unquestioned military superiority. If the United States can convince China of its ability to protect the interests of oil dependent states in the Middle East and on the high seas, it might avoid the emergence of Chinese force in the region. China may never be as satisfied with U.S. dominance as Japan; however, the U.S. could take steps to make it more palatable to China. Seeking to promote a high-profile joint venture exploration project in the Middle East between U.S. and Chinese oil firms would be one example of a confidence building strategy designed to demonstrate to Chinese policymakers that the U.S. accepts Chinese international investments. This may assuage some of China's concern over the vulnerability of their foreign investments.

Recommendation 4: Emphasize the Confluence of U.S. and Chinese Interests

The U.S. must do all it can to pull China in the direction of using what power and influence it has as a responsible stakeholder in the international system, mostly because there is no feasible alternative. To this end, America must recognize that its current approach – to frequently scold China – has proven ineffective in Sudan, Iran, and even Zimbabwe. Chinese officials proudly put their nation's own interests ahead of what they perceive to be America's goals, and thus they continue to import Iran's oil and welcome its President even as the UN Security Council considers sanctions. American policymakers must identify how this behavior undermines China's interests, arguing that China is unnecessarily enriching those with a determined interest in undermining the international economic and political system that has given rise to both American and Chinese power. To counter China and Iran's mutual philosophy of multi-polarity, American policy must advance international policies that protect the capitalist system and the preeminence of the UN Security Council. Finally, while both states recognize the threat of terrorism exported from the Middle East, and neither can afford such developments, the United States must make a stronger case that Iran, China's long term friend, promotes the kind of instability feared by China.

In conclusion, rapidly growing Chinese energy imports from the Middle East should be watched closely, but on their own do not constitute a threat to U.S. interests in the region. China has shown a pragmatism on its oil supply sources that is a positive signal of their intention to diversify supply without making strong commitments of political or military support to one state over any other. Moves to restrict Chinese investment in oil fields only serve to push China further away from the U.S., possibly to the point of contemplating retaliatory moves such as more material military support for anti-American regimes. Engagement and cooperation with China on energy development is a far better option; it can help keep the price of oil stable and mitigate China's willingness to challenge the U.S. through support of states like Iran. Fears that China can "lock up" resources or create a military alliance in the SCO to rival NATO are significantly overblown. While Chinese military buildup is certainly cause for significant long-term concern, their activities in the Middle East do not yet constitute a real challenge to U.S. interests in the region.

Appendix: Chinese Security Policy and the Military Dimension of the SCO

The public face of Chinese security strategy is inwardly focused. Chinese leaders continue to be adamant that increased defense spending is “in accordance with economic development, to be used mostly for pay raises and benefits to soldiers. Only a small percentage will be used for equipment [arms, new technology, etc.]”¹¹⁷ Nonetheless, significant doubts remain among western experts about hidden spending.¹¹⁸ It is only very recently that any public discussion has begun to emerge on the protection of Chinese interests abroad or the projection of Chinese power and influence beyond the border defined by long-standing claims of sovereignty over Taiwan and the South China Sea. Where this issue is discussed, it is recognized as beyond the scope of current capabilities, and something that can only receive proper focus when the primary goals of “territorial integrity” and political stability have been achieved.¹¹⁹

In part, China's internal focus reflects recognition that domestic political problems, such as consolidation of power over restive non-Han regions (Tibet, Xinjiang), and especially the Taiwan issue, must form the core of any short-term strategic thinking. This is not to say that discussions of overseas projection of military power are not taking place secretly within the halls of Chinese political and military power, only that to date their secrecy has remained remarkably complete. From the Chinese perspective, their military is not modernizing fast enough even to deal effectively with their primary concern of Taiwan, let alone to expand its power projection capabilities beyond the region:

Military capabilities are lagging behind expansion of national interests. Major countries in the world are all increasing military spending, especially their information capability. The gap between developed and developing countries in military technology and capability is getting bigger. China still lacks the information capability to win a localized war, much less to live up to the fast expansion of national interests.¹²⁰

While some discussion has taken place within China of the potential for non-traditional threats, such as the ideological threat posed by radical Islam and terrorism, it has mostly been in reference to possible threats inside Chinese territory (i.e. Xinjiang), not to Chinese interests abroad. China has been wary of trying to enlist the support of even its closest partners in traditional security concerns, preferring to keep them at arm's length and focus on cooperation on other issues in the hope of building good will and allaying U.S. fears over Chinese designs on regional political/military dominance.¹²¹

