



**China's Oil Strategy:
The Potential of the Strategic Partnership with Saudi Arabia**

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DECLARATION

The work presented in this thesis entitled “China’s Oil Strategy: The Potential of the Strategic Partnership with Saudi Arabia” is entirely my own and was carried out between October 2007 and September 2011 at Durham University. Therefore, I declare that no portion of this thesis has previously been submitted for a degree in this or any other university.

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DEDICATION

الى روح والدي الطاهرة

To the Memory of My Beloved Father

To My Great Mum

To my Lovely Wife and our Three Angels – Leanne, Nadia and

Sam

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ABSTRACT

China's Oil Strategy: the Potential of the Strategic Partnership with Saudi

Arabia

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This thesis focuses on the growing relationship between China, the world's second-largest oil consumer, and Saudi Arabia, the world's top oil exporter. The high interdependence between China and Saudi Arabia represents a theoretical challenge: Does economic interdependence increase or decrease the probability of conflict between China and other significant energy users, notably the United States, over Middle East oil? The study is literature-based and expanded by exploratory case study research using different variables or indicators (import dependence, trade, energy, arms sales and political factors). The thesis' main aim is to investigate the causes of China's motives to establish a strategic relationship with Saudi Arabia and its implications for the United States, using a qualitative method with quantitative resources as primary data and the state as unit of analysis. On the basis of the theoretical frameworks, it raises three hypotheses, respectively: (1) China is not seeking to challenge the United States in the Middle East; (2) China will contribute to the stability of the Middle East because it expects its trade and energy imports from the region to increase in the future; and (3) China will not use the military means to protect its interests in the Middle East. To verify these hypotheses, the study attempts to address the theoretical flaws of both realism and liberalism in regard to Sino-Saudi relations, guided by Trade Expectation Theory (TET). The finding is simple: China's policy of strengthening its relationships with Saudi Arabia is neither aimed at undermining U.S. regional interests nor aimed at challenging the U.S.'s dominant position; it is primarily driven by economic imperatives.

KEY WORDS: CHINA, SAUDI ARABIA, U.S., MIDDLE EAST, INTERDEPENDENCE, OIL, ENERGY, LIBERALISM, REALISM AND TRADE

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REGIONAL AND COUNTRY GROUPINGS

Caspian

Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan

China

Refers to the People's Republic of China (PRC)

European Union

Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovak Republic, Slovenia, Spain, Sweden and United Kingdom.

G20

Canada, France, Germany, Italy, Japan, Russian Federation, United Kingdom, United States, Argentina, Australia, Brazil, China, India, Indonesia, Mexico, Saudi Arabia, South Africa, Korea, Turkey and the European Union.

GCC- Gulf Cooperation Council

Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates

Middle East (Oil Countries)

Iran, Iraq, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates and Yemen

North Africa

Algeria, Egypt, Libya, Morocco and Tunisia

North America

Canada, Mexico and the United States

OECD

Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Israel, Ireland, Italy, Luxembourg, Netherlands, Norway, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom, Canada, Mexico, United States, Australia and New Zealand

OPEC

Algeria, Angola, Ecuador, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, United Arab Emirates and Venezuela

Saudi Arabia

Refers to Kingdom of Saudi Arabia (KSA)

The League of Arab States

Algeria, Bahrain, Comoros, Djibouti, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Palestine, Qatar, Saudi Arabia, Somalia, Sudan, Syria, Tunisia, United Arab Emirates and Yemen

ABBREVIATIONS

ARAMCO: Saudi Arabian Oil Company
Bn: billion (1,000 million)
BofAML: Bank of America Merrill Lynch
Bpd: barrels per day
CAAGR: compound average annual growth rate
CIA: Central Intelligence Agency
CIA: China Islamic Association
CNOOC: China National Offshore Oil Corporation
CNPC: China National Petroleum Corporation
CRS: Congressional Research Service
CSIS: Center for Strategic and International Studies
DOE: The United States Department of Energy
DSCA: U.S. Defence Security Cooperation Agency
EIA: Energy Information Administration
EIU: Economist Intelligence Unit
ESCAP: The Secretariat of the Economic and Social Commission for Asia and the Pacific
ETIM: East Turkistan Islamic Movement
EU: European Union
FDI: foreign direct investment
FMCS: Military Construction Services
FMS: Foreign Military Sales
FTA: Free Trade Agreement
G20: The top 20 economy in the World
GCC: Gulf Cooperation Council
GDP: Gross Domestic Product
IAEA: International Atomic Energy Agency
IEA: International Energy Agency
IMF: International Monetary Fund
IRBM: Intermediate Range Ballistic Missiles
JCCI: Jeddah Chamber of Commerce and Industry
JDAM: Joint Direct Attack Munition
KSA: Kingdom of Saudi Arabia
Mb/d: Million Barrels Per Day
MEDB: Middle East Development Bank
MEED: Middle East Economic Digest
MEES: Middle East Economic Survey
MENA: Middle East and North Africa
Mn: million

MOFCOM: Ministry of Commerce of China
MOU: The memorandum of understanding
Mt: Metric Tonne
Mtoe: Million tonne of oil equivalent
MWA: Muslim World Association
Na not available
NBS: National Bureau of Statistics of China.
NCC: Saudi National Competitiveness Centre
NGL: Natural Gas Liquid
NPT: International Treaty on the Non-proliferation of Nuclear Weapons
ODI: Outward Foreign Direct Investment
OECD: Organisation for Economic Co-operation and Development
OPEC: Organization of the Petroleum Exporting Countries
PPP: Purchasing Power Parity
PRC: People Republic of China
QDR: Quadrennial Defence Review
RSAF: Royal Saudi Air Force
SABIC: Saudi Arabia Basic Industries Corporation
Sachem: Saudi International Petrochemical Company
SAGIA: Saudi Arabian General Investment Authority
SAMA: Saudi Arabia Monetary Agency
Samba: Saudi American Bank
SCCI: Council of Saudi Chambers of Commerce and Industry
SCO: Shanghai Cooperation Organization
Sinopec: China Petroleum and Chemical Corporation
SIPRI: Stockholm International Peace Research Institute
SWF: Sovereign Wealth funds
TN: trillion (million million)
U.A.E: United Arab Emirates
U.K: United Kingdom
U.S.: United States
UN: United Nations
UNCTAD: United Nations Conference on Trade and Development
USAF: U.S. Air Force
USGS: United States Geological Survey
WEO: World Energy Outlook
WTO: World Trade Organization

CHAPTER ONE

INTRODUCTION

1.1 OVERVIEW

This thesis focuses on the oil relationship established between The People's Republic of China (PRC), the world's second largest oil importer, and The Kingdom of Saudi Arabia (KSA), the world's top oil exporter. Due to Saudi Arabia's dominance of the world oil market, China is increasingly focusing its attention on the Kingdom as a reliable oil supplier while Saudi Arabia sees China as an enormous potential market and strategic trade partner. The study's main aims are: to investigate the causes of China's motives to establish a strategic relationship with Saudi Arabia; to outline the potential for successful co-operation between the two countries; and to address the wider implications for the U.S. in the Middle East.

Over the last three decades, China has been the world's fastest growing economy with annual growth over 9 percent. Today, China, the country with a population of over 1.3 billion, is the world's second largest economy. China could be the world's largest economy as early as 2016 (IMF, 2011) and is likely to be some way ahead of the U.S. by 2030 (PricewaterhouseCoopers, 2010). China's booming economy is leading to large increases in the demand for oil and China's need for oil is growing faster than any other country. China is drawn to the Middle East because of its need for oil. China was self-sufficient in energy until 1993 but, after three decades of rapid growth, it has turned abroad for its growing energy needs. The country now is the second largest oil consumer after the United States. China has been also a net oil importer and

is now the second largest, behind the U.S., and is expected to lead global consumption and imports in around twenty years (EIA, 2010).

According to the International Energy Agency (IEA), in 2010 the country's oil demand reached about 9.1 million barrels per day (IEA, July 2011), China only produced about 45 percent of the oil consumed (Ibid). The rest was imported, and about half of it has come from the Middle East (almost 20 percent from Saudi Arabia's alone), (Wang Qian, 2010). China, where demand has surged over the past decade, will contribute 36 percent to the projected growth in global energy use, its demand rising by 75 percent between 2008 and 2035 (IEA, March 2011). By 2035, China is projected to account for 22 percent of world demand, up from 17 percent today and could overtake the United States to become the largest oil consumer in the world (Ibid). That situation will lead to a high economic interdependence between China and the Middle East in general and Saudi Arabia in particular.

In this context, China views Saudi Arabia with great importance for three reasons: (a) Saudi's history as a reliable partner with all of its customers; (b) The Kingdom is the world's largest petroleum exporter, with current crude oil production capacity to around 12 million barrels per day. That is a capability unmatched in the industry (Al-Naimi, November 2010); (c) The Kingdom has a vast amount of oil which China desires. China realises that nearly 20 percent of the world's proven oil reserves are located in the Saudi Arabia (BP Statistical Review, 2011: 6), and nearly 60 percent of the world's proven oil reserves are located in the Middle East (Ibid); (d) Saudi Arabia is the largest economy among the Arab countries and the Kingdom is also a member of the Group of Twenty Finance Ministers and Central Bank Governors, (G20); and

(e) China recognises that Saudi Arabia, the leading member of the Organization of Petroleum Exporting Countries (OPEC), will play an increasingly vital role in supplying global energy in the future. Just less than 80 percent of the world's proven reserves are concentrated in eight countries, of which only Canada (with oil sands included) and Russia are not OPEC members (Oil & Gas Journal, 2009: 23-24). With all these issues in mind, China is turning to Saudi Arabia as a strategic trade and oil partner.

On the other hand, Saudi Arabia is adopting a "Look East" policy and sees China as one of the most important strategic markets for its oil exports. At the same time Saudi Arabia also has strong political, economic, and security relations with the United States. Thus, this study is the first attempt to discuss the evolution of oil relationship between China and Saudi Arabia within the framework of the interdependence model and the Trade Expectations Theory (TET). It wishes to set energy in a broader framework of strategic and regional change particularly the implications for the U.S. Furthermore, it is hoped that this study will inspire further research in relation to the issue of political economy, especially with regard to China's new role in the Middle East.

1.2 PROBLEM STATEMENT

Does economic interdependence between China and Saudi Arabia increase or decrease the probability of conflict between the U.S. and China in the Middle East?

With the growing of China's role at the global stage, there is heated debate about the impact of China's "rise" on the global system in general and the Middle East in particular. There are explanations provided by liberals and realists, but both fail to show the conditions under which high energy interdependence between China and Saudi Arabia in particular will lead to a pacific or belligerent China.

1.3 SIGNIFICANCE OF STUDY

China's rising demand for energy has been of special importance to the global political economy in recent years, and that will likely be even truer in the foreseeable future. In this context the challenge of energy security will grow more urgent in the years ahead. With the prospect that China will become the world's largest economy within the next decade, this study expects a significant increase in the volume of economic and oil interests in the Middle East. These interests make the study a great importance in understanding China's new role in the Middle East.

In this context, the concept of energy security in the Middle East will be a key theme for the U.S. and China for at least the next decade or two. As China is becoming a new player in the Middle East and its interests still evolving in the region, the study attempts to provide a comprehensive vision of the Sino-Saudi relationship, which could help to understand the Chinese behaviour in the region. Currently there is confusion about China's role in the Middle East and its relations with Saudi Arabia.

From this standpoint, the significance of this thesis is to clarify the relationship in a comprehensive and objective academic manner.

One of the original ideas provided also by the research is addressing China-Saudi relations through the use of international relations theories and in particular its development within the framework of the interdependence school of thought and the Trade Expectations Theory (TET). Further highlighting the importance of the study, the author, through his research, did not come across a single book addressing these relations in a comprehensive way as most previous literature focuses mainly on the American and Western influence in the Middle East. Today there is an important debate regarding China's role in the Middle East, and the main aim of this study is to shed light on those relations and open the way for other researchers to study the other important aspects which are not covered in this research. The author hopes that this study helps to fill some of the gaps and contributes positively to the debate.

Most important of all, in light of the developments that have swept the Middle East and North Africa in 2011 and the effects that have occurred in world energy markets, especially after the cessation of Libyan oil, the spotlight on China-Saudi relations is of great significance, (especially if we know that Saudi Arabia is the largest oil exporter in the world and China is the second largest oil consumer and importer) as it will help to understand China's role in the region and her impact in the region in an objective way. Additionally, there are doubts among many of the ruling elite in the Middle East in general and Saudi Arabia in particular, about the U.S.'s credibility as a strategic ally after they witnessed the speed of how the American Administration abandoned its allies in the region. Here comes another important point of the research as it sets out

to provide a clear understanding about China's intentions in the region, and to examine if China could provide a strategic alternative to the United States.

1.4 AIMS & OBJECTIVES OF THE STUDY

This study aims to assess the growing China-Saudi relations by directly evaluating the logic behind it and uncovering the scope of the relations. In doing so, the study attempts to correlate directly the developments and trends in Saudi Arabia's relations and the impact of the United States. To facilitate identified aims, the following objectives are developed:

- To fill a gap in the literature and stimulate a debate on China's new role in the Middle East by looking specifically at Sino-Saudi relations.
- To suggest an evaluative and analytical research framework needed to determine China's intentions towards Saudi Arabia and the Middle East.
- To identify the challenges and obstacles of China-Saudi relations and their impact on the U.S.
- To evaluate future scenarios for China-Saudi relations and its implications on U.S. policy.

1.5 RESEARCH HYPOTHESES & QUESTIONS

According to Cooper and Schindlerth, research literature disagrees about the meaning of the terms proposition and hypothesis (Cooper & Schindler, 1998: 43). They argue that the immediate purpose of explorations (research) is usually to develop hypotheses or questions for further research (Ibid: 131). A research proposition is a statement about the concept that is judged as true or false if it refers to observable phenomena. When a proposition is formulated for empirical testing, it is called a hypothesis. As a declarative statement, a hypothesis is of a tentative and conjectural nature (Ibid: 43). In that regard the following research hypotheses were formulated:

- **H1: China is not seeking to undermine the American influence, but is looking to secure its energy needs and meet its expanding economic interests.**

To decipher China's objectives H1 is required in order to investigate two research questions, Q1 and Q2:

Q1: What have been China's core (or primary) objectives in pursuing closer ties with Saudi Arabia?

The thesis tries to decipher Chinese intentions toward Saudi Arabia. This is the main question of the thesis and attempts to address whether Chinese actions were in accordance within the realism model or the economic interdependence school of thought. If China is acting in the realism model (offensive), it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence. If China is acting in accordance with the economic

interdependence model, it should interact economically with Saudi Arabia in a manner which makes economic sense; and developing a Sino-Saudi relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship.

Q2: Why does the Middle East region have particular significance for China in meeting its energy objectives (or security)?

- **H2: China will support the stability of Saudi Arabia because it expects a significant increase in its trade/energy with Saudi Arabia in the future.**

To measure Saudi Arabia's significance for China and Beijing motivations H2 is required in order to answer two questions, Q3 and Q4:

Q3: Why is Saudi Arabia an indispensable partner for China?

Q4: What is the nature and extent of China's strategic motives in pursuing a partnership with Saudi Arabia?

- **H3: China will work to protect its interests in the region through economical and political means and not through using military power.**

To look at the balance between energy and politics in China-Saudi relations and to examine if China could provide a strategic alternative to the United States H3 is required in order to answer two questions, Q5 and Q6:

Q5: Does the relationship between China and Saudi Arabia suggest that this is a strategic – political or energy – economic partnership?

Q6: What are the implications for the region and the United States?

1.6 RESEARCH DESIGN & METHODOLOGY

To answer these questions, this thesis will be using the single case study with qualitative method. This study will adopt literature, statistical analysis and document analysis to unfold its arguments. The case that will be examined is Saudi Arabia. This case was picked because Saudi Arabia not only has the world's largest oil reserves, but it's also the top oil exporter to China. Saudi Arabia also is the largest economy in the Middle East and North Africa (MENA) and China's top trade partner in this region since 2001. Further highlighting Saudi Arabia importance to China, it is the only "swing producer" capable of substantially increasing output in a short period of time. In addition, Saudi Arabia plays a vital role in the U.S.'s strategy in the Middle East. Taking into account these important issues, the case study will provide strong indication about the Chinese intentions and objectives in the region.

The next sections will describe the methods used in conducting this case study research. They explain why the case study methodology was selected, the components of a case study, the rationale for the procedures used in the case study and how the study was analysed and reported.

1.6.1 Research Process

- **Step 1:** My interest in the relations between China and Arab countries began at the start of my career, but this interest expanded academically during my

time at Durham University in 1999, while writing my Master's dissertation on oil projects in the Caspian region. After my graduation, I worked at the League of Arab States in London and with several Arab press institutions and through these roles I began to follow closely the Chinese policy in the Middle East and start formulating the research interests over the years.

- **Step 2:** At this point some important developments emerged. In January 2006 Saudi King Abdullah visited China and it was his first visit after assuming the throne in 2005. Three months later Chinese President Jintao Hu visited Saudi Arabia. I was then working in the economic section of Pan-Arab daily newspaper *Asharq al-Awsat* in London, where we covered extensively those visits. During that time the idea of my thesis begun to take shape as I started to investigate the topic in an academic way, using all resources available to me about China's Middle Eastern policy. Meanwhile, through my work's experience and attending many international conferences, I became convinced that my idea is significant for several reasons: (a) The lack of the number of qualified Arab (and Saudis) professionals specialising in China; (b) The absence of comprehensive references on Chinese-Arab relations in general and Saudi Arabia in particular; and (c) China's new rule in the region started to generate a "hot" political debate in the region. The whole experience was useful in gaining an early understanding of the topics and developing the study's objectives and defining my research question.
- **Step 3:** I started looking extensively at literature on the subject studied using manual and computer-based methods. In addition to attending several

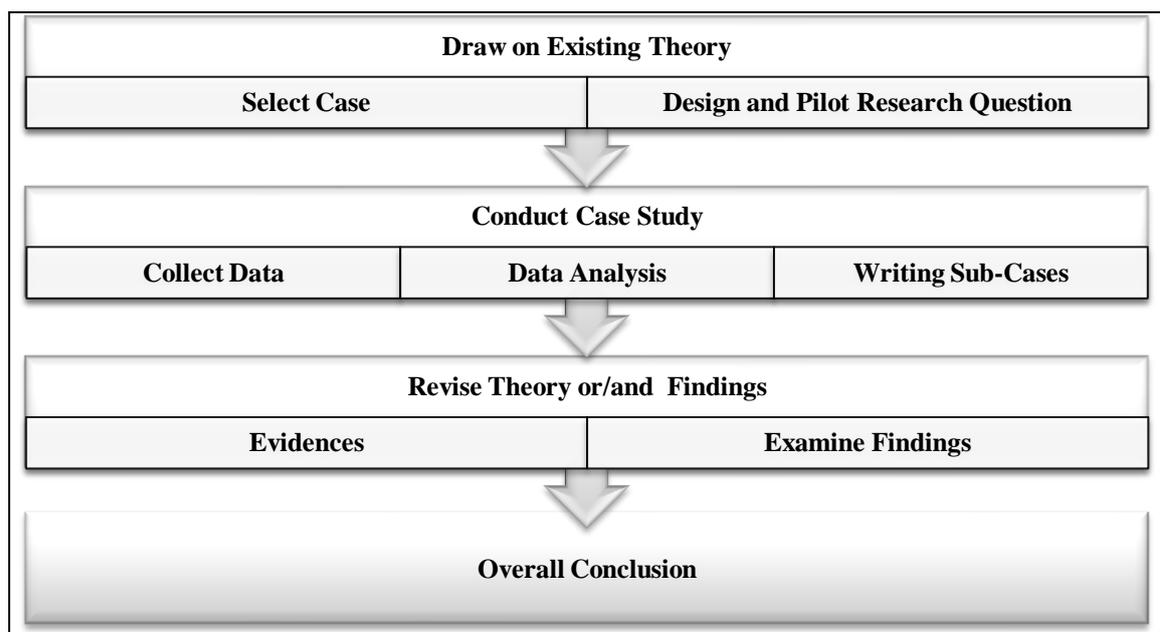
conferences and seminars, several discussions with the academic supervisor, colleagues and professional staff in selected organisations were also conducted to extract valuable information in order to construct a framework for this research. This was followed by the formulation of a theoretical framework which formed a structure for the study. The study started to generate a large amount of data from multiple sources, so I had to go through databases in order to categorise, sort, store, and retrieve data for analysis.

- **Step 4:** At this stage I started preparing the research design. As time passed I found out that a case study is a particularly useful strategy when: (a) “How” or “why” questions are being posed; (b) The investigator has little control over events; and (c) The focus is on a contemporary phenomenon within its real-life context. Additionally, that “case” should be addressed within theories of international relations and political economy (liberalism and realism in particular) for the following reasons: (a) The decisions of China-Saudi relations are taken at the highest political levels; (b) Most of the trade and commercial exchanges are between the National Oil Companies (NOC); and (c) The relations are strategic in nature and they have regional and international dimensions and repercussions.
- **Step 5:** The next step was collecting the data. Information and data that were collected in stage 4 were analysed and evaluated using many interpretations in order to find linkages between the research case and the outcomes with reference to the original research questions. A qualitative approach was adopted for the China-Saudi study since it is well suited to the questions that

require exploration, where a detailed, close-up view is needed and where phenomena is to be studied in their natural setting. This approach enabled processes to be explored and linkages between different aspects of political and historical context, levels of commercial exchanges, energy trade and investments and the military dimensions, and the various interested parties to be teased out. In all cases, the author treated the evidence fairly to produce analytical conclusions.

- **Step 6:** The next stage was generalisation and interpretation, then preparation of the report which contains the conclusion for each case (chapter) which leads us to reach the overall conclusion and answer the research’s main question. Here, I hope that the final results will be compelling and open the way for other researchers to discuss the subject from different angles so it can be a benefit to everyone. Figure 16.1 summarises the whole process of the thesis.

(Figure 1.6.1.1): Research Process



1.6.2 What is Research?

The difference between research and non-research activity is in the way we find answers: the process must meet certain requirements to be called research. The research is a process of trying to gain better understanding of the complexities of human experience and, in some genres of research, to take action based on that understanding, (Marshall & Rossman, 1999: 21). Through systematic and sometimes collaborative strategies, the researcher gathers information about actions and interactions, reflects on their meaning, arrives at and evaluates conclusions, and eventually puts forward an interpretation most frequently in written form (Ibid). Therefore, this “research” investigates the causes of China’s motives to establish a strategic relationship with Saudi Arabia, and to address the wider implications for the U.S. in the Middle East.

1.6.3 Research Strategy and Study Design

Research designs refer to the overall strategy or approach of the study. In this case the research strategy is determined by the nature of the research question. Research strategies are merely tools: it is the researcher’s responsibility to understand the variety available and the different purposes of each strategy, to appreciate in advance the ramifications of selecting one method over another, and to become astute in the selection of one method over another, (Morse, 1994: 220-235). The design is a crucial part of research development because it enables your research to be investigated

efficiently. In other words the research design provides the “glue” that holds the research project together. Cooper and Schindler define research design as the plan and the structure of investigation so conceived as to obtain answers to research questions. The plan is the overall scheme or programme of the research. It includes an outline of what the investigator will do, from writing hypotheses and their operational implications and the final analysis of data. A structure is the framework, organisation, or configuration of the relations among variables of a study, (Cooper, Schindler 2003: 146). Or as Zikmund puts it: a research design is a master plan specifying the methods and procedures for collecting and analysing the needed information, (Zikmund, 2006: 65).

In this regard, Yin suggested that the three conditions could determine the type of research programme indicated: (a) The type of research question; (b) the degree of investigator controls possible; and finally, (c) the degree of focus on contemporary events desired versus historical events, (Yin, 1984: 23). Table 1.6.3 provides an outline of the relative performance of each type of research strategy under each condition.

(Table 1.6.3.1): Relevant Situations for Different Research Strategies

Strategy	Form of Research Question	Requires Control Behavioural Events?	Focuses on Contemporary Events?
Experiment	How, why?	Yes	Yes
Survey	Who, what, where, how many, how much?	No	Yes
Archival Analysis	Who, what, where, how many, how much?	No	Yes/No
History	How, why?	No	No
Case Study	How, why?	No	Yes

Source: Yin, 2003:5

Yin explained that “What” questions usually suggest that exploratory research is indicated, or may actually be rephrased as ‘how many’ or “how much” questions? “How” and “why” questions are more explanatory by nature, and are likely to lead to the use of experiments, histories and case studies. These questions tend to deal with operational links which occur during a span of time, rather than the incidents or phenomena which occur at intervals over time, (Ibid). In this context, as our form of research question is “how” and “why” with the focus on contemporary issue (China-Saudi relations), that makes the case study strategy the logical choice.

1.6.4 Case Study as a Strategic Methodology

This research reviews the literature on case study as a strategic qualitative research methodology. Although case studies have been criticised by some authors as lacking scientific rigour and do not address generalisability, this research, however, reiterates its appropriateness when dealing with a process or complex real-life activities in great depth. Case study has been commonly used in social science fields like sociology, industrial relations and anthropology even though generally it was considered an underutilised strategy, (Mohd Noor, 2008: 1602-1604). Case study research excels at bringing us to an understanding of a complex issue or object, and can extend experience, or add strength to what is already known through previous research. Case studies emphasise detailed contextual analysis of a limited number of events or conditions and their relationships, (Ibid). In this context, the case that will be examined is China’s oil policy towards Saudi Arabia within the economic

interdependence theory. This case was selected because Saudi Arabia not only has the world's largest oil reserves, but it's also the top oil exporter to China. Saudi Arabia is also the largest economy in the Middle East and North Africa (MENA) and has been China's top trade partner in this region since 2001. Further highlighting Saudi Arabia importance to China, it is the only "swing producer" capable of substantially increasing output in a short period of time. In addition, Saudi Arabia plays a vital role in the U.S.'s strategy in the Middle East. Taking into account these important issues, the case study will provide strong indication about the Chinese intentions and objectives in the region.

1.6.4.1 What is Case Study?

A case study is a research methodology common in social science and it is based on an in-depth investigation, (Shepard, 2003: 22). According to Stacks, case studies are in-depth studies of particular people, organisations, events, or even processes. They provide a richly detailed and complete understanding of the case under study that is not available through other methods, (Stacks, 2002: 169). The case study is an obvious extension of secondary research, although when researching a case study other qualitative methods may also be employed, particularly interviewing and in some instances focusing on groups and participant-observation. Furthermore, case studies often include quantitative data obtained from secondary research or from studies reported in various documents (Ibid: 157). Robert Yin defines the case study research method as an empirical inquiry that investigates a contemporary

phenomenon within its real-life context (Yin, 1994: 23). The case study is the most flexible of all research designs, allowing the researcher to retain the holistic characteristics of real-life events while investigating empirical events. In general, a case study is an empirical inquiry which (a) investigates a contemporary phenomenon within its real-life context when (b) the boundaries between phenomenon and context are not clearly evident; and (c) in which multiple sources of evidence are used (Ibid).

Gilgun argues that the case study research is important because of its contributions to theory. A case study is an intensive look at an individual unit, (Gilgun, 2011: 1-6). In political science, the archetypal case is the dominant political unit of our time, the nation state. However, this is a matter of convention. The study of smaller social and political units (regions, cities, villages, communities, social groups, families) or specific institutions (political parties, interest groups, businesses) is equally common in many social science disciplines, (Gerring, 2007: 19). Gerring goes further to give the “case study” a more comprehensive definition: (a) that its method is qualitative; (b) that the research is holistic, thick (a more or less comprehensive examination of a phenomenon); (c) that it utilises a particular type of evidence (e.g., ethnographic, clinical, non-experimental, non-survey-based, participant-observation, process-tracing, historical, textual, or field research); (d) that its method of evidence gathering is naturalistic (a “real-life context”); (e) that the topic is diffuse (case and context are difficult to distinguish); (f) that it employs triangulation (“multiple sources of evidence”); (g) that the research investigates the properties of a single observation; and (h) that the research investigates the properties of a single phenomenon, instance, or example (Ibid: 17).

1.6.4.2 Strength & Weakness of using Case Study

Case study methods, referring now to single case as well as comparative designs, offer several significant advantages relative to statistical methods. (a) More comprehensive and more detailed it can stimulate new research and contradict established theory, (Hayes, 2000: 133). (b) Case studies are generally better than the alternatives for documenting processes. The world political economy is marked by significant processes - market innovation, competition, collusion, equilibrium, influence, bargaining, communication, conflict, learning, institutional change, regional integration and disintegration, and politics. (c) Case methods allow stronger empirical grounding for a hypothesis for the cases studied. Fuller reporting makes it more likely that readers will construct alternative interpretations of the same events and generate new hypotheses.

However, case studies have been criticised by some as lacking in scientific rigour and reliability and that they do not address the issues of generalisability, (Johnson, 1994: 47). Critics of the case study method also believe that the study of a small number of cases can offer no grounds for establishing reliability or generality of findings. Others feel that the intense exposure to study of the case biases the findings. Some dismiss case study research as useful only as an exploratory tool, (Ibid).

1.6.4.3 Research Method & Strategy

It is obvious that the first question that comes to mind is: What Is Research Methodology? The system of collecting data for research projects is known as research methodology. There are two basic methodological traditions of research in social science, namely positivism and post positivism (phenomenology). Positivism, thus, which is based on the natural science model of dealing with facts, is more closely associated with quantitative method of analysis. Quantitative research uses mathematical measures and statistical techniques to determine relationships and differences among large samples of target populations, (Shao, 1999: 151). Highly structured, quantitative research involves designing questions with a choice of specific responses so that the responses can be measured and analysed mathematically, (Ibid). On the other hand, post-positivism that deals with understanding the subjectivity of social phenomena, requires a qualitative approach, (Noor, 2008). Qualitative research is less formally structured than quantitative research and it uses smaller samples. The data gathered using qualitative techniques is subjective and non-quantifiable, (Shao, 1999).

The qualitative case study is an approach to research that facilitates exploration of a phenomenon within its context using a variety of data sources. This ensures that the issue is not explored through one lens, but rather a variety of lenses which allows for multiple facets of the phenomenon to be revealed and understood, (Baxter, 2008: 544-559). Qualitative methods, according to Landman, “seek to identify and understand the attributes, characteristics, and traits of the objects of inquiry, and the nature of the method necessarily requires a focus on a small number of countries”, (Landman,

2008: 68-8). Yin argues that five features distinguish qualitative research from other kinds of social science research, (Yin, 2011: 7-8): (a) Studying the meaning of people’s lives, under real-world conditions; (b) Representing the views and perspectives of the people in a study; (c) Covering the contextual conditions within which people live; (d) Contributing insights into existing or emerging concepts that may help to explain human social behaviour; and (e) striving to use multiple sources of evidence rather than relying on a single source alone.

According to Yin there are three types of case study research and these are exploratory, descriptive, and explanatory, (Yin, 1984: 11-15). Researchers in business-related subjects sometimes limit case studies to the exploratory use. For example, pilot case study can be used as a basis for formulating questions or hypothesis testing. Descriptive case study is an attempt to describe, for example, what happens to a product when it is launched. Explanatory research can be useful for example to study processes in companies, (see Table 1.6.4.3.1).

(Table 1.6.4.3.1): Main Types of Case Study Research

Case Study Type	Definition
Explanatory	This type of case study would be used if you were seeking to answer a question that sought to explain the presumed causal links in real-life interventions that are too complex for the survey or experimental strategies. In evaluation language, the explanations would link program implementation with program effects.
Exploratory	This type of case study is used to explore those situations in which the intervention being evaluated has no clear, single set of outcomes.
Descriptive	This type of case study is used to describe an intervention or phenomenon and the real-life context in which it occurred.

Source: Yin, 2003

Exploratory research will be used in this study to provide greater understanding of China-Saudi relations through defining the nature, motives and the scope of these relations within regional and global context. The qualitative case study establishes general hypotheses about the actions of the actors in their particular context. The case study in this research considers the nature of China's behaviour towards Saudi Arabia as the dependent variable. The independent variables, political contacts, trade, investment, energy, arms sale and technology transfer, provide a framework for analysing the topic.

1.6.5 Research Strategy

In social research two reasoning methods are used to find a relationship between research theory and the data collected. *Deductive* reasoning works from the more general to the more specific. Sometimes this is formally called a "top-down" approach. Conclusion follows logically from premises (available facts). *Inductive* reasoning works the other way, moving from specific observations to broader generalisations and theories. It is important to acknowledge that there are elements of deduction in qualitative research, as there is induction in quantitative research.

(Table 1.6.5.1): Deduction and Induction in Research

Key Stages in Deduction	Key Stages in Induction
<ul style="list-style-type: none">• Draw on existing theory• Conjecture hypothesis• Collect data• Examine findings• Confirm or reject hypothesis• Revise theory	<ul style="list-style-type: none">• Select general research question• Select sites and participants• Generate data• Interpret data• Develop concepts• Repeat the above cycle• Generate hypothesis

Source: Miller, 2010: 60

Positivism emphasises that scientific knowledge is arrived at through the accumulation of facts, made possible by hypothesis testing. Science is a compendium of empirically established facts, and scientists get progressively closer to discovering the ‘right’ explanations. Here, the purpose of science is to generate hypotheses that can be tested, thereby allowing explanations to be assessed. This is deduction, (Rhodes, 2010: 60). On the other hand qualitative researchers usually begin with a general explanatory question or with preliminary concepts (rather than a specific hypothesis). They then collect data, observe patterns emerging in the data and organise these into a conceptual framework. This is done by systematically comparing empirical cases to see whether emerging hypotheses fit. If not, the hypothesis is reformulated (or the phenomenon re-defined to exclude the case). The discovery of negative cases disproves the explanation and requires a reformulation. This is induction, (Ibid: 61). This cycle may be repeated several times until a conceptual framework is well developed, and until new data yields only minimal or no new information, (Ibid).

As the aim of this research is to analyse China-Saudi relations and its implications on the U.S., the *deductive* reasoning approach could not be used due to the exploratory

nature of the study (as discussed in the research design section). Therefore, this study adopted the *inductive* reasoning approach in order to find general patterns of China's behaviour towards Saudi Arabia and evaluate its implication on the U.S. This study has adopted a qualitative method with quantitative resources as primary data. Since large amount of data exists, in general terms, on the subjects of interest, it is clear that use of the quantitative resources to address the objectives outlined was a time consuming but very productive task when employed in this context. This is important, as new findings on the investigation subject have been investigated in a comprehensive way, as issues related to energy security in both China and Saudi Arabia are considered as strategic issues and will be dealt at the highest levels.

The quantitative secondary resources will be used primarily for this thesis. The resources selected for this study will be authoritative and mainly from official speeches, interviews and statistical economical reports from several international organisations such as the IMF Direction of Trade Statistics (DoTS), the World Bank, the United Nations (UN COMTRADE) and China/Saudi Arabia official statistics. The study will also explore the reports published by energy analysts. Data and analysis for oil supply and demand will be adapted from reports such as the International Energy Agency (*World Energy Outlook*), Energy International Agency (*EIA's World Energy Outlook*), The United States Department of Energy (DOE), International Energy Outlook (IEO), Organization of Petroleum Exporting Countries - OPEC- (*World Oil Outlook*) and *BP Statistical Review of World Energy*. The literary research will also involve books, newspapers, pamphlets, grey literature and laws; published and unpublished statistical material. As for the military statistical data that will be gathered from the U.S. Congressional Research Service (*Conventional Arms*

Transfers to Developing Nations), Stockholm International Peace Research Institute (*SIPRI Yearbook*) and the U.S. Defence Security Cooperation Agency, (*DSCA Historical Facts-book and Fiscal Year Series*). Internal validity is automatically established in qualitative research because the group acts as its own point of reference. External validity cannot be established in the traditional sense with qualitative approach because it is not trying to reach a general conclusion about the population. Instead, validity for qualitative research is best described as rigorous, credible, and trustworthy.

1.7 LIMITATIONS OF STUDY

As for the limitations, similar to any other study, this study also has a certain limitation as an inevitable part of controlled research. The main limitation of this thesis is the fact that the study focuses on the oil sector as a result of its centrality in the development of China-Saudi relations; this fact may also serve as a limitation because this case will not show how China's policies are geared for non-energy sectors; however, this limitation is not vital since: (a) Much of the China-Saudi relations revolves around the oil sector; and (b) China's activities in Saudi Arabia is driven by its desire to improve its energy security.

The thesis focuses on relations between China and Saudi Arabia at the state level (or within the perspective of international relations) and does not focus on the sectoral level (i.e. oil companies, political lobbying, human rights organisations or even individuals, etc.). This limitation also is not vital since: (a) Oil is vitally important to

national survival and the enhancement of national power, in the cases of Saudi Arabia and China, to regime survival as well, one must consider the political-strategic subtext of Sino-Saudi relations; (b) The political system in both countries is authoritarian; therefore, issues related to energy security will be considered as strategic issues and will be dealt at the highest levels; (c) China-Saudi relations have been largely restricted to oil exports to China and limited cross-investment. (d) Saudi Arabia does not allow Chinese companies to invest in its upstream (exploration and production) oil sector; (e) Chinese companies are new players in Saudi Arabia and do not contribute to the formation of the oil sector in Saudi Arabia, which is the case with U.S. companies.

Furthermore, it was very difficult to obtain official documents relating to oil or economic agreements between China and Saudi Arabia, due to the secretive system in both countries. Thus, it is important to note here that this shortcoming is not just facing the author alone, even the international institutions (the International Energy Agency in particular) complained on several occasions about the lack of transparency in the oil sector, both in China and Saudi Arabia. The irony also here is that even the Chinese and the Saudis complain about each other in that issue. In addition, conducting interviews was rather difficult, as it was difficult to schedule (or travel to) an appointment for an interview with some participants particularly those in high positions. It's important to note that personal and logistics reasons prevented the author from travelling to conduct private interviews with senior Chinese/Saudi officials. Despite the limitations and difficulties, the study helps us get an expansive picture of the Sino-Saudi relations, its nature with respect to the oil sector and the factors associated with its success and growth. The study also provides an analysis to

the future developments by providing the true picture of the relations which could help many scholars and decision-makers to pursue objective and pragmatic policies.

1.8 THE ORGANISATION OF THE RESEARCH

The research consists of eleven chapters; three of them or part I (Chapters one, two and three) are related to the theoretical foundations of the study. Seven others (from three to nine) are devoted to the empirical study; while Chapter ten presents the implication for the United States and puts forward the future scenarios. Finally Chapter eleven provides the overall conclusion and the key finding of the study.

Chapter one starts with an introduction to the research. It provides a statement of the problem, significance of the study, aim and objectives of the study, research hypothesis, research design and methodology as well as the outline of the research. While Chapter two lays the theoretical foundations of the research, it also attempts to provide a comprehensive survey of the nature and implications of China's growing role in the Middle East and its developing relations with Saudi Arabia from the realist and liberal perspectives. In the first two sections, studies from various fields, such as realist theories, liberal school of thought, political economy and foreign policy analysis are reviewed in conjunction with an analysis of their most studied research questions, key variables, policy prescriptions and contribution to the overall study of China-Saudi relations. The third section of Chapter two discusses China's energy concept and how China's growing dependence on foreign oil will affect its

international behaviour. Chapter three will play a very important role in the theoretical argument as it provides statistical data to China's oil needs and how it fits with its oil strategy. This chapter will specifically try to answer the question: why does the Middle East region have particular significance for China in meeting its energy objectives (or security)? Subsequently, the chapter will give strong indications of China's intentions towards its relations with the Middle East.

The next three chapters try to (or part II) explain the logic behind the emerging Sino-Saudi relations and attempt to find answers for questions three and four. Indeed, Chapter four provides an explanation of the development of relations between China and Saudi Arabia in the scope of historical and political context. That brings us logically to Chapter five, which will measure Saudi Arabia's significance for China and examine Beijing motivations to answer questions three and four. Chapter six presents in detail the Saudi policy toward China, as the picture cannot be complete without discussing the Saudi perspective of China.

Having established the nature and the logic of China-Saudi relations; part III (Chapters seven, eight and nine) provides further empirical evidences and looks at the balance between energy and politics in China-Saudi relations and examines if China could provide a strategic alternative to the United States. Chapter seven explores the scope of the economic relationship that China and Saudi Arabia have formed over the two decades. The following will be examined in the economic realm: (a) The scope of trade ties; and (b) Cross- investments. Additionally the chapter will identify the opportunities and impediments for China-Saudi relations. Chapter eight discusses oil ties between the two countries and provides strong evidence to show that the oil trade

is at the heart of the emerging relations between China and Saudi Arabia. Furthermore the chapter will also identify the impediments for the oil trade between the two countries. Chapter nine examines the military affairs and technology transfers that China and Saudi Arabia have formed over the last three decades. The variety and volume of Sino-Saudi arms sales will be examined in the context of the global arms trade.

Having uncovered the scope of the Saudi-China relationship, consequently Chapter ten assesses the implications for the U.S. as the dominant power in the region and attempts to predict some future scenarios. Finally, Chapter eleven presents the overall conclusion and the key finding of the case study based on the empirical findings of the research, in addition to the recommendations and suggestions for further research.

China and Saudi Arabia (Selected Data and Indicators 2010)

 Saudi Arabia	Country	 China
 Head of state, prime minister: King Abdullah Bin-Abd-al-Aziz Al Saud	Leader	 Head of state: President Jintao Hu
US\$448.3 billion	GDP	US\$5.8 trillion
23	World's Ranking by GDP	2
55	World's Ranking by Human Development	89
17	World's Ranking by Competitiveness	26
129	World's Ranking by Gender Gap	61
Monarchy	Political System	Communist state
Kingdom of Saudi Arabia (KSA)	Official Name	People's Republic of China established (PRC)
23 September 1932 (unification of the Kingdom)	Independence Date	October 1, 1949
Saudi riyals (SAR))	Currency	Renminbi Yuan (RMB)
Middle East, bordering the Gulf and the Red Sea, north of Yemen	Location	Eastern Asia, bordering the East China Sea, Korea Bay, Yellow Sea, and South China Sea, between North Korea and

		Vietnam
2,149,690 km sq	Area	9,326,410 km sq
27,136,977	Populations	1,342,700,000
Riyadh	Capital	Beijing
Riyadh (population: 4,205,960)	Largest city	Shanghai (population: 14,608,500)
US\$16,641	GDP per Capita	US\$4,283
39	World's Ranking by GDP per Capita	95
85.0	Literacy Rate (%)	93.3
50	Worldwide Corruption Perceptions Ranking	78
Legal	Death Penalty	Legal
Muslim 100%	Religion	Daoist (Taoist), Buddhist, Christian 3%-4%, Muslim 1%-2% <i>note: officially atheist (2002 est.)</i>
Arabic	Languages	Standard Chinese (or Mandarin)
10.0	Unemployment Rate	4.1
petroleum and petroleum products 90%	Exports	electrical and other machinery, including data processing equipment, apparel, textile, iron and steel, optical and medical equipment
7	World's Ranking by Military Expenditure global	2
2,640 km	Coast Line	14,500 km

Source: IMF, World Bank, UN, Transparency International, World Economic Forum, CIA's World Factbook, Stockholm International Peace Research Institute, NBS and Saudi Central Department of Statistics & Information (CDSI), (all figures as for 2010)

CHAPTER TWO

THE THEORETICAL FRAMEWORK

2.1 INTRODUCTION

According to the International Energy Agency (IEA), China had overtaken the U.S. as the world's biggest energy consumer by the end of 2009, (IEA, July 2010). Furthermore, by the end of 2010, China had also overtaken Japan to become the world's second largest economy, (U.N., March 2010). Most important of all, in 2010, China had become the world's top manufacturing country by output, returning the country to the position it occupied in the early 19th century and ending the U.S.'s 110-year run as the largest goods producer, (Marsh, March 14, 2011). China, by 2010, even had surpassed the World Bank as the largest lender to developing nations, particularly in Africa, the Middle East and South East Asia, (Dyer, January 18, 2011). The year of 2009 will also be remembered in the Beijing's economic history as when China surpassed Germany as the world's biggest exporter, (Atkins, February 9, 2010). Additionally, China became the world's largest automobile market, having surpassed the U.S. (*The Wall Street Journal*, January 12, 2010) and the world's second largest oil importer, (Bloomberg, January 27, 2010).

This impressive performance and rapid economic expansion of China, coupled with its high level of growing oil imports has stimulated a heated debate over China's role in the Middle East and potential conflict in the region between China and the United States over oil. What are the international repercussions of the "rise" of China in the Middle East? Will prosperous China contribute to regional prosperity or threaten

American interests in Saudi Arabia? Will a strong China be tempted to use military power to challenge the American “order” in the Middle East, or will it be constrained by potent forces of global economic interdependence? Will a more open and reform-oriented China gradually move towards political liberalisation, thus enhancing the stability and security in the Middle East, or will it throw its weight around and challenge the American hegemony in the Middle East, providing Saudi Arabia with a political and military alternative to America? On the other hand will the United States try to contain China in the Middle East and block its access to the region’s resources, or will it be cooperative and understand the Chinese genuine need for energy to sustain their economic growth?

There has certainly been no shortage of publications that address some of these important questions. However, while the analysts may occasionally refer to some international relations theories or make some theoretical points in their discussion, little systematic effort has been made to place the entire debate on the “China’s challenge” within specific theoretical framework. One consistent shortcoming in much of the literature is that the analysts speak past each other rather than addressing the different views about this complex subject, or as Kristin Forbes, a former member of the White House Council of Economic Advisers and a professor at the Massachusetts Institute of Technology, puts it, “China is the West’s greatest hope and greatest fear...no one was quite ready for how fast China has emerged”, (*New York Times*, January 27, 2010).

This chapter attempts to provide a comprehensive survey of the nature and implications of China’s growing role in the Middle East and its developing relations

with Saudi Arabia from the realist and liberal perspectives, because as Harvard University Professor Stephen Walt puts it, “Two international relations theories, liberalism and realism, that are relevant to the central government’s efforts and describe the general policies that each exhibits”, (Walt, 1998). The thesis argues that while both school of thoughts have made useful contributions to the current debate, neither of them is adequate in offering satisfactory answers to the questions raised above. China’s oil strategy is yet to be understood clearly, conflicting incomplete information, changing circumstances and an occasional measure of “paranoia” or “theoretical mentality” of the Cold War has led to speculation over concrete analysis. Or as Daniel Yergin described it in very interesting words: “China’s thirst for energy has become a decisive plot element in suspense novels and films”, (Yergin, 2006: 69-82).

It is, therefore, necessary to combine the strength of two theories to reach proper understanding of China-Saudi relations and its implications to the region and the United States. More specifically, I will be guided by the theory of trade expectation to the analysis of factors that will shape China’s oil policy towards Saudi Arabia. Given their different intellectual origins and theoretical orientations, realism and liberalism have provided divergent interpretations of consequences of China’s oil policy towards Saudi Arabia. Most realists believe that an economically powerful China will become more assertive and expansionist, because of structural constraints. As China’s capabilities increase, they argue, its intentions will become less benign and within this context they see China’s actions in the Middle East as intended to expand Chinese power and influence at the cost of U.S. power and influence in the Middle East. This may eventually lead to a conflict between the two powers.

Liberals, however, contend that China's increasing role in the Middle East will foster greater interdependence and cooperation between the United States, China, and Middle Eastern states, which would lead to benefits for all sides. Both realism and liberalism recognise the salience of high economic interdependence in determining China's future behaviour, but they fail to offer a dynamic theory that will demonstrate precisely the conditions under which oil interdependence will have a positive or negative impact on Chinese policy towards Saudi Arabia.

Drawing on Trade Expectation's Theory (TET), which departs from the two other approaches by incorporating both the level of interdependence and the dynamic expectations of future trade, and simultaneously considering the levels of interdependence and expectations of future trade, could lead to new predictions. In this regard I will show the conditions under which high energy interdependence between China and the Middle East in general and Saudi Arabia in particular will lead to a pacific or belligerent China. If decision-makers' expectations of future trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future trading environment they will likely take action to protect their interests in the region.

This chapter is organised around four main sections. The first two sections present the realists and liberal perspectives of China's policy towards the Middle East and its relations with Saudi Arabia. The third section shows why I will be guided by theory of trade expectation. The fourth section presents evidence of China's concept of energy security and highlights the situation which will determine if China is guided by political aims or if it is guided merely by economic necessity.

2.2 REALIST INTERPRETATIONS: THE CONFLICT IS INEVITABLE

Realism remains the dominant paradigm of international relations theory. The tenets of realism include the notions that states seek power to survive and major powers dominate the international system, (Zhou, 2008). The realist view of international relations is based on the assumptions that the world is essentially anarchic and has no central authority governing the behaviour of individual states, (Li, 2004: 24). To protect their national security and survival in such a help system, states must seek to acquire or maximise their power through economic and military means, (Ibid). There are two main approaches to the role of power in international relations. The first has been described as “defensive realism” and is characterised by the work of Kenneth Waltz, (Waltz, 1979: 105). Waltz saw the international system as “a self-help system...in which those who do not help themselves, or who do so less effectively than others, will fail to prosper, will lay themselves open to dangers, will suffer”, (Waltz, 1979:118). He claims that nations have a tendency to “balance” the power of other states. If they do not do so, they may suffer the consequences and may be eliminated from the system.

The second approach is “offensive realism” which is also dominant among realists and largely typified by the work of John Mearsheimer, (Mearsheimer, 2001:30). Unlike Waltz, Mearsheimer actually seeks to predict what nations will do when faced by opposing power. They will either “balance” or “buck pass” in response, but they will not generally “bandwagon.” Mearsheimer’s Offensive Realism paradigm is often seen as the theoretical basis for the “China Threat” theory. Offensive realism makes five key assumptions: (a) States are the key actors in world politics, and they operate

in an anarchic system; (b) Great powers invariably have offensive military capability; (c) States can never be certain whether other states have hostile intentions; (d) Great powers place a high premium on survival; and, and (e) States are rational actors who are reasonably effective at designing strategies that maximize their chances of survival, (Mearsheimer, 2001).

Waltz puts the argument as follows: “Actors within a domestic polity have little reason to fear the dependence that goes with specialisation.” The anarchic structure of international politics, however, makes states worry about their vulnerability, thus compelling them “To control what they depend on or to lessen the extent of their dependency.” For Waltz, it is this “simple thought” that explains, among other things, “Their imperial thrusts to widen the scope of their control”, (Waltz, 1979: 106). Meanwhile, Mearsheimer argues that nations that “depend on others for critical economic supplies will fear cut off or blackmail in time of crisis or war.” Historical precedents suggest that it is when the energy security of nations is most precarious and vulnerable that they are most dangerous. Clearly that was true of expansionist Imperial Japan in the days leading up to *Pearl Harbor*. Indeed, Japan’s lack of stable energy supplies was a major factor in its decision to strike on December 7, 1941, (Yergin, 1991). Consequently, Mearsheimer argues that “nations may try to extend political control to the source of supply, giving rise to conflict with the source or with its other customers.” Realists equate interdependence with vulnerability; therefore “Interdependence will probably lead to greater security competition”, (Mearsheimer, 1990: 45). The difference between Waltz and Mearsheimer is that in the eyes of an offensive realist, the international system forces great powers to maximise their

relative power over other nations at every possible opportunity, (Mearsheimer, 2001: 30-31).

In Mearsheimer's view, all great powers have some offensive military capability, which means that they can hurt each other. Moreover, no state can know the future intentions of other states with certainty. The best way to survive in such a system is to be as powerful as possible, relative to potential rivals, (Brzezinski and Mearsheimer, 2005: 46-50). The mightier a state is, the less likely it is that another state will attack it. States that gain regional hegemony have a further aim: to prevent other geographical areas from being dominated by other great powers. In a realist world, states will compete for power regardless of their regime type, and neither international institutions nor global norms will ameliorate this drive for power, (Drezner, 2008: 51-70). In this context, China, whether it remains authoritarian or becomes democratic, is likely to try to dominate Asia the way the U.S. dominates the Western hemisphere, (Mearsheimer, 2001: 35).

Realists believe that status quo powers rarely exist in global politics. They believe that since the international system creates great benefits and incentives for states to look for opportunities to gain power and influence at the expense of their rivals, states are encouraged to take advantage of those situations where the benefits outweigh the costs. By expanding their relative power over their rivals at every opportunity, the survivability and security of that great power is increased. In Mearsheimer's words, "survival mandates aggressive behaviour", (Mearsheimer, 2001: 21). He also believes that a state's ultimate goal is to be the hegemony in a system, (Ibid); however, even if a state cannot achieve hegemony, Mearsheimer believes that states will still act

offensively to gain as much power as possible because states are almost always better off with more rather than less power, (Ibid).

Realists also note that, throughout history, rising powers have tended to be troublemakers, at least insofar as their more established counterparts in the international system are concerned. This is the case, in the realists' view, regardless of regime type; it was as true of a rising, democratic United States as it was of a rising, autocratic Germany, (Friedberg, 2005: 7-45). Historians since Thucydides¹ have pointed to a long string of conflicts generated by the emergence of rising powers that disturb the old order and challenge the existing power structure and predict the same gloomy future for China's rise, (Zakaria, 2007/2008). The realists argue that relative material power establishes the basic parameters of a country's foreign policy; they note, in Thucydides' formula, that "the strong do what they can and the weak suffer what they must", (Strassler, 1996: 89). Look at history, realists say, when a new power rises, it inevitably disturbs the balance of power, unsettles the international order and seeks a place in the sun. This makes it bump up against the established great power of the day (that would be U.S.), so Sino-U.S. conflict is inevitable, (Steinberg, 2009).

Theoretically, China has the raw capacity for becoming a great power, or as former U.S. Secretary of State Condoleezza Rice said: "China is a very important – I used to say emerging power, but I'll say emerged power that can no longer be ignored", (Scott, 2007: 162). Indeed, China has all the requisite elements of power – an

¹ Greek historian, his History of the Peloponnesian War recounts the 5th century BC war between Sparta and Athens to the year 411 BC. Modern realists claim Thucydides as their founding father. See: Lebow, Richard N. (2003). *The tragic vision of politics: ethics, interests and orders*. Cambridge: Cambridge University Press.

extensive industrial base, a strong state, a nuclear-armed military, a continental-sized territory, a permanent seat on the United Nations Security Council, (Pei, 2010), a huge market with a population of over 1.3 billion renders it the most populous nation on earth, accounting for a fifth of the world's population; while its 2.25 million troops form the world's largest armed force, though not the most advanced, (Zinzius, 2004: 5).

From the realists' perspective, China by every measure is a rising power; therefore China's rise has led to several anxieties in the western world. The first is that a rising China will disrupt existing economic and political arrangements. As Stefan Halper argues, China arrives with "the power of a governing idea that will produce rapid growth, stability, security — but not freedom in the public square", (Williamson, 2011). The second is that China's combination of an extremely dynamic economy and an extremely authoritarian political structure constitutes an alternative development model that will be embraced by poor countries and undermine the moral authority of Western concepts (Kroeber, 2008: 29-44). In this context, Wu Xinbo, a professor at Fudan University in Shanghai, argues that in the post-Cold War era, the U.S. model used to be hailed as the only way to economic prosperity. Now, the Chinese model seems to provide an alternative. He went on to say the record of its tiding over two financial crises (the 1998–1999 Asian financial crisis and the 2008–2009 global financial crisis) and securing three decades of a high economic growth rate testifies to its strength. Unlike Washington, Beijing does not like to boast of its model and impose it on others, but the increased appeal of the Chinese experience will certainly enhance Beijing's international status and augment its influence among developing countries, (Wu, 2010: 159).

Indeed, the recent global economic slowdown has also bolstered this narrative of liberal international decline, (Ikenberry, 2011: 56-68). Ever since the U.S. became the world's largest economy, towards the end of the 19th century, the most powerful economy in the world has been a democracy. But, if China remains a one-party state over the next decade, that will change. The confident western slogan that "freedom works" will come under challenge as authoritarianism becomes fashionable, once again, (Rachman, 2011). The third is that other western analysts worry that broadening China-Middle East economic relations could hamper developed economies by sucking away trade opportunities the United States and Europe might otherwise have in the region, (Teslik, 2008). For example, Nobel Prize winner Paul Krugman calculated that China's "mercantilism" is costing America 1.4 million jobs, (Krugman, 2009). The Chinese show many signs of understanding these conditions and have recognised the potential dangers that a rising power can create. China's chief strategist, Zheng Bijian, coined the term "peaceful rise", (Zheng, 2005: 18-24), to describe just such an effort on Beijing's part to enter into the existing order rather than overturn it. Since 2007, and the 17th Communist Party Congress in Beijing, the concept has evolved into one of "peaceful development", largely because many observers outside China found the use of the word 'rise' somewhat ominous, (Brown, 2010: 151). The question is whether this will be sufficient?

Hypothetically, it should be possible for new powers to emerge in a manner that is both peaceful and non-destabilising. The Chinese, wisely, have set the goal of developing peacefully. However, many realists argue this model has not yet been successfully implemented in the modern world. At the same time, accomplishing a

peaceful and non-destabilising rise does not depend simply on the intentions and behaviour patterns of the rising power. If other major powers feel threatened by the rise, or are not prepared to accommodate the interests of the rising power, their reactions could precipitate conflict as easily as the conduct of the emerging country, (Stapleto, 2005). As the emergence of China as a great power in the 21st century seems highly probable, realists warn that a rising China will present the international community with an immense challenge that will not be easy to manage, (Li, 2004: 26).

Historically, the rise of great powers typically has been accompanied by periods of power transition and, except in a few cases, is rarely peaceful. While Beijing has on many occasions sought to reassure the U.S. that its intentions are peaceful, Washington has yet to be convinced and continues to harbour deep concerns, (Yuan, 2009). In this regard, a recent *Pentagon* report stated: “China is developing and fielding large numbers of advanced weapons...she has shared only limited information about the pace, scope, and ultimate aims of its military modernisation programs, raising a number of legitimate questions regarding its long-term intentions”, (QDRR, 2010). Interestingly, the new US defence strategic guidance “Sustaining US Global Leadership: Priorities for 21st Century Defence”, which was released on Jan 5, 2012 emphasizes that the US will continue to strengthen its presence in the Asia Pacific region:

Over the long term, China's emergence as a regional power will have the potential to affect the US economy and our security in a variety of ways. Our two countries have a strong stake in peace and stability in East Asia and an interest in building a cooperative bilateral relationship. However, the growth of China's military power must be accompanied by greater clarity of its strategic intentions in order to avoid causing friction in the region. The United States will continue to make the necessary investments to ensure that we maintain regional access and the ability to operate freely in keeping with our treaty obligations and with international law. Working closely with our network of allies and partners, we will continue to promote a rules-based international order that ensures underlying stability and encourages the peaceful rise of new powers, economic dynamism, and constructive defense cooperation, (defence strategic guidance, 2012:2).

(Table 2.2.1): China’s Current Military Modernisation

Section	Program
Military Budget	China will beef up its military budget by 12.7 percent in 2011, a return to double-digit spending increases that will stir regional unease.
Army	- China is trying to transform the 2.3 million-strong People’s Liberation Army into a smaller, sleeker modern force capable of short, high-intensity conflicts against high-tech adversaries. - Electronic warfare and computer network attack capabilities.
Air Force	- Development of J-20 stealth fighter jet. - Advanced fighter aircraft, and counter space systems. - Developing in-flight refuelling capacity to give its fighters a greater reach, and early warning aircraft.
Navy	- Upgrading its destroyers and frigates. - Launched its first aircraft carrier in 2011. - Building new “Jin-class” ballistic missile submarines, capable of launching nuclear warheads while at sea. - New attack submarines equipped with advanced weapons
Missiles	- Anti-ship ballistic missile program, which could challenge U.S. aircraft carriers in the Pacific. - China successfully tested emerging technology aimed at destroying missiles in mid-air.

Source: Adapted from IISS, Reuters and Quadrennial Defence Review

Another joint report by three leading U.S. think-tanks - the *American Enterprise Institute*, the *Heritage Foundation*, and the *Foreign Policy Initiative* - cast doubts about China’s intentions:

Actions by the People’s Republic of China (PRC) have called into question its previous assertions that its rise to great-power status would be peaceful declaring that its core interests now included some 1.3 million square miles of the South China Sea, dismissing complaints of neighbours as failing to recognise that China is a big country, ignoring North Korean acts of terror, challenging U.S. naval ships on the high seas, creating new confrontations with Japan over disputed islands, slashing its export of rare earth elements, continuing cyber attacks on American defence and commercial entities, or testing a new stealth fighter during the visit of the American secretary of defence, the picture that emerges is of a China that believes it can now throw its considerable economic and military weight around, (Donnelly, 2011).

In the economic realm, thirty years after it embarked on a path of economic reform and opening up to the outside world, China has emerged as a dynamic economic power. China’s newly acquired power and influence have enabled it to expand its presence around the world, looking for resources and establishing economic and

political ties, and any realist expects that China's presence and the influence around the world will increase in the future, as its economy becomes stronger. Nobel Laureate Economist Robert Fogel predicts that China's economy will be an eye-popping 40 percent (123 trillion) of global GDP by 2040, (Larson, 2010); while the historian Paul Kennedy has predicted that by the time the UN celebrates its centenary in 2045, "China could well constitute the largest economic and productive force in the world, bigger even than the United States", (Kennedy, 2006).

Other predictions expect that the Chinese are coming sooner. *Goldman Sachs* predicted that China's GDP would overtake America in 2027, while *Standard Chartered* forecast that it will happen early or by 2020, (The *Economist*, December 16, 2010). *PricewaterhouseCoopers LLP* projections suggest the same outcome that China could be the largest economy in the world as early as 2020 and is likely to be some way ahead of the U.S. by 2030, ((PwC, 2010). *Citigroup* also in a recent report goes in the same direction to predict that China should overtake the U.S. to become the largest economy in the world by 2020, (Buiter, 2011). The *Economist* forecasts that China will get there in 2019, (The *Economist*, 2010). More recent projections by others have calculated significantly earlier dates. In the most extreme estimate Arvind Subramanian of the *Peterson Institute of International Economics*, argues that in PPP terms, China has already overtaken the U.S., (Subramanian, 2011). *The Conference Board* estimates China's GDP, again in PPP terms, could overtake the U.S. in 2012 (The Conference Board Total Economy Database, 2011).

More interestingly, The International Monetary Fund (IMF) has made an optimistic prediction that China will become the world's largest economy in five years in terms

of purchasing power parity (PPP). For the first time, the IMF has set a date for the moment when the “Age of America” will end and the U.S. economy will be overtaken by that of China. According to the latest IMF official forecasts, China’s economy (US\$ 18.6 trillion) will surpass that of America (US\$ 18.2 trillion) by the end of 2015, (based on World Economic Outlook; September 2011).

(Table 2.2.2): The Top 10 Largest Economies in the World (US\$ trillion)

Rank	Country	2010 (IMF)	Country	2015 (IMF)	Country	2020	Country	2030
1	US	14.52	US	17.39	China	23.1	China	57.1
2	China	5.87	China	10.60	US	23.0	US	35.7
3	Japan	5.45	Japan	6.61	Japan	6.7	India	24.8
4	Germany	3.28	Germany	3.87	India	6.4	Japan	9.2
5	France	2.56	India	2.73	Germany	4.5	Brazil	8.7
6	UK	2.25	Brazil	3.165	Brazil	4.2	Russia	7.3
7	Brazil	2.09	France	3.161	Russia	3.8	Indonesia	7.2
8	Italy	2.05	UK	3.05	UK	3.6	Germany	6.4
9	India	1.63	Russia	2.81	France	3.5	UK	5.8
10	Canada	1.57	Italy	2.41	Canada	2.7	France	5.2

Note: GDP is measured in trillion current USD converted at market exchange rates

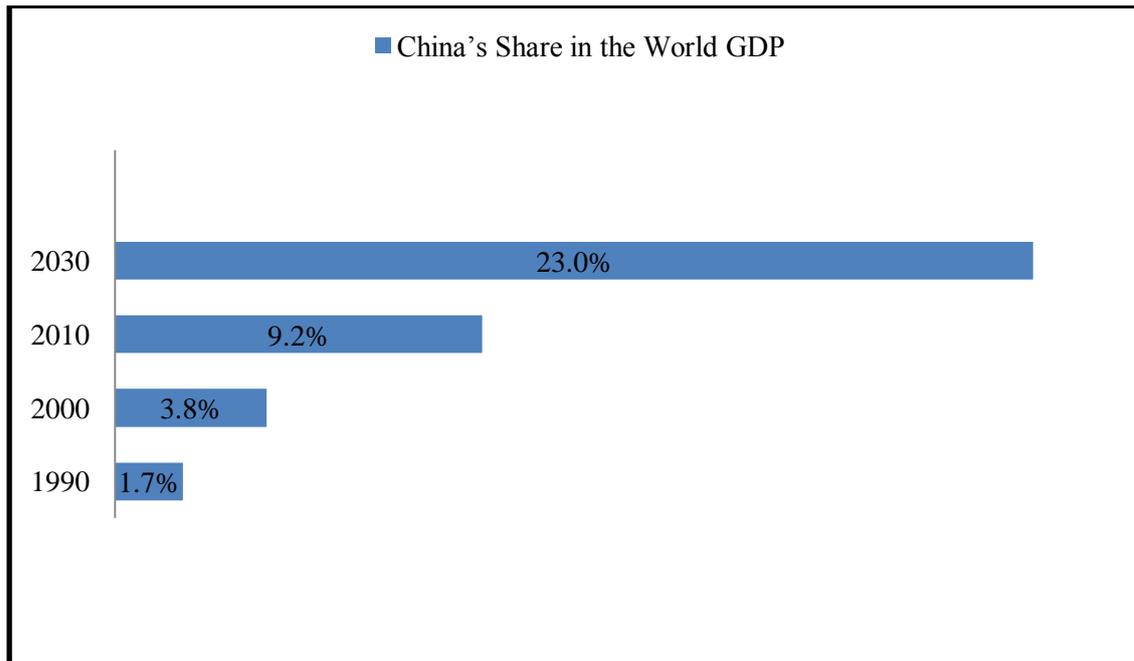
Source: Citibank, (February, 2011) and World Economic Outlook, (September 2011)

From a realist standpoint, a great power’s behaviour is determined not so much by its intentions but by its capabilities. As China’s economy expands, it will use its newfound power to extend its spheres of influence and to defend its economic interests whenever and wherever these interests are challenged, (see Figure 2.2.1 below). In this regard, the U.S. National Military Strategy 2011 document, both in direct references and in implied messages between the lines, amply illustrates that China figures as the prime military threat to the United States.

The United States will remain the foremost economic and military power for the foreseeable future, though national debt poses a significant national security risk. Asia will increase its regional share of global wealth. Though it faces a number of domestic challenges, continuation of China’s decades-long economic growth is expected to facilitate its continued military modernisation and expansion of its interests within and beyond the region... We will

continue to monitor carefully China's military developments and the implications those developments have on the military balance in the Taiwan Strait... We remain concerned about the extent and strategic intent of China's military modernisation, and its assertiveness in space, cyberspace, in the Yellow Sea, East China Sea, and South China Sea, (The US National Military Strategy, 2011: 1-3 & 14).

(Figure 2.2.1): China's Growing Economic Might



Source: adapted from IMF and Citi Investment Research and Analysis

A fast growing economy has made it comparatively easy for China to sustain a large and expanding military effort. Realists believe there are good reasons to expect that China will be able to build and deploy more increasingly capable military systems in the years ahead, (Friedberg, 2005: 7-45). While growing rapidly, China's military spending is still dwarfed by that of the United States, which has about US\$700 billion in outlays of 2010 for national defence, (Wines, 2010). China would remain very clearly in the top 2, the ratio between U.S. and Chinese military spending would decrease from (6.6:1) to (3.2:1), (SIPRI Yearbook, 2010: 203). (See Table 2.2.2)

(Table 2.2.3): The Countries with the Highest Military Expenditure in 2010

Rank	Country	Spending (US\$ billions)	World Share (%)	Change, 2009–2010 (%)	Change, 2001–2010 (%)	Share of GDP (% est.)
1	US	698	42.8	2.8	81.3	4.8
2	China	[119]	[7.3]	3.8	189	[2.1]
3	UK	59.6	3.6	-0.8	21.9	2.7
4	France	59.3	3.8	-8.4	3.3	2.3
5	Russia	[58.7]	[3.6]	-1.4	82.4	[4.0]
6	Japan	54.5	3.3	0.8	-1.7	1.0
7	Saudi Arabia	45.2	2.7	4.0	63.0	10.4
8	Germany	[45.2]	2.7	-1.3	-2.7	[1.3]
9	India	41.3	2.5	-2.8	54.3	2.7
10	Italy	[37.0]	2.2	0.3	-5.8	[1.8]
	World	1630	100	1.3	50.3	2.6

Source: SIPRI, Year book 2010: 203, [] = estimated figure.

(Table 2.2.4): Military Expenditure by U.S. & China, (2001-2010)

	U.S		China	
	Military Expenditure (US\$ billions)	Military Expenditure of GDP (%)	Military Expenditure (US\$ billions)	Military Expenditure of GDP (%)
2010	698,3	4.8	119,4	2.1
2009	668,6	4.7	110,1	2.2
2008	618,9	4.3	92,7	2
2007	576,3	4	84,1	2.1
2006	561,5	3.9	72,9	2
2005	552,9	4	62,1	2
2004	527,8	4	55,2	2.1
2003	484,2	3.8	49,8	2.1
2002	425,4	3.4	45,9	2.2
2001	378,9	3.1	39,5	2.1

Source: SIPRI, various issues

Additionally, a strong economy will provide extra resources to enhance the capabilities of research and development. According to a recent report by the *Royal Society*, Britain's leading academic institution, China is fast becoming a scientific superpower and now ranks second only to the U.S. in its share of published research,

(The Royal Society, 2011: 16). China may surpass the United States as the global leader in scientific output by as early as 2013, thanks to huge investments in research and development (R&D) and education, (Ibid: 17) (see Table 2.2.4).

(Table 2.2.5): Top 5 Countries in Number of Patent (2006-2010)

Applications Filed Worldwide 2006-2010								
Ranking	Country	2006	2007	2008	2009	2010 estimate	2010 percent	2010 growth
1	U.S.	51,280	54,043	51,637	45,618	44,855	27.5%	-1.7%
2	Japan	27,025	27,743	28,760	29,802	32,156	19.7%	7.9%
3	Germany	16,736	17,821	18,855	16,797	17,171	10.5%	2.2%
4	China	3,942	5,455	6,120	7,900	12,337	7.6%	56.2%
5	S. Korea	5,945	7,064	7,899	8,035	9,686	5.9%	20.5%

Source: World Intellectual Property Organization (WIPO – February, 2011)

Looking at China’s capabilities: population and the size of territory, resources, economic strength, military capability, political stability, competence, (Waltz, 1979: 131), and the growing scientific and technological expertise, realists would be content to conclude that China is a rising power and that, as such, it is unlikely to behave differently than have others of its type throughout history, (SIPRI Yearbook, 2010: 203). Realists believe the rise of China, therefore, has tremendous potential to destabilise the current international system. China’s growing economic power will translate into increased military power and allow China to use force to assert its strategic aims. Realists also believe China cannot rise peacefully, and if it continues its dramatic economic growth over the next few decades, the United States and China are likely to engage in an intense security competition with considerable potential for conflict. Richard Bernstein and Ross Munro in their book “*The Coming Conflict with China*” argued that war between China and the United States was a distinct possibility, (Bernstein, 1997). While Peter Navarro envisaged the same scenario in

his book “*The coming China wars: where they will be fought and how they can be won*” which point out that oil will be the source of conflict between China and the United States, (Navarro, 2007).

Not to mention Robert Kaplan’s alarmist 2005 essay: “*How We Would Fight China*” in which he contended that whether or not there will be a Sino-American war is no longer a question, the only question, he wrote, is how the United States should fight China, (Kaplan, 2007). Moreover, after observing China’s growing assertiveness in foreign policy and purported attempts to undermine the current liberal world order, Elizabeth Economy wrote in *Foreign Affairs* that “China is transforming the world as it transforms itself. Never mind notions of a responsible stakeholder; China has become a revolutionary power”, (Economy, 2010: 142-153). Even Robert Gates, the mild-mannered then U.S. defence secretary, warned in 2009 that China’s military modernisation “could threaten America’s primary means of projecting power and helping allies in the Pacific: our bases, air and sea assets, and the networks that support them, (Thompson, 2010). Additionally, Henry Kissinger, who is against the containment policy towards China, has also argued that competition for oil will be the driving source of international conflict in the near future, (Caroline, 2005). While Patrick Seale, the leading British writer and expert on the Middle East, expects China to deploy military forces and bases in the Middle East in the coming decade as part of an effort to protect its access to valuable resources like oil, (Seale, 2010).

Against this strategic background, realists correctly recognise the security dilemma that states possess in a self-help system; but they fail to take into account that gains from trade can provide incentives for peace. China wants stability in the Middle East

to ensure the flow of oil; that is why China works within the existing institutions to secure a steady access to energy resources at reasonable prices. China's recent behaviour inside the Security Council regarding issues such as Iran's sanctions, political crisis in Yemen and the unrest in Bahrain show that trend clearly.

Contrary to realists' claim of China's potential hegemony, Saudi Arabia is eager to diversify its economy and foreign policy, subsequently, not only does Saudi Arabia (the government and the public) strongly welcome the Chinese involvement and investments, but also views such presence as vital toward the creation of balance in international relations and energy markets. The realist approach also tacitly assumes a level of coercion in the Sino-Saudi relations. However, in examining the relationship between the two sides, one would find that Saudi Arabia is much more eager to engage China economically and politically than China itself, (Olimat, 2010). From the Saudi perspective, there is little concern that China's increasing status as a world power will constitute a security threat. They don't see China as threatening to their national sovereignty, territorial integrity, or exploitative of their national wealth in the same manner they view the West. Hegemony, domination, and imperialism are not associated with China but with the West, (Ibid). Additionally, and in contrary to realists' claims, the United States exploited China-Saudi relations to pressure Iran. Cables, obtained by *WikiLeaks*, lay out how U.S. diplomats worked with Saudi Arabia and other big Middle Eastern oil suppliers to persuade Beijing to back tougher sanctions on Iran, (Lee, 2011).

In this context, the theory failed to provide a practical framework to explain convincingly how good relations between China and Saudi Arabia will result in a

conflict with the United States. Indeed, as the oil is a global commodity, Saudi Arabia, along with the other oil producing countries, has an economy that depends entirely on oil's exports so it is unlikely there would be support for any conflict with China in the region as long as China continues its current rational policy. Additionally, some realists make a wrong comparison between China's behaviour in East Asia and Beijing's new role in the Middle East. In East Asia, the "rise" of China may raise concerns among countries such as Japan, India, S. Korea, Philippines and Thailand, but the situation in the Middle East is completely different as the countries of the region welcome a stronger Chinese role. For example, the latest Japan's defence white paper states that: "China is expanding and increasing its activities in waters close to Japan. The lack of transparency of its national defence policies, and the military activities are a matter of concern for the region and the international community, including Japan, and need to be carefully analyzed", (Japan's Ministry of Defence white paper, 2011). In contrast, the Arab states always urge China to step up its involvement in the Middle East.

Finally, realists contend that interdependence, will probably lead to greater security competition. Currently there is no evidence to support this assumption, but on the contrary there are many indications of U.S. – Sino cooperation from Sudan to Iraq and more importantly both countries view Saudi Arabia's stability as a vital interest.

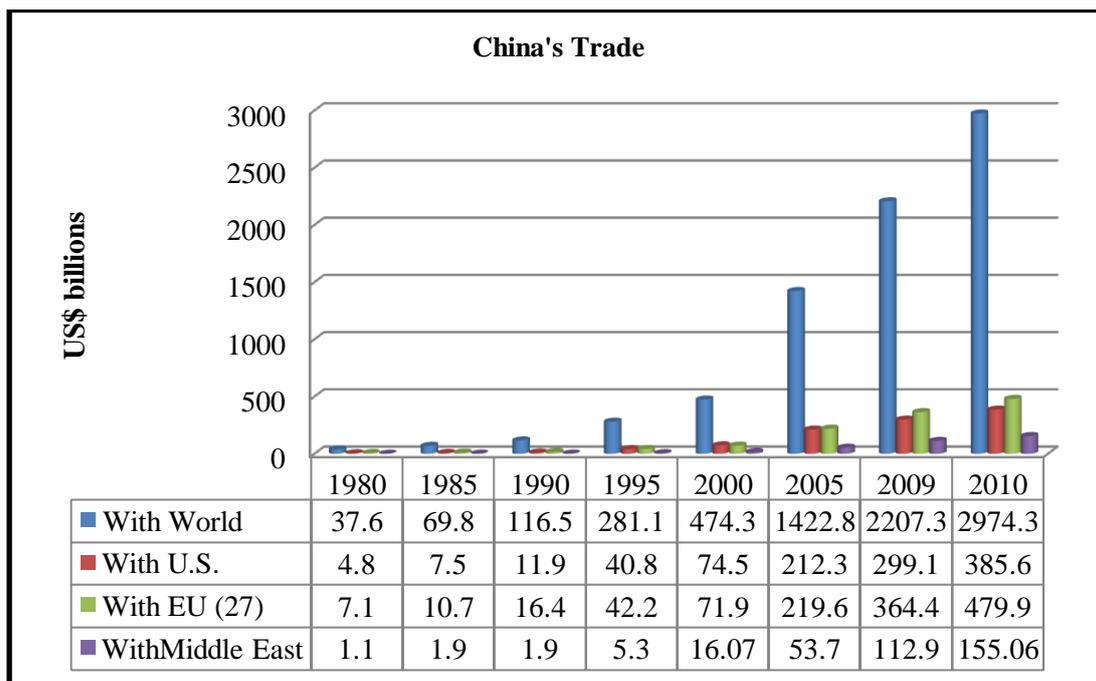
2.3 LIBERAL THEORY: INTERDEPENDENCE WILL LEAD TO STABILITY

Liberal scholars have long contended that economic interdependence can be a powerful source of peace. Liberal theory suggests that economic and social forces will eventually precipitate political change as well. Liberals advocate a policy of economic engagement in regard to China. By increasing trade and tying China's economy more tightly to that of the world, China will hesitate to initiate conflict for fear of the economic repercussions. The deepening of economic ties with the United States and the Middle East will in turn foster political developments, (Friedman, 1999: 155). Liberals' logic even influenced some of U.S. presidents. Bill Clinton proclaimed in 1994 that "The best strategy to ensure our security and to build a durable peace is to support the advance of democracy elsewhere. Democracies don't attack each other. They make better trading partners and partners in diplomacy", (Clinton, 1994). While in 1999, two years before China's accession to the World Trade Organization, former U.S. President George W. Bush (junior) argued that "Economic freedom creates habits of liberty. And habits of liberty create expectations of democracy.... Trade freely with China and time is on our side", (Rachman, 2011).

One of the liberals' major arguments regarding trade is that increased economic interdependence decreases the probability of war, (Madison, 1981: 113). This belief, mainly held by liberals, owes its intellectual origins to Immanuel Kant, who believed that free and fair trade between nations provides incentives to develop and maintain cooperative and mutually profitable relationships, (Ibid). In other words, the more two countries are engaged in bilateral trade, the less they are likely to go to war, (Russett

and Oneal, 2001: 145). Interdependence between two countries influence their political behaviour in two ways: (a) because both countries are dependent on each other, they have an economic interest in continuing peaceful exchanges, and (b) the interdependence between the two countries provides a medium of communication that can be useful in preventing or resolving disagreements short of armed conflict, (Mansfield, 2001: 139). In this context, liberals argue that interdependent states would rather trade than invade, (Copeland, 1996: 5-41), or as Fareed Zakaria, a former editor of *Newsweek International*, puts it “A new world war is highly unlikely. Nuclear deterrence, economic interdependence and globalization all militate against it.” However, he suggests that we will see instead a “Soft War, a quiet competition for power and influence across the globe. China and the U.S. will be friends one day, rivals another, cooperate in one area, compete in another”, (Zakaria, 2005) (see Figure 2.3.1 & Table 2.3.1 below).

(Figure 2.3.1): China’s Trade with the World (selected economies and years)



Source: IMF (DOTS, July, 2011)

Integration into global markets has been a central component of China's economic development strategy. Since the late 1970s, China has transformed itself into a major trading power. China has also become one of the world's leading destinations for foreign direct investment (FDI), and in recent years China's outward FDI has also increased rapidly, (see Table 2.3.1). China is now one of the world's largest foreign investment destinations. More than 470 of the top 500 global companies have established their presence in China. By July 2010, China had received 1.05 trillion U.S. dollars of foreign investment in cumulative terms, ranking the first among developing countries for 18 years in a row, (Xinhua, September 13, 2010).

From the liberals' perspective China is indeed a "responsible stakeholder" as a recent study conducted by IEA showed that the available evidence suggested that much of Chinese equity oil abroad was sold to local or international markets instead, (Jiang & Sinton, 2011: 17). The study also concluded that there is no evidence to suggest that the Chinese Government currently imposes a quota on the NOCs regarding the amount of their equity oil that they must ship to China. Decisions about the marketing of equity oil, where the Chinese companies have control over the disposition of its share of production, appear to be dominated by market considerations, (Ibid: 18). Additionally, a closer look at the China model makes it clear that it is not so easily replicated. Most developing countries do not have China's bureaucratic depth and tradition, nor do they have the ability to mobilise resources and control personnel in the way that China's party structure allows, (Ibid).

(Table 2.3.1): China's Inward and Outward FDI Flows, (1990-2010, US\$ billions)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
FDI Inward (\$bn)	40,7	46,8	52,7	53,5	60,6	72,4	72,7	83,5	108,3	95,0	105,7
(%) World's Total	2.9%	5.6%	8.3%	9.4%	8.2%	7.3%	4.9%	3.9%	6.1%	8.5%	9.4%
FDI Outward (\$bn)	0,91	6,8	2,5	2,8	5,4	12,2	21,1	22,4	52,1	56,5	68,0
(%) World's Total	0,7%	0,9%	0,4%	0,5%	0,5%	1,3%	1,5%	0,9%	2,7%	4,3%	5,0%

Source: UNCTAD; World Investment Report, various issues

China is currently a major trading partner of most of the world's biggest economies. China has not only increased its relative share in world trade but also its rank as a top trading partner of major economies. A decade ago, China was the fifth largest trading partner of the United States, fourteenth largest trading partner of the European Union, third largest trading partner of Japan, and eighth largest trading partner of oil-exporting countries in the Middle East and North Africa. China is currently the second largest trading partner of the United States, eighth largest trading partner of the European Union, and the largest trading partner of Japan and the Middle East and North Africa, (ESCAP, 2011: 11). Mark Crosby from the Melbourne Business School believes that the rise of China in the new global economic order has made for a more prosperous and stable world, (University of Melbourne, 2009). Currently China conducts around 10 percent of world trade and produces around 10 percent of global GDP, (UNComtrade, 2011). Over the ten years to 2010, China's exports grew by an annual average of 23 percent in dollar terms, more than twice as fast as world trade, (Ibid). If it continued to expand at this pace, China might grab around one-quarter of world exports within the next decade, (The *Economist*, January 7, 2010).

(Table 2.3.2): World Merchandise Imports/Exports by Region

Selected Periods and Economy,(billion dollars and percentage)									
	1948	1953	1963	1973	1983	1993	2003	2009	2010
Exports									
World (US\$ billions)	59	84	157	579	1838	3676	7376	12178	14851
U.S. (%)	21.7	18.8	14.9	12.3	11.2	12.6	9.8	8.7	8.6
China (%)	0.9	1.2	1.3	1.0	1.2	2.5	5.9	9.9	10.6
Middle East (%)	1.9	2.7	3.2	4.1	6.8	3.5	4.1	5.7	6.0
Imports									
World (US\$ billions)	62	85	164	594	1882	3786	7689	12421	15077
U.S. (%)	13.0	13.9	11.4	12.3	14.3	15.9	16.9	12.9	13.1
China (%)	0.6	1.6	0.9	0.9	1.1	2.7	5.4	8.1	9.3
Middle East (%)	1.7	2.0	2.2	2.6	6.2	3.3	2.7	4.0	3.7

Source: WTO, (International Trade Statistics 2011)

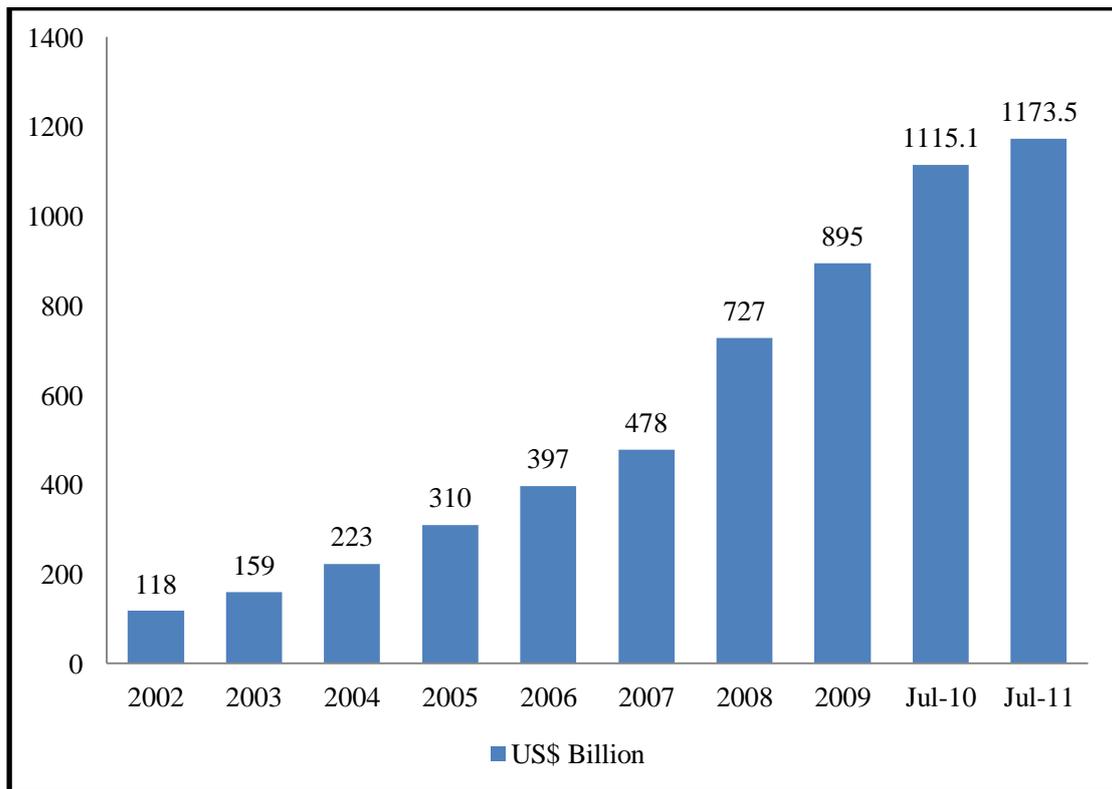
For these reasons liberals argue, in geopolitical terms, China may be a rival, but in economic terms it's one of the U.S.'s most important partners. China tops the world as a target of foreign direct investment (FDI). China holds more in U.S. Treasury bills than any other country, and China has become an active purchaser of overseas resources, (Wang & others, 2011: 413-431).

(Table 2.3.3): China's Holdings of U.S. Treasury Securities: 2002-2010

(US\$ Billions and as a percent of total foreign holdings)									
	2002	2003	2004	2005	2006	2007	2008	2009	2010
China's Holdings (US\$ billions)	118.0	159.0	222.9	310.0	396.9	477.6	727.4	894.8	1,160.1
China's Holdings of Total Foreign Holdings (%)	9.6%	10.4%	12.1%	15.2%	18.9%	20.3%	23.6%	24.2%	26.1%

Source: U.S. Treasury Department, year-end data.

(Figure 2.3.2): China's Holdings of U.S. Treasury Securities, (2002-2010)



Source: U.S. Department of the Treasury (September 2011)

The country is also a favourite investment area for American companies and consumers reap enormous benefits from the low prices of Chinese goods. Additionally, liberals argue that China's economy is creating hundreds and thousands of jobs in the U.S. and millions of jobs around the world. According to some estimates, since China joined the (WTO) in 2001, it had created in less than a decade more than 16 million jobs around the world. Most important of all, China is not just an export machine, its ratio of imports to GDP (which peaked at 32 percent in 2005) was in 2010 about 24.2 percent almost twice that of U.S., (based on UN Comtrade database, 2011).

(Table 2.3.4): Jobs Dependent on Exports to China (2001-2009)

Country	Exports to China (2001-2009, annual average in US\$ billions)	Jobs (million)
Philippines	11.7	3.46
Thailand	15.1	2.91
South Korea	71.4	2.08
Taiwan	70.2	2.00
Malaysia	20.5	1.44
Japan	99.6	1.41
Russia	15.1	1.20
U.S.	52.1	0.59
Germany	34.5	0.49
KSA	13.2	0.31
Brazil	13.2	0.27
Australia	18.5	0.26
Singapore	14.4	0.26
Total	449.2	16.00

Source: CEIC; IMF, National statistics and the Economist

From the start of China's reform in 1978 to the end of the twentieth century, the value of the trade moving between the China and America grew from one billion dollar, (Friedberg, 2005), to about 450 billion dollar in 2010, (see Table 2.3.3). In addition, the Americans are active investors in the foreign invested sector, whose share of China's output is around 15-20 percent, but which dominates the export sector, accounting for nearly 60 percent of all exports and 90 percent of exports designated "high tech" by China. Foreign enterprises are also crucial conduits for the import of new technology, management expertise and ideas, (Kroeber, 2008). For example China high-tech exports reached US\$377 billion, about 31 percent of China's total exports in 2009; about 82 percent was processed/assembled high-tech products, mainly made of imported parts and components from industrialised economies, such as Germany, Japan, Korea, Taiwan and the U.S. China contributed very little intellectual properties to these assembled high-tech products, (Li, 2011) (see Table 2.3.3).

(Table 2.3.5): Foreign Direct Investment in China (2000-2009)

	2000	01	02	03	04	05	06	07	08	09	2010
Total Non – Financial Foreign Direct Investment in China											
Number of Projects	22,3	26,1	34,1	41,0	43,6	44,0	41,4	37,8	27,5	23,4	27,4
Growth (%)	32.1	17.0	30.7	20.2	6.3	0.8	-5.7	-8.7	-27.3	-14.8	16.9
Utilized FDI (US\$ billions)	40.7	52.7	53.5	60.6	60.3	69.5	67.1	74.8	92.4	90.0	105.7
Total US Direct Investment in China											
Number of Projects	2,60	2,59	3,36	4,06	3,92	3,74	3,20	2,62	1,77	NA	NA
Utilized FDI (US\$ billions)	4.4	4.9	5.4	4.2	3.9	3.1	3.0	2.6	2.9	NA	NA
US Share of Utilized Investment (%)	10.8	10.4	10.2	7.9	6.5	5.1	4.1	3.5	3.2	NA	NA

Sources: The US-China Business Council and China's Ministry of Commerce (MOFCOM)

U.S.-China trade rose rapidly after the two countries re-established diplomatic relations in January 1979. In 1979 (when China's reforms began), total U.S.-China trade (exports plus imports) was US\$2 billion; China ranked as the 23rd-largest U.S. export market and its 45th-largest source of U.S. imports. In 2010, bilateral merchandise trade was US\$457 billion; China was the second-largest U.S. trading partner (after Canada), the third-largest U.S. export market (after Canada and Mexico), and the largest source of U.S. imports, (Morrison, 2011). The trade between China and the United States has increased about 400 percent between 2000 and 2010. Chinese Premier Wen Jiabao noted that "The two countries have become increasingly interdependent", (Xinhua, September 23, 2010).

(Table 2.3.6): China's Trade with the United States (US\$ billions 1980-2010)

	1980	1985	1990	1995	2000	2005	2006	2007	2008	2009	2010
US Export	3.8	3.9	4.8	11.7	16.3	41.8	55.2	65.2	71.5	69.6	91.9
US Imports	1.1	3.9	15.2	45.6	100.1	243.5	287.8	321.5	337.8	296.4	364.9
Total Trade	4.9	7.8	20.0	57.3	116.4	285.3	343	386.7	409.2	366.0	456.8
US balance	2.7	0.0	-10.4	-33.8	-83.8	-201.6	-232.5	-256.3	-266.3	-226.8	-273.1

Sources: U.S. International Trade Commission DataWeb.

In addition to their faith in trade as an instrument of peace, liberal optimists place great store in the role of international institutions of various kinds. Today, China is a member of 52 intergovernmental institutions, (Union of International Associations, 2009), is an active participant in many, has signed over 270 international treaties and enshrined a significant body of international law in its domestic legal code, (Kent, 2007: 60). Furthermore, people-to-people and cultural exchanges are very important in fostering closer U.S.-China bilateral relations. More than 100,000 Chinese are now studying in the United States, and the U.S. side will receive more Chinese students and facilitate visa issuance for them. The United States has approximately 20,000 students in China. The United States seeks to encourage more Americans to study in China by launching a new initiative to send 100,000 students to China over the coming four years, (U.S.-China Joint Statement, 2009).

China and the U.S. have important common interests, (fighting terrorism, dealing with proliferation, coping with environmental degradation, and addressing public health crises). These issues provide strong incentives for both Beijing and Washington to work hard to manage and contain bilateral conflict, (Goldstein, 2005). Furthermore, John Ikenberry argues that China has become more prosperous and capable by

operating inside the existing international order. Their economic success and growing influence are tied to the liberal internationalist organisation of world politics including the World Trade Organization (WTO) and the newly organised G-20, and they have deep interests in preserving that system, (Ikenberry, 2011). Liberals believe that, through cooperation and dialogue, China and the U.S. can advance their common interest in securing access to sustainable energy resources at fair prices while avoiding costly and dangerous competition over scarce oil resources. James Reilly suggests three key steps: first, support for energy efficiency and environmental protection in China; second engage China in multilateral energy institutions, (particularly the International Energy Agency); and finally improve energy efficiency and conservation in the U.S. (Reilly, 2007). Additionally, China could be drawn further into the liberal order through its desire to have its currency the renminbi (yuan) become an international currency rivalling the US dollar. According to a recent World Bank report, “the most likely scenario for the international monetary system is a multicurrency system centred on the US dollar, the euro, and the renminbi. Under that scenario, the dollar would lose its position as the unquestioned principal international currency by 2025, making way for an expanded international role for the euro and a burgeoning international role for the renminbi”, (The World Bank, 2011: 125-126).

Above all else, liberals always argued that democracy is a force for peace, (Friedberg, 2005). Liberals believe that, although it is still far from finished, the process of democratisation is already well under way in China. This process is being driven largely by economic development, which, in turn, is being accelerated by China’s increasing openness to trade. Rising per capita incomes are creating a growing Chinese middle class, (Ibid). They argue that, as China develops further, the pressure

to change illiberal systems such as state-run media will continue to grow. Indeed, a new and authoritative research shows that China and other emerging markets are likely to become more democratic as they get richer. A paper from the Federal Reserve Bank of San Francisco, titled *Re-establishing the Income-Democracy Nexus*, used broader historical data to overturn previous studies that questioned the link between democracy and wealth, (Benhabib & others, 2011). According to estimates from the Chinese Academy of Social Sciences, half of the city dwellers in China will be part of the middle class by 2023. Based on data from 2000 to 2009, researchers calculated that 37 percent of city dwellers were part of the middle class in 2010, (Chen, 2011).

China has so far remained resistant to political change. In the short term, there is little likelihood of significant political reforms between 2011 and 2015, as China's rulers will concentrate on maintaining stability during the transition to a younger generation of political leaders in 2012-13, (EIU, 2011: 3), but the democratisation of China is critical in the long run. Indeed, there is little evidence that authoritarian states can become truly advanced societies without moving in a liberal democratic direction. As the economist Amartya Sen has noted, "While democracy is not yet universally practiced, nor indeed universally accepted, in the general climate of world opinion democratic governance has achieved the status of being taken to be generally right", (Ikenberry, 2011). Li Rui, an outspoken liberal who is a Chinese Communist Party (CCP) member and former secretary to Mao Zedong, argues strongly that Chinese and foreign histories prove that autocracy is the source of political turmoil. As the collapse of the Soviet Union shows, the root cause is autocracy, (Pei, 2006). Modernisation is possible only through democratisation. This is the trend of the world in the twentieth

century, especially since the Second World War. Those who follow this trend will thrive; those who fight against this trend will perish. This rule applies to every country — and every party, (Ibid).

More broadly, Zbigniew Brzezinski emphasises that China is determined to sustain its economic growth. He argues confrontational foreign policy could disrupt that growth, harm hundreds of millions of Chinese, and threaten the Communist Party's hold on power. China's leadership appears rational, calculating, and conscious not only of China's rise but also of its continued weakness, (Brzezinski and Mearsheimer, 2005). He goes further to argue: to have a real collision, China needs a military that is capable of going toe-to-toe with the United States. At the strategic level, China maintains a posture of minimum deterrence. In a conflict, Chinese maritime trade would stop entirely. The flow of oil would cease, and the Chinese economy would be paralysed, (Ibid).

Robert Rollick agrees that the overwhelming priority of China's senior officials is to develop and modernise a China that still faces enormous internal challenges. He goes on to say, "While proud of their accomplishments, China's leaders recognise their country's perceived weaknesses, its rural poverty, and the challenges of political and social change. Two-thirds of China's population, nearly 900 million people, live in poor rural areas, living mostly as subsistence farmers, and 200 million Chinese live on less than a dollar a day. In China, economic growth is seen as an internal imperative, not as a challenge to the United States", (Rollick, 2005). While Zheng Yongnian, the Director of East Asian Institute, National University of Singapore, goes further to say that China's economic growth came with a huge price: "Environmental degradation,

resource wastage, ethnic tensions, widening income disparity, polarisation and rampant corruption”, (Xinhua, 2010). Furthermore Dominic Barton, the global Managing Director of the consulting firm McKinsey, argues that “The leadership in China is always worried about how do you stay ahead of the growth to create enough jobs...They have to create over 30 million jobs a year. They know that. That is why there’s such an obsession with the GDP numbers there”, (Freeland, 2011).

Nye states that China has a long way to go to equal the power resources of the United States, and it still faces many obstacles to its development, (Nye, 2010: 2-12). Like Japan, China is becoming an ageing society, the share of the population 60 years and above will be 17 percent by 2020, and this ageing will increase healthcare and pension costs while reducing savings and investments. China’s future growth also lies in the country’s export-led growth model. China has relied on exports to increase its growth, while this strategy has served China well for the past two decades, its future viability is now deeply in doubt, (Pei, 2010). China’s rise to superpower status will also be constrained by a host of political factors. First and foremost, at the moment, China is economically prosperous but ideologically bankrupt. Nye argues that the ideology of communism is long gone, and the legitimacy of the ruling party depends upon economic growth and ethnic Han nationalism. The Chinese political system lacks legitimacy, suffers from a high level of corruption, and is vulnerable to political unrest should the economy falter, (Nye, 2010: 143-153). Secondly, risks of internal fragmentation, on top of the perennial Taiwan problem, will mean structural weakness makes China less able to project power abroad and more vulnerable to the machinations of its competitors, who could exploit China’s ethnic tensions to tie Beijing’s hands. Geopolitically, the limits on Chinese power will be equally severe;

China has to contend with strong regional rivals - India, Japan, and Russia. China's rise has already triggered a regional geopolitical realignment aimed at checking Beijing's ambitions and reach, (Ibid).

As far as China's military capability is concerned, liberal scholars agree that it's exaggerated by the "China threat" school. Despite China's determination to achieve military modernisation, its defence budget is relatively small compared with that of the United States and at the moment (even in the next few decades) the U.S. is the dominant military power in the Middle East. According to Andrew Shearer, Director of Studies at Australia's Lowy Institute for International Policy: "China has naval aspirations but they're still a long way from realising that", (Critchlow, 2011). Furthermore, Feng Zhu, the Deputy Director of the Center for International & Strategic Studies (CISS) at Peking University, argues that: "China's navy modernisation is impressive. But its naval capability, in the foreseeable future, remains a 'disruptive' military technology, rather than comparably 'rivalling' military force... No one will actually believe that China's navy will be able to carry out deadly long distance strikes merely by the virtue of numbers of submarines and destroyers", (Feng, 2010).

In this regard, some argue it's the other way round and that it is China who should worry of an "American threat" in the region (Li, 2004: 34). The *Economist* recently quoted a retired Chinese admiral who compared the American navy to a man with a criminal record "wandering just outside the gate of a family home", (The *Economist*, March 14, 2009). While Mearsheimer noted that America has been at war for 14 of the 21 years since the Cold War ended and is preparing for a war against Iran. That is

two out of every three years, (Mearsheimer, 2010: 381-396). Ivan Eland goes further to say that: “The American national-security establishment knows that a threatening nation-state needs to be found to justify future generations of complex U.S. weapon systems. The national-security establishment and conservative hawks must identify a substantial “threat” to the nation and must make that threat seem imminent. Indeed, they have already done so in a rising China”, (Eland, 2006).

Even Kissinger, who is not within the liberal camp, goes further to say China’s emerging role is often compared to that of imperial Germany at the beginning of the 20th century, the implication being that a strategic confrontation is inevitable and that the United States had best prepare for it. “That assumption is as dangerous as it is wrong...it is unwise to substitute China for the Soviet Union in our thinking and to apply to it the policy of military containment of the Cold War...only the reckless could make such calculations in a globalized world of nuclear weapons”, (Kissinger, 2005). He goes further to say, “There is no doubt that China is increasing its military forces...But even at its highest estimate, the Chinese military budget is less than 20 percent of America’s”, (Ibid). Additionally, Eland argues that the Chinese defence spending is being eaten up by that conversion and by the need to pay higher salaries to soldiers who might have better opportunities in the rapidly growing private sector. Thus, China’s investment in new military equipment as a percentage of its total defence expenditures is actually fairly low when measured against that of comparable countries, (Eland, 2006).

Liberals believe strongly that the policy designed to contain China and prevent its rise would be exceedingly difficult to implement and would eventually fail. Unlike the

U.S. effort to contain the former Soviet Union, an attempt to contain China would find little support from the countries whose support is essential for such a strategy to succeed. On the contrary, with a few exceptions, such an approach would most likely aggravate relations with many American allies and partners around the world, (Goldstein, 2005). In the liberals' view, the United States cannot thwart China's rise, but it can help ensure that China's power is exercised within the rules and institutions that the U.S. and its partners have crafted over the last century, rules and institutions that can protect the interests of all states in the more crowded world of the future, (John, 2008: 23-37).

Yet, despite liberals' "convincing" arguments, they are less explicit on the exact causal mechanism that prevents conflict. Liberals also provide no explanation regarding how states determine the costs of conflict versus the benefits of trade. Liberals fail to develop a consistent and complete causal logic of when trade makes the difference between conflict and peace. Liberals may be correct that trade can cause citizens within a specific country to seek alternatives to war in order to avoid disrupting of trade; but they fail to acknowledge the other side of the coin. Individuals within a country are just as likely to put pressure on a country to go to war when they believe they are not obtaining enough wealth because other states are preventing gains from trade. Thus, while liberals are correct to identify how gains of trade can provide incentives to forgo war, the failure to develop an exact causal mechanism that explores how states determine when the benefits of trade outweigh the costs of war makes most liberal arguments regarding the influence of trade incomplete.

2.4 Constructivism Approaches: Impact of Ideas vs. Material Factors

Constructivism offers alternative understandings of a number of the central themes in international relations theory including the meaning of anarchy and balance of power, the relationship between state identity and interest, an elaboration of power, and the prospects for change in world politics, (Hop, 1998:171-200). Constructivism aspires to describe itself as a “middle ground” position. Nicholas Onuf introduced the actual label of constructivism to IR in 1989. Alexander Wendt has followed with influential articles and a book in the 1990’s, (Uzgören, 2007). Constructivism holds that international politics are not merely influenced by state interaction, trade relations, or military power, but also by the identity, the beliefs and norms of the political elites who direct state policies. Whereas realism and liberalism tend to focus on material factors such as power and trade, constructivist approaches emphasize the impact of ideas, (Walt, 1998: 38). In short, constructivism challenges the material and rational assumptions of the mainstream IR theories and attempts to address neglected issues, (Price & Tannenwald, 1996).

According to constructivists, the international system “is a set of ideas, a body of thought, a system of norms, which has been arranged by certain people at a particular time and place”, (Jackson & Sorenson, 2006). In this regard, three elements make constructivism a distinct form of international relations theorizing. Firstly, global politics is said to be guided by the inter-subjectively shared ideas, norms, and values held by actors. Secondly, the ideational structure has a constitutive and not just regulative effect on actors. Thirdly, ideational structures and actors (“agents”) co-constitute and co-deter-mine each other. Structures constitute actors in terms of their

interests and identities, but structures are also produced, reproduced, and altered by the discursive practices of agents, (Copeland, 2000: 187-212). Constructivist theory rejects the basic assumption of neo-realist theory that the state of anarchy (lack of a higher authority or government) is a structural condition inherent in the system of states, (Wendt, 1992: 391-426). Rather, it argues, in Alexander Wendt's words, that "anarchy is what states make of it". That is, anarchy is a condition of the system of states because states in some sense "choose" to make it so, (Ibid). Thus, constructivist theory holds that it is possible to change the anarchic nature of the system of states, (Ibid).

The main limitation of this theory is that it is better at describing the past than anticipating the future. Thus the theory is not equipped to explain China-Saudi relations for several reasons. Firstly, the relations between China and Saudi Arabia are contemporary with very little historical interaction and yet it is important to anticipate the future scenarios for this relationship. Secondly, the relationship is between two states that are external to each other's regions. The only thing that ties them in terms of identity is the Islamic question, and so that as long as this does not get out of control there will not really be an identity issue to mar the convergence of pragmatic interests. Thirdly, the development of ties at present are based on material factors and interests (i.e. trade and oil) and do not require close convergence of values. Finally and most important of all, policy-makers decisions are driven by the convergence of pragmatic concerns, or as Herman puts it: "material circumstances ... affect the intellectual evolution and policy choices of political decision markers is not in dispute", (Herman, 1996:276). There may be some research programme to be developed in the future about the normative similarities and differences between East

Asian states and Arab states but this is not a highly significant factor at present in the development of the China-Saudi partnership.

2.5 TRADE EXPECTATION THEORY (TET)

Realism and liberalism both recognise the salience of high economic interdependence in determining China's future behaviour, but they fail to offer a dynamic theory that will demonstrate precisely the conditions under which economic interdependence will have a positive or negative impact on Chinese policy towards Saudi Arabia.

(Table 2.5.1): The Competing Theories

	Core Liberal Theory (e.g., Rosecrance)	Core Realist Theory (e.g., Waltz, Mearsheimer)	Trade Expectations Theory (Copeland)
Nature of the System	Anarchy	Anarchy	Anarchy
Nature of the State	Generally rational, unitary calculator of costs/benefits, but may also have aggressive, unit-level drives	Rational, unitary actor seeking to reduce vulnerability to improve security	Rational
Analytical Focus	The individual state's concern for its own dependence	The state's concern for its own dependence	The state's concern for its own dependence
State's Decision for War or Peace Driven by	Benefits of trade (the "gains from trade" from specialization)	Costs of several trade (the costs of adjustment after being cut off, due to specialization)	Benefits of trade and costs of several trades, plus expectations of future trade
Ultimate Reason that State goes to War	If level of dependence low (i.e., trade is low), "restraint" on unit-level aggressive tendencies removed	High dependence creates a systemic incentive to use force to overcome vulnerability	High dependence and pessimistic expectations for future trade, creating a low or negative expected value for trade
Reason for State Choosing to Stay at Peace	If level of dependence high (i.e., trade is high), then high dependence "restrains" by making benefits of trade greater than value of war	Low dependence removes another systemic incentive for war	High dependence and optimistic expectations for future trade, creating a high expected value for trade

Source: Copeland, Economic Interdependence and War: A Theory of Trade Expectations

This dynamic feature of TET allows it to avoid the pitfalls of both liberalism and realism by being able to explain variance in state behaviour over time. Trade expectations theory introduces a new causal variable, the expectations of future trade, (Copeland, 1996). High interdependence can be either peace-inducing or conflict-inducing, depending on the expectations of future trade. This dynamic perspective helps bridge the gaps within and between current approaches, (Ibid).

This brings up the second casual variable of (TET) - expectations of future trade (EFT). This variable will enable us to predict that the lower the expectations of future trade, the lower the expected value of trade, and therefore the more likely it is that conflict will be chosen. In this context I will show the conditions under which high energy interdependence between China and the Middle East in general and Saudi Arabia in particular will lead to a pacific or belligerent China. If decision-makers' expectations of future trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future trading environment they will likely take action to protect their interests in the region.

2.6 CHINA'S RESPONSE TO WESTREN THEORIES

2.6.1 Peaceful Development vs. China Threat

The People's Republic of China, following its founding in 1949, has endorsed and practiced a consistent policy of peaceful diplomacy. New China cherished its independence, actively sought peaceful coexistence with other countries around the world and worked hard to improve its external environment, particularly in its

surrounding areas, (Jiabo, 2004). In the 1950s, Zhou Enlai played a crucial role in formulating the well-known “Five Principles of Peaceful Coexistence”; in the early 1980s, Deng Xiaoping proposed to implement “independent and peace-oriented diplomacy”; and since the turn of the century, the Chinese leadership has pledged to take a “path of peaceful development”, characterized by good neighbourhood relationships, (Ronghua, 2006). Later on, after China joined the WTO and after rapidly becoming integrated to the international system and the world market, China’s President Hu Jintao articulated the, “Harmonious World” perspective at the United Nations 60th anniversary in 2005, (Hu, 2005).

In handling international relations, China has consistently taken the “Five Principles of Peaceful Coexistence” as the guide instead of using social system, ideology or the concept of values as the criterion, (Embassy of China in the U.K, 2003). The Five Principles of Peaceful Coexistence were first articulated by Chinese Premier Zhou Enlai in December 1953. They were eventually written into the “Agreement between the People’s Republic of China and the Republic of India on Trade and co-operation” signed between the two countries in April 1954, (UN, 1958). The “Five Principles of Peaceful Coexistence” and are a set of principles to govern relations between states. (1) Mutual respect for each other’s territorial integrity and sovereignty, (2) Mutual non-aggression, (3) Mutual non-interference in each other’s internal affairs, (4) Equality and mutual benefit, and (5) Peaceful co-existence

In the decades that followed, Chinese leaders continued to advocate these principles internationally. While the Five Principles of Peaceful Coexistence remain as guiding principles of Chinese foreign policy, over the years, China’s policies have been

adapted to the changing international conditions and its own capabilities. Perhaps 1960s was an exceptional period in modern Chinese history, when indeed China attempted to export its brand of revolutionary communism including Mao Zedong's so-called "Three World Theory". Following Mao's explanation, the first world in his theory of world order comprised the USA and the Soviet Union; the second world was represented by Japan, Europe, Australia and Canada, whereas the third world consisted of the remaining socialist, least developed states and former colonies. China, in this model, was classified as socialist state and part of the "Third World", opposing hegemonic claims of the USA and the Soviet Union (Ye, 2001:131-134).

However, already by the late 1960s, it became clear that this was not a sustainable policy as it was deflecting attention from China's primary goal of economic development, (Pant, 2008). Later in the 70s, China entered a strategic partnership with the United States against the Soviet Union, and embarked upon an open up policy. Indeed, since 1978, China has adopted a uniquely pragmatic reform approach, with frequent changes in policy approaches, and constant political contestation. This pragmatism also marked the new approach to international collaboration, (de Haan, 2011). In the earlier 1980s, Deng Xiaoping forwarded the "Peace and Development" (*heping yu fazhan*) theory, arguing that the challenges China faced were "matters of North South divide", rather than East West differences. China faced no threat of war, but was threatened by its own lack of (economic) development, (Zheng & Tok, 2007).

But a few years later and in the wake of the 1989 "Tiananmen square massacre", the China "Threat Theory" of today began to emerge and with the end of the Cold War in the early 1990s, which abruptly ended the West's honeymoon courtship with China,

(Kwok, 2011). In response, Deng laid down two main post-Cold War foreign policy paths for China in March 1990, namely, pursuing anti-hegemonism, and establishing a new multi-polar international order of politics and economics, (Zhu, 211). The “New Security Concept”, espoused since the mid-1990s, calls for a departure from ‘Cold War mentality’ and hence US bilateral alliances, and has been pivotal in China’s co-operation with ASEAN as it resonates with their idea of ‘cooperative security’, (Acharya, 2004).

In the first decade of the 21st century, China took a turn in its international diplomacy to match its economic power and to dispel fears that as China rises it will become dangerous. As Avery Goldstein has argued, a central objective of China’s current “grand strategy” has been to reassure other countries of its benign intentions and this has been in large part a reaction to the ‘China threat’ debate, (Goldstein, 2005:203). The process of reassurance came with the doctrine of China’s *peaceful rise* in 2003, (Dellios, & Ferguson, 2011). Zheng Bijian, one of China’s leading intellectuals and former vice-chair of the Central Party School and deputy to Chinese President Hu Jintao, is often given credit as the first person to espouse “peaceful rise” as a policy of China in a speech entitled “A New Path for China’s Peaceful Rise and the Future of Asia” given on November 3, 2003 at the Bo’ao Forum for Asia. In the speech, he says that “China’s path is not only to strive to rise, but to adhere to peace, and never seek hegemony...China’s only choice is to strive to rise and, more importantly, to strive for a peaceful rise”, (The Brookings Institution, 2005). However in 2004, the Chinese government quickly retracted this concept and renamed it to an even less threatening term “peaceful development” because “rise” was too distressing for some; and in

recent years, it has come to promote the concept of “win-win” to characterize joint-cooperative efforts with other countries, (Cho, 2011).

A more proactive slogan came in the form of “harmonious world”, which matched the domestic slogan of “harmonious society” (Zheng & others, 2005). In July 2005 the “Harmonious World” idea made its way into a joint statement by China and Russia during Hu’s visit to Moscow. Hu Jintao then sketched it out further in September 2005 at the United Nations, (Yee, 2008). In his speech Hu said that the “Harmonious World” is based on four basic principles: (1) Uphold multilateralism to realize common security. (2) Uphold mutually beneficial cooperation to achieve common prosperity. (3) Uphold the spirit of inclusiveness to build a Harmonious World together. Diversity of civilizations is a basic feature of humanity and an important driving force behind human progress. (4) Promote UN reform actively and prudently. The purposes and principles of the UN Charter are consistent with the historic tide of peace, development and cooperation, (Hu, 2005).

Building a “Harmonious World” has become a new vision for China’s diplomatic theory. It has ushered in a new era for China’s diplomacy, in which China will stick to peaceful development while contributing to world harmony, (Wenbin, 2011). Indeed the idea of “Harmonious World” has become a strategic conception of constructing a new world order through diplomatic effort. “Harmonious World,” being the development of an independent foreign policy of peace to a higher level, has become the major item in the three ideas of the Chinese government; peace, harmony and win-win, and it clearly declares to the outside world China’s resolution to peaceful development, (Hao, 2009: 34).

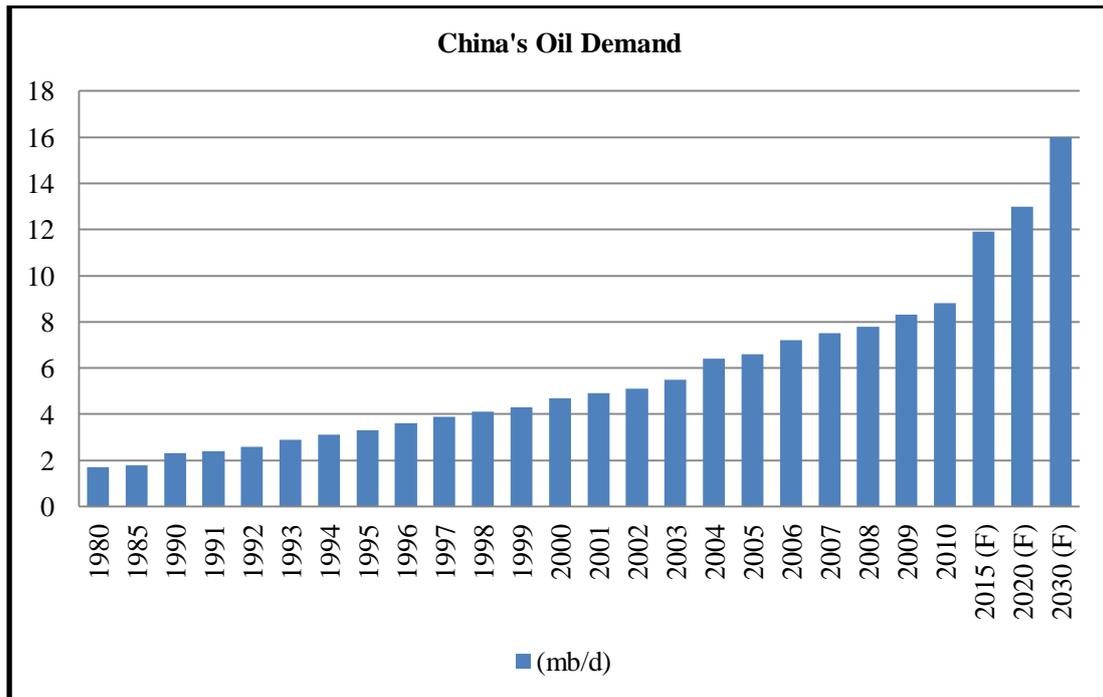
Most Chinese official and academics disagree with those arguments based on power transition theory, according to which, the rise of China will ultimately lead to Chinese power parity with the US, (Li & Worm, 2011). From the Chinese perspective, the concept of “Peaceful Development” is China’s strategic reaction to counter the so-called “China Threat Theory”, (Ronghua, 2006). Deng Xiaoping’s admonition that China should *tao guang yang hui* (to bide our time and build up our capabilities) still dominates China’s strategic thinking. There have been calls, especially from the People’s Liberation Army and some nationalistic and realists scholars, for China to play a bigger role in international affairs and be tougher in dealing with disputes. At the academic level there are also hot debates about “China’s Model” or “China alternative”. However, Chinese leaders seem to agree that China still has a long way to go before becoming a developed country, (Zhu, 2011). Indeed at the state level, China’s priority in the “important strategic opportunity period” is still domestic development so that China would try her best to avoid conflict and seek peace, (Li & Worm, 2011). Additionally, at the global level, the international system is characterized by economic interdependence and nuclear weaponry. This reality makes a military or confrontational power-shift/rise less likely or too costly for China to even consider, (Ibid).

2.6.2 The Evolution of China’s Energy Policy

Since it became an oil importer in 1993, China has sought to enhance its energy security by gaining access to the world energy market, diversifying its energy supply through imports and by acquiring overseas assets, (Tunsjø, 2010: 25-45). Yet China

still imports more than half of its oil needs. Growing dependence on imported oil later combined with rising oil prices and political/military developments has steadily pushed oil security up the Chinese Government's agenda (Andrews-Speed, 2010).

(Figure 2.6.2.1): China Growing Appetite for Oil (1980-2030)



Source: EIA (1980 to 2010) and OPEC (2015 to 2030), F= forecast

2.6.2.1 What is Energy Security?

The International Energy Agency (IEA) defines the energy security as: the uninterrupted availability of energy sources at an affordable price, (IEA, 2010). While the UN concept of energy security is as follows: a nation-state is energy secure to the degree that fuel and energy services are available to ensure: (a) Survival of the nation; (b) Protection of national welfare; and (c) Minimisation of risks associated with

supply and use of fuel and energy services, (UN, 2006: 149). Daniel Yergin argues that the objective of energy security is to assure adequate, reliable supplies of energy at reasonable prices and in ways that do not jeopardise major national values and objectives, (Yergin, 1988: 110-132). On the other hand, Saudi expert Anas Alhajji provides a different view; he argues that historically researchers and politicians have limited the concept of energy security to consuming countries, (Alhajji, September 2007). According to Alhajji, almost all OECD countries have designed their energy policies around three dimensions: security of supplies, the environment, and economics, (Ibid). In this regard, Alhajji provides a more comprehensive definition for energy security as “The steady availability of energy supplies in a way that ensures economic growth in both producing and consuming countries with the lowest social cost and the lowest price volatility”, (Alhajji, January 2008).

Saudi ARAMCO’s president and CEO Khalid A. Al-Falih argues that “Energy independence is a misleading, unachievable goal; rather, the focus should be on energy interdependence...energy security should be addressed in the framework of a strong interdependent relationship between suppliers and consumers”, (Martinchalk, 2010). While Prince Turki al-Faisal, the Chairman of the King Faisal Centre for Research and Islamic Studies and the former Director of Saudi intelligence and ambassador to Britain, Ireland, and the United States, takes the argument further to argue that American politicians should scrape the term of “energy independence” once and for all:

“Energy independence” has become a byword on the American political scene, and invoking it is now as essential as baby-kissing. All the recent U.S. presidential candidates employed it, and to this day, the White House Website lists as a guiding principle the need to ‘curb our dependence on fossil fuels and make America energy independent’...But this ‘energy independence’ motto is political posturing at its worst — a concept that is unrealistic, misguided, and ultimately harmful to energy-producing and -consuming countries alike...The

allure of demagoguery is strong, but U.S. politicians must muster the courage to scrap the fable of energy independence once and for all. If they continue to lead their people toward the mirage of independence and forsake the oasis of interdependence and cooperation, only disaster will result, (Al-Faisal, 2009).

In the debate about China's conception of energy security Yergin notes that "Many describe Beijing's policy options in ways that come perilously close to the shortage-equals-security-threat scenarios of the 1970s", (Yergin, 1998: 36). Similarly, and more recently, Erica Downs argues that the mainstream thinking about energy security in China shares the characteristics of the "traditional" approach: it is state centric, supply-side biased, overwhelmingly focused on oil and tends to equate security with self-sufficiency, (Downs, 2004: 22-23). While Phillip Andrews-Speed argues along these lines that the Chinese Government has adopted a "strategic" approach to China's energy security and, as such, prefers political means to economic ones to ensure the country's energy security, (Andrews-Speed, 2002:16-17). Meanwhile, the International Energy Agency recognises that the strategies deployed by China to respond to its increasing dependence on foreign markets are "the classic moves" of nations that find themselves in a new situation of reliance on imports, (IEA, 2000:74).

In this context, China's energy security concerns include the following aspects: (a) Unavailability & Political Risk; Oil is no longer a simple economic product, but a political product and a strategic material, (Beijing Times, May 31, 2006). Political instabilities in the Middle East, Africa, Latin American and Russia also can cause sudden falls in oil supply. Some hostile countries can use embargos and sanctions to cut off China's oil supply from the international market; (b) Fluctuation of oil price: high oil prices or the fluctuation of oil prices impact on China's macroeconomic instability, (Ibid). Bank of America-Merrill Lynch estimates that each US\$1 increase

in oil prices per barrel may cut China's annual trade surplus by US\$1.9 billion, (Bloomberg, 2011). For example, between January 2007 and July 2008, the price of a barrel of oil rose from US\$50 to more than US\$140; by the end of 2008, it had crashed to just over US\$30; less than a year later, it had breached \$80 again. In early 2011, on the back of strong global demand and the political turmoil in the Middle East, oil sold for over US\$120 a barrel, (Robert & Michael, 2011). China paid for crude oil imports over US\$11.6 billion in 2001 and more than US\$47 billion in 2005. The amount jumped to US\$135 billion in 2010 and the first half of 2011 China paid for crude oil imports only about US\$95.2 billion, (MOFCOM, July 2011) (see Table 2.6.2.1.1 below).

(Table 2.6.2.1.1): China's Oil Imports Bill (US\$ billions, 2001-2010)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Crude Petroleum Oils	11,6	12,7	19,7	33,9	47,7	66,4	79,8	129,3	89,2	135,2
Petroleum Oils, not Crude	3,7	3,7	5,8	9,2	10,4	15,5	16,6	30,1	16,9	22,4
All other Energy Products	2,1	2,7	3,6	4,8	5,9	7,1	8,6	9,7	17,7	31,2
Total Energy Imports	17,5	19,3	29,2	48,0	64,0	89,0	105,1	169,2	123,9	188,9

Source: UN COMTRADE, (December, 2011)

(c) Safety of international shipping lanes and pipe lines such as the Strait of Hormuz and the Strait of Malacca (around three quarters of China's oil imports cross through Strait of Malacca); and (d) Most important of all, the ruling Chinese Communist Party (CCP) has staked its legitimacy on its ability to deliver ever-wider prosperity. As a result, the government's focus on energy security is not merely an economic necessity - it is also a fight for political survival, (The *Economist*, July 12, 2007). Subsequently,

there are three major goals for China's energy strategy: (a) Ensuring China's long-term economic growth and prosperity; (b) Reducing China's energy vulnerability; and (c) Protecting the environment and avoiding ecological degradation and diseases, (He & Qin, 2006: 93-104).

2.6.2.2 The Evolution of China's Energy Policy

China began to pay attention to the issue of energy as early as 1980. On August 26, of that year, the Fifth National People's Congress Standing Committee decided to establish a National Energy Commission, (Bo, 2010). The Commission was soon dissolved in 1982 as it had too many overlapping responsibilities with other government commissions and ministries, (Wu & Wang, 2010: 17-20). In 1988 China formed the Ministry of Energy (MOE) after abolishing four other ministries - water conservancy and power, petroleum (where China National Petroleum Corporation or CNPC was formed), coal, and nuclear power, (Ibid).

Five years later, in 1993, however, the Ministry was also abolished in another round of the State Council restructuring, (Bo, 2010). Energy security became a major concern for China since the country became a net oil importer in 1993. Securing long-term oil supply has been a primary issue in China's policy towards the Middle East, where almost two thirds of the world's crude oil reserves are located, (Zhang, 2008). As early as 1993, the then Chinese Prime Minister Li Peng set the stage by defining the objectives of the country's energy policy as "to secure the long-term and stable

supply of oil to China.” This fundamental objective guided most of the energy decisions taken during almost the rest of the decade, (Scott, 2007: 137).

By February 1999, a major report was issued that indicated Chinese rethinking of energy security issues. China’s Energy Research Institute (ERI), under the State Development Planning Commission (SDPC, later became SDRC), issued *Study on Long Term Energy Development Strategies of China*, (Christoffersen, 2004). The report called for a radical break with past Chinese practices for energy security, changing from a coal-dependent, self-sufficient energy policy to the expansion of natural gas production and increasing imports of oil, (Ibid).

China’s vision for its companies to become international players was spelled out only in 1999 with the introduction of the “goes-out” policy, (EIU, 2010: 5). Chinese concerns about oil supply security became widespread in 2000, when the volume of China’s oil imports almost doubled to 70.2 million tons (1.4 mb/d), (Zha, 2005: 39-54). This was coupled with the sharp rise in crude oil price in 1999–2000, (Lee, 2005: 265-301), followed later by the events of September 11, 2001, which had a profound impact on international relations and strengthened the links between China and the Middle East, especially the Gulf region. There was a significant change in China’s policy on the Middle East as a whole, (Zhang, 2008). Subsequently, the issue of Chinese energy security had been inserted into the 10th Five-year plan (2001-2005), for the first time recognising it as a security issue, (Christoffersen, 2004).

2.6.2.3 China's "Goes-Out" Strategy

Since 2001, however, which was the year when China became a member of the World Trade Organisation (WTO), the support of the overseas expansion of Chinese companies became a major concern for the Chinese Government, (Schüller and Turner, April 2005: 3-14). In order to seize the opportunities the WTO entry and the closer global economic integration offered to the Chinese economy, the government wanted them to become internationally competitive players, (Ibid). With explicit reference to China's forthcoming accession to the WTO, Shi Guangsheng, the former Ministry of Foreign Trade and Economic Cooperation, underlined the importance of overseas investment as follows:

By "Going Global", the enterprises can invest and set up factories overseas, better utilize the domestic and foreign markets and resources, further expand the export of equipment, materials and labour service and create new export growth points. Thus we can enhance the level of China's opening to the outside world. (Ibid)

After entering the WTO in November 2001, China refocused its economic diplomacy on the tasks of securing access to energy and other resources, building competitive international companies, and opening developing country markets to Chinese goods and investment, (Saunders, 2006). At the end of 2001, the Chinese Government officially launched a broader policy of global economic engagement, namely the "*Zou Chu Qu*" or "goes-out" strategy. Later, "*Zou Chu Qu*" became an essential element in China's energy development strategies, (Zhang, 2008). In this regard Hongtu Zhao , one of the leading experts in Chinese energy politics, defines the "goes-out" policy in a comprehensive way: "Goes-out" (sometimes translated as 'going out' or 'go abroad') is actually a part of China's policy of opening up which means "invites in" and "goes out" to learn from the outside and integrate with the world. In the energy sector, "invites in" means attracting energy investment from overseas, lifting tariffs,

opening petroleum sales and carrying out initial public offerings (IPOs) of stock, (Hongtu, 2010). “Goes-out” means getting involved in the world market to be internationalised and developed into multinational corporations with high international competitive ability, (Ibid).

This policy of overseas investments in oil assets by the state-owned oil companies is meant to help China’s energy security by (1) diversifying oil supplies sources, (2) ensuring a better control on the production of these supplies, (3) depleting overseas deposits instead of national resources; and (4) insulating China’s economy from outside shocks, (Downs, 2004: 19-23). Additionally, it calls for Chinese companies to move into global markets to grow their revenue, to learn to be globally competitive, and, if possible, to acquire international brands, (Medeiros, 2009: 66) (see Table 2.6.2.3.1 below).

(Table 2.6.2.3.1): China’s NOC Motivations and Strategies

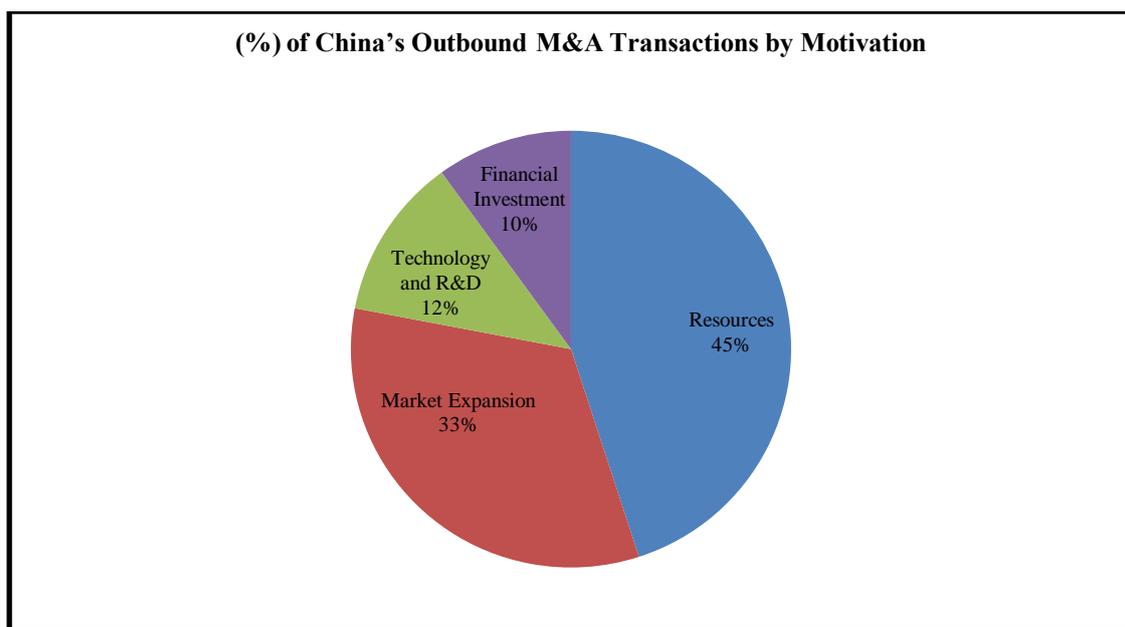
Motivations for Investing Abroad	Main Strategies Used to Expand
Expand oil and gas reserves and production.	Diversify energy supply sources and take advantage of new business opportunities.
Diversify energy supplies to avoid risks.	Target assets to add synergy to existing assets.
Become “international NOC.”	Partner with other NOCs and IOCs, build relationships and diversify risk.
Develop an integrated supply chain.	Pursue market-for-resources deals that exchange access to China’s market for access to resources.
Gain technical know-how and streamline managerial capacities.	Utilise strong financial resources and government policy support.

Source: Jiang & Sinton, 2011: 13

By 2003, the Chinese Government realised that their country was facing an energy crisis and that the main threat to security of energy supply was domestic rather than

international. A year later Beijing announced a new draft energy strategy which emphasised the overriding importance of energy efficiency and energy conservation and which set specific targets for energy savings, (Andrews-Speed, 2005). Energy security became a top priority in China’s diplomacy after two key events: U.S. military deployments to Central Asia after 9/11 and the U.S.-led invasion of Iraq in 2003. China sought to diversify its reliance on imported oil and gas from Middle Eastern suppliers, (Medeiros, 2009: 136). These developments were followed by a power crunch and in 2004 as China suffered severe power shortages, (Bai & Miles, 2011), when severe energy shortages at home resulted in a sharp increase in China’s demand for imported oil, causing international energy prices to soar to 20 year highs, (The *Economist*, July 12, 2007). Since then China has aggressively supported the “goes-out” policy. According to EIU, almost half of China’s outbound M&A transactions have been driven by the need to support the country’s growing demand for energy and natural resources (EIU, 2011) (see Figure 2.6.2.3.1 below).

(Figure 2.6.2.3.1): Motivations of Chinese Investment Abroad (2004-2009, %)



Source: CICC, Thomson Reuters, EIU

Despite that enthusiasm, China shortly realised that “goes-out” policy is not the “magic” solution for its energy security. In May 2005 Ma Kai, Chairman of the China’s National Development and Reform Commission (NDRC), which is in charge of planning and regulating the overall development of energy, defined four elements in the achievement of energy security: (a) Energy diversification; (b) Conservation; (c) Renewal; and (d) Cooperation, (Yao, 2006: 165-201). Two complementary strategies have been used by Beijing to diversify and secure their oil supplies. On the one hand, the government has used its diplomatic resources to lock long-term supply and transport agreements with producing countries; on the other, bilateral cross-investments in the oil and gas industry, (Downs, 2004).

Indeed, after implementing the “goes-out” strategy, it became clear that, while the companies have profited, neither Chinese citizens nor policymakers have seen much reward. If all the equity oil produced outside China was transported home (it is not) it would still only meet a fraction of the country’s import needs. This means it actually provides little insurance against supply disruptions, (Houser, 2011). Subsequently, a growing number of Chinese energy experts started to believe that “goes-out” strategy may not be fundamentally improving China’s energy security, and that the need for oil imports is simply growing too quickly to be met through equity investments and bilateral deals with producing countries, (Herberg & Zweig, 2010). There are also some in Beijing who feel that the overseas investment interests of China’s NOCs are not necessarily synonymous with China’s energy security interests. For example, most of the oil produced by China’s NOCs abroad is not shipped back to China, but sold into the global market in the same way other commercial oil companies do, (Ibid). In this regard, Downs noted that several Chinese oil company executives have stated

publicly and privately that they disagree with the notion that the acquisition of oil assets abroad can enhance China's energy security, (Downs, 2006).

On the global stage, Beijing's "goes-out" strategy was rapidly becoming a source of geopolitical tensions between China and the United States and had been regarded as "mercantilist", (see Table 2.6.2.4.2). The attempt of a Chinese NOC to buy out the American oil corporation UNOCAL in July 2005 triggered a political backlash in the U.S. Congress causing the final withdrawal of the Chinese company, (Li and Clark, 2010). The incident indicates the lack of trust of the U.S. in China's energy diplomacy, because the Chinese move was interpreted as undermining American energy security, (Ibid). In September 2005, the then U.S. deputy secretary of state, Robert Zoellick, called on China not to adopt a mercantilist strategy for achieving energy security, not to deal with failed or weak states, and to become "a responsible stakeholder" in the international system, (Zoellick, 2005). Additionally, the U.S. Administration's focus on China's quest for oil at that time was signalled when it published a revised National Security Strategy in March 2006, approved by then President Bush. The document stated that country's leaders are "expanding trade, but acting as if they can somehow 'lock up' energy supplies around the world or seek to direct markets rather than opening them up, as if they can follow a mercantilism borrowed from a discredited era", (The White House, March 2006).

Indeed, China's activities abroad have generated international concerns about possible confrontation between China and the West over energy resources. These concerns include: (a) China would disrupt the existing oil supply through the acquisition of overseas assets in the energy field or purchase of equity oil; and (b) China's interest in

developing a stronger military capability to protect the safety of oil transportation, (Tang, 2006). As for the Middle East there are a number of reasons for analysts to believe that China's growing energy relations with the Middle East, may cause a change of the status quo in the Middle East and pose security challenges to the United States. (a) Dependence on Middle Eastern oil might affect its international behaviour and shape its foreign policy; (b) China takes a strategic approach to energy security instead of a market-oriented one; (c) China's oil companies are still largely instruments of the State and are being treated as an arm of the Chinese Government's international expansion; and (d), China has no qualms about supporting some so-called "problematic countries" in these regions such as Iran and Sudan, (Hongtu, 2007).

Recognising these various constraints as a major bottleneck for achieving its social and economic strategies, the Chinese Government in 2007 put energy concerns at the top of its list of priority problems to be resolved in its development path, thereby fundamentally altering its development philosophy, (United Nations Environment Programme, 2011: 106). The 11th Five-Year Plan for Economic and Social Development (2006-2010) sets 22 quantitative indicators of which eight are mandatory targets, five of them related to environment and resources, (Ibid). It targeted reducing the energy consumption per unit of GDP by 20 percent in five years (from 2005 levels). According to the Chinese Government the country has met that target by the end of 2010, (Miles, 2011). Most important of all we witnessed a major shift in the behaviour of Chinese companies when they started to buy stakes in companies through the mechanisms of the international market (Canada, Australia,

Brazil, etc.), this in addition to entering into partnerships with western companies (Iraq, Saudi Arabia, Kuwait, etc.), (UNEP, 2011).

Furthermore, in January 2010, China established the National Energy Commission with Chinese Premier Wen Jiabao as the director of it, (*People's Daily*, January 27, 2011). The Commission includes the Ministry of Foreign Affairs, Ministry of State Security, and People's Liberation Army (PLA). Beijing's inclusion of the foreign affairs, security, and military intelligence apparatus in the NEC reflects China's deep concerns about energy security, (Lin, April 2011). Subsequently, China's "12th Five-Year Plan for National Economic and Social Development" (2011-2015) has introduced 24 major targets/indicators, some of which are binding while some are not. In relation to resource and environmental protection, seven out of the eight targets are binding, (Xinhua, March 31, 2011). This has resulted in the main target of (a) raising the share of non-fossil fuels in primary energy consumption to 11.4 percent, (Ibid). Finally, with the power shortage still gripping many parts of China (2004, 2008, 2010 and 2011), amid growing concerns that these shortages could lead to public anger and slow the economic growth, energy security debate will always be in the top of the Chinese leaders' agenda for years to come, (Wang & Li, 2011).

2.6.2.4 Chinese Energy Debate

China's shift to a net oil importer has generated much speculation outside China about how China's growing dependence on foreign oil will affect its international

behaviour, (Downs, 2004). While still a very significant oil producer, China now imports more than half of its crude oil needs (over 9 million barrels per day in 2010). China's share in global oil consumption rose from 6 percent in 2000 to over 10 percent in 2010, (World Economic Outlook 2011: 94). OPEC's *World Oil Outlook 2011* projects that China's share in global oil consumption will rise to around 12 percent in 2015 and jump to over 14 percent in 2020, (World Oil Outlook 2011: 63). The growing dependence on oil imports has created an increasing sense of "energy insecurity" among Chinese leaders, (World Economic Outlook, 2011).

(Table 2.6.2.4.1): China's Share of Global Oil Consumption, 1965-2010 (%)

	United States	OECD (excluding United States)	China
1965	37.0	37.3	0.69
1970	32.1	42.5	1.2
1975	29.8	40.4	2.4
1980	27.7	38.6	2.7
1985	26.4	36.1	3.0
1990	25.4	36.4	3.4
1995	25.3	38.2	4.8
2000	25.7	36.5	6.2
2005	24.9	34.3	8.3
2010 ^a	21.7	30.5	10.3

Source: IMF, (World Economic Outlook, April 2011)

(a) Adapted from IEA, (Oil Market Report , December 2011)

To meet China's quickly growing energy demands, Chinese leaders have struggled between a market-oriented approach and a state-centred approach. The market-oriented approach (liberals) mainly relies on national and international energy markets and seeks to reduce the risk of disruption by improving the efficiency of these markets, (Umbach, 2004: 137-168). The liberals' approach seeks energy security through enhanced integration of national and international markets and encourages

domestic and international investment in production and transportation, (Andrew-Speed, Liao, Dannreuther, 2002: 16-17). State intervention would be limited to the diffusion of information in a multilateral context, the support of innovation, and, for some, the management of a strategic oil reserve which would be used in case of momentary supply disruption, (Constantin, 2007: 1-30).

In contrast, the strategic (mercantilist) approach primarily involves state-sponsored economic measures and political initiatives, (Yuanming, 2009: 165-201). The mercantilist theory argues that the world economy is an arena of competition among states. States will seek to ensure their self-sufficiency in key strategic industries and commodities, and by using trade protectionism (tariffs and other limits on exports and imports), subsidies, and selective investments in the domestic economy and abroad, (Baylis & Steve, 2001: 285). It is also based upon neo-mercantilist thinking that relies on bilateral diplomatic contacts with oil producing countries to beef up energy security by the use of national resources and state-owned enterprise investments in overseas energy assets and a tight control of exports and imports of energy products, (Zhao, 2008: 207- 227). Accordingly, there is tension between those arguing that China's increasing dependence on imported oil supplies presents a strategic threat to China's national security, and those arguing that China's increasing oil imports should be treated as a normal by-product of its growing interdependence with the rest of the world, (Zha, 2006: 2-16).

(Table 2.6.2.4.2): The Differences between Strategic and Market Approaches

	Strategic Approach (realists)	Market Approach (liberals)
Supply-Side Economic Measures to Reduce Probability of Disruption	<ul style="list-style-type: none"> • Control through state companies • Self reliance • Investment in domestic and overseas production and transportation 	<i>Liberalize energy markets:</i> <ul style="list-style-type: none"> • Integrate with international markets • Encourage domestic and international investment in production and transportation
Demand-Side Economic Measures to Reduce Probability of Disruption	<i>Use administrative measures to:</i> <ul style="list-style-type: none"> • Increase energy efficiency • Adjust transport policy • Diversify transport fuels 	<i>Use market measures to:</i> <ul style="list-style-type: none"> • Increase energy efficiency • Adjust transport policy • Diversify transport fuels
Political Measures to Reduce Probability of Disruption	<ul style="list-style-type: none"> • Enhance political links with energy exporters • Outward investment and aid to energy exporters 	<ul style="list-style-type: none"> • Promote the efficient functioning on international markets
Measures to Reduce Impact of Disruption	<ul style="list-style-type: none"> • Strategic reserves • Oil sharing • Emergency response procedures • Fuel switching • Surge capacity 	<ul style="list-style-type: none"> • Strong U.S.-China cooperation • Implement <i>IEA</i>'s framework of strategic oil reserves (oil stocks equivalent to 90 days of its prior year's net imports). • Effective cooperation with <i>IEA</i> and the International organisations • Deepen interdependence with oil producers.

Source: Andrew-Speed, Liao, Dannreuther 2002: 16-17 and Zha, 2006: 2-16

Shambaugh argues that China's "realists" are the dominant group in the discourse on international relations and China's global role today, (Shambaugh, 2011: 7-27). Kenneth Lieberthal goes along similar lines to say that "China's energy strategy currently appears rooted in a statist, mercantilist mentality among political leaders in Beijing", (Lieberthal and Herberg, 2006: 9). Chinese realists take the nation-state as

their core unit of analysis, uphold the principle of state sovereignty above all else, and reject arguments that transnational issues penetrate across borders. Like realists elsewhere, they tend to see the international environment as anarchic and unpredictable, thus placing a premium on building up a strong state that can navigate its own way in the world and resist outside pressures, (Ibid). Chinese realists argue that China should accelerate naval build-up because its military self-defence capability lags far behind China's energy interest and military warfare, especially military warfare on the sea, which is the final means for great powers to solve international trade disputes, (Zhang, 2003: 16). Even the Chinese Government in its 2010 Defence White Paper proclaimed that its navy would take on a more expansive role, reaching out beyond its traditional focus on the coastline.

In line with the requirements of offshore defence strategy, the PLA Navy (PLAN) endeavours to accelerate the modernisation of its integrated combat forces, enhances its capabilities in strategic deterrence and counterattack, and develops its capabilities in conducting operations in distant waters and in countering non-traditional security threats. It seeks to further improve its combat capabilities through regularized and systematic basic training and actual combat training in complex electromagnetic environments. By organizing naval vessels for drills in distant waters, it develops training models for MOOTW missions. New types of submarines, frigates, aircraft and large support vessels have been deployed as planned. The PLAN enhances the construction of composite support bases so as to build a shore-based support system which matches the deployment of forces and the development of weaponry and equipment, (China's 2010 Defence White Paper, March 2011).

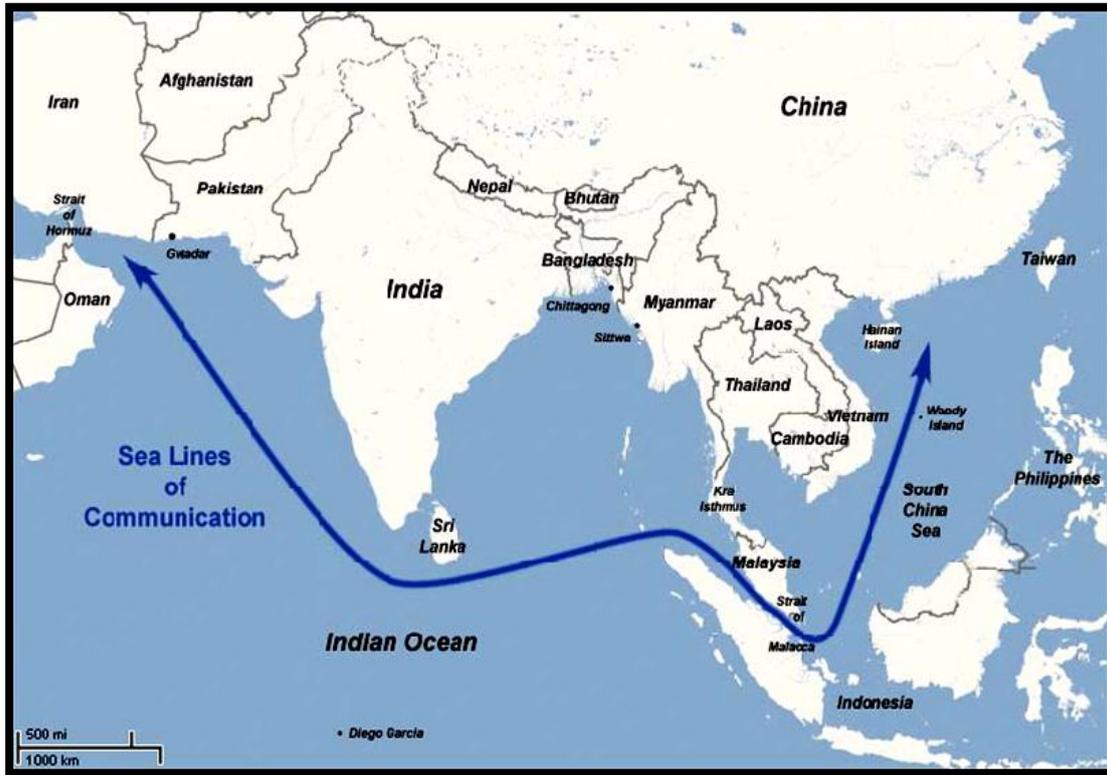
Zhang Wenmu, a famous Chinese realist, argues that China is almost helpless to protect its overseas oil import routes. This is an Achilles heel to contemporary China, (Zhang, 2006: 17-31). The most crucial conduit connecting China with the Middle East and with the rest of the world is the sea lanes and, therefore, China must have a powerful navy, (Ibid). Zhang goes further to say: "We must build up our navy as quickly as possible...Otherwise, China may lose everything it has gathered in normal international economic activities, including its oil interests, in a military defeat", (Wemmu, 2003). Chinese influential scholar Shi Yinhong argues that the majority

among China's political elites are hoping for long-term accommodation with the United States, but seriously doubt its probability, believing that perhaps there may be a long "Cold War" confrontation or even major conflict between China and the United States in the coming decades, (Shi, 2001).

On the extreme, Liu Mingfu, a senior colonel who is a professor at the elite People's Liberation Army's National Defence University and the author of "*The China Dream*", has declared that replacing the United States as the world's top military power should be China's goal, (Wang, 2011: 68-79). Liu call for China in his recent published Chinese-language book to abandon modesty about its global goals and "sprint to become world number one...China's big goal in the 21st century is to become world number one, the top power...If China in the 21st century cannot become world number one, cannot become the top power, then inevitably it will become a straggler that is cast aside", (Buckley, March 1, 2010). Liu and other PLA officers, however, say they see little chance of avoiding deepening rivalry with the United States, whether peaceful or warlike.

In this regard, some Chinese officials and scholars also noted that China is uncomfortable with the fact that the United States' navy dominates the sea lanes stretching from the Middle East to the South China Sea through which the bulk of China's oil imports must pass. PLA Gen. Qian Guoliang stated that the threat to China emanates concurrently from "one point and one lane." While the "point" refers to Taiwan, the "lane" was an allusion to the long voyage of Chinese tankers returning home via the Indian Ocean and the Straits of Malacca, (Jha, 2010).

(Figure 2.6.2.4.1): China's Sea-lines of Communications



Source: Google's maps

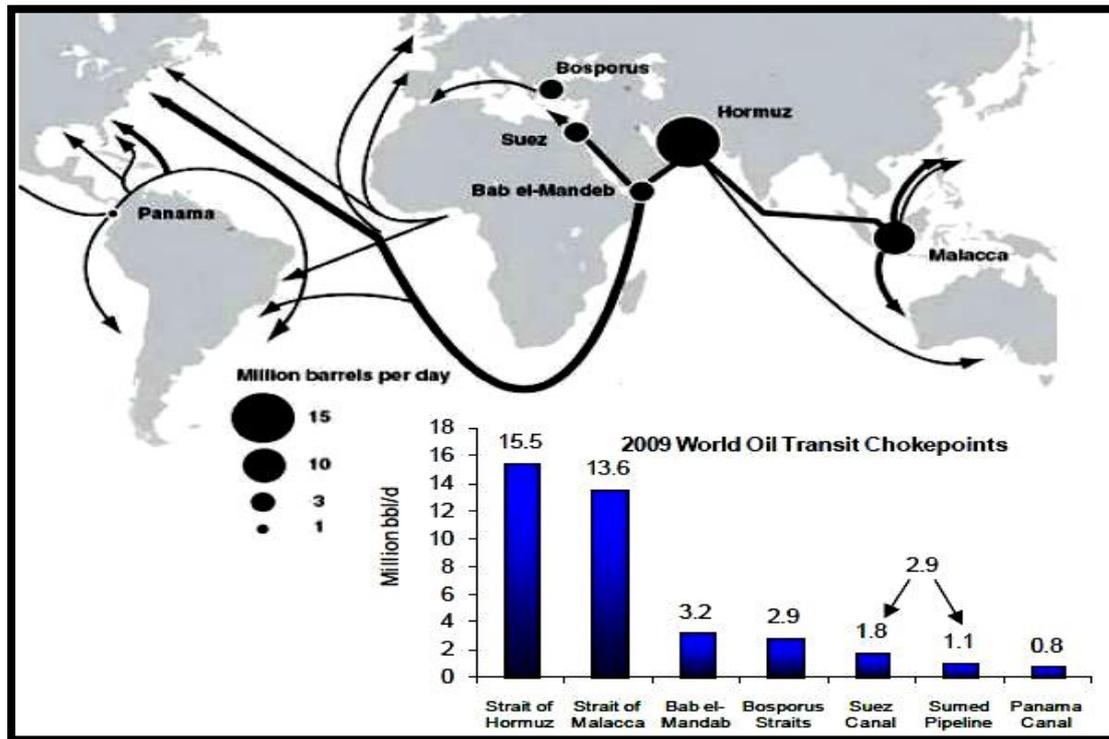
Another Chinese commentary puts it strongly, “It is no exaggeration to say that whoever controls the Strait of Malacca (SOM) will also have a stranglehold on the energy route of China”, (Zhongguo Qingnian Bao, 2004). In fact, some Chinese analysts have accused the United States, Japan, and India of using transnational threats (especially piracy) in the area as a pretext to bolster their regional naval forces. According to Lu Guoxue, Washington’s intention is to curtail China’s rising power by restricting its access to energy supplies through the SOM, (Ibid). While Chinese scholar, Chen, argues that in every respect the Straits of Malacca² can be regarded as

² The Straits of Malacca are one of Important World oil transit chokepoints. Located between the east coast of Sumatra Island in Indonesia and the west coast of Peninsular Malaysia and linked with the Strait of Singapore at its southeast end, the Straits of Malacca are 600 miles long and provide the main corridor between the Indian Ocean and the South China Sea, (Chen, 2009).

a lifeline of the rising dragon. However, as China lacks the capacity to project its naval power, her growing reliance on the Strait is rapidly turning into a strategic weakness, (Chen, 2009). China's President Hu calls this strategic weakness "the Malacca dilemma", and considers it key to China's energy security. He is concerned that "certain powers (a codeword for the United States) have all along encroached on and tried to control the navigation through the Strait", (Zweig & Jianhai, 2005:24-38).

In this context Chinese scholars recognise the American dominant position in the Arabian Gulf and Middle East's instability, noting that since 1951 ten of the sixteen major global oil supply disruptions have originated in the region, (Erickson and Goldstein, 2009: 43-76). There is a concern that if Sino-U.S. relations sour, the United States could use its superior military power to disrupt China's oil supply, (Downs, 2004: 45). The U.S. navy controls all critical energy transport sea lanes, (Greg, 2005). China does not possess the military capabilities to secure the sea lines of communication, (through which the majority of its oil imports travel), but must rely on the United States to guarantee safe passage, (Downs, 2004).

(Figure 2.6.2.4.2): World's Major Oil Transit Chokepoints



Source: EIA, 2011 (data estimates based on APEX tanker data); GAO (map)

Furthermore, the former Chinese special envoy to the Middle East “*Sun Bigan*”, a 30-year veteran of the Middle East, a former Ambassador to Iran, Iraq, and Saudi Arabia and, now retired, who now works for a government-run association promoting ties with Asia and Africa, argues “clashes are unavoidable” between China and the United States in the Middle East. He thinks that China and the United States risk deepening rifts over influence and oil in the Middle East. He also believes “the U.S. has always sought to control the faucet of global oil supplies. There is cooperation between China and the U.S., but there is also struggle, and the U.S. has always seen us as a potential foe...bilateral quarrels and clashes are unavoidable. We cannot lower vigilance against hostility in the Middle East over energy interests and security”, (Reuters, September 30, 2009). He also thinks “U.S. Obama’s new Middle East policy is merely a tactical adjustment, and the United States will not and cannot alter its global

goals and dominance...both now and in the future, the Middle East should be our first choice in importing oil and developing oil cooperation...China should focus on strengthening trade with Saudi Arabia, Iran and Oman”, (Ibid). His worries were echoed by Dai Songyang, an energy journalist writing for the internet-based China Energy Web. Dai argues that “The United States recognises Yemen’s geographic ability to choke China’s oil import lifelines.” He then hints that the United States may bring the war on terror to Yemen, in order to “strangle China’s oil imports and its economy”, (Simpfendorfer, 2010). Additionally, Soozhana Choi, an oil analyst with *Deutsche Bank* in Singapore who has just published a report on the subject – “*China’s SPR ambitions*” – argues along these lines that the recent events in the Middle East and North Africa “only serve to emphasise the importance of energy security and strategic oil reserves as a policy tool”, (Blas, 2011).

On the other hand, Chinese liberals argue that oil is a global commodity which needs cooperation not conflict. For Chinese liberals, it is not in geopolitics but the politics of conservation that Beijing policymakers need to turn. Factors such as “efficiency, liberalization of domestic energy investment and markets, and other domestic components of energy security” offer much more leverage against the challenge, (Blair, 2006: 32-64). Professor Zha Daojiong of Peking University, a leading representative of a market or interdependent view, argues that “China’s dependence on maritime energy transportation is a natural state of affairs that must be managed, (Zha, 2006). China’s path to oil security lies in greater integration with the existing global oil market, (Zha, 2005). While Chu Shulong of Qinghua University, one of China’s pre-eminent experts on U.S.–China relations, has criticised the notion that China can or should try to match U.S. military power, whether to protect the sea lines

of communication through which energy shipments flow or for other reasons. In his view, such a goal would be unrealistic, unnecessary and provocative, (Kennedy, 2010: 137-158). Furthermore, Fu Mengzi, an assistant president of and a research professor with the China Institute of Contemporary International Relations argues that on the security front, the U.S. has the enviable capability of “striking balance”, while China’s influence is growing in its neighbourhood and it has more say in regional thorny issues, (Fu, 2011). For Chinese liberals economic interdependence serves as the single most powerful deterrent against an embargo or blockade by China’s neighbours. According to them, China must now view energy security in terms of economic threats and market solutions rather than military threats and diplomatic responses, (O’Brien, 1997: 8-13).

Indeed, Hongtu Zhao, deputy director of the Institute of World Economics Studies at the China Institutes of Contemporary International Relations, argues that an oil blockade by the U.S. would only be likely to occur in wartime. The United States would not be able to insulate itself from the disruption of the world oil market that would result, and that it would be impossible to blockade the Malacca Strait effectively without cutting off oil to Japan and South Korea as well. Zhao thus sees an American-led blockade of China as unlikely, (Kennedy, 2011). While Chinese scholar, Mao Yushi, furthers this point: “War and killing over resources has been rendered unnecessary. Taking Japan as an example once again, it remains a resource-poor country, yet it has achieved the status of a world economic power. It purchases all vital resource and energy needs”, (Mao, 2006: 106-115). Zhang Jian, a consultant in the office of the Chief Economist at the World Bank, argues that the impact of the recent global financial crisis after the 2008, as well as turmoil in many parts of the

Middle East and North Africa in early 2011, have caused Beijing to further realise the importance of energy source diversification, the linkage of fiscal and monetary policy with energy policy, especially monetary policies that relate to international energy, commodity trading, equity markets, and financial markets, (Chen, 2011).

2.7 CONCLUSION

In sum, China through her evolving energy policy since 1993 seems to combine the two approaches (Market and Strategic) by pursuing a two-pronged strategy toward energy; (engages but hedge). Beijing will continue on the one hand to enhance cooperation with the U.S. and political links with energy exporters, increase energy efficiency, diversify, accelerate investments and overseas production and transportation, while on the other hand will strengthen China's emergency response.

(Table 2.7.1): Summary of China's Oil Development

The Development History of China's Oil Industry	
Phase 1: 1978 - 1992	Self-reliance and self-sufficiency are the key objectives of energy policy. The National Development and Reform Commission is founded and placed in charge of the energy sector. State-owned enterprises can access limited foreign markets.
Phase 2: 1993 - 1999	Production of oil can no longer meet domestic demand. Government starts to conduct reform to increase competitiveness of the SOEs. Enterprises start to seek oil in foreign markets
Phase 3: 2000 - 2008	"Goes out" starts to become the main slogan and government encourage firms to go abroad. China's accession to WTO further increases domestic business competition. SOEs and private firms expand their business worldwide.
Phase 4: 2008 - present	"Go abroad and buy", is the response to the financial turmoil that began in 2008, and hastened China's investment expansion at the global level. China's investments in resource and energy sectors have increased dramatically.

Source: Chen, 2011:6

This thesis expects growing interdependence between China and the Middle East in general, and Saudi Arabia in particular.

- The study forecasts that the volume of bilateral trade between China and Saudi Arabia could double over the next few years
- Our research projects that China will overtake the U.S. and become Saudi Arabia's top oil importer during the next five years

Within the framework of these expectations and guided by Trade Expectations Theory (TET), the study expects that the stability of Saudi Arabia and the Arab Gulf States will be at the top of China's interests in the coming years.

CHAPTER THREE

CHINA-MIDDLE EAST OIL BACKGROUND

3.1 INTRODUCTION

With the end of the Cold War and China's emergence as a net oil importer, Beijing's primary interest in the Middle East has been to gain access to the region's vast energy supplies in order to expand its economic opportunities. While China is trying to diversify its energy import supplies, the Chinese still depends on the Middle East for half of their oil imports, (IEA, 2011). In the last decade, China has been upgrading its diplomatic, economic, cultural, and military relations with several countries in the Middle East, (Medeiros 2009: 160). China's growing demand for energy is an important driver of this upgrading but it is not the only one, (Ibid) or as Weilie Zhu, the Director of the Middle Eastern Studies Institute at Shanghai International Studies University, puts it: "Its geographical position, religious significance, and, above all, massive oil reserves all make it a critical region for any country that wants to retain its status as a great power", (Zhu, March 31, 2011).

Since China became a net oil importer, the amount of oil from overseas increased from nil to over 50 percent in merely two decades, (Economides, January 26, 2010). China's surging imports have risen from zero imports in 1992 to over 4.8 million barrels a day in 2010 and are expecting to rise to about 7 million barrels daily (mb/d) in 2020, (see tables 3.11, 3.2.1.4 & 3.2.1.2). This will inevitably elevate the Middle East to the top of China's supply chain, (Blair, Yali, & Hagt. 2006: 33-63). This dependence on foreign oil has become a key driver for Beijing to establish close

economic and political ties with major oil producing countries, especially Saudi Arabia, (Tu, 2006).

(Table 3.1.1): China's Oil Production, Consumption and Imports, 1990-2010

	Total Oil Supply (mb/d)	Total Consumption of Petroleum Products (mb/d)	Oil Imports (Thousand Barrels Per Day)
1990	2,76	2,29	58
1991	2,83	2,49	121
1992	2,85	2,66	230
1993 ^a	2,90	2,95	312
1994	2,95	3,16	251
1995	3,05	3,36	349
1996	3,21	3,61	459
1997	3,28	3,91	717
1998	3,30	4,10	579
1999	3,31	4,36	744
2000	3,37	4,79	1400
2001	3,43	4,91	1353
2002	3,52	5,16	1394
2003	3,55	5,57	1805
2004	3,65	6,43	2448
2005	3,79	6,69	2598
2006	3,86	7,26	2904
2007	3,92	7,53	3264
2008	3,98	7,81	3568
2009	3,99	8,22	3880
2010	4,30	9,08	4787

Source: EIA, International Energy Statistics, various years

(a) China became net oil importer in 1993

This chapter provides a statistical survey to China's oil situation and describes how it fits in with Beijing's Middle East strategy. The chapter will give a strong indication of China's intentions towards its relations with the Middle East and will discuss why the Middle East region has particular significance for China in meeting its energy objectives. This case study attempts to decipher Chinese motives towards the Middle East. If China is acting within the realist model, it should be attempting to expand its

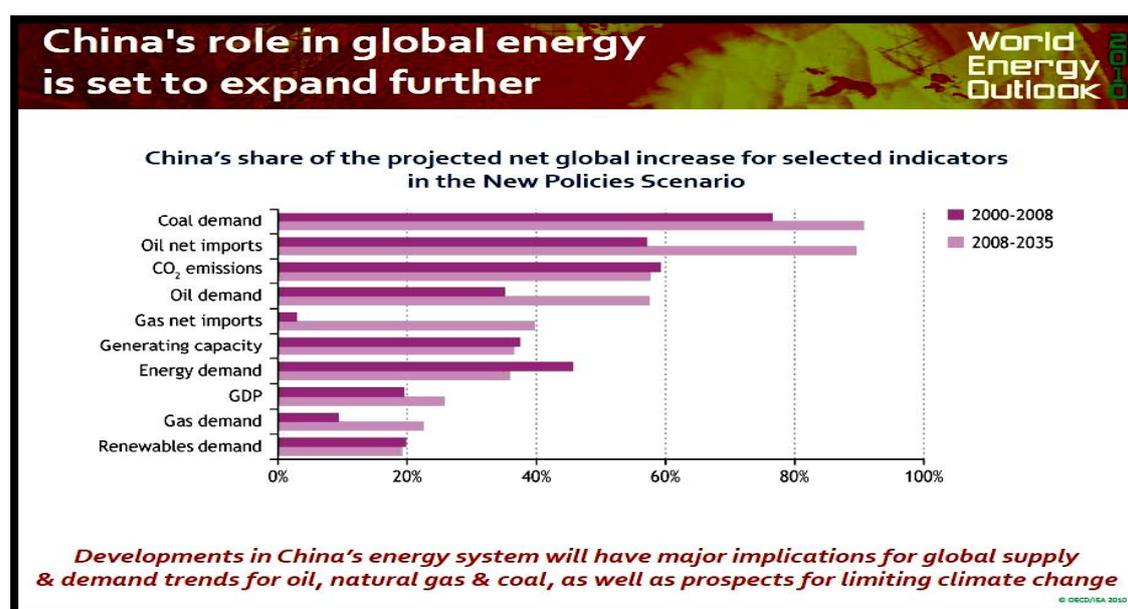
power and influence in the Middle East at every opportunity with the intent to undermine U.S. influence. If China is acting in the economic interdependence theory, it should be developing a Sino-Middle East relationship based on energy security and not based on a political agenda. In this regard we will show the conditions under which high energy interdependence between China and the Middle East will lead to a pacific or belligerent China. If decision-makers' expectations of future trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future trading environment they will likely take action to protect their interests in the region.

3.2 CHINA'S OIL SITUATION: STATISTICAL EVALUATION

China's growing appetite for oil is the product of the country's 30-year-long economic boom, which has seen expanding external trade, rising incomes, a growing population, and increasing urbanisation. Over the last 10 years, Chinese GDP has almost tripled and its energy consumption has more than doubled, (Dudley, May 24, 2011). It has become the world's largest energy producer, (Ibid) and the largest energy consumer (20.3 percent of the world's total) (BP Statistical Review, 2011: 2), taking over from the U.S., and the largest aggregate emitter of energy-related carbon dioxide, (Dudley, 2011). British Petroleum "Energy 2030 Outlook" suggests China's energy demand will increase by 80 percent over the next 20 years – that is twice the rate of growth for the world as a whole and is likely to account for over 40 percent of the increase in total energy demand in this period, (BP Energy Outlook 2030, 2011).

Drawing from the World Energy Outlook 2010, three scenarios are presented in this chapter (and the next chapters), differentiated by the underlying assumptions about government policies. The *New Policies Scenario* takes account of the broad policy commitments that have already been announced and assumes cautious implementation of national pledges to reduce greenhouse gas emissions by 2020 and to reform fossil-fuel subsidies. The *Current Policies Scenario* (Reference Scenario in OPEC’s World oil Outlook) takes into consideration only those policies that had been formally adopted by mid-2010. The third scenario, the *450 Scenario*, assumes implementation of the high-end of national pledges and stronger policies after 2020, including the near-universal removal of fossil fuel consumption subsidies, to achieve the objective of limiting the concentration of greenhouse gases. In this regard the International Energy Agency (IEA) forecasts in its annual World Energy Outlook 2010, that China will drive a surge in world oil demand over the next quarter century, (see Figure 3.2.1 below)

(Figure 3.2.1): China’s Share of the Projected Net Global Oil Net Imports



Source: World Energy Outlook 2010

3.2.1

China's Oil Demand: Skyrocketing Trend

China's oil demand tripled over the past two decades, increasing from 2.95 million barrels per day (mb/d) in 1993 to over 9 (mb/d) in 2010, (IEA, May 12, 2011), or over 10 percent of the world's global demand, making it second only to the United States, (Ibid). China consumed an estimated 9.1 (mb/d) of oil in 2010, up nearly 900 thousand barrels per day, or over 10 percent from year-earlier levels. China's net oil imports reached about 4.8 (mb/d) in 2010 and it became the second largest net oil importer in the world behind the United States in 2009, (EIA, May 2011).

Chinese and international oil experts alike agree that China's demand will increase, the only question is by how much? Oil experts also agree that China's oil demand will continue to grow through to 2035, although their projections vary. Recent estimates range from 7 (mb/d) to around 13 (mb/d). Different assumptions about the growth rate of China's gross domestic product (GDP) and the income elasticity of demand probably explain a large portion of the discrepancies. In addition, China does not release official oil demand statistics, and reporting agencies often have differing figures for the country's apparent oil demand. If history is any guide, higher estimates may prove to be more accurate; both Chinese and international forecasters have repeatedly underestimated China's oil demand, (Downs, 2006).

(Table 3.2.1.1): Real GDP Growth by Selected Region

Compound Average Annual Growth Rates					
	1990-2008	2008-2020	2010-2015	2020-2035	2008-2035
China	10.0%	7.9%	9.5%	3.9%	5.7%
India	6.4%	7.4%	8.1%	5.6%	6.4%
Middle East	3.9%	4.0%	4.3%	3.8%	3.9%
Africa	3.8%	4.5%	5.5%	2.8%	3.55%
Latin America	3.5%	3.3%	4.0%	2.7%	3.0%
Brazil	3.0%	3.6%	4.1%	3.1%	3.3%
United States	2.8%	2.0%	2.4%	2.1%	2.1%
EU	2.1%	1.4%	2.1%	1.7%	1.6%
Japan	1.2%	1.0%	1.9%	1.0%	1.0%
Russia	0.6%	2.9%	4.1%	3.1%	3.0%
World	3.3%	3.6%	4.1%	2.9%	3.2%

Sources: IMF and World Bank Databases

In the medium term the IEA's forecasts for global oil demand a growth of 1.3 percent annually over the next five years as the economy expands in China. Global oil consumption will increase 1.2 million barrels a day over the next five years, (IEA, June 2011: 36-56). Net oil demand growth of 7.2 (mb/d) during 2010-2016 (+1.2 mb/d annually) derives entirely from the non-OECD countries, with China alone accounting for 41 percent of the total, or about 2.9 million barrels, (Ibid: 16-52). As for the Chinese estimates, according to Liu Xiao Li of the Energy Research Institute, part of China's economic planning agency, the National Development and Reform Commission (NDRC), demand for oil will grow 4-5 percent a year to hit 530 -560 million tonnes (10.6 -11.3 mb/d) in 2015, with transport fuel and chemical feedstocks driving the increase. Growth will then slow to 2-3 percent a year, to reach 590-650 million tonnes (11.8-13 mb/d) by 2020, (Platts, May 24, 2011). While China's Social Science Academy forecasts that China's oil consumption could reach 10.6 million barrels per day by 2015, and imported oil is likely to reach the U.S. level of 65

percent of total consumption by 2020. It is estimated that China may need 16.1 percent of the tradable oil in the world market by 2020, (Economides, 2010).

(Table 3.2.1.2): Forecast of Global Oil Demand, 2010-2016 (mb/d)

	2010	2011	2012	2013	2014	2015	2016
Global Demand	88,02	89,3	90,6	91,92	93,1	94,2	95,2
China	9,07	9,6	10,1	10,5	11,0	11,5	12,02
Non-OPEC Supply	52,7	53.2	54.1	54.2	54.3	55.1	55.3
OPEC Crude Capacity	35.7	34.2	34.4	35.8	36.9	37.6	37.8

Source: IEA, Medium-Term Oil and Gas Markets, (June 2011)

In the long-term, BP’s “Energy Outlook 2030” projects that Non-OECD Asia (mainly China and India) accounts for more than three-quarters of the net global increase, rising by nearly 13 (mb/d), (BP Energy Outlook 2030, 2011: 27). While the IEA’s World Energy Outlook 2010 New Policies Scenario, predicts that global demand for oil will continue to grow steadily, reaching about 99 (mb/d), (excluding bio-fuels) by 2035 — 15 (mb/d) higher than in 2009. All of the growth comes from non-OECD countries, 57 percent from China alone, mainly driven by rising use of transport fuels; demand in the OECD falls by over 6 (mb/d), (World Energy Outlook, 2010: 101), while oil demand increases the most in China (7.1 mb/d), (Ibid: 77). The IEA in its World Energy Outlook 2010 “Current Policies Scenario/Reference Scenario” projects that China’s daily demand for oil will be higher to reach 11.4 million barrels a day by 2020, to hit over 14 (mb/d) by 2030, (World Energy Outlook, 2010). While in BP’s Energy Outlook 2030 predicts that China will be the largest source of oil consumption growth, with consumption forecast to grow by 8 (mb/d) to reach 17.5 (mb/d) by 2030, overtaking the U.S. to become the world’s largest oil consumer, (BP Energy Outlook 2030, 2011: 33). More interestingly, OPEC and U.S.’s projections put China’s oil demand even higher, (see Table 3.2.1.3).

Indeed, China will continue to lead the charge as the No. 1 energy consumer over the next quarter century, and oil will remain the dominant fuel despite huge investment in alternatives. China is expected to account for more than a fifth of world demand by 2035. The World Energy Outlook 2010 predicted that China's demand would jump 75 percent between 2008 and 2035, contributing 36 percent to the projected growth in global energy use. Global demand would reach 16.74bn metric tonnes of oil equivalent by 2035, (World Energy Outlook, 2010). The biggest increase in demand in absolute terms occurs in China, where it jumps from just over 9 mb/d in 2010, (IEA, July 13, 2011), to more than 15 (mb/d) in 2035 — an increase of 2.4 percent per year on average in the New Policies Scenario, (World Energy Outlook, 2010: 104) (see Tables 3.2.1.2 and 3.2.1.3 below).

(Table 3.2.1.3): Oil Production and Supply by Source and Scenario (mb/d)

			New Policies Scenario		Current Policies Scenario		450 Scenario	
	1980	2009	2020	2035	2020	2035	2020	2035
OPEC	25.5	33.4	40.5	49.9	41.9	54.2	40.1	41.7
Non-OPEC	37.1	47.7	48.2	46.1	48.9	49.9	45.1	36.7
World production	62.6	81.0	88.7	96.0	90.8	104.1	85.2	78.5
World Supply	63.8	83.3	91.3	99.0	93.5	107.4	87.7	81.0

Source: World Energy Outlook 2010

(Table 3.2.1.4): China Oil Demand and Projection 2015-2030

Reference Case/Current Policies Scenarios (mb/d)										
	2010	2015			2020			2030		
		OPEC	IEA	EIA	OPEC	IEA	EIA	OPEC	IEA	EIA
China total	9.07	11.6	11.6	12.1	13.8	-	13.6	17.1	14.1	16.4
World total	88.24	92.9	94.4	93.3	97.8	-	97.6	105.8	106.4	108.0
China's Share of World Demand (%)	10.3	12.4	12.2	12.9	14.1	-	12.5	16.1	13.2	14.3

Source: based on World Oil Outlook 2011, World Energy Outlook 2010, International Energy Outlook 2011 and IEA, Medium-Term Oil and Gas Markets, (June 2011)

Indeed, by 2035, China could overtake the United States to become the largest oil consumer in the world, as oil demand in the United States declines from 17.8 mb/d in 2009 to 14.9 mb/d in 2035, (World Energy Outlook, 2010: 86). Although China's per-capita energy consumption is currently below the world average, in 2035 it is predicted to be 40 percent higher than today's global average (or 30 percent higher than the 2035 global average), thanks to strong economic growth and relatively slow population growth, (Ibid: 89). By 2035, China will account for 22 percent of world energy demand, up from 17 percent today, (Ibid: 47) (see Table 3.2.1.4).

(Table 3.2.1.5): China's Total Consumption of Energy and Its Composition 1990-2010

	Total (million metric tonnes of coal equivalent)	As Percentage of Total Energy Consumption			
		Coal (%)	Oil (%)	Natural gas (%)	Others (includes hydro-, Nuclear and Wind Power)
1990	987.0	76.2	16.6	2.1	5.1
1991	1037.8	76.1	17.1	2.0	4.8
1992	1091	75.7	17.5	1.9	4.9
1993	1159.9	74.7	18.2	1.9	5.2
1994	1227.4	75.0	17.4	1.9	5.7
1995	1311.8	74.6	17.5	1.8	6.1
1996	1351.9	73.5	18.7	1.8	6.0
1997	1359.1	71.4	20.4	1.8	6.4
1998	1361.8	70.9	20.8	1.8	6.5
1999	1405.7	70.6	21.5	2.0	5.9
2000	1455.3	69.2	22.2	2.2	6.4
2001	1504.1	68.3	21.8	2.4	7.5
2002	1594.3	68.0	22.3	2.4	7.3
2003	1837.9	69.8	21.2	2.6	6.8
2004	2134.6	69.5	21.3	2.5	6.7
2005	2360.0	70.8	19.8	2.6	6.8
2006	2586.8	71.1	19.3	2.9	6.7
2007	2805.1	71.1	18.8	3.3	6.8
2008	2914.5	70.3	18.3	3.7	7.7
2009	3066.5	70.4	17.9	3.9	7.8
2010 ^a	3247.4	70.0	19.1	4.3	6.6

Source: China Statistical Yearbook, (2010)

(a) Adapted from *The Wall Street Journal* (28 February, 2011)

Despite increases in the use of renewable and nuclear energy sources, the pattern of China's primary energy usage has remained relatively constant since 1978 as illustrated in Table 3.2.1.5. Oil accounts for only about 20 percent of China's total energy consumption in the past decade and is unlikely to change in the next decade, (see Tables 3.2.1.6, 3.2.1.7 and Figure 3.2.1.1). Coal remains the dominant energy source, making up 70 percent of China's total energy consumption. Unless new clean coal technologies drive up the cost, coal will remain inexpensive relative to other resources in China and it is likely to remain China's main source of energy in the next few decades, (Jian, July 2011).

In general, transport can be regarded as a "captive market for oil", as there is no cost-effective and efficient substitute for oil in this sector. Fatih Birol, the IEA's chief economist, argues that: "The greatest driver for oil demand will come from the transportation sector." Indeed, China's transport fuel and chemical feedstock will account for 70 percent of the oil demand in 2020, up from less than 50 percent in 2000, with oil production in 2020 expected to be 200-230 million tonnes, which would imply an import dependence of around 65 percent, (Ibid). Demand for cars in China is set to increase about tenfold by 2035, (Pfeifer, November 9, 2010) (see Tables 3.2.1.5 & 3.2.1.6).

(Table 3.2.1.6): China's Future Oil Demand in Current Policies and 450 Scenarios

		Energy Demand (Mtoe) (a)						Shares (%)			
		2020	2030	2035	2020	2030	2035	2020		2035	
		Current Policies Scenario (CPS)			450 Scenario			CPS	450	CPS	450
TPED (b)		3288	3907	4125	3097	3094	3131	100%	100%	100%	100%
Fossil Fuels											
Coal		2104	2422	2574	1878	1398	1189	63.9%	60.6%	61%	38%
Oil	(Mtoe)	567	698	755	543	605	617	17.2%	17.5%	18%	20%
	(mb/d)	11.4	14.1	15.2	10.9	12.2	12.4				
Gas		179	270	326	178	266	321	5.4%	5.7%	8%	10%
Renewable Energy											
Nuclear		124	174	189	143	288	358	3.7%	4.6%	4%	11%
Hydro		92	106	112	94	117	120	2.8%	3.0%	3.0%	4.0%
Biomass and Waste		191	184	196	200	259	308	5.8%	6.4%	5.0%	10%
Other Renewable		32	54	63	61	162	218	0.09%	1.9%	10.0%	7.0%

Source: World Energy Outlook 2010

(a) Million Tonne of oil equivalent & (b) Total Primary Energy Demand

(Table 3.2.1.7): China's Energy Demand in New Policies Scenario

		Energy demand (Mtoe)					Shares (%) (a)				
		2008	2015	2020	2025	2030	2008	2015	2020	2025	2030
TPED		2131	2887	3159	3369	3568	100	100	100	100	100
Fossil Fuels											
Coal		1413	1879	1952	1981	1990	66.3	65.1	61.7	58	55.7
Oil	(Mtoe)	369	509	558	616	675	17.3	17.6	17.6	18.2	18.9
	(mb/d)	7.4	10.2	11.2	12.4	13.5					
Gas		71	142	181	223	277	3.3	4.9	5.7	6.6	7.7
Renewable Energy											
Total Renewable		278	357	468	549	278	13.1	11.4	14.6	16.1	13.1
Nuclear		18	60	136	178	210	0.08	2.0	4.3	5.2	5.8
Hydro		50	74	94	106	112	2.3	2.5	2.9	3.1	3.1
Biomass and Waste		203	200	195	196	215	10.7	6.9	6.1	5.8	6.0
Other Renewable		7	23	43	69	95	0.03	0.07	1.3	2.0	2.6

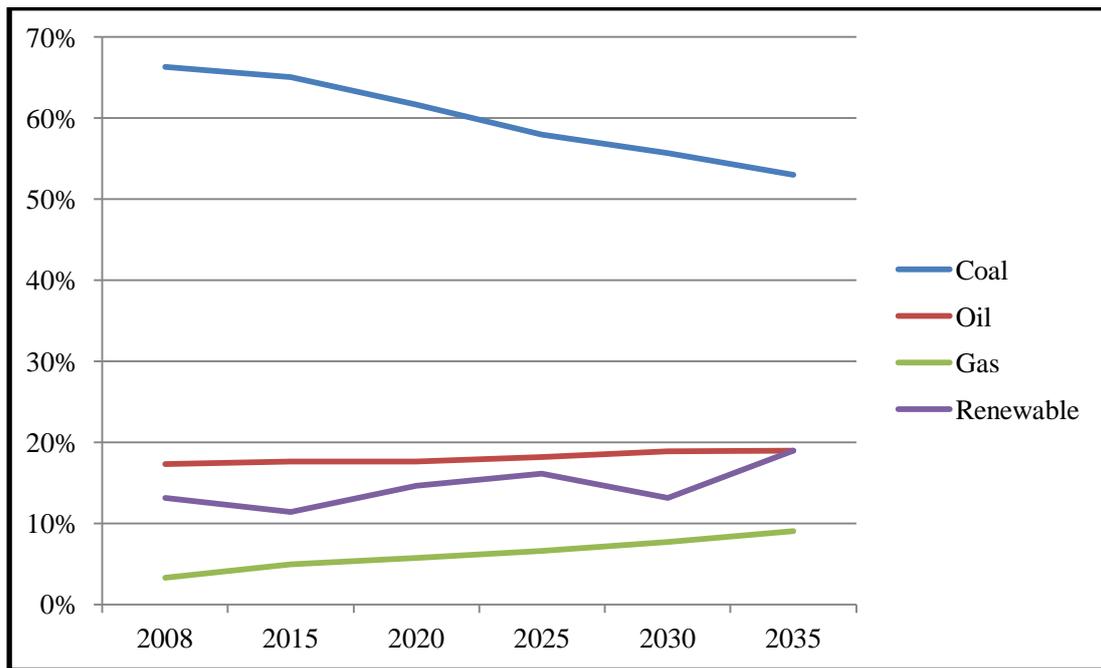
Source: World Energy Outlook 2010

(a) Percentages were calculated by the author

China's strategy to mitigate the risk associated with such a high dependence on imports includes efforts to improve energy conservation and efficiency; increased focus on domestic exploration and production; increased investments in oil and gas abroad; diversification of import sources; and the development of alternative transport fuels. The country is also investing heavily in clean energy technologies, as well as electric cars, and could become a big exporter, (Pfeifer, 2010). China aims to reduce the portion of coal in the energy mix from 70 percent to 63 percent and to increase the proportion of non-fossil fuels in overall primary energy use to 11.4 percent by 2015, (Xinhua, March 4, 2011). The target has been included in the 12th Five-Year Plan (2011-2015), (Ibid); as part of China's long plan to achieve the goal of 15 percent by 2020. Currently non-fossil fuels account for 8 percent of China's total energy consumption, (Xinhua, September 14, 2010).

Cheng Siwei, a renowned Chinese economist and a former senior legislator, estimated that China could reduce the proportion of fossil fuel (natural resources: coal, oil and natural gases, and various forms of these, such as oil shales, methane, clathrates and lignite), in its total energy mix from the current 91 percent to 85 percent in 2020, (Xinhua, 2011). But most of the decline in fossil fuels has to come from the consumption of coal. China's National Energy Administration (NEA) predicts that China's coal consumption is likely to drop to 63 percent of total energy consumption by 2015, down from 70 percent in 2010. Non-fossil fuels will provide 11 percent of China's energy needs in 2015 and 15 percent in 2020, (Xinhua, July 20, 2010) (see Figure 3.2.1.1).

(Figure 3.2.1.1): China's Energy Mix Forecast by Fuel, 2008-2030 (%)



Source: World Energy Outlook 2010

It's predicted that China's oil demand will keep rising as the country is indeed in the middle of three rapidly evolving and energy intensive transformations: Industrialisation, Urbanisation and Motorisation. Industrialisation is driven by heavy industries like steel, cement and petrochemicals, all big energy consumers, (Dirks, September 13, 2007). The pace of urbanisation is progressing rapidly each year with almost 15 million rural Chinese moving into cities. Every year, China adds a total of 2 billion square meters of building space, (Ibid). According to Tianyong Zhou, a professor at the Party School of the Central Committee of the Communist Party of China, currently, about 200 million rural residents have migrated into cities, and an additional 400 million to 500 million are going to do so, (Zhou, March 10, 2011). Around 55-60 percent of Chinese are expected to live in urban areas in 2020 (Goldman Sachs, February 2011), compared to 47 percent today (635.8 million of 1.34 billion), (UN, May 2011) and 20 percent in the 70s and 80s, (Yeo, 2010).

Additionally, McKinsey Global Institute has projected 15 “super-cities” for China with an average population of 25 million or 11 “city-clusters” each with combined populations of more than 60 million, (Ibid).