¹¹⁷ Speech by Zhou Wenzhong, Chinese Ambassador to the US given at Georgetown University, October 5, 2005. Accessed on August 10, 2006 on Chinese Foreign Ministry website:

<http://www.fmprc.gov.cn/chn/wjb/zwjg/zwbd/t215308.htm>. Translation by John Keefer Douglas

¹¹⁸ Carrie Gracie, “China's Rise Leaves West Wondering,” BBC website, accessed August 12, 2006:

<http://news.bbc.co.uk/2/hi/asia-pacific/4797903.stm>. Also, the 2006 US Defense Department report, “Military Power of the People's Republic of China,” states, “Estimates place Chinese defense expenditure at two to three times officially disclosed figures.” (p. 5) Accessed September 1, 2006, at <http://www.defenselink.mil/pubs/pdfs/China%20Report%202006.pdf>

¹¹⁹ Yang Yi.

¹²⁰ Yang Yi.

¹²¹ Sun Xuefeng and Chen Hanxi, “The Strategic Impact of China's Regionalist Policy,” *World Economy and Politics (Shijie jingji yu zhengzhi)* 2006, no. 5. Translation by John Keefer Douglas.

In addition to internal Chinese defense policy, the SCO serves a security function for its member states, and the specter of a military alliance including China, Russia, and Iran has reportedly raised alarm in some hallways of the Pentagon.¹²² The SCO will hold joint “anti-terrorism” exercises next year in the Volga-Ural military district of Russia. The drills will be the first to involve all six SCO member countries, but they will not involve observer Iran. Although the scale of these activities has raised eyebrows, Chinese Foreign Minister Li Zhaoxing explains, “Such co-operation is strictly in line with the SCO's nature as a non-aligned organization which neither promotes confrontation nor targets any third country or organization.”¹²³ Central Asia experts generally agree that SCO security cooperation does not represent an anti-western military alliance intended to challenge NATO.¹²⁴

Despite assertions by experts after the 2006 SCO meetings, the SCO is far from being an anti-American military alliance through which China has exchanged security guarantees for Iranian oil. SCO members chose to delay the induction of new members, despite Iran's application to join, demonstrating that the current SCO membership is wary of military cooperation with the Islamic Republic.¹²⁵

Even the six core SCO member states are hesitant to work together due to a long history of conflict. China and Russia remain mutually suspicious, and the four smaller states have not forgotten the period of Soviet domination from which they have recently emerged. In fact, NATO's Partnership for Peace, to which all SCO members other than China and Russia belong, continues to play an active role in central Asia, and in September 2006 NATO will conduct “Steppe Eagle” military exercises in Kazakhstan, a major oil producer (forecast to produce more than Iran by 2012) with which the U.S. is eager to expand relations.¹²⁶ As scholar J. Brandon Gentry pointed out in 2005, the SCO is “a potential challenge to U.S. interests, but one which is in danger of being pulled apart by disparate aims and pressing economic limitations.”¹²⁷

¹²² Steven R. Weisman, “As the Price of Oil Soars, So Does Its Power to Shape Politics From Washington to Beijing,” *The New York Times*, July 25, 2006.

¹²³ Xing Zhigang, “SCO 'does not target any country'- FM,” *China Daily*, Updated: June 13, 2006.

¹²⁴ For instance, Kirill Nourzhanov, of Australian National University, told *The Financial Times*: “The image of a mighty and organically anti-western military alliance is misleading.” Geoff Dyer and Richard McGregor, “Opposition to US inspires 'Nato of the east' Is the Shanghai Co-operation Organisation a threat to the west?” *Financial Times* (London, England) June 22, 2006.

¹²⁵ Rowan Callick, “Shanghai group's power play,” *The Australian* (Australia), June 16, 2006.

¹²⁶ Vice President Cheney and Secretary of State Condoleezza Rice recently visited and praised the government. President Nursultan Nazarbayev is scheduled to visit Washington to meet with President Bush in September. “Vice President Cheney to visit Kazakhstan in May,” News Bulletin of the Embassy of the Republic of Kazakhstan, No16, April 25, 2006; Ariel Cohen.

¹²⁷ Gentry.

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