(Table 3.2.1.8): China’s Population Projections, Reference Case, 2010-2030

	2010	2015	2020	2030
Population (millions)	1,35	1,389	1,421	1,458
Urbanisation (%)	46.9	51	55	60.2

Source: World Oil Outlook 2011 and NBS

Motorisation is another major driving force for oil demand. The key forces driving China’s transport oil demand include (a) the rapid growth of road transport, (b) the dieselization of rail transport and (c) the remarkable development of domestic air transport, (Leung, February 2010). Transport consumed about 14.7 percent of oil used in 1990, but this share had risen to about 45 percent in 2010. The sector is still expanding rapidly: China overtook the U.S. in car sales in 2009, when its people bought 13.7 million cars (a 50 percent increase from 2008), rising to 17 million in 2010, (Fangfang, January 31, 2011).

(Table 3.2.1.9): Projection of China’s Vehicle Population Through 2050 (Million car)

	2010	2020	2030	2040	2050
Total	63.5	184.8	383.8	499.0	606.7
Passenger vehicles	50.1	165.8	342.8	477.8	585.4
Buses	1.13	1.86	2.28	2.46	2.65
Trucks	12.3	17.1	18.7	18.7	18.7

Source: (Hao, 2011:1351)

As road transport is fuelled overwhelmingly by oil, its rapid expansion is assumed to have contributed significantly to the increase in transport oil demand. Tianyong Zhou, a professor at the Party School of the Central Committee of the Communist Party of China, estimates that at least 60 percent of the world's newly increased oil consumption in the future will be to fuel vehicles in China, (Zhou, 2011). While Wang Fuchang, the Chinese Director of the Department of Equipment Industry under the Ministry of Industry and Information Technology, estimates that automobile ownership in China will exceed 200 million in 2020, causing serious energy security and environmental issues, (see Table 3.2.1.8). As no efficient and economical substitutes exist for diesel, gasoline and jet fuel (aviation kerosene) for transport and the military, oil is a necessity to the economy and military, therefore the oil's share in transport fuel mix in China could increase during the next decade, (World Energy Outlook 2007: 262) (see Table 3.2.1.10 below).

(Table 3.2.1.10): China's Oil Demand, (2008-2030)

In Economic Sectors, Reference Case (mb/d)					
	Level (million barrel per day)				Growth (%)
	2008	2010	2020	2035	2008- 2035
Oil Demand in Road Transportation	2.3	2.6	5.2	6.2	3.9
Oil Demand in Marine Bunkers	0.2	0.2	0.6	2.1	1.9
Oil Demand in Residential/Commercial/Agriculture Sectors	1.2	1.2	1.8	2.4	1.3
Oil Demand In other industry	2.0	2.1	2.4	2.6	0.6
Oil Demand in Domestic Waterways and Railways	0.5	0.6	1.0	1.5	0.9
Oil Demand in Aviation	0.2	0.3	0.4	0.7	0.4
Oil Demand in Petrochemicals	0.9	1.0	1.2	1.3	0.5
Oil Demand in Electricity Generation	0.2	0.2	0.2	0.1	- 0.1
Total	8.3	8.9	13.8	18.4	

Source: World Oil Outlook 2011

3.2.2 China's Oil Supply: Not Enough Any More

China produced an estimated 4.3 (mb/d) of total oil liquids in 2010, of which 96 percent was crude oil, (EIA, May 2011). China ranked as the world's fifth biggest oil producer in 2010, (see Table 3.2.2.2). China's oil output in 2010 accounted for 5.2 percent of the world's total, following Russia, Saudi Arabia and the U.S., and Iran (see Table 3.2.2.1).

(Table 3.2.2.1): Top 10 World Oil Producers, (2010, mb/d)

Rank	Country	Production	2010 share of World's Total (%)
1	Russia	10,27	12.9%
2	Saudi Arabia	10,00	12.0%
3	United States	7,51	8.7%
4	Iran	4,24	5.2%
5	China	4.07	5.2%
6	Canada	3,33	4.2%
7	Mexico	2,95	3.7%
8	United Arab Emirates	2,84	3.3%
9	Kuwait	2,50	3.1%
10	Venezuela	2,47	3.1%
	Total World	82.09	100%

Source: BP Statistical Review of World Energy (June, 2011)

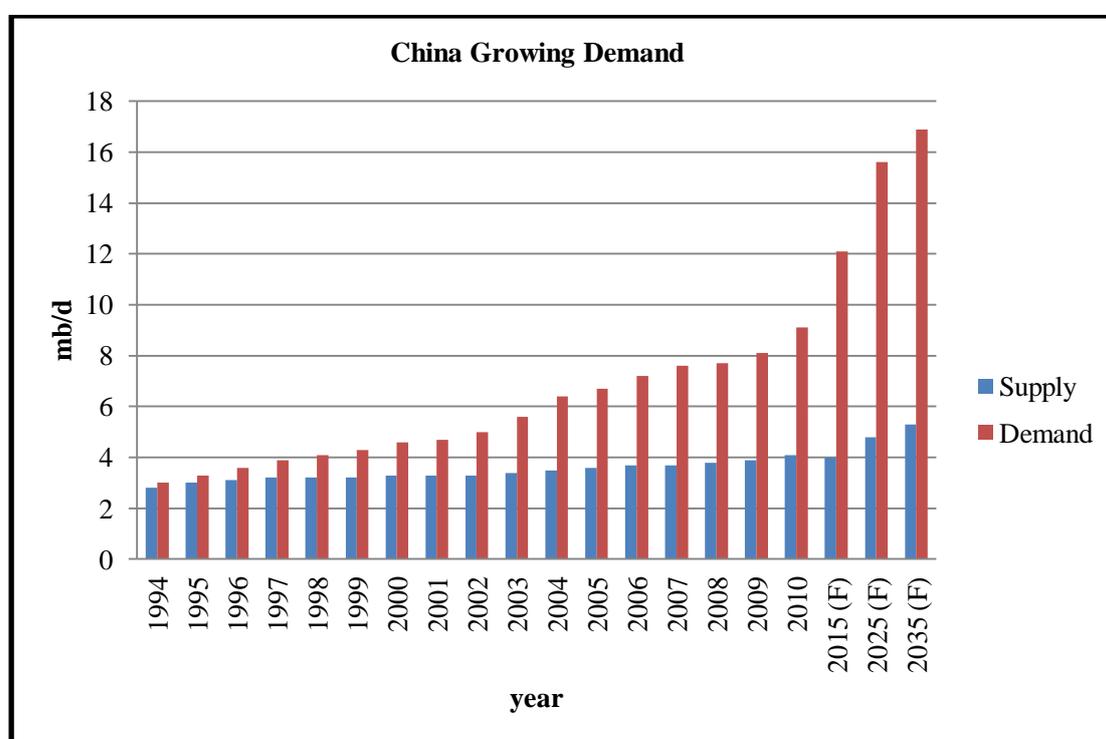
According to China's National Statistical Bureau crude oil output in 2010 hit 203.01 million tonnes, or 4.06 (mb/d), up 6.9 percent from 2009, while it warns that oil output could fall down to 190 million tonnes in 2011, (Bai, January 19, 2011). China's apparent oil demand rose by 11.1 percent to 9.1 (mb/d) in 2010 which is equivalent to over a third of global demand growth in that year, (IEA, May 12, 2011). While China's oil demand in 2011 is projected to grow 6 percent, the equivalent of 40 percent of global demand growth to 9.9, (Ibid) and oil supply will increase from 4.1 (mb/d) to 4.3. As a result, China could import around 5.6 (mb/d) in 2011, (Ibid).

(Table 3.2.2.2): China's Oil Profile (selected indicators)

	At end 1999	At end 2010	Share of World's total at end 2010 (%)
Proved Oil Reserves (m/b)	15.1	14.8	1.1%
Total Oil Production (mb/d)	3.21	4.07	5.2%
Consumption (mb/d)	4.47	9.05	10.6%
Refinery Capacities (mb/d)	5.40	10.12	11%

Source: BP Statistical Review of World Energy (June 2011)

(Figure 3.2.2.1): China's Demand Surpassed Production (1994-2035, mb/d)

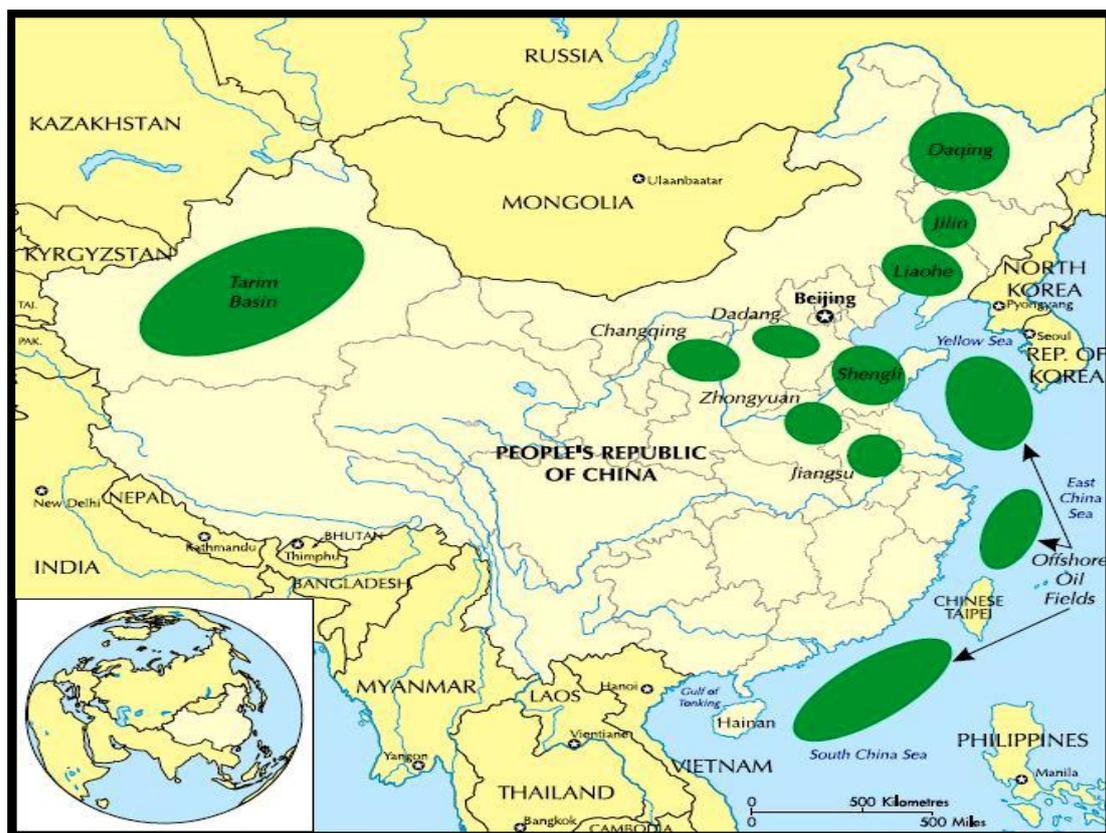


Source: IEA, May 2011 (years 1994-2010) and EIA, September 2011 (years 2015-2035)

The Chinese oil and gas sectors are dominated by the big three, China National Petroleum Corporation (CNPC), China Petroleum and Chemical Corporation, (Sinopec), and China National Offshore Oil Corporation, (CNOOC). Together they account for 88 percent of China's oil and 94 percent of gas output, (World Energy

Outlook 2007: 268). China's onshore oil reserves are mostly located in the Northeast and in Xinjiang. China's indigenous oil production rose from about 2.7 million barrels a day in 1990, (Chen, March 3, 2009), to nearly 4.06 million barrels a day in 2010 (see Figure 3.2.2.5). The newly increased demand is mainly met by imports. China's overseas equity oil production grew significantly this decade from 140,000 barrels per day in 2000 to 1.2 (mb/d) in 2009, (EIA, May 2011 May). Analysts forecast China's net overseas oil production at 1.7 (mb/d) by 2015 and 2 (mb/d) by 2020, (Dittrick, February 8, 2010).

(Figure 3.2.2.2): Map Of China Indicating Major Provinces and Oil Field

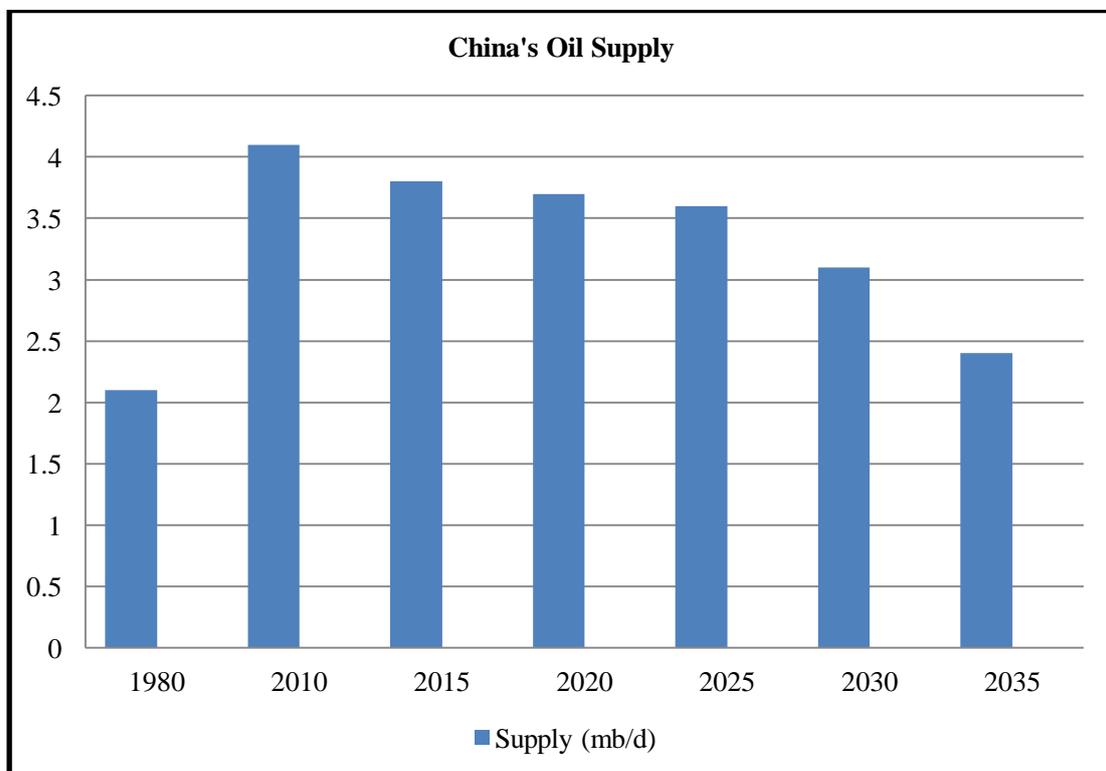


Source: Rigzone

Domestically, China relies on coal to meet nearly 70 percent of its total energy needs. Chinese policymakers clearly understand that there are good reasons to diversify

away from coal but China has limited domestic alternative supply options, (Dirks, 2007). The skyrocketing and sustained economic growth, in conjunction with a population of more than 1.3 billion people, has demanded more energy supplies. Despite the surging demand, domestic supply of oil has been a disappointment. China's domestic oil supply has failed to keep pace with demand, and the outlook for substantially increasing it is grim. China also till now has never discovered large oil reserves. Its traditional fields are old and their production is either flat or declining, (Ibid) (see figure 3.2.2.3 below). Recent projections of China's oil production for 2030 expected the production to increase from 4 million barrels per day in 2010 to 4.5 (mb/d) in 2030. There is no evidence (till now) to suggest that China's domestic oil reserves will double or triple in the next decade, thus a significant proportion of its incremental consumption will have to be met by imports.

(Figure 3.2.2.3): China's Oil Production in the New Policies Scenario (mb/d)



Source: World Energy Outlook 2010 and China's NSB (2010)

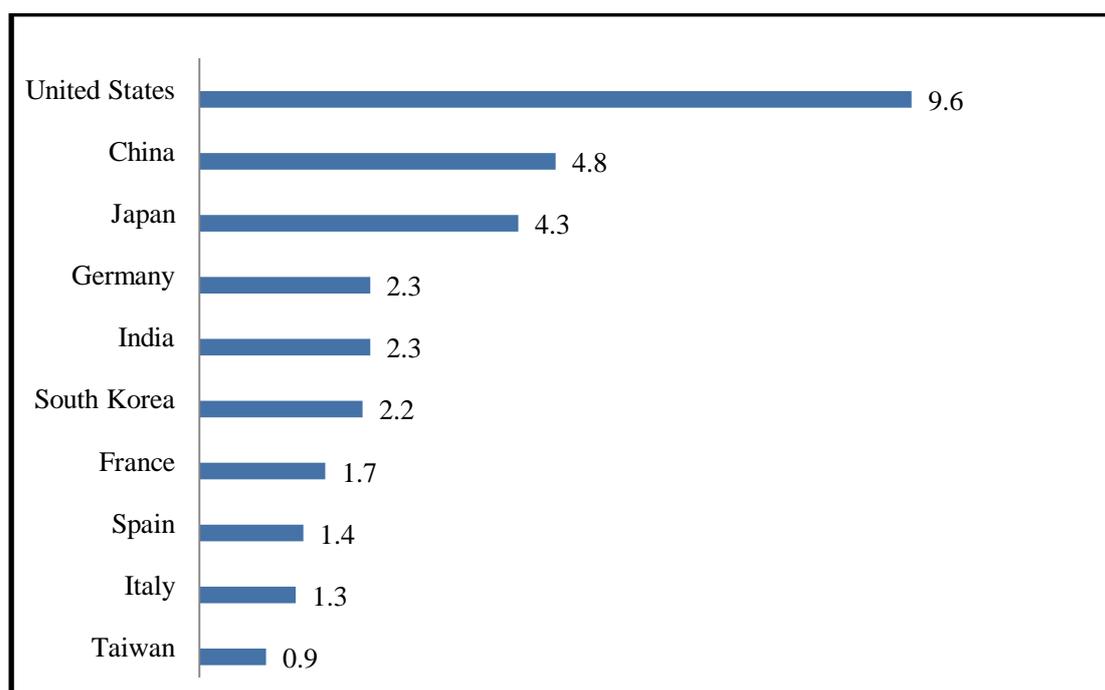
3.2.3

China's Oil Imports: Growing Appetite

Currently, China is the second largest oil importer in the world and there is every reason to believe that it will soon top the United States in consumption of foreign petroleum. China's emergence as a major oil importer has occurred both relatively recently and quite rapidly. It testifies to the nation's success in growth and development. China, the world's fastest-growing major economy, has grown 9.88 percent annually over the past 30 years. So to begin, in terms of China's oil demands and imports, it's important to note that China was self sufficient in oil as recently as 1993.

Ten years later, in 2003, China with a 5.6 (mb/d) consumption rate surpassed Japan to become the world's second largest consumer of oil, (The International Crisis Group, 2008: 2). In 2004, China became the world's third largest importer of oil behind the United States and Japan. And in 2009 Japan dropped to third place among oil importers, behind the U.S. and China, (Sato & Okada, 2010). China has made large strides in exploiting its domestic resources, but the effects of growth have outstripped those resources and led to rising net oil imports. The trend has probably become irreversible, unless large new reserves of economically-exploitable oil can be found, (IEA, 2000: 43). The widening gap between China's oil demand and domestic supply indicates that it will be increasingly dependent on imported oil (see Figure 3.2.3.1).

(Figure 3.2.3.1): Top Ten Net Oil Importers, 2010 (mb/d)



Source: EIA, Short-Term Energy Outlook (April 2011)

Since China became a net oil importer in 1993 its net import dependency soared from 7.5 percent in 1993 to around 54 percent in 2010 and about 55 percent in the first half of 2011, (Fei, 2011). The psychological 50 percent threshold made China's "energy security" an inevitable issue among the country's national press, think tanks and the authorities, (Economides, 2010). According to Lin Boqiang the director of the China Center for Energy Economic Research at Xiamen University, China's foreign oil dependency ratio, (the ratio of crude oil imports to overall oil consumption), has grown 2.8 percent annually over the last 10 years, (Boqiang, 2011). According to China's Ministry of Industry and Information Technology (MIIT), China's foreign crude oil dependency ratio in the first half of 2011 recorded about 55 percent, for the first time exceeding that of the United States, (Cai, 2011).

(Table: 3.2.3.1): China's Oil Production, Consumption and Imports, 1990-2010

	Oil Production (million metric tons) (a)	Oil Consumption (million metric tons)	Oil imports (million metric tons)	Oil Exports (million metric tons)	Net Oil Imports (million metric tons)	Net Oil Dependency (%) (b)
1980	106.0	87.6	0.4	13.3	- 12.9	- 14.7
1985	124.9	91.7	0.7	31.2	- 30.5	- 33.3
1990	138.3	114.9	7.6	31.1	- 23.5	- 20.5%
1991	141.0	123.8	12.5	29.3	-16.8	- 13.6%
1992	142.1	133.6	21.2	28.6	- 7.3	-5.5%
1993	145.2	147.2	36.2	25.1	11.1	7.5%
1994	146.1	149.5	29.0	23.8	5.2	3.5%
1995	150.1	160.6	36.7	24.5	12.2	7.6%
1996	157.3	174.3	45.4	27.0	18.4	10.6%
1997	160.7	194.1	67.9	28.2	39.7	20.5%
1998	161.0	198.2	57.4	23.3	34.1	17.2%
1999	160.0	210.7	64.8	16.4	48.4	23.0%
2000	163.0	224.4	97.5	21.7	75.8	33.8%
2001	164.0	228.4	91.2	20.5	70.7	31.0%
2002	167.0	247.9	102.7	21.4	81.3	32.8%
2003	169.3	271.3	131.9	25.4	106.5	39.3%
2004	175.9	317.0	172.9	22.4	150.5	47.5%
2005	181.4	325.3	171.6	28.9	142.8	43.9%
2006	184.8	348.8	194.5	26.3	168.3	48.2%
2007	186.3	366.5	211.4	26.6	184.8	50.4%
2008	190.4	373.2	230.2	29.5	200.7	53.8%
2009	198.8	408.3	251.5	33.1	218.4	53.5%
2010	203.01	442.3	239.3	3.3	236.01	53.4%
©						

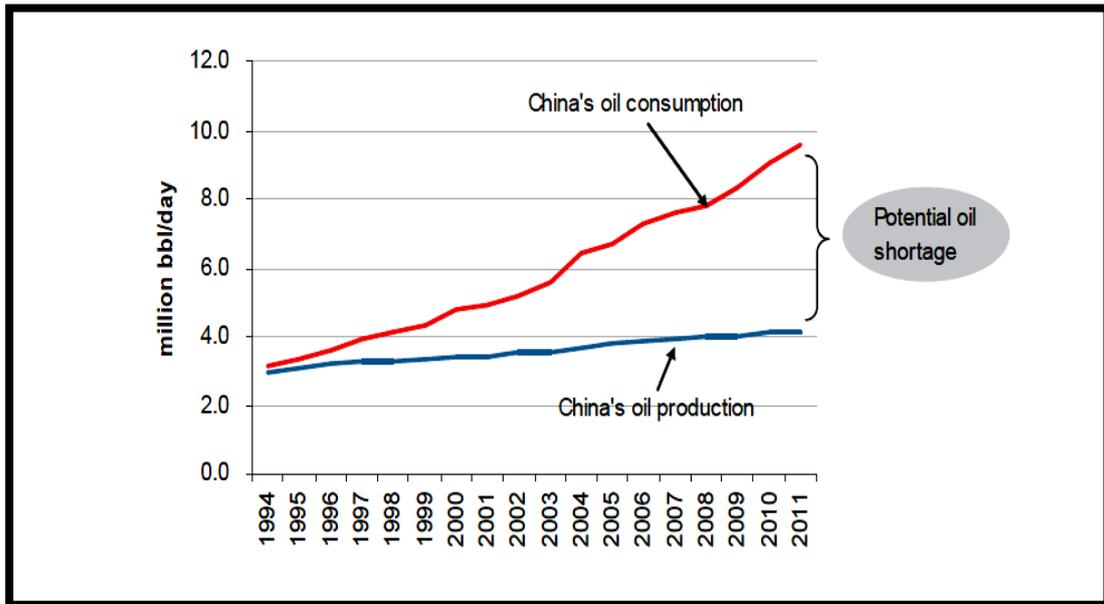
Source: China's Energy Statistical Yearbook, 2010, 2005 and 2003

- (a) One metric ton oil = 7.33 barrels of oil (Approximate conversion factors, BP Statistical Review of World Energy, June 2009)
- (b) Net oil dependency stands for the percentage of the amount of net oil imports over the amount of total oil consumption
- (c) China daily (January 21, 2011)

Indeed, China will become increasingly reliant on imports for its growing oil demand as domestic production will see no big breakthrough in the years ahead. China's production levels are expected to be near peak. There are relatively few new source projects in the inventory to offset declines in the producing base. Without significant improvements in new reserve discoveries production will begin to decline in less than

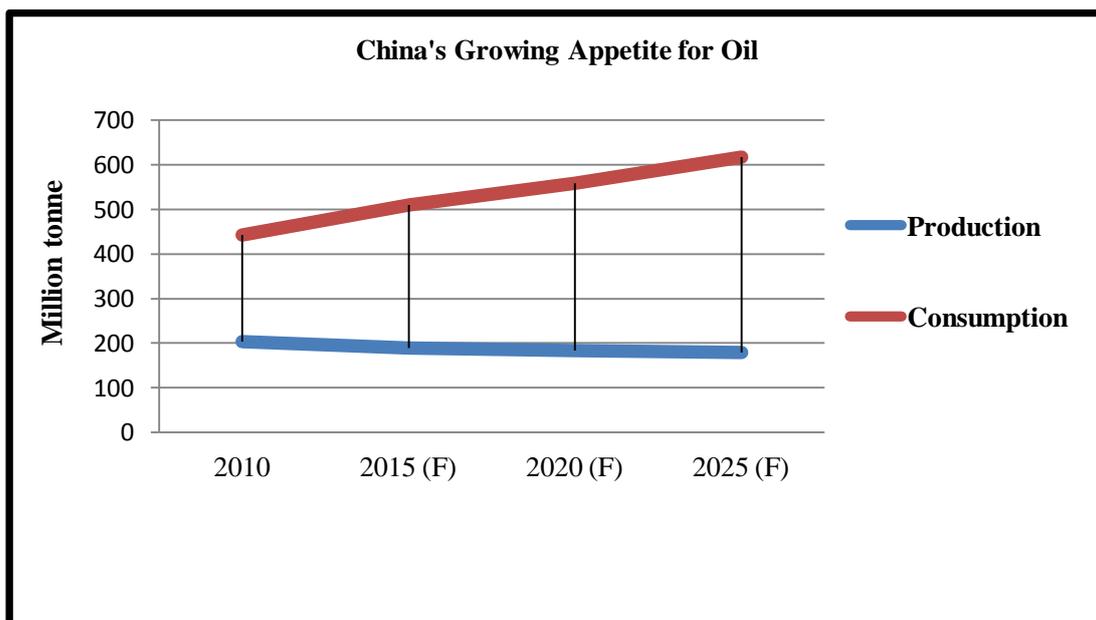
a decade. Based on future demand growth crude oil imports would have to double by the middle of the next decade (see Figure 3.2.3.2 & 3.2.3.3 below).

(Figure: 3.2.3.2): China's Current Oil Demand Supply Gap (1994-2011)



Source: EIA database

(Figure: 3.2.3.3): China's Future Oil Demand Supply Gap (2010-2025)



Source: China's Energy Statistical Yearbook 2010 and World Energy Outlook 2010; F= forecast

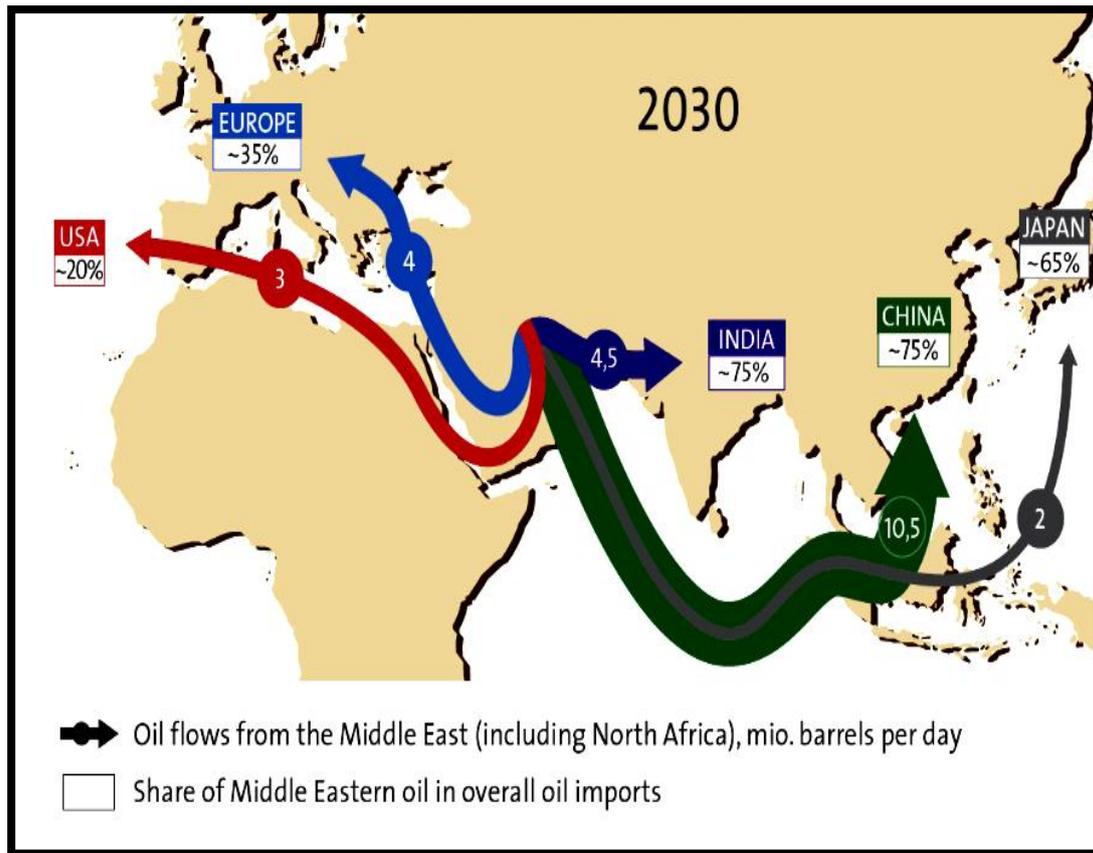
In this context, Beijing will have to rely on imports for 60-78 percent of its total oil demand by 2020-2030, (up from 54 percent now). Based on the demand and supply projections, China's oil imports are expected to increase from about 4.8 million barrels per day (mb/d) in 2010 to between 6-8 (mb/d) in 2015 and 7-11 in 2030, (see Table 3.2.3.2). This wide projected range reflects the uncertainty about China's future economic growth. Chinese and international experts expect China's oil demand and imports to continue to grow. Chinese scholars suggest that oil imports will account for 60 percent of Chinese energy needs, while the International Energy Agency believes that the figure could be higher. Ultimately, it doesn't matter how different the figures and predictions are, the fact is that China therefore will have no choice but to rely on imported oil from Middle East in particular. While analysts may quibble over the actual figure, there is consensus that the Chinese thirst for oil will only increase, (Jin, 2005: 3-10). According to the Chinese Academy of Social Sciences (CASS), 64.5 percent of the country's oil consumption is likely to be met by imports in 2020, (Wan, December 21, 2009). While IEA put the figure at 67 percent, (see Table 3.2.3.2 below). According to the International Energy Agency, by 2030 foreign supplies (mainly from the Middle East) will account for 78 percent of China's total oil consumption, and the U.S. Energy Information Administration puts it at 77 percent (World Energy Outlook 2008: 105).

(Table: 3.2.3.2): Estimates of China's Oil Imports Dependency 2010-2030, (mb/d)

	2010	2015	2020	2030
Supply	4.0	3.8	3.7	3.1
Demand	8.8	11.3	11.4	14.1
Balance	-4.8	-7.3	- 7.6	-11
Imports dependency	54%	65%	67%	78%

Source: based on World Energy Outlook 2010 (Current Policy Scenarios)

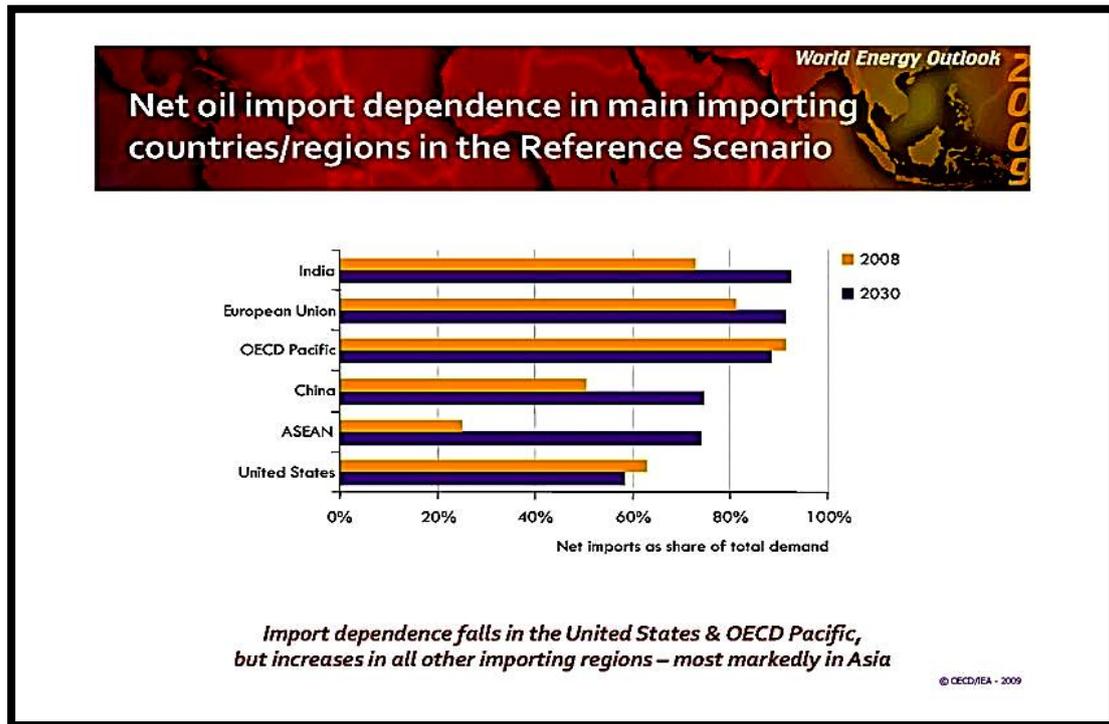
(Figure: 3.2.3.4): Oil Imports From Middle East (2030)



Source: Strategic Trends 2011 (Center for Security Studies, ETH Zurich)

China is not unique in this position and it is not the only major country that has passed the 50 percent energy security alert level, the U.S., Japan and Germany, to name a few, import on a considerable scale. Almost half of U.S. oil consumption comes from abroad, (EIA, 2011). Germany has virtually no domestic oil production and its 2.5 (mb/d) consumption relies on external supply, (Ng, 2007 and EIA, 2011). Japan for example buys 90 percent of its crude oil from the Middle East, while Singapore gets about 85 percent of its needs from the region and South Korea about 82 percent. India imports 80 percent of its crude oil needs, mostly from the Middle East, (Rook, 2011) (see Figure 3.2.2.3). This situation will definitely bring China closer to the oil consumer countries in coordinating measures to stabilise the world oil market.

(Figure: 3.2.3.5): China's Net Import Dependence 2008-2030



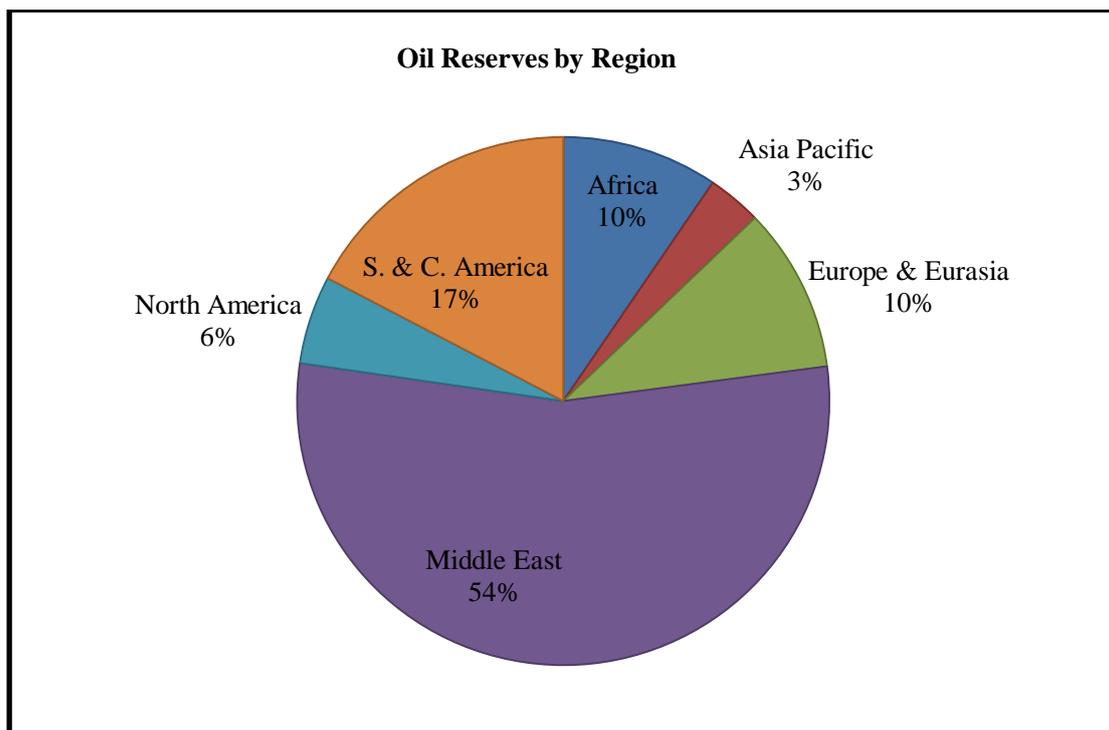
Source: World Energy Outlook, 2009

3.3 MIDDLE EAST OIL: VITAL ROLE AND FEW ALTERNATIVES

The importance of the Middle East oil cannot be over-emphasised. The Middle East is by far the well-endowed region in the world. In 2010, it held 753 billion barrels of proven reserves, (EIA, 2011). In the same year, the region produced 25.45 million barrels per day (mb/d), accounting almost 30 percent of the world's total. Unlike many other producers, the Middle East exports the bulk of its oil production, and thus the region's exports constitute more than 42 percent of the world's crude oil exports, (see Table 3.3.3). Spare capacity is concentrated in three Gulf Cooperation Council (GCC) member states of Saudi Arabia, Kuwait, and the UAE, with Saudi Arabia holding the bulk of the world's available spare capacity. This has allowed the KSA to

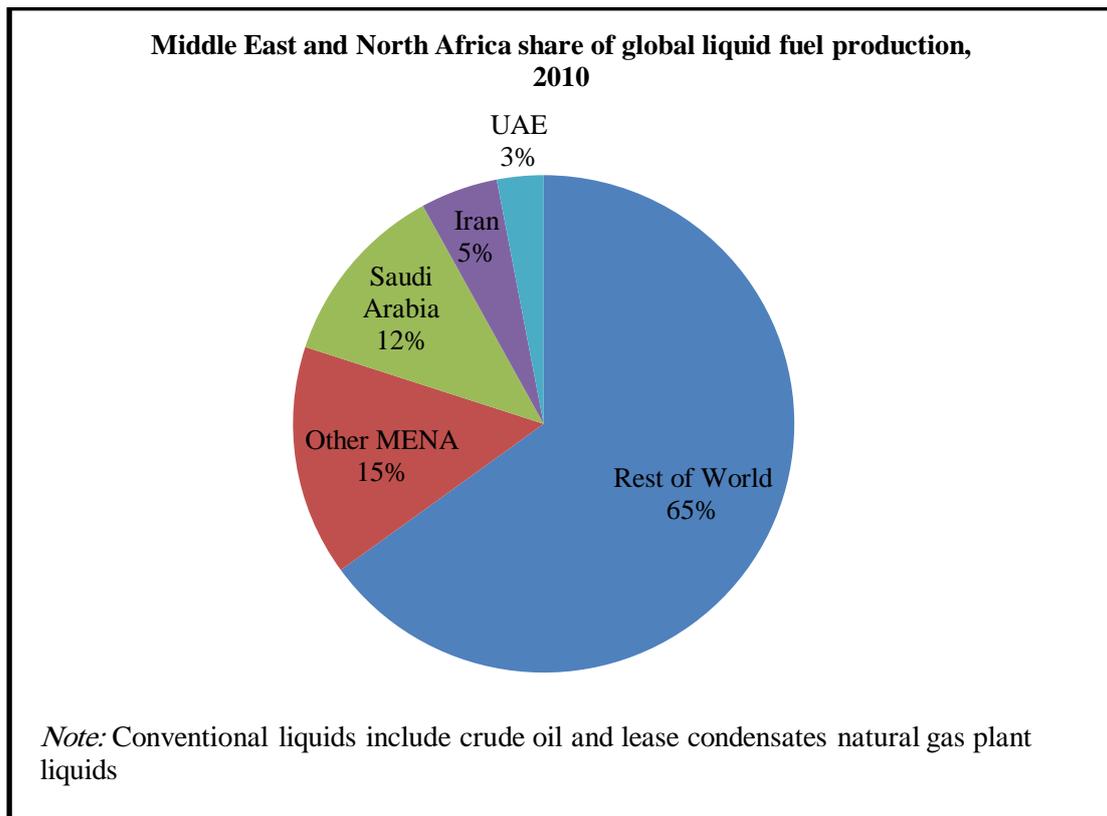
act as swing producer, filling the gap at times of supply disruptions. Finally, Oil reserves in the Middle East countries are among the cheapest to find, develop and produce in the world. The IEA estimates total production costs typically average between US\$3 and US\$5 per barrel of oil produced. This compares with over US\$15 in the North Sea and US\$12 in the Gulf of Mexico, (IEA, 2005: 133). In spite of China aggressive policy to diversify its oil imports, in 2010 nearly half of China’s oil imports was supplied by the Middle East. Growing oil imports from the Middle East since the mid-1990s can be partly attributed to China’s active oil diplomacy of targeting large oil producers, ((Lai, 2007: 519-537). As late as 1995 China’s oil imports from the Middle East primarily relied on smaller oil producers, such as Oman and Yemen. By 2003 the large producers Saudi Arabia and Iran had surpassed Oman and Yemen to become China’s top two oil suppliers, (Ibid) and since then Saudi Arabia hold the position of China’s top oil supplier.

(Figure 3.3.1): Middle East Proved Oil Reserves (at end 2010)



Source: BP Statistical Review of World Energy (June 2011)

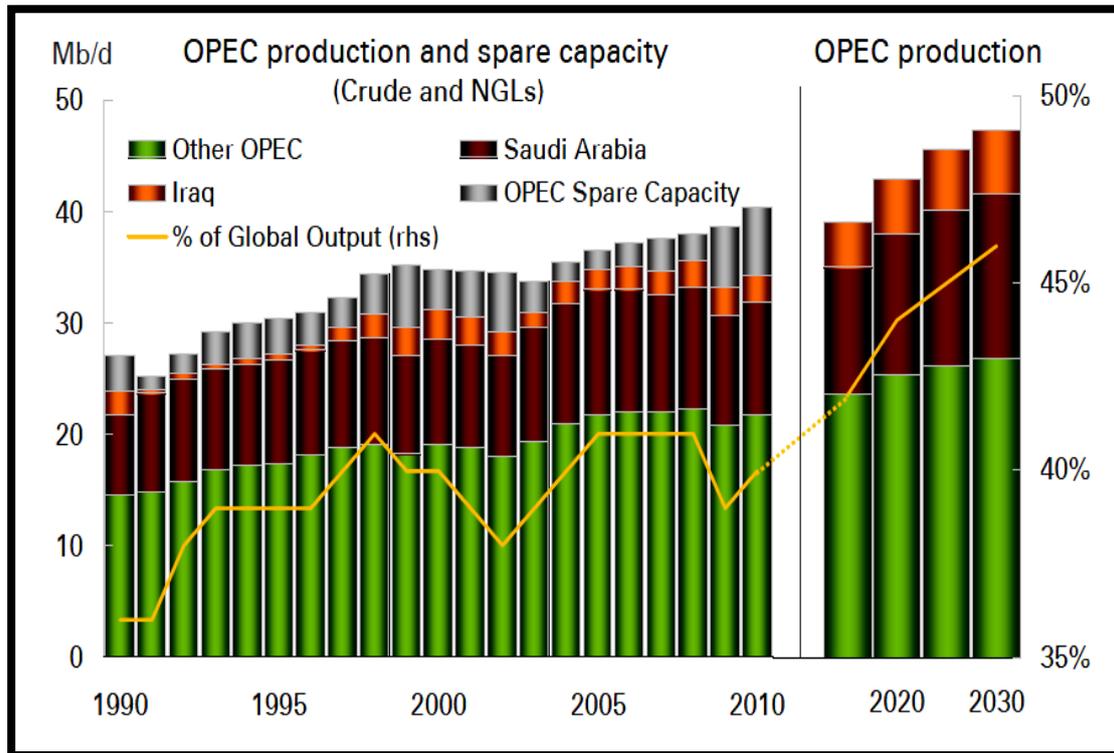
(Figure 3.3.2): Liquid Fuels Production in MENA, (at end 2010)



Source: U.S. Energy Information Administration, (March, 2011)

OPEC, which is mainly controlled by Middle Eastern countries, will see its power increase over the decades. OPEC's share in global oil production is set to increase from 41 percent currently to 46 percent by 2030, a share not seen since 1977, (BP Energy Outlook 2030, 2011:79). Projections suggest total OPEC production will rise continually through to 2035, with its share of global output increasing to 52 percent. Gains will be concentrated in Saudi Arabia, which will boost output 52 percent to 14.6 million barrels a day by 2035, (World Energy Outlook 2010: 101). By contrast, total non-OPEC oil production is broadly constant to around 2025, as rising production of NGLs and unconventional production offsets a fall in that of crude oil; thereafter, production starts to drop, (Ibid) (see Figure: Table 3.3.2).

(Figure 3.3.3): OPEC’s Critical Role in the Oil Market



Source: BP’s Energy Outlook 2030 (January 2011)

China’s appetite for oil is set to grow in the coming years and its dependence on Middle Eastern sources of energy is also set to increase, (Pant, 2008). The Middle East (excluding North Africa) holds about 54 percent of the world’s proven conventional oil reserves. The world’s proven oil reserves reach 1383.2 billion barrels, (excluding Canadian oil sands), Middle Eastern producers accounted for 54.4 percent of global reserves (752.5 billion barrels), led by Saudi Arabia with 264.5 billion barrels or about 20 percent of the world’s total, (BP’s Statistical Review of World Energy, 2011: 6).

(Table 3.3.1): Middle East Oil Production

In the New Policies Scenario (Selected indicators, mb/d and %)								
		1980	2009	2015	2020	2025	2030	2035
Total Middle East		18.5	24.8	29.6	31.3	32.8	35.2	38.1
Total OPEC	Production	25.5	33.4	38.5	40.5	42.7	46.0	49.9
	(%) of World's total	41%	41%	44%	46%	47%	49%	52%
Total non-OPEC	Production	37.1	47.7	48.2	48.2	48.2	47.4	46.1
	(%) of World's total	59%	59%	56%	54%	53%	51%	48%
Saudi Arabia		10.0	9.6	11.2	11.5	12.2	13.2	14.6
Iraq		2.6	2.5	3.6	4.8	5.3	6.1	7.0
Iran		1.5	4.3	4.7	4.8	5.0	5.1	5.3
Angola		0.2	1.8	1.5	1.6	1.7	1.5	1.4
Canada		1.7	3.2	3.8	4.0	4.5	4.9	5.3
Mexico		2.1	3.0	2.5	2.4	2.4	2.5	2.5
Caspian		0.9	2.9	3.7	4.4	5.3	5.4	5.2

Source: World Energy Outlook 2010

The Middle East also controls a significant portion of the hydrocarbons that are yet to be discovered. According to the U.S. Geological Survey, over 50 percent of the undiscovered reserves of oil and 30 percent of gas are concentrated in the region primarily in Saudi Arabia, Iran, Iraq, Kuwait, UAE, and Libya, (Gal, June 2, 2008). Additionally, the U.S. Geological Survey estimates there are some three trillion barrels of *heavy oil*³ in the world, about 100 years of global consumption at current levels, (Casselmann, May 25, 2011). It is therefore no surprise that diplomatic, economic and energy relations between China and the Middle East have been systematically deepened over the last ten years, (Andrews-Speed, July 13, 2009). Nobuo Tanaka, the Executive Director of the International Energy Agency, predicts

³ Heavy oil, which can be as thick as molasses, is harder to get out of the ground than light oil and costs more to refine into gasoline. Only a fraction of it - about 400 billion barrels - can be recovered using existing technology. Nevertheless, Saudi Arabia and Kuwait have embarked on an ambitious experiment to coax it out of the Neutral Zone.

that the global dependency on the members of the Organization of Petroleum Exporting Countries for oil (OPEC) will rise in the next five to 10 years as production by non-OPEC countries declines, and the cost of production in OPEC states is also much cheaper, (Sharma, September 3, 2010). The Middle East now supplies around half of China's oil imports. Saudi Arabia alone, in 2010, accounts for around 20 percent of this oil portion, (China Oil Web, March 1, 2011). The Middle East remains the largest and key swing supply region, (IEA, May 2011: 17). Middle East sales average 16.7 (mb/d) by 2016, and exports to non-OECD Asia rise by more than 1.7 mb/d, (Ibid) (see Table 3.3.2 below).

(Table 3.3.2): OPEC's Members Proved Oil Reserves (at end 2010)

	Country	Billion Barrels	Share of World's Total
1	Saudi Arabia	264.5	19.1%
2	Venezuela	211.2	15.3%
3	Iran	137.0	9.9%
4	Iraq	115.0	8.3%
5	Kuwait	101.5	7.3%
6	U.A.E	97.8	7.1%
7	Libya	46.4	3.3%
8	Nigeria	37.2	2.7%
9	Qatar	25.9	2.0%
10	Angola	13.5	1.0%
11	Algeria	12.2	0.9%
12	Ecuador	6.2	0.4%
Total OPEC	All Countries	1029.4	77.3%
Middle East -OPEC	Saudi Arabia, Iran, Iraq, Kuwait, U.A.E. and Qatar	741.7	53.7%
GCC - OPEC	Saudi Arabia, Kuwait, U.A.E. and Qatar	489.7	35.5%
World	All Countries	1383.2 ^a	100.0%

Source: Adapted from BP Statistical Review of World Energy (June 2011)

(a) Excluding Canada's oil sand

Within this context, China views the Middle East with great importance for four reasons. (a) The Middle East has a vast amount of oil which China desires. (b) China

realises that nearly two-thirds of the world's proven oil reserves are located in the Middle East, (Ibid). Currently over one trillion barrels are believed to be in (OPEC) Member Countries, (El-Badri, 2010). This figure will certainly increase in the future, given the under-explored status of most of OPEC's countries and the potential for increases in the ultimate recovery factors. Furthermore, China recognises that Middle Eastern nations belonging to the Organization of Petroleum Exporting Countries (OPEC) will play an increasingly vital role in supplying global energy in the future.

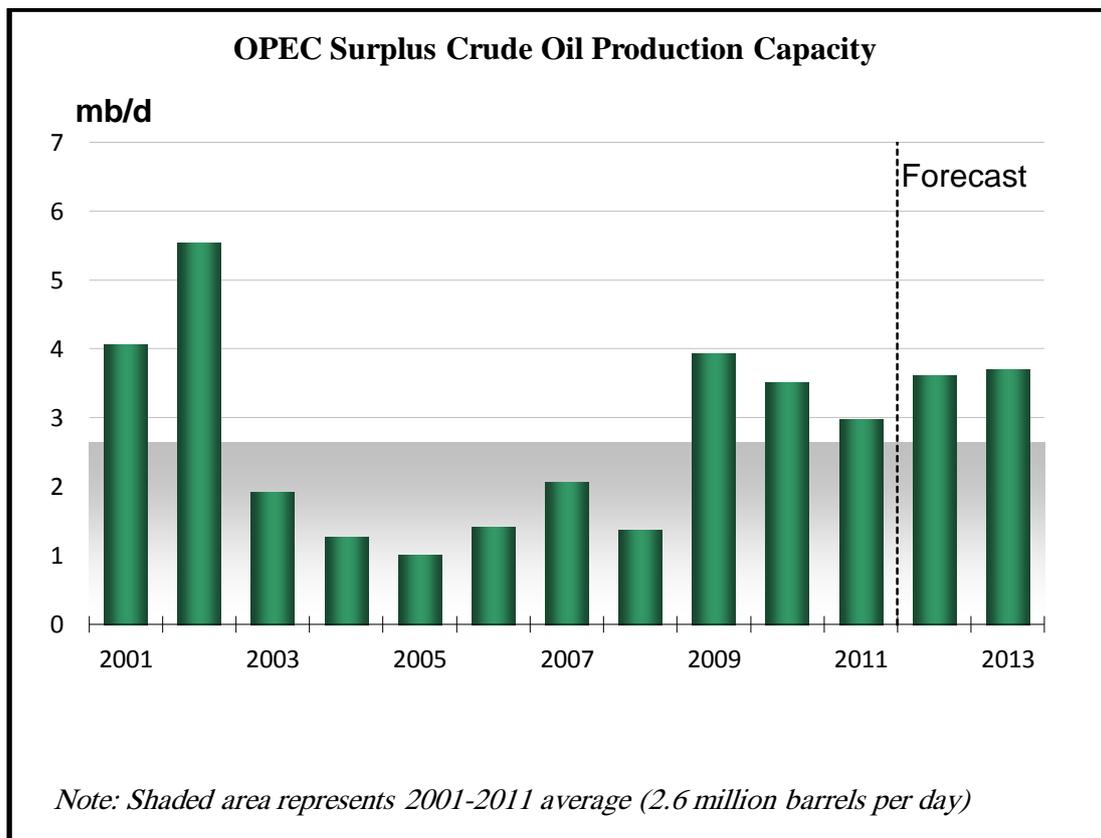
(c) The Middle East is currently the region with the lowest production cost for oil, and

(d) China can offset much of its oil costs by increasing its export of construction and labour services; export goods; and by attracting Arab Gulf investments, (Shichor, 2006: 665-683).

China is seeking to diversify its sources of crude oil toward overland sources of supply such as Russia, Central Asia and Africa, but the reality of the balance of oil reserves globally means that China has little choice but to seek new reserve access in the Middle East, (Andrews-Speed 2009: 9). If China only needed two to three million (mb/d) of oil, it might be able to purchase them from neighbours such as Russia, Kazakhstan and Asian countries, supplemented by purchases from smaller Middle Eastern and African producers. But with the huge oil imports predicted for the next decade and beyond, China is compelled to turn to the Middle East, (Ghafouri, 2009: 80-90). In this regard, Saudi Arabian Oil Minister Ali al-Naimi argues that Russia's rising crude shipments to Asian markets via the Pacific Ocean pose no threat to Middle Eastern producers' position as the largest suppliers to the region, (Alejandro, March 16, 2010). He went to highlight the importance of OPEC by saying: "We're not concerned about a blip here and there...We've got the world's highest reserves,

the world's largest production capacity -- we can compete with anyone big or small", (Ibid). Indeed, OPEC has most of the world oil spare capacity. OPEC's spare capacity now is put at anything between 6 (mb/d) (by OPEC) and 3-5 (mb/d) (by industry analysts); Saudi Arabia's share of that excess is perhaps 3-3.5 (mb/d), (The Economist, March 11, 2011) (see Figure 3.3.3).

(Figure 3.3.4): OPEC's Spare Oil Capacity, 2001-2013



Source: EIA, Short-Term Energy Outlook, (January, 2012)

The Middle East region also has other comparative advantages compared to the two other major oil producing regions, Africa and Eurasia, in terms of reliability. Most countries in the region have a strong political will to ensure stability of oil supply due to the high dependency of their economies on oil revenue. Middle Eastern oil also has

a comparative price advantage, as the average cost of lifting a barrel of oil in the regions is much lower than other regions, (Ma, June 2008) (see Table 3.3.3 below).

(Table 3.3.3): World Oil Production/Exports (mb/d)), 2001-2010

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Share of 2010 (%)
Total Oil Supply											
World	77.67	76.98	79.59	83.11	84.57	84.53	84.40	85.40	84.23	86.7	100%
OPEC	30.59	28.92	30.63	33.26	34.95	34.72	34.37	35.70	33.87	35.05	40.4%
Middle East	22.77	21.54	22.90	24.65	25.55	25.18	24.55	25.84	24.40	25.4	29.2%
Saudi Arabia	9.15	8.80	10.07	10.49	11.09	10.66	10.24	10.78	9.76	10.5	12.1%
Crude Oil Exports											
World	38.05	38.04	39.96	43.27	44.41	43.56	42.67	42.69	41.22	37.82	100% ^a
OPEC	20.40	19.41	21.03	23.46	24.96	24.56	24.09	24.77	22.73	22.77	60.2% ^b
Middle East	15.53	14.50	15.33	17.05	17.85	17.25	16.72	17.53	15.77	15.98	42.2% ^c
Saudi Arabia	6.25	5.98	6.87	7.14	7.69	7.30	6.94	7.24	6.35	6.64	17.5% ^d

Source: EIA (2011) and OPEC Annual Statistical Bulletin 2010/2011 (for a, b, c and d)

Since 2000 China has attempted to diversify sources of energy and has increased imports from Africa, Latin America, Central Asia and other regions. Yet, in 2010 almost half of China's oil imports came from the Middle East. Given the global oil reserve and production pattern and statistics, the Middle East's status as China's leading oil supplier is unlikely to change any time soon, (Zhu, May 12, 2009). In the coming years, China can perhaps moderate, but will not escape, dependence on crude oil from the Middle East, (IEA 2000: 64). According to Raja Almarzoqi Albqami, Director of the Saudi-based Institute of Diplomatic Studies, "Fifty percent of China's oil imports currently come from the Middle East region and by 2015 this share will increase to 70 percent", (EIU, May 9, 2011: 9) (see Table 3.3.4).

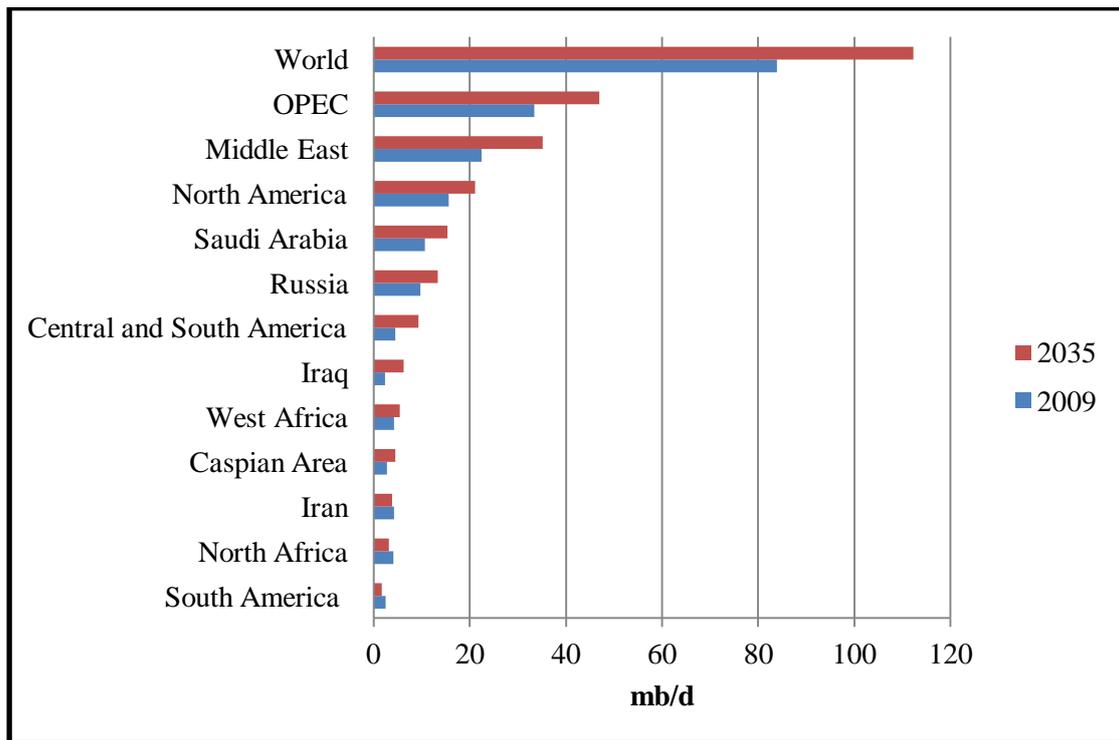
(Table 3.3.4): China's Oil Dependence on Middle East (1993-2010, million tons)

Year	China's Import from Middle East (Mt)	China's Total Import (Mt)	Middle East of China's Total Oil Imports (%)
2010	114.1	239.3	47.7
2009	97.4	203.7	47.8
2008	89.6	178.8	50.0
2007	72.7	163.1	44.5
2006	65.6	145.1	45.1
2005	59.9	127.0	47.2
2004	55.7	122.8	45.4
2003	46.3	91.1	50.8
2002	34.3	69.4	49.5
2001	33.8	60.2	56.1
2000	37.6	70.2	53.5
1999	16.9	36.6	46.1
1998	16.6	27.3	61.0
1997	16.7	35.4	47.3
1996	11.9	22.6	52.8
1995	7.7	17.0	45.4
1994	4.9	12.3	39.7
1993	6.5	15.6	42.1
Average 1993-2010 (%)			48.4

Source: China's Energy Statistical Yearbook, various years

The vital role of the Middle East in China's energy strategy is due to their cordial economic and political relationship, the advantages of the region as an oil supplier, and the difficulty for China to substitute Middle East oil by other sources. Taking into consideration global oil distribution, producing capacity, supply potential, import costs and other factors, most of China's future oil imports, accounting for more than half of the total, will have to come from the Middle East and North Africa particularly from the Arab Gulf States, (John, 2007). China has no near term substitute for Middle Eastern oil. It is no secret that even as China is attempting to diversify its foreign sources of energy, the Middle East remains a key supplier of the oil that China depends upon to sustain its continuous economic growth, (Jiang, 2007: 12-15) (see Figure 3.3.3).

(Figure 3.3.5): Oil Production by Country and Region, 2008 and 2035



Source: International Energy Outlook 2011 (September, 2011)

In this regard, the Economist Intelligence Unit (EIU) predicts that the world's dependence on GCC oil and gas will rise between now and 2020. Most of the increases in oil supply are expected to come from the Middle East, which has the bulk of the world's proven reserves and relatively low production costs, (EIU, March 2009). Much will come from the GCC; Iraq and Iran have significant long-term output potential but their development will be hampered by political factors, (Ibid). The scope for non-OPEC supply growth appears to be limited. Large new projects (in Brazil and Kazakhstan among others) will be partly offset by falling production in maturing fields (for instance in Mexico and the UK), (Ibid). Finally, there are expectations that unconventional oil (shale rock, oil sands, and heavy oil formations) production will rise rapidly in the U.S., Canada and South America over the next decade. Taking into consideration the timetable, producing capacity, supply potential,

import costs and other factors the Middle East will still be dominant in years or maybe decades to come.

For example, non-OPEC supply, including non-conventional, bio-fuels and NGLs, will likely peak by 2011 at around 52.3 (mb/d). Thereafter, we see steady declines in production, reaching 51 million (mb/d) by 2015. As a result, reliance on OPEC crude will only grow from now to 2015. In contrast OPEC oil supply will increase from over 34 (mb/d) in 2009 to around 43 (mb/d) in 2015, (Bank of America Merrill Lynch, February 16, 2010). OPEC plans to add 12 million barrels to its daily production capacity by 2015, equal to Saudi Arabia's current capacity. Global oil demand is expected to advance 1 percent a year to 105 million barrels a day by 2030 from over 87 million barrels a day in 2010. Most of the increase in output would need to come from OPEC countries, which hold the bulk of remaining recoverable conventional oil resources. OPEC's oil production is expected to increase 1.8 percent a year through 2030 to 53.8 million barrels a day. The group's share of global oil output is forecast to rise to 52 percent, (Martinez, 2010).

Abdullah El-Badri, OPEC's Secretary-General, told the *Financial Times* recently: "OPEC's member countries now have a total of 150 projects under development, which would add about 12 (mb/d) of oil-production capacity by 2014...We base our projection not mainly on OECD countries: 80 percent of the growth that we see in the future will come from India and China, and the Middle East and Asia as a whole", (Hoyos, March 30, 2010). He noted that demand from developed nations would shrink by 4.4 (mb/d) and that growth in Asian demand would be almost the same amount. "Really the world is going east as we see it. Whatever the decline in OECD

countries is, it is picking up in Asia”, (Ibid). Indeed, China’s share of total global oil consumption is forecast to increase from 10 percent today to 16 percent (see Table 3.2.1.4). The largest volumes of exports are likely to come from the Middle East. Some forecasts envisage China’s reliance on Middle East oil (see Table 3.3.5) reaching as high as 70 percent of net import by 2015, (Ma, 2008).

(Table 3.3.5): World Total Liquids Production by Region and Country

Reference Case, 2008-2035							
	2008	2015	2020	2025	2030	2035	Average Annual Percent Change, 2008-2035
OPEC	35.6	38.6	40.8	43.1	45.0	46.9	1.0
Middle East	24.2	27.0	28.9	31.2	33.3	35.2	1.4
Iran	4.2	4.0	3.8	3.7	3.8	3.9	-0.3-
Iraq	2.4	2.9	3.6	4.5	5.5	6.3	3.7
Kuwait	2.7	3.0	3.1	3.3	3.7	4.0	1.4
Qatar	1.2	1.9	2.1	2.3	2.5	2.5	2.7
Saudi Arabia	10.7	11.6	12.8	13.9	14.6	15.4	1.4
United Arab Emirates	3.0	3.6	3.5	3.5	3.3	3.2	0.2
North Africa	4.1	3.5	3.4	3.4	3.3	3.2	-0.9-
Algeria	2.2	2.6	2.7	2.6	2.5	2.3	0.3
Libya	1.9	0.9	0.7	0.7	0.8	0.8	-3.0-
West Africa	4.2	5.3	5.5	5.5	5.4	5.4	1.0
South America	3.1	2.9	3.0	3.0	3.0	3.1	-0.1-
Non-OPEC	50.0	54.7	56.8	60.1	63.0	65.3	1.0
Russia	9.8	10.8	11.4	12.2	12.8	13.3	1.1
Caspian Area	2.6	3.5	3.8	4.2	4.4	4.5	2.1
China	4.0	4.0	4.2	4.8	5.2	5.3	1.0
Middle East (Non-OPEC)	1.5	1.6	1.4	1.3	1.1	1.1	-1.3-
Africa	2.7	3.0	3.2	3.4	3.5	3.5	1.0
Central and South America	4.3	6.2	7.2	8.1	8.9	9.4	3.0
Total world	85.7	93.3	97.6	103.2	108.0	112.2	1.0
Middle East share of world production^a	27.2%	28.3%	26.8%	28.9%	29.6%	30.2%	
Arabian/Persian Gulf share of world production	27%	28%	27%	29%	30%	30%	

Note: Conventional liquids include crude oil and lease condensates natural gas plant liquids and refinery gains
(a) All percentages were calculated by the author

Source: International Energy Outlook (September 2011)

3.4 CONCLUSION

This chapter has attempted to decipher Chinese intentions towards the Middle East. The main question it attempted to address was whether Chinese actions are primarily guided by economic imperatives or a political agenda. This chapter has shown that China's oil policy toward the Middle East is primarily driven by economic imperatives. Among these imperatives, China's need for oil is the most important. China is seeking to diversify its sources of crude oil toward overland sources of supply such as Russia, Central Asia and Africa.

However, the reality of the balance of oil reserves, production and exports globally means that China has little choice but to seek new reserve access in the Middle East. This chapter has also shown that the Middle East region has particular significance for China in meeting its energy needs. The orientation of China's oil policy towards the Middle East, both in terms of timing or location fits with the economic interdependence theory as China realises that its ability to meet its future energy demands strongly hinges mostly on the Middle East region. China has no near term substitute for Middle Eastern oil, given that its own oil fields are almost fully exploited. As for the future, this study expects Saudi Arabia (and the Middle East) to play a major role in meeting Chinese demand for oil the next two decades.

CHAPTER FOUR

STRATEGIC AND POLITICAL FOUNDATIONS OF CHINA-SAUDI RELATIONS

4.1 INTRODUCTION

China and Saudi Arabia cherish a long tradition of friendship, and the two peoples started contacts quite early. The *Prophet Mohammed* is said to have advised Muslims to, seek knowledge even unto China. This famous remark of the Prophet of Islam both affirmed the value of Chinese culture and ties between the two countries and encouraged later generations to continually strengthen contacts, (Liu 2006). In 650 CE, the Muslim Caliph Uthman Ibn Affan sent one of the companions of the *Prophet Mohammed* as an emissary to the newly established Tang Dynasty. That date marks the beginning of Islam in China. Ever since, Muslims have played a prominent role in Chinese society, (Freeman, 2011).

Contemporarily, the political relations between China and Saudi Arabia date to the mid-30s and 40s of the last century. These relations were stopped after the founding of communist China in 1949. However, after China's opening up to the outside world in 1979, despite the absence of diplomatic relations, unofficial ties between the two countries have been developed in three directions. At the beginning came resuming the Chinese Muslims *Hajj* (pilgrims) to Makkah at the end of the seventies, then economically through the entry of Chinese goods to the Saudi market at the beginning

of the eighties, and finally militarily by providing Saudi Arabia with long-term missiles in the second half of the eighties. Relations later developed further to peak in 1990 after the resumption of formal diplomatic relations.

This chapter attempts to provide a historical and political background of Chinese behaviour towards Saudi Arabia and to decipher whether China's actions were based on economic interests or a political agenda to undermine the American influence.

4.2 HISTORICAL PERSPECTIVE

In recent history Saudi Arabia's diplomatic relations with China span back to 1939, when the Kingdom was the first Arab country to normalise its political ties with China. Also, Saudi Arabia was the first Arab country to support the Chinese people's struggle against the invasion of Japan as some sources claim that the Saudi King Abdul Aziz met with a political delegation of China's Muslims in 1937 and expressed sympathy and support to the cause of the Chinese people against the threat of Japan, (Jafar, 1999). The relationship came even closer, when the two countries signed the treaty of amity in Jeddah, on November 15, 1946.

His EXCELLENCY THE PRESIDENT OF THE NATIONAL GOVERNMENT OF THE REPUBLIC OF CHINA, on the one hand, and His MAJESTY THE KING OF SAUDI ARABIA, on the other hand, Animated by the desire to establish and to consolidate the bonds of friendship and good understanding between their respective countries, have resolved to conclude a Treaty of Amity and have for this purpose appointed as their Plenipotentiaries: His Excellency the President of the National Government of the Republic of China: His Excellency Mr. Cheng Ye-tung, Ambassador Extraordinary and Plenipotentiary of the Republic of China to Iran; His Majesty the King of Saudi Arabia: His Excellency Sheikh Youssif Yasseen, Acting Foreign Minister of Saudi Arabia, Who, having communicated their Full Powers, found in good and due form, have agreed as follows:

Article I: There shall be perpetual peace and amity between the Republic of China and the Kingdom of Saudi Arabia as well as between their peoples.

Article II: The High Contracting Parties agree to establish diplomatic relations between the two States in conformity with the principles of Public International Law. They also agree that diplomatic representatives of each State shall enjoy, on the basis of reciprocity, in the territory of the other, the treatment recognized by the general principles of Public International Law...”, (United Nations Treaty Series Online Collection, 1946).

The relations continued until the Chinese Communist Party (CCP) seized power in China in 1949, and the diplomatic relations between the two countries was broken off, (Jafar, 1999). Despite the absence of diplomatic relations, unofficial meetings between China and Saudi Arabia continued and date back to 1950s, through the so-called “Hajj diplomacy.” For example, with the support of their government, Chinese Muslims, in 1952, organised the first Hajj team of 16 people. Subsequently, China sent Muslims every year to Saudi Arabia for *Hajj* (pilgrimage). The *Hajj* was suspended for a period of time during the Chinese Cultural Revolution in the 60s and 70s, but China resumed the *Hajj* activities after the open-up policy, (see Table 4.2.1).

In this regard, Chinese Scholar Wu Bingbing noted that China’s Gulf policy has witnessed six phases since the late 1950s: (1) a focus on Iraq (1958-1967); (2) a focus on revolutionary movements in the Gulf (1967-1971); (3) opposition to Soviet expansionism (1971-1979); (4) a focus on Iran and Iraq (1979-1990); (5) a focus on Iran (1990-2001); and (6) a focus on Saudi Arabia and Iran (2001 till now), (Wu, 2011: 10). Although Saudi Arabia is still playing a pivotal role in Beijing’s strategy in the Middle East, China started to pay attention to the Arab countries in general, especially with the changes or the so-called Arab Spring that swept the Middle East and North Africa in 2011.

(Table 4.2.1): Timeline of Contacts between China and Saudi Arabia (1949-1990)

Year	Place	Notes
1952	China & Saudi Arabia	Chinese Muslim organised the first Hajj team of 16 people
1955-1964	China & Saudi Arabia	China sent Muslims every year to Saudi Arabia for Hajj (pilgrimage). The pilgrimage was suspended for a period of time.
1979	China	China resumed the pilgrimage activities.
1981	Cancun, Mexico	<ul style="list-style-type: none"> - Chinese Premier Zhao Ziyang shook hands with Crown Prince Fahd at the North- South conference. - Unconfirmed reports that Saudi prince made unannounced visit to China.
1985	Oman	<ul style="list-style-type: none"> - Chinese Vice-Premier Yao Yilin initiated a conversation with Crown Prince Abdullah. - Saudi Arabia began negotiating to purchase the missiles from Beijing in 1985 after it became apparent that the U.S. would be prevented by congressional opposition from selling Saudi Arabia up to 48 F15 jet fighters.
1986	Washington DC	U.S. Congress rejected selling missiles to Saudi Arabia.
1987	Saudi Arabia	The first major envoy of Chinese entrepreneurs visited Saudi Arabia. Headed by Jia Shi, President of the China Council for Promotion of International Trade, the delegation met with the Second Deputy Prime Minister Prince Sultan, and negotiated for increased Sino-Saudi economic collaboration.
1988	Washington, D.C	<ul style="list-style-type: none"> - Chinese and Saudi ambassadors to the United States, Han Xu and Prince Bandar respectively, signed on November 11, 1988 a memorandum of understanding in Washington, D.C. stating their intention to establish “commercial representative offices”, creating the first permanent representative bodies between the two nations. - On April 6 Xinhua published a statement by Chinese Foreign Minister Wu Xueqian confirming China’s sale of CSS-2 model ground-to-ground missiles to Saudi Arabia.
1989	Beijing	China appointed as its first representative Arabic-fluent businessman Deng Shaoqin.
1990	China and Saudi Arabia established diplomatic relations	<ul style="list-style-type: none"> - Saudi Ambassador to the United States Prince Bandar travelled to Beijing on July 9, 1990. - Saudi Arabia’s Minister of Industry and Electricity visited Taipei where he delivered a letter requesting to downgrade their embassies to “representative offices.” - Chinese Foreign Minister Qian Qichen travelled to Riyadh on July 20, 1990, and on July 21 the nations issued a joint communiqué announcing official recognition of each other’s governments.

Source: adapted by the author from various media reports

4.2.1 The Islamic Dimension

In 1955, when the Bandung International Conference of Non-Aligned Countries was convened in Indonesia, the late Chinese Premier Zhou Enlai met with Saudi Crown Prince (and the future King) Faisal at that time, (China Radio International, 2010), and discussed with him the *Hajj* (pilgrimage) of Muslim Chinese. In the meeting Prince Faisal agreed to allow Chinese Muslims to make the pilgrimage to Makkah. In the same year, a 20-member Chinese team, which included famous Chinese Muslims Da Pusheng and Ma Yuhuai, accomplished their mission, (Yong, 2010). Between 1955 and 1964, the China Islamic Association organised 10 Hajj trips to Makkah. From 1955 to 1964, China sent Muslims every year to Saudi Arabia for Hajj. A few dozen did so every year until 1966, (Gresh, 2010).

The *Hajj* was suspended during China's Cultural Revolution between 1966 and 1976.⁴ Relations deteriorated further when Riyadh established diplomatic relations with Taipei (Taiwan), and took an active part, in the 1960s and 1970s, in the World Anti-Communist League founded by Chiang Kai-shek, (Gresh, 2010). Fourteen years later the *Hajj* visits resumed, on October 19, 1979, the Chinese Muslim Delegation with Zhang Jie as president went to Makkah for *Hajj*. Ties were also set by the Peking leadership to a delegation of Chinese Muslims who visited Saudi Arabia in November 1979, (Shoujiang and Jia, 2004). The number of the *Hajjis* has grown considerably from 2,200 in 1985, then exceeded 6,000 in the 1990s, and by 2009 had ballooned to over 12,700, (China View, 2009) to reach 13,500 in 2010, (Yong, 2010).

⁴ Between 1966 and 1976, Chinese leader Mao Zedong implemented the "Cultural Revolution," 10-year political and ideological campaign aimed at reviving revolutionary spirit, producing massive social, economic and political upheaval.

This initial exchange established a pattern of interaction based on Islamic cultural similarities. The annual Chinese *Hajj* came to include prominent Chinese officials, notably local government officials from the Ningxia Hui and Xinjiang Uyghur autonomous regions, both of which possess large Muslim populations. Such pilgrims pursued political missions as well, gaining audiences with high-ranking Saudi officials.

Indeed, in 1984, King Fahd granted an audience to Ilyas Shen Xiaxi, Vice-President of the China Islamic Association (CIA), and extended an invitation for larger future pilgrimages. China responded by sending thousands to Makkah in 1985, (Anderson, 2004). Greater freedom of travel was also given to Chinese Muslims, businessmen and students, facilitating an exchange of trade and ideas between the two communities. Funds from Saudi Arabia and other Arab nations funnelled into Muslim regions, financing the construction of mosques, the purchase of the *Holy Qur'an*, and scholarships for study abroad, (Ibid). The greatest sign of an increasingly friendly Sino-Saudi dialogue over Islam came in 1987, when the Saudi-sponsored Muslim World Association (MWA) coordinated with the China Islamic Association (CIA) to hold a five-day conference of three hundred Muslim leaders in Beijing. Extensively covered in the Chinese and Saudi press, it underlined China's new role in the Muslim community, (Ibid).

There are no doubts that these missions provided a link between the two countries and demonstrated to some extent China's tolerance of the Islamic religion, (Harris, 1981), and helped to lay the foundations for establishing the diplomatic relations between the two countries a few years later.

4.2.2 Pursuing Diplomatic Relations

After the Communist Revolution, China and Saudi Arabia had conflicting interests in various fields including political and economic development. The Saudi policy was allied with the West in the fight against communism, while China adopted the support of revolutionary forces in the region. China did seek to generate anti-colonial sentiment in the region in the 1950s and 1960s and this was mainly in the context of supporting the Arab countries in winning and preserving their independence in the struggle against “imperialism” and “colonialism”, (Li, 2009). In addition, China was seeking to check Moscow influence in the 1970s. It was not until the late 1970s and 1980s that Beijing, in conjunction with its broader political opening to the world, started to become more seriously involved in the Middle East, (Yetiv, 2009: 199-218).

In the early years of the Cold War, China attempted to export its brand of revolutionary communism throughout the *Third World*, including the Middle East which was seen as a potentially fertile ground for radical ideologies. However, already by the late 1960s, it became clear that this was not a sustainable policy as it was deflecting attention from China’s primary goal of economic development, (Pant, 2008). Later in the 70s, China entered a “strategic partnership” with the United States against the Soviet Union, and embarked upon an “open up” policy. As a result, China’s bilateral relations expanded both in number and complexity. China’s interest and involvement in the Gulf during the 1970s reflected these general trends, (Calabrese, 1992: 471-485). A set of substantive and tangible interests gradually have dominated China’s Middle East policy since the 1980s. Among these interests, the quest for oil is the most important one, followed by strengthening economic relations

with the Middle East and arms sales, (Yetiv and Lu, 2007). After the end of the Cold War, China fundamentally altered its internal and external strategies; internally Beijing's focus shifted to economic and social development, and externally the government focused on maintaining world peace and promoting global development and cooperation, (Li, 2009).

Concerted efforts on the part of China to improve its relations with Saudi Arabia began in 1978. China was motivated by a number of factors to continue to push towards improving relations with the Arabian Kingdom. Seeking to balance Soviet power, China saw relations with Saudi Arabia as a positive step in securing the Gulf region, (Anderson, 2004). China's balancing efforts focused on Iran and Egypt throughout the 1970s; the Chinese had been "walking on two legs" in the Middle East. One "leg" was the Shah of Iran; the other, President Sadat of Egypt. China decided to renew its relations with Saudi Arabia in the early 1980s, while the alliance between Beijing and Washington was strengthening, and again it used "hajj diplomacy" or as Yitzhak Shichor puts it: "The Chinese wanted to kill two birds with one stone: they wanted to show their Muslim population that they were not against religion, and they wanted to get closer to Saudi Arabia, (Gresh, 2010).

After the fall of the Shah in late 70s and the assassination of Egyptian president Anwar Sadat in 1981, the Chinese began to look for an alternative plan, as well as for an alternative ally. Both could be offered by Saudi Arabia, (Shichor, 1982: 101-110). The Saudi hostility to the Soviet Union converged with China's principal interest in the Middle East. Yet, unlike both Egypt and Iran, Saudi Arabia seems to have enough leverage to influence American policies in the region. As the undisputed centre of

Islam and the supreme distributor of funds, Riyadh has been respected by most of the Arabs, moderate as well as radical. In addition, the Saudis' moderate stand on oil prices, though serving their own interests as well, is intended to minimise the difficulties for Japan and the West, a policy which the Chinese of course appreciate, (Ibid). In addition, China saw in Saudi Arabia a chance to gain further legitimacy by urging Gulf nations to shift diplomatic recognition to Beijing away from Taiwan, (Ibid). Finally, trade with Saudi Arabia was an obvious step towards improving trade with the region, providing a desirable market for Chinese goods. For these and other reasons, China developed an ambitious agenda to improve Sino-Saudi relations throughout the 1980s, consisting of the following phases: the demonstration of common interests, utilization of Muslim identity, development of trade ties, and support of Saudi Arabia's security efforts, (Anderson, 2004).

Initial forays towards diplomatic relations with Saudi Arabia were made through Kuwait (Kuwait established diplomatic relations with China in 1971), whom China sought to use as a mediator towards improving the relations with Saudi Arabia. While these largely failed, yielding no new official dialogue between China and Saudi Arabia, Beijing continued urging Kuwait to work towards improving relations with Saudi Arabia, on the basis of China's support for the Palestinian cause, (Ibid). While this concerted diplomatic pressure gained minor concessions from Saudi Arabia, namely their allowance of minor amounts of indirect trade, its failure to secure improved relations led China to amplify efforts towards a common agenda. Chinese periodicals began to grant increased attention to Saudi affairs, lauding Saudi efforts to build up unity among the Gulf countries, bring about a ceasefire in Lebanon, and resolve the Soviet presence in Afghanistan, (Ibid). Beijing has made persistent efforts

to impress upon Riyadh their common interest in preventing Soviet dominance in the Gulf. The Saudis have, however, remained adamant in their refusal to establish diplomatic relations with Beijing, (Harris, 1980).

Following the assassination of the Egyptian president Anwar Sadat in 1981, Chinese support swung away from the Camp David agreements between Egypt and Israel towards Saudi Crown Prince Fahd's eight-point peace plan⁵, praising it as "genuine, comprehensive, fair, realistic and concrete." Through such efforts, analyst John Calabrese maintains, "China gradually built a reputation as a supportive rather than a subversive force in the region", (Calabrese, 1992). China was rewarded for its efforts by a growing Sino-Saudi dialogue. In 1981, Chinese Premier Zhao Ziyang shook hands with Crown Prince Fahd at the North-South conference held in Cancun, Mexico, and pursued talks that were later described by Chinese officials as "very productive" and "quite fruitful", (Ibid). Arab diplomats in Beijing also reaffirmed that Saudi Chinese negotiations to establish formal relations had already begun, (Ibid).

On May 27, 1981, just two days after the Gulf Cooperation Council (GCC), was formed, China established diplomatic ties with it, (Ibid). Significantly, in 1983 China began to import crude oil from Oman as a temporary measure, in order to alleviate the problem of transporting its own oil from its northern provinces to refineries on the Yangtze River, (Ghafour, 2009: 82-93). Two years later, the first Sino-Saudi official meeting took place in Oman in November 1985, following several years of heightened contact between the two countries, (Yetiv, 2007). At a second meeting between high-level Chinese and Saudi officials in Oman in 1985, the then Chinese

⁵ For more details about the plan see the United Nations at:
<http://domino.un.org/UNISPAL.NSF/0/5fb09709f4050b8985256ced007390d8?OpenDocument>

Vice-Premier Yao Yilin initiated a conversation with Crown Prince Abdullah, praising Saudi Arabia's support for the Palestinian cause and regional stability, and discussing possibilities for improved relations. Beijing Radio later described the meeting as a "new page in the annals of a relationship between China and Saudi Arabia", representing the opening of dialogue between the two nations, (Anderson, 2004) (see Table 4.2.1). During the 1980s, China established diplomatic ties with other Arab smaller states in the Gulf. This action included the United Arab Emirate (UAE) in 1984, Qatar in 1988 and Bahrain in 1989. Yet, it was not until 1990 that China established diplomatic relationship with the regional power, Saudi Arabia, (Zhang, 2009).

4.2.3 Security and Trade

The most important development came when the secret talks between the two nations commenced in China during the mid-1980s. Prince Bandar bin Sultan, the Saudi Ambassador to the U.S at that time, negotiated a billion-dollar purchase of Chinese long range missiles, (Kaiser, and Ottaway, 2002). In 1987, during the Iran-Iraq War, China secretly sold an estimated 36⁶ CSS-2 intermediate-range ballistic missiles (IRBM) to Saudi Arabia for about US\$3-3.5 billion. The range of the Saudi CSS-2s is about 2,800 km (1,740 miles), enough to reach Iran, Iraq, and Israel. The Saudis reportedly approached China for missiles after the Reagan Administration could not persuade Congress to lift the limit of 60 F-15 fighters that could be sold to Saudi

⁶ Some sources put the number up to 50 and others may be more, most put them between 30 to 50

Arabia. Riyadh said it acquired the missiles as deterrence against possible missile attacks from Tehran, (Shuey, and Kan, 1995). The United States - and Israel - failed to discover what was going on for two years. When intelligence agencies in both countries realised what had happened, they were livid. The U.S. State Department instructed Hume Horan, the recently arrived US ambassador in Riyadh, to see King Fahd in March 1988 to deliver a stern message expressing “surprise and disapproval of this action”, (Kaiser, Ottaway 2002). In this regard, the then Ambassador of Saudi Arabia to the United States reassured the Americans that the missiles would be deployed in a way that made it clear that they were no threat to Israel. They had a conventional warhead and were intended to deter Iraq and Iran, Saudi’s traditionally hostile neighbours, and would be used only in retaliation, (Ibid).

For China the sale helped to gain the political and strategic benefits of subsequent diplomatic recognition from Riyadh, the continuing presence of Chinese military advisers and technicians in Saudi Arabia, and Riyadh’s recognition of China as a great power patron in the region, (Gill, 1993). Geoffrey Kemp Director of Regional Strategic Programs at The Nixon Center argues that the Chinese missiles sales apparently contributed towards an effort to convince Saudi Arabia to switch recognition from Taipei (Taiwan) to Beijing, which Riyadh did in 1990, (Kemp, 1991: 62). Interestingly here to read what *The Washington Post*, 23 years ago said in its commentary on the subject:

Chinese Foreign Minister Wu Xueqian today vigorously defended his government’s increasing international weapons sales, including the recent sale of intermediate-range ballistic missiles to Saudi Arabia. Wu, speaking at a news conference, confirmed that China had sold “some nonnuclear, conventional surface-to-surface missiles” to Saudi Arabia. China’s sale of missiles to Saudi Arabia has caused concern in Israel, even though Saudi Arabia is believed to want them as protection against Iran. The missiles, which could be equipped with nuclear warheads, have a range of up to 1,625 miles. They could be used with conventional warheads to attack cities, but are not considered accurate enough to be useful against military targets, (*The Washington Post*, April 7, 1988).

In this context, the trade was also moving forward in parallel with the political and military contacts. Since the late 1970s, and almost without notice, Saudi Arabia had become one of the largest importers of Chinese goods in the Middle East absorbing a quarter of all Chinese exports to the region, (Shichor, 1982). Saudi Arabia had initially yielded to small amounts of indirect trade in 1979. China, encouraged by the initial reception of Saudi imports, doubled the trade volume by 1980. Saudi businessmen first attended the Canton trade fair in the early 1980s, and began investing in Chinese development projects, (Anderson, 2004). Trade blossomed between 1980 and 1990, nearly doubling from US\$152 million in 1980 to US\$297 million in 1990, (Embassy of China in Saudi Arabia, 2004). This growing trade relationship encouraged the first material step towards establishing diplomatic relations.

In 1987, the first major envoy of Chinese entrepreneurs visited Saudi Arabia. Headed by Jia Shi, President of the China Council for Promotion of International Trade, the delegation met with the then second Deputy Prime Minister Prince Sultan, and negotiated for increased Sino-Saudi economic collaboration. China and Saudi Arabia signed the Memorandum of Understanding (MOU) on the mutual establishment of a trade representative office on November 11, 1988. The trade representatives of the two countries assumed their posts in 1989, (Ibid). China appointed as its first representative an Arabic-fluent businessman, Deng Shaoqin. On April 11, 1989, he stated his intentions to the Saudi press: “We will work and make efforts to increase mutual understanding, strengthen co-operation, and develop Saudi-Chinese relations in all fields, so that our relations can reach a higher level in the interest of both countries and both peoples”, (Anderson, 2004). By framing his mission in political,

not just economic terms, Shaoqin indicated that his mission went beyond trade; indeed, trade offices were merely a step on the road to full recognition.

China's sensitivity and willingness to support Saudi security efforts was a final step in alleviating Saudi concerns. By 1989, Saudi Arabia was alone among the Gulf States in not recognising China. Saudi reluctance to make ties official stemmed from its long-standing relationship with Taiwan. But, while such concerns delayed the Saudi concession, it did not do so indefinitely. In this regard, the former Chinese ambassador to Saudi Arabia and first Chinese ambassador to the Kingdom "Sun Bigan" noted that:

“...The Kingdom of Saudi Arabia has strengthened its exchanges with China after the mid-eighties of the last century, where China was also willing to cooperate with Saudi Arabia. Hence the relations between them have evolved rapidly. However, conditions in the late eighties were very complex and the Saudis developed the “two steps” strategy to further the relations between the two countries. The first step is to create a trade representation office in the capital of each country; the other step is to further develop bilateral relations after the establishment of offices and the establishment of diplomatic relations. In our view, the signing of memorandum of understanding to exchange trade representation in 1988 played a positive role in the development of bilateral relations”, (Arab Information Centre, 2010).

Finally, Saudi Arabia had come to view an official relationship with China as being in its interest, (Ibid). Saudi Ambassador to the United States, Prince Bandar, travelled to Beijing on July 9, 1990, receiving little to no press coverage in the Arab or Chinese media. Shortly afterwards, Saudi Arabia's Minister of Industry and Electricity visited Taipei (Taiwan) where he delivered a letter requesting to downgrade their embassies to “representative offices.” Chinese Foreign Minister Qian Qichen travelled to Riyadh on July 20, 1990, and on July 21 the nations issued a joint communiqué announcing official recognition of each other's governments, (Anderson, 2004).

On July 21, 1990, China and Saudi Arabia signed a Communiqué and announced the establishment of diplomatic relations between the two countries. Analysis of the wording of Communiqué Concerning the Establishment of Diplomatic Relations between the People's Republic of China and the Kingdom of Saudi Arabia on July 21, 1990, summaries the political dynamics of the new Sino-Saudi relationship:

The Government of the People's Republic of China supports the policy of the Government of the Kingdom of Saudi Arabia in pursuit of achieving its security, stability and national interests. The Government of the Kingdom of Saudi Arabia recognises that the Government of the People's Republic of China is the sole legitimate government that represents the entire Chinese people. The two Governments have agreed to develop cooperation and friendly relations between the two countries on the basis of the principles of mutual respect for sovereignty and territorial integrity, mutual non-aggression, non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence, (Communiqué Concerning the Establishment of Diplomatic Relations between the People's Republic of China and the Kingdom of Saudi Arabia, 1990).

4.3 ESTABLISHING A COMMON AGENDA

Despite the delayed diplomatic establishment, China and Saudi relations have been strong in both political and economic spheres in recent times. Since the establishment of diplomatic ties between China and Saudi Arabia in 1990, bilateral ties have witnessed smooth and rapid development, helped by the joint efforts of the leaders, the governments and people of both countries. The Chinese Consulate General in Jeddah opened on April 25, 1993. In April 1998 China agreed on the establishment of the Consulate General in Hong Kong by Saudi Arabia. The two countries founded the Sino-Saudi Friendship Association and the Saudi-Sino Friendship Association respectively in October 1997, (Anderson, 2004).

The significance of a strong bilateral relationship between China and Saudi Arabia, founded on energy but extending to other spheres cannot be overemphasised in economic, as well as strategic terms. Despite their obvious differences – China, a Communist state with the world’s largest population, and Saudi Arabia, a monarchy whose constitution is the Islamic *Sharia’a* Law – the two nations share substantial similarities in many terms, (Matthews, 2005).

From a political standpoint, both countries’ leaders have the same paramount objective: regime survival. In China’s case, this means the continued rule of the Chinese Communist Party (CCP); while for Saudi Arabia, it refers to the power of the “Royal Family”, (Ibid). For both, regime survival depends on economic prosperity, which depends largely on energy: China must secure enough energy to fuel rapid economic growth, and Saudi Arabia must find a market for its abundant energy resources. The two countries are also similar in that both are aspiring powers: China aspires to become a world power, while Saudi Arabia aspires to be the global economic power house.

Furthermore, China and Saudi Arabia are important countries in eastern and western Asia respectively. China is a permanent member of the United Nations Security Council, and enjoys ever enhancing international status and influence, while Saudi Arabia, as a big Arabian and Islamic country, serves a heavyweight in the Arab World, Gulf region and the Muslim world. Both states are dominant in their own regions, with Saudi Arabia the driving force behind the six-nation Gulf Cooperation Council (GCC) and China a major actor throughout East Asia, (Ibid). The two

countries hold a shared perspective on many major international and regional issues, and have maintained coordination and cooperation in international affairs.

According to Li Guofu, a Middle East expert at the China Institute of International Studies, “There’s no fundamental conflict of interest between China and Saudi Arabia. They both share the same or similar views on many important international issues, like the establishment of a new international order, a multi-polar world, anti-terrorism and reconstruction in Iraq. The cooperation on energy lays a good foundation for friendly political relations”, (Li, 2006: 3). Moreover, both pursue an independent foreign policy of peace, hold the same or similar opinions on many major international and regional issues and coordinate with each other in international affairs, (Liu, 2006). Furthermore, Beijing and Riyadh are in one key way alike, in that both seek to take advantage of economic globalisation without endangering their political status quo, (Pant, 2008).

Additionally, both states are led by an older generation of leaders, many of whom witnessed or actually participated in the weaving of the basic fabric of their respective nation-states; these older leaders, with assistance from younger technocrats providing important international economic and geopolitical analysis, enjoy a rare perspective from which to make important strategic decisions for the good of their citizens, (Matthews, 2005). Finally, both states also, due to their ideological underpinnings as well as their significant strategic positions, are often solitary actors on the world stage, eschewing regional and international coalitions and group diplomacy when they deem their own interests not to be fully aligned with those of other states, (Ibid).

In the economical realm, China is an important polar of the world economy, while Saudi Arabia is among the world top 20 economies. Both are developing countries and the two economies are highly complementary. Along with continuous economic growth China will accordingly need more energy. Saudi Arabia, with world top petroleum reserve and production, is worthy of the name “Kingdom of oil”, (Liu, 2006). In this regard, what is working to the Kingdom’s advantage is that China is the second largest economy in the world, with a vast potential demand for energy. With its growth predicted on using hydrocarbons, China needs Saudi oil and the Kingdom needs to “look East” to find growing markets for its oil and petrochemicals over the coming decades, (Ramkumar, 2010). Saudi Arabia and China are partners at various levels. Both are key members of the G20. The Kingdom represents the supply side of global energy economics in the bloc, while China represents the emerging economies.

Since energy is vitally important to national survival and the enhancement of national power, and in the cases of Saudi Arabia and China, to regime survival as well, one must consider the political-strategic subtext of Sino-Saudi relations. At the geopolitical level, both want long-term stability for the Middle East-Gulf region and long-term energy supply security with emphasis on Asia, (Ibid). In addition, both countries are exporting nations and, as a result, both countries hold massive foreign reserves and particularly U.S. government paper, (Sfakianakis, 2009), which enable them to influence the exchange rate of the dollar. Meanwhile, Saudi Arabia and China share common geopolitical and cultural interests, which should deepen along with economic ties. These include a desire to liberalise their economies without losing governmental control, support for a counterbalance to U.S. dominance in global affairs, resistance to perceived U.S. and UN “meddling” in internal affairs and human

rights criticisms, and finally, interest in maintaining stability in the Middle East and unfettered access to global oil supplies, (Obaid, 2002: 28).

It is also interesting to look at the development of Sino-Saudi economic ties at the level of economic enterprises. The energy sectors in both countries, while in the process of being restructured, are controlled by a handful of giant firms. Saudi Arabian Oil Company, (ARAMCO), for example, is the largest oil company in the world which has a monopoly on upstream oil development and controls virtually all of the country's oil reserves. ARAMCO and Saudi Basic Industries Corporation (SABIC), the biggest petrochemicals firm in the Middle East, dominate the Saudi economy. In China, the picture is similar in the sense that three oil giants dominate the energy sector: CNPC, Sinopec, and CNOOC. Of the three, CNPC is by far the largest and the most active overseas. The most obvious consequence of this concentration of power and wealth in both countries is that energy firms are considered by many as largely instruments of the state. The consolidation of Sino-Saudi energy ties can thus be viewed as an extension of state policy, (Calabrese, 2005), or to form the so called – “Oil Diplomacy.”⁷

Finally, culturally, both countries have brilliant civilisations. China is an oriental ancient civilisation while Saudi Arabia is the birthplace of Islam. Both the Islamic culture and traditional Chinese culture belong to oriental civilisation and consequently bear many similarities in social values and morals. In that regard, both China and Saudi Arabia stress the respect for cultural diversity, equal-footed dialogue and

⁷ Oil diplomacy is defined as the foreign activities with explicit involvement of the central government aiming to secure foreign oil and gas resources or promote interstate oil and gas business cooperation (See Journal of Chinese Political Science, Vol. 13, No. 1, 2008. pp. 80 -104)

exchanges between different civilisations, and oppose cultural conflict and confrontation. This serves a common language between the two countries for further strengthening humanity exchanges and expanding cultural cooperation, (Liu, 2006).

4.4 BUILDING POLITICAL MUTUAL TRUST

The Sino-Saudi relationship, being established in 1990, is relatively new when compared to the U.S.-Saudi relationship. Ever since relations were established, the two countries have witnessed rapid development in exchanges and cooperation in political, economic, cultural, educational, religious and other aspects. The Chinese Ambassador to Saudi Arabia, in an article to Saudi daily newspaper *Arab News*, summaries two decades of high-level visits between China and Saudi Arabia by regarding them as a model of the friendly cooperative relations between China and Arab States:

The Sino-Saudi relations can be regarded as a model of the friendly cooperative relations between China and Arab states. Since the establishment of diplomatic relations 20 years ago, the Sino-Saudi strategic friendly relations have developed rapidly. We have seen frequent high-level exchanges with growing mutual political trust. King Abdullah visited China in 1998 as the crown prince and in 2006 again during his first overseas visit after his accession as king. President Jintao Hu visited Saudi Arabia in 2006 and 2009 respectively. Chinese Vice President Xi Jinping visited Saudi Arabia in June 2008. In 2010, Yang Jiechi, Chinese foreign minister, and Chen Deming, minister of commerce of China visited Saudi Arabia respectively. In May, Prince Saud Al-Faisal, Saudi Arabian foreign minister, visited China and attended the Fourth Ministerial Meeting of the China-Arab Cooperation Forum. This year the leaders of the two countries also exchanged congratulatory messages on the 20th anniversary of diplomatic ties, (Yang, 2010)

(Table 4.4.1): Saudi Arabia and China Major Official Visits 1990-2010

Year	Party	Official Visit
1990	Saudi	Foreign Minister Saud AL-Faisal and Undersecretary of Foreign Ministry
	Chinese	State Councillor and Foreign Minister Qian Qichen
1991	Saudi	
	Chinese	Chinese Prime Minister Li Peng
1992	Saudi	Saudi Minister of Finance and National Economy Aba Al Khail
	Chinese	President of the Chinese People's Association for Friendship with Foreign Countries Han Xu
1994	Saudi	Minister of Oil Hisham Nazer and Minister of Commerce Sulaiman Salaim Minister of Oil Hisham Nazer
	Chinese	Vice Foreign Minister Tian Zengpei
1995	Saudi	Minister of Petroleum Ali al-Naimi
	Chinese	State Councillor and Secretary-General of the State Council Luo
1996	Saudi	Minister of Finance and National Economy Dr. Ibrahim Bin Abdul Aziz Al-Assaf
	Chinese	Vice Chairman of the Central Military Commission of the CPC Central Committee, State Councillor and Defense Minister Chi Haotian and Vice Chairman of the Chinese People's Political Consultative Conference (CPPCC) Ye Xuanping
1997	Saudi	Minister of Petroleum Ali al-Naimi and Minister of Higher Education Dr. Khalid Al-Angary
	Chinese	Vice Foreign Minister Tian Zengpei
1998	Saudi	Crown Prince Abdullah, Deputy Prime Minister, Commander of the National Guards and
	Chinese	Qian Qichen Minister of Foreign Affairs of China
1999	Saudi	Prince Salman, Emir of Riyadh District and Minister of Commerce Osama bin Jafar Faqih
	Chinese	President Jiang Zemin and Vice Foreign Minister Ji Peiding
2000	Saudi	Second Deputy Prime Minister, Minister of Defense and Aviation and Inspector-General Prince Sultan bin Abdulaziz, Minister of Information and Minister of Agriculture and Water Conservancy,
	Chinese	
2001	Saudi	Ali Al-Naimi Minister of Petroleum and Vice Foreign Minister Dr. Nizar bin Obaid Madani
	Chinese	Vice Governor of Hebei Province Guo Shichang, Vice Minister of the General Administration of Sport Yu Zaiqing, President Wang Tao of the Sino-Saudi Friendship Association, Vice Governor of Hebei Province Guo Shichang, Vice Minister of the General Administration of Sport and Yu Zaiqing President Wang Tao of the Sino-Saudi Friendship Association
2002	Saudi	Salih bin Hamid, Chairman of the Consultative Conference of Saudi Arabia and Minister of Higher Education Khalid Al-Anqari
	Chinese	State Councillor Wu Yi, Vice Foreign Minister Yang Wenchan, and Minister of Water Resources Wang Xucheng
2003	Saudi	President of China-Saudi Friendship Association and Chairman of Saudi Arabian Council of Industry and Commerce Hilashi
	Chinese	China's special envoy to the Middle East Wang Shijie
2004	Saudi	Ali Al-Naimi Minister of Petroleum
	Chinese	Foreign Minister Li Zhaoxing, Chinese Assistant Minister of Commerce Yi Xiaozhun and chief of SINOPEC Wang Jiming.

2006	Saudi	King Abdullah Al Saud
	Chinese	Chinese President Jintao Hu
2007	Saudi	Minister of Petroleum and Mineral Resources Ali Al-Naimi
	Chinese	
2008	Saudi	Prince Muqrin bin Abdul Aziz, special envoy of Saudi Arabian King Abdullah bin Abdul Aziz Secretary-General of Saudi Arabia's National Security Council, Prince Bandar bin Sultan bin Abdulaziz and Abdallah Jum'ah Abdallah then Aramco president
	Chinese	Chinese Vice President Xi Jinping and Foreign Minister Yang Jiechi
2009	Saudi	Ali Al-Naimi Minister of Petroleum and Khalid Al-Falih Saudi Aramco President
	Chinese	Chinese President Jintao Hu
2010	Saudi	Foreign Minister Saud AL-Faisal, Minister of Commerce and Industry of Saudi Arabia, Mr. Abdullah Alireza and Khalid Al-Falih Saudi Aramco President
	Chinese	Foreign Minister Yang Jiechi, Chinese Public Security Minister Meng Jianzhu and Chinese Minister of Commerce Chen Deming

Source: Adapted from various sources and reports

Indeed, in recent years, their political mutual trust and exchanges of high-level visits have also been on the rise. Between 1991 and 1998, over sixteen high-level exchanges occurred, only occasionally resulting in a solid agreement; instead, they served to reinforce the relationship between the two parties, (Anderson, 2004). In this regard Sun Bigan, the former ambassador to Saudi Arabia, said that:

“The tasks of Chinese diplomats in Saudi Arabia were many and very important, especially the one to introduce the Chinese to the Saudi royal family and to increase confidence in the Chinese Government. The second task was to establish links with Saudi businessmen, and explain to Saudi officials the situation of China in the areas of industry, trade and arranging meetings between officials of the two countries in these two areas, in order to push trade”, (Arab Information Centre, 2010)

The relationship moved to higher level, as King Abdullah, then crown prince, visited China for the first time in 1998, becoming the highest-level Saudi official ever to visit China, (Ibid). In that visit Crown Prince Abdullah called China “the best friend of Saudi Arabia”, (Zhang, 2009)... “There is no doubt that the great Chinese people and their history have a place in the hearts of the people of Saudi Arabia”, (Saudi Embassy of Saudi Arabia in Washington, 1998). Referring to the long discussion he

had with the Chinese Premier Zhu Rongji on political and economic affairs, the crown prince said: “There have never been differences between the two sides on political issues.” Concerning economic cooperation, he said: “I had an impression of truth and openness during my talks with the Chinese Premier”, (Ibid).

The Sino-Saudi relationship further expanded, with even higher level visits. Among all these visits, two were particularly significant. The first was President Jiang Zemin’s visit in 1999 and the second was King Abdullah’s trip in 2006. Jiang’s one was the first time a Chinese President had visited Saudi Arabia. During his visit, the Chinese President pronounced a “strategic oil partnership” between China and Saudi Arabia, (Zhang, 2009). This trip is regarded as having cemented bilateral relations since the establishment of diplomatic relations between the two countries, (Ibid). In Jiang’s state visit to Saudi Arabia in 1999, China and Saudi Arabia signed an agreement which “inaugurated a strategic oil partnership”, and through talks with Premier Zhu Rongji and President Jiang Zemin, the two sides formulated a joint press communiqué which indicated they had “reached consensus” on a variety of issues, (Ibid). In a speech there, Zemin emphasized the five principles of peaceful coexistence⁸ and “Third World” nature of both China and the Arab world; as a result, he noted, “The two sides share broad common views on human rights and a wide range of other issues”, and were engaged in a common identity and community of interests, (Anderson, 2004).

⁸ The five principles of peaceful coexistence are: mutual respect for sovereignty and territorial integrity, mutual non-aggression, non-interference in each other’s internal affairs, equality and mutual benefit, and peaceful coexistence.

The year of 2006 brought about a renewed effort to develop closer Sino-Saudi relations. The visits between President Jintao Hu and Saudi King Abdullah bin Abdul-Aziz in 2006 and the impressive array of new agreements between the Saudi and Chinese Governments indicate such a trend. First was the visit of King Abdullah bin Abdulaziz al-Saud's to China in January 2006. This visit carried special significance due to two reasons: (a) It came five months after succeeding his half-brother, it was King Abdullah's first visit outside the Middle East since he took the throne in 2005. (b) It was the first visit by a Saudi monarch to the People's Republic since diplomatic relations were established in 1990, (Madsen, 2006). The new king's (at that time) decision to visit China, rather than the U.S., was a sign of the growing importance of Riyadh's trade ties with Beijing, (Evans, 2009). During King Abdullah's visit to China in January 2006, both countries signed numerous agreements for cooperation in energy (petroleum, mineral, and natural gas), trade, and professional training/technical matters, (Asia Times, 25 January 2006).

A short three months later, President Jintao Hu made a diplomatic visit to Saudi Arabia further highlighting the seriousness of Sino-Saudi relations. That visit was also important for several reasons: (a) Hu's trip to Saudi Arabia occurred only three months after Abdullah's trip to China. 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; (b) Hu was only the second foreign president to address the Saudi Consultative Council, after former French President Jacques Chirac; and (c) Hu's visit ended with tangible results, not only in regards to energy, but also other fields, such as health and trade, (Douglas and others, 2006). 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”, (Ibid).

The mutual trust continues between the two countries through many channels. When China was struck by a severe earthquake in May 2008, Saudi Arabia donated US\$60 million to the stricken areas, becoming the largest donor to the Chinese Government. This certainly played a positive role in bilateral relations. For example, on the evening of June 6, 2008, Chinese President Jintao Hu held a telephone conversation with Saudi Arabian King Abdullah bin Abdul-Aziz. Hu said King Abdullah offered sympathy and condolences to the Chinese Government and people and swiftly provided aid to the quake-stricken area at this crucial moment when a strong earthquake shocked China’s southwestern province of Sichuan. The move embodied the profound friendship of the king, the Saudi Arabian Government and its people toward the Chinese people, (China’s Ministry of Foreign Affairs, June 6, 2008). One month after the earthquake, Xi Jinping, the Vice President of the PRC, visited the Saudi Arabia and signed The Joint Statement of the PRC along with Saudi Arabia on Strengthening Cooperation and Strategic Friendly Relations, (Xinhua, June 22, 2008).

Six months later after the Jinping visit, President Jintao Hu made another trip to Riyadh, his second in three years, (Zhang, 2009). Hu met with Saudi Arabian King Abdullah bin Abdul-Aziz in February 2009 and the two leaders vowed to deepen their strategic friendly ties, work together to tackle the global financial crisis and strengthen coordination in international and regional affairs. Following the talks, the two leaders witnessed signing ceremonies for five cooperation deals in energy, health, quarantine, transportation and culture, (Xinhua, February 11, 2009).

In addition, Hu raised a six-point proposal on developing China-Saudi Arabia strategic friendly ties, (China's Ministry of Foreign Affairs, February 11, 2009). (a) Maintain high-level visits and establish a high-level consultation mechanism. (b) Take advantage of their resources and markets, promote an all-round energy partnership and expand two-way investment. (c) Expand the scale of economic and trade cooperation and raise the level of cooperation. The Chinese Government encourages more competent businesses of the country to participate in Saudi Arabia's infrastructure construction and enhance cooperation on project contract and labor. (d) Advance exchanges in the fields of education, sports and tourism and expand personnel contacts. (e) Strengthen communication and coordination in major international and regional issues and safeguard regional peace and stability. (f) Enhance the cooperation between China and the Gulf Cooperation Council (GCC).

Having consecutive head-of-state exchanges in such a short time is considered unusual. In its daily opinion column, the Saudi daily paper *Al Jazirah* described the relations between the countries: "Three visits between the leadership in Saudi Arabia and China in just three years. This fully demonstrates the qualitative development and big step forward in their relations", (Al Jazirah, February 10, 2009). Indeed, both Beijing and Riyadh feel that closer Sino-Saudi political relations will lead to great economic benefits. China hopes that closer political relations will lead to greater energy access and larger trade markets. Saudi Arabia is hoping that closer political relations will lead to a stable market for its oil exports and greater Chinese investments and assistance in economic development. In this regard during a meeting between Chinese President Jintao Hu and special envoy Prince Bandar bin Sultan bin Abdulaziz of Saudi King Abdullah, in March 2011, Hu said China treasures its

friendship with Saudi Arabia, and considers the country a reliable good friend and a sincere partner, (Xinhua, March 18, 2011). He added, “We are willing to make joint efforts with Saudi Arabia, to consolidate political trust, enhance strategic coordination and substantial cooperation, to boost bilateral strategic and friendly ties to a new high”, (Ibid).

The most interesting aspect of all these developments is that Washington is following the Sino-Saudi relations very closely. In one of the confidential documents leaked by *Wikileaks*, James Smith, the U.S. ambassador to Saudi Arabia, wrote to Secretary of State Hillary Clinton, as she prepared for the February 2010 visit to Saudi Arabia, summarising the results of the Chinese foreign and commerce ministers to Saudi Arabia in January 2010:

Since King Abdullah’s historic visit to Beijing in January 2006, the Saudi has focused predominantly on energy and trade. However, the relationship may be showing signs of political evolution. While the Chinese would likely prefer to stay away from political controversy, their economic power and permanent seat on the UN Security Council has made it more and more difficult for them to avoid politics altogether...The incentives for the Saudis to try and leverage their economic relationship with China for political gain with respect to sensitive regional issues, such as Iran and the Israeli-Palestinian conflict, are significant and growing. After patiently focusing on building the economic relationship since 2006, FM Sauds public and private prodding of FM Yang indicates the Saudis are ready to try and cash in some political chips, (Wikileaks, January 27, 2010).

4.5 CONCLUSION

This chapter has shown that Chinese economic interests are the driving force behind the expansion of the Sino-Saudi relationship – and not China’s desire to expand its power and influence in the Middle East at the cost of the United States. China was in its quest to establish diplomatic relations with Saudi Arabia not attempting to increase its power and influence in Saudi Arabia at the cost of the United States as realists may contend. China’s policy to improve relations with Saudi Arabia came after the implementation of China’s policy of openness to the outside world and focus on economic development away from ideological considerations.

In fact, the entry of China to the Middle East was not, as happened with the former Soviet Union to counter U.S. influence but, on the contrary was for the following reasons: (a) China entered a “strategic partnership” with the United States against the Soviet Union, and embarked upon an “open up” policy; (b) China’s desire in strengthening economic relations with the Middle East and arms sales; (c) the quest for oil and their appreciation of Saudi Arabia’s oil policy; (d) China saw in Saudi Arabia a chance to gain further legitimacy by urging Gulf nations to shift diplomatic recognition to Beijing away from Taiwan. China’s actions were closely aligned with the economic interdependence theory. If China was acting in the realism model, it should be actively pressuring Saudi Arabia to weaken its political ties to the United States; thereby increasing the amount of Chinese influence in Saudi Arabia. There has been no indication that this has been the case. On the contrary China’s actions were helpful to American policy on many occasions. More important of all, China decided to renew its relations with Saudi Arabia in the early 1980s, while the alliance between Beijing and Washington was strengthening.

CHAPTER FIVE

CHINA'S SEARCH FOR A RELIABLE PARTNER

5.1 INTRODUCTION

While gaining access to the region's vast energy resources is China's primary motivation for deepening relations with Saudi Arabia, there are also a number of other factors driving China's Middle East policy. (a) Politically, China is seeking to enhance the security of its oil imports from the Middle East by increasing its diplomacy in the region. The Chinese Government appears to believe that strong bilateral political relationships can produce greater supply security during crises, (Downs, 2000: 49). (b) In the security realm, they intend to fight what the Chinese call the "three ugly forces" - religious extremism, national separatism and terrorism. Since Saudi Arabia is the religious centre of the Islamic world, China has attempted to maintain good relations with Riyadh in order to get their support on the Uyghur insurgency in Xinjiang Province and maintain amicable relations with the over 20 million Muslims residing in China, (Li, 2009). (c) China is seeking full support of the Arab States in the international arena on issues like the Taiwan or "One China Policy", as well as its position on Tibet and other domestic controversies in the international arena like human rights. (d) It laid the groundwork for the expansion of commercial ties with Saudi Arabia with the hope that this would stimulate commerce with other Gulf States as well, (Calabrese, 1998: 351-366).

In this context, Zhang Xiaodong, Deputy Chief of the Chinese Association for Middle East Studies, argues that, "The Arab nations need China's help in protecting their

rights, as China is a permanent member of the UN Security Council. And China hopes to be backed up by Arab nations in certain issues, such as Taiwan, climate change and human rights”, (Wu, 2010). One good example illustrating this mindset occurred on December 10, 2010 when Saudi Arabia with other Arab countries supported China by not attending the *Nobel Peace Prize* ceremony for Chinese dissident Liu Xiaobo, (BBC, December 7, 2010).

China has got along well with Arab countries for a long time now and has avoided intervening in their domestic affairs. Indeed, during the turbulences that swept the Arab World, Beijing enforced that policy in very clear way and called to solve the problem without any outside interference. In that regard China’s special envoy to the Middle East Wu Sike told *China Daily* at the National Committee of the Chinese People’s Political Consultative Conference (CPPCC) National Committee on March 2011 that: “The U.S.’s values and interests clashed (in the regional chaos in the Middle East) this time, and it chose to protect its interests...Washington’s support for discarding Hosni Mubarak, the former Egyptian president, a long-term strategic ally of the U.S., hurt and disappointed both Arab leaders and America’s other allies in the region”, (*China Daily*, March 14, 2011).

This chapter will examine China’s perspective of developing relations with Saudi Arabia and attempts to answer two questions. Why is the Saudi Arabia an indispensable partner for China? And what is the nature and extent of China’s strategic motives in pursuing a partnership with Saudi Arabia? The chapter also attempts to decipher Chinese intentions in regarding to Saudi Arabia. If China is acting within the context of realist theory, it should be attempting to expand its power

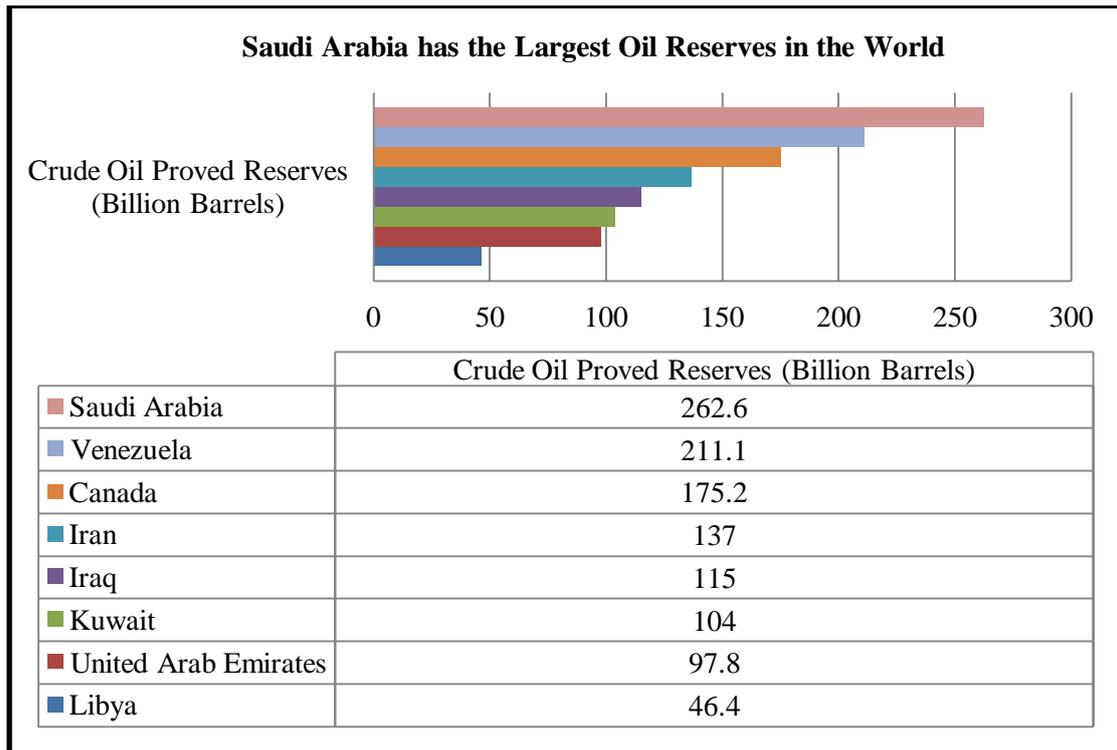
and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence and to encourage Saudi Arabia to shift their close political relations from the United States over to China. If China is acting in the economic interdependence model as the liberals argue, it should be developing a Sino-Saudi political relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship. In this regard I will show the conditions under which high interdependence between China and the Saudi Arabia will lead to a pacific or belligerent China. If decision-makers' expectations of future relations and trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future environment they will likely take action to protect their interests in the region.

5.2 THE SIGNIFICANCE OF SAUDI ARABIA IN CHINA'S OIL STRATEGY

Over the past several years Sino-Saudi relations have grown closer, as Riyadh seeks to reduce its dependence on the United States, and Beijing's thirst for oil has increased, (Wu & Storey 2008: 190-208). Today, Saudi Arabia is China's top oil provider and Saudi Arabia is the largest market for Chinese products in the Middle East, (Ibid). China's efforts to develop closer political relations with Saudi Arabia are based on two goals, (Jin, 2005). First, China is attempting to ensure it has access to Saudi energy sources in the future in order to meet its energy demands. Secondly, China is also attempting to maintain its diversity in energy sources. While China may

be limiting the amount of Saudi oil it imports, Saudi Arabia still plays a vital role in maintaining the diversity in Chinese oil supplies (i.e. keeping China from becoming too reliant on Angola, Iran and Russia), (Ibid).

(Figure 5.2.1): Top Proven World Reserves by Country



Source: EIA (August, 2011)

In a Speech by Yang Honglin, the Chinese Ambassador to the Kingdom of Saudi Arabia, made on the occasion of the Chinese National Day in 2008, he stated the Chinese position regarding Saudi Arabia in a very clear way: “An influential country in the Middle East and Gulf region and the largest energy supplier in the world, Saudi Arabia has played an important role in maintaining the peace and stability of the region, pushing forward the regional economic development, enhancing Arab countries’ solidarity, promoting dialogue among different religions and civilisations

and safeguarding the stability of international energy supply”, (Yang, 2008). While former Chinese ambassador to Saudi Arabia Zheng Dayong described the Sino-Saudi relations in very interesting words:

I can use a vivid description to introduce the country: it's a country 'grasping with its two hands' – one hand for oil and the other for the Qur'an ... Oil and religion play an important part in its people's lives. Saudi Arabia is the world's leading petroleum exporter. Saudi Arabia is also the birthplace of Islam. The two holiest places in Islam – Mecca and Medina—are in Saudi Arabia, and 1.3 billion Muslim pilgrims from all over the world head to Mecca each year. (*China Daily*, February 12, 2009)

Indeed, spiritually-wise, Saudi Arabia plays a unique role for the world's 1.3 billion Muslims as the birthplace of Islam and home of the two holiest cities. Politically, its leaders enjoy broad domestic support, regional influence and global reach. Economically, as the world's sole energy superpower and the de facto central banker of the global energy markets, Riyadh is the economic powerhouse of the Middle East, representing 25 percent of the combined gross domestic product of the Arab world. The Kingdom has amassed around half trillion dollars in foreign reserves, (Obaid, 2011).

China and Saudi Arabia enjoy the mutual benefits of very complementary economies which has strengthened economic ties. China is currently the fastest growing oil consumer, while Saudi Arabia is the largest oil producing country. As China's demand for oil continues to rise and with Saudi Arabia seeking to secure stable markets, Sino-Saudi relations are expected to rapidly expand in the coming years. Analysis of the wording of Memorandum of Understanding on Petroleum Cooperation between China and Saudi Arabia, (October 31, 1999), reveals the economical dynamics of the new Sino-Saudi relationship:

The two sides shared the view that the stability of the international oil market is in the interest of oil producing and consuming countries and health of the world economy. Both sides agreed that Saudi Arabia is a large, dependable, reliable and secure petroleum supplier, while China is a large, dependable and reliable consumer; therefore, the two countries are strongly

complementary to each other in this field. Both sides expressed their willingness to establish long-term friendly and cooperative relationship in the field of petroleum, (Memorandum of Understanding on Petroleum Cooperation between the Government of the People's Republic of China and the Government of the Kingdom of Saudi Arabia, 1999).

From the Chinese perspective, energy security lies at the heart of the bilateral relationship with Saudi Arabia, as has been the case with many of China's most important strategic relationships over the past decade, (Wagner & Karasik, 2010). According to the Chinese ex-ambassador to Saudi Arabia, Song Wei, there are two key words as far as ties between China and Saudi Arabia is concerned, they are "energy cooperation", (Wei, 2009). He added, "Energy cooperation has gone far beyond a buy-and-sell relation...when I was an ambassador to Saudi Arabia, Saudi Arabia suggested that we build a strategic cooperation, which means Saudi Arabia needs a stable market, and China needs a stable supply", (Ibid). Indeed, Saudi Arabia has been the top supplier of crude oil to China since 2002, and it is unlikely to give up this leading position in near future, (Ebel, 2009: 2).

China recognises Saudi Arabia's uniquely dominant role among the world's oil producers and continues to work hard at building closer ties to the Kingdom. The Chinese investment in Saudi Arabia has also expanded significantly. Strategically, these trade and investment ties are meant to reinforce Beijing's efforts to establish itself in Saudi calculations as a desirable long-term customer for the Kingdom's oil exports. There are no other producers capable of stepping into Saudi Arabia's shoes now or at least in the next decade. Only Russia and the United States produce volumes comparable to Saudi Arabia's, (IEA, 2010). But Russian oil, which is more expensive than Saudi low-cost oil, is ill suited to serve as spare capacity, and Russia has also shown little interest in cooperating with other producers to help stabilise prices. Nor is there any prospect in the near future that the United States will step

back into the swing-producer role it played half a century ago, when it held huge low-cost reserves and was not massively dependent on imported oil, (Robert & Michael, 2011). Within this context, China regards Saudi Arabia as a very reliable supplier of crude oil. Over the past decade, the Saudis have repeatedly told the Chinese that they can count on Saudi Arabia to provide China with the oil it needs for continued economic growth, (Down, 2011: 62). Perhaps the greatest reassurance the Chinese have received from the Saudis about their reliability as an oil supplier came during President Jintao Hu's state visit in February 2009. While Hu was in Riyadh, the Saudis promised to guarantee the supply of crude oil to China at all times as part of a "gentleman's agreement" between Saudi Aramco and China Petrochemical Corporation (Sinopec), (Ibid).

From the Chinese perspective, Beijing needs a reliable supplier of oil. Indonesia is now a net importer of oil, Iran and Sudan are unreliable, Russia has political agendas, Canada and Venezuela are too far away and Iraq needs long years to recover. A comment by the China News Agency summarised Beijing's view of the emerging Sino-Saudi relationship: "Saudi Arabia is a very good and reliable oil supplier. It is not like Nigeria, which is so fraught with uncertain factors that its oil supply fluctuates sharply. Neither is it like Iraq and Iran, whose oil supply was affected by unstable political situations", (Alterman, 2008: 33). Even Venezuela, which has the second largest oil reserves in the world, can't match the production power of Saudi Arabia. Venezuelan oil output peaked in mid 2009 at 3.0 mb/d; today it is down to 2.5 mb/d in spite of record demand and high prices, (*Financial Times*, August 16, 2011). Iran is similar: output peaked at 4.2 mb/d in mid 2006; today it has fallen to 3.5 mb/d, (Ibid).

Indeed, Saudi Arabia has always been banking on its credibility as a reliable oil supplier, or as Ali Al-Naimi, Minister of Petroleum and Mineral Resources of Saudi Arabia, puts it, the Kingdom “has an important role to play in promoting stability in world oil markets. The most powerful tool we have for achieving a balanced market is our maintenance of spare production capacity”, (Al-Naimi, 2009). Paul Horsnell, the veteran oil watcher at Barclays Capital, notes that when it comes to production increases, “Saudi Arabia is the world’s sole swing producer, giving it a level of control not seen since the heights of OPEC in the 1970s”, (*Financial Times*, August 16, 2011). While John Sfakianakis, the Chief Economist of Banque Saudi Fransi, argues along similar lines: “For China Saudi Arabia is a voice of moderation and stability – and undoubtedly the single most important country in the world of energy. It is the driving force that tries to bring moderation in prices and to supply global markets with sufficient oil”, (Sfakianakis, 2009). Saudi Arabia’s ability to calm global markets in periods of high stress gives the Kingdom an important political influence. If Saudi ARAMCO’s spare capacity shrinks, oil prices will become even more volatile, (*Peter, 2011*). In a recent speech to “Royal Air Force Molesworth, UK” Prince Turki Al Faisal underlined the pivotal role rule of Saudi Arabia:

Saudi Arabia itself now possesses 75 percent of the spare production capacity in the world, with every other country possessing a very small amount or practically nothing. To put this into perspective, Saudi Arabia has so much production capacity – nearly 4 million barrels/day – that we could almost instantly replace all of Iran’s oil production. This massive spare capacity is the outcome of a capacity expansion program from 10 million barrels per day to 12.5 million barrels per day, which the Kingdom undertook between 2002 and 2008 at a capital cost of over US\$45 billion. Current plans are in place to sustain this capacity further by a new field development at Manifa, which will bring on a further 900 thousand barrels of oil capacity per day by 2014 at a capital cost of US\$16 billion to offset decline at other fields. In addition to this spare production capacity, Saudi Arabia is committed to insuring sufficient refining capacity on a global basis to guarantee its oil production reaches the end use markets across the world. Current plans are to increase its Saudi based refining capacity from 2 million barrels per day to 3 million barrels per day by 2014 at a capital cost of over \$26 billion dollars, (Al Faisal, 2011).

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. 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, (Douglas & others, 2006). In China’s eyes, stable relations with Saudi Arabia are the best possible approach to avoid being shut-off from vital oil resources in the case that the Sino-American relationship should take a turn for the worse, (Jochen 2006), or/and in the event of political turmoil as it has been demonstrated in Libya in 2011. Indeed, Saudi Arabia has boosted its crude oil production, reaching a 30-year high of almost 10 (mb/d) in July 2011, (*Financial Times*, August 16, 2011). Tellingly, the last time that Saudi Arabia was pumping as much crude oil as it did in July, 2011 was in early 1981, when the Kingdom was replacing the production lost after the Iranian revolution and the start of the Iran-Iraq war, (Ibid).

At the moment, the Saudis are in a unique position; Saudi Arabia is the largest oil producer of the Organization of the Petroleum Exporting Countries (OPEC). With approximately one fifth of the world’s proven oil reserves and some of the lowest production costs, Saudi Arabia is expected to remain the world’s largest net oil exporter for years to come, (EIA, January 2011). Saudi Arabia produced over 10 (mb/d) of oil in 2010, the majority of which was crude oil. Asia, including Japan, South Korea, China, and India, now receive an estimated 50 percent of Saudi Arabia’s crude oil exports, as well as the majority of its refined petroleum product and NLG exports, (Ibid). Saudi Arabia is also the world’s only “swing producer”: the country retains the single, largest spare production capacity of all oil producers. This means

that the world market and the world’s largest oil consumers have a major interest in a cooperative Saudi Government, (Aarts & Rijsingen, 2007: 23-58), (see Table 5.3.1).

(Table 5.2.1): Estimated OPEC Sustainable Crude Production Capacity (mb/d)

	2010	2011	2012	2013	2014	2015	2016
OPEC	35.74	34.65	35.48	36.39	37.04	37.82	38.07
Saudi Arabia	12.07	12.04	11.88	11.73	11.59	11.82	11.90
Iraq	2.50	2.76	3.16	3.51	3.88	4.25	4.36
Iran	3.87	3.70	3.53	3.46	3.30	3.12	2.98

Source: IEA, Oil Market Report, (December, 2011)

Saudi Arabia continues to have substantially more spare capacity than any other OPEC member and, as such, should be prepared to ramp up volumes as demand recovers, (Bank of America Merrill Lynch, 2010). Saudi Arabia has recreated its spare production capacity by bringing new facilities on-stream. Riyadh has spent billions of dollars in new oil fields and its maximum production capacity has steadily risen over the last decade. Today Saudi Arabia could boost its production further to more than 10 mb/d, potentially up to 12.5 mb/d, (*Financial Times*, August 16, 2011). This enables it to retain its OPEC leadership and consolidate its international influence, (Shell International BV, 2011: 26). The increase in Saudi Arabia’s spare production capacity will be the critical element in moderating oil price volatility in the next few years. Over the next two decades, according to official forecasts, the world will rely even more heavily on Saudi oil. The International Energy Agency, which represents the oil-consuming countries, predicted in its latest “New Policies” scenario that by 2035 Saudi Arabia’s oil output would have roughly doubled from over 8 (mb/d) in 2009, (World Energy Outlook 2010: 133) to 15.4 million barrels per day in

2035, (The International Energy Outlook 2011: 34) The Kingdom's share of total world oil production would rise from 12 per cent to almost 14 per cent, (Ibid:34-35) (see Table 5.3.2).

(Table 5.2.2): Production of World Key Oil Producers, (2010-2030)

In the New Policies/Reference Scenarios(mb/d)									
	IEA (in the New Policies Scenario)					EIA(in the Reference Scenario)			
	2010	2015	2020	2025	2030	2015	2020	2025	2030
Saudi Arabia	8.4	11.2	11.5	12.2	13.2	11.6	12.8	13.9	14.6
Russia	10.4	10.2	9.5	9.2	9.2	10.8	11.4	12.2	12.8
U.S.	7.7	6.9	6.9	6.8	6.9	10.4	11.2	11.7	12.2
Iran	3.7	4.7	4.8	5.0	5.1	4.0	3.8	3.7	3.8
China	4.1	3.8	3.7	3.6	3.1	4.0	4.2	4.8	5.2
Canada	3.3	3.8	4.0	4.5	4.9	4.2	4.7	5.4	6.0
Mexico	2.9	2.5	2.4	2.4	2.5	2.3	1.8	1.4	1.5
Caspian	3.1	3.7	4.4	5.3	5.4	3.5	3.8	4.2	4.4
U.A.E	2.3	3.5	3.5	3.6	3.9	3.6	3.5	3.5	3.3
Iraq	2.4	3.6	4.8	5.3	6.1	2.9	3.6	4.5	5.5
Kuwait	2.3	2.9	3.0	3.1	3.3	3.0	3.1	3.3	3.7
Venezuela	2.5	2.8	2.7	2.9	3.4	2.4	2.5	2.5	2.5
Nigeria	2.1	2.1	2.1	2.3	2.5	3.0	3.2	3.3	3.3
Brazil	2.1	3.1	4.4	5.0	5.2	3.8	4.7	5.5	6.0
Algeria	1.2	2.0	2.1	2.1	2.2	2.6	2.7	2.6	2.5
Angola	1.7	1.5	1.6	1.7	1.5	2.2	2.3	2.2	2.1
Libya	1.5	1.7	1.7	1.8	1.9	0.9	0.7	0.7	0.8
Qatar	0.8	2.2	2.3	2.3	2.5	1.9	2.1	2.3	2.5

Source: Adapted by the author from IEA, World Energy Outlook 2010 and EIA, International Energy Outlook 2011

The world, (China in particular), will continue to rely on traditional fossil fuels for most of its energy needs for the coming decades. In fact, these energy sources, namely coal, oil and natural gas, are expected to account for about four out of every five units of energy that mankind will consume for the foreseeable future, (Al-Falih, September 13, 2010). Oil remains the world's leading fuel, at 33.6 percent of global energy consumption, but oil continued to lose market share for the 11th consecutive year, (Statistical Review of World Energy 2011: 2).

(Table 5.2.3): World Primary Energy Demand by Fuel and Scenario

	1980	2008	New Policies Scenario		Current Policies Scenario		450 Scenario	
			2020	2035	2020	2035	2020	2035
Coal	25%	27%	27%	24%	29%	29%	26%	17%
Oil	43%	31%	30%	28%	30%	28%	29%	26%
Gas	17%	21%	22%	22%	12%	22%	21%	20%
others	15%	21%	21%	26%	29%	21%	24%	37%

Source: World Energy Outlook 2010

Over the medium term, most of the increase in the global production of crude oil is expected to come from the GCC countries (and Iraq). The GCC countries, and in particular Saudi Arabia, are the only credible, sizable, long-term alternative providers of crude oil to China. Saudi Arabia is also a source of capital for China and can provide the chemical products that China needs to continue gaining export markets as well as the refined products and crude oil to manufacture these chemicals themselves, (Andrews-Speed, 2009: 50).

According to Khalid AL-Falih, President of Saudi ARAMCO, “Oil reserves in Saudi Arabia of about 260 billion barrels represent roughly a fifth of the world’s proven reserves and, at our current production rate, these reserves are enough for more than 80 years of production, (Al-Falih, September 13, 2010). Yet AL-Falih expects that over time those reserves will grow by an additional 40 percent, and ARAMCO is working to raise the rate of recovery from Saudi’s major oil fields to 70 percent, or twice the worldwide average, (Ibid). In sum, as a result of all the previous reasons, China cannot ignore the position of Saudi Arabia in global oil markets, which makes Saudi Arabia an indispensable partner for China for years to come.

5.3 EXPANDING ECONOMIC INTERESTS

Saudi Arabia represents over 20 percent of the combined GDP of the Middle East-North Africa (MENA) region and an estimated quarter of the Arab World's GDP according to the latest IMF numbers, (IMF, September 2011), making it the economic engine of the region and the logical choice to be a permanent influential member of the G20. The Saudi stock market represents about 50 percent of the entire stock market capitalisation of the MENA region and the listed Saudi companies make up 5 of the top 10 companies in the region with the top two slots being the Saudi conglomerates, ARAMCO and SABIC, (Al Faisal, June 8, 2011). The Saudi Arabian Monetary Agency (SAMA), the Kingdom's central bank, is the world's third largest holder of foreign exchange reserves managing just under US\$550 billion, (Ibid).

Since the establishment of diplomatic relations in 1990, the trade between the two countries flourished based mainly in Saudi oil exports, but also provided the Chinese with new markets. The two-way trade between Saudi Arabia and China in the last two decades increased almost 34 times from US\$1.28 billion in 1990 to almost 44 US\$ billion in 2010, Saudi Arabia is now China's largest trading partner in the Middle East and North Africa, (Xinhua, May 12, 2010). Saudi Arabia has been China's biggest trade partner in West Asia (including the Middle East and the League of Arab States), for the last nine consecutive years, (Xinhua, January 11, 2011).

China is seeking to not only improve its energy security but also to expand its trade. Saudi Arabia has emerged as a major Middle Eastern trading partner for China and it is looking to further expand this relationship. Currently, the Middle East is also one of

the most important destinations for China's labour-intensive products. And the GCC countries, rich in capital but short of labour, are a particularly important market for China's contract labour exports, (Jin, 2010), (see Table 5.3.1 below).

(Table 5.3.1): China's Exports and the World Trade, 2001-2010^a

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World Total Exports (US\$ trillions)	6,06	6,38	7,45	9,12	10,38	12,07	13,8	15,9	12,14	15,23 ^b
China's Total Exports to:										
World (US\$ billions)	266,1	325,5	438,2	593,3	761,9	968,9	1220	1430	1201	1578
(%) of World's Total	4.3	5.2	5.8	6.5	7.3	8.02	8.8	8.9	9.8	10.4
Arab World (US\$ billions)	7,2	9,6	13,05	17,6	23,6	31,7	43,2	59,3	51,8	64,9
(%) of China's Total	2.7	2.9	2.9	2.9	3.1	3.2	3.5	4.1	4.3	4.1
Saudi Arabia (US\$ billions)	1,3	1,6	2,1	2,7	3,8	5,05	7,8	10,8	8,9	10,3
(%) of China's Total	0.5	0.5	0.4	0.4	0.5	0.5	0.6	0.7	0.7	0.6

Source: General Customs Administration of China and UN COMTRADE

(a) Percentages were calculated by the author (b) WTO

Additionally, Saudi Arabia plans to spend hundreds of billions of dollars over the next five years to improve infrastructure and develop the economy and to promote diversification. These future plans provide tremendous opportunities for Chinese companies. As part of its larger economic strategy, China continues to promote its goods to the region, while the Arab Gulf States look to China and the rest of Asia for its own exports and investments. Saudi Arabia has a growing need for more

investment in technology, management skills, science, technology and infrastructure. China has an opportunity to establish an important commercial presence in the Kingdom beyond an energy relationship. China also has the capability to expand its already significant export of labour services to a region with a growing demand in construction areas, (Ramady, 2007), (see Tables 5.3.2 & 5.3.3).

(Table 5.3.2): Future Major Market Opportunities in Saudi Economy

Sector	Market Opportunities
Government Spending	The government is planning to spend US\$400 billion on roads, airports and energy projects over a five year period between 2009 and 2014. US\$70 billion of this expected to be invested in 2010. Saudi Arabia in March 2011 announced increases in government spending. The package included US\$67 billion on housing and funds.
Energy	Saudi ARAMCO, pledged US\$130 investment programmed, over the next five years, with a growing share spent on gas, (US\$70 billion of investment in the petrochemical sector by 2011 is expected).
Infrastructure	Saudi Arabia's ambitious rail plans are fuelling activity in the infrastructure sector, with US\$30 billion worth of contracts under way or at the bidding stage.
Electricity	The state-owned Saudi Electricity Company (SEC) intends to invest US\$28 billion to add approximately 13GW of power in the next three years. The utility company also plans to spend US\$70 billion by 2018 to add 25GW to meet the growing demand from a rapidly increasing population.
Water	Saudi Arabia is the third largest consumer of water <i>per capita</i> in the world, but has limited groundwater to tap. Desalination forms the backbone of the government's water strategy. US\$6 billion a year has been committed by the government to bolstering the water sector over the next two decades.
Information Technology (IT)	Saudi Arabia has the biggest IT market in the Gulf region, with a forecast value of US\$3.7 billion in 2010 expected to rise to US\$5.2 billion by 2014.

Source: USDC, Arab News, May 18, 2011, Abed, 2010: 2 and Crooks, 2010.

(Table 5.3.3): Saudi Ninth Five-Year Plan Allocations 2010-2014

Development Sector	Allocations (US\$ billions)	Share (%)
Human Resources	195	50.6
Social and Health Services	73	19
Economic Resources	60.7	15.7
Transportation & Communications	29.6	7.7
Municipal and Housing Services	26.8	7
Total Expenditures	385.1	100

Source: Saudi Arabia Ministry of Economy and Planning

In addition, the Middle East is a major source of global investment flows. For example, the six GCC states could invest a staggering US\$250 billion in Asia over the next five years, most of which would go to China, (Kawach, September 23, 2010). According to the Sovereign Wealth Fund Institute, the Middle East Sovereign Wealth Fund has US\$1438.78 billion by the end of 2010, representing 35 per cent of the world's total assets of Sovereign Wealth Funds,⁹ (see Table 5.3.4). The combined foreign assets of GCC governments, state institutions, and banking systems (i.e. excluding non-financial corporate sector), estimated around 1.5 trillion by the end-2010 and projected to rise to US\$1.7 trillion in 2011, (Abed, 2011: 2-5).

(Table 5.3.4): Sovereign Wealth Funds, World's Market Share by Region (2010)

Country	Billion Dollars	% World's share
China (including Hong Kong)	1123.3	26.3
United Arab Emirates	709.3	16.6
Norway	556.8	13.0
Saudi Arabia	444.4	10.4
Singapore	392.8	9.2
Kuwait	202.8	4.7
Russia	142.5	3.3
Qatar	85	1.9
Libya	70	1.6
U.S.	58.2	1.3
Others (25 countries)	470.8	11.0
Region	Billion Dollars	% World's share
Asia	1687.3	39.6%
Middle East	1481.8	34.8%
Europe	760.3	17.8%
Africa	134.4	3.1%
Americas	106.7	2.5%
Other	85.4	2%
Total	4,255.9	100

Source: Calculated by the author from Sovereign Wealth Fund Institute (March, 2011)

⁹ SWF Institute, See [<http://www.swfinstitute.org/fund-rankings/>]

Chas Freeman, the former United States Ambassador to Saudi Arabia, argues that Middle East markets, including its capital, arms, and consumer markets, are prizes for the world's great powers to compete in. Its political economy is a central determinant of the global future, (Freeman, 2009). In the future, the GCC (including Saudi Arabia), will grow in importance as an economic and trading hub. In 2020, the GCC is projected to be a US\$2 trillion economy, providing nearly one-quarter of the world's oil supplies as well as increasing quantities of petrochemicals, metals and plastics. As economic weight gradually shifts southwards and eastwards, emerging markets will become increasingly important trading partners and investment destinations. Gulf investors and sovereign wealth funds are likely to diversify their assets into Asia and Africa, and the region is likely to export more of its oil to industrialising countries, (EIU, March, 2009).

China on the other hand, is also increasing investments in the GCC region, with Chinese firms having contracts to build everything from railways and cement plants in Saudi-Arabia, to a port in Kuwait, and a sewage system in UAE. Furthermore, China is predicted to considerably strengthen GCC relations as experts predict China will import 20 percent more oil from the region in the next few years, going from the current 50 percent to 70 percent in 2015, (Mobrez, 2008). China also seeks to increase petrochemical, phosphate and aluminium imports, which are abundant in GCC countries. China may be importing 16.82 million tonnes of petrochemicals by 2015, almost 3.5 times more than the imports in 2008. It is anticipated that 90 percent net imports of ethylene derivatives and 70 percent net imports of propylene derivatives in the world will come from Middle East by 2013, (YarnsandFibers, March 16, 2010). The six Gulf Cooperation Council (GCC) countries, which sit atop 45 per cent of the

global recoverable crude aluminium deposits, produced around 2.2 million tonnes of aluminium in 2009 and are pushing ahead with mega aluminium projects which will boost their output to 10 million tonnes and allow them to control around 20 percent of the world's total aluminium output, (Kawach, September 10, 2010).

Saudi Arabia is expected to become a major aluminium exporter when three mega smelter projects worth more than US\$10 billion start production of nearly 2.4 million tonnes within five years, (Kawach, May 5, 2010). In addition, Saudi Arabia today accounts for about 62 percent of chemical production in the GCC region and approximately 8 percent of global production. Saudi Arabia is already the world's largest methanol producer and the second largest ethylene producer. By 2015 the Kingdom's petrochemical production is projected to increase from today's levels of about 60 million tons per year to more than 80 million tons per year, (Al-Naimi, December 9, 2009). Saudi Arabia alone is committed to producing 10 per cent of the world's petrochemicals output by 2015, (KPMG, 2011). Increased dependency on GCC oil, phosphate, and aluminium exports, could result in further Chinese investments in the region, (Kawach, May 5, 2010).

Overall, the future of Sino-Saudi relations seems to be promising, considering China's overwhelming growing need for energy security. GCC's oil exports to China are expected to grow an average of 3.7 percent annually through to 2030, (Al-Naimi, December 9, 2009). In short, China can't ignore its economic interests in the Kingdom. Saudi Arabia is the largest economy in the Arab States and Middle East. It is also a member of the top 20 economies in the world (G20) and also has a strong influence in the IMF, (see Table 5.3.5).

(Table 5.3.5): Saudi Arabia Regional Power and Global Influence

The largest Economy in the Middle East and North Africa	Saudi Arabia's 2010 GDP was over US\$448.3 billion, about 20% of the total GDP of MENA and almost quarter of the total Arab League aggregated economies. ¹⁰
The Largest Stock Market in the Region	At its peak during February 2006, Saudi Arabia's market capitalisation reached over US\$800 billion. Despite a massive correction, it still represents approximately 50% of region's market capitalisation.
The World's Leading Petroleum Power:	Saudi Arabia has the largest oil production capacity, the largest oil spare capacity and is the largest oil exporter and holder of the largest oil reserves in the world. Saudi Arabia is also the world's largest exporter of petrochemicals and it boasts the fifth largest reserves of natural gas.
The World's Leading Financial Power:	<ul style="list-style-type: none">- Saudi Arabia has one of largest Foreign assets, It's Sovereign Wealth fund by the end of 2010 has US\$444.4 billion- Member of the top 20 economy in the world (G20)- Occupies the eighth place of members' quotas and voting power in the Fund IMF

Source: IMF, World Bank, SWFs Institute and SAMA

5.4 CHINA'S GEOSTRATEGIC INTERESTS

Chinese strategist Dai Bingguo, who plays a major role in Beijing foreign policy making, identified China's "core interests" as: "The PRC's first core interest is the survival of China's 'fundamental system' and national security, second, the safeguarding of China's sovereignty and territorial integrity; and third, continued stable economic growth and social development", (Wu, 2009). In specific terms, Tibet, Xinjiang, Taiwan and South China Sea Islands as well as strategic resources and trade routes. Thus, China regards the situation in Middle East and Saudi Arabia in particular with strategic lenses.

¹⁰ The IMF GDP data for the year 2010 for all 22 members of the Arab League was US\$ 1,697,123 billion

China today maintains good relations with all of the region's potential energy suppliers, (Zweig & Jianhai 2005: 84). China's strategic advantages here are obvious: Beijing is first unencumbered by the historical ballast of a colonial power and, second, it is at present not pursuing a grand design for the region. Without any exaggerated political ambitions, China's leadership appears above all to be motivated by pragmatic considerations: how best to promote China's policy of economic modernisation and to secure the supply of energy it needs, (Ibid). In this regard China's special envoy to the Middle East, Wu Sike, argues that China is not seeking to compete with the United States in exerting influence in the Middle East but is confident about its ties to the region despite recent power transfers, (*China Daily*, March 14, 2011)... Despite these setbacks for the U.S., Beijing is not trying to surpass Washington in exerting influence in the Middle East, (Ibid)... There is no need for comparisons or to think that as the U.S. goes down, China will necessarily fill the void", (Ibid).

5.4.1 Security Interests

While the United States has focused on weeding out global terrorist networks such as Al Qaeda, China is more interested in maintaining security within its borders, (Zhu, May 12, 2009). The collapse of the Soviet Union brought about a second wave of Islamic extremism throughout the Middle East in general, and in Central Asia in particular, which stimulated the rise of what the Chinese call the "three ugly forces": religious extremism, national separatism, and terrorism, (Li, 2009). Since then, and

from China's perspective, the three ugly forces have been the major threat to stability and security in the region. For quite some time, the Middle East has been the source of religious extremism and has served as a hiding place for the three "ugly forces." Therefore, the Middle East has been regarded as the front line in fighting the three "ugly forces" with the aim of preserving the security and stability of the region around China's western borders, (Ibid).

As the ideological centre of the Islamic world, China has attempted to maintain good relations with the Arab world in order to get its support on the Uyghur insurgency in the Xinjiang autonomous region and maintain amicable relations with the Muslims residing in China, (Bajpae, 2006). While China's main efforts in preventing external factors from fuelling the Uyghur insurgency have focused on Central and South Asian states, countries in the Middle East, most notably Saudi Arabia and Iran, have also had an important role to play in quelling the insurgency given their moral and material support. Most notably, the so-called "Salafi/Wahabbi version of Islam", which some scholars regard as "an export" from Saudi Arabia, has played a significant role in the rise of extremists in Pakistan, Afghanistan and the Central Asian republics on China's western borders, (Ibid).

China's relationship with its Muslim population and fear of Islamic extremism is a major factor that impacts on Chinese policy in the Middle East. China cannot ignore the existence and influence of the Muslim states, and cannot ignore their sympathy and support in international affairs. China is home to a large population of adherents of Islam. Chinese official figures indicate there are more than 20 million Muslims from 10 ethnic groups, (Wen, September 7, 2009). The Central Intelligence Agency

CIA World Factbook states that about 1-2 percent of the total population in China are Muslims, (The World Factbook-China, 2011). Furthermore, a 2009 study done by the Pew Research Centre, based on China's census, concluded there are 21,667,000 Muslims in China, accounting for 1.6 percent of the total population, (Pew Research Centre, 2009:7 & 28). Additionally, Chas Freeman argues that "There is a lot of evidence that suggests that the number of Muslims in China is well over 100 million, (Freeman, 2009).

There are Muslims living in every region of China, the highest concentrations are found in the northwest provinces of Xinjiang, Gansu, and Ningxia, with significant populations also found throughout Yunnan province in southwest China and Henan Province in central China. Of China's 55 officially recognised minority peoples, ten are predominately Muslim. The Hui and Uyghur are the largest groups, followed by the Kazak, Dongxiang, Kirghiz, Salar, Tajik, Uzbek, Bonan, and Tatar. Except for the Hui, these other groups are based in northwest China, and most have their own Turkic-related language, and unique culture, (Armijo, 2006). Xinjiang – or "New Frontier" – is a vast province that covers a sixth of China and shares borders with eight countries, including Afghanistan and Pakistan, and in this regard, China shares a 2,800-km (1,740-mile) border with Central Asia but has long remained on the sidelines, keeping a watchful eye on regional power politics from afar, (Golovkina, 2010). The Uyghur, the biggest ethnic minority in the region, are predominantly Muslims, speak a Turkic language and have close cultural ties with other groups in central Asia, (Dyer & Anderlini, 2008).

Domestically, China can ill afford to ignore its many Muslim voices, which have grown more vocal in recent years. Although proportionally small in population, the majority of Muslims are concentrated in the north-western regions bordering Mongolia, Russia, Kazakhstan, Kyrgyzstan, Tajikistan, Afghanistan, and Pakistan, (Gladney, 1994). The Islamic religious and political ideologies from the Middle East and Central Asia often influence the Muslims in China. If the religious ideologies integrate with the minority separatism, it will be a great challenge to the social stability and economic development in Northwest China. Therefore, in both international and internal affairs, Islam challenges Chinese policy-making and academic circles. For example, following the Chinese Government's harsh response to the 1997 Uyghur riots in the Xinjiang city of Yinning, Saudi clerics called upon the Saudi Royal Family to support Chinese Muslim populations financially and diplomatically. The late Sheikh Abdulaziz bin Baz, former grand mufti of Saudi Arabia, proclaimed, "We have a moral obligation to help our Muslim brothers." It was in response to this incident that the Chinese leadership began its charm offensive to co-opt Muslim leaders, (Ibid).

China sees Xinjiang as a security bulwark that projects its influence into Central and South Asia. China believes that the region is exposed to the influence of militant Islamists in nearby countries. Beijing rejects out of hand any demands to grant Uyghur full self-rule or independence, (Reuters, September 5, 2009). Xinjiang, more than any other area of China, is strategically vulnerable. This is partially as a result of its location in one of the most fractious neighborhoods in the world outside the Middle East. Xinjiang is rich in oil, gas, and mineral deposits. The region also contains numerous sensitive Chinese military installations, including some of the

country's premier nuclear research and testing facilities, (Clarke, 2010). Zhang Xiuming, a retired senior security official of Xinjiang, argues that dozens of terrorist organisations and armed groups are based in the crescent-shaped belt to the west of Xinjiang - parts of Kyrgyzstan, Uzbekistan, Tajikistan, Afghanistan and Pakistan - turning the region into a hotbed of terrorism, (Xinhua, September 11, 2010).

While most Uyghur in China want more political and religious autonomy, and most importantly, greater economic parity with the continuous stream of Han immigrants, some Uyghur call China's presence in Xinjiang a form of imperialism, and they stepped up calls for independence—sometimes violently—in the 1990s through separatist groups like the East Turkestan Islamic Movement (ETIM), (Bhattacharji, 2009). Pan Zhiping, a researcher with the Central Asia Studies Institute under the Xinjiang Academy of Social Sciences, says that among the “East Turkistan” forces, the most violent and dangerous is the East Turkistan Islamic Movement (ETIM) - based somewhere along the Afghanistan-Pakistan border. The United Nations and the Chinese Government have labelled it an international terrorist organisation, (Xinhua, September 11, 2010).

In the face of a complicated and changeable international situation, China must soberly consider and work out a strategy and policy to deal with the key area of Islam — the Middle East, (Blumenthal, 2005: 11-19). China's initial strategy was, rather predictably, to focus on acquiring international support for its efforts to maintain domestic stability, which it did by accepting U.S. intervention in Afghanistan (which shares a very short border with China) while linking Uyghur separatists to *Al-Qaeda* in order to pressure the United States to label such groups as terrorist organisations.

The United States ultimately labelled ETIM a terrorist organisation, but did not designate other groups as such, (Fishman, 2011). In the Xinjiang Uyghur Autonomous Region (XUAR), Beijing's strategy is a carrot-and-stick policy. The carrot is the economic development of Xinjiang; US\$300 billion of investments are planned up to 2015. The stick is the threat to eliminate any elements considered to be potentially subversive, (Peyrouse, 2011).

One of the ways in which China has tried to quell unrest in its Muslim dominated region is by building ties with the Middle Eastern states which are the ideological centre of global Islam. States such as Saudi Arabia and Iran have been most active in propagating their version of Islam across the globe by providing resources and training to various organisations, (Pant, 2008). China feels that it is necessary to have their support if it wants to successfully tackle Uyghur insurgency even though it's primarily the Central and Southern Asian states from where Uyghur militants have found support, (Ibid).

Inside China, the July 2009 ethnic riots in Xinjiang – the largest ethnic riots between the Uyghur and the Chinese Han majority since 1949 – demonstrated the gravity of the situation. Renewed violence in the region in late July 2011 confirmed that the problem is far from resolved, (Peyrouse, 2011). But in the Muslim world the Chinese strategy so far appears to be working. The silence from Muslim governments is grounded in growing economic relations but it is also bolstered by China's policy of non-intervention in the internal affairs of its trading partners, (Hauslohner, 2009). Both Riyadh and Tehran have been largely silent about the Chinese Government's post-9-11 crackdown on the Uyghur, particularly in the 2009 riots that swept Urumqi

the capital of Xinjiang which killed hundreds. The silence of the Middle Eastern states on the issue of the Chinese Government's attitudes towards its Muslim population perhaps indicates a measure of success that China has achieved in keeping this issue under control, (Ibid).

Indeed, no muftis¹¹ in the Islamic world have yet found the time to issue any *fatwa* against China. The same applies to the Arab League, governments of Muslim countries and Muslim organisations in Europe and Asia. They have either been mute or their reaction has been too little, too late, (Moises, 2009). Even some *Jihadis* were not very critical towards China. Hamid al-Ali, a prominent Kuwaiti activist and religious adviser well known among *Jihadis* around the globe, has argued that competition between the West and China for allies and resources creates opportunities for *Jihadis* to reduce the West's global influence, which he said was at the heart of the *Al-Qaeda* project. He urges China to seek peace with "Islamic nation" and to stop the persecution of Muslims in China:

"Today it is our duty to stand with the plight of the Uyghur Muslims against Chinese repression, (a) because this is our duty with all the Muslim people; (b) to send a strong message from our nation to China, that the persecution of Muslims in China, will only benefit the West, which will take advantage of this racial discrimination in order to deepen the hostility between China and the Islamic World, then to free the world stage for the ambitions of Western and Zionists." He urges China to seek peace with the "Islamic nation" because it's the nation that will have a future, (Al-Ali, 2009).

In addition, China remains relatively popular among Arab populations, not just its governing elite. A 2010 poll found that China (16 percent) is second only to France (35 percent) among Arabs when asked which country they would prefer to be the world's only superpower. When asked which two countries posed the biggest threat to

¹¹ A mufti is an Islamic scholar who has the authority to issue legal opinions known as *fatwa* about fine points of Islamic law

them, only 3 percent answered China compared to 77 percent that mentioned the United States (Israel ranked highest with 88 percent), (Telhami, 2010). For now, China's position in Xinjiang is more secure than at any previous time in the 60-year history of the PRC. China's sovereignty over Xinjiang is not challenged by any other state, territorial disputes with its Central Asian neighbours have largely been settled, Xinjiang–Central Asian trade is blossoming and Xinjiang has experienced substantial economic development, (Clarke, 2010).

5.4.2 Taiwan Issue

The *New York Times* columnist Thomas Friedman once summarised the two major objectives of Chinese foreign policy in the 21st century: unification with Taiwan and search for oil, (Zhu, 2009). Therefore, China needs the support of Arab countries in the international arena on issues like the “One China policy” and human rights, (Li, 2009). Analysis of the wording of Communiqué Concerning the Establishment of Diplomatic Relations between the People's Republic of China and the Kingdom of Saudi Arabia on July 21, 1990, summaries the Saudi position in Taiwan issue:

“.The Government of the Kingdom of Saudi Arabia recognises that the Government of the People's Republic of China is the sole legitimate government that represents the entire Chinese people.”¹²

China is seeking full support of Arab States regarding Taiwan and the “One China” principle, as well as its position on Tibet and other domestic controversies, (Zambelis,

¹² Communiqué Concerning the Establishment of Diplomatic Relations between the People's Republic of China and the Kingdom of Saudi Arabia, (July 21, 1990), available on: [<http://www.mfa.gov.cn/eng/wjb/zzjg/tyfls/tyfl/2631/t15494.htm>]

2008: 60-72). During the talks held between Chinese President Jintao Hu and Saudi Arabian King Abdullah Bin Abdul-Aziz on January 23, 2006, the Saudi King reaffirmed Saudi Arabia's position with regard to Taiwan: "Saudi Arabia will continue to resolutely pursue the "One China" policy and commit to promoting in-depth development of bilateral friendly cooperative relations", (China's Ministry of Foreign Affairs, January 23, 2006). China also has Arab full support regarding the Taiwan issue. Indeed, during Chinese President Jintao Hu's meeting in Beijing with Arab representatives to the Fourth Ministerial Meeting of the China-Arab Cooperation in May 2010, Arab nations assured the Chinese leader that they would adhere to the "One China" policy and support China's peaceful reunification, and work with China in the future development of the forum in a bid to build the strategic cooperation relationship as a model between states, (Xinhua, May 14, 2010).

5.4.3 Protecting Chinese Interests in the Middle East

China is looking to protect its economic interests in the Middle East by curtailing U.S. unilateral actions. China feels uncomfortable with the current Middle East environment for two main reasons: (a) The preponderance of U.S. military forces in the region; and (b) the U.S. willingness to take unilateral action. These two reasons are interrelated for obvious reasons. The first, the preponderance of U.S. military forces allows the United States to take unilateral action in the region. There is no denying that China is seeking to curtail U.S. power and influence in order to preserve the status quo in the Middle East which provides China with a steady flow of energy,

(Fandy, 2005). Secondly, by expanding its political and economic relations with Saudi Arabia (or the Middle East) and increasing the common interests they share, China may be seeking to influence U.S. behaviour through the Sino-Saudi relationship.

As discussed in earlier chapters, the bulk of China's oil imports come from the Middle East; with China importing nearly 50 percent of its overseas oil imports from the region. Accordingly, the peace and stability of the Middle East is of strategic interest to Chinese political calculations. In recent years, Beijing increased its political activities across several hot spots in the region. China is now the largest exporter to the Middle East, the biggest importer of Saudi oil, the second-biggest importer of Iranian oil, and the largest player in the Iraqi oil game, (Dehghanpisheh, 2010). Thus, the Chinese are making a very delicate act in the region particularly between Saudi Arabia and Iran. On one hand China does not want war/conflict, or sanctions stringent enough to trigger war that would further destabilise the inherently unstable Middle East. This is especially true of the Gulf, the source of most of China's crude oil. On the other hand, the Chinese are not particularly fond of nuclear proliferation that would also destabilise the region, so they nudge Iran to negotiate, (Ibid).

5.4.3.1 Promoting the Role of Responsible Power

China is seeking to enhance the security of its oil imports from the Middle East by increasing its diplomacy in the region. The Chinese Government appears to believe that strong bilateral political relationships can produce greater supply security during

crises, (Ibid: 49). Chinese officials also appear to believe that, by cultivating closer ties to Saudi Arabia, a long-standing U.S. ally, they may compel the United States to take China more seriously as a global player, (Leverett & Bader, 2005: 187-201). The Middle East is also a region where Beijing can demonstrate its role as a responsible power. China's diplomacy in recent years indicates that it regards participation in the peaceful solution of regional disputes as a significant part of its strategy of national image-building, (Jin, 2010).

For all the above reasons China's engagement in the Middle East has enhanced significantly. Over the past decade or so, China's relationships with Arab countries developed very quickly and, with frequent exchanges of high level visits, relations have entered a new stage. At the same time, China has shown a new willingness to be increasingly active and engaged in Middle Eastern affairs. China in 2002, for the first time, appointed a special envoy to travel to regional capitals and promote the Middle East peace process, (Li, 2009). While this has had little significance for the Israeli-Palestinian peace process, it has, nevertheless, demonstrated China's increasing attention to the region, (Bajpae, 2006). This has also been shown by the establishment of the China-GCC Forum in 2003, its active role in the UN peace missions in the Middle East, and the wide engagement in issues related to the region, (Olimat, 2010: 307-335). In 2004, at the initiative of the Arab League, China and the Arab countries established the China-Arab Cooperative Forum, which has provided an important platform for both sides to regularly exchange views on international, regional, and bilateral issues, (Li, 2009). China also held the First Ministerial Meeting of the Strategic Dialogue between China and the Cooperation Council for the Arab States of the Gulf (GCC) in Beijing on June 4, 2010, (*People's Daily*, June 4, 2010).

China also attended the second round of strategic dialogue in Abu Dhabi (UAE) in May 2011, (China's Ministry of Foreign Affairs, May 3, 2011).

The recent turbulence (2011) in the Middle East made China re-evaluate its policy, but up until now Chinese diplomacy is also proving to be proficient in creating a balance between contending interests in the region, and striking a balance between adversaries in the turbulent Middle East. China's economic growth is also one of the main factors leading to the Sino-Middle Eastern strategic partnership, and provides an inspiring model of development, (Olimat, 2010). Besides economic cooperation and national image building, factors shaping China's Middle East policy also include its national identity as a developing country, its belief that international disputes should be resolved by peaceful means, and its interaction with the U.S. and other major world players.

5.4.3.2 Advancing the Middle East Peace Process

China's efforts in the Middle East peace process are also worth mentioning. China is not a part of the Quartet addressing the Palestine-Israel conflict, but since 2002, China has appointed three special envoys on the issue. Their mediating efforts among the parties have helped prevent the escalation of tensions, (Jin, 2010). The multilateral track of the Arab-Israeli peace process that began in Madrid in 1991 provided China with the opportunity to play a constructive role in the peace process and thereby earn political credit with the Arab Gulf States. China participated in the five multilateral

working groups, chaired the Water Committee, dispatched observers to the 1996 Palestinian elections, and bid for membership in the Middle East Development Bank (MEDB), (Li, 2009). China also capitalised on the initial progress toward peace to normalise its relations with Israel in 1992, at a point in time when the risk of offending Arab sensibilities was relatively low.

In this context, Wu Sike, China's Special Envoy to the Middle East, argues that China can play a role in two aspects. Firstly, China can advance the Middle East peace process through bilateral engagements. China has maintained good bilateral relations and mutual trust with related countries in the Middle East. China can push forward related work through bilateral channels. Secondly, China can conduct some work through the United Nations and at other multilateral occasions, (Wu, 2009).

5.4.3.3 Resolving Iran's Nuclear Standoff Peacefully

China and Iran first established diplomatic relations in August 1971. The relationship continued even after the 1979 Islamic revolution, (Canning, 2007: 47-63). From the Chinese perspective, Iran is a major power in the Middle East region. With a population of nearly 74 million, it is the most populous country in the Middle East. Moreover, Iran has the second largest territory in the region. Tehran's military capabilities exceed those of other countries in the region. As a Middle Eastern power, Iran could play a key role in helping China to expand its influence in the region. China's oil security strategy seeks to maintain a stable supply of reasonably priced

energy resources and to ensure the safety of crude oil shipments to Chinese ports, (Chen, 2010: 39-54). China has contradictory interests in the Middle East, specifically regarding the Iranian nuclear issue, and balances those contradictory interests in an effort to protect both. On one hand, Beijing wants access to Iran's fabulously rich but still largely unexploited oil and gas resources to meet China's skyrocketing demand for imported energy, (Garver, 2011: 75-88). On the other hand, Beijing must cooperate strategically with the United States (and Saudi Arabia) to maintain a favourable macro-climate for China's development drive, (Ibid).

In Beijing's view, Iran could play a dual role in strengthening the security of China's oil supply. First, Iran has the natural capacity to be one of China's key oil suppliers. Second, Iran could provide China with a westward source of oil, (Ibid). Iran is strategically located between the Caspian Sea and the Arabian Gulf. It has the world's second largest reserves of natural gas and the fourth-largest reserves of oil. Negotiations have taken place on the construction of a pipeline in Iran to transport oil about 620 miles to the Caspian Sea and link up with the Sino-Kazakh pipeline to China, (Basit, 2008). Another option is to build a pipeline from Iran to Pakistan and then transport energy by rail, road, pipeline or ship to China. If these plans are realised, China will have additional land routes for its energy supplies, which avoid sea routes and the narrow straits of Hormuz and Malacca, (Ibid). Iran has also joined the Shanghai Cooperation Organization (SCO) as an observer. Some observers contend that the SCO is largely a Chinese tool to counter U.S. presence in Central Asia and also to promote Beijing's interests, (Chang, 2010).

Against this background, China's energy ties with Iran are constrained and conditioned by Sino-U.S. cooperation and competition and by the Middle Eastern power structure, particularly the dispute over Iran's nuclear programme. In contrast to what many believe, China's position on the Iranian nuclear issue is consistent. China has always supported and safeguarded the international nuclear non-proliferation system, and opposed the possession of nuclear weapons by Iran. At the same time, Iran is a signatory to the Nuclear Non-Proliferation Treaty (NPT) and has the right to use nuclear energy for peaceful purposes, (Wu, 2009). Beijing's active participation in the six-party mechanism on the Iran nuclear issue since early 2006 is one of many recent two-way interactions between China and the West, and a sign of China's gradual integration into the world, (Jin, 2010). While China has long held that Iran must adhere to the international nuclear non-proliferation scheme and not pursue nuclear weapons, it has also resisted attempts by the United States to gather international consensus to punish Iran by "crippling" sanctions, (STRATFOR, March 17, 2010).

In recently published memoirs China's long-time ambassador to Tehran, Hua Liming, admitted that his diplomacy in Iran after China became an oil importer in the early 1990s had been entirely dictated by energy politics. In 2010, Iran accounted for about 9 percent of China's oil imports, ranking third among China's main oil suppliers after Angola and Saudi Arabia, (Wines, 2010). China relies on Iran's vast energy reserves, perhaps 15 percent of the world's natural gas deposits and a tenth of its oil, to offset its own shortages. The Chinese are estimated to have US\$120 billion committed to Iranian gas and oil projects, and China has been Iran's biggest oil export market for the past five years, (Ibid). On paper, the European Union (EU) still ranks as Iran's

largest trading partner, but if Chinese goods imported in Iran via the United Arab Emirates are considered, China has already overtaken the EU, (Becker, 2010). Although it's a hard political game, China will do its utmost to find a balance between Iran, the United States and Arab Gulf States to protect China's interests in the region, (Ibid), (see Table 4.6.3.3.1).

(Table 5.4.3.3.1): China's Trade with Iran, (2001-2010, US\$ billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
China's Exports	0,88	1,3	2,3	2,5	3,2	4,4	7,3	8,2	7,9	11,09
China's Imports	2,4	2,3	3,3	4,4	6,7	9,9	13,3	19,5	13,2	18,2
China's Crude Petroleum Oils Imports (US billions)	2,0	1,9	2,6	3,5	5,3	7,7	10,4	15,7	9,8	12,05
Total Trade	3,3	3,7	5,62	7,04	10,08	14,4	20,6	27,7	21,2	29,29

Source: General Customs Administration of China and UNCOMTRADE

But economics is not the only reason; China is guided in its foreign relations by two primary principles, both of which reflect domestic priorities. First, China wants to encourage a stable international environment in which it can best pursue domestic development without conflict or other limiting factors. To that end, Beijing is much more likely to pursue diplomatic means that preserve cordiality and de-emphasise conflict in international relations. Secondly, China is extremely sensitive to international policies that "interfere" in sovereign decisions, because of sensitivities to perceived international interference in Taiwan, Tibet, and Xinjiang, (Freeman, 2010).

China would, even without its increasing economic interests in Iran, be less inclined to impose sanctions, (Ibid). In this regard Li Weijian, director of the Research Center

of West Asian and African Studies at the Shanghai Institutes for International Studies, argued that the U.S. tactic to “bribe and threaten” China through its oil trade with Middle East producers will not work. He said: “China has established an oil supply network based on various importers. Iran and Saudi Arabia are part of the multiple sources.” He added that China’s stance on the Iranian nuclear issue is not subject to Beijing’s demand for Iranian oil imports, but based on judgment of the whole picture, (Kang, 2010). Meanwhile, Evron provides a very interesting argument: although China opposes possession of nuclear weapons by Iran, it is interested in continued economic relations with it and does not wish to be perceived as doing Washington’s bidding. On the other hand, China also does not intend to allow Iran to jeopardise its relations with the U.S. It is therefore expected that it will continue to manoeuvre to avoid taking a strong stand or playing a significant role in the matter”, (Evron, 2009).

China’s strong relations with Iran do not indicate that Beijing is on a collision course with Saudi Arabia’s agenda in the region. On the contrary, it is not China’s veto power in the Security Council over sanctions against Iran that matters, but that China’s balanced and perceived fair diplomacy could be an influence on Iran. The key to China’s diplomacy is to hold a firm line on non-proliferation while avoiding prejudging Iran’s nuclear intentions, (Afrasiabi, 2010). China emphasises Iran’s right to develop peaceful nuclear programs, while urging Iran to put its nuclear program under the watch of the IAEA. From the Chinese perspective, China’s position on a peaceful solution to Iran’s quest for nuclear power benefits all, instead of just protecting its oil supply, as perceived by many.

That is why China's approach is shared by many Muslim and Arab countries, including Saudi Arabia. The Saudis seem to understand the Chinese position but hold deep concerns of the Iranian intentions. Indeed Saudi Prince Turki Al-Faisal, the former Saudi Arabian Ambassador to the US and former Head of Saudi Intelligence, in a speech in November 2010 at the Carnegie Endowment for International Peace, said: "No one denies that a nuclear Iran is a major international danger, but claiming that the U.S. must take military action against Iran to push forward the Israeli-Palestine peace process is to attempt to harvest apples by cutting down the tree ... A war over Iran's nuclear program would be calamitous and not just catastrophic ... It would turn back the clock on peacemaking across the Middle East; from Iraq to Israel ... Iranians have to be aware of the explosive nature ... of pursuing their present course of enrichment", (Al-Faisal, November 4, 2010).

China also supported the Arab draft in building a Middle East nuclear-weapon-free zone, maintaining that Israel should join the NPT as a non-nuclear-weapon state at an early date, and put all its nuclear facilities under the comprehensive safeguards of the International Atomic Energy Agency (IAEA), (Xinhua Agency, September 17, 2010). In addition, China supports the United Arab Emirates' (UAE) position to regain the islands occupied by Iran in the Gulf. Recently the Speaker of UAE's Federal National Council (FNC), Abdul Aziz Abdullah Al Ghurair, hailed China's stance in support of the UAE side in the issue of its three Islands - Lesser and Greater Tunb and Abu Musa - that are currently under Iranian occupation. He held in high esteem China's initiative to mediate between UAE and Iran to resolve the dispute by peaceful means consistent with international law, (WAM, September 21, 2010). To cite another example concerning the Arab Gulf States, in November 2010, Iran summoned

China's ambassador to protest after organisers of the 16th Asian Games in Guangzhou (China) used the term "Arabian Gulf" at the opening ceremony, (Middle East Online, November 17, 2010). In short, China's policy toward Iran is based on realistic goals within a strategy that aims to promote the diversification of energy sources and is not directed against the United States.

5.4.3.4 Maintaining the Stability of Iraq

The view from Beijing is that a stable Iraq is good for the region and for China's core economic interests. Indeed, China's position in Iraq evolved quickly, from among the most outspoken of critics of the 2003 U.S.-led invasion to topple Saddam Hussein, to emerging as one of the biggest economic beneficiaries of the war, snagging five lucrative deals. While western firms were largely subdued in their interest in Iraq's recent oil auctions, China snapped up three contracts, shrugging off the security risks and the country's political instability for the promise of oil, (Salaheddin, 2010).

Beijing is betting big in Iraq, which many Western companies are avoiding. In November 2009, the Chinese National Petroleum Co. (CNPC) won a large stake in a US\$15 billion deal to develop the Rumaila oil field in southern Iraq, thought to be the second largest in the world. That followed a US\$3 billion deal to develop the Ahdab oil field in 2008. And two other Chinese firms just closed a deal on a large oil field in eastern Iraq. Chinese companies have also shown much greater willingness to take on risk by placing their own nationals in war zones: CNPC has an office in Baghdad

partly led by Chinese nationals, (Dehghanpisheh, 2010). Again, China's policy in Iraq is directed mainly towards energy as part of its oil imports diversification.

5.5 CONCLUSION

This chapter has attempted to decipher Chinese intentions toward Saudi Arabia. The main question it attempted to address was whether Chinese actions were in accordance with the offensive realism theory or economic interdependence model. As stated earlier in the chapter, if China is acting in the offensive realism model: (a) It should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence; (b) Encouraging Saudi Arabia to shift their political allegiance from the United States over to China. If China is acting in the economic interdependence model, it should be: (a) Interacting economically with Saudi Arabia in a manner which makes economic sense (i.e. profitable); (b) Developing a Sino-Saudi political relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship.

China's political objectives of the Sino-Saudi relationship are also closely aligned with the economic interdependence school of thought for numerous reasons. Firstly, China's political policies are geared towards increasing its energy security. China is looking to develop closer Sino-Saudi ties so Saudi Arabia remains a vital long-term energy source and to keep Chinese energy sources diversified. Secondly, China is also

looking to expand its trade market in Saudi Arabia. Thirdly, China is seeking full support of Saudi Arabia in the international arena on issues like the Taiwan as well as its position on Tibet and other domestic controversies in the international arena like human rights. These three main Chinese objectives are economic and defensive in nature which aligns Chinese actions closer to the economic interdependence model rather than the realism model. If China was seeking to decrease U.S. influence in the Middle East, its objectives in the Sino-Saudi political relationship should not be mainly economic in nature and should be geared towards weakening the U.S.-Saudi political relationship; thereby increasing the amount of Chinese influence in Saudi Arabia. There has been no indication that China has been taking such actions.

While there is no denying that China is looking to curtail U.S. unilateral action in the Middle East region, even this intention fits within the economic interdependence model. China is seeking greater influence in the Middle East not because it wants to expand its powers at the cost of the United States, but because it is seeking to prevent the United States from taking unilateral actions which may damage Chinese economic interests. This indicates that China is mainly concerned about economic matters and not on balance of power issues; therefore, China's actions fit more closely along the lines of the economic interdependence model. China's expectations of future relations and trade with the Middle East in general and Saudi Arabia in particular are high; subsequently they will likely pursue policies that will enhance security in the region.

CHAPTER SIX

SAUDI ARABIA HEDGING FOR THE FUTURE

6.1 INTRODUCTION

On September 23, 1932, the Kingdom of Saudi Arabia was founded by King Abdulaziz. The U.S. officially recognised the Saudi Kingdom in 1931, though their mutual interests were not well defined until 1933 after Saudi Arabia signed an oil concession with the U.S. firm of Standard Oil of California, (Brown, 1999: 9-56). Despite the recognition of the Kingdom in 1931, no American diplomat visited in a formal capacity until 1940, when the U.S. envoy to Egypt, Bert Fish, was co-accredited to the Kingdom of the *Hijaz* and *Najd* and Its Dependencies, as it was then called, (Hart, 1998: 35-37). In mid-February 1945, King Abdulaziz (Ibn Saud) met with the American President Roosevelt in the Great Bitter Lake, between the north and south part of the Suez Canal on aboard the USS Quincy, (Yergin, 1991), (see Table 6.1.1).

When the founder of Saudi Arabia, King Abdulaziz (Ibn Saud), died in 1953, he was succeeded by his eldest son, King Saud (1953-1964). However, Ibn Saud also named his second-eldest son, Faisal, crown prince. Since then the throne has passed from elder brother to the next in age - and Ibn Saud had thirty-four sons who survived him, born to seventeen of his twenty-two wives. After Saud came his half-brother King Faisal (1964-1975), then King Khalid (1975-1982), then King Fahd (1982-2005), and now, King Abdullah (2005 -), (Henderson, 2006 and Royal Embassy of Saudi Arabia, Washington D.C, 2011).

(Table 6.1.1): Chronology of Establishment of Saudi-U.S. Relations

1932 July 14,	First oil concession in Saudi Arabia granted to Standard Oil of California
1932 September 23,	Unification of the modern Kingdom of Saudi Arabia under the leadership of King Abdulaziz Bin Abdulrahman Al-Saud.
1933, November 7	Agreement signed establishing diplomatic relations between Saudi Arabia and the United States; Also covers commercial relations and navigation.
1938, March 3	Oil found in large quantities in the Eastern Province.
1940, February 4	U.S. Minister Extraordinary and Plenipotentiary in Cairo, Bert Fish, accredited as Chronology of Saudi-U.S. Relations envoy to Saudi Arabia.
1942, April 13	James S. Moose, Jr., sent to Jeddah as chargé d'affaires of the first U.S. legation in the Kingdom.
1943, October	Prince Faisal and Prince Khalid meet with President Roosevelt in Washington; It is first high-level Saudi Arabian delegation to visit the United States.
1944	Saudi Arabian legation opens in Washington, later raised to the rank of embassy; U.S. consulate established in Dhahran, Saudi Arabia.
1945, February 14	King Abdulaziz and President Franklin D. Roosevelt meet on board the USS Quincy in the Great Bitter Lake of the Suez Canal.

Source: Royal Embassy of Saudi Arabia, Washington D.C, (July 2011)

Ever since the 1940s, the United States and Saudi Arabia have shared a close beneficial relationship. An article written in the *Middle East Insight* by then Ambassador of Saudi Arabia to the United States, Bandar bin Sultan, as introduced into the Congressional Record on March 12, 1996, summarised the US-Saudi relations in a few words:

[T]he historic meeting between King Abdulaziz Al-Saud and President Franklin D. Roosevelt aboard the USS Quincy . . . launched the special relationship between the Kingdom of Saudi Arabia and the United States of America...Two people who work so closely together toward the common goals of security, prosperity, and economic advancement will surely remain friends, and partners, far into the future, (Bandar, 1996).

While Kaiser and Ottaway described the Saudi-American relationship in very interesting words “the relations was always more like an arranged marriage than a romantic union ... the alliance has been convenient for both parties, giving Saudi

Arabia the security it craved in a dangerous neighbourhood while assuring the United States a reliable supply of oil at - nearly always - an affordable price”, (Kaiser, Ottaway 2002). Indeed, the strategic features of the relationship are manifest in many ways. Chief among them are the contracting of American corporations to help build military facilities in Saudi Arabia and to train local military personnel and the sales of weaponry to the Saudi state by American industries, (Conge, Okruhlik, 2009: 359-374). Economically, Saudi Arabia agreed to play a vital role in providing the United States with enough oil to meet its demands at a reasonable price. Militarily the United States provided Saudi Arabia with a security guarantee to protect Saudi Arabia from international threats.

During the Cold War the U.S.-Saudi relationship has been characterised as “oil for security.” The U.S. energy needs were partially met by the first oil producer country in the world in exchange for guaranteeing the long-term security of the Kingdom under the U.S. military umbrella, (Petrini, 2006: 65-82). The security guarantee that the United States provided became more vital to the Saudis as time passed, particularly after the Iranian Revolution and also after the invasion of Kuwait by Iraq. Aarts identifies four pillars that traditionally characterised the U.S.-Saudi relationship. The first two are energy and security. The third is the Saudi moderate policy toward the Israeli-Palestinian conflict; and the last pillar concerns the Saudi “balancing” role in the Middle East, which was evident particularly during the Cold War, (Aarts, 2005: 399-429).

This mutually beneficial relationship continues. However, the attacks on the United States on September 11, 2001 (9/11) have put a strain on this relationship. In addition

the rising anti-American sentiment in the Middle East, as a result of the unpopularity of the occupation of Iraq and Afghanistan coupled with the continued Israeli occupation of Palestine, has further strained the U.S.-Saudi relationship. The strains imposed on the US-Saudi relationship have provided China with an opportunity to develop closer relations with Saudi Arabia. Over the past few years, Arab countries (including Saudi Arabia) have diversified their foreign policies by shifting their focus from the West to the East as a response to changing international and regional situations. This is partly a means to neutralise American pressure, and partly because Asian economies, particularly China and India, have developed rapidly. The Arab countries believe that the successful Asian economies have provided them with an alternative development model and/or markets, (Li, 2009).

From the Saudi Arabia perspective, 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. Saudi Arabia has recognised 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, notably China and India. Furthermore, by distancing itself from a disproportionate reliance on the U.S. energy market, Saudi Arabia will be in a better position to extricate itself from the political costs of a close relationship with the United States, (Douglas & others, 2006).

6.2 SAUDI ARABIA'S DESIRE FOR SECURITY

Saudi Arabia's primary parameter is its desire for security, and the survival of the Saudi Royal Family. Threats to Saudi Arabia have shifted from Nasser's Egypt in the 1960s to Iran in the 1980s to Iraq in the 1990s and to internal and external terrorism after 2001, (Anderson, 2004). For these reasons, Saudi evaluations of interest put security concerns squarely at the top of its priorities, (Ibid). The 1979 Iranian revolution and the Soviet invasion of Afghanistan helped fuel a decade of collaborative U.S.-Saudi foreign policy efforts, including shared support for anti-Soviet mujahidin fighters in Afghanistan and for Saddam Hussein's war against Iran, (Blanchard, 2010). Throughout the 1980s, the two countries worked together, at first quietly, and then more visibly, to roll back Soviet aggression in Afghanistan and Iranian ventures throughout the Gulf and in Iraq, (Bronson, 2009: 82).

During the 1990s the Soviet forces were driven out of Afghanistan; the Iranian revolutionary momentum was blunted; the Cold War was won by the Americans, with support from Riyadh and elsewhere, (Gause, 2009: 75). In his own words Prince Saud AL-Faisal Foreign Minister of the Kingdom of Saudi Arabia described the Saudi-U.S. relations during the Cold War:

“...We have proven to be a reliable ally during the Cold War and our contributions in the political, security and especially in the economic spheres, attest to that beyond any doubt”, (Prince Saud Al-Faisal, September 30, 2003).

According to Niblock two developments emerged which were to change the dynamics of the U.S.-Saudi relationship: the Iraqi invasion of Kuwait in August 1990 (leading to the Gulf War of 1991) and the disintegration of the Soviet Union. The latter brought to an end the perceived Soviet security threat to the region. The confrontation

with Iraq deepened the military and political cooperation between Saudi Arabia and the United States. The Saudi decision to invite U.S. military forces onto Saudi territory, taken within 10 days of the Iraqi invasion, was unprecedented in Saudi history, (Niblock, 2006: 151). For the Saudis the period of the entire nineties was devoted to dealing with the threat of Iraq and Iran. Economic interest largely defined the relationship between China and Saudi Arabia in that era, as Saudi Arabia's security concerns were met by the United States, and China's concept of centrality led to a focus on the domestic policy of economic development.

Then we witnessed the second development which was the disintegration of the Soviet Union and the end of the Cold War. The United States was now no longer in need of Saudi support in the confrontation with Soviet communism, (Ibid). At that time some basis for Saudi-U.S. cooperation on the global level still existed. Niblock argues that Saudi Arabia's Islamic role had three possible uses for the United States, within the New World Order. The first was as a counter to Russian influence in the Caucasus and Central Asia. The second was to prevent the expansion of Iranian religious influence (again, mainly in the Caucasus and Central Asia), given that Iran was also seeking to use religious channels to strengthen its political position. The third was to bring the excesses of radical Islam under control, through spreading a more conservative vision of Islam, (Ibid).

It is safe to say that the Gulf War of 1990-91 was the high point of Saudi-American cooperation, with the military and civilian infrastructure built using Saudi petrodollars and American construction companies during the 1970s and 1980s, (Gause, 2009: 75). American presence in Saudi Arabia did not come without costs. There had

been a decade of drift in the U.S.-Saudi security relationship, highlighted by the obvious discomfort of the House of Saud with the continuing presence of U.S. forces operating out of Prince Sultan Air Base. With the presence of these forces seized upon for criticism by emerging domestic political forces in the Kingdom, the House of Saud found it could no longer quietly conduct business with the Americans out of the public view, (Crooke, 2010: 7-20).

Changes to the region's security environment also flowed from a variety of incidents. Firstly, in 1996 and 1998, bin Laden issued a fatwa calling on Muslims to kill Americans, even civilians. In August 1998 al Qaeda terrorists attacked the U.S. embassies in Kenya and Tanzania, (Williams, 2011). Subsequently, the Salafi jihadist issue began to cause tensions in the Saudi-American relation, (Niblock, 2006: 167). Secondly, Niblock argues that the 9/11 attacks became the central issue in the greatest crisis the relationship had experienced since the 1973-74 oil embargo, if not since the inception of the relationship. The 9/11 terrorist attacks and the U.S.-led war on terror caused both Riyadh and Washington to re-evaluate their "special relationship", (Ibid). The Kingdom had moved within a few months from being a key friend and partner of the United States to having the status of a problem country, (Ibid). Even worse than that, for example, Laurent Murawiec of the Rand Corporation to the U.S. Defence Policy Board on July 10, 2002, described the Kingdom as an enemy of the United States, (Prince Saud AL-Faisal, August 6, 2002). In response, Saudi Foreign Minister Saudi Saud AL-Faisal described the Murawiec statement as "pure fiction." And added: "...It is unfortunate that there are people in some quarters who are trying to cast doubt and undermine the solid and historic ties between our two countries. I am confident that they will not succeed", (Ibid).

One symbol of the changed relationship between the two countries in the period following 9/11 was Saudi Arabia's non-participation in the two major U.S. military operations in the region at that time: those in Afghanistan (from November 2001) and in Iraq (from March 2003), (Ibid). These developments pushed Saudi Arabia and China politically closer regarding the use of force by the Americans. For example, Chinese Foreign Ministry spokeswoman Zhang Qiyue told reporters in January 2003 that China supported a Saudi Arabian initiative to dissuade the United States from attacking Iraq, adding it remained committed to a political solution and "some countries, like Saudi Arabia, have urged a peaceful settlement...These efforts are in the spirit which China has espoused...China's consistent policy to seek a political and diplomatic settlement within the framework of the United Nations remains unchanged", (Middle East Online, January 16, 2003).

After the *AL-Qaeda* attacks, it was no longer realistic to imagine that Saudi religious influence could be used to promote U.S. security and political interests within the region, (Ibid). Ever since September 11, 2001, when it emerged that fifteen of the nineteen men who carried out the terrorist attacks on New York and Washington were Saudi citizens, the American media had been full of tales of Saudi laxity in fighting terror. Public anger at the Saudis had also begun to be reflected in the workings of the U.S. Government. Anti-Saudi sentiment in Congress was also running high, and there has been a steady drumbeat of opposition to the presence of American forces on the Saudi peninsula, (Luft & Korin, 2004). Saud AL-Faisal, Saudi Arabia's long serving foreign minister in a public speech, summarised the situation:

..Saudi Arabia has since (9/11) been forced to witness a distressing change in the way Americans perceive our country. We are concerned by what we believe is an organised campaign waged against the Kingdom by some in the United States", (Prince Saud Al-Faisal, September 30, 2003).

Meanwhile, the retention of the U.S. bases in the country added fuel to the fire of those opposing the regime that used the U.S. presence as a rallying point and an example of the disloyalty and deviance of the Saudi regime, which opponents said sullied the sacred soils of Saudi Arabia with U.S. military personnel, (Friedman, 2004). To complicate the situation even further, in 2003, following the defeat of Saddam Hussein, the Bush Administration responded to this pressure by withdrawing the bulk of those forces, relocating them in nearby Qatar. Though it was done quietly, the American military departure may turn out to be a major strategic turning point. It certainly has created new opportunities for both the Saudis and the Chinese to strengthen their relations, (Ibid). Furthermore, due to the unfolding revelations by the IAEA that had long been suspected by many – that Iran is engaged in a comprehensive and systematic program to develop fissile material outside of international oversight, this has created an incentive for the Saudis to work together with the Chinese. Last, but not least, is an emerging and complicated domestic political landscape within the Kingdom that is forcing the ruling family to play to its varied “publics”, yet at the same time it is waging an increasingly active war against an entrenched militant infrastructure, (Crooke, 2010). This has been an important factor in pursuing the relations with China in order to assure the Saudi public in regard to the balanced foreign policy of their countries.

In Saudi Arabia itself, growing U.S. animosity has fed doubts about America’s dependability as an ally, if not outright fears of Washington’s long-term intentions. Many worry, with reason, that the liberation of Iraqi Shiites from Saddam Hussein’s oppressive rule may ignite discontent among the Kingdom’s own Shiites, who happen to be situated geographically atop of the largest oil fields, (Luft & Korin, 2004).

Equally disturbing for many Saudis is the American effort to revive Iraq's shattered oil industry. The infusion of an additional 6 million barrels per day into world oil markets will inevitably mean fewer petrodollars for the economically stretched Kingdom, (Ibid). In addition, Saudi public opinion, never particularly pro-American because of the Arab-Israeli issue, among other things, reacted very negatively to the American wars in Afghanistan and Iraq. These were the makings of a serious rift, and opened the doors for expanding Sino-Saudi relations, (Gause, 2009: 75). George Friedman, CEO of the private intelligence corporation "Stratfor", goes further to point out that, one of the key goals of the U.S. war in Iraq was to put increased pressure on - - and effect change in -- Saudi Arabia, (Friedman, 2004). These developments promoted a strong Saudi response and opposition to Americans to reform the Middle East, for example, the interesting words from the Saudi Foreign Minister reflected that sentiment: ". Reform is a response to the aspiration of the people and their needs, and not a theory in the head of some planner. It is for their benefit in order to provide them with good governance and transparency", (Prince Saud Al-Faisal, September 30, 2003).

It is in this context that Riyadh has begun courting an Asian alternative, (Pant, 2006: 45-52). The Saudi leadership was disturbed by the anti-Saudi backlash in both the "Congress" and in U.S. public opinion following the September 11 attacks. As a result of these concerns, the Saudis have been pursuing a "hedging strategy" toward the United States, its traditional partner, by developing a more robust strategic relationship with China, (Leverett & Bader, 2005-06: 187-201). For example, the Saudi foreign minister Saud AL-Faisal told an audience in Bahrain in December 2004 that the security of the region should not depend on the United States, but should stem

from guarantees, he went on to say "...Provided by the collective will of the international community through a unanimous declaration by the Security Council guaranteeing the sovereignty, independence and territorial integrity of all the countries of the Gulf and promising to act forcefully against any external threats", (Ibid).

Shortly after that Prince Saud AL-Faisal expressed his concerns strongly to an American audience at the Council on Foreign Relations in New York in April 2004: "Saudi Arabia and the United States have enjoyed a well known 'special relationship' which, over a period of 70 years, had developed and blossomed into a strategic alliance that benefited both countries. Recently this relationship has come under extreme strain. A critical juncture has been reached, and unless joint efforts are brought to bear to redress and rectify the underlying causes, the damage may be grave", (Prince Saud Al-Faisal, April 27, 2004). He went on to lash out at the Saudis critics: "The ensuing onslaught on Saudi Arabia has been intense and at times purposefully malicious...Instant so-called experts sprang from nowhere and everywhere, most of whom have never even visited Saudi Arabia, claiming a gift of analysis denied to mere mortals. By using such words as jihad, Wahabbism, madrassa, they endow them with emotively negative contents that surpass the realm of objectivity and defy any sense of reality. These are at the core of the attacks for what may be termed 'Saudi bashing'", (Ibid).

Meanwhile Osama bin Laden had ambitious plans to follow up the attacks of 9/11. He had a third front (after Afghanistan and Iraq) in mind: his own homeland in Saudi Arabia, where he would wage a terrorist campaign with the intention of driving the

United States and its British allies out of Islam's holy land and of toppling the "apostate" Saudi monarchy, (Riedel & Saab, 2008: 33-46). This development changed the landscape of the Saudi-U.S. relations. The 2003 terrorist attacks in Saudi Arabia mobilised the Saudi regime to take an active role in confronting the Salafi jihadist movement with cooperation with the United States on intelligence sharing and steps to dry up the sources of financial support for jihadist groups, (Gause, 2009: 76). Within this context, Aarts identifies also a fifth pillar characterising the Saudi-U.S. relationship in addition to the four enlisted above, namely the fight against terrorism. He argues that 9/11 produced a new common ground linking Riyadh and Washington. In his view, the war on terror is likely to encroach further rather than divide the U.S. and Saudi Arabia, (Aarts, 2005).

Despite the Chinese limited involvement in this regard, they offered a very much needed political support to Saudi Arabia, On November 9, 2003, President Jintao Hu sent a message to King Fahad, strongly condemning the terrorist bombing in the Saudi Arabian capital, Riyadh, which caused mass casualty of innocent civilians. Hu expressed sincere condolences to the wounded and families of the victims, (China's Ministry of Foreign Affairs, November 10, 2003). Hu emphasised that, "The Chinese government is firmly opposed to terrorism in any form and is willing to make unremitting efforts with Saudi Arabia and other members of the international community to safeguard the world's peace and security", (Ibid).

On the other hand the situation between the Saudi Arabia and the United States improved further when in its final report, released on July 23, 2004, the U.S. National Commission on Terrorist Attacks upon the United States (the 9/11 Commission)

described Saudi Arabia as having been “a problematic ally in combating Islamic extremism.” However, the Commission found “no evidence that the Saudi government as an institution or senior Saudi officials individually funded AL-Qaeda”, (Blanchard, 2010). The report acknowledged increased Saudi efforts in that regard after mid-2003, when terrorists began attacking targets in Saudi Arabia with more frequency. The Commission concluded that the Saudi Government had become “locked in mortal combat with Al Qaeda”, (Ibid).

Other developments put the Saudis in the driving seat, with Iraq in a mess and Iran a continuing challenge to American power and goals in the region, the U.S. could not afford a further deterioration of its only working relationship with a major Gulf power, (Ibid). Indeed, increased official counterterrorism cooperation and shared concerns about Iranian foreign policy have provided a new strategic logic for U.S.-Saudi security relations since 2003. Long-standing defence ties remain intact, and U.S. arms sales have continued, with over US\$18.7 billion in potential foreign military sales to Saudi Arabia approved by the executive branch and Congress since 2005, (Ibid). The relations recovered quickly in May 2008 with the visit of President Bush’s to Riyadh to commemorate the 75th anniversary of the establishment of U.S.-Saudi relations. On the eve of the visit the then U.S. National Security Adviser, Stephen Hadley, argued that the U.S.-Saudi relationship was in “pretty good shape”, (Ibid).

The culmination of the improvement came in June 2009 when President Obama visited Saudi Arabia (it came almost four months after the visit of the Chinese President on his first leg of a Mideast trip). President Obama said that he was

confident that the United States and Saudi Arabia can “make progress on a whole host of issues of mutual interests.” He went on to say that he was “struck by his [the king’s] wisdom and his graciousness. Obviously the United States and Saudi Arabia have a long history of friendship. We have a strategic relationship”, (CNN, June 3, 2009). Tellingly, in that visit President Obama greeted the King’s of Saudi Arabia with a full bow from the waist, which was strong indication of the shift in American policy towards Saudi Arabia.

Nevertheless, Riyadh and Washington differ, often widely, on preferred strategies. For example, Riyadh was not supportive of the American decision to significantly reduce forces in Iraq, believing that the decision was premature and would contribute to further chaos. At the same time, Riyadh was deeply concerned about the American decision to surge forces into Afghanistan. The Saudi Government has also been quite vocal in its critique of the administration’s approach toward the Israelis and Palestinians, (Bronson, 2009: 84). Chief among all differences is the growing assertiveness of Saudi Arabia as it confronts Iranian influence in the region. The Saudis are very concerned with U.S. policy or as the Saudi expert and a consummate insider Nawaf Obaid, puts it: “Riyadh fights a cold war with Tehran, Washington has shown itself recently to be an unwilling and unreliable partner against this threat”, (Obaid, 2011). In this regard a secret document sent by David Rundell, the Deputy Chief of U.S. Mission in Saudi Arabia, and leaked by “*WikiLeaks*” in November 2010 summarises the Saudi American differences in very interesting words:

While U.S.-Saudi relations have improved dramatically since their post-9/11 nadir, differences remain over U.S. Middle East policies. The Saudis have three principal issues areas of concern about U.S. policies: (a) As the author of the 2002 Arab Peace Initiative, King Abdallah risked his personal prestige to advocate a comprehensive Middle East peace as the “strategic option” for the Arabs, only to be frustrated by what he saw as U.S. reluctance to engage over the next seven years. (b) Similarly, in the Saudi view, we ignored advice from the King and Foreign Minister against invading Iraq. In the words of Saudi Foreign Minister Prince Saud AL-Faisal,

“Military intervention in Iraq and Afghanistan has tilted the (regional) balance of power towards Iran.” (c) Finally, the U.S. debate over whether and how to engage Iran has fuelled Saudi fears that a new U.S. Administration might strike a “grand bargain” without first consulting Arab countries bordering the Persian Gulf, (Wikileaks, March 31, 2009).

These differences surfaced strongly in 2011 due to the Saudi king’s anger at Washington’s response to uprisings across the Arab World, especially its abandonment of Hosni Mubarak, the deposed Egyptian president, who was a long-time Saudi and U.S. ally. On the key political issues Abdullah Askar, the Vice Chairman of the Foreign Affairs Committee of the Saudi Arabia’s Consultative Council, or *Majlis Shura*, in Riyadh, told the *Los Angeles Times* recently “the Obama Administration doesn’t really listen to the Saudi views”, (Richter and Banerjee, 2011). In May 2011, Saudi grievances were laid out in a *Washington Post* op-ed by Nawaf Obaid, a senior fellow at the King Faisal Center for Research and Islamic Studies headed by former Saudi intelligence chief Prince Turki AL-Faisal. Describing a “tectonic shift” in the Saudi-U.S. relationship, he argues that: “Riyadh intends to pursue a much more assertive foreign policy, at times conflicting with American interests”, (Obaid, 2011). He went on to say: “For more than 60 years, Saudi Arabia has been bound by an unwritten bargain: oil for security...American missteps in the region since September 11, an ill-conceived response to the Arab protest movements and an unconscionable refusal to hold Israel accountable for its illegal settlement building have brought this arrangement to an end”, (Ibid). Obaid also echoed some of the criticisms made in 2010 by Prince Turki al Faisal, a former ambassador to the United States, who said that “negligence, ignorance and arrogance” had cost America the “moral high ground” it held after 9 / 11, (Lister, 2011).

Deeply frustrated with the Obama Administration’s stalled efforts on Israeli-Palestinian peace, Riyadh is pushing for UN recognition of Palestinian sovereignty,

an approach the White House is determined to thwart, (Richter and Banerjee, June 19, 2011). In July 2011 Prince Turki AL-Faisal Prince Turki al Faisal, the former Saudi intelligence chief and ambassador to the United States, and who holds now no official position but is part of the ruling family issued in the *Washington Post*, a thinly veiled warning to Washington of further looming problems:

There will be disastrous consequences for U.S.-Saudi relations if the United States vetoes UN recognition of a Palestinian state...American leaders have long called Israel an 'indispensable' ally. They will soon learn that there are other players in the region - not least the Arab street - who are as, if not more, 'indispensable' (*Washington Post*, June 10, 2011).

The United States and Saudi Arabia are drifting apart on energy, too. For decades both countries saw mutual benefit in holding down oil prices. But now, with Riyadh stepping up foreign aid and embarking on a US\$ 130-billion domestic subsidy program to prevent internal unrest, it needs steeper oil prices (Richter and Banerjee, June 19, 2011). Riyadh is less certain about the strength of its alliance with Washington and may thus be less willing to incur the costs and risks involved in contributing to the U.S.-Saudi partnership in these ways, (Robert & Michael, 2011).

This shift doesn't mean the end of the 70-year-old U.S.-Saudi alliance, but it does mean a further loss of influence for Washington in the Middle East, (Richter and Banerjee, June 19, 2011). Thomas Lippman, a scholar at the Middle East Institute in Washington and an expert on US-Saudi relations, argues that this marriage of convenience is likely to survive the latest strains, "Where are they going to go? When there is real danger, who are they going to call? Beijing? Moscow? Islamabad? I don't think so", (*Financial Times*, June 17, 2011). While David Rothkopf, a foreign policy analyst and former Clinton administration official, goes on similar lines: "It's a fraught but critical relationship...My sense is that they're trying to manage it because of what they used to call during the Thatcher era the 'Tina' phenomenon - There Is

No Alternative”, (Ibid). Furthermore, Tom Donilon, the national security adviser in the U.S., emphasised recently that the U.S.-Saudi relationship has remained “in pretty good shape” despite “scratchy” disagreements over Arab Spring revolutions, (AFP, September, 16, 2011). Tom believes that Washington and Riyadh “have a shared interest in seeing that no country or force in the region seeks or tries to achieve dominance...We have a very important shared interest in seeing restrictions on weapons of mass destruction proliferation in the region. We have a shared interest in counterterrorism cooperation. We have a shared interest in the pursuit of peace. We have a shared interest in a stable supply of energy and in a healthy global economy. And that is the basis on which we work with the Saudis”, (CNN, 2011).

Indeed, the two countries continue to cooperate closely on counter-terrorism, and have collaborated on the political crisis enveloping Yemen that has raised the spectre of a resurgent Al Qaeda. The United States is selling the Saudis US\$60 billion (with the upgrade to the Saudi navy it could reach US\$90) in arms and other military hardware in a multiyear deal, the largest U.S. weapons transaction ever, (Richter and Banerjee, June 19, 2011). The United States and Saudi Arabia are quietly expanding defence ties on a vast scale, led by a little-known project to develop an elite force to protect the Kingdom’s oil riches and future nuclear sites, (Burns, 2011). Bremmer of the Eurasia Group says the United States does hold important cards - through multi-billion-dollar arms contracts and long-established relationships in the oil industry. And regional analysts say that ultimately Saudi Arabia would likely appeal for and get U.S. help in any showdown with Iran, (Lister, 2011). In a secret letter sent to U.S. Secretary Hilary Clinton on her visit to Saudi Arabia on February 2010 and published by “Wikileaks”, U.S. Ambassador James B. Smith to Saudi Arabia wrote that: “Saudi

leadership still sees the United States as its most important strategic partner and guarantor of its stability”, (Wikileaks, February 11, 2010).

As for China, in the post 9/11 era, the economic interests still largely defined the Sino-Saudi relations but they have developed rapidly, coupled with frequent high-level exchanges with growing mutual political trust. It is clear that China was not looking to provide Saudi Arabia with the protection it gets from the United States, which maintains air, naval and army bases in the Gulf, (Meyer, 2010). Shi Yinhong, a professor of international relations at *Renmin University* in Beijing, argues that increasing economic ties to Saudi Arabia: “Will play some role in gradually eroding American preponderance over that country, but this is not a very elaborate and conscious objective of China’s relationship with Saudi Arabia..This is a by-product. China’s objective is energy”, (Ibid). In this context, Prince Turki AL-Faisal noted in a discussion with *USA Today*, that: “China is not necessarily a better friend, but a less complicated friend. I don’t think, nor does anybody in Saudi Arabia think, that China is a counterweight to the United States. But your country (U.S.) is courting China because you obviously think that it is important to court China. We’re simply following your lead”, (Royal Embassy of Saudi Arabia, May 10, 2006). While Turki went on to state that Saudi Arabia does not see China as a counter-weight to the U.S., his comment can be read as a realisation by many in Saudi Arabia of the negative aspects of too close an association with the U.S.

A Saudi analyst summarised the Kingdom’s position when he told the *Financial Times* that the politics was a factor for the Kingdom after the September 11, 2001 attacks on the U.S. strained relations with traditional allies in the West. “The

relationship with the US will always be strong. . It's a long relationship and we cannot ignore it whatever happens. But after the September 11 attacks, when we started looking around, nobody was there because we had never built relationships with Russia or China. And we thought: Let's build bridges with other countries", (England, 2009).

6.3 ECONOMIC DYNAMISM: LOOK EAST POLICY

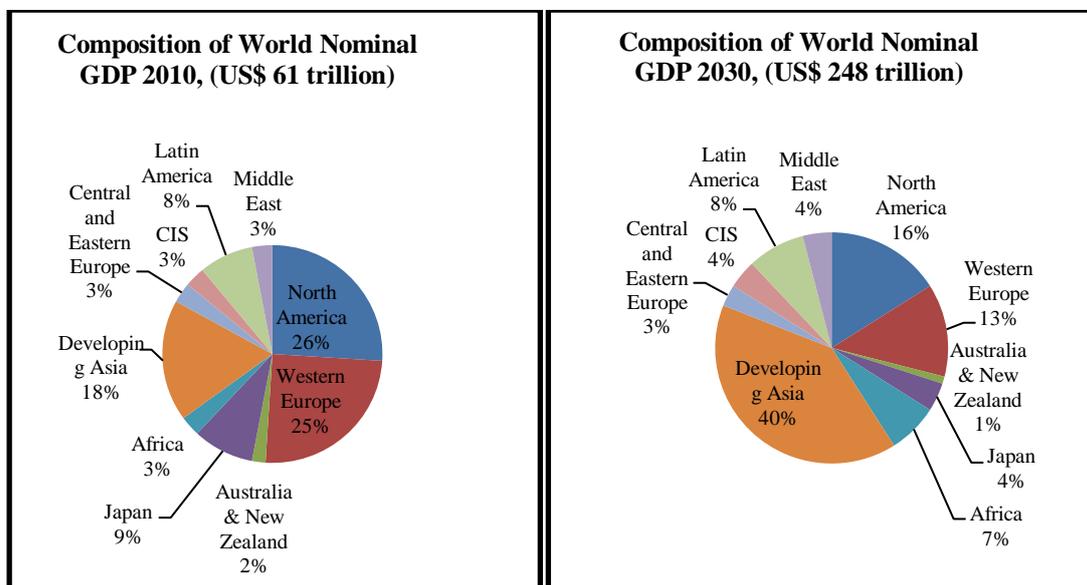
These political developments were coupled with change in the geopolitical landscape of the world's energy demand and supply. First, most consumers in the West are starting to view "green" sources of energy in a more favourable light than the fossil fuels that have hitherto largely powered the industrialised world, (Hoyos, 2010). Second, and perhaps more importantly, the oil industry – and specifically OPEC, is facing a significant shift in demand from West to East. Demand from the customers which OPEC has supplied for the past 50 years is stagnating, as market saturation and environmental policies move the U.S. and Europe away from oil. However, energy-hungry Asian nations, such as India and particularly China, are taking their place, refocusing the organisation's attention eastward, (Ibid).

Developing Asia¹³ will be the fastest growing region, driven by population and income per capita growth; it will grow by 7.0 percent annually between 2010 and

¹³ Developing Asia: Bangladesh, Bhutan, Cambodia, China, Fiji, Hong Kong, India, Indonesia, Kiribati, Lao People's, Democratic Republic, Malaysia, Maldives, Myanmar, Nepal, Pakistan, Papua

2030, (Ibid). While the region’s share is predicted to rise from 27 percent of world GDP to 44 percent in 2030 (Ibid) and per capita GDP growth rates will be highest in Developing Asia (6.1 percent p.a. between 2010 and 2030), (Ibid). Saudi official figures show that “between” 1989-2010 Saudi oil exports declined in all regions of the world except Asia, where oil’s demand has been growing rapidly over the last 20 years.

(Figure 6.3.1): Economic Weight is shifting to Asia



Note: GDP is measured in current USD converted at market exchange rates.

CIS = Commonwealth of Independent States

Source: adapted from Citi Investment Research and Analysis, (February, 2011)

Accordingly, energy demand is shifting from the developed world to the developing world, and Asia is expected to account for much of the growing demand during the next 20 years, (Dittrick, 2010). In its latest projections OPEC expects the world’s oil demand outlook in the Reference Case to hit 105.8 (mb/d) in 2030. Over the period

New Guinea, Philippines, Samoa, Singapore, Solomon Islands, South Korea, Sri Lanka, Taiwan, Thailand, Tonga, Vanuatu and Vietnam.

2010–2030, consumption in developing countries will increase by more than 21 mb/d. Of the total global oil demand growth in the long-term, 75 percent is in developing Asia (half of it or 8.2 mb/d in China only), (World Oil Outlook 2011: 63). In this regard the International Energy Agency (IEA) has said Chinese oil demand will rise by 3.5 percent every year until 2030, and that it will take over the United States to become the world’s largest oil and gas consumer by 2025, (Reuters, January 15, 2010). The IEA also noted that producers such as Saudi Arabia and Russia are shifting supplies from their traditional customers to China and other rapidly developing countries. The changing global market reflects a stark division between the stagnating developed world and the rebounding emerging economies. Jim Williams, Energy Economist with WTRG Economics Inc, told the *global and Mail*: “They’re going where the customers are...It’s not a strategy to exclude us. It’s a strategy to go where the market growth is”, (McCarthy, 2010) (see Table 6.3.2).

(Table 6.3.1): World Oil Demand Outlook in the Reference Case, (2010-2030)

Region (mb/d)	2010	2015	2020	2025	2030	2035
OECD	46.1	46.0	45.2	44.2	43.1	41.9
South Asia	4.0	4.8	5.8	6.8	8.0	9.2
Southeast Asia	6.2	6.8	7.6	8.4	9.1	9.9
China	8.9	11.6	13.8	15.6	17.1	18.4
Developing countries	35.9	41.8	47.2	52.2	57.0	61.9
World	86.8	92.9	97.8	102.0	105.8	109.7

Source: World Oil Outlook 2011

Within this context, Saudi Arabia increasingly recognised that Asia will provide the region’s largest and fastest-growing oil and gas export markets in the future. Already, two-thirds of the Saudi Arabia’s oil exports go east to Asia, reflecting this profound shift in the balance of global oil, (Andrews-Speed, 2009: 8). Between 1989 and 2010

Asia's share of Saudi's oil exports jumped from nearly 31 percent to almost 65 percent. But, in contrast, Saudi crude exports to the U.S. in 2009 have taken a deep plunge and now are at their lowest level in 20 years to nearly 386 million barrels (1.05 mb/d). Saudi oil exports to Western Europe are also plummeting to their lowest level since 1989 (see Table 6.3.2).

(Table 6.3.2): Saudi Crude Oil Exports by Region, 1989-2010 (%)^a

	North America	South America	Western Europe	The Middle East	Africa	Asia and the Far East ¹⁴	Oceania	Total
2010^b	18.2%	10.0%	9.9%	4.4%	2.2%	64.1%	0.7%	100%
2009	16.8%	1.01%	9.9%	4.5%	2.6%	64.8%	0.1%	100%
2008	22.1%	0.86%	11.6%	4.1%	2.8%	58.4%	0.07%	100%
2007	22.5%	0.88%	12.04%	4.4%	2.8%	57.1%	0.1%	100%
2006	20.8%	0.9%	14.6%	4.3%	3.1%	56.1%	0.1%	100%
2005	20.1%	0.9%	16.7%	4.2%	3.2%	54.5%	0.01%	100%
2004	22.4%	0.8%	18.4%	3.8%	3.5%	50.3%	0.4%	100%
2003	25.0%	1.0%	18.2%	3.0%	4.0%	48.2%	0.2%	100%
2002	25.3%	1.1%	17.7%	2.5%	3.5%	48.8%	0.7%	100%
2001	25.4%	1.6%	18.4%	2.6%	2.9%	48.4%	0.4%	100%
2000	25.2%	0.9%	21.1%	2.6%	3.4%	45.7%	0.6%	100%
1999	25.5%	1.2%	21.7%	3.3%	3.5%	44.1%	0.3%	100%
1998	23.3%	1.3%	27.6%	3.2%	2.1%	41.6%	0.5%	100%
1997	21.6%	1.4%	26.1%	3.4%	1.7%	44.7%	0.7%	100%
1996	21.9%	2.1%	23.7%	3.7%	1.5%	46.1%	0.7%	100%
1995	21.9%	2.3%	26.0%	3.5%	1.5%	43.8%	0.8%	100%
1994	22.9%	2.6%	26.4%	3.5%	1.5%	42.0%	0.7%	100%
1993	21.2%	2.6%	27.3%	3.2%	1.4%	42.9%	0.1%	100%
1992	25.5%	2.8%	26.4%	3.2%	1.4%	39.7%	0.7%	100%
1991	27.8%	3.0%	26.1%	3.3%	2.5%	36.1%	0.8%	100%
1990	29.2%	3.6%	23.1%	4.7%	1.9%	36.1%	0.7%	100%
1989	31.2%	2.9%	26.3	5.7%	0.3%	31.9%	1.4%	100%

Source: adapted from Saudi Arabian Monetary Agency Annual Report, (July, 2010)

(a) All percentages were calculated by author

(b) OPEC Annual Statistical Bulletin, (2011: 47)

¹⁴ Territories and regions conventionally included under the term Far East are: China, Hong Kong, Japan, Macau, Mongolia, North Korea, South Korea, Taiwan, Brunei, Cambodia, East Timor, Indonesia, Laos, Malaysia, Myanmar, Papua New Guinea, Philippines, Singapore, Thailand, Vietnam and Russian Far East

Saudi Arabia has cast its eye on Asia with greater fervour over the past decade, recognising that Japan's thirst for oil, combined with China's and India's economic growth and increasing influence in the global economy, meant that Asia will eventually replace the West as the largest consumer of Saudi oil, (Wagner & Karasik, 2010). As Table 6.3.2 shows, Saudi Arabia's exports to Asia doubled between 1990 and 2010, while the exports to U.S. and Western Europe declined dramatically. Indeed, Noé van Hulst, secretary-general of the International Energy Forum, told the *Financial Times* recently that the shift is of "overwhelming importance...The Middle East is looking east more and more, that is where the growth (in demand) is", (Hoyos, 2010).

From the Saudi perspective the argument is very simple: Just as China wants to secure energy supplies, Saudi Arabia wants to guarantee buyers and is eager to build its relationship with a fast-growing customer, (Oster, 2006). On the one hand, there is China, the world's fastest-growing major importer of oil, and, on the other hand, the Middle East, a region set to dominate world oil and gas supplies for the next two decades. It is therefore no surprise that diplomatic, economic, and energy relations between China and the countries of the Middle East have systematically deepened over the last ten years, (Andrews-Speed & others, 2009: 19). Saudi Arabia strategy to court China is two-pronged, one is diplomatic, in which they are increasing diplomatic activities to high-level state visits that indicate on the diplomatic level that the Gulf States are interested in tightening their relations. Secondly, there has been a marked increase in economic activities as well, (Basu, 2009).

Saudi Arabia regards China as a reliable customer for oil, a promising market and place to invest, an investor, a friend on the UN Security Council, and, not least, a leading political power that could serve as a counterweight to the dominant influence wielded by the U.S. in the region, (Jochen, 2006) (see Table 6.3.4). John Sfakianakis, Chief Economist at Banque Saudi Fransi in Riyadh, argues that: “China offers demand security, something that for a long time the oil-producing countries including Saudi Arabia have called for...As global demand has been picking up in the east. . Saudi Arabia has been looking east... The U.S. wants to reduce her dependence on foreign oil and encourage renewable fuels. Meanwhile, Saudi Arabia wants stable markets for its oil reserves”, (Meyer, 2010) (see Table 6.3.4).

(Table 6.3.3): China’s Economic Power

The World’s Second Largest Economy	China surpassed Japan as the world’s second-largest economy after the U.S. in the second quarter of 2010
The World’s Biggest Energy Consumer	According IEA China overtook U.S. as world’s biggest energy consumer in 2009
The World’s Top Exporter	In 2009 China passed Germany as World’s Top Exporter
The World’s Largest Car Manufacturing Country	China has overtaken the United States and Japan to become the world’s largest car manufacturing country in 2009
The World’s Leading Financial Power	<ul style="list-style-type: none"> - China is by far the largest holder foreign reserves, with stockpiles of US\$3.2 trillion at the end of June 2011. - The Top Foreign Holder US’s Treasury Securities: According to the US Treasury, China is Top Foreign Holder US’s Treasury Securities, holding of U.S. government debt of US\$ 1165.5 billion (26.1% of total) at the end of June 2011. - Member of the top 20 economy in the world (G20) - A voting power in the IMF
The world’s factory	China today produces three-quarters of the world’s toys; two-thirds of the world’s digital electronics; around half of all computers; and more than a quarter of the world’s clothes

Source: U.S. Department of the Treasury, IEA, Bloomberg, Reuters, Financial Times and McKinsey

The development of Gulf-Asia relations has been propelled by other factors beside the energy market. Gulf countries are seeking to rebalance their relations with the major powers. More specifically, they are seeking to reduce their level of dependence on the United States, as well as their susceptibility to U.S. pressure, (Calabrese, 2009). For Saudi Arabia, China has, especially since 9/11, become a profitable and relatively secure haven for huge gains from the Saudi oil business. Furthermore, Saudi Arabia has managed to successfully diversify its export strategy in its trade with China, above all by supplying the gigantic Chinese textile industry with Saudi petrochemical products – at the expense of China’s traditional Asian suppliers, (Jochen, 2006).

Saudi Minister of Petroleum and Mineral Resources Ali AL-Naimi seemed to prognosticate the implications of these developments for Sino-Saudi relations as early as 2001 and was one of the first to introduce the now-common language of interdependence to describe Sino-Saudi relations. Speaking before the World Petroleum Congress in Shanghai September 19, 2001, AL-Naimi noted that: “China is the second biggest economy in Asia and the seventh in the world; it is the second largest oil consumer in Asia after Japan and the third worldwide. Saudi Arabia, on the other hand is the largest economy in the Arab World, and also the largest world oil producer...This interdependent relationship in the energy field between our two countries makes for a model strategic partnership for the world”, (AI-Naimi, 2001) (see Tables 6.3.5).

(Table 6.3.4): Saudi Arabia Exports Main Regions 2002-2010 (US\$ billions)

		2002	2003	2004	2005	2006	2007	2008	2009	2010
Saudi Arabia Total exports		72,4	93,2	125,9	180,7	211,3	234,9	313,4	192,3	213,4
To Asia	Total	36,01	54,5	77,4	112,5	136,5	150,4	161,2	123,7	143,2
	Mineral fuels, oils, distillation products, etc	33,6	46,9	66,1	99,3	120,7	130,4	153,6	106,7	125,6
To China	Total	3.4	5.1	7.5	12.2	15.0	17.5	31.0	23.6	32,8
	Mineral fuels, oils, distillation products, etc	2.4	3.7	5.4	9.2	11.8	13.6	26.4	19.3	25,8
To Europe	Total	12,0	13,2	19,6	26,2	28,1	24,5	31,8	15,6	21,3
	Mineral fuels, oils, distillation products, etc	10,2	11,1	16,7	22,7	23,7	19,8	27,0	12,4	16,4
To North America (US, Canada and Mexico)	Total	13,8	19,5	22,5	28,9	33,0	37,1	57,0	23,2	35,0
	Mineral fuels, oils, distillation products, etc	13,2	18,7	21,8	28,1	32,4	36,4	56,2	22,6	33,9

Source: Calculated by the author from UNCOMTRADE (July, 2011)

Saudi Arabia sees the its strategic and energy future as revolving around becoming a global economic and energy power, “an indispensable economic power”, based on being a dominant global supplier not only of oil but also of other energy-based commodities, (Andrews-Speed & others 2009:8). The country is seeking to be the largest, at least in chemicals and fertilisers, as well as a dominant player in aluminium, cement and steel, (Seznec, 2009: 41-51). According to Jean-Francois Seznec, a professor for contemporary Arab studies at Georgetown University in Washington DC, China also buys a significant amount of petrochemicals from Saudi Arabia as it strives to maintain the quality of packaging for the vast range of goods the country sells, (Guiffrida, 2011). Additionally, China is becoming a major investor in Saudi Arabia, less so in the energy sector but more in petrochemicals, mining, and railroads. Finally, expanding Saudi-Chinese relations would allow the Saudis to

become less dependent on the United States for their economic and even strategic future, (Ibid).

In this context, Prince Walid bin Talal, Saudi billionaire investor and member of the Royal Family, told the *New York Times*: “We are opening new channels, we are heading East...China is a big consumer of oil. Saudi Arabia needs to open new channels beyond the West. So this is good for both of us...When you have a country of 1.3 billion people growing at 10 percent annually, importing millions of tons of oil, Saudi Arabia has to be there...It’s clear Saudi Arabia is going where its interests are, and China is going where its interests are”, (Fattah, 2006). That argument was echoed by the then Saudi Minister of Commerce and Industry, Fawaz AL-Alami, who pointed out that: “The growth in our oil exports and petrochemicals will be China and India...Once dependent in its foreign policy almost exclusively on the U.S., Riyadh has been diversifying its friendships in recent years, with Asia, where demand for Saudi oil is at its highest, emerging as an important strategic partner”, (Khalaf, 2006).

Meanwhile Ben Simpfendorfer, the Editor of *China Insider* and the former Chief China Economist at the Royal Bank of Scotland, argues that the partnership between Saudi Arabia and China is part of a broader strategy by the Saudis to supply Asian markets and extend their global influence. It also helps Saudi Arabia reduce reliance on the United States, which since World War II has protected Saudi security in return for stable oil supplies, (Meyer, 2010). Furthermore, Li Wei, a Chinese diplomat in Riyadh, shares that view: “China’s rise has provided Saudi Arabia with an excuse to knock on Washington’s door and to say - You are not our only partner”, (Ibid).

Indeed, for the Saudis, partnership with China has advantages and does make economic sense. Although oil is bought and sold on the market, it comes in its crude form in many varieties, and countries often lack the refineries to process some forms. Saudi investment in Chinese refineries will help to make the country captive consumers for Saudi crude, (Giridharadas, 2006). China's market will almost certainly be the largest incremental oil market in the world for the next twenty years. As such it will be the target of marketing campaigns by all of the world's suppliers capable of increasing output at a rapid rate, (Obaid, 2002). From the Saudi perspective, to penetrate China's markets it will need to insure that its crude oil can be refined into useful products. Saudi ARAMCO invested in China's refining industry and upgraded some of its capacity to handle Saudi crude oil. Not only will this give China priority access to Saudi crude, it will also give Saudi Arabia a direct entry into the downstream sectors in China, one of the fastest growing markets in the world, (Lee & Dan, 2007).

In addition, Saudi Arabia needs to find growing markets for petrochemicals over the next decades, (Sfakianakis, 2009). The Kingdom also needs to build its market knowledge in Asia. China offers important economic advantages to Saudi Arabia's downstream expansion into the wider region. And closer to home, China's affordable contractors and low-cost labour force do offer Saudi Arabia an extra cushion for the country's development projects, (Ibid). Speaking on the subject of "Saudi Arabia and China: Natural Partners in the Global Economy", at the *Financial Times* China-Middle East Summit, held in Riyadh May, 2008, Saudi Basic Industries Corporation (SABIC) Vice Chairman and CEO Mohamed Al-Mady argued that Saudi Arabia's large hydrocarbon resources made the Kingdom a "natural strategic trading partner"

for China's dynamic industrial and economic growth, (*Arab News*, May 7, 2008). Also, Al-Mady said that China's rapidly growing population provides important markets for Saudi Arabia's growing petrochemical industry. He went on to add: "Saudi Arabia and China are indeed natural trading partners supported by cooperative political ties. The geographic location of the partners permits an economic pathway for two-way trade", (Ibid). Furthermore, Isam Fakhru, Chairman of the Bahrain Chamber of Commerce and Industry and head of the Federation of the Dammam-based GCC Chambers, argues that the two sides "strategically need each other...Each party realise this fact", (Kawach, 2010).

6.4 POLITICAL FACTORS: NEW PATTERN OF PRIORITIES

The current Saudi foreign policy calculations are driven by a deep fear and suspicion of expanding Iranian influence. Saudi leadership has begun to look at all regional security issues through the prism of their fears about growing Iranian influence. They see Iran's activities as dangerously provocative, not only in Iraq, but also in Lebanon, Palestine, Bahrain, Yemen, parts of Africa, and Southeast Asia. Indeed, the Iranian "threat" moved again to Riyadh's top list of priorities. In a secret letter, leaked by *Wikileaks*, summarising the trip of White House counterterrorism adviser John Brennan to Saudi Arabia in March 2009 concerning his meeting with the Saudi King, U.S. Political Counsellor at the U.S. Embassy in Saudi Arabia, Lisa Carle, wrote that, in summarising his history with Iran, Saudi Arabia King Abdullah concluded: "We have had correct relations over the years, but the bottom line is that they cannot be

trusted”, (Wikileaks, March 22, 2009). Prince Turki Al-Faisal argues that: “Iran is very vulnerable in the oil sector, and it is there that more could be done to squeeze the current government to join the world efforts toward peace”, (Al-Faisal, June 8, 2011). According to Stuart Levey, a senior fellow at the Council on Foreign Relations who served as Under Secretary of the Treasury for Terrorism and Financial Intelligence, “Iran’s ability to develop its most critical industry and create jobs for its young people is at great risk”, (Reed, Stanley & others, 2011). In this regard, The International Energy Agency forecasts a 20 percent decline in Iran’s production capacity, now about 3.6 million barrels per day, in the five years through 2016. Sanctions are blocking foreign investment and delaying projects, (IEA, Medium-Term Oil & Gas Markets 2011).

As discussed earlier in the previous chapters, the first major breakthrough in Chinese-Saudi relations did not occur in the energy field, but came with a controversial missiles deal in the late 1980s, (Nonneman, 2005: 344). At that time Saudi Arabia had reasons to reach out to China to not only curtail arms sales to Iran but to lure China away from Iran with higher bids and diplomatic pressure, (Obaid, 2002). As a former assistant director in the Saudi General Intelligence Directorate put it:

“Clearly, we [Saudis] are going to have to give the Chinese numerous incentives for them to stop supplying the Iranians with those long-range missiles. One way is clearly going to have to be a redirection of Saudi purchases to also include Chinese military equipment. The usual suppliers [U.S., England, and France] won’t lose importance, of course”, (Ibid).

These reasons are still valid today, in the Saudi political calculations; Riyadh is betting that strong Sino-Saudi relations could prevent Beijing in following a policy which might represent a threat to the Saudi national security. In this regard it’s very interesting to mention that in a confidential memo leaked by “*Wikileaks*” commenting

on the trip of the Chinese Foreign Minister to Saudi Arabia in January 2010, U.S.

Ambassador James B. Smith to Saudi Arabia wrote that:

“...Since King Abdullah’s historic visit to Beijing in January 2006, the Saudi-Chinese relationship has focused predominantly on energy and trade. However, the relationship may be showing signs of political evolution. While the Chinese would likely prefer to stay away from political controversy, their economic power and permanent seat on the UN Security Council has made it more and more difficult for them to avoid politics altogether. The incentives for the Saudis to try and leverage their economic relationship with China for political gain with respect to sensitive regional issues, such as Iran and the Israeli-Palestinian conflict, are significant and growing. After patiently focusing on building the economic relationship since 2006, FM Saud’s public and private prodding of FM Yang indicates the Saudis are ready to try and cash in some political chips”, (Wikileaks, January 27, 2010)

There are several other factors that are pushing Saudi Arabia to develop closer relations with China. Firstly, most Muslims do not have a negative political perception of China, (Rubin, 1999). Due to the fact that China is not associated with hegemony, imperialism and domination as the United States and European nations are, (Alistair, 2006). There is also little concern that China’s increasing status as a world power will constitute an international threat, (Jiang, 2007: 12-15). While there is not negative perception of China, the same cannot be said of America. Anti-American sentiment still exists strongly in Saudi Arabia, two years after U.S. President Barack Obama called in a groundbreaking speech from Cairo for a “new beginning” in relations with the Muslim world. The United States’ popularity in the Arab World has plummeted to levels lower than the last year of the George W. Bush Administration (2008), (Zogby, 2011). According to James Zogby’s survey (2011) of public opinion in six Arab countries, an overwhelming majority of more than 4,000 people surveyed in Egypt, Jordan, Lebanon, Morocco, Saudi Arabia and the United Arab Emirates, told the Arab American Institute that they felt that Obama had not met the expectations he laid out in the June 2009 Cairo speech, (Ibid). Secondly, most Saudis have a certain degree of admiration for China. They are impressed with China’s explosive economic growth believing that it has occurred without China

sacrificing social justice, law and order, or traditional values, (Jiang, 2007: 12-15). Finally, relations with China keep the Saudi Arabia's future options open and give them a political flexibility as the Arab World (including Saudi Arabia) expects China to play a bigger role in the Middle East as well as in international affairs, (Jin, 2004).

The "China model" has captivated Arab governments in two ways. First, it promises rapid growth without regime change. There is a tendency for the West to link economic reform as a "Trojan Horse" for political reform. Second, the China model also promises independence from the West, (Simpfendorfer, 2009: 162). From a Saudi perspective, on one hand the Saudi public sees China as a counter balance to the United States; on the other hand China's conservative approach to political and economic development and modernisation appears to be a model worth adopting and a viable alternative to U.S. - and western-inspired reform models, (Zambelis & Gentry, 2008). Prince Turki AL-Faisal stated, "With China, there is less baggage; there are easier routes to mutual benefit", (Meyer, 2010). According to Freeman (a former U.S. ambassador to the Kingdom), the simple bargain of oil for security has become more complex because after 9/11 there are "all sorts of other agendas that the Saudis either find irksome or difficult to address", (Freeman, 2006). In this regard, Freeman astutely observed:

The Arabs see a partner who will buy their oil without demanding that they accept a foreign ideology, abandon their way of life, or make other choices they'd rather avoid. They see a country that is far away and has no imperial agenda in their region, but which is internationally influential and likely in time to be militarily powerful... They see a country that unreservedly welcomes their investments and is grateful for the jobs these create. They see a major civilization that seems determined to build a partnership with them, does not insult their religion or their way of life, values its reputation as a reliable supplier too much to engage in the promiscuous application of sanctions or other coercive measures, and has no habit of bombing or invading other countries to whose policies it objects, (Ibid).

Additionally, through Saudi's lens, China could be regarded as a valuable source of support as Riyadh continues on a path of cautious and selective economic

liberalisation while seeking to deflect U.S. pressure in the area of political reform, (Douglas & others, 2006). In this context, Clovis Maksoud, a former Arab League ambassador to the United Nations, United States and India, said, “America will be more deferential to the Saudi and Arab priorities in the future, because they will realise the traditional bilateral relations between Saudi Arabia and the United States, though sustainable, is no longer exclusive”, (Giridharadas, 2006).

6.5 CONCLUSION

The chapter has shown that Saudi Arabia’s objectives of the Sino-Saudi relationship are closely aligned with the economic interdependence school of thought for numerous reasons: (a) Saudi Arabia’s energy strategy is not a strategy to exclude the United States. It’s a strategy to go where the market growth is; (b) Saudi Arabia sees a need to diversify its political relations as a result of the rise in criticism of U.S.-Saudi relations; (c) Saudi Arabia is hoping that closer Sino-Saudi relations will affect the Sino-Iranian relationship. As stated earlier, the Saudis would like to see decreased Sino- Iranian military relations and get China onboard to support tougher action in the event of Iran continuing to pursue its nuclear program. For Saudi Arabia, maintaining good relations with the United States remains its key foreign policy objective, given the long-standing economic and military ties between the two countries. Though China and Saudi Arabia have expanded their cooperation, Saudi Arabia will probably attempt to strike a balance between the United States and China and avoid compromising U.S. interests to please the Chinese or the vice versa in the near future.

CHAPTER SEVEN

THE SCOPE OF CHINA-SAUDI ECONOMIC RELATIONS

7.1 INTRODUCTION

Since the establishment of diplomatic relations between China and Saudi Arabia in 1990, bilateral ties have witnessed smooth and rapid development. China attaches great importance to its ties with Saudi Arabia and will further strengthen the friendly cooperation, ((Xinhua, January 14, 2010). The market share of Chinese products in the Saudi market is going up every year, (Yu, 2010). Today Saudi Arabia remains China's top partner in the Middle East and North Africa (MENA), for nine consecutive years, (Yang, 2010).

This chapter will examine the economic relationship that China and Saudi Arabia have formed over the past two decades. The following will be examined in the economic realm: (a) Trade relations; (b) Cross-investments between the two countries; and (c) The factors which could slow China-Saudi economic ties. The chapter attempts to decipher Chinese intentions with Saudi Arabia. If China is acting within the realist theory, it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence. This would include proactive actions such as: (a) Providing Saudi Arabia with massive economic assistance and incentives to develop closer Sino-Saudi economic and political ties with the intent to degrade the U.S.-Saudi relationship; and (b) Allocating

huge investments in Saudi Arabia's economy to make it dependent on Chinese capital significantly. On the other hand if China is acting within the economic interdependence school of thought, it should be: (a) Interacting economically with Saudi Arabia in a manner which makes commercial sense; and (b) Developing a Sino-Saudi political relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship. In this regard we will show the conditions under which high energy interdependence between China and the Middle East will lead to a pacific or belligerent China. If decision-makers' expectations of future trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future trading environment they are likely to take action to protect their interests in the region.

7.2 TRADE TIES: GROWING INTERACTIONS

The trade between Saudi Arabia and China commenced before they established their official diplomatic relations in 1990. Concerted efforts on the part of China to improve its relations with Saudi Arabia began in 1978, particularly when China embarked on the economic openness. In 1981 Saudi Arabia lifted a long-standing politically and religiously motivated ban on direct imports from China, (Shichor, 1998). A small volume of Chinese goods had entered Saudi markets indirectly, but from the early eighties Chinese exports increased steadily and Saudi Arabia became one of China's most important Middle Eastern trading partners, (Ibid). Since 1990 the two-way traffic between the capitals has led to a series of trade deals. Between 1990

and 2000, the bilateral trade between the two countries grew ten-fold to reach US\$3.098 billion, (*People's Daily*, April 1, 2002). By mid 2000s the trade was booming; bilateral trade between the two countries in 2005 increased further in excess of US\$14 billion, (AP, January 23, 2006), to jump in 2008 to a new record as the bilateral trade volume reached 41.8 billion U.S. dollars. In 2009, although being affected by the global financial crisis, the bilateral trade volume also reached 32.6 billion U.S. dollars, (see Table 7.2.3). But 2010 saw a significant increase in trade between the two countries. According to the statistic report of Chinese Customs, the bilateral trade volume between China and the Kingdom of Saudi Arabia reached a record high of US\$43.18 billion in 2010; increased 32.7 percent compared to the previous year, and exceeded the historic record US\$41.8 billion in 2008, (China's Ministry of Commerce, February 9, 2011). On other hand trade data provided by the U.S. Census Bureau shows that the value of imports and exports between the U.S. and Saudi Arabia reached US\$43.011 billion in 2010, a 30.9 percent increase from 2009. U.S. exported US\$11.59 billion worth of goods and services to the Kingdom, while the U.S. imported US\$31.42 billion worth of Saudi products and services, (U.S. Census Bureau, February, 2011).

These figures show that China took over the U.S. as trade partner (excluding military and security contracts) for the first time since 1990. Meanwhile, Chinese products are gaining a stronger foothold across the Gulf. Analysts point to the success of DragonMart, a shopping centre in Dubai, in which 4,000 Chinese businesses are housed, as an indicator that low-tech Chinese products may soon dominate in other markets in the region, despite the Arab population's penchant for high-end Western products, (Guiffrida, 2011). In this regard, John Sfakianakis, Chief Economist at the

Banque Saudi Fransi in Riyadh, noted that: “Over the past few years, the U.S.’ total market share of Saudi Arabia trade has declined, while it has been increasing for the Chinese”, (Ibid) (see Table 7.2.1 & 7.2.2).

(Table 7.2.1): China’s Exports (Selected Indicators US\$ Billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
China’s Exports to World	266,09	325,5	438,2	593,3	761,9	968,9	1220	1430	1201	1578
China’s Exports from Middle East	8,6	11,4	16,2	21,1	28,3	39,8	59,3	75,3	64,5	80,6
China’s Exports to GCC	4,07	5,5	8,085	10,435	13,76	18,38	27,84	38,74	31,27	36,05
China’s Exports to Saudi Arabia	1,3	1,6	2,1	2,7	3,8	5,05	7,8	10,8	8,9	10,3

Source: General Customs Administration of China and UNCOMTRADE

(Table 7.2.2): China’s Imports (Selected Indicators US\$ Billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
China’s Imports From World	243,5	295,1	412,7	561,2	659,9	791,4	956,11	1132	1003	1394
China’s Imports from Middle East	9,4	9,8	15,1	22,4	31,8	41,8	49,3	82,2	58,6	90,6
China’s Imports from GCC	5,6	6,01	8,7	14,2	19,9	26,5	30,2	53,7	36,6	56,3
China’s Imports from Saudi Arabia	2,7	3,4	5,1	7,5	12,2	15,08	17,5	31,02	23,5	32,8

Source: General Customs Administration of China UNCOMTRADE

Indeed, trade is at the heart of the growing links between the two countries, which centre on the crude oil and petrochemicals industries. Chinese Vice President Xi Jinping in an address to a meeting of Saudi and Chinese businessmen held at the Jeddah Chamber of Commerce and Industry (JCCI) in June 2008, said: “The situation is favourable for further growth of economic cooperation in diverse fields between the Kingdom and China... KSA is our largest economic partner in the Middle East as the volume of trade is on the path of continuous growth”, (Fakkar, 2008). Indeed, the

growth of China-Saudi trade jumped in the last three decades in dramatic way, between 1978 and 2010 the volume of trade increased over 1115 times, (see Table 7.2.3 below).

(Table 7.2.3): Trade between China and Saudi Arabia, 1978-2010 (US\$)

	China's Trade with Saudi Arabia	China's Trade with the World	China - Saudi Trade of China's Total (%) ^a	Saudi Arabia's Trade with the World	China - Saudi Trade of Saudi's Total (%) ^b
2010	43,230,400,000	2,974,320,000,000	1.45%	334,747,000,000	13.01%
2009	32,566,250,000	2,207,330,000,000	1.47%	265,421,900,000	12.26%
2008	41,853,200,000	2,561,260,000,000	1.63%	418,102,000,000	10.01%
2007	25,360,140,000	2,174,964,000,000	1.16%	299,393,400,000	8.47%
2006	20,140,930,000	1,761,493,000,000	1.14%	266,236,900,000	7.56%
2005	16,111,240,000	1,422,872,000,000	1.13%	214,328,900,000	7.51%
2004	10,299,660,000	1,154,918,000,000	0.8%	155,726,900,000	6.61%
2003	7,341,840,000	851,323,000,000	0.8%	122,388,000,000	5.99%
2002	5,109,230,000	621,223,000,000	0.8%	97,714,900,000	5.22%
2001	4,079,570,000	510,290,000,000	0.7%	99,866,600,000	4.08%
2000	3,098,230,000	474,398,000,000	0.6%	105,447,000,000	2.93%
1999	1,855,329,000	360,659,000,000	0.5%	76,923,400,000	2.41%
1998	1,703,953,000	324,136,000,000	0.5%	68,749,300,000	2.47%
1997	1,679,958,000	325,089,000,000	0.5%	89,195,900,000	1.88%
1996	1,588,204,000	290,120,000,000	0.5%	88,555,200,000	1.79%
1995	1,287,411,000	281,129,000,000	0.4%	77,491,500,000	1.66%
1994	1,027,133,000	236,581,000,000	0.4%	65,957,800,000	1.55%
1993	697,392,000	195,333,000,000	0.3%	70,597,700,000	0.9%
1992	571,704,000	167,494,200,000	0.3%	83,560,500,000	0.6%
1991	525,668,000	135,846,700,000	0.3%	76,890,600,000	0.6%
1990	417,096,600	116,570,400,000	0.3%	68,498,800,000	0.6%
1989	319,263,000	112,057,700,000	0.2%	49,538,200,000	0.6%
1988	425,200,000	103,017,100,000	0.4%	45,522,100,000	0.9%
1987	354,400,000	82,689,600,000	0.4%	42,624,700,000	0.8%
1986	185,900,000	74,675,900,000	0.2%	39,296,600,000	0.4%
1985	155,200,000	69,813,200,000	0.2%	51,101,700,000	0.3%
1984	160,900,000	50,779,100,000	0.3%	71,216,900,000	0.2%
1983	167,700,000	43,409,000,000	0.3%	85,042,800,000	0.1%
1982	192,700,000	40,786,500,000	0.4%	116,492,200,000	0.1%
1981	232,100,000	43,107,000,000	0.5%	148,472,000,000	0.1%
1980	151,600,000	37,644,200,000	0.4%	132,179,000,000	0.1%
1979	76,400,000	29,332,000,000	0.2%	82,909,400,000	0.09%
1978	37,000,000	20,660,000,000	0.1%	58,165,000,000	0.06%

Source: IMF (DoTS), (September 2011)

(a) & (b) Percentages were calculated by the author

The above tables demonstrate that the relations between the two countries have developed rapidly in the last two decades. Working through both high-level and low-level contacts, China and Saudi Arabia were able to coordinate their efforts in pursuing several mutual interests, most notably economic and development endeavours. An investment agreement was signed in 1992, followed by a series of further pacts to strengthen economic ties, (Mirza, 2009) and an economic agreement also signed in 1992 encouraged cooperation, most notably on establishing a refinery capable of processing Saudi crude oil in China. Saudi Oil Minister Ibrahim al-Naimi furthered such discussions in 1995, claiming that such ventures would “give China a permanent and steady source of oil, as Saudi Arabia is considered a safe and reliable source for petroleum supplies”, (Anderson, 2004). Specifics on financing were worked out through a series of meetings in 1996, yielding two joint refinery projects in Shandong and Guangdong provinces. King Abdullah, the then Crown Prince, visited China for the first time in 1998, becoming the highest-level Saudi official ever to visit China, (Ibid). In 1999, Prince Salman, Governor of Riyadh province, pursued a similar strategy in an attempt to promote Sino-Saudi cooperation on infrastructure development; his efforts yielded an agreement with the Mayor of Beijing to collaborate in the fields of “urban infrastructure, real estate, transportation, and entertainment facilities”, (Ibid).

Recognising Saudi Arabia’s pre-eminent place among the Middle East oil producers, China has cultivated what former President Jiang Zemin described as a “strategic oil partnership” with Saudi Arabia. In November 1999, accompanied by a delegation of Chinese businessmen, Jiang paid what was the first ever visit to Saudi Arabia by a head of state of China. During the trip, agreements were signed whereby the Saudis

opened their oil and markets (except for “upstream” exploration and production) to Chinese investment and in return the Saudi national oil company, Saudi Aramco, was allowed to participate in China’s “downstream” refining sector, (Pham 2009: 177-193). As shown in Table 7.2.1, the trade also accelerated after the 9/11 terrorists attacks. By 2002 Saudi Arabia had become China’s leading foreign supplier of petroleum, and the Chinese were gaining from the Saudis, (Ibid).

The year of 2006 was a turning point. Tang Zhichao, director of Middle East Studies under the China Institute of Contemporary International Relations, argues that: “Since then, Saudi Arabia has valued its relations with China much more highly”, (Ding, 2009). Indeed, Saudi-China relations reached their zenith in January 2006 when King Abdullah bin Abdulaziz al-Saud had visited China in what was the first visit by a Saudi monarch to the People’s Republic since diplomatic relations were established in 1990. The king’s visit also was the first since Saudi Arabia became a full (WTO) member in December 2005 potentially signalling a new strategic partnership, (Mirza, 2009).

The visit saw the signing of five agreements, including a landmark pact for expanding cooperation in oil, natural gas and minerals. Saudi Foreign Minister Saud al-Faisal told reporters during the visit that the four other agreements focused on nurturing economic, trade and technical cooperation; avoiding dual taxation and preventing tax evasion; cooperating on vocational training; and extending a Saudi Arabian Development Bank loan to the predominantly Muslim city of Aksu in western China, (Oster, 2006). In addition, Saudi Arabia has also officially joined the World Trade Organisation (WTO), offered Chinese companies investment opportunities in the

country's enormous infrastructure sector that includes petrochemicals, gas, desalination, power generation and railways, (Madsen, 2006).

Three months later in April 2006, Chinese president Jintao Hu reciprocated the visit. The two heads of state signed five additional accords that expanded Sino–Saudi economic cooperation, including agreements on cooperation in oil, gas, and mining; health care; and on quality inspection and standards of goods and services, (Ibid). The highlight of the visit was the signing of a major public works agreement for the first time between the two countries, specifically a US\$1.8 billion deal for the China Railway Construction Corporation to build a high-speed monorail linking Islam's two holiest cities, Makkah and Medina, (Ibid). Furthermore, economic relations between Saudi Arabia and China in February 2009 received a shot in the arm with the signing of five landmark agreements, during the second visit of Chinese president Hu, (Shaheen, 2009) aimed at taking ties to a new height. The agreements included one for the ambitious Makkah mono-rail project; cooperation in oil, gas and mining; in the field of health; on quality inspection and standards of goods and services; and a Memorandum of Understanding to set up King's Abdul Aziz Public Library in Beijing, (Ibid).

Within this context, relations between Saudi Arabia and China are mutually strategic in nature. China is the second largest economy in the world. Saudi Arabia is the largest economy in the Middle East and North Africa region and plays a unique systemic role in the global oil market, (Sfakianakis, 2011). China is an exporter of goods and Saudi Arabia is a significant importer, while China's growth and acute demand for oil imports has been largely supplied by Saudi Arabia. China is the

second largest source of imports to the Kingdom and is ranked fifth as a destination for Saudi exports. Saudi Arabia is most interested in China's bustling labour market and the products the country can manufacture cheaply, such as textiles. Just as Saudi Arabia has large oil surpluses, China has large labour surpluses; this dynamic has driven the rapid expansion of China-Saudi trade. Amr Dabbagh, Governor and Chairman of the Board of Directors of the Saudi Arabian General Investment Authority (SAGIA), argues that: "The theory of comparative advantage would lead to a situation where energy-intensive goods from Saudi Arabia are traded for labour-intensive goods from China", (Teslik, 2008).

Indeed, since the establishment of diplomatic relations in 1990, Sino-Saudi ties have become one of the most dynamic bilateral relationships in the region, (Zambelis, 2010: 4-7). The Sino-Saudi economic relationship has grown at an impressive rate. According to the Council of Saudi Chambers of Commerce and Industry (SCCI), trade between China and Saudi Arabia grew at an annual rate of 30 percent and 50 percent in 2003 and 2008, respectively. Bilateral trade rose 64.7 percent in 2008 and over 40 percent in 2010 and is estimated to rise 50 percent by 2015 (see Table 7.2.4).

(Table 7.2.4): China's Trade 2001-2010, (Selected indicators – US\$ in billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World's Total Trade (US\$ trillions)^a	12,34	12,93	15,09	18,54	21,01	24,32	27,89	32,17	24,53	30,63 ^c
China Total Trade										
World (US\$ trillions)	0,509	0,620	0,850	1,15	1,421	1,76	2,176	2,56	2,20	2,97
(%) of World's Total^b	4.05%	4.85%	5.6%	6.2%	6.75%	7.21%	7.8%	7.95%	8.95%	9.7%
Arab Countries (US\$ billions)	14,69	17,74	25,40	36,69	51,26	66,16	84,25	129,64	103,91	145.40
(%) of China's total	2.88%	2.86%	2.98%	3.15%	3.6%	3.75%	3.9%	5.15%	4.75%	4.89%
Saudi Arabia (US\$ billions)	4,07	5,10	7,31	10,29	16,07	20,14	25,40	41,84	32,59	43.19
(%) of China's total	0.7%	0.8%	0.8%	0.8%	1.13%	1.14%	1.16%	1.63%	1.14%	1.45%

Source: General Customs Administration of China and UNCOMTRADE

(a) Total Trade = Exports + Imports, calculated by the author. (b) The percentage were calculated by the author; (c) WTO

Furthermore, Saudi Arabia accounts for about a third of the total volume of Sino-Arab trade, as the total volume of Sino-Arabic trade grew to 132.8 billion U.S. dollars in 2008 from 5.8 billion U.S. dollars in 1996, but fell slightly in 2009 due to the economic crisis, to about US\$107, (US\$32.6 billion with Saudi Arabia alone), (Xinhua, September 26, 2010). According to figures cited by the Saudi Finance Minister Ibrahim Al-Assaf, trade relations between Saudi Arabia and China grew more than 25-fold during the past decade, the volume of trade between the two countries in 2008 reached more than US\$40 billion, a goal set by leaders of both

countries in 2006 and to be achieved by 2010, (Hamidi, 2010) (see Table 7.2.5& 7.2.6).

(Table 7.2.5): China's Exports 2001-2010 (Selected indicator)^a

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World Total Exports (US\$ trillions)	6,06	6,38	7,45	9,12	10,38	12,07	13,82	15,94	12,14	15.23 ^b
China total Exports										
World (US\$ trillions)	0,266	0,325	0,438	0,593	0,761	0,968	1,22	1,43	1,20	1.57
(%) of World's Total	4.3	5.2	5.8	6.5	7.3	8.02	8.8	8.9	9.8	10.4
Arab Countries (US\$ billions)	7,21	9,6	13,05	17,62	23,63	31,79	43,22	59,38	51,81	64.90
(%) of China's total	2.7	2.9	2.9	2.9	3.1	3.2	3.5	4.1	4.3	4.1
Saudi Arabia (US\$ billions)	1,35	1,6	2,14	2,77	3,82	5,05	7,83	10,8	8,97	10.36
(%) of China's total	0.5	0.5	0.4	0.4	0.5	0.5	0.6	0.7	0.7	0.6

Source: General Customs Administration of China and UNCOMTRADE

(a) Percentages were calculated by the author. (b)WTO

(Table 7.2.6): China's Imports 2001-2010 (Selected indicator)^a

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World's Total Imports (US\$ trillions)	6,27	6,55	7,63	9,42	10,63	12,25	14,06	16,23	12,38	15.40 ^b
China total Imports										
World (US\$ trillions)	0,243	0,295	0,412	0,561	0,659	0,791	0,956	1,13	1,003	1.39
(%) of World Total	3.8	4.5	5.4	5.9	6.2	6.4	6.8	7	8.1	9.0
Arab World (US\$ billions)	7,48	8,11	12,35	19,07	27,63	34,36	41,02	70,26	52,10	80.49
(%) of China Total	3.07	2.7	2.9	3.4	4.1	4.3	4.3	6.2	5.2	5.7
Saudi Arabia (US\$ billions)	2,71	3,43	5,17	7,52	12,24	15,08	17,56	31,02	23,62	32.82
(%) of China Total	1.1	1.1	1.2	1.3	1.8	1.9	1.8	2.7	2.3	2.3

Source: General Customs Administration of China and UNCOMTRADE

(a) Percentages were calculated by the author. (b) WTO

Al-Assaf also said that the Chinese companies are involved in 100 important projects in infrastructure in the Kingdom, with a total of around 44 billion riyals (US\$11.7 billion). He called on Chinese firms to enter the competitions implementation of other projects in the Kingdom, (Ibid). Meanwhile China's commerce minister Chen Deming drew an optimistic picture of the relations between the two countries as he projects that the trade volumes between the two countries will increase by 50 percent by 2015, "We want to increase the trade volume to US\$60 billion by 2015 after the target of US\$40 billion (for 2010) was surpassed early in 2008", (Laessing, 2010). Some experts say that bilateral trade between China and Saudi-Arabia could "far exceed" the goal of US\$60 billion by 2015 and further strengthen trade ties with the Middle Eastern region, (Ding, 2010). Tang Zhichao, Director of Middle East Studies with the China Institute of Contemporary International Relations, argues that: "It (the goal) is a conservative estimate. There is high possibility that the China-Saudi Arabia trade would far exceed the target by 2015, as bilateral relations are getting stronger and the two nations' industries are highly complementary", (Ibid).

This optimism was clear during his official visit to Saudi Arabia in January 2010 where Saudi Arabia hosted the fourth session of the joint committee meeting, (Yu, 2010). The Minister of Commerce of China, Chen, hailed the rapid growth of bilateral economic and trade ties since the third meeting of the joint committee in 2006, noting that bilateral trade has accomplished, two years in advance, the goal of US\$ 40 billion by 2010, and Saudi Arabia has been China's biggest trade partner in West Asia for eight consecutive years, (Xinhua, January 11, 2010). In demonstrating Beijing's commitment to strengthening the economic ties binding China and Saudi Arabia, Minister Chen made a five-point proposal, in which he said both countries should

strive to expand bilateral trade to reach US\$ 60 by 2015, (Ibid). He also proposed to maintain the long term and steady crude oil trade between the two sides, in addition to enhancing cooperation on exploiting gas, oil projects and in the petrochemical industry, and by establishing a cooperation mechanism on trade remedy, (Ibid).

It's not surprisingly then that Saudi Arabia has become the biggest potential overseas contracting market for China. Yang Hongelin, the Chinese Ambassador to Saudi Arabia, told leading Saudi daily newspaper *Arab News* in September 2011 that over 80 projects under construction in Saudi Arabia are implemented by Chinese enterprises, with a total contract value of US\$12.5 billion, and there are about 16,000 Chinese business people working in Saudi Arabia, (Yang, September 30, 2011). The Chinese Ambassador also pointed out that the contracts have been signed for 35 projects worth 23.2 billion riyals (over US\$6 billion) in 2009; the finished turnover was US\$3.6 billion, (Jibril, 2010). In addition, China also signed 27 new industrial projects in Saudi Arabia during the first half of 2010, (Carey, 2010).

China is establishing itself in the Saudi market, constructing high-speed railways, desalination plants and aluminium and cement factories, (Gresh, 2011). Furthermore, Chinese contracting companies have won great reputations in the Saudi market on the basis of efficient cooperation, competitive quotation and pioneering spirits, (Yu, 2010). Projects captured by Chinese contractors range from the expansion of King Khalid University, the Makkah-Medina high-speed rail link to a scheme to build 200 schools in the Kingdom, (Drummond, 2010). Perhaps the most notable improvement of Saudi Arabia's many projects is the railway built to accommodate *Hajj* pilgrims which shuttled tens of thousands of people around the holy sites. As the modern, high-

tech trains picked up and dropped off passengers, they created a newfound respect for Chinese-made products and Chinese-engineering prowess, (Wahab, 2010). Indeed, the state-of-the-art rail system is changing people's perceptions about the country. China has overnight become a nation to respect and emulate, (Ibid) (see Table 7.2.7 below).

(Table 7.2.7): Chinese Major Contracts in Saudi Arabia 2004-2010

Company	US\$	Year	Place	Sector
Sinopec	300 millions	March 2004	Rub' al Khali (Empty Quarter)	Energy/Gas
SINOMA	276 millions	May 2005	Muzamiyah	Construction/Cement
Sinopec	380 millions	September 2005	petrochemical refinery in Yanbu	Chemicals
China National Machinery Industry Corp (SINOMACH), and China Nonferrous Metal Industries (NFC)	4 billions	April 2007	Jizan Economic City	Metals/Aluminium
China Petroleum Pipeline Bureau and China Petroleum Engineering and Construction		June 2007	360km pipeline oil from Saudi Arabia's to Fujairah.	Construction/ pipeline Energy
China's Guizhou Hongfu Industry & Commerce Development Company (Hongfu)	350 millions	December 2007	Al-Jalamid mine	Metals/ phosphate
China Harbour Engineering Company	443 millions	November 2007	Jeddah	Construction/ container terminal at Jeddah Islamic Port
Chalco	1,2 billion	November 2007	Binladin MMC	Metals/Aluminium
Guangdong Overseas Construction	612 millions	July 2008	King Khalid University	Real Estate/Construction
China Railway Construction	1,78 billion	February 2009	Makkah	Transport/Rail

China Railway 15 Bureau Group Corporation	533 millions	July 2009	Saudi Arabia	Construction/ 200 school buildings
China Civil Engineering Construction Corp	720 millions	September 2009	Riyadh to Al-Qassim	Transport/Rail
Sinopec	141 millions	January 2010	Wasea in Ritadh	Construction /Energy distribution plant
China's Sinoma International Engineering Co	200 millions	May 2010	Hail	Construction/Cement
China's Sepco III Electric Power Construction Corp (with partners)	2.4 billion	September 2010	Ras Al Zour	Water/power and desalination plant
China Harbor Engineering Company	85 millions	December 2010	Eastern Province	Expansion of Ras Al-Zour
China's Sepco III Electric Power Construction Corp (with partners)	1.0 billion	January 2011	Ras Al Zour	supply power plant components

Source: SAGIA, ARAMCO, Bloomberg, Reuters and MEED

To put things in context, after the 9/11 terrorist attacks, U.S. suppliers shunned the Kingdom, while Chinese and Asian firms rose in prominence. America's market share in Saudi trade declined from about 20 percent in 2000, (Allam, 2010), to around 14 percent in 2010, (see Table 7.3.8). If the growth of trade between Saudi Arabia and China continues in future at this rate, China is very likely to become a top trade partner of Saudi Arabia. According to John Sfakianakis, Chief Economist at Riyadh-based *Banque Saudi Fransi*, "In absolute terms, the U.S. is the biggest trading partner with Saudi Arabia...But they are losing market share. Chinese companies are competing on all fronts", (Carey, 2010), (see Table 7.3.8).

(Table 7.2.8): China and Saudi Arabia Trade with Main Partners (2010)

The Major Trade Partners					
Saudi Arabia			China		
Rank	Partners	(%)	Rank	Partners	(%)
1	EU27 ^a	15.3%	1	EU27	17.0%
2	United States	13.6%	2	United States	13.6%
3	China	13.3%	3	Japan	10.5%
4	Japan	12.7%	4	Hong Kong	8.1%
5	South Korea	7.4%	5	South Korea	7.3%
6	India	7.1%	6	Australia	3.1%
7	Singapore	3.6%	7	Malaysia	2.6%
8	Thailand	2.4%	8	Brazil	2.2%
9	Brazil	1.8%	9	India	2.2%
10	U.A.E	1.7%	10	Singapore	2.0%
11	Indonesia	1.7%	11	Russia	2.0%
12	Turkey	1.5%	12	Thailand	1.9%
13	Bahrain	1.5%	13	Saudi Arabia	1.5%
14	Pakistan	1.4%	14	Indonesia	1.5%
15	South Africa	1.4%	15	Canada	1.3%

Source: IMF (DoTS, May 2011)

(a) European Union: 27 members.

Despite this rapid growing trade between the two countries, if we exclude the importance of Saudi oil exports, the total volume of trade between Saudi Arabia and China constitute less than 1.5 percent of China's total foreign trade. On the other hand we find that the Saudi trade with China accounted for more than 13 percent of Saudi Arabia's total foreign trade. This trend indicates that Saudi Arabia could be the one who is courting the Chinese market, not the other way round (see Table 7.2.9).

(Table 7.2.9): China's Trade with the World and KSA (2002-2010, US\$ billions)

		2002	2003	2004	2005	2006	2007	2008	2009	2010
World	Exports (trillion)	325.6	0.438	0.593	0.762	0.969	1,22	1,43	1,20	1,54
	Imports (trillion)	0.295	0.412	561.2	660.0	791.5	956.1	1,13	1,00	1,41
	Total Trade (trillion)	0.620	0.851	1,154	1,421	1,76	2,17	2,563	2,20	2,95
	Balance (billion)	30.4	25.5	32.1	102.0	177.5	264.3	298.1	196.1	130.8
Saudi Arabia	Exports (billion)	1,67	2,14	2,77	3,82	5,05	7,83	10,82	8,97	32.81
	Imports (billion)	3,43	5,17	7,52	12,24	15,08	17,56	31,02	23,62	10.37
	Total Trade (billion)	5,10	7,31	10,29	16,07	20,14	25,40	41,84	32,59	43.18
	Balance (billion)	-1,76	-3,03	-4,75	-8,42	-10,03	-9,73	-20.2	-14,65	-22,44

Sources: UNCOMTRADE, (May, 2011)

As for Chinese projects in Saudi Arabia, although their share is important, in China's overseas projects it is still small or less than 4 percent of the total volume and value. According to China's official statistics, the turnover of China's over 3000 overseas contracted projects reached US\$92.2 billion in 2010, up by 18.7 percent year-on-year; and the value of newly-signed contracts was US\$134.4 billion, up by 6.5 percent year-on-year. By the end of 2010, the accumulated turnover of China's foreign contracting projects amounted to US\$435.6 billion with the contract value of US\$699.4 billion, (Ministry of Commerce, January 28, 2011). Furthermore, by the end of 2010 over 15,000 overseas enterprises were started up by Chinese state companies, according to data from the State-owned Assets Supervision and Administration Commission of the State Council (SASAC). The total assets of those overseas enterprises exceeded US\$ 1 trillion, (Min, 2011) while the Chinese workers in Saudi Arabia represent about 2.4 per cent of China's total workers abroad. By the end of 2010, the labour dispatched

overseas totalled 847,000, 69,000 more than that of 2009, (China's Ministry of Commerce, January 30, 2011).

It is also important to point out that when analysing the composition of trade between China and Saudi Arabia, the large share of its trade is in small consumer goods, such as the ornaments, hammers, and clocks which typically sell for less than a few dollars, (Simpfendorfer, 2009: 155). In the table below, the Chinese exports do not contain sophisticated technology ...their composition is similar to China's exports to most countries in the region. Its low-price products, including textiles, garments and toys, have a ready market among migrant workers and the low and middle income workers in Saudi Arabia, where they do not compete with local products as they do in Africa and some other Arab countries, (Gresh, 2010) (see Table 7.2.11).

(Table 7.2.10): Saudi Arabia's Top 5 Products Imported from China (2001-2010)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
All Products (US\$ billions)	1,3	1,6	2,1	2,7	3,8	5,0	7,8	10,8	8,9	10,3
In US\$ millions										
Women's Suits, dresses, skirt etc & short, knit/croch	53,8	83,8	134,2	136,5	134,8	99,3	330,7	345,1	350,4	453,1
Electric Applications for Line Telephony, Incl curr Line System	8,1	5,5	10,1	60,5	59,9	61,7	191,7	442,9	562,6	447,7
Other Furniture and Parts thereof	17,7	35,5	58,5	73,5	103,4	152,9	176,7	264,1	333,6	337,9
Automatic Data Processing Machines; Optical Reader, etc	13,6	17,4	23,1	34,5	48,9	106,4	139,4	239,0	259,6	305,4
Men's Suits, Jackets, Trousers etc & Shorts, Knit/Croch	28,2	47,1	69,3	93,9	104,9	82,2	245,3	236,0	234,5	302,8

Source: adapted from UNCOMTRADE, (May, 2011)

On the other hand, when analysing the composition of China's imports from Saudi Arabia, we will find that exports of oil, chemicals, and plastics account for almost 100 percent of the total Saudi exports to China. They represent about three quarters of the total trade volume between China and Saudi Arabia, evidence that the trade is based on oil.

(Table 7.2.11): Saudi Arabia's Top 5 Products Exported to China

(US\$ billions, 2001-2010)										
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
All Products	2,7	3,4	5,1	7,5	12,2	15,0	17,5	31,0	23,6	32,8
Mineral Fuels, Oils, Distillation Products, etc	1,9	2,4	3,7	5,4	9,2	11,8	13,6	26,4	19,3	25,8
Organic Chemicals	0,380	0,517	0,745	1,2	1,7	2,0	2,6	2,6	2,7	4,0
Plastics and Articles thereof	0,408	0,411	0,486	0,656	1,0	1,0	1,0	1,0	1,3	2,3
Polymers of Propylene or of other Olefins, in primary forms	0,028	0,069	0,083	0,078	0,148	0,165	0,163	0,276	0,439	0,911
Cyclic Hydrocarbons	0,051	0,071	0,130	0,265	0,251	0,267	0,266	0,355	0,541	0,757

Source: adapted from UNCOMTRADE, (May, 2011)

7.3 CROSS INVESTMENTS: LOOKING FOR OPPORTUNITIES

In the last two decades, several factors have contributed to improving Saudi Arabia's investment environment. (a) The Saudi Government does realise the importance of diversification, as the Saudi economy remains heavily dependent on oil, which accounted for about 85 percent of its budgetary revenue in 2010 and around 31 percent of its gross domestic product, leaving the Kingdom exposed to price volatility,

(Shamseddine, 2011). (b) The Kingdom's desire to join the World Trade Organisation (WTO) since the late nineties. (c) The repercussions of 9/11 confirmed to Saudi leadership the urgent need for structural reforms to cope with external pressures and to address domestic problems.

In this context, the Saudi Government started to lay the economic foundation to achieve economic liberalisation and diversification. On April 2000 the Saudi Arabian General Investment Authority (SAGIA) was created by the Saudi Government as part of measures geared towards formalising the process of economic liberalisation. SAGIA is responsible for managing the investment environment in the Kingdom. Its objective is to achieve rapid and sustainable economic growth by creating a pro-business environment, providing comprehensive services to investors and fostering investment opportunities in key sectors of the economy, including energy, transportation, ICT and knowledge-based industries, (SAGIA, 2010).

Afterwards, in October 2002, the Saudi Ministry of Economy and Planning held a symposium to address the issue of Saudi development strategies. Through this symposium, Vision 2020 was developed which is an “expression for the national development strategies of the Kingdom of Saudi Arabia up to the year 2020”, (Saudi Ministry of Commerce and Industry, 2010). In Vision 2020, the strategies were organised along five distinct themes (Ibid): (a) Economic diversification; (b) Development of human resources; (c) Expansion of public services needed to support these objectives; (d) Promoting the expansion of the private sector as a key partner in the implementation of Vision 2020; (e) Streamlining and modernising the governance structures of the public sector to meet the challenges of implementation, (Ibid).

Two years later, one of King Abdullah's most ambitious plans, the 10x10 Program, was established in 2004. In the plan Saudi Arabian General Investment Authority seeks to establish Saudi Arabia as one of the world's ten most competitive countries by the year 2010. Three major initiatives have been implemented to help Saudi achieve its 10x10 target (Ibid): (a) Establishment of a National Competitiveness Centre (NCC). The NCC is an independent body set up to monitor, assess and support competitiveness in Saudi Arabia. (b) Instrumental to this plan, six new economic mega-cities, four of which have been launched to encourage private-sector involvement, which will allow 100 percent foreign ownership. The objectives of the economic cities are to: promote balanced regional development, achieve economic diversification, create jobs and enhance competitiveness in Saudi Arabia. And (c) Sector opportunities: SAGIA is actively pursuing investment in the sectors where Saudi has a current or potential competitive advantage. These include energy, transport and knowledge-based industries, (Ibid).

By joining the World Trade Organisation in December 2005, Saudi Arabia committed to opening up its economy through reform of its trade and investment policies as well as that of its regulatory structure – with the private sector as a key driver of economic development. Economic reforms have created many opportunities for foreigners seeking new trade and investment avenues. In addition, this development was coupled with the establishment of the Saudi National Competitiveness Centre (NCC) in 2006. Saudi Arabia became a developing country making the transition from selling its raw materials to a country selling processed goods. The initial outcomes were impressive:

1. Saudi Arabia was one of the top 10 most attractive countries in the world for Foreign Direct Investment (FDI) in 2009 with inflows reaching US\$36 billion, according to the World Investment Report (WIR 2010), (World Investment Report 2010: 4), ranking 12 on 2010 (see Table 7.3.1).
2. Saudi Arabia's ranking in the World Bank report of Doing Business 2012 jumped from to 67 in 2005, to 12 in 2011, (World Bank 2012: 6). Additionally, Saudi Arabia remained the regional leader with a global ease of doing business, ahead of the U.A.E., Bahrain, and Qatar. The report also ranks the Kingdom ahead of advanced economies, such as Canada, Japan, Germany, France, and Spain, (Ibid).
3. Saudi Arabia has been ranked among the world's top 10 countries in terms of the least risky debt sovereign. According to the fourth quarter of 2010 sovereign debt credit risk data by financial research firm CMA Vision, the Kingdom has a 5.2 percent chance of defaulting over the next five years - on par with Germany, (CMA Vision, January 7, 2011).

(Table 7.3.1): World's Top 10 (FDI) Destinations in 2010 (US\$ Billions)

	Country	FDI inflows
1	United States	228
2	China	106
3	Hong Kong	69
4	Belgium	62
5	Brazil	48
6	Germany	46
7	UK	46
8	Russia	41
9	Singapore	39
10	France	34
11	Australia	32
12	Saudi Arabia	28

Source: UNCTAD, World Investment Report, (July 2011: 4)

Five years ago Chinese firms used to look solely for manufacturing in the Middle East. Now, though, they are increasingly seeking to take equity in the projects they help develop, or even be the principal developer. One example is the case of Chinese firms Sinomac and NFC, which are contracted to build two aluminium-processing plants in the south-eastern Saudi Arabian city of Jazan. Under the terms of the agreement, NFC will help raise funds for the project from Chinese banks. But NFC has entered into a partnership with a U.S. metal trading company in the hope of taking a 25 percent stake in the two plants, (O'Neill, 2007).

In recent years, Saudi Arabia has invited China to invest and assist in developing Saudi Arabia's massive infrastructure sector and China has shown some interest in doing so. When the Saudi Monarch visited China in 2006, King Abdullah invited Chinese businessmen to invest in Saudi Arabia and take advantage of the Kingdom's economic reforms and privatisation of some state-owned firms, (Pant, 2006: 45-52). With Chinese investments, Saudi Arabia hopes to improve its infrastructure which includes a wide range of investment opportunity encompassing gas, water desalination, power generation and railways, (Madsen, 2006). Outside of investments in Saudi Arabia's infrastructure, China has expressed interest in investing in certain industries within Saudi Arabia. China has already invested over US\$4 billion in Saudi Arabia's refinery to produce alumina or aluminium oxide, (Amy, 2006). In March 2009 Saudi Arabia also awarded a SR6.79 billion (US\$1.8) railway infrastructure contract to a consortium including a unit of China Railway Construction Corp, contractors. The rail section will link Jeddah's airport to the cities of Makkah and Medina, home to Islam's holiest sites, (China Economic Review, December 14, 2009).

China could be an essential partner in enhancing Saudi Arabia's national industrial strategy in the years to come. Doubling industrial contribution to 20 percent of GDP by 2020 is Saudi Arabia's goal, (Sfakianakis, 2011). Saudi Arabia is particularly eager to attract Chinese investments in its petrochemical industry. The Governor of SAGIA, Amr AL-Dabbagh, made it clear that Saudi Arabia intends to be a major player within the global petrochemical industry when he laid out Saudi Arabia's goal of: (a) Capturing 15 percent of the global plastic market by 2020; and (b) Increasing ethylene output, from 7 to 14 million tonnes by 2010, (Amy, 2006). Saudi Arabia is attempting to become one of the top three countries in this sector and has on numerous occasions' courted Chinese support to develop their petrochemical industry, (Ibid). AL-Dabbagh was confident that Saudi Arabia would reach its goals to the point that he stated: "China should invest in Saudi Arabia's petrochemical sector or risk becoming a victim of the Gulf nation's aggressive bid to use its energy reserves to become an industry leader", (Ibid).

From the Saudi perspective, China is an extremely attractive partner to solicit petrochemical investments from because it is an export-oriented country, and much of their exported goods use petrochemicals (i.e. plastics, fertilisers, detergents, resins). The greater the amount of Saudi petrochemicals the Chinese use to produce its export products, the greater the Saudi profits; therefore, as Chinese global exports grow, so too will Saudi profits. In AL-Dabbagh's words, Saudi Arabia needs an investor "who could also push the product, and they (the Chinese) have markets that can take these products. They have the distribution channels", (Reuters, November 10, 2006). For the Chinese, it does make economic sense to invest in the Saudi petrochemical industry. It would be cheaper for Chinese companies to process petrochemicals in

Saudi Arabia and then ship to China rather than shipping the raw materials and resources to China and then processing petrochemicals there, (Ibid). Saudi Finance Minister Ibrahim Al-Asaf, for his part, said that Saudi Arabia hopes to see and will provide convenience for more Chinese enterprises to participate in Saudi economic construction as the country is speeding up its petrochemical industry, urban development, and traffic and environmental protection projects, (Xinhua, January 11, 2010).

Within this framework, China and Saudi Arabia are making capital investments in one another's markets. Often, these investments are targeted at improving the effectiveness of pre-existing trading relationships, or catalysing new ones. AL-Dabbagh said that direct Chinese investment has helped to enhance the competitiveness of his company's mining projects, in turn bolstering the quantities of commodities the firm is able to export to China, (Ibid). While there has been limited Sino-Saudi cooperation in the petrochemical field (see Table 7.3.5), China has yet to substantially invest in Saudi's petrochemical industry, despite Saudi Arabia's aggressive efforts to solicit Chinese investments.

Interestingly, Saudi companies have instead invested in Chinese petrochemical factories to gain a foothold in the Chinese economy. On November 10, 2006, Saudi Basic Industries Group (SABIC) stated that it intends to form a joint venture to build petrochemical facilities in China, (SABIC, November, 2006). Saudi Basic Industries Corp. (SABIC) and China Petroleum and Chemical Corp. (SINOPEC) announced in May 2010 the start-up of a commercial production at the newly constructed petrochemical complex in Tianjin, China, (SABIC, May 11, 2010). Mohamed al-

Mady, SABIC's chief executive, said: "SABIC's growth in China has no limits, especially when the Chinese market is currently the world's biggest for petrochemical products", (Reuters, December 6, 2009). Al-Mady also told the *Financial Times* that "China and Saudi Arabia are our most important markets," (Allam, 2010).

However, if the demand for Chinese goods and petrochemicals increases and the Chinese do determine that it would be more cost-efficient to produce petrochemicals in Saudi Arabia, great potential exists for Chinese investments in Saudi Arabia's petrochemical industry in the future. The Sino-Saudi relationship in this realm is mutually beneficial. While Chinese companies have an opportunity to profit from investing in various industrial projects, Saudi Arabia would also be benefiting from whatever Sino-Saudi economic arrangements it enters by receiving: (a) Chinese investments and technology for its industries, and/or (b) Chinese assistance in developing the necessary infrastructure that Saudi industries rely on to further grow and become competitive. There is no doubts that the amount of Chinese investments into Saudi Arabia is projected to increase in the future as China and Saudi Arabia are studying a plan to establish a fund to promote investment between the two countries, (Ibid). It is also important to note that, despite the fact there is great potential in this realm for the Sino- Saudi relationship, other than the US\$4 billion investment China made in Saudi Arabia's alumina or aluminium oxide refineries (and other two projects, see Table 7.3.5), there has not been much Sino-Saudi interaction as of yet.

While each side is taking the first steps for the Sino-Saudi relationship to grow in this area there has not been any substantial investments, or mega-projects. According to figures cited by the Saudi Minister of Finance Ibrahim Al-Assaf, he pointed to the

weakness of the volume of joint projects between the two countries, where there are only 19 joint ventures, (Hamidi, 2010). Furthermore, Mohammed Ajlan, Vice President of Saudi-Chinese Business Council, told *Asharq AL-Awsat* newspaper on January 22, 2011 that: “The volume of licences granted by Saudi Arabia to Chinese investments is US\$ 8.5 billion, while the amount actually invested in the Kingdom doesn’t exceed US\$ 400 million. This figure is tiny compared with Chinese investments in other countries, (Ziani, 2010). In addition, Saudi Arabia’s share of China’s total global outward investment “between” 2005 and 2010 was only 4.6 per cent and ranked in 8th position (see Table 7.3.2).

(Table 7.3.2): China’s Outward Investment Destinations, (2005-2011)

Non-Bond Transactions, From January 2005 to June 2011			
	Country	U.S. billions	(%) of Total (a)
1	Australia	38.4	14.6%
2	U.S.	30.5	11.5%
3	Brazil	18.3	6.9%
4	Iran	17.1	6.5%
5	Nigeria	15.3	5.8%
6	Argentina	14.0	5.3%
7	Indonesia	13.5	5.1%
8	Saudi Arabia	12.2	4.6%
9	Kazakhstan	11.5	4.3%
10	Canada	10.4	3.9%
11	Algeria	9.2	3.4%
12	Russia	9.1	3.4%
13	Britain	9.0	3.4%
14	Switzerland	7.3	2.7%
15	Vietnam	7.2	2.7%
16	Singapore	7.0	2.6%
17	South Africa	6.6	2.5%
18	D.R Congo	6.6	2.5%
19	Iraq	5.5	2.0%
20	Greece	5.2	1.9%
21	Others	9.1	3.4%

Source: Adapter from Heritage Foundation, China Global Investment Tracker 2011

(a) Percentages were calculated by the author

Meanwhile the Saudi direct investments in China are still small compared to the size of the economy and the amounts of the overall FDI in China. The biggest Saudi investments in China concentrate in the energy sector. Saudi Aramco has 25 percent in the US\$ 5 billion refinery in China's Fujian province, while SABIC collaborated with Sinopec to build a petrochemical complex in the northern Chinese port city of Tianjin. Outside of the energy sector the Saudi investments are insignificant. Mohammed Ajlan, Vice President of Saudi-Chinese Business Council, noted that Saudi companies' investments in China are limited and estimated they are worth about US\$8 billion, mostly in the petroleum and petrochemicals sectors. According to the Chinese official figures, the Arab States' total investment in China was estimated at US\$2.15 billion by mid-2010, mainly in the real estate, chemical and food sectors, (Ding, 2011) (see Table 7.3.2 and Table 7.3.3).

(Table 7.3.3): China and Saudi Arabia Cross FDI, (2002-2010)

Year		2002	2003	2004	2005	2006	2007	2008	2009	2010
Economy	FDI									
China	Inward (US\$ Billions)	52,7	53,5	60,6	72,4	72,7	83,5	108,3	95,0	105,7
	Outward (US\$ Billions)	2,5	2,8	5,4	12,2	21,1	22,4	52,1	56,5	68,0
	To Saudi Arabia (US\$ billions)	0,001	0	0,001	0	1,1	1,4	1,3	1,6	
	Saudi Share of China's Total Outward (%) ^a	0	0	0	0	5.1%	6.3%	2.5%	3.4%	
Saudi Arabia	Inward (US\$ billions)	0,453	0,778	1.9	12,1	17,1	22,8	38,1	32,1	28,1
	Outward (US\$ billions)	2,02	0,473	0,079	6,6	5,3	12,7	1,4	6,5	
	Saudi Utilized FDI into China (US\$ millions)	13,14	3,55	7,01	9,3	8,1	122,6	275,2	113,65	
	China's Share of Saudi total Outward (%) ^b	0.5%	0.7%	8.8%	0.1%	0.1%	0.9%	18.9%	1.7%	

Source: UNCTAD, China's Ministry of Commerce and SAGIA

(a) & (b) All percentages were calculated by the author

Indeed, the U.S. is still Saudi Arabia's largest source of FDI in Saudi Arabia. In 2010, there were 357 U.S.-Saudi joint ventures with a value US\$21.9 billion, (U.S.-Saudi Arabian Business Council, November 2010). U.S. Undersecretary for International Trade Affairs Francisco Sanchez noted that American investments represent more than 25 percent of all direct foreign investments in the Kingdom. Furthermore, a number of U.S. corporate giants, including Exxon Mobil, are seeking new joint ventures with Saudi Arabia, (Royal Embassy of Saudi Arabian Washington, December, 2010). Although China has increased its direct investments towards Saudi

Arabia since 2006, China is still ranked sixth, and its (FDI) represented only 4.6 percent of the total FDI in Saudi Arabia, compared to U.S., which is in the first place (see Table 7.3.4 below).

(Table 7.3.4): Top 10 Countries Investing in KSA 2009 (US\$ millions)

		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Total FDI Inflows to KSA		183	504	453	778	1,942	12,097	17,140	22,821	38,151	35,514
USA	FDI (US\$)	7	16	8	268	269	84	1,594	3,978	5,228	5,830
	(%) of Total^a	3.8%	3.2%	1.7%	34.0%	13.0%	0.6%	9.2%	17.4%	13.7%	16.4%
Kuwait		2	29	9	2	13	25	267	2,370	4,638	4,299
UAE		1	5	1	10	846	5,015	-19	2,381	5,595	3,787
France		8	5	16	28	2	2,057	2,053	1,136	3,022	2,558
Japan		3	0	0	1	1	2,540	3,512	1,068	3,246	2,044
China	FDI (US\$)	0	0	1	0	1	0	1,100	1,428	1,323	1,665
	(%) of Total^b	0%	0%	0.0%	0%	0%	0%	6.4 %	6.2 %	3.4 %	4.6 %
Netherlands		5	0	0	10	2	49	820	904	1,363	1,344
Bahrain		3	0	2	42	116	445	789	593	1,681	1,095
UK		1	2	36	4	68	147	636	444	998	886
Jordan		17	27	34	32	42	73	557	384	841	818

Source: Saudi Arabian General Investment Authority (SAGIA), (2010)

(a) & (b) Percentages calculated by the author

7.4 FACTORS COULD SLOW CHINA-SAUDI ECONOMIC EXPANSION

Despite the surge in trade since 2000, experts note a slew of factors slowing expansion, comprising of mutual suspicions and a lack of developed business relationships. Further obstacles which remain also include trade disputes, language barriers, business attitudes, methods of dealing with the outside world, differences

between Saudi and Chinese laws as well as a lack of transparency in information and data on potential investment projects, (Ramady, 2006):

- (1) The absence of a database on the volume, types of investment and trade opportunities available to Chinese companies and/or the Saudi investors, (Elsidafy, 2009). In addition, there is a significant shortfall in the numbers of the specialised companies which study and market opportunities.
- (2) While China provides Saudi producers with a lucrative market today, there is no guarantee that it will remain so in the longer term. This means that if China's growth slows down in the future — which most economists agree will happen, yet they do not know when — Saudi producers will face harder competition with Chinese firms in the Chinese market, (Yamada, 107).
- (3) The absence of direct communication could be a factor undermining China-Saudi relationship going beyond energy. Unlike the West, there are very few Chinese experts in the Gulf. Very few Chinese companies have employees who speak Arabic, and vice versa, (Zhang, 2008). For example, businesses from either side do not always know what to expect when they venture into the other: some experts say going into the [Saudi] economic cities, Chinese companies' leaders will wonder who is in charge. Is it the Saudi companies? Is it the central government? Is it the regional government? When large amounts of money are on the table, these unknowns become very real business risks, (Teslik, 2008). Local companies are often able to work around these market eccentricities and skirt bureaucracy through connections, but it takes time to develop these relationships and to garner the trust that makes them work effectively, (Ibid).

- (4) The perception that the Chinese companies lack advanced technology in comparison to western companies. Still China has a big sales job in persuading buyers that the qualities of their high-end products are just as high as that of its competitors. For example, Saudi tycoon Abdulrahman Abdullah Al Zamil told *Forbes* magazine: “I received a very competitive price from China for [red-brick making] machinery... Even though [the price] was 30 percent cheaper, my partners refused; they said we need German machinery. The Chinese are going to have difficulty changing minds”, (Andelman, 2006).
- (5) Failure by Chinese companies which export products to Saudi Arabia to abide by standard specifications and quality levels, (Elsidafy, 2009). Faced with copycat and quality problems, many companies in China are struggling to shake off the “made in China” stereotype. Abdul Rahman Al-Jeraisy, Vice President of the Council of Saudi Chambers of Commerce and Industry, expressed these Saudi concerns strongly: “We are concerned about the quality of the imported goods to protect the Saudi consumers from fraud and counterfeit products”, (Rasooldeen, 2010). While Saudi Minister of Finance Ibrahim Al-Assaf said that the obligation to “quality and specifications” will be a key condition for boosting trade exchange between the two countries during the coming period, (Hamidi, 2011). In this context, there are also serious allegations against Chinese industries. In January 2011 the Chairman of the Saudi Consumer Protection Society (SCPS) warned that some products imported from China could contain cancerous materials, (Fakkar, 2011). This issue also worries the Chinese. During a visit to the Saudi capital on March 2011, Qong Izeng, the Deputy Governor of Jajiang Chinese province, urged

local businessmen not to import counterfeit or poor quality goods from his country, saying that such products not only damage China's reputation but also result in huge losses for the Kingdom's economy, (Abdullah, 2011).

- (6) The obstacles of Chinese markets to Gulf commodities and goods, especially petrochemicals; China has accused Saudi Arabia in the past of dumping petrochemicals on its markets, (*The Economist*, 2010). China's ethylene producers may be hurt from imports from the Middle East that have a price advantage, (YarnsandFibers, 2010). Currently, China has 19 ethylene producers, mainly subsidiaries of Sinopec and PetroChina, China's largest refiners. In Middle Eastern countries, the production costs of such petrochemical products as ethylene, polyethylene and glycol is less than 30 percent of most Chinese refineries, (Ibid).
- (7) Sectors such as mining, electrical power, transport, manufacturing, scientific research and telecoms are seen as "vital industries in key sectors" by the Chinese government, limiting foreign investment in them. There are exceptions. A petrochemical is considered a strategic sector, but it is an area in which Saudi Arabia's technological level is higher than China's, (Ibid).
- (8) Many foreign companies (including the Chinese) in Saudi Arabia still complain of an unsatisfactory regulatory climate, requirements for maintaining large local bank balances, particularly in the case of foreign-owned trading companies, and "Saudization" of the work force, as specific impediments to further growth and investment.
- (9) A rise in the cost of Chinese commodities in recent years, which has prompted Gulf consumers to obtain commodities and goods from Southeast Asia; and

the limited availability of airlines and shipping firms to carry goods from China on a regular basis.

(10) The Chinese and Saudis do have another bone of contention: workers' unrest. Chinese workers on the Makkah underground damaged train carriages and smashed windows in protest against their low wages and poor working conditions in 45-degree heat (to the displeasure of the Saudi authorities), (Gresh, 2011). Slashing prices has a cost; a much-heralded project, a railway between Makkah and the holy sites of Mina and Mount Arafat, recently built by the Chinese, has ended in a row, with China Railways threatening to sue the Saudi authorities for the losses it has made on the investment, (*The Economist*, 2010). The project was a technical success, but the pressure Beijing exerted on its company to complete the project resulted in a US\$600 million loss for the firm, (Ramzy, 2011). Some firms would have been put off by the fact that non-Muslims are barred from working in Makkah, so China simply converted hundreds of railway workers to Islam. The project also ran into problems over the allocation of land, cost overruns, and even workers' riots, which rarely occur in Saudi Arabia, (Ibid). Other blunders have been sillier – a shop selling safes in the new China Mart only had catalogues and instructions in Chinese, (Gresh, 2011).

(11) Rising numbers of trade disputes. According to the Economic and Commercial Counsellor's Office of the Embassy of the People's Republic of China in the Kingdom of Saudi Arabia, the trade dispute cases claimed and coordinated in 2010 amounted to 84 with the sum of US\$6,615,454. The cases claimed by Chinese companies are 9, and account for 10.71 percent, with the sum of US\$515,776, accounting for 7.8 percent of the total. The cases claimed

by Saudi companies are 75, and account for 89.29 percent, with the sum of US\$6,099,678, accounting for 92.2 percent of the total (Economic & Commercial Counsellor's Office of Chinese Embassy in Saudi Arabia, January 31, 2011). Complaints from Saudi companies to Chinese companies account for a big proportion. The main reasons of trade disputes are Internet shopping fraud, quality problems and breach of contracts, etc, (Ibid).

(12) With the continued U.S. and international pressure on China to revalue its currency, there are increasing concerns among Saudi economists and traders that this step will make Chinese goods more expensive at a time of high rates of inflation in the Kingdom.

(13) And finally, despite his optimism, Ben Simpfendorfer, who is a well-known economist and expert in China and the Middle East, also injects a few notes of caution: politically, other parts of Asia have stronger Islamic ties with the Arab world than China does. Beijing must ensure that its "Go out" policy of encouraging local firms to venture abroad does not swamp Arab markets with imported goods, destroying jobs and goodwill, (Wheatley, 2009). Ties are flourishing but have to be seriously stress-tested. Simpfendorfer concludes: "It is still too early to judge the outcome...Tensions between the China growth model and Go Global are a useful reminder that relations between the Arab world and China are still delicately poised", (Ibid).

7.5 CONCLUSION

This chapter has attempted to decipher Chinese intentions toward Saudi Arabia. The main question it attempted to address was whether Chinese actions were in accordance with the offensive realism model or economic interdependence school of thought. As stated earlier in the chapter, if China is acting in the realism model, it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence. This would include proactive actions to: (a) Provide Saudi Arabia with massive economic assistance and incentives to develop closer Sino-Saudi economic and political ties with the intent to reduce U.S. power and influence; and (b) Allocate huge investments in Saudi Arabia's economy to make it dependent on Chinese capital significantly. If China is acting in accordance with the economic interdependence model, it should be: (a) Interacting economically with Saudi Arabia in a manner which makes economic sense; and (b) Developing a Sino-Saudi political relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship.

This chapter has shown that Chinese intentions are more along the lines of the economic interdependence school of thought rather than the realism model. China views Saudi Arabia not only as a long-term energy source but also as an opportunity to further expand economically - not as a state that it wishes to wrestle away from U.S. power and influence. With respect to the Sino-Saudi economic relationship, China is primarily concerned with three things: (a) Securing Saudi Arabian energy sources in order to continue its economic growth over the long term; (b) Expanding its trade market in Saudi Arabia; and (c) Taking advantage of various investment

opportunities in Saudi Arabia. These three goals are all economic in nature and are not intended to undermine U.S. influence in the region. If China was acting in the realism model, it should be taking advantage of every opportunity to use its economic resources, even if its policies do not make economic sense, towards a political agenda of developing closer Sino-Saudi ties in a manner which decreases U.S. power and influence in Saudi Arabia. On the contrary, Chinese economic policies toward Saudi Arabia make economic sense and are not political in nature with respect to the international balance of power. China has not arbitrarily invested in Saudi Arabia with the sole purpose to develop closer Sino-Saudi ties. It is also interesting that China has not invested heavily in Saudi Arabia, despite the Kingdom's government desire for more Chinese investments. These actions are not consistent with a state that is aggressively trying to expand its power and influence in a region at the cost of the United States.

As for future trade expectations, great potential exists for Sino-Saudi relations to expand substantially in the future. As was evident in the preceding chapters, China's needs for oil, petrochemical, plastic and aluminium will increase steadily in the future and Saudi Arabia will be a major player in providing China with those needs. Saudi Arabia is also pumping hundreds of US\$ billions for the development of infrastructure, employment and housing projects and the Chinese companies will play an important role in the completion of these projects. Additionally, future initiatives to broaden China-Saudi trade links include the ongoing negotiations with regards to a Free Trade Agreement (FTA) between China and the GCC countries.

CHAPTER EIGHT

OIL - THE BACKBONE OF GROWING TIES

8.1 INTRODUCTION

A decade ago, China imported relatively little crude oil from Saudi Arabia; today, it is one of the top three markets and is the fastest growing international market, (Saudi ARAMCO Annual Review: 2010: 35). Currently, Asia accounts for about two thirds of Saudi crude oil, refined products and natural gas liquids exports, while China accounts for one fifth of the Saudi Arabia's Asian export market, (Dawnay, 2011). The bilateral relationship is also of growing importance; for nine years (2002-2010), Saudi Arabia has consistently been China's top oil provider. A reflection of the importance of China for Saudi Arabia came in May 2010. In the first time in its history, Saudi ARAMCO'S Board of Directors met in China in 2010. The regular spring semi-annual meeting in Beijing on May 6-7 was a good occasion to celebrate the company's strong, multi-faceted and mutually beneficial relationship with China, (Saudi ARAMCO Annual Review: 2011: 5).

This chapter's main aim is to decipher Chinese intentions toward Saudi Arabia. The main question it attempts to address is whether Chinese actions are in accordance with the realism model or economic interdependence school of thought. If China is acting in the realism model, it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. influence. This would include proactive actions to: (a) Provide Saudi Arabia with massive energy assistance to develop closer Sino-Saudi ties with the intent to reduce U.S. influence;

(b) Allocate huge investments in Saudi Arabia's energy sector to make it significantly dependent on Chinese capital; and (c) Import more Saudi oil to make the Kingdom more reliant on the Chinese market. If China is acting in accordance with the economic interdependence model, it should be: (a) Interacting economically with Saudi Arabia in a manner which makes financial sense; (b) Developing a Sino-Saudi oil relationship based on furthering their economic interests and not based on degrading the U.S.-Saudi political relationship; and (c) Working to diversify sources for oil suppliers without becoming more dependent on Saudi Arabia. In this regard we will show the conditions under which high energy interdependence between China and the Middle East will lead to a pacific or belligerent China. If decision-makers' expectations of future trade are high they will likely pursue policies that will enhance security in the region. On the other hand, if they have a negative view of their future trading environment they will likely take action to protect their interests in the region.

8.2 CHINA'S OIL POLICY: EMERGING OF A RELIABLE PARTNER

China is using its state-owned energy corporations to pursue a "two imports and one export" strategy in the Middle East and North Africa Region (MENA). The Chinese energy companies conclude long-term supply agreements for oil and gas (e.g. with Saudi Arabia, Iran, Oman, Sudan, Yemen, Libya, Kuwait, Qatar, and Algeria). At the same time, the region's financially powerful (and often higher-tech) energy companies (Saudi-ARAMCO above all) are encouraged to invest in the Chinese downstream sector. This strategy's export element is bound up with a direct

involvement of Chinese companies in the development of oil and gas fields as well as in the production of oil, (Steinhilber, 2006). For example, China's oil company, Sinopec, is committed to the exploration of natural gas in the Saudi region, while Saudi ARAMCO and SABIC have made significant investments in the development of the oil refinery and petrochemical infrastructure in China, (Mobrez, 2008). Furthermore, since the 1980s, China's relationship with Saudi Arabia has evolved from one centred around arms sales to one which ensures the supply of energy resources to support China's economic growth. China has made significant efforts to diversify its sources of oil, developing resources in Russia, Central Asia, Africa, and Latin America. However, for almost the last decade, Saudi Arabia has consistently been China's top oil provider and this is likely to continue for the foreseeable future (see Table 8.2.1 below).

(Table 8.2.1) China-Saudi Arabia Energy Trade, (2002-2010, US\$ billions)

Selected Indicators			2002	2003	2004	2005	2006	2007	2008	2009	2010
China	Middle East	Total Trade	21,3	31,3	43,5	60,2	81,6	108,6	157,6	123,2	171,3
		Mineral Fuels, Oils, Distillation Products, etc	7,2	11,3	17,1	25,2	34,1	39,2	68,6	45,8	68,7
	Saudi Arabia	Total Trade	5,1	7,3	10,2	16,07	20,1	25,4	41,8	32,5	43,1
		Mineral Fuels, Oils, Distillation products, etc	2,4	3,7	5,4	9,2	11,8	13,6	26,40	19,3	25,8
		(%) Saudi of Total Middle East Trade	23,9	23,3	23,4	26,6	24,6	23,3	26,5	26,3	25,1

Source: UNCOMTRADE, (May, 2011)

China's oil imports from Saudi Arabia between 1990 and 1999 were small in terms of volume or value, as countries like Oman and Iran were China's top major oil partners during that period. China began limited crude oil imports in 1988, favouring low-sulphur heavy waxy crudes from Indonesia and elsewhere which were similar to its domestic grades that were suited to China existing refineries, (Yamaguchi & others, 2002). Indeed, Oman and Iran were the only two Middle Eastern countries which exported oil to China in 1989. Even in the 1990s, China's oil imports from the Middle East were mostly focused on Oman and Yemen, (Hongtu, 2010).

As demand continued to grow, China itself became a net oil importer in 1993 and a net crude oil importer in 1996. In the period (1993-1998) China's main oil import partners were Oman, Yemen, Iran and others, (Ibid). For example, in 1995, Saudi Arabia was China's 25th largest exporter of oil but moved quickly to seventh place in 1999, then occupied the fourth position in 2000, then later climbed to second place in 2001. In 2002, Saudi Arabia became for the first time China's top supplier of oil (ARAMCO, June 23, 2008) and since then Saudi Arabia still dominates this position, (see Tables 8.2.2 and 8.2.3).

(Table 8.2.2): Chinese Oil Imports 1992-1998 (selected countries thousand b/d)

	1992	1993	1994	1995	1996	1997	1998
China's total	227.2	313.4	247.0	341.8	452.4	709.4	546.4
Oman	61.2	81.6	67.2	73.0	113.0	180.6	115.8
Yemen	8.6	33.0	25.0	49.4	75.2	81.0	80.8
Iran	2.2	1.3	1.3	18.6	46.2	55.0	72.4
U.A.E	4.6	11.4	1.3	7.2	n/a	0.9	10.2
Saudi Arabia	3.6	4.2	2.8	6.6	4.6	9.8	36.0

Source: Derived from Chinese customs data and converted at 7.3 barrels per tonne.

In fact, the increase in China's oil imports from Saudi Arabia has occurred only during the past decade, especially after the Chinese president Jiang Zemin visited the Kingdom in 1999. China's oil imports from Saudi Arabia jumped dramatically in the last decade with about a quarter of China's crude imports now coming from the Kingdom, or about 1 million barrels a day compared with 455,000 barrels a day in 2005, (Meyer, 2010), 228,744 barrels/day in 2002 (ARAMCO, June 23, 2008) and about 50,000 barrels a day in 1999 (see Table 8.2.3 below).

(Table 8.2.3): China's Top Oil Suppliers, 1999-2010, (million tons^a)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
China's Total	36.6	70.2	60.2	69.4	91.1	122.8	127.1	145.2	163.2	178.8	203.7	239.3
China's Top Oil Suppliers (b)												
Saudi Arabia	2.4	5.7	8.7	11.3	15.1	17.2	22.1	23.8	26.3	36.3	41.8	44.6
% of Total	6.5	8.1	14.5	16.4	16.6	14.04	17.4	16.4	16.1	20.3	20.5	18.6
Angola	2.8	8.6	3.7	5.7	10.1	16.2	17.4	23.4	24.9	29.8	32.1	39.4
% of Total	7.6	12.2	6.3	8.2	11.1	13.2	13.7	16.1	15.3	16.7	15.7	16.4
Iran	3.9	7.0	10.8	10.6	12.3	13.2	14.2	16.7	20.5	21.3	23.1	21.3
% of Total	10.6	9.9	18.0	15.3	13.6	10.7	11.2	11.5	12.5	11.9	11.3	8.9
Oman	5.02	15.6	8.1	8.04	9.2	16.3	10.8	13.1	13.6	14.5	11.7	16.7
% of Total	13.7	22.1	13.5	11.6	10.1	13.3	8.5	9.0	8.3	8.1	5.7	7.0
Russia	0.572	1.4	1.7	3.02	5.2	10.7	12.7	15.9	14.5	11.5	15.3	15.2
% of Total	1.5	1.9	2.8	4.3	5.7	8.7	9.9	10.9	8.8	6.4	7.5	6.3
Sudan	0.266	3.3	4.9	6.4	6.2	5.7	6.6	4.8	10.3	10.4	12.1	12.5
% of Total	0.7	4.7	8.2	9.2	6.8	4.7	5.2	3.3	6.3	5.8	5.9	5.2

Source: General Customs Administration of China, various years

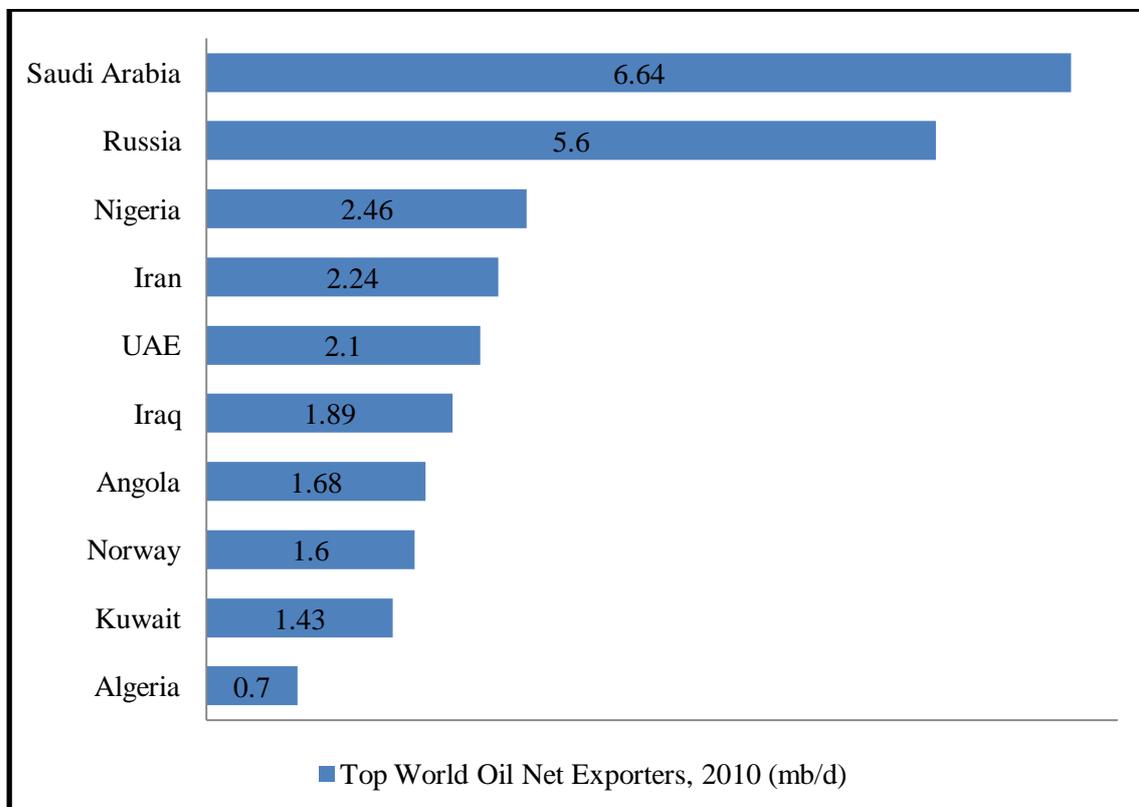
(a) One ton = 7.33 barrel

(b) All percentages were calculated by the author

China recognises the implications of Saudi dominance of the world energy markets, and has responded by increasing its economic, diplomatic, and cultural ties with the

Kingdom. China also needed to develop domestic capacity to process the cheaper higher-sulphur crudes of greater international availability. Acknowledging that its domestic oil industry is no longer capable of self-sufficiency, China has moved to modernise its refineries, expand domestic production of oil products, increase quality, and integrate its oil sector more extensively with the international industry, (Yamaguchi & others, 2002). According to David Kirsch, Director of Market Intelligence at PFC Energy in Washington, “No single producer is really going to challenge the Saudi position in China in the long run...China is a key market and Saudi doesn’t want to lose market share there. It doesn’t want to lose out to Russia and Iran. And that is part of why they will continue to push for long-term refinery deals in China”, (Webb, 2010).

(Figure 8.2.1): Saudi Arabia the World’s Top Oil Exporter (2010)



Source: OPEC Annual Statistical Bulletin 2010/2011

Saudi Arabia in its part recognises that energy demand is shifting from the developed world to the developing world, and China (Asia) is expected to account for much of the growing demand during the next 20 years, (Dittrick, 2010). Asia accounted for around two thirds of Saudi crude exports in 2010 and Saudi Arabia is the top crude oil supplier to China, the world's second-largest oil consumer, (Shamseddine, 2011). The growing importance of China and the wider Asian region to Saudi ARAMCO's and to the petroleum industry as a whole became evident when the company Board of Directors met abroad in May 2010 in Shanghai for the first time in its history, (ARAMCO, May 12, 2010). Indeed, Saudi Arabia's primary target is Asia. China is the lynchpin of Saudi strategy and it has put considerable effort into building a strategic relationship, (Lidstone, 2009). With one of the world's most developed energy sectors in terms of infrastructure and operating efficiency, Saudi Arabia is not desperate to attract foreign investment to help expand its capacity to produce and export oil. Instead, Saudi Arabia is keen on identifying a stream of steady, long-term demand, an urgent priority as the United States and other western countries look to decrease their consumption of oil and incrementally adopt conservation methods and alternative fuels, (Alterman & Garver 2008: 58).

While exports to the United States rebounded in 2010, in the long run the decline in American demand and the growing importance of China represent a fundamental shift in the geopolitics of oil, (Mouawad, 2010). ARAMCO's President Khalid AL-Falih agrees with that assessment: "We believe this is a long-term transition...Demographic and economic trends are making it clear — the writing is on the wall. China is the growth market for petroleum", (Ibid). Some international organisations also argue that China's oil consumption is projected to increase to 1.7 (mb/d) by 2015 and 7

(mb/d) day by 2030. China's and Asia's demand are projected to be met mainly from supplies from Saudi Arabia and the other Arab Gulf states, (Al-Naimi, 2009). Saudi Arabia's position as OPEC's top oil producer and holder of a fifth of the world's oil reserves also gives it the advantage over other producers when competing for new markets, (Reuters, February 19, 2010) (see Tables 8.2.4 below).

(Table 8.2.4): World Oil Demand Outlook in the Reference Case (mb/d)

	2010	2015	2020	2025	2030	2035
North America	23.9	24.1	23.8	23.4	22.9	22.3
Western Europe	14.5	14.2	14.0	13.7	13.3	12.9
OECD Pacific	7.8	7.7	7.4	7.2	6.9	6.7
OECD	46.1	46.0	45.2	44.2	43.1	41.9
Latin America	5.2	5.7	6.0	6.3	6.6	6.8
Middle East And Africa	3.4	3.7	4.0	4.4	4.7	5.1
South Asia	4.0	4.8	5.8	6.8	8.0	9.2
Southeast Asia	6.2	6.8	7.6	8.4	9.1	9.9
China	8.9	11.6	13.8	15.6	17.1	18.4
OPEC	8.1	9.2	9.9	10.7	11.6	12.5
Russia	3.1	3.3	3.3	3.4	3.4	3.4
World	86.8	92.9	97.8	102.0	105.8	109.7

Source: World Oil Outlook 2011

8.3 BILATERAL RELATIONSHIP: INTERDEPENDENCE AT WORK

Saudi ARAMCO's President and CEO Khalid A. Al-Falih argues that: "Some observers - particularly those outside of China and Saudi Arabia - superficially see our bilateral relationship with China as a one-way flow of oil from our company to this country, and view our ties exclusively through the narrow lens of energy supply security. Certainly that supply of petroleum is important, (Al-Falih, 2009). But viewed from the other side of the equation, security of supply can also be seen as

security of demand, and it is important to understand that we rely on China as a consumer as much as China looks to us as a producer. This dynamic of mutual dependence will only become stronger as Saudi ARAMCO continues to invest in multi-billion dollar infrastructure and development projects, and as its level of crude oil exports to China continues to rise in the decades ahead, (Ibid).

An early indication of that interdependence came after an oil cooperation agreement was signed in the late nineties, (Obaid, 2002: 30). Already, in 1998, China concluded a supply contract for 10 million tons of Saudi oil annually for a 50 year period, (Christie, 2010). Saudi ARAMCO also established a sales and marketing subsidiary office in Beijing in 1998, at a time when China's crude oil imports were small, (Wan, 2009). But China took a big step in 1999; Chinese President Jiang Zemin visited Saudi Arabia and signed an agreement with the Kingdom which in his words "inaugurated a strategic oil partnership." This agreement set forth two things: (a) Saudi Arabia would open its domestic oil and gas markets to China with the exception of upstream oil exploration and production; and (b) China agreed to open its downstream sector to Saudi ARAMCO.

The signed Memorandum of Understanding on Petroleum Cooperation between China and Saudi Arabia, (October 31, 1999), reveals energy dynamics of the new Sino-Saudi relationship: "Both sides agreed to facilitate investments in refining, petrochemical sectors and petroleum technical services cooperation in their respective countries", (Memorandum of Understanding on Petroleum Cooperation between the Government of the People's Republic of China and the Government of the Kingdom of Saudi Arabia). While this agreement was driven by mutual strategic benefits, it was

also catalysed by the need to resolve a major technical obstacle, (Lee & Dan, 2007). The growth in Chinese oil imports from Saudi Arabia has less to do with politics than with technicalities. Saudi oil tended to have too high a sulphur content for Chinese refining capability.

The Chinese Government has turned the impediment into advantage, though, as it gives Beijing an opportunity to engage the Saudis not only politically but also economically, (Jin, 2005: 3-10). Both countries also engaged in talks to allow Saudi ARAMCO to expand the capacity of Sinopec's existing oil refining facilities and other petrochemical complexes in China to handle Saudi oil, (Wan, 2010). In addition to its highly sought after premium grade light sweet crude reserves, Saudi Arabia is keen on securing a market for its medium grade crude oil in China, as well as other parts of Asia, (Chris, 2010:6).

Medium grade crude oil, while cheaper than its premium grade counterparts, is far denser and contains a higher amount of impurities and sulphur content compared to light sweet crude, meaning that it will yield less gasoline, diesel, and other finished products after what is a more complex refining process, (Ibid). In 2001 and after several years of negotiations, Saudi ARAMCO, ExxonMobil, and Fujian PetroChemical took another step toward the ultimate completion of a 240,000 b/d upgrade of a major Fujian refinery by signing an agreement for a Joint Feasibility Study (JFS), (Obaid, 2002: 31), coupled with a new, large ethylene production facility, (Calabrese, 1998: 351-366). Abdulaziz F. Al-Khayyal, Senior Vice President of Saudi ARAMCO, said at that time: "The signing of the JFS submission agreement marks a key milestone in the development of the Project and Saudi ARAMCO's

strategic partnership in China”, (Obaid, 2002: 31). Moreover, China agreed to allow the partners in this deal to open and manage 600-700 gas stations in the province. In return, China received a 30-year supply contract for 30,000 per day of Saudi crude oil, (Ghafouri, 2009: 80-92).

But the year of 2002 was a turning point, as since that year Saudi oil shipments to the U.S. have been declining while shipments have been increasing to China. Indeed, in 2002, Saudi Arabia became China’s leading source of oil imports, (Bajpae, 2006). However, large scale Sino-Saudi cooperation in the energy field kicked off only in 2003. As a result, Sinopec and Saudi ARAMCO began to collaborate on downstream projects in China, joining forces to build a refinery in Qingdao and to expand a petrochemical facility in Quanzhou, (Christie, 2010). China also needed to increase its domestic refining capacity to cope with the rise in imports from Saudi Arabia. To this end, Saudi ARAMCO, the U.S.’ ExxonMobil Corporation and state-owned China Petroleum & Chemical Corporation (Sinopec) signed an agreement in 2007 to expand the capacity of the Quanzhou refinery in Fujian province, in the southeast of the country, (Mirza, 2009).

In addition to purchasing energy from Saudi Arabia, China has expressed interest in entering into energy exploration contracts with Saudi Arabia. In March 2004, Sinopec signed a US\$300 million gas exploration licence for nearly 40,000 square km in a north-western block of the Rub al-Khali gas fields, an area that Saudi Arabia has opened up to foreign firms for the first time in 25 years, (Jiang, 2007). In April 2006, China was awarded the contract to explore and produce natural gas in the Rub al-Khali Basin in Saudi Arabia, (Fandy, 2005). Saudi ARAMCO also awarded three

contracts, worth a total US\$300m, to the CNPC-led BGP Arabia consortium in November 2009. The contracts were to gather seismic data on new gas reserves in the Rub al-Khali and Red Sea, and oil reserves at the Manifa field, (Lidstone, 2009).

Indeed, Saudi officials increasingly see the writing on the Great Wall: China will be their biggest oil market in the future, making it important to cultivate good relations with China. Ali Al-Naimi, the Minister of Petroleum of Saudi Arabia, argues that: “We view China as a strategic partner and seek to strengthen and enhance such partnership. Soon after assuming the throne, King Abdullah bin Abdulaziz underscored the importance of our relationship by making China the destination for his first state visit”, (Al-Naimi, 2009). The visit by Saudi King Abdullah bin Abdul Aziz to China in January 2006 demonstrated the deepening ties between the world’s fastest growing oil market and the world’s biggest oil supplier, (Pant, 2008). During the Saudi king’s visit, the two countries signed an agreement on oil, natural gas and mineral cooperation, in which Saudi Arabia promised to increase the annual oil and gas exports to China by 39 percent. As part of the agreement, a 100-million-ton crude oil storage facility was planned for construction in China’s Hainan province, (Tu, 2006).

In the aspect of oil trade, with the signature of the “Energy Cooperation Agreement” and “Complementary Protocol” in 2008 and 2009, China’s oil import from Saudi Arabia increased from 36.36 million tons in 2008 to 42.00 million tons in 2009, accounting for over 20 percent of the total volume of oil imported by China. Saudi Arabia has become one of the most important and stable overseas oil suppliers for China, (Yu, 2010). In addition, Saudi ARAMCO signed a memorandum of

understanding with China Petroleum and Chemical Corp., (Sinopec), under which, China would increase its imports from the Saudi producer up to 1 million barrels a day (50 million tonnes a year) by 2010, (Xinhua, November 13, 2009) and to 1.5 million barrels per day by 2015, (ARAMCO, June 23, 2008).

ARAMCO is also participating in oil processing and storage projects in Asia. These actions are to improve access to markets there amid the region's increasing consumption of fuel and crude. China may increase refining capacity by one-third to more than 12 million barrels a day by 2015 to feed economic growth, (EIA, November 2010). ARAMCO marked the completion of a project to expand refining capacity and integrate petrochemical production with an existing refinery in its first equity venture to China. Khalid Al-Falih Saudi, ARAMCO's President, told the audience at the Inauguration of the Fujian Refining & Ethylene Project, Quangan, Fujian Province, in China in November 2009 that: "I view today as a moment to celebrate Saudi ARAMCO's thriving relationship with the wider Chinese energy sector. Ten years ago, China imported relatively little crude oil from us; now, it is one of our top three markets, and is the fastest growing market for us globally. At this moment, we are providing nearly a million barrels of crude oil to China each and every day, accounting for a quarter of this country's total imports and a sizable portion of its overall energy requirements", (Al-Falih, 2009).

Saudi Arabia's ties to China are expanding beyond the crude oil trade and deepening in the area of refining operations. ARAMCO plans to ship 200,000 barrels per day (bpd) to Fujian after starting up in 2009. The Saudi company is also looking to invest in a second Chinese refinery, a 200,000 (bpd) plant in the eastern port of Qingdao,

(Reuters, February 19, 2010). Furthermore, China National Petroleum Corp, parent of Asia's largest oil and gas producer PetroChina, has signed an agreement with Saudi ARAMCO for further cooperation. The Memorandum of Understanding (MOU) was signed during a visit by CNPC's General Manager Jiang Jiemin to Saudi Arabia on December 18-21, 2010, (Hua & Miles, 2010). Additionally, Saudi ARAMCO Chief Executive Khalid al-Falih said in April 2011 that the company's daily refining capacity would soon grow 50 percent from its current level to more than 6 million barrels per day, (Al-Falih, 2011). That growth will be accomplished through two new refineries already under construction in Saudi Arabia and four more refineries are currently being considered, including one in the Kingdom along with joint venture refinery projects in China, Vietnam and Indonesia, (Ibid).

In this context China and Saudi Arabia announced within one week of March 2011 in two separate MOUs that they will build two refineries; one in Saudi Arabia and another in China. Firstly, China Petrochemical Corporation (Sinopec) signed a Memorandum of Understanding (MOU) on March 16, 2011 to jointly build a US\$10-billion Yanbu refinery on the Red Sea coast, a pact that further cements ties between the two energy giants, (ARAMCO, March 16, 2011). ARAMCO said it would hold a 62.5 percent stake in the Red Sea Refining Co. which was formed to develop the 400,000 barrels per day refinery in Yanbu, while Sinopec would own the remainder, (Ibid). The venture would be the first refining project the Chinese state oil major, parent of top Asian refiner Sinopec Corp, builds outside China. The Yanbu plan is expected to start operations in 2014 and accounts for just under a quarter of Saudi plans to add around 1.7 (mb/d) of refining capacity to the current 2.1 (m/b), (Ibid). China's National Development and Reform Commission (NDRC) has approved a

400,000 bbl/day refinery joint venture at Yanbu in Saudi Arabia between Sinopec and Saudi ARAMCO in June 2011, (Zhang, 2011).

Secondly, just four days later ARAMCO and Sinopec announced ARAMCO Overseas Company B.V., a subsidiary of Saudi ARAMCO, and PetroChina Company Limited, a subsidiary of CNPC, signed on March 17, 2011, a Memorandum of Understanding (MOU) related to the planned development of a 10 million metric tons per annum (200,000 barrels per day) grassroots full conversion refinery in Yunnan Province in the People's Republic of China. China National Petroleum Corp., the state-owned parent of PetroChina, said that the new refinery in Yunnan province will receive crude through a pipeline being built from the coast of Myanmar to China, (Said, 2011).

Meanwhile, in July 2009, Saudi Basic Industries Corporation (SABIC), the world's largest chemicals producer by market value, was also given approval by the Chinese regulator, the National Development & Reform Commission (NDRC), to help develop a US\$3bn petrochemicals complex at Tianjin (which became operational in 2010), in the northeast of the country, (Mirza, 2009). SABIC will take a 50 percent stake in the project, with state-owned Sinopec holding the remaining 50 percent. Once completed, the plant will produce about 3.2 million tonnes a year (t/y) of petrochemicals, including the basic plastics polyethylene and polypropylene.

According to SABIC CEO Mohamed Al-Mady: "China is the world's biggest petrochemical market and is growing... We want to invest in more than one project in China", (Reuters, January 20, 2010). SABIC is particularly interested in tapping into

the Chinese automotive, aircraft and construction sectors, (Ibid). Indeed (SABIC), announced in May 2011 that it is planning a US\$1 billion-plus facility in China with China Petroleum & Chemical Corp (Sinopec) to tap into the country's robust demand for plastics, (Leung, 2011). The project in the eastern port city of Tianjin would have an annual capacity of 260,000 tonnes of polycarbonate and is expected to be operational by 2015, (SABIC, May 17, 2011) (see Table 8.3.1 below).

(Table 8.3.1): Saudi Downstream Co-operation with Chinese Partners

Investors from Saudi Arabia	Chinese partners	Number of filling stations planned		Location
Saudi ARAMCO/ExxonMobil	Sinopec	750		Fujian(China)
Investors From Saudi Arabia	Chinese partners	Refinery Product Types and Crude Processing Capacity (Mt/y)		Location
Saudi ARAMCO/ExxonMobil	Sinopec	Crude oil: 12 Mt/y	Ethylene: 0.8 Polyethylene: 0.8	Quanzhou, Fujian (China)
Saudi SABIC	Sinopec	Ethylene: 1 Polyethylene: 0.6 Glycol: 0.4		Tianjin (China)
Saudi ARAMCO ^a	Sinopec	10 Mt/y		Yunnan (China)
Saudi ARAMCO ^b	Sinopec	20 Mt/y		Yanbu /Red Sea (Saudi Arabia)
Saudi SABIC ^c	Sinopec	260,000 Tonnes of Polycarbonate		Tianjin (China)

Source: IEA (February, 2011), ARAMCO (March, 2011) and SABIC (May, 2011)

- (a) & (b) Memorandum of Understanding (MOU) signed on March 2011 for both refineries
- (c) Memorandum of Understanding (MOU) signed on May 2011

8.4 OIL COOPERATION: DIVERSITY NOT DEPENDENCY

Despite these growing relations, China-Saudi relations have been restricted to oil exports to China and limited cross-investment. Chinese NOCs' activities in Saudi Arabia are very much limited to engineering services, such as pipeline and well repair, seismic data collection, and natural gas projects, which involve higher risks and capital input, (Hongtu, 2010). Saudi Arabia does not allow Chinese companies (or any foreign companies) to invest in its upstream (exploration and production) oil sector, but it has allowed them to invest in the upstream gas sector.

Saudi Arabia's tight restrictions on inward investment in the oil sector and the high degree of competence for Saudi ARAMCO are likely to limit the engagement of China's NOCs in the Kingdom, except in the gas sector, which to date has proved to be of little interest, (Andrews-Speed, 2009: 13-28). Likewise, the growth of Saudi ARAMCO's investments in China's refining industry will be constrained as long as China's domestic pricing policy for oil products is unfavourable to refiners, (Ibid). As Jon B. Alterman and John W. Carver describe in their book, "*The Vital Triangle: China, the United States and the Middle East*", the relationship between China and Saudi Arabia, is simple "uncomplicated by either country's sense of its global role or its global responsibility. Saudi Arabia has gas and oil; China needs gas and oil. On that basis, agreements were made between the China and Saudi Arabia", (Alterman & Garver, 2008: 1). Indeed the bulk of the trade between the two countries is of crude oil (see Table 8.4.1).

(Table 8.4.1): Share of Oil Products in China-Saudi Arabia Total Trade (2001-2010; US\$ in thousands)

	Total Trade between China & Saudi Arabia	China's Imports from Saudi Arabia	Saudi Arabia's Imports from China	Mineral Fuels, Oils, Distillation Products, etc	Share of Mineral Fuels, oils, Distillation Products (of All Products %)^a
2010	43,195,659	32,825,960	10,369,699	25,861,054	59.8%
2009	32,598,096	23,620,244	8,977,852	19,351,188	58.04%
2008	41,846,166	31,022,698	10,823,468	26,400,192	63.08%
2007	25,400,435	17,560,476	7,839,959	13,644,629	53.7%
2006	20,140,366	15,084,532	5,055,834	11,876,934	59%
2005	16,070,130	12,245,715	3,824,415	9,284,592	57.7%
2004	10,298,103	7,522,645	2,775,458	5,427,437	52.7%
2003	7,319,125	5,172,322	2,146,803	3,763,615	51.4%
2002	7,319,125	3,435,351	1,671,544	2,460,056	33.6%
2001	4,070,010	2,715,895	1,354,115	1,910,992	46.9%

Source: General Customs Administration of China and UNComtrade

(a) Percentage calculated by the author

While there is no denying that China and Saudi Arabia have extensive energy ties, it is clear that China is also attempting to limit its ties to Saudi Arabia. Despite Saudi Arabia having the largest proven oil reserve in the world, China has shown a desire to keep its oil sources diversified. China has made significant efforts to diversify its sources of oil, developing resources in Russia, Central Asia, Africa, Latin America and the Middle East. As Table 8.4.2 shows, in relation to oil sources, China has developed relations with many countries.

China is also wary about becoming too reliant on Saudi oil and has attempted to diversify its domestic oil refineries. For example three major oil refining projects in the southern Chinese province of Guangdong are set to begin operations in 2011. These projects include two joint venture plants, including one between China Petroleum & Chemical Corp (CPCC) or Sinopec and Kuwait Petroleum Corp (KPC).

Another is the deal between PetroChina Co and Petroleos de Venezuela SA (PDVSA), (Su, 2011). The third project is the expansion of an existing refinery run by China National Offshore Oil Corp (CNOOC), the parent of Cnooc Ltd. Additionally, in September 2010 Russian oil company OAO Rosneft agreed to build a 260,000-barrel-a-day refinery in Northern China in a joint venture with China National Petroleum Corp, (Hall, 2011). The three oil refineries with foreign joint venture when completed will increase crude oil processing capacity by about one (mb/d), (Ibid).

(Table 8.4.2): China's Oil Imports by Major Suppliers, 2001-2010, (US\$ Billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World	17,51	19,32	29,24	48,02	64,08	89,09	105,17	169,25	123,97	188,6
Saudi Arabia	1,91	2,46	3,76	5,42	9,28	11,87	13,64	26,40	19,35	25,8
Angola	0,721	1,08	2,20	4,71	6,57	10,93	12,87	22,35	14,61	22,7
Iran	2,16	2,07	2,96	3,98	6,06	9,02	11,64	16,79	10,56	13,07
Russia	0,008	1,28	2,09	4,18	6,554	9,46	9,35	11,94	9,38	12,7
Oman	1,59	1,44	1,97	4,27	4,10	6,08	6,59	11,24	5,00	9,09
Australia	0,279	0,488	0,785	1,13	1,11	1,39	1,70	1,72	6,43	8,03
South Korea	1,92	1,32	1,94	3,21	3,50	5,81	6,53	9,94	5,48	7,8
Indonesia	0,653	0,822	1,16	1,30	2,00	1,64	2,47	2,57	4,26	7,2
Sudan	0,009	1,15	1,43	1,65	2,57	1,87	4,14	6,29	4,64	6,5
Iraq	0,073	0,096	0	0,319	0,415	0,652	0,764	1,32	3,29	6,2
Kazakhstan	0,098	0,170	0,248	0,393	0,590	1,33	3,22	4,32	2,81	5,7
Kuwait	0,327	0,337	0,346	0,510	0,731	1,66	2,06	4,70	3,00	5,6
Venezuela	0,009	0,052	0,327	0,271	0,712	2,34	2,57	5,78	3,71	5,5
Singapore	0,780	1,01	1,54	2,29	2,20	2,50	1,84	4,32	2,90	4,6
Libya	0,052	0	0,028	0,381	0,941	1,69	1,52	2,55	3,15	4,4

Source: General Customs Administration of China, UNComtrade

With respect to China's efforts to build strategic oil reserves, it has used a variety of methods to fill its reserves in the first and the second phases. China's total strategic petroleum reserve capacity reached 24.38 million tonnes or 178 million barrels by the end of 2010, suggesting that 76 million barrels has been added to the project's second phase, (Bai, 2011). The filling of the first phase of 102 million barrels took 30 months

since the first batch of tanks were ready in October 2006. The prices for the crude oil stored in the first phase averaged at about US\$58 a barrel, (Ibid).

The Chinese do not seem to be placing much urgency on filling their oil reserves from Saudi Arabia for many reasons. Firstly, there is domestic and international concern as to the effects on oil prices should China decide to fill its strategic oil reserves at a rapid pace. Instead, China is taking a more patient approach by filling its strategic oil reserves gradually over many years. Secondly, China is unwilling to pay a high price for oil that will be used to fill its strategic oil reserves. Zhang Guobao, the Vice Minister of the Chinese State Development and Reform Commission, stated that: “It would be a great financial risk for China to buy oil at the international market for its strategic reserve program as the current global oil price has been fluctuating at a high level”, (Chen, 2006). China is content to wait until oil prices drop to what they consider an acceptable level prior to importing oil into their strategic oil reserves. In the meantime, China has filled its first strategic oil reserve using domestic oil instead of imported oil, (Ibid). China also may be looking to fill its strategic oil reserves with overseas oil assets which Chinese firms own stakes in, (Wang, 2006).

Despite this, Saudi Arabia agreed with Beijing in 2006 to build a crude oil storage facility on Hainan Island, which has been selected to become a site for its state and commercial oil reserves, nothing has been decided upon what role, if any, the Kingdom will play in the project, (Pachymuthu & Topham, 2010). On the contrary, Saudi Arabia’s Oil Minister Ali al-Naimi said in December 2009 that the Kingdom had accepted an offer to put “millions of barrels” of crude oil in commercial storage in Japan, (Ibid). Indeed, in February 2011, Saudi ARAMCO agreed to lease storage

tanks from Japan Oil, Gas and Metals National Corp (JOGMEC) for the storage of Arabian crude oil at Japan's Okinawa storage facilities, (ARAMCO, February 9, 2011).

This is the second agreement for storage that ARAMCO reached with Japan as the company seeks greater access to Asia, its largest export market. ARAMCO had already agreed in June 2009 with Japan's Agency for Natural Resources and Energy to store another 3.8 million barrels of oil, also on Okinawa, (Anthony, 2011). The additional storage capacity gives ARAMCO a bigger cushion against disruptions to supply through the Strait of Hormuz, (Ibid). The agreement allows for about 3.8 million barrels of Arabian crude oil to be stored at the storage facilities initially, with the option of expanding storage in the future.

Al Troner, President of Houston-based Asia Pacific Energy Consulting (APEC), argues that: "The Saudis want a break bulk point and this is another way for them to get into China... Japan will act as a springboard...smaller tankers can be used to move the oil to smaller refineries in China located on the coast", (Ibid). Meanwhile, David Kirsch, PFC Energy's Director of Market Intelligence Service, believes that: "The Saudis have storage in what they know is a key market, and they'd be able to get the oil to Japan or/and China in case of any disruptions" (Ibid).

As for Saudi Arabia, despite its aggressive policy towards China, it has also shown a desire to keep its energy sources diversified. Saudi ARAMCO is the single largest supplier of oil to China, India, Japan, the Republic of Korea, Taiwan, Singapore and Philippine, (ARAMCO, 2010:19). Geographical diversity is also a priority.

ARAMCO's energies have been increasingly directed outside the Kingdom in recent years, with more than a third of its refining capacity now based in other countries, (Lidstone, 2009). As well as the joint Chinese venture, the company is involved in four other refining and marketing ventures outside of the Kingdom: Motiva in the US; SsangYong Oil Refining in South Korea; Petron in the Philippines; and Motor Oil (Hellas) in Greece, (Ibid).

(Table 8.4.3): Main Markets for Saudi Crude oil (2001-2010, US\$ billions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Position in 2010
Japan	9,9	9,5	11,7	14,9	24,2	31,8	29,9	45,1	26,0	32,4	Top Supplier
U.S.	13,0	13,0	18,2	20,8	26,3	31,5	35,2	55,3	22,1	31,1	3rd Supplier
China	1,6	2,08	3,2	4,6	8,2	11,0	13,1	25,8	18,9	25,5	Top Supplier
South Korea	6,6	6,2	7,4	9,3	13,2	17,4	18,3	28,6	16,7	22,8	Top Supplier
India	0,17	0,19	0,29	0,48	0,71	9,7	15,1	21,1	13,0	17,0	Top Supplier
Taiwan (China)	1,9	1,6	3,3	4,2	6,0	8,08	8,3	12,2	7,1	9,05	Top Supplier
Singapore	3,8	3,5	3,5	5,0	8,3	8,6	8,0	13,6	7,2	8,9	Top Supplier
Thailand	1,1	0,999	1,4	1,9	3,5	3,7	3,9	6,4	3,4	4,8	2nd Supplier
Pakistan			1,1	1,6	2,1	2,5	3,3	5,0	2,8	2,9	2nd Supplier
South Africa	1,6	1,2	1,8	2,4	2,7	3,3	3,2	4,8	2,9	2,7	2nd Supplier
Philippine	0,87	0,99	1,2	1,3	2,2	2,9	3,5	5,04	1,5	2,4	Top Supplier

Source: UNComtrade, (July, 2011)

On the other hand there is no evidence to say that China is using advanced technology that is owned by Saudi ARAMCO to develop the production of energy within China. On the contrary, China is striving to get this technology from all over the world. Indeed, Chinese oil majors are set to accelerate their overseas buying spree in

unconventional oil and gas assets, with an eye on technology, the key to help shift China's reliance on coal to lower-carbon fuel over the next decade. Such technology will be critical for China to boost energy security and tap into its own potentially vast unconventional gas resources - part of the drive by the world's fastest-growing major economy to triple gas use - as Chinese firms lack the expertise, (Master, 2011).

In that regard foreign upstream mergers and acquisitions (M&A) activity by China's national oil companies (NOCs) reached a staggering US\$26bn in 2010 – up by 85 percent on 2009's US\$14bn almost none in Saudi Arabia. The 2010 figure represented 15 percent of global upstream deals, according to IHS Herold, a consultancy, (*Petroleum Economist*, February 2011). Fu Chengyu, General Manager of CNOOC, said recently that his company alone plans to spend as much as US\$151bn by 2015 to boost production, (Ibid). The latest trend is that they are giving priority to the technology of developing unconventional reserves, such as tight gas, coal bed methane (CBM), shale gas and oil sands, as well as deep-water drilling.

According to Peter Gastreich, Executive Director at UBS in Hong Kong: “In the case of China, I don't think they are purely interested in becoming operators for the sake of additional resources...What they are really interested in now is more on the technology side with the aim of applying this expertise to China”, (Master, 2011).

8.5 ENERGY IMPEDIMENTS & GEOPOLITICAL CONSTRAINTS

As discussed above, China-Saudi relations have been restricted to oil exports to China and limited cross-investment; additionally there have been several hurdles and obstacles that may have slowed the pace of economic relations between China and Saudi Arabia. Firstly, energy is a very sensitive sector to both countries. To penetrate the upstream sector in the Middle East, China is facing some legislative obstacles and contractual hardships in such countries as Saudi Arabia and Kuwait, where foreign investment in the oil upstream sector is not allowed, (Xu, 2002).

Secondly, as the competition in the Chinese market intensifies, it is likely that the Chinese government will face stronger lobbying pressures from domestic producers to protect their products against imports. China has been known as a frequent user of anti-dumping tariffs since its accession to the WTO in 2001, and the majority of them were applied to petrochemical imports, (Yamada, 2011:108).

Thirdly, the IEA has repeatedly said that China's oil demand forecasts aren't precise as Beijing doesn't publish figures on a key element which are needed to calculate this — the amount of oil it holds with regard to strategic and commercial reserves. (*Wall Street Journal*, February 10, 2011). China has held on to its oil inventories dearly, more than four years after the start of its first strategic crude reserve base in 2006, and is likely to guard them tighter as it accelerates building reserves. China treats stocks of other commodities from grain to metals as state secrets, (Chen, 2010). In a speech titled: "A Pillar of Global Stability: Saudi Arabia's Petroleum Policy", (November 2010) at James A. Baker III Institute for Public Policy, Saudi Prince Turki Al-Faisal called for countries like India and China to be transparent in reporting their energy

consumption as this would lead to a more efficient and stable global energy market. He went on to say, “We must work together to make sure that all nations have the resources and incentives to publish accurate and valuable information on their energy supplies and uses”, (AL-Faisal, November 11, 2010).

Fourthly, Amy Myers, an energy expert at Rice University’s James A Baker III Institute for Public Policy in Texas stated that China would likely improve the efficiency of its oil usage faster than experts had predicted, (Stanton, 2010). If China implemented the types of energy efficiency improvements that western countries introduced during the 1970s oil crises, Myers believes, China’s use of oil over the next two decades could be millions of barrels per day lower than originally forecast, (Ibid).

Finally, industry experts say that differences on shouldering the financial risk are complicating the joint ventures in modernising the refinery in Quanzhou (China) and building Yanbu’s new refinery (Saudi Arabia). In China, the government tightly regulates retail prices for petroleum products; Beijing reportedly does not want to share the financial risk with the Saudi side. In Saudi Arabia, the Chinese probably want assurances with regards to managing the risk properly, (Baxter, 2011). Finally, in every case, China is facing intensive competition in the Middle East when it bids for major projects. Chinese companies are at a disadvantage in competition for large projects, (Xu, 2002). One reason that Chinese companies like Sinopec have made little progress in getting more acreage in Saudi Arabia is because they lack the technical expertise the Kingdom requires. Saudi Arabia’s oil fields are vast but many

of them are ageing, and it likely needs to find new ways to keep pumping oil from mature fields at high volumes, (Winning, 2009).

Some of these obstacles gradually could be removed through regular contacts and visits by Saudi and Chinese investors. Indeed, the Council of Saudi Chambers called on investors in China for the need to increase their investments in Saudi Arabia via eight suggestions made by Saudi businessmen to their Chinese counterparts, at the meeting held in Riyadh, the Saudi capital, in October, 2010, (Council of Saudi Chambers, 2010).

A number of Saudi businessmen, from the Saudi-Chinese Business Council, presented suggestions to strengthen trade between the two countries which included: (a) Urging Chinese companies within the Kingdom to cooperate with Saudi contracting companies in the implementation of projects assigned to it; (b) Supporting joint projects in promising industrial areas such as in the field of petrochemicals; (c) Establishing a direct air route between the two countries to facilitate the transportation of passengers and goods; (d) Reducing travel costs for small and medium-sized company sectors, (e) Establishing a factory for spare machine parts and equipment specifically for the manufacture of cement, (f) Urging the Chinese Government to encourage Chinese companies to make the Kingdom the regional hub for its businesses; (g) Discussing the establishment of a specialised institute to serve the cement industry and to provide personnel to operate it; and (h) Setting up a joint company in Saudi Arabia in which the majority would be Chinese employees, (Ibid).

Of course it's not just only economic in geopolitical terms there are also several factors which could also affect the Sino-Saudi relations: (1) Inside the Chinese Government there is no agreement among the policy makers to determine to what extent should China get involved in the Middle East; (2) A severe economic downturn in China leads to a decline in crude oil consumption and subsequently decreases the volume of imports of oil from Saudi Arabia or/and the Middle East. Although this scenario is unlikely, it is still a risk or as the *Economist Intelligence Unit* puts it: "The risks associated with a downturn would be great both within China and abroad. Internationally, the main impact would likely be on commodity markets. Chinese demand, and assumptions that it will continue to rise rapidly, underpin current prices for oil, metals and a number of other commodities. If China's GDP slowed, commodity exporters, especially those in the developing world, would be badly affected", (Economist Intelligence Unit, June 16, 2011); (3) Middle Eastern issues have been intertwined with many complex interests, many of which have to be looked into individually; and (4) Climate change could be a factor which could force China to rationalise its energy structure. It may consequently affect China's demand for oil imports from Saudi Arabia in the long term, (Zhang, 2009). Finally, Ben Simpfendorfer offers a cautionary note:

Given China's economic importance to the Gulf, the country's efforts to rebalance its economic model and control its inflation problems are crucial to the rest of the region. In effect, the country is attempting to reverse its growth model of the last 30 years: rather than rely on exports from wealthy coastal provinces to developed countries, China will increasingly rely on consumption by its poorer interior provinces. Clearly, the rise of China's interior provinces can have a significant impact on the country's consumption of consumer goods, housing and, importantly, oil. For sure, the interior provinces might be relatively poorer, but they are huge in size. They have a combined GDP of \$2,900bn and population of 790m, figures that are significantly larger than the Gulf's combined GDP of \$1,450bn and population of 170m, (Simpfendorfer, 2011).

(Table 8.5.1): Geopolitical Factors that could Constrain/Delay Energy Investment between China and Saudi Arabia

	Description	Impacts	Countries potentially demonstrating risk
Depletion policies	Policies to preserve resources over time. Choice to deplete resources more slowly in order to provide a wealth fund for future generations or simply through belief that in a context of rising prices, resources are worth more left in the ground for extraction in the future.	Less willingness to supply export market; higher prices.	Saudi Arabia; Kuwait; Mexico; Venezuela; Qatar.
Resource nationalism	Lack of access to reserves for IOCs and/or risk of appropriation.	Reliance on NOCs often less technologically advanced leads to inefficient exploitation of resources; less supply to global market.	Reserves inaccessible to IOCs: Saudi Arabia; Iran; Iraq; Kuwait; Mexico. Access restricted: UAE; Venezuela; Russia; Libya; Nigeria; Kazakhstan; Qatar; Algeria, Libya.
Political instability and terrorism	Military conflict or terrorist activity or popular revolt	Acts as a deterrent to foreign investment and/or makes operations difficult.	Nigeria; Algeria; Libya; Iraq; Iran; Saudi Arabia. The civil war in Yemen and its possible spill over into Saudi Arabia.
Transit risks	A dispute among supplier and transit nations prevents supplier's consumer obligations from being met. Transit routes in potential conflict zones.	Supply shortages through political interference or physical infrastructure damage.	Russia; Ukraine; Turkey; Georgia; Straits of Hormuz; Gulf of Aden; Malacca Straits; Suez Canal.

Source: adapted from the UK Department of Energy and Climate Change (DECC)

8.6 CONCLUSION

This chapter has shown that Chinese intentions are better placed within the lines of the economic interdependence school of thought rather than the realism model. China views Saudi Arabia not only as a long-term energy source but also as an opportunity to further expand economically - not as a state that it wishes to wrestle away from

U.S. power and influence. With respect to the Sino-Saudi energy relationship, China is primarily concerned with three issues: (a) Securing Saudi Arabian energy sources in order to continue its economic growth over the long term; (b) Maintaining Saudi Arabia's continued role in providing diversification in Chinese energy sources; and (c) Taking advantage of various energy investment opportunities in Saudi Arabia. These three goals are all economic in nature and are not intended to undermine U.S. influence in the region.

If China was acting in the realism model, it should be taking advantage of every opportunity to use its economic resources, even if its policies do not make economic sense, towards a political agenda of developing closer Sino-Saudi ties in a manner which decreases U.S. power and influence in Saudi Arabia. On the contrary, Chinese economic policies toward Saudi Arabia make economic sense and are not political in nature with respect to the international balance of power. China has not arbitrarily invested in Saudi Arabia with the sole purpose to develop closer Sino-Saudi ties. It has also shown an unwillingness to become overly reliant on Saudi oil or drawn to projects with financial risks. These actions are not consistent with a state that is aggressively pursuing to expand its power and influence in a region at the cost of the United States.

As for future trade expectations, great potential exists for Sino-Saudi relations to expand substantially in the future. There is no doubt that the economic relations between China and Saudi Arabia will thrive, especially with the increase of China's dependence on oil from the Middle East and with China becoming the biggest market for Saudi oil in the coming years.

CHAPTER NINE

CHINA-SAUDI MILITARY COOPERATION

9.1 INTRODUCTION

China's arms sales to the Middle East range from small arms and ammunition to transfers of some advanced weapons systems. During the 1960s and early 1970s, China was particularly active in supplying revolutionary governments and movements, especially in Asia and Africa. However, from the mid-1970s, China diversified its recipients to include Israel and Saudi Arabia (neither had diplomatic relations with China at the time), Chile, Iran, Iraq, Myanmar, Oman, Sri Lanka, Syria and Thailand, (Medeiros & Gill, 2000). China was an important arms supplier to certain developing nations during the 1980s, through arms agreements with both sides during the Iran-Iraq war, (Grimmett, 2005). However, over the past thirty years, arms sales have generally declined in importance to China as a tool of influence, particularly as China's weapons systems became less competitive compared to the more sophisticated systems available from Western or Russian sources, (Office of the U.S. Secretary of Defence, 2010).

The China-Saudi military cooperation was recently highlighted by an unprecedented visit (the first ever) by the People's Liberation Army Navy (PLAN) at Jeddah Port in Saudi Arabia on November 27, 2010. While the exact purpose of the Jeddah port visit is uncertain, the motive behind the visit appears to be strategic, (Hsiao, 2010 December). This chapter will examine the military affairs and technology transfers that China and Saudi Arabia have formed over the past three decades. The variety and

amount of Sino-Saudi arms sales will be examined. The case study attempts to decipher Chinese intentions towards Saudi Arabia.

If China is acting in the offensive realism model, it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. hegemony by: (a) Selling Saudi Arabia sophisticated weapons and providing security assurances to make Saudi Arabia less dependent on the United States and more so on China; (b) Interacting militarily with Saudi Arabia regardless to the International Treaty on the Non-proliferation of Nuclear Weapons (NPT)¹⁵; and. (c) Providing Saudi Arabia with the technology and expertise to make it less dependent on the U.S.

If China is acting in the economic interdependence theory, it should be: (a) Interacting militarily with Saudi Arabia in a economically profitable manner and not providing Saudi Arabia with massive amounts of advanced military hardware in order to make Saudi Arabia less reliant on the U.S. security assurances and arms sales; (b) interacting militarily with Saudi Arabia according to the International Treaty on the Non-proliferation of Nuclear Weapons (NPT); and (c) Ensuring that the cooperation between China and Saudi Arabia regarding technology and science is conducted in a manner to advance the economic relations between the two countries. As for future trade expectations, as the quality of Chinese weapons systems improves in the long run, the trend of western and Russian monopoly over the arms trade may reverse.

¹⁵ The Treaty on the Non-Proliferation of Nuclear Weapons, also Nuclear Non-Proliferation Treaty (NPT or NNPT) is a treaty to limit the spread (proliferation) of nuclear weapons. The treaty came into force on 5 March 1970, and currently there are over 190 states party to the treaty.

9.2 CHINA AND THE ARMS MARKET

China's diplomacy in the Middle East started to take advantage of the situation during the Iraq-Iran war between 1980 and 1988 to use its arms trade within the region, (Zhu, 2009). China became an important supplier of less expensive weaponry during that war in the 1980s. During that conflict China demonstrated that it was willing to provide arms to both combatants in quantity and without conditions, (Grimmett, 2010). China also supplied long range missiles to several other countries in the region, including Saudi Arabia, in addition to "Silkworm" anti-ship missiles to Iran. "Between" 1980 and 1990, China sold US\$2.6 billion in conventional arms to Iraq alone, making it the world's fourth largest weapons supplier to the Third World - largely as the result of arms transfers to the Middle East. During the peak years (1986-90) of its sales to its three primary Gulf customers (i.e., Iran, Iraq, Saudi Arabia), China earned an estimated US\$3.9 billion, (Calabrese, 1992).

By the mid-1990s, the Middle East was Beijing's largest and most lucrative weapons export market, accounting for over 50 percent of China's deliveries, (Medeiros & Gill, 2000). From 1992 through to 1999, the value of China's arms transfer agreements with developing nations averaged US\$860 million annually, (Grimmett, 2000). China's principal recipient in the Middle East was Iran, while substantially smaller amounts went to Israel (US\$100 million), Libya (US\$100 million), Saudi Arabia (US\$800 million), and Iraq (US\$200 million) , (Medeiros & Gill, 2000). Over the 1990s, China's customer base contracted significantly and shifted from the Middle East to Asia. Chinese arms exporters recruited a few new buyers for conventional weapons, relying mainly on modest transfers to traditional clients like Iran, Pakistan,

Myanmar (Burma), Sri Lanka, and a few African countries, (Ibid). China sells primarily to developing countries, where Beijing's low cost weapons are able to achieve market access, (Office of the U.S. Secretary of Defence, 2010). A significant portion of China's totals can be attributed to a significant contract with Pakistan, a key client, associated with the production of the J-17 fighter aircraft, (Ibid).

During the 2000s Pakistan continues to be a key Chinese client attributable to the sale of frigates and jet aircraft to Pakistan, a client of long standing, (Grimmett, 2002). From 2003-2006, the value of China's arms transfer agreements with developing nations averaged about US\$1.5 million annually, a figure inflated by very large agreements with Pakistan in 2005, (Grimmett, September 2011). From 2007-2010, the value of China's arms transfer agreements with developing nations averaged over US\$1.9 billion annually, (Ibid). In that period (2007-2010), China sold approximately US\$8 billion worth of conventional weapons systems worldwide. China's arms agreement total in 2010 (US\$900 million) was its lowest total since 2003. Meanwhile Saudi Arabia has received almost nothing from China's military arms sales during the 2000s. (See Tables 9.2.1)

(Table 9.2.1): Saudi Arabia's Arms Transfers Supplier 1995-2010

New Arms Deliveries by Supplier, ((In Current Million US\$; 0 = Less than US\$ 50 million)					
	1995-1998	1999-2002	2003-2006	2007-2010	1995-2010
US	2,800	4,900	4,200	13,800	25,700
Russia	0	0	0	0	0
China	0	0	800	100	900
Major W. European	300	1,500	10,000	13,800	25,600
All Other European	1000	200	300	1,100	2,600
All Others	0	0	100	100	200
Total	4,100	6,600	15,400	28,900	55,000

Source: Adapted from Grimmett, various editions

The total value of all arms transfer agreements with developing nations from 2003-2010 was US\$284.6 billion (in current dollars). Saudi Arabia alone accounted for 15.5 percent of all developing-world arms-transfer agreements during these eight years, (Grimmett, 2011). Nearly 50 percent of foreign military sales signed between 2006 and 2009 were with Middle Eastern countries. During that time, Saudi Arabia purchased about US\$ 13 billion worth of American weapons, (Kimes, 2011). According to data published by Stockholm International Peace Research Institute (SIPRI), the Middle East spent US\$111 billion on military expenditure in 2010, an increase of 2.5 per cent over 2009. The largest absolute rise in the region was by Saudi Arabia, (SIPRI, April 2011).

Indeed, Saudi defence procurement spending for 2010 is estimated at US\$ 19 billion, (Entous, 2011). A new industry analysis also concludes that military procurement by Middle Eastern states, primarily Saudi Arabia, the United Arab Emirates, Iraq and Israel, is expected to grow by 14 percent over the next five years, (UPI, January 2011). Middle Eastern states are expected to spend US\$123 billion on arms in that period. U.S. arms sales will account for most of all this, (UPI, February 2011). Most recently, Saudi Arabia has been the principal arms purchaser in the Middle East region. In the period from 2007-2010, Saudi Arabia's total arms agreements were valued at US\$28.9 billion (in current dollars), (Grimmett, September 2011). Saudi Arabia was the leading developing world arms purchaser from 2003-2010, making arms transfer agreements totalling US\$44.3 billion during these years (in current dollars), (Ibid).

Furthermore, according to SIPRI, the five biggest suppliers of major conventional weapons in 2006–10 were the United States, Russia, Germany, France and the United Kingdom (see figure 2 and table 1). The USA and Russia remained by far the largest exporters, accounting for 30 per cent and 23 per cent of all exports, respectively, (SIPRI, March 2011). The top five suppliers accounted for 75 per cent of all exports of major conventional weapons in 2006–10, compared with 80 per cent in 2001–2005, (Ibid). Indeed most Chinese weapons for export are less advanced and sophisticated than weaponry available from western suppliers or Russia. China was not a major supplier of arms during the last four decades and consequently, does not appear likely to be a key supplier of major conventional weapons in the world conventional arms market in the immediate future. On the contrary, China was a major arms recipient particularly from Russia, (See Figure 9.2.1 and Tables 9.2.3).

(Table 9.2.2): The Five Largest Suppliers of Conventional Weapons, 1995–2010

Supplier	Share of Global Arms Exports (%) (2006-2010)	Main Recipient (share of suppliers transfers, 2006-2010)	Share of Global Arms Exports (%) (2005-2009)	Share of Global Arms Exports (%) (2000-2004)	Share of Global Arms Exports (%) (1995-1999)
USA	30	South Korea (14%) Australia (9%) UAE (8%)	30	31	48
Russia	23	India (33%) China (23%) Algeria (13%)	23	32	13
Germany	11	Greece (15%)	11	6	5
France	7	Singapore (23%)	8	8	11
UK	4	USA (23%)	4	5	7

Source: SIPRI Yearbook various issues and SIPRI Fact Sheet (March 2011)

9.2.1 US-Saudi Security Dimension

In this context, Sino-Saudi military cooperation has been progressing slowly, because of Saudi Arabia's special security relations with America. Saudi Arabia is an important partner with whom the U.S. have an over seven-decade-long history of close political-military relations.¹⁶ Dating back to the Cold War, the United States has viewed the security of Saudi Arabia as part of its national interests. The United States followed through with its promise to protect the Saudi Kingdom in 1979 during the Iranian revolution, and in 1990 when Iraq invaded Kuwait; the United States sent its military to the region to protect the Saudi Kingdom and also to force Saddam Hussein to retreat from Kuwait. Furthermore, a U.S.-Saudi military partnership was demonstrated in the basing of U.S. fighters and surface-to-air missiles in Saudi Arabia between 1992 and 2003, which played a critical role in enforcing sanctions in Iraq. It also was demonstrated during the U.S. invasion of Iraq in 2003, (Cordesman, November 2010).

Despite the relations between Washington and Riyadh being badly damaged by the 9/11 attacks and post U.S. invasion of Iraq (as discussed in earlier chapters), common strategic interests and pressures generated by the arms industry and the recession helped smooth differences, (Black, 2010). The U.S.-Saudi military relationship is longstanding and a centrepiece of the U.S.-Saudi political relationship. Furthermore, Washington-based Center for Strategic and International Studies (CSIS) expert Anthony Cordesman argues that: "The U.S.-Saudi security cooperation is becoming

¹⁶ On February 14, 2011 the two countries marked the 66th anniversary of the historic meeting between H.M King Abdul Aziz Al-Saud and President Franklin D. Roosevelt aboard the U.S.S. Quincy in Egypt's Great Bitter Lake. Many of the issues discussed that day in 1945, such as U.S.-Saudi military cooperation and the Kingdom's prospects for economic development, still hold relevance today.

steadily more important as Iran expands its capabilities for asymmetric warfare in the Gulf, increases its long-range missile forces, and moves toward a capability to build and deploy nuclear weapons. The same is true of the enduring threat from terrorism, dealing with Iraq's weakness and uncertain political leadership, the problems of Yemen, and instability and piracy in the Red Sea area and Indian Ocean", (Cordesman, September 2010).

Additionally, the then-U.S. Secretary of Defense Robert Gates and U.S. Secretary of State Hillary Clinton wrote to Congress on November 12, 2010 to argue that: "Saudi cooperation on counterterrorism issues is significant, and U.S. law enforcement and intelligence agencies continue to benefit from this relationship. Saudi Arabia played an integral role in helping the U.S. thwart the cargo package bomb plots of late (October 2010) emanating from Yemen, and we have publicly thanked the Saudis for this critical information sharing. The Saudi Government has also taken numerous regulatory and institutional steps to counter terrorist financing. Moreover, Saudi Arabia has been very involved in addressing regional Gulf security issues", (Gates and Clinton letter, 2010).

The U.S.-Saudi defence relationship has been also a major outlet for American arms sales and defence supplies. Saudi Arabia is the biggest military spender in the Gulf. The U.S. Defence Security Cooperation Agency (DSCA) has documented the history of arms sales to Saudi Arabia, (DSCA, 2011). From 1950 through to 2010, Saudi Arabia has purchased and received from the United States weapons, military equipment, and related services through Foreign Military Sales (FMS) worth over US\$69.32 billion, (Ibid) and Foreign Military Construction Services (FMCS) worth

over \$17.32 billion (figures in historical dollars), (Ibid). These figures represent approximately 18.7 percent of all U.S. FMS deliveries and about 83 percent of all FMCS deliveries made worldwide during this period, (Ibid). The largest single recent U.S. foreign military sale to Saudi Arabia between 1950-2010 was a US\$9 billion contract for 72 F-15S fighter aircraft, (Christopher, 2011) (see Table 9.2.1.3).

(Table 9.2.1.1): U.S. Arms Sales to Saudi Military, 1950-2010^a

Selected Indicators (US\$ thousands)						
	Total Sales Agreements	Total Sales Deliveries	FMS Agreement	FMS Deliveries	FMCS Agreement	FMCS Deliveries
2010	2,490,284	1,679,545	2,081,074	1,587,402	409,210	92,143
2009	3,295,751	1,750,010	2,862,225	1,715,752	433,526	34,259
2008	6,306,101	911,285	6,264,101	894,733	42,000	16,553
2007	1,712,830	1,051,156	1,657,662	1,013,788	55,168	37,367
2006	805,944	1,031,807	805,944	977,675	-	54,132
2005	735,833	1,012,974	735,833	981,232	-	31,743
2004	1,843,465	1,243,168	1,790,332	1,223,121	53,133	20,047
2003	676,670	1,064,279	649,618	1,007,629	27,052	56,649
2002	861,321	1,356,298	861,321	1,265,441	-	90,857
2001	665,373	1,990,567	665,373	1,875,852	-	114,715
2000	687,839	2,045,418	638,472	1,967,593	49,367	77,825
1999	828,360	4,443,098	781,362	4,354,650	46,999	88,449
1998	2,257,598	4,631,704	1,987,710	4,283,205	269,887	348,499
1997	521,538	4,476,122	521,538	4,439,368	-	36,754
1996	1,129,523	3,517,945	1,115,523	3,468,894	14,000	49,051
1995	434,406	4,044,856	434,406	3,936,895	-	107,961
1994	1,501,315	2,589,828	1,495,464	2,498,537	5,851	91,291
1993	10,616,039	3,481,117	10,488,331	3,359,984	127,708	121,134
1992	875,107	2,564,120	871,107	2,347,794	4,000	216,326
1991	9,055,096	3,013,918	8,700,365	2,740,530	354,732	273,388
1990	6,941,955	1,137,016	6,385,290	873,923	556,665	263,093
1989	1,096,440	963,332	1,096,440	616,731	-	346,602
1988	1,575,809	1,297,228	1,557,141	937,582	18,668	359,646
1987	627,903	3,072,918	627,903	2,830,371	-	242,546
1986	633,348	2,742,906	627,348	2,195,879	6,000	547,027
1985	3,178,392	2,255,847	2,261,522	1,354,731	916,871	901,117
1984	2,873,404	3,570,374	2,511,735	2,099,562	361,668	1,470,812
1983	732,615	5,804,087	716,211	3,650,917	16,404	2,153,170
1982	3,877,359	3,849,632	3,813,819	2,074,036	63,540	1,775,596
1981	1,841,171	2,839,176	963,771	1,347,579	877,400	1,491,597
1980	4,193,512	2,577,816	2,554,409	1,119,901	1,639,103	1,457,916
1979	5,974,209	2,440,508	5,118,847	940,394	855,361	1,500,114
U.S. Total 1950-2010	506,661,716	396,998,826	482,971,575	375,987,528	23,690,141	21,011,299
U.S. Saudi Arabia 1950-2010	100,031,371	86,653,175	81,568,397	69,326,609	18,462,974	17,326,567
Saudi Share of Total (%)^b	%19.7	%21.8	%16.8	%18.4	%77.9	%82.4

Source: adapted DSCA Historical Facts-book and Fiscal Year Series as of September 30, 2010, (October 2011)

(a) U.S. fiscal year begins on October 1 and ends on September 30

(b) Percentages were calculated by the author

In addition, record oil revenues have allowed the Saudi Government to boost public spending on numerous security projects, including addressing concerns over terrorism, criminal cross-border activities, and national defence/internal security coordination. The Kingdom forecasts to procure SR53 billion (US\$14 billion) worth of security systems and services over the next six years, (Wahab, March 2011). Saudi Arabia also increased its military expenditure by 2.7 percent in real terms, or 33 percent of its total national budget, (SIPRI Yearbook 2010). Indeed, the Saudi defence budget swelled from US\$24.9 billion in 2001 to US\$41.3 billion in 2009, a 65 percent increase, (UPI, February 2011), to reach almost 45 billion in 2010 (see Table 9.2.1.2 below).

(Table. 9.2.1.2): Saudi Arabia’s Military Expenditure, (2001–2010 in US\$ bn^a)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Expenditure	25,1	21,9	22,1	24,6	29,6	33,8	38,9	38,2	39 ,2	45,2
(%) of GDP	11.5%	9.8%	8.7%	8.4%	8.0%	8.3%	9.2%	8.2%	9.4%	10.4
(a) The figures for Saudi Arabia are for expenditure on defence and security.										

Source: SIPRI Yearbook 2010 and 2011

This is resulting in tremendous market opportunities for U.S. defence and security companies. Saudi Arabia maintains one of the world’s fastest growing markets for safety and security solutions, equipment, and systems. In that regard, according to a report revealed by the *Washington Post* published on January, 2010, the Obama Administration was quietly working with Saudi Arabia to speed up arms sales and rapidly upgrade defences for oil terminals and other key infrastructure in a bid to thwart future military attacks from Iran, (Warrick, 2010). The expanded cooperation includes new U.S. agreements with Saudi Arabia to help establish a facilities-protection force under the country’s Interior Ministry to harden defences for oil

facilities, ports and water desalination plants, (Ibid). The new force will be used to deter attacks by Al-Qaeda, as well as possible strikes by Iran or Iranian-inspired extremist groups, (Ibid). The new force is expected to grow to at least 35,000 members, trained and equipped by U.S. personnel and overseen by U.S. Central Command, (Burns, 2011).

Most important of all, President Obama notified Congress on October 20, 2010, of the largest arms sales in American history to Saudi Arabia, including the proposed sale of fighter aircrafts, attack and utility helicopters, upgrades of existing Saudi fighter aircrafts, and related weaponry and services. If all options are exercised, the proposed sales may be worth over US\$60 billion dollars over a period of ten to fifteen years, (Congressional Research Service R41556, 2011). The proposed sales include 84 new F-15SA fighter aircrafts, the upgrade of 70 F-15S fighter aircrafts, 70 new AH-64D Block III APACHE helicopters, and dozens of UH-60M BLACKHAWK and other helicopters. The Obama Administration hopes the proposed sales will help “sustain long-term relationships to ensure continued U.S. influence for decades”, (Ibid), or as the *Economist* put it:

“...the package of sales would not only tilt the balance of conventional weaponry in the Gulf decisively against Iran, whose suspected bid to acquire atomic bombs frightens its Gulf neighbours as well as Israel and the West. It would signal the return to normal of America’s tight, 70 year-long alliance with Saudi Arabia. This had frayed following the revelation that 15 of the 19 hijackers who attacked American cities on September 11, 2001 were Saudi nationals. Fearing congressional opposition, Saudi Arabia had in recent years sought weaponry from other sources”, (The *Economist*, September 15, 2010).

The deal is unique and very significant for several reasons: (a) A package of U.S. arms worth more than US\$60 billion for Saudi Arabia accounts for the largest single component of this military build-up; (b) The package provides a huge boost to the American defence industry, (Khalaf & Drummond, 2010); (c) The deal will prevent Saudi Arabia from pursuing other means (nuclear) of strengthening its security and

will lock Riyadh and Washington into a close military relationship for another two decades; (d) Arms purchases from the U.S. are central to Saudi Arabia's strategy of asserting its military leadership in the Gulf and confronting Iranian influence; and (h) Totally offensive in nature, the package, with its attack planes, helicopters, and "bunker-buster" bombs, is clearly designed to deter Iran, (Teitelbaum, 2010).

In addition, supporters of the arms deal argue that there are other strategic aspects to the deal: (1) U.S. arms sales to Saudi Arabia help sustain American influence in Riyadh; (2) From a U.S. viewpoint, these arms transfers are part of a new post-Iraq War security structure that can secure the flow of energy exports to the global economy, (Cordesman, September 2010). Stepping up - or "burden sharing", as military types like to call it - is the theory that arming allies with U.S. weapons will lighten the load for U.S. troops, (Kimes, 2011). Alexander Vershbow, the Assistant Secretary of Defence for International Security Affairs, argues that: "This is not solely about Iran...It's about helping the Saudis with their legitimate security needs ... they live in a dangerous neighbourhood and we are helping them preserve and protect their security...so it means we may have to station fewer forces on a continuing basis in the region", (Reuters, October 20, 2010); and (3) Others say arms sales are just one part of a complex dance the U.S. engages in with allies. Lawrence Korb, a senior fellow at the Center for American Progress and former assistant to the U.S. Secretary of Defence, points out that when the U.S. sells conventional arms to Saudi Arabia, for example, it deters the country from pursuing nuclear options, (Kimes, 2011).

Since the September 11 attacks, Washington and Riyadh have each been hesitant to press the issue of major arms sales, fearing that congressional debate might prove too

bruising for the recovering bilateral relationship, (Oxford Analytica, 2010). The deal falls within the framework of a policy announced by President George W. Bush in July 2007, which intended to approve a large scale sale of arms to member states of the Gulf Cooperation Council (GCC), (Yiftah, 2010). The then-U.S. Secretary of Defense Robert Gates and U.S. Secretary of State Hillary Clinton in their defence of the deal, after Members of Congress had written to the Obama's Administration on November 12, 2010, to raise "concerns and pose a number of strategic questions about the impact such sales would have on the national security interests of the United States and our allies", argued that:

"...This proposed sale will directly support U.S. interests by reinforcing our longstanding defense and security partnership with Saudi Arabia, enhancing Saudi Arabia's ability to deter and defend itself against terrorist groups and other regional threats, improving "interoperability"¹⁷ with the U.S. military, and sending a strong message to all countries that the United States is committed to supporting the security of its key partners and allies in the Gulf and broader Middle East...We believe the proposed package promotes U.S. strategic and foreign policy interests, and it is a key component of our overall regional strategy. The United States is committed to deepening its bilateral and multilateral security relationships in the Gulf to enhance regional stability and security. A key component of our regional cooperation is enhancing the defensive capabilities of our Gulf partners", (Gates and Clinton letter, 2010).

According to U.S. Assistant Secretary of State for Political and Military Affairs Andrew Shapiro, "This proposed sale has tremendous significance from a strategic regional perspective. It will reinforce our longstanding security partnership with Saudi Arabia...It will send a strong message to countries in the region that we are committed to support the security of our key partners and allies in the Arabian Gulf and broader Middle East. And it will enhance Saudi Arabia's ability to deter and defend against threats to its borders and to its oil infrastructure, which is critical to our economic interests", (Shapiro, 2010).

¹⁷ Refers to the U.S. military's capacity to coordinate attacks with Saudi Arabia

The Washington-based Center for Strategic and International Studies (CSIS) argues along similar lines in a recent report outlining how this arms deal would help advance U.S. national security interests. The report, titled “The Saudi Arms Sale: Reinforcing a Strategic Partnership in the Gulf”, argues that the United States shares critical strategic interests with the Saudis which “shape the proposed Saudi arms sale.” These interests include addressing Iranian threats in the region, securing Gulf energy exports critical to the U.S. economy, and easing the U.S. defence burden in the region. The United States, the report states, needs allies who “can fight effectively alongside the U.S., and that can ease the burden on the U.S. by defending themselves”, (Cordesman, November 2010). Most important of all, Cordesman argues “in fact, strong U.S. security ties to Saudi Arabia offer Israel a far better alternative than Saudi Arabia turning to European or other suppliers and questioning U.S. support if it faces a crisis with Iran...They will also help ensure the U.S. strategic position in the region at a time when other powers like China are becoming key players in global energy, and when recycling “petrodollars” is even more important than in the past”, (Ibid).

Within this context, the announcement of the sale was formalised in four separate notifications to Congress, representing various arms of the Saudi armed forces, (Ibid): The biggest, totalling US\$29.4 billion includes the sale of 84 Boeing F-15 fighter aircraft and the upgrade of another 70 F-15s, as well as advanced missiles, night vision goggles and guided munitions. The other three packages, which total US\$31.1bn, include 72 Blackhawk helicopters, 70 Apache attack helicopters and thousands of Hellfire missiles. Not included are a naval upgrade and missile defence, both currently under discussion and could add another US\$30 billion.

1. **The Royal Saudi Air Force (RSAF)** was prepared to purchase 84 F-15SA aircraft, 1,100 GBU-24 PAVEWAY III Laser Guided Bombs (2,000-lb.), and 1,000 GBU-31B V3 Joint Direct Attack Munitions (JDAM) 2,000-lb. bombs, along with 193 LANTIRN navigation pods (3rd Generation-Tiger Eye), 170 APG-63 (v) 3 Active Electronically Scanned Array Radar (AESA) sets, Harpoon, HARM (anti-radar), and Sidewinder missiles. Also included are the upgrade of the existing RSAF fleet of 70 F-15S multi-role fighters to the F-15SA configuration, communication security, site surveys, trainers, simulators, publications and technical documentation, personnel training and training equipment, U.S. government and contractor engineering, technical, and logistical support services, and other related elements of logistical and program support. The estimated cost is US\$29.432 billion, (DSCA, October 2010)
2. **The Royal Saudi Land Forces (RSLF)** was to receive 24 AH-64D Block III Apache Longbow helicopters and associated missiles and electronics. Also included are trainers, simulators, generators, training munitions, design and construction, transportation, personnel training and training equipment, publications and technical documentation, U.S. government and contractor engineering, technical, and logistics support services, and other related elements of program support. The estimated cost is US\$3.3billion, (DSCA, October 2010)
3. **The Saudi Arabian Royal Guard (SARG)** signed up for 10 AH-64D Block III Apache Longbow helicopters with the requisite missiles and electronics. Also included are trainers, simulators, generators, training munitions, design and construction, transportation, tools and test equipment, ground- and air-based SATCOM and line-of-sight communication equipment, personnel training and training equipment, publications and technical documentation, U.S. government and contractor engineering, technical, and logistics support services, and other related elements of program support. The estimated cost is \$2.223 billion, (DSCA, October 2010)
4. **The Saudi Arabian National Guard (SANG)** components were 36 AH-64D Block III Apache helicopters, 72 UH-60M Blackhawk helicopters, 12 MD-530F light turbine reconnaissance helicopters, and 36 AH-6i light attack helicopters, along with missiles and electronics. Also included are trainers, simulators, generators, munitions, design and construction, transportation, wheeled vehicles and organisation equipment, tools and test equipment, communication equipment, spare and repair parts, support equipment, personnel training and training equipment, publications and technical documentation, U.S. government and contractor engineering, technical, and logistics support services, and other related elements of program support. The estimated cost is \$25.6 billion, (DSCA, October 2010)

Further to that deal the Defence Security Cooperation Agency notified Congress of a possible Foreign Military Sale to the Government of Saudi Arabia of 150 JAVELIN Guided Missiles and associated equipment, parts and logistical support for a complete package worth US\$71 million, (DSCA, November 2010). Saudi Arabia will use the enhanced capability as a deterrent to regional threats and to strengthen its defence. Saudi Arabia currently does not have JAVELIN Anti-tank missiles in its inventory, but will have no difficulty absorbing these additional missiles, (Ibid). In May 2011 the

DSCA also notified Congress of a possible Foreign Military Sale Order to the Kingdom of Saudi Arabia for various night and thermal vision equipment, including parts and logistical support with an estimated cost of US\$330 million, (DSCA, May 2011). The proposed sale will augment Saudi Arabia's capability to meet current and future threats from potential adversaries during operations conducted at night and during low visibility conditions, (Ibid).

Furthermore, in June 2011 the Defence Security Cooperation Agency (DSCA) also notified Congress of a possible Foreign Military Sale to the Government of Saudi Arabia of a variety of light armoured vehicles and associated equipment, parts, training and logistical support for an estimated cost of US\$350 million, 404 CBU-105D / B Sensor Fuzed Weapons and associated equipment, parts, training and logistical support for an estimated cost of US\$355 million and a variety of light armoured vehicles and associated equipment, parts, training and logistical support for an estimated cost of US\$263million, (DSCA, June 2011). Additionally, in September 2011, the DSCA notified Congress of a possible Foreign Military Sale to the Kingdom of Saudi Arabia of Howitzers, radars, ammunition and associated equipment, parts, training and logistical support for an estimated cost of \$886 million, (DSCA, September 2011). Cordesman summed up the Saudi-U.S. military cooperation with very interesting words: "The U.S. can still count on some support from allies like Britain and France, but the fact remains that it will need its friends and allies in the Gulf even more. The same forces that have made the U.S. and Saudi Arabia key de facto partners in Gulf security will become even more important in the future", (Cordesman, 2010).

9.2.2 China-Saudi Military Cooperation

Saudi Arabia and China began their relationship slowly, commencing with Chinese purchases of Saudi Arabian crude oil. In the 1980s, China supplied a total of some US\$5 billion in military goods to Saudi Arabia, including in 1988 some 30-50 CSS-2 intermediate-range surface-to-air missiles and 15 mobile launchers valued at US\$3 billion, (Cordesman, 1997). The unfavourable experience Saudi Arabia had with China in the CSS-2 missile system deal may also play a role in explaining the minimal Sino-Saudi military relations. The downside to the CSS-2 missile system is twofold: (a) It is an extremely cumbersome system; and (b) The accuracy of the CSS-2. Although the Saudis have modified the CSS-2s to improve their accuracy, the missiles are still outdated and relatively inaccurate when compared to ballistic missile systems possessed by other countries, (Ibid). However, no publicly available evidence suggests that Riyadh is attempting to purchase new systems. China-Saudi cooperation in the defence sector actually decreased in the 1990s in the aftermath of the first Gulf War, with Saudi Arabia procuring much of its defence upgrades and replacements from the West. Chinese arms exports to Saudi Arabia likely did not exceed US\$1.5-2.0 billion throughout this decade, (Calabrese, 2004). Since Saudi Arabia took delivery of CSS intermediate-range ballistic missiles in 1988, there has been no documented evidence for transactions of a similar nature. Nor since then have there been credible reports of sales by China for significant quantities of conventional arms to Saudi Arabia, (Calabrese, 2005).

Due to Saudi Arabia's relations with the United States, Sino-Saudi military relations have been very limited. In the mid-eighties China supplied Saudi Arabia with long-

range missiles at the same time but not really much happened after that. Militarily, China's relations with Saudi Arabia remained as a buyer and seller relationship and did not move to strategic levels whereby China can place a greater control on the country security, (Sager, 2011). In this regard, Anthony Cordesman argues: "Saudi Arabia has strong incentives to maintain its security cooperation with the United States and to build up its forces to deter and defend against Iran and other potential threats. It faces the same challenges and threats, it needs a strong ally, and it faces many of the same strategic uncertainties. Moreover, there is no credible regional alternative", (Cordesman, September 2010). Indeed, China does not have the same capability to project power globally as the United States does and therefore cannot provide the same security assurances against the international threats Saudi Arabia faces, particularly against Iran or/and the internal dangers of terrorism. Even if the Chinese had the capability to project power globally, the Saudis may question the reliability of China's security assurances due to the long relations China has with Iran.

Additionally, the Saudis view China as a poor substitute for U.S. support against the other threats the Saudi Kingdom faces on the domestic front from terrorism (Calabrese, 2004), or from instability in Yemen. For example in 2009 during the Saudi military's two months' campaign against Yemeni Houthi rebels, the Kingdom turned to the U.S. for emergency provision of munitions, imagery and intelligence to assist them to operate with greater precision. According to a secret U.S. diplomatic cable sent in December 2009 and released by *WikiLeaks*, the U.S. Ambassador to Saudi Arabia, James B. Smith, acknowledged supplying Riyadh with "stocks of ammunition for small weapons and artillery." He would later approve using U.S. satellites to target the Yemeni rebels near Saudi Arabia's southern border,

(WikiLeaks, December 2010). In addition to the security assurances provided by the United States, Saudi Arabia also purchased a substantial amount of arms from the United States further expanding U.S.-Saudi military relations.

Interestingly, China itself was the world’s biggest arms importer over the past five years, with 9 percent of the total, followed by India, South Korea, the UAE and Greece, (Norton-Taylor, 2010). Saudi Arabia was the leading recipient of arms deliveries among developing world recipients in 2003-2010, receiving US\$29.0 billion in such deliveries. China ranked third in arms deliveries with US\$13.2 billion. India ranked second with US\$16.9 billion, (Grimmett, 2011). According to Stockholm International Peace Research Institute the major recipient countries for 2006–2010 were India, China and South Korea. Asian and Middle Eastern countries are expected to remain among the world’s largest importers, (SIPRI Yearbook 2011) (see Tables 9.2.2.1 & 9.2.2.2).

(Table 9.2.2.1): Arms Deliveries/Transfer Agreements to/with Developing Nations, 2003-2010

By the Leading Recipients (in millions of current U.S. dollars)				
	Arms Deliveries		Transfer Agreements	
Rank	Recipient	Value	Recipient	Value
1	Saudi Arabia	29,000	Saudi Arabia	44,300
2	India	16,900	India	38,100
3	China	13,200	U.A.E	18,700
4	Egypt	12,100	Egypt	14,400
5	Israel	10,300	Pakistan	13,000
6	U.A.E.	8,600	Venezuela	12,700
7	Taiwan	8,300	South Korea	10,000
8	Pakistan	7,600	Brazil	9,800
9	South Korea	7,300	Algeria	8,700
10	Algeria	4,500	Iraq	8,600

Source: Grimmett, (September, 2011)

In addition, most Chinese weapons for export are less advanced and sophisticated than weaponry available from western suppliers or Russia. China, consequently, does not appear likely to be a key supplier of major conventional weapons in the developing world arms market in the immediate future (see Table 9.2.2.2 below).

(Table 9.2.2.2): Arms Transfer Agreements or Deliveries to/with World

2003-2010; (in millions of current U.S. dollars , selected indicators)									
	2003	2004	2005	2006	2007	2008	2009	2010	TOTAL 2003-2010
Arms Deliveries to the World									
World Total	34,145	34,814	30,575	35,520	35,108	36,223	37,405	34,989	278,779
U.S.	10,845	11,614	11,775	12,320	12,308	11,923	14,305	12,189	97,279
(%) of Total	31.76%	33.36%	38.51%	34.68%	35.06%	32.92%	38.24%	34.84%	34.89%
China	800	900	1,100	1,500	2,000	1,900	1,700	2,200	12,100
(%) of Total	2.34%	2.59%	3.60%	4.22%	5.70%	5.25%	4.54%	6.29%	4.34%
Arms Transfer Agreements with the World									
World Total	31,386	41,775	46,294	57,268	60,794	66,917	64,175	40,355	408,964
U.S.	14,286	12,375	12,594	15,468	23,894	36,717	22,275	21,255	158,864
(%) of Total	45.52%	29.62%	27.20%	27.01%	39.30%	54.87%	34.71%	52.67%	38.84%
China	600	1,000	2,800	1,900	2,700	2,100	2,100	900	14,100
(%) of Total	1.91%	2.3%	6.05	3.32%	4.44%	3.13%	3.27%	2.23%	3.44%

Source: Adapted from (Grimmett, September 2011)

(a) Major West European category includes France, United Kingdom, Germany and Italy

Saudi Arabia has more recently preferred to limit the quantity and type of weapons it buys from China in order to maintain its close ties with the U.S., Saudi Arabia's largest arms provider, and China has done nothing to try and divert Saudi Arabia from this course, (Pant, 2008). The only reported deal was in 2007 which said China had signed a contract to provide Saudi Arabia with PLZ-45 155mm self-propelled howitzers for one battalion. This was the first time for the Saudi Arabian army to purchase Chinese-made weapons, (see Table 9.2.2.3).

(Table 9.2.2.3): The Suppliers of Major Suppliers to Saudi Arabia, (2005–2009)

Recipient	Supplier (a)						
	China	France	Russia	UK	USA	Others	Total
Saudi Arabia	6%	4%	0	42%	40%	8%	100%
Gulf region	4%	21%	9%	5%	54%	7%	100%

Source: SIPRI database

(a) Figures are suppliers' percentage shares of each recipient's total volume of imports.

(Table 9.2.2.4): China's Arms Sales to Saudi Arabia 1950-2010

No. ordered	Weapon designation	Weapon description	Year of order	Year(s) of deliveries	No. of produced
50	DF-3/CSS-2	IRBM	1986	1987-1988	50
54	PLZ-45 155mm	Self-propelled gun	2007	2008-2009	54

Source: SIPRI database

This lack of activity in the Sino-Saudi military relationship may be explained by the fact that the stability and preservation of the current Saudi Royal Family is in both Chinese and U.S. interests; (in particular due the recent instability in the Middle East), China is content with the strong U.S.-Saudi military relationship. The Chinese may view the situation as the United States being obligated to protect Chinese interests without China having to take an economic hit. In this light, China's behaviour would definitely be in line with the economic interdependence model. China is content with the status quo because it benefits and/or preserves Chinese economic interests and therefore will not take any actions which may change it. While the Sino-Saudi military relations has the potential to expand in the future (partially as a result of the growing Iranian threat and the Sino-Saudi security agreement signed in April 2006 and October 2010), China and Saudi Arabia have yet to take the big step.

As for the future, there is potential for the Sino-Saudi military relationship to expand. However, Sino-Saudi relations are still in their infancy and it is still uncertain which 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 military alternative to the United States, (*Financial Times*, March 18, 2011). In this context many analysts argue that increased energy trade will not necessarily lead to growing political and military ties as is the case with India, Japan and South Korea. This relationship will be driven by energy considerations, at least in the foreseeable future. Indeed, China doesn't present a viable replacement for the U.S. role and has never claimed to be so.

In this regard Andrew Shearer, Director of Studies at Australia's Lowy Institute for International Policy, argues that: "Asia has been something of a bystander in the Middle East and importantly, in the case of China, an increasingly anxious bystander", (Critchlow, March 2011). Abdulaziz Sager, the Chairman of the Gulf Research Center based in Dubai-UAE, goes further to say: "China will not have a significant role on the region security in the next twenty years because number one military deployment in the region is the western type, the majority of American and European position. And the Chinese always have a problem in communication, language in this part of the world and we see it in many aspects. Their primary interest is energy supply; they don't have this much political interest", (*Moscow Times*, February 24, 2011)

Barak Barfi, a research fellow with the New America Foundation, argues that: "The Chinese focus on economic interests and want regional stability, but are willing to do very little to ensure it", (Critchlow, March 2011). Indeed, the United States spends

around US\$50 billion per year to protect the free flow of oil from the Arabian Gulf to the global economy, (Yetiv, April 2011). China, by comparison, spends virtually nothing on Gulf security, while pursuing its strategy of building political and economic relations with oil-rich countries in order to secure oil for its growing economy. This is nowhere more apparent than in China's relationship with Saudi Arabia, the world's biggest oil power, (Ibid). In this light, China's action would definitely be in line with the economic interdependence model.

Additionally, with recent developments in the Arab World, Saudi Arabia remains fearful of the ability of Iran to destabilise 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. Here China still lags far behind America, which remains the Saudis' military mainstay. In this context, John Garver, a professor at the Georgia Institute of Technology in Atlanta-U.S., argues that: "Middle Eastern authoritarian regimes that survive the upheaval -- especially Saudi Arabia -- may well look upon China as a more reliable supporter than the U.S...But the problem is that China is simply not prepared, materially or psychologically, to meet the security needs of those countries", (Buckley, March 2011). The presence of American troops in the Gulf, though no longer on Saudi soil, reassures the Saudis - and China, since it can bank on America's presence, (*The Economist*, December 2010).

However, the Saudis are still keeping their options open. The overwhelming uprisings that swept the Arab countries in 2011 and resulted in overthrowing some Arab leaders made Saudi Arabia angry at the American reactions and the way they abandoned

Egypt's Mubarak. This could have very serious implications in the long term. It might make the Saudi Royal family more cautious in foreign policy. In that regard, China and Saudi Arabia also signed several security agreements, although the details of the agreements have not yet been released. During the Chinese President Jintao Hu's visit to Saudi Arabia in April 2006 the two sides signed a security cooperation agreement and a contract for some defence systems.¹⁸ China and Saudi Arabia also on October 11, 2010 have agreed to set up a joint security commission, (AFP, October 11, 2010). Chinese Public Security Minister Meng Jianzhu and his counterpart Saudi Interior Minister Prince Nayef bin Abdul Aziz signed a letter of intent on security training and exchanges. They also agreed to form a joint body of "high-level security officials" to boost cooperation in the field, (Ibid).

In summary, China and Saudi Arabia have not had close military relations. There are two primary reasons for this: (a) The United States has provided Saudi Arabia with advanced military equipment to strengthen the Saudi military and National Guard against foreign and domestic threats; and (b) The U.S. has provided security assurances to Saudi Arabia that China cannot provide. While U.S. military might has long offered the capability to protect Saudi Arabia's vast energy resources, links between the leading oil exporter and China are chiefly commercial. More than ever, as a revolutionary tide has swept away entrenched Arab leaders and rocked the oil-producing Middle East to its core, Saudi Arabia could need powerful back-up, (Laessing & Lewis, 2011).

¹⁸ For example see, in Arabic: "The Kingdom and China are Signing Agreements for Security and Defence Cooperation and a Memorandum of Understanding for the Advancement of Trade," Al-Riyadh, Apr 23, 2006, Issue 13817, available on: [<http://www.alriyadh.com/2006/04/23/article148704.html>], (accessed on September 9, 2007)

9.3 SAUDI ARABIA NUCLEAR OPTION

Speculation about the Kingdom's potential interest in acquiring nuclear weapons goes back to the 1980s. Saudi Arabia originally signed the NPT in 1988 to address concerns that it wanted to arm its newly Chinese acquired DF-3 (CSS-2) intermediate range ballistic missiles (IRBM) with nuclear warheads. Many experts noted that Saudi Arabia's commitment to nuclear non-proliferation has not resulted in a safeguards agreement with the International Atomic Energy Agency for more stringent inspections of nuclear-related facilities. Moreover, the Saudis refused to sign the Comprehensive Nuclear Test-Ban Treaty (CTBT). Such resistance may be further evidence that Saudi Arabia is seeking to keep its options open regarding future nuclear weapons development, (Feldman, 2004). In this context, four major issues could alter the Saudi's proliferation calculus in the future, making it more likely that Saudi Arabia would decide to acquire nuclear weapons. According to Russell, the Saudis "already have in place a foundation for building a nuclear weapons deterrent", (Reuters, 2004).

Firstly, deterioration of the U.S.-Saudi relationship could cause Saudi Arabia to consider nuclear proliferation to deter foreign aggression independently of U.S. security assurances. This scenario would only be likely if Saudi leaders completely lost confidence in the U.S. promise of protection during crises. Michael Freund argued recently in the Israeli newspaper *Jerusalem post*, that: "The lack of American will to confront the ayatollahs and stop them in their tracks has given various Arab leaders plenty of incentive, as well as a good excuse, to proceed down the nuclear trail ... If the Iranians aren't stopped, and soon, we may wake up a few years from now to

discover that Saudi Arabia and other unfriendly regimes have decided to upgrade their ‘civilian’ nuclear programs into weapons-making industries”, (Freund, 2010). While Luft goes further to say that Saudi Arabia could break its military dependence on the U.S. either by entering into an alliance with some other existing nuclear power or by acquiring its own nuclear capability. In either case, China would play a crucial role, (Luft, 2004).

Secondly, many analysts in Washington and the Middle East assume that in the event of a nuclear breakout by Iran, Saudi Arabia would feel compelled to build or acquire its own nuclear arsenal. Given Saudi Arabia’s vast wealth and strategic weakness, such a decision might seem logical, (Lippman, 2008). Riyadh’s view that the Iranian threat is serious and immediate was recently expressed by Saudi Foreign Minister Saud al-Faisal: “Sanctions are a long-term solution ... But we are looking at an Iranian nuclear program within a shorter term because we are closer to the locus of the threat. We are interested in immediate rather than in gradual solutions”, (Burns, 2010). Diplomatic cables obtained by *WikiLeaks* and published recently by the *Guardian* newspaper revealed that Saudi King Abdullah had privately warned Washington in 2008 that if Iran developed nuclear weapons “everyone in the region would do the same, including Saudi Arabia”, (*The Guardian*, June 29, 2011). Whether Saudi Arabia relied on its emerging nuclear power program to manufacture nuclear weapons (which would take approximately a decade), or simply bought ready-made atomic bombs from Pakistan, China will play a vital role, (Weitz, 2010).

Thirdly, Israel is also cited as a potential motivator for Saudi nuclear proliferation, since, as a regional rival, Israel’s nuclear and ballistic missile capabilities could prove

threatening to Saudi Arabia, (Report to the Committee on Foreign Relations, 2008). In an interview with the *Washington Post* Saudi Foreign Minister Prince Saud Al-Faisal raised this concern strongly. He said: “Iran is always mentioned but no one mentions Israel, which has [nuclear] weapons already”, (Prince Al-Faisal, 2005). The emergence of a nuclear Iran would conceivably tempt Israel to declare its nuclear capabilities openly. Israel may consider an overt Iranian deterrent too dire a threat to continue its opacity policy, thus creating strong pressure in Saudi Arabia to acquire its own deterrent vis-à-vis Israel, Iran, (McInnis, 2005).

Finally, external factors, however, are not the sole sources of motivation behind nuclear proliferation. Domestic circumstances must also be considered. (a) In a discussion of future Saudi proliferation decisions it is important to consider who will replace the ageing King Abdullah as the next ruler of Saudi Arabia. It is important to keep in mind that a new ruler in Saudi Arabia could have an important influence on the propensity of the Kingdom to proliferate. (b) Saudi nuclear ambitions crystallised in the run-up to the 2009 Copenhagen Summit, when it was realised that global efforts to control climate change could end up punishing countries that put off including non-carbon-based energy sources in their power portfolios, (Jha, 2011). (c) Saudi Arabia depends almost solely on oil export revenues to develop its economy. Burning oil for electricity production currently consumes about a quarter of the crude oil Saudi Arabia produces, (Hibbs, 2011). In 2010 Saudi Arabia consumed an average of 2.6 (mb/d), (IEA, June 2011) and the country is on course to consume an average of 2.8 (mb/d) of oil in 2011, up from 1.9 (mb/d) in 2007 and 1.6 million (mb/d) in 2003, (Jadwa, 2011), making it the world’s sixth-largest oil consumer behind the U.S., China, Japan, India and Russia. On a per capita basis, its oil consumption is sky high.

In 2011, its consumption is set to jump by 5.6 per cent, way above the global average of 1.4 percent, (Blas, 2011). Saudi oil demand has risen by 75 percent in the ten years since 2001 due to strong economic and industrial growth and subsidised prices. The strong surge contrasts with the more modest increase of 39 percent in the 1990-2000 periods, (Ibid).

Some economists argue that if Saudi Arabia's current energy consumption continues at the current rate, that within 20 years the Kingdom will burn the equivalent of almost all its recent daily output - more than eight million barrels a day - or around two-thirds its total production capacity", (McDowall, 2011). The Saudi investment firm "Jadwa" even paints a bleak picture for the future of oil exports in Saudi Arabia as the Kingdom could face a serious revenue crisis within the current decade as it will have to cut exports to meet rising demand. Jadwa pointed out the Kingdom's oil exports had declined from around 7.5 (mb/d) in 2005 to 5.8 (mb/d) in 2010 and could drop further by 2015, (Jadwa, 2011). In this context Jareer Ellass and Amy Jaffe from James A. Baker III Institute for Public Policy, Rice University, argue that:

"...It is in the Kingdom's long-term geopolitical and security interests to maintain its leadership role in the global oil arena. Riyadh's ability to threaten other oil producers that it could flood the oil market is a critical aspect buttressing its leadership role inside OPEC and gives the country regional clout as well. Saudi Arabia's ability to singlehandedly alter the price of oil gives the Kingdom significant geopolitical power, and it has used its ability to lower the price of oil to its geopolitical advantage on many occasions over the decades. With this oil superpower stature comes much of the global influence that Saudi Arabia enjoys on the international stage", (Ellass & Jaffe, 2011).

(Table 9.3.1): Saudi Break Even Oil Forecast at Current Spending Patterns

	2005	2010	2015f	2020f	2025f	2030f
Oil Indicators (million barrels per day)						
Oil Production	9.4	8.2	9.3	10	10.7	11.5
Oil Exports	7.5	5.8	6.3	6	5.6	4.9
Domestic Consumption	1.9	2.4	3.1	3.9	5.1	6.5
Budgetary Indicators (SR billion)						
Total Revenue	564	735	843	961	1,108	1,120
Total Expenditure	346	627	893	1,147	1,620	2,453
Balance	218	109	-50	-186	-512	-1,334
SAMA Net Foreign Assets	564	1,652	1,958	1,331	375	375
Domestic Debt	475	167	167	167	949	5,889
Breakeven Oil Price (US\$ per barrel)¹⁹						
Saudi Export Crude	30.3	71.6	90.7	118.5	175.1	321.7

Source: Jadwa Investments (July, 2011); f= forecast

Against this strategic backdrop, Saudi Arabia's signalling that it is prepared to go down this road may be an effective way of testing the U.S. by pressuring the American Administration to demonstrate more strongly its commitment to defend the Kingdom, especially after "abandoning" a longstanding regional ally like Mubarak, (McDowall, 2011). Indeed, many analysts believe that Saudi words about developing nuclear arms may have been intended to focus western attention on Saudi concerns about their regional rival rather than to indicate any kind of definite decision by Riyadh because the practical and diplomatic obstacles of doing so would be immense, (*The Guardian*, June 29, 2011). Within this context, those who believe Saudi Arabia would not respond to an Iranian acquisition of nuclear weapons by pursuing a weapon of its own usually emphasise one of three arguments.

¹⁹ A new estimate by the Institute of International Finance suggests that Saudi Arabia will need at least US\$110 oil by 2015 to balance its budget, up from US\$88 a barrel in 2011 given rising spending needs, (Elass & Jaffe, 2011).

The first argument suggests the value the Saudis place on their relationship with the United States would dissuade them from taking a nuclear decision that would severely damage their most important bilateral relationship, (Report to the Committee on Foreign Relations, 2008). Saudi Arabia depends on the United States for conventional armaments and military support during crises. Riyadh does not want to proliferate at the present time because doing so would deeply strain the U.S.-Saudi relationship, perhaps to an irrevocable degree, (Cabrera & Salama, 2006). Riyadh's desire to maintain a strong U.S.-Saudi relationship impedes the development of nuclear weapons within the Saudi Kingdom, as does the Royal Family's desire to prevent unconventional terrorism within their own borders, (Amlin, 2008).

The second argument relates to the character of the regime. Some argue the Saudi regime is too conservative, too timid to take such a bold and controversial step. Lippman is convinced that confrontation and defiance are not Saudi Arabia's style. He argues: "The Saudis' weapons of choice are cash and diplomacy. It is difficult to imagine the Princes of the House of Saud deliberately positioning themselves as global outliers and inviting reprisal from countries capable of inflicting serious damage on them", (Lippman, 2008). While Nield noted that Saudi Arabia has committed itself to a major industrialisation campaign that will require sustained engagement with the rest of the world ... It's not rational that they would jeopardise this in favour of a pre-emptive strike against the theoretical possibility of a nuclear-armed Iran", (Nield, 2010). Additionally, Amlin believes that the Saudi leaders do not want to incur the political and economic backlash that would result from their development of a nuclear arsenal at a time when they are trying to integrate more into the international economy, (Amlin, 2008).

The third argument often cited suggesting that Saudi Arabia would not pursue nuclear weapons relates to Saudi Arabia's nuclear technology capabilities. There exists a relatively strong consensus regarding the immature state of Saudi Arabia's nuclear technology infrastructure. Saudi Arabia lacks the human expertise and the technical knowledge necessary to develop a nuclear weapons program on its own, (Report to the Committee on Foreign Relations, 2008). For instance, since Saudi Arabia does not operate nuclear power facilities, its scientists do not have the experience necessary in enriching uranium for reactor fuel, in nuclear fuel conversion, or in operating nuclear reactors, (Feldman, 2004). Despite this, Saudi Arabia started a new civilian nuclear programme, but it will need years to be developed. Mohammed ElBaradei, then the International Atomic Energy Agency (I.A.E.A) Director General, in a visit to Saudi Arabia in 2007, estimated that the Saudi nuclear civilian plan might take up to 15 years, (Broad & Sanger, 2007).

However, if the Saudi pursues the "nuclear option" China could theoretically be an attractive partner, but in the current strategic environment it's hard to imagine that this could be a realistic scenario. From China's perspective Iran is not yet a nuclear power and has not reached the "point of no return." Li Guofu, Director of the Chinese Center for Middle East Studies at the Institute for International Studies (CIIS), argues that China is not 100 percent convinced that Iran is pursuing nuclear weapons. He indicated that observers who believe there is a "point of no return" in Iran's technical development of nuclear weapons were incorrect, because the problem was fundamentally a political one and not technical, (Wikileaks, 2009). Furthermore, China is a member of the NPT system (since joining in 1992), and obliged "not in any way to assist, encourage or induce any non-nuclear weapon State to manufacture or

otherwise acquire nuclear weapons or other explosive devices, or control over such weapons or explosive devices”, (Lippman, 2008). Under the Nuclear Proliferation Prevention Act of 1994, China would face revocation of the U.S. nuclear cooperation agreement it worked so hard to secure, as well as economic sanctions, if it were deemed to have “aided or abetted” the acquisition of nuclear weapons, (Ibid).

The well known economist Simpfendorfer noted that a nuclear Iran and regional arms race would be bad for business. He argues that even Chinese academics have signalled that Iran’s unpredictable behaviour is challenging China’s relations with its other regional partners, especially Israel and Saudi Arabia. While China may not agree to sanctions easily, its support for Iran is often overstated, and the idea of a non-nuclear Iran with still strained relations with the United States is not an unattractive outcome for China’s leadership, (Simpfendorfer, 2010). From the Chinese perspective if Iran pursues the nuclear weapons it will violate its international obligations. Subsequently, it will be difficult for China to support Tehran’s action. Secondly, China’s economic and strategic interests in Saudi Arabia and the Gulf states are much more important than its interests in Iran. In this regard the Saudi Arabia and the Arab Gulf States, (even Iraq) could easily make up Iran’s oil exports to China in the event of an oil embargo on Iran. Most important of all, the prospect of a nuclear arms race in the Middle East could push China strongly towards cooperation with the United States and the oil-consuming nations such as Japan, South Korea and India for the stability of the Gulf region thus containing the Iranian threat.

Indeed, China has broad interests that cannot be made hostage to Iran’s ideological priorities or its regional goals. While the priority for China is stability, for Iran it is

change, including disruptive change. Chinese scholar Zha Daojiong argues that, “part of Chinese strategy is to respect America’s concerns about Sino-Middle-Eastern relations”, (Zha, 2007). Furthermore, Garver suggests a desire to keep a certain distance; China has avoided the use of the word “strategic” in its relations with Iran, although it has had no such hesitation in relation with Saudi Arabia, (Garver, 2006). Even from the Iranian perspective, a virtual or ambiguous nuclear capability could be attractive to Iran as a way of avoiding expanded international economic sanctions and isolation, or even worse possible U.S. or Israeli strikes. Moreover, Iran does not want to jeopardise its partnership with China or provide a pretext for the GCC states, especially Saudi Arabia, to acquire a nuclear weapon capability of their own, (Davis, 2011). Hence, in the short to medium term Iran is likely to strive to stay within the bounds of international norms and laws established by the NPT while continuing with uranium enrichment and warhead experimentation, (Ibid).

For Sino-Saudi interests to be maintained, however, Saudi security needs must be met; their status as a primary parameter of Saudi national interest does not permit them to be ignored. Up until now, this role has been filled by the United States, allowing the Sino-Saudi relationship to flourish based on other interests, combined with the light level of security dialogue. If U.S.-Saudi relations falter, China would doubtless feel pressure to take a more active role in Saudi defence. Failure to do so would defy the community of interests China has established over the past several decades, (Anderson, 2004). However, Bahgat has concluded that no evidence suggests that the U.S.-Saudi relationship will sour in the near future, and the United States and Saudi Arabia are likely to share common interests for many years, creating a strong reason for Saudi Arabia not to develop nuclear weapons, (Bahgat, 2011).

Saudi Arabia is currently linked to arms deals with the United States for at least the next decade. While Riyadh's civilian nuclear program could also take a decade to develop the potential human and technical resources that Saudi Arabia would need. At present there is no solid evidence that Riyadh intends to go down this route and there is also no evidence which points to the Saudi acquisition of weapons of mass destruction. For all of these reasons, Saudi Arabia does not appear to be interested in developing - or seem to be developing - a weapon of mass destruction, nor is China actively supporting Saudi Arabia in acquiring nuclear weapons.

9.4 TECHNOLOGY TRANSFER & EDUCATION EXCHANGE

China and Saudi Arabia have undertaken efforts to further develop their relationship in science, education and technology transfer. The number of personal and professional contacts and exchanges has risen in recent years, overcoming the linguistic-cultural divide, and establishing in both countries a widening band of educated elites who are familiar with each other's societal norms and traditions, knowledgeable about each other's distinctive ways of conducting business, and attuned to their counterparts' national and institutional interests, (Calabrese, 2004).

The two nations are also witnessing enhanced cultural, educational and religious cooperation and exchange, which has deepened understanding and friendship between the two peoples, (Xinhua, June 21, 2008). Saudi Arabia has created Chinese language study programs to prepare Saudis to work in the Jizan Economic City, where planned

Chinese investments in aluminium production and other industries will create thousands of new jobs. Saudi Arabia also has offered loans to support Chinese government education projects, (China Daily, February 6, 2009). Educational cooperation between China and Saudi Arabia has achieved considerable progress. With full support from the Chinese Government, the King Abdullah Scholarship Program chose China as one of the five destination countries in Asia for its applicants, (Perspectives ASIA, 2009). Indeed, Khalid Al-Anqari, Saudi Minister of Higher Education, recently led a Saudi delegation constituting of more than twenty universities to China. During the visit, Saudi universities signed ten cooperation treaties with Chinese education institutions in the field of higher education, (Ali Khan, 2011). Following the visit of the Saudi delegation, a high-level Chinese delegation comprising chairmen of a number of universities visited Saudi Arabia, (Ibid).

Scientific cooperation is booming. The Gene Institute of the Chinese Science Academy is working closely with its Saudi counterpart on improving the gene of Saudi date. The relations also witnessed strengthening cooperation in bio-chemistry, nanotechnology, meteorology, precision instrument and other advanced areas of science and technology, (Perspectives ASIA, 2009). King Abdul Aziz City for Science and Technology (KACST) has also signed a Memorandum of Understanding (MOU) with Huawei Technologies, China's major telecommunications equipment manufacturer, to strengthen cooperation in telecom technology and personnel training, (Ibid). Most important of all, in April 2011, Saudi Arabia announced its plan to sign a nuclear cooperation agreement with China. The Saudi Cabinet said it has authorised Hashim Yamani, President of the King Abdullah City for Nuclear and Renewable Energy, to hold talks with Chinese officials to reach a deal for the peaceful use of

atomic energy, (Arab News, April 12, 2011). The agreement allows the two countries to cooperate in the fields of production, use and transfer of knowledge regarding the peaceful uses of nuclear energy, (Ibid).

The emphasis on education is perhaps the most spectacular of the king's revolutionary changes. The Saudi Government has already offered scholarships to thousands of students to study in the United States, Canada, Malaysia, Australia, New Zealand, Japan, China and others. According to the Saudi Minister of Higher Education Khalid Al- Anqari, Saudi students worldwide reached in 2011 a total of over 120,000 noting that more than 43,500 Saudi students now were studying in the United States alone. An additional 5,000 students will participate in the scholarship program (2011-2012), (Royal Embassy of Saudi Arabia in Washington, 2011). In contrast, ten years ago, there were only twenty to twenty five students from Saudi Arabia studying in China, but that number now is up, (*China Daily*, April 29, 2009). The total number of students studying in China under this program had reached 147 by the end of 2007, (Perspectives ASIA, 2009). That number rose to 400 in 2008 and then jumped to 500 in 2009, (*China Daily*, April 29, 2009). Today, according to Yang Honglin, the Chinese Ambassador to Saudi Arabia, 1100 Saudi students are currently studying in universities located in different Chinese cities, (Ali Khan, 2011). Few would know that Saudi Aramco has been sending students to study in China since 1986, (Sfakianakis, 2009).

To put these figures in perspective, they represent less than one percent of the total Saudi students studying abroad. In comparison almost half of the Saudi students studying abroad are in the United States and the United Kingdom, the U.S. has

received 30 percent of Saudi scholarship students, followed by the U.K. 15 percent, Canada 11 percent, Australia 8 percent and Egypt 6 percent, (Abdul Ghafour, March 13, 2011). The Saudi's student number in the U.S. is a higher number than the one prior to 9/11 and the Saudis are in the top ten student nationalities list studying in the U.S., (Wahab, 2010). Moreover, as of 2010, an estimated 15,616 Saudi students were in the United Kingdom alone, (Wanger, 2010). On the other hand around 50 Chinese are enrolled at various Saudi universities, (Ali Khan, 2011). For the Chinese and Saudis students the U.S. is still the favourite technological destination. China is the leading place of origin for international students in the United States with 127,628 in 2009/10, an increase of 30 percent from the previous year, (Institute of International Education, 2010).

While Saudi Arabia realises the importance of technology transfer there has been little Sino-Saudi interaction here. There is not much data available regarding this topic suggesting that there has not been much Sino-Saudi interaction in this realm (mostly educational). As stated earlier, while China and Saudi Arabia seem to be taking the first steps in increasing the Sino-Saudi technology transfer by signing cooperation agreements over the last few years, a strong Sino-Saudi relationship in this realm is yet to be seen. Neither side is aggressively pushing the other for more cooperation in this area.

9.5 CONCLUSION

This chapter has attempted to decipher Chinese intentions towards Saudi Arabia. The main question it attempted to address was whether Chinese actions were in accordance with the realism model or economic interdependence model. As stated earlier in the chapter, if China is acting in the offensive realism model, it should be attempting to expand its power and influence in Saudi Arabia at every opportunity with the intent to undermine U.S. hegemony. This would include proactive actions to: (a) Sell Saudi Arabia sophisticated technologies and arms and provide security assurances to make Saudi Arabia less dependent on the United States and more so on China; (b) Encourage Saudi Arabia to shift its political allegiance from the United States over to China; and (c) Provide Saudi Arabia with the technology and expertise to make the country less dependent on the U.S.

If China is acting in the economic interdependence model, it should be: (a) Interacting militarily with Saudi Arabia in a business manner, and not providing it with massive amounts of advanced military hardware with the sole purpose to make it less reliant on the U.S. security assurance and arms sales; (b) Interacting militarily with Saudi Arabia according to China-U.S. relations and to the International Treaty on the Non-proliferation of Nuclear Weapons (NPT); and (c) Basing its technological cooperation with Saudi Arabia in a manner to advance the economic relations.

This case study has shown that Chinese intentions are more along the lines of the economic interdependence school of thought rather than the realism model. Thus the developing dependence of China on Middle-Eastern oil does not seem to point

towards future oil for weapons deals that would undermine the security of this region. On the contrary, the Chinese leadership appears to have relinquished that tactic to secure its oil supplies. Indeed, China and Saudi Arabia have not had close military relations. There are two primary reasons for this: (a) The United States has provided Saudi Arabia with advanced military equipment to strengthen the Saudi military, Air force and National Guard against domestic threats such as the Al-Qaida groups; and (b) The United States has provided security assurances to Saudi Arabia against international threats that China cannot provide.

While China may be limited in the military assistance it can provide to Saudi Arabia, if it was acting in the offensive realism model it should still be attempting to undermine the U.S.-Saudi military ties in order to further the Sino-Saudi military ties. For example, if China wants to advance military ties with Saudi Arabia in order to keep it away from U.S. influence, it would be possible to do what China did with Pakistan through the development of missile capabilities and/or nuclear weapons in Saudi Arabia in order to be able to protect itself without the urgent need for the United States. Until now there has been no documented evidence to support such scenario. The chapter has shown that this is not the case; on one hand China does not want to be an alternative to the U.S., on the other Saudi Arabia is still pursuing security cooperation with the United States and China has done nothing to undermine it. Yet some analysts point to the possibility that China will encourage Saudi Arabia to adopt the nuclear option and the development of long-range missiles, but there is no evidence confirming this to be the case, for several reasons: (a) That such choices are strategic in nature which may lead to serious confrontation with the U.S., something that both Saudi Arabia and China do not want to happen; (b) That such a

program is not difficult to be detected or monitored especially in light of advanced technological resources owned by the United States or its allies; and (c) It needs the human capital/talents and infrastructure in Saudi Arabia which is not currently available.

Energy is undoubtedly the primary driver of the Saudi-China relationship today, and will remain so in coming decades. Yet, as for Saudi Arabia, the new situation presents it with a dilemma. On the one hand, given China's rising global status, Saudi Arabia has an interest in strengthening bilateral ties, especially in energy sector. In addition, strengthening ties with China may offer Saudi Arabia an additional means to promote its campaign against the Iranian nuclear program. On the other hand, having previously "suffered" due to its missiles deal with China, Saudi Arabia is not interested in creating the impression that cooperation is growing, thereby yet again arousing American suspicions. These limitations are clear to China, and because it is sincerely interested in a long term strengthening of energy relations with Saudi Arabia, China has not and will likely not force Riyadh to choose between China and the US. Chinese military policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States as realists may contend. All China's military actions closely align with the economic interdependence school of thought. As for the future of militarily, educational and technological fronts the study forecasts that Saudi Arabia will depend on the U.S. at least for the next decade. While the Sino-Saudi military relations has the potential to expand in the future for three reasons: (a) The Sino-Saudi security agreements signed in April 2006 and October 2010; (b) As the quality of Chinese weapons systems improves; and (c) The Saudi desire to keep their options open as a hedge policy to balance the American power.

CHAPTER TEN

IMPLICATION FOR THE U.S. & ASIA'S MAJOR OIL CONSUMERS

10.1 INTRODUCTION

The case studies have shown Saudi Arabia needs the United States to remain (at least in the near future) the major strategic force in the Gulf, in particular to constrain what the Saudis perceive as potential military threats from Iran. At the same time China's and other Asian powers growing weight is more consistent with the Saudi view of the new "oil silk-road." While Beijing's approach is more gravitational than confrontational, China seeks influence so that the United States and its allies will not work together to limit China's options, (Fredriksen, 2006; 209). As China and India influence grows in the Middle East two contradictory points should be highlighted: on one hand, the old "oil for security" paradigm of U.S.-Saudi relations could weaken as China's (and India) economic and political gravitational force grows over time, (Andrews-Speed, 2009: 8). On the other hand, while there is fear for the future of the U.S. role, there is at the same time no alternative to it. No other country has the military resources or the will to safeguard what is, in the end, a global commons, (Alterman, 2011: 71). Indeed, a recent study by the Center for Strategic and International (CSIS) finds that citizens of countries of the Middle East are more apt to expect a weakened United States over the next decade. But there is also still a sense that the United States is the only actor with the ability to play the role of external guarantor of security for the region, (CSIS, 2011).

10.2 IMPLICATIONS FOR THE U.S.

In this geopolitical environment where China is acting in the economic interdependence model, there are three scenarios regarding the Sino-U.S. relationship predicted for the Middle East: (a) Containment: the U.S. will see China's "rise" in the Middle East as a threat which should be contained. On the other hand, the resource scarcity could lead China to adopt a more aggressive foreign policy; or (b) The unilateral approach: pursue U.S. objectives in the Middle East while refusing to acknowledge or take into account Chinese interests; or (c) Cooperate but hedge: maintain the status quo and pursue U.S. objectives in the Middle East while acknowledging or respecting Chinese interests. While concern over access to resources will continue to act as a constraint on China's foreign policy and also as an inducement for avoiding conflict with the United States, at the same time America will respect the Chinese interests while working to keep the U.S. as a dominant power in the Middle East.

10.2.1 Scenario One: Heading for a Collision

Of greatest concern to the U.S. in this scenario is the potential for the burgeoning competition to escalate or progress into a military confrontation over resources, or access to them. The theory of a "China threat" still has influential supporters in Washington and in several U.S. think-tanks. A popular view among many U.S. analysts is to see China's pursuit of foreign energy supply as an integral part of China's grand strategy to build up the country's power, (Zha, 2007). They argue that China adopted a "String of Pearls" strategy which is a manifestation of China's rising

political influence through efforts to create access to ports and airfields, develop special diplomatic relationships, and modernise military forces that extend from the South China Sea through the Strait of Malacca, across the Indian Ocean, and onto the Arabian Gulf, (Pehrson, 2006). In this regard, Lieberthal and Herberg noted that China has greatly increased cooperation, port access agreements, and maritime ties with Pakistan, Bangladesh, and Myanmar in an apparent effort to be better positioned to protect its maritime energy transport routes during a future crisis. This cooperation, in turn, risks exacerbating the broader tensions between the United States and China over the increasing pace and scale of China's military and naval modernisation, (Lieberthal and Herberg, 2006). Indeed, Richard Bernstein and Ross Munro have written in their book *"The Coming Conflict with China"*, "China and the United States were not headed toward cooperation and friendship but toward a multifaceted and potentially dangerous rivalry", (Bernstein and Munro, 1997).

Hardliners in Washington also believe that China's global oil strategy signals a dangerous threat to U.S. interests. They call for denying China access to energy resources while building up U.S. military capacity and strengthening alliances with key oil producing states, (Schmitt & Blumenthal, 2005). Dan Blumenthal and Joseph Lin, of the American Enterprise Institute, characterise energy importation as a "zero-sum game" and describe China's energy purchases as reflecting "the paranoia that drives Chinese thinking on energy security." In a longer-run sense, Blumenthal and Lin foresee China's "perceived military necessity and an intense sense of national pride [that] may already be leading China to its own variant of sea control...American offers of cooperation [with China]...may well be overpowered by the nationalist instinct to control one's own trade... [leading China] to compete with America for sea

control”, (Blumenthal & Lin June 2006). But the bluntest words describing this dooming scenario came from Robert Kaplan who wrote recently:

In the background of the ongoing Middle Eastern drama looms the shadow of a rising China. China is not a “responsible stakeholder” in the international system, as we proclaim it should be; it is a “free rider.” We are at war in Afghanistan to make it a safe place for China to extract minerals and metals. We have liberated Iraq so that Chinese firms can extract its oil. Now we are at war with Libya, which further diverts us from concentrating on the western Pacific—the centre of the world’s economic and naval activity—which the Chinese military seeks eventually to dominate, (Kaplan, 2011).

On the other side, many Chinese scholars believe 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, democratisation, free trade, and energy supply are understood to be subsumed within this conceptual framework. Within this context, they stress two points: the first is that because oil is a finite commodity it is viewed as a vital interest for both the economic and national security realms. They also argue that the current American hegemony in the Middle East could pose a long-term strategic threat to China if and when its relationship with Washington deteriorates and leads to a war over Taiwan. In that case, the Americans could be in a position to deny the Chinese access to the energy sources in the Middle East, (Hadar, 2010). Indeed, a wide variety of influential Chinese experts, including scholars, policy analysts, and members of the military, believe that the United States can sever China’s seaborne energy supplies and in a crisis might well choose to do so, (Erickson & Collins 2010).

The second point is that China’s economic prosperity, survivability, and relative position in the world is dependent on securing energy sources to meet future energy demand. With such considerations in mind, it would appear that politicians in Beijing are worried that the U.S. seeks to exploit China’s energy weakness. Dependence on

imported oil, domestic energy shortages, rising oil costs, and the spectre of long-term global energy “scarcity” could undermine the country’s economic growth and seriously jeopardise job creation, raising real risks of social instability in China, (Reilly, 2007). In this geopolitical context, the potentially explosive combination of a China less willing to passively accept U.S. leadership and the prospect of competition between China and other states for control over vital energy resources poses particularly critical challenges to U.S. interests in the Middle East. China’s search for oil is making it a new competitor to United States for influence in the Middle East. If not managed prudently, this competition will generate multiple points of bilateral friction and damage U.S. strategic interests in the region, (Leverett & Bader, 2005).

Yet, conflict between China and America is not likely to play out in the near future. Richard S. Williamson, a senior fellow at the Brookings Institution, former assistant to President Ronald Reagan and U.S. Ambassador to several international organisations including a spell between 2007 and 2009 as the U.S. president special envoy to Sudan, argues that recent events have emboldened Chinese leaders. They are seeking their own path. They will not sign on uncritically to the global architecture the United States has had such a major role in erecting. But this is not an irrational approach by the world’s most populous country with a surging economy. The challenge for the United States is to be clear eyed about its interests, keep faith with its values, and engage with the rising China to chart a course of cooperation and competition that respects China’s legitimate interests while protecting America’s (Williamson, 2011). Steve Yetiv, a widely sought expert on the Middle East and University professor of political science, goes further to say that the growing Sino-Saudi relationship could well challenge - but need not hurt – U.S.-Saudi relations. The

United States remains an important market for Saudi Arabia. It is also vital to Riyadh's goal of diversifying its economy and joining the global economy. Most importantly, it is the key provider of Saudi security. China cannot replace that role for the foreseeable future, if at all, and the Saudis know this very well, (Yetiv, 2011). He continued by saying that the growing Sino-Saudi relationship helps bolster China's economic growth. Provided that China plays a responsible global role in the future and does not undermine U.S. foreign policy, that is good for the United States, for global trade and business, and for China's long-term domestic stability, (Ibid). There is no question that China's high interdependence with the Middle East will make it more challenging for the United States to successfully pursue its objectives and follow through with unilateral action, but despite China's increasing influence and economic power in the Middle East, neither China nor the United States will take hostile military actions against each other for various reasons. Firstly, the most obvious reason is that nuclear weapons make it suicidal to risk a great-power war. Recently Secretary of State Hillary Clinton denied the United States was seeking to contain China, she argued that:

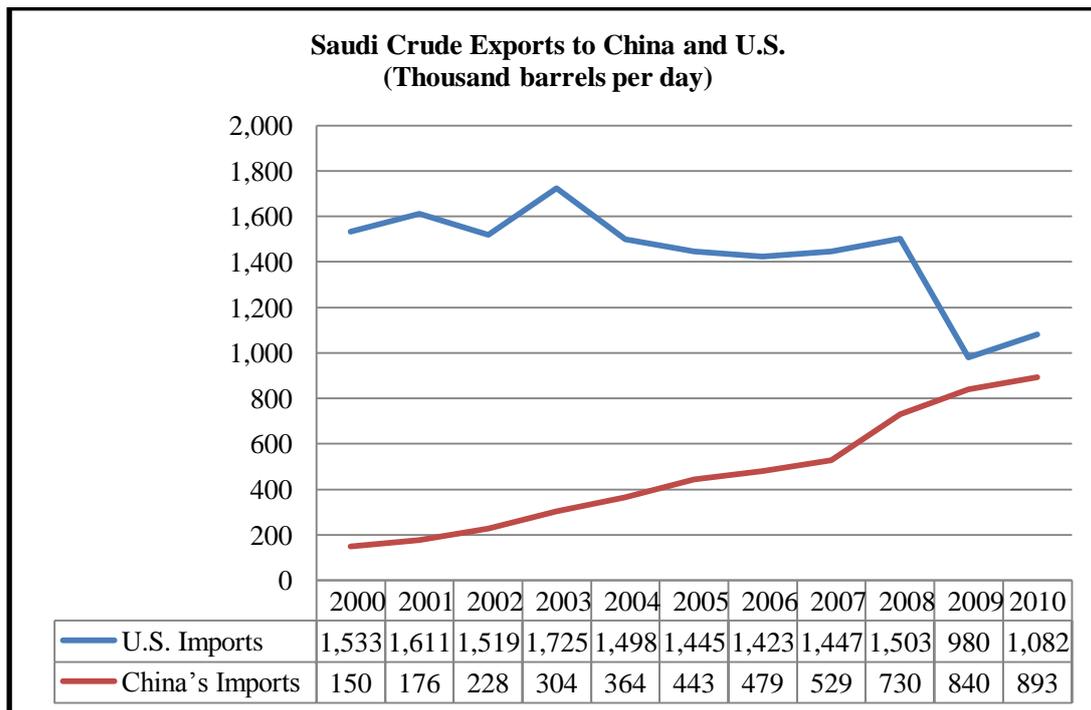
“...The relationship between China and the United States is complex and of enormous consequence and we are committed to getting it right... There are some in both countries who believe that China's interests and ours are fundamentally at odds. They apply a zero-sum calculation ... so whenever one of us succeeds, the other must fail... But that is not our view”, (Reuters, October 28, 2010).

Secondly, since China is highly economically interdependent with the United States, and the Middle East, it will seek to prevent any situation which may jeopardise the ongoing peaceful economic exchanges among them. Therefore, China will seek greater cooperation with all sides in order to avoid an armed conflict in an effort to protect its economic interests. If Beijing believes that the U.S. is manipulating energy policies to weaken and contain China, then China (as Reilly argues) will likely

respond by increasing the pace of its military modernisation, tying Chinese energy investments abroad ever more closely to dubious regimes, promoting security cooperation with adversarial governments, and politicising global energy markets. Hardliners in Beijing, who warn of the U.S. military threat, will be strengthened, rendering the “China threat” a self-fulfilling prophecy, (Reilly, 2007). According to the Chinese scholar Zha Daojiong, any unilateral action against China may produce unintended consequences by giving weight to voices in China that see politically motivated diplomacy as the ultimate instrument for securing China’s oil supplies, (Zha, 2006).

Thirdly, as China becomes more economically interdependent with the Middle East, so the United States will not be able to exclude China from the region. On the contrary, as a result of its reliance on Middle Eastern oil, the interests of the United States and that of China and all of the oil producing countries in the Middle East region will more closely align. Because both the U.S. and China are reliant on oil, regional stability and the preservation of the status quo are in both countries’ economic interests. The stability and security of Saudi Arabia are now in the interests of both the United States and China; therefore, cooperation between the two countries should increase, (Zhang, 1999). Loren Brandt argues that looking beyond short-term friction over trade balances and currency valuations “we see substantial overlap between China’s economic interests and those of the United States.” She goes on to say that, “As a big importer of natural resources, China, like the United States, will benefit from and may actively seek to promote stability in the Middle East and other resource-rich regions”, (Barandt, 2007).

(Figure 10.2.1.1): China and U.S. Imports of Crude Oil from Saudi Arabia



Source: EIA and General Customs Administration of China

Alterman noted that the United States is not the principal oil export market for any country in the region, nor is any Middle Eastern country the principal source for U.S. imported oil, (Alterman, 2011:77). Comparatively speaking, the Middle East and Saudi Arabia are more important to China than to the United States as oil suppliers. Only two of the top ten suppliers of oil to the United States in 2010 were from the Middle East. Saudi Arabia was the U.S.'s third supplier and only supplied about 11 percent of total American oil imports. In contrast, five of the top ten suppliers of oil to China in 2010 were from the Middle East and supplied Beijing with about 40 percent of its total oil imports.

(Table 10.2.1.1): U.S., China Crude Oil Imports from Top 10 Countries in 2010^a

	U.S.		China	
	Total Oil Imports = (9.2 mb/d)		Total Oil Imports = (4.8 mb/d)	
	Country	(%) of total imports	Country	(%) of total imports
1	Canada	21.3%	Saudi Arabia	18.6%
2	Mexico	12.5%	Angola	16.4%
3	Saudi Arabia	11.7%	Iran	8.9%
4	Nigeria	10.6%	Russia	7%
5	Venezuela	9.8%	Oman	6.3%
6	Iraq	4.5%	Sudan	5.2%
7	Angola	4.1%	Iraq	5%
8	Colombia	3.6%	Kuwait	4%
9	Algeria	3.5%	Kazakhstan	4%
10	Brazil	2.7%	Brazil	3%

Source: EIA and China's General Customs Administration

(a) All percentages were calculated by the author

Currently, as the above table shows, the pattern of China's overseas oil dependency is complementary to that of the U.S. China is much more reliant on the Middle East and Africa, while the U.S. sources more from its North and Latin American neighbours. That lessens the short-term prospects for direct competition between the world's two largest economies for sources of crude oil, (Hook, 2011). Another point is made by Amy Myers Jaffe who argues that, by the 2020s, the capital of energy will likely have shifted back to the Western Hemisphere, where it was prior to the ascendancy of Middle Eastern mega-suppliers such as Saudi Arabia and Kuwait in the 1960s, (Myers, September 2011:86). The reasons for this shift are partly technological and partly political. She noted that geologists have long known that the Americas are home to plentiful hydrocarbons trapped in hard-to-reach offshore deposits, on-land shale rock, oil sands, and heavy oil formations. The U.S. endowment of unconventional oil is more than 2 trillion barrels, with another 2.4 trillion in Canada and 2 trillion-plus in South America. The latest breakthrough will make these

resources technologically accessible, (Ibid). If this is correct, that will lessen the prospects for direct competition between China and the U.S. For now and despite that the U.S. is decreasing its dependence on both Saudi and Middle East oil, at the same time the U.S. still gets almost half of its oil from OPEC member countries. Indeed, six of the top ten suppliers of oil to each of the U.S. were OPEC members, (Table 10.2.1).

(Table 10.2.1.2): U.S. Crude Oil Imports (selected indicators, mb/d)

	From World	From OPEC	OPEC's Share of Total (%)^a	From Middle East^b	Middle East's Share of U.S. total (%)^c	From Saudi Arabia	Saudi Arabia's Share of Total (%)^d
2010	9,21	4,55	49.4%	1,71	18.6%	1,08	11.7%
2009	9,01	4,35	48.2%	1,66	18.0%	0,980	10.8%
2008	9,78	5,41	55.3%	2,35	24.1%	1,50	15.3%
2007	10,03	5,38	53.6%	2,16	21.5%	1,44	14.3%
2006	10,11	4,78	47.2%	2,22	21.9%	1,42	14.0%
2005	10,12	4,81	47.5%	2,24	22.1%	1,44	14.2%
2004	10,08	5,04	50.0%	2,40	23.8%	1,49	14.7%
2003	9,66	4,57	47.3%	2,47	25.5%	1,72	17.8%
2002	9,14	4,08	44.6%	2,25	24.6%	1,51	16.5%
2001	9,32	4,08	51.9%	2,70	29.03%	1,61	17.2%
2000	9,07	4,54	50.0%	2,43	26.8%	1523	16.8%
1999	8,73	4,05	46.3%	2,36	27.05%	1387	15.8%

Source: EIA (October, 2011)

(a), (b), (c) & (d) All figures and percentages were calculated by the author

China and the United States have a high level of dependence on energy imports, particularly oil; they are exposed to the same risks of the international oil markets, (Zha & Hu, 2007). The argument that the U.S. Government conspires to manipulate world oil prices fails to consider the implications of the United States' place as the largest importer of oil in the world. It would be self-destructive for the U.S. Government to support a rise in world oil prices, as oil is openly sold to whoever is willing to pay the highest bidding price. If the price were manipulated in any

direction, any damage to China would also hurt the United States, (Ibid). Therefore it is in the interests of China and the U.S. to both cooperate together towards price stability and keeping reliable oil supplies.

Alterman made another important point that while China has shown an interest in purchasing discounted heavy crude from Saudi Arabia and is further investing in its capacity to refine it, the United States is focused on importing lighter crude that is both easier to refine and less environmentally damaging, (Alterman and Garver, 2008: 58-59). The oil production and consumption network is a perfect example of global economic interdependence... China's exposure to oil price shock caused by supply disruptions is thus exactly equal to America's exposure, and to all other nations around the globe regardless of their dependence on oil imports. Tellingly, as Table 10.2.3 shows, the United States is more exposed than China to fluctuations in world oil prices, (Blair, 2006) (see Table 10.2.3 below).

(Table 10.2.1.3): Oil Imports by U.S. & China^a (selected indicators, 2001-2010)

Mineral Fuels, Oils, Distillation Products, etc (US\$ billions)									
	OPEC's Yearly Basket Price (US\$)	U.S.				China			
		Total (US\$ bn)	(%) Of U.S. Total Imports	From OPEC (US\$ bn)	From Middle East (US\$ bn)	Total (US\$ bn)	(%) Of China's Total Imports	From OPEC (US\$ bn)	From Middle East (US\$ bn)
2010	77.45	362,7	18.4%	146,8	51,2	188,6	13.5%	91,3	67,9
2009	61.06	279,1	17.4%	109,8	38,3	123,9	12.3%	63,1	45,4
2008	94.45	501,9	23.1%	222,9	87,5	169,2	14.9%	86,8	68,5
2007	69.08	372,3	18.4%	162,03	53,7	105,1	10.9%	49,6	39,2
2006	61.08	345,1	17.9%	148,4	50,2	89,09	11.2%	41,2	34,1
2005	50.64	298,07	17.2%	124,5	43,3	64,08	9.7%	27,5	25,2
2004	36.05	216,4	14.1%	91,3	35,1	48,02	8.5%	17,5	17,1
2003	28.10	163,2	12.5%	64,9	27,05	29,24	7.0%	10,5	11,3
2002	24.36	122,08	10.1%	46,6	19,9	19,3	6.5%	6,7	7,2
2001	23.12	129,1	10.9%	53,4	23,08	17,5	7.1%	6,2	7,1

Source: UNComtrade and OPEC

(a) All figures adapted and calculated by the author

Even if the United States attempts to persuade its Arab States allies to isolate China, the likelihood that they would abide by the U.S. request is very minimal. The possibilities of a politically motivated embargo against China by Saudi Arabia and other Middle Eastern exporting countries remain very low. There are several reasons for this optimism. (a) China has pursued a balanced foreign policy towards the Middle East and the long running Arab-Israeli conflict in the region and most Arabs appreciate China's position. This reduces the possibility of Arab oil exporters joining hands to blockade against China. (b) As discussed earlier, Saudi Arabia (and the Middle East in general) has too much to gain from maintaining good Sino-Saudi relations, (particularly in light of the Saudi Government accelerating its economic development to provide jobs and opportunities for Saudi youth) and would likely push aside U.S. requests to minimise that relationship. And (c) China and the Gulf Cooperation Council (GCC) member countries including Saudi Arabia are working toward establishing a free trade area. In this context Chinese scholar Daojiong argues that growing levels of interdependence between China (and the U.S.) and the Middle East serves as a useful warrant against a blockade against China, (Zha, 2006).

Furthermore the Chinese scholars Zha Daojiong and Hu Weixing reject the argument that the United States is planning to control international oil production and movement. They argue that since China began to import oil in the early 1980s, there has not been a single case of the United States intercepting oil moving into or out of China, (Zha & Hu, 2007). The only confrontation occurred in July 1993 when the Clinton Administration suspected that a Chinese cargo ship, called the *Yinhe* (Milky Way) was going to Iran with chemicals that could be used for chemical weapons and sought to inspect its cargo. Afterwards, the U.S. State Department said that the

suspected chemicals were not found on the ship at that time. China has raised this Yinhe incident as a grievance against the United States and against the credibility of U.S. intelligence in particular, (Kan, 2011). According to Daojiong and Weixing that unfortunate episode in Chinese-U.S. relations, however, was related to non-proliferation rather than the Chinese acquisition of Middle Eastern oil, (Zha & Hu, 2007). Additionally, China benefits from the freedom of commercial navigation through the Strait of Hormuz and it is certainly in China's interest for movement of oil through the Strait of Hormuz to continue to be safeguarded against sabotage, (Ibid). According to Steve Yetiv, the United States spends around US\$40 to 50 billion per year to protect the free flow of oil from the Arabian Gulf to the global economy, more than the entire defence budgets of all but a few countries. China, by comparison, spends virtually nothing on Gulf security, while pursuing its strategy of building political and economic relations with oil-rich countries in order to secure oil for its growing economy. This is nowhere more apparent than in China's relations with Saudi Arabia, the world's biggest oil power, (Yetiv, 2011).

Ryan Clarke made another important point; he argues that irrespective of capabilities, the United States cannot also enforce a naval blockade that would starve China of energy resources. If it attempted to do so, America's failure to effectively execute the blockade would damage the prestige of the U.S. Navy (and the entire military for that matter) with obvious negative implications for American diplomacy and the nation's global standing. It would be impossible to discriminate between ships as a wide range carry China's energy resources, thus inevitably harming the energy security of American allies while also severely disrupting the global economy, (Clarke, 2009). While Bruce Blair adds that any oil blockade is tantamount to a declaration of war

and if China's retaliation were to stop all shipping to the rest of North East Asia, it would lead to situation that would plunge the world economy into chaos. The potential damage would be so devastating to the global economy it makes for an almost impossibly remote scenario, (Blair, 2006). Additionally, taking overt actions to limit Chinese influence in the Middle East would likely yield more anti-American sentiments not only in the Middle East, but also with states throughout the world. In this globalised world, China has strong economic ties with countries throughout the world (including America and U.S. allies) and as a result there could be a global backlash against the United States.

Finally, even in the event of an oil embargo against China, the affect in the country's economy would not be devastating because (a) China's economy is still coal dependent; (b) China produces about 4 (mb/d) of oil; (c) China has built-up strategic oil reserves; and (d) China has the ability to obtain oil from other countries that reject the boycott of China. In this regard Blair emphasises that the Chinese economy is more resilient to oil price shocks caused by supply disruptions than may be commonly believed. In the event of the sudden and total disappearance of Saudi oil from the global supply, the adverse impact of the resulting price spike on China's economy would not be severe, (Blair, 2006). Furthermore, Robert Ross argues that growing Chinese imports of oil is a widespread nationalist argument for expanded power-projection capability. But Chinese coal, hydropower, nuclear power, and domestic sources of oil and natural gas supply China with nearly all of its energy requirements. China relies on imported oil for about 10 percent of its total energy usage, and an increasing share of this oil comes across land borders with Central Asia and Russia. The International Energy Agency forecasts that through 2030 oil will remain a

marginal Chinese energy resource and suggests that domestic oil production will be sufficient to fuel China's commercial transport sector, (Ross, 2009).

While China and other importers may feel vulnerable to Middle Eastern oil disruptions the dependencies are mutual. This deepening of economic ties implies that Saudi Arabia will have to consider the impact on its own economies of punitive actions against Beijing in the area of oil supply. Indeed, the world's largest exporter by far, Saudi Arabia, for example, cannot stop pumping oil without shattering its fragile social contract with its own population, (Ibid). As Iraq's experience has shown, even the Middle Eastern countries that have overthrown authoritarian governments are unlikely to dwell on China's reluctance to condemn their fallen leaders. John Calabrese, a scholar at the Middle East Institute in Washington, argues that, "To the extent that they need customers for their commodities and foreign direct investment in their economies, memories of China's position (or lack of one) in the political upheaval could prove short", (Buckley, 2011).

These factors do not make this option appealing or likely to happen, much less the most beneficial course of action to take regarding Sino-U.S. relations involving the Middle East. As much as the United States desires to maintain the power and influence it has in the Middle East, this option of considering China as a rising threat and taking actions to undermine it does not seem to be successfully attainable, and would be a very dangerous option.

10.2.2 Scenario Two: U.S. Unilateral Approach

As the dominant geopolitical power in the Middle East, the United States could persist in a more unilateral approach to the most strategically critical region of the world, in a manner that is dysfunctional for the interests of other important regional and international players, and eschews effective leadership in reforming the global energy architecture to accommodate rising powers like China, (Leverett, 2008). While the United States may be able to pursue its policies in the Middle East without cooperating with China, whether the pursuit of those policies will be successful is another matter. But if the U.S. chooses to pursue its objectives regardless of the Chinese, the long-term consequences for America's regional position in the Middle East and its international standing generally are potentially serious.

Firstly, Iran remains an emerging challenge deeply involved in strategic competition with the U.S. and its friends and allies in the region, (Cordesman, 2010). In this regard China could cause problems for the United States and its policies. If China feels that U.S. policies act against Chinese core interests, it can undermine U.S. actions in numerous ways and China will not hesitate to use its economic, political, and possible military means to further its objectives and undermine U.S. policies. Secondly, under these conditions, Middle Eastern energy producers and China, may ultimately forge a de facto strategic alliance and look collaboratively for non-military means to contain American influence in the Gulf region, (Leverett, 2008). At least three options for strategic cooperation between China and Middle Eastern energy producers to contain U.S. influence in the Arabia Gulf present themselves. (a) China and the Middle Eastern states could ultimately move to use their continued willingness to finance

America's burgeoning current account deficit and overall debt levels as a source of strategic leverage over U.S. foreign policy. (b) China and the Middle Eastern states with substantial influence in OPEC could coordinate their actions to shift away from the U.S. dollar, (Ibid). And (c) the single most important long-term implication of the instability in the Middle East may well be consolidation of the Gulf Co-operation Council under Saudi leadership, a move that would leave the Gulf monarchies less reliant on Washington for regional security, (Bremmer, 2011).

Yet, the Chinese behaviours are more consistent with economic interdependence. Yoram Evron argues that, if Chinese conduct is examined through the prism of its diplomatic actions, the general balance appears to be positive. China has adjusted its policy to the American line in most international crises, and in some cases has even acted to help the U.S. For example, China cancelled its nuclear agreements with Iran in 1997, immediately embraced the U.S. declaration of war on global terrorism in 2001, refrained from vetoing most UN Security Council sanction resolutions sought by the U.S., and has played an active and important role in the North Korean crisis, (Evron, 2009). As discussed previously, China's support for Iran is often overstated. China's lack of military capability in the Gulf region has forced it to resort almost exclusively to other tools of statecraft to protect and advance its interests, (Yetiv & Lu, 2007). There is no strong evidence that the Chinese engagement with the region is designed to undermine U.S. interests. While not being entirely compliant with Washington's wishes, Chinese officials, nevertheless, have repeatedly emphasised the commercial nature of China's relations with the Middle East, (Jiang, 2007). Freeman believes that what China is not, and is not likely to be in the foreseeable future, is either a substitute or a counter to American military power in the Middle East. It will

likely take a couple of decades for this to change substantially, (Freeman, 2009). In the interim, the United States will remain the central element in the balance of power in the Middle East, (Ibid).

Beijing will continue to rely upon Washington for its energy security interest in the Middle East. Given Beijing's limited political influence and the unstable geopolitical situations in the region, China shows no interest in exploiting the energy relationships it might have to influence the oil-producing countries in the region, thereby challenging America's influence and strategic interests, (Wu & Liu, 2007). Professor Tim Niblock of Exeter University argues along these lines by highlighting China's cautious approach, "The Chinese are perfectly aware of the fact that oil supplies from the Gulf are dependent on the U.S. Navy, both in the Gulf and the Straits of Malacca, and are keen to integrate into the global leadership role, not challenge it", (EIU, 2011:15).

Analyst Mustafa Alani at the Gulf Research Center in Dubai is sceptical that China could step in and he argues that: "Certainly in the region (the Arabian Gulf) we feel the United States losing credibility, and we feel that in the near future we're going to see a vacuum in the region...But we still believe the Chinese [are] not a mature power: Politically, it's still really very weak; strategically, it still is not trusted. We don't feel China is a replacement to United States in any sense", (Kenyon, 2008). Certainly, China is becoming more influential economically, and its military is increasing its capacity, but it has little ability to project force beyond its borders, and Beijing has shown little interest in supporting or paying for the global commons that underpins the world economy. For now, China prefers to be largely a "free rider" on

the international system that helps safeguard trade routes, sea lanes and relative regional stability — allowing Beijing to focus on pressing domestic challenges, (Larson, 2010).

The United States has thrice in the past two decades put its military might behind securing access to Middle East oil supplies, (these include military interventions in Iraq both in 2003 and in 1990-91 and the Gulf “tanker war” in the mid-1980s). The U.S. Navy controls the sea lines of communication (SLOC) in all the key energy transit bottlenecks, including the Straits of Hormuz, the Malacca Straits, and the Southeast Asian sea lanes, (Lieberthal & Herberg, 2006: 7). In all cases there is no evidence that the United States plotted to undermine China’s interests. On the contrary, Beijing has been a major beneficiary of the enormous U.S. efforts to maintain stability and security in the greater Middle East and seems content to freeload on the U.S. policy of securing sea lanes for the time being. For example, in the first Gulf War (1990-1991), the liberation of Kuwait by U.S. forces, did not prevent the flow of Kuwaiti oil to China or stop trade relations between Kuwait and China to thrive. On the contrary, China’s interests in Kuwait expanded and increased as the volume of trade jumped to more than US\$8.5 billion by the end of 2010, (UNComtrade, 2011).

Iraq serves as another example. After the American invasion, Iraq turned into an important energy/trade partner for China, similar to Kuwait. The trade between Iraq and China doubled almost 20 times. The volume of trade between China and Iraq jumped to US\$9.86 billion by the end of 2010 from US\$517.1 million in 2002, (Ibid). Also ironically, (a) the U.S. imports from Iraq of crude oil in 2010 were less in

volume in comparison before the invasion; (b) the first oil license awarded by Iraq's government after the U.S.-led invasion was to state-run China National Petroleum Corp. (CNPC) who won a US\$3.5 billion development contract for Iraqi oil field *Al-Ahdab* in November 2008, (Bloomberg, July 7, 2011). And (c) the U.S. was encouraging Saudi Arabia and others Arab producers (including Iraq) to increase their oil exports to China to make it less dependent on Iranian oil. Additionally, China and Iraq recently consolidated their trade ties with the two countries signing agreements on economic cooperation and personnel training, (Qin, 2011).

(Table 10.2.2.1): U.S. Imports from Iraq of Crude Oil (mb/d)

	Before the U.S. Invasion			After the U.S. Invasion						
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Iraq Total Oil Exports	1,85	1,49	0,911	1,60	1,43	1,55	1,61	1,65	1,87	1,89 ^a
To the U.S.	0,795	0,459	0,481	0,655	0,527	0,553	0,484	0,627	0,449	0,414

Source: EIA, (July, 2011)

(a) OPEC Annual Statistical Bulletin (2010/2011)

(Table 10.2.2.2): Iraq Main Trade Partners (2010)

Main Destinations of Exports, 2010 (share of total)		Main Origins of Imports, 2010 (share of total)	
US	24.3%	Turkey	24.1%
India	17.3%	Syria	18.6%
China	12.1%	China	14.7%
South Korea	8.1%	US	6.5%
Italy	6.8%	Germany	3.7%
Japan	6.5%	Jordan	3.6%
Others	24.9%	Others	28.8%

Source: based on IMF (DoTS), (July 2011)

The International Energy Agency (IEA) is predicting that an additional 3.6 million b/d from both Iraq and Saudi Arabia will be needed to balance demand by 2030, (Elass &

Jaffe, 2011). And more worryingly for both China and the United States is the fact that many countries in the Middle East are vulnerable to domestic unrest or political crises and oil exports could easily be curtailed by work stoppages or strikes by oil workers or political unrest. Thus, it is very important that the United States and China should work together to ensure: (a) Stability in the Gulf region; (b) Iraq's ability to complete the required projects to develop the oil sector major export infrastructure development projects.

(Table 10.2.2.3): Over 21 (mb/d) of Middle East Oil Production could be at Stake from Middle East Turmoil and Political Contagion

Country	Median Age (years)	Unemployment Rate	Oil Production (mb/d)
Algeria	27.1	10%	2.1
Libya	24.2	30%	1.5
Syria	21.5	8%	0.4
Yemen	17.9	35%	0.4
Saudi Arabia	24.9	11%	9.5
Iran	26.3	15%	4.5
Iraq	20.6	15%	2.8

Source: (Elass & Jaffe, July 2011).

As for the dollar issue, China and the Arab Gulf States has amassed around US\$5 trillion (more than three of them belong to China alone) of foreign exchange reserves much of it held in U.S. Treasury securities. About two-thirds of China's US\$3.2 trillion (end-June, 2011) in currency reserves, the world's largest by a wide margin and which are estimated to be invested in U.S. dollar-denominated assets, (Rabinovitch, 2011). Some observers have described this as a great shift in the global balance of power and China could bring the United States to its knees by threatening to sell its dollars. But in doing so, China would not only reduce the value of its reserves as the price of the dollar fell, but it would also jeopardise U.S. willingness to

continue to import cheap Chinese goods, which would mean job loss and instability in China. As Nye put it bluntly, “If it dumped its dollars, China would bring the United States to its knees, but might also bring itself to its ankles”, (Nye, October 2010).

Andy Rothman, an analyst in Shanghai for the investment bank CLSA, goes on the similar lines to say: “If Beijing even hinted that it might try to sell part of its American debt other countries might sell their dollar assets noting that this would drive down the value of China’s holdings...It would be financial suicide for China”, (Barboza, 2011). China carefully manages its currency, the renminbi (RMB), to closely track the value of the U.S. dollar. Any major disruption in the stability of the dollar would therefore have powerful implications for the stability of the RMB and have potential complications for China’s own economic health, (Freeman & Bean, 2011). While China holds 25 percent of U.S. foreign-held treasury securities, a sizable percentage, China does not hold a strategic hammerlock on the United States’ international financial position, (Department of the Treasury/Federal Reserve Board, July 18, 2011). China is unlikely to pre-emptively abandon the dollar because of its own fears of resulting international chaos. However, China’s certain goal to reduce its dependence on U.S. dollar–denominated debt is becoming more urgent, (Freeman & Bean, 2011).

In this regard, Yi Gang, China’s Director of State Administration of Foreign Exchange, explained that “Chinese investments in U.S. Treasuries are market investment behaviour and we don’t wish to politicise them,” (Anderlini, 2010 March). Overall China’s options may be limited. Dong Yuping, an economist with the Institute of Finance and Banking at the Chinese Academy of Social Sciences (CASS),

argues that “China faces a dilemma in its holding of the US T-bonds ... Beijing has little choice but to continue to buy the U.S. debt because Beijing wants a stable dollar. And the US Treasury bonds remain the most liquid investment product in the market”, (*China Daily*, July 20, 2011). While Zhang Ming, also expert at (CASS), agrees that, “China has no choice but to keep buying ...After all, US Treasury bonds are still the largest and most liquid investment product in the world...There’s really nothing different they can do”, (Barboza, 2011). Furthermore, Nicholas R. Lardy, a China expert with the Peterson Institute for International Economics, agreed that the Chinese government has little incentive to begin any large sell-off of U.S. securities, and probably could not find a market to buy them even if it did, (Richburg, 2009). He went on further to say, “If it was known they were beginning to sell their holdings, prices would come down and they’d take bigger losses. They’d be shooting themselves in the foot. They’re in the dollar trap...There’s no easy way out of it”, (Ibid). But, unlike the Cold War, Kenneth Lieberthal, a China specialist with the Brookings Institution in Washington, argues that the current economic version of a stalemate is not necessarily antagonistic; both sides benefit, (Ibid).

Today, with the downgrade of U.S.’s credit rating, many influential voices in China have started calling loudly to make the Chinese currency convertible and dump the investment in the U.S. dollar. Yu Yongding, a former academic member of the Monetary Policy Committee at China’s central bank, urged Beijing to stop buying dollar-denominated assets in order to reduce its vulnerability to swings in the world’s major reserve currency. He argues that: “China must stop buying U.S. dollars and allow the renminbi exchange rate to be decided by market forces as soon as possible. China should have done so a long time ago... The situation is ultimately

unsustainable. The longer it continues the more violent and destructive the final adjustment will be”, (Yongding, 2011). But Yu’s comments were at odds with recent remarks from Xia Bin, a current academic member on the Chinese central bank’s Monetary Policy Committee, who said that China can’t have a freely floating yuan in the next decade, and that the dollar would be a key global reserve currency for a long time, (Wang, 2011).

On the other hand, The Saudi Arabian Monetary Agency’s holdings of foreign securities rose 12 percent this year to a record 1.32 trillion riyals (US\$ 350 billion), as shown on June 30, 2011 according to central bank data. HSBC Holdings Plc estimates a “large proportion” of those investments are in Treasuries, (Varma & Maedler, 2011). The advance boosted the reserve assets of the world’s biggest oil exporter by 12 percent to 1.86 trillion riyals, (US\$496 billion) as shown on central bank data, (Ibid). Liz Martins, Dubai-based senior economist at HSBC, noted that,: “Given that Saudi export revenues are predominantly U.S. dollar-denominated, we assume a large proportion of these holdings to be U.S. Treasuries, and we do not expect a major shift in this policy”, (Ibid). In this regard, a secret cable was leaked by *Wikileaks* of a meeting between US Treasury Secretary Timothy Geithner and Saudi Finance Minister Ibrahim Al Assaf in Riyadh in 2009. In the meeting Al Assaf told Geithner, “We still believe that the dollar will be the dominant reserve currency and trading currency for a long time to come...Our policy is to support this and maintain the riyal-dollar peg”, (Wikileaks, July 30, 2009). Currently there is no evidence that either China or Saudi Arabia are dumping the dollar. On the contrary China increased its holding of U.S. Treasury securities to US\$1159.8 billion by the end of June 2011 and

from US\$867.7.2 billion by the end of June 2010, (U.S. Department of the Treasury/Federal Reserve Board, July 15, 2011).

Additionally, Charles Freeman and Jeffrey Bean from the Center for Strategic & International Studies (CSIS) made another important point: as China heads toward a year of political transition in 2012, any external source of instability will be examined through a prism of domestic political stability. A crisis in the value of the dollar that could spur inflation or a disruption in China's export machine will therefore be viewed with alarm, (Freeman & Bean, 2011). Finally, even if China and oil producing countries decided to diversify away from the dollar it would be gradual and not coordinated and based on the U.S.'s economic performance rather than based on political reasons. China and the Saudi Arabia would be better advised to move to a managed float against a basket of currencies than to peg to another currency if there were to be a change, (*Financial Times*, August 6, 2011).

The scepticism regarding the U.S. and the dollar is reinforced by the weakening American economy. The world needs another reserve currency. The problem is there is no credible alternative yet. Stuart Gulliver, the Chief Executive of HSBC and formerly a currency trader, argues along similar lines: "On a secular basis, the dollar will continue to weaken. But on a cyclical basis, there is no alternative. There is a lack of [other] things to buy. There is a real absence of alternatives", (*Financial Times*, August 6, 2011). The U.S. dollar still has "reserve-currency status", as Table 10.3.2 shows that throughout the last decade, an average of two thirds of the total allocated foreign exchange reserves of countries have been in U.S. dollars. The dollar may remain dominant currency for at least the next decade because: (a) the Chinese

currency “yuan” currently is non-transferable and could take another decade to become a convertible currency in world markets; (b) the troubles faced by the euro zone now; and (c) the small size of Japan and the British currency markets.

(Table 10.2.2.4): Currency Composition of Official Foreign Exchange Reserves

	1995	2000	2005	2006	2007	2008	2009	2010
US Dollar	59.0	70.5	66.4	65.7	64.1	64.1	62.1%	61.5%
Euro		18.8%	24.3%	25.2%	26.3%	26.4%	27.6%	26.2%
Pound Sterling	2.1%	2.8%	3.6%	4.2%	4.7%	4.0%	4.3%	4.0%
Japanese Yen	6.8%	6.3%	3.7%	3.2%	2.9%	3.1%	2.9%	3.8%
Swiss Franc	0.3%	0.3%	0.1%	0.2%	0.2%	0.1%	0.1%	0.1%
Other	13.6	1.4	1.9%	1.5%	1.8%	2.2%	3.1%	4.4%

Source: IMF, (June 2011)

As for the future, the National Intelligence Council in its comprehensive study “*Global Trends 2025: A Transformed World*” predicts that, “The United States will remain the single most powerful country but will be less dominant...The need for the U.S. to act as regional balancer in the Middle East will increase, although other outside powers - Russia, China and India - will play greater roles than today, (National Intelligence Council, 2008). In this regard U.S. President Barack Obama in a May 19, 2011 speech on the Middle East and North Africa identified what he called four “core interests” in the region. (1) “Countering terrorism”, (2) “Stopping the spread of nuclear weapons”, (3) “Securing the free flow of commerce and safeguarding the security of the region”, and, (4) “Standing up for Israel’s security and pursuing Arab Israeli peace”, (Office of the White House Press Secretary, 2011). The U.S. military and intelligence presence in this region is designed to support these objectives and to reassure U.S. allies while deterring potential adversaries such as Iran, (Terrill, 2011). From the Chinese perspective they have no problem (as they

demonstrated in the past) to respect the American interests as far as the U.S. respects the Chinese interests in the region. Indeed, China will continue to rely upon the U.S. for its energy security interest in the Middle East. Given Beijing's limited political influence and projected power and the unstable geopolitical situations in the region, China shows no interest in exploiting the energy relationships it might have to influence the oil-producing countries in the region, thereby challenging America's influence and strategic interest.

In sum, it will be very difficult for the U.S. to pursue her objectives in the Middle East while refusing to acknowledge or take into account Chinese interests. If the United States remains in control of the Middle East, but still takes into account the interests of China, Beijing will not stand in the face of U.S. hegemony at least in the next decade or two. Of course there will be differences in policies between the two countries, but they will be manageable if each side respect the interests of the other.

10.2.3 Scenario One: Engage But Hedge

Under this scenario, the United States will encourage China to play a larger global role and will not view China's increased influence in the Middle East as a threat to U.S. hegemony or interests. On the contrary, the United States will gladly offer China more prestige. In return, however, Washington will expect Beijing to shoulder greater international responsibilities and obligations, (Schweller, 2011). Former U.S. Secretary of State Henry Kissinger argues that the United States and China should

“find a way to cooperate” to avoid strategic confrontation. Kissinger’s advice in his recent book *“On China”* is this, “The U.S. should not seek an enemy in China à la Huntington but cooperation in a global condominium.” Kissinger believes that: “Chinese thinkers developed strategic thought that placed a premium on victory through psychological advantage and preached the avoidance of direct conflict... Relations between China and the United States need not – and should not – become a zero-sum game... Key issues on the international front are global in nature. Consensus may prove difficult, but confrontation on these issues is self-defeating”, (Kissinger, 2011). In *On China*, Kissinger says:

“Eight American presidents and four generations of Chinese leaders have managed this delicate [non-conflictual] relationship in an astonishingly consistent manner, considering the difference in starting points.” Yet their exceptionalisms go in different directions: “American exceptionalism is missionary. It holds that the United States has an obligation to spread its values to every part of the world. Chinese exceptionalism is cultural. China does not proselytise; it does not claim that its contemporary institutions are relevant outside China.”

Furthermore, Franklin Lavin, who previously served as Undersecretary for International Trade at the U.S. Department of Commerce, where he was lead negotiator for China and has also served as U.S. Ambassador to Singapore (2001–2005), uses similar lines to argue that: “Since the Nixon-to-China moment, we have had about four decades of relations, across eight presidents, both political parties, a range of philosophies, different challenges, and different times. But, there is a high degree of continuity in that relationship and I think there are two pillars that allow for that continuity. One is the pillar of engagement that, regardless of the issue or the challenge, we were not going to break off or try to diminish relations but always try to find a way to improve them. The second pillar is respect for China’s “One-China” policy, that we would not seek to undermine that, although we certainly have interests vis à vis Taiwan. But we never tried to directly do something to diminish the one-China policy”, (Lavin, 2011).

Indeed, the U.S. and Chinese economies - the world's largest and the fastest-growing major economy, respectively - have become inextricably intertwined, locked in a kind of co-dependency that neither side thinks is particularly healthy, but which for the moment neither will move to break, (Richburg, 2009). China depends largely on the United States as the most important market for its cheap goods. America, with growing budget deficits and a huge national debt, depends on China as the main holder of U.S. Treasury securities, with Beijing's stockpile officially estimated to be nearly US\$1.15 billion (at the end of June, 2011).

(Table 10.2.3.1): China's Top 5 Export Partners in 2010

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
U.S	54,3	70,0	92,6	125,1	163,3	203,8	233,1	252,7	221,3	283,6
Hong Kong	46,5	58,4	76,2	101,1	124,5	155,4	184,2	190,7	166,2	218,2
Japan	45,0	48,4	59,4	73,5	84,0	91,7	10,21	116,1	98,0	120,2
South Korea	12,5	15,5	20,0	27,8	35,1	44,5	56,1	73,9	53,6	68,8
Germany	9,7	11,3	17,5	23,7	32,5	40,3	48,7	59,1	49,9	68,0

Source: IMF (July, 2011)

In this context Kenneth Lieberthal argues that, "China and the U.S. are in a fairly advanced stage of economic mutual interdependence...I think the Chinese can pull the rug out from under our economy only if they want to pull the rug out from under themselves...I think it is in neither of our interests to see that unravel." He added: "If we can find ways to manage our differences and cooperate where we can, we both win. If not, we both lose", (Ibid). Indeed, as the case studies have shown, the United States alone cannot single-handedly shoulder the task of stability and security of the Middle East. Meanwhile, China is still incapable of projecting power in the Middle East and that robs it of significant strategic and political leverages in the power play in the Middle East, (Kapila, 2011). Also Kierman argues on similar lines that China's

rise as a Middle East power can be managed by the United States if Beijing can be convinced that it shares the same interests as the developed-economy oil consumers - stability in oil-producing areas, resource development through cooperation, reduced oil and gas consumption - and if at the same time the U.S. recognises that China has legitimate concerns about its own energy security that can be addressed in a cooperative way, (Kiernan, 2008).

Despite that the U.S. views China's presence in the region with some apprehension, so far there is no evidence that it has an exclusionary policy toward China. The U.S. seems to be accommodating to China's oil needs, and China is reciprocating by being sensitive to American interest in the Middle East, (Olimat, 2010). Indeed the case studies have shown that the Chinese strategy towards Saudi Arabia and the Middle East is not a government conspiracy, nor is it indicative of aggressive Chinese strategic posturing. Alterman and Garver argue in their book, *"The Vital Triangle: China, the United States and the Middle East"*, that two nations (Saudi Arabia and China) made narrow agreement in their mutual interest, uncomplicated by either country's sense of its global role or its global responsibility. Saudi Arabia has oil, China needs oil. On that basis, agreements were made, (Alterman & Garver, 2008). They go further to say, China is not and does not seek to be a rival of the United States in the Middle East, (Ibid).

The case studies have also shown that Chinese actions are more closely linked to the economic interdependence theory of international relations; therefore, it may be possible to increase Sino-U.S. cooperation as long as each side acknowledges and respects each other's economic and national interests. China is not determined to

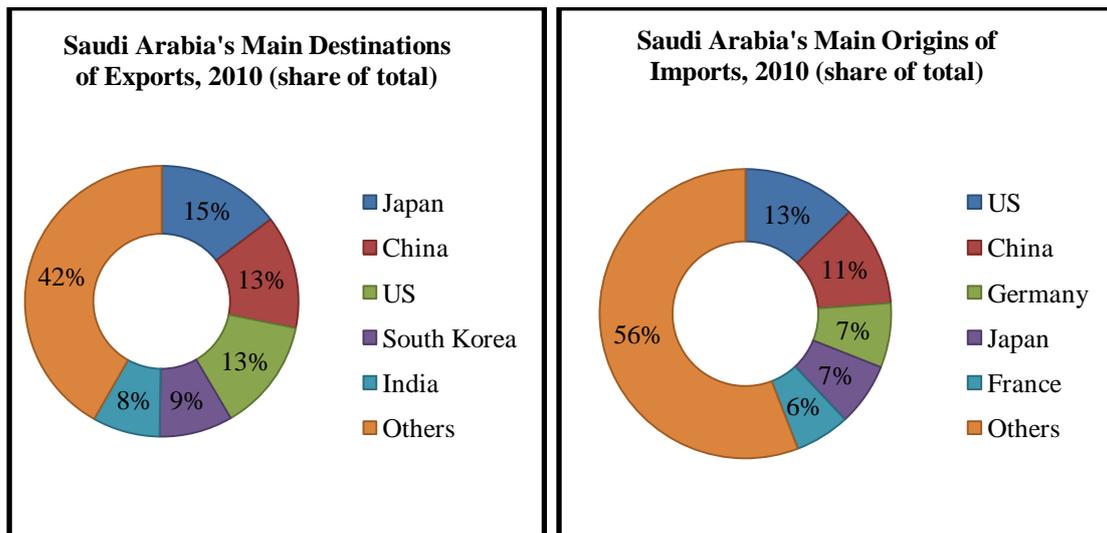
undermine U.S. objectives in the Middle East as long as it does not feel its economic interests are threatened. We have seen this in China's stance on many Middle Eastern crises such as Kuwait, Iraq, Bahrain, Sudan, the Iranian nuclear crisis, the Libyan conflict and even in Saudi Arabia. The main point of controversy between China and the United States in the Gulf region is certainly Iran. While it is in China's economic interest to see a strong Iranian regime that can provide it with long-term energy, China has gradually weakened its support for Iran culminating in its June 2010 UN vote to support a resolution imposing a new round of sanctions on Iran for continuing its uranium enrichment program. The change in the Chinese stance is because they realise that the proliferation of nuclear weapons is not beneficial for China and is also counterproductive towards Middle East stability and security. Somewhat ironically, the United States is now said to be urging Saudi Arabia and others to step up oil and gas exports to China in order to undercut Chinese dependence on Iran, (Freeman, 2009).

While some analysts in China and the U.S. may believe that it may not be possible for China and the United States to work together, there are indications that state otherwise. In the public levels, polls by the Pew Global Research Center in July 2011 indicate that 51 percent of Americans still have a generally favourable view of China, while about 44 percent of the Chinese people have a generally favourable view of the U.S., (Pew Global Research Centre, July 13, 2011). The two countries instituted the China-U.S. Strategic and Economic Dialogues mechanism. China and the United States have carried out practical cooperation in a wide range of areas including economy and trade, energy, the environment, counter-terrorism, law enforcement and culture. The two countries have maintained close contact and coordination in dealing

with major international and regional hotspot issues and addressing global challenges, such as climate change and the international financial crisis. The strategic significance and global impact of China-U.S. relations have been on the rise, (*The Washington Post*, 16 January, 2011).

Politically, China and the United States still share a wide range of common interests. These include promoting the peace process in the Middle East, bringing to an end the Palestinian–Israeli conflict and stabilising the Iraqi situation, (Li, 2009). The two countries also share a need for cooperation in areas such as counter-terrorism and WMD and missile technology non-proliferation efforts which are crucial to maintaining regional stability in the Middle East, (Rachel, 2006: 312). Above all, both countries share a deep interest in regional stability and the free flow of energy, (Alterman & Garver, 2008). The interruption of energy supplies is not in the interest of either country, and on this front there is considerable room for Sino-American cooperation, (Wehrey, 2010: 62). This view is shared by John Sfakianakis who believes that is a noticeable shift in trading flows and that this, in itself, is offering economic alternatives to Saudi Arabia. However, he argues that the relationship should not be seen as a shift in Saudi Arabia’s politico-military direction, (Sfakianakis, 2009).

(Figure 10.2.3.1): China and the U.S. Highly Interdependent with Saudi Arabia



Source: Economist Intelligence Unit, (July, 2011)

Yitzhak Shichor goes further to suggest that giving the highest priority to economic relations may, in fact, constrain China's political options. Moreover, China's integration into the international economy subordinates the Chinese to a variety of norms, regulations, and rules that limit their room to manoeuvre, (Shichor, 2006). Nawaf Obaid, a Saudi expert who has insight in this issue, argues that Chinese dependence on Saudi Arabia for its energy needs will not present any direct threat to U.S. national interests, (Obaid, 2002). In general Chinese reliance on foreign oil will lead to its deeper integration into the global economy, (Ibid).

While China has sought to expand its footprint in the region and become more proactive in ensuring its access to Middle East markets and share of the region's oil and gas, this expansion of China's role in regional affairs is likely to proceed gradually and remain focused on the economic dimension, (Wehrey, 2010: 56). It seems that the Chinese are aware of these equations as well. In this regard, Xia

Yishan, a researcher specialising in China's energy strategy at the China Institute of International Studies, argues that: "China's influence in the Middle East should be estimated realistically. It is just an active participant in the redistribution of international resources. The U.S. position in the Middle East won't change in a very long period. In the Middle East, China should focus on economic relations and endeavor to boost its cooperation with multinational oil companies. Chinese companies should change their usual practice of seeking oil alone, and instead look for ways of sharing risks", (Chen and Huang, 2011). Li Guofu goes in the same direction to say: "At present, whether we like it or not, the United States is the most dominant outside power in the region and it has broad regional interests in the Middle East. We have made it clear to the United States that China's policy of strengthening its relationships within the region is neither aimed at undermining U.S. regional interests nor aimed at challenging the U.S.'s dominant position", (Li, 2009). China might not be comfortable accepting a "free ride" on American military protection. But, at least for the time being, it has no alternatives, (Obaid, 2002).

In the energy realm, China and the United States are the two biggest players on the international energy markets and will retain their positions as the world's largest oil importers far into the future, (Lieberthal & Herberg, 2006: 42). Both countries also face similar serious energy challenges: increasing dependence on foreign sources of energy, high energy prices, and increased environmental degradation caused by the rise in energy use, (Medeiros, 2009). The two countries also share enormous interests in maintaining overall supply security and price stability, two goals that are well served by far greater and more effective bilateral and multilateral cooperation, (Lieberthal & Herberg, 2006).

As the two largest consumers of oil worldwide, the U.S. and China share common interests: avoiding disruption to global energy supplies, ensuring political stability in key oil producer regions, accelerating the development of alternative energy sources, limiting domestic consumption, increasing energy efficiency, creating greater transit and fuel flexibility, and reducing the environmental impacts of fossil fuel consumption. Beijing and Washington should seek to ameliorate differences on tense energy issues. Although dialogues on energy security conceptualisations and policy preferences are positive, they must move beyond talking toward a true partnership that can confront the common challenges they face as importers, (Zha & Hu, 2007). Chinese Premier Wen Jiabao, in his address at the Copenhagen climate change summit (Copenhagen, December 18, 2009) argued that both Beijing and Washington have begun work to increase the use of clean energy as well as to develop new energy sources. Though China is arguably the world's largest greenhouse gas emitter, it also ranks first in the installation of hydroelectric power capacity, nuclear power capacity under construction, the coverage of solar water panels, and photovoltaic power capacity, (Jiabao, 2009). Meanwhile, since Obama entered office, the United States has become more active in developing its green economy. The two countries have also agreed to cooperate in a wide range of areas related to energy and the environment.²⁰

Within this context some specific measures can build mutual trust while reducing the risk of U.S.-China conflict over oil. Firstly, China should be engaged in multilateral energy institutions such as the International Energy Agency (IEA). In order to foster

²⁰ See the Memorandum of Understanding to Enhance Cooperation on Climate Change, Energy, and Environment between the Government of the United States of America and the Government of the People's Republic of China, available on: [<http://www.state.gov/documents/organisation/126802.pdf>.]

more Sino-U.S. dialogue on energy security and to coordinate international energy security policies with China's policies, the United States should support China's admission into the International Energy Agency (IEA). As long as China is not part of the IEA, Chinese energy security policies may continue to pose a challenge to the western nations' efforts on energy security, (Leverett & Bader, 2005/2006). A sensible and prudent approach would start by ensuring that the market has as much information about supply and demand as possible. More reliable data would dampen short-term volatility by reducing uncertainty and facilitating timely investments in production capacity, limiting the amplitude of price extremes over the long term, (Robert & Michael, 2011). The Chinese Government has been particularly reluctant to participate in such arrangements so far. But, as its oil consumption balloons, China increasingly stands to gain from stamping down volatility, too, (Ibid). Nobuo Tanaka, Executive Director of the IEA, recently told the *Financial Times*: "Our relevance is under question because half of the energy consumption is already in non-Organisation of Economic Cooperation and Development (OECD) countries. And for oil it is soon coming that the majority of consumption is happening in non-OECD countries, (Hoyos, 2010)... In many ways they [the Chinese] are already working closely with us. But eventually we wish they would join us...For the sake of transparency, we need their help", (Ibid).

Chinese coordination with the IEA and participation in its various activities could prove to be very important in the event of future oil supply uncertainty on the international markets, (Lieberthal & Herberg, 2006: 33). The United States expressed support for China to join the organisation as a non-OECD member, but to date, however, China has not sought to join. Beijing remains uncomfortable with

international energy markets and institutions, and it would prefer not to rely so heavily on other countries to secure the sea lines of communication on which it depends, (Stanway, 2011). Beijing has been wary of joining multilateral organisations it sees as being controlled by rich developed countries, particularly the U.S., (Hoyos, 2010).

China has been relatively slow to give out critical oil market data, but it is beginning to work more closely with the IEA and the IEF, which collects data from both producers and consumers. Yet, the IEA on its “Medium-Term Oil & Gas Markets 2011” noted that at the international level, policy is moving in the right direction but moving too slowly. Multilateral forums like IEA, the International Energy Forum, and the G-20 all have oil market transparency squarely on the agenda. IEA has also stepped up its bilateral engagement, working with China’s National Energy Administration to improve the quality of Chinese energy statistics and forecasting, (IEA, medium-term oil & gas markets 2011). Mid-ranking Chinese officials have been allowed to attend IEA committee meetings on issues such as the energy security dialogue and energy technologies. They have also attended meetings on more sensitive subjects, such as emergency response and long-term policy planning, (Hoyos, 2010). Meanwhile, China’s ministry of science and technology is translating much of the IEA’s work into Chinese and the IEA itself has a Chinese version of its website, (Ibid).

Furthermore, the so-called “Arab Spring” of 2011 and its aftermath have provided a reminder that global events are unpredictable and play a vital role in shaping the direction of the oil market and highlight the need of cooperation. That cooperation

between China and the International Energy Agency was demonstrated on June 2011 when the IEA consulted China before it authorised the release of 60 million barrels of its emergency reserves in June 2011, (Ma, 2011), in response to the ongoing disruption of oil supplies from Libya to ensure that adequate supplies of oil were available to the global market, (IEA, June 2011). In a statement released after the IEA action China's National Energy Administration (NEA) said that, "China appreciates and supports the International Energy Agency's (IEA) decision to release strategic oil reserves to ease supply disruptions in Libya...The IEA's move will increase the global supply of crude oil and help to stabilise prices", (Xinhua, June 24, 2011).

Although IEA officials do not expect Chinese membership overnight, they do believe it could be possible within the next five years. In this regard, IEA's Executive Director believes that China eventually will join and he cites five reasons why closer co-operation with the IEA would be beneficial: (a) Enhanced energy security through support from IEA partners as well as coordination during major disruptions in the supply of oil; (b) Participation in a community which is influential in shaping future energy security and sustainability on a global level; (c) Participation in open discussions relating to technology policy and better access to state-of-the-art technologies themselves; (d) The opportunity to learn and benefit from best practices of other countries in areas such as statistics or energy efficiency; and (e) The chance to demonstrate to the world that China is reaching the point of development where it can confidently engage alongside other developed economies in areas of global importance, (Tanaka, 2011).

Additionally, Stanway urges that Washington should reinvigorate efforts to draw the new major oil-consuming states, such as China, into coordinating their policies on strategic reserves. China is finally building strategic reserves and a report issued by the China National Petroleum Corp's research unit showed that China's total storage capacity reached 24.38 million tonnes (178 million barrels) by the end of 2010, suggesting that 76 million barrels of the project's second phase has now been built, (Stanway, 2011). This development should share the burden of responding to disruptions with the United States and others. A coordinated policy would make the world better able to respond to supply disruptions and thus limit unnecessary price swings, (McNally & Michael, 2011).

Secondly, encourage Chinese energy efficiency and environmental protection. China will aggressively pursue clean energy policies for the foreseeable future, driven mostly by the desire to reduce its dependence on overseas energy supplies. China is working to reduce its economy's "energy intensity" as the Chinese Government has committed to reducing its carbon intensity reduction target. China's 12th 5-Year Plan (2011-2015) has set targets to further reduce energy intensity by 16 percent by 2015. Along with measures to reduce pollution and increase the shares of non-fossil fuels in the energy sector, China has set goals to improve its CO₂ intensity by 40-45 percent by 2020, with an interim target in the 12th 5-Year Plan of 17 percent by 2015, (The China Greentech Initiative, 2011: 24). According to the recent report published by McKinsey & Company titled, "China's green revolution: Prioritizing technologies to achieve energy and environmental sustainability", China could build a "green economy" and emerge as a global leader in clean energy technologies during the next two decades, (McKinsey & Company, 2009: 10). By investing in technologies

commercially available today, China could reduce its projected oil imports by up to 30 to 40 percent, cut demand for coal by 40 percent, and reduce greenhouse gases by up to 50 percent throughout to 2030. China could also emerge as a global leader in green technologies such as electric vehicles, (Ibid).

Daniel Kammen, the chief technical specialist for renewable energy and energy efficiency at the World Bank Group, noted that quiet cooperation between China and America does exist, in the form of decades of joint work on energy efficiency standards, (Kammen, 2011). That cooperation reached its peak in November 2009, when U.S President Barack Obama and Chinese President Jintao Hu announced seven new U.S.-China clean energy initiatives during their Beijing summit: (A) U.S.-China Clean Energy Research Center; (b) Electric Vehicles Initiative; (c) Energy efficiency action plan; (d) Renewable Energy Partnership; (e) 21st century coal; (F) Shale gas (produced from shale) resource initiative; and (g) Energy cooperation program. All of these initiatives work on cooperation projects in renewable energy, developing electric cars, smart grid, clean transportation, green building, clean coal, combined heat and power, and energy efficiency, (DOE, January 2011). The seven areas of cooperation are also within the U.S.-China Framework for the ten year cooperation on energy and environment within the U.S.-China Strategic and Economic Dialogue, (S & ED) (DOE, June 2011).

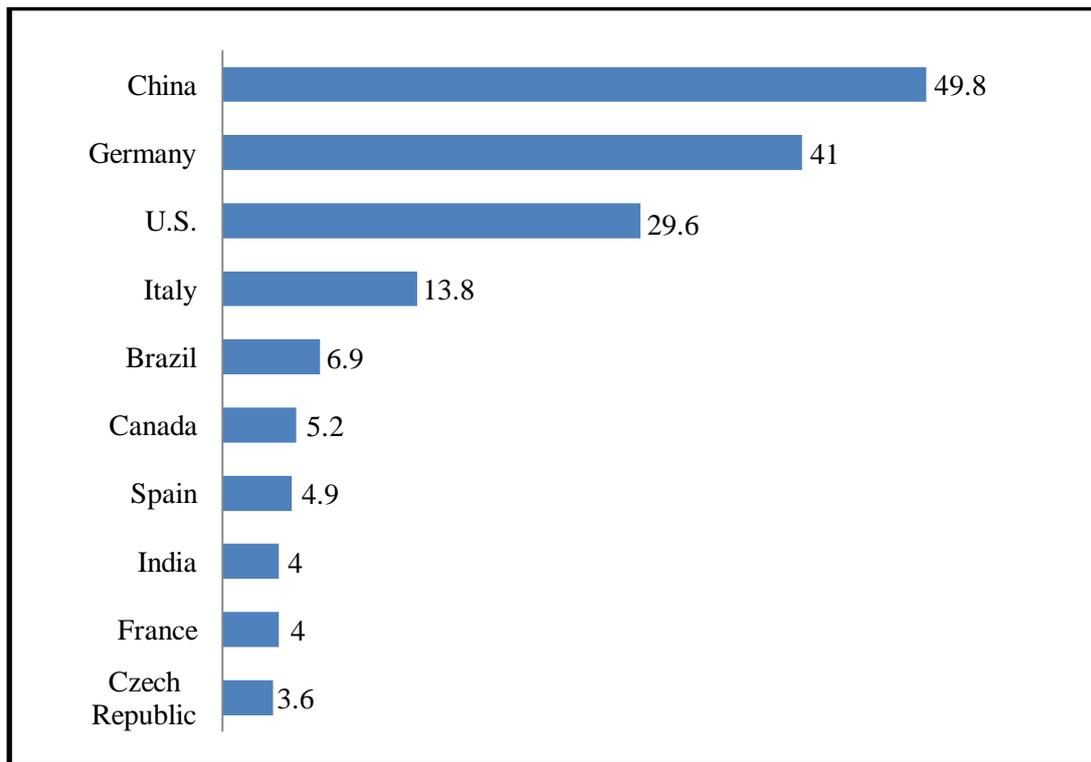
There is no doubt that this cooperation will enhance energy security in both countries. And, of course, will open a huge market for clean energy, which will provide enormous economic opportunities for U.S. companies. About 70 percent of China's energy and 80 percent of its electricity come from coal. The U.S., too, is dependent on

coal, 49 percent of its electricity in 2010 came from coal, and both countries import more than 50 percent of their total oil consumption, (Kammen, 2011). Additionally both nations have made clean energy investment central to national energy strategies and the two countries need each other in order to build a clean energy economy for the 21st century, (Ibid). In short, this situation will provide both countries with strong incentives to cooperate in energy and other issues. China Greentech Initiative estimated that China's addressable "green-tech market" could reach US\$500 billion to US\$1 trillion by 2013, (The China Greentech Initiative, 2011: 24). In this regard, the United States Secretary of Energy, Steven Chu, wrote on January 2011 in the introduction of the progress report by the U.S. Department of Energy titled, "U.S.-China Clean Energy Cooperation" in which he summarised the cooperation between China and the United States and stated U.S.'s in a very pragmatic way:

"... As the world's largest producers and consumers of energy, the United States and China share many common challenges and common interests. Our clean energy partnership with China can help boost America's exports, creating jobs here at home, and ensure that our country remains at the forefront of technology innovation. At the U.S. Department of Energy, we are committed to working with Chinese partners to promote a sustainable energy future. Working together, we can accomplish more than acting alone." (DOE, 2011)

China is already the world's largest investor in the renewable energy sector and emerging as the world's clean energy powerhouse. For the first time, China took the top spot for overall clean energy finance and investment in 2010, (UNEP, 2011: 5). According to the United Nations Environment Programme (UNEP), "Global Trends in Renew Energy Investment 2011", the world invested in 2010 a record US\$211 billion in renewable energy. It was boosted in particular by wind farm development in China and small-scale solar PV installation on rooftops in Europe. China's total of US\$48.9 billion dwarfed all other countries, accounting for more than two-thirds of the developing countries total and more than a third of the global total. (UNEP, 2011:11-12 & 18), (See Figure 10.4.1).

(Figure 10.2.3.2) Top 10 in Renewable Energy Investments, (2010, US\$ bn)



Source: Bloomberg New Energy Finance, UNEP (2011)

In the military realm, the military relations between the two countries are weak, meaning they are often the first and the most affected when the China-U.S. relations experience ups and downs, (*People's Daily Online*, July 14, 2011). Regular contact has been suspended a number of times over the past two decades and each new cancellation sparks a round of worrying over the causes of the rift, (Auslin, 2011). Schiffer Michael, U.S. Deputy Assistant Secretary of Defence for East Asia, argues that the military-to-military relationship remains among the least developed parts of the U.S.-China relationship. The U.S. Congress sought to limit the scope of the military relationship in the National Defence Authorization Act for Fiscal Year 2000 (P.L. 106-65), when it barred exchanges or contacts with China that include “inappropriate exposure” to a range of subjects, including surveillance and

reconnaissance operations and arms sales, (Schiffer, 2011). The U.S.-China relations also remain dogged by long-standing mutual mistrust. For the United States, points of friction included China's currency and industrial policies; its reluctance to condemn a series of North Korean provocations; its expansive claims to disputed territory in the South China Sea; and its ongoing suppression of domestic dissent, (Lawrence & Lum, 2011). For China, points of friction include U.S. arms sales to Taiwan; the American President's meeting with Tibet's exiled spiritual leader, the Dalai Lama; U.S. joint military exercises with South Korea in the Yellow Sea; and the U.S. declaration of a "national interest" in the freedom of navigation in the South China Sea, (Ibid).

Yet, Obama's Administration has pushed hard for a Chinese commitment to a "reliable and sustained" military relationship, arguing that, "The on-again-off-again cycle that has all too often characterised the military-to-military relationship increases the risks and dangers of an incident or accident that could derail the overall bilateral relationship", (Michael, 2011). U.S. President Barack Obama and Chinese President Jintao Hu decided during a 2009 presidential summit in Beijing to advance and sustain military-to-military relationships. China abruptly cut off military exchanges after the United States announced arms sales to Taiwan in January 2010, (Miles, 2011). But China-U.S. relations have rebounded thanks to joint efforts from both sides, (*People's Daily Online*, July 14, 2011). The Obama Administration's decision to open up some sensitive military installations can be interpreted as a sign of goodwill towards China as well as reciprocation of China's gesture to open up its own military bases, such as the PLA Second Artillery Command Post, to the U.S., (Teng, 2011). Additionally, Admiral Mike Mullen, Chairman of the U.S. Joint Chiefs of

Staff, recently visited China in January, 2011. This visit is a response to top Chinese General Chen Bingde's earlier visit to the Washington, (Miles, 2011).

Within this context, the then-U.S. Defence Secretary Robert M. Gates believes that, "Military-to-military contacts between U.S. and China contributes, not only to greater understanding, but contributes to avoiding miscalculations and misunderstandings and miscommunications", (Garamone, 2011). Gates is hoping that a system of regular contact between the U.S. and Chinese defence officials can help avoid an arms race, increase transparency, reduce suspicion, and eases the pressure that would otherwise push for greater military preparation on both sides, (Haddick, 2011). While Admiral Mike Mullen, Chairman of the U.S. Joint Chiefs of Staff, regards the American military ties with China as "absolutely vital", (Bloomberg, July 10, 2011). He offers "three tones" for both nations to build on as they renew their military relationship to complement cooperation being seen in political and economic channels, (Miles, 2011). First, both the United States and China must "work from a posture of mutual respect", recognising each others' strengths and achievements. Secondly, both the United States and China must recognise that local issues that impact Asia and the Pacific often have global implications. Finally, the two nations should look "to the future, not to the past", (Ibid).

Many policy makers in Washington may be opposed to this approach because closer coordination between the United States and China will force the United States to acknowledge Chinese economic, military, and political interests. These policy makers may view this as a decrease in U.S. power and influence in the Middle East, which may be the case. But other options would likely cause an even larger decline in U.S.

power and influence. Working against or ignoring Chinese interests will only embolden China to undermine U.S. efforts in the Middle East even further. On the other hand, China's Minister of Defence General Liang Guanglie suggested that any future Taiwan arms sales could again disrupt the relationship. During a joint press conference with the then U.S. Secretary in Beijing in January, 2011, Liang stated that, "The United States arms sales to Taiwan seriously damaged China's core interests and we do not want to see that happen again; neither do we hope that the U.S. arms sales to Taiwan will again further disrupt our bilateral and military-to-military relationship", (U.S. Department of Defence, January 10, 2011).

While some analysts may believe that it may not be possible for China and the United States to work together, there are indications that state otherwise. China and the United States have shown that they can work together towards mutual objectives with their handling of the Taiwan issue, the North Korean nuclear crisis, Iraq's post-invasion energy sector development, Iran's UN sanctions, Libyan conflict and the independence of South Sudan. Through intensive dialogue and cooperation, China and the United States were able to overcome their differences peacefully. The foundation to increase Sino-U.S. dialogue and cooperation exists. The question is whether the United States and China will take advantage of the situation. Chinese scholar Jianqun Teng argues that relatively stable security relations between China and the U.S. will endure for a while. With the U.S. presidential election just around the corner, Obama needs to score diplomatic points while trying to avoid losing points for issues like North Korea's nuclear program. There's not much room for the U.S. to show off its talents in northeast Asia and keeping China close will reinforce Obama's image. On a deeper level, with China and the U.S. becoming more and more

interdependent, direct confrontation benefits no one, (Teng, 2011). Teng suggests several reasons for his optimism and these can be summarised as follows: (a) Political relations between the two countries have gradually improved and developed, and the deepening of dialogue on security issues has guaranteed the smooth development of China-U.S. military exchanges; (b) China's capabilities have been greatly enhanced especially in the last decade, along with the strengthening of its military power, and this has led the U.S. to pay close attention to China's military development; and (c) Although the U.S. has adopted aggressive policies in the Asia-Pacific region, its fundamental interest still lies in maintaining stability in the region instead of sparking off conflicts or causing direct confrontations, (Ibid).

Finally, Yan Xuetong, Director of Tsinghua University's Institute of International Studies, sums up the U.S.-China relations in very interesting words: "Despite the interdependence and the mutual benefits, many in both countries remain deeply suspicious of each other's intentions...At this point no one can say China and the United States are friends. It's better to say we are competitors, like McDonald's and Burger King are competitors...McDonald's wants to open more shops, not destroy Burger King and in the process destroy itself. Why would we be so silly as to hurt ourselves? (Richburg, 2009)

10.3 IMPLICATIONS FOR THE MAJOR ASIAN POWERS

The centre of gravity of international relations is decisively shifting towards Asia. In such a scenario, the rise of China and India is taken for granted. The rapid economic rise of the two countries—each with a population of more than a billion—has contributed to the notion of ‘Chindia’ in popular imagination, (Holslag, 2010). The current great and emerging powers of the world, including the United States, China, India, Japan, and the European Union, all vie for natural resources from the Middle East. China, India and to less extent the United States are the main powers that seek to secure oil and natural gas from the region to fuel their economies, (Gresh, 2010). China is currently the second- largest economy in the world, while India will likely surpass Japan in the next decade to become the second-largest economy in Asia (and the third in world).

Consequently, the geopolitical landscape of the world’s energy demand and supply has changed. First, most consumers in the West are starting to view —greenll sources of energy in a more favourable light than the fossil fuels that have hitherto largely powered the industrialised world, (Hoyos, 2010). Second, and perhaps more importantly, the oil market, is facing a significant shift in demand from West to East. Demand from the customers which Saudi Arabia has supplied for the past 50 years is stagnating, as market saturation and environmental policies move the U.S. and Europe away from oil. However, energy-hungry Asian nations, such as India and particularly China, are taking their place, refocusing the country’s attention eastward, (Ibid). Indeed, the Asia Pacific region was importing an average 18 (mb/d) in 2010. This total rises to an estimated 22 (mb/d) in 2015, (BMI, 2011:14) and could reach over 30

(mb/d) in 2030, (EIA, 2011). The principal importers will be China, India, Japan and South Korea, (BMI, 2011:14).

Japan continued to be one of the biggest importers of petroleum from Saudi Arabia and the Middle East. According to EIA, Japan consumed 4.4 (mb/d) of oil in 2010, making it the third largest petroleum consumer in the world, behind the United States and China. However, oil demand in Japan has been declining since 2005. This decline stems from structural factors, such as fuel substitution, an aging population, and government-mandated energy efficiency targets, (EIA, Japan: Country Analysis Briefs, 2011). In the medium and long terms, Japan's total oil consumptions and imports will continue to be flat or decline, (see tables Table 10.2.1 & 10.2.2). Overall, though, Japan is unlikely to become a major military power given its colossal fiscal and debt burdens (which reduce the scope for a bigger defence budget) and a lack of public support for such a role. In the event of intensified Sino-Indian rivalry in the Indian Ocean, most projections expect Japan to be sympathetic to India and the US, but Tokyo cannot afford to antagonise Beijing, given that China is now Japan's top trade partner, (BMI, Pakistan Defence & Security Report, 2010:50).

But Japan's strategic relationship with the US remains a central pillar of its foreign policy. Despite the growing debate within Japan between those (in a minority) that want foreign policy to focus on improving ties with China, owing to its growing diplomatic and economic weight, and those that view China's rise as a threat that should encourage Japan to remain close to the US, (EIU, Country Report: Japan, January, 2011:5). Japan needs to sustain the alliance with the US, on which it is

dependent for its military security; and this requires it to accommodate US demands, (Miyagi, 2011).

Meanwhile, South Korea's oil consumption has remained relatively steady over the past decade and will continue in the same direction in the next two decades, (see tables Table 10.2.1 & 10.2.2). South Korea imported over 2.2 (mb/d) of total oil in 2010, and was the world's sixth largest crude oil importer in 2010. South Korea is highly dependent on the Middle East for its oil supply, with the Arabian Gulf accounting for nearly 75 percent of its 2010 total oil imports. Saudi Arabia was the leading supplier, and the source of more than a quarter of total oil imports, (EIA, South Korea: Country Analysis Briefs, 2011). Since the 1950s, Seoul's foreign policy has been driven principally by deterrence and defense requirements vis-à-vis North Korea, (Min, 2011:160). While South Korea's immediate defence concerns will naturally focus on North Korea, the government is looking beyond the threat from Pyongyang and is seeking greater naval capabilities. Seoul has joined anti-piracy activities, and many experts expect South Korea to increase its naval capabilities along the route to the Arabian Gulf. However, it is probably too weak to exert influence independently, (BMI, South Korea, 2010:50). South Korea will seek to maintain warm relations with the US. Both countries recognise the importance of their strategic partnership in the political and economic arenas. This will be strengthened now that their respective legislatures have finally ratified the South Korea-US bilateral free-trade agreement (FTA), which was signed in 2007, (EIU, Country Report: Japan, January, 2011:6).

(Table 10.3.1): Asia Pacific Oil Consumption, Production and Imports, (selected countries 2010-2015)

		Projections					
		2010	2011	2012	2013	2014	2015
China	Consumption	8.907	9.426	9.945	10.392	10.829	11.235
	production	4.076	4.079	4.089	4.114	4.135	4.112
	Imports	4.831	5.347	5.856	6.287	6.694	7.123
India	Consumption	3.315	3.450	3.610	3.818	4.038	4.265
	production	0.910	1.035	1.095	1.150	0.940	0.925
	Imports	2.405	2.415	2.515	2.668	3.098	3.340
Japan	Consumption	4.422	4.188	4.138	4.088	4.088	4.113
	production	0.017	0.017	0.017	0.017	0.015	0.015
	Imports	4.405	4.171	4.121	4.171	4.073	4.098
South Korea	Consumption	2.249	2.267	2.293	2.315	2.335	2.351
	production	0.015	0.015	0.015	0.015	0.015	0.015
	Imports	2.234	2.252	2.278	2.300	2.320	2.336

Source: All figures adapted and calculated by the author from (BMI, 2011)

In this context, China and India are seen as racing ahead in terms of explosive economic growth, as competitors over energy markets and increasingly indispensable pillars of regional stability, (Bidawai, 2010). China and India are expected to remain as the twin engines of global oil demand growth over the next two decade on the back of strong economic growth. The numbers behind China and India's seemingly insatiable thirst for energy are mind-boggling. For example, Chinese demand for petroleum reached over 9 million barrels per day in 2010, and is projected to jump to around 16.4 billion barrels in 2030. Although China has massively increased its refining capacity to meet most of its current and projected needs, the estimate is that China will still need to import over 12 million barrels of crude oil in 2030, up from 4.8 million barrels currently. This means 70 percent to 80 percent of China's crude oil needs will be from imports, (Annual Energy Outlook 2011). The numbers for India are smaller but still overwhelming. India consumes 3.3 million barrels per day, two-thirds

of them imported. According to EIA analysis of projected trends, India will eventually be importing around 6-7 million barrels per day, roughly 90 percent of its future petroleum needs, (Ibid).

(Table 10.3.2): Liquids Consumption by Selected Country, (2015-2035, mb/d)

	Projections, (Reference case)				
	2015	2020	2025	2030	2035
U.S	20.4	20.7	21.0	21.4	21.9
China	12.1	13.6	15.6	16.4	16.9
Japan	4.3	4.6	4.7	4.6	4.5
India	3.8	4.6	5.7	6.8	7.5
South Korea	2.3	2.4	2.4	2.5	2.6
Total World	93.3	97.6	103.2	108.0	112.2

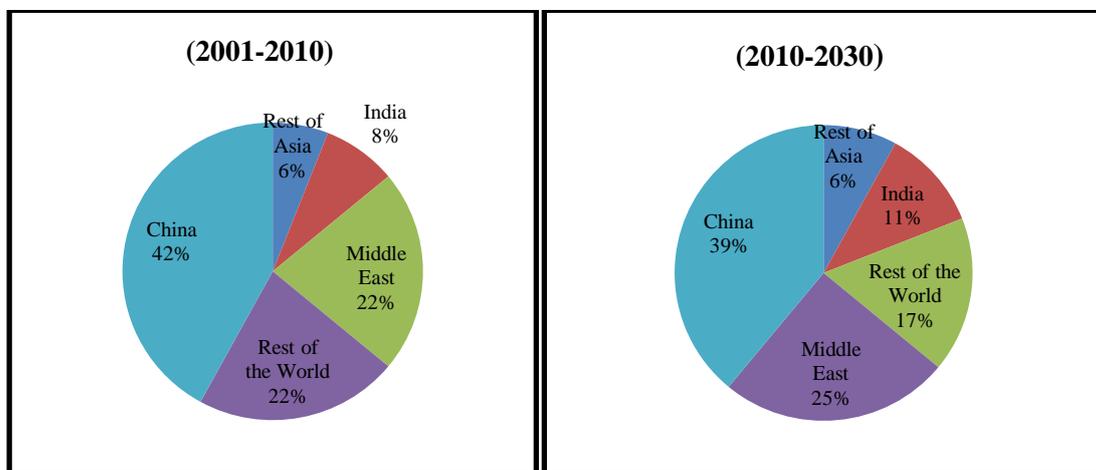
Note: Conventional liquids include crude oil and lease condensates natural gas plant liquids
Source: EIA, Annual Energy Outlook 2011

As a result, the realists argue that geopolitics dominates the Sino-India relationship, (Scott, 2008). China's relationship with Pakistan, and forays in the Indian Ocean Region, are seen as encirclement strategies, prompting India's Look East policy. This competition is accentuated due to the increasing energy demands in both countries, (Garver, 2001:447). On the other hands Liberals predict that the imperative for economic development will propel India and China towards peace, (Guihong, 2005). The liberals feel that India and China's economies have advantages in different sectors, thus they are complementary, (Frazier, 2004). This theory sees greater convergence between India and China on issues relating to global economic governance and views the border conflict as a legacy of the past, (Emmott, 2009:315).

Though India's relations with China have improved considerably in the last few years, this relationship remains by and large competitive, if not in outright conflict. This is

particularly true with the competition for global energy resources, (Pant, 2011) Moreover, India’s aspirations to emerge as a major global power may also lead it to counter China’s growing influence around the globe, (Ibid), and rivalry for regional and global influence, (Sujit, 2011). In this context, Jonathan Holslag the Head of Research at the Brussels Institute of Contemporary China Studies in his recent book *China and India: Prospects for Peace* argues that between China and India is economic competition and rivalries. Holslag gives four main reasons for his scepticism. Firstly, economic complementarities between India and China will disappear once India begins to challenge China in manufacturing and China competes with India in IT and services. Cooperation will then be replaced by economic competition and rivalries, (Holslag, 2010:168). Secondly, public perception in both countries is characterised by acute mutual suspicion. This will constrain the political leadership from having a cooperative relationship, (Ibid). Thirdly, ‘trade and mutual economic gains have not neutralised the military-security dilemma’. There has been no breakthrough in the border dispute. Finally, the two countries are increasingly vying for influence in the South Asian neighbourhood and in the Indian Ocean, (Ibid).

(Figure 10.3.1): Share of Global Incremental Oil demands, (2001-2030)



Source: Facts Global Energy, (2011)

India from its part is worried by Chinese territorial claims on vastly-populated regions of India, (Sujit, 2011). The Indian security community also worried about China's military build-up in areas close to the Indian borders. India, long suspicious of China's close relations and military support for Pakistan, views an increased Chinese presence in northern Pakistan and expanded civil nuclear cooperation between Beijing and Islamabad as particularly worrisome, (Curtis & Cheng, 2011). Indian military strategists believe they must plan for the possibility of a two-front war with Pakistan and China even as they actively seek dialogues with both to diminish the chances of such a dire scenario, (Ibid). Indian military strategists also believe that Chinese naval ties with Pakistan, Sri Lanka, Bangladesh, and Myanmar are one source of concern for India, (Ciorciari, 2011). China's bases or installations in those countries threaten to encircle India with a Chinese "string of pearls"-points from which China can exert naval influence along the Asian littoral from the Straits of Malacca to the Middle East, (Ibid). In this regard, while China's naval capabilities focus primarily on deterring US intervention in a conflict in the Taiwan Strait, from an Indian perspective they could be used over the long term to expand China's sea-denial capabilities in other regions, including the Strait of Malacca and the Indian Ocean, (Bajpae, 2010). Additionally, China is also set to emerge as a "manufacturing threat" to India. China is emerging as a "slow killer" for India's domestic manufacturing industry through cheap imports that are not able to compete with Chinese imports on cost factor, (Kumar, 2011).

On the other hand, from the viewpoint of China, the Indian rapprochement with the United States may lead to a broader alliance in the future may include Japan, South Korea and perhaps other countries to counter China. The US's strategic outreach to

India from 2000 is seen as a move by America to gain a new regional ally with which to jointly contain China, (BMI, Pakistan Defence & Security Report, 2010:47). China has been concerned with its ocean-going navy being small compared to other major powers like the United States, Japan or India which dominate the Indian Ocean, especially at the mouth of the Strait of Malacca choke-point (Zweig and Jianhai, 2005: 34). Furthermore, the Chinese security community is worried at the adverse strategic implications of the Indo-US nuclear deal, which is perceived as bringing India and the US together against the Chinese. At the same time, Chinese assessments of Indian military planning suggest a view in Beijing that New Delhi sees China as a major threat. One Chinese assessment concludes that the Indian military sees Pakistan as the main operational opponent and China as a *potential* operational opponent. It also describes the Indians as seeing China and Pakistan as closely aligned in threatening India, (Curtis & Cheng, 2011).

To be sure, nations have long competed for finite energy and other resources. But Asia has not seen a powerful China and India since the 1600s. Their rapid modernization over the past three decades means energy competition is occurring on an unprecedented scale, (John & Charles, 2010). In this environment of uncertainty and security concerns, the Indian Ocean, through which raw materials from Africa and the Middle East regularly pass en route to China, is fast emerging as a potential zone of contention between China and India, (Singh, 2011). China and India are significant military powers, possessing small but growing arsenals of nuclear weapons and fielding two of the three largest militaries in the world, (Fravel, 2011:65). Given China and India's growing strategic interests in the Indian Ocean, through which 80 percent of Chinese and over 60 percent of Indian oil imports transit, each is likely to

perceive the other's naval modernization initiatives as inherently threatening, (Aiyar, 2011).

Yet, in both India and China, there is a realization that this is an important relationship, it has to be managed well, and if managed well it can bring huge economic and security gains. Indeed, the two countries over the last two decades or more have avoided developing a rivalry, notwithstanding significant differences over several issues. After all, both are developing countries with similar needs to improve the quality of life of their populations, including environmental improvement, (Dellios & Ferguso, 2011). Despite the rivalry between China and India, a Cold War-style confrontation, let alone a shooting war, is far from inevitable or even probable, and any tensions between the two could be reduced by promoting regional military cooperation by means of a NATO-like organisation that includes China, India, the US and other concerned powers, (BMI, Pakistan Defence & Security Report, 2010: 53).

India and China in recent years have expanded their functional cooperation in areas as diverse as science and technology, space, coal, renewable energy, water resources, forestry, agriculture, railways, culture, tourism, youth affairs, media and information, traditional medicine, labour, human resource development, auditing, anti-corruption and policing, (Ghoshal, 2011).

Growing economic interdependence and confidence building measures are likely to deter open hostilities over the short to medium term. On the economic front, in the past decade China and India have forged strong economic ties. Trade volume between the two countries rose from over US\$270 million in 1990 to US\$1.16 billion in 1995 and about US\$3 billion in 2000 to US\$43 billion in 2008, (IMF, December 2011).

Currently, China has emerged as India’s second-largest trading partner after the EU. Bilateral trade exceeded US\$61 billion in 2010 and in the first six months of 2011, bilateral trade amounted to US\$36.3 billion, a 44 percent increase over the same period in 2010, (Ibid). India has emerged as the 6th largest export market of China and 9th largest trade partner. China became the second largest trade partner of India, (Ibid). The ever-expanding trade between the two countries automatically gives them a huge stake in keeping co-operation alive, despite occasional hiccups.

(Table 10.3.3): Trade between China and India, (2000-2010)

	2000	2005	2006	2007	2008	2009	2010
Total Trade (US\$ billions)	2,91	18,71	25,05	38,69	51,85	43,40	61,73

Source: IMF, (DoTS, December 2011)

Politically, both states have common interests in combating terrorism and establishment of a multi-polar world order. China and India also maintained a relatively united front during the climate talks as neither wanted to be bound by an emissions regime, (Bagchi, 2010). India remains a staunch supporter of the “One China” policy and recognizes the People’s Republic of China on the mainland over the Republic of China authorities on Taiwan, (Bajpae, 2007). Most important of all, India is unlikely to join the U.S.-led alliance structure in Asia given New Delhi’s legacy of non-alignment, desire to maintain “strategic autonomy” in conducting its foreign policy, and an increasingly non-ideological foreign policy approach that seeks to promote trade and attract foreign investment to meet India’s development needs, (Ibid). India remains wary of being seen either as aligning or band-wagoning big powers and would be unable to join any power-driven multi-polar order. India instead feels more at home with norm and institution-driven multilateralism, (Singh, 2011).

Indeed, there is no guarantee that an Indo-US alliance, whether formal or informal, will emerge. Firstly, such cooperation would antagonise China, perhaps leading to a counter-alliance. Secondly, China and India are generally trying to improve relations, not to mention boost bilateral trade. Thirdly, an empowered India could in time conceivably challenge US interests in the region. With this in mind, it would make sense for the US to balance geopolitical power in the Indian Ocean, (BMI, Pakistan Defence & Security Report, 2010).

In the military sphere, although China has had an apparent head start in the new competition for the Indian Ocean, no major power is likely to achieve hegemony over the whole ocean. From a military point of view, China's "string of pearls" is far from assured, and even if Beijing were to develop bases in each "pearl", India is already taking counter-steps. Meanwhile, the US is still the only truly global naval power, and has considerably more maritime experience than China or India, which could take decades more development to match the United States. Furthermore, the US already has 11 aircraft carrier battle groups, whereas China and India combined are unlikely to field as many for decades to come, (Ibid, 2010:52). Most important of all, the international energy market is dependent upon secure and safe transport through global maritime shipping channels, (Ciorciari, 2011). The three major global maritime choke points (the Bab el- Mandeb Strait at the Gulf of Aden, the Strait of Hormuz at the Gulf of Oman, and the Strait of Malacca) all feed into the Indian Ocean, (BMI, Pakistan Defence & Security Report, 2010:39). The blockage of a chokepoint, even temporarily, can lead to significant increases in energy prices around the world. Additionally, maritime chokepoints leave oil tankers susceptible to pirate hijackings, terrorist attacks, and other hostilities, (Ciorciari, 2011). These factors are a recipe of

cooperation not conflict because it's in the interest of all oil consumers to keep the uninterrupted availability of energy sources at an affordable price. More important, till now, the US navy has ensured secure oil movement from and beyond the Gulf. India has been a free rider, getting oil security at no cost. China's presence in the region has until now been minimal, (Aiyar). It is unlikely the status quo will change soon or at least in the next two decades.

At the regional level, both countries are highly interdependent with Saudi Arabia and the Middle East. Both China and India have become more economically interdependent with the Middle East and the two countries will not be able to exclude each other from the region. As a big importer of natural resources, India, like China, will benefit from and may actively seek to promote stability in the Middle East and other resource-rich regions. Additionally, China and India have a high level of dependence on energy imports, particularly oil; they are exposed to the same risks of the international oil markets. Therefore it is in the interests of China and India to both cooperate together towards price stability and keeping reliable oil supplies. The Middle East oil producers export more oil to Asia than to Europe and North America combined. In fact, about two-thirds of GCC oil exports are channelled to the Asia Pacific market, (Calabrese, 2009). Asia Pacific countries, individually and collectively, are heavily dependent on oil from the Gulf. Japan sources roughly 80 percent, South Korea 75% and India imports almost two thirds of their oil from the GCC states, (EIA, 2011). The International Energy Agency (IEA) forecasts that China will import 70% of its oil from the GCC by 2015, (Ibid). India is projected to replace Japan and emerge as the third-largest consumer of energy (after the United States and

China) by that time. The bulk of Indian supplies come from the Gulf; this dependency is expected to change only marginally, (Ibid).

(Table 10.3.4): Oil Interdependence of Major Powers with the Middle East

Selected indicators, 2010							
	GCC		Middle East		Saudi Arabia		Saudi Position
	Trade Value (Billion US\$)	% oil ^a of total Trade ^b	Trade Value (Billion US\$)	% oil of total Trade ^c	Trade Value (billion US\$)	% oil of total Trade ^d	
U.S.	72,69	52%	149,59	34%	44,24	71.6%	3rd Oil Supplier
China	92,52	49.6%	171.40	40.1%	43,19	59.9%	Top Oil Supplier
Japan	122,63	82.7%	148,80	78.5%	42,45	83.5%	Top Oil Supplier
South Korea	78,96	81.5%	109,12	70.3%	31,32	82.7%	Top Oil Supplier
India	88,75	36.6%	119,45	39.6%	19,59	67,3%	Top Oil Supplier

Source: UN COMTRADE, (December, 2011)

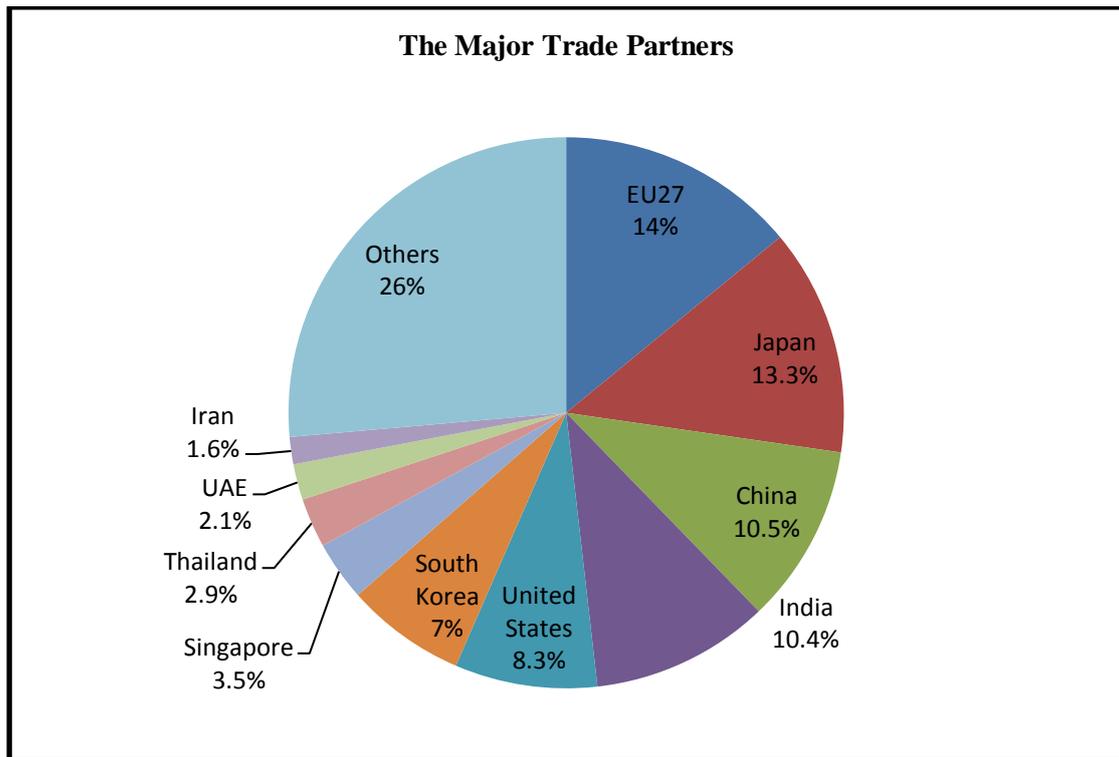
(a) Mineral fuels, oils, distillation products, etc

(b), (c) & (d) All figures were calculated by the author

In this geopolitical environment; China and India are acting in the economic interdependence model, and there is no evidence to suggest otherwise. Firstly, the two countries will depend on the import of large quantities of oil from the Middle East and Saudi Arabia; therefore, the stability of the region is in their interest. Secondly, Saudi Arabia and most of the Middle East countries do not allow investments in the upstream oil sector (exploration and production), thus there is no room for competition between Chinese and Indian firms. Thirdly, China and India do not yet (and maybe decades to come) have the capability to deploy significant naval forces in the Middle East and Indian Ocean and will remain dependent on the US presence. Fourthly, The Middle East countries depend on oil exports to sustain their economies, thus they will not encourage any party against the other in order to ensure stable

markets. Fifthly, the fight against terrorism and prevent the spread of nuclear weapons are also a common interest for all Asian countries and Middle East states. Finally, it is arguable that it is in the interests of both countries to enhance their collective leverage over energy suppliers.

(Figure 10.3.2): GCC Trade with Main Partners (2010)



Source: IMF (DoTS, December 2011)

In this context, common interests suggest that intense security competition between the two countries in the next decade is unlikely. Enhanced cooperation with a rising India allows Beijing to avoid a potentially costly confrontation that would harm the growth of both countries, block the formation of a close U.S.-India relationship, and reduce the overall influence of the U.S. over China, (Fravel, 2011:97). India, like China, needs a peaceful and stable security environment for its continued

development. Because of this focus on growth, they see India as inward-looking and thus as having strong incentives to avoid a confrontational relationship with China that would harm India's own growth prospects, (Ibid: 78)

Indrani Bagchi a leading foreign policy journalist and the Diplomatic Editor at The Times of India eloquently summarized the evolving Indo-China relationship as “competition on some levels and co-operation on others”, wherein some discomfort, ambivalence and hedging will always remain, despite the level of engagement, (Bagchi, 2010). Indeed, China's strategy toward a rising India combines engagement with deterrence. China pursues comprehensive political, economic, and international engagement with India to advance its broader strategic objectives. China also seeks to deter India from undermining Chinese interests by withholding cooperation or maintaining its policies on specific issues, such as its ties with Pakistan, (Tellis, 2011:6). Correspondingly, India has adopted a prudent dual strategy, reaching out to China to reap the benefits of trade and diplomatic engagement while hedging and balancing China by striking strategic partnerships with Japan and the United States, deepening ties with Western Europe and Southeast Asia, and keeping up ties with Russia, (Ibid).

10.4 CONCLUSION

This chapter has shown that China is acting in interdependence environments: (a) China is weak militarily in the Middle East and the U.S. will be the dominant power for the foreseeable future; (b) China is highly economically interdependent with the United States; (c) China, India, Japan, South Korea and the U.S. are also highly economically interdependent with Saudi Arabia and the Middle East. In this context the study projects that the third scenario is the most logical outcome regarding China's relations with the United States (and India). Yet, concern over access to resources will continue to act as a constraint on China's foreign policy and also as an inducement for avoiding conflict with the United States. China's worries about external dependence remain prevalent, as Beijing has come to rely more and more on imported energy. China now imports more than 50 percent of its oil, and if present trends continue, that figure may reach 70- 80 percent by 2030. Most of these imports are likely to come from the Middle East and Africa, crossing the Indian Ocean and passing through the narrow Malacca Strait. China will continue pursuing a two-pronged strategy toward energy; (engages but hedge), on the one hand to enhance cooperation with the U.S. (and India), advance China's political links with energy exporters, increase energy efficiency, diversify, accelerate investments and overseas production and transportation, while on the other hand strengthening China's emergency response. Meanwhile the United States will continue to recognise Chinese legitimate energy interests but at the same time will monitor Chinese actions in the region closely to prevent any "hostile" development which could threaten the American dominant position.

CHAPTER ELEVEN

OVERALL CONCLUSION

11.1 INTRODUCTION

This chapter is a summary of the thesis which presents outcomes of this research. In the first section the key findings of the thesis will be summarised, and in the second section the hypotheses for the research questions will be revisited. In the third section the findings for the research questions will be systematised, while the final section provides recommendations for further research regarding China's oil policy towards the Middle East.

11.2 SUMMARY OF KEY FINDING

- China is not seeking to undermine the American influence, but is looking to secure its energy needs and meet its expanding economic interests. China's policy of strengthening its relationships with Saudi Arabia is neither aimed at undermining U.S. regional interests nor aimed at challenging the U.S.'s dominant position; it's primarily driven by economic energy imperatives.
- China's overriding foreign policy objective is to secure energy supplies to fuel its domestic growth. China does not want to rely entirely on Saudi oil, but looks to Saudi Arabia as an important trading partner and a reliable source for the supply of oil, thus helping the diversity of its sources.

- China (India, Japan and South Korea) has no near term substitute for Middle Eastern oil, thus it is expected that Saudi Arabia (and the Middle East) will play a major role in meeting Chinese and Asian demand for oil the next two decades.
- China will support the stability of Saudi Arabia and the Middle East because it expects a significant increase in its trade/energy with Saudi Arabia in the future. Chinese energy policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States. China is looking at Saudi Arabia (and the Middle East) as a long-term energy source and as an opportunity to further expand economically - not as a country (or a region) that it wishes to wrestle away from U.S. influence.
- The relationship between China and Saudi Arabia suggests that this is an energy – economic partnership not strategic – political alliance. China’s economic interests are the driving force behind the expansion of the Sino-Middle East relationship – and not China’s desire to expand its power and influence in the Middle East at the cost of the United States. The Saudis and the Chinese recognise that, for at least the next two decades, the United States will remain the only country in the world capable of projecting substantial amounts of conventional military power into the Arabian Gulf. That makes the United States a strategically indispensable partner to Saudi Arabia for years to come.
- Saudi Arabia increasingly recognises that Asia will provide the region’s largest and fastest-growing oil and gas export markets in the future. Already, two-thirds of Saudi Arabia’s oil exports go east to Asia, reflecting this profound shift in the balance of global oil. Though China and Saudi Arabia

have expanded their cooperation, Saudi Arabia will probably in the short and medium terms attempt to strike a balance between the United States and China and avoid compromising U.S. interests to please the Chinese or vice versa in the near future.

- The U.S, China, India and all Asia's major powers are becoming more economically interdependent with Saudi Arabia and the Middle East, so these countries will not be able to exclude each other from the region. Because they are reliant on oil, regional stability and the preservation of the status quo are in interest of all countries.

11.3 TESTING THE HYPOTHESES

The thesis' main aim is to investigate China's primary objectives in pursuing closer relations with Saudi Arabia. It also focuses on the implications of high interdependence between China, the world's second-largest oil consumer, and Saudi Arabia, the world's top oil exporter, for the U.S. and the Middle East region. In Part I, the thesis establishes the theoretical frameworks of trade expectations theory and China's oil situation in Chapters two and three respectively. The two chapters individually validate Hypothesis I that China's oil strategy is primarily driven by economic imperatives. Among these imperatives, China's need for oil is the most important.

Part II and Part III are then employed to testify the hypotheses. Part II starts with Chapter four which attempts to provide a historical and political background of

Chinese intentions toward Saudi Arabia. This knowledge of history is followed with an examination of China's perspective of developing relations with Saudi Arabia, and also deciphers the Chinese real motives in regarding the Arabian Kingdom throughout Chapter five. Of course, this part would not be completed without the discussion on the goals of Saudi Arabia to establish partnership with China in Chapter six. The analysis of China's motives towards Saudi Arabia validates Hypothesis II by revealing that China is cautious in the political realm when dealing with Saudi Arabia. China is not seeking to undermine American influence, but is looking to meet its energy needs and expand its economic interests.

This strengthens the argument for Hypothesis I. Also, the argument on China's political motives indicates the Chinese objectives are economic and defensive in nature as China is seeking influence in Saudi Arabia not because it is seeking to expand its power, but because it desires to protect its economic interests from U.S. unilateral action, or from the complex political developments in the Middle East. Meanwhile, for Saudi Arabia, maintaining good relations with the United States remains its key foreign policy objective. Though China and Saudi Arabia have expanded their cooperation, Saudi Arabia will probably - in the near future - attempt to strike a balance between the United States and China and avoid compromising U.S. interests to please the Chinese or vice-versa; particularly when the Saudis are very disturbed by what they consider as a growing "Iranian threat."

Part III further tests Hypothesis I that China's oil strategy is primarily driven by economic imperatives and validates Hypothesis III that China expects a significant increase in its trade and oil imports with Saudi Arabia in the future. In Part III, the

thesis provides strong evidence of the high economic interdependence between China and Saudi Arabia as Chapter seven shows that trade is at the heart of the growing links between the two countries. Between 1990 and 2010, the bilateral trade between the two countries multiplied about 100 times. As for future trade expectations, great potential exists for Sino-Saudi relations to expand substantially in the future. There is no doubt that the economic relations between China and Saudi Arabia will thrive, and their trade could double within the next decade.

Chapter eight further examines the scope of the interdependent relationship in the energy realm in which Saudi Arabia relies on China as a consumer as much as China looks to Kingdom as a key producer. This dynamic of mutual dependence will only get stronger with the prospects that oil demand in China could double over the next two decades, which means China is expected to become the biggest market for Saudi oil. In contrast Chapter nine shows that, due to Saudi Arabia's relations with the United States, Sino-Saudi military relations have been very limited. China still lags far behind America, which remains the Saudi Arabia's military mainstay. Saudi Arabia remains fearful of the ability of Iran to destabilise 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 still Saudi Arabia's final guarantor at least in the foreseeable future.

The three Chapters (seven, eight and nine) individually further tests Hypothesis I and indicate that China's oil strategy is primarily driven by economic imperatives. This suggests that the relationship between China and Saudi Arabia is an energy-economic partnership and not a strategic-political alliance. The three chapters also validate

Hypothesis III, which introduces the variable of expectations of future trade (EFT). This variable predicts that China expects a significant increase in its trade and oil imports with Saudi Arabia in the future. China will likely pursue policies that will enhance security in the region and support the stability of Saudi Arabia and work to protect its interests in the region through economical and political means (soft power) not by using force or military power (hard power). Finally, Chapter ten further tests Hypothesis III. On one hand China is highly economically interdependent with the United States and Saudi Arabia, while the United States is highly economically and militarily interdependent with the Saudis. On the other hand the United States, China and the rest of the oil producing countries in OPEC are highly economically interdependent in the oil market. Thus, the regional stability and the preservation of the status quo are in both the U.S. and China interests. Subsequently, the stability, security and the survival of Saudi regime are now (and for the foreseeable future) in the interest of both the United States and China.

11.4 SYSTEMATISING THE FINDINGS FOR THE RESEARCH QUESTIONS

The thesis is structured according to the six research questions and provides key findings in the corresponding chapters.

- **H1: China is not seeking to undermine the American influence, but is looking to secure its energy needs and meet its expanding economic interests.**

Q1: What have been China's core (or primary) objectives in pursuing closer ties with Saudi Arabia?

Q2: Why does the Middle East region have particular significance for China in meeting its energy objectives (or security)?

- **H2: China will support the stability of Saudi Arabia because it expects a significant increase in its trade/energy with Saudi Arabia in the future.**

Q3: Why is Saudi Arabia an indispensable partner for China?

Q4: What is the nature and extent of China's strategic motives in pursuing a partnership with Saudi Arabia?

- **H3: China will work to protect its interests in the region through economical and political means and not through using military power.**

Q5: Does the relationship between China and Saudi Arabia suggest that this is a strategic – political or energy – economic partnership?

Q6: What are the implications for the region and United States?

The thesis discusses China's primary objectives or motivations in pursuing closer ties with Saudi Arabia from the realist and liberal perspectives in Chapter two and to explore China's oil situation and the significance of the Middle East region for China in meeting its energy security needs in Chapter three. Both chapters show that China's economic interests are the driving force behind the expansion of the Sino-Middle East relationship – and not China's desire to expand its power and influence in the Middle East at the cost of the United States. Chinese energy policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States as

realists may contend. China is looking at Saudi Arabia (and the Middle East) as a long-term energy source and as an opportunity to further expand economically - not as a country (or a region) that it wishes to wrestle away from U.S. influence. Because China is not using its power (political, military and economical) to further an international political agenda to decrease U.S. power and influence, China's actions closely aligns with the economic interdependence theory.

As for the future, the thesis expects that the stability of Saudi Arabia will be at the top of China's interests in the coming years. Accordingly, this study predicts that Saudi Arabia's political and economic relations with China will expand strongly in the coming years especially in light of: (a) China's growing oil demand and need to import more oil from the Middle East; (b) The political consensus between the two countries in most regional and international issues; (c) The Saudis' desire to keep China-Iran relations in check; and (d) The Saudi concerns of "American meddling" after the Arab uprising to promote democracy in the Middle East. But, due to what the Saudis perceive as a growing "Iranian threat", the Kingdom currently has no alternative but to count on the military guarantees provided by the United States. Thus, Saudi Arabia will seek in the foreseeable future to balance the relations between China and the United States.

The key finding of the thesis regarding question one could be summarised as follows: Politically, (as the study demonstrates on Chapters four and five) China's overriding foreign policy objective is to secure energy supplies to fuel its domestic growth. China does not want to rely entirely on Saudi oil, but looks to Saudi Arabia as an important trading partner and a reliable source for the supply of oil, thus helping the

diversity of its sources. China's policy of strengthening its relationships with Saudi Arabia is neither aimed at undermining U.S. regional interests nor aimed at challenging the U.S.'s dominant position; it's primarily driven by economic energy imperatives. China has geared its policies regarding Saudi Arabia towards addressing its energy security. China's policies have grown closer to Saudi Arabia in order to: (a) Ensure access to future energy supplies; (b) Maintain Saudi Arabia's role in keeping Chinese energy sources diversified; (c) Possibly look to Saudi Arabia to influence the United States in curtailing U.S. unilateral action. China views U.S. unilateral action (particularly towards Iran) as a threat to Chinese economic interests in the Middle East and therefore is seeking to avoid that scenario; and (d) Enlist Saudi Arabia's support of its "core interests" such as dealing with the Chinese Muslims, Tibet, Taiwan and human rights issues.

There is no doubt that with China's economic, technological and military ascent there will be the potential for a comprehensive global power shift. China's persistence in actively securing natural resources and building strategic alliances is, and will remain, a source of direct economic competition to the U.S. for the near future. Yet, there is no evidence to support the "China threat" theory in the Middle East, neither is there a concern in Saudi Arabia (and in the Middle East) that China will constitute a threat. It is important to note that some of the fundamental aspects of the U.S.-Saudi relationship are not likely to change in the foreseeable future. The Saudis and the Chinese recognise that, for at least the next decade, the United States will remain the only country in the world capable of projecting substantial amounts of conventional military power into the Arabian Gulf. That makes the United States a strategically indispensable partner to Saudi Arabia for years to come. As for China, the country is

trying to benefit from the Middle East's economy while strategically hedging against American military power by moving even closer to Saudi Arabia and other states. Meanwhile the Saudis are pursuing what could be called a "hedging" strategy. They are cultivating a genuinely strategic relationship with the world's most important rising power, at least in part as a hedge against a further, precipitous decline in their relationship with the established superpower. China's political actions are defensive in nature, because China is not using its political power to further an international political agenda to decrease U.S. power and influence in Saudi Arabia, subsequently China's political actions closely aligns with the economic interdependence model.

Economically, (as the study demonstrates in Chapters three, seven and eight) the crude oil is at the heart of Sino-Saudi trade. While China does import a large volume of oil from Saudi Arabia: (a) It has not invested a great amount in Saudi Arabia's energy sector; (b) China does not provide huge investments and/or massive economic assistance to Saudi Arabia in order to make Riyadh more dependent on Beijing; and (c) China does not provide advanced technology to deepen Saudi's economic dependency on China. Because China is not using its economic power to further an international political agenda to decrease U.S. power and influence in Saudi Arabia, China's economic actions closely aligns with the economic interdependence school of thought. While there is great potential for the Sino-Saudi relationship to expand in this area, both countries are taking their time developing these relations. China is content with focusing on Sino-Saudi energy matters and improving Chinese energy security. China's oil consumption will rise strongly and could double during the next two decades. Despite China's attempts to diversify its oil sources, there is no substitute for

the Middle East in the near future. Thus, the study expects deepening energy interdependence between China and Saudi Arabia over the next decade.

Militarily, (as the study shows in Chapter nine) China has not had strong relations with Saudi Arabia. This is most likely due to the fact Saudi Arabia has strong military relations with the United States. Additionally, since China views Saudi Arabia as a long-term energy source, its interests fall in line with U.S. interests regarding Saudi Arabia. Both the United States and China view Saudi Arabia as a vital energy source and both want the preservation of stability and security within Saudi Arabia. Saudi Arabia relies almost entirely on arms imported from the western countries especially the United States. It also depends on the security agreements with the United States to combat internal terrorism and external threats. There is no supporting evidence that the China is working to jeopardise this situation. Saudi Arabia will rely on the security umbrella of the U.S. over the next decade and there is no evidence to show that China either seeks to be a substitute for the United States, or is there evidence to suggest that China is working to undermine the U.S.-Saudi relations.

To answer question two, the thesis has shown in Chapter three that China has attempted to diversify sources of energy and has increased imports from Africa, Latin America, Central Asia and other regions. Still, in 2010, about half of China's oil imports came from the Middle East. Given the global oil reserve, production pattern, exports trends and the projections of future oil, the Middle East's status as China's leading oil supplier is unlikely to change any time soon. Diversification away from the Middle East, however, has its limits. Two-thirds of proven oil reserves are located in the region, mostly in the Arabian Gulf. Regardless of efforts to increase domestic

production and diversify its energy supply, China cannot avoid increased dependence on the Middle East and Saudi Arabian oil in the next two decades. In sum, Saudi Arabia (and the Middle East) will have particular significance for China in meeting its energy objectives (or security) for a long period to come.

To answer question three, Chapters four and five show that there are many reasons that make Saudi Arabia a very important partner for China. Firstly, Saudi Arabia is the cradle of Islam and China needs the Saudi support in dealing with Chinese Muslims (Uyghur) in the Xinjiang region. Secondly, Saudi Arabia represents an area with huge economic opportunities as the Kingdom represents over 20 percent of the combined GDP of the Middle East-North Africa (MENA) region (and an estimated quarter of the Arab World's GDP) making it the economic engine of the region. Thirdly, from the Chinese perspective, energy security lies at the heart of the bilateral relationship with Saudi Arabia. China's efforts to develop closer relations with Saudi Arabia are based on two goals. (a) China is attempting to ensure it has access to Saudi energy sources in the future in order to meet its energy demands. And (b) China is also attempting to maintain its diversity in energy sources. While China may be limiting the amount of Saudi oil it imports, Saudi Arabia still plays a vital role in maintaining the diversity in Chinese oil supplies (i.e. keeping China from becoming too reliant on Angola, Iran and Russia).

Furthermore, China recognises Saudi Arabia's uniquely dominant role among the world's oil market. Saudi Arabia is the largest oil producer of the Organization of the Petroleum Exporting Countries (OPEC). Despite the questions that hover over the future of oil in Saudi Arabia, at the moment, and perhaps for many years to come,

there is no alternative to the Kingdom. With approximately one fifth of the world's proven oil reserves and some of the lowest production costs, Saudi Arabia is expected to remain the world's largest net oil exporter in the near future. Saudi Arabia is also still the world's only "swing producer": the country retains the single largest spare production capacity of all oil producers. Saudi ARAMCO, the Kingdom's national oil company, is the world's largest producer and exporter of petroleum and has by far the world's largest sustained production capacity infrastructure at about 12 million barrels-per-day and also has the world's largest spare capacity - currently estimated at about 70 percent of global unused capacity.

Additionally, Saudi Arabia, from China's perspective, is a voice of moderation and stability - and undoubtedly the single most important country in the world of energy. In China's eyes, maintaining stable relations with Saudi Arabia is the best possible approach to avoid being shut-off from vital oil resources if the Sino-American relationship should take a turn for the worse, or/and in the event of political turmoil as demonstrated in Libya in 2011. There are no other producers capable of stepping into Saudi Arabia's shoes. As a result and for all these reasons, China cannot ignore the economic and political power of Saudi Arabia.

To find out the nature and extent of China's strategic motives in pursuing a partnership with Saudi Arabia, Chapter five further highlights the importance of Saudi Arabia and tries to answer question four. Due to the close relationship that Saudi Arabia has with the United States, China hopes to limit the United States' ability to act unilaterally through closer Sino-Saudi ties. While realists may view these actions as China attempting to expand their power and influence in the Middle East at the cost

of the United States, China's actions do not fit well with their theory. First, China's political policies are geared towards increasing China's energy security and economic interests. China is not only looking to develop closer Sino-Saudi ties so Saudi Arabia remains a vital long-term energy source, but also to keep Chinese energy sources diversified.

There is no great risk or any indications that Saudi Arabia and China will enter into exclusive oil supply relationship. Secondly, China is also looking to expand its trade market in Saudi Arabia, as the Kingdom is the largest market in the Arab World and the Middle East. Thirdly, China is seeking Saudi support in fighting what the Chinese call the "three ugly forces": religious extremism, national separatism, and terrorism. China is also seeking full support of Saudi Arabia and other Arab States in the international arena on issues regarding Taiwan or "One China Policy" and human rights issues. These Chinese objectives are economic and defensive in nature, which aligns Chinese actions closer to the economic interdependence model rather than the realism theory. There is no denying that China is looking to curtail U.S. unilateral action in the Middle East region; however, even this intention fits within the economic interdependence model. China is seeking greater influence in Saudi Arabia (and the Middle East) not because it is seeking to expand its power, but because it desires to protect its economic interests from U.S. unilateral action or from the complex political developments in the Middle East. This indicates that China is mainly seeking to avoid armed conflict in order to preserve its economic interests; therefore, China's actions fit more closely along the lines of the economic interdependence model.

To answer question five it was essential to know the scope of China-Saudi relations in all areas (economic, energy and military) in order to find out whether the relationship is politically driven or an energy/economic partnership. In the economic realm, Chapter seven has shown that China's economic interests are the driving force behind the expansion of the Sino-Saudi relationship – and not China's desire to expand its power and influence in the Middle East at the expense of the United States. Chinese economic policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States as realists may contend. China is taking a cautious approach with regard to the Sino-Saudi relationship which does not fit in well with the realism theory. China is looking at Saudi Arabia as a long-term energy source and as an opportunity to further expand economically - not as a state that it wishes to wrestle away from U.S. power and influence. China is not using its economic power to further an international political agenda to decrease U.S. power and influence; instead China's economic actions closely align with the economic interdependence school of thought. This is illustrated by three developments:-

Firstly, China is not providing Saudi Arabia with massive economic benefits to develop a closer Sino-Saudi relationship as the United States and Soviet Union did to its proxy states during the Cold War. China's economic policies are geared primarily towards addressing its energy security and possibly taking advantage of economic opportunities within Saudi Arabia. China is not looking to reduce U.S. power and influence in Saudi Arabia through its Sino-Saudi economic ties, and is in fact, taking a cautious approach to the Sino-Saudi relationship.

Secondly, China has shown a reluctance to become too heavily invested in Saudi Arabia. While Saudi Arabia provides China with energy and vast economic opportunities, it has not taken full advantage of those economic opportunities. This may be for two reasons: (a) Saudi Arabia may not need Chinese capital as much due to its massive oil revenues and its strong ties to the United States; and (b) China does not see any urgency in assisting Saudi Arabia; on the contrary, the Kingdom is seen to be the side aggressively courting Chinese investments (particularly in the petrochemical industry) and China is the side restraining its investments. This does not fit in well with the realists' model because the Saudis courting Chinese investments can be viewed as an opportunity for China to gain more power and influence in Saudi Arabia. Instead, China has so far refused to take advantage of this opportunity. The low amount of Sino- Saudi activity in this realm indicates that China is selective about what investments it wants to make in Saudi Arabia. This behaviour fits more consistently with the economic interdependence model. China is not arbitrarily investing in Saudi Arabia in order to further the Sino-Saudi relationship at the cost of the U.S.-Saudi relationship. China invests in Saudi Arabia only if it feels that the investment is in its economic interests and/or is making economic sense.

Thirdly, although important, the Chinese projects in Saudi Arabia with regard to their share in China's overseas projects, are still small or less than 4 percent of the total volume or value. If China was indeed acting within the realism model, it should be aggressively pursuing closer economic ties with Saudi Arabia by expanding its projects. China has not done so; instead the Chinese companies were looking for profitable investments. The only project which some analysts have said could have a political dimension was the *Makkah* railway, even though this project opened new

economic opportunities to the Chinese and also created a newfound respect for Chinese-made products (made in China) and Chinese-engineering prowess in the region.

In the energy realm, Chapter eight has shown that China's economic interests are the driving force behind the expansion of the Sino-Saudi energy relationship – and not China's desire to expand its power and influence in the Middle East at the cost of the United States. China's energy policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States as many realists may contend. China is taking a cautious approach to developing a Sino-Saudi relationship. This action does not fit in well with the offensive realism school of thought. China is looking at Saudi Arabia as a long-term energy source and as an opportunity to further expand economically - not as a state that it wishes to wrestle away from U.S. power and influence. China is not using its economic power to further an international political agenda to decrease U.S. power and influence; China's economic actions closely align with the economic interdependence school of thought. This is illustrated by several developments:

Firstly, while there is no denying that China and Saudi Arabia have extensive energy relations, it is clear that China is also attempting to limit its ties to Saudi Arabia. Despite Saudi Arabia having the largest proven oil reserve in the world, China has shown a desire to keep its oil sources diversified. China has made significant efforts to diversify its sources of oil, developing resources in Russia, Central Asia, Africa, Latin America and the Middle East. This strategy has resulted in the fact that currently over 80 percent of China's oil imports are not coming from Saudi Arabia.

China is also wary about becoming too reliant on Saudi ARAMCO and has attempted to diversify its domestic oil refineries to include several foreign partners such as Kuwait Petroleum Corp (KPC), Petroleos de Venezuela SA (PDVSA), Russian oil company OAO Rosneft and the American company ExxonMobil.

Secondly, with respect to China's efforts to build strategic oil reserves, it has used a variety of methods to fill its reserves in the first and the second phases. The Chinese do not seem to be placing much urgency on filling its oil reserves from Saudi Arabia for many reasons. (a) China is taking a more patient approach by filling its strategic oil reserves gradually over many years; (b) China is unwilling to pay a high price for oil that will be used to fill its strategic oil reserves; and (c) China has filled its first strategic oil reserve using domestic oil instead of imported oil. China may also be looking to fill its strategic oil reserves with overseas oil assets in which Chinese firms own stakes in. Finally, China has shown a reluctance to become too heavily invested in the Saudi Arabia energy sector. China does not want to share the financial risk with the Saudi side. In China, differences on shouldering the financial risk are complicating the joint venture modernisation of a refinery in Quanzhou. While in Saudi Arabia, the Chinese took a cautious approach of Yanbu's new refinery project as they wanted assurances with regards to managing the risk properly. This behaviour fits more consistently with the economic interdependence model.

In the military realm, Chapter nine has shown that China isn't looking to provide Saudi Arabia with the protection it gets from the U.S. which maintains air, naval and army bases in the Arabian Gulf. While China may be limited in the military assistance it can provide to Saudi Arabia, if China was acting in the realism model it should still

be attempting to undermine the U.S.-Saudi military ties in order to further the Sino-Saudi military ties. This has not been the case. Instead, there exists only two known instances where China sold limited military equipment to Saudi Arabia during the 1980s and 2007, and it would appear there have not been any significant Sino-Saudi arms deals since then.

Due to Saudi Arabia's relations with the United States, Sino-Saudi military relations have been very limited for several reasons. (a) China does not have the desire to expand its power and influence in the Middle East at the cost of the United States; (b) China does not have the same capability to project her power globally as the United States does; and (c) Saudi Arabia views China as a poor substitute for U.S. support against the other threats the Kingdom faces on the domestic front in the form of terrorism. Chinese military policies are not directed at increasing its power and influence in Saudi Arabia at the cost of the United States as realists may contend. China is taking a very cautious approach as to the extent of the Sino-Saudi military relationship, which does not fit in well with the realism school of thought.

Chapters seven, eight and nine individually strengthen the argument that China's primary objectives in pursuing closer ties with Saudi Arabia is to establish an energy – economic partnership. Indeed, the three chapters have shown that China's policy in the Middle East is not geared towards expanding its power and influence at every opportunity in order to challenge the United States as the offensive realism model would predict. Instead, China is seeking to maintain the status quo which is allowing the Chinese economy to grow at an astonishing rate and to protect its economic interests in the Middle East. These two goals are highly dependent on: (a) Avoiding a

disruption in energy flow from the Middle East as a result of an armed conflict; (b) Maintaining good Sino-Saudi and Sino-U.S. relationships; and (c) Maintaining its economic expansion in the Middle East. Because China's actions are geared towards fulfilling those three economic goals, which are not intended to undermine U.S. influence, its actions are closer to the economic interdependence model, which suggest that the relationship between China and Saudi Arabia is an energy – economic partnership and not a strategic – political alliance.

Within this context, what are the implications for the region and the United States? Chapter ten has shown that China's involvement in the Middle Eastern political economy may have some (from U.S. perspective) negative effects. But the United States and China share many common goals in the region and there are prospects for cooperation between them on energy, peace, religion, and other issues. Hardly any evidence shows that China is engaged in a “zero-sum” competition with the United States in the Middle East, or that the U.S. is plotting to exclude China from the region.

It is premature to declare that the Middle East (or Saudi Arabia) will become a new battleground for the two powers to compete for influence and control. Many international and regional problems cannot be solved without cooperation between China and the United States. For the United States, paranoia about a coming “China threat” and a misguided policy based on this assumption will be the wrong choice. China is already heavily involved in a Middle Eastern political economy. The U.S. strategic calculations in the Middle East will have to take Chinese interests into consideration. It is impossible for the United States to exclude or isolate China from the region. What the United States can do now is to actively engage China, and

address China's legitimate needs and concerns. There is no question that China's high interdependence with the Middle East will make it more challenging for the United States to successfully pursue its objectives and follow through with unilateral action. Despite China's increasing influence and economic power in the Middle East, Beijing shows no interest in exploiting the energy relationships it might have to influence Saudi Arabia, thereby challenging America's influence and strategic interests. There are no doubts that there will be challenges ahead, but the two countries can establish a constructive relationship and lay a solid foundation for future cooperation in the Middle East.

In sum, the thesis has shown that China's policy towards Saudi Arabia is not geared towards expanding its power and influence at every opportunity in order to challenge the United States as the realism model would predict. Instead, China is seeking to maintain the status quo which is allowing the Chinese economy to grow and to protect its economic interests in the Middle East. These two goals are highly dependent on: (a) Avoiding a disruption in energy flow from the Middle East as a result of an armed conflict; (b) Maintaining good Sino-Saudi and Sino-U.S. relations; and (c) Maintaining its economic expansion in the Middle East. Because China's actions are geared towards fulfilling those three economic goals which are not intended to undermine U.S. influence, its actions are closer to the economic interdependence model. As for future trade expectations, the case studies indicate: (a) Growing interdependence between China and the Middle East; (b) The volume of bilateral trade between China and Saudi Arabia could double over the next few years; and (c) China could overtake the U.S. and become Saudi Arabia's top oil importer within the next five years. Thus the study indicates the stability of Saudi Arabia and the Arab

Gulf States will be at the top of China's interests in the coming years, and these interests could bring China even closer to the American policy in the Middle East.

11.5 RECOMMENDATIONS FOR FUTURE RESEARCH

As with most research projects, some issues need further investigation as a result of this thesis. Future studies would need to be carried out to gain deeper knowledge and understanding of China's Middle East policy. Therefore, in the course of this thesis, four specific areas worthy of future research have become apparent. The fact that the study focuses on the oil sector as a result of its centrality in the development of China-Saudi relations; further research is needed to show how China's policies are geared for non-energy sectors. The current thesis focuses on relations between China and Saudi Arabia at state level (or within the perspective of international relations) and did not focus on the sectoral level (i.e. oil companies, political lobbying, political behaviours in the international bodies, human rights organisations or even individuals, etc.). Further research is therefore warranted specifically addressing the sectoral level. Thirdly, while Saudi Arabia provides a solid representation of aspects of China's foreign oil activities, it does not make up a comprehensive review. It is important to consider other countries in the Middle East, Central Asia and Africa. Finally, studies at the public level are needed, trying to figure out people's opinions on the development of Sino-Saudi Arabia and how political leaders interact with these opinions.

Additionally, general specialised studies of particular interest would include: (a) Chinese investments in Arab countries and how the process of decisions-making influence that issue; (b) The impacts of high oil prices on the Chinese economy and its effect on Arab-Chinese relations; (c) The impacts of Chinese investments in the energy sector on the governance practices of Arab countries and their foreign policies; (d) Motivations, roles and influence of the various parties in deals concerning transnational pipelines to China from Central Asia, Russia, and Myanmar and its impacts on Middle Eastern (or GCC) oil producers; (e) Scenario analysis of possible supply disruptions, including the impact on the relationship between the Chinese Government and the NOCs on one hand and the impact on China's relations with Arab (Middle Eastern) countries on the other hand; and (f) Comparison of the strategies followed by China's NOCs in their Middle East oil and gas investments and other regions such as Africa and Latin America along with a comparison between China's strategies in South East Asia and the Middle East.

EPILOGUE

The thesis' main aim is to investigate the causes of China's motives to establish a strategic relationship with Saudi Arabia and its implications for the United States. In doing so, the study attempts to decipher China's intentions in establishing strategic relations with Saudi Arabia. In attempting to fulfil these aims, two forms of research data were gathered to guide the research investigation in this study. Quantitative or secondary data were in the form of political, economic, military and energy reports and studies, government statistics and other forms of quantified data on oil and energy in Saudi Arabia and China. Qualitative or primary data were in the form of documents, published interviews and opinions of experts and leaders in the oil industry as well as oil experts employed in academic organisations and government agencies. The empirical analyses have provided valuable results and indicated the nature of Sino-Saudi relation with its implication to the United States. This study also aimed to enumerate a set of recommendations that would assist in overcoming the potential difficulties and sustain its competitive advantage in the sector. This study, thus, has fulfilled its aims and objectives; and hence, is now completed.

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APPENDICES

APPENDIX I

No. 289

CHINA

and

SAUDI ARABIA

Treaty of Amity. Signed at Jedda, on 15 November 1946

Chinese, Arabic and English official texts communicated by the Acting Director of the office of the Permanent Chinese delegation to the United Nations. The registration took place on 20 September 1948.

CHINE

et

ARABIE SAOUDITE

Traité d'amitié. Signé à Djeddah, le 15 Novembre 1946

Textes officiels chinois, arabe et anglais communiqués par le Directeur par intérim du Bureau de la délégation permanente chinoise auprès des Nations Unies. L'enregistrement a eu lieu le 20 septembre 1948.

No. 289. TREATY OF AMITY BETWEEN THE REPUBLIC OF CHINA AND THE KINGDOM OF SAUDI ARABIA. SIGNED AT JEDDA, ON 15 NOVEMBER 1946

His EXCELLENCY THE PRESIDENT OF THE NATIONAL GOVERNMENT OF THE REPUBLIC OF CHINA, on the one hand, and

His MAJESTY THE KING OF SAUDI ARABIA, on the other hand,

Animated by the desire to establish and to consolidate the bonds of friendship and good understanding between their respective countries, have resolved to conclude a Treaty of Amity and have for this purpose appointed as their

Plenipotentiaries:

His Excellency the President of the National Government of the Republic of China:

His Excellency Mr. Cheng Ye-tung, Ambassador Extraordinary and

Plenipotentiary of the Republic of China to Iran;

His Majesty the King of Saudi Arabia:

His Excellency Sheikh Youssif Yasseen, Acting Foreign Minister of Saudi Arabia,

Who, having communicated their Full Powers, found in good and due form, have agreed as follows:

Article I

There shall be perpetual peace and amity between the Republic of China and the Kingdom of Saudi Arabia as well as between their peoples.

Article II

The High Contracting Parties agree to establish diplomatic relations between the two States in conformity with the principles of Public International Law.

They also agree that diplomatic representatives of each State shall enjoy, on the basis of reciprocity, in the territory of the other, the treatment recognized by the general principles of Public International Law.

Article III

The High Contracting Parties agree that either High Contracting Party may establish consulates in such localities of the territory of the other as may be agreed upon. The consular officers of either High Contracting Party shall enjoy, On the basis of reciprocity, in the territory of the other, the treatment recognized by the general principles of Public International Law.

Article IV

The High Contracting Parties agree that the nationals of either High Contracting Party residing or travelling in the territory of the other shall be accorded the most-favoured-nation treatment in regard to the protection of their person and property.

Article V

The High Contracting Parties agree that on the death of a national of either High Contracting Party in the territory of the other, if there is no lawful trustee to take care of the property of such a national, such property, after the carry out of judicial procedures concerned, shall be handed over to the nearest consular officer of his own country for forwarding to his rightful heir.

Article VI

The High Contracting Parties agree to regulate in a convention to be concluded later the commercial relations between their respective countries.

Article VII

The present Treaty shall be ratified with the least possible delay by the High Contracting Parties in accordance with their respective laws. The instruments of ratifications shall be exchanged as soon as possible.

The present Treaty shall enter into force on the day of the exchange of ratifications.

IN FAITH WHEREOF the respective Plenipotentiaries have signed the present Treaty.

DONE at Jedda this fifteenth day of the eleventh month of the thirty-fifth year of the Republic of China, corresponding to the twenty-second of Zilhegga of the year one thousand three hundred and sixty-five of Hagira, that is, 15th November 1946, in duplicate, and in the Chinese, Arabic and English languages, all being equally authoritative.

(Signed) Y. T. CHENG
(Signed) Youssif YASSEN

Source: U.N.

APPENDIX II

Communiqué Concerning the Establishment of Diplomatic Relations between the People's Republic of China and the Kingdom of Saudi Arabia

The Governments of the Kingdom of Saudi Arabia and the People's Republic of China have decided to establish diplomatic relations between the two countries at the ambassadorial level as of 29 Thul Hijjah 1410 AH, corresponding to 21 July 1990 AD

The Government of the People's Republic of China supports the policy of the Government of the Kingdom of Saudi Arabia in pursuit of achieving its security, stability and national interests.

The Government of the Kingdom of Saudi Arabia recognizes that the Government of the People's Republic of China is the sole legitimate government that represents the entire Chinese people.

The two Governments have agreed to develop cooperation and friendly relations between the two countries on the basis of the principles of mutual respect for sovereignty and territorial integrity, mutual non-aggression, non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence.

QIAN QICHEN

Minister of Foreign Affairs of the People's Republic of China

SAUD AL FAISAL

Minister of Foreign Affairs of the Kingdom of Saudi Arabia

21 July 1990

Source: Minister of Foreign Affairs of the People's Republic of China

APPENDIX III

Memorandum of Understanding on Petroleum Cooperation between the Government of the People's Republic of China and the Government of the Kingdom of Saudi Arabia

Building on the strong bilateral relations between the People's Republic of China and the Kingdom of Saudi Arabia, H. E. Mr. Zhang Zhigang, Vice Minister of the State Economic and Trade Commission of the People's Republic of China met with the Minister of Petroleum and Mineral Resources of the Kingdom of Saudi Arabia in Riyadh on October 30, 1999. The two sides discussed the bilateral relations in the field of petroleum.

The two sides shared the view that the stability of the international oil market is in the interest of oil producing and consuming countries and health of the world economy. Both sides agreed that Saudi Arabia is a large dependable, reliable and secure petroleum supplier, while China is a large dependable and reliable consumer; therefore, the two countries are strongly complementary to each other in this field. Both sides expressed their willingness to establish long-term friendly and cooperative relationship in the field of petroleum.

Both sides agreed to facilitate investments in refining, petrochemical sectors and petroleum technical services cooperation in their respective countries. Both sides also agreed to encourage their enterprises to actively engage themselves in the scientific and technological cooperation, experience exchange and personnel training activities.

Both sides wish to further strengthen bilateral exchange, establish the contact channels between the respective institutions, meeting periodically or whenever is needed to enhance mutual understanding and friendship.

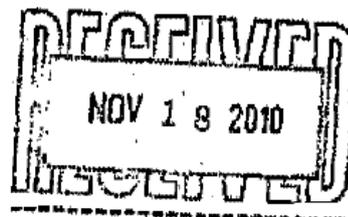
Signed by the respective representatives of the two governments in Riyadh

October 31, 1999

Source: Minister of Foreign Affairs of the People's Republic of China

APPENDIX IV

The Honorable Howard L. Berman, Chairman
Committee on Foreign Affairs
House of Representatives
Washington, D.C. 20515



Dear Chairman Berman:

Thank you for your letter of November 10th regarding potential arms sales to Saudi Arabia. We welcome the opportunity to address your questions regarding the impact such a sale would have on the national security interests of the United States.

To meet the criteria for U.S. government approval, any sale of defense articles and services must, among other considerations, support U.S. strategic and foreign policy interests, according to the Conventional Arms Transfer Policy (CAT), as detailed in Presidential Decision Directive 34 (PDD -34, February 10, 1995).

We believe the proposed package promotes U.S. strategic and foreign policy interests, and it is a key component of our overall regional strategy. The United States is committed to deepening its bilateral and multilateral security relationships in the Gulf to enhance regional stability and security. A key component of our regional cooperation is enhancing the defensive capabilities of our Gulf partners.

Saudi Arabia is an important partner with whom we have a long history of close political-military relations. We coordinate closely with Saudi Arabia on a wide range of issues pertaining to Middle East regional security and we have long been the principal supplier of defense equipment and defense services to support Saudi Arabia's legitimate defense needs. Our six-decade-long security relationship with Saudi Arabia is a primary security pillar in the region. This package continues that tradition.

This proposed sale will directly support our interests by reinforcing our longstanding defense and security partnership with Saudi Arabia, enhancing Saudi Arabia's ability to deter and defend itself against terrorist groups and other regional threats, improving interoperability with the U.S. military, and sending a strong message to all countries

that the United States is committed to supporting the security of its key partners and allies in the Gulf and broader Middle East.

For the past twenty years, the F-15 has been a cornerstone of the relationship between the U.S. Air Force (USAF) and the Royal Saudi Air Force (RSAF). Selling new F-15SAs, upgrading the current F-15S fleet to the SA configuration, and providing the training component will enhance Saudi air defense and deterrence capabilities, ensure interoperability between the USAF and RSAF, and sustain long-term relationships to ensure continued U.S. influence for decades.

The proposed package will also enable the Saudi Arabian National Guard, Royal Saudi Land Forces, and Saudi Royal Guard to deploy the AH-64D, UH60M, AH-60i, and -rvID-530F helicopters to defend vital government and energy installations, and bolster Saudi Arabia's counterterrorism capabilities, while increasing Saudi interoperability with the US Army.

You asked what conditions were placed on the potential sale. All sales of U.S.-origin defense articles and defense services are subject to restrictions outlined in the Arms Export Control Act (AECA), as amended, including Section 4's limits on the purposes for which military sales are authorized and Section 3(g)'s requirement that any agreement for the sale of defense articles or services shall state that the United States Government retains the right to verify credible reports that any such article has been used for an unauthorized purpose. As with all Foreign Military Sales or Direct Commercial Sales, actual or possible end-use violations, will be notified to Congress as required by Section 3(e) of the AECA.

On the question of threats to Saudi Arabia and its ability to meet those threats, Saudi Arabia faces an Iranian threat, including destabilizing actions in the region, and in the past year has faced Houthi attacks along its border with Yemen. Saudi Arabia also faces considerable challenges in countering domestic and regional terrorism, as exhibited by the February 2006 attack on the Abqaiq oil facility. This proposed sale will help improve Saudi Arabia's ability to deter and defend against threats, and carry out counterterrorism operations. .

On the question of repercussions of future political change in Saudi Arabia, our strong political-military relationship with that nation helps ensure a continued long-term partnership between our countries. The Saudi choice to partner with the United States through such sales will have a decades-long impact, strengthening and deepening our military-to-military relationship, and leading to extensive collaborative training and exercises. Such engagement helps deepen our relationship with Saudi Arabia beyond the senior political level, minimizing the chance that political change will negatively impact our relationship. Our close ties to Saudi Arabia also help to guard against potential repercussions for our friends in the region.

You highlighted that a recent GAO report noted the Administration, "did not consistently document how arms transfers to Gulf countries advanced U.S. foreign policy and national security goals ... " We read the recent GAO report with great interest and are investigating the possibility of implementing their suggestions, where appropriate and feasible. Though record-keeping can always be improved, our departments thoroughly analyze every potential arms sale to gauge the impact on U.S. national security interests.

Regarding your concerns about Saudi support for wider regional U.S. policy goals, the Middle East Peace Process is one area where we coordinate closely with Saudi Arabia both publicly and privately. As a key member of the Arab League, the Saudis played a leadership role when the Arab League supported President Abbas's decision to enter into direct negotiations with Prime Minister Netanyahu. More recently, Saudi Arabia has granted the Palestinian Authority an additional \$100 million in budget support, above the \$46 million it provided in accordance with its Arab League commitment. We will continue to urge Saudi Arabia and other Arab countries to take concrete steps toward implementing the vision embodied in the Arab Peace Initiative.

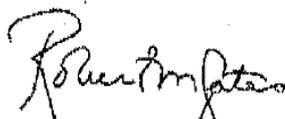
You also raised a number of questions regarding aspects of Saudi Arabia's regional policy and its commitment to other key U.S. goals, including counterterrorism and countering terrorist financing. Saudi cooperation on counterterrorism issues is significant, and U.S. law enforcement and intelligence agencies continue to benefit from this relationship. Saudi Arabia played an integral role in helping the U.S. thwart the cargo package bomb plots of late October emanating from Yemen, and we have publicly thanked the Saudis for this critical information sharing. The Saudi government has also taken numerous regulatory and institutional steps to counter terrorist financing. These steps include a historic fatwa criminalizing terrorist finance released in April 2010 and endorsed by King Abdullah in May 2010, the development of regulatory and oversight infrastructure to counter money laundering and terrorist financing, and active participation by the Saudi government in international bodies devoted to these issues. Additionally, Saudi Arabia has been very involved in addressing regional Gulf security issues related to Yemen. Saudi Arabia has been an active partner in the Friends of Yemen process and has made numerous efforts to help Yemen improve its ability to govern, which in turn reduces terrorism's appeal. We have every confidence that the proposed sale will deepen our partnership with Saudi Arabia, which in turn will reinforce and make more productive our work with Saudi Arabia on critical regional issues.

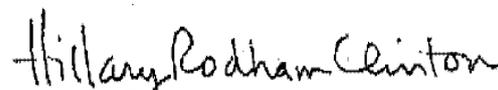
On counter-proliferation, Saudi Arabia has been responsive to UNSCR 1540 reporting requirements and has recently shown its support for a more substantive regional dialogue on counter-proliferation by offering to host a GCC workshop, scheduled for December 2010, on 1540 issues. The United States is developing an Export Control and Related Border Security (EXBS) Program with Saudi Arabia. As a next step in this program, a senior Saudi delegation is expected to visit Washington in January

2011 to meet with U.S. export control experts to discuss the importance of strategic trade controls and the provisions and processes essential for their effective implementation. The United States and Saudi Arabia also have signed a Memorandum of Understanding (MOU) on cooperation in nuclear energy. This MOV contains a statement of intent by Saudi Arabia to rely on the international market for fuel cycle services as an alternative to the pursuit of enrichment or reprocessing capabilities. This MOD was signed in May 2008 and entered into effect in January 2009 when Saudi Arabia brought its Nuclear Non- Proliferation Treaty safeguards agreement into force. .

With regard to your concerns about the impact that this proposed sale will have on Israel's security and Qualitative Military Edge (QME), we concluded, as required by law and after a thorough interagency assessment, that this sale will not negatively impact Israel's security interests or it's QME. A more detailed analysis on this issue was briefed to Congress as part of the Congressional notification process, and was provided in the Congressional Notification package: Our commitment to Israel's QME is rock solid and longstanding. Apart from evaluating our arms sales to the rest of the Middle East against QME criteria, the U.S. government ensures Israel's QME is upheld in numerous ways, including through sales of defense equipment to Israel, robust security assistant cooperative research and development programs, and extensive combined training" and exercises. .

We believe that the sale of these advanced aircraft will support the national security interests of the United States now and in the years to come. We hope this information is useful to you. Please do not hesitate to contact us again if we can be of further assistance.


Robert M. Gates
Secretary of Defense
NOV 16 2010


Hillary Rodham Clinton
Secretary of State
NOV 16 2010